Reading the Economic and Transportation Tea Leaves

April 10, 2024

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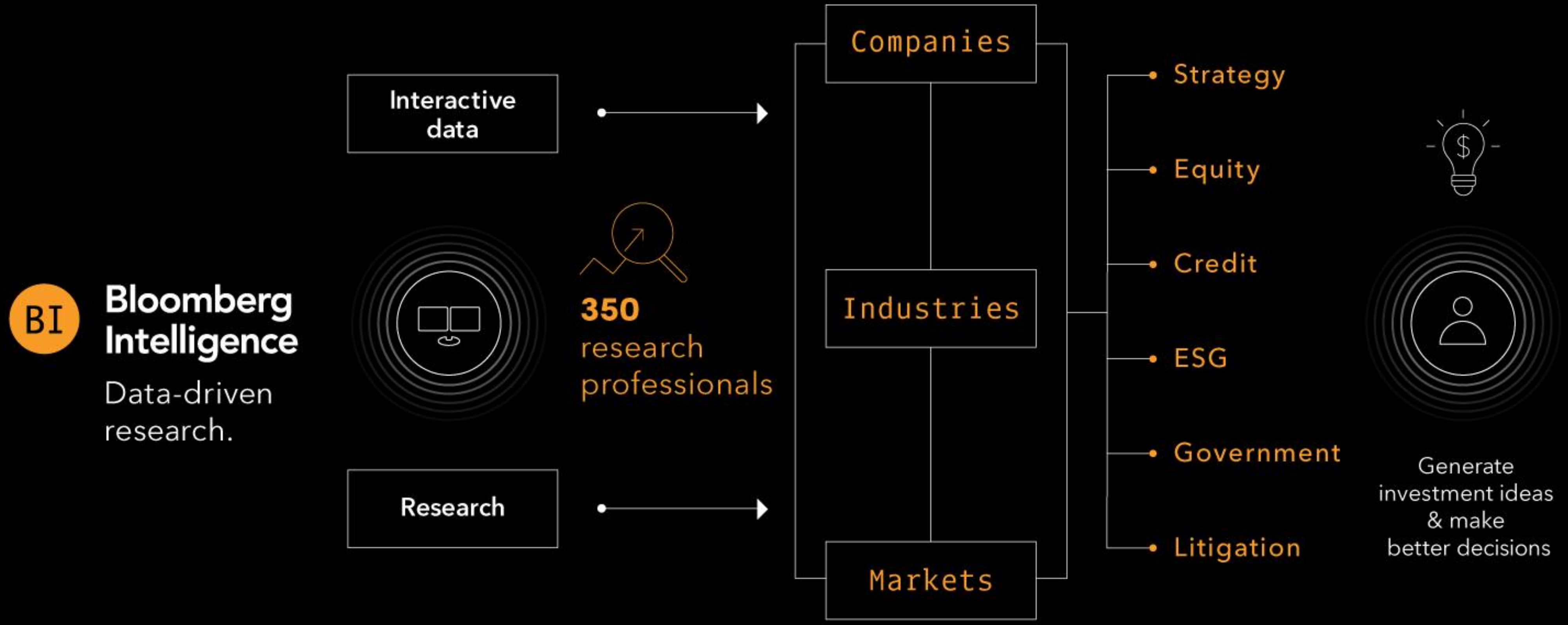

Freight Markets and Economic Outlook

Health & Personal Care Logistics Conference (HPCLC) 2024

April 10, 2024

Today's Speaker

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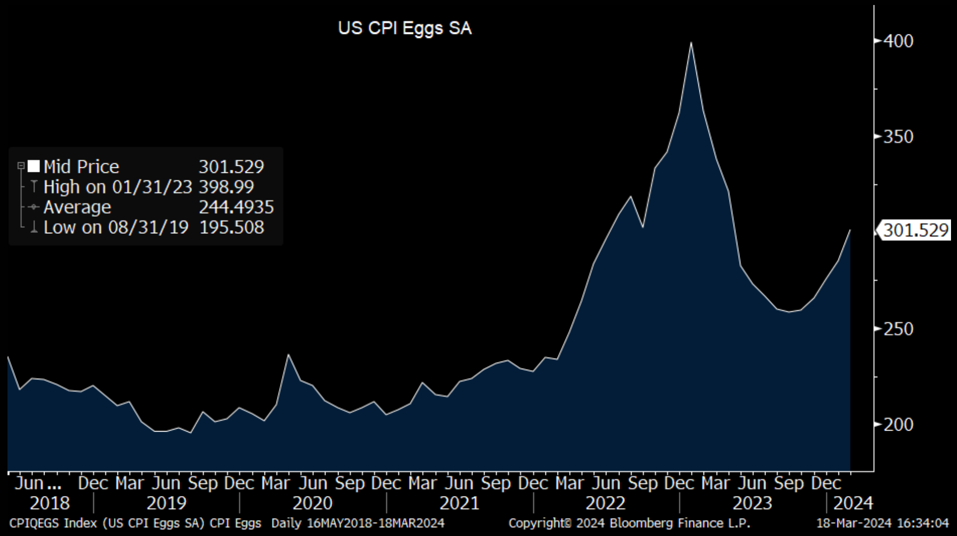
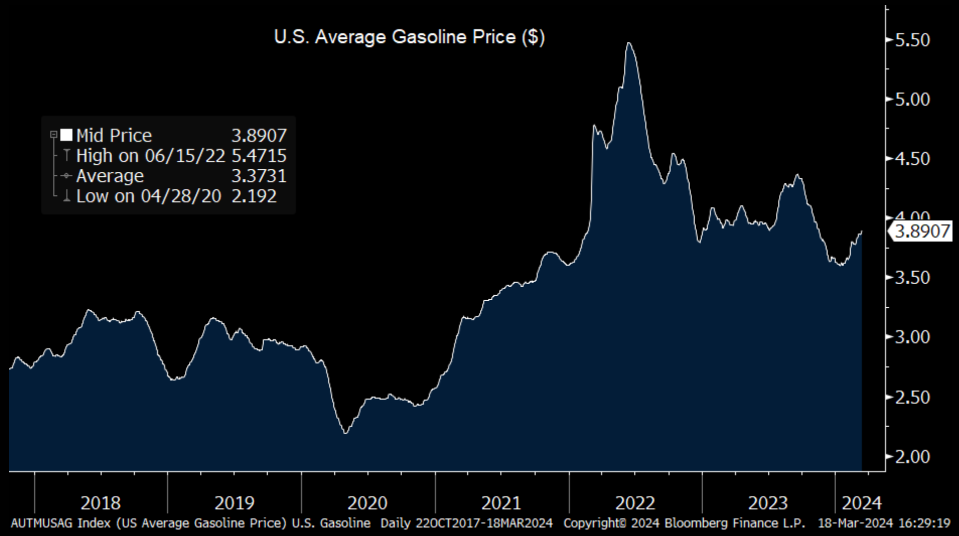
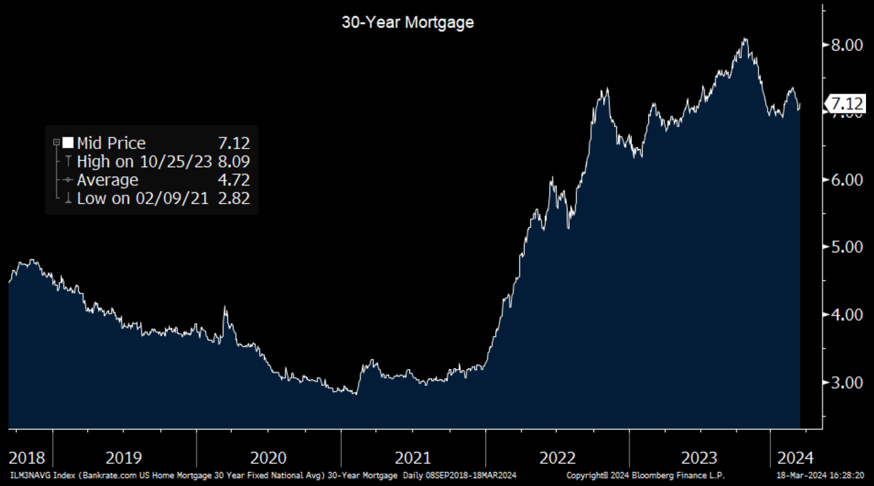
Challenges Abound







