Waste Connections, Inc. [WCN]
Third-Quarter 2020 Earnings Conference Call
Thursday, October 29, 2020, 8:30 AM ET

Company Participants:
Worthing Jackman; President and Chief Executive Officer
Mary Anne Whitney; Senior Vice President and Chief Financial Officer

Analysts:
Tyler Brown; Raymond James & Associates
Jeff Goldstein; Morgan Stanley
Hamza Jaffer; KeyBanc Capital Markets, Inc.
Mark Neville; Scotiabank
Hamzah Mazari; Jefferies
Kevin Chiang; CIBC World Markets
Chris Murray; AltaCorp Capital
Michael Hoffman; Stifel Financial Corp.
Walter Spracklin; RBC Capital
Noah Kaye; Oppenheimer & Co., Inc.

Presentation:

Operator: Greetings, and welcome to the Waste Connections Third-Quarter 2020 Earnings Conference Call. [Operator Instructions] As a reminder, this conference is being recorded Thursday, October 29, 2020.

I would now like to turn the conference over to Worthing Jackman, President and CEO. Please go ahead.

Worthing Jackman: Thank you, Operator, and good morning. I'd like to welcome everyone to this conference call to discuss our third-quarter results and our outlook for Q4 and to provide some early thoughts for 2021. I'm joined this morning, safely distanced, by Mary Anne Whitney, our CFO.

As noted in our earnings release, sequential improvement in solid waste volumes and increased recovered commodity values drove better than expected results in the third quarter and provide incremental momentum going forward. We believe our strong operating results, financial performance and frontline support continue to differentiate Waste Connections during this year's unprecedented health, economic and social challenges.

Higher margin flowthrough from improving revenue during the quarter provided better than expected adjusted EBITDA margin and adjusted free cash flow generation. Adjusted EBITDA as a percentage of revenue in the period was approximately 40 basis points above our outlook in spite of 30 basis points higher than expected discretionary front line and incentive compensation costs impacting the quarter, which resulted from our more than $35 million commitment in incremental cost primarily directed to discretionary supplemental pay for frontline employees.

Solid waste margins expanded by almost 200 basis points compared to the year-ago period, with collection, transfer and disposal accounting for 80% of that increase. Moreover, year-to-date adjusted free cash flow of $778 million, or 19.2% of revenue, increased year over year, putting us firmly on track to exceed the adjusted free cash flow outlook for the full year that we communicated in August and positioning us for double-digit growth in adjusted free cash flow in 2021.

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

Mary Anne Whitney: Thank you, Worthing, 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, including forward-looking information within the meaning of applicable Canadian securities laws. Actual results could differ materially from those made in such forward-looking statements due to various risks and uncertainties. Factors that could cause actual results to differ are discussed both in the cautionary statement included in our October 28th 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, 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 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 diluted 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. Other companies may calculate these non-GAAP measures differently.

I will now turn the call back over to Worthing.

Worthing Jackman: Thank you, Mary Anne.

We're extremely pleased by our performance in the third quarter, as our results reflect both the resilience of our solid waste business and the accountability of our over 18,000 employees who have stepped up during such a challenging year.

Better than expected, 390 basis points sequential solid waste volume improvement in Q3 as compared to Q2 drove strong results in the period. The rates of recovery in solid waste revenue largely reflect the extent to which the reopening process has affected economic activity levels following slowdowns due to the closure restrictions and requirements in effect since the onset of the COVID-19 pandemic. The shape and pace of recovery of lost revenue continues to vary by geography, market size and customer mix. The volume improvement we saw in Q3 was most pronounced in regions which had experienced the greatest impacts from COVID, with Canada showing 750 basis points sequential improvement in our Eastern Region, which includes the Northeast US, up approximately 600 basis points sequentially.

In the aggregate through Q3, about 68% of solid waste commercial customers and 57% of associated revenue in competitive markets we track that had suspended or reduced service had reached out for the resumption of service or increasing frequency, up from 53% and 42%, respectively, at the end of Q2. Not surprisingly, the most impacted regions accounted for the majority of the Q3 increase, as the less affected

markets had already led the commercial revenue recovery we saw in Q2. And the rate of growth in those markets has since slowed, in many cases hitting a near-term plateau in the range of 60% to 65% revenue recovery levels.

While the shape and pace of recovery may have varied by region and market, our focus on quality of revenue and cost control has been consistent, as evidenced by the strong underlying solid waste margin expansion during the third quarter in spite of about 80 basis points of additional discretionary front-line and incentive compensation costs. We are well on the way to meeting our commitment of over $35 million this year in incremental employee support, primarily directed at supplemental pay for our frontline employees.

Our safety focused, Servant Leadership-driven culture has guided Waste Connections' response to this year's unprecedented health, economic and social challenges and that response has resulted in higher engagement, lower voluntary turnover and improved safety, providing for execution at a high level. Our safety-related incident rates continue to decline, even as economies reopen and volumes return, such that we are seeing incident rate levels at multiyear lows. These improvements have been augmented by a more than 20% reduction in voluntary turnover year to date, as another benefit of a more stable, experienced workforce with fewer incidents and accidents.

And we are excited to further improve on these trends as we complete our fleetwide rollout of the next generation of onboard camera technology that incorporates machine vision and AI. Our commitment to the health, welfare and development of our employees, environmental stewardship and the support of our local communities are detailed in our 2020 Sustainability Report, released earlier this week, which includes long-term aspirational targets and our commitment of over $500 million over a 15-year period for investments to meet or exceed our targets. These investments primarily focus on reducing emissions, increasing resource recovery of both recyclable commodities and biogas, reducing reliance on offsite disposal for leachate, increasing employee engagement and further improving our industry-leading safety performance. At Waste Connections, sustainability initiatives have always been integral to and consistent with our strategy and focus on long-term value creation for our shareholders. As such, the investments will be undertaken in the ordinary course of business with attractive ROI expectations and are not additive to what we consider to be typical capital expenditures.

Looking at acquisitions, we're on pace for another solid year of activity in spite of COVID-related constraints. In fact, the pace of activity has increased over the past few months. Year to date we have signed or closed 16 acquisitions in 11 states in the US and 1 province in Canada, totaling approximately $135 million in annualized revenue. They include, as noted last quarter, a new market collection transfer and recycling company with $40 million in annualized revenue and, more recently, another new market collection and transfer company with about $25 million in annualized revenue, both of which are on track to close mid-Q4. Dialogue remains as active as we have seen in years, especially with some tax-driven sellers interested in getting deals closed by year end.

Our strong operating performance, free cash flow generation and balance sheet strength positioned us for a double-digit percentage increase in our quarterly cash dividend. As announced yesterday, our board of directors authorized a 10.8% increase in our regular quarterly cash dividend, our tenth consecutive double-digit percentage increase since initiating the dividend in 2010. Still, our dividend remains at less than 25% of adjusted free cash flow. That level, coupled with liquidity of over $2 billion and leverage of about 2.3x net debt to EBITDA, provides tremendous flexibility to fund both continued outsized acquisition activity and opportunistic share repurchases.

Now I'd like to pass the call to Mary Anne to review more in depth the financial highlights of the third quarter and provide a detailed outlook for Q4. I will then wrap up and provide some early thoughts on 2021 before heading into Q&A.

