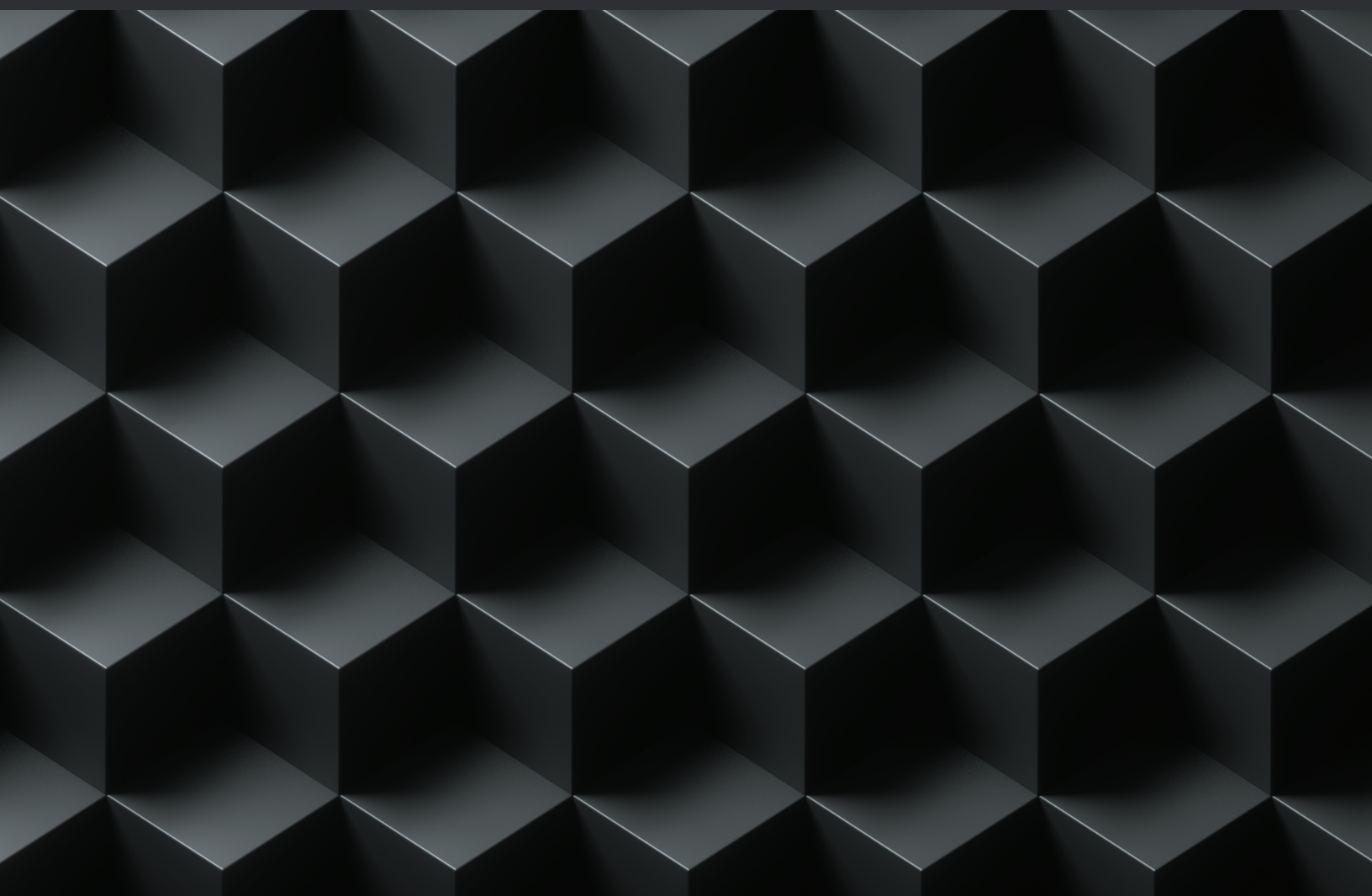


February 14, 2024

# Fourth quarter and full year 2023 earnings call



# GXO Logistics Q4-FY 2023 Earnings Call

## Presenters

**Malcolm Wilson** – Chief Executive Officer

**Baris Oran** – Chief Financial Officer

**Adrian Stoch** – Chief Automation Officer

## Q&A Participants

**Stephanie Moore** – Jefferies

**Chris Wetherbee** – Citigroup

**Scott Schneeberger** – Oppenheimer

**Ravi Shanker** – Morgan Stanley

**Brandon Oglenski** – Barclays

**James Monigan** – Wells Fargo

**Amit Mehrotra** – Deutsche Bank

**Brian Ossenbeck** – JP Morgan

## Operator

Welcome to the GXO fourth quarter and full year 2023 Earnings Conference Call and Webcast. My name is Daryl 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 would now like to turn the call over to GXO's Chief Executive Officer, Malcolm Wilson. Mr. Wilson, you may begin.

### **Malcolm Wilson – GXO Chief Executive Officer**

Thank you, Daryl, and good morning, everyone. I appreciate you joining us today for our fourth quarter and full-year 2023 earnings call. With me in Greenwich are Baris Oran, our Chief Financial Officer; and Adrian Stoch, our Chief Automation Officer.

2023 was a stellar year for GXO.

- We raised our adjusted EBITDA expectations through the year, delivering \$741 million for the full year.
- We converted a record 40% of that adjusted EBITDA into free cash flow.
- We signed a billion dollars of annualized new business wins, positioning GXO for continued growth.
- We deployed a record amount of automation, helping our customers to operate more efficiently.
- And we acquired PFS, a premier fulfillment provider in high-growth verticals.

For the fourth quarter of 2023, we generated revenue of \$2.6 billion, and we delivered adjusted EBITDA of \$193 million, in line with our expectations.

We benefited this quarter from our balanced portfolio. Over 1,000 companies partner with GXO across 27 countries where we operate. We handled record volumes for some, while managing a softer peak for others.

