SYLVAMO: 3rd Quarter Earnings Conference

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SPEAKERS

Hans Bjorkman – Vice President, Investor Relations
Jean-Michel Ribiéras – Chairman and Chief Executive Officer
John Sims – Senior Vice President and Chief Financial Officer

PRESENTATION

Moderator

Welcome to Sylvamo's Third Quarter 2022 Earnings call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, you will have an opportunity to ask questions. As a reminder your conference is being recorded.

I would now like to turn the conference over to Hans Bjorkman, Vice President of Investor Relations.

H. Bjorkman

Good morning and thank you for joining our call today. Our speakers this morning are Jean-Michel Ribiéras, Chairman and Chief Executive Officer, and John Sims, Senior Vice President and Chief Financial Officer. Slides 2 and 3 contain important information, including certain legal disclaimers. For example, during this call, we will make forward-looking statements that are subject to risks and uncertainties. We will also present certain non-US GAAP financial information. Reconciliations of those figures to US GAAP financial measures are available in the appendix. Our website

also contains copies of the third quarter earnings press release as well as today's presentation.

I would now like to turn the call over to Jean-Michel.

J. Ribiéras Good morning, and thank you for joining our call. I'll begin my comments on Slide 4. On October 1st, we completed our first year as a public company. Our first year was one of significant achievements. As we build the world's paper company, we generated strong earnings per share and free cash flow, which we used to reduce debt, begin returning cash to shareowners and reinvest in our business.

We agreed to acquire the Nymölla mill in Sweden and divested our Russian business. Then we repaid our Term Loan B and achieved our gross debt target of $1 billion. We have also exited our transition services agreement. I'm proud of our teams and accomplishments over the last year. More importantly, I'm pleased that we are well positioned to navigate any macroeconomic headwinds and resulting industry challenges.

Slide 5 highlights our third quarter results. Our three-prong strategy of commercial excellence, operational excellence and financial discipline

was the foundation of our success. On a quarter-over-quarter basis, we increased adjusted EBITDA by 14% to $216 million and we grew our margin by 160 basis points. We increased adjusted earnings per share by 24% to $2.51 per share. We generated $114 million in free cash flow and repaid $88 million of debt in the quarter.

These results were above the high end of our guidance. Our continued strong performance reflects our talented teams, our iconic brands and our low-cost mills, all of which enable us to remain the supplier of choice for our customers.

Slide 6 highlights our key performance metrics compared to the second quarter and to last year's third quarter. We increased net sales by 6% to $968 million. Our adjusted EBITDA of $216 million represents a margin of 22.3%, the highest margin level we have achieved. We generated $114 million in free cash flow, which was an increase due to higher earnings, less capital spending and a reduction in working capital. These strong performances demonstrate our ability to continue to deliver on our investment thesis. Our teams performed well, creating value for all our stakeholders.

Now John Sims will discuss our third quarter performance in more detail.

J. Sims

Good morning, everyone. Let's turn to Slide 7 please. As Jean-Michel said earlier, we earned $216 million in adjusted EBITDA in the third quarter. This is a 160 basis point improvement and was driven by $60 million in price and mix improvements, as realization of price increases exceeded our outlook and we continue to drive mix optimization.

Volume increased slightly by $3 million with stronger shipments in Latin America and North America. Our order backlogs were strong in all regions in the quarter. We also had a slight increase in operations and costs, which increased by $3 million. We spent $14 million less on outages than in the second quarter. We successfully conducted the planned maintenance outage at our Mogi Guaçu mill. Input and transportation costs increased by $46 million as costs for energy, fiber and chemicals continue to increase.

Let's take a look at our regional results on Slide 8. Each region continues to perform very well, demonstrating the strength and resilience of our talented teams, iconic brands and low-cost mills as well as favorable industry conditions. Each region benefited from realizing price increases,

which offset escalating costs and inflation. Our volumes remain strong in all regions and we continue to outperform the industry shipments.

We operated well in all three regions. Input costs and transportation availability remained under pressure and we have seen some relief in truck availability in North America, but obtaining adequate rail service continues to be a challenge. The appendix contains additional details on our regional performance.

