Werner Enterprises

Q3 2021 Earnings Conference Call

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CORPORATE PARTICIPANTS

Derek Leathers - *Chairman, President, Chief Executive Officer*

John Steele – *Executive Vice President and Chief Financial Officer*

PRESENTATION

Operator
Good afternoon and welcome to the Werner Enterprises' Third Quarter 2021 Earnings Conference Call. (Operator Instructions)

Earlier this afternoon, the company issued an earnings release for its Third Quarter 2021 results and posted a slide presentation. These materials are available at the company's website at werner.com. Today's webcast is being recorded and will be available for replay beginning later this evening. Before we begin, please direct your attention to the disclosure statement on Slide 2 of the presentation as well as the disclaimers in our earnings release related to forward-looking statements.

Today's remarks contain forward-looking statements that may involve risks, uncertainties, and other factors that could cause actual results to differ materially. Additionally, the company reports results using non-GAAP measures, which it believes provide additional information for investors to help facilitate the comparison of past and present performance. A reconciliation to the most directly comparable GAAP measure is included in the tables attached to the earnings release and in the appendix of the slide presentation.

I'd now like to turn the conference over to Mr. Derek Leathers, Chairman, President, and CEO. Please go ahead.

Derek Leathers
Thank you, and good afternoon, everyone. With me today is our CFO, John Steele. I'm pleased to report that Werner delivered record third quarter earnings, our fifth consecutive record-setting quarter.

During third quarter, freight demand remained strong, and the driver market remains very challenging. Our strategic investments in driver sourcing and driver pay in a competitive labor market enabled us to grow our fleet sequentially by 75 trucks. In addition, we grew another 500 trucks with the ECM truckload acquisition that closed at the beginning of the third quarter.

We are very pleased with ECM's performance during our first four months of ownership. ECM service and safety record is excellent, their driver turnover post-acquisition remains low, their financial performance is stellar, and our integration is going well and tracking on schedule.

Employment in the trucking industry remains 1% below pre-COVID levels, while the Cass Truckload Freight Index is 16% higher. Strong consumer demand, combined with extraordinary supply chain bottlenecks are keeping retail inventory to sales ratios at historically low levels, which will boost inventory replenishment for multiple quarters going forward. At the same time, truckload industry capacity is significantly constrained by an ultra-competitive driver market and shortfalls in new truck builds. We expect a strong freight market through the balance of this year and well into 2022.

Despite a very difficult driver market, we were able to organically grow 75 trucks in TTS from second quarter to third. Our driver sourcing costs were higher in third quarter due to start-up costs for our new and planned driving school locations, increased training pay for drivers hired from schools, driver hiring incentives, and driver lodging. In other words, we made investments in driver sourcing that precede the benefits we expect to realize going forward.

Werner continues to be well-positioned to achieve strong financial results as we benefit from our consumer-oriented freight base with winning retailers, driver-preferred Dedicated fleets, industry-leading cross-border Mexico business, engineered lanes in our One-Way Truckload segment, our recent ECM acquisition, and our comprehensive capacity solutions in Werner Logistics.

Moving to slide four, here's an updated snapshot of Werner. Our truck fleet grew 6.6% year-over-year to over 8,200 trucks with just over 5,100 in Dedicated and 3,100 in One-Way truckload. Werner continues to have a consumer-centric freight base with 75% of third quarter revenues in retail and food and beverage. About half of our revenues are with our top 10 customers and 78% from our top 50. Werner has long-standing and growing relationships with winning companies in their industries.

Let's move to slide five for a summary of our third quarter financial performance. For the quarter, revenues increased 19% to $703 million. Adjusted EPS grew 14% to $0.79 per share. Adjusted operating income increased 15% to $73.9 million, while our TTS adjusted operating margin, net of fuel, declined 150 basis points to 14%. Our operating income growth was primarily due to rate per mile increases, fleet growth, and strong Logistics results. Our operating margin declined due to lower miles per truck and some higher-than-normal cost increases, which John will explain further in his comments.

Dedicated freight demand remained strong in third quarter as our customer base in discount retail, home improvement retail, and food and beverage continue to generate strong sales. Dedicated average trucks grew over 10% year-over-year and 2% sequentially. To fund that truck growth, we incurred start-up costs for driver pay and pay guarantees that increased expenses during the period in which our Dedicated miles per truck were 8% lower. One-Way truckload freight demand also remained strong in third quarter. ECM's financial results are included in One-Way Truckload, and ECM represents 17% of the trucks in this fleet.

We achieved significantly improved results in our Logistics segment in third quarter with a 35% increase in revenues and $8.5 million of operating income growth.

During third quarter, we received fewer new trucks and trailers than planned as OEMs are increasingly challenged to meet current demand levels with shortages of semiconductor chips, raw materials, components parts, and labor. We expect this industry trend will continue well into 2022.

To enable us to organically grow our fleet and continue to meet our freight commitments with our customers, we reduced the number of trucks and trailers we sold in the quarter. Significantly higher used truck and trailer pricing per unit and strong execution by our fleet sales team produced $15.3 million of equipment gains in the quarter.

In third quarter, the market value of our equity investment in TuSimple declined while the market value of our equity investment in Mastery increased. The net effect of these market value changes during the quarter was a $16.1 million unrealized gain, or 18 cents a share, which increased our non-operating income in third quarter. We adjusted for these items in our third quarter non-GAAP EPS.

At this point, I'll turn the call over to John to discuss our third quarter financial results in more detail. John?

John Steele
Thank you Derek, and good afternoon. Beginning on slide 7, total third quarter revenues increased $113 million to $703 million. Our TTS revenues per truck per week increased 3.2% due to a 15% year-over-year improvement in revenues per total mile, offset by a 10% decline in miles per truck.

The competitive driver market, the acquisition of the shorter haul ECM fleet, which has lower miles per truck, and other factors were the primary drivers of a 5% sequential decrease in TTS miles per truck from second quarter to third quarter. The other significant factors that contributed to lower our miles per truck in third quarter included truck and driver downtime due to delays caused by severe truck and trailer parts shortages, and more drivers were unavailable to work due to COVID quarantine protocols. In addition, parts shortages caused our weekly minimum driver pay guarantees to occur more frequently in the quarter due to increased truck downtime.

