The Mullen Group Limited

Fourth Quarter Earnings Conference Call and Webcast

Transcript

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Speakers:

Mr. Murray K. Mullen
Chairman, CEO & President

P. Stephen Clark
Chief Financial Officer

OPERATOR:

Welcome to the Mullen Group Limited Year-End and Fourth Quarter Earnings Conference Call and Webcast.

As a reminder, all participants are in listen-only mode and the conference is being recorded. After the presentation, there will be an opportunity to ask questions. To join the question queue, you may press star, then one on your telephone keypad. Should you need assistance during the conference call, you may signal an Operator by pressing star, and zero.

I would now like to turn the conference over to Murray K. Mullen, Chairman, CEO, and President. Please go ahead.

MURRAY K. MULLEN:

Thank you. Good morning, all, and welcome to Mullen Groups' quarterly conference call.

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

With me this morning, all social distancing, is the entire Executive Team of Stephen Clark, who's our CFO, Richard Maloney, Senior VP, Joanna Scott, Corporate Secretary and VP of Corporate Services, and Carlson Urlacher, who is our Corporate Controller.

Thank you for joining us today, and it was just a few short weeks ago that we held our 2021 Budget and Business Plan Update with our shareholders and investors, and as such really there's not much that has changed since early December 2020, either as it relates to our business or that dastardly COVID-19, so let's keep everything I say today within the context that it all depends on COVID.

I am going to turn the call over to Stephen here shortly who will discuss our 2020 results, but before I do, here is a recap of what I saw as the big picture, and this is clearly from my perspective.

Number one; the consumer reigns supreme in this economy. Now, after that dreadful second quarter, the buying power of the Canadian consumer just took off. They seem to want to buy everything in sight, which is music to our LTL teams, and by the way, they did a fantastic job adapting to all of the necessary safety protocols for essential workers, and meeting the demands of the consumer and of our customers. Heck, even our LTL businesses in Alberta did okay, which is astounding because everyone knows that Alberta was crushed with low oil prices and a struggling economy.

Now, number two; since we're on the theme of consumer-driven economy, there's a transition to the e-commerce direct-to-consumer trend that absolutely hit another gear in 2020. This is probably the single highlight trend we see in the logistics industry today, and one that we believe we are going—is not going to go away anytime soon. We know firsthand what this changing landscape can have on your business if you are e-commerce ready.

Our DWS group, for example, based in Toronto, absolutely crushed it for their customers, so much so that I personally received calls from a customer thanking the team for helping them meet the challenges associated with e-commerce deliveries spike—that spiked during 2020.

The third thing that I'm going to talk about as the big picture, it's diversification pays dividends. Now, it's pretty evident that not all of our business units had an easy year, especially those that were tied to the resource sector of the economy, yet in spite of some of the business struggles, we had a very successful year.

The fourth big picture trend, I would say, is acquisitions that were on our radar, but we just didn't get to the goal line because of our view on valuations, along with trying to rationalize, how do you drive margin improvement given the no travel environment, etc., etc., under COVID? We got a couple of nice tuck-ins completed, but nothing to move the needle, so truthfully, from that perspective, I have to say that's a bit of a disappointment.

So, let me summarize 2020 this way. Revenues were down, margins were up, and that equals a pretty darn good year.

Within this backdrop, I'll turn the call over to Stephen who has the details as it relates to 2020. Steph, it's yours.

P. STEPHEN CLARK:

Thank you, Murray, and good morning, fellow shareholders.

I'll get a little bit more granular. However, our annual financial review contains the full details that explains our performance. As such, I will only provide some high-level commentary.

As Murray alluded to, it has been a year for the record books. Although revenue in all three segments declined, each segment continued its long march to a full recovery that started in Q3 and continued in the fourth quarter.

For the quarter, consolidated revenue declined by approximately 5%. The effects of COVID-19 are widespread. However, it appears investors have shed their hesitancy and are looking past COVID and towards the wide distribution of a vaccine and the consumer confidence to spend. We saw signs of this in the fourth quarter. However, in the meantime, efforts to contain the virus will continue to constrain the economy.

Revenue in the consumer-driven, Less Than Truckload segment rose by 1.8%, more or less flat when you adjust for acquisitions. However, the Logistics and Warehousing and Specialized and Industrial services segments declined by 5.3% and 15.2%, respectively. This is considerable improvement from the lows in Q2, and reasonable given the current crisis.

We are seeing regional differences, but for the most part, the consumer is back spending again in usual seasonal fashion. The resurgence of the virus has prompted governments to re-impose containment measures, and the start/stop nature of the economy will likely haunt us for the foreseeable future.

Overall, year-over-year revenue decreased by $16.9 million to $290—yes, year-over-year for the quarter decreased by $16.9 million to $297.7 million, including the effects of $8.6 million of

acquisition revenue and $6 million decrease in fuel surcharge revenue. Excluding the effects of acquisitions and fuel surcharge fluctuation, revenue decreased by approximately $20 million, or 7%, largely due to the weakness in the S&I, the Specialized and Industrial Services segment.

On a sequential basis, consolidated revenue increased by $6.8 million for the quarter from $290.9 million achieved in Q3 of 2020, reflecting signs of a strengthening economy. As for profitability, operating income before depreciation and amortization, commonly referred to as a EBITDA, for the quarter increased by $2.3 million, or 4.6%, to $52.2 million.

