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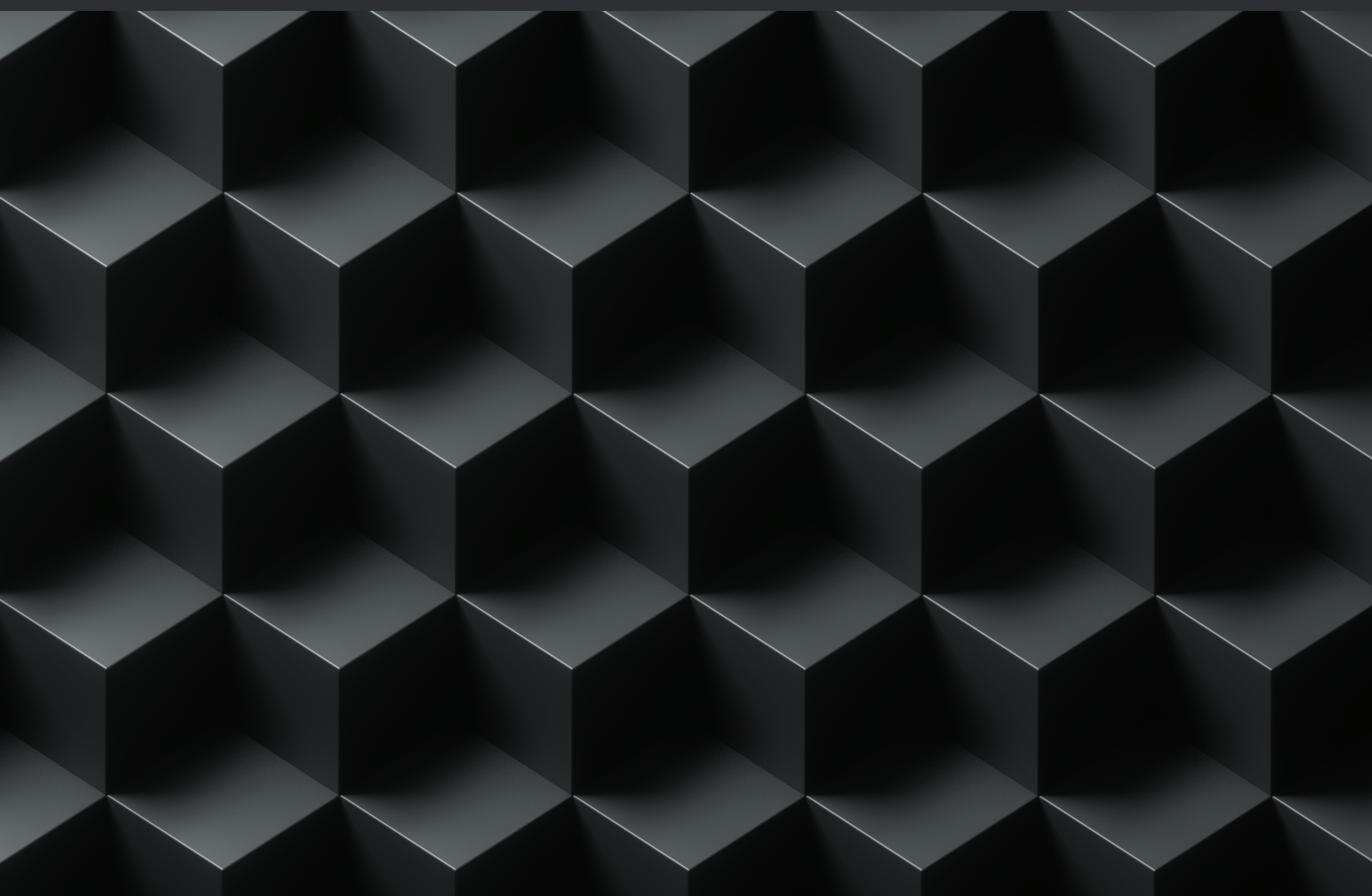
First quarter 2024 results



GXO Logistics Q1 2024 Earnings Call

Presenters

Malcolm Wilson – Chief Executive Officer
Baris Oran – Chief Financial Officer
Richard Cawston– Chief Revenue Officer

Q&A Participants

Stephanie Moore – Jefferies
Scott Schneeberger – Oppenheimer
Jason Seidl – TD Cowen
David Zazula – Barclays
Ben Moore – Deutsche Bank
Bascome Majors – Susquehanna
Brian Ossenbeck – JP Morgan
Kevin Gainey – Thompson Davis & Company

Operator

Welcome to the GXO first quarter 2024 Earnings Conference Call and Webcast.
My name is Camilla and I'll be your operator for today's call.

At this time, all participants are in a listen-only mode. Later, we will conduct a question-and-answer session. If anyone should require operator assistance during the conference, please press star-zero on your telephone keypad.

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, the use of non-GAAP financial measures, and the Company's guidance:

- During this call, the Company will be making certain forward-looking statements within the meaning of applicable securities law, 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. 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.

- The Company also may refer to certain non-GAAP financial measures as defined under applicable SEC rules during this call. 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 are on its website.

- Unless otherwise stated, all results reported on this call are reported in United States dollars.

- The Company will also remind you that its guidance incorporates business trends to date and what it believes today to be appropriate assumptions. The Company's results are inherently unpredictable and may be materially affected by many factors, including fluctuations in foreign exchange rates, changes in global economic conditions and consumer demand and spending, labor market and global supply chain constraints, inflationary pressures, and the various factors detailed in its filings with the SEC.

- It is not possible for the Company to actually predict demand for its services, and, therefore, actual results could differ materially from guidance. 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 on the Company's website.

I will now turn the call over to GXO's Chief Executive Officer, Malcolm Wilson.
Mr. Wilson, you may begin.

