

WESTPEAK

RESEARCH ASSOCIATION

Clearwater Paper Corporation (NYSE: CLW)

Consumer Staples – Pulp & Paper Products

Clearwater Paper, Clear Flow into the Future

February 18, 2021

Clearwater Paper Corporation (CLW) is a US manufacturer and supplier of private label tissue products and bleached paperboard distributed domestically and internationally. The business is organized into two segments: Consumer Products and Pulp and Paperboard.

Thesis

Clearwater Paper Corporation has positive and growing earnings starting from 2020, compared with its previous years' unsatisfying performance. We believe this is not all due to the pandemic but is attributed by the company's sustainability approaches as well as its operational strategies towards more free cash. Although the market view on the company is pendent because of the high debt ratio, we suspect the company, based on its market positioning and the new management team's operating, will be able to reduce near-term debt.

Drivers

Inflating income and the growing hygiene consciousness have latently changed consumers' purchasing patterns. The tissue sector is originally economic resilient; with the emphasis on hygiene, Clearwater Paper would have more space to grow. Meanwhile, with the e-commerce upsurge driving the demand for packaging, the company, as an efficient manufacturer and a sustainable player, would benefit from this ongoing trend in the pulp sector.

Valuation

Given the current price of Clearwater Paper Corporation at \$40.80, we believe the company is undervalued by the market. Our target price \$51.44 is derived from the DCF analysis and comparable company analysis, each weighted 50%. Therefore, we initiate a **BUY** rating on the company.

Analyst: Yewen Wang, BCom. '23
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Equity Research	Canada/US
Price Target	CAD\$ 51.44
Rating	Buy
Share Price (Feb. 18 Close)	CAD\$ 40.80
Total Return	26.1%
Key Statistics	
52 Week H/L	\$45.81/\$11.88
Market Capitalization	\$676.2M
Average Daily Trading Volume	143K
Net Debt	\$811M
Enterprise Value	\$1.57B
Net Debt/EBITDA	3.38x
Diluted Shares Outstanding	16.57M
Free Float	98%
Dividend Yield	N/A

WestPeak's Forecast

	2020E	2021E	2022E
Revenue	\$1896M	\$1928M	\$1949M
EBITDA	\$253M	\$212M	\$211M
Net Income	\$62M	\$39M	\$41M
EPS	\$3.72	\$2.33	\$2.42
P/E	7.8x	17.5x	16.9x
EV/EBITDA	5.8x	8.3x	7.9x

1-Year Price Performance



Business Overview/Fundamentals

Company Overview

Clearwater Paper Corporation (CLW) is a US manufacturer and premier supplier of private label tissue, bleached paperboard as well as other pulp and paper products distributed domestically and internationally. The company also offers services of custom sheeting, slitting and cutting. The target market consists of grocery, retail stores, mass merchandisers and high-end users of the packaging industry within large distribution channels. Its business is organized into two segments, Consumer Products and Pulp and Paperboard, aimed at providing more sustainable alternatives and high-quality products that people use every day.

Segment 1 – Consumer Products

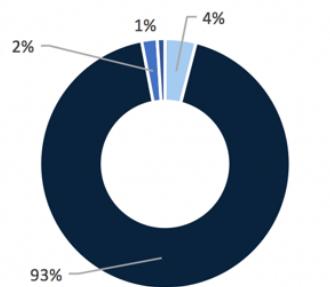
The Consumer Products segment mainly manufactures and sells a complete line of at-home and away-from-home (AFH) tissue products. Tissues are need-based and economically resilient. In this segment, Clearwater Paper has five tissue converting facilities and four tissue manufacturing facilities. The company produces private label paper and tissue products and sells them to large retail channels. Primary products include bath tissue, facial tissue, paper towels and napkins. The company's annual tissue paper capacity is 435K tons with its private brand taking 17% of the market share.



(Source: company website)

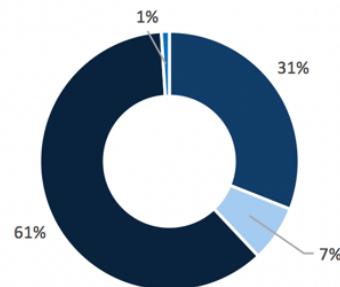
The company generates revenue mainly through sales to grocery outlets, mass merchandisers and club stores. Approximately 90% of the Consumer Products segment's revenue is generated from retail tissue; and within retail tissue, at-home products contribute the most revenue. Sales of the Consumer Products segment were 51.5% of the company's total sales in 2019.

Consumer Products Segment Tissue Shipment



■ AFH ■ Retail ■ Parent Rolls ■ Other

Pulp and Paperboard Segment Paperboard Shipment



■ Cup and Plate ■ Liquid Packaging ■ Folding Carton ■ Other

(Source: 2019 Clearwater Paper Investor Presentation)

Segment 2 – Pulp and Paperboard

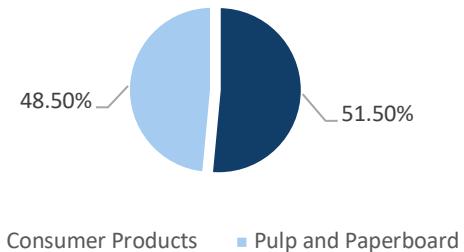
Pulp and Paperboard is a high-end segment, in which the company manufactures pulp and bleached paperboard products for packaging industrial use. CLW has factories and facilities that process pulp and wood materials into paperboard for packaging cosmetics, pharmaceuticals and other premium retail goods. At present, the company's paperboard business is well-positioned for trends towards sustainable packaging and food service products. Clearwater Paper has five paperboard sheeting facilities and two pulp and paperboard mills. The segment consists of folding cartons, liquid packaging, cup and plate products, blister and carded packaging, top sheet and commercial printing grades and softwood pulp. Clearwater Paper's Pulp and Paperboard segment occupies 15% of the North American market share.



(Source: company website)

The company utilizes various methods for the sale and distribution of its paperboard. The majority of its paperboard is sold to packaging converters domestically through sales managers located throughout the United States, with a smaller percentage channelled through distribution to commercial printers. Sheeted paperboard products are directly sold to folding carton converters, merchants and commercial printers. The company does not convert its paperboard directly to specific end-use products, maintaining its independent status to attract a diverse group of customers. One exception is the service of just-in-time sheeting and narrow rolls. Clearwater Paper can convert its paperboard into flat sheets and narrow rolls. We believe this service will help expand its in-market service capabilities and support packaging converters to buy the sheeted paperboard and convert to end-products more easily. Major customers (top 10) contributed to 40% of its total revenue in 2019. Clearwater Paper's relationship with its most important customers depends on its ability to continue to meet customer's quality needs and services at competitive prices. With its in-market service capabilities and just-in-time sheeting, the company might have the ability to retain its customers. As for converters, it's usually not easy to switch over to another manufacturer that provides tailored services of the same quality. However, there could still be a risk if the company loses one of its major customers or experiences a decline in the level of purchases by any major customers. 48.5% of the total sales derived from Pulp and Paperboard segment in 2019.