Mary Anne Whitney: Thank you, Worthing.

In the third quarter revenue was $1.39 billion, or about $20 million above our outlook, on better than expected solid waste volumes during the period and higher recovered commodity value. Revenue on a reported basis was down $22 million, or 1.6%, year over year, on E&P waste activity down $43 million year over year. Acquisitions completed since the year-ago period contributed about $47.1 million of revenue in the quarter, or about $44.2 million net of divestures. Solid waste price plus volume growth on a same-store basis in Q3 was negative 2%, reflecting an improvement of 330 basis points from Q2 and ranging from positive 2.6% in our mostly exclusive West Coast markets to negative 4.5% to 5% in our most COVID-impacted Eastern and Canada regions.

Pricing growth overall in Q3 was 3.7%, including core price of 4.1% partially offset by a 40 basis point reduction in surcharges. Pricing ranged from 2.6% in our more exclusive markets in the Western Region to an average of over 4% in our more competitive regions.

Solid waste volume growth in Q3 was down 5.7%, ranging from flat volume in our Western Region to down approximately 9% in our most impacted regions in the Northeast US and Canada. As we have noted, our volumes largely reflect the pace and shape of shutdown and reopening activity across our markets, which varies and depends on geography, size and customer mix in each market.

Looking at year-over-year results in the periods on a same-store basis, we saw sequential improvement in Q3 from Q2 in solid waste in every line of business. Commercial collection revenue, which was down 7.6% in Q2, improved by over 500 basis points to down approximately 2.5% in Q3. Excluding the most impacted markets in the Northeast and Canada, commercial collection revenue was up about 30 basis points year over year.

Roll-off revenue decreased approximately 8% on pulls down about 7% year over year and revenue per pull-down about 1% on lower weights. This compares to revenue on pulls-down 13% and 12%, respectively, in Q2.

Solid waste landfill average price per ton increased 4% year over year on revenue down about 2% on a same-store basis, as total tons declined about 6% year over year, about 400 basis points better than Q2. Q3 MSW tons were down about 3%. Special waste was down 9% and C&D was down 12%.

Looking at E&P waste activity, we reported $23.6 million of E&P waste revenue in the third quarter, down about 64% year over year, in line with our expectations on reduced drilling activity, which appears to have found bottom around current levels with rig counts up nominally in recent weeks.

Looking at Q3 revenues from recovered commodities, that is, recycled commodities, landfill gas and renewable energy credits, or RINs, excluding acquisitions in the aggregate they were up about 25% year over year due to both higher RINs and higher recycled commodity revenues due to strong fiber value.

Adjusted EBITDA for Q3, as reconciled in our earnings release, was $432.6 million, about $13 million above our outlook due to higher revenue and stronger flowthrough from returning disposal and commercial collection volume as well as higher recovered commodity values. Adjusted EBITDA as a percentage of revenue was 31.1% in Q3, about 40 basis points above our outlook, and down 30 basis points year over year. A 190 basis point year-over-year improvement in solid waste, including a 30 basis

point benefit from recycling and RINs, was more than offset by a 130 basis point drag from lower E&P waste activity, an 80 basis point impact from discretionary COVID-related front line and incentive comp, plus another 10 basis points from the margin-dilutive impact of acquisitions completed since the year-ago period.

Fuel expense in Q3 was about 3.4% of revenue, down about 40 basis points year over year on fewer gallons, lower rates and a CNG credit of about $900,000. We averaged approximately $2.33 per gallon for diesel in the quarter, down about 10%, or $0.27, from the year-ago period.

Our effective tax rate for the third quarter was 17.6%, slightly lower than expected.

GAAP net income per diluted share was $0.60 and adjusted net income per diluted share was $0.72 in the third quarter. Adjusted net income in Q3 primarily excludes intangibles amortization and other acquisition-related items.

Year-to-date adjusted free cash flow of $778.4 million, or 19.2% of revenue and 63% of adjusted EBITDA, was up $15.5 million year over year in spite of lower EBITDA, given the benefits of working capital, including reduced DSOs, and the deferral of payroll taxes as provided for by the CARES Act. As noted earlier, given our outsized conversion of adjusted EBITDA to adjusted free cash flow, we are well on our way to exceed the full-year outlook for adjusted free cash flow of $805 million to $835 million that we communicated in August.

Debt outstanding at quarter end remained at about $4.7 billion. As Worthing noted, total available liquidity remains over $2 billion, including cash balances of $859 million. Our leverage ratio, as defined in our credit agreement, was about 2.7x debt to EBITDA and on a net debt basis our leverage remained at around 2.3x debt to EBITDA at the end of Q3. Our current weighted average cost of debt is approximately 3.3%, with essentially all of our debt at fixed rates.

I will now review our outlook for the fourth quarter 2020. Before I do, we'd like to remind everyone once again that actual results may vary significantly based on risk and uncertainties outlined in our safe harbor statement and filings we've made with the SEC and the securities commissions or similar regulatory authorities in Canada. We encourage investors to review these factors carefully.

Our outlook assumes no significant change in underlying economic trends. It also excludes any impact from additional acquisitions that may close during the remainder of the year and expensing of transaction-related items during the period.

Revenue in Q4 is estimated to be approximately $1.335 billion. We expect solid waste price of approximately 4% and volumes of approximately negative 6%. Although we haven't seen a weakening in volumes, we think it's appropriate to remain cautious, as we have throughout the pandemic. Given concerns about additional shutdowns or other restrictions potentially being imposed, especially as we head into the winter months. In addition, we expect revenue from both resource recovery activities and E&P waste to remain similar to Q3.

Adjusted EBITDA in Q4 is estimated to be approximately $400 million, or about 30% of revenue, which would be down 80 basis points on a reported basis and down just 30 basis points year over year, adjusted for the 50 basis point benefit from CNG in 2019, which resulted from the 2-year catchup in CNG credits in that period.

Our outlook cautiously assumes that certain costs, such as medical, which was down 30 basis points as a percentage of revenue in Q3, become headwinds in Q4 in the event that deferred or discretionary individual spending patterns should change.

Depreciation and amortization expense for the fourth quarter is estimated to be about 13.8% of revenue. Of that amount, amortization of intangibles in the quarter is estimated to be about $32.5 million, or about $0.09 per diluted share net of taxes. Interest expense net of interest income in Q4 is estimated to be approximately $40 million. And, finally, our effective tax rate in Q4 is estimated to be at about 20.5%.

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

Worthing Jackman: Thank you, Mary Anne.

Again, we are extremely pleased with our year-to-date performance, particularly given the challenge of projecting the business and managing through COVID-driven uncertainties which have been amplified by the headwinds of high-margin decrementals from lower E&P waste activity and negative solid waste volumes.

In spite of it all, we have continually raised the bar and consistently beaten our expectations. Our Q3 results and Q4 outlook would put us about $60 million of revenue, $25 million in adjusted EBITDA and 20 basis points in adjusted EBITDA margin, above the full-year outlook we provided in August, without the benefit of expected incremental acquisition contribution and with strong free cash flow conversion.

In this evolving environment, our employees have remained focused on controlling what they can, with an uncompromising commitment to protecting the health and safety of their colleagues, providing the highest level of customer service and supporting the communities we have the privilege to serve.