Malcolm Wilson – GXO Chief Executive Officer

Thanks, Camilla, and good morning, everyone. I appreciate you joining us today for our first quarter 2024 earnings call. With me in Greenwich are Baris Oran, our Chief Financial Officer; Richard Cawston, our Chief Revenue Officer; and Kristine Kubacki, our new Chief Strategy Officer.

As you will have seen two weeks ago, we issued preliminary results for the first quarter of 2024 in conjunction with our bond offering to finance the acquisition of Wincanton. These results reflect the resiliency of our business model and the acceleration of our growth.

Today, we'll walk you through our first quarter, and discuss our outlook for the remainder of this year, as well as for our longer-term 2027 targets.

GXO had a strong start to 2024.

We generated revenue of $2.5 billion, up 6% year over year, and adjusted EBITDA of $154 million. We delivered positive organic revenue growth for the quarter and continued to gain market share. When we last spoke, we said that the fourth quarter was the bottom for organic growth, and that's reflected in the sequential improvement in the first quarter, as well as the sales and pipeline activity we're seeing.

We signed approximately $250 million of new business, up 55% year over year, including new contracts with Boeing, Guess, Michelin, Puma, and WH Smith. More than half of these new contract wins came from customers outsourcing to us or partnering with us for the first time.

Earlier this week, we announced a landmark new 20-year partnership with Levi's in Germany, where we've been building our presence following our acquisition of Clipper. This will be a highly automated, newly outsourced operation, with a lifetime value of nearly $1 billion. This is just one example of the trend we're seeing, where customers are looking for longer-term partnerships to address their fulfillment needs.

To that end, our sales pipeline is growing, and ended the quarter at $2.2 billion – a 12-month high. We've more than replenished the pipeline after converting a quarter-billion-dollars of new wins. We're continuing to see larger deal sizes and longer contract lengths. Additionally, the turnover of the pipeline is accelerating, creating more new business opportunities.

Another highlight of the quarter was the announcement of the acquisition of Wincanton, which we closed last week. Wincanton exemplifies our M&A strategy:

It expands GXO's presence in strategic growth verticals in the UK, including aerospace and industrials, providing GXO with a springboard to offer these services across Europe, and it will be accretive to earnings per share in 2024, excluding synergies on a pro-forma basis, and double-digit accretive including full run-rate cost synergies.

Wincanton builds upon our proven track record of leveraging newly acquired platforms to drive growth through revenue synergies. For example, since the Clipper acquisition, we've executed on our strategy to establish a meaningful operating presence in Germany, the largest economy in Europe. As of the end of the first quarter, Germany is the fourth-largest pipeline in all of GXO, and one of the fastest growing. We're converting it with high-quality deals like Levi's.

Similarly, when we acquired PFS in the fourth quarter of 2023, we set out to leverage the combination of GXO's global footprint with PFS's leadership position in health & beauty, jewelry and luxury. Since the acquisition, we've integrated the two businesses and expanded legacy PFS customers, like Glossier and Refi Beauty, across multiple geographies.

This is proof positive of our execution on our M&A strategy, and especially of our ability to capitalize upon the strengths of the companies we acquire.

We're speaking to major global customers every day, and as Richard will discuss in a moment, a consistent thread in our discussions is the expectation of a gradual recovery of consumer goods demand. Businesses are building for the future, planning their fulfillment strategies to meet their expected needs – and we're positioning ourselves to take market share by providing best-in-class solutions.

One way we're doing this is through our intensified commitment to leading the market in automated and AI-driven fulfillment. Automation is a key tenet of our value proposition, and we're a first-mover in trialing the integration of cutting-edge automation like humanoids and AI inside the four walls of the warehouse.

We've recently introduced some exciting innovations in AI:

First, the warehouse optimization pilot we mentioned last quarter was a success, driving a productivity increase of approximately 15%, and we're rolling out the app across our sites as we speak.

Second, we've recently piloted a proprietary workforce management tool which we've developed in house. Our tool makes more than 15 million decisions per minute to streamline inventory replenishment, adding about 7% of capacity at no additional cost. We'll be deploying this solution broadly across our operations starting this year.

All this to say, I'm delighted with the way our business is performing, and we anticipate continued acceleration in organic revenue growth throughout 2024 and beyond.

With our growing pipeline and accelerating pace of new business wins, our focus on automation and sales excellence, and the pace of outsourcing in this $450 billion total addressable market, GXO is set to take significant market share over the long term.

Now I'll hand you over to Richard, to update you on what we're hearing from our customers.

Richard, over to you.

Richard Cawston – GXO Chief Revenue Officer

Thanks, Malcolm. Good morning, everyone.

I've had the pleasure of meeting some of you over the past few years, as the leader of GXO's European business. In my new role as Chief Revenue Officer, my mission is to convert the significant market opportunity Malcolm just mentioned into outsized growth for GXO.

And we're off to a great start of doing just that.

As Malcolm highlighted, our new sales wins signed in the first quarter totaled $250 million, which was an increase of 55% year on year. And we're on track to outperform our $1 billion of new wins from 2023.

We serve the bluest of the blue-chips, and what we're hearing from our customers, both current and prospective, is the need to build efficiencies into their operations to support their future growth. As a result, we're seeing demand strengthening.

I'd like to underline a few other sales highlights from the quarter which underpin our confidence in our growth trajectory.

First, our pipeline stands at $2.2 billion, up quarter on quarter. We added more than a billion dollars of new opportunities in the first quarter alone.

Second, our customers are making faster decisions to outsource their supply chains, reflecting returning confidence in their long-term outlook. As a consequence, sales cycles are shortening, and our pipeline is delivering results faster, with deals getting larger and contracts getting longer.

