Sonoco Products (Q2 2024 Earnings)
August 1, 2024

Corporate Speakers
- Lisa Weeks; Sonoco; Vice President of Investor Relations
- Howard Coker; Sonoco; President and CEO
- Robert Dillard; Sonoco; CFO
- Rodger Fuller; Sonoco; COO

Participants
- Matt Roberts; Raymond James; Analyst
- George Staphos; Bank of America; Analyst
- Ghansham Panjabi; Robert W. Baird & Co.; Analyst
- Mark Weintraub; Seaport Research Partners; Analyst
- Gregory Andreopoulos; Citi; Analyst

PRESENTATION

Operator^ Good day. And thank you for standing by. Welcome to the Q2 2024 Sonoco Earnings Conference Call. (Operator Instructions)

Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today, Lisa Weeks, Vice President of Investor Relations.

Please go ahead.

Lisa Weeks^ Thank you, Operator. And thanks to everyone for joining us today for Sonoco's Second Quarter Earnings Call.

Last evening we issued a news release highlighting our financial performance for the second quarter. And we prepared a presentation that we will reference during this call.

The press release and presentation are available online under the Investor Relations section of our website at sonoco.com.

As a reminder, today's call we will discuss a number of forward-looking statements based on current expectations, estimates and projections.

Statements are not guarantees of future performance and are subject to certain risks and uncertainties.

Therefore actual results may differ materially.

Please take a moment to review the forward-looking statements on Page 2 of the presentation.

Additionally, today's presentation includes the use of non-GAAP financial measures which management believes provides useful information to investors about the company's financial condition and results of operations.

Further information about the company's use of non-GAAP financial measures including definitions as well as reconciliations to GAAP measures is available under the Investor Relations section of our website.

Joining me this morning are Howard Coker, President and CEO; Rob Dillard, Chief Financial Officer; and Rodger Fuller, Chief Operating Officer.

For today's call we will have prepared remarks regarding our results for the quarter and our outlook for the third quarter followed by a question and answer session.

If you will please turn to Page 5 in our presentation, I will now turn the call over to our CEO, Howard Coker for business update.

Howard Coker^ Thank you, Lisa. Good morning, everyone. And thank you for joining our call today.

As we announced late yesterday, we had a solid quarter, where we delivered sequential improvement in adjusted EBITDA and [earnings]. In the second quarter, sales were $1.6 billion, adjusted EBITDA was $262 million and EBITDA margins remained strong at 16%.

Our adjusted earnings per share were $1.28 and operating cash flow was $109 million. These results reflect improved industrial volumes on a year-over-year basis.

Mixed with some continued softness in consumer sales. During the quarter, we had continued price cost headwinds across the portfolio, primarily in industrials that we believe will improve in the second half.

Productivity in the second quarter came in at $51 million, continuing our strong operating trends and bringing our first half productivity total to just over $100 million. All in all, another good quarter from the Sonoco team.

If you'll please turn to Page 6. Let me now update you on recent progress with our near-term strategic priorities.

As always, we're fully committed to operating with discipline.

Our productivity results in the first half of the year were over $100 million. These figures are ahead of schedule to our expectations for the year they were not by chance.

As you know we have doubled internal CapEx in the last three years, targeted towards value driving growth and productivity projects.

We continue to make high-return investments to drive better and more efficient manufacturing processes, and those investments are paying off.

Our sort of actions to improve productivity from the right capital allocation portfolio simplification and strong expense management continue to yield results, and I couldn't be more pleased with the efforts from the entire Sunoco team.

We also continue to invest strategic capital and innovation to support organic growth and sustainability initiatives.

At the recent environmental packaging live event, we were awarded the 2024 Gold Award in snacks and confectionery packaging and the Silver Award for sustainable packaging innovation for a greater than 90% paper Pringles Canvas.

We're delighted to be recognized for our proprietary designs that help our customers achieve their sustainability packaging goals. This new design is being rolled out in store shelves across Europe and will be launched internationally in the near future.

Regarding high-return capital investments, we're pleased to announce the acquisition of Eviosys in late June, representing an important milestone in our strategy to scale our can packaging platform. The approval and review processes are well underway, and Roger and team are making great progress on planning for a seamless integration. Touched on the current schedule, we expect to close the transaction in the fourth quarter of 2024.

