

Watchlist Investing

Patently finding and following great public companies

Issue #33 | January 2024



“One person said to me, 'I have a list of 300 potentially attractive stocks, and I constantly watch them, waiting for just one of them to become cheap enough to buy.' Well, that's a reasonable thing to do. But how many people have that kind of discipline? Not one in 100.” – Charlie Munger

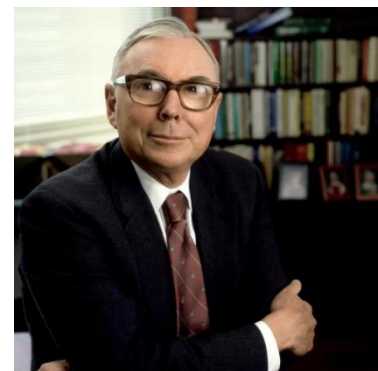
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This first issue of 2024 is dedicated to Charlie Munger, my hero and intellectual grandfather, who died just shy of his 100th birthday, in November 2023.

Charlie’s wisdom continues to guide my thinking in investing and in life.



Editorial comments / notes: Last year I began a transition to providing more updates on companies already on the Watchlist rather than just one-and-done Deep Dives. In 2024, I would like to strike the right balance between the updates, which are important to the type of patient, disciplined investing I subscribe to, and prospecting for new names to add to it. My initial thinking for the year is as follows:

1. Three to four new names, such as this month’s Deep Dive on Mainfreight
2. Two or three industry updates, such as the May 2023 banking industry update, to give specific updates on multiple companies within the broader context of the industry
3. Half a dozen or more specific company updates (the two-pagers)
4. Russell Rebalancing additions and deletions (double issue June/July)
5. One or two Deep Dive refreshments. Some early issues, like Hingham Savings, will be three years old this year. It is time to provide comprehensive updates to a few of them.
6. Berkshire Hathaway update in April. This is a “cornerstone” issue on the calendar every year.

This list looks like a solid year’s work and deserving (I hope) of the \$299 price tag.



Deep Dive

Mainfreight, Ltd

(Tickers: XNZE: MFT | OTC: MFGHF | Disclosures: None)



Mainfreight came on my radar thanks to [Jessie Rancourt](#), a friend and fellow value investor, who mentioned it during a subscriber meetup a few months ago.

Mainfreight is in the supply chain logistics industry, an extremely broad category covering a huge segment of the world economy and harboring (pun intended) many niches and specialties. I decided a look at the company would fit in well with my coverage of [Old Dominion Freight Line \(ODFL | Disclosure: None\)](#) in the U.S. less-than-truckload space and [Triumph Financial \(TFIN | Disclosure: Long\)](#) in the banking-cum-truckload finance space.

Mainfreight is based in New Zealand with offices around the world and provides shipping services to companies primarily in customer verticals such as food, beverage, DIY, pharmaceuticals, perishables, and retail. Its three segments give a good idea of how it makes money: transport (via road and rail, sometimes with its own fleet), air & ocean (contracting with other service providers), and warehousing (though its own or contracted space).

The company is run by its founder and appears to have maintained a decentralized, entrepreneurial culture. I like what I see in the numbers, in management, and the fact that it is an interesting combination of network benefits and semi-capital intensity. There's also ample room for reinvestment and a long runway ahead. It is a worthy addition to the Watchlist.

A simple but not easy growth strategy (from the 2019 annual report):

THE KEY TO NETWORK INTENSIFICATION

- > Be where our customers need us
- > Trust those closest to our customers to make the decisions. They know more and can do a better, faster, job than someone 100 kms away
- > Expand the network to maintain continuous custody of customers' freight and control quality

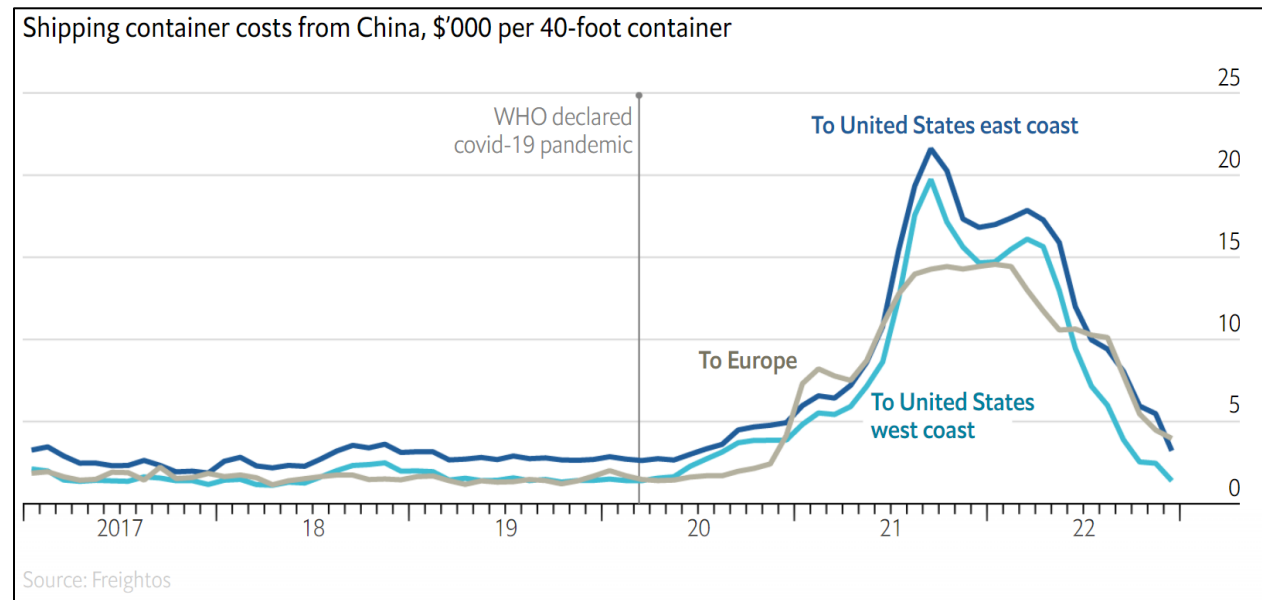
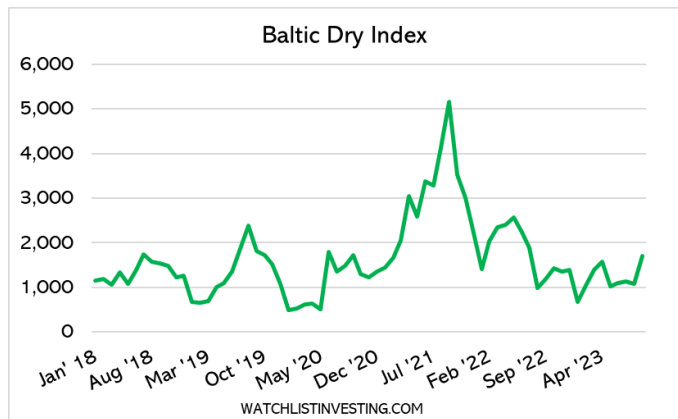


INDUSTRY OVERVIEW:

The worldwide market for shipping / logistics services is huge at about \$10.7 trillion or 10% of world GDP in 2023. Third-party logistics services, like those provided by Mainfreight, account for \$1.3 trillion worldwide, still a huge number. Safe to say that the market is highly competitive and not subject to control by just a handful of competitors, though there are some very large players. Demand for services depends on world GDP and cross-border trading volume. E-commerce is a driving factor in the industry.

One measure of worldwide pricing of logistics services is the Baltic Dry Index. The spike in mid-2021 is evident no matter what index you use. Pandemic-induced demand caused havoc on the global supply chain and resulted in delays and prices going through the roof.

Here's data provided by the Economist in January 2023:





Ocean Freight: Measured in TEUs (twenty-foot equivalent units), ocean freight forwarding volume worldwide was around 67 million units. Note that the global volume for total TEUs through all ports was 851 million units in 2021. Globally, the capacity of container ships has increased from 11 million dwt (deadweight tons) in 1980 to 26 million dwt in 1990; 64 million dwt in 2000; 169 million dwt in 2010; 275 million dwt in 2020, and 293 million dwt in 2023.

