Suominen

Company update

7/2018

inderes.

Waiting for a trend change

We retain our 3.50 euro target price and reduce recommendation for Suominen. We estimate that Suominen's earnings will recover from difficult years of 2016 and 2017, where critical elements are pricing, product mix transformation, and production ramp-up in Bethune. However, we consider short term valuation too high given major uncertainty over the speed of profit recovery in challenging trading conditions. Medium term potential remains but we are not willing to stretch short term valuation at this point.

Strategic direction is right even if recent progress has been adverse

Suominen executes its growth strategy, which is based on value added nonwovens, organic growth and product mix transformation and geographical expansion to Asia (most likely with M&A). The company plans to reach organic growth mostly with its current production platform (incl. full leverage from Bethune) while R&D, commercial excellence and customer orientation should drive absolute and relative growth of value added products. We argue that the strategy is credible and it takes advantage of Suominen's strengths. Nonwoven demand supports the growth strategy as Suominen's current main markets (Americas and Europe) grow 3 % p.a in volume. However, increasing supply in the market, increasing raw-material prices and slow start-up in Bethune have kept the company's profits under pressure recently. This confirms that the strategy (i.e. reducing exposure to the most competitive value for money segments) itself is right but on the other hand strategy execution remains challenging.

Current estimates remain clearly below the company's very ambitious targets FY'21

Suominen set over 6 % growth CAGR, on average 15 % ROI-% and 40-80 % gearing level as its financial targets for the strategy period of 2017-2021. In addition, the company disclosed its net sales will be over 600 MEUR and EBIT-margin over 10 % in 2021 if the strategy execution is successful (2017: net sales 426 MEUR, EBIT-% 3.5 %). We argue that the targets are very ambitious given current trading environment. Our medium term estimates remain well below the target levels (2021e: net sales 502 MEUR, EBIT-% 6.6 %). Increasing share of value added products (drives up sales and gross margin) should be the main driver to close the profitability gap. In addition, some more volumes (increasing sales and gross margin through efficiency) and also lower SGA-% (operating leverage) will be required to restore profitability. We argue dependence on key customers, limited pricing power and overcapacity represent the most concrete risks related to medium term profit growth (and its speed). In addition, the start-up still late in schedule in Bethune adds uncertainty to FY'18.

We are not willing to strech short term valuation before the profit trend goes upward

Suominen's P/E-ratios based on our estimates are 24x and 13x FY'18 and FY'19, while corresponding EV/EBITDA-ratios are 7x and 6x. We consider FY'18 levels elevated for Suominen while FY'19 figures are close to neutral. There could be significant medium term upside in the share should the company go even close to its 2021 targets. However, we are not yet ready to stretch short term valuation before the profit trends upwards and therefore continue to wait an entry point with better risk/reward.

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Recommendation and target price

Reduce

Previous: Reduce

3.50 EUR

Previous: 3.50 EUR

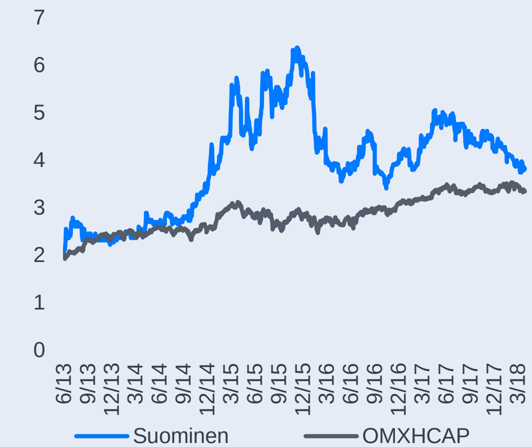
Share price: 3.40 EUR
Potential: 2.9 %

Key figures

	2017	2018e	2019e
Net sales	426	433	459
Growth-%	2,2 %	1,7 %	6,0 %
EBIT (adj)	31,2	16,0	24,6
EBIT-% (adj.)	3,5 %	3,7 %	5,4 %
Pre-tax profit	12,4	11,0	20,4
Net earnings	14,5	8,1	15,3
EPS (adj.)	0,27	0,14	0,26
DPS	0,11	0,11	0,12
Payout-%	44 %	79 %	46 %
P/E	16,4	24,4	12,9
P/B	1,9	1,4	1,4
P/S	0,6	0,5	0,4
EV/S	0,8	0,6	0,6
EV/EBITDA	9,7	7,5	5,7
EV/EBIT	21,4	17,7	10,5
Dividend yield-%	2,5 %	3,2 %	3,5 %

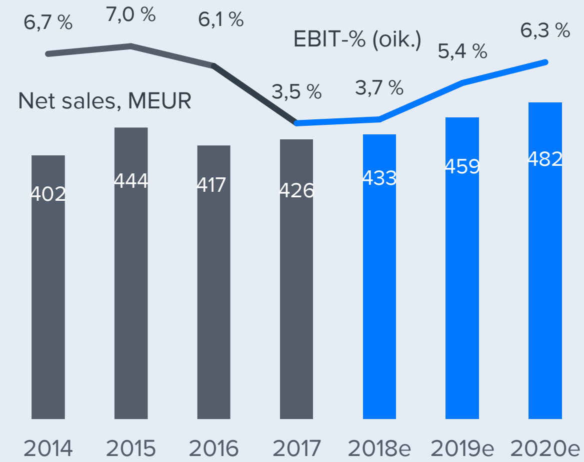
Source: Inderes

Share price development



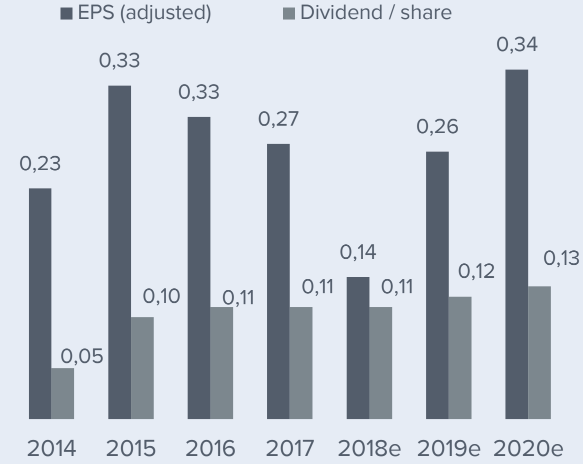
Source: ThomsonReuters

Net sales and EBIT-% (adj.)



Source: Inderes, Suominen

EPS (adj.) and dividend



Source: Inderes, Suominen

P/E (adj.)
24x
2018e

EV/EBITDA
7x
2018e

P/B
1.4x
2018e

Yield-%
3 %
2018e

Drivers

- Growing nonwoven market supports the growth efforts
- Increasing share of value added grades increase profitability
- Some SGA leverage
- Nonwoven demand is fairly defensive
- M&A option

Risks

- Overcapacity in babycare and flushables
- Value chain position keeps pricing power limited
- Competition remains intense in certain segments
- Raw-material price risk
- Profits are sensitive to EUR/USD-rate

Valuation

- Short term multiples remain elevated due to weak earnings run-rate
- Volume or balance sheet valuation does not support the share yet
- Medium term potential exists but current profit trend does not justify to look more far away
- We continue to wait for a better risk/reward-ratio

Contents

Company description (1/2)

Global nonwoven leader in wiping

Suominen is a manufacturer of nonwovens and the company consist of two BA's, Convenience and Care. The first produces nonwovens for wiping products while the latter focuses on selected niches in hygiene and medical nonwovens. However, the company reports financial results only on group level. The company has more 650 employees in 5 countries. In 2017 Suominen's net sales were 426 MEUR and comparable EBIT 15.0 MEUR.

Suominen is the leading global producer in wiping and supplies a range of nonwoven roll goods, which the company manufactures in US, Spain, Italy, Brazil and Finland. Due to its manufacturing footprint, Suominen achieves significant sales in the North and South America as Americas bring over 60 % of the group's net sales, US being clearly the biggest single market by over 50 % of the group's net sales. The second major market is Europe (mostly Western Europe) representing over 35 % of net sales. Net sales is low in other areas as overseas sales is typically difficult in nonwoven business due to logistical issues (low value/volume-ratio of the products).

Sales come from various mostly consumer driven segments

Suominen divides its sales to five revenue streams based on product type:

- **Baby care** is the biggest segment of the company as it brought 41 % of the company's sales in 2017. Baby care wipes is a extremely competitive low growth and high volume value for money segment in developed North America and Europe (demand in baby care reflect birth rates). In emerging world (incl. South America) baby care is a well growing segment due to higher birth rates and lower penetration rates of nonwoven products.

- **Personal care** wiping such as wipes for facial cleaning, makeup removal, refreshing and intimate care, travel&catering end-use and flushable WC products constituted 21 % of the group sales in 2017. Personal care is mostly a value added segment that exists currently mostly in developed countries. Growth in personal care has recently slowed down due to fast commoditization and corresponding price erosion in flushable WC products.

- **Home** wiping is a value added segment that brought some 19 % of Suominen's sales in 2017. This segment includes cleaning related wiping products that are used in developed western world at homes. Thus, home wiping is mostly value added business.

- **Workplace** wiping consist of Suominen's wiping products to B2B end-customers, which generated 9 % of the group sales in 2017. These products are used from fast food restaurants to factories, thus the portfolio consisting of different kind of value added products is wide. The main markets are US and Europe. Suominen targets the new production line in Bethune plant to improve value and volume growth especially in Home and Workplace and to potentially smaller extent in flushables.

- **Medical&Hygiene** (Care) brought some 9 % of Suominen's sales in 2017. Unlike other segments Care does not include any wiping products but nonwoven components to other products. In Care, Suominen has focused on fluid management, thus the company does not (at least yet) try to be all over on the large hygiene and medical markets but focuses on selected value added niches. The main markets of Care are in North America and Europe currently.

As illustrated, Suominen's products end up mostly to consumer related end uses and they can be characterized to either staples or discretionary. The relatively defensive nature of the wiping market is a positive factor from investors' point of view in our opinion.

Historical development

Suominen has a long history from the year 1898 but the company was rebirth in August 2011 when Suominen agreed to acquire Ahlstrom's Home & Personal BA for 170 MEUR (EV). This transaction made Suominen a global company that is focused on nonwovens in the wiping segment. Since then nonwovens have been the only core business of the company but at the beginning of 2012 Suominen had also two other businesses, Codi Wipes and Flexibles, which were divested as non-core assets for 9 MEUR (EV) and 20 MEUR (EV) in 2013 and in 2014. In addition, the company acquired also Paulinia nonwoven plant in Brazil from Ahlstrom for 17.5 MEUR (EV) in 2014. Therefore, two acquisitions and two divestments made Suominen a global leader in its core business in 2010's.

Company description (2/2)

In addition to strategic and structure changing transactions, Suominen required a major operative turnaround as the company had been seriously struggling with its profitability before Ahlstrom H&P acquisition. Historically weak profitability and the acquisition raised the company's gearing to unsustainably high levels at over 100 % at the end of 2011. As the first step in the turnaround, Suominen outlined a new strategy at the beginning of 2012, in which the company decided to focus on value added nonwovens. In short, the strategy aimed to reduce weight in highly competitive bulk production in the portfolio and grow in value added grades carrying higher gross-margins (GM-%).

As the company left from a distressed position and the large acquisition required integration, Suominen focused heavily on internal issues such as direct cost savings (10 MEUR cost saving program completed in 2012/2013) and other internal efficiency improvements (two supply chain development programs in 2012-2014) in its strategy execution in 2012-2014. Correspondingly, debt reduction dominated the company's capital allocation during this phase.

The company was successful in its rebuilding efforts as the savings, the efficiency improvements, the strategic transactions, moderate volume growth and gradual product mix transformation raised Suominen's EBIT margin from 3.3 % to 6.7 % in 2012-2014. In addition, the company generated very strong cash flow during the rebuilding phase as CAPEX was limited to maintenance (clearly below depreciation) and efficiency improvements released NWC. Therefore, the company's gearing dropped from 101 % to 43 % in 2012-2014 (includes also 17.5 MEUR equity increase as the company used a convertible hybrid bond to finance Paulinia acquisition). Therefore, Suominen managed to refinance its expensive debt portfolio at the end of 2014, which was the last step of the very successful rebuilding.

After the rebuilding, Suominen launched a strategy update at the end of 2014. There were no changes in big guidelines but the new strategy for 2015-2017 shifted clearly Suominen's focus from efficiency improvement to organic growth for which the rebuilding had created a solid foundation. In addition, this strategy included heavy CAPEX as the company invested over 100 MEUR (most of them to new production line in Bethune US) to enable product mix transformation in 2015-2017.

Despite the company's efforts to change the gear, 2015-2017 have been challenging time for Suominen. Suominen reported its highest net sales and EBIT in 2015 but this was mostly driven by favorable FX development (strong depreciation of EUR/USD). However, organic growth slowed down in US already in 2015 while the progress was adverse growth and profitability wise in the both main markets in 2016 and 2017 (and in Q1'18). This was mostly due to increased supply of certain nonwoven grades, which pushed demand and sales prices down in 2016. To make the matters worse, raw-material prices began to raise, product mix improvement stopped and start-up in Bethune caused challenges in 2017. Thus, Suominen's profitability dropped to clearly unsatisfactory levels in 2017. The big picture has not changed at the beginning of 2018.

The management and shareholder structure

Suominen appointed Nina Kopola as its CEO after the H&P transaction and she is currently managing the company. In addition, also CFO Tapio Engström has been in the company since 2012, thus the top management has a fairly long experience from the company and nonwoven business. Suominen's financial track-record is decent under the current management if we look at the last 5 years as a whole. The entire management team consist of 8 members as the company has strengthened resources in the top management during the last years.

Suominen's board of directors constitutes of 6 members. The chairman of board has been Jan Johansson since AGM in 2017. There are 5 independent members in the board, thus the structure of the board seems to be adequate from investors' perspective in our opinion.

Suominen's shareholder structure is fairly centralized as 15 of the biggest shareholders control around 75 % of the company. Ahlstrom Capital became the main shareholder in Suominen in 2014 and it holds 24 % of the shares and votes in the company. Ahlstrom Capital is a family owned long term investor and we believe they are committed to long term value creation in Suominen. Other large shareholders are mostly Finnish institutions and private investors. Therefore, we do not consider the shareholder structure to carry any additional risks. However liquidity of the share has been recently limited, thus we argue certain liquidity premium must be taken into account in the shares' valuation.

Suominen in brief

Suominen is a global market leader in wiping segment in the nonwoven industry.

