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International Paper Company (IP) CEO Mark Sutton on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-31-19 Earnings Summary

Press Release SEC *10-Q* *Slides*

EPS of $1.09 beats by $0.10 | Revenue of $5.57B (-5.64% Y/Y) misses by $-65.34M

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International Paper Company (NYSE:IP) Q3 2019 Earnings Conference Call October 31, 2019 10:00 AM ET

Company Participants

Guillermo Gutierrez - Vice President, Investor Relations

Mark Sutton - Chairman & Chief Executive Officer

Tim Nicholls - Senior Vice President & Chief Financial Officer

Conference Call Participants

Mark Wilde - BMO Capital Markets

Mark Connelly - Stephens Inc

George Staphos - Bank of America Merrill Lynch

Steve Chercover - D.A. Davidson

Anthony Pettinari - Citi

Mark Weintraub - Seaport Global

Gabe Hajde - Wells Fargo

Adam Josephson - KeyBanc Capital

Chip Dillon - Vertical Research

Debbie Jones - Deutsche Bank

Brian Maguire - Goldman Sachs.

Operator

Good morning and thank you for standing by. Welcome to today's International Paper Third Quarter 2019 Earnings Day Conference Call. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, you will have an opportunity to ask questions. [Operator Instructions]

I'd now like to turn today's conference over to Guillermo Gutierrez, Vice President, Investor Relations.

Guillermo Gutierrez

Thank you, Holly. Good morning and thank you for joining International Paper's third quarter 2019 earnings call. Our speakers this morning are Mark Sutton, Chairman and Chief Executive Officer; and Tim Nicholls, Senior Vice President and Chief Financial Officer.

There is important information at the beginning of our presentation on slide two, 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. A reconciliation of those figures to U.S. GAAP financial measures is available on our website.

Our website also contains copies of our third quarter 2019 earnings press release and today's presentation slides. Relative to the Ilim JV and Graphic Packaging investment, slide two also provides context around those financial information and statistical measures presented on those entities.

I will now turn the call over to Mark Sutton.

Mark Sutton

Thank you, Guillermo, and good morning, everyone. We will begin our discussion on slide three. International Paper continues to deliver solid earnings and outstanding free cash flow. Our results again demonstrate the strength and resilience of our cash generation and the flexibility of our company to navigate well in a challenging environment.

Demand in the quarter was mixed. North America packaging improved seasonally, largely as we had expected. However, export containerboard and pulp shipments faced pressure from continued supply/demand imbalance. Operational performance was strong. We took full advantage of our manufacturing and supply chain expertise and managed cost well in our three businesses.

Taking a look at our cash. Through the first three quarters, we generated $1.8 billion in free cash flow and returned nearly $1.1 billion to shareholders through dividends and share repurchases. And we also used $400 million for debt repayment.

Earlier this month, we increased our dividend for a 10th consecutive year, reinforcing our policy of a strong and sustainable payout of 40% to 50% of free cash flow, which is an important part of our capital allocation strategy and a brief update on our portfolio.

Yesterday we announced the completion of the sale of our controlling interest in the papers business in India. We are now passive investors with minority ownership of a company which we intend to fully exit. I want to thank our team in India for their dedication and wish them well in the future.

Continuing with our third quarter performance on slide four, we leverage the flexibility of our system, operated well and controlled costs to deliver $1 billion of EBITDA and margins of 18% in the third quarter. Revenue was down 6% year-over-year due to the impact of lower pricing in our packaging and pub businesses, especially in our export channels.

Our equity earnings were $27 million, which includes $18 million from our Ilim joint venture and about $10 million from Graphic Packaging. Ilim equity earnings were largely as expected and they reflect the impact of lower softwood pulp prices into China.

Free cash flow in the quarter was very strong at nearly $600 million. Through the third quarter, we have generated free cash flow per share of $4.43, compared to just under $4 per share for the full year in 2018.

Now I'll turn it over to Tim, who will cover our business performance and our fourth quarter outlook. Tim?

Tim Nicholls

Great. Thank you, Mark. Good morning, everyone. I'm on slide five, which shows our quarter-over-quarter operating earnings per share bridge. Price/mix was a headwind mostly due to the impact of prior index movements in North American packaging and Global Cellulose Fibers, as well as the flow-through of lower prices for export containerboard.

Volume improved modestly in the third quarter, driven by higher seasonal demand in North American packaging, as well as improved containerboard exports. This was partially offset by lower seasonal demand in our European packaging business.

Operations and cost performance was strong. We continue to optimize our mill and converting networks as we match our production to our customers' needs. We did experience $10 million of additional costs in the quarter related to Hurricane Dorian, mostly in our cellulose fibers business.

Maintenance outage costs were favorable, and input costs were better due to lower fiber costs across our businesses and geographies. Corporate expense and taxes were higher in the third quarter with an effective tax rate of 27% compared to 25% in the previous quarter. Most of this was related to adjustments to the federal tax provision after finalizing our 2018 tax return.

I'll now turn to the segments and start with Industrial Packaging on slide 6. Our business performed well and the North American business earned $525 million with margins of nearly 23%. Across the segment, price and mix was unfavorable, mostly on the impact of prior index movements in North America, and realization of lower export containerboard pricing. Volume was flat. Improved volume in North American packaging and containerboard exports was offset by seasonally slower demand in Europe as well as weaker demand in our packaging business in Turkey.