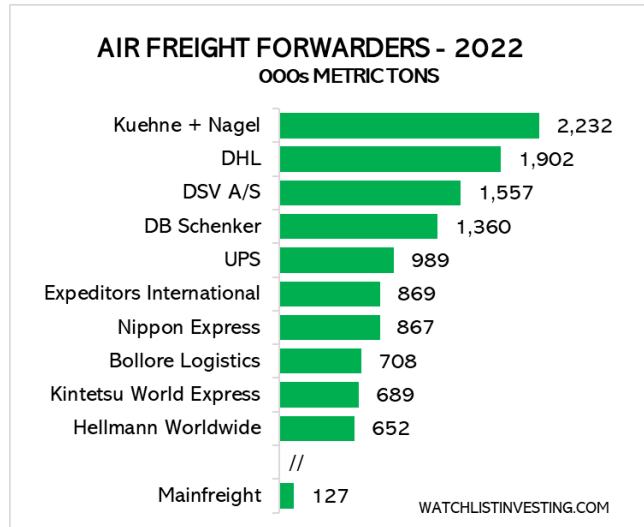
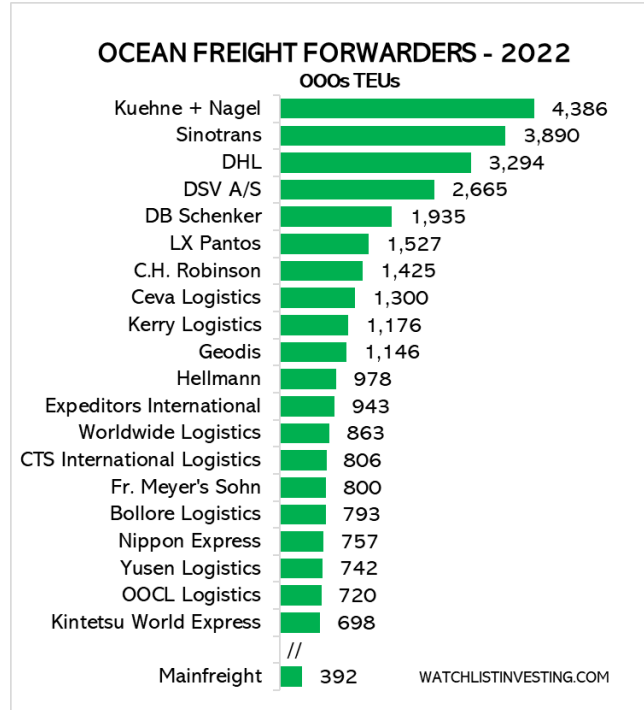
In 2023, Mainfreight moved 0.43 million TEUs over ocean (ranking 29th) while Kuehne + Nagel, the largest, moved 4.39 million. C.H. Robinson, by contrast, ranked 7th with 1.43 million TEUs.

Air Freight: The global air freight market was forecast to be about 57.7 million metric tons in 2023. In dollar terms it is valued at approximately \$142 billion.¹ Kuehne + Nagel again ranks first in air freight while Mainfreight comes in at 28th.

Land Freight: Global land freight statistics are hard to come by and not as relevant as regional or local statistics.

In 2022, Mainfreight moved 7.3 million tons of freight over land.

Warehouse Space: Mainfreight had just over 1 million square meters of warehouse space at the end of 2022. This compares to K + N having 10.3 million square meters. Here K + N ranks 15th while Mainfreight doesn't even make the list. The industry leader for dry storage warehouses is DHL with 150 million square feet across 520 warehouses. Second is Ryder Supply Chain Solutions with 95 million square feet and over 300 warehouses.



¹ Source: [IATA Industry Statistics](#)



BUSINESS MODEL:

The business model of a logistics company is simple when it gets right down to it, though the execution is difficult. It’s all about moving goods as efficiently as possible from Point A to Point B.

Logistics companies come in all sorts of flavors. On the one extreme are asset-based companies that own the physical infrastructure. Others are non-asset-based (“asset light”²) and simply manage the shipping process (to greatly simplify), contracting with asset-based companies for their space and availability.

Companies like FedEx and UPS own a ton of delivery infrastructure and move packages across the globe all the way to your doorstep. On the other end of the spectrum is a company like C.H. Robinson whose job it is to employ people who manage the shipping process on behalf of others, contracting with land, ocean, and air freight companies to move parcels anywhere they need to go and handling customs / border paperwork, etc.

Revenue / net fixed assets provides a good indication of capital intensity. You see Mainfreight is more asset intensive, which reflects the company’s ownership of physical delivery and warehouse assets. Both asset-based and asset-light logistics businesses can have moats protecting returns on capital.

COMPANY	TICKER	REVENUE	NET FIXED ASSETS	REVENUE / NFA
FedEx Corporation	FDX	\$90,155	\$58,045	\$1.55
United Parcel Service Inc	UPS	\$100,338	\$38,474	\$2.61
Mainfreight Limited	MFGHF	\$3,523	\$1,298	\$2.71
GXO Logistics Inc	GXO	\$8,993	\$3,187	\$2.82
JB Hunt Transport Services Inc	JBHT	\$14,814	\$4,980	\$2.97
Deutsche Post AG	DHL	\$94,436	\$28,688	\$3.29
Forward Air Corporation	FWRD	\$1,973	\$391	\$5.05
Hub Group Inc	HUBG	\$5,340	\$887	\$6.02
DSV Panalpina A/S	DSDVF	\$33,557	\$2,987	\$11.23
Expeditors International	EXPD	\$17,071	\$1,009	\$16.91
RXO Inc.	RXO	\$4,796	\$278	\$17.25
Kuehne & Nagel	KNIN	\$39,398	\$2,157	\$18.27
Landstar System Inc	LSTR	\$7,437	\$315	\$23.61
Echo Global Logistics Inc	ECHO	\$2,512	\$70	\$35.71
CH Robinson Worldwide Inc	CHRW	\$24,697	\$532	\$46.46

Notes:
Data from Quickfs.net.
Mainfreight ticker MFGHF is the unsponsored ADR.

PARTY TIME!!!

The logistics industry can be split into five different segments:

1PL (First Party Logistics):
The producer or receiver of goods, handling their own logistics. Example: A manufacturer using its own trucks to transport products.

2PL (Second Party Logistics): Provides transportation services such as shipping or trucking companies. Example: A dedicated freight carrier or a commercial cargo shipping line.

3PL (Third Party Logistics): Offers comprehensive logistics services including transportation, warehousing, and fulfillment. Example: FedEx or UPS providing package delivery, warehousing, and distribution.

4PL (Fourth Party Logistics): Manages resources, technology, and infrastructure of the entire supply chain for a client. Example: Amazon’s fulfillment services on its e-commerce platform.

5PL (Fifth Party Logistics): Provides strategic, innovative supply chain solutions, often through technology and data analysis. Example: A company like IBM offering integrated supply chain solutions with advanced analytics.

² RXO, a recent spinoff of XPO, annoyingly mentions the fact it considers itself an asset-light company no less than 14 times in its 2022 10K, including four times in half a page in the company overview section. It reads more like an advertisement than a statement of fact. – End rant –



COMPANY HISTORY:

Mainfreight continues to be run by its founder, Bruce Plested. The company has grown steadily, becoming one of the largest logistics companies in New Zealand and ranks in the top 30 worldwide. The history below is largely sourced from the company's [website](#).

