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ACM - Q1 2018 AECOM Earnings Call

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OVERVIEW:

Co. reported 1Q18 adjusted EPS of $0.57. Expects FY18 adjusted EPS to be $2.50-2.90.

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PRESENTATION

Operator

Good morning, and welcome to the AECOM First 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 part without the prior written permission of AECOM is prohibited.

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I would like to turn the call over to 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 growth 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 excludes the impact of acquisition and integration-related expenses, one-time financing charges, the amortization of intangible assets, financial impacts associated with non-core businesses and assets, and discrete tax items associated with U.S. tax reform, unless otherwise noted. Today's discussion of organic growth is on a year-over-year and constant-currency basis.

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

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. We delivered strong first quarter results, building on our record backlog position entering the year, the growing momentum across our end markets, and continued solid project execution. Organic revenue increased by 8%, marking the fifth consecutive quarter of positive growth. Our performance was highlighted by 10% growth in our higher-margin management services segment, where our backlog has increased by more than 50% since the start of the fiscal 2017 year. In our Americas Design business, we grew 3%, driven by our public sector-focused transportation and water markets, where our clients are benefiting from increased funding levels.

In our Building Construction business, we grew 22% and are on pace to achieve a fourth consecutive year of double-digit growth, reflecting strength in our core New York market and our successful expansion into new markets. Our EBITDA and EPS performance met our expectations, and we generated positive cash flow consistent with normal seasonality.

Across the business, we expect this strong performance to continue. We delivered $6.1 billion of wins in the first quarter, marking the third time in our history that we have had quarterly wins of at least $6 billion. As a result, our backlog increased by 11% to a new all-time high of $49 billion. Wins were highlighted by a 1.5 book-to-burn ratio in our MS segment and strong contributions from our DCS and CS segments. With these accomplishments, we are on track with our outlook for the full year.

Before turning to our view of the business, I'd like to spend a moment highlighting the expected benefits from U.S. tax reform. Overall, we anticipate the new U.S. tax law will be a catalyst for our business. Specifically, our clients will benefit from a lower tax rate, repatriation and immediate expensing of capital investments. Several companies have already announced plans for increased domestic investment, including the automobile manufacturing and high-tech sectors, markets where our capabilities position us to benefit.

For AECOM and our stockholders, the timing of tax reform couldn't be better. We have expanded our capabilities, invested in business development, and are executing on our strategy. Today, we are positioned to benefit from a period of synchronized global growth, increasing public support for infrastructure investment, favorable market conditions and strong corporate balance sheets.

Accordingly, our confidence is high in achieving our 5-year financial targets for a 5% organic revenue CAGR, a 7% adjusted EBITDA CAGR, a 12% to 15% adjusted EPS CAGR and at least $3.5 billion of cumulative free cash flow. This plan supports our capital allocation policy, which includes achieving 2.5x net leverage by the end of this fiscal year, at which point we expect to execute share repurchases under our $1 billion authorization. Through this policy, we are committed to driving industry-leading stockholder value.

Please turn to Slide 4 for a discussion of our business and market trends. Beginning with the DCS segment in the Americas, organic revenue growth accelerated in the first quarter and backlog increased by 12%. Our transportation and water business, which accounted for over half of our revenue in the Americas, are reflecting a better public funding environment. A number of factors support our view of a sustained up-cycle and infrastructure investment.

First, funding is improving. The $200 billion of ballot measures approved by voters in Los Angeles, Seattle, San Francisco and Atlanta during the 2016 election are leading to improved levels of activity. Additionally, we are benefiting from the $305 billion FAST Act, the $54 billion Road Repair and Accountability Act in California and several state-level initiatives to raise gas taxes or enable P3 delivery. And the creation of an over $30 billion infrastructure bank in Canada is a positive development for that market.

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Second, ongoing hurricane and recovery efforts in the U.S. are fueling a substantial long-term pipeline. In this market, our scale and ability to quickly mobilize a broad array of services has resulted in several hundred million dollars of wins and a multibillion-dollar long-term rebuilding and resilience pipeline.

Finally, while many of our markets already have momentum, there is substantial opportunity for further improvement. Federal infrastructure spending as a share of total federal spending is only half of the levels experienced in the 1960s. State and local spending on infrastructure is at a multi-decade low, and the federal gas tax, a key funding source, has held constant since 1993, despite fuel efficiency and general inflation. And only 5 of the top 50 airports in the world are in the U.S., supporting a 5-year, $100 billion estimated investment in U.S. aviation markets.

In his State of Union address, the President highlighted this opportunity with his commitment to a $1.5 trillion plan and focus on driving further regulatory efficiencies. There is still much work to do to achieve a transformative bipartisan infrastructure plan, but these signs inspire confidence.

