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Quanta Services, Inc. (PWR) CEO Earl Austin on Q3 2019 Results - Earnings Call Transcript

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Q3: 10-31-19 Earnings Summary

Press Release SEC *10-Q*

EPS of $1.14 beats by $0.09 | Revenue of $3.35B (12.31% Y/Y) beats by $177.96M

Earning Call Audio

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Quanta Services, Inc. (NYSE:PWR) Q3 2019 Earnings Conference Call October 31, 2019 9:00 AM ET

Company Participants

Kip Rupp - VP, IR

Earl Austin - President, CEO, COO, and Director

Derrick Jensen - CFO

Conference Call Participants

Andrew Kaplowitz - Citigroup

Jamie Cook - Credit Suisse

Sean Eastman - KeyBanc Capital Markets

Noelle Dilts - Stifel

Chad Dillard - Deutsche Bank

Blake Hirschman - Stephens

Adam Thalhimer - Thompson Davis

Alex Rygiel - B. Riley

Steven Fisher - UBS

Michael Dudas - Vertical Research

Bill Newby - D.A. Davidson

Operator

Greetings. Welcome to Quanta Services' Third Quarter 2019 Earnings Conference Call. At this time, all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. [Operator Instructions] Please note that today's conference is being recorded.

At this time, I'll turn the call over to Kip Rupp, Vice President of Investor Relations. Kip, you may begin.

Kip Rupp

Thank you and welcome everyone to the Quanta Services third quarter 2019 earnings conference call. This morning, we issued a press release announcing our third quarter results, which can be found in the Investors & Media section of our website at quantaservices.com, along with a summary of our 2019 outlook and commentary that we will discuss this morning.

Please remember that information reported on this call speaks only as of today, October 31st, 2019, and therefore, you're advised that any time-sensitive information may no longer be accurate as of any replay of this call.

This call will include forward-looking statements intended to qualify under the Safe Harbor from liability established by the Private Securities Litigation Reform Act of 1995. These include all statements reflecting Quanta's expectations, intentions, assumptions, or beliefs about future events or performance that do not solely relate to historical or current facts.

Forward-looking statements involve certain risks, uncertainties, and assumptions that are difficult to predict or beyond Quanta's control and actual results may differ materially from those expressed or implied.

For additional information concerning some of these risks, uncertainties, and assumptions, please refer to the cautionary language included in today's press release along with the company's 2018 annual report on Form 10-K and its other documents filed with the Securities and Exchange Commission, which are available on Quanta's or the SEC's website.

You should not place undue reliance on forward-looking statements and Quanta does not undertake any obligation to update such statements and disclaims any written or oral statements made by any third-party regarding the subject matter of this call.

Please also note that we will present certain historical and forecasted non-GAAP financial measures in today's call, including adjusted diluted EPS, backlog, EBITDA, and free cash flow. Reconciliations of these measures to their most directly comparable GAAP financial measures are included in our earnings release.

Lastly, if you would like to be notified when Quanta publishes news releases and other information, please sign up for e-mail alerts through the Investor Relations section of quantaservices.com. We also encourage investors and others interested in our company to follow Quanta IR and Quanta Services on social media channels listed in our website.

With that, I'll turn the call over to Mr. Duke Austin, Quanta's President and CEO. Duke?

Earl Austin

Thanks Kip. Good morning everyone and welcome to the Quanta Services' third quarter 2019 earnings conference call. On the call, I will provide operational and strategic commentary before turning it over to Derrick Jensen, Quanta's Chief Financial Officer, who will provide a detailed review of our third quarter results. Following Derrick's comments, we welcome your questions.

We are pleased to report this morning that Quanta achieved record quarterly revenues, operating income, adjusted EBITDA, and adjusted earnings per share in the third quarter. We also ended the third quarter with record total and 12-month backlog.

Our backlog growth to record levels was driven broadly across our end markets and customer base, including through the support of electric and gas utility customers, incremental programmatic spending, and our communication customers' plans to push fiber deeper into their networks in preparation for the 5G platform. We believe this supports our continued favorable view of multiyear growth opportunities.

We are focused on continuous improvement and accountability to our multiyear plan. We have executed well against our strategy over the past several years and expect that 2019 will be a record year for Quanta.

As a result of our performance and the addition of several previously announced strategic acquisitions, we are increasing our revenue, adjusted EBITDA, and adjusted diluted earnings per share expectations for 2019.

We believe our solid year-to-date results and these increases in guidance demonstrate the successful implementation of our strategic initiatives, our strong position in the marketplace, and favorable trends for multiyear demand of our services. We also believe our results reflect the benefits of service line diversity and our portfolio approach to managing risk, while enhancing earnings power.

Our Electric Power segment performed well during the quarter considering several unique challenges that pushed out some revenues and softened margins a bit. I will note, however, that despite these challenges, our U.S. Electric Power operating margins were double-digit in the quarter and we expect the same in the fourth quarter.

During the quarter, we experienced certain production and labor challenges associated with short-term fluctuations in activity due to high fire risk periods and fire hardening initiatives in California. We believe this was due in part to the unprecedented demand for our resources in the western region of the United States and continued to work through these challenges with our customers. Because our customers' resource needs can change rapidly, we have taken a prudent approach to our fourth quarter utilization expectations.

That said, we believe efforts to fire-harden the power grid in Western United States to enhance safety and service reliability in response to wildfire risk will ultimately result in significant fire hardening grid investment that could last well over a decade.

In Canada, we experienced short-term mobilization delays that impacted resource utilization on two projects. While these effects have carried into the first part of the fourth quarter, we expect improved resource utilization on these projects later this year and further utilization improvements in 2020 and 2021 as construction begins to ramp-up on these projects as well as the Watay transmission project, which is expected to begin construction in the first quarter of 2020.

