[WCN] - Waste Connections, Inc.,
Q2 2021 Earnings Conference Call
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Officers
Worthing Jackman, President, CEO
Mary Anne Whitney, EVP, CFO

Analysts
Walter Spracklin, RBC Capital Markets
Hamzah Mazari, Jefferies
Jeff Goldstein, Morgan Stanley
Jerry Revich, Goldman Sachs
Michael Hoffman, Stifel Nicolaus
Sean Eastman, KeyBanc
Tyler Brown, Raymond James
Noah Kaye, Oppenheimer
Michael Feniger, Bank of America

Presentation

Operator: Greetings, and welcome to the Waste Connections Second Quarter 2021 Earnings Conference Call. (Operator Instructions). Afterwards, we will conduct a question-and-answer session. (Operator Instructions). As a reminder, this conference is being recorded today, Thursday, August 5, 2021.

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

Worthing Jackman: Thank you, operator, and good morning. I'd like to welcome everyone to this conference call to discuss our second quarter 2021 results, an updated outlook for the full year and provide a detailed outlook for the third quarter.

I'm joined this morning by Mary Anne Whitney, our CFO.

As noted in our earnings release, broad-based strength driven across-the-board [deep] in the second quarter. Revenue and adjusted EBITDA in Q2 increased 17.5% and 23% respectively over the prior year period, primarily as a result of continued improvement in solid waste pricing volume growth and strength in recovered commodity values. These trends drove year-to-date adjusted EBITDA margin expansion of 110 basis points and adjusted free cash flow of over $585 million, up 18.5% year-over-year.

And given expected continuing momentum and margin expansion from these trends, position us to raise our full year outlook for revenue, adjusted EBITDA, adjusted

EBITDA margin and adjusted free cash flow.

2021 also has the potential to be another outsized year of acquisition activity. Year-to-date, we have signed or closed 14 acquisitions with total annualized revenue of approximately $115 million, including $75 million of franchise operations in California, Nevada and Oregon expected to close later this year.

We continue to see record amounts of seller interest driving elevated acquisition dialogue, and as communicated throughout the year, expect closings related to most of this activity to be more weighted to the second half of the year, which will provide further upside to our increased outlook for the year and strong rollover growth into 2022.

Before we get too much more into 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 U.S. 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 August 4th earnings release and in greater detail in Waste Connections' filings with the U.S. 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 measures. 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. In the second quarter, solid waste price plus volume growth of 11.4% exceeded our expectations by almost 150 basis points, primarily as a result of higher-than-expected volumes as the recovery trends that began in Q1 continued throughout the quarter, with landfill tons and roll-off pulls returning to levels about in line with or above pre-pandemic levels.

Total price of 4.9%, up 70 basis points sequentially, was above our outlook on higher core pricing of 4.7%, once again reflecting the strength of pricing retention we noted in Q1, plus about 20 basis points in fuel and material surcharges. Our Q2 pricing ranged from 2.6% in our mostly exclusive Western region to a range of about 4.5% to 7% in our more competitive regions.

Looking ahead, we are positioned for higher sequential pricing growth during the second half of the year as a result of incremental price increases we have already put in place to offset certain cost pressures.

Reported volume growth of 6.5% in Q2 reflected sequential improvement of approximately 1,000 basis points from Q1 and was led by those regions where markets were hardest hit during the pandemic including the Northeast U.S. and Canada. All regions showed sequential improvement from Q1 and all reported positive volumes in Q2.

Volumes range from about 4% in our Central region, where comparisons to the prior year were tougher as many markets were relatively less impacted by the Covid-19 pandemic, to almost 10.5% in Canada, one of our most impacted regions where the volume recovery had been remarkably strong, arguably outpacing the reopening activity particularly when considering that many restrictions in Canada extended through Q2 of this year.

Also noteworthy is our Western region, where volumes led our other regions going into the pandemic and continue to be the strongest in the U.S. at about 8.5% in Q2.

Looking at year-over-year results in the second quarter on a same-store basis, all lines of business increased by double-digits. Commercial collection revenue was up 16% year-over-year. Roll-off pulls increased by over 11% year-over-year, led by Canada, up almost 20% and back to above pre-Covid-19 levels. In the U.S., pulls were up about 10%, and all regions showed year-over-year improvement, most notably in our more impacted markets, including in the Northeast.

Landfill tons were up 17% year-over-year on MSW tons up 11%, C&D tons up 20% and special waste tons up 33%. As a result, landfill tons have returned to above pre-pandemic levels in all of our regions, except the Eastern region, which was slightly below prior levels as a result of the delayed reopening activity in markets in the Northeast.

Looking more closely at results, as noted, all waste types were up double-digit percentages year-over-year. However, the outsized amount of special waste activity was particularly noteworthy as Q2 activity propelled tons back to 13% above pre-pandemic levels with all regions up year-over-year, perhaps due to a little pull-forward from Q3.

Looking at Q2 revenues from recovery commodities, that is recycled commodities, landfill gas and renewable energy credits, or RINs, excluding acquisitions, collectively, they were up about 95% year-over-year, resulting in a combined margin tailwind of about 130 basis points, 90 basis points of which was from recycling and 40 basis points from landfill gas and RINs.

Recycling revenue increases were driven by both higher commodity values, including old corrugated containers or OCC, up 25%, and plastics and metals, both up over 100%. Higher volumes also contributed year-over-year, again reflecting the pandemic impact.