Segment EBITDA increased in the LTL, L&W and S&I segments by $2.1 million, half a million and $0.9 million respectively. Of course, this number comes in part as a result of CEWS, but the underlying number of $46.9 million as compared to $49.9 million in Q4 of 2019 is virtually flat dollar-wise on reduced revenue. The underlying EBITDA number reflects the strength of our business model, but also one underlying fundamental.

Diesel prices fell by an average of 29% during the quarter. This benefited our business, but also reduced fuel surcharge revenue and reduced fuel as a percentage of revenue from 9.4% to 7.6%. This difference of 1.8% added about $3.9 million to the bottom line. Now, I will note that some issuers prefer to report Adjusted EBITDA margin by reducing the revenue and the cost by the quantum of the fuel surcharge revenue. Of course, this is a non-GAAP measure, and by making this adjustment to the denominator in this fashion results in a contrived margin expansion. We prefer to report in generally accepted fashion, so our margins are based on full revenue and full costs.

Without any accounting trickery, our operating margin improved to 17.5% from 15.9% in 2019 primarily due to a greater proportion of higher-margin revenue—thank you pre-made pipeline—lower diesel prices, and cost control measures. CEWS was also a factor, but it was not as large as it was in previous quarters. The CEWS adjusted margin was 15.8%, or more or less on par with prior year.

Revenue for the year declined by 8.9% to $1.2 billion, down from $1.3 billion. However, EBITDA improved by 8.3% to $217.6 million, up from $200.9 million, and was due to the strong performance by all three segments. Operating margin adjusted for CEWS improved by 0.7% to

16.4% as compared to 15.7% in 2019. Full details, including a segment breakdown, can be found starting on Page 23 of our Annual Financial Review.

Looking at other notable items, net cash from operating activities for the year was up to approximately $225 million. We used some of this cash to invest in our Company; firstly by buying back stock for $53 million, and by purchasing $35 million of trucks, trailers, and other equipment, as well as $15 million of much valued facilities for total net CapEx of approximately $50 million.

We also funded the acquisitions of Pacific Coast Express and IWD for approximately $20 million. After those investments, as well as paying our taxes and interest obligations, we still have excess cash and we paid about $35.5 million in dividends. So, after all that, we remained with approximately $105 million of cash on the balance sheet, and in addition to our cash, we have an undrawn $150 million line of credit and substantial positive working capital.

Our total net debt to operating cash flow financial covenant under a private placement agreement, which gives us the benefit of our in-the-money currency hedges, was 2.10 to 1, or about 2 times cash flow; rather conservative position to be during a recession.

Lastly, a quick word on ESG. Lots of people ask me about this. Much talked about by some, but some conversations regarding ESG lacks common sense. Outside rating agencies do a poor job of assessing ESG, in my opinion, so consider these facts when reading their reports on us.

Our safety record, as measured by lost time injury frequency, is less than half the industry average; in fact, world class at less than one lost time claimed injury frequency. That is just absolutely hitting it out of the park and—but some rating agencies would say you've seen a trend where you've gone from 0.9 to 1, so you're going the wrong way. Well, of course, if you're an acquisitive company, sometimes you acquire companies that don't have a good a safety records and you average up, but I can assure you that we see improvement in all our businesses every year.

Secondly, our SmartWay partnership is not very well understood by many of the ESG rating firms. SmartWay is a partnership between industry, the U.S. EPA, and Natural Resources Canada, and it is committed to reducing greenhouse gases. We were one of the first to enroll,

and today, there are approximately 4,000 participants. Why would you voluntarily subject yourself to a governmental annual review of your greenhouse gas emissions? Because you're committed to ESG, committed to ESG long before it was fashionable. Under SmartWay, firms are reviewed annually and benchmarked against their peers. Our subsidiary, Kleysen Group, is one of only 12 with high performer status, and each other of our BUC annual improvement.

Lastly, if you are concerned about ESG, please consider our commitment to our frontline workers during the COVID crisis as articulated in our March 2020 news release. Action like these simply do not fit in an ESG ratings box. Putting aside $5 million dollars for our frontline workers before government programs were instituted speaks volumes to our commitment to ESG and our frontline workers.

On that note, I would like to personally thank our frontline workers who tirelessly delivered essential goods each and every day, ensuring our cupboards are full and our economy moves on.

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

MURRAY K. MULLEN:
Yes. Thanks Steph. Well done today.

As we move into this next section before we get to the Q&A, what is it that I really see today that I didn't see eight weeks ago? Well, let's start with we still have COVID to deal with—that—so that hasn't changed. In fact, if anything, I’d have to view the recent actions by governments as harmful to business on the economy. Now, all we have to do is look at the recent employment numbers, and to be blunt, they're just awful, so will all of this alter consumer behaviour? This is truly the unknown to—from my perspective, and it's one that bears watching carefully. It is pretty evident, however, that if you give consumers money, if you give them a reason to buy, they certainly will, and until we see a return to growth in the overall economy, I can tell you that our focus will be on margin.

Number two; the supply chain remains under stress, and the evidence is clear. We see it in the shipyards. We see it at the rail yards. We see it at our terminals that handle container freight. This suggests to us that the increased inefficiency in the supply chain will bring a need for more

warehousing. It's all going to bring along increased cost into the system. In fact, the bottlenecks in the supply chain that everyone is noticing, and it's slow—it's really slowing everything down, and from my perspective, that combination of an increase in consumer demand, which was real, but it's been masked a little bit, because when you layer that on top of an inefficient supply chain, which what we have today, it creates the illusion that it's actually busier than it really is. Now this bears a lot of close attention.

