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WM.N - Q2 2020 Waste Management Inc Earnings Call

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OVERVIEW:

Co. reported 2Q20 results. Expects 2020 revenues to decline 4-5% vs. 2019.

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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to the Waste Management Second Quarter 2020 Earnings Release Conference Call. (Operator Instructions)

Please be advised that today's conference is being recorded. (Operator Instructions)

I would now like to hand the conference over to your speaker today, Ed Egl, Senior Director, Investor Relations. Please go ahead, sir.

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

Thank you, Marianne. Good morning, everyone, and thank you for joining us for our second quarter 2020 earnings conference call. With me this morning are Jim Fish, President and Chief Executive Officer; John Morris, Executive Vice President and Chief Operating Officer; and Devina Rankin, executive Vice President and Chief Financial Officer. You will hear prepared comments from each of them today. Jim will cover high-level financials and provide a strategic update. John will cover an operating overview, and Devina will cover details of the financials.

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. The Form 8-K, the press release 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. We will also be discussing our updated financial outlook for 2020. This outlook excludes transaction and advisory costs and post-closing financial contributions resulting from our planned acquisition of Advanced Disposal Services, Inc., which may be also referred to as ADS.

Once we complete this acquisition, we expect to provide an updated outlook.

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 and subsequent Form 10-Qs.

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 second quarter of 2019.

Net income, EPS, operating EBITDA margin and SG&A expense results have been adjusted to enhance comparability by excluding certain items that management believes do not fundamentally -- that do not reflect our fundamental business performance or results of operations, including costs incurred in connection with the pending acquisition of ADS. These adjusted measures, in addition to free cash flow, are non-GAAP measures. Please refer to the earnings press release and the 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 until 5:00 p.m. Eastern time on August 13. To hear a replay of the call over to the Internet, access the Waste Management website at www.wm.com. To hear a telephonic replay of the call, dial (855) 859-2056 and enter reservation code 9164328.

Time-sensitive information provided during today's call, which is occurring on July 30, 2020, may no longer be accurate at time of a replay. Any redistribution, retransmission or rebroadcast of this call in any form without the expressed written consent of Waste Management is prohibited.

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

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

Thanks, Ed, and thank you for joining us. The strength and resilience of our business was clearly demonstrated in the second quarter as our results exceeded our expectations. At the outset of the quarter, governments and businesses across the continent were responding to the pandemic with stay-at-home orders and shutdowns of broad sections of the economy, resulting in sharp volume declines in our collection and disposal business. Our immediate priorities were protecting our employees and providing safe and reliable service to our customers and communities. With a framework in place to achieve those early priorities, we then focused on optimizing our business for the new environment, and we saw measurable improvements as we progressed through the quarter.

Year-over-year declines in operating EBITDA in the collection and disposal business improved each month of the quarter as we were able to successfully flex down our operating costs, eliminate discretionary spending and improve productivity. I'm extremely proud of our team. Clearly, the shutdown of the entire economy had a dramatic impact on the top line of our business. Yet, even with a 10% decline in our second quarter revenues, our team was able to improve operating expense as a percent of revenue by 30 basis points, hold SG&A expenses as a percent of revenue relatively flat and most importantly, deliver 10 basis points of operating EBITDA margin expansion. As we progress through the third quarter, we are firmly confident in our operating model and are well positioned to deliver on the revised expectations we have for the remainder of the year.

Our second quarter results prove that putting our people first so they can take care of our customers, communities and the environment is the right approach to ultimately rewarding our shareholders. Putting people first is fundamental, not just to our ESG philosophy but to our business strategy. On our first quarter call, we discussed the actions we took to protect our employees' health, safety and financial well-being.

We also took steps to support our customers, particularly the small and medium-sized businesses that have been impacted most adversely during the COVID-19 pandemic. We helped our customers rightsize their service levels, temporarily paused price increases, extended payment terms and gave a free month of service to qualifying open-market small and medium business customers. While these actions had a short-term impact on our price metrics, we've strengthened our customer relationships and increased customer loyalty. Our customer churn for the second quarter was our lowest on record at 6.9%.

We've also seen significant increases in our Net Promoter Scores, a measure of customer loyalty. Overall, second quarter Net Promoter Scores increased 82%, and our commercial line of business score tripled. We are now turning our focus to the longer-term to ensure that we come out of this pandemic a stronger, more differentiated company.

At our Investor Day last year, we laid out our plan to continue to invest in technology to enhance our customers' experience with us and increase the lifetime value of a WM customer. At that time, we felt we had a strong plan to achieve some big technology wins over the next several years. However, during this pandemic, several things have become abundantly clear to us. First, our customer service digitalization investments, otherwise referred to as CSD, is unquestionably the right approach. This end-to-end digitalization of our entire customer experience from the first customer contact to the service confirmation will be unmatched. And as we've seen during COVID-19, the companies with a superior end-to-end online model will truly be differentiated in the post-COVID world.

Second, it became very clear to us early in this pandemic that when we all move in unison as one organization towards the accomplishment of a goal, there is nothing we can't accomplish and accomplish quickly. No one within Waste Management thought we could move thousands of employees to a work-from-home environment in 1 week's time but we did. This gave us confidence that we can be more ambitious and agile when it comes to technology advances.

That's why we are now accelerating our efforts around CSD. Using the onboard units, the smart truck platform and our data and analytics capabilities, all of which we've discussed for several years, we will seamlessly connect all the WM functions required to service our customers so we can give them a completely digitalized customer experience. This will put us on par with other great companies and other industries who have separated themselves through their own digitalization efforts. We'll have more details as we roll this out, but we expect to see some early wins this year.

And finally, we're excited about the milestone we reached on the Advanced Disposal acquisition last month. At the end of June, we announced a revised agreement with ADS. Additionally, earlier this week, we and ADS introduced an agreement to -- an amendment to the previously announced agreement with GFL Environmental, and GFL is now contracted to purchase all anticipated regulatory divestitures for $863.5 million. We expect both transactions to close by the end of the third quarter of 2020 once we receive regulatory approval and the approval of the ADS shareholders.

With all the additional work we've done since the deal was announced in April of 2019, we're confident in our projection to achieve more than $100 million in synergies, even though divestitures are greater than we originally expected. We are looking forward to completing this transaction, integrating the ADS team and operations and creating long-term value for our shareholders as we add 3 million additional customers to our platform and service capabilities.

