

August 17, 2023

## XPO, INC. | XPO

**BUY**

*Patient Preparation Paying off for XPO's LTL 2.0; Price Target to \$80*

PRICE \$70.43

PRICE TARGET \$80.00

### KEY TAKEAWAY

XPO reported a 6% adjusted EBITDA beat for Q2'23 (\$244M versus \$230M), driven by higher revenue and better margins. Shipments in the quarter were up 2% yr/yr, with volumes in July up 9% yr/yr. We believe XPO may have increased shipments +10% yr/yr in the last two weeks of July given the end-of-month concerns around Yellow. Our sense is a combination of XPO's service level improvements, greater operating efficiency, and the Yellow bankruptcy has driven near-term volume and yield increases. XPO has outperformed its LTL peers in yet another quarter; as such, we are raising our 12-month price target from \$55 to \$80 to reflect current industry tailwinds and our view that XPO's LTL 2.0 plan is coming to fruition.

*Transportation and Logistics*

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### KEY POINTS

**A quarterly beat for Q2'23.** XPO reported Q2'23 adjusted EBITDA of \$244M (-16% yr/yr), which was above our forecast and consensus of \$230M. The beat was a combination of higher revenue and higher margins. Total revenue of \$1.92B (-6% yr/yr) was above our \$1.91B estimate. Total adjusted EBITDA margin was 12.7%, which was above our forecast by 70 bps.

**Building consistency in LTL.** North American LTL adjusted EBITDA came in above our forecast by \$11M (\$208M versus our \$197M). Shipments-per-day increased 2% yr/yr, which we believe is driven by XPO's service improvements. In our sense customers are migrating back to XPO as the freight market enters later innings in the down cycle. XPO appears to be gaining shipments from competition, while also growing yields which we think can build a valuable foundation for inflection.

Adjusted operating ratio was 87.5%, which was 100 bps better than our estimate. Although the operating ratio continues to be down yr/yr, we are enthusiastic that sequential improvement was manageable in the quarter. Management noted that typical seasonality of OR declines is 230 bps from Q2 to Q3, we currently forecast only a 100 bps decline (versus the outlook of 130 bps). Much of our decline is due to heightened depreciation and purchased transportation costs.

**Yellow timing ideal for LTL 2.0.** The Yellow bankruptcy has created a dynamic shift in the freight markets, particularly LTL. The timing of the exit of roughly 10% of LTL capacity should provide XPO with an opportunity to fill its own ~20% excess capacity in its LTL system. There is a sense that Yellow's exit could also provide further support for rising yields, given the lack of competing bids.

**Raising estimates on improving fundamentals.** We are raising our FY'23 adjusted EBITDA estimate from \$861M to \$904M, reflecting both the outperformance of Q2 as well as renewed optimism for Q3-Q4. Our FY'24 adjusted EBITDA estimate goes from \$1.01B to \$1.07B, driven by volume (+2% yr/yr), yield (+2% yr/yr), and operating margin (+260 bps improvement yr/yr) in North American LTL.

**Reiterate Buy, target to \$80.** We are reiterating our Buy rating on XPO and raising our 12-month price target from \$55 to \$80. Our new \$80 price target reflects an EV/EBITDA multiple of 11.0x on our 2024 EBITDA estimate of \$1.07B. Our view is that XPO should continue to outperform its peers given the favorable environment for continuous improvement within its LTL 2.0 plan.