2019 Revenue Generation by Segments



(Source: 2019 Clearwater Paper 10-K Report)

Company Strategy

Expansion of Tissue Facilities

The company first installed a facility with TAD process in Shelby, North Carolina in 2010. (TAD stands for “Thru-Air-Drying” which abandons water and passes hot air through sheets). This drying technology is beneficial for the softness and strength of tissue products. Consecutively in



(Source: company website)

2017 and 2019, the expansion of tissue making and converting machines to the company’s existing factory in Shelby facilitated Clearwater Paper in manufacturing and distribution processes. This capital project can help meet market growth forecasts by boosting production. In 2019, the Shelby facility produced 152K tons of tissues and 141K tons in tissue converting, leading the production capacity of facilities in other locations. With the fast speed and high quality of production, the company is able to satisfy customers’ needs in a timely manner. This characteristic is

essential to Clearwater Paper. The company’s target market consists of small and medium-sized customers that rely on very few manufacturers and compete for timeliness. In addition, the technological advancement of these tissue machines allows Clearwater Paper to produce ultra-premium tissue-related products, to satisfy the customers’ needs for high-quality usage. Within the saturated tissue market, the branded tissue sector has been moving from standards to quality, and even the private-label sector initiates a sign of quality-driven production. Investing in technology will enable the company to have a competitive advantage to sustainable leadership and a promising market share in the private-label sector, compared with other manufacturers.

Sustainability Approaches

Clearwater Paper committed to sustainability in 2013 by initiating its first CSR report. In the following years, the company has strived to achieve its environment-friendly and energy-saving goals by sustainability approaches. The aforementioned TAD process avoids great water consumption in tissue making. The company’s responsible sourcing ensures its fibre sources are not from sensitive forests or habitats for endangered species. The partnership with responsible suppliers also contributes to the continuity and transparency of its supply chain and quality control. In 2019, the company has launched NuVo®, a new brand of cup stock paperboard that offers up to 35% post-consumer recycled fiber. In 2020, Clearwater Paper continued to introduce ReMagine™ as another new sustainable paperboard solution. In the meantime, the adoption of the Global Reporting Initiative (GRI) Reporting Principles introduces stricter materiality assessment that could affect the business and corresponding stakeholders. We suppose that these trademarks and employed principles will add credibility to the company’s

product upgradation. Moreover, these initial investments will likely help generate economies of scale when the production keeps increasing in the future.



(Source: U.S. Chamber of Commerce Foundation)



(Source: Clearwater Paper website)

Consumer Products Segment: Private-label Brand Focus

As the branded tissue products market is saturated, the company positions itself mainly in the private-label brand market. Private-label tissue products are usually cheaper than branded tissue products. This price advantage incentivizes small to medium-sized retailers to become regular customers. The company will continue to support such level of customers to reintegrate in-store inventory. It is expected that the segment's sale will add slightly to growth and then be normalized at a stable level.

Pulp and Paperboard Segment: Product Positioning and Service Quality

The paperboard segment is diversified by various kinds of end products for different uses. The company primarily occupies in high-quality Solid Bleached Sulphate (SBS) paperboard, aligned with market trends and consumer preferences. The SBS paperboard is usually used when the quality of printed image is required, commonly tailored towards high-end packaging including homecare, pharmaceutical, cosmetics, liquid and frozen food packaging. Furthermore, associated with manifold applications, Clearwater Paper also provides services such as just-in-time sheeting and converting to narrow rolls based on needs. The entire value chain exists to retain loyal consumers, as the company not only manufactures high-quality paperboard with various uses, but also customizes its in-market services to ensure the after-sales applicability.

Capital Allocation

Clearwater Paper's near-term strategy is to prioritize free cash flow to relieve stress on debt. For example, the company utilized \$40 million in free cash to reduce its debt. The reduction of debt adds more liquidity to its operation. Furthermore, Clearwater Paper's annualized Debt-to-EBITDA was approximately 3x at the end of Sep 2020; its target Debt-to-EBITDA ratio is 2.5x, compared to the industry median of 3.54x. Clearwater Paper's capital allocation objectives include large capital spending to be normalized \$60MM per year and \$45MM for 2020 fiscal year. Some of the company's debt is scheduled to mature in future years: \$300.0MM, \$199.9MM and \$275.0MM in 2025, 2026 and 2028, which indicates more liquidity to be added to its operation.

Industry Analysis

Tissue Products Industry Overview

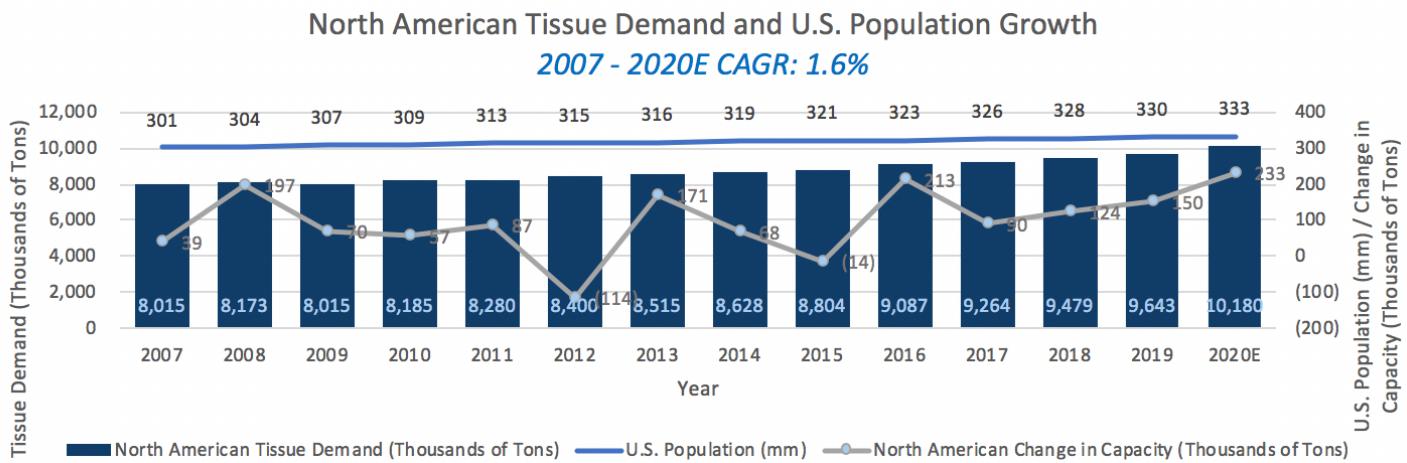


From 2007 to 2020, the sector has grown at a CAGR of approximately 2%, with a faster growth trend in recent years. The global tissue market is expected to grow at a CAGR of approximately 6.5% from 2020 to 2025. The US tissue market is the “main force” of the industry around the globe. This tissue market consists of one-third of away-from-home (AFH) products as well as two-thirds of at-home products. In 2019, consumer expenditure in the US reached \$44K per capita. Bathroom tissue remains as the key player, driving the tissue market forward through a combination of necessity and economic resilience of toilet culture.

