

INTERNATIONAL PAPER

# Maximizing Free Cash Flow

## Investor Day

June 9, 2009



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# Speakers

# John Faraci

***Chairman & Chief Executive Officer***



John Faraci was named chairman and chief executive officer in November 2003. He served previously in the positions of president, executive vice president and chief financial officer. John joined International Paper in 1974.

John also serves as a director of United Technologies Corp., the Grand Teton National Park Foundation and the National Park Foundation. He is a member of the Citigroup International Advisory Board, American Enterprise Institute and the Denison University Board of Trustees.

John earned a bachelor's degree in history and economics from Denison University and a master's degree in business administration from the University of Michigan.

John and his wife, Heath, have two daughters.

# Tim Nicholls

## *Senior Vice President & Chief Financial Officer*

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Tim Nicholls was named senior vice president and chief financial officer in November 2007. He served previously as vice president and chief financial officer of International Paper-Europe, president of Weldwood (formerly a wholly owned subsidiary of International Paper), director of finance and strategic planning for industrial packaging, and general manager of the international packaging business. Tim joined the company in 1999 through the acquisition of Union Camp, which he joined in 1993.

Tim earned a bachelor's degree in management from the University of South Carolina and a master's degree in business administration from the University of Georgia.

Tim and his wife, Catherine, have two sons.

# Carol Roberts

## *Senior Vice President, Industrial Packaging*



Carol Roberts was named senior vice president of Industrial Packaging in November 2005. She served previously as vice president of the container business, vice president of human resources, general manager of kraft packaging and mill manager. Carol joined International Paper in 1981.

Carol earned a bachelor's degree in mechanical engineering from Yale University.

Carol and her husband, Craig, have two daughters.

# H. Wayne Brafford

***Senior Vice President, Printing & Communications Papers***

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H. Wayne Brafford is senior vice president of Printing & Communications Papers. He served previously as senior vice president of industrial packaging. Wayne has held a number of financial, strategic planning and general management leadership positions throughout his career in printing papers, consumer and industrial packaging, wood products, forestry and diversified businesses. Wayne joined International Paper in 1975.

Wayne earned a bachelor's degree in pulp and paper science and technology from North Carolina State University and a master's degree in business administration from Tulane University.

Wayne and his wife, Scottie, have three sons.



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# Forward-Looking Statements

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These slides and statements made during this presentation contain forward-looking statements. These statements reflect management's current views and are subject to risks and uncertainties that could cause actual results to differ materially from those expressed or implied in these statements. Factors which could cause actual results to differ relate to: (i) increases in interest rates and our ability to meet our debt service obligations; (ii) industry conditions, including but not limited to changes in the cost or availability of raw materials, energy and transportation costs, competition we face, cyclicality and changes in consumer preferences, demand and pricing for its products; (iii) global economic conditions and political changes, including but not limited to the impairment of financial institutions, changes in currency exchange rates, credit availability, credit ratings issued by recognized credit rating organizations, the amount of our future pension funding obligation and pension and health care costs; (iv) unanticipated expenditures related to the cost of compliance with environmental and other governmental regulations and to actual or potential litigation; and (v) whether we experience a material disruption at one of our manufacturing facilities and risks inherent in conducting business through a joint venture. We undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events or otherwise. These and other factors that could cause or contribute to actual results differing materially from such forward looking statements are discussed in greater detail in the company's Securities and Exchange Commission filings.

# Statements Relating to Non-GAAP Financial Measures

- During the course of this presentation, certain non-U.S. GAAP financial information will be presented.

- A reconciliation of those numbers to U.S. GAAP financial measures is available on the company's website at internationalpaper.com under Investors.

# Today's Schedule

| | |
|---|---|
| 8:00 – 9:15 | Meeting |
| 9:15 – 9:30 | Break |
| 9:30 – 10:45 | Meeting |
| 10:45 – 11:45 | Panel Questions & Answers |
| 11:45 – 12:30 | Boxed Lunch |



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# Transformation Progress

John V. Faraci,
Chairman & Chief Executive Officer

# Agenda

| | |
|---|---|
| **Transformation Progress** | **John V. Faraci** |
| **Financial Update & Direction** | **Tim S. Nicholls** |
| **Corrugated Packaging** | **Carol L. Roberts** |
| **Uncoated Papers** | **H. Wayne Brafford** |
| **Strategy & Capital Allocation** | **John V. Faraci** |
| **Panel Questions & Answers** | **All** |

# IP Transformation

## *Improving IP's Strategic Position*

- **More Focused**
- **Reduced Capital Intensity**
- **Stronger Businesses**
- **More Global**
- **Lower Cost**
- **More Profitable**
- **More Sustainable Cash Flow**

# IP Transformation

## *Improving IP's Strategic Position*

| | 2005 | 2008 |
|---|---|---|
| # of Operating Businesses[1] | 12 | 4 |
| # of Employees[1] | 80,000 | 62,000 |
| Capital Employed[1] ($ Billion) | $30 | $23 |
| Overhead ($ Billion) | $3.2 | $2.8 |
| Debt[1] ($ Billion) | $14.6 | $12.1 |
| EBITDA ($ Billion) | $2.8 | $3.0 |
| Free Cash Flow ($ Billion) | $0.4 | $1.7 |

[1] 2005 represents January 1, 2005
EBITDA before special items including discontinued operations; free cash flow before dividends

# IP Transformation
## *Smaller Capital Base*

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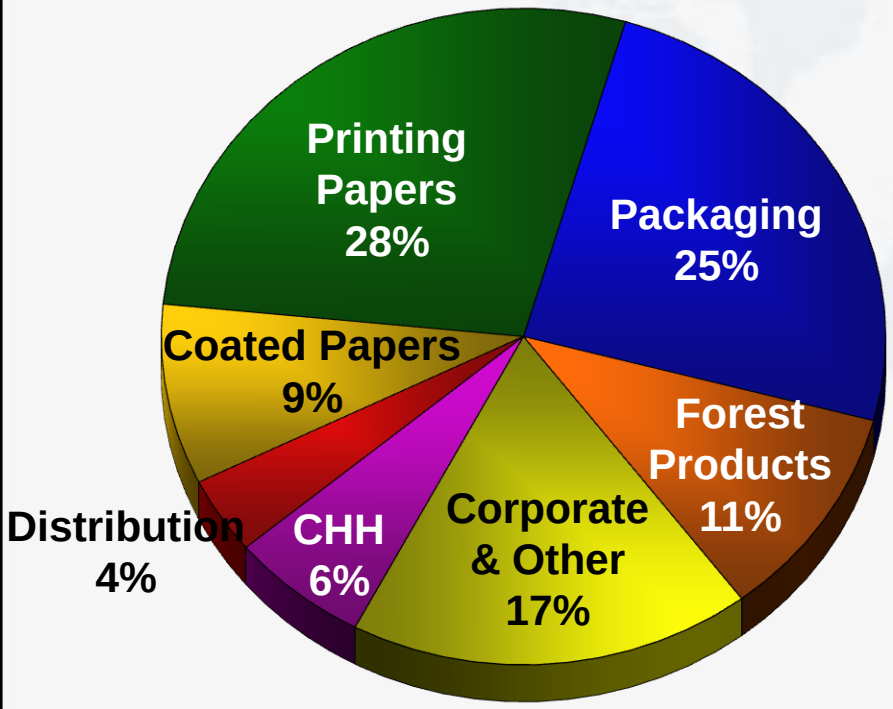
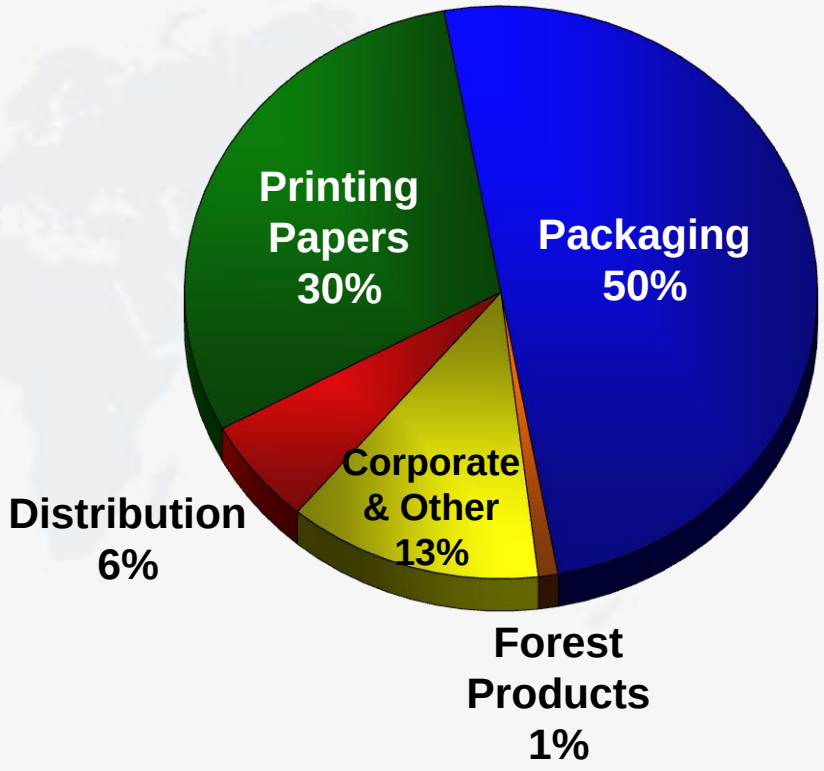
**2005**
**Capital Employed**
**$30B**




**2008**
**Capital Employed**
**$23B**




2005 capital employed represents January 1, 2005; 2008 capital employed represents December 31, 2008
Packaging includes Consumer Packaging & Industrial Packaging

# IP Transformation

## *#1 or #2 Position in Strategic Regions*

| | Supplier Position | |
|---|---|---|
| **North America** | **2005** | **2008** |
| Corrugated Packaging | 3 | 1 |
| Uncoated Papers | 1 | 2 |
| Bleached Board | 1 | 1 |
| Distribution | 1 | 1 |
| **Emerging Markets** | | |
| Latin America - Uncoated Paper | 2 | 1 |
| Russia - Paper, Pulp & Packaging | 3 | 1 |
| China – Bleached Board | - | 1 |

# IP Transformation

## *North American Printing Papers*

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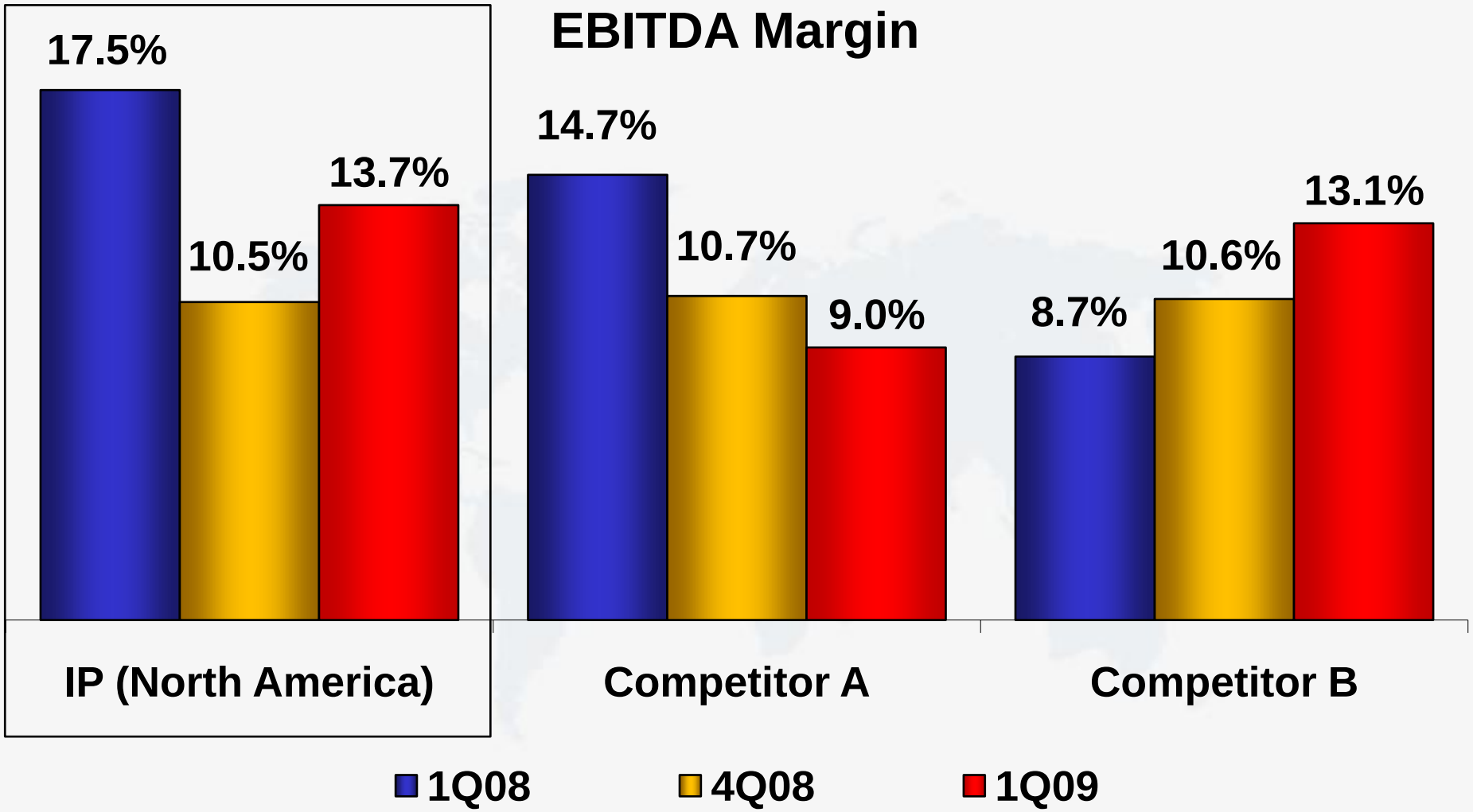


Source: Earnings calls, press releases, SEC filings, IP Analysis
EBITDA margin equals EBITDA divided by sales

# IP Transformation

## *North American Coated Paperboard*

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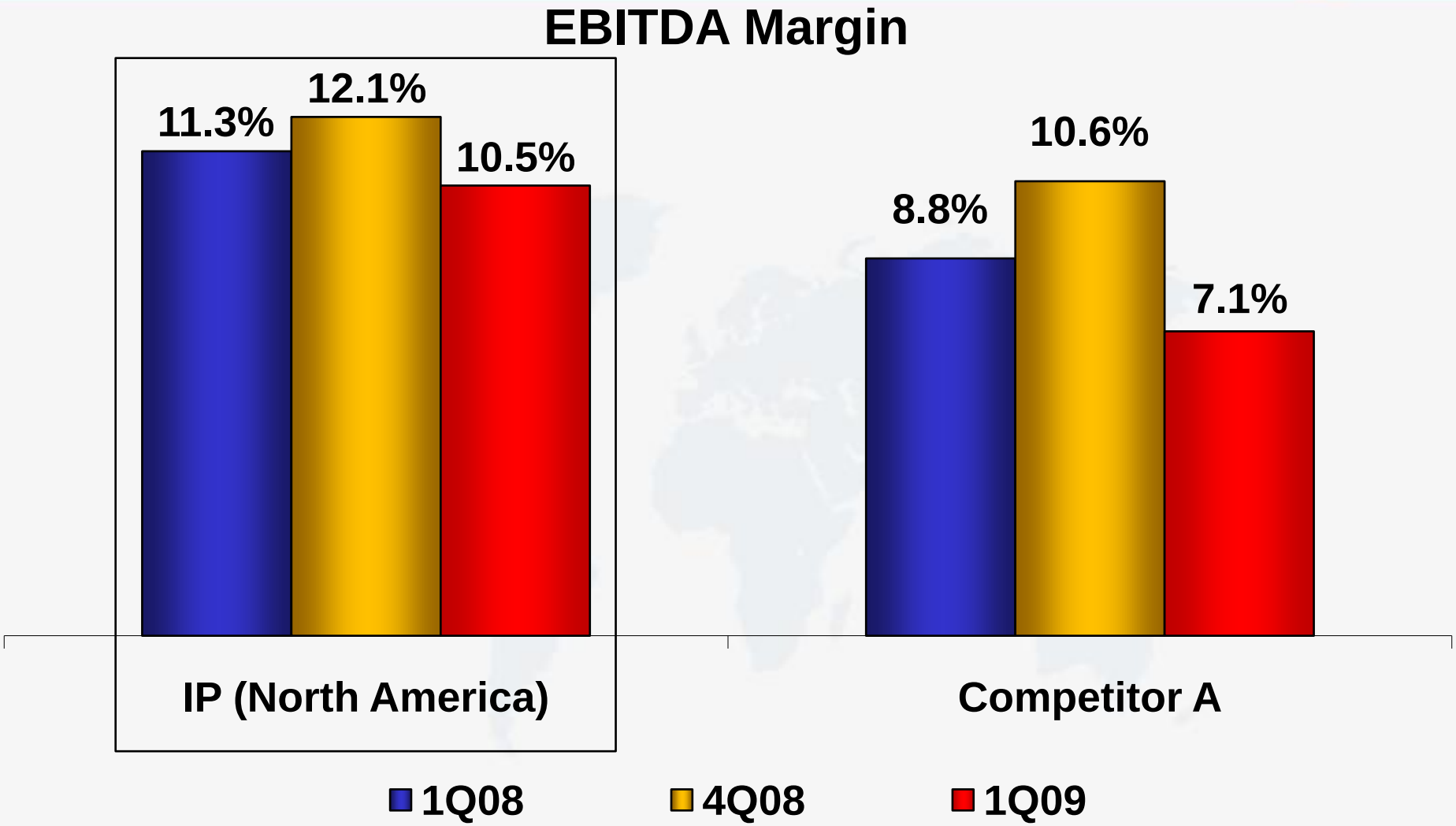


Source: Earnings calls, press releases, SEC filings, IP Analysis

EBITDA margin equals EBITDA divided by sales

# IP Transformation

## *North American Industrial Packaging*

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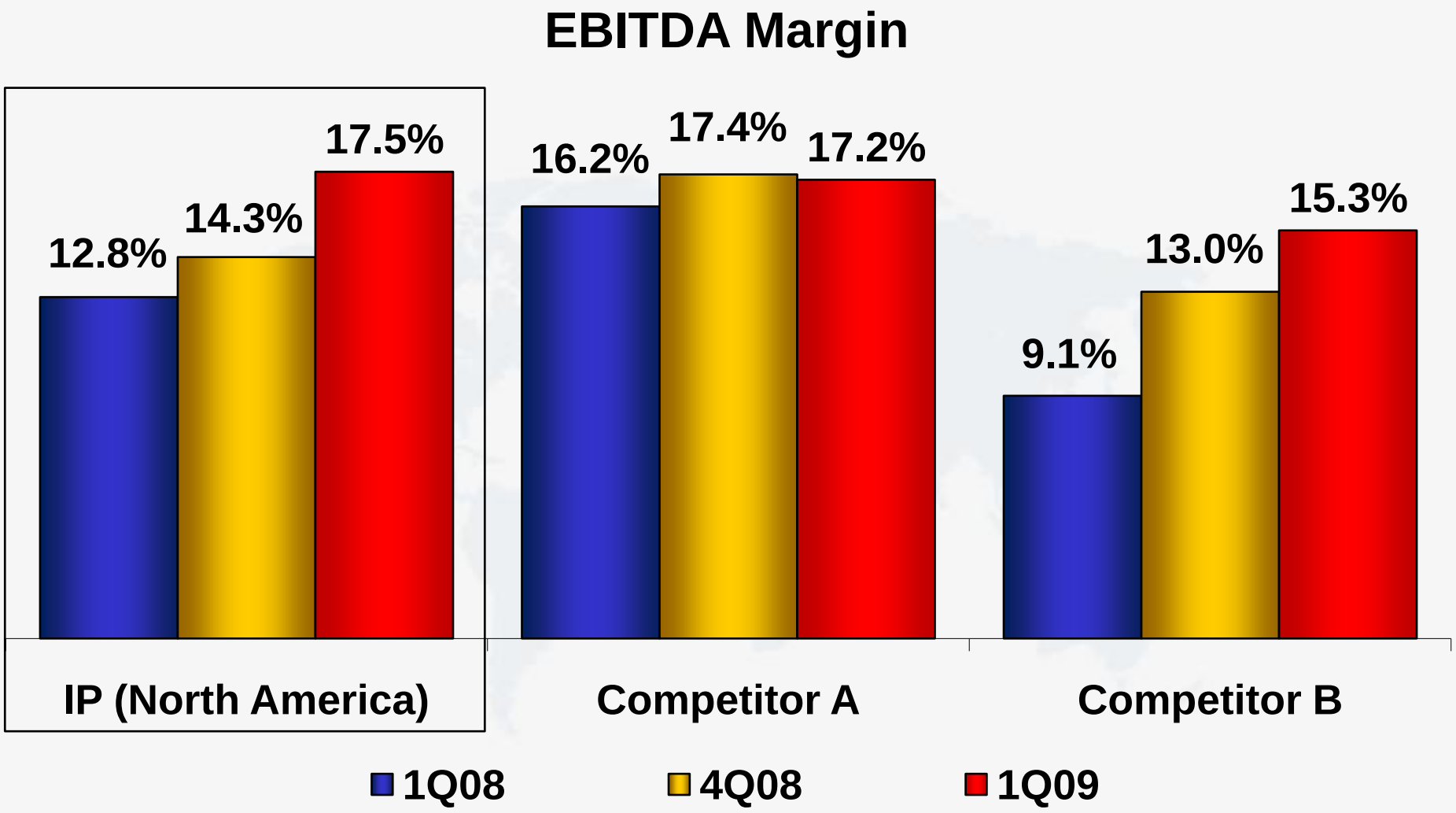


EBITDA margins for IP legacy business. Source: Earnings calls, press releases, SEC filings, IP Analysis

EBITDA margin equals EBITDA divided by sales

# IP Transformation

## *Strategic Fit of Recent Acquisitions*

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| | |
|---|---|
| **WY PKG** | • **Strengthened core business**<br>• Increased cash generation<br>• > $500 million of synergies<br>• Achieved #1 market position |
| **Ilim Joint Venture** | • **Secured low-cost capacity at low entry multiple**<br>• Strong market position with attractive fiber base<br>• Platform for future growth |
| **Brazil** | • **Strengthened existing business**<br>• Secured global low-cost capacity<br>• Achieved leading supplier position<br>• Growing market |
| **Sun Joint Venture** | • **Secured capacity at low capital cost**<br>• Established a beachhead in the largest market<br>• Low-cost, high-demand-growth market |

# IP Transformation

## *Strategic Fit of WY PKG Acquisition*

- **Strengthened Core Business**
- **Leading Supplier Position**
- **Quality Assets**
- **Strong Free Cash Flow**
- **Already Overcame Execution Risks**
- **Significant Upside Earnings Potential**

# IP Transformation

## *Synergies Driving Returns*

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| | Original | Revised |
|---|---|---|
| **Purchase Price** | **$6.0B** | **$6.0B** |
| **NPV of Tax Step Up** | **$1.4B** | **$1.3B** |
| **Net** | **$4.6B** | **$4.7B** |
| **Synergies at Full Run Rate** | **$400M** | **$500M** |
| **Estimated EBITDA Multiple** *(Net of Tax Benefit & with Synergies)* | **4.3X** | **4.6X** |

Revised EBITDA Multiple based on 1Q09 YTD annualized results

# IP Transformation

*Expanded Global Footprint in Emerging Markets*

| | |
|---|---|
| **Brazil** | **Luis Antonio & Tres Lagoas** |
| **Russia** | **Ilim Joint Venture** |
| **China** | **Sun Joint Venture** |

# IP Transformation

***Emerging Markets Contributing ~25% of IP EBITDA***

| | 2005 | 2008 Pro Forma |
|---|---|---|
| **Sales** ($ Billion) | **$1.5** | **$3.7** |
| **EBITDA** ($ Billion) | **$0.4** | **$0.8** |
| **EBITDA Margin** | **27%** | **21%** |

Results include Brazil, Svetogorsk, Kwidzyn, Sun joint venture without machine start-up costs & pulp inventory write-down, & Ilim pro forma adjusted to approximate IP's 50% ownership excluding gain on sale of KPK mill

# IP Transformation

## *Brazil - Greater Focus, More Profitable*

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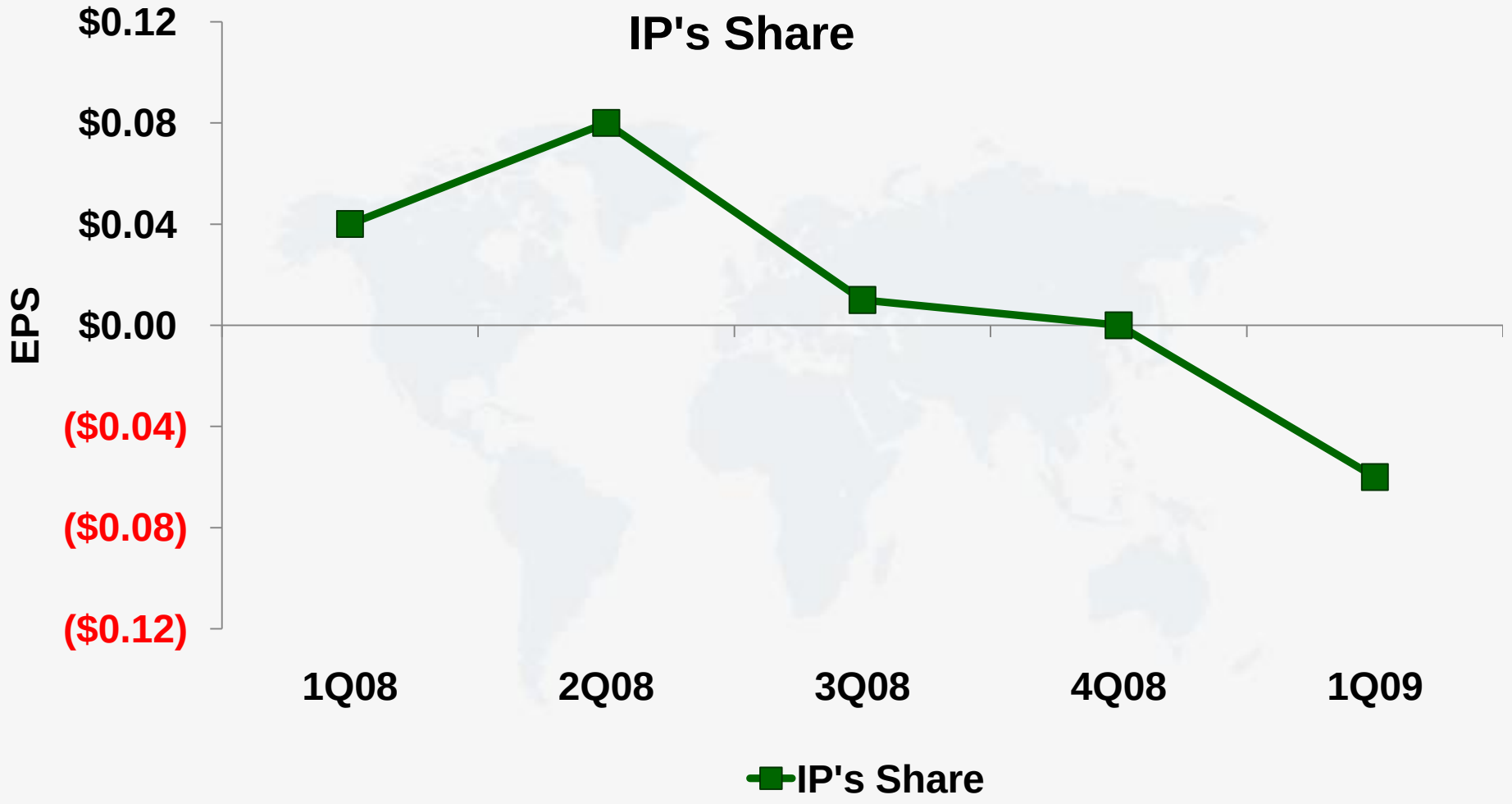
| | 2005 | 2008 |
|---|---|---|
| **# of Businesses** | **4** | **1** |
| **Sales** ($ Million) | **$684** | **$950** |
| **EBITDA** ($ Million) | **$217** | **$317** |
| **EBITDA Margin** | **32%** | **33%** |
| **UFS Supplier Position** | **#2** | **#1** |

# IP Transformation

## *Ilim - IP's Cumulative Share = $0.07*



# IP Transformation

## *Ilim - Improving Market Conditions*

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**Market Pulp for China**

- 50% of Ilim total capacity
- YTD pulp imports up 25% vs. 2008 levels
- Softwood pulp pricing starting to improve
- Hardwood pulp pricing nearing bottom

# IP Transformation

## *Ilim - Remain Positive on Russia*

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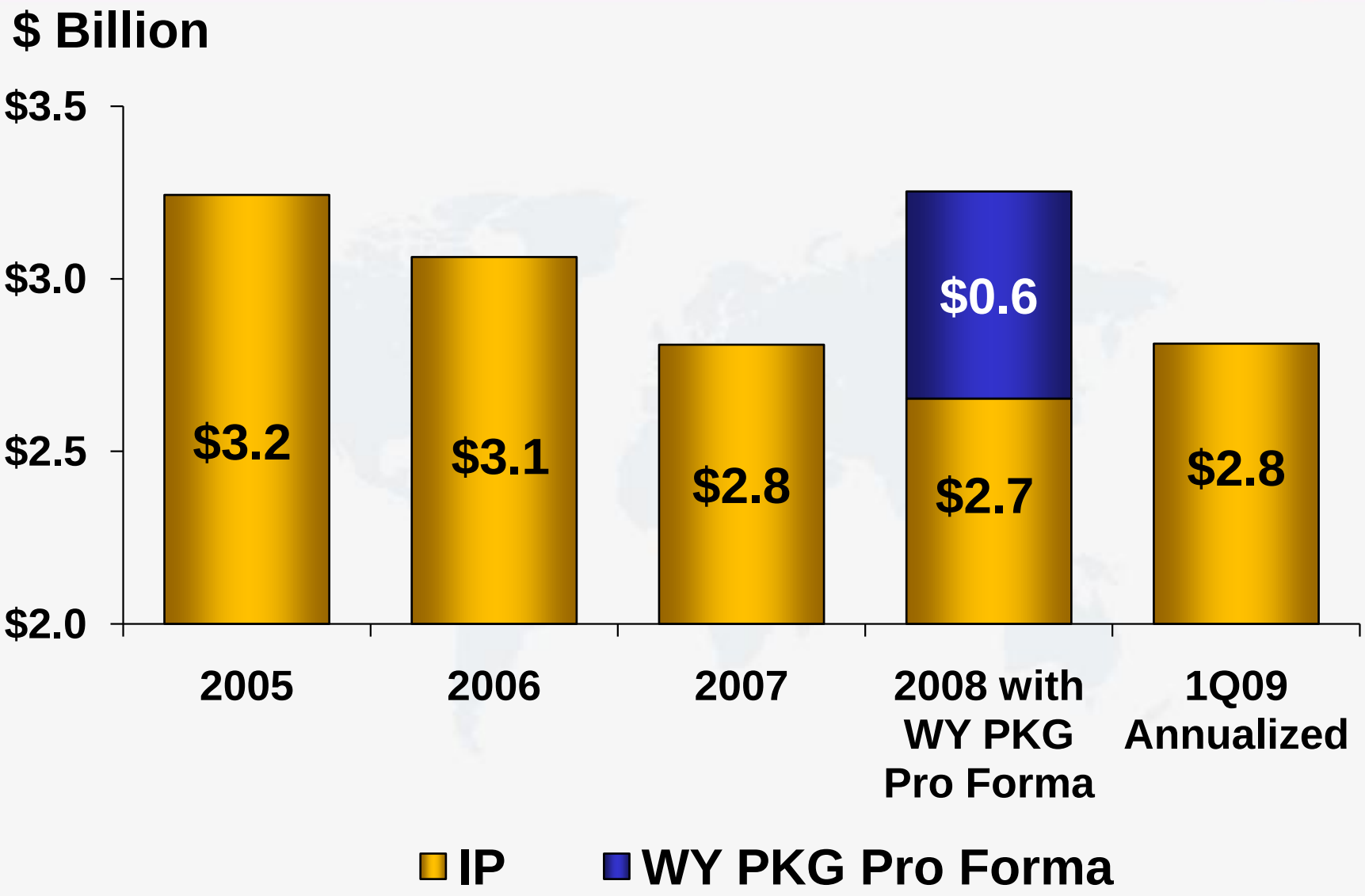
- Worst part of economic crisis is over
- Siberian mills remain potential long-term, low-cost China market pulp suppliers
- Attractive growth opportunities
- Significant cost reductions underway
  - Fiber
  - Employees
- Timing of capital investments remain dependent on internal cash flow generation