In North America, box demand improved seasonally. We had strong double-digit year-on-year growth in e-commerce and the protein segment continues to perform well. Process food improved modestly, but beverage, nondurables and durables remain weak.

In October, we've seen a slight pickup in demand. Overall, we're confident in our commercial outlook and the trajectory of our growth as we move into the coming year. The segments we serve, our customer portfolio and recent business wins add to our confidence.

Containerboard export shipments also improved in the third quarter, although a bit less than we expected. Underlying demand was actually pretty good, but customer inventories took longer to draw down.

Operational performance was strong. We leveraged the flexibility of our system and control costs effectively to mitigate the impact of economic downtime in the quarter as we adjusted production to meet our customers' needs. And finally, wood and recovered fiber costs were favorable versus the prior quarter.

I'd like to come back to containerboard exports for just a moment on slide 7 and give you a regional view on how we see things shaping up. Underlying demand has improved throughout the year generally as we expected, while inventories took about a quarter longer to normalize than we anticipated and have pressured shipments through the first three quarters.

Summarizing the regional dynamics. In Latin America, more favorable weather conditions are contributing to better crop harvest for bananas and other agricultural products that require kraftliner to go to market. In Europe, customer inventories took essentially three quarters to normalize while demand improved modestly.

Shifting to Asia. In China, demand remains sluggish as tariff uncertainties linger. And in other regions in Asia, demand is mixed, although customer inventories are back to normal levels. The takeaway here is that we expect export containerboard shipments to continue to recover, and we are seeing this in October.

Turning to Global Cellulose Fibers on slide 8. Third quarter results were impacted by lower prices across all regions, which was partially offset by better mix on improved fluff pulp shipments. Volume improved by $4 million, also driven by improved fluff pulp shipments in the quarter. Supply/demand conditions remain challenging. And although we see better customer demand, overall industry inventory levels remain high and trade and tariff uncertainties continue to weigh on China demand.

Against this backdrop, we continue to focus on optimizing our system and controlling costs. We ran well and successfully mitigated some of the impact of Hurricane Dorian in the quarter. Operations and cost also includes the impact of economic downtime as we adjusted production to meet our customers' demand. Input costs improved by $6 million.

Printing Papers on slide 9. Overall, the business performed well and delivered earnings of $162 million in the quarter. Across the segment, price and mix decreased mostly due to lower pricing for exports from our Latin American and European Papers businesses. Volume was essentially flat. The seasonal demand pickup in Latin America was a bit less than we anticipated, and lower volume in India fully offset increases in other regions.

In our North American business, we had strong performance in cut size as we continue to ramp up new customer business. However, performance in the roll business was weak due to challenging conditions in commercial printing.

In Latin America, supply and demand conditions are challenging as we enter the fourth quarter due to pressure from pressure from imports, especially from Asia. In North America, underlying demand is decreasing within our expected range of 3% to 4% annually, while the level of imports decreased in the quarter.

Operational performance was very strong. We ran well and controlled the cost across the system. In North America, we also benefited from a favorable LIFO inventory revaluation of about $10 million. And input cost improved on lower hardwood cost in North America.

On Slide 10, the Ilim joint venture delivered operating EBITDA of $113 million and an EBITDA margin of 24% before foreign currency charges. Earnings were impacted by lower export pulp prices as well as the completion of the highest maintenance outage quarter of the year, which also affected volume in the quarter.

Equity earnings were $18 million and were impacted by a non-cash foreign charge on Ilim's U.S. dollars denominated net debt, of which IP's portion was $4 million in the quarter.

So, let's turn to the outlook on Slide 11. I'll start with Industrial Packaging where we expect price and mix to lower earnings by $45 million on the impact of prior year index movement in North America and export price flow-through as well as the negative mix impact of export volume recovery.

Volume is expected to improve by expected to improve by $25 million on improved demand in North America and continued export containerboard recovery. Operations in costs are expected to lower earnings by $15 million due mostly to non-repeats of positive items in the third quarter.

Staying with Industrial Packaging, lower maintenance outage expense is expected to improve earnings by about $45 million and input costs are expected to remain stable.

In Global Cellulose Fibers, we expect price and mix to lower earnings by $30 million on the impact of prior index movement. Overall, volume is expected to be stable with higher fluff volume offset by lower market pulp.

Operations and costs are expected to be flat sequentially with the non-repeat of the hurricane impact being offset by higher seasonal energy cost and inputs are expected to remain stable.

Moving to Printing Papers, we expect price and mix to lower earnings by $25 million, mostly in our North American and Latin American businesses. Volume is expected to improve by $20 million on stronger seasonal demand in North America and Brazil.

Operations and costs are expected to lower earnings by $40 million related to the higher seasonal energy consumption across our papers portfolio as well as the non-repeat of LIFO benefits in the third quarter. And input costs are expected to improve by $10 million on lower fiber cost in North America and Brazil. Lastly, under equity earnings, you will see the outlook for the Ilim joint venture.

