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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, everyone, and welcome to the Covanta Holding Corporation Second Quarter 2018 Financial Results Conference Call and webcast. An archived webcast will be available two hours after the end of the conference call and can be accessed through the Investor Relations section of the Covanta website at www.covanta.com. The transcript will also be archived on the Company's website.

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

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

Thank you and good morning. Welcome to Covanta's second quarter 2018 conference call. Joining me on the call today will be Steve Jones, our President and CEO; and Brad Helgeson, our CFO. We will provide an operational and business update, review our financial results, and then take your questions.

During their prepared comments, Steve and Brad will be referencing certain slides that we prepared to supplement the audio portion of this call. Those slides can be accessed now or after the call on the Investor Relations section of our website, www.covanta.com. These prepared remarks should be listened to in conjunction with these slides.

Now, on to the Safe Harbor and other preliminary notes. The following discussion may contain forward-looking statements and our actual results may differ materially from those expectations. Information regarding factors that could cause such differences can be found in the Company's reports and registration statements filed with the SEC. The content of this conference call contains time-sensitive information that is only accurate as of the date of this live broadcast, July 27, 2018. We do not assume any obligation to update our forward-looking information unless required by law. Any redistribution, retransmission or rebroadcast of this call in any form without the express written consent of Covanta is prohibited.

The information presented includes non-GAAP financial measures. Because these measures are not calculated in accordance with U.S. GAAP, they should not be considered in isolation from our financial statements, which have been prepared in accordance with GAAP. For more information regarding definitions of our non-GAAP measures and how we use them, as well limitations as to their usefulness for comparative purposes, please see our press release which was issued last night and was furnished to the SEC on From-8K.

With that, I'd like to turn the call over to our President and CEO, Steve Jones. Steve?

Stephen J. Jones

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

Thanks, Dan and good morning, everyone. For those of you using the Web deck, please turn to Slide 3. I'll provide a brief overview of the financial results along with an update on some of our strategic initiatives, and then I'll go through more color on the key drivers that impacted the quarter. The momentum we built during the first quarter continued as we generated $103 million of adjusted EBITDA and $26 million of free cash flow during the second quarter. These results reflect progress on many fronts including record production at many of our facilities, strong waste pricing, growth in profile waste, improvements in metal recovery and pricing, and effective cost management. We are reaffirming our full year guidance and with our current view on the year, we now expect full year adjusted EBITDA to be above the midpoint of our guidance range.

Not surprisingly, a key driver of the results was the performance of the fleet. We've now completed a majority of our planned maintenance work and remain on track for our full year spending plan. Several of the largest plants are positioned to reach record waste and energy volumes and that is a credit to our operational teams and the impact of our plant investments as well as ongoing continuous improvement programs. With improved plant performance, the profile waste sales team was able to accelerate activity, a focus on customer service, internalization of waste from the material processing facilities and diversification of flows to incremental plants in the fleet led to a 9% growth year-over-year. While our key assets are performing well, we continue to move forward on the portfolio optimization plan. We recently decided to close our 550 ton per day energy from waste plant in Warren County, New Jersey.

This was a difficult decision as the facility has run consistently well and the team has done a fantastic job there. However, given its size and the challenging local market conditions, we didn't see its potential to be a significant financial contributor going forward. Closure is expected in early 2019, and we do not expect it to have a material impact on the financial metrics. Some of you may have also noticed that we reached an agreement to sell our stake in a hydro plant during the quarter. We expect to receive $12 million of proceeds when we close the sale in the near future. This activity is part of our broader plan to rationalize non-core operations. We also have a number of other smaller assets that we hope to monetize in the coming months.

Looking longer term and echoing comments I'd made previously, we continue to review our fleet and the profitability of all the plants to ensure that our resources are best utilized. You can view this type of activity as an ongoing effort that will result in periodic repositioning of assets and facilities as we strive to improve the returns and focus our efforts.

Now I'll get into detail on the markets and operations. I'll start with the waste business. Please turn to Slide 4. Similar to the first quarter, waste and service revenue drove our performance with both price and volume as key same-store drivers. We realized 5% same-store volume growth, primarily due to a full quarter of operation at Fairfax and improved throughput around the fleet. We expect this trend to continue to the balance of the year.

With our strong performance year-to-date, we now expect both tip fee volumes and revenues to end the year near the high end of the range. On the pricing side, we saw same-store improvement of over 3% in the quarter due to a combination of rising spot prices, contractual escalators and our success in ramping profiled waste. We continue to see a robust market for waste treatment and disposal, with strong values coming into our assets. While transportation costs are increasing, this will result in better pricing for our well-located facilities. In addition, we're beginning to see some improvement in our contractual escalators which are tied to regional CPI or other labor or materials indices. This is important as nearly $1 billion of our waste and service revenue benefit from some form of inflation escalator.

Now let's move on to talk about Covanta Environmental Solutions, which manages our profiled waste business. Overall, we had a very successful quarter in this group; with Environmental Services revenues growing 14%, virtually all of which was organic. Profiled waste revenues into our Energy-from-Waste facilities grew by 9% and this growth ramped through the quarter and hit its highest level during June, which I believe bodes well for future quarters. We continue to see opportunities to better utilize Covanta Environmental Solutions' material processing facilities, or we call them MPFs to drive more volume and better serve our customers. Further, with the start-up of the Indianapolis MPF, we're now more focused on internalizing material from the MPFs into our Energy-from-Waste plants, which enables us to improve our weight handling and better manage profiled waste volumes.