Turning to our full year outlook. Our second quarter results, combined with the early stages of economic recovery, provide greater clarity for our 2020 financial results. This has allowed us to again provide full year guidance based on current economic conditions and before the contribution from ADS. We now expect a revenue decline of between 4% and 5% when compared to 2019, adjusted operating EBITDA margin in the range of 28% to 28.5% and free cash flow approaching $2 billion, again completely exclusive of the impact from ADS. Our impressive cost flexing in the second quarter, combined with the recovery from the reopening of North America, both of which we anticipate will carry into the back half of the year, mitigates what certainly would have been a more significant impact from the pandemic.

In closing, despite the challenging backdrop, we're confident in our ability to continue to meet our commitments to our customers and deliver solid 2020 results. During these unprecedented times, our business model has once again proven its resilience, and we remain focused on using this opportunity and our technology investments to create a differentiated customer experience that puts our customers at the center of everything we do to increase workplace flexibility for our people.

With that, I'll turn the call over to John to discuss our operational results for the quarter.

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

Thanks, Jim, and good morning, everybody. Our team has remained focused on the fundamentals of providing safe, reliable and efficient service to our customers despite the challenging backdrop. Our focus on execution paid off in the second quarter as we improved efficiency across the commercial, industrial and residential lines of business. By calibrating our cost to the current volume environment, we achieved total operating -- total company operating EBITDA of 28.8%, a 10 basis point improvement over 2019.

The volume recovery trend we are seeing is encouraging. Volume declines in the collection and disposal business improved throughout the second quarter. Through the first few weeks of July, we've seen further volume improvements despite certain areas of the country slowing their plans to reopen. We've adopted a proactive approach to service restoration, and to date, we have resumed service for more than half of the commercial and industrial volumes that were suspended with the March shutdowns. While we are seeing some markets recover faster than others, we're encouraged that commercial businesses, the backbone of the U.S. economy, are showing strong signs of recovery.

While residential container wastes have declined from their peak increases, they are still elevated by mid-single digits when compared to last year. This strengthens our case with municipalities as we work to improve the profitability of our residential business and change the structure of residential contracts. It will take some time to reshape this business, but we are making headway.

Turning to landfill volume. External volumes for the quarter were down a little more than 18% or around 13% if you adjust for natural disaster volumes in 2019. Similar to what we experienced with our collection volumes, our landfill volumes improved throughout the quarter with June being the best month, down 11% compared to June of 2019, adjusted for work days and natural disasters. Looking specifically at MSW volume, which tends to be the most resilient and a good indicator of trends particularly during a recovery, the quarter was down right at 9% while June improved to a 3.5% decline.

Moving to pricing. We have taken intentional customer-focused steps to help our small business customers in this tough economic climate, which we believe will generate long-term customer loyalty, and we're already seeing signs of it in our numbers. As Jim mentioned, our Net Promoter Score has increased. We took these steps knowing that there would be downward pressure on pricing metrics in the second quarter, but we see these consequences as short term as we stay disciplined in executing our pricing programs.

Second quarter core price was 1.3%. This includes almost 3% core price in the landfill business and 3.1% in the transfer business as we continue the positive momentum with post-collection pricing initiatives. We remain committed to the pricing discipline we have worked hard to instill to cover our rising costs and protect our margins. In July, core prices started to trend back toward pre-pandemic levels.

Our impressive cost flexing drove the solid results for the quarter. We improved operating expenses as a percentage of revenue by 30 basis points compared to the prior year. The team increased efficiency across all collection lines of business, along with significantly decreasing overtime hours, reducing routes and optimizing the fleet. Overtime costs decreased 30% in the collection line of business in the second quarter, driven by reductions in the commercial and industrial businesses.

With regard to maintenance, our focus on asset utilization for our fleet is yielding results. We reduced downtime by 23% in the second quarter, achieving 99% fleet availability. Year-to-date, the improvement in downtime hours has resulted in $5 million of savings. We're also flexing down our post-collection operating cost by reducing variable expenses such as overtime and heavy equipment operating hours. Second quarter overtime costs decreased by 39% across the landfill, transfer and recycling businesses. The team has done a good job of managing costs through this pandemic, and we expect that to continue through the second half of 2020.

And lastly, let me briefly touch on recycling. The good news is that in the second quarter, we continued the trend of improving operating EBITDA for the business. For the quarter, we improved the bottom line by nearly $8 million, driven by a stronger blended commodity rate of $57 per ton, our focus on operating expenses and continued progress toward a fee-for-service model. We remain confident that our strategy for recycling, including our recent investment in MRF technology in Chicago is pushing our recycling business toward operational, environmental and economic sustainability.

So overall, our second quarter results exceeded our expectations as we demonstrated our ability to proactively manage our operations in uncertain times. I am extremely proud of the hard work of the men and women on the front lines who were instrumental in flexing costs down while continuing to provide high-quality service to our customers.

And with that, I'll now turn the call over to Devina to further discuss our second quarter financial results and full year outlook.

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

Thanks, John, and good morning. We're pleased with our second quarter financial results, which reflect the resilience of our business model, the strong execution of our frontline team members who safely and efficiently serve our customers and communities each day and the solid proactive steps our team has taken to manage costs and capital expenditures in this dynamic environment. Our strong performance in the second quarter positioned us to deliver on our top financial priorities of strong adjusted EBITDA margins and robust net cash provided by operating activities and free cash flow.

As we started to assess the impacts of COVID-19 on our business several months ago, we quickly focused on the EBITDA margin impacts that revenue declines in our highest margin industrial, commercial and landfill lines of business might have on our near-term results. We initially estimated that 2020 adjusted EBITDA margins could be impacted by as much as 100 basis points. In the second quarter of 2020, which we expect to have the toughest revenue comparisons of the year, we managed cost to deliver an adjusted EBITDA margin that meaningfully exceeded those initial expectations. With the benefit of this strong performance and our economic outlook, we now expect 2020 adjusted EBITDA margin to be in the range of 28% to 28.5% or flat to down 50 basis points on a year-over-year basis.

Our strong adjusted EBITDA result is the largest single contributor to our cash flow results in the second quarter. Our net cash flow from operations was $856 million or about 24% of revenue in the quarter. As we saw at the end of March, there is pressure on working capital from a slowdown in customer receipts, which we attribute to customers taking steps to protect their own financial positions.

