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Call Participants

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Presentation

Operator

Good morning. Thank you for standing by. Welcome to Silvamo's First Quarter 2026 Earnings Call. [Operator Instructions] As a reminder, this conference is being recorded. I will now turn the call over to Hans Bjorkman, Vice President, Investor Relations. Sir, the floor is yours.

Hans Bjorkman

Vice President of Investor Relations

Thanks, Samantha. Good morning, and thank you for joining our first quarter 2026 earnings call. Our speakers this morning are John Sims, Chief Executive Officer; and Don Devlin, 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-U.S. GAAP financial information. Reconciliations of those figures to U.S. GAAP financial measures are available in the appendix. Our website also contains copies of the earnings release as well as today's presentation. With that, I'd like to turn the call over to John.

John Sims

CEO

Thank you, Hans, and good morning, everyone. I'm glad that you're joining our call. I'm on Slide 4. Today, I'd like to begin with a few important macro developments that have occurred since our fourth quarter call in February, which have led us to change our operating strategy to achieve our plans this year. First, the U.S. Supreme Court invalidated IEPA tariffs and the U.S. government responded to this by placing 10% tariffs on all trading partners. Europe had previously been at 15%, while Brazil was at 50%. This change benefits Silvamo. And late in the first quarter, we began to bring product into the U.S. from our Brazilian operations while ramping down imports from our European operations.

Second, the Middle East conflict has resulted in higher energy, logistics and input costs. Across our regions, we are looking to reduce costs and taking commercial actions to help offset these impacts. Let's move to Slide 5. Our first quarter highlights include implementing the previously communicated uncoated freesheet price increases to our customers across all our regions. We had a difficult first quarter operationally, reliability issues, particularly in Europe and Brazil, negatively impacted us by almost \$9 million relative to the fourth quarter, and we expect some additional costs in the second quarter. The root cause of these issues have been identified and fixed or will be corrected and the annual outages will be taking this quarter.

The one exception is that our Nymolla Mill, where an issue with a debarking drum will not be corrected until the fourth quarter. We look at an important -- we took an important step in achieving our vision by launching our lean transformation journey in our Latin American business, along with our Mogi Guacu mill. I was in Brazil last week and was very encouraged by the energy and commitment the teams have in learning and executing the lean transformation. Lastly, yesterday, we completed the refinancing of our 2027 debt to extend our maturity profile, which sustains flexibility and maintains our strong financial position. Let's move to the next slide.

Slide 6 shows our first quarter key financial metrics. As a reminder from our last call, 2026 is a transition year as we work through some short-term capacity constraints due to the termination of the Riverdale supply agreement at the end of April and the extended outage at Eastover later this year as we execute our strategic investments there. Our first quarter results came in as expected, except for the operational issues I mentioned.

We built inventory, which resulted in lower sales volume, and we also incurred the incremental cost due to sourcing and converting. We earned an adjusted EBITDA of \$29 million with a margin of 4%. Adjusted operating earnings were negative \$0.53 per share. As anticipated, free cash flow was impacted by lower earnings, the unfavorable impacts of our inventory build and the timing of payments. Keep in mind that

our free cash flow is heavily weighted to the second half of the year. In the last few years, we generated the vast majority of our free cash flow in the second half, and we expect to do so again this year. Now I'll turn it over to Don to review our performance in more detail.

Don Devlin

Senior VP & CFO

Thank you, John, and good morning, everyone. Slide 7 contains our first quarter earnings bridge versus the fourth quarter. As John mentioned, the quarter played out largely as we expected, with the exception of operations and other costs, which I'll cover shortly. In the first quarter, we earned \$29 million of adjusted EBITDA compared to \$125 million in the prior quarter. Price and mix were unfavorable by \$13 million. Overall, mix was \$17 million unfavorable, which more than offset the price improvements we saw in the quarter. About half of the mix was due to seasonally weaker mix in Latin America, which is normal for Q1, and the other half was driven by unfavorable North American customer and sourcing mix.

On the favorable side, paper prices improved in North America and Latin America as Q1 increases were implemented. Paper prices in Europe bottomed out in the quarter and previously communicated price increases are expected to realize in Q2. Volume decreased by \$36 million due to normal Latin America seasonality and the anticipated inventory build in North America as we prepared for the end of the Riverdale Mill supply agreement and the extended Eastover mill outage in the fourth quarter. Operations and other costs were unfavorable by \$29 million, with about half due to non-repeat of favorable fourth quarter items from year-end LIFO accounting in North America and green energy in Europe.

The other half was related to \$9 million in manufacturing costs across our regions that John described earlier as well as \$3 million in FX. Planned maintenance outage costs were flat Input and transportation costs were unfavorable by \$18 million, primarily due to energy in North America, highly impacted by a onetime charge of \$10 million from International Paper's Riverdale mill due to the exceptionally high natural gas cost from the winter storm.

