

Forestry & Paper

Sappi: Q4 21E Insights

Key message: Maintain **OVERWEIGHT**. Strong Q4 expected, marking the 5th consecutive quarter of improving EBITDA to USD 189mn and EPS of USD 0.11/share. We expect net debt/EBITDA to decline to 3.8x.

- **Q4 21E results this Thursday (11 November), key numbers to look out for:** Q4 to mark the fifth consecutive quarter of EBITDA improving to USD 189mn (+130% y/y and +30% q/q) and EPS of USD 0.11/share. [Refer to Segmental outlook.](#)
- **Another strong quarter expected for DWP:** The CCF DWP price (lagged 3m) increased by 74% y/y and by 16% q/q. Additionally, the ZAR weakened by 2% q/q. SAP guided for an incremental c.50kt in the quarter; however, we have pencilled in 43kt as global supply chain disruptions continue. FY 22E looks to be promising, as we expect the average DWP price to be 10% higher y/y. Additionally, we estimate an incremental 93kt of volumes sold in South Africa (Ngodwana oxygen issues: +23kt; Saiccor expansion delay: +40kt; Logistic issues: +10kt; Saiccor expansion ramp-up: +60kt and impact from the conversion of the calcium line: -40kt).
- **North America firing on all cylinders, with momentum from Q3 continuing into Q4:** US CFS producers have been fully sold out on the back of strong demand. This has seen demand in Q4 exceed 10%, with producer inventories declining during the quarter. Additionally, the pricing environment remains strong, with the CFS price up 15% y/y and 7% q/q.
- **Despite guidance for European margins to remains flat q/q we believe there is downside risk due to higher energy and pulp costs:** We estimate a Q4 21E EBITDA margin of -2%. FY 22E looks to be promising in the absence of surcharge pricing eroding demand further in favour of online. The spot CWF price is already up 9% since 30 September and encouragingly, the European softwood pulp marked its first decline this year of -2% this week. We estimate a FY 22E EBITDA margin of 5.1% (more than 2x), but still below the LT average of 8.1%. This is on the back of energy costs adversely impacting margins. SAP is c.50-55% integrated (function of net short pulp position), with energy costs hedged four years in advance.
- **FY 22E FCF to improve significantly:** With no material CapEx approved after the Saiccor expansion, this should unlock USD 150-200mn FCF next year. Coupled with EPS growth of 300% to USD 0.45/share, this should reduce net debt by 18%, with net debt/EBITDA declining further to 2.4x (FY 21E: 3.8x).
- **Maintain OVERWEIGHT:** SAP has rallied 36% 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 6.2x (10-yr average 10.2x) and 4.7x (10-yr average 5.4x), respectively. We value SAP using a SotP EV/EBITDA and set a 1-yr TP of ZAR 60.24/share.

Financial summary

USDmn (to September)	FY 19A	FY 20A	FY 21E	FY 22E	FY 23E
Sales	5 746	4 609	5 488	5 914	5 763
EBITDA ex. special items	687	378	543	699	667
EBITDA margin (%)	12.0%	8.2%	9.9%	11.8%	11.6%
EPS ex. special items	44	-5	15	45	41
FCF (USDm)	150	66	36	436	401
FCF/share	0.28	0.12	0.06	0.78	0.67
Net debt	1 501	1 957	2 088	1 704	1 347
Net debt/EBITDA (x)	2.2	5.2	3.8	2.4	2.0
ROCE (%)	11.0%	1.6%	5.2%	9.1%	8.8%

Source: Company data, Chronux Research estimates

Date: 09 November 2021

Analyst

Sean Ungerer CA (SA), CFA
+27 82 319 3373

sean.ungerer@chronux.co.za

Rating:

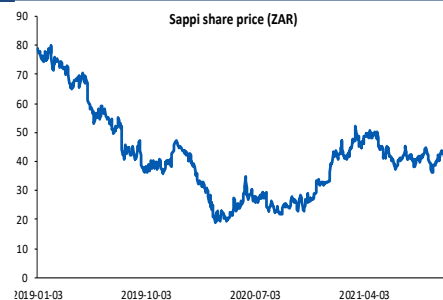
Overweight

Price (09/11/2021):	R44.38
Target Price:	R60.24
Total return:	36%
Market cap	R25.4bn
Shares in issue	547.4mn

Q4 21E results on Thursday: 9am, with a conference call at 4pm ([Conference call registration](#)).

Key price changes for Q4 21E			
Graphic Paper	y/y % chg.	q/q % chg.	q/q % chg.
CWF (EUR)	1%	5%	5%
CM (EUR)	-2%	5%	5%
CFS (USD)	15%	7%	7%
Pulp			
	y/y % chg.	q/q % chg.	q/q % chg.
BHKP pulp (EUR)	65%	16%	16%
NBSK pulp price (EUR)	57%	15%	15%
BCTMP HW (USD)	19%	-13%	-13%
DWP lagged 1-quarter (USD)	74%	16%	16%
Average FX			
	y/y % chg.	q/q % chg.	q/q % chg.
USD/ZAR	-15%	2%	2%
EUR/USD	1%	-2%	-2%