Prices for OCC averaged about $135 per ton in Q2 and our RIN pricing averaged about $2.72.

And finally, on to E&P waste activity, we reported $31.2 million of E&P waste revenue in the second quarter, up 26% sequentially from Q1, reflecting increased activity across multiple basins.

Looking at acquisition activity, as noted earlier, we've already signed or closed 14 acquisitions with annualized revenue of approximately $115 million, approaching what we would consider an average amount of activity for the full year. These transactions include multiple West Coast franchise markets, which are core to our strategy and provide unique opportunities to expand our exclusive contract portfolio.

Moreover, our pipeline still reflects record levels of seller interest driving the potential for outsized activity in 2021, primarily given tax-related considerations. That said, we continue to be selective and disciplined in our approach to acquisitions as we recognize the importance of value creation for our shareholders as well as market selection and asset positioning.

Now I'd like to pass the call to Mary Anne to review more in depth the financial highlights of the second quarter and our increased outlook for the year and to provide a detailed outlook for Q3. I will then wrap up before heading into Q&A.

Mary Anne Whitney: Thank you, Worthing. In the second quarter, revenue was $1.534 billion, about $44 million above our outlook due primarily to higher-than-expected solid waste growth and recovered commodity values. Revenue on a reported basis was up $228 million or 17.5% year-over-year, including acquisitions completed since the year-ago period which contributed about $47.6 million of revenue in the quarter or about $44.1 million net of divestitures.

Adjusted EBITDA for Q2 as reconciled in our earnings release was $484.9 million, about $17 million and 20 basis points above our outlook at 31.6% of revenue, up 140 basis points year-over-year.

Commodity-driven impacts account for about 100 basis points of margin expansion, net of a 30-basis point impact from higher fuel on diesel rates up almost 20% year-over-year. Ex- fuel, solid waste collection transfer and disposal margins expanded by 50 basis points, as we more than offset a 60-basis point increase in incentive compensation costs, 50 basis points from higher medical and 50 basis points from increased discretionary expenses.

And finally, acquisitions completed since the year-ago period accounted for about 10 basis points of margin dilution.

Regarding discretionary expenses, we've begun the process of returning to a more normalized operating environment, including in-person training, meetings and other activities we consider integral to sustaining our culture and expanding our bench strength ahead of future growth. Given the challenging labor environment, we have also proactively implemented supplemental wage adjustments in many markets as we anticipate or combat labor constraints. These purposeful wage and discretionary cost additions, along with higher incentives, medical and other costs resulting from more typical activity levels, largely replaced last year's Covid-19-related frontline support costs, the majority of which did not repeat this year.

As noted earlier, we've already implemented incremental price increases to address these higher costs, resulting in full year 2021 price of approximately 5%, up from 4% in our original outlook.

We delivered adjusted free cash flow up 18.5% year-over-year through Q2 at $585 million or 20% of revenue, putting us on track to achieve our revised adjusted free cash flow outlook of approximately $1 billion.

I will now review our outlook for the third quarter 2021 and our updated outlook for the full year. Before I do, we'd like to remind everyone once again that actual results may vary significantly based on risks 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, including as a result of or related to impacts from the Covid-19 pandemic or the Delta variant of the coronavirus. 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.

Looking first at Q3, revenue in Q3 is estimated to be approximately $1.56 billion. We expect solid waste price plus volume growth of about 7% in Q3 with pricing of about 5%. Recovered commodity values and E&P waste revenue are expected to remain in line with current levels, with RINs generally in line with Q2 levels and OCC trending slightly higher.

Adjusted EBITDA in Q3 is estimated to be approximately $495 million or 31.7% of revenue, up 60 basis points year-over-year and up sequentially from Q2.

Depreciation and amortization expense for the third quarter is estimated to be about 13.3% of revenue, including amortization of intangibles of about $33.8 million or a rounded $0.10 per diluted share net of taxes.

Interest expense, net of interest income, is estimated at approximately $40 million. And finally, our effective tax rate in Q3 is estimated to be about 21.5%, subject to some variability.

Turning now to our updated outlook for the full year as provided and reconciled in our earnings release, revenue for 2021 is now estimated to be approximately $5.975 billion or $175 million above our initial outlook, with the primary drivers being an additional 150 basis points of solid waste price plus volume growth and higher recovered commodity values as compared to our initial outlook, plus $25 million from acquisitions completed year-to-date.

Adjusted EBITDA for the full year is now estimated to be approximately $1.875 billion or about 31.4% of revenue and up about $75 million over our initial outlook. Moreover, full year adjusted EBITDA margin guidance is 40 basis points above our initial outlook, up 90 basis points year-over-year.

At 31.4%, our adjusted EBITDA margin outlook reflects continued year-over-year margin expansion in the second half of 2021 in spite of wage and inflationary pressures and tougher year-over-year comparisons.

Adjusted free cash flow in 2021 is now expected to be approximately $1 billion or over 53% of EBITDA and up $[15] million from our initial outlook despite CapEx up $50 million from our original outlook.

Last week, we closed our new $2.5 billion credit facility, which increased borrowing capacity by almost $300 million, reduced borrowing spreads and enhanced flexibility for continued growth. Our balance sheet strength, together with this increased capacity, positions us for potential above-average acquisition activity and an increasing return of capital to shareholders. We have already returned over $400 million to shareholders in 2021 through share repurchases and dividends. And we are in the process of renewing our normal course issuer bid, authorizing the repurchase of up to 5% of our outstanding shares per annum.

