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AECOM (ACM)

Management Services Segment Divestment Update Call
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MANAGEMENT DISCUSSION SECTION

Operator: Good morning my name is Kristina, and I will be your conference operator today. At this time, I would like to welcome everyone to the conference call. I would also like to inform all participants that this broadcast is copyrighted property of AECOM, and rebroadcast of this information in whole or part without 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. All lines have been placed on mute to prevent a background noise. After the speakers remarks, there will be a question and answer session. [Operator Instructions]

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

William J. Gabrielski  
Vice President, 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 are using 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.

We will refer to pro forma adjusted EBITDA in our presentation. Pro forma adjusted EBITDA is comprised of the company's Design & Consulting Services, Construction Management, and AECOM Capital businesses, and assumes all stranded costs associated with planned separations and divestitures are eliminated. Reconciliations
of pro forma adjusted EBITDA for fiscal 2020 to the most directly comparable GAAP measure is not available without unreasonable effort, because the company cannot predict with sufficient certainty all of the components required to provide such a reconciliation at this time.

We believe pro forma adjusted EBITDA provides additional insight into the estimated impact of the proposed transaction and other strategic initiatives on the company's future financial performance. However, such estimates are forward-looking statements and are inherently uncertain. As such, you should not place undue reliance on such statements as actual results may differ materially.

Today's announcement relates to a transaction that has not yet been completed and includes potential risks and uncertainties such as the possibility that the transaction does not close or that closing may be delayed. Beginning today's presentation is Mike Burke, AECOM's Chairman and Chief Executive Officer. Mike?

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Thank you, Will. Joining me today are Randy Wotring, our Chief Operating Officer and Troy Rudd, our Chief Financial Officer.

I will begin with an overview of the strategic and financial benefits of today's announcement. I will also review our long-term strategy and fiscal 2020 financial guidance. Troy will provide additional financial details on today's announcement, before turning the call over for our question-and-answer session.

Please turn to slide 3. This morning we announced the definitive agreement to sell the Management Services business for a purchase price of $2.405 billion, which is 11.6 times expected fiscal 2019 adjusted EBITDA. This transaction reflects a premium valuation and is expected to generate substantial cash proceeds that we will use to reduce debt and to repurchase stock. Importantly, with the sale, we will unlock value sooner than anticipated under our prior plan to spin-off the business.

The successful separation of the MS business was amongst the largest opportunities to unlock value that we have been pursuing and adds to the successful strategic initiatives we have been executing over the past two years. These actions include de-risking and simplifying our operating structure, enhancing our margins to capitalize on strong growth trends, and deploying industry leading cash flow for debt reduction and stock repurchases.

The transaction marks the completion of a robust and thorough evaluation process that began with our June 17 separation announcement. As you may recall our decision to separate MS was motivated by our belief that the MS business is undervalued within AECOM. A significant buyer interest and the premium valuation announced today validate our view.

I also want to acknowledge the contributions of the MS team. Today's outcome is also a testament to the high caliber leadership and employees within the MS business and as the result of AECOM's commitment to enhancing value.

Please turn to slide 4. With today's announcement, we will generate substantial net proceeds that will accelerate debt reduction and enable us to more quickly seize upon the tremendous value creation opportunity, we expect to realize by allocating capital to share repurchases. Based on Friday's closing stock price, our industry leading professional service franchises trade at a significant discount to peers in the broader market.
In fact, including expected record fiscal fourth quarter cash flow and deal proceeds our stock is trading at approximately 8 times fiscal 2020 pro forma adjusted EBITDA guidance. This represents a substantial opportunity to enhance value through continued stock repurchases. As such, upon closing the MS sale, we intend to allocate capital towards debt reduction and then to share repurchases with the goal of maintaining a long-term net leverage target of between 2 times and 2.5 times and substantially reducing our share count over time.

Please turn to slide 5. We are committed to value creation. Over the past two years, we have taken a series of deliberate actions in close consultation with our board and strategic advisors to transform our portfolio into a higher returning, lower risk professional services company.

We are extracting ourselves from riskier geographies and businesses by executing on our plan to exit more than 30 countries, and we'll continue our review of how to best optimize our geographic footprint. In addition, we intend to exit nearly all at-risk self-perform construction businesses. We have substantially increased our margins through ongoing restructuring activities.