If you'll turn to Page 7, the Eviosys, we're excited to expand our footprint and global capabilities to address the increased demand for innovation and meet growing expectations for the highest levels of customer service. The addition of Eviosys will position us as one of the leading food can and aerosol packaging manufacturers globally, and it represents a platform where we can drive differentiated value in the market by leaning into service, quality and innovation, the absolute hallmark of successful Sonoco businesses.

The combination of our existing innovations infrastructure and EBS' technical advanced and well-invested manufacturing footprint will be more effectively serve both existing and new customers. and unlock new opportunities in attractive end markets and geographies.

We've initially identified meaningful near-term operating and procurement synergies that should drive roughly $100 million annually. And this does not include expected

commercial and innovation synergies. The financial profile of this combination is compelling.

The transaction will be immediately accretive to earnings and cash flow. And first year returns are expected to be well in excess of our cost of scope.

But most importantly, it gives us strong, a powerful operating platform from which to advance both commercial and operating improvements. that will help us continue to drive sustainable value and returns to our shareholders, further demonstrating the strength of our clear and dynamic capital allocation process.

Our businesses continue to identify and bring forward exciting opportunities for value-generating investments. The clarity of our dynamic process will continue to support these opportunities. Where Sonoco can generate strongest return and value proposition for shareholders. And you will see us continue to distance ourselves in businesses that do not regularly offer the same opportunities.

We view capital allocation as a part of our strategic planning process to generate increased value for our shareholders, and we'll keep you fully posted on our progress.

With that update, I'm going to turn it over to Rob to talk about financials for the quarter. Rob?

Robert Dillard^ Thanks, Howard.

I'm pleased to present the second quarter 2024 financial results, starting on Page 9 of this presentation.

Please note that all results are on an adjusted basis and all growth metrics on a year-over-year basis, unless otherwise stated. The GAAP to non-GAAP EPS reconciliation is in the appendix of this presentation as well as in the press release.

As Howard said, we continue to deliver resilient financial results through our enduring operating model and strong market positions.

Adjusted EPS was $1.28, which was within our guidance range and exceeded the consensus analyst estimates. This result was driven by positive productivity of $0.38 per share and positive volume mix of $0.09 per share.

Offset by negative price cost of $0.37 per share.

Sequentially, we drove 14% growth, EPS growth through $0.05 of volume mix, $0.11 of price/cost and $0.08 of productivity. Which was partially offset by $0.11 of specific other costs.

For the quarter, net sales decreased 4.8% to $1.62 billion due to negative contractual resets and price and negative $101 million of strategic actions to exit or divest nonstrategic positions. Excluding these strategic actions, net sales would have grown 1.1%.

We believe that divesting the Protective Solutions business exiting nonprofitable thermoforming markets and reclassifying the recycling business, increase our ability to focus and execute our strategy.

It's notable that volume mix was positive low single digits in the quarter as low single-digit volume increases in consumer and double-digit volume increases in industrial overcame declines in all other.

Organic volume/mix was flat as low single-digit increases in Industrial offset low single-digit declines in consumer and declines and all other.

We continue to experience negative contractual resets and price as paper, metal and some resin benchmarks have declined from their peak.

In the quarter, price impacted sales negative $32 million. We anticipate that year-over-year price comparisons will improve as the year progresses. Adjusted EBITDA was $262 million, and adjusted EBITDA margin was 16.2%.

The Specific other expenses that we believe were onetime in nature were higher $23 million due to increased employee expenses, bad debt reserves and other accruals.

For a year-over-year comparable EBITDA margin would have been 17.6% excluding these specific other expenses. This gives us conviction in our expectation that EBITDA margins will improve in Q3 as we expect volume mix and productivity to improve and volume mix, price/cost and productivity to improve on a sequential basis.

In the second quarter, we achieved historically strong profitability through improving volume mix and strong productivity despite challenging price cost.

From an EBITDA perspective, volume mix was positive $5 million in the quarter. This was the first positive organic volume mix for EBITDA in eight quarters. Productivity was positive $51 million in the quarter. In the last 12 months, we have achieved over $180 million of productivity.

