CAPACITY

LEADING SIGNS OF A LOOMING CAPACITY CRISIS

For years, industry observers from across the spectrum have predicted a dire capacity shortage in the freight transportation industry. Citing a growing driver shortage, an aging and crumbling infrastructure, increased regulatory burdens and uncertainty in the marketplace, company executives, politicians and financial experts agree that a time of reckoning is coming.

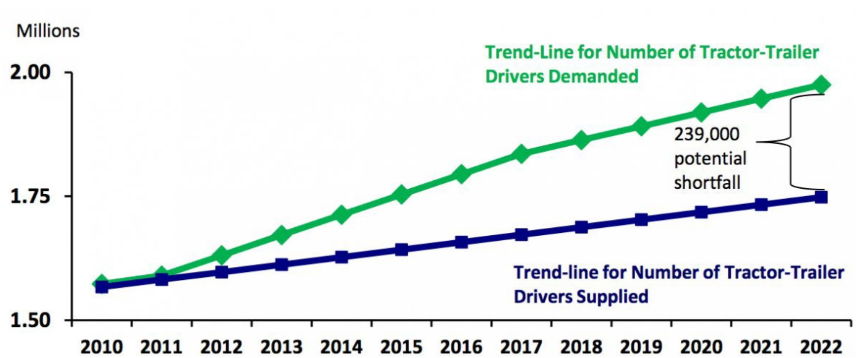
WILL 2017 BE THE YEAR THAT THE CAPACITY SHORTAGES REACH CRISIS STATUS?

Driver Shortage

Drivers are retiring in droves and there is a growing shortage of trained and licensed drivers willing to replace them. Truck driving schools, as well as carriers, are actively recruiting with limited success. The most likely candidates are single people without young children or families. They are lured by the freedom to live on the road while hauling across the country. However, the lure is not what it once was. Among the resources being tapped for a new workforce are single women and military veterans seeking good incomes and the independence that comes with a promise of a new career ahead.

Currently, the largest cohort of the truck driving workforce – 34.3 percent – is aged 45 to 54, with the second largest group aged 35 to 44 at 31.8 percent and 55 to 64 at 13.9 percent.

"We, as an industry, by 2024, need to bring in nearly 900,000 new drivers that are not in the industry today," said Bob Costello, chief economist for the American Trucking Associations. "The number one reason is the retirement of existing drivers. The natural market reaction is to raise wages, but there are many other causes of the driver shortage, with demographics being one of them. The average age of a truck driver today is 47 and the average age of the U.S. worker is 42. Today, 47 percent of all workers are female and 6 percent of all truck drivers are women. Even though jobs are available, some regulations hinder productivity and require more trucks to haul the same amount of freight. There is no one solution."

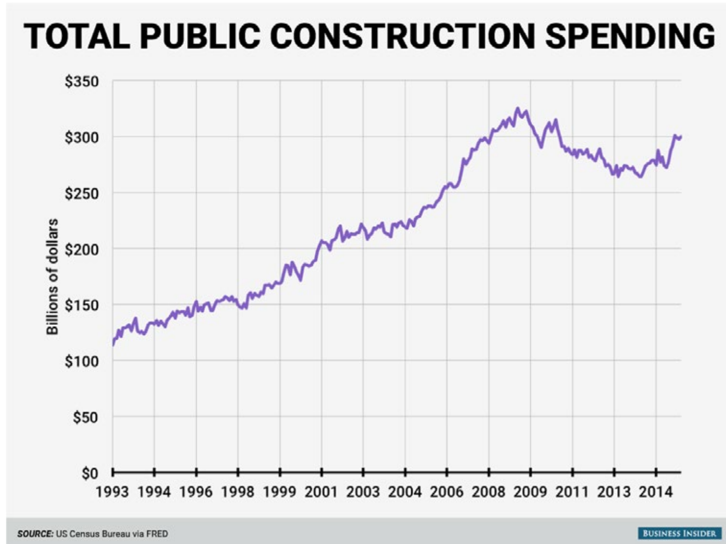


Source: ATA

AGING INFRASTRUCTURE

American infrastructure in key areas, such as transportation, the Internet and energy is widely viewed as subpar.