For the full year 2023, we generated \$9.8 billion of revenue, growing 9%, of which 2% was organic. As you'll recall, our initial adjusted EBITDA guidance for the year was a range of \$700-\$730 million. We are proud to say we beat the midpoint of that guidance by a healthy \$26 million, with our full-year adjusted EBITDA coming in at \$741 million.

During the year, we closed a tremendous \$1 billion of annualized new business wins, signing significant new partnerships and expansions with a diverse group of customers, including Kellogg's, LVMH, Nike, PepsiCo, and Unilever.

I can't emphasize this point enough: GXO's ability to win a billion dollars of new business with blue-chip customers speaks volumes about the demand for our superior solutions.

At the time of the spin, we talked about a \$450 billion total addressable market, of which \$300 billion is handled in-house – presenting a huge growth opportunity. Only two short years later, about 40% of our wins in 2023 came from outsourcing, up from about 26% in 2022, as customers look to GXO to make a strategic change in their business.

We deployed a record amount of automation into our operations and set all-time volume records at two of our highly automated sites. And we're trialing some very exciting cutting-edge technologies, including AI-powered robots and humanoids, which I'll ask Adrian to update you on in a few moments.

Our expertise in automation and robotics continues to set GXO apart, and our market share is higher in verticals where we've automated for our customers. Our automated solutions enable us to improve service and lower costs for our customers. We are creating the warehouses of the future, and our leadership in this area is a critical part of our long-term growth trajectory.

Through our acquisition of PFS, we've gained an amazing portfolio of over 100 of the world's most iconic brands. PFS is a valued partner for brands looking to achieve a differentiated consumer experience in the luxury and beauty markets. This is a resilient and growing business that had excellent trading results in the fourth quarter.

Now, we're focused on supercharging PFS's growth. For example, our recent North American expansion with Glossier was the product of a strong PFS relationship in one country and the global scale of GXO.

Turning to our outlook for this year. We've issued guidance of 2-5% organic growth, with \$760 million to \$790 million of adjusted EBITDA, for the full year 2024. Baris will cover the detail behind our financial projections, but I'd like to just touch upon a few trends we're seeing that indicate a positive growth trajectory ahead.

- First, the pace of supply chain outsourcing is accelerating. I noted a moment ago that about 40% of our billion dollars of new sales wins in 2023 were activities that were being outsourced. Customers are increasingly turning to GXO to help them navigate the complexities of their supply chain operations.

- Second is the increasing need for returns and reverse logistics. Our reverse logistics grew faster than the group as a whole in 2023 and represents a high-single-digit percentage of GXO's revenues, as both new and existing customers are increasingly asking us to help them manage this critical part of their supply chain.
- And the third, and perhaps the most pronounced trend running through our commercial discussions, is the demand for greater efficiency. In nearly every conversation, our customers are asking for our guidance on how to use automation to improve service and lower costs throughout their supply chains. As the leader in logistics automation, we're uniquely positioned to deliver on these objectives and capture even more of our total addressable market.

We are continuing to sharpen our commercial strategy in order to meet the huge and accelerating demand for our services. On that note, we've appointed Richard Cawston, our head of European operations, to serve simultaneously in a newly created role of Chief Revenue Officer. Our customers are demanding more and more globally networked services, and we're adapting our organization to support them and capitalize on this accelerating trend.

We are also doubling down on our automation leadership to improve our site-level productivity, which Adrian will update you on in a moment.

GXO is firing on all cylinders, with a sound vision for what's ahead. We're winning incredible new business, growing share, and delivering best-in-class services to our customers.

And with that, I'll hand you over to Baris to walk you through our financials and guidance.

Baris, over to you.

## **Baris Oran – GXO Chief Financial Officer**

Good morning, everyone.

As Malcolm laid out, 2023 was a remarkable year for GXO.

- Revenues grew 9%, operating income grew 31%, and net income grew 16%.
- We maintained an operating return on invested capital above our target of 30%, delivered strong margin performance in a lower growth environment, and converted more than 40% of our adjusted EBITDA to free cash flow.

Turning to the details:

For the full year of 2023, we generated revenue of \$9.8 billion, growing 9%. We delivered adjusted EBITDA of \$741 million. Our adjusted EBITDA margins were also resilient, overcoming a headwind of approximately 70 basis points due to the net effect of pensions and FX.

Our operating income for the full year 2023 was \$318 million, up 31% year over year. We delivered net income of \$229 million, up from \$197 million in 2022.

In the fourth quarter, we generated revenue of \$2.6 billion, as well as adjusted EBITDA of \$193 million. As Malcolm mentioned, we won a billion dollars of new business in 2023, and the average length of contracts signed in the fourth quarter set a new all-time record of well above six years.

Our fourth quarter operating income was \$87 million, growing 18% year over year, and net income was \$73 million, up from \$46 million in 2022. Our operating return on invested capital, at 36%, was once again well above our target.

In 2023, we surpassed all expectations on free cash flow. We have sharpened our focus on capital effectiveness. From a capex perspective, we have allocated investment to technologies and services that drive the greatest returns for our customers. On the working capital side, we achieved stellar cash collection. All of which drives high compound returns for GXO.

As a result of these actions, we delivered an outstanding \$151 million of free cash flow in the fourth quarter, taking the full year to \$302 million. We converted more than 40% of our adjusted EBITDA, which was significantly ahead of our target of 30%. I'm very pleased that in 2024 we also expect to be ahead of this target.

We lowered our net leverage levels to 1.6x, down from 1.8x at the start of 2023, which includes the financing of our \$150 million acquisition of PFS. Operationally, we are ahead of the net leverage targets that we set at the beginning of 2023.

Our balance sheet remains rock solid and investment grade. We have no debt coming due in 2024, and we're pleased to have received credit ratings outlook upgrades from S&P, Moody's, and Fitch in 2023.

This illustrates both the significant need for innovation in the market, and GXO's exceptional ability to meet that demand.

