

CREDIT OPINION

29 June 2023

Update

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RATINGS

Essity Aktiebolag

Domicile	Sweden
Long Term Rating	Baa1
Type	LT Issuer Rating - Fgn Curr
Outlook	Stable

Please see the [ratings section](#) at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Essity Aktiebolag

Update to credit analysis

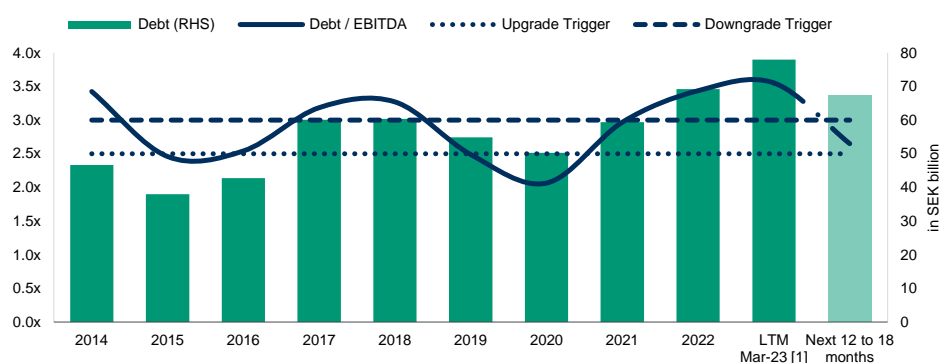
Summary

[Essity Aktiebolag's](#) Baa1/P-2 ratings with a stable outlook primarily reflect the company's large scale, with revenue of SEK165 billion for the 12 months that ended March 2023 (around \$15.9 billion), and a broad product portfolio; its leading market positions, with well-recognised brands and a good track record of innovation; its global footprint, with the faster-growing emerging markets representing around one-third of its revenue; the fairly good underlying growth and the stable demand for its products; its financial policies, which are aimed at protecting its solid investment-grade rating; and Essity's track record of generating significant positive free cash flow (FCF), which it tends to use for tuck-in acquisitions and can be used to reduce leverage, if needed.

Essity's ratings are primarily constrained by its exposure to volatile input costs, pulp in particular, which can be passed through only with a significant delay; its somewhat below-average profitability compared with that of most of its peers we rate similarly, such as [Kimberly-Clark Corporation](#) (K-C, A2 stable) and [The Procter & Gamble Company](#) (P&G, Aa3 stable), with a Moody's-adjusted EBITA margin of 9.0% for the 12 months that ended March 2023; and a certain degree of debt-funded M&A risk, which, however, falls within the company's commitment to maintaining a solid investment-grade rating (see Exhibit 1).

Exhibit 1

We expect Essity's leverage to move back into the range expected for the Baa1 rating category during 2023



All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

The forward view represents Moody's view and does not incorporate any material divestments and acquisitions.

[1] Due to less detailed disclosures in the quarterly reporting leverage shown for the 12 months that ended March 2023 is higher than it would be with full information available. Moody's estimates actual Moody's-adjusted leverage to be 3.3x debt/EBITDA when excluding derivative liabilities for the 12 months that ended March 2023.

Source: Moody's Financial Metrics™

Credit strengths

- » A strong business profile, with a broad portfolio of well-positioned global (Tork and Tena) and regional brands
- » Fairly good underlying growth and stable demand for most of its products
- » A financial policy that is aimed at protecting its solid investment-grade rating

Credit challenges

- » Exposure to volatile input costs, such as pulp and recycled paper
- » Ongoing need for innovation in the Consumer Goods and Health and Medical businesses to preserve pricing levels
- » Event risks, such as debt-funded M&A or shareholder-friendly actions

Rating outlook

The stable rating outlook reflects our expectation that Essity's strong market position will enable the company to pass on the rising input costs to its customers and manage cost, and, thus, strengthen credit metrics back into the range we expect for the Baa1 rating category.

