Packaging & Paper/Forest Products

BofA Global Ag & Mats Conf: Upgrading IP, PKG, & BALL to Buy

Rating Change

04 March 2024

Equity
United States
Packaging

George L. Staphos
Research Analyst
BofAS
+1 646 855 4495
george.l.staphos@bofa.com

Cashen Keeler
Research Analyst
BofAS
+1 646 855 4256
cashen.keeler@bofa.com

Lucas Hudson
Research Analyst
BofAS
+1 917 861 6981
lucas.hudson@bofa.com

Presentations + panels drive more positive view

Following our BofA Global Agriculture & Materials Conference, we raise International Paper (IP), Packaging Corp. (PKG) and Ball Corp. (BALL) to Buy. Company and panel presentations suggested a containerboard upcycle has begun, supporting our recent Boxmaker Survey, while bevcan comments were fairly positive regarding North America. And while there have been lower entry points for the names in recent quarters and multiples are high for BALL and PKG (we discuss), given our POs, upward tension in fundamentals, and a still-Neutral consensus rating for the three, we upgrade. New forecasts and additional points are at right and below, while conference-day reports are available for IP, for PKG and for BALL. Our top picks are SEE (SEE), Graphic Packaging (GPK), Sonoco (SON) and O-I Glass (OI).

Containerboard/paper cycles look better

Ahead of “Pricing Friday” in February, we published our survey discussing why industry pricing and demand should improve (pricing increased $40/ton). At the conference, PKG discussed that billings were up 10%, up from the +8% cited during 4Q reporting. It also announced a $100/ton uncoated free sheet (UCFS) hike and Buy-rated Sylvamo (SLVM) was also positive on UCFS. PKG's multiple is high but an upcycle is ahead – our Equity Strategy team has seen this elsewhere in the market. Meantime, IP continues to see 3% industry growth in ’24 and relayed that early-1Q is in-line/positive with guidance. With good momentum in its “Value over Volume” initiative (and confidence in its $68mn 1Q estimate), IP also stated that e-commerce, distribution, protein and other markets were better. Meantime, our Containerboard Panel was generally positive on recent demand trends and saw an 88% operating rate (up v. ‘23), as well as some longer-term positives.

Beverage cans improve, BALL getting back in groove

BALL’s comments were generally positive at the conference — versus guidance, volume trends so far in ’24 are in-line or better. While its multiple is high, we are increasingly encouraged with comments that continuous improvement, Kaizen and Lean should return operating leverage to 2x-plus. Quick deployment of its Aerospace-sales proceeds to a debt tender and $1bn buyback this year offsets divestiture dilution and supports a higher multiple, while it remains constructive on new products across aluminium packaging. Neutral-rated Ardagh (AMBP) also stated volume trends were in-line/better.

Updated PO, valuation work; generally raising multiples

Early in a gradual containerboard recovery, we take multiples up ~1x for both earnings and EBITDA while also increasing our growth rates by 1pct. We also increase our normal free cash flow (FCF) estimate for PKG to $800mn from $750mn, partly as we raise UCFS pricing by $50/ton starting 2Q (see Exhibit 3). Given the continuous-improvement thesis and Aerospace points above, we increase BALL multiples by 1-2x. We remove Aerospace earnings, assume $2bn in debt reduction and, partly financed by Aerospace proceeds, assume $3bn in buyback through 2026 (Ball reminded investors a few times that it repurchased 15% of the equity during 2014-16 – 15% of the current cap is $3bn).

Exhibit 1: PO Changes

A summary of PO changes in this report

	Old	New
BALL	$61	$72
IP	$37	$42
PKG	$178	$202

Source: BofA Global Research estimates
BofA GLOBAL RESEARCH

Exhibit 2: EPS Changes

A summary of EPS changes in this report

	2024E		2025E		2026E	
	Old	New	Old	New	Old	New
BALL	$3.25	$3.25	$3.75	$3.75	$4.15	$4.15
IP	$2.10	$2.10	$2.70	$2.70	$2.75	$2.75
PKG	$8.45	$8.50	$9.70	$9.90	$10.25	$10.45

Source: BofA Global Research estimates
BofA GLOBAL RESEARCH

Refer to important disclosures on page 7 to 10. Analyst Certification on page 6. Price Objective Basis/Risk on page 3. 12666572

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Exhibit 3: BofA UCFS Price Forecasts, 2024E-2026E
We raise our UCFS forecasts by $50/ton

