

DOMTAR CORPORATION **ANALYST REPORT**

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RECOMMENDATION:
BUY

YALE SCHOOL OF MANAGEMENT

DOMTAR CORPORATION SHOWS UNDERVALUATION SIGNS THAT DON'T REFLECT ITS FUNDAMENTAL VALUE

- Closely following the company's trends, projections from management and our own assumptions and interpretations of the paper mills market, we developed a 3 scenario valuation that yielded:

Share Price	USD 52.81
Current Price	USD 44.19
Premium	20%

- The company presents strong cash flows, a solid balance sheet and consistent capital structure
- Favourable performance in Paper and Pulp have offset the difficult quarter for Personal Care. Sales growth is expected to continue with the announcement of higher prices in the market
- Lower maintenance costs should help realize growth quicker heading into the fourth quarter as raw material and commodity prices remain constant
- The company shows a strong balance sheet, stable capital structure with low leverage
- Provided substantial amounts of money back to shareholders over time and expect to continue doing so

Please see the disclaimer at back of this report for important information.

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Section 1: Company Overview

Introduction

Domtar Corporation is a world-leading manufacturer, marketer, and distributor of fiber-based products in North America. Domtar operates in its two product segments: 1) Pulp and Paper, and 2) Personal Care. Domtar's products consist of various communication papers, absorbent hygiene products, and specialty and packaging papers. Domtar has approximately 10,000 employees working for the firm and its CEO is John D. Williams. Domtar has early roots as it was founded in England in 1848 and continued to expand and grow into the North American territory. Domtar's main headquarter office is located in Fort Mill, South Carolina. Domtar has its corporate offices and divisional headquarters situated in 3 locations: South Carolina, North Carolina, and Quebec.

Exhibit 1.

Key Domtar Snapshot (As of Dec 3, 2018)

Open	Day Range	52 Week Range	Market Cap	Shares Outstanding	Public Float	Beta	Revenue/Employee
\$44.44	43.35-44.77	40.72-54.50	\$2.74B	62.9M	62.83M	1.16	\$540.2K
P/E Ratio	EPS	Yield	Dividend	Ex-Dividend Date	Short Interest	% of Float Shorted	Avg Volume
N/A	\$-2.31	3.94%	\$0.44	Dec 31, 2018	2.3M	3.66%	651.07K

(Source: MarketWatch)

**Exhibit 2.
Domtar Office Locations**



(Source: Domtar: <https://www.domtar.com/en/who-we-are/all-locations>)

Domtar has approximately 29 locations in 5 countries (Canada, USA, Spain, Germany, Sweden). Most of its locations are heavily situated in the United States and Canada. Domtar has tried to expand a bit globally, but has only done so with regards to their personal care products.

**Exhibit 3.
Domtar Facilities**



(Source: Domtar: <https://www.domtar.com/sites/default/files/2018-05/Domtar-coportate-FactSheet-2018-v2.pdf>)

Provided above is a facility breakdown of the main mills, site, and plants that Domtar owns. Domtar has most of its facilities invested in pulp and paper mills. The 10 converting sites in North America are used to process the raw paper and complete it into a finished product. The personal care plants are quite new and several locations are situated in Europe.

Section 2: Product Analysis

Exhibit 4.

Revenues by Segmentation

Business Segments						
	Reclassified 3 months Q2	Reclassified 3 months Q3	3 months Q4	3 months Q1	3 months Q2	3 months Q3
For the Fiscal Period Ending	<u>Jun-30-2017</u>	Sep-30-2017	Dec-31-2017	Mar-31-2018	<u>Jun-30-2018</u>	Sep-30-2018
Currency	USD	USD	USD	USD	USD	USD
Revenues						
Pulp and Paper (Incl. Distribution)	999.0	1,054.0	1,090.0	1,100.0	1,123.0	1,146.0
Personal Care	238.0	251.0	262.0	262.0	247.0	237.0
Intersegment Sales	(16.0)	(15.0)	(15.0)	(17.0)	(17.0)	(16.0)
Total Revenues	1,221.0	1,290.0	1,337.0	1,345.0	1,353.0	1,367.0

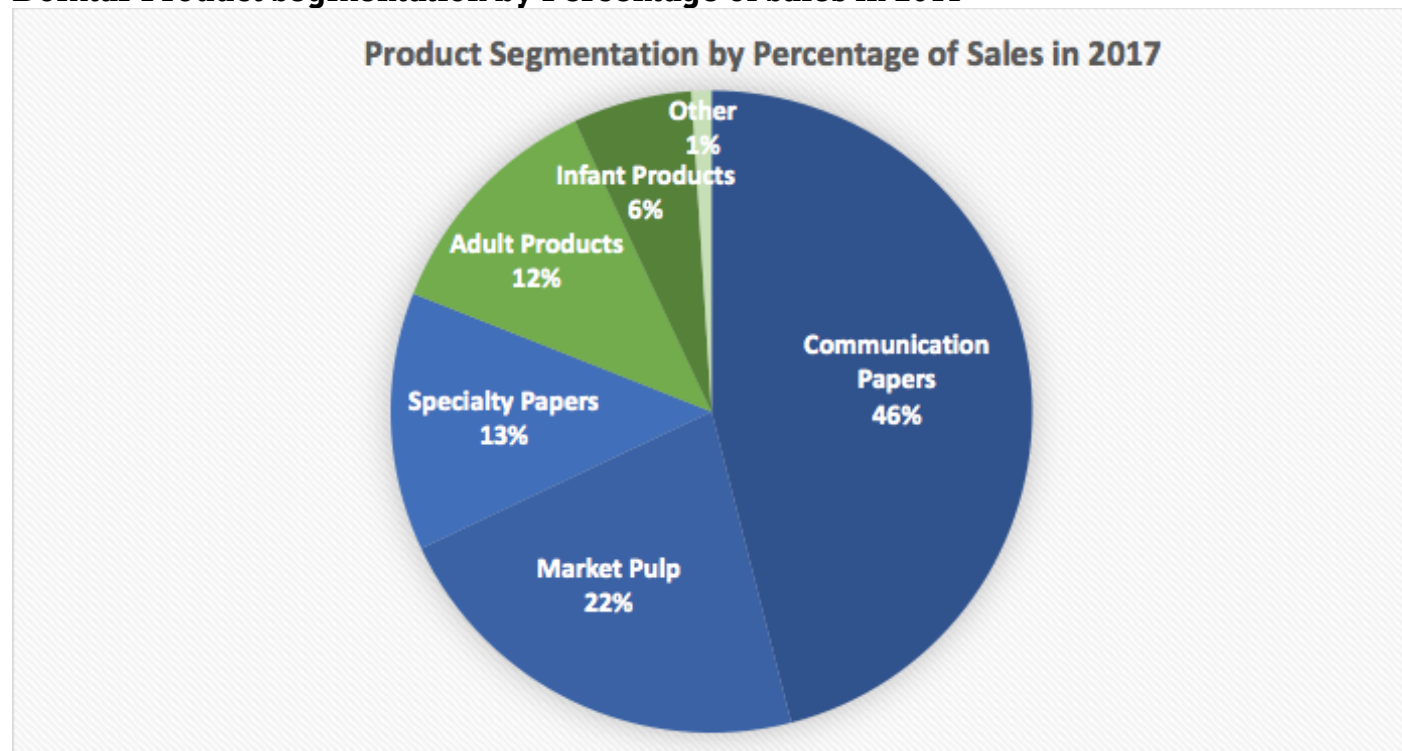
(Source: Capital IQ)

Pulp and paper has increased in the past quarter, while personal care has struggled slightly.

The main reasons for personal care dwindling in revenue growth is due to increased raw material costs with lower prices. The recent closure of a facility in Waco, Texas will help revert this effect moving forward. Pulp and Paper has performed well and offset the weaker quarter in personal care. Pulp and Paper's large segment has the ability to offset the performance by Personal Care by the overwhelming proportion Pulp and Paper has. Personal Care is also dependent on Pulp and Paper as raw materials from Pulp and Paper actually channel through to the Personal Care segmentation. Personal care will gain relevance and produce positive impact as it has greater margin potential

Exhibit 5.

Domtar Product Segmentation by Percentage of Sales in 2017



(Source: Domtar: <https://www.domtar.com/sites/default/files/2018-05/Domtar-coportate-FactSheet-2018-v2.pdf>)

Subsegments observed in blue are within the paper and pulp segment and portions in green are within the personal care segment. The paper and pulp segment dominates the sales breakdown at 81% with the personal care segment at 19%. The segmentation is quite diverse with communication papers topping the breakdown at 46% and market pulp at 22%.

1. Paper and Pulp

Paper Products:

i) Business Papers (52% of Paper Product Shipments)

Includes copy, electronic imaging, computer, preprinted forms, and digital papers. These products can be used along with inkjet printers, laser printers, photocopiers, and fax machines.

ii) Commercial Print & Publishing Papers (31% of Paper Product Shipments)

Includes uncoated freesheet papers and roll fed offset paper for commercial print papers.