It is also understood that quality infrastructure is a key asset in economic competition in today's globalized economy.



Source: US Census Bureau

President-elect Donald Trump has made his commitment to rebuilding the nation's infrastructure clear. The infrastructure, he noted in his acceptance speech, "will become, by the way, second to none." This commitment has created nationwide expectations that federal dollars could trickle down to public construction projects long left dormant. But Trump's plan, what little we know about it, is far different than the kinds of government-spending programs that state officials have become accustomed.

So far, the biggest clue to Trump's infrastructure plans came in a 10-page policy paper his campaign released in late October. Written by leveraged-buyout master Wilbur Ross and the University of California - Irvine economist Peter Navarro, it promises to create $1 trillion in new roads, ports, bridges and other concrete-and-rebar public works, all by providing $137 billion in income tax breaks for any private companies willing to front the cost.

REGULATORY BURDEN

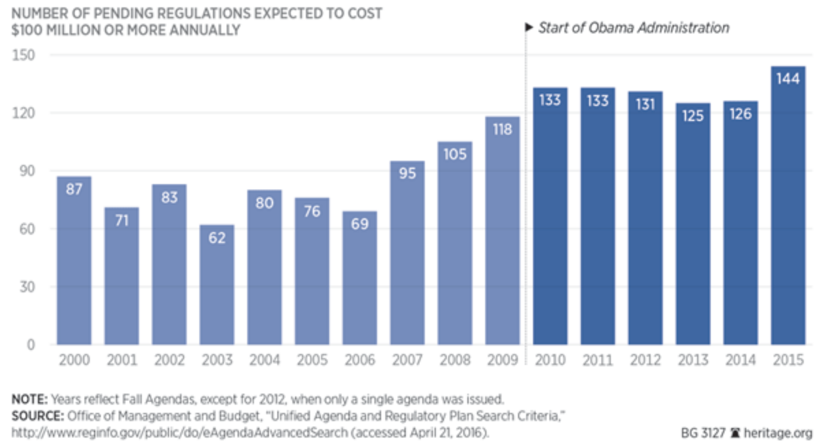
Government trucking regulations are expected to have a great impact on transportation rates, trucking capacity and overall economic productivity.

Currently, there are no fewer than 20 laws expected to have a steep impact on transport costs. Chief among them is the so-called Driver Coercion Law, CSA Compliance, Hours of Service and e-Logs. Some changes in these laws affect various businesses in different and distinctive ways. For example, a broken law could carry heavy financial penalties on shippers, motor carriers, as well as logistics operators. These regulation infractions could possibly add to costs by revoking the operating authority of freight brokers, forwarders and carriers. For the trucking company, trucker transport shortage is already being felt with a critical loss of more than 5,000 trucking companies and 400,000 trucks now off the road.

The Electronic Logging Device Mandate will affect about 3 million drivers and went into effect in December 2017. About half of the trucking industry has already installed ELDs, but if the remaining half doesn't equip the device, they'll be forced to exit the industry, resulting in a significant loss of capacity. Even though ELDs have constructive implications, the mandate could create logistics headaches by taking away capacity and increasing rates.

Gordon Klemp, founder and president of the National Transportation Institute said that "while regulatory drag has been around for a long time," its impact on the industry is about to be felt intensely. "ELDs are here, and speed limiters are on the horizon, with hair testing [for drug use] tending to grow in use," he said. "When we see them [ELDs] roll through the industry, I think we'll settle out to a 5 percent net loss in productivity."

He predicts that the much-debated speed limiter rule will cost the industry another 3 to 5 percent in productivity, with wide variances among fleets.



"With hair testing, everyone we talk with says the same thing – it's painful to start with," Klemp added. For driver candidates testing positive in urine-based drug tests, Klemp says results initially "went from 5 percent to 8 percent rejection rates to an 11.6 percent rejection rate. But then it dropped back down to 5 percent." One reason for that decline is that candidate "self-select" themselves out. "But that [11.6 percent rejection rate] is higher than I would have ever thought, and it will lower the labor pool by 5 percent."

Add it all up, and the industry is facing a 15 percent loss in productivity due to regulatory drag, "and it's probably more when you look at the whole boat [of regulations] and not just the three we picked out," Klemp concluded.