So, let's turn to Slide 9. In the third quarter, uncoated freesheet industry fundamentals remain favorable across our regions. Demand in Latin America and North America continued to rebound from pandemic levels while demand in Western Europe declined by 2%, which in part was driven by the lack of supply in Europe.

Relative to 2019, 2022 year-to-date imports were about flat in Western Europe and down about 20% in each of the Americas. And, as the bottom row shows, capacity is down 10% to 20% in our regions relative to pre-pandemic levels.

The cost curve in Europe remains quite steep with more than 25% of the capacity being non-integrated. The non-integrated producers are at a competitive disadvantage due to elevated market pulp and energy costs.

On the other hand, our Saillat mill is integrated and generates 85% of its own energy, giving us a competitive advantage. In summary, demand is recovering, capacity and imports are down and mill inventory levels in our regions remained below their historical averages.

Moving to Slide 10, not only do we operate in the most attractive regions, we continue to win with key customers. We also continue to optimize our product mix and increase our positions in high-margin segments. We are growing with key customers. For example, we expect to increase our Chamex volume with a strategic retail customer in Latin America by 25%.

In all regions, we continue to focus on the evolving needs of end users. We are optimizing our mix. For example, in Europe, we will increase our brand mix to 50% in 2022 versus 30% in 2021. In North America, we are optimizing our portfolio to ensure it aligns well with our channel partners and consumer trends.

Furthermore, we are updating our business practices so that we are adequately paid for the value-added services we provide and we are segmenting our service levels. We are growing in high-margin segments. For example, we continue to expand our e-commerce presence in North America. Our commercial excellence efforts drive higher volumes and margins, increase customer loyalty and allow us to outperform industry demand.

Now, back to Jean-Michel for a discussion of our recent moves in Europe.

J. Ribiéras

I'm now on Slide 11. First, some perspective on the recent divestiture of our Russian business. After the invasion of Ukraine, we made a principle-based decision to exit Russia. In October, we sold the business and received $390 million in net proceeds.

The divestiture of our Russian business allowed us to avoid a $220 million recovery boiler project, reduced our exposure to the more cyclical market pulp segment by 30% and significantly decreased our geopolitical risk and uncertainty. Completing this deal also eliminated a major distraction for our management team, which is now focused on our core business.

Let's move to Slide 12. We are taking advantage of the opportunity to acquire the Nymölla mill in Sweden at an attractive price. This 500,000 ton uncoated freesheet mill fits well with our strategy. It will strengthen our position in uncoated freesheet and enable us to better serve our customers in Europe and around the world. We agreed to pay 150 million euros for this mill, which will benefit from a $40 million pulp mill upgrade that will be mostly completed before we take ownership of the mill. As you might imagine, we are excited to add this mill to our European business in the first quarter.

Slide 13, please. The Nymölla mill is one of the largest integrated uncoated freesheet mills in Europe. It is 85% energy self-sufficient and has strong environmental practices. The mill produces multiple grades for cutsize business forms, digital papers and offset papers. It produces iconic brands that fit well with our strategy.

Let's move to Slide 14. The Nymölla mill is an excellent fit with our three-pronged strategy of commercial excellence, operational excellence and financial discipline. In addition to the complementary uncoated freesheet product mix and iconic brands, the mill maintain strategic channel

partnerships and a complementary geographical mix. It also has a customer-focused culture and shared values with our company.

The mill is low cost and in an attractive location. It fits well within our portfolio and strategy. This purchase price represents an attractive price, and we expect more than $20 million in synergies and an internal rate of return greater than 25%. The deal will be immediately accretive to our earnings per share and free cash flow.

Let's turn to Slide 15. Using the last 12 months of adjusted EBITDA as of the end of June, the transaction multiple is 2.5x and is expected to be below 2x after $20 million in synergies, including the pulp mill project previously mentioned. We estimate $15 million one-time cost and capital to achieve the synergies and $14 million in information technology, transition services and other integration costs. We look forward to closing as soon as we receive the required regulatory approvals and to welcoming new colleagues to Sylvamo as soon as possible.

Now back to John for a discussion of our fourth quarter outlook and revised investment thesis.

