

August 3, 2023

RXO, INC. | RXO

BUY

A Freight Cycle Trough May be Near; Reiterate Buy, \$25 Target

PRICE \$19.64

PRICE TARGET \$25.00

KEY TAKEAWAY

RXO reported a 9% adjusted EBITDA beat (\$38M versus our \$35M) for Q2'23. Total revenue slightly missed our forecast (\$963M versus \$1.05B). Volume growth at brokerage was 10% yr/yr, which was the highest growth over the last 4 quarters. We believe that RXO continues to capture market share from competition, as the freight market contracts with best-in-class brokers and technology. Early trends for Q3'23 are consistent with brokerage volume growth and our thought is the freight cycle trough may be near. We have lowered our estimates for FY'23 and FY'24 given macro uncertainty surrounding consumers but believe that signs of a seasonal peak could provide upside. We reiterate our Buy rating and 12-month \$25 price target.

Transportation and Logistics

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KEY POINTS

Small beat in Q2. RXO reported Q2'23 adjusted EBITDA of \$38M, which was above our \$35M estimate and consensus of \$36M. The beat was driven by higher margins. RXO reported an adjusted EBITDA margin of 3.9%, which was ahead of our forecast by 60 bps. Total revenue of \$963M missed our \$1.05B forecast.

Trucking along the bottom. RXO reported yr/yr brokerage volume growth of 10%, which was an improvement from the 6% in Q1'23 and 4% in Q4'22. RXO continues to execute its plan of growing market share in turbulent freight times. Our sense is RXO continues to gain share from both large and small brokerage firms.

The volume growth was led by the truckload business, which also experienced an uplift in synergistic opportunities via less-than-truckload. RXO's brokerage business has benefitted from its ability to capitalize on its people, technology, and service to further prepare for an upward trending freight cycle.

Last mile—a business to rally behind. For us, the last-mile business outperformed expectations (\$261M versus our \$235M). At the end of Q1, RXO was able to increase pricing on its continued best-in-quality service offering. We anticipate expansion of these pricing initiatives given the flow of contract renewals throughout the year.

Q3 starting favorably. July trends seemed to continue the pacing in June, as both gross profit per load and truckload revenue per load stabilized sequentially. Furthermore, RXO grew volume yr/yr for the month of July, which gives the company confidence that yr/yr volume growth will continue into Q3'23.

Lowering estimates on uncertainty in the cycle. We are lowering our Q3'23 adjusted EBITDA to \$25M (from \$30M), largely to reflect the softened freight environment. Our FY'23 estimate goes to \$131M (from \$140M), and our FY'24 estimates goes to \$219M (from \$240M). Our belief is that if there is recovery to come in the cycle, Q3'23 may reveal early signs of that trajectory.

Maintain Buy, \$25 target. We are maintaining our Buy rating and 12-month price target of \$25. Our sense is the weakness of the current freight cycle has created a "perfect storm" for RXO to gain market share from competition and position itself for an inflection in the cycle.

COMPANY STATISTICS

52-Week Range	\$14.75-\$25.50
Market Capitalization (M)	\$2,346
Average Daily Volume (000s)	1,389
Debt/Total Cap	44%
Dividend	NA
Shares Outstanding (M) fd	119.5
Estimated 3-yr EPS Growth	-19%
Enterprise Value (M)	\$2,677
Float (M)	117.3

FINANCIALS

FYE Dec	2021A	2022A	2023E	2024E
P/E Ratio	13.3x	12.6x	78.9x	25.5x
EV/EBITDA	10.3x	8.7x	10.4x	12.2x
Revenue (M)	\$4,689	\$4,796	\$3,953	\$4,371
Op Inc (M)	\$192	\$123	\$35	\$147
EBITDA (M)	\$261	\$298	\$131	\$219
EPS (A) Q1	---	\$0.39	\$0.11A	\$0.12
Q2	---	\$0.56	\$0.08A	\$0.23
Q3	---	\$0.34	\$0.01	\$0.14
Q4	\$0.41	\$0.28	\$0.05	\$0.28
Total	\$1.48	\$1.56	\$0.25	\$0.77
Consensus	---	---	\$0.28	\$0.65

Consensus estimates from FactSet

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Valuation. RXO is currently trading at 20.4x our 2023 EV/EBITDA estimate. Our 12-month price target of \$25 is based on 15.3x our 2024 EV/EBITDA estimate and therefore assumes multiple compression. Average multiples among RXO's public peers are currently 14.4x 2023 EV/EBITDA. Our sense is the current macro environment continues to compress earnings expectations and multiples. Once the macro environment shows some form of upside, we believe multiples may expand.

