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Covanta Holding Corp. (CVA)

Q4 2020 Earnings Call

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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to the Covanta Holding Corporation's Fourth Quarter and Full Year 2020 Financial Results Conference Call and Webcast. And our current webcast will be available two hours after the end of the conference call and can be accessed through the Investor Relations section of the Covanta website at www.covanta.com. The transcript will also be archived on the company's website.

At this time, for opening remarks and introductions, I'd like to turn the call over to Dan Mannes, Covanta's Vice President of Investor Relations. Please go ahead.

Daniel Mannes
Vice President-Investor Relations, Covanta Holding Corp.

Thank you, Lisa, and good morning, everyone. Welcome to Covanta's fourth quarter and full year 2020 earnings conference call. Joining me on the call today will be Mike Ranger, our President and CEO; Derek Veenhof, our COO; and Brad Helgeson, our CFO. On today's call, Mike will provide an update on the strategic review, Derek will discuss our operating performance, and Brad will provide a more detailed financial update. Afterwards, we will take your questions.

During their prepared remarks, Mike, Derek, and Brad will be referencing certain slides 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, onto the Safe Harbor and other preliminary notes. The following discussion may contain forward-looking statements and our actual results may differ materially from these 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

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this live broadcast, February 19, 2021. 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 expressed written consent of Covanta is prohibited.

The information presented includes non-GAAP financial measures. Because these measures are not calculated in accordance with US 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 limitations as to their usefulness for comparison – 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 now to turn the call over to our President and CEO, Mike Ranger. Mike?

Michael W. Ranger

President, Chief Executive Officer & Director, Covanta Holding Corp.

Thanks, Dan. Good morning, everyone. When I stepped into this role about 3.5 months ago to lead the company and the strategic review process, I brought a good perspective on the issues and opportunities given my experience with the company in similar situations. However, we did not bring a fully formed plan at that point and we committed to let our analysis and the data direct our decisions and actions.

As we announced in October, our initial focus has been an in-depth review of the company's businesses and strategies to understand where value can be unlocked and how to do so. With our efforts to-date, I see a clear opportunity to deliver more value to shareholders and we are now in the process of selecting how exactly to do just that. Allow me to lay out some of the specific objectives and initiatives.

First, we believe that some assets of the company are undervalued by the market. As such, we will evaluate the best alternatives to recognize this value. In some cases, this could result in our testing the market demand for certain parts of our business in order to capitalize on potential value differentials.

Second, in our core Waste-to-Energy business, the profitability of our operations is not uniform. A subset of our plant still drives the majority of our current cash flow. Our efforts here will be to improve asset level contributions or if not possible, we will work to exit less profitable operations. The specific levers we will use for this effort will be unique in each plant situation. But we will act decisively to reduce risk and improve cash flow. In many ways, this will be the most challenging part of the strategic review is the execution. But it is an area of great importance as we look to best position the company for the future.

Our third objective and a likely consequence of any resizing of our asset portfolio would be an evaluation of our costs and capital allocation. I expect that the company that emerges from this review will be leaner and more focused. Importantly, we expect to be better able to pursue and fund growth in the remaining business.

Lastly, an expected outcome of our activities will be reducing financial leverage. While the company is under no market rating agency or liquidity pressure, the board and I believe that the current leverage is an overhang on our public equity valuation. By delevering, we can both increase the mix of equity in the enterprise value and potentially increase our trading multiples as a broader universe of investors are able to participate in our story.

An added benefit of a less leveraged capital structure over time is increased optionality on capital allocation whether for aggressive growth opportunities or shareholder returns. While we are not making any discrete announcements today, I anticipate that the strategic review will occur through a series of steps that will play out

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over the coming quarters and I anticipate that we will begin to make announcements on specific actions by the middle of this year.

A key component of the strategic review that we have discussed explicitly is ensuring that the value of our international business is fully recognized in the share price. This is a critical piece of our growth, and we have made remarkable strides in meeting the goals that we set three years ago when we announced the partnership with GIG. Since that time, we have moved four projects totaling 1.5 million metric tons of waste processing capacity into full construction. This was no small task as this occurred during the debate over Brexit. And the last two projects reached financial close in the midst of the COVID-19 pandemic in related lockdowns. And the result is that we will soon have, when coupled with our Dublin project, five new assets located in one of the best markets in the world in terms of waste pricing and public support.

