REFINITIV STREETEVENTS

EDITED TRANSCRIPT

WM.N - Q4 2022 Waste Management Inc Earnings Call

EVENT DATE/TIME: FEBRUARY 01, 2023 / 3:00PM GMT

OVERVIEW:

WM reported 4Q22 results.

CORPORATE PARTICIPANTS

Devina A. Rankin *Waste Management, Inc. - Executive VP & CFO*

Edward A. Egl *Waste Management, Inc. - Director of IR*

James C. Fish *Waste Management, Inc. - President, CEO & Director*

John J. Morris *Waste Management, Inc. - Executive VP & COO*

Tara J. Hemmer *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

CONFERENCE CALL PARTICIPANTS

Bryan Nicholas Burgmeier *Citigroup Inc., Research Division - Associate*

Devin Dodge *BMO Capital Markets Equity Research - Industrials Analyst*

Jerry David Revich *Goldman Sachs Group, Inc., Research Division - VP*

Kevin Chiang *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

Michael Edward Hoffman *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Michael J. Feniger *BofA Securities, Research Division - Director*

Noah Duke Kaye *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Patrick Tyler Brown *Raymond James & Associates, Inc., Research Division - MD*

Sean D. Eastman *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

Stephanie L. Yee *JPMorgan Chase & Co, Research Division - Analyst*

Stephanie Lynn Benjamin Moore *Jefferies LLC, Research Division - Equity Analyst*

Toni Michele Kaplan *Morgan Stanley, Research Division - Senior Analyst*

Walter Noel Spracklin *RBC Capital Markets, Research Division - MD & Analyst*

PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the WM Fourth Quarter 2022 Earnings Conference Call. (Operator Instructions) Please be advised that today's conference is being recorded.

I would now like to hand the conference over to your speaker today at Ed Egl, Senior Director of Investor Relations.

Edward A. Egl - *Waste Management, Inc. - Director of IR*

Thank you, Josh. Good morning, everyone, and thank you for joining us for our fourth quarter 2022 earnings conference call. With me this morning are Jim Fish, President and Chief Executive Officer; John Morris, Executive Vice President and Chief Operating Officer; Devina Rankin, Executive Vice President and Chief Financial Officer; and Tara Hemmer, Senior Vice President and Chief Sustainability Officer.

During their prepared comments, Jim will cover high-level financials and provide a strategic update, John will cover an operating overview, and Devina will cover the details of the financials. Following comments Jim, John, Devina and Tara will be available to answer questions. Before we get started, please note that we have filed a Form 8-K this morning that includes the earnings press release and is available on our website at www.wm.com.

In addition, we have published a supplemental presentation with additional information about our multiyear plan for investments in our renewable energy and recycling businesses, and it is also available on our Form 8-K and our website at investors.wm.com. The Form 8-K, the press release, the supplemental presentation and the schedules of the press release include important information.

During the call, you will hear forward-looking statements, which are based on current expectations, projections or opinions about future periods. All forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially. Some of these risks and uncertainties are discussed in today's press release and in our filings with the SEC, including our most recent Form 10-K. John will discuss our results in the areas of yield and volume, which unless otherwise stated, are more specifically references to internal revenue growth or IRG from yield or volume. During the call, Jim, John and Devina will discuss operating EBITDA, which is income from operations before depreciation and amortization. Any comparisons, unless otherwise stated, will be with the fourth quarter of 2021.

Net income, EPS, operating EBITDA and margin and SG&A expense results have been adjusted to enhance comparability by excluding certain items that management believes do not reflect our fundamental business performance or results of operation. These adjusted measures, in addition to free cash flow, are non-GAAP measures. Please refer to the earnings press release and tables, which can be found on the company's website at www.wm.com for reconciliations to the most comparable GAAP measures and additional information about our use of non-GAAP measures and non-GAAP projections.

This call is being recorded and will be available 24 hours a day beginning approximately 1:00 p.m. Eastern Time today. To hear a replay of the call, access the WM website at investors.wm.com. Time-sensitive information provided during today's call, which is occurring on February 1, 2023, may no longer be accurate at the time of a replay. Any redistribution, retransmission or rebroadcast of this call in any form without the expressed written consent of WM is prohibited.

Now I'll turn the call over to WM's President and CEO, Jim Fish.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Thanks, Ed, and thank you all for joining us. 2022 was another very successful year at WM. Coming into an uncertain 2022, I wouldn't have predicted that we would grow adjusted operating EBITDA by more than 9.5% for the year, and 8.8% for the fourth quarter, all of our recycling was down $59 million for the year on a sharp drop in commodity prices. That's exactly what happened.

Strong operational execution and an unweaving commitment to our strategic priorities led to our full year adjusted operating EBITDA growth of $480 million. We achieved this tremendous growth in the face of elevated inflation, a tight labor market and a downturn in the recycled commodity price market. So we're very proud of our results. Our robust operating EBITDA translated into record cash from operations of more than $4.5 billion, which allowed us to return more than $2.5 billion to our shareholders through dividends and share repurchases.

As 2023 kicks off, we're confident that our long-term focus is on sustainable growth, transforming our business through technology and automation are setting us up to meet the changing needs of our customers, our people and our business environment while leveraging our competitive advantages. Turning to our high-level outlook for 2023. We expect to deliver adjusted operating EBITDA of between $5.825 billion and $5.975 billion in the year ahead, representing growth of just over 7% at the midpoint, which continues the trend of robust operating EBITDA growth that we've delivered since 2019. Since then, we've grown operating EBITDA almost 26%. And at a time when the economic outlook is increasingly uncertain, we're pleased to be anticipating another strong year of earnings growth in 2023.

The essential nature of our service, our diverse customer base and recurring revenue streams provide stability in times of economic uncertainty. Much of the growth in our 2023 outlook comes from deliberate steps that we've already taken to grow revenue and efficiently manage costs. Overall, we're anticipating between 40 and 80 basis points of adjusted operating EBITDA margin expansion in the year ahead, driven by our collection and disposal business.

Moving now to our sustainability growth investment. Let me give you an abbreviated overview of the supplemental deck that was posted to our investors' website. The investment in our renewable energy business is a unique opportunity that we simply couldn't afford to mass. You're all aware that since the passage of the Subtitle B and associated air quality regulations in the 1980s and '90s, landfills have been required to install gas collection systems.

Historically, we've been collecting our landfill gas, converting much of it into electricity, which provides an earnings stream for us. Fast forward to present day, with landfill gas designated as a renewable resource, we are increasing the value of the gas that's an inevitable byproduct of most landfills. These RNG plants are simply taking gas that's naturally produced from the landfill and converting it into a cash-generating machine with a 3-year projected payback and a far better environmental outcome than the status quo.

And our returns far surpass those of our competition by virtue of our CNG fleet, which today represents 74% of our routed vehicles. As a result, we're better positioned to close the loop and capture extremely valuable regulatory RIN credits. At the same time, the recently enacted Inflation Reduction Act will provide tax credits and benefits that served to amplify the value creation of WM's renewable energy business.

The supplemental presentation to the earnings press release provides details on the investments and our projections for cash flow and operating EBITDA growth. But suffice it to say, we view this as a very strong positive for shareholders. We have a number of attractive options for our renewable energy portfolio. Internally, we said there are 3 possible outcomes from this opportunity, good, really good or great. And we're heading down the great path by owning the landfill gas and renewable energy facilities, generating RINs through our CNG fleet and maximizing the value of new tax benefits to increase the resulting earnings and cash flows.

