

Metsä Board Half-year financial report January-June 2019

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Mika Joukio:

Good afternoon everyone, and welcome to Metsä Board's results update for the first half of the year. My name is Mika Joukio, and I am the CEO of Metsä Board.

Together here with me I have our CFO Jussi Noponen and Head of the Investor relations, Kati Sundström. As usual, I will first go through the presentation, and after that, we will be happy to answer your questions.

First, the second quarter 2019 in summary.

In folding boxboards, the demand has been good and average selling prices have increased year-on-year.

In white kraftliners, the market situation has been clearly softer. After the very strong first half of 2018, demand - especially in Europe - has declined. This has been evident also in our delivery volumes. In addition, during the second quarter, the average price in kraftliner sales decreased a bit, which was mainly caused by changes in our sales mix.

The pulp market has continued to weaken, both in Europe and China, and this had a big negative impact on our Q2 results. I will return to this later.

As always, our second quarter was loaded with annual maintenance work especially at our mills in Finland. This had roughly 7 million euros negative impact on our operating result compared to the first quarter, which was almost a maintenance-free quarter.

So, all in all, the negative EBIT delta of roughly 20 million euros in the second quarter compared to the first quarter was almost totally due to the weakened pulp market and the annual maintenance works.

The big news during the quarter were our investment plans and those of our associated company Metsä Fibre. Starting with the latter, Metsä Fibre is planning to build a new bioproduct mill with an annual pulp capacity of 1.5 million tonnes in Kemi, Finland, to replace the existing pulp mill. In addition, they plan to build a new pine sawmill with an annual capacity of 750,000 cubic metres in Rauma, Finland. The total investment value of these two projects would be approximately 1.7 billion euros.

Then to Metsä Board. We are planning to renew our pulp mill at Husum integrated mill in Sweden. The current pulp mill is old, and we have had several technical problems with it

Metsä Board Half-year report January-June 2019 during the past few years that have burdened our profitability. Instead of keeping the pulp mill running with higher maintenance costs, we are confident that the renewal is the best alternative to secure pulp production in Husum mill in the future. I will return to this at the end of this presentation.

Then to the quarterly paperboard delivery volumes.

In the second quarter, the volumes were slightly up from the first quarter, but down by 9 per cent compared to the corresponding quarter last year. However, during the first half of 2018, and especially in the second quarter, the demand for both folding boxboard and white kraftliners was really strong. So, despite the fairly big decline from last year, this year's volumes have been on a good level.

Then a closer look at the delivery split in the first half of the year compared to the corresponding period last year.

In folding boxboard, the changes are quite small – In Americas, we have continued our actions to improve the sales mix, meaning that we emphasize profitability over volumes. Our actions have paid off, and our average selling price in FBB has improved by more than 100 euros per tonne in that area within a year.

In white kraftliners, our deliveries have developed nicely in Americas. However, the declined demand in the EMEA-area can be seen in our delivery volumes. For this reason, we have adjusted the production levels of our coated white kraftliners to better meet demand.

Then the sales and operating result.

January–June 2019 sales amounted to 964 million euros, 5 per cent lower compared to the corresponding period in 2018. The decrease was due to declined sales in market pulp and white kraftliners. Profitability in the first half was also weaker – the operating margin was at 10.7 per cent, compared to 12.7 per cent in the first half of 2018.

Let's take a closer look at the items which particularly impacted profitability.

As already said earlier, the Q2 operating result was mainly impaired by weakened pulp prices and more maintenance compared to the first quarter. Small positive items were the improved average prices of FBB and slightly smaller energy costs.

Then in the review period, from January to June, the operating result was 103 million euros, which was 25 million euros less compared to the corresponding period in 2018.

Starting from the positive items, we had clearly higher average selling prices in paperboard, and in FBB in particular. Also, the impacts from FX were favourable to us - resulting to 21 million euros positive impact year-on-year.

