The Mullen Group Limited
Second Quarter 2023 Earnings
Conference Call Transcript

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Speakers:

Murray K. Mullen
Chair, Chief Executive Officer, President

Carson Urlacher
Senior Accounting Officer

Richard Maloney
Senior Operating Officer

Operator:
Welcome to the Mullen Group Limited Second Quarter Earnings Conference Call and Webcast.

As a reminder, all participants are in listen-only mode and the conference is being recorded. (Operator Instructions)

I would now like to turn the conference over to Murray K. Mullen, Chair, Senior Executive Officer and President. Please go ahead.

Murray Mullen:
Thank you and welcome all to Mullen Group's quarterly conference call. We will be providing shareholders and interested investors with an overview of our second quarter financial results. In addition, we will discuss the main drivers impacting our operating performance, our expectations for the year, and close with a Q&A session.

But before I commence today's review, I'll remind everyone that our presentation contains forward-looking statements that are based on current expectations and are subject to a number of risks and uncertainties, and as such, actual results may differ materially. Further information identifying the risks, uncertainties and assumptions can be found in the disclosure documents, which are filed on SEDAR and at www.mullen-group.com.

This morning, I'm calling in from our brand new state-of-the-art facility in Kamloops, BC. It's a 36,000 square foot cross-dock, it's got 40 doors and warehouse capabilities, including we can service our ambient capabilities for our customers. The terminal is now occupied by Apps Cargo, it's a leader in the west coast logistics space, it provides—and this provides Apps with a great facility, ensuring they can service the entire interior BC from a central location, and as our shareholders know, LTL is one of the core investments identified by our organization, and this facility is just another great example of an investment by our Company and how we ensure our LTL businesses are positioned for the future.

Now back in Okotoks, the corporate office, the other members of the Senior Executive Team are joined on the line. I have Richard Maloney, Senior Operating Officer, Joanna Scott, Senior Corporate Officer, and Carson Urlacher, who is our Senior Accounting Officer and he's the primary architect of the interim report, and he'll be reporting on analysis and discussion on our financial performance.

Let's start this morning's call with a review of our Q2 2023 financial operating performance, and in this section, I really will address two topics. The first is how we—how did we do, and the second is how did we do it? From my perspective, I have to say Q2 was another very good quarter for our organization. We managed to mitigate most of the collateral damage from the change in the economy, and from that perspective, what I really mean is we saw consumers alter their spending patterns away from buying goods doing things, like travel, personal services, going out to restaurants, concerts, etc., but the consumer, I think, only tells half the story here.

Business has also changed. Retailers, manufacturers, shippers, they finally realized late last year that they miscalculated their supply chain requirements and begin to right-size inventory levels, after ordering way too much in ’21-‘22. This combination, changing consumer’s habits and business rightsizing, led to lower freight volumes and more competitive pricing in 2023,

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which is the exact opposite of last year. So, in other words, we went from a freight boom in 2022 to a freight recession in 2023, all within a few quarters.

Now, the other thing to remember about our results, you've got to—the last year was punctuated by high fuel prices that were passed onto customers via fuel surcharges. Now this year, there's been a moderation in fuel prices, and as a result, fuel revenues are down $20.8 million year-over-year just in the second quarter. This alone represents the majority of the consolidated revenue decline of $27.2 million.

Now, despite all of these changes in the market, we still managed to generate some pretty nice results. Basically what the numbers tell us is that we had a pretty good quarter, which as I mentioned is even more compelling when comparing to the boom in 2022, a year of supply chain disruption, off-the-chart freight demand, and pricing surcharges implemented due to the surge in demand. So, I would say, yes, revenues were down in the quarter, they're down about 5% year-over-year. But perhaps a better way to look at our performance is to compare not to the boom year of 2022, but compare to our five-year average or, as I like to say, the period before 2022. In fact, excluding last year's results and looking at our five-year historical average, you'll see that we exceeded prior year periods by a mile. So, when I say I'm pleased with our performance in Q2, in fact for the first six months of 2023, you will know what I am referring to, and that's the long term.

Most shareholders have come to expect that we will grow this Company in a prudent and thoughtful manner. We always think about tomorrow. We never chase deals, particularly at the top of the market like last year. We have a long term game plan and we stick to it.

Now, let me just give the next couple of comments here about how we did it. Firstly and most importantly, I'd say it has to do with our diversified portfolio of service offerings and our brand name business units that are involved in multiple different verticals within the North American economy. This diversity is all part of our risk management strategy. It helps in times like last quarter, where we saw some pretty stiff revenue and price declines in the big consumer markets like metropolitan GTA in Ontario or in Vancouver, and in the United States where the freight market was hit particularly hard.

There was, however, we saw some pockets of strong demand such as transload services, which is where our Kleysen Group shines, and from our vantage point, western—the western Canadian market was the best performing market, with energy and mining industries continuing to provide a solid base for companies like our—that are in our oilfield services business, or at Canadian Dewatering, which everyone will know is a leader in water management and logistical support services, and at the Bandstra Group, which is by the way a key supplier to BC's mining industry. In other words, diversification matters in times like this.