# IP Transformation

## *Systematic Overhead Cost Reductions*




Includes discontinued operations

# IP Transformation

## *28% Headcount Reduction by 2009*

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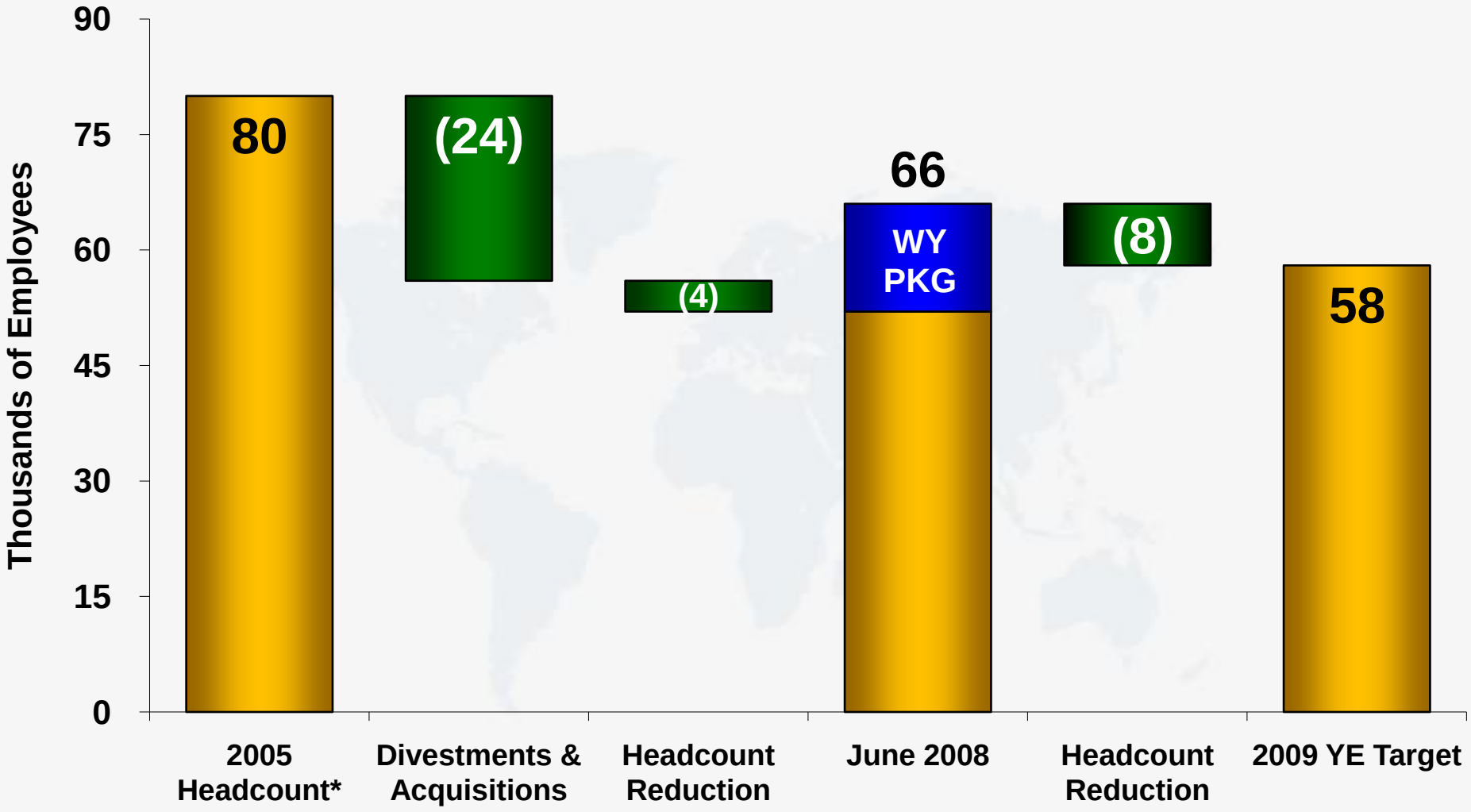
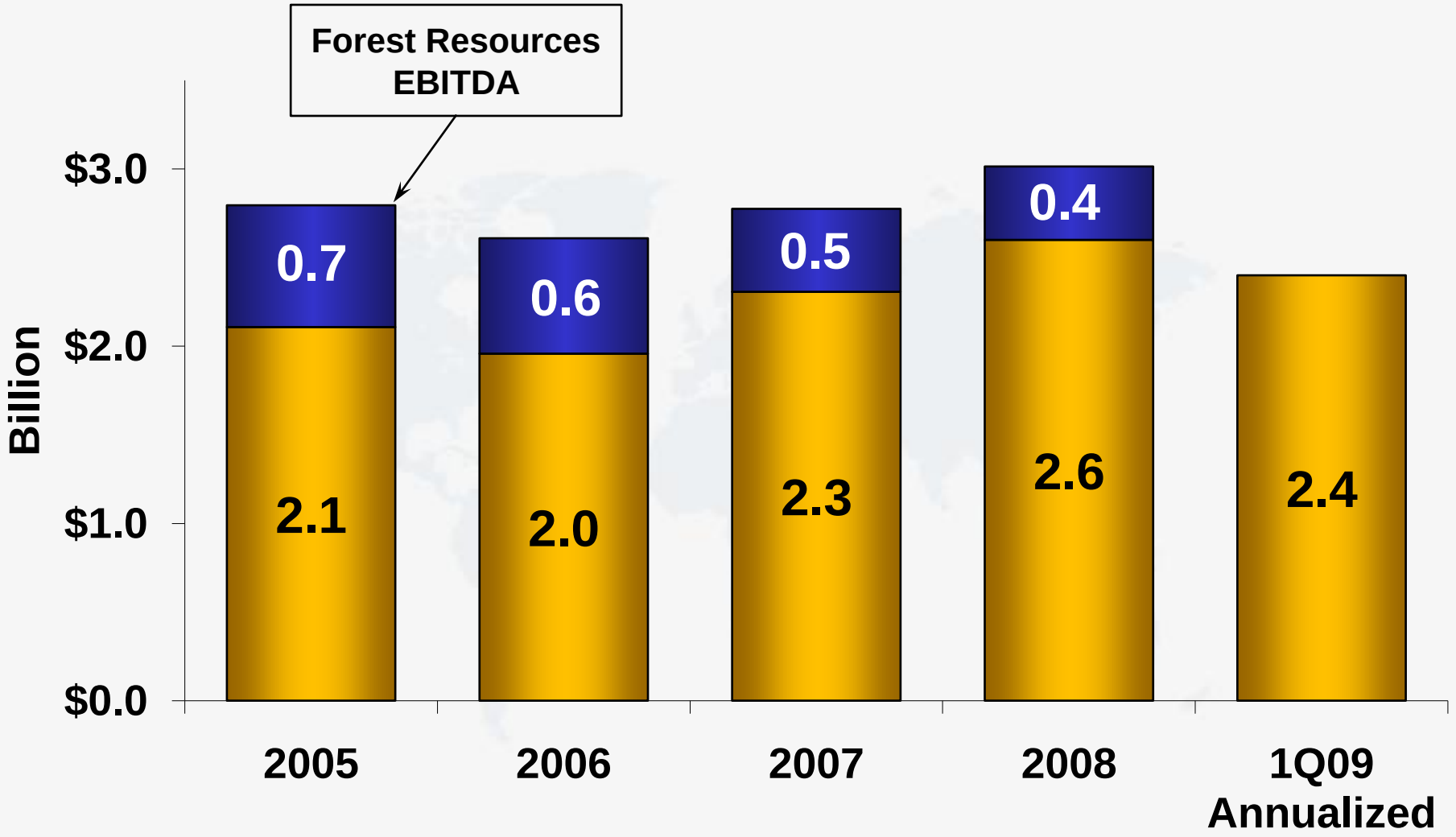



* At January 1, 2005
Excludes Ilim joint venture employees

# IP Transformation

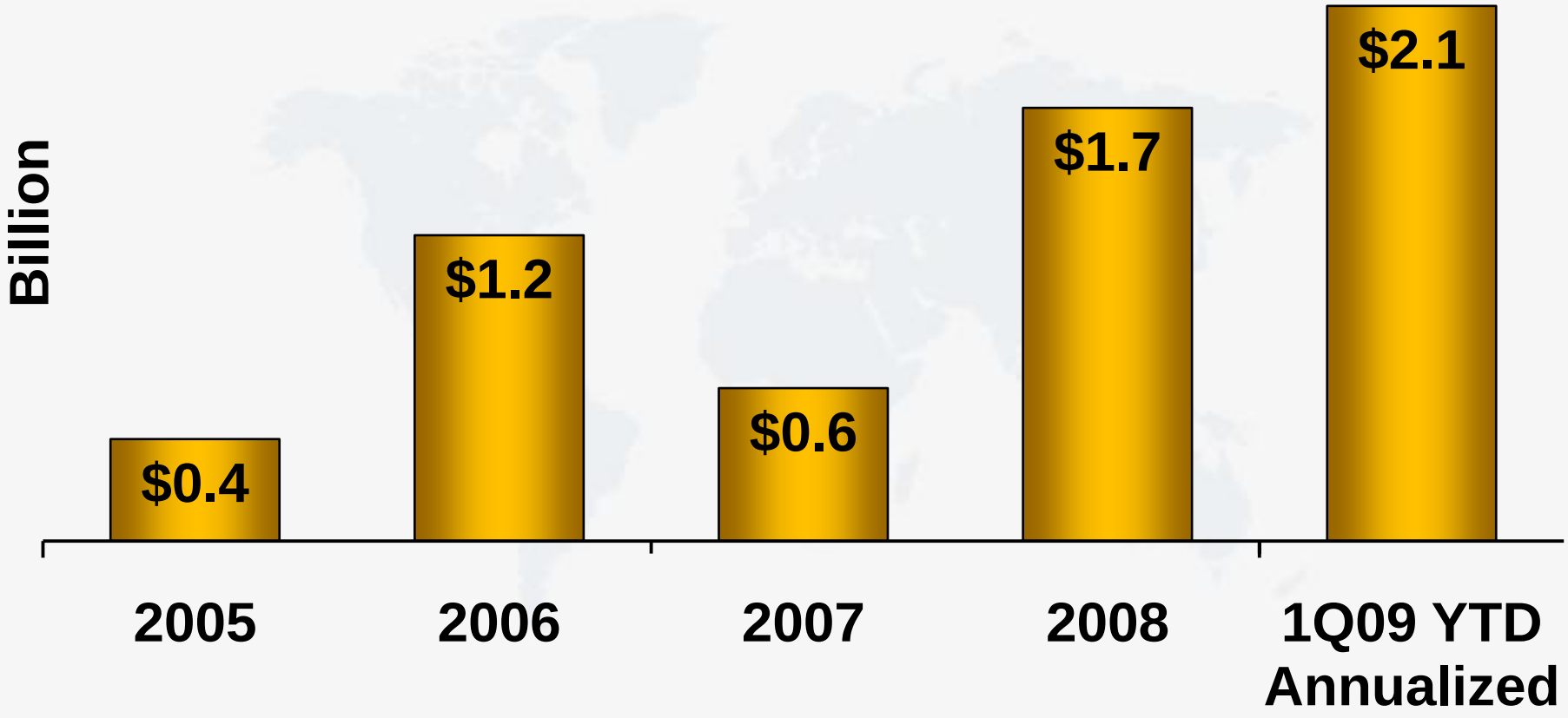
## *Improving EBITDA Quality*




EBITDA before special items including discontinued operations

# IP Transformation

## *Increasing Free Cash Flow*




Free cash flow before dividends; 1Q09 YTD annualized excludes $145 million in alternative fuel mixture tax credits

# IP Transformation
## *Summary*

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- **Greater Focus**
- **Strengthened Core Businesses**
  - Lower-Cost Assets
  - Improved Results
- **Replaced Forest Resources Earnings**
- **Generated Record Free Cash Flow**
- **Strategic Investments in Emerging Markets**

# 2009 Performance Update

## *World Changed in the Last Six Months*

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| | 2005 – 3Q08 | 4Q08 – May 09 YTD |
|---|---|---|
| Volumes | Steady | Declined Significantly |
| Prices | Increasing | Eroded Slowly |
| Input Costs | Significant Increases | Cost Relief |
| Cost Reduction | Steady Progress | Increased Progress |
| Operations | Good | Excellent |
| Market Downtime | Very Limited | 20% – 30% |
| Free Cash Flow | Mixed | Good |

# 2009 Performance Update

## *Transformation Driving Improved Results*

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- **Strong Free Cash Flow**
- **Improved Margins**
  - **North American Industrial Packaging**
  - **North American Printing Papers**
- **Improving Balance Sheet**
- **Ability to Generate Higher Returns**



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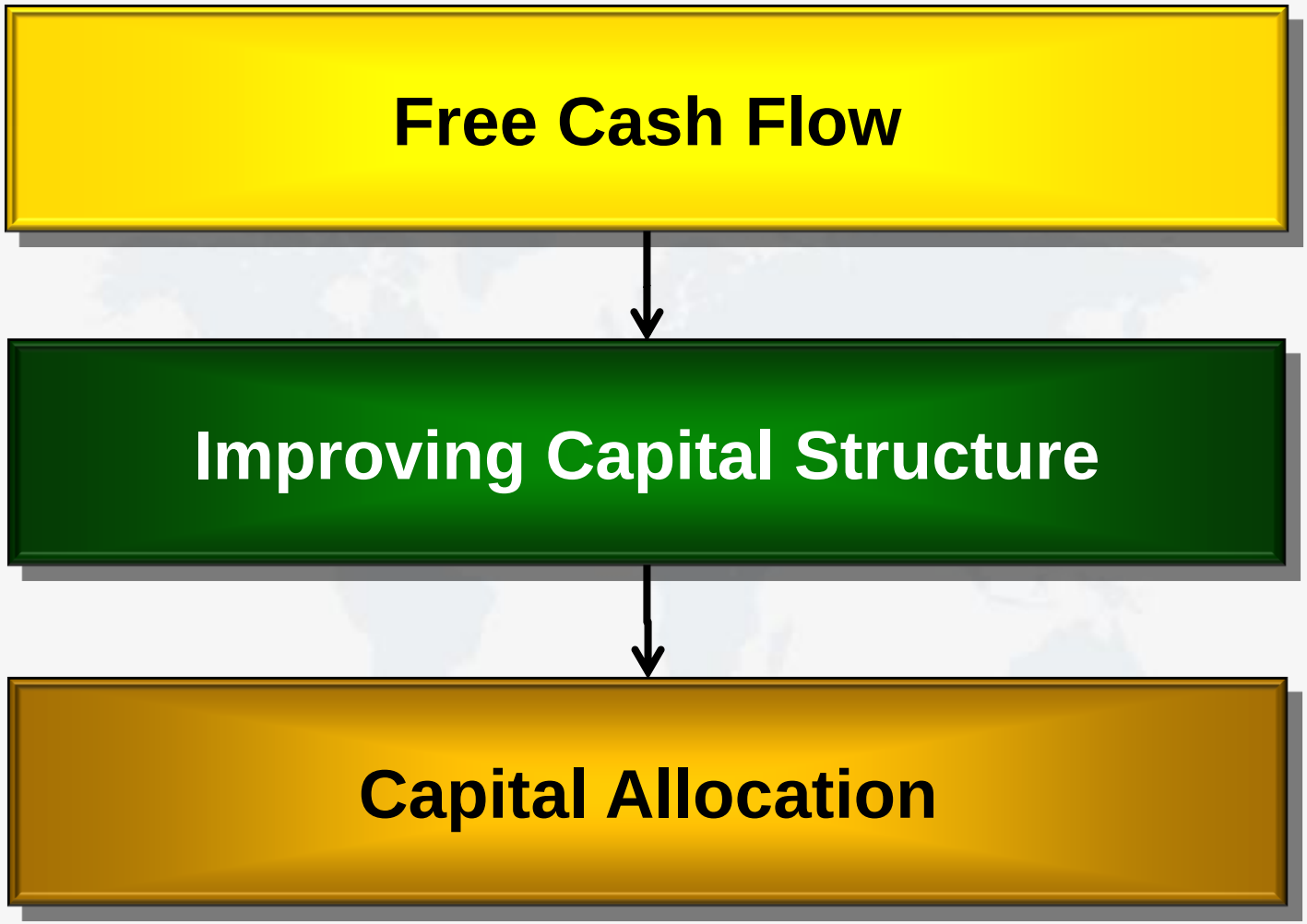
# Financial Update & Direction

Tim S. Nicholls,
Senior Vice President & Chief Financial Officer

# Agenda


Free Cash Flow
Improving Capital Structure
Capital Allocation

# Increasing Free Cash Flow

## *Fewer, Larger, Lower-Cost Mills*

| | Manufacturing Cost Position | |
|---|---|---|
| | 1st Quartile | 2nd Quartile |
| NA - Containerboard | 60% | 20% |
| NA - Uncoated Freesheet | 90% | 10% |
| NA - Coated Paperboard | 100% | - |
| Brazil – Uncoated Freesheet | 80% | 20% |
| Russia – Softwood Market Pulp | 70% | 30% |
| China – Coated Paperboard | 75% | 25% |

Based on Poyry's 2008 CostTrac model global cost curves at 4th quarter input costs and exchange rates

# Increasing Free Cash Flow

## *22,000 Headcount Reductions by 2009*

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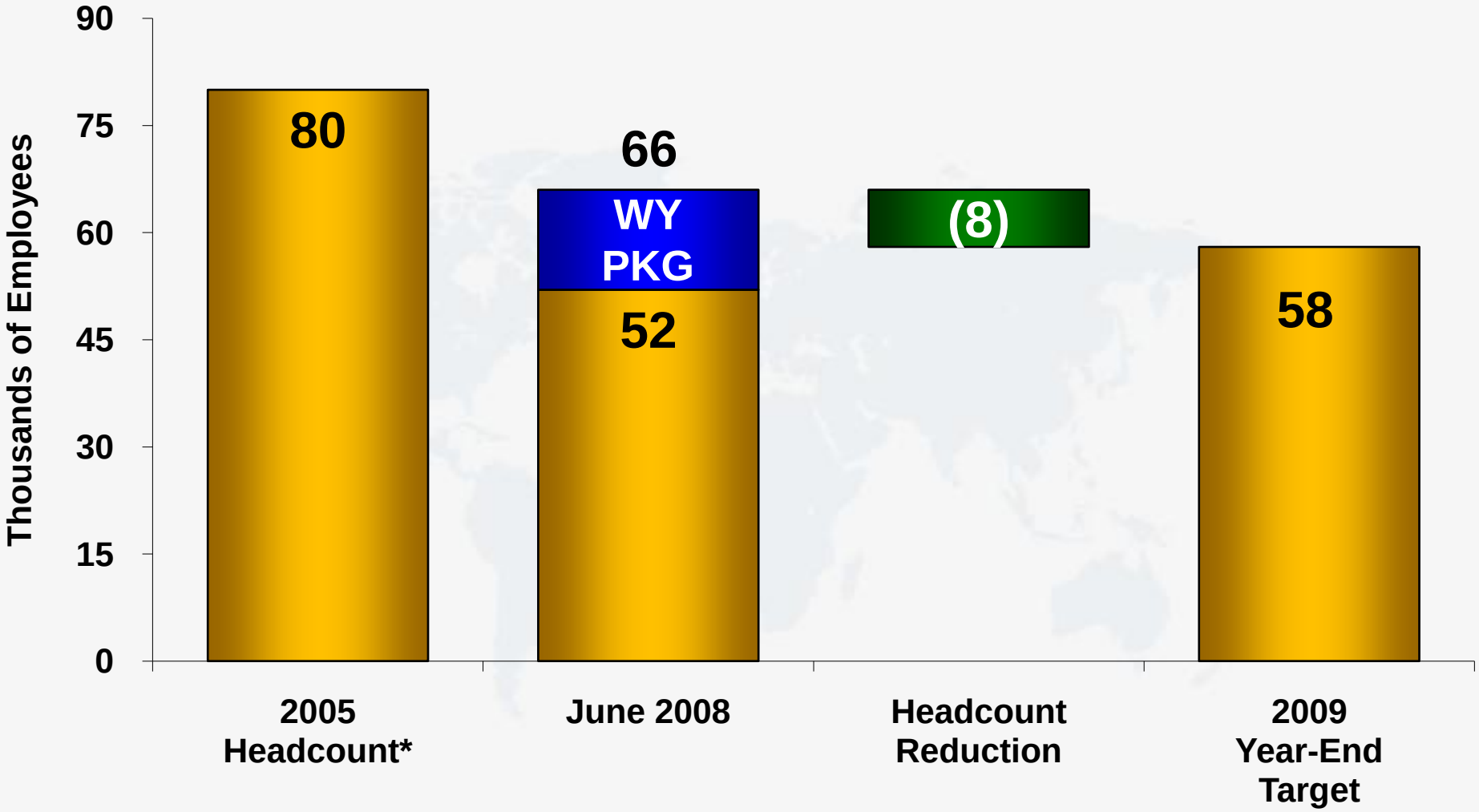


* At January 1, 2005
Excludes Ilim joint venture employees

# Increasing Free Cash Flow

## *Overhead Cost Reduction 2008 - 2010*

| | $ Million |
|---|---|
| Salaried Expense Reduction | $405 |
| Non-Employee Savings | $65 |
| **Total with Balance of 2009-10 Projected** | **$470** |

Salaried expense reduction includes approximately $200 million of WY PKG integration synergies

# Increasing Free Cash Flow

## *Reduced 2009 Input Costs of $875 Million*

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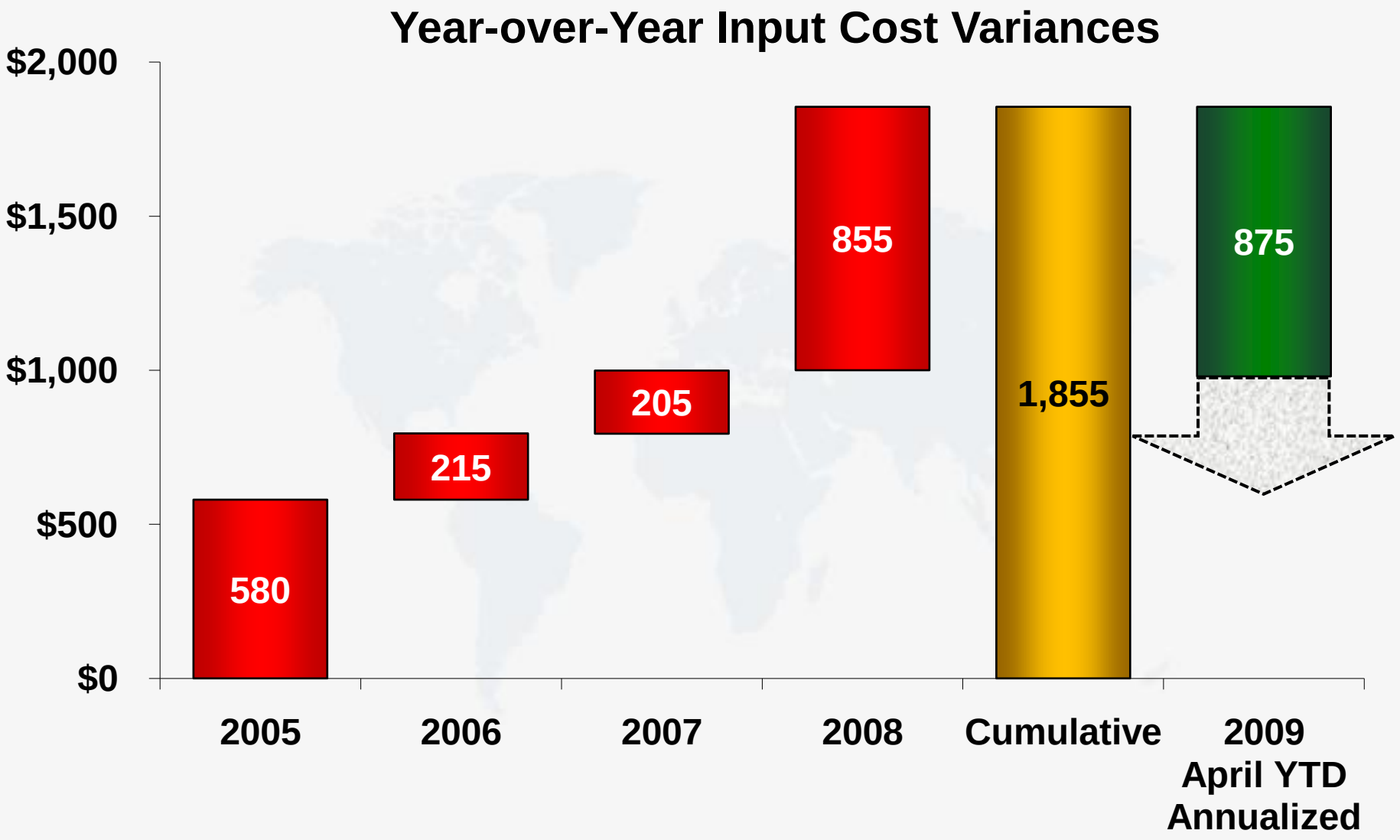
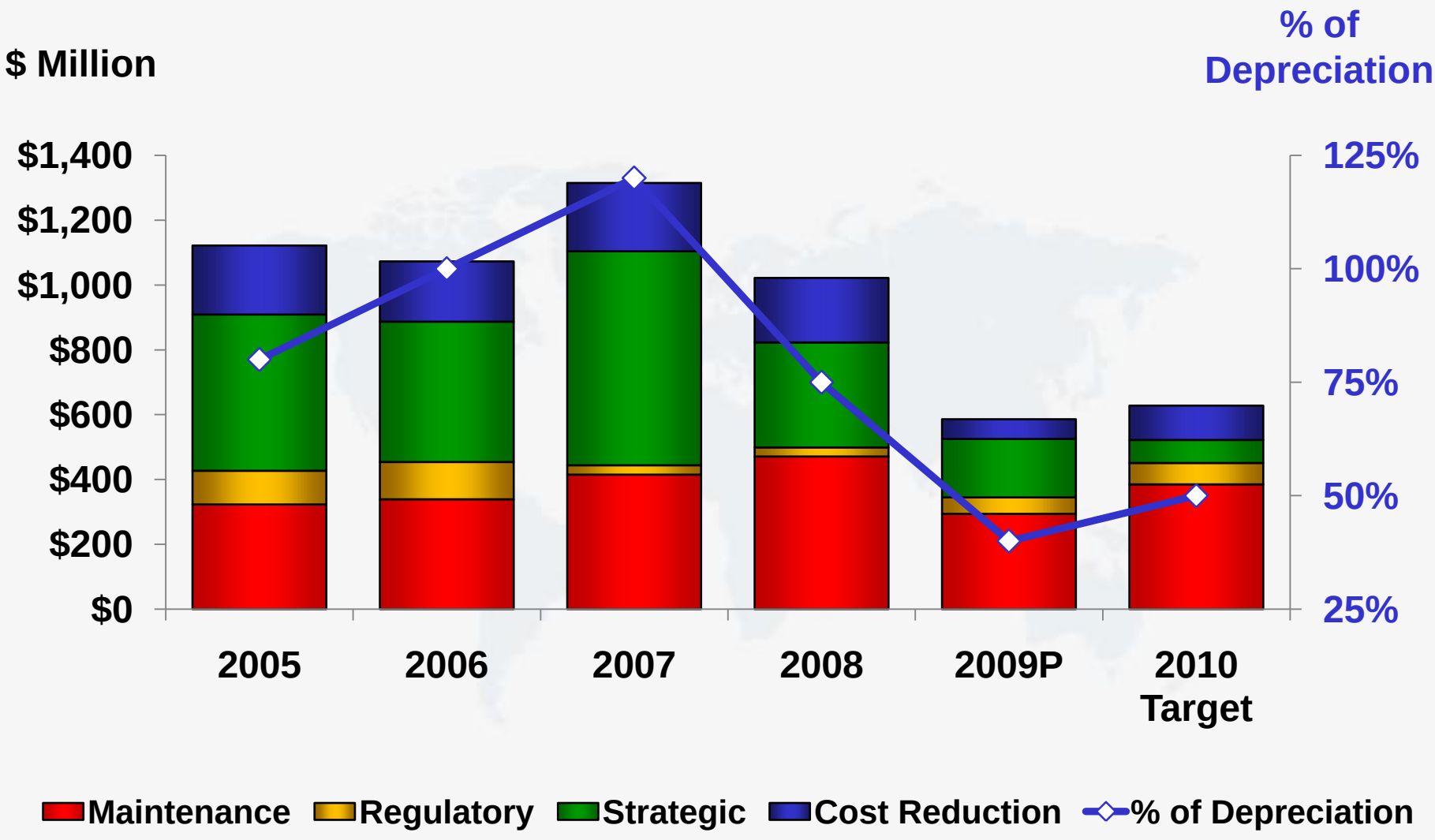



April 2009 YTD annualized input cost savings versus 2008 levels

# Increasing Free Cash Flow

## *Reducing Capital Spending*



# Increasing Free Cash Flow

## *More-Focused Capital Spending*

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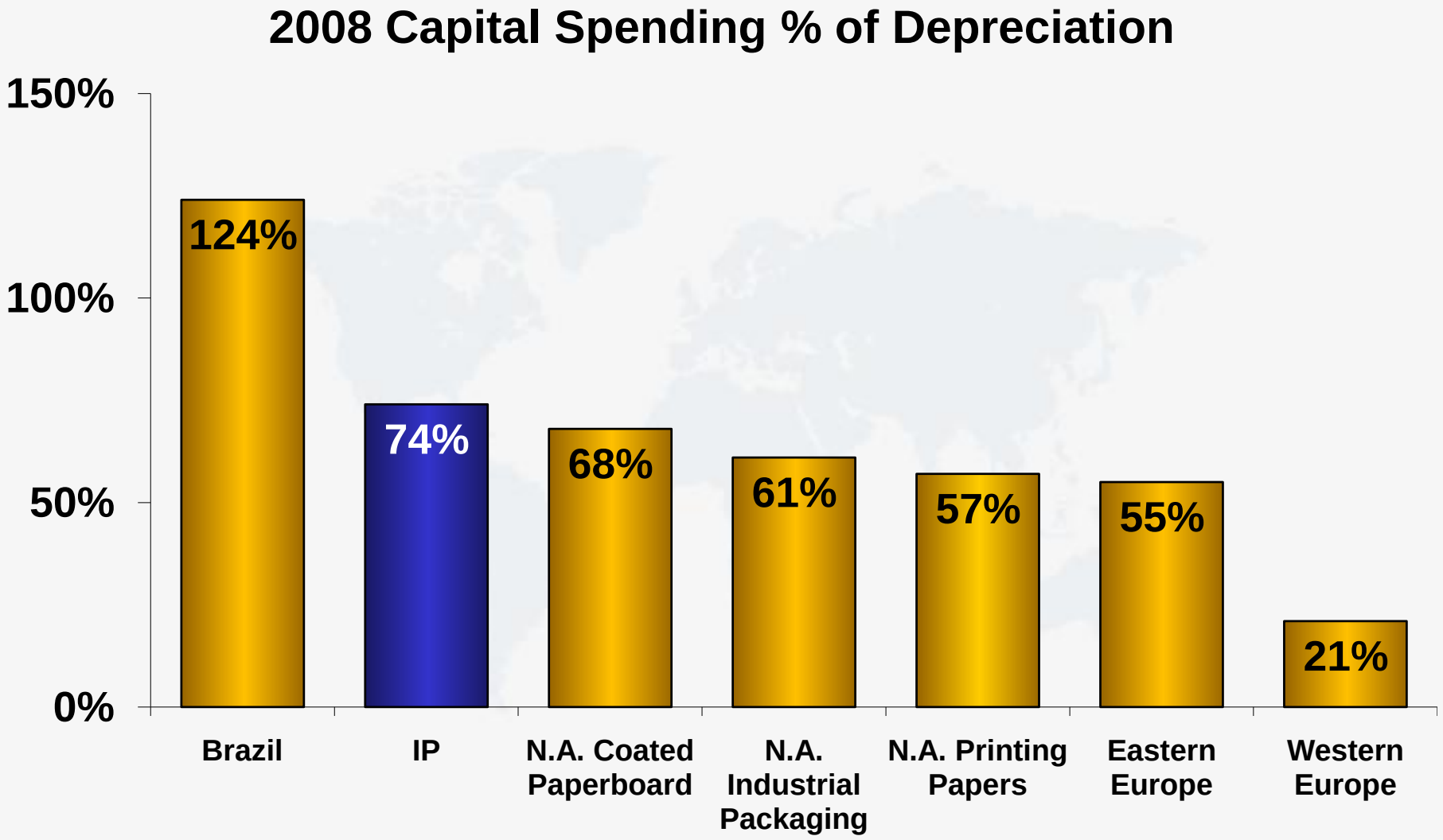


Sun joint venture capital spending in 2008 was approximately $150 million.