Turning to our design markets into Europe, Middle East and Africa. In the U.K., our largest market in the region, key transformational rail projects continued to progress through execution and proposals, such as the more than $40 billion plan for Highways England to build new expressways are creating a great deal of opportunity. In India, we continue to grow at a rapid rate. India is projected to be the fastest-growing economy in the world in each of the next 2 years, and we have positioned ourselves to benefit through our substantially increased presence in this market.

In the Asia-Pacific region, we continued to deliver strong performance. The Hong Kong market remained stable, with solid execution on our existing portfolio of projects and good backlog visibility. Our leading civil design capabilities in this market are a key differentiator in pursuits across the region. This is especially true in Southeast Asia, where our work on large transit projects contributed to another quarter of double-digit revenue growth. In Australia, improving economic conditions, declining employment, and increasing infrastructure budgets, resulted in another solid quarter, building on the momentum that began 1 year ago.

Let's pivot to the Management Services segment. Our focus on business development resulted in wins of $1.4 billion. And our backlog has increased by more than 50% since the beginning of fiscal 2017. As a result, revenue growth accelerated to 10% in the first quarter. Our pipeline remains strong with more than $30 billion of qualified pursuits, continued political support for sustained defense budget increases and a growing set of international opportunities.

A 2018 budget agreement would be a catalyst for faster decision making on key pursuits and sustained funding increases. Importantly, as we look forward, the President is expected to request over $700 billion of defense funding for fiscal 2019, which would result in spending levels not seen in nearly 1 decade when war spending was at its peak. While achieving this level of growth would require the repeal of the Budget Control act, we are optimistic that the outlook for defense spending remains favorable.

Finishing with the Construction Services segment. Revenue in our Building Construction business increased by 22%. This growth included strong execution across our portfolio. Our book-to-burn ratio was above one, and we are pursuing more than $10 billion of opportunities with several important decisions expected this year. Several of these opportunities reside outside of the New York market, demonstrating successful investments to expand into new geographies.

The integration of the recently acquired Shimmick Civil Construction business has gone exceptionally well. Shimmick is a tremendous cultural and strategic fit with AECOM, greatly expanding our integrated civil infrastructure business and complementing our leading transportation design capabilities. Clients are increasingly utilizing integrated delivery, and Shimmick's Western U.S. expertise positions us to advance our fully integrated strategy.

Across AECOM, we are experiencing strong levels of activity and growth. With dedicated infrastructure funding measures in place, accelerating economic activity, and U.S. tax reform creating another meaningful catalyst for investment, we are as confident as ever in the outlook for our business and the markets we serve.

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

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

Thanks, Mike. Please turn to Slide 6. We are pleased to begin the year with strong first quarter results. Importantly, we are growing across the business. We delivered 8% organic growth, which included at least 5% growth in all 3 segments and growth in all geographies. With at least 8% growth in the last 2 quarters, we have now had positive revenue growth for 5 consecutive quarters. Wins of $6.1 billion included book-to-burn ratios of greater than 1 in all 3 segments, and was led by growth in our higher-margin MS and DCS segments with a book-to-burn ratio of 1.5 and 1.2 respectively. Our backlog is at a new all-time high.

Adjusted EPS was $0.57. Our adjusted effective tax rate was effectively 0, which reflects the impact of a lower rate from corporate tax reform. This provided a $0.03 benefit in the quarter. Excluding this benefit, our tax rate would have been 5%, which is consistent with the rate contemplated in our prior guidance.

We're also pleased with the underlying execution and margin performance. After adjusting for a previously disclosed legal settlement in the year-ago period and restructuring costs this year, adjusted EBITDA increased by approximately 20%. Free cash flow was $34 million and reflect normal seasonality. We are on track with our full year free cash flow guidance of between $600 million and $800 million. Our strong free cash flow performance reflects our diverse business model and culture focused on driving cash flow and is a key enabler of our capital allocation policy that includes share repurchases under our $1 billion authorization upon achievement of a 2.5 net leverage ratio.

Please turn to Slide 7. Revenue in the DCS segment increased by 5%, our highest growth in several years with strong contributions across the globe. We are benefiting from improved client funding in many of our markets. And our established local presence and history of storm recovery support are creating new opportunities. After adjusting for approximately $20 million of restructuring cost to improve operational efficiency in the first quarter, our operating margin was 5.8%. We're on track with our full year guidance for better than 6% margins.

Please turn to Slide 8. Revenue in the Management Services segment increased by 10%, which is the strongest growth rate in several years. This performance is a result of more than 50% backlog growth since the start of 2017 and positive momentum across the business. The operating margin was 5.9% and reflected strong performance across the business. We did not recognize any material incentives or award fees during the first quarter. Importantly, we continue to forecast margins to approximate our 7% target for the year.