Factors that could lead to an upgrade

- » EBIT margin consistently above 12% in the company's business areas
- » Retained cash flow/net debt above 25%
- » Debt/EBITDA well below 2.5x
- » Continued positive FCF, which is applied towards debt reduction

Factors that could lead to a downgrade

- » EBIT margin remaining below 9%
- » Retained cash flow/net debt below 20% on a sustained basis
- » Inability to reduce leverage below 3.0x debt/EBITDA
- » FCF turning negative
- » Erosion of the company's solid liquidity

This publication does not announce a credit rating action. For any credit ratings referenced in this publication, please see the issuer/deal page on <https://ratings.moody's.com> for the most updated credit rating action information and rating history.

Key indicators

Exhibit 2

Essity Aktiebolag [1][2]

	Dec-18	Dec-19	Dec-20	Dec-21	Dec-22	LTM Mar-23	Next 12-18 months [3]
Revenue (SEK billion)	118.5	129.0	121.8	121.9	156.2	164.8	170 - 175
Revenue (USD billion)	\$13.6	\$13.7	\$13.3	\$14.2	\$15.5	\$15.9	\$16 - \$17
EBIT Margin %	9.7%	11.4%	13.7%	10.4%	7.5%	8.3%	9.0% - 11.5%
EBITA Margin %	10.6%	12.2%	14.7%	11.3%	8.4%	9.0%	10.0% - 12.5%
Debt / EBITDA	3.3x	2.5x	2.1x	3.0x	3.4x	3.6x [4]	2.5x - 2.8x
RCF / Net Debt	20.0%	22.0%	29.6%	19.4%	16.0%	23.8% [5]	20% - 25%
FCF / Debt	3.0%	14.9%	10.9%	1.9%	-0.6%	5.5% [6]	5% - 8%
EBITA / Interest Expense	8.8x	10.2x	15.2x	15.4x	8.6x	7.5x	7.0x - 10.0x

[1] All figures and ratios are calculated using Moody's estimates and standard adjustments.

[2] Periods are financial year-end unless indicated. LTM = Last 12 months.

[3] This represents Moody's forward view, not the view of the issuer, and unless noted in the text, does not incorporate significant acquisitions and divestitures.

[4] Moody's estimates actual Moody's-adjusted leverage to be 3.3x debt/EBITDA when excluding derivative liabilities for the 12 months that ended March 2023.

[5] 16.6% adjusted for dividend payment in April 2023.

[6] -1.0% adjusted for dividend payment in April 2023.

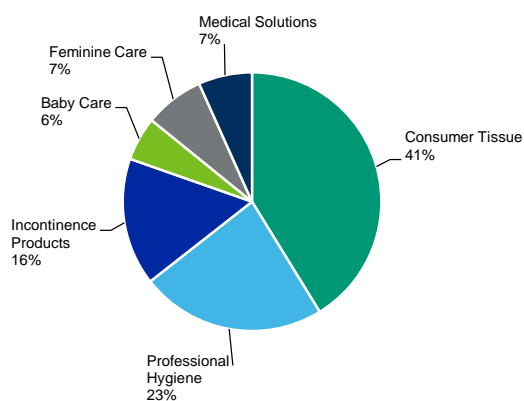
Sources: Moody's Financial Metrics™ and Moody's Investors Service estimate

Profile

Headquartered in Stockholm, Sweden, Essity Aktiebolag is one of the leading global hygiene and health companies, with sales of SEK165 billion for the 12 months that ended March 2023 (around \$15.9 billion). The company develops, produces and sells a wide range of products, including incontinence products, baby diapers, feminine care products, consumer tissue, away-from-home tissue, and products for wound care, compression therapy and orthopaedics. With a workforce of around 48,000 employees, Essity operates in about 150 countries worldwide under a number of well-recognised brands. Essity was formed in 2016 and spun off in June 2017 from Svenska Cellulosa Aktiebolaget. The company is listed on the Stockholm Stock Exchange, with a market capitalisation of around SEK199 billion as of 12 June 2023.