We believe that this performance is an indication that our strategy of investing to drive earnings growth through productivity is working, and we anticipate that this trend of positive productivity will continue. Price cost was negative $49 million, primarily due to industrial. We anticipate the price cost will improve as the year progresses.

Page 10 has our consumer segment results.

Our consumer businesses continue to improve profitability through productivity and commercial execution despite uneven volume. Demand is improving, but promotions at retail have yet to stimulate demand to legacy trends across all sectors. Consumer net sales decreased 4% to $928 million. Consumer volume mix increased low single digits due to the NPL acquisition and positive organic volume mix in flexibles and metal packaging.

Consumer price decreased 2% due to contractual price resets. We expect these pricing trends to continue for the remainder of the year. Consumer EBITDA increased 11% to $148 million, primarily due to improved productivity.

Our capital investments in consumer are generating meaningful results and the first sequence of investments from one to two years ago was a primary driver for the improvement in productivity to $25 million.

Consumer EBITDA margin increased 216 basis points to 15.9%. We anticipate that EBITDA margins will increase in Q3, as volumes continue to normalize and metal packaging entered its primary pack season.

On a more granular level, RPC sales declined low single digits due to low single-digit volume mix decline.

We anticipate that this will continue through the balance of the year, and we are taking appropriate actions to ensure profitability. [PFP] Sales decreased mid-single digits as positive mid-single-digit organic volumes in flexibles and strong acquisition performance from NPL partially offset the impact of the exit of a nonprofitable thermoforming market.

Metal Packaging sales decreased mid-single digits as positive low single-digit volume mix was offset by negative contractual price resets. Volume mix was positive in both food and aerosols.

We expect metal packaging volume mix to increase double digits in the third quarter. Volume was positive mid-single digits, excluding onetime customer reserves in Q2.

While metal packaging price was negative on a sales basis, on an EBITDA basis, price/cost was meaningfully positive.

We expect positive price cost on an EBITDA basis in metal packaging for the remainder of the year.

Page 11 has our Industrial segment results.

Industrial market conditions are improving. And while we are optimistic, we believe that we are still in a U-shaped industrial market trend and that there has not yet been a broad-based market recovery.

Industrial sales increased 3% to $601 million, volume increased 10% and organic volume mix increased 2%. These results include the reclassification of recycling which reduced sales by $23 million in the quarter.

Adjusted for the impact of recycling and reclassification, industrial sales would have increased 7%.

Industrial price decreased 2% due to contractual price resets.

Industrial EBITDA was $98 million due to $47 million of negative price costs, offsetting $23 million of productivity and $15 million of positive volume mix. Between 2019 and the end of 2023, industrial price costs increased $184 million. And year-to-date in 2024, industrial price cost has decreased $102 million.

We believe that we are now close to a balanced price cost position and that future trends will be positive based on strategic pricing.

We believe that this is evidence that our pricing strategy in industrial is working and we expect price cost will trend positive over the long run.

We continue to seek market price increases to offset higher OCC and other inflationary inputs.

We anticipate paper benchmarks will accurately reflect the inflationary environment and improving market conditions in the second half of the year.

Industrial EBITDA margin was 16.3%.

We believe that industrial margins will continue to improve with volume recovery and future pricing actions. Page 12 has our results for the -- our Other businesses. All other sales were $95 million due to volume mix declines and the sale of the Protective Solutions business.

Our other EBITDA was $17 million due to lower volume mix and negative price cost offsetting $3 million of productivity.

Moving to Page 13.

Our capital allocation framework aligns with our business strategy to drive value creation through earnings growth and margin improvement. The four pillars of our capital allocation model are capital investment to drive growth and improve profitability, dividend increases to reward shareholders, programmatic M&A to action portfolio strategy and share repurchases to return capital and maximize shareholder value.

Our goal is to be the most disciplined deployer of capital in our industry and to drive the highest ROIC and strong cash conversion while also returning capital to shareholders. To achieve this goal, we remain focused on our dynamic capital allocation strategy.

We believe that this strategy is working and that the productivity results we are now generating and the growth that we are anticipating are indications of the success.

As Howard mentioned, our long-range planning and capital allocation process continues to yield great results.

We have a meaningful amount of highly strategic, high-return capital opportunities, primarily in our RPC and metal packaging businesses.

As we evaluate these opportunities, we will continue to tighten our focus on fewer bigger businesses.

