

GFL Environmental Inc

Downgrade to Neutral post the rally: 2024 a pause to a solid long-term story

Rating Change: NEUTRAL | PO: 35.00 USD | Price: 33.83 USD

Downgrade to Neutral post rally – limited upside to PO

While it was a volatile year, GFL finished '23 as the second best performing waste stock (RSG +30%, GFL +18%, WM +16%, WCN +13%, CWST +8%). We downgrade GFL to Neutral as there is only moderate upside to our PO. In our view, GFL reigniting growth initiatives is positive long-term, yet likely weighs on valuation near-term given the acute focus around leverage. We continue to see GFL's transformation bearing fruit yet already forecasts GFL to report the highest margin expansion in the sector (exhibit 2).

Reigniting the growth engine: positive long-term basis...

GFL's focus in 2023 was simple: divest assets, less M&A, pay down debt, de-lever, drive margins up (+130bps). GFL is somewhat pivoting back to growth mode in 2024: \$250-300mn in investments related to sustainability projects (i.e., renewable natural gas, recycling), \$600-650mn in M&A, normal baseline capex \$850-900mn. To be clear, these sustainability projects are high returns yet likely not to move the needle in 2024 (full run rate expected by 2026) and GFL has a successful track record of M&A integration.

...yet likely weighs on '24 given acute focus on leverage

Most waste operators are investing in sustainability projects, baseline capex, and M&A, yet GFL's leverage is higher and FCF more seasonal. Notable de-leveraging progress was made (Q323 4.3x vs Q422 5.02x), partly helped by divestures (\$1.6bn of gross proceeds). GFL expects growth initiatives in 2024 to add ~20bps to net leverage, offset by normal organic de-leveraging. Can GFL run with higher leverage, invest in growth, and naturally de-lever? Yes. Is the room for error smaller, especially with a seasonal FCF profile (FY23 target: \$705mn vs \$339mn YTD – big Q4 ramp) and some RNG project uncertainty? Yes.

Valuation: there are two ways the discount can close...

We make slight adjustments to our model and leave our PO of C\$46/\$35 unchanged at ~11.5x 2024e EV/EBITDA (vs 11x prior) as peers multiples have re-rated. GFL is likely to close the valuation discount to national peers (13-14x) over the long-term yet this may be difficult over next 12 months (higher spending, constrained FCF). The other way the discount narrows is more sector specific – defensive premium vs cyclicals narrow (exhibit 7-8) as industrial cycle indicators bottom, inflection, and recover in the 2H.

Estimates(Dec) (C\$)	2021A	2022A	2023E	2024E	2025E
EPS	(1.83)	(0.72)	0.06	0	0.38
GAAP EPS	(1.83)	(1.07)	0.06	0	0.38
EPS Change (YoY)	41.0%	60.7%	NM	NM	NA
DPS	0.04	0.05	0.05	0.06	0.06
Common - Dual Listed EPS (C\$)	(1.83)	(0.72)	0.06	0	0.38
Common - Dual Listed DPS (C\$)	0.04	0.05	0.05	0.06	0.06
Valuation (Dec)					
P/E	NM	NM	743.5x	NA	120.3x
Dividend Yield	0.1%	0.1%	0.1%	0.1%	0.1%
EV / EBITDA*	17.3x	14.7x	12.7x	11.5x	10.4x
Free Cash Flow Yield*	-13.4%	-6.0%	4.3%	0.3%	2.9%

* For full definitions of *IQmethod*SM measures, see page 6.

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12647970

Timestamp: 19 January 2024 06:00AM EST

19 January 2024

Equity

Key Changes

(C\$)	Previous	Current
Inv. Opinion	B-1-7	B-2-7
Inv. Rating	BUY	NEUTRAL
2023E Rev (m)	7,479.6	7,483.0
2024E Rev (m)	8,132.1	8,074.9
2025E Rev (m)	8,766.7	8,600.4
2023E EBITDA (m)	1,999.7	2,000.2
2024E EBITDA (m)	2,259.6	2,215.2
2025E EBITDA (m)	2,484.9	2,429.7