Exhibit 3

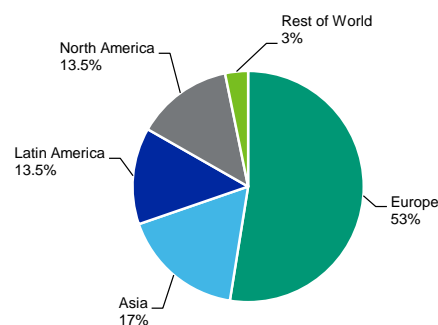
Revenue split by product For full-year 2022



Source: Essity Annual Report 2022

Exhibit 4

Revenue split by geography For full-year 2022



Source: Essity Annual Report 2022

Detailed credit considerations

Wide product portfolio, with a number of leading positions globally

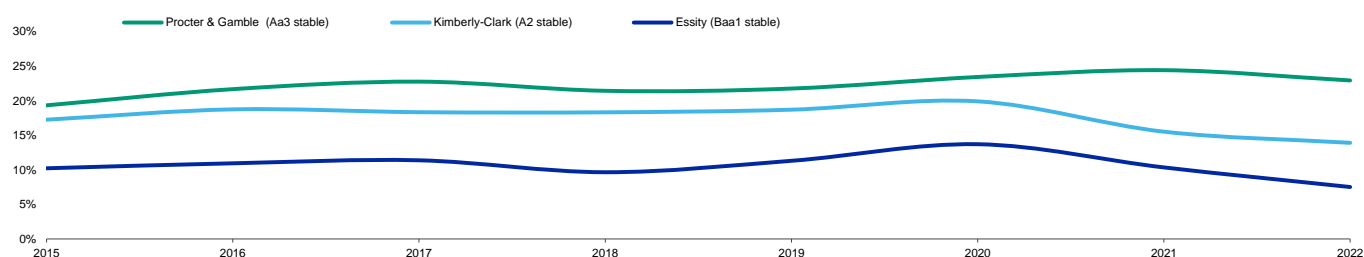
Essity's Baa1/P-2 ratings reflect the company's strong market position as one of the leading global hygiene and health companies, active in around 150 countries, with sales of SEK165 billion. Among others, the company is the global leader in incontinence products under the Tena brand and in professional hygiene under the Tork brand. In addition, the company has strong brands and market positions within the markets for baby diapers, feminine care and consumer tissue, as well as regional and global brands. Essity also has leading market positions in wound care, compression therapy and orthopaedics, with brands such as Jobst and Leukoplast. Overall, the company holds the first or second position within at least one product segment in around 90 countries.

The Consumer Goods and Health and Medical businesses are fairly competitive and subject to periods of temporary oversupply, which require producers to continuously focus on innovation to protect brand strength and optimise costs. In the tissue business, which is generally more competitive and less profitable, Essity competes primarily with [Georgia-Pacific LLC](#) (A3 stable), Hengan International Group Company Limited, K-C and Sofidel S.p.A. In the Health and Medical business, Essity's key competitors are K-C, P&G and Unicharm Corporation. In 2017, following the debt-funded acquisition of BSN Medical for €2.7 billion, the company entered the market for low-technology medical devices, such as wound care and compression therapy, which benefits from robust and stable demand and above-average profitability.

We expect Essity to focus on growing its Health and Medical product offerings while further increasing the efficiency of its tissue operations. In this context, Essity acquired additional shares in Asaleo Care Ltd. and Productos Familia S.A. during 2021, for a total cash consideration of around SEK9.4 billion, which was partially debt funded. In 2022 the company completed the acquisition of an 80% stake in Knix Wear Inc., a Canadian provider of leakproof apparel for menstrual periods and incontinence, for a total cash consideration of SEK3.3 billion (\$313 million), along with the acquisition of Modibodi, a leading leakproof apparel company in Australia, New Zealand and the UK, for a cash consideration of SEK985 million (\$93 million), making Essity the global market leader in leakproof apparel. This strategy will help narrow the profitability gap with the company's more profitable competitors, especially K-C and P&G, which benefit from a higher share of the more profitable personal care business and the generally more profitable US market.