My view is that, yes, consumers are strong, and they're probably going to remain the best part of the economy, but the supply chain is bottlenecked. We're hearing it all over, whether it's chips, or whether it's some foodstuffs, it's container traffic, all of that stuff. We have to be very, very careful on watching whether this is a—what's this long-term trend, so our job is to be thoughtful and to strategically position our Company to capitalize on these trends. So, that's what we'll be doing.

LTL remains the most resilient part of the freight business. The consumer is still spending. Maybe it's because we're bored. We're sitting at home and we just go and do stuff. I'm not sure, but the packages seem to still be delivering to the houses, but the other reasons that our LTL business is doing well, I've got a highlight them. We're investing in this part of our business. We've got some new terminals that we've opened up. We're going to expand coverage. This improves operational efficiency, but it also—we're changing so that we can have the capabilities to handle more e-commerce deliveries, which is—as you all know, is direct to the consumer, not to the retail store, direct to the consumer, as well as the move towards ambient freight, which is a form of LTL movement. So, LTL remains the most resilient part of the freight business, and the staple of our business.

Higher commodity prices, what has changed? Well, clearly, higher commodity prices are in the news these days, and that's changing a lot of the prospects for the oil and gas industry. We see the rig count up from last year, although not up to where it was in 2019, so I think we still have a long ways to go, but this is a welcome change that we see in the marketplace today, and everything we see suggests that 2021 will be a lot better than 2020 in the oil and gas industry, thankfully.

Here's what I'm going to leave you with. The world wants what Canada has. That's pretty evident. The question is will Canada participate, or will Canada's oil and natural gas industry

simply make more money as commodity prices worldwide increase, and it seems to me that if no one wants the industry to invest, which keeps the lid on commodity prices, then no one should complain when prices rise.

The last discussion point I've got is on acquisitions. Now, clearly, the capital markets want growth and they'll reward companies that have a growth trajectory. There's an unlimited amount of capital in the system. The lowest bond yields ever hit in the United States this week. It's easy to see how valuations can get stretched. The challenge, as I see it, is finding growth that makes sense over the longer term. We have our work cut out given the current easy money environment, but until then, we have a big cash position that is looking for a really good home.

So, all in all I would say to you not much has changed from our perspective, and we remain focused on achieving our 2021 Budget and Business Plan that we outlined on December 9, 2020, so I would—I'll just summarize it by saying this. I think it's going to be slow out of the starting gate due to COVID, and I would not be surprised to see a nice, strong finish to 2021. That's our prognosis for today.

Thanks for joining with us, and I'll now be glad to entertain some questions.

OPERATOR:

We will now begin the question-and-answer session. To join the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

At this moment, we have five callers in the queue, and the first question comes from Konark Gupta with Scotiabank. Please go ahead

P. STEPHEN CLARK:

Good morning

KONARK GUPTA:

Morning, Stephen. Maybe the first one’s for you.

Looking at the Q4 numbers, I can see there seems to be some negative foreign exchange impact in Logistics and Corporate, as well as below the line, and there was probably an increase in the loss of active sales of $4.3 million in the numbers. Just confirming if these items are not adjusted out of the $52 million EBITDA and $0.10 EPS, and if that's the case, can you suggest what would be (inaudible 00:20:32)?

P. STEPHEN CLARK:

Okay, so for foreign currency, what we have is we go mark-to-mark on the foreign currency within primarily our Logistics and Warehousing division where we have receivables and payables, and so we mark-to-mark those, and those are in the table. I don't have the page number in front of me, but you'll see that within that segment primarily, and you'll see it on the consol—on the S&A costs.

Below the EBITDA line, that foreign currency really relates to the mark-to-mark that we have to do on our hedges, our swaps, and our debt, so accounting-wise, there's a bit of variation there, and we normalize that portion in our adjusted normalized earnings which you will find in our Annual Report on Page 28, and so it's adjusted for that, but I would remind you that it’s not our intention to really trade those hedges in the market. We have those, and our intention to hold those to maturity in 2024 and 2026, and we have to net present value those using a discount rate for counting purposes, so it comes up with a little bit of a variation, but from an economic point of view, we’re fully hedged on that debt. All $229 million of U.S. currency is fully hedged at about $1.10, $1.11. We locked those in when we took out the debt, so from that perspective, that's the noise there. We could get more into detail offline if you want to?

KONARK GUPTA:

Yes. No, absolute. Thanks for that, and the $4.3 million loss on active sales, the increase and loss versus last year, what was that about?

P. STEPHEN CLARK:

We just cleaned up the garage, and sold some older equipment. It was just not a great time to be selling used equipment in Q4, so we took some asset losses there, and we also sold a property in Drayton Valley that we also experienced a loss on.

KONARK GUPTA:

Okay. Thanks, so moving on then. The second question is on margins, I guess, excluding CEWS, of course. All three segments clearly expanded margins from last year, which we also saw back in Q3 as well, but this time, the margins in Q4 were not as much better as they were in Q3, so does CEWS adds to—is there anything between Q3 and Q4 that seasonality, and that's non-seasonality that would have diluted the margins a little bit here? I don't see a PCX being dilutive as much as I think people might have thought before, so any thoughts there on the margin, that'll be appreciated.

MURRAY K. MULLEN:

It's Murray. Good morning, Konark.