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Stock Data

Price (NYS / TOR)	33.83 USD / 45.66 CAD
Price Objective	35.00 USD / 46.00 CAD
Date Established	2-Nov-2023 / 2-Nov-2023
Investment Opinion	B-2-7 / B-2-7
52-Week Range	26.87 USD - 39.06 USD
Market Value (mn)	12,157 USD
Free Float	71.9%
Average Daily Value	40.57 USD
Shares Outstanding (mn)	359.3 / 359.3
BofA Ticker / Exchange	GFL / NYS
BofA Ticker / Exchange	YGFL / TOR
Bloomberg / Reuters	GFL US / GFLN
ROE (2023E)	0.3%
Net Dbt to Eqty (Dec-2022A)	152.0%

ESGMeterTM

Medium

ESGMeter is not indicative of a company's future stock price performance and is not an investment recommendation or rating. ESGMeter is independent of BofA Global Research's equity investment rating, volatility risk rating, income rating, and price objective for that company. For full details, refer to "BofA ESGMeter Methodology".

RNG = renewable natural gas

iQprofileSM GFL Environmental Inc

iQmethodSM – Bus Performance*

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Return on Capital Employed	-0.4%	0.2%	0.3%	0.4%	2.6%
Return on Equity	-11.7%	-4.5%	0.3%	0%	1.9%
Operating Margin	-1.2%	0.9%	1.1%	1.3%	7.4%
Free Cash Flow	(2,049)	(954)	690	46	472

iQmethodSM – Quality of Earnings*

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash Realization Ratio	NM	NM	NM	NA	13.7x
Asset Replacement Ratio	3.2x	2.0x	0.7x	1.3x	1.1x
Tax Rate	14.9%	49.0%	25.0%	25.0%	25.0%
Net Debt-to-Equity Ratio	134.8%	152.0%	125.9%	117.4%	102.7%
Interest Cover	-0.2x	0.1x	0.1x	0.2x	1.4x

Income Statement Data (Dec)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Sales	5,526	6,761	7,483	8,075	8,600
% Change	31.7%	22.4%	10.7%	7.9%	6.5%
Gross Profit	528	798	901	993	1,410
% Change	177.5%	51.2%	13.0%	10.2%	42.0%
EBITDA	1,464	1,721	2,000	2,215	2,430
% Change	35.9%	17.6%	16.2%	10.7%	9.7%
Net Interest & Other Income	(647)	(422)	58	(100)	(450)
Net Income (Adjusted)	(662)	(264)	22	0	140
% Change	40.8%	60.0%	NM	NM	NA

Free Cash Flow Data (Dec)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Net Income from Cont Operations (GAAP)	(607)	(183)	104	1	140
Depreciation & Amortization	932	1,009	1,129	1,235	1,313
Change in Working Capital	(87)	(86)	(970)	(733)	(708)
Deferred Taxation Charge	(166)	(196)	0	0	0
Other Adjustments, Net	826	552	1,233	1,130	1,172
Capital Expenditure	(2,947)	(2,051)	(805)	(1,588)	(1,446)
Free Cash Flow	-2,049	-954	690	46	472
% Change	47.0%	53.4%	NM	-93.3%	921.8%
Share / Issue Repurchase	NA	NA	NA	NA	NA
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	1,805	752	0	0	0

Balance Sheet Data (Dec)

(C\$ Millions)	2021A	2022A	2023E	2024E	2025E
Cash & Equivalents	190	82	753	778	1,227
Trade Receivables	1,135	1,118	2,039	2,434	2,557
Other Current Assets	171	183	225	177	189
Property, Plant & Equipment	6,011	6,540	6,217	6,069	5,702
Other Non-Current Assets	10,831	11,844	11,246	11,100	10,912
Total Assets	18,337	19,768	20,480	20,558	20,586
Short-Term Debt	17	18	18	18	18
Other Current Liabilities	1,505	2,674	2,667	2,281	1,707
Long-Term Debt	7,962	9,249	9,249	9,249	9,249
Other Non-Current Liabilities	2,272	966	966	966	966
Total Liabilities	12,598	13,724	13,717	13,330	12,757
Total Equity	5,776	6,044	6,764	7,228	7,829
Total Equity & Liabilities	18,374	19,768	20,480	20,558	20,586

* For full definitions of iQmethodSM measures, see page 6.

