

Seminar 69

Freight Market Outlook

Don't Shoot the Messenger

August 24, 2023

Tim Denoyer, VP, Senior Analyst

- Industry Analyst, Transportation Equipment
 - Freight forecast, DAT & Cass partnerships
 - Used truck price forecasts
 - Carrier databases
 - Projects
- 6 years with ACT, following 15 years covering US industrial economy in the investment community, mostly as an ACT client
- Kids soccer coach



Agenda

- Overview – The Bottoming Stage of the Freight Cycle
 - Where we are in the cycle
- Trucking Supply / Demand Balance
 - Freight volume outlook
 - Labor & equipment factors
- Rate cycle outlook
 - Bouncing along the bottom
 - Where we're heading: *lower for longer, but tighter market in 2024*



Forecast Overview

	2021	2022	2023F	2024F	2025F
Economy (Y/Y % Δ)					
GDP	5.9%	2.1	2.3	2.2	2.2
ACT Freight Comp	11.1%	2.0	-0.5	2.3	3.4
Rates (Y/Y % Δ, net fuel)					
DAT TL Spot	30%	-12%	-18%	21%	8%
DAT TL Contract	21%	6%	-12%	2%	10%
Equipment Production (000s)					
NA CI 8 Build	265	315	337	285	320
US Tractor Sales	169	199	215	172	192
NA CL 5-7 Build	235	241	260	242	262
US Trailers	267	308	313	281	304
US Dry Van	165	188	197	173	190

**US Tractors: 36%
of NA Classes 5-8
volume, ~150% of
the volatility**



Trucking Overview: Bouncing Along the Bottom

Demand:
down, then up

- Late innings of substitution back to services & destock
- Goods demand fundamentals improving
- Restock likely in 2024

Supply:
for-hire down,
private up

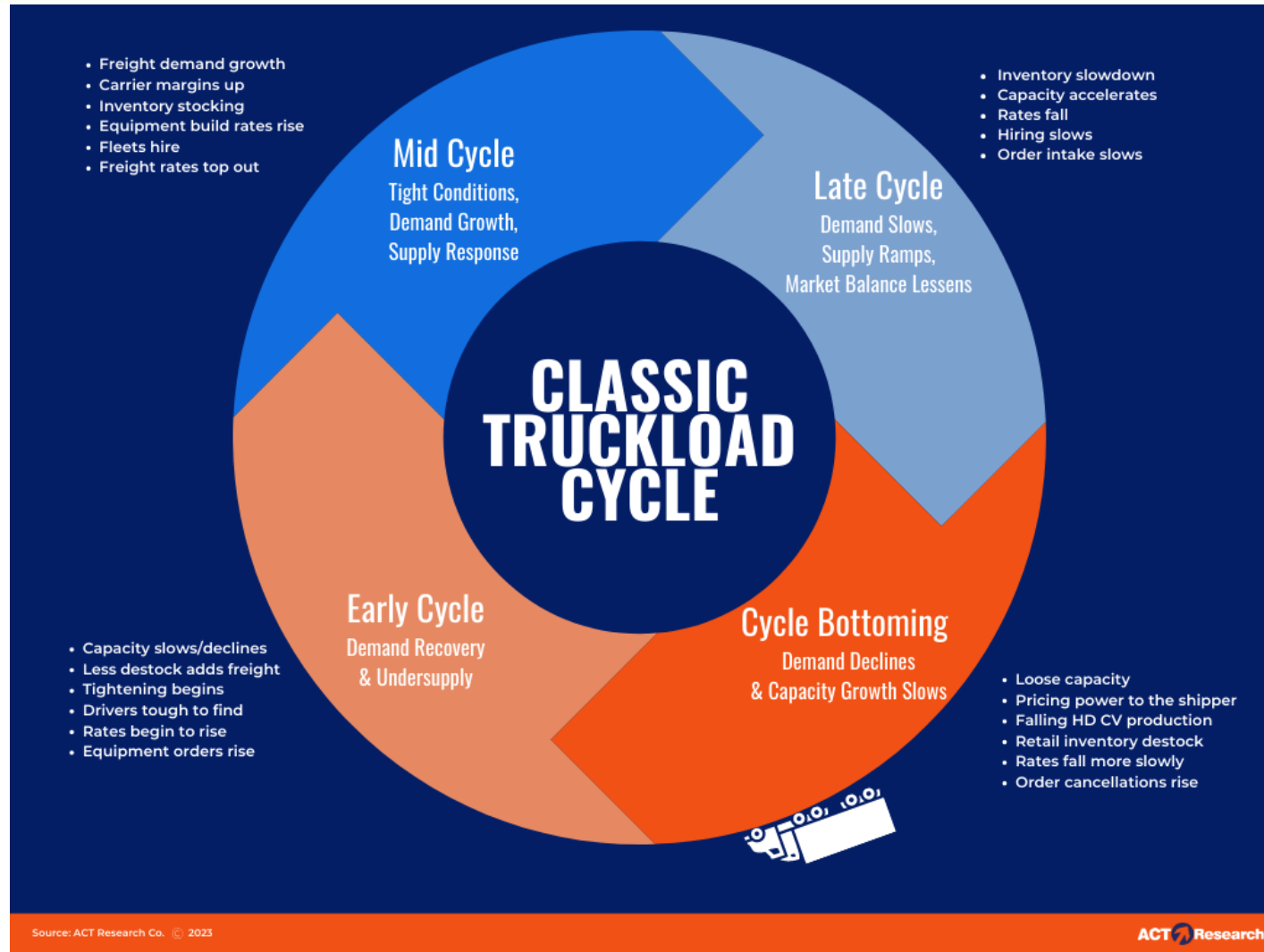
- Class 8 tractor fleet growing briskly
- Layoffs and revocations show for-hire market contracting
- LTL market unique, but tightened in a weekend

Rates: still finding
bottom

- Demand recovery on the come, capacity starting to react
- Spot rates adrift for now, higher in Q4 and 2024



Where are we in the Cycle?



- Oversupply, bottoming phase
- Heading to early cycle when conditions in place

Boom to Bust

The Economist

Menu

Weekly edition

The world in brief

Search

Business | Logistic nightmares

America's logistics boom has turned to bust

A pandemic-era frenzy of hiring and investment has gone into reverse

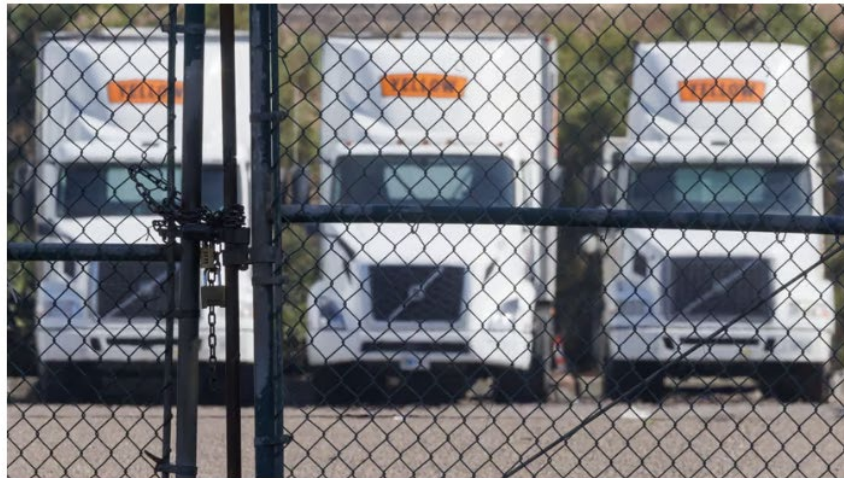


IMAGE: REUTERS

Aug 10th 2023

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The Economist

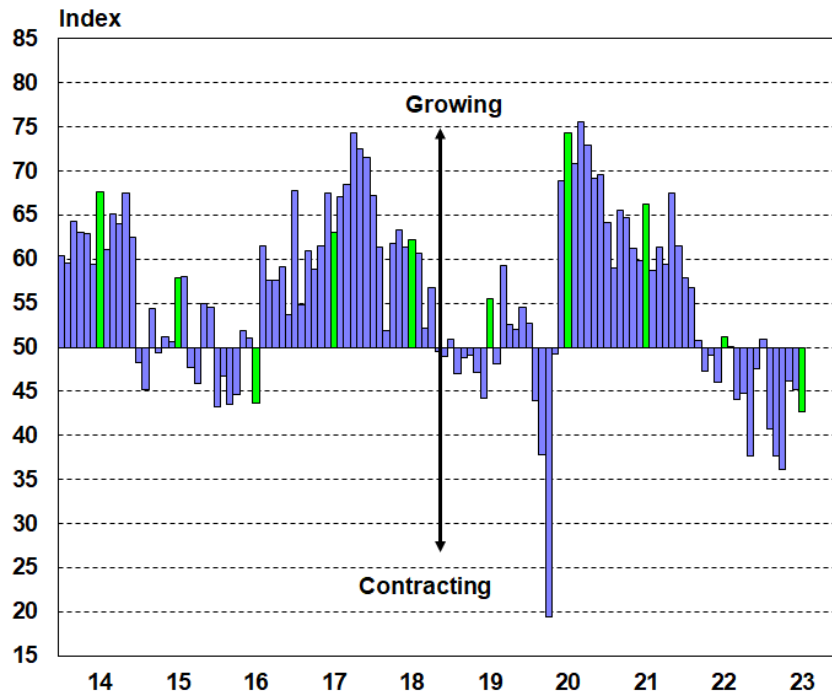
reach them. Revenues in the logistics industry have now clocked up three consecutive quarter-on-quarter declines (see chart). The Cass Freight Index, a measure of rail and truck activity, is down by 5% over the past year. The volume of goods flowing through American ports in July was 14% lower than in the same month last year, according to Descartes, a supply-chain-technology company.

As demand has slumped, so, too, have prices. The cost of “dry van” shipping—the most common way to transport non-perishable goods on the road—is 21% lower than in early 2022, according to DAT Freight & Analytics, a logistics-data provider. That, in turn, is squeezing margins and putting less competitive firms out of business. Some 20,000 truck operators, nearly 3% of the national total, have ceased activity since mid-2022, says ACT Research, another data provider.

Those that have survived are shedding staff. American parcel-delivery firms have jettisoned 38,700 workers since October last year when employment in the sector peaked, based on data from the Bureau of Labour Statistics. Warehouse operators have cut 60,800. More retrenchments are likely to come, given the frenzied hiring of the past few years. Lay-offs in the industry have thus far fallen short of what one might expect given the stagnation in consumer spending, argues Aaron Terrazas, chief economist of Glassdoor, an employment portal. Having long suffered from labour shortages, many firms have been reluctant to lay off workers, reckons Tim Denoyer of ACT Research.