To this point, adjusted operating margins in the DCS segment have increased by a 100 basis points to the first three quarters of fiscal 2019 and we expect another at least a 100 basis point increase in fiscal 2020 as part of a plan to deliver a 200 basis point improvement from 2018 levels. And as today's announcement confirms, we have moved quickly to unlock value by announcing a sale at a premium valuation.

Importantly, we remain deeply engaged with our board and key advisors to identify additional opportunities to create value. Recently, we enhanced our engagement with Bain and are now evaluating areas for further margin upside, including expanded use of best cost shared service centers and global design centers.

In addition, we expect to eliminate all stranded costs related to this transaction to ensure no long-term earnings dilution. All of these initiatives provide a benefit to employees, our clients, and as a result, our stockholders. For AECOM, we are more profitable and competitive. Our employees benefit from more focused, streamlined organization that is better positioned to invest in advancing our capabilities and growth. Our clients benefit from more efficient project delivery while continuing to access our network of unparalleled expertise.

Please turn to slide 6. In addition to today's announcement, we also announced that we closed fiscal 2019 with significant momentum and strong performance across our business. We expect fiscal 2019 adjusted EBITDA and adjusted EPS to approximate the midpoint of our prior guidance ranges, including achieving our guidance for 12% adjusted EBITDA growth for the year. We also expect to deliver record free cash flow in the fourth quarter and to hit our full year free cash flow guidance.

Turning to fiscal 2020. Strong end market trends and the anticipated benefits from our value creation actions underscore our expectation for pro forma adjusted EBITDA growth of 17% at the midpoint of the range, including continued margin improvement. Troy will provide a more detailed financial review of today's transactions and 2020 financial guidance shortly.

In closing, the board and our management team have been on a very deliberate path to create value. And I'm energized by the progress we have made to transform the company into a higher returning and lower risk business. The expected proceeds from this transaction will strengthen our balance sheet and create increased flexibility to repurchase shares in an attractive valuation, which provides additional benefit to all stakeholders.

With that I will turn the call over to Troy.
W. Troy Rudd
Chief Financial Officer, AECOM

Thanks, Mike. Please turn to slide 8. Today's announcement marks a significant milestone. We are delivering on our commitments including a strong finish to fiscal 2019 and our expectation for 17% pro forma adjusted EBITDA growth in fiscal 2020.

The agreement to sell MS is a great achievement for the organization. And the transaction meets all the criteria and objectives that we set forth when we announced the MS separation in June. First, we are realizing a premium valuation that confirms our view that the MS business is undervalued within AECOM. Second, we expect the transaction will generate substantial cash proceeds that strengthen our financial profile and will enable share repurchases.

Third, it creates certainty for our stakeholders including an attractive valuation for our stockholders and certainty on the direction of the business for our employees. And finally, it furthers our focus on our higher returning and lower risk professional services business, allowing us to concentrate management time and investment dollars in areas that we believe will generate the strongest long term returns.

We expect net cash proceeds of approximately $2.35 billion. This is inclusive of approximately $150 million of contingent purchase price. The transaction is expected to close in the first half of fiscal 2020 and is subject to customary closing conditions. We expect to eliminate all stranded costs resulting from this transaction, which is consistent with our prior expectations.

Please turn to slide 9. We expect to report our fourth quarter and full year financial results on November 12. On a preliminary basis, as Mike noted, we expect our adjusted EBITDA and EPS for fiscal 2019 to approximate the mid-points of our prior guidance ranges. We expect to deliver record free cash flow in the fourth quarter and achieve our guidance for at least $600 million of free cash flow for the year. As a result, we expect to report substantially lower debt in the fourth quarter.

We’re also introducing financial guidance for fiscal 2020. For the entire company, we are guiding to adjusted EBITDA of $1.050 billion to $1.070 billion. This would mark 13% growth and a second consecutive year of double-digit growth. We’re also providing guidance on pro forma adjusted EBITDA which excludes the adjusted EBITDA associated with our Management Services business and our at-risk, self-perform construction activities, which includes our professional services, capabilities across the design, construction management and AECOM Capital businesses. On this basis, we are guiding to $720 million to $760 million for fiscal 2020, which would represent approximately 17% year-on-year growth at the mid-point.