Last quarter, we mentioned an expanded focus on healthcare solutions, including our receipt of a permit to dispose of regulated medical waste at a third Energy-from-Waste plant in our fleet. During the second quarter regulated medical waste revenues increased by 39%. While they still represent less than 10% of the profiled waste sent to our Energy-from-Waste plants, we expect continued growth especially as we begin taking volumes into the third site later this year.

Now let's move on to Energy. Please turn to slide 5. Similar to waste, we saw strong year-over-year improvement in energy production, given the performance of the fleet and Fairfax in particular. As we look to the full year and given the plant production outlook we also expect both energy generation volumes and revenue to trend towards the higher end of our forecast ranges. Realized pricing was weaker year-over-year as expected, primarily due to the pricing of our hedges. That said, weather has generally been favorable year-to-date which has driven energy demand. This has resulted in five-year lows for natural gas in storage, in spite of significant natural gas production growth.

This environment of modestly improved market power prices led us to slightly tighten our full year expectations for realized prices. That said, we have we have still not seen improvement in the forward electricity market which remains subdued. I'm also pleased report that we agreed to a new 15-year power purchase agreement at our Marion County Energy-from-Waste facility in Oregon. The new power sales will begin in the later part of 2019. The pricing in this agreement reflects the plant's capability as a base load renewable energy provider and we expect it to improve the plant's overall economic proposition.

Separately, we entered into a new one-year power purchase agreement for a portion of the output at Fairfax. This agreement includes value for the renewable aspects of the plant and the – the impact is reflected in the outlook for average prices in 2018. This is not the first time we put in place a short-term power – power agreement for Fairfax, which drives value to the facility and we're hopeful we can enter into additional agreements like this in the future. These agreements represent a continuation of our efforts to reduce energy price volatility while simultaneously achieving additional value for our renewable attributes.

Now let's move on to the Metals business on Slide 6. Metals represent another positive story this quarter and we continue to increase the recovery rates, due to both better plant output and investments in separation equipment. For ferrous, same-store revenues grew 43%, driven by both better prices and increased sales volumes. From a market perspective, steel tariffs have resulted in improved pricing for U.S. produced finished steel and are driving higher utilization of domestic mill capacity. The net result for us is better demand and pricing for our scrap ferrous, with average pricing through July exceeding $330 per ton on the Heavy Melt Steel or HMS index. We're now raising our full year outlook for HMS to $275 to $325 per ton, and at the same time increasing the full year revenue outlook for ferrous.

We also continue to optimize the ferrous sales mix. The presence of our centralized processing facility gives us tremendous flexibility to consolidate and upgrade ferrous material. However, with strong demand for ferrous and high transportation costs, we're finding that in some cases it makes more sense to sell directly to customers from our plants, and as such, you may see lower – a lower percent of index price in future quarters. This will be offset by the beneficial impact of reduced costs through transportation of efficiencies and will be a net positive to Covanta.

While the ferrous side has been unambiguously bullish, the non- ferrous side is more nuanced. Second quarter results were excellent as revenue more than doubled year-over-year. This was driven by our ability to get full value for the higher value fractions post-separation as well as greater shipments of higher value material relative to last year. As of now, nearly all of the plants in the fleet are shipping their non-ferrous materials to the central processing facility in Pennsylvania. The pricing outlook here is more muted. We have seen a recent pullback in the prices of aluminum and copper, primarily due to trade tensions and concerns on global growth.

The majority of our non-ferrous volumes are light products like aluminum that we sell domestically. However certain fractions of heavier metals such as copper, brass, and zinc, yield better pricing in China. Due to China's recent change in policy, we no longer have access to these markets. We have identified other options for selling the products at modestly reduced pricing. The positive from our standpoint is that given the high-quality product that we sell, there was ample demand. But we will need to adjust our sales efforts in order to execute on these opportunities. The net result is that we're trimming our full year outlook for non-ferrous prices and we may see some timing shifts as product may be sold in 2019 rather than 2018. As we look at metals in the aggregate, our full year range is unchanged from before, but we now expect a higher contribution from ferrous and a lower one from non-ferrous.

Let's just move on to maintenance and operating expenses, please turn to Slide 7. Total energy from waste maintenance spend for the quarter included – including both expense and CapEx was $103 million versus $110 million last year. We have now completed approximately 60% of our expected full-year Energy-from-Waste spend, and given our experience to date, we remain comfortable with the full-year range of $390 million to $410 million. Outside of maintenance, other plant operating expenses increased 6% year-over-year. The biggest driver of this increase was a full quarter of operations at the Dublin Energy-from-Waste facility. Managing costs effectively is an important initiative for me and those efforts certainly aided the quarterly results. As you look at the balance of the year, you should also expect a slower pace of growth in other plant operating expenses as well as in SG&A as we keep a keen focus on cost control throughout the organization.

Before I hand this over to Brad, I want to give an update on our UK development efforts. As you may recall from our first quarter discussion, the Rookery project which received its operating permit from the UK Environment Agency earlier this year is subject to a claim challenging the agency's permit issuance process. A brief hearing is scheduled for mid-October, at which we expect the agency to vigorously defend its process and decision. We're confident that the permit will be upheld and expect the Court will issue its decision during the fourth quarter, after which we'll move to financial close. We're also making progress on our development efforts at both Protos and Newhurst, the two projects that we are partnered with Biffa. And both are well advanced in permitting, enabling them to potentially move into construction early next year.

