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PRESENTATION

Operator

Welcome to the XPO Q4 2023 Earnings Conference Call and Webcast. My name is Sherry, and I will be your operator for today's call. (Operator Instructions) Please note that this conference is being recorded.

Before the call begins, let me read a brief statement on behalf of the company regarding forward-looking statements and the use of non-GAAP financial measures. During this call, the company will be making 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 the company's SEC filings as well as in its earnings release.

The forward-looking statements in the company's earnings release or made on this call are made only as of today, and the company has no obligation to update any of these forward-looking statements, except to the extent required by law.

During this call, the company may also refer to certain non-GAAP financial measures as defined under applicable SEC rules. Reconciliations of such non-GAAP financial measures to the most comparable GAAP measures are contained in the company's earnings release and the related financial tables or on its website. You can find a copy of the company's earnings release, which contains additional important information regarding forward-looking statements and non-GAAP financial measures, in the Investors section of the company's website.

I will now turn the call over to XPO's Chief Executive Officer, Mario Harik. Mr. Harik, you may begin.

Mario A. Harik ***XPO, Inc. - CEO & Director***

Good morning, everyone. Thanks for joining our call. I'm here in Greenwich with Kyle Wismans, our Chief Financial Officer; and Ali Faghri, our Chief Strategy Officer.

I'm pleased to report that we capped a strong year with a quarter that exceeded expectations, and we've carried that momentum into 2024. Company-wide, we reported fourth quarter revenue of $1.9 billion, which is 6% higher year-over-year. And we grew adjusted EBITDA to $264 million, for an increase of 28%, excluding real estate gains in 2022. Our adjusted diluted EPS for the company was $0.77, which was also better than expected. I want to thank our team for delivering these great results in a soft freight environment.

Looking at our North American LTL segment, we reported our strongest progress since we launched our LTL 2.0 plan in 2021. We grew adjusted operating income year-over-year by 51% and improved our adjusted operating ratio by 380 basis points. We delivered the best damage claims ratio in our history at 0.3%, as well as a record level of employee satisfaction. And we significantly accelerated our year-over-year yield growth, excluding fuel, to 10.3%. We also improved cost efficiency for the fourth consecutive quarter with further increases in labor productivity and linehaul insourcing. And we continue to deploy capital efficiently as we reinvest back into the business.

All of these are proof points that our plan has strong traction. And the 28 service centers we recently acquired from the Yellow Network will build on this momentum. This acquisition is a once-in-a-generation opportunity to integrate prime locations into our network to support yield growth and margin expansion. When the market recovers and industry capacity tightens, we'll be in a stronger position to serve our customers and drive profitable growth for years to come.

Now I want to share some details of the quarter, starting with the first pillar of our LTL 2.0 plan: service improvements. We improved every major component of customer service quality in the quarter, including our customer satisfaction rating, which has risen by more than 40% since 2021. Our on-time performance was 3 percentage points better than in the prior fourth quarter. And I mentioned that our damage claims ratio of 0.3% is a new record for us. To put that in context, it's a vast improvement from 1.2% when we launched our plan. These are metrics our customers watch closely as an indicator of service quality. Our top priority is to become the customer service leader in our industry. And we're continuing to equip our team with the tools to make this a reality.

One example is the new freight airbags I spoke about on our last call. The rollout has been going well, and this solution is now installed at over 50% of our doors. The airbags have reduced damages by more than 20% at those locations, and the benefit will spread across our network. We expect to finish the installations by the middle of this year.

The second pillar of LTL 2.0 is to invest in our network to drive long-term growth. We added more tractors and trailers in 2023 than any year in XPO's history, to both grow and refresh our fleet. This resulted in record network fluidity and supported our strategy to insource more linehaul miles.

On the tractor side, we purchased more than 1,400 units in 2023. This reduced our average fleet age to 5 years at year-end, compared with 5.9 years in 2022. On the trailer side, we manufactured over 6,400 units at our in-house facility in Arkansas, exceeding our production target.

For 2024, we expect our LTL CapEx level to be in the low teens as a percent of revenue, and again, primarily allocated to our fleet.

In terms of the 28 service centers we acquired from Yellow, the largest impact on our capital strategy is timing. We've pulled forward dozens of real estate investments that we planned to make over the next several years.

I'll add some strategic color to my earlier comments on the acquisition. These service centers will deliver important benefits to the business for years to come. First, they'll get us closer to customers, and give us larger facilities in major metro areas. This should drive substantial cost efficiencies across our linehaul, pickup-and-delivery and dock operations.

Second, they'll enhance our yield growth by further improving our service with fewer freight rehandles, reduced damages, and better on-time performance. And third, they'll give us more capacity in key metros like Indianapolis, Columbus and Las Vegas. These are markets where we are currently turning away profitable customers because we don't have enough door capacity. We plan to start bringing these locations online in April and have all of them operational within the next 12 to 18 months.

We expect the transaction to be accretive to EPS and our LTL operating ratio in 2025. This assumes no underlying recovery in industry volumes. Any market rebound would represent an upside to our baseline forecast.

The third pillar of our plan is to drive above-market yield growth, which is our single biggest lever for margin improvement. You can see this dynamic in the fourth quarter when we drove yield, excluding fuel, higher year-over-year by 10.3%. This helped us deliver nearly 400 basis points of adjusted operating ratio improvement.

We got there by executing on service improvements, accessorials and volume growth within our local customer base. These are the 3 levers of our long-term pricing opportunity.

The exciting trends in our service metrics translate to value for our customers, with a direct correlation to the price we earn. Increasingly, our customers see XPO as a high-value business partner with the resources to help them succeed. This was reflected in our contract renewal pricing, which was up year-over-year by 9% for the second consecutive quarter.

Accessorials are another opportunity to grow our yield, by delivering more value through premium services. We plan to expand our range of offerings this year. We saw an early impact in the fourth quarter with the introduction of our retail store rollout offering. We already have over a dozen customers using this service to distribute critical product launches for retailers.

