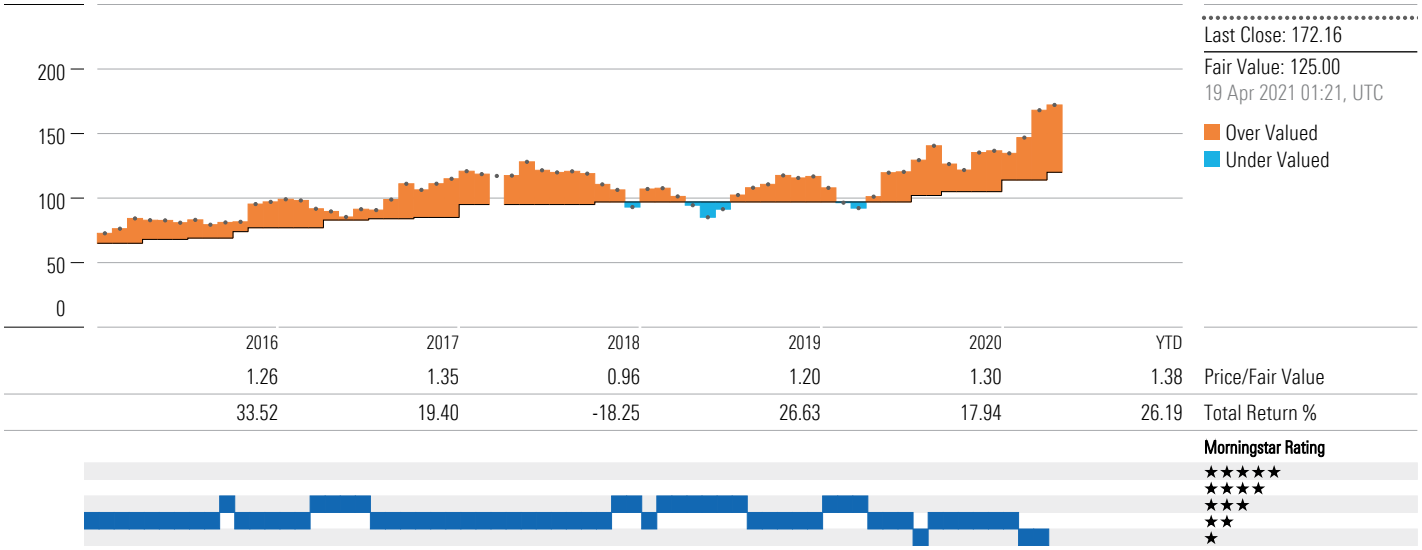
JB Hunt Transport Services Inc JBHT ★ 19 Apr 2021 01:24, UTC

Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Moat Trend™	Uncertainty	Capital Allocation
172.16 USD 16 Apr 2021	125.00 USD 19 Apr 2021 01:21, UTC	1.38	18.19 USD Bil 16 Apr 2021	Narrow	Stable	Medium	Standard

Price vs. Fair Value



Total Return % as of 16 Apr 2021. Last Close as of 16 Apr 2021. Fair Value as of 19 Apr 2021 01:21, UTC.

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J.B. Hunt's Q1 Pricing Surges; Intermodal Volume Again Pressured by Rail Congestion, but Improving

Analyst Note Matthew Young, CFA, Equity Analyst, 16 Apr 2021

Trucking and logistics giant J.B. Hunt posted a 15% jump in first-quarter revenue, ahead of our expected run rate as higher than anticipated rate gains for truck brokerage (ICS) and for-hire truckload (JBT) comfortably offset sluggish intermodal volumes. Container volume (down 3%) once again missed our forecast due to rail network congestion linked to the interplay of robust demand, equipment imbalances, and constrained driver supply for drayage, and winter storms made matters worse. That said, intermodal demand is otherwise quite strong thanks to tight truckload capacity and heavy retailer restocking, and volumes rose 4% year over year in March as rail congestion is slowly recovering. Those same factors are providing significant demand and pricing tailwinds for the other divisions as well, and JBT's "360box" trailer-capacity offering is gaining lots of traction.

Total operating margin improved 110 basis points to 7.9% on leverage from overall revenue growth (including accelerating contract rates), which was enough to offset surging driver costs, heavy IT investment, and COVID-19 expenses. Adjusted intermodal margins (excluding BNSF-related accruals last year) fell on decreased network fluidity and rising driver wages in the drayage operations, but we expect gradual improvement.

Revenue and margins for ICS, JBT, and Final Mile came in nicely ahead of our expectations, and management's commentary gave us more confidence in these segments' profit trajectory. We've been

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Sector
Industrials

Industry
Integrated Freight & Logistics

Business Description

J.B. Hunt Transport Services ranks among the top surface transportation companies in North America by revenue. Its primary operating segments are intermodal delivery, which uses the Class I rail carriers for the underlying line-haul movement (49% of sales in 2020); dedicated trucking services that provide customer-specific fleet needs (23); for-hire truckload (5%); heavy goods final-mile delivery (7%), and asset-light truck brokerage (17%).

conservative with our assumptions because these operations are evolving, while investing heavily, but we are comfortable raising our longer-term forecasts. Management tempered its targeted margin ranges for intermodal and JBT, but we've already been assuming intermodal wouldn't reach the previous goal given certain network velocity constraints may linger for years to come. We expect our model adjustments to boost our $120 fair value in the ballpark of 5%. The shares, however, continue to look rich.

Business Strategy & Outlook Matthew Young, CFA, Equity Analyst, 7 Apr 2021

At its core, J.B. Hunt is an intermodal marketing company--it contracts with the Class I railroads for the line-haul movement of its containers. It was one of the first truckload carriers to venture into intermodal shipping, forming a partnership with Burlington Northern Santa Fe in the West in 1990. Years later, it forged an agreement with Norfolk Southern in the East. Hunt is now the largest intermodal provider, with a 20%-plus share of a $22 billion-plus industry. The next-largest competitor is Hub Group, followed by Schneider National's intermodal division and XPO Logistics' intermodal unit. Intermodal makes up half of Hunt's total revenue.

Hunt isn't immune to downturns, but it's reduced its exposure to the more capital-intensive for-hire truckload business, which represents 30% of sales (including for-hire and dedicated-contract business) versus 60% in 2005. Furthermore, the firm has established a clear leadership position in intermodal shipping in terms of size and service capabilities, while also investing in asset-light truck brokerage and final-mile delivery.