Adjusted operating income increased 15% year-over-year in third quarter, on top of 19% adjusted operating income growth in the same quarter a year ago. Adjusted TTS operating income increased slightly.

In Logistics, our revenues continued to strengthen with 35% growth year-over-year. Logistics had a strong quarter with significant operating income improvement. Stronger financial performance from our driver training school network and other factors increased corporate and other operating income by nearly $1 million despite the fact that the school network is incurring higher start-up costs for adding new locations.

Adjusted earnings per share in the third quarter was $0.79, up 14% year-over-year on top of 21% adjusted earnings per share growth in third quarter a year ago.

Beginning on slide eight, let's review results for our Truckload Transportation Services segment. In third quarter, TTS revenues increased 15% due to the higher rates, increased fuel surcharges, more trucks, and partially offset by the decline in miles per truck. Adjusted operating income was $65.4 million. Although our TTS adjusted operating ratio increased 150 basis points, we produced a solid 86% operating ratio.

Turning to TTS Fleet metrics on slide nine. For Dedicated, we added 484 trucks year-over-year and Dedicated revenues net of fuel increased by 11% to $271 million. Dedicated revenues per truck per week increased slightly, which was below our expectations as 9% higher rates were offset by 8% lower miles per truck. Dedicated miles per truck were lower due to the parts shortages, COVID impacts, less driver seniority due to fleet growth, and the addition of 16 new Dedicated fleets in the last year with a lower miles per truck profile. We expect to gradually improve our Dedicated miles per truck and our revenue per truck per week over the next few quarters. Our Dedicated customer pipeline remains very strong.

One-Way Truckload revenues, net of fuel, increased 10% to $190 million. Average trucks increased 2%. Revenues per truck per week increased 7.8% as a result of a 21.8% increase in rate per total mile. Our One-Way Truckload miles per truck declined 11.4%. The addition of the shorter haul, lower mileage ECM fleet in third quarter had an expected favorable impact to the year-over-year One-Way Truckload rate per total mile and an expected unfavorable impact on miles per truck, with an overall minimal impact on revenue per truck per week.

Driver pay costs were higher in third quarter 2021 due to driver pay per mile increases, incentive recruiting bonuses, and minimum pay guarantees with lower-than-expected miles per truck. Drivers who had their mileage impacted due to parts shortages were compensated. Our TTS driver pay for company mile increased 20%, which we expect will begin to moderate going forward as our mileage productivity improves.

Insurance and claims expense increased $4.4 million year-over-year in third quarter and $7 million sequentially from second quarter. The primary factors were less favorable claims development, increases in insurance premiums for liability insurance above our claim retention levels, and less favorable claims experience. Health insurance expense increased $4.6 million year-over-year in third quarter due to increased claim frequency and severity.

Health insurance expense increased $6.2 million sequentially from second quarter to third quarter, primarily due to a higher cost per claim, in part due to multiple high-cost medical claims, including four claims paid in third quarter that reached our annual stop-loss insurance level per member. The combined effect of higher insurance and claims expense and higher health insurance expense reduced adjusted third quarter 2021 earnings per share by 10 cents year-over-year and by 15 cents sequentially from second quarter.

Moving to Werner Logistics on slide 10. In third quarter, Logistics revenues of $158 million grew 35%. Excluding Werner Global Logistics, which we sold in first quarter, revenues grew 50%. Truckload Logistics revenues increased 63%, driven by a 33% increase in revenues per shipment and a 23% increase in shipments. Power-only and project business continued to generate strong revenue growth, increasing over 175% from third quarter a year ago.

Intermodal revenues grew 19%, supported by a 25% increase in revenues per shipment, while shipments declined 5%. Intermodal volumes were off due primarily to a decline in rail velocity, chassis shortages, and increased dwell throughout the rail and customer networks. Logistics produced strong operating income improvement of $8.5 million in an

excellent freight market. We continue to expect our Logistics segment to achieve strong growth through this capacity constrained period.

On slide 11 is a summary of our Cash Flow from Operations, net Capital Expenditures, and Free Cash Flow over the past five years. Expanded operating margins and less variable net CapEx resulted in higher free cash flow during the last four years. We expect to continue to generate meaningful free cash flow going forward.

We lowered our net CapEx guidance for the full year of 2021 by $25 million. Based on recent discussions with our OEMs, we expect to receive fewer new trucks and trailers this year than originally planned. The higher sales prices we are achieving for used trucks and trailers are also contributing to lower net CapEx.

On slide 12 is a summary of our disciplined strategy for capital allocation. Our unwavering priority for capital continues to be investing in our fleet with feature-rich trucks and trailers with the latest safety, driver-friendly, and fuel-efficient capabilities. In July, we opened a new driver and maintenance facility, which is strategically located in Lehigh Valley, Pennsylvania, and replaced a smaller leased facility.

In a subsequent slide, Derek will discuss the progress we are making with our Werner Edge technology initiatives.

We see intrinsic value in our stock based on our long-term growth expectations, and we purchased over 1 million shares this quarter at an average price per share of $45.52.

On July 1, we completed the acquisition of 80% of the equity of the elite regional truckload carriers of the ECM Transport Group based in Cheswick, Pennsylvania. ECM performed very well in third quarter and exceeded our expectations for driver retention, fleet growth, and profitability. We implemented several buying power, cost-saving synergies with ECM during the quarter and are excited about how our companies are working together.

We are committed to maintaining a strong and flexible financial position. Our long-term leverage goal is a net debt to annual EBITDA ratio of 0.5 to 1x. With the acquisition of ECM and our stock repurchases during third quarter, we ended the quarter with a net debt-to-EBITDA ratio of 0.5.

I'll now turn the final portion of our prepared remarks back to Derek. Derek?

Derek Leathers
Thank you, John. During third quarter, the average age of our new truck and trailer fleet inched up slightly as a result of the OEM build challenges. Every Werner truck is equipped with advanced collision mitigation safety systems, industry-leading emissions and fuel mileage technology, automated manual transmissions, forward-facing cameras, and an untethered tablet-based telematics solution.

The driver market is competitive and dynamic. In addition to implementing market-based driver pay increases, we are expanding and leveraging the strategic advantage of our industry-leading driver training school network and our inherently strong culture. So far

this year, we increased our school locations from 13 to 17 and have five more planned openings to be completed by the first quarter of '22. These new school locations were selected in cities with strong driver demographics that align with our freight network.
The financial investments we are making in these new driving schools are proving successful as we have already increased the number of school graduates who have decided to join Werner. Each of these driver graduates then develops further driver proficiency through our proprietary program with certified and experienced Werner leaders. The investments we have made in driver sourcing and hiring are working. From the end of the second quarter to the end of third quarter, our drivers increased by 3.3%, not including the addition of ECM.