	1Q24E	2Q24E	3Q24E	4Q24E	2024E	1Q25E	2Q25E	3Q25E	4Q25E	2025E	1Q26E	2Q26E	3Q26E	4Q26E	2026E
Uncoated Freesheet - 20-lb repro	$1,455	$1,450	$1,450	$1,450	$1,451	$1,430	$1,430	$1,440	$1,440	$1,435	$1,440	$1,440	$1,440	$1,440	$1,440
Uncoated Freesheet - 20-lb repro (old)	$1,405	$1,400	$1,400	$1,350	$1,389	$1,380	$1,380	$1,390	$1,390	$1,385	$1,390	$1,390	$1,390	$1,390	$1,390

Source: Source: Fastmarkets RISI / Pulp & Paper Week, BofA Global Research estimates. All prices per short ton.

Exhibit 4: Companies mentioned
Companies mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
BALL	BALL US	Ball Corp	US$ 64.28	B-1-7
GPK	GPK US	GraphicPackaging	US$ 25.48	B-1-7
IP	IP US	Intl Paper Co	US$ 35.05	B-1-7
OI	OI US	O-I Glass Inc	US$ 17.21	C-1-9
PKG	PKG US	Packaging Corp	US$ 180.19	B-1-7
SEE	SEE US	Sealed Air Corp	US$ 34.76	B-1-7
SON	SON US	Sonoco Products	US$ 56.71	B-1-7

Source: BofA Global Research

BofA GLOBAL RESEARCH

Investment Rationale

Ball Corp.

We rate BALL at Buy as we believe a beverage can rebound is gradually taking shape for 2024-25. Meantime, the company's work towards continuous improvement, including Kaizen and Lean, should return operating leverage to 2x-plus. Furthermore, deployment of its Aerospace-sales proceeds to a debt tender and $1bn buyback (and $3bn buybacks in total that we see through 2026) offsets divestiture dilution and should support a higher multiple.

International Paper Co.

We rate IP at Buy as our research, including our proprietary Box Surveys and BofA Global Ag & Materials Conference company & panel commentary, suggests a containerboard upcycle has begun. IP's commentary suggests trends, after a choppy period, have stabilized and are improving, including the benefits it expects to generate from its "Value over Volume" approach.

Packaging Corp. of America

We rate PKG at Buy as our research, including our proprietary Box Surveys and BofA Global Ag & Materials Conference company & panel commentary, suggests a containerboard upcycle has begun. Further, PKG fundamentals have been stronger than peers, with good momentum in billings and productivity. Lastly, uncoated free sheet fundamentals look like they have begun to improve.

Price objective basis & risk

Ball Corp. (BALL)

Our $72 price objective is based on a three-part valuation approach, which takes: (1) a 19x 2025E P/E multiple, (2) a sum-of-the-parts (SOTP) valuation which values North and Central America at 14x EBITDA, EMEA at 13x, South America at 13x, and Other at 12x, (3) our intrinsic free cash flow (FCF) valuation, which assumes $1.2bn of normalized FCF, 11% cost of equity and a 3% growth rate. Multiple ranges are higher vs. past valuation levels given packaging group valuations and the growth trajectory offered by the beverage can market.

Risks to our PO are (1) increasing operational challenges from new capacity onboarding, (2) potentially increased competition arising from new entrants, (3) BALL's ability to realize benefits from prior capital spending (e.g., new capacity, custom cans, productivity, etc.), (4) input cost volatility including energy cost volatility in Europe, (5) overseas/emerging market risks (for example, currency), (6) demand trends in beverages, including the risks to overall valuation, demand and pricing should growth slow, (7) seasonal-weighting of full-year earnings to the key 2Q/3Q period, (8) potential governmental policy and regulatory changes in the US and elsewhere, (9) increasing risk from Russia and South America.

And, there are numerous macro risks and other risks around volumes, pricing, and input costs.

Graphic Packaging (GPK)

Our $31 PO is based on the average of (a) an EV/EBITDA valuation calculated by applying a 8x EV/EBITDA multiple to our 2024 EBITDA estimate of $1.8bn (our multiple is consistent with where comparable companies have traded), (b) a P/E valuation calculated by applying a 15x P/E multiple to our 2024 EPS estimate of $2.75 (our multiple is consistent with where comparable companies have traded), (c) a free cash flow (FCF) valuation based on our estimate of $676mn in FCF, a calculated cost of equity of 10% and forecast rate of growth of 2%.

