Bernstein's Annual Strategic Decisions Conference
Interview with Brad Jacobs and Matt Fassler of XPO Logistics
Conducted by David Vernon of Bernstein
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1. **David Vernon, Bernstein**: Good morning, everyone. My name is David Vernon. I'm Bernstein's transportation and airlines analyst. Welcome to our 36th Annual Strategic Decisions Conference. We're privileged to be joined by Brad Jacobs, CEO of XPO Logistics, and Matt Fassler, Chief Strategy Officer, who is also on the line. We're going to go through a little bit of Q&A with Brad. He's going to kick it off with a few prepared remarks on the state of the business.

   With that, we'll turn over the mic to Brad Jacobs of XPO Logistics to give us a sense of the state of the business and how it's faring through the early stages of the crisis we're all dealing with.

2. **Brad Jacobs, XPO**: Thank you, David. We've adapted very quickly. The majority of our people are at work performing essential services. We've got close to 100,000 employees in 30 different countries, and fewer than 10,000 are working from home. The rest have been going to the 800 logistics warehouses we operate, and driving the trucks and running the cross-docks in our LTL business. We're the third-largest LTL provider in the United States. We're the second-biggest contract logistics provider worldwide. Our brokerage business, which is #2 globally, is being run all from home using our technology. So, the business has been up and running well.

   Don't get me wrong though, the pandemic hit us just as hard as it hit everybody else. Volumes were way down and they're still down. But, they're up from the bottom — in Europe, they're up significantly from the bottom. Europe has definitely bounced back more than we have in the United States, and by a significant amount. If you look at the trough — and you can measure that in many different ways — in Europe we're seeing volumes anywhere from a third to two-thirds up from the bottom. Even though we're not back to where we were pre-COVID, we're definitely solidly up and to the right. That's especially true in France, followed by Spain, followed by the UK.

   Some of our customers and managers in Europe are very upbeat about the recovery. Some think they're going to get back to nearly normal levels within two to three months. Here in the United States, things have gotten better, but they're still bad. We're nowhere near a third to two thirds up from the trough, in terms of the same kind of metrics I mentioned for Europe. But it's up from the trough. The next few weeks are going to be very telling. We're going to be watching the numbers closely to see if we have a real recovery going on here or if there's something holding back the US that we're not quite understanding yet.

After the pandemic is behind us, we'll emerge very strongly. One reason I say that is our outsized presence in e-commerce. That's a business that was already growing fast and is going to keep growing even more. Reverse logistics is the fastest-growing component of e-commerce — we manage almost 200 million units of returned merchandise a year. Whether that's telephones or whether that's sneakers, we're big in reverse logistics. We're also big in omnichannel retail logistics. And our XPO Direct shared distribution platform has got a lot of wind at its back now. So, there are a lot of positive things that will make us grow even faster post-pandemic, and I'm looking forward to getting past this.

3. **David Vernon, Bernstein**: As you think about managing through, obviously you guys are a logistics provider, so the absolute economic activity is going to drive the demand for some of your services. How should we think about the earnings resiliency across the different XPO segments in light of lower volumes? Is this a situation where you'll be able to quickly adjust the cost structure down with the volume? Or, should we be expecting some deleveraging in parts of the business? How can you help investors think through the earnings sensitivity to this shock?

4. **Brad Jacobs, XPO**: About 23% of our costs are fixed and about 77% are variable. The two biggest chunks of the variable costs are labor, at about $6.5 billion annually, and purchased transportation, which varies with the market, but is several billion dollars.

   With labor, fortunately, we had already invested in developing a proprietary labor management tool that we named XPO Smart. We pioneered it in our logistics business, where it saved upwards of 5% in labor costs almost immediately. Next, we deployed it in our LTL business and we're seeing similar results there. We're just so fortunate that we have that tool in hand. We didn't realize how invaluable XPO Smart would prove to be in terms of right-sizing the labor force in such an efficient way.

   With purchased transportation, like many things going on in our company, that's going through a process of automation, meaning it's being done more by computers than by humans. It's being done more accurately, and it takes elasticity into consideration. So, overall, we've done a very good job at managing our biggest costs, labor and purchased transportation. This is not going to be our best quarter in the history of the company. I don't think it's going to be the best quarter for any transportation and logistics company, or for most companies in general. But it could have been a lot worse if we weren't as well-prepared to deal with change as we are.

5. **David Vernon, Bernstein**: As you think about the different parts of the business — maybe separating out contract logistics from transportation — is the leverage you'd expect to see different in any appreciable way? I know the aggregate data points, the 23% fixed and 77% variable. How would you think about that differently by segment?

