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International Paper Co. (IP)

Baird Global Industrial Conference

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CORPORATE PARTICIPANTS

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

OTHER PARTICIPANTS

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

MANAGEMENT DISCUSSION SECTION

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Good morning, everybody. Thanks for joining. My name is Ghansham Panjabi, I'm the Packaging and Materials Analyst here at Baird on the Equity Research side. Welcome again to our 56 Conference. This is my 18th...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

Wow.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

...just so you know, Andy. So with us next, we have International Paper. And from International Paper we have Andy Silvernail. Andy, this is your third conference together at International Paper with us.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

No it is my – I want to say it's my – I came here the first time in 1994, believe it or not.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

That's amazing.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

Yeah, as an analyst.

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Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Well we appreciate your loyalty. So Andy has been at International Paper as CEO since May of 2024.

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

Yeah.

Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Right? Lot's happened in the industry since then. We also have Lance in the audience, the CFO and Mandi as well. So thanks again for joining. This is meant to be interactive. This is an uncovered company. I'm going to turn it over to Andy to give us a high level overview of the company. We'll go from there.

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

Yeah. Thank – first of all, thank you for having me. It's always good to be here. This is, in my opinion, the premier conference, one or one of two that really does a tremendous job around Industrial. So thank you. Appreciate it.

Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Absolutely.

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

So, look, the last 2.5 years have been a heck of a journey, right. With the fundamental turnaround of International Paper, the insanity of the external world in terms of tariffs and wars and inflation, and now the separation of IP from the DS Smith, where DS Smith spinning out here or selling in, at some point in the near future. And that's a really important milestone. As I sit here today when I joined in in May of 2024, right. The level of the transformation required on International Paper was monumental.

And with this separation of a company, the really big things are done, right. The really big rocks that had to be moved, that had to be changed. The fundamental things that had been in the way of international paper succeeding. We will have changed the vast majority of those. And so then you move from there to, what do you become, where you International becomes the leader in sustainable packaging in North America by quite a bit. And our view is that it's a marketplace that it's a good market, it's a good business, structurally it's a good business, that structurally getting better. It's structurally getting better over time.

We've made the decisions around assets. We've made the decisions around business segments. We've made the decisions around structure and overhead, the things that should have been done for a very, very long time. And importantly, we've made the decisions around investment. So we've doubled the level of investment going back into the North American business over the last couple of years and on fewer assets, right. So we've doubled the amount of CapEx going back into the business to rebuild the productive capabilities of the business. And it's on fewer assets. So as you think about it as investment per unit of asset, it's changed radically over the last few years.

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Why does that matter? It matters because you started to see it in the third quarter. You started to see the inflection of profitability in terms of EBITDA margin spiking in the third quarter. We expect that to continue as we go into the fourth quarter. We've radically restructured the excess capacity that we held, right. So we've taken out about 20% of the total capacity of the business to be rightsized for the marketplace. And that's something that the company had hesitated to do over time.

And importantly, right, we have changed the commercial structure and we have brought in some real, some excellent fresh blood, including Lance from the outside, to infuse an industry that, frankly, had not seen a lot of people from the outside. It's an industry that had been very insular. And in that, I think comes pretty poor decision making. And so we've radically changed that and we'll continue to change that. And so I'm excited for the future. I'm excited for what International Paper is becoming, I'm excited for the structure of the business within the structure of the industry and the promise of the future.

That being said, lot of things, lots of headwinds and lots of stormy things that are out there in the world that you have to deal with. And one of the things that I love to do is I love to confront reality. Just tackle it, right. Tackle what's in front of you. And go after it. And position your business to thrive within whatever world that we're in. And I think the world that we're in is going to continue to be tough, right. I don't see 2027, I don't see a miracle in 2027 in terms of economic change.

We were talking a little bit in the hallway that maybe we're seeing a few things here and there at our customer base that are promising. But I think we should expect 2027 to be a slog. I really do. And I think it's going to be a slog in terms of demand. And I think we have a lot of headwind from inflation that is still rolling through the system. And our job is to overcome that. And I think we're well positioned to do that as we go into 2027.

So with that, I'll turn it to you.