Please turn to Slide 9. Revenue in the Construction Services segment increased by 11%. As Mike detailed, we had strong revenue growth in the building, construction and power businesses, where the pipeline remains strong. We also had solid wins in the quarter, led by a 1.3 book-to-burn ratio in Building Construction. I would note that our backlog does not reflect the full construction value of all work awarded to us. Specifically, we had a sizable $700 million win, where only our fee is included in our backlog, because the work was contracted on an agency basis.

Adjusted operating margin was 2.4%, which is a 100 basis point increase over the prior year. We are benefiting from a favorable mix shift to higher-margin power and civil work and strong execution across our portfolio. The Shimmick integration was successful and the business is performing ahead of expectations. Accordingly, we continue to expect margins to approximate 2% this year.

Please turn to Slide 10. First quarter operating cash flow was $52 million and free cash flow was $34 million. We remain on track to deliver our full year free cash flow guidance of between $600 million and $800 million for a fourth straight year. Our consistent execution on cash flow is notable as an industry that tends to have lumpier cash flow performance and is a key for stockholder value creation.

Please turn to Slide 11. Our strong start to the year provides us with tremendous confidence. We are delivering industry-leading revenue and backlog growth, and visibility remains strong. In addition, we are confident that tax reform will be a catalyst for increased investment in the U.S., and our international markets are performing well. As a result, we are reiterating our full year adjusted EBITDA guidance of $910 million and adjusted EPS guidance of $2.50 to $2.90. After adjusting for favorable legal resolutions that we recognized in 2017 and normalizing for tax, our adjusted EPS and EBITDA guidance reflect 10% and 7% growth respectively.

We continue to expect $0.08 of earnings from AECOM Capital at the midpoint of our guidance range. We did not have any realizations in the first quarter, but we have an attractive portfolio of properties at various stages of maturity and line of sight to achieving this year's guidance.

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I should note that because we are on a September fiscal year, our tax rate will be a blended rate of 24.5%, which reflects 9 months of the new 21% rate. Accordingly, we now expect our tax rate to be approximately 20% for the full year, which reflects the improved blended rate on U.S. earnings, which is partially offset by the loss of certain other items included in our initial rate guidance.

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

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Michael Dudas of Vertical Research.

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

Mike, you indicated some pretty visible catalysts for 2018. I would argue, probably, even beyond 2018 from an organic revenue front. Can you give a sense of it is it -- where do you think you see the weighting of like where the more immediate catalysts amongst what you're seeing? And is it weighting towards a private market response? Or just the continued strength in what we're seeing out of public-sector funding and demand opportunities?

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

Yes. First of all, thank you for the question. Listen, we have a number of catalysts in front of us. But before you even get to that catalyst, we had a quarter with revenue up 13%, 8% organically. We have backlog up 11% before we see the benefit of those catalysts. But the catalyst that we see in front of us are multifaceted. First of all, the amount of money that has come into the public sector over the past 18 months or so from all these $200 billion of specific tax measures for infrastructure at the state and local level in the United States is just starting to come into the market, right? We saw those enacted 18 months ago. It takes a while for it to get to the market. So that's in front of us now. So the catalyst is the projects actually coming to the market. So we see that in front of us. Secondly, at the federal level, we saw the President's proposal in the State Of The Union Address, for a transportation infrastructure bill that we are hopeful will make its way through the legislature this year. Third, we saw the President put his request in for a $700 billion defense budget, which we would benefit from significantly. So that's on the horizon. And then, the private sector has been an incredibly strong market for us. As you heard us mention, we are expecting our fourth year of double-digit revenue growth in our Building Construction business, and that is almost entirely private sector funding. And we see now another catalyst being the over $1 trillion of tax offshore earnings that are going to be repatriated to the U.S. under the tax bill as another catalyst for capital expenditure in the U.S. So we see a whole host of catalysts, both the public and the private sector, right in front of us here over the next 12 and 24 months.

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

And Mike, are you talking to the executives and companies that are looking to put this tax money to work yesterday?

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

Oh yes. They're -- you're seeing announcements from a whole host of companies in various industries that are suggesting that they want to put this money to work in the U.S., They want to relocate manufacturing in the U.S., and we think that's a real strong catalyst right here in front of us.

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

And just my final follow-up for, maybe, Troy. You talked about the growth -- or when you guys talk about growth in India and some of the other international markets, is that a market that's, obviously, by itself looks good, but also using some of the high-value engineering and expanding that group to help improve margins as you move forward on the DCS front? And how quickly can AECOM kind of move in and shift -- or get -- grow that type of business to help the margins going forward?

