Inside the Numbers

with Lou Smyrlis

Publisher & editorial director, *Transportation Media*

IN DEPTH ANALYSIS OF THE FACTORS AFFECTING YOUR PROFITABILITY

VOLUME 4, ISSUE 2

STARTING TO "FEEL" RIGHT

And the numbers are backing up the feeling

I'm going to do something I usually hate to do. I'm about to talk about "feelings". No, not the mushy, lovey dovey type of feelings but rather the "feelings" trucking industry stakeholders have for their prospects for the remainder of the year. Generally I'm a "show me the numbers" guy. After all, my determination to put perceived industry trends and forecasts to the test by subjecting them to objective research was the impetus behind the creation of Inside the Numbers.

But after listening to scores of industry supplier, motor carrier and shipper executives at the recent Mid America Truck Show, Truck World and CILTNA Outlook conference, it's hard to dismiss the one common thread from all these events: This is the most optimistic I've seen industry executives in five years. Even when I deliberately point that out to them, they grin and say "yeah, we are all growing more optimistic." When that many executives are feeling good, it has to count for something.

Considering the hits many balance sheets took during this very difficult winter when even ordinary deliveries sometimes required extraordinary effort, the optimism seems misplaced. So what's going on?

As I showed in the previous Inside the Numbers newsletter, motor carrier executives are growing more positive about freight volume growth. An even better sign is that the Canadian shippers participating in our research are more optimistic than the carriers about freight volume growth.

And there is more positive evidence mounting. Canadian spot market freight volumes reached an unprecedented high in March and set a new record for the first quarter. TransCore Link Logistics' Canadian Freight Index recorded a 16% increase in freight volumes over February, and a 50% increase year-over-year. The company reports its March volumes were the highest ever recorded for any month. Increases in load volumes were seen across the board, in inbound, outbound and inter-Canadian freight movements.

A recently published report on the Canadian motor carrier market, published by GE Capital, provides further evidence that things are looking up.

"Despite the soft freight trends in 2013, industry profitability remains strong," states GE Capital's *Industry Research Monitor: Canada Truck Transportation*. Its report found that in December the leading indicator of profitability for truck transportation rose to 111.57, the highest in the last three years.

GE expects to see Canadian GDP growth rise to 2% in 2014, boosted in part by stronger European demand for exports thanks to Canada's new

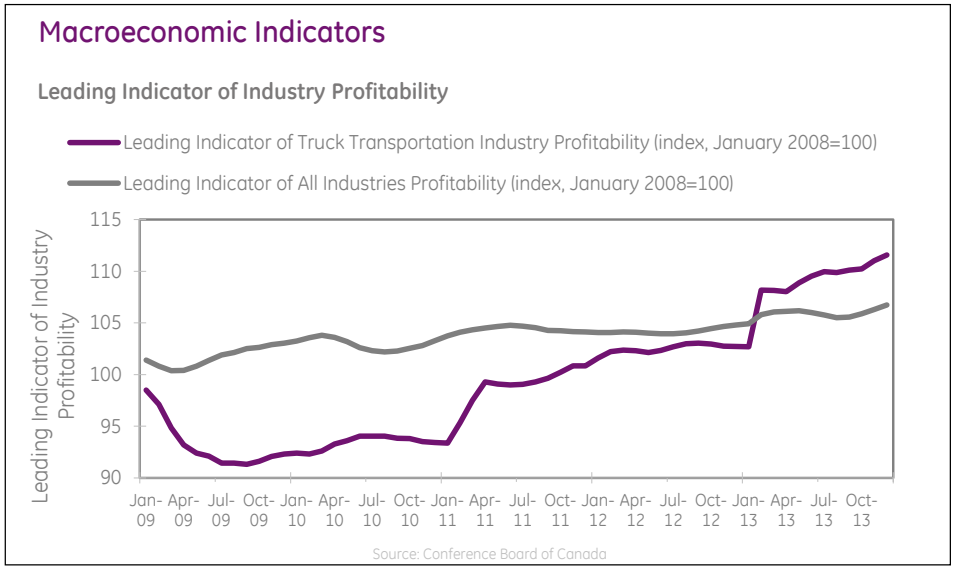
free trade agreement. The company also noted the unemployment rate is falling and the purchasing manager's index is increasing, which bodes well for freight haulers.

