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AECOM (ACM)

Q4 2020 Earnings Call
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning, and welcome to the AECOM Fourth Quarter 2020 Conference Call. I would like to inform all participants this call is being recorded at the request of AECOM. This broadcast is a copyrighted property of AECOM. Any rebroadcast of this information in whole or part without the prior written permission of AECOM is prohibited. As a reminder, AECOM is also simulcasting this presentation with slides at the Investors section at www.aecom.com. [Operator Instructions]

I would now like to turn the call over to Will Gabrielski, Senior Vice President, Investor Relations. Please go ahead.

William J. Gabrielski  
Senior Vice President, Finance, Investor Relations, AECOM

Thank you, operator. I would like to direct your attention to the Safe Harbor statement on page 1 of today’s presentation. Today's discussion contains forward-looking statements about future business and financial expectations. Actual results may differ significantly from those projected in today's forward-looking statements due to various risks and uncertainties, including the risks described in our periodic reports filed with the SEC. Except as required by law, we undertake no obligation to update our forward-looking statements.

We use certain non-GAAP financial measures in our presentation. The appropriate GAAP financial reconciliations are incorporated into our presentation where available, which is posted on our website. As a reminder, we sold the Management Services business in January and intend to exit our remaining at-risk, self-perform construction
businesses which includes the October 16th sale of the Power construction business. These businesses are classified as discontinued operations in our financial statements.

Today’s comments will focus on the continuing operations of the Professional Services business otherwise noted. Today’s references to margins and adjusted operating margins reflect segment-level performance for the Americas and International segments. We will also refer to net service revenue or NSR, which is defined as revenue excluding subcontractor and other direct costs. Our discussion of NSR growth will be adjusted for the impact of an extra week in the fourth quarter. Our discussion of margin will be on an NSR basis unless otherwise noted.

Beginning today’s call is Troy Rudd, our Chief Executive Officer. Troy?

W. Troy Rudd  
Chief Executive Officer, AECOM

Thank you, Will, and thank you all for joining us today. I will highlight our accomplishments over this past year, our confidence in fiscal 2021, and review our strategy and key priorities. Lara Poloni, our President, will discuss key operational priorities; and Gaurav Kapoor, our CFO, will review our financial performance and outlook in greater detail. We will conclude with a question-and-answer session.

2020 has been anything, but a normal year, and I want to begin by acknowledging the great work of our teams over this past year. The pandemic had profound impacts on the daily lives of our employees and their families, our clients, our communities and our business. At AECOM, our professionals mobilized quickly to provide extraordinary support for our clients and communities during these challenging times. Our teams led the industry for disaster response work, including delivering temporary hospitals at the initial COVID peak in April. And we advised several prominent clients on their safe reopening, including the NBA’s successful season in Orlando.

We also changed the way we work, with more than 90% of our employees working remotely at peak. We launched innovative solutions to help our employees remain deeply engaged with our clients, including our virtual public consultation solution. Through it all, our client satisfaction scores have increased and our organization has come together in new ways to deliver for our clients. We all take great pride in what we have accomplished, and I want to say thank you to all of our people for their effort, dedication and resilience.

I also want to now acknowledge Randy Wotring, who recently announced his retirement after a 40-year career. Randy provided critical leadership to the organization over the past few years and his contributions have been vital to our success. On a personal note, Randy has been a great partner and I want to thank him for his support and continuing counsel.

Now, let’s turn to our financial results. Despite the unprecedented challenges in 2020, we improved our underlying business and delivered on our financial commitments, including 14% adjusted EBITDA growth and $341 million of free cash flow for the year. Both metrics exceeded our guidance. Our backlog remains near an all-time high, increasing 13% and providing us with visibility to execute with certainty. We continued to deliver new highs of profitability. The segment adjusted operating margin was 12.3% for the year, reflecting a 160 basis point improvement from fiscal 2019.

We're proud of the progress we have made on our margin improvement initiatives. To fully deliver on the value creation opportunity we see, we completed $455 million of stock repurchases between September and mid-November. We are confident in the trajectory of the business and we believe the purchase of our stock continues
to be a great opportunity. Accordingly, our board of directors recently approved an increase in our overall repurchase authorization to $1 billion.

Finally, we have made substantial progress in our transformation into a pure-play professional services firm. In January, we completed the sale of the Management Services business. And last month, we closed on the divestiture of the Power construction business. We are well positioned on the exit of our remaining at-risk construction businesses. With our accomplishments in the year, we are energized by a renewed sense of urgency to realize the full potential of our company. To describe how we'll unlock this potential, today we unveiled our new Think and Act Globally strategy.

As a global company with scale, our goal is to drive collaboration across the organization and to bring the best of AECOM to all clients. This strategy includes several key elements. First, we have simplified our business. This includes our recent announcement of one global design organization, creating clear lines of accountability on our key priorities, while creating a culture that embraces collaboration to bring our global expertise to each client.

Second, we're deepening our engagement with the clients to better capture untapped market share in our core markets. For instance, our top 20 clients represent approximately 20% of our NSR; and more broadly, our top 9 geographies represent more than 90% of our profitability. We will focus our time and capital on these relationships and markets with an emphasis on delivering the full breadth of our capabilities to our clients. We view this as a key organic growth driver.

Third, we are transforming how we work. This will include our Workplace of the Future initiative designed to leverage technology and innovation to create efficiencies and greater flexibility for employees. Our performance through the pandemic has made it clear that our people are consistently delivering for their clients while working remotely, including continued strong productivity and increased client satisfaction. Our clients are executing similar initiatives, which positions us to do what we do best, provide knowledge-based solutions to shape how our clients address challenges and to capitalize on new opportunities.

