

Casella

Capping a transformational year on a high note

Reiterate Rating: UNDERPERFORM | PO: 92.00 USD | Price: 92.80 USD

4Q results solid, broadly in line: pricing a key bright spot

CWST capped off a transformational 2023 (acquired seven acquisitions, including market entries into new regions) on a high note. Q4 results were solid: adj EBITDA of \$82mn increased 46% YoY on a 32% revenue gain, and was in-line with consensus (\$82mn). CWST disclosed certain one-time items that impacted the quarter including a \$3.9mn charge related to a landfill capping veneer failure, which is undergoing an engineering analysis to determine root causes and responsibility of the event. Bright spots in the quarter: EBITDA margin of 22.8% expanded 220bps YoY, and solid waste price of 7.5% stepped up sequentially from +6.9% in 3Q as a result of CWST's flexible pricing program.

2024 guidance positive yet consensus is broadly there

CWST provided 2024 guidance that was largely in-line with consensus, albeit slightly above the preliminary outlook provided last quarter in certain areas: sales of \$1.48-\$1.51bn (+17-19% YoY), EBITDA of \$350-\$360mn (+19-22% YoY), and adj. FCF of \$140-\$150mn (+9-17% YoY). We note that consensus is already positioned a bit on the high end of its EBITDA range (\$359mn) and CWST is reflecting a cautious outlook on Construction & Demolition volumes. However, there are some revised bright spots: pricing +5-6% YoY (vs +5-5.5%), margin expansion +30-50bps YoY (vs +30-40bps prior).

Continues to invest and see growth opportunities

2023 was a transformational year: acquired 7 business for ~\$315mn in revenue (highest in company history). Moreover, these acquisitions expand CWST's footprint into new markets (for e.g., Mid-Atlantic) – providing more room for tuck-ins. Capex is expected to be ~\$180mn (+16 YoY) in FY24 as the company continues to make investments to enhance its portfolio, including \$5mn associated with its McKean landfill rail project.

Reiterate Underperform as valuation limits upside

We update our estimates post 4Q. We raise our PO to \$92 (\$86) based on ~17x 2024 EV/EBITDA, as we believe a higher multiple is warranted given higher pricing (vs 16x prior). CWST is a quality operator with attractive disposal assets, yet out target multiple is at a premium to the sector and closer in valuation to 'best-in-class' peer, WCN. While we do not see absolute downside to shares, we struggle to see valuation upside from here given constrained FCF yield, lower liquidity & no dividend – reiterate U/P rating.

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	1.10	0.94	0.70	1.24	1.62
GAAP EPS	1.03	0.46	0.68	1.22	1.60
EPS Change (YoY)	22.2%	-14.5%	-25.5%	77.1%	30.6%
Consensus EPS (Bloomberg)			1.16	1.48	1.48
DPS	0	0	0	0	0
Valuation (Dec)					
P/E	84.4x	98.7x	132.6x	74.8x	57.3x
GAAP P/E	90.1x	201.7x	136.5x	76.1x	58.0x
EV / EBITDA*	27.3x	22.7x	18.8x	17.1x	15.7x
Free Cash Flow Yield*	1.6%	1.5%	1.6%	2.3%	2.4%

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

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Timestamp: 16 February 2024 12:09AM EST

16 February 2024

Equity

Key Changes

(US\$)	Previous	Current
Price Obj.	86.00	92.00
2024E Rev (m)	1,500.2	1,494.9
2025E Rev (m)	1,609.5	1,614.8
2026E Rev (m)	NA	1,720.1
2024E EPS	1.32	0.70
2025E EPS	1.65	1.24
2026E EPS	NA	1.62

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Stock Data

Price	92.80 USD
Price Objective	92.00 USD
Date Established	16-Feb-2024
Investment Opinion	B-3-9
52-Week Range	72.33 USD - 95.78 USD
Mkt Val (mn) / Shares Out (mn)	5,289 USD / 57.0
Free Float	99.0%
Average Daily Value (mn)	26.46 USD
BofA Ticker / Exchange	CWST / NAS
Bloomberg / Reuters	CWST US / CWST.OQ
ROE (2024E)	7.5%
Net Dbt to Eqty (Dec-2023A)	154.5%
ESGMeter TM	Medium

