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Corporate Participants

Jan Johansson

SCA - CEO

Presentation

Host

Hello and welcome to SCA’s half year and second quarter report for 2013. Today our CEO Jan Johansson will go through the report and we will as usual have a Q&A session with our CFO Lennart Persson who will attend as well. Welcome to you on the telephone conference and welcome to you in the room. With this, I hand over to you, Jan.

Jan Johansson – SCA, CEO

Thank you very much and once again welcome, ladies and gentlemen. Let me just start with some macro updates, and as you all know we still are not very much helped by the growth globally. We still have a very weak European market. The expectations for this year is actually that we will have a decline in growth. US is growing a little bit below 2%. China still on a good level, 7.8%, but still of course lower than we saw before. Looking at our business areas, we still see some growth in Tissue in Europe and we also have a reasonably strong demand on our Personal Care side and in particular then of course in the emerging market where we still have a very good growth. We have seen some change in the Forest operation. The solid wood is much more positive than we saw from the first quarter. We also have some stronger kraftliner operation but publication paper is still quite weak and of course I will get back to this when I get into the different business areas.

Coming into Q2 to Q2, we do have sales growth of some 18%, of that 13% is coming from acquisitions. If we look at the Hygiene business we have a growth of 21% and of that 17% is coming from acquisitions. We still have an underlining growth, organic growth, in the company.
Looking at the operating profit of 4%, of course with a growth of 18% you would expect a little bit higher growth in operating profit but the difference is actually mainly coming from the Forest operation where we have a negative development in Forest of some 183 million, but the Hygiene business improving by 300 million Q2 to Q2. Working capital is 100% coming from payables. It depends very much when we have the end of the month whether or not it will be a positive impact or a negative impact. Inventories have not been changed; it is the same lower level as we always have had.

Looking at the efficiency programme, it’s going according to plan. If we look at the first programme with 231 million, of which 141 is coming from Tissue and 90 is coming from Personal Care. Q1 to Q2 we have an additional 179 million in savings and during Q2 we had a saving of 428. So it’s running according to plan and as you know the GP synergies will come a little bit later and we will have that 100% in 2016 and the others will be in ’15 and ’14.

Looking into the results, what we have to remember also that we still are in a transit mode, you could say, because we are divesting businesses and in these results we have the divestment of Aylesford and Laakirchen. It impacted the sales with some 900 million SEK. Currency is also of course impacting us. The sales is impacting negatively by 1 billion if we look at Q2 to Q2 and of course a negative impact on operating result. The currency is reducing operating margin with 0.3 Q2 to Q2. If we look at earnings per share, it may look a little bit strange. We have to remember that in that line we did have Packaging last year and that’s the only line we had it on so that’s why you see the difference in earnings per share. Also looking at the debt to equity ratio. We had got the sales revenue from Packaging but we hadn’t paid GP at the time, that’s why you see the difference in debt to equity.

Looking at Q1 into Q2. As you remember, we sold the remedies from the GP acquisition, we also sold Laakirchen during Q1 impacting all in all the sales with 1.2 billion and the operating result with 100 million, so that’s of course something we have to delete to see the underlying business. And if we do that we had a sales increase of 4% and increase in operating result of some 3%. We also had quite a good quarter when it comes to growth in Away-From-Home. We actually grew Away-From-Home with 7% globally and even in Europe we had a growth of around 5% Away-From-Home, so we are gaining market share all the time in our brand Tork.

If we look at Forest, the result has improved by 9% and having said that we also have to remember that we had a capital gain of 121 million Q1 so in spite of that it’s an improvement of
9% in profit. And we also had 80 million in cost for maintenance in Forest during the second quarter.

Then coming into Personal Care. We have some 10% growth, of which 5 is from acquisitions. Incontinence is growing by 6%. In Europe we have been growing incontinence by more than 4%, the market has grown by 2-2.5%. We have been growing the retail business in inco with 9% and we have been able to increase penetration in men inco with 14%. So we have actually accelerated the investment in inco during the quarter. And if you look at Personal Care in total you have to remember we have a business area with a return on capital employed above 28% here and of course the increase is substantially higher on that. So we are taking market shares, we are growing it and we are growing penetration and of course both long-term and short-term that will be a huge benefit for the company.

