# Strategic Report for FedEx Corporation

Mitch Amsler
Jed Cullen
JC Erdmenger

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# Executive Summary

FedEx is a global shipping and solutions corporation that provides services to consumers and businesses worldwide. Headquartered in Memphis, Tennessee, FedEx Corporation is the parent company that provides strategic and logistical support for a variety of operating divisions, currently known as FedEx Express, FedEx Ground, FedEx Freight, and FedEx Services. These various entities compete collectively and are managed cooperatively under the FedEx brand name but operate relatively independently from one another. The company is currently the global leader in the express delivery market and offers delivery to and from individuals and businesses in over 220 countries. In 2009, FedEx was named to Fortune Magazine's *100 Best Companies to Work For* and *10 Most Admired Companies*.

FedEx was unable to escape damage during the economic slowdown and saw its revenues fall slightly and net income plummet in the 2009 fiscal year. The company is subject to high fixed costs due to the nature of the business which made the drop in package volume across all of its divisions in 2009 especially hard to swallow. FedEx, however, cut costs in a strategic fashion, streamlined operations, and continued to invest in both its brand and its customers. As a result, the company is poised to emerge strongly from the recession. After issuing impairment charges of over $2 billion in 2008 and 2009 (mostly related to the 2004 acquisition of Kinko's) that ate severely into its net income, FedEx has posted strong profit results for the first three quarters of FY10. Due to the highly competitive environment in which FedEx operates, the company faces constant pressure to innovate, satisfy consumers, and gain market share. As the company looks to achieve growth in both revenue and profits in the future, it is our recommendation that FedEx focus on additional expansion into international markets, further differentiating itself from UPS, and cementing the superiority of the FedEx brand in the eye of consumers. This can be done through successful implementation of our strategic recommendations listed below.

# Company Overview

## History

The company, conceived as Federal Express, is the brainchild of Frederick W. Smith. While Smith was an undergraduate student at Yale, he wrote an economics term paper about the prospects of overnight delivery service in the computer age; a paper for which he reportedly received a "C". Fedex Corporation's roots trace back to 1970 when Fred Smith purchased a controlling stake in Arkansas Aviation Sales, which focused on selling and trading both new and used airplanes. He recognized that the entities currently involved in the business of shipping packages and airfreight still used inefficient route delivery systems and so he continued to develop his idea for a reliable and more efficient overnight delivery service. Smith came up with the name Federal Express for his new business and incorporated the new company in 1971.

Federal Express operated 14 small planes and offered service to 25 U.S. cities when it officially began operations on April 17, 1973 with the delivery of 186 packages. Smith moved the company headquarters from Little Rock, Arkansas to Memphis, Tennessee shortly thereafter due to its weather and geographic related advantages. The company experienced trying times over the course of its first few years but did finally show its first profit in July of 1975. By this time, the company was delivering an average of 19,000 packages per day.

Fedex benefitted greatly with the passage of the Airline Deregulation Act of 1977 which removed restrictions on routes used by cargo aircraft and allowed for the company to add Boeing 727s and other much larger airplanes to its fleet. The company went public and issued shares on the NYSE in 1978. Over the next two years, Fedex implemented a couple of different centralized computer systems to manage packages, weather, vehicles, airplanes, and people in real time. By 1980, Fedex had expanded delivery to 90 U.S. cities and added Canada to its roster in 1981. It was now delivering over 65,000 parcels daily. In 1983, the company reported over $1 billion in revenues. That year, the company introduced ZapMail, a satellite-based fax service that guaranteed the delivery of up to five pages in less than two hours for just $35. However, the traditional fax machine was just beginning to gain broader acceptance and ZapMail went on to become a huge failure for the company, costing it hundreds of millions of dollars over the course of just a few years. In 1984, the firm made its first acquisition, package courier Gelco Express. Other acquisitions soon followed, including businesses in Europe and the Middle East. International expansion continued in 1985 when Federal Express established a European headquarters in Brussels, Belgium. Sales grew to $2 billion.

Acquisitions in 1987 included Cansica and Island Courier Companies. The firm added to its international holdings in 1988, with the purchase of Italy's SAMIMA and three freight carriers based in Japan. Earnings grew to $188 million as sales neared the $4 billion mark. Federal Express also launched a new unit, called Business Logistics Services, which offered transportation and operations management to other businesses.

In its largest purchase to date, Federal Express paid roughly $885 million for Tiger International Inc. in 1989. Tiger operated an air cargo delivery service known as the Flying Tigers, which held runway rights in major metropolitan airports across 21 countries in Asia, Europe, and South America. The purchase allowed the firm to strengthen its airfreight services, particularly overseas, where sales nearly doubled. However, it also brought with it government safety regulation issues and additional debt. When the deal was completed, Federal Express was forced to contend with a debt load of more than $2 billion.

By the start of the 1990s, Federal Express held 43 percent of the express transportation market, compared to the 26-percent market share of its largest rival, UPS. The firm effectively brought a price war to its close when it upped its rates for the first time in seven years. The following year, the company launched international cargo service EXPRESSfreighter and a new subsidiary known as FedEx Aeronautics Corp. In May of 1992, Federal Express shuttered its domestic operations in Italy, Germany, France, and the United Kingdom, focusing instead on shipping freight to and from Europe, rather than from one destination to another within the continent. By the end of the year, sales had grown to $7.6 billion. Express packages delivered daily averaged 1.4 million in 1993.

In 1994, Federal Express changed its name to FedEx finding that customers used the term as a verb, meaning, "to send an overnight shipment." That same year, the company also launched www.fedex.com. To compete with the same-day delivery and early morning delivery services offered by UPS, FedEx began offering similar services for both packages and letters in 1995. The firm also began making deliveries to eight countries located in the former USSR. Targeting the rapidly growing small business and home office markets, FedEx convinced OfficeMax to let it place self-service drop boxes at OfficeMax stores nationwide. The firm also became the only U.S. cargo carrier allowed to fly in China with its acquisition of Evergreen International Airlines. The firm's fleet had grown to 590 airplanes and 38,500 vehicles. In 1997 FedEx opened its hub at Fort Worth Airport and in 1999 opened a European hub at Charles de Gaulle International Airport in France.

FedEx benefitted in the form of 850,000 additional packages per day when UPS employees went on strike in 1997. The company created FDX Corp. with the acquisition of ground carrier Caliber System Inc. in 1998. Subsidiaries also included in the deal were Roadway Package Systems (RPS), Roberts Express, and Viking Freight. This move allowed FedEx to begin competing properly with UPS for market share in the domestic ground delivery market.