We are taking proactive steps to work with our customers to ensure that these pressures on working capital are managed and balances are collected for services provided. In spite of these efforts, we expect that a delay in the timing of cash receipts from customers could create an $80 million to $100 million headwind in the working capital contributions to free cash flow in 2020.

Our operating cash flow for the quarter also reflects the impact of the deferral of payroll tax payments as provided for by the CARES Act. This deferral benefited our current quarter cash flow by about $40 million, and we expect the full year benefit to be $125 million.

Second quarter capital spending was $436 million, $142 million lower than the second quarter of 2019. While we continue to prioritize investments in the long-term growth of our business, we have decreased our capital spending to align with the current economic outlook. The majority of the targeted reductions were the result of adjustments in landfill cell construction schedules and a decrease in the purchase of steel containers. We will not reduce the amount of capital allocated to our fleet in 2020 but are considering the current volume environment as we finalize our planning for truck builds and deliveries in 2021.

At the beginning of the second quarter, we targeted a 10% decrease in capital spending from the initial range of $1.7 billion to $1.8 billion for 2020. The team has worked hard to execute on this plan for focused and disciplined reductions in capital expenditures, and in spite of the volume recovery that's tracking above our prior expectations and our plan to accelerate the pace of CSD, we expect to deliver on this goal and have revised our 2020 outlook for full year capital expenditures to between $1.55 billion and $1.65 billion.

In the second quarter of 2020, our business generated $423 million of free cash flow. Despite the challenges from COVID-19, our cash conversion was in the low 40% range, an increase compared to the second quarter of 2019.

For the full year, we expect our solid operating performance and disciplined capital spending to yield free cash flow approaching $2 billion, excluding the impact of ADS. As a reminder, when we originally established our 2020 free cash flow outlook, we excluded impacts of ADS, including advisory and integration planning costs, from the target. We plan to provide a more complete view of the free cash flow impacts of the acquisition post close. Through June 30, our operating cash flow and free cash flow included $45 million paid for integration planning efforts.

Our strong free cash flow positions us to invest in our business and return cash to our shareholders. In the second quarter, we paid $230 million in dividends. We remain fully committed to our dividend program, a strong balance sheet that provides certainty through any economic cycle and balanced allocation of remaining available cash to strategic acquisitions and share repurchases. In the near term, as we further develop our outlook for volume recoveries and position ourselves for a successful close of the ADS acquisition, we will continue to conserve cash and focus on a modest deleveraging towards our long-term targeted range of 2.5 to 3x total debt to EBITDA.

Turning to SG&A costs. Second quarter SG&A was $353 million, a decrease of $32 million compared to the same period last year. SG&A as a percentage of revenue was 9.9% despite the significant revenue decline in the quarter. These results include lower incentive compensation accruals as well as the steps we have taken to reduce discretionary spending in response to business impacts related to COVID-19.

Even as the business environment begins to improve, we're maintaining extreme discipline in evaluating our ongoing level of spending for nonessential costs such as consulting, travel and entertainment. Our cost management actions were partially offset by an increase in our bad debt expense of $12 million in the quarter. In light of the trend we have seen in our receivables and the acceleration of CSD which will increase SG&A spending in the back half of year, we expect full year adjusted SG&A to be slightly higher than 10% of revenue. We're confident we're on the right path with CSD to continue to differentiate our service and provide long-term value to our customers and shareholders.

Finally, our strong balance sheet and liquidity position us well for the current economic environment as well as funding the acquisition of ADS. Current and forecasted post-acquisition leverage ratios are well within the financial covenant of our revolving credit facilities, and we have more than $3 billion of available capacity under our primary revolving credit facility. Additionally, this week, we closed on a $3 billion 364-day revolving credit facility that positions us to immediately fund the transaction at close and then look for the right window to access the capital markets for long-term financing alternatives.

Our solid financial results this quarter demonstrate both the resiliency of our business and the success we are having in dynamically managing our costs. I want to thank the entire Waste Management team for their hard work, which allows us to deliver on our commitments to our customers, communities and shareholders.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from the line of Brian Maguire, Goldman Sachs.

Derrick Laton - *Goldman Sachs Group, Inc., Research Division - Associate*

This is Derrick Laton on for Brian. I appreciate the color and the details you provided so far on the exit rate volumes for 2Q and how things were looking in June. And it sounds like things maybe are still sequentially improving through the first 2 weeks of July. But just hoping maybe if you could quantify any of those numbers and amongst the different lines of business, if you could.

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

Sure, yes. We are, to your point, seeing July continue to accelerate, albeit at a slightly slower pace. I mean, look, this kind of went from 0 to -- not 70 miles an hour, but probably 0 to 60 miles an hour pretty fast, and now we're moving back towards 70 miles an hour.

The one area that John focused on was really MSW. That has really been impressive. The second area that's -- we're down 3.5% in MSW. The other one that was surprising to us because we expressed some concern about it in the first quarter was commercial. And at its low point, the commercial line of business was down as much as 15%, even more in some areas, and that has returned to down kind of 5% or 6%. So it's really rebounded, and it continues now through July to show improvement.

The one that kind of is starting to jump a bit right now that's good for us is special waste. It had been down -- even through June, it had been down pretty significantly on a year-over-year basis. And when I looked at the rolling week numbers, which compare to prior year, just yesterday, those numbers are starting to really show improvement in special waste. So we're now actually up double digits there in special waste, whereas we had been down deep in the double digits previously. So we are pleased with the progress we're showing on virtually all of our waste streams in our collection lines of business.

Derrick Laton - *Goldman Sachs Group, Inc., Research Division - Associate*

I appreciate the details. Certainly, it's encouraging. And then maybe if I could just get one follow-up. Just the updated guidance for the year, for 2020 with the revenues expected to be down 4% to 5%, just hoping maybe if you could help us better understand kind of the moving parts there. Does that basically assume that pricing yields will hold flat from 2Q levels for the rest of the year? And maybe just the moving parts between pricing yield and volume and what your expectations are there.

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

Yes, it's a great question. We're not specifically giving outlook for the back half of the year on the price and volume component. But what I would say, Jim just gave tremendous color with regard to the improving volume outlook. And I think that, that coupled with the fact that the Q2 execution on pricing was intentional and focused on being customer-centric, and so we certainly expect an improving result in the back half of the year on price.