The 2018 capacity crunch in the competing truckload market reignited intermodal truck-to-rail conversion activity, particularly in Eastern U.S. corridors. That said, the crunch dissipated and TL rates corrected sharply in 2019, driving down intermodal's value proposition relative to trucking. Thus, 2019 was a hangover year and fallout from pandemic lockdowns further pressured container volume into early 2020. However, truckload capacity has since tightened drastically, contract pricing is on the rise across all modes, and underlying intermodal demand is rebounding sharply on the spike in retail goods consumption (intermodal cargo is mostly consumer goods) and heavy retailer restocking. Hunt is grappling with near-term rail-network congestion that's constraining volume, but that should ease as 2021 progresses. We expect 2.5%-3.0% U.S. retail sales growth and conversion trends to support 3.0%-3.5% industry container volume expansion longer term, with 2.0%-2.5% pricing gains on average, though Hunt's intermodal unit should modestly outperform those trends given its favorable competitive positioning.

Bulls Say Matthew Young, CFA, Equity Analyst, 18 Apr 2021

- Intermodal shipping enjoys favorable long-term trends, including secular constraints on truckload capacity growth and shippers' efforts to minimize transportation costs through mode conversions (truck

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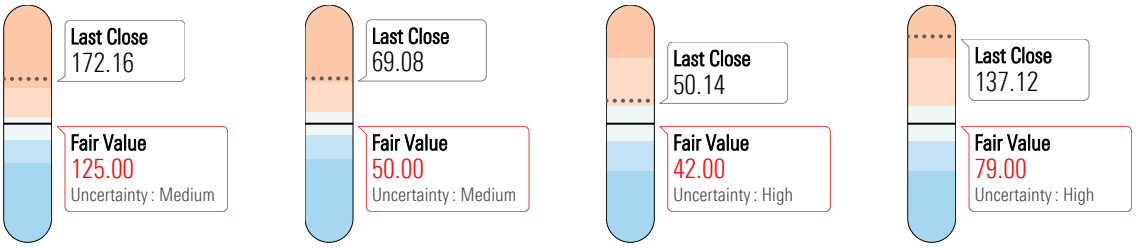
Competitors



	JB Hunt Transport Services Inc JBHT	Hub Group Inc Class A HUBG	Knight-Swift Transportation Holdings Inc A KNX	XPO Logistics Inc XPO
Economic Moat	Narrow	Narrow	None	None
Moat Trend	Stable	Stable	Stable	Stable
Currency	USD	USD	USD	USD
Fair Value	125.00 19 Apr 2021 01:21, UTC	50.00 8 Apr 2021 20:45, UTC	42.00 11 Mar 2021 18:42, UTC	79.00 22 Feb 2021 21:00, UTC
1-Star Price	168.75	67.50	65.10	122.45
5-Star Price	87.50	35.00	25.20	47.40
Assessment	Significantly Over Valued 18 Apr 2021	Significantly Over Valued 18 Apr 2021	Over Valued 18 Apr 2021	Significantly Over Valued 18 Apr 2021
Morningstar Rating	★19 Apr 2021 01:24, UTC	★16 Apr 2021 21:21, UTC	★★16 Apr 2021 21:21, UTC	★16 Apr 2021 21:21, UTC
Analyst	Matthew Young, Equity Analyst	Matthew Young, Equity Analyst	Matthew Young, Equity Analyst	Matthew Young, Equity Analyst
Capital Allocation	Standard	Standard	Standard	Standard
Price/Fair Value	1.38	1.38	1.19	1.74
Price/Sales	1.84	0.66	1.83	0.86
Price/Book	6.68	2.05	1.41	5.65
Price/Earning	33.56	31.54	20.89	175.79
Dividend Yield	0.63%	—	0.64%	—
Market Cap	18.19 Bil	2.38 Bil	8.30 Bil	15.31 Bil
52-Week Range	95.30—178.40	37.00—70.29	34.58—50.63	55.81—138.32
Investment Style	Mid Core	Small Core	Mid Value	Mid Core

to rail).

- We believe intermodal market share in the Eastern U.S. is still relatively low, suggesting decent growth potential via share gains from shorter-haul trucking.
- J.B. Hunt's asset-light truck brokerage operations are benefiting from solid execution and branch expansion. It's also moving very quickly in terms of boosting back office and carrier sourcing automation.

Bears Say Matthew Young, CFA, Equity Analyst, 18 Apr 2021

- The firm's intermodal and trucking divisions currently face heightened demand uncertainty stemming from economic fallout linked to COVID-19 containment measures.
- The stubbornly limited driver pool is placing upward pressure on wages and recruiting costs in Hunt's intermodal drayage and for-hire and dedicated truckload units.
- In Hunt's core intermodal division, transportation costs and customer satisfaction depend heavily on the

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performance of the firm's partner Class I railroads, which can vary.

Economic Moat Matthew Young, CFA, Equity Analyst, 7 Apr 2021

Because the for-hire full-truckload industry can be a tough business in which to differentiate, our narrow moat rating for J.B. Hunt primarily stems from its intermodal shipping operations, which benefit from a combination of the network effect and scale-based cost advantage. In terms of scale, we think it would be difficult for a small competitor to replicate Hunt's vast in-house drayage capabilities (about 5,650 tractors) and fleet of more than 97,400 53-foot-high cube containers capable of double stacking--by far the largest in the industry. The firm's intermodal container fleet provides preferred access to rail capacity and would be costly to replicate. Preferred access is no small edge, given that the truck-versus-rail decision for shippers is heavily influenced by service levels (in addition to the cost gap). We think this is a key reason Hunt has outperformed its peers in terms of container volume growth over the years.

The concept of the network effect suggests that the value of a service becomes more powerful and tougher to replicate with more users. Within its core intermodal business, Hunt's large network of shippers and long-standing partnerships with major rail carriers reinforce a compelling value proposition and generate healthy barriers to entry because duplication by small providers with fewer resources would prove difficult. For shippers (customers), the firm's immense customer base affords significant buying power (greater rail capacity access and discounts), and its industry-leading container fleet acts as a highly valuable source of capacity.

From the perspective of the Class I rail carriers, Hunt is an attractive source of cargo because of its ability to aggregate fragmented demand across an immense pool of customers looking to capitalize on multimodal capabilities.

Fair Value and Profit Drivers Matthew Young, CFA, Equity Analyst, 18 Apr 2021

Following first quarter results, we are boosting our fair value estimate to $125 from $120. Revenue and margins for ICS, JBT, and Final Mile came in nicely ahead of our expectations, and management's commentary gave us more confidence in these segments' profit trajectory. We've been conservative with our assumptions because these operations are evolving, while investing heavily, but we are comfortable raising our longer-term forecasts.

The 2018 truckload capacity crunch drove strong pricing across Hunt's intermodal, trucking, and asset-light highway brokerage operations. However, capacity loosened materially in 2019 on slower U.S. economic growth (especially industrial end markets) and operating conditions softened, while Hunt's intermodal division grappled with with heightened truck competition. The pandemic pushed the hangover into early 2020, but freight demand has since surged off pandemic lows with help from heavy retailer inventory restocking driven by robust U.S. goods consumption.