Now, we also did a couple of nice tuck-in acquisitions where we saw a good fit, the price was right, and where there were lots of synergies to be had. In fact, acquisitions added $22.6 million to our consolidated revenues and that mitigated the loss of business in—most of the loss of business in fuel surcharge revenue.

In terms of operating profitability, often referred to as OIBDA by the accounting profession, we adjusted and we did a great job of managing operating costs, especially generating a very healthy $83.4 million in the quarter, and that represents a margin about 16.9%. It's down about 1%, but I think we can make this up once we get these new acquisitions fully integrated to our

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network, which I expect to occur by year end 2023, and that will set us up, I think pretty good for 2024.

For more on the quarter, I'm going to turn it over to Carson. Carson, it's your turn, you're up, bud.

Carson Urlacher:
All right. Well, thank you Murray, and welcome everyone. Today I'll provide the highlights from our second quarter, the details of which are fully explained in our second quarter interim report.

Consolidated revenues declined by $27.2 million to just shy of $500 million and was due to the net impact of four factors. First, revenue excluding acquisitions and fuel surcharge declined by approximately $25.5 million due to lower freight volumes, particularly in Eastern Canada, and from the more normalized pricing environment compared to the elevated levels of last year. Second, fuel surcharge revenue declined by $20.8 million as diesel fuel prices decreased by 35% year-over-year. Thirdly, we disposed of our hydrovac assets and business in 2022, which contributed to a $3.5 million reduction in revenue; and lastly, somewhat offsetting these revenue declines was $22.6 million of incremental revenue from acquisitions.

OIBDA decreased by $10.5 million to $83.4 million, largely due to a decline in the LTL segment. OIBDA in our other three segments remained relatively flat year-over-year. Operating margin decreased by 1.1% to 16.9%.

Now let's take a closer look at how we performed by segment.

Starting with our largest segment, revenues in the LTL segment were down $17.3 million to $193.4 million due to lower fuel surcharge revenue, lower freight volumes in Eastern Canada, and from a more normalized pricing environment. As a result, OIBDA was down $7.9 million to $34.5 million. Operating margin decreased by 2.3% to 17.8%, primarily due to lower margins experienced by B&R, our most recent acquisition. The financial results of B&R contributed to almost a one full percentage point decline in segment operating margins.

Our second largest segment is our L&W segment. Revenues in the L&W segment were down $13.8 million to $142.9 million due to the continuation of the inventory rebalancing cycle and softer freight demand. Other factors contributing to the decrease in revenue consisted of lower fuel surcharge revenue and a reduction in revenue from the sale of our hydrovac business. OIBDA remained relatively flat year-over-year at $30 million while operating margins improved by 1.5% to 21%. Operating margins improved due to the strong results at Kleysen Group and from the ability of us to use owner-operators and subcontractors more efficiently.

Moving to the S&I segment, revenues were up by $6.8 million to $107.3 million on $13.3 million of incremental revenue from acquisitions, which was somewhat offset by lower demand for some of our services due to extreme wildfires, curtailing activity levels, and from the timing of certain turnaround and maintenance work activity. Lower fuel surcharge revenue and the sale of our hydrovac assets also contributed to a reduction in revenue. OIBDA in absolute dollar terms was relatively flat year-over-year at $20.6 million. Operating margins declined slightly to 19.2% due to higher S&A costs as a percentage of revenue.

In our non-asset-based U.S. 3PL segment, revenues declined to $50.8 million due to lower freight demand in the U.S. for full truckload shipments. OIBDA decreased to $0.9 million, which

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was mainly due to higher S&A costs as we added IT staff to continue the development of our proprietary software known as SilverExpress. Operating margins declined to 1.8% on higher S&A costs. Operating margin on a net revenue basis was 18.8% compared to 43.1% in 2022.

Net income decreased by $6.2 million to $36.5 million or $0.41 per common share. This decrease was mainly attributable to lower OIBDA and from a reduction in earnings from equity investments, which was somewhat offset by lower income tax expense and a positive variance in net foreign exchange.

The number of common shares outstanding decreased in the quarter as we repurchased and canceled approximately 2.1 million common shares for $31.5 million or an average price of $15.11.

We continue to generate strong cash flows in excess of our operating needs as net cash from operating activities in the second quarter was $88 million, an 80% increase compared to $48.8 million in 2022. This increase was mainly due to the changes in non-cash working capital items.

Our balance sheet remains very strong. Our debt to operating cash flow covenant under our private debt agreement is at 1.95 to 1. We have a total of $250 million of bank credit facilities available to us, of which we had $115.7 million drawn at the end of the second quarter.

With that, Murray, I will pass the conference back to you.

Murray Mullen:
Thanks Carson, and as we get close to wrapping up this morning's official commentary, I'll now provide some thoughts on how we're looking at the market, the economy and our business, and in this quarter, I'm going to keep it quite simple because our outlook really hasn't changed from Q1 presentation back on April 27, 2023. I invite any interested listeners to check out the transcript of my comments last quarter, and you'll see really the outlook really hasn't changed much.