Then to the negatives. The largest single item impairing our profitability was the weakened pulp market. Both the delivery volumes and price levels for market pulp decreased year-on-year. Our share from Metsä Fibre's result was 19 million euros smaller compared to the first half of 2018. Also, the production costs for both paperboard and pulp were clearly higher. In 2018, cost inflation was fast and especially the wood prices increased. In addition, the decreased paperboard delivery volumes had a negative impact on the first half results.

The global pulp market has continued to be under pressure. A small recovery was seen in the first quarter of this year – especially in China, but in the second quarter, the market situation weakened again. In Europe, pulp prices have been sliding throughout the whole year. The PIX price for long-fibre pulp is over 200 dollars per tonne cheaper than it was at the beginning of the year.

The second and the third quarter includes a lot of annual maintenance shutdowns, which will decrease pulp supply to some extent. Also, some producers have announced production curtailments. However, many of these have already materialized. The weakened pulp prices will continue to burden our profitability at least in Q3.

Then to production costs.

In the first half of the year, our profitability was still burdened by higher wood costs compared to the corresponding period last year. Wood costs have remained at a high level, and we don't expect to see any major changes in the coming months.

In the second quarter, the costs remained at a high level, however, we saw slightly lower energy costs compared to the first quarter

January-June cash flow from operations amounted to 67 million euros. During 2019, working capital has increased due to increased inventories and trade receivables.

Investments in the first half of 2019 were 24 million euros.

Our net debt increased from the previous quarter, and was 380 million euros. The increase was mainly due to the dividend payment, 103 million euros. Leverage was at 1.2x, so well below the targeted maximum level.

Then an update of our ongoing pre-engineering phase of Husum's pulp mill investment or renewal.

At the moment, we are waiting for the Swedish authorities to make a decision on the environmental permit for the renewed pulp mill. We expect to get more information on this during August.

When the environmental permit is confirmed, we will finalize the competitive tendering for the main equipment. We estimate that the final investment decision for the first phase of the investment could be made in the fourth quarter of this year, at the earliest.

Earlier today, we launched our new sustainability targets for 2030, and here is a summary of selected highlights.

Our main target is to achieve fossil-free mills by 2030 with zero fossil CO₂ emissions. This ambitious target includes both emissions from our own energy production as well as those from purchased energy. Currently, 82% of the energy consumption at Metsä Board mills is free from fossil CO₂ emissions.

These new targets demonstrate our commitment to mitigate climate change supporting the UN Sustainable Development Goals. The renewal of Husum pulp mill will take us one step closer to this ambitious target.

Then news from our R&D and innovation work, which are both strongly based on sustainability.

Our recently renewed and improved FBB portfolio answers to increasing demands for sustainability, product safety and brand promotion. Our light and high-quality paperboards help customers save resources and reduce their own carbon footprint.

Our eco-barrier products replacing the plastic materials, have been well received by the markets and we continue our R&D work with this.

Then in June, we announced that we will establish an R&D excellence centre in Äänekoski to boost the development of new paperboard and packaging solutions of the future. I am very excited about this new centre, where we will be able to organise packaging design workshops and innovation days together with our customers and partners in order to demonstrate the full potential of our lightweight, fresh fibre paperboards.

And how do we see the near-term outlook

We expect our Q3 paperboard delivery volumes to remain roughly at the Q2 level.

We see good demand and stable pricing for Folding boxboards to continue, but for white kraftliners the outlook is more mixed. On the other hand, we see demand gradually picking up and our order books to improve, but at the same time we can't rule out the possibility of further decreases in average selling prices.

Throughout 2019, we have seen pulp prices to weaken, and this will have a clear negative impact on our results in the coming months.

The Q3 annual maintenance shutdowns will take place in Kemi integrate mill and partly in also Husum integrate mill. The rest of Husum's maintenance work will then take place at the beginning of Q4.

All in all, the negative impact from the maintenance is around 5 million euros higher in Q3 compared to Q2. And we expect the production costs and FX impacts to be fairly flat in Q3 compared to Q2.

Based on these assumptions, we expect that our comparable operating result for the third quarter will weaken compared to the second quarter.

