TRANSCRIPT

Q3 2024 Earnings Conference Call

WillScot Holdings Corp. (Nasdaq: WSC)

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WILLSCOT PARTICIPANTS

Brad Soultz, Chief Executive Officer

Tim Boswell, President & Chief Financial Officer

Nick Girardi, Vice President FP&A

MEETING PARTICIPANTS

Andrew Wittmann, Robert W. Baird & Co. Incorporated

Angel Castillo, Morgan Stanley

Faiza Alwy, Deutsche Bank

Luke McFadden, William Blair & Company L.L.C.

Philip Ng, Jefferies LLC

Ronan Kennedy, Barclays Bank PLC

Scott Schneeberger, Oppenheimer & Co. Inc.

Steven Ramsey, Thompson Research Group, LLC

TRANSCRIPT

Operator

Welcome to the Third Quarter 2024 WillScot Earnings Conference Call. My name is Sherry, and I'll be your operator for today's call. (Operator Instructions) Please note that this conference is being recorded. I would now like to turn the call over to Nick Girardi, Vice President, FP&A, Nick, you may begin.

Nick Girardi

Good evening, and welcome to the WillScot Third Quarter 2024 Earnings Call. Participants on today's call include Brad Soultz, Chief Executive Officer; and Tim Boswell, President and Chief Financial Officer.

Today's presentation material may be found on the Investor Relations section of the WillScot website. Slide 2 contains our safe harbor statements. We will be making forward-looking statements during the presentation and our Q&A session. Our business and operations are subject to a variety of risks and uncertainties, many of which are beyond our control. As a result, our actual results may differ materially from today's comments. For a more complete description of the factors that could cause actual results to differ and other possible risks, please refer to the safe harbor statements in our presentation and our filings with the SEC.

With that, I'll turn the call over to Brad Soultz.

Brad Soultz

Thanks, Nick. Good afternoon, everyone, and thank you for joining us today. I'm Brad Soultz, Chief Executive Officer of WillScot.

As highlighted on Slide 16, our team executed well in Q3 despite a market environment that continues to be worse than we anticipated. On the positive side of the ledger, adjusted EBITDA margins were at record levels of 44.4%, and adjusted free cash flow and return on invested capital were also near record levels. And we've continued to advance several key enterprise-wide initiatives that position us well for 2025 and beyond.

On the negative side, nonresidential construction starts square footage was off 14% year-over-year in the quarter and are now tracking 15% below 2019 levels. Consistent with that contraction, we saw delays in a lot of the encouraging order activity in our pipeline in Q2, which both impacted the quarter and makes us more cautious towards the end of the year.

However, we continue to see steady demand from larger projects and both backlogs and customer sentiment remains strong among our larger national accounts and contractors. Similar to prior quarters, smaller, more rate sensitive commercial construction projects made up the bulk of the decline and we increasingly heard customers point to the election as factoring into their timing decisions for project starts.

So we do believe this is a portion of the demand that's simply pushing to the right. Given the flexibility in our model, we reacted quickly to the lower activity levels and reduced variable costs by over $20 million relative to our forecast for the quarter, which is on top of the approximately $40 million of annualized indirect cost takeout that we executed heading into the quarter.

This contributed to the sequential and year-over-year margin expansion that we delivered in the quarter and positions us well for margin expansion in 2025 and beyond. So while volume-related headwinds remain in the immediate term, the team is executing well through those and those volume headwinds do continue to moderate as we head into next year, although not to the extent we had anticipated when we spoke a quarter ago.

Many investors have asked separately to me what comes after the termination of the McGrath transaction? And it's very straightforward. We're continuing to execute the proven playbook that has allowed us to have already achieved and, in many cases, exceeded the ambitious 3 to 5-year margin and return milestones that we established just 3 years ago.

Heading into 2025, we're 100% focused on operating and optimizing our business, delivering for our customers and driving growth across the portfolio. As depicted on Slide 10, we do continue to move full speed ahead with ongoing investments in operational efficiency and customer-focused initiatives, which will allow us to further differentiate our unique and expanding portfolio space solutions.

You will recall in Q1, we combined the legacy Mobile Mini and WillScot field sales and operating team. In Q2, we completed our final major systems integration along with the consolidation of our field service and dispatch platform teams.

In Q3, we consolidated under the WillScot brand and launched a combined website, introduced new powerful digital marketing customer service and sales tools. And as we head into 2025, we'll continue to further optimize and leverage all of these while also turning our focus to streamlining our order-to-cash process from a customer service and back office efficiency standpoint.

Optimization of our order to cash processes represents a meaningful opportunity to improve both our customer and employee satisfaction. These are the right organic investments to drive sustainable growth and enhance the customer experience, and we believe that represents significant points of operating leverage heading into 2025.

