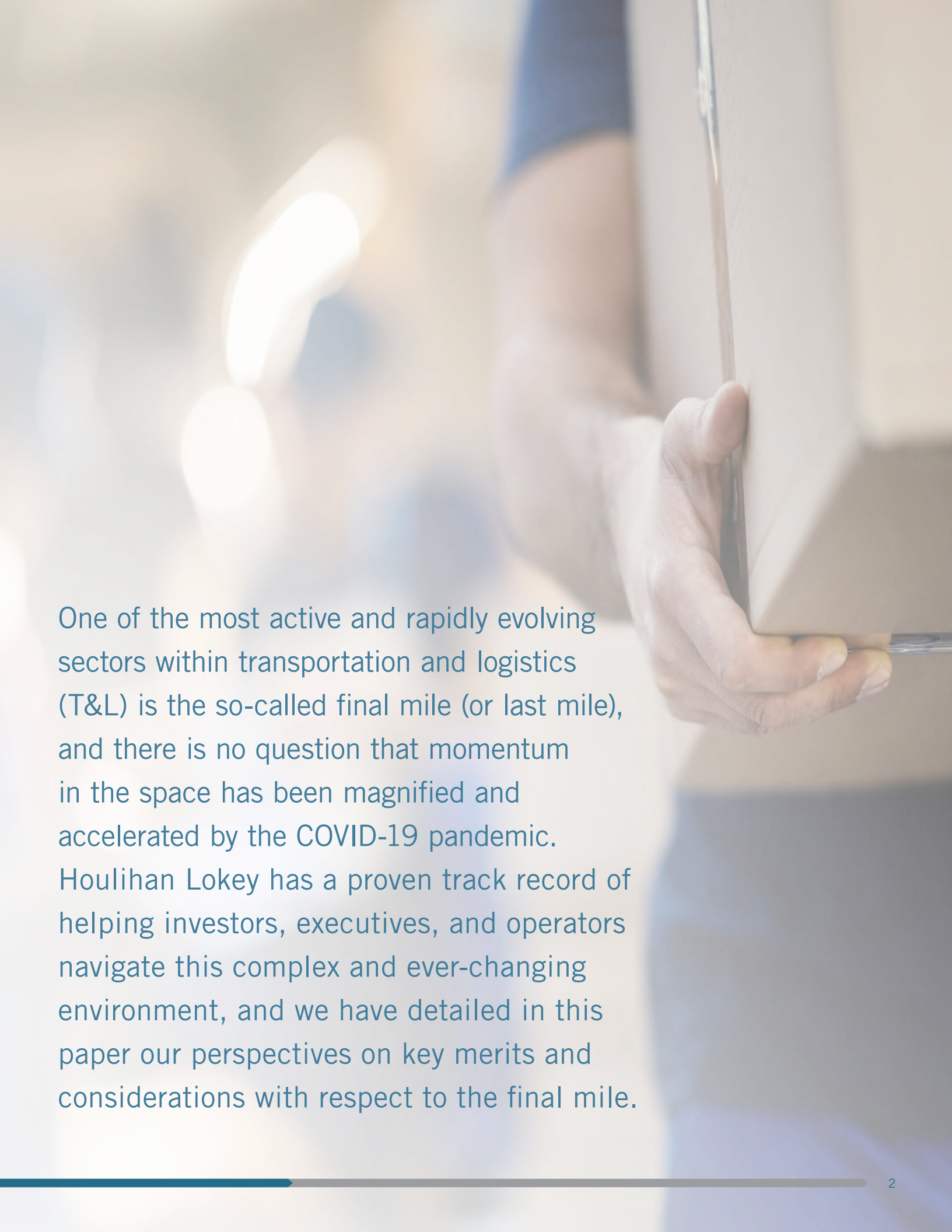




HOULIHAN LOKEY

WHAT'S DRIVING FINAL MILE?

Emerging Opportunities
in the Logistics Space



One of the most active and rapidly evolving sectors within transportation and logistics (T&L) is the so-called final mile (or last mile), and there is no question that momentum in the space has been magnified and accelerated by the COVID-19 pandemic. Houlihan Lokey has a proven track record of helping investors, executives, and operators navigate this complex and ever-changing environment, and we have detailed in this paper our perspectives on key merits and considerations with respect to the final mile.