And with the third lever, our local channel, we grew shipment counts by double digits for the third consecutive quarter. Our local sales team at year-end was over 20% larger than in 2022, reflecting the importance we place on this high-yielding margin-accretive business. So we have a lot of avenues leading to yield growth, and each step forward helps to align our pricing with the value we deliver.

The fourth and final pillar of LTL 2.0 is cost efficiency. The main opportunities here are with purchased transportation, variable costs and overhead. In the fourth quarter, we reduced our purchased transportation cost by 22% year-over-year by in-sourcing more miles and paying lower contract rates to third-party providers. We ended the quarter with less than 20% of linehaul miles outsourced, for a year-over-year reduction of 290 basis points. On a sequential basis, we reduced our reliance on outsourcing by 190 basis points.

We've come a long way since the beginning of 2022 when we were outsourcing about 25% of our linehaul miles. Today we're well on the way to bringing down that percentage to the low teens by 2027.

Lastly, a quick update on our initiative to add driver teams in sleeper cab trucks for long hauls. The goal here is to increase the efficiency and flexibility of our linehaul network. We started putting these teams in place last quarter, and we currently have over 50 teams in operation. We expect to have a few hundred long-haul teams on the road by the end of this year. This should help to accelerate our in-sourcing plan.

We're also continuing to manage our variable labor costs effectively, growing our volume by more than our head count year-over-year for the fourth consecutive quarter. And the spread in the quarter was substantial. Our shipment count was up 5.7%, while our head count was up just 1.7%. This is a credit to the team's operational discipline, supported by our proprietary technology for labor planning.

In summary, in 2023 we made significant progress on our plan across the board, while laying a solid foundation for the future. We improved our operations in all 4 quarters of the year, by generating record service levels, making strategic investments in the network, further accelerating yield growth, and operating more cost efficiently. As a result, the business performed above expectations, with robust margin expansion and earnings growth and strong forward momentum.

Now I'm going to hand the call over to Kyle to discuss the fourth quarter financial results. Kyle, over to you.

Kyle Wismans ***XPO, Inc. - CFO***

Thank you, Mario, and good morning, everyone. I'll take you through our key financial results, balance sheet and liquidity.

It was a strong fourth quarter overall. Revenue for the total company was $1.9 billion, up 6% year-over-year. This includes a 9% increase in our LTL segment. Excluding fuel, LTL revenue was up 14% year-over-year.

Salaries, wages and benefits for LTL were 10% higher in the quarter than a year ago. The increase primarily reflects wage and benefit inflation, as well as incentive compensation aligned with our strong fourth quarter performance. These impacts were mitigated by our productivity gains. We've now improved our labor hours per shipment on a year-over-year basis for 4 straight quarters throughout 2023.

We were also more cost efficient with purchased transportation through a combination of in-sourcing and rate negotiation. Our expense for third-party carriers was $83 million in the quarter, which was down year-over-year by 22%.

Depreciation expense increased year-over-year by 23% or $13 million as we continued to reinvest in the business. This remains our top priority for capital allocation in LTL. In the fourth quarter, our CapEx was primarily allocated to our fleet, as we purchased new tractors from the manufacturers and build more trailers in-house.

Next, I'll add some detail to adjusted EBITDA, starting with the company as a whole. We generated adjusted EBITDA of $264 million in the quarter, up 28% from a year ago and improved our adjusted EBITDA margin by 230 basis points. These metrics exclude the impact of real estate gains in the fourth quarter of 2022, to give you a like-to-like comparison. We had no real estate gains in the fourth quarter of 2023.

Our fourth quarter corporate expense was $5 million, for a year-over-year savings of 44% or $4 million. We're continuing to rationalize our corporate structure for the stand-alone business and expect to report further reductions this year.

Looking solely at the LTL segment, we grew our adjusted operating income by 51% year-over-year to $160 million. And we grew adjusted EBITDA to $233 million. The gains we achieved through revenue growth and cost efficiencies more than offset the nonoperational headwinds from lower fuel surcharge revenue and pension income.

In our European Transportation segment, adjusted EBITDA was $36 million for the quarter.

Company-wide, we reported operating income of $119 million for the quarter, compared to $4 million in the prior year. Our net income from continuing operations was $58 million, for diluted earnings per share of $0.49, compared with a loss of $36 million or $0.31 a year ago. This represents an improvement of $0.80 in diluted EPS from continuing operations, driven by significant year-over-year reductions in transaction and integration costs and restructuring charges.

On an adjusted basis, our EPS for the quarter was $0.77, which is down 21% from a year ago. This primarily reflects the impact of real estate gains in 2022 as well as lower pension income and higher interest expense in 2023. Our acquisition of the 28 service centers closed on December 20, and did not have a material impact on our operating results and income statement.

And lastly, we generated $251 million of cash flow from continuing operations in the quarter and deployed $151 million of net CapEx, excluding spend related to the acquisition.

Moving to the balance sheet, we ended the quarter with $412 million of cash on hand. Combined with available capacity under committed borrowing facilities, this gave us $920 million of liquidity. We had no borrowings outstanding under our ABL facility at quarter-end.

In December, we raised $985 million through a combination of $585 million of senior notes and $400 million of term loans. We used $870 million of proceeds to complete our acquisition of 28 LTL service centers, and we refinanced our existing senior notes due in 2025. We now have no funded debt maturities until 2028. We also maintained all corporate and issue-level credit ratings.

Our net debt leverage at year-end was 3x trailing 12 months adjusted EBITDA.

The investments we're making in the business will enhance our earnings trajectory for a high return on capital, consistent with our long-term goal of achieving an investment-grade profile.