And to summarize:

The outlook for our end products is somewhat mixed:

In folding boxboard, we see good market situation continuing but in white kraftliners, the demand looks stable, yet at a clearly lower level compared to last year. And there is still pressure in pricing.

The global pulp market will remain uncertain in the second half of 2019.

Based on our new sustainability targets, all our mills are fossil free by 2030. We think this is a very ambitious target and naturally it means actions and investments in order to fulfil it.

The renewal of Husum pulp mill would take us closer to this target.

So, this was the presentation part from my side, and now, we are ready for your questions, please.

Operator: Ladies and gentlemen, if you would like to ask a question, please signal by pressing star one on your telephone keypad. If you're using a speakerphone, please make sure your mute function is turned off to allow your signal to reach our equipment. As again, star one to ask a question. We will pause for just a moment to allow everyone an opportunity to signal for questions. And we take our first question from Linus Larsson from SEB. Please go ahead.

Linus Larsson: Thank you very much and good day to everyone. If I may start with the question of dividend, your policy is based on net earnings and it seems now pretty clear that 2019 is very likely to be weaker than 2018 in terms of net profit. So, I just wonder if you could spend a minute or two on the prospects for dividend and not least given your Capex plans ahead, and if you could provide us with any sort of reassurance on your dividends going forward please?

Mika Joukio: Okay Mika Joukio here, so our dividend policy is clear, so 50% of the net result and that has been this year policy, and no reason to believe that it would be something else next year at this stage. And if you think about our EPS, during the first half of this year, it's pretty much at the same level as last year. So I can't tell much more about that.

Linus Larsson: And do you think your Capex plans even though your target is based on a net profit payout, does it have implications?

Mika Joukio: Too early to say at this point.

Linus Larsson: Okay. Thank you. And then regarding Metsä Fibre clearly, you've seen a weakness in terms of pulp pricing, but also it appears Metsä Board's pulp shipments came down quite a lot actually even if regardless, if you look sequentially or year-on-year, is there something that we should know about that anything that any bounce back that we should expect in the third quarter.

And also in connection to this, if you could maybe update us on the ramp-up at Äänekoski, how far is that? Is there more ramp-up ahead and maybe also in terms of ramp-up if you could just briefly touch upon the folding boxboard ramp-up schedule at Husum? Thank you.

Mika Joukio: Okay first, I think from folding boxboard in Husum, so it's the board machine is running pretty much as targeted. So it's running full and then production is at a good level, so quite okay. Concerning then this pulp situation of course, the volumes were lower, and that clearly had a negative impact on our result in Q2. And at the moment we see that the price development in China it has been quite dramatic drop, more than 30% decline, and now it seems that the prices have stabilized, but remains to be seen what will happen then in Q3 and in coming months.

As far as Europe is concerned, still the price gap between Europe and China is quite high. So let's see what will happen here, but there is certain pressure in pulp prices in Europe. As far as Äänekoski pulp mill is concerned, it's running as targeted and as planned in the investment, so nothing special there.

Linus Larsson: Right, but how much is there still to go in the Äänekoski ramp-up, or is it complete by now?

Mika Joukio: Of course, I can't remember by heart the exact figures, but as I said it's really months as we originally targeted. So no dramatic changes.

Linus Larsson: Okay and that depart anything else to note regarding the weakened pulp shipments at Metsä Fibre in the second quarter. Did Metsä Fibre take market-related downtime for instance?

Mika Joukio: No, not at all.

Linus Larsson: Okay, thank you.

Operator: We take our next question from Gustaf Schwerin from Pareto Securities. Please go ahead.

Gustaf Schwerin: Hi, thanks for taking my questions. Firstly, on the demand side for white kraftliner, you said that it's quite stable still. But sometime, measured this negative mix effect, can you elaborate on that a little bit on this, is it just that you're setting less coated volumes. And then perhaps related to that as well, how much are you looking at curtailing production here and also if there's anything on the expected price drop quarter-on-quarter for Q3 at this moment? Thank you.

