Essity Aktiebolag (publ)

Transcript
Half-year Report 2019
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Slide 1

Magnus Groth: Good morning, everyone. On this first front page is a picture of our recent launch event of Libresse V-Comfort in China. And we have the ambition of becoming the #1 e-commerce brand in the premium towel segment, a big investment for the future where we are very excited about growing our Personal Care business in China going forward.

Slide 2

Slide 3

Summary – Q2 2019 vs Q2 2018

Moving on to the numbers. We saw strong organic net sales growth with 3.9 percent, including lower mother reel sales in the quarter; and an adjusted EBITA margin that increased with 30 basis points to 11.6 percent.

And this came from better price/mix and higher volumes in all business areas, but this higher growth also comes with higher sales and marketing investments. And of course, the launch of Libresse V-Comfort is just one example of that, but still those investments are lower as percent of sales, important to note.

We continued to see strong contributions from cost savings. And something I'm sure we will discuss later is that we still have higher raw material and energy costs in this quarter even though we expect that to reverse going forward and a significant negative impact from stock revaluation due to lower raw material prices. And I'm sure we'll get back to that.

On a very positive note, we more than doubled our operating cash flow to SEK 3.7 billion. And we also had the highest earnings per share in a quarter, with SEK 3.24, that we have seen since Essity was founded a little bit over two years ago, which brings me to my next slide which actually shows a time series.

Slide 4 *Increased Sales and Profits*

And the reason why we put this slide is that we have discussed now almost since the birth of Essity when will we see the turning point that the headwinds from raw materials decline. And the benefits from price increases and cost savings and efficiency programs, when will we see the impact?

And based on this time series, I dare to say that we saw it now in the second quarter of 2019. Starting down in the left-hand corner, you can see the organic net sales development; and that for the last three quarters now we have had growth above our long-term target of 3 percent, with a nice development there 3.3 percent, 4.3 percent and now 3.9 percent in the quarter. So I think that's one indication.

Another indication is that – if you look down at the bottom to the right, adjusted EBITA margin, that we increased the EBITA margin to 11.6 percent, which is actually the highest margin since the last quarter of 2017. So a turning point there also resulting in, if you look at, the overall adjusted EBITA which came out at SEK 3.7 billion, which is the highest adjusted EBITA in absolute terms that we've seen since Essity was born.

Slide 5 *Net Sales - Q2 2019 vs Q2 2018*

Getting back then to the two bridges that we always present. It's positive that we see that the organic net sales comes from a good mix of price/mix and volume, and we see improved price/mix and volume in all business areas.

Slide 6 *Adjusted EBITA - Q2 2019 vs Q2 2018*

The adjusted EBITA bridge then looks a little bit different than we're used to: Very strong contributions from price/mix and volume also to adjusted EBITA; still negative impact from raw material and energy, as I already mentioned, with an impact of almost – negative impact of almost 1 percent in the quarter, but this will then change in the coming quarters.

Cost savings, COGS, this is where we are committed and planning to see annual savings of around SEK 1 billion per year. So SEK 175 million in the second quarter, which is then a little bit lower if you average the SEK 1 billion over four quarters, but we are very confident that we will be in the range of SEK 1 billion by the end of the year, which means that we expect to see higher cost savings in COGS in the second half of the year than in the first half of the year.

Moving then to the cost savings program: We have a separate slide on that. That's developing according to plan. And then finally the unusually high others, SEK 709 million negative, which consists of three parts of equal magnitude. The first one is higher sales and marketing costs, which is important for driving the growth in the company.

Still it's lower as a percentage of sales but, of course, growing at the rate that we've been growing now for three quarters. We need to fuel that with higher sales and marketing costs. The other big part, which accounts for about 1/3 of the other SEK 709 million, is stock revaluation. And stock revaluation is simply that, at the end of each quarter, we value our stocks and compare to the stocks we had at the beginning of the quarter.

And when you then compare that with the same difference last year, you arrive at a quite big number, and this is because raw materials increased quite dramatically in second quarter last year and are coming down throughout the end of the second quarter this year. And I'm sure you have questions about that I will get back to later.

And the third part and also accounting for about 1/3 of this other line is a mix of different other components. And we're just mentioning a few here: Somewhat lower profitability in the pulp mill that we still have integrated in Mannheim due to lower pulp prices; higher distribution costs, which has been a theme now for a number of quarters; and still some trade tariffs in the second quarter, which actually now went away.

So we will not see any negative trade tariffs that we know of, anyway, going forward, but we still have some impact there. And then some other smaller other costs. And then finally a positive impact from currency.

So just to reiterate. When it comes to the cost savings in COGS and the cost-saving program, we're fully committed to achieving a savings of around SEK 1 billion on COGS; and to our cost savings program, where we have a plan to have a run rate of SEK 900 million at the end of the year and savings in the P&L this year of around SEK 600 million.

Slide 7 *Raw Material Development*

Raw material development. And as we can see from this slide, it looks as if most of these lines are pointing down. This is very unpredictable, as you know. We expected pulp prices to come down a little bit in the middle of the year and then move up again.

This is still the case, but it, the fall, especially in pulp prices, has been quicker. And there's been a bigger fall than we expected, and now we expect that to last also for longer even though most market reports still show an increase in pulp prices towards the end of the year.

So in our usual prediction here for the next quarter, the third quarter of this year, starting then with the market pulp, which is very relevant for Consumer Tissue, we expect lower pulp prices quarter three over last year's quarter three and sequentially significantly lower pulp prices.

When it comes to paper for recycling, which impacts Professional Hygiene, we expect lower prices quarter over last year's quarter and sequentially stable prices because they have already come down quite significantly.

And finally then, oil-based raw materials, which is the main cost driver together with fluff pulp for Personal Care, where we expect stable prices quarter over last year's quarter and sequentially slightly lower raw material prices.

And when it comes to energy, we expect lower energy costs and prices both sequentially and quarter over last year's quarter. So that's our expectations for quarter three. So quite positive from that perspective. And then who knows going forward.