Slide 12 summarizes our full year outlook. As we continue to perform well in uneven global environment, our focus is on free cash flow generation and executing our framework for capital allocation.

For the full year, we expect EBITDA of $3.8 billion and we expect free cash flow to be $2 billion. On capital allocation, through the third quarter, we've returned about on $1.1 billion to shareowners through dividends and share repurchases and we've used another $400 million to strengthen our balance sheet.

And earlier this month, we also increased our dividend. Looking ahead, you can expect our capital as allocation choices to be consistent with our framework.

With that, I'll turn it back over to Mark.

Mark Sutton

Thanks Tim for covering the details on the quarter and for the outlook. As I always do at the end of our call, I'd like to just close with a few thoughts about the company and quarter.

Our solid earnings and outstanding free cash flow in the third quarter, I think, again, demonstrates that we built a really resilient company that can perform well in just about any environment. And while the U.S. economy remains healthy, we've been managing through some inventory headwinds and broader trade tension that are impacting our exports.

That said, our focus at International Paper is to execute well and maximize results in any environment. For us, that means being relentless about our pursuit of long-term value creation for our shareowners by focusing on free cash generation and executing our capital allocation strategy with that free cash flow.

And for our businesses, that means managing well what we can control, exceeding our customers expectations and strengthening our value proposition, making sure we optimize the full value chain and running our manufacturing network well and leveraging the strength and flexibility of our mill and converting systems. When we put all of this together, we perform well and generate very strong free cash flow.

Our free cash flow per share is up year-over-year. Our strong execution in the company's LIBOR allows us to raise our full year 2019 free cash flow year 2019 free cash flow outlook to $2 billion. We had unique capabilities to drive to just about any challenge we may face. Most importantly, we have the people, the innovation, the products and a low-cost high quality system to succeed with fantastic customers.

And with that, we are ready to take your questions.

Question-and-Answer Session

Operator

[Operator Instructions] Our first question will come from the line of Mark Wilde, BMO Capital markets.

Mark Wilde

Thanks. Good morning Mark, good morning Tim.

Mark Sutton

Good morning.

Timothy Nicholls

Good morning.

Mark Wilde

Mark, just kind of staying on the free cash flow theme, I wondered, if you are in a position to give us any thoughts on the sort of CapEx as we move into kind of 2020 and kind of wrapped up with that. What do you think the proper kind of maintenance CapEx is for IP kind of across the cycle? I think you're about 70 to 80 of maintenance capital for this year?

Timothy Nicholls

Hey, Mark, its Tim. It's a good question. We are still -- we're getting close, but are still finalizing what 2020 is going to look like and we'll report that out when we release fourth quarter earnings. Question on maintenance capital, depending on the schedules, these are big pieces of equipment that have different time lines. So are always looking to make sure that we are being balanced by what an asset needs, but also recognizing that there is flexibility in timing. And we're always looking at how we can do it for less money in terms of outage schedules, how we use contractors, how we use our own labor. So it can go up and down, but there is some flexibility there that we can realize over time.

Mark Sutton

So I would just add to what Tim said, Mark. One of the objectives we shoot for on the whole maintenance subject and as we look at that is protecting today's cash flows and making them sustainable, there's the CapEx piece, but there's also the expense piece. And what we try to do is make sure we use our resources effectively, so we lower the total cost of maintenance. And it's all cash, and we try to lower the total cost. So if the CapEx solution can solve a recurring maintenance expense issue, it's probably the right thing to do to go ahead and eliminate that issue. So we really do look at it holistically.

Mark Wilde

Okay. And then just to follow-on, Mark. You did call out an overhead reduction of about $20 million and I don't recall having heard about that initiative before. So perhaps you could give us a little color on that and what the trajectory might look going forward?

Timothy Nicholls

Yes, it's Tim again, Mark. I'd just say its kind of normal practice. We had some charges last year due to restructuring. We're always looking at how we deploy across the organization for what we need to run the business and try to get better and do it at a lower cost with better processes. So there's initiatives underway. We don't promoted them. We don't talk about them broadly, but its just continues improvement and trying to make sure that we don't spend any money that we don't need to. So that's really the charge in the third quarter. And the charges in the third quarter, because we know where there is going to be impact, the savings from that charge will play out over a series of quarters as we implement.

Mark Wilde

Very good. I will turn it over.

Operator

Thank you. Our next question will come from the line of Mark Connelly, Stephens Incorporated.

Mark Connelly

Your price cost performance in the containerboard was excellent again, despite all the down time. Is there any reason you would change the way you manage that downtime if we have to continue at the sort of levels? I'm just wondering if there's things that you do that work in the short run, but that you don't want to do longer term to keep those level of performance so high?

Mark Sutton

That's a great question, Mark. I think the way we try to look at it on the output of our system, especially containerboard given its so large, as we look at things that are structural versus cyclical, and obviously, if you that there are structural changes in the amount of containerboard, we needed to supply all of our box customers and open market customers, then you probably do some things differently.

But right now, we believe we built the system, through the last few years by integrating warehouse and integrated temporary then kind of normalizing our capability at the mills and taking a real focused view on marginal cost that we have lack of a better term, we have a throttle on the company

We can run wide open, we can run less than wide open, and we can shed certain types of costs and variabilize a lot of things that used to look fixed. So for us its whatever we believe about the near term and long term growth and the fundamentals in the industry and right now we see what's happening right now is mostly cyclical, not structural.