Includes tradebook and lightweight uncoated papers (ex: textbooks, magazines, financial documents), base papers (ex: envelopes, business forms) for publishing papers.

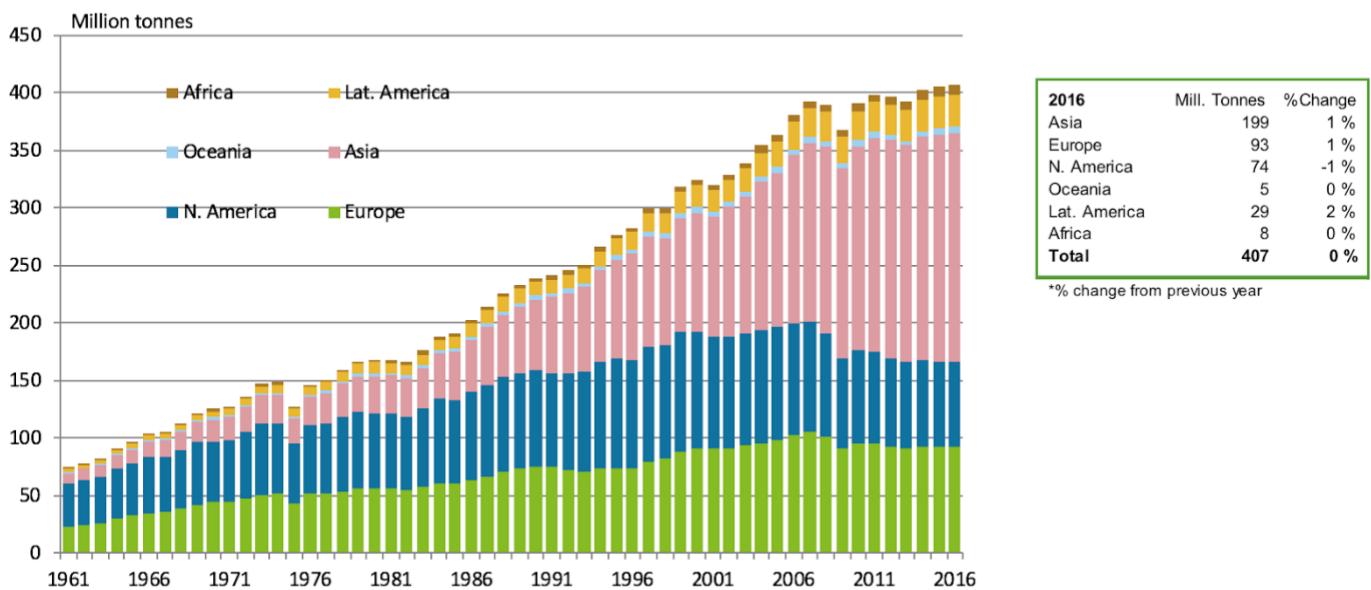
iii) Speciality and Packaging Papers (17% of Paper Product Shipments)

Includes thermal and flexible printing, food and medical packaging, sandpaper backing, carbonless printing, and labelling applications. Manufacturing of industrial and specialty applications of carrier, treated, security, and specialized papers are also produced.

Exhibit 6.

Global Paper and Board Consumption

PAPER AND BOARD CONSUMPTION BY WORLD REGIONS



2016	Mill. Tonnes	%Change
Asia	199	1 %
Europe	93	1 %
N. America	74	-1 %
Oceania	5	0 %
Lat. America	29	2 %
Africa	8	0 %
Total	407	0 %

*% change from previous year

SOURCE: FAO
3.8.2017

(Source: Finnish Forest Industries: <https://www.forestindustries.fi/statistics/pulp-and-paper-industry/>)

World consumption has substantially increased over time. Various paper and board usage is necessary for daily tasks, product delivery, and the working world. Paper is a commodity that is needed in today's society and will be in the foreseeable future.

Exhibit 7.

Paper Segment Breakdown on EBITDA

Paper Segment Breakdown (Each \$10/tonne change in the selling price of below products)	Annualized impact on EBITDA
Business Papers	\$15
Commercial Print & Publishing Papers	\$9
Specialty & Packaging Papers	\$6

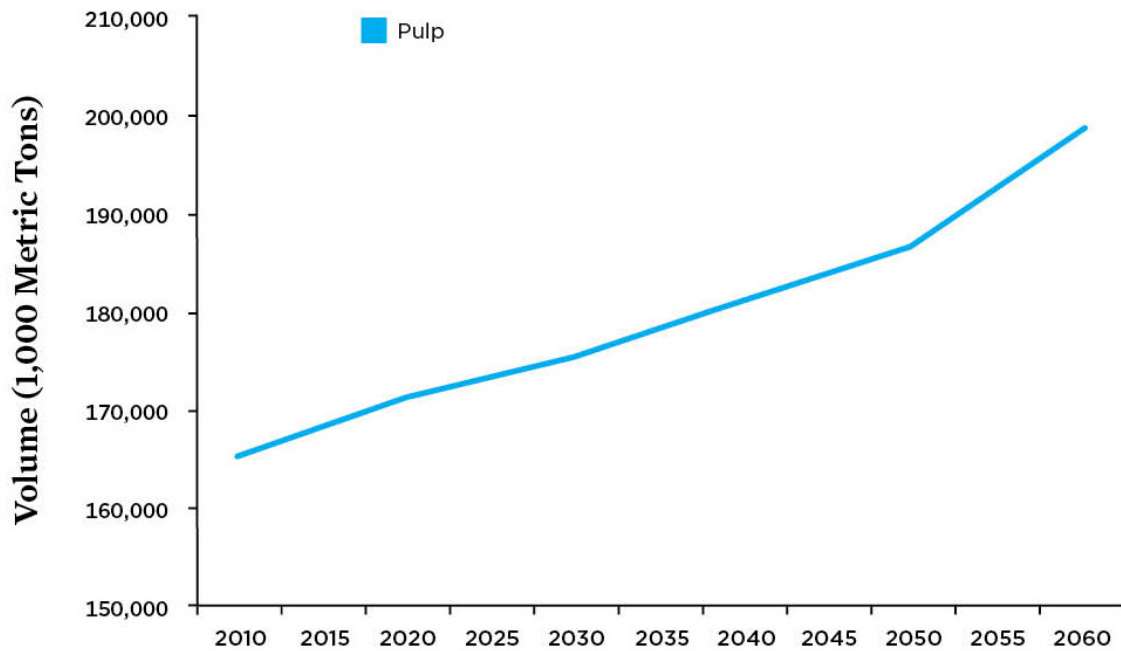
(Source: Domtar Corporation Quarter 3 Earnings Call)

Pulp Products:

Includes products derived from softwood, fluff, and hardwood kraft, which are eventually sold to end-customers globally. Products include diapers, personal hygiene products, bathroom and facial tissue, specialty and packaging papers, printing and writing grades, and insulating papers.

Exhibit 8.
Wood Pulp Consumption, 2010-2060

Projected Consumption of Wood Pulp, 2010-2060



(Source:UCSUSA: <https://www.ucsusa.org/sites/default/files/images/2016/03/tfci-drivers-consumption-wood-pulp.jpg>)

Demand for wood pulp and paper is expected to significantly increase over the next half century. Pulp becomes a commodity of need because increased usage of end products related to pulp.

Exhibit 9.

Pulp Segment Breakdown on EBITDA

Pulp Segment Breakdown (Each \$10/tonne change in the selling price of below products)	Annualized impact on EBITDA
Softwood Pulp	\$10
Fluff Pulp	\$7
Hardwood Pulp	\$1

(Source: Domtar Corporation Quarter 3 Earnings Call)