1898
THE COMPANY WAS ESTABLISHED

2011
M&A CREATED ”THE NEW SUOMINEN”

#1 MARKET SHARE*
GLOBAL MARKET OF NONWOVENS FOR WIPING
* SUOMINEN

426 MEUR (2.2 % vs. 2016)
NET SALES 2017

15.0 MEUR (3.5 % of sales)
ADJUSTED EBIT 2017

664
PERSONNEL (AVERAGE) IN Q1’18

8
PLANTS IN 3 CONTINENTS

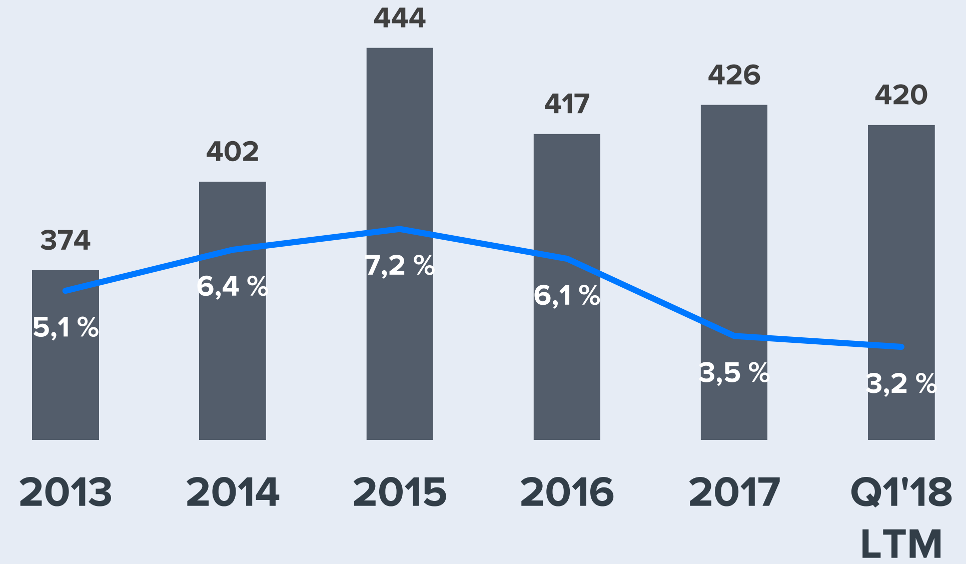
Rebuilding in 2012-2014

- Focus on savings and efficiency
- Low CAPEX, NWC release
- Debt reduction
- Divestment of non-core assets
- Paulinia acquisition
- Product mix transformation

Focus on growth in 2015-2017

- Major CAPEX
- FX tailwind in 2015
- Competition intensifies
- Mix fluctuates
- Cautious dividend payout
- Start-up burden from Bethune in 2017

Suominen’s net sales and EBIT-% in 2013-Q1’18 LTM



Source: Suominen, Inderes

Investment profile, potential and risks

Suominen is a growth company

After the rebuilding and corresponding turn-around case, investors categorize Suominen as a growing manufacturing company. Also, the company's current strategy and nonwoven market's long-term growth above GDP growth support "the growth profile". Therefore, we believe Suominen aims to stay as a growth company also beyond the on-going strategy period even if tools driving growth may change over time.

Typically growth requires certain CAPEX and ties some NWC in the manufacturing industry, which reduces dividend payout capacity at least in the short term. Suominen's capital needs seem fairly limited for the next years (CAPEX below depreciation) but the company's gearing is in the upper side of the target range after recent investments and weak profitability development. Thus, the company is not and should not be considered as "a dividend stock" in the foreseeable future.

Potential

- **Organic growth:** Nonwoven demand has traditionally somewhat exceeded GDP growth in developed Western countries. In emerging markets the gap is even wider as wiping products can be considered as discretionary. In addition, certain value added grades, which are in Suominen's focus, grow even faster than the markets on average. Therefore, the market gives Suominen a solid foundation to grow in the coming years and the company should have a competitive product portfolio in order to exceed the market growth. In profitability perspective, organic growth should leverage on the group's fixed cost structure and also we should see improved GM-% through improving production efficiency.
- **Product mix transformation:** Suominen's has managed to increase the share of value added products from 50 % to some 60 % (of net sales) in its product portfolio in 2012-2017. Value added products typically carry a clearly higher GM-% than value for money grades, thus the product mix transformation should support the company's profitability. This progress should continue if the company manages to capitalize its recent investment in machinery (especially in the new line in Bethune), R&D and commercial activities (especially pricing). We estimate that Suominen aims to push share of value added grades to 65-70 % until 2021, which could lead to a couple of %-point expansion in EBIT-margin on the group level through higher GM-%
- **Low CAPEX needs:** Even if Suominen aims to change gear in terms of growth and profitability in the next years, the company argues that no major CAPEX is required. This is due to heavy CAPEX in 2015-2017, which is mostly uncapitalized (the new line Bethune is still in ramp-up phase), competitive old asset base and the product related strategy. Therefore, we expect Suominen's CAPEX to remain clearly below depreciation in 2018-2021. This should lead to hefty free cash flow (exceeding earnings). Even if we expect some deleveraging, the management may have extra cash to be allocated in M&A, greenfields or dividends at the beginning of the next decade. This could occur as a positive problem for the shareholders.
- **Value creation by M&A:** As a new element in the strategy update in 4/2017, the company disclosed that it is monitoring opportunities to expand to new geographical markets. The fast growing Asian market is definitely the hottest prospect (and the only given current geographical footprint) in this sense. We believe M&A is the most probable tool as M&A would allow faster positive cash flows than greenfield investments. "The new Suominen" has been created by 4 transactions, thus the company and also the current management have a solid track-record in this sense and from both sides of the table. Therefore, we see a fair chance the company can make value creating M&A in Asia in the coming years. However, every transaction must be evaluated separately in relation to quality and price of the target.

Risks

- **Raw material price risk**: As raw materials form a vast majority of Suominen's cost of goods sold (70-80 % of COGS, 60-70 % of total costs), the company is always carrying raw material price risk. This risk realized at the end of 2017 and at the beginning of 2018. Suominen is not hedging its raw material purchases but it is tackling this issue through raw material price clauses, which are included in half of the net sales (likely consisting mostly of large key accounts and/or baby care clients). The lag between the price increases varies from 2 to 5 months depending on the customers.

Investment profile, potential and risks

Overall the lag between the raw material price development and the actual price increases is fairly long. This can cause some fluctuation on quarterly level but should shield the company reasonably well over the longer time period as there has been no disrespect to the clauses. The other half of the contracts do not include raw-material clauses, which is an intentional business decision from the management. We believe Suominen has not included raw material clauses in deliveries where cost of its product represents only a small part of total costs of the customer's end product. In this type of deliveries, the customer's awareness of Suominen's raw-material price development may not be the best and the customers' resistance against price increases the most severe, which should give Suominen some pricing power. In addition, short-term or spot sales do not include raw-material clauses.

In general, we consider the company's hedging from changes in raw-material prices appropriate but raw-material prices increases require fast reactions. Thus, we see raw-material risks tolerable in the long time frame In addition, during the overcapacity raw-material price increases could cause severe problems as seen in baby care and flushables in 2017.

- **Losing a major customer:** Suominen's two largest clients brought 20 % and 14 % of the company's net sales in 2017 while 10 key customers accounted for 63 % of total net sales. Therefore, losing any one of these key customers would cause a significant drop in sales in the short term, which would have also an impact on profitability. However, the average customer relationship of Suominen is around 14 years, which implies very low customer turnover. Thereby, we see the overall risk of losing a major customer fairly small. However, large global brand houses and retailers barely give all their orders for one supplier but use 2-3 manufacturers. Customers' order allocation to suppliers may also vary, which may also create pressure on Suominen's sales even if the customer is not totally lost. We believe Suominen suffered this type of changes in 2015-2016.
- **Overcapacity:** Due to the relatively low price per volume unit, the production in nonwovens has to be located fairly close to the end user. This growing nature of the business and step-like capacity increases result always to a risk of local oversupply. Magnitude of the overcapacity would naturally depend on the amount of new capacity and growth rate of the product segment. Usually overcapacity leads to price erosion and/or higher unit costs in production. The latter fact is due to decreasing operational efficiency deriving from lowering capacity utilization. Overcapacity is especially poisonous in value for money products, where products are very homogenous as perceived in 2017 in baby care. Furthermore, there have been recently capacity expansions in North America and Europe, which will increase capacity also in some value added grades. This reflected also negatively on Suominen's results in 2016 and 2017. There are still some capacity expansion plans in the pipeline going forward but in the coming years supply/demand-balance should somewhat improve through growth. However, this risk remains actual for Suominen in the short and long term.
- **Competitive pressure by large competitors:** Even if Suominen is globally the leading player in wiping, it is still relatively small when looking at nonwovens as a whole. Therefore, there is always a risk for the competitive pressure from large competitors, which could dominate the business by economies of scale. There has been also consolidation in the fragmented sector, which may well continue. These two factors could change the competitive environment to a more unfavorable direction from Suominen's perspective in the long term.
- **Sensitivity to EUR/USD:** FX is a risk for Suominen as the company generates over 50 % of its sales and probably an even greater share of EBIT (excl. recent start-up losses in Bethune) from US. According to the company, a 10 % change in EUR/USD has a 2.5 MEUR impact on annual EBIT given the current business structure. The impact comes through translation to the income statement, which limits opportunities to hedge. Therefore, EUR/USD can have a significant impact on Suominen's reported sales and results. FX sensitivity is naturally a two folded coin but we consider in general FX driven earnings volatility a somewhat negative factor from investors' perspective.
- **Regulation** may become risk for Suominen in the long term as the company manufactures products from synthetic raw-materials and these products are difficult to be recycled. However, the company could use solely renewable raw-materials if end users were willing to pay higher prices, which would somewhat help to tackle potential changes with potentially tightening use of Suominen's raw-materials and/or products.

Investment profile

1. Organic growth
2. Competitive environment
3. New products
4. Low CAPEX needs
5. M&A (+/-)

Potential

- Growing and developing nonwoven markets support growth efforts
- R&D and commercial efforts gradually improve product mix (i.e GM-%)
- Moderate potential to push SGA-% down
- Potential expansion to Asia through M&A or greenfields

Risks

- Raw-material price risks
- Limited pricing power due to value chain position
- Competition is very fierce in certain segments
- Losing a large customer
- FX (EUR/USD) can cause volatility in earnings

Source: Inderes

Business model

Suominen is a traditional manufacturing company

Suominen operates in the manufacturing industry, which transforms fiber materials to nonwovens. In addition to manufacturing, the company takes care internally of product development, marketing and sales. Therefore, the business model is typical for a company in this type of manufacturing industry. Raw-materials the company purchases from the market.

Nonwovens can be produced by several technologies but Suominen utilizes mostly spunlace technology in its production. In addition, the new line Bethune is based on wet-laid technology resembling somewhat the paper-making process. We consider Suominen's technological choices adequate as spunlace and wet-laid technologies enable production of soft, smooth, stretch, absorbent, resilient and/or liquid repellent products, which are some key characteristics in value added grades. Thus, we do not believe Suominen aims to expand to new technologies in the near future but is determined to develop its current technology portfolio.

Consumers drive the business, customer base is fairly centralized

The company's key customers are global brand owners and private labels, which sell converted nonwoven products to consumers with their brands or private label trademarks. Thus, Suominen sells only B2B even if consumers are the end-users of the company's products. As a consumer driven business, demand of non-wovens is also fairly stable over the economic cycles. Traditionally consumers do not stop using nonwoven products during economic slowdown or recession but tend to switch their products to lower quality (i.e. cheaper price). Thus, economic cycles have some impact on Suominen from value and volume perspective but in general we consider the defensive and stable nature of the business positive for investors' perspective.

Suominen has not publicly disclosed its customers but we believe global consumer goods companies and retailers such as Procter&Gamble, Unilever, L'Oreal, Johnson&Johnson, Mölyncke Healtcare, Rockline Industries, Walmart and Carrefour could be the company's clients. As discussed, the two largest customers brought 20 % and 14 % of the group's net sales in 2017. In general, 10 biggest key accounts constitute over 60 % of Suominen's sales while some one third of the sales come from smaller sources. Therefore, the company's customer pool is fairly concentrated even if we believe Suominen's customer portfolio consist of altogether hundreds of customers.

Given the size of the key accounts (global sourcing) and centralized customer base, we argue that Suominen and other nonwoven manufacturers have fairly limited pricing power against clients. Neither fairly homogeneous nature of the products (especially in value for money segments) aid in this sense as tangible differentiation is difficult excluding certain value added segments. On the other hand, raw-material prices are determined by supply (controlled by few large players) and demand in global markets, thus there is neither pricing power to the opposite side of the value chain.

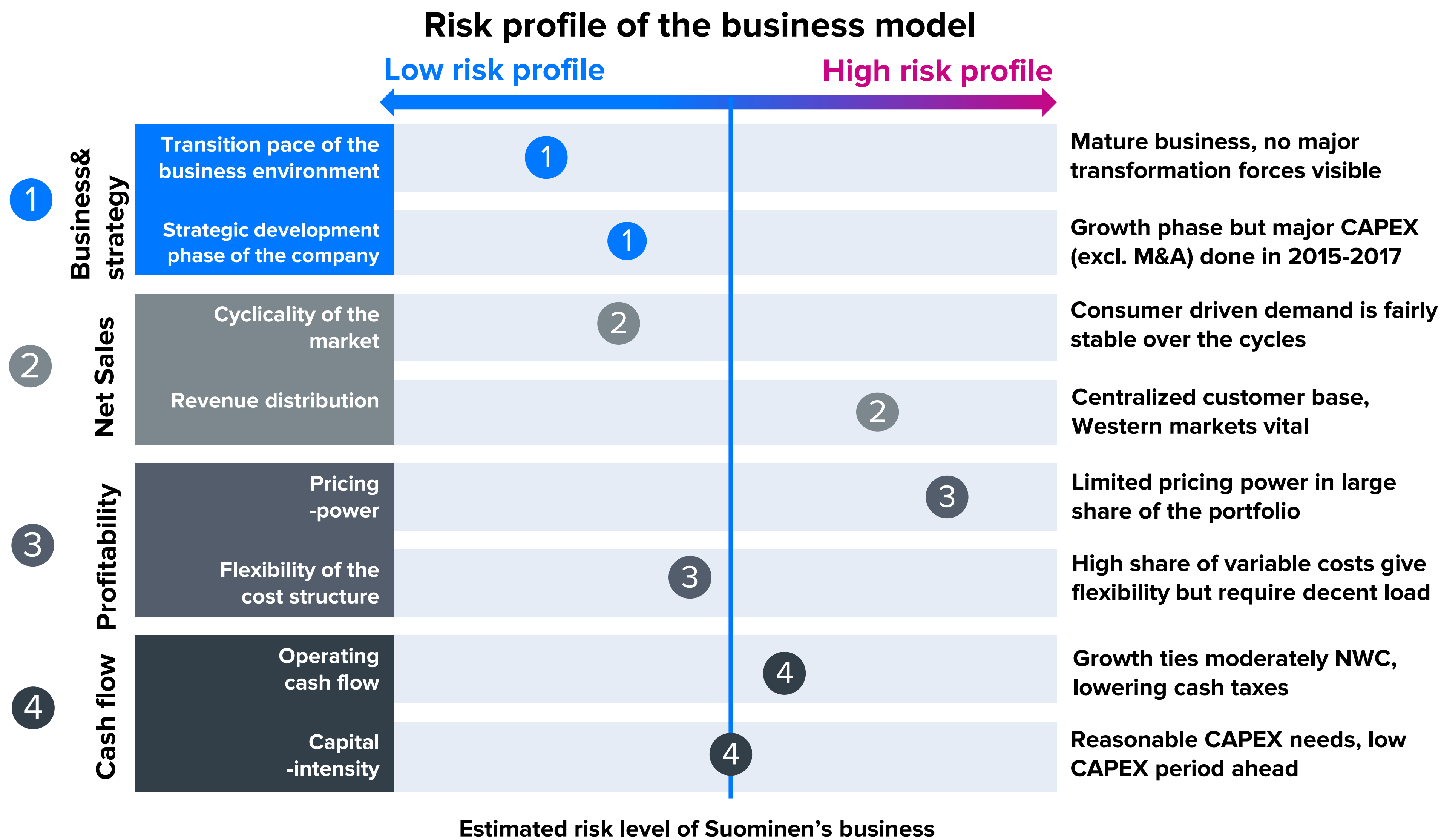
Despite imbalanced distribution of pricing power in the value chain, typical supplier-client relationships between nonwoven manufacturers and brand houses or retailers are relatively long. This indicates that brand owners and retailers are not very keen to change their suppliers despite their pricing power, which could be due to the indirect costs (i.e. product auditions) or uncertainty (delivery reliability and quality) that changes in well-established relationships with the supplier can cause. Also the delivery contracts are long, typically 2-3 years. Therefore, customers are not continuously bidding their contracts despite pricing power advantage.

