

Covenant Logistics Group 4th Quarter 2025 Conference Call

Mr. Grant – Good morning everyone and welcome to the Covenant Logistics Group fourth quarter 2025 conference call. As a reminder:

This call will contain forward-looking statements under the Private Securities Litigation Reform Act, which are subject to risks and uncertainties that could cause actual results to differ materially. Please review our SEC filings and most recent risk factors. We undertake no obligation to publicly update or revise any forward-looking statements.

Our prepared comments and additional financial information are available on our website at www.covenantlogistics.com/investors.

Joining me today are CEO David Parker, President Paul Bunn and COO Dustin Koehl.

We're going to modify our opening comments from the usual format and address three key areas before covering the usual statistical and segment information: (1) our view on the freight market, (2) the equipment impairment charge and our capital plan, and (3) a small acquisition we made in the fourth quarter.

The Freight Market. We believe the freight market continues to evolve toward equilibrium between shippers and carriers. In fact, we might be at equilibrium now. During the fourth quarter, spot rates rose meaningfully. Revenue trends during the first three weeks of January have meaningfully improved compared to the prior year in all business units. We are also experiencing a sharp increase in bid activity with shippers who are interested in securing capacity contractually. Currently we have also secured a few low to mid-single digit rate increases that take effect during the first quarter within our Expedited fleet and anticipate additional increases across both Expedited and Dedicated to take effect early in the second quarter. Based on regulatory changes, cost inflation, and the amount of insurance and claims risk inherent in the industry, we would not be surprised for industry-wide driver and truck capacity to continue to decline, perhaps materially. At the same time, most trucking cycles are led by demand. In our view, inventory restocking, tax stimulus, and corporate earnings are biased in favor of improved demand.

Equipment Charge and Capital Plan. Operating a safe, fuel-efficient, late-model fleet requires constant cycling of equipment to keep operating costs down and driver satisfaction up. With intentional fleet reductions and declining used equipment values in 2025, we deferred some trades, stacked up deliveries, and have too much underutilized equipment. To improve our operations and balance sheet, we have moved a group of assets to "held for sale" status and lowered our expectation on disposition prices. Since our current sized asset-based fleet is not generating the desired return on capital, we will not replace all the units disposed. We expect a modestly smaller fleet at the end of 2026 and only \$40 million to \$50 million of net capex for the year. Within our asset-based fleets, we expect the agriculture related business within our Dedicated segment to grow and the other fleets serving more commoditized freight to shrink or remain stable through our weed and feed approach. Overall, our goal is to reduce balance sheet leverage and improve return on capital.

The Acquisition. During the fourth quarter, we acquired the assets of a small truckload brokerage business. The business, which we will operate under the name Star Logistics Solutions, has two niche customer bases: (i) state and federal government emergency management departments, which represents an episodic and highly profitable disaster response capability that scales quickly to address hurricanes and other natural disasters, and (ii) high-service consumer packaged goods companies, which affords leverage to general commodity freight market cycles that our asset-based truckload operations lack. With synergies, we expect Star to be accretive to earnings during the first half of 2026.

With that background, I will move on to the quarter's statistical review.

Year-over-year highlights for the quarter include:

- Consolidated freight revenue increased by 7.8% or approximately \$19.5 million to \$270.6 million.
- Consolidated adjusted operating income shrank by 39.4%, to \$10.9 million, primarily as a result of margin compression in our Expedited, Managed Freight and Warehousing segments, partially offset with improvement to Dedicated operating income within our Dedicated segment.
- Our net indebtedness as of December 31st increased by \$76.9 million to \$296.6 million compared to December 31, 2024, yielding an adjusted leverage ratio of approximately 2.3x and debt-to-capital ratio of 42.3%, as a result of executing our share repurchase program and acquisition related payments.
- The average age of our tractors at December 31st increased to 24 months, compared to 20 months a year ago as a result of year over year reductions to our high mileage Expedited fleet and growth in our less capital intensive Dedicated fleet.
- On an adjusted basis, return on average invested capital was 5.6% versus 8.1% in the prior year.

Now providing a little more color on the performance of the individual business segments:

- The Expedited segment reported an adjusted operating ratio of 97.2% for the quarter, a performance that did not meet our expectations, even in light of a softer freight environment. Results were partially impacted by the U.S. government shutdown, which persisted for nearly half of the quarter. Despite these external challenges, the segment did not perform to our operational standards. Accordingly, we will continue our disciplined approach to fleet optimization by reducing fleet size and focusing on higher-yield freight. Looking ahead, we anticipate fleet capacity will adjust modestly in response to market conditions. As the market improves, our strategic priorities remain enhancing margins through targeted rate increases, exiting less profitable business, and onboarding more profitable opportunities.
- Dedicated's 92.2% adjusted operating ratio was the best for any quarter during the year. We were pleased by how this segment improved its results each quarter throughout the year and are excited about the momentum we are taking with us into 2026. Dedicated grew the fleet by 90 average tractors or approximately 6.3% compared to the prior year, as we have continued to win new business in specialized and high-service niches within that segment. Going forward, we plan to focus our efforts on continuing to grow these high-service niches and reduce certain of our fleet that is exposed to more commoditized end markets where returns are not justified.
- Managed Freight experienced a significant improvement to freight revenue in the quarter as a result of the Star Logistics Solution acquisition that occurred in October, but margins were compressed as a result of the growing cost to secure quality brokerage capacity. Over the longer term, our strategy is to grow and diversify this segment. Given the asset light nature of this business, we note that an operating margin in the mid-single digits generates an acceptable return in capital given the asset-light nature of this segment.
- During the quarter, our Warehouse segment successfully launched operations with a key new customer, resulting in a 4.6% increase in freight revenue, or \$1.1 million, compared to the same period last year. However, adjusted operating income declined by \$1.6 million, primarily due to increased startup costs and operational inefficiencies associated with onboarding the new customer, as well as higher labor expenses, including overtime, at other warehouse locations to manage peak volume demands. Looking

ahead, we remain committed to driving organic growth within this segment and are focused on enhancing our operating income margin, with a target of reaching high single digits.

- Our minority investment in TEL contributed pre-tax net income of \$3.1 million for the quarter, compared to \$3.0 million in the prior year period. The impact of compressed leasing margins, soft used equipment market and incremental bad debt expense in the quarter placed continued pressure on TEL's pre-tax net income. Although TEL's overall business and balance sheet remains strong, exiting capacity from the general freight environment is expected to continue to impact them over the short term.

Regarding our outlook for the future:

We remain optimistic about improving freight fundamentals, our ability to be more efficient with our equipment and capture operating leverage and improve financial results in 2026. The improvements are likely to come later in the year, with the first quarter being impacted by seasonality, extreme weather, a still-developing freight market situation, and a potential margin squeeze in Managed Freight.

The last few years have been characterized by acquisitions, dispositions, and share buybacks as we have revamped the company. We have a stronger, more stable business and have recently added a piece that restores a measure of freight cycle upside. 2026 is all about execution, and we are hard at work to get that done.

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