On the technology front, our Werner Edge team continues to work on our cloud-first cloud-now strategy by developing innovative products that are integrated via APIs with third-party SaaS solutions. We are building a tech stack that will improve process efficiencies and help drive operational excellence. Our rollout of MasterMind, which began with our Logistics division, is on track with transactional volume increasing daily at all domestic U.S. brokerage offices. This is the first of multiple phases that will continue over the next three years.

We continue to deliver on our commitment to create products and solutions that empower our drivers, shippers, carriers, and associates.

For our drivers, we've delivered enhancements to our in-cab device that has resulted in 250 hours of daily time savings across our fleet. We provided our drivers with a new ETA software engine that has improved arrival time accuracy. We digitized our DOT inspection process, which improved efficiency and contributed towards Werner's commitment to sustainability.

When it comes to quick and accurate shipper bids, we've implemented new software to streamline the bulk bid process and improve our response time to our customers. We've strengthened our carrier platform by delivering tools to streamline rate negotiation and help identify best matches for loads, and this process utilizes machine learning to improve matching and increase overall transactional efficiency.

On slide 15, you can see the results of our 5Ts + S initiatives in both truckload and logistics. In August, we were once again named the 2021 Quest for Quality Award winner by Logistics Management in both the Dry Freight Truckload, and Logistics categories. This 38th annual shipper survey is widely regarded as the most important measure of customer satisfaction and performance excellence in transportation and logistics. 4,100 shippers participated in this survey. Werner received the second-highest carrier rating of all public company dry freight truckload carriers, and Werner is one of only two of these carriers that received this award in each of the last five years.

Next, on slide 16, we continue to make significant progress in our ESG program. In July, we published our inaugural Corporate Social Responsibility report following the recognized standards from the United Nations Sustainable Development Goals and the Sustainability Accounting Standards Board. You can now find Werner as a reporting company under the SASB framework on their website.

We launched WernerBlue, our branded sustainability endeavor. We set new ESG goals and milestones with four of the nine goals targeted for completion in 2022. These goals will continue to drive accountability for our ESG efforts across our company and increase engagement by our associates. The four goals are: create an advancement and a retention plan to increase and elevate women and diverse talent in our management team; increase employee engagement with the expansion of our associate volunteer program by adding a volunteer hours option that will support employee involvement with qualifying charities of their choice; we created a stand-alone ESG Board committee that commences in 2022; and we will form a task force of senior leadership, associates and board members to further the goals of WernerBlue, our branded sustainability program. During the quarter, we added three new associate resource groups. For the year, we have introduced eight new ARGs.

This week, Werner was awarded the 2021 SmartWay Excellence Award for outstanding environmental performance for the seventh time in the last eight years. This is the highest recognition in our industry given by the United States Environmental Protection Agency.

Next, on slide 17, I would like to spend a moment discussing our durable business model. Here is a history of our annual TTS adjusted operating margin percentage, net of fuel, since 2008. The bars show the percentage of our TTS fleet that is Dedicated, and the line chart shows our annual TTS operating margin percentage.

During the last five years, while we successfully implemented our 5Ts strategy and as we grew our Dedicated fleet, we achieved meaningful TTS operating margin improvement. A year ago, we established a long-term annual adjusted operating margin goal range from 10% to 16%. After calibrating and carefully modeling our TTS margin performance, we are increasing our TTS annual adjusted operating margin goal to a range of 12% to 17%. We have increased confidence in our ability to perform in less attractive markets, which allows us to raise the bottom end of the range by 200 basis points, and the structural improvements we have made give us confidence in our ability to perform better in stronger freight markets, which allows us to raise the top end of the range by 100 basis points.

Our carefully constructed and optimized fleet mix is designed to generate strong adjusted operating margin performance in good freight markets as evidenced by the 15.9% TTS margin we achieved over the last 12 months. At the same time, we are increasingly confident we will perform very well in tougher freight markets due to our resilient Dedicated fleet and strengthened One-Way Truckload fleets with specialization in Mexico cross-border, expedited engineered fleets, Temp-controlled, and ECM.

Let's now move to slide 18 and a review of our 2021 guidance framework, how we are progressing against this guidance, and updates to our outlook.

During third quarter, we increased our truck count by 575 trucks sequentially, including the 500 trucks we acquired from ECM. Our end-of-period trucks are up 5% year-to-date, and we expect our fleet to remain flat or decline slightly in fourth quarter as a result of normal seasonal holiday activity. For the full year 2021, we expect our fleet to increase from 3% to 5%.

Pricing in the used truck and trailer sales market was better than expected in the third quarter on anticipated lower unit sales, resulting in higher-than-expected equipment gains of $15.3 million, up slightly from $13.5 million in the second quarter. For the fourth quarter, we expect continued strong pricing with fewer units sold than third quarter, resulting in expected gains in the range of $10 million to $12 million.

Net capital expenditures were $163 million for the first 9 months of 2021. We now expect CapEx to be $25 million lower for the full year, and to come in at a range of $250 million to $275 million based on fewer new truck and trailer deliveries.

Dedicated revenue per truck per week increased slightly in third quarter. The shortfall relative to our guidance was due to the factors that lowered our miles per truck. For fourth quarter, we expect to begin to make progress restoring our Dedicated revenue per truck per week growth in the 1% to 2% range.

One-Way Truckload revenues per total mile for the third quarter increased 21.8%. For fourth quarter, we expect our One-Way truckload revenues per total mile to increase 17% to 19% above fourth quarter a year ago.

In the first four weeks of October, freight demand trends in our One-Way Truckload unit have remained strong.

We are reaffirming our effective tax rate of 24.5% to 25.5% and expect the average age of our truck fleet to be 2.2 years and the average age of trailers to be to 4.4 years at year-end. Werner remains well-positioned with a superior team and an active talent pipeline that will continue to yield strong and sustainable results.

At this time, I'd like to turn the call over to our operator to begin our Q&A.

Question and Answer

Operator

(Operator Instructions) Also, the call will end at 5:00 p.m. Central time following the company's closing remarks.