We will continue to approach share repurchases opportunistically and anticipate announcing another double-digit percentage per share increase in our cash dividend in October. 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, broad-based strength continues to drive results ahead of expectations as we benefit from reopening activity in a supportive macro environment, including tailwinds from recovered commodity values. We've once again demonstrated the importance of being selective about markets and intentional about driving results. Quality of revenue and comparative price retention across markets matter.

We're extremely pleased to be in a position to raise our outlook for the full year. We are set up for continuing margin expansion through the second half of 2021 as proactive unbudgeted price increases offset wage and inflationary pressures. We are on track for adjusted free cash flow of approximately $1 billion and adjusted EBITDA margins back above pre-Covid-19 levels.

Finally, we expect to announce another double-digit percentage increase in our regular quarterly cash dividend in October, and remain well positioned for potential significant

increase in acquisition outlays to drive further growth in 2021 and beyond.

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

Questions and Answers

Operator: Thank you. (Operator Instructions). Walter Spracklin with RBC Capital Markets.

Walter Spracklin: So I'd like to zero in on your M&A pipeline. And my question is what is the main driver of your pace of acquisitions? Obviously, it's not financial leverage, but is it just the availability of sellers? Is it valuations on offer prices, or is it your own kind of acquisition processing and integration capacity? Because the reason I'm asking is that the sector is clearly consolidating rapidly here and good companies are being gobbled up by you and your competitors.

And I'm just curious as to whether now is the time to kind of stretch your acquisition activity even more than you've already done, and perhaps add leverage or turn of leverage there to achieve a more rapid pace, given how fast and how rapidly good companies are being acquired in your sector right now.

Worthing Jackman: Walter, that's a great question. Look, we've always said that sellers determine the timing when good businesses are sold, right? These are family-driven issues, tax-driven issues, lineage transition issues, etc. And we've always wanted to maintain the flexibility to be there to write the checks when they make the decision to sell. And that's why you've seen us keep a lot of dry powder on our balance sheet, not that we'll spend all this. But we could theoretically write a $3 billion check right now and still stay around 3x leverage.

And I say that because this year, you are seeing a lot of folks come to the table. In the U.S., a lot of that is driven by potential tax changes, increase the capital gains rates. When the administration says something like, well, we might go to 40% on cap gains, and you recognize in a state like California, that would mean cap gains would be taxed at over 57%. These are 3, 4-generation old companies that all of a sudden have to give most of the proceeds to the government after all their 100 years of work. And so these are real considerations for people in the U.S.

And so we've seen a lot of tax-driven conversations; we have seen some lineage transition-driven conversations. We've got people who are -- some sellers who were just exhausted having gone through a pandemic, having gone through the struggles around labor, increased investment requirements in the business to keep up with regulations and changes looking ahead. The businesses are back above pre-pandemic levels, and so they know it's a good time to come to the market. So there's a variety of things that drive

sellers. But again, in our model, sellers determine when the timing is right for them.

Walter Spracklin: Okay. I appreciate that color, Worthing. My follow-up question is on landfill gas energy opportunities. A lot of your competitors now are starting to talk about that opportunity. Could you give us a little bit of a flavor for how many facilities do you see as poised to or potentially participating in that trend? And even if you have some numbers around that in terms of revenue and cash flow opportunity, that would be helpful as well.

Worthing Jackman: Sure. And we've been consistent about this conversation. Obviously, we've said a lot more about it in our sustainability report that we published a year ago. And frankly, we're pivoting from a position of knowledge because we've got the largest plant right now in North America with regards to this. And look, we've said all along that we've got 3 to 5 opportunities for high-BTU plants within our current network we've been working on for many years; 2 are further along in the process than others. We expect to commence construction next year on 2 plants that we've already approved.

Understand that lead time for some of these plants, once you say go, can still be at least 18 months for some critical components. Again, you think about some of the delays on the manufacturing side, it affects construction and timetables for these plants as well. And so we've been consistent to say at the earliest, we would expect the contribution from these to start in 2023 and hit their full stride sometime second half of that year into 2024.

The numbers around it are simple. We are between the couple of plants that we're looking at right now, and a couple of recycling plants as well that we're looking to build. That kind of investment could be anywhere between $100 million to $125 million collectively. And you look at that and that means the revenue opportunity at that is probably close to 75% or 80% of that. And EBITDA flow-through is probably close to 70% of that revenue.

And so as you can see in today's environment especially, the payback can be a lot quicker than that, when you see EBITDA could be higher than that. But we've always said payback can be in that 3-year plus or minus range with regards to these kind of investments. Again today, it's quicker than that.

Walter Spracklin: Appreciate the time, Worthing, and congrats on a good quarter.

Operator: Thank you. Hamzah Mazari with Jefferies.

Hamzah Mazari: I guess my first question is maybe you could help talk about just the interplay between pricing and inflation. And what we mean by that is, how much of the price increase is sort of playing catch-up to inflation versus sort of flowing to the bottom line? Maybe help us think about that. And as you answer that, maybe you can layer in your incremental margin assumption as sort of demand improves further.

Mary Anne Whitney: Sure, and good morning, Hamzah. Thanks for the question. So first of all, with respect to pricing, as we described, we've already implemented price increases

that are leading to the higher reported pricing in the back half of the year, which is, of course, an anomaly, right? We would typically report our highest price earlier in the year. And just on a reported basis, it would step down over the course of the year just mathematically.