In January 2000, FedEx unleashed the power of its global brand. In a move to further integrate the company's portfolio of services, FDX Corp. was renamed FedEx Corporation. In addition, Federal Express became FedEx Express, RPS became FedEx Ground, Roberts Express became FedEx Custom Critical, Viking Freight became FedEx Freight, and Caliber Logistics and Caliber Technology were combined to make up FedEx Global Logistics. To centralize the sales, marketing, customer service and information technology support for FedEx Express and FedEx Ground, a new subsidiary named FedEx Corporate Services was formed and began operations in June 2000. Over the next few years, a number of acquisitions and realignments further changed the size and scope of various FedEx operating companies. FedEx Corp. soon acquired TowerGroup and World Tariff Ltd. and later rebranded them as FedEx Trade Networks Transport & Brokerage, Inc.

In 2001, FedEx Express signed a 7-year contract to transport Express Mail and Priority Mail for the United States Postal Service. This contract allowed FedEx to place drop boxes at every USPS post office, and has recently been extended until September 2013. USPS continues to be the largest customer of FedEx Express.

FedEx Corp. acquired Kinko's Inc. in February 2004 for $2.4 billion in cash to better compete with UPS after their acquisition of Mailboxes Etc. in 2001. Two months later, Kinko's was rebranded as FedEx Kinko's (and later as FedEx Office in 2008). For FedEx, the acquisition meant expanded retail access to all of the 1,200 FedEx Kinko's stores in operation at that time, enhanced FedEx document management services and a broader reach to customers of all sizes. In September 2004, FedEx Corp. acquired Parcel Direct, a leading parcel consolidator, and later rebranded it FedEx SmartPost. This acquisition served to complement the company's contract with USPS and provides customers in the e-retail and catalog segments with a proven, cost-effective solution for low-weight, less time-sensitive residential shipments.

The financial crisis of 2007–2010 hit FedEx Corporation and especially its revenue leading Express division hard. Many companies looking for ways to save money stopped shipping altogether or moved to cheaper alternatives, such as ground, freight and sea shipping. FedEx Corporation announced large network capacity reductions at FedEx Express, including retiring some of its oldest and most inefficient aircraft such as the McDonnell Douglas DC-10 and the Airbus A310. FedEx also announced layoffs and work hour reductions at some of its hubs. Additionally, the company implemented temporary freezes in pay, and eliminated retirement fund matching contributions, and bonuses for employees.

## Business Model

FedEx is a global shipping and solutions corporation that provides services to consumers and businesses worldwide. Headquartered in Memphis, Tennessee, FedEx is led by FedEx Corporation, which "provides strategic direction and consolidated financial reporting for the operating companies that compete collectively under the FedEx name worldwide: FedEx Express, FedEx Ground, FedEx Freight, and FedEx Services." These companies function under the motto of "operate independently, compete collectively and manage collaboratively." By operating independently, each FedEx company can focus exclusively on delivering the best service for its specific market and avoid wasting time and resources on problems unaffiliated with its core market. Competing collectively under the well-known FedEx name ensures that all of the operating companies benefit from being a part one of the world's most recognized brands.

FedEx Corporation has invested heavily in innovation and capital over the years, but its main driver of expansion and growth has traditionally been through acquisitions. Previously, the company kept the name of its acquisitions intact but, starting in 2000, it began to leverage the power of its brand and renamed all of its various divisions under the FedEx banner. Also at the core of the company's business model is its employment structure where all drivers are classified as contract workers as opposed to full-time employees.

FedEx is currently a $29 billion company and posted revenues in excess of $35.5 billion in fiscal 2009. From shipping just 186 packages on its first day of operations back in 1973, the company has grown to the point where it now handles approximately 8 million shipments on a daily basis. Across all divisions, FedEx operates a fleet of 660 aircraft and over 80,000 vehicles, while employing 280,000 individuals and serving over 220 countries.

The company's flagship division, FedEx Express, is currently the worldwide leader in the express delivery and transportation market, providing nearly two-thirds of the company's revenue stream. It utilizes a global network of planes and vehicles to provide time sensitive delivery with a money-back guarantee ensuring an on-time delivery. FedEx Express is often utilized for transportation of documents and small packages that necessitate a speedy (generally same day or next day) delivery. FedEx SupplyChain and FedEx Trade Networks provide full service, end-to-end support for companies utilizing FedEx for international trade purposes. Both of these also fall under the FedEx Express segment. FedEx Express generated an operating profit of $794 million on revenues of $22.364 billion in 2009. Last year this division handled approximately 3.4 million packages and 10 million pounds of freight on a daily basis.

FedEx Ground was formed with the acquisition of Roadway Packaging Systems (RPS) back in the late 1990s when FedEx sought to better compete with UPS in the domestic ground delivery market. This operational unit generally caters to those needing small and medium packages delivered to business addresses, especially those which are less time sensitive. A unit of FedEx Ground, FedEx Home Delivery, is designated for retailers and individuals who are shipping to residential areas. Drilling further down, FedEx SmartPost utilizes the USPS for final delivery to residences. FedEx Ground posted an operating profit of $807 million on $7.047 billion in revenues in the 2009 fiscal year. This was the first time in the company's history that the Express segment did not lead the company in operating profit. Utilizing a fleet of over 22,000 delivery vehicles, FedEx Ground handled an average of 3.5 million packages per day in 2009.

FedEx Freight was formed through the acquisition of Viking Freight and subsequent acquisition of American Freightways. This division operates in the less-than-truckload (LTL) market and allows customers and businesses to transport larger shipments on a less time-sensitive schedule. FedEx Custom Critical also operates under this banner and provides fast, door-to-door same day and next day delivery of urgent freight, specialty/valuable items and hazardous goods. FedEx Freight had an operating loss of $44 million on $4.415 billion in revenue and was charged with handling an average of 779,000 shipments per day in 2009. Rate increases have been announced to help ensure that this unit does not operate at a loss for the foreseeable future.

FedEx Services provides marketing, information technology, planning, and administrative services for the umbrella of FedEx units with the purpose of serving a support function to the revenue-generating transportation and delivery divisions. The exception to this is FedEx Office (formerly FedEx Kinko's), which FedEx created after acquiring Kinko's for $2.4 billion in 2004. FedEx Office provides over 1,900 brick-and-mortar locations for individuals and businesses to access the FedEx plethora of services and delivery options. FedEx Services generate revenues of just $1.977 billion and posted an operating loss in fiscal 2009 of over $800 million for the second year in a row due to large impairment charges associated with the Kinko's acquisition. Profit in this unit has steadily declined since 2004.