Mark Connelly

Okay. The performance there has really been excellent and the throttling effect is clearly massively different than what you've been able to do historically. My second question is a simple one. You are dealing pretty well with the challenges in the pulp market. Are you seeing any difference in the way customers are thinking about contract terms in terms of pass-throughs or anything else?

Mark Sutton

I think there’s always some discussion on how the commercial arrangements are constructed. When you’re in the moment of the excess pulp supply, sometimes customers do want to revisit the way contracts are structured. Usually the conversation goes to a normalized period and not just a cyclical high or low.

So there's always discussions on that, Mark. And I am able to say one thing. What we're seeing in the targeted markets we have, which is the absorbent products, it really is becoming very customer-specific and what type of economics, they're looking for based on their go-to-market strategy for that baby diapers and the other products.

And they’re not all the same and years ago I use to see much more of a similar approach or desire by most customers. But we are seeing it segment into unique commercial types of conditions.

Mark Connelly

Great. Thank you very much.

Operator

Our next question from the line of George Staphos, Bank of America.

George Staphos

Hi, everyone. Good morning. Thanks for all the details. Hey, Tim, hey, Mark, I thought I heard you mention during your prepared remarks that there were some recent win, I think you mentioned related to the containerboard business. If you could comment a bit more in detail, if there's something that we should keep in mind there and relatedly, I think you said your business is up modestly in October. But if you provide a bit more color about what you're seeing in the containerboard, especially domestically and then I had a follow on.

Tim Nicholls

Yes, George, it's Tim. It's actually speaking to our box business for were constantly working with customers about innovative solutions and how we address their needs and there is a cadence to these things. They don't neatly follow quarters, even multiple quarter sometimes, but we've been very active this year on -- with our commercial team, talking with customers in some cases, existing, and some cases new. And a number of wins that we've had for the box business that will start coming through over the next few quarters. So that was what I was relating to in the prepared comments. We feel really good about the teams win so far.

George Staphos

Okay. And just related point. How are you doing in July did you say – July and October?

Tim Nicholls

Well, July, I can tell you about that. October was a little bit better. We don't have a clear view on shipments. We have a clear view on what we're processing through our facilities, and so, when we close the month we'll see how much of that flow directly to customers versus preparing inventories for seasonal demand, especially around e-commerce. But yes, we saw a slight uptick in demand for October and feel good about it. We think it's going to be a good season for the fourth quarter.

George Staphos

Okay. And related question, I'll turn it over. The wins that you’re seeing is there any kind of common denominator in terms of what IP is offering that might be somewhat different than what's being offered in the market? We tend not to hear so much from IP on how your narrowing systems and machinery with your corrugated business, is there any benefit that you’re getting there? Can you just give us a bit more color in terms of why you're winning this business recognizing it doesn’t always come in smoothly? And how sustainable that is going forward? Thank you, guys.

Tim Nicholls

Yes, thank you, George. We do because of our size and where we service customers, we do some of everything, and we do most of them in a very big way, so yes, machinery and yes, all types of innovative solutions. Innovative solutions are really important customer by customer for what they need, not for creating something that tried to go sell across the entire space.

Mark Sutton

I think just to add on that George, the approach we're taking with the large segment that tend to be the faster-growing segment like e-commerce, like protein, some of the things that IP has build over time, our scale and our reliability as a supplier and then bringing some innovation on top of that has allowed us to grow our position with customers that we already have a very large position with and we try to earn at that every single day, every interaction. And I would give a lot of credit, maybe it's not differentiated. I can’t speak for other companies. I would give a lot of credit to the IP people that served these customers.

We have employees that are embedded with some of our customers, helping them solve the problems, helping them run package at faster rates. And I think that really works well for us, when we bring the full skills of IP to our customers. When I made my prepared remarks, I said something about leveraging and optimizing the entire value chain, and this is what we mean by doing that. It's not just the product, but it’s how we provide the service and how we give even some of our Human Resources to our customer, our manufacturing team, for example, even go out and help customers in their manufacturing operation if it's applicable.

George Staphos

Very good. It’s very solid quarter. Thank you, very much.

Operator

Our next question comes from the line of Steve Chercover, D.A. Davidson.

Steve Chercover

Thanks and good morning. I wanted to actually focus on the specialty cellulose business. So first of all, can you just remind us what you thought the mid-cycle earnings or EBITDA potential of the segment was post Weyerhaeuser?

Mark Sutton

So I think what we said on our few quarters ago that we believe that that business had a $600 million EBITDA potential, and we still believe that. We are in a period right now of some disturbances in the softwood pulp market and absorbent pulp is not immune to that. It affects both the pricing and also affects demand. So we believe that, that still an achievable objective. I'll remind you though, Steve, one of the things we stated as a strategy is to have our business at about 85% of our capacity focused on absorbent pulp. So fluff pulp in the specialty grades that are kind of a bubble for fluff pulp and the product continue. We're only about 74% right now. So are making some products, market pulp products and other products that they're not long-term products for us given the North American fiber and cost structure.

