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Covanta Holding Corp. (CVA)

Q1 2016 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to the Covanta Holding Corporation's First Quarter 2016 Financial Results Conference Call and Webcast. This call is being taped and a replay will be available to listen to later this morning. For the replay, please call 877-344-7529 and use the replay conference ID number of 10084165. The webcast as well as the transcript will also be archived on www.covanta.com.

At this time, for opening remarks and introductions, I'd like to turn the call over to Alan Katz, Covanta's Vice President of Investor Relations. Sir?

Alan Katz
Vice President-Investor Relations

Thank you and good morning. Welcome to Covanta's first quarter 2016 conference call. Joining me on the call today will be Steve Jones, our President and CEO; and Brad Helgeson, our CFO. We'll provide an operational and business update, review our financial results and then take your questions.

During their prepared remarks, Steve and Brad will be referencing certain slides that we prepared to supplement the audio portion of this call. Those slides can be accessed now or after the call on the Investor Relations section of our website, www.covanta.com. These prepared remarks should be listened to in conjunction with these slides.

Now, on to the Safe Harbor and other preliminary notes. The following discussion may contain forward-looking statements and our actual results may differ materially from those expectations. Information regarding factors that could cause such differences can be found in the company's reports and registration statements filed with the SEC. The content of this conference call contains time-sensitive information that is only accurate as of the date of this live broadcast, April 27, 2016.

We do not assume any obligation to update our forward-looking information unless required by law. Any redistribution, retransmission or rebroadcast of this call in any form, without the express written consent of Covanta, is prohibited. The information presented includes non-GAAP financial measures. Because these measures are not calculated in accordance with GAAP, they should not be considered in isolation from our financial statements, which have been prepared in accordance with GAAP.

For more information regarding definitions of our non-GAAP measures and how we use them, as well as the limitations as to their usefulness for comparative purposes, please see our press release, which was issued last night and was furnished to the SEC on Form 8-K.

With that, I'd like to turn the call over to our President and CEO, Steve Jones. Steve?

Stephen J. Jones

President and Chief Executive Officer

Thanks, Alan, and good morning, everyone. For those of you using the web deck, please turn to slide three. We've had a good start to the year and we're making great progress on our key initiatives. In terms of financial results, Q1 adjusted EBITDA was $76 million, a decline of $3 million from Q1 2015 and free cash flow was a negative $5 million, lower by $21 million.

The decline in adjusted EBITDA was driven largely by the impact of lower year-over-year commodity prices, accrual for variable incentive compensation and lower energy revenues from our biomass facilities, partially offset by the positive impact of growth in our Environmental Solutions business.

Free cash flow was impacted by these same factors as well as by higher maintenance CapEx as a result of increased scheduled maintenance activity in the quarter. Given the lower year-over-year power prices in 2016, note that we did more maintenance this quarter than last year.

Our financial results were in line with expectations as of our last call. And in last night's press release, we affirmed our guidance for 2016.

In terms of our strategic initiatives, we continued to grow our Environmental Solutions business with another quarter of record revenue. We also acquired another small material handling facility in Augusta, Georgia earlier this month. This will support the profiled waste programs at our Energy-from-Waste facilities in Florida, Alabama and Virginia. We completed the first step in our China asset swap and sale and are now going through the process to complete this transaction, which is the sale of equity to CITIC. We still expect to complete this process by the end of this quarter.

Our Continuous Improvement initiative is going well and we have uncovered a number of opportunities across the business. I continue to be impressed with the size of the projects that we're working on in this area.

We had a strong quarter operationally with boiler availability, energy production and metal recovery right on target. We're also in the final weeks of our heaviest maintenance period of the year and overall, things are going very well. Now let's move on to the markets and operations. I'll start with the Waste business. Please turn to slide four.

Our North American Energy-from-Waste same-store volume was flat while pricing was higher by $6 million versus Q1 2015. This was driven primarily by the impact of profiled waste.

In March, we completed a full year of service at the Queens MTS, taking waste deliveries to our Niagara and Delaware Valley facilities via rail. This contract is going well and we continue to displace lower-priced spot waste with New York City Waste in these markets as the city ramps up volumes.