# Competitive Analysis

| Force | Strategic Significance |
|---|---|
| Internal Rivalry | High |
| Supplier Power | Low to Moderate |
| Buyer Power | Moderate |
| Threat of New Entrants | Very Low |
| Substitutes and Complements | Moderate |

## Market Definition

Broadly speaking, FedEx Corporation operates in the shipping and delivery market. The North American Industry Classification System (NAICS) defines FedEx under code 4921, which is classified Couriers. FedEx's Standard Industrial Classification (SIC) is under Air Courier Services, code 4513. Although the company began operations strictly in the domestic express delivery services market, over time it has expanded into ground, freight, and less-than-truckload (LTL) shipping both domestically and worldwide.

## Internal Rivalry

FedEx competes quite heavily with other firms across all of its service lines. They are especially well-known for their intense rivalry with competitor UPS. These two firms, along with DHL and other, smaller players, compete most notably with each other on price. Interestingly enough, despite offering a lower price for most services due to government subsidies, the USPS doesn't really compete with FedEx in the same sense that UPS does. UPS is far and away the leader in the US domestic ground shipping market with a current market share of nearly 60%. However, since its acquisitions of RPS Ground and Caliper Systems in the late 1990s, FedEx has found success in slowly, but surely eroding UPS' dominance in this arena. Unfortunately, UPS has also moved to take market share from FedEx in the express delivery market. The two firms are in a constant battle to maintain market share in their respective areas of expertise while becoming a larger player in the other's arena. Both firms spend heavily on advertising and often match each other when it comes to fuel surcharges, increases/decreases in pricing, and even acquisitions (UPS purchased Mailboxes Etc.; FedEx followed suit with its purchase of Kinko's). When it comes to the international shipping market, DHL is considered to be the leader. FedEx, however, benefitted greatly when DHL chose to exit the US express delivery market a few years back. The company is attempting to better compete with DHL by acquiring companies that are already established in various international markets and investing heavily in infrastructure (planes, trucks, routes, and hubs) in those locales. As can be seen in the chart above, rivalry is the most significant of Porter's Five Forces for FedEx. A number of reasons that explain the intensity of the rivalry are presented in more detail under the other Forces. These include the presence of high fixed costs, a low level of product differentiation, and low switching costs in the industry.

## Supplier Power

The bargaining power of suppliers is a bit confusing to analyze because there are considered to be a few separate and distinct types of suppliers to the company. Those that supply products to the company such as packaging materials, vehicles, and planes have a relatively low degree of power because of the competition present in their respective industries and the general indifference that FedEx has towards using one company over another. Sure, FedEx may have a relationship with a particular supplier of boxes but that tends to go out the window if a competitor offers a somewhat better substitute. The same is true when it comes to the company's vehicles and planes. It makes sense to order these respective modes of transportation in bulk from a single company for price and maintenance purposes, but the competition in these industries intense enough, and FedEx is a large enough player that it is actually the one with the power. Suppliers of fuel to FedEx do have some degree of bargaining power as the company is nothing without fuel, but they can partially offset their vulnerability with futures contracts and/or fuel surcharges. Those that supply services to FedEx such as pilots, drivers, mechanics, and sorters do possess bargaining power, but it pales when compared to the immense power that the equivalent employees at rival UPS hold. At FedEx, only the pilots are unionized, whereas at UPS, nearly all employees are represented by unions. As long as the company ensures that its drivers remain independent contractors and continues to invest in implementing increasing levels of automation throughout the shipping process, employees will continue to exhibit low bargaining power. The supplier with the largest amount of power over FedEx is actually the Federal Aviation Administration (FAA) which controls access to what is known as the National

Airspace System (NAS). The FAA has the power to grant or restrict landing rights as well as access to airspace. The same power is true of equivalent governing bodies in the foreign nations in which FedEx operates. Generally, once airspace and landing rights are issued, they are not taken away, but the company is still much more vulnerable to these government entities than it would prefer to be.

## Buyer Power

Buyer bargaining power is moderate in the industry because of the presence of fierce competition and low switching costs. Although individual users of FedEx's services possess little power, larger companies that contract with FedEx for shipping purposes wield a high degree of power because of the large amount of business that they bring to the company. FedEx and UPS compete heavily (see Internal Rivalry) for the right to serve these companies and, since both offer the same general services, they must do so via price.

## Threat of New Entrants

The threat of new entrants realistically competing with FedEx is very low. This is due in large part to the huge costs associated with entering the delivery market on a wide scale. The capital expenditures that would be necessary to acquire the proper levels of planes and vehicles combined with building up the necessary infrastructure is mind boggling. Secondly, it is important to address the roadblock that a new firm would face in the form of the Federal Aviation Administration and air routes/landing rights. The extent of difficulty that a new entrant would face in competing in this industry is exemplified by the fact that, despite its existing shipping infrastructure, huge capital expenditures, and dominance in the ground shipping market, UPS has had a lot of difficultly competing with FedEx in the express delivery market. International behemoth DHL invested heavily to the tune of $10+ billion in an attempt to compete with FedEx in US express delivery and left the market with its tail between its legs after a just a handful of years. Additionally, FedEx has shown that it's not afraid to spend its cash to acquire companies operating in a region or sector that it desires a presence.

## Substitutes and Complements

The worldwide expansion of the internet has served as both a bane and a boon to FedEx and the shipping/delivery industry as a whole. On the one hand, just as with the fax machine, the emergence and now commonplace use of e-mail has undoubtedly cut into FedEx's revenue stream, specifically in the overnight letter delivery market. While individuals and businesses can now use fax machines and e-mail for certain papers that they would have shipped overnight in a previous era, many important documents still necessitate an express delivery of a hard-copy. On the other side of the coin, FedEx has benefitted enormously from the emergence of electronic retailers and the continued globalization of the economy. Generally speaking, the threat of substitute products is very low, as the only real substitutes present in the shipping market are the method by which a product is shipped. FedEx currently offers most delivery options, including air express, ground, home delivery, truckload, freight, etc., so customers can switch between delivery methods and still retain the company's services.

Complements represent a very important force for the shipping industry. By offering certain complementary products and services, a firm can serve to differentiate itself from the competition in this industry. A customer is certainly invested in price and convenience when shipping something, but they are also invested in being party to a successful, on-time, and hassle-free delivery for their own benefit and more importantly for the benefit of the recipient. This is especially true for online companies that need to ship products to customers. In order for their business to remain successful, they need to be able to rely on a shipper to consistently offer a premium delivery experience to the consumer. Initially, only those with a FedEx account could easily use the company to deliver a product. FedEx recognized that access to services and ease of use was a huge factor in obtaining and retaining business. In response, the company has installed drop boxes at USPS offices, Staples and Office Max stores, and other locations, all in addition to developing a true brick-and-mortar presence through its acquisition of Kinko's. Other complements that are present include online tracking of packages, online pickup requests, delivery guarantees, and shipping insurance.

