

FedEx Keeps USPS Contract; No Change to Estimates; Reiterate Buy

As we expected, FedEx kept the U.S. Postal Service (USPS) contract for Priority Mail/Express Mail airfreight linehaul, signing a new seven-year agreement worth roughly \$1.5bn per year. FedEx has provided excellent service to the USPS for roughly 12 years now, so we believe the cost/risk of switching providers was a significant consideration for the USPS in choosing its partner. This should remove some overhang in FedEx's stock price, as some investors feared UPS would steal away FedEx's largest customer, even though we viewed that scenario as highly unlikely. The next couple of quarters could be soft/sloppy for FedEx, as the initial costs of its \$1.7bn operating profit improvement plan will be reported without much benefit being realized yet, but we remain buyers of the shares based on the company recently putting the cold pack on its trans-Pac-itis. As the swelling in its international network comes down, margins and the stock should move higher, in our opinion.

Here is our understanding of the new 7-year, \$10.5bn agreement with the USPS:

- Since the USPS is looking to improve profitability in the face of uncertain and potentially declining volumes, the annual minimum it will pay FedEx under the contract is lower than the prior contract. [We are unsure what those minimum numbers might be, though.]
- Volume is expected to be the same; it is unclear whether or not they were also awarded the small amount of Priority Mail business UPS currently flies, though.
- FedEx operating costs should decline over the course of the 7-yr contract, in our view, due to aircraft fleet replacements and its general domestic express operational restructuring.
- USPS gave FDX \$1.6bn last year, according to one published source (we believe it was less than that, because FedEx does more than just haul Priority Mail and Express Mail for the USPS), but even if we assume the contract next year for the same volume goes from \$1.6bn to \$1.5bn, we believe it would represent a ~\$0.20 EPS headwind (3% of our current EPS estimate) in FY14. Much of this was already baked in, so we will leave our EPS estimates unchanged (company will issue initial guidance for FY14 in June, but we are unsure whether or not they will break out magnitude of the USPS contract headwind).
- Basically, given the potential outcomes of the company's negotiation with the USPS, the contract signed could be considered a "best case scenario" for FedEx. Now, if only the global airfreight market were to enter "best case" mode this year...

Changes	Previous	Current
Rating	—	Buy
Target Price	—	\$131.00
FY13E EPS (Net)	—	\$6.05
FY14E EPS (Net)	—	\$7.15
FY13E Rev (Net)	—	\$44.23B
FY14E Rev (Net)	—	\$45.93B

Price (04/23/13):	\$93.17
52-Week Range:	\$110 – \$84
Market Cap.(mm):	29,522.8
Shr.O/S-Diluted (mm):	316.9
Enterprise Val. (mm):	\$28,392.7
Avg Daily Vol (3 Mo):	2,423,633
LT Debt/Total Cap.:	12.2%
Net Cash/Share:	\$3.56
Book Value/Share:	\$51.30
Dividend(\$ / %)	\$0.56 / 0.6%
S&P Index	1,578.78

EPS (Net)	2012A	2013E	2014E
Q1	\$1.46	\$1.46A	\$1.54
Q2	1.57	1.42A	1.72
Q3	1.55	1.23A	1.57
Q4	2.00	1.95	2.31
FY May	\$6.59A	\$6.05	\$7.15
P/E	14.1x	15.4x	13.0x

Rev (Net)	2012A	2013E	2014E
FY May	\$42.68B	\$44.23B	\$45.93B

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All relevant disclosures and certifications appear on pages 7 - 8 of this report.

Target Price Methodology/Risks

Our 12-month target price is \$131, or 13.5x our CY15 EPS estimate of \$9.70.

Risks to target price:

U.S. and/or global economic downturn, slower-than-expected international growth, failure to achieve targeted profit improvements, sharply rising fuel prices, high fuel prices, price competition from large competitor(s), new competitors, pending litigation concerning the company's independent contractor model and potential for significant legal settlements and changes to operations, unionization of workforce, and any change in IRS tax treatment of independent contractors.