Slide 8 *Cost Savings – SEK 322m in Q2 2019*

Some more detail about the additional cost savings program and the regular COGS savings.

Starting with the regular COGS savings, SEK 175 million. Those are the savings that we see from Tissue Roadmap, from ongoing operational efficiency improvements, material rationalization and sourcing savings. And they are a bit lumpy.

In the first half of the year, we've actually been working intensely with Tissue Roadmap activities and – but also with some start-ups of machines in Inco and in Mexico a tissue machine and so on. And all of this has resulted in slightly lower COGS savings in the first half of the year, but again we expect that to improve in the second half.

And the cost savings program, very much according to plan, mostly impacting SG&A. And as I already mentioned, we expect to see the run rate of SEK 900 million that we have communicated by the end of the year.

And already at the end of Q2, we have annualized run rate savings of around SEK 690 million, so moving forward here. And the headcount reductions to date are about 744 positions out of 1,000, and as you can see to the right, this leads to a reduction of SG&A as a percent of sales even though we are also investing in this area for growth.

Slide 9 *Improving Everyday Life through Innovations*

Innovation, of course, the heart of what we do. And here are some examples: To the left, a complete relaunch of TENA in the health care part of our business. There's a new trademark. If you look at the TENA brand there, it looks – it's modernized, completely new packs, completely new products. And our ambition is to own the skin health territory in incontinence care.

So we're very excited about this launch. Cutimed, extending the assortment of our advanced wound care assortment. Libresse, I think I already mentioned the big launch that we did in the second quarter in China. And some examples of more everyday innovations, where we have upgraded our base assortment in tissue in Europe with additional layers, improved softness and some other features.

Slide 10 *Achievements Improving Well-being*

Adding to that, to give you some flavor of what we're doing in the business. And these are just some examples that we're quite proud of, starting out with the great growth we are seeing quarter after quarter after quarter in fem care, very much driven by innovation but also from great advertising actually. And we won 13 lions at the Cannes international advertising festival, which is the big annual event for advertisers.

This means not only that our advertising is great but also we can actually attract the best marketing teams to work for Essity going forward. Another achievement in the quarter is that we won a contract for the Changi Airport in Singapore, which means not only that they will install sensor-enabled dispensers in this new airport all over, but it's also then 1,000 dispensers in one deal, which is a lot of dispenser and of course a lot of paper to be filled and refilled in those.

And it shows the benefit of having these very advanced products that we are continuously developing now in Professional Hygiene. And finally, to the right, an example how we're working here in medical with the compression stocking for a little girl that needs this because she has a heart condition and how we are tailor-making these products for every size and also every design. And you can see the pink lacing there and some other features that, of course, is very important to make these products more attractive. So just some examples of how we are improving well-being every day in Essity that we're very proud of.

Slide 11 *Personal Care - Q2 2019 vs Q2 2018*

Moving over to the three specific business areas. Organic net sales in Personal Care increased with 3.1 percent, with most of that coming from emerging markets, 7.8 percent; and mature markets, 0.6 percent. We saw higher volumes, higher prices and cost savings in Personal Care, but this is actually the business area where we continue to see significant raw material and energy headwinds up to 190 basis points.

And this is, of course, fluff pulp. It's oil-based material, but it's also negative currency impacts. And in this area, as I already mentioned a number of times, we have invested in higher growth but lower as percentage of sales.

This is also a business where we have seen quite significantly higher distribution costs in the quarter. It's very important that we deliver on time and according to our agreed service levels with our customers, and this is leading to higher distribution costs.

Looking down at the bottom right-hand corner, by product segment, you can see that Incontinence Products is having another great growth quarter, 5.5 percent, growing in most areas. Medical solutions was weak, minus 2.2 percent. There are some specific reasons.

We are still working on the turnaround in the U.S. This will take another couple of quarters. We also had to some extent tough comps, the second quarter last year was the strongest of the year. And we also had fewer invoicing days. We typically don't talk about the invoicing days in Essity, but actually for our medical business it has a big impact.

And we had 1 less invoicing day this year than the second quarter last year. Baby Care, flat. We're focusing very much on margin improvement, so I think that's OK. And then continued excellent growth in Feminine Care both in Latin America and in Europe. So really continuing to develop in an excellent way.

Slide 12 *Consumer Tissue - Q2 2019 vs Q2 2018*

Moving over then to Consumer Tissue, where we also saw the best organic net sales in the quarter, 5.7 percent, with volume accounting for 2.7 percent, coming very much from emerging markets; and price/mix, coming from all parts of the business but primarily Europe and mature markets.

Again we have to remember this is the last quarter, but we still have a quite negative impact from closure of mother reel capacity. The negative impact this quarter was 70 basis points, but overall a very good development, higher prices; higher volumes; better mix; stable raw materials, which will then move to lower raw materials in the next quarter; and cost savings. And as you can see in the upper right-hand corner, an improvement with 160 basis points of margin here compared to a year ago, so big improvements.

This scenario where we have significant negative impact from stock revaluation due to lower raw material costs and higher energy costs, we still saw in the quarter. When it comes to raw materials and pricing, we have done all the price increases that we planned to do in wave two, so that's done and according to plan.

During the quarter, raw materials have moved down faster and more significantly than expected, so looking forward we are happy to stabilize pricing in the market for the next couple of quarters in preparation for the annual price negotiations while we follow the development of the pulp prices.

And how we move with prices going forward will be very much dependent on where pulp prices are a quarter or two from now, but right now we're very, very happy with what we've achieved in price increases and, of course, with the development of pulp prices.

Moving to the bottom right-hand corner. Western Europe, which is most of our mature markets, had a slight growth which is then mostly price, some mix, while emerging markets, we saw actually fantastic growth everywhere: 15 percent in Asia, 12 percent in Russia, 10 percent in Latin America. So – and this comes from price/mix and volume, very much volume also.