# SWOT

## STRENGTHS

- Strong brand image
- Unmatched reputation for on-time delivery
- Lots of planes, well-located hubs, great routes/landing rights
- Ranked as one of the best companies to work for many years in a row
- Great R&D, quite innovative
- Extensive capital expenditures
- Focus on customer satisfaction
- Clear leader in domestic express delivery market
- At present, drivers are independent contractors, unlike at UPS where they are unionized

## WEAKNESSES

- High prices relative to competitors
- Not as strong internationally
- Lag UPS in the ground delivery market
- Not fully differentiable from UPS
- Very exposed to economic conditions and fuel prices

## OPPORTUNITIES

- Economy is beginning to recover, especially in Asia (China specifically)
- Currently offer services to 220+ countries and barring government intervention, can expand in them as it sees fit
- Continued globalization of the world marketplace means more contracts are available and at higher volumes as well
- Expansion of online retailing creates an increased need for on-time, hassle-free shipping
- Focus on taking away international market share from DHL and domestic ground delivery from UPS

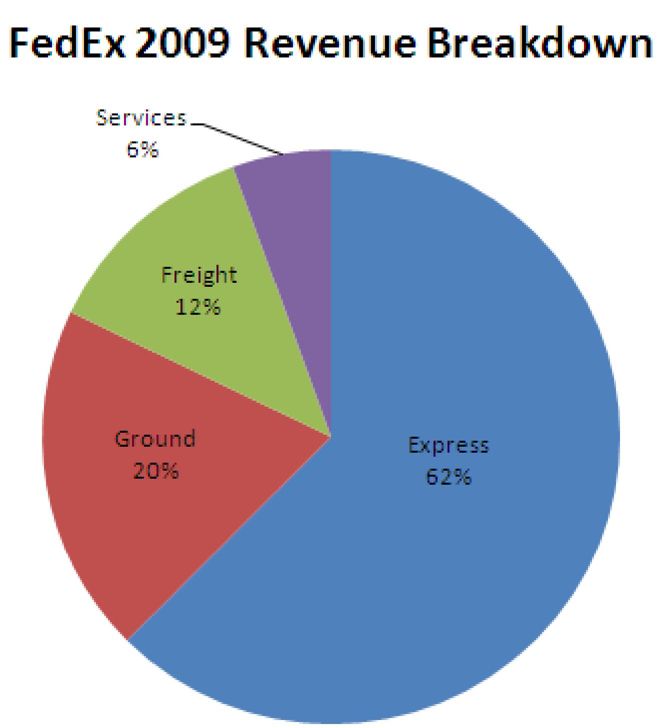
## THREATS

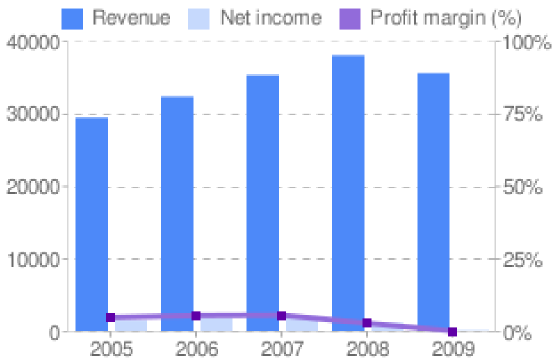
- High fixed costs
- Drivers and other workers are trying to unionize
- Economic downturn has cut down on volume overall
- Many consumers and businesses are switching to slower delivery options to save money
- UPS is attempting to take away market share in the express delivery arena
- E-mail may take away from overnight document delivery market

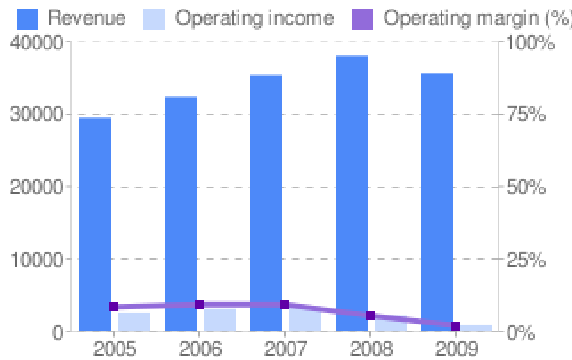
# Financial Analysis

## Overview

Fedex reported revenues of $35.497 billion for fiscal 2009 (ending 5/31/2009), down 6.47% from $37.953 billion in FY08. Additionally, in FY09, gross profit fell 11.2% to $9.058 billion while net income plummeted 91.3% to just $98 million. Needless to say, it's quite obvious that the recession hit the company fairly hard, especially because nearly two-thirds of its revenue comes from its Express division which offers the fastest and therefore most expensive form of shipping to consumers and businesses.






However, the company has managed to recover fairly well in fiscal 2010, posting net income of $181 million, $345 million, and $281 million in the first three quarters, respectively. In Q310, revenue rose 7% from its Q309 level to $8.70 billion. Remarkably, as we emerge from the recession, FedEx appears to have gained market share as smaller, weaker competitors were forced to cease operations. The company was hit hardest by the overall drop in volume that it was shipping across all service lines on a daily basis but it cut costs and streamlined operations to mitigate the damage. All of the company's business lines saw increases in profit and revenue for the most recent quarter, with the exception of FedEx Freight which posted a loss due to increased costs. The company has announced a nearly 6% rate increase for this segment which its customers appear quite willing to accept.

## Solvency and Liquidity

| | **2009** | **2008** | **2007** | **2006** |
|---|---|---|---|---|
| Debt as % Assets | 10.65% | 7.83% | 11.03% | 10.76% |
| Debt as % Equity | 18.96% | 13.82% | 20.91% | 21.21% |
| Current Ratio | 1.57 | 1.35 | 1.22 | 1.18 |
| Cash as % Current Assets | 32.21% | 21.25% | 23.67% | 29.97% |
| Receivables % Current Assets | 47.65% | 60.17% | 59.47% | 54.39% |