Additionally, as depicted back on Slide 4, we continue to expand our portfolio of space solutions, including climate control storage, clearspan structures and sanitation, among others, that are in incubation. Collectively, when combined with our core offering, these new adjacencies offer further opportunities to extend our differentiated value proposition to existing customers.

Individually, they also expose a diverse set of new customers and end markets to which we can, in turn, offer our full entire portfolio of space solutions. And we're approaching all of these with a balanced combination of organic investment, acquisitions and new product innovation.

While the contributions from these adjacencies were modest in 2024, their run rate doubled throughout the course of the year, and we expect they can double again in 2025. These represent new levers to expand our total addressable market and grow our business.

Looking ahead to 2025, we think we're set up for a return to modest growth, and Tim will take you through our preliminary views on that as we head into our budgeting process. Taking a longer-term view, we remain extremely optimistic with respect to continued growth inherent in this platform.

To that end, we anticipate hosting our next Investor Day during the first half of next year and expect we will announce those logistics before the end of this year. Themes for our 2025 Investor Day will center on strong organic growth, the expansion of adjacent solutions, developments of verticals, our advancements in technology, investments in human capital, new 3 to 5-year financial targets and any applicable updates to our capital allocation framework.

Meanwhile, we'll continue to execute our disciplined capital allocation strategy, which has resulted in more than $2.1 billion of capital delivered to our shareholders and a 21% reduction in our economic share count since 2021.

As always, organic CapEx will be demand driven, driven in part by market conditions, but also by value-added products, new markets and categories that we're already pursuing. We'll continue to execute tuck-in acquisitions in both our core and adjacent markets, including a few smaller transactions that we've already executed in Q3 and Q4 as we reprime that pipeline. And we'll continue to return available surplus capital to our shareholders through our share repurchase authorization, which our Board of Directors recently increased to $1 billion. In the meantime, we'll remain laser-focused on flawless execution as we progress towards our $4 of free cash flow per share milestone.

With that, I'll hand it over to Tim to discuss Q3 and our outlook in a bit more detail.

Tim Boswell

Thanks, Brad, and good evening, everyone. Page 23 shows a high-level summary of the quarter. Clearly, the quarter and the revised outlook did not play out as we expected coming out of Q2, although we see plenty of bright spots that give us confidence our model is working and positioned for the recovery when markets stabilize.

For context, in the last 2 years, we've seen the largest contraction of nonresidential construction square footage since the global financial crisis. That contraction has been longer and deeper than we expected and has impacted volumes However, those volume headwinds are moderating as we progress into 2025.

Meanwhile, margins are improving as expected as we progress through the year, given both the flexibility in our cost structure and structural improvements we've implemented, leveraging our technology platform. Free cash flow remains stable and predictable with best-in-class free cash flow conversion and free cash flow margin and with adjusted free cash flow per share increasing by 13% to $3.12 over the last 12 months.

ROIC remains stable and supports economic value creation, and we are back to allocating capital across organic opportunities, tuck-ins and shareholder returns, which has been a quite effective formula historically, and gives us a familiar playbook heading into 2025. So we remain quite confident in our strategy, our unique platform and capabilities and the strength of the WillScot team.

Turning to Page 24. Revenue of $601 million declined 1% year-over-year, driven primarily by volume headwinds impacting both storage leasing revenues and delivery and installation revenues, which were down 13% and 1%, respectively. These were offset by modular leasing revenues and VAPS, which were up 4% and 1%, respectively, as well as sales revenue.

So overall, no real change to the recent trend of solid modular results offsetting storage. Value-added products penetration for modular units inflected positively this quarter, which we've been expecting for some time with average rates up 3% year-over-year and delivered rates in the third quarter, up 1% versus prior year. Storage value-added products continued to grow rapidly with average rates up 28% and delivered rates over the last 12 months, up 16%.

Growth of these penetration rates in a challenging market and competitive environment is a testament to the underlying customer value proposition. And I'm excited about other systemic improvements we're putting in place heading into next year to present our turnkey offerings more effectively.

There are no real changes to pricing trends in the quarter. Average monthly rental rates were stable across the portfolio with storage average monthly rental rates up 9.5% and modular average monthly rates up 6%.

In terms of profitability, we generated $260 million of adjusted EBITDA, up 1% year-over-year at a margin of 44.4%, which itself was up approximately 50 basis points versus last year and up 80 basis points sequentially. We always expected margins to expand in the second half of the year, so we continue to be pleased with our margin trajectory heading into 2025.

That said, revenues came in late in the quarter relative to our expectations. So we offset that with over $20 million of variable cost reductions that were executed during the quarter. That variable cost reduction built on the approximately $40 million of annualized indirect cost takeout that we executed in Q2.