Nonwovens are not very capital intensive in manufacturing industry scale

Due to characteristics of the industry, Suominen's GM-% is low. However, the company is efficient as the rebuilding phased pushed SGA-costs down. We argue that some 20 % of the company's costs are fixed and 80 % variable. Thus, there is reasonable flexibility in the cost structure but also some operational leverage on net sales growth. In general, effective capacity utilization (including decent load and reasonably large product lots) is one of the key factors in nonwoven industry like in every manufacturing business.

Suominen's tangible assets to net sales -ratio should be around 20 % in a normal situation (2016/2017 are abnormal due to investment in Bethune). Therefore, the nonwoven business is not very capital intensive compared to certain other manufacturing industries (i.e. steel, pulp). This enables fairly high ROCE-% or ROI-% with high single digit EBIT-% and also decent payout potential to shareholders. In addition, Suominen's net sales to NWC -ratio has been 8-10 % recently. Thus, neither NWC ties significant amount of capital in the business but naturally the growth is never free in the manufacturing industry.

Business model



Source: Inderes

Suominen's business environment

Customers*

Hundreds of brand houses or retailers

Unilever
P&G Procter&Gamble
Johnson&Johnson
Mölnlycke Health Care
Walmart
Rochline Industries

Competitors

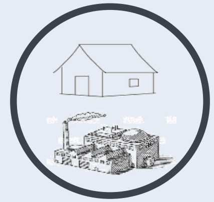
Berry Plastics
Freudenberg
Sandler
Jacob Holm
Kimberly-Clark

Suominen

"Suominen's purpose is also to develop nonwovens and expand their possibilities. We make nonwovens better."

Segments (2017 of net sales %)

Value for money wiping
41 %



Value added wiping
50 %

Care
9 %

Products

Baby wipes

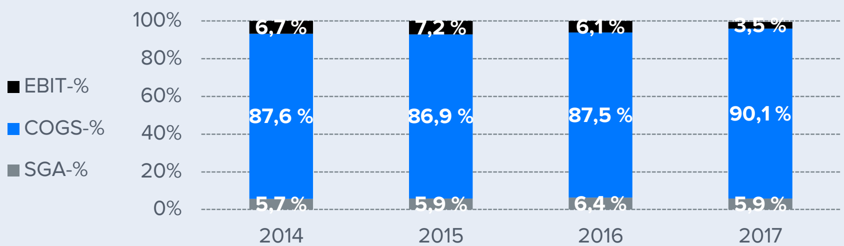
Personal care wipes

Workplace wipes

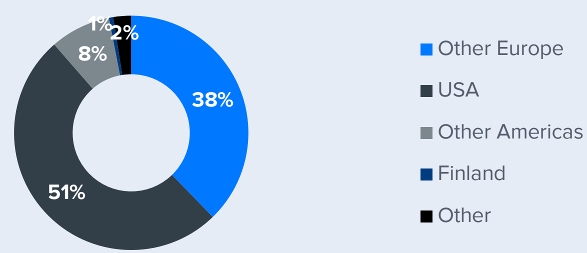
Household wipes

Medical&Hygiene

Cost structure 2013-2017



Geographical net sales split 2017



Source: Inderes, Suominen *Inderes' estimates of Suominen's potential customers, Suominen has not disclosed its customers

Strategy and financial targets (1/3)

Product driven growth strategy

Suominen has been executing its strategy that leans on global footprint and increasing share of value added products since 2012. The rationale of the strategy is fairly straightforward as value added products are carrying clearly higher GM-% and are less vulnerable to competition than value for money products. The company's recent profitability struggles in baby care has confirmed the strategy correct. In addition, Suominen is the market leader in wiping, has a strong market position in Western markets and is serving global customers. These factors and long term growth potential in emerging markets support global perspective in the strategy rather than focusing on certain areas.

As discussed, during the first strategy period of "the new Suominen" in 2012-2014 the company focused on internal efficiency and debt reduction while the second period in 2015-2017 shifted focus to growth investments and based foundation for growth. In April 2017 the company published its latest strategy update, which did not change the big guidelines but aims to increase speed of growth and profitability improvement. In addition, geographical expansion is on Suominen's radar in this strategy period of 2017-2021.

The following three factors are the cornerstones of Suominen's current strategy:

1) **Business excellence**

2) **R&D and new products**

3) **Personnel**

These cornerstones describe capabilities, which are required to drive the product mix transformation and correspondingly growth and profitability improvement. We consider the cornerstones adequate for product related strategy. Basically, the cornerstones underline the company's focus on understanding consumers (the customers' customer) and their needs. This is crucial to develop current products and new products that fulfill the needs. This process will be done in co-operation with the customers in order to share created value. Close co-operation with the customers should also make Suominen harder to replace as a supplier. Product development and customer co-operations require skilled and committed personnel, which is why the staff has become one of the cornerstones in the strategy.

There are no numeric targets for the mix

Suominen has published no numeric targets regarding the product mix but we believe that at the end of the on-going strategic period in 2021 baby care should bring around 25 % of Suominen's net sales leaving the rest roughly 75 % for the value added grades. We would like to remind that baby care still has a role in Suominen's portfolio despite weak margins as its high volumes give critical load for the production system. This is important from efficiency perspective. However, growth expectations lay especially on workplace, household and personal hygiene in wiping. In Care Suominen focuses on personal hygiene while growth outlook and the company's market position (incl. technologies) is weaker in medical.

R&D focuses especially on the new products

During the last strategy period, Suominen has built a R&D-team, which consists of some 20 members in US and Finland. Altogether, Suominen's R&D spending has climbed to over 1 % of net sales, which is in our opinion a good level in this type of industry. Therefore, we argue the company has sufficient human (incl. commercial resources) and financial capacity to drive product development and correspondingly product mix transformation in the coming years.

In R&D Suominen focuses on 6 key areas (fluid management, texture & patterning, disinfecting & sanitation, dispersibility & flushability, skin wellness, performance superiority) in order to improve current products and create new products. These focus areas are well in line with the product strategy in our opinion. The seventh focus area is cost innovation where the focus is especially in efficient use of raw-materials. Costs should always be a key priority in this type of highly competitive industry in our opinion.

The strategy does not require big investments

The strategy execution does not require significant investments as the company has disclosed that it expects CAPEX to be around 12 MEUR per annum on average (excl. potential M&A or greenfield investment) during the period. This is clearly below depreciation. To put this on perspective, Suominen has invested 106 MEUR in 2015-2017 of which some 65-70 MEUR have gone to the new line in Bethune. Basically 12 MEUR per annum on average enables the company to make maintenance (around 1 % of sales per annum) and some small quality improving and/or bottleneck removing investments. Moderate CAPEX outlook means also that Suominen is not looking to expand to new manufacturing technologies but rather focuses on developing its current technologies and add adjacent technologies to the portfolio. On the OPEX-side we expect some increase in SGA on absolute terms as the company grows.

Strategy and financial targets (2/3)

However, neither major SGA uplift should come during the strategy period and the management seems to be extremely focused to maintain tight cost control despite growth efforts. This is in our opinion a necessity due to fierce competition.

Asian expansion is on the radar now, M&A the most likely tool

As discussed, Suominen disclosed in the strategy update, that they will examine opportunities to expand their business to new market regions, primarily to Asia. Asia is the fastest growing nonwoven market (some 7 % p.a.) and expansion would support Suominen's global position, thus we took the very unsurprising addition positively. Another and most likely complementary option to geographical expansion is to grow South American operations in Paulinia by debottlenecking the current production line or building new line to the plant.

Suominen could basically execute the expansion though greenfield investment or M&A. We believe that the latter has become a primary option as M&A enables positive cash flows faster. In addition, M&A brings also new customers in the portfolio to which the company could add potentially some new volumes from the current globally operating key accounts. This could give a decent load and mix for the M&A-target fast while the greenfield on a new market would require much more patience. On the other hand, a greenfield investment would give the company more degree of freedom with technology and geographical location but these factors do most likely not offset advantages of M&A. The potential M&A-target must have reasonable technological fit to take advantage of Suominen's product portfolio, which is one of the key elements in the Asian expansion. We believe Suominen is looking for financially healthy targets while acquiring turnaround cases is unlikely even if they were cheap.

There are several options in Asia

Geographically the huge Chinese market is one potential option. China has also reached GDP level in which the market begins to absorb also value added grades. In addition, there could be less competitive and faster growing options for example in India, Vietnam, Indonesia, Philippines or Thailand. Japan is a developed market with existing value added demand but we believe the company is not willing to commit the next big strategic investment to a slowly growing market.

We believe there could be at least 10-20 potential M&A-targets for Suominen in Asia of which the majority are located most likely in China. Valuation of the potential targets remain unclear at this stage but the recent deals have been closed with EV/EBITDA LTM 6x-8x (i.e. Ascania/Mondi 6x, Berry Plastics/Avintiv 8x). We argue that prices going below this range would be attractive for a healthy target while going towards the upper end of the range or over the range would require new technology to scale to other plants as significant synergies are difficult to reach. Suominen has been valued historically at EV/EBITDA 6x, which gives a good reference point to acceptable valuation range.

We expect Asian expansion at the second half of the strategy period

We believe the potential Asian expansion will most likely happen at the latter half of the strategy period. First, the company remains busy with Bethune for the next 2-3 years in order to capitalize the investment fully. Secondly, there is still non-capitalized potential in Paulinia, which also advocates to keep short term focus on the current asset base. Thirdly, currently valuations are in general high, which may make value creating M&A challenging from the buyer's side. Despite that, we believe the company is ready to act if lucrative targets appear for sale earlier.

After heavy investments and deteriorating profitability in 2016-2017 Suominen could also need some time to create more financial flexibility to their balance sheet as the management seems to be conservative with leverage. If the company can change the profit trend, we argue Suominen should have financial flexibility to make small to medium size M&A (EV some 30-70 MEUR) at least at the beginning of the next decade. Raising equity or other equity instruments would also allow bigger deals. However, we do not believe Suominen is necessarily looking for large market consolidating or synergistic M&A but rather for portfolio balancing and/or a "bolt on" target, which would fill in the geographical hole in Asia. We argue the latter option is financially feasible without new equity during the strategy period.

The strategy is credible

We consider Suominen's strategy adequate and believe it guides the company to the right direction. The company's competitive edge should be in product portfolio and supply chain management efficiency as we argue it is very difficult to create any sustainable advantage by CAPEX (i.e. long lifecycle of technology, limited efficiency differences, low share of fixed costs). Therefore, reaching margins over the industry average require success in these two factors.. In addition to the strategy itself, Suominen should have resources and capabilities to execute the strategy effectively but neither the best strategy is fully immune to competitive environment.

Strategy of Suominen

Strategic drivers	Strategic actions	Financial targets
Supportive long term market growth outlook	• Rebuilding in 2012-2014 and investments in 2015-2017 to position for growth	• Net sales growth 6 % on average per annum in 2017-2021
Emerging markets and niches grow fast	• Product mix transformation to find fast growing niches in US and Europe, Brazilian expansion in 2014 and potential to Asian expansion in 2018-2021	• ROI-% of 15 % on average in 2017-2021 • Gearing between 40-80 %
Leading market position	• Reinforcing global footprint, active management of global key accounts	• Dividend payout at least 30 % of profit for the period
Fierce competition	• Positioning in value added grades, cost innovations in baby care and R&D, pricing efforts, efficiency improvement	• If strategy execution is successful, net sales will be over 600 MEUR and EBIT-% over 10 % in 2021
➢ Suominen has a competitive product portfolio ➢ The company has made CAPEX and OPEX investments to position for growth ➢ Low SGA costs, tight cost control, continuing focus on operational efficiency	➢ The company has a foundation to grow, lots of uncapitalized potential in current asset base ➢ Reinforced R&D function has proved its ability to create new products, commercial focus to be sharpened ➢ Fierce competition has hit margins recently but the company has proved earlier it can reach healthy margins	➢ Especially 2021 net sales and profitability targets are very ambitious ➢ EBIT-% expansion should come mostly from product mix but some volume and SGA leverage is required too ➢ No major CAPEX is required to reach the targets but debt must be reduced to create financial flexibility for M&A

Source: Inderes

M&A strategy of Suominen

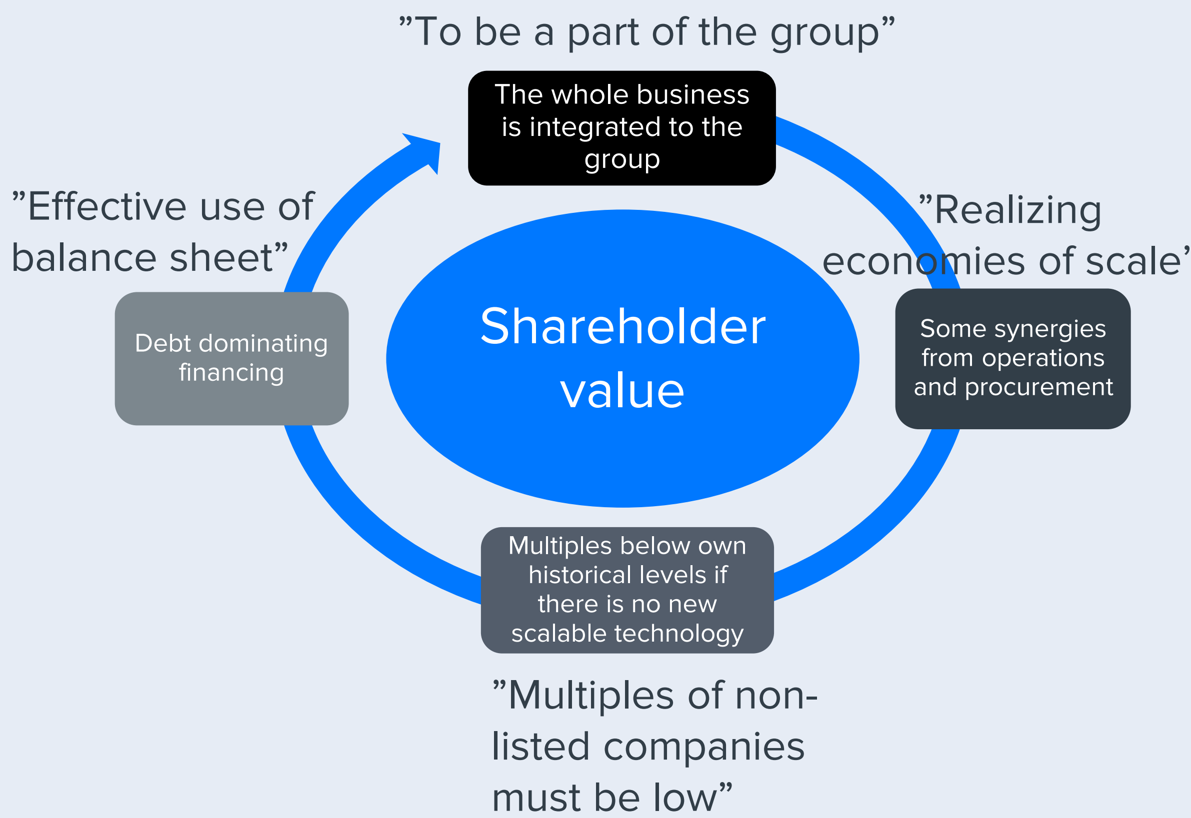
Suominen's criteria for M&A

Supports the strategy
- Expansion to new markets (i.e. Asia)
- Technological fit
- Main focus on Suominen's current products (wiping)

Financially healthy
- Strong local position, good customer portfolio
- Decent financial track-record from near history

Fits to the business model
- No overlaps with the current structure
- Opportunity to integrate in to the group

Shareholder value creation by M&A



Strategy and financial targets (3/3)

Financial targets and dividend policy

Suominen revised its financial targets for the on-going strategy period of 2017-2021 in the strategy update in April 2017. They are:

- **Growth:** 6 % organic growth on average p.a
- **Capital efficiency:** ROI-% of 15 % on average
- **Leverage:** Net gearing between 40-80 %
- **Dividend payout:** At least 30 % of its profits for the period

Moreover, Suominen has disclosed that its net sales will exceed 600 MEUR and EBIT-margin 10 % in 2021 if the strategy execution is successful.

