INDUSTRY NOTE

Stephens Inc.
Investment Bankers

February 26, 2007

Thom Albrecht, Managing Director
804-727-6235
talbrecht@stephens.com

Mark Rosa, Associate
804-727-6234
mark.rosa@stephens.com

Neal Deaton, Associate
804-727-6231
neal.deaton@stephens.com

Companies Mentioned:

CLDN	**$18.01**
CVTI	**$11.91**
HTLD	**$17.62**
JBHT	**$28.07**
KNX	**$20.23**
LSTR	**$47.51**
MRTN	**$18.63**
PTSI	**$24.05**
SWFT	**$30.86**
UACL	**$26.93**
USAK	**$17.02**
WERN	**$20.81**
XPRSA	**$20.68**

Truckload

Reason for Report: Industry Update

First Impressions of U.S./Mexico Border Opening

INVESTMENT CONCLUSION:
On Friday, the U.S. Department of Transportation announced it will open up the U.S. market to 100 Mexican trucking firms in a year-long pilot program that could begin in about 60 days. In addition, 100 U.S.-based carriers will be able to haul freight into Mexico. Originally, the border was supposed to open in 1994 but has been postponed since 1995, with a new round of delays in 2001 and 2004. **We anticipate minimal change in the truckload industry during this year-long pilot.** In the short to intermediate term, U.S. carriers with a strong Mexican presence could benefit from both lower costs and increased demand as shippers look to expedite deliveries using carriers already experienced within the Mexican market. **We believe Celadon is the best way to play this development.**

KEY POINTS:

- Under existing law, U.S. carriers are restricted to a 23-kilometer transfer zone on each side of the border. Freight involves 3 drivers and 3 tractors, regardless of whether the freight is northbound or southbound. With the border opening, trucks will be able to go all the way to their final destination.
- **The opening only covers international freight**, i.e., deliveries will not be allowed in between U.S. cities. Once a load is delivered in, say, Dallas, that Mexican truck must return to Mexico, although it can return with a load. It will not be allowed to go from Dallas to Memphis, for example. This is similar to the cabotage laws that govern international airlines arriving in the U.S.
- **Our sense is that most Mexican fleets have feared the opening of the border, while the non-union U.S. truckload industry relishes this opportunity.** Mexican carriers have feared it because their equipment is much older (and less efficient) and due to concerns that carriers will be ripe for consolidation by U.S. companies (see below). Many U.S. carriers have relished it because it could give them access to cheaper labor and/or the opportunity to make acquisitions. However, not every carrier is comfortable with the cultural challenges posed by either a Mexican driver or carrier, so we do no expect as much of a gold rush as some envision.
- **While Mexican labor costs are much cheaper (see next page), that is the only cost advantage for its fleets**. Interest rates for Mexican carriers to finance trucks are significantly above their U.S. counterparts, putting them at a disadvantage. In addition, Mexican fleets, on average, operate older trucks (less efficient and more costly to maintain), while larger U.S. fleets are the safest and best insured in the world.
- **The Teamsters and the owner-operators' trade groups** are likely to be the primary opponents in trucking that oppose this.

See important disclosures and analyst certification on page 3 of this report.

OTHER POINTS TO PONDER

Here are a few other pertinent points to consider. While a lot of uncertainties exist, change is inevitable, and an eventual opening of the border, with no restrictions, is a positive for many U.S. carriers, especially those wanting to make acquisitions.

- **Many Mexican fleets oppose the opening because they anticipate eventually being bought**. Current law limits U.S. carriers to 49% ownership stakes, with two exceptions. Celadon and Swift each bought 100% of a carrier years ago before the current 49% restriction. **We are unaware of any U.S. fleets that have sold stakes to Mexican carriers.** We estimate that at least 100 Mexican fleets have sold up to 49% of their companies to U.S. carriers. In the short term, the 49% limit is expected to remain in place.

- **The opening means rates will come under pressure due to increased capacity. This won't happen with just 100 fleets, in our opinion.** A stringent inspection program will be administered, covering driver records and truck compliance (brakes on Mexican tractors and trailers could be a failing point, for example). Even if/when the entire border opens, we believe most Mexican fleets are ill-prepared to meet U.S. safety and environmental standards. **Canada and the U.S. opened the border in 1989, and rates did not plummet.** While Canadian driver wages were not at a big discount, more of their fleets met U.S. safety and environmental standards.

- **The language barriers are real**, which is why we believe most fleets won't send drivers much past Dallas (a market with a large Hispanic population) for a few years. In addition, some fleets may fear the litigation climate, knowing full-well that various watchdog groups may be looking for opportunities to sue after accidents occur.

- Beside taking advantage of existing ownership stakes to run freight northbound into the United States, some U.S-based carriers will in all likelihood seek to put Mexican drivers in U.S.-domiciled trucks. Our initial sense is that most of those drivers won't go much farther north than Dallas, which is about 450 miles north of the border or about one day's drive. Freight would then be handed off and taken to its final U.S. destination by U.S. drivers. **Celadon already has a leg up on this, as it uses over 105 Mexican drivers to run freight to Dallas rather than Laredo**. Most fleets use zero Mexican drivers.

- **Mexican driver wages for cross-border runs are up to 50% higher than for intra-Mexican runs.** Intra-Mexican drivers make less than $0.15 per mile, while Mexican drivers running to Dallas make $0.20 to $0.24 per mile. U.S.-based drivers make about $0.40 a mile, on average, including benefits. Obviously, some fleets' pay scales, including benefits, are closer to $0.45 to $0.50, but these figures are a guideline of what the "averages" look like.

Who are potential beneficiaries? Celadon is the best way to play this development, in our opinion. Celadon uses Mexican-domiciled drivers to run freight to Dallas. Separately, it also owns a Mexican carrier (Jaguar) that can either grow and expand in Mexico or grow and expand into the U.S. Jaguar generates about $28 million in revenues and operates over 250 trucks. Other carriers, besides Swift, with sizable business in Mexico include Werner and USA Truck. However, both generate less than 10% of their business in and around Mexico, whereas CLDN's business is over 35% and strategically positioned, as it already owns a Mexican fleet and its Mexican drivers already go to Dallas.