So that tells you we already had strong pricing retention in Q2, and the pricing is increasing in Q3 and Q4. And as we further describe, that is offsetting is covering the incremental wage pressure, in some cases where we did market adjustments proactively, in other cases where we've seen those labor constraints. And so we feel we have that covered with these incremental price increases. And so that's one aspect of it.

I'd say more broadly, when we think about the incrementals, we talked about the 40%-plus as volumes return. I think that's the same way to think about it. Of course, being mindful of the fact that what's come back most quickly are landfill tons, which would have higher incrementals than what's really left if we think about what pieces aren't back in. We said on the call that landfill tons and roll-off pulls are really back to pre-pandemic levels. So that tells you that last point, point and a half of volume, which isn't in our numbers yet, is more commercial, and so could have slightly lower incrementals, but still the right way to think about it.

Hamzah Mazari: Great, very helpful. And just on M&A, do you -- I know you sort of outlined what you have in the second half. Maybe just if you could update us on whether you think the pipeline can come in a lot higher than that. And just as it relates to M&A, how quickly does M&A become accretive for you? And is it faster now because you have higher scale than it was historically for you?

Worthing Jackman: Well, first, the second point. M&A comes in accretive to free cash flow day one. Now margin profile is different because to the extent, as you know, Hamzah, we're already running 31%-plus in EBITDA margins, and we're buying a collection operation. A good collection operation might be in the mid-to-high 20s with regards to margin. And we'll improve that a little bit. But what gets us to the 31% or higher is our integrated network of landfills and some other higher-margin things we do.

And so it's always -- it pulls a little bit on margins. You saw in this quarter, acquisitions were about 10 basis points dilutive to the overall. But because the base business is getting so much bigger, the dilutive impact of acquisitions, the collection-only just is getting lesser and lesser. But obviously, on a free cash flow basis, it's accretive as it comes in.

With regards to the environment, look, as we think of the setup for acquisitions, we signed or closed $115 million of revenue so far. That already provides about 1.5% rollover growth into next year. If we simply double that in the balance of the year, we're going into next year with 3% from acquisitions. Obviously, if we do more of that, that increases that 3%. But that 3%-plus, right now running at around 7% price plus volume growth, puts double-digit revenue growth going into next year, not out of the question. Obviously, more things get done next year, provide further growth from that.

And so M&A activity this year will increase. We will do more than the $115 million. But

with double-digit revenue growth already in hand as we kind of enter the year at a minimum, that plus-margin expansion drives great flow-through, as you know, to earnings growth, and more importantly, free cash flow per share growth.

Hamzah Mazari: That's very helpful. Just last question, I'll turn it over. On your Q3 volume estimate of 2%, just frame for us how conservative that is. Are you assuming education, sports all comes back? I don't know how much exposure you have there. And is the special waste a good indicator of what's to come on volumes? Thank you.

Mary Anne Whitney: Sure. So with respect to Q3, where we guided 7% price plus volume we said about 5% is price and therefore 2% is volumes. We haven't assumed continued reopening activity, Hamzah. So basically, it says that at a point in time, based on kind of where we were in Q2, how do we think about the rest of the year. And so to the extent there's any improvement, particularly in those most impacted markets, as we described, the Northeast, for instance, which hadn't come back yet or to a much lesser degree, that would be incremental. That would be upside to what we communicated.

And to that point, similarly, on recycled commodities, E&P activity, RINs, to the extent there's continued improvement in any of those, that would also be upside to what we've guided.

And to your question regarding special waste, just to close on that, the observation there was just how strong it was in Q2 and a reminder how lumpy special waste can be. And the observation is you don't know that that level, that pace would continue. It might have been some pull-forward from Q3. And so we'll watch during the quarter to see where that plays out.

Hamzah Mazari: Got it. Thank you so much.

Operator: Jeff Goldstein with Morgan Stanley.

Jeff Goldstein: I just want to follow up a little bit on that last question around volumes and just trying to parse that out a little bit more. Just looking at the quarter, your 6.5% increase, you're still about 300 basis points below 2Q 2019 levels. And I know you've kind of mentioned a lot of positives around things like C&D and special waste. But maybe you could just add a little bit more about what you think is lagging and really what is the source of upside if we are going to reach pre-pandemic levels by the end of the year and if you think that's feasible.

Mary Anne Whitney: Sure. And to frame it, the way we think about it, when we finished 2020, we said at that point, there's really about 3% that's not back in these numbers, negative 3% volume. And what we've observed already in the first half of the year that that volume recovery had outpaced our expectations by about 100 basis points, a little more than that. So from our purview, there's probably 1.5 points in volume which isn't back in the numbers yet as compared to pre-pandemic levels.

And to the observation about the fact that tons are essentially back, pulls are essentially back, it tells you that it's really the commercial piece, which is lagging, which, of course,

would take longer to get back. Those tons and pulls are good real-time indicators of activity.

And so to your question, that's where we see the remaining piece, and we certainly see that if we look at that 1.5%, there's a large portion of it which is concentrated in the Northeast of the U.S., particularly in New York City and in Canada, both of which were more impacted by the pandemic and slower to reopen. And so we look forward to seeing that and again, it's not in with the way we've guided the rest of the year.

Jeff Goldstein: Okay, understood. That was all very helpful. And then with the recycling industry being so strong right now, I'm curious if you're doing anything different to take advantage of it, meaning are there any investments to call out, or any other initiatives you're taking to really capitalize on the high commodity prices right now and just the growing appetite for recycling in general really?