The expected growth in our professional services business is higher than the enterprise growth in fiscal 2020. This is largely driven by continued margin expansion in the DCS segment. Resulting from the restructuring actions, we have already taken and we'll continue to take towards our goal of achieving industry-leading margins over time. Our forecast includes continued momentum in our DCS margins, consistent with our plan to deliver a greater than 8% adjusted operating margin in fiscal 2020.

This translates to approximately 11.5% on a net service revenue basis, which is consistent with peers. In order to provide investors with the best understanding of our underlying pro forma financial performance, stranded costs are excluded from our fiscal 2020 adjusted pro forma EBITDA guidance.
I want to spend a moment discussing cash flow. The company is positioned to build momentum in the fourth quarter and deliver another year of strong free cash flow in fiscal 2020. On a pro forma basis, which adjusts out Management Services and the at-risk self-perform construction businesses we plan to exit, we expect to convert adjusted EBITDA to unlevered free cash flow at a rate of between 75% and 80% on a normalized basis. This will create continued opportunities for capital deployment.

Please turn to slide 10. We will continue to prioritize debt reduction and share repurchases while maintaining a long-term net leverage target of 2 times to 2.5 times, which we believe is appropriate for our lower-risk professional services business. Furthermore, as Mike explained, the implied valuation discount in our professional services business creates a very compelling opportunity to repurchase shares in an attractive price.

With that, I will now turn the call over for a question-and-answer session. Operator?

**QUESTION AND ANSWER SECTION**

**Operator:** Thank you. [Operator Instructions] Your first question comes from the line of Andy Kaplowitz from Citi. Your line is open.

**Andy Li**

*Analyst, Citigroup Global Markets Asia Ltd.*

Hi, guys. It's Andy Li on behalf of Andy Kaplowitz. First of all, thanks, thanks for the presentation and the call. I just have three questions. So number one, can you talk about how this deal came about given it's only been roughly four months since our initial announcement. And was this like an option process? Just any color on that will be very helpful. Thank you.

**Michael S. Burke**

*Chairman & Chief Executive Officer, AECOM*

So, thank you. Let me – it's Mike, let me touch on that. When we announced the spin, we immediately had inbound interest. We had two banks involved to not only capture that inbound interest, but then also to solicit outbound interest to all of the right strategic buyers, as well as the right financial buyers. That led us through a process over the course of the last four months, which was a highly competitive process that had varying stages and varying gates.

We ended up in the past three or four weeks with three buyers that were competitively bidding against us, so we had the right competitive tension, all the way up until last Thursday night before we reached a final agreement with one of the parties. So it was a very robust competitive process with both strategic buyers and financial buyers.

Okay. Great. Thanks. And then number two, I guess, how should we think about the cash deployment, given with the after tax proceeds and roughly $600 million in free cash flow in 2019? I think our net cash position will be improved significantly, so can you talk about how you would deploy cash in terms of buybacks, M&As, and the timing or reducing leverage 2 times to 2.5 times in the long term?
Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Yeah. So a couple of things. Between the proceeds of a transaction and our fourth quarter free cash flow, just those two components alone will equate to a total cash proceeds equal to about 50% of our total market cap. So you’re spot-on, on the amount of cash coming into the organization.

As we said in our press release this morning, we expect to reduce our debt, as well as, execute on stock repurchases to maintain our long-term net debt leverage ratio between 2 times and 2.5 times. And you asked about acquisitions, we have no plans at all to entertain acquisitions.

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

Michael S. Dudas
Analyst, Vertical Research Partners LLC

Good early morning, gentlemen.

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Good morning, Michael.

W. Troy Rudd
Chief Financial Officer, AECOM

Hi, Mike.

Michael S. Dudas
Analyst, Vertical Research Partners LLC

So following – continuing on the leverage point, you’ve said 2 times and 2.5 times was your longer term, but is that an optimal? What’s the – I know it’s a lot of days, you’ve been working at it for years, but given the new structure of the company, given it’s in much better cash flow conversion and visibility especially amongst your public sector infrastructure client base globally. Can that range over time change and one – and from that standpoint? And then longer term, the targets that you set up through 2022 are those still kind of in the ballpark or will that – can we look to maybe think about being adjusting that relative to the new structure and the positioning of the company?

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

So, Troy, do you want to take that?