I'd like to reiterate how incredibly proud I am for the way our team has supported our front line and their families and delivered on their commitments to drive these results. We've always maintained that at Waste Connections it's our people who are our greatest differentiator and this year has made that all the more important and apparent.

As we look ahead, we expect to emerge from this challenging period better positioned financially, with tremendous flexibility with respect to capital allocation, and operationally, with higher operating leverage in solid waste and both safety-related incidents and voluntary turnover levels already achieving multiyear lows.

We expect to expand reported margins in 2021 and capitalize on additional growth opportunities. Moreover, given the strength of our year-to-date adjusted free cash flow, we are well positioned for double-digit percentage growth in adjusted free cash flow in 2021.

Although we won't provide formal outlook for 2021 until next February, we're able to provide some early thoughts, assuming no change in the current economic environment. In summary, we believe 2021 likely sets up for solid waste price growth to range between 3.5% and 4.0% with volumes expected to turn positive after we anniversary the start of the pandemic. Price-led organic growth and high flow-through from improving volumes should drive underlying margin expansion in solid waste collection, transfer and disposal in spite of the hopeful return of certain discretionary expenses that we either reduced or eliminated this year due to the pandemic or the normalization of other expenses that declined as a result of the shutdowns.

In addition, depending on the level of activity between now and year end, we could enter 2021 with more than 2% in revenue growth in place from completed acquisitions. We would expect to have better visibility on the tone of the economy and expected acquisition contribution, E&P waste activity and recovered commodity-driven revenue in February when we provide our formal outlook for the upcoming year.

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

Questions & Answers:

Operator: Thank you. [Operator Instructions] And our first question comes from the line of Tyler Brown with Raymond James.

Tyler Brown: Worthing, so thanks for the details about the recovery. It feels like things are kind of on track here. And I appreciate that 68% of the paused commercial customers have returned. Maybe you gave this figure a couple quarters ago, but what percent of the commercial book is that applicable to? And at this point, based on the intelligence that you have, how do you feel about that last 30%? Is it structurally gone or do you still feel like there's -- some of that will come back?

Worthing Jackman: So, Tyler, good question. So where we track it obviously is where we have a sales force where we can track account by account and account-by-account recovery and the payouts for that. That probably accounts for about 80% of our commercial business, because obviously in markets where we have franchises, we do not have sales people. We have 100% of the business. And so that accounts for about 80% or so of the commercial activity.

Look, it's hard to say with regards to those that have not returned yet. We definitely assume that there's some permanently closed shops. Right? And it's hard to see, hard to anticipate or project those shops reopening and returning. So this is the new jumping-off point. Perhaps there's incremental positive volume growth next year if through another stimulus plan those shops try to get recharged and reopened. But without a doubt there will be casualties in small business as a result of the pandemic and we're not going to sit here and project a percentage recovery on that because, to your point, I think some of that's permanently gone.

Mary Anne Whitney: And, Tyler, just to follow up on that, I would say that we continue to believe that customer cancellation statistics aren't a good barometer because we continue to not see a material difference year over year. And to Worthing's point, we know that there are cancellations coming.

Tyler Brown: That's very helpful. And then, Mary Anne, obviously margins were very good this quarter, particularly at the core level. And I think you mentioned right at the tail. I just want to make sure it's clear. So in Q3 healthcare was actually a tailwind. We didn't see that actually shift over to a headwind, but you are expecting it as a headwind, presumably in Q4 and then probably in '21?

Mary Anne Whitney: Yes, Tyler. That's a fair way to characterize it. We had talked about the fact that in Q2 it was a nice tailwind. And we said that we expected that if people started getting out more -- this would be one of those costs that went away as a result of shutdowns. Right? So it impacted behavior and we thought that that behavior would begin to normalize over time. And what I'd say is Q3 versus Q2 some of those costs came back, but it continued to be a tailwind. And, yes, specifically I mentioned that if you're thinking about sequentially why is the margin, the underlying margin expansion, in solid waste in

our projections, our outlook for Q4, less than Q3, that would be an example of what we're factoring in. To the extent that we're wrong and it doesn't come back as much as we thought, it would continue to be a tailwind in Q4.

Tyler Brown: Okay. And then -- so this is a conceptual question. You guys talked about it a little bit. 2020 has been very bizarre on many fronts -- I think we could all agree on that -- but particularly with all of the movement in costs. You guys talked about expanding solid waste margins, so that into '21, despite all of the idiosyncratic things -- travel, healthcare, things like COVID, supplemental comp, kind of maybe easing. But is there any way to kind of just frame for us what we're kind of thinking next year from a solid waste margin perspective? Is that a 50 basis points? Or any just high-level thoughts there?

Worthing Jackman: Good question, because we were clear in our script that we expect reported margins to expand next year. And to the extent that E&P just remains flat year over year, or even at current -- if it remains at current run rates even, then that obviously provides, or could provide, a 40 or a 50 basis point headwind to reported margins next year. And so for us to say that reported margins are expanding, to your point, it means that solid waste margins are expected to expand north of 50 basis points next year.

Tyler Brown: Okay. Very helpful. And then just last -- a quick modeling question. So, Mary Anne, just based on the deals signed or closed, just from a modeling perspective right now based on everything, how much acquired revenue should we think about in '21?

Mary Anne Whitney: So if you think about $90 million, $95 million, in '21 and the cadence being kind of by quarter 30, 30, 15, 15 is a fair way, or 20, 15 is a fair way to think about it.

Worthing Jackman: And, Tyler, they'll be some additional things that will likely get done this year that will be additory to that as we give formal guidance in February.

Tyler Brown: All right. Well, thank you very much.

Operator: And our next question comes from the line of Kyle White of Deutsche Bank. Pardon me, Mr. White. Your line is open. I'm sorry; Mr. Kyle White, could you please check the mute function on your phone? I'm sorry, sir. We're unable to hear you. We'll move on to the next question.

And our next question comes from the line of Jeff Goldstein with Morgan Stanley.

Jeff Goldstein: I just wanted to ask the recovery question a little different. So just looking at the pace here, volumes are down 5.7% in the quarter, which is better than you thought but also in line with I know when you had disclosed in July basically implying trends had been flat. And then now your guidance for 4Q is a similar number. So I guess just kind of bigger picture, is it -- do we need a vaccine? Are you looking for additional maybe stimulus post-election? Just what do we need here really to get volumes moving towards flat again?

Worthing Jackman: Again, I think it's the [anniversarying], as we've said all along, of the pandemic. Right? I mean, we'll -- the pandemic started hitting numbers in middle of March. And so once we get through Q1 and we fully anniversary the effects of the pandemic, volumes should start turning positive in Q2. That's not dependent on a vaccine. That's not dependent on a stimulus. That's just math. Because if you look at the rate of recovery since the lows of Q2, our revenue run rate in every metric is much stronger than what was reported in Q2 this year. And so, just running flat to current levels of activity produces positive volumes beginning in Q2. Now, to the extent that the economy reopens because of the vaccine, or because of stimulus plan that provides some juice to the activity, then that's just further improvements in reported volumes in that year.

Jeff Goldstein: Okay. That's helpful. And then --

Worthing Jackman: [Wish I could] say [indiscernible] more insightful than that, but it is math.