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

Yes. Mike, we -- as I said in my prepared comments, we actually saw all of our geographies grow in the quarter. So I wouldn't single out some of the geographies like India. They, in fact, are part of the overall businesses that is growing. And in terms of our margin performance, I wouldn't single out, as you said, high-value design centers. I think we think across the business as driving quality through our work, which improves our margins. And we see in particular in the DCS business, we see margins improving. As the business grows, we will benefit from operating leverage. If you think about this particular quarter, we did have restructuring charges in our DCS business during the quarter. And we also had a write-off as we were closing the books related to some receivables we had from a contractor in the U.K. They just entered into bankruptcy. If adjusted for those items, we had our DCS margins in the quarter being 6.2%, which reflected the improvement from the growing businesses. But again, I see growth coming from across the board, which is very positive for the overall business and our performance.

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

Yes. And Mike, let me just close out on the issue. Countries like India -- first of all, India, we're going to have our third year of north of 20% organic growth in that market. So that's been a market that's been hot for us for 3 years. But I -- it's not as much about the market as it is a signal of AECOM's ability to be agile across our global platform when we see real hot market opportunities. Our size, scale and geographic reach allows us to attack those markets when we see opportunities. And India has been one, and we're experiencing incredible growth there. But there are many other markets that heat up very quickly. One of the ones that's heating up right now is Saudi Arabia. And whether it's large-scale investments in their infrastructure or the number of very large new cities like NEOM and Khadia that are on the table right now, where you'll see very large infrastructure spending. And so I think it's more a signal of when we see a market heat up, we have the ability to be very agile and nimble, and move into those markets to take advantage of those opportunities.

Operator

Our next question is from Andrew Kaplowitz of Citi.

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

Mike, obviously, organic growth has ticked up over the last couple of quarters. I mean, you did 8% this quarter, 9% last quarter. It seems like the rate of backlog burn, especially in MS versus contracted backlog, has ticked up. So can you talk about your sustainability regarding this kind of organic burn for the rest of FY '18? Do you have good visibility toward, at least, your 5% organic growth longer-term revenue target in FY '18? And do you think MS revenue growth, specifically, could be 5% or better?

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

Yes. So I -- we look at a whole host of early indicators through our pipeline and then through the book-to-burn. But when you have a backlog up 11%, it portends well for future growth. And if you look at MS in particular, our highest-margin segment, we had $1.4 billion of wins in the quarter. We had a 1.5 book-to-burn in that segment, and our backlog is up more than 50% since the beginning of FY '17. So I feel pretty good about the book-to-burn across all of our segments. The Americas business, which is we've been watching very closely, because it's such a big, big part of the engine here, had a 1.2 book-to-burn that we -- we've been seeing real strength in that market. So the CS business tends to be a little bit lumpy.

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And there, even with a 1.0 book-to-burn, that's influenced by the nature of some of the contracts. When you have a win like we had that's an agency win, where you don't necessarily get the revenue, but you get the earnings, those kind of projects might skew the numbers a bit. But the bottom line is that we feel really good about the pipeline of activity. We feel good about the wins. And we think we can continue, fairly comfortably, along the path of those 5% long-term revenue growth targets that we set out.

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

So Mike, just to follow up on that, in MS, last quarter, you had mentioned $16 billion of expected decisions over the next few quarters. Today, you kind of alluded to we need to see some of that back and forth in Washington sort of take care of itself. Have you seen any bit of a slowdown in decision-making over the last couple of months? Or has it still been relatively steady? So even if we kind of still have a bit of back and forth, MS should be okay here this year.

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

Yes. If it's okay, Andy, I'll let Randy take that question.

Randall A. Wotring - *AECOM - COO*

Yes. Andy. Look, I think the pace of opportunities remains high. We have several key decisions over the next couple of months that are expected and just a continuing stream. So we have bids that have been submitted and awaiting award for 1 to 2 years. So we expect that those will continue to move through any minor delay or slowdown associated with the delays we're seeing in Washington today. They are going to be minimally impact us. We don't see it slowing down. So there's enough throughput to continue to see something come out at the end of the funnel.

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

Okay. That's helpful, Randy. And then, Troy, I just wanted to ask you about accounting for revenue recognition. Did that impact your business at all? Was it meaningful at all to how AECOM reports?

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

So the answer is no, it wasn't. And we're not implementing the new revenue recognition guidance until the end of this fiscal year. So it will take place in '19. But even when -- even as we move to '19, we don't see anything at this point that indicates it will have a meaningful impact on how we're recognizing revenue, and specifically, how we're recording things in our backlog.

Operator

Our next question is from Jamie Cook of 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, back to the Management Services. The backlog and the organic growth has been growing at a very fast rate. Mike, I'm just wondering as we think over the longer term, how do you think about the opportunity to get those margins, in Management Services, back to sort of the high single digit or low teens range? Is it further out just based on when you see opportunities for milestone payments? Or is it more a function of just the accounting for the contracts? Because while it's growing higher, the margins are at a much lower rate. And then, my second question, could you just remind me what your assumptions are for 2018 around your energy business? How big that is today, and could that potentially provide some upside based on what you're seeing in the markets and where oil prices are?

