

THE SPIN-OFF REPORT

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UPDATE: Sylvamo Corp.

Sell-Off in Sylvamo Presents Increasingly Attractive Risk Reward Scenario; Upgrade SLVM to BUY (from NEUTRAL), Maintain \$45 Fair Value Estimate

- On October 1, 2021, before the market open, International Paper Co. (NYSE: IP) completed the spin-off of its printing papers business into a standalone publicly traded company, which adopted the corporate moniker Sylvamo Corp. (NYSE: SLVM).
- IP Shareholders of record as of September 15, 2021, received one share of SLVM for every 11 IP shares owned. IP retained a 19.9% stake in SLVM with the expectation that IP will ultimately monetize its ownership position.
- Since the close of the first day of regular way trading, shares have declined 24.8%, with total volume of 15.8 million shares having been traded. Over the same time period, the S&P SmallCap 600 has declined 0.9%.
- Our initial NEUTRAL recommendation was rooted in the belief that investors in pre-spin IP would likely exit their ownership position in SLVM for a variety of reasons, including the lack of a dividend at Sylvamo, its inclusion in the S&P SmallCap 600 versus IP's S&P 500 membership, and the printing paper industry's structural issues (i.e., the secular decline demand for printing paper).
- Given the recent decline in share price, we think the current quote represents an attractive risk reward scenario for investors who may be shorter term in nature.
- In terms of valuation, at the current price shares trade at 4.4x our 2022 EBITDA estimate, while other paper companies trade at 6.8x average. We believe the forced selling dynamics resulting from the spin-off will ease over time and shares of SLVM will trade in closer proximity to the peer group.
- We do note that continued selling may occur before our expected return to a peer trading multiple as total shares traded since beginning regular way only represents 36% of Sylvamos's 44 million shares outstanding.
- From a sampling of recent spin-offs, initial high-volume trends typically trail down towards a normalized trading level (in terms of shares traded per day) over a six to eight day period following the distribution, irrespective of the price direction. Given this framework, shares of SLVM could see around four more days of "heavy" volume before reaching a normalized/sustainable volume level, which could be an indicator that the shareholder rotation has been mostly completed and the supply demand has normalized.
- Investors interested in initiating a position in SLVM may wish to average down if the selling pressure persists through this initial period of shareholder rotation.
- In support of our view that shares may be reaching a tipping point on selling pressure, we point to the company's ability to generate free cash flow. Pre-COVID the company generated more than \$400 million in annual cash flow in 2018 and 2019. Through 1H 2021 free cash flow has totaled \$190 million. Assuming a normalized free cash flow generation capability of \$400 million shares currently yield

Sylvamo Corp. - BUY

Current Share Price (10/6/21): \$24.80
Ticker: SLVM

Fair Value Estimate: \$45 per share

Shares Outstanding: 44.4 million
Market Capitalization: \$1.1 billion

Market capitalization at current share price.



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~16% while peers trade with free cash flow yields closer to 12%. By our calculation, if SLVM were to trade at a 12% free cash flow yield (and generate \$400 million in free cash flow) the shares would be valued at \$44 per share.

- We acknowledge the structural issues within the printing paper industry, however SLVM's vertically integrated business model allows for the company to be a low-cost producer, which should be viewed positively versus peers.
- We fairly value shares of SLVM at \$45 per share by applying a 6.0x multiple to our unchanged 2022 EBITDA estimate of \$563 million.
- For more details, please refer to *The Spin Off Report* dated August 27, 2021, and UPDATE on October 1, 2021.

Exhibit Sylvamo Corp.: Fair Value Estimate

(\$ in millions, except per share data; shares in millions)

	<u>Sylvamo</u>
2020 Revenue	\$ 3,009.0
Growth	10.0%
2021 Revenue	3,309.9
Growth	2.0%
2022E Revenue	3,376.1
Margin	11.5%
Operating Income	388.3
D&A	175.0
EBITDA	563.3
Multiple	6.0x
Enterprise Value	3,379.5
Net Debt	1,403.0
Market Capitalization	1,976.5
Shares Outstanding	44.4
FVE \$ / Share	\$ 44.56

Source: Company reports, Bloomberg, and *The Spin-Off Report* estimates.

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Disclosures

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