Exhibit 5

Essity's margins have been lower than those of its main competitors Moody's-adjusted EBIT margin



All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Source: Moody's Financial Metrics™

Good underlying demand growth, especially in emerging markets

Essity benefits from the underlying growth in demand for its products, supported by megatrends such as population growth and higher disposable income, as well as the increased prevalence of people with chronic diseases. While mature markets continue to record modest annual growth in the low-single-digit percentages, the growth potential in emerging markets is substantial, and we estimate that the annual growth in these markets will be in the high-single-digit percentages. This is because the per capita consumption of Consumer Goods and Health and Medical products in emerging markets is significantly lower while living standards are rapidly improving.

To benefit from this development, Essity focused on growing its presence in emerging markets over the past decade. This was done both organically and through M&A, most notably through the acquisition of a majority stake in the Asian hygiene company Vinda

International Holdings Ltd (Vinda) — based in Hong Kong SAR, China — in 2013, along with the recent stake increase in Asaleo Care and Familia. In 2022, emerging markets represented 37% of Essity's net sales, and we expect this share to increase further.

In April 2023, Essity announced its decision to initiate a strategic review of the company's majority ownership of Vinda and of the Consumer Tissue Private Label Europe business with the aim of reducing the Consumer Tissue's share of the company's total sales. The strategic review includes exploring different options and may result in divestments, although no such decisions have yet been taken. The potential disposal will marginally weaken Essity's strong business profile initially because it will reduce its geographic diversification. However, the ultimate effect on Essity's credit profile depends on management's decision regarding the allocation of the divestment proceeds, which we estimate could reach up to around SEK25 billion. A potential disposal could be beneficial to Essity's business profile in a scenario where the proceeds from the divestment were deployed towards value-accretive investments and acquisitions in the higher-margin Health and Medical and Professional Hygiene business segments, which would potentially indicate further diversification in Essity's product portfolio.

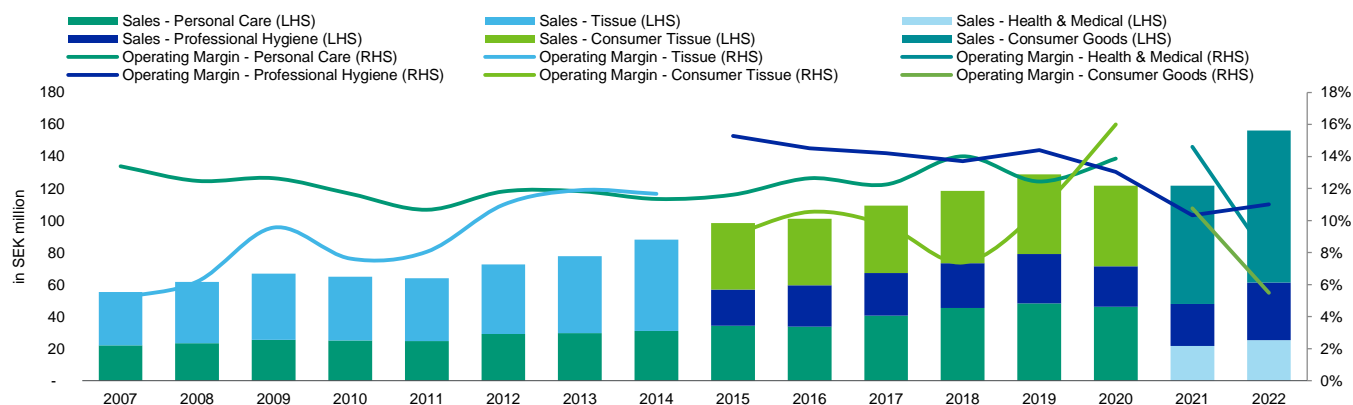
Profitability exposed to volatile input costs

The demand for Essity's products has historically been fairly stable through the cycle. Even during the 2008-09 global economic downturn, which was unprecedented in its magnitude, the company hardly faced any decline in organic sales, and the margins for both the Consumer Goods and Health and Medical businesses, the latter one in particular, remained robust. The continued increase in demand for tissue products indicates an ongoing megatrend towards the increasing use of hygiene products, although it was temporarily normalised during H1 2021 when revenue in the former consumer tissue (currently included in Consumer Goods) segment declined by 9% compared with H1 2020, driven by lower prices and the fact that consumers were stockpiling tissue products during the outbreak of the coronavirus in Q1 2020.