Third, significantly, more than half of our wins in the first quarter were with customers outsourcing or turning to GXO to support them for the very first time.

And finally, in addition to new logos, we're also expanding our relationships with existing customers. We serve more than a quarter of the Fortune 100 companies, and the success of our land-and-expand strategy is evident in that half of our revenues come from our customers we partner with in more than one country.

We're seeing these trends develop across our regions.

For example, this coming Friday, we'll be cutting the ribbon on a new warehouse that is the largest building in the state of Maryland. We're supporting personal care and appliance manufacturer Conair in this 2.1 million square foot facility. This solution consolidates three sites into a single automated operation that handles all of Conair's brands across retail and direct to consumer, enabling their growth and combining fulfillment with high-value-added services like product testing.

We've also recently expanded our 13-year partnership with global apparel company Guess, originally in Europe, across the ocean to the US, turning it into a global partnership. Guess had previously run their North American operations in-house, and they've entrusted us to help them unlock value in their supply chain by outsourcing. We now operate three sites for Guess: in Italy, the Netherlands and now the US.

These are examples of our consultative approach, where we engage with our customers at the highest levels of leadership to design a solution that fits their needs.

In Europe, as Malcolm mentioned, we just announced our landmark Levi's win. We're delighted to take on a newly outsourced, highly automated operation for an iconic global brand.

I was in Germany last week to visit the site, which is Levi's' "super-hub," allowing Levi's to supercharge their omnichannel growth strategy. It was extremely exciting to kick off this partnership – the ambition and the momentum on both sides are palpable. This is Germany's greenest warehouse, with phenomenal sustainability features that raise the bar in the logistics industry.

This new win is especially significant because it exemplifies why a brand such as Levi's partners with GXO to transform their operations and drive a competitive advantage through their supply chain.

As Malcolm mentioned, in the past few months, we've scaled up our sales and account management teams, while intensifying our focus on high-growth verticals and geographies to really capitalize on the opportunity.

We've had an excellent first quarter, and our investments in our teams, strategy and processes are already translating to pipeline growth and new partnerships with blue-chips across the globe.

This is why I'm confident that we'll deliver strong growth in new sales wins in 2024 and beyond, taking share of our enormous addressable market.

And with that, I'll pass the mic to Baris to take you through our detailed financials, our 2024 guidance, and our 2027 targets.

Baris, over to you.

Baris Oran – GXO Chief Finance Officer

Good morning, everyone.

We started the year on strong footing, and we are pleased to see a continuation of the positive trends we noted last quarter and a return to organic revenue growth. We believe that the fourth quarter was the bottom.

For the first quarter of 2024, we generated revenue of $2.5 billion, growing 6% year over year, of which 1% was organic. Our organic growth was led by our largest verticals: omnichannel retail and technology, particularly in the semiconductor space.

Our first quarter adjusted EBITDA was $154 million. We recorded a net loss of $36 million, which was primarily driven by a one-off legacy litigation expense, as well as one-time transaction costs for Wincanton, which are in line with the costs associated with our earlier acquisitions.

As we noted on our call last quarter, our growth, margins, adjusted diluted earnings per share, and adjusted EBITDA this quarter reflect the optimization of our customer footprint, our productivity initiatives and our investments in our capabilities. Our laser focus on these capabilities is paying off, and you'll see the results in our new business wins going forward.

Our operating return on invested capital this quarter was above our target at 33%, demonstrating our ability to continue to invest back into our business with high returns. We expect to maintain this level of return going forward.

In 2023, we surpassed all expectations on free cash flow, and we continued to generate excellent free cash flow this quarter, which improved by $26 million year over year. This underpins our confidence in our full-year free cash flow conversion target.

Our balance sheet remains rock solid, and we are committed to our investment-grade rating. We are expecting leverage levels of about 2.5x by the end of this year, and about 1.9x by the end of next year. We have no debt coming due in 2024.

As you know, one of our most important achievements this quarter was the acquisition of Wincanton, which we completed last week.

We acquired Wincanton at a very attractive valuation, taking into account the cost synergies we expect to deliver. We expect the deal will be accretive to earnings in 2024, with double-digit accretion to adjusted diluted EPS once we fully integrate – and this level of synergy realization is borne out in our previous acquisitions of Clipper and Kuehne & Nagel's UK operations.

The business also gives us exciting exposure to the industrial and aerospace sectors in Europe, with well-positioned customers like BAE Systems, EDF and Alstom.

Wincanton carries a high proportion of resilient cost-plus contracts, which – even before the £45 million of cost synergies we expect Wincanton to contribute – will deliver very stable, slightly lower, margins, as well as higher returns and predictable cash flow generation.

Now, returning to our guidance.

For the full year of 2024, inclusive of Wincanton, we now expect double-digit adjusted EBITDA growth at the midpoint of our guidance range, which is $805 million to $835 million. We have reiterated our previous organic revenue growth guidance of 2-5%. Our first quarter organic growth shows an upward trend, and we anticipate continued acceleration throughout the balance of the year. April has shown an acceleration in organic growth versus the first quarter. We expect to convert 30-40% of our adjusted EBITDA into free cash flow, above our 30% long-term target.

We have also updated our 2027 targets. These revised targets reflect our performance for 2023, and our guidance for 2024. Additionally, following the close of our acquisition of Wincanton, the expected impact of this transaction is embedded in our new plan.

Our revised 2027 targets, which include $15.5 to $16 billion of revenue, and $1.25 to $1.3 billion of adjusted EBITDA, reflect the following over the next three years:

First: Double-digit organic revenue growth on average over the period from 2024 to 2027, as we grow our wins and market share, reflecting a gradual recovery in our customers' volumes through 2024 and 2025.