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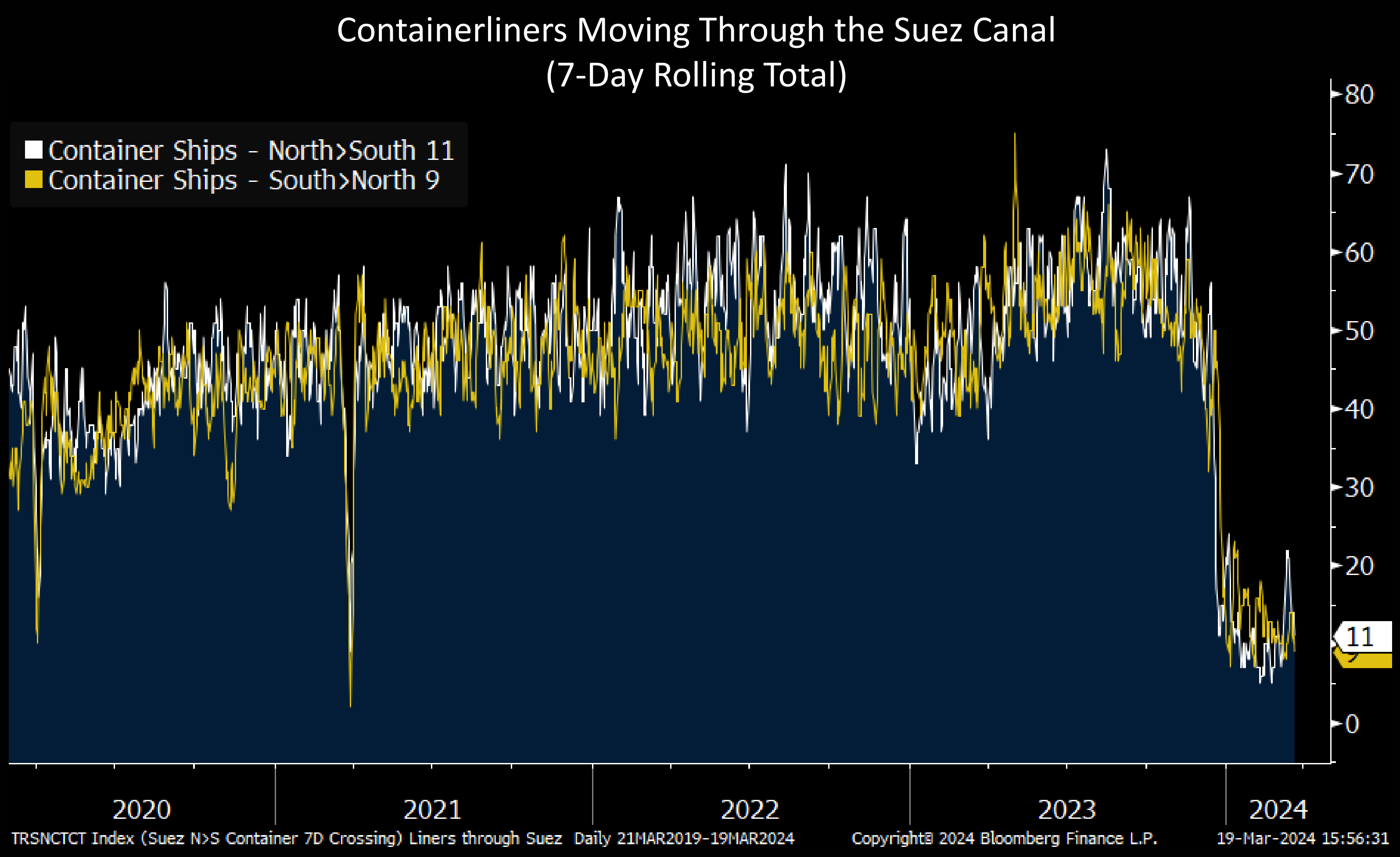
Source: Bureau of Labor Statistics, AAA, Bankrate.com, bloomberg.com, Bloomberg L.P.

Latest Black Swan Event – The Suez Canal Dislocation



- The Suez Canal is a major artery for the global economy, with about 10-12% of world trade passing through it each year.
- The canal ensures the efficient flow of materials and goods between Asia and Europe, and is key to keeping global supply chains moving.
- Vessels are adding 10-12 days to their voyage when they are diverted away from the Suez Canal to around the Cape of Good Hope.
- Ships hauling commodities from Iran and Russia will likely be the major users of the Suez since those countries are aligned with the Houthis.
- Shipping rates are beginning to normalize as capacity adapts to the new normal.

Source: Bloomberg L.P.

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Only Less-Than-Truckload Carriers have Outperformed the Broader Market Over the Last 12 Months

- Freight transportation and logistics shares face headwinds from moderating economic demand and normalizing rates.
- Less-than-truckload carriers got a boost from Yellow ceasing operations, solid pricing and margin expansion opportunities.
- U.S. railroads leading the Class I higher on self help initiatives at CSX and Union Pacific as well as Norfolk Southern targeted by activists.
- Over the last five-years the performance has been mixed relative to the broader market (+82%)
    - BI LTL (+370%)
    - BI Railroads (+73%)
    - BI Express Carriers (+15%)
    - BI Truckload (+10%)

Source: Bloomberg L.P.

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Number of Factors Weighing on Economic Growth, Freight Demand

Indicator	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
Economic Activity										
Real GDP (YoY%)	2.5	3.0	2.5	-2.2	5.8	1.9	2.5	2.1	1.7	2.0
Consumer Spending ...	2.6	2.7	2.0	-2.5	8.4	2.5	2.2	1.9	1.7	2.0
Government Spendin...	0.6	2.0	3.9	3.2	-0.3	-0.9	4.0	2.4	1.0	1.1
Private Investment ...	4.4	5.8	3.1	-4.7	8.7	4.8	-1.2	2.1	2.4	3.1
Exports (YoY%)	4.1	2.9	0.5	-13.1	6.3	7.0	2.7	2.2	2.5	3.2
Imports (YoY%)	4.7	4.0	1.2	-9.0	14.5	8.6	-1.6	1.4	2.5	3.2
Industrial Production (Yo...	1.3	3.2	-0.7	-7.2	4.7	3.4	0.2	0.3	1.5	1.8
Price Indices										
CPI (YoY%)	2.1	2.5	1.8	1.2	4.7	8.0	4.1	2.8	2.4	2.3
PCE Price Index (YoY%)	1.8	2.1	1.4	1.1	4.2	6.5	3.8	2.2	2.1	2.1
Core PCE (yoy%)	1.6	1.9	1.7	1.3	3.6	5.2	4.1	2.4	2.1	2.1
Housing Market										
Housing Starts (000s SAA...							1395	1424	1467	1500
New Home Sales (000s S...							681	688	735	756
Existing Home Sales (Mln...							4.1	4.1	4.7	5.0
Building Permits (000s S...							1452	1495	1518	1545

Economic growth, higher fuel costs, tight labor markets and supply chain constraints has created inflationary pressures not seen since the 1980s.