1978	Mainfreight founded by Bruce Plested on March 6 th
1979	100-year vision adopted
1984	First Air & Ocean branches open in Christchurch and Auckland, New Zealand
1989	Began operating in Australia as Mainline Distribution
1991	First warehousing branch opens in Auckland
1994	Acquired of Daily Freightways and Chemcouriers in New Zealand
1996	Listed on the New Zealand Stock Exchange
1998	Opened 50 th branch and celebrated 1,000 th employee
1998	Entered Asian market with partial acquisition in Hong Kong (balance acquired in 2007)
1999	Entered the United States market through the acquisition of CaroTrans (balance in 2000)
2003	Acquired Owens Group in New Zealand (balance in 2005)
2004	Opened 100 th branch
2006	Welcomed 3,000 th employee
2007	Expanded into the United States with the acquisition of Target Logistics (34 offices)
2009	Revenue reaches NZ \$1 billion
2011	Opened 200 th branch and welcomed 5,000 th employee
2011	Acquired Netherlands-based Wim Bosman Group
2014	Celebrated operations in 20 countries
2022	Opened 300 th branch and welcomed 10,000 th employee
2023	Global warehousing footprint exceeds 1 million square meters

MANAGEMENT / OWNERSHIP:

- **Bruce Plested, Chairman and Founder (81):** Plested founded Mainfreight and has chaired the board since 2002. He has eschewed a salary and directors fees since at least 2014. He owns 14.8% of the company.
- **Don Braid, Managing Director (63):** Braid has been with Mainfreight 29 years and was in the industry 16 years prior to that. He was paid \$3.5 million in 2023. He owns 2.9% of the company.

In addition to Plested and Braid, the Mainfreight board consists of four independent directors, each of whom is paid \$120,000 for their services. Update: As of January 2024, the company nominated two additional independent directors.



KEY VARIABLES / METRICS:

Key Metric #1: Volume

A logistics business is all about moving “stuff”. How much stuff can be measured in tons (or tonnes)³ on land and air, or twenty-foot-equivalent units (TEUs) for sea freight. Also important is the volume of warehouse space. Related are the number of branches and countries, which give an idea of the level of worldwide breadth the company has achieved.

Volume	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Land freight tonnes	(1)			6,148,933	6,866,867	7,349,327	7,700,213	7,660,242	7,286,572	7,321,452
Air freight tonnes	73,367	86,547	113,120	121,553	127,174	126,669	126,071	114,736	138,279	126,941
Sea freight TEUs	230,320	251,685	267,144	280,539	311,586	342,143	337,504	347,638	424,610	392,279
Warehouse footprint (sq. meters)	410,979	465,042	524,795	578,724	614,037	679,225	729,684	804,288	929,502	1,041,016
Branches	233	242	239	239	247	260	282	297	305	331
Countries	20	20	21	21	22	24	26	26	25	26

1. Data on land freight tonnes prior to 2017 did not include Europe and would not be comparable. No company-wide total was available to back into European volume.

Key Metric #2: Capital intensity

Key Metric #3: Operating margin

Capital requirements & ROCE	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	
<i>Avg. as % revenues:</i>											
Core working capital	(1)	2.3%	2.1%	1.8%	1.9%	2.6%	2.5%	2.5%	2.3%	2.1%	1.9%
Net fixed assets, ROU assets, software		21.0%	22.9%	24.6%	26.1%	23.8%	22.8%	34.9%	42.1%	31.5%	34.3%
Total capital employed		23.3%	25.0%	26.4%	28.0%	26.4%	25.3%	37.4%	44.4%	33.6%	36.2%
Revenue / avg. capital employed		\$4.29	\$3.99	\$3.79	\$3.57	\$3.79	\$3.95	\$2.67	\$2.25	\$2.98	\$2.76
Operating margin		6.7%	5.9%	5.9%	6.6%	6.2%	6.8%	7.4%	8.0%	9.8%	10.8%
Pre-tax return on capital employed		28.8%	23.7%	22.5%	23.4%	23.7%	26.9%	19.8%	18.1%	29.1%	29.8%
After-tax assuming 25% tax rate)		21.6%	17.8%	16.9%	17.6%	17.8%	20.2%	14.9%	13.6%	21.9%	22.3%

1. Core working capital = total current assets minus cash, trade creditors & accruals, and employee entitlements.

Capital intensity and operating margin cannot be assessed wholly independent of one another since they interplay depending on business type. Trends over time are important. In the case of Mainfreight, it's clear that its investment in net fixed assets (primarily warehouse space, as seen in the growth in the volume section), is causing the business to operate with more capital per dollar of revenue. Said another way, revenue per capital is declining, as seen in the bolded figures below.

On the other hand, looking at operating margin we see an upward trend from around 6% in 2014 to almost 11% in 2023. Note that the freight boom in the 2022 into 2023 surely pushed margins above trend.

Put capital intensity and margins together and you get pre-tax return on capital employed. Mainfreight clearly has made a tradeoff between gaining more margin at the expense of greater capital intensity. One can look at this in several ways. First is the ‘why bother’ question to which the answer is (I think) that investing in physical infrastructure allows greater control of the system which results in greater customer service, which results in greater growth. The other aspect is the ability to put capital to work at satisfactory rates of return. Sure, a high return business is great, but the *value* of a business with a slightly lower return profile with greater and longer reinvestment prospects could be higher, all things being equal.

³ I'll use ton and tonne interchangeably. However, it is important to note that ton is imperial units and is equal to 2,000 pounds. A tonne is metric and equal to 1,000 kilograms or 2,204 pounds.



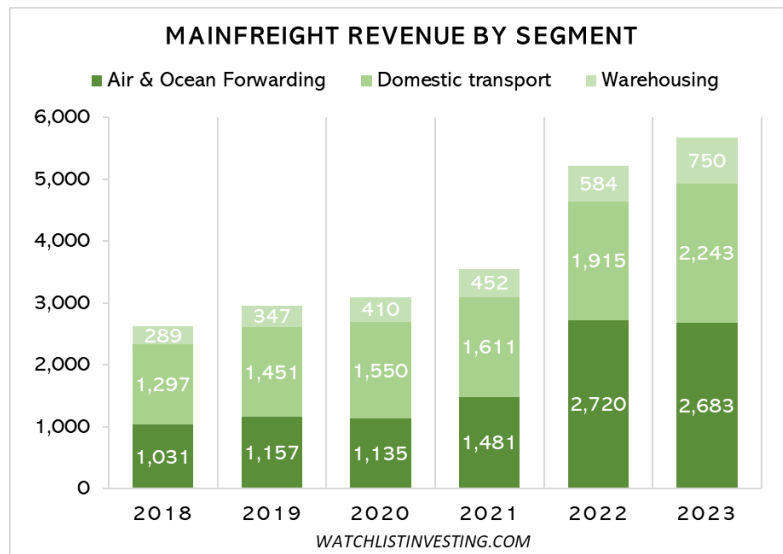
FINANCIAL ANALYSIS:

