

XPO, Inc.

# Mid 1Q24 Update: Vol and pricing ramp continues; See rising potential; PO to \$137

Reiterate Rating: BUY | PO: 137.00 USD | Price: 123.32 USD

## Volume trending ahead of expectations w/ February ramp

XPO posted its mid-1Q24 Less-than-Truckload (LTL) update, with February Tons/Day up 3.5% y-y, accelerating from -1.1% in January. The company highlighted that volumes grew 4.3% sequentially from Jan to Feb, outpacing normal seasonality of +1.2%. It also saw strong momentum in the last 2 weeks of February, noting that volume growth was above its prior expectations. XPO's Jan-Feb tonnage combo average was +1.2%, compared to our prior 1Q24 target of +1.7% (now +3%). Its acceleration in February volume growth was led by a 5.8% year-year increase in LTL Shipments/Day (from +1.4% in January) offsetting a 2.2% year-year decline in LTL Weight/Shipment (from -2.5% in January). For 1QTD, Shipments/Day and Weight/Day are up 3.6% y-y (we target +5.2%) and down 2.4% y-y (we target -2.1%), respectively. The company reiterated its focus on achieving double digit ex-fuel yield growth in 1Q (we target +10.9% Rev/Hundredweight) through ramping its local sales channel and converting service gains to price.

## See potential for returns ramp given cost and mix focus

Given its better than anticipated volumes and strong pricing momentum, we expect XPO to achieve a 1Q24 LTL Operating Ratio of 86.6%, a 10 bps sequential deterioration from 4Q23, outperforming its historical seasonality of a 40 bps deterioration. March typically represents 50% of its 1Q24 volumes but face easier comparisons (-5% in 2023), which should offset two less working days given Easter timing. Increased mix of local sales channels (up double-digits in 4Q23 for the 3<sup>rd</sup> consec quarter), lower usage of Purchased Transportation, as well as its 9.0% 4Q contract renewal rate should all aid in improved returns. Although its QTD volume growth lags Saia's +7.2% (yet better than Old Dominion -3.0%), we see idiosyncratic self-help opportunities driving margin gains above peers. It aims to ramp 23-24 facilities it acquired in the Yellow auction by year-end, which may accelerate tonnage growth into 2H24 as it grows into its added capacity.

## PO to \$137; Remains one of top transport picks

We reiterate our Buy on XPO's shares and increase our PO to \$137 (from \$132) on 37x our '24e EPS (from 36x) given better-than-expected metrics. The company is set to deliver outsized earnings growth over the next few years (30% CAGR '24e-'26e) given its moves to ramp its network and reduce costs. We increase our 2024/2025 EPS 1% each, to \$3.70/\$5.10, from \$3.65/\$5.05, and could see additional margin upside (it targets 150-250 bps improvement in 2024, noting it could top that, we're at 200 bps).

Estimates (Dec) (US\$)	2022A	2023A	2024E	2025E	2026E
EPS	3.53	2.93	3.70	5.10	6.35
GAAP EPS	1.58	1.63	2.94	4.34	5.59
EPS Change (YoY)	82.0%	-17.0%	26.3%	37.8%	24.5%
Consensus EPS (Bloomberg)			3.47	4.78	5.85
DPS	0	0	0	0	0
Valuation (Dec)					
P/E	34.9x	42.1x	33.3x	24.2x	19.4x
GAAP P/E	78.1x	75.7x	41.9x	28.4x	22.1x
EV / EBITDA*	28.7x	28.6x	21.7x	17.7x	15.2x
Free Cash Flow Yield*	5.3%	-5.7%	0.7%	2.2%	3.4%

\* For full definitions of *IQmethod™* measures, see page 5.