6. **Brad Jacobs, XPO**: In contract logistics, the business is just what it says, contractual. Our contracts usually last five years. It's a much more stable, predictable, boring-in-a-good-way business than the transportation business. Contract logistics is doing better than transportation in the current environment because there's less pressure on the top line, and because the structure of our contracts helps our bottom line. By contrast, in transportation, volumes go up and down quite a bit based on GDP. That said, we'll do better than the market in most of the businesses that we're in, because we have leadership positions in them and we're very tech-enabled.

7. **David Vernon, Bernstein**: One high-level question I want to ask you is: as you're thinking about moving the company beyond the pandemic, as you're sitting with your leadership team, has anything shifted in the way you're thinking about the business as a result of this pandemic? Anything with respect to either cost take-out potential or investment levels? More work-from-home? Has anything changed as you're thinking about your approach to cost management at investment levels post-pandemic?

8. **Brad Jacobs, XPO**: The majority of our work will not be work-from-home, because you can't drive a truck from home and you can't run a warehouse at home. You can do the brokerage part from home, and more and more of that will happen. Although, in our surveys, it's very interesting: We find that the younger people in our organization want to work in a physical workplace. The older people, forty-five and above, want to work from home. We see this repeated all around geographies, all around business units — go figure. That seems to be a mega-trend: people's age as a factor in whether they want to come back to work in business settings.

   Bigger picture, how do you run this business five or 10 years from now more efficiently through automation? One way is by creating the warehouse of the future, which we're doing through our 15-year joint venture with Nestlé in the UK. That's where we're creating *the* warehouse of the future. And every OEM for any type of robotics or any type of automation in a warehouse tends to pitch to us. They want to hitch their wagon to our star, because it's a very high-profile project. It will show what can be done in running a contract logistics facility of the future in terms of efficiency, productivity, safety and the morale of the people who remain in the facility.

9. **David Vernon, Bernstein**: I definitely want to dig into the automation issue and how that works in contract logistics. But, before we get into that, I want to talk a little bit more about the high-level picture. About seven or eight years ago, you had reached out to me as you were starting to get involved in XPO Logistics. You wanted to talk about the market and let us know on the sell side that you were out there. I think the original vision was rolling up non-asset-based logistics. Then it seemed like you shifted to broadening the service components, with trucking in Europe and the LTL network in the US. Then, right before the crisis, it seemed like you were going to shift again, a little bit, around narrowing the focus of the business. Can you give me a sense, or just help investors think about where your head is now in terms of where you want to take XPO

Logistics? Things change. You learn more about the business as you're coming into it. You guys have done a great job at this. I'm just trying to get a sense for how you're thinking about the future. Diversification? Focus? Breadth? Depth? Additional service capabilities? How should investors be thinking about this?

10. **Brad Jacobs, XPO:** The strategy since the beginning of the company is the same strategy we have today. In broad terms, it's to create dramatic shareholder value. How about that for a novel thought? The purpose of a management team is to create demonstrable value for the shareholders who have given them their money and want to get a return. We consider creating shareholder value our prime mission in life. By the way, that's not totally surprising, since about a fifth of the company is owned by management and directors, so we're very shareholder-focused. That said, we're mindful of the value we create by treating our other stakeholders — employees, communities, vendors, the environment, etc. — with maximum respect.

Now, the narrower remit we've had — and we've had this one from the beginning, too — is what do we do? What is our mission? Our mission is to help customers move goods through their supply chain in the most efficient way, and always within that framework of our over-arching goal to create massive long-term shareholder value.

We were the seventh best-performing stock of the Fortune 500 of the last decade, and our goal is to beat that in the next decade. I think we're starting this decade with a lot of wind to our back because of the decisions we've made over the last 10 years.

The way we can beat our performance of the last decade is by staying true to our discipline in how we allocate capital. As senior management, we consider our job to be to take the finite capital we have and make sure we get a return that very much exceeds our cost of capital. What's a rational, objective, clinical comparison of what it will look like if we put this money into capex? How soon are we going to get our money back? How long will that stream keep going on? What's the risk involved? That's different from M&A. If we buy something, what's the plan to integrate that? To get synergies? To get cost savings? To cross-sell? To apply our technology? To dramatically improve the profitability of that company within a short period of time?

Outsourcing, in our view, is increasing. It's been the prime driver of growth in our industry for the past decade and it's only going to accelerate moving forward. We hear it all the time from customers who want to de-risk their supply chains, and who want to offload their supply chain to a company like XPO that spends hundreds of millions of dollars a year on technology, has the right logisticians in place and has access to global capacity. If you take just the services we provide and nothing else, depending on exactly how you define it, the addressable market is over $1 trillion. So even at $15 or $20 billion revenue, we only have 1.5% to 2% share of the market. There's also the various sales and marketing initiatives that we have going, in order to penetrate the market organically.