Risks to our PO: (1) closing and integration risks associated with the acquisitions, (2) demand trends in food & bev and other GPK end markets, (3) potential volatility in fiber, energy, other input costs, (4) paper/board sector volatility & demand trends, including trade flow volatility created by exchange rates, (5) fundamental trends that could wind up being worse than expected, (6) should trends reverse in the policy outlook for the current Administration, that would present a source of volatility and risk for the shares, (7) various factors associated with its new CRB machine

Also, industry & economic trends could prove weaker or stronger than modeled. Greater-than-expected weakness could lead to valuation multiples and earnings below our forecasts, even as better-than expected trends could lead to a higher relative multiple premium & stock price.

International Paper Co. (IP)

Our $42 price objective is based on an average of (a) an EPS forecast of $2.70 in 2025E and a P/E of 14x, which is consistent with historical ranges, (b) a normalized free cash flow (FCF) estimate of $1bn, a calculated cost of equity of 10% and forecast rate of growth of 2%, (c) our IP sum-of-the-parts (SOTP) value, based on normal EBITDA, which is an average of historical periods 2016-22 and our forecasts through '25E.

Risks to our price objective are (1) the broader employment & macro picture, (2) paper/board sector volatility & demand trends, (3) wastepaper/input cost volatility, (4) trends in the US$ and its effect on trade flows, (5) emerging market risk, (6) operational risks related to investment projects, (7) IP's pension, (8) the potential for new capacity to come into the market, (9) potential volatility coming from any future Administration policy changes. Fundamental trends could wind up worse than expected, causing further downside to the shares relative to our PO. Better performance or macro news could cause the shares to perform better than our price objective.

O-I Glass Inc (OI)

Our $21 PO is based on an average of P/E, EV/EBITDA and intrinsic free cash flow (FCF) valuations. We use a 8x 2024E P/E multiple, a 6-7x 2024E EV/EBITDA multiple, and our intrinsic FCF valuation, which assumes $350mn normalized FCF, 13% cost of equity, and a -3% growth rate. Multiples are in line with those of metal/rigid packaging peers. Similar to CCK, OI has a larger international presence relative to its peers.

Risks to our PO are: (1) unfavorable demand and pricing, (2) the potential for pension or asbestos risks/claims to consume greater amounts of earnings or cash flow, (3) unfavorable international market volatility and FX risks, (4) integration risk with acquisitions, (5) risks in Mexican pricing and pack mix, (6) potential governmental policy changes in the US and other portions of the world. As is the case with all our coverage, packaging and paper/forest stocks are highly sensitive to macro, FX, commodity inflation and other factors which could create variances with our forecasts and POs. Similarly, should the factors discussed above prove less negative or more positive to forecasts, OI's price could exceed our PO.

Packaging Corp. of America (PKG)
Our $202 price objective is based on an average of (a) an EPS forecast of $8.50 in 2024E and a P/E of 20x, in line with peer multiples, (b) a normalized free cash flow (FCF) estimate of $800mn, a calculated cost of equity of 8% and forecast rate of growth of 4%, (c) a sum-of-the-parts (SOTP) value, based on forecast midcycle EBITDA or per ton(ne) replacement values.

Risks to our price objective being achieved are (1) PKG's leverage to economic cycles, (2) containerboard market volatility and demand trends, (3) input cost volatility, (4) demand, supply-chain and other risks created by the Covid-19 pandemic, (5) potential structural changes in the economy, (6) the potential for mill or converting operations to perform less well than anticipated, (7) the potential for new capacity to come into the market, (8) volatility coming from changes by the Administration. While we've tried to be conservative in our modeling, fundamental trends could wind up worse than expected, causing downside risk to the shares relative to our price objective. Similarly, PKG results could wind up stronger than our forecasts, causing the shares to move beyond our PO.

Sealed Air Corp. (SEE)
Our $40 price objective is derived from a three-part valuation approach, which includes: (1) a 14-15x 2024E P/E multiple, (2) a 10x 2023E EV/EBITDA multiple, and (3) our intrinsic free cash flow (FCF) valuation, which assumes $450mn of normalized FCF, 11% cost of equity, and a 3% growth rate. Our target multiples are based on SEE's past trading history and also peer multiples. SEE has been able to trade in the high teens to low twenties on a P/E basis, and a premium to the market when fundamentals improve.