More broadly, we see continued strength in programmatic spending by our electric utilities on their transmission and distribution networks. We are collaborating with our customers and providing solutions that include large-scale distribution programs, sub-transmission system expansions and a range of technology solutions designed to enhance and modernize the grids of the future, which will benefit the consumer.

Quanta is increasingly managing large portions of these multiyear multibillion-dollar programs, which we believe are in the early stages and will be long-term in duration.

Quanta plays a critical role in facilitating the technologies and lower carbon footprint of the future. For example, the implementation and widespread adoption of new technologies and services such as electric and autonomous vehicles and 5G require power and new infrastructure. And the power grid of today must evolve if it is to meet those additional demands.

We are in active discussions with key players developing technologies, helping them understand the needed infrastructure and how Quanta can help execute their go-to-market strategies.

As these industries deploy new technologies and continue to invest in the future, we believe Quanta will play an important role that becomes increasingly apparent to the investment community.

We continued to gain visibility into the 5G deployment opportunity and believe it is large and that the build-out will take many years due to the density requirements of small cells and the massive amounts of fiber required.

We believe Quanta is uniquely positioned to provide solutions that bridge the gap between wireless carriers and utility companies as 5G infrastructure is increasingly deployed on the electric distribution system, which will require significant time and resources.

Our consolidated communications operations did well in the quarter and we continue to expect full year 2019 revenues of approximately $400 million. We ended the quarter with total backlog of more than $770 million, representing a nearly 18% sequential increase. Our U.S. communications operations are leading the growth and profitability gains for these operations.

We continue to believe we are on track to grow this operation to approximately $1 billion of annual revenue over the coming years. Next year, we see opportunity for double-digit revenue growth for our U.S. communications operations with operating margins approaching double-digits on a full year basis.

Our pipeline and industrial segment had its best quarter in several years. Revenues increased nicely, but more importantly, operating income was a quarterly record and operating margins were 9%, a meaningful increase over the same quarter of last year.

The strong margin performance was driven by solid execution across our operations with materializing benefits of scale from our gas utility operations, excellent execution on our big pipe work, solid results from industrial services, and strengthening midstream activity in the U.S. and Canada.

We have made progress over the past few years towards our upper single-digit annual operating margin goal. We know one quarter is not a trend. However, we believe this quarter demonstrates the profit potential of our pipeline and industrial segment and is evidenced that the margin improvement strategy we've implemented over the past several years is paying dividends. I think it is worth revisiting the key components of that strategy, noting what we have done and what we are doing for sustainable margins going forward.

First, for the last several years, we have been focused on increasing and gaining scale in the base business and diversifying the services and geographies of the segment to create a more sustainable and consistent operation.

The steps we have taken to achieve that include organic expansion of our gas utility operations, the acquisition of Stronghold to establish a leading industrial services capability, and most recently, the acquisition of the Hallen Construction Company, which further enhances the scale of our gas utility operations, particularly in the northeast United States, and improves the margins of our gas utility operations. Going forward, we will continue to focus on growing that base business, both organically and by opportunistically pursuing select acquisitions.

Second, we sought to right-size and rationalize underperforming and non-core operations. In 2017, 2018, and 2019, we shut down, restructured and sold underperforming non-core operations and assets in our pipeline and industrial segment that were previously impacting segment margins by more than 50 basis points. Much of this effort is complete. However, we continue to evaluate our operations for additional steps that can be taken to improve this segment margins.

And finally, we wanted to complete problem projects and focus our efforts on opportunities within our core capabilities. We worked through and completed various problem projects over the past few years that generated unacceptable results.

For example, in the third quarter, we reached mechanical completion on a processing plant that has generated disappointing results for several quarters and has masked the positive results of other margin improvement initiatives.

Going forward, we are focused on pursuing and executing work consistent with our core capabilities. We are confident that our ongoing margin improvement strategy is delivering results and puts us on a path to achieve upper single-digits annual operating income margin goal.

We continue to evaluate opportunities to strategically expand our pipeline and industrial operations as we gain scale and diversity. We believe the result will be a segment with higher margins, less cyclicality, and high-quality repeatable and sustainable earnings streams.

Though we have more work to do, we are proud of our accomplishments to-date and want to recognize the dedication of our field leadership to that end. Over the years, we have also executed on a strategy to mitigate risks inherent to -- in our business, including economic risk due to diversification.

We have a diverse customer base with low customer concentration, a broad and diverse geographic presence and a diverse and expanding line of services. We believe our diversification strategy, favorable industry dynamics, and the strategic investments we have made will continue to benefit our results over a multiyear cycle.

We are confident in our long-term strategy and are focused on generating a more resilient and predictable earnings stream. Our end markets and visibility are strong, and we continue to believe we're in a multiyear up cycle with opportunity for continued record backlog this year and in 2020.

On a consolidated basis, approximately 90% of our 2019 estimated revenue is expected to come from base business activity. We believe we can grow those revenues at a mid to upper single-digit CAGR over at least the next three years.

Additionally, we continue to pursue billions of dollars of electric transmission and pipeline project opportunities and believe some could be awarded over the coming quarters.

While we provide our formal commentary and 2020 expectations on the fourth quarter earnings call next February, we currently expect growth in consolidated revenues, net income, adjusted EBITDA, and earnings per share in 2020 and for Quanta to achieve another year of record results. We are focused on operating the business for the long-term and expect to continue to distinguish ourselves through safe execution and best-in-class field leadership.

