

Sappi Limited

Registration number: 1936/008963/06

JSE code: SAP

ISIN code: ZAE000006284

Issuer code: SAVVI

Third quarter results for the period ended June 2020

Short-form SENS announcement

US\$ million	Quarter ended			Nine months ended		
	Jun 2020	Jun 2019	%	Jun 2020	Jun 2019	%
Sales	907	1,371	-34%	3,517	4,292	-18%
EBITDA excluding special items	26	118	-78%	296	502	-41%
Profit (loss) for the period	(73)	8	-1013%	(47)	161	-129%
Net debt	1,977	1,728	14%	1,977	1,728	14%
Headline EPS (US Cents)	(12)	2	-700%	(6)	31	-119%
Basic EPS (US Cents)	(13)	1	-1400%	(9)	30	-130%
EPS excluding special items (US Cents)	(10)	4	-350%	(1)	33	-103%
Net asset value (US Cents)	326	375	-13%	326	375	-13%

Sappi is a global diversified woodfibre company focused on providing dissolving pulp, packaging and speciality papers, graphic papers as well as biomaterials and biochemicals to our direct and indirect customer base across more than 150 countries.

Our dissolving pulp products are used worldwide mainly by converters to create viscose fibre for fashionable clothing and textiles, as well as other consumer products; quality packaging and speciality papers are used in the manufacture of such products as soup sachets, luxury carry bags, cosmetic and confectionery packaging, boxes for agricultural products for export, tissue wadding for household tissue products and casting release papers used by suppliers to the fashion, textiles, automobile and household industries; our market-leading range of graphic papers are used by printers in the production of books, brochures, magazines, catalogues, direct mail and many other print applications; biomaterials include nanocellulose, fibre composites and lignosulphonate; biochemicals include second generation sugars.

The wood and pulp needed for our products are either produced within Sappi or bought from accredited suppliers. Sappi sells almost as much as it buys.

Commentary for the quarter

The overall economic effect of the Covid-19 pandemic and related lockdowns, changes in consumer behaviour and logistical challenges, had a severe impact on the business in the quarter. Previously weak graphic paper and dissolving pulp (DP) markets were further affected by significant declines in demand and lower sales prices. DP and graphic paper sales

volumes were 29% and 40% lower respectively. In response, a number of cost containment initiatives were implemented which, along with a positive currency movement, resulted in fixed costs being US\$67 million less than the equivalent quarter last year. Consequently, the group generated EBITDA excluding special items of US\$26 million compared to US\$118 million in the equivalent quarter last year, which led to a decline in profitability and a loss of US\$73 million for the quarter.

We developed a comprehensive Covid-19 action plan, where our priority remains the safety of our people. Our mills and other operations apply stringent guidelines to mitigate the spread of Covid-19. This ensured that we continued to operate in a safe and uninterrupted manner where demand for our products permitted. The group's focus on the preservation of liquidity and cash flow resulted in a number of steps that were taken during the quarter. These included the cost containment initiatives mentioned above, a reduction in capital expenditure, delays to major annual maintenance shuts, furloughing of staff where possible and a focus on optimising working capital.

The growth of the packaging and specialities business continued, with sales volumes increasing by 11%, and combined with lower input costs and delayed annual maintenance shuts at Ngodwana and Tugela, offset some lower selling prices. As a consequence, profitability in the segment more than doubled. This business has proven resilient in difficult economic circumstances and supports our strategy to diversify the product portfolio into higher margin and growing segments.

The lockdowns and the corresponding economic slowdown had a serious impact on graphic paper demand. Many companies including retailers and consumer-related businesses reduced advertising spend and printers halted production. Due to depressed demand and our focus on reducing inventory, we implemented 490,000 tons of commercial downtime across the group within the segment, reducing EBITDA by US\$125 million and graphic paper inventory by 63,000 tons. Pricing declined moderately in most markets, in line with variable costs.