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WCN = Waste Connections, CWST = Casella, U/P = Underperform

iQprofileSM Casella

iQmethodSM – Bus Performance*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	5.6%	3.1%	3.4%	4.4%	5.1%
Return on Equity	12.4%	10.1%	7.5%	12.0%	13.8%
Operating Margin	8.8%	6.4%	7.2%	9.0%	10.1%
Free Cash Flow	86	78	86	120	125

iQmethodSM – Quality of Earnings*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	3.8x	4.5x	6.6x	4.4x	3.6x
Asset Replacement Ratio	1.0x	0.9x	0.8x	0.9x	0.9x
Tax Rate	29.2%	31.4%	29.2%	30.0%	30.0%
Net Debt-to-Equity Ratio	105.0%	154.5%	128.4%	94.9%	65.5%
Interest Cover	4.1x	2.2x	2.1x	3.2x	4.3x

Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	1,085	1,265	1,495	1,615	1,720
% Change	22.0%	16.5%	18.2%	8.0%	6.5%
Gross Profit	362	433	519	569	615
% Change	18.0%	19.5%	20.1%	9.6%	8.0%
EBITDA	245	295	355	390	425
% Change	20.5%	20.1%	20.5%	9.9%	9.0%
Net Interest & Other Income	(20)	(43)	(52)	(45)	(40)
Net Income (Adjusted)	57	52	40	72	94
% Change	23.0%	-9.1%	-21.8%	77.3%	31.0%

Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	53	25	39	71	93
Depreciation & Amortization	126	171	221	218	224
Change in Working Capital	(11)	51	23	389	372
Deferred Taxation Charge	17	0	0	0	0
Other Adjustments, Net	33	(14)	(18)	(363)	(353)
Capital Expenditure	(131)	(155)	(180)	(195)	(210)
Free Cash Flow	86	78	86	120	125
% Change	45.3%	-9.4%	9.5%	40.6%	4.0%
Share / Issue Repurchase	0	496	0	0	0
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	27	433	0	0	0

Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	71	231	318	438	564
Trade Receivables	101	94	118	114	113
Other Current Assets	35	35	35	35	35
Property, Plant & Equipment	721	1,552	1,510	1,486	1,472
Other Non-Current Assets	521	512	503	494	485
Total Assets	1,449	2,424	2,484	2,569	2,670
Short-Term Debt	9	9	9	9	9
Other Current Liabilities	169	189	209	223	232
Long-Term Debt	585	1,031	1,031	1,031	1,031
Other Non-Current Liabilities	189	672	672	672	672
Total Liabilities	951	1,901	1,921	1,935	1,944
Total Equity	498	523	563	634	727
Total Equity & Liabilities	1,449	2,424	2,484	2,569	2,670

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

Company Sector

Industrial Machinery

Company Description

Casella Waste Is a regional environmental services company located in the Northeast. The company operates in six states - Vermont, New Hampshire, New York, Massachusetts, Maine, and Pennsylvania. CWST provides services to residential, commercial, municipal, and industrial customers in solid waste collection, disposal, transfer, recycling, and organics services. Casella is vertically integrated, owning 43 waste collection operations, 58 transfer stations, 9 landfills, and 20 recycling facilities.

Investment Rationale

We have a positive outlook for Casella Waste driven by pricing power, M&A, stability of solid waste, and an attractive landfill footprint across the Northeast. That said, we believe this is fully reflected in valuation, which remains a notable premium to the waste sector. While we do not see much downside to Casella Waste on an absolute basis, we see less relative upside given the elevated valuation and market rotation to more cyclical sectors.

Stock Data

Average Daily Volume 285,155

Quarterly Earnings Estimates

	2023	2024
Q1	0.10A	0.35E
Q2	0.36A	0.38E
Q3	0.35A	0.48E
Q4	0.13A	-0.42E

Price objective basis & risk

Casella (CWST)

Our 12-month price objective on Casella Waste is \$92 per share. This is based on 17x 2024 EV/EBITDA, in-line with its seven year average (7-25x). Our target multiple is a premium to our valuation framework in the waste sector given Casella's growth prospects are higher than the industry. We note CWST has lower liquidity and does not pay a dividend. On our \$92 PO, CWST would trade on a 2.4% FCF yield (below sector average 2.7%) although we expect the company to deliver over double digit FCF growth rate over the next few years.

Upside risks:

- i) Stronger than expected price gains across collection and disposal business lines.
- ii) Higher than expected M&A activity.
- iii) Expanding EBITDA margin and FCF conversion above expectations.

Downside risks:

- i) Elevated costs and capex required to sustain growth.
- ii) Labor, inflationary costs impact solid waste margin more than anticipated.
- iii) Competitive pricing dynamics emerge in the Northeast disposal market.

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

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	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



US - Machinery Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
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	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

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

Denominator

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

Quality of Earnings

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

Numerator

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

Denominator

Net Income
Depreciation
Pre-Tax Income
Total Equity
Interest Expense

Valuation Toolkit

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

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

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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Casella (CWST) 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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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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