As you consider our portfolio, I'd also highlight the notable construction progress we've made over the last two years with no material pandemic-related delays on the three English projects, which represent the vast majority of the profitability in our UK portfolio. As a company, we took the lead on development and construction on these projects and we'll be the operator of all three construction – once construction is complete.

Looking at the project photos in our investor presentation, you can see the progress on some of the projects, which reached financial close over the last two years. Most advanced, as you know, is Rookery, which reached financial close in March 2019, so roughly two years ago. Rookery is right on schedule and budget with major construction nearly complete.

Around the middle of this year, we expect to begin receiving and processing waste as the plant moves into the hot commissioning phase. Given our progress to-date and experience commissioning new plants, we expect Rookery to be in full operation and generating EBITDA in the first half of next year. With the transition to commercial operations at Rookery approaching next year, I wanted to highlight the sizable contributions we expect from these projects when construction is completed.

Including the already operational Dublin facility, we anticipate generating at least $100 million to $110 million of annual adjusted EBITDA from our UK and Ireland portfolio with free cash flow of at least $50 million to $60 million.

Now leading this effort is our new President of Covanta Europe and fellow board member, Owen Michaelson. Owen's role will be to drive the successful completion of the four construction projects, build out the operating and management team, and create additional value through development of projects in our pipeline. In that vein, I would remind you that the UK market remains attractive for additional Waste-to-Energy development given the significant regulatory support and market demand for landfill alternatives. From that perspective, you should view the financial outlook for international as a floor, not a ceiling. In sum, the UK remains a primary growth avenue and we believe our source of tremendous potential value for shareholders.

Now, we move on to our financial update. With a strategic review ongoing, it would be easy for the team to lose focus. But we finished 2020 with strong results reporting full year adjusted EBITDA of $424 million, which fell inside of our original pre-pandemic guidance range. We also generated free cash flow of $95 million even as we undertook a greater than typical volume of planned maintenance capital investment. These results, which Derek and Brad will discuss in more detail, were possible only with the tremendous effort of our team in incredibly challenging conditions. It is a credit to the resiliency of our people and business model and to the essential nature of our services.

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Looking ahead, we expect to build on these results in 2020. Prior to the impact of any actions from the strategic review, we are initiating 2021 adjusted EBITDA guidance of $435 million to $465 million and free cash flow of $100 million to $140 million. While we are committed to creating value through the strategic review process, I am confident that this team will remain focused on the core business and on driving improved financial results.

With that, I'd like to turn it over to Derek to discuss our operational and business highlights. Derek?

Derek W. Veenhof

Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

Thanks, Mike, and good morning, everyone. I'll be referring to the investor presentation and will begin my comments on slide 4. 2020 was obviously a unique year that tested our people, assets, and plans in ways we never could have anticipated. And, overall, I think we passed the test handily. For that, I'd like to take a moment and thank all of our employees and our customer base for meeting the challenges of the pandemic and for the personal sacrifices people made along the way. It really will be a year we will never forget in this regard.

From a waste market perspective, we witnessed a significant contraction in commercial waste volumes beginning late in the first quarter, due to the impact of the pandemic. In response, our waste marketing team leaned heavily on our integrated portfolio of assets, including strategically located transfer stations along with our strong client relationships to ensure a steady flow of waste into the plants. Given our preferential locations and the quality of our counterparties, we kept our tip fee plants full throughout the year. After volumes and prices bottomed during our second quarter, our weighted average tip fee prices ticked up sequentially in both the third and fourth quarter. In total, even with a greater reliance than typical on lower priced spot waste, we drove 3% same-store tip fee price growth for the full year. At the same time, we opportunistically increased the total volume of contracted residential waste, which we believe provides even more stability to our mix going forward.

Looking ahead, I am pleased with the stabilization we are seeing in waste flows in our core markets. We continue to see trends in our market – markets that support longer term higher prices, including a tightening of disposal capacity. Similarly, we continue to see increased demand by companies looking for solutions to meet their sustainability goals. When combined with ongoing increases in new contract pricing, during 2021, we expect to see 3% to 5% same-store tip fee price improvement even in this low inflation environment.