On both projects, we're simultaneously finalizing commercial agreements, holding discussions with contractors and lining up financing. Some events of our experience at Rookery is indicative of issues we may face on other projects. The reality is that each development is unique and the local dynamics differ, so predictable similarities do not exist. However, it is worth noting that permits for both Protos and Newhurst are already issued and the current process we're undertaking, relates to an amendment of existing – of an existing permit rather than a request for a new permit. We believe this like – this lessens the likelihood of a successful challenge.

With that, I'll turn the call over to Brad to discuss the quarterly results in greater detail.

Bradford J. Helgeson

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

Thanks, Steve, and good morning, everyone. I'll begin my review of our second quarter financial performance with revenue on Slide 9. Total revenue was $454 million in the quarter, up $30 million or 7% over last year. Excluding commodity prices, revenue grew $31 million organically with strong plant production driving volume growth across waste, energy and metals. Commodities were a mixed bag in the year-over-year comparison, with stronger metal prices contributing $3 million, but lower energy prices reducing revenue by $4 million.

The Dublin facility contributed $8 million of service revenue in the quarter, reflecting the fee that Covanta earns for operating the plant on behalf of the joint venture. Long-term contract transitions were an $8 million headwind in the quarter, primarily resulting from the expiration of a legacy power contract in New England last year and our exiting of an operating contract earlier this year.

Moving on to Slide 10. Adjusted EBITDA was $103 million in the quarter, an increase of $10 million or 11% year-over-year. Excluding commodity prices, adjusted EBITDA grew $7 million organically, primarily driven by strong plant production in particular at Fairfax. So this was partially offset in the year-over-year comparison by the $16 million of business interruption insurance proceeds received in Q2 2017.

Flowing straight from the revenue line, commodities had a limited net impact as higher metals prices were offset by lower energy prices. The Dublin facility contributed $10 million of adjusted EBITDA in the quarter, which comprised both our O&M services and the proportion to adjusted EBITDA from our 50% JV ownership in the project.

As you look ahead to the rest of the year, this should approximate the quarterly run rate contribution from Dublin; but be aware that the year-over-year comparison in the fourth quarter will be against approximately $20 million of adjusted EBITDA in Q4 2017, when we still owned 100% of the project. Contract transitions represented a $6 million decline in aggregate. Looking ahead to the third quarter, I'll remind you that we recognized an $8 million benefit in Q3 2017 related to the settlement of our dispute with the municipal client that we categorized as a contract transition impact in this presentation.

Turning to Slide 11, free cash flow was $26 million in the quarter. Before working capital movements, free cash flow was roughly flat year-over-year as the $10 million increase in adjusted EBITDA included our proportional adjusted EBITDA from the Dublin project, which does not contribute to cash flow until dividends are distributed to the equity holders, which we expect in the second half.

Maintenance capital expenditures were lower year-over-year, which was offset by certain other items reconciling adjusted EBITDA to cash. As presented in the bridge to our full year outlook for free cash flow, we expect this category of other items to be positive over the balance of the year driven by restricted cash distributions.

Looking at our reaffirmed guidance range for free cash flow for the year, while we expect adjusted EBITDA to come in above the midpoint of our range, free cash flow will ultimately be impacted by movements in working capital. So it's probably not appropriate for us to be more precise within our expectation within the range at this point. Of course, our primary focus is growing cash flow sustainably over the long term with our target to hit $250 million in annual free cash flow by the middle of next decade.

Now please turn to Slide 12, where I'll discuss our outlook for growth investments. In 2018, we plan to invest around $20 million in organic growth projects relating primarily to material processing facilities or MPFs in our CES business and increased metal recovery and spend approximately $15 million for new transportation equipment in preparation for commencing operations at the Manhattan Marine Transfer Station next year. These estimates are unchanged from last quarter.

We continue to make progress on the permitting of our first total ash processing system and we'll update our capital spend plans when that timeline is more clear. Similarly, for our UK project pipeline we look forward to providing more color our planned spend as those projects progress towards financial close. So keep in mind that the UK projects will be project financed with the required equity investments shared with JV partners.

Please turn to Slide 13 where I'll conclude with an update on our balance sheet. At June 30, net debt was a little over $2.4 billion, down $41 million from the beginning of the year. We had one financing transaction worth noting during the quarter. We issued $30 million of 20-year tax exempt corporate bonds at a coupon of 5% to fund capital expenditures in the state of Virginia. We've tapped this very attractive market in the past to fund spending in other states and we'll continue to look for opportunities like this to optimize the cost, tenure and structure of our capital.

At quarter end, our consolidated leverage ratio was 5.7 times, which is a tick higher than Q1 as expected. Remember of course that this is over a full turn lower than where we were at this time last year. The senior credit facility covenant was three times at quarter end which is flat sequentially. As previously discussed, we anticipate remaining in this range on both leverage ratios through the end of the year, with our long-term plan to de-lever meaningfully further over the next several years.

With that opera tor, let's open the lines for Q&A.

