



Forestry & Paper

Sappi: Q3 21E Insights

Key message: Strong Q3 expected. However, Q4 key for SAP in terms of capturing the benefit from higher DWP prices. In South Africa, we estimate a Q4 EBITDA impact of USD 0.5mn for every ton of DWP.

- **Q3 21E results this Thursday, key numbers to look out for:** EBITDA USD 134mn (+417% y/y and +9% q/q) and EPS of USD 0.04/share. [Refer to Segmental outlook.](#)
- **Recent unrest in South Africa and Transnet force majeure will impact Q4:** SAP had already guided to lower volumes (DWP: -28kt and Graphic Paper: -7kt) due to unrest in KwaZulu-Natal, thus lowering Q4 EBITDA by USD 16mn. Subsequently, Transnet declared force majeure due to disruptions from a cyber-attack on 22 July. We expect SAP to provide a detailed update in terms of their efforts to ship product and the associated impact on the Saiccor expansion (we assume a Q1 22E ramp-up).
- **Another strong quarter expected for South Africa thanks to DWP:** We expect EBITDA to increase by 49% q/q to USD 70mn, with the EBITDA margin expanding to 21.5%. This is driven by a higher DWP price (average for Jan-March '21: USD 933/t +36% q/q), more than enough to offset a stronger ZAR (+5% q/q & +21% y/y vs. the USD). We have pencilled in average realised DWP price of USD 840/t.
- **North America firing on all cylinders, with momentum from Q2 continuing into Q3:** EBITDA margin to expand to 12% (+90bps q/q) and EBITDA to increase by 22% q/q to USD 57mn. This is driven by higher DWP prices and SAP's paper machines running full due to industry capacity rationalization in 2020.
- **Europe to come under further pressure due to higher pulp prices and coated paper prices still lagging:** We expect a decent quarter from a graphic paper volume perspective (in the green), supported by market share gains from closures. However, with limited price increases realised and cost pressures from pulp (+25-35%), the European EBITDA will come under further pressure, -72% q/q to USD 8mn (EBITDA margin: 1.5%).
- **Gearing to improve with net debt/EBITDA to decline further:** Net debt likely to be below USD 2.1bn in Q3 with net debt/EBITDA of 4.7x. Encouragingly, we expect net debt/EBITDA to be below 3.5x in Q1 22e.
- **Maintain OVERWEIGHT but lower TP by 9%:** SAP has rallied 27% YTD, ahead of most of its peers. SAP continues to offer further double-digit upside. SAP is currently trading on a 1-yr rolled forward P/E (x) and EV/EBITDA (x) of 5.6x (10-yr average 9.3x) and 5.3x (10-yr average 5.5x), respectively. We value SAP using a SotP EV/EBITDA and set a 1-yr TP of ZAR 65.20/share.

Financial summary

USDmn (to September)	FY 19A	FY 20A	FY 21E	FY 22E	FY 23E
Sales	5 746	4 609	5 257	5 700	5 545
EBITDA ex. special items	687	378	533	720	675
EBITDA margin (%)	12.0%	8.2%	10.1%	12.6%	12.2%
EPS ex. special items	44	-5	14	56	53
FCF (USDm)	150	66	-5	473	439
FCF/share	0.28	0.12	-0.01	0.86	0.80
Net debt	1 501	1 957	2 144	1 723	1 328
Net debt/EBITDA (x)	2.2	5.2	4.0	2.4	2.0
ROCE (%)	11.0%	1.6%	4.8%	9.9%	9.5%

Source: Company data, Chronux Research estimates

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Rating:

Overweight

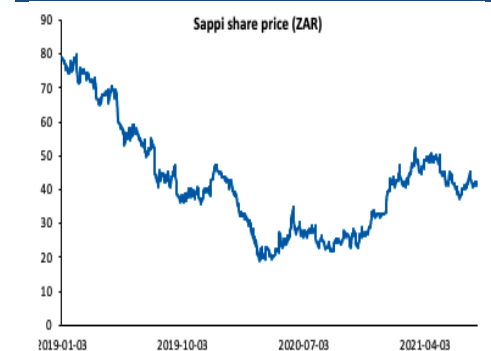
Price (03/08/2021): R40.33
Target Price: R65.20
Total return: 62%

Market cap R23.1bn
Shares in issue 547.4mn

Q3 21e results on Thursday: 9am, with a conference call at 3pm ([Conference call registration](#)).