Slide 13 *Professional Hygiene - Q2 2019 vs Q2 2018*

Finally, Professional Hygiene, with organic net sales increasing 2.1 percent coming from both volume and price/mix. The highlight this quarter in Professional Hygiene is actually that North America turned to growth and had an accelerating growth throughout the quarter with both higher volumes but also the other improvements in prices and mix and cost savings.

And another business area where we have significant negative impact from stock revaluation. We saw higher energy costs in the quarter but actually slightly declining raw material costs already in this quarter.

When it comes to the adjusted EBITA margin, which was actually down 80 basis points from 14.1 percent to 13.3 percent year-over-year, this is mostly due to stock revaluation has the biggest impact here.

And down at the right-hand corner, you can see again that most of the growth is coming from emerging markets with price/mix and positive volumes, while in mature markets it's all coming from price and mix actually, with some variations. In North America we had positive volumes as well.

Slide 14 *Contributing to a Sustainable and Circular Society*

We work hard to stay at the forefront when it comes to contributing to a sustainable and circular society. And as you have seen, we've launched additional sustainability targets, especially for packaging and with a focus on plastics.

And if you have any questions, I'm happy to answer them, but we're really, I think, ambitious in this area. And as you know, also during the quarter, we announced an investment in sustainable alternative fiber technology in Mannheim, SEK 400 million.

Slide 15 *Summary - Q2 2019*

So to summarize. Strong organic net sales with 3.9 percent and an increased adjusted EBITA margin to 11.6 percent. Price increases have had a positive impact on both growth and profitability. Our investments in sales and marketing are contributing to higher growth.

We see a less-negative impact from raw material prices in the quarter even though they're still negative. Our efficiency efforts are according to our plans, and we continue to focus on innovations to strengthen our offering and improving our mix for the future.

Thank you for listening.

Slide 16 *Q&A*

Joséphine Edwall Björklund:
So with that, please, operator, help us to open up the lines so we can start the Q&A session.

Operator: Your first question comes from the line of Martin Melbye.

Martin Melbye, ABG Sundal Collier: Yes, good morning. You stated that stock revaluations were like SEK 230 million in Q2. What will that number be like in Q3 given that the pulp prices continue down?

Magnus Groth: I hand over to Fredrik. Please.

Fredrik Rystedt: It will remain on a high level. We don't give an exact number, but it will remain on a high level. This is basically a negative for this quarter in Q2, but of course, it was also a corresponding positive in Q2 of last year, as pulp prices and other material costs increased at that time.

And if we look at Q3, we can see that pulp prices have continued down. And we also saw in Q3 of last year that pulp prices went up at the time, so we have a similar situation. Exactly the amount will depend on the market development of pulp and other materials, but it will remain on a high level.

Martin Melbye: OK. And then you said, tissue prices, they will be stable in Q3 versus Q2, right?

Magnus Groth: We have most of the price increases in the second quarter. We continue in Europe. We're through wave two. We will continue, as we see fit, to adjust prices and increase prices in other markets, depending then on inflation and specific cost developments in those markets. So there could be some more price increases, but the big wave two initiative, primarily in Europe, has come to an end and we're very happy with the outcome. It's according to our plans.

Martin Melbye: Thank you, that is all for me.

Operator: Next question comes from the line of Faham Baig.

Faham Baig, Credit Suisse: I'm going to come back to the other line and stock revaluation. If we could get a bit more clarity on this, it would be helpful because I think at the Q1 stage the similar number was SEK 350 million. And that was seen as abnormally high levels and for – to fall from then, but this time around we're seeing over SEK 700 million.

Now if the stock revaluation is around SEK 230 million – I'm just trying to understand the delta from the SEK 350 million to SEK 700 million. So let's say the stock revaluation, I don't know, is SEK 50 million to SEK 80 million higher than Q1. Then what explains the difference in the other line versus Q1? That's my first question.

And secondly, going back to Consumer Tissue in developed markets, which is largely Western Europe. Number one, the pricing decrease sequentially, for me, was slightly more than I thought it should have been. Is that largely due to you having to pull back on some of the prices taken in Q1, or is there something else? Could you just go into a bit more detail there, please?

Fredrik Rystedt: I can start with the stock revaluation. I guess you will come back to the price issue, Magnus, but first of all, it's kind of complicated when you call a line other because it's really not other. It's everything else than what we have in volume and price and mix and raw material and savings. So it's everything that's in there.

So other is just our way of lumping a lot of stuff together, so of course the analysis is much deeper, which is exactly your point. What is it that actually has increased? So let me try and take you through that a little bit. First of all, when we look at this in normal circumstances, as we grow and as we pick up more sales and marketing expense, you'll see exactly that happening in – coming into the line other.

One other very typical line that you also will see being related to the other line and also to growth is when we, for instance, invest into a new plant, as an example. You build a plant and you acquire costs to do exactly that, to run that plant, but you don't initially have the volume.

Of course, that difference when we expand capacity, as we for instance have done in incontinence where we most commonly do also in China, you would see an underabsorption coming in that line. These are just examples. And then we have this line stock revaluation.

And you can say stock revaluation is in – to the absolute majority is, of course, materials, so it's we could actually put that stock revaluation to material, but the reason we separated, Faham, is basically that this is forward looking. So what we do, we purchase material, and as raw material prices either increase or decrease, that will basically be revalued.

And we do that at the end of the quarter. So inherently if you have a very negative, as we have in this case, stock revaluation in a specific quarter, that is actually, you could argue, positive for the future because that basically suggests that you have a lower input cost factor.

So with that background. It's basically a lot of different things. And then you may have other things like, in this particular case, because also of falling raw material prices, we have a lower result from the pulp mill. These are just examples, as I mentioned. We have also, Magnus mentioned, I think, tariffs and other things. So it is complicated because there are, of course, a lot of moving parts, all of them into others.

So let me just allude to exactly where that difference comes from. First of all, we do spend more on sales and marketing than we anticipated at the end of Q1. That's clear. And I think we have talked a little bit about the very, very low underlying costs that we had in Q4 of last year and Q1.