QUESTION AND ANSWER SECTION

Operator: Certainly. [Operator Instructions] Your first question comes from the line of Tyler Brown from Raymond James. Please go ahead. Your line is open.

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

Q

Hey, good morning.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Good morning.

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

A

Good morning.

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

Q

Hey, nice quarter. Hey, Steve, I appreciate the comments on the potential to rationalize some assets. I think you noted a few smaller items. But maybe as you see it right now, how much in proceeds do you think that that pipeline could potentially yield?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

It's interesting, we're not really doing it from a proceed standpoint. I mentioned this the last couple of calls. When I first got here, I asked for kind of a ranking of our plants from an EBITDA and free cash flow standpoint. And there are a handful of plants at the bottom of that list that we've been – I've been putting pressure on the team here to either fix them or sell them or we're going to shut them down. So, Warren County, we just talked to the employees, so we were able to talk about it on this call. But that's a situation where the market there and it's a case in several of these plants in this handful at the bottom of the list. The market for tip fees and the market for power is just not good and we didn't see it changing anytime soon. So, in a case like Warren County, we'll try to sell the facility but we've kind of put a stake in the ground at this point and said and if we don't sell it, then we're going to shut it down.

Now interestingly, challenging the challenging the same team, the third regulated medical waste permit that we got, that was another plant that was having some trouble and we were able to get the third regulated medical waste permit that allows that, which is of great value to that plant, which basically allowed us to kind of fix that plant. So again, kind of a long answer to your question but we're focused on trying to look at the plants that aren't really performing or we're not getting a sufficient return on our efforts and trying to fix them, and if we can't fix them then we'll try to sell them or exit from the situation.

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

Q

Okay. Yes. That's very helpful. And maybe just switching gears over to waste pricing. So same-store waste pricing was up 3%. That is a nice acceleration I think from the last couple of quarters. But do I have this right that it benefited from the escalators' higher spot pricing and profiled waste but didn't that number also include a drag from Fairfax coming back?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp. A

Yes. Go ahead.

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

Yes. So Tyler, you see the impact of Fairfax from a mix perspective in the average tip fee, but the 3% growth is truly a same-store. So it does not impact negatively by Fairfax in the mix. And you hit the drivers within the...

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

Okay.

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

...within the 3%, we're in the ballpark of 2% on our contractual escalators on the tip fees. And then spot pricing I mean, we're approaching double-digits now in our core markets.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp. A

But you are right, Tyler, on slide 4, you look at the contracted line; it's down in Q2 2018. Some of that is – a lot of that is from Fairfax. I mean Fairfax is typically aren't as good as some other markets out there. So I mean you're looking at the right way.

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

Okay. And then maybe my last one here. If we think about though into next year, I mean, CPI is getting better. I presume there's a lag to that. It feels again that the spot market's very strong profiled waste really has good footing again. Why wouldn't we see same-store pricing be better than at 3% in 2019?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp. A

We very well might see that. I keep telling the employees it's a good time to be a waste company. Certainly, there's markets that are out there where there's upward pressure on pricing and that – and we're seeing it. As contracts roll over, now realize we have 85% or so of our waste under contract. So those contracts roll we're pushing pricing at this point. So yes, I think you will see upward movement.

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

And on the contractual escalators, a lot of those kick in mid-year.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes.

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

A

So, we'll start to see that more going forward. I mean, it's – I mean you touched on all the drivers. It's hard to find the headwinds right now to waste pricing.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Right. I mean that's a good way to put it.

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

Q

Okay, perfect. Thanks guys.

Operator: Your next question comes from the line of Michael Hoffman from Stifel. Please go ahead. Your line is open.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Hi. Thank you very much. Can we talk a little bit about the thought process behind whether you close and keep or close and sell, and is it a function of just the end market pricing or is it also size?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

It's a function of how much free cash flow we can generate from a facility and EBITDA to a lesser extent, but – so what I did. When I walked in the door here Michael, I said rank the plants. I want to see who our best performers are and who aren't our best performers and I've been putting pressure and it's hitting a crescendo at this point. I've been putting pressure on the team here to say those plants that are, where we're not getting what I'll call a fair return for our efforts, we either need to get out of the plants or sell the plants or fix the plants. And I'd say there's a handful – we get a handful of plants in this category, some of them we will fix, some of them we have – we have fixed, and the regulated medical waste permit is a good example.

And then some like Warren, I just didn't see – we came to a decision that, it just – it's just – with that tip fee market and power market and there wasn't going to be a change anytime soon. So, so there is – and it depends on the plant. I mean you've been close to these plants for a long time. There's different drivers on different plants and I just got to the point where it was time to make some decisions on our underperforming plants and that's why – that's why you see certain things like the impairment the – the impairment write-off that we took. I mean, we're starting to make some of the harder decisions and I think they're the right decision. If you're a shareholder, it doesn't have a big impact from a financial metrics standpoint, but if you're a shareholder you would want us to look at these plants and say, okay, you're not getting a reasonable return for your efforts there.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

And I'm curious, is – is there, could this be better in other people's hands because of different corporate structural issues that could allow that to be effective and that's why there potentially could be a sale opportunity?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes. Yes, I mean, there might be others who look – who have got a different cost structure or quite frankly, they want to – and we had some interest in some of these plants, who want to come in. The waste permits are valuable. And so, they might have new technologies that they want to try out and they want access. They want a site where they don't have to go through the permitting process. So the permits in and of themselves may be valuable and that's kind of what we're looking at. We've been out there with our M&A team talking about some of these plants, where it doesn't look like we're going to – it doesn't look like we're going to fix them, is there a potential buyer who's got a different view of the asset or the location or the fact that it's got a great connection. There's certain physical attributes that may be valuable to some other buyers.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Got it. And then on the profiled waste side, there are sort of two approaches to this. I can't – you maybe don't want to get down to a plant level, which three plants got the permits or if you will, please, but what part of the country are you being able to take advantage of this?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

So in the West, and then in the East. So middle so – and that's really how it plays out. There is – there is – that – where the population centers are, and we're looking at some other locations. So we've got good coverage out in the West and now we're starting to look at the East Coast more so.