We're also advancing our planned recycling investments and have provided more details in the supplemental presentation on our website. Our portfolio of projects to automate existing and build new material recovery facilities have 3 key financial benefits: reduced labor costs, improved product quality that commands a price premium and capacity growth. In the fourth quarter, labor costs per ton at our single-stream automated MRFs improved by 35%.

The automation of these plants enable us to reduce 137 positions through attrition in 2022. And in 2023, we expect to reduce labor dependence by another 200 positions. By the end of 2023, we're anticipating about a 15% increase in processing capacity from our automated facilities and new markets. We will host a virtual information session for investors on April 5 to provide even more insight into our recycling and renewable energy growth plans. Devina will discuss our 2023 capital allocation plans in more detail, but I want to emphasize our confidence in our ability to continue to allocate capital to all of our priorities, including investing in these high-return sustainability growth projects, returning cash to shareholders through dividends and share repurchases and acquiring accretive businesses.

In closing, I want to thank the entire WM team for another fantastic year. We look forward to 2023 as we continue to execute on our operating plans and progress our investments in renewable energy, recycling and automation to drive growth. I'll now turn the call over to John to discuss our operational results.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Thanks, Jim, and good morning, everyone. Jim described our fantastic results in 2022 and that all begins with our collection and disposal business. In the face of some of the highest inflationary cost pressures, our collection and disposal business delivered double-digit in adjusted EBITDA for the full year.

During the fourth quarter, collection and disposal results were even more impressive as adjusted operating EBITDA grew more than 11% and margin expanded 40 basis points. This momentum sets the stage for continued growth in 2023 and strengthens our conviction that the investments we're making in our people in automation and in differentiating our service offerings are the right decisions. The growth in our collection and disposal business starts at the top of the income statement with robust organic revenue growth. Full year core price was 7.8% with collection and disposal yield of 6.7% and volume of 1.8%.

As we work to keep pace with decade's high inflation, our revenue management teams delivered record core price in 2022 in every one of our lines of business, led by 10.5% in our commercial line of business. We talk often about our focus on generating appropriate returns in our residential and post-collection lines of business. And in 2022, we delivered core price of 6.5% in the residential line of business, 6.4% in our landfills and 5.9% at our transfer stations.

Our revenue metrics demonstrate that our customers' receptivity to our pricing remained favorable through the fourth quarter. Our rollback percentage was almost 400 basis points better for the full year, while new business pricing increased more than 6% in our commercial line of business. The results clearly demonstrate our ability to manage cost pressures through continued pricing discipline and momentum while maintaining our focus on customer lifetime value. As we move into 2023, our disciplined pricing programs combined with the strong momentum from 2022 and are expected to deliver core price of between 6.5% and 7% with yield approaching 5.5%. Our expectation is for strong rollover of '22 price performance.

Given the acute inflationary environment in 2022, we increased certain fees that we don't expect to step up again at the same level. We remain committed to securing pricing that outpaces our cost inflation which is demonstrated by the operating EBITDA margin expansion that we're anticipating in 2023. Shifting to volumes, in the fourth quarter, event-driven volumes remained strong with special waste and C&D volumes growing double digits. Our commercial and industrial volumes were positive for the full year. However, we saw some softening in the fourth quarter. Given these recent trends, we are tempering our volume expectations in the year ahead.

Our guidance includes 2023 collection and disposal volumes that are relatively flat with 2022. We continue to see the rate of labor increases easing in our business, and we remain focused on managing our operating expenses and flexing down costs, flexing costs down with the changing volumes. In our collection and disposal business, we are seeing improvements in our labor costs as inflationary wage pressures are easing. Turnover trends are improving and the investments that we are making in automation are showing benefits.

These improvements were on display in the fourth quarter -- in our fourth quarter results as we saw operating expense margin improved by 30 basis points despite still stubbornly higher maintenance and repair costs. For the full year of 2022, operating expenses increased 50 basis points as a percentage of revenue, but that was largely driven by negative impacts from higher fuel costs and recycling commodity prices that together impacted the measure by 80 basis points.

This increase was partially offset by lower labor and related benefits costs in our collection and disposal business and improved risk management costs. Putting it all together, when you combine our pricing efforts with our progress on cost containment, we expect 2023 operating expense as a percentage of revenue to improve between 30 and 50 basis points for the full year, with those improvements beginning in the second quarter of 2023. In the fourth quarter, our recycling operating EBITDA remained solidly positive even with the sharp decline in commodity prices to about $47 per ton. Over the last several years, we have intentionally taken steps to shift the business to a fee-for-service model that has reduced our sensitivity to commodity market changes. When we started this journey in 2017, commodity prices were 60% higher than what we are anticipating in our 2023 outlook, yet 2023 operating EBITDA is expected to be about 13% higher than in 2017.

This clearly demonstrates that our business model is profitable and generate solid returns in any economic environment. As we look to the future of recycling, we remain focused on advancing automation across our MRF network, which we have proven can lower the cost of process material, achieve better quality while enhancing recycling profitability.

Our employees delivered strong results in 2022, and I want to thank the entire WM team for their commitment to providing the best customer service while focusing on improving our operations. The team has done an exceptional job, and I know that this will continue in the year ahead.

I'll now turn the call over to Devina to discuss our 2022 financial results and 2023 financial outlook in further detail.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Thanks, John, and good morning. Once again, our solid waste business was at the center of WM's strong quarterly results, capping off a great 2022. Our team delivered strong organic revenue growth with a diligent focus on leveraging core price to offset cost inflation while prioritizing customer service and customer lifetime value to minimize customer churn, all resulting in record high yield. .

When combined with strong cost control, these efforts delivered an 80 basis point expansion of operating EBITDA margin in the fourth quarter. Importantly, we achieved these excellent results while investing in technology and sustainability growth that will benefit WM for years to come. Full year adjusted SG&A was 9.6% of revenue, a 40 basis point improvement over 2021 as we achieved back-office operational efficiencies through standardization and process improvement that enabled us to reduce more than 600 positions through attrition.

You can clearly see our strong performance and the record cash flow from operations that we achieved in 2022, which grew 4.6% to $4.536 billion. The increase in cash allowed us to accelerate investments at year-end, which brought full year capital spending to the high end of our expectations. 2022 capital expenditures totaled $2.587 billion with $2.26 billion of that related to normal course capital to support the business and the remaining $561 million related to the strategic growth of our recycling and renewable energy businesses.

Putting these pieces together, 2022 free cash flow was $1.976 billion despite an increase in cash taxes of $370 million. During 2022, we returned a record $2.58 billion to shareholders, paying $1.08 billion in dividends and repurchasing $1.5 billion of our stock. In addition, we spent $377 million on traditional solid waste and recycling acquisitions to grow our business. We accomplished all of this while accelerating our sustainability and growth investments and achieving our targeted leverage ratio of about 2.75x.

Our balance sheet is well positioned for growth through capital investments in our business or strategic acquisitions. Moving to our 2023 financial outlook. As John mentioned, we anticipate organic growth approaching 5.5% from yield. Given an expectation for a little more than 1% revenue growth from acquisitions, and a decrease in revenue contributions from recycled commodity sales and fuel surcharges, we anticipate total revenue growth of between 4% and 5.5%.

