S&P Global
Ratings

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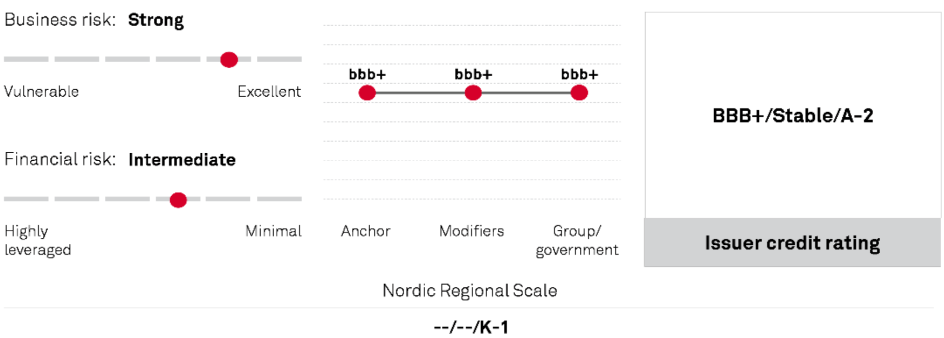
Essity AB

September 2, 2022

Ratings Score Snapshot



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Credit Highlights

Overview

Key strengths	Key risks
Nondiscretionary product categories such as adult and baby incontinence products, consumer tissue, and professional hygiene.	Ongoing increase of input costs including pulp, oil-derivative materials, energy as well as transportation will pressure operating margins in 2022.
Established leading position in the incontinence (TENA) and professional hygiene segments (TORK) and emerging leadership in the washable absorbent underwear category through KnixWear and Modibodi acquisitions.	Continued supply constraints in the energy market could affect manufacturing capabilities.
Branded proposition and focus on innovative and sustainable products support relatively fast sales price increase during current inflationary period.	Competitive nature of the European consumer tissue and personal hygiene markets due to high penetration of private label offering.
Global presence, with about 62% exposure to developed countries and 38% to fast-growing emerging markets.	Limited headroom to accommodate other debt-funded acquisitions in 2022 as we expect S&P Global Ratings-adjusted debt to EBITDA will rise into the 3.0x-3.2x range this year.

Sales price increases can only partly compensate the current high inflation, therefore S&P Global Ratings-adjusted EBITDA margin should contract by 300 basis points (bps)-350 bps to about 13% at year-end 2022. In our view Essity's solid portfolio of well-known brands, including Tena and TORK, as well as its focus on innovative and sustainable products, should allow the company to increase prices and successfully manage the current raw material price inflation along with increased freight and logistic costs. In the first half of 2022, Essity posted 16.3% organic sales growth, about 28% on a reported basis with a solid price and product mix development of about 11%. Despite the exceptional pressures on the costs, EBITDA declined only 8% in the same period, although the reported EBITDA margin dropped 500 bps to 13%. We notice that the unprecedent high level of inflation requires frequent pricing adjustments, translating into some delay for the group to fully offset the cost increases. Also, in the health and medical segment (16% of group sales in the first half of 2022), price adjustments are less frequent because tenders for this business are conducted every three years. Therefore, as raw material costs are expected to increase further in the third quarter of 2022, we estimate the company will continue to increase prices in the second half of 2022 supporting 20%-25% top-line growth for the year. Essity's product categories are essential (mainly in developed markets), and so we do not expect consumers will reduce consumption of personal hygiene products. However, budget-conscious consumers could increasingly opt for private label value ranges to save money, which could partially hit Essity's volumes, mainly in European countries. In countries such as France and Germany, private label penetration accounts for 45%-55% of the total tissue and hygiene market in 2021 by retail value, according to Euromonitor. Other developed countries such as U.S. have lower but increasing penetration of private labels in the range of 20%-25%.

Essity's global manufacturing footprint should alleviate pressures on production in case of severe energy shortages in European countries. At the end of 2021, energy accounted for 4%-5% of the group's sales. We believe that supply constraints in European countries linked to the unwinding of commercial relations with Russia could hit production. This could stem from imposition of the EU's embargo or Russia increasingly reducing gas flows to Europe. Under these circumstances, the energy price could further increase and we would also expect lower utilization capacity imposed by local governments to firms. Essity relies on a well-diversified geographic manufacturing footprint, which is required to ensure customer proximity and adequate service levels, and to reduce logistics expense. In the most energy-intensive consumer tissue and professional hygiene segments, about 12% of Essity's global manufacturing capacity is in Germany, which is the group's largest manufacturing country in Europe. Other main production countries, such as China and the U.S., accounted for 30% and 13% of the total capacity at the end of 2021. Therefore, Essity has some capacity to avoid severe disruption by relocating capacity in other countries. Alternatively, the company could use liquified natural gas (LNG) instead of pipeline gas, and could rely on the current stock to prevent any immediate pressures in case of gas shortages.

Essity has limited headroom in 2022 to complete large acquisitions given we expect leverage will increase into the 3.0x-3.2x range this year. This is slightly above the 2x-3x range threshold for the current rating and reflects the temporary erosion of EBITDA due to the high input cost, as well as the increased leverage to finance the recently announced acquisition of washable absorbent underwear companies KnixWear and Modibodi. These acquisitions resulted in roughly Swedish krona (SEK) 5 billion additional debt, including the put/call option on the 20% of stake in Knix that Essity does not own. Excluding those acquisitions, we estimated leverage would have remained at or slightly below 3.0x. We believe Essity should be able to quickly reduce leverage into the 2.5-3.0x range from 2023 thanks to the pro-active raise in sales prices to meet the high inflation. We also view positively Essity's commitment to the current rating, which will likely translate into a cautious approach on capital allocation. Therefore, we do not expect other material debt-funded acquisitions in the reminder of the year, given the very limited headroom under the leverage ratio.

Outlook

The stable outlook reflects our view that Essity's established brand portfolio supporting sales price increases and product innovation should limit EBITDA erosion this year from continued raw material and logistic price hikes. While we expect S&P Global Ratings-adjusted debt to EBITDA to increase into the 3.0x-3.2x in 2022 and we believe the group should reduce leverage from 2023 to below 3.0x supported by the group's financial policy discipline.