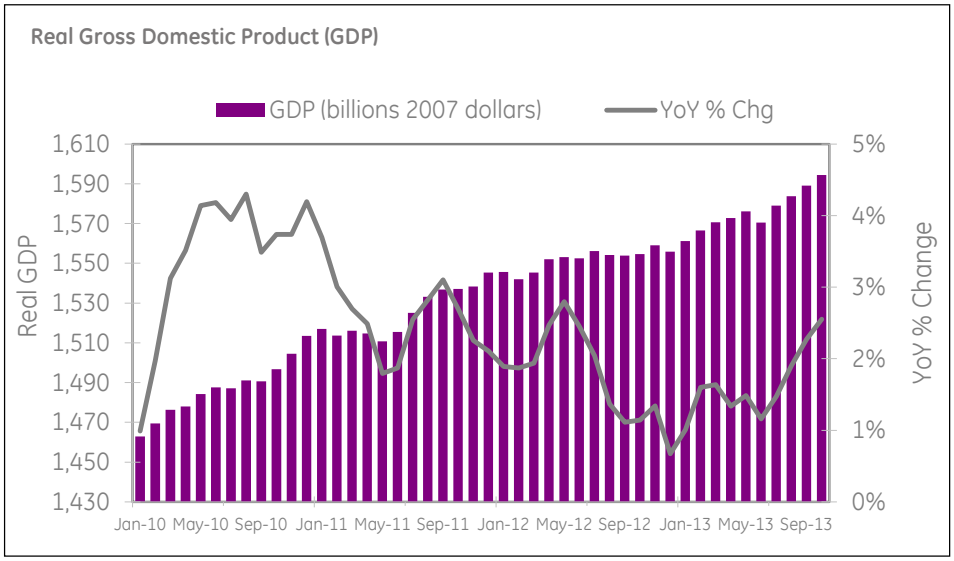
Pierre Cleroux, chief economist with Business Development Bank of Canada, was similarly optimistic about economic conditions when he recently addressed the CILTNA's Annual Transportation Outlook Conference in Montreal.

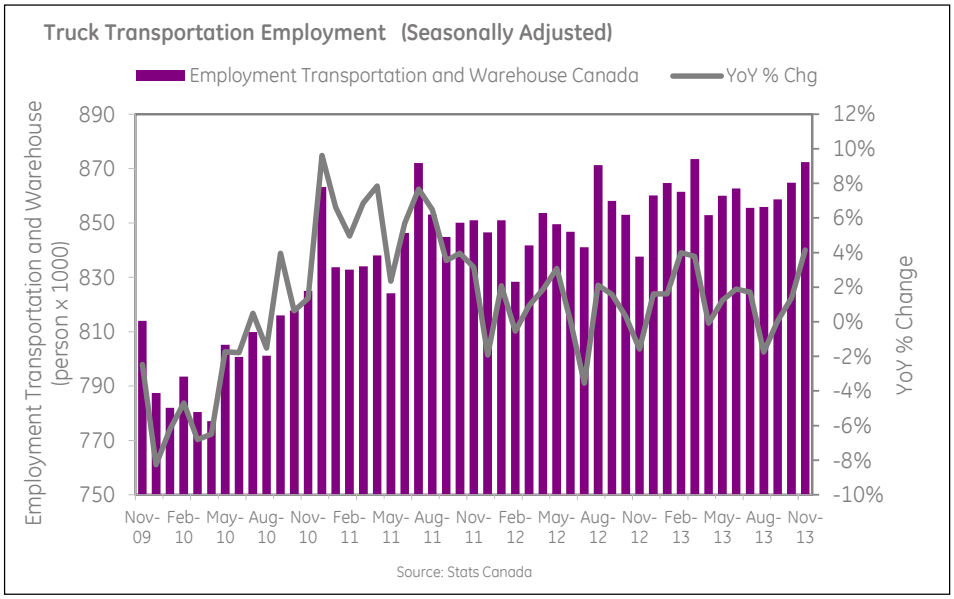
"The world economy is shifting from a post recession period to a growth period and it will be stimulated bythe US and Europe," Cleroux said, pointing out there will be positive growthat last in the European Union in 2014 and that US GDP is forecasted to grow by3%. "For Canada, this will provide more opportunities for exports.There will be robust global demand for commodities. Our ability to export will have a huge impact on our economy over the next two years."

GE also points out that truck transportation employment continued to improve through 2013. On a seasonally adjusted basis, employment increased 4% in November, reaching a peak of 872,000 from a low of 770,000 in March 2010. If carriers are hiring, they are optimistic about the future.

Even the much and long-talked about need for upward momentum on rates is showing some signs of coming to reality. GE cited a recent survey from Transport Capital Partners that indicated 66% of truckload carriers surveyed expect rates and volumes to increase over the next 12 months. Results issued by the Canadian General Freight Index (CGFI) show that the total cost of ground transportation for shippers in Canada went up by 0.75% in February from January. Since August of 2013 total freight costs have risen for the seven straight months.







Next five years will be better for tanker and refrigerated trucking industry

BY CAROLYN GRUSKE

Volatile gas prices and a slow recovery from the recent recession are just some of the factors that have caused the tank and refrigerated trucking industry to experience a decline in revenues.

A new report authored by Nick Petrillo and published by IBISWorld, entitled *Tank and Refrigeration Trucking in Canada*, finds the industry at the tail end of a recovery cycle. According to the research company, since 2009, "total industry revenue declined at an average rate of 3.8% to $9.5 billion over the five-year period, with some industry firms consolidating operations to regain a portion of the industry's slim profit margins."

But the report finds the news is not all bad. IBISWorld predicts a growth in revenues next year. In 2015, it expects revenues to rebound 3.2%, and looking further out, the forecast is also positive, as industry revenue is expected to grow "steadily in the five years to 2019. Over the five-year period, IBISWorld projects that industry revenue will increase at an annualized rate of 2.2% to $10.6 billion," mainly due to higher volumes of freight being moved during that time period.