Before I close, I'll summarize the full year 2024 assumptions we provided in our investor presentation to help you with your models. They are as follows. Gross CapEx of $700 million to $800 million. Interest expense of $240 million to $260 million. Pension income of approximately $25 million. An adjusted effective tax rate of 23% to 25%. And a diluted share count of 121 million shares.

Now I'll turn it over to Ali, who will cover our operating results.

Ali-Ahmad Faghri ***XPO, Inc. - Chief Strategy Officer***

Thank you, Kyle. I'll start with our LTL segment, which reported another quarter of profitable growth.

On a year-over-year basis, we increased our shipments per day by 5.7% in the quarter, led by 12% growth in our local sales channel. This resulted in growth in tonnage per day of 2%. Our weight per shipment was down 3.4% year-over-year, which was notably less of a decline for the second consecutive quarter. On a monthly basis, our October tonnage per day was up 2.5% year-over-year. November was down 0.5%, and December was up 3.6%. Looking just at shipments per day, October was up 6.2% year-over-year, November was up 3.7%, and December was up 6.6%. In January, our tonnage per day was down 1.1% year-over-year, while shipment count was up 1.4%. The transportation industry was disrupted by weather events in January, but we saw a rebound more recently and ended the month with stronger volumes.

And sequentially, both our tonnage and shipment count increased from December to January, outperforming seasonality.

We also outperformed on yield in the fourth quarter, delivering a second consecutive quarter of acceleration. We grew yield, excluding fuel, by a strong 10.3% compared with the prior year. Importantly, our underlying pricing trends are strong as we continue to align our pricing with the better service we're providing. Our contract renewal pricing was up 9% in the quarter compared with a year ago.

Turning to margin. Our fourth quarter adjusted operating ratio was 86.5%, which was an improvement of 380 basis points year-over-year. Our strong margin performance was primarily driven by yield growth and underpinned by our cost initiatives and productivity gains. Sequentially, our adjusted OR increased by 30 basis points, which outperformed seasonality by 280 basis points.

Moving to our European business, we delivered revenue growth of 2% year-over-year, despite ongoing challenges in the macro environment. This growth was supported by strong pricing, which outpaced inflation. And in some regions like the U.K., we grew adjusted EBITDA versus the prior year, reflecting disciplined cost control. While our volume declined slightly year-over-year, we outperformed the industry, and we mitigated the decline with new customer wins as the quarter progressed. And this trend improved in January.

The team is executing well and earning new business from high-caliber customers. This momentum, together with the growth of our sales pipeline, should continue to strengthen our position in key European regions.

I'll close with a summary of the 3 main achievements you heard from us this morning, as they relate to our expectations for a strong 2024. First, we're continuing to deliver more value for customers in the form of service quality with our metrics at record levels. And we're on an excellent trajectory.

Second, we accelerated yield growth to double digits as we exited 2023, and we expect to deliver another robust yield performance this year with a direct benefit to profitability. And third, we're showing that we can operate more productively by leveraging our technology and improving our cost to serve.

In short, we've taken major strides with our network operations, and we're still in the early innings of significantly improving our operating ratio.

Now we'll take your questions. Operator, please open the line for Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Our first question is from Scott Group with Wolfe Research.

Scott H. Group ***Wolfe Research, LLC - MD & Senior Analyst***

Any thoughts on how to think about the OR from Q4 to Q1 and maybe full year margin improvement? And then, bigger picture, Mario, you made a comment that all this terminal growth is additive to yields and margins. I guess, that's why it should be good for volume, but maybe some thoughts on how it actually helps yield and margin as well?

Mario A. Harik ***XPO, Inc. - CEO & Director***

Sure. Thanks, Scott. First, starting with the first quarter outlook. We typically give tonnage yield and what OR would look like. Starting with tonnage, following the gains we had in the fourth quarter, we do expect to outperform seasonality in Q1. Typically, a normal seasonality for us is, call it, flattish tonnage sequentially from Q4 to Q1, and we expect to do better than that. So we expect Q1 tonnage should be up low single digits, somewhat in the same ZIP code as where we were in the fourth quarter on a year-on-year basis.

Now when you look at January tonnage specifically, it did do better, as Ali mentioned earlier, compared to seasonality when you roll forward December into January. And we had a strong end of the month as well, despite the weather earlier in the month.

On the yield front, we expect a strong performance for yield across the board this year. We do expect yield to be up on a year-on-year basis in the first quarter, somewhere in the same ZIP code as we were in the fourth quarter year-on-year. And ultimately, from an OR standpoint, usually, typical seasonality for us, Q4 to Q1, we see OR deteriorate about 40 basis points, and we expect to do better than that. Now how much better will depend on how the rest of the quarter plays out. Usually in Q1, as you know, March is the big month of the quarter. But that implies roughly 300 basis points of OR improvement year-on-year.

For the full year 2024, we also expect a strong year for us in terms of OR improvement. Given all the things we're doing in yield, tonnage, cost and efficiency improvement and service improvement, we expect OR to be up in the 150 to 250 basis points range for the full year. And there's a path for us to do better than the top end of the range, depending here on how the year plays out.

Now taking a step back on your question on the acquired (added by company after the call) service centers and how they impact yield. So we see a big cost benefit first, and that cost benefit comes from higher efficiency and having bigger break bulks that lead to cost savings and linehaul, having service centers closer to the customer leads to lower P&D cost and also lowering dock-handling costs associated with that. Now the way they help yield is because larger service centers help improve your service product and service product can drive yield.

But also we mentioned premium services. And when you think about premium services in some markets like Las Vegas, we're tapped on capacity. And by having now the largest service center in the biggest market, we're going to be able to launch new offerings, like trade shows as an example, and this comes also at a higher yield and higher margin as well.

Operator

Our next question is from Ken Hoexter with Bank of America.