Downside scenario

We could consider lowering the rating if, due to the current inflationary environment, consumers become a lot more price sensitive and shift to private-label products or the company loses market share because it is not able to serve its customers due to raw material (i.e. energy) availability. Under this scenario we would expect Essity's market position to deteriorate and operating performance to likely weaken, translating into adjusted debt to EBITDA permanently exceeding 3x.

We could also consider a negative rating action if we were to observe an aggressive financial policy that led to increased financial leverage, because of large debt-funded acquisitions or unexpectedly large shareholder distributions, pushing debt to EBITDA above 3x for a prolonged period.

Upside scenario

We could consider a positive rating action if Essity generated very solid free operating cash flow (FOCF) among its three divisions and uses it to improve its leverage ratios, with debt to EBITDA approaching 2x. Achieving these targets consistently also depends on the group's commitment to adapt its future debt-funded acquisitions to said targets.

Our Base-Case Scenario

Assumptions

- Real GDP growth of 2.4% in 2022 in the U.S. compared with 5.7% in 2021. We also expect lower real GDP growth in the eurozone at 2.6% versus 5.4% a year earlier. China's real GDP is expected to expand 3.3% this year compared with 8.1% last year.
- Essity's reported sales to increase in the range of 20%-25% in 2022 mainly driven by sales price increase across its three divisions and a marked recovery of volumes in the professional hygiene division. We also assume 8%-9% positive impact from foreign currency exchange effects, mainly due to the appreciation of the U.S. dollar versus the Swedish krona. Our sales forecast assumes pro-forma effects of the acquired businesses KnixWear and Modibodi, the exit of Russia (2% negative impact), and the closing of the baby diapers operations in Latin America. For 2023 we currently estimate modest sales growth of 5% because the group will benefit from the full-year impact of sales price increases and adjustments of prices in the health and medical segment as contracts are gradually renewed.
- Given the current trends in raw material prices, we expect the S&P Global Ratings-adjusted EBITDA margin will contract to about 13% in 2022 versus 16.4% in 2021. Although Essity maintains a proactive approach to increasing sales prices, there is some lag in the time it takes to fully recover the raw material hikes. This is exacerbated by the ongoing increase of costs, which requires multiple price adjustments. Furthermore, Essity’s innovative pipeline of new products supports a better product mix. From 2023, we expect S&P Global Ratings-adjusted EBITDA margin will approach 14%-15% under the scenario that main costs will stabilize at a high level.
- Capital expenditure (capex) of SEK8.0 billion-SEK8.5 billion over the next two years (about 5%-5.5% of sales). This includes investment to support Essity's digital transformation.
- About SEK5 billion invested in acquisitions this year, which only include the acquisitions of Legacy Converting, KnixWear and Modibodi. Therefore, in our base case, we do not assume additional deals for the rest of the year. We estimate SEK5.0 billion in annual acquisitions from 2023.
- Dividends of about SEK5.2 billion, including SEK307 million paid to minority shareholders in 2022. In 2023, we assume dividends will increase to SEK5.4 billion-SEK5.5 billion.

Key metrics

Essity AB--Key Metrics*

Mil. SEK	2020a	2021a	2022e	2023f	2024f

Revenue	121,752	121,867	151,500- 152,500	159,000-160,000	163,000-164,000
EBITDA margin (%)	19.8	16.4	~13	14-15	16-17
Capital expenditure	6,587	7,358	8,000-8,500	8,000-8,500	8,000-8,500
Reported Free operating cash flow (FOCF)	11,212	7,309	6,000-7,000	9,000-10,000	12,000-13,000
Dividends	4,813	5,312	5,000-5,500	5,000-5,500	5,500-6,000
Acquisitions (including minority interests)	668	10,363	5,000	5,000	5,000
Debt to EBITDA (x)	1.8	2.8	3-3.2	2.5-3.0	2.5-3.0
FFO to debt (%)	43.9	28.2	25-30	25-30	30-35
FOCF to debt (%)	25.5	13	10-15	10-15	15-20

*All figures adjusted by S&P Global Ratings. a--Actual. e--Estimate. f--Forecast. SEK--Swedish krona.

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Company Description

Essity is a Swedish health and hygiene group created when Svenska Cellulosa spun off its hygiene division in 2017. It produces and sells personal care, tissue, and health and medical products. In the 12 months ended June 30, 2022, Essity posted roughly SEK137.6 billion sales (up about 18.5% versus the same period a year earlier) and reported EBITDA of about SEK19.8 billion with an EBITDA margin of 14.4%.

Essity operates through three main divisions:

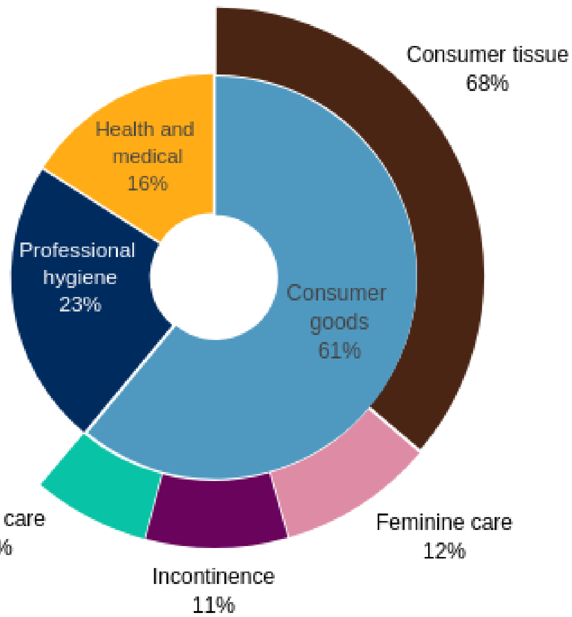
– Consumer Goods (61% of Essity's sales as of June 2022). It includes adult incontinence products (global market leadership with Tena brand), baby care (such as baby diapers, baby pants/diapers), feminine care products (pads, panty liners, tampons), and consumer tissue (toilet paper, household towels, facial tissues, wet wipes, napkins, and face masks) sold in the retail trade channel and online.
– Professional hygiene (23% of sales). The group develops and markets complete hygiene solutions under the global leading brand Tork. These include toilet paper, paper hand towels, napkins, hand sanitizer, tissue and dispensers, and service and maintenance for companies and office buildings, universities, health care facilities, restaurants, hotels, and other public venues.
– Health & Medical (16% of sales) comprises wound care, compression therapy, and orthopedics products. Essity established a solid presence in the market following the acquisition of BSN in 2017. Its global and regional brands include Leukoplast, and Jobst, among others.