So based on that, we expect continued sequential margin expansion into Q4 and another year of modest expansion for the full year next year based on initiatives we have in place heading into 2025. As we disclosed back in September in Q3, we incurred approximately $203 million of broken deal costs, including the McGrath termination fee, and we have backed these out of the adjusted financial metrics to isolate our operating performance.

This resulted in adjusted EBITDA of $267 million, adjusted income from continuing operations of $72 million, adjusted diluted earnings per share of $0.38 and adjusted free cash flow per share of $0.77 for the quarter and $3.12 over the last 12 months.

Moving to Page 25. Cash provided by operating activities continues to be quite strong and would have totaled $202 million in the quarter, were up 6% year-over-year, excluding broken deal costs. Net capital expenditures were up $16 million year-over-year to $59 million, primarily due to a large property sale last year and accelerating organic run rates in our newer product lines.

Again, excluding broken deal costs, adjusted free cash flow for Q3 was $143 million with a 24% margin. So we continue to feel very good about our free cash flow trajectory heading into 2025. And the overall cash conversion efficiency of our business model. Over the last 12 months, adjusted free cash flow totaled $583 million at a 24% margin, which represents $3.12 of adjusted free cash flow per share on our September 30 share count.

That's up over 13% versus the prior year LTM period and represents an 8% free cash flow yield on today's market capitalization. Cash flow visibility remains an incredible strength of the business. Free cash flow per share is compounding at mid-teens rates in a down market, and we remain on track towards our $4 free cash flow per share milestone and our longer-term $700 million free cash flow milestone.

Turning to Page 26. Leverage ticked up 1/10 of a turn in the quarter to 3.4x net debt to last 12 months adjusted EBITDA due to payment of deal breakage costs and resumption of share repurchases. We remain inside our target leverage range of 3.0x to 3.5x, and we have the capacity to deleverage by approximately 1 turn per year when we so choose, so are unconstrained from a capital allocation standpoint.

Between our internally generated cash flow and our $1.7 billion of revolver availability, we have significant excess liquidity. Taking into account our interest rate swaps, our debt structure is approximately 89% fixed and 11% floating rate. So we have limited immediate interest rate exposure and have opportunities to refinance higher coupon bonds opportunistically if interest rates continue to moderate.

As of September 30, 2024, our weighted average pretax cost of debt stands at 5.8%. I'll note our 2025 senior secured notes mature in June next year. We have ample liquidity available to simply draw on our ABL revolver and repay the 2025 notes. So between internally generated cash flow, available ABL capacity in the bond market or some combination thereof, we have multiple options to refinance the 2025s at a time of our choosing and to optimize our cost of capital.

Page 28 shows our capital allocation over the last 12 months, which remains largely consistent with the framework we outlined at our 2021 Investor Day. In the right-hand chart, over the last 12 months, net CapEx of $231 million is very much in line with our framework target and likely increases into our guidance range of $250 million to $280 million by the end of the year.

Over the last 12 months, we allocated $164 million to tuck-in acquisitions, which were primarily in the cold storage and Clearspan product lines during this period. And over the last 12 months, we have reduced our share count by approximately 3.3% and returned $286 million to shareholders.

We've highlighted the $212 million of broken deal costs over the LTM period, the majority of which were in Q3 this year. However, those are behind us, and it's easy to see how that capital will be reallocated to shareholder returns in our framework as we move forward. Just as an example, the 13% free cash flow per share growth that we delivered over the past year would have been in the high teens had we allocated that capital to the repurchase.

So based on the strong returns and our cash flow visibility, our Board of Directors increased our share repurchase authority again in September to $1 billion. And overall, we continue to see between $800 million and $1 billion of capital available annually to allocate, which is critical to how we compound returns.

Heading into 2025, our capital allocation framework is consistent with how we've operated for the last several years. And to the extent we make adjustments, we will discuss that rationale with you in detail at our next Investor Day.

Before turning it back to Brad, Page 28 shows our outlook for 2024. Based on our performance year-to-date and our visibility into Q4, we revised our outlook to a midpoint of $1.060 billion of adjusted EBITDA, which reflects the reality that nonresidential construction markets are likely to continue bottoming into the first half of 2025 as customers get more certainty around the political and interest rate landscape, that is longer and deeper than we expected, and we've reduced our revenue assumptions primarily for Q3 and Q4 relative to our prior outlook.

That said, volume headwinds do continue to moderate as we progress into 2025, although not to the full degree we expected in July. But this still represents a meaningful improvement relative to our run rate entering 2024. Also on the positive side, we are absolutely seeing the margin expansion that we expected in the second half, even despite meaningful operating leverage headwinds from lower volumes.

So while we are disappointed with the short-term results, our longer-term trajectory towards stronger margins, free cash flow and return on invested capital are all clear and would respond powerfully when markets stabilize, which is what we still anticipate in our base case for 2025.