Looking at our Covanta Environmental Solutions business, EfW profiled waste grew 16% this quarter compared with Q1 2015. We've completed two acquisitions so far in 2016 and the integration of the Materials Handling Facilities and Services businesses that we acquired in 2015 has gone well in terms of both cost synergies and sales force integration.

Now let's move on to energy. Please turn to slide five. As many of you have likely seen, the power markets, particularly in the Northeast, were under significant pressure in the first quarter given the mild winter and low gas prices. Average market pricing for the quarter was $28 per megawatt-hour. However, our full-year expectation is that the portfolio will likely still be around $50 per megawatt hour.

Production was in line with expectations and there have been no changes to our outlook for the full year. We did hedge a bit more for this year and for 2017, as you can see in our energy portfolio detail on slide 16.

I'll note that as expected, earlier this month, we shut down all of our biomass facilities and don't anticipate any additional biomass revenues for the remainder of the year. We'll have some minimal carrying costs moving forward which we included in our guidance. Note that we continue to look at options for these assets.

Let's spend a few minutes on the Metals business. I'm now on slide six. Market pricing continued to have a significant impact on Metals revenue year-over-year. The average price for the HMS #1 Index was $158 per ton in Q1 versus $255 per ton in the same quarter last year. However, we're starting to see some positive movements with recent HMS Index prices coming in above $200 per ton. Given the recent move in the markets, we now expect our average revenue per ton for ferrous to be between $80 and $95 for the full year.

In terms of volumes, ferrous volumes increased by 9% this quarter as a result of new recovery systems that we installed in 2015, the impact on our Fairless Hills facility and more metal in the waste stream which we believe was driven by lower market prices. This increase is after the effect of the cleaning process at Fairless which reduces volume. Non-ferrous volume increased by 6% versus Q1 2015, also driven primarily by investments made to increase recovery at certain facilities; so overall metals volumes have been very good.

Forward prices of recycled aluminum are holding steady and our outlook for the full-year non-ferrous price is unchanged at approximately $600 per ton. While we're still a ways off from historical averages, it's encouraging to see some price support in the ferrous market.

Now let's move on to operating expense and CapEx. Please turn to slide seven. Total EfW maintenance spend in the quarter, including both expense and CapEx, was up 19% versus Q1 2015. As I mentioned, this increase was primarily the result of a relatively lighter outage scope in Q1 last year in an effort to capture higher power prices. Our outlook for the full year Energy-from-Waste maintenance spend is unchanged at $350 million to $370 million.

We completed about a third of our total expected maintenance spend in Q1 and will complete another 30% in Q2, very much on track in terms of – we're very much on track in terms of our full-year maintenance spend.

North American Energy-from-Waste other plant operation expenses were down 1% on a same-store basis this quarter compared with Q1 2015, primarily due to cost savings from our Continuous Improvement initiatives.

We've been reducing the amount of fuel and other chemicals used in our processes and this has had a favorable impact on costs. This is a classic example of Continuous Improvement productivity.

I'll wrap up with some thoughts on our business outlook for the rest of this year and beyond. Our core business is running extremely well. While the commodity markets continue to be volatile, we're focusing on things that we can control. We're generating record revenue on profiled waste and continuing to build out our Environmental Solutions platform. Our Continuous Improvement effort is moving ahead nicely.

In terms of growth projects, Dublin is coming along very well, with construction approximately 60% complete. We're currently installing the stoker, boiler and air pollution control equipment. We still expect to have first fire by this time next year and are on track for commercial operations by the fourth quarter of 2017.

We also continue to look for other growth opportunities both here in the U.S. and abroad. One of these, Perth, which we discussed a bit at our Analyst Day, is still in the development stage. We're looking closely at the cost of construction and the contracts and should come to a conclusion on whether we want to move ahead with this project in the next several months. There are a number of other opportunities that are in the pipeline for expansions, newbuilds and growth within the Environmental Solutions business. We're off to a great start for the year and I continue to be excited about the avenues for growth that I see for this business.

With that, I'll turn the call over to Brad to discuss the first quarter results in more detail.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

Thanks, Steve. Good morning, everyone.