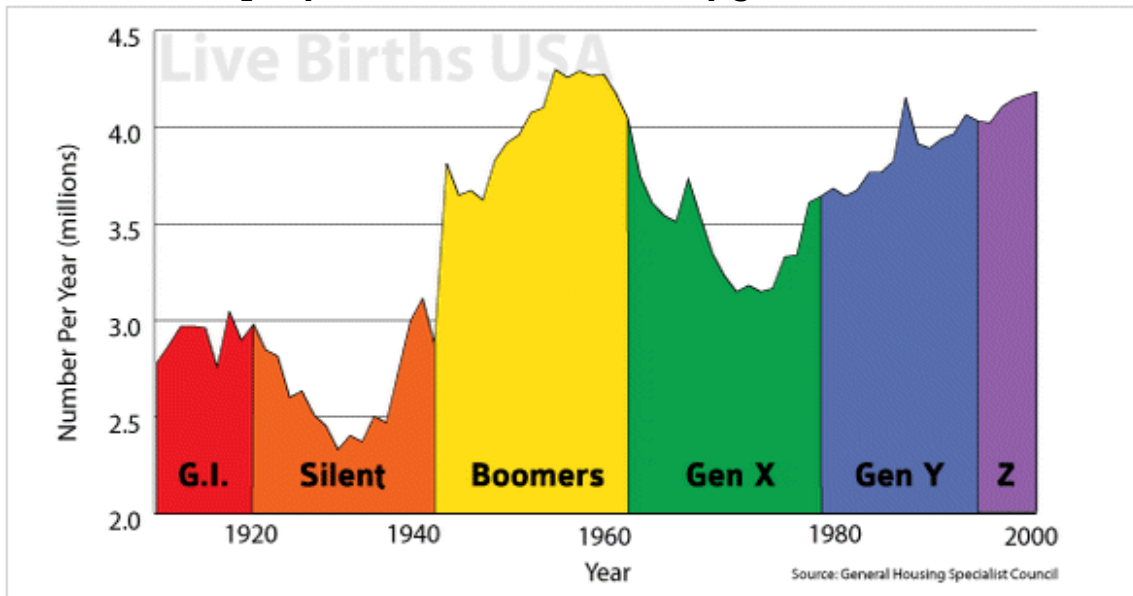
2. Personal Care Products (Absorbent Hygiene Products)

i) Adult Products - 12% of 2017 Sales

Adult incontinence will become far more important in the next few decades because baby boomer generation will continue to grow older. The average lifespan continues to expand with increased growth in technology and medical advances, so incontinence will becoming a pertinent issue.

Exhibit 10.

Number of live births per year in the USA, divided by generation

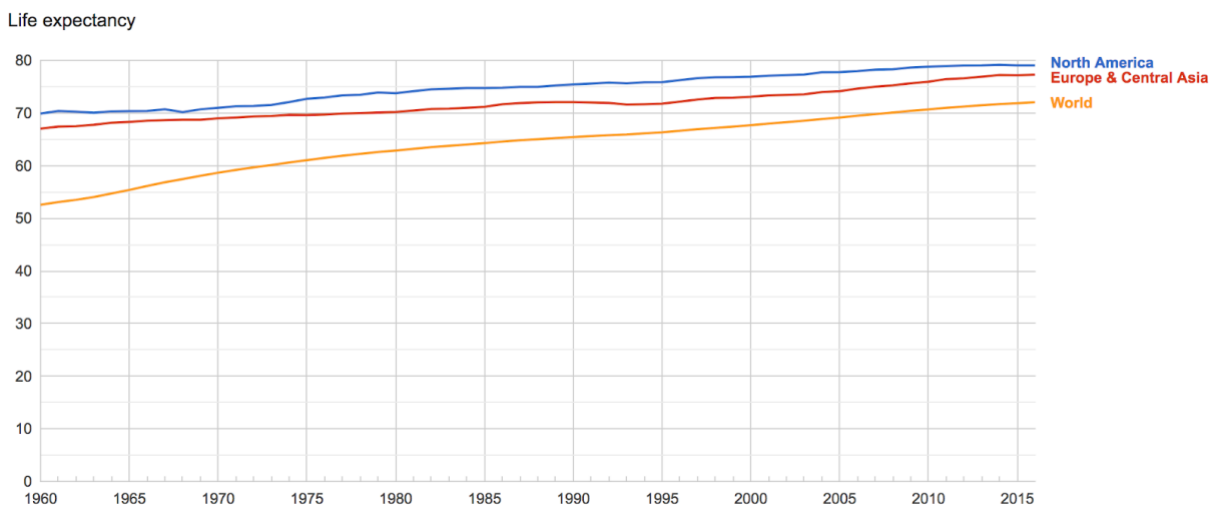


(Source: <http://www.doctorhousingbubble.com/wp-content/uploads/2014/03/Gen-Breakdown.gif>)

Baby boomers highlighted in yellow are a significant portion of the population that will be entering retirement and older age, meaning that adult incontinence products will become more and more relevant as the years continue in the long-term.

Exhibit 11.

Life Expectancy for North America, Europe, and the World



(Source: Google Public Data - World Bank)

Another important aspect to consider is that with increased medical advancements and technology, our population has the fortunate ability to live longer, more prosperous lives. With this, more personal care products will be needed in the future for elderly people to use.

Acquisition of Home Delivery Incontinent Supplies

Approximately two years ago in 2016, Domtar acquired Home Delivery Incontinent Supplies Company (HDIS). Based in Missouri, HDIS is a leader of adult incontinence products. The acquisition helped Domtar take a huge step forward into revolutionizing their personal care and adult incontinence products, since their segmentation is rather low. The integration was successful and the purchase price was \$52M.

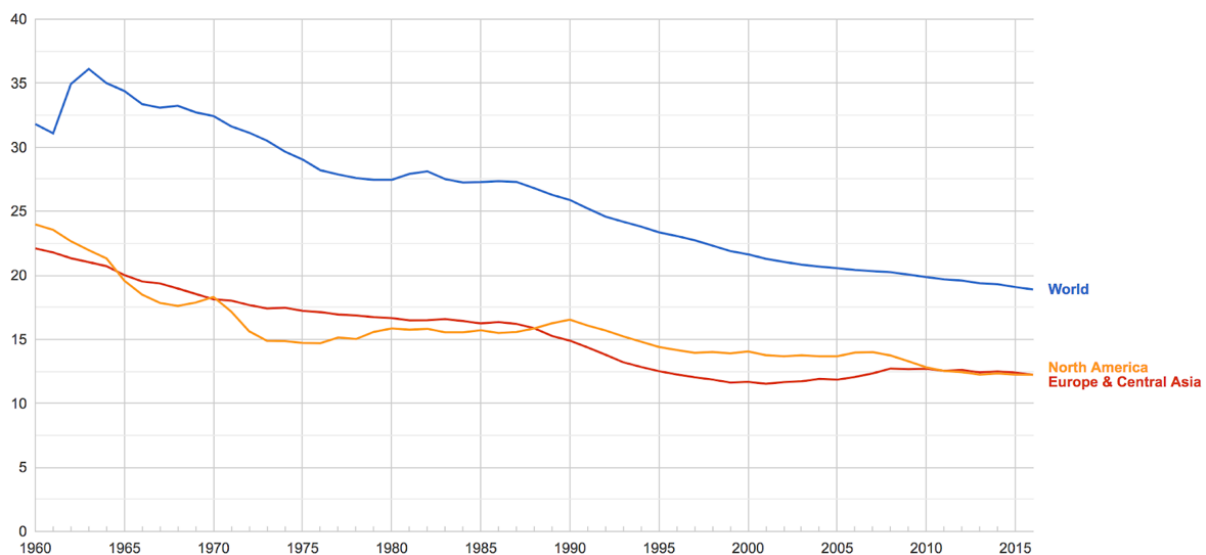
ii) Infant Products - 6% of 2017 Sales

The space for infant diapers and training pants is exceedingly competitive, especially with procuring contracts with the major retailers who dominate the North American market. The demand of this product segment is expected to have flat growth based on birth rate.

Exhibit 12.

Crude Birth for North America, Europe, and the World

Birth rate, crude (per 1,000 people)

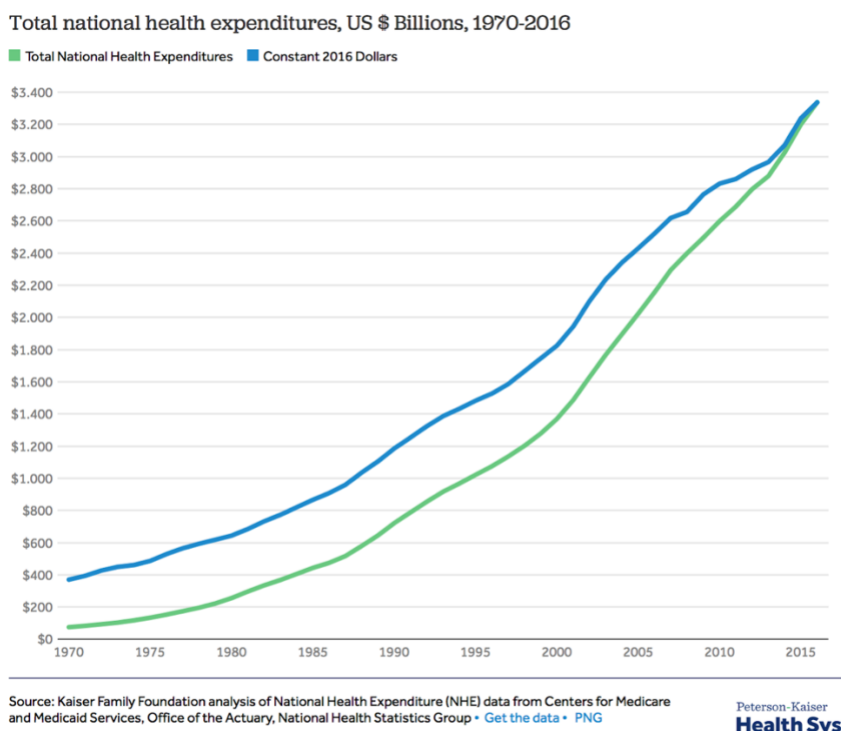


(Source: Google Public Data - World Bank)

The main takeaway here is that the North America and Europe crude birth rates have flat growth and this means that the infant product segment will continue to remain competitive with birth rates staying the same.