And the only place we really plan to make nonabsorbent pulp is in our mill in Canada, which makes a high-quality northern softwood. So we got a pretty clear strategic path. We've lost a little bit of time given this kind of softwood supply issue of time given this kind of softwood supply issue globally and the commercial things we talked about globally and the commercial things we talked about from last year. But we are very convinced that this is going to give International Paper the right growth profile. It's a great product line, the types of things that go into, and we believe he can get the business to that point. It's just going to take us all bit of time.

Steve Chercover

Okay. Thanks for the detail there. And I'm not trying to change dramatically -- it looks like we're going to start 2020 from a pretty low point. So I'm wondering are there anything -- any plan you have to do in place to improve results? And are you still being impacted by the commercial slow power or whatever you want to call it that impacted you earlier this year?

Mark Sutton

So the exit rate of 2019, you're right, will put us in a challenging position. And yes, we have commercial initiatives. The good news is we're commercial initiatives. The good news is we're commercial initiatives. The good news is we're beginning to see commercial wins in the targeted customers and grades we want to make and which is the absorbent products, and that will start to come to fruition as we go into 2020. And then there is a lot of opportunity on the cost structure. We have -- essentially we two 2 we have 2 businesses. We have the Weyerhaeuser business we acquired, which is doing very well. It was built for purpose pulp mills. And then we have the IT legacy part of that business, which is largely mills converted from other usage and not yet optimized. And there's still the ability to optimize several of those facilities and get out total cost down. So combination of commercial success, cost and then operating in this environment of supply and demand where pricing returns to more normalized level, all of that should come to fruition. The question is just, how long does it take on the market based stuff? The other things we control and we'll begin working on that as we go forward.

Steve Chercover

Thanks. Hopefully you'll count that as one pump question. I just wanted to ask about the Italian antitrust fine. Is this another situation where you chose to settle as opposed to litigate and are there other folks who were also impacted? Thanks.

Tim Nicholls

No. It's Tim, Steve. We were acetifying, we're appealing that decision, and so we're recognizing the charge in the moment while we go through the build process.

Operator

And our next question comes from the line of Gabe Hajde with Wells Fargo Securities. Gabe, your line is open. I'm going to go to the next question. Our next question is going to come from the line of Anthony Pettinari, Citi.

Anthony Pettinari

Good morning. One of your competitors recently called out the capital investment to increase their OCC processing capacity. And I'm wondering for your North American system, are there opportunities to shift from virgin to recycled, given what looks like this potentially a structure lower OCC prize. And then maybe if you could just remind us what your system mix is between virgin and recycled?

Mark Sutton

Anthony, the system mix is roughly 35% recycled fiber. We have -- what we look at is the actual fiber cost through the system to where you actually form that sheet of paper. So we call that fiber to the head box because there's other cost involved. For example, you want to make sure your maximize your energy production in the integrated mills, even if you're blending and recycling fiber.

So if look at some of the investments we made over the last few years, we've increased our capacity at 100% recycled mills, and we've increased our capacity at some of our virgin mills that used certain amount of recycled fiber. So we have the ability to do more. But we look at more than just the cost of OCC. It really is the cost of the fiber to the forming part of the equipment that really matters because if you leave more OCC, and it causes you to generate less boiler fuel to make your biomass energy, you have not done anything on your cost. So that's how we look at it.

Anthony Pettinari

Okay. No, it's very helpful. And then maybe a related question, pulp and paper recently introduced the recycle liner index. Do you anticipate any commercial impact from this index? And do you the index makes sense? I mean, it seems kraftliner has a pretty standard basis way. Recycled line seems lot that they used to may be quality differences, your thoughts on that?

Tim Nicholls

Yes. Anthony, it's Tim. Our belief is the box market is pretty competitive and the market's pretty efficient. And so knowledge -- there's not any new knowledge that's being created here. It's just being represented different way. So I can't speculate on what will happen. It's not hard to tell, see how it plays out. But in one sense, we don't see this as a significant change that's been put in the market.

Anthony Pettinari

Okay. That’s helpful. I will turn it over.

Operator

Our next question will come from the line of Mark Weintraub, Seaport Global.

Mark Weintraub

Thank you. And I'm trying to tiptoe into what's a complicated question. So I realize it may be hard to really answer in this context. But you've mentioned your view on footprint that you look to see whether there are structural changes on the containerboard side to guide your actions, which makes perfect sense.

And I guess, one of the things that's been very now exposed, the fall off in demand has really been more weighted to the export business and domestic business. So if kind of focusing on the export business, how confident are you that, that bounces back?

And I guess, the two things -- the two variables that play, which maybe great to get your perspective on is, you have the slide where you showed China demand has been pretty weak, which given that they are importing so much less OCC has been somewhat fledgling even recognizing that maybe their economy slower. And then the second part being, you know, there is a reasonably large amount of capacity that's being started up outside of North America. How much of that is the issue for the export business versus what's obviously, again, in a weak macro situation overseas?