Source: Bloomberg, CCF, FOEX



Source: Bloomberg, Chronux Research

Peers	Share price performance		
	CY 19A	CY 20A	CY 21A YTD
Grasim	-11%	25%	13%
Lenzing	0%	0%	31%
Mondi	10%	5%	9%
Sappi	-45%	-25%	36%
Stora Enso	27%	21%	-8%
UPM	40%	-1%	1%
Verso	-22%	-33%	96%

Source: Bloomberg, Chronux Research

Segmental outlook by region in local currency

Figure 1 Europe segmental outlook (EURmn)

EURmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21A	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	2 587	2 067	482	483	536	568	2 069	2 181	2 141
Operating profit excluding special items	93	7	-	-8	-15	-40	-63	-8	95
Operating profit excluding special items to sales (%)	3.6%	0.3%	0.0%	-1.7%	-2.8%	-7.1%	-3.1%	-0.4%	4.4%
EBITDA excluding special items	206	128	29	23	14	-12	54	111	210
EBITDA excluding special items to sales (%)	8.0%	6.2%	6.0%	4.8%	2.6%	-2.0%	2.6%	5.1%	9.8%
Depreciation & amortisation	113	121	29	31	29	29	118	119	115
EUR/USD average	1.13	1.12	1.19	1.21	1.20	1.18	1.19	1.16	1.16
Sale volumes (kt)	3 241	2 698	658	669	733	758	2 818	2 765	2 660
Coated paper	2 764	2 220	536	540	592	614	2 282	2 213	2 102
Packaging and specialties	477	478	122	129	141	144	536	552	558
Average European selling price (EUR/t)	798	766	733	722	731	750	734	789	805
Graphic paper	745	698	650	637	641	671	651	711	721
Packaging and specialties	1 072	1 113	985	1 076	1 081	1 087	1 059	1 101	1 123

Source: Chronux Research, Company data

Figure 2 North America segmental outlook (USDmn)

USDmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21A	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	1 466	1 385	384	408	438	474	1 704	1 945	1 857
Operating costs	-1 439	-1 412	-386	-397	-407	-432	-1 622	-1 808	-1 795
Operating profit excluding special items	27	-27	-2	11	31	42	82	137	61
Operating profit excluding special items to sales (%)	1.8%	-1.9%	-0.5%	2.7%	7.1%	8.9%	4.8%	7.0%	3.3%
EBITDA excluding special items	110	79	27	35	57	68	187	238	157
EBITDA excluding special items to sales (%)	7.5%	5.7%	7.0%	8.6%	13.0%	14.3%	11.0%	12.3%	8.4%
Depreciation & amortisation	83	106	29	24	26	26	105	101	96
Sales volumes (kt)	1 379	1 516	421	427	428	425	1 701	1 814	1 790
Graphic Paper	904	733	175	189	198	185	794	794	770
Matane pulp	-	121	53	47	37	40	177	200	200
DWP	290	253	69	69	75	70	283	300	300
Packaging and Specialties	210	330	129	127	136	130	522	520	520
Average price realised (USD/t)	1 063	914	912	956	1 024	1 115	1 002	1 072	1 037
Graphic paper	1 036	978	960	970	990	1 059	995	1 043	982
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	724	840	977	798	874	778

Source: Chronux Research, Company data

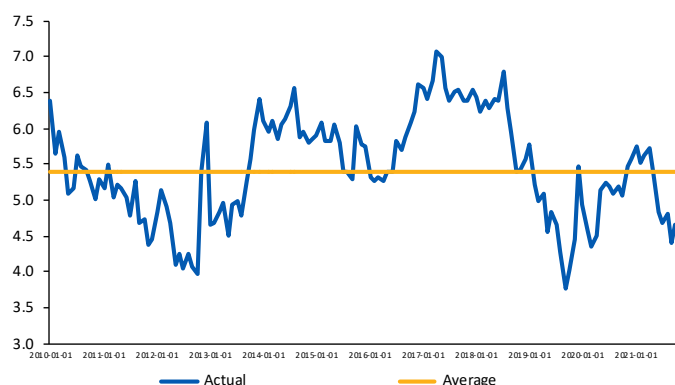
Figure 3 South Africa segmental outlook (ZARmn)

ZARmn (to September)	FY 19A	FY 20A	Q1 21A	Q2 21A	Q3 21A	Q4 21E	FY 21E	FY 22E	FY 23E
Sales	20 402	15 918	3 489	4 743	4 764	5 783	18 779	20 679	20 502
Operating profit excluding special items	3 832	1 217	267	438	744	1 639	3 088	3 700	2 718
Operating profit excluding special items to sales (%)	18.8%	7.6%	7.7%	9.2%	15.6%	28.3%	16.4%	17.9%	13.3%
EBITDA excluding special items	4 864	2 450	550	707	1 029	1 963	4 249	5 075	4 105
EBITDA excluding special items to sales (%)	23.8%	15.4%	15.8%	14.9%	21.6%	34.0%	22.6%	24.5%	20.0%
Depreciation & amortisation	1 032	1 233	283	269	285	325	1 162	1 375	1 387
USD/ZAR average	14.35	16.22	15.72	14.95	14.14	14.62	14.85	15.30	15.36
Sale volumes excl. Forestry (kt)	1 639	1 406	296	414	372	406	1 488	1 589	1 688
Graphic Paper and Packaging and Specialties	650	545	116	176	163	157	612	621	621
DWP	999	861	180	238	209	249	876	968	1 067
Forestry	1 363	1 168	308	330	397	397	1 432	1 432	1 432
Average price realised (USD/t)	765	711	759	703	825	825	777	673	673
Graphic Paper and Packaging and Specialties	765	711	759	703	825	825	777	673	673
DWP	853	610	650	724	840	977	798	874	778
Forestry	59	52	55	58	58	58	57	61	61