Growth target reflects double the market growth

Suominen's relevant markets (Europe and Americas) are expected to grow some 3 % p.a. in volume in the coming years. Thus, the organic growth target is challenging but not unreachable as Bethune's new line should bring in new volumes and product mix improvement continues. Historically the company has reached over 6 % organic growth in 2013 but was left clearly behind the target in 2014-2017. This describes that the target sets the bar high. We argue that the company should aim for slightly faster volume growth than the market in order to reach the target level. The rest must come from value side as increasing share of value added products increase average prices and boost reported growth. However, part of mix improvement will probably go to offset price pressure, which the bulkiest products has faced and will face over long term. Thus, clear mix effect is required to drive average prices up. 6 % organic growth per annum would raise net sales to some 540 MEUR in 2021. The company has stated that the over 600 MEUR net sales goal in 2021 is reachable without inorganic growth but reaching the target organically requires an even more challenging net sales CAGR of almost 9 % in 2018-2021. We consider this unlikely without M&A at this point.

ROI-target less challenging than 10 % EBIT

2021 EBIT-% target of over 10 % is extremely challenging in our opinion in this type of industry. To illustrate the height of the bar, Suominen has reached slightly over 7 % EBIT-% in 2015 and neither of its main competitors have reached double digit margins. Comparing to 2013-2017 average, the company should improve its EBIT-% over 4 %-points (2013-2017: average of EBIT-% 5.7 %) while the gap is much more wider in relation to current start point (Q1'18 LTM EBIT-% 2.6 %). First, product mix transformation should drive GM-% up. This should be clearly the greatest contributor in profitability improvement. Second, the company should grow its volumes at least at the pace of the market, which would increase GM-% through operational efficiency and leverage to fixed production cost structure. Third, growth should improve slightly SGA-% as we expect overhead costs to grow more gently than net sales (cutting absolute SGA is most likely not sustainable). Therefore, we argue that the company should reach some 15-16 % GM-% and 5-6 % SGA-% in order to exceed 10 % EBIT-% (2017: GM-% 7.4 %, SGA-% 5.9 %). We consider the target ambitious even if a part of the current value added portfolio reaches 15 % GM-%.

As CAPEX outlook is clearly below depreciation for the next years, Suominen's balance sheet should not grow significantly during the strategy period (excl. potential M&A or greenfield) even if the growth will most likely tie some NWC. Thus, we argue some 5-6 % net sales CAGR and gradual EBIT-% improvement to around 8 % is enough to meet the ROI-% -target of the strategy period in single year. Thus, we consider the ROI-target clearly easier to reach than 2021 EBIT-% goal. However, we remind that average ROI-% of 15 % would represent excellent performance given the industry fundamentals.

Balance sheet gives flexibility for Suominen

Due to Suominen's position in the value chain, we believe that it is businesswise necessary to maintain a strong balance sheet. However, the company operates in a somewhat capital intensive manufacturing industry, where certain leverage is required to ensure optimal return on equity. Currently, the company is in the upper part of target leverage range despite heavy CAPEX in 2015-2017. Thus, Suominen's financial position is solid even if the investments (i.e. Bethune) are mostly on the balance sheet but do not generate any cash flow yet.

Despite recently increasing net debt, we see no major worries with the balance sheet. However, it has become crucial that the company improves its profitability to stop increase in net debt and keep balance sheet risks away. In addition, as the Asian expansion is on the radar we believe Suominen would like to have some financial flexibility even if we believe that the management does not exclude going out of the range temporarily. Correspondingly, Suominen should not have difficulties to meet its current cautious payout target but increasing the dividend requires change in the profit trend.

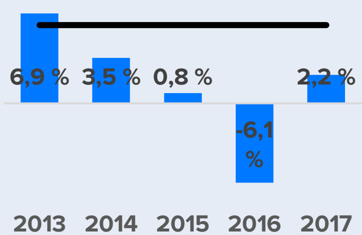
Strategy and financial targets 2017-2021

Growth

Growth over 6 % on average p.a.

Q1'18

-1.5 % LTM

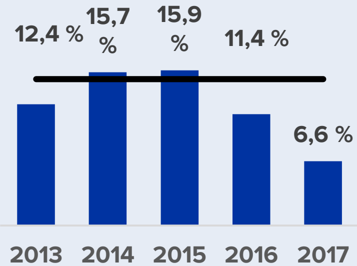


Capital efficiency

ROI-% of 15 % on average

Q1'18

4.6 % LTM

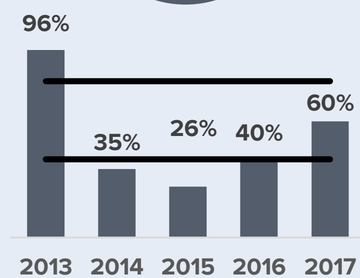


Leverage

Gearing in the range of 40-80 %

Q1'18

68 %

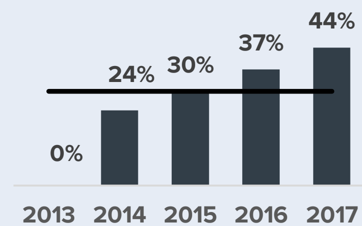


Dividend policy

At least 30 % of profits for the period

2017

44 %



If the strategy execution is succesfull, Suominen's net sales exceed 600 MEUR and EBIT-% 10 % in 2021 (2017: net sales 426 MEUR, EBIT-% 3.5 %)

Source: Suominen, Inderes

Nonwoven industry and competition (1/3)

Suominen is focusing on a few segments in nonwoven markets

Suominen operates in a global nonwoven market and the overall market size is estimated to be 26 billion USD. This is of course divided between various segments as nonwovens have several end-use applications in different solutions. Suominen operates in wiping through its Convenience BA while Care BA has focused on selected niches in medical and hygiene segment. Suominen is not present in other segments of the market.

Wiping (incl. sub-segments of baby care, workplace, household, personal hygiene) is globally a market worth of some 2.1 billion USD. Suominen's Convenience BA is present all over the wiping market. Medical is a small market worth of some 800 million USD but hygiene is the largest single segment in the nonwoven market worth of some 6.5 billion USD. In Care Suominen is focusing only in selected applications (for example fluid management in hygiene) and does not even try to compete all over the segments as Suominen's technology portfolio supports fairly sharp focus areas.

Nonwovens is a local business

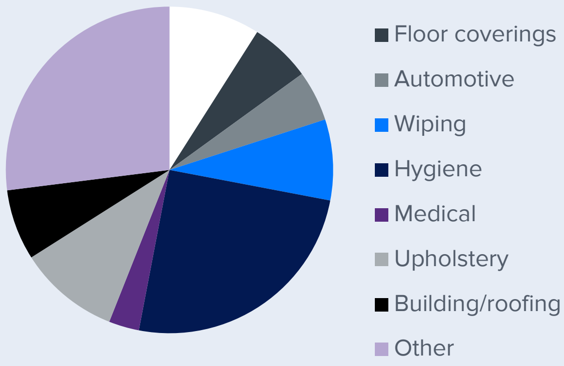
As the nonwovens are fairly low cost and high volume products, they are unable to carry significant logistics costs. Thus, the nonwoven business is local by nature and production must be continental or in certain cases even more local. More expensive value added products can carry somewhat higher logistics costs than the cheapest value for money products, which slightly expands the potential market area at the high end. However, we argue overseas sales is still challenging in the business. This is proved also by Suominen's geographical sales split as only 2 % of net sales came from the regions in which the company did not have production in 2017. The same goes for the raw materials, which the manufacturers purchase continentally.

We believe locality reduces somewhat Suominen's global operational synergies and ability to utilize its key accounts consisting of large brand companies without expanding its plant portfolio geographically. However, unsustainably high transportation costs shield Suominen's European and North American markets from Asian low cost exports. This limits competitive pressure in the company's main markets. Therefore we argue that the local nature of the industry is a two-folded coin for Suominen.

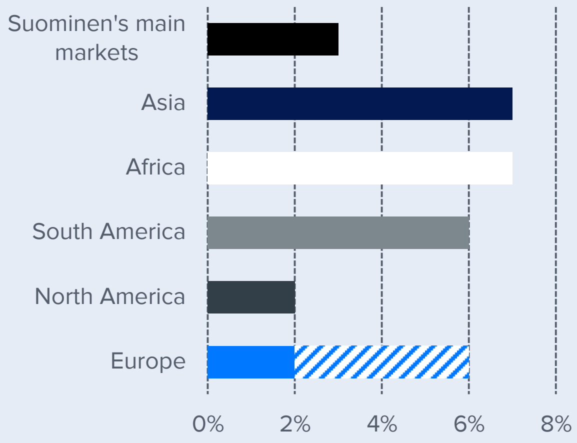
Historical market growth exceeds GDP growth

Demand for nonwoven products has grown historically 2-4 percentage points faster than GDP in developed Western markets (US and Europe). This has been driven by several sustainable trends such as population growth and aging, increasing consumption on personal health and urbanization. In the future, these trends will be increasingly present in developing markets, which have a clear impact on the market growth expectations in future. According to Suominen's market outlook, demand for nonwovens in wiping is expected to grow around 2 % per annum in North America, 2-6 % in Europe, 6 % in South America and 7 % in Asia and Africa. These are expected growth rates for volume but we argue that value of the market should grow slightly faster than volume as value added grades grow the fastest, which could offset long term price pressure that value for money grades will face. The figures make approximately 3 % expected CAGR for Suominen's main markets (Europe and Americas) and some 5 % globally for the next years in volume terms.

Nonwoven market segments



Geographical growth outlook



Source: Inderes, Suominen

Nonwoven industry and competition (2/3)

These figures represent the overall growth for non-woven demand while growth varies greatly between end-use segments. This gives Suominen the opportunity to focus on the most interesting and fastest growing segments. Generally, value added categories of Convenience and Care have higher growth outlook than value for money products. In other words, 60 % of the company's current offering are expected to exceed the average market growth in the future. Thus, the company should have room to exceed overall market growth in its most profitable product categories, which supports Suominen's aims to exceed market growth and to improve profitability. The results will depend on the company's success in strategy execution but the demand outlook is definitely supportive in the long term.

Fragmented markets in global scale

Given Suominen's sales in Conveniece and the mentioned market size, Suominen has a 20 % market share in wiping, which makes the company a global market leader in the segment. As a whole, the wiping market is very fragmented globally. The four biggest tier 1 competitors (Berry Plastics, Kimberly-Clark, Jacob Holm, Sandler) in wiping have together some 30 % market share, thus the five biggest hold only slightly above half of the market. The other half is controlled by small local players. In medical and hygiene Care BA is a minor player and does not have any significant market share. Also, these markets are fragmented structurally.

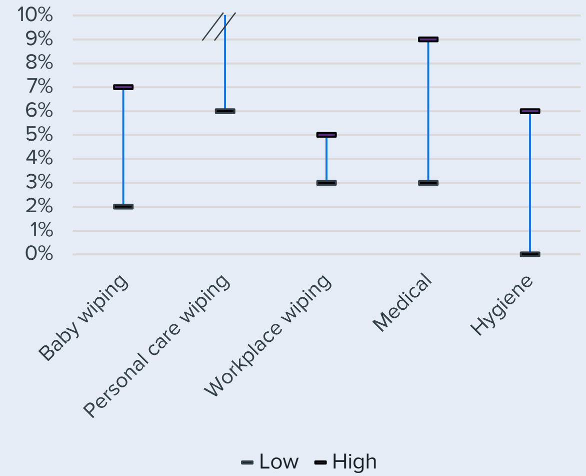
There is overcapacity in European baby care and flushables, other grades are in reasonable balance

The whole wiping business has been suffering modest overcapacity in Europe, which was built during the boom years of 2003-2008. Clear overcapacity were cut by growth but recent investments have made the matters again clearly worse especially in baby care in Europe, where there is currently overcapacity and the balance is still weakening as Akinal is ramping up a line in Estonia currently. Magnitude of the problem is difficult to estimate but there could be overcapacity up to 10 % in European baby care. This would represent a severe problem for manufacturers as the it will take 5-7 years to reach the balance through growth. Therefore, capacity closures seems to be the only way to make the European baby care market healthier fast but so far no players are committed to cease capacity yet. North American baby care market is somewhat better balance even if competition is fierce also on the other side of the Atlantic Ocean.

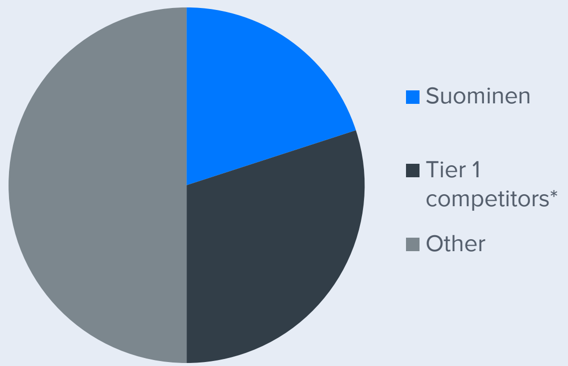
Flushables (used to be excellent business for Suominen in 2014/2015) have become another problem grade as fast growth rate of the product has attracted manufacturers to build several new lines to the segment in Europe, China and US. in the last years. This has commoditized the product very quickly and lead to price erosion. We believe there is significant overcapacity in flushables globally currently even if the market grows still fast. There is decent market balance in other value added grades currently despite certain recent investments. In general, North American markets are somewhat tighter compared to Europe also in value added business.

The South American market is growing fast but the market cannot always absorb all the volumes that come to the markets unevenly due to start-up of a greenfield plant. This is due to absolute market size in tons, which is clearly smaller in South America compared to North America and Europe. Thus, supply/demand-balance may be temporarily unfavorable but the fast growth should even out imbalances fairly quickly.

Growth outlook of segments



Market share of Suominen



*Tier1 competitors (global players): Berry Plastics, Kimberly-Clark, Jacob Holm, Sandler

Source: Inderes, Suominen

Nonwoven industry and competition (2/3)

In addition, South America is a developing market and Suominen is basically launching value added grades to the market after rebuilding was completed in Paulinia plant in 2015. Therefore, it will take time to reach on group level significant value added sales in Brazil. Recently, Brazilian nonwoven markets remained fairly robust despite the challenges in the economy resulting from declining commodity prices in 2015-2016. This confirms the defensive nature of the business. Recently Brazilian economy has been recovering, thus Suominen should be operating in fairly favorable environment is South America right now.

Capacity increases are inevitable

Capacity increases are natural and inevitable as the markets keeps on growing but they always impact the market balance at least in the short term. For example, the capacity additions in 2015-2016 in US and Europe kept Suominen's volumes more or less flat in 2014-2016 (no changes in raw-material use) and pushed sales prices clearly down in 2016-2017.This describes the fierce competitive environment in the sector, which will remain as such also in the future.