Mark Sutton

So you're right. That's a complex question or set of questions, Mark. But I think taking it up a level, the view that we have on containerboard is informed by the view we have on corrugated packaging growth globally. And the role that what we do export kraftliner plays in that, and we still see growth in boxes globally as a preferred method of packaging and we'll see were sustainability and all this discussion to go.

But we think it bodes well for fiber-based packaging, which then feeds into a kraftliner growth rate. We used to think it was 3.5%, its probably somewhere in that neighborhood. But for right now, we've seen a demand decline, and we saw inventories built last year. And when you put the two together we have a correction in the year of 2019.

We haven't seen any structural that changes the ultimate driver of the containerboard demand which is box demand. And the fact that kraftliner plays a very important technical role or reality role, which is it is the feedstock for the global recovered fiber market. So they really work together, and we still believe and see the future is very bright in corrugated packaging, which informs our view of our containerboard business.

Mark Weintraub

Okay. And just – I did – did you give a specific indication on the EPS expectation for this year? I think I may have misheard but did you actually give a number there? Or did I miss here?

Tim Nicholls

We did not.

Mark Weintraub

Okay. I am sorry. Thank you.

Operator

Our next question is going to come from the line of Gabe Hajde with Wells Fargo Securities.

Gabe Hajde

Thanks for taking the questions. Sorry, about that gentlemen. My question was on the Riverdale conversion down in Selma, and I was trying to maybe see if you could frame up for us the impact to first half of next year. If I recall back the Riegelwood in 2016, I think it caught some of us by surprise the magnitude of differential between taking the mill down and doing the work and then when it ramps back up. I don't know if there's any context you can give us around that.

Tim Nicholls

No. It will be a pretty long outage. There's a lot of work to be done, when we take it down and start making the conversion. I think it's premature to lay that out at this point. We are finalizing what that all looks like next year. I'm sure we'll be able to give some general indications as we report on fourth quarter. But at some point papers will -- the production of Printing Papers will shut down on the machine and then all of the preparations for -- we tried to do as much work on ancillary equipment ahead of time. So that work is done, construction work, but then on the machine itself and related parts of the back-end of the mill, that work will begin early in the first quarter as we've outlined, and so we can give you more insight on that as we report fourth quarter.

Gabe Hajde

Okay. Thank you, Tim. And one more, I guess, focusing on the conversion. I've read some pieces different places that the capacity conversion may be more net neutral to capacity, which seemingly imply a shuttering somewhere else. And I was curious – you guys have taken a pretty decent amount of economic downtime this year, how you're thinking about your network and your needs as you see, commercial winds and the corrugated downstream business and what you might need elsewhere in the organization?

Tim Nicholls

Yes. So, Gabe, you may be thinking about is how it relates to white-top liner, but not the system overall. So we run our system based on our customers' needs. So that's where we start from. But this will be incremental available productive capacity. What it's actually going to free up is other facilities that they're currently producing this product to produce other products. One of which has a large position in gypsum facing board and will now be able to grow that position. So, it won't all show up in containerboard necessarily, but gypsum facing board or gypsum facing paper is something that we've been in that market for a long time. We have great customers. We think we provide good products and good service and we really would like to grow that position over time.

Gabe Hajde

Thank you.

Operator

Our next question will come from the line of Adam Josephson, KeyBanc Capital.

Adam Josephson

Mark and Tim good morning. Thanks for taking my question. I appreciate it.

Mark Sutton

Hi, Adam.

Adam Josephson

Mark, just one on your box demand on the quarter is – call it flat in the quarter. If memory serves, on the last call you talked about your thought that your customers had little down their finished goods inventories quite considerably, and I think you expected somewhat of a pick up in the second half as a result of that. So, did you see that? I'm just trying to square that with the flattish demand and relatedly you talked about e-commerce continuing to grow at double-digit and I'm also trying to square that with flattish demand in the quarter?

Tim Nicholls

Yeah. So, Adam, we did not see, to your point, we didn't see to the extent that we thought we would. We did see it in e-commerce. We feel really good about e-commerce. On protein side, we saw good performance. Process food, as I mentioned, was slightly better but not as much as a pick up as we thought it would be. And then some of the other segments, other non-durables, beverage and the like, did not come through the way we expected it to. But we also had in terms of some of these consolidation plays that have happened across the industry, we've had some business lost due to those that happened at the moment in time and then the replacement volume for that comes through on a longer time line, but that's what I was referring to with these customer wins. We feel good about the commercial activity in the quarter that will show up in the coming quarters.

Adam Josephson

I appreciate that, Tim. And then just one also on e-commerce, I'm just trying to connect the e-commerce growth with total market growth. So back in 2016 and 2017, obviously, everyone was talking about e-commerce. It was growing double-digit. Box demand was up 2% but it happened to coincide with the economy really, taking up. And now you're still talking about e-commerce growing at double-digit, but you're demand is flat. So I'm just trying to – what do you think the relationship is between your e-commerce growth for the market e-commerce growth in total, box demand growth given the relationship this year seems to have delinked, if you will?

Tim Nicholls

Yeah, I think it's appearing to be delinked only because we've had some of these losses that I talked about that kind of creates noise in the number. I think you're going to see that reverse itself over the next couple of three quarters. So I don't think anything structurally has changed.