Peers	CY 19A	CY 20A	CY 21A YTD
Grasim	-11%	25%	15%
Lenzing	0%	0%	30%
Mondi	10%	5%	19%
Sappi	-45%	-25%	27%
Stora Enso	27%	21%	7%
UPM	40%	-1%	13%
Verso	-22%	-33%	5%

Source: Bloomberg, Chronux Research



Source: Bloomberg, Chronux Research

Segmental outlook by region in local currency

Figure 22 Europe segmental outlook (EURmn)

EURmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21E	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	2 587	2 067	482	483	415	477	1 858	1 877	1 865
Operating profit excluding special items	93	7	-	-8	-22	-28	-58	-50	27
Operating profit excluding special items to sales (%)	3.6%	0.3%	0.0%	-1.7%	-5.2%	-5.8%	-3.1%	-2.7%	1.4%
EBITDA excluding special items	206	128	29	23	6	-0	58	50	124
EBITDA excluding special items to sales (%)	8.0%	6.2%	6.0%	4.8%	1.5%	0.0%	3.1%	2.7%	6.7%
Depreciation & amortisation	113	121	29	31	28	28	116	100	97
EUR/USD average	1.13	1.12	1.19	1.21	1.20	1.21	1.21	1.21	1.19
Sale volumes (kt)	3 241	2 698	658	669	567	645	2 539	2 493	2 444
Coated paper	2 764	2 220	536	540	446	519	2 041	1 980	1 921
Packaging and specialties	477	478	122	129	121	126	498	513	523
Average European selling price (EUR/t)	798	766	733	722	732	740	732	753	763
Graphic paper	745	698	650	637	638	656	646	663	665
Packaging and specialties	1 072	1 113	985	1 076	1 081	1 087	1 058	1 100	1 122

Source: Chronux Research, Company data

Figure 23 North America segmental outlook (USDmn)

USDmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21E	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	1 466	1 385	384	418	472	489	1 763	1 955	1 896
Operating costs	-1 439	-1 412	-386	-400	-444	-446	-1 676	-1 796	-1 806
Operating profit excluding special items	27	-27	-2	18	28	43	87	159	90
Operating profit excluding special items to sales (%)	1.8%	-1.9%	-0.5%	4.2%	5.9%	8.8%	4.9%	8.1%	4.7%
EBITDA excluding special items	110	79	27	47	57	72	202	270	193
EBITDA excluding special items to sales (%)	7.5%	5.7%	7.0%	11.1%	12.0%	14.6%	11.5%	13.8%	10.2%
Depreciation & amortisation	83	106	29	29	29	29	115	111	103
Sales volumes (kt)	1 379	1 516	421	423	448	458	1 750	1 877	1 850
CFS	904	733	175	189	198	198	794	904	877
Specialty (Westbrook)	20	13	5	5	5	5	20	20	20
Market pulp (US ops)	35	70	-	10	10	10	30	-	-
Matane pulp	-	121	53	50	50	50	203	200	200
DWP	290	253	69	69	75	75	288	333	333
Packaging and Specialties	190	317	105	100	110	120	435	420	420
Average price realised (USD/t)	1 063	914	912	988	1 054	1 068	1 007	1 041	1 025
Graphic paper	1 036	978	960	970	990	990	978	990	990
Packaging and specialties	1 186	1 127	1 135	1 155	1 185	1 185	1 185	1 197	1 197
DWP	853	610	650	717	840	977	796	903	770

Source: Chronux Research, Company data

Figure 24 South Africa segmental outlook (ZARmn)

ZARmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21E	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	20 402	15 918	3 489	4 743	4 592	5 145	17 969	20 976	21 105
Operating profit excluding special items	3 832	1 217	267	438	672	1 195	2 572	4 431	3 855
Operating profit excluding special items to sales (%)	18.8%	7.6%	7.7%	9.2%	14.6%	23.2%	14.3%	21.1%	18.3%
EBITDA excluding special items	4 864	2 450	550	707	989	1 519	3 765	5 799	5 234
EBITDA excluding special items to sales (%)	23.8%	15.4%	15.8%	14.9%	21.5%	29.5%	21.0%	27.6%	24.8%
Depreciation & amortisation	1 032	1 233	283	269	317	324	1 193	1 368	1 379
USD/ZAR average	14.35	16.22	15.72	14.95	14.14	14.34	14.79	14.84	15.64
Sale volumes excl. Forestry (kt)	1 639	1 406	296	414	379	383	1 472	1 637	1 728
Graphic Paper and Packaging and Specialties	650	545	116	176	155	157	604	621	621
DWP	999	861	180	238	224	226	868	1 016	1 107
Forestry	1 363	1 168	308	330	330	330	1 298	1 298	1 298
Average price realised (USD/t)	765	711	759	712	759	759	745	673	673
Graphic Paper and Packaging and Specialties	765	711	759	712	759	759	745	673	673
DWP	853	610	650	717	840	977	796	903	770
Forestry	59	52	55	58	58	58	57	61	61

Source: Chronux Research, Company data

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