Now, turning to our guidance.

For the full year 2024, we expect to deliver organic growth of 2-5%. We anticipate a sequential acceleration of growth throughout the year. Our early trading results in January indicate that our first quarter organic growth shows an upward sequential trend. Based on the input from our customers, we believe the fourth quarter was the bottom.

We're basing our full-year growth projections on the following factors:

- First, we have several significant new business starts ramping up throughout 2024, including notable wins in the aerospace and industrial verticals, as well as with brands such as LVMH, Mars, and Sainsbury's. Some of these are highly automated sites that take slightly longer to fully implement, hence the ramp-up throughout the year.
- Second, while many of our verticals are performing very strongly, several of the consumer customers that saw softer volumes in the second half of 2023 are expecting sequentially higher growth throughout the year.

- Third, our year-on-year comparisons get significantly easier as we progress through the year.

We also expect to deliver \$760 million to \$790 million of adjusted EBITDA. And to reiterate, we expect to convert 30-40% of our adjusted EBITDA into free cash flow, above our 30% long-term target. This cash conversion trajectory points to approximately 1x net debt to EBITDA by the end of 2025.

Roughly half of our billion dollars of new business won in 2023 will go live in 2024, and we've already booked nearly \$230 million of additional incremental revenue for 2025. All taken, we expect to see revenue accelerate through the year. With incremental 2025 revenue already 29% higher than at this stage last year, we are very excited about our long-term growth trajectory.

GXO continues to drive and compound great returns on capital. Our operating return on invested capital is significantly above 30%. We have generated an unprecedented amount of cash flow this year while taking our leverage to 1.6x. This provides us with the balance sheet flexibility to continue our disciplined M&A strategy.

While our primary focus is on organic growth, we're delighted to be able to allocate capital into more and more automation contracts that are getting longer, proving the value we create to our customers — global brands, across the world.

And with that, I'll hand it over to Adrian to update you on our automation progress and outlook.

Over to you, Adrian.

### **Adrian Stoch – GXO Chief Automation Officer**

Thanks, Baris. Good morning, everyone.

2023 was a standout year for GXO in automation.

- We won multiple long-term, highly automated contracts with global blue-chips, and over half of our billion dollars of new business wins in 2023 are expected to generate revenue from automated operations.
- We are delivering on our long-term promise of increasing our revenue from automated operations, which has risen from 37% to 42% year over year as of the fourth quarter.
- A major contribution to this was increasing our total units of warehouse automation by about 50% year over year.
- We further entrenched our technology leadership position and trialed a broad range of new hardware and software solutions, including humanoids, AI-powered robotics and autonomous vehicles. As Malcolm noted, we are creating the warehouses of the future.

We're talking with customers every day about supply chain efficiency and how to solve their complex problems. Every company with goods to move is looking for ways to make their

fulfillment operations more productive today and more resilient tomorrow. Our competitive advantage is helping our customers bring efficiency to life in their site operations.

Customers' needs for automation differ based on their experience and business model. Some want to invest in transformational large-scale automation. Others need a new partner to take over an existing operation. And many are outsourcing their operations for the first time. We pride ourselves on being able to meet any customer need with tailored solutions for best-in-class results.

Of our billion dollars in new wins for 2023, approximately 45% will be automated through the contract. In addition, we typically see annual conversion rates of 5-7% from manual to modular adaptive tech through our own continuous improvement programs. This means we expect over half of that billion dollars of new wins will result in automated revenue for GXO.

One of the biggest wins is a 15-year contract with a global sports brand, where we've selected and designed the appropriate technologies to enable a completely integrated end-to-end flow through the warehouse. This solution is key to the customer's European growth plan. It will provide them capacity for same-day fulfillment of up to 3 million units per week. Our deep experience and domain expertise with this level of complex automation was the primary driver for our success in winning this contract, and continues to differentiate GXO in the market.

Looking forward, the industry as a whole is nearing an inflection point with more and more global brands pursuing this type of transformation. We have nearly half a billion dollars of large-scale automated sales opportunities.

On average, these large-scale automations carry a significantly longer contract duration. Our automation portfolio also delivers margins more than 200 basis points above group levels, making our business stickier and our growth more profitable.

In addition to driving momentum in automated sales, our team is heavily involved in retrofitting both mature and new technologies to improve site-level productivity. We regularly pilot new innovations, and if the solution meets our performance thresholds, we then deploy it across our network.

In 2023, we increased our total units of warehouse automation by 50%, that included doubling our vision tech, which optimizes order validation and minimizes errors. It's a highly efficient technology that can be rolled out in operations across numerous verticals, without requiring significant capital investment. The operations where we implemented this tech saw an average margin expansion of 300 basis points.

We're also actively identifying practical applications for AI in our existing operations and have successfully trialed solutions for pick productivity and workforce management. We're excited that the pick solution delivered a productivity increase of approximately 15%, and we're now rolling out the application to dozens of sites in 2024.

Finally, given our rapidly expanding scale and leadership position, we're beginning to achieve meaningful procurement savings. We're already benefiting from significant reductions to list price in various categories.



GXO has built a global technology ecosystem that is unrivaled in our industry, and the need for our solutions continues to grow every day.

Our scale and reach have materially shaped the warehouse automation landscape, and we're beyond excited as to what lies ahead and the major impact of GXO's role in building the supply chain of tomorrow.

And with that, I'll pass back to you, Malcolm.

## **Malcolm Wilson – GXO Chief Executive Officer**

Thanks, Adrian.

This was the year that we proved our business model, with resilient margins, strong cash flow, and adjusted EBITDA growth that surpassed our expectations. We won a billion dollars of great new business and expanded the gap with the competition through our investment in high-return automation that meets our customers' increasing demand for outsourcing.

Before we close, I want to thank our employees for their tremendous performance during peak and throughout 2023. Their hard work and continued commitment to our values was the engine that delivered a truly great year for GXO.