We generate lots of cash. Even in this lousy environment, we're going to generate hundreds of millions of dollars of free cash flow this year. Do we just take that cash and pay down our net debt and assume that for every dollar of debt we pay down we'll get a dollar of equity creation? Maybe we'd get a higher multiple as a result of bringing down the leverage? We look at the different alternatives and we're opportunistic, we're rational and objective within the broader parameters of what we're trying to accomplish.

11. **David Vernon, Bernstein:** I think one of the most interesting things about your approach to this is you haven't been constrained by the traditional sort of 3PL orthodoxy of asset ownership vs. non-asset ownership. I guess what I'm trying to really understand, though, is as you think about the business as it exists today — fairly broad, maybe not as deep in areas like international freight forwarding — if investors were to start looking at the stock or being involved with the stock, should we be expecting it to continue to broaden? Or, should we be expecting it to come back to this notion of maybe realigning the portfolio to unlock a better valuation multiple, as you were thinking maybe just a few months ago?

12. **Brad Jacobs, XPO:** We will pursue all of our options simultaneously. We'll always be studying capex opportunities. We'll always be understanding M&A opportunities. We'll always be understanding all the different types of M&A opportunities: going deeper into verticals we're already in; expanding our verticals; staying in our geography; going to new places; buying back our stock; doing divestitures if it makes sense. It's all about returning the shareholder value to our shareholders. It's the prime mission that we have. If we're going to be criticized for being opportunistic in how we became the 7th best-performing Fortune 500 stock of the last decade, and hopefully even better this decade, we'll take the criticism, because we're doing very well with our prime mission.

13. **David Vernon, Bernstein:** Should we expect to see more share repurchases in the weeks to come? Could you also give us your thoughts on prudence for the environment of capital allocation and M&A targets you've historically always looked towards? How are you guys thinking about allocating capital? About liquidity?

14. **Brad Jacobs, XPO:** We take allocating capital very seriously and we spend a lot of time on that internally. As a senior management team, our two big jobs are to allocate time and capital. We're always debating how accretive our decisions will be in the medium and long-term, whether it's to buy back our stock, to do M&A, to invest in capex (particularly technology) or to just pay down debt. Those are our four big categories of choices for how we can spend our money. The answer is going to be different depending on the time and circumstances. We keep all those options on the table and close none of those doors.

With respect to liquidity, we have $2.8 billion of liquidity, including $2.3 billion of cash in the bank and another half a million in various credit lines. From a financial perspective, the company is very strong and well-positioned for when the crisis is over. When that time comes, I think we're going to do really, really well through our outsized exposure to e-commerce with the largest e-fulfilment platform in Europe; through the nearly 200 million units of reverse logistics we manage; through the omnichannel logistics that we do; and through XPO Direct, our proprietary shared distribution network that's helping our customers help their customers.

15. **David Vernon, Bernstein:** As you think about that ability to create value, if you're thinking about adding a service line or adding a component, how does 1+1=3? Where is the operating synergy between these businesses? And particularly, when you think about the history of logistics, a lot of the one-stop-shop entities that have tried and failed in the past have been unable to unlock some of that cross-selling synergy or back-office synergy. How do you think about how 1+1=3 when you put these different service lines together?

16. **Brad Jacobs, XPO:** We looked carefully at 2,000 acquisitions in the last decade and ended up picking 17 to buy. We integrated them very tightly and operated them as a cohesive unit, and grew them dramatically. When we stopped doing acquisitions in 2015, the company was about a $15 billion company. If you fast forward four or five years later, we added $2 billion of revenue to that before the pandemic. Where did that $2 billion come from? It didn't come from M&A, because we didn't do M&A. It came from growth. It came from organic growth. It came, in part, from cross-selling within two of our business units, North American Transportation and European Transportation, and from good old-fashioned sales and marketing.

    We've got a great product, we've got a great service offering. We let our customers know about that and we got more share of their wallet, and also added new customers. More important than adding the $2 billion of revenue is that we grew EBITDA from about $1.1 billion by more than half a billion dollars on top of that in just a few years. The numbers tell the story. We picked good companies to buy. We bought them at good prices. We integrated them well. We stuck to the plan. We executed the plan as it was originated. And the profit and the revenue increased quite substantially. And, not surprisingly, the stock price followed, but it didn't follow enough. The story is complex; it requires a lot of work. We will ultimately get the multiple we deserve. Multiple expansion is one of our goals and we're going to achieve that.