And so later this year, I mean, the regulated medical waste is a very good market. The tipping fees are orders of magnitude higher than MSW as you well know, and there is a kind of a shortage of disposal for regulated medical waste in the U.S. and so we've been working with some of the folks who pick-up regulated medical waste, because that's not our thing, and talking to them about where they need to have coverage, and I think the East Coast needs some additional coverage is my take on it.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. And then lastly, inside the profiled waste, you said less than 10% is medical waste. Can you frame for us the characterization of the other 90%?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Some of it's – it's some of the things we've talked about. Some of it is folks who want assured destruction. So think about fashion houses, purses and jeans and things that they want a sure destruction. You have some folks who – it's drug take back programs and that you're starting to see us in the news a lot around drug take back programs because with the opioid crisis, and this is a small part of it too by the way; but it's going to grow – is folks who want to make sure these drugs are – there is assured destruction of the drugs. And then a good part of it quite frankly are just companies who want to advance their sustainability goals. So, and it's all the big guys. You think of Subaru, you think of any large company, most of them have a sustainability goal, and one of those goals tends to be something around having less of their waste go to a landfill and go to alternative disposal, and some of its recycling. But that's what drives, that's the biggest category. It's kind of all the name brand companies. For example, I saw AT&T issued a press release a few – like a month or so ago where they want to take their waste from 100 of their plants, and not have it go to landfills. And if they're doing that, there's a opportunity for us to take that waste into an Energy-from-Waste plant. That's the biggest part, that's the biggest component it though.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

And where I was going with that was, have you tapped out aspects? Like the medical waste piece, sounds like there's opportunities for that, that go from 10% to something higher, maybe the drugs money and clothes is tapped, but sustainability still has room. That's what I was trying to understand.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

I think they all have room. What we're going to need to balance is how much MSW we take in and quite frankly, and we get this question a lot is – they have a different impact on the plant and so we price these different types of waste depending on the work our sales team does, and our engineers on what impact that might have on plant maintenance, things like that. So it's kind of a complicated equation, but there is upside. I mean I think we've talked about this before. We're at roughly 900,000 to 1 million tons, in that range of profiled waste and we can get up to 2 million without too much trouble and then we'll start to look at how much MSW we want to back down under long-term contract.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Last question on this being, the market is flooded with volume right now, between the China brands.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

There's got to be a lot of plastic, a lot actually of highly assorted paper, that is potentially a double-edged sword.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

I mean what the implications for you to take advantage of driving price up, but also as their performance related issues because of BTU limits, things like that. How do we see that balancing act?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes, that's a good question, Michael, because I don't think a lot of people fully understand it. When I was on Jim Cramer's show I started to talk about this a little bit. We prefer that the recycling gets recycled. Quite frankly it burns too hot, I didn't get into this level of detail. But it burns too hot in an Energy-from-Waste plant, which is counterintuitive to the most folks. So – but we're so far – and so there's a lot of waste out there. You know this. The other large waste companies reported this week. Good time to the waste company. There's a lot of waste out there.

We are not seeing bales of plastic or bales of paper come into our facilities, and quite frankly if they come there, we say go do what consumers wanted to do, which is recycle that material. But we are starting to see kind of paper and plastic get lost in the MSW, and so we've actually added some more eyes to our tipping floor. So put people on the tipping floor to make sure we're not getting kind of plastic sliding into the MSW. And so I'd say there's again a handful of plants where we're starting to see the BTU content creep up a little bit, and so there's something going on there. But it's not large scale at this point. Again, we're not seeing bales of plastic or bales of paper show up at our plants.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

All right. I'd say one last question. There's a new county executive being elected or should be elected, he won the primary. And so it's a de facto in Montgomery County Maryland. And he's running on a platform of, I'm going to close that incinerator.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Would you handicap it at?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

You know I don't know they're going to do with their waste. They have a beautiful system there, right. Right. So, and they spent a lot of money on it. It's the most advanced system I've come into contact with. You probably had the same reaction. So, I don't know if I can handicap it, as much as they spend a lot of money on that system, I think there's going to be some folks on the other side of the equation who are saying know okay, what else are we going to do with our waste? We're going to start to bury in the hole in the ground? And so I think more to come there but we have been watching this situation there and that's – that's a – by the way that's a plant that we just operate and if they go in a different direction, they go in a different direction. It won't have a material impact for us.

Michael E. Hoffman
Analyst, Stifel, Nicolaus & Co., Inc.

Q

Okay. Thank you.

Operator: Your next question comes from the line of Noah Kaye from Oppenheimer. Please go ahead. Your line is open.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.
Q

Good morning. And first Steve thanks for the update on the UK pipeline...

