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OVERVIEW:

Company Summary

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PRESENTATION

Operator

Good day, and thank you for standing by. Welcome to the WM Fourth Quarter 2023 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, 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 and full year 2023 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'll 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 the details of the financials and our 2024 outlook.

Before we get started, please note that we have filed a Form 8-K 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. 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 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 stated otherwise, 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 prior year period.

Net income, EPS, income from operations and margin, operating EBITDA and margin, SG&A expense and prior period operating 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 operations. These adjusted measures, in addition to free cash flow, are non-GAAP measures.

Please refer to our 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 www.investors.wm.com.

Time-sensitive information provided during today's call, which is occurring on February 13, 2024, may no longer be accurate at the time of a replay. Any redistribution, retransmission or rebroadcast of this call in any form without the express 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*

All right. Thanks, Ed, and thank you all for joining us. The WM team delivered a remarkably strong finish to 2023, driving fourth quarter operating EBITDA of 15% higher. This accelerated earnings growth led to full year operating EBITDA that exceeded the high end of our most recent guidance range by nearly $25 million and achieved the midpoint of our original expectations from the beginning of the year.

Our strong financial results for both the quarter and the year were powered by our collection and disposal business. This performance starts with disciplined organic revenue growth that exceeded our expectations. And once again, our success in managing the middle of the P&L really stands out in our results, as our teams continue to make progress in optimizing our cost structure with the help of technology and automation. When you combine our revenue performance with the improvement in operating costs, we saw a widening of our price to cost spread and increased profitability.

Operating EBITDA margin reached a record 29.9% in the fourth quarter and full year margin expanded 90 basis points to 28.9%. As 2024 kicks off, we're confident that our continued focus on optimizing our cost structure and executing on sustainability growth projects sets us up for another year of outsized growth. We anticipate operating EBITDA growth of 7.7% at the midpoint of our guidance, which translates to more than $450 million, of which $115 million comes directly from our sustainability growth investments.

We remain excited about the economic and environmental benefits of our expanded -- of expanding our renewable natural gas and recycling platforms. Our execution is tracking well, and we expect to commission 5 new renewable natural gas facilities by the end of the year, reaching 30% of our run rate renewable natural gas volume growth. We're also on track to complete automation upgrades at 10 recycling facilities and add 3 recycling facilities in new markets in 2024.

Turning to capital allocation. You'll hear from Devina on this topic in more detail, but I want to stress our confidence in our ability to continue to allocate capital to all of our priorities. This includes investing in our high-return sustainability growth projects, acquiring accretive businesses, and returning cash to shareholders through dividends and share repurchases.

Our tuck-in acquisition pipeline is robust, and there are some indications that 2024 could have heightened activity in this regard. We're committed to a disciplined approach to acquiring companies, ensuring that any deals we pursue yield appropriate returns, particularly given the high returns in our sustainability opportunities.

In closing, I want to thank the entire WM team for another great year. We were just at the WM Phoenix Open last week, and I've said before, we work hard for this event to create a representation of the bigger company with a central focus on people and the environment. We've been the title sponsor for 15 years now, and the tournament has been recognized as the largest zero waste sporting event in the world for 12 years running. It makes me proud to see the WM team out there making waste diversion operations run smoothly and demonstrating our sustainability leadership so well. I look forward to working with this great team in 2024 as we continue to drive growth by executing our operating plans and progressing our investments in technology, automation and sustainability.

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. We're more than pleased with the strong operational performance our team achieved in 2023, showing continuous improvement throughout the year with standout results in the fourth quarter.

During this period, operating expenses as a percentage of revenue improved 240 basis points year-over-year, landing at 60.3% and marking our second best quarterly performance ever. This improvement was primarily fueled by our collection and disposal business benefiting from the robust operating leverage of our strategic cost optimization. Our proactive measures to accelerate and improve cost efficiency include leveraging technology to manage labor, managing repair and maintenance costs, and optimizing our overall cost structure. These initiatives led to a substantial improvement in WM's cost to serve metrics, bringing estimated unit cost inflation to low single digits by the fourth quarter.

When combined with solid results from our pricing initiatives, we greatly enhanced overall margins. Our strong second half performance translated into full year operating expenses as a percentage of revenue of 61.7%, an improvement of 70 basis points. That momentum has carried into 2024 and is evident in our January results even as we face severe weather in some areas we serve.

Two of the key cost categories driving our operating improvements are labor and repair and maintenance. On the labor front, this begins with our persistent focus on reducing turnover. In the fourth quarter, we achieved a noteworthy milestone as driver turnover reached its lowest point at 18.4%, showing improvement as the year progressed.

Additionally, our strategic automation initiatives are yielding positive results in collection efficiency, with all 3 lines of business improving meaningfully in the fourth quarter compared to last year.

The results of our technology and automation investments gained traction in the latter part of 2023, leading to significant strides in labor cost management. We expect this to continue into 2024 as we broaden the deployment of our tools across additional sites.

Turning to repair and maintenance. With a full lot of trucks received in 2023, we successfully removed over 1,000 excess assets from our operation, improve the age of our routed fleet and reduce truck rental utilization by nearly 60% since the beginning of 2023.