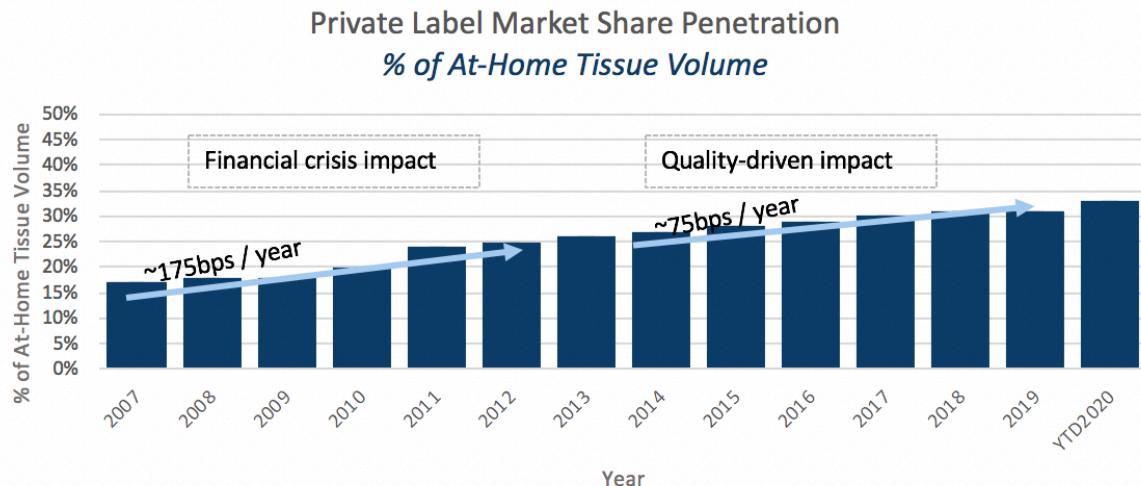
(Source: company website)

Rising household incomes, increased awareness of sustainable tissue products, and government policies to promote public health are also part of the major forces driving the market growth. There was a sudden spike in the demand because of the spread of the COVID-19 pandemic. The manufacturers in this sector are producing 20% more than the normal levels which might strain the supply chain.

The US consumer tissue market is also highly concentrated, with roughly 70% of sales in the hands of the top three manufacturers Kimberly-Clark, Procter & Gamble and Georgia-Pacific. The remaining 30% of sales are from private label brands. Private label brands in the US tissue market have the potential to grow in future years given their lower price and unsaturated competitor landscape. In addition, based on private label market share penetration level, the industry is now moving towards quality-driven impact instead of financial crisis impact ten years ago. The pursuit of high-quality products indicates more growth opportunities for companies that incorporate new technology and weigh more on product quality advancement—for instance, Clearwater Paper.



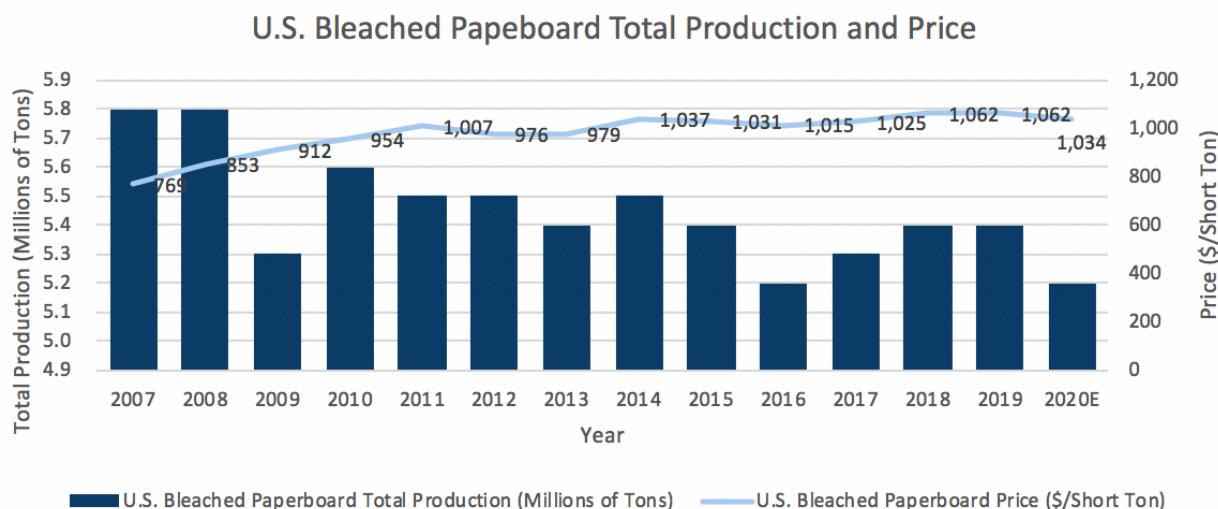
(Source: Fastmarkets RISI | Pulp and Paper Industry Intelligence)



(Data source: Clearwater Paper website; original source: Fastmarkets RISI)

Pulp and Paperboard Industry Overview

The US paperboard market has been decreasing at a steady rate of 0.4% from 2008 to 2018 with slight fluctuations. Its market value has declined over the past ten years. The revenue of the US paper mill industry was \$38 billion in US dollars in 2020. This industry has been mainly divided into unbleached, solid bleached sulphate and recycled paperboard. More and more diversified applications are emerging from the industry, such as folding cartons, carded packaging, liquid packing, plate and cup packing. Major players are International Paper, Domtar, Schweitzer-Mauduit International, and Neenah. The lifecycle of the industry is at the mature stage so pricing, demand and supply are relatively stable in the market. Even though the industry indicates a shrinking trend in the past few years, with consumer purchasing patterns gradually shifted from plastic to paper packs, paperboard packaging continues to serve a broader customer base.



(Data source: Fastmarkets RISI | Pulp and Paper Industry Intelligence)

Drivers

Consumer Products Segment - Customers' Changing Purchasing Patterns

Inflating income levels and the rising hygiene-consciousness among individuals have escalated the demand for personal care and hygiene products like tissue and kitchen rolls across the globe. Furthermore, the COVID-19 pandemic has increased the demand for paper hygiene products, such as paper towels and couch rolls, across the residential sector, as well as hospitals, healthcare institutions and other essential services. In the Consumer Products segment, Clearwater Paper's Q3 2020 shipments were 14.5 million cases compared to 13.2 million in Q3 2019 driven by the elevated demand. It is true that the pandemic triggered the fast-growing period in the paper products market. The progress in vaccination will relieve the stress under COVID-19 but will not shift the evolving purchasing patterns in the hygiene sector. With people's living habits moving towards a clean and healthy style imperceptibly, we believe this trend is not a flash in the pan and would maintain in the long run instead.

