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ACM - Q3 2018 AECOM Earnings Call

EVENT DATE/TIME: AUGUST 07, 2018 / 4:00PM GMT

OVERVIEW:

ACM reported 3Q18 revenue of $5.1b. Expects 2018 adjusted EPS to be $2.50-2.90.

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PRESENTATION

Operator

Good morning, and welcome to the AECOM Third Quarter 2018 Earnings Conference Call. I would like to inform all participants this call is being recorded at the request of AECOM. This broadcast is the copyrighted property of AECOM. Any rebroadcast of this information in whole or in 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)

(technical difficulty)

Will Gabrielski, Vice President, Investor Relations.

Will Gabrielski - *AECOM - VP of IR*

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 take no obligation to update our forward-looking statements.

We are using non-GAAP financial measures in our presentation. The appropriate GAAP financial reconciliations are incorporated into our presentation, which is posted on our website. Please note that all percentages refer to year-over-year progress, except as noted. Our discussion of earnings results and guidance is adjusted for noncore business and asset dispositions, loss on disposals and on assets held for sale, acquisition and integration-related items, financing charges in interest expense, amortization of intangible assets, deferred taxes, and tax effects and discrete tax items associated with the U.S. tax reform, unless otherwise noted. Today's discussion of organic growth is on a year-over-year and constant-currency basis.

Beginning today's presentation is Mike Burke, AECOM's Chairman and Chief Executive Officer. Mike?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Thank you, Will. Welcome, everyone. Joining me today are Troy Rudd, our Chief Financial Officer; and Randy Wotring, our Chief Operating Officer. I will begin with an overview of AECOM's results and discuss the trends across our business. Then, Troy will review our financial performance and outlook in greater detail, before turning the call over for a question-and-answer session.

Please turn to Slide 3. Our third quarter results included several strategic and financial accomplishments. We delivered new highs for revenue, backlog and wins, which clearly demonstrate the successful execution of our strategy and momentum across our markets. Total revenue increased by 13% to $5.1 billion, and organic revenue increased by 10%. This marks the seventh consecutive quarter of organic growth, and we continue to experience a favorable mix shift to our higher-margin DCS and MS segments.

Excluding the AECOM Capital gain from the year-ago period, adjusted EBITDA increased by 15%. In fact, both revenue and adjusted EBITDA growth are outperforming the targets we set in our 5-year financial plan. Wins were $9.4 billion, a new high for the company, and have now exceeded $6 billion for 3 consecutive quarters. Our year-to-date wins of $22 billion is a 22% increase from the year-ago period. Our backlog increased by 16%, reaching a record-high of $54 billion. Importantly, the composition of our backlog is strong, with an increasing share of larger projects that carry a longer duration.

We are off to a strong start in the fourth quarter, with several sizable wins across the business, and we expect our backlog to be even higher at year-end. As a result of these accomplishments and our backlog momentum already in the fourth quarter, we are pleased to announce that we intend to enter into a $150 million accelerated share repurchase agreement, which will take effect when our trading window opens on Thursday. This marks the first tranche of our repurchases under our $1 billion authorization. We are confident in our financial outlook and believe that repurchasing stock at current levels puts us on a great path to maximize shareholder value.

Please turn to Slide 4 for a discussion of our business trends. Beginning in Management Services. Wins totaled $6.7 billion and backlog reached a new high of nearly $20 billion, which is an increase of 124% since the start of fiscal 2017. This growth represents a transformation of the business, including substantial wins for our U.S. Departments of Defense and Energy clients. Our win rate remains strong and includes a growing presence in the classified sector, where the barriers to entry are higher, and contract durations are longer.

Looking ahead, our MS pipeline remains robust, with an approximately $30 billion pipeline of pursuits, including more than $10 billion of bids under client evaluation. Our clients are in a strong funding position. The 2-year defense budget that passed in February included a double-digit increase in overall spending, and House and Senate fiscal 2019 appropriation bills have cleared their respective committees. As a result, we expect elevated levels of activity to persist.

Turning to the DCS segment. Revenue increased by 12% and backlog increased by 9%. This is the eighth consecutive quarter of backlog growth, led by continued momentum in our largest market, the Americas. We are benefiting from the more than $200 billion of state and local level infrastructure ballot measures that passed in 2016, full funding of the FAST Act, and strong activity in Canada.