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QUESTION AND ANSWER SECTION

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah. So lots of new energy at the company including...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah, exactly.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...Lance, same analysts covering it.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

That's all right. That's good.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

I couldn't resist. In terms of, your journey of the company. So obviously the macro is what it is, right?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...when it's widely telegraphed and you're exposed to that to a big extent. But the company has also been through a lot.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

So when you joined DS Smith was announced roughly around that time.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

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Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

And now there's...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

It was announcement a little bit before I joined. Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Exactly. And so now we're on the flip side of that where you're...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...looking at options for that.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

So take us through the thought process as it relates to the strategy behind that?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah. So, when I joined the company and many of you have heard me say this many times, I was right there as that decision was being concluded. And so one of the things that the conversations that I had pretty forthright was I have the right to – I reserve the right to change anything, right. And so I spent about 16 weeks in Europe last year, hands – on the ground. My wife and I moved, took her little dog and we moved to Europe. And we moved to Europe, we spent a bunch of time in London, and then traveled throughout Europe, then a bunch of time in France and travel throughout Europe.

And what became apparent as I dug in deeper and deeper and deeper, is that while the business is a good business or structurally DS Smith is a business that can succeed. If you think about two vectors of why companies are together, right? They're usually together around customer commonality and cost commonality, right? And the more of the two of them, the more arguments you have for what I'll call real synergy.

And on the surface, both of those arguments were true, right? On the surface, both of those arguments were true. You could argue that lots of global customers and you could argue that there was a cost base that could be shared globally. And when you got into the fundamentals of how it really worked, that was not true. And so I

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remember sitting this time kind of last year a little bit maybe a month ago from this time last year, with my board going, we need to separate this.

And of course, you can imagine what the whole world said was, really? And my experience has been that once you've concluded something, and you have real certainty around that and we went and did a lot of deeper work around those hypothesis, I started to see early on. We did a lot of deep work, but once you've made that conclusion, you should move. Time is not your friend. Time is no longer your friend once you've made those conclusions. And so I would rather reposition both companies to win in their independent markets with unique balance sheet, unique investment capabilities, right?

The structures of the markets are different. How competition happens is different, how customers buy is different, let them go thrive. Let capital allocation move to where it should move, the human resource allocation move to where it should move, and let the businesses thrive on their own. And so we made the decision in January of this year. And we've been moving fast. Lance has been leading the separation efforts and he's done a phenomenal job around that. And we should conclude that relatively soon.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Okay. What would you say – so there's no – just from the sidelines following your or from the dynamics in the industry, there's no global procurement contract?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

Kind of.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

And here's what I say. There's what I would call theoretical interest in that. But when you get into the mechanics of how this business really works, even inside the US to some degree, like we say we have a national account or we say we have an account. The primary relationship is actually a plant in a plant, right. We're servicing one of our customer's main plants, some of our big customers who you know really well, they're going to have 10, 20, 30, 40, 50 plants that we're going to service with 10, 20, 30, 40, 50 plants. That's the primary relationship.

And that primary relationship is actually how things get built up into contracts. Contracts don't come like my office and I dream it up and I'm like, oh, let's have a national contract or a global contract. That's not how it works. The plant in Tupelo, they have needs. They have a certain type of box with certain construction characteristics that they need, that will roll up across our customers 50 other plants. And that's what becomes a national contract, that's just nationally. Now, there you actually have integration across that customer. Like they will make a decision nationally. Once you get the global stuff now.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

Got you.

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

And so it actually when you dug into, wait a second, this is actually bad for us, right? Because there's this theoretical opportunity of more business. Right? Okay, I've got $100 million of business in the US and I got $20 million in Europe and should be just as much, the two people making the buying decisions, they don't probably even know each other and the other company. And so I think like many businesses, you fall into a fantasy of synergy versus how it really works at the fundamental level.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

I get it. I cover...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

...companies like that...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.

Q

...other ones as well. As you think about the structural differences in the market, Europe versus the US, what would you highlight there?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

Yeah, a few things. And they're big things, right. So let's start with kind of customer concentration and how you think about that. Not customer concentration, but rather customer decision making, who the customer is? In Europe, it's a lot more fast moving consumer goods, a lot more. So think of a lot more lightweight boxes, much, much faster innovation changeover, right? Because it's actually branding, right. It's fundamental branding. And we have that in the US, too. But in Europe if it's 70/30, in the US it's 30/70, it's really different. The US tends to have a much more logistics heavy structural dynamic to it, right. Because we're moving things over much longer distances, typically, right. Because of the infrastructure and the size and the territory and whatever.