Mark Sutton

I think, Adam, we talked about the box demand kind of trailing GDP by 50, 70 basis points, somewhere in that neighborhood, total box demand. You got a couple of sub-segments like e-commerce that are growing very, very fast, but we've got pluses and minuses in some of the other segments, some of these trade wars and that crimp some of the exporters from the U.S. There's always something going on. But think about the third quarter. GDP 1.9, box demand, 1 5 and so it's possible that e-commerce can be growing double-digit, which it is, and box demand can be a shade below GDP. So I think the GDP number and what drive the U.S. economy, the components of it, are really what we need to look at in terms of trying to understand box demand. And there's obviously some periods where there's three quarters in a row where it attracts perfectly, and then there is some noise in the system. You think about when this noise started, it started to really show up around the time, we started talking about tariffs and trade, and a number of those things. So, I do think this notion of it being right below GDP is still pretty solid.

Adam Josephson

Thanks so much, Mark.

Operator

Our next question will come from the line of Chip Dillon, Vertical Research.

Chip Dillon

Hi. Good morning and thanks for all the details. I wanted to just pick-up on the whole e-commerce piece again. Could you give us an idea of what proportion today it makes up of your overall domestic U.S. box demand? And it sounds to me, if it's up double-digit, that at least seems to be that it has either at versus flattening with what you've seen in recent years or maybe achieved and accelerated a little bit from what was at least earlier this year when Seok [ph] and other concern seems to suggest that may be the demand growth would slow from e-commerce.

Mark Sutton

Chip, it's in the neighborhood between 5% and 10% of our demand. And you're right, things like Seok until you actually implement those. There's lot of different opinions on how it works. But again, back to the fundamental role, corrugated can play in the supply chain, most of those initiatives we see as if we do our job right and innovate, we see those as more net positives for corrugated box demand than negatives.

Chip Dillon

Okay. And would you say there's been any real change in growth rate as you look at where we are now versus the last couple of years from e-commerce?

Mark Sutton

No. Not really, it's still holding up solid double-digit.

Chip Dillon

Okay. And then just two quick ones, as a follow-up. You had caution with the whole China export board side from China, that would seem to be the one that had the most yellow, I would say, on the chart. Is that more from a knowledge that you think it's going to stay weak for an indefinite period or just the fact that the information from China just seems to be so murky, you just can't tell?

And then other question is, can you just update us on long-term timing of some of the projects, we've heard about at Ilim in the next several years?

Tim Nicholls

Yeah. So the view that we shared in the prepared remarks up on demand and inventory in the region, that's our current view. It comes from a lot of sources. Yeah, there are some reported numbers in places, it's what we see on the ground is we interact with customers for the most part.

Chip Dillon

Okay.

Tim Nicholls

And then on Ilim, the project around containerboard has been approved. It will start going forward. But that's a couple of 2.5 years, three years before anything starts slowing to market.

Chip Dillon

Got you. Thank you.

Operator

Our next question will come from the line of Debbie Jones, Deutsche Bank.

Debbie Jones

Hi. Good morning.

Mark Sutton

Good morning, Debbie.

Debbie Jones

I wanted to ask about the volume guidance, sequential volume guidance of up $25 million in Industrial Packaging. You typically in the past, we've seen the seasonal move being down at least in the North American business. So I wanted to understand what your assumptions are for domestic box shipments and containerboard going into that? And is this being fully offset, any sequential weakness being offset by expert, is that way to think about it? Or have we reached a point where e-commerce benefited actually making 4Q less having seasonal impact?

Tim Nicholls

Yeah. I think on the box side, we're anticipating a strong season. We'll see how it plays out. We expect e-commerce to be in a solid place. We are also starting to see export volume and export demand pick up, and so that is going to impact our fourth quarter in a positive way for volume that we did not have in the second and third quarter.

Mark Sutton

I think, Debbie, on the e-commerce question, I think if you look back at the data over the last few years, the past peak in the third quarter dropped off in the fourth quarter has been evening out, because e-commerce would their value proposition have shortened shipping times and people are still active in the fourth quarter.

And then it even, to some extent, spilled into the first quarter with the whole return cycle. So there's just been an evening out of the demand, less of the peak, less of the drop off. And that started if you remember right, probably in 2016 and then 2017 it become more even and we continue to see that.

Tim Nicholls

The other thing that may be in your memory, Debbie is just the difference in days, especially last year from third to fourth. We had two less days in the fourth quarter last year versus the third, and we've got one less day this year. So it's a little bit better in than regard.

Debbie Jones

Okay. Thanks. That's helpful. And my second question is focusing on paper. Could you talk a little bit more about the seasonal uptick in LatAm paper that didn't really materialize as you're expecting in the quarter. And I wanted to understand a bit better the improvement in operations and cost sequentially, you mentioned the LIFO benefit, and I didn’t have any of that my model, just weren’t understand where most of that came from?

Tim Nicholls

Easy on the LIFO, we had a better fit in the third quarter that we don't expect to repeat in the fourth, and so that was what that comes it is about. On the seasonal demand, that didn't pick up. There were some delays in government buying programs around certain segments of Printing Papers in Brazil that came through, but came through late. And the export business, especially around other parts of Latin America where we ship just been pressured from imports and people have plenty of inventory so it's working off inventory position.