And, second: Margin expansion, through our focus on business development, technology and automation, with a significant focus on AI – as well as the cost synergies we expect to deliver from Wincanton.

We have a clear path to achieve compounding double-digit top-line growth, with 15% adjusted EBITDA CAGR, and even faster growth in adjusted diluted earnings per share.

GXO's growth is accelerating, and we are delivering operating return on invested capital and free cash flow conversion ahead of our long-term targets. We have just completed a great acquisition at an attractive valuation, and we will continue to allocate capital in the best interests of our shareholders.

And with that, I'll hand it back over to Malcolm.

Malcolm Wilson – GXO Chief Executive Officer

Thanks, Baris.

We've had a strong start to 2024.

We're seeing growing demand from global blue-chip customers as they focus on building the future of their supply chains. We're positioning GXO to take market share as customers build efficiencies into their operations to support their future growth. And, we're making big moves in automation and AI.

Our laser focus on profitable growth gives me great confidence in achieving our long-term targets and creating outsized shareholder value.

With that, we'll hand the mic back to Camilla and transition to Q&A.

Question & Answer Session

Operator

Thank you. We will now be conducting a question-and-answer session. If you would like to ask a question, please press star-one on your telephone keypad. A confirmation tone will indicate your line is in the question queue. You may press star-two if you would like to remove your question from the queue. And for participants using speaker equipment, it may be necessary to pick up your handset before pressing the star keys. One moment please while we poll for questions.

Our first questions come from the line of Stephanie Moore with Jefferies.
Please proceed with your questions.

Stephanie Moore – Jefferies

Hi, good morning. Thank you.

I wanted to start with just the organic growth performance. If you could touch on the 1Q performance and maybe really focusing on that, maybe the same-store sales or volume component. But importantly, how that bridges to the full year expectations for 2024 and just what you're hearing in the underlying operating environment to give you confidence in those – in that target? Thank you.

Malcolm Wilson – GXO Chief Executive Officer

Hi Stephanie, good morning. It's Malcolm here.

Stephanie, while we're not seeing any material change in customer volumes, particularly on the consumer goods side, what we have seen is a more positive trend as we've gone through quarter one. When we compare quarter one to quarter four, we can see sequential improvements. And as Baris just mentioned, in early part of quarter two, April, already, we can see that trend has continued to go forward.

When we see the three regions that we're working in, Continental Europe, well, that's continued to be very resilient. I can't say it's growing, but it's equally not deteriorating. It's very resilient compared to what we've seen in the past.

Our U.S. business, that's been mixed but it reflects a wide range of different industries that we're servicing. Consumer volumes are now stable.

U.K., in fact, that's been our strongest growth market during quarter one. And it's interesting that, in fact, it was the first to show signs of slowdown in '23, and it seems to be the first to show really strong signs of improving.

So, all in all, that's the picture that we see.

If I look across every territory or what we can see, consumer demand for goods is very different than consumer demand for services. For goods, it continues to be sluggish. Companies are starting to restock. We can see that from the dialogue that we have with our customers. I think we've seen the bottom of the destocking environment. And what we're clearly evidencing is customers in order to meet their plans, they're going to need to start restocking through the course of the year – so that's a good sign for us. But I do want to level set. Overall, it's a sluggish environment in '24, just as you see from many of the parcel carriers and the real estate companies, the destocking activity, that's impacted – particularly in the small proportion of our business where we have multi-customer sites. So, we have capacity.

But overall, from a Q1 highlights perspective, the sales pipeline is up, business wins are up. Customer decision-making is speeding up. That's probably the most important aspect. $2.5 billion top line, 6% growth. $154 million, in line with consensus. Our Wincanton deal, as Baris mentioned, that's a deal done at a very attractive price. Increases in automation and AI. So overall, we're off to a really good start.

Baris, maybe you can comment on the actual evolution of growth as we expect this year.

Baris Oran – GXO Chief Financial Officer

Sure. Let me first start with Q1.

The bridge to our 1% organic growth in the first quarter is roughly: new business contributing around 6.5%; volumes, including customer consolidation of footprint, sequentially improved from Q4, but still negative year-over-year, around minus 3%; pricing, mainly inflation, is about 2%, and the remainder is coming from the retention, in line with our long-term averages.

As Malcolm mentioned, April has already shown an improvement versus the prior quarter.

If I look at the entire year of 2024, the bridge for our organic growth is – which was about 2.5%: new business expected to contribute around 9% as we continue to see a lot of takeover-in-place and outsourcing projects, such as Levi's. Number two, volumes plus consolidation of footprint, expected to be around minus 3%. Pricing, primarily inflation, around 2% and the remainder coming from the impact of retention, which we expect to be in line with our long-term averages. That's our bridge for the entire year.

Stephanie Moore – Jefferies

Got it. That's very clear. I will leave it at that. Thank you so much.

Baris Oran – GXO Chief Financial Officer

Thank you.

Operator

Our next question comes from the line of Scott Schneeberger with Oppenheimer. Please proceed with your question.

Scott Schneeberger – Oppenheimer

Thank you very much. Good morning, everyone.

I want to focus on this new win of Levi's – pretty exciting for you. When will that start to contribute? Just an idea of when that's, how that's going to ramp?

And then also, you just kind of shared the contribution you're anticipating from new business wins. But there's been some discussion of this speeding up, Malcolm, you mentioned of decision-making. So, if you could just kind of work in what you're seeing there, much appreciated.

And then lastly, as part of this long-term contract, 20 years, is this a new trend we're seeing on Levi's, and I think we've seen that with other deals recently?

Richard Cawston – GXO Chief Revenue Officer

Good morning Scott, it's Richard Cawston. Delighted to meet you this morning. It was my first earnings call, so I'm looking forward to a great conversation.

