Waste Connections, Inc. [WCN]
Q3 2017 Earnings Conference Call
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Company Representatives:
Ronald Mittelstaedt, Chairman, CEO
Worthing Jackman, CFO

Analysts:
Mario; Macquarie Capital
Tyler Brown; Raymond James & Associates
Brian Maguire; Goldman Sachs
Derek Spronck; RBC Capital Markets
Joe Box; KeyBanc Capital Markets
Michael Hoffman; Stifel Nicolaus
Noah Kaye; Oppenheimer & Co.
Corey Greendale; First Analysis
Kevin Chiang; CIBC World Markets

Presentation

Operator: Ladies and gentlemen, thank you for standing by and welcome to the Waste Connections third-quarter 2017 earnings conference call. (Operator Instructions) As a reminder, this conference is being recorded Thursday, October 26, 2017.

I would now like to turn the conference over to Mr. Ronald Mittelstaedt, Chairman of the Board and CEO. Please go ahead, sir.

Ronald Mittelstaedt: Okay. Good morning. I'd like to welcome everyone to this conference call to discuss our third-quarter 2017 results and provide both a detailed outlook for the fourth quarter and some early thoughts on 2018. I am joined this morning by Worthing Jackman, our CFO, and several other members of our senior management team.

As noted in our earnings release, continued strength across all lines of business enabled us to once again exceed our outlook for the third quarter. Adjusted EBITDA as a percent of revenue in the quarter expanded 100 basis points year over year as expected, in spite of the impact from two hurricanes. This is especially noteworthy in light of the dilutive margin acquisitions completed since the year-ago period.

Most importantly, adjusted free cash flow remains notably strong at $614 million year to date, or 17.7% of revenue and 55.8% of adjusted EBITDA.

Our divesture program is mostly behind us now after we completed a multi-market swap with Republic Services in early September.

We announced another double-digit increase in our regular quarterly cash dividend and we remain well positioned to fund expected above-average acquisition activity in the near term, while continuing to increase our return of capital to shareholders.

Before we get into much more detail, let me turn the call over to Worthing for our forward-looking disclaimer and other housekeeping items.

Worthing Jackman: Thank you, Ron, and good morning.

The discussion during today's call includes forward-looking statements made pursuant to the safe harbor provisions of the US Private Securities Litigation Reform Act of 1995 and forward-looking information within the meaning of applicable Canadian securities laws. Actual results could differ materially from those made in such forward-looking statements and information due to various risks and uncertainties. Factors that could cause actual results to differ are discussed both in the cautionary statement beginning on Page 2 of our October 25th earnings release, and in greater detail in Waste Connections' filings with the US Securities and Exchange Commission and the securities commissions or similar regulatory authorities in Canada.

You should not place undue reliance on forward-looking statements and information, as there may be additional risks of which we are not presently aware, or that we currently believe are immaterial, which could have an adverse impact on our business. We make no commitment to revise or update any forward-looking statements and information in order to reflect events or circumstances that may change after today's date.

On the call, we will discuss non-GAAP measures such as adjusted EBITDA, adjusted net income attributable to Waste Connections on both a dollar basis and per share, and adjusted free cash flow. Please refer to our earnings releases for a reconciliation of such non-GAAP measures to the most comparable GAAP measure. Management uses certain non-GAAP measures to evaluate and monitor the ongoing financial performance of our operations and other companies may calculate these non-GAAP measures differently.

I will now turn the call back over to Ron.

Ronald Mittelstaedt: Okay. In the third quarter solid waste price plus volume growth was 3.8%, exceeding our 3% to 3.5% outlook for the quarter, primarily due to better than expected volume growth.

This is the first full quarter for incorporating the contribution from operations acquired in the Progressive Waste acquisition within reported price and volume growth. As discussed on previous calls, we estimate the shedding of low quality and unsafe-to-service revenue across the former Progressive Waste footprint to be at least a 1% drag to reported volume growth in the near term. This reflects a purposeful price/volume tradeoff to improve the quality of revenue and, as a result, margins and free cash flow in these acquired markets. As expected, pricing came in above prior quarters, at 3.3%, our highest reported price increase in over five years.

On a same-store basis, commercial collection revenue increased about 3% and roll-off increased about 6% in Q3 from the prior-year period. Roll-off pulls per day increased 1%, driven primarily by our Western and Eastern regions, which more than offset declines in other regions, primarily related to the purposeful shedding of lower quality revenue.

Solid waste landfill tonnage in Q3 on a same-store basis increased 6% over the prior-year period. MSW tons rose 5%, special waste tons increased 19%, and C&D tons declined 8%, predominantly due to limitations under the new conditional use permit at our Chiquita Canyon landfill in Southern California, the purposeful shedding of poorly priced roll-off activity and tough comps in a few markets.

Recycling revenue, excluding acquisitions, was about $37 million in the third quarter, up about $8 million, or 28%, year over year due to higher commodity values for fiber.

Prices for OCC, or old corrugated containers, averaged about $184 per ton during Q3, up 50% from the year-ago period and up 7% sequentially from Q2. Widely publicized actions by China significantly reduced the value of recycled fiber in early October. OCC prices currently average around $85 per ton, down almost 55% sequentially from Q3's average and down about 30% from the level we averaged in last year's fourth quarter.

