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CREDIT OPINION

12 January 2017

Update

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RATINGS

SCA Hygiene AB

Domicile	Sweden
Long Term Rating	Baa1
Type	LT Issuer Rating - Fgn Curr
Outlook	Negative

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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SCA Hygiene AB

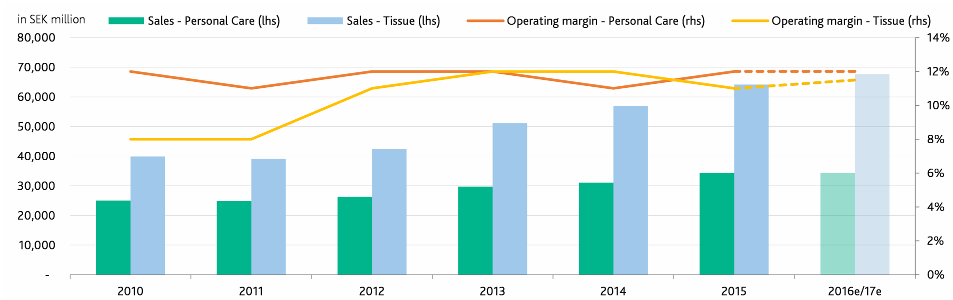
Update following the announced acquisition of BSN and the change of the outlook to negative

Summary Rating Rationale

The Baa1/P-2 ratings for SCA Hygiene AB ("SCAH") - an entity that will host the Personal Care and Tissue operations of Svenska Celullosa Aktienbolaget ("SCA", P-2 stable) - primarily reflects SCAH's strong business profile enabled by a number of #1 or #2 market positions across the portfolio, with both branded and private label products. This, in connection with fairly resilient consumer end markets, has helped SCAH to generate stable and solid margins through the cycle (we estimate pro-forma Moody's-adjusted EBIT margins of around 11-12% for SCAH currently).

Exhibit 1

SCAH has delivered stable and solid profitability in last couple of years in its Tissue and Personal Care operations



Note: Numbers as reported by SCA
Source: SCA's annual reports 2011-2015

The brand strength is partly balanced by the fact that SCAH generates the majority of sales in low-growth mature markets generally characterized by intense competition and/or periodic oversupply. However, via a combination of organic and external growth, the proportion of products supplied to emerging markets has been constantly increasing; a trend that we expect to continue.

Following the announced acquisition of BSN Medical Luxembourg Group Holding S.a.r.l. (BSN, B2 review for an upgrade) for the purchase price of around €2.7 billion (on a debt and cash-free basis) in mid-December 2016 SCAH's Baa1 will be initially weakly positioned providing fairly limited headroom for further debt-funded growth or weaker than expected operational performance, which is reflected in the negative outlook. We expect that within 18-24 months after the closure of the transaction Moody's adjusted debt/EBITDA will return towards below 3.0x (estimated to be close to 4.0x for 12 months to September 2016, pro-froma including external debt of SCA as well as BSN's purchase price), which is still commensurate with a weak Baa1 rating.

Credit Strengths

» Strong business profile with segmental diversification and well positioned global (Tork, Tena) and regional brands

» Expanding Consumer Products business with positive sales growth driven by bolt-on acquisitions in emerging and mature markets

» Profitability improvements given ongoing efficiency measures and shift towards higher margin product offering

» Financial policy aimed to protect solid investment grade rating

Credit Challenges

» Majority of sales in stable but low-growth domestic markets with periodic overcapacity issues

» Ongoing need for innovation in the Personal Care and Tissue business areas to preserve pricing levels

» Event risk: potential M&A activity, alternatively shareholder returns, special dividend

Rating Outlook

The negative outlook reflects weak positioning at Baa1 level following the fully debt financed acquisition of BSN for the purchase price of around €2.7 billion, which will lead to some leverage deterioration, with a return of Moody's adjusted debt/EBITDA towards below 3.0x only after 18-24 months after the acquisition.