J. Sims

I'm now on Slide 16. In the fourth quarter, we project price and mix to improve by $30 million to $35 million as we continue to realize prior price increases in all three regions. We expect volume to be flat to decreasing by zero to $5 million with seasonally weaker volume in Europe and North America. We project operations and costs to increase by $35 million to $40 million driven by seasonally higher costs in Europe and North America, foreign exchange impacts in Brazil and an increase in incentive compensation accruals.

We expect input and transportation costs to be flat to increasing by zero to $5 million largely due to higher energy and input cost inflation. Maintenance outage expenses are projected to increase by $21 million as we conduct two planned maintenance outages. This will be our heaviest planned maintenance outage quarter of the year.

All in, we expect to deliver fourth quarter adjusted EBITDA of $180 million to $190 million, which would put us slightly below or at the low-end of our full year guidance of $740 million to $780 million. This change is largely driven by the increase in foreign exchange impact on our Brazilian earnings and compensation accruals, which were not included in our previous guidance.

We expect fourth quarter earnings per share of $2.05 to $2.25 and we expect free cash flow of more than $25 million for the quarter, which increases our full year outlook to greater than $210 million. The appendix contains additional information on fourth quarter outlook. Also Appendix Slide 37 shows that we have reduced our outlook for 2022 capital expenses by $20 million to $155 million. We will be unable to complete certain projects in 2022 due to supply chain constraints and contractor delays. We project spending this $20 million in 2023.

Slide 17 shows the three pillars of our capital allocation framework. This is how we think about allocating cash to create shareowner value. At the time of the spin-off, we prioritized debt reduction and returning capital spending to the levels necessary to maintain our mills.

Now that we've reached our $1 billion gross debt target, we are putting greater emphasis on returning cash to shareowners. We remain a cash flow story. We will leverage our strength to drive high returns on invested capital and generate free cash flow. We'll use that cash to increase shareowner value by maintaining a strong financial position, returning

more cash to shareowners and reinvesting in high return projects in our business.

Let's move to Slide 18 to review our fortified financial position. Since the spin-off, we've reduced debt by more than $560 million. We repaid the initial amount drawn from the revolving credit facility and have entirely repaid our Term Loan B.

Also, we renegotiated our credit agreement to raise the limits on restricted payments prior to the final settlement of the Brazil tax dispute, so that we now match the terms of our bond agreement. Under the revised agreement, our annual restricted payment limit was increased to $90 million from $75 million as long as our gross debt is less than 2 times our adjusted EBITDA. Currently, that ratio is less than 1.5 times. Appendix Slide 35 provides more details.

As a result of reducing our debt, our annualized interest expense will decline by more than $20 million at the current interest rates. Note also that our pension fund remains well funded at more than 95%. So as you can see we head into the second year with a strong financial position.

Back to you Jean-Michel.

J. Ribiéras

Slide 19, please. We are well positioned to create value for shareowners. We have reduced total debt significantly and $128 million in 2022 spin-off related payments will not recur next year. Returning cash to shareowners is a core component of our investment thesis. We started by paying $10 million in dividends this year and by establishing the authorization to repurchase up to $150 million of shares.

I'm pleased that today, our Board has approved an increase that more than doubled our quarterly dividend to $0.25 per share effective in the first quarter of 2023. As John discussed, we will continue to reinvest in our business to increase returns on capital and generate free cash flow. This includes our investment in the Nymölla mill and our high-return capital projects.

We are investing in our business to increase our cost competitiveness and to remain the supplier of choice. I'm grateful for our talented and engaged colleagues and their dedication to working safely, delivering on our promises to customers and for creating value for shareowners. We remain committed to creating value for all of our stakeholders and are confident in

our ability to achieve our vision of being the employer, supplier and investment of choice.

With that, I'll turn the call back over to Hans.

H. Bjorkman Thanks, Jean-Michel and thank you John. Lois, we're now ready to take any questions.

Moderator We have a question from Ed Brucker from Barclays.

E. Brucker Just had a couple. First one just on guidance that it come in on the lower end of the original guidance, but the quarter was strong and it seems like in the fourth quarter might be stronger too. I was just wondering if you're thinking a little conservatively given the environment right now? I guess on top of that, how do you expect given the uncertainty, how do you expect the go-forward outlook for your market in uncoated fressheet?