Essity is present in more than 150 countries globally, with Europe accounting for 52.6% of total sales as of June 30, 2022, Asia Pacific 17.5%, Latin America 13.4%, and North America 13.2%. Other countries account for the remaining 3.3%

Essity is listed on the Nasdaq Stockholm exchange with its largest shareholder being AB Industrivärden with an about 10% stake at the end of 2021. Essity's market capitalization was about $17 billion as of August, 2022.

Essity AB--Net Sales By Business Area

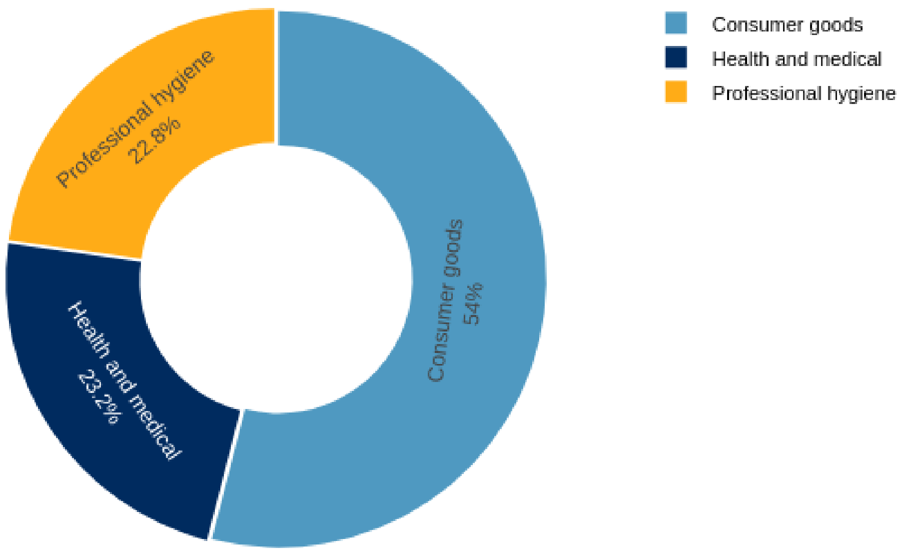
as of June 2022



Source: Company presentation

Essity AB--EBITA By Division

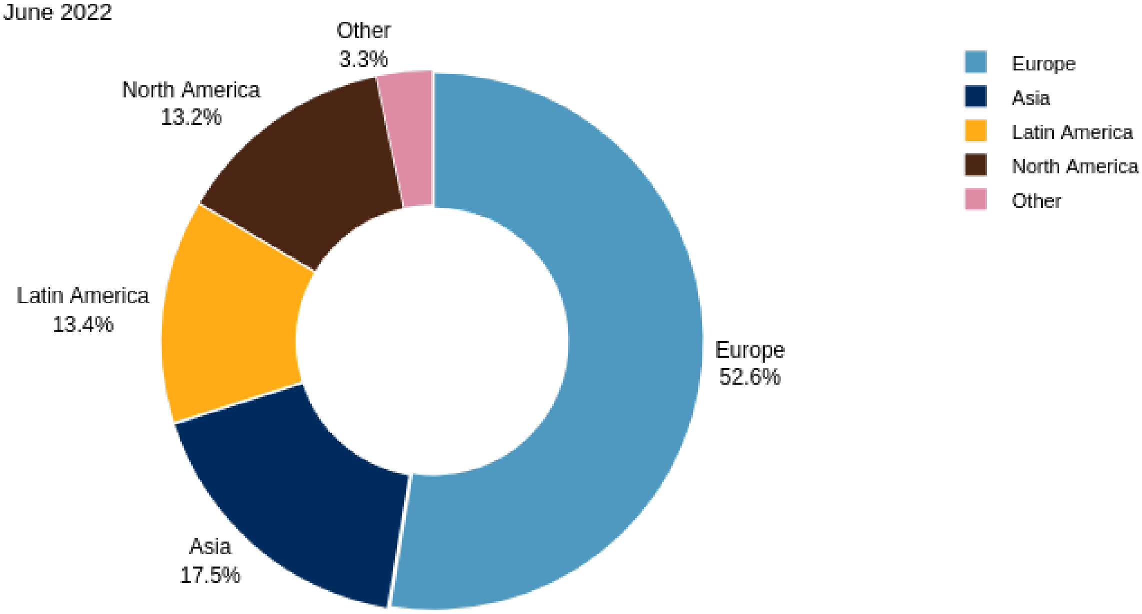
as of June 2022



Source: Company presentation

Essity AB--Net Sales By Region

as of June 2022



Source: Company presentation

Peer Comparison

U.S.-based Kimberly Clark (KC) is Essity's closest peer. It is the No.2 player globally in tissues and hygiene products, while Essity is No.3. KC's EBITDA margin has been structurally higher than Essity's, at above 20% on average over 2018-2021 compared with Essity's 17%. We believe this is partly explained by KC's U.S. domestic market being more profitable than several of the European countries in which Essity operates. In fact, private labels have a lower penetration in the U.S. than in Europe, which allows U.S. players to maintain higher prices. KC has five "billion-dollar" brands, while Essity has two (TENA and TORK). KC has, over time, maintained more conservative credit metrics with S&P Global Ratings-adjusted debt to EBITDA at 2.0x-2.2x while 2021 and expectations for 2022 points to higher leverage in the 2x-2.5x range which explains the current negative outlook.

German company Henkel is larger and more diversified than Essity in terms of products. It competes in home care, personal care, and adhesive technologies. Henkel is the global leader in adhesive technologies, whereas in home care and personal care it usually ranks No.2, No.3, or lower, behind large players such as Procter & Gamble (P&G), Unilever, or L'Oreal. Competitive pressures in core segments like home care and personal care, as well as inflationary pressures, explain a deterioration in the EBITDA margin of about 12% expected in 2022 compared with 16% in 2020 and 2021; Henkel maintains a very conservative financial risk profile and its adjusted leverage is below 1.5x. However, our 'A' rating incorporates Henkel's ambition for external growth and a potential increase in leverage.

