Wolfe Research Transportation and Industrials Conference
Fireside chat with Brad Jacobs, Malcolm Wilson and Matt Fassler of XPO Logistics
Conducted by Scott Group, Managing Director, Wolfe Research
May 26, 2021

1. **Scott Group, Wolfe**: We've got Brad Jacobs, chairman and CEO of XPO Logistics; Malcolm Wilson, the CEO of Europe; and Matt Fassler, the chief strategy officer. We're going to jump right into questions.

   Brad, I always like to start with you, to take us around the globe and talk about the demand trends that you're seeing everywhere. Is Europe starting to catch up to the US? Which parts of the business are seeing the best trends right now? What, if anything, is lagging? There's lots and lots to talk about.

2. **Brad Jacobs, XPO**: First of all, thank you for once again inviting us to speak at your conference, Scott. We appreciate the opportunity. To answer your question, it's hard to find anything lagging. We had our monthly operating reviews last week, and everybody was in a great mood. The only country where conditions are bad right now, sadly, is India, because of COVID. We don't have a lot of business operations in India, but we have a lot of shared services there. It feels similar to where the US was in the middle of last year.

   In the main countries where we have business — the US, France, the UK, Spain — our business is booming. You asked whether Europe is ahead of the US or vice versa; that's been ping-ponging back and forth. There was a time when Europe was coming out of the pandemic faster than the US, but that reversed when the US got people vaccinated faster and Europe went back into lockdowns. Now, Europe is rebounding, too.

Within Europe, of all the countries we operate in, the UK is the closest to the American rebound. That's followed by Spain, and then France is right behind. The recovery in Europe is definitely on the cusp of being just as good as it is here. There's this feeling in Western Europe, and here as well, of COVID being almost over. Demand is coming back quite a bit.

You also asked about the three main parts of our business. In LTL, the primary underlying driver is the industrial rebound. Industrial activity wasn't great even before the pandemic, mainly because of the tariffs, and then during the pandemic, the industrial economy took it on the chin. It's started to come back in the last three to four months, and it's coming back more each month than in the previous month. Our tonnage is good in LTL. Yield is good, too.

There are a lot of company-specific things — beyond the macro drivers — that we're doing at XPO to further improve our LTL business. These are mostly technology-related. They've been contributing, and should continue to contribute, to our industry-leading margin expansion. We have the second-best profit margin in the US LTL industry, and we have the best track record of expanding that margin. The biggest gating factor to LTL growth is the lack of available drivers. We would have tons and tons — pun intended — more business if we could get more drivers. The flip side of that is, fortunately, we have a lot of driver schools. We're graduating more and more people, so we have some access but, boy, we could use a lot more drivers.

In truck brokerage, Scott, if I could summarize the market in one word it would be "tight." Brokerage is a line of business where the driver shortage is actually helping us, because it's inhibiting additional capacity and we have access to capacity. Demand is increasing, so the seesaw is very much tipped in favor of those who have capacity.

The other thing that's driving our brokerage business, and the reason we've been outperforming, is XPO Connect, our digital freight marketplace. We started on the path of being technology-enabled in brokerage back in 2011. Ten years later, fast forward, and we have XPO Connect growing by leaps and bounds. This technology is the main factor why we're doing better than the industry.

Finally, our logistics business — which will be called GXO after the planned spin-off. It's a great model. Revenue growth has really accelerated recently. You heard on our earnings call that we announced several whales — major business wins whose life-of-contract values were $400 million, $500 million, $600 million, and one that was $1.8 billion. There are three factors behind all of the success we're having. First, the outsourcing trend is accelerating because many customers learned in the pandemic that they don't do logistics very well themselves, whereas our operations performed swimmingly during the pandemic. So, they see the value in outsourcing more. Factor number two is the growth in e-commerce, which is our biggest vertical. Factor number three is the increasing customer demand for more heavily automated warehouses — more robotics and advanced automation. That's driving our growth because we're an industry leader in warehouse automation. That's my whirlwind tour.