In addition, our agility and breadth of our capabilities is an advantage. This is apparent in our quick mobilization to support the storm recovery efforts in the southeastern U.S. and Caribbean. Our wins to date are approaching $1 billion, and we expect key decisions on large opportunities in the coming months.

Turning to international markets. In the Asia-Pacific region, strength in Australia and Greater China contributed to solid growth. Following the close of the quarter, we won a substantial contract as part of Melbourne's metro tunnel project in Australia, which provides visibility into next year. Overall economic population and urbanization trends as well as our broad capabilities and backlog growth position us well for continued growth going forward.

In EMIA, prospects are improving in the Middle East. High-energy prices are leading to increased long-term planning for large investments, such as the proposed $500 billion NEOM development in Saudi Arabia. Across the region, clients are focused on modernizing infrastructure to attract capital in support of more diverse economic future. This is providing a positive offset to trends in the U.K. where opportunities remain, but the pace of our activity has slowed.

Pivoting to Construction Services. In our Building Construction business, we expect to deliver double-digit growth for the fourth consecutive year. We are executing well on our portfolio of iconic vertical and stadia construction projects, and our outlook remains bright. Today we have nearly $13 billion backlog, which is more than 2 years of annual revenue. Our pipeline of pursuits remains robust and continues to reflect our growing geographic and end market diversification. We have already had a number of successes in the fourth quarter, including another more than $1 billion construction project in New York. And we are pursuing several large projects that we expect to add to our visibility.

Our civil construction and power business continued to perform to our expectations. The Alliant gas power plant remains on schedule and budget and is now nearly 70% complete. We expect to finish construction on this project in 2019. In our civil business, the integration of Shimmick acquisition is progressing much better than planned, with a strong pipeline in our core California market, including a more than $23 billion pipeline of integrated opportunities.

Turning to AECOM Capital. To date, our investments have resulted in nearly $3 billion of construction value to be performed by AECOM. AECOM Capital has enabled us to very deliberately expand our construction business in several U.S. cities and enhanced our overall value proposition to key partners and clients. We are progressing on our path to raise third-party capital for a new fund, which will expand the investment capacity of AECOM Capital. We'll provide more details upon closing the fund.

Across our business, markets are healthy, and we are winning work at a very strong rate. Given that backdrop, we are executing a number of strategic actions this year to hone our focus and improve profitability. This includes our previously announced plan to sell and exit certain noncore oil and gas businesses and our decision to no longer pursue fixed-price combined cycle power plant construction.

We are also expanding on our use of global design and shared service centers. Today, the share of our work being delivered from lower cost and specialized offices is sub-scale. We have a substantial opportunity to deliver an increased share of our work from these centers over time and drive improved efficiency and quality for our clients. These decisions de-risk our portfolio and position us to best capitalize on the substantial opportunities apparent across our business.

I will now turn the call over to Troy, who will do will discuss the quarter in more detail.

W. Troy Rudd - *AECOM - Executive VP & CFO*

Thanks, Mike. Please turn to Slide 6. We are pleased with our strong performance across nearly all metrics. Our 10% organic growth included positive contributions from all 3 segments. Our growth continues to shift to our higher-margin DCS and MS segments. These 2 segments accounted for the majority of our growth again this quarter.

Based on the mix shift in our backlog, we expect this trend to positively impact margins over time. As Mike noted, we had $9.4 billion of wins and finished the quarter with a record $54 billion backlog. Today our backlog provides nearly 3 years of revenue visibility, which is a multiyear high and indicative of the momentum we see in the business and confidence in achieving our growth targets.

Adjusted EBITDA and EPS of $223 million and $0.62 respectively were ahead of our expectations for a sequential improvement. In addition, excluding a large AECOM Capital gain from last year, our adjusted EBITDA increased by 15%.

Free cash flow was $48 million. Our cash flow was positive for the 23rd time in 25 quarters. However, this was below our normal third quarter performance. There were a few items that impacted this result. First, we continued to make investments in growth. We grew by double digits in the quarter, but this growth required a working capital investment to accelerate and deliver storm recovery work. While we expect this work to remain at high levels, billings have increased, and we expect cash flow to improve in the fourth quarter and into 2019.

Second, through the course of selling noncore parts of the oil and gas business, there was some distraction in the business that led to a few larger collections shifting into the fourth quarter and possibly 2019.