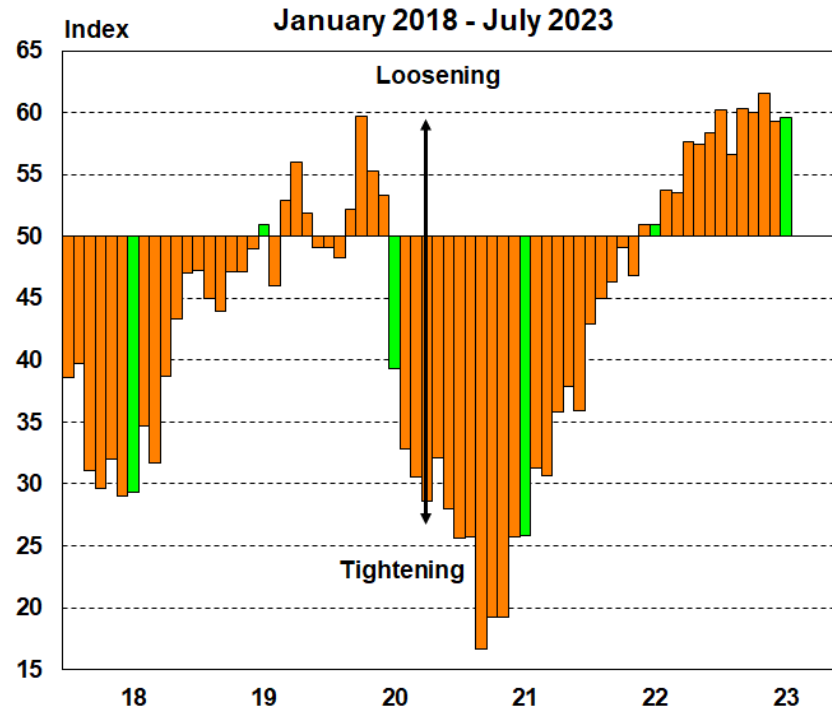
Demand Down, Supply Up

ACT For-Hire Trucking Index: Volumes
(Seasonally Adjusted)
January 2014 - July 2023



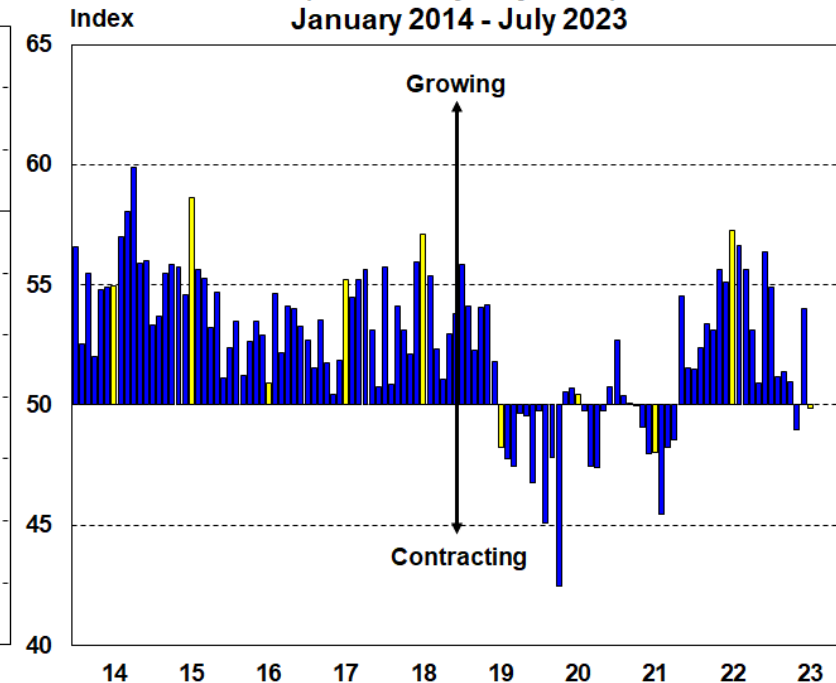
Source: ACT Research Co. © 2023

ACT For-Hire Trucking Index: Driver
Availability
January 2018 - July 2023



Source: ACT Research Co. © 2023

ACT For-Hire Trucking Index: Fleet
Capacity
(Seasonally Adjusted)
January 2014 - July 2023

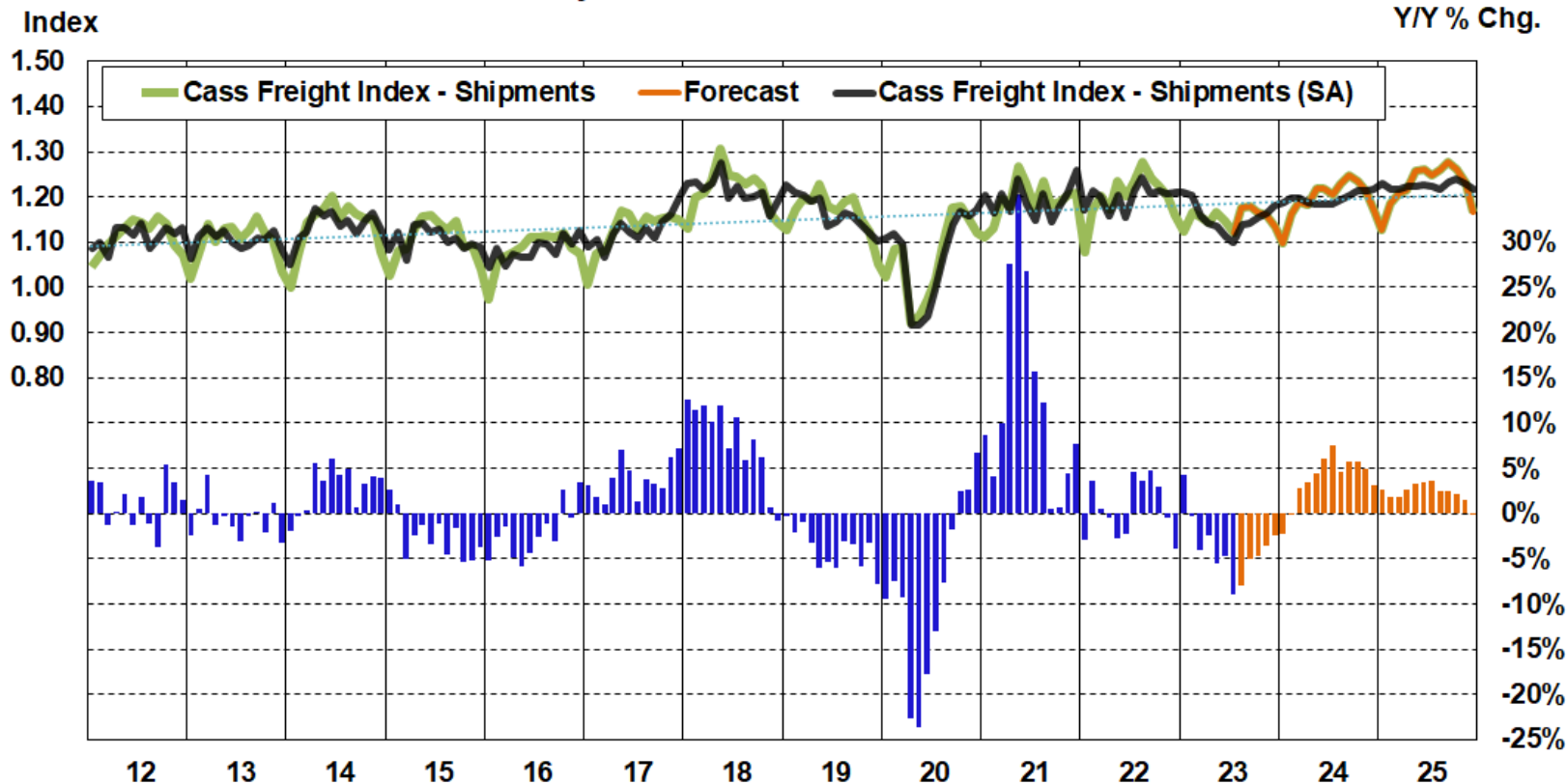


Source: ACT Research Co. © 2023

US Freight Volume Outlook: Down, Then Up

Cass Freight Index® - Shipments

January 2012 - December 2025 Forecast



Source: Cass Information Systems, Inc., ACT Research Co. © 2023

Trucking Demand Outlook

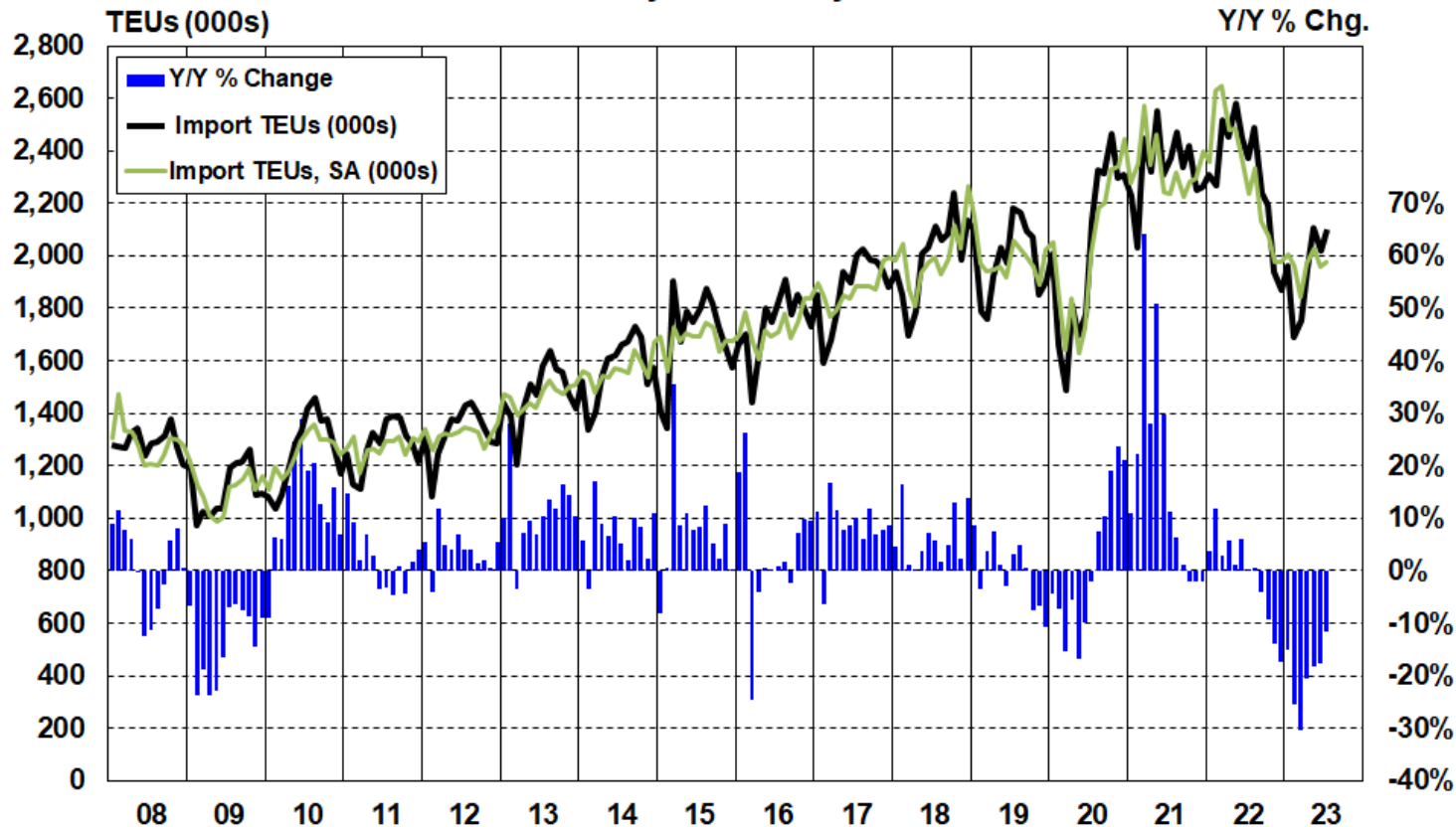
Freight recession in 22/23 returns to growth in 24/25, based on:

- Inventory cycle
- Consumer income growth supports retail rebound
- Industrial recovery driven by infrastructure, semiconductors, decarb, near-shoring
- Produce market recovery

Container Imports Show Big Destock

N.A. Ports: Inbound Loaded Containers

January 2008 - July 2023



Note: Port of Vancouver added in 2013 and Lazaro Cardenas added in 2015. Y/Y changes are adjusted to normalize.