Kenneth Scott Hoexter ***BofA Securities, Research Division - MD & Co-Head of Industrials and Basic Materials***

Congrats on some solid performance here on the OR. Maybe just digging into that, though. Talk about the ramp of the 28 facilities. How should we anticipate the drag versus your forecast? And I guess with that, it seems like you're bumping up against your kind of long-term targets now of the 600 basis point improvement. How -- does that shift or the speed with which you can get there start changing in your thought process?

Mario A. Harik ***XPO, Inc. - CEO & Director***

Thanks, Ken. Starting with the ramp of the service centers. In terms of getting them up and running, we do expect to get them up and running in -- the first dozen or so service centers, over the next 3 to 6 months, the next dozen over the next 6 to 12 months, and then the remaining 4 or 5 will go live next year, call it, 12 to 18 months.

Now we don't anticipate an OR drag from them that would be material to our numbers. And the reason why, because the majority of these service centers are in markets where we already operate. So if you think about it, there is one case where we move our team, our existing team, from a smaller service center to a larger service center. The carrying cost of real estate is fairly low on a per door basis, but we get the immediate benefit of cost efficiencies and cost savings associated with having a larger facility to operate from.

In markets where we are adding a service center and keeping the existing one, in that particular case, we split the team between the 2 service centers based on volume, and we only step up if there is an inflection in volume and we have incremental volumes.

So we don't anticipate the service centers to have a drag on OR this year. We do expect them to be accretive for EBITDA. We do expect a drag on EPS driven by the incremental debt. And we expect them to be accretive on all these KPIs in 2025 and beyond.

In terms of the long-term targets, we've always said 600 basis points -- I mean, at least 600 basis points. And there's nothing magical about 600 basis points, there's nothing magical about 2027. With all the momentum that we have here and with all -- with the new service centers, the pricing, the service improvements, we do expect to outperform, and I would hold us to get to the 70s and well into the 70s over time from an OR perspective.

Operator

Our next question is from Jon Chappell with Evercore ISI.

Jonathan B. Chappell ***Evercore ISI Institutional Equities, Research Division - Senior MD***

I'm not sure if Mario or Ali wants to take this, but this is the second straight quarter now with contract renewal pricing up 9%. Where do you stand on the book of business as it relates to kind of marking to market for the new service? Do you still have a couple more quarters where you think that kind of high single-digit contract renewal is on the agenda? Or are you kind of close to kind of marking it to market and you think maybe that moderates a little bit to maybe mid-single digits, in line more with the GRI levels?

Kyle Wismans ***XPO, Inc. - CFO***

Jon, it's Kyle. So if you think about contract renewals right now, we did accelerate heavily in the back half from 5% to 9%. And so far in the year -- or in the back half, we negotiated 50% of the book. So there's still some more to work through. I still think we're in a favorable market for renewals, and we should expect positive momentum to carry forward here in 2024.

Jonathan B. Chappell ***Evercore ISI Institutional Equities, Research Division - Senior MD***

Just to be clear, though, it's like if you're done with 50%, is this the first half higher end of that range, reacceleration similar to the back half of '23, and then kind of more of a normalized level in the back half? Or do you think that what you've done over the last 6 months, as you continue to improve service, kind of lead you more towards what you've done in the last 6 months or so, on a percentage basis?

Kyle Wismans ***XPO, Inc. - CFO***

I think renewals are probably going to follow where we see yields for the first half. So we're expecting strong yield to continue. If you think our Q1 yield guide, we think Q1 yield is going to be up high single digit, in line with what we saw in Q4. That should carry forward into our contract renewals to the start of the year.

Operator

Our next question is from Chris Wetherbee with Citigroup.

Christian F. Wetherbee ***Citigroup Inc., Research Division - MD & Lead Analyst***

I guess I want to talk a little bit about some of the initiatives that maybe you guys are thinking about for 2024. So we've talked about sort of the team drivers, you talked about the in-sourcing of linehaul. Curious kind of, as you start to think about adding those up in the context of the 150 to 250 basis points of OR improvement, how much you get from that versus maybe what would be kind of core pricing above cost inflation and maybe a little bit of leverage on the volume? I don't know if you can unpack that, but any detail you can give us would be great.

Mario A. Harik ***XPO, Inc. - CEO & Director***

I'll talk on the initiatives. And Chris, the way we look at it, our plan involves substantial yield improvement. It does involve continuing our great service momentum or service product improvement momentum. Tonnage improvement, we do see tonnage going up for the full year, but we do expect it to be up, call it, in the same ZIP code of where we were in the fourth quarter, so low single digit, because our goal is to drive more yield than it is to drive volume. Similarly, our goal is to drive cost efficiencies, as you mentioned. So I'll give a quick update on the initiatives.

Part of our plan is to in-source more third-party linehaul miles because that comes both at a cost benefit, but it also comes as a service benefit. When we go from using a third-party carrier with a 53-foot trailer versus having two 28 feet pups, which gives us more space, gives us safe stack into the trailers where we can separate the freight physically, and our drivers show up on time 100% of the time, we can continue to improve that service product. Now that will come with cost savings here in 2024, but the longer-term cost savings also come when you think of an inflection in truckload rates at some point, that's going to be obviously material savings for us from what we would be spending internally on a per mile basis versus what we're spending for third-party carriers.

So our expectation is to continue to -- we insource 290 basis points here in the fourth quarter year-on-year. We are sub-20% at this point, we're at 19%-and-change. And we're going to drive that in the first phase down to the low teens and beyond that as we ramp up those teams as well.

Operator

Our next question is from Fadi Chamoun with BMO Capital Markets.

Fadi Chamoun ***BMO Capital Markets Equity Research - MD & Transportation Analyst***

So my question is you mentioned the double-digit growth that you're seeing in the local accounts. I'm thinking this has obviously been a pretty decent tailwind for density and cost per shipment and, ultimately, the yield. Where are you in this kind of trajectory of improving local account penetration? Are we in the first innings of that? Is there an opportunity that is of significant size still in front of you?