On the operation side, I'm proud of the fact that even with all the challenges of operating during the pandemic, we were able to maintain a 91.3% boiler availability, demonstrating our strength and execution and the success of our robust protocols. This level of availability enabled us to process 21.2 million tons of solid waste. 2020 was also a year of significant planned investment with maintenance CapEx of $160 million. To take on this volume of work during a pandemic required incredible planning and diligence. This CapEx included a number of large work scope projects that will ensure the long-term reliability, safety and environmental compliance of our fleet.

Looking ahead, we expect maintenance capital to be significantly lower in 2021. As we look to future years, I expect 2020 will be a high watermark for maintenance capital spending. Our maintenance schedule for 2021 will have a more typical cadence than we experienced in 2020. Assuming the operating environment continues to normalize, you should expect a heavier weighting of spend in the first half of 2021 compared to our 2020 spend. As we deliberately deferred outage activity at the onset of the pandemic, this timing difference will be more acute in the first quarter.

On the commodity front, 2020 was a very challenging year with weak prices for both energy and metals. In both cases, we remain focused on maximizing throughput and managing our risk. In particular, on energy, we remain

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highly hedged for the next 12 months and we will utilize our load serving business to drive incremental margins for our base load renewable energy facilities.

In the latter part of 2020, we began to see improvement in metals prices. There are multiple drivers including an improving global economy, limited inventories of finished steel and the increased demand for recycled metals as the US steel industry transitions towards electric arc furnaces that rely heavily on scrap steel. As a result, we entered 2021 with better pricing as compared to 2020 in both ferrous and non-ferrous metals.

Moving on to slide 5. I'd like to remind you of Covanta's ongoing commitment to sustainability. The foundation of our company is our ability to provide an environmental – environmentally preferable alternative to the landfilling of waste. This mission drove the construction of our plants initially and really defines our commitment as a business. All of our growth initiatives are centered around providing sustainable solutions to our clients and customers.

When we look at waste energy, we see a multitude of benefits to the broader environment. We reduce waste going to landfills, which mitigates land usage, avoids leachate production and significantly reduces Greenhouse Gas emissions compared to the methane released by landfills. We also generate electricity, which offsets the need to burn fossil fuels and in 2020, we've produced enough base load renewable electricity to power 1 million homes.

Through our metal recovery efforts, we recycled materials, which reduces energy-intensive mineral extraction activities. Taken as a whole, for each ton of waste we process, we reduce Greenhouse Gases by net nearly 1 ton on a lifecycle basis compared to the same waste going to a landfill. In 2020, our plants reduced Greenhouse Gas emissions by a total of almost 19 million metric tons. In a time of increasing awareness of the risks of climate change and a clear focus of the new administration, we think it is essential to highlight our role in decarbonization.

Outside of our beneficial Greenhouse Gas impacts, we also continue to prioritize sustainability throughout our organization and in the communities where we live and work. We have a diverse workforce today and we have goals in place to even better represent the communities where we operate. Our workforce is the backbone of our company, and we believe their safety is paramount. During 2020, even with the additional challenges of operating during the pandemic, our safety protocols proved highly effective as we achieved the recordable injury rate of 0.73, a 9% decrease compared to last year and the lowest in our history. This is a testament to our team and their commitment to operating safely. As you can see, from an ESG standpoint, we have a solid cultural focus and continue to drive improvement.

With that, I'll turn it over to Brad to discuss the financial results. Brad?

Bradford J. Helgeson

Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

Thanks, Derek. I'll begin my review of the financial results on slide 6. Total revenue for 2020 was $1.9 billion, up $34 million from 2019 driven by higher tip fee prices, which added $16 million and new electricity load serving revenue, which added $31 million. These were partially offset by lower environmental services revenue related to the pandemic slowdown over the spring and summer and lower project refurbishment activity at client owned facilities for which we earned revenue.

Commodity market prices had a $6 million negative impact on revenue in 2020, split roughly evenly between energy and ferrous metal. Transactions overall reduced revenue by $10 million with asset divestitures enclosures partially offset by a full year of operation at the Manhattan Marine Transfer Station. Completing the year-over-year bridge, long-term contract transitions added $6 million.