Throughout 2023, our emphasis remained on streamlining maintenance processes, which has resulted in enhanced technician productivity, reduced overtime expenses and diminished reliance on external repair services. This has paid off in the form of lower repair and maintenance costs in both dollars and as a percentage of revenue compared to 2022. We accomplished all this with an unwavering commitment to safety and by enhancing the quality of our fleet. We're proud of the strides we made throughout 2023 and look forward to sustained progress.

Another core element of the equation that fueled our strong financial results is disciplined organic revenue growth. Growth from price and volume in the collection and disposal business totaled 6.3% for the year, which outpaced our expectations. Our pricing programs continue to be focused on striking the right balance between maximizing customer lifetime value and increasing price to recover higher costs. Our full year churn rates remain at the lower end of historical range at about 9%, and the year-over-year improvement underscores our consistent delivery of quality service to our customers.

Looking ahead to 2024, we anticipate sustained momentum in our disciplined pricing programs to result in core price between 6% and 6.5% and yield approaching 5%. We remain committed to maximizing customer lifetime value while securing pricing that exceeds our cost inflation. We have seen that spread improve as 2023 progressed, and we are confident that our teams are poised to deliver another successful year ahead.

Turning to volumes. Our fourth quarter collection and disposal volume grew by 1.9% on a workday-adjusted basis. Growth was primarily driven by MSW landfill and commercial collection, 2 bellwethers for demand of our services. Overall growth in landfill volumes was somewhat muted due to the elevated volumes from the Hurricane Ian cleanup in 2022.

Similar to recent quarters, residential collection volumes declined modestly due to our intentional shedding of low-margin contracts as we work to ensure that we achieve acceptable returns for all parts of our business. You can see the benefits of this focus because while our residential collection volumes declined, total revenue and earnings in this line of business both improved. This is a winning equation, and we'll continue to execute on this strategy in the year ahead.

Organic revenue growth in all collection lines of business remains positive and operating EBITDA continues to grow. In the fourth quarter, new business grew and net services increases remain firmly positive, reflecting our quality of service and focused differentiation.

Looking ahead to 2024, our guidance anticipates collection and disposal volume approaching 1%, mirroring the performance achieved in 2023.

And finally, I want to convey my appreciation to our frontline teams for their unwavering commitment to delivering safe and reliable service to our customers and communities on a daily basis. It's their efforts that made 2023 successful and laid the groundwork for growth in the years ahead.

I will now turn the call over to Devina to discuss our 2023 financial results and 2024 financial outlook in greater detail.

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

Thanks, John, and good morning. Cost optimization was a significant theme in the fourth quarter and throughout 2023.

Our team was pleased that our collective focus delivered WM's best-ever full year SG&A as a percentage of revenue of 9.4%. The 20 basis point improvement from prior year was realized through investments in customer-facing technology, leveraging enhanced back office systems to become more efficient and a continuous focus on optimizing our spend. We're pleased with the progress made to improve this measure, while at the same time, investing in our talent, customer engagement channels and technology capabilities.

SG&A optimization delivered 20 basis points of our 90 basis point expansion in adjusted operating EBITDA margin in 2023. The remaining 70 basis points was from the collection and disposal business which benefited from a combination of fuel price impacts and operating efficiencies. We gained meaningful traction in optimizing labor efficiency and repair and maintenance costs in our collection and disposal business in the back half of the year, lifting our full year adjusted operating EBITDA margin to 28.9%. This result is 30 basis points ahead of the high end of our expectations and positions us to continue to deliver margin expansion in the year ahead.

Our operating performance translated into robust cash flow in 2023. Our full year cash flow from operations grew to $4.79 billion, and our free cash flow before sustainability growth investments was nearly $2.7 billion. Each of these cash flow measures finished the year near the high end of our initial guidance range. This result demonstrates our strong earnings growth, effective management of interest and taxes and optimizing cash conversion and our disciplined capital expenditure management processes.

During 2023, we returned $2.44 billion to shareholders, paying $1.14 billion in dividends and repurchasing $1.3 billion of our stock. In addition, we spent $173 million on traditional solid waste and recycling acquisitions to grow our business.

We accomplished all of this while accelerating our sustainability growth investments for future growth and development, and maintaining our leverage target ratio -- our targeted leverage ratio of about 2.75x. Our balance sheet remains strong and our earnings and cash flow growth are robust, positioning us to continue our commitment to shareholder returns and long-term growth.

Moving to our 2024 financial outlook. We're anticipating total company revenue growth between 6% and 7%, driven by organic growth in the collection and disposal business approaching 6%. Operating EBITDA is expected to grow by $450 million at the midpoint of our outlook.

When we think about the cadence of our growth over the course of the year, we're expecting collection and disposal growth to be weighted more to the front half of the year given the momentum we've gained from strong operating efficiencies in the back half of 2023. And we're expecting sustainability business growth to be more significantly weighted to the back half of the year as our new recycling and renewable natural gas projects come online.

Altogether, we expect this to result in a relatively balanced operating EBITDA growth over the course of the year. We expect capital spending to support the business for the year to total $2.25 billion at the midpoint, and we expect to invest another $875 million on our high-return sustainability growth projects. Free cash flow before these sustainability investments is anticipated to grow almost 7% at the midpoint to $2.85 billion.

