Sappi Limited
Registration number: 1936/008963/06
JSE code: SAP
ISIN code: ZAE000006284
Issuer code: SAVVI
("Sappi" or "the company")

Fourth quarter results for the period ended September 2022 and cash dividend declaration

Short-form SENS announcement

	Quarter ended			Year ended		
US$ million	**Sep 2022**	**Sep 2021**	% Change	**Sep 2022**	**Sep 2021**	% Change
Sales	1 923	1 425	35%	7 296	5 265	39%
EBITDA excluding special items	391	177	121%	1 339	532	152%
Profit for the period	26	35	-26%	536	13	4023%
Net debt	1 163	1 946	-40%	1 163	1 946	-40%
Headline EPS (US Cents)	37	9	311%	130	5	2500%
Basic EPS (US Cents)	5	6	-17%	95	2	4650%
EPS excluding special items (US Cents)	44	11	300%	138	15	820%
Net asset value (US Cents)	417	351	19%	417	351	19%
Dividend per share (US cents)	-	-	N/M	15	-	N/M

N/M – Not meaningful

Sappi is a leading global provider of everyday materials made from woodfibre-based renewable resources. As a diversified, innovative and trusted leader focused on sustainable processes and products, we are building a more circular economy by making what we should, not just what we can.

Our raw material offerings (such as dissolving pulp, wood pulp, biomaterials and timber) and end-use products (specialities and packaging papers, graphic papers, casting and release papers and forestry products) are manufactured from woodfibre sourced from sustainably managed forests and plantations, in production facilities powered, in many cases, with bio-energy from steam and existing waste streams.

Together with our partners, Sappi works to build a thriving world by acting boldly to support the planet, people and prosperity.

Commentary

Fourth quarter September 2022[1]

The strong operating performance continued into the fourth quarter. Improved profitability for the pulp segment and another excellent performance by the North American region more than offset substantially higher raw material costs, principally energy in Europe. Consequently, the group delivered a new record quarterly EBITDA excluding special items of US$391 million, which was US$20 million above the previous record achieved in the prior quarter.

The graphic paper segment continued to benefit from favourable market conditions, which supported quarter-on-quarter sales price increases. However, extraordinary cost inflation in Europe, particularly for energy, reduced segmental margins relative to the prior quarter. Graphic paper sales volumes declined 4% year-on-year due to lower inventory levels and a shift towards packaging and speciality paper grades. Order activity began slowing towards the end of the quarter as consumer sentiment dampened with the inflationary pressures and challenging economic environment.

The packaging and speciality papers segmental year-on-year sales volumes were up 3%, constrained by an extended shut in South Africa during the quarter for a quality and product range upgrade to the containerboard machine at the Ngodwana Mill combined with low inventory levels in North America and South Africa following the strong sales earlier in the year. EBITDA for the segment grew by 37% compared to last year but was below the record of the prior quarter as the lower South African sales and escalating costs, particularly in Europe, eroded margins.

VSF and hardwood DP market prices dropped during the quarter responding to weaker demand in China related to Covid-19 lockdowns, which negatively impacted operating rates for VSF producers, and general concerns around global inflation and recessionary impacts on textile demand. Despite these challenges, the profitability of the pulp segment improved substantially year-on-year with a 61% rise in EBITDA due to increased sales volumes and pricing. Net sales pricing for DP benefited from the lag in contract pricing as the market price peaked in the third quarter and formed the basis of fourth quarter contract sales. Pulp sales volumes for the quarter of 378,000 tons were 44% higher than the prior year as a result of improved logistics, particularly for exports from South Africa, which were aided by the implementation of breakbulk shipping during the year.

Earnings per share excluding special items for the quarter was 44 US cents, which was a further improvement on the 39 US cents in the prior quarter and indicative of the record profitability for the group. Special items for the quarter reduced earnings by US$213 million, primarily due to the US$183 million write down to fair value and costs related to the held-for-sale European assets.