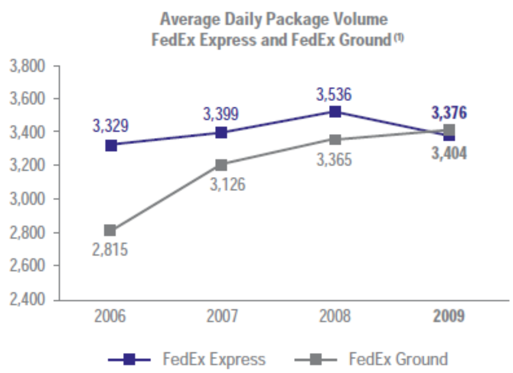
Over the past five years, FedEx has reduced its debt load by $1 billion while increasing shareowner equity by $5.6 billion during the same period of time. It has done an excellent job of reducing its debt specifically over the past few quarters from $2.58 billion in Q409 to $1.95 billion in Q310. Their debt, both long-term and short-term is relatively insignificant when viewed as a percentage of assets or equity. Competitor UPS presently has a much higher debt load and consequently, its debt as a percentage of assets and debt as a percentage of equity are 29.86% and 124.78%, respectively. Despite its proclivity for acquisitions and recent expansion plans, FedEx far outpaces UPS when it comes to debt management. It does initially serve as some cause for concern that FedEx has posted a -$743 million net change in cash through the first three quarters of fiscal 2010 but, with $1.55 billion of cash still remaining in its coffers, this does not pose a problem at present. It is also important to note that most of this cash used in FY10 has gone towards paying off debt early. FedEx currently sports a very impressive current ratio of 1.57, which has increased at an increasing rate every year since 2006 as a result of paying down debt and increasing assets.

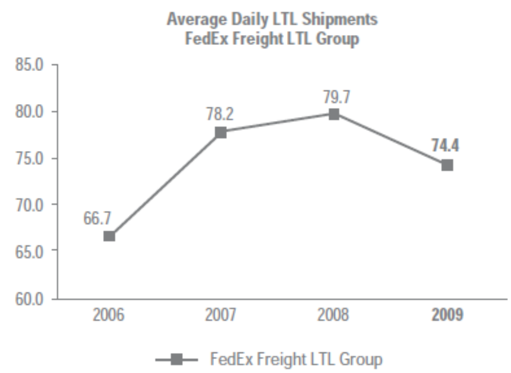
## Profitability and Growth

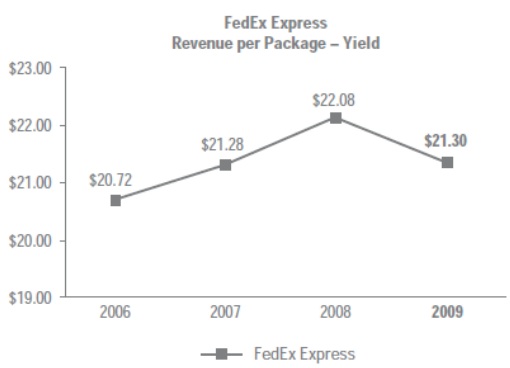
FedEx paid $2.4 billion to acquire Kinko's in 2004. In 2008, the company issued an $891 million impairment charge on this acquisition. In FY09, yet again the company wrote down an additional $810 million as a goodwill impairment charge related to this acquisition. Additionally, the company also wrote off $90 million related to poor performance of FedEx National LTL (acquired in 2006 as Watkins Motor Lines) and $300 million in aircraft related asset impairments and employee severance and facility reduction costs. The good news about these write downs is that there is essentially nothing left from the Kinko's deal for future impairment and in 2009, of $1.2 billion in write downs, $1.1 billion was considered to be "non-cash".

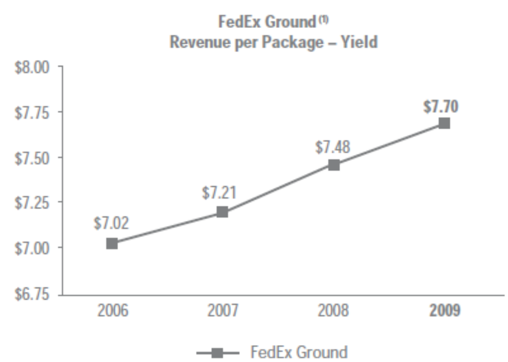
FedEx has properly recognized that the economy will recover more quickly internationally than it will domestically and has moved to position itself to better take advantage of this. Most recently, its new advertising campaign, "FedEx Delivers to a Changing World," indicates that it is moving ahead internationally. Six new freight-forwarding offices were recently opened in Europe, the Middle East, Africa and Latin America. Since 2008, FedEx has opened 22 international freight-forwarding locations. FedEx also rolled out its first Boeing 777 Freighter to serve mainland China, with plans to have as many as 15 of the planes in service by 2014. Internationally, the company is expanding service in Asia to capitalize on growth there, just recently opening its largest hub outside of the U.S. in Guangzhou, China. Domestically it's pursuing more commercial business at this time because that's where current growth can be found. In addition, the company streamlined operations and implemented huge cost reductions during the heart of the recession that are continuing to pay dividends.

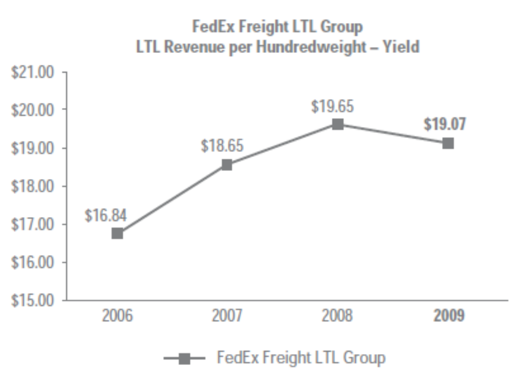
The Ground division at FedEx proved to be the one shining star in fiscal 2009, with revenue per package increasing by 3% and average daily volume also inching up by 1%. On the flip side of the coin, FedEx Express and FedEx Freight saw respective declines of 3.5% and 3% in revenue per package and volume drop-offs of -4.5% (Express) and -6.6% (Freight).