U.S.- based P&G competes with Essity in many geographies in the personal care market. However, it is much larger in scale and operates with a more extensive personal care and household products portfolio, so it is much more diversified. These factors, coupled with much higher profitability in the 25%-30% range, contribute to our more favorable view of P&G's business risk. P&G also has stronger metrics, with leverage generally in the 1.0x-1.5x area.

Essity AB--Peer Comparisons

	Essity AB	Kimberly-Clark Corp.	Henkel AG & Co. KGaA	Procter & Gamble Co.
Foreign currency issuer credit rating	BBB+/Stable/A-2	A/Negative/A-1	A/Stable/A-1	AA-/Stable/A-1+
Local currency issuer credit rating	BBB+/Stable/A-2	A/Negative/A-1	A/Stable/A-1	AA-/Stable/A-1+
Period	Annual	Annual	Annual	Annual
Period ending	2021-12-31	2021-12-31	2021-12-31	2022-06-30
Mil.	$	$	$	$
Revenue	13,478	19,440	22,822	80,187
EBITDA	2,207	3,636	3,654	21,364
Funds from operations (FFO)	1,713	2,885	2,846	17,069
Interest	90	272	39	465
Cash interest paid	93	259	68	477
Operating cash flow (OCF)	1,591	2,871	2,503	16,917
Capital expenditure	803	1,007	736	3,156
Free operating cash flow (FOCF)	788	1,864	1,767	13,761
Discretionary cash flow (DCF)	201	(52)	847	(5,012)
Cash and short-term investments	432	686	2,407	7,214
Gross available cash	432	686	2,706	7,214
Debt	6,075	8,992	1,716	26,992
Equity	7,577	737	22,512	46,854
EBITDA margin (%)	16.4	18.7	16.0	26.6
Return on capital (%)	11.2	27.5	10.8	24.1
EBITDA interest coverage (x)	24.5	13.4	94.5	45.9
FFO cash interest coverage (x)	19.5	12.1	42.7	36.8
Debt/EBITDA (x)	2.8	2.5	0.5	1.3
FFO/debt (%)	28.2	32.1	165.8	63.2
OCF/debt (%)	26.2	31.9	145.8	62.7
FOCF/debt (%)	13.0	20.7	103.0	51.0
DCF/debt (%)	3.3	(0.6)	49.4	(18.6)

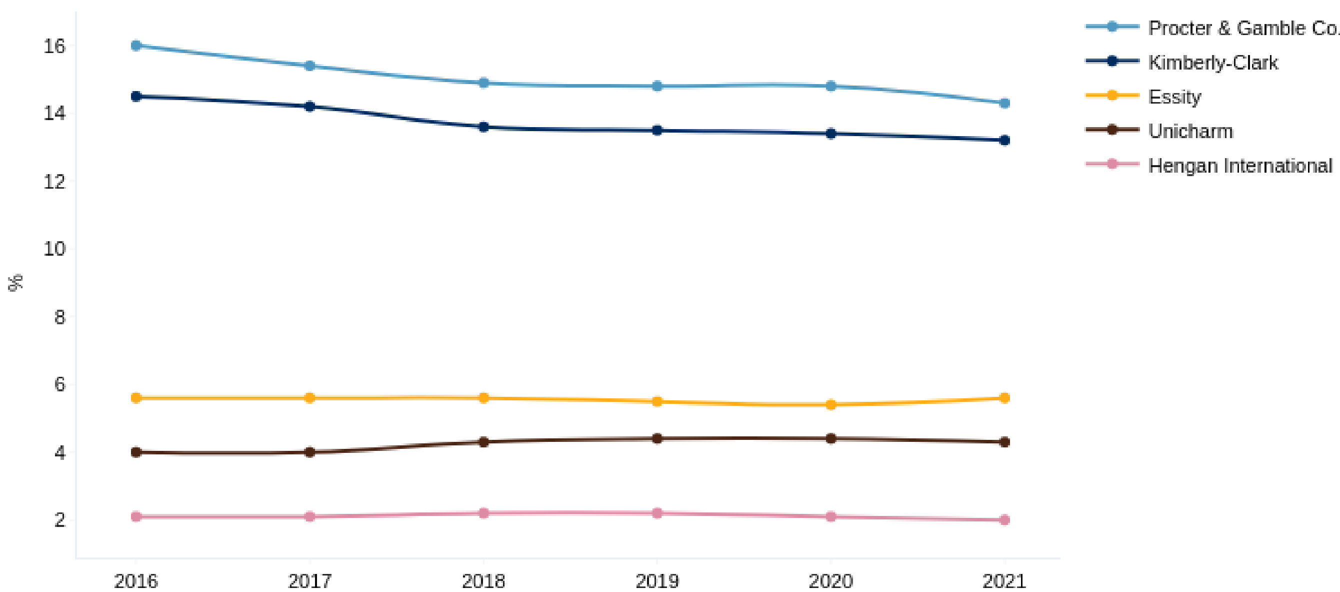
Business Risk

Essity ranks no. 3 in the global tissue and personal hygiene market with a 5.6% market share at the end of 2021. The global tissue and hygiene market was worth US$201.6 billion by retail value at the end of 2021 according to Euromonitor. It estimates the market will expand at a compounded annual growth rate (CAGR) of 5.5% over 2021-2026 compared with the 4% average over 2016-2021. The adult incontinence segment has the strongest growth prospects and over 2021-2026 is expected to grow at 8.5% CAGR in the light adult incontinence segment and 10% in the moderate/heavy adult incontinence segment, according to Euromonitor. This is supported by aging populations in mature markets and increasing awareness of incontinence issues in young adults.

At year end 2021 Essity's market share slightly increased to 5.6% compared with 5.4% a year earlier, retaining its No.3 position ahead of Unicharm (4.3% market share). The market remains dominated by large multinationals such as P&G and KC with 14.3% and 13.2% market share, respectively.