When combining our plan to deliver strong organic revenue growth with a focus on optimization and cost control to drive 40 to 80 basis points of operating leverage, we expect to generate adjusted operating EBITDA of $5.825 billion to $5.975 billion in 2023. We expect to allocate $1.1 billion to capital investments in recycling and renewable natural gas growth projects in the coming year. And 2023 is expected to be the peak investment year for each business. While these investments are reported as a component of our capital expenditures, and therefore, reduce our traditional measure of free cash flow. We view these investments as better than an acquisition dollar as they will produce even higher return growth as a strong complement to our existing business.

Our normal course capital to support our business is expected to be between $2 billion and $2.1 billion in 2023. And free cash flow is projected to be between $1.5 billion and $1.6 billion, including the impact of sustainability growth investments. Our outlook anticipates an increase in cash interest and taxes of $175 million to $215 million and about an $80 million headwind from working capital due in large part to the timing and amount of incentive compensation payments. As Jim discussed, even as we step up our investment in high-return recycling and renewable energy growth projects, we remain well positioned to allocate our cash among all of our capital allocation priorities, including returning cash to our shareholders.

Given the Board of Directors intended 7.7% increase in the 2023 dividend rate, we expect dividend payments to total about $1.1 billion in the year ahead. We also expect to continue our share repurchase program in 2023 as the Board recently provided authorization to repurchase up to $1.5 billion of our stock. While our guidance does not specifically include acquisition growth, we will continue to be opportunistic in pursuing the right deals at the right price. In closing, we are proud of what we achieved in 2022, and we're excited about the opportunities that lay ahead for 2023 and future years. I want to thank our hard-working team members for all of their contributions to our success.

With that, Josh, let's open the line for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Jerry Revich with Goldman Sachs.

Jerry David Revich - *Goldman Sachs Group, Inc., Research Division - VP*

Yes. I'm wondering if you could just talk about the puts and takes around the guidance, if recycled commodity prices remain tough over the year. That should be about a $50 million drag to EBITDA, give or take. And in that scenario, I'm wondering if we should be thinking about yield that's above the 5.5% target that we're laying out here this morning, actually we think about the potential for the yield number to move higher over the year as we've seen over the past couple of years?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Jerry, let me tackle the first question first on recycling, and then I'll touch on yield overall. Recycling, obviously, fell off the table there at the end of the year. I think a lot of it had to do with China itself, even though China isn't a big customer of ours anymore, they still affect the overall market, particularly when we think about OCC. And their Zero-COVID policy certainly destabilized the market. I think as they've reopened, we've started to see some stabilization there. So that should help, and that's part of why we are a bit more optimistic in '23 with pricing starting to climb back up. It did climb up a bit in December, and we think it will continue to climb, albeit not back up to where it was for the year in 2022.

To your question about yield in general and 5.5%, yield is doing exactly what we thought it would do. It's doing exactly what we said it would do, last year. I kind of felt like we yield and cost, we're in a fistfight for the last 18 months with really no winter. And what we said was that we hope that when inflation moderated, which it is, that we would start to be able to use yield to not only cover costs but also put a few points on the board in terms of margin. And that's exactly what's happening. So we think that 5.5% yield number is absolutely the right direction. We're sensitive to customers. I mean some of our yield numbers last year were double digits. And when inflation comes back down to 4%, 4.5%, I don't expect to take commercial increases at the 11.5% range. So I think we're pleased with the projection, and we're pleased actually with the fact that costs are starting to moderate and we can actually apply a little bit of our yield to the margin line.

Jerry David Revich - *Goldman Sachs Group, Inc., Research Division - VP*

Super. And Jim, maybe just to expand on that last point, given the margin cadence over the course of the year to get the margin expansion that you're targeting for '23, it looks like you're going to be exiting the year with margins up maybe closer to 100 basis points year-over-year in the fourth quarter, just given the seasonality and cadence. Can you just comment on that and whether that momentum could continue into early '24.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes, Jerry, I think that overview that you provided is spot on in terms of how it is that we're looking at margin for the year ahead, 60 basis points of margin expansion at the midpoint indicates our confidence that the momentum that we saw in the back half of 2022 should continue into 2023. We expect some of the margin pressure from the recycling part of the business to continue in the first half. So we are seeing strong fundamentals in the solid waste part of our business that should help to offset that as they did in Q4.

That being said, some of the cost execution, we really are laser focused as a management team on what we're doing on the cost side of the business. And that's not just looking at inflation and responding to it but being proactive in terms of what we can do to manage it appropriately. And truck delivery trends are favorable now relative to where we started 2022, and that should give us some relief both in repair and maintenance and in truck rental costs. Our frontline retention efforts are showing really strong benefits, and we expect that to continue in 2023. We're managing down professional fees, particularly in our SG&A.

And then on the SG&A front, we're also leveraging technology to automate our processes, which is improving the customer experiences and reducing our cost to serve. So all of that gives us confidence that it's our strong execution on the cost side of the equation that will complement the yield that Jim just spoke to in terms of delivering that margin expansion and exiting 2023 with 100 basis points above kind of this current run rate feels like the right target for us.

Jerry David Revich - *Goldman Sachs Group, Inc., Research Division - VP*

Super, Devina. And can I just sneak one more in. I really appreciate the landfill gas disclosures. I'm wondering, Rankin, can you just give us an update on offtake agreements. A quarter ago, you were at 1/3 of your 3-year offtake agreements were done. Can you just give us an update on where that stands today and whether the pricing point on offtakes in the market is still in the 20s or if that's come in, given the pullback in Henry Hub gas.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. So Jerry, in 2022, we were at 30%, and we're projecting in 2023 to be at 40% of our offtake in fixed. And I think what's important to note here is we really took a look at this back in early 2022, looking at the volume ramp of our R&D, and we were pretty intentional about thinking through how to tap into those voluntary markets.

So those markets today, we're seeing them be quite robust. If you think about large public utilities and industrial end users. This is a great way for them to tap into a low-carbon fuel and we're not seeing any price pullback at the moment. We'll give a bit more detail in April on what it looks like longer term as well.

Operator

Our next question comes from Toni Kaplan with Morgan Stanley.

Toni Michele Kaplan - *Morgan Stanley, Research Division - Senior Analyst*

Wanted to start out on renewable energy. Thanks for all the details in the supplemental presentation. I know you had previously talked about '23 as an elevated year for investment. But it seems like maybe you decided to accelerate it and expand even more. So I guess what sort of -- why is this the right time? And maybe just cadence of the investment during the year. And maybe just -- does this mean that M&A will be lower this year versus last year?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

We didn't really give guidance on M&A. Historically, we've said $100 million to $200 million. So it's likely going to be kind of in that range. But the reason to your point that we've decided to accelerate some of this is just simply the opportunity itself. I mean, I mentioned it in my prepared remarks, but it really is part of our solid waste business. This is gas as a result of Subtitle D in air quality regulations that's coming to us anyway. About half of that gas has been monetized over the last, I don't know, 20 years, but we still have half left and we're certainly not monetizing the full amount when you look at that deck, but that, that we are monetizing, we're effectively paying kind of a 3x multiple instead of what you might pay for an acquisition, which would be kind of 8 to 12x. So that's why we're feeling so good about it.