Despite seeing slight upticks in recent OCC bids, we believe it's too early to predict either when or by how much fiber values will recover. At recent lows in fiber values we estimate the P&L impact in Q4 compared sequentially to Q3, to be about a $15 million reduction in revenue, a $10 million hit to EBITDA and a corresponding $0.03 impact to EPS.

Regarding E&P waste activity, we reported $54.7 million of E&P waste revenue in the third quarter, up 82% year over year and up 16% sequentially from Q2, with margins well above our corporate average. Although activity slightly exceeded our expectations in the period, we still expect E&P waste revenue to decrease sequentially in Q4, primarily due to seasonality in the oil and gas drilling CapEx spend.

As noted earlier, we made significant progress in Q3 on our divestiture program related to certain markets acquired in the Progressive Waste acquisition. In early September we completed a multi-market swap with Republic Services in which we exited certain markets in Southeast Texas and Louisiana in exchange for two markets in North Central Illinois. This further expands our position and will drive additional internalization and synergies within our group operations. We expect our divestiture program to wrap up in Q4, with the expected sale of an approximate $30 million revenue, single-digit margin collection operation.

As noted on our earnings call in July, we are quite pleased with the expected overall outcome of the divestiture program. From an initial estimate of approximately $250 million of revenue we targeted to divest, swap or fix, we'll end up reducing revenue by approximately $100 million to $110 million after swaps and divestitures and EBITDA should increase by about $15 million on the lower revenue base.

Looking at acquisition activity, this remains one of the most active deal environments that we've seen in years. We completed the previously announced acquisition of a $15 million revenue franchise collection operation in Alaska and have made significant progress on other potential acquisitions currently under letters of intent. If the projected timeline plays out as we expect, we anticipate deploying a meaningful portion of our existing cash balance on acquisitions late in this quarter or very early in Q1 2018.

Finally, as also announced yesterday, our board of directors authorized a 16.7% increase in our regular quarterly cash dividend, our seventh consecutive double-digit percentage increase since commencing the dividend in 2010. Even with this increase, our dividend remains less than 20% of our expected annual free cash flow, providing tremendous flexibility to fund our growth strategy and further increase the return of capital to shareholders.

And now I'd like to pass the call to Worthing to review more in depth the financial highlights of the third quarter and to provide a detailed outlook for Q4. I will then provide a few early thoughts on 2018 and wrap up before we head into Q&A.

Worthing Jackman: Thank you, Ron.

In the third quarter revenue was $1.206 billion, up $121.6 million over the prior-year period and $21 million above our outlook for the period. Acquisitions completed since the year-ago period contributed about $60 million of revenue in the quarter, or about $40 million net of divestures.

Adjusted EBITDA for Q3, as reconciled in our earnings release, was $393.4 million, or about $7 million above our outlook for the period, due to higher than expected revenue. Adjusted EBITDA as a percentage of revenue was 32.6%, consistent with our margin outlook.

Year-over-year our adjusted EBITDA margin reported for the third quarter increased by 100 basis points. Underlying margin expansion of over 150 basis points estimated to be driven equally by solid waste and E&P waste was partially offset by the dilutive impact of comparably lower-margin acquisitions completed since the year-ago period and limitations under the new conditional use program at our Chiquita Canyon landfill, which took effect August 1.

Fuel expense in Q3 was about 3.7% of revenue and we averaged approximately $2.51 per gallon for diesel in the quarter, which was up about $0.18 and $0.04 per gallon, respectively, from the year-ago period and sequentially from Q2.

Depreciation and amortization expense for the third quarter was 13.6% of revenue, down 50 basis points year over year and in line with our outlook.

Interest expense in the quarter increased $4.9 million over the prior-year period to $32.5 million due to higher average outstanding debt balances and higher interest rates as compared to the prior-year period. Net of interest income, interest expense increased $3.4 million year over year.

Debt outstanding at quarter end was about $3.9 billion and our leverage ratio as defined in our credit agreement was about 2.6x debt to EBITDA.

Our effective tax rate for the third quarter was 34.3%, or 530 basis points higher than expected, due in part to a $3.8 million increase in the income tax provision associated with an increase in our deferred tax liabilities resulting from a 33% hike in Illinois' corporate tax rates enacted in the period. Our underlying effective rate net of these items in Q3 was about 28.5%.

GAAP and adjusted net income per diluted share were $0.47 and $0.60, respectively, in the third quarter. Adjusted net income in Q3 primarily excludes the impact of intangibles, amortization, other acquisition-related items, including mark-to-market accounting for share-based awards assumed in the Progressive Waste acquisition, and the increase in the income tax provision resulting from the change in Illinois' corporation tax rate.

Adjusted free cash flow through the first nine months of the year was $614 million, or 17.7% of revenue. We remain on track to meet or exceed our upwardly revised full-year adjusted free cash flow outlook of $750 million.

I will now review our outlook for the fourth quarter of 2017. Before I do, I would like to remind everyone once again that actual results may vary significantly based on the risks and uncertainties outlined in our safe harbor statement and filings we've made with the SEC and the securities commissions of similar regulatory authorities in Canada. We encourage investors to review these factors carefully.

Our outlook assumes no change in the current economic environment and operating environment. It also excludes any rebranding costs or other items resulting from the Progressive Waste acquisition and any additional acquisitions or potential divestitures that may close during the period.