And it won't just be revenues that will be up. Profits are also likely to rise from "4.6% of revenue in 2014 to 5.1% of the total of revenue in 2019." This increase in percentage resulted from companies being leaner as a result of cost-cutting measures implemented to deal with the recession. Now IBISWorld says these streamlined enterprises will attempt to offer more value-added services including logistics, geolocation tracking, and freight-forwarding services.

Just as companies suffered economic pressures between 2009 and 2014, so did the people employed in the industry. The report finds that "[t]otal wages…declined each year over the past five years, declining at an annualized rate of 3.8% from 2009 to 2014, further evidence of the industry's intensifying price-competition" – price-competition that has played a significant part in the recent drivers strikes and protests at Port Metro Vancouver.

But just as companies are expecting the next half-decade to be improvement over the previous one, employees and owner/operators should experience slightly better economic times as "industry wages are estimated to increase at an annualized rate of 2.1% to $2.5 billion over the five years to 2019."

IBISWorld notes that volatility in fuel prices (in particular a 30.6% spike in 2011) make it difficult for refrigerated and tanker trucking companies that "seek to charge competitive rates to customers, but must also charge rates high enough to cover a substantial portion of the fuel costs incurred through shipping operations," but adds that over the next five years, the level of volatility should decrease. The report states "the world price of crude oil is expected to stabilize, increasing slowly at an average rate of 0.2%, while total retail sales are expected to increase at a strong 3.8% annual rate over the five years to 2019. Industry operators will likely continue to levy fuel surcharges to recover a portion of profit margins lost from changes in the price of diesel fuel. This will generate additional revenue, although price competition among firms will continue to restrict the additional revenue generated from surcharges."

Although IBISWorld found there was a tiny bit of consolidation in the market over the past five years, the industry has yet to be dominated by any major players. According to its figures, TransForce Inc. has 5.7% of the market share, followed by TransX Group of Companies with an estimated 1.8% and Mullen Group with less than 1% of the market.

Playing to win in the rate increase game


PRIES


JONES


ARMOUR

Although the North American economic outlook is solidifying, and carriers are keen to return to more profitable rate structures, shippers remain vigilant about cost increases. Three motor carrier executives – all members of the prestigious list of Canada's Best Managed Companies – weigh in on how to provide cost-effective solutions for shippers that also represent a fair return for the carrier.

Jeff Pries, senior vice president, sales & marketing: No question, shippers are very cost conscious. Cost matters but most customers are interested in their carrier making a profit. They understand that if the carrier is not making a profit that is not a sustainable situation. Our experience recently is that we have been able to demonstrate to our customers that in many cases our costs are on the rise – driver pay, fuel, equipment. We are working with our customers to either drive costs down or raise revenue quality. We strive to provide options for customers in a collaborative way. We look at variables such as day of week shifting, ease of loading and unloading, days on trailer, and so on. Those are ways to mitigate price increases. Today's pricing structure for most trucking companies is much different than it was 10-15 years ago when the focus was on the base rate. There are many accessorials that need to be looked at now. It's not always about the base rate.

Mike Jones, vice president operations, TransX: I think there are three main keys that provide for a win-win relationship in the business, not only with retail, but with the manufacturing core that supplies the finished goods to the retailers. The first key is to listen and really understand what it is that they need. Of course, everyone wants lower rates; but behind the lower rates, is the attention and consideration to the levels of capacity, service and complexity that must support getting their product to market, on time, and in the right condition. You can't do this without the second key, which is achieving and maintaining a great relationship with the companies to whom you provide these services. The last key is execution; if you can't execute, all the rest of it is a waste of time.

Wes Armour, president and CEO Armour Transportation Systems: The reality is that we are living in a tough economy right now in Atlantic Canada. Transportation companies in general are operating "lean and mean".

Severe weather during the first quarter of 2014 caused our supply chains to be even more disrupted. Snow, sleet, freezing rain and extremely cold temperatures repeatedly disrupted normal manufacturing, distribution and transportation patterns. This winter was very costly to our industry, but volumes have remained steady with some increase with new customers.

The encouraging news is the economy is growing slowly and steadily. Overall, 2014 is expected to be a better year for carriers, but not the year that marks the start of a great economic upturn.

While getting our rates back in line with an improving economy is a true focus of ours, we are also concerned about keeping our costs in line. Therefore, we continue to look at everything we do with a lean eye. Our operational costs are constantly rising with respect to parts, tires, fuel, equipment and the low value of the Canadian dollar. This all adds up to a great deal more to operate a truck today than it did 3-5 years ago.

In the area of cost reduction, we are reducing line haul costs by using short-sea shipping, intermodal and Longer Combination Vehicles (LCVs). We also continue to upgrade our fleet with new fuel efficient and reliable trucks.

I believe these operational efficiencies help to keep us on a level playing ground with shippers and move us forward in terms of eliminating waste from our processes, improving our performance and productivity, while creating value for our customers.

We are continually looking for ways to do things smarter in all aspects of our organization.

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Looking to Grow?