Source: Chronux Research, Company data

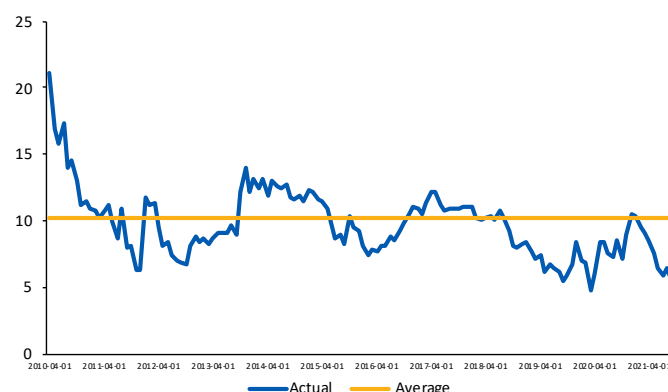
Valuation and key charts

Figure 4 Sappi historical 1-yr fwd EV/EBITDA (x)



Source: Bloomberg, Chronux Research

Figure 5 Sappi historical 1-yr fwd P/E (x)



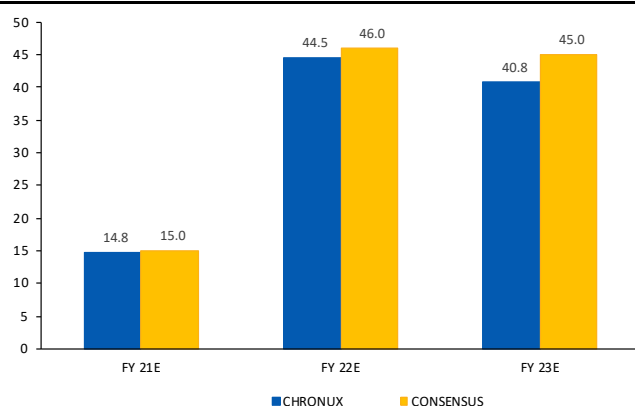
Source: Bloomberg, Chronux Research

Figure 6 Sappi SotP EV/EBITDA (x) – using spot FX

Details (USDm)	Y1 rolled EBITDA	EV/EBITDA (x)	EV by region (USDm)	% of total EV
Europe	141	5.5	776	17%
North America	229	6.0	1 376	31%
South Africa	333	7.0	2 331	52%
Group	703	6.4	4 483	100%
Last reported net debt			-2 055	
Equity value			2 428	
WANOS (m)			601.4	
TP (USD/share)			4.04	
Spot USD/ZAR			14.92	
TP (ZAR/share)			60.24	
Current share price			44.38	
Expected 1-yr return			36%	

Source: Bloomberg, Chronux Research, Company data,

Figure 7 EPS outlook (USD/share)



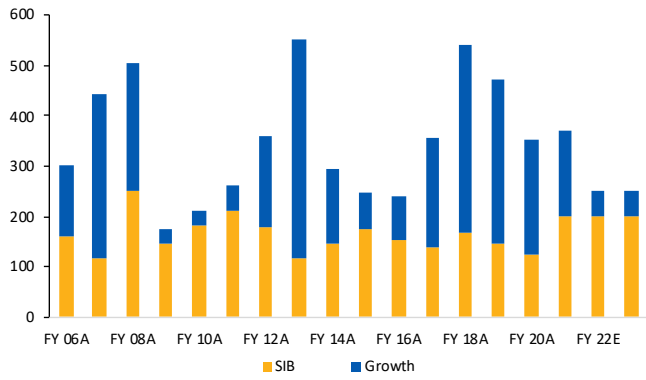
Source: Chronux Research, Company data

Figure 8 FY 22E EPS sensitivity

		Average exchange rate (USD/ZAR)					
		14.00	14.50	15.00	15.50	16.00	16.50
Average DWP price (USD/t)	750	0.12	0.15	0.18	0.21	0.23	0.26
	800	0.22	0.25	0.28	0.31	0.33	0.36
	850	0.32	0.35	0.38	0.41	0.44	0.46
	900	0.41	0.44	0.47	0.50	0.53	0.56

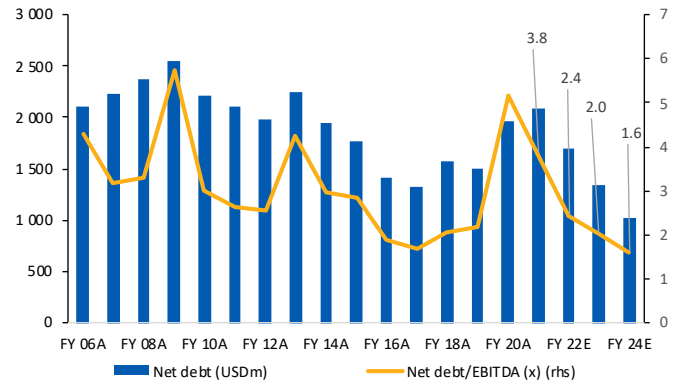
Source: Chronux Research, Company data

Figure 9 CapEx outlook (USDmn)