We will pursue opportunities to enhance Quanta's base business and leadership position in the industry and provide innovative solutions to our customers. We believe Quanta's diversity, unique operating model, and entrepreneurial mindset form the foundation that will allow us to continue to generate long-term value for all of our stakeholders.

With that, I will now turn the call over to Derrick Jensen, our CFO for his review of our third quarter results. Derrick?

Derrick Jensen

Thanks Duke and good morning everyone. Today, we announced record third quarter 2019 revenues of $3.35 billion, a 12% increase over the third quarter of 2018. For the third quarter of 2019, net income attributable to common stock was $136.1 million or $0.92 per diluted share. Adjusted diluted earnings per share, a non-GAAP measure, was a record $1.14.

Our Electric Power revenues increased 16% when compared to the third quarter of 2018 to $1.88 billion and represent record quarterly revenues for this segment. This is the sixth consecutive quarter of sequential revenue growth for the electric power segment, which continues to be driven by base business activities as our utility customers expand their investment in grid modernization and infrastructure hardening, particularly in the western U.S.

The strength of the base business in the third quarter of 2019 offset approximately $100 million in reduced revenues from larger projects when compared to 3Q 2018. Also contributing to the increase were approximately $50 million in revenues from acquired companies.

Telecom revenues, which are included within our Electric Power segment, were slightly over $100 million with growth largely driven by our U.S. operations. Our U.S. telecom revenues have grown sequentially each quarter since the first quarter of 2017 when we officially reentered the U.S. telecommunications market.

Operating margin in the Electric Power segment was 9.4% in the third quarter of 2019 versus 11.1% in 3Q 2018. This decrease is primarily attributable to the revenue contribution and solid execution in the third quarter of 2018 on the Fort McMurray transmission project in Canada, which was completed earlier this year.

Comparatively, during 3Q 2019, our electric operations in Canada were negatively impacted by delays on certain larger projects as well as record rainfall across parts of Alberta and Manitoba.

Margins in our telecommunications operations were mid-single-digit led by performance in our U.S. telecom operations, but dilutive to overall segment margins. Excluding our telecommunications operations, Electric Power margins were 9.6% for the quarter.

Our pipeline and industrial segment revenues increased 8% when compared to the third quarter of 2018 to $1.48 billion. This increase is primarily due to elevated levels of smaller transmission and pipeline projects and gas distribution services, which offset a decline in revenues from larger pipeline projects. Additionally, third quarter revenues for 2019 included approximately $40 million from acquired companies.

Operating margin for the pipeline and industrial segment was 9% in 3Q 2019, an increase over the 7% margin in 3Q 2018. The margin -- the improvement in margin was primarily driven by strong execution across both larger pipeline projects and our gas distribution services.

Additionally, the third quarter of 2018 was negatively impacted by project losses associated with the processing facility Duke referenced that has now reached mechanical completion as well as challenges encountered on natural gas pipeline project in the northeast of the United States. The projects combined to impact 3Q 2018 margins by slightly over 200 basis points, but had minimal impact on 2019's third quarter results.

Corporate and non-allocated costs increased $16 million as compared to the third quarter of 2018. This increase is primarily due to a $9.9 million increase in acquisition-related costs, $4.6 million of increased amortization expense, and a $5.2 million increase in expense associated with changes in the fair value of contingent consideration liabilities. These increases were partially offset by a $4.2 million net decrease in incentive and stock-based compensation expense.

Overall, 3Q 2019 adjusted EBITDA, a non-GAAP measure, was a record $312 million, a 14% increase compared to $274 million in the third quarter of 2018. This represents the first time we have exceeded $300 million of adjusted EBITDA in a quarter and illustrates the strength of our portfolio approach.

For the third quarter of 2019, we have free cash flow, a non-GAAP measure, of $30 million. Cash flow provided by operating activities was $91 million and net capital expenditures were $61 million.

Days sales outstanding or DSO for the quarter was 91 days, in line with the second quarter but 13 days higher than the 78 days in the third quarter of 2018. Continuing to impact our DSO are balances associated with the Fort McMurray project, certain balances associated with pipeline that projects largely completed in prior periods, and elevated receivables associated with two customers that implemented further billing modifications during the quarter. Of note, the Fort McMurray retainment was collected in full in early October and represents approximately $100 million of cash flow in the fourth quarter.

Additionally, while billing modifications have resulted in elevated receivables, payments were received during the quarter, albeit at a slower pace, and no items are in dispute. Subsequent to quarter end, billing and collections associated with these customers is improving and has contributed to a positive cash flow for the first four weeks of October.

Excluding the impacts described above, DSO for the quarter would have been approximately 82 days, higher than 3Q 2018, but more in line with historical levels, which have averaged 79 days over the 20 quarters from 2014 to 2018.

Based on projected revenue levels for the remainder of the year, the collection of the Fort McMurray retainment and positive developments in billing and collection with some customers, we continue to expect DSO improvement between now and year-end.

We did not purchase any of our common stock during the third quarter of 2019 and had approximately $287 million of available authorization remaining on our $500 million stock repurchase program at September 30, 2019. Additionally, during the third quarter of 2019, we announced our fourth quarterly cash dividend of $0.04 per share totaling $5.6 million.

During the quarter, we amended our credit facility, which among other things provided for an incremental term loan of $687.5 million, and increased commitments on our revolving credit facility by $150 million to approximately $2.14 billion.

At September 30, 2019, we had $80 million in cash and $1.87 billion of borrowings outstanding under our credit facility, $1.26 billion of which is borrowed under the term loans and $608 million of which is borrowed under revolving loans. In addition, we had $347 million in letters of credit outstanding, leaving us with total liquidity of $1.26 billion.