It may be time to consider some new business models for courier & LTL freight

BY DAN GOODWILL

Two developments over the past five years have reshaped the Canadian freight industry. The Great Recession in the late 2000s caused many Canadian trucking companies to shrink in size or leave the freight industry. During the past couple of years, there has been considerable consolidation in the small parcel, domestic LTL over the road and Intermodal segments of the Canadian freight industry. Shippers looking for a national courier or LTL carrier now see many familiar brands in the hands of a small group of companies.

Shippers worrying about whether there will be full and fair competition in the Canadian freight industry in the years ahead can take solace from what is happening south of the border. Our American friends experienced the same economic downturn in 2007. Some experts believe that as much as 15% of the freight capacity in the United States left the market during the Great Recession.

The good news is that as this capacity left the market, several emerging trends suggest that new strategies and business models are providing increased competition in the LTL sector.

Build a Carrier Partnership Network

Some significant carrier partnerships and alliances have been formed to provide more competition on the national and regional level. In an effort to compete with the national LTL players (e.g. YRCW, FedEx Freight, Old Dominion etc.), The Reliance Network was formed. It brings together:

Averitt Express and its core network of 13 Southern states.
Canadian Freightways and Kingsway that cover Canada.
Lakeville Motor Express services the Midwestern US states.
Land Air Express covers New England and upstate New York.
Mountain Valley Express services the Pacific Southwest
Peninsula Truck Lines services over 950 cities and towns throughout the Northwest United States.
Pitt Ohio is the LTL partner that services the mid-Atlantic states.

For regional Canadian LTL carriers seeking to provide both intra, inter-provincial and cross-Canada LTL service, this is one model to follow. There are a number of quality asset-based regional Canadian LTL carriers that could form alliances to provide another national or super-regional LTL network.

Grow your business with an Asset-Light Model

In recent years there are several "asset-light" LTL carriers that have emerged in the United States to provide another level of competition on a super-regional or national basis. Three companies to examine are Roadrunner Freight Systems (www.rrts.com), Shift Freight (shiftfreight.com) and Daylight Transportation (www.dylt.com). In each case the company has combined some its own assets with its partners' assets and linked them together on an integrated IT platform to offer a complete LTL service within their respective geographic networks. This is similar to what was done in Canada years ago as new domestic LTL intermodal operators created service networks by renting terminals on rail lines in major Canadian cities, integrated them by using local cartage companies in each market to do the local P and D and the rail lines to provide long haul transportation. These American companies have come up with a modified version of this model in their service areas.

Use a Non-Asset-Based Model

A third approach is to provide national or regional LTL service on a totally non-asset-basis. There are various models that can be looked at. The LTL and Intermodal markets have been growth sectors for freight brokers and freight management companies in recent years. Surveys have shown that the LSP share of the LTL freight industry has been growing. Then there are the web portal players that allow shippers to log in, enter their origin and destination points and let the technology (and the carriers backing them up) provide the required service.

Canada is a large country in terms of geography with a small population. It is very costly to build or buy a truly national asset-based small parcel, LTL over the road or intermodal terminal network. But as many name-brand players are acquired by the industry giants, this creates an opportunity for entrepreneurs with vision, determination and the business skills to take one or more of these business models and apply them to the Canadian freight market.

Dan Goodwill, president of Dan Goodwill and Associates has more than 20 years of experience in the logistics and transportation industries in both Canada and the US. He has held several executive level positions in the industry. He can be reached at dan@dantranscon.com.