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

Sure.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.
Q

Good to see you set that date. And hopefully the timeline is firming up a little bit more there. I wonder if you could give us an update on the timing for your [ph] beneficial last (36:34) processing just when that is, when do you think you can open that facility?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

Yes. So, the TAPS work continues. Pennsylvania, so the first system will be in Pennsylvania. We've got the site for it, and we're and then the other side of it is Pennsylvania needed to issue an umbrella permit because it's the first of its kind, and they did that now and then we had them issue our specific permit for this site, which again is going to be a ferrous. So it's in ferrous sales along with where our recovered metals recovery systems are. So we can – we've got some cost synergies there and things like that but we now have issued our specific permit for that site and we have to give him a way out of the – of what we're going to put in there. That's in the process now. We suspect that will get wrapped up, probably early fall here, in that timeframe

And then at the same time, our technology provider is actually building some of the units. So we're modularizing some things and we were – one of the team was down there last week looking at some of the equipment that's already being built. And so we expect we'll start kind of construction in earnest in kind of in the fall timeframe. And then we're looking at early next year or first quarter kind of timeframe to start – start the facilities up.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.
Q

Right. And was that called out in the growth capital schedule?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

No because we don't have the – we don't have the exact time – we don't have the permit yet. Once we get the permit, we'll firm all this up and then we'll also give you kind of – well, we've told already, the capital is in the $25 million range, and then we'll give you some idea on what we think the financials are.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.
Q

Okay, great. And one more from me. I think more folks are starting to look at 2019. We heard that for the waste companies. Obviously not looking for guidance, but I do note that there are some one-time items this year that may not repeat next year. And I just want to make sure we have a full view to that at least halfway through the year here. You're getting about I think $10 million of insurance recoveries on Fairfax. You're not going to have, say, you know $3 million to $4 million of EBITDA from Dublin. Anything else as you kind of look at what's been done so far in the balance of the year? Stuff that you might call out as non-recurring?

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

A

Yes. Hey, Noah. It's Brad. And, yes, I mean I'll start with the caveat that you already noted. I mean it is early for us to be talking 2019. But in terms of the big movers, you mentioned Dublin of course benefiting us in 2019 will be the startup of the operations at the Manhattan MTS under the New York City contract. Round numbers, those probably wash, I mean, I think for modeling purposes at this point. I think the big driver – as we've been talking about, the big driver next year is going to be organic growth and that 3% to 5% percent annual growth target, we think that's the right – that's the right expectation for people to have and by the way that 3% to 5% would be inclusive of or net of the $10 million or so of business interruption insurance that we expect this year. So, 3% to 5% truly incremental.

And then, the – the big variable you're left with is commodity prices. On the metal side, those prices obviously tend to be volatile, though there's pretty good reason to feel bullish about metals prices as we move forward. And then, on energy prices, I would note that the – the curve is slightly backward dated. So you'd probably see energy prices take a step lower for us next year. Again, that's just based on what the forward curve looks like today. We'll see how it plays out. And then the other item impacting the energy line is capacity. So we are generating about $50 million of capacity revenue this year. Based on the results of the capacity auctions in New England and PJM East, which now are two years ago now; we're probably looking at a $5 million to $10 million decline on the capacity revenue line next year and that's one that people may not have been focused on up till now. That's really it. And again, our focus is on all the things that we're doing to drive that 3% to 5% as high as we can.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.

Q

Okay. And so just to clarify, when you're talking about – this was really helpful, but to clarify, you said that the 3% to 5% you're thinking about inclusive of even the $10 million rollback. So the number for this year is the baseline number for next year. Is that what you mean or you're going to characterize that? Okay.

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

A

Yes. That's correct, yes.

Noah Kaye
Analyst, Oppenheimer & Co., Inc.

Q

Perfect. Thank you so much.

Operator: Your next question comes from the line of Jeff Silber from BMO Capital Markets. Please go ahead.

Jeffrey Marc Silber
Analyst, BMO Capital Markets (United States)

Q

Thanks so much. Just a couple of quick follow-up questions. One is on the Warren County plant. Is that a positive contributor to free cash flow right now or has it been?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

It is – it's kind of going in and out of positive over the last several years. You're not going to – you're not going to notice that it's closed down from a free cash flow standpoint; let me put it that way.

Jeffrey Marc Silber
Analyst, BMO Capital Markets (United States)

Q

Okay. That's fair. Are there any other related cost that might be one-time in nature?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes. We've kind – we've done, I've been through this before in a previous life. We've done the analysis of keep versus shut down, and there are some costs. I mean we've rolled that all into the analysis when we look at whether it was better to shut it down and potentially sell it. Again, we were talking about that a little earlier, but there are – there are some costs.

We have some kind of lingering obligations to take in waste, but I think there's a – so we're going to be taking in some waste and putting it into the landfill that's right down the street, and that's part of the problem there is there's a landfill right down the way there. So there's some lingering cost, but when you do the analysis, it was better to – the shutdown case was better financially than the keep running case.