And we've modeled these at very conservative numbers. Right now, we're well above those. So I think the opportunity just started to present itself through the designation of this gas as being renewable. The markets themselves opening up and now with an opportunity which (inaudible) go into about electricity. In those cases, we don't even have to add capital, if we already have electric facilities generating facilities out there.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

The only other thing I would just add to what Jim said regarding the acceleration of the investment is the investment tax credit and the fact that, that is a really strong pathway for us to get some tax credits on our investments and there's a time line associated with that. And we feel really positive about where we are in our ability to capture those tax credits. We've modeled about $300 million, which you see in the deck.

Regarding our broader portfolio, I mean, this is one of the reasons why we talk about this opportunity being so great because we preserved so many options for WM because we own the gas. We own our projects. We announced 20 projects. There's a whole pipeline that can come after that. And then with the ERINs pathway, if you look at our legacy landfill gas to electricity projects, we can create an earnings stream with no incremental capital, and that's not in our numbers today. So that's upside long term. So we're really optimistic about what we have in front of us here.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

And one -- maybe one last point here that I did mention also, but I'll mention it again. That differentiates us from our competition, and that is that CNG fleet. I mean 74% of our fleet is CNG and the way RINs works is you have to burn the fuel before you can monetize the RIN and having a fleet that is 3/4 natural gas gives us a potential stream there, earnings stream that our competition who might be at 15% to 30% CNG, they simply don't have that or at least don't have it to the same potential that we do.

Toni Michele Kaplan - *Morgan Stanley, Research Division - Senior Analyst*

Super. And I wanted to ask about volume. You mentioned the softening in commercial and industrial in the fourth quarter. Maybe just a little bit more color there, the magnitude, how quickly, how it -- like was it early in the quarter or throughout the whole quarter, et cetera? And if you're expecting any softer volumes in the remainder of the business implied in the guide?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

There were a few moving parts in the volume that was down slightly for Q4. Some of it was by design, residential specifically. Some of it was a couple of lost contracts in the commercial line of business and that was typically going to be in our National Accounts group. And then some of it is maybe softness showing up in the roll-off line of business. I guess if there's any good news there, and it is that when we just looked at our January numbers this morning, they were actually better than Q4 on the volume front, particularly C&D, although some of that C&D might be coming from the hurricane cleanup in Florida.

But MSW was a positive sign for January. So even with that, we felt that a negative 0.5 to a positive 0.5. So a flat volume with last year, as John mentioned, was appropriate. And I guess as we look at the tea leaves for the economy, there are a few factors that are concerning out there. The housing slowdown for sure.

I mean, that's been widely discussed and that housing slowdown. While our C&D volume has been very good and continues to be good. We think that C&D will come back a bit. It almost has to with the housing slowdown. Special waste continues to be a strong point for us and the pipeline is good there. But I think as you think about whether it's the housing slowdown or whether you think about the consumers saving at 7% in 2020 and now down to almost 0 because inflation has eaten up that savings. That's going to affect the consumer. But the good news for us is that our strategy is really not built around the volume aspect. It's built around cost controls, it's built around building out this sustainability strategy, and it's built around pricing. And so we're pleased with being able to come in at the top end of the range on EBITDA at 7% for 2023.

Operator

Our next question comes from Tyler Brown with Raymond James.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

But I do kind of want to get to the heart of it. So is the idea here that the contribution in '26 between RNG and recycling maybe it's now expected to be $740 million, I think, if my math is right, and that was upsized, is that right?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

That's correct.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

But you're also in the midst of a labor automation effort. And I just want to make sure that I'm not double counting because some of that is probably in recycling. But how much additional EBITDA are you expecting by 26 from that effort as well?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

So there is a bit of the -- when we automate in the recycling piece in the deck, there is a bit of that in the $260 million, I think was the number, but...

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes, there's $70 million in the deck on...

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

But there are other areas where we're automating away positions and that are not captured in that deck at all that really have nothing to do with RNG or recycling.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Yes. That's my point. Can you quantify that piece?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Tyler, I would tell you that it's too early for us to predict the impact of that to 2026 and beyond. What we're really emphasizing in our 2023 outlook is that we're starting to see some of the benefits. Yes, recycling is a piece of that.

But beyond the recycling line of business, we're seeing back office to 600 headcount attrition that I mentioned in customer experience, specifically is a strong example of that. And the leverage we've gotten in SG&A margin is in large part due to some of that success. So the 40 to 80 basis points of margin expansion really is all solid waste.

And so that strong performance in 2023 is an indicator of future value that we think will come as we start to see, in particular optimization efforts in the collection line of business take hold. Some of that is delayed because of truck deliveries as well as some of our efforts to take that across additional lines of business. We started in the industrial line of business intentionally, and we're seeing strong success in some of those pilots. And we're happy with where we are, but too early for us to predict how much efficiency gain we can get across all lines of business in 2026 and beyond. But I think taking the 40 to 80 basis points accomplished or predicted for 2023 is a strong indicator of the strength of those initiatives.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Let me expand real quick on what she just said about the 600 positions because that will become close to 1,000 positions just in customer experience. And we've talked a lot over the last couple of years about automation. But we haven't really given you kind of the numbers and where it's benefiting the bottom line. This is a good example. I mean what we really did there was used a turnover number that was close to 50%. And customer experience, took advantage of that attrition. And at the same time, we automated the customer experience, which every other industry, by the way, has done over the last 20 years, and we hadn't. It was -- ours was still kind of a person-to-person experience. We haven't eliminated the person-to-person experience, but we've just made it available, made a self-service option available to our customers.

And as a result, our call volume is down close to 25%. That's a huge drop in call volume. And hence, our ability to take advantage of attrition to the tune of 600 positions in '22 and another close to 400 positions in '23.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Okay. Yes, that's extremely helpful. A lot on to come there. Okay. Devina, kind of coming back to '23 margins, though, and I don't want to be super -- I do want to be specific. Can you just talk about first half and second half margins. So are margins going to be a little bit more flat in the first half and then up quite a bit in the second half. I just want to make sure that we all kind of get the shape of the year right and could margins actually be down in Q1 year-over-year?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Margins could be backward in the first quarter of the year. The pressure from the recycling line of business is the most acute. And while drop in commodity prices is typically something that we see benefit our margin in that part of the business because of the pass-through elements of some of it.

We have seen some pressure. So we are predicting some flatness, I would say, in the first quarter with expanding margin in the second quarter, particularly on the cost side of the business and starting to see the pricing parts of the business really contribute as they did in the second half of 2022 as we anniversary some of those impacts from the recycling line of business I mentioned.

So first half, second half, I would say you'll see more muted margin expansion in the first half, stronger margin expansion in the back half. That being said, I wouldn't expect the minus 100 plus 100 that we saw in 2022 because we've overcome so many of the operating cost headwinds that we were experiencing this year and really starting to see some strong momentum there.