We still view the macro picture as stable, but risks become more elevated each hike in interest rate. We continually ask ourselves when will the consumer break, but I can tell you from what we've seen thus far in 2023, they haven't done so yet. As such, it's reasonable to assume the economy will continue to grow, perhaps slowly but it still looks like there's some growth. Under this scenario, freight demand will remain under pressure and probably until manufacturers, shippers and retailers begin to restock inventories.

As I commented earlier about what happened last quarter, it was a lot of the freight—loss of freight demand was not end consumer demand, it was really about businesses adjusting inventories. Well, I can tell you the warehouses are emptying pretty fast these days, so eventually they're going to have to restock inventories if the consumer is going to keep spending as they are. This suggests that our LTL and L&W segments will continue to perform, I think at levels consistent with this past quarter, and truthfully I think, our number one challenge will be in finding productivity gains to alleviate cost pressures that have built up over the last couple of years, so we're 100% focused on that, both at the corporate offices and in our business units.

The U.S. 3PL segment, and what I'm referring to here is Haulistic, they're going to continue to be impacted by—the most by the freight recession. I think the good news is that this is a non-asset based business, and the senior team at Haulistic, they focus simply on one thing - that's

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managing the spread, and that's the difference between what the market offers and the price the subcontractors are willing to work for, and thus far there is more capacity than there is freight, which means the contractors are very price competitive. However, our margin will suffer a little bit because we are focused on the long run, and we've added new IT talent to the team to help build out SilverExpress 2.0, and that increases your S&A expenses in the short-term. This is so unlike our competitors that are downsizing, and that's really for one reason, we believe the future of the 3PL business lies in the technology offering.

Turning now to mining and energy, we see these as growth areas, which is why we are optimistic that our S&I segment will continue to exceed last year's performance, at least that's our expectation today.

On the corporate front, well, we're going to continue to balance the balance sheet, as Carson says, with a high degree of respect that the market could be vulnerable to a slowdown. If this were to occur, having a strong balance sheet would be very, very strategic. We will, however, continue to pursue acquisitions that meet our three criteria. That is fit, the right price, and we must find synergies. We have a great book of business, an excellent team throughout, and we're well positioned to be very opportunistic, because I can tell you from the calls we're getting, there's—some people are getting stretched.

Thank you. I'll now turn the call over to the Operator and we'll go straight to the Q&A session.

Operator
Thank you. We will now begin the question and answer session. (Operator Instructions)

Our first question comes from Konark Gupta of Scotiabank. Please go ahead.

Konark Gupta:
Thanks Operator. Good morning Murray and everyone.

Murray Mullen:
Good morning.

Konark Gupta:
Good morning. Good quarter for sure.

What I wanted to understand was, you know, the L&W segment had a pretty good margin, and as Carson pointed out, it's the Kleysen Group that had a pretty good performance in the quarter, which is not surprising. The transport business seems to be good. I'm just wondering how sustainable is this margin performance at Kleysen or the entire segment? Do you see any signs of, I don't know, maybe the cost or pricing pressure, or tailwinds on either side, and how should we think about this segment in the next 6 to 12 months?

Murray Mullen:
Yes, it looks like that segment, we've got some competitive advantage in that. Number one is the Kleysen Group, as we talked about - they've got a very strong book of business involved in transload, and those are assets that just are not subject to the same market pressures that—because there's not a lot of competition, very, very few strategic transload operations, so we've got it. We're not subject to the same pricing pressures that you might have in the general consumer general business, so that's a—you know, that's a good sign for us.

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The other one is the Bandstra Group is included in that, so our two biggest businesses there are Bandstra, which is tied to the mining business in British Columbia, which is going through a bit of a growth spurt right now because if you're going to move towards—if you're going to look at energy, you have to think mining and energy are correlated because if you're going to move towards cleaner forms of energy, well, you have to find the minerals and the metals, which is through mining. It's not through just asking for it, you got to go find it, so mining has got a bit of —has got some good tailwind with it for the next bit, and Bandstra very well positioned in British Columbia, so that was a very good acquisition. Those two are doing very well.

The rest of our businesses, Konark, we kind of manage the spread. We have a lot of owner-operators in there, use a lot of subcontractors, so our business units just manage that spread. You've heard me talk about that. If you have all company trucks and there's price pressure, well, you're going to take it on the chin; but right now, it's the one that owns the truck that's taking it on the chin because there's too much supply for how much demand there is, so—but we can still maintain margins.

Revenues are going to be down a little bit because of fuel. That's not really load count, that's just a—that's a flow-through, so all in all, not too bad from that. I think it's going to be pretty stable on there, at least that's my projection for today.

Konark Gupta:
That's good colour, Murray. Thanks so much.

Then just a follow-up on the trucking market in general. Your segments kind of give us an indication as to how the Canadian market is a little bit different than the U.S. market clearly, and it seems like the U.S. market went up a little bit higher last year and it's coming down from that cliff, perhaps. What I wanted to understand on the U.S. side was there's a situation right now in that market where there's a very large player - Yellow, is going through a major labour and business uncertainty at this point, so has there been any change that you have noticed in your U.S. 3PL segment because of the Yellow situation at this point, and what are your thoughts on that whole situation?