And our first question will come from Chris Wetherbee with Citi.

Christian Wetherbee, Citi
Maybe just want to start on the TTS side and maybe if we can get a better, or maybe more of a breakdown of what was going on from a cost perspective in the quarter. So it sounds like there was two dynamics that impacted the profitability. There was the lack of miles per tractor and then there was also some cost dynamics. So maybe if you could kind of split the two of those apart and give us a sense of sort of what the impact of each one of those was we have a better sense of what maybe kind of ongoing profitability might look like in the segment?

Derek Leathers
Sure, Chris. This is Derek, and thanks for the question. I'll start and then John will jump in with more detail, I'm sure. But, in a word, miles were a major problem in the quarter. We suffered throughout the quarter from ongoing parts issues and parts availability problems. I think we were impacted greater than others that maybe don't have the same decentralized Dedicated kind of footprint. Much of our infrastructure, if you will, relies on dealers and dealer networks to be able to support these Dedicated footprints. And given the service expectations of those fleets, we had to do quite a bit of repositioning and really incur some incremental cost that if mileage productivity would start to resume to normalized levels, which it has been doing as of late, we will see a lot of that pressure go away.

On the cost line, we talked a lot about we had some significant increases in both health insurance and liability insurance. Interestingly, the bulk of those were sort of out-of-period developments, if you will, that took place in both cases that we needed to address in the quarter, and we chose to do so. Parts and some of the OEM disruptions that we went through impacted us across a few other items as well, like driver lodging, driver layover pay, and also tows were up in the quarter, what I would refer to as a material amount as we had to work through some of those issues.

We've taken several steps to address them and have made considerable progress on those issues. And the most important one of which is we've started to see just improvement in the overall supply of many of those parts that were causing that. On the driver pay side, we saw a significant increase in driver pay. A lot of that is where guaranteed minimum pay really started to come into effect and leak into the P&L because those are designed as truly kind of a fail-safe, not something intended to come into play on a week-in, week-out basis in any broad format. But based on the structure and…that we have put in place, it came into play more than we had anticipated.

We've done a couple of things there. One, an eye toward productivity, which will obviously prevent that from happening, but secondarily looked and evolved some of those plans to better reflect or better protect and have a more shared risk as those situations may arise. So, as we look forward, it's going to be about a return to normalcy from a productivity perspective, both in Dedicated and in One-Way, as well as having evolved a few of the pay packages and pay programs to better reflect market, put us in a position to hire…to attract, hire, and retain but have basically that risk profile shared just a little bit better than it was at times during Q3. I don't know if that fully answers or, John, if you have any color you'd like to add?

John Steele
Yes. Just a couple of things, Chris. So clearly, the health insurance and the insurance and claims were higher than normal. There was a $0.15 a share sequential impact due to those 2 items and a $0.10 per share impact on a year-over-year basis. Then the other part of it is that we were able to begin getting back our truck growth in the quarter. So from second to third quarter, on an average truck basis, we were up over 100 trucks, most of that in Dedicated. And that excludes the ECM 500 trucks that we added in the quarter. So we're one of the few carriers that was able to invest in drivers and get some growth back this quarter.

So the hiring incentives, driver lodging was about a $0.05 per share impact on a year-over-year basis. And then the minimum pay and layover pay were about $0.05 a share as well on a year-over-year basis. Sequentially, the hiring incentives and lodging was about $0.03 a share sequentially and minimum pay and layover pay were about $0.01 a share sequentially from second quarter. So hopefully, that gives you some more information to clarify.

Christian Wetherbee, Citi
Yes, that's really helpful color so I appreciate all the detail there. I guess the follow-up question would just be, as you think about 4Q and maybe 1Q, 2Q, first half of next year, it sounds like there's progress being made there, based on your comments maybe about productivity being able to pick back up, but also just given some of the dynamics for the supply chain, it would also sound like some of the cost headwinds might still be around for the next few quarters. So if you could sort of give us a little bit of help in terms of understanding how quickly this process clears or do we need to think about this really as being a major issue in 4Q and maybe getting better in the first half.

Derek Leathers
Yes, I'll start there. So clearly, some of it is confined to the quarter. Things…we are on top of the parts issue, parts shortage. We're working more closely with these dealers. We've even started to work to supply them with parts that we had better availability to than they were able to on their own behalf. We've clearly become more aggressive on where we will go service ourselves versus rely on others to do so. Those things have cleared. Minimum pay will come much less into play as productivity has already started to increase and really taking it out of play. So that one is predominantly behind us.

It's tougher on health insurance and liability because obviously, we're in the quarter, and it's difficult to predict. But at this time, those would not appear to be trending as we saw in the third quarter, and we don't have reason to believe that…that won't have an opportunity to return to closer to normalized levels.

Now we did take a pretty significant increase in, which we disclosed, I believe the last quarter, in our health insurance premiums, and that obviously is here to stay. But a lot of it is behind us…lodging, we had several Dedicated accounts that went into effect at the beginning of this quarter that you simply can't miss implement on those. And so there was a chunk of this, the costs are reflected in the third quarter. But as you look in the fourth quarter, you now at least start to offset that with revenues and yield.

Driver pay line itself, the actual pay line itself, that's more ongoing. So what I'm referring to there is salary increases and the impact of salary changes that took place. And again, that's with an eye toward the most robust Dedicated pipeline we've had in a long time and our need to deliver on the closed business that we have coming down the pipe. That new business has been priced with this new reality in mind. But the cost to get it ramped up and be prepared for it was borne in the quarter.

John Steele
So, Chris, I would add that the 20% increase in driver pay per company mile; that is higher than it should trend going forward, because our miles were down 10%, and we expect to get the miles back. So on a per mile basis, we think that percentage increase will come down. It's trended from up 7% year-over-year in first quarter to 11% in the second quarter to 20% in third quarter, but we think it will moderate as we start in the fourth quarter and into the next year.

Operator
And the next question will be from Scott Group with Wolfe Research, LLC.

Scott Group, Wolfe Research
Hey thanks, good afternoon guys. So, Derek, John, I know you don't typically answer this question, but just given the third quarter operating ratio and just people trying to understand how sustainable this is or not, any thoughts on fourth quarter operating ratio and if it can improve and, or not?