Finally, AECOM Capital realizations are expected to benefit our cash flow in the fourth quarter this year versus the third quarter last year. While we still expect free cash flow to meet or exceed $600 million for a fourth straight year, because of these impacts, we expect to be closer to the low end of our $600 million to $800 million guidance. However, I want to emphasize that we have not experienced a fundamental shift in the cash-generative nature of our business.

Please turn to Slide 7. Revenue in the DCS segment increased by 12%. The Americas grew by 17%, which is the highest growth rate in several years. We saw an uptick in storm recovery work in the quarter, where we are proud of our quick mobilization to support our clients. We expect growth to continue, both from the fundamental strength driving our markets, and from storm recovery work. The adjusted operating margin was 6.1%, which is a 50 basis point improvement from last year and consistent with our expectations for margins to exceed 6% for the year. Our strong performance in the Americas has more than offset lower levels of activity in the U.K.

Please turn to Slide 8. Revenue in the MS segment increased by 9%. Our strong backlog growth is a key contributor to this performance. In addition, we continued to benefit from additional levels of activity on existing contract vehicles as well as higher levels of funding across our client base.

The adjusted operating margin was 8.1%, which is consistent with our expectation for higher margins in the second half of the year. We continued to deliver solid performance across our portfolio of projects.

Our backlog increased by 52% from the prior year and 124% from the start of fiscal 2017. Through this growth, we've added certain larger wins with longer-than-typical duration. As a result, we currently expect next year's revenue to approximate 20% of our current backlog.

Please turn to Slide 9. Revenue in the CS segment increased by 8%. The Building Construction business delivered double-digit growth in the quarter. We made progress on the noncore oil and gas dispositions we announced last quarter. We closed on one sale, and we are working diligently to complete the second over the next several months. The adjusted operating margin was 1.6%. Our year-to-date margin of 1.8% has us on track with our full year expectation of 2%.

Please turn to Slide 10. As Mike noted, we are pleased to move forward with a planned $150 million accelerated share repurchase program. This announcement reflects the increased confidence we have in our balance sheet, in our growing backlog, and achieving our 5-year financial targets.

Since last September when we announced our capital allocation priorities, we have generated strong cash flow; our backlog has reached record highs; our revenue, adjusted EBITDA and adjusted EPS are on a positive trajectory; and our core markets have strengthened. Our stock performance over the same period has not reflected this momentum. We still view achieving our 2.5x net leverage target as a priority. However, the current disconnect between our stock price and underlying business fundamentals creates an opportunity to redirect cash to repurchases.

Upon completion of the planned ASR, we will continue to evaluate all options for capital deployment. If our stock is at an attractive price, we will deploy additional cash to repurchases, while continuing to reduce our leverage through debt reduction and through EBITDA growth.

Please turn to Slide 11. Based on our year-to-date performance, we are reiterating our full year adjusted EPS and adjusted EBITDA guidance of $2.50 to $2.90 and $880 million, respectively. We continued to expect $0.08 of earnings from AECOM Capital at the midpoint of our adjusted EPS guidance, though the timing of planned transactions could result in a better outcome.

With that, I will turn the call over for Q&A. Operator, we're now ready for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Operator, we see there's someone in the queue there. Can you open it up?

Operator

We have Tahira Afzal from KeyBanc Capital Markets.

Tahira Afzal - *KeyBanc Capital Markets Inc., Research Division - MD, Associate Director of Equity Research, and Equity Research Analyst*

So I guess my first question is, we're obviously seeing very high revenue, organic revenue growth, maybe stronger than you guys had expected maybe a year or 2 ago, when you set that $3.5 billion free cash flow target. I know you've got some moving parts with storm restoration, collections and what have you, that are impacting the very near-term profile of free cash flow. But can you talk about what your free cash flow could look like if you continue to really exceed and drive double-digit kind of organic growth?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

So Tahira, we set out our 5-year target quite some time ago. And that 5-year target was to have a 5% compound growth at the revenue line, 7% at the EBITDA line and 12% to 15% at the EPS line. We also projected a $3.5 billion of free cash flow over that 5-year period of time. And clearly, we are ahead of schedule on all of those metrics. The cash flow, as you point out, was a little lighter this quarter for good reasons. We had outsized growth, and we invested in working capital to fund that growth. So, we still feel very good about our ability to exceed $600 million of free cash flow this year. We feel very good about our ability to exceed the $3.5 billion of free cash flow over the 5-year period of time.