17. **David Vernon, Bernstein:** On this notion of how to get synergies between the businesses, this may be something that I've noticed or even seen from the inside of companies in the past. When you have a non-asset business like freight forwarding, you don't have a lot of asset risk. Then you have an asset-based business, like the LTL trucking business. You know the economic drivers of leverage: the price point you get on the asset side is much more important than the volume you might get in forwarding.

How do you manage that tension when customers come to you and ask you to do more things? Commercially, if the economics of the underlying businesses are different, how do you balance the idea that you want to be big without becoming a discounting engine across the different services?

18. **Brad Jacobs, XPO:** Price is the most important lever to push in almost any business, and certainly our business. There's not a penny of cost associated with price, so every time you put price up a bit, it goes right to pre-tax. Every time you take it down a bit, it takes away from pre-tax. We don't pursue what I think you're referring to — a "bundling" philosophy in sales, where we would give a discount if you use more than one service. It turns out that most of our customers use us for many services, but we don't lead with price in any of our businesses.

    Our business model is to provide a high quality of service and to charge a fair price for that. If you look at the last mile sector in the United States, where we're #1 for heavy goods, we get a complaint from a customer, a claim, in one out of 590 deliveries. It takes 590 deliveries before we get an exception. That's outstanding. Really extraordinary. Our high level of service is what allows us to charge a premium price that the customer is happy to pay, because their consumers that we're delivering to are happy. That's our strategy all along: to deliver the best service, not the cheapest service.

19. **David Vernon, Bernstein:** Maybe if you step back from it, because, being involved in the design and creation of how people move goods, you guys have a perspective on supply chains that's very different than a tactical railroad or just a domestic freight broker. When you are talking to your different customers and the team is talking to different customers, what are the three or four biggest trends that you can identify across these different industry verticals? And can you talk about how you're positioned to take advantage of those trends, or what you need to better take advantage of them?

20. **Brad Jacobs, XPO:** The biggest trend is outsourcing. This has been going up over the last 10 years or so, and now it's going up even more. In my opinion, what we're seeing is customers wanting to de-risk their supply chains. They don't want to go through what they just went through with COVID in the last few months. They want to outsource to people who do this for a living; people who spend hundreds of millions of dollars on technology a year, like we do; people who have logisticians on-staff, PhDs, engineers, people with specialized degrees who really understand supply chains really well. Customers want partners who have the systems in place — and we talked about automation before — to actually run these well-conceived supply chains. So, for all these reasons, I think outsourcing is going to drive more growth going forward. That's going to benefit us. It's going to benefit our competitors, as well. And the outsized exposure we have to e-commerce, that's another big trend. That's bigger than XPO Logistics, but we're a big beneficiary of that e-commerce trend.

Automation everywhere, particularly in the warehouse, is another trend where we lead. We're actually a catalyst for that trend. We can provide a contract logistics service for a customer at a lower price and a higher margin than our non-automated competitors. This is a huge advantage for us, and that gulf is going to widen over time. On the brokerage side of the business, the trend is to execute transactions over the internet rather than on the phone. We pioneered our digital freight marketplace, called XPO Connect, starting in 2012. Digitization is a big growth driver for us and a big trend, and we're right smack in the middle of that. If you look at our truck brokerage numbers for the first quarter, we had 9% more loads with 15% fewer people. So, with a 15% lower headcount, we got 9% more volume. We're automating this process and taking cost out, while providing a better service for our customers. We've been quietly growing the digital freight marketplace for years, and doing so very profitably.

The other trend I would mention is something that we developed in response to customer requests: our XPO Direct product. It's a shared distribution network of warehouses and hubs across the US. Instead of storing their own goods and taking a long time to deliver them, our customers can disburse their inventory across the country through XPO Direct and reduce their costs. We do the fulfillment in a much faster timeframe and with a much lower inventory carrying cost. That's an idea whose time has come.

21. **David Vernon Bernstein:** One of the things that I didn't hear is something that pops up from time to time: regionalization of supply chains. Maybe moving away from a world of continuous offshoring toward Asia and toward more regional manufacturing and regional value-add. What's your perspective on that? Is it reasonable to expect that transport regionalization is real? Or is that something that could happen naturally over time but probably doesn't get accelerated too much in this period?

