Waste Connections

Materials
NYSE: WCN | TSX: WCN
Market Perform | Hold

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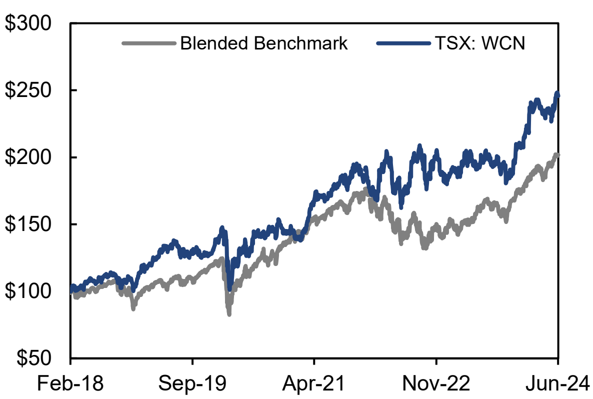
Max Konwitschny, Portfolio Manager
Connor Bot, Investment Analyst

Return on Investment	
Current Share Price	$175.36
Target Price	$189.00
Dividend Yield	0.65%
Implied Return	8%
Conviction Rating	2

Market Profile	
52-Week Range	$127.88 - $175.78
Market Capitalization (US$mm)	$45,269
Net Debt (US$mm)	$6,944
Enterprise Value (US$mm)	$52,218
Beta (5-Year Monthly)	0.71

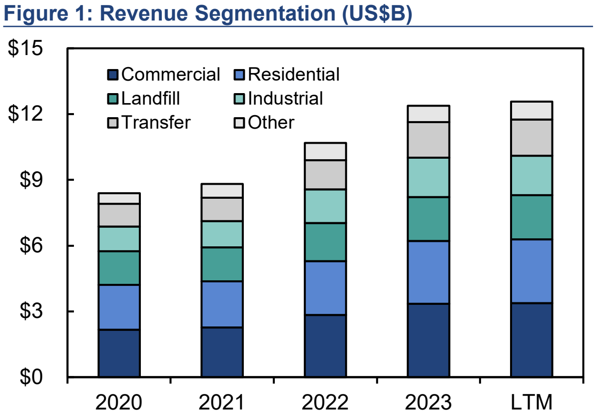
Metrics	2024E	2025E	2026E
Revenue (US$mm)	$8,824	$9,707	$10,677
EBITDA (US$mm)	$2,758	$3,033	$3,337
EPS	$ 4.45	$ 4.89	$ 5.53
EV/EBITDA	18.9x	17.2x	15.6x

Holding Period Trading Performance (Indexed to $100)



Source: S&P Capital IQ

Figure 1: Revenue Segmentation (US$B)



Source: Company Filings

Business Description

Waste Connections (TSX: WCN) is a North American integrated solid waste services company that provides non-hazardous waste collection, transfer, disposal, and resource recovery services. The Company serves approximately nine million residential, commercial, municipal, and industrial customers in largely exclusive and secondary markets across 46 U.S. States and six Canadian provinces. WCN also provides non-hazardous oilfield waste treatment, recovery, and disposal services in the U.S. and Canada, as well as intermodal services for the rail haul movement of cargo and solid waste containers in the Pacific Northwest through a network of intermodal facilities.