Market Share Evolution: Global Tissue And Hygiene Market (2016-2021)

Top 5 players



Source: Euromonitor 2021

Essity has a good diversity in the personal hygiene market and its brand portfolio holds best-in-class market share in many product categories and regions. Essity generated 61% of its sales in the consumer goods division with presence across multiple categories distributed mainly through retail-trade and online. Consumer tissue accounted for 68% of the consumer goods division, feminine care for 12%, adult incontinence products for 11%, and baby care for 9% at the end of June 2022. Essity ranks No.1 in Western Europe in the consumer tissue market, supported by its established brands Lotus (leading brand with 3.8% market share), Tempo, and Zewa, while Kimberly Clark (Andrex brand) and Sofidel (Regina brand) rank second and third. In Mainland China, Essity – through Vinda - has the leading position in the tissue market with a 18.4% market share at end 2021, according to management. Essity is the leader in Latin America in feminine care through its local Nosotras and Saba brands. In the baby care segment, it is No.2 in Europe with its Libero and Lotus brands, and No.1 in Malaysia with its Drypers brand (about 45% market share according to management).

The professional hygiene segment accounted for 23% of Essity's net sales as of June 2022 and we estimate the group has a global leading position with its Tork brand. We expect this division will lead the group's top-line growth in 2022 thanks to a more normalized demand in the customer segments of the hotels, restaurants, commercial buildings, schools, and universities affected by pandemicrelated restrictions. We expect the improved operating leverage will also support profitability, despite the hit from the high raw material prices including pulp and energy as well as freight expenses. Lastly, the health and medical division accounted for 16% of sales, which refers to the sale of incontinence products in the healthcare channel (58% of the business' sales) to pharmacies and hospitals (TENA brand mainly) and medical solutions brands such as Leukoplast and Jobst, among others. The market offers positive growth prospects due to aging populations and increasing demand for chronic wound and compression treatments.

Kimberly Clark is the leader company in the adult incontinence in the retail channel, with an 18.3% market share stemming from a diversified brand portfolio comprising Depend, Poise, and Plenitud, among others. However, Essity's brand TENA retains global leadership in the market with its 16.9% global market share by retail value at end-2021 according to Euromonitor.

Essity aims to establish leading position in the fast-growing washable absorbent underwear market thanks to the acquisition of KnixWear and Modibodi. According to Essity's management the core washable absorbent underwear market is worth US$540 million globally (it excludes Asia, Middle East, India, Asia, and non-core European countries). The industry is expected to grow at a 20% CAGR over 2021-2026 which is above the average rates for other personal hygiene categories, such as male and female incontinence. This is because of their convenience and the sustainable feature of these products being washable and reusable compared with other common disposable incontinence products. At the end of 2021, Essity had a limited presence in this market through its reusable underwear products sold under the brands Tom Organic, Tena, and Bodyform (Libresse).

To further accelerate its presence, Essity recently finalized two acquisitions:

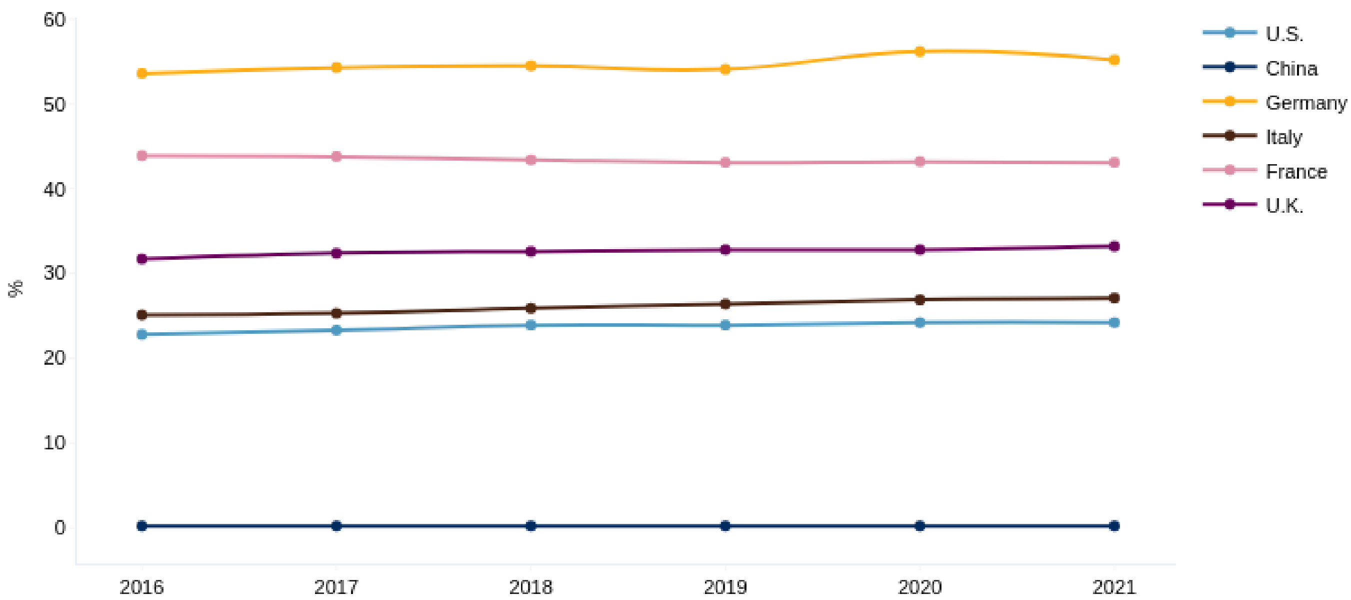
- Canada-based company KnixWear operating in the functional intimate apparel and activewear and generating close SEK914 million net sales in 2021 predominantly in U.S. and Canada through direct-to-consumer channel, mainly e-commerce based. The company has about 30% market share in North America. The transaction involved 80% stake for a purchase price of roughly SEK3.3 billion. The remaining 20% stake will be held by KnixWear's founder and CEO.
- Modibodi is an Australian company competing in the underwear and swimwear market with leading market share in Australia of about 40%. It generated SEK985 million sales at the end of 2021 of which 95% online and purchase price was roughly SEK985 million.