Source: ACT Research Co. © 2023

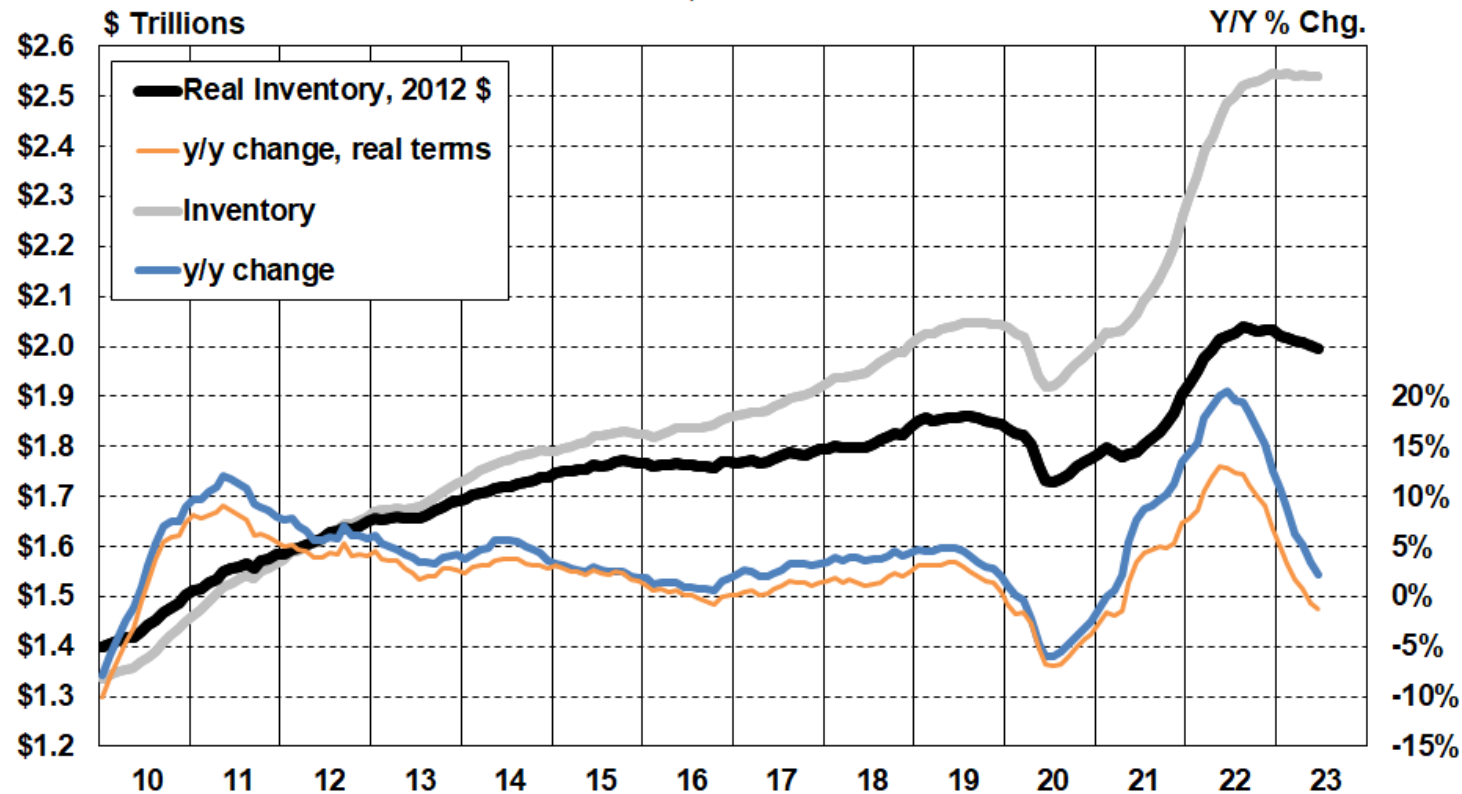
**Container imports -21%
y/y 1H'23, -12% in July**

Larger than 2009 declines

**Imports will recover, but
near-shoring starting to
gain ground**

Inventory Restock to Restart by Early '24

Inventories: Total Business
January 2010 - June 2023
Billions of Dollars, End of Period - SAAR



Source: Census Bureau, ACT Research Co. © 2023

After record cycle, destock well underway

4% annualized decline in 1H, real terms, inventory down 1.2% y/y in June

Freight will start to recover as destock starts to slow

Restocks inevitably follow destocks

Walmart Data Support Ending of Destock

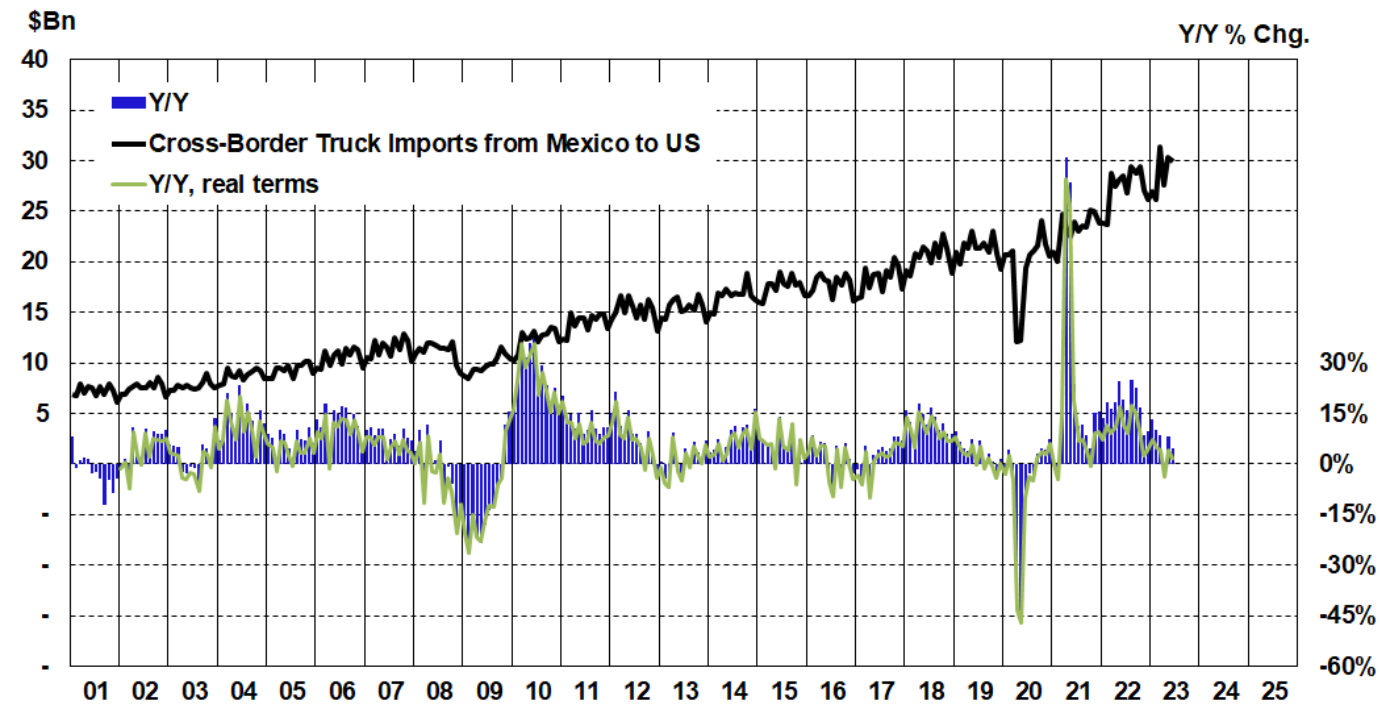


July quarter-end real sales accelerated and inventory turns improved

Source: Dr. Jason Miller, MSU

Evidence of Near-Shoring

Cross-Border Truck Imports from Mexico to US



Real truck imports +11% in 2022 vs exports +9%

Imports still +2.8% y/y in 1H'23 vs exports +3.7%



1998
Built Barbie plant in Monterrey, MX



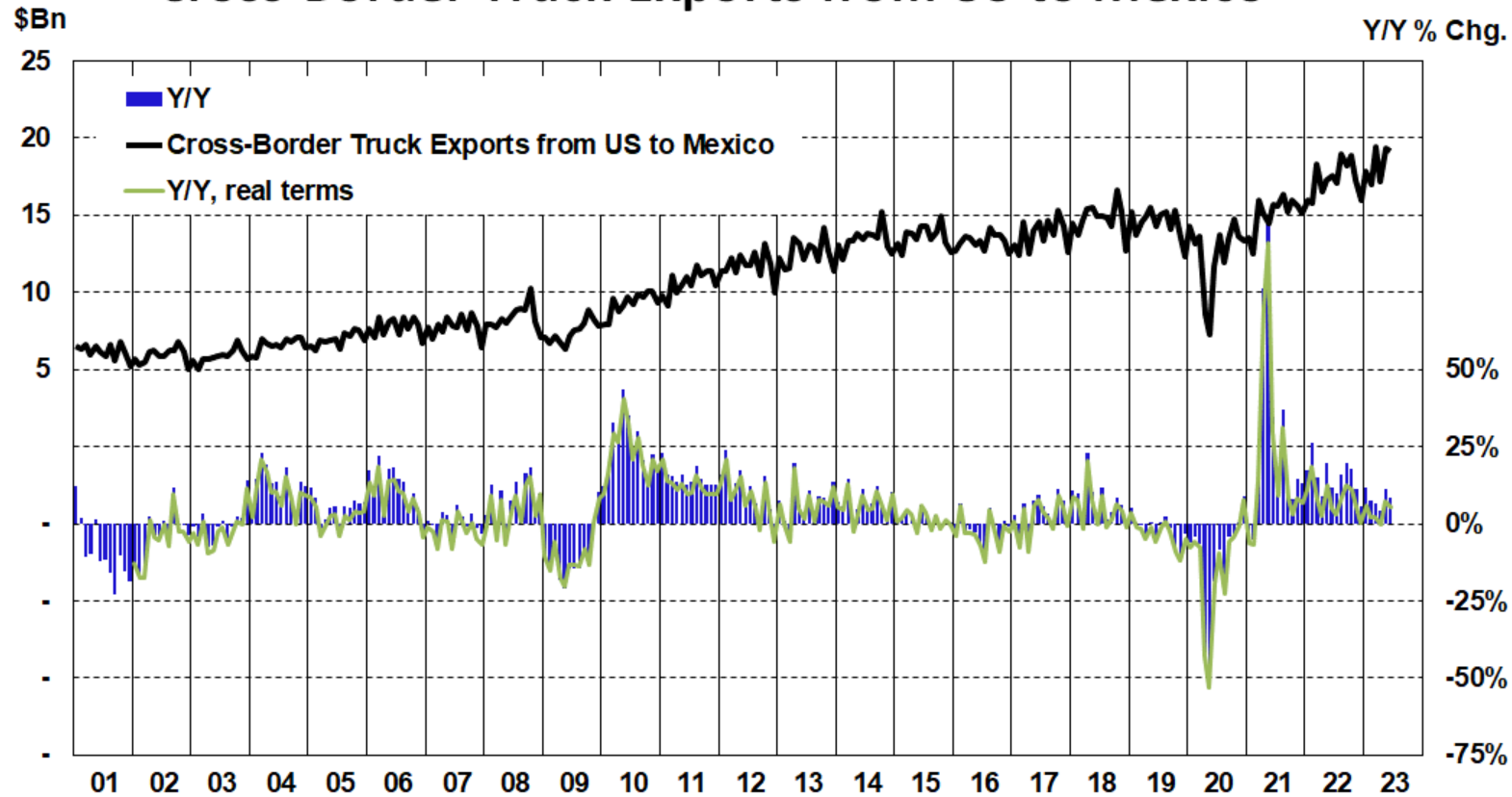
2018
Announced closure of plant as cost cutting measure