Jeff Goldstein: No, I appreciate it. And then I was just hoping for some more color on the temporary roll-off side, especially around housing and if that at all has impacted the improvement. Down 8%, which I think was about a 500 basis point acceleration. Just given what we're seeing kind of in the strength of the housing market and what we're hearing around continued supply constraints there, are you seeing any type of benefit? Do you think it could continue? Just what are you seeing on temporary roll-off really.

Mary Anne Whitney: So, to your point, we did see nice sequential improvement in roll-off. I'd say that certainly the housing can be a factor on that. There's also just the reopening. And I look at, for instance, where that sequential improvement was strongest and it was in Canada, by way of example, where you had the whole holistic shutdowns of economies and there was arguably some pent up demand when they turned things back on and we saw construction projects that had been put on hold get restarted. And so I'd say that was as much a factor, if not more, than for instance the housing numbers getting a little better.

I'd say the other thing that stands out is I just think in general the best volumes we continue to see are on the West Coast, where I'd say that over the past few quarters we have seen that that return of housing did help those numbers. So it's a factor, but it's one of a few different factors that I think are driving that sequential improvement.

Worthing Jackman: I know it feels like this has been a dog year with regards to remembering things, but recall when the shutdowns happened in Q2, not every state or -- shut down construction as well. Right? Washington, for instance, was a state that shut down construction as part of the pandemic, and so you saw a great -- large snapback in Q3, sequentially Q2, Q3 in Washington. Canada the same way. When you look at Ontario or Quebec especially, would shut down construction activity as part of the closures. And to Mary Anne's point, as those reopened obviously you have a snapback sequential improvement Q2 to Q3 in that area as well.

Jeff Goldstein: All right. Appreciate the color.

Operator: And our next question comes from the line of Sean Eastman with KeyBanc.

Hamza Jaffer: This is Hamza Jaffer speaking for Sean Eastman. I just wanted to turn the question over to volume. So last quarter we talked about a monthly volume trend. I was just curious if you could give us more color on September. And we've seen this deurbanization trend this year, but it's being -- it remains to be seen. I was just curious if you think Waste Connections has been benefiting from this dynamic, with such a significant amount of volume driven by secondary markets and whether you think this could be a nice tailwind for the business in the coming years.

Worthing Jackman: Okay. Well, first, in the secondary markets, as we laid out in the script, a lot of those markets were not as heavily impacted in COVID and were kind of early to recover most of what they had lost in Q2. And that was a big contributor to Q2's uplift. We still continue to see volume strength in those marketplaces and in many of those markets we expect positive volume potentially in Q4. And so, while most of those reflected that flat volume year over year in Q3, that continued momentum could turn positive in Q4.

With regards to the current trends, again, I think we laid out in our outlook that we still expect volume declines to be about 6%. We're probably running a little bit better than that as we sit here today. But, as

Mary Anne pointed out, it's important to stay cautious as you look ahead, given the winter season that we're entering into. And so obviously if the trends that we see right now continue through the balance of the quarter, we should set ourselves up for nice repeat on the top line with regards to revenue reported versus expectations.

Hamza Jaffer: Got it. Thank you. And then just level setting on the M&A environment, clearly the election and policy is a big variable. So just as we look out into 2021 and 2022, what are the primary [watch points] there in terms of whether we see greater or less than normal acquisition activity for Waste Connections?

Worthing Jackman: Well, if you look at this year, in spite of pandemic this will be an above-average year in total revenue activity for us and what I would call an average year, a typical year, with regards to the number of transactions. I mean, this year we'll get probably 3 or 4 transactions done in that $25 million to $40 million range. We'll probably get a dozen or more tuck-ins done as well. So to be doing 16 to 20 or so transactions, I'd call it a typical year, which is, again, remarkable given the backdrop that we're in.

I say that as a setup because we've also said a lot of our transactions are kind of lineage-transition driven and those will continue to influence the sale of companies in '21 and beyond. Obviously, exhaustion can also lead to folks' desire to sell. I mean, it's tougher and tougher to -- it was tough running a business before the pandemic, given many constraints, and the pandemic's made that even more magnified for many operators. So exhaustion can also lead to that. Obviously, tax-driven transactions as well, that's driven some people to come off the sidelines this year and get some things done. And to the extent that the tax dialogue in '21 -- if tax law changes in '21 is it retroactive or not? Do they -- like, in the Trump period in the first 2 years took them 2 years to get tax reform in place. So do they get it done in '22, which might [prod] people to get deals done in '21. It's uncertain.

But, look, what drives our typical transactions with second, third, the fourth-generation type businesses is lineage transition. And we expect M&A activity to continue beyond this year.

Hamza Jaffer: Got it. Thank you very much. Congratulations on the excellent quarter.

Operator: And our next question comes from the line of Mark Neville with Scotiabank.

Mark Neville: First, great quarter and just a generally great job managing through the pandemic. So good on you.

Maybe just going back to the recovery -- and I apologize if you touched on some of these points. But just from a high level, I'm just curious, in the markets that were sort of first to open, are you still seeing sort of month-over-month, week-over-week sort of sequential improvement in the volume recovery? Or are there certain markets where your sort of volume is sort of hitting a ceiling? And then, I guess similar type question, in the markets that are slower to open or reclosing, like here in Montreal, I'm just curious sort of how [indiscernible] specifics, but just generally how much room upward is there before you sort of get to a more normalized or to where the other markets may be?

Mary Anne Whitney: So happy to cover that, Mark. So what we've said is that in the aggregate the recovery of revenue in the commercial markets we track is about 57%. And I would break that into the ones that you described had come back more quickly and were less impacted. So the less impacted markets are in the low to mid-60s, between 60% and 65% recovered, as contrasted with what we would describe as the more impacted -- Canada, the Northeast US, are in the low 50s. So that's the delta we're seeing that remains between those two buckets, if you will.

And to your question about the rate of recovery, we've absolutely seen that slow down in those less impacted markets. And that, as Worthing described in his remarks, that really what lead the Q2 recovery were those markets and that what lead Q3 were the more impacted markets. We talked about the sequential improvement in Canada, for instance, being 750 basis points overall volumes and our Eastern region 600 basis points. You contrast that with, say, a 300 basis point improvement in a place like the West Coast or our Southern region. I look at individual markets -- a place like Toronto, which through Q2 had about 30% recovery is now in that low to mid-50s, so perfect example of one of those impacted markets coming back strong in Q3. And I'd contrast that with, for instance, North Texas in a place like Dallas where through 2Q they were already back to the low to mid-50s and now they're back to low to mid-60s, again in line with the average we're seeing in those markets. So I think that speaks to the flattening.

And, again, we don't know where the ceiling is. We describe it as a near-term plateauing, because that's what we've been seeing over the past few months.

Mark Neville: Okay. That's super helpful. And, sorry -- in those markets, the low 60s, or 60, 65 [belt], is there still -- or maybe you just answered the question -- but is there still sort of sequential improvement happening there? Or is it really just leveled off almost completely?

Mary Anne Whitney: Again, to be clear, we saw it throughout Q3. And there's still opportunity, because you have various markets within those buckets. And, for instance, New York City -- I talk about these impacted markets are on average around back 50, 55%. New York City is still in the mid-30s.

Worthing Jackman: And so it's our fastest growing market right now.

Mary Anne Whitney: Right. It's a great point. Smaller base, but fast growing.

Worthing Jackman: Yes.