22. **Brad Jacobs, XPO:** It's definitely going to go through an acceleration spurt right now, and it's going to be on a couple levels. Even before the whole COVID thing, companies didn't want to have such a high percentage of their supply chains leveraged to China, because the relationship got really poor with the tariffs. So, you saw migration from China to places like Vietnam, India and Malaysia. That trend is continuing, for sure. It's probably going to accelerate, because the relationship with China and the US hasn't gotten any better. When customers start changing up their supply chains, that's good for us, because we're positioned to help them achieve the right solutions.

The second trend we're seeing is on critical supplies. Any of the producers of PPE — masks, gloves, sanitizers, all the stuff you need in a moment's notice — that's going to get stockpiled here, and it's going to get manufactured here increasingly, as well. That's going to be more regulated, in my opinion. It's going to be mandated by law to do that locally, including many medicines and pharmaceuticals. A large percentage of our pharmaceuticals come from Asia. That's going to change. There will be more manufacturing close to home.

23. **David Vernon, Bernstein:** As you think about the traction you're seeing commercially with the XPO Direct offering, and given how consolidated parts of retail are — whether it's the Walmart marketplace or Shopify or some of these other companies that are coming in to compete for that space — how successful can that be? Do you think there's a lot of runway to expand XPO Direct? Or do you run into a world where you've got Walmart over here and Amazon over here and everybody else is kind of fighting for air underneath that?

24. **Brad Jacobs, XPO:** They're all fighting for air, for sure. The ones who are fighting the hardest are the bricks and mortar ones who didn't fully develop an e-comm strategy for whatever reason. They're accelerating their e-comm now. We're one of their first calls, because with XPO Direct, we can put them within one to two days of 95% of the US population. We can use our predictive analytics to help them figure out where their goods should really be. And not just in three DCs across the country, but in dozens that are much closer to the customer.

    I see a huge amount of potential demand for the shared distribution network we're offering. That's one example of how we're growing in contract logistics, but it's only one. We had several whale contracts coming online this year, big business wins. I mentioned one of them, Nestlé, the 15-year warehouse of the future, which opens up soon after two years of prep.

    We also won, in February, a three-year contract that starts in July with Waitrose, one of the biggest UK grocers. The contract is for about $85 million a year. Obviously, that will help us in the second half of the year. Thirdly, Kuehne + Nagel agreed to sell us three of their verticals in the UK: their e-commerce business, their food and beverage business and their tech business. It's a transaction that's very accretive for us. Those are three verticals that we have a lot of expertise in and that we like a lot.

    There's a lot of wind to our back, regardless of how COVID plays out, from specific self-help things we have.

25. **David Vernon, Bernstein:** Do you talk to investors at all about top-line revenue goals, ex acquisitions and divestitures? Once we re-base to whatever the economy's going to be at, what kind of organic growth rate are you expecting out of the portfolio?

26. **Brad Jacobs, XPO:** Some multiple of GDP. We tend to grow faster than GDP because of our leadership positions, and the trends we'll benefit from, that I talked about earlier. But, until we see the situation stabilize more in Europe and here in the US, it's too early to predict with confidence what the growth rate will be. A few months from now we can answer that question much more thoughtfully.

27. **David Vernon, Bernstein:** One of the other things you guys highlighted in your investment materials is that you have a $700 million to $1 billion profit growth opportunity. Can you walk us through the levers to unlock those gains?

28. **Brad Jacobs, XPO:** Absolutely. We crowd-sourced, through our entire company, the question, "What's your best idea to improve the profitability of the company?" and we got tens and tens of thousands of ideas and we went through every single one of them. We quantified them, we risk-adjusted them, we figured which ones would have the greatest return on capital and the greatest return on time, and we settled on 10 big initiatives. Together, they represent a pool of potential uplift of $700 million to $1 billion of profit. For a company our size, that's massive.

    The biggest lever is something we talked about earlier, which is automating pricing. It's done by advanced algorithms instead of people picking prices out of the air. We have a lot of pricing scientists working on that. Warehouse automation is another lever we talked about.

    And there's labor productivity: what's the right ratio between permanent and temporary workers? What's the right length of shift? We found that LTL volumes weren't coming in in three, eight-hour shifts, so we changed all the shifts — when they start, when they end, how long they last. There are fundamental changes to the way we're running LTL that have massive upside margin improvement opportunities. Although we've taken the margins up by 1,000 basis points in the last four and a half years, we're nowhere near done. We're actually just beginning. We're at the beginning of all the different projects we have going to improve LTL's profitability.