As a result, we are planning to expand our divestiture program. And we believe that we have the potential to yield more proceeds from divestitures in the next 12 to 18 months than the previously expected $1 billion.

As previously communicated, we believe that we have a strong base plan to finance the Eviosys acquisition, which we anticipate will close in the fourth quarter.

We believe that expanding our divestiture program has the potential to further accelerate our portfolio simplification strategy, improve our pro forma leverage and increase shareholder value.

As always, we are being disciplined in our strategic activity. And we expect to provide further updates as our plans progress.

On Page 14, we have our cash flow performance for the quarter.

In the second quarter, we generated operating cash flow of $109 million. Capital expenditures was $93 million for the quarter.

We're on track with all major initiatives and anticipate investing between $350 million and $375 million in 2024.

Over the past few years, we've updated our capital allocation process to focus on strategic, high-return value-adding projects.

As we improve this process, we are allocating an increasing amount of capital to value-adding projects versus value maintaining projects.

We anticipate that this capital efficiency will enable us to maintain this level of capital investment even as we increase our scale.

Turning to Page 15. The foundation of our value creation strategy is disciplined management of our investment-grade balance sheet. This strategy provides Sonoco incredible access to capital, strong liquidity and low cost.

In the second quarter, we have had over $1.4 billion of liquidity, a weighted average maturity of 6.8 years and a weighted average cost of debt of 3.9%.

We repaid $75 million of debt in the quarter and reduced net debt to adjusted EBITDA to 2.8x.

On Page 16, as our guidance for Q3 2024. Guidance for Q3 2024 adjusted EPS is $1.40 to $1.60.

We expect consumer volumes to remain on trend in Q3 and expect year-over-year volumes to increase due to acquisitions and improvements in metal packaging.

We expect industrial volumes to improve in Q3 as we are experiencing improved order rates and backlogs, especially in the North America paper markets.

However, we are not yet anticipating robust recovery. Industrial price trends are expected to improve and price cost is expected to improve sequentially.

OCC is expected to remain flat in the quarter and [hand] bending chip index is expected to reflect market increases later in the second half of 2024.

We are reaffirming our guidance for full year 2024 adjusted EPS and to $5 to $5.30.

Similarly, we are reaffirming our full year 2024 adjusted EBITDA guidance to $1.05 billion to $1.09 billion, and our operating cash flow guidance of $650 million to $750 million.

Now Roger will further discuss the outlook for the business.

Rodger Fuller^ Thanks, Rob.

Please turn to Page 17 for a review of segment performance drivers for the third quarter, of 2024.

In the consumer segment, we expect sales to be up both sequentially and year-over-year. Our metal packaging business is performing well. Sales are expected to be up sequentially and year-over-year.

(Inaudible) sales are solid as we're entering the pack season for fresh vegetables and Aerosol sales are strong as the demand for household products is improving after destocking in the same period in last year.

We continue to monitor fuel supply based on domestic constraints and tariff uncertainties, but our team is doing a great job to support our customers through strategic purchasing execution.

In rigid paper containers, we see sales up marginally year-over-year with some sequential improvement in North America from snacks and other discretionary food products.

We believe lean green and high share prices continue to mute consumer purchases, and we're looking to the future for promotions to stimulate higher volumes.

As Howard mentioned earlier, we continue to invest and innovate to meet sustainable packaging goals of our customers and have a multiyear funnel of great opportunities to support future rigid paper can growth.

In our thermoform Flexible Packaging business, we anticipate sales to be flat sequentially but up year-over-year. Less was organic volume is solid and total volume is aided by the NFL acquisition in Brazil, which continues to perform above our expectations.

We remain in the early stages of our integration of flexibles and thermoforming businesses, and we continue to see upside opportunities and synergies for combining these businesses well into the future.

So in total, for the consumer segment versus same quarter last year, we anticipate that organic volumes will be up mid-single digits. Price cost will be slightly negative year-over-year, and we expect continued positive productivity across each of our consumer business.

In Industrial, we expect sales to be flat sequentially from last year and up year-over-year from organic volume growth and acquisitions.

In our North American paper business, volumes in support of tissue and tile consumer end markets remained solid. The capacity utilization of our North American paper operations will remain strong in the third quarter at well over 90%. The same is true for our North American converting businesses, where volumes are up year-over-year, increased demand in our tubes and core business for the industry, which is driven by both consumer and industrial end markets.