Headline CPI rose 3.2% in February, moderating from 9.1% in June 2022.

Low unemployment and stubborn inflation could mean the Fed could be slow to begin easing.

Geopolitical and black swan events are the biggest risks to economic recovery.

China's economy isn't recovering from Covid-19 restrictions as quickly as anticipated, as seen by weaker import and export data. This sluggish recovery will be a headwind to freight demand and rates in the near term.

A return to seasonality a welcome sign as demand patterns normalize.

Source: Consensus Estimates, Bloomberg L.P.

Earnings Growth May Rebound in 2024 as Freight Markets Normalize

	2022 Revenue Growth	2022 EPS Growth	2023 Revenue Growth	2023 EPS Growth	2024E Revenue Growth	2024E EPS Growth
North American Class I Railroads	14.1%	14.6%	-1.6%	-5.1%	3.2%	6.9%
North American Truckload Carriers	21.7%	28.8%	-10.5%	-48.1%	3.8%	1.5%
North American Less-Than-Truckload Carriers	20.5%	39.2%	-6.3%	-20.1%	8.5%	20.1%
Global Integrated Logistics Providers	21.7%	1.1%	-16.0%	-17.4%	-2.2%	6.9%

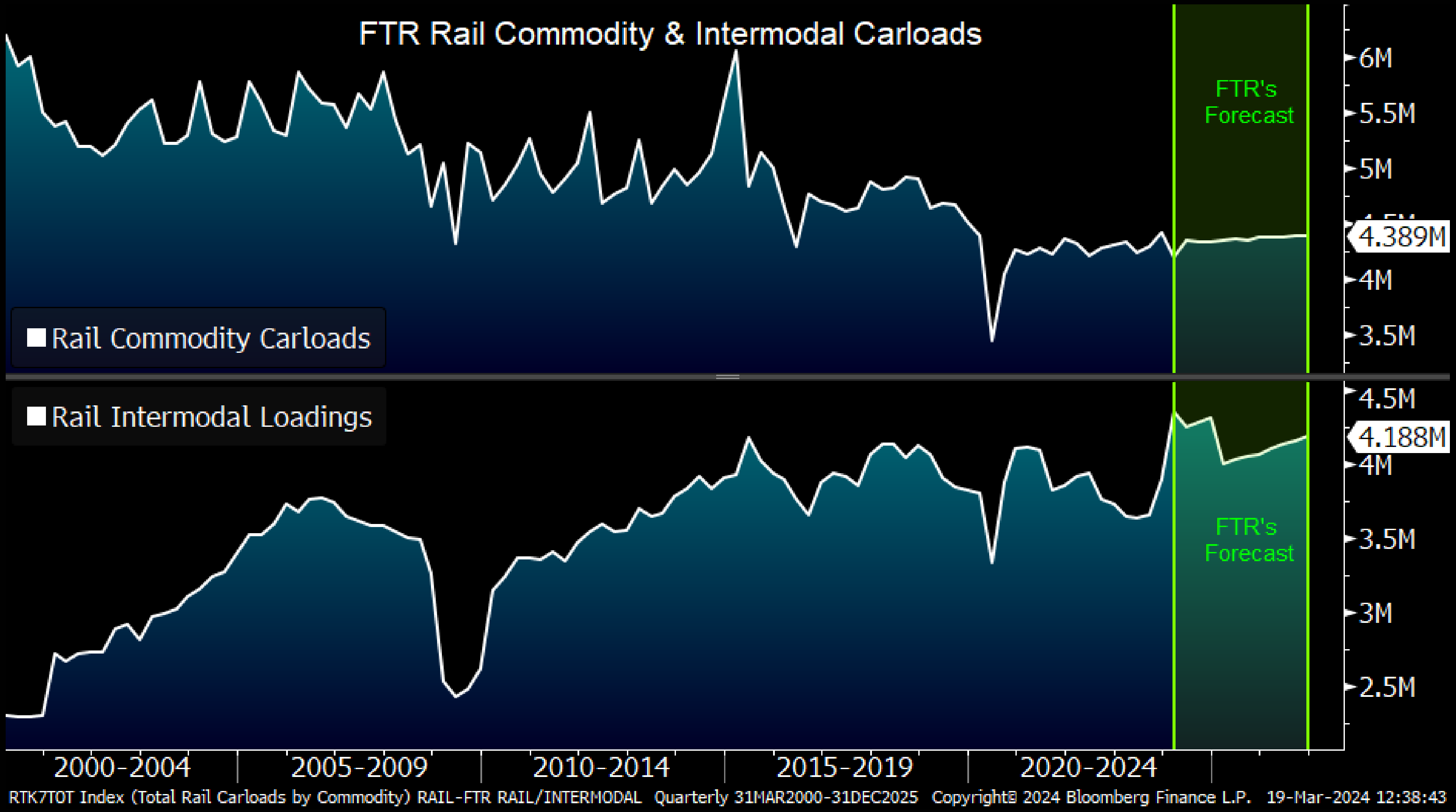
Key drivers for revenue and earnings growth into 2024:

- Rails – Intermodal could lead volumes higher as the industry makes more progress related to reliability and service. Rate increases offset inflationary pressures coupled with improved fluidity
- Truckload – Slack capacity limits meaningful rate increases until 2H when the demand picture could improve
- Less-Than-Truckload – Pricing remains strong, market share wins from Yellow mitigate weak demand backdrop
- Parcel Carriers – Aligning resources, rate-driven margin gains, technology-fueled productivity gains, B2B recovery

Source: Consensus Estimates, Bloomberg L.P.

Intermodal May Lead Railroad Volume Higher in 2024

- After two years of volume declines, North America railroad volume growth may inflect into positive territory in 2024, in our view.
- FTR expects U.S. intermodal traffic to rebound 6.2% in 2024 after 3.4% declines in 2022 and 2023.
- Intermodal growth will be driven by inventory destocking, normalizing season trends and improving railroad service, in our view.
- Commodity carloads may decline 0.3% in 2024 according to FTR forecasts. Weakness in forest products, motor vehicles and coal will be a drag growth lower this year.
- Coal growth may inflect negatively in 2024, continuing its long-term secular decline.



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Source: FTR, Bloomberg L.P.