Our debt to EBITDA ratio calculated under our senior secured credit facility is approximately 2.1 times. This debt to EBITDA ratio is above our targeted operating level of around 1.5 times. However, is attributable to the acquisition activity in the period as well as the previously discussed pressures on our DSO.

With the expected DSO improvement and earnings contribution from acquired businesses, we expect the leverage ratio to return to targeted levels in the near term. As of September 30, 2019, our aggregate total remaining performance obligations were estimated to be approximately $4.4 billion, approximately 66% of which is expected to be recognized in the 12 months.

Our total backlog was a record $13.3 billion, an increase of 9% as compared to the third quarter of 2018 and 8% over year-end 2019. 12-month backlog was $7.6 billion, slightly above the third quarter of 2018 and an increase of 8% from December 31, 2019.

Additionally, the Watay transmission project in Canada recently achieved financial close and Quanta received a notice to proceed. As a result, we will include the contract value of the project in our fourth quarter backlog. We will also include a large pipeline that was signed in October and was highlighted in this morning's press release, which we believe will result in record backlog again at year end.

Our total backlog continues to expand as we capitalize on the growing infrastructure investment activity across our end markets and specifically, the longer term demand for our base business activity.

Turning to guidance, given the continued strength across our base business activities and incremental contributions from acquisitions made during the quarter, we are increasing our consolidated revenue expectations for the year to approximately $12 billion.

With regard to the Electric Power segment, we expect revenues for the year to be approximately $7.2 billion. On an annual basis, we now see aggregate Electric segment operating margin ranging from 8.3% to 8.5%, with the $79.2 million effect of the Peruvian project discussed in our second quarter earnings call negatively impacting annual operating margins by roughly 110 basis points.

Due to the uncertainty around the timing of the commencement of activities certain larger projects in Canada and associated impact on fixed costs absorption, we now expect full year margins for the electric power operations to come in slightly below double digits. However, as Duke commented, our U.S. Electric Power operations are expected to exceed 10% for 2019.

Regarding our telecommunications operations, we continue to see the opportunity for operating margins to achieve upper single digits in the fourth quarter of 2019, with our U.S. telecommunications operations leading the way with the potential to hit 10% in the fourth quarter.

We now expect pipeline and industrial segment revenues to range between $4.75 billion and $4.85 billion with full year margins between 6.2% and 6.4%. We expect our full year diluted earnings per share to range between $2.49 to $2.62 and our adjusted diluted earnings per share to range between $3.16 and $3.28.

With regard to the acquisitions made in the third quarter, their results were in line with our expectations. And we continue to expect adjusted diluted earnings per share contribution for the full year to be approximately $0.06. Our expectations for adjusted EBITDA, including the $79.2 million second quarter charge, now range between $904 million and $932 million.

From a cash flow perspective, due largely to reduced revenues associated with the seasonality of our work and therefore reduced working capital requirements; we expect free cash flow for the fourth quarter to range between $300 million and $400 million, resulting in full year free cash flow between $100 million and $200 million.

Due in part to slight changes in working capital expectations for the year as well as incremental cash paid for acquisitions during the quarter, we now expect interest expense for the year to range between $65 million and $66 million.

We believe our third quarter results highlight the continued strength of our end markets and our ability to profitably execute across our operations. We remain confident in our long-term prospects for profitable growth and the repeatable and sustainable nature of our core markets.

This concludes our formal presentation and we'll now open the line for Q&A. Operator?

Question-and-Answer Session

Operator

Thank you. We'll now be conducting the question-and-answer session. [Operator Instructions]

Thank you. Our first question is coming from the line of Andy Kaplowitz of Citigroup. Please proceed with your question.

Andrew Kaplowitz

Hey good morning guys.

Earl Austin

Good morning.

Andrew Kaplowitz

Duke, 9% margin in pipeline and industrial is the highest we've seen since I think 2014 and we know it's a seasonably strong quarter for you. You talked about the reasons why margin's higher now. but does this give you more confidence that margin in 2020 could get a lot closer to that 8% to 10% margin goal you have for that segment, given the positive mix that comes from Hallen as well? Is there anything other than weather that stands in your way for a significant step-up in that margin moving forward?

Earl Austin

Yes, thanks for the comments. When we look at the pipeline and industrial segment, I think what you've seen us, and we've been consistent over the past three years talking about strategy there to build that base business up, continue to be more repeatable and sustainable. And that's what you're seeing here, broad-based beat on the quarter. And I do think as we move forward, we'll continue to get better and continue to get up in the upper single-digit-type ranges going into next year.

So, I think it is our seasonal quarter that is high for us. We, like I said, we executed through from Stronghold all the way through our big pipe, really nice quarter. It's something for us that we continue to see this. We've seen it for a long time and our strategy that we're making the right decisions in the field from a scalability standpoint and our expansions. How far we can go will depend on the markets in the northeast with our acquisition of Hallen as well as what we do when we book big pipe in the next year. So, we'll give commentary a little deeper there when we give our 2020 guidance.

Andrew Kaplowitz

That's helpful. And then can you give us some more color on the impact of Canada and particularly California utilization on Electric Power? Kind of seems relatively self-explanatory, utilization get better as large transmission projects ramp up. But are the utilities in California pushing off work there because of how difficult the season has been? Because I would have thought that there would too much work for you there now and the growth in that region will be the highest in your businesses.

Earl Austin

So, California is our biggest state. It's extremely complicated when you start talking about that amount of resources with the fires. And first of all, our main concern is make sure the safety of our people and also make sure that we're supporting our clients in a manner that's efficient. And so when we think about it -- when you think about these resources and resource ramp-up, utilization plays a big role there.