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Now moving on to slide 7. Adjusted EBITDA was $424 million in 2020, a $4 million decline compared to 2019. Positive drivers were 3% tip fee growth, the new wholesale load serving contracts, higher EBITDA from Covanta Environmental Solutions and lower overhead costs reflecting the cost savings program that we instituted in response to the pandemic.

These items were essentially offset by higher costs of operating during the pandemic and higher planned maintenance expense. Commodity prices represented a $5 million headwind to adjusted EBITDA, while transactions and long-term contract transitions added $3 million in total.

Now, turning to slide 8. Free cash flow was $95 million for the year compared to a $140 million in 2019. With adjusted EBITDA relatively flat, a primary year-over-year driver was higher planned maintenance CapEx consistent with our guidance at the beginning of the year. This was partially offset by increased cash flow from working capital, which reflected a $20 million upsize of our accounts receivable securitization program during the fourth quarter.

I'll now review our outlook for 2021. Please turn to slide 9. We are initiating 2021 adjusted EBITDA guidance of $435 million to $465 million. The year-over-year increase is driven primarily by our forecast for higher recycled metals prices as Derek discussed. [ph] Before (19:53) commodities, we're expecting results to be generally similar year-over-year. However, there are a number of variances under the surface both positive and negative as the pandemic leads to some noise in the comparisons.

We expect tip fee growth of 3% to 5% as waste markets have largely returned to normal, and we resume trend growth. This remains the key driver for our results. On the expense side, we expect to see some difficult comparisons. Our pandemic cost reduction program saved nearly $25 million in 2020. And while we remain highly focused on controlling costs in 2021, most of those savings were onetime in nature most notably the temporary salary reductions and furloughs and will not recur in 2021. In addition, like many companies, we experienced a reduction in medical benefit experience in 2020. Our guidance range assumes a return to normal – towards normalized levels. So, we'll see how that plays out.

Lastly, with macro pressures in the insurance market specifically adverse claims experience and low interest rates, we're seeing an increase in property and casualty insurance costs of approximately $10 million this year. I will note that our guidance discussed today does not reflect any potential actions taken as part of the strategic review. When we announce specific steps, we'll update guidance at that time if and as appropriate.

Now turning to slide 10, we expect to generate free cash flow in the range of $100 million to $140 million in 2021. The main drivers are the year-over-year improvement in adjusted EBITDA as discussed and significantly lower maintenance CapEx. Lastly, we expect working capital to represent a $10 million to $30 million headwind on a year-over-year basis, essentially implying relatively flat working capital in 2021 compared to the positive cash inflow in 2020.

Now please turn to slide 11 where I'll discuss capital allocation. We are expanding our usual presentation here to look at the overall utilization of free cash flow. From a discretionary growth perspective, we're planning approximately $20 million of investment this year, primarily funding construction in the UK. During 2019 and 2020, we garnered premiums and development costs recovery as our partners bought into the Rookery, Protos, and Newhurst projects at financial close. This helped to defray our investments in these projects.

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Our dividend policy change announced in April resulted in a $44 million reduction in dividend payments in 2020 with an annualized reduction of approximately $90 million as the new rate reflected in 2021. We can now confidently point to a path of reducing our leverage before taking into account any actions resulting from the strategic review and our baseline expectation is to have $40 million to $80 million available for debt reduction in 2021, all else being equal.

Now please turn to slide 12 where I'll provide an update on the balance sheet. At December 31, net debt was $2.5 billion, a $16 million increase from year-end 2019. Our consolidated leverage ratio was 6.2 times, which has remained largely flat during 2020. And our senior credit facility covenant ratio was 2 times. Available liquidity under our revolving credit facility was $443 million at year-end.

I'll conclude my remarks with an update on our growing business in the UK and Ireland. Please turn to slide 13. We now have four projects under construction in the UK, which are expected to move into operations in the following order. Rookery in the first half of 2022; Newhurst and Earls Gate in 2023; and Protos in 2024. The schedule on the top right of this slide presents Covanta's required equity investment into the UK projects, sale proceeds and premiums received, and the net of the two. We estimate an additional $140 million of net investments through 2024 to complete construction of the four projects with the majority to come in 2022. We have more than ample cash flow and liquidity to fund these amounts.