We remain committed to investing in an industry-leading network of renewable energy and recycling assets, including renewable natural gas projects, recycling, automation in new markets and advancements in resource recovery. Our sustainability growth investment strategy is progressing well. So as you would expect, there have been a number of refinements to the plan since its inception. We've worked our way through customary changes to project schedules and impacts from inflation, all the while delivering completed projects that meet and sometimes exceed the environmental and economic objectives we planned.

These successes have positioned us to grow the sustainability project pipeline. In particular, our refreshed outlook includes 2 new recycling projects in Canada, that WM has awarded through a competitive process. We now expect growth investments across our recycling and renewable energy platforms to total between $2.8 billion and $2.9 billion from 2022 through 2026.

We expect these projects to contribute run rate adjusted operating EBITDA of about $800 million by the end of 2026. This outlook utilizes the same pricing assumptions we've used consistently, $125 per ton for recycled commodities and $26 per MMBtu for renewable natural gas. We have a great deal of confidence in the value of the projects that are underway, and we're enthusiastic about the strong complement they provide to our existing business.

In conclusion, 2023 has clearly illustrated that we are driving growth through our diligent focus on optimizing our business, investing in technology and automation and growing our leadership in sustainability. We take pride in our accomplishments and look forward to what we can achieve together in 2024. A heartfelt thank you to our dedicated team members who have been instrumental to our success.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question comes from Noah Kaye with Oppenheimer.

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

First one, maybe for John. You talked in some good details about some of the cost optimization and productivity efforts and the gains they got this year. Can you step back and remind us, and perhaps Jim as well, where we are at in kind of the broader march towards automation and productivity investments, and some of the key KPIs that we should be thinking about in terms of progress for 2024?

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

Yes. Noah, it's a good question. Originally, we started talking about this in terms of the elimination of some labor dependency in the 5,000 to 7,000 job range. And it was across a handful of pretty broad areas. One was the customer experience group, one was through our routing, which would reduce our dependency on kind of frontline driver labor and obviously, then recycling, a little bit on SG&A.

And what I would tell you is, if you think about it this way, we're about 75% through what we had planned for, for the customer experience side on the resi automation. And this has as much to do with truck deliveries, which did improve in 2023. We're about 40% of the way through there.

On the recycling side, as Jim mentioned in his remarks, we've got a number of plans that are going to be automated this year. Tara can comment more on that, we're about 20% of the way through there.

So I would tell you, we're making great progress. I think it showed up, obviously across the board in our margins and specifically in labor in Q4 and as the year progressed, but we still got plenty of opportunity out there. We feel like we're on a good pace.

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

Very helpful. Just trying to think about cadence on EBITDA margins for the year. I know we have the typical seasonality, and it sounds like the front half of the year, the growth is really a story of kind of the collection and disposal side. But Devina, are there any sort of guidepost you can give us in terms of thinking about margin cadence for the first quarter or for the first half?

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

Yes, I think it's a great question, Noah. And similar to what we talked about in terms of the EBITDA dollar growth, the cadence story for margin is pretty similar. We expect margin expansion to be more heavily weighted toward the front half of the year, particularly in the collection and disposal business. The SG&A margin expansion will be fairly even over 2024.

But then with regard to the sustainability businesses, the commodity price benefits that we expect to see in 2024 aren't quite significant, right? They're pretty muted on a year-over-year basis. But as a reminder, commodity price expansion in the recycling line of business can have some margin compression because of a really high return on invested capital part of our brokerage business.

And on the renewable natural gas part of the business, we expect margin expansion there, too, because those are such great margin projects, but those will be heavily weighted toward the back half.

So from a margin perspective, while the collection and disposal business is definitely the thing that delivered in Q4, we do expect that to be the thing that lifts margin most significantly in the year ahead, and that will be weighted toward the first half of the year.

Operator

Our next question comes from Bryan Burgmeier with Citi.

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

Guidance seems to imply collection and disposal yield growth that you saw in 4Q '23 will be essentially flat throughout '24, kind of around 5%. So can you just help us kind of understand that pricing strength. It was a bit better than what we were forecasting. Is it about better restricted pricing starting to flow through? Or do you attribute that to maybe mix, underlying strength in the market. Just anything you can kind of call out on that really sticky pricing that it looks like we're going to see in '24?

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

Yes. Bryan, a couple of standouts really were -- continue to be residential pricing and disposal pricing. Those actually showed increases year-over-year. Not surprisingly, the other collection lines of business were down, but that wasn't unexpected.

As we move into '24, we think that kind of 4.5% to 5% yield number is a good target for us. And pricing continues to be a strength. We said at the beginning of '23, that our focus areas for the year would be pricing and then the cost controls that John went through. So pricing is going to continue to at least add a little bit of margin for us, we think, as opposed to '22, where we -- I've said several times, we kind of felt like we were in hand-to-hand combat with our cost structure.

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

Got it. Yes, last question for me, and then I can turn it over. I know in 2023, there was a small decline in the event-driven business that kind of prompted a guidance revision midyear. I'm just wondering, does '24 guidance assume that, that comes back? And then if there's anything else you'd like to flag on the event-driven book, that would be helpful.