Debbie Jones

Okay. Thanks. I’ll turn over.

Operator

Our next question will come from the line of Brian Maguire, Goldman Sachs.

Brian Maguire

Hey, good morning Mark and Tim.

Mark Sutton

Hey, Tim.

Brian Maguire

Just wanted to come back to the really strong cost management in the quarter, a lot of moving pieces there, but on slide 30, you talked about some of the input cost trends there. It looks like fiber was a pretty meaningful one.

I guess, I'm just trying to square the significant benefit you got from wood fiber, on that lets say the ballpark in $20 million with the average cost over to the right being up 1%, that you're paying.

Just trying to figure out how that could have been. And maybe a little bit really to answer these questions earlier, just theorizing maybe you shifted a little bit more of the production over to recycled base from virgin. Is that part of it? Or other factors in there?

Tim Nicholls

Yeah. It's Tim. So we've been battling wood cost all year long. If you remember, tremendous amount of rain and wet weather starting late fourth quarter last year and continuing into well into the first quarter this year.

So, it's just a matter of being able to access and have availability. And then buy intelligently as we can to maintain the kind of inventory levels, that the mills that we need for wood fiber.

It's starting to normalize. We're probably be pretty close to a more normalized cost, as we exit the year, but the wood piece has been a challenge all year long, of course.

Brian Maguire

Okay. So the average cost up 1% or were they actually down versus 2Q, just trying to square that.

Tim Nicholls

Slightly down. We've been managing it down all year long. So, we were really high as we exited last year. And it's been hardwood and softwood. Hardwood has been the one that's been a little bit harder to bring down. Softwood, we've had a greater degree of success faster so.

Brian Maguire

Okay, great. And then adjust for my follow-up. Some of the new box business you called out that will kick in, in a couple of quarters.

Just wonder if you could comment on the mixed impact of that, might have on pricing or margins, just how would you describe your business versus the current portfolio and the legacy portfolio?

Tim Nicholls

Could you restate the question? I'm sorry we didn't hear the first part.

Brian Maguire

Yeah. I was just asking about some of the new box business that you called out, taking into the next couple of quarters. Just interested to hear what the mix impact of that would be on the pricing on margin. How would you kind of compare that to maybe just same portfolio of customers?

Tim Nicholls

Yeah. I think it's probably pretty flat. We're out there winning business on the capability. What we do for our customers? How we service them? The innovation we bring and the quality. So, it's a pretty mix neutral type of equation.

Brian Maguire

Okay, thanks very much.

Operator

And our final question today will come from the line of Dr. Mark Wilde, BMO Capital Markets.

Mark Wilde

Thanks. Tim, I've got a couple of box questions to kind of finish up on. One is we have the Chicago PMI up this morning, which was now more than five points just month-to-month.

Can you help us think about, how you think about the relationship between indicators like that and your box business? And then, I got one other question on boxes?

Tim Nicholls

Sure. Yeah. I mean, this is definitely related. I didn't see the numbers; I haven't called out to it yet. Whether it in the moment or there are some time lag. It's sort of manufacturing activity is what drives box demand. So there's got to be relationship there. I don't know if that's a moment in time and then reversion.

But, as I said, our volume, we saw pickup in October and we're still anticipating a pretty strong fourth quarter. So, we'll see how it plays out.

Mark Sutton

I think important thing, Mark, on things like purchasing managers index and those things is give it enough time. I mean, we've got a lot of disruption in the supply chain from manufacturing in the U.S., a lot of it related simply to the GM auto strike. And as you've got to let the data to play out but it is an input to many -- to our on demand model.

Mark Wilde

Okay. And the other one I wondered about is just how you think about the impact of new converting capacity, because it seems like there is a lot of new converting capacity coming into the market. Just to name a few, you've got the D Smith and box-propalable building these mega plants in Indiana. France, building -- bringing a lot of capacity into the market. And then you've got some domestic public and private competitors that are also adding kind of a box capacity. So what kind of effect are you seeing in the market from all of this? And how do you think about how it plays out, especially in flat demand or flattish demand?

Mark Sutton

I think the issue with converting is one of the tenants that needs to be, because of the nature of the product, on empty boxes what you're making. It needs to be close to the demand centers. And so what you see sometimes is in our case, we add to learning capacity where we have customers and the desire for it.

We may actually have that capacity, but it could be clear across the country and will just not use that capacity and take a shipped out or to do whatever we have to do and then use the capacity close to the customer.

So, I can't speak for all these companies that are building or adding. But that's how we think about it is. Converting capacity is that last step in value add and transformation of containerboard into something people actually buy. And for us, it's about capabilities near where our customers and our growth is.

Mark Wilde

Okay. Good luck in the fourth quarter and as we move into next year.

Mark Sutton

Thank you, Mark.

Operator

I'd now like to turn the call over to Guillermo Gutierrez for closing comments.

Guillermo Gutierrez

Thank you again for joining International Paper's Third Quarter Earnings Call. As always, Michele and I will be available for your follow-up questions. Thank you.

Operator

Thank you again for participating in today's International Paper Third Quarter 2019 Earnings Day Conference Call. You may now disconnect.