And we're in fire areas; obviously we shut down some of the areas. We have some crew movements in the quarter. We've worked really hard with all of our clients in California to make sure we're supporting them all in this. I think this is a long-term fire hardening approach, somewhat what you've seen from the hurricanes in the southeast in California now with the fires even in the west.

So, it's not just California, it's all of us. It has drained a lot of the cross-skilled labor resources out of the country into California. It's a big place for us. We're right in the middle of it. We're supporting them across the board. The quarter was a little inefficient. I do think that will work out.

We've taken a prudent approach to guidance, but it's a long-term build there and certainly, something that we're right in the middle of it as we go forward with planning and things like that. From that standpoint, we really like the business there long-term. We're just getting through some of the strife of the season here as you see on the news.

Andrew Kaplowitz

To be clear, you're actually hiring in California, right? You can't get enough resources there. It's just all that's going on in there, correct?

Earl Austin

We're hiring across the Board. If you look at our employee count for the quarter, we're up 4,000 quarter-over-quarter.

Operator

Thank you. Our next question is from the line of Jamie Cook with Credit Suisse. Please proceed with your question.

Jamie Cook

Hi, good morning and congratulations on the pipeline and industrial margins. I've been waiting for this quarter for some period of time. I guess first just to follow-up on Andy's questions on the sustainability of these margins. I think you said next year, you target or whatever, upper single-digit. I mean what are your assumptions on that in terms of is that based on stuff you have to win? And I'm trying to understand how much of the acquisition that you did in the quarter is also sort of really helping margins, or if any of this is pricing scale, so just more color there.

And then my second question also as we shift to 2020, obviously you talked about free cash flow improvement in the fourth quarter. But is there any sort of structural improvements we can think about in the cash flow as we exit 2019? Thanks.

Earl Austin

Yes, Jamie, I'll out talk about the P&L margins. And we're not in a position to give 2020 guidance at this point. But what I will say is we incrementally get better. And I do believe we can operate in the upper single-digit margins the base business alone can operate there.

So, in my mind, we continue to get better and we'll operate better. We don't know all the synergies are, but I know there synergies there an expansion in the northeast will certainly be accretive to the segment. So, when we think about it, that's how we think about it going into next year. It's too early to say how much big pipe we can book, but we have said on a consolidated basis, we can grow the company next year. And 85% to 90% of that base business over a three-year period, we think we can grow kind of mid to upper single-digit.

So, we're giving you pretty good guidance on what we see from CapEx and OpEx of our utility customers, which is the very base of the whole company. And also we'll stack on the larger projects as we have in the past. And we'll be able to formulate what I believe is extremely good guidance going into 2020. We'll do it in February.

Derrick Jensen

Yes, Jamie, relative to the free cash flow dynamic, 2019, we had a larger growth through the year compared to our original guidance at the beginning of the year. And as you know, the dynamics of that revenue growth is draw of working capital. So that creates largest portion of fluctuation for the extent going into 2020. Duke commented about confidence in consolidated revenue growth.

To that end, I think what we see is that will have a very somewhat comparable draw of working capital historically. We run about 15% working capital trailing 12 months. You just kind of think about it going in 2020.

On the aspect of dynamics of changes, DSO put a lot of pressure here through the third quarter. I talked about that as far as some of the billing dynamics. I think it improves a little coming into fourth. In 2020, I don't think that continues to linger. I think we'll be able to see improvements in DSOs more trending towards kind of historical levels.

Jamie Cook

All righty. Thank you. I'll get back in queue.

Operator

The next question is from the line of Sean Eastman of KeyBanc Capital Markets. Please proceed with your question.

Sean Eastman

Hi team. Nice quarter. Thanks for taking my questions. I wanted to start on the Electric Power margins. So, it looks like you guys will actually have three good-sized transmission projects all running at the same time in Canada starting in 2020. It would just be great if you could give some color on how powerful that Canada utilization uptake could be as we look out the next year. Are you able to quantify what may be the relatively low Canada utilization drag on electric is this year? Or any way to approach that kind of dynamic would be great.

Earl Austin

Sure. When we look at Canada for the quarter, even for the year, they're somewhat down off West McMurray. We knew we were booking big work in the fourth quarter. We do have some drag in inefficiency with people and equipment and utilizations in Canada for even the year.

That being said, I think with Watay and some things moving along there, it stabilizes our Canadian market for the next 24 to 36 months, which gives as an anchor to grow our base business and do some other things there. So, we really like the margin profile going into 2020 and beyond, which will stabilize Canada and be accretive to what it was at this year for sure.

And it's continually -- we continually say and I'll say it again, we'll operate in this segment double-digit margins. We will over time. We'll have some quarters, we'll have some periods where it'll be 9.7, and you'll see it bump in to 10.3. So it's going to operate in that space.

I've said it over and over and I continue to stand by the segment has over time. No matter if its large transmission, small transmission, operated in double-digits, and that's our expectation going forward.

Sean Eastman

Great. It was nice to see you guys close on solidly accretive acquisitions this quarter. Can you maybe give as an update on how the pipeline targets looks out there? Do you think we can see another Hallen [Indiscernible] transaction in the near-term? Maybe you guys prefer the buyback in the near-term, or maybe you want to pay down some leverage, any color there would be great.

Earl Austin

Sure. When we look at Hallen, it's a great company. It's been in business since 1935. We worked on that for over two years. So, that was u s and that team and that management team working together. They want to be a part of Quanta. We wanted them to be a part of us. They fit really nicely into our strategy.

I want to say that our strategy is long-term and we've been working on this strategy for three and a half years. It's not a transformation. It's certainly something that's core to us to find great companies with the right culture. We're selective in how we go about it.

Certainly, there's companies out there that fit. And as we go forward, we have a strategy. You've seen is implement it. You've seen our uses of cash. We'll be opportunistic on how we do that, both from a company standpoint. We do have some growth -- organic growth.