# Increasing Free Cash Flow

## *Improving Global Mill Efficiency*

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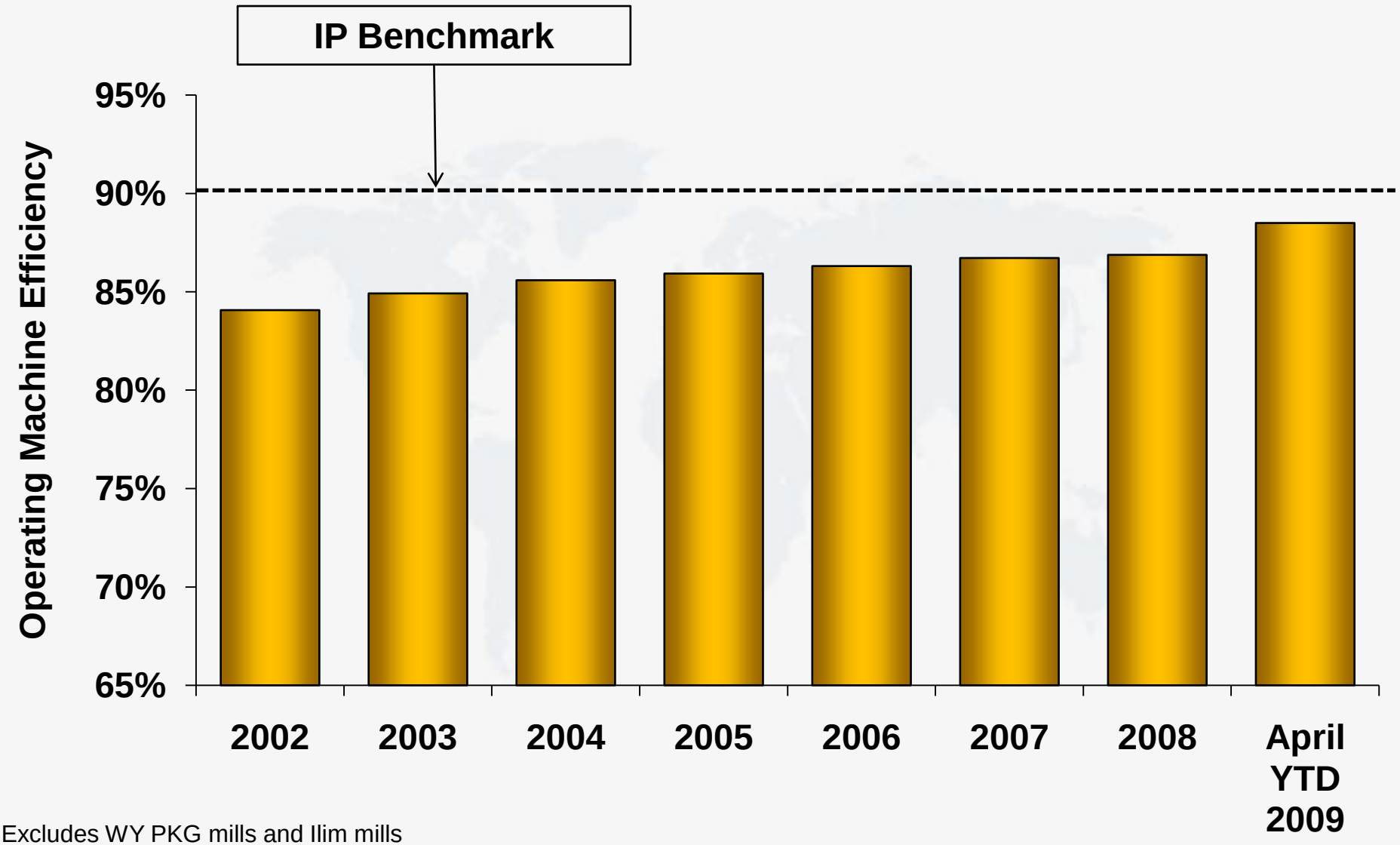


Excludes WY PKG mills and Ilim mills

# Increasing Free Cash Flow

## *Reducing Energy Consumption*

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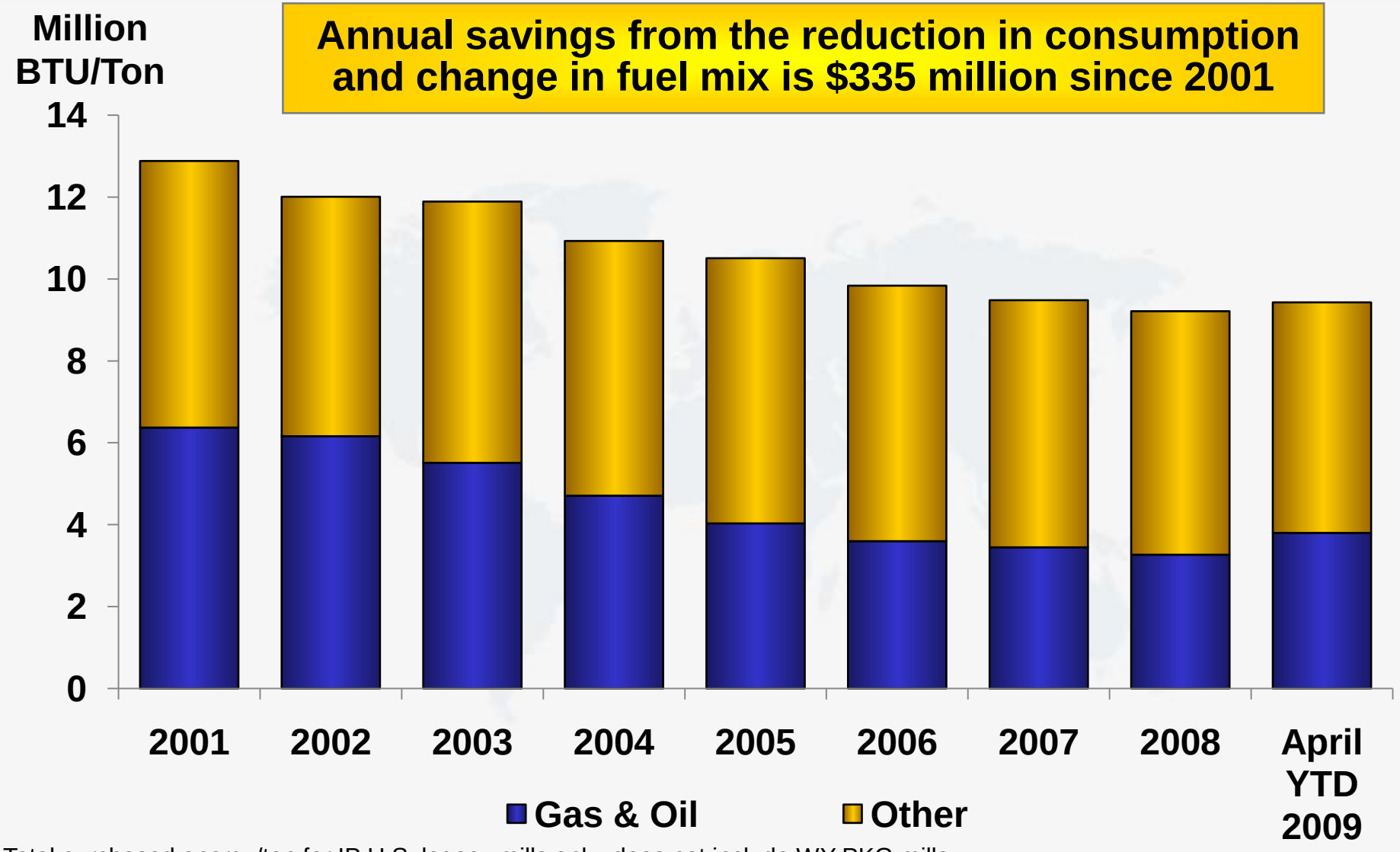
**Annual savings from the reduction in consumption and change in fuel mix is $335 million since 2001**




Total purchased energy/ton for IP U.S. legacy mills only; does not include WY PKG mills

"Other" includes purchased electricity and steam, coal, purchased wood waste, and other materials

# Increasing Free Cash Flow

*Largest Renewable Energy Generator & User*

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- **70% of IP's total mill energy needs are from renewable resources**
- **Black liquor energy is clean, carbon-neutral, renewable & efficient**
- **In 2008, IP produced 6 billion kilowatt-hours of electricity from renewable energy sources**
- **Black liquor renewable energy should be treated on an equal tax basis with other sources of renewable energy**

# Increasing Free Cash Flow

*No Additional Fossil Fuel Used to Qualify for Credits*

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**Total Self-Generated Mill Power**
**(70% from Renewable Resources)**

**Power Boilers**
**(Oil, Gas, Coal, Wood Waste)**

**Recovery Boiler**
**(Black Liquor)**

**Diesel fuel now consumed in recovery boilers replaces fossil fuels consumed in power boilers**

# Increasing Free Cash Flow

## *Industrial Packaging Integration Synergies*

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| Category | Amount ($ Million) |
|---|---|
| Reduce Salaried Headcount | $200 |
| Optimize Mill & Box Plants | $120 |
| Improve Box Margins | $105 |
| Reduce Mill Freight | $40 |
| Rationalize Box Plants | $35 |
| Total Forecasted Synergies | > $500 |

Does not include $90 million in procurement savings

# Increasing Free Cash Flow

*Reduced Dividend to Create Financial Cushion*

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## Dividend Reduction

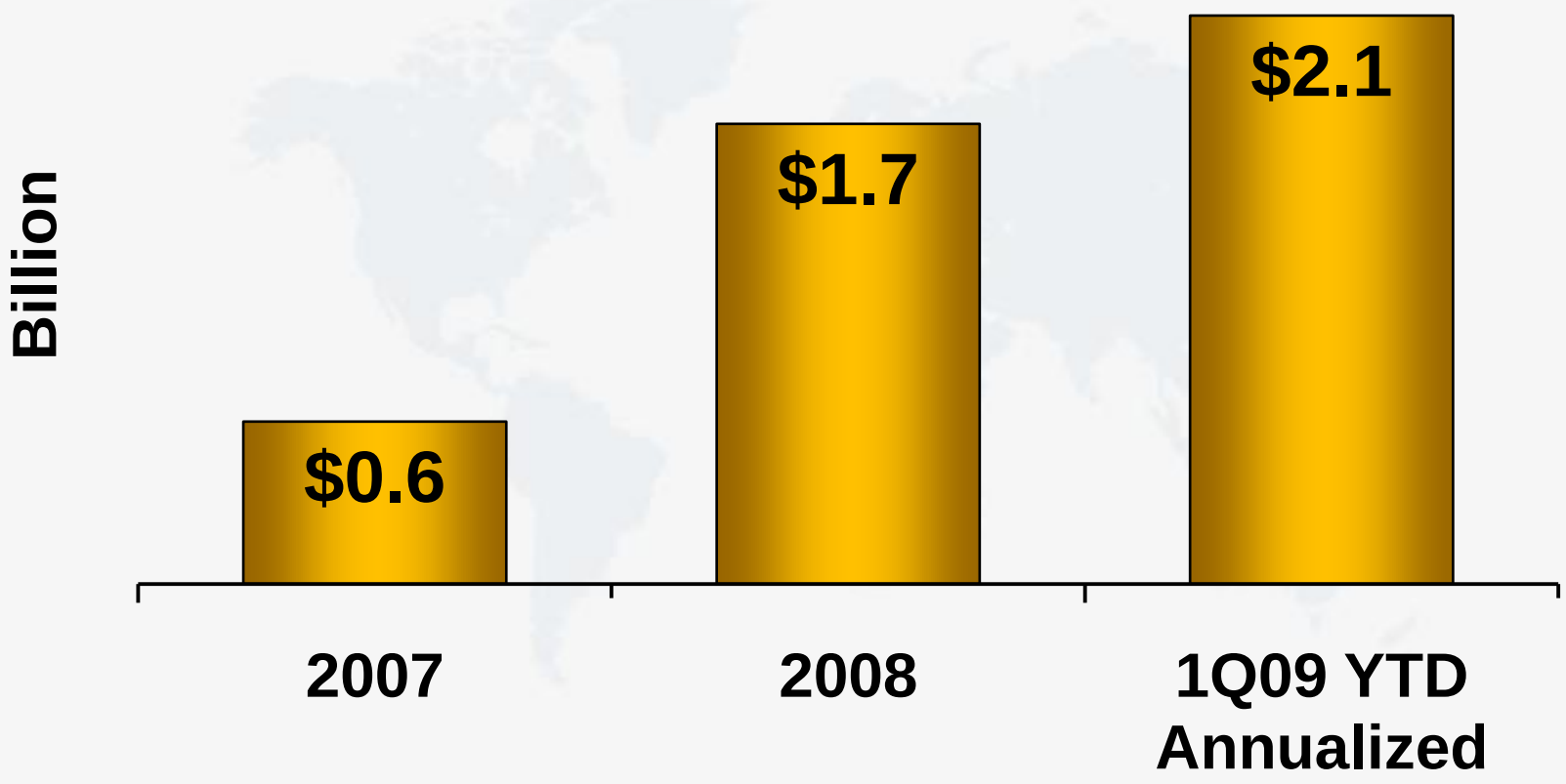
- Followed many other cash conservation efforts
- Uncertain economic conditions
- Frozen credit markets
- Managing cash conservatively
- Diverting cash to reduce debt at faster pace

## Dividend Increase

- Stable economic conditions
- Liquid credit markets
- Approaching target debt-to-EBITDA ratio

# Increasing Free Cash Flow

## *Improving in a Tough Environment*




Free cash flow before dividends.

1Q09 Annualized is free cash flow before dividends, excluding $145 million impact of alternative fuel mixture tax credits.

# Increasing Free Cash Flow

## *Significant, Continuous Progress*

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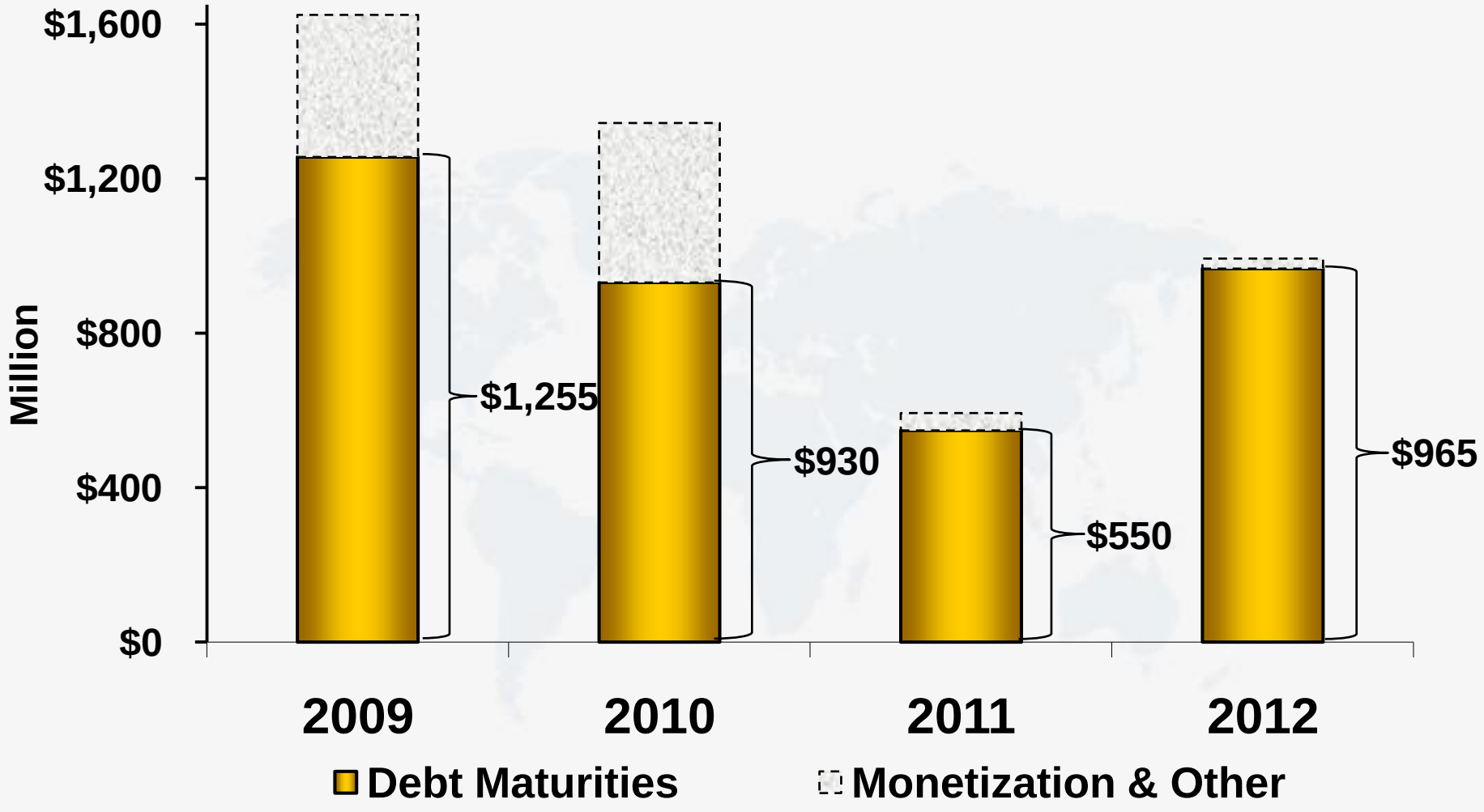
- **Eliminating positions**
- **Freezing salaries**
- **Reducing operating costs**
- **Reducing capital spending**
- **Earning alternative fuel tax credits**
- **Generating greater merger synergies**

# Liquidity Management & Debt Reduction

## *Maturities before Repayments & Refinancing*

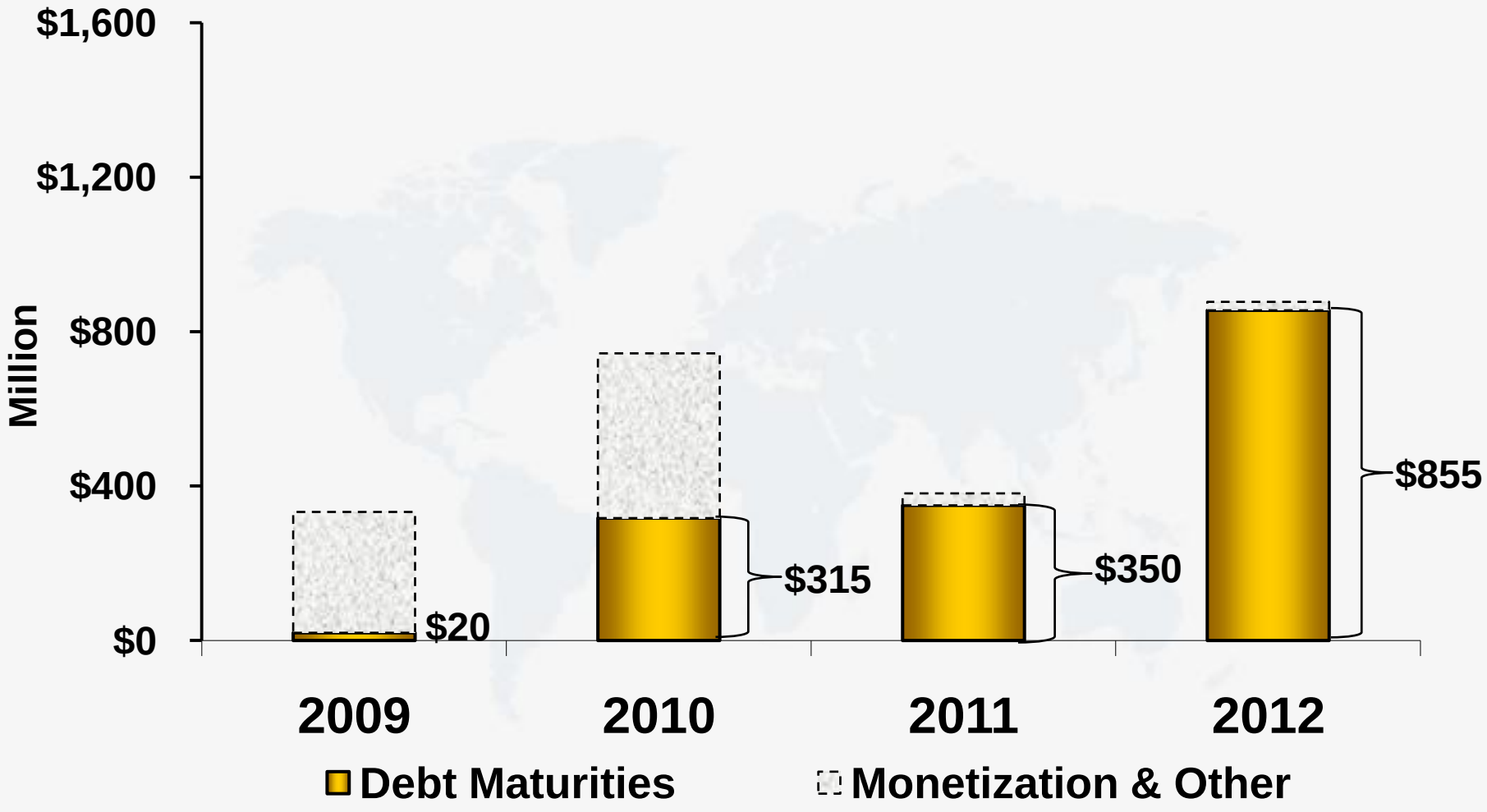



Debt maturity profile as of December 31, 2008

Monetization & Other: Intend to rollover or refinance timber monetization debt, Sun JV debt and other foreign subsidiary debt

# Liquidity Management & Debt Reduction

## *Maturities after Repayments & Refinancing*




Debt maturity profile as of May 31, 2009

Monetization & Other: Intend to rollover or refinance timber monetization debt, Sun JV debt and other foreign subsidiary debt

# Liquidity Management & Debt Reduction

## *Maturities after Repayments & Refinancing*

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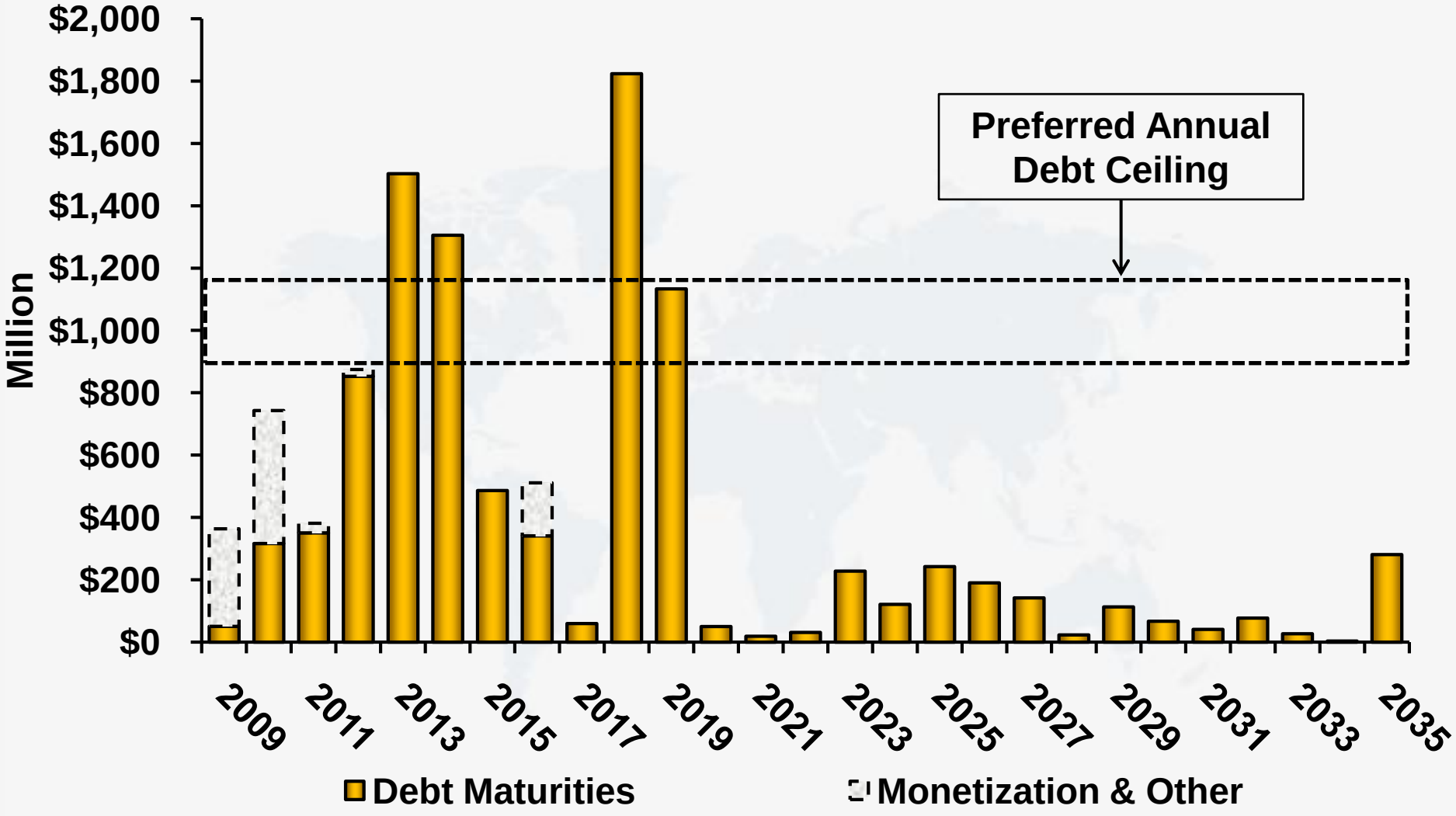


U.S. debt as of May 31, 2009; foreign debt as of April 30, 2009

Monetization & Other: Intend to rollover or refinance timber monetization debt, Sun JV debt and other foreign subsidiary debt

# Liquidity Management & Debt Reduction

## *Credit Ratings & Debt Covenants*

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| | Rating | Outlook |
|---|---|---|
| Standard & Poor's | BBB | Negative |
| Moody's | Baa3 | Negative |

| | Covenant | 1Q09 Actual |
|---|---|---|
| Maximum Debt-to-Total Capital | 60% | 50.3% |
| Minimum Consolidated Net Worth | $9B | $11.4B |

# Liquidity Management & Debt Reduction

## *Strong Back-up Liquidity*

| | Maturity | Facility | Cost |
|---|---|---|---|
| Estimated End of May Cash Balance | - | $1.3 Billion | - |
| $1.0B[1] Accounts Receivables Program | JAN 2010 | Zero Drawn | CP Rate[2] + 150 bps |
| $1.5B Corporate Revolver | MAR 2011 | Zero Drawn | LIBOR + 50 to 60 bps |
| Total Cash & Committed Facilities | | $3.8 Billion | - |

Cost includes commitment fees

[1] $950 million available at April 30, 2009 based on eligible receivable balances

[2] Conduit's rate

# Liquidity Management & Debt Reduction

## *$1.8 Billion Reduction in 10 Months*

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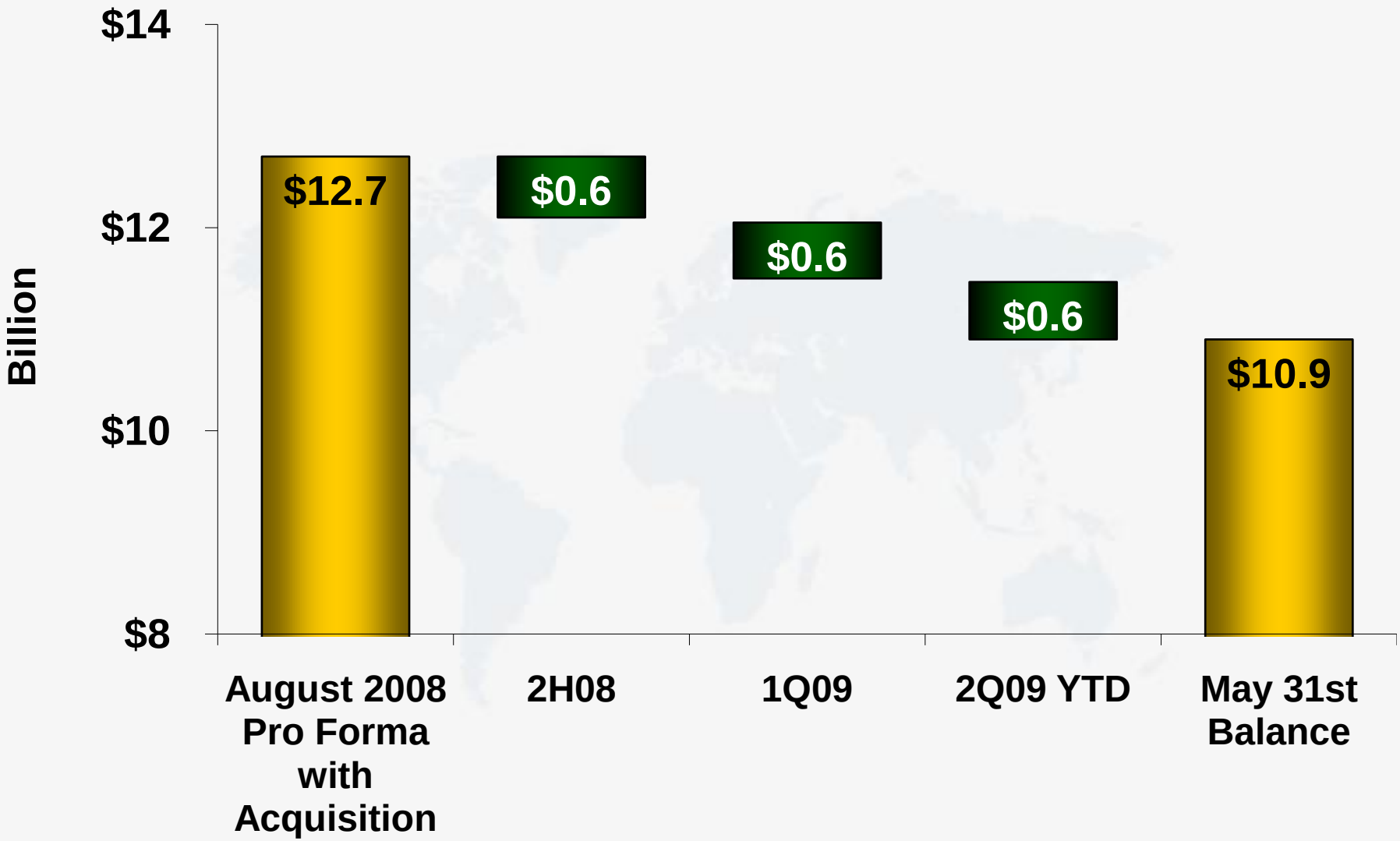