So – of course, the cost-saving program is part of the story, but we also took costs down for things like consultants and travelling and all sorts of things. They're still on low level, but as we said, in Q1 and Q4, we had a very, very sharp decrease. And we're back now more to normalized levels. As we said, it would be difficult to sustain that kind of level. So that's part of the story more going back to normal.

And in addition, as Magnus alluded to, we have spent some additional funds relating to growth primarily in Asia and in Latin America. And you can see the growth for both of these areas being very, very high. So this is a big, big part. Stock revaluation, to your point, is a little bit higher or a lot higher actually than we saw in Q1. And of course, this is inherently just the same thing.

We have an accelerating decline of raw material and correspondingly last year. Now in a world where raw material is absolutely flat you will see zero there. So once again this is moving parts depending on the development. And then the other parts being tariffs, and this is predominantly between U.S. and Canada, that we have and that will go away in coming quarters, and we have some other tariffs that's on that line, but largely it's something that will go away.

And then the pulp mill and some other issues. So these are perfectly explainable. It's just very difficult to explain every single line, so we have chosen to put it in others and just make examples like this. So it's not unnormal and it's not bad performance. It's just a result of the things we actively do plus external things like raw material changes and distribution costs.

So that was a long answer, Faham, but it's good perhaps to explain it.

Faham Baig: That was helpful. Can I just have two follow-ups on that, please? Number one, I know historically we've spoken about rebates and how it's helped the other line. Are we now seeing a negative impact from that as pulp prices fall down? First question.

And second follow-up would be it becomes – because there are so many moving parts in there, it becomes very difficult to forecast going forward. Are you able to give us any help how we think, how we should think about this particular line going into the second half?

Fredrik Rystedt: Yes, I can try and do that. First of all, rebates is typically not in other. That's in the cost savings in COGS. So it's impacting. And as we've said in previous quarters, it's a little bit on lower levels, and that remains the case. So of course, that's impacting but not this other line.

When you look at the stock revaluations or if you take the other line in general, I alluded to before we expect sales, marketing costs and growth to continue to be high. We expect stock revaluation to also be high, and the pulp mill, et cetera.

It's really difficult to forecast exactly, but it will remain on a high level given what we now can estimate relating to the raw material and distribution costs. Tariffs will go away to some extent. So there are moving parts.

Magnus Groth: OK. Should I continue with Consumer Tissue pricing, which was your second question? And I guess the difference compared to what we said and expected in the first quarter and also after the fourth quarter is that mostly pulp prices actually have moved but also, to some extent, that the recycled fiber prices have moved down quicker than we had expected, which has this big impact on other through stock revaluation.

Of course, the very positive part is that over time we will have lower costs, which helps our P&L. So I mean it's negative on the other line, but overall it's positive, and so it's an indicator of a positive development going forward. And this also is important for our pricing strategy going forward.

And as I mentioned, we are very happy with the pricing that we have achieved in Western Europe, and it's completely according to plan. And if you look back 1.5 years, two years, we've improved prices actually with over 5 percent.

And we still have slightly higher pulp prices in the second quarter, but they are moving down.

And in some cases, we actually did three price increases in a year, which also has led to higher shelf prices all through Europe, the price increases that have been put in place. So we see higher shelf prices on our products in tissue all over Europe compared to a year ago.

So that's really having an impact, but now with the faster-than-expected decline in pulp prices, we just have to see where this ends up. But of course, that decline is positive for our margin going forward.

And then there might be a mix issue here in your expectations because a lot of the growth comes from emerging markets, where we on average have slightly lower margins than in mature markets. So of course, that impacts the margin development in Consumer Tissue to some extent. So I hope that answers your question.

Faham Baig: Thanks.

Operator: Next question comes from the line of Iain Simpson.

Iain Simpson, Barclays: Two questions, if I may. Firstly, on pricing, have you taken any incremental pricing thus far this year? Or should we expect your pricing to go to zero by year-end as you annualize last year's pricing?

And then secondly, on that step-up in sales and marketing costs, you flagged that Q4 and then Q1 had very low sales and marketing expenditure. Is your sales and marketing now at a level where you feel that you're supporting your brands adequately, or could we perhaps expect a further step-up in coming quarters?

Magnus Groth: So the first question. We have continued to raise prices also in the first half of this year, so there will be some positive impact also going forward. And so we actually finalized wave two during the third quarter – or during the second quarter, excuse me.

And then when it comes to SG&A costs, it's, they will follow, of course, our sales growth to some extent. What's important for us is that they grow less then, that we have a scale benefit here that they grow less as a percentage of sales. Exactly where that's going to be, I think it's difficult to give an estimate. I don't know, Fredrik, if you have anything to add there.

Fredrik Rystedt: No, not really. I think it's fine.

Operator: Next question comes from the line of Linus Larsson.

Linus Larsson, SEB: First, a follow-up question on the raw material cost inflation, which was SEK 166 million year-on-year in the current quarter. How much of that was FX?

Fredrik Rystedt: Yes. Of the total number, you talk for the company as such, the whole company.

Linus Larsson: As a whole, raw material cost inflation. And I understand that part of it is the underlying local price cost decline and part of it is changes in FX.

Fredrik Rystedt: It's about SEK 130 million is the currency impact, roughly.

Linus Larsson: So that's a negative...

Fredrik Rystedt: Yes.

Linus Larsson: It's SEK 130 million of the SEK 166 million. Great. And then I wonder on the stock revaluation. I know we've spent a lot of time on it already. And you're saying SEK 230 million. Will it be possible to split that between the divisions roughly?

Fredrik Rystedt: Yes, I don't think we have that? Yes, 1/3, yes, but have we actually communicated that? I'm checking here just so we don't give..

Fredrik Rystedt: Yes, but you're talking about for the different divisions, right.

Linus Larsson: Right, right, right.

Johan Karlsson: But the big impact is – they are in Consumer Tissue.