Revenue in the fourth quarter is estimated to be approximately $1.125 billion. We expect core price plus volume growth for solid waste to be between 3% and 3.5%, with no notable impact from the two hurricanes.

Adjusted EBITDA in Q4, as reconciled in an 8-K we are filing contemporaneous with this call, is estimated to be about $350 million, or approximately 31.1% o revenue.

We are pleased with the potential for another year-over-year reported margin increase in the upcoming quarter in spite of the estimated 100 basis points year-over-year drag from lower recycled commodity values and acquisitions completed since then and an estimated 30 to 40 basis points full-quarter negative margin impact from the new Chiquita Canyon landfill permit.

Depreciation and amortization expense for the fourth quarter is estimated to be about 14.5% of revenue. Of that amount amortization of intangibles in the quarter is estimated to be about $29 million, or about $0.07 per diluted share net of taxes.

Interest expense net of interest income in Q4 is estimated to be approximately $31 million.

Our effective tax rate in Q4 is estimated to be about 28.5%, subject to some variability.

Finally, non-controlling interest is expected to reduce net income by about $225,000 in the fourth quarter.

And now let me turn the call back over to Ron for some final remarks before the Q&A.

Ronald Mittelstaedt: Okay, thank you, Worthing.

Again, we are extremely pleased with the underlying fundamentals, margin expansion and free cash flow generation in our business. Our year-to-date results, combined with our Q4 outlook, puts us on track to meet or exceed the increased full-year outlook we communicated in July in spite of the recent significant deterioration in recycled fiber values.

We just announced another double-digit percentage increase of our regular quarterly cash dividend and we remain well positioned for a potential significant increase in acquisition outlays later this quarter or early next year, which will have a nicely positive impact to 2018's revenue and EBITDA.

Although we won't provide our formal outlook for 2018 until next February, we are able to provide some early thoughts assuming no change in the economic environment or additional acquisitions.

In summary, we believe we've already positioned for at least a 50 basis point expansion in adjusted EBITDA margins in 2018, even if recent lower recycled fiber values persist. Any recovery in recycled fiber values or further increase in E&P waste activity could provide additional margin upside. We expect to have better visibility on this expected margin expansion, acquisition outlays and recycled fiber values in February when we provide our formal outlook for the upcoming year.

We appreciate your time today. I will now turn this call over to the operator to open up the lines for your questions. Operator?

Questions & Answers

Operator: Thank you. (Operator Instructions) Hamzah Mazari; Macquarie.

Mario: This is Mario filling in for Hamzah. Quick question regarding the mix of business. Could you update us on what percentage of your mix is franchise today? And do you think you can keep that mix consistent or stable even by doing more acquisitions?

Ronald Mittelstaedt: Yes. Mario, today the franchise or what we consider exclusive business, our long-term contract business, is about 42% to 43% of revenue. And it has been very consistent at that since the close of the Progressive transaction almost 18 months ago. Of course in this quarter we closed a franchise operation in Alaska, so that moves that number just a little bit up. But if we look at our available acquisition opportunities, it is pretty well balanced between 40% and 45% in exclusive market and 55% in the balance. So over time, if our track record remains what it has, we should stay in that 40% to 43%, 44% band exclusive.

Mario: Okay, thank you. And a quick follow-up. Could you give us a sense of what your M&A pipeline looks like in Canada versus the US and whether you think tax reform is still a catalyst for private company deals to happen?

Ronald Mittelstaedt: Sure. Well, the predominant amount, the vast majority of our M&A pipeline is in the US versus Canada. Of course today our business is about 13%, 14% in Canada and 86%, 87% in the US. And we would tell you our pipeline of acquisitions is greater than that percentage in the US and a little less in Canada. So we expect that percentage to stay about the same or climb a little bit in the US over time.

Yes, we definitely feel that tax reform, depending on what it looks like -- if it comes out as it has been at least advertised, we definitely believe that is a catalyst to M&A activity for a whole host of reasons. And we believe that, as we've said, if that occurs over the next two and a half to three years before there is a next national election, that that would likely set up a lot of M&A activity between now and then.

Mario: Perfect. Thank you so much.

Operator: Tyler Brown; Raymond James.

Tyler Brown: Ron, so we continue to hear a lot about a very tight craft labor market. We're really seeing it acutely on the commercial driver side. I was just hoping that you guys could talk about two major cost buckets specifically, so front-line labor and also the third-party subcontracted line-haul. Can you talk about where you expect maybe unit cost inflation for those buckets, but maybe specifically unit cost inflation for next year?

Ronald Mittelstaedt: Sure. Well, let's see, Tyler. As you appropriately pointed out, the entire labor market, both skilled and unskilled, obviously more so in skilled, is extremely, extremely tight. And it tends to be pretty uniform across the country. I would tell you, having said that, that we view it as probably tightest in the South and the Southeast at this point, where we're seeing the most growth in the market areas, just organic growth, housing growth, et cetera, and then, second, along the West Coast. It is a little less tight in the Midwest and parts of the East. It remains a continuous challenge. It's the number one issue that we spend time on at all times, is recruiting and retention of employees.