Mika Joukio: So in linerboards, of course, the demand has been lower during this year than last year. Of course, we need to remember that last year was very, very hot, so to say the first half of last year, especially Q2 was really, really hot. And at the moment the order books have improved slightly comparing to the situation few months ago, but still there are some uncertainty in linerboard side, and the curtailments there, they are not remarkable. Both in Husum and Kemi we are running pretty much as normal.

Gustaf Schwerin: Just a follow-up on that perhaps a bit then just to understand the mix effect as we're seeing maybe the larger price drops in for example testliner or uncoated or unbleached kraftliners. I mean, do you see that this is just relay a substitution effect that you have to provide a lower quality grade in order to compete with those?

Mika Joukio: Yeah, so we are the biggest producer of white kraftliners in Europe, and of course, I mean we -- how would I say, we act responsibly at the market, and we don't see any dramatic drop in prices during Q3. Maybe some influence on the price mix or customer mix, but nothing dramatic.

Gustaf Schwerin: Okay and then last one for me on your wood cost, you mentioned that you see stable cost for Q3. When do you foresee that we will see some lower cost for wood is that by the end of 2019 or we have to look further ahead?

Mika Joukio: Now, that is very difficult to speculate. What we see is that if you compare to Q3 and Q2, the production costs will be relatively stable, so no major changes there. But what will happen then at the end of this year or early next year that's -- I don't have competence to look at that crystal ball.

Gustaf Schwerin: What I mean the reason for you not seeing lower costs in Q3 is that, not only a lag effect or are you simply not seeing lower input cost for wood?

Mika Joukio: So we are saying that the production cost will be stable in Q3 comparing Q2.

Gustaf Schwerin: Okay, thank you.

Operator: We take our next question from Mikael Doepel, UBS. Please go ahead.

Mikael Doepel: Thank you. Good afternoon everybody. A couple of questions here, firstly with regards to the folding boxboard volumes in the US. Now looking at the first half, it seems as if volumes are down a bit in the US, which is to me maybe even a bit surprising given your ambitions to grow your presence in that markets. Maybe you could start by talking a little bit of what's happening in the US right now and how you are performing there?

Mika Joukio: Yeah, so what we already mentioned in Capital Markets Day last year, so now, we're really focused on profitability. And we have significantly been able to improve the price mix, customer mix, sales mix in the Americas market, so that the average prices have increased roughly 100 euros per ton that is a remarkable increase.

And of course, we have then I mean, lost some customers, but that has been pretty much by papers, that I mean if they're not ready to pay the decent price for a good product then we don't continue with them. And of course, we are targeting and searching new customers, and our original target about 300,000 tons a year is still intact, no reason to change that. But now we have been very strong and determined concerning the price mix in improvement in that market. Demand is good.

Mikael Doepel: Okay. But then on Husum and the bulk investment there and on Capex overall, you think about the Capex for 2019/2020, what should we -- how, what kind of the Capex level should we assume for these years if we take into consideration the Husum pulp investment?

Mika Joukio: You mean this year?

Mikael Doepel: This year, and 2020, if you can say anything about that?

Mika Joukio: So at the moment, our estimation is still this 300 million as we have said roughly 300 remains to be seen. Of course, then we know more when we have studied more about this case. And then depending on when we are able to make the decision so then it's of course, some money will be used already this year, but I can't say precise figures at the moment, but anyway this 300 million or whatever is the final sum that that will be for 2019/2020 and 2021. Even some part of 2022, so three or four years.

Mikael Doepel: Okay, and as I understand that this is mainly a replacement investment, is there any earnings benefit you expect to get out of this?

Mika Joukio: Yeah, it's mainly replacement investment, of course, we probably are able to improve our energy generation, and then of course the less disturbances in power production means slightly higher power production, but we come back to these figures when we have the final decision in hand. But this is pretty much replacement investment.