Patrick Tyler Brown - *Raymond James & Associates, Inc., Research Division - MD*

Okay. Perfect. That's extremely helpful. And my last one, just real quick. You kind of went through quite a bit on the free cash flow puts and takes. But can you kind of go back over what the expectation is year-over-year for cash taxes, cash interest and then maybe working capital? Just trying to help build that bridge.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Sure. So EBITDA growth at the midpoint is $390 million, and so that will be the driver of free cash flow growth, cash flow from operations growth next year. Unfortunately, with this interest rate environment, we're going to have to give some of that back because our cost of debt is going up. As you can see when you look at our fourth quarter results, our weighted average borrowing rate in the fourth quarter actually went up 80 basis points. And so that was an increase of $26 million in the quarter.

We were virtually flat all year long in advance of Q4. And when we take that Q4 impact and extrapolate it to 2023, that's what's going to be driving our interest costs higher. So that in and of itself is a little over $100 million of impact. And then we do expect our debt balances to increase in the year ahead. Our debt balances are going to increase because we are seeing such strong growth, and we are going to be investing in all elements of capital allocation with that strong balance sheet. So not pulling back any on our allocation of cash to share buyback in the year ahead, is our current plan.

We may moderate it some, but we'll give you more color on that over the course of the year. So with the higher debt balances and the higher interest cost that really is all of the $175 million to $215 million that I mentioned in interest and taxes. Taxes are actually going to be essentially flat. So while we would have expected some moderation in that because of the onetime payment that I mentioned of $100 million, we're really seeing that offset by 2 things: one, higher pretax income; and the other being the expiration of a piece of bonus depreciation and the asset mix that we're putting in place.

So those are the interest and tax pieces. The $80 million headwind I mentioned on working capital, we had an $88 million contribution to working capital in 2022. So we're essentially saying that we think we might give some of that back. Some of that is a moderation in DSO just because of the recessionary environment that we're predicting. But a large contributor is timing and amount of incentive compensation payments.

Operator

Our next question comes from Noah Kaye with Oppenheimer.

Noah Duke Kaye - *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

D&A stepped up in 4Q. Can you first provide a little color on that and then give us what should be D&A for 2023?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Sure. So the color there is really inflation in our landfill costs. And it's both from normal inflationary cost pressures as well as the regulatory environment, that's driving some of our costs more closure, post-closure higher. So the charge that we took in the fourth quarter relates predominantly to our closed site part of the portfolio, though some of it is also representative of changes we're seeing in management of the active landfills, too.

In terms of next year's DD&A, we're not predicting another step change from this current level, but we are expecting DD&A levels to reflect better delivery of trucks in the year ahead. So you'll see some increased depreciation in the first half of the year rather than waiting to see all of that impact in Q4.

Noah Duke Kaye - *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Okay. But we could -- again the above kind of that $2 billion number for '23. So net-net D&A would step up year-over-year.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Net-net D&A is going to be moderately higher just with the capital expenditure deliveries, but it's not going to be another step change from this level. .

Noah Duke Kaye - *Oppenheimer & Co. Inc., Research Division - Executive Director & Senior Analyst*

Yes. Okay. And then just on pricing, I guess, Jim, listening to your comments around some of the softening in the commercial sector. How do we think about the cadence of price growth expectations? It seems hard to sustain double digits in C&I as we go through the balance of the year. There is some math on that, of course. But how do we think about pricing? And what elements of the business may see the greatest sequential price declines on a cadence basis?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Well, I think we think about it -- I mean, we're thinking about pricing because there are -- there's a kind of a twofold exercise here. One is combating cost increases or inflation, which was why the last 18 months have been so challenging. Because we really felt like it was almost all, in fact, in many cases, all of it was going towards combating inflation. And then a second piece is adding a few margin points for us. So as we look at this through our price group, particularly for commercial since that's where your question was, we think that pricing will moderate a bit because inflation is moderating significantly. And that ends up being a good thing for us. If you look at collection and disposal yield for last year versus our guidance for this year. Last year was 6.7, this year guidance is 5.5. So there is some moderation in yield there. But significantly, we're projecting at least a significantly different cost picture. So we think the price starts to contribute to margin again, whereas it hasn't for the last probably 3 years.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I think the only add I would make there, Jim, is the residential line of business specifically, if you look at our volume loss there, clearly, we continue to make deliberate decisions. We mentioned some of the franchises that we've parted ways with. And even if you look at the 4.5% or 4.7% negative volume, our revenue was still up over $50 million for the quarter in residential. And as we've said, we're going to continue down that path until we get acceptable returns and margins for that line of business. And so we're happy with that progress. We don't like intentionally shedding that business. But under these conditions, like Jim said, the inflation is what we're combating and it's been most acute in residential, partly due to the labor intensity there.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes, I think maybe one place where it might not moderate as much is on the landfill side. I mean we have a differentiated product there. And so not that we don't have a differentiated product on the collection side, but landfill in particular, the yield was 6.2% MSW last year. I think that's probably the highest annual yield for MSW maybe in our history. And I don't expect that to come back that a lot.

Operator

Our next question comes from Bryan Burgmeier with Citi.

Bryan Nicholas Burgmeier - *Citigroup Inc., Research Division - Associate*

I understand free cash flow will get near term. But do you think WM can emerge from this investment period with structurally higher free cash flow conversion from EBITDA than you had in 2021 and before. It seems like these investments will be highly cash generative once ramped and can potentially exceed where you were before the investment period.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes, Bryan, you're spot on there. Our ability to convert revenue and EBITDA dollars to free cash flow with the sustainability investments will be heightened as we come through the investment period. Fundamentally, that's because there's a different capital outlay model for this part of our business than there is for the collection and disposal business where you're having to spend capital dollars effectively each day that you service the customer. So with maintenance capital levels meaningfully lower in both recycling and renewable energy we're optimistic that cash flow conversion will be stronger after this investment period.

Bryan Nicholas Burgmeier - *Citigroup Inc., Research Division - Associate*

Got it. And last question for me. The press release called out investment in plastic recycling infrastructure. Maybe just from a high level, is it possible to say what makes that such an enticing market for WM longer term, do you have any thoughts on how the margins or returns could compare to your existing business?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Sure. The investment we made in Natura PCR, this is really about taking film and film plastic and mechanically recycling it. Film has very low recycling rates today. And on top of that, if you look at all of the brands out there, CPG companies have very strong commitments to use more recycled content products. So it's a market where there is a very strong need and we have a strong fit. Also, if you think about the plastics that we collect on the brokerage side of the house. So it felt like a natural fit for us. What you're seeing in the press release are some capital dollars to invest in building out that plant portfolio in Houston and also in the Midwest, and we'll be providing a bit more information on that in April.

Operator

Our next question comes from Kevin Chiang with CIBC.

Kevin Chiang - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

Thanks for the supplemental information here. If I look at your pro forma earnings contribution from these sustainability investments of -- and if I do kind of a quick back of the envelope math, it seems like you'd get to something like 15%, maybe even upwards of 20% of your earnings coming from recycling, RNG. And then the payback looks phenomenal. ROIC is obviously very big. But I guess how do you think about the underlying earnings volatility of the business now that it becomes more commodity exposed once these investments are completed?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes, I can speak to the commodity volatility on both sides of the business. So on the R&D side of the house, we've talked a lot and I mentioned it today that we have 40% of our volume that's really tied into fixed price markets. And then we also have the ability on the transportation side of the house to leverage WM suit and tie it into ERINs. We're really -- sorry, RINs, conventional RINs, we're really being thoughtful about how our ramp looks long term and how to tap into those fixed versus transportation markets. And so we'll give a bit more information on that in April. But suffice it to say that it's something that we're tracking very closely, and we have a whole host of options to ensure that we can navigate that.