Derek Leathers
Yes, so the expectation in Q4 would be to see operating ratio improvement from Q3. We've just talked about several costs that are transitory, although some are more structural. Those transitory ones are being addressed as we speak and many have already…we've already changed course or made adjustments to see improvement on them. As we think about…the question we also never answer but it's going to come up, so I'd like to talk about it now is Q3 to Q4 sequential improvement. That will come up at some point, so let's take that head-on.

If you look at our 5- and 10-year history of Q3 to Q4 sequential improvement, I believe the 5-year sequential history of improvement is about 20%. At this point, with the changes and those portions of the costs that were transitory in nature, we believe that is a number we're comfortable with making that type of improvement as we look into Q4. And if we can make further progress on some of the headwinds in particular as it relates to miles, as impacted by parts availability and some of the ramped-up incentive hiring that we had to do to meet contractual obligations, that there could be some upside to that.

Scott Group, Wolfe Research
Okay. And then I want to ask on the vaccine. How you guys are thinking about this and what's the latest you're hearing on carve-out or not and what you're doing to prepare for it?

Derek Leathers
Yes. So there's a lot there, but I'll start with…we know we have a contingency of our fleet that is at this point, unvaccinated. It's tough to pin that down to an exact number because within that contingency, there is a group that chooses to not declare despite how much we may be asking or pushing. We are certainly pro-vaccine, and we were setting up on-site vaccination clinics, and doing a variety of things to get our vaccination rate up. But I would tell you that I think we're not dissimilar from the industry, which is probably in that 50% unvaccinated range, potentially even a little higher than that.

We're preparing and thinking about and modeling what it would look like to route and test. Those costs are very prohibitive if that was to be the route that was taken. We feel encouraged that the dialogue has been ongoing relative to a potential carve-out for transportation similar to what they did in Canada. I think it makes all the sense in the world. These are remote workers that don't interact with the general public and clearly don't come near the grave danger test that this entire vaccine mandate was based on, based on the nature of their work. But we're also going to continue to prepare for worst-case scenario.

I don't see a world, Scott, to be honest…we're at a time when the supply chain is under the level of duress it's on already, that we could risk a 20% to 25% exodus industry-wide. That's not a Werner number; I'm just saying industry-wide. And nor do I see a justification to possibly defend the 100 employee count in an industry as fragmented as ours that also is daily tasked with hauling, delivering, and making available the very PPE, vaccine, and other medical supplies that are absolutely critical at this time. So where it will go from here? I don't know. We do expect to hear something inside the next, call it, 2 to 5 days, and we're going to be standing by on the ready to react as will everybody else. But it's a concern, but one that's at this point, a bit out of our control until we get more detail.

Operator
The next question will be from Jack Atkins with Stephens Inc.

Jack Atkins, Stephens, Inc.
Okay, thank you for taking my questions. I guess, Derek, maybe to pivot a little bit and maybe look forward some more to next year. Obviously, with strong demand trends, we've got visibility into that, at least into the first half of next year, it's very difficult for carriers to add capacity both on the driver side and the equipment side. I guess would you care to maybe update the market in terms of how you're thinking about the potential for contractual rate increases in 2022 on the One-Way truck side? Any sort of kind of parameters you want to maybe think about that or just want to put out there for the market. And then within that kind of broader framework, do you think it's realistic to expect margin expansion in 2022 for Werner? If you can kind of think about that for us, that would be helpful. Thank you.

Derek Leathers
Sure. So I'll start with, Jack, thank you. I'll start with this. We've made our move on driver pay early. We felt it was important to be fully staffed and ready prior to peak and then to set ourselves up for the Dedicated pipeline that's ahead of us that is either landed or near closed. And so that's important as it relates to whatever happens with rate because at this point, I feel more confident than ever that we have got a variety of packages and/or safety nets for our drivers that position us very well to continue the trend we've seen as of late for both organic growth and then, of course, with the ECM acquisition, demonstrated the ability to add capacity organically as well.

With all of that said, there are inflationary pressures across the P&L, and we're going to be asking our customers to support us as we support them through this peak and beyond. Early in the year, you've got lapping effects of some contracts that maybe didn't get the full effect of what needed to be done last year when they were negotiated, call it, late '20, with implementation dates in early '21. Well, we're now at that stage today. So in those

scenarios, we're certainly in the double digits and above type range and in some cases, higher than that. As you get into next year, we haven't really given firm guidance, but I think the thoughts of that sort of mid-single digit are no longer prevalent at all. It's got to be north of that. And I think it's a lot more rational to think about it in a double-digit format as we think about rate renewals.

That doesn't mean the whole network moved by that amount because clearly, we have certain longer-term agreements and other things in place. But those longer-term agreements also are generally coupled with lower turnover fleets with lower pressures on some of the lines across the P&L. So, margin expansion is possible. That's got a lot to do with why we changed our long-term guidance range. Yes, it's a quarter that didn't meet everybody's expectations and most importantly, our internal ones. But at the same time, we took several strategic decisions this quarter and spent money to invest in what we believe is a longer story that runs through the cycle even though this cycle, we think, has longer legs with each passing month.

Jack Atkins, Stephens Inc.
Okay. That's very helpful, Derek. Thank you for that. And I guess, maybe a bigger picture question. This has been such an unusual freight cycle in so many ways. And I think everyone expects this to continue on for some time into the future. I would just be curious to get your take on the feedback you're getting from your shipper customers.

Are they looking for ways to maybe more closely partner with carriers like Werner, who can provide high levels of service and capacity to them consistently through cycles? It just feels like we kind of go through this annual bid process and one party is trying to get something from the other almost every other year. I'm curious, Derek, for your thoughts on if that can potentially change prospectively moving forward, just given how unusual and how strong this freight cycle has been and the pressure it's put on your shipper customers.

Derek Leathers
Well, the easy part would be yes. Shippers, obviously, in a market that's tight are aggressively looking to find and establish longer-term kind of agreements, longer-term arrangements, partnerships, whatever word you may want to use. The onus is on us to make sure that that happens and aligns with people that we think are winners in their space, that have longer-term runways to their own internal models and their own internal capabilities.

As we do that, we want to make sure it's people that have looked to buy across the portfolio that have needs that fit what we bring to the table; size matters, and a lot of these things. Our ability to give a more guaranteed rate of return over a longer period of time to our shareholders matters to us. And we're pretty open about that. And so, as we see the opportunity to get deeper into Dedicated with shippers that also have needs in Intermodal and Logistics and in One-Way, those are places that we're going to look to better align ourselves with long term. And we're setting expectations as we put capacity toward their needs this peak that are beyond the rate.