So, one of the things we think it's a misnomer is our company, albeit we all believe is a management team of value, it's certainly a growth company in our mind as well. We're putting it up, we're showing the growth and you'll see it over time. So, from our standpoint, we'll continue to be opportunistic with cash and look for the best way to drive shareholder value.

Operator

Thank you. The next question comes from the line of Noelle Dilts of Stifel. Please proceed with your question.

Noelle Dilts

Hi, good morning and congratulations on a nice quarter.

Earl Austin

Thank you, Noelle.

Noelle Dilts

So, my first question, I think in your prepared remarks, you mentioned that you're seeing strengthening in the midstream market. And I think you've heard more cautious views out of some of the MLPs and developers and just general concern that there might be a little more conservative of cash. So, it was encouraging to hear those remarks.

I was wondering first if you have any thoughts on sort of what you're seeing in the market versus some of that commentary and what's giving you some confidence in the 2020 outlook?

Earl Austin

So, when we look at -- first of all, midstream market, when we look at our markets and what we're doing, it's a small piece of our pipeline segments. So, I'll just say just in our areas of the Canadian markets as well as some of the basins of that we're in on the midstream side; we do see some projects moving there.

So, I think you build a lot of big pipe over the last four, five years and you will come back in. We said it all along you'll start to see midstream pick up to fill up the pipe. LNG exports and things like that going on. There's still drilling places. In our mind, you'll continue to see that midstream be there for the foreseeable future.

That being said, we still see projects. And obviously price of all of things of that nature affect drilling, there's no doubt about it. It is cyclical on the drilling side. But the pipe side there's multiple projects. The opportunities are there backing up LNG and others. So, we're optimistic that we'll book our fair share of work into big pipe as well going into next year.

And when you look at the confidence in what we're saying, we said it over and over again that we will building a repeatable, sustainable segment. And that was our strategy three and a half years ago. That's backed up by 30-year builds of what we're seeing on distribution side of cast iron, steel replacements, large things all over the big programmatic spends much larger than things you're seeing on one piece of the pipe.

And from a permitting standpoint, from a regulatory standpoint, it's certainly more efficient for us and we can certainly guide better on those areas. So, those things are really stabilizing that segment and give us confidence that we can move up from a margin standpoint as well as giving good certainty that's a repeatable, sustainable segment.

Noelle Dilts

Thanks. That's really helpful. And then on telecom, any changes on how you're thinking about the timing of some of the opportunity here in the U.S. are the trajectory of span? I understand you're a player and there's huge opportunity to grow. But overall when you think about the market, any changes in your thinking?

Earl Austin

No, the macro market in telecom business is certainly there. We'll be smart about how we enter areas and things like that where I think we play a unique role as 5G and the small cell deployment. As it relates to the electric distribution as it comes on systems, it's more efficient for that infrastructure. It's against density to be put on distribution, electric distribution facilities, we play a unique gap -- we bridge the gap there between the carrier and the utility, which I think that looks substantial as we go forward.

And the fiber behind it, everybody's trying to get closer to the customer with data and I think you'll start to see the 5G platform as they develop technology and things that gets the platform, the infrastructure that we see today will not supportive.

So, in my mind, technology and how it is forward will drive the infrastructure build as it has in the past. So, you're going to start to see that and I think the telecommunications and where we sit there, we play and I's unique role and the macro just macro market is good. We'll be patient and systematic about it.

Like we said, we added 4,000 employees. We are really concerned that we made sure from a safety standpoint and from an execution standpoint that we execute properly in the field. And we'll pace that growth. I would expect the telecom to grow similar numbers that we have this year ex-Peru.

Operator

Thank you. Our next question is from the line of Chad Dillard of Deutsche Bank. Please proceed with your question.

Chad Dillard

Hi, food morning guys.

Earl Austin

Good morning Chad.

Chad Dillard

So, I just wanted to understand the cadence in transmission business. I think ensuring volume to 2020. Just trying to think through the impact of costs absorption from Fort McMurray rolling off, but at the same time, some of the new transmission projects, large projects in Canada starting to ramp up. Just given that, I think it tends to be a more first half-weighted opportunity. How do we think about just cadence in 2020?

Earl Austin

Yes, I mean I think as I said in the past, I think the segment itself will grow. I also think it will certainly operate in double-digit margins or have the opportunity there over time. And for sure this segment will. Canada plays a big part in that. I believe if you look at the U.S. margins this year in the segment, they're double-digits.

So, Canada is somewhat of a small drag, albeit last year with Fort McMurray, it was accretive. So, when I think about it over time, Canada is more project-based. And when we come off a large project and we know we are going into another large project, which if you look at Watay and East-West Tie together, it's over $1.5 billion worth of work. So, over the next 24 to 36 months when we look at that, we will making sure we have resources and we're making sure we have the people there that are qualified to start building that.

It is somewhat the climb there allows us to work more in winter when it freezes. It's hard to predict when it does freeze. So, that being said, it will have some cyclicality from a seasonality standpoint. When you have breakups certainly in your third quarter, it's countercyclical to the segment. So, in our mind, it's very, very good for Canada to be moving forward with these larger projects.

Chad Dillard

Got it. And then just on telecoms, can you just talk about what you're seeing in the ramp on 5G fiber? Because last 12 months compared to the next 12 months will look like in terms of your revenue growth keeping all that stuff?

Earl Austin

I think 5G is a platform. As you look at that platform and what it can do, it's really -- latency goes way down. High speeds as software develops against that and other things develop against that, you'll see more and more fiber. Everyone will want to get closer to the customer. And we continue to see that and the infrastructure in place today won't support the platform.