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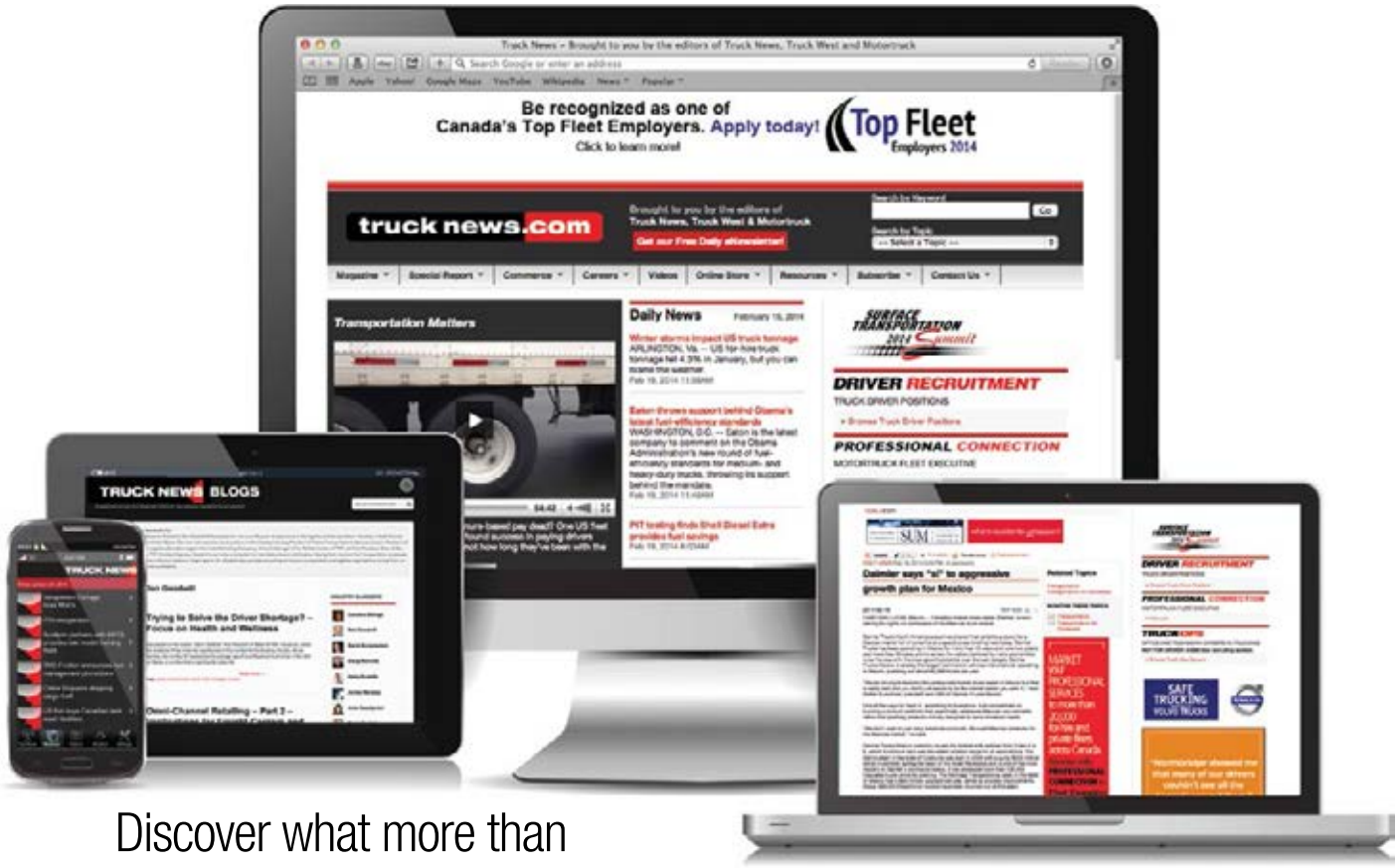

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Canadian spot market freight volumes surge in March

Canadian spot market freight volumes reached an unprecedented high in March and set a new record for the first quarter.

TransCore Link Logistics' Canadian Freight Index recorded a 16% increase in freight volumes over February, and a 50% increase year-over-year. The company reports its March volumes were the highest ever recorded for any month.

The first quarter results were up 52% compared to Q1 2013 and 51% higher than Q4 2013 volumes. Meanwhile, equipment postings for the first quarter were the lowest seen since 2005. Posted trucks ewre down 18% compared to Q1 2013. TransCore's truck-to-load ratio for March represented the tightest capacity on record.

TransCore indicates increases in load volumes were seen across the board, in inbound, outbound and inter-Canadian freight movements.

Cross-border postings accounted for 71% of total load volumes. Loads from Canada into the US surged 92% year-over-year, while loads originating in the US destined for Canada were up 42% y-o-y.

CGFI research shows freight costs, fuel surcharges on the rise

Results issued by the Canadian General Freight Index (CGFI) show that the total cost of ground transportation for shippers in Canada went up by 0.75 % in February from January.

Average fuel surcharges also increased. Fuel was 20.86% of base rates in January compared to 21.78% in February.

"Since August of 2013 total freight costs have risen for the seventh straight month. Fuel is also on the rise." said Doug Payne, President & COO, Nulogx. "Fuel has now risen to the March/April levels of 2013."

US truck tonnage climbs slightly in March

US for-hire truck tonnage inched up 0.6% in March, on the heels of a 1.9% gain in February, which was less than the 2.8% growth originally reported.

The American Trucking Associations For-Hire Truck Tonnage Index read 127.3 in March. The all-time high of 131 was recorded in November 2013.

March tonnage was up 3.1% year-over-year, representing the largest y-o-y gain of 2014.

Tonnage for the first quarter was down 2.5% compared to the previous quarter, representing the worst quarterly decline since the economic recovery began, ATA reports. However, compared to Q1 2013, tonnage was up 2.3%.

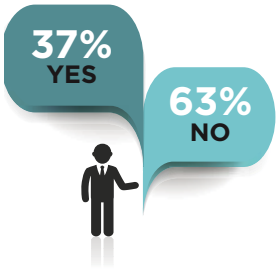
"Tonnage continued to claw its way out of the hole that was dug in December and January," said ATA chief economist Bob Costello. "However, with a cumulative gain of 2.5% during the last two months, we still have a way to go to offset the total loss of 5.2% in December and January. Despite the fact that tonnage hasn't snapped back to the levels we saw late last year, the fundamentals for truck freight continue to look good.

"While it will take time to regain what was lost due to weather and other factors, like a potential inventory correction in the first quarter, I remain optimistic for 2014; however, don't expect a 6.3% annual gain in truck tonnage like during 2013."