Source: Chronux Research, Company data

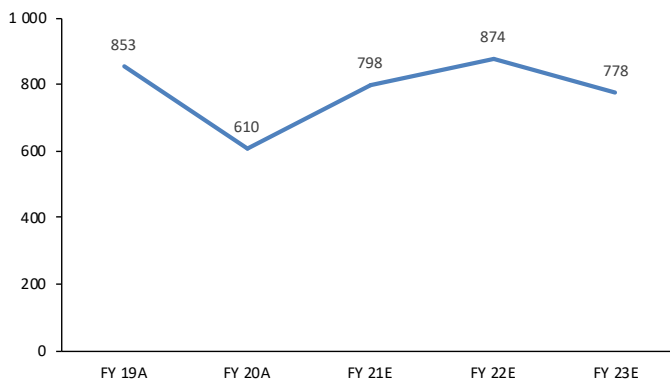
Figure 10 Gearing outlook (USDmn)



Source: Chronux Research, Company data

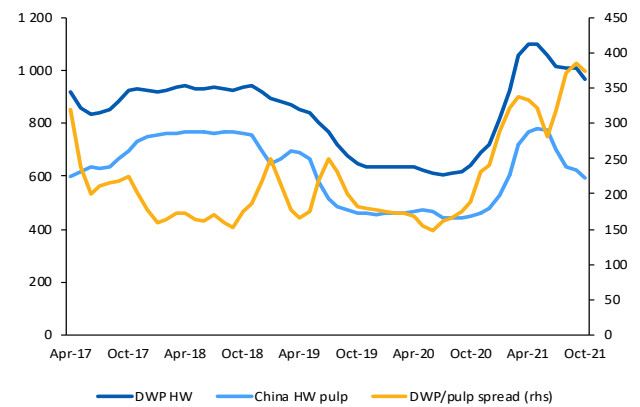
Dissolving wood pulp and VSF prices and key metrics

Figure 11 DWP price outlook for Sappi's FY (USD/t)



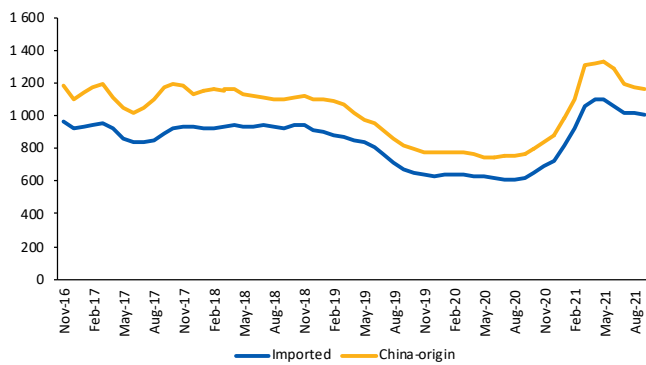
Source: Chronux Research estimates, Company data

Figure 12 DWP/HW Pulp spread (USD/t)



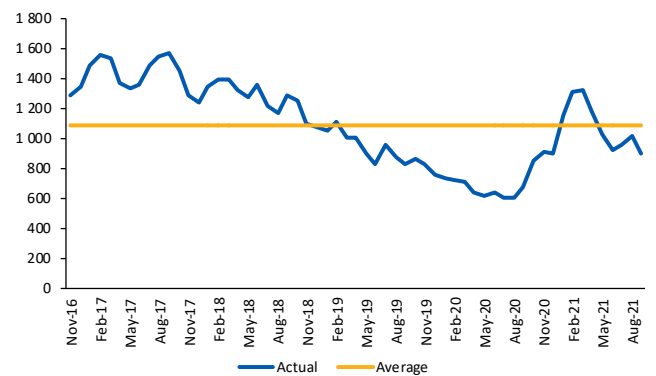
Source: CCF, Chronux Research, FOEX

Figure 13 Hardwood DWP prices (USD/t)



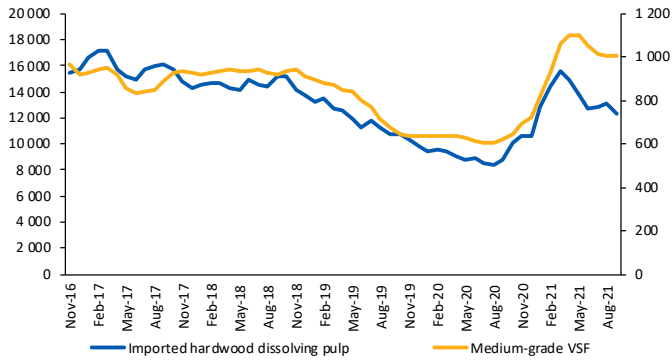
Source: CCF, Chronux Research

Figure 14 VSF/DWP spread (USD/t)