Thanks for the question. We're super proud about this win with Levi's. It underpins our progression into Germany that we set out to do last year following the acquisition of Clipper, that give us a strong foundation. It's Europe's largest economy, and we absolutely should be there with our automation, our know-how and our agility and our laser focus in the warehouse. And I think if you recall, last year, we opened up a speculative warehouse, which we don't normally do in Germany because the opportunity is so big. And I'm pleased to announce that that warehouse is full now, including aerospace wins that have come into us in this region.

Pivoting to Levi's, so it's a great iconic brand. We entered into a consultative process and a deep partnership. That's what reflects the 20 years. This is a high investment; Germany's greenest warehouse – so, the development is a very big deal. So, the partnership really reflects that level of scale, automation, investment. But Levi's is an iconic brand – 170-years-old – when you think about these sorts of partnerships in that lifespan, it's entirely normal.

When will it go live? June. We start very slowly. We ramp up the new automation. We start off taking over around 70 colleagues from Levi's, welcoming them into our 80,000 strong European workforce. And we'll ramp up over the 12, 18 months to full production, which is around 750 people and 60-some million units. So, this really will be a superhub for Levi's, and we're absolutely thrilled to become their partner.

Scott Schneeberger – Oppenheimer

Thanks Richard, I appreciate that.

I'm going to follow up, I think Baris probably for you. Just on the 2027 financial target update, could you bridge what's changed from your prior 2027 financial target update to what you have now, just to kind of compare and contrast the two? Thanks so much.

Baris Oran – GXO Chief Financial Officer

No problem.

Since January 2023 guidance, you've seen the realities of a lower volume environment reflected in 2023 and 2024 guidance, which led us to rebase our expectations for 2027. We see 2024 gradually improving but it's still a sluggish year.

So, if I go into the components of our EBITDA targets from the prior target to the current target, there are three components.

About 1/3 of this impact comes from rebasing to lower volume levels in the consumer verticals we have seen in 2023 and forecasting in 2024. The rebasing effect is already in our numbers and is primarily behind us.

Another 1/3 is a result of customer realization of footprint given weaker product demand, which has impacted our revenues and also led to a slightly lower margin contribution.

And the last one, as before, we still expect to see a margin uplift from automation and given significant wins in the first outsourcing, this ramp-up has simply been pushed out. But simply put, in 2023, we won a lot of first-time outsourcing projects with low capital intensity and automation. You can see that in our realization of free cash flow in 2023. So those three items is the bridge from the prior 2027 target to the current one.

Scott Schneeberger – Oppenheimer

Thanks, Baris.

Baris Oran – GXO Chief Financial Officer

Thank you.

Operator

Our next question comes from the line of Jason Seidl with TD Cowen.
Please proceed with your question.

Jason Seidl – TD Cowen

Thank you, Operator. Good morning from this analyst here.

Impressive amount of new business wins. I wanted to explore sort of what's going on in the marketplace a little bit. You mentioned you're taking market share. Do you think you're taking market share from existing players who are offering automated services? Or do you think you're taking more market share from players that aren't offering automation?

Also, can you talk a little bit more about your technology offerings, including AI and how you think they're helping you sort of win business? And then I have a follow-up on Wincanton.

Richard Cawston – GXO Chief Revenue Officer

Great. Thank you, Jason. It's Richard Cawston again, I'll answer.

So, look, our focus is on this massive TAM we have of first-time outsourcing. And we're seeing that in the number of deals in our pipeline, we're seeing customers looking to outsource for the very first time like WH Smith, Puma, Castore, et cetera. And what they are looking for is our skill set to help them automate. Automation is, as you know, running at more than 40% of our activity, and it's in every tender, every submission we make and it's on every discussion with the customer. Why is that? Well, it makes the efficiency more optimized. It covers difficulties like labor shortages. And the ROICs are strong and the levels of automation are ever improving. So, it's absolutely the thing they want from us, and it's absolutely the skill set and agility GXO can bring to this massive TAM.

Malcolm Wilson – GXO Chief Executive Officer

And Jason, it's Malcolm here. I think you mentioned you had a follow-up on Wincanton. Let me cover that.

So clearly, we're very delighted to have made this agreement with Wincanton. The deal is now closed. It's a super deal for us. It's a great company, great management team, great team of people and super customers, and I do want to kind of comment that we've been really bowled over by the very positive feedback that we've had from all of the Wincanton management organization and teams and indeed the customers. So, a big, big shout out for that. We're very pleased about that.

As a business, this is going to bring us a lot of revenue synergies. We have not yet done the detailed work on it, but what we can see in our past experience of former M&As with people like Kuehne + Nagel and Clipper and PFS, we can see very clearly the same characteristics. It's going to importantly open up big, new verticals for us. So, industrials, it's not our strength area in the U.K. This is going to make it a strength area. Aerospace, as Baris mentioned, some really big blue-chip customers, public sector spending – and these are all things we can convert not just in the U.K. but across our Continental Europe-wide business. So, it's very, very good from that perspective.

It's accretive pretty much from the get-go, and that's even in advance of the synergy savings that we're going to be bringing in; about $45 million of cost savings. That sounds a lot, but it's bang in line with what our experiences have been in Clipper, in PFS, in other M&A. So, we're very, very confident about that. It's really a very attractive deal from all of that side.

Last comment to say is, look, there's still some regulatory process for us to go in, that's starting now. We expect that will be concluded by the end of the year. We have a lot of experienced people working on that. They work with the CMA just as we did with Clipper. So, we expect a satisfactory outcome on that.

And my last comment is, I mentioned earlier, our U.K. business seems to be the market where we're seeing the earliest real recovery of consumer goods spending. So it’s great news that we're doing this deal right now. I think the timing of it is really very, very good. Baris, maybe just to finish up, I mean we have got Wincanton in our '24 plan. It's in our plan going out to '27. Maybe just worth for Baris to call it out in detail for everyone.