Despite the extraordinary tight market conditions in FY2022, the graphic paper markets are in long-term decline and indications are that demand in FY2023 will again be under pressure. A key element of our Thrive25 strategy is to reduce our exposure to declining graphic paper markets. Aligned to this objective, on 29 September 2022, Sappi signed an agreement with Aurelius Investment Lux One S.à.r.l. to divest the Maastricht Mill in the Netherlands, the Stockstadt Mill in Germany and the Kirkniemi Mill in Finland. The decision was taken following a detailed and thorough strategic review and will significantly reduce our exposure to graphic paper markets. The sale will be subject to various standard suspensive conditions and is anticipated to close in the second financial quarter of 2023. The enterprise value of the transaction amounts to approximately €272 million. The proceeds will be used to reduce debt further, which will provide a platform for future expansion in our identified growth market segments.

Cash flow and debt

Net cash generated for the year was US$506 million compared to US$29 million in the prior year. The noteworthy improvement in cash generation was largely due to substantially higher profitability despite a large investment in working capital of US$270 million related to inflationary increases for inventories and accounts receivables. Capital expenditure of US$368 million for the year was below expectations due to timing of certain payments and consequently approximately US$20 million will roll over into the 2023 financial year.

Our Thrive25 strategic objective to reset the balance sheet was largely achieved. Net debt at financial year-end decreased to US$1,163 million (FY2021 US$1,946 million) as a result of the substantial cash generation and a positive translation impact of a weaker EUR/US Dollar exchange rate on the predominantly Euro-denominated debt. This is the lowest net debt level in over 20 years. The covenant leverage ratio reduced substantially from 3.7 at the end of the prior year to 0.9.

We recognise that global macroeconomic volatility and uncertainty remain significant risks to our business and have therefore set a new long-term strategic objective to target net debt of approximately US$1 billion. This materially lower debt level will provide more flexibility to withstand market downturns and, combined with strong anticipated future cash generation, should provide sufficient opportunity to fund growth in our targeted market segments.

At year-end, liquidity comprised cash on hand of US$780 million and US$615 million from the committed unutilised revolving credit facilities (RCF) in South Africa and Europe.

Directorate

The following independent non-executive directors were appointed to the board. Mr Louis von Zeuner with effect from 1 September 2022 and Mr Nkululeko Sowazi and Ms Eleni Istavridis with effect from 3 October 2022.

Post balance sheet events

On 12 October 2022, a tender offer to purchase for cash a portion of the outstanding 3.125% Senior Notes due 2026 was concluded. As a result, US$206 million of the aggregate principal amount of the 2026 bonds in the tender offer was repurchased at a purchase price of 92.41% (plus accrued and unpaid interest). The transaction is fully aligned with the Thrive25 strategic objective to strengthen the balance sheet and yielded a gain of US$15 million net of the accelerated amortisation of upfront costs and will reduce gross annual interest payments by approximately US$6 million per annum.

Dividends

On 10 November 2022, the directors approved a dividend (number 89) of 15 US cents per share which will be paid to shareholders on 16 January 2023. This dividend was declared after year-end and was not included as a liability at the end of the 2022 financial year and will be funded from cash reserves.

The 2022 dividend is covered 9 times by basic earnings per share, excluding special items. The group aims to declare ongoing annual dividends.

Outlook

Macroeconomic uncertainty has increased considerably in recent weeks. Ongoing lockdowns in China, the geopolitical turmoil in Europe and unprecedented inflation are increasing the likelihood of a global recession in 2023. This poses a risk to our business as weakening consumer sentiment and diminishing discretionary spend will likely weaken demand in our graphic paper and dissolving pulp segments in upcoming quarters. Order activity in these segments has slowed and destocking is occurring across the value chain. The Covid-19 pandemic demonstrated that the underlying demand for packaging and speciality papers is more resilient in economic downturns, particularly for product categories in food, beverage and healthcare. Furthermore, the shift from plastic to paper offers significant opportunity to grow this segment.

Rising input costs remain a risk in the year ahead although the prices for some raw materials, specifically natural gas and pulp, have decreased in recent weeks. We remain focused on maximising our operational efficiency and will balance our production with demand to proactively manage our costs and preserve pricing.

In South Africa, a fire at a municipal electrical substation in KwaZulu-Natal impacted production at our three local mills for a few days in October 2022. In addition, a strike at Transnet[(2)] has negatively impacted DP supply chains once again and we anticipate that severe congestion at the Durban port may impact sales volumes in the first quarter. Sales volumes in North America will be impacted by the annual maintenance shut at Somerset Mill.

