

Waste Connections Inc

Garbage man delivers

Reiterate Rating: BUY | PO: 174.00 USD | Price: 156.55 USD

WCN finishing a rather turbulent 2023 on a high note

WCN reported Q4 EBITDA of \$656mn, up 16% YoY, on a 9% revenue gain. EBITDA came in 1% ahead of cons due to a slightly higher margin expansion (+200bps YoY) and strong flow-through (56%). While the shine in WCN's Q4 is not as bright as the impressive result by WM (record margin of 29.9% up 240bps YoY, ~70% flow through – albeit, the expectations bar was lower), we still believe WCN results is rather positive in the context of 2023 and the momentum into 2024. In our view, WCN finished the year on a high note to help put a rather uncharacteristically turbulent 2023 (CEO change, landfill ETLF issue) in the rearview mirror and to build momentum into 2024 – reiterate Buy rating.

Positive margin story unfolding – eye on +34% target

A powerful margin story is unfolding across the waste sector and particularly WCN. Q4 Margin of 32.2% was up 200bps YoY primarily led by underlying solid waste margin expansion – a great starting point for next year. 2024 guidance includes 120bps of expansion: 50-60bps is attributable to M&A & commodities, with the remaining margin expansion derived from the core solid waste business. The company is observing strong price vs cost dynamics and improvement in key metrics (OT, turnover, productivity) providing visibility to 34% margin (or higher as Secure acquisition kicks into gear).

M&A: sticking to core WCN with more runway left

WCN is guiding to over 9% revenue growth in 2024 with 4% from M&A (including Secure Energy, closed Feb 1st). We hold a favorable outlook on the Secure acquisition given its footprint, FCF accretion, and idiosyncratic drivers in Canada energy side. In our view, WCN's recent acquisitions (Secure, Arrowhead) likely open up more M&A runway for the operator to stay within its core competency and compound cash flow. Leverage remains within the 2.5-3x range and we expect there is still an active pipeline.

WCN attending BofA event - look for more clues

WCN is guiding 2024 outlook: sales of \$8.75bn (+9.1% YoY), EBITDA \$2.86bn (+13.4% YoY). WCN is attending BofA Florida Conference on Feb 29th - look for more clues on price vs cost, FCF conversion post 2024, margin progression. We update estimates and raise our PO to \$174 (\$165) based on 17.5x 2024e EV/EBITDA as higher multiple is warranted given the strong margin development (vs 17x prior).

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	3.82	4.19	5.09	5.72	6.40
GAAP EPS	3.24	2.95	5.09	5.72	6.40
EPS Change (YoY)	18.3%	9.7%	21.5%	12.4%	11.9%
DPS	0.95	1.05	1.21	1.35	1.51
Valuation (Dec)					
P/E	41.0x	37.4x	30.8x	27.4x	24.5x
GAAP P/E	48.3x	53.1x	30.8x	27.4x	24.5x
Dividend Yield	0.6%	0.7%	0.8%	0.9%	1.0%
EV / EBITDA*	21.2x	18.7x	16.5x	15.1x	13.8x
Free Cash Flow Yield*	2.8%	3.0%	3.0%	3.9%	4.2%

* For full definitions of *IQmethod*SM measures, see page 4.

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Timestamp: 14 February 2024 05:00AM EST

14 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	165.00	174.00
2024E Rev (m)	8,746.4	8,779.7
2025E Rev (m)	9,405.7	9,439.5
2026E Rev (m)	NA	10,145.5
2024E EPS	4.81	5.09
2025E EPS	5.44	5.72
2026E EPS	NA	6.40
2024E DPS	1.17	1.21

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Stock Data

Price	156.55 USD
Price Objective	174.00 USD
Date Established	14-Feb-2024
Investment Opinion	A-1-7
52-Week Range	126.12 USD - 158.49 USD
Mrkt Val (mn) / Shares Out (mn)	40,334 USD / 257.6
Free Float	99.4%
Average Daily Value (mn)	150.28 USD
BofA Ticker / Exchange	WCN / NYS
Bloomberg / Reuters	WCN US / WCN.N
ROE (2024E)	16.2%
Net Dbt to Eqty (Dec-2023A)	86.7%
ESGMeter TM	Medium