So you can expect that the yield component gets back to closer to normal levels, our outlook for 2020 and an improving volume trend. When we look at the back half specifically, we're projecting that you have a decline in revenue of -- in the range of 3.5% to 5.5%. And that's more significant in Q3 and then tapers in Q4 to about half the Q3 levels what we're projecting.

I do want to point out, particularly given what we're seeing in the market today, that fuel prices did have a 2% impact on the revenue line in Q2. Difficult to predict that specifically. We weren't predicting any added pressure on the top line from fuel in the back half of the year, so that's certainly out of our control and not necessarily representative of the strong execution of the business, which we're really encouraged to see the momentum that we saw at the end of Q2 and beginning into Q3.

Operator

Your next question comes from the line of Walter Spracklin, RBC Capital Markets.

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

So I'd like to start with margins. Obviously, you've guided to impressive cost control, doing much better than what you had thought you would be able to do, which is great. Just curious on the structural nature of this. When volumes start to come back, can we see operating leverage such that you can maintain -- I don't know, Jim, you alluded to a better organization or a strong organization post COVID. Does that mean you can run and you expect to run at margins above historical trends once Advanced Disposal is integrated? Or would you see that when volumes come back, resources would have to come back as well and get you back to a more normalized kind of historical levels?

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

Yes. Walter, I'll start this one. I think it's a really interesting question. Rather than specific on post-ADS margin, I'm going to focus really on WM base business because we're going to wait to give any financial outlook for the integration of ADS until post close.

So when we think about the strong margin execution in the second quarter, I mean, hats off to our operators and the frontline for doing a tremendous job, and I think what you saw in those results is that we got the most expensive hour out of the route and we got the most expensive truck off of the street. And so through efficiency, through improved maintenance, improved downtime, there were really fundamental tremendous improvements in the operating nature of the business. And those are things that the team is working hard to see how we hold on to in a post-COVID environment with improvement in volume outlook in commercial and industrial collection. I do think the residential collection margin impacts that we've talked about, we're focused more on the price side of that equation to be sure that we recover the increase in our cost to serve, but looking for efficiency in that part of the business as well.

In terms of the strong execution in Q2 and how we think about that for the remainder of the year, I think of the improving volume trends and price. Price is really an important piece of that because we delivered this margin result in spite of having lower contributions from core price, which we see really flow all the way through on margins, so particularly impressive when you consider that aspect.

There are certain elements of the cost structure that increase in the back half of the year. As an example, fuel tax credits were something that we got a benefit for in the fourth quarter of 2019. Instead of that being a second half of the year phenomenon this year, those are spread -- those benefits are spread over the course of the year. So that has some margin pressure in the back half, as does the increased acceleration of spend on CSD, which Jim spoke about. So really strong execution in operations, and we expect that to continue particularly with the improving volume backdrop.

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

Okay. That's great and encouraging as well. So moving on to price. I know you just alluded to it.

Can you speak to what happened with core price? As you mentioned, you did not get the benefit of core price. And what is the risk? And how does it work that -- you implied here that it is going to come back. Does that just come back because of the overall macro environment and easier to drive forward? Or is there something more detailed to that in addition to what you had mentioned with regards to residential and recapturing some of those higher volume through higher pricing?

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

Yes. I mean, I think there's a couple of points to make here with respect to price, and maybe the first one would be to your last point there. I mean there is this price discipline that we've talked about this morning that remains. We certainly haven't lost any price discipline. But we felt like that it was absolutely the right approach to take during the quarter to pause on these price increases and some fees and also to really help small business emerge out of this by giving them a free month of service.

I mean that's -- I can't imagine if I were a small business owner sitting in my living room opening my mail and getting the -- my big price increase from Waste Management. That would not have gone over well with me as a small business owner. So it was unquestionably the right approach to take in Q2. And honestly, into Q3, that will persist to a lesser degree because some of these small businesses have not reopened.

And what we told them with respect to the free month of service was that we would give you your free month of service once you reopen. So I'm sitting in downtown Houston, and there are a lot of small businesses that have not opened in the central business district here. I suspect it's the same in other big cities.

So we will still see some of that weakness in pricing, but the point that I think Devina was really touching on was that when you think about price discipline and once we get past this short-term COVID effect, the price discipline is still there. John talked about it, too, in terms of landfills and transfer. That is something that is truly ingrained in our culture, and so we don't kind of kick that to the curb. When COVID goes away, that becomes immediately reestablished. But there is a -- there was, of course, in Q2, a big impact from this more kind of sympathetic approach to these customers, and we'll see some of that in Q3 as well.

Operator

Your next question comes from the line of Sean Eastman, KeyBanc Capital.

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

So compliments on a good second quarter performance here. I just wanted to drill in on the second half. I mean I'm just trying to understand where you see the big swing factors in the second half '20. So visibility has clearly improved around the volumes, but I'm just curious where you think some conservatism is still warranted in that second half outlook and just maybe where you guys don't want to get over your skis just yet as we think about trajectory here from a revenue margin perspective in the second half.

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

Yes. Sean, I'll start that, and then I think the others can add some color. I think the place that we start that discussion is on the top line. And as I mentioned, the outlook for the back half of the year is currently revenues being down 3.5% to 5.5%. When you look at how we finished June and see July coming together, we do think that there's some potential for optimism in the top line results for the back half of the year. But it's appropriate for us to be reserved in going too far in terms of how quickly we start to see the recovery, certainly with the number of case increases that have been seen across the southern part of the United States.

And so that's really where that back half question mark starts, but we feel really good that 4% to 5% is representative of how we'll finish the year.

In terms of the cost part of the equation, it really does come down to the operating cost leverage as the biggest driver. There are certain elements of cost, overtime being one of them, which John spoke a lot about in terms of our ability to flex the number of overtime hours. That translated into $45 million of operating cost savings in the second quarter, and that's a tremendous result. But ensuring that as we see volumes grow back and whether it be the efficiency part of the business, increased traffic on the roads, thinking about how we manage the work day, that $45 million of savings is something that we have our eye on.

Other elements of the labor line, which is the biggest single component of our cost structure, is really where we're focused. The pieces that are in SG&A, we have at hand. I would tell you that the results that you saw in the second quarter, we're confident that we can continue to deliver. As I mentioned, the increased investment in CSD in the back half of the year means that those costs will increase, but that's an intentional investment for the long-term growth and customer-centric nature of our business.