As Rob said earlier, there's certainly not a robust recovery, but volume levels have increased over the depressed levels that we saw last year.

Price cost is impacting industrial profitability to a lesser degree than the first half of 2024. There remains a drag year-over-year as higher input costs for raw materials and labor have not yet fully been recovered in our announced price increases, but we do expect that the contracted price resets will reflect improved pricing in the second half of the year.

Similar to consumer, we expect industrial productivity to be positive across all industrial businesses in the third quarter, and we expect total industrial volumes up low single digits year-over-year.

In all the other sales will be lower on a year-over-year basis after the sale of our Protective Solutions business.

Sales will be up sequentially from seasonally higher volumes from our temperature-assured packaging business.

We also expect year-over-year margin improvements driven by improved mix and profitability.

Our teams continue to do a real fantastic job on the productivity front, as shown by our first half '24 results.

As Howard mentioned earlier, our clear and focused investments in value-generating capital over the last several years are really paying off. These investments, coupled with effective cost management and a strong focus on continuous improvement across the organization have also underpinned outstanding productivity performance. And I just want to -- as well as Howard and Rob have done, thank the entire organization for these results.

So with that, Howard, back to you.

Howard Coker^ Great. Thanks, Roger.

In closing, on Page 18, I just want to take a moment to remind everyone of the plans we laid out to deliver long-term shareholder value.

At our Investor Day earlier this year, we provided our outlook over the next five years.

We're targeting adjusted EBITDA of $1.5 billion with high teens EBITDA margins.

We're expecting to generate cumulative operating cash flow of $4 billion to $5 billion, all while we remain committed to growing and paying a competitive dividend.

We are in full execution mode of our next era enterprise strategy. And certainly with the highly strategic Eviosys transaction, we expect to deliver results in excess of these targets.

We're building a stronger portfolio that delivers greater value, simplifying the company and unifying our global operating model to improve financial results while maintaining our disciplined capital structure.

So we're really looking forward for you to see what's next for Sonoco.

And with that, Operator, we'd be happy to take any calls or questions.

QUESTIONS AND ANSWERS

Operator^ (Operator Instructions) Our first question will come from Matt Roberts of Raymond James.

Matt Roberts^ Good morning, everybody. And thank you for the time, Rob, on the incremental divestitures you mentioned, I was wondering if you could provide any additional color on either product lines or segments that you've expanded that program to and any type of EBITDA contribution you're considering just trying to get a sense of the magnitude of what you're looking at and what the business will look like on the other side.

Operator^ I'm here on the line with you. You may answer your question.

Howard Coker^ I'm not sure where we are in terms of the Q&A process. So Matt, is your question still pending?

Operator^ I will move Matt Roberts back to the stage. And Matt Roberts line is open. He is on the stage.

Matt Roberts^ So still on the first question, really just…

Rodger Fuller^ Operator, I'm not sure what's happening here. Matt, or audio wasn't working. Bill wasn't working.

I think you need to re answer.

Operator^ (Technical difficulty) And George's line has been promoted.

George Staphos^ Always nice to be promoted. Can you guys hear me okay? I can ask a question, but I'm not sure they'll hear it.

Operator^ Please ask your question, and I'll promote them back to the stage.

George Staphos^ Okay. I think I was going to ask the same question as Matt, which is, can you talk to what else you were adding perhaps to the divestiture queue. And Rob, maybe a specific question on ROIC. You talk about ultimately want to be the most disciplined capital allocator and have the highest ROIC in the industry.

What is the starting point for ROIC in your view? Where are you relative to peers? And what's the goal in three years? So the divestitures in ROIC kind of my two questions.

Howard Coker^ Our position at this point in time to talk about specific businesses that we're targeting our thought processes have evolved as we look at the materiality of the current transaction acquisition and really allows to -- force us the opportunity to take a look at two things: one is to pull forward on the strategies that simplification strategy where we have yet to define to you guys exactly what we're looking at. And I know you're trying to get to that, but we do -- we will be bringing it to in the very near future.

But it allows us to do a couple of things. One is move forward the simplification strategy and improve the capital structure of the company.