Exhibit 13.

Increased Healthcare Spending



(Source: Peterson-Kaiser Health System Tracker: <https://s3.eu-central-1.amazonaws.com/datawrapper-exports/exports/u34BE.png>)

The main takeaway of this chart is demonstrate the drastic increase in healthcare expenditure in the US, that it is actually skyrocketing to newer heights annually.

Raw Materials

Increasing raw material costs in the personal care segment with challenging marketing conditions have dampened quarter 3 for the personal care segment. The main materials used in the personal care product process are fluff pulp, nonwovens, and super absorbent polymers.

Closing of Waco, Texas Personal Care Manufacturing and Distribution Facility

This closure is part of a margin improvement plan that will reduce costs and improve long-term positioning for personal care. The closure will now proceed with relocation of its assets in manufacturing and workforce allocation across the personal care industry. Operations were close in quarter 3 and had a temporary working loss of 148 full-time employees.

Section 3: Business Analysis

Margin Improvement Initiatives

The purpose of the initiatives is to actually target approximately \$25-30M of EBITDA

Improvement. Long-term, Domtar hopes to reduce cost base and strengthen their competitive position by implementing the following actions:

- Headcount Reduction
- Price Initiatives
- SKU rationalization
- Customer rationalization
- Productivity and Supply Chain Efficiencies
- Equipment Relocation

(Source: Domtar Quarter 3 Earnings Call Deck)

Exhibit 14.

2020 Sustainability Initiatives

Initiative	Benchmark Goal	Actual Result	Analysis
Reduce recordable safety incident rate by 0.50 by 2020 while increasing focus and efforts on preventing more serious injuries	0.50	0.78	Benchmark not met. Incident rate decreased to a best year of 0.78. However, a fatality occurred at the British Columbia mill, which is not reflective in this rate. This death has made Domtar more focused on injury prevention and elimination of hazardous tasks.

Establish EarthChoice Ambassador (ECA) Teams in all our facilities by 2020, engaging employees in commitment to sustainability.	100%	76%	Benchmark not met. Expansion is rather slow, but spread has now included 26 locations in 4 countries. There is promise in growth, and expectation will hopefully reach benchmark by 2020.
Reduce total waste to landfill from pulp and paper mills 40% by 2020 from 2013	40%	36%	Benchmark not met. Through source reduction and beneficial use, Domtar has set its sights to reduce its waste, but is currently at 36%.
Increase the level of Forest Stewardship Council (FSC) certified fiber procured for our pulp and paper mills to 20% of total fiber used by 2020.	20%	22%	Benchmark fulfilled and exceeded. Domtar has been increasingly more compliant with the FSC, who is responsible for management of forests worldwide and setting standards on forest products, ensuring they are eco-friendly.
Reduce total direct and indirect greenhouse gas (GHG) emissions from purchased energy at pulp and paper mills 15% by 2020 from 2010 levels.	15%	18%	Benchmark fulfilled and exceeded. Domtar has greatly reduced their GHG emissions from mills and is far ahead of schedule.
Develop a model for pulp and paper mills to measure and more strategically manage the full cost of using water.	100%	100%	Benchmark fulfilled. Water-cost model was completed, which was used at 5 mills in the past two years to address water conditions. Domtar has future plans to further assess water-cost models.

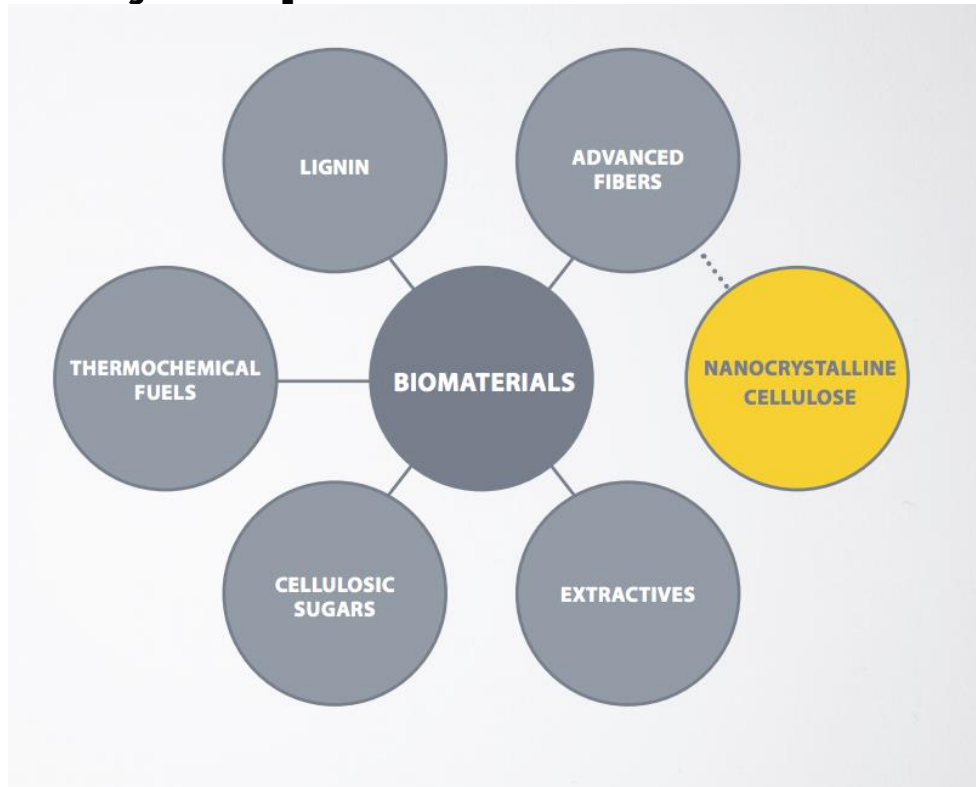
(Source: Domtar website: <https://www.domtar.com/sites/default/files/2018-06/Domtar-2018%20Sustainability-Update-En.pdf>)

Domtar's promise to its sustainability initiatives make this company very exciting and promising in the long-term. Half of its initiatives have been met and some even exceeded. By

2020, Domtar is confident that it can meet its aims to produce better quality work and sustainability.

Exhibit 15.

Domtar Innovation Agenda: Expansion into Biomaterials



(Source: Domtar 10K)

Domtar owns approximately 1.8M tons of high-quality market pulp capacity, mainly serving global softwood and fluff pulp markets. Domtar is a leading expert in using trees as feedstock, but they are now trying to branch out and produce feasible biodegradable alternatives that can be achieved with materials or chemicals. This product line has not been released, but Domtar has hopes to eventually release a Biomaterials segment to craft high-quality, advanced and sustainable products. The goal is to combine Domtar's expertise in fiber and secure new horizons that can reshape sustainability for customers.

Section 4: Financial Analysis

Exhibit 16.

Domtar Stock Performance

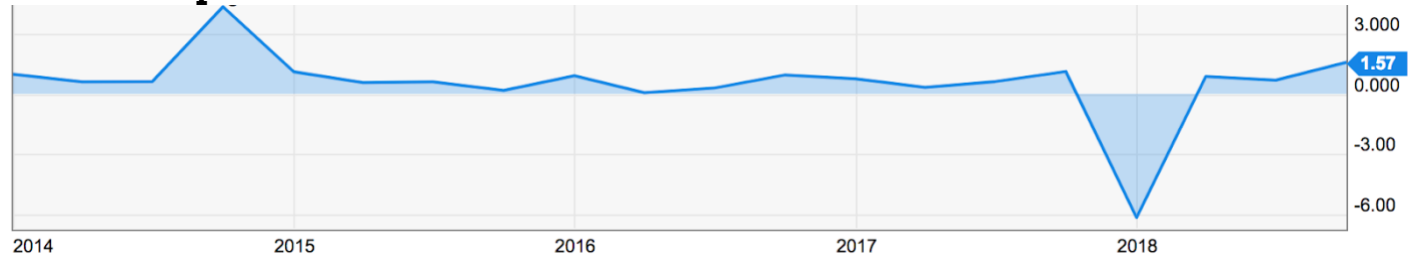


(Source: MarketWatch)

Domtar's stock performance over time has shifted a number of times. However, Domtar is an opportune company to purchase stock in because of their momentum entering the fourth quarter with respect to their pulp and paper segment, reduction of cost base, maximization of price initiatives, and strengthening of long-term outlooks.