Mainfreight Dashboard										
Figures in NZ \$mil										
	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Total revenues	\$1,924	\$2,054	\$2,285	\$2,334	\$2,617	\$2,954	\$3,095	\$3,544	\$5,218	\$5,676
Revenue growth	2.1%	6.8%	11.2%	2.1%	12.1%	12.9%	4.8%	14.5%	47.2%	8.8%
Transport costs % revenue	63%	63%	62%	61%	61%	61%	58%	60%	64%	61%
Labor costs % revenue	20%	20%	20%	20%	21%	21%	22%	20%	17%	18%
Operating income	129	122	136	153	164	201	230	284	510	612
Operating margin	6.7%	5.9%	5.9%	6.6%	6.2%	6.8%	7.4%	8.0%	9.8%	10.8%
Cash	56	65	94	75	81	115	116	140	202	342
Core working capital	(1)	38	48	34	56	78	67	88	74	140
Net fixed assets, ROU assets, software	423	520	603	614	632	718	1,445	1,540	1,748	2,145
Net debt + leases	209	245	265	213	197	130	784	688	612	658
Shareholders' equity	442	509	581	646	710	838	966	1,115	1,429	1,727
Net debt / equity	47%	48%	46%	33%	28%	16%	81%	62%	43%	38%
Shares outstanding (000s)	99,303	99,788	99,946	100,547	100,699	100,699	100,699	100,699	100,699	100,699
Growth capex (neg. = net investment)	(29)	(92)	(54)	(18)	(17)	(36)	15	64	12	(75)
Acquisitions	(1)	(2)	(0)	0	(0)	0	0	0	0	0
Dividends	(28)	(33)	(34)	(40)	(43)	(48)	(59)	(64)	(101)	(173)
Change in debt & leases	0	45	49	(71)	(11)	(32)	655	(73)	(13)	186
Change in core working capital	0	6	(7)	13	25	(18)	20	(25)	40	(69)
Revenue / avg. capital employed	\$4.29	\$3.99	\$3.79	\$3.57	\$3.79	\$3.95	\$2.67	\$2.25	\$2.98	\$2.76
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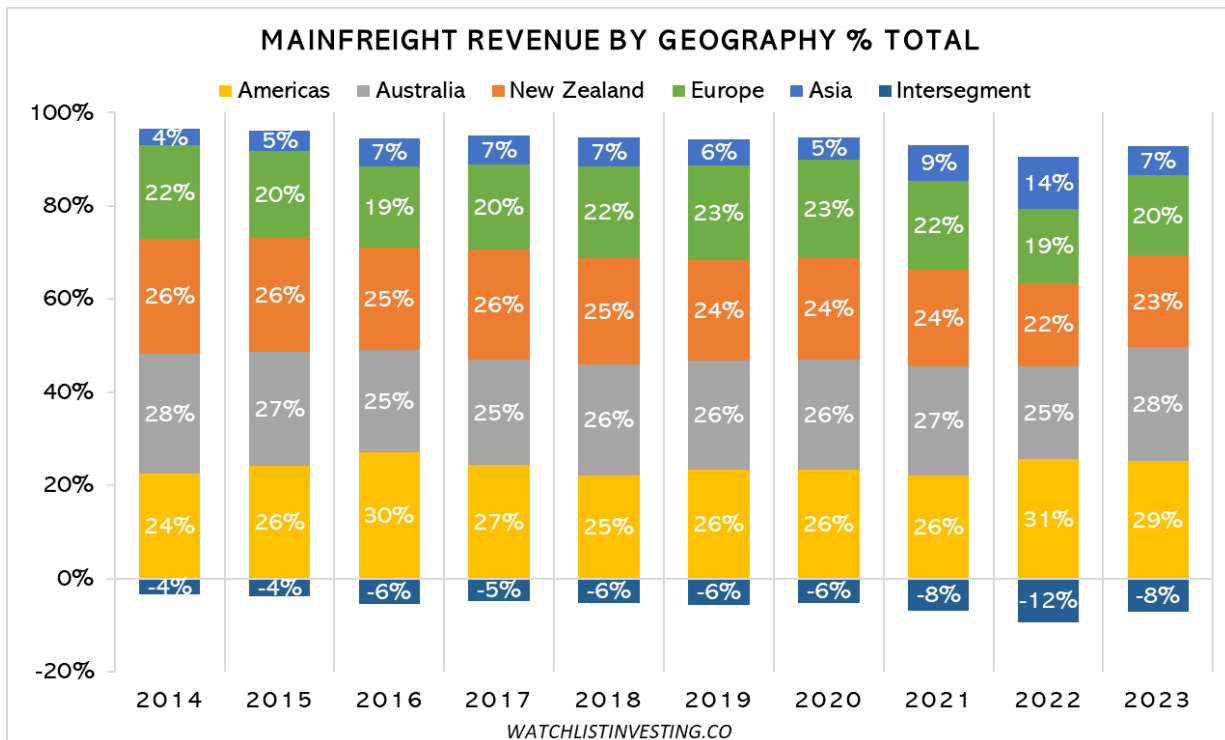
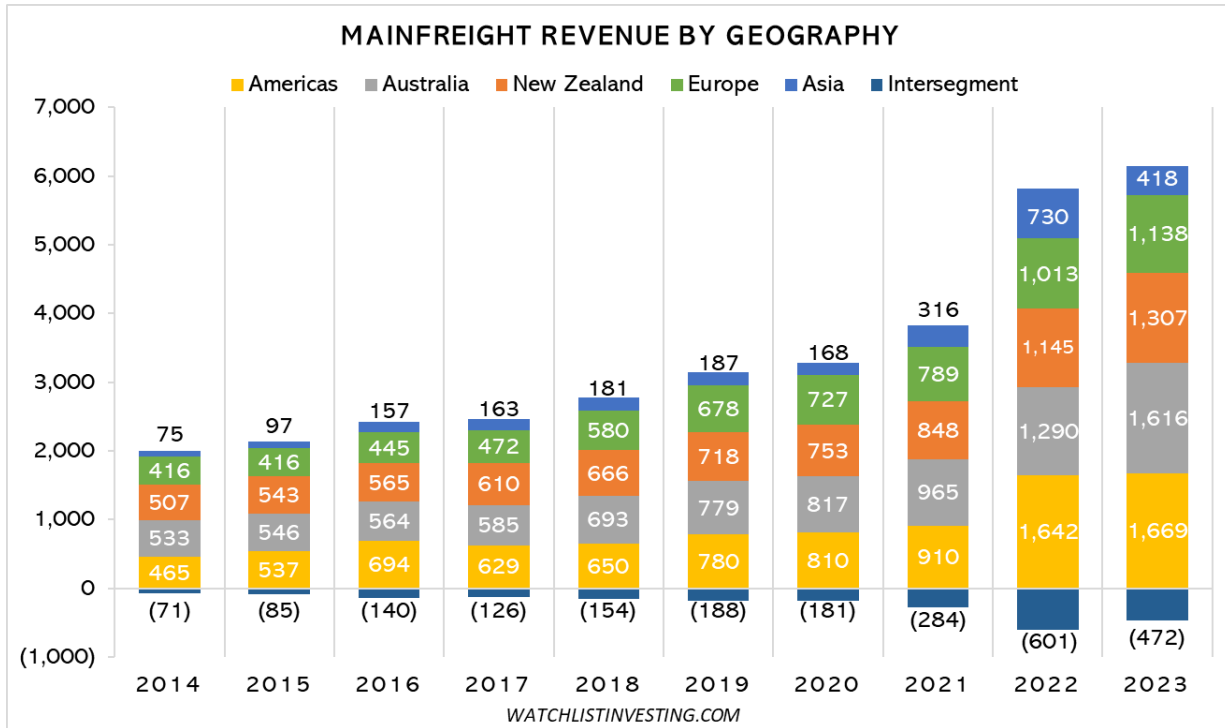
1. Core working capital = total current assets minus cash, trade creditors & accruals, and employee entitlements.

2. Data on land freight tonnes prior to 2017 could not be determined.

Mainfreight breaks its revenue down by segment and by region. Looking at each gives us a clue as to the growth trajectory of the business. Unfortunately, the segment revenue detail gets a little fuzzy prior to 2018. Nonetheless, it shows the company's international expansion efforts, with warehousing and air & ocean forwarding growing by over 2.5x compared to just 1.7x for domestic transport.



Turning to geography, we can see the clear shift toward Australia as the first natural expansion point for the business and then to the Americas, which now represents the largest revenue segment by geography.



Here I think it is worth discussing capital expenditure to put a finer point on the type of business being conducted in each region. Mainfreight is, first and foremost, a New Zealand company. It began in NZ and grew to become the one of the largest logistics companies on the island. Its natural expansion from there was to Australia. This is reflected in capex by region (see chart on next page).