Let's move to Slide 8. European industry supply and demand remains challenging, but pulp prices improved throughout the first quarter, and we are realizing the previously communicated paper price increases in April.

We have communicated a second paper price increase effective in May and expect the realization to occur through the second and third quarters. In Latin America, we moved from the seasonally strongest demand in the fourth quarter to the seasonally weakest first quarter, but now expect demand to increase each quarter throughout the year. This should positively impact our volume and geographic mix as the year progresses. We are realizing the previously communicated paper price increases to our customers in Brazil and to our export customers across other Latin American countries as well as the Middle East and Africa region and should continue to see additional realization throughout the second quarter.

In North America, industry supply and demand dynamics have improved as 7% of annual uncoated freesheet industry supply was removed with the Riverdale mill conversion. After peaking in June of last year, imports into North America have declined significantly throughout the second half of last year and into the first quarter. We also began realizing the previously communicated paper price increases to our customers and expect to see additional realization through the second quarter. We expect the Middle East conflict to continue pressuring costs across our regions as we go through the year.

We are already seeing increases in energy, chemicals, diesel and ocean freight in the second quarter. Let's move to Slide 9. As John mentioned earlier, the changes in U.S. tariffs have led us to bring in product from our Brazil operations while ramping down imports from our Europe operations. Last quarter, we provided you with an estimate of the adjusted EBITDA impacts of the North American footprint transition, which we indicated was about \$85 million negative for the full year. Assuming that tariffs remain at the current levels, we now estimate total full year impact to be around \$65 million negative, which is \$20 million improvement from our prior estimate and will be realized mostly in the second half.

This improvement is the result of the mix improvement by redirecting our Brazil imports from the Middle East and Africa to the U.S. We will stay close to the situation and be prepared to go back to our prior plans

should the tariffs increase in the second half. Let's move to Slide 10. Our capital allocation philosophy remains unchanged. We will deploy every dollar with the goal of improving. Let me go back -- excuse me. We're on Slide 10. This slide is to remind everyone of our planned maintenance outage schedule for the full year by region and by quarter.

We will have an increase of \$20 million in the second quarter versus the first quarter as we have more outages in Latin America. 2026 is also different than past few years, where we have more than 80% of the total cost in the first half. This year, we have more than 50% of the total cost in the fourth quarter as we complete the investments in Eastover. Now let's move to Slide 11. Our capital allocation philosophy remains unchanged. We will deploy every dollar with the goal of improving our competitive position and delivering the best possible shareholder returns over time.

We plan to maintain a strong financial position, reinvest in our business and return cash to shareowners. The refinancing of our long-term debt allows us to navigate this uncertain environment without changing our thoughtful long-term approach to capital allocation. With a strong financial position, we can navigate the geopolitical and economic challenges and focus on improving customer experience, continue reinvesting in low-risk, high-return projects as well as execute through the end of the Riverdale supply and the Eastover mill outage later this year.

These investments and improvements will help to grow earnings and cash flow in the future. Let's move to Slide 12. Yesterday, we refinanced 2027 debt to extend our maturity profile. We refinanced our term loan F that matured in 2027 with a new term loan F3 that matures in 2032. We also extended our accounts receivable securitization facility out to 2029. And here on Slide 12, you can see the before and the after picture of our maturity profile. This move provides flexibility and allows us to maintain our focus on taking care of our customers and improving our business while we navigate these external challenges. Further details are in the appendix and will be included in our 10-Q that will be filed later today. I'll now turn the call back to John.

John Sims
CEO

Thank you, Don. I'll pick back up on Slide 13. Last quarter, I shared our vision that Sylvamo will be legendary. Legendary for the way we relentlessly pursue and achieve world-class excellence in all that we do. Consistently performing at world-class levels will create substantial lasting value for our employees, customers and shareowners and will enable us to be the employer, supplier and investment of choice.

Let's move to Slide 14. As we strive to achieve world-class standards in the areas that define our success, we are establishing an employee-driven continuous improvement culture by transforming the company to a lean-driven mindset. By incorporating a lean mindset and best practices into our everyday efforts across all functions, we expect significant improvement in the following areas:

Customer centricity. Lean transformation will help to enable a new standard of customer experience and loyalty, where we strive to be truly outstanding, and this is critical to our strategies.

Operational excellence, lean transformation will also help to enable best-in-class levels of efficiency, reliability and performance in our mills and supply chains, ensuring that our operations consistently deliver to the highest standards.

Cost leadership, the impact that lean transformation will have on our customer centricity and operational excellence to combine to enable us to attain industry-leading cost effectiveness through an employee-driven continuous improvement culture, strengthening our competitive position and ensuring sustainable results.

Now let's turn to Slide 15. Lean is a long-term company-wide strategic transformation, not a short-term change program. Over the next 3 years, our objective is to embed continuous improvement into how we run the business, so performance improvement becomes systematic and self-sustaining. Our lean transformation is focused on maximizing customer value by eliminating waste, improving performance and engaging every employee, starting with a structured hands-on rollout supported by expert partners. We kicked off our efforts in our Latin American business and have value stream mapping underway at our Mogi Guacu mill to identify waste and unlock cost savings across end-to-end processes.