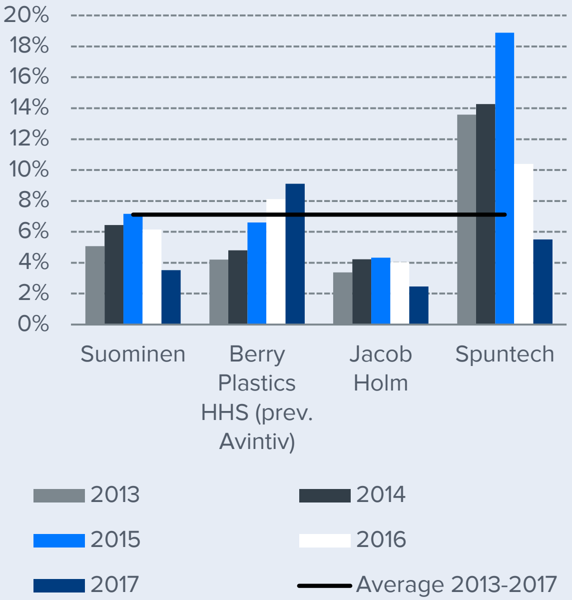
We argue that one typical new production line in Europe or North America will raise up local production capacity some 2-3 % on wiping level. Basically given the size of the market, one line per continent annually is required to meet demand growth but several lines would create market pressure if old capacity was not simultaneously ceased. This is the big picture on overall market conditions while in single product grades situation may vary significantly. Therefore, industry investments and supply/demand-balances are definitely factor to follow in Suominen.

Performance versus sector peers'

Even if Suominen faces competition from global players such as Kimberly-Clark, Jacob Holm, Sandler and Berry Plastics (prev. Avintiv) in wiping, it is difficult to compare Suominen's financial performance to other players directly. This is due to fact that straight competitors are private equities or parts of big corporations, which have different businesses that reduce comparability. In addition, different product segments can reduce comparability. However, we have benchmarked Suominen's financial performance against certain peers, which compete against Suominen at least to some extent. We have included in the comparison Berry Plastics HHS-division, Jacob Holm and Spuntech.

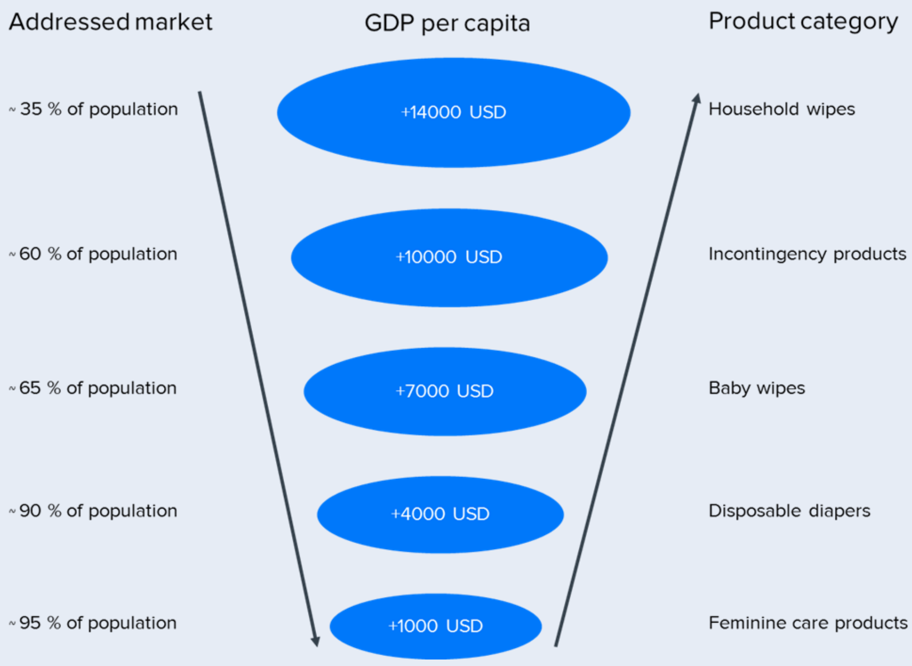
Suominen has performed recently in line with peers in terms of profit margins, which confirms our view on the company's decent relative position. The company has also outperformed Jacob Holm, which is a direct competitor. This is somewhat a relief for investors as the company seems to be competitive despite the recent negative profit trend. However, despite adverse trend, earnings of the sector seem to be still positive. This may keep the players reluctant to cut capacity in problematic grades in the near future, which would be the fastest tool to return sector's margins back to healthy levels. 5-year average of peer groups' EBIT-% is 7.1 % (5.3 % excl. Spuntech), which gives some impression on the long term margin potential in the business. In addition, exceptional long term performance of Spuntech illustrates profit potential value added niches as the company used to be very focused niche player at least at the beginning at the on-going decade.

Suominen vs. peers



Industry and Suominen’s competitive forces

Global reach of nonwoven products



Competitive forces of Suominen

+ Global market leader in wiping
+ Competitive product portfolio
+ Effective R&D function
+ Delivery reliability (several sites)
+ Up to date plant portfolio
– Minor player in medical&hygiene
– No presence in Asia
– Production mostly in high cost countries
– Limited technology portfolio

Source: Suominen, Inderes

Financial position (1/2)

Low GM-%, competitive SGA-level

Suominen's GOGS are typically some 87-89 % of sales (GM-% 11-13 %) and we estimate that some 70-75 % of Suominen's COGS are raw-materials. Raw-materials such as pulp (mostly fluff), viscose and polypropene are mainly priced in the global markets with global market prices. The second big variable component in COGS is energy, which could constitute around 10 % of COGS. Price of energy is determined also in the markets but energy markets are more local than for example raw-material markets. The third large variable cost component in COGS must be wages of production personnel, which could represent another 10 % total COGS. Almost entire production staff of Suominen is located in the developed countries where wages are high. However, as the nonwoven business is local by nature, Suominen's position is not significantly worse in relation to competitors. Basically, high wages could be competitive disadvantage in Europe where Suominen could face competition from Eastern European manufacturers, which have lower personnel related costs. Rest of the COGS is depreciation of production assets (majority of depreciation). Altogether, Suominen has no clear cost advantages in COGS, thus GM-% expansion must come from the mix side.

In the SGA the largest item is administration expenses. The second biggest item is sales & marketing while other items (R&D, other costs and other income) are around 1 % or less of the net sales. Overall these SGA costs accounted for 6.4 % of sales or 27.2 MEUR in 2017. We argue this is a fairly competitive level and the management has maintained very tight cost control even if growth has increased absolute SGA cost base in 2014-2017 and will most likely increase it also in future. However, Suominen reached its lowest SGA-% of 5.5 % in 2013. This proportional level should be reachable for the company with topline growth.

No major financial costs burden but the tax rate remains high if Trump does not help

As Suominen's balance sheet is decent, the net financing costs of the company are on a reasonable level of around 1 % of the net sales. This includes interest payments and other fixed financing related costs. However, high taxes used to burden Suominen's net results due to country mix but US tax reform fixed the tax issue to large extent. Therefore, Suominen's normalized tax rate should be around 25 % going forward (30-35 % before US tax reform) but there is still some uncertainty due to complexity of the tax reform and currently loss making operations in Bethune. The company has some losses to reduce in Europe, which could slightly limit their taxes further in the coming years if the company can improve profitability of certain units.

Investment cycle makes free cash flow deviate

As Suominen depreciates its asset base fairly fast the company's EBITDA-% has been some 4-5 %-points higher than EBIT-% at 8-11 % recently. Therefore, the company has generated solid cash flow from operations of some 22-28 MEUR per annum in 2015-2017. This should continue as NWC growth should be moderate and paid interest costs and taxes should not differ significantly from figures in the income statement. However, the company's free cash flow depends heavily on their investment cycle. Recently FCF has dropped to the negative side (strong FCF during the rebuilding) but should improve clearly from 2018 onwards when CAPEX drops back below depreciation, as discussed earlier. However, free cash flow recovery requires improved profitability.

No write down risks in non-current assets

The majority of Suominen's non-current assets consist of tangible assets, which are mostly plants and machinery. At the end of Q1'17 tangible assets were 130 MEUR consisting mostly of machinery. At the end of Q1'17 the balance sheet contained some 15 MEUR of goodwill representing 12 % of equity attributable to shareholders. Other intangible rights were 18 MEUR at the end of Q1'17. We see no write-down risks in these items as the company depreciates its assets fairly fast and units carrying goodwill have been generating well positive cash flow in the last years.

Vendor loan is an interest bearing receivable

On the non-current asset side, the fourth meaningful non-current item is a loan receivable of 3 MEUR (Q1'18). This is related to Flexibles' divestment as Suominen gave a vendor loan for the buyers to finance the transaction. The item is treated as an interest bearing receivable in accounting. The receivable is divided to a loan note maturing at the end of 2018 and which has an interest of 6 % p.a. and a subordinated loan note maturing at the end of 2024 with an interest rate of 9 % p.a.

Financial position (2/2)

Thus, the company should get some 0.4-0.5 MEUR per annum as financial income from the vendor loan. We see the receivable current as Flexibles' (currently Amerplast) have managed to improve its financial performance and Amerplast has also paid its debt back to Suominen in schedule. In addition, Suominen has an earn-out of 1 MEUR based on Flexibles' financial performance but there is still major uncertainty over its realization and timing (could be 1-4 years). In addition, Londsdale Capital Partners will most probably aim to exit from Amerplast after the successful turnaround. This would allow also Suominen to sell its equity stake of 19.9 % in Amerplast potentially with a one-time profit but visibility to potential divestment remains very limited.

NWC has tied capital recently

On the current asset side, the three biggest items were inventories (43 MEUR), trade receivables (58 MEUR) and cash (17 MEUR) at the end of Q1'18. Suominen was able to trim down its NWC (including payables in liabilities) clearly during the rebuilding phase to 8-10 % of net sales but at the end of 2017 the NWC to net sales ratio had climbed to 13 %. We believe that the current level is somewhat elevated for Suominen even if growth and rising raw-material prices tend to tie up more capital in NWC (especially on inventories). Therefore, we expect the NWC will remain on uphill track on absolute terms but proportional level of 10 % of net sales should be reachable for the company in our opinion when start-up in Bethune is completed. Other items in current assets have fairly limited significance on the group level.

The company is financed with equity and bond

In the liabilities side Suominen has 127 MEUR of equity attributable to owners of the parent company. The hybrid bond that the company used to finance Paulinia acquisition was converted to equity at end of 2017 as we expected. During the last year (Q1'17-Q1'18), the company's equity has decreased almost 13 MEUR but the adverse development derives from FX driven (appreciating EUR/USD) asset revaluation. Therefore, the has been no drama with equity recently but the recent drop in equity highlights that FX (EUR/USD) has also a clear impact on the company's balance sheet.

Suominen's non-current liabilities included a 95 MEUR bond finance (carrying amount). This consists of five-year 85 MEUR bond (nominal) issued in October 2017 and 15.7 MEUR residual (nominal) of the 75 MEUR bond the company issued in 2014 and did not manage to buy back in the tender offer in September 2017 (the difference between the carrying amount and sum of nominal values is valuation difference). The 85 MEUR senior bond has a coupon rate of 2.5 %, while the 15.7 MEUR residual of 75 MEUR bond is yielding 4.4 % for the bond holders until September 2019. As discussed, we consider the company's cost of financing competitive. In addition, the company had a 10 MEUR short term bank debt from 100 MEUR long term revolving credit facility (RCF). Therefore, the company has enough liquidity to execute its strategy in the next years.

Current liabilities are dominated by payables of 60 MEUR (positively slightly above receivables).

Total assets were at 308 MEUR at the end of Q1'18, thus Suominen operates with reasonably light and current balance sheet given the scale of the business.

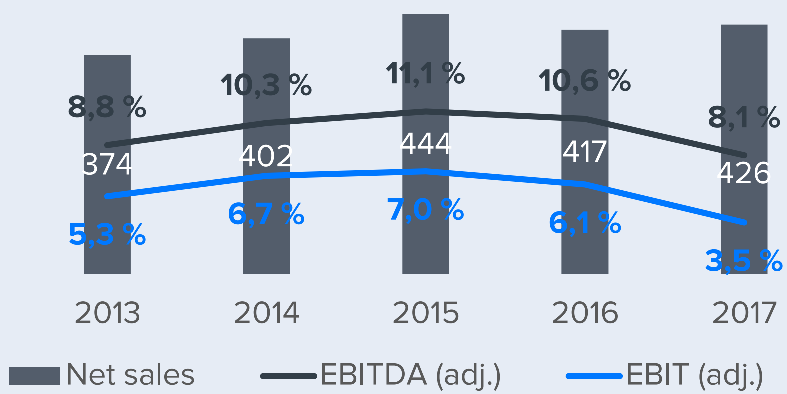
Further increase in leverage would be undesirable

Suominen's gearing was 69 % and equity ratio 41 % at the end of Q1'18. Gearing is in the upper range of the company's target of 40-80 %, thus the company is still well between the boundaries. Profitability is also a key to improve net debt to EBITDA -ratio (Q1'18 LTM) that has climbed to somewhat elevated level at 2,6x. Altogether, we see yet no worries with the balance sheet but further worsening of the balance sheet figures would be undesirable in our opinion.

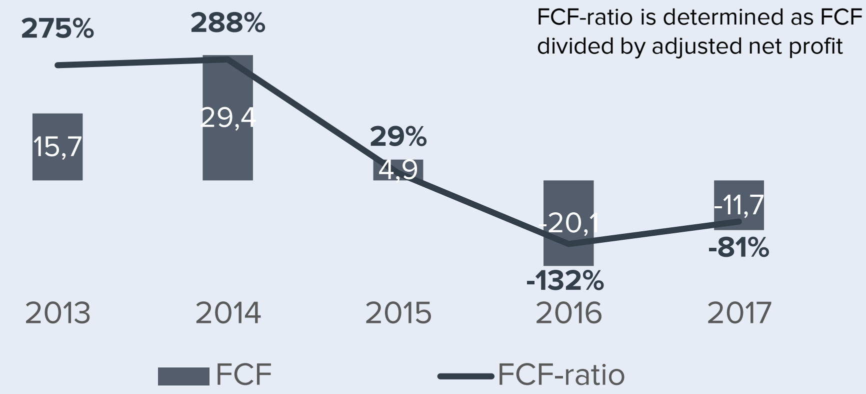
As mentioned, we argue that Suominen needs certain leverage to keep WACC-% reasonable and to boost return on equity. We argue the company's sweet spot should be the lower end of the current target range. In addition, the growth strategy may include M&A, for which Suominen needs certain financial headroom. Therefore, we expect the management aims to slightly deleverage the company in the next years to maintain flexibility to execute long term growth strategy as planned.

Financial position

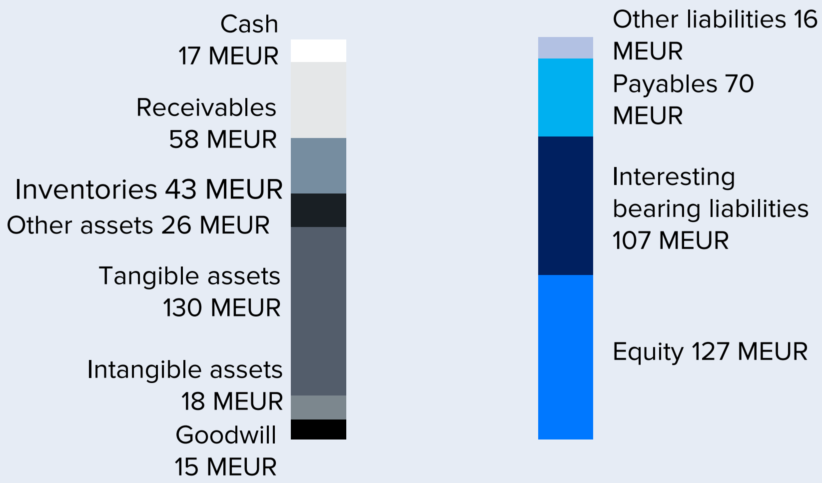
Development of sales and profitability



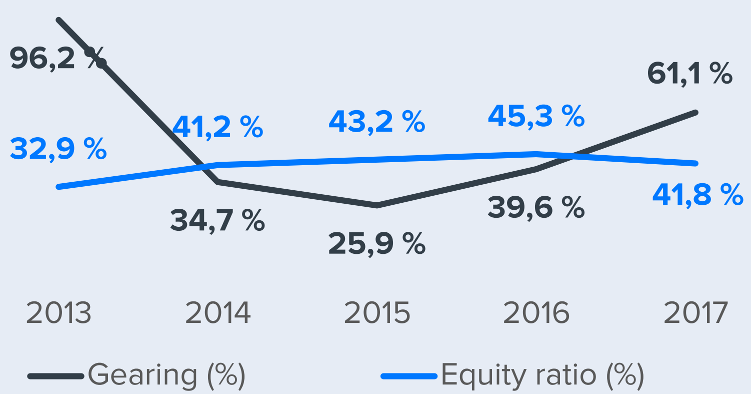
Free cash flow



Balance sheet structure at the end of Q1'18



Historical development of balance sheet



Source: Inderes, Suominen

Estimates (1/3)

Macroeconomic outlook

Suominen's main relevant macroeconomic drivers consist of GDP growth and consumer confidence. Considering Suominen's main markets, GDP growth accelerated in North America and Europe in 2017 and reached also a good level of over 2 % on absolute terms. Accelerating growth derived mostly on ECB's on going QE and FED's loose monetary policy that supported consumer spending and recently also investments.

