Investor Questions and XPO Responses

Truck Brokerage

Margin

1. *On brokerage, there was a 400-basis-point sequential contraction in net revenue margin. What would you attribute that to?*

   XPO: Some of that is related to seasonality — that typically results in some margin degradation from Q1 to Q2. Also, the cycle is maturing a bit. In Q1, we had tons of rail congestion, and freight that typically went by intermodal was moved by truckload instead.

   While the margin percentage was down, our total dollars are moving in the right direction. We're very focused on net revenue per load. Our net revenue per load was up versus last year, and last year was a good number. We had the best load growth we saw at any of the publicly reporting companies in brokerage, while generating very strong net revenue per load. Our load count was up 38%, and net revenue was up 47%. So, when you look at the combo of our volume and our profitability, we had a very good outcome. And that's against what was actually a pretty good quarter for us in truck brokerage last year, despite all kinds of macro issues.

Market share

2. *What is going on in brokerage? You guys are growing net revenue by nearly 50%. You're doing well in the face of what is a tight gross margin profile situation. Are the incumbents losing?*

   XPO: The way the market is set up, if you have scale and technology, you're going to do well. There are numerous, smaller players who don't have the wherewithal to invest in tech. We've been able to leverage tech to procure capacity at good prices, and also drive more loads through the system without increasing heads at that same rate. Over the past five years, we've been able to grow loads at twice the rate of headcount.

Brokerage technology

3. *You guys would put your brokerage technology platform up against any of these digital guys? Do you feel like you need any additional investment there?*

   XPO: We started investing heavily in brokerage tech in 2011 and we'll continue to invest as we keep innovating. We have first-mover advantage, and our adoption rates validate that. Our customer usage nearly doubled year-over-year, and our carrier usage is up 87%. The cumulative downloads of our Drive XPO app for truck drivers are at 475,000 right now, which is more than three times where it was a year ago.

Headcount

4. *We're very curious about revenue per employee in truck brokerage. How is that trending?*

   XPO: The best measure of brokerage productivity is loads per employee, which we improved year-over-year. Our headcount was up in Q2, and loads were up slightly more than headcount. Revenue per employee was up a lot, reflecting both productivity and higher market pricing. Importantly, net revenue per employee also rose, which reflects both the productivity of our salesforce and XPO Connect, and higher net revenue per load. Note that our year-over-year headcount growth will soon begin to moderate.

Cyclicality

5. *Truck brokerage really stood out in your second quarter results. I would appreciate any perspective on how sustainable those levels are, and how much is cyclical strength versus how much is attributable to XPO Connect?*

   XPO: It's both. It's hard to assign a precise split. The tightness of the market is benefiting everybody, but that will change eventually. It could go on for another couple of years, and, at the moment, there are no signs that it's abating. That's due primarily to two things: the driver shortage, which is the worst it's ever been, and shipper demand. Demand is coming back at a time when there's less supply of capacity. The industry will figure out ways to get more drivers back on the road, the chip shortage will end, and the economy will turn down at some point. In terms of what we're doing on the XPO side, it's the whole XPO Connect ecosystem and the digital edge we expect it gives us in any macro. Anybody can say they have great technology, but nobody has the traction that we do.

Stickiness

6. *In the brokerage business, congratulations. It's quite eye-opening compared to some of your larger competitors in the space, especially in terms of volume. There was mention on the call that this business has been stickier than in the past. What's driving that trend?*

   XPO: We did invest strategically in headcount, and we have strong customer relationships. We have the resources to help our customers navigate a challenging freight market. The tech makes it stickier on both sides of the transaction. Our carrier and customer usage of XPO Connect keeps going up and to the right. We're really thriving from that perspective. One real evolution in our outlook internally, from the beginning of the year, is the idea that these volume levels are sustainable, certainly for the remainder of the year. We've been very focused on driving that, and it's worked in our favor.

Less-Than-Truckload

Capacity

7. *On the LTL side, some other providers seem a little more focused on top-line growth right now. When I think about where your terminal infrastructure is, how are you doing on capacity? Is there still an opportunity with pricing before you think about expansion?*

   XPO: From a network standpoint, we're at 291 terminals right now, and we feel good about that. It's not that we won't add any in the future, but we know we have available capacity within the network as it exists today. The shortage of drivers is the bottleneck; it's an issue for the whole industry. Pricing remains very healthy and we see that continuing. In Q2, our yield was up 4.5% year-over-year, and on a two-year stack it's up 6.5%. Contract renewals are up 8%.