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

Great question, Jamie. I'll ask Troy to address the margin-related issues there.

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

Yes. So Jamie, on the MS margins, if -- just taking you back a little bit in time is, we sort of set a long-term rate for margins and we set it at 7%. And that was driven based on a change in our mix of revenues. Meaning that we would have less from joint ventures. We don't consolidate revenues. And more where we were taking the lead or primary position, where we'd have more revenue that would consolidate into our financial statements. So we see the 7% being a target for the year and being a long-term target based upon the backlog and the types of work that we're bidding. And we also see upside in those margins periodically based on incentive fees and award fees that we have in those projects from time to time that can swing that in our favor. And then, with respect to your second question, on oil and gas, is oil and gas represents a few percentage points of our business in terms of revenue. And it is not a contributor at this point in time, but if things continue to improve and environment continue to improve, that there would be some upside to our results from the oil and gas business.

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

Okay. Mike. And then, just one follow-up question. Just based on the strength that you're seeing in the backlog and the awards over the past couple of quarters. Are you getting concerned at all about sort of capacity constraints on the labor side? Or are there any areas that you feel like you need to sort of beef up on the professional services side or construction side?

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

No, I don't have any abnormal concerns. Labor and talent is something we focus on quite a bit, and we always have. And so it's nothing outside of the normal concerns about ensuring that we get the best talent everywhere we are. But there's still capacity in the markets, Jamie, mostly because of the large CapEx drop-offs that we saw in the oil and gas sectors. There's still plenty of talent around to meet these needs. And we've got a long window of planning for all these projects that should not present a problem.

Operator

Our next question is from Andy Wittmann of Baird.

Andrew John Wittmann - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

I guess I wanted to ask on free cash flow and the benefits, I guess, from the tax law that was recently passed. You guys, your cash taxes, I guess, this year have been benefiting versus your GAAP taxes for various reasons that we've talked about in the past. I guess, Troy, can you talk a little bit about how we should be thinking about the free cash flow benefits from the tax law on a longer-term basis? I guess, maybe it doesn't help you as much this year as it otherwise would have, but longer term, it should. And if you could just give us some brackets around that, I think, that would be helpful.

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

Sure. Andy. Thanks for the question. Again, I just -- I want to make a point on the current year first, which is that our free cash flow guidance this year remains unchanged. We still expect to be in the $600 million to $800 million range. So in terms of the tax reform impact on the current year, we don't see it having an impact that would cause us to have any concern about hitting those targets. In the longer term, of course with the rate going down, we do see a tailwind in terms of cash flow. We haven't projected what that impact is going to be on our longer-term operating

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performance. We had originally forecast in our long-term guidance a 27% tax rate. I would say that we're still working through that now as we're getting more clarity from the government on how to interpret certain elements of tax reform. But I would expect our tax rate to go into the mid- to low 20% range, which of course that's GAAP and that's also tax. And it would provide a tailwind to our long-term cash performance or free cash flow.

Andrew John Wittmann - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

On Shimmick, I know there's a look back on acquisitions done as an asset purchase. Are you going to pick up any cash tax benefit from looking back on Shimmick? Or is that -- was that one closed too early?

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

I don't expect any cash pick up. I think purchase kind of reflects the results of the acquisition. (inaudible)

Andrew John Wittmann - *Robert W. Baird & Co. Incorporated, Research Division - Senior Research Analyst*

Okay. Great. And then maybe -- okay. Mike, I guess, you went to kind of the private sector benefits of the tax law causing -- hopefully, causing your customers to invest more. Is it -- how much should we be considering the negative impact of the lack of a deductibility of the salt tax and higher-tax states maybe unwilling to raise taxes to fund their infrastructure portion? I just -- some of your thoughts on that would be helpful as well.

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

Yes. Sure. If you look at the recent -- past 18 months and what we're seeing at the state and local level, I think your point about the reluctance to increase the general fund taxation or income taxation is probably correct. But what we're seeing is states and municipalities that are very comfortable voting to increase specific tax measures, like the sales tax that we saw in California and in Los Angeles, that are producing wholly dedicated infrastructure funds. And we don't see any reluctance on the part of either government or taxpayers for that matter, to increase their taxation if it's wholly dedicated to infrastructure. It tells you that our taxpayers recognize the need for more infrastructure and are willing to pay for it. In Los Angeles, we had a 72% voter approval rate to increase the sales tax to produce a wholly dedicated transportation infrastructure fund. So I think you'll see more of that, then you're going to see a general increase in income tax rates.

Operator

Our next question is from Tahira Afzal of KeyBanc Capital Markets.