We will also be conducting Kaizen improvement events driving employee engagement and building a culture of continuous improvement from the ground up. Later this month, we'll kick off our lean efforts in our North America business and across our corporate functions at our world headquarters. We'll then roll out lean in our Ticonderoga mill later in the second quarter. We'll continue expanding across all regions, businesses and locations, targeting efficiency improvements and margin gains.

Let's go to Slide 16, where I'll provide an update on our investments at our Eastover mill. Our high-return strategic investments at our Eastover mill are on track and making solid progress. The paper machine optimization project will add 60,000 tons of uncoated freesheet, reduce costs and improve our mix and efficiency. This project is on schedule with the bulk of the work to be completed in the fourth quarter during a 45-day planned maintenance outage.

The brand-new state-of-the-art sheeter is also on schedule and will start to be installed in the third quarter and will be ramping up in the fourth quarter. The woodyard modernization project is on track. The hardwood line is operating as of May 1, and we're already seeing significantly improved chip quality and expect to see better yield going forward. We plan to start up the softwood operation in the first quarter of 2027. These are high-return projects that will generate incremental earnings and cash flow for the long term.

Now I'll conclude my remarks on Slide 17. As I stated in my CEO letter to shareowners earlier this year, 2025 and '26 will be low points in our free cash flow generation as we weather the cyclical industry downturns, particularly in Europe and complete these investments at our Eastover mill. We are focused on long-term value creation by making disciplined data-driven decisions that position the company for sustainable success and strengthen Sylvamo for decades to come.

We will generate strong and sustainable results by diligently executing our flagship growth strategy, adhering to our disciplined capital allocation principles, becoming more customer-centric, institutionalizing lean continuous improvement principles and digitally transforming our business and operations. As industry conditions turn, our capital spending normalizes, the benefits from our investments begin to materialize, we have the potential to generate annually greater than \$300 million of free cash flow and greater than 15% returns on invested capital. So with that, I'll turn it back over to Hans. Hans?

Hans Bjorkman

Vice President of Investor Relations

Thanks, John, and thank you, Don. Okay. Samantha, we're ready for questions.

Question and Answer

Operator

[Operator Instructions] Your first question comes from the line of George Staphos with Bank of America Securities.

George Staphos

BofA Securities, Research Division

Appreciate the detail. I'll ask a couple of questions and come back in the queue, but I do have a bunch to go through. I guess, first of all, John, the company talks about operational excellence being legendary in terms of service and the like. And I recognize you're still early in that journey. That said, what was going on with operations reliability in that \$9 million number that you called out, particularly in LatAm, as I recall, and correct me if I'm wrong, I thought LatAm was expected to be better operationally or at least not as much of an issue as Europe in this quarter. So that's question number one.

Question number two, you called out or pointed to some mix factors in North America in the first quarter. What was behind that? And related to price, not expecting you to talk about future price increases forward-looking or whatever. But for the pricing that is in the markets right now in the publications, if we hold that, what price benefit do you get in 2Q versus 1Q sequentially or for the year?

John Sims

CEO

George, thank you. I thank you for joining the call and your questions. So I anticipated the questions on the reliability issues. And yes, I mean, I guess, key to our performance if we're going to delight the customer and increase customer loyalty, reliability and operational efficiencies is critical to that. That's why we're implementing the lean process, but also we are strengthening and have been focusing on mill reliability process and systems. And the biggest focus we've got there is ensuring that we're investing to maintain the equipment and also we're putting in the right processes and also training and development of our workforce.

And those are all critical aspects to being world-class in that performance. And we're clearly not there. I mean this is what this indicates the issues that we've had is we've got work to do around our reliability. As it pertains to the particular items we had, both Mogi and Luiz Antonio had issues in the power plant and also in the digesters that needed to be fixed actually in the annual outage. So Mogi is right now down going through its annual outage. So the issues that we had in the first quarter, we actually continue to see that in the first month of this quarter, and now we're planning on fixing that. Luiz Antonio's outage is not until June.

So we are continuing to struggle some there with that mill and its performance, and that's driving higher increased operating costs, the use of chemicals and whatnot that's impacting us. If you look at Europe, the biggest issue we had was Saillat. There was a turbine generator that's operated by a third party that tripped. And the issues we had in Europe also occurred in area when it was a cold winter and probably the worst timing that we could have. But this issue knocked the Saillat mill offline for a couple of days until we could get back up and running.

And then Nymolla, we also had boiler issues at the beginning of the year. And then as I mentioned, I think, in the prepared remarks that we have 2 debarking drums in Nymolla, but one of debarking drums due to mechanical failure is offline. It won't be -- we won't be able to fix that until the fourth quarter this year.