On a more rapid basis than otherwise we had thought. So more to come on that side, and I will pass it on to Rob on the ROIC question.

Robert Dillard^ Yes. Yes. Thanks, George, and hopefully, I've been promoted to -- from a ROIC perspective, we're really excited about this capital allocation program and the initial results that we're getting.

It's given us a lot of conviction to really move forward with the strategy from a portfolio perspective. And as we think about that, that's going to give us a lot of opportunity to further expand the ROIC on two fronts.

One, from doing really smart capital investments and deploying our operating model. And then also managing the portfolio in a really active way. Where we're starting now is we're above 11%.

So we feel like that's a strong ROIC but one that we can definitely improve. We don't have a specific goal, but I would tell you that the focus businesses in our portfolio have over 20% ROIC. And so we're investing with expectations that the ROIC of our investments exceed that, and we feel really good that we'll be able to meet those expectations.

Operator^ In one moment for our next question, which comes from Ghansham Panjabi.

One moment.

Ghansham Panjabi^ Thank you. I'll just ask one question just to eliminate future issues.

On the consumer business, maybe you can give us a bit more color on the step function and productivity that you generated in which I think was $25 million for the segment versus 15% in 1Q.

What drove that differential because that was obviously the biggest component of your margin increase? And then second, in terms of the outlook for Consumer, I think you said mid-single-digit growth in the back half of the year.

Is that just a function of purely easier comparisons, the lapping of inventory destocking or just directional increase in promotional activity? What's behind those numbers? And I'll turn it over after that.

Rodger Fuller^ That's where we focused. The tremendous amount of our capital, productivity capital focus on generating incremental capacity out of our best lines. Automation is a huge effort for our consumer businesses.

We've got a backlog of automation projects for the company expanding until the end of 2025. And then a real focus on cost control and getting our footprint right, with a number of footprint consolidations.

You add that with improving volume, as we said back in February. If you remember, back in February, we laid out $300 million to $500 million of productivity over the planning period, which averages about $100 million a year.

Obviously we're ahead of that pace. We said at that time, improving volume would help us increase and continue to drive to the high end of that $300 million to $500 million level.

So just -- I'd say it's across the company, not just consumer, but yes, very strong. It was manufacturing productivity, driven by the plants on a day-to-day basis.

On second half consumer, you're right, some of that is versus an easier, I guess, comparison with third quarter last year being our most difficult quarter from a consumer volume standpoint.

But as I said in my prepared comments, we're seeing the effects of any kind of inventory build through coming out of COVID, especially in our metal can business go away. All our teams are leading in service and quality, and we continue to gain some share in that area.

So yes, it's a combination. We've not yet seen a big impact of promotions, but we're expecting that, based on what we hear from our large consumer customers to see more promotions coming as we get into the second half of the year.

Operator^ Thank you. And our next question should come from Mark Weintraub of Seaport Research Partners.

Mark Weintraub^ Thank you. So I'm hoping you can hear me now. So just following up on the expanded divestiture program, does that potentially have implications for the plan to issue up to $500 million of equity. And then second, on rigid paper containers, I know you've been very optimistic on the business six months, 12 months ago and certain -- I thought there were certain opportunities you thought were going to be coming through this year. Are those just delayed?

I know you mentioned the high shelf prices, but maybe a bit more color on what's going on in that business.

Howard Coker^ (technical difficulty) But we could with the appropriate valuation in terms of divestiture, draw that down.

So I'll leave that where that is and on our paper container business, really, it's almost a discrete issue. With a couple of larger customers still dealing with the pricing dynamics in the marketplace and getting that right.

So we view that as a short-term type of phenomenon really, when we're talking about RPC and the amount of capital we have been putting towards that business, that's next year, following a multiyear journey in terms of new facilities that are starting up in Latin America and Asia, new capacity we're adding around the world, just like any capital investments, it will take time for those just truly start showing up in a material fashion, but the current situation is more discrete than that.

Rodger Fuller^ Yes. Mark, this is Rodger, I'd just add.

If you look at the third quarter, I mean there is actually strong growth in the rigid paper can business outside of North America. Just to build on what Howard said, the really a North American issue the discrete issue that Howard talked about.