Fourth, core to everything we do is driving efficiency throughout our operations. By delivering higher margins, we can create a virtuous cycle of capital generation, wherein we are able to increase our investments in the business to drive further growth and increase our returns to our shareholders. Finally, we are committed to leading our industry in ESG, which is becoming a critical growth driver for our business. As the global leader in environment and water markets and a leading green designer and builder, we are uniquely well-positioned to capitalize on this trend.

Please turn to the next slide for review of market trends and our fiscal 2021 guidance. I'd like to begin with the brief comments on the recent US presidential election, which is poised to create opportunities for us. We are a leader in transportation, environment, water and clean energy markets, providing knowledge-based critical services to public and private sector clients who are increasingly focused on ESG and sustainability.

As it stands today, we see bipartisan support for funding to help our state and local clients weather the impacts of COVID, a continued focus on infrastructure investments as a job creator and competitive differentiator for the US, and an increasing regulatory emphasis on environment and water markets. This is great news for AECOM and we stand ready to deliver for our clients.

Looking across our markets more broadly, trends are mixed. In addition, for the impact of COVID in our markets, other factors are influencing our business. In the US, our pipeline remains solid. The client decision making has
slowed due to funding uncertainty. In UK, Brexit continues to weigh heavily on private sector activity, which is impacting growth even as our win rate and activity in the public sector improves.

And in the Middle East, weak oil and gas prices continued to create market headwinds. Nevertheless, our win rate remained high and backlog increased this year, including a win for a key nine-figure pursued in the third quarter, which will underpin our position in this market for several years. Encouragingly, tax revenues in the US have recovered from the lows earlier this year, and vehicle miles traveled and user fees are trending positively.

In Canada, Hong Kong and Australia, infrastructure spending remains a bright spot and we are benefiting. We are seeing indications that private sector clients are advancing major projects again. And we recently won a substantial environment contract from a large energy client. We're also seeing customers increasingly invest in new sources of clean energy, a market where our leading environment and energy capabilities position us well for growth. The efforts we have made internally to align our cost structure with changing market trends, has allowed us to deliver profit growth despite mixed market trends.

Turning to our guidance. We are forecasting another year of earnings growth in fiscal 2021, including adjusted EBITDA growth of 9% at the midpoint of our range. We're also initiating guidance for adjusted EPS growth of 23% at the midpoint. Underpinning this growth is the 13% backlog increase in 2020 and our expectation to improve our industry-leading margins by 90 basis points in 2021. As always, the cash generative nature of our business remains firmly intact and supports our expectation for another year of strong free cash flow.

Taken together, our results this year, our strategy for the path ahead inspire confidence in our outlook. While we recognized that certain markets are challenging, we're encouraged by how we've responded and delivered in fiscal 2020, and by the progress we have made on our ongoing actions to create a more resilient and a more profitable business. We have an exceptional opportunity to extend our position in the market, and I'm excited to be leading this great organization of professionals who share my passion in pursuing this opportunity.

With that, I will turn the call over to Lara.

Lara Poloni
President, AECOM

Thanks, Troy. Please turn to the next slide. We are energized by the tremendous opportunities in front of us, as we work to further distinguish ourselves in the marketplace. We hold number one rankings in several key markets including transportation, facilities and environment. And we are a top green design firm and green builder. From this position of strength, we are excited about what's possible over the next several years. Our Think and Act Globally strategy is designed to help us achieve our goal of setting a new standard of excellence in the Professional Services industry.

To identify areas for improvement, we conducted an in-depth analysis of our business in the eyes of our clients and against our competitors. This analysis revealed that we are an industry leader in client satisfaction. In fact, we have seen our client satisfaction scores increase through the pandemic and we continue to be widely regarded as a technical leader by our clients, which is a testament to our team.

We also focused our efforts on identifying organic growth opportunities. This includes our emphasis on better collaborating to bring our best to each and every client and deploying best practices that produce consistent results across the entirety of our business. In certain markets, we have delivered exceptional results for our clients and have a clear lead over the competition. However, we haven’t reached our potential for every client.
And as Troy noted, while our top 20 clients represent approximately 20% of our NSR, we see opportunities to grow our revenue and profit with these clients by upwards of 50%.

Today, we are focused on building stronger and deeper relationships with clients. This includes senior executive sponsorship of key pursuits and client relationships, leveraging the global expertise of AECOM on every key client account, targeting hiring based on expertise that aligns with clients’ priorities and accountability for results. This is a big opportunity for AECOM. While bringing the organization together to Think and Act Globally, we are also reinforcing our commitment to equity, diversity and inclusion. The ability to draw on diverse, global perspective is a competitive advantage for AECOM.

One key program to capitalize on this opportunity is our Thrive with AECOM initiative. This includes reverse mentoring programs with participation of our most senior leaders, expanded partnerships with communities to enhance the diversity about recruiting efforts and holistic anti-bias training programs. We must continue to embrace diversity and celebrate our differences to reach our full potential. In addition, we are positioned to fully capitalize on ESG opportunities. No other company is better suited to address these growing priorities.

We have a culture that is committed to building a better world and that is helping clients advance more sustainable and energy efficient solutions. Whether it’s managing the construction of LEED Platinum buildings in New York City, helping clients develop and implement energy efficiency and savings programs, or advancing proprietary solutions for the cleanup of PFAS and other emerging contaminants. We are uniquely well suited for the increased prioritization and spending on ESG initiatives.