So we at least want to share our current framework for thinking about that year. Our base case sitting here today assumes nonres starts will flatten in 2025, in contrast to the double-digit declines we've incurred all year. This supports moderating volume headwinds as we progress through the year, which we are beginning to see, and we do see opportunities for improved commercial execution in certain areas, and we have very tangible growth across some of the newer product lines.

That combination supports modest organic revenue growth for the year and continued margin expansion in 2025, which we think is a balanced acknowledgment of both the recent deceleration and the underlying longer-term opportunities. Obviously, we'll be prepared for all scenarios, and we'll be actively developing upside opportunities.

So sitting here today, this is generally the organic framework we are using to set our internal targets for the year. As always, we strive for transparency with our operating assumptions welcome insights from our shareholders have high expectations for our team and appreciate the ongoing partnership with our over 85,000 customers.

We look forward to meeting with many of you before the holidays and welcoming you to our second Investor Day in the first half of next year, most likely in Phoenix, with details coming soon.

So with that, Brad, any closing thoughts?

Brad Soultz

No, just quickly, I'd like to thank our shareholders for continued trust with their capital, employees for continuously raising the bar while caring for each other and our customers; and most importantly, as Tim said, thank you to the 85,000 customers that partner with us to meet their critical space solution needs.

Operator, would you please open the line for Q&A?

Operator

(Operator Instructions) Scott Schneeberger with Oppenheimer.

Scott Schneeberger - Oppenheimer & Co. Inc.

I'm going to start off with a volume question, and then I'll follow after with a pricing question. For you guys repeatedly referenced volume -- the volume headwind moderating and just shared a little glimpse of what you were thinking about for 2025, could you kind of put some substantiation behind why you view volume -- the volume headwind moderating and maybe break it out between the modular and the storage segment?

Tim Boswell

Yes, Scott, this is Tim. I'll start. I mean if you look at the average unit on rent deficit versus prior year in Q3, you're down about 3%. Entering 2024, that would have been closer to 5%. So we see that continuing to slowly converge, although not to the degree we expected in coming out of Q2.

And you see a similar dynamic in storage. Sitting here today heading into the end of October, I'd expect units on rent are actually pushing towards 130,000 units on rent. So we are seeing that sequential build in the storage business, which if it continues, again, puts us in a smaller volume deficit heading into 2025 than we had coming into 2024, although, again, not to the degree we expected in Q2.

So that's the dynamic that we're referring to. It just means that relative headwind in the business is not as forceful as it would have been entering this year, which means we can lean on those other levers that we talked about to drive lease revenue growth.

Scott Schneeberger - Oppenheimer & Co. Inc.

Okay. Great. Understood. On the pricing perspective, you guys have referenced that there's a slide in this deck with regard to VAPS modular delivery rates up 1% year-over-year, storage up 16% year-over-year. I'm curious, could you share that what the metric would be for the core rate? And then kind of the bigger picture is, how is pricing integrity for both the modular and the storage categories right now?

Tim Boswell

Okay. Well, let me start just -- I'm not sure I understood the question around core rate as you related to VAPS, Scott, so maybe we come back to that one if I don't cover it.

We saw storage average monthly rental rate up 9.5% year-over-year. And you saw that increase modestly sequentially from Q2 to Q3, which is exactly what we expected coming out of the Q2 call. If you break that down and take the climate controlled storage out of that, traditional storage AMR was up about 1% year-over-year.

And then you have the VAPS contribution on top of that. So we continue to see stability in traditional storage rates, although that is an area where spot rates have not moved to the degree we would have budgeted this time last year sequentially through the course of the year.

But overall, the average billing rate remains up 1% year-over-year for storage, excluding VAPS. Cold storage, again, is going to become a bigger mix of the portfolio. That's more of a volume story right now with unit on rent up about 15% year-over-year versus where it would have been in September last year.

Not a ton of AMR change through the course of this year, but we are seeing spot rates move up meaningfully in cold, which is pretty encouraging going into in 2025. And then modular, it's kind of a continuation of the story unit rental rates, excluding VAPS, were up about 7% year-over-year in the quarter, average value-added products per unit on rent up about 3% year-over-year. And yes, you correctly called out that, that delivered rate in modular also increased about 1% year-over-year in the quarter. It was a little stronger than that if you exclude some of the third-party services, which we're deemphasizing.

Scott Schneeberger - Oppenheimer & Co. Inc.

Yes. Yes, you kind of got it on. I was really looking to get into spot rate pricing on the 2 categories. That's the way I confused it with the VAPS mention, but I was looking for just core in isolation as opposed to VAPS for the trailing 13 weeks to get the spot. So yes, you covered it a bit there. Just wanted to get a sense of directionally, how is spot trending in each of the 2 categories, modular in particular, with it? And anything you'd like to add or if you feel you covered it, that's fine.