And as far as unit cost inflation, we're looking next year at probably around 2.4% to 2.5% all-in cost inflation. There are obviously components in markets that are higher than that, and we're seeing wage increases in certain markets between 3% and 6%. That's offset in other places with substantially less than that. But all in, we feel very comfortable in that, a little less than 2.5% overall.

Tyler Brown: Okay. So not materially different than what you've experienced.

Ronald Mittelstaedt: No, not materially different. Barring any change, that would be up around 20 to 30 basis points year over year, with the vast majority of that being in labor.

Worthing Jackman: Tyler, we're seeing that same pressure this year, so really next year is a repeat of what we're seeing this year.

Tyler Brown: Okay. And then maybe just on the margin side -- so I think maybe a year or two ago you guys had maybe talked about post-Progressive as we get out to 2018 being in that 33% EBITDA margin range for solid waste, which I think you're not quite maybe guiding to that for [sketch] out next year. But as we look ahead, do you think that that number becomes more of an asymptote? Or do you think that that's maybe more just a run on the ladder?

Worthing Jackman: Boy, there you go again. We've got to look up another word, Tyler.

Ronald Mittelstaedt: Yes, I'm not sure what that big word means. But what we would say, Tyler, is -- look, I mean, again, we're not providing any specific, but we just commented that we believe that we're at least 50 basis points up year over year. We approached 32% this year in 2017, which is where we said we would be at the end of 2018 when we did the Progressive merger. So we're over a year ahead. So that takes you to somewhere in the 32%, 32.5% in 2018 based on what we said today. And we have said that is in current commodity pricing, which is clearly the 50 basis points dilutive right now to where we were 60 days ago. So if you go back to that recycled commodity pricing environment, you would be at 33% for 2018.

Worthing Jackman: And add back the impact of dilutive margin acquisitions completed since then.

Ronald Mittelstaedt: But even so.

Worthing Jackman: Yes.

Ronald Mittelstaedt: Even so. We did those at the beginning of the year. So in my mind that's basically -- we're right where we thought, which is about 33% adjusted for that, only that issue.

And to your question, I do view it as a rung on the ladder. There's nothing magical that 33% illustratively is a cap on our margin. In this economic environment we would continue to see a 30 to 50 basis point sort of EBITDA margin expansion without really any artificial ceiling that's out there. If we're able to get 2.5% to 3% price -- we're getting better than that. If we're able to have positive volume growth and we're able to manage our costs at 3% or less, you're going to get margin expansion on a year-in, year-out basis.

Tyler Brown: Okay. Very good. Then maybe just quick last one. I am a bit dense on this, but assuming no additional M&A and that the divestures and swaps that you've announced are all that you do -- let's just say that -- in 2018 how much M&A revenue will roll over? Will that only be maybe $10 million? And then how much should we expect the divestiture to work against revenue in 2018?

Worthing Jackman: Yes. Right now the acquisition rollover as we sit here today is about $15 million, because obviously the Groot transaction was in the full-year results this year and we've done very smaller acquisitions since then. The divestitures would take away probably about $35 million to maybe $40 million as you look at next year, based on the timing. That's assuming that final divestiture gets done as we anticipate before the end of this year.

Tyler Brown: Okay. So assuming that last divestiture --

Ronald Mittelstaedt: Yes, and that's, again --

Tyler Brown: Yes. Sorry; go ahead.

Ronald Mittelstaedt: And again, that's assuming nothing closes between now and year end which, you know, we would tell you as we sit here today that that is unlikely, that nothing closes. So there would be certainly incremental rollover above the $10 million. But that is what the rollover is today.

Tyler Brown: Okay, perfect. All right, thanks.

Operator: Brian Maguire; Goldman Sachs.

Brian Maguire: A couple questions on the EBITDA margin outlook. I think earlier you had guided for the full year to be 31.7% on EBITDA margin. And I think your press release commented you're going to reiterate in the full-year guide. So does that imply a 4Q number kind of around that 31.7%? Is that what I heard from you, Worthing?

Worthing Jackman: Well, the guide -- remember, we guided revenue, we guided EBITDA and we guided free cash flow. The margin you just cited is just EBITDA divided by revenue. But you've got to focus on the (technical difficulty) [dollar] EBITDA. If you want to get back to the 31.7% you would add back the $10 million impact of recycling in the period. That would get you to the 31.7%. But, again, what we're focused on is the $1.45 billion of EBITDA at a minimum for the full year.

Brian Maguire: Okay. Got it. It sounds like we're getting to that $1.45 billion a little different way than -- originally expected maybe a little bit higher revenue, slightly lower margin. And then just looking out to 2018, Ron, on your comments on the 50 basis point increase there, just so I understand, does that include any of the potentially dilutive margin acquisitions that you've got in the pipeline? And maybe you could speak to what some of the factors are that could drive that expansion, given all the headwinds you talked about, like Chiquita Canyon and the recycling price headwinds that you've got.

Ronald Mittelstaedt: Yes. Well, first off, it does not include the impact of any margin -- any margin impact of any acquisitions we've not yet closed in that, positive or negative. Now the reality is most acquisitions come on at margins lower than our corporate average.

It does, however, Brian, include the rollover impact of the dilutive margin of the Chiquita Canyon permit, because we already know what that obviously is and have factored in. And it also includes the dilutive margin impact of commodities staying at where they are right now, so [both of those]. So despite both of those and between the two of those, those are well more than a 50 basis point drag. So really we're saying there was a 100 basis point margin expansion on the base company heading into 2018, prior to the change in the last six weeks in commodity prices and the finalization of the Chiquita Canyon permit.