# Liquidity Management & Pension Funding

## *No Required Cash Contributions in 2009/10*

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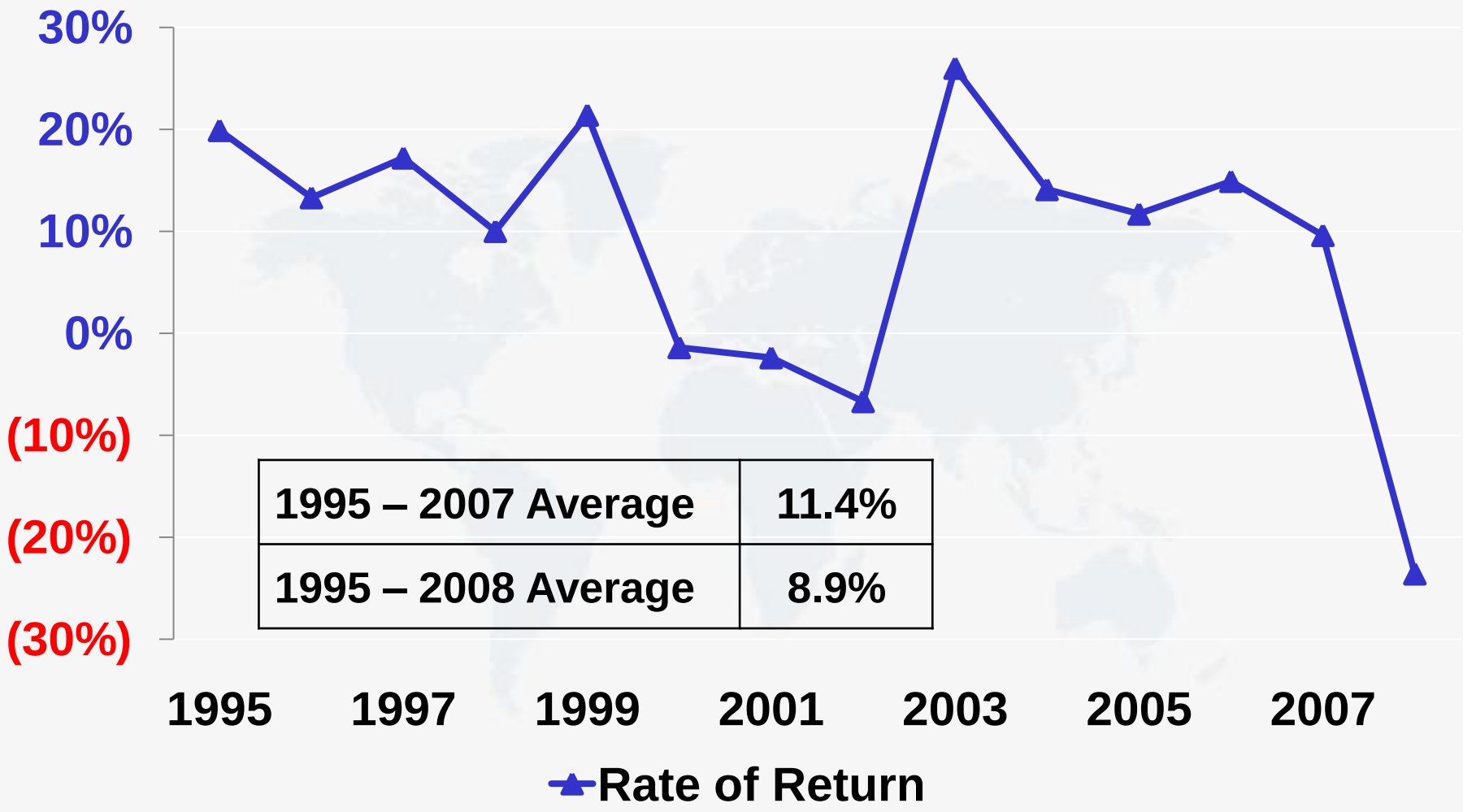
| Assumptions | 1995 – 2008 Actual Average | January 1, 2009 |
|---|---|---|
| Return on Assets | 8.9% | 8.25% |
| Discount Rate | 6.8% | 8.15% |

| Contributions | 2009 | 2010 |
|---|---|---|
| Fund-to-Minimum | $0 | $0 |

# Liquidity Management & Pension Funding

## *Historical Asset Return Rates*

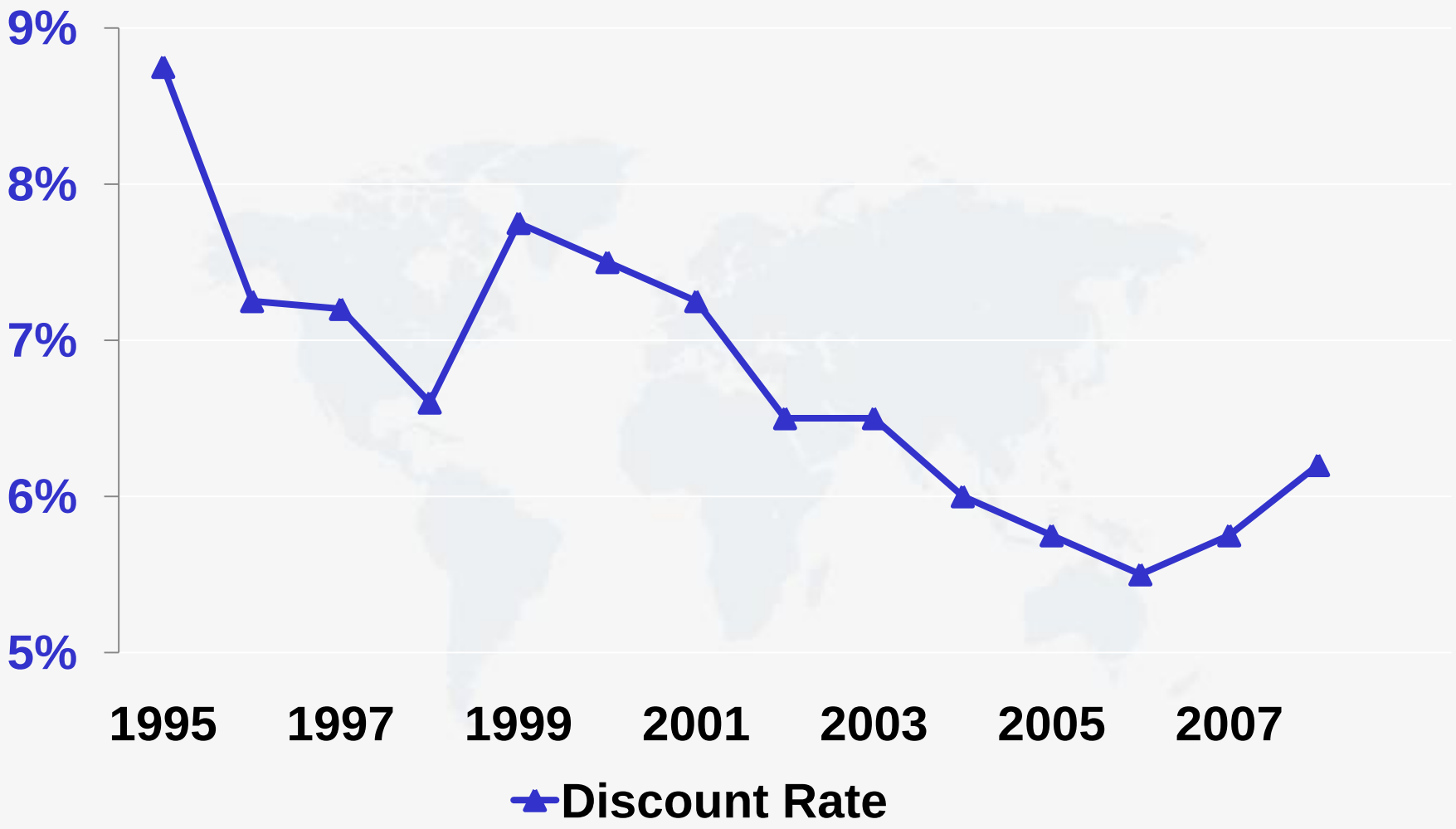



| | |
|---|---|
| 1995 – 2007 Average | 11.4% |
| 1995 – 2008 Average | 8.9% |

# Liquidity Management & Pension Funding

## *Historical Discount Rates*

INTERNATIONAL PAPER



# Free Cash Flow, Liquidity & Debt Reduction

## *Efforts Producing Results*

- **Generated 1Q09 FCF of $520 million***
- **Reduced debt by $1.2 billion in 2009YTD**
- **Reduced & extended 2009-12 maturities**

* Excludes $145 million of alternative fuel mixture credits

# Liquidity Management & Debt Reduction

## *Guidelines*

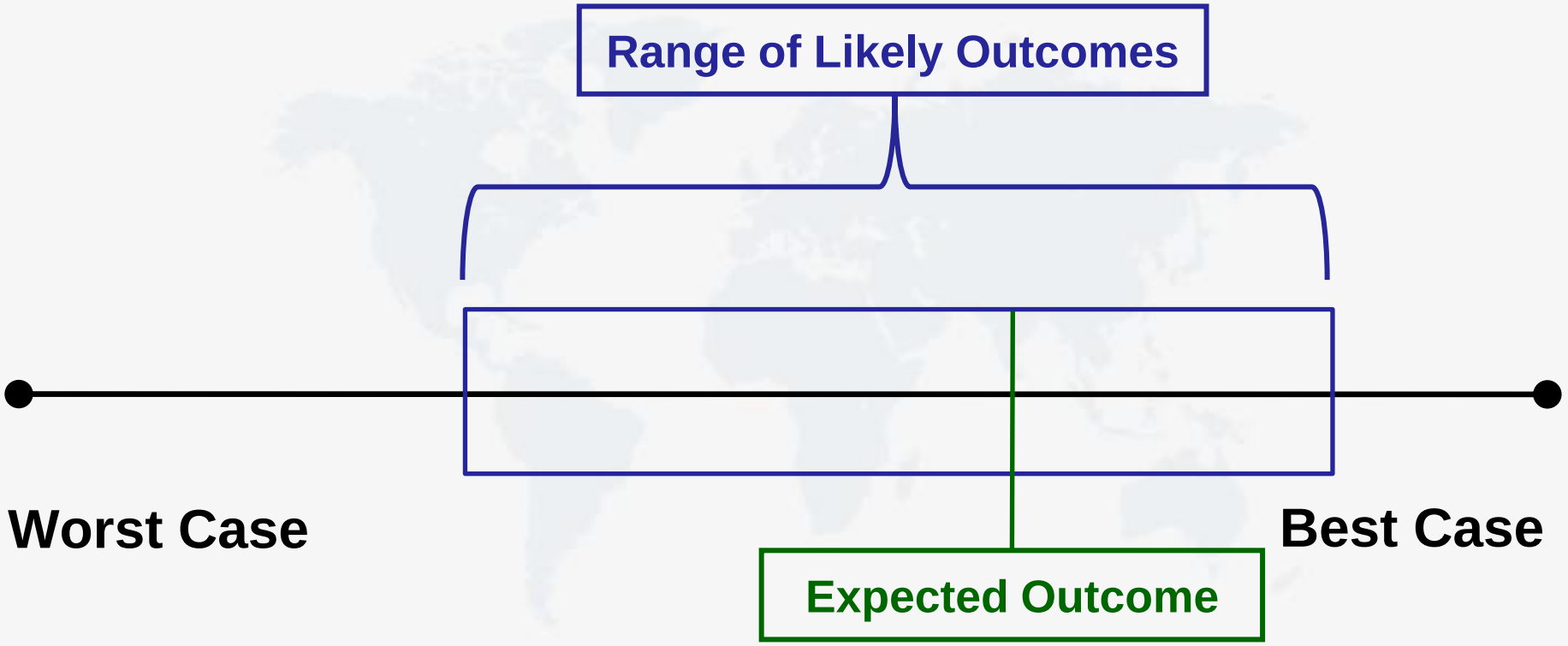
- **Total Debt-to-EBITDA Target of < 3X**
- **Limit maturities to ~ $1B per year**
- **Minimum cash & backup liquidity of ~20% of debt**

Total debt includes estimated pension liabilities & operating leases

# Risk Assessment
## *Improving our Process*

INTERNATIONAL PAPER

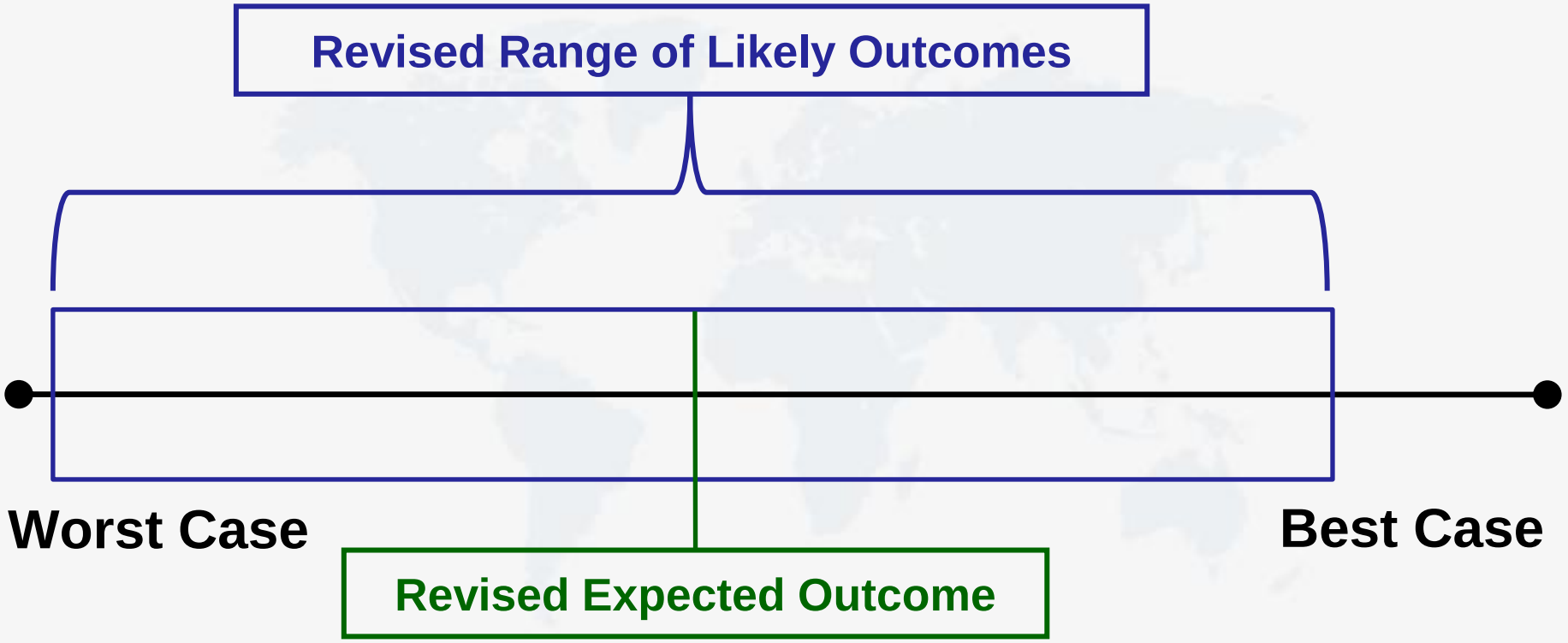
### Total Range of Potential Outcomes



# Risk Assessment
## *Improving our Process*

INTERNATIONAL PAPER

### Total Range of Potential Outcomes



# Capital Allocation

## *Current Focus on Debt Reduction*

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**Pursue Total Debt-to-EBITDA Ratio of < 3X**

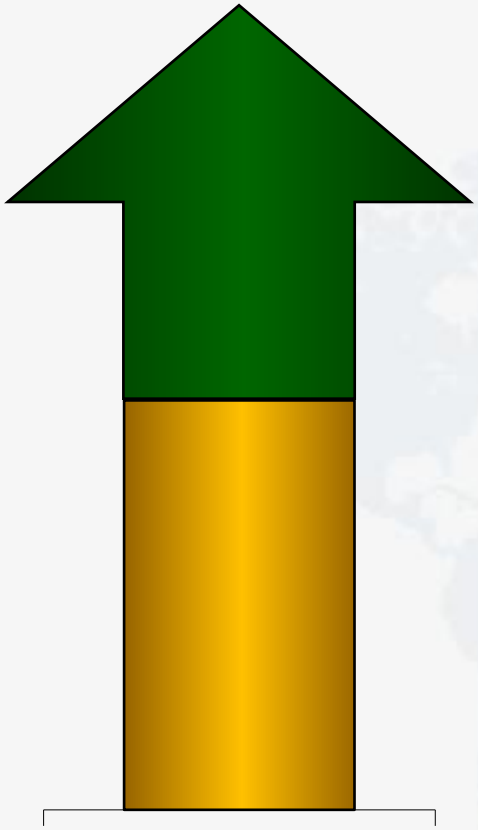
**Balance Use of Cash to Maximize Shareowner Value with Appropriate Risk**

Total debt includes estimated pension liabilities & operating leases

# Cash Flow & Debt Reduction Outlook

*Positioning for Stronger Cash Flow, Earnings*

INTERNATIONAL PAPER



Cash Flow
& Earnings

- Incremental Synergies
- Cost Reductions
- Lower Interest Expense
- Improved Margins
- Increased Volumes
- Reduced Downtime Costs



INTERNATIONAL PAPER



INTERNATIONAL PAPER

# North America Industrial Packaging

Carol L. Roberts,

Senior Vice President

# Agenda

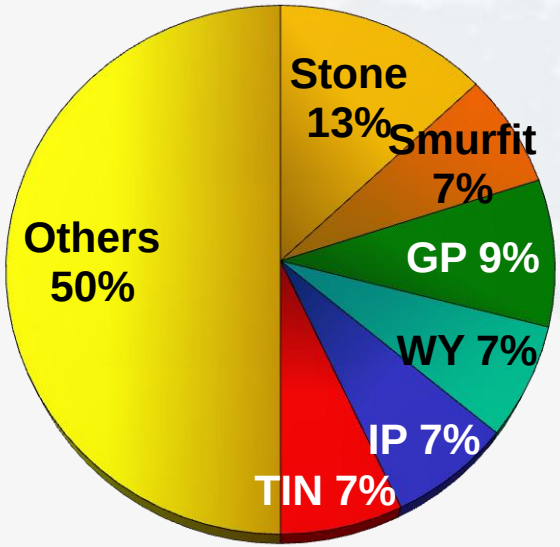
- **Containerboard Industry**
- **IP Strategy & Execution**
  - **Weyerhaeuser Packaging Integration**
  - **Low-Cost Mills**
  - **Profitable Box Plants**
  - **Market Access & Supply Management**
- **Financial Performance**

# North American Containerboard Industry

## *Consolidated Supply Positions*

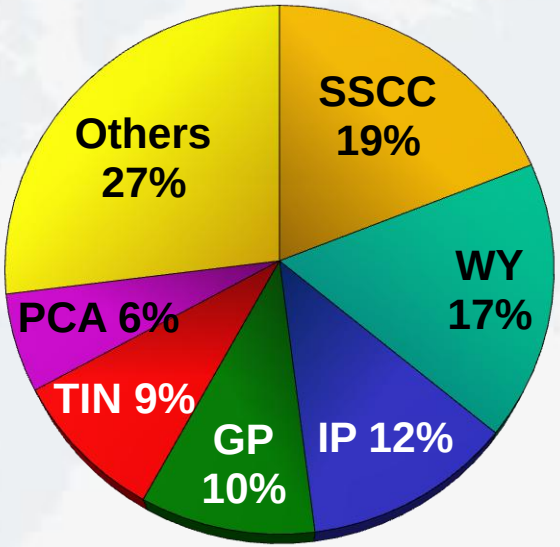
INTERNATIONAL PAPER

**1995**



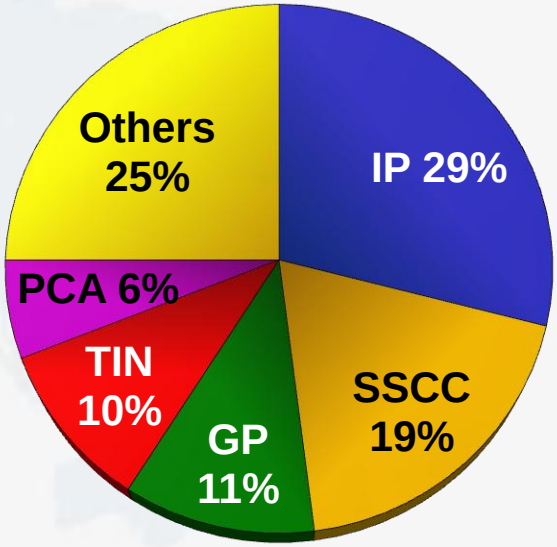

**Top 5 = 43%**

**2005**




**Top 5 = 67%**

**2008**




**Top 5 = 75%**

Source: SEC Filings, RISI, IP Analysis

# Global Containerboard Industry

## *Box Demand Growing with Global GDP*

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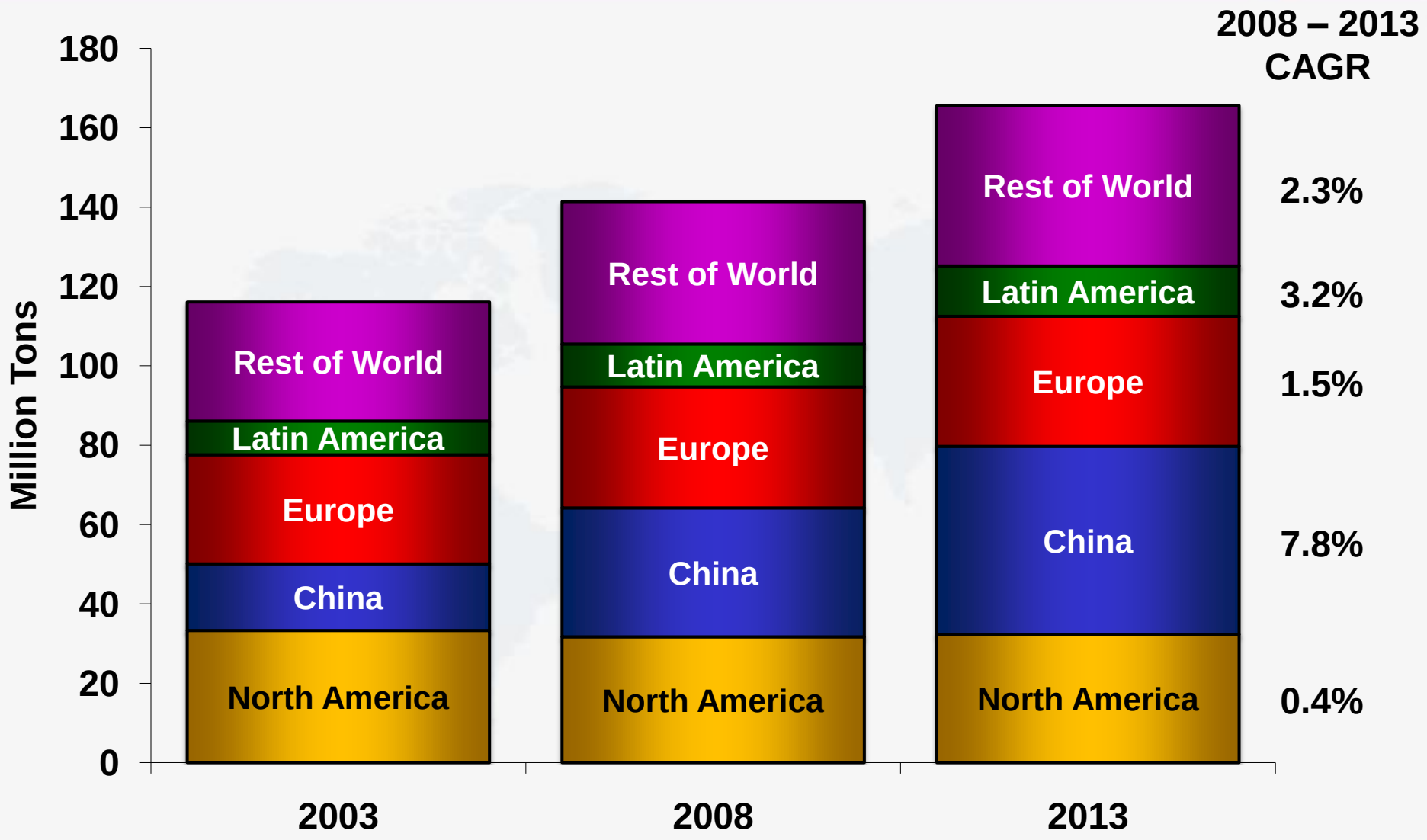


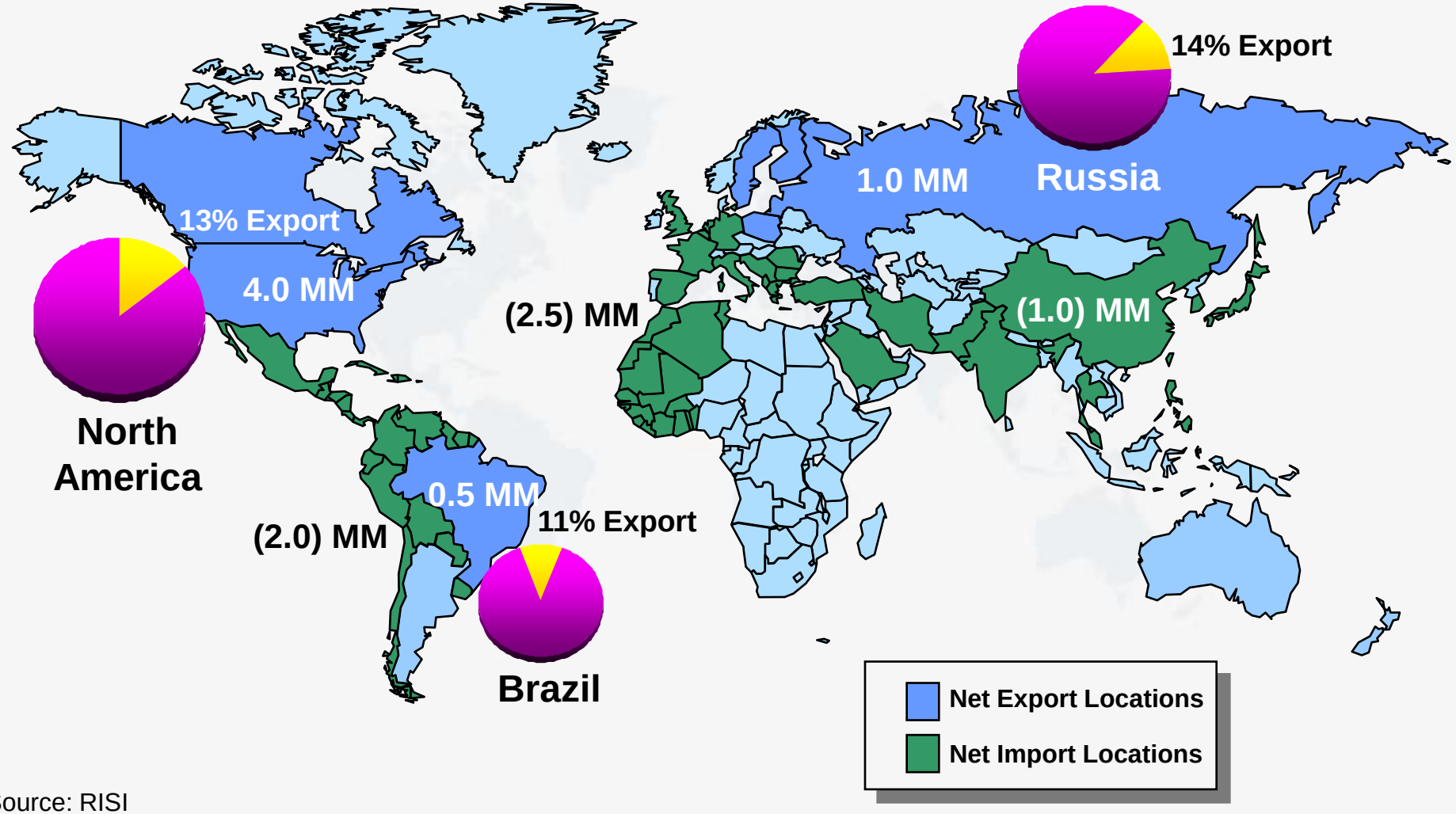

Source: RISI April 2009 Forecast

# Global Containerboard Industry

*North America Plays Key Role Supplying Growing Regions*

INTERNATIONAL PAPER

## Virgin Containerboard Trade Flows




Source: RISI

# IP Strategy & Execution

*Positioning to Generate Strong Free Cash Flow*

INTERNATIONAL PAPER

| | |
|---|---|
| **Vision** | **Become the premier North American producer of containerboard & corrugated packaging** |
| **Mission** | **Generate strong free cash flow & cost-of-capital returns** |

# IP Strategy & Execution

*Positioning to Generate Strong Free Cash Flow*

INTERNATIONAL PAPER

- **Greater synergies at faster rates**
- **World-class, low-cost mill system**
- **Competitive, profitable box business**
- **Optimize capacity & market access**
- **Maximize free cash flow**