Fredrik Rystedt: Yes, of course. I mean we – because this is largely pulp, you have it in every area. So we also have it in Personal Care, but of course there's – as we saw in Magnus's presentation, Professional Hygiene is very much impacted by it. And of course, Consumer Tissue is the same because this is largely pulp related, but we also have it in Personal Care. But the absolute predominant is in Consumer Tissue and Professional Hygiene.

Linus Larsson: Well, one would maybe think that Consumer Tissue was most affected.

Fredrik Rystedt: Yes, of course.

Linus Larsson: Yes, yes. OK. And then so in the other costs context, distribution costs, how do you see that develop going forward? What's the market situation when it comes to distribution, if you like?

Fredrik Rystedt: We've had a higher distribution cost now for some time, and this is not due to our own actions. And in fact, if you look the underneath, we actually have good development in the sense that we are systemizing our approach here and actually savings.

So this is largely market-driven. And of course, we operate very, very rarely with spot-related contracts. We have super high service levels to our customers, so we work with long-term contracts. So if you look at the recent development in the spot market, you will actually see distribution costs having actually come down a little bit.

And we are not able to benefit from that, but over time of course, as we see, if this continues in terms of distribution, our distribution development should be actually positive coming both from market-related issues and from our own.

But of course, we have to wait for that to come in more to the contracts. So it's difficult to say, but the increases you've seen in distribution overall is related more to the past than – year-on-year, so to speak, than sequential.

Linus Larsson: Great. That's very helpful. Is there a quarter that you would maybe pinpoint as the quarter when you might expect the year-on-year easing on distribution costs?

Fredrik Rystedt: I think it's difficult to do that, Linus. It's a good question, but I think it's difficult because we, of course, remain on whatever contract discussions we have with our suppliers in this area. And it's difficult to pinpoint, but of course, as you've seen these distribution costs being high in a couple of quarters, you can say that it's still some time left.

Linus Larsson: Thank you very much.

Operator: Next question comes from the line of John Ennis.

John Ennis, Goldman Sachs: A couple from me. And sorry for coming back on the stock revaluation side of things, but I just wondered if you could tell us how much of a positive this was in Q3 and Q4 last year. Because I guess our starting point assumption should be that this fully reverses and more so, I suppose.

And then if you could give us a rough sensitivity on the proportion of pulp declines, so i.e., if pulp declines by 10 percent sequentially, this ends up being x percent in offset that would be really helpful in helping us forecast that going forward.

And then the second question is on Medical Solutions. So the growth clearly deteriorated quite significantly on a sequential basis. I just wondered if you could help us bridge that slowdown from plus 3 percent in Q1 to minus 2 percent in – sorry, plus 3 percent in Q1 to minus 2 percent in Q2. That would be really helpful.

Fredrik Rystedt: Yes, John, thanks for the questions. Let me just start with the first one. Last year – this year. This is kind of tricky because we – last year, of course, the stock revaluation impact was the difference between Q1 and Q2, right?

And this year is between Q1 and Q2 of 2019. And the stock revaluation number that you see, the SEK 230 million that has been alluded to in this call, is roughly the change of those two, so if you want to separate those between the 2 years, it was, you can say, more positive last year and slightly less negative this year, if you put it, but of course the combination of those makes up that number.

The sensitivity is really, really difficult to say, and we don't provide that number. It depends a little bit on the nature of the stock, where we buy it, when we buy it during the quarter and the development of the stock price within that given quarter.

So of course, it's really, really difficult to say, but we will have a high stock revaluation also in Q3. I think that's safe to say given the fact that we know the raw material development during Q2 and Q3 last year.

And we can see that, that was actually, of course, positive, that revaluation. And we can guess, I think it's fair to say, that pulp prices will be lower in Q3. So we will have that negative number and it will be – it's difficult to say exactly, but it will be high as it has been here in Q2.

Magnus Groth: Medical Solutions. So the difference has much do with comps, that we had tougher comparables both in the U.S., especially here now in the second quarter; and also when it comes to invoicing days, where of course one less invoicing day. So a little bit more than that has a quite significant impact on sales.

So those two combined. And the tougher comps regarding the U.S. is partly related to the fact that we are making big changes. And I think we're starting to see some benefits there, but it will take another couple of quarters before we're through that. So that's the explanation regarding Medical Solutions.

John Ennis: I guess, just as a quick follow-up on medical. Is there a level of growth you would need that business to get to on a sustainable basis before you would consider more M&A in that particular area?

Magnus Groth: We believe that we should achieve a run rate growth of 3 percent and that we will get there over time. And when it comes to M&A, that's not related to the growth of medical specifically in one quarter or the other.

It has to do with the attractiveness of that business and the pricing, of course, and the synergies that potentially that would have with – so if it would support our existing medical business, of course, we would still do it, but again we expect to have better growth in medical going forward than what we've seen here in this last quarter.

John Ennis: Ok, thank you.

Operator: Next question comes from the line of Oskar Lindström.

Oskar Lindström, Danske Markets Equities: I have a question around the distribution costs again. And I'm wondering if there's a structural element to distribution cost inflation for you in that most of your volume growth is happening in emerging markets and one could speculate that distribution costs or share of costs is higher there than in mature markets. Is that the case and that we should sort of expect a permanent or a structural increase in distribution costs for you going forward?

Magnus Groth: No, we don't really see any structural difference there. This is quite specific costs that are to a large extent related actually to Europe and North America, where we've over a long time seen increasing distribution costs due to a lack of transport capacity, I think we've spoken about that and some other issues like a lack of capacity in the U.S. and in France specifically and some difficulties also actually in general moving freight in France during the unrest and so on and so forth.

But again as Fredrik mentioned, what we're seeing as a leading indicator is now that the spot prices are coming down in – on distribution, which indicates that over time also our fixed contract costs will come down following that. So no, I'm not concerned about a structurally higher distribution cost.

Oskar Lindström: My second question is also around Medical Solutions and the weaker performance there. Could you be a little bit more specific exactly what is it that's being problematic?

Is it only a certain geography or a segment of the market? And then also if – the problems that you're experiencing now, is that something which impacts your – to an extent your interest in this segment? Or is it more of a temporary issue?