Operator

Your second question.

George Staphos*BofA Securities, Research Division*

I guess -- so just before we go there, you described what happened. I guess my question would be following up, why? So like why did the issues come up at Mogi in Luiz Antonio, why didn't necessarily -- not you, but the team sort of determine what was happening and prevent it from occurring. And the same thing in Nymolla, especially with the boiler and the debarking.

John Sims*CEO*

Yes. So in terms of the why it would be different for each of these, whether it's mechanical failure or an operating area. We do a detailed root cause failure analysis on any of these significant events, and those have been done here. And then we put a lot of effort into ensuring that we correct and also communicate what we learned across those failures. But in all those cases, we think that -- except for the one in Saillat because that was out of our control, that was a third-party operator area.

Everyone points to an area where we've got to either improve our reliability process systems, identifying those areas that could fail and making sure that we're taking corrective actions before that occurs or training and improving the quality of our workforce so that the right operating decisions are made, and that's all what we're working on, George.

George Staphos*BofA Securities, Research Division*

Appreciate that.

Don Devlin*Senior VP & CFO*

John I can take that...

George Staphos*BofA Securities, Research Division*

On the pricing and mix?

Don Devlin*Senior VP & CFO*

Yes, George, this is Don. I'll take that mix question. So George, Q1, a couple of big things in mix in Q1. So in Latin America, it's seasonally weaker for us. And what's happened typically is there's less domestic Brazil volume, which is our most profitable and more export as a percentage of the mix. And so that has a -- we expect that. It's normal for the quarter. And in Brazil, what typically happens is it gets stronger as the year goes on all the way through the fourth quarter. And in North America, it's a little different situation. We are -- as we prepare for the Riverdale and Eastover, the Eastover outage later in the year and the Riverdale supply agreement going away, we're using third-party sheeting.

We're buying some volume from third parties buying paper. And we're doing this so that we have the inventory to serve our customers and really preserve our customers as we ramp up Eastover later in the year. And so it's a cost that shows up in mix because the margins on that either externally sourced or converted paper is a bit lower. So those are the 2 main reasons. And really, we cited this as a one -- the North American piece is a onetime in our February call that we wouldn't expect to have next year as we ramp up the Eastover and the sheeting operations in Sumter.

George Staphos*BofA Securities, Research Division*

Okay. And on the pricing impact?

John Sims
CEO

Make sure I understand your third question was around the pricing and the pricing realization.

George Staphos
BofA Securities, Research Division

Yes. If we just hold where the publications are right now, what would it mean for benefit, if any, price-wise, 2Q versus 1Q or rest of year versus 1Q? However you want to discuss it?

John Sims
CEO

Sure, George. So we announced increases across all the regions. So I think it's best if we just go around the regions to talk about what we saw and what we're in the process of realizing from what we've announced to our customers. So in North America, we communicated a price increase of 5% to 8% range to our customers. We're realizing that increase within that range. We began to -- we start to see that in March, and it's going to go through the bulk of it, we'll see that in the second quarter coming through. In Brazil, we announced a 5% increase on cut size for January, and we realized about 2/3 of that in the first quarter.

In the other LatAm markets, we communicated about a 7% increase for Q1, and we realized about 1/3 of that in the first quarter. And that's about all we're going to get from that one, but we did announce a second increase of 7% to customers for the second quarter we will start to realize that in May. In Middle East and Africa, and we export this from -- mostly from Brazil, but also some from our European operations, we implemented a 4% increase in the first quarter. and we realized that in the first quarter, and we're implementing a second increase for the second quarter, which we should start realizing in May.

And in Europe, we communicated a 4% increase to our customers in the first quarter. And in Europe, we actually saw prices go down in the first part of January. And then we started to see -- realize this 4% increase, and we'll get about half of it through April. And that's probably about all we're going to get from that first increase. However, we communicated the second increase of 8% effective in May, and we expect to start realizing that in the second quarter.

George Staphos
BofA Securities, Research Division

And you'd rather not give us a dollar number for 2Q versus 1Q at this juncture given all of that.

John Sims
CEO

That's right. Yes.

Operator

Your next question comes from the line of Matthew McKellar with RBC Capital Markets.

Matthew McKellar
RBC Capital Markets, Research Division

A couple just on costs. Could you speak to the input and transportation cost pressures you're seeing compared to where you were at the start of the year, what does that incremental headwind look like on an unmitigated basis? And what amount do you expect to be able to mitigate in some way? And then just circling back on Nymolla debarker, what's the ongoing cost impact there before you can address that in Q4? And is that just a cost issue? Or are there constraints on production as well?

Don Devlin
Senior VP & CFO

Thank you, Matt. This is Don. I'll take those questions. So relative to cost and input and transportation, --

what -- so the cost in Q1 was relatively small. But as we look forward and for Q2, in particular, we think it will be about \$15 million, and that's across things like chemicals, energy and distribution. And it's split fairly evenly across our regions. So roughly \$5 million per region. And for Nymolla, so this debarking drum issue, it occurred in March.