Company Sector

Industrial Machinery

Company Description

GFL is the fourth largest diversified environmental services company in North America that serves municipal, residential, commercial, and industrial customers. GFL is vertically integrated, owning 450+ post collection facilities, 160+ transfer stations, and 90+ landfills.

Investment Rationale

We have a positive long-term outlook for GFL Environmental given the stability of the solid waste industry, portfolio transformation, and M&A runway. Solid waste is a relatively defensive industry due to its diverse customer base, high degree of annuity-type revenue, essential service for the public health, and barriers to entry. That said, GFL's growth initiatives in 2024 are likely to weigh on FCF and de-leveraging prospects in the near-term.

Stock Data

Average Daily Volume	1,199,243
Shares / Common - Dual Listed	1.00

Quarterly Earnings Estimates

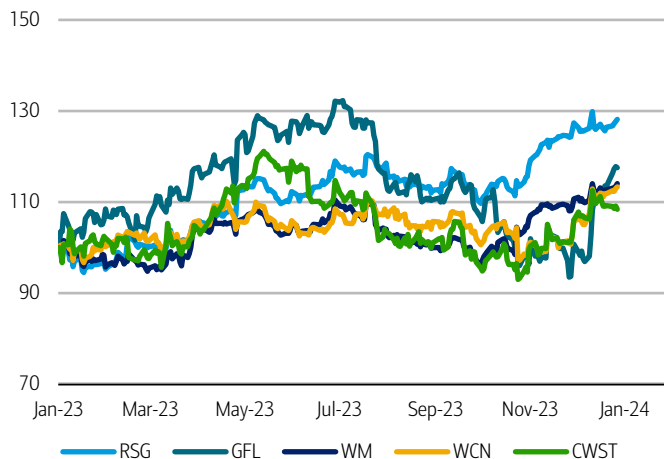
	2022	2023
Q1	0.32A	-0.66A
Q2	0.17A	0.72A
Q3	-0.55A	0.05A
Q4	-0.65A	NAE

Key Changes

(C\$)	Previous	Current
Inv. Opinion	B-1-7	B-2-7
Inv. Rating	BUY	NEUTRAL
2024E EPS	-0.03	0
2025E EPS	0.34	0.38

Exhibit 1: Stock Performance - Waste Companies

GFL finished 2023 as the second best performing waste stock

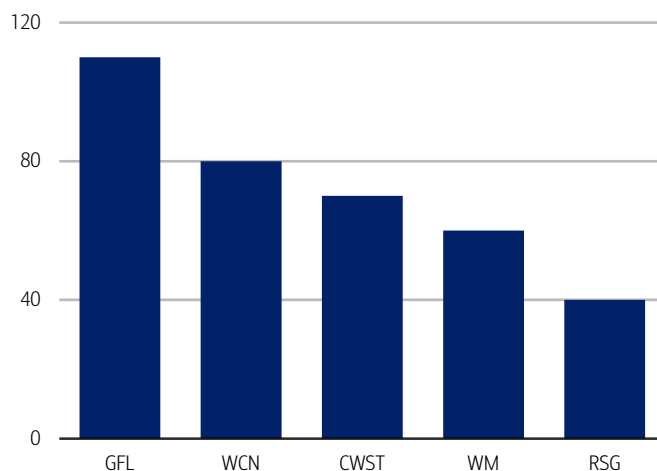


Source: Bloomberg, BofA Global Research

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Exhibit 2: 2024 Consensus Margin Expansion – Waste Companies

Consensus forecasts GFL to report the highest margin expansion in the waste sector in 2024