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

Yes, it's a great question. And your outlook -- your recollection of our outlook revision midyear is spot on with regard to some of the softness we were seeing in the special waste part of the business. And we saw a strong recovery of that in the fourth quarter, which is one of the reasons that we saw revenue exceed our expectations later in the year. We're not necessarily expecting a rebound of special waste volumes in the year ahead, but we are expecting some of this momentum that we saw in Q4 to carry over, but nothing outsized.

The one thing that I would call out as a reminder with regard to some of the special project-type work is 2023 did have a benefit from Hurricane Ian volumes, particularly in the first quarter. And so that certainly will have an impact on the Q1 comparisons in 2024.

Operator

Our next question comes from Jerry Revich with Goldman Sachs.

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

Devina, I wonder if you could just talk about margins, really outstanding performance by the team in the fourth quarter. If we were to just run the seasonally adjusted annual rate, that's about over 30% margin equivalent that you folks put up in the fourth quarter, the full year guidance for '24 is about 1 point lower than that. It sounds like yield is still very much at a good place. So I'm just trying to make sure that there are no items that you would view as one-off in the fourth quarter versus, "Hey, it's early in the year, and we just want to make sure we have room to execute."

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

I definitely think the way that you summarized it there on the last part of your comment is the way that we're thinking about this, in particular, when we were setting our margin expectations for the year ahead. The momentum that we had in the fourth quarter shows that we have tremendous confidence in having the cost improvement work that we've been so focused on as an organization through automation technology and importantly, the delivery of trucks is something that we can continue to see benefits from -- in the year ahead.

The caution for us, I would say that may have us below that seasonally adjusted margin outlook that you've done really relates to a couple of things. It's one, some of the weather impacts that we saw in January; two, last year, when we gave inflation outlook, we tended to see that inflation was sticking around and being more stubborn than we had predicted. And so we're taking a more cautious view on inflationary pressures in the year ahead than we did a year ago.

But really, what I want to highlight is that there is tremendous confidence in the fundamentals, the price/cost spread has improved, the accelerated truck deliveries and our optimization efforts and the discipline in SG&A are all showing strong results. I think the best line to look at is actually our repair and maintenance line and the operating expense as a percentage of revenue category. And over the long term, that had trended below 9% of revenue for us. And through the first 9 months of 2023, we were at 9.9%, that measure was down to 9.1% in Q4.

So we know that we've got some really strong momentum coming into the year ahead that will continue those cost benefits that you saw us produce in the fourth quarter into 2024, we just think that it's prudent to be on the conservative side when predicting full year margin.

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

So Jerry, real quickly, we did kind of anticipate that there will be some questions on margin. And so just a couple of things here. First of all, the margin, obviously, for Q4 was as strong as we could have expected it to be. And that has continued as we look at the month of January. January came in quite strong for us. So we're pleased with that.

The second point would be around some of the questions that you're asking around conservatism on margin for '24 and Devina did a really good job of explaining that. I think it's really just -- I guess you could argue that it's conservative based on 90 basis points of improvement from '22 to '23. But there seems to be an uncertain year in front of us every time we come to this point. We don't know exactly what the economy is going to do. Some days, I feel great about the economy, other days, not so great.

So you can argue there's a little bit of economic conservatism in there and also a little bit of forecasting conservatism coming off such a strong year that you want to try and say, we're going to do the same thing going forward into '24, but we do feel really good about the way we finished the year and honestly, the way we've started the year so far through January.

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

Really appreciate the color. And Jim, can I ask you just on a separate topic. Landfill gas transactions are coming in at really attractive levels. Enbridge transaction was $270 per MMBtu. It's costing you folks $50 per MMBtu to bring your assets online. So just given how fairly deep the market is for those type of assets, can you just update us on how you're thinking about what it would take for you to consider monetizing some of the landfill gas assets when you bring them online? Has the attractive market price impacted how you're thinking about the owned versus sale opportunity?

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

So I'm going to -- I'll say one word on that, and then I'm going to turn it over to Tara Hemmer to maybe give a little bit more color. But that's always an option for us. And we have multiple options, and it's good to be in a place where you have multiple options. But at this point, we're pleased with the progress we're making on building these plants. We have a number of plants that are at various stages of construction.

Tara, anything to add to that?

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

I would just say this aligns really well with our business, and we are making great progress on building out these plants. The 5 that we're going to bring online in 2024, we're going to have strong contribution from them exiting 2024. And this is going to be something we're going to continue to grow.

Operator

Our next question comes from Tyler Brown with Raymond James.

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

Tara, actually, I want to come back to the updated sustainability CapEx figures of $2.8 billion to $2.9 billion. So I may have missed it. But if I'm not mistaken, that number was closer to $2.2 billion back at the Analyst Day. Now I get that there are $350 million in incremental recycling opportunities, but what makes up the difference, call it, that $300 million, was that just inflation?

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

Yes. The difference really is related to inflation, primarily in our renewable natural gas builds and related to inflation, related to supply chain, also a little bit on construction increases and interconnect. So that is the difference.