Profitability for both the Consumer Goods and Health and Medical businesses has been fairly stable over the last decade, which also indicates Essity's ability to manage its key input costs. Some of the input costs, such as pulp (38% of total raw materials and consumables, and 17% of total operating expenses at the group level in 2022) and recovered paper (9% of total raw materials and consumables, and around 4% of total operating expenses), have fairly high volatility, and price increases can be typically passed on to customers only with delays of up to one year. Even in an environment of substantially increasing pulp prices in 2017 and H1 2018, the company delivered a fairly robust performance, with less volatility than that of its key tissue peers in Europe. In 2022, profit margins were hurt by higher costs for raw materials, energy and distribution, partly offset by higher volumes and selling prices, leading to a Moody's-adjusted EBITA margin of 8.4% compared with 11.3% in 2021. In Q1 2023, higher selling prices and a better mix in all business areas offset higher costs for raw materials, energy and distribution along with salary inflation, leading to a Moody's-adjusted EBITA margin of 9% for the 12 months that ended March 2023.

Exhibit 6

Essity has had fairly stable demand patterns and profitability through the cycle



Data as reported by the company (that is, without our adjustments).

Sources: Essity financial reports and former Svenska Cellulosa Aktiebolaget segmental reporting

M&A risk, but within the limits of Essity's financial policies, which target a solid investment-grade rating

Essity's financial policies are centred around its commitment to retain a solid investment-grade rating, which drives its capital allocation priorities, including dividend payouts, as well as M&A. Although the company will continue to complement organic growth with M&A in the next couple of years, especially in the low-technology medical devices market, which is still relatively fragmented, at this point, there is no capacity for debt-funded growth.

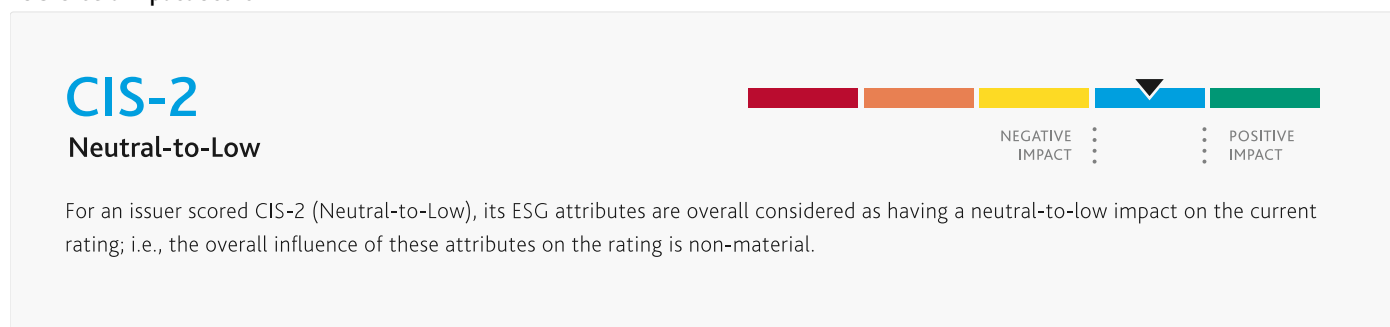
While Essity's leverage currently exceeds the upper end of the 2.0x-3.0x range set for the Baa1 rating category, we consider the company is solidly positioned in its rating category. Essity will be willing and able to operate with leverage below 3.0x through the cycle, supported by both EBITDA growth, as the company continues to pass through increasing input costs to its customers, and actual debt repayments. Taking into consideration Essity's capital spending of 5% of sales and dividends typically of around 50% of net income, we expect the company to continue to generate positive FCF, in the high-single-digit percentages of Moody's-adjusted gross debt, which could be potentially used for debt repayments. We will assess further smaller acquisitions within the limits of the company's FCF on a case-by-case basis.

ESG considerations

Essity Aktiebolag's ESG Credit Impact Score is Neutral-to-Low CIS-2

Exhibit 7

ESG Credit Impact Score



Source: Moody's Investors Service

Essity's CIS-2 indicates that ESG considerations are not material to the rating primarily due to a conservative financial policy, aimed at protecting its solid investment-grade rating.