I don't think there's anything real serious. I think what you're really starting to see, though, if you want my honest opinion, is I think you're starting to see some costs come into the system. There's inefficiencies in the bottleneck—in the supply chain that we talked about, so we are not quite as efficient as we once were. We did bring back people in anticipation that is was going to get busier, so I just think that's the primary reason, to be honest. There's nothing alarming, but you're spot on is the initial initiatives that we had to reduce cost, we couldn't keep pressing the button on those forever.

You have to let off the pedal a little bit, and a lot of it had to be that'll bring the people back and you've got to pay them, and I think that's the single biggest reason, along with those inefficiencies in the supply chain. We're just, God darn it, it's just, it's awkward. You get going, and then a customer cancels their—have to shut down their factories, so that happens, and then you get trucks moving, so there's been some inefficiency that—it's not changing everything, but it does-incrementally, it does impact margin, that's for sure.

P. STEPHEN CLARK:

We also saw a little bit of the cost of contractors go up as a percentage of revenue, so we've seen freight rates go up, but we also had to pay our subcontractors, those third parties, a little bit more, so that's also a bit of a factor.

KONARK GUPTA:

Yes, actually I was about to ask you on the contractor front as well. Seems like that went up, so is it—the plan, is it because of the contractor rates going up minus the volume decline, or is it both volume of contractor. Have you started using substantially more contractors?

P. STEPHEN CLARK:

It's mainly the rate, mainly in the L&W, and our fluid hauling businesses where you're playing the spot market for a lot of that stuff and trying to fulfill customers needs that way, and there was some strengthening in the fourth quarter, and although our guys are usually very good at managing the spread, we got caught behind a little bit during the quarter.

KONARK GUPTA:

Okay. Thank you, and that's my two.

MURRAY K. MULLEN:

Thank you.

OPERATOR:

Our next question comes from Kevin Chiang with CIBC Capital Markets. Please go ahead.

KEVIN CHIANG:

Thanks. Good morning, and hope you're doing well, Murray and Stephen.

Maybe if I could maybe ask a question on one of your comments you made there, Murray, on maybe 2020 being a little bit of a disappointment on the M&A front because you didn't do a bigger deal, you didn't see a bigger deal. I know you have the dry powder, $250 million of liquidity. Just wondering what the appetite is to do one, especially when you look at some of your other publicly-traded Canadian trucking comps out there having started this year with some pretty transformative deals. Do you see an opportunity to do something similar on your front, or do you think 2021's more of a repeat of 2020, and it's more of a tuck-in variety?

MURRAY K. MULLEN:

Yes. That's just a really good question, and I touched on it a little bit. We all know the liquidity that's in the system, and that has been driving acquisitions. It's just unbelievable some of the

transactions that have happened. The issue that I have struggled with, to be honest with you, is there's something fundamentally changing in the economy that would say that margins are going to change in the trucking business, and I don't see—unless we have some real bump in the economy, I don't see massive demand. You need a significant demand increase for us to see a big step change in pricing.

The United States has seen it better than we have in Canada, and there's way more opportunity in the United States than there is in Canada. That's just fact (inaudible 00:27:56), so I was probably not as aggressive as what the capital markets would have liked. There's no doubt from that perspective, but in each case when I look at an acquisition, I say, okay, how do I change the denominator? How do I change what you're buying, because in most of these transformational acquisitions you're talking about, the companies that they're buying don't have good margins, but the management team say they've got a good plan on how to change the denominator and change the profitability of those business units.

I didn't see that, so we didn't go ahead with the major ones, but we sit looking for the right one, and we play the long game, Kevin. We'll be patient, and when—but when I find the right ones that I think can change, then we're going to be very, very aggressive on those things, so those would be LTL. You know we like LTL. That's a good part of our business, and we like regional LTL. I don't like big LTL in the big centres, because the big centres, to be honest with you, I think are going to get crushed. LTL's going to get hurt by direct-to-consumer, because they're not going to be going to the storefront. You're going to be going direct to the consumer, so that implies more warehousing and e-commerce than it does LTL, per se, so I've been blunt with everybody. I might have out thought it last year in 2020, certainly within the context that there was so much money available and everybody was chasing things, and we'll see how it plays out from that way. The others have got their work cut out, but I give them credit for being aggressive. We were not. We focused on margin, but I can tell you we look every day at ones, and when I see ones that I think we can make the change, we're going to be extremely aggressive.

What we did last year—clearly, we were aggressive last year in acquisitions. We bought back our own stock when the market mispriced us. That was the most aggressive move we did, so, so far, so good. That was a good move. Now, if we want top line, we're going to have to do acquisitions, because it's pretty evident the Canadian economy is stalled. It's going

nowhere, and the consumer remains robust, but the consumer's not going to be—on its own, be able to drive growth in the Canadian economy. You need to get that pool of capital, as you know, growing and being deployed in the economy, not just in the stock market, so I suspect that acquisitions is your only clear path towards it, so within that—we know there's a clear path towards margin and margin improvement with tuck-ins. We know that. We've been good at it, and we will continue to pursue that as number one, and then we'll do a transformational or a big one when we see that that gives us a growth platform in a new growth market.

I'm going to make—over the next bit, we're going to have to think long and hard about our U.S. strategy, because as I said, the opportunities appear to be down south, not in Canada.

KEVIN CHIANG:
You took the words out of my mouth there.

MURRAY K. MULLEN:
Yes. If you're going to do that, you have to have a well thought out strategy. You just can't go play in that big shark tent and expect to be—to go in there and just take over. You're going to have to be—if you go in there, you're going to have to be as aggressive as the American carriers are. You can't go in and just dip your toe. You're going to have to go in and you're going to have to fight hard and you're going to have to grow like crazy.