Baris Oran – GXO Chief Financial Officer

Sure. Wincanton is a sizable business with a top line of around £1.4 billion, $1.8 billion, of which we will be capturing eight months in our P&L – around $1.1 billion. And the EBITDA contribution this year will be about $45 million, going from the consensus IFRS EBITDA and adjusting for the IFRS to U.S. GAAP adjustments. And that is already included in our plan.

And taking into account the funding we have done, we expect Wincanton acquisition, prior to cost synergies, will be accretive about $0.03 per share in 2024. That accretion will increase to double-digit percentages as we complete the integration. Very attractive valuation. We are very excited on the integration and potential prospects of Wincanton.

Jason Seidl – TD Cowen

Well, that's some great color.

If I could just quickly follow up here. How should we look at future M&A sort of after Wincanton? Are you looking at expanding into some different geographies?

Malcolm Wilson – GXO Chief Executive Officer

Jason, it's Malcolm here again.

I think right now, our focus is on digesting Wincanton. As Baris mentioned, it's a sizable business. And our teams, they're very skillful at integrating businesses. As I mentioned, Wincanton comes with just a very admirable team of people. So, we're really delighted on that. But right now, our focus throughout '24, really '25, is going to be really on the integration of that.

Thereafter, look, as we've explained, business strategy is always to consider M&A when it's appropriate, when it can bring something new to our business.

Wincanton, a great example – new verticals. Verticals that we're not present in right now that are very difficult to enter without actually being present in the market.

Clipper, you remember when we acquired Clipper – two years ago now – we said very clearly that this would give us the springboard into Germany. And now two years on, well, you're really seeing the evidence of that strategy coming into life. And that's what makes our M&A strategy, I think, a very exciting one. So, we're not really thinking now about M&A for the future. Right now, all minds on making a very smooth integration, delivering on what we've committed to in terms of the Wincanton deal.

Jason Seidl – TD Cowen

Makes sense. I appreciate the time as always, gentlemen.

Baris Oran – GXO Chief Financial Officer

Thank you.

Operator

Our next question comes from the line of David Zazula with Barclays.
Please proceed with your question.

David Zazula – Barclays

Hey, thanks for taking my question.
Just noticing the cash flow guidance, Baris, has not changed from what you previously had. If you could talk about expectations on the cash flow side for the Wincanton acquisition and your expected profile and how that converts to dollars?

Baris Oran – GXO Chief Financial Officer

Of course, David.

Our cash flow in Q1 was actually better than last year, about $26 million year over year up. Our strong Q1 puts on track to achieve 30-40% EBITDA to free cash flow conversion guidance. So, when you're calculating the expectation for the entire year, I would take, including the Wincanton contribution and increased EBITDA number when you convert into cash flow.

Our working capital management has been favorable. We continue to be favorable in 2024. And despite investing very heavily in a lot of projects, we have a very high capital discipline throughout the enterprise. We have high cash flow generation expected this year, above our long-term target of 30-40% in 2024, and we still write high-quality contracts with high return on invested capital.

David Zazula – Barclays

Thanks. And then on the Levi's contract, I don't know – Richard, who wants to take – but you hinted at some automation opportunities in some existing automation. Can you discuss the current automation level of the facility there and what the automation opportunity might be?

Richard Cawston – GXO Chief Revenue Officer

Yes, absolutely, David.

So, in fact, the Levi's is fully fitted out with state-of-the-art automation, end-to-end processes. So really showcased phenomenal attributes to the site, along with its ESG credentials.

As you know, about 42% of our operations are automated. That's split into fixed automation, around 30%, and what we call adaptive tech of around 12%. Now that adaptive tech is absolutely fly in. These are the cobots, the robots, the shuttles and the AI-driven technology that's coming to the market.

You saw our Digit robot announced last year, our humanoid robot, or the earlier part of this year. So that sort of technology we can plug and play into many existing operations, and we can also use it to pivot manual operations into long-term automated operations. When we do that, we improve the margin. We generally drive longer duration contracts, and we enjoy better returns that we share with our customers. So, it's a great thing.

David Zazula – Barclays

Great, thanks very much. I appreciate it.

Richard Cawston – GXO Chief Revenue Officer

Thank you.

Operator

Our next question comes from the line of Amit Mehrotra with Deutsche Bank. Please proceed with your question.

Ben Moore – Deutsche Bank

Hi, this is Ben Moore for Amit at Deutsche Bank. Thanks for taking our questions.

Your 2027 EBITDA target has moved down more than your revenue target implying a lower EBITDA margin. Can you let us know why that's happening?

Baris Oran – GXO Chief Financial Officer

Hi Ben, this is Baris here. Let me take that question.

If we go look into how our margin is improving throughout the new plan from today to 2027, there are primarily three buckets from today's margin. First, is automation. Looking forward, we expect about 30 basis points of incremental margin from higher levels of automation and adaptive technology deployment. We are particularly encouraged with how AI is improving the ROI of automation for our customers.

Number two, Wincanton, we have great confidence in achieving the cost synergies of £45 million given our muscle memory of achieving higher percentage of revenues with Clipper integration. This £45 million is equivalent to about 35 basis points of margin improvement, out to 2027.

And the last component is productivity and central efficiencies, and synergies from prior acquisitions. As a reminder, we have a run rate of about $40 million in 2024 from these programs and we expect another $35 million of savings. So around 30 basis of margin improvement out to 2027.

So, three components: automation, 30 basis points, Wincanton, 35 basis points, and productivity and central efficiencies, primarily giving us another 30 basis point margin improvement versus this year.

Ben Moore – Deutsche Bank

Great, thanks. And maybe a two-parter.