Worthing Jackman: Well, I think the overall approach probably is not too dissimilar from the way other folks look at this, which is we've shifted over time to more of a domestic customer with regards to moving the commodities. We've looked at putting contracts in place to try to consolidate our sales effort to make sure we have the offtake there. We've invested in more optical sorting and robotics within the facility to improve the quality of the material that's being sent to those customers, which drives higher price points per ton as well.

Obviously, to the extent we can continue to take labor out of that, it reduces our reliance and dependence on headcount going forward. And we've taken that all into account as we've designed these 2 new facilities we're building to try to do what I think us and others recall there is (inaudible) the future, which puts all that together and puts us in a position to again take labor out, improve the quality of the material, improve the overall revenue profile of the facility.

And as you know, the synergy has already derisked that business somewhat by moving to a tip fee structure for third parties that come in the facilities to make sure were more than covering our OpEx and CapEx and returns from the tip fees and then letting some of the commodity values be gravy on top of that.

And so I think the whole industry has migrated over the past 3 or 4 years into this opportunity. Obviously, the increased commodity values and the strong economy backdrop driving some of that has helped make that look even better.

Jeff Goldstein: All right. Thanks a lot.

Operator: Jerry Revich with Goldman Sachs.

Jerry Revich: Worthing, so last quarter, we spoke about 4 to 5 potential landfill gas pipeline development opportunities. And earlier on the call, you mentioned what the economics look like for those types of investments. I'm wondering if you were to say, okay, today, when prices are sustainable, is there a next layer of projects that you folks would consider if you got confidence in when prices staying around current levels, what

could that next wave of opportunities look like? Is it a handful of plants? Is it more than that? Can you just help us understand what the pipeline looks like behind these top 4 or 5 plants that you're looking at in this [way]?

Worthing Jackman: Sure. Well, (inaudible) our confidence isn't just because RIN prices are where they are right now. We look at these over a long period of time and assume that prices can fall; and understand that if it's a 2-or-3-year payback and if it gets cut in half, and that could stretch to a 4-or-6-year payback, that's still a very attractive incremental investment. We have so much already preexisting investment in the landfills that it just -- it sounds so attractive. But remember, there's a lot of other capital that's been invested that people aren't accounting for and would look at this incremental investment just for the BTU plant.

Look, I understand while we talk about both the 3 to 5 or so and the timetables and that stuff, and what we're doing, the fact that we've got RFPs out for construction, that we put deposits down for equipment and stuff, we're always looking at the portfolio, right? There are existing contracts in place where we just have gas offtake based on the older model of project developers coming in and putting electric plants at the facility. As those contracts are winding down, that gives us opportunities to renegotiate those contracts as more of our landfills mature. Obviously, that's increase in the gas production and it brings sites over time that don't have enough production now into the fold as you look ahead 5 or 7 years.

And so the portfolio will continue to expand and obviously, we've kind of laid that out in our ESG report. But the near-term actionable, as we think about the next 2 to 3 years are what we're just talking about right now.

Jerry Revich: Okay, terrific. And then on the pricing conversation, nice to see the pricing outlook improving. So given the comps are easier in the back half of the year, I'm wondering if you could just help us understand how much are you folks planning to raise pricing in the back half of the year versus the first half of this year compared to normal seasonality?

Worthing Jackman: Yes, well, as Mary Anne pointed out, we've already put in the supplemental price increases during the second quarter, which have all hit the builds. And so the actions that need to be taken for the second half have already been taken and so we know those numbers. And as we guided, overall reported price will be about 5%, meaning probably come in a little higher than that as you look at Q3 and into Q4. But also importantly is it gives us a higher entry point rollover into next year.

And so with this pricing environment will sustain itself if inflation abates and some of the cost pressures that we see in the system or on CapEx abate, then maybe -- if pricing doesn't need to stay at 5%, but in this environment, as you know, we look to cover our cost and then some. And it's not just P&L; you've got to recall that you're seeing escalations especially related to steel, steel surcharges on fleet [painters]. You're seeing inflationary pressures on the manufacturing side as well on the construction side of landfills. Plastics are up, so liner costs are up. It's everywhere in the system and so we

feel right now that 5% is the appropriate amount of pricing needed to cover it.

Jerry Revich: Got it. I appreciate the discussion. Thanks.

Operator: Michael Hoffman with Stifel.

Michael Hoffman: Mary, I want to tease out, if I can, just a little bit on the 1.5 that's left in commercial. Could you frame for us your New York City-specific business, how it looks sunny, say, compared to 2019? What's left to come back there? Because that's a big driver of this, I believe.

Mary Anne Whitney: Sure. As I said, if I look at that remaining piece, about half of it I could put in the buckets of the Northeast and Canada. And within that, there's as much as $30 million in New York City still to come back.

Worthing Jackman: As you know, Michael, with most of the return to office, folks looking at post-Labor Day, that's why to Mary Anne's point earlier, we don't assume any sort of recovery of that, let that be upside. And my assumption is that could be more of a Q4 event than Q3.

Michael Hoffman: Yes, because like our shop is talking about back office September 7, so the quarter's over, right?

Worthing Jackman: And we'll see what the Delta variant does to those expectations and so it's why we [left] that to the upside.

Michael Hoffman: Right. And just to emphasize that, price is baked at this point, volume could have an upside depending on what happens with what you just referred to, but -- .