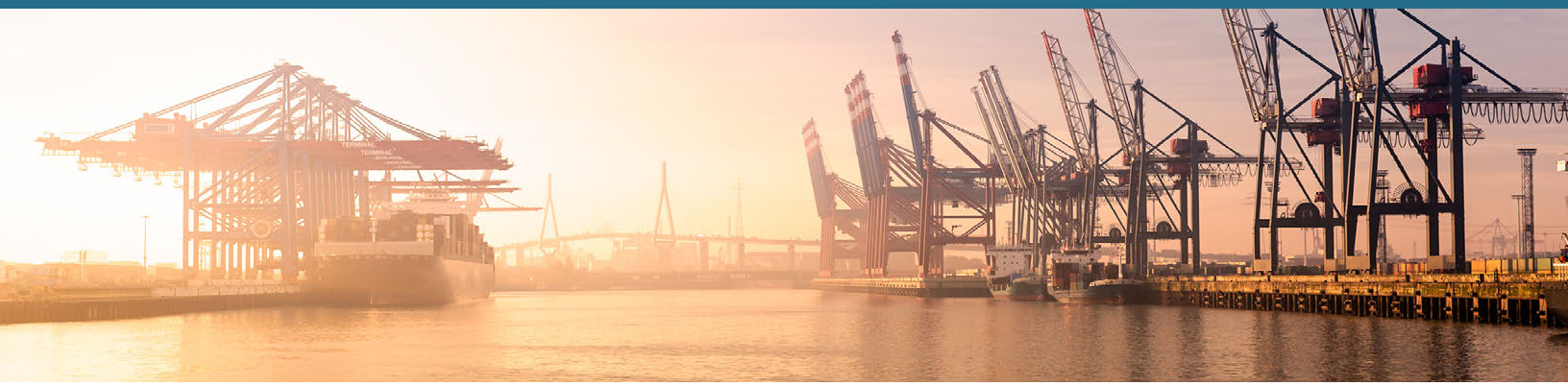


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Final mile represents the last step in transporting products to end users—to both consumers (B2C) and businesses (B2B)—and is often the most complex and expensive part of the fulfillment chain. Final mile service providers must navigate more uncertainties than ever before, but they are also positioned to experience higher levels of growth, profitability, and consumer loyalty if they can respond effectively to the recent e-commerce boom. Because of the pandemic-driven rise in e-commerce, many companies have accelerated their final mile offerings and/or taken a strategic approach to technology, customer service, partnerships, and M&A to differentiate themselves in this fragmented space.



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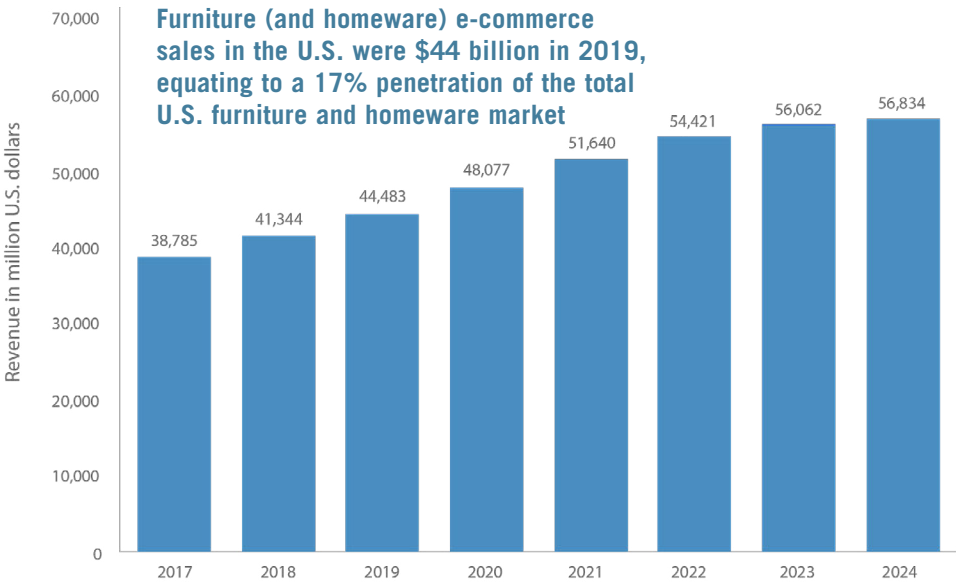
E-commerce, coupled with rising consumer expectations, has introduced new levels of complexity for retailers, manufacturers, and transportation providers to navigate.