Mikael Doepel: Yeah. And a final question on FX. You had a, I think you mentioned a year-over-year positive impact in the first half of about 21 million euros also on a net basis in operating profit. Assuming current spot rates, what would you expect to see in the second half of the year on a year-over-year basis?

Mika Joukio: You mean what would we expect of FX?

Mikael Doepel: That's correct.

Mika Joukio: Maybe Mr. Jussi Noponen can look at the crystal ball.

Jussi Noponen: Yes, we are hedging on a rolling basis for roughly the next six months. The remaining months of this year have been hedged already, and we are guiding flat FX impact Q3 on Q2, and also for the fourth quarter, you should not expect any massive impacts from FX.

Mikael Doepel: All right, thank you very much.

Operator: We take our next question from Robin Santavirta from Carnegie. Please go ahead.

Robin Santavirta: Thank you. So to start with regarding the delivery volumes now you seem to be very happy – or quite happy with the performance in Q2 and I state that demand is good in folding boxboard and stable in white kraftliners, yet when I look at the numbers, I see paperboard deliveries declined by 9% year-on-year and 7% compared to Q2 '17, so quite significant declines also compared to deliveries in Q2 17. What is explaining this? I would assume for the folding boxboards and also in white kraftliners. The end demand or usage of these products are probably not declining in the same rate. Are your clients adjusting inventories? Are you losing market share or what is going on?

Mika Joukio: Yeah. We must remember, and we have stated several times last year, first-half and especially Q2 was super-hot. I mean, the demand was really not normal. Now, it's pretty much normalized the situation and that is simply the case. We need to, of course,

remember that in Q3 the demand last year was slightly lower than Q2, or clearly lower than Q2, because then inventory levels went up both in linerboard as well as in folding boxboard and then that affected Q3 and partly Q4 also. So now we see that the market situation is quite normal.

Robin Santavirta: And do you see any destocking from your clients or is it restocking or could you talk a little bit about what you see, sort of, your clients doing in Europe and North America; do you have any visibility about this?

Mika Joukio: You mean at the moment?

Robin Santavirta: Exactly.

Mika Joukio: No. We see that it's quite – and demand is okay and we don't see this kind of destocking or other kind of stocking-related issues at the moment.

Robin Santavirta: Alright, thanks. Then if I take your Group earnings and then I deduct Metsä Fibre's earnings, then I end up probably with something which reflects mainly your paperboard business – a little bit pulp sales as well as something else. But then if I do this exercise, I can see reminding – remaining part of the business or Group earnings excluding Metsä Fibre are also down year-on-year, and also down compared to Q2 '17. So it seems as the paperboard business profitability, despite higher sales prices year-on-year, and certainly compared to Q2 '17, are higher, so still you're seeing the profitability is weaker in the paperboard business. Is this only due to the volume and the cost impact or is there something else, and how should we expect this also to continue to evolve?

Mika Joukio: I mean, you're quite right. So it's mainly volume-related and then also then, of course, the cost-related, so wood prices and also logistic costs especially in North America. So these other elements, even though we have been able to increase prices quite nicely during this year, but still that is the case, as you said. And the main reasons are those that I listed.

Robin Santavirta: Alright, thanks. And two questions still, if I may. Maybe for Jussi in terms of inventories it seems that you are reducing your inventory and driving up your earnings by that in a sense, at least technically your inventories are up almost 30% year-on-year. How do you plan to manage, sort of, working capital and inventories and what is driving up those inventories?

Jussi Nojonen: Yes. I can take this question. So the increase in inventory is two parts – volume and value. And there has been quite a lot of volume increase and it has been in pulp and in linerboard, not in folding boxboard. And we have been confident that the volumes will start moving going forward. And for that reason we have made the decision to increase the

inventory levels slightly. There is also the seasonal impacts. So every year in the first half working capital has increased and then decreased in the second half. So if the demand stays normal in the market, we could expect some release from working capital in the second half of the year.