Mary Anne Whitney: So, yes, there's still absolutely opportunity. We're just talking at a high level in what we're seeing.

Mark Neville: Yes. I appreciate that again. Again, it's just pretty fluid. So, again, I don't want to get too detailed. But I appreciate all that. Maybe just on the free cash for next year --

Worthing Jackman: [Indiscernible] --

Mark Neville: Oh, sorry. Go ahead.

Worthing Jackman: The week-to-week trends, for instance in New York City, are quite notable. It's interesting to see how the city is turning back on.

Mark Neville: Okay. Thanks. Again, just maybe on the free cash then, through 2021 I know you like to sort of talk free cash conversion over time down to the low 50s, obviously much better. When we think about next year, is there any sort of discrete or certain items you want to point out or maybe don't want to give us an exact item where you think the conversion falls, but just something -- anything you want us to keep in mind when we're mulling out next year's free cash conversion? Thanks.

Worthing Jackman: I think we've been consistent throughout the third quarter in laying out our expectations about 2021. And that's been to put a marker at $950 million and just lay out an expectation

that we ought to do $950 million or better for the full year. And, again, you back into that and that's why we talk about double-digit growth in free cash flow year to year.

Mark Neville: Good. Sorry, just one last one. Worthing, you mentioned some deals in Q4 that look set to close. And I think you put some numbers around those. I just didn't catch them.

Worthing Jackman: Well, I think Mary Anne put the numbers around the quarterly expectations for next year based on the $135 million we'd already signed or closed. And what I said is anything that we do -- which we should get a few more things done this year -- would be additive to that and that we would lay that expectation and those numbers in in February. But in the aggregate what we said is that if you look at what we've signed or closed and what we think we'll get done, we'll likely go into 2021 with 2% top line growth already in hand from M&A.

Mark Neville: Thanks again and, again, great job.

Operator: And our next question comes from the line of Hamzah Mazari with Jefferies.

Hamzah Mazari: My question is largely around share buyback. Is there a reason why you're not buying back more stock? And why I ask is historically when the Company had average to slightly above average M&A years, I think you still bought back stock at the same time and size. Because your leverage is the lowest it's been in history. You're sitting on a lot of cash. Free cash flow is running double digits. And it looks like acquisitions are not going to be as big as 2018 and '19. Even if you look out -- 2020 is almost done -- 2021's a big question mark. I doubt it will be as high as 2019 or '18, unless you say otherwise. So just any views there or any high-level thoughts or what you're thinking?

Worthing Jackman: Sure. Look, we were active earlier this year in buying back our stock. We always use the word "opportunistic" with regards to timing of when we do things, because we also like to maintain flexibility for growth opportunities that come along. But you tell me who's going to win the presidential election and you tell me what's going to happen to tax laws next year. You tell me what's going to happen to the stock market as a result of that. But lot of folks, as you know, talk about a sugar high if a stimulus gets done, which will flow through the stock market and may prop it up into early next year. Then if the reality of the tax law changed, that could be harsh. But that could create opportunities to buy the stock back.

We try to play the long road here. We try to look ahead at expectations around the stock markets. And I'd rather be patient and buy right than just be a willy-nilly buyer at any price every day.

Hamzah Mazari: Got it. And then my other question is just around ESG. And I actually want to ask about the E rather than the S and the G. And I know you put out your Sustainability Report. But I know you do renewable, landfill, gas and recycling, but how do you view landfills as part of the E equation? Do you think they're misunderstood by the ESG community in that they're sort of bad for the environment? Any thoughts as to the E, where you rank there, what you can do better there?

Worthing Jackman: So I think what we can all do better is just continue to be more up front and more visible at what we do. Look, a lot of things that we talked about in our ESG report are things we've been doing for 20-plus years. We've just stayed below the radar screen in telling our story.

With regards to landfill, with landfills, you tell me. First off, look at other economies without the type of strict hygiene and regulatory environment around waste disposal. I'll put what we do in the US up against any other economy and landfills play a big part of that. But landfills are also a big biogas generator and

renewable energy source. You see some -- many of our efforts around increasing investments within biogas facilities now that are landfills are getting more mature and gas generative enough to do that.

So by all means, landfills that -- you're right, they do have bad names and bad connotations in many communities. Many cases of which communities that weren't there when the landfills were built. They built themselves up next to landfills. But, look, it's a double-edged thing, but the scarcity of landfills turns into pricing opportunities within many markets because it is a scarce resource. It's an ever-increasing, increasingly higher cost to operate landfills and to build out landfills. And that will drive higher pricing on landfills. But, again, its source for renewable energy is one that will become better understood if we tell the story right, because the opportunities there are tremendous. And the returns on those kinds of investments, more importantly, are incredible.

Look, ESG doesn't mean you should go and throw away money and dilute returns. What we're talking about are opportunities and running the good business that is not only good for the E, as you say, but also good for the P&L, too.

Hamzah Mazari: Got it. And last question. I'll turn it over. We talked a lot about commercial volume. How do you think this cycle is different than past down cycles for waste? And at a high level, waste lags going into a downturn, lags coming out. It doesn't look like it's lagging coming out today. And so that may be a difference. I don't know, maybe the cost structure is different, because some of what you alluded to a little bit on the margin performance this quarter. Just any thoughts as to how this cycle's different for waste than prior cycles?

Worthing Jackman: Well, I think you almost answered your own question in that prior cycles were more coincident with the decline in temporary inactivity. And commercial stayed strong. This is a decline that hit commercial, so the way it was hit is almost tracking the way the macro economy has been hit and GDP has been hit, meaning the temporary side of the business has still remained, I guess, a little more resilient than what we saw as a quick contraction in commercial. But commercial as it recovers is very sticky. And so as that recovers and you see the high margin flow through, that will continue to benefit this industry.

But to your other point, the cost structure is different. And I think that's a statement that could be said about most businesses across multiple industries. How we accepted it and how we did things and how we travel, what we spend money on, et cetera, has changed. And so I don't see all those costs really ever coming back fully into the P&L, because we will be doing things differently. We still want -- we still pine for the days that we're together, that we're having big parties, that we're spending a lot at the bar, so to speak. But clearly as the economy reopens, as people get more comfortable being together based on changes in the pandemic or vaccines, et cetera, it's still hard to see that the shape of how we do things is -- gets back to where it was pre-pandemic. And that creates a different cost structure in our P&L and others.

Hamzah Mazari: Got it. Thank you.

Operator: And our next question comes from the line of Kevin Chiang with CIBC.

Kevin Chiang: Congrats on a good quarter there. Maybe if I could just dig into some of your assumptions, I guess for volumes in the fourth quarter. And, maybe specifically, I appreciate the conservatism just given all that you don't know and some of the rollbacks and the reopenings in some of these economies like here in Canada and I suspect in parts of the US. Has that changed how you think about maybe your bad debt assumptions as you get to the winter season? Just anecdotally here in Toronto, lot of small businesses have been pretty clear that if they have to get through another shutdown that they

probably don't make it through the other side of this through a tough winter season. Just wondering how you're looking at your bad debts over the next quarter or two.