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OT = Overtime, WM = Waste Management,
WCN = Waste Connections, RNG =
Renewable Natural Gas

iQprofileSM Waste Connections Inc

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	7.8%	8.0%	9.1%	9.5%	9.8%
Return on Equity	14.0%	14.6%	16.2%	16.3%	16.3%
Operating Margin	20.0%	20.7%	22.2%	22.7%	23.2%
Free Cash Flow	1,110	1,193	1,207	1,577	1,713

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	2.1x	2.0x	1.8x	1.8x	1.7x
Asset Replacement Ratio	1.2x	1.1x	1.3x	1.1x	1.1x
Tax Rate	21.0%	23.0%	22.0%	22.0%	22.0%
Net Debt-to-Equity Ratio	95.9%	86.7%	71.0%	54.8%	40.2%
Interest Cover	7.2x	6.2x	7.3x	8.1x	8.9x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	7,212	8,022	8,780	9,440	10,146
% Change	17.2%	11.2%	9.4%	7.5%	7.5%
Gross Profit	2,876	3,277	3,731	4,059	4,403
% Change	15.2%	14.0%	13.9%	8.8%	8.5%
EBITDA	2,221	2,523	2,867	3,134	3,419
% Change	15.7%	13.6%	13.6%	9.3%	9.1%
Net Interest & Other Income	(193)	(253)	(265)	(264)	(264)
Net Income (Adjusted)	985	1,081	1,310	1,465	1,630
% Change	16.4%	9.7%	21.2%	11.9%	11.2%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	836	763	1,310	1,465	1,630
Depreciation & Amortization	919	1,003	1,067	1,136	1,210
Change in Working Capital	73	13	(30)	3	(21)
Deferred Taxation Charge	93	6	0	0	0
Other Adjustments, Net	102	342	10	10	10
Capital Expenditure	(913)	(934)	(1,150)	(1,038)	(1,116)
Free Cash Flow	1,110	1,193	1,207	1,577	1,713
% Change	16.3%	7.5%	1.2%	30.7%	8.6%
Share / Issue Repurchase	(425)	0	(173)	(173)	(173)
Cost of Dividends Paid	(243)	(271)	(309)	(345)	(384)
Change in Debt	1,742	(233)	0	0	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	79	78	699	1,558	2,515
Trade Receivables	834	857	674	698	750
Other Current Assets	205	206	206	206	206
Property, Plant & Equipment	7,143	7,490	7,918	8,165	8,416
Other Non-Current Assets	8,874	9,284	9,129	8,974	8,819
Total Assets	17,135	17,916	18,626	19,602	20,707
Short-Term Debt	7	26	26	26	26
Other Current Liabilities	1,513	1,661	1,448	1,476	1,507
Long-Term Debt	6,890	6,725	6,725	6,725	6,725
Other Non-Current Liabilities	1,618	1,805	1,805	1,805	1,805
Total Liabilities	10,028	10,218	10,004	10,033	10,063
Total Equity	7,107	7,698	8,526	9,474	10,548
Total Equity & Liabilities	17,135	17,916	18,530	19,507	20,612

* For full definitions of iQmethodSM measures, see page 4.

Company Sector

Industrial Machinery

Company Description

Waste Connections is the third largest non-hazardous waste operator, servicing commercial, industrials, municipal, and residential customers across 39 states and 5 Canadian Provinces. The company is vertically integrated, owning 260 collection operations, 135 transfer stations, 93 active solid waste landfills, 70 recycling centers, and multiple E&P waste treatment facilities. Waste Connections has significant economies of scale, with 55% of the waste it collects disposed at its own landfill.

Investment Rationale

We expect Waste Connections (WCN) to be a chief beneficiary of improving waste volumes, a stronger pricing environment, and a more buoyant M&A backdrop. Over the long term, WCN is likely to emerge a winner as a fragmented waste industry consolidates. Connection's is a best-in-class operator with sector leading profitability and FCF conversion. We expect investors to appreciate WCN's earnings visibility, margin expansion opportunity, rising free cash flow, and proven M&A track-record.