    Purchased transportation is another lever that we talked about before. Within LTL, how do you optimize the pickup and delivery? How do you optimize the dock? How do you optimize the 2.5 million miles a day that we drive on linehaul? It's really process optimization. It's identifying waste and removing it, identifying inefficiencies and getting rid of them. The only two levers that we've not been going full speed ahead on are ones that, because of COVID, don't make sense right now. For example, the consolidation of our shared services in our global back office; there aren't a lot of people in those back offices right now. It's hard to execute on something like that in this pandemic. The other one is procurement, where we have a great team. They've saved us lots of money over the years. We've refocused them almost entirely on PPE to protect our employees, making sure we don't run out of anything anywhere. That's been a full-time job, and not an easy one. Protecting our employees is our first and foremost priority. We've been consumed with doing everything possible to protect our people from the pandemic.

29. **David Vernon, Bernstein:** As you think about the segments, where do you see the biggest opportunities to push margins forward? Is any of this opportunity you've identified in the past going to be negatively affected by a volume reset with COVID? Is it volume-agnostic, the benefit? Or is it going to be sized in relation to volume?

30. **Brad Jacobs, XPO:** There's no doubt about it: negative volumes are bad for us, let's be very clear. We want more volume. We don't want less volume. All of our levers and all of our six sigma and LEAN, that's all great stuff and we'll all keep working on that really hard, but when you have volumes down 20%, you can do all those good things and you're not going to be able to overcome the 20% down. Having said that, when we get out of this COVID situation, the company will come back leaner, meaner — in a nice way — more profitable and more focused.

We run the company with about the top 35 people: the business unit leaders and the senior leadership who partner with them. Then there's the next 65 or so people who are the next level of middle management down. Then there are about 2,500 leaders who are site managers and warehouse operators and team leads, who are doing the blocking and tackling. Below that, you have the workers driving and moving and picking and packing and so forth. We've engaged in a lot of introspection over the last two to three months during this pandemic, figuring out ways that we never dreamed of before to run the business better. Circumstances are forcing us to communicate more effectively while traveling less. The process of introspection and of being open-minded to any ideas — and it being okay to voice ideas — all of that was there before but it has definitely increased in our culture.

31. **David Vernon, Bernstein:** Getting back to the contract logistics business, it sounds like, in XPO Direct, you're taking the asset risk in terms of the shared facility and the lease, and then you're selling that off, or subletting it if you will. In the rest of the contract logistics business, how much of the assets involved in the automated facilities you're running for a particular customer are your assets versus your customer's assets?

32. **Brad Jacobs, XPO:** Mostly ours, and on the automation part it's very fungible. If we've got an autonomous robot in a facility in Memphis, say, and that facility is going into "un-peak" with lower volumes, we can very easily move the robot to another site within driving distance, and plug and play. We're all set up where there's activity and demand for it, so we don't have down time with the automation. We can share most of that pretty easily. In terms of the risk, it really comes down to utilization. If you have something that has a low utilization rate, that's something maybe you shouldn't be owning. The assets that we sweat have high utilization.

That's a trend throughout the whole organization. We're always looking at the utilization of our assets. For example, in LTL, in Q1, we ran about 23% fewer empty miles versus a year ago. With the same amount of trucks, we're carrying more freight. That's a beautiful thing. Anywhere we can optimize the use of our assets, whatever those assets are, that's part of our business plan.

33. **David Vernon, Bernstein:** In the contract logistics space, I'd imagine that's a fairly intimate relationship with whoever the customer is, right? They're involved in the

design of it, they're understanding the costs and they're understanding the pricing. Over the life of a contract, if you're able to kind of drive these efficiencies, how do you avoid not giving that back in the next contract renewal? There's going to be some visibility to that. The customer's going to know the KPIs. In my experience, in a former life, the customers who you're dealing with demand a lot of visibility on the contract and the efficiency metrics. How do you make sure that you're able to capture some of that value on an enduring basis, and it's not a situation where you get it in one contract and give it back in the next?

34. **Brad Jacobs, XPO:** In some cases, customers have visibility into what we're doing. Those are called "open-book" or "cost-plus" contracts. That's a minority of our contracts. That's more prevalent in the UK, for example, culturally. Most of our contract logistics business is closed-book, so we don't share everything with our customers.

Having said that, we're absolutely going to share some of that margin with our customers. We're a service company. We have to do that. All of our customers are always looking at ways to reduce their transportation and logistics costs — always. That's their job. Their job is to take costs out of their supply chain. We help them with that. We want every interaction they have with us to be a breath of fresh air. We help them achieve what they're trying to achieve, which is to move their goods through their supply chain in the most efficient way, and that includes the most cost-effective way.

35. **David Vernon, Bernstein:** I want to talk a little bit about the LTL franchise. You guys have done a tremendous job with what I think was thought of at the time as a fairly undermanaged asset: Con-way. When you guys came into it, can you talk about where the biggest opportunities were and what it took to get that 1,000 basis points of margin improvement out of the LTL network?