### COMPANY STATISTICS

52-Week Range	\$24.75-\$76.77
Market Capitalization (M)	\$8,311
Average Daily Volume (000s)	2,149
Debt/Total Cap	69%
Dividend	NA
Shares Outstanding (M) fd	118
Estimated 3-yr EPS Growth	17%
Enterprise Value (M)	\$10,539
Float (M)	116

### FINANCIALS

FYE Dec	2021A	2022A	2023E	2024E
P/E Ratio	36.2x	20.0x	31.8x	22.8x
EV/EBITDA	13.0x	10.6x	11.7x	9.8X
Revenue (M)	\$7,202	\$7,718	\$7,565	\$7,819
Op Inc (M)	\$386	\$515	\$440	\$685
EBITDA (M)	\$812	\$997	\$904	\$1,073
EPS (A) Q1	\$0.23	\$0.46	\$0.56A	\$0.68
Q2	\$0.66	\$1.14	\$0.71A	\$1.00
Q3	\$0.41	\$0.95	\$0.51	\$0.98
Q4	\$0.64	\$0.98	\$0.44	\$0.44
<b>Total</b>	\$1.94	\$3.52	\$2.22	\$3.09
<b>Consensus</b>	—	—	<b>\$2.43</b>	<b>\$3.36</b>

*Consensus estimates from FactSet*

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**Valuation.** XPO is currently trading at 11.7x our 2023 EV/EBITDA estimate. Our 12-month price target of \$80 is based on 11.0x our 2024 EV/EBITDA estimate and therefore assumes multiple compression. Average multiples among XPO's public peers are currently 11.0x 2023 EV/EBITDA. We believe continued execution of XPO's LTL strategy should lead to multiple expansion to peer levels. Over the past five years, XPO has traded at an average of 10.2x EV/EBITDA.

**Risks.** Risks to the stock as well as to the achievement of our price target include macroeconomic conditions, project execution risks, inability to acquire necessary materials, and input cost inflation. Additionally, XPO has laid out strategic initiatives to return LTL profitability to more normalized levels, but failure to continue to achieve said levels could create further risk to the achievement of our price target.