Murray Mullen:
Yes, so you're right - that's a headline news item, and Yellow has—you know, they're a big company but they've always been on the edge of not doing well, and so there's reasons, I don't know what they are, but they're having some real challenges right now because of the market and because of their labour issue.

What we are seeing right now is they're having some—customers are shifting and they're shifting some of that business. Now, that is not—if I'm Yellow, that's not a very good situation. That's not new demand, that's just a shift in demand, so there will be some winners and some losers of that. Now, we don't do any business with Yellow in our network, in our LTL network. We do business with some of the other LTL carriers and we provide—like EstesGroup, we deliver their freight in Canada for them, and Estes, their load count is going up even though the market is not going up, and that's most likely a shift of freight from Yellow. So there's a shift going on, and that's a specific market issue there.

In Canada, our biggest issue that we've got up here has probably got to deal with the disruptions in the ports and stuff like that - that's backing up inventories coming in. There's too

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many ships waiting to come in, and I can tell you that the side effect of that is our warehouses are emptying out pretty fast. That could resolve the Canadian freight recession awfully quickly from my perspective, because our inventory levels are being drawn down pretty fast. But end consumer demand has not changed dramatically, and the consumer still seems to be pretty good. That's what we're seeing.

Konark Gupta:
Great, that's very helpful. Thanks for the colour. Appreciate it.

Murray Mullen:
You bet.

Operator:
Our next question comes from Kevin Chiang of CIBC. Please go ahead.

Kevin Chiang:
Thanks for taking my question, and I'll echo Konark's comments - a good second quarter here.

Maybe if I extend out the questions related to your comments around Yellow, obviously LTL has been a focus area for you here in Canada and you do a little bit of it through your brokerage arm in the U.S. on the 3PL side.

Murray Mullen:
Yes.

Kevin Chiang:
Do you think with the potential bankruptcy of Yellow, that that opens up the door for you potentially taking a step into the U.S. LTL market? Is that a market you'd be interested in? You know, it's much more consolidated, much more rational. You've had great success here in Canada in consolidating the market north of the border. Does this accelerate maybe a timeline to enter into the U.S., or is that something that doesn't interest you?

Murray Mullen:
No. If you're going to get into the LTL business, Kevin, you're going to have to go big, you can't fart around. I don't—that would be such a big step out, so I don't—we won't enter that freight. That doesn't make any sense to us.

Where we are going to move freight in LTL is through our Haulistic group. We don't move the freight, we help customers drive the best value - that's what our technology is about, because the little customer is going to get squeezed here, and Haulistic is just a—they're a bulk buyer and they manage the spread on that, so Haulistic will benefit. They're being awfully careful about using Yellow right now as a contractor, and—but Kevin, I'll be honest with you, that business will be gobbled up in a heartbeat.

Kevin Chiang:
Right, right.

Murray Mullen:
Yes, it won't take—it won't be as disruptive as what people think, I don't think. That's my personal opinion. Those other—those facilities, if they do go into it, those facilities will be

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gobbled up by somebody else and it will be disruptive for a few quarters, but even as big as they are, it's not huge compared to the total size of the market.

Kevin Chiang:
No, that's great colour there.

The one thing I did notice, and you mentioned this in your opening remarks how we're in a freight recession, and I appreciate Canada might be a little bit different than the U.S. But one thing that did stand out to me is, if I look at your LTL margins in 2019, I appreciate there's M&A in here and fuel surcharges will kind of whipsaw your reported margin, but if my numbers are correct, it looks like you did something like 15.5%, just a tick over 15.5% in margins in 2019.

If I look at the last three quarters here in LTL, you're kind of in the 16.5% to 17% range despite the fact that we're in a freight recession. How do you think about your margins in LTL here through the cycle? Do you think you're kind of at a—it seems like you're at a higher high and maybe—or a higher high and a higher low here through the cycle. Just wondering if you'd agree with that, that you've kind of taken a step function, maybe 200 basis point step function increase in your overall margins through the cycle.

Murray Mullen:
Yes, we're going to increase margin in LTL over time. You've got to remember, I think, really our investments in LTL have really only been over maybe the last 10 years or something like that, so I think we're in the early, early stages of building out what you need in LTL, which is you need lane density and critical mass, and you've got to have the right business units. I think, we've done a really good job of getting some great businesses in our organization, and we're just—I think we're in the early stages of finding our stride and doing that.

For example, I'm out in Kelowna right—in Kamloops right now, and in a brand-new LTL facility. That's the future, and we are building for the future. We don't build facilities to make no margin. We're very optimistic that we'll build the lane density and get the critical mass that's required, and our business units, they're running a good job and so margin will improve in LTL over time.