Mary Anne Whitney: That's the right way to think about it, yes.

Michael Hoffman: On the M&A piece, to your comment about [when] more gets closed, is it mostly tuck-insurance, or do you have some new market opportunities like you did in, say, Rhode Island and Tucson or Southern Virginia a couple of years ago? And then that creates an incremental compounder going forward as you consolidate them?

Worthing Jackman: Yes, as you know, for us to be doing a typical year, that means were doing 2 to 4 new market entries of between $20 million and $40 million in revenue, and we're doing 15 or 16 or so tuck-ins, again, the compounders I talked about within our network. So for us to bat above the average, it means you're right, we are looking at many new markets, which then provide additional platforms to continue the strategy.

Michael Hoffman: Okay. So that adds even a greater sort of lengthening of the compounding on the M&A is the point of that.

Worthing Jackman: Absolutely.

Michael Hoffman: And then how do you frame your wage inflation versus your coming

into the year and where we are? And then how do you think about that trend into 2022?

Worthing Jackman: Sure. Look, just like we saw kind of the last what I'll call labor pinch in kind of late 2018, early 2019, we saw wage escalations average upwards of 5% to 5.2% in certain periods back then. While we had expectations going into the year at 3% to 3.5% for wage escalations, I'm not surprised that as we got into Q2, we find ourselves running 5%, 5.5% because we made the decision, the recognition of everything that the field has gone through over the past 15 months or so. And in light of the current environment to be proactive and get in front of wage escalations, so we put a couple of hundred more basis points into the system during Q2 and I think our folks deserve it.

And so knowing that, as we always do, we looked at our P&L and make sure we want to recover it. Look, 5% price increases, probably half or less of what you're hearing from consumer product companies and other customer-facing industries that are -- have embedded cost inflation that they're trying to recover. The good news is this industry is set up to recover it. And so when our folks deserve it, we need to go out and recover it.

I would think that wage inflation may abate next year, if you think you play through the pandemic and the impact of that and folks kind of coming back into the work environment. But I've always questioned [Jay Paul], and used the word "transitory." So I'd hate to tie the word "transitory" to wage inflation, too. So we'll see what happens next year and obviously, we'll be responsive and cover whatever is needed.

Michael Hoffman: Okay. And then historically, on your landfill gas side, you have partnered. Am I hearing sort of implicitly you're not on these 3 to 5, that you're going to do them all yourself or is there still a partnering? And tied to that, is there a way to try and hedge some of the exposure on the RINs so we take some of the volatility out, but you enjoy the returns economic still?

Worthing Jackman: Look, we're open-minded to partnering. Remember, in a lot of these instances, it's not just the plant you're looking at, it's also the marketing agreement with regards to monetizing the gas. There could be a pipeline involved with it as well. And so there are various parties that are around the table when you're developing these sorts of projects and we evaluate all alternatives, having one or two of those partner with us or us taking it all on. And so we don't have any restrictions or access to capital limitations that don't allow us to do it all.

But we want to be mindful looking long term, how do you tie everyone's accountability to the success of the project together? And yes, you're right, we can hedge and derisk these sorts of revenue streams as we look ahead. And just like right now, we've got a portion of our RINs hedged. We may look at the same thing as with regards to these [plans] as well.

Michael Hoffman: Okay. And then on the incremental $50 million in capital spending, what's going to be the focus of that spend?

Worthing Jackman: Yes, you've seen us really opportunistically and fortunately, I think, have a big increase in the number of units fleet that we've been able to acquire this year.

We've also been able to buy some parcels of land around certain locations to increase our footprint for the long haul. But we've taken CapEx up where others talked about, well, if they can't spend it, we'll spend it. Some of this will give us a nice prepositioning of 2022 and a pull-forward of 2022 capital in this year. And so as we look ahead, it doesn't put pressure year-over-year on CapEx outlays next year because a lot of what we're doing this year.

Michael Hoffman: Got it. And the last two for me are where are the two new [MURFs] going and what's the 10% swing in recycling commodity book equal today?

Worthing Jackman: Well, the two new [MURFs] are going in the U.S., if that is the question.

Michael Hoffman: (Laughter).

Worthing Jackman: And obviously, we've purchased recently another recycle facility in Montreal last year and so we've expanded our footprint in Canada too. But the greenfield ones are in the U.S.

And Mary Anne, for the 10% question?

Mary Anne Whitney: And the 10% around $125 million, that would suggest about $12 million would be a 10% swing in commodity values.

Michael Hoffman: Okay. Thank you so much.

Operator: Thank you. Sean Eastman with KeyBanc.

Sean Eastman: Nice quarter. A lot of companies are talking about sort of having to turn down growth opportunities because of labor availability. Where are you guys at there? Can you stay on the offensive on growth or how would you characterize that?

Worthing Jackman: Look, I don't think you necessarily will notice the impact in the numbers. But without a doubt, there are markets where we are short drivers. Being short labor is, I think, a statement that most industries are talking about right now. And so with regards to some incremental roll-off activity that could have gotten done in the period versus it might slip into another period, absolutely, there's a little bit of that going on. But all in all, you won't really see it in the numbers because it is such a small amount.

Sean Eastman: Okay, fair enough. And you mentioned part of the $115 million in deals that are signed or closed represent West Coast franchise acquisitions. Could you just remind us what the significance of that is? And as we look at the near-term pipeline, is a big part of that also West Coast franchises?