3. **Scott Group, Wolfe**: That's great. Now I want to get more into each of the different lines of business. I certainly want to talk about the spin-off, as well. Let's start with LTL. You mentioned the lack of drivers and capacity. That all sounds good for pricing. Talk about the pricing environment that you guys see in LTL right now. Is this the year where you think you finally break through over that $1 billion of LTL EBITDA?

4. **Brad Jacobs, XPO**: Not in 2021, but I do feel that 2022 is likely the year we break through the $1 billion of adjusted EBITDA in LTL. This year, we're not guiding to $1 billion. I don't want to put a false expectation out there. Having said that, it's a very favorable LTL environment right now. Unlike truckload, where capacity generally comes into the market when pricing improves, there's really no net new capacity coming into the industry in LTL. Our services are in great demand, so tonnage is up and yield is up. At the same time, we have those company-specific initiatives I mentioned that are expanding margin, so we expect to see nice operating ratio improvement and a good

year-over-year comparison.

5. **Scott Group, Wolfe**: One of the things that everyone in LTL is dealing with to some extent right now is headwinds from purchased transportation — except you guys. You didn't really see any of that in the first quarter. What are you doing differently relative to prior periods around purchased transportation?

6. **Brad Jacobs, XPO**: We do some third-party purchased transportation for the linehaul portion of LTL, but we mostly move freight on our own trucks. We've brought purchased transportation down a lot from a few years ago. We were at 35% of linehaul miles in 2016. In the first quarter, we were below 24%.

7. **Matt Fassler, XPO**: To add a little color on this point, Scott, we use in-house capacity to manage the increased activity. We increased trailer utilization in the quarter, and we continued to work on route optimization — that's a long-term project that pays dividends in an environment like this one. We reduced empty miles by 6% year-on-year; and, again, we were able to reduce our use of third-party linehaul at a time when it's really important to do so.

8. **Scott Group, Wolfe**: How do you think about the long-term margin potential for LTL? If we were to allocate some of the corporate costs to the individual segments, what's the underlying operating ratio right now, looking at it apples-to-apples with some of your

peers? Do you see the potential to get to a sub-80 operating ratio in LTL over the next few years?

9. **Brad Jacobs, XPO**: Definitely. We will be in the 70s for OR. That's our mission. That's our objective. That's our goal. We're marching toward that very determinedly, and we will achieve that, for sure.

10. **Scott Group, Wolfe**: LTL is clearly the crown jewel of XPO.

11. **Brad Jacobs, XPO**: You think so? I was thinking logistics is, but I'm also very proud of LTL. And, of course, brokerage is nothing to sneeze at, either! So, I'm not so sure LTL is the sole crown jewel. I think we have three crown jewels. We have logistics, LTL and truck brokerage, and they're all very shiny crown jewels.

12. **Scott Group, Wolfe**: When do you think about starting to grow the footprint of LTL?

13. **Brad Jacobs, XPO**: We don't. We don't because we're already delivering to more than 99% of all US zip codes. I'm not sure we need to have a physical presence in the few remaining, thinly populated areas. We have nationwide coverage now, so for us it's not about adding more service centers, like some of our competitors are doing. Our tonnage growth year-over-year is true same-store growth. We can grow the business by yield, by tonnage and by operating margin expansion, so the growth curve on the bottom line

should be really nice — all the while generating significant amounts of free cash flow. It's not about growing the footprint.

14. **Scott Group, Wolfe**: Let's now turn to the logistics part and GXO. I know we don't have all the details, yet. I'm guessing we'll get them soon. Big picture, high-level, Malcolm, how should we think about the growth profile of GXO, the return on capital, the margins, the free cash flow? How do you think about each of those pieces?