Exhibit 17.

Domtar Corporation Diluted EPS

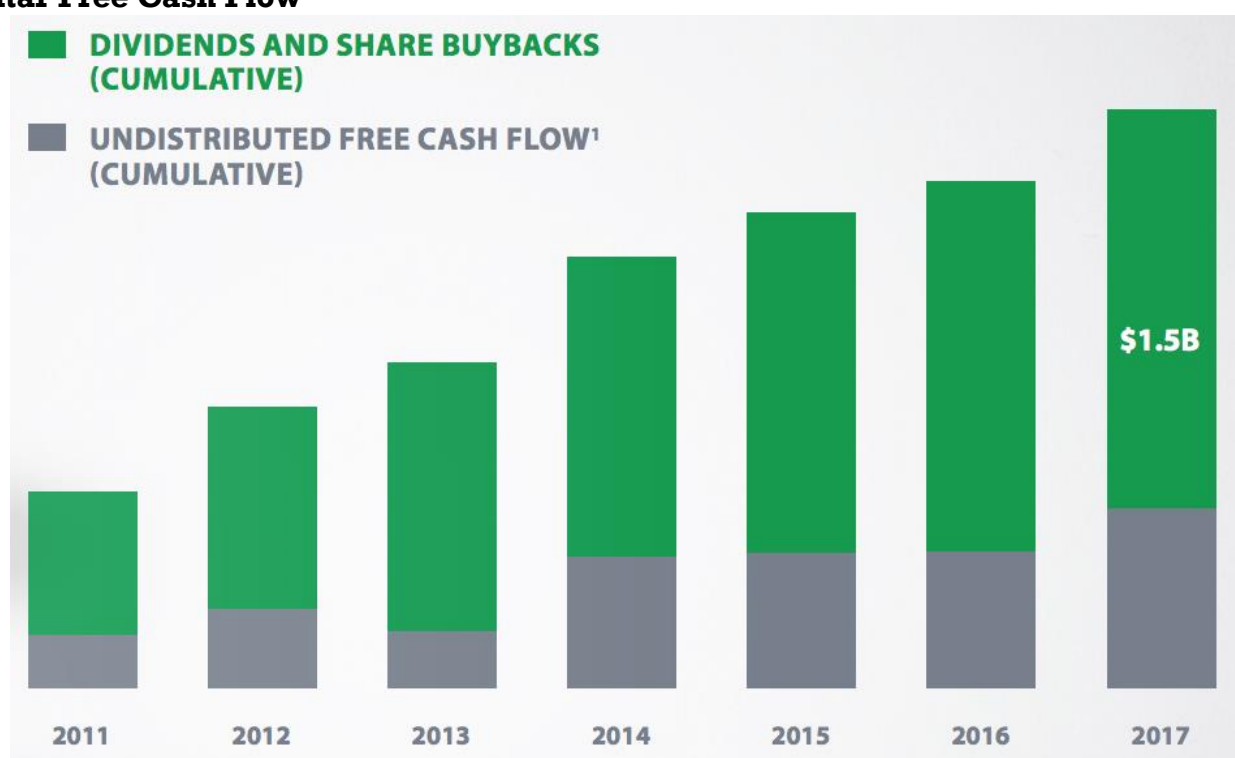


(Source: YCharts: <https://ycharts.com/companies/UFS/eps>)

EPS has increased in the short-term. The major drop in EPS at the brink of 2018 is due to several factors taking place. At the quarter end of 2017, Domtar suffered a non-cash goodwill impairment charge with respect to personal care at \$578M. In quarter 4 of 2017, Domtar also realized a net tax benefit of \$140M from the US Tax Reform and a net gain on disposal of PPE of \$9M. At the start of 2018, Domtar had closure and restructuring costs ranging at \$2M, while also having a gain on disposal of PPE of \$1M.

Exhibit 18.

Domtar Free Cash Flow



(Source: Domtar 10K)

Domtar has significantly increased its dividends and share buybacks over the past several years. Of the \$1.5B shareholder return in 2017, approximately \$600M was used in dividends and \$900M was channeled for share buybacks. A major commitment has been to return a major portion of the free cash back to the shareholders, which is a promise that Domtar has maintained. Of the \$2.2B of free cash flow, 0.7B (31%) of it remains undistributed. Fueled

primarily by the pulp and business segment, Domtar has continued to provide tremendous value and low-cost business to support monetary value back to its shareholders.

Exhibit 19.

Domtar Ratios in Comparison with other Competitors

Company Comp Set			
Company Name	TEV/EBITDA LTM - Latest	P/TangBV LTM - Latest	P/BV LTM - Latest
Packaging Corporation of America (NYSE:PKG)	7.8x	7.2x	3.6x
Berry Global Group, Inc. (NYSE:BERY)	9.0x	NM	4.6x
WestRock Company (NYSE:WRK)	6.2x	4.3x	1.0x
Empresas CMPC S.A. (SNSE:CMPC)	9.1x	-	-
International Paper Company (NYSE:IP)	7.0x	5.1x	2.7x
Resolute Forest Products Inc. (NYSE:RFP)	2.7x	0.6x	0.5x
Clearwater Paper Corporation (NYSE:CLW)	6.6x	1.4x	0.8x
Sappi Limited (JSE:SAP)	6.0x	1.5x	1.5x
Mondi plc (LSE:MNDI)	8.0x	4.3x	2.9x
Daio Paper Corporation (TSE:3880)	9.9x	1.6x	1.1x
Domtar Corporation (NYSE:UFS)	5.8x	1.4x	1.1x
Summary Statistics	TEV/EBITDA	P/TangBV LTM -	P/BV LTM -
High	9.9x	7.2x	4.6x
Low	2.7x	0.6x	0.5x
Mean	7.2x	3.3x	2.1x
Median	7.4x	2.9x	1.5x

(Source: Capital IQ)

Domtar has one of the lowest price to book values among competitors. Its TEV/EBITDA is at 5.8x, which is below the mean and medium. The ratios for P/Tang BV and P/BV LTM are also below the mean and medium, which suggests the firm's high potential.

Exhibit 20.

Domtar Capital Structure

Capital Structure Data

For the Fiscal Period Ending Currency	12 months Dec-31-2016		12 months Dec-31-2017		3 months Sep-30-2018	
	USD		USD		USD	
	Millions	% of Total	Millions	% of Total	Millions	% of Total
Total Debt	1,293.0	32.6%	1,130.0	31.3%	1,104.0	30.2%
Total Common Equity	2,676.0	67.4%	2,483.0	68.7%	2,553.0	69.8%
Total Capital	3,969.0	100.0%	3,613.0	100.0%	3,657.0	100.0%










Source: Capital IQ




This figure demonstrates the split in capital structure of Domtar's debt and common equity.

Domtar has a 30% debt to 70% equity breakdown structure-wise, demonstrating their consistency in the past two years.

Exhibit 21.

Domtar Supply Chain Relationships are Strong

Rel Type	Rel Rank	Company	Ctry	Industry	Relationship Value (\$)	Mkt Cap (\$)	Disclosures/Source	3M Price Correlation
	1	Staples	USA	Office Supplies and Stationery Retail	516	-	Direct	-
	2	Xerox	USA	Computer Peripherals	-	6,415	Direct	0.48
	3	Minerals Technologies	USA	Nonmetallic Minerals Products	-	1,984	Reverse	0.93
	4	Rayonier Advanced Materials	USA	Specialty/Performance Fibers and ...	-	753	Direct	0.86
	5	Argan	USA	Infrastructure Construction/Contract...	-	677	Reverse	-0.20
	6	Columbia Forest Products, Inc.	USA	Forest Products	-	-	Direct	-
	7	TRC Cos	USA	Infrastructure Construction/Contract...	-	-	Reverse	-
	8	Canadian National Railway	CAN	Road and Rail Transportation Oper...	-	62,556	Reverse	0.55
	9	Elementia	MEX	General Construction Materials Ma...	-	710	Reverse	0.65
	10	Sanacorp Phahold VZ	DEU	Healthcare Distributors	-	312	Reverse	0.57

 SUPPLIERS
  CUSTOMERS
  PARTNERS

5 3 10

(Source: FactSet)

Domtar's Supply Chain relations with various companies are strong including its suppliers, customers, and partners. The industries that these relationships are fostered with are also diverse and wide-ranging, including office supplies, computer peripherals, and nonmetallic minerals to simply name the top three. The prestige that these supply chain connections are profound and most are located within the USA, where Domtar performs a majority of its operations.

Section 5: Quarter 3 Earnings Call

Exhibit 22.