So, what you'll see as you continue to see our carriers develop the infrastructure behind the platform and that's what we see today. How fast they do it will depend on demand and as you see people want more demand, high-speed, we certainly think the generation that people want readily available data and that will only happen with the platform and the amount of fiber in data centers and things like that are in place to get to the customer quicker. So, it will continue to move forward. I think the denser it gets into the communities and into the suburbia will only broaden out the amount of work we do.

Operator

Thank you. Our next question comes from the line of Blake Hirschman with Stephens. Please proceed with your question.

Blake Hirschman

Yes, good morning guys.

Earl Austin

Good morning.

Blake Hirschman

Apologies if I missed it. But is there any update to kind of call out on the situation down in Peru. Has anything really changed since the last call?

Earl Austin

So, I think we were silent by design. It's really from our standpoint; we said we believe we ring-fenced it. We're certainly in conversations with the government there. We stay in conversations. We're handing over the network as promised. We are doing everything from our standpoint to put us on the right side of that situation.

I do believe that we have not seen anything there that would change at all our position. We still feel very comfortable in what we've done there on and on the right side of the law and what our contract says. We're in very good shape.

I would say the geopolitical environment in LatAm is ever-changing. And we assess -- we continue to assess and ring fence it. The work we have there is small in nature and nothing would be material other than what we already talked about. We think we're handing over the Peruvian network like we're supposed to do.

So, we feel comfortable just we'll continue to work with the government and do the right thing there. So, we're in conversations. I would just say nothing's changed financially there in my mind or from a risk standpoint, other than we continue to derisk the segment -- that division.

Blake Hirschman

Got it. And on capital allocation, it doesn't look like you bought back any stock in the quarter and haven't really done much year-to-date either. Just curious is that due to just you're pretty close on these deals and ended up closing it in September?

Earl Austin

That's right. I mean I think its sources and uses of capital. We knew we were very close, to close in some acquisitions we thought, in our mind, we'll be accretive going forward. So that was where we chose to deploy capital. We are a couple of turns there. We're two turns. We want to delever and I think you'll see us do that over the next few quarters. Derrick, any comment?

Derrick Jensen

No, nothing.

Operator

Thank you. The next question is from Adam Thalhimer with Thompson Davis. Please proceed with your question.

Adam Thalhimer

Hey Duke, can you give us a better sense for the fire hardening opportunity from the west. Big picture if you think about it in next five to 10 years, what that could mean for Quanta?

Earl Austin

Look, I think when you look at it; it's hard to say what's going on there today. It's difficult for not only the consumer but the utilities to try to get their hands around what is expected and what's the expectation. It's an older grid. It needs to be modernized, we said that in the past and I think that remains.

The output is a large piece of our business in California. It depends on what they do if they start to turn around and things like that, it could really expand other than what it is, it's a large multiyear-type build. And as that -- I think it needs to stabilize for us to be able to predict. And it has now stabilized at all yet.

So, I think when it stabilizes, we'll know more about what to look for from a CapEx spend. But if you look at our customer base there, they've all announced large fire hardening programs in the last. It's not just California. It's your western states and that's consistent.

And when we think about it, it's a large build. I don't know how to put a number on it at this point, other than to say if you look at what's happened from a storm hardening standpoint in the south and southeast, even in the Eastern Seaboard, it's bigger than that.

Adam Thalhimer

I guess I don't understand this. When you talk about stabilization, you're talking about the stabilization of one large customer or are people still trying to figure out how to deal with the problem?

Earl Austin

I think it's you have a large customer in California that covers a lot of the state. But it's multiple states, multiple issues on fire and just in general. It's similar to what you saw with hurricanes when hurricanes came through. Its wind events, fire events. You can call it climate change, I'm not sure. But what I would say is the fires are more violent. They're causing more issues in California and in the West.

So, that being said, like you've seen on hurricanes, it's the same type of dynamic you have to go back in and take infrastructure that was put in 50, 60 years ago and modernize it for today's environment. And that -- we haven't done a lot of that in the West, so you'll start to see that as we move forward.

Operator

Thank you. Our next question is from the line of Alex Rygiel with B. Riley. Please proceed with your question.

Alex Rygiel

Thank you. Good morning. Nice quarter. Can you remind us what you think the free cash flow -- power of free cash flow generation is with your asset base today? And maybe if you can identify the top three uses in 2020?

Derrick Jensen

Yes, what we talked about is the growth of the base business. We continue to think that is a big driver of more repeatable, sustainable EBITDA and repeatable, sustainable cash flow.

As growth levels even at mid-single-digit on a go-forward basis on base business, at -- with those types of expectations, that would be different than just kind of double-digit growth we've had over the last several years.

We still have the opportunity for that, but when we look at about a more mid-level percentage of that growth, it gives opportunity for cash flow. I think you're looking at something along the lines of -- we talked about kind of 40% EBITDA level, 40% to 50%.

The drivers of growth, we look at how we lean into growth is always the number one place we end up putting into working capital and impacts free cash flow.

CapEx, we continue to be fairly capital-intensive. This year, we're going to have CapEx around $265 million. If I look forward, I think I would tell you somewhere in the $275 million to $300 million-type level.

And then this year with the aspect of some of these delays in billing, it puts a little bit of pressure on that. I still as I said in earlier comments with Jamie, I think those will ease up a bit, and we'll be able to see DSOs trending back down to closer to historical levels. And so to that end, -- we have the opportunity to finish very strong free cash flow over time.

Pinpoint at any individual year is always challenging for us. The starts and stops of projects, seasonal dynamics most, specifically how the storm events happen particular fourth quarter is an example, can put pushes and pulls and so we want to be mindful of those fluctuations.