15. **Malcolm Wilson, XPO:** It's a great business. As Brad mentioned, we are seeing some big trends at the moment. More and more companies are outsourcing their logistics. During the pandemic, they realized that logistics was not their core competency. E-commerce fulfillment has been a real shift in the buying behavior of consumers. I think we can all testify to that in the way we are buying products. Some of the hyper-growth might temper as brick-and-mortar retail goes back to work, but our experience so far is that e-commerce is staying very strong. We think that change in buying behavior is here for the long-term.

Those same trends are requiring more and more automation, and that's also driving our growth. About 38% of our global logistics business is in e-fulfillment. We have the largest e-fulfillment centers across Europe and we're building up this business rapidly across North America. All of these things are enabling us to grow gross margin and EBITDA margin. We're expecting to see high-single-digit to low-double-digit organic growth in the business. And, we have good operating leverage to transfer that to the bottom line.

We are in a new phase of growth as a result of these big secular tailwinds in the industry, and our early adoption of tech enablement is a strong differentiator for the business. We've become the go-to partner for many big companies looking to outsource their logistics.

16. **Scott Group, Wolfe:** How about the returns on capital in this business? Could you talk directionally?

17. **Malcolm Wilson, XPO:** We have a very strong governance process when it comes to return on capital. We look at each individual project and target a minimum 20% return — but in reality, we're often seeing closer to 30%. When we set up a contract with a customer, we make sure that we're getting a relatively prompt payback of the cash, driving our free cash flow. There is very little maintenance capex involved, so the main use of capex is for growth. And even after we've established a contract, over time, we validate that the business is seeing the levels of return that we anticipated. We have a strong boilerplate contract that enables us to go back to the table with the customer if there's any variance.

We're seeing strong ROIC right now, and we expect that to increase. Customers are continuously asking us to bring more complexity to their projects, and so we're adding more value to our customer base. Our recent announcement of the Apple contract is a great example of that. We're setting up a million-square-foot, highly automated facility for Apple, and we'll be using robotics to personalize their products before they get dispatched to consumers. That's an example of the kind of added value that helps us to achieve a higher level of margin. And, this is more and more the type of business that we're doing.

18. **Scott Group, Wolfe:** How do you think about your competitive positioning versus other large players like Deutsche Post or UPS?

19. **Malcolm Wilson, XPO:** That's difficult to compare. Deutsche Post Supply Chain and UPS Supply Chain are good companies, but these are businesses that are embedded within larger organizations. The great thing about GXO is that, out of the gate, it will be the second largest contract logistics company in the world and pure-play logistics. All of the laser-focus of the management team is going to be directed to logistics. Our management team has great experience at growing margins and growing EBITDA, as well as organic growth, while throwing off a lot of free cash. And, we are doing that while continuing to invest in new sites. We opened 15 sites in the first quarter, which is up nearly 15% year-over-year. And, we're pushing out more and more automation and

robotics across the business, because that's improving the overall level of annual return we're seeing from the business.

20. **Scott Group, Wolfe:** You announced some huge contracts. What is the duration of those contracts? What's the realistic growth from the contracts that you've announced so far?

21. **Malcolm Wilson, XPO:** Typically, when we onboard a new customer, they discover pretty quickly that they like working with us. We make life simple for them by taking the strain off of them. For that reason, it's easy for us to expand a customer relationship. If I think about our largest customers, only a few years ago, we would be operating a single location for most of them. Now, it's more typical to have activity across different geographies for the same customer — ranging from Mexico, North America, to all parts of Europe. That's how we're growing our business with existing customers.

    At the same time, we're beefing up our reputation for reliability, efficiency and as a tech innovator. When we deploy robotic technology, our productivity levels improve tremendously. That's what's bringing new blue-chip customers like Apple, who want to work with us for the first time. The vast majority of our contracts are multi-year, giving us visibility into our growth for 2021 and 2022 by looking at the business we've secured now. That's what gives us a high degree of comfort about our top-line growth, which we're sure we'll leverage to the bottom-line, as well.