J. Sims Yes. As we mentioned, our guidance put us on the lower end of our full year guidance, but that's really driven by FX impact we're seeing as the Brazilian real strengthens. So that's kind of a question where that ends up but also it also reflects the fact that we've had to take an additional accrual

on our incentive plan. Just to remind everybody on the call, we really target our incentive plans to match up with the interest of our shareowners and is driven by EBITDA margins and free cash flow. The increase in the incentive compensation is the fact that the strong cash flow that we're generating this year. I think that's a testament to the focus that we have on free cash flow.

But in terms of being conservative, everything else essentially continues as we had thought in the fourth quarter. That meaning that the price increases that we've been able to realize from our prior price announcements have come in. Those are more than compensating the input costs and in fact, we're seeing input costs kind of flatten out across all the regions. So, certainly at an elevated level and a high level, but we feel going in— it's hard to predict what 2023 is going to be.

I mean given some of the uncertainties we have and everybody I think can read about but one of the things we feel very good about is our exit rate and how well positioned we are from a balance sheet perspective, being at $1 billion of debt and also from where we are from the margins, earnings and order backlog and the strength that we have with our customers and our positions in all our markets.

E. Brucker Yes. I mean it's testament how well you've done with the balance sheet. I guess next question is about that. Just if you are thinking about a potential leverage target through the cycle or if I guess a max leverage you'd be willing to take it up given your capital allocation priorities have shifted a bit given that you have paid down so much debt. Just want to get your thoughts on where leverage kind of fits in is in there?

J. Sims Well, we set the $1 billion target because we felt that that would allow us to continue to invest through the cycle in high-return projects into the business and continue to improve our business and also, return cash back to our shareowners. Now, we'll continue to have to pay down some debt, because we have amortization requirements for the term loan that we do have.

So, in terms of your question is what's the max that we go, yes, I think we're comfortable in stating where we want to be is at that $1 billion or slightly less. We think that's a very good position for us to be in to be able to execute the rest of our strategy.

Moderator We'll move to the line of Ron Gutfleish from Elm Ridge.

R. Gutfleish Last year going near the fourth quarter, you expected operations to hit $15 million because of normal seasonality. So could I assume that— I realize energy expenses are up from last year— that all of your guide 35 to 40 more in the fourth quarter, about half is normal seasonality and half is the incentive accrual?

J. Sims Yes, the incentive— you're right, but it's also the FX. So add the FX with the incentive accrual and you're close to that 50% of that cost is driven by those two items.

R. Gutfleish So going to the next quarter whatever is the incentive accrual, let's assume, are they roughly equal? Because whatever the incentive accrual ought to go back to some normal level. I realize you were under looking earlier in the year but the extra incentive accrual ought to go back and I guess the FX you would just hope to be flat. But roughly the incentive accrual, would it be in the $10 million range?

J. Sims Yes, $10 million— that's correct and about $5 million or so for the FX.

R. Gutfleish Secondly, you're going to be way, way under the leverage that you're looking at by the end of next year. I realize you have $150 million going out the door, but you're generating so much free cash. Is there a thought to renegotiating the terms on the agreement or really what you're going to do is deploy it and see you can get more— I'm going to pronounce this wrong— Nymölla?

J. Sims Ron, I guess, we're looking through the options in terms of what we can do from the bond perspective to get more room on the restricted payment terms, but we're analyzing that right now. Let me just add another comment. The acquisition is not core to our strategy. We said that previously. We also said that we will opportunistically look at acquisitions that make strategic fit with us and that certainly was the case in the Nymölla perspective.

J. Ribiéras Maybe I can add a point is know that we reach our $1 billion debt target and as John mentioned, Nymölla was probably very unique opportunities, which is not core to our strategy. But what is core to our strategy is to returning cash to shareholders. It has become even a higher priority for capital allocation.

So that's why we increased dividend. We more than doubled and at current share price, repurchasing share is very attractive. So maybe you might ask why we haven't done it before. As you might understand in the third quarter we have blacked out due to material nonpublic information. We had Russia, we had Nymölla, the third quarter earnings. So really we're back to returning cash to shareholders is really a high priority right now. That's why I would put in front of.