Mary Anne Whitney: Sure. So interestingly, Kevin, we talked about bad debt last quarter as being one of the costs, if you will, of COVID. And it's actually come down this quarter and it's actually closer to our more normalized rate for us. And we've talked about DSOs coming down as well. A portion of that will be E&P, of course, still. And it's also solid waste. What we're finding is that as customers come back, they're paying us. Right? So we're seeing the recovery of volumes. Coincidental with that is a reduction in bad debt. So that's encouraging.

And to your point about those customers who aren't going to come back, as I said earlier, we're not -- we're mindful of the fact that cancellation rates are still what I would say is artificially low. And so that's why we're not baking in more recovery. And we think it's prudent at this point to kind of think in terms of current levels remaining the same. So I'm not expecting any big bad debt comeback, but I'm not expecting it to get materially worse from here at this point.

Worthing Jackman: Yes. We've been cautious on how we've positioned ourselves for potential deteriorations in bad debt.

Kevin Chiang: Okay. That sounds very prudent as well.

Worthing Jackman: [Indiscernible] --yes. So we've already positioned for that and it's not as bad as we think. Again, that will be upside.

Kevin Chiang: Maybe my second question here -- and I think Mark was asking about the free cash flow. If I just take -- and I know that you'll exceed it, just based on your comments today. But if I look at your free cash flow guidance, I guess, your conversion from the outlook you provided last quarter, it's about 52% of EBITDA, yet you're tracking well ahead of that through year to date. You're getting good flow through even with the challenges of E&P. If I ask this question maybe a different way, do you think you can get back to, like, a mid-50% free cash flow conversion of EBITDA, even with E&P sitting where it's at today, just given how strong your conversion has been through a very challenging year already?

Worthing Jackman: Yes. Well, look, we've always said own us for 50 to 52, love us in the years we do 55. Right? And so I would never model a -- do a long-term model at a consistent 55%. Obviously, things can change. As you look ahead, whether it be tax law changes in the US around bonus appreciation as those wean off in '23. Changes in tax rates obviously could influence that a little bit as well. So, look, we're still comfortable in that longer-term view of 50 to 52%, even without E&P coming back. Obviously, to your point, if E&P comes back that's another potential boost and a tailwind to get that higher as well. But, look, we're already well positioned to do the upper end of that or better this year. That is still leaps and bounds ahead of our peers and the years that we do better than 52%, we'll just take that and enjoy it.

Kevin Chiang: For sure. And maybe just one housekeeping question for me, and maybe this is to Mary Anne. I did -- maybe surprising to me -- I did notice the core price sequentially did improve in Canada. I'm just wondering if that's just a reflection of that sharp volume rebound you noted that you saw in Q3, or if it's anything unique that happened in Canada in the third quarter.

Kevin Chiang: Of course. That's a good point, Kevin. You did see that increase, which went counter to the rest of the price movement, which of course is playing out as we expected, that it's stepping down. In Canada you had some PIs that were pushed out last quarter that got implemented in Q3. And so that's why you saw that. It dropped a little lower in Q2 then we would have otherwise planned and came back a little in Q3.

Worthing Jackman: It was a conscious decision to defer those price increases.

Kevin Chiang: Perfect. That makes a ton of sense. Thanks. And that's all my questions. Great quarter.

Operator: And our next question comes from the line of Chris Murray with ATB Capital Markets.

Chris Murray: Thinking about acquisitions, historically you've always talked about acquisitions being kind of 3 to 4% of revenue as you go into the next year. You're kind of calling out 2 this year. I guess maybe as we start thinking about the next couple of years, is it a function of kind of the law of large numbers or was just -- is it something around the acquisition pacing. How much of that was impacted by COVID this year? And is it something we should be thinking about getting back to that number? So I'm just trying to maybe frame it over how to think about acquisition growth over the next couple of years.

Worthing Jackman: Sure. No, we typically -- we look at a typical year and think in terms of $125 million to $150 million of acquired revenue. And that right there is -- I'm just going to round -- 2 to 3% or so of growth in the year. If you look at this year, again, we're knocking down -- we've already knocked down the midpoint of that $125 million to $150 million and anything we do the balance of the year we'll push that to the upper end or higher. Going into a year at 2% growth, obviously what we don't have in that number yet is everything we get done in 2021, which will be additive to that 2%.

And so, look, we are not chasing a growth rate, to your other point. Obviously, as the business grows a typical year of $125 million to $150 million will be a slightly lower percentage as time passes. But without a doubt you episodically see larger transactions, $50 million to $100 million type revenue transactions, into the mix, that individually can push that 2 to 3% to something like 3 to 4%. Right? And so, we've seen that year in, year out the past few years, but we always think in terms of an average year being that $125 million to $150 million and the percentage top line will be what it is.

Chris Murray: Okay. So just think about that as the base number in terms of what you're kind of looking for for growth. That's fair enough. And then just going back to your ESG Report --

Worthing Jackman: [Indiscernible] -- we always say don't own us for that, but let that be upside.

Chris Murray: Sure. Going back to your ESG report and sort of your thoughts around the $500 million in spending, one of things that I know we've certainly been discussing with clients is in a change of administration, probably like we saw in the change of the last administration, different things happen. RIN pricing certainly moved around with changes in regulation. And I know it's hard to try to figure out where this goes. But certainly if you think about things like gas capture and RIN credits and even vehicles and shifting there -- certainly California had made some disclosures about wanting to get off any sort of fossil fuel type powered vehicles in the next few years. What's the feasibility of your ability to either accelerate or pivot into some of those technologies? Or -- and I guess what I'm curious about is it still seems like early days, or do you think that the maturity of the technology is more than just a science project to this point?

Worthing Jackman: No. Look, some of your observations with regards, for instance, to gas, I mean, the maturing of our landfill network creates more opportunities looking ahead for biogas capture investments, with very attractive ROIs, than in the rearview mirror. Right? And do we are very bullish on that.

And that's -- obviously you mentioned the changing administration. I mean, we know what this current administration has -- how that's influenced our P&L with regards to the value of gas spreads, things like

that. If the changing administration happens and you know their platform, you know the value of that kind of line of business should go up dramatically.

With regards to EV, look, we've already taken delivery of our first full EV truck. Obviously we're beta testing it. We expect that to meet all of our weight limits and route distance limits with regards to battery life. And so -- but the limiter there, while even though state regulations have passed, for instance in California, the limiter is still the manufacturing capacity. Right? And so many of the units you see people talk about are EV chassis, but not electric bodies. And the future should be a combination of both of those, so it is a full EV product. So all we can do is make sure we're beta testing and positioned to know how those fleets behave, make sure the rat models are proven, make sure the maintenance cost reductions are as promised, to make sure that the incremental cost of the unit is [headed] to payback or, more importantly, in markets can we put it in the rate base to make sure that we don't have stranded capital.

So, look, I think we're well positioned for all of the above. We tried to lay that out in our Sustainability Report. I think this industry is very well positioned with regards to the opportunities that lay ahead, if there's a change in administration, for instance, as you point out. And so, no, we feel quite good about how we're laying out our money, expected returns and, more importantly, what it does with regards to broadening sustainability initiatives.

Mary Anne Whitney: And, Chris, just to add one point to what Worthing said about the landfill gas, the biogas project, it's not as though we need to pivot or accelerate something. We're actually -- we have a number of projects on the drawing board, or in conversation about them. And so, to your point, if there's a more favorable environment it just means you probably move forward more quickly on things that we're already planning to do.