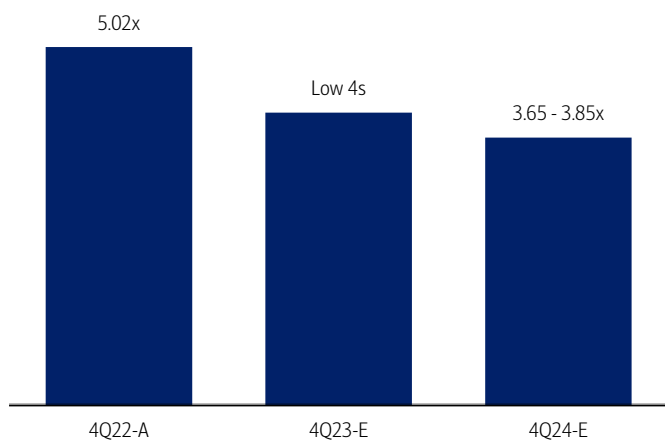


Source: Bloomberg, BofA Global Research

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Exhibit 3: GFL Targeted Net Leverage Profile (4Q22A to 4Q24E)

GFL intends to delever to the low 4s by 4Q23 and 3.65-3.85x by 4Q24

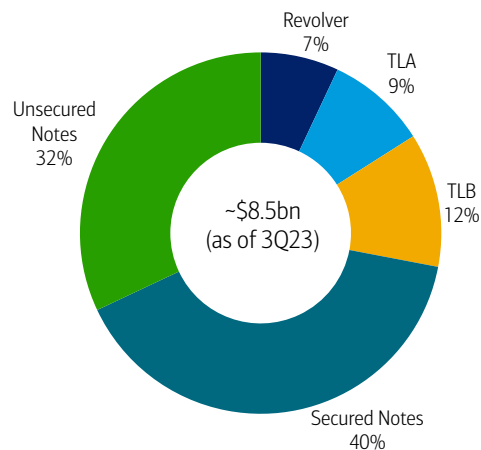


Source: GFL Filings, BofA Global Research

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Exhibit 4: GFL Variable vs Fixed Interest

~72% of GFL's current debt stack has a fixed rate as of 3Q23

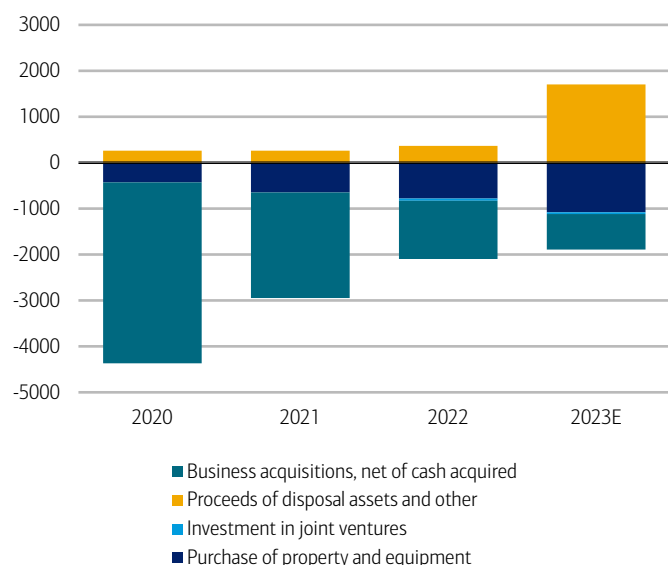


Source: GFL Filings, BofA Global Research

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Exhibit 5: GFL Capex Profile Breakdown (2020-2023E)

In 2023, GFL has been focused on divesting assets, less M&A, paying down debt, and de-leveraging

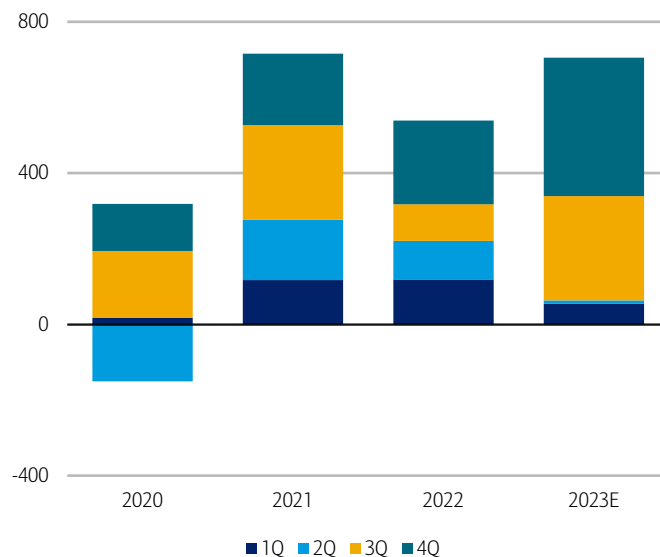


Source: GFL Filings, BofA Global Research, 2023E from Bloomberg Consensus

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Exhibit 6: GFL FCF Ramp By Quarters (2020-2023E)