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05 March 2024

### Equity

#### Key Changes

(US\$)	Previous	Current
Price Obj.	132.00	137.00
2024E Rev (m)	8,423.6	8,470.6
2025E Rev (m)	8,889.6	8,931.7
2026E Rev (m)	9,407.5	9,455.5
2024E EPS	3.65	3.70
2025E EPS	5.05	5.10
2026E EPS	6.30	6.35

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### Stock Data

Price	123.32 USD
Price Objective	137.00 USD
Date Established	5-Mar-2024
Investment Opinion	C-1-9
52-Week Range	29.02 USD - 125.18 USD
Mrkt Val (mn) / Shares Out (mn)	14,811 USD / 120.1
Free Float	96.5%
Average Daily Value (mn)	189.69 USD
BofA Ticker / Exchange	XPO / NYS
Bloomberg / Reuters	XPO US / XPO.N
ROE (2024E)	29.9%
Net Dbt to Eqty (Dec-2023A)	236.3%
ESGMeter™	Medium

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# iQprofile<sup>SM</sup> XPO, Inc.

## iQmethod<sup>SM</sup> – Bus Performance\*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Return on Capital Employed	8.5%	8.6%	9.8%	11.5%	26.5%
Return on Equity	38.0%	30.4%	29.9%	31.1%	68.3%
Operating Margin	7.8%	7.8%	9.5%	11.3%	12.5%
Free Cash Flow	785	(839)	103	326	510

## iQmethod<sup>SM</sup> – Quality of Earnings\*

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash Realization Ratio	3.2x	2.0x	1.9x	1.7x	1.6x
Asset Replacement Ratio	1.3x	3.5x	1.7x	1.6x	1.5x
Tax Rate	22.0%	23.1%	23.5%	24.0%	24.0%
Net Debt-to-Equity Ratio	204.7%	236.3%	138.0%	95.5%	NA
Interest Cover	4.5x	3.6x	3.3x	4.5x	5.9x

## Income Statement Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Sales	7,718	7,744	8,471	8,932	9,455
% Change	7.2%	0.3%	9.4%	5.4%	5.9%
Gross Profit	NA	NA	NA	NA	NA
% Change	NA	NA	NA	NA	NA
EBITDA	661	663	873	1,075	1,249
% Change	-26.4%	0.3%	31.7%	23.1%	16.2%
Net Interest & Other Income	(80)	(153)	(221)	(203)	(179)
<b>Net Income (Adjusted)</b>	<b>409</b>	<b>346</b>	<b>446</b>	<b>613</b>	<b>759</b>
<b>% Change</b>	<b>84.1%</b>	<b>-15.3%</b>	<b>28.8%</b>	<b>37.5%</b>	<b>23.9%</b>

## Free Cash Flow Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Net Income from Cont Operations (GAAP)	408	346	446	613	759
Depreciation & Amortization	392	432	434	460	492
Change in Working Capital	1	(99)	(36)	(13)	(13)
Deferred Taxation Charge	80	31	0	0	0
Other Adjustments, Net	425	(16)	(3)	(3)	(3)
Capital Expenditure	(521)	(1,533)	(738)	(731)	(725)
<b>Free Cash Flow</b>	<b>785</b>	<b>-839</b>	<b>103</b>	<b>326</b>	<b>510</b>
<b>% Change</b>	<b>128.9%</b>	<b>NM</b>	<b>NM</b>	<b>217.8%</b>	<b>56.6%</b>
Share / Issue Repurchase	0	0	0	(100)	(100)
Cost of Dividends Paid	0	0	0	0	0
Change in Debt	0	2,891	0	0	0

## Balance Sheet Data (Dec)

(US\$ Millions)	2022A	2023A	2024E	2025E	2026E
Cash & Equivalents	460	412	688	595	0
Trade Receivables	954	973	1,058	1,086	0
Other Current Assets	216	208	208	208	0
Property, Plant & Equipment	1,832	3,075	3,359	3,619	0
Other Non-Current Assets	2,807	2,824	2,824	2,824	0
<b>Total Assets</b>	<b>6,269</b>	<b>7,492</b>	<b>8,137</b>	<b>8,332</b>	<b>0</b>
Short-Term Debt	59	69	69	69	0
Other Current Liabilities	1,448	1,521	1,571	1,586	0
Long-Term Debt	2,473	3,335	2,980	2,650	0
Other Non-Current Liabilities	1,277	1,301	1,806	1,803	0
<b>Total Liabilities</b>	<b>5,257</b>	<b>6,226</b>	<b>6,426</b>	<b>6,108</b>	<b>0</b>
<b>Total Equity</b>	<b>1,012</b>	<b>1,266</b>	<b>1,712</b>	<b>2,224</b>	<b>0</b>
<b>Total Equity &amp; Liabilities</b>	<b>6,269</b>	<b>7,492</b>	<b>8,137</b>	<b>8,332</b>	<b>0</b>

\* For full definitions of iQmethod<sup>SM</sup> measures, see page 5.