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

Yes. And one quick thing and then, I think, John wants to touch on OpEx, too. But Sean, when you think about the conversation we just had about price, obviously, it was uniquely soft. I mean -- but that softness dissipates over the next quarter or 2 back to much more of a normalized level of price increases and where we've been prior to COVID. So that certainly is upside for us.

And -- but we knew the downside was going to be there, and it was the right thing to do.

And then, of course, volume, which we talked about early on in this call, we think that volume, while it has started to slow from the really steep increase that we saw in June, it still is increasing. And I talked about special waste showing some really nice improvement and then MSW and commercial. Industrial has lagged a little bit. It showed a nice tick up, but we are seeing some differences by geography. And it's interesting when you look at kind of the southern part of our network versus the northern part of our network. The northern part of our network, whether it was the U.S. or Canada, tended to shut down a bit more quickly and reopen a little later. And so we think there's some real opportunity.

I was in Boston a couple of weeks ago. And honestly, Boston, for the first time in -- since COVID, really started -- is starting to feel open. I mean we were in restaurants, eating inside. And so those businesses are starting to reopen. And so while Boston and our New England area is still down relative to some of the areas in the South, that will provide more of a kind of a spike upturn in volume for markets like New England, New Jersey, New York, Pennsylvania.

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

Sean, the only thing I would add to your point about getting over our skis, I think when you look at -- and as Jim mentioned, we're looking at this literally on a daily basis by region, by line of business, is making sure that we continue to hold tight on the reins in terms of adding cost back. And I think when you look in some of the numbers we all referenced in our prepared remarks and even as late as yesterday, looking at the ratio of volume coming back and what we're still able to do on the cost side, specifically overtime, as Devina mentioned, that's the area where we are absolutely focused on.

I will tell you, the ratios of volumes coming back versus overtime is still favorable. And I think that's why when you think about us having the margins we had in Q2 compared to where we lost the volume, which was really landfill, commercial and industrial, for the team to hold that -- to hold those margins, and there's puts and takes, Devina mentioned some of them, it is really impressive. But I think getting out over our skis, that -- we are absolutely focused on making sure we keep the reins very tight on OpEx as we watch this volume shift.

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

Got it. Super helpful. Next one for me, hopefully a little quicker. Could you help bridge us from the down 100 basis points year-over-year margin outlook you provided on the 1Q call to the revised flat to down 50 basis points? Just any granularity between the volume recovery, cost control in that bridge would be appreciated.

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

Yes. I don't know that I can get super granular for you, but what I would tell you is you've hit on 2 of the primary factors. So volume recovery outpaced our expectations, and so that certainly had some upside impact on the margin decremental impact that we had originally predicted. And then cost control, particularly on the operating line, was even better than expected based on what we know the margins of these lines of business to be.

I mentioned overtime specifically. Health and welfare costs are another example where we saw some value to the results. From a granularity perspective, I guess what I would tell you is that health and welfare by itself, as an example, is just one of those cost categories that's difficult to predict, but it had a marked contribution. And around 25 to 50 basis points is what we see as a benefit for the year in health and welfare costs alone.

Operator

Your next question comes from the line of Hamzah Mazari, Jefferies.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

My first question is just around the election. If U.S. tax reform goes away, is that a $300 million headwind to you? I guess pre tax reform, the free cash flow base, I think, was 1 point -- close to $1.7 billion, then it went to $2 billion. That was a big step change. And then you also have bonus depreciation potentially going away, too. So maybe if you could frame for us how to think about that potential tax headwind. Clearly, we don't know what will happen with the election.

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

Yes. I think Hamzah, that last point is really the most important one for us. And rather than get too granular in terms of specifically measuring what we think tax reform could do, I think we all know that we went from a 35% rate to 22%, and so that dramatic change in the tax rate to ongoing business, that's going to have consequences. The bonus depreciation that you mentioned could have consequences.

But just none of us are going to be able to predict the outcome of the election or then any follow-on impacts to tax policy should there be a change in -- a significant shift in who's in office. So I think you've framed it well. I think all of the pieces that you mentioned are the ones that we are paying attention to and the level of impact to cash is something that is significant and therefore, we'll have a close eye on that, but not trying to predict it at this point.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

Got it. Understood. And then just on customer churn, it was pretty good. Traditionally, half of customer churn for the sector has been bankruptcies. And so with stimulus running out, I appreciate you guided revenue growth down 4% to 5%. But do you think that we're out of the woods on commercial? Specifically, do you think that small business bankruptcies are going to be a potential risk as you think about your revenue growth over the next 12, 13 months? Anything you're hearing from your customers? Or I realize you don't have a crystal ball, but -- so any comments you can make high level would be appreciated.

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

Yes. Hamzah, this is John. So we've mentioned early on when we were in the Q1 and the early innings of this that we were seeing cancellations just under 1%. We're seeing that number's crept up to about 2.5%, a little bit north of that, but it's leveled out there. So we're not seeing big numbers in terms of cancellations.

What we have seen and what we talked about is, obviously, folks turning off their service or pausing their service and then gradually turning it back on. I think the one number we can center around is, whether it's commercial or industrial, we are over 50% recovered in terms of units. And honestly, if you look at commercial, we all know education is a fairly good-sized chunk of our -- of the portfolio there. And with the uncertainty there -- actually, our commercial recovery is over 60% if you net out the education facilities, which we all know is kind of a moving target at this point.

Hamzah Mazari - *Jefferies LLC, Research Division - Equity Analyst*

Got it. Lastly, I'll turn it over, just on the ADSW transaction, synergies over $100 million on a smaller revenue base. Maybe you could just frame for us where you're seeing the upside come from. And the $100 million does not include revenue synergies, correct?

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

The -- that's correct. What I would tell you, Hamzah is, obviously, this process, particularly around COVID, has taken a little bit longer. And I guess the silver lining is it's afforded us the opportunity to do that much more work, and we have that much more confidence in our integration plans. And it's given us the opportunity to look more closely at a granular level, not just about kind of the normal SG&A and corporate overhead synergies, but really getting a little bit further into the details and have that much more confidence in what we're going to be able to execute against in the field, and that's really what's driving that number.

Operator

Your next question comes from the line of Kyle White, Deutsche Bank.