R. Gutfleish Can I follow-up one quick one on that. So the $90 million a year— you haven't done any this year, could you sort of reach forward in the fourth quarter, because the $90 million starts again for 2023?

J. Ribiéras We've done $10 million in dividends out of the $90 million for this year and then it starts again $90 million, January 1st.

R. Gutfleish So you have lots of room to do it in the fourth quarter this year.

J. Ribiéras We do.

Moderator The next question is from Paul Quinn from RBC Capital Markets.

P. Quinn Just on the increased brands in Europe from 30% to 50%, what's the margin impact on that and then what happens with the addition of the Sweden mill?

J. Sims We don't want to give specifics on the margin difference between the brands. There is a margin increase and there is a premium as we drive it, but there's also other benefits as well. Mostly you can think about in terms of brands being more sticky with customers, barriers to both imports and also to competition. So there's also other values in terms of increasing our brands that we were able to realize across all the regions.

J. Ribiéras Concerning Nymölla, they have also a strong brand, which is called Multicopy. So on the cutsize side of the business, it's going to continue to be Sylvamo's strong brands approach.

J. Sims The other thing that Nymölla brings to us that we didn't really have with the Saillat mill is strong brands in their commercial printing and forms business. So that's actually an increase market segment for us, an opportunity for us to really leverage that.

P. Quinn Then just maybe you could give us a little bit more color on this $40 million pulp mill upgrade at Nymölla, as well as when are you taking maintenance at Saillat?

J. Sims So I'll answer your second question. Saillat is on 18 months. So we won't have any maintenance, we won't have an annual outage this year. So it will be next year, around April time frame I believe.

In terms of Nymölla, the mill modernization project, this has been actually completed, mostly completed by Stora this year. So all the benefits will begin to accrue to us next year when we finally do take ownership of the mill.

What they've done is they've upgraded the back-end of the mill specifically two areas is a new digestor with increasing the ability to produce softwood pulp. So that will expand the capacity there. Also an O2 deliquification, which will reduce cost. So the mill has a somewhat different pulping process than our other mills. It's a sulfite process of increasing softwood pulp consumption and production is a positive for that mill and that's what this mill upgrade does.

P. Quinn So just lastly, does that upgrade affect the production capacity of the mill at 500,000 tonnes?

J. Sims No. What it does increase is the pulping capacity and so you have to buy less open market. It's not open market tonnes of pulp rather, I'm sorry.

P. Quinn So that just begs the question how much are you buying that— how much is that mill purchasing on the open market right now? What's the self-sufficiency on the pulp side, pre and post pulp mill upgrade?

J. Sims It doesn't buy a lot of market pulp. It buys hardwood pulp for a product grade and this upgrade now allows us to substitute that with softwood that we can source the fiber in Sweden.

Moderator The next question is from Adam Ritzer, Private Investor.

A. Ritzer I just had one quick question. You guys gave kind of a pro-forma debt number after the Russia sale of, what, $957 million, I think it is. How much cash are you going to have on a pro forma basis after the sale?

J. Sims After the sale, I have to think— maybe we ought to get back to you. We'll probably be in about $100 million range. Let us get back to you on that.

A. Ritzer So if you had $390 million in proceeds from the sale and you paid down about $270 million of debt. So is that difference, add to the cash you had at the end of Q3? Is that the right way to look at it?

J. Sims That's the right way to look at it.

A. Ritzer Okay. We could talk about with you that later. That's all I wanted to ask.

J. Sims We're using cash to pay for the Nymölla mill.

A. Ritzer Right, but that's not going to be till Q1 right?

J. Sims Right. Yes, the number I gave you, I was subtracting the paying for the Nymölla mill out of that cash, because we're expecting to hopefully close that early in the first quarter.

A. Ritzer Right. Okay. So you take that cash minus the $150 million assuming that plus whatever free cash you generate in Q4. Okay. Understood.

Moderator I'll now turn the call back over to Hans Bjorkman for closing comments.

H. Bjorkman Thank you everyone for joining our call today. We appreciate your interest in Sylvamo and we look forward to continued conversations in the coming days, weeks and months ahead. Have a great rest of your day and a great week.

Moderator Once again, we would like to thank you for participating in Sylvamo's Third Quarter 2022 Earnings call. You may now disconnect.