Bulletin:

Essity's Solid Financial Profile Can Absorb Acquisition Debt And Quarterly Performance Volatility

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PRIMARY CREDIT ANALYST

Salvio Cascarino
Milan
+ 00390272111303
salvio.cascarino@spglobal.com

SECONDARY CONTACT

Barbara Castellano
Milan
+ 390272111253
barbara.castellano@spglobal.com

ADDITIONAL CONTACT

Industrial Ratings Europe
Corporate_Admin_London@spglobal.com

MILAN (S&P Global Ratings) April 23, 2021--S&P Global Ratings said today that although Sweden-based global hygiene and health company Essity AB (BBB+/Stable/A-2) is set to increase its ownership in Productos Familia S.A. and showed some volatility in its operating performance for first-quarter 2021, this should not put the company's full-year credit metrics under pressure. Essity has agreed to increase its stake in Colombia-based Productos Familia S.A. to 94% from the current 50%. We do not expect this acquisition to pose integration risk since Essity has had a stake in the company since 1985.

We believe the acquisition will support Essity's profitable growth in Latin America, where Productos Familia enjoys solid leading positions in its key markets like Colombia (50% of sales in 2020) and Ecuador (21% of sales), through its main brands Nosotras and Familia in product categories such as feminine care (38% of sales in 2020), consumer tissue (31%), baby care (13%), incontinence products (11%), and professional hygiene (7%). Productos Familia is already fully consolidated in Essity's accounts; and at year-end 2020 generated Swedish krona (SEK) 6,950 million of sales and SEK1,419 million of EBITDA, enjoying similar profitability as the Essity group at about 20%.

We understand the purchase price for the 44% stake will be roughly SEK5.7 billion, which values Productos Familia at SEK13 billion ($1,540 million) on a free-debt basis at an EBITDA multiple of 9.3x. Following the acquisition, we estimate a lower dividend outflow to Productos Familia's minority shareholders, which averaged SEK151 million-SEK227 million over 2018-2020.

Essity's debt will increase to finance the acquisition. However, we estimate the S&P Global Ratings-adjusted debt-to-EBITDA ratio will remain close to 2.5x, which is comfortably within the range commensurate with the 'BBB+' rating. Essity entered 2021 with significant headroom under its credit metrics after closing 2020 with S&P Global Ratings-adjusted debt to EBITDA at 1.8x. As a result, we believe the company is well positioned to face a contraction of performance in first-quarter 2021. The 18.3% sales decline was partly due to a 7.7% impact from foreign currency effects, organic decline of 9.9%, and change in perimeter (0.7%). Approximately half of the organic decline reflects the difficult conditions compared with the same quarter in 2020 after stockpiling by customers and consumers at the beginning of the pandemic.

In addition, ongoing COVID-19-related restrictions and lockdowns translated into weaker performance in the Personal Care segment (due to a slight decrease of consumption with consumers spending more time at home) mainly in the baby care and medical solutions categories. We also noticed a 34.4% decline in sales in professional hygiene, mainly in mature markets, due to high exposure to businesses like offices, schools, restaurants, and hotels. Since restrictions could remain in place for part of the second quarter, we expect professional hygiene to post a more solid recovery from the second half of the year.

The volume decline, negative operating leverage, and higher transportation and marketing costs to support innovation resulted in the EBITDA margin declining 200 basis points to 18.8% in first-quarter 2021. From the second quarter, we expect additional pressure on margins from a spike in raw material prices such as pulp, recycled pulp, and oil derivatives. Essity is proactively managing this through sales price increases, which should fully compensate for higher costs by first-quarter 2022.

We therefore estimate Essity's top line in 2021 will be broadly similar to that in 2020 at SEK121 billion-SEK122 billion, including negative foreign currency effects, and the S&P Global Ratings-adjusted EBITDA margin to contract to 18%-19% from 19.8% in 2020 and recover to 19% or higher from 2022.

This report does not constitute a rating action.