Tahira Afzal - *KeyBanc Capital Markets Inc., Research Division - MD, Associate Director of Equity Research, and Equity Research Analyst*

Got it. That's helpful, Mike. And then, I just wanted to get an idea of the operating margins on the segment side. Earlier on, you had provided some segment margin guidance around DCS, Construction Services in particular. Does that still hold? Or has the third quarter changed any of that outlook for this year?

W. Troy Rudd - *AECOM - Executive VP & CFO*

Tahira, it's Troy. Simple answer is our outlook that we guided at the beginning of the year is unchanged. We still expect Construction Services to be around the 2% guide. And that's even taking into account the decision that we made in the second quarter to de-risk the business, exiting the combined cycle construction work and spending some costs to reposition that business. And then for DCS, we still expect that business to exceed the 6% target that we have for the year, and that's including some of the restructuring costs that we took in the first quarter. So overall, we are right on track with where we would expect it to be, and exceeding the results, certainly, in DCS.

Operator

The next question comes from Michael Dudas from Vertical Research.

Michael Stephan Dudas - *Vertical Research Partners, LLC - Partner*

Mike or Randy, backlog growth, the numbers are the numbers are pretty -- quite strong pretty much across the board. How is that translating into like the margin that you're booking in your divisions, relative to what you've been working off the last 12 to 18 months? And given that, is there a sense of being a little bit more choosy or focused on projects or bids? Or how you submit relative to your recurring requirements or cash requirements, given that you're -- you look to be from a position of strength, given such strong growth in the backlog growth trends?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

So a great question. First of all, the backlog obviously up 16%, but one thing to note is it is a favorable mix shift. And so the margins within the different segments themselves are somewhat consistent, but the backlog is growing faster in both the MS and the DCS segment than the CS segment. So what that means is that when you take the backlog overall, the margins inherent in that backlog are up, primarily due to the mix shift. And then, the second part of your question was around the investment of cash in working capital, right?

Michael Stephan Dudas - *Vertical Research Partners, LLC - Partner*

Just looking -- also, just following up, you have this backlog strength, looking at new awards, new bidding, how you're positioning yourself, roughly, on a risk-scale from a better cash or better margin, given that you should be dealing with a position of strength in many of your end markets.

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Yes. So clearly, the mix shift is going to help margins going forward. So the wins are coming in those markets. From a cash flow perspective, we're investing in things like the storm recovery work. We have -- we've won $1 billion of projects in that space for the hurricane recovery in Puerto Rico and the Southeastern United States. That market is growing fast, but the cash flow is a little slow. But it's coming from a AAA quality credit U.S. government customer, so we feel pretty good about the cash flow from that space. And we think investing in working capital for high-margin, high-growth areas is good. With respect to fixed-price, we have approximately 5% of our revenue today is in fixed-price risk. We de-risked the portfolio by stopping the pursuit of new business in the combined cycle gas business. So overall, our portfolio has de-risked over a period of time, and we feel really good about that 5% fixed-price risk in our portfolio.

Michael Stephan Dudas - *Vertical Research Partners, LLC - Partner*

And not to look too far ahead into 2019, but that mix shift in backlog, will we see elements of that showing up in business flows for 2019? Or because of the longer lead times and longer duration of projects, it will take a little bit longer to see that run through to the margin line?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Yes. We're not prepared to give guidance on '19 yet. We'll do that along with our fourth quarter results in November. But I'm very comfortable affirming the confidence in the business trends we're seeing. And obviously with backlog up 16% year-over-year, $9 billion of wins in the third quarter, our year-to-date wins are up 22% over the prior year. Margins are progressing along on the right track. The wins in the first part of this -- the first month of this first quarter, we had $1 billion-plus construction win in New York last week. We've had 3 very significant aviation wins in the first month of the year here. And so, we're expecting another good quarter with book to burn in excess of 1 that will cause our backlog to increase again in Q4. So everything seems to be moving in the right direction for us. The mix shift should drive margins, and we're expecting a pretty good 2019.

Operator

The next question comes from Andrew Kaplowitz from Citi.

Andrew Alec Kaplowitz - *Citigroup Inc, Research Division - MD and U.S. Industrial Sector Head*

Troy, I wanted to follow up on what you said about MS backlog conversion. I think you said 20% of the backlog will convert in '19. So, suggests mid-single-digit organic growth, and despite the backlog growth that we're seeing. Obviously, there's these long-lead projects, which you signed, I just want to clarify that. And then, Mike, maybe just stepping back, you definitely talk about the transformation of the business, and we see it in the backlog growth. But when do you think -- and really, actually, in the revenue growth recently. But when do you think that translates into earnings and cash? Obviously, you've been in a range in cash. You're a little bit lower this year. Do you get the cash back next year? And I know you don't want to talk about '19, but why shouldn't we be comfortable with double-digit EPS growth in '19?