I think there's very strong fundamentals. If you look at what the EPA did with their announcement on the renewable volume obligation and setting a 3-year pathway. So it really shores up where we're headed on the renewable natural gas side of the house. On the recycling side of the house, I think what's interesting is if you look at the $240 million in EBITDA, 60% of that is really independent of commodity prices, and that really speaks to the fact that a big piece of it is coming from labor and labor improvements.

35% exiting the quarter in labor cost per ton improvements at our automated facilities. And then revenue quality. And a great example of that is how we're able to take mixed paper and remove cardboard from those bales and sell it at a higher price premium. And that's independent of market prices. So a lot of what we're doing will help us inflate ourselves from those wings.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I might add one thing because in your question about adding volatility, I mean, I guess you could say that. But look, as I said, and Tara has mentioned as well, this gas is coming to us regardless. I mean, this is gas that is produced by these landfills as a result of MSW going into them. And about half of it is monetized in some form today. All we're doing here is taking advantage of a situation that was presented to us but also taking advantage of our natural gas fleet and turning that 50% that isn't monetized into some value add for shareholders.

Does it add some volatility? I guess it adds some, although Tara has gone through a part of her answer to question earlier was to -- that we are looking to take some of that volatility away by fixing some of the pricing. But I think there's this view that why would you add a volatile business here? And the answer is we're just taking gas that's being produced by these sites and turning it into a very, very profitable revenue stream with very, very strong paybacks.

Kevin Chiang - *CIBC Capital Markets, Research Division - Executive Director of Institutional Equity Research & Analyst*

That's great color, Jim. That's very helpful. Maybe just my second one just maybe on some of the automation you were talking about on the customer service side. It sounds like, obviously, some huge wins there. Just wondering what you're seeing from -- I guess, the labor cost savings, would you track, I guess, like a Net Promoter Score or like a customer churn, as you roll that technology out and maybe do some of the friction that some of your customers might have had calling into call centers. Are you seeing other benefits, whether something that promoter score or churn rate that you'd be tracking alongside just the labor cost savings?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

Yes, that's a good question. A few things are happening on that front. One is we've digitized a lot of the customer-facing elements of sort of these transactions. So customers have the better ability to transact with us when and how they want to from a digital perspective. We're seeing that translate to NPS scores, not a surprise that we in the beginning of the year had some dips in our NPS scores as we were challenged on some of the labor and asset fronts that Devina and Jim commented on, but that started to improve in the second half of the year, which has also helped our service quality.

So we're seeing our NPS score start to move the right way in the back half of the year. And we're also, at the same time, seeing the benefits from some of the labor arbitrage. As Jim mentioned, these are not jobs we're moving out. These are jobs that we're not replacing because they're high turnover. And I think Tara and Jim gave good color on what's happening with the recycling and the recycling front with respect to automation benefits. And we've touched on the other big bucket is moving from sort of the traditional manual rear load system to the ASL system. That's another element of automation where we're clearly seeing benefits.

Operator

Our next question comes from Walter Spracklin with RBC Capital Markets.

Walter Noel Spracklin - *RBC Capital Markets, Research Division - MD & Analyst*

And just following up on Kevin's question there regarding -- and to your point, Jim, it is fluctuation, but it's something that can be managed and it looks like you're doing -- you're setting up for a great job managing some of that fluctuation. But I guess investors are -- and you touched on it on your pricing, right? In the solid waste sector, investors are accustomed to price never going down. Yes, it might go up less and the volatility is really just how much more does it go up 1 year to the next.

But with some of the renewable energy fluctuations and recycled commodity prices as you pointed out. I mean, you're getting EBITDA going down this year as a result of those. My question, I guess, is that as you build these out more, is this something that you would consider spinning off while retaining a stake as to kind of separate the 2 so that investors who desire that volatility, want that volatility and willing to pay for the volatility can do so and then those that are -- prefer the more steady EBITDA stream that your company has delivered so well in the past, can focus more on -- is that something that is in the cards in the future? How much have you thought about it? Just curious in that regard?

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Well, a couple -- I think you're making a couple of points here. Just to maybe correct one thing. Price isn't going down, if that's what you were implying. It's not going down. It's just going up by slightly less than it did last year. And to your question about whether we would consider spinning off the RNG business.

I mean, first of all, there's a lot of options for us, and we would never take any options off the table. But what Tara said earlier, which I think is important is we -- part of the value for us is that we like owning the gas, we like owning the facilities. And so for the time being, the answer is we're going to develop these ourselves. We're going to -- and we're going to see the full benefits come to ourselves. And we'll do everything we can to try and mitigate the volatility but we like owning the gas itself. We like being in a position -- I've been in a position in the field where I managed the landfill where we didn't own the well field.

And that was not a great position to be in, having been there a number of years ago. So we like being in a position where we manage the well fields that produce the gas. Not to say we wouldn't consider that down the road. But for now, we're kind of in our infancy and we're going to own and develop on our own for now.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I was just going to add on the recycling side. If you look at that separately from the RNG comments you made, if you went back 5 or 6 years ago and looked at the commodity price versus what the earnings stream was out of the recycling facilities was much different. But in my prepared comments, you're at $47 a ton. We're still seeing strong earnings and returns in our -- in all of our MRFs, not to mention the fact that when you were to carve out the automated plants, which is only a small portion, we're going to add to that next year, as Tara mentioned, those margins are even higher. So I would argue that we've taken out a lot of the volatility in the recycling business, and that's why you continue to see our conviction in those investments going forward.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes, I'm glad you made that point, John, because did change a lot of these contracts from 4 years ago, and I think that's your point.

Walter Noel Spracklin - *RBC Capital Markets, Research Division - MD & Analyst*

No, that's absolutely -- that's clear that you've done a lot of good work in terms of restructuring those contracts to produce some of that volatility. Just curious in terms of the spinout, but address that question.

Operator

Our next question comes from Sean Eastman with KeyBanc Capital Markets.

Sean D. Eastman - *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

First one, I just wanted to reconcile the -- there was a 35% labor costs per ton reduction on the recycling footprint mentioned, also a headcount reduction of, I think, 127. Just trying to reconcile those 2 data points.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. So John mentioned in his remarks, the 35% reduction on our automated plants on labor cost per ton, and that's what we saw in Q4. And then that 137 number is related to the headcount attrition related to automation in 2022, and we're expecting $200 million in 2023.

Sean D. Eastman - *KeyBanc Capital Markets Inc., Research Division - Senior Equity Research Analyst*

Okay. Helpful. It's impressive. And then the other one is just kind of nitpicking here, but the -- some of the inputs on the guidance for this year, $70 OCC, $2.30 RIN price. Could you just tell me where those numbers are today? And if you can, just how to think about sensitivity to the extent we don't climb up to those numbers?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes. So just to clarify, it's $70 per ton in our commodity basket, not on OCC, just to -- yes, so $70 a ton number for 2023, exiting December of this year, just north of $50 a ton. And we're seeing some signs on the plastic side is a great example where we're seeing plastic pricing increase a bit. And we've seen that uptick related to, again, CPG companies trying to meet their sustainability commitments on using recycled content. So we expect, if you look at that ramp through Q1, Q2, Q3, we'll start to see that ramp over the quarters when you look at how commodity prices will move on the recycling side of the business.