W. Troy Rudd
Chief Financial Officer, AECOM

Yes. I’ll take the – why don’t I take the cash piece, Mike? And then you take the longer term view. So, yeah, Mike, we’re not changing or moving away from what we’ve said it’s a long-term leverage guidance. So, for the time being and through the close of the transaction, that’s the guidance that we have. And of course as you just stated, over time, as the company evolves and transforms and becomes a professional services business, we certainly have the opportunity to re-evaluate it at that point in time.
Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*  

Yeah. So, just to follow on that point, first of all, based on the strong cash flow in Q4, our net debt leverage is already below 2.5 times, but we’re not moving away from that. And it will depend on how much stock we can buy back frankly. But we feel very comfortable at the 2.5 times leverage with the stable cash flows in the, what I'll call, the RemainCo business.

In terms of long-term cash flow, obviously, without the component of Management Services, you've got to adjust for that. But otherwise, the way to think about it is this business going forward would generally generate about 75% of EBIT into free cash flow. But we'll have on our Investor Day in December, we'll get into a lot more detail about that to ensure you've got the right numbers to model out.

Michael S. Dudas  
*Analyst, Vertical Research Partners LLC*  

Two quick follow-ups gentlemen. First maybe how do you think about timing relative to fourth quarter cash flow, deal closing? I'm assuming this is a first quarter target. I'm anticipating first quarter calendar. And the structure of how to de-lever and what kind of share repurchase program or thoughts from that standpoint, is something that as soon as practically possible or is this more of a timing issue as we move into fiscal year 2020?

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*  

Yeah. So on the timing of the transaction, a good guess would be 90 days to 100 days to close. We've got the Hart-Scott-Rodino and the EU Antitrust regulatory hurdles to get through. Those are very, very low hurdles for this type of a business. And our contract does have the so-called hell or high water provision, which would require the buyer to carve out any businesses in order to receive regulatory approval. But that’s probably a 90 day to 100 day process. So call it January timeframe, first calendar quarter.

And then, we would expect to, as soon as practical, engage in buybacks upon that close. We have looked at all of the various options. And while we haven't made a final determination, it does appear that a tendered offer would be the best way to go about that.

Michael S. Dudas  
*Analyst, Vertical Research Partners LLC*  

Makes sense. And final thought, relative to your 2020 pro forma guidance range on EBITDA, very healthy mid-point growth. You certainly highlighted margin. Other drivers in that? Are you seeing more visible, better momentum, better cross-selling, better opportunities that give you more confidence improving on the 2020 number, soon before for November on your Investor Day?

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*  

Yes. So a couple of things, when we build out our guidance, we start with what kind of momentum we have from FY 2019 going into 2018, how we’re feeling about the markets. But most importantly, we’re looking at the backlog that we have. And we had a pretty solid growth rate in our backlog in the remaining portion of the business in FY 2019. So the backlog helps us there.
There's a little bit of top line growth in there. But the real opportunities is the movement of our margins from 5.9% in FY 2018 to over 7% in FY 2019 to over 8% in FY 2020, so continued margin expansion. And on a net service revenue basis, we would expect approximately 11.5% margins in FY 2020. So it's a little bit of top line growth, it's a little bit of bottom line growth, and we still think we have more opportunity for margin growth as we continue to rightsize the business and become more efficient.

Michael S. Dudas  
Analyst, Vertical Research Partners LLC

Excellent, Mike and Troy. Thanks for your thoughts.

Michael S. Burke  
Chairman & Chief Executive Officer, AECOM

Thank you.

Operator: Your next question comes from Sean Eastman from KeyBanc Capital Markets. Your line is open.

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

Hi, gentlemen. Congratulations on the announcement this morning.

Michael S. Burke  
Chairman & Chief Executive Officer, AECOM

Thank you.

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

First one for me is just given we're seeing a kind of a stable business being divested here, cycle concern certainly front of mind for investors nowadays. Can you just talk to RemainCo and market mix whether you've seen any kind of signs of slowing on the commercial side? What portion of the business is maybe looking a little shakier over the next couple of years, talk about visibility on top line growth over the next couple of years. Just commenting on that subject would be super helpful.

Michael S. Burke  
Chairman & Chief Executive Officer, AECOM

Sure. So, first of all, the RemainCo business is a lower-risk professional services business. So the risk factor drops quite a bit. We still have a business that has, on a top line basis, a real healthy mix of diverse funding from private, state and local governments, US governments, non-US governments.