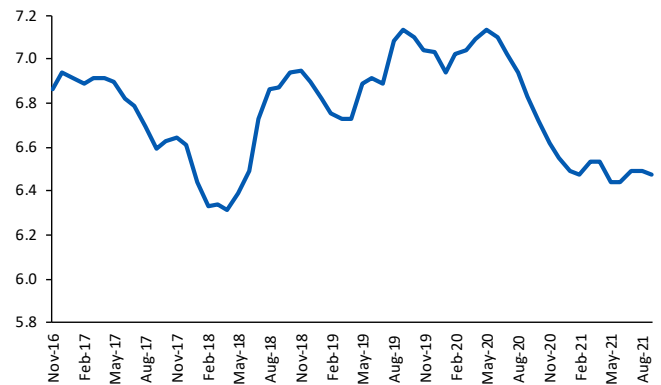
Source: CCF, Chronux Research

Figure 15 VSF price vs. DWP price



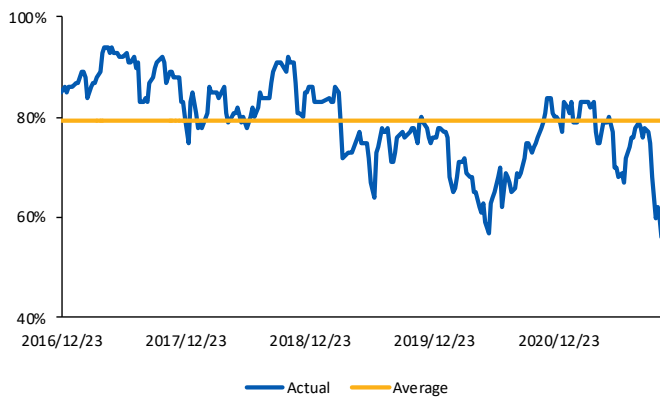
Source: CCF, Chronux Research

Figure 16 USD/RMB FX



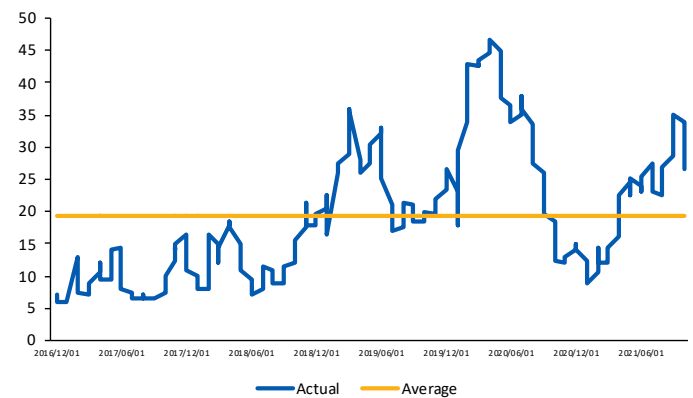
Source: CCF, Chronux Research

Figure 17 China VSF operating rate (%)



Source: CCF, Chronux Research

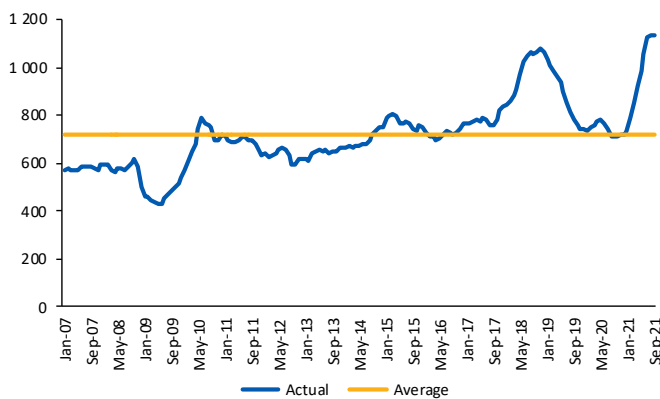
Figure 18 China VSF inventory days (#)



Source: CCF, Chronux Research

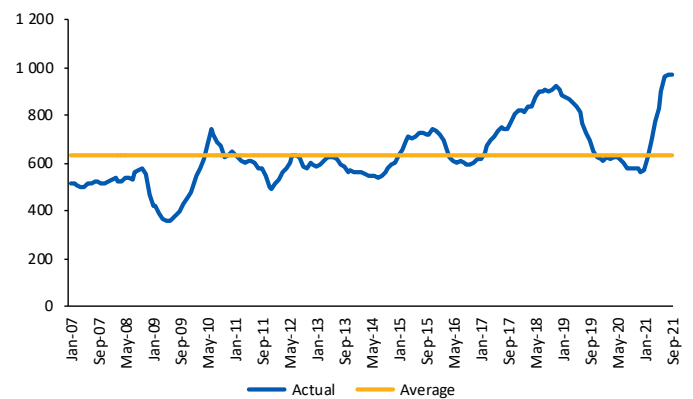
Pulp and Graphic Paper prices

Figure 19 Europe Softwood pulp price (EUR/t)



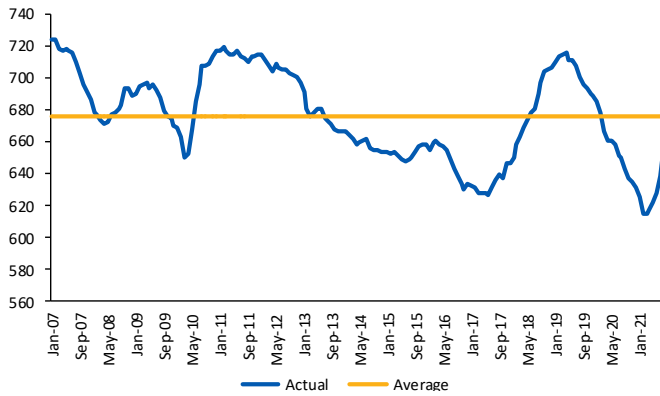
Source: Chronux Research, FOEX

Figure 20 Europe Hardwood pulp price (EUR/t)