# IP Strategy & Execution

## *Significant Increase in EBITDA and Margins*

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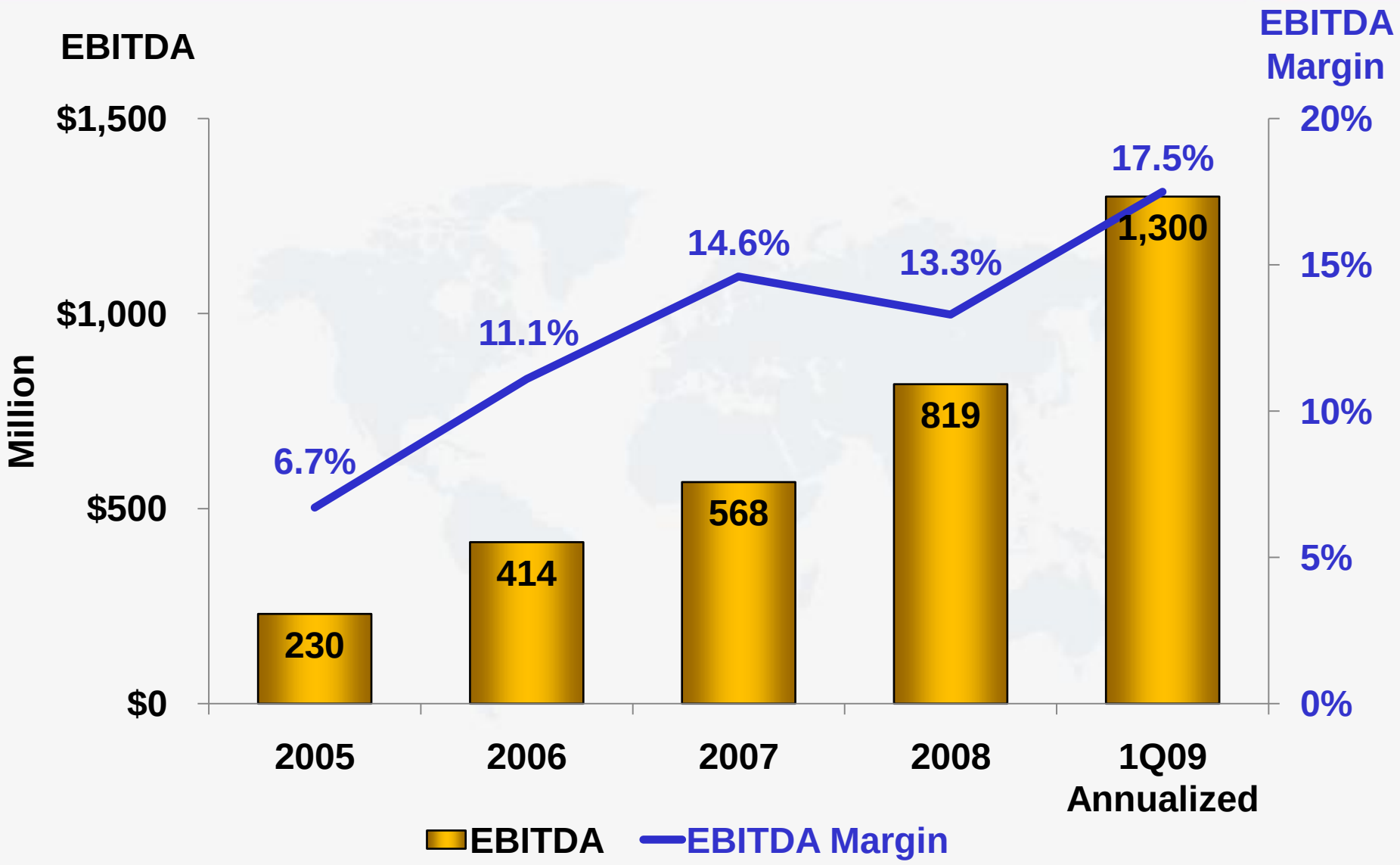


# IP Strategy & Execution

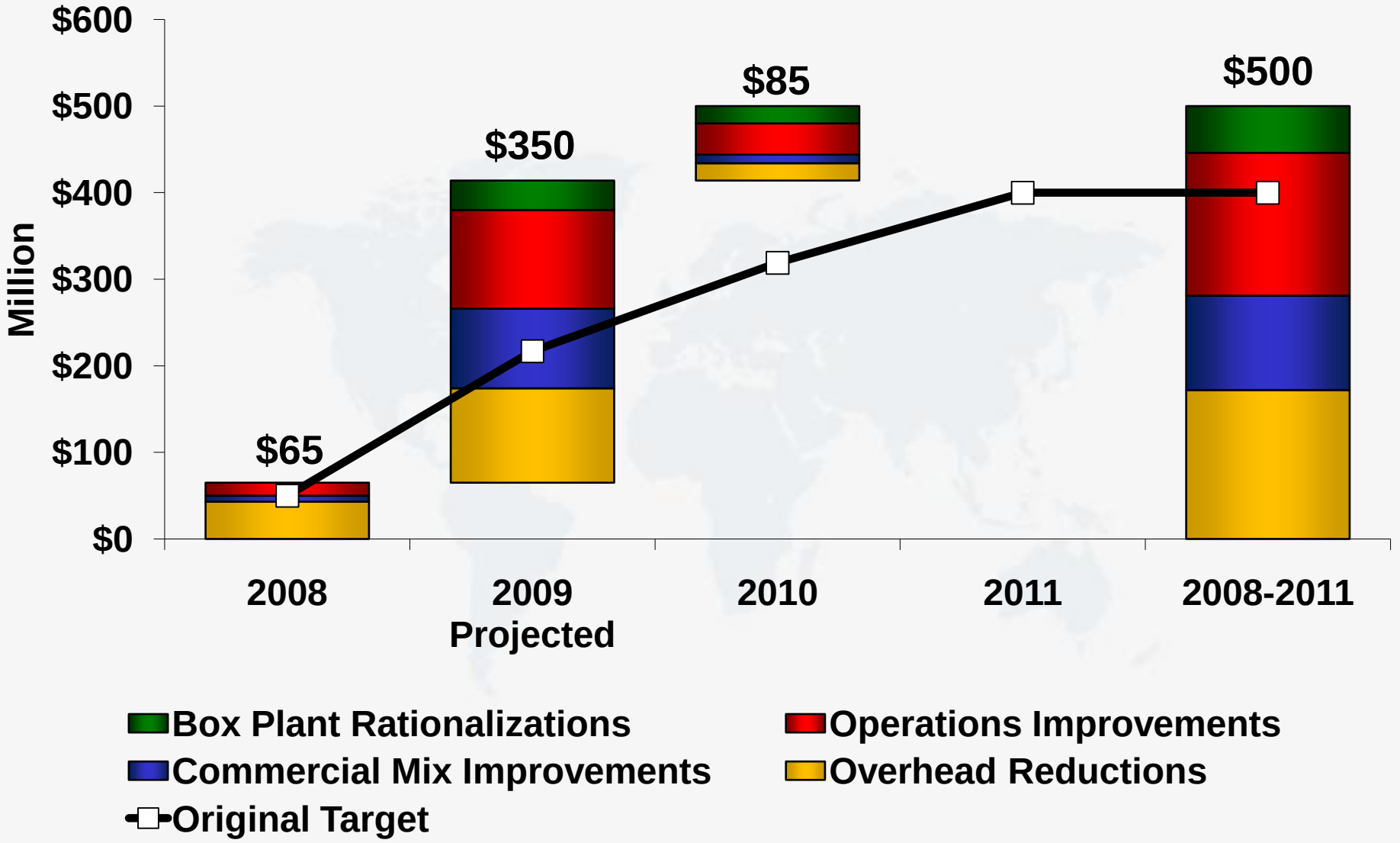
## *Acquisition Exceeding Expectations*

INTERNATIONAL PAPER

| Target | Status |
|---|---|
| Good Strategic Fit | • Enhanced containerboard & box businesses |
| Improves Core Businesses | • Premier North American & global positions |
| Low Integration Risk | • Executing well and quickly |
| Significant Synergies | • More benefits at faster pace |
| Quality Assets | • Low-cost, expanded capability & flexibility<br>• Outstanding people |
| Cash Accretive | • Strong cash flow |

# IP Strategy & Execution

## *Synergies Exceeding Original Target*




Does not include $90 million in procurement synergies

# IP Strategy & Execution

## *Line of Sight to $500 Million in Synergies*

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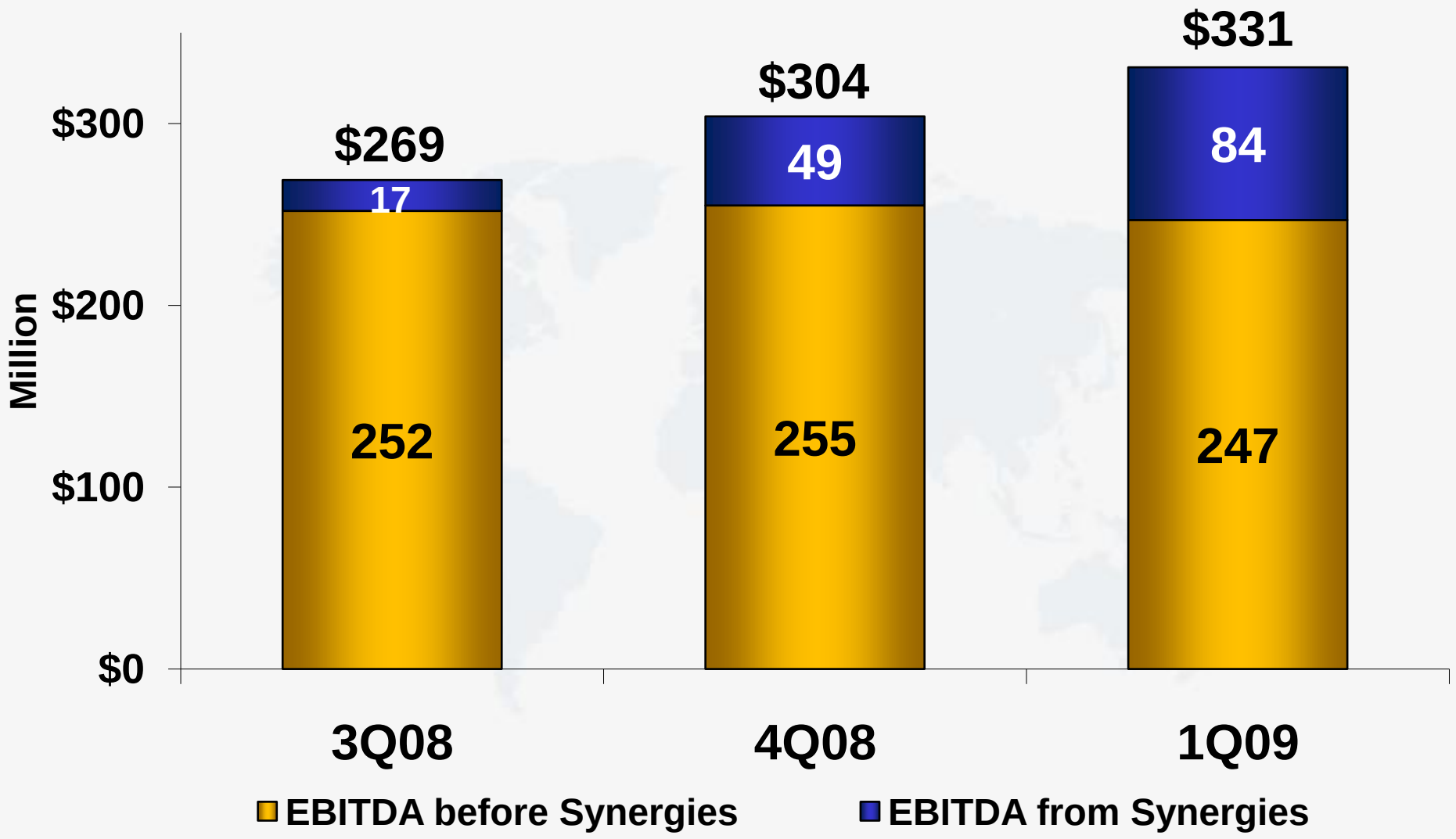
| Category | Synergies ($ Million) | Comments |
|---|---|---|
| Salaried Headcount Reductions | $200 | · Reduced business & corporate headcount by 26% |
| Mill & Box Plant Operations | $120 | · Improved reliability<br>· Increased efficiency<br>· Reduced hourly headcount |
| Box Margins | $105 | · Commercial improvements<br>· Mix improvement<br>· Right-weighting |
| Mill Freight Savings | $40 | · Fewer total miles<br>· Increased weight/load by 15-20% |
| Box Plant Rationalizations | $35 | · 13 plant closures (12 box, 1 sheet)<br>· 96% sales volume retained<br>· Hourly headcount |

Excludes $90 million in procurement synergies

# IP Strategy & Execution

## *Delivering Synergies to Bottom Line*




Earnings before special items.

# IP Strategy & Execution

## *Increased Mill Capacity and Flexibility*

INTERNATIONAL PAPER

| | 2005 | May 2008 | May 2009[1] |
|---|---|---|---|
| **# of Mills** | **8** | **6** | **14** |
| **# of Containerboard Machines** | **13** | **11** | **24** |
| **Average Capacity** (Thousand Tons per Mill) | **610** | **870** | **790** |
| **Mill Headcount** | **2,800** | **2,500** | **4,500** |
| **Total Capacity** (Million Tons) | **4.9** | **5.0** | **11.1** |
| **Capacity** (Tons per Mill Employee) | **1,700** | **2,000** | **2,500** |
| **Recycled as % of Total Capacity** | **20%** | **16%** | **38%** |

[1] Excludes Mexican mill and Valliant #3 machine.

# IP Strategy & Execution

## *80% of Capacity in 1st & 2nd Quartiles*

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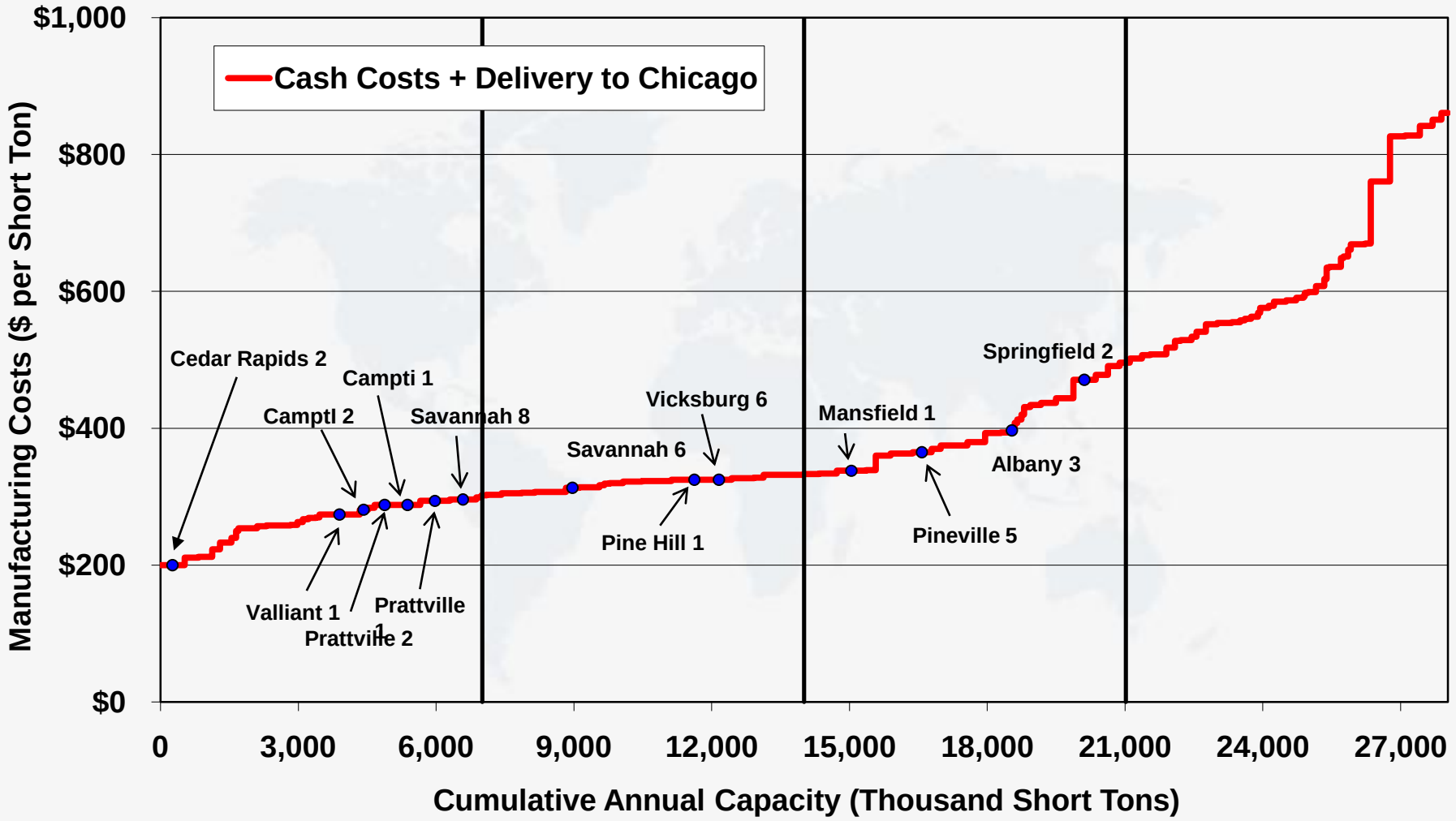
***Identified $200MM incremental improvement over next 3 years***



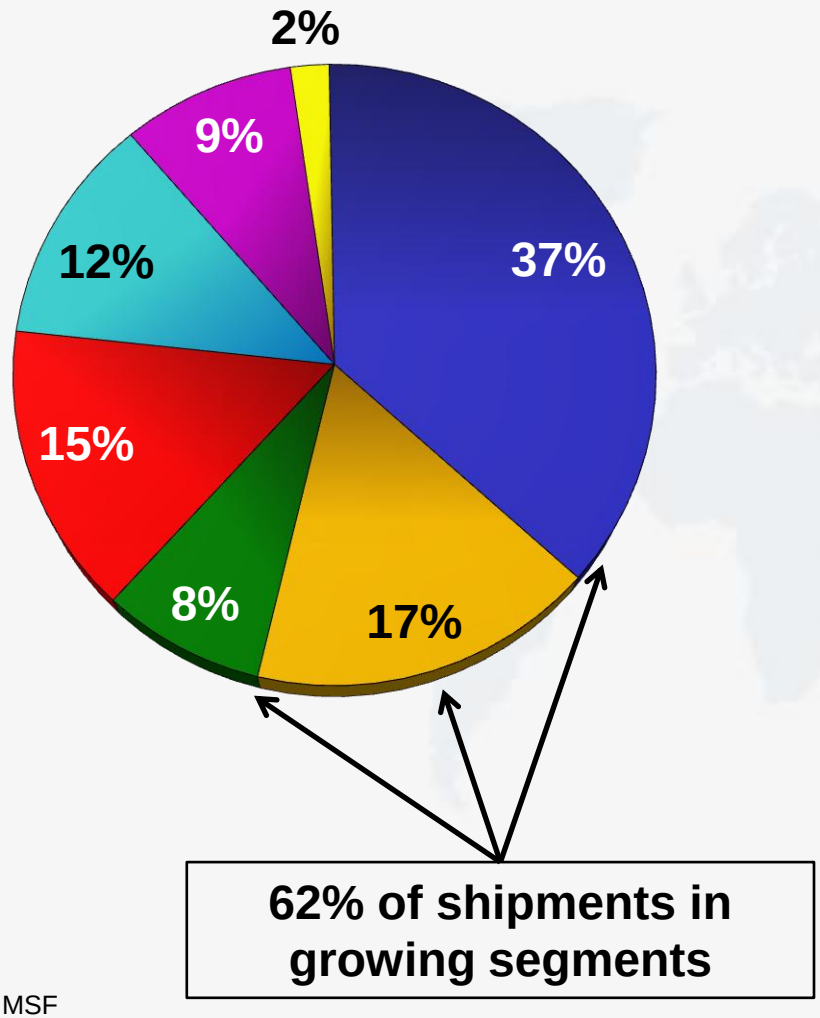

Source: Poyry's 2008 42# Global Kraft Linerboard CostTrac model at 4th quarter input costs and exchange rates.

# IP Strategy & Execution

*Well-Positioned in Attractive Customer Segments*

INTERNATIONAL PAPER

## IP Box Shipments by Segment

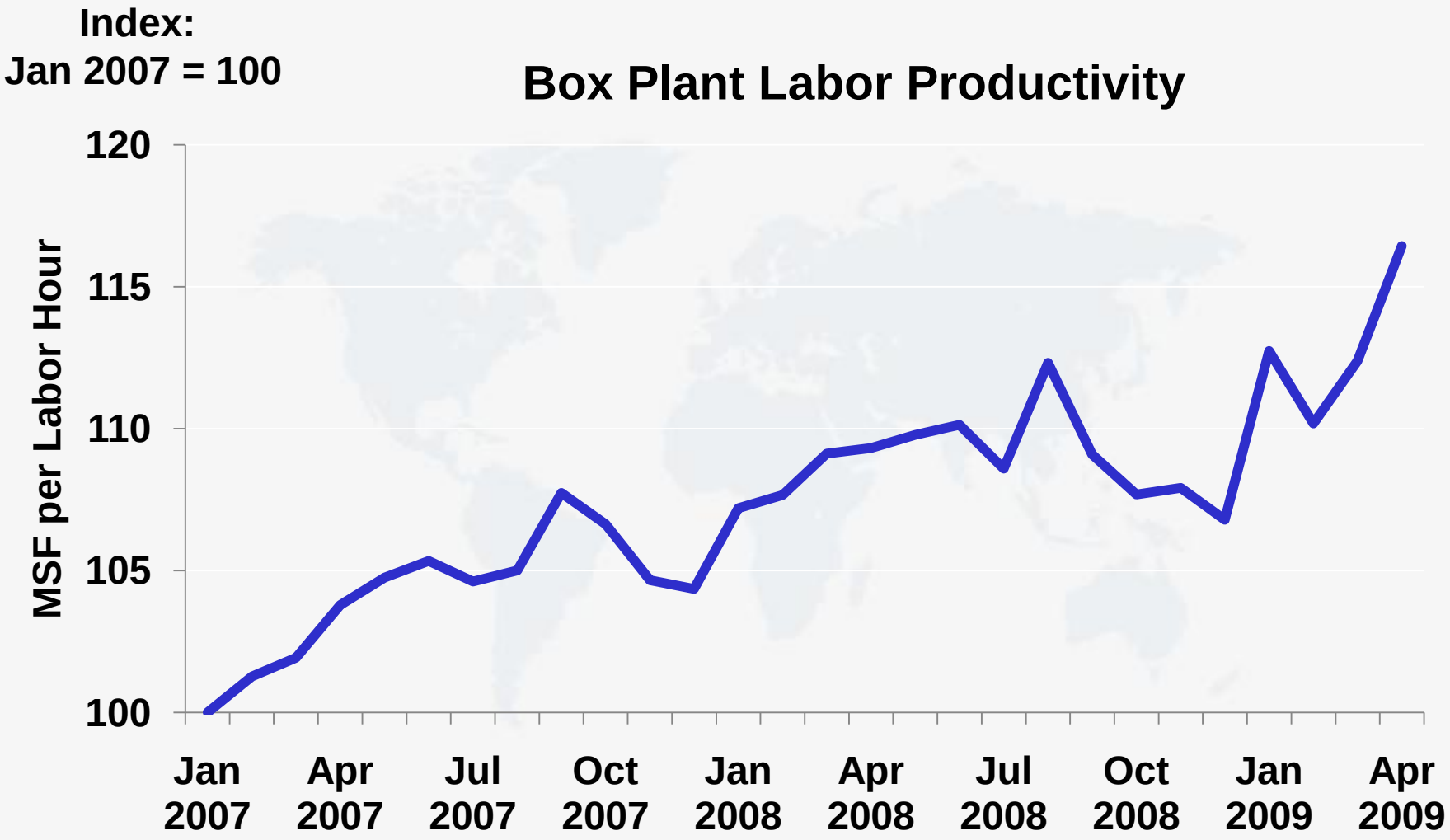



Box shipments in MSF
Source: Fibre Box Association, IP Analysis

# IP Strategy & Execution

*7% Productivity Improvement since Acquisition*

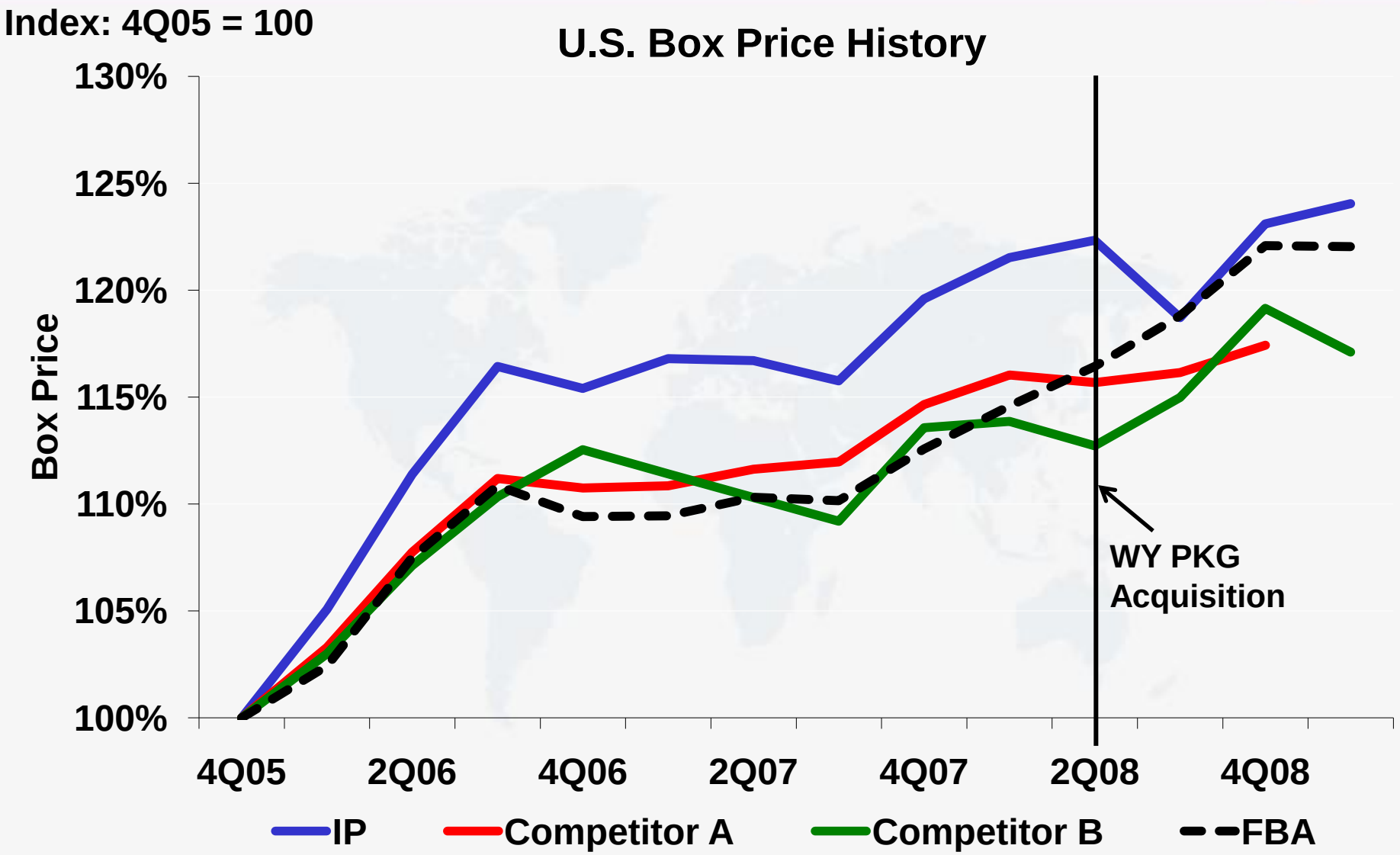
INTERNATIONAL PAPER



# IP Strategy & Execution

## *Continuing to Outperform Industry and Competitors*

INTERNATIONAL PAPER




IP's price is for Fibre Box Association facilities.

Source: Competitors' earnings calls, press releases, and SEC Filings, FBA

# IP Strategy & Execution

## *Successful Box Plant Rationalizations*

INTERNATIONAL PAPER

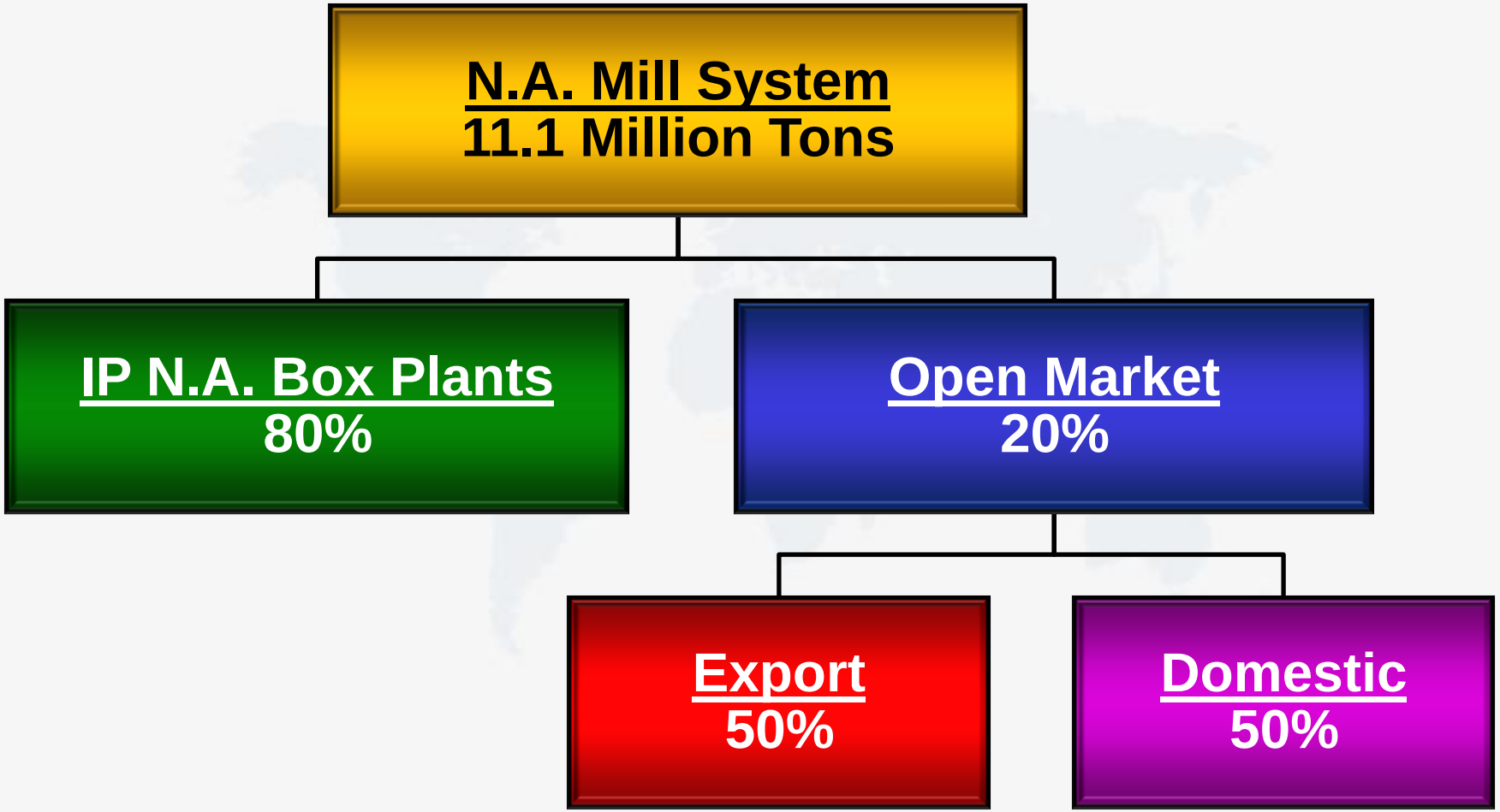
| | |
|---|---|
| **# of Box Plants Closed[1]** | **8** |
| **Customer Retention[2]** | **96%** |
| **S&A Reduction** ($ Million) | **$20** |
| **Variable Cost Reduction** ($ Million) | **$15** |
| **Synergy EBITDA Impact** ($ Million) | **$35** |

[1] Excludes closures of 5 plants that were announced on April 3rd, which are still operating today
[2] Box plant rationalizations

# IP Strategy & Execution

INTERNATIONAL PAPER

***IP's market access provides choices for maximizing value***



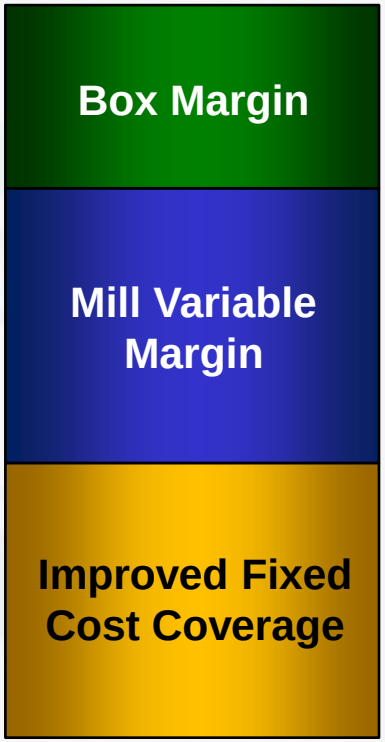
# IP Strategy & Execution

## *Matching Supply to Customer Demand*

INTERNATIONAL PAPER

| | 3Q08 | 4Q08 | 1Q09 |
|---|---|---|---|
| **Lack-of-Order Downtime** (Thousand Tons) | **35** | **640** | **730** |
| **Inventory Change** (Thousand Tons) | **—** | **(75)** | **(110)** |
| **Cost of Downtime**[1] ($ Million) | **$5** | **$75** | **$95** |

**Earnings Potential from Incremental Volume**




[1] Unabsorbed fixed cost

Excludes lost tons at Vicksburg Mill, Valliant #3 and maintenance downtime of 50K, 89K, and 177K in the last three quarters respectively.