Stock Data

Average Daily Volume 959,936

Quarterly Earnings Estimates

	2023	2024
Q1	0.89A	1.04E
Q2	1.02A	1.22E
Q3	1.17A	1.39E
Q4	1.11A	1.44E

Price objective basis & risk

Waste Connections Inc (WCN)

Our \$174 price objective values WCN on 17.5x 2024e EV/EBITDA, in line with the average of the valuation range the last 7 years (12-21x). Our PO implies 33x Price to FCF in 2024e, at the higher end of the historical range (20-32x), justified by Connection's sector leading profitability and FCF conversion, in our view. Our PO implies nearly a 0.8% dividend yield, in line with its current valuation over the last 12 months. Relative to history, our higher valuation stems from an improving pricing backdrop for the waste industry, more active M&A environment, and ability to improve margins and FCF generation (double digit growth) through the cycle.

Upside risks to our PO are: 1) stronger-than-expected housing data, 2) higher-than-expected CPI trends, 3) more aggressive cash return to shareholders than we currently envision, and 4) stronger-than-expected recovery in Exploration and Production (oil and gas) activity.

Downside risks to our PO are: 1) lower-than-expected CPI, 2) environmental liabilities, 3) higher than expected inflationary costs, and 4) execution risk around 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
	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



US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
	Martin Marietta Materials	MLM	MLM US	Michael Feniger
	NV5 Global Inc.	NVEE	NVEE US	Michael Feniger
	PACCAR Inc	PCAR	PCAR US	Michael Feniger
	RB Global, Inc	RBA	RBA US	Michael Feniger
	Waste Management	WM	WM US	Michael Feniger
UNDERPERFORM				
	Allison Transmission Holdings Inc.	ALSN	ALSN US	Sherif El-Sabbahy
	Casella	CWST	CWST US	Michael Feniger
	Cummins Inc	CMI	CMI 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
	Terex Corp.	TEX	TEX 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

$\text{NOPAT} = (\text{EBIT} + \text{Interest Income}) \times (1 - \text{Tax Rate}) + \text{Goodwill Amortization}$
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
 $\text{EV} = \text{Current Share Price} \times \text{Current Shares} + \text{Minority Equity} + \text{Net Debt} + \text{Other LT Liabilities}$
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

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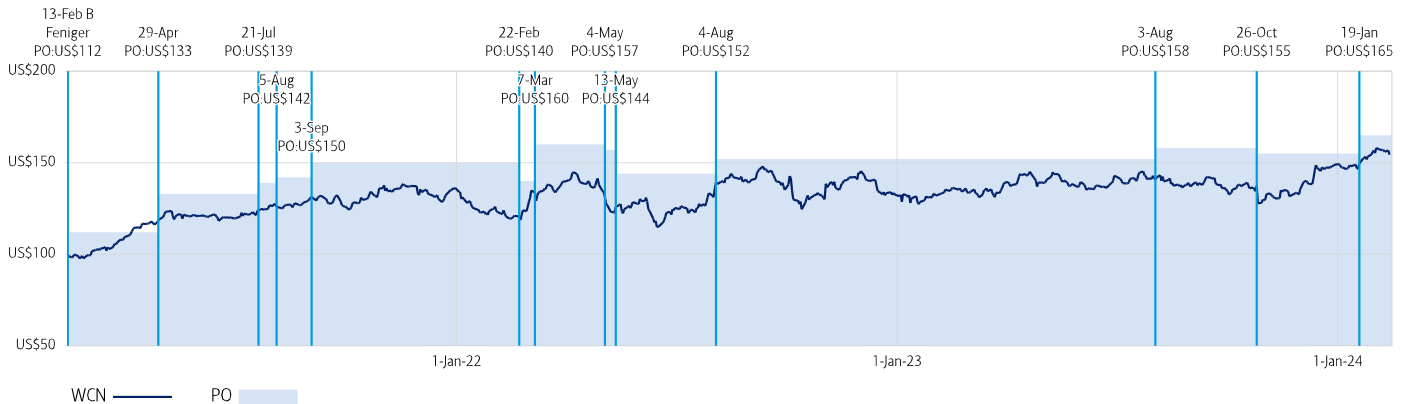
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Waste Connections (WCN) Price Chart



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.

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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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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