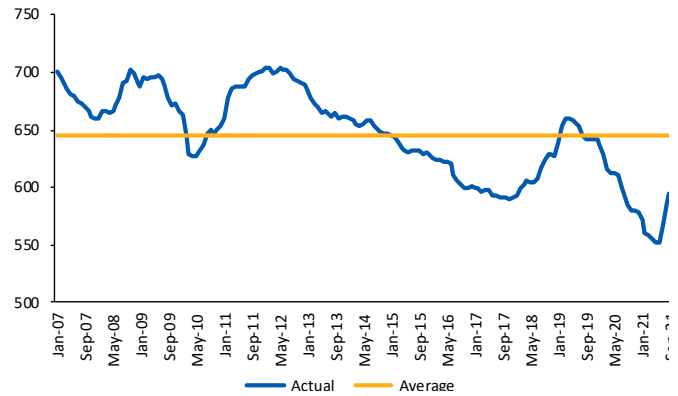
Source: Chronux Research, FOEX

Figure 21 Europe CWF price (EUR/t)



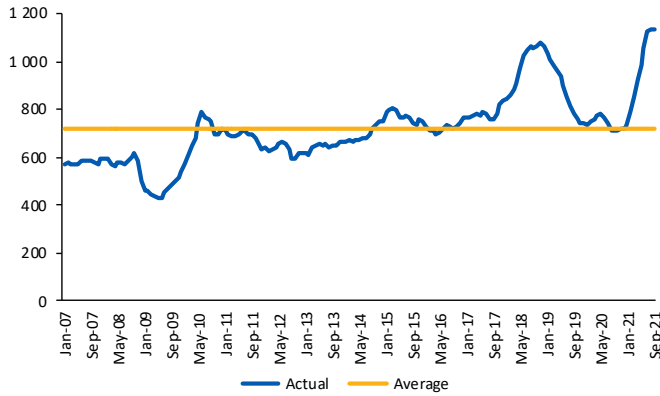
Source: Chronux Research, FOEX

Figure 22 Europe CM price (EUR/t)



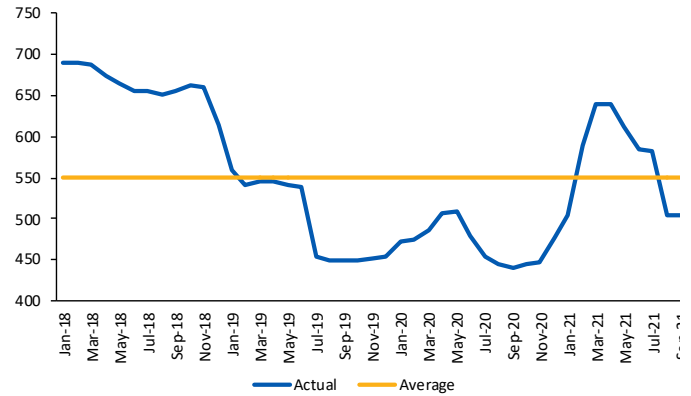
Source: Chronux Research, FOEX

Figure 21 US CFS price (USD/t)



Source: Chronux Research, FOEX

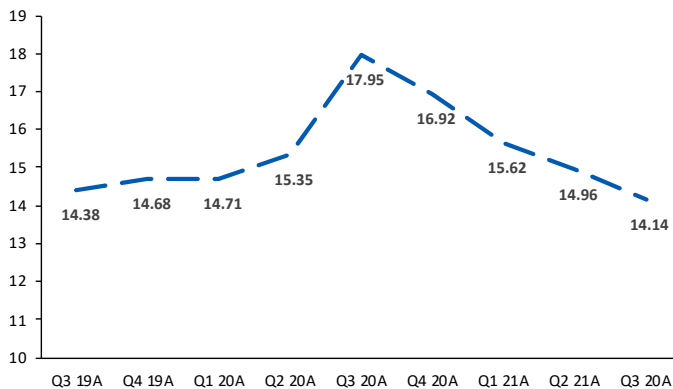
Figure 22 BCTMP HW China import price (USD/t)



Source: Chronux Research, FOEX

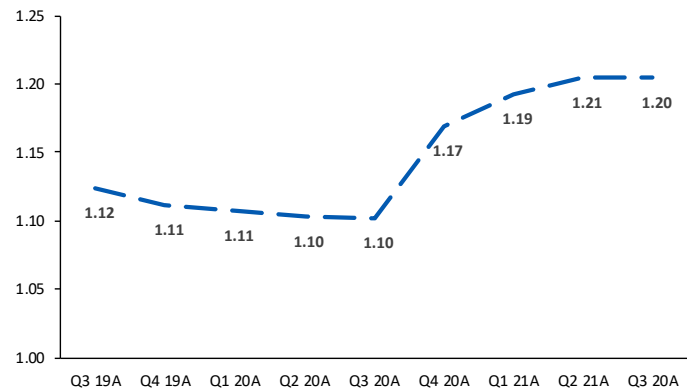
Average FX rates

Figure 25 USD/ZAR average rate by quarter



Source: Bloomberg, Chronux Research

Figure 26 EUR/USD average rate by quarter



Source: Bloomberg, Chronux Research

European graphic paper stats

Figure 27 *Europe Graphic Papers 2021 YTD Printing-writing stats (%)