KEVIN CHIANG:
Makes sense.

Stephen, maybe just a—I'll call it a clarification question. I noticed you did have an impairment assessment of goodwill for your S&I segment, which looks like you've addressed just looking at the disclosure, and it looks like a lot of the sensitivities suggest you'll be able to recover the future cash flows just looking at the MD&A there, but just wondering how you see the risk of a potential impairment with owing an additional impairment to your S&I segment, especially given the move in rig counts and in energy prices as we sit here today versus maybe when this assessment was done in late 2020.

P. STEPHEN CLARK:

Yes, so there's a lot of subjectivity to those models, and it's a discounted cash flow model, and by IFRS regulations, you're doing it for a 5-year time horizon. We're certainly expecting a lift in the rig count and the revenue over time more than the 2.5%, but we're not talking 50% increases here, so were—we're thinking that, more or less, 2019 would be more of a comparative base year, and if we did what we did in 2019 going forward, and 2020 was below that, that we'll do okay and we won't have impairment.

I'll remind you we did take $100 million of impairment hit in 2018, so we wrote off quite a bit there, and so what's left there, $78 million, is mainly in companies like Canadian Dewatering, as you can see on the list in the financial statements on page whatever it is, it's pretty fair around Page 100, but—so there's not a lot left, necessarily, in that; clearly no impairment in LTL or Logistics and Warehousing, so you're right. That segment is the only one that's still at risk, but as I say, if you look at the list and see who's got goodwill that's still left there, like Canadian Dewatering and such, there's not much risk there, and we're just really counting on the economy improving back to at least 2019 levels, which we think is a fair—given—especially today, I can tell you in January, we're ahead of our models, but it's only one month, but I think that's a fair assessment to say 2019, when oil was $50, $55 a barrel—we're not counting on $100 a barrel—I think that's a reasonable macro environment to base a model on, and so that's what we did at the end of 2020.

KEVIN CHIANG:

No. I appreciate the colour there, and that's it for me. Thank you very much for taking my questions

P. STEPHEN CLARK:

Thank you.

MURRAY K. MULLEN:

Thank you.

OPERATOR:

Our next question comes from Walter Spracklin with RBC Capital Markets. Please go ahead.

WALTER SPRACKLIN:

Yes, thanks very much, Operator. Good afternoon, everyone.

I guess when I characterize your comments around your guidance, which to your point, Murray, you had provided just a couple months—or not even a couple of months ago, your—maybe demand is maybe a touch more complicated. You like that the consumer's still buying supply chain, I hear you, is a negative from that period, I guess. Your LTL resiliency is unchanged. Higher commodity prices are positive, and then acquisitions, I mean, I'm gauging you could call that a question mark, I don't know, so when I put all that in the mix, you're effectively saying, okay, the guidance is unchanged. We're starting off weaker than we had hoped, but we'll wait and see. Is that the right message here Murray, or are you indicating...

MURRAY K. MULLEN:

Yes. No it's pretty close. I didn't know that every provincial jurisdiction was going to lock down nearly everybody. The issues that you're having with some of the supply chain are real. You can see that even in the auto sector now where you can't get a part, and you have to shut down the line. Well that's backing everything up, so the system's not working as efficiently.

I will tell you where they are working, really, really, the economy is doing fantastic. It's China. China is making everything that the world buys, that the consumer buys, and the supply chain is bottle-necked coming out of China on the containers, so they're busy. The factories are busy, and we're busy consuming, but they're busy creating and building, and that some of the supply chain has been bottle-necked. You can see it in the shipping rates. You can see it in the container companies, and in the big ports. They're backed up, and so the costs are there. That's troubling, and it doesn't help the bottom line, and it slows things down a little bit.

As I said, I think it creates the illusion that we're—when you have bottlenecks, that you're busier then what you really are. It's not. We're sitting and waiting way too much, and then, of course, the fight comes on with the customer, who's going to pay? Is it a driver? Is it us? Is it the customer? Is it the ship line? Oh my God, it's—everybody's fighting with everybody these days because there's not—the supply chain's just not working on a just-in-time business model anymore, so yes, I think it's going to be slower coming out of 2021. That shouldn't surprise anybody. Nobody can do anything, so that shouldn't be a surprise. What we're all waiting for is

okay, when do we get out, and when do we go back getting the economy going again, and I don't have the answer to that. Nobody does, but clearly, it's been slow out of the gate to start the year. I'll be blunt with you.

Now, the one thing it hasn’t been slow on, and I'm going to just make this caution again, is on the commodity price side, and the reason the commodity prices are up is because China and other places in the world are absolutely booming, it's—and commodity prices are going up, and that's going to help those in the energy space, particularly those that are the producers, and then they're spending a little bit more money, and I'm hopeful that by the end of the year, that they spend even a little bit more, so that—but that's also going to raise fuel prices, and then fuel prices lead to fuel surcharges, and your fuel costs will go up, so there's some stresses in the system, but overall, slow out of the gate, but the thesis is intact. Once you get the consumer out and about and they can spend, they're going to spend, and that will be—that will lead to a decent, pretty good second half, and that's how we're looking at it.

WALTER SPRACKLIN:

Okay. Just as a follow-up then on the M&A side, Murray, would you characterize your lack of activity there as being—was it because there’s just nothing available in the regions that you at the time were looking, or was it—there's lots available, but just at a price that was above what you were willing to pay?