**XPO, Inc.**  
Earnings Model

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(\$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
Revenue	\$1,894	\$2,047	\$1,946	\$1,831	\$7,718	\$1,907	\$1,917	\$1,898	\$1,843	\$7,565	\$1,936	\$2,031	\$1,971	\$1,881	\$7,819
Salaries, wages and employee benefits	725	752	739	729	2,945	762	783	780	760	3,085	765	795	790	785	3,135
Purchased transportation	510	525	480	449	1,964	457	444	450	430	1,781	460	470	445	435	1,810
Fuel, operating expenses and supplies	418	434	425	410	1,687	427	390	378	393	1,588	403	408	393	403	1,607
Other operating expenses	71	60	55	59	245	56	59	62	56	233	60	60	55	55	230
D&A	94	96	99	103	392	101	107	114	103	425	108	108	101	101	418
Transaction and integration costs	7	7	2	42	58	22	17	10	5	54	0	0	0	0	0
Restructuring costs	6	2	7	35	50	24	10	5	2	41	2	0	0	0	2
<b>Operating Income</b>	<b>63</b>	<b>171</b>	<b>139</b>	<b>4</b>	<b>377</b>	<b>58</b>	<b>107</b>	<b>99</b>	<b>94</b>	<b>358</b>	<b>138</b>	<b>190</b>	<b>187</b>	<b>102</b>	<b>617</b>
Adjustments to operations	20	18	19	81	138	27	19	19	17	82	18	17	17	16	68
<b>Adjusted Operating Income</b>	<b>83</b>	<b>189</b>	<b>158</b>	<b>85</b>	<b>515</b>	<b>85</b>	<b>126</b>	<b>118</b>	<b>111</b>	<b>440</b>	<b>156</b>	<b>207</b>	<b>204</b>	<b>118</b>	<b>685</b>
Interest expense, net	37	31	35	32	135	42	43	45	45	175	45	45	45	45	180
Foreign currency (gain) loss	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
Other income, net	(14)	13	(15)	0	(16)	(5)	20	0	0	15	0	0	0	0	0
<b>Pre-Tax Income</b>	<b>40</b>	<b>127</b>	<b>119</b>	<b>(28)</b>	<b>258</b>	<b>21</b>	<b>44</b>	<b>54</b>	<b>49</b>	<b>168</b>	<b>93</b>	<b>145</b>	<b>142</b>	<b>57</b>	<b>437</b>
Income taxes	8	31	27	8	74	4	13	14	13	44	23	36	36	14	109
<b>Net Income (Cont. Ops.)</b>	<b>32</b>	<b>96</b>	<b>92</b>	<b>(36)</b>	<b>184</b>	<b>17</b>	<b>31</b>	<b>39</b>	<b>37</b>	<b>124</b>	<b>69</b>	<b>109</b>	<b>107</b>	<b>42</b>	<b>327</b>
Noncontrolling interests	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
<b>EPS (Cont. Ops.)</b>	<b>\$0.28</b>	<b>\$0.83</b>	<b>\$0.79</b>	<b>(\$0.31)</b>	<b>\$1.59</b>	<b>\$0.15</b>	<b>\$0.26</b>	<b>\$0.33</b>	<b>\$0.31</b>	<b>\$1.05</b>	<b>\$0.58</b>	<b>\$0.91</b>	<b>\$0.90</b>	<b>\$0.35</b>	<b>\$2.75</b>
Shares outstanding (Diluted)	116	116	116	115	116	116	118	118	119	118	119	119	119	120	119
Adjustments for adjusted EPS	27	48	22	168	265	59	64	29	21	173	15	13	13	13	54
Tax impact from adjustments above	(6)	(12)	(4)	(19)	(41)	(11)	(12)	(8)	(5)	(36)	(4)	(3)	(3)	(3)	(14)
<b>Adjusted EPS (Cont. Ops.)</b>	<b>\$0.46</b>	<b>\$1.14</b>	<b>\$0.95</b>	<b>\$0.98</b>	<b>\$3.52</b>	<b>\$0.56</b>	<b>\$0.71</b>	<b>\$0.51</b>	<b>\$0.44</b>	<b>\$2.22</b>	<b>\$0.68</b>	<b>\$1.00</b>	<b>\$0.98</b>	<b>\$0.44</b>	<b>\$3.09</b>
Shares outstanding (Diluted)	116	116	116	115	116	116	118	118	119	118	119	119	119	120	119
<b>EBITDA</b>	<b>\$171</b>	<b>\$254</b>	<b>\$253</b>	<b>\$107</b>	<b>\$785</b>	<b>\$164</b>	<b>\$194</b>	<b>\$213</b>	<b>\$197</b>	<b>\$768</b>	<b>\$246</b>	<b>\$298</b>	<b>\$288</b>	<b>\$203</b>	<b>\$1,035</b>
Adjustments	13	35	9	155	212	46	50	25	15	136	12	9	9	8	38
<b>Adjusted EBITDA</b>	<b>\$184</b>	<b>\$289</b>	<b>\$262</b>	<b>\$262</b>	<b>\$997</b>	<b>\$210</b>	<b>\$244</b>	<b>\$238</b>	<b>\$212</b>	<b>\$904</b>	<b>\$258</b>	<b>\$307</b>	<b>\$297</b>	<b>\$211</b>	<b>\$1,073</b>
<b>Margin Analysis</b>															
Adjusted EBITDA margin	9.7%	14.1%	13.5%	14.3%	12.9%	11.0%	12.7%	12.5%	11.5%	11.9%	13.3%	15.1%	15.1%	11.2%	13.7%
Adjusted operating margin	4.4%	9.2%	8.1%	4.6%	6.7%	4.5%	6.6%	6.2%	6.0%	5.8%	8.0%	10.2%	10.4%	6.2%	8.8%
Adjusted operating ratio	95.6%	90.8%	91.9%	95.4%	93.3%	95.5%	93.4%	93.8%	94.0%	94.2%	92.0%	89.8%	89.6%	93.8%	91.2%
Operating margin	3.3%	8.4%	7.1%	0.2%	4.9%	3.0%	5.6%	5.2%	5.1%	4.7%	7.1%	9.4%	9.5%	5.4%	7.9%
Pre-tax margin	2.1%	6.2%	6.1%	(1.5%)	3.3%	1.1%	2.3%	2.8%	2.7%	2.2%	4.8%	7.1%	7.2%	3.0%	5.6%
Net margin	1.7%	4.7%	4.7%	(2.0%)	2.4%	0.9%	1.6%	2.1%	2.0%	1.6%	3.6%	5.4%	5.4%	2.3%	4.2%
Tax rate	20.0%	24.4%	22.7%	(28.6%)	28.7%	19.0%	29.5%	<b>27.0%</b>	<b>26.0%</b>	26.4%	<b>25.0%</b>	<b>25.0%</b>	<b>25.0%</b>	<b>25.0%</b>	25.0%
<b>YR/YR Δ</b>															
Revenue	9.7%	9.3%	6.3%	3.3%	7.2%	0.7%	(6.4%)	(2.5%)	0.7%	(2.0%)	1.5%	6.0%	3.9%	2.0%	3.4%
Adjusted EBITDA	3.4%	21.9%	26.6%	37.9%	22.8%	14.1%	(15.6%)	(9.4%)	(18.9%)	(9.3%)	22.7%	25.9%	25.2%	(0.9%)	18.6%
Adjusted operating income	13.7%	42.1%	68.1%	(1.2%)	33.4%	2.4%	(33.3%)	(25.6%)	31.2%	(14.6%)	83.1%	64.4%	73.9%	5.4%	55.6%
Operating income	3.3%	42.5%	113.8%	(93.9%)	20.8%	(7.9%)	(37.4%)	(29.1%)	2262.3%	(5.0%)	137.2%	77.7%	90.2%	7.4%	72.2%
Pre-tax income	700.0%	78.9%	(893.3%)	(160.9%)	141.1%	(47.5%)	(65.4%)	(55.0%)	(276.8%)	(34.9%)	341.0%	229.8%	166.0%	14.2%	159.9%
Net income	540.0%	68.4%	(807.7%)	(176.6%)	91.7%	(46.9%)	(67.7%)	(57.5%)	(201.7%)	(32.8%)	308.5%	251.1%	173.3%	15.7%	164.7%
Adjusted EPS	96.8%	71.4%	134.0%	54.0%	81.4%	22.6%	(37.6%)	(46.3%)	(55.2%)	(36.9%)	21.3%	40.4%	91.8%	(0.9%)	39.0%