2022
Monterrey, MX now Mattel's largest plant

A Two-Way Highway

Cross-Border Truck Exports from US to Mexico

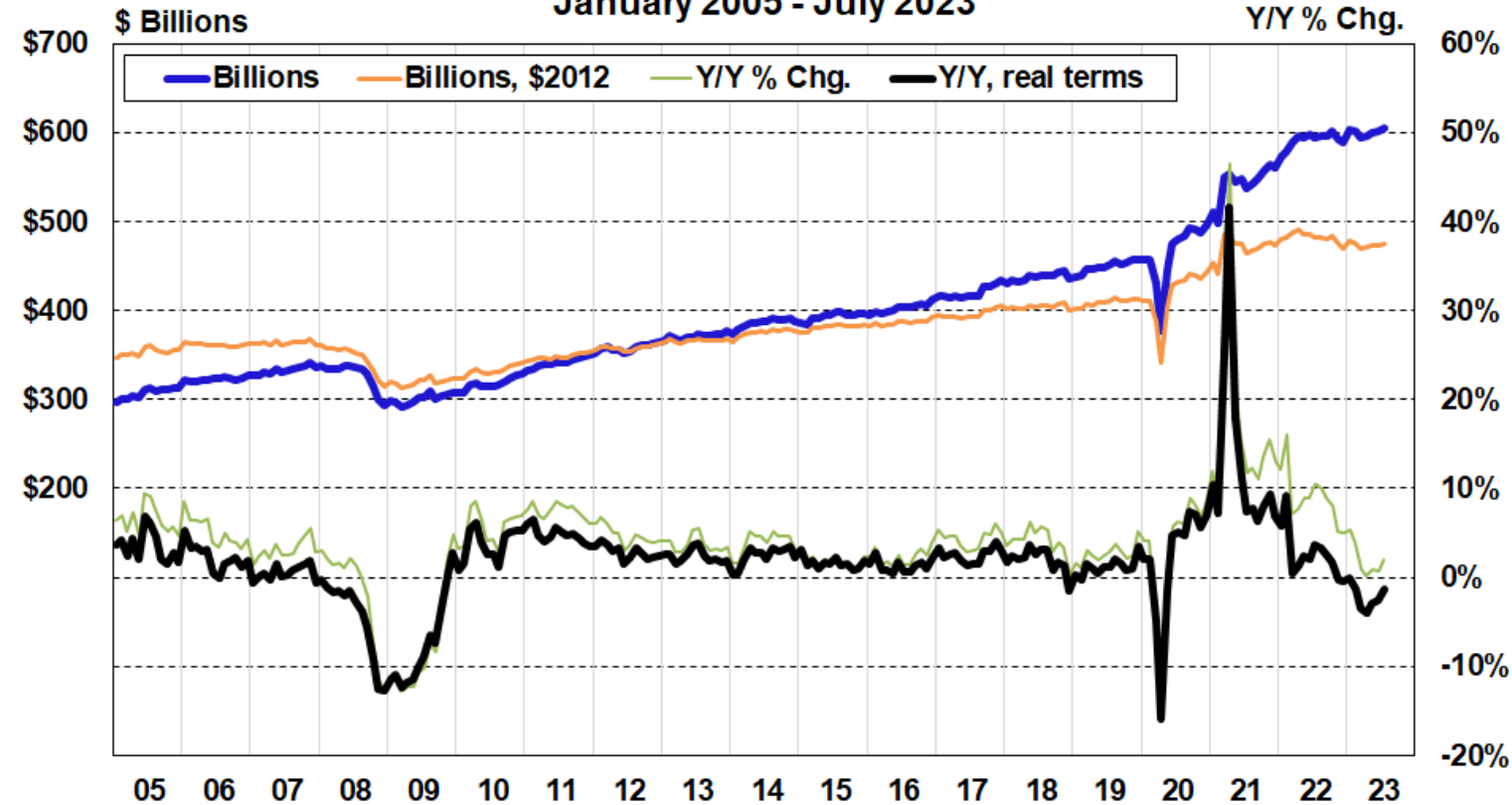


Source: Bureau of Transportation Statistics, ACT Research Co. © 2023

More evidence of near-shoring
Trade balance steady

Consumer Fundamentals Improving

US Retail Sales
Billions of Dollars - SAAR
January 2005 - July 2023



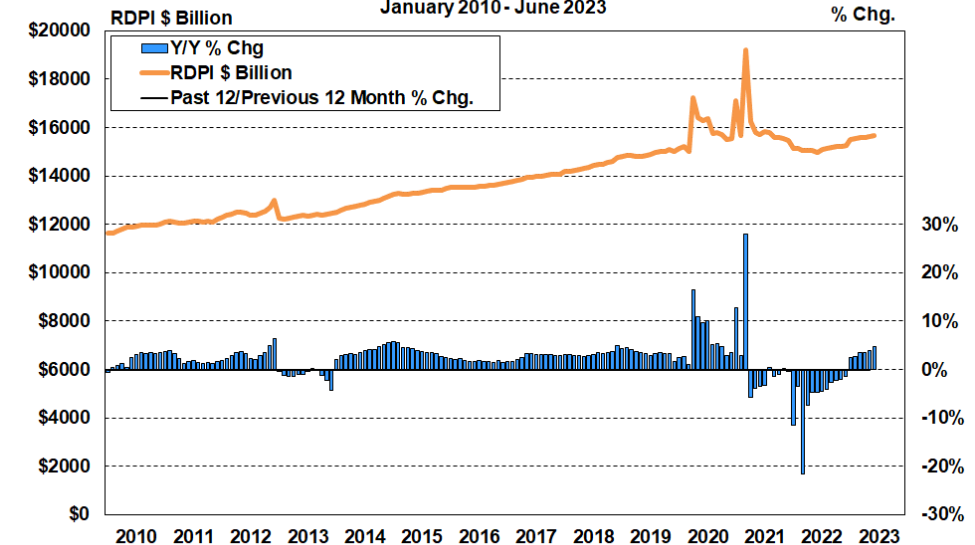
Source: US Census Bureau, ACT Research Co. © 2023

Real retail sales bottoming

RDPI +4.8% y/y in June, aided by disinflation

Declines in consumer spending are rare and brief

Real Disposable Personal Income
Percent Change Y/Y
January 2010 - June 2023

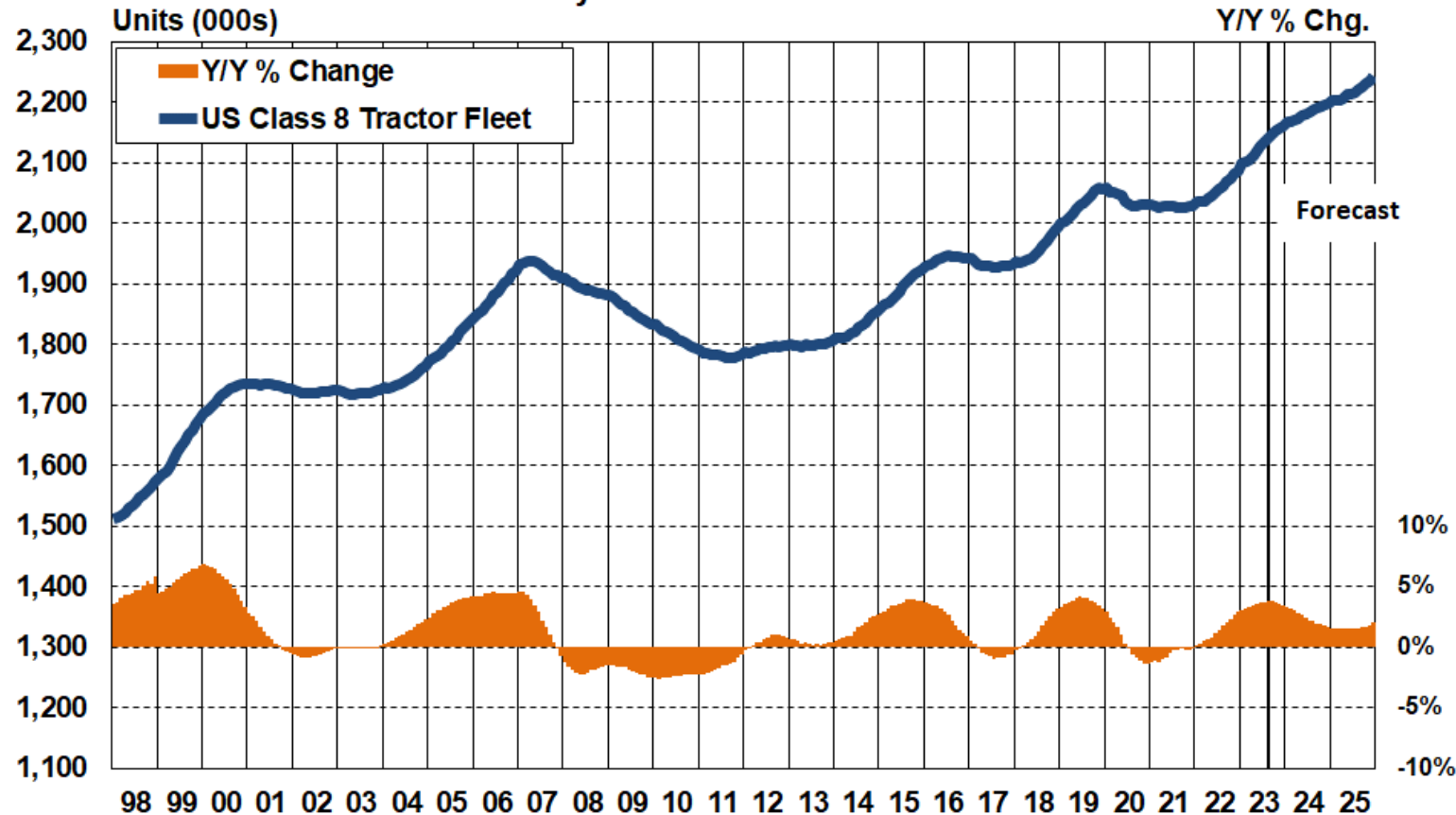


Source: BLS, ACT Research Co. © 2023

Capacity Additions Persist

U.S. Class 8 Useful Tractor Population

January 1998 - December 2025

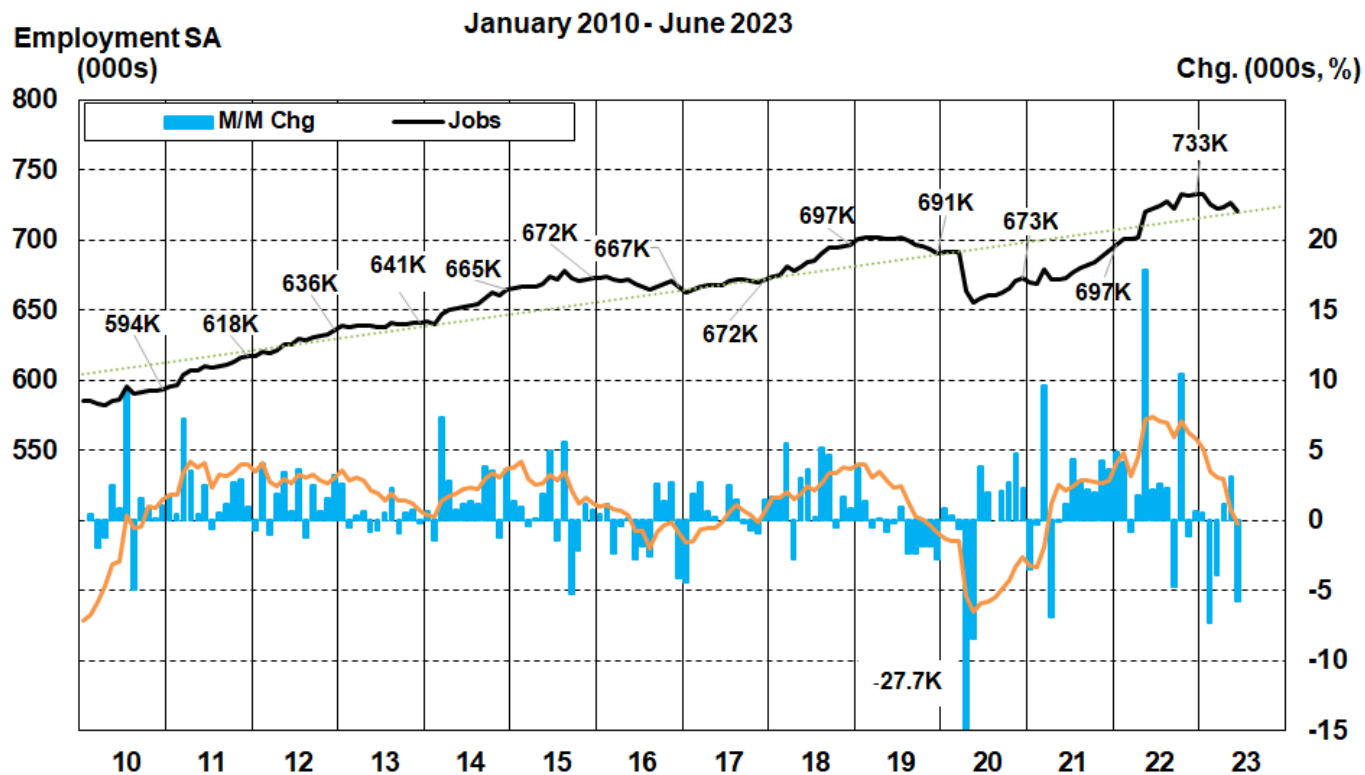


Source: ACT Research Co. © 2023

- Not seeing truckload price signals
- Strong new equipment demand lengthens the freight cycle downturn
- Elevated retirements offset some of this growth
- The first rule of holes is to stop digging