If you look at acquisitions and you look at that we did a massive acquisition this year -- massive in our model -- called Groot and we did it at the beginning of the year. And it was dilutive to our margins. You've seen us increase margins this year 100 basis points, despite overcoming over a 40 basis point across the platform margin dilution from Groot in the beginning of the year.

So it's a long way to tell you that we view the 50 basis points right now next year as sort of a floor in what margin expansion should look like, and we would do that even with pretty material acquisitions coming in.

Brian Maguire: Is it safe to say that some of the positive offsets are the swaps you're doing, which seems like they're margin accretive, and then some of the pricing actions in the BIN portfolio?

Ronald Mittelstaedt: Absolutely. I mean, we've dropped revenue, as we said, by a net of $100 million to $110 million and increased the EBITDA on the lower revenue, through the swap and improvements, by $15 million. That's a 20 to 30 margin basis point expansion right there through the divestures.

Worthing Jackman: And, Brian, one thing I'd just comment on on margins. Obviously this year, even going into this year, we've all along said this is the year we focus on EBITDA dollars and free cash flow dollars, because it was hard to predict the timing of the divestiture program. The fact that this remaining divestiture of $30 million is staying in our portfolio through an entire fourth quarter -- in other words, it gets you more revenue than the reported number, but it ends up being dilutive to reported margins because we're holding on to a very low margin business for an extra three months in the current year.

Brian Maguire: Okay. That's a good point. Thanks. And just one last question for me. I apologize if you already talked about it, but just was wondering if you could size the impact of the hurricane costs in the current quarter. And I think you said you don't expect any volume pickup in 4Q from that, but just wondered if you could speak to why you wouldn't expect any volume pickup either in the Houston or Florida areas from the hurricanes. Thanks.

Ronald Mittelstaedt: Yes. Well, first, the second part of your question. I mean, we have seen volume pickup in both South Texas, the Houston market, and Florida, and we certainly didn't mean to imply that we haven't. We're just saying that when you look at it in the overall scheme of the entire Company's portfolio, a $10 million to $15 million movement in revenue in a period doesn't materially move numbers. You're talking about less than 10 basis points of movement. So that is why. We definitely didn't say we didn't get it, because we have.

Worthing Jackman: Yes, because if you add up the cost -- I mean, the way we estimate the cost is between $3 million and $4 million of incremental costs in the quarter, and some incremental activity on the top line likely offset a little over half of that in the period. So to Ron's point about the drag, it's a drag on margins probably between 10 and 15 basis points in the period. It's probably a boost of 15 to 20 basis points on the volume side. So it's not a material movement on the top line. And, again, that's mostly behind us as we look at the benefit.

Brian Maguire: Okay. Fair enough. Thanks a lot.

Operator: Derek Spronck; RBC Capital Markets.

Derek Spronck: Just wanted to commend the job you did managing through the hurricanes and taking care of your employees through that situation.

Just in terms of the M&A market, how rational is it right now, both from a seller's expectation as well as from the buyer -- how aggressive are the buyers right now, including the private equity?

Ronald Mittelstaedt: Well, I would say -- as we said in a few previous calls, Derek, that you've seen some movement over the last couple of years as you've had sustained very low interest rates and there's a benefit in part to the capital structure of companies because of that. We've seen some movement by about 1 to, in some cases, up to 2 turns of EBITDA being paid by the buyers, whether they are public companies or private companies or private equity.

I would tell you that we don't really look at what other people are paying. We look at what we can pay. It's done on a return on capital and an NPV basis of the discounted cash flows. So I have not seen material movement.

Certainly buyers' expectations have become, I would call it, inflated. You've got a lot of the small boutique investment bank firms, as well as largers, running around touting public company multiples as a way to lure potential fees from private sellers. And so they let them know what us and others are trading at and then those sellers end up disappointed when that doesn't come to fruition. And then we have to go through a prolonged negotiation. There's reasons we trade at what we do and there's reasons that private companies aren't worth those kind of multiples.

But, be that as it may, we would tell you that we are seeing more discussion leading to more letters of intent where we -- so obviously to do that we are closing the gap between sellers and buyers in a negotiated fashion to get to binding letters of intent on structure and valuation. So despite whatever rumors you hear out there, or that are real, we're able -- if the seller's looking to do something and it's in our market area, we're usually able to figure something out.

Derek Spronck: Okay, that's great color. Thanks, Ron. Just one more for me. When you look at your free cash flow conversion rates and as a percentage of revenue, 18% this quarter, year to date over 17%, EBITDA numbers [and] well over 55%, are you able to continue to improve it? Like, are we walking up from, like, the 15% of revenue more on a sustainable basis? Or is it going to be lumpy on a quarterly basis due to the CapEx timing? Or are you actually able to continue to improve this conversion ratio that seems to be coming in higher than expectations on a fairly regular basis?

Worthing Jackman: Yes, again, Derek, as we've talked in the past, you've got timing of things that move in and out certain quarters. Some quarters have higher cash flow generation due to a lack of cash tax payments in the period, the way those are timed. Other quarters have lower cash conversion characteristics because of the nature of the timing of CapEx.