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Overall, Hunt's total revenue grew 5% in 2020 despite the pandemic, thanks to a strong rebound in demand and pricing for the trucking and highway brokerage divisions. While intermodal demand bounced off pandemic lows, Hunt's container volume was constrained by rail network congestion and revenue fell 1.5%. Intermodal network imbalance, rising driver wages, and the need to outsource more drayage also tempered margins in 2020.

For 2021, we expect total revenue to rise 16% as heightened retailer restocking drives strong demand across all segments throughout the first half, and as intermodal network inefficiencies subside. We're also modeling 120 basis points of adjusted operating margin expansion, to 8.6%, on leverage from what we expect to be unusually healthy contract rate gains across the trucking and intermodal segments (aided by very tight truckload-market capacity) and as the firm brings more intermodal drayage activities back in house. We also look for intermodal container repositioning costs to ease and box turns to improve this year as Class I rail service and terminal throughput re-calibrates to strong demand levels. We think Hunt is capable of midcycle organic revenue growth in the ballpark of 5%-6%, reflecting 5%-6% growth for intermodal, 4%-5% for the dedicated and for-hire trucking segments, 5% for the final-mile delivery unit, and around 6% for the asset-light truck brokerage operations. Our fair value estimate also bakes in a midcycle EBIT margin of 9.0%-9.5%.

Risk and Uncertainty Matthew Young, CFA, Equity Analyst, 7 Apr 2021

As with all transportation providers, volume trends in J.B. Hunt's intermodal and trucking operations are subject to variability in U.S. macroeconomic conditions. Cyclical downturns in demand compress profitability because excess capacity normally drives providers to slash rates in an attempt to salvage asset utilization. Along those lines, COVID-19 disruption to U.S. economic conditions via lockdowns and restrictions brings elevated uncertainty to our intermodal, truckload, and truck brokerage volume and pricing assumptions.

Hunt's intermodal operations are subject to the service quality standards of its partner Class I rail carriers, which handle the underlying line-haul movement of the firm's containers. While the railroads have made significant infrastructure investments and vastly improved intermodal service options across the U.S. during the past decade, customer satisfaction is partly out of Hunt's control in this segment. This risk was evident throughout parts of 2018-19 due to railroads' intermodal scheduling tweaks linked to precision scheduled railroading initiatives which drove network congestion and sluggish train speeds.

Changes in diesel fuel costs are largely passed through to shippers in the form of surcharges. That said, asset-based truckers often see temporary margin benefits during periods of rapid fuel price declines, as it takes time to adjust fuel surcharge programs to shippers. The opposite tends to occur when fuel prices rise. Of note, low diesel fuel prices reduce the cost advantage of intermodal relative to trucking, especially on shorter-haul business under 1,000 miles. While the intermodal value proposition remains

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strong thanks to secular constraints on over-the-road truckload capacity, truck-to-rail conversion activity can decline in the short run when diesel fuel prices plummet rapidly.

Capital Allocation Matthew Young, CFA, Equity Analyst, 7 Apr 2021

We assign J.B. Hunt a Standard capital allocation rating, which reflects our overall assessment that the firm's balance sheet is healthy and that its investing (reinvestment and acquisitions) decisions have been reasonable and support its competitive positioning. We also think its shareholder distributions are appropriate.

Hunt's highly experienced senior leadership team has diversified the company's service portfolio and developed an industry-leading competency in intermodal shipping, while prudently allocating capital. Impressive execution has driven relatively consistent market share gains over the years, and improvement in the firm's consolidated operating ratio (expenses/revenue) from 95% in the late 1990s to roughly 91% on average during the past five years. Additionally, J.B. Hunt is expanding its presence in the fragmented asset-light highway brokerage industry, which offers market share opportunities for nimble providers that can capitalize on the power of the network effect. While pandemic disruption weighed on 2020 gross and operating margins, Hunt executed admirably in terms of penetrating the highly competitive highway brokerage landscape while boosting its level of transaction automation. Hunt is one of only a handful of traditional asset-based truckload carriers to accomplish this--others include Knight-Swift and Schneider National.

In early 2011, longtime CEO Kirk Thompson moved from president and CEO to board chairman. Previous chairman Wayne Garrison remains a director. Thompson had served as CEO since 1987, overseeing Hunt's transition from a traditional long-haul trucker to an intermodal specialist. Company veteran John Roberts III took the helm as president and CEO following more than a dozen years leading the dedicated contract services division. J.B. Hunt pays a quarterly dividend, which has increased annually over the past decade, and it has a long history of share repurchases.

Analyst Notes Archive

Underlying Freight Demand Robust in J.B. Hunt's Q4, but Rail Congestion Derails Intermodal Loads.

Matthew Young, CFA, Equity Analyst, 20 Jan 2021

Trucking, intermodal and logistics giant J.B. Hunt's fourth-quarter revenue rose 12% year over year, slightly below our expectations. Total top-line growth accelerated nicely, but container volumes in the flagship intermodal division missed our forecast on continued rail network congestion linked to the interplay of robust demand, equipment imbalances, and constrained driver supply for drayage services. The firm otherwise posted strong growth in the highway brokerage, final mile, and legacy full-truckload shipping (JBT) units. Freight demand has surged off initial pandemic lows, with a massive boost from heavy retailer restocking rooted in the remarkable spike in U.S. retail goods consumption. On top of that,

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truckload-capacity has tightened drastically, driving up spot rates and setting the stage for strong contract rate gains in 2021 for all Hunt's segments, including intermodal.

Total operating margin fell 80 basis points to 7.6%; not far off our expectations given a solid showing in highway brokerage and truckload segment margins. That said, intermodal margins weren't stellar, falling 150 basis points year over year on lost productivity and high repositioning costs from heavy rail-network congestion, especially on the West Coast. Also, driver availability issues forced Hunt to use more-expensive third-party drayage capacity at terminals.

Management is optimistic that easing network congestion and contract-pricing tailwinds (double-digit gains are possible) in 2021 will allow intermodal to progress toward its 11%-plus target, and we concur. That said, given network inefficiencies are severely restricting load growth and productivity (despite robust underlying demand), we think the stock could see slight selling pressure at market open as investors might temper their first-half EPS forecasts. Even so, we expect to raise our $105 fair value estimate in the ballpark of 3%-5% on the time value of money and lifting our longer-term JBT margin forecasts.

J.B. Hunt's Q3 Intermodal Demand Rebounds, but Rail Congestion Tempers Volume Gains and Margins Matthew Young, CFA, Equity Analyst, 16 Oct 2020

Diversified trucking and logistics giant J.B. Hunt's third-quarter revenue increased about 4.5%, slightly ahead of our expectations and much better than the 5% year-over-year decline posted last quarter during the height of pandemic-driven demand disruption. Most segments saw strong sequential load-volume recovery as lockdowns eased and given the remarkable bounce in U.S. retail goods sales (heavy retailer restocking), particularly for truck brokerage and the flagship intermodal division.