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Prior to the rise of e-commerce, a traditional distribution model existed: goods from the manufacturer were shipped to a distribution center, then to the retail outlet, and then the local retail outlet would deliver goods to the households and businesses that purchased them. For the most part, retailers themselves handled the final mile service, especially when it came to large or bulky items.

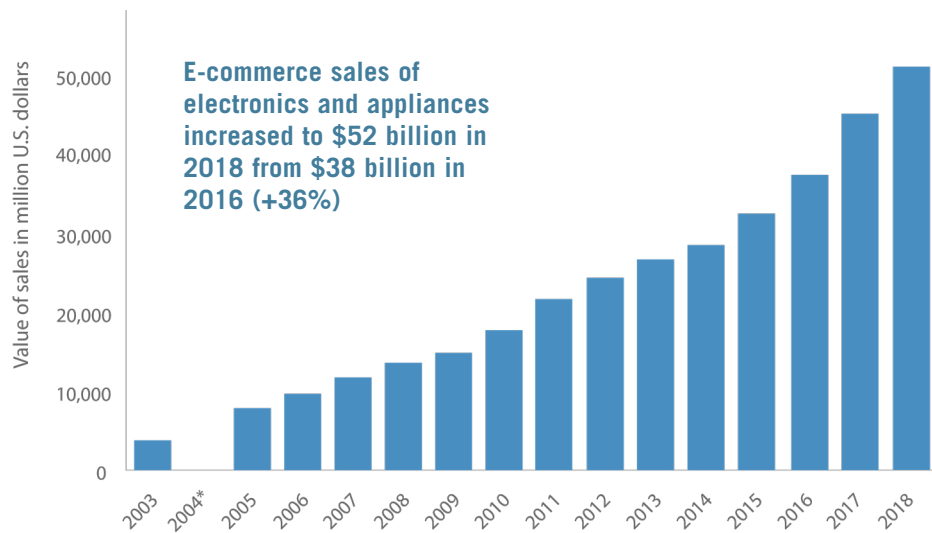
E-commerce has completely disrupted the traditional distribution model, as products purchased online may be shipped directly from the manufacturer or shipped from a retailer’s distribution center or warehouse. Final mile responsibilities have shifted from the retailer’s local staff to a wide variety of third-party providers. Many of these providers, especially those delivering light goods, simply ring the doorbell and drop off the product at the consumer’s doorstep or a business’s lobby/reception area. This “ring-and-run” service does not meet consumer expectations when it comes to larger, bulkier, and more expensive items. Providers delivering these items increasingly provide “white-glove” service, in which delivery staff bring the product into the consumers’ homes or businesses, install it for them, and even provide tips or advice regarding the product. E-commerce, coupled with rising consumer expectations, has introduced new levels of complexity for retailers, manufacturers, and transportation providers to navigate.

U.S. furniture and home furnishings e-commerce revenue (2017–2024)



Source: Statista.

U.S. e-commerce sales of electronics and appliances (2003–2018)



Source: Statista.

* The estimate for 2004 did not meet Statista's publication standards because of high sampling variety or poor response quality.

Final mile remains the fastest-growing segment in T&L, with a market size estimated between \$35 billion and \$40 billion and growing.

Despite its inherent complexity, final mile remains the fastest-growing segment in T&L, with a market size estimated between \$35 billion and \$40 billion and growing.⁽¹⁾ Despite its large size, the space is heavily fragmented, and while this “fragmented landscape creates a black hole of customer experience,” it can also create opportunities for providers with certain capabilities.⁽²⁾ Because of this fragmentation, no significant brand identity exists with regard to final mile providers, especially for large and bulky items. Herein creates an opportunity for companies willing to invest in and build brand identity; although fragmented, the final mile space remains so large that it will not be a winner-take-all landscape. Instead, there will be room for specialization and subspecialization for companies that can provide a superior customer experience to grow their businesses and differentiate themselves from other providers. The key drivers behind this differentiation run the gamut from technical expertise and digitization to staffing and product/installation expertise.

The Drive Toward Digitization

Despite usually being the shortest leg from vendor to end user, the final mile is typically the most expensive and complex part of the fulfillment chain. These costs and complexities have become especially alarming, given the 37.1% growth in e-commerce from Q3 2019 to Q3 2020.⁽³⁾ Providers have long believed that technology would play a critical role in final mile's future, but largely refrained from making the investments required to boost their technological capabilities. The pandemic-driven growth in e-commerce has accelerated this investment, as companies have either accelerated their existing digitization plans or relied on M&A to enhance their digital capabilities (e.g., Walmart's acquisition of JoyRun in November 2020).