Paper and Pulp Outlook

PAPER (in millions of dollars)				PULP (in millions of dollars)			
	3Q'18	vs. 2Q'18	vs. 3Q'17		3Q'18	vs. 2Q'18	vs. 3Q'17
Sales	\$820	↑ 1%	↑ 7%	Sales (incl. intersegment sales)	\$326	↑ 6%	↑ 12%
EBITDA before items*	\$134	↑ \$28	↑ \$9	EBITDA before items*	\$63	↑ \$26	↑ \$36
Shipments (manufactured, in thousands of short tons)	727	↓ 4%	↑ 1%	Shipments (in thousands of ADMT)	390	↑ 3%	↓ 8%
Transaction prices (US\$/ton – net, all regions)		↑ \$40	↑ \$73	Transaction prices (US\$/ADMT – net, all regions)		↑ \$23	↑ \$141

(Source: Domtar Quarter 3 Earnings Call Deck)

Paper and Pulp have performed well in quarter 3 with regards to sales and in response to the announcement of increased prices. The transaction prices seen are drastically higher and are expected to maintain the quarter 3 price going into quarter 4. Shipments have performed decently relative to past indices.

Exhibit 23.

Personal Care Outlook

(in millions of dollars)

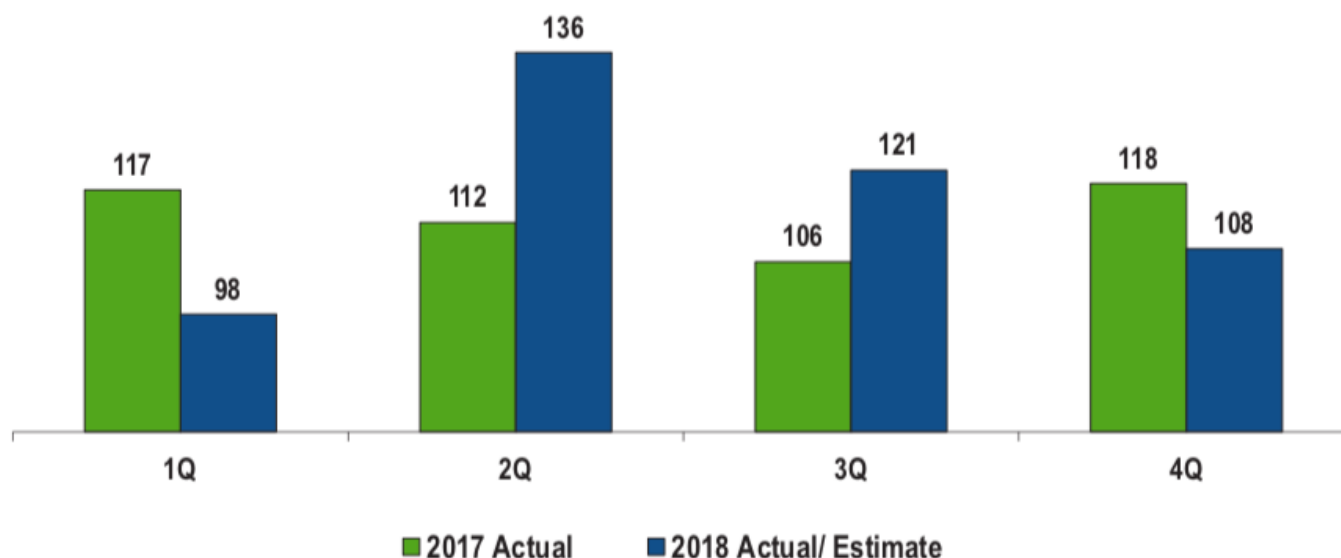
	3Q'18	vs. 2Q'18	vs. 3Q'17
Sales	\$237	↓ 4%	↓ 6%
EBITDA before items*	\$14	↓ \$6	↓ \$11
Same Currency Sales (@2Q'18 FX rate)	\$240	↓ 3%	-
Same Currency Sales (@3Q'17 FX rate)	\$238	-	↓ 5%

(Source: Domtar Quarter 3 Earnings Call Deck)

Personal Care took a hit this past quarter with sales and EBITDA underperforming than previous indices. Personal Care can improve especially after commodity prices stabilize and the Waco Personal Care facility undergoes full closure of its centre and reallocation of staff.

Exhibit 24.

Lower Maintenance Costs in Paper and Pulp



(Source: Domtar Quarter 3 Earnings Call Deck)

The Pulp and Paper segment is expected to continue having lower maintenance costs which will improve the growth of the segment drastically. The spike in second quarter maintenance costs are expected because of the compensation that Domtar had to make in order to address higher input costs for raw materials. The cost inflation for commodities and raw materials is expected to stagnate, so maintenance costs should become more manageable and decrease going into quarter 4.

John D. Williams

Domtar President, CEO, and Director

“We're also undertaking pricing initiatives and ways to maximize top-line contribution through our commercial means wherever conditions allow. The sum of these actions will reduce our cost base and strengthen our long- term competitive position. Challenging market conditions in Personal Care aside, we have strong momentum to finish 2018 on a high note and the confidence that our Paper and Pulp businesses will enter 2019 with the best momentum in many years”

Validity: Agreed. The challenges in personal care have made this quarter especially challenging. THE momentum heading into 2019 is clearly visible with the Paper and Pulp segment at the forefront. The initiatives to reach target EBITDA are well-founded and are reasonable. Domtar is in a strong position.

Daniel Buron

Domtar CFO and SVP

“As you can see, the fourth quarter will be a less active quarter with regards to major planned maintenance shut down in our Pulp and Paper business. We expect to spend approximately \$13 million less than what we spent in the third quarter, and this decrease should largely impact our Pulp business”

Validity: Agreed. The completion of the Waco, Texas closure and allocation of work in addition to lower maintenance costs will contribute to a less active quarter. The Pulp business should prosper with reduced spending and higher prices imposed.

Section 6: Valuation

Current Pricing

Domtar Corporation, when analyzing ratios and its balance sheet shows very strong fundamentals. By December 05, 2018, the stock traded at USD 44.19, not far from Book value (BV/share = USD 40.59). This valuation is reserved for dying companies, and Domtar is not one of them, in fact it is alive and kicking. With facilities in the main markets they sell, they have their market covered and they are diversifying their portfolio and strengthening high margin products. The company is vertically integrated, which allows it to eliminate multiple marginalization and be subject to less volatility in supplier compliance. As we will see in the valuation, there is value that is not being enjoyed by investors.

Valuation

Overview for Base Case:

Using Discounted Cash Flows (DCF), we arrived at a target price of USD 52.81 for a 12-month investment horizon, which signals an upside potential of 20% from its last traded price of USD 44.19 on December 04, 2018. To achieve this weighted share price, we developed three scenarios, giving each corresponding probabilities. We then made a sum of the weighted share prices. Our target price obeys the following assumptions:

Revenue Assumptions:

We expect revenues to grow as the company's investments in modifying mills to produce more packaging products and acquisition of personal care business realize their synergies. On the base case scenario, as the industry is mature, we expect growth of 2% and on the upside 4%, not too far from inflation.

Expenses Assumption:

As has been the trend, expenses are keeping up the pace with revenue growth. As reported by the company in the last earnings report, cost of goods should go up as inputs for paper manufacturing become more costly. On the SG&A side, the climb is expected at 7% based on management's expectation of shipping supplies, delivery charges and sales commissions to continue climbing.

Tax Rate Assumptions:

We assumed a tax rate of 22% from 2018 onward taking into consideration the tax reduction implemented by the current administration.

WACC Assumptions:

Our WACC of 7.37%, estimated with a 5-year beta calculation comparing the percent change of Domtar Stock to the S&P 500.

Exhibit 25.

WACC	
Beta	0.26
Risk free rate	3.05%
Market risk	24.59%
Cost of Equity	8.73%
Cost of Debt	5.98%
Tax rate	26%
D/V	31.35%
E/V	68.65%
WACC	7.37%

Changes in NWC & CAPEX:

We assumed yearly change in capital expenditure to be -2%, considering the historical trend of Domtar and around 6% yearly increase in net working capital, also based on historical trends and expectations for the evolution of the business.

Exhibit 26.