While up sequentially, intermodal revenue fell 2% year over year on lower fuel surcharges and flattish core pricing, partly offset by 2% higher container volume. Pricing was already soft prior to the pandemic because of heavy competition from the truckload sector, and during the quarter the firm restrained from chasing higher-priced opportunities to honor its capacity commitments amid constrained capacity. That said, we expect the upcoming bidding season to prove favorable as capacity across the trucking and intermodal markets should stay constrained, giving the firm more rate leverage. Management noted that intermodal load volume would have been materially higher if not for heavy rail-terminal congestion, which pressured network velocity, thus forcing Hunt to turn loads.

Adjusted EBIT margin fell a disappointing 190 basis points, to 7.1%, which was below our forecast. The decline stems in large part from intermodal network inefficiencies and higher costs driven by rail congestion, especially at terminals. Rising driver wages and lower truck brokerage gross profit margins

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(net revenue/gross revenue) also contributed.

Although rail congestion may constrain intermodal volume gains in the quarters ahead, we continue to expect an overall growth rebound in 2021 across all segments, also including the dedicated, final mile, and brokerage operations. We tweaked our 2020 margin forecast lower, but we don't expect to materially alter our $105 fair value estimate.

Demand Disruption in Full Force During J.B. Hunt's 2Q, but Intermodal Trends Likely Bottomed

Matthew Young, CFA, Equity Analyst, 17 Jul 2020

Narrow-moat intermodal specialist J.B. Hunt's second-quarter revenue swung to a 5% year-over-year decline. As we expected, pandemic-related disruption appeared in full force, hitting load volumes across the intermodal and truck brokerage operations. On a positive note, intermodal volumes (down 2%) outperformed the broader marketplace (down high single digits), pointing to share gains, and the intermodal and truckload shipping segments saw a "steady rebound" in May and June as the economy started reopening--a trend noted by other transports that have reported. Visibility into the second half remains quite low, but this is a good development. Intermodal volume fell 6% and 4% in April and May, but was up 5% in June (year over year). Revenue growth came in ahead of our forecast on better-than-expected intermodal loads.

Despite good cost control and IT-enabled efficiency gains, Hunt's profitability cannot hide from falling volume and COVID-19-related costs, and its adjusted EBITDA margin fell 130 basis points to 8.2%. That said, EBIT margins came in ahead of our expected run rate thanks to low driver turnover (in drayage) and good management of box positioning in intermodal, partly offset by sluggish gross margins in the highway brokerage unit.

While our midcycle model assumptions remain intact, we expect to boost our $97 fair value by around 5% due to raising our near-term revenue and margins forecasts, and the time value of money. Note we are baking in a recovery in 2021, with revenue rising in the mid to high single digits, which carries risk. Management once again did not offer guidance given ultra-low visibility. Overall, the shares are trading in modestly overvalued territory relative to our long-term expectations for revenue, profitability, and free cash flow growth. This is likely due in part to Hunt's excellent track record of execution and the potential for strong EPS growth next year should the U.S. economy continue to open up and demand recovers.

J.B. Hunt Posts First-Quarter Revenue Growth, but COVID-19 Disruption Will Derail That Trend

Matthew Young, CFA, Equity Analyst, 15 Apr 2020

Narrow-moat intermodal specialist J.B. Hunt's top line increased 10% year over year, excluding fuel, in the first quarter, slightly ahead of our forecast, as COVID-19 disruption didn't really creep in until the

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Last Price	Fair Value Estimate	Price/FVE	Market Cap	Economic Moat™	Moat Trend™	Uncertainty	Capital Allocation
172.16 USD 16 Apr 2021	125.00 USD 19 Apr 2021 01:21, UTC	1.38	18.19 USD Bil 16 Apr 2021	Narrow	Stable	Medium	Standard

end of March. Relative to the same period last year, the increase stems from previous business wins, along with a spike in truckload shipping demand midquarter--food and beverage and household goods restocking surged as consumers stocked up on essentials amid nationwide lockdowns. That said, intermodal volume began to deteriorate by the end of March as the impact of government containment measures began to weigh on retail and industrial end markets. While the firm has been able to reposition dedicated-truckload equipment to customers that need capacity, we think Hunt's full-truckload and truck brokerage (ICS) operations are seeing roughly the same demand deterioration of late. The impact of COVID-19 disruption will be much more evident in the second quarter for J.B. Hunt and its intermodal, brokerage, and truckload peers.

Before the earnings release, we had already tempered our forecasts to account for COVID-19 disruption. Thus, we don't expect to materially alter our $97 fair value estimate. Despite high macroeconomic uncertainty and the broader market sell-off, J.B. Hunt's shares have held up well. In fact, the stock is trading in fairly valued territory, likely due in part to its track record of strong execution and solid ability to weather the current storm, including a healthy balance sheet.

Big picture, 2019 was already a challenging year for the intermodal and trucking industries, as they emerged from an unusually robust backdrop in 2018. COVID-19 headwinds will make for another tough year in 2020 as a likely heavy pullback in U.S. economic growth will probably drag down freight demand into at least the third quarter. We are baking in a recovery throughout 2021 and 2022, though the risk of a prolonged recession hasn't disappeared.

Heavy IT Investment and Rising Rail Capacity Costs Pressure J.B. Hunt's Fourth-Quarter Margins

Matthew Young, CFA, Equity Analyst, 17 Jan 2020

Narrow-moat intermodal specialist J.B. Hunt (along with its peers) grappled with a hangover throughout 2019 as it emerged from an incredibly robust operating backdrop in 2018 that benefited from the unprecedented truckload-industry capacity crunch and related pricing surge across the trucking, logistics, and intermodal markets. Additionally, industrial end markets have slowed. Continuing the theme, fourth-quarter top-line trends across the firm's operations were mostly sluggish but not far off our expectations. Profitability, on the other hand, did fall short of our forecast. In general, Hunt's total EBIT margin is facing incremental pressure from rail purchased-transportation cost increases amid a soft intermodal backdrop, lower truck-brokerage gross margins, and elevated IT spend. Since our midcycle forecasts remain mostly intact, we don't expect to materially alter our $97 fair value estimate. At about $113, the shares are modestly overvalued relative to our long-term expectations for free cash flow generation.