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

I guess, first question, if I look through your end markets and those of legacy URS, it seems that you could be going into a pretty high-powered growth phase in a lot of your core markets that haven't all worked together. Could you talk, Mike, talk a bit about where that growth rate could go maybe over the next year or 2 versus your long-term outlook right now, your metrics that you put out there?

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

So Tahira, we are not changing our long-term guidance, which is a 5% CAGR and a 12% to 15% growth in EPS, although with tax rates going down and all the positive signs that we're seeing of course, it causes us to lean into the higher end of that range from a long-term growth perspective. And when I say the higher end range of that 12% to 15% EPS growth. So where could it go? Again, I don't want to increase the long-term guidance just yet. But when you see back-to-back quarters of 8% and 9% organic growth and book-to-burn rates of 1.2 and backlog up 11%, all of that seems

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very positive. And we don't see that abating in the near future. So I'd like to leave it at that for our long-term guidance. We feel an even higher level of confidence in the guidance that we've already put out, but not prepared to raise 5-year guidance just yet. But we'll continue to update you on that as the quarters develop. But we do like the trend here of back-to-back quarters of 8% and 9% organic growth, and more importantly, that growth coming in our higher-margin segments of DCS and MS. So all that feels pretty good for the future.

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

Okay. Mike, that's actually helpful. I guess, my second question is, we've got this highly-anticipated infrastructure bill coming out. You guys have done a phenomenal job taking stakes and being nifty around private stakes within some of the projects, more on the commercial side. If there is more of a public-private partnership plan to the bill that comes out, is that going to favor market share gains for yourself?

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

Without question, Tahira. We have invested in that space. As you know, most of our investments so far have been on the private sector side. Although we have hired up teams on the public-private partnership side and the private infrastructure side. We have significant teams in place with very experienced investors that will help us bring capital to those markets, so that we can continue to differentiate ourselves in a market that is going to have much more private sector involvement. Whether or not we have an infrastructure bill coming out of the Federal government, the private sector has large pools of capital that would like to bring it into the infrastructure space. And we are geared up to facilitate that market right now.

Operator

Our next question is from Chad Dillard of Deutsche Bank.

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

So how sustainable are your DCS incremental margins? If I take out some of the onetime items past quarter, I get around 11%. And if I look back to the prior quarter, it's about 16%. And that's all while you actually start to get back to your organic growth in that segment. So as we continue to grow here, I'm just trying to understand, I mean, is that the right level kind of at the low double-digit to contemplate?

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

Yes. So I would think about that this way, is we said that we would have a 6% target. And with growth, we would see that improving over time through the 6s and into the 7% in our long-term forecast. So we expect that to continue to improve from the -- off the 6% base we forecast for this year, and have some upside in it. If you look at, incrementally, the margins and the incremental revenue in the quarter. So comparing it to other revenue and operating profit was in a prior quarter, inherent in that incremental margin is the 12% margin in that business. So we certainly are seeing a margin improvement across the business and driven by growth.

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

And then, can you speak to your project margins in backlog and MS? Are they higher today than they were a year ago? I'm just trying to understand the underlying pricing for your new projects versus old projects. I guess, I'm thinking more about just the ones that are consolidated in your business, just to stay apples to apples.

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

Yes, Chad. It's consistent with our -- it's consistent with the long-term guidance that we've given. Margins and our backlog are consistent with our expectations for the current year and our 5-year forecast.

Operator

Our next question is from Bobby Burleson of Canaccord.

Robert Joseph Burleson - *Canaccord Genuity Limited, Research Division - MD & Analyst*

So just curious, in the Senate introduction of the new water infrastructure investment reform legislation. They're talking about a $500 billion shortfall in water infrastructure funding. I just wanted to get your thoughts on that potential legislation and how you guys are positioned to capitalize on that?

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

Yes. So I think we go back for many, many years where water infrastructure has been underfunded at the federal level, it's been underfunded at the state and local level. So we are, of course, very strongly in favor of any new water infrastructure. But the -- when we went back to the WRDA bill a few years back, it was $5 billion. It was not something significant. And so anything that comes out of the federal government would be a real plus up for us. But without it, the market is still okay. It's not our strongest market, although we have seen very nice growth in the water infrastructure business here in the Americas this past quarter. But anything coming out of the federal would be a good, positive catalyst for us. But with or without it, the market doesn't change too much.

Robert Joseph Burleson - *Canaccord Genuity Limited, Research Division - MD & Analyst*

Okay. And then, you did touch on hurricane recovery in the formal comments. Curious what the pricing looks like, given the expedited nature of some of that work?

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

So first of all, we've been very fortunate that we've had over $200 million of wins to date from the hurricane recovery. Again, it speaks to our broad geographic presence and our agility to move to those opportunities as quickly as possible. But more importantly, we've got another $1 billion of opportunities that we're pursuing due to hurricane relief, and the margins are consistent with our traditional DCS margins.