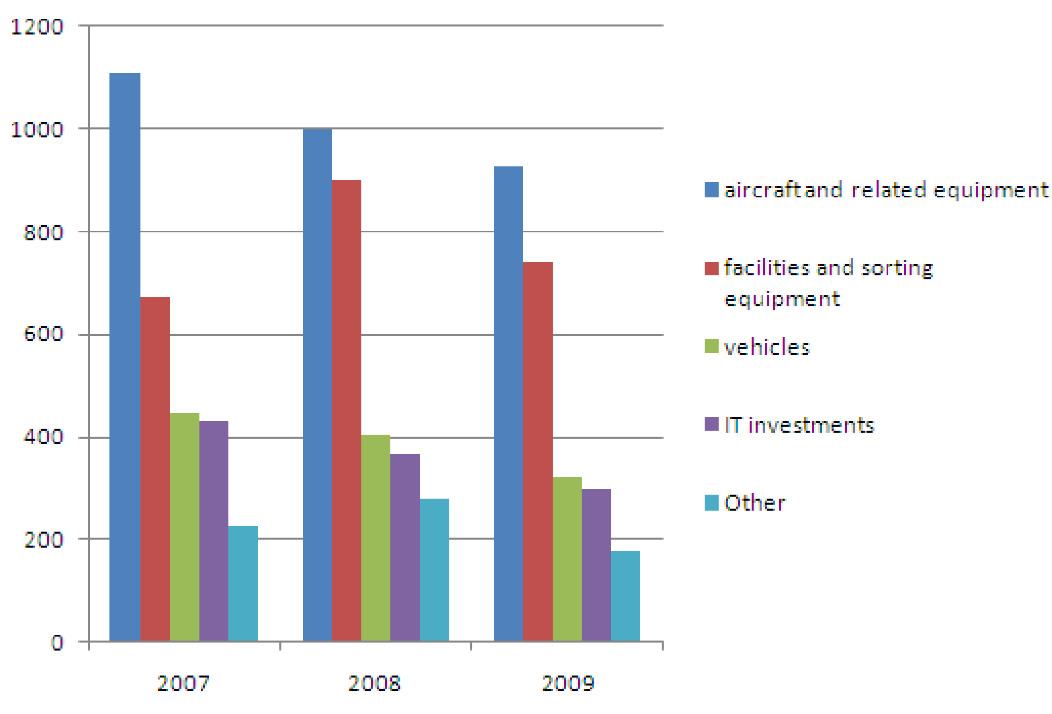



Fedex, however, has benefited recently from higher shipping volume, particularly at its international Express and Ground units. Led by exports from Asia, average daily volume in International Priority packages grew 18 percent year-over-year for the most recent quarter. Average daily package volume at FedEx Ground, concentrated in the US, grew 5 percent. Most of that growth was due to businesses shipping more packages to other businesses as US consumers have yet to show the same signs of a turnaround. Excluding the Freight division, the first three quarters of fiscal 2010 have been kind to FedEx with regard to daily volume and yield (revenue per package) in terms of a year-over-year comparison.

The company has always made capital expenditures a huge part of its business model, which is a big reason that ROA and ROE have tended to lag UPS and the industry in most years. The company opines that its cash can be best put to work in constantly improving and upgrading everything upon which its livelihood depends. Although the company's capital expenditures dropped to approximately $2.46 billion in 2009 as it weathered the recession, FedEx recently announced that 2010 capital expenditures will return to its 2008 level of $2.9 billion. The company estimates that in FY10, 61% of capital expenditures will go towards "growth initiatives" with the remaining 39% designated for ongoing maintenance activities.

Annual Capital Expenditures in Millions of USD



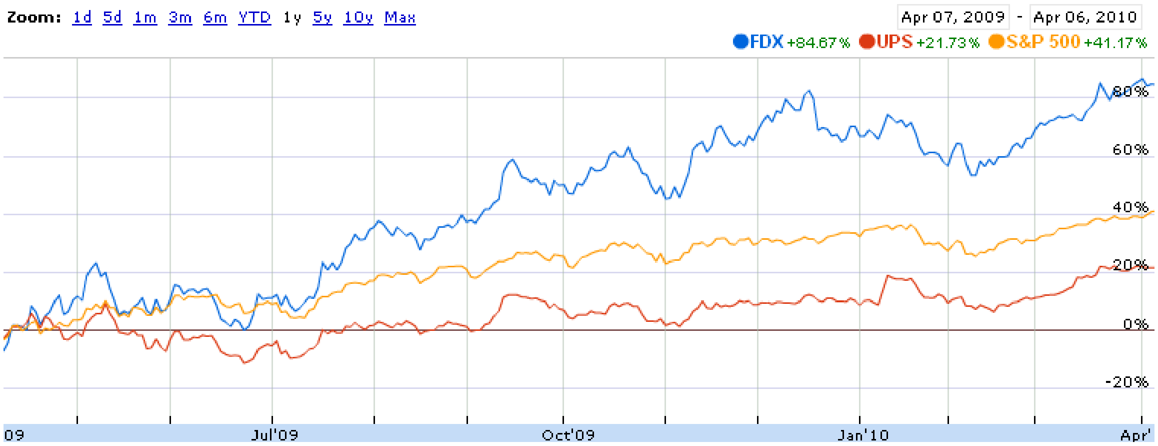
## Stock Price Analysis

FedEx Corporation is listed on the NYSE under the ticker FDX. As of the closing bell on April 13, 2010, the stock was trading $92.37. At just over 313 million shares outstanding, the company presently has a market capitalization of nearly $29 billion. As shown in the charts below, the stock is up 85% from April 2009, but is actually flat from where it was trading five years ago in April 2005.



Across the board, analysts are predicting strong growth in the coming years for FedEx Corporation and expect package volume, revenues, and earnings to exceed peak levels from 2008 by the 2011 fiscal year.

Relative to its archrival UPS and the S&P500 index, FDX has significantly outperformed over the past twelve months. This is due in large part to the strong recovery that FedEx has shown over the past three quarters after a disappointing FY09.




# Strategic Recommendations

The global shipping and transportation market is often viewed as a leading indicator of where the global economy is headed, and based on the results posted by FedEx and UPS over the past few quarters, things are certainly looking promising. We are of the opinion that FedEx has thus far done an excellent job of strategically positioning itself to take full advantage of a recovery in the economy.

FedEx's $2.4 billion acquisition of Kinko's in 2004 has proved itself to be a nightmare. Profit in this division has steadily declined since 2004, culminating with FedEx issuing write downs of over $1.6 billion in impairment charges in the past two years with respect to this acquisition. This deal was an ill-conceived attempt to match UPS' new retail presence with its pickup of Mailboxes, Etc. The synergies that FedEx expected from running Kinko's never materialized and the value of the Kinko's brand name has been marginalized. Vector Strategy Group advises the company to invest in transforming the FedEx Office division back into the well-respected company that Kinko's was before its acquisition. This means an investment in people/training (customer service), capital (facilities and equipment upgrades), and advertising. As the US economy recovers in the coming years, consumers and small businesses will once again require more of the services that FedEx offers. The company is advised to make it be known that FedEx Office is a retail storefront for which all of the company's other services can be utilized. As the internet continues to be more ubiquitous in everyday life, we would also recommend investing in an upgrade of the FedEx Office website to allow for easy online ordering and submission of material for copying/binding/etc. Theoretically, it should be possible for a consumer or business to have something printed and then shipped/delivered without ever needing to leave their computer. One other possible way to eventually realize value for shareholders from this deal would be to spinoff the vast amount of real-estate acquired into a REIT. However, for the foreseeable future, we do not advise such a transaction because the company has adequately positioned itself for good shareholder returns through strong growth in all other divisions in addition to already marking down the majority of this asset.