I'll begin my review of our first quarter 2016 financial performance with revenue on slide nine. Revenue was $403 million, up $20 million versus Q1 2015. North America Energy-from-Waste revenue declined $5 million year-over-year on a same-store basis. Within that amount, waste and service revenue increased by $5 million, with higher average revenue per ton driven by the continued growth of profiled waste volume, as well as contractual escalation. Energy revenue declined by $3 million and recycled metal revenue declined by $7 million, both driven by lower year-over-year market prices.

North America EfW contract transitions were a net positive $3 million year-over-year, with two months of benefit from our Fairfax facility, now operating under a tip fee contract structure, partially offset by lower debt service revenue.

Outside of North America EfW operations, the Environmental Solutions business was up $16 million, primarily as a result of the acquisitions that we completed in 2015. All other operations netted to a $6 million increase, with higher year-over-year service fee revenue from the New York City MTS contract, partially offset by lower biomass revenue. As Steve mentioned, we're no longer operating any of the biomass facilities given the economics in the current energy price environment.

Moving on to slide 10. Adjusted EBITDA was $76 million in Q1 2016 compared to $79 million in Q1 2015. The year-over-year decline was driven by lower energy and recycled metal prices in the North America EfW portfolio, which reduced adjusted EBITDA by $10 million on a same-store basis. Contract transitions added $1 million to adjusted EBITDA in the quarter, with the Fairfax transition partially offset by lower debt service revenue.

New business, including the New York City MTS contract which commenced towards the end of the first quarter last year and acquisitions in the Environmental Solutions business, together added $8 million to adjusted EBITDA in the quarter. The other significant impact in the quarter when compared to the prior year was the relatively heavier scheduled maintenance outage calendar, which Steve discussed.

Turning to slide 11, free cash flow was negative $5 million in the first quarter compared to positive $16 million in the prior year. This was driven by the operational factors that impacted adjusted EBITDA in the quarter, totaling $3 million, higher maintenance CapEx of $10 million year-over-year and higher cash payments for interest and taxes, totaling $5 million. Cash flow from working capital was similar to the same period in 2015.

The first quarter is often a seasonal low point for cash flow and free cash flow can sometimes be negative in a given quarter depending on maintenance activity, as we had this quarter, or working capital movements, as we've seen in the past. In any event, these are seasonal and timing factors and therefore nothing should be extrapolated from this for our full-year outlook. Our expectations for full-year free cash flow are unchanged as we affirmed in yesterday's press release.

Our growth investment outlook, which is detailed on slide 12, is unchanged for the year. We invested $14 million in organic growth projects in the first quarter primarily related to metal recovery systems and some investments in new equipment for the Environmental Solutions business. Investments in the infrastructure to support the New York City MTS contract and in the emissions control system at the Essex County facility are on track as expected, as was our Dublin spend this quarter. As Steve mentioned, the Dublin facility construction is progressing well.

Turning to slide 13, I'll quickly touch on our balance sheet and leverage ratios. Net debt increased in Q1 to $2.4 billion versus $2.3 billion at the end of 2015, resulting from further drawdown of the Dublin facility project debt and seasonal revolver borrowings. The net-debt-to-adjusted-EBITDA ratio for Q1 was 5.7 times.

As I've discussed in the past, we expect leverage to remain elevated until we begin to realize contribution from the Dublin project, after which we expect leverage to trend lower as we seek to return to our long-term target of approximately four times.

The calculation of the leverage ratio covenant under our senior secured credit facility was 3.1 times at March 31 versus the covenant limit of four times. Remember, this ratio isn't impacted by the increased leverage from Dublin as that non-recourse debt is excluded from the calculation during facility construction. So even though our consolidated metrics are elevated for the time being, we remain well within our debt covenants as we move through this period in our investment cycle.

In conclusion, I'll quickly reiterate the theme of Steve's commentary. 2016 is off to a very strong start in the execution of our strategic, operating and financial objectives for this year and beyond.

And with that, let's open up the line for questions.

QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] Our first question comes from Tyler Brown of Raymond James. Please go ahead.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Hey. Good morning, guys. Nice start to the year.

Stephen J. Jones
President and Chief Executive Officer

A

Thanks, Tyler.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Hey, Steve, so we've been working on Continuous Improvement now for the better part of a year. You guys have added some talent there to really drive the cadence. It sounds like you've been successful, but can you guys talk a little bit about what types of projects are in that opportunity stack? Secondly, maybe are those initiatives here in the beginning targeted at the tip fee fleet? And three, do you still believe that there's annually maybe $10 million to $15 million of annual cost saves out there over the next couple of years?