The DP segment experienced a rapid downturn in demand as retail stores globally were shut in response to the Covid-19 pandemic and clothing sales were particularly hard hit. This led to a chain reaction throughout the supply chain as orders were cancelled. There were some volume gains in the Chinese market which partially offset greater volume reductions from our major customers. In response to the lower demand, we curtailed 93,000 tons of production, and switched some capacity at Ngodwana and Cloquet to paper pulp production, both for internal consumption as well as external sale. In total 86,000 tons of BCTMP and kraft paper pulp were sold from Matane, Ngodwana and Cloquet in the quarter and were included in the segment sales volumes.

Earnings per share excluding special items was a loss of 10 US cents, compared to the profit of 4 US cents earned in the equivalent quarter last year. Special items reduced earnings by US\$20 million and related mainly to the write-down of the Umkomaas Lignin (Lignotech) joint venture and the mechanical breakdowns at the Stockstadt and Alfeld Mills.

Cash flow and debt

Net cash utilised for the quarter was US\$67 million, compared to the US\$17 million in the equivalent quarter last year. The increase in cash utilisation was due to lower cash generation from operations and increased finance costs, offset by lower capital expenditure.

Cash taxes for the quarter were a receipt of US\$13 million, principally due to a refund following a tax review in South Africa.

Net debt increased by US\$98 million from the prior quarter to US\$1,977 million as a result of the cash utilised in the quarter and the US\$30 million impact of currency movements on the translation of Euro and ZAR debt.

Liquidity comprised cash on hand of US\$190 million and US\$503 million available from the group's committed revolving credit facilities.

Outlook

As indicated in the Covid-19 update issued on 30 March 2020, we will not be providing a profit forecast or guidance as the potential impact of the virus cannot be estimated reliably. We expect the slow recovery in our markets to progress in the coming quarter and estimate sales volumes of 75% and 70% of prior year levels for DP and graphic papers respectively.

Current liquidity headroom in the group remains good, with cash deposits at the end of the quarter of US\$190 million and committed revolving credit facilities of approximately US\$503 million. As previously communicated, due to the uncertainty regarding short-term trading conditions and to ensure we have adequate liquidity for the duration of this difficult period, we negotiated the suspension of our credit facility financial covenants from June 2020 to March 2021. This suspension is subject to customary conditions for this kind of relief, which only apply during the suspension period, and include no dividend payments, limitations on incurrence of indebtedness, maximum capex spending limits, a minimum liquidity requirement and no M&A activity without prior bank approval.

Demand for DP appears to have reached a low point in late May. Subsequently we have seen a steady recovery in demand. We will continue to make some additional paper pulp at Cloquet for internal use, foregoing some less profitable DP sales. Pricing remains under pressure as viscose staple fibre pricing and operating rates remain at depressed levels.

Logistics problems at the Durban port, and a reduction in the number of container ships docking in South Africa, partially as a result of port issues, are currently hampering a further recovery in sales volumes.

The packaging and specialities segment continues to grow, and with much of our volumes sold into the food and hygiene sector, should be more resilient during the crisis. As lockdowns ease in various parts of the world and various industries recover, we expect demand for products such as release liner and digital imaging to accelerate and qualification of new products to resume.

We believe that the decline in graphic paper demand in Europe and the US due to Covid-19 reached a low in June, and a slow recovery is underway as economies open and retail and advertising activity increase. Significant capacity reduction in the US and Europe by our competitors, along with our own paper machine closures at Westbrook and Stockstadt mills, should result in improved operating rates in the new financial year.

As a result of the *force majeure* declaration at the Saiccor expansion project, completion is now estimated in the third quarter of FY2021. Work on the expansion recommenced fully in July. All remaining material discretionary projects and major maintenance shuts have been moved out as late as practically possible. As a result, capital expenditure in the last quarter is expected to be approximately US\$110 million.

On behalf of the board

S R Binnie
Director

G T Pearce
Director

30 July 2020

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 on 30 July 2020 via the JSE link and also available the sappi website at www.sappi.com.

Copies of the full announcement may be requested by contacting Jeanine Olivier on telephone: +27 (0)11 407 8307, email: Jeanine.Olivier@sappi.com.

The JSE link is as follows: <https://senspdf.jse.co.za/documents/2020/jse/isse/SAVVI/sappiQ320.pdf>

JSE Sponsor: UBS South Africa (Pty) Ltd