The acquired companies will be run independently from Essity and therefore we do not expect material integration risks emerging from the acquisitions. That said, we believe Essity's size and well diversified geographic footprint have potential to accelerate the growth of the acquired companies.

Persisting inflationary pressures could lead to increase consumer preference for private label products. The growth of the personal hygiene market is primarily driven by increasing awareness related to the health benefits of maintaining cleanliness and personal hygiene. The outbreak of COVID-19 led consumers to increasingly adopt best hygiene practices which could reduce infections and spread of viruses. Overall, we believe that personal care products are an essential consumer product category, mainly in developed countries, and we do not expect a material contraction of demand, despite higher prices pushed by raw material inflation. However, we anticipate potential changes in consumer shopping habits in light of a general increase of the entire grocery shopping basket. In this context. private label manufacturers, as well as small and niche manufacturers, could gain momentum as they can take benefit of better cost competitiveness associated with good quality, innovation, and improved sustainability credentials. Essity has limited private label operations in the European consumer tissue division, accounting for 5%-6% of total sales at the end of June 2022 according to our calculations. In the second quarter of 2022 this division posted 31.7% organic growth, exceeding the performance of the entire consumer tissue division and growing at 21.6% rate, supported by both volumes and prices.

Evolution Of Private Label Penetration--Global Tissue And Hygiene Market (2016-2021)

In U.S., China, Germany, Italy, France and U.K.



Source: Euromonitor 2021

Essity is well placed to capitalize on the momentum of e-commerce and increasing demand for sustainable products. Tissue and hygiene has seen an increasing number of small eco/green brands entering the market over the past few years, primarily with e-commerce operations and increasingly expanding through subscriptions or entering the retail trade. This trend was accelerated by COVID-19 and many consumers are likely to continue shopping online thanks to the convenience, budget-friendly deals, and good range of options offered. Essity has strengthened its online capabilities and its online sales grew 25% in the second quarter of 2022 versus the same period last year, accounting for 15% of total sales at the end of June 2022, compared with 10% in 2019. This is above the global tissue and hygiene market average of about 13% at year-end 2021.

Our business risk profile assessment also takes in consideration Essity's focus on innovation with stable R&D expenses at 1.2% of total sales for 2021 (about SEK1.5 billion) and commitment to launch at least 50% sustainable innovations per year, leading to social or environmental improvements. It supported continuing market share expansion, for approximately 50% of branded sales in the retail trade over the 12 months ended June 30, 2022 , according to management.

Essity's profitability is structurally exposed to some degree of volatility, mainly because of fluctuations of pulp prices. Pulp is the largest component of Essity's cost structure, accounting for 13%-14% of total sales in 2021. Over the past few years, Essity has been able to avoid significant erosion of its profitability thanks to sales price management, improved product mix, and ability to achieve cost savings in the range of SEK500 million–SEK1,000 million per year supported by optimization of manufacturing capacity. Since 2021 there has been general increase of raw material prices, such as super absorbents and non-woven products accounting for 4%-5% of total sales in 2021. Also, the rapid increase of energy prices (4%-5% of Essity's sales) and potential natural gas shortages in Europe driven by the Russia-Ukraine conflict pose additional challenges to Essity's profitability in the short term.

We believe the company could restore S&P Global Ratings-adjusted EBITDA margin to close to 17% in the next two to three years, compared with about 13% expected in 2022; however, there will be some time delay because sales prices in the retail trade can only be negotiated once there is evidence that raw material prices have increased and will remain elevated. Also, in the health and medical division, contracts are based on an auction system and agreements usually last three years, during which prices cannot be renegotiated.

Essity has a well-diversified geographic footprint by sales with a focus on fast-growing emerging markets. China is Essity's largest market, accounting for 14% of total sales at the end of 2021. Germany and the U.S. accounted for 10% and 11% of sales, respectively, while France and the U.K. account for about 8% each. Other countries generated less than 5% of total sales each. The group aims to expand its penetration in emerging markets, which accounted for 38% of its sales in 2021 (37% in 2020). This is because of better growth prospects as market penetration of hygiene and health products is lower than in the mature markets. As an example, Essity calculated usage of incontinence products in Asia is only about one-sixth of those in Western Europe. Also, tissue consumption in Eastern Europe is only about one-third of that in Western Europe.

Furthermore, emerging markets are showing rapid development of urbanization, retail, and e-commerce infrastructure, as well as improving health care systems. We understand that Essity plans to prioritize growth in selected emerging markets such as China, Southeast Asia, Latin America, and Eastern Europe. The company announced its intention to exit Russia, which accounted for 2% of 2021 sales or SEK2.8 billion, and recently exited its baby diapers operations in Latin America, which we estimate will have an annual impact on sales of less than SEK200 million.

