

Stifel Transportation & Logistics Conference
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Stifel Analyst: Bruce Chan

Werner Enterprises: Derek Leathers, Chairman and CEO and
Chris Wikoff, EVP, CFO & Treasurer

Bruce Chan

Welcome back. Really pleased to welcome Werner to the stage. We only have about 30 minutes here and a ton to talk about, so we'll kick it right off. Very pleased to be joined by Derek Leathers, CEO; and we've also got Chris Wikoff to handle all of the difficult questions on the finance side. So, thanks to both of you for joining us today.

As I said, there's a ton to talk about in your model. You've had some big changes announced recently, including certainly the acquisition of FirstFleet, which really firms up the Dedicated presence in your portfolio. So maybe you can give us a little color on what motivated the acquisition and how you're thinking about Dedicated as a long-term strategic driver of your model.

Derek Leathers

Sure, so when FirstFleet became available, we were excited right away. The more we got to know and learned about it, the more excited we got. I think the things we like about it a lot is it's a pure-play Dedicated company, and so there's not a lot of those out there. So, when you can find 2,400 trucks, 10,000 trailers that's 100% Dedicated with longstanding customer relationships, that's really good news. When you can find it where it lays directly over our existing network, whether that be terminal network or other Dedicated fleets and basically just where our existing density was, that's even better news.

It allows for all kinds of asset sharing, it allows for tons of efficiencies. That we can kind of manage our own destiny on in terms of how we help support not just their customers but our own. When we looked deeper and realized the breadth and depth of the relationships they had with their customers, the top four customers have been with them on average for 25 years. Their average of the entire customer base is about 17 years tenure with FirstFleet. So that's pretty exciting because what they've been doing for 25 years and 17 years respectively is selling one product to them.

And yet they've got these very deeply entrenched relationships with these customers and had only one product to sell. So, closing plus day one, you now have a whole portfolio you can bring to some relationships that have deeply embedded trust and longstanding history with one another. And so, we're excited about what that cross-selling opportunity looks like as well.

Bruce Chan

What does the move into Dedicated tell us about where shippers' minds are in terms of de-risking their portfolio? Obviously, this is something that you've been thinking about for a very long time. But just maybe give us a sense of where shippers are positioning and how they're thinking about managing risk in their supply chain.

Derek Leathers

Yes. Look, I think just the reality is, supply chains nationwide are becoming more and more time sensitive. People want everything tomorrow, if not today. We used to be fighting over two-day deliveries and then it was next day, now it's same day and now it's hours. And so, to do that, you've got more and more structure you have to put around your supply chain and Dedicated plays a major role in that. So, whether we're doing store deliveries, middle mile or we're doing final mile out the back door of the store, all of those things are where the market is moving to. So that's one issue and that's why we like it a lot. We like it, because it's resilient and the work we focus on is hard to do, hard to replicate. It's driver-involved work.

So, it's not just paying for the truck and the driver to move freight. It's – drivers are actually participating in the activities related to that particular customer in most cases. And what we've seen in our own fleet as well as in their fleet is that's what leads to decades-long relationship. Contrary to popular opinion, a lot of people worry about what's the margin profile over time. Eight out of ten years Dedicated outperforms One-Way. Most of those years, it outperforms One-Way significantly. So, we think that's pretty attractive. And so, we're going to continue to do that and play and build out sort of a longer-term, more durable portfolio.

In a market inflection, like, the one we're going through right now, Dedicated isn't the anchor that people kind of try to make it out to be. We've proven in the last major upturn, we were neck and neck with the very best players in the industry in terms of what happened with our financials and our results. So, there is operating leverage in Dedicated. Despite what people think, I mean, our ability to fill the backhauls more consistently at a better rate, our ability to see fleet add-backs into existing Dedicated accounts at higher margin contribution, our ability to see more customers migrate to Dedicated, because they are looking for that safe haven you talked about.

So, all of those things play into Dedicated being a place where we feel like we can execute on the leverage there. And then on the One-Way side, as we talked about in Q4, we did go through some painful but necessary restructuring. And although it is a little leaner and a little smaller One-Way unit, it's also better positioned, we believe, for this inflection to be able to capitalize on where this market's headed over the next several quarters.