So it's not just what the rate opportunity may be on a particular project, but it's what happens after that. Once peak has come and gone and some level of normalcy returns to some of the bottlenecks in the supply chain, we want to make sure that relationship has runway left. So those conversations are going great. I had several of them here recently that are encouraging. And I think the kind of investments, just as an example, we made in Q3 to meet our commitments, once again show that when we make those commitments, they matter. And we keep our word. They're expensive at times, and in the short term, they're even painful. Over the long haul, I think they make the most business sense.

Operator
The next question comes from Bascome Majors from Susquehanna. Please go ahead.

Bascome Majors, Susquehanna
Yes, thank you for taking my question. I wanted to go back, and maybe with the hindsight of hearing some of your peers talk about their quarters and results, I mean, has anything stuck out to you? Were you surprised that some of the profitability of some of your competitors, who admittedly are maybe a little more One-Way levered, but even a big Dedicated carrier added 700 or so trucks sequentially, and it was fairly flat in operating income doing that? Just anything that stuck out to you and any thoughts on where you are on pay versus peers at this point in that fleet as we look forward? Thank you.

Derek Leathers
Yes, Bascome, great question. I mean, look, it would be, we'd be remiss and really somewhat derelict in our duties if we didn't always challenge ourselves about our model versus other people's, and how they may be performing versus us. But with that challenge, I can assure you we don't do it just quarter…on an individual quarter basis.

We've talked for years about the fact that we want to return this organization to best-in-class service, mid-single digit or better revenue growth through the cycle, and double-digit earnings growth on an annual basis through the cycle. And to do that, you have to have a portfolio that is structured in a way that's more diversified, that's more…that customers can buy, and we can meet them where their needs are.

The one that can survive the ups and downs and cyclicality of the One-Way market, and sure, there is no doubt in my mind that we could have made more money in Q3 at the expense of our long-term objectives. I mean the best example of that I can think of is, it's a very easy time to sell a bunch of trucks and trailers right now and make a lot of money in gains on sale. We chose not to do that. We'd rather hold that truck and trailer, especially given some of the supply chain disruptions and our diversified Dedicated footprint. So we pay a higher price for our long-term strategy inside of one quarter, but I think it stands up over time, and we'll continue to do so.

We have five consecutive quarters of new EPS records. We have 11 of the last 15, the 12th one missed by $0.01; two of the others were in the 2019, which was the…and we were the only carrier whose EPS went up from '18 to '19. So, over the cycle, which is what we've talked about, we think this is a play that continues to hold its value and improve and enhance our returns and results for our shareholders, our customers, and really everybody involved with the Werner story.

Occasionally, you pay the price. When you've got Dedicated fleets that are coming in place and the timing is such that you've got large outlays at the end of the quarter and the benefits of such, coming in the following quarter, you don't get to pick when they implement. Well, you pick, but you don't choose based on a quarterly EPS, you choose based on the long-term relationship with that customer. And so, we'll work through this. Not happy, you can probably tell that by the tone of my voice. But at the same time, I'm very proud of the ongoing story that we have developing here, and it's not yet written to its fullest extent.

Bascome Majors, Susquehanna
Thank you for that answer. If I could just focus a little bit on the driver pay portion. And I realize that Dedicated is very local and situational so it's hard to paint a broad brush. But do you feel like what you did in 2Q and 3Q got you back to market, or do you feel like you've invested to get ahead of market, and that's going to really give you some momentum going forward? Thank you.

Derek Leathers
Yes. Great question. I think a couple of things. One, I think we are ahead of market in some of the new stuff we're doing. And in the short term, we might have a little slightly higher cost profile on some of those, but it allows us in a tough market, not just to attract and retain drivers, but to attract and retain the highest quality ones that we need for the type of work we're going to be signed up for doing. So I think that's part of it. To be frank, I think there's also a few other packages in the quarter that were innovative in nature, that have been now evolved quickly to better adapt to some circumstances that were really never foreseen. I mean if you…if anybody had ever told me that we would have the magnitude of trucks, again, because of our dealer reliance, that were idled during the quarter, and thus, the impact on some of the guarantees and some of the safety nets, I would have… it was just something we didn't expect.

What do you do? You learn from it, you adapt, and you improve it. So we're still going to provide our drivers with guarantees, and we still have opportunities for them to have strong, viable safety nets, but we've got to think through and improve upon some of our proactive planning around how to avoid those from coming into play. One of the things I told our team this morning is as frustrated as I may be with where we ended up, the fact that we're angered, frustrated, whatever the right word you may want to use about an 86% OR, I think, is a telltale sign of where our standards are. It wasn't long ago that, that was something that we were striving to get to, and it's something that many, many carriers still aspire to someday. And for us, it's simply unacceptable in this market condition and one that we will improve on.

Operator
Next question will come from Tom Wadewitz with UBS. Please go ahead.

Michael Triano, UBS Securities
This is Mike Triano on for Tom. So I wanted to ask about drivers. With the minimum pay kicking in for a lot of drivers in 3Q, was that helpful from a retention perspective? And then, on the increase in driver schools, how are you thinking about the impact on the One-Way fleet and, in particular, your ability to potentially grow the One-Way fleet in '22?

Derek Leathers
Yes. So the first question first on the minimum pay. It was definitely impactful and effective. We've seen a fairly, actually better than modeled benefit, if you will, from a retention perspective on some of the minimum guarantees we put in place. Now they come into play more often as I've said several times than we had expected or wanted, and we've got to fix that. That's our job. That's not the driver not doing their part. It's us needing to make sure we put the miles on those trucks and keep those trucks on the road and running. But overall, directionally effective with some modifications that we need to take and improve upon. I apologize. You had a second part of your question?

John Steele
Yes, the driver schools and the new locations, we really do think they are helping. We've been able to get back to sequential fleet growth this quarter where we haven't been able to achieve that in the last few quarters. We added 75 trucks, excluding ECM. And we're up to 17 locations now. We have five more planned in the next six months that we think will really help us train and develop drivers to be able to continue to have that sequential fleet growth in a market where there's a significant competitive headwind for labor. And we're, I think, doing a good job of fighting that headwind with our driver school program.