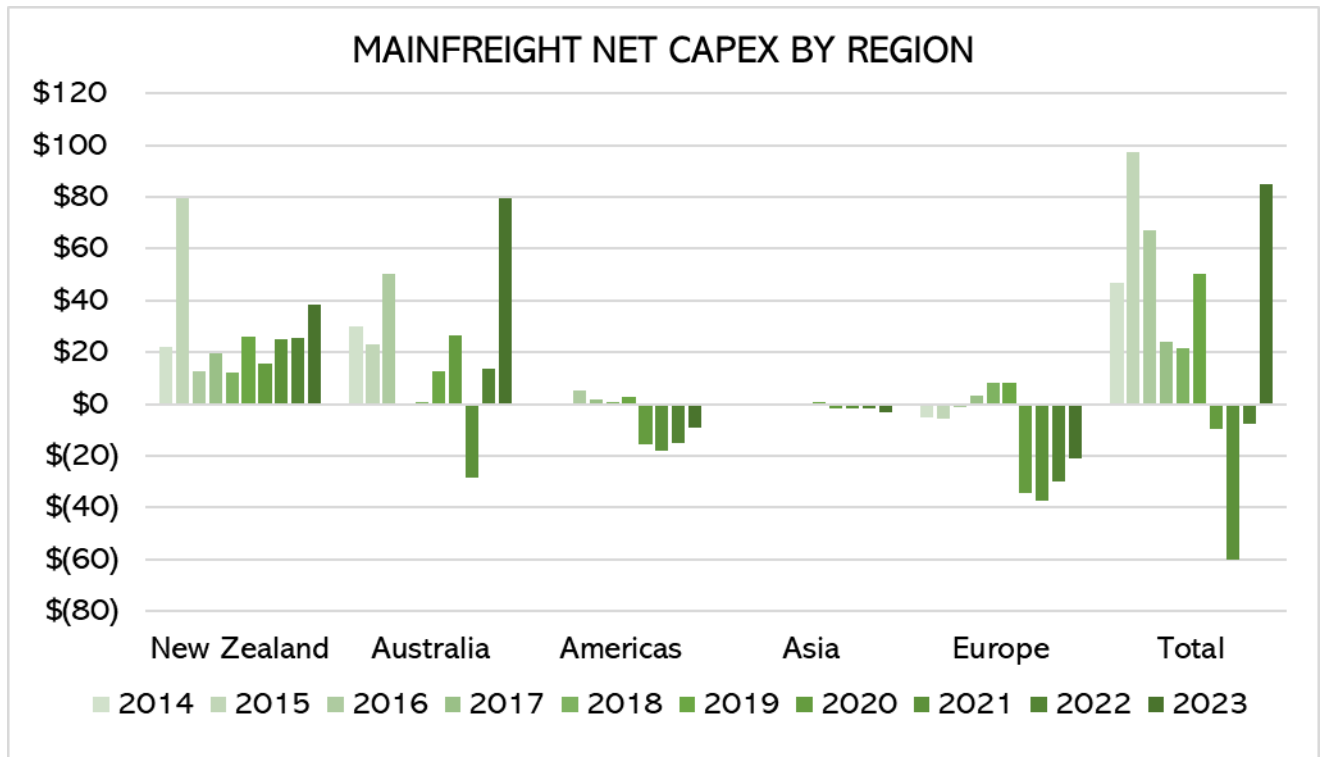


In New Zealand primarily and to a lesser extent in Australia, Mainfreight operates as an asset-intensive logistics company. It owns trucks and warehouses, the physical infrastructure necessary to move goods around. Its activities in the other regions are more heavily focused on the brokerage side and warehousing as evidenced by the growth in revenues with comparatively little (or negative) net investment in the Americas, Asia, and Europe.

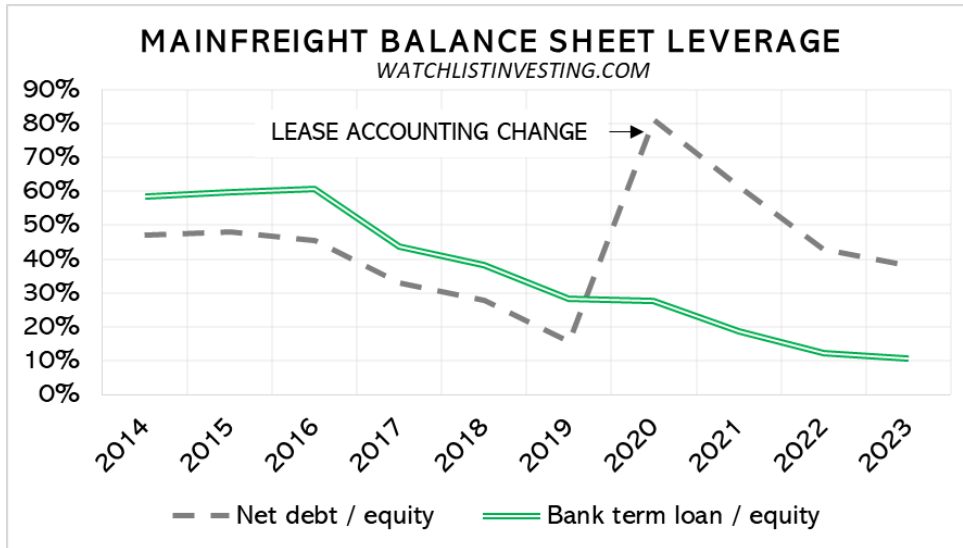
To put an even finer point on America, Mainfreight has its eyes set on competing in the less-than-truckload (LTL) space in the United States, becoming a registered motor carrier in the country. The company is not naïve when it comes to the difficulties it faces. From the 2023 annual report:

It [the company's experience over the past two years] has also exposed our weaknesses and lack of maturity in this market, and a shortage of customers across market verticals that provide regular, daily freight volumes, no matter the economic cycle... However, the growth we did experience has allowed us to find some measure of scale in what will become our biggest market...

The report goes on to say that the company is planning to acquire land and build new facilities, including cold storage and perishable facilities. One would expect capex to reflect this buildout over time.



Since 2014, Mainfreight has grown while improving its financial health. Leverage is shown two ways since the 2020 accounting change capitalizing leases skews the numbers upward in that year. However, the trend over the subsequent three years is apparent.



Interim Results (6 Months September 2023):

Mainfreight’s results for the first half of fiscal year 2024 reflect the weakness seen across the industry. Reduced freight volumes and pricing industrywide hit Mainfreight to the tune of a 22% decline in revenue and a 43% decline in profits.

New Zealand and Australian markets were relative bright

spots with revenue down 14% and 9%, respectively. Profits in those regions declined 18% and 10.6%, respectively. The America’s segment fared worst with revenue down 42% and pre-tax profit down 80%. Go back and look at the shipping container cost at the beginning of the industry section to see the steep decline from 2022 to 2023.

Operating margin came in just under 8% for the 2023 period compared to 10.4% for the same period in 2022. This suggests that the business is probably back to normal and not falling off a cliff, even though it might seem like that in isolation.

In response to the slowdown, management cut its capex guidance by \$113 million to \$563 million for FY 24 and 25 combined. Expectations are for the second half to improve marginally.

Income Statement
For the Six Months ended 30 September 2023

Notes	Six Months Ended 30 Sept 2023 unaudited	Six Months Ended 30 Sept 2022 unaudited
	\$NZ000	\$NZ000
Total Revenue	2,355,042	3,003,333
Transport Costs	(1,304,577)	(1,895,050)
Labour Expenses	(538,549)	(520,152)
Other Expenses	(191,595)	(165,632)
Earnings before Finance Costs, Tax, Depreciation and Amortisation	320,321	422,499
Depreciation of Right to Use Assets	(85,204)	(70,562)
Finance Costs Relating to Lease Liabilities	(9,719)	(8,010)
Other Depreciation & Amortisation Expenses	(47,637)	(38,968)
Other Finance Costs	(2,924)	(3,247)
Profit before Taxation	174,837	301,712
Income Tax Expense	(50,287)	(84,694)
Net Profit for the Period	124,550	217,018



CAPITAL ALLOCATION:

Accounting made analyzing Mainfreight's capital allocation a bit tricky⁴, but in the end came down to a few big buckets:

1. Dividends at 36% of net income
2. Growth capex at 13%
3. Debt and lease payments of 34%
4. Increase in cash of 17%

Mainfreight Core Capital Allocation 2014-23		
Net income	1,720	100%
Dividends	(624)	-36%
Growth capex	(231)	-13%
Change in cash	(294)	-17%
Net repayment of loans	(128)	-7%
Lease principal payments	(474)	-28%
Total	(32)	-2%

Working capital is not a constraint on growth, as evidenced by the mere \$15 million increase in core working capital since 2013, all while revenue has tripled.

The company spent most of its net investment in capex on physical property. The growth in warehouse space from 2014 to 2023 tells that story.