So if you look at our full-year guidance -- to remind you, we guided about $750 million of cash flow, $1.45 billion of EBITDA, almost a 52% conversion for the full year. Q4 has higher CapEx in it based on the timing really on the manufacturing side of when the manufacturers on the trucking side could get the trucks to us based on certain issues within their manufacturing line. So there's a higher amount of fleet coming in Q4. That's just a timing issue. Don't try to walk the conversion ratio up above 52%, because what we've said over time, as our cash tax to GAAP accrual rises you'll likely see that over a multi-year period approach 50% versus the 52% that we're doing right now.

On a percentage of revenue this year we'll be about, what, 16.5% or so. And that's a better area to focus on, assuming the EBITDA margins stay where they are. If EBITDA margins creep up you'll see that percentage of revenue creep up as well as we continue to convert 50% or better.

Derek Spronck: Okay, that's great. Thanks.

Operator: (Operator Instructions) Joe Box; KeyBanc Capital Markets.

Joe Box: So obviously Groot was margin dilutive just by nature of where it came in at in the beginning of the year. Can you maybe just talk about where you're at in the process of internalizing that waste, how the new asset swap fits in and how should we think about the margin profile here as we start to migrate into 2018?

Ronald Mittelstaedt: Sure. Well, let's see. As we said at the time of closing, Groot being a large transfer and -- excuse me, a large collection, transfer and recycling company, was not integrated on their own. They were in the 20% to 25% margin range on an EBITDA basis as a private company when we acquired them. We obviously owned a couple of landfills in North Central Illinois. We were able to internalize certain of the Groot volume in Year 1. That ramps up in Year 2. So we moved their margin profile closer to that 25% to 28% on an integrated basis with that.

Then through the swaps that we were able to complete with Republic Services, we picked up incremental revenue and transfer capacity that allowed us to internalize a greater amount throughout 2018 and 2019 of Groot's volume through transfers we picked up in the Republic Services swap, plus [lot] synergies and overhead synergies in that market area.

So when we come through 2018 and you get into 2019 and we're able to fully internalize things, you will see we will have moved Groot up from, call it, the low 20% level to the low 30% level, so about an 800 or 1,000 basis point improvement on that platform over about a 24-to-30-month period. And certainly the Republic Services swap we were able to do and picking up incremental transfer capacity from them as well as some very, very nice contracts, excellent facilities, excellent assets and employee base, that is all additive. So it was something we were very pleased to do.

That swap worked the way a swap should, which is 1 and 1 equal more than 2, for both parties. Republic had substantial asset infrastructure and key assets in parts of Texas and Louisiana that they picked up. And I'm sure that 1 and 1 equals 3 for them as well. And that's how a swap should work when it goes right.

Joe Box: Got it. Perfect. That's good color. Thanks. And I know it doesn't get talked about often, but your Intermodal and Other segment, it does seem like it's put up nice revenue growth over the last year. Can you maybe just give the outlook there as we start to really run up against tougher comps?

Worthing Jackman: Yes. You might be looking at the line of Intermodal and Other. I mean, there's a handful of things. Intermodal's up nominally this year, probably in that 1% to 2% range. Obviously what's in the Other basket, you also have landfill gas sales and, again, the value of landfill gas and green credits has risen year over year. So that's predominantly a big driver of that increase in Other as well.

Joe Box: Okay, great. Thanks, guys.

Operator: Michael Hoffman; Stifel.

Michael Hoffman: So, given the breadth of questions, now I have to figure out how to be erudite about asking this next round. But free cash flow conversion, you got asked a lot about that. We should continue to assume it's 50% to 55%? That's the right way to think about it?

Worthing Jackman: Well, I think we'd say it's about 50% to 52%. We've never gone to as high as 55%. And that's a full-year number. Obviously there may be one quarter or a couple quarters we can get a number higher than the 52%, but the full year is not 55%.

Michael Hoffman: Fair enough. And then capital spending this year, still $460 million or were you expected to go up?

Worthing Jackman: $460 million is still a good number.

Michael Hoffman: So 10% of revs, 10% for next year is a good place to start?

Worthing Jackman: That's a good place to start.

Michael Hoffman: All right. And then five years into this recovery, how would you now frame the state of solid waste when you think about it through your line items? Like, in front-end loader, where are we in the addition of adding routes? Is it an accelerating condition, a stable but continuous, service interval changes, things of that nature? Can you frame that for us in the context of the state of the business?

Ronald Mittelstaedt: Sure. Michael, I think the way you said it regarding commercial where you said stable and continuing to improve, meaning the pace of improvement of having to add routes has stabilized. It's not on quite as steep a trajectory as it was, say, three to four quarters ago. We are continuing to add routes due to new growth and new business. That's happening throughout many markets again, and really very broadly based. We're seeing that in all our solid waste regions in the US.

As we reported, we're continuing to see incremental growth in the roll-off business. We don't provide it, but we're continuing to see incremental increase in house count on the residential side as well. So we would tell you, growth improvement continues in all the business lines, stable, manageable, a little flatter just because you're cycling on higher denominators, as you said, as we're in the fifth year or sixth year of this recovery.

