# Covenant Logistics Group 1st Quarter 2022 Conference Call

**Mr. Hogan** – Welcome to the Covenant Logistics Group first quarter 2022 conference call.

As a reminder:

> *This conference call will contain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated by the forward-looking statements. Please review our disclosures in filings with the Securities Exchange Commission, including, without limitation, the Risk factors section in our most recent Form 10-K and our current year Form 10-Qs. We undertake no obligation to publicly update or revise any forward-looking statements to reflect subsequent events or circumstances.*

A copy of the prepared comments and additional financial information is available on our website at www.covenantlogistics.com\investors. I'm joined by Tripp Grant, our Chief Accounting Officer, and Paul Bunn and David Parker are available via phone.

We are very proud and pleased with our first quarter results, which represent yet another quarterly earnings record for any quarter in company history. In addition, it's the first time in our history where first quarter earnings were greater sequentially than the fourth quarter. This exciting achievement could not have been accomplished without the contribution from each of our business units. All business units improved it's OR versus the fourth quarter. The small acquisition we made in February combined with the repurchase of 655 thousand shares at an average price of $22.60 per share under our share repurchase program, produced earnings accretion to the quarter and is expected to continue. With this strong start to the year, and the hard work of our team transforming our business to a less cyclical model, we are confident that we will exceed 2021's full year adjusted earnings per share for the full year of 2022 absent something truly unexpected.

**In summary, the key highlights of the quarter were**:

- Freight revenue grew 28% to $258 million compared to the 2021 quarter,
- Adjusted earnings per share increased 141% to $1.35 per share from the year ago quarter,
- Our asset-based truckload's freight revenue grew 15% versus the first quarter of 2021 with 218 fewer trucks,
- Our less asset intensive ("asset light") managed freight and warehouse segments combined grew 55% compared to the first quarter of 2021,
- On the safety side, our chargeable DOT rate was the lowest on record and 31% lower than year ago,
- Our TEL leasing company investment produced a record quarter, contributing $0.30 per diluted share, or an additional $0.17 per share versus the year ago period,
- Due to the strong cash flow in the quarter, our net indebtedness increased only $22.1 million after utilizing a combined $52 million of cash and borrowings under our ABL credit facility on the small acquisition and share repurchases,
- We finished the quarter with a leverage ratio of slightly less than .4x, debt to equity ratio of 12%, and return on invested capital of 14%.

**Now Paul will provide a little more color on the items affecting the business units:**

- For the quarter, our Asset light business's (comprised of managed freight and warehouse) were once again our largest group for the quarter both in freight revenue and adjusted operating profit. This group comprised 40% of total freight revenue and 50% of consolidated adjusted operating profit. The sheer volume of overflow and special project freight dropped throughout the quarter, but overall revenue margin expanded covering much of the volume decline. Our warehouse team is doing a great job building a nice pipeline with several startups planned for the remainder of the year. This group remains a top priority for growth, focusing on talent acquisition and technology enhancements. We are very excited about the prospects with this group.

- The Expedited division was 31% of consolidated freight revenue and 38% of adjusted operating profit in the quarter. It grew its revenue 16% versus the year ago quarter due to strong rate improvements and contribution from the small acquisition. The acquisition contributed to the sequential weighted average growth of 36 trucks in the quarter. Expedited produced a record first quarter with an 88 adjusted OR, 260 basis points better than the fourth quarter, a first for our company. Even in a slowing environment, new business startups continue, and our team count is growing in the second quarter. After multiple increases in 2021, we feel our driver pay is in good shape at the present time but continue to watch closely.

- The Dedicated division was 29% of consolidated freight revenue and 12% of adjusted operating profit in the quarter. This division continued its steady sequential improvements with adjusted OR improving 180 basis points from the fourth quarter and 580 points from the year ago quarter. Revenue per truck continues its sequential improvement (+8% from the fourth quarter) which has been a big key to sustainable gains. Also, the "weed and feed" plan for accounts continue, with 7 startups completed in the first quarter (61 trucks) and 5 to 6 planned for the second quarter (82 trucks). The pipeline for the remainder of year remains robust, supporting our expectation that margin improvement will continue.

- We plan to begin briefly discussing each quarter the performance of our 49% interest in Transport Enterprise Leasing or "TEL". TEL is an investment that we've had since 2011. During that time, TEL has grown to over 2,000 tractors and 6,500 trailers in its portfolio. Meanwhile, our investment in TEL, included in Other Assets in our consolidated balance sheet, has grown from our cash investment of $4.9 million to $51.0 million including the cumulative earnings we have recognized. TEL focuses on a) managing lease purchase programs for clients, b) leasing trucks and trailers to small fleets or shippers and c) aiding clients in the procurement and disposition of their equipment through a robust equipment buy and sell program. TEL contributed a total of $.30 per share to our overall results or an additional $.17 versus the year ago quarter. TEL's revenue in the quarter grew 41% and pre-tax operating profit margin increased to 43%. Due to the business model, gains and losses on sale of equipment is a normal part of the business and can cause earnings to fluctuate from quarter to quarter. We are very happy with the TEL leadership team, it's future and contribution to Covenant's future. TEL is an untapped value for our shareholders.

**Regarding our outlook for the future:**
As we said in the release, we expect to have a good second quarter and deliver record full year adjusted earnings per share in 2022. This expectation takes into consideration our expectation of a more balanced freight environment in the second half of the year. On this point, we think it is important to differentiate between the spot market, which has more volatile rates and volumes and receives a lot of analyst and investor attention, and the contract market, where most of our freight comes from, and which our customers tell us will retain consistent demand for the remainder of the year. Thus, while some of the "froth" may come out of our rates and volumes, we expect the core to remain solid at least for the next couple of quarters, absent a shock to the system. Even in a moderating freight environment and with increased capital expenditures for the remainder of the year, we expect to generate positive cash flow, giving us resolve to stay focused on good, long term strategic investments. Looking farther ahead, we also believe that 2023 will be a breakout year for Covenant, proving that our model is

more durable than in the past. We stand firm that the changes we've made to our business model over the past two years will provide more consistent earnings and cash flows compared with our results in past cycle troughs. We believe time and performance will provide clarity. In the meantime, we will continue to produce cash to maximize opportunities for our shareholders.

**Thank you for your time and we will now open the call for any questions.**