So the investments we're making, driving sustainable packaging across Europe and paper, investing in stacked chip capacity outside of North America is performing exactly as expected. So really, it's just waiting for that North American volume to get back to more normal levels.

Operator^ And our next question will come from Gregory Andreopoulos of Citi.

Gregory Andreopoulos^ Good morning, everyone. Just a few quick ones for me.

So just on consumer, I guess, first, you spoke about kind of this modest uptick in discretionary categories in the second quarter. I think snacks were referenced. So I'm wondering if you've seen any other mix trends that you would consider notable in consumer that maybe suggest to you that there's some underlying shift in consumer trends going on? Or any other mix items that you think are worth flagging -- and then maybe just one more on productivity. Year-to-date, you've gotten over $100 million. How do you think about the cadence of productivity versus the $300 million to $500 million that you guided to at the Investor Day for '24 to '28. And just kind of -- has your productivity came in above or below your expectations? And is that kind of pull forward from the $300 to $500 million? Or is that incremental -- is there incremental upside to those numbers? I'll turn it over.

Rodger Fuller^ Yes. It's Rodger. On the consumer volume, I think the only to highlight, if you look at cocoa pricing, any chocolate type products from our customer base have been hit by significant inflation.

So as we look at promotions and price on shelf, any chocolate type products we're seeing continue to be in a pretty high range, and that's generating, obviously some pullback from the consumer. Beyond that, other than the one item that Howard has already mentioned in North America, we're seeing -- starting to see some improved demand versus same time last year and quarter-over-quarter outside of North America.

So for me, again, it's really a North American specific challenge and hopefully, promotions and some pullback on pricing on the shelf will help -- will help with that.

On productivity, I wouldn't really call it a pull forward. I think, again, we said in February, we had a range of $300 million to $500 million that we could push towards the top of that range with excellent execution and good volume, and we're starting to see volume improve.

Obviously we can come back and relook that and see if we can improve on that.

So it's again, it's an impact from the capital investments we're making, the good work our team is doing. And I think the other significant event this year, on the industrial side is a great job our paper team is doing in North America from a capacity utilization standpoint.

As you know we've taken out some high-cost capacity, put more product into our lowest cost, best running mills. And we've been running in that mid-90% capacity level for the last few quarters, and that generated some pretty significant productivity for our paper business as well.

So I think for me, those would be the highlights versus what we've already talked about.

Operator^ Our next question will come from Matt Roberts of Raymond James.

Matt Roberts^ Hopefully, you all can hear me this time. So a question on paper price. So last quarter, when you spoke to this, you guys were constructive on the February increase that was been partially reflected in the index shortly thereafter. So maybe if you could speak to what you're seeing in the recently announced price increase. Are you seeing that reflected in open market contracts -- and how is -- how are demand and backlogs trending compared to the environment last quarter when the price was reflected in the index? And then to that, does the outlook or the guidance anticipate any index pass-through?

Rodger Fuller^ Yes. I'd say it's fairly similar. We just talked about capacity utilization in the -- in our North American paper mills. AF&PA just published the latest results for the second quarter. You see backlogs continue to be pretty solid, pretty flat with where we were same time last quarter.

As far as open market pricing, we've been very pleased with the contracts that we have in our open market.

And both of the increases, we've got a high yield out of the first and in process getting high yield out of the second.

So as Rob said in his prepared remarks, we're expecting some of that to come through from an index pricing in the second half of the year, timing to be determined, of course, but we expect it to come through.

We didn't build it into our guidance, but if it comes through in the next month or two, it'll have an impact really late this year but a more significant impact on 2025.

So I'd say at this point stable, pretty table where we were in the second quarter. And as far as mill utilization pretty stable to where we were in the second.

Matt Roberts^ Okay. Great. Other kind of just to a different point here. On your leverage, in regard to maintaining your investment grade. It seems like you do have some buffer where your current ratings are to maintain that investment-grade rating. But is there some kind of minimum leverage number or benchmark throughout the next 24 months post close that you think you need to achieve in order to maintain that investment-grade rating? And along those lines. I mean maybe holistically, why is that so important when some of your other peers don't stress it as much. I mean do you have any needs for your incremental debt here or any covenants depending on maintaining that existing rating?

Robert Dillard^ Yes. That's a good question. Certainly we don't feel there is no bright line in terms of leverage for investment-grade ratings.