Base Case Scenario Valuation:

Key Financials											
For the Fiscal Period Ending		12 months	12 months	12 months	12 months	12 months	12 months	12 months	12 months	12 months	
		Dec-31-2014A	Dec-31-2015A	Dec-31-2016A	Dec-31-2017A	Dec-31-2018E	Dec-31-2019E	Dec-31-2020E	Dec-31-2021E	Dec-31-2022E	
Currency		USD	USD	USD	USD	USD	USD	USD	USD	USD	
Total Revenue		5,563.0	5,264.0	5,098.0	5,157.0	5,260.1	5,365.3	5,472.6	5,582.1	5,693.7	
<i>Growth Over Prior Year</i>		3.2%	(5.4%)	(3.2%)	1.2%	2.0%	2.0%	2.0%	2.0%	2.0%	
Cost Of Goods Sold		4,396.0	4,147.0	4,035.0	4,131.0	4,226.0	4,323.2	4,422.6	4,524.4	4,628.4	
<i>Growth Over Prior Year</i>		0.8%	(5.7%)	(2.7%)	2.4%	2.3%	2.3%	2.3%	2.3%	2.3%	
Gross Profit		1,167.0	1,117.0	1,063.0	1,026.0	1,034.1	1,042.1	1,050.0	1,057.7	1,065.3	
<i>Margin %</i>		21.0%	21.2%	20.9%	19.9%	19.7%	19.4%	19.2%	18.9%	18.7%	
Selling General & Admin Exp.		419.0	398.0	430.0	459.0	491.1	525.5	562.3	601.7	643.8	
<i>Growth Over Prior Year</i>			(0.1)	0.1	0.1	0.1	0.1	0.1	0.1	0.1	
Depreciation & Amort.		384.0	359.0	348.0	321.0	305.0	289.7	275.2	261.5	248.4	
<i>Growth Over Prior Year</i>			(0.1)	(0.0)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	
Other Operating Expense/(Income)		(17.0)	13.0	(2.0)	0	0	0	0	0	0	
EBITDA		765.0	706.0	635.0	567.0	543.0	516.6	487.7	456.1	421.5	
<i>Margin %</i>		13.8%	13.4%	12.5%	11.0%	10.3%	9.6%	8.9%	8.2%	7.4%	
EBIT		381.0	347.0	287.0	246.0	238.0	226.9	212.5	194.6	173.2	
<i>Margin %</i>		6.8%	6.6%	5.6%	4.8%	4.5%	4.2%	3.9%	3.5%	3.0%	
Tax Adjusted EBIT		238.1	216.9	179.4	153.8	185.7	177.0	165.7	151.8	135.1	
<i>Plus</i>											
Depreciation & Amortization		384.00	359.00	348.00	321.00	304.95	289.70	275.22	261.46	248.38	
Capital Expenditure		(236.00)	(289.00)	(347.00)	(182.00)	(178.36)	(174.79)	(171.30)	(167.87)	(164.51)	
<i>Growth Over Prior Year</i>			0.2	0.2	(0.5)						
Stock based compensation		9.00	10.00	16.00	20.00	24.00	28.00	32.00	36.00	40.00	
<i>Less</i>											
Change in Net working capital		(17.00)	68.00	(84.00)	(13.00)	(13.78)	(14.61)	(15.48)	(16.41)	(17.40)	
Free Cash Flow		378.13	365.1	112.58	299.27	322.49	305.3	286.18	264.98	241.54	
Valuation											
Discounted FCF		\$1,164.89									
Terminal Value		\$4,569.13									
Discounted TV		\$3,201.30									
Enterprise Value		\$4,366.19									
Net Debt		\$848.00									
Shares Outstanding		62,901,876									
Price with current shares outstanding		55.93137567									
Premium over current price		28%									

(Source: Self-generated)

Exhibit 27.

Optimistic Case Valuation

Key Financials									
For the Fiscal Period Ending	12 months Dec-31-2014A	12 months Dec-31-2015A	12 months Dec-31-2016A	12 months Dec-31-2017A	12 months Dec-31-2018E	12 months Dec-31-2019E	12 months Dec-31-2020E	12 months Dec-31-2021E	12 months Dec-31-2022E
Currency	USD	USD	USD	USD	USD	USD	USD	USD	USD
Total Revenue	5,563.0	5,264.0	5,098.0	5,157.0	5,363.3	5,577.8	5,800.9	6,033.0	6,274.3
<i>Growth Over Prior Year</i>	3.2%	(5.4%)	(3.2%)	1.2%	4.0%	4.0%	4.0%	4.0%	4.0%
Cost Of Goods Sold	4,396.0	4,147.0	4,035.0	4,131.0	4,296.2	4,468.1	4,646.8	4,832.7	5,026.0
<i>Growth Over Prior Year</i>	0.8%	(5.7%)	(2.7%)	2.4%	4.0%	4.0%	4.0%	4.0%	4.0%
Gross Profit	1,167.0	1,117.0	1,063.0	1,026.0	1,067.0	1,109.7	1,154.1	1,200.3	1,248.3
<i>Margin %</i>	21.0%	21.2%	20.9%	19.9%	19.9%	19.9%	19.9%	19.9%	19.9%
Selling General & Admin Exp.	419.0	398.0	430.0	459.0	495.7	535.4	578.2	624.5	674.4
<i>Growth Over Prior Year</i>		(0.1)	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Depreciation & Amort.	384.0	359.0	348.0	321.0	295.3	271.7	250.0	230.0	211.6
<i>Growth Over Prior Year</i>		(0.1)	(0.0)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Other Operating Expense/(Income)	(17.0)	13.0	(2.0)	0	0	0	0	0	0
EBITDA	765.0	706.0	635.0	567.0	571.3	574.3	575.9	575.8	573.9
<i>Margin %</i>	13.8%	13.4%	12.5%	11.0%	10.7%	10.3%	9.9%	9.5%	9.1%
EBIT	381.0	347.0	287.0	246.0	276.0	302.6	325.9	345.8	362.3
<i>Margin %</i>	6.8%	6.6%	5.6%	4.8%	5.1%	5.4%	5.6%	5.7%	5.8%
Tax Adjusted EBIT	238.1	216.9	179.4	153.8	215.3	236.1	254.2	269.8	282.6
<i>Plus</i>									
Depreciation & Amortization	384.00	359.00	348.00	321.00	295.32	271.69	249.96	229.96	211.57
Capital Expenditure	(236.00)	(289.00)	(347.00)	(182.00)	(180.18)	(178.38)	(176.59)	(174.83)	(173.08)
<i>Growth Over Prior Year</i>		0.2	0.2	(0.5)					
Stock based compensation	9.00	10.00	16.00	20.00	24.00	28.00	32.00	36.00	40.00
<i>Less</i>									
Change in Net working capital	(17.00)	68.00	(84.00)	(13.00)	(14.17)	(15.45)	(16.84)	(18.35)	(20.00)
Free Cash Flow	378.13	365.1	112.58	299.27	340.25	341.94	342.77	342.54	341.08

Valuation

Discounted FCF	\$1,387.01
Terminal Value	\$6,458.13
Discounted TV	\$4,524.80
Enterprise Value	\$5,911.82
Net Debt	\$848.00
Shares Outstanding	62,901,876
Price with current shares outstanding	80.5034019
Premium over current price	85%

(Source: Self-generated)

Exhibit 28.

Pessimistic Case Valuation

Key Financials										
For the Fiscal Period Ending	12 months Dec-31-2014A	12 months Dec-31-2015A	12 months Dec-31-2016A	12 months Dec-31-2017A	12 months Dec-31-2018E	1	2	3	4	5
Currency	USD	USD	USD	USD	USD	USD	USD	USD	USD	USD
Total Revenue	5,563.0	5,264.0	5,098.0	5,157.0	5,208.6	5,260.7	5,313.3	5,366.4	5,420.1	
<i>Growth Over Prior Year</i>	3.2%	(5.4%)	(3.2%)	1.2%	1.0%	1.0%	1.0%	1.0%	1.0%	1.0%
Cost Of Goods Sold	4,396.0	4,147.0	4,035.0	4,131.0	4,213.6	4,297.9	4,383.9	4,471.5	4,561.0	
<i>Growth Over Prior Year</i>	0.8%	(5.7%)	(2.7%)	2.4%	2.0%	2.0%	2.0%	2.0%	2.0%	2.0%
Gross Profit	1,167.0	1,117.0	1,063.0	1,026.0	995.0	962.8	929.4	894.9	859.1	
<i>Margin %</i>	21.0%	21.2%	20.9%	19.9%	19.1%	18.3%	17.5%	16.7%	15.9%	
Selling General & Admin Exp.	419.0	398.0	430.0	459.0	482.0	506.0	531.3	557.9	585.8	
<i>Growth Over Prior Year</i>	(0.1)	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Depreciation & Amort.	384.0	359.0	348.0	321.0	308.2	295.8	284.0	272.6	261.7	
<i>Growth Over Prior Year</i>	(0.1)	(0.0)	(0.0)	(0.1)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)	(0.0)
Other Operating Expense/(Income)	(17.0)	13.0	(2.0)	0	0	0	0	0	0	0
EBITDA	765.0	706.0	635.0	567.0	513.0	456.7	398.1	337.0	273.3	
<i>Margin %</i>	13.8%	13.4%	12.5%	11.0%	9.8%	8.7%	7.5%	6.3%	5.0%	
EBIT	381.0	347.0	287.0	246.0	204.8	160.9	114.1	64.3	11.6	
<i>Margin %</i>	6.8%	6.6%	5.6%	4.8%	3.9%	3.1%	2.1%	1.2%	0.2%	
Tax Adjusted EBIT	238.1	216.9	179.4	153.8	159.8	125.5	89.0	50.2	9.0	
<i>Plus</i>										
Depreciation & Amortization	384.00	359.00	348.00	321.00	308.16	295.83	284.00	272.64	261.73	
Capital Expenditure	(236.00)	(289.00)	(347.00)	(182.00)	(182.00)	(182.00)	(182.00)	(182.00)	(182.00)	
<i>Growth Over Prior Year</i>	0.2	0.2	(0.5)							
Stock based compensation	9.00	10.00	16.00	20.00	24.00	28.00	32.00	36.00	40.00	
<i>Less</i>										
Change in Net working capital	(17.00)	68.00	(84.00)	(13.00)	(13.65)	(14.33)	(15.05)	(15.80)	(16.59)	
Free Cash Flow	378.13	365.1	112.58	299.27	296.29	252.99	207.92	161.0	112.15	

Valuation

Discounted FCF	\$863.02
Terminal Value	\$2,113.61
Discounted TV	\$1,480.87
Enterprise Value	\$2,343.89
Net Debt	\$848.00
Shares Outstanding	62,901,876
Price with current shares outstanding	23.78
Premium over current price	-46%

(Source: Self-generated)

Exhibit 29.