Also, in Europe there's a lot more shelf ready product. In the US it's happening, but it's happening very slowly. And so those combinations of things make the buying side really different, right? Just what gets bought gets really different. US more consolidated, Europe less consolidated. US is much more virgin, right? And again, it's almost – it's interesting. It's almost the same dynamic as the consumer versus because it's the lightweight aspects of it. So much more virgin in the US, less recycled, recycled and lightweight growing. Europe, a lot more recycle and a lot more lightweight, right.

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So there really very, very different businesses. Because of the dynamic of lightweight versus heavyweight, of virgin versus recycled. How energy gets produced and consumed is also very different. In the US we make about 70% of our own energy and almost all the rest of the energy comes from natural gas, which is plentiful and it doesn't move very much. In Europe, right, because you don't have the virgin process to recycled energy, to recycle steam. You're buying energy on the markets and you're buying energy and natural gas. And we've all seen the volatility of natural gas, right. So they're really, really different markets. It doesn't mean that one is better than the other. It means they're really different in how they behave. And it means that how you think about investment criteria, how you think about capital allocation decisions, how you think about people, how you think about innovation, how you think about design. They are both made from fiber and that is where it kind of ends.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

I'll ask one more question on that, then I'll open it up to the audience. In terms of the separation, is it sort of a, to use my words, dual track?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah, that's a great way to put it.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. And what is the timeline? Because, going through a transition...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...shareholders have to endure the volatility of news flow and so on and so forth.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

When does it get cleaner?

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah. So we laid it out when we first announced it, we said 12 to 15 months. That was the timeline, that was the end of first in February, end of January last year. We have never stated anything different than that. You can read in based on what you've seen in the news and whatnot. You can read into that how you will. But certainly within that timeframe that we originally said.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. Call it, 1Q of next year of next year, plus or minus.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

At the very least.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yes. Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

At the very least.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Any questions in the audience? Okay, we'll keep going. Let's switch to North America.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

So North America, I remember when you joined, you had a different view in terms of just given your background, your skill sets with the 80/20 and you've permeating that in the organization. And I – initial conversation that, one of the questions I asked you about the time it takes to permeate...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...right? Because you have a mature company in a mature industry and it takes time to kind of get the message through and the metrics through and so on and so forth. Where we are on that?

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.

A

We've made tremendous progress. And I – when I think of 80/20, I think of it from the kind of very top level all the way down to the granular decisions that get made. What I would say is, if you think of it from portfolio, right? So, portfolio geography kind of really big buckets of decision making. Where do you want to be? Where do you not want to be? We're vastly done with that. So when as I said when the spin is done, those sorts of things will have been done. We've sold GCF, we have exited a series of small businesses, product lines in this – and little things left to do, but those are mostly done now and will be vastly done when DS Smith spins out.

Then you start to move towards levels of decision making around capacity and capital. Those are the big decisions of what we're not going to do are mostly done. They'll always be things that go on but big mill closures, obvious box plant consolidations. Those things have mostly been done, right. We've taken out huge amounts of structural cost out of those things. And very importantly, we stopped putting money into assets that really had no economic life.

Like we had some really big assets that had huge capital needs that were sucking from the system that we didn't have the courage to shut down because I call it, building a church for Easter Sunday, right. We got to have it because someday, dot, dot, dot, dot, dot. We had to believe in something around the growth of the business and/or the ability to invest and change the quality of the assets to believe in those things.

And so we made those really hard decisions. We took a huge amount of capacity out of the mill system. And all of that capacity was either negative cash, right, or below its cost of capital through a cycle. So we basically took stuff out that was just a cash suck, right? Big cash suck that required. And we took those assets – with those that investment and we have moved all of it and more over into a new mill at NORPAC, right, opening Waterloo.