Exhibit 8

ESG Issuer Profile Scores



Source: Moody's Investors Service

Environmental

Essity's E-3 reflects the company's exposure to natural capital and waste and pollution risks. Natural capital risk reflects the use of pulp in the production process in line with industry peers. Essity's exposure to waste & pollution stems from the release of air pollutants and hazardous waste.

Social

Essity's S-3 IPS mirrors the industry-wide exposure to risks related to health & safety, responsible production and demographic and societal trends. The company's risk related to customer relations is low given that the majority of revenue is generated with retail chains. Also, sourcing of employees is not considered to be an issue for Essity.

Governance

Essity's G-2 balances risk related to board structure and policies given it has A and B shares with different voting rights and a concentrated ownership against a conservative financial policy, aimed at protecting its solid investment-grade rating.

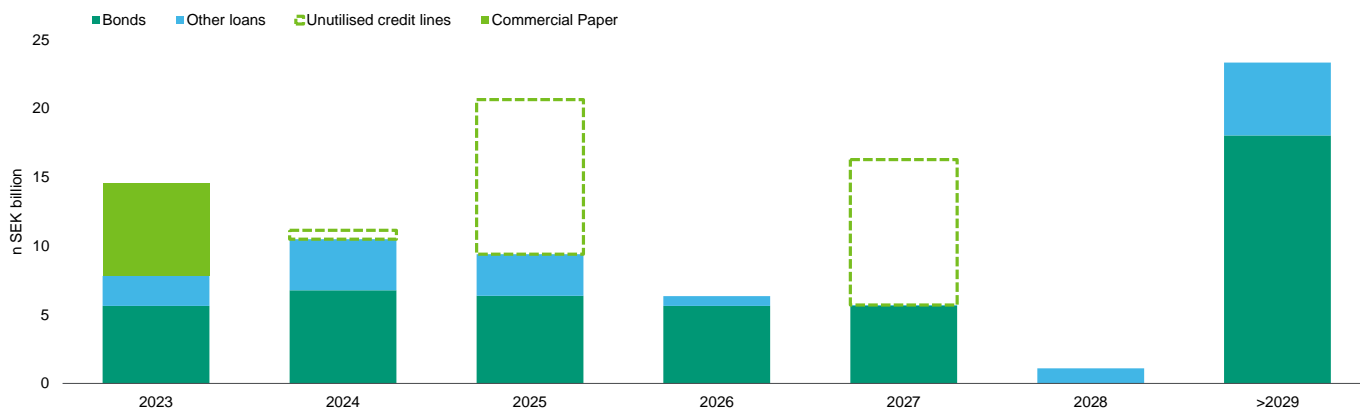
ESG Issuer Profile Scores and Credit Impact Scores for the rated entity/transaction are available on Moody's.com. In order to view the latest scores, please click [here](#) to go to the landing page for the entity/transaction on MDC and view the ESG Scores section.

Liquidity analysis

Essity's liquidity is good, primarily based on our expectation that the company will continue to generate significant positive FCF over the next four to six quarters. As of the end of March 2023, the company reported around SEK8.9 billion of cash and cash equivalents, around one-third of those in countries with currency restrictions. In addition, the company had access to various largely undrawn credit facilities, totalling roughly SEK22.6 billion, consisting primarily of two syndicated facilities, each of around €1.0 billion, maturing in 2025 and 2027, respectively. In May 2023 the facility maturing in 2025 has been refinanced with a new facility maturing in 2028 with two extension options of one year, each (5+1+1). The facilities are of high quality, without significant adverse change clauses and other conditionality language, and have also served as backstop facilities for the company's commercial paper programme, which has been a central source of Essity's short-term funding needs. As of the end of March 2023, the company reported around SEK14.6 billion in short-term debt, which includes SEK6.7 billion under Essity's commercial paper programme. The company's maturity profile is generally well spread, with an average maturity of around 4.3 years.