In fact, more than 1,500 companies and 800 cities around the world have set their own goals to achieve net zero emissions targets. And we are working with our clients to advance their initiatives such as our work on the Washington Transit Department’s pursuit of an ambitious electric retrofit to their bus fleet. We are also working with Shell on the initial steps to achieve their net zero emissions target by converting traditional fuel stations to hydrogen, among the first in the European region.

Our unrivaled expertise differentiates us in the market and positions us to grow our business over the next several years. I’m excited about the opportunities in front of us. We are leaders in our industry and more focused than ever on prioritizing time and capital to our best growth opportunities.

With that, I will now turn the call over to Gaur, to discuss our financial performance and outlook in greater detail.

Gaurav Kapoor
Chief Financial Officer, AECOM

Thanks, Lara. Please turn to the next slide. Our financial performance in fiscal 2020 exceeded our expectations, highlighted by adjusted EBITDA and free cash flow above our guidance range and margins that exceeded our full year guidance by 60 basis points. I should also note that we exceeded our earnings guidance despite an approximate $15 million headwind from changes in foreign exchange rates compared to our plan. In a normal year, this would be an impressive outcome. To deliver this result against the uncertainty over the past year is a real testament to our team's commitment to deliver for our clients every day.

We have made important progress on our portfolio transformation over the past year. We sold the Management Services business in January; and in October, we closed on the sale of our Power construction business. Related to the sale of our Power business and the exit of our remaining at-risk construction businesses, we recorded an impairment to our balance sheet of $247 million in the fourth quarter. We have eliminated all stranded costs associated with the planned and executed business divestures.
With our transformation into a professional services firm, our business has several inherent advantages that enable us to perform through periods of uncertainty. We have a highly variable cost model which creates flexibility to quickly align our cost structure with market conditions. We have also demonstrated that our workforce is delivering quality work efficiently and effectively, while working remotely. Finally, we have a highly cash-generative business with high-quality public and private sector clients and a culture focused on cash, including incentive metrics for return on invested capital and shareholder value creation. These inherent advantages, combined with a near record backlog, creates visibility and confidence in our business and our ability to drive strong results. This past year serves as a great example of this.

Please turn to the next slide. In the Americas, NSR declined slightly on an organic basis in the year and our backlog increased by 14%, including 14% growth in contracted backlog. Our private sector clients were impacted by near-term headwinds from the pandemic and lower oil and gas prices. Our transportation and water markets performed well for the year, but budget pressures and slower decision making did impact the fourth quarter. Canada remains a bright spot. We delivered well against our plan for the year and more than $10 billion of infrastructure in stimulus plans support our expectation for another solid year in 2021. Our Construction Management business also performed well and maintains a near record contracted backlog across a diverse set of industries within our core market. Nearly, every project that paused earlier in the year has resumed activity and we completed several iconic projects during the year, including One Vanderbilt in New York and SoFi Stadium here in Los Angeles.

The Americas segment had a 16.9% adjusted operating margin for the quarter, which contributed to a 16.8% margin for the full year. This set a new annual high for the Professional Services business and reflected a 160 basis point improvement over the prior year. Our margin performance serves as clear evidence that actions we have taken to drive better profitability are delivering results.

Please turn to the next slide. Turning to the International segment. NSR declined by 4% on an organic basis in the full year with trends mixed across our core markets. In Australia, we delivered growth led by transportation and our backlog increased. However, our Greater China and UK businesses declined and the Middle East market remains pressured by low oil and gas prices. Our international backlog increased by 6% for the year, including an increase in our contracted backlog which creates visibility for fiscal 2021.

Importantly, our focus on improving margins delivered results. Our adjusted operating margin in the fourth quarter was 6.5%, an 80 basis point increase over the prior year. Since the beginning of fiscal 2019, our margin is up nearly 400 basis points. We delivered this margin improvement despite revenue declines which underscores our confidence in driving double-digit international margins over time.

Please turn to the next slide. Turning to cash flow, liquidity and capital allocation. We delivered another strong year of cash generation. Fourth quarter free cash flow of $619 million resulted in full year performance above our guidance range. We benefited from tax deferrals in the year as a result of COVID-related government stimulus programs, some of which will unwind over the next year. Importantly, our balance sheet is strong. We exited the year with gross leverage of 2.7 times, which is consistent with our long-term target to operate the business with less than 3 times leverage going forward. This is also an improvement from 3.4 times in the prior year.

Nevertheless, we remain confident in our ability to convert 75% of our EBITDA to unlevered attributable free cash flow on a normalized basis which is reflected in our $425 million to $625 million free cash flow guidance. Importantly, our balance sheet is strong. We exited the year with gross leverage of 2.7 times, which is consistent with our long-term target to operate the business with less than 3 times leverage going forward. This is also an improvement from 3.4 times in the prior year.
We are committed to allocating substantially all our available cash and free cash flow to share repurchases to ensure we fully capitalize on the value creation opportunity present in our shares. We completed $455 million of repurchases since September, which reduced our diluted share count by nearly 7%. And with strong cash generation expected in fiscal 2021, combined with our expanded stock repurchase authorization from $305 million to $1 billion, we expect to continue to be in the market throughout the year.