Intermodal revenue came in flat as container volume flipped slightly positive (+1.6%) on new awards but was offset by a 1.2% drop in revenue per load, which swung negative as we expected. Intermodal is grappling with heavy competition from depressed rates in the competing full-truckload industry and

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lingering pressure from rail service adjustments. Difficult comparisons, scant spot activity, and loose market capacity weighed on the for-hire truckload and asset-light truck brokerage operations (ICS). We note that on top of competitive pricing pressure, Hunt's brokerage segment is investing heavily in digital freight matching platforms, which helped drive operating losses in the second half. Overall, J.B. Hunt and its diversified trucking and logistics peers will face a tough operating backdrop through the first half of 2020 due to moderating U.S. economic growth, tough pricing comparisons, and loose truckload market capacity.

J.B. Hunt Grappling with Near-Term Intermodal and Trucking Market Hangover Matthew Young, CFA, Equity Analyst, 16 Oct 2019

Narrow-moat intermodal specialist J.B. Hunt is amid a hangover this year as it emerges from an incredibly robust backdrop in 2018 that benefited from the truckload-industry capacity crunch and related pricing surge across the trucking, logistics, and intermodal markets. We also believe inventory levels among retail shippers remain elevated, pressuring restocking activity and overall freight demand. Third-quarter results across most of Hunt's operations were thus uninspiring, though we found no major surprises. Intermodal revenue increased year over year, but was still sluggish thanks to softening pricing conditions and competition from depressed rates in the competing trucking industry, while difficult comparisons, scant spot activity, and loose market capacity weighed on the for-hire truckload and asset-light truck brokerage operations. Of note, on top of intensifying competitive pricing pressure, Hunt's truck brokerage segment is investing heavily in its digital freight matching platforms, which helped push the segment to an operating loss in the quarter.

J.B. Hunt and its diversified trucking and logistics peers will face a tough operating backdrop this year and into the first half of 2020 due to moderating U.S. economic growth, tough comparisons, and excess truckload capacity. Further the firm's flagship intermodal operations have grappled with incremental volume pressure linked to the Class-I rails' precision railroading efforts that often disrupt service. That said, these headwinds are generally not permanent. We look for more favorable operating trends to emerge by the second half of next year, particularly because we expect truckload-market supply and demand to reach a more balanced state, which should allow rates to find their footing. Overall, we don't expect to alter our DCF-derived $97 fair value estimate. At $112, the shares are trading in modestly overvalued territory relative to our long-term expectations for free cash flow generation.

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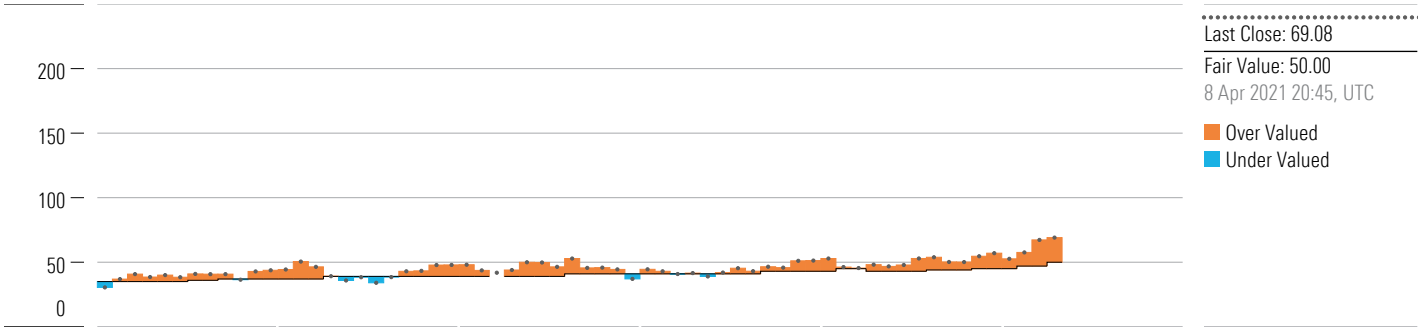
Competitors Price vs. Fair Value

Hub Group Inc Class A HUBG



Last Close: 69.08

Fair Value: 50.00

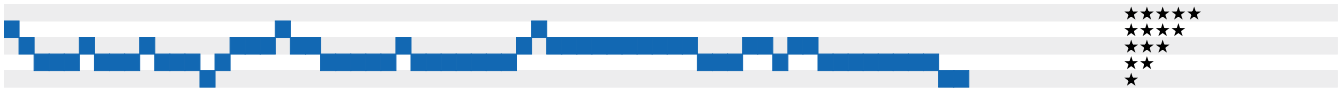
8 Apr 2021 20:45, UTC

Over Valued

Under Valued

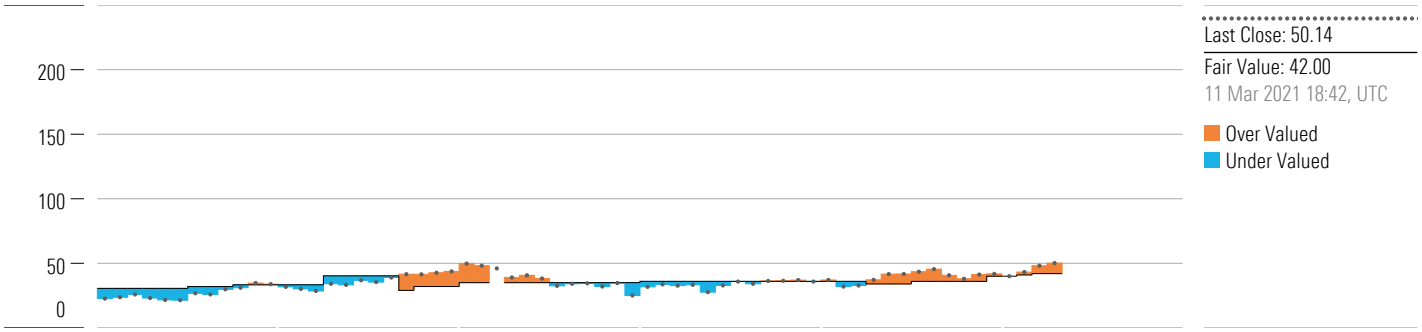
	2016	2017	2018	2019	2020	YTD
Price/Fair Value	1.18	1.23	0.90	1.19	1.27	1.38
Total Return %	32.78	9.49	-22.61	38.36	11.13	21.19

Morningstar Rating



Total Return % as of 16 Apr 2021. Last Close as of 16 Apr 2021. Fair Value as of 8 Apr 2021 20:45, UTC.

Knight-Swift Transportation Holdings Inc A KNX



Last Close: 50.14

Fair Value: 42.00

11 Mar 2021 18:42, UTC

Over Valued

Under Valued

	2016	2017	2018	2019	2020	YTD
Price/Fair Value	1.02	1.37	0.72	1.00	1.05	1.19
Total Return %	78.00	30.14	-42.11	43.92	17.58	20.09

Morningstar Rating

Total Return % as of 16 Apr 2021. Last Close as of 16 Apr 2021. Fair Value as of 11 Mar 2021 18:42, UTC.