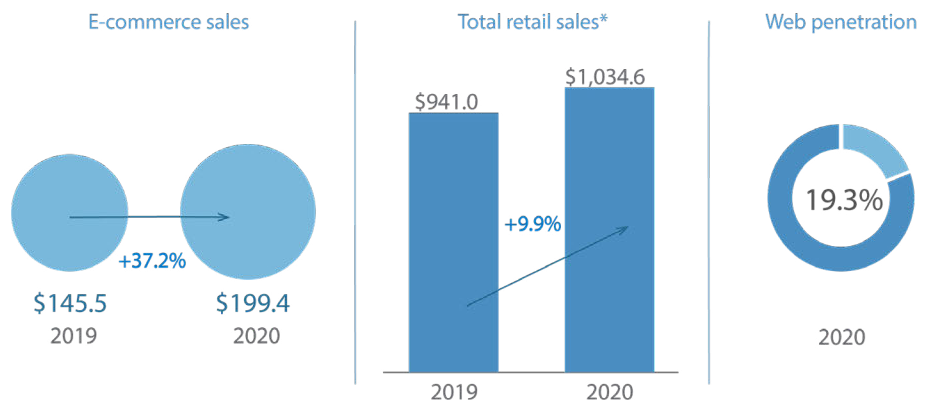
(1) Freightwaves: Freight Intel Research, “Final Mile Report,” June 2020.

(2) Interview with JP Hampstead, FreightWaves, September 28, 2020.

(3) U.S. Census Bureau, “Quarterly Retail E-Commerce Sales: 3rd Quarter 2020,” December 15, 2020: https://www.census.gov/retail/mrts/www/data/pdf/ec_current.pdf.



U.S. retail landscape during Q3 2020 (\$ in billions)



Source: Digital Commerce 360 analysis of U.S. Department of Commerce data.

* Total retail figures exclude sales of items not normally purchased online such as spending at restaurants, bars, automobile dealers, gas stations, and fuel dealers.

Many providers now have customer service portals to rapidly respond to and resolve disputes.

Many final mile providers focus chiefly on customer experience by providing real-time tracking and visibility. Consumers have long grown accustomed to being able to track the progress of their parcels and light goods shipped via USPS or other providers, and increasingly expect to do so for larger, higher-value items. Providers are increasingly expected to be able to send routine-update notifications to shippers and recipients alike. These updates not only provide greater levels of transparency, but they also reduce the likelihood of costly failed deliveries and rescheduling. For example, Ryder's 2018 acquisition of MXD enhanced its real-time tracking capabilities and increased the robustness of its "white-glove" service options to consumers and businesses.

Digitization has also driven innovation in customer service and KPIs. Many providers now have customer service portals to rapidly respond to and resolve disputes. Since 10%–20% of large items ordered online

are damaged during the delivery process, providing an easy-to-use online portal meets consumer expectations and creates deeper levels of satisfaction and loyalty. These digital solutions have enabled many final mile providers to meet or exceed the level of service that consumers have grown to expect. Given how fragmented the final mile space currently remains, this ability to create consumer awareness and brand identity through exceptional customer service has become a strategy and competitive differentiator.

Because of the complexities and costs associated with final mile, digitization is likely the only way to balance this heightened level of customer experience with route-level profitability. The many players who have tried and failed to consolidate final mile often stumbled because of the challenges of balancing route-level profitability with scale as their businesses grew. As final mile remains a thin-margin business where providers must focus on controlling costs at every step, digitization could allow providers the visibility and cost savings necessary to thrive.

Another group of companies fueling this drive toward digitization are those that optimize routing, freight matching, and other operational efficiencies. While these innovations indirectly increase consumer satisfaction by allowing for more timely deliveries, their real impact comes in the increased operational efficiency they afford and their potential to expand current services, such as same-day delivery. Providers operating in urban



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areas routinely suffer from traffic and myriad other scheduling delays stemming from a lack of suitable areas to unload or park due to local rules and regulations. Rural operators may be more adversely affected by road conditions or other logistical concerns. Matching the right piece of freight with the right vehicle and driver, creating the most efficient route, predicting the peaks and valleys of traffic flow, and remaining cognizant of an always-changing regulatory environment have increasingly become more seamless, thanks to digitization. Digital solutions in these areas reduce the likelihood of cost overruns by lowering the rate of (i) returns, (ii) failed deliveries, and (iii) need for rescheduling.