Please turn to the next slide. Our performance in fiscal 2020 instills confidence in the organization. We expect to deliver another year of earnings growth despite varied conditions in our markets. Key drivers of this expected growth are organic growth initiatives to continue capturing market share, benefits from execution of our restructuring and cost efficiency plans in prior year, and a streamlined organizational structure.

For fiscal 2021, we expect to deliver 9% adjusted EBITDA growth to $810 million at the midpoint of our range, which includes our expectations for another 90 basis points expansion in our segment adjusted operating margins to 13.2%. We are reintroducing EPS as a guidance metric consistent with our focus on creating per share value. We are guiding to adjusted EPS in the range of $2.55 to $2.75, a 23% increase from fiscal 2020 at the midpoint. Our guidance incorporates the benefit of already completed share repurchases in fiscal 2021 to-date and a 153 million average diluted share count.

With that, operator, we are ready for questions.

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**QUESTION AND ANSWER SECTION**

**Operator:** [Operator Instructions] Your first question comes from Sean Eastman with KeyBanc Capital. Your line is open.

**Sean D. Eastman**  
*Analyst, KeyBanc Capital Markets, Inc.*

Hi, team. Congrats on the strong finish to the year. I just wanted to start high level around the growth strategy. We're rolling out the Think and Act Globally strategy. Would just be curious to get a sense from you on the response from the employee base, maybe from a sentiment cultural perspective and just perhaps how engagement has trended recently relative to say two to three years ago? Some perspective on that front would be helpful.

**W. Troy Rudd**  
*Chief Executive Officer, AECOM*

Sure, Sean. It's Troy. Why don't I take that question and then I'll let Lara add to that. First of all, we've been having this discussion internally for a few months now and we've now unveiled the strategy. And I think this simply is, it's been very positively received. And I think our people, as I hear from them and as I speak to them, they're excited about the opportunity to be focused on our clients; to be focused on an equity, diversity and inclusion agenda; and to be focused on a broad ESG agenda.

It is absolutely what our clients are focused on and they're setting large ambitions and it's what our people are excited about. So, I also get the feedback that there's clarity to what we're focused on and that gives them – it gives them a real sense of directed purpose.
So Lara, do you have anything to add?

Lara Poloni  
**President, AECOM**

Yeah, sure. Thanks, Troy, and thanks for the question, Sean. So I think, absolutely, the feedback has been very positive from employees around the world. They’re excited about the Think and Act Globally strategy. In particular, I mean they’re excited that we’re going to use our scale and investments to expand our already strong leadership position across all the global markets and create value for all of the stakeholders and also creating at the same time an elevation of technical expertise and practice; and with that comes greater clarity on career paths for employees as well.

So, I think everyone’s very energized. It’s an exciting time and I’m very confident that we’re going to be able to deliver on this commitment. Thanks for the question.

Sean D. Eastman  
**Analyst, KeyBanc Capital Markets, Inc.**

Okay. Excellent. Yeah. I think that's important. Second for me, it's great to see you guys standing by the 15%-plus segment level margin target. It would just be great to get a sense for how achievable that is and maybe some sort of rough timeline. I mean, just with you guys exiting fiscal 2020 here and leading the pack here on margins, it'd just be great to try and get comfortable around that next 200 basis points essentially, and even just some broad strokes around that bridge would be very helpful.

Gaurav Kapoor  
**Chief Financial Officer, AECOM**

Hey Sean, this us Gaur, I'll take that question. You hit the nail on the head, right, as to what we have accomplished to date just over the last two-year period. We've had significant margin expansion. You saw that again in our 2020 results both in our Americas and International segment. And for 2021, even though we may have headwind, we're not expecting any growth built into our plan. We still see margin expansion of 90 basis points going to 13.2%.

So as we look forward beyond that, we're not giving any specific timelines. But what I can tell you, some of the initiative that that are in place specifically in international where our aspiration is really to continue to deliver significant margin expansion, as that's going to help us get to that 15% aspirational target. But if you just look at International isolation, it's up 150 basis points year-over-year, where we do expect top line headwind in 2021.

We still, based on all the actions we have taken initiatives that are put into play for 2021, we expect it to grow by another 100 basis points. And then beyond that, our global DCS strategy which Troy and Lara articulated to you about, is going to provide us opportunity to become more efficient in capturing better market rates and delivering to our clients. We're going to continue to flex on our global design services and our global business service center, and we will continue to have focus to make sure every capital dollar being spent in our International and Americas business has ROI focus and the right margin profile for us, which we've exited 30 countries globally and we will continue that rigorous process because that is now ingrained in the culture of how we operate.

And lastly, I'll also point to digital transformation and Workplace of the Future, those type of initiatives. But there is absolutely no doubt in our mind that those margins will continue to expand because continuous improvement is now being ingrained into our operational culture. And lastly, I'll just say before I turn it over to Lara to give you overview of the market, once these markets do stabilize and top line stabilizes for us, our new strategy of Think
and Act Globally will not only help us achieve peer margins in International, but it'll help us exceed those margins. That's what we're really shooting for here.

So with that, I'll turn it to Lara.

Lara Poloni  
President, AECOM

Yeah. Absolutely. Sean, we're absolutely focused on margin expansion. And if we look at our International business in particular today, we're seeing a lot of the trends in our core markets. Certainly, very focused on recovery and infrastructure which is obviously our strong foundation and an opportunity to really capitalize on our leading capabilities in ESG. And we're one, we continue to win a lot of work in that sector, particularly in the last years and at very strong gross margins as well.