   Our technology investments in LTL are focused on giving us a better understanding of price elasticity. We're also doing some things to ease the driver shortage, like graduating more drivers from our CDL training schools. We're definitely getting a lot of traction there, but we know that alone won't solve it. So, we're also making sure we're able to leverage our tech to utilize the drivers we do have in the most efficient way possible.

8. *I keep asking about the tonnage growth in LTL because I think it makes sense for you to be investing in the top line of that business. Do you have any thoughts on that?*

   XPO: We like the coverage we have. We're able to execute on our plan, and our plan has been working. We're aware of what our peers have been doing, but most of them are still not at the level of coverage that we have.

9. *Why not be more growth-oriented in LTL?*

   XPO: We're adding more tonnage, but our broader approach to running the business has been working. We run the business to maximize EBITDA, and also with an eye toward free cash flow and financial returns. We generate robust free cash flow and substantial returns in LTL, and we expect to continue to grow earnings nicely. We're always evaluating new opportunities, but we're executing the successful strategy we've had in place for the past several years.

10. *You guys had a fantastic margin outcome in LTL this quarter. It sounded like a lot of focus was on efficiency, on getting price and improving margins. What about the growth*

angles in the network? Is there another way that growth can be approached? How should we think about the top line?

XPO: First of all, we had excellent top-line growth in Q2 — more so on volume, but significantly on price as well, and also in revenue per shipment. We're definitely committed to growth, and we're first and foremost committed to EBITDA growth. There is a path to EBITDA growth through a combination of volume and price and efficiency. It's working well for us, and that's the path we're sticking with.

11. *What about capacity in the LTL network? You stated you're not currently planning to add terminals. Do you have room to grow volume?*

    XPO: Yes, we have room to grow. Capacity is driven by terminals and doors and drivers and fleet. We've got excess capacity in rolling stock and terminals in about the 15% range, probably higher in some areas. That's a growth lever. We're graduating three times as many students from our driver schools as we did last year. We're attracting applicants with competitive compensation, and we're reaching more candidates through our sourcing partnerships.

Tonnage

12. *Do you have to choose between getting your operating ratio down and tonnage growth?*

    XPO: No. We're driving for EBITDA growth and high return on capital. That typically comes with some revenue growth and some OR improvement. All things equal, we're more likely to drive OR growth through pricing efficiency than through volume.

13. *You mentioned the 291 terminals. Is there any trading around of terminals within metro areas that would be a potential use or source of capex?*

    XPO: We added a terminal in Texas at the beginning of the quarter. We're constantly looking at our network to make sure it's optimized with the right mix of dock capacity versus pickup-and-delivery demand — that type of thing.

Purchased transportation and the driver shortage

14. *We expect purchased transportation on the LTL side to be highly inflationary given what's going on with truckload. We're assuming that'll stick around for the back half of the year. Anything specific that we should be thinking about?*

    XPO: You're right, purchased transportation is obviously an area where we're seeing inflation in the truckload world. If that inflation moderates, it will help us with linehaul costs. Our use of third-party linehaul miles was down as a percentage of total linehaul miles in Q2, and that's because we worked to reduce our dependence on third-parties, given what happened to truckload rates. That's going to be a continued emphasis for us.

15. *What percentage of linehaul are you doing yourself versus pre-pandemic, versus your target, and what is your target?*

XPO: In 2016, the first full year we owned the business, we were purchasing outside power for roughly 35% of linehaul moves. Last year that number was 25%, and this year to date, we're running at about 23%. It won't go to zero, but we expect to get it down below 20% in the next few years.

16. *Wouldn't you guys be able to attract experienced drivers instead of getting them right out of driver school, given that LTL is a better work-life balance and they make a bit more money as well?*

XPO: We're very active on both fronts — getting new drivers graduated and recruiting more experienced people. We advertise on all of the traditional channels, like XM radio. But the organic growth is really going to come from new drivers.

Mix

17. *Regarding the increase in your weight per shipment, is that due to a change in the mix of types of shipments coming through the network?*

XPO: It's not due to any one thing. We look closely at the mix by vertical, and the weight per shipment was up with consistency across most verticals. It's a sign of the macro rebound, and it's working its way into our weight per shipment.