We also have a good growth in emerging markets of some 16%, of which 10% is coming from acquisition. We have a slightly lower margin in Personal Care from 12 to 11.9. It's actually 0.04 if you calculate it right. And that is mainly due to more investment in the market but also higher raw material during the quarter. And then we of course have volume impacting positively and also cost saving. But since Incontinence is an extremely important area for us. We are the dominant player in the world, as you know, and we are by far the dominant player in Europe and if we can grow our market share and particularly grow the penetration, which is still below 40% in mature markets. That will have a huge value for SCA. So we have accelerated, very successful, the penetration and the growth of inco during the quarter.

Coming into Tissue where we have a growth of 28% and of course acquisition is quite substantial since GP and that is 25% of the growth. The emerging market is growing by 14% and here we only have 6% that is actually coming from acquisition, the rest is organic growth. And of the profit improvement of 33%, 16% is coming from acquisition. When it comes to Tissue, as I think we clearly communicated, the first quarter we didn’t see an opportunity to price increases in Q2. There will be price increases for the second half, both in Consumer Tissue and Away-From-Home, mainly in Europe which is our biggest market. We have already concluded new agreements and we are in discussions with others to increase the prices. So that’s also going according to the plan as we communicated during Q1.

Forest operations, as I said, very positive development in solid wood with price increases of 7%. We estimate to continue some price increases during the second half of the year. Not in the level of 7% but at least it will be more price increases. We have managed to get €15 out of the €20 in
kraftliner and it seems to be very difficult today at least to get the remaining €20 in kraftliner and the reason is that the difference between test and kraftliner is a little bit too big at the moment, so if it’s getting too big then it’s difficult to get. Even though the balance is very strong in kraft, demand is very strong, but if the difference is too big it tends to be more difficult to get further price increases into the market.

We also had, as you know, quite a substantial negative currency impact from Forest compared to last year with 100 million SEK. But we had a cost saving of 110 million and also some lower raw material costs. Looking at the publication paper, we do see price increases in use. Our main part of the contracts are on a yearly basis, which means the impact of that will come next year. The price increases, the level of it is difficult to say now but let’s say something between 2-4% in price increases. Seems to be more difficult to get price increases in LWC today and, as I said, impact on that part mainly next year.

So if we summarise the quarter, we do have a higher sales and profit for the Hygiene business. We have still very good sales in emerging markets. We are gaining market shares in all our categories. Forest is suffering, but once again; sequentially it’s actually improving quite substantially in parts of the business. Efficiency programme is according to plan and as we also communicated previously there will be price increases within Tissue for the second half, mainly later in the third quarter but fully impacted in the fourth quarter, in particular in Consumer Tissue. So with that, ladies and gentlemen, I will open up for questions.

**Questions and Answers**

**Host**

Let’s start. We have a question. Go ahead, please.

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**Linus Larsson - SEB**

Thank you. It’s Linus Larsson, coming back to your comment about your investments in the market, if you could shed some more light on how you see A&P spend for the full year compared to last year, how you see the second half compared to the first half of this year.
Jan Johansson – SCA, CEO

If I look at the second half compared to the first half, at least what I see today will be on the same levels, so we’re not going to increase it for the second half.

Linus Larsson - SEB

And for the full year?

Jan Johansson – SCA, CEO

If you take the first half, double that and you will get to the full year.

Linus Larsson - SEB

I was thinking just to get an illustration of the competitive landscape, if you are spending more in 2013 compared to 2012 on A&P in relation to sales, something like that.

Jan Johansson – SCA, CEO

It’s mainly not because of the competitive landscape that we are accelerating. It’s actually to grow the category since it is such a profitable category for us, and also to drive penetration. With 40% penetration the potential is huge if we can start to drive the penetration. But it will be, if you summarise that, yes, I guess it will be slightly higher than last year.