So, I think it's going to remain a very strong focus for us. And in line with ESG, we're also seeing similar trends not just in the Americas, but in the Middle East, whether it's a sustainability work of – the work we're doing for NEOM, the coastal restoration opportunities in Asia. So, that combined with our strength in infrastructure I think positions us very well in addition to all the things that Gaur talked about to continue to improve those margins.

Sean D. Eastman  
Analyst, KeyBanc Capital Markets, Inc.

Terrific. I really appreciate the responses. Thanks.

W. Troy Rudd  
Chief Executive Officer, AECOM

Okay. Thanks, Sean.

Gaurav Kapoor  
Chief Financial Officer, AECOM

Thanks, Sean.

Operator: Your next question comes from Michael Dudas with Vertical Research. Your line is open.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC

Good morning, gentlemen, Lara.

W. Troy Rudd  
Chief Executive Officer, AECOM

Good morning.

Gaurav Kapoor  
Chief Financial Officer, AECOM

Good morning, Mike.
Lara Poloni  
President, AECOM  

Good morning.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC  

Yeah.

W. Troy Rudd  
Chief Executive Officer, AECOM  

Good afternoon for you.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC  

Thank you. Appreciate that. First, Troy, you talked about top 20 customers, 20% of revenues, going 50% over time. Can you share us a little bit more clarity on that? The top 20 customers like public versus private, I assume government agencies are weighted in that front. And is that growth you think over time is more organic cyclical growth? And what combination of this environmental social aspect that could – that these type customers can drive even further organic growth for you guys, as you lay out the plan?

W. Troy Rudd  
Chief Executive Officer, AECOM  

Sure, Mike. So first of all, when we talk about our top 20% of our top clients, it includes private clients and public sector clients. So, we don't differentiate between the two. And so, those are – again, globally, those are our largest clients. And as we think about increasing that, it's not about them spending more money; it's about us becoming more embedded within that client and taking market share or helping them with a greater portion of their initiatives or their spend.

And that's really what we're looking at is we're looking at effectively improving the market share or working with them in a greater capacity to take more of their overall spend. And certainly, focusing on an ESG agenda or a low-carbon agenda will help with that. We're very well positioned to do that type of work. And as we look across that client base, in fact all of our client base, we see that on their agendas ESG is important. And in particular, in that low-carbon agenda, they're all setting these large ambitious goals that they're working on developing plans to achieve and we're along with them to do that.

And then over the long period of time, the expectation is that we'll help them evolve and spend the CapEx to achieve those ambitious agendas. So again, it's about being closer to our clients, to have a better relationship and do more work, and to clearly help them with their individual ESG agendas which are of incredibly important to them.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC  

That makes sense. So my follow-up, Troy, is you highlighted certainly Q4 some of the headwinds that we're all seeing throughout the world, given COVID et cetera. Maybe you could break down a little bit on some of the markets that may be a little slower to recover, weighing through either the administration, confidence in vaccine, just getting budgets together? So, is it – it looked like more of a second half fiscal year weighted versus first half...
generally. And relative to your margin targets with peers, it sounds like you're not expecting much overall revenue growth in 2021. And if there is, that certainly could be upside. I just wanted to confirm that.

W. Troy Rudd  
Chief Executive Officer, AECOM

Yes. So Michael, I'll work backwards on your question. In terms of our growth, we're seeing this next year look flat. Potentially, we see some modest revenue growth in the year, but I think that's ultimately dependent on a number of different factors as you described. And I think a lot of that would be driven by the impact of things that might happen in the second half of the year. So there's no question that the impact of the pandemic has changed the world. But as we look forward, we have some optimism or even line of sight to things improving in the second half of 2021.

We also look at across our markets and it's varied. We have some markets where it's clear that our clients with government support have ambitious infrastructure agendas. We see that in Australia and we see that in Canada, we see that in China and even in Hong Kong. But here in the United States, we're seeing within our large client base, particularly state and local government client base, continued uncertainty over funding. But we do believe that with the change in government that in the second half of the year, there'll be some certainty around funding that might be helpful for state and local governments.

We see that their revenues – their used revenues, certainly for transportation, will be returning. And then, we also see opportunity for an ambitious presidential agenda focused on a climate change which again, has already said, our clients have great ambitions for. And then, there seems to be some – again, some interest in a broader infrastructure investment from the new administration.

So again, I'm optimistic those things are kind of lining themselves up to address some of that uncertainty that exists in our large US market today. So, that's why we're getting to kind of flat to a little bit of growth in this next year. But again, underpinning all of our expectations on revenue is our backlog. So, we're at least comfortable and well positioned to have some confidence around that range of outcomes.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC

Excellent, Troy. I appreciate your thoughts. Thank you.

W. Troy Rudd  
Chief Executive Officer, AECOM

Okay. Thanks, Mike.

Operator: Your next question comes from Andy Kaplowitz with Citigroup. Your line is open.

W. Troy Rudd  
Chief Executive Officer, AECOM

Andy, you're on mute.

Operator: Andy Kaplowitz, your line is open. Your next question comes from Jamie Cook with Credit Suisse. Your line is open.
Jamie Cook  
*Analyst, Credit Suisse Securities (USA) LLC*

Hi. Good morning and nice quarter. I thought the other interesting comment you guys made in the prepared remarks was the top nine geographies. I think you said represent about 90% of profitability. Just interesting in the context as we think about Americas versus International margins. So can you give us a little more color on which geographies are driving that?