# IP Strategy & Execution

## *IP Profit More Sensitive to Price than Volume*

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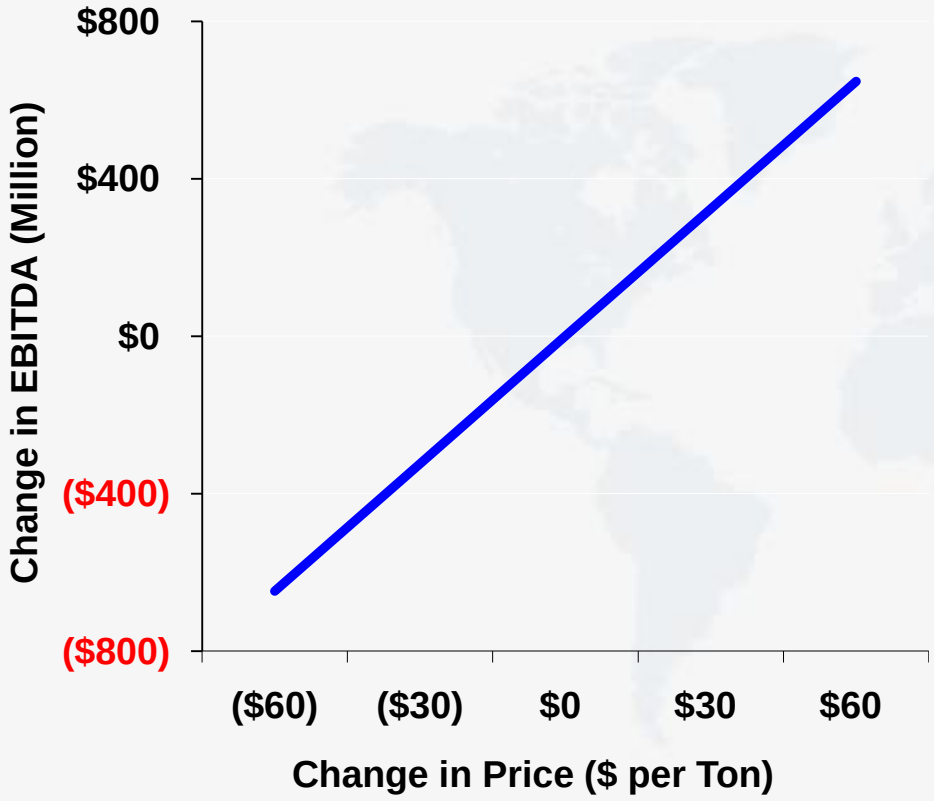
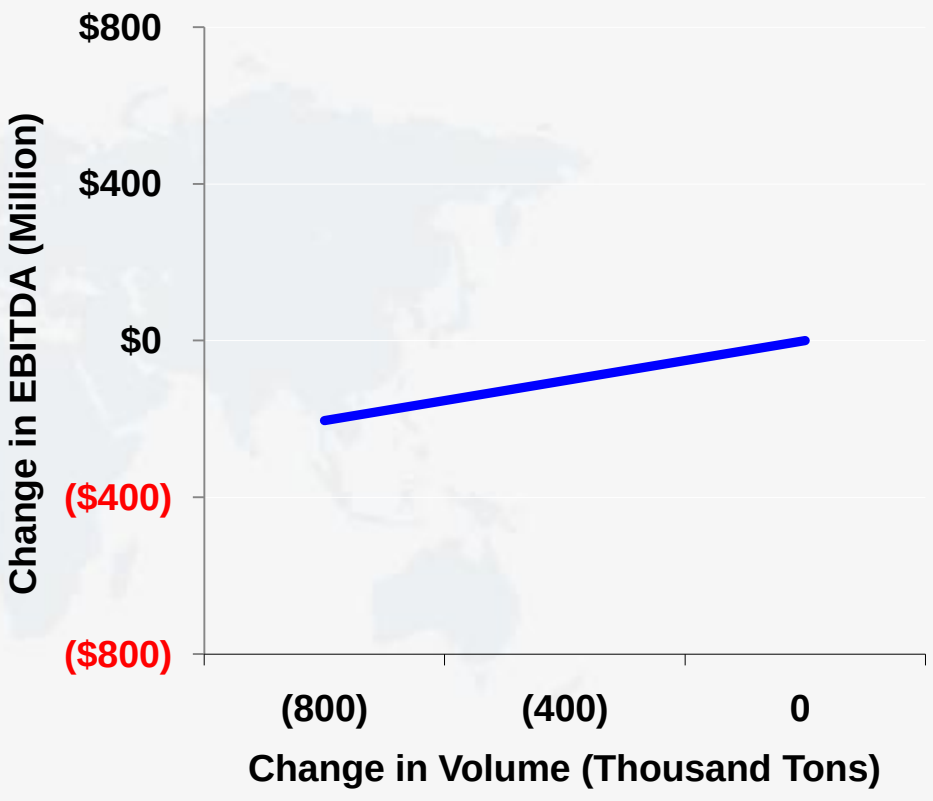
### IP Profit Impact from Change in Price




### IP Profit Impact from Change in Volume



# Financial Performance

## *Outperforming Competitors in 1Q09*

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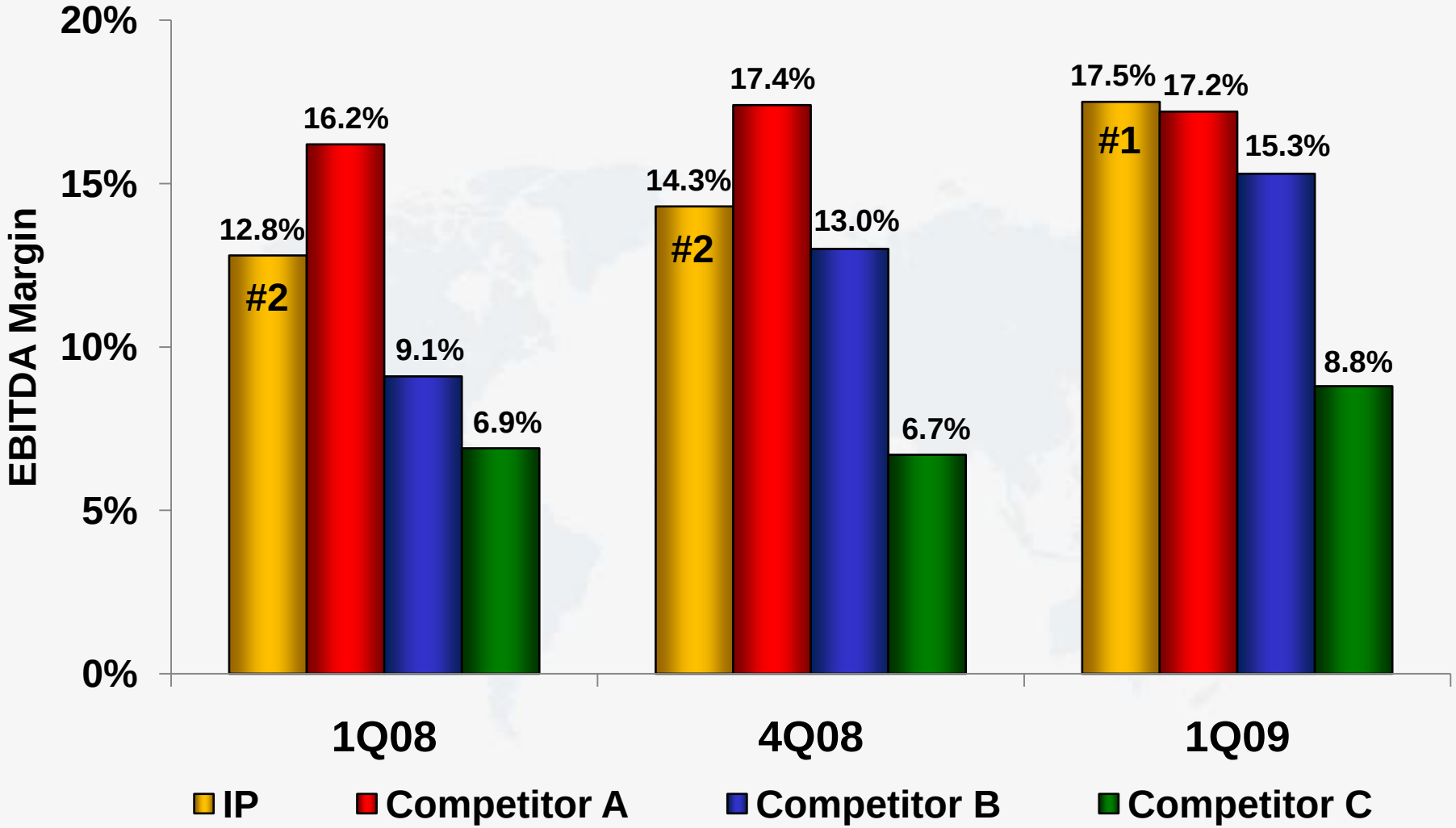
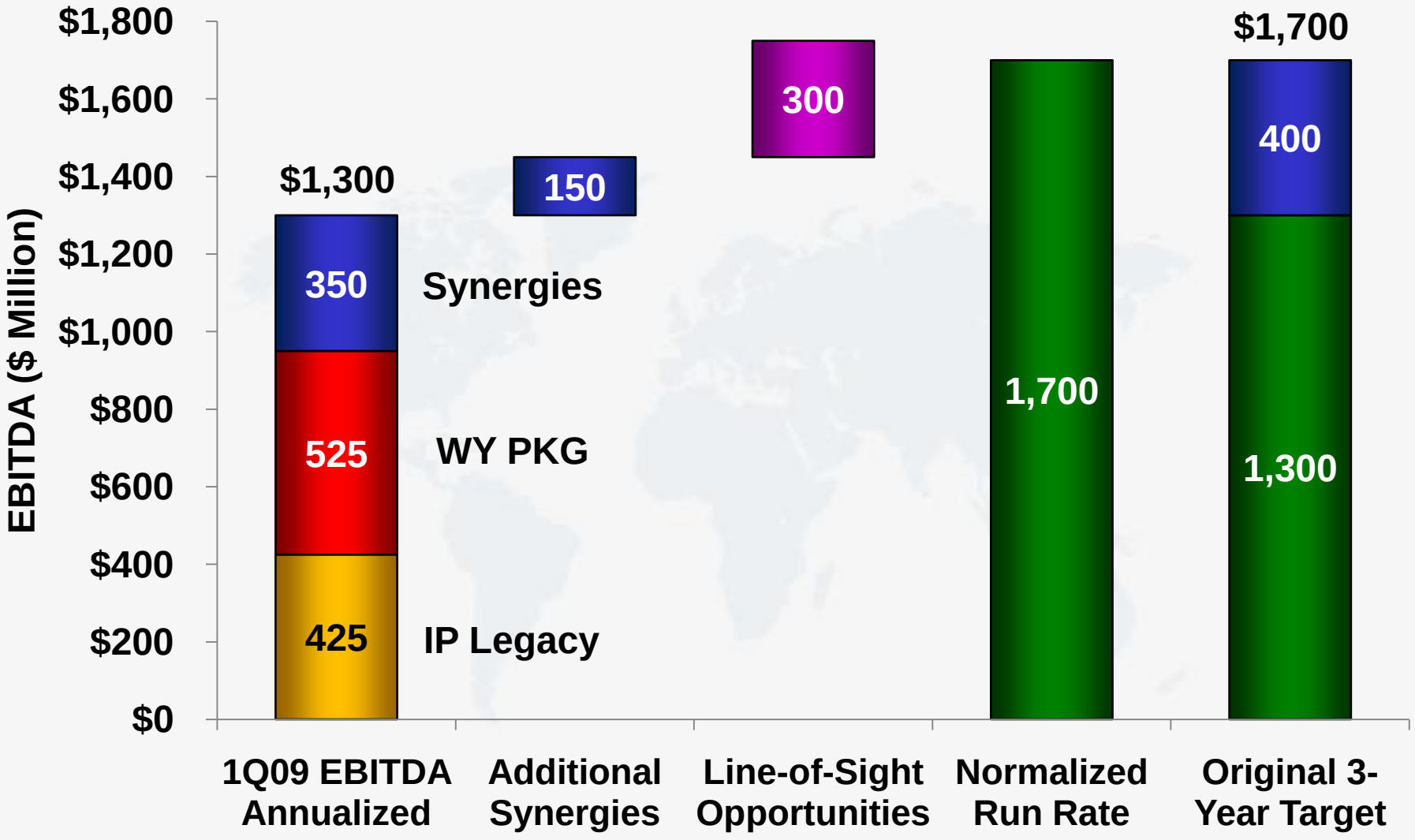



IP EBITDA margins based on North American Industrial Packaging operating profit before special items
Competitor EBITDA margins obtained from public filings and IP analysis

# Financial Performance

## *Line-of-Sight to Reach the Target*




Excludes special items

# IP North American Industrial Packaging

## *Generating Strong Free Cash Flow*

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- **Strategic acquisition exceeding expectations**
- **Greater synergies at faster pace**
- **Strong free cash flow**
- **Line-of-sight to significant upside potential**
- **Pursuing cost-of-capital returns**



INTERNATIONAL PAPER




# Printing & Communications Papers

H. Wayne Brafford
Senior Vice President

# Agenda
## *Transformation Challenges*

INTERNATIONAL PAPER

- **Maximizing Free Cash Flow**
- **Understanding Demand**
- **Managing Supply**
- **Generating Strong Results**

# Maximizing Free Cash Flow

## *Margin Improvement despite Declining Demand*

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| | 2001-05 Average | 2006 | 2007 | 2008 | 1Q09 Run Rate |
|---|---|---|---|---|---|
| **Pulp & Paper Shipments** (Million Tons) | **5.5** | **5.0** | **5.0** | **4.7** | **3.8** |
| **EBITDA** ($ Billion) | **$0.4** | **$0.6** | **$0.8** | **$0.7** | **$0.5** |
| **Pulp & Paper EBITDA Margin** | **10%** | **15%** | **19%** | **16%** | **14%** |
| **Paper-Only EBITDA Margin** | **11%** | **17%** | **19%** | **19%** | **19%** |

# Maximizing Free Cash Flow

## *Strategy*

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- **Maintain low-cost position**
- **Continue manufacturing excellence**
- **Reduce overhead and headcount**
- **Reduce capital spending & working capital**
- **Innovate cost-effectively**

# Maximizing Free Cash Flow

## *Fewer, Larger, Low-Cost Mills*

INTERNATIONAL PAPER

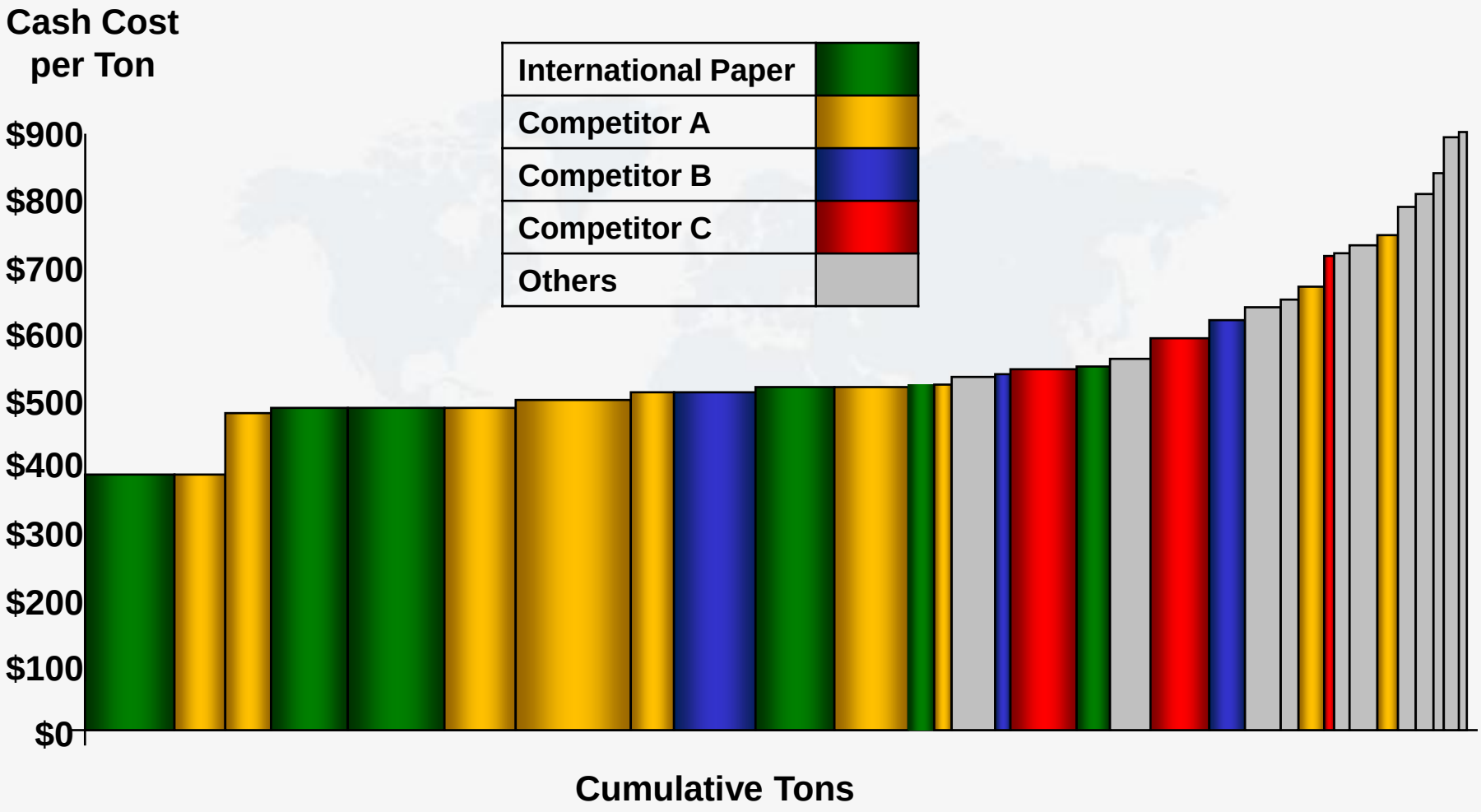
| | 2000 | 2005 | 2009 |
|---|---|---|---|
| **# of Mills** | **12** | **9** | **6** |
| **# of Pulp & Paper Machines** | **43** | **24** | **19** |
| **Average Capacity (Tons/Day)** | **400** | **600** | **650** |
| **Headcount** | **13,000** | **7,700** | **6,200** |
| **Total Pulp & Paper Capacity** (Million Tons) | **6.2** | **5.2** | **4.4** |
| **Capacity per Employee** | **475** | **675** | **710** |

# Maximizing Free Cash Flow

## *IP Commodity Mills Well-Positioned*

INTERNATIONAL PAPER

### 4Q08 North American Cash Cost Curve for UFS Rolls




Source: Poyry, IP Technology, P&C Strategic Planning

# Maximizing Free Cash Flow

## *Continuous Cost Reduction*

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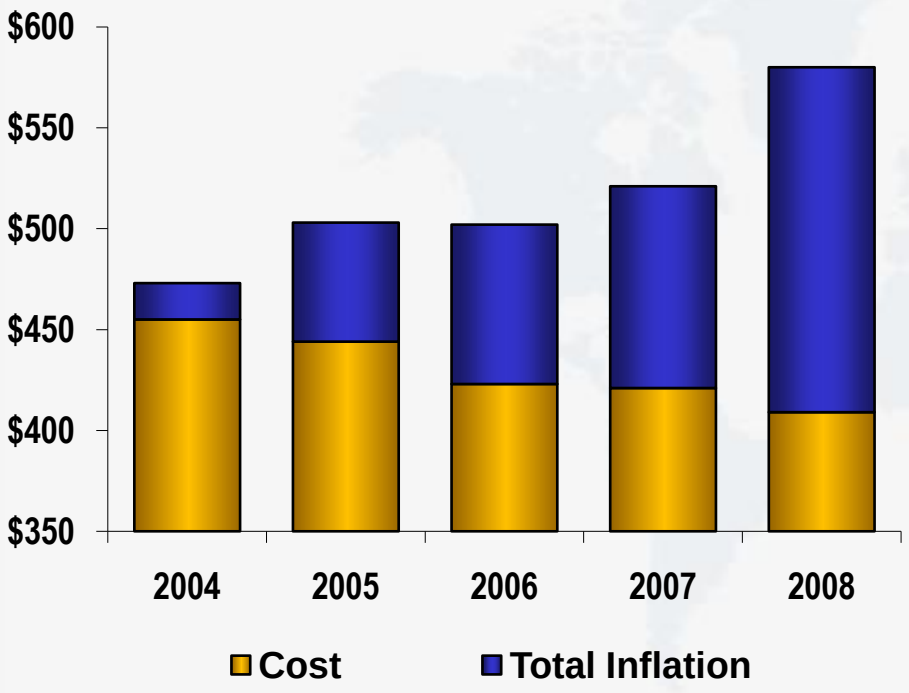
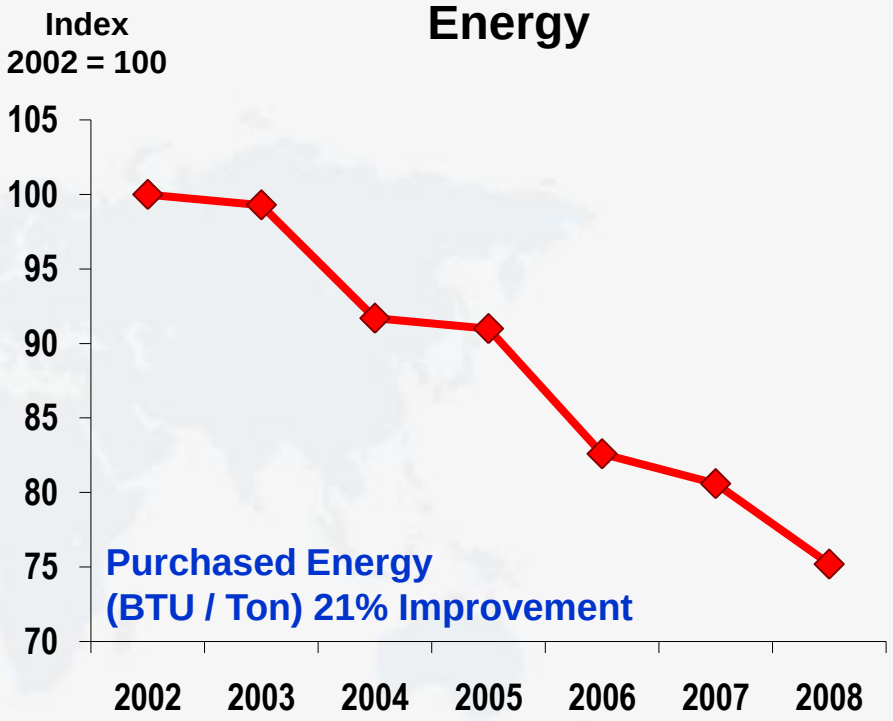
### Manufacturing Cost / Ton




### Energy



# Maximizing Free Cash Flow

## *Driving Lower Overhead & Headcount*

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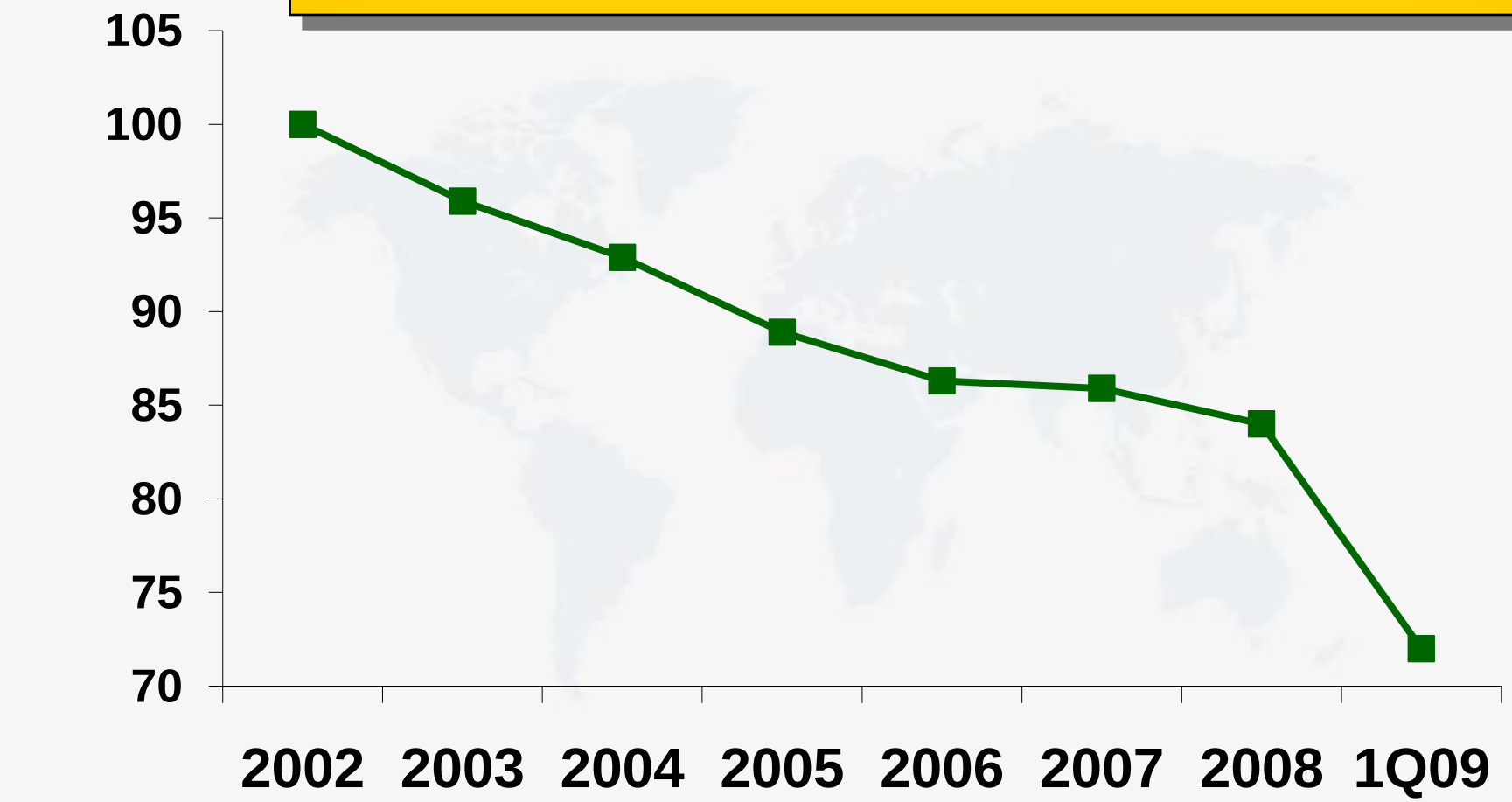
**Total Headcount Improvement of 28%**



# Maximizing Free Cash Flow

## *Reducing Working Capital & Capex*

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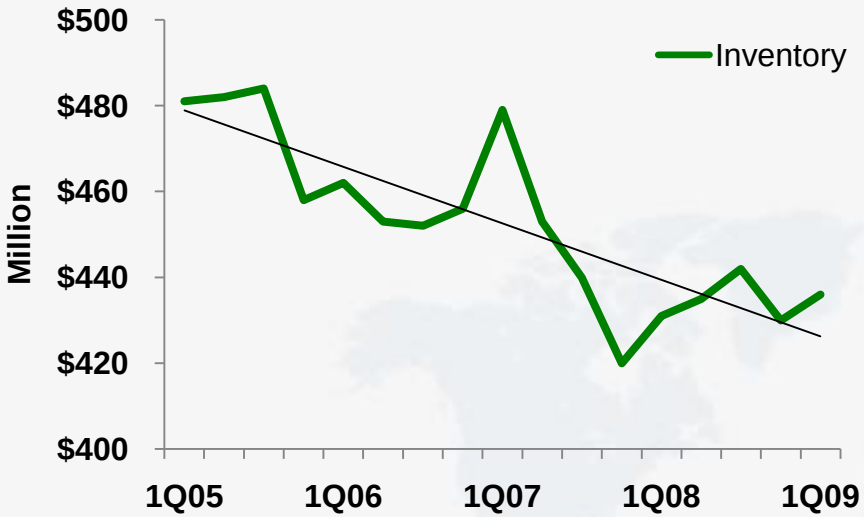