MARKET UNCERTAINTY

In 2017, the U.S. population is expected to rise to 332 million. That's a 70 percent increase in the past 50 years. Population growth in cities is placing a strain on existing transportation systems and creating demand for more transportation choices. Industries and consumers depend on the consistent, timely flow of goods and services. The mounting volume and availability of information and the rapid development and adoption of technologies are transforming all aspects of life, including transportation.

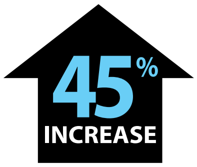
Transportation connects industries; it's the key to globalization. Today, about a third of world trade consists of shipments between branches of multinational companies. Technological advances have expanded the global marketplace, highlighting the need for a transportation system that is international in reach. Faster and cheaper transportation systems enable multinational corporations to build facilities across the globe while maintaining scheduled deliveries.

According to the U.S. Department of Commerce, in the last 25 years, U.S. imports and exports grew from $726 billion to $2.6 trillion. The Bureau of Transportation Statistics reports that the transportation sector represents 11 percent of the overall U.S. GDP and accounts for 1 in 7 jobs in the U.S. economy.

Sales of self-driving trucks in the U.S. are forecast to reach 60,000 by 2035, estimates IHS Automotive. That would amount to 15 percent of sales for trucks in the big Class 8 weight segment. Recently, Uber acquired self-driving trucking startup Otto. Uber says they plan to put the company to work in the long-haul freight business in 2017. Otto's technology will enable existing businesses to retrofit their fleet with self-driving technology that can handle driving on U.S. highways.

Self-driving trucks can operate around the clock, enabling much faster delivery at significantly lower costs. There is also a considerable potential for autonomous trucks to increase safety and efficiency.

CONCLUSION



FREIGHT TONNAGE

Nearly 54 million tons of freight worth more than $48 billion currently moves through the U.S. transportation network each day. Freight tonnage is expected to increase by 45 percent by 2040, requiring additional capacity for highways, railroads and ports. Freight transportation is an integral part of our economy, with over 44 million jobs directly dependent on the industry. Failing to make strategic plans to improve could hurt the country's growth. Studies estimate that roadway congestion delays cost shippers approximately $10 billion each year.

In the future, two things could happen: the economy could slip back into another recession or the economy could continue its slow but gradual recovery. If the U.S. slips into a recession, even a mild one, many smaller carriers may exit the market, drivers could gravitate towards large carriers who could keep them busy and drivers could leave the industry for more profitable work. This exit from the industry could severely exacerbate the driver shortage. Capacity would become very tight and shipping costs could explode.

On the other hand, if the economy continues its recovery and there's a slight uptick in freight volume, it could still spell trouble for the over-the-road transportation industry. Capacity could reach or pass its threshold and the effect of the driver shortage would be in full swing. There could be insufficient trailer space for all the freight that needs to shipped and transportation rates could rise rapidly.

Besides, in both scenarios the average age of a truck driver is around 49. So drivers will be retiring at faster rates every year no matter what happens. Carriers anticipate difficulty, but as mentioned above, several regulations could make these looming problems even worse.

Shippers will have to be concerned with more than just price; they have to think about reliable capacity.

"Shippers can take advantage of a moderately loose trucking environment. This is mainly due to the continued weakness in economic and freight conditions, especially in manufacturing and mining. And, shippers benefit from the fuel environment, which has remained subdued, helping maintain cost reductions," says Jonathan Starks, chief operating officer at FTR. "Now, a stable pricing environment seems the most likely scenario. That means that costs won't fall significantly, but neither should fuel prices surge. Driver wages are an essential item to understand going into 2017. Shippers that understand how to utilize a driver's time best, will be able to take significant advantage of the process to help drive better rates during a time in which the market may once again see 2014-like surges in prices."

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USA Truck provides comprehensive capacity solutions to a broad and diverse customer base throughout North America. Our Trucking and USAT Logistics divisions blend an extensive portfolio of asset and asset-light services, offering a balanced approach to supply chain management including customized truckload, dedicated acontract carriage, intermodal and third-party logistics freight management services. Learn more about the Capacity Solutions from USA Truck by visiting usa-truck.com or usatlogistics.com.

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