Magnus Groth: No, it's not at all impacting our interest in the segment. And most geographies and businesses are doing quite well and according to our plans. And we've had areas where we've been making changes and improving performance throughout the last two years.

And now lastly, and maybe that's something we should have done in hindsight earlier, we have turned to the U.S., where we actually hadn't integrated the business because it was doing OK but not fantastic for the first one or two years. And since we were also working with the turnaround of our incontinence care business, we decided not to integrate them.

And now that we took that decision six months ago, we can see that there are huge improvement areas in the U.S., and we're starting to see some benefits. And I think we know exactly what we need to do, but this is very much based on our own performance and nothing else.

But of course, we continue to have – our brands are just as strong. Our offering is just as strong. And we think that it's very much go-to-market related, and we think we are – I'm convinced that we are fixing this now in the next couple of quarters. So very much related to the U.S. and to go to market.

Oskar Lindström: All right. And the negative organic growth that you had in this quarter or especially compared to what you had the previous quarter, is that a consequence of the actions that you're now taking, like you're ending certain sales contracts and moving out of certain contracts in there? Or is it...

Magnus Groth: No, we're not ending contracts. It's more has to do with maybe handling stock situation, distributor stock levels; and also integrating the organization.

Oskar Lindström: So is that number – that minus 2.2 percent in this quarter, is that something that should get worse before it gets better?

Magnus Groth: No. We expect that, that should not get worse. Our plan is, of course, to grow in medical. This is a one time impact even though I believe that our U.S. business will actually weigh on the overall growth for a couple of more quarters going forward.

Oskar Lindström: Ok, thank you very much.

Operator: Next question comes from the line of Charles Eden.

Charles Eden, UBS: Magnus, Fredrik, two questions from me, please. Firstly, just looking at Personal Care and the pricing trajectory there: Is – the pricing you sort of see in Q2 of plus 0.9 percent, is that sort of what we could expect for the balance of the year given your commentary on further price increases given the raw material move?

And then my second question is specifically on Baby Care. And obviously, it's marginally positive organic sales growth in the quarter. Could you help us understand the breakdown there between both price/mix and volume and then also the development between developing and emerging markets and whether the trends are broadly similar to what you reported in Q1?

Magnus Groth: Fredrik, do you want to start with the pricing?

Magnus Groth: On Personal Care in general was first and then Baby Care.

Fredrik Rystedt: Yes. We – I can start specifically because, I guess, they're both related. If you take that division – you asked about mature markets and emerging markets. If you take Baby Care, in mature markets the volumes were slightly higher but a little bit negative price and mix.

Or rather actually price was still negative in the Baby Care side, if you look at the mature markets. If you take the emerging markets and – we had a negative volume development in – for baby and slightly higher price and mix.

So that's the split between those two, and that of course adds up to a total of slightly positive organic growth. And of course, needless to say part of our baby business is related to a couple of areas that we've talked about before, one, of course, being Turkey that we have now exited and sold and closed in July. So that's part of that development in emerging market. And then Personal Care, I missed the question actually, Magnus, so maybe you can take that.

Magnus Groth: Pricing was up in the quarter. And my understanding was that you wanted a breakdown of pricing.

Charles Eden: Sorry. Maybe I can, I'm just sort of asking whether your commentary around raw material price development – specifically you were talking, I think, about Consumer Tissue at the time. But whether you were expecting to take any further pricing in Personal Care this year given the raw material development.

Magnus Groth: Yes, sure. Absolutely. So – and that's a good question because we don't talk enough about that, but we're working to increase prices both in incontinence care and in fem care. So in baby, as we just discussed, it's always challenging, but – and we're also relaunching in some countries in Baby Care, just to add to what Fredrik already said, but we're definitely focusing on increasing prices to compensate for raw materials in the other Personal Care categories.

Operator: Next question comes from the line of Sanath Sudarsan.

Sanath Sudarsan, Morgan Stanley: Fredrik, Magnus, just one quick question from me more in relation to the industry behavior or industry participants' behavior in terms of pricing and the profitability levels in Consumer Tissue. How have you seen that evolve over the last two quarters? And what do you expect this behavior to be, more rational, more profitable or driven by more pricing?

Magnus Groth: We've seen a very strong price increase momentum specifically in Europe over the last year. And as I mentioned, we've been able to raise prices three times in a year in some cases, so that's been very encouraging. And right now, I think there's – there will be a little bit of a lull when it comes to price negotiations because pulp prices are continuing down at a faster rate than expected and because annual negotiations are coming up in a quarter or so.

So I expect a stable price development on Consumer Tissue specifically, but as always and as we just discussed during the previous questions, we are looking at improving our margins in many areas in Professional Hygiene, in Personal Care, in – and especially in emerging markets where you have the big fluctuations also in currencies and so on. So it's still a strong focus for us, but the big wave two effort in Europe is done, with a good result.

Sanath Sudarsan: Sorry, Magnus. I was just trying to understand from the other participants' behavior. Have they been more price rational? Are they now profitable? Because there was a stress on profitability from them – from their perspective. Are they now in a position to maybe start cutting prices ahead of competition or ahead of you guys maybe? So I just wanted to understand your perspective about the other participants, not Essity specifically.

Magnus Groth: Yes. And that's, of course, then partly just my speculations. And that's why what I can refer to is that we've had strong price momentum in the last year, which means that all major participants are equally, of course – or equally but all interested or asking for price increases. So I mean that's something that we've seen very clearly in the last year, which then indicates that – I guess, that most players are quite rational.

Because as you know, we think that, believe that many of our competitors, especially in Consumer Tissue, have about half the margins we have. So when we were at all-time low in Consumer Tissue here a year ago or three quarters ago, many of them must have been in the red or at best breaking even. So I guess that's an indication of rational behavior, that everybody needs price increases to improve their margins and their profitability.

Sanath Sudarsan: Ok, thanks.

Operator: Next question comes from the line of Iain Simpson.