Jeffrey Marc Silber
Analyst, BMO Capital Markets (United States)

Q

Got it. And then just switching gears over to the metal side of the business, you mentioned the impact, or potential impact of the shift to ferrous from non-ferrous on sales or revenues, excuse me. Is there a meaningful impact when you see that shift on EBITDA?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

This is – the heavy metal, this is – so the impact so far, again ferrous is better, non-ferrous is – the bigger pieces or heavier pieces of non-ferrous that are going to China – China has kind of shut their doors for the time being. We'll end up selling that material in Europe, and it will cost us – from an EBITDA standpoint it will be a few million dollars, but it's not a big impact. It's – quite frankly, we're looking at, okay when do we – when do we want to sell this material as trying to going to open up. And there's actually part of it – I won't get too detailed here, but part of it is trying to get value for the zinc that's in this metal and there's some self-help where we can take the zinc out ourselves and sell it separately. So there's – we'll sort this one way or the other but over the remainder of this year, it's probably a few million dollars or so from an EBITDA standpoint. It's not a big deal. That's why you heard me say, when you kind of put everything in the hopper and look at it, we kind of – we're at the same range, ferrous is a little better, non-ferrous is a little worse.

Jeffrey Marc Silber
Analyst, BMO Capital Markets (United States)

Q

Got it, and again this is all incorporated in the EBITDA updated guidance you gave us earlier?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

That's correct. Yes, that's correct. Yes.

Jeffrey Marc Silber
Analyst, BMO Capital Markets (United States)

Q

Okay. Just wanted to double-check on that. All right, thank you so much.

Operator: Your next question comes from the line of Brian Lee from Goldman Sachs. Please go ahead.

Brian Lee
Analyst, Goldman Sachs & Co. LLC

Q

Hey, guys thanks for taking the questions. Maybe just...

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Hi, Brian.

Brian Lee
Analyst, Goldman Sachs & Co. LLC

Q

...one quick. Hey, good morning. A quick follow-up on the previous one. Just I appreciate the EBITDA color on the non-ferrous impact. Can you actually quantify the – from a tonnage perspective, I may have missed it, but what China represents as a percent or of the kind of 28 to 33 sold tons of guidance for this year?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

20% of our non-ferrous volumes have historically been shipped to China.

Brian Lee
Analyst, Goldman Sachs & Co. LLC

Q

Okay, great. And then just from again, I know you're too early to really talk about 2019. But as you think about that part of the business and try to set some early expectations for ferrous versus non-ferrous mix, I mean, that's something that you're navigating here through the back half of the year, but is that something you think will be a structural shift we need to be maybe factoring into our views for next year and going forward or is this a view that it is more of a temporary dynamic and ultimately you do normalize back in China?

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

A

Well. I think – hey Brian, it's Brad. I mean, that's very difficult to predict, given the political and trade undercurrents here between the U.S. and China. I think what we've been focused on is, and Steve touched on removing the zinc from the material in order to sell that separately and generate value there, I think what we've really focused on and we're at a great point here as we sit here in 2018 and look forward to where, with the centralized processing – I'm talking about the non-ferrous business. With the centralized processing facility at Fairless Hills, we have the ability to react to whatever happens with China or any of the other end markets. We could sell domestically, we can send it East, we can send it West.

And so obviously we can't control what happens in the market. But I think we're in a position to react appropriately. And so long story short, impossible to answer the question you're asking. But I think there are some gives and takes with all of this. So with these political undercurrents, we're having to pivot where we sell the – as Steve said it's a heavy fraction of our non-ferrous, most of the non-ferrous is aluminum that we sell domestically. But then going the other way is we're seeing much stronger U.S. Steel production, mill utilization and that flows through into ferrous scrap pricing and so our outlook for ferrous has gone up. How that plays out, your guess is as good as ours.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp. A

I mean, the nice thing is that versus 2015 when – when there was a lot of turmoil in the metals markets, we've got more – we've – we've got more self-help now where we can pivot in a lot of different directions and so that's it. That's the thing that's changed kind of during the last several years as we've got – we've got more optionality associated with the metal that we – the product that we're selling, the quality is better and then where we sell it.

Brian Lee
Analyst, Goldman Sachs & Co. LLC Q

Okay. No, that's great. It all makes sense. Second question, and I'll pass it on, is on the energy business, you mentioned the – the 15-year Marion County PPA. Any sense of pricing that you can provide in terms of where that got struck versus maybe the fee average or contracted average and then, you specifically called out the renewable attribute. Could you elaborate on what that means? Are you getting – are you selling recs along with the power? And then maybe just lastly on that – on that line of questioning, any other sort of PPA activity or interest that you are seeing in other areas of the fleet right now? Thank you.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp. A

Yes, so, Marion, basically, the new contract – the pricing is closer to our fleet-wide average right, and – because that – that previous pricing and it's not a – it's not a big plant but the previous pricing was pretty low. So, we were able to enter into a PPA that's closer to our average pricing. And I don't want to get into actual pricing. There are some sensitivities around that. We were pleased with Marion and we – and I mentioned this before. We are looking at other facilities to see where you have local folks who are interested in the green attributes or the environmental attributes of Energy-from-Waste plant.

So effectively buying Green Power. And so, we have a lot of activities underway where we're – we're looking at direct selling to companies or it's not usually utilities, but it's companies who think it's really somewhat novel to be able to take their waste into an Energy-from-Waste plant and get the power back, right, so kind of a round trip.