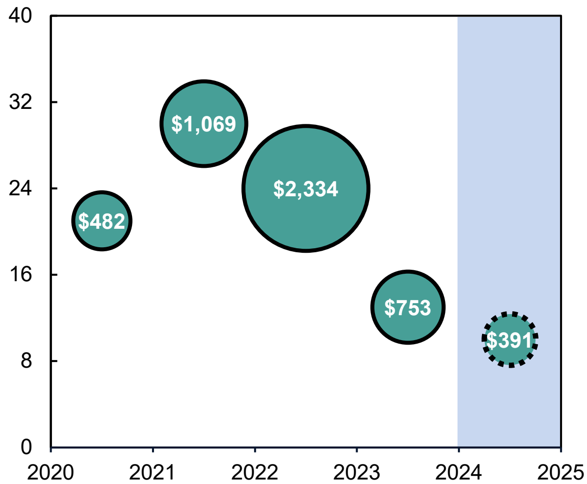
Industry Overview

WCN is the third-largest operator in the North American waste collection, transfer, and disposal industry. The sector is regionally fragmented and regulated, with dense municipal areas garnering significant competition from both major and regional operators. GFL Environmental (TSX: GFL), Republic Services (NYSE: RSG), Waste Management (NYSE: WM), and WCN are among the major operators that account for ~61% of the U.S. and Canada's Municipal Solid Waste landfill volume. Local governments control approximately 27% of these volumes, with the remainder controlled by private operators. Municipal governments have been increasingly privatizing this sector in the last decade as operating costs rise, waste disposal complexity increases, and environmental regulations tighten. This has favoured the integrated, scalable business model of major operators, and has spurred significant consolidation within the industry. For major operators, acquisition-driven growth is often the best use of capital due to advantages including (1) access to competitive waste collection areas under exclusive arrangements such as franchise agreements or municipal contracts, (2) vertical integration opportunities through consolidating collection and disposal services, and (3) access to niche markets through the provision of proprietary treatment and disposal technologies. As such, waste asset acquisitions in Canada and the U.S. amounted to ~US$6.3B and ~US$4.2B for 2022 and 2023, respectively.

The current waste landscape incentivizes operators to build up high barriers to entry in certain regions through a combination of exclusive agreements, landfill ownership, and competitive pricing. Companies that have already consolidated disposal assets are becoming more focused on building out and acquiring operators with collection, transfer or materials recovery facility (MRF) assets that can bolster their vertically integrated positions. Controlling the point of transfer from collection to landfills has become vital as landfills continue to reach capacity and incremental disposal capacity moves farther from their respective collection market. By controlling the waste stream from collection to disposal, major operators can optimize routes, transfer facility volumes, and landfill capacities, significantly raising margins. This has further widened the pricing gap between highly efficient, vertically integrated operators and regional waste service companies.

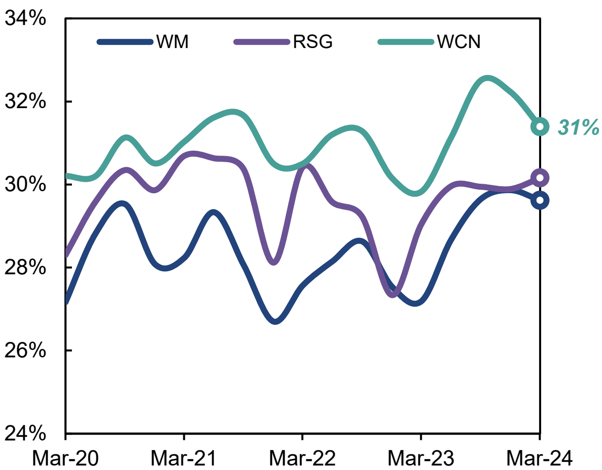
Tipping fees are also a primary driver of waste service economics and are generally set by the state or province. Fees vary (cont.)

Figure 2: Acquisition Count & Spending (US$mm)



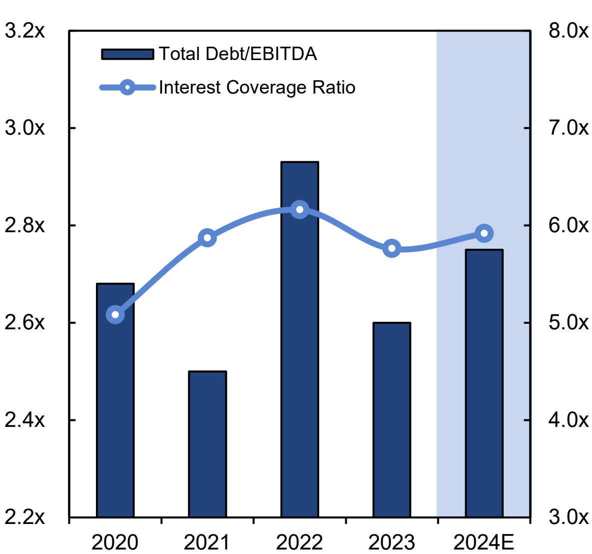
Source: Company Filings

Figure 3: Adjusted EBITDA Margin vs Peers



Source: Company Filings

Figure 4: LHS Net Debt/EBITDA vs RHS Interest Coverage



Source: Company Filings

regionally with population density, waste disposal regulations, distance to collection networks, and a variety of other factors. The Northeast U.S. and Pacific Northwest generally carry the highest tipping fees in North America, as permitting, building, and commercializing a private landfill can take multiple years. However, privately owned landfills carry favourable pricing terms including inflation-linked and fuel pass-through charges. As such, tipping fees at privately owned landfills have increased by 23% since 2017, compared to publicly-owned facilities at only 4%. Going forward, the Fund expects the trend of landfill privatization to continue, with major operators poised to benefit the most by integrating acquired collection routes into low-cost, self-owned disposal capacity.

