North America
Canada
United States
Industrials
Trucking

Industry
U.S. Transportation

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Recommendation Change

Where we have conviction, and where we don't

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On the back of 4Q results we have increased conviction in our positive stance on **Knight Transportation** (KNX), **XPO Logistics** (XPO) and **CSX Corp** (CSX). We remain comfortable with our sole-Sell ratings on **Old Dominion** (ODFL) and **Canadian National** (CNI), while our Buy on **UPS** was wrong and we are using this report to downgrade our rating to Hold and lower our price target to $115. Our company-specific thoughts are below, and see details within this note for our industry takeaways post results:

- **KNX - best earnings revision potential across our coverage universe:** For KNX we see potential for EPS to approach $3.60 per share in 2019, which is 30% above current consensus. This is based on 15% operating margin on 2019e revenue ex. fuel, which is 200bps better than what KNX-SWFT achieved on a consolidated basis in 4Q'17- despite being in the early innings of integration and cyclical recovery. Our bullishness is supported by highly accommodative cyclical and non-cyclical factors, such as high-single-digit growth in U.S. truck tonnage and contract rates, double-digit improvements in yield, and plenty of low-hanging cost opportunity at Swift. See Figure 1 within this note for our walk to mid-teens operating margin.

- **XPO- we see potential for very strong 2019 free cash flow:** Our long-held positive stance on XPO has been predicted on accelerating revenue and free cash flow growth. Indeed, organic growth accelerated to +10.4% in 4Q, and free cash flow has tripled in two years- from $211M in 2016 to expected $625M this year. In the context of this free cash trajectory, an exact tripling of equity value in a little over a year is highly explainable, if not conservative, as it implies little in the way of multiple expansion (i.e. equity value has increased almost exactly in-line with free cash flow). Our 2019 free cash forecast of $750M implies 20% yoy growth, with upside to 35% growth (to $835M) if current organic growth rates are sustainable- which we think is a realistic outcome given macro backdrop, e-commerce exposure, and the company's growth investments. From this standpoint we see a relatively quick trajectory to our $133 price target, which represents 40% add'l upside. See Figure 2 within this note for our 2019 FCF walk for XPO.

- **UPS - Downgrading to Hold (lowering PT to $115):** Following 4Q capex guidance- which was worse than even the most bearish expectations-

Key Changes

Company	Target Price	Rating
UPS.N	135.00 to 115.00	Buy to Hold
HTLD.OQ	22.00 to 20.00	-
LSTR.OQ	95.00 to 105.00	-
YRCW.OQ	21.00 to 13.00	-
WERN.OQ	42.00 to 43.00	-
GWR.N	88.00 to 84.00	-

Source: Deutsche Bank

Top picks

Knight-Swift (KNX.N),USD48.30	Buy
XPO Logistics (XPO.N),USD93.99	Buy
FedEx Corporation (FDX.N),USD243.30	Buy

Source: Deutsche Bank

Sector valuation and risks

We utilize P/E to value transportation stocks, with our target multiple assumptions heavily supported by our discount cash flow models and sum of the parts (where applicable). Risks to the group include U.S. recession, weak industrial production, pricing, and management execution.