Demand for packaging and speciality papers in North America is particularly robust and our customers are actively seeking to increase their volumes with Sappi. The board has therefore approved a US$418 million investment at Somerset Mill to convert PM2 from coated woodfree graphic paper to solid bleached sulphate board (SBS). The machine capacity will also be increased during the conversion from 240,000 tons to 470,000 tons per annum. The project is expected to be completed in early 2025 and will be funded from free cash flow from operations taking into account our net debt target of approximately US$1 billion. The capital expenditure will be phased over three years with the majority of the spend taking place in FY2024 and FY2025. This investment is fully aligned with our Thrive25 strategic focus to reduce our exposure to declining graphic paper markets and transition our portfolio to packaging and speciality papers, pulp and biomaterials.

Capital expenditure in FY2023 is estimated to be US$430 million and includes approximately US$70 million for the Somerset PM2 conversion project, US$60 million for sustainability projects and US$20 million capex spill-over from FY2022.

Deleveraging of our balance sheet has been material and combined with substantial cash reserves we are well positioned to navigate any market downturn. We remain encouraged by the increasing resilience of our business and opportunities for growth in our packaging and speciality papers segment.

Notwithstanding the inflationary cost pressures and weakening demand in some product segments, we anticipate that the EBITDA for the first quarter of FY2023 will be above that of the equivalent quarter in FY2022.

(1) "year-on-year" or "prior year/last year" is a comparison between Q4 FY2022 versus Q4 FY2021; "Quarter-on-quarter" or "prior quarter" is a comparison between Q4 FY2022 and Q3 FY2022.
(2) Transnet is the state owned South African rail, port and pipeline company.

Dividend announcement

The directors have resolved to declare a gross cash dividend (number 89) of 15 US cents per share, payable in ZAR at an exchange rate (US$1=ZAR) of ZAR17.81877, being ZAR267.28155 cents per share, for the year ended September 2022 out of income, in respect of Sappi ordinary shares in issue on the record dates as detailed below.

The South African dividend tax (DT) rate is 20% and the net dividend payable to shareholders who are not exempt from DT is ZAR213.82524 cents per share. Sappi currently has 565,225,532 ordinary shares in issue. The income tax reference number is 9175203711.

In compliance with the JSE Listings Requirements the salient dates in respect of the dividend are detailed below.

Currency conversion determined on:	9 November 2022
Declaration and finalisation date:	10 November 2022
Last day to trade to qualify for the dividend:	10 January 2023
Shares commence trading ex-dividend:	11 January 2023
Record date:	13 January 2023
Payment date:	16 January 2023

Dividends payable to shareholders on the South African register will be paid in South African Rand and all dividends attributable to holders of ADR shares on the NYSE will be dealt with in accordance with their custody agreements in place with their local custodian.

Certificated shareholders who previously held their shares on the UK register, which has subsequently been discontinued, shall be paid in Pounds Sterling at the ruling exchange rate at the time.

No currency elections are permitted.

All shareholders need to ensure that their current bank mandates with their service providers are up to date. Furthermore, shareholders who have not yet done so, should submit their service providers with their tax numbers and other relevant information for dividend tax purposes. Where shareholders qualify for withholding tax exemptions, they need to ensure that such exemption applications have been lodged with their service providers.

Certificated and own name shareholders can call Computershare in South Africa on 0861 100 950 for assistance in this regard.

Share certificates will not be dematerialised or rematerialised from 11 January 2023 to 13 January 2023, both days inclusive.

On behalf of the board

SR Binnie
Director

GT Pearce
Director

10 November 2022

Short form announcement

This short-form announcement is the responsibility of the directors. It is only a summary of the information in the full announcement and does not contain full or complete details. Any investment decision should be based on the full announcement accessible from 10 November 2022 via the JSE link and also available on the home page of the Sappi website at www.sappi.com.

Copies of the full announcement may be requested by contacting Rosa Moodley on telephone: +27 (0)11 407 8515, email: Rosa.Moodley@sappi.com.

The JSE link is as follows:
https://senspdf.jse.co.za/documents/2022/JSE/ISSE/SAVVI/sappiQ422.pdf

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