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Race to Bottom, as Huge Drops in Shipper Demand Parallel Equal or Greater Losses in Carrier Capacity

Bank Actions Could Take an Even Greater Slice Out of Carrier Market; Big Problems as Economy Recovers?

SCDigest Editorial Staff

It's an interesting contest – will truckload and LTL carriers be able to shed capacity more rapidly than shipper demand has fallen?

Although there are actually many hopeful signs for the economy starting to emerge, right now these are some of the worst times ever for carriers. A freight recession that really started for the industry in at least 2007 and maybe even a bit earlier combined with the overall economic downturn to create incredibly tough times for carriers in virtually all modes. (Though we note recently rising stock prices for the carriers may be a leading indicator of recovery, as it usually is.)

The American Truck Associations' monthly truck index dropped 12.2% in March compared with a year ago, falling to the lowest level since March 2002, just one of many data points illustrating the industry's challenges.

But while demand for freight carriage has been decimated, there has been a corresponding loss in truck carrier capacity – though not quite as steep as demand has fallen. As a result, the supply-demand situation is still strongly in the shippers' favor.

(See graphic on page 2.)

In the truckload and LTL sectors, the capacity reduction is coming from two fronts.

First, many carriers and independents are going bankrupt or otherwise leaving the market. Second, surviving carriers are cutting back drastically on their assets.

Many financially troubled carriers for now have not been forced into bankruptcy by their lenders, in part because of the low current sell-off value of the assets that secured the loans (trucks and terminals).

Jon Langenfeld, a transportation industry analyst at Robert W. Baird, said it looked like only 70-75,000 class 8 trucks would be procured by US carriers this year – versus a normal expected need for 220-230,000 as pure "replacement" units. The difference is lost capacity.

Despite the huge drop in truckload and LTL capacity, many observers have been surprised the losses haven't been even greater. There is a reason for that, says **John Larkin** of Stifel, Nicolaus & Co.

Larkin says that a huge additional swath of capacity could leave the market rapidly – if bankers take a new tack. Many financially troubled carriers for now have not been forced into bankruptcy by their lenders, in part because of the low current sell-off value of the assets that secured the loans (trucks and terminals).

If the banks take a hard-line approach, however, and force many carriers under, it could accelerate the change in the supply-demand equation that almost everyone predicts.

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The Truckload Segment has Witnessed the Greatest Reduction in Capacity; How Much More Capacity Will Leave the Market?

Segment	Short-Term Reduction	Long-Term Reduction
TL	18%	15%
LTL	8%	6%
Rail	15%	0%
Barge	15%	0%
Parcel	3%	3%
Express	12%	8%
Air Freight	4%	0%
Ocean	11%	0%

Source: John Larkin, Stifel Nicolaus

The lost capacity already seen is potentially setting the stage for a possible fast and steep surge in the other direction when the economy recovers, many believe.

With many shippers continuing to push carriers for lower rates when they are already at loss-inducing levels, "many shippers have burned bridges with their carriers as a result of price actions in the first half of 2009," Larkin said. "Expect the favor to be returned in those cases when the supply-demand environment changes."