Worthing Jackman: A number of these conversations are already years old. I mean, this isn't something you just wake up and say, "Hey, let's do this." We've been at this for quite some time.

Chris Murray: Yes. No, that was actually my point. I was, like, it's kind of nice that everybody says, "Let's go green tomorrow," but it takes some time to get done. Right? And you worry about the technology and how resilient it is before you apply it. Anyway, thanks, guys.

Worthing Jackman: Well, look, we've just put I think probably one of the largest robotic orders in for our recycling facility. To your point, we didn't run in at Version 1.0. We waited for Version 2.0 or later to make sure the technology is proven and we can get the kind of -- the payback that we're looking for with that kind of deployment.

Chris Murray: Thanks.

Operator: And our next question comes from the line of Michael Hoffman with Stifel.

Michael Hoffman: Free cash flow, can we come back to that? You've given guidance of $805 million to $835 million for this year, $778 million now. The $805 million to $835 million if I recall correctly did not include the benefit of $40 million from the CARES Act. But did I understand your comment correctly, Mary Anne -- the $778 million has it in it, from a reported standpoint at the moment?

Mary Anne Whitney: Yes.

Michael Hoffman: Year to date.

Mary Anne Whitney: That's correct. That's correct, Michael.

Michael Hoffman: Okay. So but if you have intentions to still --

Worthing Jackman: [Indiscernible] --

Michael Hoffman: -- be inside your guidance or at the top end of it, so the expectation would be everybody should be prepared for the conversion rate in 4Q isn't going to be even 50%. It will be less because you've got a lot of cash outflow things planned for fourth quarter.

Mary Anne Whitney: That's a fair way to think about it, Michael, yes. That would be the math behind still achieving -- we said we're positioned to exceed the $805 million to $835 million. But, yes, so if you took the high end or just above that and use that conversion rate it would absolutely be below what we've demonstrated our ability to do this year, which says we are paying more outflows in Q4. Yes.

Worthing Jackman: Just apply a 52% -- the upper end of the 50 to 52% range to our year-to-date EBITDA plus our guided Q4 EBITDA and you'll get a number above the $835 million that was the prior upper end of our original range.

Michael Hoffman: Right. And you've always talked about, Worthing, are you even getting credit for exceeding that number this year, so prepay everything you can, pull forward capital spending. So to that end, what is your revised view of cash flow from ops and capital spending for 2020?

Worthing Jackman: Well, it really depends on what we can take delivery of. I mean, we've already put another $20 million of orders out there for fleet and Yellow Iron. We're trying to take advantage of some units that fit our specs that are still sitting on some lots out there. If we can get that in there, that will be kind of a good -- a nice head start to the outlays for 2021. Obviously, taxes go up in Q4. There's another cash tax payment due middle of December. The size of that's hard to determine, because obviously as if that Yellow Iron and fleet comes in, that will increase the bonus appreciation. Acquisitions, if they get done prior to that day, that increases the deductibility of acquired CapEx.

And so there are a lot of moving components in this thing. But what we know is that, to your point, we can manage where we want to come out at year end based on the flexibility that we have. It's a better conversation to have than asking, "Can you make your number?"

Michael Hoffman: Oh, no, I get that. I just -- you've given us a double-digit improvement year over year, [950]. If I just use 10% I'm at [865] as the starting number. But I'm also curious, like, why not prepay the CARES Act instead of just having this lingering around in the numbers for 2 years?

Worthing Jackman: We have a lot of flexibility to do a lot of things, Michael.

Michael Hoffman: Okay. You were very clear about telegraphing to the market in 2020 how to think about the cadence of price and volume trends. And I know you don't have the guidance out, but is there anything that should be noted about how to think about cadence for '21? For instance, 1Q is ugly in volume but 2Q's positive. So the first half kind of nets itself out and then the second half's positive. Is that the right way to think about it? And then price --

Mary Anne Whitney: Yes.

Michael Hoffman: Sorry. Go ahead.

Mary Anne Whitney: Sorry; I didn't mean to interrupt. I was going to say, yes, that's just the way I would characterize the volume side. And as you'll recall and kind of the tip of the year for us, pricing the cadence is that on a reported basis it always starts out high in Q1 and decreases over the course of the year, just really relating to the size of the denominator and the timing of our price increases, the majority of which are put in early in the year, mostly in Q1.

So the 3.5 to 4.0% that Worthing talked about for price next year, if you started at the high end there and worked your way down to the lower end, that might be a fair way to think about the cadence for next year. And to your point, volumes are negative in Q1, turn positive with the easiest comp in Q2, right? And then you see to the extent there's any reopening or improvement, more positive volumes in the back half of the year.

Michael Hoffman: Okay. And then, I'm less about the volume than I am sort of the total number of customers on the commercial side. Do I recollect correctly that in the Great Recession if you take the '08 through, say, '13 before the housing cycle recovered, that the lost number of customers was approaching 5%? And that happened over a very long time and you could absorb it very gradually. Are we looking at something like that, but just more compressed based on the level of recovered, if it stops here and, accordingly, you'll adjust the business model -- have to do it faster, but you'll adjust it like you did '08 to '13? You improved productivity dramatically. You got a lot more pricing, and so on and so forth?

Worthing Jackman: Well, the adjustment's already in place. And I think you see the strength of the flow through and the shape of the cost structure by just, even at the current levels, with 65% or so of the customers that have reached out and, what, 55 or more percent of the revenue, you see a 200 basis point margin improvement year over year. So I think the performance is already there to see. You're right that in the Great Recession it was about a 5% loss in revenue. We use revenue, not customer base, but revenue. And, again, you look at right now, you'll see the stats that we gave for this year. With the recovery that's plateaued right now but for some markets that are still expanding, that's the jumping off point for any further recovery within that customer base. But we've already kind of adjusted or adapted the shape of the business based on the realities that we currently have. We're not waiting to adjust the shape of this.

Michael Hoffman: All right. And that's what I was -- I probably teased that out poorly -- the point being is that anything that happens from this point forward is fine tuning. You don't have to take another big swing to account for it if that group never comes back.

Worthing Jackman: Well, because of the shape of the structure, the cost structure of the business has already been adjusted for it. That's why you see as revenue comes back such a high flow-through.

Michael Hoffman: Right. One of the correlations in the business has been good household formation has historically driven new business formation. So I get it's early, but in places where it's healthier, so maybe some of the secondary markets, places like that where they're longer in the cycle, are you seeing any empty storefronts starting to backfill? Is there -- because housing is very strong on a relative basis. We're at a 1.4 million, 1.45 million starts. That's a pretty healthy number.

Worthing Jackman: Yes. We've had what I would call the pandemic migration, so to speak, out of some more densely populated areas into some more rural -- kind of the 3-hour drive away from where you're currently living. As you've seen increased population settlements, or resettlements, in the near term, we have been seeing storefronts open. I mean, they're following the people. They're following the money. But it's a tough thing to say as a broad statement that business formation is going to follow household formation in general. Because right now most of the household formations are just people moving from

one home to another and deciding to re-enroll their kids in school or do it remote from a far away place. And, again, the economic activity has followed those people, is following and benefiting local businesses.

Michael Hoffman: Okay. But there's a little bit of hope there.

Worthing Jackman: Well, it depends on where you live.