So, we're looking at those types of situations. We're also looking at a lot of situations where we – where we can get more from the steam that we produce. So, there has been a number of activities underway, and I've mentioned them a few times, where we're looking in and around our plants and we had a whole effort. We have a whole effort underway where we look in and around our plant, to sell steam rather than electrons, because steam is more valuable than electrons these days. And so that's the kind of work we're doing. We wanted to highlight Marion, because it is – I don't think anybody has signed a long-term PPA agreement in many, many years in the U.S. So we thought that was interesting, and also that the fact that it does help pricing overall and it's a healthy economic proposition to that, that Energy-from-Waste plant.

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

And Brian, just I'll put a slightly finer point on Steve's comment about the pricing being consistent with the fleet average. I think, the way to think about it is it's – you are generally consistent with our fleet average for our contracted sales, not the overall point.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes. Good point.

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

A

And as Steve also mentioned previously, we have been selling there at market prices in a market that's probably under pressure relative to what our average is for the open position across the fleet.

Brian Lee
Analyst, Goldman Sachs & Co. LLC

Q

All right. Thanks for the color guys.

Operator: Your next question comes from the line of David Katter from Baird. Please go ahead.

David Katter
Analyst, Robert W. Baird & Co., Inc.

Q

Good morning guys, thank you for taking the question. I was – I just wanted to ask about the 3% to 5% growth that you guys referenced and I'm sorry if I missed it but can you talk about some of the capacity headwinds that may happen next year and then the 3% plus same store pricing is factored into that. So if you could, what's the breakdown of that growth between pricing and maybe volumes or other initiatives?

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

A

Sure, David. It's Brad. So just to clarify, our 3% to 5% organic growth target is exclusive of commodity price changes and the change in capacity rates, we would – we would categorize as a commodity price change. So you think about it in two categories. In this – in this case where 3% to 5% would be growth in waste pricing to the extent that we have additional capacity for greater plant production through things like continuous improvement, metals recovery. So think of it volume generally and then the capacity as I mentioned a few minutes ago, as we sit here today it looks like we have a headwind of between $5 million and $10 million next year on the – on the capacity line which again is – is separate from the 3% to 5%.

David Katter
Analyst, Robert W. Baird & Co., Inc.

Q

Got it. That's helpful. Thank you. And last one from me, can you remind us on the kind of construction timeline for some of the projects in your pipeline? So I know if they all get under construction by 2020, how long does it take from construction to kind of seeing the benefits flow through the P&L?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Construction on energy plants is generally about three years. So we're expecting to have four in construction by that 2020 timeframe.

David Katter
Analyst, Robert W. Baird & Co., Inc.
Q

Got it. Thank you, guys.

Operator: Your final question comes from Tyler Brown from Raymond James. Please go ahead.

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

Hi.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

We lost you a little bit there, Tyler.

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

Oh, hey. You there?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

Yes.

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

Hey sorry, sorry. Hey Brad, were the hydro – yes, sorry, were the hydro assets, were they consolidated or were they in equity income?

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

Equity income.

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

Equity income. Okay. And then again, I hate to kind of beat on this capacity thing, but I thought I read earlier this quarter that your PJM capacity auctions were actually pretty strong on the closure of some nukes in coal capacity. I get the $5 million to $10 million in 2019 but won't that rise in 2020 or 2021?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.
A

Yes.

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

Yes.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes, good point.

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

Q

Will it – will it rise over $50 million?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

The recent capacity auctions were improved, right. So that's coupled with two years, three years out now and that now come back around. And you had another question. I'm sorry I interrupted you.

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

Q

No. No. Sorry. Will it – will it rise back over $50 million or was it just hard to say?

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

A

Yes. I mean, it's pretty premature for us to give that specific guidance on it, but – but certainly as you point out the auction results more recently have been more positive than what we'll realize from a couple of years back next year.

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

Q

Okay. And then just lastly is – I may have this wrong, but is Marion County, is that in EBITDA contributor under the new PPA, meaning is it incremental EBITDA positive?

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Yes. Yes, it is.

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

Q

Okay.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

It has improved the economic proposition. I think in my prepared works – words, I said it would improve the economic proposition of the Marion County facility. So that's what we're looking at. I mean, we're going to be producing the power. Power's coming out of these plants or steam. It's how do we get more value for that. And so, this is a good example of us looking at a facility going, we can get more power in our – in our electric – our power group going how can we get more value for that and figuring out a pretty clever way to get a long-term increase in our power pricing.

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

A

And Tyler, just one detail on that PPA. We wouldn't see any benefit from that immediately. It's really going to be more of a 2020 and beyond story.

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

Q

Oh, okay, that's very, very helpful as well. Well, anyway, I appreciate the time and again, nice quarter. Thanks.

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

A

Thank you.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

A

Thank you.

Operator: And there are no further questions at this time. I will now turn the call back over to Steve Jones for closing remarks.

Stephen J. Jones
President, Chief Executive Officer & Director, Covanta Holding Corp.

Thank you. Thanks everyone for participating in our call today. I want to take a moment to reiterate some of my earlier comments as we sit here today at the halfway point of the year. Things are moving along very nicely. We're excited about the progress in our organic growth initiatives, and we're focused on moving our UK development into construction. I'd like to thank the team for their efforts, which are paying off and we're committed to continuing this performance as we move through the balance of the year. So thanks again for joining us today and have a good weekend. Thanks.

Operator: This concludes today's conference call. You may now disconnect.