Supply Tightening Slowly, Then All at Once

Trucking Employment - Long-Distance Drivers*



The Washington Post
Democracy Dies in Darkness

ECONOMY

Truck drivers are leaving boom-and-bust supply chain jobs

Earnings plummet as retailers work through swollen inventory and consumers spend more on in-person experiences



By David J. Lynch

July 31, 2023 at 6:00 a.m. EDT

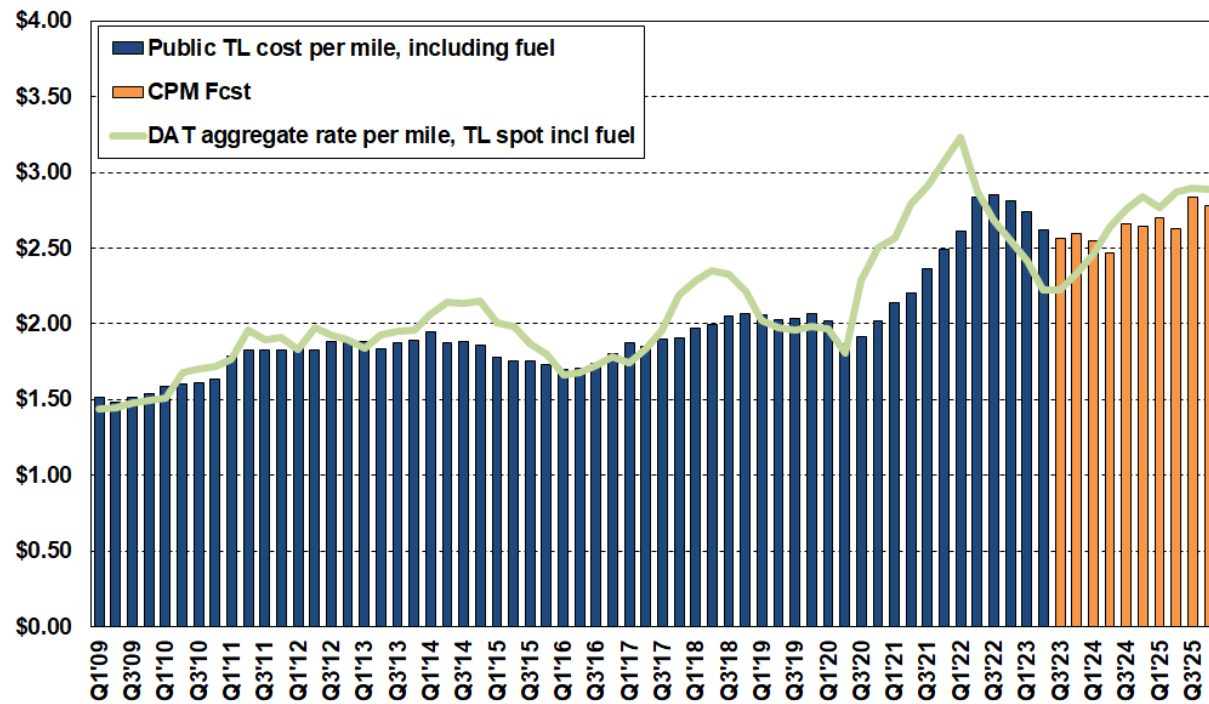
Driver Surplus is Rebalancing

Hiring has slowed since August 2022
2,800-job reduction YTD industry-wide
12k driver jobs* lost 1H'23
Not many union shops left for Yellow workers

Spot Rates Well Below Fleet Costs

Spot Rates Vs Cost Per Mile

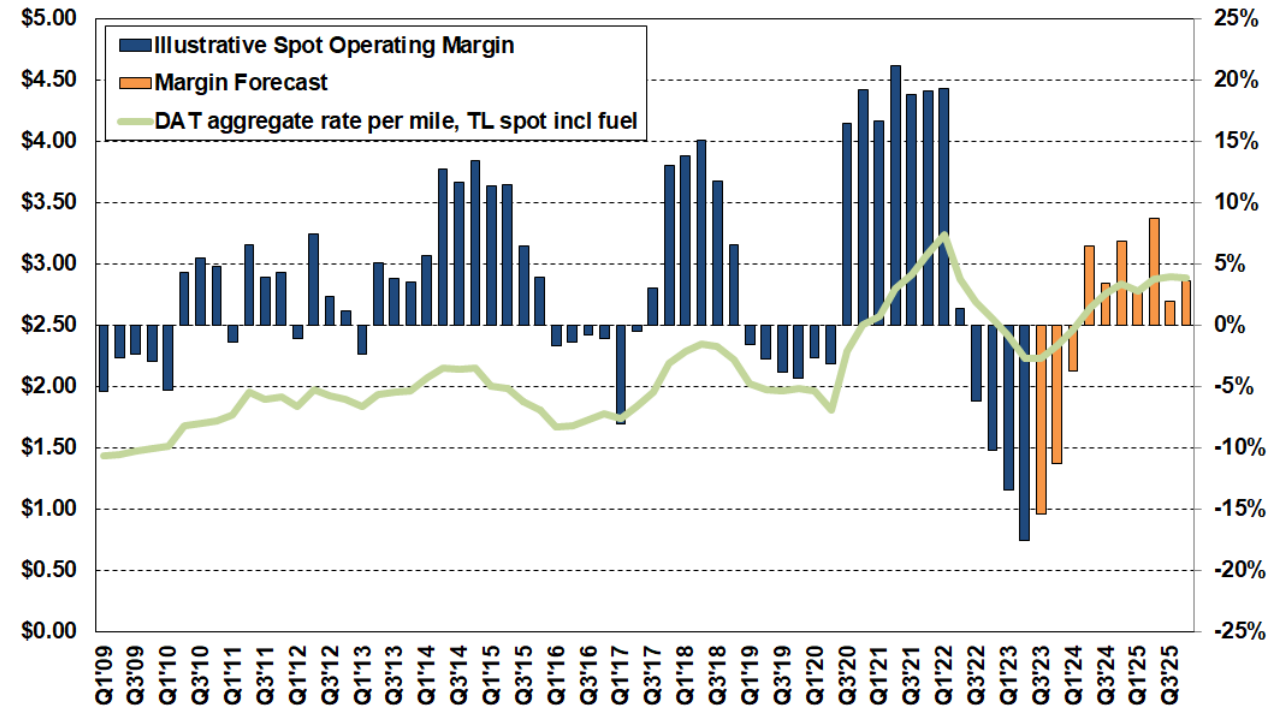
2009 - 2025E



Source: ACT Research Co. © 2023

Illustrative Spot Operating Margin

2009 - 2025E



Illustrative operating margin = aggregate DAT spot rate / all-in publicly traded fleet cost per mile.

Source: ACT Research Co. © 2023

Spot rates now about 15% below fleet costs

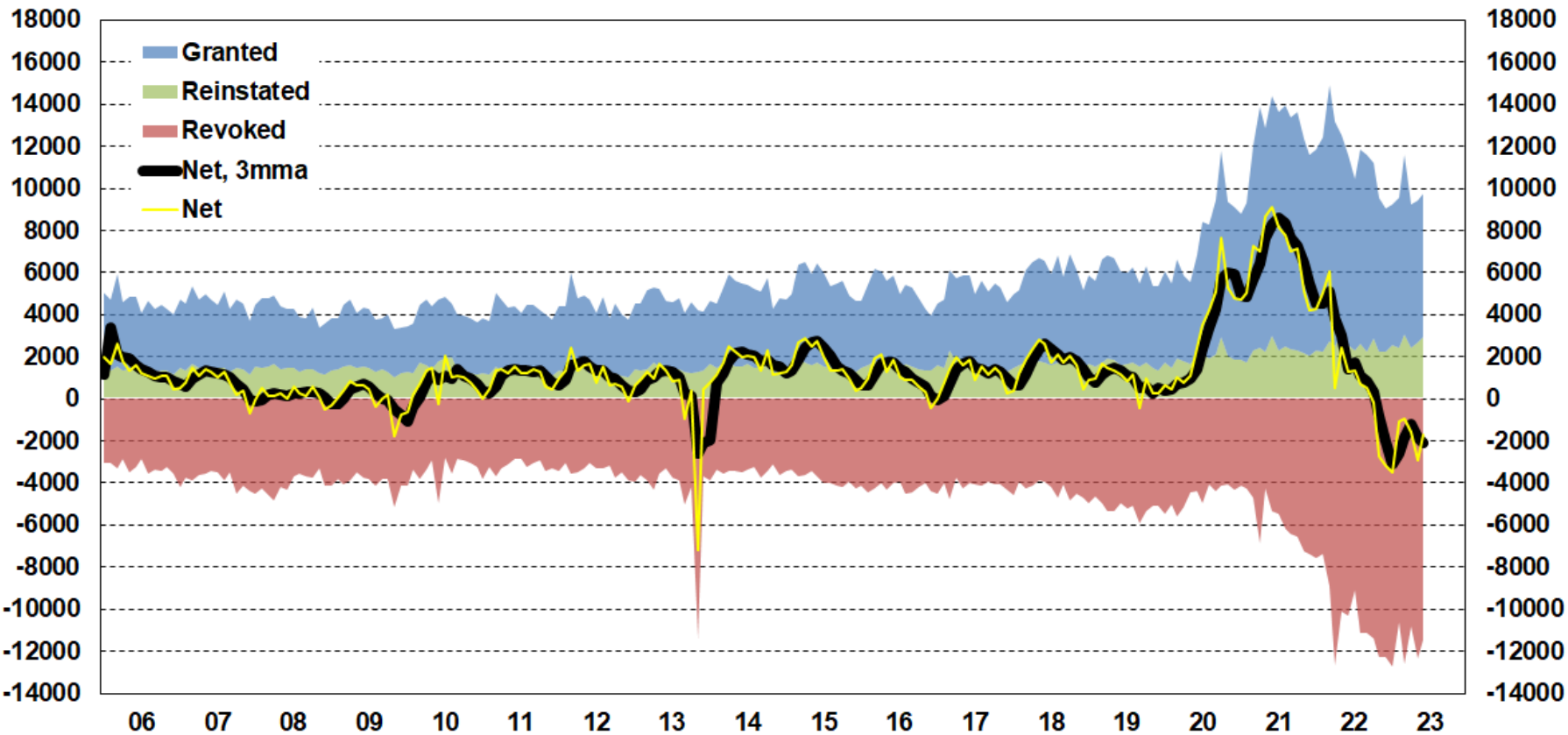
Rates don't stay below costs too long, but it can get worse