The macroeconomic big picture has remained mostly intact at the beginning of 2018 even if Europe has reported somewhat weaker than expected figures in Q1'18. US growth gained speed from the tax reform at the beginning of 2018. Consumer confidence has remained at all time high in both continents. Brazil has been recovering as rising commodity prices have supported the economy even if uncertainty has remained over internal issues in the country. The main risks are political as politicians have failed to fix structural issues especially in Europe while US' efforts to balance global trade may lead to trade war. In addition, debt levels are high in several countries, which cause certain uncertainty. Also geopolitical issues with North Korea, Middle East and Russia remain as a risk factor.

From macroeconomic perspective our profit estimates for Suominen are based on IMF's and OECE's GDP forecasts, which expect US' GDP to grow 2.9 % in 2018 and 2,7-2.8 % in 2019. Corresponding figures for Eurozone are 2.3-2.4 % in 2018 and 2.0-2.1 % in 2019. Therefore, we expect the supportive macroeconomic environment in Suominen's major markets for the next years in the base case.

2018 estimates

Suominen got a weak start for 2018 since the company's net sales decreased 5.6 % to 106.6 MEUR in Q1. Topline growth was burdened by FX (appreciating EUR/USD) while good trading conditions reflecting GDP growth and high consumer confidence lead to all time high volumes. However, prices increased only slightly as mix did not improve and decreasing prices in baby care dragged average price. As raw-material prices increased and new line in Bethune reported negative gross-profit, GM-% fell 4.7 %-points to 7.4 % while SGA-% dropped 0.7 % to 5.9 % at least partly due to FX. Thus, Suominen's EBIT was 1.8 MEUR in Q1, which corresponds to a EBIT-margin of 1.5 %. EPS went on red at -0.01 euro per share as net financing costs were high due to FX and while taxes were minimal due to negative PTP. As discussed the new line in Bethune improved its performance month on month but certain technical challenges remained (and lead to weak volumes) and the line did not reach positive GM in Q1 as the management expected at the end of last year.

The management retained its guidance for FY'18 in the Q1'18-report. Thus, Suominen expects that its net sales and comparable EBIT will be higher compared to year 2017 (2017: net sales 426 MEUR, comparable EBIT 15.0 MEUR). As discussed, demand outlook has remained healthy but on the other hand pricing suffers still from recent capacity increases in the certain segments while raw-material prices have remained on moderate uphill track. This may still put pressure on margins, which the company tries to offset by new program focusing on pricing, performance and planning.

World GDP growth in 2007-2017 and world GDP growth estimates 2018e-2020e

Source: OECD, IMF, World Bank

Estimates (2/3)

In addition, ramp-up continues in Bethune but the company did not give any new estimate when break-even profitability is reached. Thus, the company's profit outlook remains challenging and visibility weak regarding Bethune but also the "old portfolio".

Currently we estimate Suominen will grow 1.7 % and report 433 MEUR net sales in 2018. Gradually increasing volumes from Bethune will drive net sales growth especially in H2 while we estimate pricing efforts will put some pressure on volumes in other plants (this would be most likely positive from profitability perspective as prices increases are vital). Pricing and mix support topline slightly while the worst FX burden seems to be behind at least temporarily. We estimate GM-% to remain basically flat at 10.1 % as raw-materials offset slight mix improvement, pricing efforts and progress in Bethune. We estimate SGA-% to remain flat at 6.4 % in 2018 due to strict cost control and FX aid. Therefore, we forecast comparable EBIT of 16 MEUR for Suominen in 2018. We have made moderately negative estimate revisions recently due to recent raw-material price development and uncertainties related to pricing and Bethune.

As illustrated, our estimates are only slightly above the last years' levels and correspondingly the company's guidance. As safety margins are thin, visibility to pricing and start-up in Bethune is weak and pricing power questionable, we would like to highlight that there is a profit warning risk around the company. As Suominen is well behind the guidance after Q1 and the margin pressure does not seem to be over, the profit warning risks will remain until the end of year in all cases. This increases investors' risks on the short term even if potential magnitude of the warning diminish gradually as the year goes on.

Below EBIT we forecast Suominen's net financing costs to be at -5 MEUR in 2017, which means basically 1 MEUR/Q net financing costs for Q2-Q4. This is a fairly normalized level considering the company's debt structure and other annual financing costs.

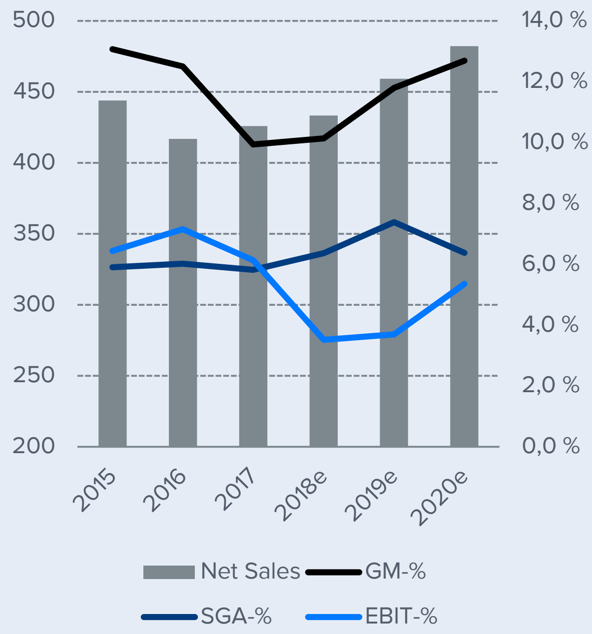
We expect tax-rate to drop to 25 % due to US tax reform. Altogether, we estimate EPS to decrease to 0.14 euro (the company accounted significant one off tax gains in 2017 due to US tax reform). However, we expect Suominen to keep its dividend at 0.11 euro per share as we believe the company aims to avoid dividend cut even if payout (2018e: 79 %) increases clearly above the minimum payout of company's dividend policy (at least 30 % of profits). FCF should recover 2018 as CAPEX normalizes even if NWC ties most likely some capital due to increased inventory value. This will push gearing down moderately.

2019 estimates

We expect positive progress that should begin in H2'18 to continue in 2019 as market fundaments reflecting good GDP growth in Europe and US should support the sector also in 2019. However, Bethune's new line should give clear support to volumes and mix in 2019. We expect that Suominen should be able to improve its product mix somewhat faster in 2019 as new value added products launched in 2015-2017 have had time to take off and Bethune investment enables faster mix transformation. Pricing and raw-materials remain that the risk but the margin pressure should somewhat even out as time goes on (unless raw-material inflation again accelerates)

We estimate net sales of 459 MEUR for Suominen in 2019. This corresponds for 6.0 % growth, which comes once again from volume and value driven mostly by the Bethune investment. Our GM-% estimate for 2018 is 11.8 % which reflect product mix transformation and easing margin pressure.

Estimates 2015-2020e



Estimates (3/3)

We see that SGA will continue to face pressure upwards in 2019 on absolute terms but operating leverage should keep relative figure flat at 6.4 %. Therefore, topline and GM-% expansion should boost Suominen's EBIT to 24.6 MEUR in 2019, which corresponds satisfactory EBIT-% of 5.4 %.

Financing costs should remain somewhat intact at around 4.2 MEUR/a (large share of bond financing). We estimate Suominen's tax-rate to remain at 25 % in 2019. Altogether, we expect Suominen to make EPS of 0.26 euro in 2019. Positive progress of EPS should return dividend on uphill track and we estimate Suominen pays out 0.12 euro DPS, being in line with the company's dividend policy (2019e: 46 % payout). In addition, CAPEX remain moderate in 2019, which correspondingly should pull FCF upwards. Therefore, net profit and strong FCF should push gearing to lower end of the company's target range (2020e: gearing 41 %).

2020 estimates

2020 should not offer any changes to the big picture of nonwoven markets that remain growing steadily supported by the previously named drivers even if GDP growth keeps on slowing down slightly in the base case. We expect Suominen's growth to remain above market growth in 5 % as gradual improvement of product mix continues and Bethune reaches its full volume potential. Our net sales estimate is 482 MEUR FY'20.

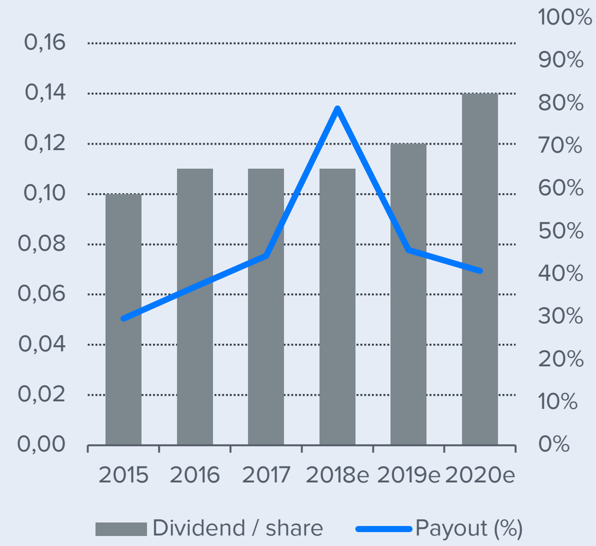
We expect Suominen's GM-% to reach 12.7 % in 2020 as improving product mix and efficiency support GM-% expansion, which is still partially offset by fierce price competition and raw-material prices. We forecast SGA-% to remain flat. Topline growth and GM-% expansion will lift Suominen's EBIT to 30.5 MEUR in 2020 in our estimates, which corresponds decent EBIT-% of 6.3 %. In 2020 we estimate net financial items of 3.8 MEUR due to diminishing interest bearing debt in the balance sheet and normal tax rate of 25 %. FY'19 EPS estimate is 0.34 and DPS estimate 0.14 euro. FCF remains strong and the balance sheet keeps on strengthening, which gives the management even more options to capital allocation (possible M&A in Asia). However, visibility to 2020 is very limited as time lag is long and competitive environment unpredictable.

Long term estimates

From 2021 onwards we are expecting growth to be in range of 2.0-4.1 %, which represents the average growth rate of the industry and GDP growth in the main markets over the long term. We estimate EBIT margin to peak at 6.6 % in 2021 and to decrease to 4.5-6 % over long term when competition intensifies. Thus, our long term estimates stay significantly below the company's 2021 targets. Therefore, there could be clear upside in medium term estimates if the company can demonstrate its ability to pull its profitability to new levels in the coming decade. However, the company's recent adverse progress advocates being cautious with the estimates over longer time frame.

These estimates are based on organic growth even if we believe that Suominen will make M&As at the latest at the end of the current strategy period and/or over the long term. Thus, potential transactions could have significant impact on estimates but their timing is naturally impossible to estimate. In addition, long term estimates are non-cyclical averages as neither timing of cycles is possible to forecast.

Dividend estimates 2015-2020e



Estimates

Quarterly earnings	2016	Q1'17	Q2'17	Q3'17	Q4'17	2017	Q1'18	Q2'18e	Q3'18e	Q4'18e	2018e	2019e	2020e
Net sales	**416,9**	**112,9**	**112,1**	**102,3**	**98,7**	**426,0**	**106,6**	**113,1**	**108,0**	**105,6**	**433,3**	**459,4**	**482,3**
Nonwovens	*416,9*	*112,9*	*112,1*	*102,3*	*98,7*	*426,0*	*106,6*	*113,1*	*108,0*	*105,6*	*433,3*	*459,4*	*482,3*
EBITDA	**44,1**	**10,9**	**8,9**	**9,4**	**5,1**	**34,3**	**6,5**	**9,2**	**11,2**	**10,2**	**37,2**	**45,2**	**49,6**
Depreciation	-18,5	-4,7	-4,6	-4,8	-5,4	-19,3	-5,0	-5,4	-5,4	-5,4	-21,2	-20,6	-19,2
EBIT (excl. NRI)	**25,6**	**6,3**	**4,4**	**4,6**	**-0,3**	**15,0**	**1,5**	**3,8**	**5,8**	**4,8**	**16,0**	**24,6**	**30,5**
EBIT	**25,6**	**6,3**	**4,4**	**4,6**	**-0,3**	**15,0**	**1,5**	**3,8**	**5,8**	**4,8**	**16,0**	**24,6**	**30,5**
Nonwovens	*25,6*	*6,3*	*4,4*	*4,6*	*-0,3*	*15,0*	*1,5*	*3,8*	*5,8*	*4,8*	*16,0*	*24,6*	*30,5*
NRI	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*
Net financial items	-3,2	-0,2	-0,3	-1,1	-1,0	-2,6	-1,9	-1,1	-1,1	-1,1	-5,0	-4,2	-3,8
PTP	**22,4**	**6,1**	**4,1**	**3,5**	**-1,3**	**12,4**	**-0,3**	**2,8**	**4,8**	**3,8**	**11,0**	**20,4**	**26,7**
Taxes	-7,2	-1,9	-2,0	-1,7	7,6	2,0	0,0	-0,7	-1,2	-0,9	-2,9	-5,1	-6,7
Minority interest	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0
Net earnings	**15,2**	**4,2**	**2,1**	**1,8**	**6,3**	**14,5**	**-0,4**	**2,1**	**3,6**	**2,8**	**8,1**	**15,3**	**20,0**
EPS (adj.)	**0,30**	**0,08**	**0,04**	**0,03**	**0,12**	**0,27**	**-0,01**	**0,04**	**0,06**	**0,05**	**0,14**	**0,26**	**0,34**
EPS (rep.)	**0,30**	**0,08**	**0,04**	**0,03**	**0,12**	**0,27**	**-0,01**	**0,04**	**0,06**	**0,05**	**0,14**	**0,26**	**0,34**

Key figures	2016	Q1'17	Q2'17	Q3'17	Q4'17	2017	Q1'18	Q2'18e	Q3'18e	Q4'18e	2018e	2019e	2020e
Revenue growth-%	-6,1 %	*8,7 %*	*3,0 %*	*-1,4 %*	*-1,7 %*	2,2 %	*-5,6 %*	*0,9 %*	*5,6 %*	*7,0 %*	1,7 %	6,0 %	5,0 %
Adjusted EBIT growth-%	-18,2 %	*12,9 %*	*-49,3 %*	*-41,4 %*	*-107,6 %*	-41,4 %	*-75,3 %*	*-13,2 %*	*26,4 %*	*-1914,3 %*	6,9 %	53,4 %	23,8 %
EBITDA-%	10,6 %	*9,7 %*	*8,0 %*	*9,2 %*	*5,2 %*	8,1 %	*6,1 %*	*8,1 %*	*10,4 %*	*9,7 %*	8,6 %	9,8 %	10,3 %
Adjusted operating profit-%	6,1 %	5,5 %	3,9 %	4,5 %	-0,3 %	3,5 %	1,5 %	3,4 %	5,4 %	4,6 %	3,7 %	5,4 %	6,3 %
Net profit-%	3,6 %	3,8 %	1,9 %	1,8 %	6,4 %	3,4 %	-0,3 %	1,8 %	3,3 %	2,7 %	1,9 %	3,3 %	4,1 %