36. **Brad Jacobs, XPO:** I say this in a good way: many things. There were many opportunities to improve Con-way. There was no shortage of ways to do things in a more efficient, productive, profitable way, and a more integrated way. It really wasn't one company. It had a contract logistics company with its own HR group, its own IT group, its own procurement group, its own procedures and policies. They had a brokerage group called Con-Way Multimodal and they had the big LTL business. And they had a full truckload business, which we sold because we wanted to pay down debt and we weren't getting the high returns that we demand when we deploy capital.

So, the first thing to do was look at the org chart and make some sense out of it. I've literally looked at thousands and thousands of org charts over my career. I like looking at org charts. You can learn a lot about how a company runs if you just map out on a page how the people relate to each other. Obviously, there should only be one procurement organization because that way you're going to get better pricing. Obviously, there should only be one HR organization. Obviously, there should be one IT organization. At least, that's the way we run businesses: in an integrated way, with one big shared services organization. Standardize everything you possibly can. Measure the things that matter. Compensate people to achieve those KPIs. Get the whole culture all revved up about remembering their purpose, which is to please customers and please employees in order to generate superior returns for the people who own the company, the share owners. That's very much our culture.

People understand what we're doing here. They understand who pays the bills and where we get the money to run this business. People get that, at all levels of the company. They get that we're a shareholder value creation organization, while treating all our non-owner stakeholders with maximum respect.

37. **David Vernon, Bernstein:** If you think about where you brought LTL from and where you are today, how much room is there in the future to get additional margin gain? Or is it going to be more about volume growth?

38. **Brad Jacobs, XPO:** We're not trying to move up the Fortune 200 by getting more revenue. That's just not on our list. In fact, we'd be happy to move down the Fortune 500 if it created more shareholder value.

In LTL, what we have done is to be much pickier about the type of freight that we bring into our LTL network. We're understanding our cost structure better in LTL — pallet by pallet, customer by customer, lane by lane — and culling out the freight that really isn't good freight for us. Maybe we're not making a lot of money or sometimes any money on certain freight, so we're getting rid of it and bringing in more freight that matches what we need. We brought down our empty miles by 23% year-over-year in the first quarter. It's a big focus for us to make sure we keep finding freight where we have empties, where we have dead hauls, which is empty space that's underutilized. It's almost 100% flow-through, bringing that freight on, because the alternative is the trailer's just empty.

So, it's not a revenue play per se. It's going to continue down a long road that has lots of wood to chop still, which is a good thing. How do you take out waste and inefficiencies? How do you automate things that are being done old-school that need to be done new-school? I mentioned pricing. How is pricing done in a more centralized way? How are the labor assignments done in a more centralized, regionalized way, rather than in a decentralized way? How do you do all these things while keeping an entrepreneurial culture, keeping everyone engaged in the field? There's a big engagement push for us. The human element is big; keeping everyone's head in the game to buy into doing all these different endeavors.

There's no shortage of opportunities in LTL to run the pickup and delivery better; to run the cross-docks better; to run the linehaul better. Basically, to run the entire business better and better every year and to keep pushing margin. Now, we're not going to show margin improvement the second quarter. This quarter is going to be a step back for the whole industry, for the whole world. But, over time, there's no doubt we'll continue our process of improving our operating ratio, increasing our margin in LTL. There's a ton of opportunity to do that.

39. **David Vernon, Bernstein:** As you think about the freight management side of the world, with the digital marketplace and disruption of freight management, it feels like pretty much everybody is putting a ton of money into trying to automate processes to connect supply with demand. Do you think there's going to be any one approach that beats out the other approaches? Or will this be a case of everyone kind of doing the same thing with technology and ultimately leading to more standardized sets of services? I guess what I'm trying to get at is, how do you think about extracting value from your freight marketplace with technology if everyone's investing in the same technology?

40. **Brad Jacobs, XPO:** Well, everyone's not investing in the same technology. There's some commonality, but there's also a lot of distinction between each company and what they place their bets on in truck brokerage. For us, we started that in 2012. We developed XPO Connect and our focus has been on how to procure transportation cheaper. How do you find that truck that's just the perfect truck for this lane? How do you price intelligently, so you find that Goldilocks price where you win the business if it's profitable business, but you don't win it at a price where you're leaving money at the table? Not too high, not too low.