Pulp and Paperboard Segment - E-commerce Upsurge to Boost Packaging Needs

Working-from-home mode and virtual entertainment have changed people's focus — e-commerce is growing faster as a substitute for traditional sales channels, especially in the retail industry. As a result, demand for packaging is expected to rise. Clearwater Paper's paperboard products and its cutting and sheeting services support a variety of retail chains such as cosmetics, pharmaceuticals, food and beverage, and household supplies. With Clearwater Paper's pulp mills in the US facilitating its manufacturing and sheeting, we believe the company will stabilize its revenue from the generally shrinking paperboard industry.

Investment Thesis

New Solution Tailored to Market Preference and High Quality



(Source: Clearwater Paper website)

In 2020 summer, Clearwater Paper launched ReMagine™ paperboard solution. ReMagine™ is a distinct SBS paperboard brand that includes up to 30% of recycled fibre in its components. The introduction of this new solution was inspired by the circular economy principles, according to the press release in July 2020. Since the paperboard industry is already at the mature lifecycle stage, consumers' purchasing preferences have started to shift from common paperboard to high quality and ultra-premium folding carton products. Moreover,

ReMagine™ is essential to Clearwater Paper's company value proposition, strengthening its positioning to customers under the growing trend of sustainable packaging. As Clearwater Paper is integrating the ReMagine™ paperboard new solution to its products, we expect to see the trademark having an increased exposure to more packaging and food service products. With the recycled fibre components providing its superiority, the company is well-positioned for sustainable packaging, which helps differentiate its brand name from other competitors in the crowded market. We speculate that, with the incorporation of ReMagine™ technology, Clearwater Paper would have a competitive advantage in product and manufacturing innovation over its comparable companies.

Economic Resilience Contributes to a Stable State under the Pandemic Uncertainty

Since paper products are categorized as a necessity to households, they are resilient to economic downturns, compared with other consumer products. Though there are claims that the upsurge in this sector is transient, we sustain the viewpoint that the resilience characteristic will help the company not only survive from the market trough but also stabilize when the market rebounds. Within a generally shrinking industry, it becomes more critical for manufacturers to supply paperboard or paper products with efficiency and in a high quality. Based on the installation and outperforming operation from Clearwater Paper's Shelby and Lewiston facilities, we infer that the company can retain its resilience in the uncertain economic environment.

Increasing Financial Flexibility

With a large portion of debt scheduled to mature from 2023 to 2028, it's expected that the company will incorporate more free cash for its capital expenditure and development of new technology and product innovation. It is important to note that the relatively high utilization of debt by the company in recent years has led to a high debt/equity ratio. A larger portion of debt signals risks of leverage and long-term liquidity, so the market might not have an upbeat prospect. However, we infer that with the stable demand, e-commerce surge and Clearwater Paper's operational strategies, the company will be able to secure the steady growth in earnings. Furthermore, the company has utilized approximately \$40 million of free cash flow to reduce its net debt in 2020. The net debt included a \$40 million voluntary prepayment of Clearwater Paper's term loans and its liquidity was \$277 million. In our opinion, the company has the potential to pay out its long-term debt by scheduled years, after which there will be more free cash balance to finance its operation and expansion.

Catalyst

Earnings Release

The company previously estimated its Q4 sales would decrease because of normal retail purchasing patterns and the promising outlook of the COVID vaccine. Later on, the company announced updates of increasing Q4 demand. It now expects adjusted EBITDA for the fourth quarter of 2020 to be in the range of \$71 to \$76 million instead of \$ 52 to \$62 million. The unexpected elevation could be attributed to the second wave of COVID, its virus variant

cases and people's growing consciousness affected by the pandemic. Applying to earnings releases forward, if the company's profit hits an expectation range, there might not be an upsurge in the stock price; but if the company outperforms, for example, generating EBITDA higher than expected in 2021 Q1 or Q2, there will be a rise in the price.

New Regulations Favoring Sustainable Packaging

When there are new regulations towards sustainable packaging, paperboard converters will seek more sustainable sourcing from pulp and paperboard manufacturers. It's an opportunity for brands that utilized renewable sources of energy and fibred components as major responsible sourcing, for instance, Clearwater Paper. As Clearwater Paper aligns its performance with ESG metrics and proactively markets the sustainable trademark, we believe such regulations would not negatively affect the company's performance, but will propel it to be a favorable supplier, compared with other companies in the same industry.

Improved Credit Rating

In August 2020, S&P removed Clearwater Paper's credit rating outlook from negative to stable. This indicates a seemingly promising perspective on the company's future liquidity. Looking forward, with potentially more debt relieved in the future, the company is expected to continue to improve its credit rating from the current state. However, as Clearwater Paper intends to utilize the net proceeds of senior unsecured notes due in 2028 to refinance the notes due in 2023, there exists the refinancing risk associated with the credit rating. On all accounts, a credit agency's rating on the company might have influence on its stock price.

Management Team

Clearwater Paper Corporation's executive compensation is heavily performance based. The total compensation of the CEO consists of base salary, annual incentive and Long-Term Incentive. 75% of the annual incentive is linked to adjusted EBITDA, and 25% related to strategic initiatives. Long-Term Incentive (LTI) is equity-based, of which performance shares weigh 70% and restricted stock units weigh 30%, respectively. Key YoY performance metrics include adjusted EBITDA, total shareholder's return, free cash flow, return on invested capital and stock price. We believe that the executive compensation program will align the interests of executives with the long-term best interests of stockholders.

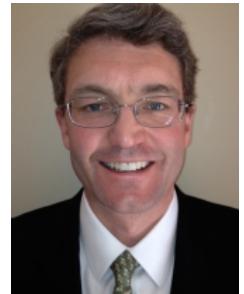
ARSEN KITCH: President, Chief Executive Officer and Director

Mr. Kitch was elected president and CEO effective April 1, 2020. He was previously the senior vice president and general manager of the consumer products division since 2019. Mr. Kitch also served as vice president of finance and vice president of financial planning and analysis. He joined the company in 2013 as senior director of strategy and planning. Before joining Clearwater Paper, Mr. Kitch held positions at Nestlé USA, KKR Capstone, and Frito-Lay. He had his bachelor's degree in business administration at the University of California, Berkeley and an MBA at Stanford University Graduate School of Business. Mr. Kitch had a base salary of \$750,000, an annual incentive target bonus of 100% of base salary, and an annual LTIP grant target value of approximately \$1.5 million. Mr. Kitch also received an RSU grant with an approximate value of \$1.0 million upon his election to President and CEO.



MICHAEL MURPHY: Senior Vice President, Chief Financial Officer

Mr. Murphy joined Clearwater Paper as senior vice president and chief financial officer in April 2020. Before joining Clearwater Paper, Mr. Murphy served as the chief financial officer for NxEdge, Inc. Between 2014 and 2018, he was the vice president, strategy and vice president, finance at KapStone Paper and Packing Corporation. He also held senior positions at Boise Inc. and J.P. Morgan Securities. Mr. Murphy started his career as an investment banking analyst at John Nuveen & Co. He had a Bachelor of Science degree in biomedical engineering and chemical engineering at Northwestern University and a master's degree in business administration, accounting and analytical finance at the University of Chicago Booth School of Business.