We will continue to do tuck-in acquisitions, which when you do those tuck-in acquisitions, the smaller little one, there's a consolidation trend going on, guaranteed, is that we'll be able to build the density within our group, but number two is you get rid of an undisciplined competitor, and when I say undisciplined, I mean, they're very, very price competitive but in this new day and age, you've got to have the technology platform to be able to integrate in with the big shippers, and whether that big shipper is another carrier in the U.S., like Estes - we're totally synergized between the companies and the data flow and then to their customers, so little companies just cannot get that, so they're boxed out.

B&R is a perfect example of that. They're in the LTL business. They've been—you know, they haul a lot of LTL freight in Northern Alberta and they don't make any money at it. I guarantee you within our network; we will make money with that.

So yes, we have a long-term game plan in LTL that's really good strategic facilities and build lane density and critical mass, and I think we're in the early stages. I mean, if you give me 10 years, another 10 years in the LTL business, we're going to be a lot—it's not going to be 16%, 17% margins, I can tell you that.

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Kevin Chiang:
That's helpful.

Maybe just one more for me, just because you're in BC there, and with the opening of a new Apps facility, just maybe how you're looking at the BC port strike and maybe how Apps is managing it, given they have an intermodal agreement with CN, and maybe how quickly you think you can recover from this disruption here.

Murray Mullen:
Well, thus far I think the biggest disruption, Kev, that I've seen is there's not any inbound freight coming into our facilities. That's why I say to you, most of the freight that we're hauling now is emptying out the warehouses, so nothing—the problem we can have with the port issue—and this is a regional issue, this is not like COVID which was a worldwide issue. This is a regional spat and it's going to impact Western Canada the most in that, including exports. There's bottlenecks, I'm sure that will be resolved, but right now what it is, there's lots of inventory and there was a lots of inventory in the system. Well, guess what? In Western Canada, that's cleaned out now because there's nothing coming in. It's all sitting on the ships, and I think they can only offload maybe one, maybe two at best ships a day.

Kevin Chiang:
Okay, that’s good colour.

Murray Mullen:
You know, you've got quite a few ships backed up there right now, so this could take—from the flow of traffic, it could take quarters, not weeks once it gets resolved and the port workers go back and become productive again.

The worst case scenario is they go back to work, they're mad and they're not productive, and things just get extended out, and that's just going to increase the cost and hurt a whole bunch of people down the line.

Kevin Chiang:
No, that’s—that makes sense, that’s great colour. Thanks for taking my questions, Murray and team.

Murray Mullen:
You’ve got it. Thanks, Kev. Appreciate it, bye.

Operator:
Our next question comes from David Ocampo of Cormark Securities. Please go ahead.

David Ocampo:
Thanks for taking my questions, Murray and team.

I guess the first one I have for you guys, I mean, when we look at the seasonality of your quarters, Q3 is typically stronger than Q2, and just based on the commentary that you guys made about inventory levels normalizing and probably the progress that you've seen in July, should we expect those normal seasonal patterns to persist this year?

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Murray Mullen:
It's complicated to—my instincts say it's going to normalize, but there's always things that can happen in the market. But let me tell you, I drove out to Kamloops last night, I don't want anybody telling me there's no freight moving. There's a lot of freight moving on the highways, so I still think the consumer is doing well. I think so long as job—you know, that we don't have a deterioration in job losses, I think this market is finding a new equilibrium. I think that we're going to be back in balance.

It's going to be a more competitive market than '23—than '22. Okay, drive your synergy, be in the right business model, be in the right lanes and I think you'll do just fine, and I think we're in pretty good shape from that perspective, the way that we built our business and that diversification model.

The other is we're going to be very, very opportunistic. Some parts of this supply chain are getting whipsawed here, and those people will get into trouble and we will take the long term view and say, okay, are those good long term returns on investment, and we'll look at putting capital to work in those markets.

David Ocampo:
That's helpful colour. Maybe I could ask the question another way. I mean, if I take a look at your H1 performance, you guys did $160 million of EBITDA, kind of reached that $300 million target that you guys have been alluding to. It kind of suggests that H2 would be down 12%, so are you looking at that $300 million number is more low-hanging fruit, then?

Murray Mullen:
Well, as I said in my commentary, I mean, in the press release—well, if it keeps going the way it's going, I guess my 300 might be a little low. We always said, look, we don't know if it's going to be 300. What we're running our business on and our balance sheet is if it's going to be 300. Thus far, we're ahead of that curve and so we feel pretty good and pretty positive. We're running it as if it might happen, but that consumer is—keeps defying the odds and the economy keeps defying, so I might have been too cautious at the 300. Thus far, I'm wrong. I'm wrong—you know, if you took Q1 times two, that's 320, not 300 million, and so it's—we've got a great business.

We just were running it as if it was going to go down to 300, so what we did is we pivoted to focus on cost, and we didn't—and we watched the balance sheet. That clearly was the right move, which is why we maintained the way we did. As we're looking at now, now we're saying, okay, it appears that the market is adjusting to 5% interest rate. I don't know how the consumer is doing it, but they're doing it, and because business is—you know, you see from our numbers, it's still pretty robust. Take out fuel, our revenues weren't down that much.

David Ocampo:
That's helpful colour. I'll hop back in the queue. Thanks a lot, Murray.