Tim Boswell

Yes. In modular, it's trending sequentially flat, right? We haven't seen a ton of movement there through the course of the year. There are some puts and takes as you kind of break it down by product category, not surprisingly, a little stronger in the complex fleet, as you might expect, a little weaker in ground level offices, just as an example. But overall, the mix of the portfolio is sequentially flat going into next year from a spot standpoint.

Operator

Tim Mulrooney with William Blair.

Luke McFadden - William Blair & Company L.L.C.

This is Luke McFadden on for Tim Mulrooney. Maybe one just to start on the modular side of the business. With interest rates coming down, how are you thinking about the more transactional units on the modular side? Is it your expectation that we should start to see this coming back at some point next year? Or do we need to see a few more rate cuts before we really start to see improvement here? Just curious around kind of the lag component as we think about further rate cuts to come.

Tim Boswell

This is Tim. I'll start, and Brad, you can add your perspective. I think certainty is as important as the magnitude of the cuts. So cuts maybe stimulate projects that otherwise didn't meet certain economic hurdles. Certainty simply allows the commercial real estate market to adjust, which maybe takes a bit longer. But either way, it can only be a net benefit to the volume equation in our business, especially among the more transactional product lines.

And it's just black and white when you look at the relative performance of the different product lines within modular, we're actually up slightly year-over-year in terms of complex unit on rent and a lot of that is coming from the FLEX product as we as we populate the market with that. And then it's just tougher on the transactional single wides and GLOs. And that contrast has been pretty black and white all year long.

Luke McFadden - William Blair & Company L.L.C.

Understood. That's helpful. And then maybe one just kind of on the storage side of the business. I think last quarter, you outlined an expectation for sequential step-up of around 10,000 storage units from 3Q to 4Q, just based on kind of more normalized trends in retail and seasonal, but it seems like maybe from some of the commentary in the slide deck, seeing a bit more pressure on the retail side versus previous expectations. So just curious how we should think about any seasonal retail dynamics on the storage side of the business heading into the fourth quarter?

Tim Boswell

The retail side is shaping up very much like we expected coming out of Q2. So as I said a minute ago, yes, I expect we'll probably end October with near 130,000 storage units on rent relative to the 122,700 that you see on average on rent for the quarter. So we're absolutely seeing that build across both modular and storage. If you just contrast kind of our outlook today to where it was back in Q2. We've reduced our overall delivery expectations by about 10% across all product lines. But the retail component is actually performing pretty much in line with what we expected coming out of Q2.

Operator

One moment for our next question, and that will come from the line of Steven Ramsey with Thompson Research Group.

Steven Ramsey - Thompson Research Group, LLC

Was thinking about 2022 being a great year of nonres activity. You're entering this time frame, if you look at the average 3-year lease duration where more of those units start coming back to you against this low starts environment. I guess, do you look at this as a double headwind or do you see it differently, just thinking about where units were in 2022 to current?

Tim Boswell

Steve, this is Tim. It's a good question. And it's really the reverse is true to an extent because as the unit on rent portfolio comes down in size, the volume of returns tends to come down proportionately. And just to give you some round numbers: Total returns in modular, if I look back to 2022, would have been just north of 70,000 units on rent and forecast for this year is probably just over 60,000 units on rent.

So we've seen the return side of the equation come down, and it's even more pronounced actually on the storage side of the business. I think we talked about this a little bit last quarter. That tends to be a kind of a dynamic in the portfolio that actually mitigates some of the new demand headwinds because you get a little bit of benefit from that return volume just simply because the unit on rent for portfolio is a bit smaller.

Steven Ramsey - Thompson Research Group, LLC

Okay. That's helpful. And then I wanted to think about with volume environment because of starts bottoming more slowly than you thought but then your commercial progress to improve cross-selling with the wider portfolio that you have, I'm curious how you think about that playing out and what benefits come first as you roll through these initiatives?

Brad Soultz

Yes, this is Brad. I'll start. And I mentioned in my prepared remarks the year behind the scenes, we combined the 2 legacy ops and sales teams and unveiled a complete portfolio of digital demand optimization, sales effectiveness, tools, customer portals, et cetera.

So I think everything is in place now. And it's as basic as we don't need 2 different people selling 2 different products. We've got 1 team selling everything. And now they have all the tools in place. And the majority of those digital tools really went into effect in the third quarter. So it gives us, again, more excitement as we look further afield into 2025 and beyond that we can really gain some traction with the cross-sell not only of modular and storage but into these adjacencies and then from the adjacencies back into core.

Operator

Andrew Wittmann with Baird.

Andrew Wittmann - Robert W. Baird & Co. Incorporated

Great. Yeah, I wanted to, I guess, dig into the volumes a little bit differently. I guess, looking at the activation, last quarter, I guess, you guys were saying that your activations were -- I think you were saying they were relatively flat on a year-over-year basis. And this quarter, that your modular activations in the slide were down 7% in storage, they were down 10%.