Interestingly enough, because it began as a company specializing in air express shipping, FedEx is treated similarly to an airline and is therefore governed by the Railway Labor Act (RLA). Its chief competitor, UPS, which began as a ground shipping company, is treated as a trucking company and thus governed by the National Labor Relations Act (NLRA). Consequently, it is much easier to unionize at UPS, who is presently the biggest employer of Teamsters, with over 240,000 of its employees unionized. At FedEx, only its 4,500 pilots are union members, as its drivers are subjected to different rules that make it very difficult to unionize. The company dodged a bullet when the U.S. Senate just recently passed a new version of the FAA bill which, unlike the House of Representatives bill that just passed, did not include a provision for switching FedEx to henceforth be subjected to the NLRA. FedEx drivers currently function as independent contractors who often own and insure their own trucks, and have the ability to operate multiple routes, sell routes, and hire helpers/additional drivers. In short, entrepreneurial potential is present. In addition to the obvious benefits that classifying drivers as contractors presents (no ability to strike, lower pay and benefits), it gives drivers more autonomy and therefore some incentives to do their job better. We advise that the company continue to monitor the situation very closely and continue spending money on advertising and lobbying to maintain its classification status under the RLA. UPS will continue to fight extensively for changes in the FAA bill to give it a more level playing field and FedEx needs to keep Congress, its employees, and the general public (its customers) on its side in this battle. It is estimated that FedEx saves over $400 million annually through employing its 100,000+ drivers as contractors. We believe that it would be highly beneficial for the company in the long run to better please its employees through meaningful merit raises, various incentive bonuses, and other benefits. Setting aside a portion of estimated savings each year for the aforementioned payouts would greatly increase employee morale, overall efficiency, and company image.

Although FedEx was at the forefront of the industry when it gave customers the ability to track packages on its website back in the mid-1990s, barcode scanning and tracking is quite the norm in the industry nowadays. We believe FedEx can generate more business and even further cement its reputation for accurate, on time delivery by offering real-time tracking of packages for an extra fee. Firstly, scanning by barcode is a laborious process that is not always accurate. Switching to RFID (radio frequency identification) tagging for packages will save costs in the long run and improve accuracy because these can hold much more information and only require that the package be within a given range. This can be further supplemented with the installation of GPS tracking on all delivery modes (planes, trucks, trains). Combining these two tracking methods would allow a customer to track not only when the shipment enters/leaves a sorting facility or is in route to a new location, but where exactly that truck/plane is at a given time. Thus, they can better know when to expect delivery. In consulting with industry experts, Vector Strategy Group is of the opinion that the next step is to offer the option of GPS tracking on an individual envelope or package for an extra fee. This would be especially useful when shipping highly sensitive or important documents and other valuable items to ensure the customer of their safe delivery. Although the costs of such implementations may outweigh monetary benefits in the near future, the intangible benefits that this extra service brings would be invaluable to the overall business.

Although FedEx has done a good job of moving into the international arena, we'd like to see it make an even bigger impact. The domestic market offers a limited amount of growth and upside, whereas the international marketplace presents a much larger playing field from which to grow and operate. It is estimated that the international package market will grow by 5-6% in the coming years, which is nearly double the expected annual growth in world GDP. We believe that the company should continue investing capital in planes, vehicles and infrastructure, especially in Asia (China specifically), but also focus on penetrating into foreign markets by partnering with local carriers. FedEx has the technological innovation, cash, and capital necessary to elevate a foreign, regional player to the next level. In turn, FedEx would receive valuable local insight into a relatively foreign and unknown market. FedEx should set up contracts that give it the option to purchase said companies for a given price if it sees a profitable future by operating and expanding into that market.

The company should continue spending heavily on advertising. When people need something delivered quickly, safely, and on-time, they say they need to "FedEx" it. This needs to be further leveraged to the benefit of the other service lines offered by the company. FedEx should work to maintain a controlling stake in the express delivery market while stealing share from UPS in domestic ground delivery. It can do this by further differentiating itself from UPS through actual innovation and service offerings or simply through manipulation in consumer perception. A big issue with the shipping business is that buyers generally have little to no brand loyalty and incur negligible switching costs when changing from one provider to another. Securing more business partnerships, even at slightly lower margins, will help develop loyalty to the brand. This is especially true of long-term contracts with large firms. One last thought would be for FedEx to offer immediate delivery and same-day guarantees on documents shipped within certain predetermined geographic areas (essentially serving the same function as a courier/bike messenger). Although branching out into a market like this may not bring much in the way of additional revenue, we believe that it would build the brand in the eye of the consumer. One of the main operational strategies that distinguishes FedEx is the autonomy under which each division operates. Obviously, this business model has worked just fine for the company, however, we would advise commissioning a study to ascertain both the financial and intangible benefits and drawbacks associated with functioning in this manner. The reality of overlap in deliveries to businesses with regard to the Express and Ground divisions is slightly worrisome, and our firm believes that there is a way to minimize this problem while still preserving the current independence of each division.

Looking forward, Vector Strategy Group believes that FedEx Corporation has optimally positioned itself for growth opportunities in the domestic ground and international markets (especially Asia) in the coming years. With the exception of its purchase of Kinko's, management has exhibited a stellar track record of acquisition and expansion, in addition to showing good financial restraint during times of easy credit. The company has proven to investors and customers that it can operate successfully, even in a tough economic climate.

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# Appendix

## Income Statement

| In Millions of USD (except for per share items) | Thru Q310 | 2009 | 2008 |
|---|---|---|---|
| Revenue | 25306 | 35,497.00 | 37,953.00 |
| Other Revenue, Total | 0 | - | - |
| Total Revenue | 25306 | 35,497.00 | 37,953.00 |
| Cost of Revenue, Total | 18978 | 26,439.00 | 27,754.00 |
| Gross Profit | 6328 | 9,058.00 | 10,199.00 |
| Selling/General/Admin. Expenses, Total | 0 | - | - |
| Research & Development | 0 | - | - |
| Depreciation/Amortization | 1470 | 1,975.00 | 1,946.00 |
| Interest Expense(Income) - Net Operating | 0 | - | - |
| Unusual Expense (Income) | 0 | 1,204.00 | 882 |
| Other Operating Expenses, Total | 3556 | 5,132.00 | 5,296.00 |
| Total Operating Expense | 24004 | 34,750.00 | 35,878.00 |
| Operating Income | 1302 | 747 | 2,075.00 |
| Interest Income(Expense), Net Non-Operating | -52 | - | - |
| Gain (Loss) on Sale of Assets | 0 | - | - |
| Other, Net | -28 | -11 | -5 |
| Income Before Tax | 1222 | 677 | 2,016.00 |
| Income After Tax | 765 | 98 | 1,125.00 |
| Minority Interest | 0 | - | - |
| Equity In Affiliates | 0 | - | - |
| Net Income Before Extra. Items | 765 | 98 | 1,125.00 |
| Accounting Change | 0 | - | - |
| Discontinued Operations | 0 | - | - |
| Extraordinary Item | 0 | - | - |
| Net Income | 765 | 98 | 1,125.00 |
| Preferred Dividends | 0 | - | - |
| Income Available to Common Excl. Extra Items | 765 | 98 | 1,125.00 |
| Income Available to Common Incl. Extra Items | 765 | 98 | 1,125.00 |
| Basic Weighted Average Shares | 0 | - | - |
| Basic EPS Excluding Extraordinary Items | 0 | - | - |
| Basic EPS Including Extraordinary Items | 0 | - | - |
| Dilution Adjustment | 0 | - | - |
| Diluted Weighted Average Shares | 941 | 312 | 312 |
| Diluted EPS Excluding Extraordinary Items | 2.44 | 0.31 | 3.61 |
| Diluted EPS Including Extraordinary Items | 0 | - | - |
| Dividends per Share - Common Stock Primary Issue | 0.33 | 0.44 | 0.3 |