Bruce Chan

Okay. That's a really good point. And I want to come back to that cycle commentary and the leverage opportunity. But you mentioned that Dedicated, at least your Dedicated operation, is very hard to replicate. When I think about Dedicated over the past, call it, three years or so, it's been a competitive environment. We've seen a lot of large and mega fleets move into that space. How important is differentiation in Dedicated and how do you think about differentiating the Werner model?

Derek Leathers

Well, I mean, I think like anything, right, it is important, but I'm okay with large, well-capitalized carriers moving into a space because they're doing it right. They're doing it legally. They're playing by the same rules I'm playing by. And if that's the place where the battle is going to take place, we like our chances. What I'm not okay with is like if we remained in One-Way or been overexposed in One-Way and you're competing with assets that are operating or coloring outside the lines, that's difficult to do. And so, yes, you're right,

there is more and more of the large, well-capitalized fleets that are participating in Dedicated. We've done it for decades and decades, so we know a little thing or two about it.

But in either case, it's relationship-based. It's much deeper of a relationship than you'd ever get in One-Way. It's differentiated by the quality of your driver. It's differentiated by the quality of your service. And it's something we know well. And like all of us, even the big carriers, they all kind of migrate to their own areas of specialty. We're really strong in retail. Everybody knows that, especially discount retail. But we're adding to that mix now with a lot more food and beverage, grocery, and others like technology and pharma. So, there's other advents that are growing verticals that we're participating in more and more as we go forward.

Bruce Chan

And you made mention to the cycle, that's obviously been something that investors have been very focused on over the past few months. The transport Group has finally caught a trade after several long and dark years. You're exposed to that cycle in kind of numerous parts of your portfolio from the One-Way side to the Dedicated side, as you mentioned, as well as Brokerage. So maybe we could just start by talking about your expectations for, I guess, most notably supply and how the cycle plays out. And then in terms of the different facets of your business, how you expect those to kind of benefit from the cycle.

Derek Leathers

Sure. I mean, look, so I think what's got us here today, like to the point of this inflection, if you will, has certainly been supply-driven up until now. I mean, that's been the predominance of it. It's a combination of all of the enforcement activity that's been taking place around the country. And I think there's a lot more where that came from that needs to be done. I think the current administration has got their eye on the ball and they're focused on making sure we clean up the roadways and make them safer.

So, I think you're going to see more attrition through enforcement. I think you're also seeing attrition, unfortunately, for those that didn't survive. This has been a really, really tough two, three-year period and really a week hasn't gone by in recent weeks where you haven't started to see regional or even kind of middle-tier players going under and filing for bankruptcy. So that's going to take more capacity out. I think the supply is supported, that constriction is supported further by now expanding enforcement to include driver training schools and the lack of standards and quality there, the lack of enforcement on electronic loggings and people now really focusing their efforts on getting their arms around that and trying to level that playing field to make sure we're doing what the law says. So, I think that's a further constriction.

And then it's further supported by what's happened at the OEMs. I mean, the OEMs have been devastated just like the rest of us over the last few years. And there's been wide-scale layoffs across all of the OEMs in recent years. And we saw post-COVID, when they had to go through that during the early days of COVID, it took them 18 months to two years to ever really get that capacity snapped all the way back. This time, they have the same kind of negative impetus on the front end, which caused them to kind of lean up their labor force and shorten shifts and limit after-hour shifts and things like that. But it's coupled with a lot of uncertainty around engines and EPA and everything else.

And so, they're like dealing with dual sets of suppliers right now, trying to make the old engine and then prepare for the new engine. And the new engine isn't even sort of totally finalized, like, what happens to warranty, what happens to right to repair, all of those different kind of components of it. And so, there's a lot of uncertainty. So, it doesn't bode well for their ability to suddenly ramp up and kind of mess up a good thing, if you will, by having a bunch of new trucks flow into the market.