Although most people think of this Management Service business as a selling off of our federal government business, we will still have almost $1 billion of revenue in our DCS segment for the US government after the transaction. So, we still have some really solid exposure to that. We still have a good mix of geographic exposure. Now, while 70-plus percent is attributable to North America, US and Canada, we still have exposure in Asia-Pacific and EMEA.

So, I think we've got the right geographic mix, we've got the right funding source mix, both commercial, federal government, state and local government, and foreign governments. And we've got the right risk profile. So, all the
right mixes are there. But we are not seeing cycle downturns in the private sector. In fact, our growth in the private sector – our backlog growth this year. Will can probably remind me that the growth in the private sector – he’s giving me a blank stare, but we had pretty significant backlog growth in the private sector business this past year.

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

Okay. Thanks, Mike. And the next one for me is, any update on the self-perform construction sale, still on track for calendar year-end. Any kind of inbound interest on that asset?

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

It’s proceeding slowly, I’ll call it that. We still have a strong desire to completely exit from the at-risk, self-perform business. We have been in the market. We are in discussions with a party right now. But we’re not prepared to sell it at any price. So, it’s been a little slower than we had hoped. But it’s a tough market for those type of assets right now. But we still have a very committed intent to dispose of that business.

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

Okay. And just as we look that self-perform construction business, are there any projects within the mix there that are in a loss position? Any kind of execution overhang within that piece of the business as we stand today?

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

I don’t think there’s always projects some perform better than others. But all of them are properly reflected on our balance sheet today. And we’re continuing to execute that business in a profitable basis as a whole.

W. Troy Rudd
Chief Financial Officer, AECOM

And Mike if I may. Just adding – building on that point. When we look forward with that business as we’ve been bidding work as we’ve been going through the sales process, we’ve been careful in the type of work that we’re taking on. Though that we’re lowering the profile of the risk in those businesses as we move forward through the sales process. So, again as Mike said, the portfolio is appropriately valued on our balance sheet. And we’re making sure that we’re not going to take on risk even, as we operated through this process that we’re selling the businesses.

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

Thanks, appreciate the time.

Operator: Our next question comes from Jamie Cook from Credit Suisse. Your line is open.

Jamie L. Cook
Analyst, Credit Suisse Securities (USA) LLC

Hi, good morning and congratulations. Most of my questions have been answered, but Mike just to clarify Mike Dudas’ question, the additional opportunities that you’re talking about, the margin improvement opportunities, I’m assuming that’s above the 8% 2020 target. So, could you just provide some color on the cost to achieve that, and
how big the potential opportunity could be? I mean could this be – could AECOM look like – the RemainCo look like, I guess a double-digit margin business? I'm just trying to understand that. Thanks.

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*

Yeah, so first of all, Jamie, as I hinted at earlier, we will begin giving more net service revenue reporting. And so that 8% translates to 11.5% on a net service revenue basis. And I don't want to get too far out on long-term margin opportunities until we get to our Analyst Day in December. But there's a whole host of things that we're doing.

We have been working with Bain as you heard us mentioned in the past. We have expanded that relationship with Bain to look for a whole host of different opportunities and whether it's our global business services center or our global design centers, changing the labor pyramid profile of our organization, changing our ratio of subcontractor costs for other design firms. There's a whole host of things that we are working on.

And our expectation is that we will drive it above that 8% gross or 11.5% net service revenue margins in the outer years. And with respect to cost to achieve, so I can't give you a cost to achieve number on that until we get into a much more detailed discussion in the future. But generally speaking, our cost to achieve have been a fraction of the opportunities that have been presented. So when you think about the $235 million cost reduction initiative that we did in FY 2019, our cost to achieve the cash was $90 million. Troy, is that right?

W. Troy Rudd  
*Chief Financial Officer, AECOM*

Yeah.

About $90 million. So that gives you kind of a sense for the cost to achieve and the incredible payback opportunities there. So many of those issues that we're talking about that get us above the 11.5% net service margin are likely not to be as expensive, but that gives you just a rule of thumb and directional guidance.

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

Okay. Thank you. Congratulations.

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*

Thanks, Jamie.

Operator: [Operator Instructions] Your next question comes from Andrew Wittmann from Baird. Your line is open.