Finally, digitization enables cost savings in the B2B final mile space, which is an even more important driver for these clients. Providers in this space often deliver mission-critical supplies on established (often same-day) schedules, allowing for more streamlined production schedules and reduced administrative and operational costs. In addition



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to dedicated, single-customer routes, B2B final mile providers heavily rely on conjunctive (or shared-use) networks to realize these cost savings for customers. Conjunctive networks combine groups of customers together into optimal routes and delivery schedules. While digitization has the potential to improve all types of routing and scheduling, its impact on conjunctive routing and scheduling will likely be the greatest differentiator for B2B final mile providers.

Importance of Customer Service

Providing excellent final mile customer service requires more than the technological routing capabilities to get the driver to the consumer with the right product during the right delivery window. It requires a driver—and for some products, a crew—with specific attributes. Delivery personnel must have the training to offload products from a box truck or sprinter van; bring them into the recipient's home or place of business without damaging either the product or the home or office itself; install the product and provide information to the recipient; and potentially remove old products from the residence or office. This heightened level of customer service requires a different type of driver training and level of professionalism. Combining a high level of technological expertise and customer service capabilities may well become what is needed to protect and grow market share.

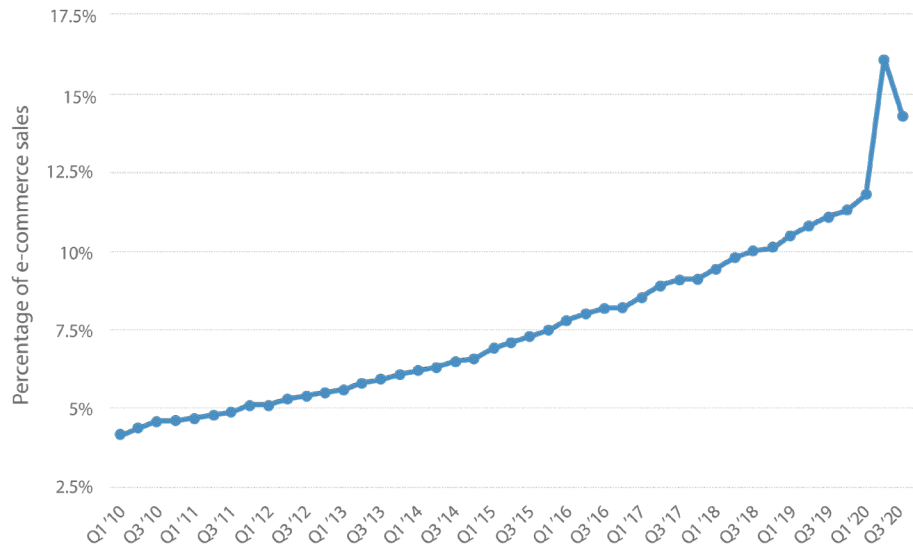
The fragmented yet opportunity-rich final mile landscape has attracted many new entrants providing same-day deliveries and prompted numerous companies to partner with one another to increase their omnichannel potential. Unlike on-demand services like Grubhub, Instacart, or Uber Eats, “white-label” delivery services create the impression that the brand itself handles an order's journey. Thanks to the rapid growth in e-commerce, these services have seen their profiles rapidly increase. For

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According to MWPVL International and ShipMatrix, Amazon currently ships 67% of its packages directly to consumers, an increase of 17% from 2019, and is expected to reach 85%–90% in only a few years.

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Quarterly share of e-commerce sales of total U.S. retail sales from Q1 2010 to Q3 2020



Source: Statista.

example, an on-demand “white-label” service such as Ohi often provides storage and pick-and-pack services for its partners while also providing faster delivery to homes and businesses—often within two hours.⁽⁴⁾ Even PICKUP, a growing player whose platform already provides coverage to 80% of U.S. households, has partnered with Postmates to meet the demands of the e-commerce boom as well as the peak holiday season. Already, projections indicate that the holidays will be “a peak season the industry has never before experienced.”⁽⁵⁾ Final mile providers increasing their expertise and capabilities could not only weather the uncertainty caused by the pandemic, but also find themselves thriving within it.