W. Troy Rudd - *AECOM - Executive VP & CFO*

So Andy, just to answer your question on MS. Just given the phenomenal success we've had in winning work in the Management Services business, we thought it was important to give you a guide for '19. Just because of the large wins and the duration of that work, we did want to make sure you had the right visibility on organic growth in that business. And just in terms of your question on cash, there is nothing fundamentally changed in our business. As I said this in the prepared comments, is to how we convert earnings to cash. And as Mike said, in our 5-year plan, we had expected 5 -- sorry, 5% organic growth. And so, we are ahead of that now. We have more confidence in that, but I don't see that impacting our 3-year -- or sorry, our 5-year free cash flow. The other thing that we're seeing is, we are seeing an improved mix more towards U.S.-based and North American clients, which again, also, brings down the DSOs over the long term. And we'd see that improvement helping working capital over the 5 years.

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

So Andy, to the second part of that question, despite me saying I'm not going to give guidance for 2019 yet, I like the way you phrased the question of why wouldn't we see double-digit growth in earnings. So yes, listen, what we've said is, on a 5-year guidance, we are going to grow at 5% on the revenue line, 7% on the EBIT line and 12% to 15% on the EPS line. Now year-to-date, our revenue is up 8%. That is accelerating. We had over 10% organic constant currency growth in this quarter. Backlog is growing faster than we have expected. Wins are up 22%. So, everything is pointing in the right direction to exceed the numbers that we put out for our 5-year target. I don't want to get too specific on 2019 yet, but I take your point, things are looking better than expected. And every -- all the signs we're seeing now, and the momentum of the business leads us to believe that we're going to do better than our 5-year guidance numbers in '19.

Andrew Alec Kaplowitz - *Citigroup Inc, Research Division - MD and U.S. Industrial Sector Head*

And then, just to push you guys a little bit on DCS. I mean volume did accelerate. You mentioned the storm work. But why aren't you getting more margin leverage in the business? I mean this is the highest revenue in a quarter we've seen out of you guys this cycle. And we're still talking about 6.1% margin, still adjusted EBITDA. Why can't you do a little better? Is it because maybe the utilization is variable in the business? Maybe the U.K. is a little worse, all that kind of stuff? Or is there something else going on?

Randall A. Wotring - *AECOM - COO*

Yes. So Andy, I'll take that. This is Randy. Look, I think our EMIA business in the U.S. continues to do really well. I think the impacts we've seen have been a little bit of a drag around EMIA. As we've said with Brexit, there's been a significant amount of uncertainty in that business. We've seen a wind-down of our backlog in the Middle East, and that's turned around and started to build. But frankly, we are -- we're bullish on our DCS business and where it's at today, and we expect it to continue to improve as we move forward.

Andrew Alec Kaplowitz - *Citigroup Inc, Research Division - MD and U.S. Industrial Sector Head*

So Randy, if the Middle East gets better, then that will help margin. I mean, who knows what happened with Brexit. But that's one key variable that we have to look at.

Randall A. Wotring - *AECOM - COO*

Yes.

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Yes. I think that's right. I mean, we are investing in the Middle East. We're starting to see the signs of it turning around in places like Saudi Arabia right now with these new cities, $500 billion investing in NEOM. That's where we're spending a lot of our investment dollars right now. And I'll be on my way to Saudi in the next couple of months here, where we're starting to deploy a lot more resources. So, we feel good about that region right now.

Operator

The next question comes from Jamie Cook from Credit Suisse.