Risks. Risks to the stock as well as to the achievement of our price target include macroeconomic conditions, increased competition, inability to increase technological innovation, the fluctuation around spot and contract rates, shipper contracts, and dependency on third-party carriers. In our view, the largest concern for RXO remains the uncertain macro environment impacting the transportation and logistics industry. However, we remain optimistic that RXO should continue to outperform its market opportunity and gain share from competition.

RXO, Inc.
Earnings Model

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(S Ms ex. Per-share)	2022A					2023E					2024E				
	Mar	June	Sept	Dec	Dec	Mar	June	Sept	Dec	Dec	Mar	June	Sept	Dec	Dec
	Q1	Q2	Q3	Q4	Year	Q1A	Q2A	Q3	Q4	Year	Q1	Q2	Q3	Q4	Year
Total revenue	\$1,312	\$1,226	\$1,138	\$1,120	\$4,796	\$1,010	\$963	\$975	\$1,005	\$3,953	\$1,038	\$1,075	\$1,083	\$1,175	\$4,371
Cost of transportation and services	1,021	904	857	842	3,624	759	723	745	760	2,987	790	805	820	885	3,300
Net revenue	291	322	281	278	1,172	251	240	230	245	966	248	270	263	290	1,071
Direct operating expense	55	56	56	59	226	61	59	60	61	241	60	60	61	61	242
SG&A	161	166	158	155	640	153	144	145	153	595	145	150	155	160	610
D&A	21	21	23	21	86	18	18	18	18	72	18	18	18	18	72
Transaction and integration costs	3	18	23	40	84	6	4	3	0	13	0	0	0	0	0
Restructuring costs & other	0	3	6	4	13	8	1	1	0	10	0	0	0	0	0
Operating Income	51	58	15	(1)	123	5	14	3	13	35	25	42	29	51	147
Interest expense, net	0	0	(1)	5	4	8	8	9	9	33	9	9	9	9	35
Other income, net	0	(1)	1	0	0	0	0	0	0	0	0	0	0	0	0
Pre-Tax Income	51	59	15	(6)	119	(3)	6	(6)	5	2	17	34	20	42	112
Income taxes	12	15	2	(2)	27	(3)	3	(1)	1	(0)	4	8	5	11	28
Net Income (Cont. Ops.)	39	44	13	(4)	92	0	3	(4)	3	2	12	25	15	32	84
EPS (Cont. Ops.)	\$0.34	\$0.38	\$0.11	(\$0.03)	\$0.80	\$0.00	\$0.03	(\$0.03)	\$0.03	\$0.02	\$0.10	\$0.21	\$0.12	\$0.26	\$0.70
Shares outstanding (Diluted)	115	115	115	116	115	119	119	120	120	120	120	120	121	121	121
Amortization of intangible assets	5	5	6	5	21	3	3	3	3	12	3	3	3	3	12
Transaction, restructuring & other	3	21	29	44	97	14	6	4	0	24	0	0	0	0	0
Income tax associated with adjustments	(2)	(6)	(9)	(12)	(29)	(4)	(2)	(2)	(1)	(9)	(1)	(1)	(1)	(1)	(3)
Adjusted net income	45	64	39	33	181	13	10	1	6	30	15	27	17	34	93
Adjusted EPS (Cont. Ops.)	\$0.39	\$0.56	\$0.34	\$0.28	\$1.56	\$0.11	\$0.08	\$0.01	\$0.05	\$0.25	\$0.12	\$0.23	\$0.14	\$0.28	\$0.77
Shares outstanding (Diluted adjusted)	115	115	116	118	116	119	119	120	120	120	120	120	121	121	121
EBITDA	\$72	\$80	\$37	\$20	\$209	\$23	\$32	\$21	\$31	\$107	\$43	\$60	\$47	\$69	\$219
Transaction & integration costs	3	18	23	40	84	6	4	3	0	13	0	0	0	0	0
Restructuring costs	0	3	6	4	13	8	1	1	0	10	0	0	0	0	0
Other	0	0	0	0	0	0	1	0	0	1	0	0	0	0	0
Adjusted EBITDA	\$75	\$101	\$66	\$64	\$306	\$37	\$38	\$25	\$31	\$131	\$43	\$60	\$47	\$69	\$219
Public company adjustments	(2)	(6)	0	0	(8)	---	---	---	---	---	---	---	---	---	---
Public company pro-forma	\$73	\$95	\$66	\$64	\$298	\$37	\$38	\$25	\$31	\$131	\$43	\$60	\$47	\$69	\$219
Margin Analysis															
Net revenue margin	22.2%	26.3%	24.7%	24.8%	24.4%	24.9%	24.9%	23.6%	24.4%	24.4%	23.9%	25.1%	24.3%	24.7%	24.5%
Adjusted EBITDA margin	5.6%	7.7%	5.8%	5.7%	6.2%	3.7%	3.9%	2.6%	3.1%	3.3%	4.1%	5.6%	4.3%	5.9%	5.0%
Operating margin	3.9%	4.7%	1.3%	(0.1%)	2.6%	0.5%	1.5%	0.3%	1.3%	0.9%	2.4%	3.9%	2.7%	4.3%	3.4%
Pre-tax margin	3.9%	4.8%	1.3%	(0.5%)	2.5%	(0.3%)	0.6%	(0.6%)	0.4%	0.1%	1.6%	3.1%	1.8%	3.6%	2.6%
Net margin	3.0%	3.6%	1.1%	(0.4%)	1.9%	0.0%	0.3%	(0.4%)	0.3%	0.1%	1.2%	2.3%	1.4%	2.7%	1.9%
Tax rate	23.5%	25.4%	13.3%	33.3%	22.7%	100.0%	50.0%	25.0%	25.0%	(12.5%)	25.0%	25.0%	25.0%	25.0%	25.0%
YR/YR Δ															
Revenue	23.2%	11.6%	(5.0%)	(15.6%)	2.3%	(23.0%)	(21.5%)	(14.3%)	(10.3%)	(17.6%)	2.8%	11.6%	11.1%	16.9%	10.6%
Net revenue profit	15.0%	34.7%	17.1%	0.7%	16.3%	(13.7%)	(25.5%)	(18.1%)	(11.9%)	(17.6%)	(1.2%)	12.5%	14.3%	18.4%	10.9%
Adjusted EBITDA	7.4%	61.0%	17.9%	(17.9%)	14.2%	(49.3%)	(60.0%)	(62.1%)	(51.6%)	(56.0%)	16.2%	57.9%	88.0%	122.6%	67.2%
Operating income	(1.9%)	23.4%	(60.5%)	(101.8%)	(35.9%)	(90.2%)	(75.9%)	(80.0%)	NM	(71.5%)	NM	NM	866.7%	292.3%	320.0%
Pre-tax income	2.0%	22.9%	(60.5%)	(110.9%)	(37.7%)	(105.9%)	(89.8%)	(136.7%)	NM	(98.3%)	NM	NM	(463.6%)	833.3%	5500.0%
Net income	(2.5%)	25.7%	(60.6%)	(109.5%)	(38.7%)	(100.0%)	(93.2%)	(131.7%)	NM	(97.6%)	NM	NM	(463.6%)	833.3%	3633.3%
EPS	(2.5%)	25.7%	(60.6%)	(109.5%)	(38.8%)	(100.0%)	(93.4%)	(130.5%)	NM	(97.6%)	NM	NM	(460.6%)	825.6%	3603.6%