Michael Hoffman: Yes. I suppose that's true. All right. Thanks very much.

Operator: And our next question comes from the line of Walter Spracklin with RBC Capital Markets.

Walter Spracklin: I'd like to start here with the contract. And we've gone through 7 months now since COVID started and you've negotiated a number of contracts, both in the commercial and residential side since then. And, Worthing, I was wondering if you could tell us a little bit about the key differences between a contract negotiated since then and what would have been negotiated before. And if you could touch on a little bit both in residential and commercial, is pricing discussions really altered in terms of getting them through, for whatever reason. Is the term changing at all versus what happened before? And then third, is the structure of the contract much different? I know you were making an effort to move residential over to a volume base versus per-household. Is there any other examples of real changes in the contract and its nature in recent contract negotiations versus what you would have done prior to COVID?

Worthing Jackman: Well, the approach to contract negotiations will reflect the period in which they're being negotiated. And those that are being negotiated right now obviously recognize that labor costs are going up. Despite record unemployment, as with essential workers and you've seen what we've done for our front line, that's rising labor costs. Obviously right now we're mindful of the shift that's occurred, already occurred, into higher loads within the residential. That's impacting those residential contracts.

Obviously, you've seen the increase in costs to handle more contaminated waste streams within the recycling side of the business. And so the cost of recycling has gone up and many of the contracts that are up for renegotiations were originally done back when China was still open and the costs and the profile and shape inside the business is fundamentally different. And so a long way of saying that many of the contracts that are getting renegotiated or discussed now, the cost structure is fundamentally different than where it might have been 7 or 10 years ago. The type of fleet that is being asked for today versus what was running under the current contract if you have to switch over a fleet makes it even more expensive. And so, no, the dialogue is dynamic. It's reflective of the times we're in right now. And you've seen in many cases easily double-digit increases in pricing because of those inputs.

Commercial right now, that dialogue hasn't changed. You see the strength of the price that we have right now and especially the spread to CPI. I'd say one of the biggest areas that we do well in is competing for accounts that have been poorly serviced. And we see those opportunities across multiple markets. And, again, that's a tip of the hat to all of our front line folks that show up every day and service their accounts and give us a good reputation in those markets and provide opportunities for our sales force to take advantage of that and gain share where possible.

Walter Spracklin: That's great color. For my second question here, just turning a little bit to trends. You've highlighted a number of things that are cause for optimism and I really hope that the reopening continues, recovery continues. But I'm seeing, obviously, with the new case counts in many jurisdictions, going up higher than they were when everything was shut down. Are you seeing any indications of policy change that would reverse some of those gains in certain jurisdictions that might, if they continue in others in the same type of trend, result in a backpedal here in terms of the reopening? Any risk of that in your view from what you are seeing right up until the kind of the date -- right up to the minute kind of

indications? And I know -- or is there things that are different? Schools, obviously, are opening now despite higher case count than when they closed. Is it just we've understood things a little bit better about how this all works, and we're taking a different approach than we did back in March?

Worthing Jackman: I'd say I would say we haven't seen it yet. In fact, October likely will play out a little better than we had originally expected. To your point, in other words, we haven't seen a rollover in that. But certainly the way we have guided the quarter, we have assumed that there may be some -- that it's prudent to stay cautious as we look ahead into November and December. We just haven't seen it yet in the numbers.

I'd say the biggest -- right now, it's more operational, as I think about what not worries me, but what we're mindful of, and that is, look, you hear it over the media about COVID fatigue or pandemic fatigue and our 18,000-plus employees need to stay vigilant and have -- in their operating procedures, in their attestations on a daily basis with regards to their health, with regards to showing up and working. Because, look, as you're seeing increases in positives throughout many markets, understand for every one person that might test positive, if they were at the office, meaning if they're at their operating location, that impacts other people through contact tracing. And in some markets where you see things [pop] high. Two or three people that might [pop] high might cause a quarantine of a number higher than that, which makes operations that much more challenging for our local folks.

And the best thing we can do is remain vigilant and remind our folks about operating procedures. Don't get COVID fatigue, don't get tired, don't relax your standards. Because I do think the next couple of months, 2 to 3 months, will be pretty widespread. And you've seen the numbers already pop. And so as long as we continue to do what we know how to do, our folks will be safe and attendance will still stay above 99%. But it's a constant reminder to our people to stay vigilant throughout this.

Walter Spracklin: Makes a lot of sense. Thanks very much for the color, Worthing, as always.

Operator: [Operator Instructions] Our next question comes from the line of Noah Kaye with Oppenheimer.

Noah Kaye: Thanks for taking all of the questions here today, so I'll just keep mine to one. And it follows right up on Walter's, which is obviously this risk of rising cases again and what that might mean in terms of slowdown in activity or potential lockdowns. And so the question is, you had very strong margin performance in 2Q. I think you commented at the time in some cases activity bounced back so quickly in certain markets that you didn't really have time to put in structural cost changes. If we do go into a second lockdown, what might you do differently, or how do you think you'll be better positioned to handle it?

Worthing Jackman: Well, look, the best way to prepare for any restrictions is to take care of your people. And we just announced a thank-you bonus, an appreciation bonus ahead of the holidays for our people. That's $800 for more than 90% of the front line. If you joined us more recently it may just be $400. But nonetheless, you lay that on top of supplemental wages that we've done through the year, emergency wages to keep people fully compensated even if they have to stay home for quarantine or child care or to take care of family members, et cetera, raising the minimum wage to $15 from a target standpoint to help those that may be below it to get up to that level. These are all things that you've got to do to position our people, to strengthen their mental fortitude for the challenges that lay ahead. And by getting ahead with a thank-you bonus ahead of the holidays, we felt that was another way to show support, to get people steeled, so to speak, for what's ahead.

And so, if you focus on your people and you strengthen their commitment, focus on their health, their welfare -- look, our people want to serve their communities. And to do that they need to be positioned to

stay healthy and to stay financially sound. And certainly that's the way we're looking at the challenge of the next 2 to 3 months. Stay ahead of it in your support; don't lag it.

Mary Anne Whitney: And, Noah, just to follow up, you made reference to the fact that the nice incrementals as those volumes came back and the commentary around not having structurally really changed the business. That's actually a good sign. What it meant is that there was such a small reduction in volume that there really wasn't the need or the opportunity, said another way, to do something like a reroute. So it's not as though it's an issue of not being prepared. The good news is most of the markets weren't that impacted. Clearly, not that we're looking for this, but in those more impacted markets, that's where you do make the changes and you actually make cuts. And so, clearly, if that were the scenario we would approach it the same way we have this time around.

Noah Kaye: Makes sense. Thank you both.

Operator: And, Mr. Jackman, there are no further questions at this time. I will turn the call back to you. Please continue with your presentation or closing remarks.

Worthing Jackman: Thank you, Jason. Again, if there are no further questions, on behalf of our entire management team, we appreciate you listening to and interest in the call today. Mary Anne and I are available today to answer any direct questions that we did not cover that we're able and allowed to answer under Reg FD, Reg G, our applicable securities laws in Canada. Thank you again. Look forward to speaking to you at upcoming virtual investor conferences, or on our next earnings call. Stay safe and healthy.

Operator: That does conclude the conference call for today. We thank you for your participation and ask that you please disconnect your line.