And then, I guess, Troy, my other question just strategically as you're looking at your clients and your geographies more closely now with the divestitures that have happened, I mean are there opportunities for you to take a look at the portfolio again, you know what I mean, either by geography or by client base to sort of accelerate the margin opportunity here, just as you're now relooking at the company again? Thanks.

W. Troy Rudd  
*Chief Executive Officer, AECOM*

Yeah. Thanks, Jamie. So yes, when we look at the geographies, there are a small group of businesses that have – that just are highest returning businesses. As you can imagine, it's the ones we typically talked about. It is our Hong Kong, China business, our Australia, New Zealand business, our Middle East business, our UK business, Canada and the US; and that's the focus. But within that business, there are also opportunities to take the expertise that we have and to take it on a project basis to the opportunities that we think we're best positioned for. So, large complex infrastructure projects.

Those are the places that our groups of professionals perform their best work. And so, even from that platform we would look to go into those businesses and those areas of the world and support our clients and to support kind of large transformational projects. So when you talked about our margin, we certainly have opportunities internationally to continue to evaluate some of our businesses and decide whether or not we're going to remain as heavily invested as we have in the past in those places. So, it is part of our overall margin improvement agenda. It is an element of it and we're going to be continuously focused on being in the places and working on the projects for clients to create the best return on our capital opportunity.

Jamie Cook  
*Analyst, Credit Suisse Securities (USA) LLC*

I guess, then in – thank you for that. One other question, just on the guidance. I'm just trying to understand your comments on revenues relative to your contracted backlog growth that you ended the year. I don't know if it's just COVID conservatism and I'm just trying to understand here, it sounds like based on the comments relative to Michael's question, but should we really expect earnings to be sort of more backend loaded just with COVID in the way your fiscal year ends? Thanks.

W. Troy Rudd  
*Chief Executive Officer, AECOM*

Sure. So when you look at, again, what we're describing as revenue compared to our backlog, remember that within a design business there certainly is a significant amount in the year of kind of work that you book and burn in a year. And so, that's kind of where we see some of that softness related to the kind of the current funding uncertainty amongst some groups of our clients.

So, I guess maybe you can view it as us being conservative in our expectations about growth based on our backlog. But we think, just given the environment that we're in, it makes a lot of sense. There's a lot of things that...
kind of need to happen in the first half of the year that would create an improvement in the second half of the year.

Now with respect to the earnings, I think we've shown and our people and our management team has shown over this last year that we can react and we can kind of manage the business to maintain profitability throughout that period of time. So, I don't see our profitability being any different than it has traditionally been in prior periods or past years.

Jamie Cook  
**Analyst, Credit Suisse Securities (USA) LLC**


W. Troy Rudd  
**Chief Executive Officer, AECOM**

Thank you, Jamie.

Operator: Your next question comes from Andy Kaplowitz with Citigroup. Your line is open.

Andrew Kaplowitz  
**Analyst, Citigroup Global Markets, Inc.**

[ph] Yes. (00:41:10) Can you guys hear me?

W. Troy Rudd  
**Chief Executive Officer, AECOM**

We can, Andy.

Andrew Kaplowitz  
**Analyst, Citigroup Global Markets, Inc.**

Okay. Excellent. So, I just want to follow-up on the sort of new strategy, Troy, in the sense that we know you were at AECOM when you set your previous targets. But you did have this significant evolution of management and then streamlining of business that you've talked about. So, does this mean a new Analyst Day or maybe setting up some new goals at some point? I mean, you talked a lot about going after existing customers, so maybe some sort of above-market growth target. We know about your return target and your margin target, but can you get to those targets faster?

W. Troy Rudd  
**Chief Executive Officer, AECOM**

Yeah. Andy, first of all, I have the feeling that maybe someone our investment relations team fed you that question teeing up our Investor Day that we're going to do in December, where we're going to talk about that. So, thank you for teeing that up for us. But the answer is, we gave some targets that we thought the business was capable of achieving in 2019.

And even in spite of all the things that have happened in the world, we still have similar expectations around the profitability of the business. But as we look forward, based on the new strategy and based on our optimism that we see beyond 2021, we certainly will talk about the impact of how our strategy would adjust to our expectations.
around the future opportunities for growth in our markets and our business. So, we do feel quite positive as we move beyond 2021, and we'll talk about that in December.

Andrew Kaplowitz  
**Analyst, Citigroup Global Markets, Inc.**

It's helpful, Troy. And then, you said in the past that your state and local government pipeline of opportunities was down about 10% plus and environmental I think was down 5% to 10% plus. Is that what you're still seeing in terms of impact on the business? I mean, would you expect that impact to follow through to revenue in those particular businesses over most of 2021?

W. Troy Rudd  
**Chief Executive Officer, AECOM**

So, we've actually seen the trends get a little better than we had been seeing in the third quarter. So the overall trends about the opportunities that are available are a little bit better, but they're certainly are down year-over-year. But nevertheless, as I said, our strategy is focused on being closer and more deeply engaged with our clients, which means that we're looking to do more work for that particular client set and we've seen that.

So our transportation business – even though the opportunities were down, our transportation business grew, which means that kind of what we're doing to be closer to our clients and drive innovation for them is working. So well, the opportunity set may be shrinking or have shrunk, it's a little – it's not quite as bad as we had thought. But nevertheless, we're still seeing the opportunities for growth because of the strength of our business and the strength of our people.

Andrew Kaplowitz  
**Analyst, Citigroup Global Markets, Inc.**

Okay. That's helpful. Troy, then just one quick follow-up to sort of level set the guidance. Q1 is usually your seasonally weakest EPS quarter. Anything different about that in Q1 maybe you'd like to talk about?