Stephen J. Jones
President and Chief Executive Officer

A

Yes. Sure, Tyler. We're working on a number of different projects. I'd say the four biggest buckets are really around outage optimization because when you spend $350 million to $370 million a year on outages, I think there's efficiencies that can occur there. Stable operations, which is – you've probably heard me talk about this before. This is basically having your best – it's as if you had your best operator on your control board every minute of the day and so we're working on that. We're looking at reagent optimization, which is really kind of the chemicals that we use in the plant and then lastly, boiler fouling. All of those buckets are much higher benefits than I've been used to in the past. So since we're in early stages of Continuous Improvement, the returns are kind of bigger buckets of savings at this point.

And it's, like, some of these like stable ops, the savings in 2016, we're looking at upwards to $1 million of savings in 2016, for example. And so, we have about seven or eight people on the team right now. Some of those – most of those have black – folks are black-belt qualified already. And as we're projecting out through 2016, we're still seeing that $10 million to $15 million benefit rolling through the P&L. So things have been going very well from that perspective. It's still early on. Realize that when you start these programs, there's a lot of data gathering and work that needs to be done. So I'd still say it's early in the process, even though I've been talking about it for about a year. It's still relatively early in the process, but I am very encouraged by the size of the projects that we're uncovering.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

And Tyler, yes, sorry. Just to answer I think one other part of your question; that the focus here, certainly initially, is on the larger tip fee facilities.

Stephen J. Jones
President and Chief Executive Officer

A

Yeah. Good point. You're right about that.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Okay. Okay. Great color. And then, Brad – excuse me – from a modeling – for modeling purposes, so as biomass completely shuts down and China kind of eventually goes away, will the total plant operating expense, ex-maintenance, will that actually decline sequentially, call it, into a new baseline into Q2 or Q3?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

It should. Yes.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Okay.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

Yeah. And that's all else being equal. Yeah.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Yeah. Okay. Perfect. And then just lastly under the current kind of knee-pool environment, can you guys talk even at a high level about how we should be thinking about PPA expirations in 2017 and maybe what that looks like from an EBITDA headwind?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

Yeah. Based on the forward prices that we observe in the market today up there, we'd expect a pretty meaningful hit to us in 2017, as we've talked about in the past. We're still a little bit away from it, but we're probably in the $20 million to $25 million EBITDA impact next year.

Patrick Tyler Brown
Raymond James & Associates, Inc.

Q

Okay. All right. Perfect. Thank you very much.

Operator: And our next question comes from Andrew Buscaglia of Credit Suisse. Please go ahead.

Andrew E. Buscaglia
Credit Suisse Securities (USA) LLC (Broker)

Q

Hey, guys. Thanks for taking my question.

Stephen J. Jones
President and Chief Executive Officer

A

Hey, Andrew.

Andrew E. Buscaglia
Credit Suisse Securities (USA) LLC (Broker)

Q

Can you touch on – you had some interesting commentary. It sounds like profiled waste in your Environmental Solutions Group is really starting to gain some traction. Can you talk a little bit about your expectations this year for further M&A growth on that side of things and where you see that shaking out for the full year?

Stephen J. Jones
President and Chief Executive Officer

A

Yeah. So I mean I'm really pleased with this business. It's been growing well. You heard the profiled waste going into the Energy-from-Waste facilities is up 16% kind of year-on-year. That continued to be really nice growth. The tip fees in this area are better than municipal solid waste. We've talked about that before. You can get two or three times higher tip fees; so we'll continue to focus on this area.

As we – M&A going forward, we're still looking for opportunities. With other calls on our capital and the fact that commodity pricing is low, we're being careful on how we put our capital to use. But if we can find good opportunities that have the returns similar to the returns we've been getting on the assets we've already bought or the businesses we've already bought, we'll certainly look at those.