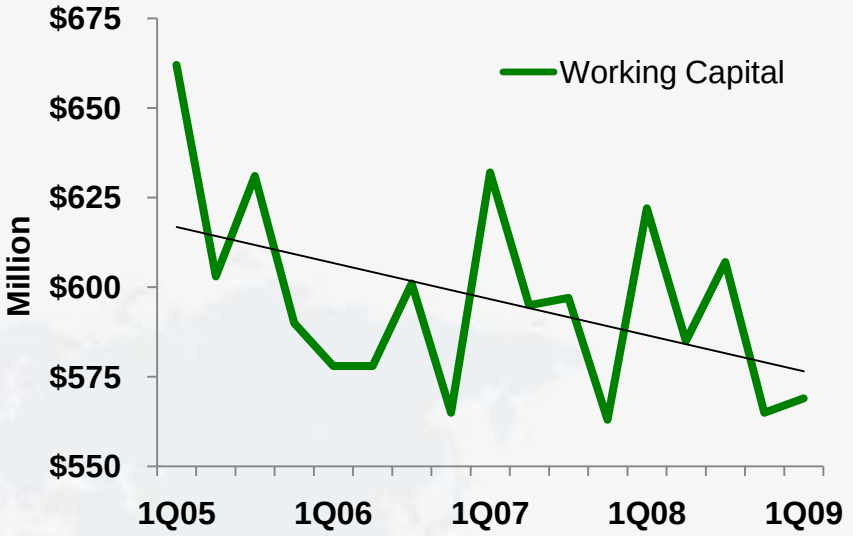


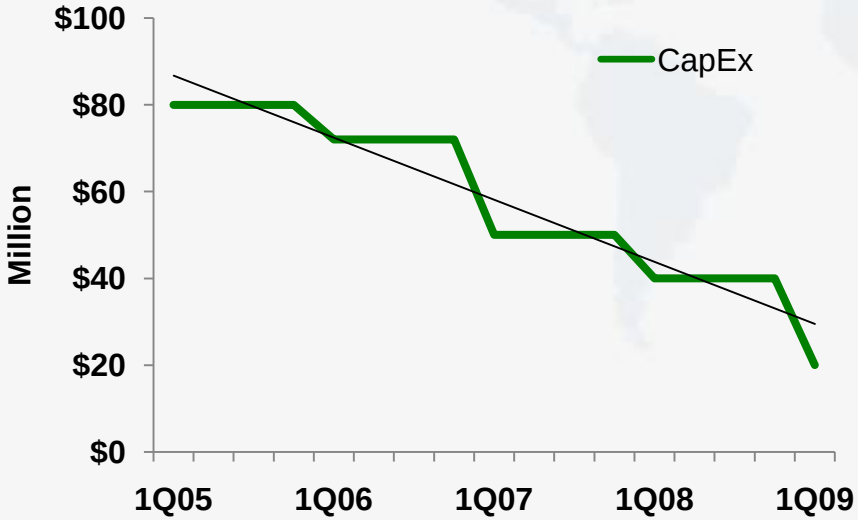


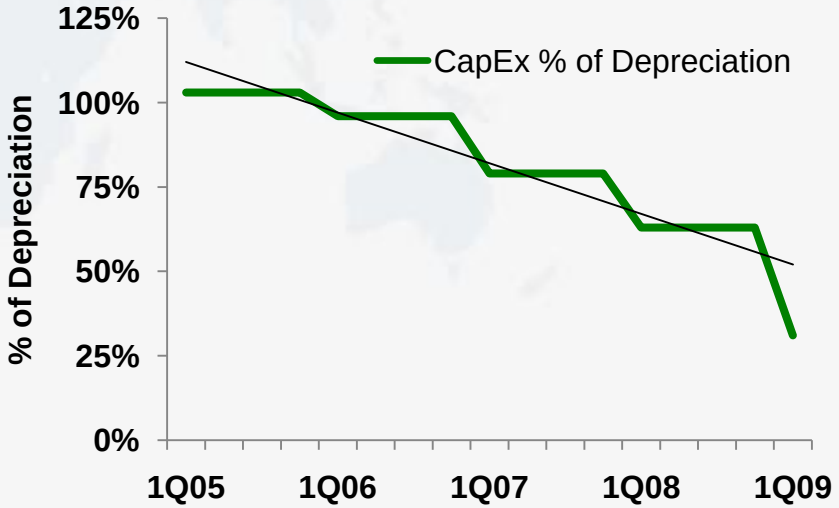

# Maximizing Free Cash Flow

## *Ongoing Commitment to Innovation*

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**Products**

- **VIP**
- **ColorLok**

**Brands**

- **Hammermill – North America**
- **Hewlett-Packard – Global**

# Understanding Demand

## *N.A. UFS Purchases vs. GDP*

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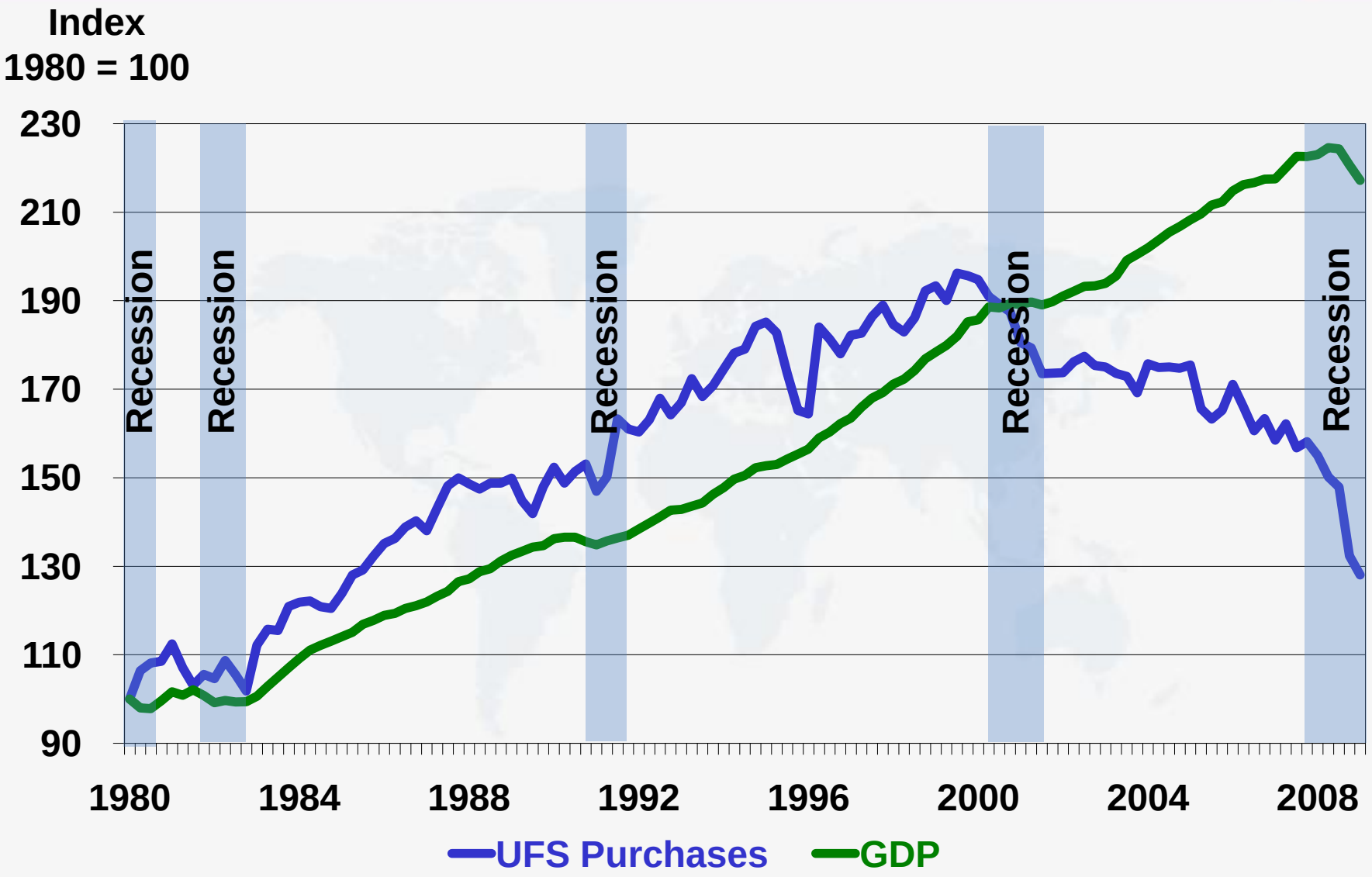
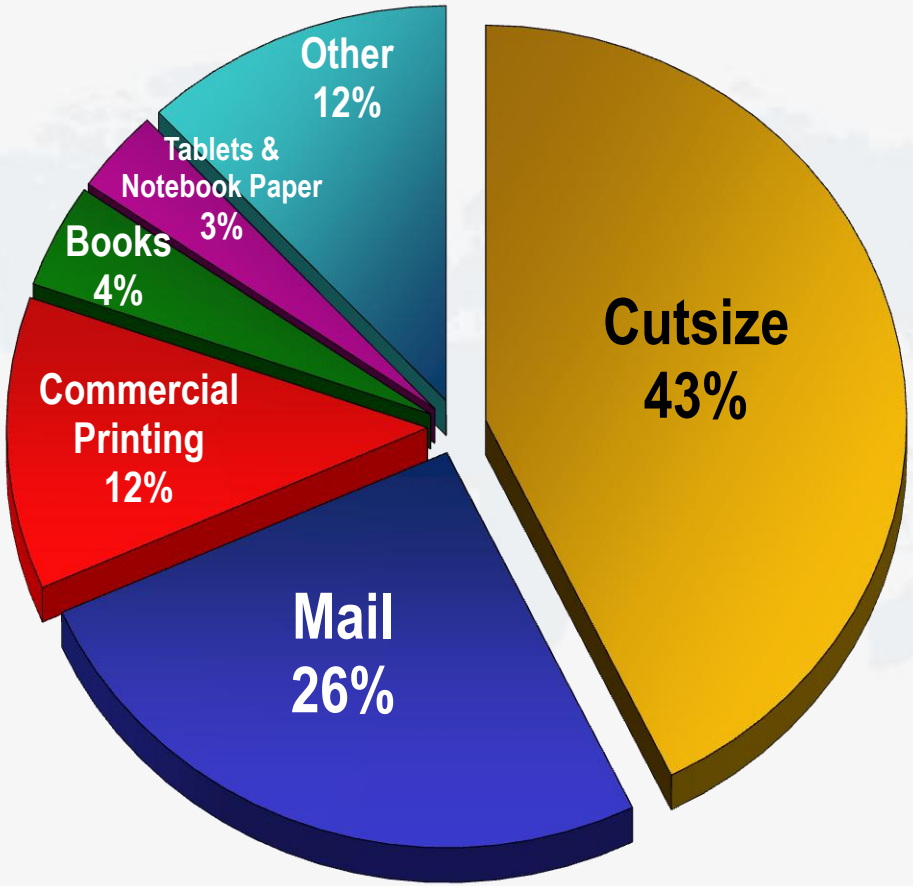



Source: AF&PA, PPPC, BEA, IP Strategic Planning

# Understanding Demand
## *UFS End Use Indicators*

INTERNATIONAL PAPER

***Cutsize & Mail Represent the Majority of UFS***




Source: AF&PA, PPPC, IP Strategic Planning.

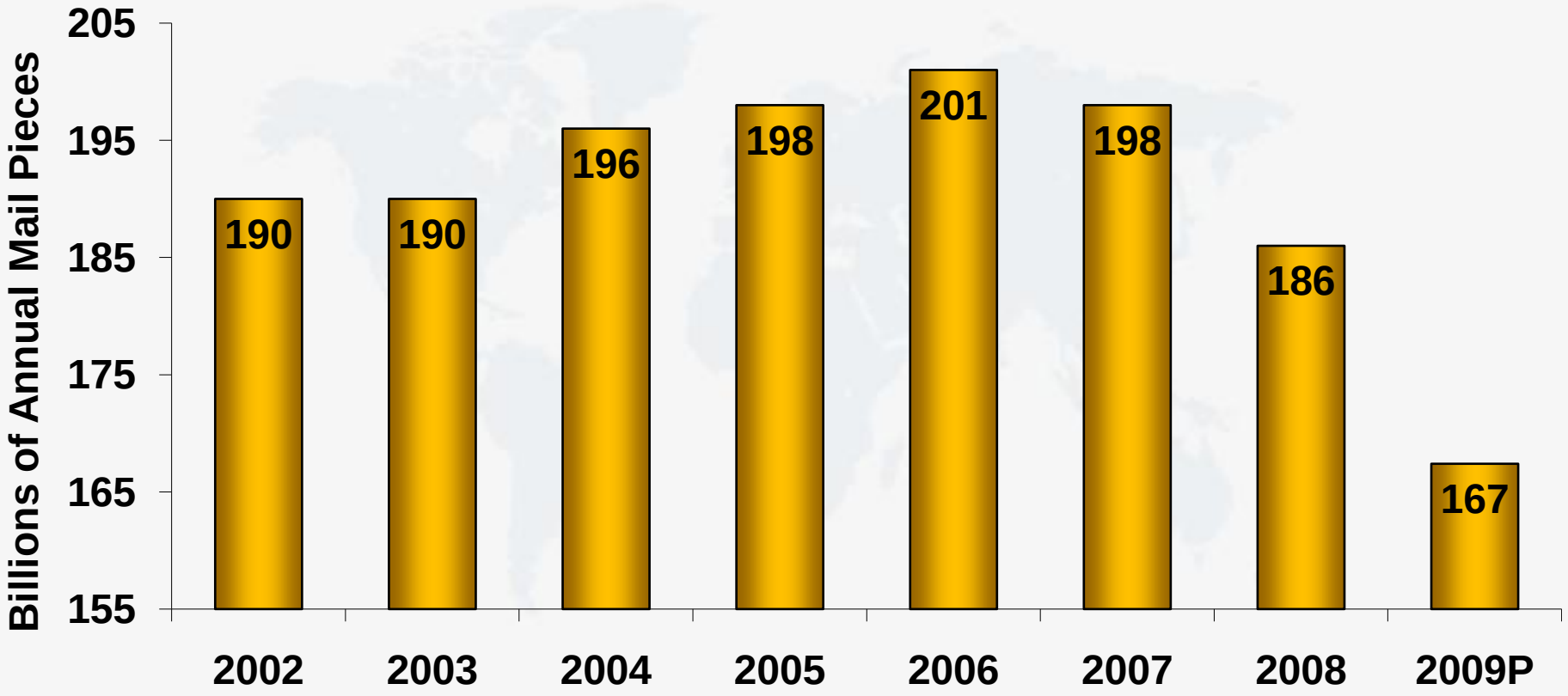
# Understanding Demand

## *Weak Economy Accelerating Mail Decline*

INTERNATIONAL PAPER

***2008 Mail Volume Down 6%***

***2009 Projected Mail Volume Down 10%***




Source: USPS, IP Strategic Planning

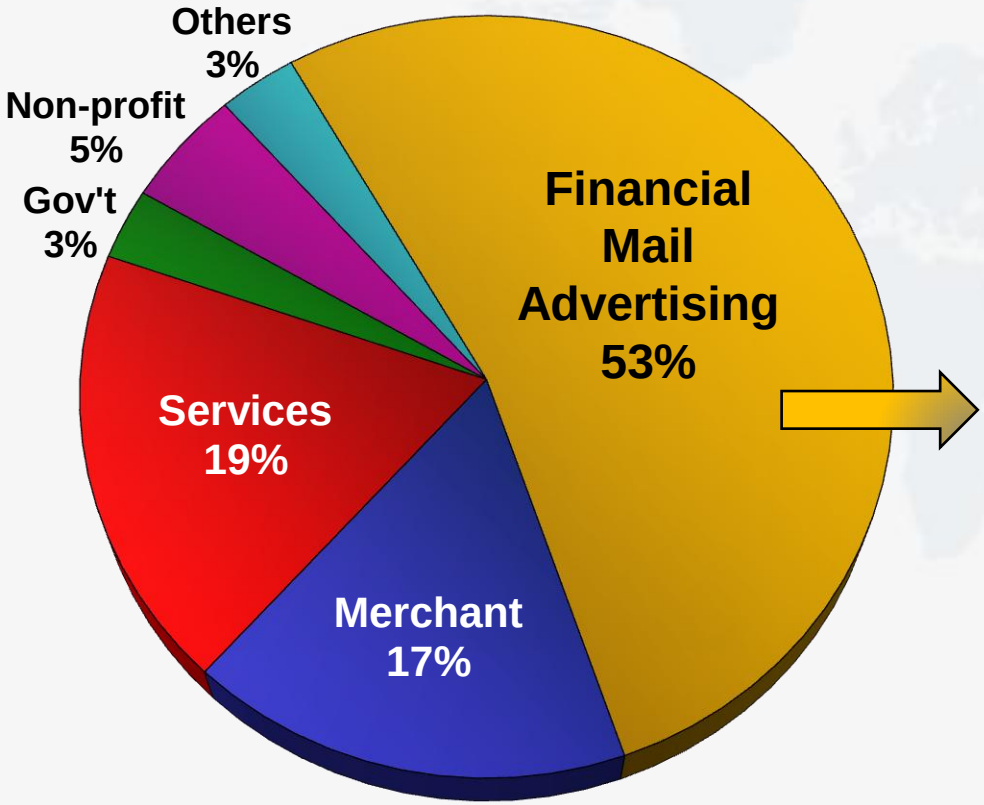
# Understanding Demand

## *Financial Services > 50% of Mail*

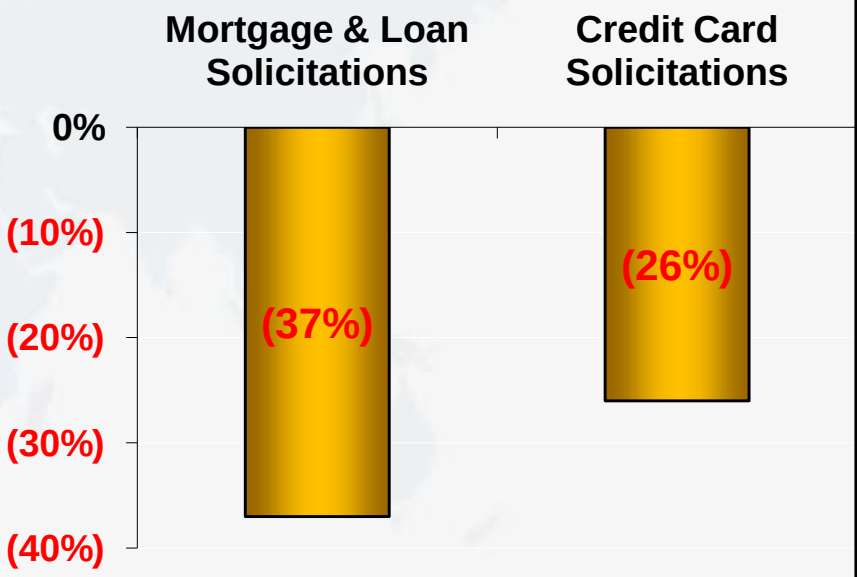
INTERNATIONAL PAPER

***All Mail Down (6%), But Especially Financial Ad Mail***

**2007 Business Mail Pieces**




**Financial Ad Mail**
**2008 vs. 2007**




Source: 2008 USPS Household Diary Study and 2008 Revenue, Pieces, Weight Report, Mintel Compremedia

# Understanding Demand
## *UFS Cutsize Consumption*

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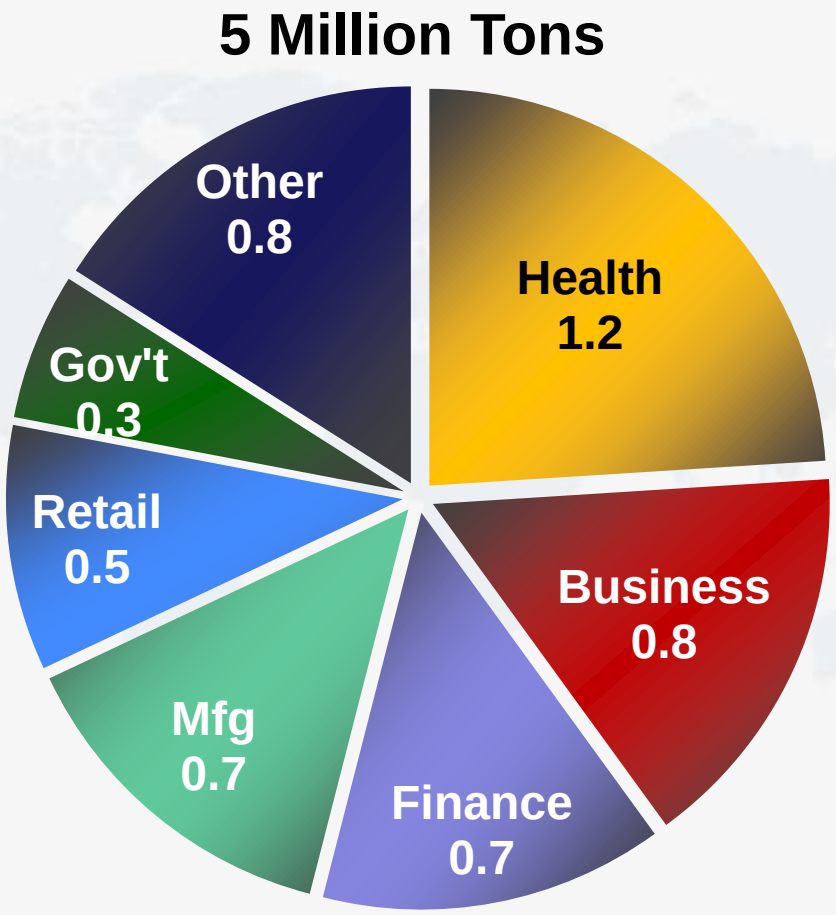
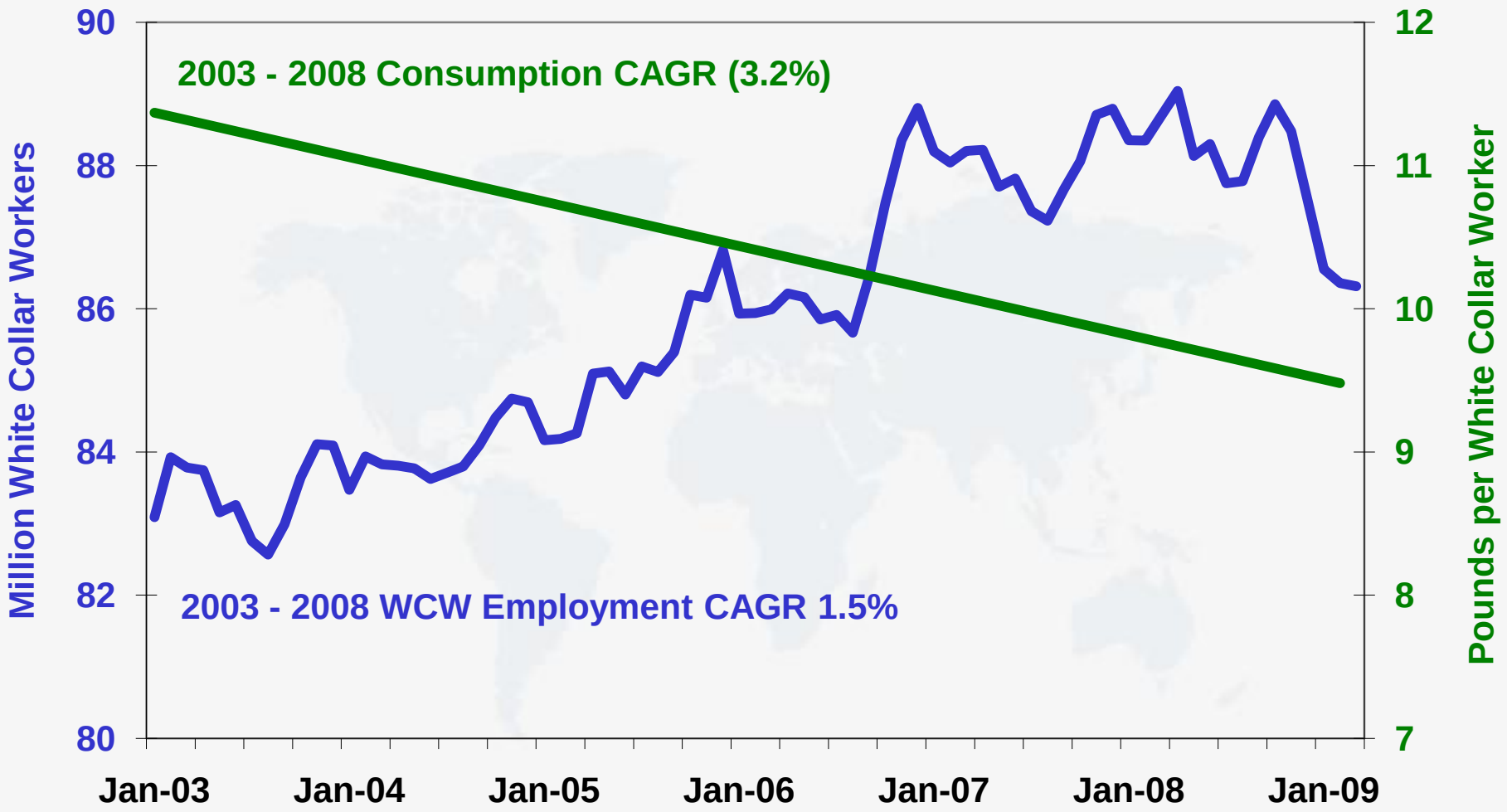
***UFS Cutsize Driven By White Collar Industries***




Source: AF&PA, 2006 InfoTrends, 2007 BLS Employment Forecast

# Understanding Demand

## *Consumption per WCW Suggests 1.7% Decline*




Source: AF&PA, US Census Bureau, IP Strategic Planning

# Understanding Demand

*>2/3 of Current Decline Likely Driven by the Economy*

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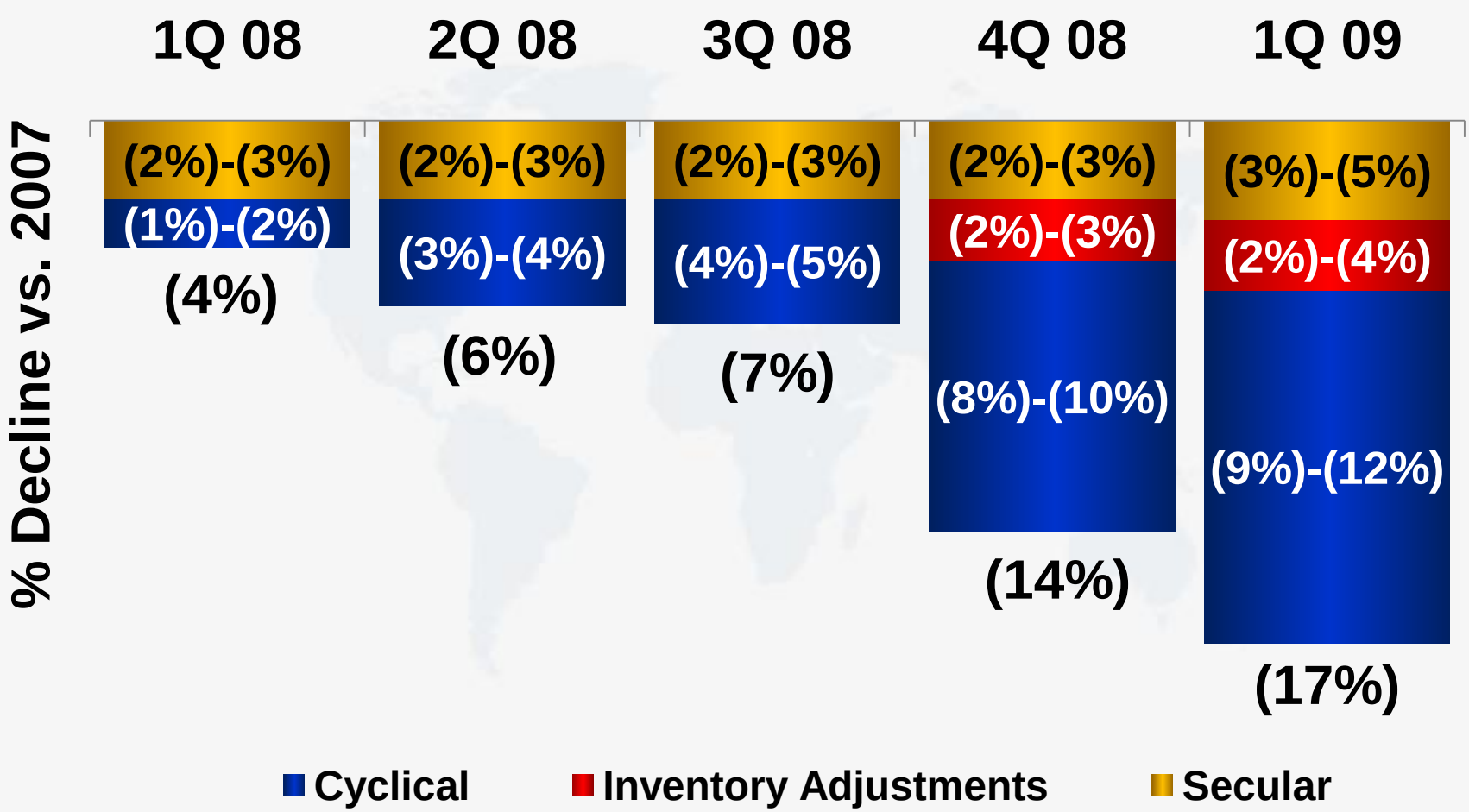
## North American Uncoated Freesheet Demand Decline




Source: AF&PA, PPPC, NPTA, EMA, IP Strategic Planning.