As you can see, the initial sale of the 50% interest in the Dublin project in 2018 when we formed our partnership with GIG along with premiums received in the UK to-date will in effect fund the entirety of our investments in the four new projects. When all projects are operational, we estimate that our business in Ireland and the UK will generate $100 million to $110 million of adjusted EBITDA, proportional for our ownership, and $50 million to $60 million of free cash flow reflecting project equity distributions and our O&M fees. Given these estimates along with our proportional share of the unconsolidated project debt of approximately $650 million on a fully funded basis, you have the necessary data to estimate the emerging value of this business.

As I mentioned, Rookery is expected to reach commercial operation in the first half of 2022. For modeling purposes as this date approaches, Rookery will generate approximately $30 million of adjusted EBITDA to Covanta on an annual basis. As Mike discussed, we're pursuing additional projects and we look forward to providing details as these developments mature. Given the continued need for landfill alternatives in the UK, attractive economics, and a supportive regulatory framework, we see more opportunities for growth here and view the financial estimates that we're providing today as our starting point.

With that, Operator, we'd like to move on to the Q&A portion of the call.

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QUESTION AND ANSWER SECTION

Operator: Thank you. We will now begin the question-and-answer session. [Operator Instructions] The first question today comes from Noah Kaye with Oppenheimer. Please go ahead.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.

Q

Good morning. Thanks for taking the questions. I hope everyone is well. Mike, can I start with a question for you? Appreciate all the color on the priorities for the strategic review. I guess I would just ask after 100 days or so of getting started with this review, what can you share with us about what you've learned or what you kind of incrementally appreciate about the business and about the opportunities you see?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Well, a couple of things. First of all, the one conclusion that we came to quickly was the business is largely organized in a homogenized fashion. So, it's very consolidated without I think enough scrutiny for capital allocation directed at the most profitable assets. And we still need to and we're in the process of rationalizing what the expense structure should look like once again to warrant expenses directed at the most profitable operations. So, that would be the first.

The other is that some of that consolidated character is helpful when it comes to things like our environmental services business where we bring the breadth of services that having Waste-to-Energy facilities have plus our dedicated environmental services facilities and together can supply an alternative for our commercial customers that is a zero landfill opportunity at premium pricing. So that's one we're together that's a pretty strong customer facing business that I think is somewhat unique.

And then clearly, the UK is completely different than Ireland because those are now the newest technology, newest plants in a waste environment that is looking for non-landfill solutions. So that's very different than a client service business in North America obviously, where you've got much more dated assets and you've got contractual both obligations and contractually constrained pricing. So being in a more merchant market in – for our own plants in North America and in the UK is obviously very preferential.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.

Q

That makes sense. And then it looks – I mean there's a lot of detail here as I think Brad said about the UK portfolio with which we can make our own valuation judgments. But it does look like you may have nudged expectations for kind of the profitability portfolio slightly higher. I'm just wondering what has improved in your view about the sort of run rate profitability of the portfolio? Can you give us any color on what you're seeing in the UK and Ireland waste markets or anything you've seen improving in the economics? Thanks.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Yeah. Noah, good morning. It's Brad. There were a few things that led us to nudging it up. In the UK, first off, as we always said when we provided preliminary ranges, those will be finalized based on our final equity ownership positions in the projects. We ended up increasing our ownership percentage in the Protos project relative to what

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had been assumed in that range, number one. Number two is currency. Obviously, the pound has strengthened pretty significantly here recently. So, we've updated and we note this on the slide, we've updated for current – forward currency rates. And then also, the range contemplates certain asset management improvement opportunities we see at the Dublin project now that we've been operating it for a few years. And so, that shouldn't be viewed necessarily as a static level of contribution.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.

Q

Okay. That's very helpful. Thank you.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Sure.

Operator: The next question comes from Michael Hoffman with Stifel. Please go ahead.

Michael E. Hoffman
Analyst, Stifel Financial Corp.

Q

Hi, thank you very much. Back to the strategic review, have you actually concluded certain assets should be marketed and advisers have been hired? And if such, if you're asking us to apply a valuation to say UK, could you give us what you're thinking about selling what that EBITDA looks like so we can incorporate that also in the analysis?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

We're at the point now where we're organized to seek third-party value from the market in terms of some specific assets. So, once we have a sense of what the market would be interested in and what those value differentials could be relative to our publicly trading – traded multiples, we'll have a much better sense of that.