GFL has typically had a seasonal FCF profile with a big Q4 ramp

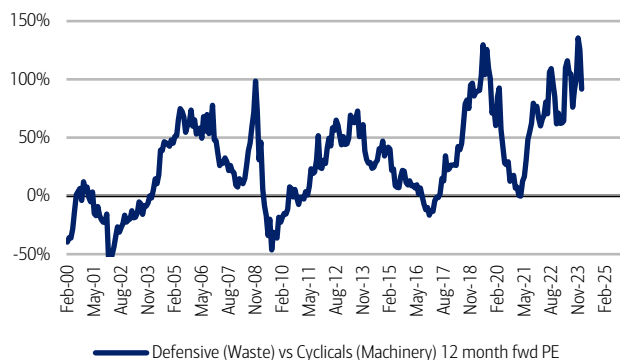


Source: GFL Filings, BofA Global Research

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Exhibit 7: Defensive (Waste) vs Machinery (Cyclical) valuation PE

Defensive premium vs cyclicals - near record levels

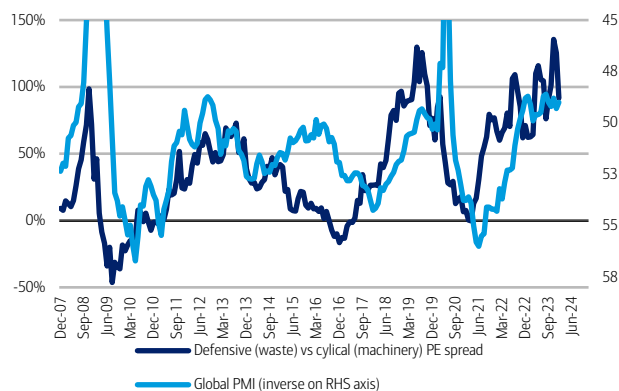


Source: DataStream, Bloomberg, Waste (average WM, RSG), cyclicals (average CAT, DE)

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Exhibit 8: Defensive premium vs Global PMI (inverse in chart)

PMI bottoms and recovers (inverse below), defensive premium narrows



Source: DataStream, Bloomberg, Waste (average WM, RSG), cyclicals (average CAT, DE)

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Price objective basis & risk

GFL Environmental Inc (GFL / YGFL)

Our 12-month price objective of C\$46 (USD \$35) is based on a target 2024E EV/EBITDA multiple of 11.5x, a discount to the public national waste operators due to higher leverage & more back end weighted FCF. We believe EV/EBITDA is the most comparable metric due to high debt levels. We rely on comparable company analysis with a group of publicly traded nonhazardous waste operators, all of which are larger and more liquid than GFL. While GFL's growth profile is significantly higher than the national players, the higher leverage ratio and M&A integration are risks.

Upside risks: 1) driving stronger top line growth than the national players over the next 2-3 years, 2) expanding EBITDA margins (ie, driving profitable growth), 3) organically de-leveraging its balance sheet over the cycle via free cash flow generation, 4) higher than expected synergies from acquisitions.

Downside risks: 1) More cyclical waste stream tied to construction, Industrial activity, new project development impact earnings more than expected, 2) struggle to generate free cash flow, limiting ability to de-lever balance sheet organically, 3) struggle to price the business above rising costs, 4) challenges with integrating acquisitions.