Bruce Chan

Yes, that makes sense. I think one of the challenges for investors right now is quantifying and trying to time the impact of those supply constraints on the market. We've heard a lot of different estimates out there. FMCSA has, of course, said something like 5% of capacity that could be affected. Do you have a view on that? It seems like some of the fleets think the number could be a lot bigger. But would it be a stretch to say that we might see a 5% supply impact, this year on the one-way OTR side? And what do you think that could mean for spot pricing?

Derek Leathers

Yes. I don't think that's a stretch at all. I think that's a very low estimate, because 5% was something that originally was being talked about relative to English language proficiency alone. I think that's probably a fair estimate. It's probably light even on that one component.

When you throw in the non-domiciled CDL issue and some of the just egregious situations that are finding their way to the surface now and how some of those licenses were issued, when you couple it with the 7,000 schools being put on notice already that they either have to correct or close. By the way, that's out of a total population of about 17,000 schools.

So, if 7,000 of them get put out of business or they correct, if they correct, they've got to spend real capital and actually invest in things like trucks. Many of these schools were operating without even owning a single truck. So, it's pretty hard to train a truck driver if you don't own a truck. But yet they were doing it and doing it at mass scale. So, these things are all going to be part of this sort of supply constraint as we go forward.

What will it do for spot rates? It's hard to tell, but I mean, let's just look at where we're at today. Year-over-year, it's up 25%, which is a lot closer reflection of where rates need to be for people to be able to reinvest back in their business. Is that the end of it or the beginning? It's hard to know until we see more of this inflection.

And what we haven't seen really is the normal impetus behind any kind of turn, which is the demand side. And yet, if you look forward at demand, you look at inventory levels across the nation, they're back to pre-COVID levels or lower. You look at what's going on with the consumer sentiment and they're still hanging in there. Inflation coming in below what everybody's sort of worst fears were and now some optimism starting to build that maybe inflation isn't as bad. The potential for an interest rate cut and having the housing market come back and show some signs of life for the first time in multiple years.

All of those things just sort of have the potential to add fuel to the fire. We're going to build our plan on trying to run as lean and mean as we can. We're going to build our year around what's already happened on the supply side with some estimation and some expectation that more will come in terms of more constraint. And the demand is just sort of an extra, that's sort of the gravy if that happens and comes back. But right now, our retailers we do business

with are doing well. They're well-run companies and their results are positive relative to volumes. I get hit with today multiple times about a particular retailer or two whose maybe stock price hasn't appreciated the way they would have liked. But I don't haul stock price, I haul goods. And so if they're pushing more volumes through the business, we have more freight to haul. And that's what matters in our network.

Bruce Chan

That's right. We haul stock price.

Derek Leathers

Yes. Yes. You've been backhauling way too much.

Bruce Chan

That's probably right. In terms of the retailers and the shippers, I mean, obviously, there's a broad range of sophistication. We probably have some in the audience right now. But when you have conversations with them, do you think they are appropriately considering the setup for this year in terms of that demand commentary and that supply commentary that you just talked about?

Derek Leathers

Yes. I mean, I think that absolutely depends on the retailer you're talking about and the level of sophistication. Look, nobody wants to, nor do we, want them to have to spend more money. We do not want that. We want to find ways to find efficiencies in their network, where maybe you can offset it with some modal shifts, maybe some truckload becomes intermodal. Maybe some LTL becomes truckload. There's things we can do to offset it. But it's always astonished me, the really fair, appropriate sort of strategic retailers when it comes to their supply chain, they're the same ones that win quarter after quarter after quarter with their own bottom line results.

And so there are people out there that, yes, they're not going to pay you a penny more than you're worth, but they'll pay you every penny you've earned. And those are the folks that win. And you see it in their same store sales and everything else. And so I've got this, I'm a Southern kid at heart and I have a lot of dumb sayings, but one of them is just alignment with winners. I challenge our sales team all the time. I want us aligned with winners, because the people that win in their space win in their supply chain too. And they may be aggressive with what they expect, but they also realize the rarefied air that it takes to deliver on those expectations. And so you do have a better shot of being compensated fairly.

Bruce Chan

And at this point in the bid season, I know it's still somewhat early, but when you look at those shippers versus where they were a year ago or two years ago, are you seeing an indication that that sentiment is coming through?