Jamie Lyn Cook - *Crédit Suisse AG, Research Division - MD, Sector Head of United States Capital Goods Research, and Analyst*

I guess, 2 questions, one, bigger picture, Mike. We've seen over the past sort of 12 months portfolio optimization be more of a theme for AECOM with the power business and the oil and gas business. You also talked in your prepared remarks, I think, about shared centers or moving to lower-cost areas. So, I'm just wondering, is this going to be a bigger focus in 2019, or a story that becomes bigger for AECOM as you start to look at where you're generating better returns in growth? And then, my second question just relates to the guide. If we take the midpoint of your EBITDA guide of $880 million, that implies the fourth quarter has to grow like 24% off of Q3 levels or 30-some-percent off of the first 9 months. So outside of AECOM Capital, which is a one-time positive, what's -- why is there such a significant earnings ramp in the fourth quarter? Is that because backlog's kicking in? Or there are a number of onetime things outside of AECOM Capital that's helping boosting the fourth quarter EBITDA?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Jamie, I'll answer the first part of that, and I'll let Troy answer the second part of it. But we continue to optimize our portfolio. We -- over the course of the past year, we moved to de-risk the portfolio, as you mentioned. We looked to concentrate our efforts in some of the markets where we thought we had bigger opportunities. So, you saw us restructure our operations in some countries in Eastern Europe, for instance, so that we could dedicate resources to some of the bigger opportunities. And I think what we're trying to do is get a little more focused. Right now, 75% of our business is coming from the United States, where we see the biggest growth opportunities in the world right now. So, we're going to start getting -- we're not going to start, we have started getting much more focused on the markets that we think are the biggest potential, rather than trying to be spread across 100 different countries, we have optimized our portfolio in terms of geographic focus as well as end market focus where we see the biggest opportunities. And it's starting to pay off. You saw us get very focused on the U.S. government Management Services business 2 years ago, where we talked about increasing, dramatically, our business development dollars in that space. And since the beginning of 2017, that backlog is up 120%. So, we saw that pay off. Our disaster recovery business is paying off as a focus there. And now we're getting much more focused on the aviation market. While -- that's -- 5% of AECOM's revenue today is in the aviation markets. We see that as a big opportunity for us. So, we're becoming much more agile in focusing on the markets that have the most growth and where we can have a concentrated and dominant position, as opposed to trying to be all things to all people in every market around the world.

Jamie Lyn Cook - *Crédit Suisse AG, Research Division - MD, Sector Head of United States Capital Goods Research, and Analyst*

But is most of the low-hanging fruit done?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

No. The world is constantly changing, Jamie. So, I think there's -- there will always be low-hanging fruit. It's just the fruit changes from season to season.

Jamie Lyn Cook - *Crédit Suisse AG, Research Division - MD, Sector Head of United States Capital Goods Research, and Analyst*

Okay. And then, on the guide for fourth quarter versus first 9 months and third quarter?

W. Troy Rudd - *AECOM - Executive VP & CFO*

Yes, Jamie. It's Troy. There certainly is a ramp. And I think the first thing is you have to think about the AECOM Capital transactions. In the fourth quarter, we anticipate those closing. And so, at the midpoint of our range, that means you take out about $0.08 of EPS, and that's approximately somewhere in the $25 million to $30 million range in terms of EBITDA. That implies that there is an 11% to 13% ramp from Q3 into Q4, which is consistent with the seasonality of our business. If you looked at the prior year, you would see a similar ramp from Q3 to Q4. And the strength of our conviction comes from, frankly, our backlog. We have been winning a lot of work, and we're seeing that translate into bottom line, top line and bottom line results. And that's driven off the strength of our Americas business and our Asia Pacific business, in particular, in the fourth quarter, in the DCS business. I mean, all businesses will be contributing to that, but that's where the strength is coming from.

Operator

The next question comes from Steven Fisher from UBS.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

On cash flow, just to what extent are there any disputed items in the quarter that might affect the cash flow going forward? I mean, you have to defend any of the receivables that you have, be it the government or Canada or otherwise?

W. Troy Rudd - *AECOM - Executive VP & CFO*

Steve, the simple answer is no. We have pointed out the storm work that we were doing. And I guess, maybe a simple way to think about that is there's a lot of hands that are billed and the information has to pass through to ultimately get those bills paid by U.S. government agency. And that just takes longer than we typically see in other parts of our business. So that's a simple explanation, but no, there's nothing that's in dispute or causing us concern.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