It's a Grind

DOT Operating Authorities

January 2006 - June 2023

Interstate Operating Authorities



Source: U.S. Department of Transportation (DOT), ACT Research Co. © 2023

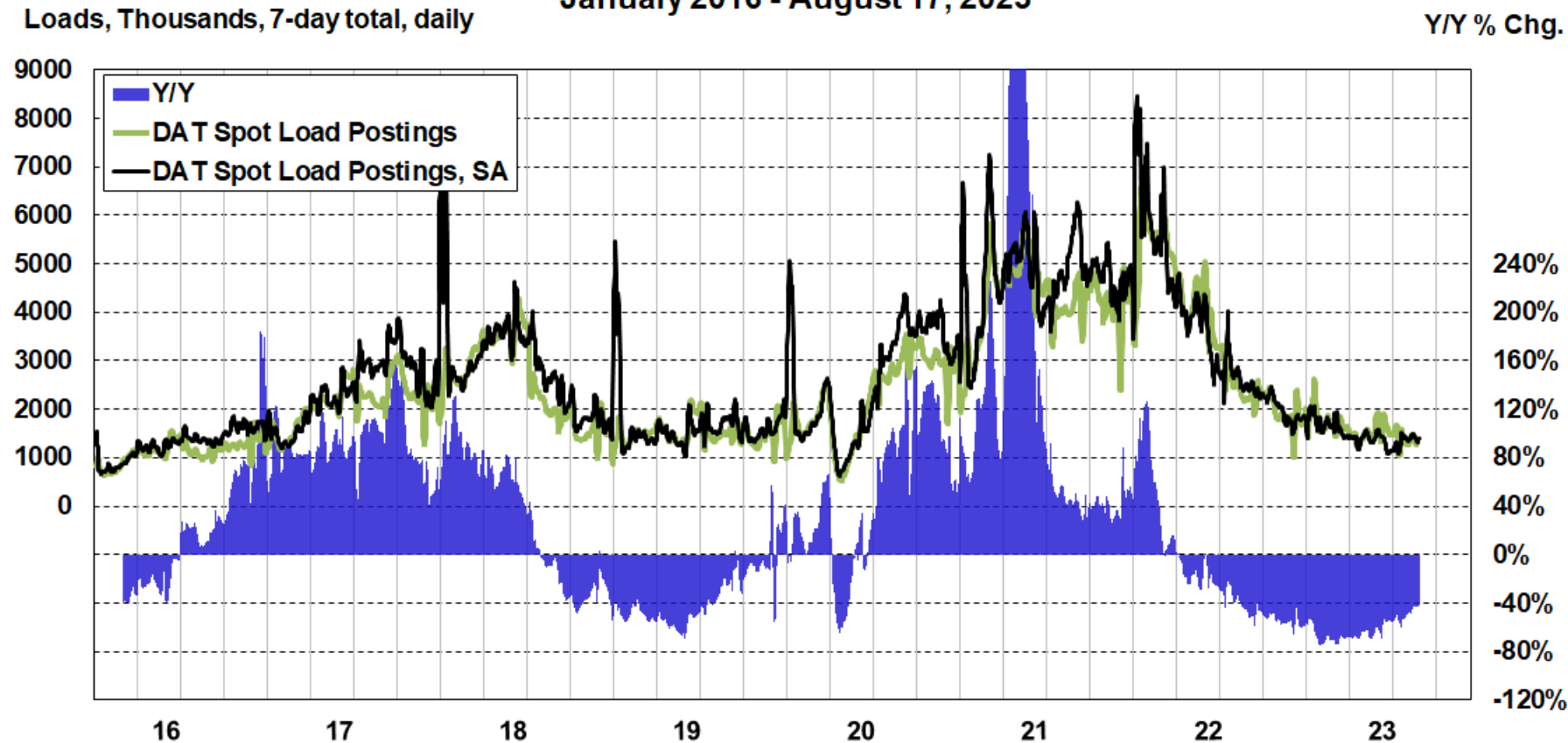
Net revocations of operating authorities at a record rate, tightening capacity, coiling the spring

- ~2k net fleets/month exiting since Oct '22

Few Signs of Life in Spot Load Postings

DAT Postings: LOADS

January 2016 - August 17, 2023



Source: DAT Freight & Analytics, ACT Research Co. © 2023

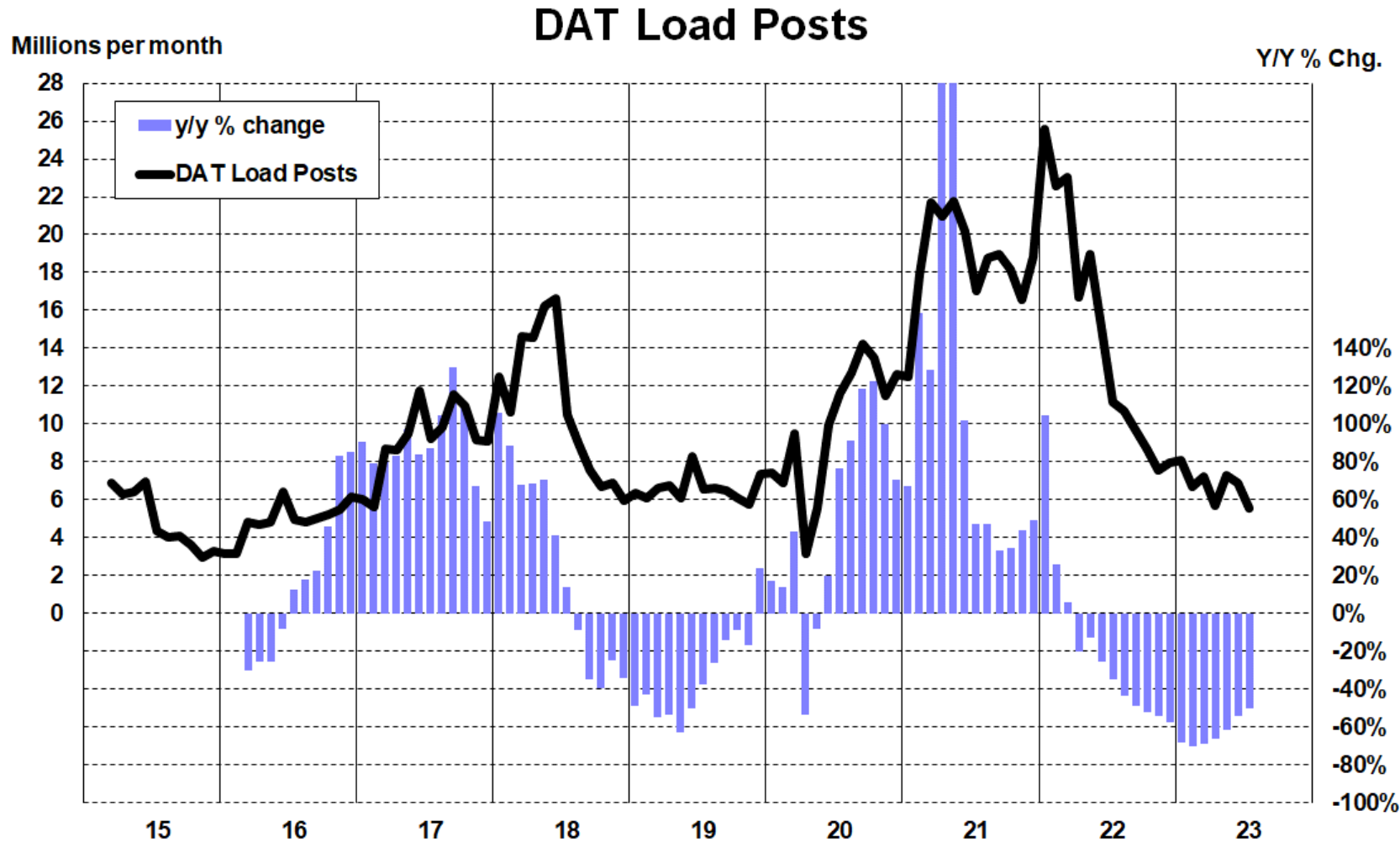
Demand bouncing along at cycle lows

**~1.4 million loads/week, vs
~1.2 million cycle lows (SA)
– small bump from Yellow**

**Seasonality picks up post
Labor Day**

**Tropical Storm Hilary likely
to add to volume, and tie up
capacity, but unlikely a
needle mover**

Spot Truckload Demand at Cyclical Lows



Second derivative improving; cold comfort for this order season

Source: DAT Freight & Analytics, ACT Research Co. © 2023

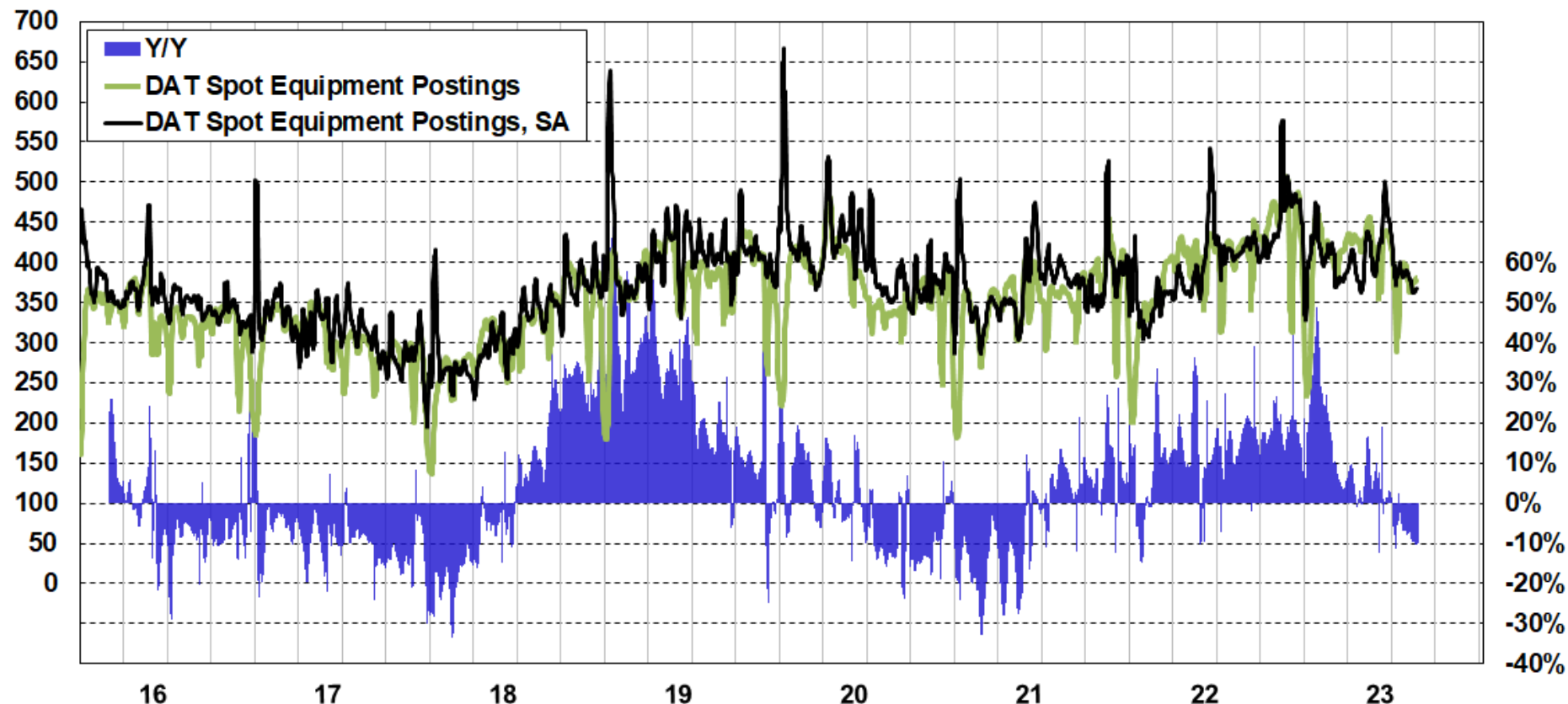
Spot Supply Beginning to Decline

DAT Postings: EQUIPMENT

January 2016 - August 17, 2023

Trucks, Thousands, 7-day total, daily

Y/Y % Chg.