Looking forward to 2024 and beyond, we're building on this momentum. Our automation leadership is driving stickiness and profitable growth with global customers looking to make their operations more efficient. We expect our growth to accelerate, driven by new wins, with incremental won revenue for 2025 tracking nearly 30% ahead of where we were a year ago.

We are very excited about our growth trajectory, as we focus on delivering the best possible solutions to our customers and generating strong returns for our shareholders.

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

## **Question & Answer Session**

### **Operator**

Thank you. We'll 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 your questions.

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

Hey Stephanie, can you check if you're muted, please? Stephanie, are you able to hear us? Okay, we'll come back to you.

## **Stephanie Moore – Jefferies**

Oh, I'm sorry. Can you hear me now? Sorry about that.

## **Operator**

We can hear you, yes.

## **Stephanie Moore – Jefferies**

Great. Okay, Baris, thank you so much for all the color and outlook for 2024.

But maybe if you could discuss what you're seeing across geographies and verticals and early 2024 results that could give you confidence that volumes and revenue growth can accelerate from 4Q? Thank you.

## **Malcolm Wilson – GXO Chief Executive Officer**

Hi, Stephanie. Good morning, it's Malcolm here. Let me cover some points on that.

So, if we look at the broad macro where GXO is operating: Continental Europe business, that's actually continued to do well. It recovered through the middle part of last year, and we're seeing similar trends right now in that business. Pleasingly, I think we're starting to see some recovery in our North American business and U.K. business. Green shoots – it's early days, but definitely we're seeing, as we've moved into '24, we're seeing a different landscape than as we've left 2023.

When we look at the different categories of products that we deal with, we can broadly say that our food and beverage related business, technology, consumer, electronics, industrial manufacturing, they're all really the highlights. I would say slower is our omni-channel retail and consumer packaged goods. So, there's no doubt the consumer is still under pressure. You know, we look at the metrics. We can see consumer spending money on services. But goods, it's still a sluggish environment.

Staying with the macro, I think one of the pronounced trends we've seen during the latter part of last year, and it's a trend we're starting '24 with, is across all of the different geographies. Our customers have been managing carefully inventory levels. I think there's been an adjustment to take into account what was generally a sluggish 2023. People have managed inventory levels smartly. We've been super proactive in working with our customers to do that also and customers have valued our inputs on that.

And generally I think we've seen organizations prioritizing price more than volume. And that gives you a feel for our last quarter volumes. It's early days, but I would say our trading results for January, they're definitely indicating a stronger trajectory for '24 than we were seeing in the last quarter. So, it's a bit early to judge what the first-half of the year will look like, but definitely encouraging signs.

When we talk to customers, I would say, directionally speaking, they all expect their activity to be increasing sequentially as we're moving through 2024. Probably a slower first-half with a faster second-half. And I think that's broadly in line with every kind of commentary that we're seeing at the moment.

What's pleasing for us is we've just finished '23, we had really a great season for new business, a billion dollars of new business against that slower macro – that should not be underestimated. So, we're very pleased with that.

As Adrian mentioned, a lot of big-ticket implementations going on this year.

Our pipeline is strong, you know, it's held up incredibly strong and maybe one of the most pleasing aspects for us is our pre-pipeline. We don't talk about our pre-pipeline a lot, but our pre-pipeline right now is about 20% up year-over-year, and there are a lot of big, transformative projects coming into that; projects that will require a lot of automation.

So, all of that gives us a good feeling about 2023. And obviously from a GXO perspective, as we move progressively through '24, you know, our comps become considerably easier as we go through. So, substantial growth on the pipeline, I think, is what we're seeing right now. And we're going into the year with a degree of confidence about '24 and how it's going to pan out.

### **Stephanie Moore – Jefferies**

Great. No, that was tremendously helpful.

And then just as a follow-up to your guidance for 2024: It does look like your free cash flow expectations assumed the higher free cash flow conversion. Is there a structural change there that we could expect a similar level of conversion on a go-forward basis? Thanks.

### **Malcolm Wilson – GXO Chief Executive Officer**

Let me hand you over to Baris, Stephanie, for that detail.

### **Baris Oran – GXO Chief Financial Officer**

Hi, Stephanie.

We had excellent collection and capital efficiency, and we had record free cash flow. Our free cash flow in Q4 was \$151 million up year-over-year, and our strong Q4 helped us deliver over \$300 million of free cash flow for the entire year, which was a conversion rate of 41%, comfortably ahead of our 30% to 40%.

And with this pace, we forecast roughly debt levels to be around 1x debt to EBITDA by the end of 2025, creating roughly \$2 billion of balance sheet capacity to be allocated either to accretive, disciplined M&A in all geographies or we evaluate potential of returning capital back to shareholders through a buyback.

So, we will create incremental cash flow beyond investing in our automation and technology, and that's driven by excellent collections and capital efficiency.

### **Stephanie Moore – Jefferies**

All right. Thank you guys so much. Appreciate it.

## **Operator**

Thank you. Our next questions come from the line of Chris Wetherbee with Citigroup. Please proceed with your questions.

## **Chris Wetherbee – Citigroup**

Hey, thanks. Good morning, guys.

I guess maybe wanted to talk a little bit about the organic revenue guide for 2024. I was hoping maybe you could break that down into the parts, what you see in terms of new business wins, what attrition looks like. Also importantly, how volume plays out. Fourth quarter volume sort of seems fairly weak, so I want to get a sense of how you see that ramping up over the course of '24?

## **Baris Oran – GXO Chief Financial Officer**

Hi Chris, it's Baris here. Let me take that.

We expect higher growth in 2024. We already signed nearly \$600 million of new business impacting 2024 and we will continue to sign more business, which we expect to grow given the good outsourcing opportunities in our pipeline throughout this year. There has been a really a great outsourcing opportunity in all geographies we see right now. Our services are high in demand.