Michael Hoffman: And housing has been a big catalyst for the activity levels and least hit a pause in housing starts this year. To the degree that you look at special waste, and that's dirt moving, doing site prep, can you read through on your outlook on special waste and say housing looks like it will pick up again at a slower rate of growth but slow growth in 2018?

Ronald Mittelstaedt: Yes. What I would say, Michael, is that the housing growth, while your words were that it may have slowed some aggregately, and while that may be true, I would argue that is again more pocketed. We're continuing to see robust housing growth in most of the West Coast. We're continuing to see robust housing growth from Texas through Florida. We're continuing to see robust housing growth in the Eastern Seaboard, particularly the Southeastern Seaboard, the Carolinas, up, up. So where we see it cooling a bit is in some of the Rocky Mountain area and in the Upper Midwest. And so we would tell you it is geographic. It is not widespread whatsoever.

Michael Hoffman: Okay. That's very helpful. Thank you for taking my questions.

Operator: Noah Kaye; Oppenheimer.

Noah Kaye: Maybe just start with E&P. Obviously you're not at the run rate that you were before the fallen oil prices, but the revenue growth year over year has been impressive. As you think about the business going into next year, in the past you talked about very high flow-through incremental margin (inaudible) growth. So how is the business sized now? And what would the incremental margins look like on any kind of growth in E&P at this point? Understanding that you're not predicting that, just want to understand what the margin profile on that would look like.

Worthing Jackman: Yes, as you know, any landfill-based business, the incrementals are quite high, as we've said, for E&P. They could run as high as 70% to 80%. That also depends on -- to the extent that you see more growth, does that require kind of expanding the cost structures at their facilities. I mean, we've been able to ramp the business, mostly due to the increase in the Permian. So as that growth comes through a certain number of facilities, you get the higher end of the flow-through initially. To the extent that drilling activity expands and we bring back additional shifts and other facilities, that initial incremental flow-through won't be as high.

But right now, again, you'll see us -- we're in that 45% to 50% margin range on an overall basis in E&P. That's up nicely year over year because of the incremental flow-through on the revenue growth. At this stage of the game we're probably cycling in that run rate of 200 to 210 on that business. And let's see where crude goes next year to see if we can see additional growth in that business.

Noah Kaye: Great. Thanks for the color. And then, just to clarify, you talked about in some of the line items you gave C&D volumes down 8%. I think you called out both Chiquita Canyon and a couple of other headwinds. What would -- if we take some of those factors out, I guess -- and ties partly back into Ron's color on housing starts and the housing environment. What does sort of normalized C&D activity look like, sort of continuing on? Because I don't think comps last year were as difficult in this space as they were for, say, MSW.

Ronald Mittelstaedt: Yes. We had, as we called out -- you were correct, we called out three issues that were predominantly contributed to this. There were the new permit at Chiquita Canyon. So first and foremost that was the largest factor. And secondly, we commented on the shedding, purposeful shedding, of low-margin business. That would be the second largest factor. That one obviously goes away in time, because we finish that.

Worthing Jackman: As well as Chiquita, when the anniversary (inaudible).

Ronald Mittelstaedt: As well as Chiquita when we anniversary it. But that was the second largest.

But we did have a couple of markets where we had tough comps. And, again, those were a good thing last year and they make it more difficult this year. So it is a little misleading to look at that number and say, you know, is the business down. Well, the business really -- well, in a reported basis it is down because of the first two. The third one is really just a comp issue.

So to answer your question, we would tell you that the C&D business is probably right now for us about flat on a normal basis. Could that be up a couple, 2%, 3% next quarter or down a couple, 2%? It could. But I think at this number, this is sort of a one-time because of the newness of the permit.

Noah Kaye: Okay, that's helpful. And then maybe just last on recycling. Maybe it would just be helpful to understand. Obviously way too early to make a call on what prices will look like in 2018. But I would like to understand how it's actually impacting the business. You sell fiber, even maybe some other products as well. But are you having to make any kind of investments in quality or sorting to meet with new compliance requirements? Is that something you anticipate at all for 2018? Or is it really just kind of waiting to see how the markets shake out before making any investment decisions?

Ronald Mittelstaedt: Well, it's a little of both, Noah. I mean, the reality is that we are constantly, in our annual budgeting process, we are constantly making capital upgrade and operating upgrade decisions to recycling facilities, and based on ever-revolving quality standards, not just from China but from mills domestically and elsewhere. And so that's sort of a continuous improvement process. So there's nothing step change that we're planning on doing in 2018. There are some things that are -- some very specific locations, based on what the throughput and the product quality looks like coming out of there.

On a real-time basis, look, there are markets where you've seen some pretty drastic changes. I'll give you an example -- a market like the State of Oregon, which has very robust recycling requirements. They're mandated. They're legislated. There are fiscal or financial penalties attached. The State of Oregon has authorized in certain cases in the last week the land-filling of comingled recyclables where there doesn't exist a market to move the product any longer, such as certain types of plastics and fibers. So that's a pretty large step from a very green recycling-progressive state. And that was done after their DEQ did a very deep investigation of what the real opportunities are to move this product. And they are stepping back what people are going to be able to recycle.

So you're seeing different things go on on a very dynamic basis by state and local market. And so we're adjusting to that. So it's one reason you don't go out and make a large recycling investment in this kind of environment when the commodity is just that, a commodity. And you've got to make sure that before doing that you know what the playing field for that revenue stream looks like.