So if activations last quarter were flat and you saw the volumes weaker, a little bit kind of stabilizing sequentially, but activations this quarter were softer, why aren't -- why isn't it that volumes are going to be even weaker next quarter? I guess, I'm not understanding, I thought maybe you could help clarify that.

Brad Soultz

Yeah, Andy, this is Brad. We'll let Tim jump in a bit. But you are correct, through the first quarter and the second quarter despite nonresi square foots being down year-over-year, modular activations were trending basically flat to prior year. That was basically a tale of 2 worlds. You had mega projects driving outsized demand primarily for our larger complex fleet, which was fully mitigating the drag, if you will, with the smaller construction projects. In the third quarter, we still continue to see that effect. We just didn't have full mitigation, right? And we touched on a number of drivers with respect to that.

Tim Boswell

Yes. I'm not sure I have a lot more to add, Andy, other than in the modular business. I think we have pulled back the return volume assumption slightly. But certainly, relative to the last outlook, our end of year unit on rent expectation is lower across both modular and storage. So I think I said in -- when I was talking about 2025 and kind of when this bottoming plays out, it's definitely pushed to the right relative to where we were forecasting back in July.

Andrew Wittmann - Robert W. Baird & Co. Incorporated

Got it. Maybe the better way to ask this question or a different way to ask the question is, do you think that the 3% decline in average units on rent in the third quarter improves in the fourth quarter or does it maybe decline a little bit more in the fourth quarter?

Tim Boswell

On modular, certainly on storage, I think there's the potential for that deficit to continue to close and we're probably around that 3% deficit in modular, Andy, where we're sitting right now.

Andrew Wittmann - Robert W. Baird & Co. Incorporated

Okay. So stabilizing that. And then I just wanted a clarification on some of the cost actions spread that you talked about. Last quarter, you talked about $40 million of annualized run rate, so something like $10 million a quarter. Was the $20 million that you guys are talking about relative to this quarter? Was that in the quarter, $20 million or is that also an annualized number, so we should think of it as 40 plus 20 equals 60 on an annualized basis? Sorry, I just wanted a clarification on that one.

Tim Boswell

Yes. It was $20 million lower variable costs relative to what we would have planned in the July time frame, Andy. So that's -- and that is demand driven, right? So it is probably not appropriate to annualize that and say, Hey, we've got a $80 million variable cost tailwind going into 2025.

Now we would gladly put that back into play to support volumes in the business. But if we pulled 10-ish percent of our volume or activation volume out of the forecast as we progress through the quarter, $20 million of variable cost goes with that in the quarter, right?

And that's one of the reasons you actually see margins going up despite an operating leverage headwind in the business. We absolutely saw the flow-through of the $40 million annualized takeout that we did in Q2, and you see that impact in kind of the SG&A line primarily that at least the SG&A that flows into our adjusted EBITDA calc, the $20 million of variable cost is coming out of cost of leasing and supporting the gross profit margin in the business.

Operator

Faiza Alwy with Deutsche Bank.

Faiza Alwy - Deutsche Bank

Yes. So I wanted to clarify on pricing. Can you confirm what the gap is between sort of spot pricing or LTM pricing, both for storage and modular relative to the reported pricing?

Tim Boswell

Yes, Faiza, on modular, it's about a 12% favorable spread. And on storage, it's about flat, but with a growing spread on the cold storage side of the business.

Faiza Alwy - Deutsche Bank

Okay. Understood. And I guess I'm curious, how should we think about your pricing strategies looking ahead into 2025, just in light of those gaps and in light of inflation decelerating?

Tim Boswell

Yes. I wouldn’t say, Faiza, there's any change to our strategy per se here right now, we are actively kind of reimplementing a new pricing technology platform as we go into next year, which I'm very, very excited about and that will have some kind of AI-informed price recommendations that we'll be able to then populate into our quoting system.

We're also concurrently building out a new quote configuration system. And the goal there is to, again, further automate the bundling of not just value-added products, but complementary fleet products. as sales reps are building out proposals for customers. We continue to see the biggest challenge and opportunity as it relates to cross-selling and value-added products is our own behavior, so providing the right technology tools to help that is, I think, a pretty interesting solution, which we're actively working on. And I think both of those programs probably go live in the first half of next year sometime. We're actively doing A/B testing on -- in different parts of the business. One example is in the out-of-term rate increases, which you'll recall on average. The vast majority of our customers retain units longer than they contract them for.

That's one of the reasons we're actually seeing the strength and stability of AMR in the storage business is the out-of-term portion of that. But we're actively testing different inflationary escalators in the out-of-term process, just as one of many different examples we're looking at as we go into next year.