Warehouse footprint detail	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	99,800	106,800	130,582	140,000	145,000	150,500	161,300	171,915	179,075	250,232
Australia	87,950	104,383	102,231	108,322	113,071	146,700	165,096	177,000	215,909	256,266
Americas	Data unclear	30,000	49,146	49,146	59,500	59,500	85,935	121,100	195,698	195,698
Europe	223,229	223,859	242,836	281,256	296,466	322,525	317,353	334,273	338,820	338,820
Total	410,979	465,042	524,795	578,724	614,037	679,225	729,684	804,288	929,502	1,041,016

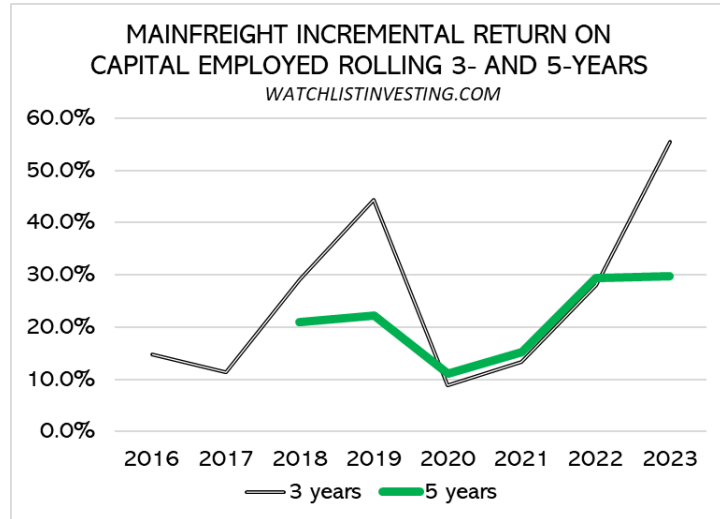
Mainfreight Capital Allocation 2014-2023			
Sources		% Total	% NI
Net income	1,720	68%	100%
Change in lease liabilities	772	31%	45%
Forex differences	18	1%	1%
Issuance of shares	16	1%	1%
Total sources	2,526	100%	147%
Uses			
Change in lease ROU assets	(745)	34%	-43%
Dividends	(624)	28%	-36%
Lease principal payments	(474)	21%	-28%
Growth capex	(231)	10%	-13%
Net repayment of loans	(128)	6%	-7%
Change in core working capital	(15)	1%	-1%
Acquisitions	(3)	0%	0%
Total uses	(2,220)	100%	-129%
Change in cash	294		
Unaccounted	12		

⁴ This was in part due to being less familiar with IFRS accounting standards, including the fact that Mainfreight revalues its property from time to time (in accordance with IFRS), and the lease accounting.



A rolling average of incremental returns on capital employed (pre-tax) demonstrates that Mainfreight has invested shareholder capital well. Rolling returns troughed in 2020 on both a 3- and 5-year basis at 10% and have been rebounding since that time.

Another standout is the lack of activity in the share count. Since 2013, it's increased from 99.2 million shares to just 100.7 million shares, a CAGR of 0.15%.



VALUATION:

One thing I've somehow managed to do is avoid looking at the price / market cap of this company, something not always easy to do during the research process.

Mainfreight almost undoubtedly has been over-earning the last two years. Starting with FY 2023 revenues of \$5.7 billion and adjusting them by 25% (slightly more than the interim decline in revenues of 22%) results in revenues of \$4.3 billion. It seems the current margin of 8% would account for reversion to the mean from the 10%+ highs while allowing for a slight improvement from the 2013 to 2020 average of 6.6%. Applying an 8% pre-tax margin to \$4.3 billion gives us operating income of \$344 million; less 25% tax and we're at \$258 million, rounded down (conservatively) to a nice \$250 million of after-tax earnings.

Mainfreight grew revenues by 6.7% on average between 2014 and 2021. If we assume 7% growth that results in revenues growing by \$300 million next year. With each dollar of revenue requiring \$0.36 of capital, the company must retain \$108 million to grow, reducing the distributable cash flow to \$142 million. Using a 10% discount rate less 7% growth that produces a multiple of 33x this distributable cash flow, or about \$4.7 billion. *As a reminder, these are New Zealand Dollars.*

Now to check the price... Shares trade on the New Zealand exchange at around NZ\$71. With 100.7 million shares that gives it a market value of \$7.1 billion. Add on net debt of \$700 million and the total enterprise value is \$7.8 billion, or 65% greater than the calculated value above.

Knowing the enterprise value, we can take the \$250 million after-tax earnings and divide it in, resulting in a current earnings yield of about 3.2%. Such a low earnings yield implies lots of high growth going forward. Mainfreight seems to have a bright future, but I'm not sure it's *that* bright.



RISKS:

Valuation aside, I see a few risks in Mainfreight:

1. **Key man risk:** Founder, Bruce Plested, has had a huge impact on the company. Eventually he will no longer be running the show. However, his #2, Don Braid, has been with the company for three decades and would likely continue running the company as he has in the past, building on the 100-year vision of Plested. The company also has a 10% profit sharing program to incentivize employees to take care of the bottom line.
2. **Capital investment:** Building an asset-heavy company risks building warehouses and other infrastructure in the wrong locations. Mainfreight seems to have a good track record of building infrastructure but it's possible that shifts in trade lanes could render owned infrastructure less valuable.
3. **US LTL:** The company has an aim to enter the less-than-truckload space in the United States. Such an entry will require a large investment in physical infrastructure and risks ill investment or botched execution. The LTL market is a great business for large, established incumbents, and it's unclear exactly how Mainfreight intends to break in and compete. Presumably they will start local/regional and expand trade lanes as they gain experience, however, the company hasn't to my knowledge fully explained their strategy.
4. **Reliance on New Zealand and Australia:** These two countries make up a large portion of revenues and have been receiving the bulk of capital expenditure dollars. As the fortunes of the countries go so will Mainfreight. Both countries appear to be growing modestly with inflation coming down. New Zealand in particular is suffering from very high housing costs, which could impact growth and demand.

SUMMARY / CONCLUSION:

Mainfreight falls into the category of businesses with highly satisfactory returns on capital and the ability to deploy that capital at attractive rates of return. The company is run by its founder and a long-time managing director (CEO), who favors organic growth, a steady dividend, and not touching the share count. The company is following the industry in returning to a more normalized level of operations but appears to be well situated long term. I'd like to see shares cut in half to be interested in buying. Aside from valuation Mainfreight has all the attributes I like to see in a business which is why I'm adding it to the Watchlist. It will also complement Old Dominion and Saia in the logistics segment.

Stay rational! —Adam

Note: Mainfreight trades on the New Zealand Exchange under the symbol MFT. There is an active unsponsored ADR by BNY Mellon (MFGHF) and there appears to be an inactive unsponsored ADR by Citi (MFGHY), both with a ratio of 2 ADRs per underlying.⁵

⁵ As of this writing shares traded on the New Zealand Exchange at NZ\$71. ADRs (MFGHF) traded at US\$44. The USD/NZD exchange rate is about \$0.61 USD to NZD. The implied USD price is \$43.31, meaning there's a slight advantage to buying direct.



SUMMARY FINANCIALS:

Mainfreight, Ltd.										
Balance Sheet										
(NZ \$mil; FYE March 31)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Cash	\$56	\$65	\$94	\$75	\$81	\$115	\$116	\$140	\$202	\$342
Trade debtors	231	261	293	315	362	389	421	489	806	619
Other receivables	39	48	44	48	61	55	73	90	49	66
Other current assets	(1) 4	7	3	2	8	0	3	0	0	30
Total current assets	329	382	434	440	511	560	613	719	1,057	1,058
Property	350	437	482	484	483	548	653	756	925	1,069
Plant and equipment	54	61	87	86	99	119	124	163	185	277
Right of use assets							615	568	586	745
Net fixed assets	404	497	569	571	582	667	1,392	1,486	1,696	2,091
Software	19	23	34	43	49	51	54	54	52	55
Goodwill	187	191	208	201	208	209	227	209	204	219
Other intangible assets	30	25	25	21	17	10	5	2	1	1
Deferred tax asset	7	7	9	9	9	6	15	18	17	20
Other assets	243	246	275	274	283	276	300	282	275	294
Total assets	\$976	\$1,124	\$1,279	\$1,285	\$1,377	\$1,503	\$2,305	\$2,487	\$3,028	\$3,443
Trade creditors & accruals	197	230	263	261	299	315	340	413	562	493
Employee entitlements	38	38	44	48	53	63	70	92	152	147
Income tax liability	9	13	5	14	12	19	19	30	57	61
Lease liability	(3) 2	2	2	3	2	2	124	118	121	156
Asset finance loans							3	9	9	9
Total current liabilities	246	283	314	326	367	399	555	663	901	866
Bank term loan	258	304	353	283	271	239	268	210	176	187
Employee entitlements	1	1	1	4	4	3	3	3	3	4
Lease liability	(3) 4	3	3	2	5	5	503	467	490	625
Deferred tax liability	25	24	26	24	22	19	7	7	11	11
Asset finance loans							3	23	18	23
Total long-term liabilities	288	333	384	313	300	266	783	709	698	850
Total liabilities	534	616	698	639	667	665	1,338	1,372	1,599	1,716
Shareholders' equity	442	509	581	646	710	838	966	1,115	1,429	1,727
Total liabilities & equity	\$976	\$1,124	\$1,279	\$1,285	\$1,377	\$1,503	\$2,305	\$2,487	\$3,028	\$3,443
Diluted shares outstanding (000s)	99,303	99,788	99,946	100,547	100,699	100,699	100,699	100,699	100,699	100,699
Total debt + lease liability	\$265	\$310	\$359	\$288	\$277	\$246	\$900	\$827	\$815	\$1,000
Net debt	\$209	\$245	\$265	\$213	\$197	\$130	\$784	\$688	\$612	\$658
Core working capital	(2) \$30	\$36	\$29	\$41	\$66	\$48	\$69	\$44	\$83	\$15
Net debt / equity	47%	48%	46%	33%	28%	16%	81%	62%	43%	38%
Bank term loan / equity	58%	60%	61%	44%	38%	28%	28%	19%	12%	11%