MURRAY K. MULLEN:

That was a culmination there of some of the bigger ones that we know about in the marketplace and some of my peers, I—we were not involved in those transactions at all. One of them, we wouldn't have looked at, at all. Actually, we wouldn't have looked at any of them. They wouldn't have been on our radar screen as something that we would have done. The ones that we did look at, the valuations have moved, and one would have to have a very good—I can get growth. We can get growth to our shareholders, top line. The bottom line growth is how do you change the denominator, and you've got to be able to find synergies, because, I'll be blunt with you, very few acquisitions do I look out there, do they make the same margins that our business model makes? It's really difficult, so then you say, okay, well how do you change the—how do you change it.

Well, we've got to be sure that we know how to go about changing it, looking for synergies. There's no doubt about it, so—but we've looked at lots. We've looked at a ton of them, and in hindsight, I could easily say, knowing what the—how the market will now reward growth, geez, we should have been more aggressive. The market would have liked that. The market comes, the market goes, and those kind of things, but you're right. We're sitting here with lots of cash and talking about acquisitions, and we haven't done any, so I've got to take responsibility for that.

WALTER SPRACKLIN:

I guess it's a bit of a virtuous cycle. I mean, the market is rewarding it. The more you do it, the higher your share price goes, the lower your cost of capital, and the more you can afford at the—get the same returns at a higher price, but I guess now with everything that you've seen, I get the sense you're looking at it a little differently, but not only differently from valuation, but also scope, and did I read it right, that you—I mean, you used to look only in kind of Alberta, Western Canada. You're considering now Eastern Canada. Now, am I correct in inferring here that you're now willing to look into what you declined—you described in the past is a cutthroat type of region, being the U.S. Are you looking that kind of regional opportunities in the U.S. now, whereas perhaps you weren't before?

Murray K. Mullen:

I have—I have not—I haven't focused on anything, but I would say I think I'm going to be forced to look in the U.S., because the opportunities in Canada are slim to none, and I just don't see the Canadian economy having a lot of growth potential. The growth potential is probably going to happen in the U.S. much more aggressive, so I'm going to be probably forced to fine-tune my attention on that, to be honest with you, so yes.

In the East, we've done acquisitions. We've done a few. We're going to do more. We're expanding our—some terminals we're expanding, did a couple of acquisitions. We've got a couple of more we're looking at, and then our other—the company we own 30% of, our Kriska Group, they've been extremely aggressive on acquisitions, and so they've already done a couple more this year, and they continue to grow their business. I'm really, really pleased with what we've got in our partnership we have with Mark Seymour and his team there. They're good, and we looked at some of the other ones that went down with some of our peers, and we passed on it. We just said that's—when I talked to Mark, and he says, Murray, it's not—that's

not one to go after. I go, well I'll take—I listen to people that are on the ground and know more than I do, so we passed on some. Yes.

WALTER SPRACKLIN:

Yes. Makes sense. Okay.

MURRAY K. MULLEN:

I know it sounds boring, but let's be blunt, the Canadian economy is not growing. If you're going to grow—even my good friends at Transport—Saline (phon 00:44:11) has done a fantastic job. That guy is just a star, and I'll tell you, if he pulls off this acquisition with UPS Freight, if he pulls that off and gets those margins up, give him the CEO of the decade in Canada. If he pulls that off, he deserves every accolade that goes and he should get all the stars, because that is gutsy, and—but clearly the market's not betting against him, and I wouldn't either, but—you even look at his numbers. I mean, he did 13 acquisitions last year to not grow—and no growth in the business, and we find exactly the same thing. There's no growth in the economy. If you want to grow, you have to do acquisitions, and even Elaine (phon 44:56), he likes tuck-ins. He's been really good at the tuck-in one, and that's our business model too.

WALTER SPRACKLIN:

Yes. Makes sense. Okay. Appreciate the time, as always, Murray.

MURRAY K. MULLEN:

Thank you, Walter.

OPERATOR:

Our next question comes from Michael Robertson with National Bank Financial. Please go ahead.

MICHAEL ROBERTSON:

Good morning. Thanks for taking my question.

I was wondering if you could provide some more colour on margins for the LTL segment in Q4, specifically looking at margins excluding CEWS both in 2020 and in 2019. In the fourth quarter, LTL margins are down 200 to 300 basis points relative to what you posted in the

second the third quarters. I know you post seasonality for LTL was lower profitability in revenue in Q1 following a busy holiday season and higher maintenance and fuel expense in the winter months, so I was wondering if we're just seeing a bit of that in Q4, or if there were something else behind it, or if maybe it's just a coincidence, because I'm admittedly looking at a small sample size here.

MURRAY K. MULLEN:

I'll let Stephen opine after I have, but I don't think there's anything major. I'm pretty impressed with how our business units manage that, but typically what happens when you head into the fourth quarter, you have a reduction in volume, just because the stores are stocked and LTL volumes start to decline a little bit which means your terminal net worth is just not as busy. You don't have as much throughput going through. Q2 and Q3 are typically the busiest months for LTL. This year it went into the fourth quarter a little bit more than regular because of what we talked about; just the bottlenecks in the supply chain, so all in all, there was nothing in there that disturbed me or gave me cause for concern. We're going to hold our own. We're going to continue to work on margin. We're going to continue to make investments so that we drive margin up, and that's what we're going to do, but the market, it does get a little softer in Q4 and Q1. In Canada, that's a natural trend, so I wouldn't read anything more into it than that. There's no other increased cost or anything that I know of other than just—you just don't have as much revenue going through your cost.