Gaurav Kapoor  
**Chief Financial Officer, AECOM**

Hey Andy, this is Gaur. We expect our phasing on earnings to be consistent with fiscal year 2019 and fiscal 2020. We don't expect any difference.

Andrew Kaplowitz  
**Analyst, Citigroup Global Markets, Inc.**

Thanks, guys. Appreciate it.

W. Troy Rudd  
**Chief Executive Officer, AECOM**

All right.

Gaurav Kapoor  
**Chief Financial Officer, AECOM**

Thank you.
W. Troy Rudd  
Chief Executive Officer, AECOM

Thanks, Andy.

Operator: Your next question comes from Michael Feniger with Bank of America. Your line is open.

Michael Feniger  
Analyst, Bank of America Merrill Lynch

Yeah, guys. Thanks for having me on, squeezing me in. Just curious, I know there’s been a lot of talk about the 15% margin target. Did you guys put that out – obviously, we've gone through COVID, we know how COVID is weighing on the top line in some of your business areas. I'm just curious, Troy, just on the cost side, you guys over the last few months really have made a lot of announcement that you relocated your headquarters and you mentioned real estate optimization.

I think you also mentioned on the call something like 90% of your workforce remote. I'm just curious from that real estate optimization, maybe leases coming up, can you provide other buckets of structural upside that maybe we're not seeing in 2021, but has tailwinds for 2022 and beyond?

W. Troy Rudd  
Chief Executive Officer, AECOM

Yeah. So, let me maybe give you the headline on it and then I'll let Gaur give you some of the details. But again, this is going back to 2019 where we set that 15% target. And again, we described it as our ambition. What we did describe was along the way of improving our margins each year. And so, we did set a target back in December of 2019 for this coming year. And as you've seen from our guidance, that's a target that we're shooting to achieve. So, we're looking to get above 13%.

So when you look at everything that's happened in this last year, despite all of that we've been making changes to business to again achieve those margin ambitions. So again, it becomes a little difficult to say that the path of 15% will be the same because the answer is, the world changed, but we're committed to delivering on that ambition eventually. And the best thing I can point to is the fact that given everything that's happened in this last year which is not a normal year, we still have the expectation to get to the margins that we said we would in 2019 and be on the path to that ambition.

Gaurav Kapoor  
Chief Financial Officer, AECOM

Hey Michael, this is Gaur, just continuing on what Troy articulated. We have a feeling full confidence not just based on what we have accomplished over the last two years, but even when you look at 2021, it shows that we still have low-hanging fruit that we need to address. It's reflected in the 90 basis point margin expansion you see from 2020 to 2021. And we feel like we're just getting started, right. It's for a lot of things I mentioned earlier, the initiatives that are available to us back in December 2019 when we communicated the 15% margins that that's going to be transformational, it's aspirational.

We're sitting here today and we're starting to see little blocks to that path being developed and we're starting to develop what our execution strategy will be on each one of those, starting from again our one global DCS where we have market-leading franchises in our core markets where we either dominate the first or second spot. And as we execute on better capture rates with already industry-leading margins, it's going to really allow us to drive
profitability not an absolute number, but also on a margin expansion. And for all the reasons I mentioned on International as well, would – always a continued focus on ROI and our markets to ensure its meeting our capital thresholds.

Michael Feniger
Analyst, Bank of America Merrill Lynch
Okay. I appreciate that. You mentioned a lot of International, is there any reason why you can't get to a double-digit margin. Is that possible or is that structurally not, not in the cards?

Gaurav Kapoor
Chief Financial Officer, AECOM
We will absolutely get to double-digit margins. As I stated, our ambitions are, just like we're in Americas where we're far ahead of our peers on Americas margins, those are our same ambitions in International.

Michael Feniger
Analyst, Bank of America Merrill Lynch
Fair enough. And...

W. Troy Rudd
Chief Executive Officer, AECOM
Yeah. This is Troy. Just to add something to that is, there are sometimes easier ways to improve the overall profitability of the business. And certainly when you're focused on two countries and a fairly large business, it becomes a little bit easier to do that. We started on this path to improve International margins by exiting 30 countries; that was no small feat. It sounds easy, exit 30 countries, but it's a tremendous amount of effort to do that and it takes time to do that when you're thinking about finishing projects for your clients and then leaving that business.

So, it's just a more difficult path. It takes a little more time. But as Gaur said, the path ultimately is the same. We focus on doing the same things. It just takes us a little bit longer time to achieve it because it is more difficult.

Michael Feniger
Analyst, Bank of America Merrill Lynch
Fair enough. And just my last question. If I look at – your net debt stands at $380 million. I think you guys plan to generate $425 million to $625 million of free cash flow. Net Leverage right now is just 0.3 times. You guys trade at a discount with some of your peers. Just, Troy, do you think you need to use that balance sheet to fill out your portfolio, to better compete with those peers? Or do you like where your portfolio sits and that cash can strictly just go to really closing that valuation gap? Thank you.

W. Troy Rudd
Chief Executive Officer, AECOM
Yeah. Well, first of all, our professionals have no problems competing with their peers. And you can see that in our backlog outgrowing our peers and you can see that based on our number one position or number two position in the markets that we're in globally. But I will say, it's obvious that people haven't recognized we're dramatically different company than we were a few years ago. And we have every intention of using our capital to buy back our stock, and with the great support of our board and you've seen that in the $1 billion authorization, they just approved.
Operator: Okay, your next question comes from Steven Fisher with UBS. Your line is open.

