Research Update:

Metsa Board Corp. Affirmed At 'BBB-/A-3' Despite Lower Leverage; Outlook Stable

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Rating Action Overview

- We believe that Metsa Board's sale of a 30% stake in the Husum pulp mill will result in stronger-than-anticipated S&P Global Ratings-adjusted debt to EBITDA of about 0.6x in 2021 and 0.8x in 2022.
- However, Metsa Board's financial policy continues to allow for a substantial increase in leverage, and our assessment of Metsa Group's group credit profile remains unchanged at 'bbb-'. In our view, both factors weigh on Metsa Board's creditworthiness.
- We are therefore affirming our 'BBB-/A-3' ratings on Metsa Board Corp. and our 'BBB-' rating on its senior unsecured notes.
- The stable outlook reflects our expectation that Metsa Board's leading market positions in Europe support a weighted-average adjusted leverage of below 2x over the next 24 months.

Rating Action Rationale

We expect Metsa Board will report modest revenue growth and lower S&P Global Ratings-adjusted EBITDA margins in 2021. Given the company's high exposure to stable end markets such as food and pharmaceuticals, we expect that demand will stay resilient. We forecast higher average paperboard and pulp selling prices that should drive revenue growth of about 3% in 2021. However, we anticipate headwinds from pulp, energy, logistics costs and foreign currency movements will weigh on profitability. In addition, the company will not receive any dividend from Metsa Fibre this year. We expect this to result in S&P Global Ratings-adjusted EBITDA margins of 14.0%-14.5% in 2021, down from 17.6% in 2020. That said, the margins are likely to recover to about 16% in 2022, supported by the renewed dividends from Metsa Fibre and higher paperboard selling prices.

Credit metrics improved due to the Husum transaction, despite a substantial investment pipeline. Metsa Board sold its 30% stake in the Husum pulp mill for €260 million in January 2021. Since the company left all proceeds on its balance sheet, there will be a resulting reduction of reported net debt for the same amount as of first-quarter 2021. We expect Metsa Board will use the funds to finance the expansion of its paperboard operations over the coming three years. In the medium term, we expect free operating cash flow (FOCF) will be constrained by significant expansionary and renewal investments, including those related to the first phase of the Husum pulp mill renewal. Positively, however, we forecast S&P Global Rating-adjusted debt to EBITDA to remain low at about 0.6x in 2021 and 0.8x in 2022.

That said, the group's publicly stated maximum leverage target allows for a material increase in leverage. Metsa Board's current credit metrics remain in line with our view of a minimal financial risk profile. However, the group's financial policy specifies a maximum net reported debt-to-comparable EBITDA ratio of 2.5x (corresponding to 2.5x-3.0x as adjusted by S&P Global Ratings). Although it is not factored into our base case for the coming two years, this financial policy allows Metsa Board to make further shareholder returns via dividends or share buybacks, or make large debt-funded investments. We therefore apply a one-notch negative financial policy modifier that results in a stand-alone credit profile of 'bbb-'. This indicates our belief that leverage could increase materially beyond our base-case assumption.

Our view of Metsa Group's creditworthiness remains unchanged at 'bbb-'. We continue to assess Metsa Board as a highly strategic subsidiary of Metsa Group, given the close integration and strong commitment of support from the parent. As a result, our rating on Metsa Board is capped by Metsa Group's group credit profile. The latter is supported by the group's low leverage and high product diversification, partly offset by its exposure to the volatile sawn timber and pulp segments. Our assessment is constrained, though, by Metsa Group's maximum leverage tolerance (minimum equity ratio of 40%), which gives it significant headroom to increase leverage beyond current levels. We believe that large investment plans at Metsa Board, Metsa Fibre, and Metsa Tissue may weigh on the group-level credit metrics over 2021-2023, but they will remain consistent with a minimal financial risk profile, in our view.

Outlook

The stable outlook reflects our expectation that Metsa Board's leading market positions in Europe support a weighted-average S&P Global Ratings adjusted leverage of below 2x over the next 24 months.

Downside scenario

We could lower the rating if we no longer anticipated that Metsa Board could maintain S&P Global Ratings-adjusted debt to EBITDA below 2.0x on a weighted average basis over a sustained period. This could happen if Metsa Board's operational performance weakened, for example due to a significant fall in paperboard prices, a material increase in wood prices or if operational issues led to margin pressures.

Furthermore, we could downgrade Metsa Board if we revised Metsa Group's group credit profile to 'bb+' or lower.

Upside scenario

We view an upgrade as unlikely, since it would require Metsa Board to publicly commit to a more conservative financial policy that includes a cap on S&P Global Ratings-adjusted debt to EBITDA of 1.5x. Additionally, we would expect S&P Global Ratings-adjusted funds from operations (FFO) to debt to exceed 60% on a sustainable basis for an upgrade.

Raising the rating would also depend on us revising Metsa Group's group credit profile to 'bbb' or higher. This could occur if we saw only a low risk of leverage increasing from current levels--for example, through major new investments--and our current assessment of the business risk profile remained unchanged.

Company Description

Metsa Board is a Finland-based paperboard and pulp producer. The group produces folding boxboards (59% of sales), white kraftliners (25%), and market pulp (12%), among other operations (5%). The company's paperboards are ultimately used in packaging applications in the consumer goods, retail, and food service industries. The group generated €1.9 billion sales and €332 million adjusted EBITDA in 2020. Around 68% of revenue was generated in Europe, the Middle East, and Africa, while the remainder stemmed from the Americas (23%) and Asia-Pacific (9%). The group has eight mills (in Finland and Sweden) and approximately 2,370 employees, and it is listed on the Nasdaq Helsinki.