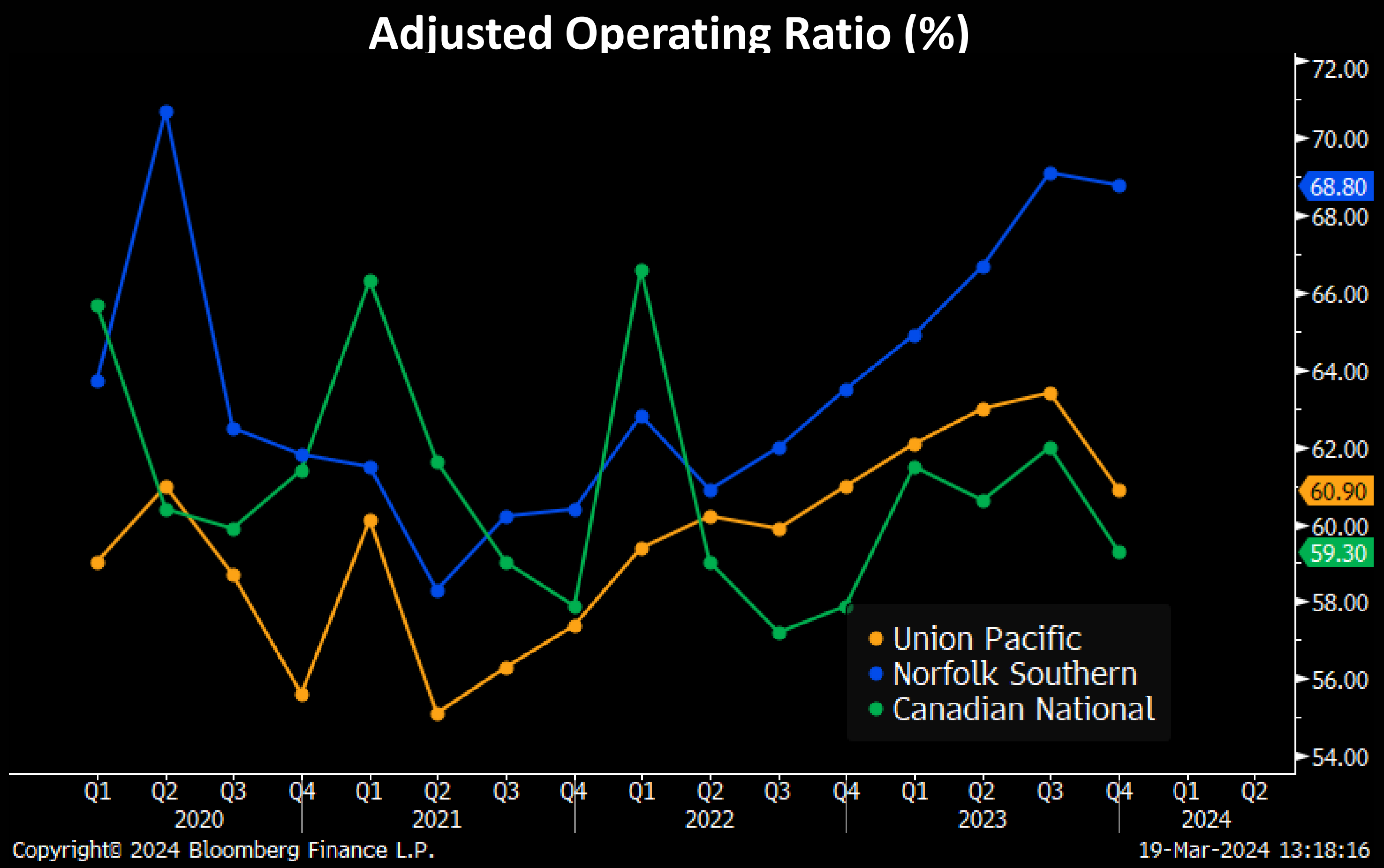
Precision Driving Operating Leverage

Precision scheduled railroading (PSR) could drive further margin improvement and profitability improvements, now that all public Class I railroads are employing the operating philosophy on their networks.

Norfolk Southern and Union Pacific are in the early innings and have the most to gain. Canadian National refocused back to margins from profitable growth. Canadian Pacific will be focused at improving KC Southern's operations.

Operating ratios may improve by 160 bps in 2024 according to consensus estimates. This would bring the median public Class I rails' operating ratio to over 61.

Better service will go a long way in improving profitability. Railroads are playing catch-up after overreacting following the decline in volumes at the start of pandemic.



Source: Bloomberg L.P.

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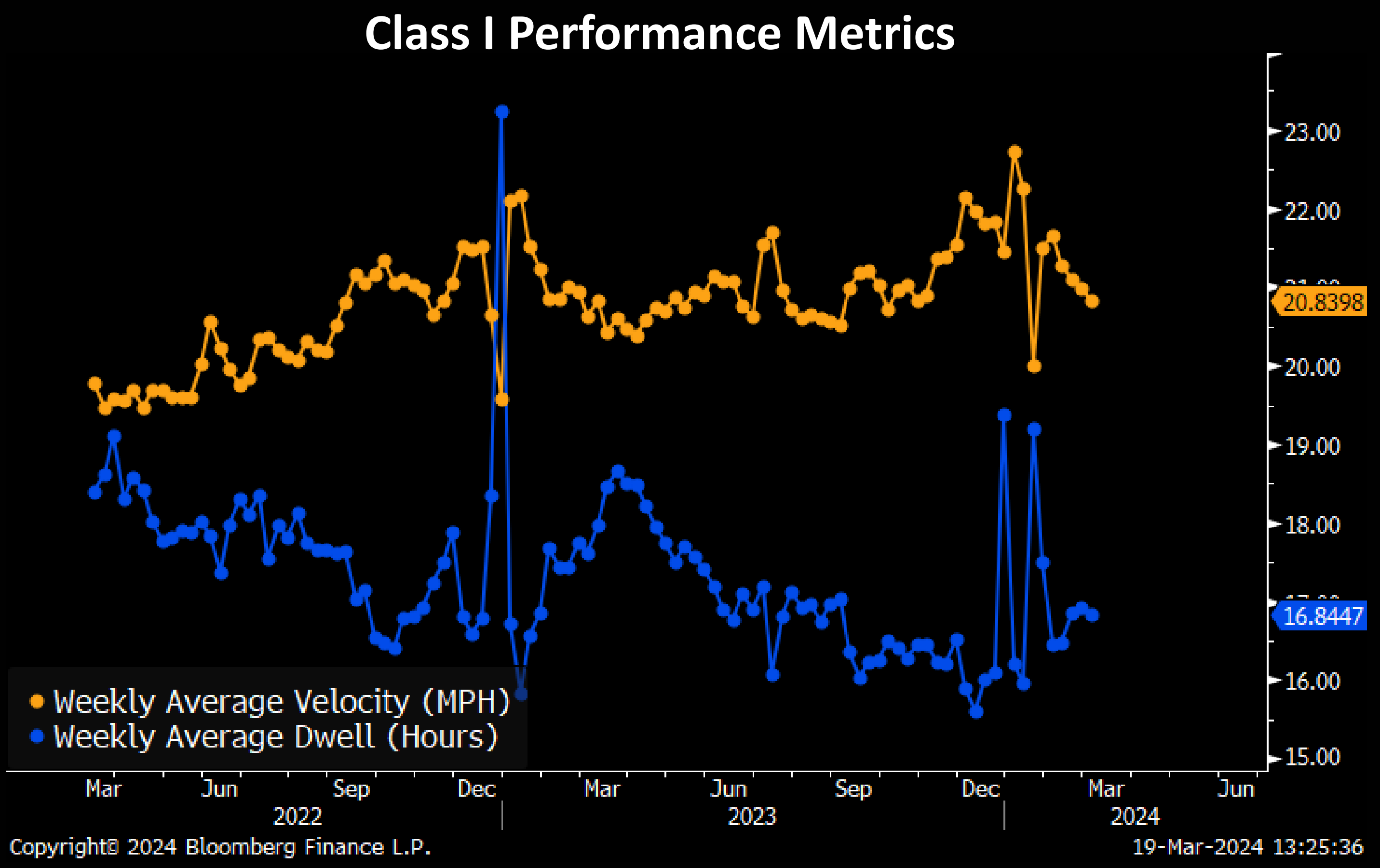
Improved Rail Service Will Make Everyone Smile

Network velocity (higher = better) and dwell times (lower = better) are moving in the right direction for Class I railroads.