Andrew J. Wittmann  
*Analyst, Robert W. Baird & Co., Inc.*

Great. Thanks. I guess I'm just going to start with a couple of, I guess more technical questions here. But for Troy, I was just kind of curious on the $150 million of contingency payments. I was wondering what some of the key
hurdles that you have to deliver to receive that payment, maybe the period of time over, which that will be recognized and held back for just so we can understand how that incremental cash flow could work from here.

W. Troy Rudd  
Chief Financial Officer, AECOM

Yeah. So work backwards there, Andy. We expect that to come in the next six months. And it relates to projects where we have some amounts that we're collecting from clients. And again, we don't expect to collect this before close. So, in the arrangement, it's been included as a contingent sales proceeds, which will turn into dollars for us to sell proceeds over the course of next six months. I don't want to give too much detail on those because those are ongoing matters with clients.

Andrew J. Wittmann  
Analyst, Robert W. Baird & Co., Inc.

Yes. Okay. That makes sense. Kind of good sense on that one. I guess the other one would just be, the other cash cost associated with getting this deal for legal bankers, break fees, professional services, and things like that nature. I have to mention they're not immaterial here, so I was wondering, if you can help us get our arms around what that could be?

W. Troy Rudd  
Chief Financial Officer, AECOM

Yes, Andy, for purposes of I think of your modeling, I would use transaction costs between $40 million and $50 million. And in terms of tax cost, this is a very efficient tax transaction. And so I would use a number that's less than $20 million for the overall tax liability associated with the sale. And you...

Andrew J. Wittmann  
Analyst, Robert W. Baird & Co., Inc.

Got it. And then my final and last – I'm sorry.

Michael S. Burke  
Chairman & Chief Executive Officer, AECOM

I'm sorry. Let me just give clarity, you had a question about break fees...

Andrew J. Wittmann  
Analyst, Robert W. Baird & Co., Inc.

Bank break fees, debt termination fees is what I was referring to. It sounds like [indiscernible] (00:32:48) that Troy was mentioning that.

W. Troy Rudd  
Chief Financial Officer, AECOM

Yes. And that factors into our plans for debt pay down as a result of the transaction. We'll pay down our debt to a certain place, so that we will not have any make whole payments with respect to our 2024 or 2027 bonds.

Andrew J. Wittmann  
Analyst, Robert W. Baird & Co., Inc.

That's helpful. Okay.
W. Troy Rudd  
*Chief Financial Officer, AECOM*

Okay.

Andrew J. Wittmann  
*Analyst, Robert W. Baird & Co., Inc.*

Yes. And then just my final question here was, Troy, related to, I think you said that cash flow conversion of 75% to 80% if I'm not mistake that you said on a normalized basis? I guess just can you help bridge that a little bit better? What's the delta from the 100%. I mean, historically, you guys have always had stock compensation and some tax savings kind of helped improve you cash flow characteristics. I just wondering if you could just give a little bit more conversation, a little bit more color as to why 75% to 80% is the right level for a time going forward?

W. Troy Rudd  
*Chief Financial Officer, AECOM*

Yeah. So Andy you're right. There are a number of items that play into that, but effectively just to be clear, we're talking about unlevered cash flow and then put it on a normalized basis, because the cash flow can be lumpy from period-to-period. We would expect EBITDA to convert at that rate. And again moving forward, we expect to be paying cash taxes. So I think that would be something that's different from the past. But all of those factors you described are taken into that conversion rate.

Andrew J. Wittmann  
*Analyst, Robert W. Baird & Co., Inc.*

Okay. Yeah. I think what I was missing there was that this is an unlevered free cash flow as opposed to the cash flow conversion on net income. And that makes sense, I guess, given that your balance sheet leverage level is going to be fluctuating here during the transition period. So, okay.

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*

Yeah. Andy, just to be clear, the percentages that Troy, gave were a percentage of EBITDA, not of net income.

W. Troy Rudd  
*Chief Financial Officer, AECOM*


Andrew J. Wittmann  
*Analyst, Robert W. Baird & Co., Inc.*

Yes. Yes. No, got it. Thank you very much, guys.

Michael S. Burke  
*Chairman & Chief Executive Officer, AECOM*

Sure. Thank you.