Derek Leathers

Yes. Again, it's a very mixed basket of goods, because you have other ones that think they're going to cut their way to profitability. And the problem isn't what they paid for trucking. It's the quality of the goods on the shelf or the execution in their four walls that's driving their final outcomes. The ones that understand and place a value on supply chains, we're having pretty good outcomes right now. On a like-like basis, we just had our earnings call last week,

we talked about this, but we're looking, we believe mid-single-digit type rate increases is where the industry can support this year.

I think it's going to need to be a multi-year phase. All you have to do is look at, trucking CPI or cost of trucking over the last three years and compare it to rates. It's pretty easy to figure out how you had a publicly traded truckload universe collectively operating with a 1% or 2% margin. Not sustainable, doesn't cover the cost of capital, isn't something that we can do forever. And so it's just working with the right folks to have a longer-term view. But nobody's walking into the meeting going, how much more can I pay you today?

Bruce Chan

Hopefully that comes soon. Maybe just in terms of timing, again, I think the market is starting to capture the possibility that that tightening happens. But when we think about things on an operating basis, are there points in the year that you're expecting to see some of these tightening events become a little bit more acute? I know we've got Road Check Week sometime in May. March is maybe when we start to see the seasonal ramp in freight volumes. What are the kind of big bookmarks in the year in terms of where we start to see some of these impacts come through?

Derek Leathers

Yes. So coming into the year, there's several milestones we look for and look to see what the market does immediately thereafter. The first and most obvious one is what happens with the first storm. I think we've already seen that, massive inflection in rates, spot rates going up double digits almost overnight, rejection rates hitting 14.7%, which are COVID-level type rejection rates. That doesn't happen if capacity is loose. You could have a storm and the recovery is quicker, the impact on rates is lesser, all of that.

The second one is what happens relative to the reefer business about this time of year because people underestimate the impact of flower season, not flour as in baking, but flowers as in order them for your wives for Valentine's Day flowers. And so, we've seen reefer rates, both storm-affected as well as flowers starting to dictate that rate higher than normal seasonality. You then get into obviously early produce season, mower and blower season. So, there's a large kind of pre-spring surge with certain retailers across the country with what I refer to as mower and blower. But what I really mean is anything outdoors. So, patio furniture and the like, and so we're seeing a lot of that order book look pretty solid.

And so we'll just keep monitoring those milestones, Road Check is, another one, obviously. End of June surge, we haven't seen that in many years. But, there was always a second peak year-in and year-out that always takes place at the end of the second quarter. And in the last few years, that's been very muted. So that would be a big milestone to clear this year and see what happens across networks at that time frame.

Bruce Chan

All right. Well, good reminder to put in your Valentine's Day orders and support Werner volumes.

Derek Leathers

Please.

Bruce Chan

We had a panel earlier this morning that talked a lot about USMCA. Obviously, there's a big decision coming up in a few months about whether that agreement is going to get renewed. Mexico cross-border is something that's certainly near and dear to your hearts, not just personally, I know your connection there, but also in terms of the business, Werner's been one of the leaders in terms of that capability. So just given all the changes with trade policy, given USMCA, how are you positioning for that opportunity? Is that opportunity better today than it was? Are there risks there?

Derek Leathers

Yes. I mean, so if you look out and you take the long view, I think the opportunities are better than they've ever been. You look at what's happened with foreign direct investment in Mexico over the last three years. It's set back-to-back-to-back records. The mix of that direct investment has been higher and higher U.S.-funded. So that's a very interesting phenomenon and one that bodes well for North American trade. It takes a while for that direct investment to translate into increased freight, but it's happening. So, we're bullish on Mexico. There's some obvious constraints and concerns around infrastructure in Mexico, safety and security.

When I say infrastructure, I'm literally talking roads, water, and electricity. They've got to get their arms wrapped around it. They're going to have to figure that out based on the amount of investment going on. But our position there is strong. We have the largest presence on the southern border with our terminal in Laredo. We have terminals and crossing points across the entire southern border. We're excited about what that future looks like. And the conversations with customers are very positive. It will take time to translate to like significant increases in freight.