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

Okay. Perfect. That's helpful. That's very helpful. And then, Devina, thank you so much for the WM renewables segment reporting. But I do just want to make sure that I've -- that I understand it all. So I get the impact in revenues from the change in the price of the commodities that are impacting that WM renewables and recycling line. But if you look at the change in that line versus the change in the net revenue for those, they don't exactly line up. So it tells me that there's likely some volume component in there.

So just to be clear, maybe this would be helpful. But when you bring on a facility like Eco-Vista, where does that show up? Does that show up as basically volume in your IRG calc? Or can you just help us with how the accounting will work?

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

Sure. And Ed and Heather will be happy to walk you through any details I don't cover here. But I'm glad, one, that the additional clarity is beneficial. The other that I would say is that on the IRG measures that we do, the internal revenue growth measures that we do, you'll see commodity price impact in the single line, which is recycling processes and renewable energy.

So that's all price. And then you'll see the incremental volume from new projects whether it be automation projects that have more throughput at the plant or the new Eco-Vista plant, that will be in the volume line.

In terms of the segment reporting line, the only thing that might be a little bit of a complicating factor is the internal revenue between the renewable business and the collection and disposal business, you can think of it as the renewable business paying the royalty to the collection and disposal business associated with the landfill gas production. That doesn't show up in the revenue line because it's effectively just a cost for the renewable business. Hopefully, that's helpful.

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

Yes, I definitely think so. We'll parse it out. But I think you mentioned that collection and disposal volume could be up maybe 1%. But again, kind of going back to that total IRG table, could we actually see that number closer to 2%? Because I would assume that with $115 million of incremental renewables EBITDA, there's probably, at least, $200 million of revenue associated with that. Does that make sense?

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

So the way to think about this is that when we gave that volume outlook, that was just the collection and disposal volume. The renewable energy business increases we have, on a combined basis, being in the range of 30 to 60 basis points in the year ahead, and that's a combination of commodity price impacts and volume.

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

Excellent. Okay. Last one here, Devina. So margins were super strong. We've talked about that. I think they're up 230 basis points year-over-year in Q4, but can you kind of help us bridge that 230 basis points? I think there was a fewer days, maybe fuel was a help, maybe commodities helped. Just any color there would be appreciated.

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

Yes. For Q4 specifically, again, the collection and disposal business and the efficiency that we drove was the lion's share of that improvement at 220 basis points. Fuel was another 50 basis points. So that really does explain almost the entirety of it. There are a few other puts and takes. But I would say that my comments earlier about repair and maintenance, and then John's comments about the labor line, those are the 2 places that are driving that 220 basis points of margin expansion.

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

I think, Tyler, a little bit of an add on here is that I've been told we don't have ourselves on the back enough. So (inaudible) ourselves on the back a little bit here.

When we started talking about some aspirational metrics, meaning margin, EBITDA margin, SG&A as a percent of revenue, OpEx as a percent of revenue a couple of years ago and then talking about technology and using attrition to reduce our labor dependence. Those numbers were pretty far out on the horizon. And now in every case, those numbers are literally a stone's throw away for us. Whether you talk about 30% EBITDA margin, we're right there for the fourth quarter, SG&A at 9%. We're very close to that, and OpEx at 60%, very close to that.

So I'm really proud of the team for executing so well on this, and being able to stand up on this call today and last quarter as well and say, those things that we put out there, those goals that we set, we're getting close to achieving those, don't mean we're satisfied. We'll continue to set higher goals. But I'm pleased with the fact that we've been able to get to those goals that were pretty far in the -- out on the horizon we initially set them.

Operator

Next question comes from Michael E. Hoffman with Stifel.

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

Back to the margin question, John, it seems like looking at this on a 2-year stack helps because you can't perfectly time when you get some of your self-help and that sort of accounts for really strong '23, a little more muted '24, but the 2 years stack is sort of 60 basis points a year.

So where the question underlying that is recycling is an incremental tailwind because you've got a pretty low estimate there relative to how you finished the year on the basket. GDP, I'm assuming, you think it's maybe 1%, 1.5% and the trend is stronger than that. So that's a tailwind. And then I think your wage growth is probably running closer to 3.5%, 4%. Therefore, there's clear spread on price cost. Am I looking at that correctly?

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

I'll start and Devina -- I think on the cost spread comment that you (inaudible), Michael, I think that's what we've been talking about for the last couple of quarters, whether you look at core price or our yield numbers. We've been talking about being disciplined in the way we approach pricing. And over time, and the last couple of quarters are a great example of that, we've been able to really drive out -- drive some operating efficiencies and drive out some of the labor dependency and Devina commented on the maintenance repair. That's another bucket where we've made a lot of progress.

I think in Q4, we were flat to slightly down year-over-year in terms of whole dollars. So that's part of what was helping us in Q4.

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

And then I'll just add a little bit of color that provide some clarity on a couple of the points that you brought up, Michael. One, with higher recycling commodity prices, the brokerage business can actually put downward pressure on margin. And so that's one of the things that we have built into our outlook for 2024.

And then in terms of wage inflation, we start at 4% with our folks. And so wage inflation is still expected to be north of 4% when you take into account spot increases that we have to provide in certain markets to be responsive to various changes. So 4% is kind of our baseline, and then you add on top of that.

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

And your GDP assumption is pretty muted.