Linus Larsson - SEB

Okay. And also coming back to the tissue price increases that you were referring to, and I understand it’s towards the latter part of the third quarter, would it be possible to in any way
quantify the tissue price increases that you’re seeing? Is it a very marginal net impact on the broad basis of the tissue division or is it something more significant that you would like to describe in any way?

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Jan Johansson – SCA, CEO

Since we are in the middle of negotiations it’s very difficult for me to comment, but of course we never get enough.

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Linus Larsson - SEB

And what’s really driving that on the tissue side? You’ve had… maybe you’ve had pulp price rising over the past two, three quarters but maybe not necessarily in the season that we’re now in the middle of.

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Jan Johansson – SCA, CEO

We have had increased raw material costs in pulp and that’s at least a good argument for us to discuss price increases.

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Linus Larsson - SEB

And then also finally one source of at least forecast volatility over the past several quarters has been the associate line. I think it was something like 35 million krona in the second quarter and I understand that it is or has been negatively affected in some quarters by restructuring. If you could tell us a bit about what’s going on there and what to expect in the second half.

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Jan Johansson – SCA, CEO

We have a board member here so I will ask him.
**Lennart Persson – SCA, CFO**

It is as you say, we saw some increase in the second quarter compared to the first quarter. I expect not lower in the second half than the speed we had in the second quarter.

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**Linus Larsson - SEB**

You think the Q2 level of profitability is pretty representative going forward?

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**Lennart Persson – SCA, CFO**

Yes, at least not lower.

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**Linus Larsson - SEB**

Great, thank you very much.

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**Mikael Jáfs - Kepler Cheuvreux**

Just a couple of housekeeping questions. Should we expect a tax rate of 26% for this year? That’s the first question. And then for the financial costs, they were down in the second quarter, what should we expect for the remainder of the year? And then the last question would be, how should we think about the non-recurring costs due to the restructuring for the rest of the year? Thank you.

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**Lennart Persson – SCA, CFO**
The tax rate, I mean the 26%, you can stick to for the remaining part of the year as well. When it comes to the financial net as you remember we had 60 million in dividend, received dividend in the second quarter, otherwise quite stable on the interest cost net, so to say. And the third question was the non-recurring items. I mean, we have now spent some 790, just below 800, and I think we can for the second half maybe not fully that amount but not far from.

Mikael Jåfs - Kepler Cheuvreux

Perfect. Many thanks.

Host

Any more questions here from the floor? No? I’ve got a sign we have from the telephone conference so, operator, please open up the line.

Operator

Thank you. If you wish to ask a question over the phone lines please press *1 on your telephone key pad. Your first question comes from Oscar Lindstrom, please ask your question.

Oscar Lindstrom – Danske Bank

Hello, this is Oscar Lindstrom from Danske Bank. Three questions. The first one concerns the increasing raw material costs in the Personal Care business which you talked a bit about ahead of the report and we now saw in the Q2 numbers. Can you be a little more specific as to exactly what sort of items are seeing cost inflation and perhaps if you could add something about the outlook for the cost inflation in the Personal Care business for the second half of this year? That was my first question. Should I go on with the second one or…?

Jan Johansson – SCA, CEO
We can take that. If we look at the raw material we have a cost increase of about 6-8 million, if I remember rightly, and if you look at the general cost inflation overall in the company we are on the level of 2-2.5% overall, which is reasonably good, looking at the business we have.

Oscar Lindstrom – Danske Bank

So this is not something that’s driven by any specific chemicals or oil prices, it’s more, sort of, general overall cost inflation, you’re saying?

Jan Johansson – SCA, CEO

No, the raw materials are of course the raw materials, but you also have cost inflation in general, that’s what I have answered, not in Personal Care but generally in the company it’s 2-2.5%. But the raw material cost is fluff pulp, as you know, and oil based products.

Oscar Lindstrom – Danske Bank

What do you see as, sort of, the outlook for the second half of this year? Should we expect continued, sort of, higher than average, I guess, or cost inflation or…?

Jan Johansson – SCA, CEO

No, we think it will be quite stable going forward.

