Covenant Logistics Group 4th Quarter 2021 Conference Call

Mr. Hogan – Welcome to the Covenant Logistics Group fourth quarter 2021 conference call.

As a reminder:

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

A copy of the prepared comments and additional financial information is available on our new website at www.covenantlogistics.com\investors. I'm joined by SEVP & COO Paul Bunn, and Chief Accounting Officer, Tripp Grant. David Parker is not able to join us this morning.

2021 was a record year by Covenant in many ways. Revenue, our minority investment, earnings per share, and return on invested capital all achieved record results. Our team battled through the continued effects of the pandemic, the most difficult driver market in history, huge growth in our managed freight division and leadership changes early in the year. We pushed through some large pay adjustments across the enterprise in all areas from drivers, to shop technicians, warehouse teammates and office staff. We're in better shape today from a talent standpoint than we've been over the last year and are excited to tackle 2022. The model transformation that we started five years ago is really starting to prove out with continued opportunities. Our results for 2021 are directly due to the Covenant community, its hard work, commitment to each other and our customers.

In summary, the key highlights of the quarter were:

- Freight revenue grew 27% to $267 million compared to the 2020 quarter,
- Our asset-based truckload group freight revenue grew 9% versus the fourth quarter of 2020 with 186 less trucks,
- Our less asset intensive managed freight and warehouse segments combined grew 56% compared to the fourth quarter of 2020,
- On the safety side, we produced another solid quarter with our DOT accident rate per mile being 19% below the year ago period, the second lowest on record, and 2021 finished the year as the best year on record,
- Our TEL leasing company investment produced a record quarter and year, contributing an additional $.10 per share versus the year ago period,
- We finished the year with an all-time low leverage ratio of .72x, all time low net debt to total capitalization of 15.8%, and all-time high return on invested capital of 13%.
- Additionally, we are very excited to announce the commencement of a quarterly cash dividend program. The work over the last few years to deleverage the company and improve our operating model to produce more consistent results, led our board to this approval. Net indebtedness has decreased by almost $240 million over the last 2 years with a potential to be close to debt free by the end of 2022. The goal is to yield 1% on an annualized basis and at our current share count will impact cash by about $1 million per quarter. We continue to evaluate a full range of capital allocation alternatives to effectively deploy our cash.

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

- For the quarter, our Managed Freight division was our largest division in both revenue and operating profit. Its revenue for the quarter grew 67% and achieved record revenue of $321 million for 2021. Managed freight's favorable results for the quarter were primarily attributable to the robust freight market, executing various spot rate opportunities and handling overflow freight from both Expedited and Dedicated truckload operations. This division remains a major strategic growth opportunity as we have invested more operations and sales resources into the division to continue its momentum into the future. We remain very excited about this leadership team and its prospects for the future.

- The Expedited division grew its revenue by 13% versus the year ago quarter due to both strong rate and utilization improvements. We did invest in our driving workforce in the quarter with a significant pay increase which after several quarters of sequential decline, we were able to hold the fleet size versus the third quarter and increase our seated count. The driver pay investment was our third pay increase for the year and has given us momentum heading into 2022. We are very thankful that our customers value our service and have supported our driving teams in this unprecedented time.

- The Dedicated division had a good quarter and achieved nice sequential and year ago margin improvement despite some unusual corporate expenses that hit both Expedited and Dedicated in the quarter. Had it not been for the 250 basis points of unusual expenses in the quarter, Dedicated would have hit the mid 90's OR target set out at the beginning of the year. Revenue per truck continues to improve as we push through our improvement plan with further rationalization coming in the first half. The 21% revenue per truck improvement in the quarter was a significant contributor to the margin improvement. The pipeline for this division is very encouraging as we start 2022.

- The Warehouse division revenue grew 11% due to the impact of new business late in the third quarter and pricing to offset cost increases. Operating income was negatively impacted due to higher labor costs as it relates to the tight labor market and escalating real-estate costs for a newly leased facility. We remain committed to our current asset light model and continue to pursue opportunities to accelerate our growth.

Regarding our outlook for the future:

We are excited about this year as the operating model continues to be refined. We do expect a good freight environment for the first half of the year with some moderation in the second half. Cost pressures will be meaningful in wages, equipment and over the road repairs for the year but the market should allow us to pass the majority of those increases along in the form of rate increases. The first few weeks of the year were tough from a truck working percentage as many of our driving teammates were impacted with the virus after the holidays, but the fleet working percentage has improved greatly and we are especially pleased with where the team count is today. The Dedicated improvement plan continues to make progress, and we are confident that we will continue to improve the margins to high single digits in 2022. Net indebtedness is already dropping in January, and we feel we will generate free cash in 2022 providing further opportunities to deploy the cash for growth and or share repurchases.

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