We're incurring about \$1 million to \$2 million a quarter of additional cost. And the plan is to do the repair in September. And so the fourth quarter, we should see improved costs. And really what we're doing is we're -- we have no impact to production as we're sourcing external chips, and that's the incremental cost.

Matthew McKellar

RBC Capital Markets, Research Division

Okay. And maybe just as a follow-up there, the \$15 million you called out, is that essentially the sequential impact that we should expect quarter-on-quarter? Would you describe, I guess, the run rate cost impact any differently based on current costs?

Don Devlin

Senior VP & CFO

It would be roughly that amount sequentially in Q2, yes.

John Sims

CEO

And Matt, these are costs that are due to the Iran war situation. So how that plays out going forward, it's anybody's guess, but that's what we see at least for the first quarter -- second quarter.

Don Devlin

Senior VP & CFO

Yes. And Matt, we had less than \$2 million, \$1 million to \$2 million of what we would call war-related inflation in Q1. So it's 15 versus 1, call it, so roughly incremental. 14.

Matthew McKellar

RBC Capital Markets, Research Division

Okay. Okay. Fair enough. And then one more for me, and I'll jump back in the queue. Pretty high-level question. You talked about having the potential to generate \$300 million of annual free cash flow. When we think about your investments and expansion in Eastover, investment in LatAm fiber supply, lean transformation and now prices inflecting in all regions, particularly maybe in North America where conditions seem quite tight. What else still needs to change in the market or in Sylvamo specifically to drive you to that \$300 million level in 2027, at least on a run rate basis, particularly if we strip out some of the remaining \$15 million or so of Eastover spend, I think you said trickles into the next year and maybe any ramp-up of your investments as well.

John Sims

CEO

Yes. So Matt, it's John. I think you captured most of the big items. So certainly, the Eastover investments and what we're doing there, the better mix in Latin America on shifting exports from EMEA to U.S., improving mid-cycle margins, particularly in Europe, but also down in Brazil and the OLA markets, the other LatAm markets, improvement there. Lower cost and improved productivity, which we're going to be driving through the lean transformations, the work that we're doing, increasing reliability and workforce planning and training, lower wood costs, particularly in Europe, and that's really driven by Nymolla because we're seeing the decreases right now coming through.

We talked about it, but we'll provide probably more detail around what we're doing with digital transformation as it pertains really to our mill system as well as on the commercial area. We haven't really explained a lot of that, but we intend to do that in future earnings calls. And then capital spending will normalize. This is after the investment at Eastover, we'll see capital spending come back to normalized

level.

Matthew McKellar

RBC Capital Markets, Research Division

Okay. So I mean, is it fair to say it's kind of continued execution of some of the programs within your control and then markets getting a little better in other LatAm and European kind of regions?

John Sims

CEO

That's right.

Don Devlin

Senior VP & CFO

Yes, I think that's correct.

Operator

Your next question comes from the line of Daniel Harriman with Sidoti.

Daniel Harriman

Sidoti & Company, LLC

I just wanted to follow up on Matt's last question. I think the \$300 million cash flow target for '27 was -- came out prior to these price increases across all 3 of your regions. So just wanted to get a sense from you of where you see the stock's valuation right now and other uses of that cash. I know there hasn't been any share repurchases in the past 2 quarters. I'm not sure if that has to do with the leverage ratio you want to get to prior to getting back into the market.

And then also around tariff sensitivity, based on the 10% tariff that's in place through July '24, just curious how you're thinking about the second half if that tariff structure changes either way or gets worse, would you go back to importing from Europe? Or are you exploring other opportunities as well?

John Sims

CEO

Daniel, let me talk about the \$300 million. So if you remember even from my CEO letter and based on that was expectations that we expected that the markets' margins, particularly in Europe, would normalize. It wasn't sustainable with where the margins are in Europe and also in the other LatAm markets. So that was built into some of that when we think about the \$300 -- achieving the \$300 million of cash flow.

Don Devlin

Senior VP & CFO

I would add to that, Daniel, that a large portion of the path to this 300 million is Eastover. We pointed out in our previous earnings call in February, the onetimes that we're experiencing, but you're also -- we'll also see the benefits of additional volume from Eastover, which is our lowest cost mill. So a large portion of the 300 million will be Eastover operating after the speed up in the new sheeter, and that's a significant portion of the \$300 million. And relative to -- we never said 2027. I think this \$300 million is a goal for us in the future as the way John stated in his CEO letter.

John Sims

CEO

Yes, but within 3 to 5.

Don Devlin

Senior VP & CFO

Within 3 to 5 years, yes. So relative to the stock -- where we see the stock value and if I step back and

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think about our cash situation for the year and our capital allocation strategy philosophy. We look at 2026, we've got big commitments both in the Eastover. Prior year, we returned last year, 350% of our free cash flow to shareowners. We're managing cash levels as we focus on executing the Eastover footprint transition. We're making big strategic investments at Eastover. We want to make sure we have a strong balance sheet through 2026.