But clearly, until we get market feedback, we would be guessing at what was of greatest interest to the market. But as we said from the beginning that everything really is on the table to try to maximize the value of the company so that interaction with the market is what we're going to be engaged in here in a pretty short period of time.

Michael E. Hoffman
Analyst, Stifel Financial Corp.

Q

Okay. So, I'm a pretty simple fellow, so very specifically you are shopping certain assets and if you get appropriate values and you're prepared to sell them and if you're not, you wouldn't. Is that what I'm hearing?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yeah. That's fairly accurate. Right.

Michael E. Hoffman
Analyst, Stifel Financial Corp.

Q

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Okay. On the capital spending side, Mike, you made a comment in the beginning about the allocation across the portfolio versus cash flow. If I look at total maintenance spend between what goes through the P&L and what goes for the cash flow statement, how would I proportion what's sort the service fee side versus the company-owned side?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

That's a good question. Some of it would be volumetric in terms of the biggest plants with the most volumes would warrant more continued investment. So – and clearly that the skewing across 39 plants in North America would be the merchant plants, garner greater capital allocation than the client service plants do.

Michael E. Hoffman
Analyst, Stifel Financial Corp.
Q

Okay. And then...

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

If you had to do a split, you would say maybe two-thirds and one-third might be about right, one-third being the client-owned plants and two-thirds being the merchant plants that Covanta owns.

Michael E. Hoffman
Analyst, Stifel Financial Corp.
Q

Okay. Right. That's very helpful. And then from a standpoint, Brad, the guidance around this transparency on slide 13, Dublin's about $30 million now. You were suggesting Rookery is about $30 million, that's the EBITDA sort of coming into the EBITDA contribution of the $100 million to $110 million. If I apply sort of a proportion of tons versus ownership, I can kind of map out the rest I'm assuming that's not a bad way to look at how to map out the rest to get to the range of $100 million to $110 million?

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.
A

No, it's not. I suspect you've come pretty close using that methodology.

Michael E. Hoffman
Analyst, Stifel Financial Corp.
Q

Okay. And then am I using a 50% of the EBITDA as the cash generation is sort of a reasonable multiple to just sort of drop the cash down from each one?

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.
A

Yeah, more or less.

Michael E. Hoffman
Analyst, Stifel Financial Corp.
Q

Okay. Yeah. All right. And then lay out the same kind of pathway about it's a first year middle – half contribution and then kind of roll it forward, so if I get to 2025, 2026, that's what I meant that $110 million to $110 million full contribution?

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Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Yeah. I mean, of course, we haven't been specific yet as to first half second half on Protos, Newhurst and Earls Gate. But if you want to assume mid-year in absence of any more specific guidance, which we'll give as we get closer, that's not inappropriate.

Michael E. Hoffman
Analyst, Stifel Financial Corp.

Q

Okay. And then given evolution of the metals markets and your own comment and I agree I cover some companies that do electric arc furnace test recycling. Is there a growing opportunity to be able to hedge some of this volatility? I mean, I get historically you haven't been able to. But can we start to hedge some of the volatility so we take that out of the business model?

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Yeah. We can and I would say for us, it's an emerging opportunity as we have increased our – and improved our recovery and sorting of non-ferrous materials, I think there'll be opportunities for us to, for example, specifically hedge copper as opposed to a mixed product, which really was not hedgeable historically. We haven't yet hedged on the non-ferrous material, but we see that as an opportunity going forward. On the ferrous side, the challenge we face is that the index we sell against for our – with our off-takers is not one that's currently hedgeable effectively with a traded contract. There is a traded contract that we would hope to transition to over time that's essentially equivalent, but has a corresponding traded financial contract. We've done that at one plant, so far, and actually have begun as a result hedging ferrous prices, again, for the output at just one plant. So, baby steps, so far. But absolutely, our objective would be to hedge this revenue increasingly going forward.

Michael E. Hoffman
Analyst, Stifel Financial Corp.

Q

All right. Thank you very much.

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Thank you.