Factors that Could Lead to an Upgrade

» EBIT margins consistently above 12% throughout all business areas

» RCF/Net Debt clearly above 25%

» Debt/EBITDA well below 2.5x

» Continued positive free cash flow generation applied towards debt reduction

Factors that Could Lead to a Downgrade

» Decline of EBIT margins to below 9%

» RCF/Net Debt falling sustainably below 20%

» Debt/EBITDA moving towards 3x

» Free cash flow turning negative

» Erosion of the company's solid liquidity profile

Detailed Rating Considerations

STRONG BUSINESS PROFILE WITH SOLID INVESTMENT GRADE CHARACTERISTICS

SCAH's Baa1/P-2 ratings primarily reflect the company's position among the leading hygiene products companies globally, as reflected by #1 or #2 market positions in Incontinence Products and Away-from-home tissue, and a geographic reach into ca. 90 countries. Strong market positions with both branded (global brands include Tena and Tork besides several regional brands) and private label products in personal care products (34% of expected group sales in 2016) and tissue (66%) are complemented by fairly resilient consumer end markets. This has helped to generate stable results at solid margins - we estimate SCAH's Moody's adjusted EBITA margin of around 11-12% currently - through the cycle and offset some of the volatility inherent to SCA's legacy Forest Products operations, which will not be part of SCAH.

This aspect will be further intensified given the retained management focus on the group's two operations in SCAH. However, following the spin-off, SCAH will have to establish reliable contracts including procurement of one of its main input materials, pulp, with an estimated consumption of 2.25m tons in 2015, that accounted for 21% of operating expenses in Tissue respectively 10% in Personal Care products, while managing the commodity's price volatility.

We understand that management will in particular focus on raising the efficiency of the group's European tissue operations, which we believe will result in gradual margin improvement over the next two to three years. While we do not expect any material capacity rationalisation, greater focus on supply chains, manufacturing excellence and sharing of best practices should allow for gradual profit improvement. Also, highly profitable BSN will also help to improve SCAH's margins towards more profitable competitors, such as Kimberly Clark Corporation (A2, stable) or Procter & Gamble Company (Aa3, stable).

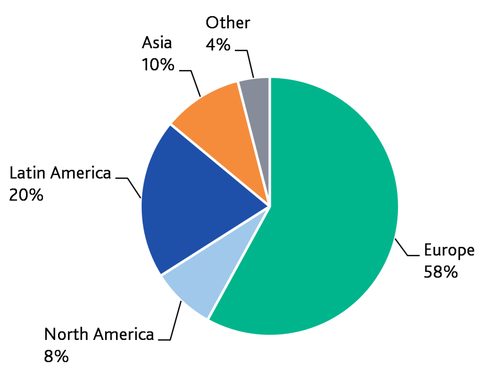
MAJORITY OF SALES IN STABLE BUT OVERALL LOW GROWTH MATURE MARKETS WITH BOLT-ON ACQUISITIONS TO INCREASE EMERGING MARKET EXPOSURE, NOW ALSO EXPANDING INTO MEDICAL DEVICES

SCAH continues to generate the majority of its sales in fairly mature markets of Europe and North America, both of which are expected to show only moderate growth in the coming years except for incontinence products with growth opportunities as a result of an aging population and so far still limited product use. During recent years the group has, therefore, been increasing its efforts to grow in emerging markets (Asia, Southeast Europe and Latin America), where still significantly lower per capita consumption of tissue and personal care products yet improving disposable income levels and living standards are expected to result in higher demand growth for hygiene products compared to mature Western markets.

Exhibit 2

Personal Care

Geographical Net Sales Split in %, as of 2015

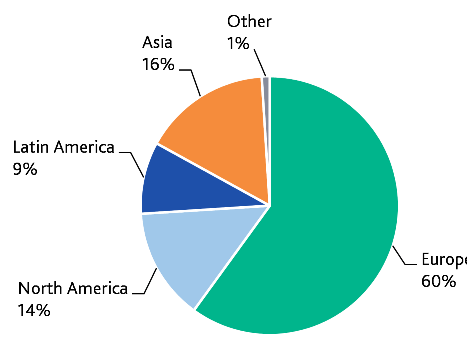


Source: SCA's annual report

Exhibit 3

Tissue

Geographical Net Sales Split in %, as of 2015



Source: Source: SCA's annual report

Following the 2012 acquisitions of Georgia Pacific's European tissue assets, as well as companies in China, Chile and Taiwan, during the fourth quarter of 2013, the group acquired additional shares in HongKong Stock exchange listed tissue company Vinda (following minority ownership since 2007), thus becoming the majority shareholder with a 51.4% ownership. Vinda produces consumer tissue, personal care and away-from-home products including toilet paper, boxed facial tissue, paper napkins, paper towels and paper tissues in addition to its extensive distribution network which led the group to divest of its business in South East Asia, Taiwan and South Korea for integration with Vinda on 1 April 2016. The increased ownership gives SCAH access to the rapidly expanding market for tissue products in China, which is estimated to grow by up to 10% annually because of demographic trends towards the occidental lifestyle among Asia's growing young population, rising income levels and urbanization. We expect SCAH to continue to play an active role in the consolidation of hygiene activities in emerging markets.