We expect to see positive, but lower contribution from pricing and look for steady underlying customer turnover. There will continue to be some impact, at least at the start of the year, from the lower footprint of our customers, given their lower inventory levels, which gives us roughly 2-5% organic growth in 2024. Our growth will accelerate given the ramp up of customer projects we have and easier year-over-year comp. And if you look into our earlier trading results in January and as we talk to our customers, that view is confirmed.

## **Chris Wetherbee – Citigroup**

Okay. And just so I'm clear, though, should we assume sort of still somewhat negative in the first part of the year turning positive as we move forward? So, 1Q maybe still is a little on the negative side, or are you able to turn positive based on what you see through January?

## **Baris Oran – GXO Chief Financial Officer**

In Q1, we definitely expect an improvement over Q4, and the earlier trading results are showing us that.

## **Chris Wetherbee – Citigroup**

Okay, helpful. And then the follow-up would just be translating that to the EBITDA side. I guess as we think about the potential for incremental margins, is '24 a year where you'll be able to see maybe some degree of expansion there? I guess maybe talk a little bit about the puts and takes that are going on there. I know you have some of the cost efficiencies flowing from '23 to '24, you have PFS – I'm just kind of curious about the moving parts there.

### **Baris Oran – GXO Chief Financial Officer**

Sure. Our margins yet again prove how strong this business model is. Our EBITDA percentage margin will be steady in 2024. Nominally, we expect \$760 million to \$790 million, with a midpoint of around \$775 million. Our organic growth, supported by deployment of robotics, automation, and outsourcing will contribute to our margin expansion. PFS is trading well and will contribute. Our central efficiencies program, which we highlighted in detail, will provide an incremental \$14 million benefit, and we've gone through the details in the earlier call.

And all of this balanced with our investment in our capabilities and organization, including our sales and business development teams, where we see phenomenal opportunities, our automation focus, which is selling really, really well, and our investment in our cloud-based systems turning our potential into performance and will fuel our growth in the future.

### **Chris Wetherbee – Citigroup**

Okay. Thanks for the time. Appreciate it.

### **Baris Oran – GXO Chief Financial Officer**

Thank you.

### **Operator**

Thank you. Our next questions come from the line of Scott Schneeberger with Oppenheimer. Please proceed with your questions.

### **Scott Schneeberger – Oppenheimer**

Thanks very much, good morning.

A couple questions. I guess the first one, Baris, for you following up on Chris's question.

Could you speak to maybe a year-over-year bridge outlining kind of the primary drivers of adjusted EBITDA in 2024 versus 2023? What are some of the big puts and takes that we're looking at year-over-year? Thanks.

### **Baris Oran – GXO Chief Financial Officer**

Sure. The largest components are organic growth and we expect that to accelerate throughout the year. As we highlighted, we've been a lot more outsourcing projects and technology, our automation and robotics is a huge enabler on that one. PFS will continue to trade well and contribute to our results. Central efficiencies, which we have gone through in detail, both will contribute \$14 million, and we will continue to invest in our capabilities in our organization.

To give you a further highlight on what those investments are. We are investing in our sales and business development teams, automation and robotics implementation teams. We are moving to cloud, both our data centers and software. This is in progress, both financial, HR, IT systems across the board. And we are actively working on outsourcing with a third-party on some non-course support functions activities.

This was all part of the plan and we're moving forward in early part of 2024 on those plans. All of those, as you would recall, was what we highlighted in our capital market day and was going to give you a full-year effect over \$100 million by 2026.

### **Scott Schneeberger – Oppenheimer**

Great, thanks, Baris.

I guess, probably for Malcolm and/or Adrian primarily: you guys have highlighted today, I mean, GXO is a really large target addressable market. It gets significantly larger when customers who don't yet outsource their warehouse and supply chain operations to a third-party provider get involved. And clearly, your mix of contract wouldn't increase substantially year-over-year. So, I guess my multi-part question here is, it sounds like reverse logistics is a big driver of this outsourcing trend. What type of growth rate are you getting? It sounds like it's above the average, but what type of growth rate are you getting in reverse logistics? And do you anticipate that accelerating?

And then also, kind of this follow on, with outsourcing a more meaningful mix, what type of gross new business win run-rate do you anticipate over the coming few years?

### **Malcolm Wilson – GXO Chief Executive Officer**

Scott, It's Malcolm here. Let me take the first part of that, and then I'll ask Baris to come in on some of the numbers.

You're absolutely right, reverse logistics, it's a huge growth area for our business. Right now, across our total company, it's starting to represent high-single-digits of our combined activities. And when I look at the sales pipeline, it's very clear to see there's a huge number of projects coming through with a high degree element of reverse logistics.

If you remember back right to the beginning of GXO, we always talked about those big tailwinds – more and more companies outsourcing their logistics. Well, absolutely in '23 we can see that in absolute action. You know, 40% of our business wins coming from that category. That's a real growth, probably outstripping our own expectations even.

We also talked about automation, and Adrian has already touched on that. And again, those outsourcing contracts – people outsourcing sometimes for the first time – automation plays a huge part of it, because people are catching up, they're recognizing that efficiency is everything and automation is a simple way for us to drive that.

And then lastly, e-fulfillment, we don't talk so much about it but it's still one of our fastest growing activities. And again, automation playing a big part of it. So, these are the trends we're seeing as we've seen in '23. We think we're going to continue to see those growth engines across our business. And really, I think we're in a super position to capitalize on that as GXO. Baris?

## **Baris Oran – GXO Chief Financial Officer**

Yes, reverse revenue is growing faster, and we expect that to grow faster yet again in 2024. And when you look in our investment strategy, what sells right now really, really well is outsourcing, automation, robotics, and that's where we are putting our human capital and monetary capital. We are giving up our team and talent in the business development and also implementation teams on automation. This is a huge cycle and GXO is winning through differentiation and automation.

## **Scott Schneeberger – Oppenheimer**

Thanks.