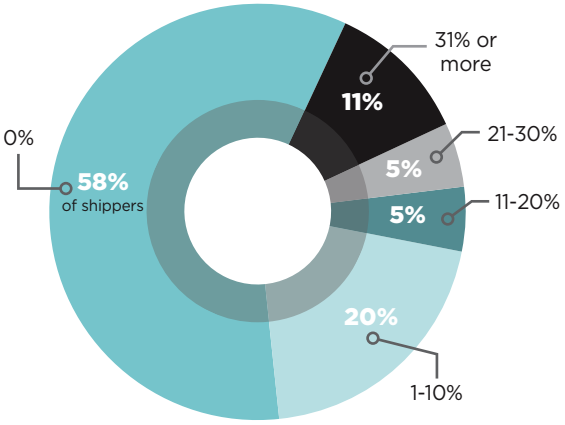
WHY CANADIAN SHIPPERS MODE SHIFT

Is there a ceiling to how high surface transportation rates can rise? Our annual Transportation Buying Trends research, conducted in partnership with FMAC and CITT, shows that there is. More than a third of Canadian shippers responding to our survey noted higher prices and/or surcharges have caused a change in their modal selection for at least some of their shipments. Increasing truck prices are the main reason shippers will switch from truck to rail, with almost 40% noting that as their reason for a modal switch. Conversely, when Canadian shippers shift from rail to truck it's primarily due to service issues with the majority (35%) blaming poor rail service or coverage, followed by almost a quarter who do so in response to customer requests.

Higher rates and/or surcharges have affected modal selection



Percentage of current rail shipments for which Canadian shippers consider trucking a viable alternative?



Main reasons Canadian shippers divert freight from rail to truck

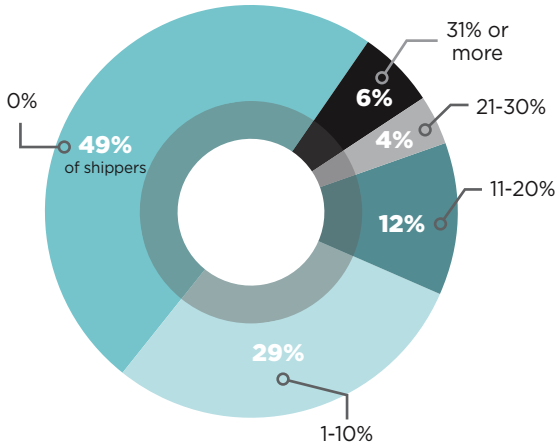
To service new markets	2% of shippers
Decreasing truck prices	2%
Responding to customer requests	23%
Increasing rail prices	12%
Faster inventory times	19%
Poor rail service or coverage	35%

GETTING REAL ON RATES

Main reasons Canadian shippers divert freight from truck to rail

10%	To service new markets
10%	Responding to customer requests
38%	Increasing truck prices
10%	Decreasing rail prices
0%	Faster inventory times
25%	Poor truck service or coverage

Percentage of current trucking shipments for which Canadian shippers consider rail a viable alternative



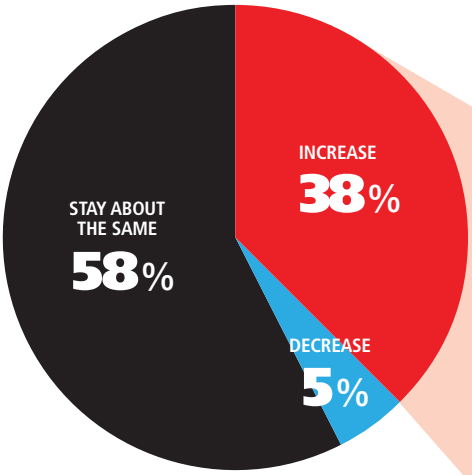
GROWING OPTIMISM

Canadian carriers on freight volumes and rates in 2014

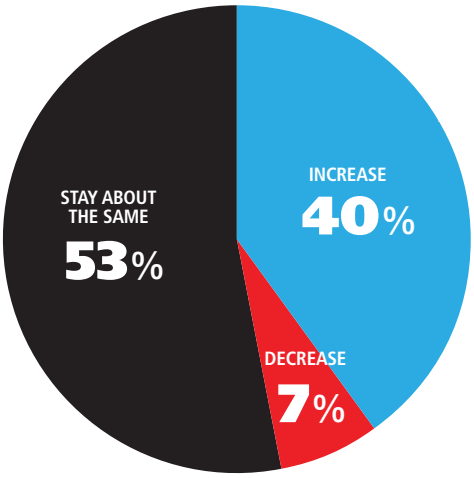
Carriers across the country are growing more optimistic about freight volume growth. Overall, 40% of Canadian motor carriers expect an increase in 2014, according to our annual Transportation Buying Trends Survey. The optimism for freight volumes is highest in Western Canada where 48% of carrier executives indicated they expect an increase this year. Despite the expected increase in freight volumes, however, only 38% of Canadian fleet executives expect to push through an increase in core rate pricing this year. The majority expect an in increase in the range of 2.1-4%. In addition 41% expect fuel surcharges to rise in 2014. Our Transportation Buying Trends Surveys have been published for a decade and are conducted in partnership with the Freight Management Association of Canada, Cormark Securities and CITT.

All charts are a percentage of respondents.