Source: Company reports and Thompson Davis & Co. estimates

IMPORTANT DISCLOSURES***Rating Definitions***

Thompson Davis & Co., Inc. (TD & Co.) uses the performance of the S&P 500 and the Russell 2000 against stock price performance to define its rating system.

Buy: Company/Industry has strong fundamentals, attractive valuation; outperforms the relevant indices in over the next 12–18 months

Hold: Stock is fairly valued; no compelling reason to buy or sell stock today; cautious about prospects over the next 6–12 months for industry or company; neutral performance relative to the relevant indices.

Sell: Fundamentals of industry or company are deteriorating; company not expected to have consistent earnings growth over next 12–18 months or business model is questionable; underperforms the relevant indices in the next 12–18 months.

Price Targets

Price targets, when established, represent our best estimate of the market price of a stock in 12 months. A 12-month price target is highly subjective and the result of numerous assumptions, including company, industry, and market fundamentals, both on an absolute and relative basis, as well as investor sentiment, which can be highly volatile.

Fundamental Trend Definitions

Improving: growth rates of key business metrics are generally accelerating

Stable: growth rates of key business metrics are generally steady

Mixed: growth rates of some key business metrics are positive, but others are negative

Declining: growth rates of key business metrics are generally decelerating

Analyst Certification

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David Campbell and/or family own shares of the following companies: EXPD and FDX.

Additional information is available upon request. Any recipient of this report that wishes further information regarding any securities in this report or review the disclosures for all companies covered in this report, should contact Thompson Davis & Co., Inc., by phone at (866) 200-8002, visit our website or write 9030 Stony Point Pkwy Ste 100 Richmond, VA 23235.

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	#	%
BUY	23	96
SELL	0	0
HOLD	1	4
TOTAL	24	100.0%