## Company Sector

Road Transport/Trucking

## Company Description

XPO is a pure play LTL carrier along with a European Transport segment (it previously spun off RXO, which included its Truck Brokerage, Last Mile, and Other brokerage operations, GXO, its warehousing and logistics segment, and sold its Intermodal operations, it has noted it continues to plan to sell its Europe operations). It has over 50,000 customers and is headquartered in Greenwich, CT.

## Investment Rationale

XPO is a pure play LTL carrier (the former Con-way), along with a European Transport segment (non-core, which it is expected to sell in the future). Given the benefits to LTL from ecommerce growth, and XPO's focus to improve ops, it should unleash earnings gain potential and trapped value. We rate XPO Buy given its progress in its Network 2.0 growth strategy, which should allow it to close a margin gap to leading industry operators.

## Stock Data

Average Daily Volume 1,547,287

## Quarterly Earnings Estimates

	2023	2024
Q1	0.56A	0.67E
Q2	0.71A	1.07E
Q3	0.88A	1.06E
Q4	0.77A	0.89E



## Price objective basis & risk

### XPO, Inc. (XPO)

Our \$137 price objective is based on a 37x P/E multiple on its 2024e EPS, above the upper end of peer range at 8x-24x, as we look for it to close the premium gap to best-in-class peers as it executes on its Network 2.0 growth plan and its purchase of Yellow real estate.

Downside risks to our price objective are a downturn in the global economy, which could reduce volume and pressure margins, while also potentially having a disproportionate impact on XPO's earnings given its leveraged capital structure. Long term inability to secure a sale of its Europe operation may also be a downside risk to our price objective. Its inability to improve cargo claims, insource linehaul, obtain tractors/trailers at pace it desires, and failure to improve pricing on its improved service levels would be a downside risk to targets/valuation. A potential turnaround at Yellow could lead to increased freight capacity and negative pricing pressures.

## Analyst Certification

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### US - Transportation Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Canadian Pacific Kansas City Ltd	CP	CP US	Ken Hoexter
	CSX Corporation	CSX	CSX US	Ken Hoexter
	FedEx Corp.	FDX	FDX US	Ken Hoexter
	J.B. Hunt Transport Services	JBHT	JBHT US	Ken Hoexter
	Kirby Corp	KEX	KEX US	Ken Hoexter
	Knight-Swift Transportation Holdings Inc	KNX	KNX US	Ken Hoexter
	Old Dominion Freight Line	ODFL	ODFL US	Ken Hoexter
	Saia Inc.	SAIA	SAIA US	Ken Hoexter
	Teekay Tankers Limited	TNK	TNK US	Ken Hoexter
	Union Pacific	UNP	UNP US	Ken Hoexter
	Wabtec Corp.	WAB	WAB US	Ken Hoexter
	XPO, Inc.	XPO	XPO US	Ken Hoexter
<b>NEUTRAL</b>				
	Canadian National	CNI	CNI US	Ken Hoexter
	RXO, Inc.	RXO	RXO US	Ken Hoexter
	Schneider National	SNDR	SNDR US	Ken Hoexter
	Scorpio Tankers Inc.	STNG	STNG US	Ken Hoexter
	TFI International	TFII	TFII US	Ken Hoexter
	TFI International	YTFII	TFII CN	Ken Hoexter
	UPS	UPS	UPS US	Ken Hoexter
<b>UNDERPERFORM</b>				
	ArcBest Corporation	ARCB	ARCB US	Ken Hoexter
	C.H. Robinson	CHRW	CHRW US	Ken Hoexter
	The Greenbrier Companies	GBX	GBX US	Ken Hoexter
	Werner Enterprises	WERN	WERN US	Ken Hoexter
	World Kinect	WKC	WKC US	Ken Hoexter
<b>RSTR</b>				
	Norfolk Southern	NSC	NSC US	Ken Hoexter

