Record earnings for Sappi despite challenging year

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Commenting on the group's results, Sappi chief executive officer Steve Binnie said: "I am very pleased with Sappi's exceptional performance this past year. Once again, the dedication and resilience of the Sappi team shone through, this year delivering EBITDA of $1,339m, well above the previous record set in FY2000 ($1,052m). The outstanding performance was particularly noteworthy within the context of a challenging macroeconomic environment. Significant headwinds included extreme weather-related events, lingering Covid pandemic effects in China as well as extraordinary global inflation, which was triggered by geopolitical turmoil and ongoing global supply chain disruptions. Amidst this volatility, we demonstrated adaptability and persistence and remained committed to our Thrive25 strategy.

Highlights for the year included strong demand and the implementation of higher sales prices to offset rising costs, combined with a focus on product and customer mix optimisation, supported margin expansion in all product segments. In addition, Sappi has resumed dividend payments, with a dividend of US 15 cents being declared.

The strategic priority to invest in packaging and speciality papers in recent years reaped rewards. The segment continued to grow and achieved record EBITDA of $359m compared to $214m in the prior year. Sales volumes increased by 9%, driven by robust global demand and renewed growth in Europe. However, sales were constrained by available capacity and low levels of inventory in South Africa and North America where demand exceeded supply.

Sales volumes for the pulp segment increased by 15% compared to the prior year on the back of strong market demand and improved logistics as we secured regular breakbulk shipping alternatives for our South African exports. Demand for Verve[1] during the year was particularly strong and sales were constrained by available production.

The graphic paper segment generated record EBITDA of $650m. The remarkable turnaround from the lows of 2020 was driven by a number of factors which led to an unprecedented global shortage of graphic paper. These included a surge in demand as economic activity normalised post-Covid and a very tight market balance due to a combination of chronic global logistical challenges and reduced supply.

Our Thrive25 strategic objective to reset the balance sheet was largely achieved. Net debt at financial year end decreased by 40%, from $1,946m to $1,163m 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 twenty years. In addition, during October 2022 Sappi repurchased $206m of the aggregate principal amount of its 2026 bonds via a tender offer. The transaction is fully aligned with the Thrive25 strategic objective to strengthen the balance sheet and yielded a capital gain of $16m and will reduce gross annual interest payments by approximately $6m per annum.

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 $1bn. 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.

Sustainability forms the foundation of our Thrive25 strategy as we strive to be a trusted, transparent, and innovative partner in building a biobased circular economy. We are on track to meet or exceed our Thrive25 sustainability targets. A highlight for the year was the validation of our 2030 decarbonisation targets by the Science Based Targets Initiative which re-enforces our commitment to climate action.

Looking forward, Binnie stated: “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.”

Financial summary for the quarter and full year

- EBITDA excluding special items
  - For the quarter $391m (Q4 FY21 $177m)
  - For the year $1,339m (FY21 $532m)
- Profit for the period
  - For the quarter $26m (Q4 FY21 $35m)
  - For the year $536m (FY21 $13m)
- EPS excluding special items
  - For the quarter 44 US cents (Q4 FY21 11 US cents)
  - For the year 138 US cents (FY21 15 US cents)
- Net debt $1,163m (FY21 $1,946m)
- Resumption of dividend 15 US cents per share

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 $391m, which was $20m above the previous record achieved in the prior quarter.

VSF and hardwood DP market prices dropped during the quarter responding to weaker demand in China related to Covid 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.

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.

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.

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 and as previously announced, on 29 September 2022, Sappi signed an agreement 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 proceeds will be used to reduce debt further, which will provide a platform for future expansion in our identified growth market segments.

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 $418m investment at Somerset 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 $1bn. 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 graphic paper and transition our portfolio to packaging and speciality papers, pulp and biomaterials.

Dividends

On 9 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. The dividend will be funded from cash reserves. 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, which will reduce EBITDA by approximately $18m.

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

[Click here to view FY22 Q 4 Results — the period ended September 2022](#).

Please click on the link below to hear more about these record results in this LinkedIn interview featuring Steve Binnie, Sappi Limited's CEO: https://www.linkedin.com/feed/update/urn:li:activity:6996469415252742145

- **Sappi signs milestone 175GWh per annum renewable energy Power Purchase Agreement with Enpower Trading** 8 May 2024
- **Promising SA-first solution to convert paper sludge, food and textile waste into bioethanol** 29 Apr 2024
- **Sappi's Pelletin achieves feed safety assurance certification for its lignin-based animal feed additive** 22 Mar 2024
- **Sappi achieves PEFC Group Scheme certification for small growers** 19 Dec 2023
- **Saiccor Mill dissolving pulp facility completes the Higg FSLM verification** 6 Dec 2023

Sappi

Sappi works closely with customer, both direct and indirect, in over 100 countries to provide them with the relevant and sustainable paper, paper-pulp and dissolving wood pulp products and related services and innovations.

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