And quite frankly, one of the things – we grew quicker than I'd anticipated. Brad and I both have said, if you'd asked us a year and a half ago, would we have had this many acquisitions so far, we wouldn't have said this number. So one of the things I've really asked the team to look at is let's focus on integration as we go through 2016 and make sure that we're getting all the benefits we can out of the assets that we – and the businesses that we've already bought. But we're still looking in the market, to answer your question.

Andrew E. Buscaglia
Credit Suisse Securities (USA) LLC (Broker)

Q

Okay. Yeah. That's helpful. And then if you could just touch on the impairment charge in the quarter, you didn't mention it, I don't think, in the prepared remarks. But are there any other things like that out there that you're looking at that we could see in the future? Is there anything else that you'd like to talk about at this time?

Stephen J. Jones
President and Chief Executive Officer

A

Well, if you look at – and – if you look at the impairment charge, it was related to an Energy-from-Waste facility where we basically have told the customer that we triggered the termination right. I don't see a lot of those out there. In this particular case, we really weren't making that much money for the operating work that we've been doing.

And one of the things I've been telling the team here is I'm not really worried about size. So having a certain number of Energy-from-Waste facilities isn't important to me. It's really about whether we're getting paid for the work that we do. And I think in this case, we, as a team, looked at this and said, we're really not getting the kind of returns on the work that we're doing there. So we've triggered that termination right and then took the – and then the impairment occurred. So again, I don't – there's not a lot of those out there; but you'll see us being kind of more rigorous as time goes on about whether we're getting the right margins on the efforts that we put out there.

Andrew E. Buscaglia
Credit Suisse Securities (USA) LLC (Broker)

Q

All right. Thanks, guys.

Stephen J. Jones
President and Chief Executive Officer

A

Sure.

Operator: And our next question comes from Noah Kaye of Oppenheimer & Company. Please go ahead.

Noah Kaye
Oppenheimer & Co., Inc. (Broker)

Q

Good morning. Maybe we can start with the pipeline of project opportunities. You mentioned Perth this morning and you talked about other projects in Australia before, China, saying they're going to build 300 new waste to energy plants in the next several years, EU's circular economy package and many member states having to move away from landfilling. It just seems like there's a more supportive environment internationally at this point for waste to energy facilities. And so I was wondering if kind of in light of that, you could talk about maybe how you see the pipeline and the set of opportunities now versus a year or so ago?

Stephen J. Jones
President and Chief Executive Officer

A

Yeah. It's interesting, there are some expansions in the U.S. and we've talked a little bit about those; there's a couple of expansions around. But you're right, Noah, the regulatory support and climate for Energy-from-Waste outside the U.S. is better than inside the U.S. and so there's opportunities – I think at our Investor Day, we talked about we like to do kind of a new plant every other year. We're trying to get the pipeline filled from that perspective; so we add Durham York this year, Dublin next year, and then we're looking at Perth. Are we able to do Perth at returns that we think are reasonable based on the risk associated with the project. We're going to be continuing to look at Australia. I mentioned China. The 13th Five-Year Plan, which came out a month or so ago was very supportive of energy from waste, so there's a number of opportunities there. We'll look at the EU; obviously, putting Dublin in the ground gives us a nice bulkhead to do other things in the EU. So we're working on a number of projects.

I'm a little reluctant to do project development in the public domain for competitive reasons. So rest assured, we've got a lot going on. And I think in the past, we were working a little bit and maybe focused a little bit more on kind of the transitions that were occurring in the U.S. Most of those are behind us; so I think the team did a nice job here of getting those transitions behind us and the mark-to-market behind us. And so now we're able to focus a little bit more on business development and growth. And you see that in Energy-from-Waste facilities, you're also seeing that in the profiled waste business.

Noah Kaye
Oppenheimer & Co., Inc. (Broker)

Q

Okay. Very helpful. And then maybe just a follow-up question for me on the profiled waste; again, really nice growth, 16% as you said year-over-year.

Stephen J. Jones
President and Chief Executive Officer

A

Yes.

Noah Kaye
Oppenheimer & Co., Inc. (Broker)
Q

And it seems like more of the waste that you're getting in that is really being driven by sustainability concerns from corporate participants. I was wondering if you could talk about that trend, maybe how you're seeing the mix of profiled waste shift a little bit and some of the initiatives that you have to kind of keep that growing. Thanks.