## **Operator**

Thank you. Our next questions come from the line of Ravi Shanker with Morgan Stanley. Please proceed with your questions.

## **Ravi Shanker – Morgan Stanley**

Thanks. Good morning, everyone.

Good job with the progress on the pipeline of new business. Can you elaborate on that a little bit more? I think, Malcolm, you said that there was some transformative projects in there. Can you expand on that a little bit?

And also, are you seeing any changes in customer behavior? Are people like looking to run with less inventory than before because of higher interest rates or something?

## **Malcolm Wilson – GXO Chief Executive Officer**

Yes. Hi Ravi, Malcolm here – good morning.

Let me cover those few topics and I'll also ask Adrian to come in on the shape of the pipeline and what customers are saying.

As I mentioned right at the beginning of this call, one of the very pronounced points that we've seen in 2023, and no surprise, customers are eager to look how we can improve, how we can bring new efficiency, help them in the task of becoming more efficient in their own organizations. And clearly, automation plays a huge part of that. It's really leaning into our wheelhouse. We're seen in the marketplace as an innovator able to help organizations bring more efficiency.

And again, no surprise, a huge amount of our business wins, are companies who are looking to outsource, looking to partners like GXO for the very first time. It's been a big source of growth and I think that's a trend that we're going to continue to see. So, higher interest rates, higher inflation, all driving people to need to look for more efficiency.

Adrian, may be useful just to share on some of that metric in the context of automation also?

## **Adrian Stoch – GXO Chief Automation Officer**

Yes, thanks, Malcolm. So, this is Adrian. Good morning, everyone.

What's occurring in the industry is a very exciting flywheel combo effect between outsourcing and automation. And the need for enterprise digital transformation is leading organizations to reexamine their entire supply chains, because they understand that they need to go through this reexamination to stay competitive for today and increase resilience for the long-term. And we see this transformational trend in the numbers that both Malcolm and Baris have cited this morning where 40% of our wins comes from outsourcing and over half will lead to revenue from automated operations.

And we need to keep in mind that this trend, we're really just at the starting point of this, what's occurring. And our excitement is not only because of the potential benefits from automation, but because this industry is still predominantly very manual, and companies understand that in order to get the resilience that they need for the future, they need to elevate how they're viewing supply chains and what they're doing today to be in that position for competitive resilience in the future.

## **Malcolm Wilson – GXO Chief Executive Officer**

And Ravi, just one last point.

You asked about inventory levels – I guess one of the trends we saw in the latter part of last year was organizations really adjusting inventory levels to suit the sale of goods. People need less inventory if they're selling less products. So, no doubt whatsoever we saw that trend. We think that will start to reverse as economies pick up. No doubt we missed customer volumes in last year, but really we expect those will start to return as general macro starts to strengthen across all of the geographies that we're seeing. So, definitely that's something that we're looking for in '24.

## **Ravi Shanker – Morgan Stanley**

Got it. It sounds cyclical more than structural.

And then maybe as a follow-up here: given the strong free cash flow end to 2023 and the guidance for '24, how are you thinking about the balance sheet and the priorities there? Any specific targets you've identified on the M&A side?

## **Baris Oran – GXO Chief Financial Officer**

Yes, Ravi we do have a very sizable pipeline of M&A targets in all geographies, all verticals – we're actively working on a number of projects. But we are also very, very sensitive about shareholder value creation. We want to extract a lot of top line growth, of incremental capabilities in additional verticals, capture a lot of cost savings, so that should pay for our shareholders.

Otherwise, when we have excess cash, buying back our shares is another option. Investing in our company through buybacks is another option. We always weigh those and always put shareholder value creation top of mind.



## **Ravi Shanker – Morgan Stanley**

Very helpful, thank you.

## **Baris Oran – GXO Chief Financial Officer**

Thank you.

## **Operator**

Thank you. Our next questions come from the line of Brandon Oglenski with Barclays. Please proceed with your questions.

## **Brandon Oglenski – Barclays**

Hey, good morning and thanks for taking the question.

I was wondering if you could talk to the organic growth outlook? Because I think if we go back to your Investor Day, the long-term CAGR was something like 8-12%, which is pretty significantly higher than what you're going to get this year.

And I think we've discussed the volume issue quite a bit on this call. But can you put it in the context of the sales pipeline because I think your pipeline was similar at this time last year. And in fact, contracted revenue for the next year was actually maybe a little bit higher if we go back just 12 months. So, is it also just cyclical?

And should we expect as volumes come back, the contracts come back and you could actually exceed the top end of that range for the next couple of years?

## **Malcolm Wilson – GXO Chief Executive Officer**

Hi, Brandon, it's Malcolm here.

Yes, I think in a nutshell, that's how we do see things.

So, effectively, '23, it's been a sluggish year. We've seen that in customer volumes, inventories, that's what we manage it throughout the warehouses. But as we're going into '24, we can see signs of a stronger sales pipeline, but also importantly, it's not just about the size of the actual, the number of dollars in the sales pipeline. It's the kind of vertical activity that we see coming through. It's the speed at which we can take business on. Big, automated sites tend to carry a longer lead time for starting up then a kind of takeover-in-place. And one of the aspects we've seen throughout last year.

And again, if we look at our sales pipeline, we can see quite a lot of projects where customers eager to transform their own supply chain, eager to transform their own warehousing activities. They're looking for GXO to step into an existing operation, and then bring automation progressively through the life of the contract. And that can take several years, and there were some large high-profile customer examples of that during 2023 that we're actually still implementing.

So, I think when we look at the future activity, all of the building blocks that we talked about in our Investor Day are really there; they're on track – lots of signing of high-quality long-term business. We saw that in '23, even against that tough macro.

Outsourcing, people choosing to outsource – that big proportion of the addressable market that really was never really part of our calculation – that's accelerating and again, we've seen that throughout '23. We see it in our sales pipeline now going forward.