Sensitivity Analysis

Sensitivity Analysis				
	Current	1	2	3
Scenario	Base Case	Base Case	Optimistic Case	Pesimistic Case
Enterprise Value	\$4,366.19	\$ 4,366.19	\$ 5,911.82	\$ 2,343.89
Shares Outstanding	62,901,876	62,901,876	62,901,876	62,901,876
Price with current shares outstanding	\$ 55.93	\$ 55.93	\$ 80.50	\$ 23.78
Probability	55%	55%	20%	25%
Premium	27%	27%	82%	-46%

Weighted Share price

\$ 52.81

Weighted Premium

20%

(Source: Self-generated)

Section 7: Risk Analysis

Risk Factors to Consider:

Even though we have great faith in the company, we are not unaware of potential risks in the business. Between the most relevant, the company could encounter difficulties restructuring operations or closing or disposing of facilities, holding unproductive or unprofitable assets. Also, Domtar depends on third parties for transportation services, which leaves it vulnerable to surges in charges for this service.

On supply side, the company's Pulp and Paper business may have difficulty obtaining wood fiber at favorable prices, or at all. The resource is finite and irresponsible use or depletion of forests could impact the industry. From a customer's perspective, Domtar relies heavily on a small number of significant customers, including one customer that represented approximately 10% of the Company's sales in 2017. This gives high bargaining power to those customers. A significant change in customer relationships or in customer demand for products could materially adversely affect the Company's business.

Finally, the pulp and paper industry is highly cyclical. Fluctuations in the prices of and the demand for the Company's pulp and paper products could result in lower sales volumes and smaller profit margins.

Section 8: Conclusion

Conclusions:

- Favourable performance in Paper and Pulp have offset the difficult quarter for Personal Care. Sales growth is expected to continue with the announcement of higher prices.
- Personal Care expects to lower SG&A and costs as well as increase manufacturing efficiency and productivity. Personal Care will also benefit because of higher volume and improvements on margins.
- Lower maintenance costs should help realize growth quicker heading into the fourth quarter as raw material and commodity prices remain constant.
- Transition from the Waco, Texas Personal Care Facility has completed its closure and can now pursue its reallocation of capital to grow more profitable side of the business.
- The company shows a strong balance sheet, stable capital structure with low leverage
- The valuation multiples in contrast with its fundamentals suggest that the company is undervalued: Low P/E, Low Price/BV.
- The stable capital structure allows for Domtar to take on more debt and finance some additional investments that way, reducing their cost of capital.
- They can undertake higher leverage because of their strong free cash flows
- Provided substantial amounts of money back to shareholders over time and expect to continue doing so.

Section 9: Appendix

Appendix 1 Domtar Balance Sheet

Balance Sheet

	DEC '17 365 DAYS	DEC '16 366 DAYS	DEC '15 365 DAYS	DEC '14 365 DAYS	DEC '13 365 DAYS	DEC '12 366 DAYS	DEC '11 365 DAYS	DEC '10 365 DAYS	DEC '09 365 DAYS	DEC '08 367 DAYS
Cash & Short-Term Investments	139	125	126	174	655	661	444	530	324	16
Growth (%)	11.20	-0.79	-27.59	-73.44	-0.91	48.87	-16.23	63.58	1,925.00	-77.46
Cash & ST Investments / Total Assets (%)	2.67	2.20	2.22	2.81	10.43	10.80	7.57	8.80	4.97	0.26
Total Assets	5,212	5,680	5,663	6,185	6,278	6,123	5,869	6,026	6,519	6,104
Growth (%)	-8.24	0.30	-8.44	-1.48	2.53	4.33	-2.61	-7.56	6.80	-21.22
Asset Turnover (x)	0.95	0.90	0.89	0.89	0.87	0.91	0.94	0.93	0.87	0.92
Return on Assets (%)	-4.74	2.26	2.40	6.92	1.47	2.87	6.14	9.65	4.91	-8.27
Total Debt	1,130	1,293	1,260	1,360	1,529	1,225	848	850	1,755	2,171
Growth (%)	-12.61	2.62	-7.35	-11.05	24.82	44.46	-0.24	-51.57	-19.16	-5.32
Total Debt / Total Assets (%)	21.68	22.76	22.25	21.99	24.35	20.01	14.45	14.11	26.92	35.57
Total Debt / Total Equity (%)	45.51	48.32	47.51	47.06	54.96	42.58	28.53	26.55	65.93	101.31
Net Debt	991	1,168	1,134	1,186	874	564	404	320	1,431	2,155
Growth (%)	-15.15	3.00	-4.38	35.70	54.96	39.60	26.25	-77.64	-33.60	-3.02
Net Debt / Total Equity (%)	39.91	43.65	42.76	41.04	31.42	19.60	13.59	9.99	53.76	100.56
Total Liabilities	2,729	3,004	3,011	3,295	3,496	3,246	2,897	2,824	3,857	3,961
Growth (%)	-9.15	-0.23	-8.62	-5.75	7.70	12.05	2.58	-26.78	-2.63	-12.96
Total Shareholders' Equity	2,483	2,676	2,652	2,890	2,782	2,877	2,972	3,202	2,662	2,143
Total Shareholders' Equity / Total Assets (%)	47.64	47.11	46.83	46.73	44.31	46.99	50.64	53.14	40.83	35.11
Return on Equity (%)	-10.00	4.80	5.12	15.20	3.22	5.88	11.82	20.63	12.90	-21.46

All figures in millions of U.S. Dollar.

(Source: FactSet)

Appendix 2 Domtar Income Statement

Income Statement

	DEC '17 365 DAYS	DEC '16 366 DAYS	DEC '15 365 DAYS	DEC '14 365 DAYS	DEC '13 365 DAYS	DEC '12 366 DAYS	DEC '11 365 DAYS	DEC '10 365 DAYS	DEC '09 365 DAYS	DEC '08 367 DAYS
Sales	5,157	5,098	5,264	5,563	5,391	5,482	5,612	5,850	5,465	6,394
Growth (%)	1.16	-3.15	-5.37	3.19	-1.66	-2.32	-4.07	7.04	-14.53	7.52
Gross Income	719	691	714	771	662	782	1,064	1,036	606	731
Growth (%)	4.05	-3.22	-7.39	16.47	-15.35	-26.50	2.70	70.96	-17.10	1.67
Gross Margin (%)	13.94	13.55	13.56	13.86	12.28	14.26	18.96	17.71	11.09	11.43
EBIT	259	262	307	354	253	422	717	692	259	324
Growth (%)	-1.15	-14.66	-13.28	39.92	-40.05	-41.14	3.61	167.18	-20.06	4.18
EBIT Margin (%)	5.02	5.14	5.83	6.36	4.69	7.70	12.78	11.83	4.74	5.07
EBITDA	580	610	666	738	629	807	1,093	1,087	664	787
Growth (%)	-4.92	-8.41	-9.76	17.33	-22.06	-26.17	0.55	63.70	-15.63	0.64
EBITDA Margin (%)	11.25	11.97	12.65	13.27	11.67	14.72	19.48	18.58	12.15	12.31
Net Income	-258	128	142	431	91	172	365	605	310	-573
Growth (%)	-301.56	-9.86	-67.05	373.63	-47.09	-52.88	-39.67	95.16	-	-918.57
Net Margin (%)	-5.00	2.51	2.70	7.75	1.69	3.14	6.50	10.34	5.67	-8.96

All figures in millions of U.S. Dollar.

(Source: FactSet)

Section 10: Important Disclaimer

Important Disclaimer

Please read this document before reading this report.

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