Our Base-Case Scenario

S&P Global Ratings believes there remains high, albeit moderating, uncertainty about the evolution of the coronavirus pandemic and its economic effects. Vaccine production is ramping up and rollouts are gathering pace around the world. Widespread immunization, which will help pave the way for a return to more normal levels of social and economic activity, looks to be achievable by most developed economies by the end of the third quarter. However, some emerging markets may only be able to achieve widespread immunization by year-end or later. We use these assumptions about vaccine timing in assessing the economic and credit implications associated with the pandemic (see our research here: www.spglobal.com/ratings). As the situation evolves, we will update our assumptions and estimates accordingly.

Assumptions

- Real GDP growth in the eurozone of 4.8% in 2021 and 3.9% in 2022, after a 7.2% contraction in 2020 due to the COVID-19 pandemic.
- Revenue growth of about 3% in 2021 and 2% in 2022, primarily driven by higher paperboard selling prices.
- S&P Global Ratings-adjusted EBITDA margin to decline to 14.0%-14.5% in 2021 (from 17.6% in 2020), as higher paperboard prices are more than offset by adverse foreign currency movements, higher pulp, and energy and logistics costs. In addition, we do not expect Metsa Board to receive dividends from Metsa Fibre in 2021. In 2022, we expect a recovery in adjusted EBITDA margins to about 16%, driven mainly by higher paperboard prices and dividends from Metsa Fibre.
- Capex of €250 million annually in 2021 and 2022, reflecting significant investments related to the first phase of the Husum pulp mill renewal and paperboard expansion projects.
- Working capital outflows of €40 million in 2021 and €20 million in 2022.
- No dividend from Metsa Fibre in 2021, followed by €20 million in dividends from Metsa Fibre in 2022.

- Annual dividends of about €92 million in 2021 and 2022.
- No acquisitions.

Key metrics

- Debt to EBITDA of 0.6x in 2021 and 0.8x in 2022, after 0.7x in 2020.
- FFO to debt above 100% in both 2021 and 2022, after 112% in 2020.

Liquidity

We assess Metsa Board's liquidity as strong and believe that the company's liquidity sources will comfortably cover liquidity uses by over 1.5x in the 12 months started Jan. 1, 2021, and over 1.0x in the subsequent 12 months. The company has a long-dated debt maturity profile, access to numerous funding sources, well-established relationship with banks, and a satisfactory standing in the credit markets.

Principal liquidity sources over the 12 months started Jan. 1, 2021, include:

- About €214 million cash and cash equivalents as of Dec. 31, 2020. This includes around €205 million of short-term deposits with Metsa Group Treasury, under a cash-pooling arrangement. We understand that Metsa Board has access to these funds at short notice.
- Fully available €200 million revolving credit facility (RCF; maturing in 2026).
- Committed bank loan facilities of €192 million (maturing 2028-2030).
- Access to loans from pension funds of about €212 million.
- Cash FFO of about €220 million in 2021.
- Proceeds of about €260 million from the saale of a stake in the Husum pulp mill, which was completed in January 2021.

Principal liquidity uses over the same period include:

- Capex of about €250 million.
- Dividend (including capital distribution) of about €92 million.
- Working capital outflows of about €40 million, in addition to intra-year working capital needs of around €20 million.

Issue Ratings--Subordination Risk Analysis

Capital structure

As of Dec. 31, 2020, Metsa Board's debt comprised €250 million of senior unsecured notes due in 2027, a €150 million senior unsecured syndicated term loan due 2026, and €33 million of bilateral bank loans, all of them issued by Metsa Board Oyj.

Analytical conclusions

The €250 million senior unsecured fixed-rate notes due 2027 issued by Metsa Board Corp. are rated 'BBB-', the same as the issuer credit rating, as no sources of significant subordination have been identified.

Ratings Score Snapshot

Issuer Credit Rating: BBB-/Stable/A-3

Business risk: Fair

- Country risk: Low
- Industry risk: Moderately high
- Competitive position: Fair

Financial risk: Minimal

- Cash flow/Leverage: Minimal

Anchor: bbb

Modifiers

- Diversification/Portfolio effect: Neutral (no impact)
- Capital structure: Neutral (no impact)
- Liquidity: Strong (no impact)
- Financial policy: Negative (-1 notch)
- Management and governance: Satisfactory (no impact)
- Comparable rating analysis: Neutral (no impact)

Stand-alone credit profile: bbb-

- Group credit profile: bbb-
- Entity status within group: Highly strategic (no impact)

Related Criteria

- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Methodology For Linking Long-Term And Short-Term Ratings, April 7, 2017
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014

- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

Ratings Affirmed	
Metsa Board Corp.	
Issuer Credit Rating	BBB-/Stable/A-3
Senior Unsecured	BBB-

Certain terms used in this report, particularly certain adjectives used to express our view on rating relevant factors, have specific meanings ascribed to them in our criteria, and should therefore be read in conjunction with such criteria. Please see Ratings Criteria at www.standardandpoors.com for further information. A description of each of S&P Global Ratings' rating categories is contained in "S&P Global Ratings Definitions" at https://www.standardandpoors.com/en_US/web/guest/article/-/view/sourceId/504352 Complete ratings information is available to subscribers of RatingsDirect at www.capitaliq.com. All ratings affected by this rating action can be found on S&P Global Ratings' public website at www.standardandpoors.com. Use the Ratings search box located in the left column. Alternatively, call one of the following S&P Global Ratings numbers: Client Support Europe (44) 20-7176-7176; London Press Office (44) 20-7176-3605; Paris (33) 1-4420-6708; Frankfurt (49) 69-33-999-225; Stockholm (46) 8-440-5914; or Moscow 7 (495) 783-4009.

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