Mario A. Harik ***XPO, Inc. - CEO & Director***

When you look at the local account strategy, Fadi, it is a segment that we are planning on growing over the years to come here. Now if you look back at 2023, we were run-rating at roughly 20% of our volume and revenue generated from that channel. Now what we have done through the course of the year is that we increased the size of our local accounts. We hired more than 20% local sellers through the course of 2023. And the goal here through 2024 is to add roughly another 10%. So, all in, to be 30% higher on the overall sales force size that is selling to that channel.

Now as you can imagine, whenever we onboard new people, it does take a ramp, usually about 6 months, for them to be fully productive and fully up and running. Now if you look at the full year, we did improve our local accounts -- on a higher run rate than the rest of our book. Here in the fourth quarter, we grew our local shipments in that channel by 12% on a year-on-year basis. And we do expect to continue to see those really strong gains in that channel since we onboarded 20% more sellers.

Now in terms of the innings, I would say, we're still in the early innings in terms of results, but we are very well underway in terms of having the team, and having them see a couple of quarters of ramp here to be pretty productive in 2024 and beyond.

Operator

Our next question is from Stephanie Moore with Jefferies.

Stephanie Lynn Benjamin Moore ***Jefferies LLC, Research Division - Equity Analyst***

I wanted to maybe touch a bit on the, I guess, continuing on the pricing discussion here. I think as pricing accelerated over 10% here in the quarter. I think you guided to more high single digits. Can you maybe walk through the drivers of the upside? What you're seeing and kind of your thoughts as we think about 2024 for further pricing acceleration, especially your view of what can happen if the macro does actually turn.

Ali-Ahmad Faghri ***XPO, Inc. - Chief Strategy Officer***

Sure, Stephanie. This is Ali. So we're seeing very strong pricing trends as we enter 2024. For the first quarter in particular, we would expect our yield on an ex fuel basis to be up somewhere in the similar range as we just delivered here in the fourth quarter. So call it roughly about 10% growth.

Now on a full year basis, we would expect yield to be up somewhere in that mid- to high single-digit range. I would add that there's certainly a path to do better than that. It's still very early in the year. So we'll update you as the year progresses.

A lot of that yield growth and the outperformance versus the industry is being driven by our internal initiatives. If you think about our service improvement, we're at record levels here in the fourth quarter. We're continuing to lean more into premium services. We rolled out retail store rollout here in the fourth quarter. We have a lot of traction there. And as Mario just noted, a lot of momentum on the local side as well, too, and this is higher yielding and margin-accretive business.

So overall, we feel very good about the yield outlook here in 2024 and expect it to be a strong year for us overall.

Stephanie Lynn Benjamin Moore ***Jefferies LLC, Research Division - Equity Analyst***

Maybe just a follow-up to that, a little bit bigger picture, as you think about incentive comp across the organization, maybe talk a little bit about what metrics that have been possibly realigned just to align interest across the organization, yield, margins, EBIT, what's the major metrics we should be focused on based on incentive comp changes in 2024?

Mario A. Harik ***XPO, Inc. - CEO & Director***

Stephanie, this is Mario. I'll take that. So in 2023 and 2022, we used to compensate predominantly our field based on EBITDA growth and EBITDA performance. But we have added a good portion of the comp plan to be more focused on service quality. So as service centers and group service quality and on-time service, they effectively -- they have a good chunk of their incentive comp based on that.

Now in 2024 will be the first year where we are switching from compensating our field from EBITDA and EBITDA growth and have it be focused on OR improvement. So it's now focused on how can we expand our margins over time. Because as you know, we want to incentivize effectively driving that better service product that leads to higher yield, while managing costs effectively, which would lead to OR expansion at the service center level and ultimately at the network level as well.

Operator

Our next question is from Tom Wadewitz with UBS.

Thomas Richard Wadewitz ***UBS Investment Bank, Research Division - MD and Senior Analyst***

I just had, I guess, one kind of quick one on the D&A and maybe how we think about the ramp-up in that given you are spending a good level of CapEx. So on that. But I guess a broader question would be on how you think about the terminal network. And I guess what's -- as you bring on terminals, like where you sit today, what's your excess capacity from a door and a terminal perspective?

And as you bring on more terminal capacity, kind of where do you want to get to? I think we've seen that a high service model, you do have some decent amount of excess capacity. But I kind of wanted to see where you're at today, where you'd like to get to on excess capacity? And then a specific one just on kind of D&A modeling.

Mario A. Harik ***XPO, Inc. - CEO & Director***

Thanks, Tom. I'll start with the network and the capacity side and turn it over to Kyle for D&A. When you look at our network today, before the 28 service center acquisition, we were run-rating call it in the mid- to high teens in terms of excess capacity in the current environment. And if we roll forward, we are adding 28 service centers: out of these, roughly half of them would be additive and the other half would be ones where we are relocating from a smaller service center to a larger service center. And we roughly acquired about 3,000 doors, and we would be adding a net, after we're all said and done with the integration, a net 2,000 doors, which is call it a 10%, 15% expansion in capacity. So once we get these service centers online, we will be in the 25% to 30% excess capacity in our network.

And that's a great place to be as an LTL network, especially in a soft freight market. So this way, whenever there's a freight market recovery and you see higher demand, our industry has been capacity constrained. Real estate comes with a very low carrying cost and this would enable us to flex up whenever that demand comes back. So this is how we look at currently where we are and as we open up those service centers where we'll be adding from a capacity perspective.

Kyle Wismans ***XPO, Inc. - CFO***

Yes, Tom. And if you think about the D&A ramp, so we are going to see increased CapEx within the LTL segment. So we'd expect about $74 million to $75 million a quarter for LTL, reflecting the increased CapEx spend.

Operator

Our next question is from Bruce Chan with Stifel.