## iQmethod<sup>SM</sup> Measures Definitions

### Business Performance

Return On Capital Employed

Return On Equity

Operating Margin

Earnings Growth

Free Cash Flow

### Quality of Earnings

Cash Realization Ratio

Asset Replacement Ratio

Tax Rate

Net Debt-To-Equity Ratio

Interest Cover

### Valuation Toolkit

Price / Earnings Ratio

Price / Book Value

Dividend Yield

Free Cash Flow Yield

Enterprise Value / Sales

EV / EBITDA

### Numerator

NOPAT = (EBIT + Interest Income) × (1 – Tax Rate) + Goodwill Amortization

Net Income

Operating Profit

Expected 5 Year CAGR From Latest Actual

Cash Flow From Operations – Total Capex

### Numerator

Cash Flow From Operations

Capex

Tax Charge

Net Debt = Total Debt – Cash &amp; Equivalents

EBIT

### Numerator

Current Share Price

Current Share Price

Annualised Declared Cash Dividend

Cash Flow From Operations – Total Capex

EV = Current Share Price × Current Shares + Minority Equity + Net Debt +

Other LT Liabilities

Enterprise Value

### Denominator

Total Assets – Current Liabilities + ST Debt + Accumulated Goodwill

Amortization

Shareholders' Equity

Sales

N/A

N/A

### Denominator

Net Income

Depreciation

Pre-Tax Income

Total Equity

Interest Expense

### Denominator

Diluted Earnings Per Share (Basis As Specified)

Shareholders' Equity / Current Basic Shares

Current Share Price

Market Cap = Current Share Price × Current Basic Shares

Sales

Basic EBIT + Depreciation + Amortization

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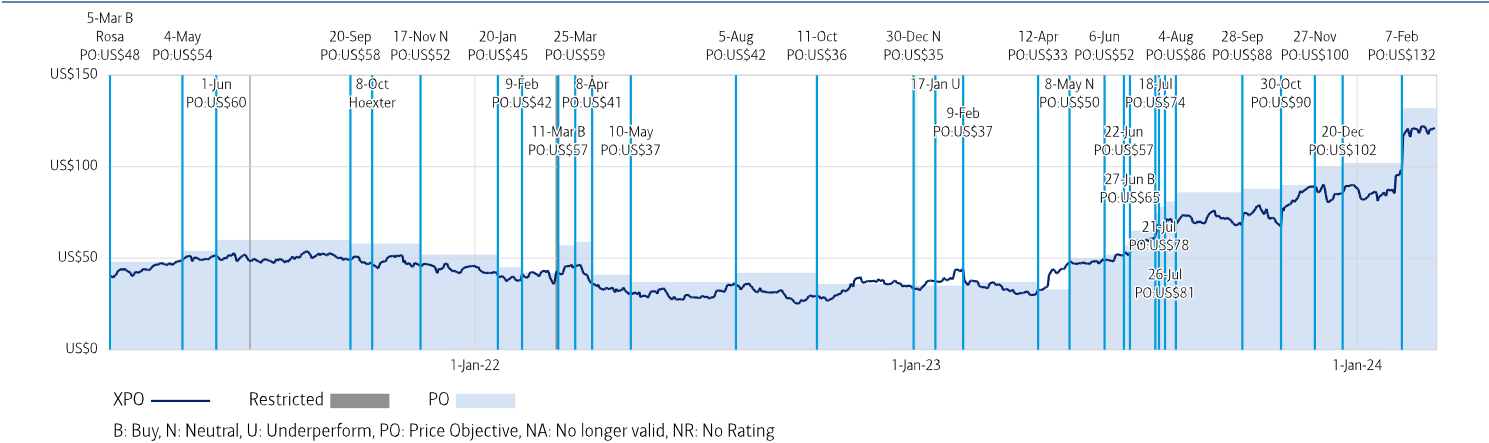
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XPO, Inc. (XPO) Price Chart



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Equity Investment Rating Distribution: Transport/Infrastructure Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	67	50.38%	Buy	44	65.67%
Hold	31	23.31%	Hold	13	41.94%
Sell	35	26.32%	Sell	17	48.57%

Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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