22. **Scott Group, Wolfe:** So, we should expect high-single-digit growth on the top-line, and then if you're going to leverage it, double-digit bottom-line growth?

23. **Malcolm Wilson, XPO:** I think that's a conservative expectation.

24. **Scott Group, Wolfe:** And do you think free cash flow grows in line with that bottom-line growth, or does it grow even faster?

25. **Malcolm Wilson, XPO:** The model is designed for free cash flow to grow in line with or better than EBITDA. This is a secular growth business. Other than technology, the main capex requirement that we have — and it's tightly managed — is a relatively small amount of capex for maintaining the business and keeping the lights on. It's very low, but it's essential. And then, everything else is growth. We're very mindful of our ability to throw lots of free cash flow off in this business. It's important for the company.

26. **Scott Group, Wolfe:** The goal is to be investment-grade for both of the businesses. Do you expect GXO to be investment-grade right from the start, and do you have any visibility in terms of how much debt you can actually move over to GXO while still being investment-grade?

27. **Matt Fassler, XPO:** We expect GXO to be investment-grade coming out of the gate. We've been in conversations with the rating agencies and we know what we need to do. We're not going to transfer debt over. We'll issue some new debt on behalf of GXO, and we'll dividend a portion of those proceeds to XPO, which we'll use to pay down XPO debt over time. So, think of GXO as being investment-grade on day one, and XPO will be investment-grade in due course. We're committed to this for both companies.

28. **Scott Group, Wolfe:** Any clarity in terms of how much debt that is initially at GXO?

29. **Matt Fassler, XPO:** Nothing that precise, but if you look across industrial comps who are investment-grade, you can see where the leverage levels typically are. It's generally been in the 1 to 1.5x range, but we'll get more precise as we finish our conversations with the rating agencies.

30. **Scott Group, Wolfe:** Brad, I want to ask you a strategic question about how we should think about investment-grade relative to acquisitions. You said you want both businesses to be investment-grade. If the transportation segment ends up trading at a higher valuation than XPO today, would you consider not going investment-grade and opting to take this asset that's now trading at a higher valuation and go out to do more deals? How do you think about balancing potential M&A relative to investment-grade?

31. **Brad Jacobs, XPO:** We're 100% committed to getting to investment-grade on day one with GXO, and in due course with XPO. The reason is our shareholders — they've told us if we bring down our leverage, our multiple will go up, which will expand the universe of investors who can buy our stock.

At the same time, there are plenty of investment-grade companies that do M&A. You might have to throw a little equity into the deal or bring in a sovereign wealth investor or some other partner, for example. There are plenty of ways to manage the balance sheet and still be conservative while growing through M&A. But we don't need to do

M&A in any of our businesses in order to grow a lot. We've got very good organic growth potential.

32. **Scott Group, Wolfe:** Is that in any way part of the rationale of splitting these businesses up? I presume one of these — XPO or GXO — is going to trade at a higher multiple than XPO today and one's going to trade at a lower multiple. So, is part of the idea that one of these businesses is going to be in a better position to do M&A?

33. **Brad Jacobs, XPO:** No, it isn't. If an acquisition is strategically sensible, financially accretive and there's a compelling reason to be doing the deal — whether that's from a customer perspective or an operations perspective, for example — then we can consider it, as long as it doesn't mess up the balance sheet.

34. **Scott Group, Wolfe:** The brokerage results have been terrific. To what extent is this down to the market being very tight and you leveraging the market well, versus XPO Connect, for example?

35. **Matt Fassler, XPO:** A great deal of it is down to XPO Connect. Consider that we've been investing in digital brokerage for 10 years. Connect has hit a sweet spot with customers and carriers, and internally, too. You saw that our brokerage loads per day were up in the mid-twenties-percent last quarter, which was the best year-over-year increase in the industry. That's indicative of significant market share gain, as we offer an attractive interface for customers and carriers.