Recognition of the Investment Opportunity

Final mile has never been an easy sector to operate in for traditional logistics or trucking companies, since it requires a different fleet and level of customer service than what these companies traditionally have at their disposal. Many incumbents have elected to use M&A to complement their existing final mile services and/or increase their existing service network size and/or route density. For example:

- AIT’s recent purchase of U.K.-based Panther Logistics (November 2020) demonstrates many firms’ desire to grow their global final mile footprints.
- CRST’s purchase of NAL Group (March 2020) allowed it to expand into the at-home/on-site delivery, installation, and assembly market and provide its customers with a new “white-glove” niche service option.

(4) Gabriela Barkho, “Amid the e-commerce boom, white-labeled delivery is having a moment,” *Modern Retailer*, October 27, 2020.

(5) Teresa Rivas and Al Root, “Holiday Shipping Will Be Wild This Year. That’s Good News for FedEx and UPS Stock,” *Barron’s*, October 6, 2020.



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As consumers become more accustomed to ordering large and bulky items online and come to view “white-glove” service as the norm, final mile providers in these areas could remain attractive acquisition targets long after the pandemic ends.

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- JB Hunt’s purchases of Mass Movement (November 2020), RDI Last Mile (January 2020), and Cory 1st Choice Home Delivery (February 2019) allowed it to expand its final mile delivery of large and bulky products.
- Forward Air’s purchase of Linn Star Transfer (December 2019) increased its reach into the Midwest and Southwestern U.S. and bolstered its in-home installation services.
- Royal Mail’s acquisition of Dicom Canada (September 2018) allowed it to expand its presence in Eastern Canada and its B2B final mile services.

Another group of companies fueling this acquisition frenzy includes retailers who recognize the value of final mile to their overall customer value proposition. For example:

- Walmart’s acquisition of JoyRun (November 2020) allows the mega-retailer to incorporate JoyRun’s peer-to-peer food and drink delivery service into its own last-mile logistics, in support of delivering products to customers as quickly and efficiently as possible.
- Target’s acquisition of Deliv (May 2020) demonstrated the retailer’s strategy of using proprietary technology to make faster and cheaper deliveries to customers.
- Costco’s acquisition of Innovel Solutions (March 2020)—formerly a subsidiary of Sears and Kmart—brought in-house the ability to provide warehousing, transportation, installation, and home delivery to Costco members as well as retailers, manufacturers, and commercial clients.

Finally, private equity firms are taking advantage of platform investment opportunities in the space, as exemplified by Greenbriar Equity’s acquisition of LaserShip and NewSpring Capital’s acquisition of USPack. Furthermore, USPack recently acquired Gumro & Associates and Freight Rite to expand its national footprint, “white-glove” service offerings, and overall omnichannel retail logistics capabilities. As consumers become more accustomed to ordering large and bulky items online and come to view “white-glove” service as the norm, final mile providers in these areas could remain attractive acquisition targets long after the pandemic ends.

What Could the Final Mile Space Be After COVID-19?

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Consumers who have experienced the added value of “white-glove” service will continue expecting that heightened level of service from all providers.

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It remains to be seen if e-commerce will continue its unprecedented level of growth since the onset of the pandemic, but one thing is certain: consumers have expanded what they feel comfortable ordering online. While that level of comfort may have been born out of necessity or health concerns, consumers will likely not be willing to sacrifice the convenience of ordering large and bulky items online going forward. Likewise, consumers who have experienced the added value of “white-glove” service will continue expecting that heightened level of service from all providers. Automation via delivery robots and drones, while a potential game changer for reducing costs, remains years out for anything approaching widespread adoption and will likely not apply to items requiring “white-glove” service, due to their size/weight and a variety of regulatory challenges.

Regarding the proverbial elephant in the room, Amazon recently accelerated and increased its build-out of delivery stations (note: delivery stations are below fulfillment centers and sortation centers in the fulfillment chain and provide final mile service via Amazon-branded sprinter vans).

According to MWPVL International and ShipMatrix, Amazon currently ships 67% of its packages directly to consumers, an increase of 17% from 2019⁽⁶⁾, and is expected to reach 85%–90% in only a few years. While this trend might not threaten large and bulky items as much as light goods, Amazon has never made a secret of its desire to own the customer experience from start to end, no matter the product ordered from its platform.