MICHAEL ROBERTSON:

Okay. That's great. Appreciate the colour.

P. STEPHEN CLARK:

Yes, Michael, I would just echo that, and just on the fourth quarter in particular, it's the first full quarter that we have Pacific Coast Express, which is 100% owner operated business, so it does have slightly lower margins, but that's the only thing that's different this fourth quarter than any other fourth quarter. It's the seasonal effects of buying patterns that stores are full by the beginning of December.

MICHAEL ROBERTSON:

Got it. Got it. All right. That's great. I'll turn it back.

P. STEPHEN CLARK:

Thank you, Mike.

OPERATOR:

Once again, if you have a question, please press star, then one. The next question comes from David Ocampo with Cormark Securities. Please go ahead.

DAVID OCAMPO:

Good morning, Murray and Stephen.

MURRAY K. MULLEN:

David, how are you?

DAVID OCAMPO:

Pretty good. Pretty good.

I just want to follow up quickly on one of the comments that you made in your prepared remarks. I was just wondering if you could provide us with sort of the split between your traditional LTL and the ambient temperature control LTL, and perhaps building on that, is there any difference in performance that you saw between the groups in 2020, and maybe even your outlook for 2021.

MURRAY K. MULLEN:

We don't have a—we don't drill into—down to that layer. I know one. It's not a huge part of the mix. Ambient, in the whole LTL world, is going to be a very, very small overall part of the LTL—the LTL network and it will be with us, but it's incremental to our LTL network. It's something we've never participated in, so it's all incremental growth for us, and we've got to focus on it to be able to provide ambient, particularly out in the—in all of the remote areas that we service. That's primarily what we're talking about with our LTL network. We serve literally hundreds and hundreds of communities across—from Toronto right to the West Coast, so that'll be an increase, along with e-commerce will be an increase to our business. That's why I say to you, LTL will do fine, and then we're doing things to make LTL better than what the market is, because we're focusing on direct-to-consumer from our terminals, and also adding that ambient capabilities, and—which is incremental in freight. It's not going to double our

revenue, but it's going to be incremental. It will help us improve the margin, because it's higher margin business relative to traditional LTL freight.

DAVID OCAMPO:

No, that was very helpful, and that's all I have for today. Thanks a lot, guys.

MURRAY K. MULLEN:

Thanks, David

OPERATOR:

Our next question comes from Matthew Weekes with iA Capital Markets. Please go ahead.

MATTHEW WEEKES:

Hi. Thank you for taking my question.

I really just have one. With the re-segmentation now including Smook Contracting in the Specialized Industrialized Services segment, I'm kind of looking at how Q4 relative to Q3 has occurred over the past couple of years using those results, it appears that there may be sort of a seasonality in that business that we could expect to be maybe regular going forward. I was wondering if you would just be able to provide a little colour on how kind of the seasonality in those industrial-focused business works within that segment.

MURRAY K. MULLEN:

Stephen, you going to tackle on that? We typically have an increase in certain sectors of that segment like oil and gas. Typically, when it gets winter, you go to work and it's a little busier. Conversely, our Canadian Dewatering business, for example, there's not as many water projects going on, it’s frozen. You're not doing as many projects, so Canadian Dewatering has a countercyclical component to it, along with our business up in Manitoba called Smook, which is the construction side, and that typically slows down in the winter, construction projects, and then picks up in the summer. So, there's nothing—I don't think there's anything quirky about it, but it will be a little choppy going into the winter months, particularly until we see whether the increased cash flows that we’re seeing in the energy space now, whether that translates into more drilling activity. If that turns into more drilling activity, then our winter months are going to be busy again. I've seen a little bit more than what they were talking about, but not back to

where we were in 2009 yet, but it sure looks a lot better right now. Their balance sheets are in pretty good shape, so we're waiting for more activity for sure. That's a little better than we anticipated, but not back to where we want it.

P. STEPHEN CLARK:

Yes, and Matthew, this is the first quarter that we're really reporting Smook within that segment. It used to be in the Trucking and Logistics segment for some strange reason. It's one of those odd ducks that really doesn't fit anywhere, right? Likewise a trucking firm into (inaudible 00:52:54) construction, but it represents about 10% of the segment revenue, just to give you a quantum of how large it is in terms of annual revenue, but fourth quarter revenue for them is half of what it is in third quarter, and same thing can be said for Canadian Dewatering. You're just not moving a lot of water in December and in the last half of November, and conversely, it depends on when it gets cold and what the price of oil is whether you're going to be billing and busy in that drilling segment or category, and this year was better. It sequentially moved up, but not to same rhythms and patterns as it has in years past. There was still some capital hesitancy and (audio interference 00:53:55) and such on our customers' part in the fourth quarter.

Now, we've seen a dramatic change in the first quarter where the red count is up handsomely, but maintenance side on the oil sands plants, which is a big part of our business now in the S&I business, still COVID delayed, COVID slowed down, constrained. You can't have people working together and whatever. It's still a bit of a—I would say an unusual year and would continue to be an unusual year as far as regular seasonality goes. I think that this is just another year for the record books where nothing worked like it did the previous year.

MATTHEW WEEKES:

Okay. That's helpful. Thank you. I'll leave it there and turn it back.