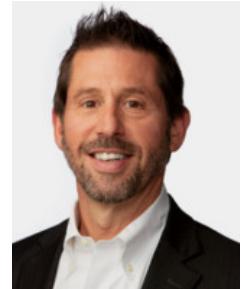
JOANNE SHUFELT: Senior Vice President, General Manager - Consumer Products

Ms. Shufelt began her career with Clearwater Paper in 2012 as the vice president of sales and marketing for the consumer products business. She was elected senior vice president and general manager of the consumer products business in June 2020. Before joining Clearwater Paper, Ms. Shufelt held sales leadership roles with Duro Standard Products, a private packaging company, and AbitibiBowater Inc, now Resolute, Inc., a pulp, paper and tissue company. Prior to that, Ms. Shufelt spent 20 years at Georgia Pacific, in sales and operations leadership roles.



STEVE BOWDEN: Senior Vice President, General Manager - Pulp and Paperboard

Mr. Bowden began his career with Clearwater Paper in October 2018 as senior vice president and general manager of the pulp and paperboard business. Before joining Clearwater Paper, Mr. Bowden was the president of America's food and beverage division for Multi-Color. He also held key leadership roles at International Paper, including the executive vice president of marketing and strategy for xpexx, formally an International Paper division. Mr. Bowden was also the mill manager for the company's Augusta, Georgia, coated paperboard facility.



In summary, this is a relatively young and new management team. On one hand, there might be concerns that the new team has less experience in managing Clearwater Paper. On the other hand, given the previous years' unsatisfying performance, this new team might be able to bring innovative and alternate solutions and operating strategies to boost performance.

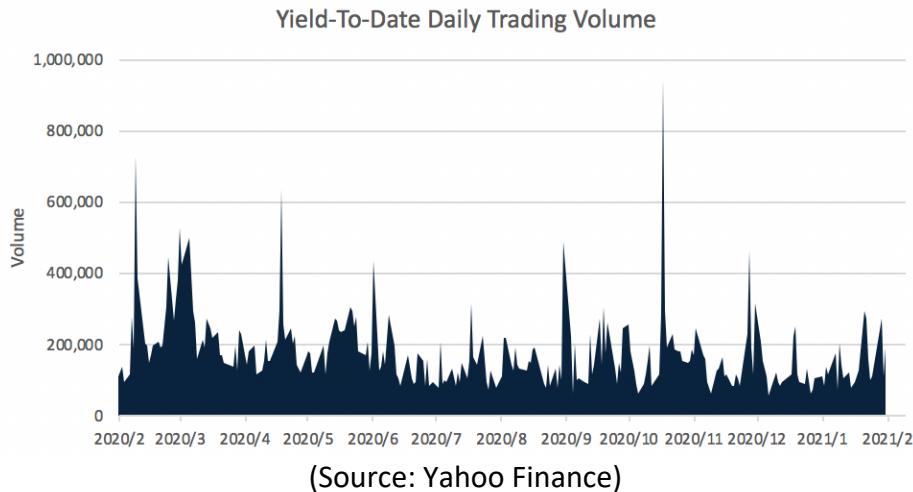
Shareholder Base, Liquidity, Market Depth

Shareholder Base

Clearwater Paper has 3.05% of shares held by insiders and 91.33% of shares held by institutions. Its top ten investors occupy over 56% of Clearwater's free float. If one of the top ten sells its shares for a larger amount, the increase in supply will drag Clearwater Paper's stock price and might also signal other major investors to sell their shares. Therefore, large institutional transactions from major shareholders will affect the company's share price relatively sharply, imposing a potential risk. The ten largest shareholders are listed below in the table.

Shareholder	# of Shares Owned	% of Shares Out
Blackrock Inc.	2,436,311	14.70%
Price (T.Rowe) Associates Inc	1,664,422	10.04%
Dimensional Fund Advisors LP	1,380,668	8.33%
Vanguard Group, Inc. (The)	1,055,509	6.37%
Private Management Group, Inc.	690,479	4.17%
First Sabrepoint Capital Management LP	532,911	3.22%
State Street Corporation	528,536	3.19%
Pinnacle Wealth Planning Services, Inc.	360,316	2.17%
Charles Schwab Investment Management, Inc.	344,353	2.08%
Wedge Capital Management, L.L.P.	333,057	2.01%

Liquidity



YTD Daily Trading Volume

As of Feb 18th, 2021, Clearwater Paper's year-to-date average daily trading volume was 180,582 with a weighted average price of \$32.24. The significant peaks usually occurred around the company's earnings release dates. The total value of outstanding shares is approximately \$5.82 million, and Clearwater's market cap is \$676 million. In addition, free float is 98% (16.26 million out of 16.57 million shares outstanding), which indicates a high level of liquidity. The bid/ask spread is usually within 7%, reflecting a more flexible market of the stock. However, as the majority shareholders hold over half of the free float, there might be liquidity risks if large investors don't trade the stock actively, making it difficult to get hold of the remaining available shares with a narrow spread.

Valuation

Discounted Cash Flow Analysis

Revenue

Given the fact that the tissue market and paperboard industry are already stable and saturated, we expect the revenue to continue to grow at approximately 3%~4% in the next five years and then normalize at a steady level. Shipment of tissue products in the Customer Products segment is estimated to be the major driver of the revenue. According to the facility expansion project, additional and advanced tissue machines will help the company achieve a full rate of shipment in 2021 and years forward.

Depreciation

We utilize a straight-line depreciation method in our modelling analysis. The useful life of 11 years is determined according to Clearwater Paper's average machine useful life in previous years. We believe there won't be substantial changes in the future.

Capital Expenditure

For the past five years, the company has spent liberally on infrastructure and capital projects, such as the Shelby NC facility, so the CAPEX remained high and started to decrease at the end of fiscal year 2019. Due to COVID-19, its tissue making facilities as well as pulp and paper mills will not expand as much as before. Following 2020 Q1 to Q3's pattern, we would assume the CAPEX will maintain at around 6% in the near future and increase more forward.

Weighted Average Cost of Capital

The weighted average cost of capital was determined from the cost of equity of 14.3% and cost of debt of 1.3%. The cost of equity was determined with a risk-free rate of 1.13%, an expected market return of 10.0% and a Beta of 1.48. The cost of debt was determined by a pre-tax cost of debt of 1.8% and an effective tax rate of 27%, aligned with the general tax rate of the industry.

Debt

The company has more debt than its peer group. According to Clearwater Paper's 2020 Q3 earnings release presentation, its near-term strategy is to reduce debt from cash balance to allow for more free cash flow. Furthermore, the company has scheduled debt maturity in 2025, 2026 and 2028, for \$300MM, \$199.3MM, and \$275MM, respectively. This would release the pressure to repay debt in the future but is not included in our five-year discounted cash flow analysis.