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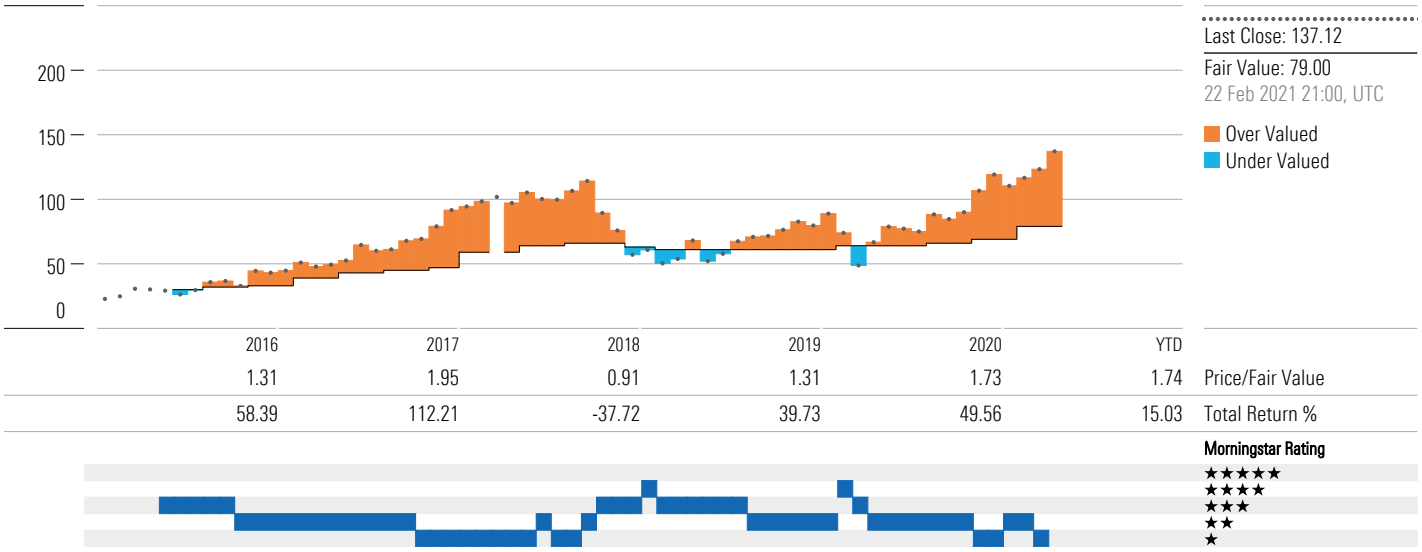
XPO Logistics Inc XPO



Total Return % as of 16 Apr 2021. Last Close as of 16 Apr 2021. Fair Value as of 22 Feb 2021 21:00, UTC.

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16 Apr 2021	19 Apr 2021 01:21, UTC		16 Apr 2021				

Morningstar Historical Summary

Financials as of 31 Dec 2020

Fiscal Year, ends 31 Dec	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	YTD	TTM
Revenue (USD Mil)	4,527	5,055	5,585	6,165	6,188	6,555	7,190	8,615	9,165	9,637	9,637	9,637
Revenue Growth %	19.3	11.7	10.5	10.4	0.4	5.9	9.7	19.8	6.4	5.1	5.1	5.1
EBITDA (USD Mil)	658	759	830	926	1,055	1,083	1,008	1,117	1,235	1,241	1,241	1,241
EBITDA Margin %	14.5	15.0	14.9	15.0	17.1	16.5	14.0	13.0	13.5	12.9	12.9	12.9
Operating Income (USD Mil)	444	530	577	632	716	721	624	681	734	713	713	713
Operating Margin %	9.8	10.5	10.3	10.2	11.6	11.0	8.7	7.9	8.0	7.4	7.4	7.4
Net Income (USD Mil)	257	310	342	375	427	432	686	490	516	506	506	506
Net Margin %	5.7	6.1	6.1	6.1	6.9	6.6	9.6	5.7	5.6	5.3	5.3	5.3
Diluted Shares Outstanding (Mil)	122	120	119	118	117	113	111	110	108	107	107	107
Diluted Earnings Per Share (USD)	2.11	2.59	2.87	3.16	3.66	3.81	6.18	4.43	4.77	4.74	4.74	4.74
Dividends Per Share (USD)	0.52	0.71	0.45	0.80	0.84	0.88	0.92	0.96	1.04	1.08	1.08	1.08

Valuation as of 31 Mar 2021

	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Recent Qtr	TTM
Price/Sales	1.3	1.4	1.7	1.7	1.4	1.7	1.9	1.2	1.4	1.6	1.9	1.9
Price/Earnings	23.0	23.0	27.6	28.1	20.5	25.7	30.7	13.1	27.7	29.4	35.5	35.5
Price/Cash Flow	9.5	13.1	17.1	15.4	10.1	12.9	16.1	10.2	10.2	13.6	16.0	16.0
Dividend Yield %	1.15	0.95	0.78	0.95	1.15	0.91	0.8	1.03	0.89	0.79	0.65	0.65
Price/Book	10.6	8.9	9.2	8.5	6.7	7.8	8.6	4.9	5.7	5.8	6.8	6.8
EV/EBITDA	9.2	10.1	11.7	11.5	8.9	10.9	13.6	10.0	11.0	12.4	0.0	0.0

Operating Performance / Profitability as of 31 Dec 2020

Fiscal Year, ends 31 Dec	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	YTD	TTM
ROA %	12.2	13.1	13.0	12.1	12.2	11.4	16.3	10.3	9.8	8.9	8.9	8.9
ROE %	45.1	45.7	38.0	33.8	34.1	31.8	42.2	24.9	23.6	20.8	20.8	20.8
ROIC %	21.6	23.3	22.3	20.3	21.2	19.1	26.4	16.2	17.0	14.5	14.5	14.5
Asset Turnover	2.1	2.1	2.1	2.0	1.8	1.7	1.7	1.8	1.7	1.7	1.7	1.7

Financial Leverage

Fiscal Year, ends 31 Dec	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	Recent Qtr	TTM
Debt/Capital %	55.2	42.5	31.2	36.2	43.4	41.1	37.1	30.0	36.4	33.4	33.4	—
Equity/Assets %	25.0	32.1	35.9	35.7	35.8	35.8	41.2	41.3	41.4	43.9	43.9	—
Total Debt/EBITDA	1.1	0.9	0.9	1.0	0.9	0.9	1.1	1.0	1.0	1.1	1.1	—
EBITDA/Interest Expense	23.1	29.7	35.8	34.3	41.3	42.8	35.0	27.6	22.6	26.1	26.1	26.1