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

Yes. Basically, what we've always said is that we believe that our volume is about a 75% flow-through from GDP. And so we did have a fairly muted outlook with regard to GDP when we built our plan. I hope your crystal ball is better than mine, but I would tell you that our expectations for economic outlook continue to be that we need to be on the cautious side of things just because there's so much left in uncertainty. You saw that with today's print on CPI as an example, which exceeded expectations.

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

Yes, I get that. Just the consumer seems to keep plowing ahead. Switching gears a little bit, Tara. If your renewable natural gas, your landfill gas is kind of a Swiss army knife of renewable fuel. When do the federal agencies wake up to this and so you -- we get a proper interpretation of the ITC or the 45Q or Z credits or come back to eRINs. What's your view of where that goes? And then the second piece is what are you assuming happens in the out years in that $1.5 billion of R&D spend, how much do you get back for credits?

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

So starting with the real positive. The one thing that the federal government did is set a 3-year RVO and having that for 2023 through 2025, you've seen clear stability in the program, and so that's been a positive.

With the ITC, we think when Treasury issued their guidance that there was a misinterpretation over what was in the Inflation Reduction Act. And we don't just share this view others do with us that are in the biogas community and generate landfill gas -- renewable energy from landfill gas. We've commented on that, and we're anticipating that Treasury will come out with some further guidance later the year and so cautiously optimistic there. So there's a whole host of credits that could be stacked. Obviously, the ITC was in our plan, and we remain optimistic related to that. And of course, looking to 2025 with the production tax credit too.

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

On the ITC point, Michael, just so that we're crystal clear in terms of the implications of that on our 2024 guidance, we contemplated $120 million of ITC benefit in our free cash flow outlook for the year.

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

Okay. And then some housekeeping, if we could. I love the segment reporting as well. Are we going to get any kind of tons in, tons out, so we can actually do a bottoms-up forecast on sales for the renewable and processing segment? And then how about megawatts and MMBtus to be able to do the same thing on the sales growth for renewables?

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

So we want to take a breath and celebrate all of the incremental transparency we've provided. We're really proud of the work that the team did because while it looks easy, it isn't, there's a whole lot of work that went into it.

With regard to the more, I would say, operational driver elements of the reporting, we'll continue to evaluate whether or not there's anything that is a strong complement to the financial measures and consider any additions in the years ahead. But right now, we're going to continue to execute on this strong reporting that we've been able to accomplish. And we actually would like to see the industry follow suit in terms of providing additional visibility because we think it's beneficial.

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

So in the K, one, when will it be recent to? Will we get quarterly data for all of '22 and all of '23 and then 3 years of forecast, so we can rebuild our models in this format?

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

So the K will be released early today, and we're in good shape for that. So thank you to the team.

With regard to the quarterly data, you'll get that over the course of the year. It will have the full year data. The quarterly recast will come quarter-by-quarter.

Operator

Our next question comes from Stephanie Moore with Jefferies.

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

So just kind of -- just looking at the 2024 guidance assumption, it looks like you're assuming RINs at about $3, which makes sense given where RINs are today. But digging into a little bit more, can you maybe talk about in terms of what contracts that you have already signed and kind of where you're able to lock in those prices going into the year, I think you said at Sustainability Day that you were looking to have 70% to 90% locked in, in any given 12-month period. So any update on where that stands for 2024 to get to that $3 RINs?

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

Sure. So we have about 2/3 of our offtake locked in for 2024. And when we think about what's locked in, it is a mix of long-term contracts and also RINs that we purchased really -- sold on the forward side into 2024, which would have been at a higher rate than $3. So on a blended basis, you sort of get a lower average there. And then the third that we would be selling in 2024, that's what's at the $3 RIN guide.

The other thing I want to just mention is those longer-term contracts that we have in place. There is a mix, anywhere from 5 to 20 years. So we're really trying to take an approach where we have different tenors that we're locked in at.

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

Got it. No, that's very helpful. And then maybe sticking on the sustainability front. You talked about some incremental investments included in your updated outlook, and you noted that, that involves 2 projects in Canada. Can you talk a little bit about the opportunity? I'm assuming that those are probably related to EPR changes in Canada, if that is the correct assumption, maybe just what -- how EPR might change the margin or growth opportunity compared to maybe your more traditional U.S. recycling business? So how you're thinking about those incremental opportunities?

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

The 2 Canadian projects are related to Extended Producer Responsibility and I think this is a great example where we were able to really showcase our automation investments and how differentiated our assets are, really taking the pro to some of the facilities that we have across the United States. And so that's a great example where we're able to win more business based on those investments.

Extended Producer Responsibility in Canada and the structure that we have there, it really is around us using those assets as manufacturing plants, and really a fee-for-service model. So it's a great example of how we can leverage this technology differentiation for more business in the future.

Operator

Our next question comes from John Mazzoni with Wells Fargo.

John Peter Bonner Mazzoni - *Wells Fargo Securities, LLC, Research Division - Associate Equity Analyst*

Maybe just a quick one in terms of the sustainability, EBITDA timing. Is this just really kind of a knock-on impact of some of the 2023 project delays? I think we noticed a change to run rate versus kind of in 2016? Any color would be appreciated.