Jizong Chan ***Stifel, Nicolaus & Company, Incorporated, Research Division - Associate VP & Equity Research Analyst***

Maybe just to start, Kyle, can you remind us of what your target leverage range is? And then I know in previous quarters you pulled back on some of the commentary around the sale of the European business. But with the need for more debt pay-down potentially with these new facilities, is there any more urgency to sell that business now?

Kyle Wismans ***XPO, Inc. - CFO***

Bruce, it's Kyle, I'm going to start, and then I'll hand it over to Mario. So when you think about our long-term leverage outlook, our intention is 1 to 2x trailing 12 months EBITDA. And we think we're in a great spot with the investments we made and the EBITDA we can generate to really make a lot of progress on that here in the next couple of years.

Mario A. Harik ***XPO, Inc. - CEO & Director***

And on the European sale, Bruce, our long-term plan remains to be a pure-play North American LTL carrier, and selling the European business is one of our strategic priorities. But we're going to be patient. Our goal is to maximize the return we get on that business. It is a business that has a scarcity value to it. We're either #1, 2 or 3 in less-than-truckload, truckload, asset-light brokerage in many geographies in Western Europe, think U.K., France, Spain, Portugal. And it's not a matter of if but a matter of when.

And meanwhile, if you take a step back, the business is performing well despite a soft economy in Europe with outperforming our peers, our revenue was up in the quarter. We've improved volume every month of the quarter and further improved in the month of January. And so credit to the team's strong execution. So again, if you take a step back, it's a matter of time and at some point we'll get there.

Operator

Our next question is from Jason Seidl with TD Cowen.

Jason H. Seidl ***TD Cowen, Research Division - MD & Senior Research Analyst***

Mario, I think you talked about accessorials and that there's about 12 different things that XPO was doing to drive them higher. Can you help us understand the timing and the ability -- your ability to implement these accessorials and the impact we should expect?

Mario A. Harik ***XPO, Inc. - CEO & Director***

So when you take a step back on these accessorials, they are predominantly what we call premium services. So these are services that our customers are asking for, that go beyond your typical pick up a few skids of freight and get them delivered to a destination. So examples are, as Kyle mentioned earlier, the retail store rollouts offering, where in that particular case, you can imagine if you have some sort of a holiday or a new product launch, a customer needs us to ship many, many shipments, it could be hundreds of shipments in a short time window, and they need somebody to coordinate all of those offerings. And that leads obviously to a higher price and the customer is happier because they're getting a service that they need.

We do have a number of other offerings. Trade shows is a good example of that. Working with retailers on a "must arrive by date"-type offering, and many others that we are launching through the course of the year here. We do expect to get them launched. They won't all be launched within a few quarters. Some of them will take a bit longer, like an expedited service as an example. But as we launch these, we expect them to be accretive to yield over time.

In terms of magnitude, roughly today, our accessorials as a percent of revenue is roughly around -- call it in the low double digits. And our goal is to grow that to the mid-teens as we launch these programs over the years to come.

Jason H. Seidl ***TD Cowen, Research Division - MD & Senior Research Analyst***

That's great color. I wanted to also follow up on the overall pricing discussion. LTL pricing this quarter has been very strong. Your renewals are at 9%, Saia is almost at 9%. ArcBest is the best they've reported since a quarter in '22. And this is all in a very sluggish demand backdrop and super cheap TL pricing. As the economy recovers and capacity tightens overall, is it crazy to think about double-digit pricing going forward for you guys?

Mario A. Harik ***XPO, Inc. - CEO & Director***

We had double-digit pricing up here in the fourth quarter, and we do expect a very strong first half of the year as well. I mean, this is an environment. If you look at our industry, it's been historically capacity constrained. If you go back before Yellow ceased operations, we didn't have enough capacity versus the demand that was out there. We are currently in a sluggish freight environment where demand is down, roughly, call it double-digit low teens, and this is when that capacity went away from the market. So whenever there is any sort -- even with some of that capacity coming back into LTL, whenever there's any form of inflection in demand, there wouldn't be enough doors and service centers in our industry. So you would see pricing accelerate accordingly.

For us specifically, we also have all the company-specific initiatives we're driving between driving better service, which comes at a premium, between driving premium services, which has been driving also expansion of our local channels. All of these would be accretive to yield as well. So double-digit pricing is not out of the question.

Operator

Our next question is from Bascome Majors with Susquehanna.

Bascome Majors ***Susquehanna Financial Group, LLLP, Research Division - Research Analyst***

I wanted to go back to the incentives focus from earlier. Can you talk more specifically about how you're tactically incentivizing your salespeople specifically and if that has changed at all as the business has evolved and your priorities have evolved over the last 10 months? And separately, from a long-term senior executive management incentive approach, how might those look different this year than they have over the last few years?

Mario A. Harik ***XPO, Inc. - CEO & Director***

Thanks, Bascome. So first, starting with the sales compensation. So it depends on what type of seller you are in the organization. We changed the comp plan accordingly. So if you're in the local channel, the goal is to grow your book as opposed to, for example, if you're in different types of accounts, you're going to have to focus on profitability more. But generally, the theme is that, if you look at a service center, they are compensated based on the OR improvement for that specific service center. If you're a local account executive, you're incentivized to grow your book, and a component of your compensation is driven by operating ratio as well. If you're handling larger accounts, then the lion's share of your compensation is around OR and profit improvement as well associated with that.

So this is how typically sales are compensated, but it is more driven by your book of business as opposed to your region or the network as a whole.

Now in terms of senior exec compensation, that's typically part of our proxy. But we incentivize our senior executives based on a combination of OR growth, EBITDA growth, and the TSR, so shareholder value creation as well.

Bascome Majors ***Susquehanna Financial Group, LLLP, Research Division - Research Analyst***

And you don't expect the long-term incentive formula to really change other than the targets for this 3-year period?

Mario A. Harik ***XPO, Inc. - CEO & Director***

The framework would be very similar to what we had in the past.

Operator

Our next question is from Jordan Alliger with Goldman Sachs.