Analyst Certification

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

US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
BUY				
	AECOM	ACM	ACM US	Michael Feniger
	Blue Bird Corp	BLBD	BLBD US	Sherif El-Sabbahy
	Caterpillar Inc	CAT	CAT US	Michael Feniger
	CNH Industrial NV	CNHI	CNHI US	Michael Feniger
	Construction Partners Inc.	ROAD	ROAD US	Michael Feniger
	ESAB Corp	ESAB	ESAB US	Sherif El-Sabbahy
	Finning International Inc.	YFTT	FTT CN	Sherif El-Sabbahy
	H&E Equipment Services Inc	HEES	HEES US	Sherif El-Sabbahy
	Knife River Corp	KNF	KNF US	Sherif El-Sabbahy
	Republic Services	RSG	RSG US	Michael Feniger
	Techtronic Industries Co Ltd	TTNDF	669 HK	Michael Feniger
	Techtronic Industries Co Ltd	TTNDY	TTNDY US	Michael Feniger
	United Rentals Inc	URI	URI US	Michael Feniger
	Vulcan Materials	VMC	VMC US	Michael Feniger
	Waste Connections Inc	WCN	WCN US	Michael Feniger
	WillScot Mobile Mini	WSC	WSC US	Sherif El-Sabbahy
NEUTRAL				
	AGCO Corp	AGCO	AGCO US	Michael Feniger
	Cummins Inc	CMI	CMI US	Michael Feniger
	Deere & Co	DE	DE US	Michael Feniger
	Fluor	FLR	FLR US	Michael Feniger
	GFL Environmental Inc	GFL	GFL US	Michael Feniger
	GFL Environmental Inc	YGFL	GFL CN	Michael Feniger
	Jacobs Eng.	J	J US	Michael Feniger
	Kennametal Inc.	KMT	KMT US	Michael Feniger
	Martin Marietta Materials	MLM	MLM US	Michael Feniger
	NV5 Global Inc.	NVEE	NVEE US	Michael Feniger
	RB Global, Inc	RBA	RBA US	Michael Feniger
	Terex Corp.	TEX	TEX US	Michael Feniger



US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Waste Management	WM	WM US	Michael Feniger
UNDERPERFORM				
	Allison Transmission Holdings Inc.	ALSN	ALSN US	Sherif El-Sabbahy
	Casella	CWST	CWST US	Michael Feniger
	Herc Holdings Inc	HRI	HRI US	Sherif El-Sabbahy
	IPG Photonics	IPGP	IPGP US	Michael Feniger
	Oshkosh Corp.	OSK	OSK US	Michael Feniger
	PACCAR Inc	PCAR	PCAR US	Michael Feniger
	Timken Company	TKR	TKR US	Michael Feniger

iQmethodSM Measures Definitions**Business Performance**

Return On Capital Employed

Return On Equity
Operating Margin
Earnings Growth
Free Cash Flow

Quality of Earnings

Cash Realization Ratio
Asset Replacement Ratio
Tax Rate
Net Debt-To-Equity Ratio
Interest Cover

Valuation Toolkit

Price / Earnings Ratio
Price / Book Value
Dividend Yield
Free Cash Flow Yield
Enterprise Value / Sales

EV / EBITDA

Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income
Operating Profit
Expected 5 Year CAGR From Latest Actual
Cash Flow From Operations – Total Capex

Numerator

Cash Flow From Operations
Capex
Tax Charge
Net Debt = Total Debt – Cash & Equivalents
EBIT

Numerator

Current Share Price
Current Share Price
Annualised Declared Cash Dividend
Cash Flow From Operations – Total Capex
EV = Current Share Price × Current Shares + Minority Equity + Net Debt + Other LT Liabilities
Enterprise Value

Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill
Amortization
Shareholders' Equity
Sales
N/A
N/A

Denominator

Net Income
Depreciation
Pre-Tax Income
Total Equity
Interest Expense

Denominator

Diluted Earnings Per Share (Basis As Specified)
Shareholders' Equity / Current Basic Shares
Current Share Price
Market Cap = Current Share Price × Current Basic Shares
Sales

Basic EBIT + Depreciation + Amortization

iQmethodSM is the set of BofA Global Research standard measures that serve to maintain global consistency under three broad headings: Business Performance, Quality of Earnings, and validations. The key features of iQmethod are: A consistently structured, detailed, and transparent methodology. Guidelines to maximize the effectiveness of the comparative valuation process, and to identify some common pitfalls.