Notes:

1. 2023: Includes \$22.4 income tax receivable and \$7.7 properties held for sale. Other years included property held for sale of: 2018: \$7.8; 2016: \$1.8; 2015: \$6.2; 2014: \$2.1.
2. Core working capital = total current assets less cash less non-debt current liabilities.
3. Lease liability in 2019 and prior consists of finance leases.



Mainfreight, Ltd.										
Income Statement										
(NZ \$mil; FYE March 31)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Revenue										
New Zealand	\$507	\$543	\$565	\$610	\$666	\$718	\$753	\$848	\$1,145	\$1,307
Australia	533	546	564	585	693	779	817	965	1,290	1,616
Americas	465	537	694	629	650	780	810	910	1,642	1,669
Asia	75	97	157	163	181	187	168	316	730	418
Europe	416	416	445	472	580	678	727	789	1,013	1,138
Intersegment	(71)	(85)	(140)	(126)	(154)	(188)	(181)	(284)	(601)	(472)
Total revenue	\$1,924	\$2,054	\$2,285	\$2,334	\$2,617	\$2,954	\$3,095	\$3,544	\$5,218	\$5,676
Transport costs										
Labor expenses	386	405	460	476	538	613	670	723	887	1,023
Other expenses	173	198	223	228	261	194	223	212	264	357
Lease costs						101				
Depreciation of right of use assets							112	114	127	155
Other depreciation and amortization	32	39	39	43	48	53	58	68	73	84
Total operating expenses	1,795	1,932	2,149	2,181	2,453	2,753	2,866	3,259	4,708	5,064
Operating profit	129	122	136	153	164	201	230	284	510	612
OPM	6.7%	5.9%	5.9%	6.6%	6.2%	6.8%	7.4%	8.0%	9.8%	10.8%
Finance costs - lease liabilities										
Other finance costs	8	7	9	8	8	8	6	6	5	7
Pre-tax profit	122	115	127	145	156	194	206	262	489	587
Income taxes										
Net profit	\$90	\$77	\$88	\$102	\$108	\$138	\$148	\$188	\$355	\$426

Mainfreight, Ltd.										
Capital Allocation										
(NZ \$mil; FYE March 31)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Net profit	\$90	\$77	\$88	\$102	\$108	\$138	\$148	\$188	\$355	\$426
Purchase of PP&E less proceeds	(54)	(121)	(80)	(42)	(47)	(74)	(138)	(101)	(172)	(294)
Purchase of software less proceeds	(8)	(10)	(14)	(20)	(18)	(16)	(17)	(18)	(17)	(20)
Total depreciation + amortization	32	39	39	43	48	53	170	182	201	239
Growth capex (neg. = net investment)	(29)	(92)	(54)	(18)	(17)	(36)	15	64	12	(75)
Share issuance	0	4	0	12	0	0	0	0		
Acquisitions	(1)	(2)	(0)	0	(0)	0	0	0	0	0
Dividends	(28)	(33)	(34)	(40)	(43)	(48)	(59)	(64)	(101)	(173)
Change in debt & leases		45	49	(71)	(11)	(32)	655	(73)	(13)	186
Change in core working capital		6	(7)	13	25	(18)	20	(25)	40	(69)

Capital allocation notes:

Lease
accounting
begin in
2020.

Misc. Cash Flow Detail:

Forex differences CF stmt	(3)	1	6	(2)	0	1	7	(7)	(2)	16
Proceeds from term loans	0	57	19	0	2	0	41	62	75	198
Repayment of loans	(17)	(1)	(0)	(57)	(28)	(27)	(32)	(118)	(105)	(197)
Principal lease payments							(101)	(107)	(119)	(147)
Adjustment to opening balance										
Transfer between asset classifications	0	(4)	(2)	0	(8)	0	0	7	0	(8)
Revaluation of land	7	11	0	(0)	0	44	0	56	84	0
Forex impact (property section)	(5)	(9)	21	(9)	6	(5)	11	(3)	(9)	14



Gross capex detail (millions)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Property	56	100	55	25	20	31	112	59	109	163
Racking, solar, energy management								16	35	71
Information technology	12	15	16	20	18	16	17	18	17	20
Other plant and equipment	11	16	22	17	27	43	27	26	27	60
Total	79	131	93	61	65	89	155	119	189	314

Capex by region (millions)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	34	93	29	39	33	49	62	74	80	102
Australia	33	28	56	6	8	21	71	19	64	138
Americas	4	5	10	7	6	9	9	10	19	42
Asia	1	1	1	1	0	1	1	1	2	2
Europe	7	6	10	15	21	23	16	19	28	40
Total	79	132	106	67	69	103	160	122	193	324

Deprec. & Amort by region (millions)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	12	13	16	19	21	23	47	48	55	63
Australia	3	5	6	7	7	8	45	47	50	58
Americas	4	4	5	5	6	7	24	28	34	51
Asia	0	0	1	1	1	1	3	3	3	5
Europe	12	11	11	12	13	15	50	56	57	61
Total	32	34	39	43	48	53	170	182	201	239

Net capex by region (millions)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	22	80	13	20	12	26	15	25	25	39
Australia	30	23	50	(1)	1	13	26	(28)	14	79
Americas	(0)	0	5	2	1	3	(15)	(18)	(15)	(9)
Asia	0	0	0	(0)	(0)	1	(2)	(2)	(2)	(3)
Europe	(5)	(5)	(1)	3	8	8	(34)	(38)	(30)	(21)
Total	47	97	67	24	21	50	(10)	(60)	(8)	85

Note: Net capex equals capital expenditures less depreciation.



Revenue by region %	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	26%	26%	25%	26%	25%	24%	24%	24%	22%	23%
Australia	28%	27%	25%	25%	26%	26%	26%	27%	25%	28%
Americas	24%	26%	30%	27%	25%	26%	26%	26%	31%	29%
Asia	4%	5%	7%	7%	7%	6%	5%	9%	14%	7%
Europe	22%	20%	19%	20%	22%	23%	23%	22%	19%	20%
Intersegment	-4%	-4%	-6%	-5%	-6%	-6%	-6%	-8%	-12%	-8%
Total revenue	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%

Segment revenue	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Domestic transport					1,297	1,451	1,550	1,611	1,915	2,243
Warehousing					289	347	410	452	584	750
Air & Ocean Forwarding					1,031	1,157	1,135	1,481	2,720	2,683
Total					\$2,617	\$2,954	\$3,095	\$3,544	\$5,218	\$5,676

Segment profit before tax %	(1)	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Domestic transport						9.9%	10.8%	7.7%	11.4%	9.6%	10.2%
Warehousing						11.5%	10.8%	8.4%	9.3%	9.5%	8.7%
Air & Ocean Forwarding						5.2%	5.5%	4.6%	5.4%	9.2%	10.9%
Total						8.2%	8.7%	6.7%	7.4%	9.4%	10.3%

1. Profit before tax & abnormals from 2020 onward. From 2019 and prior adjusted EBITDA.

Volume	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Land freight tonnes	(1)			6,148,933	6,866,867	7,349,327	7,700,213	7,660,242	7,286,572	7,321,452
Air freight tonnes		73,367	86,547	113,120	121,553	127,174	126,669	126,071	114,736	138,279
Sea freight TEUs		230,320	251,685	267,144	280,539	311,586	342,143	337,504	347,638	424,610
Warehouse footprint (sq. meters)		410,979	465,042	524,795	578,724	614,037	679,225	729,684	804,288	929,502
Branches		233	242	239	239	247	260	282	297	305
Countries		20	20	21	21	22	24	26	26	25

1. Data on land freight tonnes prior to 2017 did not include Europe and would not be comparable. No company-wide total was available to back into European volume.