Robert Joseph Burleson - *Canaccord Genuity Limited, Research Division - MD & Analyst*

Okay. And then, last one, just on the MS business. Wondering if -- you mentioned that things haven't really changed in a big way in terms of the amount of activity you're seeing out of DoD and DOE. But wondering if, maybe, the size of potential project that you're seeing has changed at all, any kind of unwillingness to commit to larger projects, given what's happening in Washington right now, on the part of the customer?

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

Randy?

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Randall A. Wotring - *AECOM - COO*

Yes. This is -- yes, Randy. I think what Mike said earlier, we are seeing positive movements regarding budgets in DoD, which is our largest federal customer. More than 50% of our revenues come from DoD, and our second largest customer is the Department of Energy. Just because of our platform and our priorities, we are focusing on bidding larger jobs. So we have a great pipeline of very large opportunities that we have visibility on over the next 3 to 4 years. So we're not -- nothing's changed. We are in a good position in that marketplace, and continue to mine and look for, and position for, those very large opportunities.

Operator

Our next question is from Steven Fisher of UBS.

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

Steve?

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

Hey, Steve?

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

Sorry about that. Can you hear me?

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

Yes.

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

We can.

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

I wonder if you could just talk about your Building Construction outlook? And from a regional perspective, where you see the growth being driven by this year, and then, beyond 2018, please.

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

Yes. Sure. So this quarter alone, we had $2.4 billion of wins in CS, and what's really encouraging there is it's a broad-based win rate. We had over $1 billion of new stadium wins. So it's not just tall vertical building. A big portion of that business is outside of New York City. And we also have about $2 billion of what I'll call soft awards. And what I mean by that is these are where the client has told us they're going to give us the work, but we haven't officially been notified yet, but -- so that's about another $2 billion of awards that we -- you should expect to see from us, literally, in the next 60 days or so. So very encouraging signs there, the pipeline is as strong as it's ever been. Like you heard me mention earlier, it's fourth -- this year will be the fourth year -- we expect this year to be the fourth year of double-digit organic growth in that Building Construction business. And that's before we see the real pickup in the industrial sector. And that's what I was mentioning earlier. We expect to see that $1 trillion of money

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repatriated due to the tax bill, where a good portion of that will be invested in the industrial sector, manufacturing-type facilities. We see that as a real strong catalyst to further diversify that business away from tall office buildings, although tall office buildings have continued to be a very strong market, showing no signs of weakness. The sports business continues to be a very strong business for us. And the other real strong market that we see is data centers, and we've been a significant player in the data center market for a while. So it's a fairly diversified end market, not just New York tall buildings.

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

Okay. And can you give us an update on what you're expecting year-over-year for business development or bid costs? And what the impact on margins is there?

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

Yes. Troy?

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

Yes. Steve, I would, again, as we go through the year, this might change. But right now, I would think about it as being flat year-over-year.

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

Steve, I just -- I left out one real important part of the Construction Services business, and that was the civil Construction business that I should have mentioned. With the acquisition of Shimmick, we're off to a real strong start there. We've got about $15 billion of integrated delivery projects we are pursuing, meaning in integrated delivery, we are pursuing both the engineering design and the Construction Services. And the real good news, and I'd say Shimmick is off to a real strong start in this quarter. Shimmick's growth, their own organic growth, if they were a stand-alone entity, was up 34% over the same quarter a year ago, and so a real strong start for that acquisition, and an incredible $15 billion pipeline in front of us for integrated civil construction. And as you know, Shimmick's focuses on -- in the western U.S., which is one of the strongest markets in the world right now for civil infrastructure.

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

Great. And by the way, I had gotten on the call late. So if you had covered any of that before, I apologize.

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

No problem, Steven.

Operator

Our next question is from Brent Thielman of D.A. Davidson.

Brent Edward Thielman - *D.A. Davidson & Co., Research Division - Senior VP & Senior Research Analyst*

Just a follow-up on the hurricane-impacted areas. You mentioned the $1 billion in opportunities you're looking at through DCS. Anything surfacing with respect to the MS segment, in regard to those areas?

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

Do you want to take that?

Randall A. Wotring - *AECOM - COO*

So there's -- the MS is supporting the DCS operations on activities in both Puerto Rico and the Virgin Islands. So that's in support of -- we're going at that as an integrated company. So all you're seeing is the numbers flow through DCS at this point in time.

Brent Edward Thielman - *D.A. Davidson & Co., Research Division - Senior VP & Senior Research Analyst*

Okay. And then, Mike, the $15 billion pipeline I think you had mentioned between Shimmick and AECOM, I think you're pursuing on the West Coast. Just to be clear, is that predominantly California?

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

Yes, predominantly California. Not all California, but predominantly, yes.