# Understanding Demand

## *Growth Rates Slowing Across All Regions*

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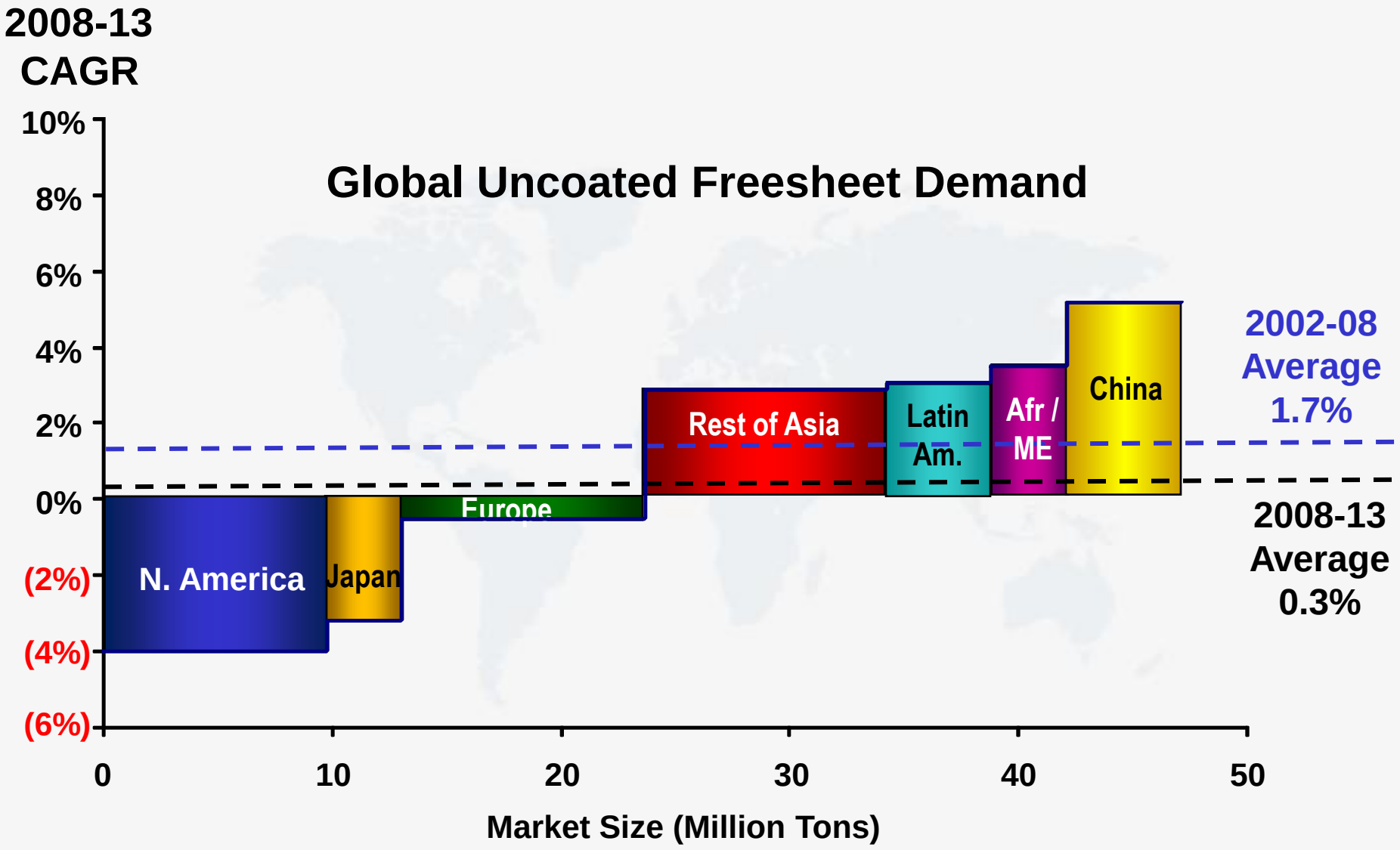


Source: Poyry Consulting, RISI, PPPC, IP Strategic Planning, IP Europe, IP Brazil, IP Asia

# Understanding Demand

## *N.A. Consumption Adjusting*

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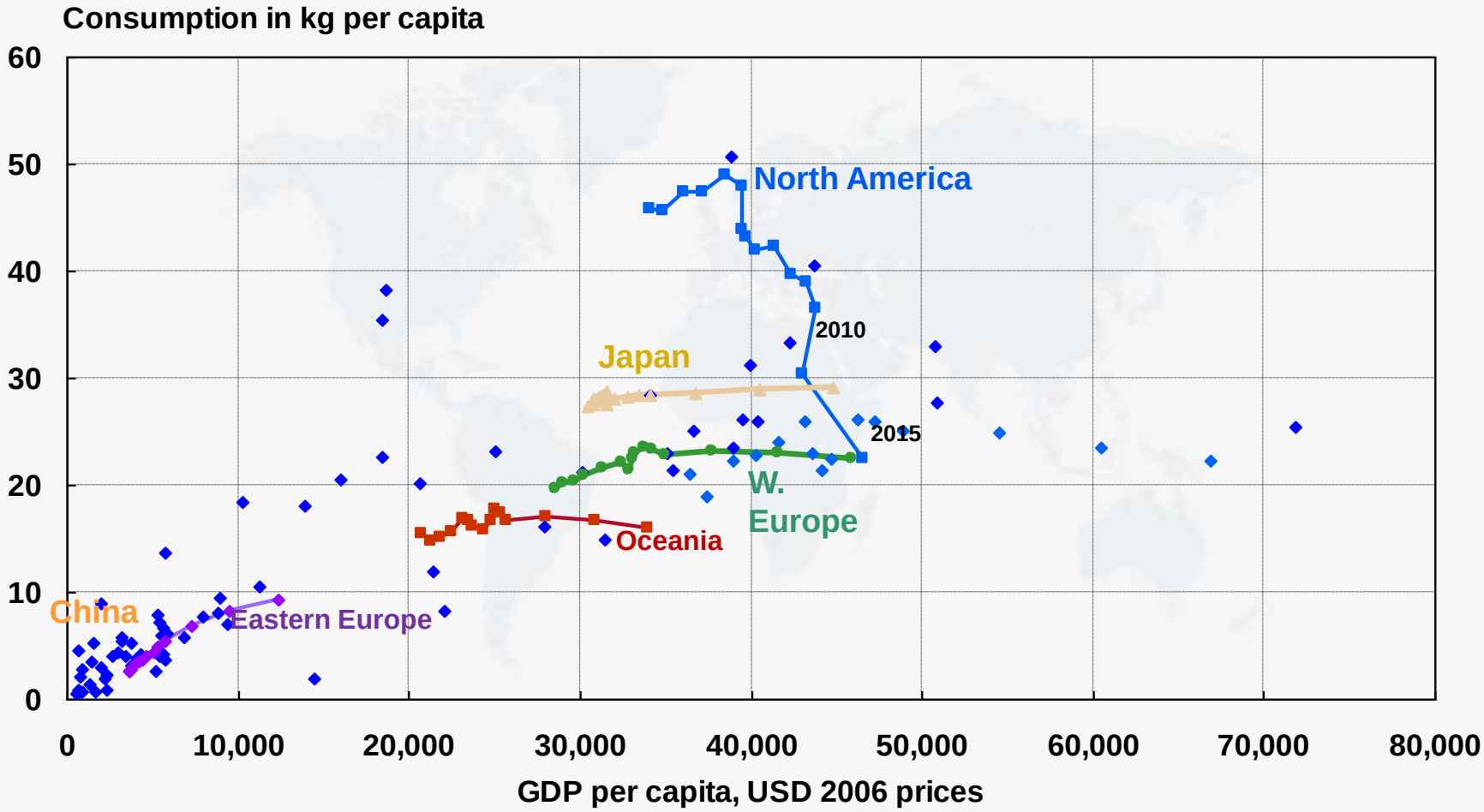
**At Western Europe's per capita consumption, North American demand will be 9 million tons/year**




Source: Poyry Consulting, regional times series 1995 – 2006 plus forecasts through 2015

# Managing Supply
## *Structural Changes*

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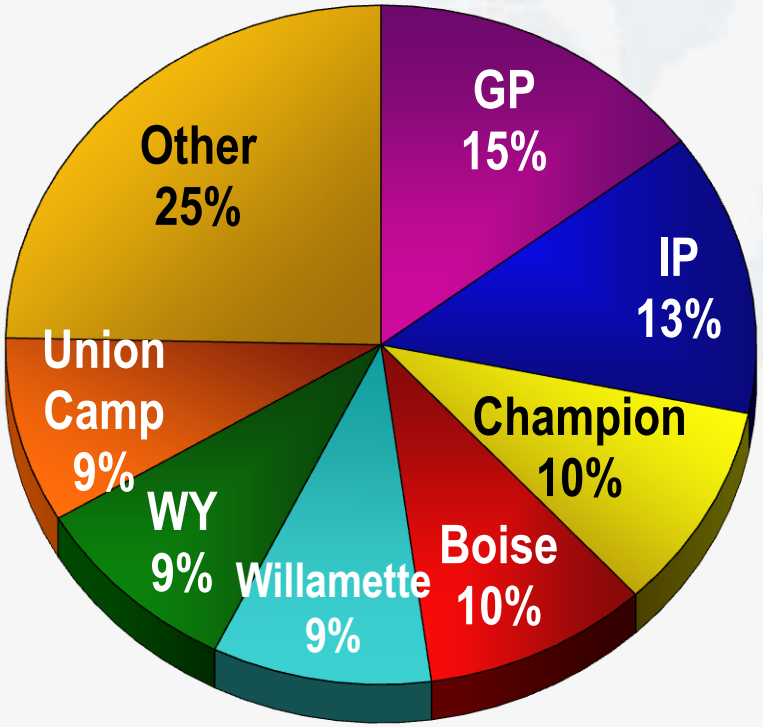
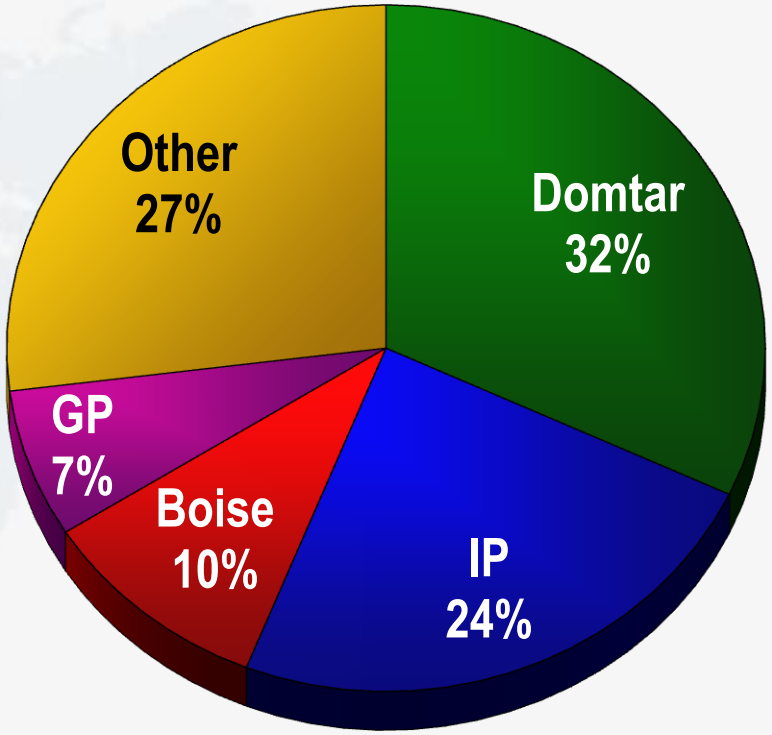
**1998 Producer Position**
**Top 2 = 28%**
**Top 4 = 48%**




**2008 Producer Position**
**Top 2 = 56%**
**Top 4 = 73%**




1998 Source: Poyry Consulting, IP Strategic Planning

2008 Source: RISI

# Managing Supply
## *2000-2009*

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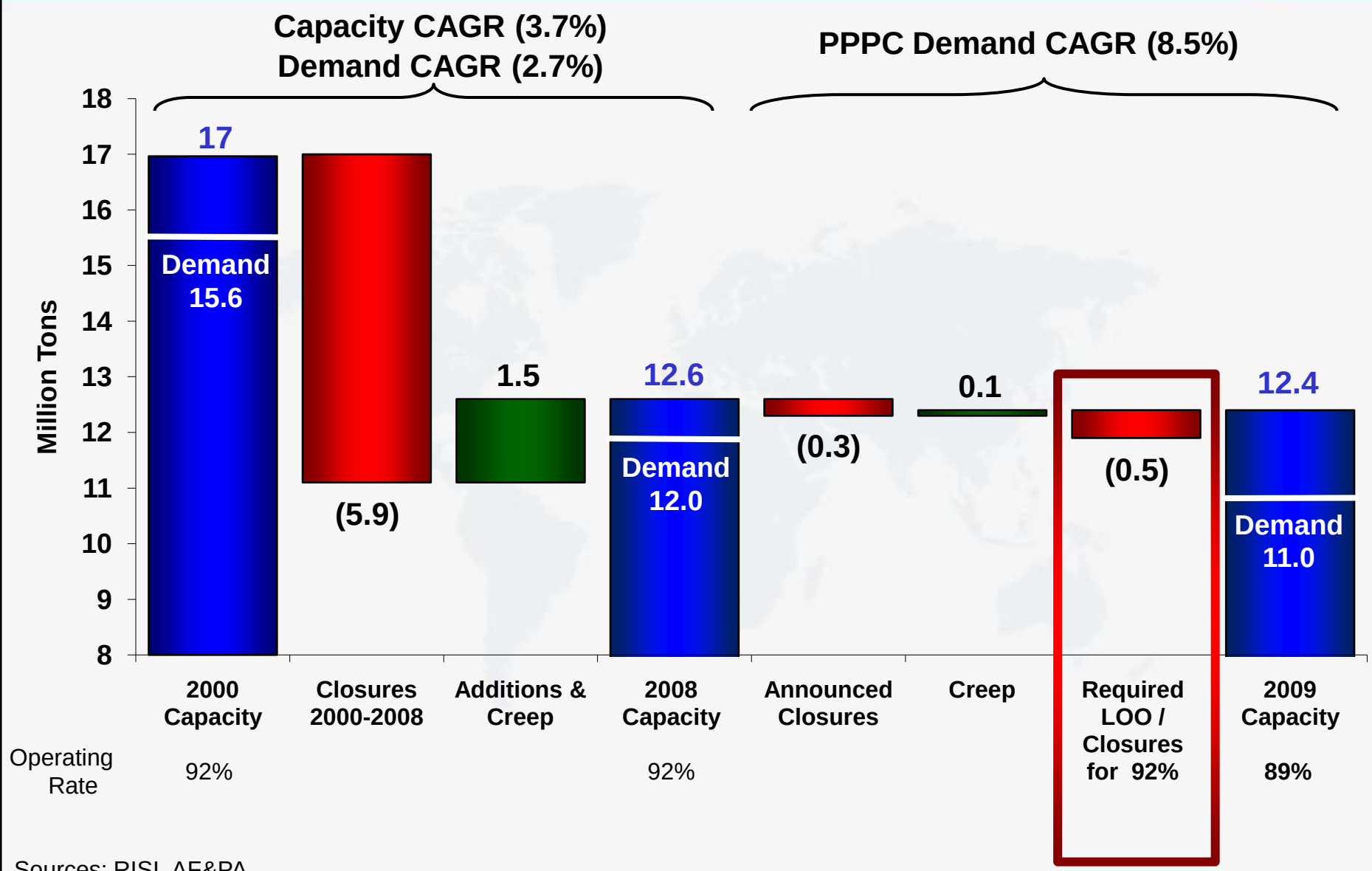


Sources: RISI, AF&PA

# Managing Supply

## *IP Profit More Sensitive to Price than Volume*

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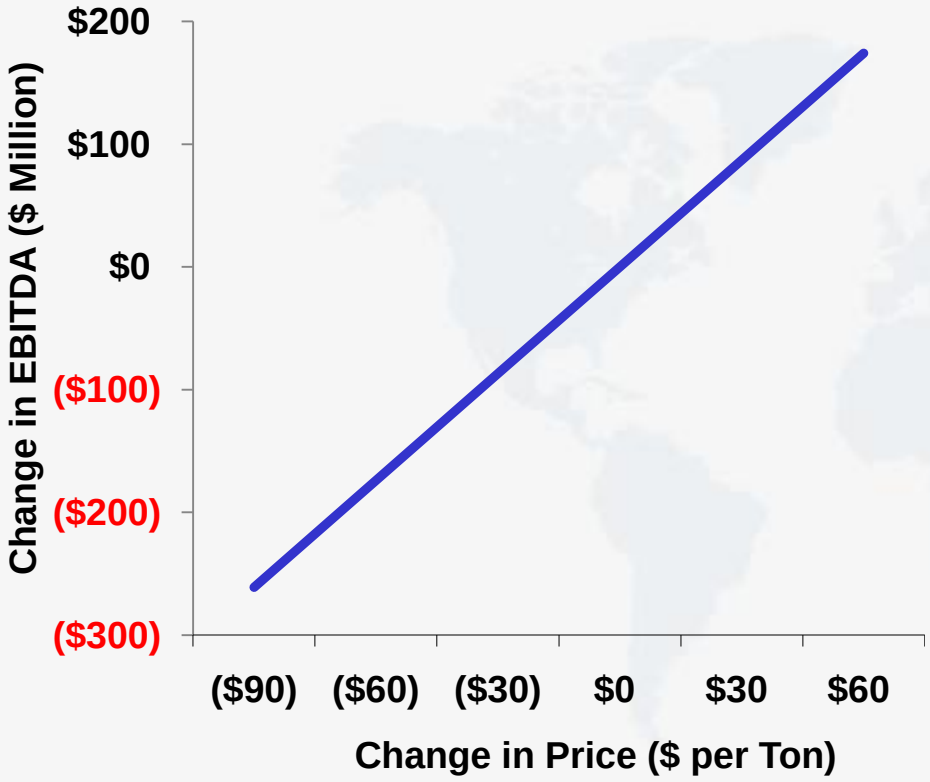
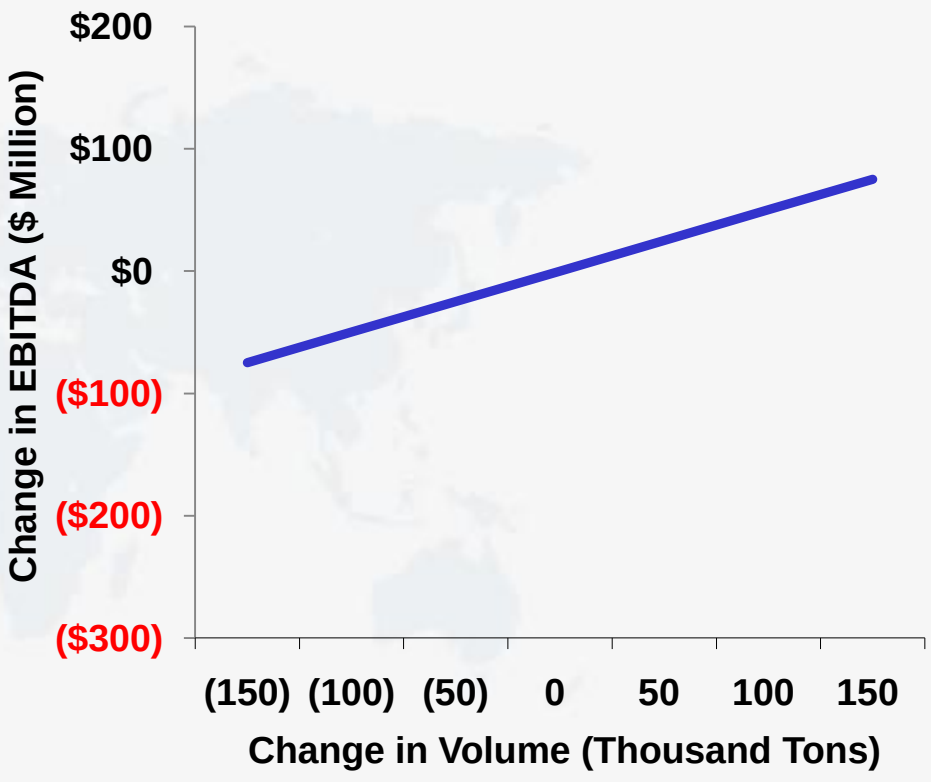
### IP Profit Impact from Change in Price




### IP Profit Impact from Change in Volume



# Managing Supply

## *Matching Supply with Customer Demand*

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| | 3Q08 | 4Q08 | 1Q09 |
|---|---|---|---|
| **Paper (All Grades) Lack-of-Order Downtime** (Thousand Tons) | **5** | **127** | **152** |
| **Inventory Change** (Thousand Tons) | **(30)** | **(1)** | **(4)** |
| **Cost of Downtime[1]** ($ Million) | **$1** | **$24** | **$36** |

[1] Unabsorbed fixed cost

# Managing Supply

## *N.A. Cutsize Price vs. UFS Consumption*

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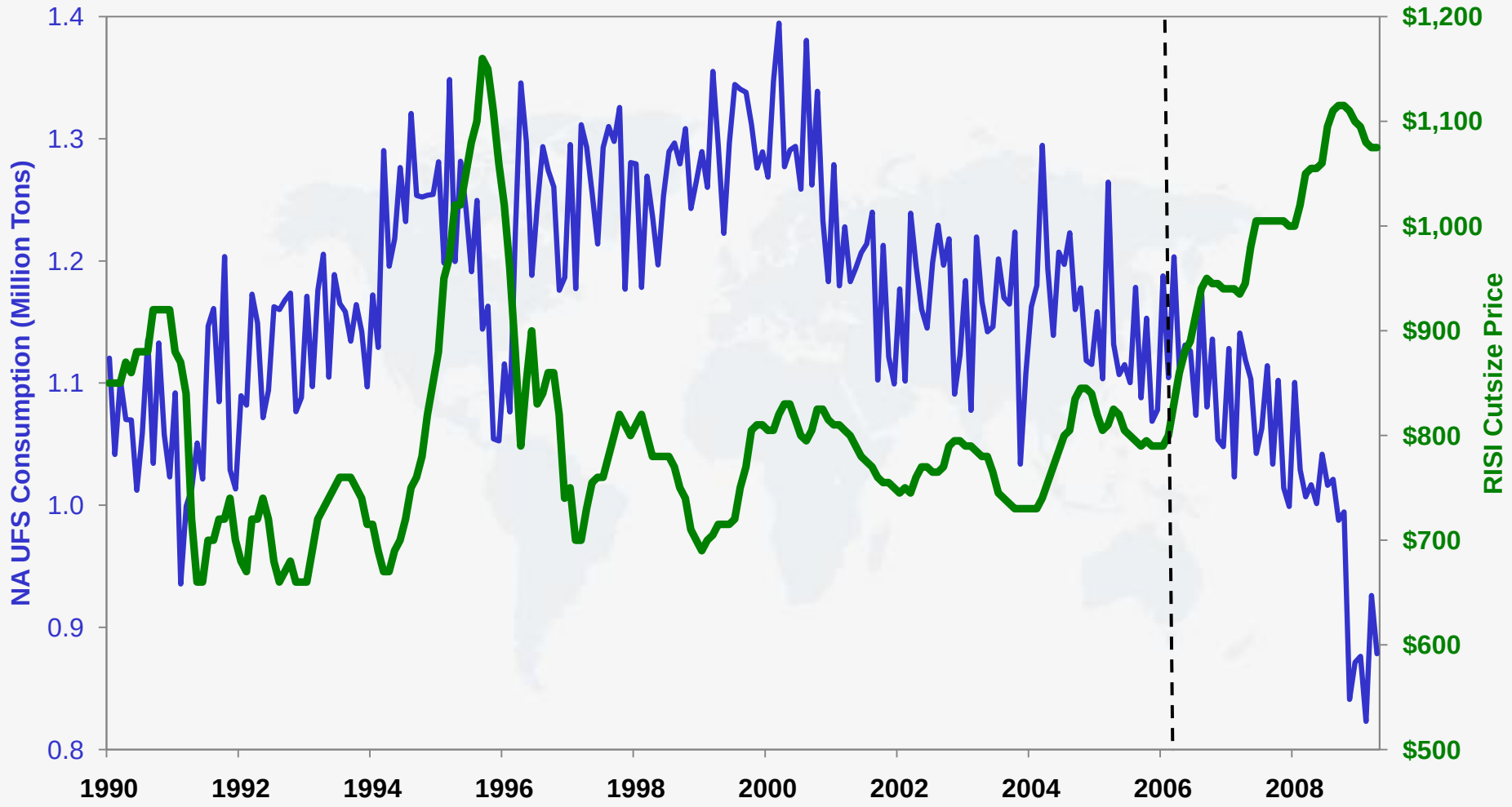


Source: RISI, AF&PA, PPPC, IP Strategic Planning

# Generating Strong Results

## *Strategy Driving Strong EBITDA & Cash Flow*

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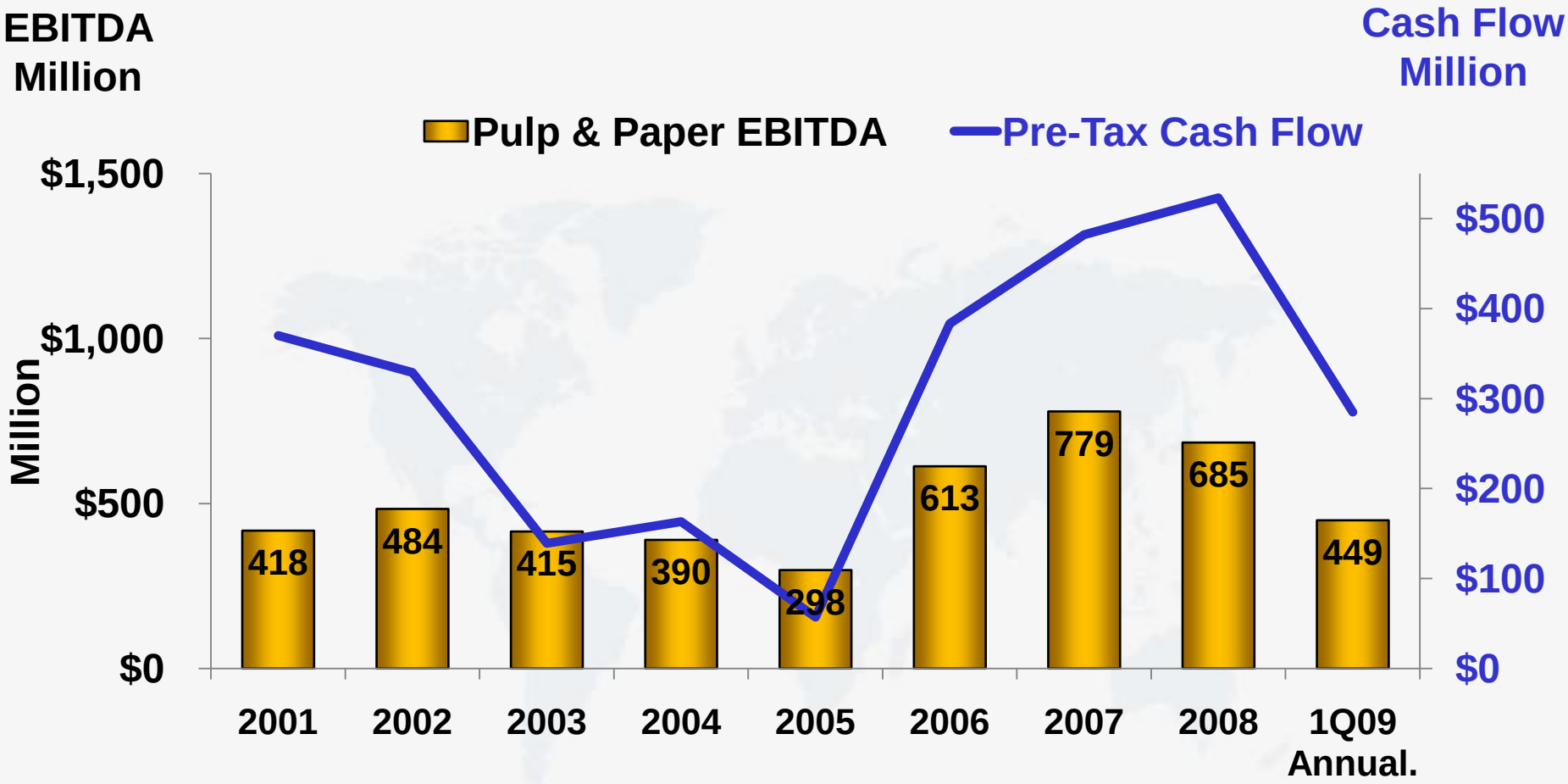


| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| Paper-Only EBITDA % | 12% | 15% | 12% | 11% | 9% | 17% | 19% | 19% | 19% |
| Paper-Only EBITDA/Ton | $102 | $118 | $93 | $83 | $70 | $142 | $170 | $189 | $187 |

# Generating Strong Results
## *Transformation Successful*

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- **Delivering Free Cash Flow**
- **Managing Supply to Customer Demand**
- **Managing Low-Cost Performance**
- **Generating Strong Returns**



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# Strategy & Capital Allocation

John V. Faraci

# IP Transformation

## *IP Vision & Elements of Strategy*

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**Vision**

**Leadership position in attractive markets with low-cost assets that can generate strong free cash flow and cost-of-capital returns**

**Elements of Strategy**

- Scale Businesses
- Leadership Positions
- Operational Excellence
- Paper & Packaging
- North America + Low-Cost Regions
- Attractive Markets

# IP Transformation

## *How Transformation Advanced the Vision*

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- **Established leading global positions**
  - **Corrugated Packaging**
  - **UFS**
  - **Coated Paperboard**
- **Exited segments where IP lacked sustainable competitive advantage**
- **Created more sustainable cash flow**
- **Focused on fewer, larger, lower-cost mills**
- **Improved profitability**

**Ability to succeed in weak market conditions**

# IP Transformation
## *What We've Learned*

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- **Execution is key**
- **Flexibility is vital**
- **Leverage cuts both ways**
- **Joint ventures challenging, but important**
- **Merger benefits drive financial returns**
- **Contingency plans critical**
- **Appropriate risk premiums**

# Where We Go from Here

## *Navigating Turbulent Waters*

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# Where We Go from Here

## *Economic Recovery*

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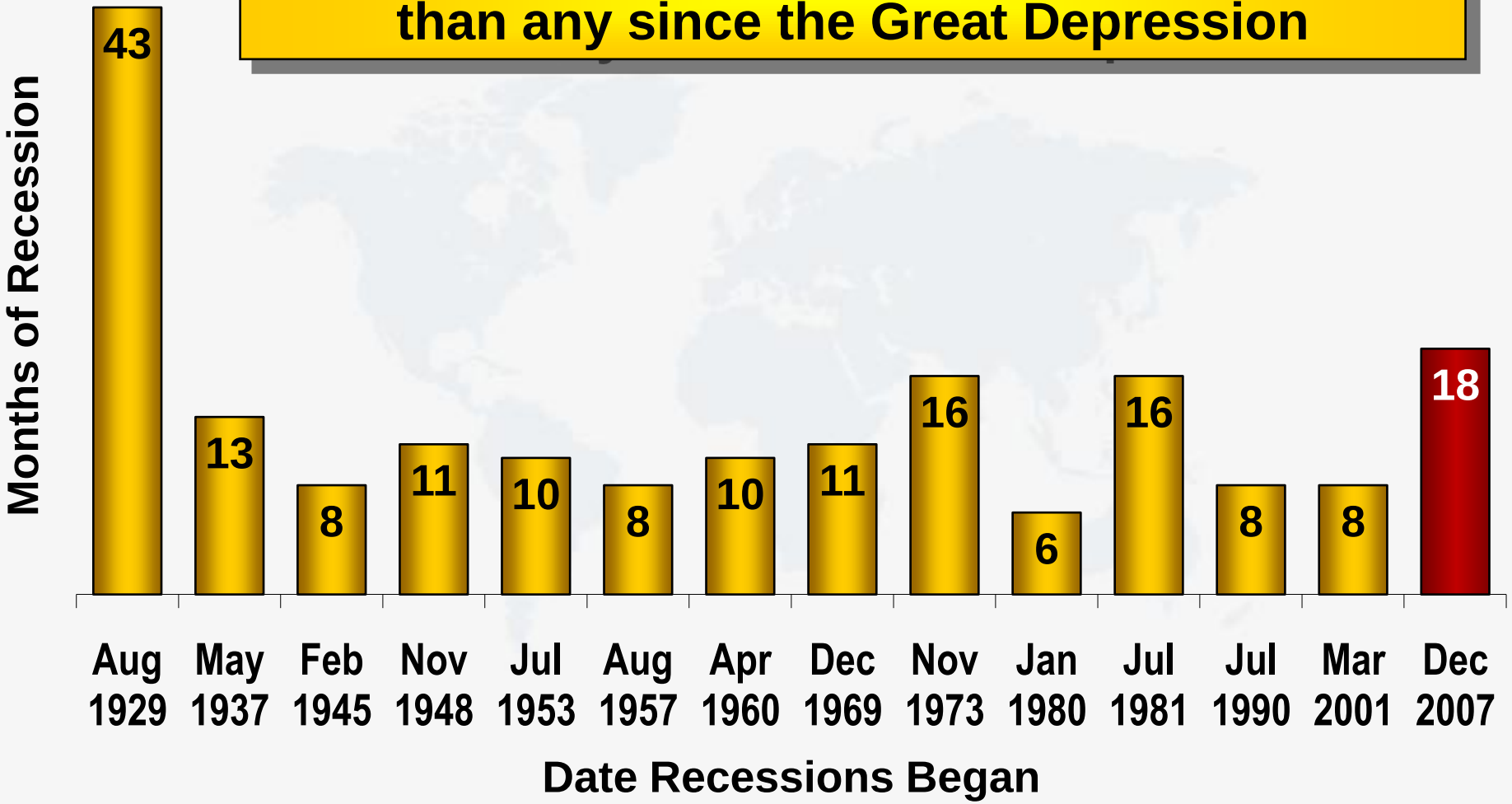
**Current recession has already lasted longer than any since the Great Depression**



# Where We Go from Here
## *Economic Recovery*

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- **Global economic conditions could start to improve by year-end**
- **U.S. economy stabilizing**
- **De-levering occurring**
- **Pent-up auto & housing demand**
- **Emerging economies improving**
- **U.S. deficits & inflation**

# Where We Go From Here

## *Priorities*

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- Maximize free cash flow
- Reduce debt aggressively
- Manage near-term maturities
- Manage our supply to protect margins
- Pursue systematic cost reductions
- Realistic strategy for each business
- Be willing to make choices

**Positions IP to outperform in any economic environment**

# Strategy & Capital Allocation

## *Upside Potential*

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**Potential for stronger earnings & increased cash flow in an economic recovery**

- Synergies
- Margins
- Volumes

- Operating Costs
- Interest Expense
- Downtime Costs

# Where We Go from Here
## *Capital Allocation*

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**Pursue Total Debt-to-EBITDA Ratio of < 3X**

**Balance Use of Cash to Maximize Shareowner Value with Appropriate Risk**

**Improving IP Asset Portfolio**

- Cost Reductions
- Margin Expansion
- Selective Reinvestment

**Reward Shareowners**

- Dividends
- Share Repurchases

Total debt includes estimated pension liabilities & operating leases

# IP Transformation
## *Summary*

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**What We've Done**

- Created portfolio of high-quality assets
- Leveraged IP's operating expertise
- Improved sustainability of free cash flow
- Reduced debt significantly

**What We're Doing**

- Maintaining strong focus on free cash flow
- Realizing greater synergies at a faster rate
- Targeting <3X total debt-to-EBITDA
- Pursuing structural cost reductions

**What We Will Do**

- Continue free cash flow focus
- Manage our supply to protect margins
- Achieve total debt-to-EBITDA target
- Balance use of cash



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