In mid-December 2016, SCAH announced an acquisition of BSN, a company active in the medical devices market with product offering centered around wound care and orthopedics product, which will provide SCAH with an additional growth platform in a fragmented market for medical devices with low technology content with good underling and fairly stable demand.

M&A RISK BUT WITHIN THE LIMITS OF FINANCIAL POLICY TARGETING SOLID INVESTMENT GRADE RATING

SCAH has been fairly acquisitive in the last decade, but with financing in line with its publicly stated commitment to a solid investment grade rating. Following the announced acquisition of BSN for the purchase price of around €2.7 billion (on a debt and cash-free basis) SCAH's Baa1 will be initially weakly positioned providing fairly limited headroom for further debt-funded growth or weaker than expected operational performance, which is reflected in the negative outlook. We expect that within 18-24 months after the closure of the transaction Moody's adjusted debt/EBITDA will return towards below 3.0x (estimated to be close to 4.0x for 12 months to September 2016, pro-froma including external debt of SCA as well as BSN's purchase price), which is still commensurate with a weak Baa1 rating. We will consider further smaller acquisitions within limits of SCAH's free cash flow generation on a case-by-case basis.

Liquidity Analysis

We expect SCAH's liquidity profile to be good, mainly supported by continued material positive free cash flow generation in the next 12-18 months. SCAH will assume essentially all external debt of SCA, including largely undrawn credit facilities totaling roughly SEK23.1 billion, primarily consisting of two syndicated facilities of each €1.0 billion, maturing in 2019 and 2021. The facilities are of high quality, without MAC clauses and other conditionality language and has served also as backstop facilities for the commercial paper programme, which has been central source of SCA's short term funding needs. As per end-September 2016 SCAH would have reported around SEK2 billion of short-term debt, which compares to almost SEK6 billion of current financial assets, cash and cash equivalents. The next material bond maturity would be in 2018. We understand that SCAH has access to committed bridge facility to finance the acquisition of BSN.

Profile

Headquartered in Stockholm, Sweden, SCAH is an entity that will host the current Personal Care and Tissue operations of SCA. In 2016 we expect SCAH to generate sales of around SEK100 billion in more than 100 countries under regional and global brands, such as TENA and Tork.

Rating Methodology and Scorecard Factors

The principal methodology used in rating SCAH is Global Packaged Goods Rating Methodology. The methodology grid indicates a weak A3 rating for our 12-18 month forward-looking view, which already incorporates the acquisition of BSN. The one notch difference is mainly attributed to a weak positioning of SCAH in the A category for Geographic diversification, Category assessment and Financial policy sub-factors.

Exhibit 4

Forward looking methodology grid

Consumer Packaged Goods Industry Grid [1][2]	Moody's 12-18 Month Forward View As of November 2016	
Factor 1 : Scale and Diversification (44%)	**Measure**	**Score**
a) Total Sales (USD Billion)	$11.5 - $13.0	A
b) Geographic Diversification	A	A
c) Segmental Diversification	Baa	Baa
Factor 2 : Franchise Strength and Potential (14%)		
a) Market Share	A	A
b) Category Assessment	A	A
Factor 3 : Profitability (7%)		
a) EBIT Margin	12.0% - 13.5%	Ba
Factor 4 : Financial Policy (14%)		
a) Financial Policy	A	A
Factor 5 : Leverage and Coverage (21%)		
a) Debt / EBITDA	2.9x - 3.3x	Baa
b) RCF / Net Debt	14% - 20%	Ba
c) EBIT / Interest Expense	8x - 10x	A
Rating:		
a) Indicated Rating from Grid		A3
b) Actual Rating Assigned		Baa1

All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
This represents Moody's forward view; not the view of the issuer; and incorporates an acquisition of BSN.
Source: Moody's Financial metrics

Ratings

Exhibit 5

Category	Moody's Rating
SCA HYGIENE AB	
Outlook	Negative
Issuer Rating	Baa1
Senior Unsecured	Baa1
ST Issuer Rating	P-2

Source: Moody's Investors Service

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