And then on the renewable energy side of the house, that $2.30 RIN price, exiting 2022, RIN prices were higher. We've seen a bit of a dip on RIN pricing that definitely recognizes what we're seeing in the market today and where we expect it will hedge throughout 2023. Just remember, 40% of our offtake is fixed. So the other 60% is exposed.

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

And I would just say the midpoint of our guidance anticipated the commodity values that Tara just went through, the downside has contemplated some of the downside risk should those values be less than what we are currently predicting.

Operator

Our next question comes from Michael Hoffman with Stifel.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

I just want to make sure this is very clear. You are not seeing unit prices come down, the rate of change in price is narrowing because inflation is coming down.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

No, sir. Michael, no, we are not.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. And you are in a position today where you have a real spread against the internal cost of inflation.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Yes. That was my earlier point. This gives us -- it gives us that spread. We had essentially no spread for the last 18 months.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. So then I want to dig into -- I think there's more power in the solid waste business than maybe everybody's understanding. Are you about 80% of your EBITDA, 80%, 85% is solid waste and then 15 to 20 is sustainable investments in recycling. Is that about the right proportioning?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

The way that I would answer the question, Michael, is if you look at our outlook for the year ahead, we're implying growth from the solid waste business of about $475 million. And that rivals the highest levels of growth that we've ever seen in our history. And so what we focus on in terms of measuring solid waste performance is our ability to fundamentally grow that business over the long term, both in terms of the pricing execution and our strong focus on operating cost efficiency and those things are what are driving that $475 million target.

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I would tell you, Michael, I think Devina and I shared this. We all do on OpEx. But I think to Jim's point, we were kind of arm wrestling with it, I forget the phrase used, Jim. I think the efforts that we undertook last year and what happened in the last 2 quarters, in particular, the fourth quarter make us feel really good about what's happening on the solid waste side and some of the commentary was about price and yield and the movement. But when you see OpEx, our guidance on OpEx moving the way it is for next year and the EBITDA improvement and Devina said what the strength of the solid waste business is we feel really good about how we're entering '23.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

And I agree. I'm trying to get there by backing into numbers a little more precisely. That's why I was asking about the mix. If I'm right, and you're in the 80%, 85% is solid waste, you're going to end up with a 9% to 10% growth in solid waste in '23 in EBITDA. And like 90 basis points, maybe even 100 basis points in the solid waste business and then you give a little bit of a back because of the other stuff.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

We are predicting that strong solid waste growth coupled with some SG&A margin expansion. Those are really the 2 levers for next year's overall EBITDA growth.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. Okay. Well, I tried. I would -- would you all consider starting to segment where you show us recurring core solid waste versus the alternatives? So we start to be able to track this better.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

We always focus on making sure that you guys have the best information available, and we'll continue to try and meet that goal, and we'll step back and look at our disclosures and ensure that they're appropriately robust. We think that they are today, but we know we can always get better.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Okay. Baseline capital spending at 2 to 2.1 comes out at 9.9% of revenues, which is below your long-term average. And it's a little surprising given the vendor side of the world is talking about a lot of inflation in their side of the business still. So I'm trying to understand why that baseline -- and it's essentially flat, sequentially in absolute dollars. So what -- I don't think you're underinvesting in your business. I know you're not doing that. But can you talk me through why that's settling the way it is?

John J. Morris - *Waste Management, Inc. - Executive VP & COO*

I think, Michael, if you look at the inflationary pressure and the performance on the revenue side related to that, we've been also very sensitive to the fact that capital shouldn't just necessarily go up because revenue is. We're looking at it by line of business and what's happened from a volume perspective. And I think that's what you're seeing part of the leverage there. On the supply side, Michael, I would tell you, this was a challenging year in terms of juggling CapEx mostly because of the truck-related issues that we had. So '23 will be more balanced, but I think you're seeing the sub-10 number as a result of our discipline around capital dollars.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

The other thing I would point out is we did pull ahead some capital into the fourth quarter. And as a result of our ability to do that, we moderated our outlook for 2023 capital slightly from our original expectations. Should we see a need to adjust that further as we get into the year and perform well as we expect to do, particularly in the solid waste business, we might take some steps to accelerate capital that much further. But this is about strong execution on capital discipline, combined with our ability to ensure that our price isn't just addressing the operating cost side of the business, but also capital inflation.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Right. Last two for me. Tara, the $500 million of EBITDA in RNG in 2026, how much of it is fixed versus spot?

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

Today, we have 40% fixed based on the roughly 4 million MMBtu, and so that is what is fixed today. We're working on fixing more of that longer term.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

But -- so you don't have a goal for that $500 million? I guess that's what I'm trying to ask. What -- how much of it.

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

We have a goal. We'll give you more information on that in April, Michael. We have a pathway to have a portfolio mix longer term.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

And will you give a sales when you do...

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

(inaudible) in April.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

And will you talk about sales in April as well, so we can model this right?

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

You're talking about revenue, yes, revenue on the RFP business? Yes.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Yes, yes. I mean in the supplemental document, we have the EBITDA and the free cash, but they don't have revenue. So we're all guessing what that means to our model.

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

You can -- I think you could figure it out based on the $26 per MMBtu number we gave you...

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Suffice to say, the margins on this business, Michael, and whether you're looking at margins on the EBITDA side are 70%-ish maybe 75%. I mean, we'll get -- as [Sisal] give more detail on in April. And then as Devina went through, the cash conversion is tremendous, too. So it's why this business -- why we're so excited about it. And nobody has asked a question about M&A, but I did mention that I'd rather do a 3x EBITDA investment than a 10x EBITDA investment where there's some uncertainty about integration. So we'll talk about revenue and what it means. But these are hugely high margins on the EBITDA line with these R&D plants.

Michael Edward Hoffman - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Group Head of Diversified Industrials Research*

Last question for me. In '19, you told us that the salvage business would compound at 5 to 7 EBITDA free cash. When I add in the $740 million by '26, will that new baseline still compounded by the aggregate number, 5 to 7? Or does that 10% increase dilute that compounding, the aggregate compounding?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

It's a great question, Michael. And what we're doing is working to segment these parts of the business very clearly so that we can articulate the level of growth that each of them is expected to have. The solid waste business has outperformed that 5% to 7% target that we established, and we couldn't be more proud of those results.

In terms of what's happening in the RNG and recycling businesses, we're talking about a new step level change in our free cash flow generation for the business. Our ability to grow that. I think Tara has done a great job of articulating the fact that this opportunity and what's outlined in the supplemental deck is just a starting point for us. Our portfolio provides tremendous upside opportunity from here. Our ability to say whether that's 5% to 7% or some other number, that will come as we further articulate our plans for building out the total addressable market that we have across our landfill network.

Operator

Our next question comes from Michael Feniger with Bank of America.

Michael J. Feniger - *BofA Securities, Research Division - Director*

Thanks, everyone. I know we're over. So I'll just keep it short. Tara, apologies if you touched on this, but why has RINs rolled over in the beginning of this year? And any policy actions that we should be monitoring that helps get that RIN recovery to that 230 for the full year?