Kyle White - *Deutsche Bank AG, Research Division - Research Associate*

I wanted to go back to some of the regional differences that you briefly touched on. Is it possible to describe how the recovery has progressed in some of the states that were first reopened and now are seeing a bit of rise in COVID cases, states such as Florida, Georgia or Texas. Have you seen any stalling in the recovery in these states? Any sort of declines in recent weeks?

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

So it's an interesting question that we expected to be asked today. When I look at our commercial line of business, and I look at those states that you just mentioned, so the big 4 kind of in terms of spike -- case spike have been Texas, Arizona, Georgia, Florida, right? And so when I look at -- 3 of those are our best 3 in terms of year-over-year comparisons. Our best 3 in terms of year-over-year comparisons right now are Texas, Georgia and Arizona. Those are the best 3 out of 17 areas. Those are the top 3 in terms of commercial yards year-over-year comparison.

So I would tell you that the spike -- and when you walk around Houston, what's happening is that everybody is wearing a mask. But businesses have not, all of a sudden, going back to April or May. They're staying open, but people are just more diligent about wearing masks. And we're starting to see those cases level off. I heard Scott Gottlieb last week on a business council call talk about the fact that you're starting to see, particularly in Arizona and Texas, those cases level off.

So our business is actually quite strong there. And as I said just a few minutes ago, where we've seen a little bit of a lag are in those areas that closed pretty quickly and then have stayed closed the longest, such as New England, such as kind of the greater Mid-Atlantic area, Pennsylvania. But those are also starting to show some rebound as well, particularly as they start to move where some of these other states already are, which is a reopening of businesses just with kind of a mask rule in place. So we're pretty encouraged by what we're seeing with respect to commercial reopenings. It's the one thing that probably stood out to us the most because we were least certain about it when we discussed it at the end of Q1.

Kyle White - *Deutsche Bank AG, Research Division - Research Associate*

That's very helpful. I wanted to also go back to the pricing discussion a bit. And just I'm curious if you could talk about the competitive environment and pricing behavior, especially among some of the smaller players. Anything notably different recently as a result of the kind of volume impact that some of these players may be experiencing?

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

I mean look, I -- we haven't seen anything over the last couple of months, but I really can only speak to our own price discipline. And I would tell you, as I said earlier, that we are -- we haven't lost an ounce of price discipline. What we -- what you've seen in terms of price erosion, if you want to call it that, was intentional, and that, we will recover. It's just we're driving ourselves to get through this -- hopefully, this short-term impact from COVID.

Operator

Your next question comes from the line of Tyler Brown, Raymond James.

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

Devina, hate to beat on the pricing optics here, but can you isolate the revenue dollar impact that the price increase in fee suspensions had in the quarter?

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

We hadn't specifically quantified that. I mean, I think the best way to think about it is the delta between the yield that we reported and the 2.5% guide that we would have given for the year. And I think that delta is fully representative of what you could say that the price impact was for the quarter.

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

Okay. So not only -- yes? Sorry, go ahead.

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

The only thing I'd add -- I was just going to say, the only thing, this is John, I would add is if you look at the -- if you look at landfill and transfer station, I would point you to that in terms of the -- where we've remained disciplined, I mean. So the impact has really been commercial and industrial, but the other lines of business, we continue to show like performance.

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

Right, right. So not only was there a dollar contribution that was unusually low, but -- and correct me if I'm wrong here, but you also had a bit of a denominator problem. I mean your volumes were down 10%. So I'm guessing that was also a driver in the pricing optics. So I mean, just to be -- I mean, I know there's been a lot of talk about this, but to be just crystal clear, there has not been a change in your fundamental pricing strategy?

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

Not at all.

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

Absolutely not.

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

Okay. And then, John, so I appreciate the resi container weight comments. And I know we talked about this last quarter, but what is the level of urgency around resi pricing specifically? I know you talked that it will take time. But if I take a walk back in history, didn't you guys meaningfully move resi pricing? I think it was around the financial crisis, if I recall. So can this be a material driver in '21?

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

Listen, Tyler, I mean, we've talked about the added weights and the pressure that's put on the line of business. Here's what I can tell you, is that the additional weights that have come via this pandemic are certainly another discussion point we need to have with some of those residential customers. But we started this program before that.

Now I can't speak to what happened back in the financial crisis. I'll trust you on that one. I'm sure we probably had some efforts at the time. What I can tell you is that, and Jim has mentioned this a few times, we've seen, obviously, a lot of pressure on the residential line of business. We've seen margin erosion.

My plan with the team -- and we have this down through the contract, by region, by area, to execute against long before this pandemic started. I will tell you what this pandemic has certainly helped us with is -- when you talk about further moving that line of business to automation, containerizing, being able to capture the waste, being able to price and get paid for the services, including disposal that you provide for, this is certainly an opportunity to highlight that.

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

Right. Okay. Yes. No, that's fantastic. And then just my last one here, Devina. So I know 2021 seems like it's a long way away. But will the CARES Act represent, call it, an idiosyncratic headwind to cash flow next year? Is that something that we need to start contemplating?

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

Yes, that's definitely something that we've got our eye on. The $125 million that I talked about for the CARES Act deferral of payroll taxes, that's something that hits us in 2021 because you effectively have a doubling of that obligation in the year ahead. But I think that yes, it's half of next year -- half in 2021 and then another half in 2022.

What I think is really important though, is that the flow-through impacts -- the really strong revenue acceleration that you should start to see in 2021 as some of the COVID-19 volume impacts and those pricing policy decisions that we made in the second quarter, we anniversary those. I think the flow-through of that to cash flow should help us to offset that year-over-year headwind, but you're exactly right, Tyler.

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

There's also somewhat of a corollary there on -- to the CARES Act with working capital and DSO. I mean we're obviously seeing an impact this year, and that's not unexpected at all or not surprising at all. So you'd like to think that as we get into 2021, the DSO starts to normalize.

Operator

Your next question comes from the line of David Manthey, Baird.

David John Manthey - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Building on a previous comment. Last quarter, you detailed the weekly upward trajectory of your roll-off business as sort of evidence of the improvement you were starting to see, and based on your comments, I assume that trend continued. But in the geographies like there in Texas or here in Florida, where the COVID cases have worsened, are you seeing actual declines in any lines of business? Or were you indicating you're just seeing a leveling off in the pace of recovery?