Perpetuity Growth Rate

We expect the perpetuity growth rate of the industry at its mature stage to be 2% in the future, aligning with the general inflation rate.

Comparable Company Analysis

Verso Corporation

Verso Corporation operates in the paper industry. The Company produces coated freesheet, coated groundwood, and uncoated super calendered papers and pulp. Verso offers its products to magazine and catalog publishers, commercial printers, specialty retail merchandisers, and paper merchants.

Neenah Paper Inc.

Neenah Paper, Inc. is a global manufacturer of premium, performance-based papers, and specialty products used in a variety of applications. The company has manufacturing operations in the United States and Germany. Its Fine Paper and Packaging segment offers printing papers and envelopes, as well as food and beverage labels, folding cartons, and box wrap. Paper and packaging customers include distributors, converters, and retailers. The US accounts for more than 70% of sales.

Glatfelter Corporation

Glatfelter Corporation is a global manufacturer of specialty papers and engineered products. Its Germany-based Composite Fibers unit makes products like coffee and tea filter paper and self-adhesive labelling paper, while the

Advanced Airlaid Materials business focuses on nonwoven fabric-like materials used in feminine hygiene products, diapers, cleaning pads, and wipes. More than half of the company's total sales are generated in the US.

Domtar Corporation

Domtar Corporation manufactures and markets uncoated freesheet paper. The company generates revenue mainly from sales of paper products, comprising office, commercial printing and publishing, and converting and specialty papers. The lines include offset printing paper, photocopying paper, as well as fine and imaging (security) papers. Its top paper, freesheet, is used for a range of printed materials with demanding image and press requirements. What sets Clearwater Paper different from Domtar is that Clearwater Paper has another revenue stream from the consumer products segment: at-home and away-from-home tissue products.

Cascades Inc.

Cascades Inc. produces paper and packaging products. The Company manufactures, converts, and markets specialty products, including boxboard, fine papers, tissue paper, and containerboard. Cascades and its subsidiaries operate in Canada, the United States, France, Sweden, Germany, and Great Britain. The Packaging group generates most of Cascades' sales, and business is divided among boxboard, containerboard, and specialty products. Cascades Tissue produces facial and bathroom tissue as well as paper towels and napkins. The company holds a greater amount of debt compared with that of Clearwater Paper.

Recommendation

Through the company's capital expansion strategy and sustainable approaches, Clearwater Paper will have a leading position in shifting products into the high-quality stage. Since tissue products are a necessity and paperboard products are relative economically resilient, Clearwater Paper has the potential to maintain its elevated trend and stabilize under the uncertainty of the COVID-19 variant and vaccination. As a large portion of Clearwater Paper's debt will mature in the next few years, the company will have more free cash for its capital expenditure as well as future product development. However, compared to peer companies, Clearwater Paper has more debt, which could impose a higher risk of bankruptcy. We would like to set the weight of discounted cash flow analysis and comparable company analysis as 50:50. Because of market cap, cash/debt ratio, and business scope difference, there are not perfectly matched peer companies. Clearwater Paper's P/E multiple is around 11x, which is below the benchmark 21.5x of other companies in the same industry. This indicates the company is currently undervalued. Following the 50:50 ratio, we have a target price of \$51.87 by discounted cash flow analysis and \$51.01 by comparable company analysis. \$51.87 is derived from 50% of perpetuity growth method and 50% of exit multiple method. As perpetuity growth method usually obtains a relatively optimistic estimate whereas exit multiple method more conservative, we would like to use equal weights to balance out. For \$51.01 by comparable company analysis, we also utilize equal weights of EV/EBITDA and P/E Multiples. The final target price is \$51.44. Therefore, we recommend a **BUY** rating on Clearwater Paper.

Risks

Increasing Competition

With the increasing number of new entrants into the private label tissue market, its market power is diluted and will potentially face decreasing customers. Demand and pricing of consumer tissue products are affected by the increased capacity as well as changing dynamics as a result of changes in consumer purchasing habits and evolving sales and distributional channels. Furthermore, the consolidation of Clearwater's major competitors in the North American paperboard industry will help them expand their business landscape, resulting in a decreasing end-user base of Clearwater Paper.

Retail Landscape

The changing retail landscape requires the company to secure customers and maintain effective relationships with important institutional end users. The challenge is for Clearwater Paper to have a better understanding of retailers and various retail channels to distribute products. The newly installed Shelby project will help the company in meeting the needs from its customers and expediting the distribution process.

Qualified Personnel Retention

As the market becomes more quality-driven, there might be increasing demand for qualified personnel, making it difficult for Clearwater Paper to attract and retain employees with requisite skills sets. Changing demographics and labor work force trends may also result in a loss of knowledge and skills as experienced workers retire. In addition, the company has its own salesforce and connection to sale managers. If the company fails to attract, motivate, or retain key personnel, they may experience manufacturing delays and declining sales, which will further negatively affect its operation efficiency and cash flows.

Cost of Inputs & Environmental Regulation

Production of bleached paperboard and consumer tissue products requires a great number of chemicals, including petroleum-based polyethylene and certain petroleum-based latex chemicals. The price of such chemicals has remained volatile. Due to the fact that there are limited suppliers, Clearwater Paper might have less bargaining power over pricing of raw materials. In addition, stricter environmental regulation at state, federal, and international levels require the company to comply with climate change policies and other conditions. Such regulation might cause the company more expenditure on revising manufacturing process and control of raw materials.