Morningstar Analyst Historical/Forecast Summary as of 16 Apr 2021

Financials

Fiscal Year, ends 31 Dec	2019	2020	Estimates 2021	2022	2023
Revenue (USD Mil)	9,165	9,637	11,133	11,915	12,521
Revenue Growth %	6.4	5.1	15.5	7.0	5.1
EBITDA (USD Mil)	1,253	1,260	1,520	1,732	1,857
EBITDA Margin %	13.7	13.1	13.7	14.5	14.8
Operating Income (USD Mil)	734	713	961	1,140	1,235
Operating Margin %	8.0	7.4	8.6	9.6	9.9
Net Income (USD Mil)	531	521	690	830	907
Net Margin %	5.8	5.4	6.2	7.0	7.2
Diluted Shares Outstanding (Mil)	108	107	106	105	103
Diluted Earnings Per Share(USD)	4.91	4.88	6.50	7.91	8.79
Dividends Per Share(USD)	1.04	1.08	1.12	1.17	1.22

Forward Valuation

	2019	2020	Estimates 2021	2022	2023
Price/Sales	1.4	1.5	1.6	1.5	1.5
Price/Earnings	23.8	28.0	26.5	21.8	19.6
Price/Cash Flow	30.2	27.7	432.1	35.3	23.3
Dividend Yield %	0.89	0.79	0.65	0.68	0.71
Price/Book	—	—	—	—	—
EV/EBITDA	10.9	12.2	12.5	10.9	10.2

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Research Methodology for Valuing Companies

Overview

At the heart of our valuation system is a detailed projection of a company's future cash flows, resulting from our analysts' research. Analysts create custom industry and company assumptions to feed income statement, balance sheet, and capital investment assumptions into our globally standardized, proprietary discounted cash flow, or DCF, modeling templates. We use scenario analysis, indepth competitive advantage analysis, and a variety of other analytical tools to augment this process. Moreover, we think analyzing valuation through discounted cash flows presents a better lens for viewing cyclical companies, high-growth firms, businesses with finite lives (e.g., mines), or companies expected to generate negative earnings over the next few years. That said, we don't dismiss multiples altogether but rather use them as supporting cross-checks for our DCF-based fair value estimates. We also acknowledge that DCF models offer their own challenges (including a potential proliferation of estimated inputs and the possibility that the method may miss shortterm market-price movements), but we believe these negatives are mitigated by deep analysis and our longterm approach.

Morningstar's equity research group ("we," "our") believes that a company's intrinsic worth results from the future cash flows it can generate. The Morningstar Rating for stocks identifies stocks trading at a discount or premium to their intrinsic worth—or fair value estimate, in Morningstar terminology. Five-star stocks sell for the biggest risk adjusted discount to their fair values, whereas 1-star stocks trade at premiums to their intrinsic worth.

Four key components drive the Morningstar rating: (1) our assessment of the firm's economic moat, (2) our estimate of the stock's fair value, (3) our uncertainty around that fair value estimate and (4) the current market price. This process ultimately culminates in our singlepoint star rating.

1. Economic Moat

The concept of an economic moat plays a vital role not only in our qualitative assessment of a firm's long-term investment potential, but also in the actual calculation of our fair value estimates. An economic moat is a structural feature that allows a firm to sustain excess profits over a long period of time. We define economic profits as returns on invested capital (or ROIC) over and above our estimate of a firm's cost of capital, or weighted average cost of capital (or WACC). Without a moat, profits are more susceptible to competition. We have identified five sources of economic moats: intangible assets, switching costs, network effect, cost advantage, and efficient scale.

Companies with a narrow moat are those we believe are more likely than not to achieve normalized excess returns for at least the next 10 years. Wide-moat companies are those in which we have very high confidence that excess returns will remain for 10 years, with excess returns more likely than not to remain for at least 20 years. The longer a firm generates economic profits, the higher its intrinsic value. We believe low-quality, no-moat companies will see their normalized returns gravitate toward the firm's cost of capital more quickly than companies with moats.

When considering a company's moat, we also assess whether there is a substantial threat of value destruction, stemming from risks related to ESG, industry disruption, financial health, or other idiosyncratic issues. In this context, a risk is considered potentially value destructive if its occurrence would eliminate a firm's economic profit on a cumulative or midcycle basis. If we deem the probability of occurrence sufficiently high, we would not characterize the company as possessing an economic moat.

To assess the sustainability of excess profits, analysts perform ongoing assessments of the moat trend. A firm's moat trend is positive in cases where we think its sources of competitive advantage are growing stronger; stable where we don't anticipate changes to competitive advantages over the next several years; or negative when we see signs of deterioration.

2. Estimated Fair Value

Combining our analysts' financial forecasts with the firm's economic moat helps us assess how long returns on invested capital are likely to exceed the firm's cost of capital. Returns of firms with a wide economic moat rating are assumed to fade to the perpetuity period over a longer period of time than the returns of narrow-moat firms, and both will fade slower than no-moat firms, increasing our estimate of their intrinsic value.

Our model is divided into three distinct stages:

Stage I: Explicit Forecast

In this stage, which can last five to 10 years, analysts make full financial statement forecasts, including items such as revenue, profit margins, tax rates, changes in workingcapital accounts, and capital spending. Based on these projections, we calculate earnings before interest, after taxes (EBI) and the net new investment (NNI) to derive our annual free cash flow forecast.

Stage II: Fade

The second stage of our model is the period it will take the company's return on new invested capital—the return on capital of the next dollar invested ("RONIC")—to decline (or rise) to its cost of capital. During the Stage II period, we use a formula to approximate cash flows in lieu of explicitly modeling the income statement, balance sheet, and cash flow statement as we do in Stage I. The length of the second stage depends on the strength of the company's economic moat. We forecast this period to last anywhere from one year (for companies with no economic moat) to 10–15 years or more (for wide-moat companies). During this period, cash flows are forecast using four assumptions: an average growth rate for EBI over the period, a normalized investment rate, average return on new invested capital (RONIC), and the number of years until perpetuity, when excess returns cease. The investment rate and return on new invested capital decline until a perpetuity value is calculated. In the case of firms that do not earn their cost of capital, we assume marginal ROICs rise to the firm's cost of capital (usually attributable to less reinvestment), and we may truncate the second stage.

Stage III: Perpetuity

Once a company's marginal ROIC hits its cost of capital, we calculate a continuing value, using a standard perpetuity formula. At perpetuity, we assume that any growth or decline or investment in the business neither creates nor destroys value and that any new investment provides a return in line with estimated WACC.

Because a dollar earned today is worth more than a dollar earned tomorrow, we discount our projections of cash flows in stages I, II, and III to arrive at a total present value of expected future cash flows. Because we are modeling free cash flow to the firm—representing cash available to provide a return to all capital providers—we discount future cash flows using the WACC, which is a weighted average of the costs of equity, debt, and preferred stock (and any other funding sources), using expected future proportionate long-term, market-value weights.