Iain Simpson, Barclays: Within incontinence care I just wondered if you could talk separately about how both the retail and the institutional channels were doing. And then just to come back to Medical Solutions: That business has perhaps not performed as well as you might have liked it to have done when you bought it. I appreciate it's early days kind of bedding it in and all that, but I just wondered if you could perhaps give some color on why Medical Solutions has perhaps been slightly slower to start performing than you might have liked.

Magnus Groth: OK, thanks. Good questions. So starting with incontinence care. We have seen a very, very good development in health care overall. So that's really growing and gaining market share both in Europe and in North America.

In retail we're seeing a positive development in most emerging markets, very good, strong developments, including Latin America which is our biggest emerging market for incontinence care. In Europe we are growing, stabilizing market shares. As you know, since our competitor launched four or five years ago, we've seen declining market shares. They are now stabilizing.

And we have high hopes for the recent launches that we've done that this will be a turning point also from that perspective in inco retail in Europe. In North America we've had slightly lower sales in the quarter, which we are addressing.

So margins are OK in North America retail, but we have slightly lower sales. So – but that's, of course, a smaller part of our business. So most of our inco business is developing really well both when it comes to volume, price and mix.

Second quarter medical. Yes, when it comes to margins, we are quite happy. So they are on the level we expected. In the integration work that we have moved forward with we have identified issues over the quarters. And I've tried to be as specific as possible, so – and as transparent as possible with those issues, where we were doing some restructuring in Latin America initially then in Asia Pacific.

That's now doing quite well. We were really working to improve the growth in Europe, and that's developing step by step. And then there was maybe an issue that we caught too late in North America with how that business was operating, and we're all over that now. And maybe that's something we could have caught earlier, but that's something that we're very convinced will improve.

We're #1 in compression. We have a very nicely growing small advanced wound care business in the U.S. And we see huge opportunities for those businesses, but that's something that we caught now and which we maybe hadn't expected.

So that's why growth hasn't been as expected. There's nothing new when it comes to the underlying market growth or our market positions really. It's all mostly based on our internal performance and improvements that we need to make.

Iain Simpson: Thank you.

Operator: Once again, please press “star” and number “1” if you wish to ask question.

Operator: Your next question comes from the line of Guillaume Delmas.

Guillaume Delmas, Bank of America Merrill Lynch: Three questions from me. The first one is on your Professional Hygiene business. I think, Magnus, in your prepared remarks you mentioned that the U.S. was back to positive growth territory.

So that's good news, yet if I look at your organic sales growth in mature markets for this division, there is a sequential slowdown in Q2 to a very modest 0.5 percent organic sales growth.

So on this my question is what happened in Western Europe. Why has growth deteriorated there? And what could be the outlook for Professional Hygiene in Western Europe for the second half of the year?

Magnus Groth: No, that's absolutely the right analysis and conclusion, that we had a declining growth in Western Europe in Professional Hygiene after a number of quarters of incredible growth with the market share gains, so I don't see this as a concern at this point in time. It's just something that happens in certain quarters.

We still have great momentum and a very, very good setup in Europe. So this was a temporary decline, which of course doesn't mean that we can continue growing market share forever at very high rates. So maybe we will see a slightly slower growth in Europe, who knows, eventually, but on the other hand, we have actually gained a number of new contracts in North America.

And we will see a gradual improvement also going forward in North America, so I think that we'll – going forward, we should see a – more of a balance maybe between our two big mature markets North America and Western Europe, but still a positive development.

Guillaume Delmas: OK. And my second question is actually relatively similar but this time on Consumer Tissue because, despite the fact that mother reels had a slightly less-negative impact on your Q2 performance relative to Q1, there was also a slowdown in mature markets in the second quarter, I mean, to 0.8 percent.

Again, any granularity you can give on your performance in Western Europe for Consumer Tissue; and as to why, despite mother reel being less of a drag, we've seen a slowdown? Is it more volume, price/mix led?

Magnus Groth: This is very much volume. And it's a consequence of the ongoing price negotiations also during the second quarter, when as you know typically during negotiations there is a negative impact on volumes as the retailers that we negotiate with tend to put pressure on us by delisting or by cutting volumes for a certain period of time and also something that we've been willingly – willing to accept because the price – the wave two price increase effort has been so important for us.

But of course, going forward we will need to find a good balance there to get back to volume growth. Because that's important for our COGS savings and cost development, that we can utilize the capacity that we're freeing up in our remaining assets as they become more efficient with higher machine efficiency and fewer stops and so on. So also an area where we are looking to find then a good balance of price/mix and volume going forward.

Guillaume Delmas: My very last question is if I go back to your Q1 conference call three months ago. I think, at the time, you were talking about significantly higher raw material costs for Consumer Tissue in Q2.

If I remember well, I think you were also talking about trying to bring down this other line, which was unusually high in Q1. And clearly, Q2 didn't play out, at least for these two moving parts, the way you were expecting it, so my question is why such discrepancy between the soft guidance you provided three months ago and the way Q2 actually played out.

Fredrik Rystedt: Guillaume, you have a great memory apparently, and you're absolutely right. And clearly I think it has been more difficult for us to forecast raw material development. And of course, both stock revaluation and raw material is very, very much related to the input costs line. So you can derive from exactly these two comments that raw material has come down to a larger extent than we did expect at the time of the call.

That's clearly the case. I think the other thing we – and this is a decision that we have taken, to spend more in terms of marketing and sales costs for the very strong growth that we have. So it's basically related to these two factors, but we did underestimate the decline of raw material. That's the biggest impact.

Guillaume Delmas: And do you feel you've got a higher level of visibility for Q3? Or there is still a great level of volatility at this stage regarding Q3.

Fredrik Rystedt: I mean, Guillaume, in a world where raw material is absolutely flat then, of course, we got zero in both those lines, right? So unfortunately, it's – even though we would like to have a crystal ball, it's super difficult to estimate. We don't.