Asset Acquisitions

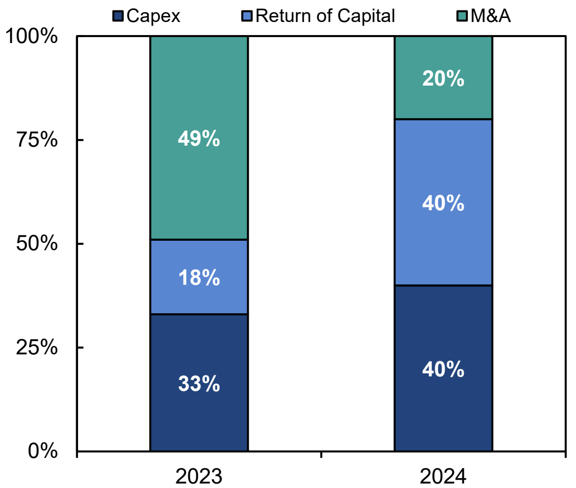
In Q1 2024, WCN closed a $1.1B all-cash acquisition of Secure Energy Services' (TSX: SES) energy waste treatment and disposal assets. WCN acquired 18 treatment, recovery, and disposal facilities, and six landfills in Western Canada. The transaction also strengthens WCN's ability to service Canadian E&Ps through the acquisition of four saltwater disposal injection wells and two disposal caverns. WCN also acquired landfill and MRF assets from Waste-Away Group in Q1 2024, solidifying the Company's presence in Indiana, a region which management intends to expand into through additional acquisitions in the long term. The Company intends to normalize M&A to ~20% of capital outlays in FY2024 and beyond, as opposed to ~50% through 2016 - 2023.

Mandate Fit

Quality Management: Following CEO Worthing Jackman's departure from WCN in April 2023, Ronald J. Mittelstaedt reassumed the role of President and CEO, a position which he had previously served since the Company's inception until 2019. Mittelstaedt has more than 30 years of experience in the solid waste industry and grew the Company into the third-largest solid waste operator in North America. Management has historically been proactive on environmental regulation and human capital, as a portion of management compensation is tied to various ESG targets including emissions reductions, biogas recovery, and recycling optimizations.

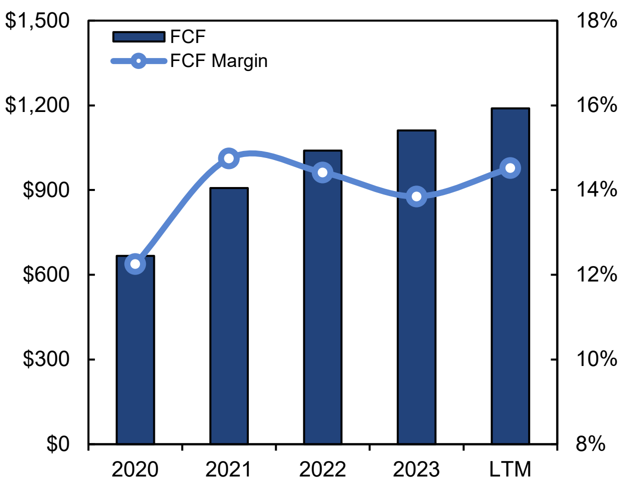
Competitive Advantage: WCN has continued to operate in the Company's historical mix of 40% exclusive markets, and 60% high-market-share competitive markets. The Company's most advantageous operations exist within the vertically integrated exclusive markets, where WCN retains ownership of local landfills and transfer facilities. This allows the Company to exert significant pricing power over collection services, out-competing all regional operators and ensuring efficient routing with fewer trucks to lower fuel costs. Additionally, WCN has historically implemented this strategy in secondary markets, achieving a higher local market share than what would generally be possible in competitive high-density urban markets. This significantly reduces collection account turnover and renewal risk, contributing to the Company's industry-leading EBITDA and FCF margins of 30.4% and 23.3% compared to the peer average of 30.3%, and 11.2%, respectively. WCN also has material footholds in niche markets such as E&P waste treatment and disposal and renewable natural gas (RNG). This has historically resulted in high-margin cashflows uncorrelated with the seasonal waste services operations. The Company also intends to open three RNG facilities in FY2024. RNG represents a new avenue of growth for the Company using its existing landfill assets, and materially lowers GHG emissions. WCN plans to have 12 RNG projects (cont.)