Source: DAT Freight & Analytics, ACT Research Co. © 2023

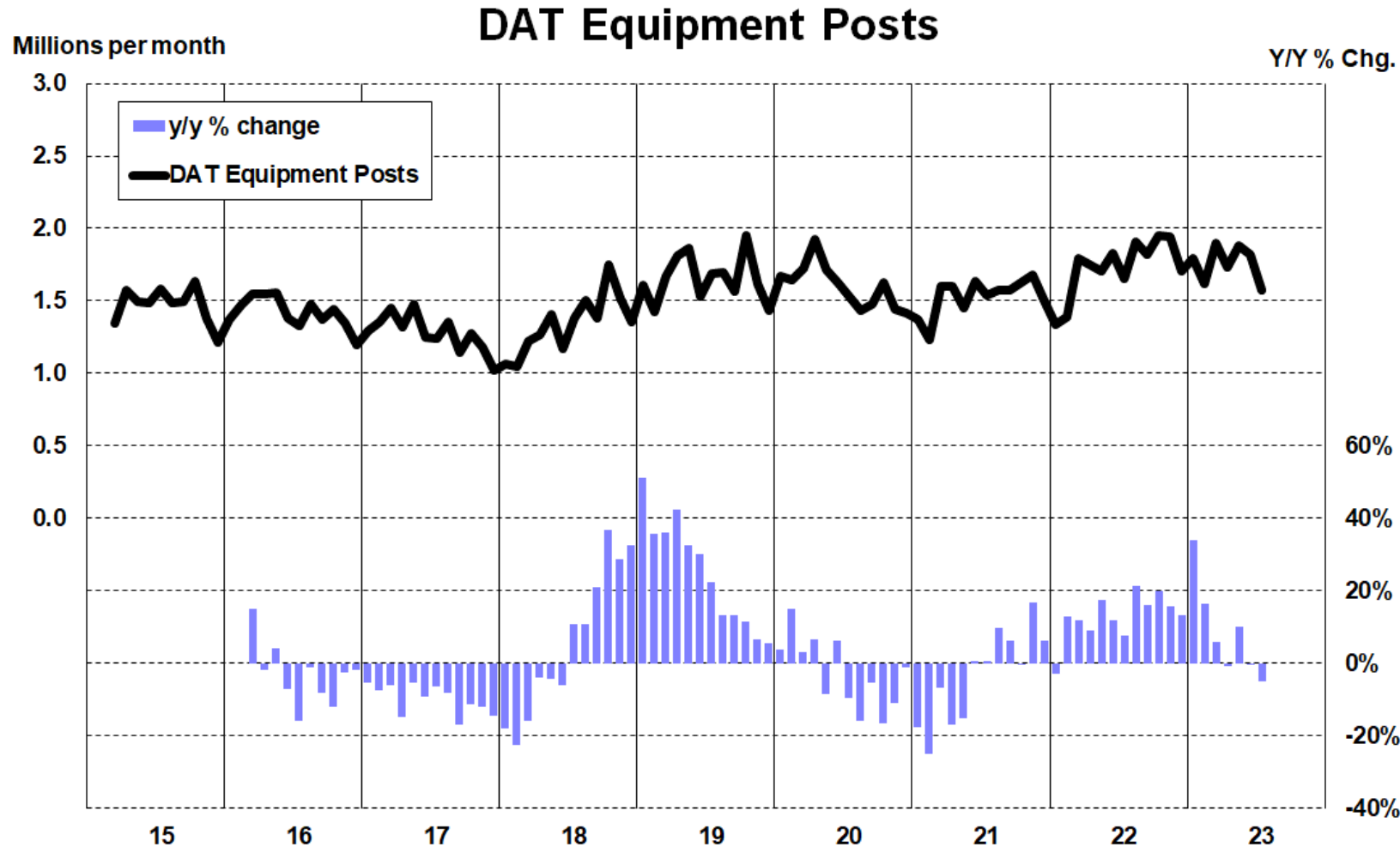
Downtrend interrupted in June as fleets moved into spot

Yellow shutdown 7/31/23

Great gauge of spot market supply now down about 10% y/y:

Spot market starting to tighten, but not enough to move rates yet

Spot Supply Beginning to Decline



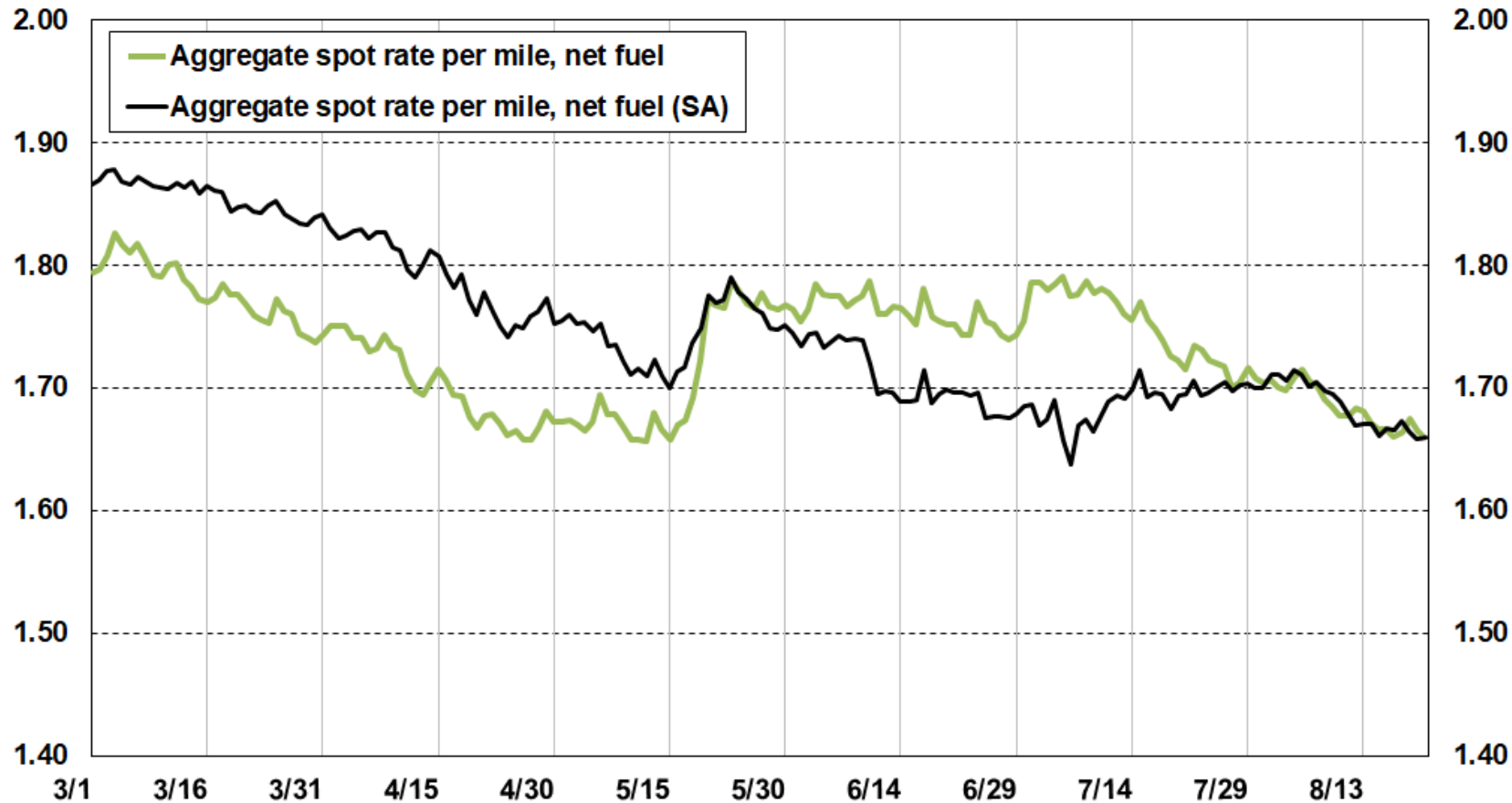
Significant drawdown since Yellow shutdown, but not fully felt due to seasonal softness

Capacity unlikely to tighten too much with build where it is

Source: DAT Freight & Analytics, ACT Research Co. © 2023

Spot Rate Cycle Finding the Bottom

DAT Daily Spot Rates
3/31 - 8/21



Source: DAT Freight & Analytics, ACT Research Co. © 2023

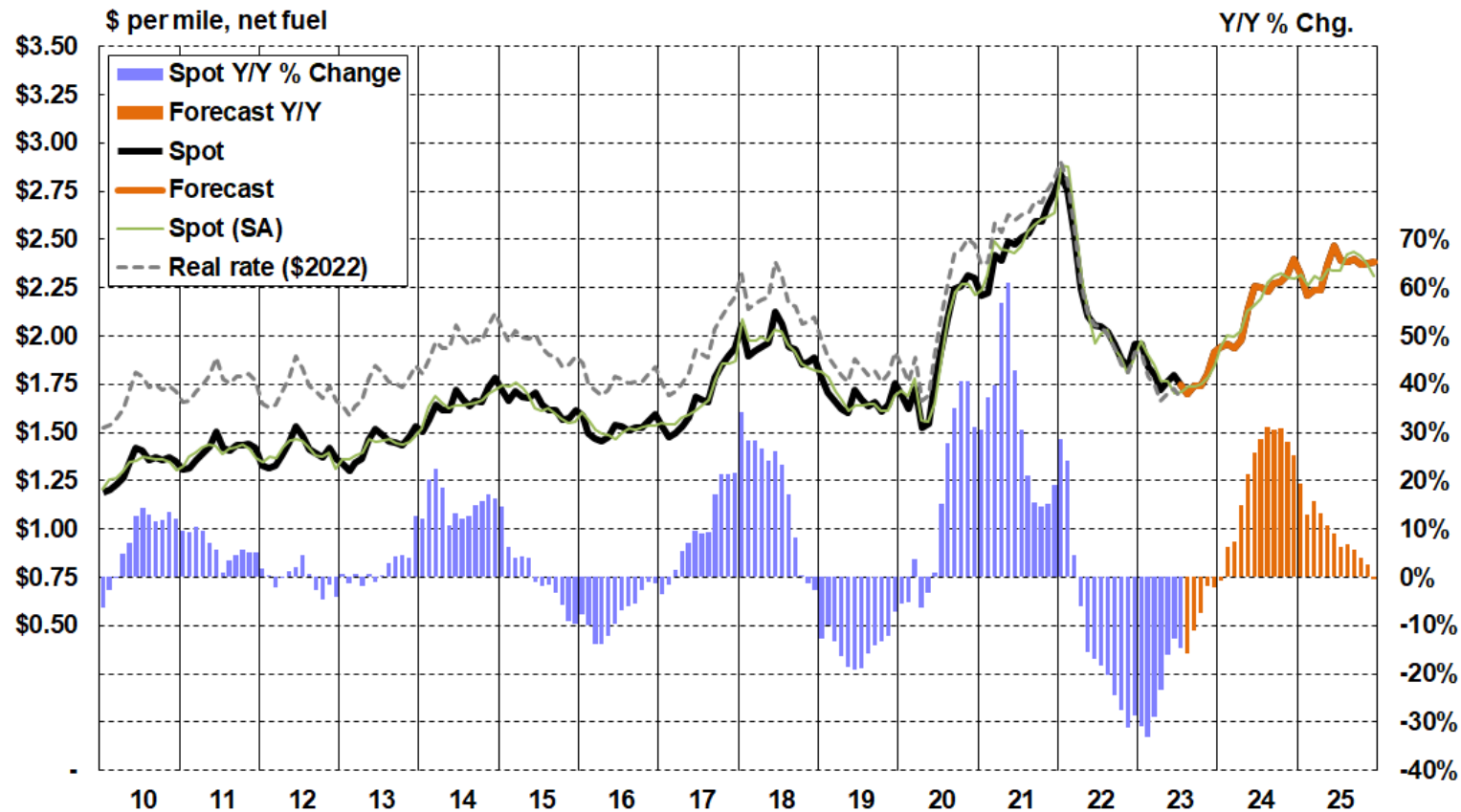
- Nice Roadcheck gains, but didn't hold
- No immediate effects from Yellow or Hilary
- 9¢/mi hit from fuel past six weeks
- Market still searching for a bottom
- August trending down 1¢/mi m/m SA



Spot Rate Cycle Bottoming

DAT Trendlines Spot Rates: Aggregate

January 2010 - December 2025 Forecast



Note: real rate adjusted using core PCEPI.