Oscar Lindstrom – Danske Bank

My second question is about China. We’ve had reports of slowing growth and price pressure in this Chinese hygiene market and you have invested quite heavily in this market over the past,
say, 12, 18 months on acquisition and you’ve increased your stake in Vinda. What’s your view of what’s happening in the Chinese hygiene products market and how is your business there doing?

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**Jan Johansson – SCA, CEO**

The market is still growing there quite substantially. What has been impacted when it comes to the lower growth in China is mainly the infrastructure part of it. It’s slowly turning into a consumer market and still, of course, the consumer part of the GDP is lower than the infrastructure but the change is clear and it will continue. There has always been tough competition and we don’t see any change in that. It has not increased and it has not decreased; it’s on a similar level.

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**Oscar Lindstrom – Danske Bank**

And the final question; do you see the consequences of Kimberley-Clark’s decision to exit the tissue and especially the baby or part of the baby market in Europe. You’ve previously said it’s a bit too early to see exactly how that will affect you. Do you have any more on this to say now?

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**Jan Johansson – SCA, CEO**

I think I said it will certainly affect us positively but we haven’t fully decided whether or not it should be 100% private label or a combination of private label and branded and we’re still looking into that, depending very much on the retailer reaction in different markets. In some markets they want to have a second brand, in some markets they don’t want to have a second brand and then of course we will choose to be the private label supplier.

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**Oscar Lindstrom – Danske Bank**

Would you say that you could fill that gap with your existing product line-up or product portfolio or will you need to make an investment and cash out in order to fill this gap?
Jan Johansson – SCA, CEO

We are running at 100% now, but of course we can switch some contracts to more profitable contracts. It’s a living material.

Oscar Lindstrom – Danske Bank

And the final one this one, would you say that this upside is ahead of you and you haven’t really benefited from this yet or have you already seen some of this perhaps? I realise it’s not something you can easily put a number on but…

Jan Johansson – SCA, CEO

No, we have not seen anything of it yet, no.

Oscar Lindstrom – Danske Bank

All right. Okay, thank you very much, those were all my questions.

Host

Operator, next question from the telephone lines, please.

Operator

Thank you. The next question comes from Kartik Swaminathan, please ask your question. The line is now open, please ask your question.

Kartik Swaminathan – Bank of America Merrill Lynch
Hi there, can you hear me now?

**Jan Johansson – SCA, CEO**

Yes.

**Kartik Swaminathan – Bank of America Merrill Lynch**

Thank you. Sorry about that. Thank you for taking my question, Kartik Swaminathan calling from Bank of America Merrill Lynch. The first question I had is just an approach to tissue pricing dynamic in another way. Can I ask whether you’ve managed to pass on the full effect of cost pressure from pulp year to date in the negotiations that have already concluded? The second question was, if you could please remind us how quickly raw material cost pressure can be passed through in the Personal Care segment and how the pricing mechanism works again.

**Jan Johansson – SCA, CEO**

If I start with the second one, on the oil-based materials it will take four to six months before we have the impact in our P&L. In the first one I think it’s a little bit too early for me to comment on that since we have concluded some but we still have some more to conclude so I rather wouldn’t like to comment on that.

**Kartik Swaminathan – Bank of America Merrill Lynch**

Okay, thank you very much. And my final question is on pulp pricing and the momentum there. We’ve seen a little bit of volatility in the price indices that you can access through Bloomberg and I was wondering if you could provide us with a little bit of market colour on whether you think prices are indeed going to roll over going into summer now that we have a little bit more visibility or is it going to be a situation where we’re probably closer to flat lining?
Jan Johansson – SCA, CEO

Well, on average we are estimating that you will have a flat second half of the year, maybe a little bit lower during the summer period and maybe a little bit higher later on in the year, but in average flat. Then of course what is even more important for us is the ratio euro-dollar since we mainly produce in euro and we buy pulp in dollar, that’s a very important factor to follow.

Kartik Swaminathan – Bank of America Merrill Lynch

Thank you very much.

Operator

Your next question comes from William Houston, please ask your question.