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

Yes, it's really the latter, it's really the latter. We're not seeing declines in any line of business. We're seeing, as I mentioned, a nice increase in special waste, some of that's through our couple of coal combustion residual projects, but not seeing declines anywhere. It's just, by geography, it's leveling a little bit where we saw big, big spikes up in June, and it's starting to accelerate a little bit in some of those places that were slower to reopen.

David John Manthey - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. And last quarter, you said that 10% of your commercial customers had a change in service and less than 1% canceled. Could you give an update on those data points for the second quarter? Are they in the same ballpark?

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

Yes, Dave. I mentioned earlier that the 1% number crept up to about 2.5% and has leveled off there. It's a little higher than that, to be exact. But what we've seen is that is -- and those are the customers that have been impacted and identified as having a COVID impact. So 2.5%, 2.6%, I think, is about right where we leveled off at in terms of cancellations.

Operator

Your next question comes from the line of Noah Kaye, Oppenheimer.

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

To start with, Jim, you mentioned expecting to see some early wins from the CSD effort that you engaged in, investment in development. But what type of customers do you expect are likely to value those offerings more? Any way to dimension out as well what you think this could contribute to organic growth?

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

Yes. I think there's going to be, in the near term, more of a cost impact, bottom line impact and then more of a top line impact longer term as we truly kind of differentiate ourselves. And it's -- and by the way, it's why we kind of chose to accelerate this. We've talked about it. We talked about it at Investor Day last year, so this isn't a strategy that's unfamiliar to you.

It's just one that we've chosen to accelerate for a couple of reasons. One is that we really felt like we learned that when we do accelerate something, we can make it happen quickly for all -- as I said in my script, all in unison behind it. So I do think there will be some changes in how our customer does business with us, and that will impact us a bit on the cost side. And then over time, we think that, that really starts to separate us from the pack.

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

Yes. Makes sense. And then just to go back to the residential line of business. John, I appreciate your commentary around levers for both pricing and technology investment. But since you've got this very granular plan, can you maybe just share with us the target or goal for your profitability improvement in the residential line of business?

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

So I think what Jim has mentioned and/or Devina on other calls is that we've been sub 10% from an EBIT line, and clearly getting well above that is the direction we're going to go. I see -- I certainly see opportunities to get into the high teens or 20% over time. And we're making some headway. And to be real specific, I probably -- when Tyler asked the question, when I look at -- even for Q2 with the elevated weights, we still, on a same-store sales comparison, made margin improvement quarter-over-quarter in Q2.

So we feel really confident about that plan. And I think the granularity is going to be helpful for us as we look at investment opportunities in that residential line of business going forward to make sure we're deploying the dollars the right way. And I've said on other calls, we don't want to do it for practice. We want to make sure we get the right returns, the right margins and the right protections in those agreements. And in some cases, we're going to have to make some tough decisions. We're fully willing to do that.

Operator

Your next question comes from the line of Jeff Silber, BMO Capital Markets.

Jeffrey Marc Silber - *BMO Capital Markets Equity Research - MD & Senior Equity Analyst*

I know it's late. I'll just ask a couple of quick ones. You talked a little bit about pricing from a competitive perspective. I'm just wondering, are you seeing any smaller haulers closed or under pressure that might provide some M&A tuck-in opportunities?

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

I don't know that I've seen -- or I haven't heard of any that have closed. I have heard of some places where they're running short on drivers. So that's not necessarily a great indication for them. And that -- and I can't tell you whether that is a longer-term trend, which we've talked a lot about previously that gen Z and millennials don't want to drive trucks and so therefore, there's this pressure on the pool. I don't know whether that's it or whether it is -- or what the pressures are coming from. But I have heard that. I have not heard though of any closures.

Jeffrey Marc Silber - *BMO Capital Markets Equity Research - MD & Senior Equity Analyst*

Okay. That's very interesting on the drivers. One number you don't talk about much is internalization. I know it's ticked up the last couple of quarters. Is that because we're seeing less third-party disposal coming in? Or are you truly disposing more of your own collected waste?

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

It's probably a bit of both, Jeff. This is John. I think in the table, it was up about 200 basis points, maybe 180 basis points for the quarter and 190 year-to-date, I might have been inverted, but almost 200 basis points. So clearly, when we're seeing some volume pressure at the landfill, we're always reevaluating what's the best use of our network and those landfill assets. So without having a number in front of me, it's probably a combination of both, some third-party volumes that were -- that went out in Q2 and our decision to backfill some of those volumes where it made sense for us.

Operator

Your next question comes from the line of Michael Hoffman, Stifel.

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

So I'm going to ask the first question a different way. Devina, the original guidance was 2.5% for the year -- yield. You did 2.2% in the first quarter. If you hadn't had the pandemic, what was the budget for second quarter yield? And is that...

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

Yes, we don't necessarily budget, Michael, our yield quarter-to-quarter. We certainly have that 2.5%. You saw some of the early impacts on the Q1 results that you just mentioned from COVID-19 because there were some early steps on fees, as an example, to proactively engage with the customers in the right way, given what we were seeing.

I would tell you we've tried to estimate where we think the yield number ends up coming in for 2020. And it's just a really difficult number because of the impact of units on the measure. But what we focus more on is that core price execution, and we expect healthy recovery in core price execution in the back half of the year.

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

Okay. John, on recycling, if the trend holds, there's an $80 million year-over-year gain in revenues in that business. So when I'm thinking about the 4% to 5% down revenue, I got to account for that. And then I -- and then there's a follow-on question about fuel that I got account for to sort of think about the down revenue.

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

Well, I think, Michael, certainly, there was a bit of a tailwind in Q2 with fiber prices specifically, OCC going up. But as you probably know, we've already seen that retract back. And while we had a good quarter in Q2, I would tell you, just a little bit under half of that was driven by price. The rest of it was really Brent and team doing a great job on managing operating expenses and SG&A and other ancillary costs.

So that's what drove the other half of that improvement. So we're not -- we still think recycling is going to be a tailwind in the back half of the year, not as big though because that revenue number is not going to hold through the balance of the year, we don't think.

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

Okay. And then could you share with us what your fuel -- average fuel cost was in 2Q '20 versus '19 and then what it was in 3Q '19 so we can try and accurately model that, given it moved that much?

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

Ed can get you the specifics after the call, Michael. But what I would tell you is the fuel impact to the quarter was $60 million to the revenue line.