We – at the early part of – or the latter part last year, we – our guess would have been that raw material, in terms of we talk at least pulp costs, would have continued to move up. And of course, we've seen a very different development since then, so clearly it has not become exactly as we have – we thought. And the visibility, we believe we do our best to estimate that, but of course it's very, very difficult.

Magnus Groth: But with all those caveats, we do see significantly lower market pulp prices in the third quarter sequentially. So – and we're – already we're a good way into July, and there are no indications that, that would change. And even lower costs in China actually for pulp than we could have ever expected in the first quarter.

So as Fredrik says, big uncertainties and huge volatilities this point in time, but still for the third quarter that we're already into, we'll see significantly lower pulp prices.

Fredrik Rystedt: And therefore, we can also conclude that stock value adjustment will be correspondingly high in accordance with that.

Operator: Next question comes from the line of John Ennis.

John Ennis, Goldman Sachs: I just wondered. And again sorry for coming back to this, but can you just give us the impact from stock revaluations in Q3 2018, 4Q 2018 and then Q1 2019 relative to the SEK 230 million impact you gave for this quarter? That would be super helpful.

Fredrik Rystedt: No, we don't do that, John. I alluded to it before, that this is just kind of explaining the change between two quarters, right? So and as I alluded to before, the positive development that we had in Q2 of 2018 was slightly bigger than the negative impact we had in 2019.

So we have got a big negative in 2019 and we got a positive in 2018. And that number of the SEK 230 million, that's basically the adding those two up. So that positive was slightly bigger than the negative, but of course it's a combination of those two.

Magnus Groth: And Fredrik, of course, and John, of course, this is an issue for the modeling and a higher also stock revaluation than we had expected due to these fluctuations in pulp prices but just to remember that overall the pulp price development is a positive for us, of course, going forward.

So it's a good thing and because it hits our margins with a 45 days delay that you're well aware of. So of course, even though it impacts negatively on this other line, it's still a leading indicator of where pulp prices are moving.

John Ennis: Ok, thank you.

Operator: Next question comes from the line of Lara Simpson.

Celine Pannuti, JP Morgan: It's Celine Pannuti from JP Morgan. Just a few follow-ups on the raw materials side. Last year, your raw mat bill was, if I remember correctly, more than SEK 4.5 billion. Could you say how much was the corresponding revaluation of stock last year so to have an idea of the net impact? And also I think, earlier this year, you said that you were expecting for the full year that the raw material bill will be less than half of what it was last year.

Now having seen what you see in H1; and with your views that the market, the pulp prices have come down, what do you think the number will be for the year? That's my first question. And then lastly, the second one is on Consumer Tissue. I understand that wave two is ongoing. However, sequentially we've seen pricing decelerating in Consumer Tissue. Could you explain why was that?

Fredrik Rystedt: Yes. Let me start with perhaps the first question. Once again, the stock value adjustments that we talk about in the bridge here is just a difference between last year and this year. So as raw material prices increased last year, it was positive all the time.

Now I think we've said a couple of different – in a couple of different occasions that we are just actually adjusting the value of the inventory at the end of the quarter, reflecting the movement of the price. So that is just kind of resetting the raw material to the incumbent level, so inherently it's just reflecting the fact that the margin is that much better as we go forward, but it was very the negative this year. It was positive last year.

We don't give a forecast, Celine, on the full impact of raw material for the year. We normally just give it for the next quarter. We do it sequentially and year-on-year, so to speak. We give a forecast there. I think the number that you were alluding to was just a calculation.

Kind of if numbers were staying where they were at the end of the year, I think that would have been the number. So we normally just provide one quarter ahead, and this has to do with the fact that we don't have that much transparency more than that quarter.

Magnus Groth: OK. Second question.

Celine Pannuti: On then I'm trying to understand last year. Could you give us the net impact of your raw mat plus revaluation? What was it in 2018?

Fredrik Rystedt: No, we – I mean we – the – as I mentioned, Celine, I can't do that because it's this is a change between two years. So we have a reset of the value each quarter on the material, so I cannot actually give you that number. This is a change between two years.

So the bridge is a positive and a negative, and as I mentioned, it was slightly bigger last year. So if you have the SEK 230 million, a bit more than half of that number was a positive last year. And then the negative part – rest is negative this year. So it was a significant number also last year, but we don't have the – we have not given the exact numbers.

Celine Pannuti: OK. And then does it, I mean then did you have an impact as well from holding maybe a bit more from – inventory than you would have because you thought that the market would continue to go up?

Fredrik Rystedt: No. And typically – just generally, Celine, we have a fairly – this is actually the absolute majority of this impact is related to finished goods, not actually pulp stock. So it's the pulp component within the finished goods that we have. That's actually the majority of it.

Normally our pulp stock is quite low. We try to keep it as low as possible. There are a couple of exceptions. So of course, we have long transportation or lead times for if you have long distances like Asia, as an example, but normally this is fairly short lead times. So this has nothing to do with inherent pulp hedging or adjusting inventories.

Magnus Groth: OK. Over to your second questions about price.

Celine Pannuti: Consumer Tissue pricing.

Magnus Groth: Exactly, Consumer Tissue. And wave two is done, so according to plan and with the results we had expected. If pulp prices had remained on very, very high historic levels, of course we would have immediately started a wave three. This is not what we're seeing. We're seeing that we have increased prices now in a number of waves to an extent that we see increasing shelf prices and market prices in general.

And now pulp prices are coming down at a more rapid rate and to a higher extent than we had expected. So right now, we are satisfied with the pricing increases achieved. And what happens then is that, of course, quarter-over-quarter we will have tougher comps as the price increases that we did throughout the last year move into the comps.

Celine Pannuti: But sequentially what was the delta on that, this pricing slowdown in Q2 versus Q1?

Magnus Groth: That's tougher comps. We made a lot of price increases already last year.

Celine Pannuti: All right, well thank you.

Josephine Edwall-Björklund: OK. Then we need to conclude today's press conference, so thank you all for calling in. I wish you a good rest of the day. Goodbye.

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