As Adrian has just mentioned, so much more in the context of automation and robotics is driving, it's really driving business towards GXO. Even last year, 67% year-over-year increases of the deployment of these kind of projects. And as Baris mentioned, all the productivity projects well on track. So, we're really feeling good about the future outlook for GXO.

### **Brandon Oglenski – Barclays**

Appreciate that, Malcolm. And a quick follow-up for Adrian.

On automation, I think you said your automated facilities went up like 50% this year. That's pretty significant. Or sorry, last year.

Can you tell us about the margin profile of these contracts and potentially maybe higher capital investments as well?

### **Adrian Stoch – GXO Chief Automation Officer**

Yes, absolutely.

So, what we typically see with our automated projects – and this comment goes both to the large-scale automation and where we do the more modular retrofits – is we see 200 to 300 basis points above the group average coming from those automated operations. And this is really a proof out of the thesis that when we automate, we're able to reduce the dependency on other elements of the cost structure, reduce dependency on labor to a certain extent. And so the automated opportunities and the efficiencies that we've always expected and suspected would come from those opportunities, they're bearing out in what we're seeing in the numbers.

### **Brandon Oglenski – Barclays**

Thank you.

### **Operator**

Thank you. Our next questions come from the line of Allison Poliniak-Cusic with Wells Fargo. Please proceed with your questions.

### **James Monigan – Wells Fargo**

Hey, guys. Good morning. James on for Allison.

I wanted to follow-up on Brandon's question around automation and the organic revenue growth guidance.

You've commented that the highly automated facilities have these longer lead times to start and it seems like the contract wins, at least in this quarter were a bit longer dated. Does 2024 sort of have to work its way through like an organic revenue growth pocket in any way because what you're winning is sort of longer dated out that sort of would fade over time? Or is it really just all essentially sort of weakness in sort of end market volume that's sort of driving that organic revenue weakness versus the long-term guide?

### **Baris Oran – GXO Chief Financial Officer**

Hi, it's Baris here. Let me help you out with that question.

In fact, the reason we are writing longer-term contracts is because we are selling more and more automation and technology. Some of these contracts are over 10 years, close to 15 years, are very, very sticky for our customers. And in this environment of high interest rates, the longer the contract, the more affordable for our customers and we expect that trend to continue.

As you highlighted, it takes a while – it takes more than three quarters to get them up and running. It takes up to 15 months sometimes to get them at full maturity for margin and capacity. So, we will see contribution from these implementations towards the second half of '24 and in '25 more vividly.

### **James Monigan – Wells Fargo**

Got it. And is there any front-loading of expenses associated with those deals in the front half? I'm just wondering if you could put a number around what that might be?

### **Baris Oran – GXO Chief Financial Officer**

Generally, the maturity of those contracts, the margins start very low and they mature over time. That's especially for the automation contract, that's valid.

However, what is impacting our margins is our investments in our core capabilities as well: in our cloud-based systems, in our sales and business development teams, and our automation and robotics teams. We are investing in those because we see huge potential for selling more and helping our customers more via these projects.

### **James Monigan – Wells Fargo**

Thank you.

### **Baris Oran – GXO Chief Financial Officer**

Thank you.

## Operator

Thank you. Our next questions come from the line of Amit Mehrotra with Deutsche Bank. Please proceed with your questions.

## Amit Mehrotra – Deutsche Bank

Thanks, operator. Good morning, everybody.

I want to start with, I guess, a bigger picture question for Malcolm. Malcolm, we're seeing high numbers of U.S. warehouse capacity that's basically available for sublease or sublet. I think the number this morning in the Wall Street Journal was almost 160 million square feet available for sublease.

I'm wondering how that impacts the business? Because on one hand I think your customer is more strategic, and obviously, the duration of the contract is longer. So, I don't know if this is more of a cyclical issue, but it will be helpful – I know you've been in this business for three, four decades – it would be helpful to get a little bit of historical perspective of the cyclicity in the amount of sublease capacity in the U.S. warehouse or the global warehouse market and how this may impact the business in the near to mid-term?

## Malcolm Wilson – GXO Chief Executive Officer

Amit, hi, it's Malcolm here.

And your question is really topical. I've also seen plenty of news reports about incremental capacity here in the North American market.

From our perspective, a good way to explain it is the core of our business is contracted, long-term contracts. So, customers tend to occupy a warehouse. They fund the warehouse. It's part of the cost makeup. It's part of the contract makeup.

So, in regard to our core EBITDA, it's actually quite a neutral aspect from our point of view. And you see that in our '23, our actual EBITDA came in ahead of our original outlook. We were well ahead in terms of the full year. What you do see, though – and this is one of the big benefits that GXO brings to our customers – is we see inventory levels will flex in any year up and down, what we have seen through '23 is a more pronounced lowering down of inventory levels.

So, customers, it takes some time to change, some time to change manufacturing plans, to reflect new sales outlook, but gradually, they've lowered down inventory levels. For us, we see that in the environment where we work with them proactively to consolidate warehousing activity. So, for large customers, we might have several fully contracted warehouses, but we might also operate some transient warehousing where for GXO, we have relatively short-term commitments on it.

Those kind of warehouses, it's in our interest and it's in our customers' interest to contract those volumes back into our main centers. And that's exactly what we've done. That's what being a proactive partner is all about. But the end result of that is you're absolutely right – when you look at the real estate market, progressively, you end up with more empty capacity.

So, for us, we see we don't see it so much in our profitability. We do see it in our top line growth because that volume we're no longer invoicing. And we expect to see that resurge back pretty much in alignment with as we would expect the macro to start becoming stronger for consumer goods. Today, it's already strong for services, but we need to really recover properly for consumer goods.

So, I hope that gives you an understanding of how we see it as a business. But we are seeing exactly what is widely reported at the moment, but not really impacting us in terms of how we judge our profitability or how we judge our customer relationships. For those, it's more an opportunity for us to demonstrate our worth to our customers.