Downside risks to our price objective are (1) risks relative to the company's ability to manage pricing and spreads, given (2) energy volatility, resin price volatility and agricultural market risks, (3) international business risks (approximately 65% of sales derived abroad), including FX and emerging market trends, (4) competitive and other factors negatively impacting volume to a greater degree than expected, (5) risks relative to execution of the company's transformation strategies over the last several years, (6) challenges associated with management transitions.

Overall, energy and commodity volatility represent ongoing risks for packaging companies. Industry and economic trends could prove weaker or stronger than we modeled. Greater-than-expected weakness could lead to valuation multiples and earnings that are below our forecasts.

Sonoco Products Co. (SON)
Our $64 price objective is derived from a three-part valuation approach, which includes: (1) a 13-14x 2024E P/E multiple, (2) an 9-10x 2024E EV/EBITDA multiple, and (3) our intrinsic free cash flow (FCF) valuation, which assumes $600mn of normalized FCF, 10% cost of equity, and -2% growth rate. The P/E and EV/EBITDA multiples are consistent with past valuation multiples within packaging.

Downside risks to our price objective are: (1) potential volatility in old corrugated container (OCC) prices, (2) execution on restructuring and integration initiatives, (3) integration of present acquisitions, (4) periodic volatility in its business, (5) execution of its consumer/growth strategies in packaging, (6) unexpected volume and pricing trends, (7) macroeconomic trends, (8) potential trend reversals related to Administration policies. In addition, energy and commodity cost volatility represent ongoing risk for all packaging companies.

Upside risks to our PO are: (1) Sonoco's ability to acquire businesses accretively, making our forecasts too pessimistic, driving SON above our PO, (2) Additionally, should volumes accelerate while input costs stay benign, this could lead to higher earnings than we are projecting and result in the stock exceeding our PO, (3) The factors noted earlier could play out in a way that causes results to exceed our forecast and drive the shares above our PO.

Analyst Certification

I, George L. Staphos, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

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US - Paper and Packaging Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AptarGroup Inc.	ATR	ATR US	George L. Staphos
	Ball Corp.	BALL	BALL US	George L. Staphos
	Berry Global	BERY	BERY US	George L. Staphos
	Brady Corp. - Cl A	BRC	BRC US	Cashen Keeler
	Crown Holdings Inc.	CCK	CCK US	George L. Staphos
	Graphic Packaging	GPK	GPK US	George L. Staphos
	International Paper Co.	IP	IP US	George L. Staphos
	O-I Glass Inc	OI	OI US	George L. Staphos
	Packaging Corp. of America	PKG	PKG US	George L. Staphos
	Pactiv Evergreen	PTVE	PTVE US	George L. Staphos
	Sealed Air Corp.	SEE	SEE US	George L. Staphos
	Silgan Holdings Inc.	SLGN	SLGN US	George L. Staphos
	Sonoco Products Co.	SON	SON US	George L. Staphos
	Sylvamo Corp.	SLVM	SLVM US	George L. Staphos
	WestRock	WRK	WRK US	George L. Staphos
	Weyerhaeuser Co.	WY	WY US	George L. Staphos
NEUTRAL				
	Ardagh Metal Packaging S.A.	AMBP	AMBP US	George L. Staphos
	Greif Inc.	GEF	GEF US	George L. Staphos
	PotlatchDeltic Corp.	PCH	PCH US	George L. Staphos
UNDERPERFORM				
	Amcor Plc	AMCCF	AMC AU	George L. Staphos
	Amcor PLC	AMCR	AMCR US	George L. Staphos
	Avery Dennison Corp.	AVY	AVY US	George L. Staphos
	Boise Cascade Company	BCC	BCC US	George L. Staphos
	Louisiana-Pacific Corp.	LPX	LPX US	George L. Staphos

Disclosures

Important Disclosures

Equity Investment Rating Distribution: Packaging Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	14	60.87%	Buy	10	71.43%
Hold	6	26.09%	Hold	5	83.33%
Sell	3	13.04%	Sell	2	66.67%

Equity Investment Rating Distribution: Paper/Forest Products Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	9	45.00%	Buy	8	88.89%
Hold	2	10.00%	Hold	1	50.00%
Sell	9	45.00%	Sell	5	55.56%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships [R1]	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

[R1] Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

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Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster[R2]
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

[R2]Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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