We've announced the Mississippi investment. We have – I can – I don't know how many corrugators we've ordered, but one of the smartest moves we did was literally when we approved the strategy in North America in the fall of 2024, which was two years ago, we did a massive pre-buy of equipment. That's still layering into the system, which is really important, because that's what's going to happen as you move that down, move down this funnel of big decisions to what I call aggressive continuous improvement. That's where we're entering, that phase is where we're entering. So it still means there's lots of productivity to go get. There's lots of reinvestment back into the customer in terms of innovation, in terms of service levels, in terms of quality. There's lots of opportunity to still go there, but we're moving into that where you end up with a much more predictable business.

If I'm in your guy's shoes, one and frankly, for me too, one of the things that is enough to make you insane about this business is there's real volatility that is you can't ever get away from, and then there's self-induced volatility, right? The real volatility in the North American Packaging business is pretty modest. If you really think about demand over time, right, really demand over time. Like even when we've been through the last two years with craziness of inflation and tariffs and all that insanity, there's really only about a three point band at the extremes, except for like in a crisis. It's kind of a three point band in the extremes. That's a pretty stable business that we have induced lots of volatility in, poured investment into assets, so you get reliability problems, you things that break, that shouldn't break at times they shouldn't break. They get very expensive. You keep excess capacity. So you keep market volatility all the time, just endless things you own – you buy businesses that are inherently much more cyclical.

So the core – one of the things I love about the core North American business is it's actually pretty darn predictable from a volume standpoint. Now, price, I don't control, right? I control what I can do around price. But there's a market out there and the market decides what happens to that. So there will always will be some

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volatility around that. But one of the biggest mistakes that we made in the past is if you think about kind of cash flows as an upward sign curve in the marketplace or could be an upward sine curve, us and most of the industry have chased the cash flows or matched cash flows and investment.

So we always – we spent money when we had money, and therefore, we spent money at the most expensive time to spend it, right. And it was volatile and it was volatile. And so what this business really requires is a steadiness of investment and a balance sheet with it that doesn't follow the sign curve. That's really, really, really important. in this business, because it's the only way you drive reliability, it's the only way you drive productivity, it's the only way you drive service levels consistently in the business. When you don't do that, everything goes like this.

And so assets out that are very volatile and not predictable, right. And investment in assets around a pretty stable volume business where we want to invest consistently year in and year out.

Ghansham Panjabi Q
Analyst, Robert W. Baird & Co., Inc.

So you're an industry in North America anyway that has no shortage of data...

Andrew K. Silvernail A
Chairman & Chief Executive Officer, International Paper Co.

Yeah.

Ghansham Panjabi Q
Analyst, Robert W. Baird & Co., Inc.

...on data out there.

Andrew K. Silvernail A
Chairman & Chief Executive Officer, International Paper Co.

Yeah.

Ghansham Panjabi Q
Analyst, Robert W. Baird & Co., Inc.

I think the industry took out about 10% of capacity last year, in North America...

Andrew K. Silvernail A
Chairman & Chief Executive Officer, International Paper Co.

Yeah, that sounds about right. Yeah.

Ghansham Panjabi Q
Analyst, Robert W. Baird & Co., Inc.

...including what you did as well.

Andrew K. Silvernail A
Chairman & Chief Executive Officer, International Paper Co.

Yeah, yeah.

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Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

The truest test is being able to translate that into some version of at least cost related pricing, right?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Correct.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Because think about this industry, at start of the year, one more Black Swan with the Iran war.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Right.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Oil spike, significant increase in cost inflation.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

How did you handle through that?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

So there are a few things. So one, all the work we had done before that wave of inflation spike has happened because – I mean, we call it the Iran war, but it's really the building of the impact of global trade and the Iran war that is now moving its way through the system. So if you look at the pricing that's happened in the market really since I've joined the company, it's basically covered inflation. That's effectively what's happened in the marketplace. There's been almost zero that has hit the bottom line incrementally.

Our 40% increase since 2024 and EBITDA is 100% of the cost [indiscernible] (00:20:23) right. And I would actually say it's more than 100%, because actually price is a little bit – has been a little bit behind the inflation curve until about now. We're just starting to see it now. So that inflation monster is going to be there. So if I just kind of look to next year as an example, and I think about, okay, so we're going to incrementally, we're going to take out between $250 million and $350 million of incremental cost next year, right, that's what's going to come out of it and that stuff that's already done and it's already lined up.

Okay. So you've got about $1 billion of incremental price, right, that you'll see make its way through call it...