Operating ratio

18. *You had a tremendous operating ratio performance. Can you walk through the drivers of that?*

XPO: Our XPO Smart tech is a big part of that. We're seeing more utilization of the software across our sites and it's helping our managers identify the right mix of labor at each dock for each shift. That's important, because you don't want freight to start piling up on the docks and have to have drivers help clear the docks. We're seeing productivity improvements across the board throughout the whole network. Also, on the cost side, we're optimizing labor expense. The other piece is what we're doing with pricing — making sure we can capture pricing that will go to the bottom line. And, of course, there's the route optimization piece. We're running roughly 2.5 million LTL miles per day and could always be running them more efficiently.

19. *What about your LTL operating ratio in Q3? Do you expect normal seasonality?*

XPO: Q2 tends to be the best from an OR perspective. Q3 OR is usually off from Q2, and that's what we expect.

20. *It seems like LTL is in the best place it's been so far — very strong demand trends, pushing pricing up. Should we look at pricing to continue to improve above your costs? Should we assume that your OR will be headed into the 70s in the near future?*

XPO: We're going for a decisively sub-80 OR, without question. If the demand stays strong, that will help us improve pricing. Contract renewals in Q2 were up 8%, so that part of the environment is very healthy. We can do more analytics to look at our network overall and determine how best to use elasticity data in our pricing. That pricing lever will be critical to improving our OR even more.

Cyclicality

21. *Is this the golden age for being an LTL company, given the supply dynamics in trucking and the consolidation in the space?*

    XPO: We're very excited about LTL. It's in a great place. For the next several years, you're likely to see higher prices, higher tonnage and better operating ratios, and therefore better returns on capital. LTL is a good place to be.

Capex

22. *On LTL capex, what is the visible trajectory of that going forward?*

    XPO: It's supposed to be higher this year than it was last year, but it's a strange time, when it's hard to spend money even if you want to spend it. We're working to get new equipment delivered, but it's not happening as fast as we had hoped. The base case for next year's capex would be for it to be in the same range as this year, but we'll take a look at that when we do the budgeting later this year.

Fleet

23. *What is your fleet age right now?*

    XPO: It's 5.79 years. It's been within the five- to six-year range for the past few years, so we're toward the upper end of the range right now. That's a function of waiting on new equipment we ordered.

Pricing

24. *Your revenue per hundredweight in North American LTL, excluding fuel surcharge, is up 4.5%. Anything to call out there, like weight per shipment changes that could be impacting that number on how core pricing is trending?*

    XPO: Our yield improved from Q1 to Q2, despite a big acceleration in weight per shipment, which rose 6%. When revenue per shipment, ex fuel, is up about 11%, that's a good indicator of a positive pricing dynamic. We achieved pricing increases of 8% on contract renewals in Q2, which bodes well for the business going forward.

25. *I wanted to get some perspective on where you see yourself in terms of pricing relative to your service level and value proposition. Are you at a good level and just finetuning?*

XPO: There are some things we need to wire differently. How do we integrate more elasticity into the way we price? How do we make sure we have the right components to build out the optimal prices for customers? There's some heavy lifting we need to do, and these things are high on our agenda as we focus on continuing to improve our OR.

Yield

26. *Your yield growth was strong at 4.5%, but lower than what some providers in the industry seem to be experiencing. What's your thought on where you stand relative to the competitive environment?*

XPO: Our yield improved from Q1 to Q2, and we had a sizeable acceleration in weight per shipment and revenue per shipment. All three of those are heading in the same direction. The average price increase on our contract renewals in the quarter was 8%. That's a pretty strong showing across the board, and we think it's an indicator of more yield to come. We're also doing a lot more with data analytics and pricing tools, which gives us confidence that we'll see a further upside to yield.

Competitive landscape

27. *LTL feels a bit frothy right now, with new players entering the market and existing players building out their networks. Do you guys worry about industry-wide overbuilding? Is there a concern that conditions might slow down when the government stops pumping so much money into the economy?*

XPO: Nothing we're seeing in the marketplace is suggesting that competition is anything other than rational. To your second point, we will all have to live with the decisions the government makes, but we have no special insight into predicting that. We're ready for whatever happens. The industrial verticals in LTL have a lot more room to bounce back still, so we think the cyclical backdrop for our LTL business is a favorable one.