Source: Inderes

Key estimate parameters	2016	Q1'17	Q2'17	Q3'17	Q4'17	2017	Q1'18	Q2'18e	Q3'18e	Q4'18e	2018e	2019e	2020e
Net sales growth (%)	-6,1 %	8,7 %	2,9 %	-1,3 %	-1,7 %	2,2 %	-5,5 %	1,0 %	5,5 %	7,0 %	1,7 %	6,0 %	5,0 %
*Volume growth (%) **	-3,4 %	7,5 %	7,0 %	3,0 %	2,0 %	4,9 %	4,0 %	3,0 %	4,5 %	5,0 %	4,1 %	5,0 %	4,0 %
*Price/Mix growth (%) **	-2,6 %	-1,0 %	-5,0 %	-1,0 %	1,4 %	-1,4 %	0,5 %	2,0 %	3,0 %	4,0 %	2,4 %	2,5 %	2,5 %
*FX change (%) **	-0,1 %	2,6 %	1,0 %	-3,3 %	-5,1 %	-1,2 %	-10,0 %	-4,0 %	-2,0 %	-2,0 %	-4,5 %	-1,5 %	-1,5 %
Gross-margin (%)	12,5 %	12,1 %	10,6 %	10,6 %	6,4 %	9,9 %	7,4 %	10,0 %	11,7 %	11,5 %	10,1 %	11,8 %	12,7 %
SGA-%	6,4 %	6,6 %	6,7 %	5,5 %	6,7 %	6,4 %	5,9 %	6,6 %	6,3 %	6,9 %	6,4 %	6,4 %	6,4 %

Suominen's main profit drivers and their outlook

Positive driver

Negative driver

Neutral driver

Nonwoven demand
High consumer confidence / good GDP growth outlook

Costs / raw-materials
Raw-material prices are picking-up, moderate inflation in other cost items

Competition / price
Capacity grows in some grades while there is strcuturally weak pricing power in certain grades

EUR/USD
EUR/USD has appreciated recentlly and global FX forwards expect fairly flat EUR/USD going forward

Product mix
Investments in machinery and innovation enable gradual product mix improvement. Markets support the efforts in the long term

Suominen

Source: Inderes

Valuation and recommendation (1/2)

Valuation cornerstones

After the rebuilding and corresponding turnaround case, investors categorize Suominen as a growing manufacturing company. Thus, Suominen will be valued by income statement based valuation multiples like P/E, EV/EBITDA and EV/EBIT in the markets. Correspondingly, cash flow based valuation by P/FCF is also a feasible metric. In addition, P/B is always a good multiple in the manufacturing industry even if in our opinion Suominen should not be directly valued by the balance sheet as the company operates in somewhat less capital intensive segment of manufacturing industry. Dividend yield is also secondary metrics for a growth company like Suominen.

The following factors have positive or neutral impact on Suominen's valuation in our opinion:

- **Trends supporting nonwoven business** give the company fairly good organic growth outlook (above GDP growth) and correspondinly value creation potential
- **Defensive nature** of the consumer related business keep cyclicality of the company limited, which we consider positive from valuation perspective
- **Position as global leader** supports the valuation even if the industry is fragmented
- **Balance sheet of the company** is still in decent shape and we see no additional balance sheet related risks at the moment

The following factors have negative impact on Suominen's valuation in our opinion:

- **Revenue streams are fairly centralized** in customer and geographical sense, which elevates slightly risk premiums
- **Difficult value chain position** from pricing power perspective increases risk level to some extent
- **Profit warning risk FY'18 and the recent negative profit trend** lower acceptable valuation in the short term
- **Free float and liquidity of the share** have been recently limited, thus we argue extra liquidity premium is required for the stock

Given that background, we argue Suominen should be valued with a P/E-ratio of 13x-15x in the current organic growth phase. Correspondingly, acceptable EV/EBITDA-ratio is somewhere between 6x-7x in our opinion, which is in line with Suominen's historical valuation. However, slight premium to historical EV/EBITDA level is acceptable going forward as tax burden has decreased. Acceptable EV-based valuation range is supported also by recent M&A-activities in the sector since Blackstone sold Avintiv to Berry Plastics for LTM EV/EBITDA 8x in the summer of 2015 while few months earlier Mondi acquired Ascania for LTM EV/EBITDA 6x. These deals give a good indication for valuation levels in the business even if several factors have impacted on transaction prices in M&A-cases.

Valuation multiples

Suominen's P/E-ratios for the next two years based on our estimates are 24x and 13x while corresponding EV/EBITDA-ratios are 7x and 6x. Given our valuation range for Suominen, we see FY'18 multiples elevated while FY'19 figures are close to neutral. Therefore, we see no clear upside in the share looking 12 months forward if the company can return uphill track as we expect. Dividend yields are on decent level at 3.2 % and 3.5 % but the dividend outlook depends heavily on the profit trend.

P/B-ratio is 1.4x while EV/S-multiple is 0.6x (2018e). These figures are below the company's medium term averages but neither multiple is actually low given current earnings run-rate. Therefore, balance sheet and volume based valuation can not yet give support for the share if risks related to profit growth and its magnitude realize. This makes the company's risk/reward-ratio somewhat more negative in our opinion and does not courage to look further.

Relative valuation is only an indication

As Suominen's direct competitors in wiping segment are private equity owned companies or parts of large corporations consisting of several business segments, valuing the share in relation to the peer group is challenging. However, we have collected a peer group, which includes a few listed companies from the other segments of nonwoven industry. On the other hand, we have included in the peer group also companies from other sectors, which have similar business model (manufacturing), type of products (not branded consumer related goods) and value chain position to Suominen. However, the peer group is far from complete in terms of size and type of companies, thus we keep its weigh limited in our valuation.

Valuation and recommendation (2/2)

Suominen is valued by premium compared to peer group by FY'18 income statement multiples while FY'19 multiples are on clear discount. Therefore, relative valuation seems to be also fairly neutral in our opinion. However, we argue some discount is justified as Suominen's business portfolio is smaller and less widely spread than the peer group on average, which makes its risks profile somewhat higher. In addition, the peer group in general seem to be better short term track-record and profit growth outlook, which also justify certain discount for Suominen.

The markets seem to accept a relatively high valuation for this type of defensive consumer related companies on absolute terms currently. This supports also Suominen's valuation in our opinion but given fairly gross valuation (2018e: median P/E 16x, median EV/EBITDA 8x) of loosely related peer group, we do not believe relative valuation will drive Suominen's share higher short term. Therefore, relative valuation does not make us too excited and we keep on paying more attention on absolute multiples.

DCF-valuation

We give a fairly low weight on DCF-value in our valuation as the model is very sensitive to changes in parameters. DCF-model, based on our long term estimates, gives a value of 4.35 euro per share for Suominen. This reflects long term potential that is in the share. However, we do not believe the share reaches its DCF-value before the company can demonstrates that it can return to organic growth and lift margins back to levels around 5-7 %. Weight of terminal value is reasonable at 54 % in the model. WACC-% of the model is at 7.7 % and cost of equity at 9.0 %. Risk free interest rate is 3.0 %, market risk premium 4.75 %, liquidity premium 1.25 % and beta 1.0.

Clear medium term potential if 2021 targets will be reached

Despite neutral valuation in the short term, there could be clear medium term potential in a positive scenario in Suominen. We estimate Suominen should make almost 0.70 EUR EPS in 2021 if the company reaches 600 MEUR net sales and 10 % EBIT-% in 2021 (net financing costs 1.0 % of sales and tax-rate 25 %). With this impressive track-record in 2021, Suominen could be easily valued by P/E 15x. This would give share price of over 10.00 euro per share at the end of 2021. As the share trades currently at slightly above three euros, investor's would get almost 200 % share price appreciation and dividends of three years if the extremely positive scenario realizes. Thus, TSR for three and half year investment would correspond to a very impressive IRR of roughly 40 % per annum. However, this scenario seems very distant given the company and its business fundaments' current state.

Target price and recommendation

We retain Suominen's target price **3.50 euro** and recommendation at **reduce.** We argue 12 month forward looking valuation is fairly neutral in our opinion while risks related to short term profit growth outlook remain elevated. These risks and lack of the support levels for the share price does not advocate taking risks with Suominen in our opinion currently.

As discussed, the positive scenario would give clear upside for the share medium term but we are not yet willing to stretch short term valuation too much before the company can provide more evidence that growth will exceed clearly market growth and margins will recover at least to levels of 2015-2016.. Therefore, we continue to wait somewhat higher margin of safety or reduced risk profile (i.e. change in the profit trend) before considering higher target price and positive recommendation for the company even if Suominen's long term investment story contains still certain interesting elements.

Valuation multiples and sensitivity analysis

Valuation	2013	2014	2015	2016	2017	2018e	2019e	2020e
Share price	2,40	4,00	6,20	4,14	4,42	3,40	3,40	3,40
MCAP	118	197	313	212	258	198	198	198
EV	194	243	354	277	341	275	259	240
P/E (adj.)	17,9	17,7	18,9	14,0	16,4	24,4	12,9	9,9
P/E	20,7	19,3	18,4	14,0	16,4	24,4	12,9	9,9
P/FCF	4,3	12,5	36,9	-9,1	43,5	11,8	7,8	6,9
P/B	1,5	1,8	2,5	1,5	1,9	1,4	1,4	1,2
P/S	0,3	0,5	0,7	0,5	0,6	0,5	0,4	0,4
EV/S	0,5	0,6	0,8	0,7	0,8	0,6	0,6	0,5
EV/EBITDA	5,8	5,4	6,4	6,2	9,7	7,5	5,7	4,8
EV/EBIT	9,8	8,2	9,5	10,5	21,4	17,7	10,5	7,9
Payout (%)	0,0 %	24,2 %	29,7 %	37,1 %	44,3 %	78,9 %	45,7 %	37,9 %
Dividend yield-%	0,0 %	1,3 %	1,6 %	2,7 %	2,5 %	3,2 %	3,5 %	3,8 %

Source: Inderes

Value matrix 2018e (2018e net sales and net debt)

		EBITDA-%					
		7,8 %	8,2 %	8,6 %	9,0 %	9,4 %	9,8 %
EV/EBITDA	5,0	1,75	1,93	2,10	2,27	2,45	2,62
	5,5	2,09	2,28	2,47	2,66	2,85	3,04
	6,0	2,43	2,64	2,84	3,05	3,26	3,47
	6,5	2,77	2,99	3,22	3,44	3,67	3,89
	7,0	3,10	3,35	3,59	3,83	4,07	4,31
	7,5	3,44	3,70	3,96	4,22	4,48	4,74
	8,0	3,78	4,05	4,33	4,61	4,89	5,16

Source: Inderes

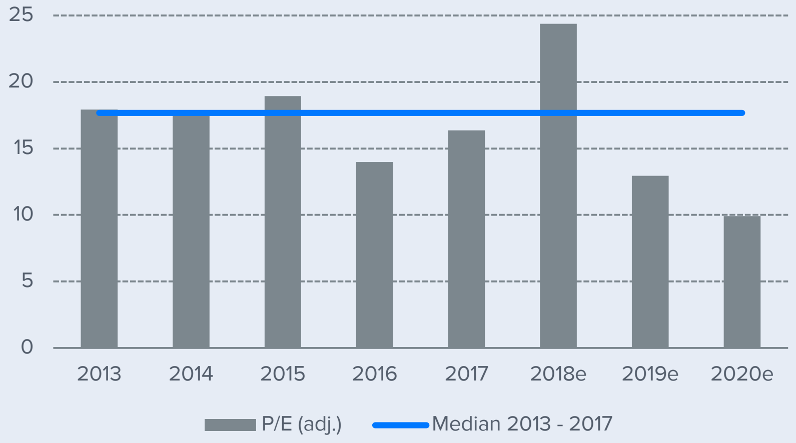
Value matrix with different sales and GM-% (2018 number of shares)

		440	450	460	470	480	490
		10,5 %	11,0 %	11,5 %	12,0 %	12,5 %	13,0 %
P/E	11	1,77	2,24	2,73	3,23	3,74	4,27
	12	1,93	2,44	2,97	3,52	4,08	4,66
	13	2,09	2,65	3,22	3,81	4,42	5,04
	14	2,25	2,85	3,47	4,11	4,76	5,43
	15	2,41	3,06	3,72	4,40	5,10	5,82
	16	2,57	3,26	3,97	4,69	5,44	6,21
	17	2,74	3,46	4,21	4,99	5,78	6,60

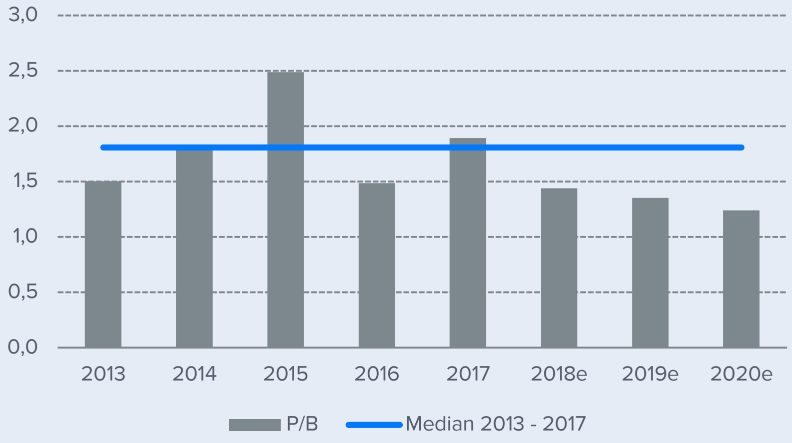
***SGA 29.6 MEUR, 4.2 MEUR net financing costs, 25 % tax-rate)**

Historical valuation of Suominen

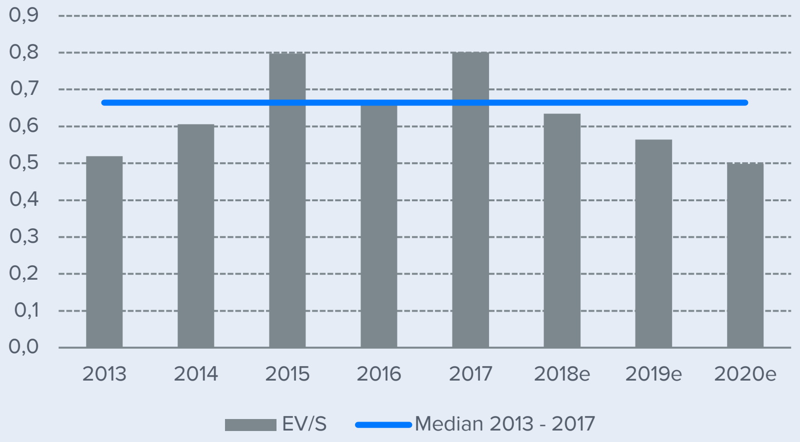
P/E (adj.)