MURRAY K. MULLEN:

Yes, just on the Smook thing, why do we have a construction company in (audio interference 00:54:34)? It's real easy. Our Kleysen Group, one of their largest customers, is out of Thompson, Manitoba and Vale, and this company did a lot of work with Vale, and we were kind of asked by the customer would this kind of work out as this company came available, and so our Kleysen Group was the one that really oversees this and looks at it. That's why it was in

the Trucking Logistics segment before, because our—it was really an extension of our Kleysen Group, but we segregated it when we went with our three segments, just to clarify that for everybody.

OPERATOR:

Our next question comes from Jeff Fetterly with Peters & Company. Please go ahead.

JEFF FETTERLY:

Good morning, everyone.

MURRAY K. MULLEN:

Hey, Jeff.

P. STEPHEN CLARK:

Jeff.

JEFF FETTERLY:

Two quick ones. Within S&I, what is your line of sight and expectation in terms of Premay and the overall pipeline piece?

MURRAY K. MULLEN:

Line of sight's at least 2021. It looks like the way it's going, probably 2022; a good chunk of it. These projects are just going brutally slow, and I know our customers don't want to hear that, but to do anything in Canada these days, you—it's just tough to get anything done, so at least 2021, probably 20—most of 2022 on the pipeline side, which we think gets us closer to when—than the spend goes into the drilling side to fill the pipes, so it'll just—I think the spend will move and the results will move from the pipeline side being busy and producing nice results to more of the related to the drilling side is our thesis on that side, so the market's a little bit tight right now. If you open those lines up, particularly Coastal Gas, somebody's got to fill them, and so that probably leads to more drilling, and that helps our drilling services component of our business, and those kind of things, so right now we're fortunate. We've got the pipeline side that's doing well, and it looks like we've got at least a couple of more years on that, and then it will translate and just move right into drilling.

JEFF FETTERLY:

For Mullen, within the pipeline piece, do you expect that ‘21 will be a better year than 2020, because I know you...

MURRAY K. MULLEN:

No. I wouldn't say a better year. Last year was an exceptional year. We've highlighted it’ll be another good year because we have a number of—the projects that we're working on are still in the throes, so it’ll be another good year, but I don't think it’ll be a better year. That's going to be tough to beat, last year, so what we think will be better than last year is the drilling side, because it was just the shits last year, so—just to put it blunt, but pipeline side will be—this is project-related, so coming right out of the chute, right out of the chute. What did BC Government do? BC Government said you can't go on to these job sites unless you have a COVID action plan, and you got this, so they shut the projects down until February, so now that doesn’t—all that does is push the project out. It doesn't cancel the project. It just shifts it, so that's why I'm saying to you, it’s—I don't know how smooth it’s going to go, and now we've got massively cold weather, but you can't do these projects right now. It's just too freaking cold, so—but once we get into the spring and the summer, I think we'll hit our full stride again and get some real productivity done.

JEFF FETTERLY:

Second thing; back in the December call you mentioned Flat Deck had been underperforming in 2020. What have you seen on that? Any improvements?

MURRAY K. MULLEN:

Very good point. Very good point. I didn't highlight on that, but I think I touched around the bases on it, Jeff, when I say the Canadian economy is not growing. The consumer part of the economy is okay, but anything to do with capital investment, and which would translate into move for our Flat Deck business, it's stubbornly quiet, and it remains that way today. That's the biggest underperformer in our Trucking Logistics—in our Logistics and Warehousing segment. That's problematic, and until we see capital going to work, then I think our Flat Deck business will underperform. Once capital goes to work, wow, that’s—we're going to be in great position, but you need to see the capital go to work in the country, and I haven't seen that catalyst for that to happen yet.

JEFF FETTERLY:

Thanks for the colour. Appreciate it.

MURRAY K. MULLEN:

Thanks, Jeff. Take care.

OPERATOR:

Our next question comes from Konark Gupta with Scotiabank. Please go ahead.

KONARK GUPTA:

Thanks. Just a quick follow-up, Murray. Back in December when you provided the 2021 business outlook, you guys were expecting in the business plan a roughly—each segment will be roughly a third, a third, a third, with, perhaps, LTL maybe slightly bigger than a third, and S&I smaller than a third. Given what you have said today, is it still kind of fair to expect those kind of ratios, and perhaps maybe a slightly greater skew toward S&I here, given the drilling activities rebounding, or would you say—what you disclosed (inaudible 61:00).

MURRAY K. MULLEN:

No. I think I'll stay with a third, a third, a third. We need to see—we've given you kind of some green shoots that we think would happen, but I still think LTL is solid. That's probably not going to change a whole bunch. I think Logistics and Warehousing will be probably fine after (audio interference 61:24) of the gate for the reasons we talked about. There's just bottlenecks in the bloody system. Maybe on the S&I, a little bit better, but there's not enough—I haven't seen enough of true conviction to go and really drill from the oil and gas companies yet. I still see M&A. I still see some things, so I'm going to stick with that original one of a third, a third, a third.

KONARK GUPTA:

Okay. Great. Thank you.

MURRAY K. 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 K. MULLEN:

Thanks, folks, for everything. Glad to put 2020 behind us. It was a year for—none of us will forget too soon. We have our work cut out this year, there's no doubt. The economy's going to be—probably have some spits and starts, and those kind of things, but—and then we're going to have our real work cut out to make sure we identify good acquisitions that can add value to our shareholders. That's my number one objective, and until we get to that, we're going to focus on costs and on margin improvement.

Thanks for joining us, and take care.

OPERATOR:

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