Faiza Alwy - Deutsche Bank

Great. That's really good color. And then just if I can ask on volumes. Just sitting from the outside, we've been looking at ABI and the construction data, like how quickly do you think your -- sort of whether it's activation volumes or generally, units on rent, like how quickly do you think that can recover?

Because I know there's -- typically, we've talked about 12- to 18-month lag to ABI and ABI is still under 50. So give us a sense of when do you -- what do you think of as sort of normal? And what do we need to see from a macro perspective to get there?

Brad Soultz

Faiza, this is Brad, and then Tim can jump in. If you think about just the core underlying markets for both modular and storage, we are in the slowest part of the year seasonally. It's basically November, December, January, February, you'll see slower activity.

So March is when we would expect to see any sequential improvements really and that also coincides with probably the earliest we'll really start to see benefits from the improvement in rates, et cetera. And certainly, I expect we'll have clarity in terms of who's in the White House, a little joke aside there. It is also, as a reminder, second quarter of next year would be when we would start to see retail remodels start to kick back in, which could be a volume driver, if you will, on top of those core markets.

Operator

Angel Castillo with Morgan Stanley.

Angel Castillo - Morgan Stanley

Just wanted to circle back on the AMR spot answer, and I apologize if I misunderstood there. But I thought I heard you say, I guess, 12% on spread between AMR and the latest spot on modular. And if I'm not mistaken, that was kind of 15% to 20% last quarter. Again, lots of earnings today, so I apologize if I misheard the numbers, but just if that is correct, it seems to imply that the spot maybe has come down on the modular side. Can you just clarify that, if that is what is going on? And maybe what's kind of driving that and the confidence in kind of that inflecting?

Tim Boswell

Yes, I think we were at 15% last quarter on modular, and that had been down from 20%. I think last year, I forget the exact periods for that. So there definitely was a contraction of the spread. That's more from older units going back and going out at today's spot than it is any compression that we've seen in spot rates themselves.

I said earlier on the call that modular spot has been sequentially flat through the course of the year with some product mix variation. But extremely stable there. And you're just returning units that were rented 2, 3, 4, 5 years ago and the volume that's going out is going out of today's spot, which has been flat sequentially through the course of the year.

Angel Castillo - Morgan Stanley

Very helpful. And then I just wanted to follow up on maybe some earlier commentary around 2025. I think I heard you say that maybe this non-resi will be bottoming into the first half of '25. And as we think about that combined with maybe some of your conversations around 2025 improvements on demand, can you just maybe talk about the cadence of that? Is the first half going to continue to -- do you kind of expect that to be below kind of the second half dynamic that we're seeing right now, and therefore, some continued contraction if things are still bottoming and it's more of a second half year? Or just what kind of cadence do you -- should we kind of envision from a margin expansion as well as a growth perspective?

Tim Boswell

Yes. It's probably a little early to give you a crystal clear sequential guidance for the year. We're going through our own planning process kind of as we speak. On a year-over-year basis, I think it's probably appropriate to assume that the first half of the year is flatter from a revenue growth standpoint just because you have lost some momentum finishing the year here.

But between a stabilization of markets, the commercial initiatives Brad talked about, some very real progress on our newer product lines. and then pricing and margin, it is -- I think we've got a couple of different recipes with levers that are in our control. that can drive kind of a modest growth year for the year with margin expansion, and we're working on the different scenarios and the different kind of recipes as we speak.

Operator

Manav Patnaik with Barclays.

Ronan Kennedy - Barclays Bank PLC

This is Ronan Kennedy on for Manav. In talking about capital allocation, you referenced consistency in a typical approach, if I may, please have a multiple-faceted question there. Could I please confirm for CapEx, the expected spend from a percentage standpoint on refurbs, organic investment in FLEX, cold storage and clearspan and adjacencies?

And then also from an end market standpoint, I think entry into education was a key commercial benefit of McGrath for diversification and stability, is that type of thing a possibility? On the M&A front, I think it was $164 million in cold storage in clearspan, is this primarily where we should expect M&A to occur has the ability to do larger acquisitions in your legacy assets been somewhat potentially impaired as a result of the FTC review? And then on buybacks, how should we think about the cadence on a quarterly basis? Is there a possibility for some catch-up activity?

Brad Soultz

Well, there's a lot in there. I'll knock 1 off, and then Tim jump in. From a tuck-in pipeline perspective, I think looking back is the right way to think about looking forward. We've deployed a little over $1 billion over the last several years into acquisitions.

About 1/4 of that has been modular. Everything else has been storage with a large majority clearspan and cold storage, so new adjacencies. So we are repriming that pipeline a bit, as I mentioned during my prepared remarks. But I think going forward, I assume we put 25% of the capital back to work to fund maintenance and growth, that will include growth in VAPS and these new adjacencies. And there's -- we expect to still see an ample pipeline for continued deployment into tuck-in M&A and don't feel there are any like undue constraints coming out of the McGrath transaction.