Operator: Your next question comes from Michael Feniger from Bank of America Merrill Lynch. Your line is open.
Michael Feniger
Analyst, Bank of America Merrill Lynch

Yeah, guys. Thanks for taking my questions and congratulations. On the fourth quarter cash flow that you guys have visibility on and are confident, can you parse out a little bit more details around maybe the collection of the storm recovery, update on the refinery receivables? Anything around the fourth quarter cash flow that you guys hinted at generating and feel comfortable at?

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Yeah. So I guess first is a headline point that you recall, we have a large portfolio of projects, so tens of thousands of projects across the company. And so, the great result that we have on cash is a result of people across the entire company focusing on those individual projects and driving that result.

With respect to those two items you referred to on the storm recovery work, we collected very little during the fourth quarter, that did not really meaningfully contribute to that cash result. And with respect to the claim we have on the refinery ore project, that did not contribute as well.

Michael Feniger
Analyst, Bank of America Merrill Lynch

Good to know. And then with the assumption on the top line growth next year, can you just provide a little bit more color on how the backlog kind of looked in the fourth quarter? Was organic growth on the backlog similar to third quarter? I mean, I know you guys will be reporting fourth quarter with the date you provided. I'm just curious with all the uncertainty right now and the fact that what we're seeing with RemainCo going forward in the pro forma, so just any more color you can give either by geographical or customer base to provide some more comfort around that assumption for next year.

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Yeah. Michael, we will talk about that in much more detail on our earnings call. We haven't finished the final audit of our books and all the numbers just yet. So, before we get too far into backlog, we feel pretty good about the year overall. Backlog is solid, but we'll give much more precise data on that in just a few weeks.

Michael Feniger
Analyst, Bank of America Merrill Lynch

Okay. That's great. Just lastly, was there any thought of running with a lower leverage range, until – I'm just curious on the timeline maybe on getting to that range and how you looked at that and how you analyze that with, obviously, MS is now divested and with the RemainCo business with that 2 times to 2.5 times sticking there? Thank you, guys.

Michael S. Burke
Chairman & Chief Executive Officer, AECOM

Yeah. So obviously, we give a lot of thought to that and it's a function of where we think the intrinsic value is in our stock and interest rates. And today with the low interest rates and when you look at RemainCo that has significant discount to its peers on an EBITDA multiple basis, we think there's an incredible opportunity for us to buy as much of our stock back as we can.
And so we feel that we've got very stable cash flows in RemainCo going forward. So we're not overly concerned about the levels of debt. And so to us, it's an opportunity to take on a little higher debt and buy more of our stock back to capture that opportunity. So we think of that range we gave out, I would personally feel comfortable with the higher end of that range.

Michael Feniger  
*Analyst, Bank of America Merrill Lynch*

Thank you.

**Operator:** Our next question comes from Chad Dillard from Deutsche Bank. Your line is open.

Hey. This is Kevin on behalf of Chad. All questions were answered. Thanks, guys.

**Michael S. Burke**  
*Chairman & Chief Executive Officer, AECOM*

Okay. Great. Thanks, Kevin.

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

Thanks, Kevin.

**Operator:** There are no further questions at this time. We will now turn the call back over to Mike Burke for closing comments.

**Michael S. Burke**  
*Chairman & Chief Executive Officer, AECOM*

Thank you, operator. So we, as I said earlier, we're very pleased with the premium valuation we were able to attract for this high quality business that we sold or we announced the sale today. And as I mentioned earlier, the proceeds from that transaction and the free cash flow from the fourth quarter amount to approximately 50% of our total market cap. So, we have a strong intention to reduce our debt to the ratios that I mentioned and use the excess cash to repurchase our stock.

And after we've completed these strategic actions, the sale of MS, and ultimately the divestiture of our self-perform, at-risk business, we will have significantly de-risked our business portfolio. We'll have significantly increased margins and we'll have a RemainCo business that has a lower risk, higher returning profile.

And we're also delighted with our results for FY 2019 and our FY 2020 guidance with a significant double-digit EBITDA improvement once again, and significant improvement in our margins once again. So, we're feeling pretty good about the direction of this business and we look forward to giving you much more detail on our earnings call in November. And then even further information during our Analyst Day in December.

So, thank you for participating today and we look forward to talking to you in a few weeks.
Operator: This concludes today's conference call. You may now disconnect.