Jordan Robert Alliger ***Goldman Sachs Group, Inc., Research Division - Research Analyst***

Just sort of curious, thanks for the layout in terms of the door opening timing, etc. In the context of your thoughts on the economy and the new door openings, is there a way to think about tonnage or volume trajectory as we go through the year, sort of like year-over-year growth potential or how you expect it to sort of ramp up? That would be the first question.

Ali-Ahmad Faghri ***XPO, Inc. - Chief Strategy Officer***

Sure, Jordan. This is Ali. I'll then pass it to Mario. So for the full year, as we noted, we expect a much higher contribution from yield and volume. We're being very disciplined on the type of volume we're onboarding onto the network, and you should expect that to continue through this year.

So overall, for the full year, we'd expect tonnage to be up somewhere in that low single-digit range for the full year and then yield somewhere in that mid- to high single digits or better. Now keep in mind, we do have tougher comps in the second half of the year. It is still early in the year and obviously, the macro can be a swing factor.

In terms of the new service centers, we don't expect any sort of meaningful contribution from volume this year. We would expect contribution from volume to be sub 1% of incremental volumes, so not a meaningful number overall.

Mario A. Harik ***XPO, Inc. - CEO & Director***

When we think about the service centers in the near term, ahead of any type of macro infection whenever it comes, there is a big benefit we're going to get from cost savings, as I mentioned earlier on, by having larger facilities. If you think about what we bought from the Yellow Network, we bought some of the largest service centers. You look at a site like Carlisle, you can't get any more than 120 acres of land right off I-76 and I-81, where we have a 300-door service center now in that market. Same thing with Nashville. We got a 40, 50-acre facility west of Nashville, with more than 200 doors in it.

So when you think about those larger facilities that enable you to run more efficiently, your linehaul, your T&D, your dock operations, that's going to lead to cost savings as soon as we start moving into them.

The other benefit is some markets, when you look at a market like Brooklyn, New York or Columbus or Indianapolis or Las Vegas, we're tapped out on capacity today. So we don't have enough doors in those markets. And by having this incremental capacity, we already have customers that are ready to go where we can onboard them as we open up those service centers.

And we have 2 small service centers. One is in Eau Claire, Wisconsin, one is Nogales, Arizona, where we -- these are net adds or new markets. But these are small service centers where we already have demand lined up based on existing customer relationships we have as well.

Jordan Robert Alliger ***Goldman Sachs Group, Inc., Research Division - Research Analyst***

Got it. And then just sort of curious, how you're going to manage the terminal opening? So in other words, is there some economic dependency on it, how good the economy is? Or is there going to be a certain amount that you're just going to open no matter what strategically or otherwise?

Mario A. Harik ***XPO, Inc. - CEO & Director***

When we think about the rollout timing, we prioritize the service centers, those markets, where we are capacity constrained today. So in a softer freight environment where we see that we don't have enough capacity. And the second priority is based on cost efficiency, so the service centers that will create the most amount of cost efficiency.

And when we think about the opening schedule, I'll call it, over the next 3 to 18 months, it will be we're going to drive through it regardless of what the freight markets are doing. This would be a reasonable time frame in terms of bringing those terminals up to our standards and doing the rebranding and these kind of things to get them up and running.

And then we -- for us -- I mentioned this earlier on, if you think about the headcount, there's no need for us to hire people ahead of volume. So what we do is that we either relocate the existing team into a larger facility, or we add a facility to an existing market where we split a team from an existing facility into 2 different service centers, so there's no incremental cost associated with that. If we do see an inflection in volume where the markets are getting better, then we staff up to be able to support that volume.

And importantly, Jordan, if you look at our year in 2023, we were able to improve efficiency every single quarter of the year. So we have the great ability between operational discipline that Dave and the team are bringing to the table, supported by our proprietary technology, to be able to run our network very efficiently from a labor standpoint.

Operator

Our next question is from Brandon Oglenski with Barclays.

Brandon Robert Oglenski ***Barclays Bank PLC, Research Division - VP & Senior Equity Analyst***

Mario, maybe we can follow up on that one there. I know you're talking about cost efficiencies of opening new terminals in the network. And it sounds like potentially you're going to move staff from one to the other. But I guess just covering transports for 20 years now, when you open new nodes in the network, especially scheduled network, isn't there like a spool of time on capacity efficiencies, especially on like linehaul and local pickup and delivery that we should be anticipating? Because it sounds like what you're guiding to, that you can instantly match efficiency, if not even get better, with these new facilities.

Mario A. Harik ***XPO, Inc. - CEO & Director***

Whenever you open up sites, you do have a small headwind in cost, but that for us would be a very short-lived. I mean, you're talking 30 to 90 days of cost headwind as you move into a larger facility. And predominantly, it comes from the carrying cost of the incremental doors. But Brandon, keep in mind that the cost of a door in our P&L is sub 5% as a percent of total. So it's a small incremental cost associated with that.

But when you think about the immediate efficiency you gain in pickup and delivery and linehaul, in all of those pieces, this is where we see that this drag is short-lived. It doesn't have a meaningful impact on the network as a whole.

And to give you an example, over the last couple of years here, we've opened up a dozen service centers, and each one of them was accretive within 30 to 60 days. Each one of them is exceeding our return hurdles as well. So we feel very good about our ability to get those onboarded with very minimal drag. And that's the reason why we don't expect any drag from an OR perspective from the service centers.

And finally, I'd say also with having Dave on the team, he has an incredible amount of experience in terms of adding capacity to a network and making sure it's accretive pretty quickly.

Operator

Our next question is from James Monigan with Wells Fargo.

James F. Monigan ***Wells Fargo Securities, LLC, Research Division - Associate Equity Analyst***

Just wanted to come back to pricing a little bit. And of the pricing gap to peers, how much of that pricing gap is sort of attributable to service level differences? And you've improved service, a good fit here. So of that gap, how much sort of is accessible to you given where service is today?