Murray Mullen:
All right. Carson, you got anything to add to that?

Carson Urlacher:
No, no. I think that was spot on, Murray. No, nothing to add.

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Operator:
Our next question comes from Cameron Doerksen of National Bank. Please go ahead.

Cameron Doerksen:
Thanks, good morning.

I guess in the MD&A, you highlighted in the specialized and industrial services segment that there was maybe some impact from the Alberta wildfires. I don't know, there's probably no way to quantify that, but just maybe you could describe what impact that had, and is there any kind of lingering impact from that that might affect Q3?

Murray Mullen:
I don't think so, Cameron, to be honest with you. I think there was—you know, there's always some type of an event or something that slows things down for a little bit, but those were for, what, a few weeks, maybe a month where it was disrupted in certain pockets, but it wasn't—it just slowed things down a little bit. All you do when you slow things down is it just backs it up and puts it into the future quarters, so I think the market is fully recovered from that now.

Some of the communities have not, they're still struggling with some of the residual effects of that, but I think business—I didn't see any real damage to infrastructure, and it certainly wasn't to our infrastructure, so I don't—I think it was kind of a situation that happened just in that quarter. I think it won't impact us this quarter.

Cameron Doerksen:
Okay, that's great.

Murray Mullen:
Now this quarter—this quarter, you're going to be impacted by the strike on the west coast port because you can't get exports out either, so we're having some of our transload business be impacted by that because you can't ship the product that's going out. We put it on to rail, it goes to rail on a ship and out to Asia or other parts of the world, and so that's being disrupted, so there's always something and I'm just hopeful that some common sense prevails here and the workers there understand, is that you're—you know, don't be too greedy here because you're going to impact a lot of other people and a lot of other businesses if you get—we need them back to work, and hopefully they will.

Cameron Doerksen:
Yes, certainly it sounds like it's moving in that direction, so that's good news.

Maybe my second question is just around M&A - I mean, you commented a little bit on it in your prepared remarks, but maybe you can just talk about the outlook. You kind of indicated there's quite a few businesses giving you a call. Where are the opportunities now, what's most interesting? Are valuations coming down further, given maybe some of the disruptions for other businesses in the freight space?

Murray Mullen:
Yes, so let's look at it from each of the different perspectives, each of the segments. In our LTL business, we'll continue to do tuck-in acquisitions like we did with B&R. We've got some other ones that we're looking at that will add density and lane capacity and get rid of an undisciplined competitor in some of our other business units, so we've got some of those files and we're

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working through those right now. That's my preferred way of doing, just layer them in. I don't increase cost, I get business, and I get rid of costs and I drive margin, and I get rid of—you know, I just get rid of the undisciplined competitor, so we'll continue to do that in L&W.

Probably no big home runners in that one unless somebody gets a—a really good opportunity comes up, and then we'll make a big step out in that to expand our coverage across Canada. But we've got a great footprint from the greater—GTA all the way out to the west coast, so we'll continue to add in there.

In L&W, we'll be opportunistic. I really like transload assets - if we find them, I'm buying them because that's your path to the future, really good business. U.S. 3PL, we're not going to buy anybody in that. We're going to focus 100% on building up the technology because, as I said, that's your competitive advantage of the future, is in the U.S. 3PL, it's all in the technology platform. That's why I kind of referred to U.S. 3PL, Haulistic as our technology group, not our logistics group, because if you don't have the technology, you're not doing the logistics, so we're focused 100% on that, not on doing acquisition. Acquisitions will come after we get SilverExpress 2.0.

Then in S&I, those are your best opportunities right now because it's still—you know, energy business is still not reflected by investors as being a good business, and those are your best opportunities. You get good cash flow and you don't have to pay a lot for it. The market is not pricing those assets as if they're generating cash or that they will generate cash, I guess, which is why we bought B&R. I mean, you're talking at maybe two to three times EBITDA, not 6 or 8 or 10.

Cameron Doerksen:
Right, okay. Well, that's very good.

Murray Mullen:
Yes, each one of them has a different—there's a different denominator that works with them. In the freight business, general trucking business, it's difficult to peg that number right now because I can't tell you when does that market—when does pricing leverage come back in that. If you don't get pricing leverage, you're just trucking, you're just generating revenue, you're not generating bottom line, and that business is ultra-competitive, which is why we're not in that business a whole bunch, Cameron. We're in different verticals where it's not quite as competitive. I think that's the power of our business model. We've built it up over 30, 40 years and it's not by chance. That's why the diversification is pretty good.

Cameron Doerksen:
Yes, absolutely. No, it certainly shows in your results, outperforming pretty much all other trucking companies, so appreciate the colour. Thanks very much.

Murray Mullen:
Thanks Cameron. Bye bye.

Operator:
Our next question comes from Walter Spracklin of RBC Capital Markets. Please go ahead.

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Walter Spracklin:
Thanks very much. Hi Murray and team.