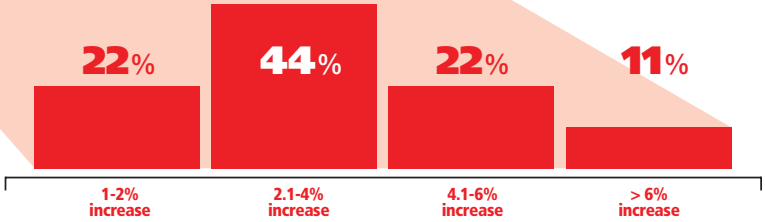
Carrier expectations for direction of core rate pricing in 2014



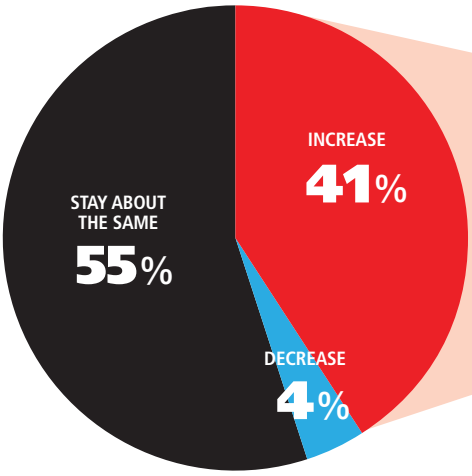
Carrier expectations for freight volumes in 2014



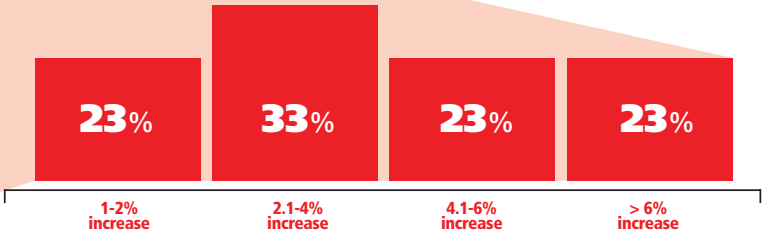
Carrier core rate pricing increase projections for 2014



Carrier expectations for direction of fuel surcharges in 2014



Carrier fuel surcharge pricing increase projections for 2014

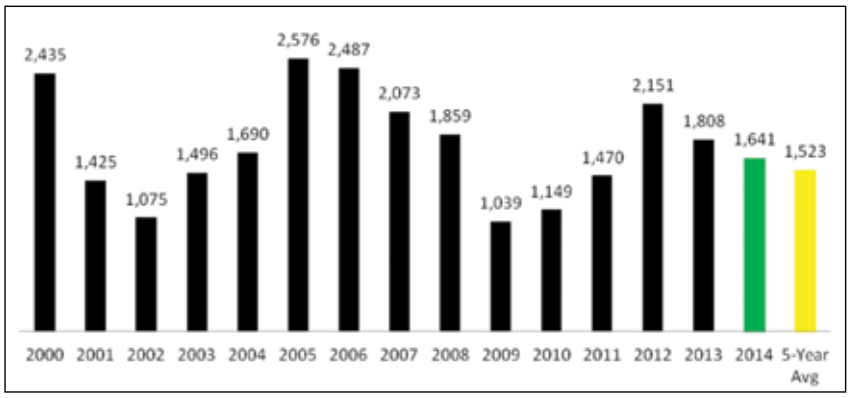


CLASS 8 Truck Sales Trends

Monthly Class 8 Sales – Feb 14

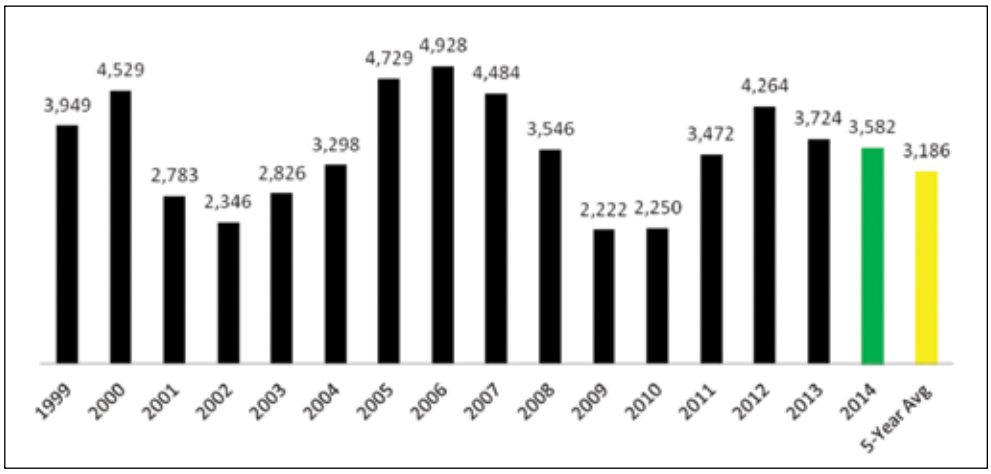
OEM	This Month	Last Year
Freightliner	347	458
International	159	250
Kenworth	316	360
Mack	146	120
Peterbilt	301	256
Volvo	231	219
Western Star	141	145
TOTALS	1641	1808

Historical Comparison – Feb 14 Sales



Class 8 truck sales started the year on a mildly positive note, surpassing last year's January totals, but February's numbers are disappointing. Not only does February represent the second consecutive month with sales below the 2,000 mark, after 10 straight months of being above it, but the month's total is short of last year's mark. Last year's market leaders Freightliner, Kenworth and International all suffered setbacks in February, falling behind last year's totals.