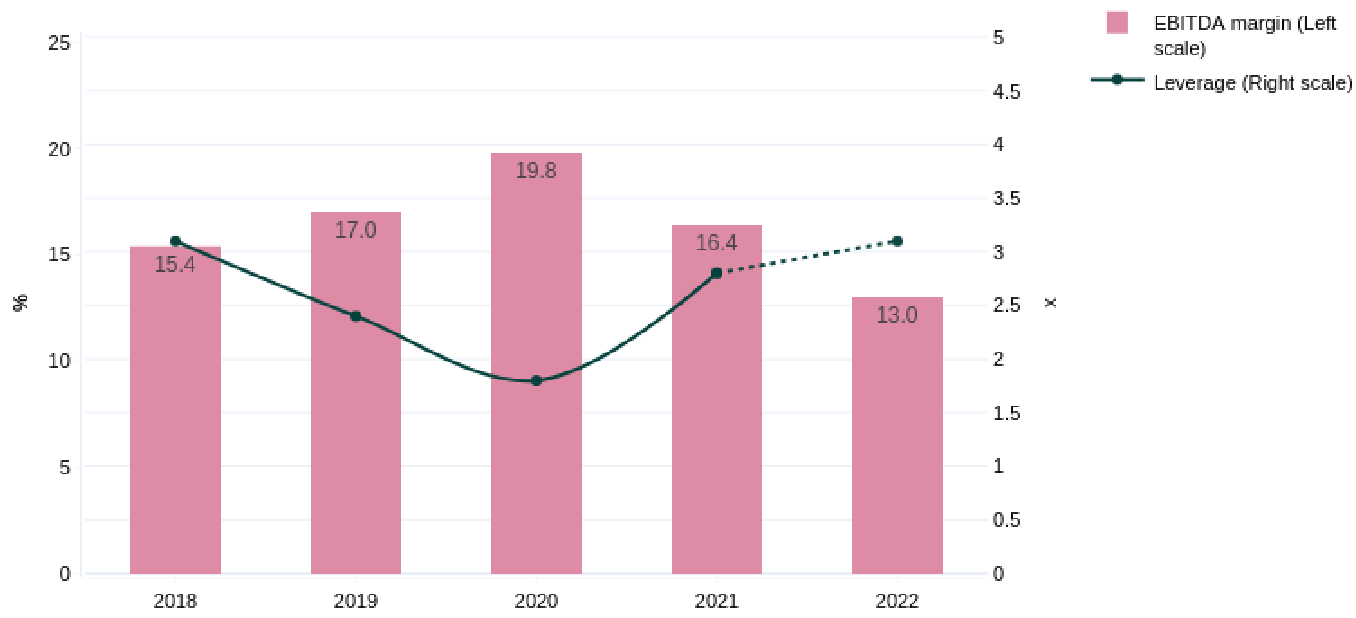
Financial Risk

Essity has been able to keep fairly stable leverage inside the target 2x-3x range over 2016-2021, with few exceptions such as 3.1x in 2018 and 3.0x-3.2x expected this year. This is despite the volatility of its main raw materials, such as pulp and recovered paper, as well as recent increases of prices for oil-based derivatives and energy prices. During the last few years Essity remained active in M&A transactions which did not materially affect the leverage ratio.

Essity has indicated interest in acquisitions, both in the medical solutions segment, and in adjacent categories of incontinence and feminine products, and professional hygiene. We assume that external growth will be commensurate with the current rating headroom because management has clearly communicated its target to keep the current rating. We assume that Essity will stay focused on cash generation and rebuilding debt headroom to pursue other bolt-on acquisitions.

We expect FOCF generation will slightly reduce into the range of SEK 6 billion–SEK 7 billion in 2022 compared with SEK7.3 billion in 2021. We anticipate cash flow generation could approach again SEK10 billion starting from 2023. We assume Essity will continue to ensure growing shareholder remuneration with increasing annual dividend payments, in line with cash flow generation growth. Essity has further flexibility to increase shareholder returns with its share buyback program, in our view. However, we do not anticipate any share purchases in our forecasts, in line with historical trends.

S&P Adjusted EBITDA Margin And Debt To EBITDA Evolution (2018-2022E)



Source: S&P Global Ratings.

Debt maturities

- 2022: SEK14.2 billion
- 2023: SEK6.5 billion
- 2024: SEK9.7 billion
- 2025: SEK7.4 billion
- Thereafter: SEK25.7 billion

Essity has the following notes outstanding:

- €500 million notes with 2.5% coupon due 2023
- €600 million notes with 1.125% coupon due 2024
- SEK850 million notes with 0.5% coupon due 2025
- SEK2.15 billion floating rate note due 2025
- €300 million notes with 1.125% coupon due 2025
- €500 million notes with 1.625% coupon due 2027
- €600 million notes with 0.250% coupon due 2029
- €300 million notes with 0.5% coupon due 2030

– €700 million notes with 0.25% coupon due 2031

Essity AB--Financial Summary

Period ending	Dec-31-2016	Dec-31-2017	Dec-31-2018	Dec-31-2019	Dec-31-2020	Dec-31-2021
Reporting period	2016a	2017a	2018a	2019a	2020a	2021a
Display currency (mil.)	SEK	SEK	SEK	SEK	SEK	SEK
Revenues	101,238	109,265	118,500	128,975	121,752	121,867
EBITDA	16,219	19,076	18,266	21,973	24,120	19,958
Funds from operations (FFO)	11,375	15,071	14,760	19,755	19,311	15,486
Interest expense	1,143	1,207	1,117	1,126	912	815
Cash interest paid	1,062	1,034	1,040	1,088	892	838
Operating cash flow (OCF)	13,095	13,084	13,698	18,337	17,756	14,389
Capital expenditure	6,289	6,119	6,882	5,811	6,544	7,263
Free operating cash flow (FOCF)	6,806	6,965	6,816	12,526	11,212	7,126
Discretionary cash flow (DCF)	2,578	6,680	2,381	8,152	6,399	1,814
Cash and short-term investments	4,244	4,107	3,008	2,928	4,982	3,904
Gross available cash	4,244	4,107	3,008	2,928	4,982	3,904
Debt	37,008	54,150	57,147	51,769	44,011	54,931
Common equity	39,580	49,570	54,899	62,801	63,342	68,507
Adjusted ratios						
EBITDA margin (%)	16.0	17.5	15.4	17.0	19.8	16.4
Return on capital (%)	14.1	14.5	10.7	12.9	15.2	11.2
EBITDA interest coverage (x)	14.2	15.8	16.4	19.5	26.4	24.5
FFO cash interest coverage (x)	11.7	15.6	15.2	19.2	22.6	19.5
Debt/EBITDA (x)	2.3	2.8	3.1	2.4	1.8	2.8
FFO/debt (%)	30.7	27.8	25.8	38.2	43.9	28.2
OCF/debt (%)	35.4	24.2	24.0	35.4	40.3	26.2
FOCF/debt (%)	18.4	12.9	11.9	24.2	25.5	13.0
DCF/debt (%)	7.0	12.3	4.2	15.7	14.5	3.3

Reconciliation Of Essity AB Reported Amounts With S&P Global Adjusted Amounts (Mil. SEK)

		Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Financial year	Dec-31-2021										

Reconciliation Of Essity AB Reported Amounts With S&P Global Adjusted Amounts (Mil. SEK)

	Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
Company reported amounts	54,418	59,874	121,867	20,590	13,199	709	19,958	14,667	5,312	7,358
Cash taxes paid	-	-	-	-	-	-	(3,634)	-	-	-
Cash interest paid	-	-	-	-	-	-	(781)	-	-	-
Trade receivables securitizations	1,100	-	-	-	-	-	-	(183)	-	-
Lease liabilities	3,771	-	-	-	-	-	-	-	-	-
Postretirement benefit obligations/ deferred compensation	-	-	-	66	66	49	-	-	-	-
Accessible cash and liquid investments	(3,204)	-	-	-	-	-	-	-	-	-
Capitalized interest	-	-	-	-	-	57	(57)	(57)	-	(57)
Capitalized development costs	-	-	-	(38)	(3)	-	-	(38)	-	(38)
Dividends from equity investments	-	-	-	72	-	-	-	-	-	-
Income (expense) of unconsolid. cos.	-	-	-	(58)	-	-	-	-	-	-
Nonoperating income (expense)	-	-	-	-	102	-	-	-	-	-
Noncontrolling/ minority interest	-	8,633	-	-	-	-	-	-	-	-
Debt: Derivatives	(1,154)	-	-	-	-	-	-	-	-	-
EBITDA - Gain/(loss) on disposals of PP&E	-	-	-	34	34	-	-	-	-	-
EBITDA: Settlement (litigation/ insurance) costs	-	-	-	(54)	(54)	-	-	-	-	-
EBITDA: other	-	-	-	(654)	(654)	-	-	-	-	-

Reconciliation Of Essity AB Reported Amounts With S&P Global Adjusted Amounts (Mil. SEK)

	Debt	Shareholder Equity	Revenue	EBITDA	Operating income	Interest expense	S&PGR adjusted EBITDA	Operating cash flow	Dividends	Capital expenditure
D&A: Impairment charges/ (reversals)	-	-	-	-	179	-	-	-	-	-
Total adjustments	513	8,633	-	(632)	(330)	106	(4,472)	(278)	-	(95)
S&P Global Ratings adjusted	**Debt**	**Equity**	**Revenue**	**EBITDA**	**EBIT**	**Interest expense**	**Funds from Operations**	**Operating cash flow**	**Dividends**	**Capital expenditure**
	54,931	68,507	121,867	19,958	12,869	815	15,486	14,389	5,312	7,263

Liquidity

The short-term global scale rating is 'A-2' and the short-term Nordic scale rating is 'K-1'. We assess Essity's liquidity as strong as we expect liquidity sources to cover uses by more than 1.5x over the next 12-24 months. Our assessment is supported by its track record of high standing in credit metrics, solid relationship with its diverse and creditworthy banking groups allowing frequent bond issuance and commercial paper availability. Essity relies on SEK15 billion Swedish commercial paper and €1.2 billion Belgian commercial paper programs (not included in the liquidity sources below). At the end of June 30, 2022, SEK10 billion commercial papers were used.

Principal liquidity sources

- Cash available of about SEK5 billion on June 30, 2022;
- Cash funds from operations of SEK16.0 billion-SEK16.5 billion in the next 12 months and SEK18.5-SEK19 billion thereafter; and
- Two undrawn bank lines maturing beyond 12 months of SEK21.3 billion (€2 billion).

Principal liquidity uses

- Debt maturities of SEK19.5 billion-SEK20 billion in the 12 months from June 30, 2022;
- Working capital outflows of SEK0.5 billion SEK1.0 billion including intra-year requirements;
- Annual capex of SEK8 billion-SEK8.5 billion;
- Committed acquisitions in the range of SEK 4 billion–SEK4.5 billion.

Environmental, Social, And Governance

ESG Credit Indicators

E-1	**E-2**	E-3	E-4	E-5

S-1	**S-2**	S-3	S-4	S-5

G-1	G-2	G-3	G-4	G-5

Environmental	Social	Governance
- N/A	- N/A	- Risk management, culture, and oversight

N/A—Not applicable. ESG credit indicators provide additional disclosure and transparency at the entity level and reflect S&P Global Ratings' opinion of the influence that environmental, social, and governance factors have on our credit rating analysis. They are not a sustainability rating or an S&P Global Ratings ESG Evaluation. The extent of the influence of these factors is reflected on an alphanumerical 1-5 scale where 1 = positive, 2 = neutral, 3 = moderately negative, 4 = negative, and 5 = very negative. For more information, see our commentary "ESG Credit Indicator Definitions And Applications," published Oct. 13, 2021.

Governance factors are a moderately positive consideration in our credit rating analysis of Essity AB. Essity's management has proven to be well prepared to address environmental and social factors, such as waste and pollution, access to health-related products thanks to its new product development strategy and sustainable manufacturing processes. Environmental and social factors are an overall neutral consideration. Essity consistently exceeded its commitment to launch at least 50% sustainable innovations leading to social and/or environmental improvements. Its leading innovations around reusable personal care products as well as increasing focus on recycled and renewable raw materials seek to address rising environmental risks and develop competitive opportunities. In our view, Essity will benefit from increasing consumer demand for personal hygiene products in its core markets, which the company serves through its strategic global footprint of products addressing all demographics, and a variety of health needs.

Rating Component Scores

Foreign currency issuer credit rating	**BBB+/Stable/A-2**
Local currency issuer credit rating	**BBB+/Stable/A-2**
Business risk	**Strong**
Country risk	Low
Industry risk	Low
Competitive position	Strong
Financial risk	**Intermediate**
Cash flow/leverage	Intermediate
Anchor	**bbb+**
Diversification/portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Strong (no impact)
Management and governance	Strong (no impact)
Comparable rating analysis	Neutral (no impact)
Stand-alone credit profile	**bbb+**

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- General Criteria: Methodology For National And Regional Scale Credit Ratings, June 25, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings Detail (as of September 02, 2022)*

Essity AB		
Issuer Credit Rating		BBB+/Stable/A-2
Nordic Regional Scale		--/--/K-1
Senior Unsecured		BBB+
Issuer Credit Ratings History		
10-Apr-2017		BBB+/Stable/A-2
10-Apr-2017	*Nordic Regional Scale*	--/--/K-1
Related Entities		
Essity Capital B.V.		
Senior Unsecured		BBB+

*Unless otherwise noted, all ratings in this report are global scale ratings. S&P Global Ratings credit ratings on the global scale are comparable across countries. S&P Global Ratings credit ratings on a national scale are relative to obligors or obligations within that specific country. Issue and debt ratings could include debt guaranteed by another entity, and rated debt that an entity guarantees.