Alex Rygiel

Thank you.

Operator

Our next question is coming from the line of Steven Fisher with UBS. Please proceed with your question.

Steven Fisher

Thanks. Good morning. So, these MSAs are an important part of your recurring revenues. So, I'm just curious what your funnel of new MSA agreements look like over the next few quarters for bookings opportunities. How many existing ones you have that are expiring, and how many new bids are coming up for a decision, et cetera, beyond what you have already reported for Q4.

Earl Austin

I think when look at it as part of the base business; we don't necessarily track MSAs to that level. And so when you look at it, it ebbs and flows. It just depends. Some can extend for a year, some can extend for three. It's difficult for us to pinpoint that.

What we will say is when you think about 90% of the business, a lot of that is made up of MSAs. And what we're saying there is it will go mid to upper single-digits for the foreseeable future. So, you can see that we're booking quite a bit of MSA were going forward.

We talked in the past about us, our top 20 customers there in the utility space being very sticky. And I think that remains and we're adding customers from programmatic spending and things of that nature across the Board.

Steven Fisher

Okay. And then just maybe frame what the bookings could be in Q4 from Watay and the MSA and then how much backlog was added in the third quarter from M&A.

Derrick Jensen

Yes, the M&A is roughly call it 600, 650 in total with about 400, 450 of that being kind of 12-month. And then from the standpoint of projects in the fourth quarter, we targeted in aggregate, it's over $1 billion.

Operator

Thank you. The next question will come from the line of Michael Dudas with Vertical Research. Please proceed with your question.

Michael Dudas

Good morning. Sorry about last night and thanks for squeezing me in.

Earl Austin

Well, it happens.

Michael Dudas

Just looking at going to 2020 given where your labor force stands today and again given the issues in California and shifting and moving and such, how do you feel relative to your current base of labor? What you think you might need to meet what your growth expectations are likely to be in 2020 and beyond? And is the utilization effort of that labor going to be additive to some margin improvement in both segments in 2020?

Earl Austin

I think when you look at it and when we think about it we've invested over $100 million over the past five years or so in labor and our labor force. We're very proud of that. And that's what we specialize in, this craft-skilled labor and understand the markets, we understand labor in general. And it's a collaborative approach with our trade association unions, whatever it may be.

So, I think we stood in a very nice spot to continue to access labor, train labor, get it in the field quicker, get to market quicker and be more efficient with some other things we've done with our curriculums, our colleges, things like that.

I think you'll continue to see us get more efficient on organic growth. You'll start to see it in the pipe side, the telecom side. Certainly in the power side, we continue to believe we'll operate in double-digits.

Every once in a while when you have big movements and Canadian softness there on some of those larger projects, and we're sitting on some labor, we're a little inefficient, but over time, I think that's the right way to look at it.

And if you look at double-digit kind of margins and the margin profile with the growth behind it, it's certainly something that we think we're doing a really nice job of it. It's very core to our strategy moving forward. And you continue to see us evolve and get better there on a daily basis. So, I like where we're at. I like what we're doing. And I think we'll only get better as we move into the next three to five years.

Michael Dudas

Thank you.

Operator

Thank you. The next question is from the line of Bill Newby with D.A. Davidson. Please proceed with your question.

Bill Newby

Thanks and good morning. Congrats again on a great quarter guys.

Earl Austin

Thanks.

Bill Newby

Just a couple more follow-ups on the pipeline business. I mean really good growth there, especially relative to what you guys were alluding to earlier this year. I mean, Duke, you noted the areas of strength. But I guess relative to what you guys were seeing three months ago, where's the biggest variances in the activity levels that you're seeing?

Earl Austin

Look again I think from our standpoint, our utility business in that area has certainly exceeded our expectations from our standpoint, from a broad-based beat there. We did really well with the whole segment. We did execute well in some pipe. Those projects were certainly -- have contingencies in. We worked through some of that in the quarter; it was a nice broad-based beat.

And I think going forward we continue to see that base business both from an industrial standpoint, our distribution standpoint, continue to evolve, continue to enhance our margins, to stabilize it, and restack on large projects, which we'll talk about in February.

So, we really like the seven. It's been a long-term strategy. I'm really proud of what we've done there. It wasn't easy. We certainly were hard at it. And our guys in the field and leadership should really be commended, because it's coming together and we really like what we see.

Bill Newby

Great. And then I guess as you get in the fourth quarter here on Stronghold, what are you seeing in turnaround activity? Activity in the Gulf, I think there's a pretty tough comp relative to last year. So, any thoughts there?

Earl Austin

I think when you look at Stronghold; they're doing very, very well in what they're doing. Obviously, some of the quarterly dynamics quarter-over-quarter are there. We like where they sit. We think they're doing a nice job. Some consolidation going on within that space, but very accretive to the margin profile, doing very well and quarter-over-quarter honestly, not really looking at it from that standpoint. Long-term on a yearly basis, they exceed our expectations.

Operator

Thank you. At this time, we've reached the end of the question-and-answer session. And I'll turn the call back to management for closing remarks.

Earl Austin

First, I'd like to say the California's strife there and the fires there for our people and the people that's affected; we certainly stand behind them and our customers. It's not an easy place to be. So, we want to make sure that we help them and collaborate with our customers there.

And for all the people, 46,000-plus that are in the field, we want to commend them on the safety and things they're doing to make this company great. It's their company as well, so we want to commend them.

And thank you all for participating in our third quarter conference call. We appreciate your questions and your ongoing interest in Quanta Services. Thank you. This concludes our call.

Operator

Thank you. Today's call has concluded. You may now disconnect your lines at this time.

Thank you for your participation.