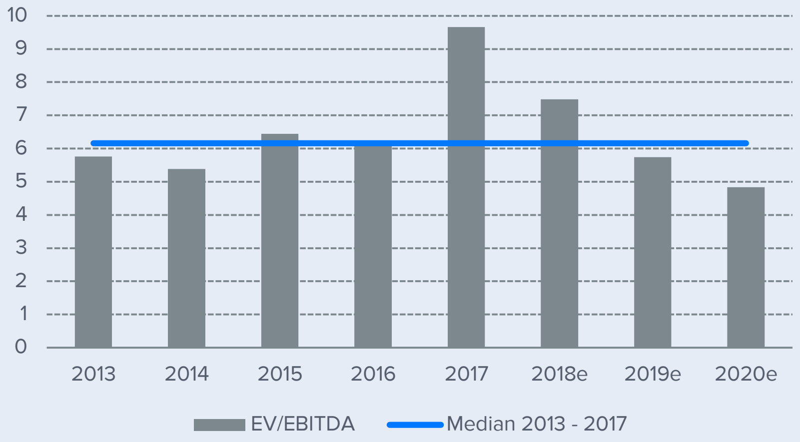
P/B



EV/S

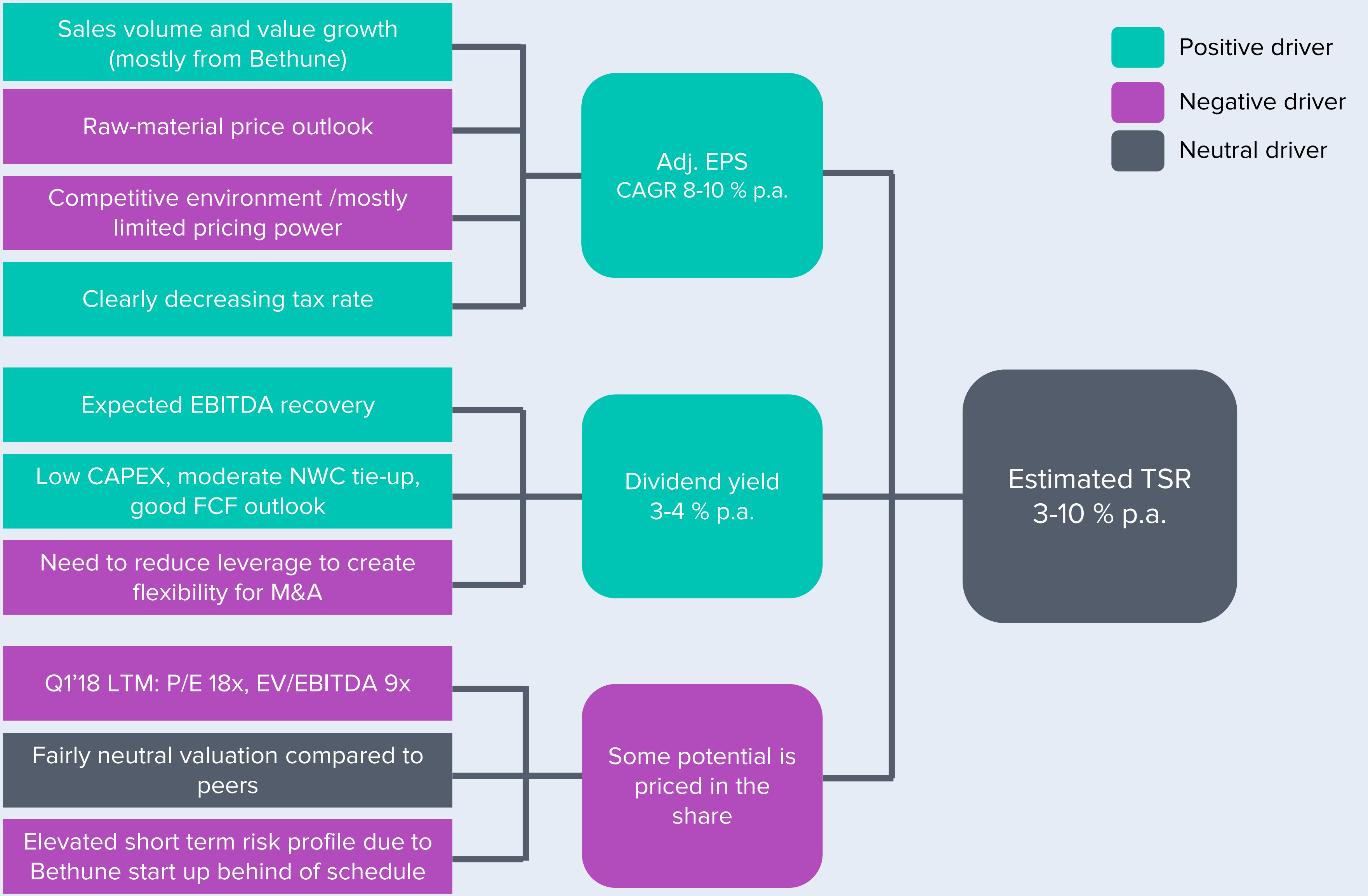


EV/EBITDA



Source: Inderes

Suominen's value drivers in 2018e-2020e



Source: Inderes

Peer group valuation

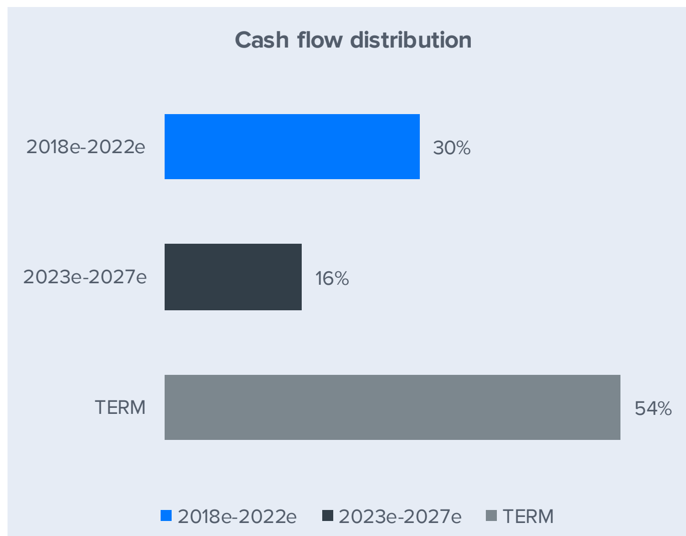
	MCAP	EV	EV/EBIT		EV/EBITDA		EV/Sales		P/E		Dividend yield-%		P/B
Company	**MEUR**	**MEUR**	**2018e**	**2019e**	**2018e**	**2019e**	**2018e**	**2019e**	**2018e**	**2019e**	**2018e**	**2019e**	**2018e**
Suominen	197	285	20,2	12,8	8,0	6,4	0,6	0,6	32,2	16,3	3,3	3,6	1,4
Huhtamäki	3335	4147	14,8	13,0	10,3	9,2	1,3	1,2	16,0	14,1	2,8	3,1	2,5
Duni	577	654	12,4	11,4	9,1	8,4	1,3	1,3	16,0	14,9	4,1	4,3	2,2
Sealed Air	5870	8523	13,8	13,3	11,4	11,0	2,2	2,1	16,9	14,9	1,7	2,0	
Riverstone	473	443							15,6		3,3	3,2	3,0
Halyard	2311	2153	47,3	21,7	28,7	17,6	4,1	3,6	105,8	35,1			2,1
Glatfelter	728	1069	13,2	8,6	6,8	5,3	0,7	0,6	17,7	11,7		2,6	1,1
Ahlstrom-Munksjö	1458	1882	13,3	9,6	7,3	5,7	0,8	0,8	13,8	10,9	3,4	3,8	1,4
Berry Plastics	5205	10128	12,3	10,9	7,9	7,1	1,4	1,3	12,7	11,4			3,8
Suominen (Inderes)	**198**	**275**	**17,7**	**10,5**	**7,5**	**5,7**	**0,6**	**0,6**	**24,4**	**12,9**	**3,2**	**3,5**	**1,4**
Average			**18,4**	**12,7**	**11,2**	**8,8**	**1,6**	**1,4**	**27,4**	**16,2**	**3,1**	**3,2**	**2,2**
Median			**13,5**	**12,1**	**8,5**	**7,8**	**1,3**	**1,2**	**16,0**	**14,5**	**3,3**	**3,2**	**2,2**
Premium/discount -% vs. mediaan			**31 %**	**-13 %**	**-12 %**	**-26 %**	**-53 %**	**-55 %**	**52 %**	**-11 %**	**-1 %**	**10 %**	**-33 %**

Source: Bloomberg / Inderes. Notification: Inderes' MCAP does not include treasury shares

DCF-model

DCF model (MEUR)	2017	2018e	2019e	2020e	2021e	2022e	2023e	2024e	2025e	2026e	2027e	TERM
EBIT (operating profit)	**15,0**	**16,0**	**24,6**	**30,5**	**33,0**	**32,6**	**32,0**	**30,2**	**28,3**	**26,2**	**26,7**	
+ Depreciation	19,3	21,2	20,6	19,2	18,0	17,1	17,1	17,4	17,8	18,4	18,9	
- Paid taxes	3,7	-2,9	-5,1	-6,7	-7,4	-7,3	-7,2	-6,7	-6,2	-5,7	-5,9	
- Tax, financial expenses	0,4	-1,3	-1,1	-1,0	-0,8	-0,8	-0,8	-0,8	-0,8	-0,8	-0,8	
+ Tax, financial income	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
- Change in working capital	-13,2	-3,1	-1,6	-1,2	-0,8	0,2	0,2	0,3	0,3	-1,3	-0,9	
Operating cash flow	**25,3**	**30,0**	**37,4**	**40,8**	**42,0**	**41,7**	**41,3**	**40,3**	**39,3**	**36,7**	**38,0**	
+ Change in other long-term liabilities	-0,1	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
,- Gross CAPEX	-19,3	-13,1	-12,1	-12,1	-12,1	-17,1	-19,1	-20,1	-21,6	-21,6	-17,3	
Free operating cash flow	**5,9**	**16,9**	**25,3**	**28,7**	**29,9**	**24,6**	**22,2**	**20,2**	**17,7**	**15,1**	**20,7**	
+/- Other	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	0,0	
FCFF	5,9	16,9	25,3	28,7	29,9	24,6	22,2	20,2	17,7	15,1	20,7	373,8
Discounted FCFF		16,3	22,7	23,9	23,0	17,6	14,7	12,5	10,2	8,0	10,2	185,0
Sum of FCFF present value		**344,2**	**327,9**	**305,2**	**281,4**	**258,3**	**240,7**	**226,0**	**213,5**	**203,3**	**195,3**	**185,0**
Debt free DCF		**344,2**										
- Interesting bearing debt		-110,5										
+ Cash and equivalents		27,2										
-Minorities		0,0										
-Dividend/capital return		-6,4										
Equity value DCF		**254,5**										
Equity value DCF per share		**4,36**										

WACC	
Tax-% (WACC)	25,0 %
Target debt ratio (D/(D+E)	25,0 %
Cost of debt	5,0 %
Equity Beta	1,00
Market risk premium	4,75 %
Liquidity premium	1,25 %
Risk free interest rate	3,0 %
Cost of equity	9,0 %
Average cost of capital (WACC)	7,7 %



Source: Inderes

Income statement

(MEUR)	2015	2016	2017	2018e	2019e	2020e
Net sales	**444**	**417**	**426**	**433**	**459**	**482**
Costs	-395	-373	-392	-396	-414	-433
EBITDA	**49,5**	**44,1**	**34,3**	**37,2**	**45,2**	**49,6**
Depreciation	-17,7	-18,5	-19,3	-21,2	-20,6	-19,2
EBIT	**31,8**	**25,6**	**15,0**	**16,0**	**24,6**	**30,5**
NRIs in EBIT	*0,5*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*
EBIT (excl. NRIs)	*31,3*	*25,6*	*15,0*	*16,0*	*24,6*	*30,5*
Net financial items	-11,1	-10,8	-11,8	-13,0	-11,3	-10,5
Associated companies	0,0	0,0	0,0	0,0	0,0	0,0
Pre-tax profit	**26,5**	**22,4**	**12,4**	**11,0**	**20,4**	**26,7**
Other items	0,0	0,0	0,0	0,0	0,0	0,0
Taxes	-9,5	-7,2	2,0	-2,9	-5,1	-6,7
Minorities	0,0	0,0	0,0	0,0	0,0	0,0
Net earnings	**17,0**	**15,2**	**14,5**	**8,1**	**15,3**	**20,0**
Net earnings (excl. NRI)	*16,5*	*15,2*	*14,5*	*8,1*	*15,3*	*20,0*
Extraordinaries	0,0	0,0	0,0	0,0	0,0	0,0
Profit for period	**17,0**	**15,2**	**14,5**	**8,1**	**15,3**	**20,0**
EPS	*0,34*	*0,30*	*0,27*	*0,14*	*0,26*	*0,34*
EPS (excl. NRIs)	***0,33***	***0,30***	***0,27***	***0,14***	***0,26***	***0,34***

Source: Inderes

Balance sheet

Assets (MEUR)	2015	2016	2017	2018e	2019e
Non-current assets	**142**	**179**	**180**	**172**	**164**
Goodwill	15	15	15	15	15
Intangible assets	13	14	17	18	18
Tangible assets	98	136	137	128	120
Associated companies	0	0	0	0	0
Other investments	1	1	1	1	1
Other non-current assets	10	9	5	5	5
Deferred tax assets	4	3	5	5	5
Current assets	**150**	**137**	**145**	**151**	**156**
Inventories	33	43	44	48	50
Other current assets	10	11	16	16	16
Receivables	52	54	58	59	62
Cash and equivalents	56	30	27	28	28
Balance sheet total	**292**	**316**	**326**	**323**	**319**

Liabilities (MEUR)	2015	2016	2017	2018e	2019e
Equity	**126**	**143**	**136**	**138**	**147**
Share capital	12	12	12	12	12
Retained earnings	66	77	15	17	26
Shares repurchased	0	0	0	0	0
Revaluation reserve	0	0	0	0	0
Other equity	47	54	109	109	109
Minorities	0	0	0	0	0
Non-current debt	**106**	**99**	**111**	**115**	**100**
Deferred tax liabilities	11	11	15	15	15
Provisions	0	0	0	0	0
Long term debt	93	87	95	99	84
Convertibles	0	0	0	0	0
Other long term liabilities	2	1	1	1	1
Current debt	**60**	**74**	**78**	**70**	**72**
Short term debt	3	8	15	6	4
Payables	56	65	63	64	68
Other current liabilities	0	0	0	0	0
Balance sheet total	**292**	**316**	**326**	**323**	**319**

Source: Inderes

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Recommendation	Upside potential*
Buy	> 15 %
Accumulate	5 - 15 %
Reduce	-5 - 5 %
Sell	< -5 %

Potential regarding to 12 month target price

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Recommentation history

Date	Recommendation	Target price	Share price
29.4.2016	Accumulate	4,50 €	4,03 €
29.6.2016	Accumulate	4,50 €	3,93 €
9.8.2016	Reduce	4,80 €	4,58 €
21.9.2016	Accumulate	4,20 €	3,80 €
27.10.2016	Accumulate	4,60 €	4,34 €
1.2.2017	Accumulate	4,35 €	4,00 €
27.4.2017	Accumulate	5,10 €	4,77 €
11.5.2017	Reduce	5,10 €	5,00 €
22.6.2017	Reduce	5,10 €	4,87 €
24.7.2017	Reduce	4,70 €	4,81 €
9.8.2017	Reduce	4,70 €	4,90 €
30.10.2017	Reduce	4,50 €	4,42 €
14.12.2017	Reduce	4,25 €	4,43 €
31.1.2018	Reduce	4,25 €	4,40 €
6.4.2018	Reduce	4,00 €	3,88 €
27.4..2018	Reduce	3,50 €	3,55 €
4.7.2018	Reduce	3,50 €	3,40 €

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Awards

2015
Estimates

2014, 2016, 2017
Recommendation

2014, 2015, 2016
Recommendation and estimates

2012, 2016
Recommendation

2012, 2016, 2017
Recommendation and estimates

2017
Recommendation

2017
Recommendation

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