As more retailers worry that Amazon is less of a partner and more of a competitor due to its in-house, private-label offerings, final mile providers could find opportunities by targeting retailers that do not sell through Amazon. Building strong connections with retailers concerned about how/ if to partner with Amazon now may create stronger relationships and synergies in the years to come. Likewise, final mile providers can help companies create omnichannel solutions, which would allow retailers’ customers access to their inventory, no matter how or where they are shopping.

For example, At Home, a home and holiday décor superstore with 219 stores in 40 states, recently partnered with PICKUP and Postmates (mentioned previously) to enhance its omnichannel capabilities, a partnership that will allow them to take full advantage of the holiday season. At Home customers now have the increased convenience of speedy local delivery during peak holiday shopping times as well as the standard curbside and buy-online/in-store-pickup options that they now expect. The omnichannel solutions that are created by partnering with final mile providers help retailers build an even bigger moat around their business, allowing them to defend and grow their market share in ways previously not available to them.

(6) Mark Solomon, “Amazon to blanket the ‘burbs with delivery stations,” *FreightWaves*, September 17, 2020.

#1 All U.S. Business Services Transactions

Refinitiv (formerly Thomson Reuters) ranked Houlihan Lokey as the top U.S. M&A advisor in the business services space in 2019.

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2019 M&A Advisory Rankings

All U.S. Business Services Transactions

Advisor	Deals
Houlihan Lokey	24
Raymond James Financial Inc.	13
Lincoln International	13
Generational Equity	12
William Blair & Co	10

Source: Refinitiv (formerly Thomson Reuters).



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Houlihan Lokey's Role

The final mile landscape will remain active and dynamic for years to come as the sector continues to evolve, and Houlihan Lokey is well positioned to help investors, executives, and operators navigate this complexity by virtue of its deep industry experience and platform, including:

- Business model expertise.
- Deep network across the T&L space, including final mile.
- Extensive knowledge of the relevant M&A and financing market trends.
- Hands-on approach with senior-level attention that ensures an optimal outcome for our clients.

Please feel free to reach out to any of the Houlihan Lokey contacts listed in this paper for a conversation about how we can work together. We look forward to hearing from you!

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SELECTED TRANSACTIONS

<p>Transaction Pending</p> <p>synovos SUPPLY AND ASSETS, IN SYNC</p> <p>has agreed to be acquired by</p> <p>e</p> <p>Sellside Advisor</p>	<p>Angel MedFlight a portfolio company of</p> <p>VISTRIA has acquired</p> <p>METRO AIR TRANSPORT</p> <p>Dividend Recapitalization & Acquisition Financing</p> <p>Exclusive Placement Agent</p>	<p>PECO PALLET</p> <p>has been acquired by</p> <p>ALINDA and</p> <p>USS</p> <p>Sellside Advisor</p>	<p>Bristow</p> <p>has merged with</p> <p>Era</p> <p>Buyside Advisor</p>	<p>19TH CAPITAL GROUP a subsidiary of</p> <p>element</p> <p>has completed the sale of certain assets to</p> <p>Hilco Global</p> <p>Sellside Advisor</p>	<p>Merchants AUTOMOTIVE GROUP</p> <p>Series A Senior Secured Notes</p> <p>Growth Capital</p> <p>\$50,000,000</p> <p>Exclusive Financial Advisor & Placement Agent</p>
<p>syncreon</p> <p>has completed a restructuring through English schemes of arrangement, a U.S. Chapter 15 filing and Canadian CCAA</p> <p>Creditor Advisor</p>	<p>Bristow</p> <p>has confirmed a Chapter 11 Plan of Reorganization</p> <p>Company Advisor</p>	<p>JACK COOPER</p> <p>has been acquired by affiliates of Solus Alternative Asset Management through an in-court asset sale pursuant to Section 363 of the Bankruptcy Code</p> <p>Company Advisor</p>	<p>MILESTONE Chassis Company</p> <p>has merged with</p> <p>MILESTONE</p> <p>each a portfolio company of</p> <p>BARINGS</p> <p>Fairness Opinion</p>	<p>PRi</p> <p>has confirmed a Chapter 11 Plan of Reorganization, restructuring \$700 million of debt and raising \$255 million of new debt and up to \$75 million of new equity</p> <p>Company Advisor</p>	<p>Grammer Industries a portfolio company of</p> <p>stalex CAPITAL MANAGEMENT</p> <p>has acquired</p> <p>Sterling Transport</p> <p>Buyside Advisor</p>



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