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

Second quarter results for the period ended March 2023

Short-form SENS announcement

	Quarter ended			Half-year ended		
US$ million	**Mar 2023**	**Mar 2022**	% Change	**Mar 2023**	**Mar 2022**	% Change
Sales	1 442	1 858	-22%	3 102	3 555	-13%
EBITDA excluding special items	167	337	-50%	457	577	-21%
Profit for the period	69	188	-63%	259	311	-17%
Net debt	1 225	1 793	-32%	1 225	1 793	-32%
Headline EPS (US Cents)	12	36	-67%	46	58	-21%
Basic EPS (US Cents)	12	33	-64%	46	55	-16%
EPS excluding special items (US Cents)	11	35	-69%	41	55	-25%
Net asset value (US Cents)	447	417	7%	447	417	7%

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 (packaging papers, speciality 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 for the quarter (1)

Sappi delivered an EBITDA excluding special items of US$167 million against a backdrop of a challenging global economy and significantly weaker paper and pulp markets. Following the record profitability achieved last year, the group faced a severe downstream inventory destocking cycle. This led to production curtailment in both the European and North American regions to match the sluggish market demand and to prevent excess inventory accumulation. Profitability was negatively affected by reduced sales volumes, cost inflation and operational inefficiencies associated with the commercial downtime.

However, paper selling prices remained relatively stable through the quarter and were significantly above the levels in the prior year.

Graphic paper markets were weaker, with demand across all product categories lower due to the ongoing industry-wide destocking cycle and negative consumer sentiment related to a slowing global economy. Additionally, the packaging and speciality business faced significant headwinds from elevated downstream inventories. In South Africa, production difficulties at the Ngodwana Mill following heavy rains and challenges associated with the recent upgrade of the containerboard machine, further impacted supply. As a result of these difficult conditions, sales volumes for graphic papers and packaging and speciality papers were 42% and 29% below the prior year, respectively.

Dissolving pulp (DP) market conditions improved during the quarter. Downstream inventories in the textile value chain dropped from the peaks of last year and clothing retail sales were better than expected. Viscose staple fibre (VSF) operating rates in China improved through the quarter with renewed economic activity following the Lunar New Year celebrations in January 2023 and the opening of the economy following the relaxation of COVID-19 pandemic restrictions. The hardwood DP market price responded positively to the improved sentiment and increased to US$920 per ton from a low of US$883 per ton in January. Sales volumes for the pulp segment were 7% below the prior year primarily due to the reduced demand at the beginning of the quarter and a swing to more paper pulp production at the Cloquet Mill. Lower net selling prices and higher input costs relative to the prior year depressed margins for the segment.

Earnings per share excluding special items for the quarter was 11 US cents, a decrease from the 35 US cents in the prior year. Special items increased earnings by US$7 million due to a positive plantation fair value adjustment of US$12 million offset by insurance-related adjustments in South Africa.

Shareholders are referred to the announcement released on the Stock Exchange News Service on 14 April 2023 wherein it was advised that the date for completion of the suspensive conditions contained in the agreement to sell three European graphic paper mills to Aurelius has lapsed and therefore the transaction will not proceed. Reducing exposure to graphic paper markets remains a strategic imperative and Sappi will explore all options for these assets. Collectively these graphic paper mills contribute positively to EBITDA and in the interim, continue to be held-for-sale.

(1) "year-on-year" or "prior/previous year" is a comparison between Q2 FY2023 versus Q2 FY2022; "Quarter-on-quarter" or "prior/previous quarter" is a comparison between Q2 FY2023 and Q1 FY2023

CASH FLOW AND DEBT

Net cash generated for the quarter of US$38 million was lower than the US$105 million generated during the prior year. This was due to lower profitability and the dividend payment of US$85 million, partially offset by a US$99 million inflow of working capital related to the lower operating activities. Capital expenditure for the quarter of US$83 million was higher than the previous year due to the commencement of the Somerset PM2 conversion and expansion project.

Our long-term net debt target of approximately US$1 billion remains a strategic imperative and we continued to progress towards this goal. Net debt decreased by US$568 million compared to the prior year and ended the quarter at US$1,225 million. A stronger Euro/US Dollar exchange rate resulted in Euro-denominated debt being converted at a higher rate and increased net debt by US$112 million for the six months to March 2023. Net debt/EBITDA improved materially to 1.0 from 2.0 in the prior year. Our liquidity position included US$557 million in cash on hand and US$670 million from committed but unutilised revolving credit facilities (RCF) in South Africa and Europe.

Office paper and newsprint sales volumes were in line with the prior year and significantly improved pricing helped to offset variable cost pressures.

Variable costs were 20% higher than the prior year primarily due to higher wood, energy and chemical costs. Ongoing poor rail service levels necessitated increased road transport to ensure reliable timber and raw material deliveries to the mills. However, reduced ocean freight rates and bunker fuel charges provided some relief during the quarter. Fixed costs were well managed with a below-inflation year-on-year increase due to savings in personnel and maintenance expenditures.

POST-BALANCE SHEET EVENTS

At the AGM held on 3 February 2023, special resolution number 1 was passed granting general authority for the repurchase of shares (not exceeding 10% of the number of Sappi shares in issue). As at 3 May 2023, the group repurchased 9,256,685 shares at an average price of ZAR43.21 per share for a combined value of US$23 million (ZAR400 million), representing 1.62% of Sappi shares in issue. The repurchased Sappi shares were cancelled and reverted to authorised share capital.

OUTLOOK

VSF and DP markets are recovering and demand from our major customers is healthy. The short-term DP supply/demand landscape is expected to remain relatively balanced. However, the DP market price remains range-bound at current levels by stagnant textile fibre pricing, which would need to increase to support further DP pricing gains. A planned maintenance shut at Saiccor as well as lower contract pricing for certain customers will impact margins and profitability for the pulp segment in the third quarter.

High levels of downstream inventory are obscuring our short-term visibility of underlying paper demand and market conditions are anticipated to remain weak until the destocking cycle is complete. Global logistics challenges are mostly resolved and destocking may take longer than expected if customers delay replenishing their supply chains and drive down inventories below historical levels in anticipation of pricing adjustments.

We will continue to diligently manage working capital through production curtailments and adapt our product and market mix to match demand. Some relief may be expected from lower input costs as many variable cost categories have passed their pricing peak and we anticipate input cost benefits to be realised in the coming quarters.

Capital expenditure is estimated to be US$410 million for FY2023 and includes US$70 million for the Somerset PM2 conversion and expansion project.

The third quarter is seasonally the weakest in terms of demand for our products. Given that global macroeconomic uncertainties continue to weigh on consumer sentiment and paper markets have yet to show signs of a sustained recovery in demand, we anticipate that EBITDA for the third quarter of FY2023 will be below that of the second quarter.

Sappi is well positioned to withstand the current market pressures given our significantly reduced debt profile and healthy cash reserves. We remain committed to our strategy to reduce exposure to graphic paper markets while investing for growth in renewable packaging, dissolving pulp and biomaterials.

On behalf of the board

SR Binnie
Director

GT Pearce
Director

11 May 2023

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 11 May 2023 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/2023/jse/isse/SAVVI/sappiQ223.pdf

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