In order to understand what we're accomplishing in truck brokerage, you need to know two numbers: 9% and 15%. In the first quarter, our loads were up 9% on headcount that was down 15%. The proof is in the pudding. The automation that we've been developing is actually working, and we've been growing that business organically and very profitably. It's largely due to making the right bets on technology and investing in technology that actually is useful for the customer and for our own organization, so that we can serve customers in a more profitable way.

And to answer your question, David, I don't think there will be one company — not even us — that will design the one platform that everyone is on. I just don't think that's the way life works. But I do think there will be a handful of companies, meaning up to five companies with large digital platforms, that will gain a larger market share than the other thousands of brokers beneath them. We will certainly be one of that handful. I believe that's where it's going. I think there will be a market share shift from the small brokers to the big brokers, and I think those top five or so will have a large amount of the market share and be able to provide a lot of cost savings to the customer.

41. **David Vernon, Bernstein:** That's interesting, because I've always thought that the bigger opportunity for the bigger brokerages was really blowing up the smaller guys — the 10- and 20-person shops that these automation technologies allow you to deliver at a lower cost. As you think about your approach to that market and getting that level of

productivity on a business that already has pretty good returns, should we be expecting you to push more growth in that market?

42. **Brad Jacobs, XPO:** I think those smaller brokerage firms are at a higher risk than the larger ones. I think they have more headwinds than the large ones. The large ones actually have tailwinds from what the long-term industry trends are. I think the smaller ones have more headwinds coming in their direction. Having said that, there are some companies that just have great personal relationships with specific shippers. But, by and large, the big ones are the ones that are going to succeed here.

43. **David Vernon, Bernstein:** How are you positioned in Europe?

44. **Brad Jacobs, XPO:** We're the second largest contract logistics company in the world, and in Europe as well. We run about 200 million square feet globally in contract logistics. In LTL, we're the largest LTL provider in France and in Spain, and we're the third largest LTL provider in the UK. In terms of truck brokerage, we're the largest truck broker in Spain, and we're the third largest truck broker in France. If you look at the perimeter of Western Europe, where we're concentrated — mainly France, Spain and the UK — we have the largest transportation network within that perimeter.

We also have the three whale contracts I mentioned coming online this year in Europe, which is great positioning. Those are the July contract start-up with Waitrose, the launch of the Nestlé warehouse of the future, and our accretive acquisition of Kuehne + Nagel's three contract logistics verticals: e-commerce, food and beverage and tech. So, we have many things in Europe driving our growth.

45. **David Vernon, Bernstein:** As we think about cash flow and capex, here are two questions — one that came in through the website here, and one just generally. Last year, I think about 30% of your cash flow came from asset sales. How should we be thinking about the gains on property sales, and stuff like that, in relation to cash flow? How should we think about cash flow to net income on a longer-term basis? The second question would be around longer-term investment levels.

46. **Matt Fassler, XPO:** We guided asset sales this year somewhere in the neighborhood of $150 million or more. That's cash flow proceeds. And, while we've withdrawn our guidance, generally speaking, that level of asset sales is still what we expect to generate. The markets where we've been selling assets remain open, and we're making good decisions based on cap rates in those markets, so that remains very much intact.

In terms of investment levels, we came into the year thinking about gross capex in the $600 million plus range. We're going to pull that back, given the year we're in, by at least a couple hundred million dollars. We maintained our investments in a number of the important projects that Brad discussed earlier. For example, the LTL technology initiatives remain very high on our priority list. The warehouse of the future joint venture with Nestlé is very important to us.

47. **David Vernon, Bernstein:** We're coming up to the end of our 50 minutes. I do want to give you a chance to close us out here. First of all, thank you very much for making the time for this. This has been great. It's great to get your perspective on this industry. I'd also love to open the mic to you in terms of how you would like to differentiate yourself as an investment opportunity to our client base, who maybe doesn't know you as well. Do you want to leave us with some closing remarks and then we'll sign off?

48. **Matt Fassler, XPO:** A lot of the most important investment points have already been addressed. We couldn't be more excited about the opportunities ahead of us. Obviously, we're making it through a very challenged environment. We're taking care of our employees, our customers and our balance sheet.

    As we move forward, we're well-positioned for the outsourcing trend, the growth in e-commerce, the demand for warehouse automation and demand for a digital freight marketplace — these are all advantages that we've been building for years. They're very much underway, and the market is giving us tailwinds that I think will drive increased demand for what it is we do — and do well — over the next number of years. Our stock, relative to that opportunity, is very attractive. Our multiple is too low for the unique franchise we have, and we see a terrific runway ahead.

49. **David Vernon, Bernstein:** Alright. I want to thank you guys again for making the time today.

50. **Brad Jacobs, XPO:** Thanks, David. Appreciate it.