We're also driving margin in brokerage, as we get good price discovery through our pricing tools within XPO Connect. And finally, we're driving productivity. Over the past five years, our brokerage rep headcount is up 3%, whereas our loads are up over 40%. We're gleaning the bulk of that productivity from Connect.

It's obviously been a robust truck brokerage market, certainly from a volume perspective. We've been participating in that, but our outperformance is mainly a function of our technology. And we think our tech edge and the growth opportunities it gives us are both sustainable.

36. **Scott Group, Wolfe:** What about the rest of transportation? LTL and brokerage make up over 90% of the EBITDA, but they make up 50% of the revenue of the transportation business. So, what's the plan to improve the margins for the remainder of that transportation segment?

37. **Matt Fassler, XPO:** Most of those other transportation businesses are asset-light with low capex requirements. We feel good about the profitability of those asset-light pieces of the transportation business. And then we have LTL, an asset-based business, which is a very high-margin.

38. **Scott Group, Wolfe:** So, your point is the operating margins might be lower, but that's still not a drag on returns?

39. **Matt Fassler, XPO:** We're focused on driving operating margins and EBITDA margins higher in every line of business, in both transportation and logistics. With the smaller

units you're talking about, we feel good about the base level of margins in each business relative to the capital that we invest in that business.

40. **Scott Group, Wolfe:** Brad, you started by saying that things feel pretty great everywhere. When I look historically, first quarter is typically 20 to 21% of full year, from an EBITDA perspective, and that could imply over $2 billion of EBITDA potential this year. So, how do you think about that in the context of the guidance? Do you feel like there's upside potential, or is there reason to think that this is not the year to be thinking about normal seasonality?

41. **Brad Jacobs, XPO:** Well, this is definitely not the year of normal seasonality, but please don't go out there with $2 billion of adjusted EBITDA potential this year. In the guidance we issued, the midpoint for 2021 adjusted EBITDA was $1.85 billion, and we feel confident about that. It's a solid number and is much higher than the previous guidance we had issued, so we've already bumped it up. And we don't want the market to get ahead of us.

42. **Scott Group, Wolfe:** Thank you guys so much. I enjoyed the conversation. We appreciate you being here.

43. **Brad Jacobs, XPO:** Thank you, Scott.

Edited for clarity

Non-GAAP Financial Measures

As required by the rules of the Securities and Exchange Commission ("SEC"), we provide reconciliations of the non-GAAP financial measures contained in this transcript to the most directly comparable measure under GAAP, which are set forth in the tables posted in the investor relations section of our website.

XPO's non-GAAP financial measures used in this transcript include: adjusted earnings before interest, taxes, depreciation and amortization ("adjusted EBITDA") and adjusted EBITDA margin on a consolidated basis; and adjusted operating income, adjusted operating ratio, adjusted EBITDA and adjusted EBITDA margin for our North American less-than-truckload business.

We believe that the above adjusted financial measures facilitate analysis of our ongoing business operations because they exclude items that may not be reflective of, or are unrelated to, XPO and its business segments' core operating performance, and may assist investors with comparisons to prior periods and assessing trends in our underlying businesses. Other companies may calculate these non-GAAP financial measures differently, and therefore our measures may not be comparable to similarly titled measures of other companies. These non-GAAP financial measures should only be used as supplemental measures of our operating performance.

Adjusted EBITDA includes adjustments for transaction and integration costs, as well as restructuring costs and other adjustments as set forth in the attached tables. Transaction and integration adjustments are generally incremental costs that result from an actual or planned acquisition, divestiture or spin-off and may include transaction costs, consulting fees, retention awards, and internal salaries and wages (to the extent the individuals are assigned full-time to integration and transformation activities) and certain costs related to integrating and converging IT systems. Restructuring costs primarily relate to severance costs associated with business optimization initiatives. Management uses this non-GAAP financial measure in making financial, operating and planning decisions and evaluating XPO's and each business segment's ongoing performance.