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

So there's 2 key things that I would want everyone to bear in mind as you think about our trajectory. The first is, in 2024, we're going to have roughly 40 projects under construction at any given time. So that really gives you a sense of how we're building and we have a lot of momentum in the ramp.

The second key piece is really exiting 2024, we're going to be approaching roughly $300 million in run rate EBITDA, which gives you a sense of where we're headed on that ramp to the $800 million. So what we're really seeing in 2024 is a true build of momentum on reaching that $800 million target.

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

John, those supply chain constraints are not that different from what we've seen on the fleet side of our business either. The good news is that, as you heard John Morris talk about it, we've started to see that free up a bit. And so Tara is seeing the same thing on the RNG and recycling side, but we definitely had some supply constraints that contributed to this, a bit of a slowdown over '22, in particular, but also the front half of '23.

Operator

Our next question comes from Tobey Sommer with Truist Securities.

Tobey O'Brien Sommer - *Truist Securities, Inc., Research Division - MD*

I wanted to get your sense for acquisition expectations. So how are the favorable trends in your business, which is a pretty long list of price cost yield, new investment production, et cetera, different than those at the smaller players with whom you have a dialogue for acquisitions?

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

So look, we said that our acquisition pipeline was robust. I think what you're seeing is that some of those -- and I'm speaking just from -- this is somewhat anecdotal and speaking to some of those folks that we have acquired is that there's kind of a multitude of challenges for them, some of which we face and some of which we don't face.

So one that we might not face is a lack of a succession plan for some of these folks. Their kids have just decided they don't want to run the business. They'd rather go take the money and live in Italy. And so that's not something we face, fortunately. But they're also having challenges with labor. We're addressing that, as you've heard today, through automation. And in some cases, they are as well. In some cases, they're not able to do that.

So there's a number of different reasons why there's a growing list of willing sellers. We're going to take advantage of that. But at the same time, we've invested heavily in these organic growth projects, and we want to make sure that we have similar returns before we go invest heavily in tuck-ins.

Tobey O'Brien Sommer - *Truist Securities, Inc., Research Division - MD*

Good to hear. I'm glad you're not going to go chase the (inaudible). So appreciate that. With respect to the fleet, are you -- after a full allotment last year, where are you in terms of being able to just renew the fleet at what might be considered a normal cadence? Do you still have some catch-up to do?

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

Yes. Tobey, we got about -- we've delivered about 1,700 units this year which was a little wide of what we had planned for, but that would be really considered a full lot. And we probably have another 300 units on top of that to deliver. So I would say that by the end of '24, we're fully caught up.

What I would tell you is, team has done a really good job of not compromising the quality of our fleet. It's showing up in our service, and it's really starting to show up in the back half of the year in terms of our operating performance, and we see that continuing into '24. And certainly, as we get the benefit of some additional vehicles.

Operator

Our next question comes from Kevin Chiang with CIBC.

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

Maybe just a clarification on the updated sustainability investments and EBITDA profile as we look out to 2026. I think if I -- if memory serves me correct, when you had the Sustainability Investor Day, I think you had about a 90% free cash flow conversion in 2026 from EBITDA into free cash flow. Is that still the rule of thumb we should be thinking about on the $800 million of EBITDA in 2026 in terms of the free cash flow potential from these investments?

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

We can specifically confirm that number for you. We didn't refresh that. But the key takeaway for us there, whether it's 70% or 90%, and that's kind of the ZIP code that I think we should be thinking about, the free cash flow conversion in these businesses is stronger because the maintenance capital is lower. And so it is right to think about that being a really strong fundamental contributing factor to the long-term yield of this business.

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

That makes a ton of sense. And just on the -- I guess, on the 2 facilities in Canada related to EPR. Are these in Ontario and just -- as you think of, I guess, EPR throughout the country as multiple provinces look to implement this, just what that pipeline of opportunity looks like from an EPR perspective and investing in more recycling facilities, I guess, coast-to-coast in Canada?

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

You're exactly right. Those 2 are in Ontario, and this is something that we're actively tracking throughout Canada and then, of course, looking at where there is pending legislation in the United States as well. There's obviously Colorado as an example, which is on the core front and making sure that we're well positioned to respond to the pros when they eventually implement.

Operator

Our next question comes from James Schumm with TD Cowen.

James Joseph Schumm - *TD Cowen, Research Division - VP*

Can you help me understand the monetization of the D3 RINs credits? Is there a meaningful difference in price if you internalize or use the RNG in your own fleet versus selling it as a transportation fuel to someone else? And I know you'll reduce your fuel cost and emissions if you internalize the RNG, but just curious if there's a monetization benefit as well?

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

The way to think about it and what is really unique about WM is because we have our own fleet of compressed natural gas vehicles, we're in a very unique spot where we are able to close the loop. We produce renewable natural gas. We can allocate that renewable natural gas to our fleet to generate the RIN. So we don't have to give up any of our RIN value. That's probably the most significant advantage with WM as compared to others in the space. And that's how we monetize and create RINs ourselves versus others having to really tie it to someone else's fleet.

James Joseph Schumm - *TD Cowen, Research Division - VP*

So Tara, just to clarify that. So when we see the D3 RINs prices, I mean, I think some people have talked about, well, the actual monetization is a little bit lower than the price that I maybe see on the screen, is that the case for you guys as well or no?