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Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Carryover.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...call it somewhere between...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...$900 million and $1.1 billion. The range is wider because depends how it gets absorbed into the market and everything else but a little bit wider range. So think of kind of $250 million to $350 million and think of $900 million to $1.1 billion of cost out and price up. Then you go to inflation. Well, normally in our world you'd look at about, call it $250-ish million of inflation, plus or minus, the kind of year in, year out to see. It's going to be more than double next year. Like if you just take the strip, it's going to be more than double. So if you kind of put all cost headwinds that we see, we see about $600 million of cost headwinds in there. So, we expect that – I do expect it to moderate over time. But the good news here on this is the cost out engine is cranking like that's moving. I don't lie, I believe the inflation headwinds will be there for some time. I don't believe we're going to see $600 million a year. I don't think that's going. Five years from now I don't think we're going to be sitting here going. Boy, you had $600 million of inflation [indiscernible] (00:22:13) could be wrong.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

I don't think so. And importantly, the price that we have gotten, even the price that we're getting today is supply side driven pricing. Right? It's inflation driven pricing that's moving everything in the marketplace. And so, any movement in demand is going to be a net really positive thing. And look the – we are very tight. We're running very tight. We will run very tight into the fourth quarter, into the – and throughout next year. And so, we're kind of looking at that reality of the tightness in the paper markets. And so with some demand, I think it's a pretty attractive scenario.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

So the bridge for next year versus this year, you have self-improvement and you just...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

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Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...kind of went through that.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

You've price cost, you went through that as well.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

What about stranded costs from the separation?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

I mean...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Is that material?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

We'll take out most of it.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Lance, the total that gets left to $30-ish million, is that right?

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

So it's pretty minimal.

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

It's pretty minimal that will show up as kind of a classics. And we'll – and even that will whittle down over time but it's things like systems that you can't – I mean we've restructured IT as most of you know we've outsourced a big chunk, the big segment of our IT. We've already done that. But then there are things kind of within systems that require work to be done before you can just take the cost out. And so you've got $30-ish million or so. Yeah, [indiscernible] (00:23:42).

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. So just to kind of step back, Andy. So if the industry had not taken out the capacity to the extent it did last year, call it 10%, right?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Would you have been able to get the pricing through as an industry this year?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

I don't – it's hard to say, right. It's hard to judge that, it's – the pricing conversation is always a dangerous conversation.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

We stay super focused on what we can control and what we do. And that's really around how we interact with our customers and the value that they see.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay. So this year, in terms of volumes, you had some issues with Ag.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah. We all did.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

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Yeah. The..

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...like I don't know how to say it, cycle or something, right?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

I won't say what I said privately. Lance is like don't say it. Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah. How did it progress, just from your point?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah it's – look it's interesting, right. So you had a few things happen that were really fast bursts and we all – we're in the news and we all joked about it and laughed about it. But believe me, it was nothing to laugh...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Material.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...about big deal. And so what you end up having is you end up having for a period of time, people stop eating less, right. They just kind of – they just stop eating bag less. That's kind of reverse now, like that's making its way through now. And so that consumer demand is coming back. But remember, it waits until the next planting season. So now you got to get to the next planting season. So you kind of end with a low. But what I would say is as you go through the fourth quarter, it appears most of that is through the marketplace. But in terms of it picking back up and getting back on what I'll call trend, it'll be in the planting season.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

The El Niño year...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

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Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...that is widely discussed.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Historically, how does that impact – how has that impacted you?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

I don't know. Mandi, do you have a point? I don't really have a point of view of that. I don't know that...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Just lots of rain.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah, it's lots of rain. But – I – look – to some degree when you're doing business with God...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...you just got to kind of deal with it.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

And...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Well said. Well said.

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...you just do it.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

The free cash flow, the guidance this year, call it two or three plus or minus on EBITDA, right?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

The free cash flow, if I have this right, $100 million to $200 million...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

...why is it so low in terms of...

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Investment?

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

We're just investing back into the business in a huge way. A little bit of – in the last quarter, a little bit of working capital catch up, right. We had a really heavy downtime in the second quarter. So we had some working capital catch up going in there. As I look to the future of free cash flow, I like that, right. It's a good dynamic even with an elevated investment like we'll keep – we're going to be in that kind of $1.250 billion to $1.4 billion CapEx range for the next couple of years. Like we'll be in and around that range. And then we'll more normalize to about 7.5% of sales as you get a...