Robin Santavirta: Alright. Good, thanks. And related to the maintenance stoppages and the earnings impact of those. I guess, you have talked about roughly 10 million euros in Q2, Q3 and Q4. But now, it seems that you have a little bit more in Q3 – you were commenting about 5 million euros up quarter-on-quarter in Q3. How should we look at Q4? If Husum is already started in September. Is Q4 a little bit lighter in terms of maintenance compared to Q3?

Mika Joukio: Yes. So Q3, as you said, so we have Kemi and then Husum maintenance shutdowns. And this year, Husum shutdown will start a little bit, a few days earlier than last year, for example, so it's more on the September side than October side, and that then effects on this plus 5 million euros as we said. Then concerning Q4 probably the maintenance costs will be a little bit lower, but it's a bit too early to say because – and it's up to then start-up of Husum mill after the investment – after the maintenance shutdown. But we don't have any other major shutdowns than this kind of tale from Husum.

Robin Santavirta: Alright, thanks. And if I just make one final, in terms of what was already touched upon, the dividend. I do realize and understand – your dividend policy is crystal clear. But still if you were sort of coming, you did not cut the dividend when you, sort of, had the cost ramping up Husum in 2016, even though your year declined is sort of – is there something else that can, sort of, impact the dividend which to, sort of, remain predictable or stable in terms of dividend? Or is it simply raw EPS and then a percent of that; or, how should we look at that?

Mika Joukio: Again, I think it's too early to say. But you are right by saying that it's not always been precisely 50%, it has been something else also. But I think we are now living in August still, so remains to be seen what will be the case.

Jussi Noponen: But what we can say is that the policy is the minimum of 50%.

Mika Joukio: Yeah.

Robin Santavirta: Thank you, Mika and Jussi.

Operator: Thank you. We take our next question from Markku Järvinen from Handelsbanken. Please go ahead.

Markku Järvinen: Yes. Good afternoon, just a few more questions from my side. Just basically regarding that production costs are stable, and volumes are stable, and lower prices for pulp and perhaps liner. And other costs should we just assume that the, sort of, only difference in cost is the 5 million euros maintenance issue or is there some seasonality in depreciation or fixed cost, otherwise?

Mika Joukio: No. It's pretty much this maintenance extra cost, so to say.

Markku Järvinen: So depreciation will remain at the Q1–Q2 level in Q3–Q4, and fixed cost is the same?

Jussi Noponen: It will be slightly lower in the second half than in the first half.

Mika Joukio: Yes.

Markku Järvinen: Okay. Good, good. And could you, sort of, at this stage comment on this folding boxboard pricing for next year? We've seen, sort of, pulp prices moving down, liner prices moving down. Is folding boxboard immune?

Jussi Noponen: Yeah. Again, it's too early. Of course, we will start during the autumn the annual negotiations and discussions concerning next year. But folding boxboard the prices are based on demand and supply and not on the pulp prices. So that is a bit different comparing to, for example, linerboard business. But at the moment, the market is good, demand is healthy, so let's see what we'll happen next year. But a little bit too early to say. Of course, we try our best and utmost to get positive development in that area also, but discussions and negotiations are just about to start.

Markku Järvinen: Very well. Thank you very much.

Operator: Once again, ladies and gentlemen, if you would like to ask a question, please press star one. We take our next question from Henri Parkkinen for OP Financial Group. Please go ahead.

Henri Parkkinen: Yes. Good day for everyone. I have one question about the North American market and your comment that through this sales mix optimization the average prices of folding boxboard has improved by around 100 euros per ton over the past year. Is this like-for-like figures? So, as we know, the Dollar has strengthened against the Euro during the last 12 months. And that if you have figures in U.S. dollar terms that would be very helpful.

Mika Joukio: It's pretty much – I mean, comparable. I don't have the exact Euro, sorry, USD prices here. But it's pretty much comparable.

Henri Parkkinen: Okay. Okay, very helpful. Thank you.

Operator: Thank you. It appears there are no further questions at this time. I would like to turn the conference back to our host for any additional or closing remarks.

Mika Joukio: Okay. Mika Joukio here. So thank you very much for good questions. And I wish you a nice afternoon and evening.