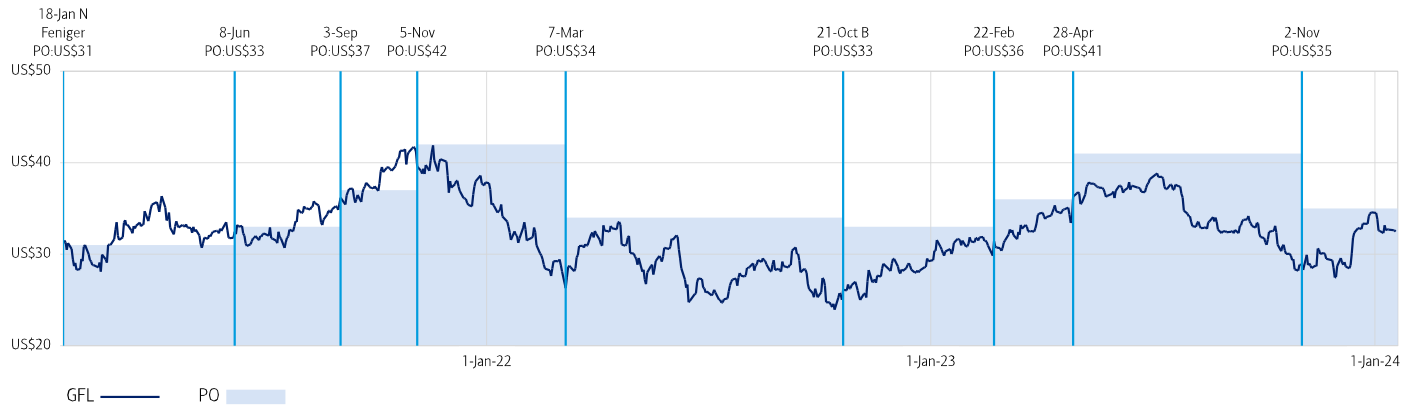
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Disclosures

Important Disclosures

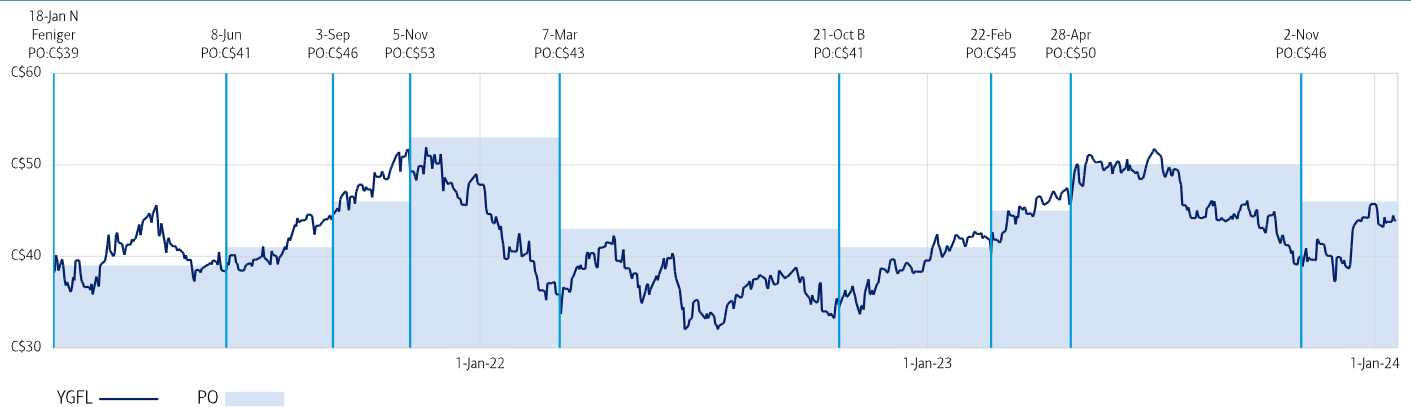
GFL Environmental (GFL) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

GFL Environmental (YGFL) Price Chart



B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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Equity Investment Rating Distribution: Machinery/Diversified Manufacturing Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships ^{R1}	Count	Percent
Buy	27	42.19%	Buy	8	29.63%
Hold	17	26.56%	Hold	8	47.06%
Sell	20	31.25%	Sell	8	40.00%

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

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

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



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

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

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