And the other reason we're bullish on Mexico, frankly, is it's hard. It's hard to do well. We do it very well. And there's less competitors. I mean, it's a place where for years there was really 5-ish quality players. During some of this nefarious activity era that we just went through over the last four years, there was lots of new startups that were coloring outside the lines, using B1 drivers, operating with cabotage, things like that. But as those outlets get tightened down or clamped down on, I think you'll get back to really a subset of less than 10 carriers that can do it well, and maybe even all the way back to kind of that five threshold. And being one of, if not the leader of those five, is a place we'd like to be.

Bruce Chan

Great. We've got about 10 minutes. So, just want to do a quick poll for questions. If you have any, we'd certainly be happy to take them. Otherwise, I've got lots more here. But I want to maybe talk about, some of the technology discussion that we've been hearing in the industry for at least a couple quarters now. A lot of companies talking about AI investments, tech investments. You've certainly done a good bit of that yourselves. Where is the focus right now for Werner? Maybe give us an update on the EDGE rollout and how that's gone and what's on the horizon for you.

Chris Wikoff

Yes, maybe I'll take that one. You mentioned the EDGE TMS rollout. We started that a couple of years ago as part of a broader technology transformation, a multi-year journey. We're in some of the later innings on rolling out EDGE, getting more volume, really with the goal there of having complete visibility of all freight opportunity, customer freight across our portfolio on the asset side, on the asset-light side. So full visibility where we can decision

better, we can decision faster, we can develop more solutions that optimize our own network and make it more cost-effective and efficient for our customers. So that really is the goal. And like I said, we are in the later innings and making good progress there.

Relative to AI, we are seeing some proof points of AI across our business. But really where I think we're going to get greater momentum and shift from some smaller AI applications and synergy around the fringe to some bigger benefits is with all of the data that really comes together by getting everything operationally onto a single platform. And that's where we can harness that data. We can connect those points, and that becomes the intelligence behind bigger AI opportunities, bigger synergies to come. So we are focused on it. That's not to say that that we're not seeing on a smaller scale some opportunities of AI right now. We are seeing it across our business, whether particularly where we have some of that data already centralized and usable.

Cases like optimizing freight selection, optimizing putting shippers and carriers together within our Brokerage business in an intelligent fashion. And then other cases that may be more nuanced that individuals may not think about, like putting more intelligence and streamlining preventive maintenance, predictive maintenance across our assets in things like warranty. When you have over 7,000 tractors on the road at any given time, a lot of equipment, a lot of parts, as we purchase our tractors, we buy the extended warranty, and there's just a lot of complexity in processing warranty claims and optimizing that. The work is one thing. The output and making that effective and maximizing that is another thing. AI has helped us do that.

So we are seeing those use cases. That's continuing to grow. To be honest, I think we're just scratching the surface. And as we get further in our technology journey, I think it will open the gates and the opportunities to have more AI benefit as we go forward.

Bruce Chan

Yes. That's a really interesting point. I mean, I guess procurement and warranty and maintenance is always something that Werner has done well. And I guess when you think about the application of AI there, any thoughts around what the magnitude of that could be on an OR basis, if that's a fair way to put it?

Derek Leathers

Yes, I think we're early enough now that it's difficult to try to quantify for you. But I can tell you that, the warranty examples a great one, right? Like, we have an entire department that works on warranty claims and making sure that we're submitting for warranty reimbursement across a wide range of different types of repairs. But AI finds things that humans would have a very difficult time doing. The connective tissue between part A that's went down, but it's actually part of, and it was a chain reaction because of part B or C. B and C are warranty items. Therefore this should be, and at least challenging our assumptions on what should or shouldn't be covered by warranty, and our ability to go back and push back and ask for reimbursement where reimbursement is the right answer. That is just a level of complexity that it's hard for individual humans to do at the rate and speed at which AI can do it.

And we're going to keep driving further. The other real-life example that I love a lot right now is working with both predictive maintenance but also driver interaction on what's going wrong or feeling wrong with the truck, and then being able to use technology to bounce it against inventory levels at a specific location and have ordered parts and parts ready and

standing by the time the truck gets there, versus racking and stacking parts for no reason and sitting on them for extended periods of time. All of which you can start to visualize is pretty significant savings, but you've got to do it at scale for it to really matter and move the needle on OR. And these are pilot tests that we're rolling out as rapidly as we can within a controlled environment to make sure we work the bugs out first.