Stephen J. Jones
President and Chief Executive Officer
A

Yes. Sure. And I've talked about this in the past. You're seeing a lot of companies now want to go to zero waste to landfill. And then I mentioned even New York City, the mayor there has mentioned that. So that's tending to drive the profiled waste business as companies try to meet their sustainability goals and zero waste to landfill goals. They're coming to companies like Covanta in order to get a sustainable solution for their waste. And that's continuing to grow. One of the things we've done around that is we're building that business out. You've seen the growth associated with that. We're adding salespeople. We've got a much greater focus on that marketplace now.

And we're also working with our plant operations folks to be able to take that waste safely and reliably into our Energy-from-Waste facility. So there's a lot of work underway. But a few years back, we saw this as a trend that's occurring with corporations. And that's what's driving the U.S. really is – it's not governments driving the U.S. in Energy-from-Waste, it's corporations who want to not utilize landfills because – and you've heard me say this, putting your waste in landfills is not a great alternative. It creates a lot of greenhouse gas, a large greenhouse gas impact. And I think companies are really starting to embrace that; that's driving the business.

Noah Kaye
Oppenheimer & Co., Inc. (Broker)
Q

Okay. Thanks so much. Appreciate it.

Stephen J. Jones
President and Chief Executive Officer
A

Thanks, Noah.

Operator: And our next question comes from Michael Hoffman of Stifel. Please go ahead.

Michael Hoffman
Stifel, Nicolaus & Co., Inc.
Q

Hey, thank you, Steve and Brad, for taking my questions.

Stephen J. Jones
President and Chief Executive Officer
A

Go ahead, Michael.

Michael Hoffman
Stifel, Nicolaus & Co., Inc.
Q

On gross margins, you've had a mix shift because of profiled waste, well mostly from energy solutions and contract revisions that have had the margins coming down. At what point do we see the benefit of Six Sigma from the mix shift having stabilized and this margin compression arrests, how do you see that time-wise?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

Yeah. It's a – hey, Michael. It's Brad.

Michael Hoffman
Stifel, Nicolaus & Co., Inc.

Q

Hi, Brad.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

It's a difficult question to answer with precision just because there are a number of variables in play, so one of the variables being the rate at which we continue to add revenue; that is service type revenue in the Environmental Solutions business. Commodity prices obviously impact that significantly. Commodity prices come with 100% margin either for better or worse. Continuous Improvement, we talked about a benefit which we baked into our guidance for this year of $10 million total between revenue and costs, though that's likely to be more weighted towards cost and that's something that we would expect to continue to grow over time. Certainly that's our goal. But it's something that's very difficult to pinpoint that given all of those variables, that by the fourth quarter this year or second quarter next year, you'll be able to really see Continuous Improvement specifically driving the margin from x to y.

Michael Hoffman
Stifel, Nicolaus & Co., Inc.

Q

Okay. I get all that. But you're the quintessential modeler. You love doing this. So in your mind, when do you think you – if all things being equal, we live with the conditions you have for pricing in your metals, electricity, the mix you have today, this is a – the margin issue settles out here in this next 12 months?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

It's another big factor actually, as I answer that question, that when you think about the consolidated total that will come into play later next year is of course the Dublin project...

Stephen J. Jones
President and Chief Executive Officer

A

Dublin.

Michael Hoffman
Stifel, Nicolaus & Co., Inc.

Q

Yeah.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President

A

...which comes in at a very, very high margin. So that'll be a significant mix shift. So you throw all that in the pot and stir it around, I would say that by the end of next year and certainly into 2018, you're going to see a much different margin profile.

Michael Hoffman
Stifel, Nicolaus & Co., Inc. Q

Okay. So talked about capital and capital deployment. How would you frame the return characteristics of profiled waste spending and Environmental Solutions spending at this point in the cycle of that – the growth of those business?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President A

Yeah. We look at whether we're buying a $500,000 shredder in one of our new Environmental Solutions facilities or we're investing in a new Energy-from-Waste facility, we look at the return the same way and everything sort of needs to stack up to the same benchmarks. And so on that basis, we're seeing the investments, both in the acquisitions and then especially to the extent that there are opportunities for add-on, more organic growth-type investments into the businesses that we acquire, we're looking at returns, cash-on-cash, IRR on the assets of low- to mid-teens. And those – it's still relatively early days. I want to give it that caveat. But I would say that the early returns are certainly favorable to our initial expectations in our models when we justified the investments.