Historical Comparison – YTD Feb 14



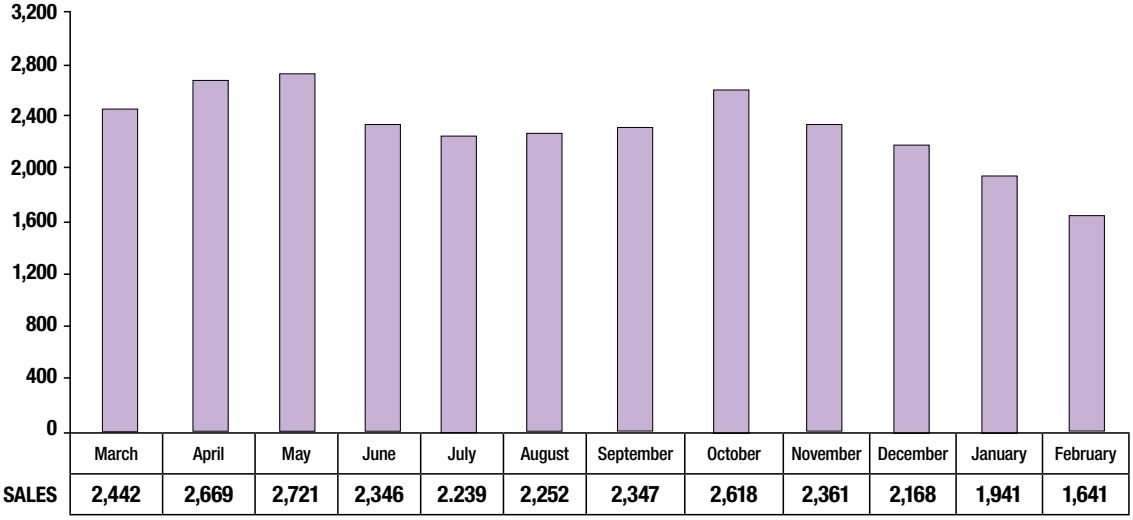
Class 8 Sales (YTD Feb 14) by Province and OEM

OEM	BC	ALTA	SASK	MAN	ONT	QUE	NB	NS	PEI	NF	CDA
Freightliner	70	135	28	30	335	165	31	8	0	0	802
Kenworth	97	287	44	1	89	83	7	0	0	0	608
Mack	26	41	21	18	118	28	3	6	0	2	263
International	17	97	13	19	244	120	28	6	3	7	554
Peterbilt	87	185	48	18	109	79	22	3	0	0	551
Volvo	63	79	14	27	183	66	17	6	0	0	455
Western Star	64	171	14	6	42	38	4	9	0	1	349
TOTALS	424	995	182	119	1,120	579	112	38	3	10	3,582

This was the eighth best February total since 1999. Monthly sales were about 400 units above the five-year average. There is optimism for an improvement in Class 8 truck sales in 2014 after 2013 proved a disappointing year but so far the Canadian market is not reflecting that optimism. The big question is whether Canada's many small fleets are ready to buy new again. Our research shows large and medium-sized carriers are in a buying mood but small carriers are not.

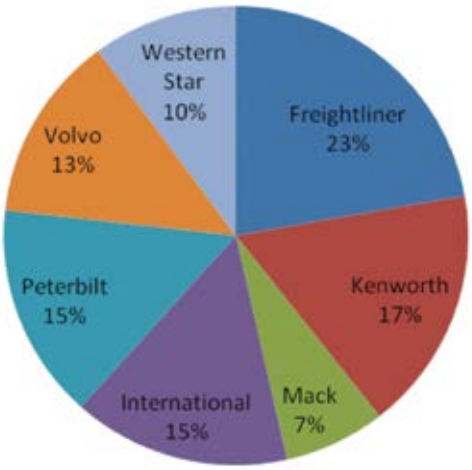
CLASS 8 Truck Sales Trends

12-Month Sales Trends



After 10 straight months of sales coming in above the 2,000 mark, reminiscent of the industry's capacity boom years of 2005 to 2007, they dropped slightly below 2,000 in January and considerably further in February. Yet with the US economy regaining its stride and the value of the Canadian dollar dropping against the US dollar, economic forecasters anticipate exports will lead the Canadian economy in 2014. That may spark increased truck sales as trucking will be the main beneficiary of improved business volumes with the US.

Market Share Class 8 – Feb 14 YTD



Freightliner, last year's Canadian market leader, has started off with a bit of a drop in market share but remains strong enough to have a controllling lead. Kenworth finished 2013 in the number two spot for market share, enjoying the fact that its strong western network is able to tap into the stronger western economy. But the company has also faltered in January and February and currently sits with 17% market share, followed by International and Petebilt, both at 15% of the market after two months.

Source: Canadian Motor Vehicle Manufacturers Association