I think our philosophy around share buybacks is the same, and it's that if we believe it's our intrinsic value, the share is trading less than our intrinsic value, then we will do buybacks. I think 2026, we're being prudent to manage through a very uncertain year with tariff changes, with economic changes and the Middle East conflict impacts as well. And I think we got to navigate 2026.

John Sims
CEO

But Daniel, let's be clear that we believe that our share price right now doesn't reflect the intrinsic value of the company. We believe it's undervalued. But we're taking a very conservative approach to cash just because of the issues -- not the issues, but the fact that we're in this transition period, so there's a big use of cash in the first half of this year. We've got a war and uncertainty. So we're taking a conservative approach with our balance sheet. And so we're deferring more to that than we are to taking an opportunity to buy back our shares.

Don Devlin
Senior VP & CFO

And I think to your last question, Daniel, today, relative to the tariffs, today, the paper products from Brazil are subject to a 10% tariff under the Section 122, and it's consistent with the tariff applied to other countries. But as of today, that expires late in July, July 24. We expect the administration will apply new tariffs on Brazil before that expiration of the Section 122 tariff.

So it's difficult to predict what level the Brazil tariffs will be set. There was a Trump and Lula meeting yesterday, and the preliminary feedback is positive, but it still doesn't give an indication. I think that the way we're thinking about this is we have flexibility at the 10% level, it makes a lot of sense for us, and we'll continue to do that. If it goes to a different rate, we'll have to reconsider what we're doing for the balance of the year after July.

Operator

Your next question comes from the line of Michael Roxland with Truist Securities.

Niccolo Piccini
Truist Securities, Inc., Research Division

This is Nico Piccini on for Mike Roxland. First off, on Europe, I think you've mentioned in the past that business has been more of a bet on the future. And I'm just wondering how you see the path to improving earnings there and your thoughts on the business, especially as your peers in the area are either contracting or reorganizing given the weaker supply-demand dynamics? And then how is the -- when is that slated to be in the kind of lean transformation process?

John Sims
CEO

So thank you for your question. Can you repeat your second one? I'm not sure, but what was your second question?

Niccolo Piccini
Truist Securities, Inc., Research Division

Yes. So the -- when does that fall in the lean transformation process that you're already doing in Latin America and are going to start doing in North America in 2Q?

John Sims
CEO

Let me address the first question about the Europe question. So yes, it's a bet on the future because we believe that over time, the industry will continue to consolidate and become more hospitable to earning above cost of capital returns. In Europe as it does consolidate as the market declines. And that, of course, isn't right now the case. It's a market that is very fractured and margins are low. We are focusing on what we can control, and it's really specific to each of our -- 2 of our facilities. So in Saillat, we've been focusing on significantly reducing fixed cost and also improving our mix of products, shifting more out of commodity cut size into more of the value-added roll business, which has higher margins and also into other type of grades there, and we're executing that, and that is going actually better than planned in terms of the mix improvement.

At our Nymolla mill, it's about reducing our wood costs. We've -- when we purchased that mill, there was an agreement that the wood was going to be supplied from a joint venture, Sodra, we have moved away from that, taking control of our own sourcing of our own wood. We've seen wood cost has come down, and we're expecting that to continue to move. We're also increasing the yield and working on consuming less wood. We've also exported in cheaper wood from the local sources, putting a lot of efforts into reducing our wood cost there and also improving our operational efficiencies at our Nymolla mill.

We believe that these moves with the increasing pricing and margins there will improve the business. going forward. And I think your second question was around the lean transformation. And where we started -- this is -- we expect the lean transformation to be a 3-year process, but we expect to get immediate and significant report results in the areas that we start to implement that. We started at Mogi Guacu mill here just recently. We've already got target improvements in certain areas that is around almost a 50% improvement in certain areas.

But as I shared with you in the presentation, we're rolling that out here and going to be in North America at the corporate areas, we'll be going back to Brazil. And then next year, early next year, we'll be in Europe as well as at the Eastover mill. I'm not sure if that answers your question, but on the lean transformation.

Niccolo Piccini
Truist Securities, Inc., Research Division

Yes. No, that's helpful. I appreciate it. I just have 2 additional follow-ons. One is on the mix issue in North America in the first quarter, given that's related to the kind of the Eastover 4Q downtime and the Riverdale conversion, should that change quarter-to-quarter, like Q1 to Q2? I apologize if I missed that earlier. And then the second one is if you can comment how your relationship is with your large shareholder.

Don Devlin
Senior VP & CFO

Yes, Niccolo, I will take the first question relative to the mix. We do expect that to continue into Q2. And so what we're doing is we're making sure we have the inventory to enable us to serve customers as we get through as the Riverdale supply agreement goes away. And as I said, the Eastover speed up in sheeter installation in Q4. So we're preparing to get through that big outage, which is 45 days at Eastover. So we'll build more inventory in Q2. It will look similar.