Technology

28. *How do your technology investments and focus help with LTL pricing?*

XPO: It's at the forefront of our tech initiatives in LTL. When you're writing a pricing proposal, how scientific are you? Ideally, you're thinking about verticals, regions, seasonality, specific lanes, the weight of the freight, your history with that customer, the competitiveness of the lanes. You have to make sure you use all of your proprietary data and all of the third-party data that's available out there to show that, given a particular set of parameters, this is the most likely way this is going to transpire. It's a big opportunity for differentiation, and the science behind it goes to the core of the skill set of Mario's tech team.

Finance

Guidance

29. *What are some things that you want to point people to in terms of the opportunity going forward?*

XPO: It starts with the strength of the business and the market presence that we have in LTL and brokerage. We'll continue to grow in those spaces and do extremely well in both of them. The transportation markets are robust, and demand is likely to continue to grow. We're capitalizing on key trends of digital brokerage and, more broadly, e-commerce and outsourcing. We're focusing on innovative technology across our lines of business. We continue to expect to generate at least $1 billion of adjusted EBITDA in our LTL business alone in 2022. From a balance sheet standpoint, we're deleveraging to move toward an investment-grade credit rating.

Cash

30. *On free cash flow, anything unique for the quarter?*

XPO: In Q2, consolidated free cash flow was $282 million. Working capital was a bit of a good guy relative to expectations, even as we grew our revenue sharply and outperformed. We're very disciplined with capex. Also, it's not like equipment orders are getting filled early these days, so there's probably some deferred deliveries that impact timing. For standalone XPO, we've guided 2021 pro forma free cash flow to a range of $400 million to $450 million for the full year.

Investment-grade credit rating

31. *On the balance sheet, you have long been a proponent of running some level of leverage. Now that you're going investment-grade. How quickly do you want to get there? Do you think of that as sustainable, or is it just a benchmark to show the Street?*

XPO: We're committed to getting to investment-grade and we'll do it as fast as we responsibly can. The two big levers are growing EBITDA and generating free cash flow, and then applying that to debt reduction. We will get there — it's just a matter of time — and we plan to stay there. Many of our investors told us that getting leverage down was the best lever we could pull to get a higher multiple, so we're going with that.

32. *When are you doing the debt paydown? How will that affect your model as a pure-play transportation company?*

XPO: The call notices went out at the beginning of August and the debt will be called in September. So, we'll get almost four months of benefit this year from the paydown and a full-year benefit next year. Some of the notes are at 6.125% and the rest are 6.75%. The cash we've been sitting on basically doesn't earn anything, so those interest rates are the pickup we're going to get, and it’s considerable. Our interest expense should be sharply lower in 2022.

SG&A

33. *The corporate expense line looks pretty significant. After you get a chance to work on that and bring it down to a more appropriate level, what is the right number and the timeline to get there?*

XPO: We agree with you that there’s an opportunity to bring that number down, but we’re not ready to guide to the amount and timing yet.

Valuation

34. *XPO is trading at 19x P/E. Do you think your conversations now will be more on a P/E valuation or adjusted EBITDA?*

XPO: It’s up to the market. We’ve always thought about it in terms of EV/EBITDA, but as we de-lever, it might be a little more about P/E. As people update their models to reflect the pro forma interest expense in the guidance we provided, that P/E ratio will be even lower, all other things being equal.

Macro Environment

Inflation

35. *You guys are fine on the top line. What about the cost side? Every company in the world is struggling with labor and wage cost inflation. Do you think it’s temporary?*

XPO: It's tough to know if it’s temporary or structural. We’re seeing inflation with rent, fuel, labor and transportation. We have two things going our way. One is pricing, where we have the ability and the opportunity to take price. That's particularly true in LTL, and it’s helped us offset the impact of cost pressures. The second is our technology. XPO Connect and XPO Smart have helped us reduce our cost structure in terms of cost-to-serve customers, cost-to-source brokerage capacity, labor productivity on our LTL docks and the way we utilize our LTL fleet.

Economic recovery

36. *Was a lot of the strength you saw across the business this quarter attributable to the industrial economy picking up?*

XPO: Industrial is definitely picking up. It’s one of our bigger verticals across the business, and particularly in LTL. Demand is growing and there’s room for it to grow more, following a prolonged downturn. Industrial hasn’t come back as strongly as the consumer verticals yet, but it was still a tailwind for us in Q2. The e-commerce piece of consumer is booming.