Company Description

FedEx Corp. provides customers and businesses worldwide with a broad portfolio of transportation, e-commerce and business services. With annual revenues of approximately \$43 billion, the company offers integrated business applications through its operating subsidiaries, which compete collectively and are managed collaboratively under the FedEx brand. Those companies are: FedEx Express, FedEx Ground, FedEx Freight, FedEx Office, FedEx Custom Critical, FedEx Trade Networks, FedEx Supply Chain Services and FedEx Services. The company's principal transportation businesses handle an average of over 10 million express, ground, freight and expedited deliveries a day in over 220 countries and territories around the world and to every address in the United States.

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Equity Comps - Transportation

Comparative Valuation Matrix

(figures in \$US millions, except per share amounts)

Company name (Ticker)	Rating	Closing Price 4/23/2013	Diluted S/O	Market cap.	Total Debt	Cash & equiv.	TEV ^(a)	Equity value as a multiple of			Enterprise value as a multiple of					TTM ROA	TTM ROE	TTM ROIC	PEG ratio ^(d)	Div. Yield	2013E FCF Yld	
								Earnings per Share			Book value	TTM Revenue	2013E EBITDA	TTM EBITDA	TTM EBITDAR ^(c)							TTM EBIT
								2012A ^(b)	2013E ^(b)	2014E ^(b)												
Global Integrators																						
Deutsche Post DHL (DPW-DE)	Buy	€ 17.50	1,210.4	27,568.6	6,244.9	3,112.1	32,285.4	13.0x	12.7x	11.2x	1.7x	0.4x	5.9x	5.7x	5.2x	8.4x	5.0%	15.6%	12.5%	0.7	4.0%	15.1%
FedEx Corp. (FDX)	Buy	93.17	316.9	29,522.7	2,242.0	3,372.0	28,392.7	14.7x	14.2x	11.1x	1.8x	0.6x	4.6x	5.5x	5.3x	9.8x	6.4%	11.8%	10.7%	0.9	0.6%	4.3%
TNT Express NV (TNTE-NL)	NC	€ 5.86	543.3	3,183.0	247.7	514.8	2,915.9	NE	NE	NE	0.9x	0.3x	NE	4.4x	4.1x	11.1x	0.4%	0.7%	1.4%	NM	0.0%	NM
United Parcel Service (UPS)	Hold	83.74	954.9	79,965.9	12,870.0	7,924.0	84,911.9	18.5x	17.1x	14.7x	16.9x	1.6x	9.0x	9.5x	9.3x	12.0x	11.9%	74.1%	25.9%	1.3	3.0%	-0.6%
Min				3,183.0	247.7	514.8	2,915.9	13.0x	12.7x	11.1x	0.9x	0.3x	4.6x	4.4x	4.1x	8.4x	0.4%	0.7%	1.4%	0.7	0.0%	-0.6%
Mean				35,060.0	5,401.1	3,730.7	37,126.5	15.4x	14.7x	12.3x	5.3x	0.7x	6.5x	6.3x	6.0x	10.3x	5.9%	25.6%	12.6%	1.0	1.9%	6.3%
Median				28,545.6	4,243.5	3,242.0	30,339.0	14.7x	14.2x	11.2x	1.8x	0.5x	5.9x	5.6x	5.2x	10.5x	5.7%	13.7%	11.6%	0.9	1.8%	4.3%
Max				79,965.9	12,870.0	7,924.0	84,911.9	18.5x	17.1x	14.7x	16.9x	1.6x	9.0x	9.5x	9.3x	12.0x	11.9%	74.1%	25.9%	1.3	4.0%	15.1%
Stifel Transportation Average				7,971.3	1,552.8	472.1	9,086.4	19.2x	18.4x	14.4x	3.1x	1.9x	8.1x	8.9x	8.9x	12.5x	5.1%	15.4%	10.4%	1.1	1.0%	3.5%

(a) Total Enterprise Value = Market Capitalization of Equity + Total Debt - Cash + Market Value of Minority Interest

(b) Stifel estimates for those rated and First Call mean estimates for unrated securities

(c) Enterprise value adjusted to include the capitalization of off balance sheet operating leases with lease expense (or rent expense) being added back to EBITDA for the valuation multiple calculation

(d) 2014E P/E divided by First Call mean or Stifel estimated long-term growth rate