Operator
The next question will be from Ken Hoexter from Bank of America Merrill Lynch. Please go ahead.

Kenneth Hoexter, BOA Merrill Lynch
Good afternoon John and Derek. Can you clarify, I guess, just real quick, the insurance and claims? Is that ongoing or was there a catch-up in the quarter? But then my question is the One-Way revenue per tractor actually declined sequentially. Maybe just delve into that a little bit to understand the mix change or what's going on. Is that due to the massively lower miles? Just want to understand the rate per mile.

John Steele
I'll take the first part. The insurance and claims, if you look at the year-over-year increase, which I believe was about $4.4 million. Not quite half of that was due to increases in excess insurance premiums for the part where we have coverage for catastrophic claims, and that's a reflection of the overall market conditions for that type of insurance. And the balance was due to increases in claims and claims development this year compared to a year ago. We got a little bit more congestion on the roadways than we did last year at this time. Our safety record is still strong but a little bit higher claim development. And then do you want to take the second part, Derek?

Derek Leathers
Yes, the One-Way revenue per truck per week, which I believe is what you had asked about. It's essentially flat from Q2 to Q3, and that is driven almost exclusively by some of the mileage productivity issues that we were faced with during the quarter. And a lot of that, again, is driven by some of the same issues we've been talking about. And that has already improved and started to reverse that trend and looks much better as we go into Q4. We've got to make sure and keep that productivity gain and continue to see that moving up as we move forward. But at this time, we've got a lot of work still ahead of us.

Kenneth Hoexter, BOA Merrill Lynch
Thanks, Derek and John. Derek, maybe just your thoughts on the new Dedicated business. It sounds like we're running up, was it a lot of new business coming on at the end of quarter, as you said. I just want to understand the costs, I thought given your scale, the incremental costs coming on board wouldn't have typically impacted you. So maybe just flush that out for us a little bit?

Derek Leathers
Sure. So you're right, it's not, it's certainly not exclusively related to that new Dedicated business. But the difference on the Dedicated business is when you're adding drivers, you want to add them all the time, when you're adding Dedicated, you have to add them at a certain time. And so there were some incremental advertising costs, onboarding, lodging, some training and development costs. And then the other thing within Dedicated is on certain fleets, the work we have to do from a finishing perspective. So training that you do after hiring them within the fleet is done either on the account or on a very similar account, whereby you see no productivity impact or enhancement by having two drivers on that truck and what you have is a significantly higher cost profile during that period.

But we met all those deadlines and those launch dates. And those launches all started in Q4 and have already all started, and they're now in place. But most of that hiring activity and a lot of the bounty bonus and incentive bonus and other things that were in place took place in Q3. By no means do I want to paint the picture that driver pay suddenly goes back to Q2 levels. That is not the case. But there is chunks of those cost items in Q3 that were unique that we will start to moderate, both through higher mileage as well as lower incentives and bounties because we've met some very critical deadlines in our implementation plans.

Kenneth Hoexter, BOA Merrill Lynch
So, Derek, just can you clarify one thing on that just so we understand the pricing on your, I guess, the new business that's coming on board, but your old Dedicated contracts? What inflators that, you know what, I thought the whole point of the business, right, is that it protects you on up and down. Can you maybe just talk through the timing to realign that with the costs that you're seeing?

Derek Leathers
Yes. That's a fabulous question. So first off, there is great deal of protection in the up and down, as you said, in most of our Dedicated contracts. There are a couple of exceptions. So, when you have absolutely down trucks, so the truck is down awaiting parts or down because of hurricanes in the Southeast where you move them out of the region and then back into the region, there are…even then, you have some baseline protections, but absolutely none when it is a nonproductive truck relative to any ability to add margin or operate at any profit. And so there's impacts there that were unique to the quarter that we have seen already rebounding.

As it relates to repricing Dedicated, we've had good success on the incumbent business throughout the year of pricing in the new pay packages that we're referring to. So when we talk about driver pay on the base level, we can get that price back in. In the quarter, some of the stuff that's not priced into that incumbent business is the sudden and fairly significant

increase that we spent across some of those incentive, bounty, advertising, lodging, and other incidentals associated to it.

Operator
The next question will be from Jeff Kauffman from Vertical Research Partners. Please go ahead.

Jeffrey Kauffman, Vertical Research Partners
Thank you very much. I'm going to apologize for re-asking Ken's question a different way. But when I looked at nonfuel revenue per vehicle per week in Dedicated, it was roughly flat with year-ago levels. And I understand what you were just explaining with the new contracts and the new pricing and the up pricing. But why haven't we made more traction over the last 12 months in that area? Is there a mix effect, is there something else going on that might not be obvious just looking at that statistic?

John Steele
What stat are you looking at specifically, Jeff? Is it revenue per truck per week net of fuel or...

Jeffrey Kauffman, Vertical Research Partners
Yes.

John Steele
Okay. So that was $4,129 in third quarter this year, $4,115 in third quarter last year, but we had 9% I think it was, 8%, I'm sorry, lower miles per truck. And so it was the part shortages and drivers out with COVID and the new fleet start-ups that reduced our mileage productivity.

Derek Leathers
Yes. I'll just add. So 16, to be very specific here. 16 of the 20 fleets we've added and Dedicated in 2021 are by design, lower mileage fleets. So you have lower cost structures to those fleets as well, and that mix has a significant impact on what happens. Now that does not explain away the entirety of that mileage degradation that we're talking about, but it is a major component of it. So if you were to go back to the Q2 call, there was a question about revenue per truck for week in Dedicated and I made the comment in Q2 something along the lines of we're struggling to find what the right metric is as our fleet mix is changing fairly significantly. And it was both with those fleets that we had landed in mind, as well as those we knew were closed and about to implement, because you can have static revenue per truck per week and increased yield if, in fact, the mileage associated with that fleet is significantly lower by design, and we are seeing more of that as of late.

Jeffrey Kauffman, Vertical Research Partners
Okay. So maybe to paraphrase what I think John said in the opening comments. Revenue per mile implied is probably up in that 9% to 10% range and then miles per truck down, and that's really the way to think about it.

John Steele
Yes, it was up 9% on rate and down 8% on miles and net is slightly higher.

Operator
The next question will come from Brian Ossenbeck from J.P. Morgan.