Figure 5: Capital Outlay Guidance



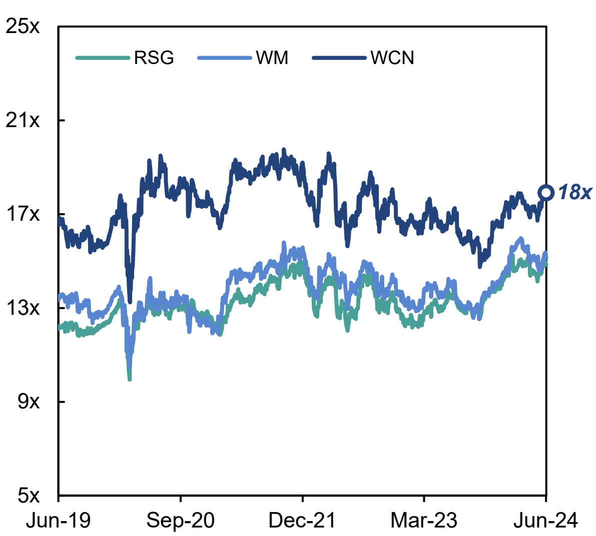
Source: Company Filings

Figure 6: LHS FCF (US$mm) and RHS FCF Margin



Source: Company Filings

Figure 7: NTM EV/EBITDA vs Peers



Source: S&P Capital IQ

in development by 2026, representing ~$200mm in annual EBITDA once fully operational. The Fund believes that WCN can comfortably sustain its exclusive and competitive market advantages stemming from its high barrier to entry waste stream integration practices and industry-leading capital allocation strategies.

Strong Balance Sheet: WCN holds a strong balance sheet with a Net Debt/EBITDA ratio of 3.1x and Debt/EBITDA ratio of 3.2x compared to the peer averages of 3.8x, and 3.0x, respectively. Management has stated an intention to keep Debt/EBITDA below 3.0x, supported by post-acquisition deleveraging and continued margin expansion from vertical integration. The Company also demonstrates its ability to meet debt obligations with an interest coverage ratio of 5.0x and holds an A- and Stable outlook rating from Fitch. For FY2023, the Company had liquidity of over US$1.5B, positioning WCN to continue acquisition activity.

Growing Free Cash Flow: WCN has continued to consistently grow FCF and dividends since Q1 2019 at CAGRs of 12% and 10%, respectively. Although management believes M&A is still the best use of capital on a long-term growth basis, the Company has shifted towards allocating 40% of capital outlays towards their capital return program (previously 18% in 2023). The shift enables WCN to pursue strategic MRF assets in competitive regions and provides ample optionality for early debt repayment, opportunistic share repurchases, or dividend increases. In combination with industry-leading FCF and EBITDA margins, management has proven themselves to be effective capital allocators, which the Fund believes will allow WCN to continue to pursue investments that deliver the highest ROIC to investors.

Risks

WCN primarily faces environmental regulatory risk on the disposal and treatment of waste post-disposal. In Q2 2024, the EPA set drinking water standards for certain poly-fluoroalkyl substances and designated PFOS and PFOA, or “forever chemicals”, as hazardous substances. Regulations such as these can increase handling costs and force companies to adopt additional sorting and disposal methods. However, disposal regulations can also provide opportunities for major operators to offer specialized disposal services at low costs through modifying in-place infrastructure.

Investment Thesis and Valuation

WCN was valued at US$189 using a five-year DCF with a WACC of 6.77%. The terminal value was derived from a 50/50 blend of (1) the Gordon Growth method, using a 3.0% terminal growth rate, and (2) an EV/EBITDA exit multiple of 18x. The CPMT is confident that WCN’s premium valuation is justified compared to its peers given industry-leading EBITDA and FCF margins and wide-moated operating areas. The Fund’s original investment thesis was based on WCN outperforming its peers stemming from a superior capitalization on waste stream internalization trends. This thesis materialized, as increased M&A activity driven by record privatization served as a catalyst for WCN’s growth between 2022 and 2024. The CPMT views the Company’s enhanced return of capital program as favourable, as there are fewer remaining competitive waste services regions that WCN can economically expand into. The Fund believes that WCN is in an optimal position to capitalize on the continued privatization of municipal waste services while weathering high interest rate and labour cost environments given the Company’s contracted cashflows and high infrastructure ownership.