## Balance Sheet

| In Millions of USD (except for per share items) | Q3 2010 | 2009 | 2008 | 2007 |
|---|---|---|---|---|
| Cash & Equivalents | 1,549.00 | 2,292.00 | 1,539.00 | 1,569.00 |
| Short Term Investments | - | - | - | - |
| Cash and Short Term Investments | 1,549.00 | 2,292.00 | 1,539.00 | 1,569.00 |
| Accounts Receivable - Trade, Net | 3,937.00 | 3,391.00 | 4,359.00 | 3,942.00 |
| Receivables - Other | - | - | - | - |
| Total Receivables, Net | 3,937.00 | 3,391.00 | 4,359.00 | 3,942.00 |
| Total Inventory | 380 | 367 | 435 | 338 |
| Prepaid Expenses | 300 | 555 | 367 | 244 |
| Other Current Assets, Total | 517 | 511 | 544 | 536 |
| Total Current Assets | 6,683.00 | 7,116.00 | 7,244.00 | 6,629.00 |
| Property/Plant/Equipment, Total - Gross | 30,675.00 | 29,260.00 | 29,305.00 | 27,090.00 |
| Accumulated Depreciation, Total | -16,672.00 | -15,843.00 | -15,827.00 | -14,454.00 |
| Goodwill, Net | 2,229.00 | 2,229.00 | 3,165.00 | 3,497.00 |
| Intangibles, Net | 1,128.00 | 118 | 189 | 767 |
| Long Term Investments | - | - | - | - |
| Other Long Term Assets, Total | 833 | 1,364.00 | 1,557.00 | 471 |
| Total Assets | 24,876.00 | 24,244.00 | 25,633.00 | 24,000.00 |
| Accounts Payable | 1,489.00 | 1,372.00 | 2,195.00 | 2,016.00 |
| Accrued Expenses | 2,600.00 | 2,499.00 | 2,671.00 | 2,773.00 |
| Notes Payable/Short Term Debt | 0 | 0 | 0 | 0 |
| Current Port. of LT Debt/Capital Leases | 283 | 653 | 502 | 639 |
| Other Current liabilities, Total | - | - | - | - |
| Total Current Liabilities | 4,372.00 | 4,524.00 | 5,368.00 | 5,428.00 |
| Long Term Debt | 1,668.00 | 1,930.00 | 1,506.00 | 2,007.00 |
| Capital Lease Obligations | - | - | - | - |
| Total Long Term Debt | 1,668.00 | 1,930.00 | 1,506.00 | 2,007.00 |
| Total Debt | 1,951.00 | 2,583.00 | 2,008.00 | 2,646.00 |
| Deferred Income Tax | 1,384.00 | 1,071.00 | 1,264.00 | 897 |
| Minority Interest | - | - | - | - |
| Other Liabilities, Total | 3,072.00 | 3,093.00 | 2,969.00 | 3,012.00 |
| Total Liabilities | 10,496.00 | 10,618.00 | 11,107.00 | 11,344.00 |
| Common Stock, Total | 31 | 31 | 31 | 31 |
| Additional Paid-In Capital | 2,168.00 | 2,053.00 | 1,922.00 | 1,689.00 |
| Retained Earnings (Accumulated Deficit) | 13,546.00 | 12,919.00 | 13,002.00 | 11,970.00 |
| Treasury Stock - Common | -3 | -4 | -4 | -4 |
| Other Equity, Total | -1,362.00 | -1,373.00 | -425 | -1,030.00 |
| Total Equity | 14,380.00 | 13,626.00 | 14,526.00 | 12,656.00 |
| Total Liabilities & Shareholders' Equity | 24,876.00 | 24,244.00 | 25,633.00 | 24,000.00 |
| Total Common Shares Outstanding | 313 | 312 | 311 | 308 |

## Statement of Cash Flows

| In Millions of USD (except for per share items) | Thru Q310 | 2009 | 2008 | 2007 |
|---|---|---|---|---|
| Net Income/Starting Line | 765 | 98 | 1,125.00 | 2,016.00 |
| Depreciation/Depletion | 1,470.00 | 1,975.00 | 1,946.00 | 1,742.00 |
| Amortization | - | - | - | - |
| Deferred Taxes | 183 | 299 | 124 | 37 |
| Non-Cash Items | -391 | 1,356.00 | 1,037.00 | 173 |
| Changes in Working Capital | -119 | -975 | -767 | -411 |
| Cash from Operating Activities | 1,908.00 | 2,753.00 | 3,465.00 | 3,557.00 |
| Capital Expenditures | -1,981.00 | -2,459.00 | -2,947.00 | -2,882.00 |
| Other Investing Cash Flow Items, Total | 31 | 76 | 50 | -1,242.00 |
| Cash from Investing Activities | -1,950.00 | -2,383.00 | -2,897.00 | -4,124.00 |
| Financing Cash Flow Items | -7 | -3 | 38 | 40 |
| Total Cash Dividends Paid | -103 | -137 | -124 | -110 |
| Issuance (Retirement) of Stock, Net | 36 | 41 | 108 | 115 |
| Issuance (Retirement) of Debt, Net | -632 | 499 | -639 | 148 |
| Cash from Financing Activities | -706 | 400 | -617 | 193 |
| Foreign Exchange Effects | 5 | -17 | 19 | 6 |
| Net Change in Cash | -743 | 753 | -30 | -368 |
| Cash Interest Paid, Supplemental | 101 | 61 | 105 | 136 |
| Cash Taxes Paid, Supplemental | -94 | 509 | 816 | 1,064.00 |