Operator: The next question is from Tyler Brown with Raymond James. Please go ahead.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Hey, good morning, guys.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Good morning, Tyler.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

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Hey, Derek, nice job on the tip fee pricing, I think, all things considered this year. I know on the deck, you talked about CPI being muted in 2021, but if we do see some higher CPI prints through this year, should we expect those to kind of flow through into 2022? And then, can you just remind us maybe how much of the book is directly tied to CPI?

Derek W. Veenhof
Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

A

Well, first of all, thanks, Tyler, for the compliment on the tip fees. I appreciate that. A lot of work went into that. So, on the inflation escalation on the waste side, I would expect – a lot of our indices move either at the midyear or towards the end of the year. So, yes, I think your question is would you see a benefit if CPI is less muted, would we see it in 2022? The answer to that would be yes. And then, when you look at the overall revenue base between the service fee plants and the waste revenue, we have roughly about a $1 billion of revenue tied to some form of escalation.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Okay.

Derek W. Veenhof
Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

A

Some of it being fixed within the contract, some of it being exposed to whatever indices that contract is governed by. So, hopefully that is...

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Right. So, they'll move in...

Derek W. Veenhof
Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

A

Yeah.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Yeah. They'll move in sympathy with CPI, I would think.

Derek W. Veenhof
Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

A

Yeah. Yeah.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Okay. Okay. And then you mentioned – yeah. And you mentioned – yeah, it's perfect. You mentioned 3% to 5% tip fee growth here in 2021. So, how much of that is simply mix versus say call it core pricing? And do you have any bigger call it chunkier volumes such a rebid over the next couple of years in the Northeast?

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Derek W. Veenhof
Executive Vice President-Sustainable Solutions, Covanta Holding Corp.

A

So, it's always going to be mixed, because we keep the plants full generally speaking, absent a major snowstorm or two. So, it's always going to be on the next side. So right now Tyler, we're [indiscernible] (00:38:26) over the last few years we've been pretty heavily contracted, committed. We actually have increased our committed alignment. Again, I think we're on the merchant side, roughly 83% committed for this fiscal year.

So, there's not a lot of wiggle room left on what's exposed currently. But I do feel pretty strongly that as contracts roll off we're re-pricing into and you're seeing it in our results. We're re-pricing into much stronger markets and stronger opportunities. And we can be a lot more disciplined I think than if you go several years back we had a lot of exposure at a lot of these plants and the reality is because of our contracted nature now we've got a lot more flexibility to be choosy about what we chase.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Okay. Okay. Very helpful. And then, Brad, just appreciate the simple EBITDA bridge, but I was hoping for a little more color in that core business piece. So, I think you gave a little bit of color on some of the – I'm going to call it cost comebacks. But specifically, how much of a headwind are all of those costs coming back, which includes healthcare and insurance and everything? Basically I'm trying to figure out how strong the core businesses that's basically offsetting that.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Yeah well...

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

If that makes sense.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

It does, yeah. I mean the three that we can point to relatively discretely are insurance, which I mentioned in my prepared remarks is about $10 million year-over-year. That's mostly driven by a pretty substantial increase in our premiums for property and casualty coverage, which is a market phenomenon. It's not a Covanta specific phenomenon.

Medical benefits for employees, the experience there. Our forecast and what's assumed in our guidance has that higher by close to $10 million as well. That's based on actuarial estimates. And so, we'll see what happens there. It's just an estimate at this point. And then the other that I cited that I would describe as relatively discrete was the specific cost reduction program that we put in place last year. We benefited from that. We calculated $24 million in total cost savings specific to that program.

We will retain some of those cost reductions and certainly travel, for example, has not gone back to where it was. We – given the macro environment and other reasons, we've maintained a pretty tight grip on new hiring as another example in the corporate office. So, we'll retain some of it. But most of it was by definition temporary that was by design. So, I don't have a specific number for you, but I would say...

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Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.
Q

Okay.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.
A

...majority – the vast majority of that $24 million should come back.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.
Q

Okay. But there could be some lingering comebacks I guess in 2022 or and there's probably some structural saves as well. But...

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.
A

Absolutely. Well, yeah.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.
Q

Okay.

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.
A

And as Mike said at the beginning, one of the things we're looking at with the strategic review of course is as our business evolves, what's the right cost structure for this business. And so, nothing we've talked about today regarding guidance reflects of course any of those thoughts.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.
Q

Right. Right.