Fluidity has improved recently. Train are running 1.8% faster from last year on a four-week moving average and dwell times improved by 3.6% as of March 1. The industry is trying to get back to pre-pandemic service levels.

Norfolk Southern fluidity was hit following the derailment in Palestine Ohio in Feb. 2023. Union Pacific was impacted the most from labor shortages in addition to recent network washouts. It has been making progress but still lag its peers.

U.S. railroads have made significant progress at hiring and training workers. They aggressively furloughed/laid off employees at the onset of the pandemic and were not prepared for when volumes surge back.



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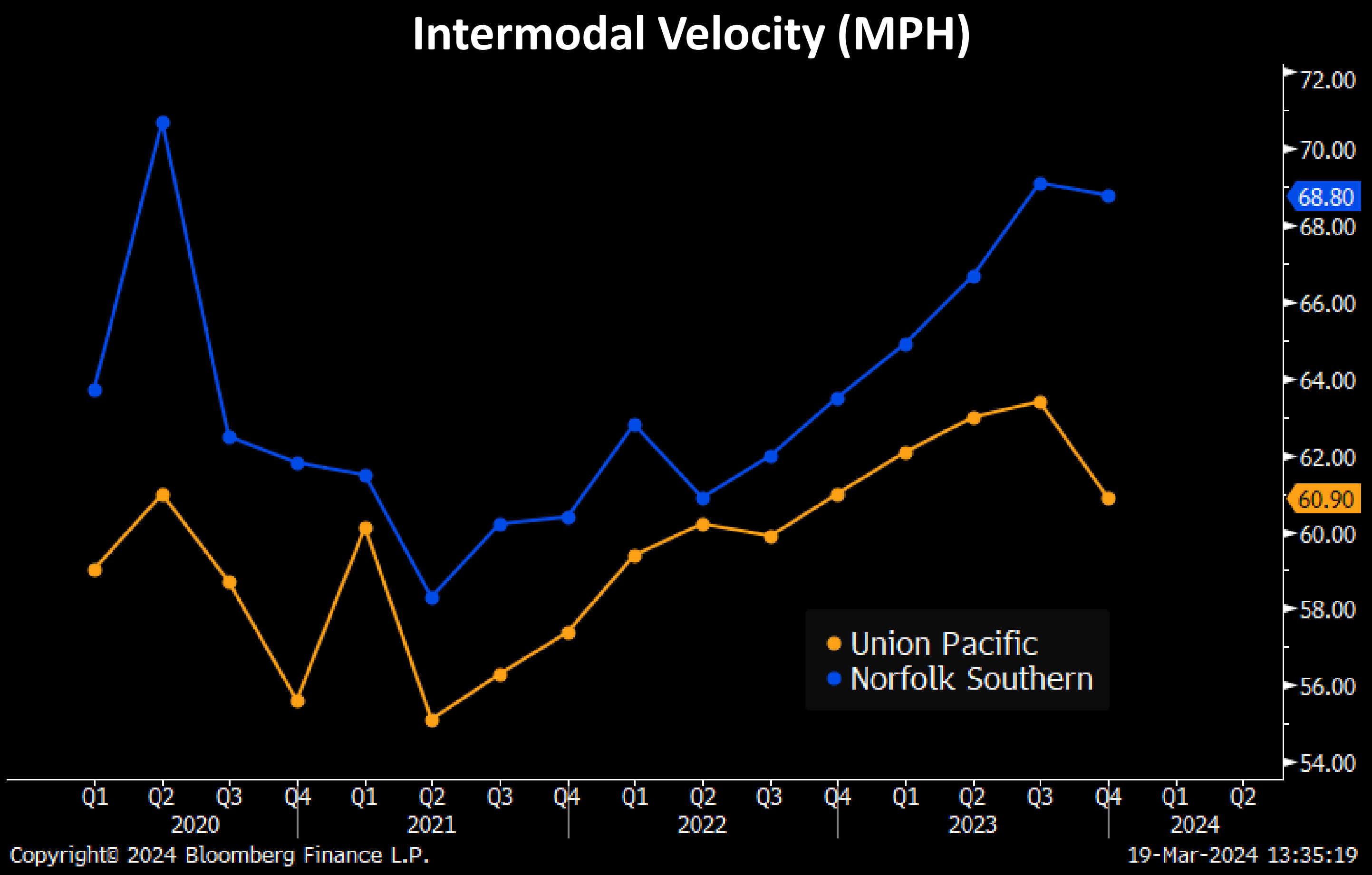
Source: Company Reports, AAR, Bloomberg L.P.

Need to Build on Better Intermodal Service



Improved network fluidity and increased consistency will go a long way at driving more intermodal freight onto the railroads.

Intermodal benefits include lower costs, reduced emissions and access to capacity.

Intermodal can be more compelling for shippers when fuel prices are high since railroads can be 3-4 times more fuel efficient than trucking.

Tighter labor markets and accidents have created inconsistent intermodal service levels.

Higher diesel prices and tighter truckload markets would bode well for share shifts to the railroads from the highways.

Source: Company Reports, AAR, Bloomberg L.P.

Intermodal Rates Waiting For Trucking Rebound

Intermodal spot rates are falling, inline with the trucking market. InTek's All-In 53-Foot Spot Rate Index is down 5.9% on average in 1Q24.

Despite the weakness rates are in good shape, up about 9% from the pre-pandemic levels in 1Q19.

Looser trucking conditions will weigh on core intermodal rates near-term. We expect truckload spot rates to show signs of growth in late 2Q, early 3Q.