Steven Fisher  
**Analyst, UBS Securities LLC**

Hello. Thanks. Good morning, guys.

W. Troy Rudd  
**Chief Executive Officer, AECOM**

Hi. Good morning, Steve.

Gaurav Kapoor  
**Chief Financial Officer, AECOM**

Good morning, Steve.

Steven Fisher  
**Analyst, UBS Securities LLC**

Good morning. Typically, you guys see a little more working capital sowing in the fourth quarter helping cash flow and you didn't have that much this quarter. And so, I'm wondering if was there any better profit conversion or key drivers there? And you mentioned some of the government unwind of some of the support there, what's the cadence of that unwind? And then, just as you think more big picture about cash flow, do you see potential to smooth that out over time from a seasonal perspective relative to where it's been historically?

Gaurav Kapoor  
**Chief Financial Officer, AECOM**

Hey Steven, this is Gaur. I'll respond to those questions. You're absolutely right, working capital conversion was much better than what we have experienced in prior years. And it kind of goes into your third question about having better seasonality of cash. That has been a focus of ours and now we're starting to see it. Now, it's not going to turn around over a short timeframe, but it's a focus of ours with continued effort to make sure we drive the best seasonality possible on our cash flows which then only benefits our capital allocation strategy of returning practically all available free cash flow to our shareholders.

And on your second question, yeah, we did benefit in the year from tax deferrals around the globe. But as we manage cash, we don't think about individual headwinds or tailwinds. And 2021, you're right, we are going to have a tailwind as some of that unwinds. But what we're focused on is delivering on our commitment to our investor community which is 75% attributable, unleveraged conversion of EBITDA. That's what our target is for 2021 and we will get to that target just like we have for the last six years; continued focus on being highly cash generative.

Steven Fisher  
**Analyst, UBS Securities LLC**

Okay. Fair enough. And then couple clarifications. Just maybe a little bit more detail on the cadence of the prior revenue guidance. Do you think that compared to say the 6% decline we saw in the Americas in the fourth quarter, should we be expecting to see a double-digit decline there before it starts to then have a potentially double-digit growth in the second half, right? How tough will that revenue line be? And then, can you just give us a quick update on some of the remaining sales of non-core assets? Thanks.
Sure, Steve. So first of all, to set expectations for this coming year is, we see the second half of the year certainly being better than the first half of the year. However, we don't see the first half of the year being anything but flat. And I guess the easiest example of that is, when I look at our October performance, our first month of the year, we did see revenue in the month of October being flat with the prior year.

So again, that sort of sets the expectations about seasonality. And then with respect to our sales, again we've been able to accomplish a part of that agenda. We are focused on the exit and the sale of the other at-risk businesses. And those processes are well underway, is the best way I can describe it.

Steven Fisher
Analyst, UBS Securities LLC

Okay. Thanks, Troy.

W. Troy Rudd
Chief Executive Officer, AECOM

Thank you, Steve.

Operator: [Operator Instructions] Your next question comes from Adam Thalhimer with Thompson Davis. Your line is open.

Adam Robert Thalhimer
Analyst, Thompson Davis & Co., Inc.

Hi all. Hey, Troy, you said that you had seen some slow client decision making, but I think you indicated that starting to thaw. Is that correct?

W. Troy Rudd
Chief Executive Officer, AECOM

When I refer to slow client decision making, really I think about that as sort of the uncertainty around their funding. It's not that their decisions are slow. I think they're just forced by having to think about the funding constraints that they have as to which projects they prioritize. And yes, based on what we had seen in the pipeline at the end of the third quarter, we've seen again a small improvement as we go through our fourth quarter. So, it's gotten a little bit better. But again, that's not our – again, our focus is looking at the opportunities to improve market share within those customers.

Adam Robert Thalhimer
Analyst, Thompson Davis & Co., Inc.

Got it. And then I've been playing with your fiscal 2021 guidance all morning. I have an easier time being at the kind of low-end to the mid-range. I'm just curious to get to the high-end of the guidance, I mean what would have to go right?
Again, I think within our guidance range, it's fairly narrow in an environment that we're in for this fiscal 2021 year. So, I don't think it's a matter of something in particular going right. But as I said, we have some more optimism here in the US in the second half of the year just around the outcomes driven by the federal election. So again, I don't think it's one thing going right. It's just maybe a little bit better outcome in terms of some of those decisions that will be driven here in the US by our government.

Adam Robert Thalhimer  
Analyst, Thompson Davis & Co., Inc.

Makes sense. Thanks, Troy.

W. Troy Rudd  
Chief Executive Officer, AECOM

Thank you.

Operator: There are no further questions at this time. I'll turn the call back over to Troy Rudd for closing remarks.

W. Troy Rudd  
Chief Executive Officer, AECOM

Thank you. And again, I'd like to just end this call by again thanking our teams, professionals for their contributions in what was a very successful year at AECOM. It was by no means a normal year, but it was a successful year. And I think we're in a great position as we move forward. We have transformed the business. We are now a higher margin, lower risk Professional Services business.

We've built a track record that we can deliver on what we said we're going to do by having our industry-leading margins, great cash flow generation, great backlog heading into this next year, and frankly a phenomenal group of professionals that we can rely on and that's been proven out over this course of this last year.

So again, thank you for your time today and your interest. And we'll speak to you in the next few months. Thank you.

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