Brent Edward Thielman - *D.A. Davidson & Co., Research Division - Senior VP & Senior Research Analyst*

Okay. And then, it sounds like you've got a pretty healthy pipeline in power as well. Obviously, good growth here this quarter. Is that still all gas-related? Are you seeing any shift to other areas?

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

It's predominantly combined cycle work, as well as the nuclear decommissioning work, like the San Onofre project.

Randall A. Wotring - *AECOM - COO*

Yes. And just to add, our power business is broadly diversified. So we build new power plants, but we do a lot of nuclear work, like you saw with our announced Bruce refurbishment contract in the Canadian nuclear sector, and our maintenance work, which is for long-standing clients. So this is all recurring in nature. So a lot of that work in power is routine stuff that we've done for years.

Operator

Our last question is from Rob Norfleet of Alembic Global Advisors.

Robert Fillmore Norfleet - *Alembic Global Advisors - MD & Senior Analyst*

Just coming back quickly to power, I know, obviously, on the one project that you are currently operating on, you're at roughly 50% completion. Obviously, that project looks like it's on track. Can you kind of give us a status of the other 2 projects that are awaiting funding at this point, and when you expect to break ground on those? And I guess, the second part of that question would be, also, can you just talk about what you're seeing from a bidding opportunity? Clearly, a number of your competitors had some issues with power-related projects, which has caused some people to step back from that market. I mean, are you still seeing an ample set of opportunities? Or have things changed from a risk perspective there?

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Randall A. Wotring - *AECOM - COO*

Yes, Rob. So this is Randy. Look, we have one large combined cycle gas power project underway. And again, it continues progressing well. It's the Alliant $700 million combined cycle plant in Wisconsin. And as you said, we're nearly 50% complete against the cost. And just, overall, really pleased with the performance on the job. The other contract we have that's large is we are executing on the 10-year decommissioning of the SONGS nuclear plant in California. This job also continues to progress well. We have been selected on 2 more combined cycle projects, but both projects are still working through financing and neither has started. We may have more clarity on that in the second quarter or towards the third quarter. But at this point in time, we're supporting activities there, but those haven't started. So look, as we talked before, we spend a lot of time assessing risk of the market. And both because of the inherent risk in large fixed-price projects and because we see the issues in the sector. Our Power group takes a very different approach where we have -- we're not only differentiated through price, but through the client and subcontractor relationships we have. Same bidding team delivering -- as the team delivering on the project. And we don't lock in our prices until we have significant costs have been locked in with our subs. We only do back to back on -- with the EPCs on performance, and we flow down risk to our subcontractors. We only work where we have extensive union labor footprint experience. And so from all those things come together, we have a great experience in this marketplace, without any significant write-downs over a 2-decade period. So I think we are not risk averse, but we really manage the risk and mitigate it where we can, and have a great track record.

Robert Fillmore Norfleet - *Alembic Global Advisors - MD & Senior Analyst*

That was helpful. Just my quick follow-up is, can you just broadly -- can you help broadly discuss the competitive landscape that you're seeing across your segments, especially in DCF -- DCS and the Americas? I guess my question is, clearly, we're seeing this increase to demand. We're seeing, obviously, this potential flood of available money that's going to be spent, which typically results in more competitors coming into the space, even international competitors. I just wanted to get your sense for what you're seeing from that perspective, and if there's any kind of change at the behavior?

Randall A. Wotring - *AECOM - COO*

We're not seeing any disruptive market -- marketing activities in place across our sectors. And across -- in the different sectors, we are seeing the level of competition change, but it's not significant. I think what we expect is that we are where we're positioned and invest in business development, we'll continue to do well. We don't see any massive change.

Operator

I will now turn the call back over to Mike Burke for closing remarks.

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

Thank you, operator. Well, I'm hoping that everyone, over the course of today's discussion, picked up a couple of key themes that we were delivering. And first of all is that, after investing for several years now in business development activities, in restructuring and adding capabilities, we are clearly delivering industry-leading growth, both on the revenue line, on the profit line, and on the backlog line. And we continue to win at an incredible pace with a double-digit growth in our backlog to $49 billion now, and we're not stopping there. There is considerable market opportunities in front of us that you've heard us mention a number of times today.

And then, of course, hopefully, you heard our message that we're committed to driving substantial value for our investors through the execution of our capital allocation policy. And as Troy mentioned, we are clearly on track to achieving our 2.5x net leverage ratio by the end of September of this year. And then, thereafter, as we said, we will begin executing our share repurchase under our $1 billion board authorization. And from where we sit, the future has never been brighter for AECOM, our employees and our shareholders.

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So thank you for your continued attention to AECOM and your participation today, and we look forward to our next discussion in May. Thank you.

Operator

Thank you, ladies and gentlemen. This concludes today's conference. Thank you for participating. You may now disconnect.

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