37. *You made a comment on the call that "customers are more than back." Do you think we're past where we were before the pandemic? Where do you think we are in the cycle?*

XPO: We think we could be at the beginning of a prolonged upcycle — with the caveat that a resurgence of COVID might disrupt that. Before the pandemic, the economy was super-strong and likely would have kept getting stronger. Now, the economy is pretty much back where it was pre-pandemic and will get a lot stronger once all the labor shortages and supply chain snafus are worked out. We're bullish. The other caveat is, we don't know where government spending will end up. How much the government spends and on what, and how it finances it, will make a difference.

38. *A lot of data indicates that inventories are still super-tight, but other sources are saying that if you exclude auto, inventories are mostly back to normal. Where do you think it stands?*

XPO: We think there's room to go. There's still some catchup to be done. One thing we hear from our customers is that they don't have the raw materials or parts they need, so the full engine of industry hasn't revved up yet. We're helping to solve some of these supply chain disruptions for our customers. The industrial piece has trailed the consumer piece, but the trajectory is right.

39. *In your view on the economy, are we back to firing on all cylinders? Do you feel this is as good as it gets regarding peak and non-peak?*

XPO: We just reported more than $5 billion of consolidated revenue and generated over half a billion of adjusted EBITDA in Q2. Customers are clearly moving goods. There's strong consumer spending, and the industrial economy is starting to recover. LTL is good. Growth is continuing. Revenue per shipment looks very good. So, life overall is good.

40. *How do you think about the two dynamics of industrial and consumer in LTL, and where are you versus where you could be in this business?*

XPO: Industrial is an area of opportunity with an upside that should play out over the next six months or so. Auto is slow, and the microchip shortage is impacting other verticals as well. Lumber, steel and rare minerals are in short supply. The consumer side has remained very strong. There's a lot of restocking that still needs to occur to meet pent-up demand, and supply issues won't resolve quickly. The back-to-school peak and the holiday peak could be particularly strong because of stimulus savings.

Chip shortage

41. *On the call, you mentioned a $10 million impact from the semiconductor shortage. Where does that show up?*

    XPO: It comes from lost volume on the customer side. If you look at automotive, for example, a lot of the volume we would normally see is logjammed and the impact is spread across several different lines of business and across geographies. Intermodal has auto exposure. LTL has a lot of industrial customers, and many are impacted by the chip shortage. We pointed to the semiconductor shortage because it's a good way to illustrate that we still have room to go to get to full earnings power.

42. *Most people think rail will come back. Underlying demand is still strong in the end-markets. The chip shortage is pushing inventory restocking later. Transports are assuming that shipper customers will ramp back up. If chips came back tomorrow, would you see a jump?*

    XPO: Yes, but we're heard the CEO of Intel state last week that the shortage might last until 2023. There's enough demand for a jump, but a lot would depend on the timing of chip availability.

August 11, 2021

Forward Looking Statements and Non-GAAP Financial Measures

In this digest of Investor Questions and XPO Responses, we make certain forward-looking statements within the meaning of applicable securities laws, which, by their nature, involve a number of risks, uncertainties and other factors that could cause actual results to differ materially from those projected in the forward-looking statements. A discussion of factors that could cause actual results to differ materially is contained in our SEC filings. The forward-looking statements made herein are made only as of August 11, 2021, and we have no obligation to update any of these forward-looking statements, except to the extent required by law. In this document, we also may refer to certain non-GAAP financial measures as defined under applicable SEC rules. Reconciliations of historical non-GAAP financial measures to the most comparable GAAP measures are contained in our earnings release and related financial tables, or on our website. With respect to our projections of adjusted EBITDA in our LTL business in 2022 and pro forma free cash flow in 2021, which are non-GAAP financial measures, reconciliations of these non-GAAP measures to the corresponding GAAP measures are not available without unreasonable effort due to the variability and complexity of the reconciling items that we exclude from such non-GAAP measures. The variability of these items may have a significant impact on our future GAAP financial results and, as a result, we are unable to prepare the forward-looking statement of income and statement of cash flows prepared in accordance with GAAP that would be required to produce such reconciliations. You can find a copy of our earnings release, which contains additional important information regarding forward-looking statements and non-GAAP financial measures, in the Investors section on our website.