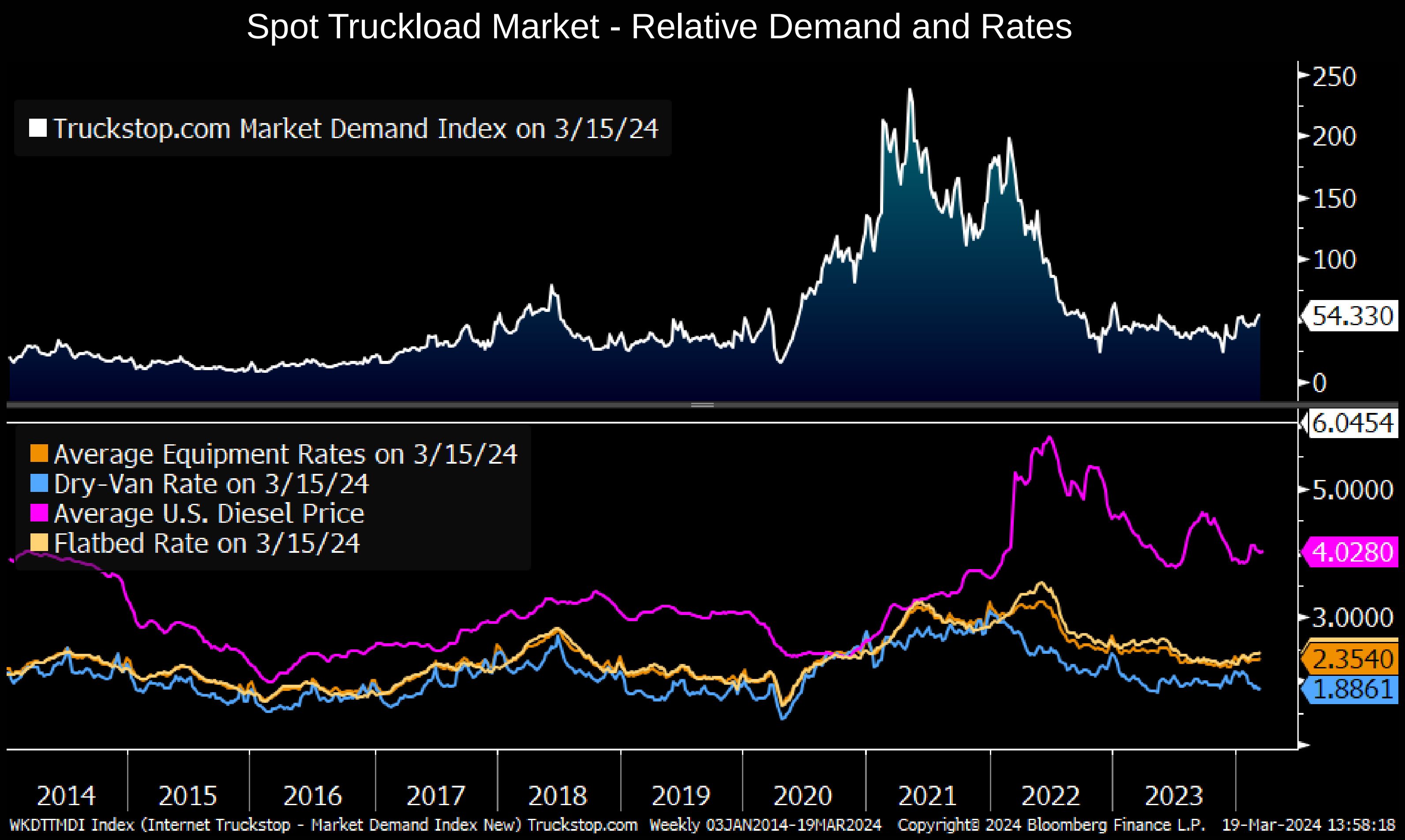
Railroads have a long history of price discipline, looking to raise rates above rail inflation.

Railroads need to mitigate rising costs, especially as it relates to labor inflation and equipment expenses.

Intermodal Spot Rates – Top 18 Lanes

Source: InTek, Bloomberg L.P.

Spot Rates Bouncing Along the Bottom



Source: Truckstop, Bloomberg Intelligence

The North America spot trucking market has been loosening since the extremely tight conditions in 2021.

Truckstop's Market Demand Index (MDI), posted its first year-over-year gain quarter-to-date in 1Q after seven quarters of declines.

Capacity has been slow to leave the market and has delayed any significant increase spot rates.

We expect spot rates could slowly improve through 2Q, which could set up a more constructive contract rates in 2H24.

Spot truckload rates excluding fuel surcharges are down 3% on average in 2024. They are currently 5% higher from 2019 levels.

Spot rates by equipment type in 2024:
Reefer (-0.5%)
Dry-van (-1.2%)
Specialized (-4.6%)
Flatbed (-4.9%)

Contract Truckload Market In Better Shape Than Spot

The weaker spot market has put pressure on contractual rates.

Truckload contractual rates decreased 11% on average in 1Q24 based on DAT data. Dry-van (-126%) are down the most, followed by flatbed (-11%) and reefer (-8%).

Contract-rate growth may inflect positively in 2H, with FTR projecting this will occur in 3Q.

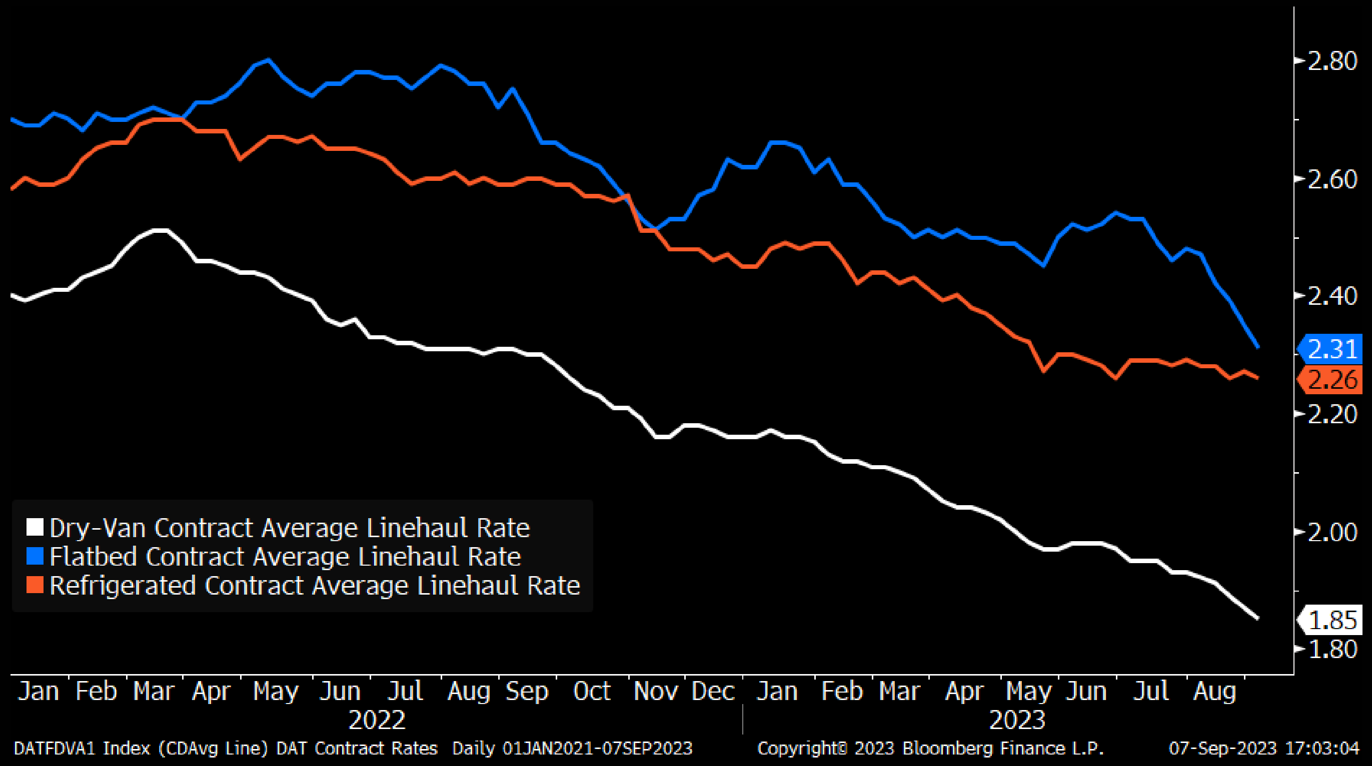
Tighter spot conditions, an end to destocking and a return to normalized demand patterns will be key for contract rate strength.