3. Uncertainty Around That Fair Value Estimate

Morningstar's Uncertainty Rating captures a range of likely potential intrinsic values for a company and uses it to assign the margin of safety required before investing, which in turn explicitly drives our stock star rating system. The Uncertainty Rating represents the analysts' ability to

Morningstar Equity Research Star Rating Methodology

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bound the estimated value of the shares in a company around the Fair Value Estimate, based on the characteristics of the business underlying the stock, including operating and financial leverage, sales sensitivity to the overall economy, product concentration, pricing power, exposure to material ESG risks, and other company-specific factors.

Analysts consider at least two scenarios in addition to their base case: a bull case and a bear case. Assumptions are chosen such that the analyst believes there is a 25% probability that the company will perform better than the bull case, and a 25% probability that the company will perform worse than the bear case. The distance between the bull and bear cases is an important indicator of the uncertainty underlying the fair value estimate. In cases where there is less than a 25% probability of an event, but where the event could result in a material decline in value, analysts may adjust the uncertainty rating to reflect the increased risk. Analysts may also make a fair value adjustment to reflect the impact of this event.

Our recommended margin of safety widens as our uncertainty of the estimated value of the equity increases. The more uncertain we are about the estimated value of the equity, the greater the discount we require relative to our estimate of the value of the firm before we would recommend the purchase of the shares. In addition, the uncertainty rating provides guidance in portfolio construction based on risk tolerance.

Our uncertainty ratings for our qualitative analysis are low, medium, high, very high, and extreme.

Qualitative Analysis Uncertainty Ratings	Margin of Safety ★★★★★Rating	Margin of Safety ★Rating
Low	20% Discount	25% Premium
Medium	30% Discount	35% Premium
High	40% Discount	55% Premium
Very High	50% Discount	75% Premium
Extreme	75% Discount	300% Premium

4. Market Price

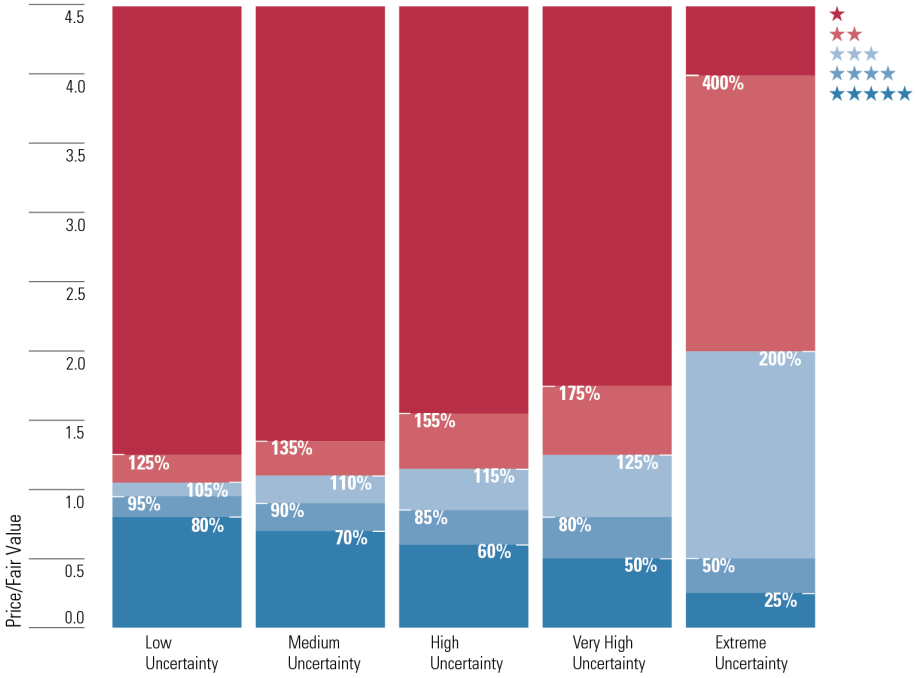
The market prices used in this analysis and noted in the report come from exchange on which the stock is listed which we believe is a reliable source.

For more details about our methodology, please go to https://shareholders.morningstar.com.

Morningstar Star Rating for Stocks

Once we determine the fair value estimate of a stock, we compare it with the stock's current market price on a daily basis, and the star rating is automatically re-calculated at the market close on every day the market on which the stock is listed is open. Our analysts keep close

Morningstar Equity Research Star Rating Methodology



tabs on the companies they follow, and, based on thor ough and ongoing analysis, raise or lower their fair value estimates as warranted.

Please note, there is no predefined distribution of stars. That is, the percentage of stocks that earn 5 stars can fluctuate daily, so the star ratings, in the aggregate, can serve as a gauge of the broader market's valuation. When there are many 5-star stocks, the stock market as a whole is more undervalued, in our opinion, than when very few companies garner our highest rating.

We expect that if our base-case assumptions are true the market price will converge on our fair value estimate over time generally within three years (although it is impossible to predict the exact time frame in which market prices may adjust).

Our star ratings are guideposts to a broad audience and individuals must consider their own specific investment goals, risk tolerance, tax situation, time horizon, income needs, and complete investment portfolio, among other factors.

The Morningstar Star Ratings for stocks are defined below:

★★★★★ We believe appreciation beyond a fair risk adjusted return is highly likely over a multiyear time frame. Scenario analysis developed by our analysts indicates that the current market price represents an excessively pessimistic outlook, limiting downside risk and maximizing upside potential.

★★★★ We believe appreciation beyond a fair risk-adjusted return is likely.

★★★ Indicates our belief that investors are likely to receive a fair risk-adjusted return (approximately cost of equity).

★★ We believe investors are likely to receive a less than fair risk-adjusted return.

★ Indicates a high probability of undesirable risk-adjusted returns from the current market price over a multiyear time frame, based on our analysis. Scenario analysis by our analysts indicates that the market is pricing in an excessively optimistic outlook, limiting upside potential and leaving the investor exposed to Capital loss.

Other Definitions

Last Price: Price of the stock as of the close of the market of the last trading day before date of the report.

Capital Allocation Rating: Our Capital Allocation (or Stewardship) Rating represents our assessment of the quality of management's capital allocation, with particular emphasis on the firm's balance sheet, investments, and shareholder distributions. Analysts consider companies' investment strategy and valuation, balance sheet management, and dividend and share buyback policies. Corporate governance factors are only considered if they are likely to materially impact shareholder value, though either the balance sheet, investment, or shareholder distributions. Analysts assign one of three ratings: "Exem-

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Capital Allocation (or Stewardship) analysis published prior to Dec. 9, 2020, was determined using a different process. Beyond investment strategy, financial leverage, and dividend and share buyback policies, analysts also considered execution, compensation, related party transactions, and accounting practices in the rating.

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