Exhibit 9

Essity's debt maturity profile is generally well spread As of 31 March 2023



Source: Essity reporting

Methodology and scorecard

The principal methodology used for assessing Essity is our [Consumer Packaged Goods](#) rating methodology, published in June 2022. The scorecard-indicated outcome was Baa1 for both the 12 months that ended March 2023 and our forward view, in line with the actual rating assigned.

Exhibit 10

Rating factors

Essity Aktiebolag

Consumer Packaged Goods Industry Scorecard [1][2]			Current LTM 3/31/2023		Moody's 12-18 Month Forward View As of 6/20/2023 [3]	
Factor	Measure	Score	Measure	Score	Measure	Score
Factor 1 : Scale (20%)						
a) Revenue (USD Billion)	\$15.9	A	\$16 - \$17	A		
Factor 2 : Business Profile (30%)						
a) Geographic Diversification	A	A	A	A		
b) Segmental Diversification	Baa	Baa	Baa	Baa		
c) Market Position	A	A	A	A		
d) Category Assessment	A	A	A	A		
Factor 3 : Profitability (10%)						
a) EBITA Margin	9.0%	Caa	10% - 12.5%	B		
Factor 4 : Leverage and Coverage (25%)						
a) Debt / EBITDA [4]	3.6x	Ba	2.5x - 2.8x	Baa		
b) RCF / Net Debt	23.8%	Baa	20% - 25%	Baa		
c) EBITA / Interest Expense	7.5x	Baa	7x - 10x	A		
Factor 5 : Financial Policy (15%)						
a) Financial Policy	A	A	A	A		
Rating:						
a) Scorecard-Indicated Outcome		Baa1		Baa1		
b) Actual Rating Assigned						Baa1

[1] All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

[2] As of LTM 3/31/2023.

[3] This represents Moody's forward view, not the view of the issuer, and does not incorporate significant acquisitions and divestitures.

[4] Moody's estimates actual Moody's-adjusted leverage to be 3.3x debt/EBITDA when excluding derivative liabilities for the 12 months that ended March 2023.

Source: Moody's Financial Metrics™

Ratings

Exhibit 11

Category	Moody's Rating
ESSITY AKTIEBOLAG	
Outlook	Stable
Issuer Rating	Baa1
Senior Unsecured	Baa1
ST Issuer Rating	P-2
ESSITY CAPITAL B.V.	
Outlook	Stable
Bkd Senior Unsecured -Dom Curr	Baa1

Source: Moody's Investors Service

Appendix

Exhibit 12

Peer comparison

(in USD million)	Essity Aktiebolag			Procter & Gamble Company (The)			Kimberly-Clark Corporation		
	Baa1 Stable			Aa3 Stable			A2 Stable		
	FYE Dec-21	FYE Dec-22	LTM Mar-23	FYE Jun-21	FYE Jun-22	LTM Mar-23	FYE Dec-21	FYE Dec-22	LTM Mar-23
Revenue	14,213	15,503	15,896	76,118	80,187	80,968	19,440	20,175	20,275
EBITDA	2,333	1,999	2,117	21,536	21,394	21,274	3,925	3,690	3,797
Total Debt	6,560	6,644	7,517	40,469	37,379	42,477	9,190	9,304	9,315
Cash & Cash Equivalents	277	186	632	10,288	7,214	7,596	270	427	524
EBIT margin %	10.4%	7.5%	8.3%	24.4%	22.9%	22.7%	15.5%	13.9%	14.4%
EBIT / Interest Expense	14.1x	7.6x	6.9x	29.1x	30.8x	22.7x	11.0x	9.3x	9.4x
Debt / EBITDA	3.0x	3.4x	3.6x	1.9x	1.7x	2.0x	2.3x	2.5x	2.5x
RCF / Net Debt	19.4%	16.0%	23.8%	32.5%	30.1%	24.0%	13.7%	13.7%	15.0%
FFO / Debt	27.6%	23.2%	22.3%	44.7%	47.7%	40.9%	30.2%	30.9%	32.2%

All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Source: Moody's Financial Metrics™