Noah Kaye: Yes. Great. Thank you so much.

Operator: (Operator Instructions) Corey Greendale; First Analysis.

Corey Greendale: First I just had a couple of housekeeping things. Is $460 million still a good number for CapEx for the full year?

Worthing Jackman: Yes.

Corey Greendale: Good. And then for the 2018 EBITDA margin [thought] you gave, are you assuming -- I think, Worthing, you said that the E&P -- is that like a $200-million-ish [run], or a little bit above? Is that what you're assuming for 2018 in that 50 basis point improvement guide?

Worthing Jackman: Yes. It's just the rollover of the current activity. Because, as we said, we think that E&P activity increases further, oil recycling, fiber prices improve further from here. That's upside to the margin outlook for next year.

Corey Greendale: Good. And the 30-to40-bp negative impact from Chiquita, is that about what we should assume going forward every quarter until it anniversaries?

Worthing Jackman: Yes. It will run through July.

Corey Greendale: Okay. And sort of different topic. Ron, interesting to hear that the M&A pipeline is robust enough that you might use most of your, or a good chunk, of your cash balance. And I understand that, just in general, the margin profile of acquisitions is lower than the corporate average. But I was hoping you might be able to comment a little more just to set expectations on kind of the nature of what you're looking at. Like, how much would be a really large opportunity versus a bunch of small ones? And a margin profile of that stuff in the near-term pipeline?

Ronald Mittelstaedt: Sure. Well, again, let's frame what is large in our market model so that we -- in case people haven't followed us a long time. Remember, in our model, which is predominantly focused on either exclusive markets or secondary suburban type markets, a large transaction is $20 million to $40 million in revenue. So an extremely large transaction is something that looks more like $75 million to $200 million of revenue, like we did in the Groot case. Remember, Groot was the third largest transaction we'd ever done.

And so what I would tell you is that in that pipeline there's a company or two that looks about like a Groot, and we hope to maybe get one of those done. There are several companies that we would consider large in our traditional platform of $20 million to $40 million, integrated operations, new market opportunity, lots of growth opportunities to build out for multiple years around it. And then there are quite a few tuck-in transactions, ranging from $0.5 million to $5 million in revenue. So you've got some in each of those baskets.

And, again, we've said that we hope to deploy. We've got about -- I'm rounding -- about $0.5 billion of cash sitting on the balance sheet today and building. We would hope that number will be north of $600 million by the end of Q4 or so. And we would hope to deploy a decent amount of that, and perhaps more than that, if we get all the things that we're working on, by the end of the Q1-ish timeframe -- some by the end of this year and others by the end of Q1 timeframe.

Corey Greendale: Great. Good luck getting that done. Thanks for the detail. I'll turn it over.

Operator: Final question comes from the line of Kevin Chiang; CIBC.

Kevin Chiang: Maybe just a clarify on the comments just made. When you get through this pipeline here, which seems very elevated on the M&A, do you assume that you get back to that normalized $150 million of acquired revenue annually and implications for the buyback moving forward after you execute on these deals? Or do you think this pipeline remains robust for the foreseeable future here?

Ronald Mittelstaedt: Well, Kevin, I think that somewhat depends on, to an extent, what happens with tax reform. But having said that, as I've recently said publicly in some other forums, that I actually don't think it matters that much. Because here's the reality. There's a lot of pent-up M&A that has been awaiting tax change that, if tax change happens and you're going to see elevated activity because those people believe that there could be a two-to-three-year window before tax change goes the other way again. And it if doesn't change and it is killed, you're also going to see elevated activity, because they know it's as good as it's going to get and it's only going to get worse. So you're going to see elevated activity either way in my opinion in the next two to three years. I believe it will be because of the first and that we will have some sort of tax change. And we've been in an albeit slow growth but a steady growth environment. People's businesses have recovered. And so a lot of things set up for that to occur.

Kevin Chiang: That's great color. And just wondering -- and last one for me -- does FX at all play a role in how you think about M&A? You know, if the Canadian dollar is $0.10 lower than it is now, does it make a Canadian acquisition more appetizing for you as you use your stronger currency? Or does that not play a role at all?

Worthing Jackman: That does not play a--

Ronald Mittelstaedt: No.

Worthing Jackman: That does not play a role.

Ronald Mittelstaedt: That does not play a role. We sort of normalize -- I mean, obviously if you can pick your [stuff on] FX, that's great. But we sort of look at a normalized 10-year rolling conversion and where that average is. So it takes out the spikes and valleys.

Kevin Chiang: All right. Well, you called the bottom on the Canadian dollar with the BID acquisition. So I guess I'll leave it there. Congrats on a good quarter.

Ronald Mittelstaedt: Sometimes better lucky than good.

Operator: Thank you. And there are no further questions on the phone line at this time.

Ronald Mittelstaedt: Okay. Well, if there are no further questions, on behalf of our entire management team we appreciate your listening to and your interest in our call today. Both Worthing and Mary Anne Whitney are available today to answer any questions that we did not cover that we are allowed to answer under Regulation FD and Regulation G.

Thank you again. We look forward to speaking with you at upcoming investor conferences or on our next earnings call.

Operator: Thank you. Ladies and gentlemen, that does conclude the conference call for today. We thank you for your participation and we ask that you please disconnect your lines.