Contract rates will not be as volatile as the spot market, which is in the process of rebalancing.

Average spot-contract spreads narrowed a steep 7.8% sequentially through March 17 based on DAT data.

Contractual rates tend to lag behind the spot market by 6-9 months.

Revenue per Mile Excluding Fuel Surcharge ($)



Source: DAT, TruckloadRate.com, Bloomberg Intelligence

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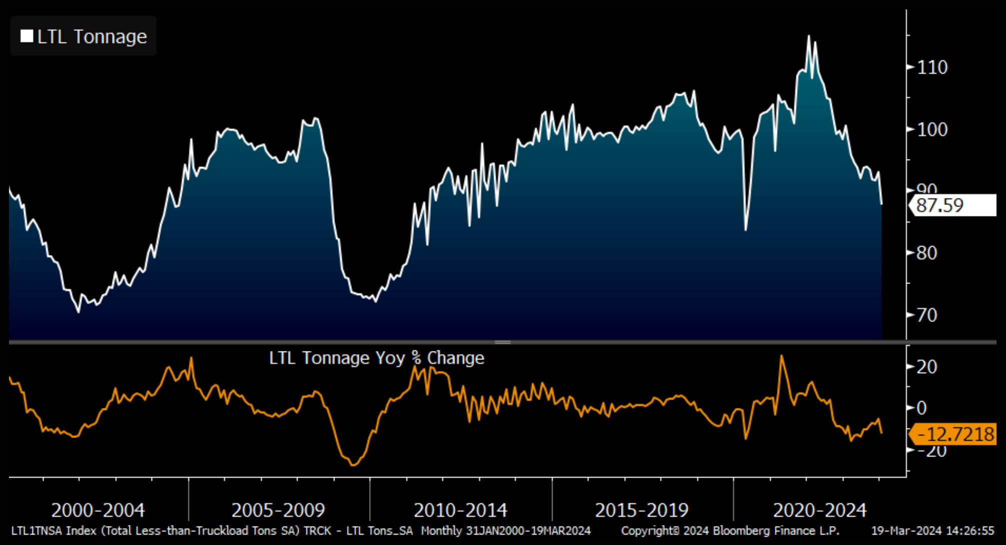
LTL Disciplined Through the Cycle

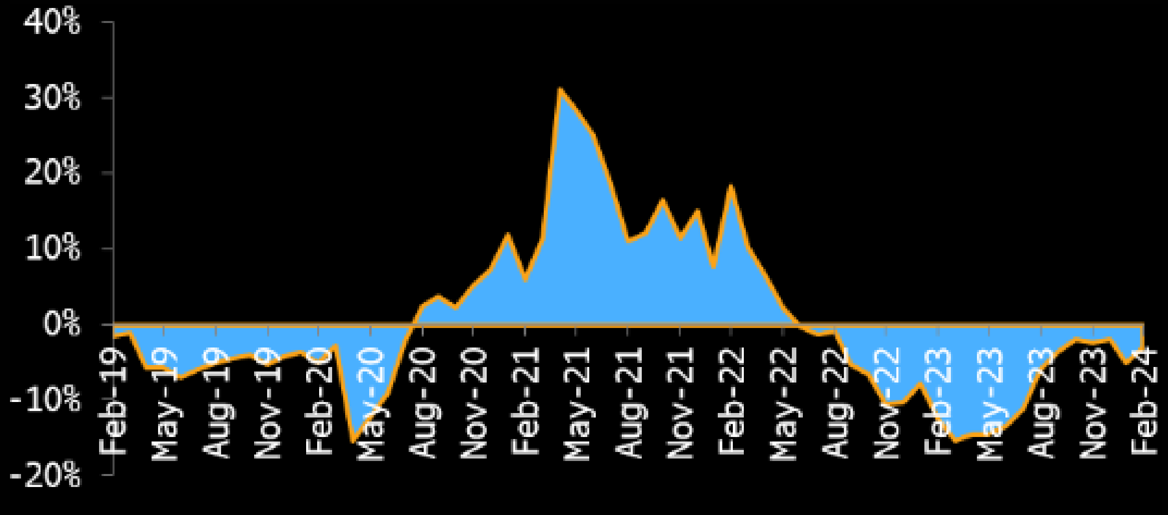
Less-than-truckload carriers' ability to exceed earnings expectations will be driven by how demand in March -- 1Q's busiest month -- shapes up. Moreover, the positive pricing environment and share gains, which were aided by Yellow's market exit, should mitigate weak demand. The median operating ratio for LTL carriers could improve 69 bps in 1Q, based on consensus.

Yellow's bankruptcy further consolidated the LTL industry, providing opportunities to gain market share and created a stronger-for-longer pricing environment for carriers.

ATA Seasonally Adjusted Tonnage



Old Dominion's Monthly Tonnage Growth (%)



Source: American Trucking Associations, Bloomberg Intelligence

Old Dominion's Statistics:
- Shipments +0.2%
- Tonnage -3.0%
- Revenue per Hundredweight Ex-FSX (QTD) +7.4%

XPO's February Statistics:
- Shipments +5.8%
- Tonnage +3.5%

Saia's February Statistics:
- Shipments +19.0%
- Tonnage +11.0%

ArcBest's February Statistics:
- Shipments -4.0%
- Tonnage -14.0%
- Revenue per Hundredweight +13.0%

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Container Liner Rates Sailing Past the Peak