Exhibit 13

Reconciliation of debt

Essity Aktiebolag

(in SEK million)	FYE Dec-18	FYE Dec-19	FYE Dec-20	FYE Dec-21	FYE Dec-22	LTM Mar-23
As Reported Total Debt	53,742	51,227	46,096	56,895	66,592	75,319
Pensions	3,830	4,133	4,207	2,500	2,631	2,631
Leases	3,334	0	0	0	0	0
Non-Standard Adjustments	(570)	(461)	0	0	0	0
Moody's Adjusted Total Debt	60,336	54,899	50,303	59,395	69,223	77,950

Source: Moody's Financial Metrics™

Exhibit 14

Reconciliation of EBITDA

Essity Aktiebolag

(in SEK million)	FYE Dec-18	FYE Dec-19	FYE Dec-20	FYE Dec-21	FYE Dec-22	LTM Mar-23
As Reported EBITDA	17,500	21,941	24,517	20,689	20,182	21,989
Pensions	10	21	(155)	24	(41)	(41)
Leases	980	0	0	0	0	0
Unusual Items - Income Statement	20	160	0	(706)	0	(7)
Moody's Adjusted EBITDA	18,510	22,122	24,362	20,007	20,141	21,948

We define EBITDA as pretax income + gross interest expense + depreciation and amortisation.

Source: Moody's Financial Metrics™

Exhibit 15

Overview of key metrics

Essity Aktiebolag

(in SEK million)	FYE Dec-18	FYE Dec-19	FYE Dec-20	FYE Dec-21	FYE Dec-22	LTM Mar-23
INCOME STATEMENT						
Revenue	118,500	128,975	121,752	121,867	156,173	164,798
EBITDA	18,510	22,122	24,362	20,007	20,141	21,948
EBITA	12,554	15,756	17,885	13,792	13,160	14,810
EBIT	11,505	14,645	16,691	12,616	11,734	13,611
Interest Expense	1,424	1,540	1,179	896	1,537	1,980
BALANCE SHEET						
Cash & Cash Equivalents	1,866	2,236	3,699	2,508	1,937	6,553
Total Debt	60,336	54,899	50,303	59,395	69,223	77,950
Net Debt	58,470	52,663	46,604	56,887	67,286	71,397
CASH FLOW						
Funds from Operations (FFO)	16,148	15,937	18,617	16,365	16,082	17,372
Cash Flow From Operations (CFO)	13,966	19,312	17,800	14,616	12,874	12,891
Dividends	4,435	4,374	4,813	5,312	5,312	396
Retained Cash Flow (RCF)	11,713	11,563	13,804	11,053	10,770	16,976
RCF / Net Debt	20.0%	22.0%	29.6%	19.4%	16.0%	23.8%
Free Cash Flow (FCF)	1,819	8,192	5,483	1,102	(391)	4,286
FCF / Debt	3.0%	14.9%	10.9%	1.9%	-0.6%	5.5%
PROFITABILITY						
% Change in Sales (YoY)	8.5%	8.8%	-5.6%	0.1%	28.2%	28.1%
EBIT margin %	9.7%	11.4%	13.7%	10.4%	7.5%	8.3%
EBITA margin %	10.6%	12.2%	14.7%	11.3%	8.4%	9.0%
EBITDA margin %	15.6%	17.2%	20.0%	16.4%	12.9%	13.3%
INTEREST COVERAGE						
EBIT / Interest Expense	8.1x	9.5x	14.2x	14.1x	7.6x	6.9x
EBITDA / Interest Expense	13.0x	14.4x	20.7x	22.3x	13.1x	11.1x
(EBITDA - CAPEX) / Interest Expense	7.6x	10.0x	14.3x	13.2x	7.9x	6.9x
LEVERAGE						
Debt / EBITDA	3.3x	2.5x	2.1x	3.0x	3.4x	3.6x
Debt / (EBITDA - CAPEX)	5.6x	3.6x	3.0x	5.0x	5.7x	5.7x
Net Debt / EBITDA	3.2x	2.4x	1.9x	2.8x	3.3x	3.3x

All ratios are based on adjusted financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.

Source: Moody's Financial Metrics™

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REPORT NUMBER 1368536