Worthing Jackman: Yes, the remaining pipeline is really coast-to-coast, so the West Coast, we still have opportunities on the West Coast but it's not particularly concentrated on the West Coast, which is what I'm trying to say. I think the unique thing about the West Coast to recall is the need for local consents. These franchises require [novation]

actions by local municipalities that adds incremental time to the process. So while we may have already gotten through HSR, we're still running the traps on getting those consents. And that can add in some cases, 2 to 4 months to the timeline to get things across the finish line. So that's the one thing that is unique about the West Coast and the need to move more quickly and to start that timeline with regards to local consents.

Sean Eastman: Okay. Thanks a lot, Worthing. I'll turn it over.

Operator: Thank you. Tyler Brown with Raymond James.

Tyler Brown: Mary Anne, so thanks so much for breaking down the $175 million, I think, in incremental revenue to the guide. I may have missed it, but big picture, how does the $75 million of incremental EBITDA break down between price and volume, commodities and M&A?

Mary Anne Whitney: Sure. So the breakdown would be the incremental solid waste, the way to think about margins is around 40%. Of course, the $25 million in acquisition contribution would be lower than that, around 25%. And those commodities ex-fuel would work out to be about 50% contribution.

Tyler Brown: Okay. Okay. That's very helpful. And then you called out incentive comp -- or sorry -- I don't recall you calling out incentive comp last quarter. You called it out this quarter. Is it safe to assume that you guys are over-accruing or doing some catch-up accruals this quarter? And then is incentive comp a sizable margin headwind in the back half? It feels like maybe it is.

Worthing Jackman: I'll answer the first thing. You've got to recall we didn't call it out last quarter because the comparison was really to a lesser pandemic impact to the quarter in the prior year.

Tyler Brown: Right, right.

Worthing Jackman: We called it out really -- frankly, we would have called it out, but every other company that reported ahead of us gave you some insight into it, so we wanted to be consistent and give you that insight as well. Obviously, the weight of that in the second half is not as big.

Tyler Brown: Okay. Okay. That's helpful. And then on the 5% pricing, and this is just more for modeling purposes -- but how much of that is just fuel?

Mary Anne Whitney: So core pricing, it's primarily core pricing. In our model, there's a small amount. You saw that 20 basis points of fuel surcharges in Q2, probably the right way to think about it as we move through the back part of the year. So that tells you that core is approaching 4%, 5% on its own.

Tyler Brown: Okay. Okay. That's helpful. And then -- yes, sorry, sorry. But and I know its early, but as you think about next year, obviously, we have some pretty good CPI [prints]. But is it safe to assume that it may be pricing a better placeholder is still maybe

in the 4, the low-4 type range? And I guess it doesn't even really matter. The key is this is all really a spread game, if you want to call it that. It's really looking to be at a positive spread over unit cost, and it's really going to depend on where unit costs come in.

Worthing Jackman: Yes, I think if you look at pricing next year, you've got 2 components. We already talked about entering the year at a higher entry point, given the more recent price increases we've put in place. And so the rollover impact of that, plus you'll have a step-up in our exclusive markets of 50 to 100 basis points year-over-year versus what we're getting this year; again, that lagging impact of price in those marketplaces. That would mean 4.5% to 5% is in sight for next year and again, we're pretty well positioned with again the entry point being higher and exclusive contributing more.

Tyler Brown: Okay. That sounds good. And then on the E&P side, and I know revenue was up slightly sequentially, and it sounds like you're baselining the current rate forward. But do you think that some of the E&Ps hedges kind of roll off that you're going to see activity maybe pick up there? Are you just hearing any chatter in the market on drilling activity?

Mary Anne Whitney: We've had some indications that drillers are coming back or that there will be a pickup. As you know, we'd always rather wait to see it before we guide to it, but we're encouraged by some of those dynamics we hear out there.

Worthing Jackman: Yes, we think 2022 is a better year than 2021.

Tyler Brown: Yes, okay. All right. Thank you. Appreciate it.

Operator: Thank you. Noah Kaye with Oppenheimer.

Noah Kaye: Maybe I can just pick up on Tyler's question actually around E&P. I think just to get into this a little bit, it looks like the live DUC count is at a 2013 level, right? There's been just so many more wells completed than drilled over the past year. I think in some of the basins that you're in, it's particularly stark. So it seems logical, like drilling activity has to pick back up. If you're hearing 2022, more likely for that recovery makes sense. But I guess do you see anything structurally getting -- keeping this from getting back to like a $50 million a quarter type business?

And the second question is how do you think about incremental margins at this point?

Worthing Jackman: Sure. I think you helped put more meat on the bone with regards to our expectation of why 2022 is a better year than 2021 because you're right, and obviously, there's more waste generated from the drilling activities than just the completion activity. And so that would be a key driver to getting us back to $50 million a quarter. It would be nice to get back to that. Again, we continue to see sequential improvement as we move through that business.

And as you know, the incrementals in this market -- in that business, because it's a landfill-based business, are in the 70% to 80% range. And so as we kind of continue to

see the kind of sequential quarterly increase, we'll click back to 50% or better margins at a lower revenue rate than we needed in the prior upside or upturn. And so this business will easily cross 50% if we are approaching $200 million on an annualized basis.

Mary Anne Whitney: And Noah, to that point, we're encouraged by the fact that in Q2 already, at $31 million in revenue, E&P was no longer a drag in the sense that the margins there were in line or slightly above the corporate average.