I want to kind of simplify your outlook as it was provided when you first gave your guidance to what's changed so far, and I guess when you're looking at your outlook, you're probably looking at three factors: the inventory de-stocking trend, the consumer trend toward more services versus goods, and a potential recession is kind of drivers of your lower $300 million target. Now that we're trending more toward a 320, as you mentioned, what would you say would be the biggest change of those three buckets? Is it that you built in a recession that you're seeing—you're not seeing manifest? Is it consumer patterns shifting back to goods a little quicker, or inventory de-stock? I know you mentioned that you're seeing the warehouses start to come down. Is that the factor that is the biggest differentiator versus the assumptions you had at the beginning of the year? Just curious as to what's (inaudible 0:43:47.1).

Murray Mullen:
Yes. I think Walter, if we go back and we look at it, and we said look, we thought that the biggest factor that was going to change in 2023 was in pricing because if you go back in, we said look, we're still going to do $2 billion in revenue. Well, guess what? We're on target for $2 billion of revenue because that's what we did last year, so it's not the revenue, it's the competitiveness that we thought and some of the surge pricing that was happening when you had this massive—these big bottlenecks that were happening, and customers were, just get it done. Well, that's over. We're now back to a competitive marketplace, and that's where we thought the biggest challenge would come from, is from that side, and for the most part we were right on, on that. It's in the pricing side that you're getting hurt.

I didn't know what was going to happen with fuel, but we projected it was going to be at best flat, but the biggest—that's the biggest surprise, is fuel is down.

The economy has held in pretty good. The consumers - God, they're resilient, but I'll tell you the biggest thing is business readjusting to the inventory levels. They totally screwed up the last cycle during COVID. I think they're overshooting again but this time to the downside, and that might get—you might find that they're going to have to go back in. Retailers are going to have to go in and start restocking the shelves pretty quick because the consumers—we're still moving freight, and it's not coming in as fast, as fast as it's going out.

Walter Spracklin:
So just to clarify, you thought pricing would come down and it just hasn't come down as much, which is why we're…

Murray Mullen:
No, pricing has come down, you can see that on our LTL side, you can see that in general trucking. Where we did fine is we said our S&I was going to do fine, and our L&W did fine with our transload and that, so—but you can see in our LTL side, it came down.

Walter Spracklin:
I'm trying to figure out what made your numbers go up? What was the difference between what you were assuming at…

Murray Mullen:
S&I.

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Walter Spracklin:
Okay, okay.

Murray Mullen:
S&I and L&W, yes. Our mining and energy business is doing better than what we had originally thought.

Walter Spracklin:
Okay.

Murray Mullen:
We're overachieving on that side.

Walter Spracklin:
So really, when you look at LTL, then, you haven't seen—the way it's playing out is as you expected, and really the upside here is if that inventory de-stocking trend, as you flagged in your opening remarks, if that continues and if even so, as you just mentioned, if they overshot on the other side, then we could see perhaps in the fourth quarter or early 2024 a nice rebound…

Murray Mullen:
A normalization.

Walter Spracklin:
A normalization versus what you've been assuming in that $300 million? Okay.

Murray Mullen:
I think that is a reasonable assumption. So long as the consumer stays healthy, and we know that what keeps the consumer healthy is a job, if they have a job, they're still going to consume. What are they going to consume on? I don't know, but it's all in the job numbers, and thus far it's pretty healthy, it's in balance right now, Walter. I think that's what you're seeing in our numbers, is pretty healthy balance, and as I say, that's why I say compared to our five-year average, not just to the surge of last year, which was a one-time event, take a look at it and you're seeing, man, you're outperforming your historical numbers pretty nicely there, Mullen Group, so.

Walter Spracklin:
Absolutely. No, I appreciate the time as always, Murray. Thank you.

Murray Mullen:
Thanks Walt. Been good chatting.

Operator:
(Operator Instructions)

Our next question comes from Tim James of TD Securities. Please go ahead.

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Tim James:
Thanks. Good morning everyone, and congratulations on a good quarter here.

Just wondering if I could return to—I guess I'm thinking about M&A when I ask this question, but are you seeing, Murray, any signs in Canada of competitors that are struggling? I mean, you mentioned some opportunities, that you've got one that's being disruptive in the market, but are you seeing any players in the industry that are struggling, and maybe you will get opportunities from that eventually?

Murray Mullen:
Yes. If you overextended yourself in '21, '22 and thought that that was the sustainable market, you overextended, you're now in trouble. Those are the ones that will pay a hefty price in this market, because the market has now normalized, and if you thought last year was going to be the new trend, you're probably in a lot of trouble, so—yes. Does that mean the whole industry is in trouble? Not a chance, but it's a bifurcated market. If you position yourself well, you can ride through it. If you didn't, the banks—you know, it costs a lot more money to borrow today, and you're getting squeezed.

What we look at is, we don't want business that just generates revenue, we want business that layers into our network so we can drive margin. That's our number one target, is companies that will fit into our network with our teams, that will drive our bottom line, not just our revenue. We don't chase revenue, Tim - that's a fool's game. We chase margin.

Tim James:
Okay, that's helpful.