Okay. And then, maybe following up on Andy and Jamie's question about going forward here on the earnings, really just trying to assess the reasonableness of consensus for next year, based on some of the puts and takes we know about today. Because if I annualize, basically, the second half of your fiscal '18 at, say, a 55% seasonality, that would be about $2.65. And then, if you want to add back say something like $0.05 to $0.10 for the buyback you're announcing so far, what might be some of the other puts and takes or headwinds and tailwinds that we should be either putting in or taking out? I don't know if conceptually, the AECOM Capital in the fourth quarter, that's something we should just kind of continue. Or is there anything else to think about that may add or take away to next year?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Steven, again, I think it's too early to really start breaking apart and analyzing guidance for '19 before we've issued it. But I think the major things that we all ought to be focused on is the business is accelerating, right? We have -- year-to-date, we've got an 8% organic growth, 10% this quarter. Backlog is growing much faster than that. It has been now for some time. And so, we're just seeing the flywheel is just starting to spin up, and we have no reason to believe that that's going to change. The wins keep continuing this quarter. The momentum has continued in the first month of this quarter. The mix shift is driving towards higher-margin work. Everything just seems to be moving in the right direction for us. And so, I think there's -- all the standard components you can build into it, revenue growth exceeding our 5-year guidance. Our EBITDA growth is exceeding our 5-year guidance right now. Cash flow, I'm not concerned about at all. We invested really well in this past quarter in investing in growing the business, in working capital. And so, I think all of that portends quite well for 2019.

Steven Fisher - *UBS Investment Bank, Research Division - Executive Director and Senior Analyst*

Okay. Yes. I mean, clearly, your revenue growth and margin mix are going to be factors and contributors. I just didn't know if there was anything else that we should be aware of in the second half of this year that might not reoccur. But it sounds like I'll have to wait for that. All right, I'll pass it on.

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Yes. But the bottom line, Steven, is there's no onetime items in the fourth quarter that are unusual. AECOM Capital gains, we've talked about that before. We talked about the size of that gain. We've had that -- those kind of gains in the past. We had one last year. We have a big portfolio of projects, another 16 or so of projects that we've invested in that are in various stages of development. That will continue to provide upside in the future, and we still feel really good about that portfolio. Those projects keep progressing along. We're designing those projects. We're building the projects. We're leasing the projects up. And then, we're taking them to market at the right time. And so, we continue to do that. So, nothing unusual in the second half of this year that we ought to be backing out. And we don't see headwinds in front of us in any of our markets that are concerning.

Operator

(Operator Instructions) The next question comes from Anna Kaminskaya from Bank of America.

Anna Kaminskaya - *BofA Merrill Lynch, Research Division - VP*

Maybe just to go back again to the free cash flow question. Any visibility you can provide what your free cash flow has looked like through the first, I guess, half of the quarter in 4Q? Have you been collecting some of the outstanding receivables that makes you very comfortable with the outlook for the full year?

W. Troy Rudd - *AECOM - Executive VP & CFO*

Yes, Anna. I, again, we -- I think it's inherent in our guidance, again, our confidence around collections through the fourth quarter. And the simple answer to your question is some of the things that impacted the third quarter, we have collected during the fourth quarter. So again, we're just on a path to hit that guide.

Anna Kaminskaya - *BofA Merrill Lynch, Research Division - VP*

Okay. And then, on the buyback for 2019, typically, you have second half of the year more free cash flow-rich, I guess. So, does it mean that if you do restart your buyback program next year, do we have to wait until 3Q? Or kind of how do you plan on it kind of on the timing of the buyback program?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

So Anna, first of all as you know, we're going to execute Thursday morning the $150 million buyback, which is ahead of the schedule. We had originally planned to start that buyback in January. We're starting it a quarter early. We feel really good about buying our stock at this price. And well that -- that transaction will close out in the first quarter. We will be in the market buying in addition to that. At some point, we will likely enter into another accelerated stock repurchase program after that. I don't want to give specific guidance whether it happens at the end of Q1 or at the beginning of Q2 or thereabouts. But without question, at these prices, we fully intend to execute on the full $1 billion stock buyback. And we'll do that over the course of the coming quarters, as we realize our cash flow. And based on the growth of the business, if it continues to grow at this pace, which we expect, we're going to be a big buyer in our stock.

Anna Kaminskaya - *BofA Merrill Lynch, Research Division - VP*

Okay. And then, just to round up on AECOM Capital gain, is there any risk to that gain slipping into 2019? Kind of how good do you feel about the timing of that divestiture being done in the fourth quarter? And then, given your kind of portfolio of projects, how do you think about incremental gains in 2019? Do you have any, I guess, assets up for sale next year?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Yes. So, we have 2 transactions right now that we are expecting in this quarter in September. We have one transaction that we fully expect to close at the beginning of the -- of September, and then a second one where we have an asset with 2 offers on the table. We are just working out the legal details right now with an expectation of closing later in September. So as of right now, we expect those 2 transactions to happen in the month of September, and we'll keep pressing forward with those transactions. With regard to other assets, we have other assets that we could sell in 2019. We don't want to -- we're not ready to give specific guidance on that just yet. But suffice to say, we have a number of assets in that portfolio that are in various stages of development, that have built-in gains that we will realize sometime in the not-too-distant future.