Appendix 1: Model Summary

(Figures in mm USD)	Dec-16	Dec-17	Dec-18	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Dec-20	Dec-21	Dec-22	Dec-23	Dec-24	Dec-25
	FY2016	FY2017	FY2018	FY2019	Q1-2020	Q2-2020	Q3-2020	Q4-2020	FY2020	FY2021	FY2022	FY2023	FY2024	FY2025
Income Statement														
Revenue	1,734.8	1,730.4	1,724.2	1,761.5	477.9	480.5	457.4	479.7	1,895.5	1,927.6	1,948.7	1,968.7	1,986.0	1,986.9
EBITDA	202.4	177.3	4.0	161.0	46.8	76.0	76.9	52.8	252.5	212.0	210.5	212.6	214.5	214.6
Net Income	49.6	97.3	(143.8)	(5.6)	10.3	22.8	21.4	7.7	62.2	39.2	40.6	44.2	46.9	48.4
Earnings Per Share	\$ 2.90	\$ 5.88	\$ (8.72)	\$ (0.34)	\$ 0.62	\$ 1.37	\$ 1.28	\$ 0.46	\$ 3.72	\$ 2.33	\$ 2.42	\$ 2.64	\$ 2.80	\$ 2.88
Cash Flow Statement														
Capital Expenditures	(155.3)	(199.7)	(295.7)	(140.1)	(10.5)	(7.3)	(9.7)	(18.0)	(45.5)	(58.8)	(57.6)	(66.9)	(65.5)	(64.0)
Acquisitions	(67.4)	-	-	-	-	-	-	-	-	-	-	-	-	-
Divestitures	0.0	1.0	70.9	-	-	-	-	-	-	-	-	-	-	-
Dividend Payment	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Dividend Per Share	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Dividend Payout to Earnings	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Dividend Payout to Core FCF	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Dividend Yield	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Balance Sheet														
Current Assets	446.5	452.8	443.9	465.8	521.0	484.4	491.9	516.2	516.2	555.7	641.9	712.9	785.7	857.6
Non-Current Assets	1,237.8	1,349.5	1,344.2	1,411.9	1,375.9	1,357.0	1,335.0	1,325.7	1,325.7	1,286.5	1,249.7	1,225.1	1,201.2	1,177.7
Assets	1,684.3	1,802.3	1,788.1	1,877.7	1,896.9	1,841.4	1,826.9	1,841.9	1,841.9	1,842.2	1,891.6	1,938.0	1,986.9	2,035.4
Current Liabilities	366.5	419.3	449.3	280.4	290.4	247.5	239.6	246.9	246.9	208.0	216.8	219.0	221.0	221.0
Non-Current Liabilities	847.9	807.6	912.4	1,165.3	1,161.7	1,123.3	1,091.1	1,091.1	1,091.1	1,091.1	1,091.1	1,091.1	1,091.1	1,091.1
Liabilities	1,214.5	1,226.8	1,361.7	1,445.7	1,452.1	1,370.8	1,330.7	1,338.0	1,338.0	1,299.1	1,307.9	1,310.1	1,312.1	1,312.1
Shareholders' Equity	469.9	575.4	426.4	432.0	444.8	470.6	496.2	503.9	503.9	543.1	583.7	627.9	674.8	723.2
Cash	23.0	16.7	24.9	22.4	61.8	49.2	48.6	(44.6)	(44.6)	(135.7)	(35.8)	28.3	95.1	166.8
Debt	828.3	841.3	909.3	1,061.9	1,096.2	985.6	940.3	940.3	940.3	940.3	940.3	940.3	940.3	940.3
Net Debt	805.3	824.5	884.3	1,039.5	1,034.4	936.4	891.7	984.9	984.9	1,076.0	976.1	912.0	845.2	773.5
Minority Interests	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Debt/EBITDA	4.0 x	4.7 x	218.7 x	6.5 x				3.9 x	5.1 x	4.6 x	4.3 x	3.9 x	3.6 x	
Operating Metrics														
Return on Equity (ROE)	10.5%	16.9%	-33.7%	-1.3%										
Return on Assets (ROA)	2.9%	5.4%	-8.0%	-0.3%										
Return on Invested Capital (ROIC)	3.4%	8.4%	-8.3%	1.8%										
Valuation Metrics	12.3%	7.2%	7.0%	7.0%	7.0%	7.0%	6.7%	3.4%	2.1%	2.1%	2.3%	2.4%	2.4%	2.4%
Stock Price (High)	\$ 68.40	\$ 47.75	\$ 39.95	\$ 29.16	\$ 25.75	\$ 39.87	\$ 42.45	\$ 40.80	\$ 42.45	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80
Stock Price (Low)	\$ 62.00	\$ 42.70	\$ 21.55	\$ 15.82	\$ 15.87	\$ 34.81	\$ 34.70	\$ 40.80	\$ 15.87	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80
Stock Price (Average)	\$ 65.20	\$ 45.23	\$ 30.75	\$ 22.49	\$ 20.81	\$ 37.34	\$ 38.58	\$ 40.80	\$ 29.16	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80	\$ 40.80
Diluted Shares Outstanding (Average)	17.1	16.6	16.5	16.5	16.6	16.7	16.8	16.8	16.7	16.8	16.8	16.8	16.8	16.8
Market Capitalization (Average)	1,115.3	748.7	507.0	371.8	345.8	623.1	647.4	684.7	487.5	684.7	684.7	684.7	684.7	684.7
Enterprise Value (Average)	1,920.7	1,573.3	1,391.3	1,411.3	1,380.1	1,559.4	1,539.1	1,669.6	1,472.3	1,760.8	1,660.8	1,596.8	1,529.9	1,458.3
P/E	22.5 x	7.7 x	n/a	n/a					7.8 x	17.5 x	16.9 x	15.5 x	14.6 x	14.2 x
EV/EBITDA	9.5 x	8.9 x	344.0 x	8.8 x					5.8 x	8.3 x	7.9 x	7.5 x	7.1 x	6.8 x
FCF Yield to Market Capitalization	1.1%	7.4%	-56.4%	-10.5%					13.0%	-6.9%	21.0%	15.8%	16.2%	16.9%
FCF Yield to Enterprise Value	0.6%	3.5%	-20.5%	-2.8%					4.3%	-2.7%	8.7%	6.8%	7.3%	8.0%
Free Cash Flow														
EBIT	111.3	72.3	(97.9)	45.4	18.8	48.2	49.2	25.5	141.7	114.0	116.0	121.2	125.1	127.1
Tax Expense	(31.1)	56.4	(10.3)	2.3	6.2	(10.4)	(9.9)	(6.9)	(38.3)	(30.8)	(31.3)	(32.7)	(33.8)	(34.3)
D&A	91.1	105.0	102.0	115.6	28.0	27.8	27.7	27.3	110.8	98.1	94.5	91.4	89.4	87.5
Capital Expenditures	(155.3)	(199.7)	(295.7)	(140.1)	(10.5)	(7.3)	(9.7)	(18.0)	(45.5)	(58.8)	(57.6)	(66.9)	(65.5)	(64.0)
Changes in NWC	(3.5)	21.8	16.2	(62.4)	(29.3)	42.8	(8.5)	(110.2)	(105.2)	(169.5)	22.5	(4.7)	(4.0)	(0.2)
Unlevered Free Cash Flow	12.5	55.7	(285.8)	(39.2)	13.2	101.1	48.8	(82.3)	63.5	(47.1)	144.0	108.3	111.2	116.0
Valuation Summary														
Current Price	\$ 40.80													
Target Price	\$ 51.44													
Total Return	26.1%													
Recommendation	BUY													
DCF Valuation														
Perpetuity Growth Implied Price	\$ 66.63													
Exit Multiple Implied Price	\$ 37.10													
Comps Valuation														
Comps - EV/EBITDA Implied Price	\$ 51.87													
Comps - P/E Implied Price	\$ 50.15													