My second question, looking to the U.S. 3PL business and the work you're doing there investing in SilverExpress, is there kind of a timeframe that you have in mind with those investments when your margin, I don't want to say matures but kind of normalizes, or maybe those investments start to slow down and you get what again would be more of a normalized level of profit margin in that business?

Murray Mullen:
Well, if you're our senior team at Haulistic, Pat Malone and his team down there, they hear from me, I want to normalize next quarter; however, they say, well Murray, we're still fighting a few headwinds here, so—but they're working on the long term game plan, Tim, not the next quarter, and I can't—when you think of technology, you can't think a quarter, you think of the long game. I can just tell you I am very pleased with the initiatives that they are undertaking.

Their business was not down as much as the U.S. freight business, which you look at all of the other providers that are going to be coming out, I bet you any money they're down 15% to 20%. Our Haulistic Group is not down 15% to 20% because they added new station agents, so we are gaining market share but we're building for the future, so we can gain more market share and be one of the number one players in the U.S. 3PL business, and so I encourage them to keep driving hard. As I tell them, you've got to beat the competition to the puck, and we've got the team down there that can do it, so I'm pretty pleased there.

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Tim James:
Great.

Murray Mullen:
But I don't think of it in terms of a quarter. I think of it in terms of—them, that's the long term. That's our long term game plan down in the U.S. market, is to build out critical mass down there.

Tim James:
Absolutely, okay.

If I could just sneak in one last one, Murray, I'd be curious to get your thoughts today on the inflation environment. Clearly we're seeing headline inflation slowing, and I'm not thinking so much about trucking rates and that, because we know what's going on there. I'm thinking about other parts, maybe the cost side of your business, whether it's labour, technology, equipment, are you seeing easing inflation in your cost structure as you sit here today and look forward?

Murray Mullen:
Richard, we—I'll have Richard chime in here. Richard and Lee Hellyer work with the OEMs on the equipment side. The OEMs, Rich, they've come to us and tried to push pricing, and we're pushing back on them because our customers are pushing back on us, so I think that we see that stabilizing. Richard, am I right on that?

Richard Maloney:
Yes, you know what? Absolutely.

Tim, with respect to OEMs, trucks, trailers and things like that, if you come—at the beginning of last year, they were telling us we were going to have to wait a long, long, long time, like just about a full year to get some stuff. Now, we're actually—they're coming back saying, hey, we might have some equipment that's coming available, and some of that is related to other operators throughout Canada that cannot take the order for whatever reason, in whether it's trailers or trucks, and yes, Murray, it's absolutely correct. We're pushing back with some of these OEMs, the truck guys in particular, and we're seeing some break in the commentary you hear from the OEMs talking about, oh, it's going to take 12 months to get a truck, and we're starting to see those orders becoming available and we're getting a little more aggressive with the pricing side of this from our perspective, where we're saying, you know what, we need better pricing because Murray is right - the customers are coming back at us with—you know, in certain regards as well.

I guess it's more telling of the OEMs and that they're calling now, looking and saying, hey, I may have another 150 trailers available that was not even in the works in January and February, because again we're seeing some of these orders not going to the customers that thought they wanted them. Their costs have gone up, the cost of borrowing has gone up, their capacity to borrow has come down, so it's—we'll be timely on that. We're not acting on that at this moment, but we will at the right point in terms of buying this equipment.

I think it's important to point out as well that some of the costs that have gone up with labour, they're not coming down. These are sticky costs, right, as well, so when Murray talks about and we talk about margins, I mean, that's our focus because as we move forward, there's not going to be any major reduction in how much we have to pay our people, because those are sticky as part of this inflationary environment here as well, so. These are all part of the world we live in,

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and then we just adjust our pricing accordingly in the business model and the size it may be, and where we're going to be doing that work.

Murray Mullen:
Tim, there's going to be pockets in this economy where you're going to have still labour's got some advantage, they're going to drive nice increases - I'm thinking in airlines, I'm thinking railways, I'm thinking ports. They've got—those are kind of monopolistic kind of market, so they can—they're going to get higher wage improvements than the general population.

Overall, though, we see it moderating. There's a little bit of catch-up, and you're hearing that from some of the contracts that are coming out - well, that's because in the last market, if you had a labour contract, they didn't benefit when prices went up because they were locked into a contract that they negotiated the last time. Well, they're playing catch-up. Well, most of ours are nonunion. Well, we went to the market, we paid people more money. I don't think we have to pay our people more money now, but I think there's catch-up in some of the union agreements that have to play—get caught up there, right, and that's going to catch a lot of the headlines, I think, over the next bit.

Tim James:
Okay, thank you. Those are helpful insights.

Murray Mullen:
Thank you.

Operator:
This concludes the question-and-answer session. I would like to turn the conference back over to Mr. Mullen for any closing remarks.

Murray Mullen:
Thanks, folks. I hope you enjoy the rest of your summer, and we look forward to chatting with you in Q3. I hope everybody has a safe and really happy summer. Take care.

Operator:
This concludes today's conference call. You may disconnect your lines. Thank you for participating and have a pleasant day.

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