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***

I, David Campbell, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject company(ies) and its (their) securities. I also certify that I have not been, am not, and will not be receiving direct or indirect compensation in exchange for expressing the specific recommendation(s) in this report.

**OTHER DISCLOSURES**

The following companies pay TD & Co. for a subscription to our transportation and logistics research services, from which our research analyst is partially compensated: XPO (XPO)

TD & Co. expects to receive or intends to seek compensation for investment banking services from all the companies that are a subject of this report in the next three months.

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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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**DISTRIBUTION OF RATINGS**

Thompson Davis & Co., Inc., rating distribution by percentage (as of August 17, 2023):

	#	%
<b>BUY</b>	23	96
<b>SELL</b>	0	0
<b>HOLD</b>	1	4
<b>TOTAL</b>	24	100.0%

**Rating and Price Target History for XPO, Inc. (XPO) as of June 30, 2023**

Date	Rating	Price	Target
2/17/2021	Buy	\$69.23	\$92*
8/11/2021	Buy	\$88.30	\$110
5/12/2022	Buy	\$51.56	\$100**
11/3/2022	Buy	\$31.90	\$65
2/22/2023	Buy	\$31.90	\$50
6/20/2023	Buy	\$51.43	\$55



\* reflects price target prior to 8/2/2021 spinoff of GXO  
 \*\* reflects price target prior to 11/1/2022 spinoff of RXO