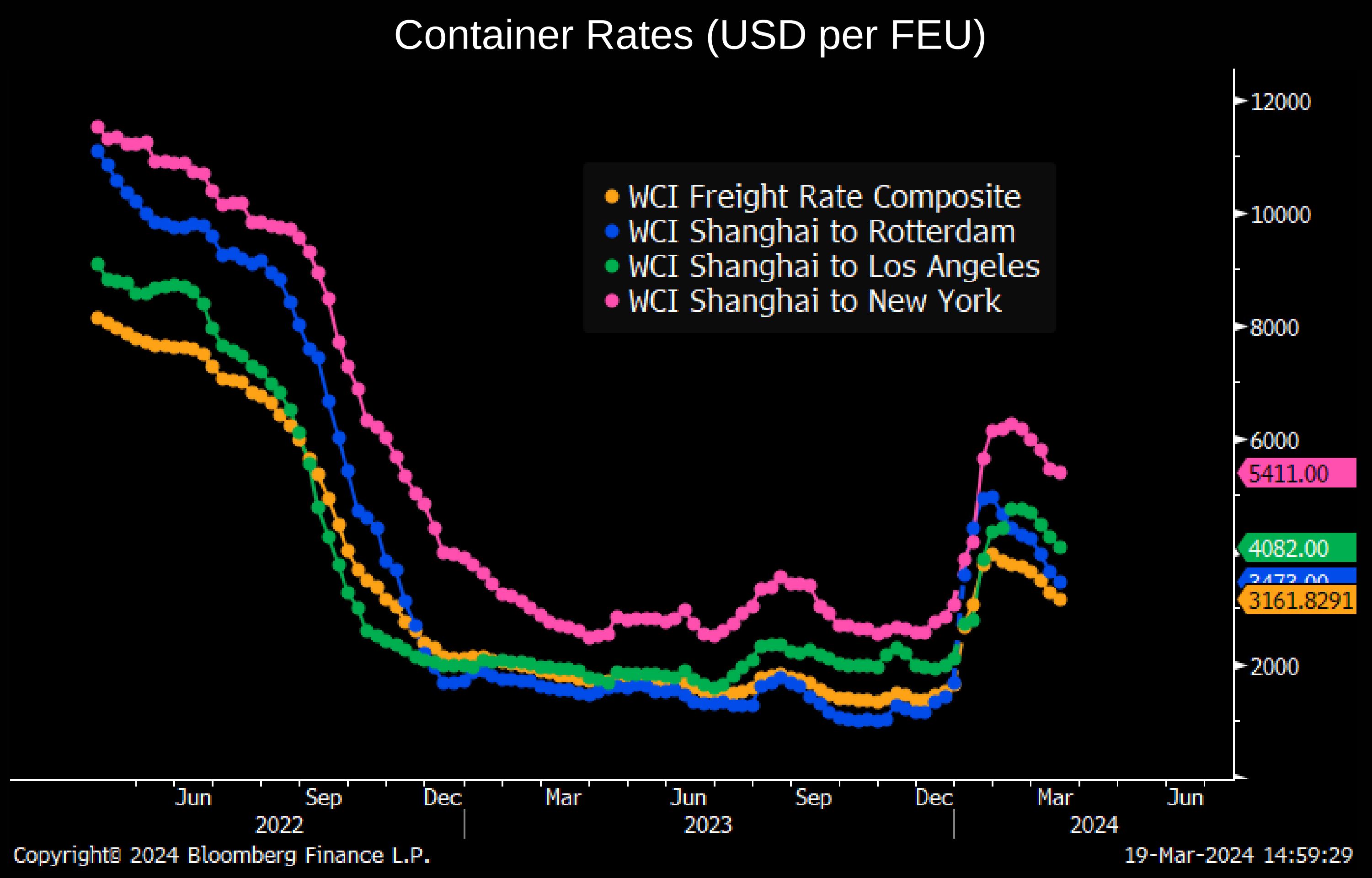
Last year will likely mark peak earnings for global containership operators now that rates are normalizing from their unsustainable levels.

Spot container liner rates from China (SCFI) are up 95% from last year, while contract rates (CCFI) are 29% higher from the dislocation created by the Red Sea crisis.

Volume was flat last year after declining 4% in 2022. It may increase by low-single digits this year.

Rates will face structural headwinds from increased ordering activity. The orderbook as a percentage of the fleet is 23.2%, 500 bps above its 10-year average, based on Clarksons' data.

Supply growth has outpaced demand growth 17 out of the last 23 years, according to Clarksons. It may happen again in 2024 and 2025.



Source: Drewry's WCI , Bloomberg Intelligence

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Air Freight Rates Descending for Sky High Levels

Supply-chain bottlenecks and capacity constraints should keep air freight spot pricing well above norms this year.

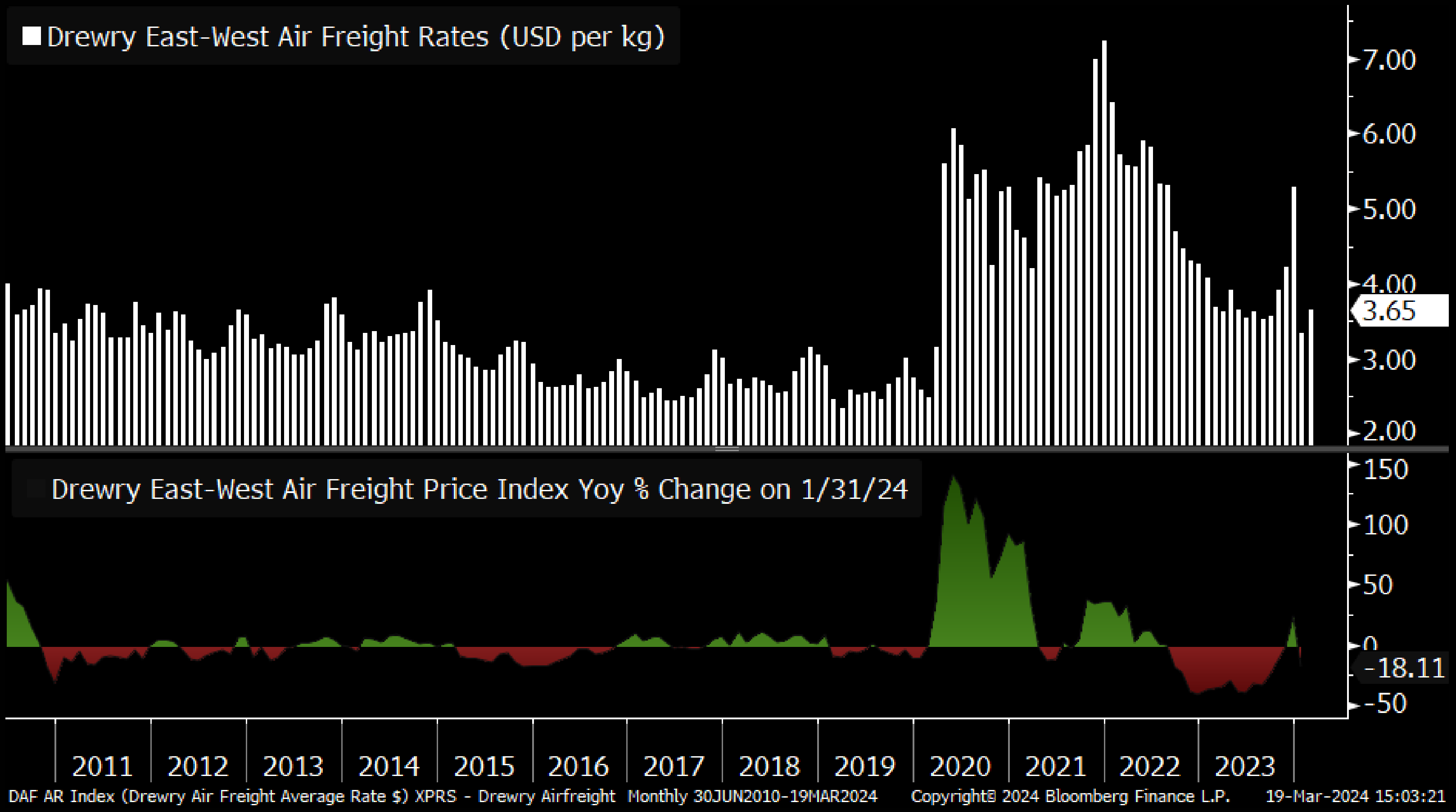
International air cargo capacity was up 18.2% in January, according to IATA data, but is near 2019 levels.

January international demand surged 19.8% and 4.0% higher from the same period in 2019 according to IATA.

Air freight rates are down 12.5% from last year during the week of March 10 according to WorldACD. Rates continue to normalized from unsustainable levels reached during the pandemic..

The Red Sea crisis has been an incremental positive for air freight demand and rates.

Air Freight Rates by Drewry



Source: Drewry, Bloomberg Intelligence

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Q&A

Thank you

Contact the Bloomberg Intelligence Analyst

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Let's connect!!

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