Operator

The next question comes from Chad Dillard from Deutsche Bank.

Chad Dillard - *Deutsche Bank AG, Research Division - Research Associate*

So in DCS, I'm looking at your contract backlog growth in the quarter, which was nearly about 10%. Why shouldn't we model a similar growth rate for revenue in 2019? Is it the work that you're taking on longer duration? And then, also, I mean, how does the margin in DCS backlog compare to your realized margin and revenue, particularly given you're going to see a greater mix of storm work, which I would imagine is a little bit higher margin?

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

So let me just take the first part of that, and then I'll turn it to Randy or Troy to answer the second part. On what you're modeling for revenue in 2019, I just -- I'm not prepared to give revenue guidance for 2019 yet. But I understand your point. Everything is pointing towards exceeding our

5-year, 5% growth in revenue. Backlog continues at that pace. And so, I could see your point that all signs are heading in the right direction to exceed that number in '19. But I just don't want to give revenue guidance for '19 just yet. But on the margins?

W. Troy Rudd - *AECOM - Executive VP & CFO*

Yes. So, it's Troy. In terms of the margins that we see in that backlog, at this point in time, we see nothing that is unchanged from what we've seen in the past. The margins across the DCS business remain consistent with the last few years. And I'm referring to the gross margins. And then as the business grows, there clearly is some operating leverage that we gain from that. So, the EBITDA margins will improve over time as that business grows. So gross margins are the same, and there is certainly upside in the EBITDA margins as we continue along the path.

Chad Dillard - *Deutsche Bank AG, Research Division - Research Associate*

And then, secondly, can you quantify the working capital impacts from the storm restoration issue? And then, on your comments about the Middle East seeing a little more activity, could you just talk about how big that business is? And if you expect the strength to potentially offset some of the weakness that you're seeing in the U.K.?

W. Troy Rudd - *AECOM - Executive VP & CFO*

So Chad we -- in the quarter, we had about -- within our DCS business alone, we had about $140 million of call it, storm recovery work. And we collected very little of that during the quarter. So that will give you a sense of the impact.

Randall A. Wotring - *AECOM - COO*

Yes. And let me talk about Saudi Arabia, this is Randy. So, we see some of the biggest opportunities in the world surfacing there with the -- with 3 new cities that are going to be designed and built. We have early contracts there and are well positioned. We do believe that we'll see growth there next year that will help us as far as our overall EMIA activities.

Operator

At this moment, we show no further questions. I would like to turn the call over to Mr. Mike Burke for final remarks.

Michael S. Burke - *AECOM - Chairman of the Board & CEO*

Thank you, operator. So, I'd like to just emphasize a few of the highlights before we conclude the discussion today. First of all, the success of our strategy and the continuing momentum in our business has been apparent in all these results, with new records for revenue, backlog and wins.

Second, we're seeing this momentum continue into the fourth quarter with the sizable wins that I mentioned just a bit ago. That gives us further confidence in our backlog growth continuing to the fourth quarter and to the future.

Third is the mix shift within our backlog. And our revenue continues to shift to the higher-margin DCS and MS segments, which will benefit our margins over time.

And then, fourth, we remain very confident in generating at least $600 million of free cash flow for the fourth consecutive year, which includes our continued expectation for the AECOM Capital contributions in the fourth quarter and improved collections in the Americas from storm recovery work that Troy mentioned just a bit ago.

And then, finally, given all this confidence has caused us to bring forward the execution of our stock buyback program starting on Thursday, and our 5-year forecast to generate at least $3.5 billion of cumulative free cash flow, which represents approximately 65% of our current market cap, underscores the substantial capacity we have to continue these buybacks and drive long-term value for our investors.

So, with all of our successes in fiscal '18 and our commitment to capital allocation here, we're increasingly optimistic about the future in front of us, for the company, our employees and our shareholders. And I look forward to discussing the FY '19 outlook in much greater detail during our call in November, and then, in our Analyst Day in December.

So, thank you, everyone. Have a great day and enjoy the rest of your summer.

Operator

Thank you. Ladies and gentlemen, this concludes today's conference. We thank you for participating. You may now disconnect.