Warehouse footprint detail	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
New Zealand	99,800	106,800	130,582	140,000	145,000	150,500	161,300	171,915	179,075	250,232
Australia	87,950	104,383	102,231	108,322	113,071	146,700	165,096	177,000	215,909	256,266
Americas	Data unclear	30,000	49,146	49,146	59,500	59,500	85,935	121,100	195,698	195,698
Europe	223,229	223,859	242,836	281,256	296,466	322,525	317,353	334,273	338,820	338,820
Total	410,979	465,042	524,795	578,724	614,037	679,225	729,684	804,288	929,502	1,041,016

Capital requirements & ROCE	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023
Core working capital	(1)	\$38	\$48	\$34	\$56	\$78	\$67	\$88	\$74	\$140
Net fixed assets, ROU assets, software		423	520	603	614	632	718	1,445	1,540	1,748
Total capital employed		\$461	\$568	\$637	\$669	\$710	\$785	\$1,533	\$1,614	\$1,888
Avg. core working capital	(1)	\$44	\$43	\$41	\$45	\$67	\$73	\$77	\$81	\$107
Avg. net fixed assets, ROU assets, software		404	471	561	608	623	675	1,082	1,492	1,644
Avg. total capital employed		\$448	\$515	\$602	\$653	\$690	\$747	\$1,159	\$1,573	\$1,751

Avg. as % revenues:

Core working capital	(1)	2.3%	2.1%	1.8%	1.9%	2.6%	2.5%	2.5%	2.3%	2.1%
Net fixed assets, ROU assets, software		21.0%	22.9%	24.6%	26.1%	23.8%	22.8%	34.9%	42.1%	31.5%
Total capital employed		23.3%	25.0%	26.4%	28.0%	26.4%	25.3%	37.4%	44.4%	33.6%

Revenue / avg. capital employed		\$4.29	\$3.99	\$3.79	\$3.57	\$3.79	\$3.95	\$2.67	\$2.25	\$2.98
Operating margin		6.7%	5.9%	5.9%	6.6%	6.2%	6.8%	7.4%	8.0%	10.8%
Pre-tax return on capital employed		28.8%	23.7%	22.5%	23.4%	23.7%	26.9%	19.8%	18.1%	29.1%
After-tax assuming 25% tax rate)		21.6%	17.8%	16.9%	17.6%	17.8%	20.2%	14.9%	13.6%	21.9%

1. Core working capital = total current assets minus cash, trade creditors & accruals, and employee entitlements.



Watchlist

As of January 31, 2024

WATCHLIST Count: 28						
Company Name	Industry	Ticker	Current Price	Market Cap	See Issue	
Boston Beer Company	Alcoholic beverages	SAM	\$349	\$4,257,967,899	7, 12	
Constellation Brands	Alcoholic beverages	STZ	\$245	\$44,799,742,046	7, 12	
Anheuser-Busch InBev	Alcoholic beverages	BUDFF	\$62	\$106,940,103,867	7, 12	
Heineken	Alcoholic beverages	HKHHY	\$43	\$48,764,547,436	7, 12	
Hingham Institution for Savings	Banking	HIFS	\$185	\$398,816,780	1	
Plumas Bancorp	Banking	PLBC	\$35	\$205,101,078	4	
Triumph Financial	Banking	TFIN	\$71	\$1,714,359,000	21	
Thomasville Bancshares	Banking	THVB	\$64	\$387,026,944	23	
Jack Henry & Associates	Banking Software	JKHY	\$166	\$12,077,100,539	11	
Vulcan Materials	Basic Materials	VMC	\$226	\$30,030,716,404	24	
Martin Marietta Materials	Basic Materials	MLM	\$508	\$31,423,997,117	24	
Creightons PLC	Beauty Products	CRL.LON			15	
Monarch Cement	Building Products	MCEM	\$152	\$389,805,216	2	
Berkshire Hathaway	Conglomerate	BRK.B	\$384	\$831,251,140,020	14	
Home Depot	Home Improvement	HD	\$353	\$351,287,596,423	18	
Lowes	Home Improvement	LOW	\$213	\$122,407,006,245	18	
Fastenal	Industrial Distributing	FAST	\$68	\$39,026,354,249	9	
Old Dominion Freight Line	Logistics	ODFL	\$391	\$42,665,598,673	8	
Saia, Inc.	Logistics	SAIA	\$451	\$11,961,965,942	8	
Mainfreight	Logistics	MFGHF	\$44	\$7,045,775,000	33	
Sherwin-Williams	Paint/coatings	SHW	\$304	\$77,910,932,329	19	
Otter Tail Corp	Utility	OTTR	\$90	\$3,771,465,142	28	
MDU Resources	Utility	MDU	\$20	\$3,972,983,279	28	
NextEra Energy	Utility	NEE	\$59	\$120,291,583,601	28	
Copart	Vehicle remarketing	CPRT	\$48	\$46,129,517,335	20	
Waste Management	Waste Management	WM	\$186	\$74,767,199,468	6	
Republic Services	Waste Management	RSG	\$171	\$53,840,596,343	6	
Waste Connections	Waste Management	WCN	\$155	\$39,953,085,438	6	

Click [here](#) to see the latest Watchlist and Suspect List on Google Sheets.



About

After nearly two decades as an individual investor, a decade in commercial credit at various banks, and a few years managing money for friends/family in the background, I decided to go full-time managing money for clients in 2020. Watchlist Investing is an extension—albeit separate and distinct—of what I do day-to-day as a practicing capital allocator. Inverting the margin of safety principle, I hope to add value to readers above and beyond the nominal cost of the newsletter.

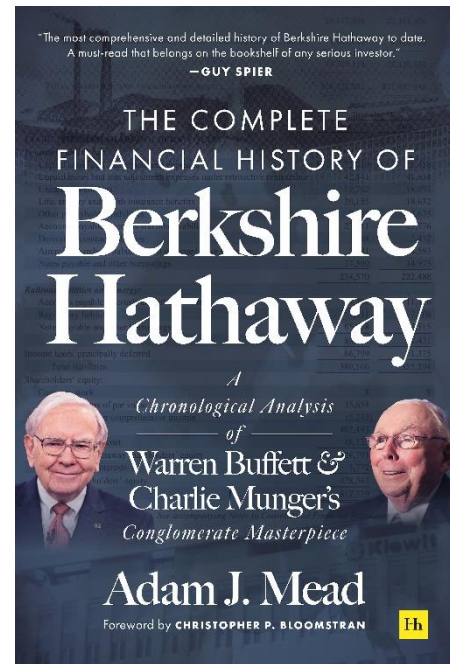
My investing style is influenced by my background growing up in a family of business owners. I followed suit selling firewood through high school and founding a welding business in college. Looking at stocks as businesses is natural to me. My investing approach rests on fundamental value investing tenets, but it's adapted to suit my style. I'm 100% certain I'm not the best investor or analyst, but I hope to improve over time.

Between 2016 and 2021, I wrote a book on Berkshire Hathaway. *The Complete Financial History of Berkshire Hathaway* was and is my passion project. I hope it brings new shareholders up to speed on the company and provides a fresh look to long-time shareholders, in addition to serving as a resource/reference book. It can be purchased [here](#). I also created www.theoraclesclassroom.com as an extension of the book, which includes an archive of a lot of BRK material.

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