Michael Hoffman
Stifel, Nicolaus & Co., Inc. Q

Okay. Thank you on that. And then on capital spending, $86 million is what's in the cash flow statement on page seven of your PowerPoint. It's – $36 million is maintenance. You get to page 12, it talks about the growth. It shows $59 million, but if you do $36 million out of $86 million, that's $50 million. So how do I reconcile what I'm – my modeling for that growth spending from a cash standpoint?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President A

Maybe rather than getting into it here, why don't we – let's take that offline and make sure we get the reconciliation exactly the way you want to look at it.

Michael Hoffman
Stifel, Nicolaus & Co., Inc. Q

Okay. Great. Thank you very much.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President A

Thank you.

Stephen J. Jones
President and Chief Executive Officer A

Thanks, Michael.

Operator: And our next question comes from Scott Levine of Imperial Capital. Please go ahead.

Scott Justin Levine
Imperial Capital LLC
Q

Hey. Good morning, guys.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Good morning, Scott.

Stephen J. Jones
President and Chief Executive Officer
A

Good morning.

Scott Justin Levine
Imperial Capital LLC
Q

Just running through the various assumptions for 2016 guidance and comparing them to what you had in your slides for the fourth quarter, looks like obviously, you're raising the metals assumption for revenue by $5 million give or take. It looks like you're leaving the energy revenue or the assumption – the revenue assumptions and the pricing intact. Just wondering whether, based on the 1Q results coming in relative to your expectations, if we should be moving up within the range or whether there are some offsets that we should be taking into consideration. Just trying to – it's pretty wide guidance – just trying to get your – some additional color behind where we should be favoring within the range, if you can provide it.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Yeah. On Energy, we're slightly negative to where we were when we looked at the forward prices when we gave guidance. And that's reflected in the updated – we didn't update the overall ranges because the change isn't, I think, significant enough to justify changing the range. But you can see that in our expectation for a lower market price and also actually lower average hedge price for the balance of 2016. So I'd say prices overall have weakened by – on the order of a few million dollars relative to where we were. But again, it's still well within the range that we talked about, so not worth changing the outlook.

Scott Justin Levine
Imperial Capital LLC
Q

Fair enough. And – go ahead.

Alan Katz
Vice President-Investor Relations
A

I would just say that there's the offsetting factor on the Metals side of things. We did tweak the range there as well and the two pretty much offset each other.

Scott Justin Levine
Imperial Capital LLC
Q

And given where you've come in for Q1, should we – and the fact that you're pulling forward some of the planned maintenance, any changes in seasonality we should expect for the second quarter or maybe as the year progresses, based on the way Q1 came in or not meaningful as well?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Not meaningfully. And when I say not meaningfully, to put it in perspective, if we talk about a percentage one way or the other of our spend on maintenance, it's $4 million; that could come right before a quarter end or after a quarter end. So there is going to be just natural variability. And I think our outlook for the first half is going to be consistent with – generally consistent with history, which has been 60% to 65% of our maintenance spend, both expense and capital in the first half. As Steve talked about and as you've seen in the numbers, relative to last year, we had a little bit more of that in the first quarter, so we'll have a little bit less probably in the second quarter. But again, it's really the – it's the first half versus the second half that's really what drives it. And again, we'll be in that 60% to 65% range.

Scott Justin Levine
Imperial Capital LLC
Q

Gotcha. One last one, if I may, on Environmental and profiled waste. Firstly, would you be willing to share – I don't know if you shared – how large is the profiled waste business in terms of revenue at this point?

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Yeah. We did about $80 million last year and we are targeting to do – and this is just profiled waste in the Energy – into the Energy-from-Waste plants. We're targeting to do close to $100 million this year, so about a 15% year-over-year increase.

Scott Justin Levine
Imperial Capital LLC
Q

Got it. And then the acquisitions, Chief and then the latest purchase from U.S. Ecology, could you quantify the revenue earnings associated with that? Are they relatively small? Or any additional color there.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Yeah. They're so small. I mean we haven't talked about the individual contribution of any of these acquisitions. And these, together, were less than $10 million purchase price. All I would say that the multiple that we have talked about that we're achieving on these going into the investment of about seven times, I would say that's a fair assumption on these as well.