Noah Kaye: Okay, excellent. And then just I think one of the things that's happened over the past year is some companies had to kind of slow the role of technology implementation in computers and the like, just given everything else going on. But it's obviously strategically important for you to keep doing so and helps you target some of the higher-risk markets. So can you just sort of update us on where some of the key technology implementation efforts are?

Worthing Jackman: Sure, and you're right in saying that we wish it was faster. But like you hear in many other industries, chip delays have slowed down our ability to roll out as fast as we like. And so look, we'll be back on schedule before the end of the year on that. And again, as we talk about the new generation in (inaudible) technologies, there's a lot of benefits that we get from that and so I think we're pleased where we stand on that.

We've already rolled out our latest and greatest updated tablet programs and so that tablet rollout is also continuing as we move through this year. But clearly, the one delay we saw was most pronounced in the camera side just based on some chip delays.

Noah Kaye: All right. Thank you very much and nice job. Appreciate it.

Operator: Thank you. (Operator Instructions). Michael Feniger with Bank of America.

Michael Feniger: I know the last time you guys were this [technical difficulty] implementations, we're talking about the late 2018 period when I think unemployment rate was at a record low, recycling was challenged. I think when you look back, your margins were actually flattish there. So this is a comparable time period you're saying with wage pressure and labor; yet your margins expand this quarter and you guys are showing confidence in the second half.

So what are some of the differences? We keep talking about that was the last time we saw this had the labor pressure, yet you're having this type of success on the margin. Is there anything we could kind of glean from that comparing it to that last period?

Worthing Jackman: Sure. And what particular period are you looking at? Because we'll give you the exact answer.

Michael Feniger: I think it was -- if I'm not mistaken, I think it was in 2018 you guys were talking about the type of cost crunch that you guys were kind of feeling in the second half of 2018, the unemployment rate.

Worthing Jackman: Yes, you've got to look first and foremost at recycling, right? That's

when China changed stripes on the recycling industry, and we [gapped] down, what, $75 million of EBITDA. And that was not much more revenue because it was all commodity driven, right? And so that was a huge impact to margins. And obviously, you had the downdrafts, going into a downdraft with regards to E&P as well. And so those are the two high-margin impacts.

But clearly, if you're looking at 2018 and the run rate there, obviously, China was the biggest disruptor with regards to commodity values. And again, we're not seeing that right now because China is off the table, but obviously, the demand in the U.S. for recovered commodities is insatiable.

Michael Feniger: That makes sense. And kind of a follow-up on, I think, Tyler's question. You guys are guiding the second half margin expansion; you guys are already getting ahead of the price cost dynamic. And you're exiting this year certainly above 5% or even higher on pricing. We have the CPI resets in the second half of 2022. So Worthing, are we not just setting up for a higher-than-normal margin expansion next year? Maybe just the puts and takes there of why we wouldn't see higher-than-normal margins for expansion for 2022.

Worthing Jackman: Yes, because the world doesn't normally move up into the right with regards to anything people model, right?

Michael Feniger: Yes.

Worthing Jackman: And so we always know that markets are like a portfolio, there's always something happening somewhere. There could be politics in some cases, it could be a cost issue in another case. And so rather than get ahead of ourselves, we likely be up to the right without any disruption to the upside. And let's assume that you've got some things that hit you all the time with regards to diluting all the good that we talk about. And so not out of the question, to your point, but we wouldn't suggest that people own us for pure [perfection] like that.

Michael Feniger: Fair enough. And just lastly, Worthing, anything you're seeing at all in July or recently with some of these hotspots that are popping up? Maybe it's too early; I'm just curious if there's anything you're hearing on the ground. Do you see these recent hotspots that are impacting volumes or anything in there? Thank you.

Worthing Jackman: Sure. Well, one thing I'd say, because you're right, there have been some hotspots, and I'll get to that. But if we look at July, right now, we're cycling at over $500 million a month in revenue in a month like July. And to look at our forecasting for that month relative to the revenue we did, we came in at around 1/2 of 1% above the revenue we had forecasted.

And so I say that because you look at the command and control and the insight, how our people know their business. Yes, there's a lot happening on the ground, but through that, what you see here is folks that still know their business and are executing the hell out of their business. And so we're quite pleased with the way July was forecasted and the way it came in.

You're right on the labor side with the Delta variant. I think in our industry, our industry reflects a lot of the data you see in the U.S. You've seen increases and again, this is more on the labor side than anything else. You've seen increasing positives. That's been regional in nature in some cases and hotspots in others. That impacts staffing, that has the contact tracing quarantine knock-off on that. But our folks work through it.

This is an industry of real people, real families, that care for children and care for their communities and want to get the job done. And it's a testament to our folks leaning into it and [hiring] the commitments as best as possible. And so it's upon us in these times and like any year to pay our people well and recognize them for their efforts.

Michael Feniger: Great, thank you.

Operator: Thank you. There are no further questions at this time. Mr. Jackman, I will now turn the conference back over to you.

Worthing Jackman: Look, there are no further questions. On behalf of our entire management team, we appreciate your listening to and interest in the call today. Mary Ann and Joe Box are available today to answer any questions that we did not cover that we're allowed to answer under Reg FD, Reg G and applicable securities laws in Canada.

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

Operator: That does conclude the conference call for today. We thank you all for your participation, and we ask that you disconnect your lines. Thank you and have a great day.