Bruce Chan

So, speaking about costs, there's certainly been a lot of inflation in the business really across the P&L when you think about equipment, when you think about insurance. And that's a little bit of a double-edged sword because on the one hand, obviously that increases your cost to serve. But on the other, I think it also helps with the competitive differentiation, especially for those fleets that aren't able to meet those rising costs as effectively. So I'll ask you a double-edged question. When you think about your P&L and your expense lines, what is creating the most pressure right now? And what do you think the implications of that are for the next cycle as far as, you know, maybe a more disciplined market?

Chris Wikoff

Yes. So, inflation has moderated a bit. It's not as widespread up and down the P&L. But it still exists in pockets, to your point, Bruce, on insurance, employee benefits, tariffs, equipment, and down into a variety of different parts, whether it be tires or other things. So inflation is a factor. That's why we've put so much focus on cost discipline, cost containment, looking for ways to be more efficient for sustainable, structural cost savings that we can realize. Over the last year three years, it's over \$150 million of cost savings that we've identified, again, largely structural and sustainable through that cost discipline. And the reality is that has helped to mitigate the impact of inflation in the last three years where it's been difficult to see any other benefit and offset through rate or anything else.

Now, with a better macro and a better backdrop as we go forward, that discipline is not going to fall off. That's part of our DNA and what we do, and we'll continue to do that. Not to jump ahead to FirstFleet and that acquisition, but we've talked about as part of that an opportunity to take good margins to great margins by focusing on cost synergies, \$18 million being cost synergies that we've already identified and have a high degree of confidence to achieve over, call it, the next 18 months.

Bruce Chan

Okay, great. Last couple of minutes here. I just want to make sure there are no other questions out there in the audience. Maybe just to kind of finish up and tie it all back together. We talked about some of the inflation issues. We talked about the opportunity for pricing this year, especially with supply out. Is this the year where you think that you'll fairly comfortably be able to earn pricing above inflation after, as we said, a couple of long dark years?

Derek Leathers

Yes, I mean, I think the setup is good to be able to take and have both the combined impact of another round of cost takeout coupled with some rate relief, given the market dynamics right now where we can start to expand margins in 2026. But we have a long road to go, not just Werner, but the entire industry. I don't recall in my 35 years ever seeing a two-year stretch where if you took the publicly traded truckload group and averaged their margins over the course of that time, that you're talking about sub-2%. I mean, that is nowhere near reinvestable, nowhere near, where it needs to be. And so we've got to take several bites at this

apple. We've got to find ways to both have rates come up to offset some of this pressure. But we also have to continue to find ways to become more efficient.

The supply side story, I think, is in the middle innings, not the later innings. And I think people underestimate, I never finished the answer earlier. You asked about what percent. Well, if you take the over-the-road trucking environment, people love to talk about 3 million trucks out there, but that's includes dedicated and private fleets and all these other things. By the time you whittle it down to what is over-the-road trucking for hire capacity, that number is a lot closer to 1 million trucks. Maybe it's 1.2 million trucks, maybe it's, 1.3 million trucks, but it's a lot closer to 1 million trucks. The publicly available data that's already been widely proliferated shows that somewhere between 250,000 and 500,000 of that million are outside the lines, whether that be non-domiciled CDLs, ELP issues, the ELD - electronic logging issues where they're being dispatched out of other countries and having hours reset on a daily basis. So, if a third of that capacity is in jeopardy, that's a pretty significant change of the game.

Now, will it all wash out in 2026? No. They're going to continue to find ways to evade and avoid, but I also think enforcement is continuing to ramp up. And one thing the administration has shown a bit of tenacity for, is enforcement. And so, I think they'll continue to stay on this because it is a safety issue for America's roads.

Bruce Chan

All right. Well, on that note, we're getting the flashing red warning light on time here. But it seems like it's going to be an exciting year, not just for you but for the industry. So, we're looking forward to watching the progress. I want to give a big thanks to Derek and Chris for joining us today. Big thanks to Werner.