Scott Justin Levine
Imperial Capital LLC
Q

Very good. Thanks, Brad.

Operator: And our next question comes from Dan Mannes from Avondale Partners. Please go ahead.

Daniel Mannes
Avondale Partners LLC
Q

Thanks. Morning, everyone.

Bradford J. Helgeson
Chief Financial Officer & Executive Vice President
A

Morning, Dan.

Stephen J. Jones
President and Chief Executive Officer
A

Morning, Dan.

Daniel Mannes
Avondale Partners LLC
Q

First, a follow-up on guidance, kind of to follow up on Scott's question. Maybe more on the Metals side, given that current HMS price is above your annual rate, are you maybe being conservative in terms of maybe some slippage in pricing? I don't know if you can talk through what you've baked into your guidance relative to where we are on spot HMS.

Stephen J. Jones
President and Chief Executive Officer
A

So the HMS, when it printed, was at about $183, and then it's trolled up from there. We're watching. We don't have a lot of visibility too far out. I mean you guys can look at the same numbers we can. There has been seasonality in the past, so the first quarters tended to be a little stronger. So we changed from $125 to $150 – up to $150 to $175 as our estimate for the full year and we'll kind of watch that as time goes on. And obviously, HMS is higher than that right now. And if the seasonality doesn't occur, then yeah, I think the numbers move up. But we don't have a lot of visibility on where it's going to head at this point.

Daniel Mannes
Avondale Partners LLC
Q

Got it. And I know obviously you were whipsawed there last year. So...

Stephen J. Jones
President and Chief Executive Officer
A

Yeah. Exactly.

Daniel Mannes
Avondale Partners LLC
Q

So the second thing is on New York City. Number one, is the initial MTS, is that – are you at the full run rate in the first quarter? Is there still a ramp? And secondly, could you give us any update on the Manhattan MTS?

Stephen J. Jones
President and Chief Executive Officer
A

Yeah. So 14 out of 15 boroughs are delivering waste now to the MTS and – but we're getting paid our full fee. So from an economic standpoint, consider us fully ramped, although the city is still doing some things around one of the boroughs.

And then on the Manhattan, we're still expecting probably late 2017 or early 2018 is the current expectation; so not a lot has changed there. We still haven't got our notice to – our kickoff notice at this point; so we're kind of watching the construction. You obviously can drive by – I mean the city is continuing to build that Manhattan MTS; so it's moving along.

Daniel Mannes
Avondale Partners LLC

Q

Got it. And then my last question, and this is a follow-up on a previous question about the impairment. When I look at the assets that you've generally either impaired or shut down, they've tended to be on the smaller side; 300, 400, 500 tons per day. I guess, obviously, is there – we know there is a lot of economies of scale in Waste-to-Energy. But how much of this relates to the increased cost of running older facilities and is there a risk that over time, we're going to see that threshold number move up from 300 tons, 400 tons per day to 1,000 tons per day and maybe over time a larger number of your plants are at risk or am I maybe misreading this issue a little bit?

Stephen J. Jones
President and Chief Executive Officer

A

I think you're misreading a little bit. This is a smaller plant. We're getting paid to operate the plant. We just weren't making a lot of money on it and most of our – realize this too, most of our EBITDA comes from our top 15 or so plants. So some of these smaller plants, they give us certain scale for procurement reasons and doing maintenance across a bigger fleet, but they don't have a big impact on our financial results.

Daniel Mannes
Avondale Partners LLC

Q

Understood. Thank you very much.

Stephen J. Jones
President and Chief Executive Officer

A

Sure.

Operator: And this concludes our question-and-answer session. I'd like to turn the call back over to Mr. Jones for any closing remarks.

Stephen J. Jones
President and Chief Executive Officer

Well, great. Thanks again for everyone participating in the discussion today. It's always a pleasure to talk about the business and we look forward to speaking with all of you next quarter. So thanks again and have a great day.

Operator: And thank you, sir. Today's conference has now concluded and we thank you all for attending today's presentation. You may now disconnect your lines and have a wonderful day.