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay.

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Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

...little further out. And so when I think about the cash flow dynamics, as we look into the out years on the North American business, this a good free cash flow business.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Okay.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Yeah.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

As it relates to, post everything you have going on the separation so on, what happens to capital allocation, how should we think about that?

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

So first things, I think we are – as long as I am CEO, we are never going to make the mistakes that we made the past 15 years.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yep.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Right. When you actually track back, if you look back and you say, where did the wheels start coming off of International Paper, you actually can track it back to about 15 years ago. And two things happened, right? So kind of think of post the Great Recession.

Ghansham Panjabi
Analyst, Robert W. Baird & Co., Inc.
Q

Yeah.

Andrew K. Silvernail
Chairman & Chief Executive Officer, International Paper Co.
A

Post Great Recession, we stopped investing aggressively back into the core business. And capital allocation started moving to things that when you track them back today, you go can't find that money, right? And it wasn't going back into our facilities. In a business like ours, it's kind of like your car. You buy a new car, you can get away with it for a little while. You could not change your oil like the first time, maybe the second time. And then it starts to catch you. And you actually saw it, you saw the separation happen about three years later where OpEx started going up. All right. CapEx was going down, but OpEx was going up.

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And then – and you actually it's a net benefit for you for a period of time and then the lines crossed. And then the net cost of the two actually turned negative compared to where they should be. That started happening in kind of the late teens and at the same time is kind of you had world synchronized growth. And so everything looked great, right? You had kind of two, three years where everything look great and then COVID happened. And when COVID happened and there was a massive demand on the system. So when we all went home and we're all ordering stuff to come to our houses, massive demand went on the system and that showed the underinvestment in IP.

And what happened was you saw it. We went from being consistently in that, kind of number one or number two in customer satisfaction. By 2022, we were dead last of the majors. We're now back to be number one. And that is all tied to the investment dearth that started in 2010-ish, 2011. So why does that all matter? It matters because you can never do that again. You have to invest in this business year in and year out. You have to – for the quality of this business, you have to do it.

And the competitive advantage is, those who have inferior assets, especially when capital costs go up and especially when asset costs go up. So to build a box plant or a mill is somewhere between 50% and 75% more expensive than it was in 2020. It's amazing. If you do replacement cost economics on our business, it's eye popping, right. So why does that matter? It means you can't let the assets die. You have to invest year in, year out. And by the way, those who don't invest and/or those who have inferior assets, the separation of quality is going to grow over time. So that's number one.

Number two, we need a dividend, right, that our investors look at and go, that is reliable, right. That's not going to move. It's going to be consistent. And what we've said is post-spin somewhere in the 40% to 50% of free cash flow. That's what we've said consistently, and we'll make that ultimate decision when the separation happens. But you can kind of do your math and you can get a sense of what that means.

The next one is around acquisitions and/or buybacks, right? So what I would say is around acquisitions. What you should expect from us is small ball. You should expect to see us buy very consistently, buy small assets in terms of converting facilities, there aren't many mills that are for sale. But if you had a high quality one like we did NORPAC, we would do that. But you're talking about $100 million to $1 billion. You're not talking about things, you could – there's a couple of assets out there you go that are multibillion, but not even five, right. That you go, I like those.

The other choices around is around buybacks, right, which and for those of you who have known me over time, I'm a big fan, right? I'm a big fan of buybacks at the right time when done well. So you put that capital allocation model and then you always have to be willing to build cash. So anyway, it's – I think capital allocation is going to be a massive piece of the story over time. And I think the discipline for those of you who have known me when I was at IDEX, that was a huge piece of our success. Over time, you should expect that same discipline.

Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Andy we're out of time. Thank you, again...

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

Thank you.

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Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

...for your loyalty.

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

Thank you very much. Thank you very much. Appreciate that.

Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Thanks everyone for joining. The next presenter will be Mueller Water Products. Thank you.

Andrew K. Silvernail

Chairman & Chief Executive Officer, International Paper Co.

Thank you.

Ghansham Panjabi

Analyst, Robert W. Baird & Co., Inc.

Yeah, thank you very much.

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