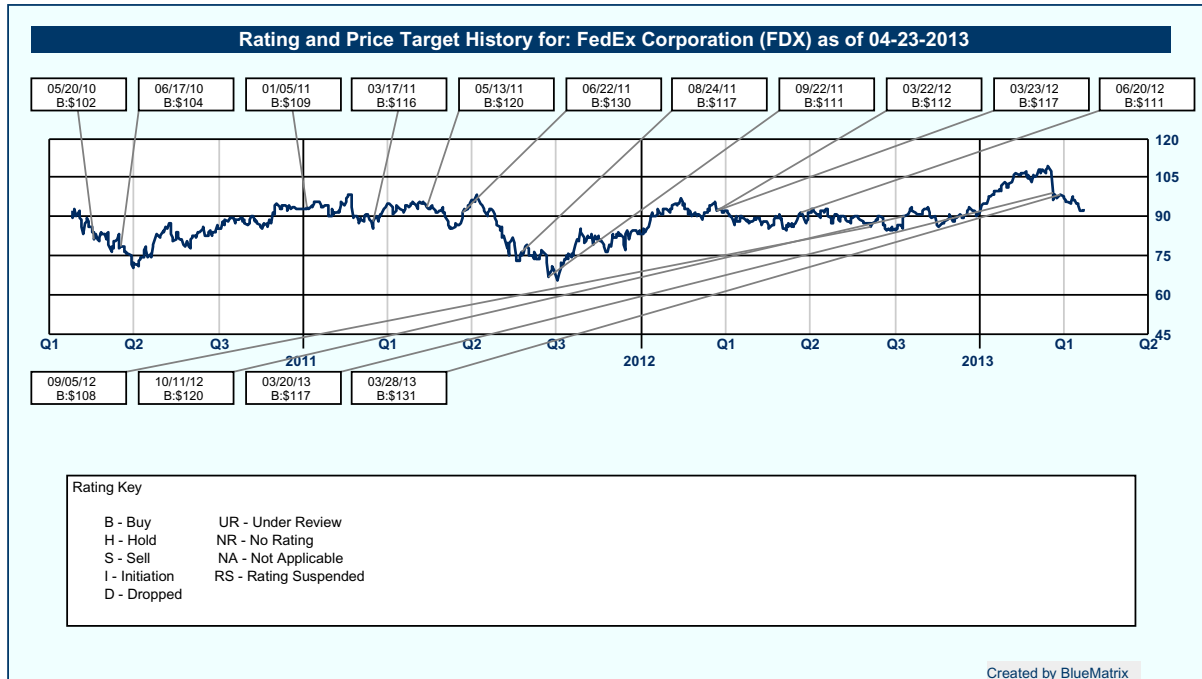
Excludes non-recurring items

Calculations may vary due to rounding

Source: Company data, First Call, and Stifel estimates

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For a price chart with our ratings and target price changes for FDX go to <http://sf.bluematrix.com/bluematrix/Disclosure?ticker=FDX>

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Our investment rating system is three tiered, defined as follows:

BUY -For U.S. securities we expect the stock to outperform the S&P 500 by more than 10% over the next 12 months. For Canadian securities we expect the stock to outperform the S&P/TSX Composite Index by more than 10% over the next 12 months. For other non-U.S. securities we expect the stock to outperform the MSCI World Index by more than 10% over the next 12 months. For yield-sensitive securities, we expect a total return in excess of 12% over the next 12 months for U.S. securities as compared to the S&P 500, for Canadian securities as compared to the S&P/TSX Composite Index, and for other non-U.S. securities as compared to the MSCI World Index.

HOLD -For U.S. securities we expect the stock to perform within 10% (plus or minus) of the S&P 500 over the next 12 months. For Canadian securities we expect the stock to perform within 10% (plus or minus) of the S&P/TSX Composite Index. For other non-U.S. securities we expect the stock to perform within 10% (plus or minus) of the MSCI World Index. A Hold rating is also used for yield-sensitive securities where we are comfortable with the safety of the dividend, but believe that upside in the share price is limited.

SELL -For U.S. securities we expect the stock to underperform the S&P 500 by more than 10% over the next 12 months and believe the stock could decline in value. For Canadian securities we expect the stock to underperform the S&P/TSX Composite Index by more than 10% over the next 12 months and believe the stock could decline in value. For other non-U.S. securities we expect the stock to underperform the MSCI World Index by more than 10% over the next 12 months and believe the stock could decline in value.

Of the securities we rate, 48% are rated Buy, 49% are rated Hold, and 3% are rated Sell.

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