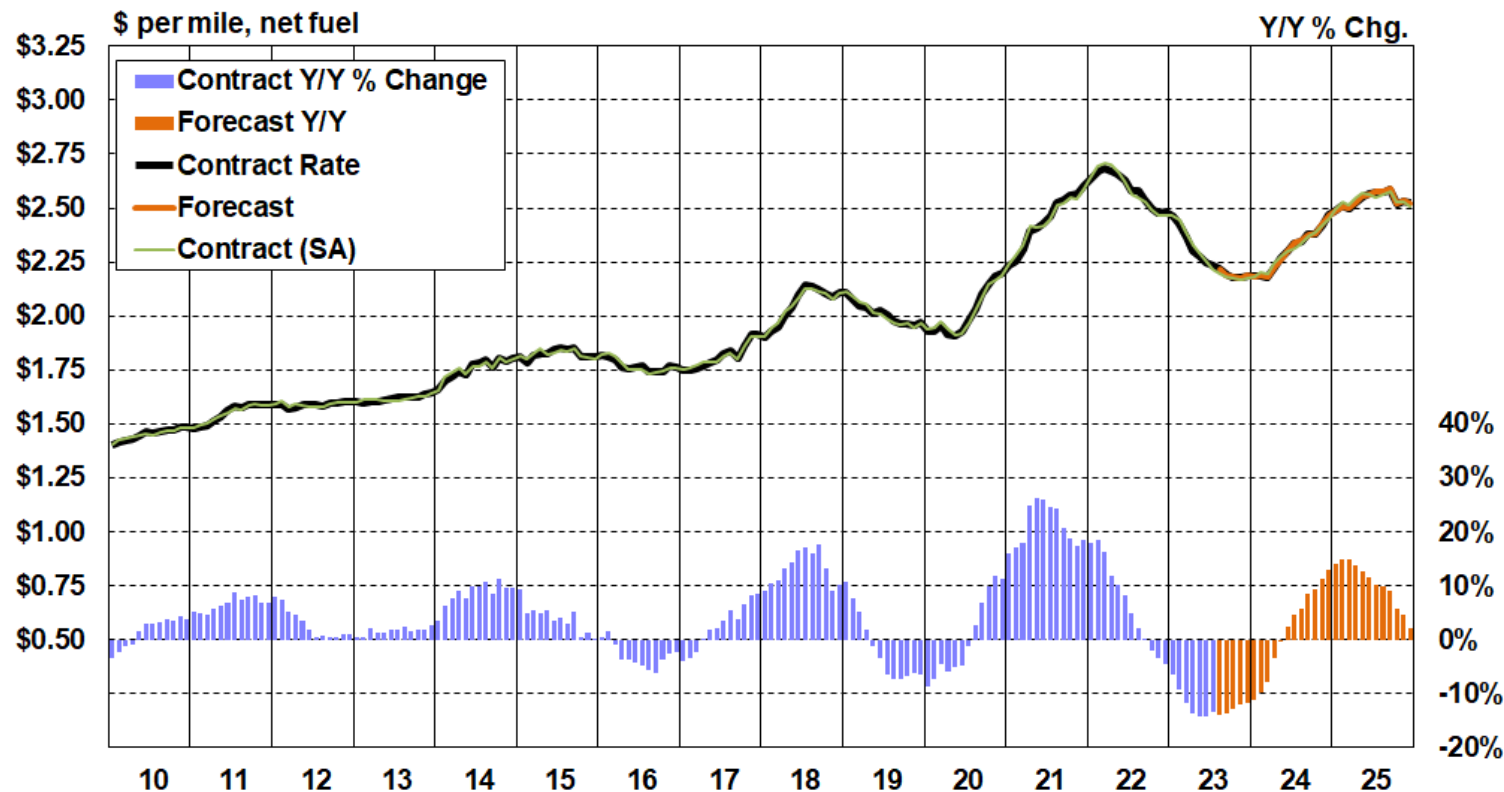
Source: DAT Freight & Analytics, ACT Research Co. © 2023

- A dismal equilibrium
- Focus on labor retention drawing out bottom
- Long-term amplitude to remain elevated on price discovery, demographics, & labor constraints

Contract Rate Declines Into 1H'24

DAT Contract Rates: Aggregate Truckload

January 2010 - December 2025 Forecast



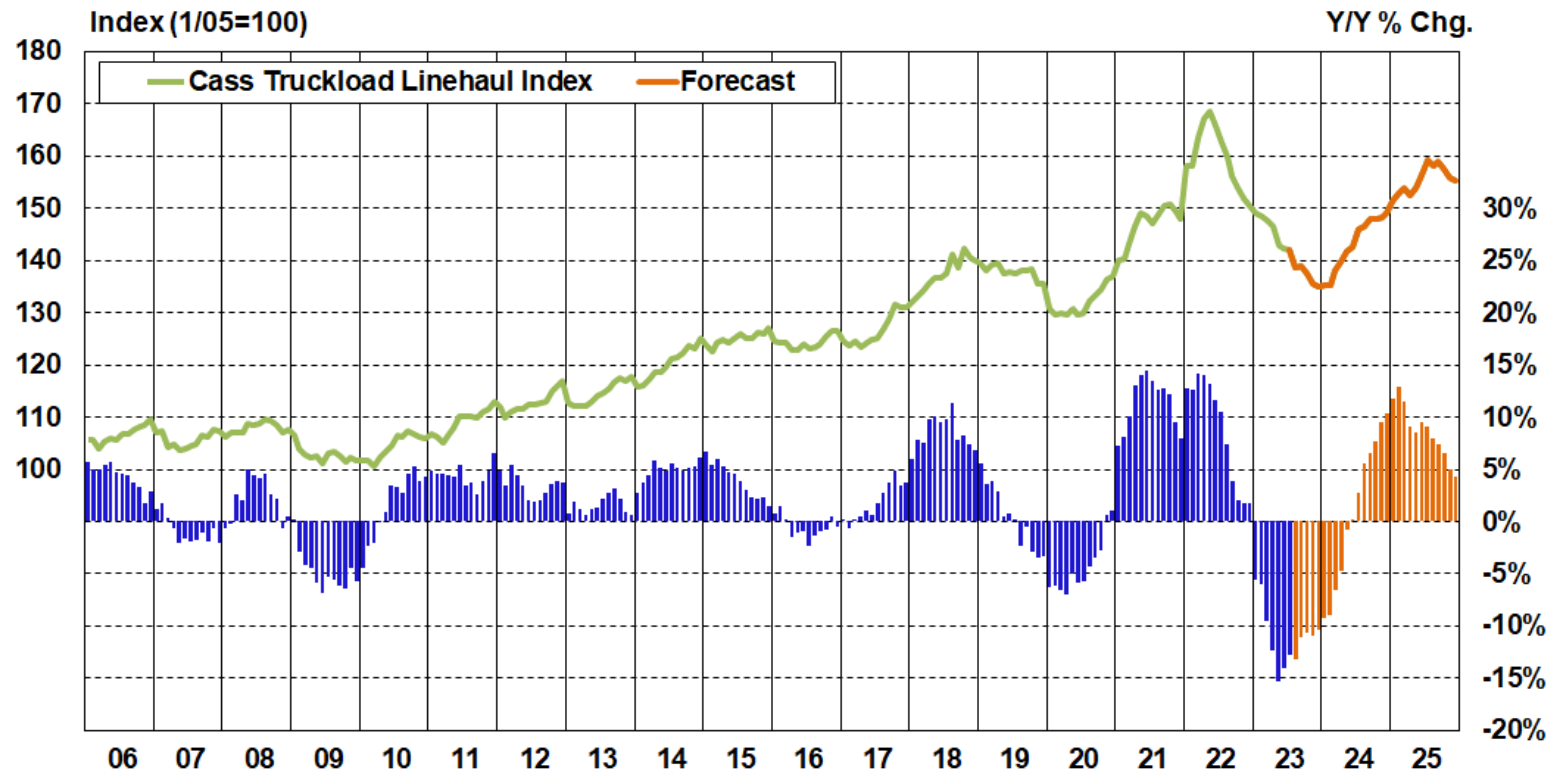
Source: DAT Freight & Analytics, ACT Research Co. © 2023

- Declines to persist into 2024
- After a 12% drop in 2023, increases in 2024 in question
- Slowing capacity and demand recovery set up recovery in 2H'24 and 2025

Cass Truckload Rates Headed Lower

Cass Truckload Linehaul Index ^(R)

January 2006 - December 2025 Forecast



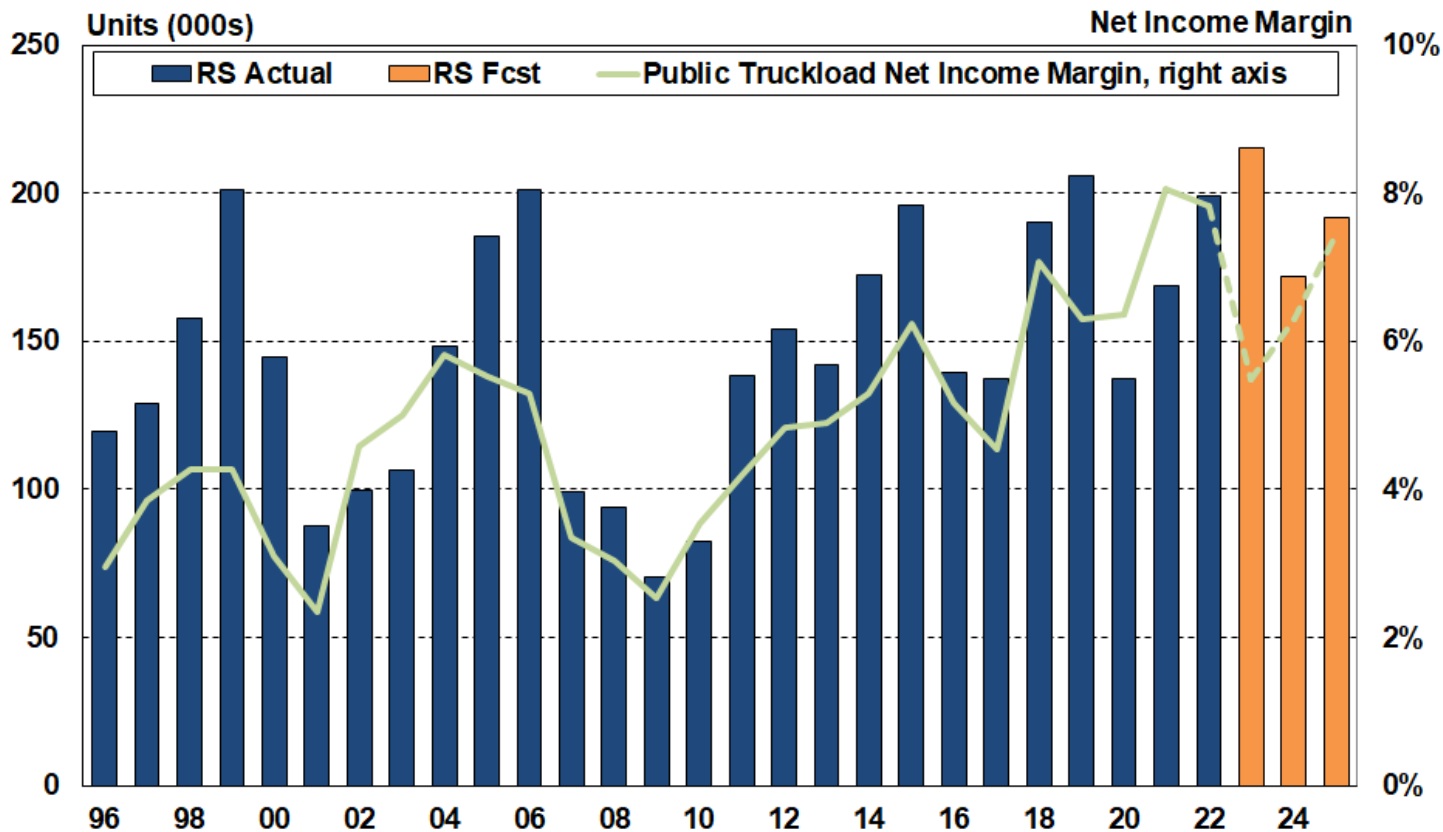
Source: Cass Information Systems, Inc., ACT Research Co. © 2023

- Unprecedented declines a clear stop sign for fleets
- 2024 a tale of two halves?
- Significant y/y rate declines likely through 1H'24
- Slowing capacity and demand recovery set up recovery in 2H'24 and 2025

Profits Hammered

U.S. Class 8 Tractor Retail Sales

1996 - 2025E



Source: ACT Research Co. © 2023

- Rates are the largest driver of industry margin changes
- Lower TL margins to impact tractor demand in 2024, with recovery cycle in 2025
- Every 1pp of margin = 25k tractors
- Risks to 2024 skew lower

Summary

- Shipper's market, still
- For-hire contraction helping spot rates bottom, but tractor build elevated
- Spot rate increase likely in Q4 as volumes begin to recover
 - For-hire volume recovery gated by private fleet growth
- Financial pressure to lower 2024 equipment demand
- Successful driver retention delaying cycle recovery, but demographics will drive another shortage in time





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