John Sims
CEO

And then I think your second question was around our largest shareholder, happy to take that. Actually, in the first quarter, I did meet with them, and I'll share with you that they expressed to us they continue to support our strategy and have confidence in the management change. They were very supportive of my CEO letter and thought we were spot on in terms of what we're focusing on and the long-term value creation targets of greater than \$300 million of free cash flow and a 15% return on invested capital. So I would characterize our relationship with Atlas is very positive, and they continue to be very supportive of our strategy. And in fact, we continue to meet on almost on a quarterly basis. We expect to meet this quarter where we continue to get their feedback, guidance and... on the company, and we do appreciate

their feedback.

Operator

Our next question comes from George Staphos with Bank of America Securities.

George Staphos

BofA Securities, Research Division

A few follow-ons. So first of all, Eastover, are you still on track for \$50 million? Should we expect that in 2027? How is that going in terms of the value generation from that?

John Sims

CEO

Yes. So George, thanks for asking the question on Eastover. Yes, everything is on track, as we said. So everything is moving on schedule within the budget that we planned from the capital spending, and we're expecting installation in the fourth quarter. And as we said, the sheeter is actually going to be landing here shortly, and we'll start to install that and start to ramp up in the training of the crew and getting that ready to operate by the time the Eastover is ramped up. And so we do have a ramp-up schedule. So the \$50 million, we still are 100% behind that number. It will ramp -- you won't see the full \$50 million in the first year because there will be a ramp-up period, but you'll see a significant portion of that in 2027.

Don Devlin

Senior VP & CFO

And George...

George Staphos

BofA Securities, Research Division

\$40 million, would that be significant as you see it, John? Sorry about that Don.

John Sims

CEO

Yes. Yes, that's directionally right.

Don Devlin

Senior VP & CFO

Yes. And just to add to that, George, the reminder of the onetimes go away. So you have the ramp up of the benefits and then the onetime costs go away. So Eastover improve next year is significant. Onetimes that we in refer in here.

George Staphos

BofA Securities, Research Division

Yes. The \$85 million, which is now \$65 million, if I'm correctly reframing, okay, great. reminding. Okay, perfect. Second question. So with lean programs, right, my time covering the sector, usually, you put in lean programs when things are relatively smooth, right? It's continuous improvement. at Sylvamo right now, I know you're working on this, but you've got a lot of individual fires you're trying to put out. You've got the digester and power issues in South America. You've got debarking issues. You're trying to bring up Eastover. Why are you putting in a lean program now? Wouldn't it be better to...

John Sims

CEO

Well, that's a good...

George Staphos

BofA Securities, Research Division

I mean everything is established and then you can do continuous improvement on a baseline?

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John Sims
CEO

George, I think the way we think about it is that first of all, we're going to have reliability issues. We want to minimize that as much as we can. But we believe that right now, where we are with our operations and our facilities, we certainly can fully implement the lean management system going forward. But we have a very engaged, highly engaged crew and team. We believe there's a lot more opportunity to really tap into the talent of those teams. And that's what lean does because it's an employee-driven continuous improvement. When I talk about being legendary in pursuing world-class excellence. We need every employee to be able to help us do that. And that's why we're implementing the lean it's the best mechanism, we think, from a cultural perspective to really tap into the talent, and we do have a very talented team. I think that's one of our strengths.

George Staphos
BofA Securities, Research Division

John, no doubt about that.

John Sims
CEO

We would think it's a miss, George. Yes. We think it would be a miss for us not to tap into it now to wait. And generally, we believe that we're not in a crisis mode, right? It's -- we have an issue that hit us really hard in the first quarter, but it's not a systemic issue that we would want to wait to implement our lean journey.

George Staphos
BofA Securities, Research Division

Okay. I appreciate that. What incremental benefit should we get out of lean? You've had other cost reduction programs. What do you get next year incremental from lean to the bottom line at Sylvamo? And what do you think you get on an ongoing basis?

John Sims
CEO

Well, we think that we could achieve probably double the improvement rate that we have been achieving, but that's when we fully implement it. So we're looking at 3 to 5 years. So as we ramp it up, we think we can double the improvement rate, which we need to do. I mean what we've been faced with is not just us, but across the industry and across the industrial sector is increased rates of inflation and costs that's making the previous rates of improvement is not at the levels that it needs to be to sustain margins.

George Staphos
BofA Securities, Research Division

Yes. John, I appreciate that. And we applaud that you're taking care of the house no matter the environment. But I was just trying to get a sense of what's behind the program, what benefit. And I know you said you get 2x the improvement, but what does that mean in terms of dollars? And then kind of my last question on this round, I appreciate you taking all these questions. Does there get to a point and when Europe just becomes -- I don't know how to say it, but too much of a drag relative to the performance you're seeing elsewhere in your operations and you need to think even more significantly about its place in the portfolio. So how much benefit from lean dollar-wise? And when does Europe become too big of a drag?