We have really constructive dialogues with both S&P and Moody's. And we think that those are really productive discussions that we've had and we'll continue to have around the rating. They feel very comfortable with kind of the prospective plan for financing Eviosys -- and as we said on the call we're continually thinking about shareholder-friendly ways to improve that financing plan.

And we think that really revolves around besides just advancing the strategy and really thinking about the portfolio we would -- we're creating plans to delever more quickly than we originally anticipated.

And as Howard mentioned, we're also evaluating the use of equity whether or not that's going to be the most efficient source of funding for us.

So we're being very thoughtful about that, and we've got a very constructive relationship with the rating agencies. They do have kind of their own benchmarks around what they would like and they publish those.

But I would say that that's part of the constructive dialogue that we have with them because, we're both a paper company and a packaging company from that perspective. And we think as we become more of a packaging company, we'll have a lot more way in terms of ratings, and that's a really constructive dollar that we have there.

Operator^ (Operator Instructions) And our next question will come from George Staphos of Bank of America.

George Staphos^ Three quick ones. First of all, can you talk to the other specific expenses that impacted second quarter and why they go away for the third quarter.

As far as potential divestitures go, question two, could some of these actually occur within the consumer segment as it's currently composed? And how would you deal with any trapped overhead the investment that you made in the past on your innovation centers, which leverage paper and flexibles and metal.

And my last question on ROIC, Rob, back to that I know you want to be the strongest ROIC company. I know you're at -- you said 11% or 12%. Why not have a goal, if that's what you aspire to be, why not have a percentage target that we can keep evaluating?

Robert Dillard^ Yes. Thanks, George.

On the other specific expenses, it was really around a couple of very discrete items, one was just some employee expenses that were extraordinary really on a year-over-year basis. They were just lower last year than you would normally expect.

Second is the -- we had an AR charge that was specific to one customer that we really wanted to be conservative around the expectation for receiving that.

And so we took a relatively meaningful charge. And then we're also kind of constantly evaluating the accruals, and we had an accrual that was meaningful as there was a catch-up from a change in a rate. And so those things all kind of sum to a relatively meaningful amount for the quarter, which we thought was extraordinary and worth calling out just for a comparable basis.

Really, the point there that if you -- we don't expect those to reoccur and that in the third quarter, you should anticipate our margin to be much higher than it was in the second quarter, more in line with the proxy that we gave.

In terms of divestitures?

Howard Coker^ Yes. I think, yes, it could be in the consumer area. And George, I'm sorry, it sounds like we're being coy, we are.

We are in the midst of having to manage a process that involves internal team members, customers, et cetera, and we'll be rolling out sooner practical, exactly what our plans are,

but we -- we do expect, as we said several times during the course of this call this should be -- will help us do two things.

One, our goal of simplification as well as the overall balance sheet implications and financing structure. So more to come on that.

Second part, need to ask for a follow-up. But [expanded] cost [I was saying] we were referencing, we see that as a real opportunity across the entire company as we further simplify as we saw in our first tranche that we -- where we came down with the structures that we have today, we generated significant SG&A productivity -- this is further leverage as we continue to -- so I don't see a real concern as it relates to any type of stranded costs if that was indeed request. It's actually opportunity

Robert Dillard^ Yes. And on ROIC, George, I love you, you're a finance guy at heart. We love to have targets and we definitely do internally. We're constantly thinking about how we can put the edge.

It's a big part of our strategy to get the ROIC right. As we get the portfolio more balanced we can come out with the total company expectation for ROIC.

But as I said, we think that it's going to be a really constructive number that will be will really show the value of the legacy portfolio that we have and also the ability that we feel like we're going to have to drive really meaningful value in some of these newer businesses that we're really investing in now.

Operator^ (Operator Instructions) I'm showing no further questions. I'll hand it back to management for closing remarks.

Lisa Weeks^ Thank you all for joining us today. And our sincere apologies for the technical difficulties. We will certainly follow up on that for future improvement.

But if you do have any follow-up questions, please contact me, and we'll be happy to set up a follow-up discussion. And we look forward to providing further business updates on our progress in the coming weeks and months.

And thank you all again, and have a great day.

Operator^ This concludes today's conference call. Thank you for participating. You may now disconnect.