Brian Ossenbeck, J.P. Morgan
Hey guys, good evening. Thanks for taking the question. Derek, just wanted to dive back into the vaccine mandate a little bit more since it sounds like something is rather imminent here. To the extent, you can help us just think through what happens next. We're assuming that there's going to be a lawsuit, maybe several that come out to challenge this as we've seen with other ETS out of OSHA.

So maybe you can talk about how you're preparing just to, I guess, educate your fleet. You may not even want to see a mandate even if it is something that's challenged in court. So do you think it will still have an effect if it is challenged? And then secondly, it's a little unclear to me at least, what happens after the six months when this emergency temporary standard expires. So I don't know if you've seen or heard anything on that front because it seems like it could be certainly counterproductive to supply chain they're trying to fix but it could also perhaps have some uncertainty after six months if and when it does get put into place. So any thoughts on all that would be helpful.

Derek Leathers
Yes, Brian, I will attempt to weigh in, and I hope you can understand the sensitivity about any answer relative to anything vaccine-related. But I'll start with the obvious. We are pro-vaccine, and we will continue to push and recommend and encourage, and we are doing that actively as we speak. We will also continue to analyze all available options relative to testing and the routing implications of such tests. And those are extremely cost-prohibitive at this point, and we are working through that.

It will have a significant impact on supply chain. And so I question the logic in trying to move forward with a group of remote workers that has no interaction with the general public to speak of, and certainly falls far short of the grave danger threshold that the entire emergency action is based on. With all of that said, at this point, we just don't know. We've had calls with OSHA. We've had calls with the Department of Labor. We've been part of other groups' calls with both as well, and there are too many uncertainties to predict where this heads from here. And I'm hoping cooler heads will prevail. And somewhere in this mix, somebody will remember that these are the very men and women that worked every day during this entire pandemic to make sure all of them were safe and interestingly, kept themself safe at far greater levels than the national average of infections. And I think it speaks to the very remote work, the very nature of the remote work that they do.

So it's tough, it's worrisome. I understand the concern from the investment community. And all I can tell you is that we will stay as close to the forefront, be prepared to react. And the last thing I'll say on this is I agree with your assessment that was buried in the question around even if it were to come out and be challenged in court, is there some risk of driver loss? Yes. And that has a lot to do with why we wanted to make sure we were fully staffed and fully equipped with drivers. And you saw, I believe, the number is 3.3% increase in driver count from Q2 to Q3, I'm sorry, year-over-year, exclusive of ECM, and that's a little bit of a hedge as well. So those things come at a cost, but I think we're in as good a situation as we can be in, in very difficult times.

Operator
The next question will come from Jon Chappell with Evercore ISI.

Jonathan Chappell, Evercore ISI
Derek, just quickly on the ECM integration. You've had four months of it now. Were there anything surprising, either the good or the bad in that first quarter, any of the impact on the total results, potentially from ECM cost integration? And then finally, has anything else kind of come across your desk because as you've integrated this business that looks attractive from a bolt-on or from entering another new market as you've done with ECM.

Derek Leathers
Yes, great question. I would start with, in general terms, we're very pleased with how the integration is going after four months. We were pretty diligent throughout the due diligence process. We had a plan in place and the team identified to handle the integration. And I would say it's on or ahead of schedule in every major category with one noticeable caveat, and that is some of the equipment synergies. Obviously, we would have liked to have had much more progress at this point on some of the buying and purchasing synergies than we've realized. We have realized some, but not nearly what we would have liked to, and that has everything to do with the very OEM supply chain challenges that everybody is well aware of. So that would be really at this point, the only downside.

The upside stuff, driver retention has been better than expected, and we are very excited about where morale sits in that fleet right now. Customer acceptance and service levels have been great. Their financial performance has been as expected or better when inclusive of some of the cost savings we thought we could bring to bear. But the big caveat, which by the way, is one of the biggest synergies is really on the purchasing and procurement side. And that's just because it's a constrained market right now.

As it relates to pipeline, the pipeline is…we do have pipelines, we have…we are continuing to look at other opportunities that we think will be additive and accretive. And I put those in that order because ECM was truly additive to our portfolio. It brings to bear a set of capabilities, a knowledge set, a reputation and brand and that we think makes us better, makes our portfolio stronger. We are looking and continue to look through that pipeline for other such opportunities that are additive to the portfolio. Accretive is important as well, and this is playing out to be such. So we will look at both of those things as we go forward. And I do think there's an opportunity out there for future ECM like or other parts of the portfolio that follow a similar path relative to quality of operation and making us stronger in our respective areas of expertise, especially those where we think the market is headed and in particular, in that short-haul kind of marketplace that ECM does so well in.

Operator
Ladies and gentlemen, this concludes our question-and-answer session. I'll now turn the call over to Mr. Derek Leathers, who will provide closing comments. Please go ahead.

Derek Leathers
Yes. Thank you, everyone. I just want to thank you again for joining us today. We achieved record third quarter earnings despite missing our own and many of your expectations. But we're in this for the long game. We made multiple investments throughout the quarter that we believe are already paying dividends as we work our way to Q4 and beyond. Our best customers are winners, and as such, they are growth companies, and their #1 question is how we can grow with them? We're leaning into that as we further position this company for the future.

We will continue to focus on cost controls and several of the period costs that impacted this quarter, we've already taken measures to improve as we sequentially move into Q4. There are some necessary and non-transitory cost portions of the P&L that have been under pressure. Those will be offset through pricing, and we are working on that actively as we speak. We keep our promises, and that is going to be true in good times and bad. And it is rewarded though over time through the bidding process, and we are seeing that reward as we get deeper into the year.

Our Dedicated model remains durable through the cycle, just like we've stated all along. Growth has happened to be more expensive right now, but as long as it's in the right business with the right customers, with the right contract terms, I think it's a sensible and smart investment.

Logistics growth has never been more important. We didn't talk about it a lot today, but we're proud of the results they put up this quarter. The high capital requirements are trucking are only going to go higher as we look forward, and it's imperative for us to continue to balance our asset exposure with our non-asset growth.

And in closing, peak is here. We're ready for it, and we're aligned with the right customers to mutually prosper, and we look forward to talking to you again next quarter. So thanks for being with us today.

Operator
And thank you, sir. The conference has now concluded. Thank you for attending today's presentation. You may now disconnect.