John Sims
CEO

George, from a dollar-wise to your question on the lean, we really haven't really talked about and publicly disclosed what our improvement levels are from a year-over-year and what our targets are. I'm hesitant to do that going forward. In terms of Europe, I think you -- we always -- and we have to, we continuously

evaluate our portfolio as part of our capital allocation strategy and philosophy when we look at it as we -- I think I talked about on the last call and also we're looking at all options. We have to. We're looking at can we operate differently, how fast can we accelerate the improvements, are there things that we can do differently.

And I think the question you raised is something we always -- we've got to continue to do, and that's look at the portfolio and does it make sense and are we -- is the right to be in Europe because ultimately, we want to drive value for our shareowners. But I can tell you right now, as we sit today, we believe that we have the right strategy that we're pursuing in Europe, and we think we've got the right leadership team. We're committed to our customers there, which we have very strong customer relationships with. So we -- our strategy right now is to continue to improve the performance of that business.

Operator

Your next comes from the line of Matthew McKellar with RBC Capital Markets.

Matthew McKellar

RBC Capital Markets, Research Division

Just one follow-up, please. With how tariffs have evolved and assuming, I guess, they don't change in magnitude from here. So whatever happens after Section 122 looks something like the 10% level, would you expect to continue to supply some amount of Latin American paper into North American markets even after the Eastover expansion ramps up? And maybe just relatedly, what's your sense of how imports into the U.S. might be evolving more broadly, just at an industry level with tariffs resetting lower?

Don Devlin

Senior VP & CFO

Yes, Matthew, I'll take the first part of your question relative to -- so we -- relative to the Brazil imports. So we do -- if the tariffs are in the right range for us at 10% is -- it works, we will continue to import from Brazil into North America. It's part of the supply plan even after the Eastover speed up. So it will be part of the plan. And it makes more sense for us if you think about low margins of Brazil exporting into Middle East and Africa versus bringing it to North America. And we have a pretty wide range on what makes sense from a tariff standpoint. So we'll continue to import.

John Sims

CEO

Matthew, I think you asked -- did you ask what is the import situation in North America with the trend? Was that your second question?

Matthew McKellar

RBC Capital Markets, Research Division

Yes. That's right. Just at an industry level and post the IEEPA tariffs coming off.

John Sims

CEO

Yes. So we did see imports increase at the beginning part of the year. They got up to around 16% of demand, but we've seen a steady decrease of imports coming into North America, and it's roughly dropped down to the lower end of what's been typical at the lower end of the range, around 10% of total demand. And some of that is driven because of the tariffs. The other is -- some of it is impacted by the Iran war. So it's increasing freight costs, but also there was a mill that exported to the U.S. from that area that's not operating as a result of the war.

Matthew McKellar*RBC Capital Markets, Research Division*

Okay. So even over the past month or so, there doesn't seem to be any kind of inflection in import activity that you're aware of despite, I guess, the tariffs moving lower and you kind of attribute that to in Atlanta and maybe transportation costs downstream of that?

John Sims*CEO*

That's right. So that's why we've actually seen imports continue to decrease, and we expect that to happen. There's a mill also in Finland that was exporting a lot of volume, I think 30,000 or so tons annually to the U.S., and that mill has been indefinitely idled as of November last year. So there's some little bit of things like that, that also have decreased the imports.

Operator

We have reached the end of our Q&A session. Thank you. I'll now turn the call back over to Hans Bjorkman for closing comments.

Hans Bjorkman*Vice President of Investor Relations*

All right. I'll let John do a quick wrap up here, and then we'll let you get on to the rest of your day.

John Sims*CEO*

Yes. Thanks, Hans. And again, thank you for joining the call. As I said, 2025 and '26 will be low points in our free cash flow generation as 2026 is a transition year for us. And it also will be a year of 2 halves. In the first half, we will be impacted by the transition costs plus input costs, while the second half should see improved pricing and margins and mix improvements across all our regions. This will be a year where we're executing our most significant investments in our Eastover mill that will drive a lot of value in the years to come.

We have launched our lean transformation and focusing on exceeding our customers' expectations and driving improvement across our operations. We are focused on long-term value creation that will generate strong and sustainable results. by executing our flagship growth strategy and disciplined capital allocation. And as I said, as industry conditions turn, our capital spending normalizes and the benefits of our investments begin to materialize, we believe we have the potential to generate greater than \$300 million of free cash flow and greater than 15% return on invested capital. So again, thank you for joining. I hope everybody has a good day. Bye.

Hans Bjorkman*Vice President of Investor Relations*

Thank you.

Operator

Thank you for participating in Sylvamo's First Quarter 2026 Earnings Call. You may now disconnect.

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