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

No...

James Joseph Schumm - *TD Cowen, Research Division - VP*

Do you get that full value?

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

I think we get the full value. And the other thing to bear in mind is you're looking at spot prices. And while we do play in the spot market, we also have been very actively looking at how we can forward sell and really look at selling our RINs, 6 months out, a year out. So there's a balance there.

James Joseph Schumm - *TD Cowen, Research Division - VP*

Okay. Great. And then just lastly for me. I know that hazardous waste is a relatively small business for you, but I think you guys have a substantial market share of the hazardous landfills. The industry seems to be more profitable now. And I was just hoping maybe you could help us quantify your business here? And what's the outlook?

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

Yes. I mean we've been in hazardous waste space for quite some time, and it continues to be a valuable component of our portfolio, and we've got coverage nationally. We've got assets on the East Coast and then, obviously, to the Southeast and on the West Coast as well. And I would tell you, we continue to look for opportunities to grow that business.

I think one of the benefits we have is we've got a tremendous network of transportation assets that allows us to access a lot of the prominent markets, I think the Southeast, the Gulf Coast is one where we are very, very well positioned in terms of our hazardous waste presence.

Operator

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

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

So I guess let's start just on the price cost spread that you kind of alluded to in your opening remarks, you indicated that it improved. And certainly, that spread when costs were rising dramatically in 2022, it kind of contracted and then as costs moderated somewhat and your pricing held in, presumably, it's been widening here in 2023 or back in 2023.

My question for you is, what your view is on the go forward of that spread? Is that something that you believe you can maintain at a higher level than it's been historically? Or is '23 just bringing it back to where it was historically, and that's likely where it's going to be going forward?

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

Well, I think you've hit on the right focal point for us, which is that price cost spread as opposed to just looking at price because, obviously, in '22, price was higher, but as I said, we were really just combating this real high inflation in '22. '23 was, as you said, back to a point where the price cost spread starts to widen a bit. And so how much that widens is a little bit of a question mark. We don't know exactly where inflation goes. This morning's numbers were maybe a little disappointing to the market.

But we feel good about the wage inflation, we feel like that is much more kind of something we have control of now, whereas 2 years ago, we really had less control over it. I think you'll see the price cost spread stay pretty close to where it's been in 2023, 2024 won't be a big change from that standpoint.

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

Okay. Perfect. And when -- I know with your sustainability initiatives, it does introduce a little bit of commodity price variability in there. When you look at the midpoint of your EBITDA guidance for '24 and you look at the growth in the dollar value of that, about 1/4 of that, I think, is from sustainability initiatives of that growth. And some of those, as you mentioned, are back-end weighted.

Can you talk to us from a risk standpoint as it relates to 2, first, when an investor asks you, what about the volatility that commodity prices brings in? Can you remind us about the -- how you lock in price and give us some assurances there? And then the second part of the risk profile, how much of it is related to permitting or completion of construction projects that might get delayed through the course of the year? How do you feel about that risk component to its contribution in 2024?

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

I can go ahead and take it in 2 parts, and I'll speak to the commodity price piece first and then the time line second.

So on the commodity price piece for recycling, I think one of the things that we've done really well is really changed our model to be a fee-for-service model, and we have 95% of our contracts through that, which has really insulated us a bit on the commodity side. And then on top of that, recall that a significant piece of the benefit is coming independent of commodity prices, really those labor cost improvements and also some price premiums that we get related to the automation benefit.

On the renewable energy side, one of the things that we've been clear on is that we're going to work towards an 80-40-20 -- 80-20 framework, where 80% of our volume would be locked up within 1 year. And that would be something that we would be working towards in 2026. You heard me mention roughly 1/3 of our offtake is already locked up. So that gives us some confidence on the commodity price side.

Related to projects, we've really been kicking this around looking at our project time lines and making sure that we're within a strong and confident range for 2024. We have 2 large projects that are coming online in Q3. And so we feel confident in our ability to hit the project time lines on both the recycling and renewable energy side.

Operator

Our next question comes from Toni Kaplan with Morgan Stanley.

Hilary Lee - *Morgan Stanley, Research Division - Research Associate*

This is Hilary Lee on for Toni Kaplan. I just wanted to ask on the sustainability EBITDA part. So if I recall correctly, during the Sustainability Analyst Day, we were expecting around $600 million from RNG, including the third-party eRINs by 2026. So just wondering what is kind of that delta between the now $510 million versus the $600 million?

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

I think you have to compare the $510 million to the $500 million because the $500 million number was without the eRINs and the third-party RNG projects. So the best way to think about it is we've increased our target by $10 million for the renewable natural gas business.

Hilary Lee - *Morgan Stanley, Research Division - Research Associate*

Got it. Appreciate that. And just on -- for the recycling, the increases, is that for essentially the 2 new projects in Canada?

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

It's -- a portion of it is from the 2 new projects in Canada and then a mix of other benefits from our portfolio of projects.

Operator

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. Well, thank you all for joining us. We're very proud of the quarter we had, very proud of the year. Excited about what 2024 holds for us. And we look forward to talking to you next quarter. Thank you very much.

Operator

Thank you for your participation. You may now disconnect.