### **Amit Mehrotra – Deutsche Bank**

Got it. Okay. That's very helpful.

And I just wanted to follow-up on the M&A question really quickly.

Because if I look at the M&A strategy over the last couple of years, it's really been about buying companies within markets that you already have a pretty strong presence in. So, I think about Clipper, or the U.K. business of Kuehne + Nagel, even PFS. Generally, you're taking out – there's significant cost synergies on the SG&A side. But then you also have verticals and geographies maybe that you're underrepresented in.

So, as we think about like where your M&A focus is going to be going forward, if you can just talk about are we talking about new verticals and geographies?

Are we talking about the same playbook, which is, 'hey, we already have a great presence in this market, this vertical. Why don't we just buy this company and kind of consolidate cost structures?'

### **Malcolm Wilson – GXO Chief Executive Officer**

Amit, let me carry on the answer. Malcolm here.

So, we review everything on it. Clearly, there are geographies where we want to be in new verticals. And when we enter a new vertical, typically, we're focused on growing that new vertical.

So, PFS is a great example. It's not a play about driving a lot of cost synergy. There is, of course, when you put two businesses together, you gain cost synergy. But it's a play about driving bigger growth, and we're off to a great start with PFS. It's already – it's doing very, very well. We're very, very pleased with the PFS team and how that business is integrated into GXO.

But there are other aspects where we have to look opportunistically as well. If there's a business out there that we like – good quality, it's in good condition, and we can see big synergies – of course, we'd be interested also in those.

So, I would say it's about what's out there in the market, what we're trying to accomplish at the time, and as Baris mentioned, overarching all of that, it's got to be delivering accretive

benefits. It's going to be in the interest of the company and in the interest of our shareholders. That's really how we look at the market.

### **Amit Mehrotra – Deutsche Bank**

Got it. Okay, very helpful, guys. Thank you. Appreciate it.

### **Operator**

Thank you. Our next questions come from the line of Brian Ossenbeck with JP Morgan. Please proceed with your questions.

### **Brian Ossenbeck – JP Morgan**

Hey, thanks. Good morning.

So, maybe a question for you, Malcolm. Do you think this change we've seen more recently – moving to more contracts that are outsourced for the first time – is that durable and something we should expect will continue? Or do you think this is sort of like a lagged impact from several years of supply chain disruptions and now people are starting to really move forward with a tranche and there might be an air pocket next year or the year after?

So, just wanted to see how you thought through that and if there's anything we should expect in the contracts in the structure? More tech, more efficiency, more automation, if those are going to change or if that more or less stays the same?

### **Malcolm Wilson – GXO Chief Executive Officer**

Hey, Brian, I think what we can see right now is a trend that's going to continue.

Remember that we called out this trend all the way back in, I think, 2020, even pre the spin of GXO, that more and more companies were going to outsource their logistics. The reason we said that at the time and the reason it really still holds correct – it's been reinforced, I think, through '23 – is the fact that, one, we've had several years of disruption (the pandemic, supply chain disruptions, manufacturing disruption).

And then on top of that, we've had 1.5 years of really severe kind of inflationary pressure, interest rate pressure. That's put a burden on so many organizations who don't want to pass those incremental burdens on to the consumer. So, they look at how can they do things differently, how can they do things more efficiently.

And for most organizations, it's very daunting when the obvious solution probably involves bringing technology into the warehouse. They're not generally equipped to do that. So, it's a logical step for them to look for an outsource partner. And as the largest pure-play contract logistics company in the market with our reputation for delivering these big projects on time, being a reliable partner – for us, it's super. I mean, this is all playing into GXO's wheelhouse. So, we're very excited about it.

That trend is set to stay. It's the very reason Baris just mentioned, and Adrian; we've doubled down on our expenditure in terms of teams, deploying automation, on our sales organization. I think it's going to be a trend that's going to service GXO very, very well in the future years.

### **Brian Ossenbeck – JP Morgan**

Thanks, Malcolm.

Just a quick follow-up on the inventory dynamics and how they've been a bit more volatile than usual, and it sounds like you expect them to sort of normalize over time for the consumer-facing side. But how does the GXO Direct offering – with the multi-tenant warehouses which expanded with Clipper as well – is that something that's sort of picking up some of that slack? Or is that not big enough to really make a dent in sort of these single-tenant facilities that can move up and down?

### **Malcolm Wilson – GXO Chief Executive Officer**

Brian, for us, it's not a substantial enough amount of our capacity for it to make a real impact. But our GXO Direct customers, just the same as pretty much all of the customers that we can think of, have not been immune to this last 12 months slower pace of consumer spending. So, clearly, across all of our business, we've seen that.

As I mentioned earlier, the vast majority of warehouses that we operate are fully back-to-back with our customers. So, the smaller proportion that sit in our GXO Direct world is really not, it's not any material impact on our outlook.

### **Brian Ossenbeck – JP Morgan**

Okay, great. Thanks, Malcolm.

### **Operator**

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

### **Malcolm Wilson – GXO Chief Executive Officer**

Yes, thanks Daryl, and again, as always, thanks for hosting our call today. We really appreciate it.

2023 has been a great year for GXO. We've delivered huge free cash flows, a billion dollars of new business wins, and, towards the end, we're super excited about the acquisition of PFS which is really performing incredibly well.

We're driving great service and efficiency benefits for both our new, and of course, our existing customers through deploying game-changing technologies right across all of our footprint.

Looking forward, we're excited by the future growth opportunities that we've been talking about on this call.

We're increasingly the partner of choice for the huge in-house portion of our market, which is looking to more and more outsource. And we're growing in a manner that is delivering fantastic returns for our shareholders.

So, with that, we'd like to wish everybody a great rest of the day. Thanks so much for joining us on this call, and your attendance. And I look forward to speaking to you again in the future.

### **Operator**

Thank you, ladies and gentlemen. This does conclude today's teleconference. Thank you for your participation. You may disconnect your lines at this time. Have a wonderful day.