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

And just to follow-up on that, I mean if you just think about it from a perspective of having a North American portfolio of 39 plants plus an environmental services business, if you make some moves to streamline the business by definition, you're going to have a step function change in cost structure. So, that's one of the things that we're spending an enormous amount of time on, which you want to come out of this in a very advantageous position and when you think about cost structure, so that's all what we're working on.

And we're trying not to do it from the top down, but from the bottom up and figure out what we need, what's essential, what will allow us to continue to operate with the integrity that we've had and in the most cost effective way. So, that's why it's taking a little more time. But it's better than trying to enforce from the top just across the board kind of reductions without that kind of thought behind it.

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Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Okay. Okay. That's helpful. And then my last one, if I can squeeze this one in. So Mike, I'm just not much of a utility guy. But basically, what is load serving? That line keeps creeping up. You've talked about it quite a few times in the call. But basically, just what is that? What drives it? And how do we think about that into the future?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

It's really a stabilizing force. It's the event – I mean Derek used the term, so I'll use it. I'll use it as well is it's a renewable sustainable base load facility, which is unusual in that regard. And so it's able to be on-call to support the system. So, if a utility, like for example in New Jersey, where we've got more wind – I mean, more solar power now because of the public policy support board, so that intermittent power needs to be levelized against when it can't operate, right? And so having the load stabilizing facilities like we have basically levelizes some of the ups and downs that you would get in the system now. So, the system is just more volatile. I mean, not to get into all this, but you could see the perfect storm in Texas was too many things that all correlated to each other. So, when you've got something like we have that can operate this way, it's very different because it's not correlated to natural gas prices. It's not going to have constraints of pipelines. So, it's going to operate in a way that is somewhat counter to those things that are most sensitive on a electric system.

Patrick Tyler Brown
Analyst, Raymond James & Associates, Inc.

Q

Okay. That's very helpful. I didn't want to go down the rabbit hole. But thank you. Appreciate it.

Operator: The next question is from Mario Cortellacci with Jefferies. Please go ahead.

Mario Cortellacci
Analyst, Jefferies LLC

Q

Hi. Good morning. Just on the strategic review, I think you touched on obviously, you're shopping some of the assets, but I guess just could you give us a sense for whether if this could be a plant or two or three and maybe separate sales or is this something where you're even considering bundling a few plants if the offer is right from a particular buyer?

Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

All the above. And that's the whole idea of value discovery in the market is to figure out what is the most attractive configuration to the market and what kind of valuation differentials can we get for it. So, everything you just described is what is in the process of being pursued.

Mario Cortellacci
Analyst, Jefferies LLC

Q

Got it. And then obviously, you're still in the process. It's just thinking about potential buyers. Would you expect something to be more from a PE perspective, are you selling to municipalities? Obviously, like I said, it's – this is more or less speculation. But if you had to guess one way or the other I guess who do you think would be the best strategic buyer for something like that?

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Michael W. Ranger
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Well, our assets fit a lot of categories. So, it depends upon where the value would come in. And clearly, the nature of our business fits pretty well with private equity infrastructure-focused pools of capital. So, I mean that's clearly one alternative. And there are strategics in every line of our business. So, we wouldn't want to discount that either. But clearly, there's a cost of capital advantage that some pools of capital would bring to the profile of our various business segments.

Mario Cortellacci
Analyst, Jefferies LLC

Q

Got it. Okay. And then just last one for me. On profiled waste, I think you guys were up 3% on the year. Does that imply you are negative in Q4? And is that just driven more from the resurgence of the virus and I guess more and more restrictions or lockdowns? And then what are you guys thinking for profiled waste in 2021 in terms of volume and price that you can get there?

Bradford J. Helgeson
Executive Vice President & Chief Financial Officer, Covanta Holding Corp.

A

Yeah. Hey, Mario, it's Brad. I'm not sure what numbers you're looking at to imply down Q4. We were up Q4 so maybe we can take that offline to help reconcile that. But looking ahead to next year, we're looking at 5% to 10% growth in profiled waste again, which has been the rate of growth we've had in that business as far back as I can remember.

Mario Cortellacci
Analyst, Jefferies LLC

Q

Got it. Thank you.

Operator: This concludes our question-and-answer session. The conference has now also concluded. Thank you for attending today's presentation. You may now disconnect.

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