Tim Boswell

Yes, Ronan, if you look at Page 27 in the deck, the right-hand pie chart shows the last 12 months of capital allocation. I'd expect the $231 million of net CapEx to go up a bit.

As we finish out the year, I think Q4 CapEx will be higher this year than it was last year, mostly because of the adjacencies that are growing organically. I think the $164 million of tuck-in volume compresses a bit as we close out the year just because there was a larger platform acquisition in Q4 last year, which will fall off.

But overall, the framework is very much the same. And you can see on LTM basis, adding back the deal costs you've got $500 million that would have been allocated to the repurchase under that scenario. And in terms of the timing and magnitude of repurchases, yes, we take valuation into account, but we also believe that, that is a steady lever that should be deployed consistently over time to compound returns.

Ronan Kennedy - Barclays Bank PLC

That's helpful and I appreciate it. On the -- I think Brad had mentioned election is factoring into timing decisions and there was a joke on clarification on the White House, who will be in the White House. Are you hearing from your customers or have you assessed potential political risks from the implications of a respective red or blue sweep or Trump or Harris administration, potentially impacting onshoring, right-shoring the energy demand that you have seen, I think, more so for the modular business? Have you assessed kind of political risk there?

Tim Boswell

Ronan, this is Tim. I've been on the road a fair amount recently. And what I've heard is more about certainty than it is about a preference 1 way or the other. You've got 2 heavy spenders, I think, on the ticket.

So I don't see a huge change there one way or the other. Maybe the mix of type of government support shifts and market to end market, but we don't really care about that that much. If you get more manufacturing with 1 and a little less green energy. Well, our services don't really change that much depending on where the end market activity is. We just need the activity to be there.

So we're not losing sleep over either outcome, but I think it's been pretty clear and consistent that customers want to know what paradigm they're operating in when they kick off a major project. And in retrospect, I think we may have heard that later than some, just given the sales cycle for us tends to be a little bit shorter, given we're such a small spend item on many of these project sites, but it has been a pretty consistent drumbeat that built during the quarter.

Operator

Philip Ng with Jefferies.

Philip Ng - Jefferies LLC

Tim, appreciate you giving us at least an early framework for 2025. You're calling out modest growth and margin expansion. So that's great. But can you help us unpack how you think about units on rent versus AMR growth for next year? Based on your comments, it sounds like units on rent will likely be down next year, but I just want to get a little more perspective on kind of how do you think about units on rent because it’s been pretty tough to predict.

Tim Boswell

Yes, it has. It will be down to start the year, although, again, not to the same degree it was down to start this year. So a moderating headwind there is still what we see, can't really predict the exact mix of the KPIs that are going to play out through the course of this year, Phil, and like I said earlier, I think we've got a couple of different pathways to deliver the very high-level framework that we're talking about.

We still have a very powerful tailwind in modular AMR. We have good traction across storage VAPS and signs of life in modular VAPS, which we expected to begin inflecting around this time. We have new product offerings. And as Brad said in his remarks, we see the run rates there potentially doubling as we progress through next year, and that's primarily a volume game across some of the newer additions we've introduced to the portfolio. And then you've got margins where I think the track record has been pretty clear.

And as we kind of optimize a lot of the commercial and operational processes here, leveraging all the technology investments that have put in place, I think we've got multiple ways to win on the margin front as we go through 2025. So those are the different levers that we're looking at sitting here today. And the mix of leasing KPIs always ends up being different than you expect in a budgeting process. So our job is to make sure we've got different ways to deliver the result.

Philip Ng - Jefferies LLC

And then, Tim, I know the demand outlook is a little different than you thought, but I think last quarter, based on the cadence you're seeing in the spread, I think you mentioned you're pretty confident that you can deliver, call it, high single-digit, call it, AMR growth in modular. Is that algo little looking different today? And then storage, just given the spread, does that look more flattish? Or you could actually see some growth on AMR looking next year for storage?

Tim Boswell

Yes, we need to see the spot rates on traditional containers pick up from where they are now to begin pulling up the AMR. You're going to get a -- absolutely get a mixed benefit from the growing cold storage population, and value-added products are up, I believe it was 16% year-over-year in the traditional storage category in Q3.

So that's probably the setup for storage and with a 12% spread currently in modular with no further spot rate improvement that probably brings you down into the low mid-single digits, if you just divide that spread by 3, but with upside across value-added products and services. So sitting here right now, I think that's the best visibility we've got.

Operator

I'm showing no further questions in the queue at this time. I would now like to turn the call back over to Mr. Nick Girardi for any closing remarks.

Nick Girardi

Thank you, Sherry. Thank you all for your interest in WillScot. If you have additional questions after today's call, please contact me.

Operator

This concludes today's program. Thank you all for participating. You may now disconnect.