Ali-Ahmad Faghri ***XPO, Inc. - Chief Strategy Officer***

Sure, James. This is Ali. So overall, we see roughly about a mid-teens pricing upside opportunity in the years to come. And it's primarily driven by 3 levers. First and foremost, it's driven by service. So as we continue to improve our service quality, we're going to be able to better align the price with the value we're delivering. We quantify that about half of that is mid-teens pricing gap, so call it about 700, 800 basis points of pricing opportunity as we continue to improve service. And we're realizing that right now. In the fourth (corrected by company after the call) quarter, we delivered a company record damage claims ratio and our yield growth accelerated to double digits. So we're in the early innings of realizing that opportunity.

Then you have another about 500 basis points or 5% of pricing upside that's tied to accessorials and more specifically premium services. As Mario noted earlier, we want to grow our accessorials as a percentage of overall revenue from roughly that 10% range right now to 15-plus percent over time. And that's about 5 points of pricing upside.

And then lastly, the local channel is also an opportunity for us from a pricing perspective. That's higher yielding and higher margin business for us. Currently, that's roughly about 20% of our revenue, and we want to grow that to 30-plus percent over time. And that's roughly about another 200 to 300 basis points of pricing upside.

So overall, there's multiple different levers we can pull to grow pricing. And as we move through 2024, we would expect those to translate to very strong yield growth for us.

James F. Monigan ***Wells Fargo Securities, LLC, Research Division - Associate Equity Analyst***

Got it. But given where service is today, the full 700 to 800 of price that is tied to service, is that like fully accessible to you? Or does service need to improve further in order for you to get that 700 to 800 basis points as you move through the contract repricing?

Mario A. Harik ***XPO, Inc. - CEO & Director***

It does take time. I mean it's not like a switch where, as you improve your service product, your customers will give you that premium immediately. But we're seeing -- we already have been seeing it play out in the course of 2023 when you look at the improvement we've seen in yield quarter after quarter, and having those very strong contract renewals.

So, if you go back 2 years ago, we had a damage claims ratio of 1.2%. We're down to 0.3%, which is a company record. But our goal continues to keep on improving that. We're a customer loving organization. We want to take care of our customers, pick up the freight on time, deliver it on time, deliver damage-free every single time. And if you think about it from that perspective, that over time earns you a premium. So when we think of that 7 to 8-point differential, it's going to take us a number of years to claw through it. But that's why when we look forward, we think of our ability to get this above market pricing is going to be driven by this continued improvement and continued focus on taking care of our customers.

Operator

Our next question comes from Brian Ossenbeck with JPMorgan.

Brian Patrick Ossenbeck ***JPMorgan Chase & Co, Research Division - Senior Equity Analyst***

So Mario, just to come back to the additional terminals and door counts. Can you give us a sense of what incremental margins overall you're assuming? And it sounds like they're reasonably high for not expecting any real OR dilution. And on that point as well, it's obviously a big purchase price, purchase price accounting takes a while to settle out, but isn't there a big D&A component from this as well? I know Kyle talked about the component before, but it sounded like that was primarily for CapEx. So it would be hopeful to hear a little bit about that.

If you can maybe just finish up with what you're seeing on the demand environment, haven't talked too much about that, seeing a little bit of improvement in PMIs, maybe some restocking ahead, but will be curious to see what you're hearing from your customers to start the year.

Mario A. Harik ***XPO, Inc. - CEO & Director***

Thanks, Brian. So I'll start first with the return on the service centers. And we expect that to be in the -- on the long run, to be in the 30% to 40% range. And I'll turn it over to Kyle shortly here to discuss the details of that.

Now when you think about the customer demand environment, it is a fluid environment. It is tough to call what the macro is going to do through the balance of the year. From one perspective, you see the rates where they are from a Fed perspective. We're seeing different mixed signals.

Now we do survey our customers on a regular basis. And for the first half of the year, roughly 2/3 of the customers are expecting either flat or slightly improving demand. So there is a bit more optimism in the first half than what we've seen in the back half of last year. But there's even more optimism for the back half where the majority of the customers did say that they expect a pickup in demand in the back half of 2024.

So we're cautiously optimistic, but it's tough to call the macro at this point. Now when you look at it more near term, you look at -- we do watch the ISM manufacturing index given 2/3 of our customers are industrial companies. And when you look through the course here of the fourth quarter, the trough was in October and November, we saw it get better in December, and here in January, it even further improved -- the ISM posted 49-and-change, which is very close to 50, which is typically your point where you start seeing an inflationary environment. So again, we're seeing demand hold. We're seeing demand slightly improve, and with more optimism towards the back half of the year.

Kyle Wismans *XPO, Inc. - CFO*

And then just to address the CapEx question associated with Yellow. When you think about the 28 service centers, we're expecting incremental CapEx about $1 million to $2 million per site, so about $50 million to $60 million in total. Now that's not spread evenly across all 28 service centers, and that's really largely tied to refreshing and refurbishing the sites, bringing up to standard. So it's going to cover construction, painting, rebranding. And that CapEx for those sites is included in our overall guide for the year. Some of these sites -- we already started to work on some of the locations. So going back to Mario's earlier comments, we expect something to come online here in Q2.

Operator

We have reached the end of our question-and-answer session. I would like to turn the call back over to Mario Harik for closing remarks.

Mario A. Harik *XPO, Inc. - CEO & Director*

Thank you, operator, and thanks all for joining our call today. As you can see from our results, our plan is working, and our service improvements are delivering revenue growth, margin expansion and earnings growth. Soon we're going to start integrating to acquired service centers into our network, which is now more productive and more cost efficient. We have a lot of strong momentum here as we start 2024, and we look forward to updating you on the next quarter.

Operator, you can now end the call. Thank you.

Operator

Thank you. This will conclude today's conference. You may disconnect your lines at this time, and thank you for your participation.