Appendix 2: Discounted Cash Flow Analysis

	Dec-16	Dec-17	Dec-18	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Dec-20	Dec-21	Dec-22	Dec-23	Dec-24	Dec-25
(Figures in mm USD)	FY2016	FY2017	FY2018	FY2019	Q1-2020	Q2-2020	Q3-2020	Q4-2020	FY2020	FY2021	FY2022	FY2023	FY2024	FY2025
WACC Calculations														
Cost of Equity														
Risk-free rate	1.1%													
Expected market return	10.0%													
Market Risk Premium	8.9%													
Beta	1.48													
Cost of Equity	14.3%													
Cost of Debt														
Pre-tax cost of debt	1.8%													
Effective tax rate	27.0%													
Cost of Debt	1.3%													
WACC														
Market value of equity	684.7													
Market value of debt	940.3													
Total Capitalization	1,625.0													
Cost of equity	14.3%													
Cost of debt	1.3%													
WACC	6.8%													
Free Cash Flow														
EBIT	111.3	72.3	(97.9)	45.4	18.8	48.2	49.2	25.5	141.7	114.0	116.0	121.2	125.1	127.1
Less: Tax expense	(31.1)	56.4	(10.3)	2.3	6.2	(10.4)	(9.9)	(6.9)	(38.3)	(30.8)	(31.3)	(32.7)	(33.8)	(34.3)
Add: Depreciation and amortization	91.1	105.0	102.0	115.6	28.0	27.8	27.7	27.3	110.8	98.1	94.5	91.4	89.4	87.5
Less: Capital expenditures	(155.3)	(199.7)	(295.7)	(140.1)	(10.5)	(7.3)	(9.7)	(18.0)	(45.5)	(58.8)	(57.6)	(66.9)	(65.5)	(64.0)
Less: Change in net working capital	(3.5)	21.8	16.2	(62.4)	(29.3)	42.8	(8.5)	(110.2)	(105.2)	(169.5)	22.5	(4.7)	(4.0)	(0.2)
Unlevered Free Cash Flow	12.5	55.7	(285.8)	(39.2)	13.2	101.1	48.8	(82.3)	63.5	(47.1)	144.0	108.3	111.2	116.0
Discount factor	-	-	-	-	-	-	-	0.25	0.25	1.25	2.25	3.25	4.25	5.25
Present Value of Unlevered Free Cash Flow								(81.0)	(81.0)	(47.5)	124.3	87.5	84.2	82.3
Discounted Cash Flow Valuations														
Perpetuity Growth Method														
Perpetuity Growth Rate	2.0%													
PV sum of unlevered FCF	249.8													
Terminal value	1,760.1													
Enterprise Value	2,009.9													
Add: Cash	48.6													
Less: Debt	940.3													
Less: Other EV adjustments	-													
Equity Value	1,118.2													
Shares outstanding	16.8													
Implied Share Price	\$ 66.63													
Current Price	\$ 40.80													
Implied Price	\$ 66.63													
Total Return	63.3%													
Exit Multiple Method														
Terminal EV/EBITDA Multiple														
	8.3 x													
PV sum of unlevered FCF	249.8													
Terminal value	1,264.5													
Enterprise Value	1,514.3													
Add: Cash	48.6													
Less: Debt	940.3													
Less: Other EV adjustments	-													
Equity Value	622.6													
Shares outstanding	16.8													
Implied Share Price	\$ 37.10													
Current Price	\$ 40.80													
Implied Price	\$ 37.10													
Total Return	-9.1%													
WACC														
	7.80%	7.30%	6.80%	6.30%	5.80%									
Perpetuity Growth Rate	1.00%	\$ 30.23	\$ 37.93	\$ 46.97	\$ 57.71	\$ 70.70								
	1.50%	\$ 36.10	\$ 44.95	\$ 55.47	\$ 68.19	\$ 83.88								
	2.00%	\$ 42.97	\$ 53.28	\$ 65.74	\$ 81.11	\$ 100.53								
	2.50%	\$ 51.14	\$ 63.35	\$ 78.41	\$ 97.43	\$ 122.23								
	3.00%	\$ 61.02	\$ 75.77	\$ 94.40	\$ 118.69	\$ 151.67								
WACC														
	7.80%	7.30%	6.80%	6.30%	5.80%									
Terminal EV/EBITDA Multiple	6.3 x	\$ 15.31	\$ 17.01	\$ 18.76	\$ 20.56	\$ 22.41								
	7.3 x	\$ 23.92	\$ 25.84	\$ 27.81	\$ 29.83	\$ 31.92								
	8.3 x	\$ 32.54	\$ 34.67	\$ 36.86	\$ 39.11	\$ 41.43								
	9.3 x	\$ 41.16	\$ 43.50	\$ 45.91	\$ 48.39	\$ 50.94								
	10.3 x	\$ 49.78	\$ 52.34	\$ 54.96	\$ 57.67	\$ 60.45								

Appendix 3: Comparable Company Analysis

(Figures in mm USD)															
Company	Ticker	Equity Value	Enterprise Value	EV/EBITDA Multiple			P/E Multiple								
				2020A EBITDA	2021E EBITDA	2022E EBITDA	2020A EV/EBITDA	2021E EV/EBITDA	2022E EV/EBITDA	2020A Diluted EPS	2021E Diluted EPS	2022E Diluted EPS	2020A P/E	2021E P/E	2022E P/E
Verso Corporation	NYSE: VRS	440.7	372.7	(19.0)	113.5	119.0	n/a	3.3 x	3.1 x	(3.0)	\$ 0.57	\$ 1.40	(4.4 x)	22.9 x	9.3 x
Neenah, Inc.	NYSE: NP	908.9	1,110.3	101.4	110.0	137.0	10.9 x	10.1 x	8.1 x	(1.0)	\$ 2.70	\$ 3.68	(56.4 x)	20.0 x	14.7 x
Glatfelter Corporation	NYSE: GLT	792.9	1,065.6	100.0	120.0	121.0	10.7 x	8.9 x	8.8 x	0.5	\$ 0.76	\$ 0.95	38.0 x	23.5 x	18.8 x
Domtar Corporation	NYSE: UFS	2,037.8	2,903.0	358.0	375.0	475.0	8.1 x	7.7 x	6.1 x	(0.6)	\$ 2.83	\$ 3.46	(59.8 x)	13.1 x	10.7 x
Cascades Inc.	TSE: CAS	1,620.1	3,083.3	358.8	441.5	470.5	8.6 x	7.0 x	6.6 x	(2.6)	\$ 2.83	\$ 3.46	(6.0 x)	5.6 x	4.6 x
Clearwater Paper Corporation	NYSE: CLW	676.2	1,567.9	252.5	212.0	210.5	6.2 x	7.4 x	7.4 x	\$ 3.72	\$ 2.33	\$ 2.42	11.0 x	17.5 x	16.9 x
Median							8.3 x	7.1 x						21.5 x	12.7 x
Mean							7.5 x	6.5 x						19.9 x	13.4 x
High							10.1 x	8.8 x						23.5 x	18.8 x
Low							3.3 x	3.1 x						13.1 x	9.3 x
Median							EV/EBITDA Implied Price							P/E Implied Price	
Mean							\$ 51.87	\$ 36.00						\$ 50.15	\$ 30.73
High							\$ 51.87	\$ 36.00						\$ 50.15	\$ 30.73
Low							\$ 74.40	\$ 57.30						\$ 54.89	\$ 45.50
							-\$ 11.64	-\$ 13.85						\$ 30.56	\$ 22.58

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