Details	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	
Graphic Papers	y/y % change								q/q % change							
Total European Shipments	-22.3%	-14.1%	-4.7%	13.9%	27.3%	33.9%	10.6%	16.2%	3.3%	16.1%	-10.3%	2.1%	6.5%	-8.6%	4.7%	
To Europe	-22.1%	-14.6%	-2.9%	20.0%	35.5%	32.0%	5.7%	11.0%	3.7%	14.5%	-12.3%	1.5%	8.4%	-7.6%	4.0%	
To Outside Europe	-22.9%	-12.0%	-10.9%	-2.8%	6.2%	41.2%	34.1%	40.5%	1.6%	22.5%	-2.6%	3.8%	0.2%	-12.5%	7.2%	
European demand	-22.3%	-15.1%	-4.5%	17.5%	32.9%	30.7%	4.5%	9.9%	3.3%	14.1%	-11.9%	1.1%	8.0%	-7.7%	3.4%	
Newsprint																
Total European Shipments	-23.2%	-20.3%	-12.2%	1.5%	8.5%	11.4%	6.9%	6.1%	4.4%	20.5%	-10.7%	3.2%	1.9%	-3.2%	0.0%	
To Europe	-26.1%	-24.0%	-11.2%	5.6%	27.7%	16.3%	10.8%	8.4%	0.0%	20.4%	-7.4%	3.0%	3.9%	-0.9%	-2.8%	
To Outside Europe	-13.5%	-9.7%	-14.6%	-8.3%	-23.0%	-0.9%	-3.9%	0.0%	16.7%	20.5%	-18.5%	3.6%	-3.5%	-10.0%	9.1%	
European demand	-26.7%	-24.3%	-12.3%	4.4%	23.7%	14.0%	8.0%	6.1%	0.4%	20.9%	-7.7%	2.6%	4.7%	-2.7%	-3.4%	
SC-Magazine																
Total European Shipments	-26.7%	-15.7%	2.4%	20.9%	17.1%	27.9%	9.0%	7.6%	18.8%	16.7%	-12.4%	-3.6%	8.0%	0.9%	3.9%	
To Europe	-22.4%	-15.4%	3.2%	23.7%	11.7%	20.0%	1.0%	2.9%	14.7%	19.8%	-13.8%	-5.7%	8.8%	-1.5%	8.7%	
To Outside Europe	-51.4%	-17.6%	-3.6%	3.8%	66.7%	121.4%	89.5%	64.7%	55.6%	-3.6%	0.0%	11.1%	3.3%	16.1%	-22.2%	
European demand	-22.4%	-15.4%	3.2%	23.7%	11.7%	20.0%	1.0%	2.9%	14.7%	19.8%	-13.8%	-5.7%	8.8%	-1.5%	8.7%	
Coated Mechanical Reels																
Total European Shipments	-25.2%	-15.3%	-12.4%	10.3%	25.7%	-29.0%	10.7%	20.5%	2.6%	13.8%	-5.9%	1.5%	-47.0%	73.2%	19.4%	
To Europe	-25.0%	-15.4%	-9.6%	15.3%	29.5%	-27.1%	2.6%	11.9%	10.5%	8.3%	-11.7%	3.7%	-40.8%	58.1%	20.5%	
To Outside Europe	-25.7%	-14.5%	-20.6%	-1.1%	15.8%	-36.7%	46.2%	60.0%	-21.3%	37.3%	13.6%	-4.3%	-64.8%	145.2%	15.8%	
European demand	-25.0%	-15.4%	-9.6%	15.3%	29.5%	-27.1%	2.6%	11.9%	10.5%	8.3%	-11.7%	3.7%	-40.8%	58.1%	20.5%	
Uncoated Mechanical (improved & others)																
Total European Shipments	-20.0%	2.4%	0.6%	17.1%	14.0%	152.8%	6.0%	8.8%	17.4%	5.9%	-4.5%	0.0%	109.9%	-55.7%	1.3%	
To Europe	-18.6%	2.3%	5.6%	30.8%	30.3%	143.4%	0.8%	3.1%	15.3%	11.8%	-7.9%	1.4%	93.7%	-52.7%	1.5%	
To Outside Europe	-25.7%	3.1%	-20.6%	-20.5%	-29.3%	189.7%	38.1%	45.0%	26.9%	-18.2%	14.8%	-6.5%	189.7%	-65.5%	0.0%	
European demand	-18.6%	2.3%	5.6%	30.8%	30.3%	147.8%	0.8%	3.1%	15.3%	11.8%	-7.9%	1.4%	97.2%	-53.6%	1.5%	
Coated Woodfree																
Total European Shipments	-27.4%	-19.2%	-2.8%	18.9%	49.5%	56.8%	30.5%	31.9%	2.3%	21.9%	-16.9%	3.5%	10.1%	-7.0%	2.7%	
To Europe	-29.9%	-21.9%	-3.6%	34.7%	72.5%	52.8%	15.0%	17.0%	1.3%	20.7%	-20.2%	2.1%	15.5%	-8.0%	3.2%	
To Outside Europe	-16.7%	-8.0%	0.0%	-10.9%	10.0%	71.4%	125.0%	121.6%	6.2%	26.1%	-5.7%	7.3%	-4.5%	-3.6%	1.2%	
European demand	-29.7%	-22.3%	-4.5%	33.7%	70.6%	52.2%	14.2%	16.2%	0.4%	20.6%	-18.8%	0.8%	14.8%	-8.2%	3.5%	
Uncoated Woodfree																
Total European Shipments	-15.0%	-8.1%	2.4%	21.7%	46.5%	41.7%	5.7%	20.2%	-6.0%	13.6%	-9.3%	3.4%	7.7%	-12.7%	1.4%	
To Europe	-13.2%	-5.9%	3.4%	22.9%	44.0%	38.8%	2.8%	16.5%	-3.7%	9.0%	-11.8%	2.3%	8.4%	-8.9%	-1.5%	
To Outside Europe	-23.0%	-19.1%	-1.9%	17.0%	56.3%	53.9%	21.4%	38.0%	-17.2%	40.3%	2.0%	7.8%	5.4%	-27.4%	15.3%	
European demand	-13.7%	-8.3%	-1.6%	15.4%	38.0%	35.5%	0.9%	13.7%	-4.0%	7.9%	-11.0%	1.8%	6.8%	-8.2%	-2.5%	