In terms of still assuming the 10% revenue CAGR growth, what is the confidence level in that?

And when can we see some operating leverage in the direct operating cost line? What can you do to drive less inflation and cost creep in that line item?

Baris Oran – GXO Chief Financial Officer

We have a $2.2 billion pipeline increasing wins and improving consumer environment, giving us great confidence as we look into the future. It's going to be a gradual climb. But if I give you the entire bridge of revenue , organic revenue growth of 10%, we roughly expect that to come from 10% coming from new business, volumes to have a low single-digit impact contribution and that is expected to ramp up '24 and '25 and hitting the potential in '26, pricing to come around inflation, which we took about 2% to 3% and the remainder is coming in line with inflation.

As far as business model is concerned, we are working on central efficiency programs which we have highlighted last year, and you see in our financials this year, we are putting more and more efficiencies. That is going to give us further margin uplift, taking cost out from our central, central cost and support cost structure.

But remember, Ben, it's a contractual business model, we have high variable cost, low fixed cost and limited, limited operating leverage in our business model that has always been the case for the last three years. The operating leverage is primarily going to come from the central cost, the site level cost of SG&A and other items. And we have been working on those, and we have been taking costs out structurally.

Operator

Our next question comes from the line of Bascome Majors with Susquehanna. Please proceed with your question.

Bascome Majors- Susquehanna

Thanks for taking my questions.

I know we're a long way from 2025, but can you talk to any of the items that you do have visibility to for next year, give a debt pay down or incremental contribution or just the timing of some of the Wincanton synergies as we think about the bridge to how you expect the business to perform out of this sort of cyclical drag you saw late last year into the early part of this year?

And secondarily, just DHL Supply Chain made some management changes. Do you read anything to that as a strategic change or opportunity for you guys? And just wanted to get your thoughts on that. Thank you.

Baris Oran – GXO Chief Financial Officer

Let me take the initial part as far as Wincanton's contribution to our numbers in 2025, beyond other items and Malcolm if you can comment on the competitive environment.

As I mentioned, Wincanton have about a top line of about £1.4 billion, $1.8 billion. Of which $1.1 is going to be this year. Therefore, you should expect another $0.5, roughly $700 million into next year.

On the EBITDA side, the full year EBITDA is around $80 million, 45 will be this year and the remainder will be next year. Of course, on top of that, we will provide cost synergy items into our guidance, then we provide the guidance in 2025 and as we highlighted, we do see an accelerated environment, which is embedded in our organic growth guidance of 2027 targets. Malcolm?

Malcolm Wilson – GXO Chief Executive Officer

Thanks, Baris, and good morning, Bascome. On the aspect of a competitive environment, and I'll touch on DHL as well. I mean DHL, it's a great company. It's a great team. So, it’s a company that we know really well, and we like them.

In terms of the overall competitive environment, industry is consolidating. I mean, Wincanton, I guess, is a good example of that. And you can see that in all of the major territories, larger companies are getting larger, and that's reflecting what customers are doing in one regard. You know, customers want to be supported by well organized, strong financially organized companies. These large, automated solutions that Richard has mentioned, you know it's really not easy for smaller companies to deploy those kind of solutions. So, the very nature of our market, more and more automation, AI, AI, you know it's really a revolutionary in what we do now in the warehouse alongside automation.

All of these things, it's really best, best accomplished by large-scale businesses. And that's why we see such a strong demand for our services. That's why you see this kind of double-digit new business type of numbers that we mentioned and that you're seeing traditionally over the period that we've been working.

So, I think overall, competitive environment, it is what it is. No large-scale companies like ourselves. There's a tiny number of them. And I think they're all set to do well from this consolidating market and the fact that solutions are becoming more and more complex favors companies like GXO.

Operator

Our next question comes from the line of Brian Ossenbeck with JPMorgan.
Please proceed with your question.

Brian Ossenbeck- JP Morgan

Hey, good morning, thanks for taking the question.

Just the first one, maybe two quick follow-ups on Wincanton. Baris, how are you thinking about FX hedging? Is that in the guidance right now? Are you still deciding will that even be a big impact, in your view?

And then maybe Malcolm, following up on Bascome's question on the synergy timing. Is this a sort of a multiyear timeline before you would get something to show up here kind of like what we're seeing in Germany with Clipper, or are there some synergies that potentially could come faster on the revenue side?

Malcolm Wilson – GXO Chief Executive Officer

Sure, Brian. Let me cover the Wincanton point first, and I'll hand you over to Baris on the other point.

So, Wincanton synergies. Our experience is we shouldn't expect much in the way of synergies during the course of '24. You know, we anticipate the review process to take place probably concluding before the end of the year, but we'll be in the busiest time of the year for our own business in the U.K. and in fact, the Wincanton business.

So, synergy will predominantly flow through during '25 and I would say, probably the first half of '26. When we acquired Clipper, I remember at the time, we talked about a three-year plan, we actually delivered the synergy plan in around two years. And I don't see really the Wincanton environment being much different than that.

So, from a synergies point of view, high level of confidence about the values. We already have identified the different areas, very durable, but we shouldn't really expect to see any significant impact of that until '25 and probably the first half of '26. I'll hand you over to Baris for the second part of your question.

Baris Oran – GXO Chief Financial Officer

On the FX side, as you know, we have sensitivity to euro and pound, roughly 1% move is moving our numbers by about €2 million and another £2 million, 1% move on each currency. And we have so far undertaken decent volume of hedging around three quarters is done for 2024, but we have not done the hedging for Wincanton yet. We will take a look at that during the next couple of weeks. Our guidance today is primarily based on average exchange rate, roughly €1.08 and £1.24, so we'll be looking into locking those so that we can de-risk the P&L for our shareholders.