We believe that adjusted EBITDA and adjusted EBITDA margin improve comparability from period to period by removing the impact of our capital structure (interest and financing expenses), asset base (depreciation and amortization), tax impacts and other adjustments as set out in the tables on our website that management has determined are not reflective of core operating activities and thereby assist investors with assessing trends in our underlying businesses.. We believe that adjusted operating income and adjusted operating ratio for our North American less-than-truckload business improve the comparability of our operating results from period to period by (i) removing the impact of certain transaction and integration and restructuring costs, as well as amortization expenses and (ii) including the impact of pension income incurred in the reporting period as set out in the attached tables.

Forward-looking Statements

This transcript includes forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended, including our company's planned spin-off of its logistics segment and our future growth prospects for adjusted EBITDA in our North American less-than-truckload business. All statements other than statements of historical fact are, or may be deemed to be, forward-looking statements. In some cases, forward-looking statements can be identified by the use of forward-looking terms such as "anticipate," "estimate," "believe," "continue," "could," "intend," "may," "plan," "potential," "predict," "should," "will," "expect," "objective," "projection," "forecast," "goal," "guidance," "outlook," "effort," "target," "trajectory" or the negative of these terms or other comparable terms. However, the absence of these words does not mean that the statements are not forward-looking. These forward-looking statements are based on certain assumptions and analyses made by us in light of our experience and our perception of historical trends, current conditions and expected future developments, as well as other factors we believe are appropriate in the circumstances.

These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions that may cause actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by such forward-looking statements. Factors that might cause or contribute to a material difference include the risks discussed in our filings with the SEC and the following: economic conditions generally; the severity, magnitude, duration and aftereffects of the COVID-19 pandemic and government responses to the COVID-19 pandemic; our ability to align our investments in capital assets, including equipment, service centers and warehouses, to our customers' demands; our ability to implement our cost and revenue initiatives; our ability to successfully integrate and realize anticipated synergies, cost savings and profit improvement opportunities with respect to acquired companies; matters related to our intellectual property rights; fluctuations in currency exchange rates; fuel price and fuel surcharge changes; natural disasters, terrorist attacks or similar incidents; risks and uncertainties regarding the potential timing and expected benefits of the proposed spin-off of our logistics segment, including final approval for the proposed spin-off and the risk that the spin-off may not be completed on the terms or timeline currently contemplated, if at all; the impact of the proposed spin-off on the size and business diversity of our company; the ability of the proposed spin-off to qualify for tax-free treatment for U.S. federal income tax purposes; our ability to develop and implement suitable information technology systems and prevent failures in or breaches of such systems; our substantial indebtedness; our ability to raise debt and equity capital; fluctuations in fixed and floating interest rates; our ability to maintain positive relationships with our network of third-party transportation providers; our ability to attract and retain qualified drivers; labor matters, including our ability to manage our subcontractors, and risks associated with labor disputes at our customers and efforts by labor organizations to organize our employees; litigation, including litigation related to alleged misclassification of independent contractors and securities class actions; risks associated with our self-insured claims; risks associated with defined benefit plans for our current and former employees; and governmental regulation, *including trade compliance laws, as well as changes in international trade policies and tax regimes; governmental or political actions, including the United Kingdom's exit from the European Union; and competition and pricing pressures.*

All forward-looking statements set forth in this transcript are qualified by these cautionary statements and there can be no assurance that the actual results or developments anticipated by us will be realized or, even if substantially realized, that they will have the expected consequences to or effects on us or our business or operations. Forward-looking statements set forth in this transcript speak only as of the date hereof, and we do not undertake any obligation to update forward-looking statements to reflect subsequent events or circumstances, changes in expectations or the occurrence of unanticipated events, except to the extent required by law.