Source: Chronux Research, EURO-GRAPH, * Western and Eastern Europe excluding Russia

US graphic paper stats

Figure 28 US 2021 YTD Printing-writing stats (%)

Printing-writing stats (y/y % chg.)	Jan-21	Feb-21	Mar-21	Apr-21	May-21	Jun-21	Jul-21	Aug-21	Sep-21	
Total printing-writing paper shipments	-25%	-29%	-20%	-3%	11%	10%	5%	14%	-4%	
US purchases of total printing-writing papers	-22%	-24%	-18%	-6%	6%	16%	9%	12%	-1%	
Total printing-writing paper levels (m/m)	3%	-1%	-5%	-2%	0%	-4%	0%	-3%	-2%	
UFS										
Shipments	-20%	-19%	-14%	13%	22%	16%	7%	12%	-8%	
Inventory level m/m	3%	0%	-6%	-3%	2%	-3%	0%	-3%	-1%	
Imports	41%	39%	5%	-21%	10%	-5%	4%	13%	31%	
Exports	-40%	-32%	-39%	14%	25%	33%	18%	17%	19%	
CFS										
US purchases	-32%	-32%	-29%	-17%	-16%	-4%	3%	20%	15%	
Inventory level m/m	2%	-2%	-6%	-1%	-1%	-6%	-2%	-3%	-4%	
Imports	-21%	-26%	-23%	-21%	-14%	-6%	32%	46%	50%	
Exports	-6%	-3%	-2%	14%	32%	58%	53%	6%	-3%	
CM										
Shipments	-33%	-38%	-40%	-35%	-14%	41%	16%	-5%	-9%	
Inventory level m/m	0%	-3%	-2%	-3%	1%	-3%	-3%	-3%	-5%	
Imports	-34%	-22%	-2%	-9%	-17%	29%	60%	27%	1%	
Exports	12%	24%	-9%	-29%	5%	41%	31%	15%	27%	
UM										
US purchases	-24%	-31%	-15%	-21%	16%	-9%	28%	14%	-1%	
Inventory level m/m	14%	-6%	-8%	12%	-15%	-5%	-4%	-6%	16%	
Imports	-19%	-22%	-20%	-1%	10%	26%	61%	33%	14%	
Exports	-8%	24%	-28%	-47%	-17%	52%	180%	33%	15%	

Source: AF&PA, Chronux Research

Disclaimer:

This report is not investment, financial, accounting or tax advice and is provided for information purposes only. In preparing this report we did not take your specific needs and investment objectives into account. Any prices or quotations provided are indicative only and may not be used or relied on for any purposes, including valuation purposes. Opinions expressed in this communication may change without any notice. This communication is not a solicitation to buy or sell any product. To the extent permitted by the law, Chronux Research Pty. Ltd. and/or the author(s) accept no responsibility or liability (in negligence or otherwise) for loss or damage resulting from the use of or relating to any error in the information provided. This information has been prepared in good faith and is based on information obtained from third party sources. Any modelling, scenario analysis past or simulated past performance (including back-testing) contained in this information is no indication of future performance. Analysts at Chronux Research might have direct exposure to companies they cover. This product may not be eligible for distribution in all jurisdictions and is directed at institutional investors who have professional experience as defined by the applicable law and/or regulation in the relevant jurisdiction. It is not for retail investors and may not be distributed into any jurisdiction where the information is not permitted. This communication is for the intended recipient only and if you have received this communication in error or in an unlawful manner the report must be destroyed, and the author notified immediately. These disclaimers and exclusions shall be governed and construed in accordance with South African law. If any provisions of these disclaimers and exclusions shall be unlawful, void or for any reason unenforceable then that provision shall be deemed severable and shall not affect the validity and enforceability of the remaining provisions. © Chronux Research Pty. Ltd. All rights of Chronux Research Pty. Ltd are reserved.