Brian Ossenbeck – JP Morgan

All right. And just to get Richard, a question on the renewals here.

It sounds like you're booking some momentum on first-time outsourcers that percentage keeps coming up. So, if you can give a little context as to why you think that's happening? Is this sort of something that once it turns, it starts to build momentum? And then maybe you can talk about why people are starting to make these decisions in ways that seem to be in bigger percentages than perhaps we've seen more recently? Thanks.

Richard Cawston – GXO Chief Revenue Officer

Yeah, yes, absolutely, Brian.

The first-time outsourcing is a secular tailwind. I mean we just, as Malcolm said, the challenges are more complex. If you look at continued inflationary environment, our customers need us to help them save money. And automation really is the only way you can deliver a competitive advantage of that. And you need to provide it like, GXO has got a vast catalog and resources to deploy those quickly in an integrated way.

In terms of the speed to market and the velocity were seeing, that's really important because if you think about our book of business and our potential book of business, it's both the magnitude and how quickly it refreshes. And I think that refreshment of the pipeline, which has almost doubled in pace from the trailing 12 months is showing that customers are making decisions and are feeling more confident about the outlook.

So, you know, we've got business coming to outsourcing where we can really help them with our takeover in-place strategy. And we've got customers making decisions faster. And all of that points to a really great year where we expect to outperform our $1 billion in 2023, in 2024.

Brian Ossenbeck – JP Morgan

Okay, thank you for the time.

Operator

Thank you. And our final question comes from the line of Kevin Gainey with Thompson Davis & Company. Please proceed with your question.

Kevin Gainey – Thompson Davis & Company

Good morning, everyone, I appreciate the question.

I think Baris mentioned this earlier, but I wanted to make a comparison on the current pipeline versus the bookings that you guys did in '23. And it goes through that appetite for automation. I think previously said that a lot of the bookings in '23 weren't very automated, and I was wondering how the pipeline for '24 stacked up against that.

Richard Cawston – GXO Chief Revenue Officer

Yes. Absolutely. We see, as we saying, we've demonstrated growth in our pipeline, the win of that pipeline and the turn and our automation is a continuous elevating feature of that. So, in 2023, over half of our wins had an automated element within them. And in our current pipeline, we see around £500 million of automation within there. So, it's a continued requirement.

As I said, there's no RFQ goes to a customer without automation in. And automation can come, is a ramp-up we can build out at the beginning, for example, like Levi's. If you take the partnership, the landmark partnership we announced last year, what we've just finished integrating this year of Sainsbury is one of the largest wins in the company's history. We are automating that over several steps and sequences and that will just bring to life more and more continued efficiency to help our customer be super competitive in their market.

Kevin Gainey – Thompson Davis & Company

Sounds good. And then maybe if you guys could touch on if there's a change in maybe customer, how customers feel with GXO with the addition of Wincanton and the industrials opportunity set that they provide you guys?

Malcolm Wilson – GXO Chief Executive Officer

Yeah, hi Kevin, it's Malcolm here.

I mean it's very early days. What we can say is when we think about our existing customers, they've been very delighted at this deal because you can imagine, we have many, many customers here in North America that want us to provide services for them across all of Europe.

But you know, there's always a hesitation with customers. They like to be able to touch and feel and see in the location, you know in the territory, like kind of services. So, the addition of Wincanton will allow us now to showcase many existing operations. And I think that's when we come to talk about synergy savings, that's why we feel pretty good about that aspect.

Likewise, when they consider the impact in terms of Wincanton customers, again, we've had really positive feedback. There's very little customer crossover. Where there is in fact, there's a small number of customers where we have joint services. But in fact, the services that we actually offer are different services. So even in regard to those customers, they're actually quite pleased to, for their first time, they will start to see a kind of common decision-making, which will help their business planning process also.

So, all in all, I think it's been very, very positive feedback. Many of the industrial customers that sit today in Wincanton, the public sector aerospace customers, you know, what it does do is it opens up the door for them on pan-European services and also, you know, where they have activities in North America for the first time as one organization, we'll be able to support them.

So, generally, I think we feel very good about the top line benefits that are going to come from this role, this deal. But as we saw in Clipper, you know, Germany is really on fire for us now. It's two years after the deal was done, and it does take, you know, whilst cost synergies, you can be very predictable about the timing, revenue synergies they need to work around existing contract timings, the opportunities have changed. So, they tend to be a little bit longer lead time on those. But we would expect to be really seeing material impact from a revenue opportunity synergy, probably two years down the line is when you'll start to see a lot of that activity.

Kevin Gainey – Thompson Davis & Company

Appreciate the color.

Operator

Thank you. Ladies and gentlemen, that is all the time we have for questions today. I'd like to hand the call back over to management for any closing remarks.

Malcolm Wilson – GXO Chief Executive Officer

Thanks, Camilla. And thanks for hosting our call today. We really appreciate it.

We've seen our growth inflect positively in quarter one and believe that we'll see that continue sequentially improving throughout 2024, as consumer spending for goods starts to recover.

We're driving great service and efficiency benefits for both new and our existing customer base and that is reflected in the 55% uplift in first quarter wins and in that growing sales pipeline Richard's commented on.

GXO, were investing to capture a greater share of a strengthening market – which continues to be driven by organizations looking to our expertise in the deployment of warehouse automation and technologies, AI. As a company we will continue to deliver great shareholder value and we look forward to showing the benefits of our acquisition of Wincanton to you in the balance of 2024 and beyond.

With that, I'd like to wish everybody a great rest of the day. Thanks for joining us today and we appreciate all of your attendance. Thank you.

Operator

Ladies and gentlemen, this concludes today's teleconference. Thank you for your participation. You may now disconnect your lines at this time. Have a wonderful day.