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

In 2Q?

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

Yes.

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

Okay. And then just important clarification on the synergies. Just to be clear, it's a free cash flow number and it's a mixture of OpEx savings, interest expense savings, capital spending. Would presume the interest expense number is up because rates are down versus the expectation. And then there's some incremental gains to be gathered in OpEx and CapEx. That's the way to think about the pieces. That's why you can stand by it.

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

I would tell you, Michael, that obviously, when we recut the deal, which was really a month ago, obviously, there's a reduced purchase price. There's higher synergies that we commented on despite over $100 million more of divestitures. And certainly, there's going to be a lower cost of CapEx, but I'll let Devina speak to the financing piece.

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

Yes. I think what's really important, Michael, is that the $100 million and the confidence in the more than $100 million of synergies is not reflecting our savings in the interest line. The savings in the interest line is what we were thinking about in terms of the returns on this investment getting over our hurdle rate and cost of capital.

We -- it's early for us to be able to speak to specifically how much of an interest savings there might be. But certainly, when we look at the requirement to redeem the bonds -- and on a weighted average basis, those were above 3.6%. And if you compare that to current interest rate, there certainly is some value to be had there. It's just too early for us to say. We are really excited to be in a position to be able to fund the transaction at close, but this will be a phased process for us, and we can't yet tell you what the long-term financing might look like.

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

Fair enough. And then a mechanical question. The votes on the 25th assume DOJ gets that, so there's a consent order not far behind that or about the same time. What happens after that? Do you close it right away? Or is there -- is this a dry and clean close at the end of September? But just mechanically, what are we looking at?

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

I mean I'm not sure I know the answer to that. I mean we -- because there's a number of pieces here involved. But what we did say was this would be the end of Q3, which basically means some time between the 25th of August and the 30th of September, which is a pretty narrow window, and it's hard though to say. While we want to do it on a certain date, because we just don't have enough certainty to say whether we're going to do it at the end of a month or at the end of a quarter, that's not our objective. Our objective is to work through with the DOJ and of course, with ADS and get this final.

Operator

Your next question comes from the line of Michael Feniger with Bank of America.

Michael J. Feniger - *BofA Merrill Lynch, Research Division - VP*

I'll try to keep it short. Just, Jim, I know you guys have moved away from CPI over the years. Can you just remind us of the CPI exposure? I understand you're driving pricing at the residential level in different contracts. But I'm just curious with the CPI. How much of that's in your control really in the next 6 to 12 months?

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

Well, Mike, it's John. I would tell you that if you look at our pricing performance, regardless of what CPI has done over the last quarters, handful of years, we've moved further and further away from that. And I think the example you gave is probably the best one, which is, historically, the residential or franchise pieces of the business have been tied to CPI or some fraction of that. And I think our ability to drive 3% core price in residential, especially in this quarter, is evidence that we're moving further and further away from that.

Michael J. Feniger - *BofA Merrill Lynch, Research Division - VP*

Got it. And just like help me understand. Like we talked about the top line. You guys provided a lot of color on Q3 versus Q4. How should we think of the business as we kind of like exit 2020 with the first half? When we think of your mix of your businesses when -- with residential right now being your highest yield, how does that kind of impact overall profitability going forward?

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

Well, that's a bit of a hard question because there is a lot in the mix here. I mean it is interesting though because -- in terms of a true kind of year-over-year comparative basis, whether you're looking at EBITDA or whether you're looking at revenue or whatever you're looking at, I honestly don't think we get to a fair apples-to-apples year-over-year comparison until the first quarter of '22 because I think '20 -- obviously, '20 is disadvantaged, and then '21 will be greatly advantaged versus prior year.

So what we're kind of looking at is when do we get to a true positive comparison versus 2019. And I think that probably happens some time -- maybe as early as Q2 of next year. It probably won't be Q1, but certainly, Q2 looks like it could happen. Q2 or Q3 is when I think we truly get to a positive comparison versus the same quarter in 2019.

And then to your question about what pieces are going to be moving in the right direction. We've talked about a whole lot of them on the call this morning. Definitely, residential. John talked about kind of sub-10% EBIT margins and a lot of work being applied to that. CPI is not representative of -- really of our cost structure anymore, and so starting to move municipalities away from that price metric for us.

Some of what John has talked a lot about -- I would tell you this is kind of all in John's court. But starting to institutionalize some of the changes that we've seen on the operations side and maybe the same is true for SG&A. There's some expense that we just don't need. We don't need to have as much travel expenses as we thought we did. The Teams product that we use a lot, the Microsoft product is a very, very good product. And so I think that will be a replacement for that.

And then as we think about some of these wins that we've discussed with customer service, digitalization, that will start to really have a positive impact on it. So there's a whole lot of pieces here that go into this. But we think, by the time we get to 2021, kind of mid- 2021, we're going to start seeing some positive comparisons to that 2019 period.

Operator

Our next question comes from the line of Kevin Chiang, CIBC.

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

Just one quick one for me. I noticed that you changed your methodology for core price, and that did result in a revision to your Q1 numbers. I was wondering, was this purely a methodology change? Or did this bring to light any untapped opportunities that you might not have been harvesting before in terms of pricing opportunities as you look ahead here and as volumes continue to recover?

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

This was purely a measurement change. And we have actually made the decision in the fourth quarter and then just made an error in reporting our Q1 with everyone in the work-from-home mode and forgot that we had made the change in the fourth quarter and reverted to our old measure. But the only difference in this is we got more precise data as we've been able to use technology more effectively across the network to measure units. And as we got more precise, we were able to give you a more accurate and representative measure of core price, and that's what we're using today.

Operator

At this time, there are no further questions. I would now like to turn the conference over to Jim Fish for any closing remarks.

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

Thank you. So in closing today, I really want to reiterate what both John and Devina have said. I want to recognize the men and women in our operations around North America. They have not missed a single day since the start of this pandemic, and they are, of course, absolutely essential to keeping all of our streets clean, ensuring that we are good stewards of our environment through recycling, providing a safe, reliable service that is absolutely critical to all citizens. So thank you to all of our men and women in our operations. And thank you all for joining us.

Operator

Ladies and gentlemen, this concludes today's Waste Management Second Quarter 2020 Earnings Release Conference Call. Thank you for participating. You may now disconnect.