William Houston – Redburn

Hi there, it’s Will Houston here from Redburn. Three questions, please. Firstly, if we look at your EBIT deviation analysis, which you provide on your website, and we look at the other line there, for the group in Q1 it was a positive 567 million SEK and then in Q2 it was only… sorry, 246 million SEK. I was wondering if you could just talk around the movements there which has caused that swing, please?

Lennart Persson – SCA, CFO

Of course some of that is coming from the cost saving programmes but then we have also the acquisitions and the divestments on that line. I think you should look at it from that point of view. We have also the deviations in market activity, for example.
So the reason for the lower positive contribution in Q2 is down to the increased spend on A&P?

Partly.

Partly, okay. And then question two, if possible, please, in terms of the central cost, that was higher in this quarter relative to Q1, could you just talk around what you expect for the full year please and maybe the balance over Q3, Q4 if possible?

We did communicate in Q1 that we expect some 550 to 600 million on a yearly base on that line and for the first half now I think we are on 300, so we will be so I guess it will end up around 600 on the yearly base.

Perfect. And then lastly, please, just on the FX guidance, given the moves in the spot rate so far this year, especially since you issued your guidance back in March and the devaluation of the krona since then, could you just update on what you’re expecting there for the full year impact, please?
We have a little bit more than 400 million for the first half year and if nothing dramatic happens, I mean, we guided I think on 500 so with the knowledge we have today I guess I have to stick to that one.

William Houston – Redburn

Okay, thanks very much.

Host

Thank you so much. I understand this was the final question from the telephone. Is there any more questions from you here in the audience? Yes, we have one.

Stellan Hellström - Nordea

Hi, this is Stellan Hellström with Nordea, I just wanted to come back a little bit on the questions on raw material price increases that we saw in Q2 in Personal Care and also if you could comment a little bit more on your possibilities to offset that with price increases.

Jan Johansson – SCA, CEO

We have quite a different business dynamic in Tissue and in Personal Care. Tissue by tradition is more, sort of, an area where you discuss raw material with your customers and you never do that in Personal Care. In Personal Care you either deal with it as cost cutting or price increases or new innovations, and since the bulk at least of our business in Personal Care is branded business you manage it in a different way. So for some aspects it’s much easier and others it’s more difficult, depending of course which category you are in. But, I mean, if you look at the history of the company, we have been able to do that for the past 50 years. I feel quite confident that we’ll do it in the future also.
Stellan Hellström - Nordea

Looking then a little bit more on the short-term, then, if you can say something? I think you talked about earlier that you think your product innovation pipeline is quite strong, and then given the raw material price increases that we’ve seen how do you feel that you can compensate?

Jan Johansson – SCA, CEO

I think if you look at the pipeline that we have today we will have a lot of new features coming out in the market next year almost in all our categories and that’s of course a very good opportunity to improve your profitability. We also are relaunching a completely new product and positions in Russia as we are speaking today and of course that is also consuming cash and profits while we’re doing it, but we feel very confident we will improve profitability and market share once we are through it. And we have some other countries in the world where we are also relaunching baby in a completely new way, Sweden as an example, and while doing it with TVC, etc, it has a negative impact but then normally you get a more positive impact once we have done it. So we are in the middle of quite a big relaunch of many categories in the world during this spring and of course that has an impact on the short-term on the margin, but still keeping a profitability above 28% return on capital employed.

Host

Any more questions or where you okay? So, any more questions from the audience? And there is none from the telephone. Jan, do you want to make any final conclusion?

Jan Johansson – SCA, CEO

Thank you. Well, looking at the developments as I think we have been describing we have had a quarter with investments in the markets, in particular in incontinence but also in other categories. We still have a very good underlying growth, even in mature markets in important categories. We have a position where we will improve the profitability on Tissue, not only by cost-cutting but also by price increases in the second half. And we do see quite a substantial turn in Forest in at least two of our products, the solid wood and the kraftliner. So from that perspective I think it’s a
positive development and we are at least looking forward to the second half. So with that, have a nice summer and see you after the summer.