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

Yes. I think the important thing to remember here is that earlier in -- really in December of '22, EPA came out with their -- that rule, which on the positive side, set a 3-year framework for renewable volume obligations, which for us for the long term is positive because at the end of the day, it really sets the standard for the program and the RIN pathway for us. I think there's been a little bit of speculation in the marketplace around whether or not those were the right numbers that EPA issued. We're confident that come June when EPA issues their final rule, there'll be more clarity. So I think that's a little bit of what you're seeing. But long term, strong fundamentals on the price side related to RINs.

Michael J. Feniger - *BofA Securities, Research Division - Director*

And just, Devina, the last 4 to 5 years, I think your EBITDA margins have been in the tight range of 28% to 28.4%. You are now guiding for 40 to 80 bps, so moving up there. Just can you quantify how much of a headwind is there on the margin for RNG and OCC in 2023 based on the guide?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

It's 10 to 20 basis points.

Operator

Our next question comes from Stephanie Moore with Jefferies.

Stephanie Lynn Benjamin Moore - *Jefferies LLC, Research Division - Equity Analyst*

We'll keep it brief. And kind of just a continuation of the last question. Just wanted to talk about what you're seeing from a pricing standpoint in your renewable energy business. I know that does include RINs, but it does include some other factors as well within your business. And then longer term, I know near term, Devina, you just kind of discussed what the EPA standards and RIN pricing. But is there any kind of risk of maybe a supply-demand in balance with more supply at some point as more and more of, certainly you guys but also your competitors also bring these renewable natural gas facilities online, just what that can mean for pricing, not necessarily this year or next, but longer term?

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Sure. I'll speak to the price side, and this is a footnote in our press release, but we did see pricing come down in the 3 categories slight decline on the power side. And as you can imagine, we saw some record power prices related to some of the dynamics in 2022 related to weather and whatnot. So that's reflected on the power side. On the natural gas side, natural gas pricing has come down. We were north of $5 in 2022 and now coming in and around 360, that's what we're guiding to. And then on RIN prices, again, 230 is what we have in our guidance. And I think I just went over a little bit of the dynamics there.

As far as the supply and demand dynamic, I think what's really important to note on the renewable natural gas side is there are 2 markets, and they're quite robust. The first is on the transportation side, which is where we generate D3 RINs. And for us, we're in a unique position. Jim has mentioned this before, where we own our own fleet, so we're able to capture more of the value, and we have robust discussions with obligated parties. So we're able to trade those RINs and have a long history with that.

At the same time, you have this voluntary market that exists where many, many public utilities have come out with announcement where they need to decarbonize their own portfolios and the fastest way for them to do that is to buy renewable natural gas and buy renewable natural gas at a price premium. And again, we'll give you more information on this in April, but we feel really positive about the options that we have for each of those.

Operator

Our next question comes from Stephanie Yee with JPMorgan.

Stephanie L. Yee - *JPMorgan Chase & Co, Research Division - Analyst*

I just wanted to come back to the 2023 guidance overall, and just ask whether you're assuming a recession in the guide or maybe just a slowing economic environment. And I guess you could probably see this most reflected in the volume guidance range. So is the low end of the range at kind of negative 1.5%, embed some conservatism on the economic environment.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

I wouldn't say that any of us are macroeconomists. So whether we're projecting a recession or not is hard to say. But we are projecting some softness for sure. We saw some softness in our volume numbers, as I mentioned, probably particularly in roll-off for Q4, and that's continued a bit in January, albeit our numbers were a little stronger volume-wise in January.

I think if we try and read those tea leaves ourselves, and we're all reading as much information as we can, it feels like there could be some type of slowdown, especially as the consumer eats through all of their savings. But I am -- the last thing I am as a macro economist. So I can't sit here and tell you, yes, we're going to see a recession next year. We're just having to manage our business to our own best abilities. And that's why we have taken cost control on very seriously. That's why pricing is still an important aspect of this. And then at the same time, for the long term, these renewable natural gas facilities and automation of a number of these positions makes a lot of sense. So that really is unaffected by any downturn in the economy.

Operator

Our next question comes from Devin Dodge with BMO Capital Markets.

Devin Dodge - *BMO Capital Markets Equity Research - Industrials Analyst*

I suspect we'll get more color on April 5, but could you provide a framework for how meaningful ERIN could be from a WM perspective?

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

So the important thing to remember is it's a proposed rule and EPA will be coming out with our final framework sometime over the summer. I think from our perspective though, you got to look at the 66 landfill gas to electricity plants that we have that we own. And this, we believe, will be a significant revenue stream for us long term. It's a great example of our ability where we have owned these facilities and invested in them and retained the value.

Now we're in a position to optimize the value with this pathway. So really waiting for a bit more color from EPA on what their final framework is going to look like, but really optimistic. Again, no incremental CapEx on that potential revenue stream.

Devin Dodge - *BMO Capital Markets Equity Research - Industrials Analyst*

Good color. Okay. So maybe on the same thread, do you think ERIN could impact the development pipeline for landfill RNG projects? Or do you still expect RNG to be the most desirable landfill gas project, assuming the site is suitable for it.

Tara J. Hemmer - *Waste Management, Inc. - Senior VP & Chief Sustainability Officer*

Yes, great question. I think we're -- first and foremost, we're really confident on the path that we're on with the 20 projects that we have in the deck. And we're actively looking at our portfolio. We're going to make the best economic decision, the best environmental decision. And the good news is we have a lot of options here. I mean that's something that Jim said earlier on, good, really good or great. We view these frameworks as great for WM. So we're going to evaluate what makes the most sense for us long term.

Devin Dodge - *BMO Capital Markets Equity Research - Industrials Analyst*

Okay. And then maybe just one kind of more detailed question. But in Q4, we saw that core price and yield in the collection and disposal business, they really converged, which is great. But it was a much tighter spread than we've seen in recent quarters. And then the 2023 guide suggested would widen back out again. Just can you provide some color on some of the factors that impacted that spread in Q4.

Devina A. Rankin - *Waste Management, Inc. - Executive VP & CFO*

Yes, it's a great question. And when we wish we had a specific science towards being able to predict. The Q4 results were best ever in terms of the difference between core price and yield. And in large part, that speaks to the strong churn that John mentioned during his prepared remarks, the 400 basis point improvement there is a really strong indicator that price is holding with our customers and that we're doing -- I'm sorry, the comment was on rollback, not on churn, but our churn has been really strong as well.

And our ability to hold on to every core price dollar and convert that to yield really was the best we've ever seen. In terms of our ability to predict that we'd still see those levels in 2023, I think it actually goes back to Stephanie's question earlier about the macroeconomic outlook. We used our long-term averages of converting our core price dollar to yield rather than the fourth quarter launch pad. Because we view the macroeconomic environment is a little more uncertain than it is today, though we are seeing those signs of softness that Jim has done a good job of articulating. We do think that all indicators point to a soft recession in '23, and we didn't want to overpredict our ability to convert core price to yield in the year ahead.

Operator

And I'm not showing any further questions at this time. I would now like to turn the call back over to Jim Fish for any closing remarks.

James C. Fish - *Waste Management, Inc. - President, CEO & Director*

Okay. Thank you. Well, we ran a bit long today, but we had a lot to cover. Thank you for your patience. Thanks for joining us, and we will talk to you next quarter.

Operator

Thank you. This concludes today's conference call. Thank you for participating. You may now disconnect.