December 18, 2019 | 12:42 PM EST

Intermodal Markets

Overview

The rails are pulling all available levers to make the low-volume, low-revenue 2019 story look as good as it can: they've improved service metrics like train velocity and terminal dwell times across the board, and most have cut headcount by double-digit percentages year-over-year. Union Pacific made the deepest cuts to its workforce, which has shrunk by 16.7% compared to the same month last year, or more than 7,400 employees.

We're starting to see green shoots in intermodal markets that could signal that a recovery is on the way for railroads and IMCs.

Intermodal volumes were down 8% year-over-year last week among the Class I railroads, significantly better than last week's -11.3% number. Tender rejections rose in Savannah and Los Angeles as capacity in those major origins tightened. Among the densest lanes, a few lanes into Chicago and from Chicago to the New York City market actually saw rates go up compared to last week.

We think about the intermodal market in relation to trucking: intermodal typically sees a delayed and diluted knock-on effect from whatever is happening in the truckload spot and then truckload contract markets. Shippers rotate in and out of modes based on price, available capacity and service levels. In the current market, certain intermodal lanes are regaining the ability to take price (we note that trucking capacity has tightened in the same markets where the rails are hiking rates).

The positive read-through from trucking should be limited through January unless the U.S. gets an economic or trade surprise to the upside.

Spot rates per mile

Chicago to Linden, NJ	$1.88
Los Angeles to Dallas	$1.56
Linden, NJ to Chicago	$1.20
Los Angeles to Chicago	$1.18
Chicago to Los Angeles	$0.92

53-foot container volume seven-day MA (weekly change)

Los Angeles to Chicago	1063.29 (-5.83%)
Chicago to Los Angeles	792.86 (-3.75%)
Chicago to Elizabeth, NJ	677.14 (+2.60%)
Los Angeles to Dallas	419.57 (-3.52%)
Elizabeth, NJ to Chicago	379.43 (-7.13%)

Outbound intermodal tender rejections

Savannah, GA	2.38%
Joliet, IL	0.00%
Chicago	0.00%
Memphis, TN	0.00%
Los Angeles	1.20%

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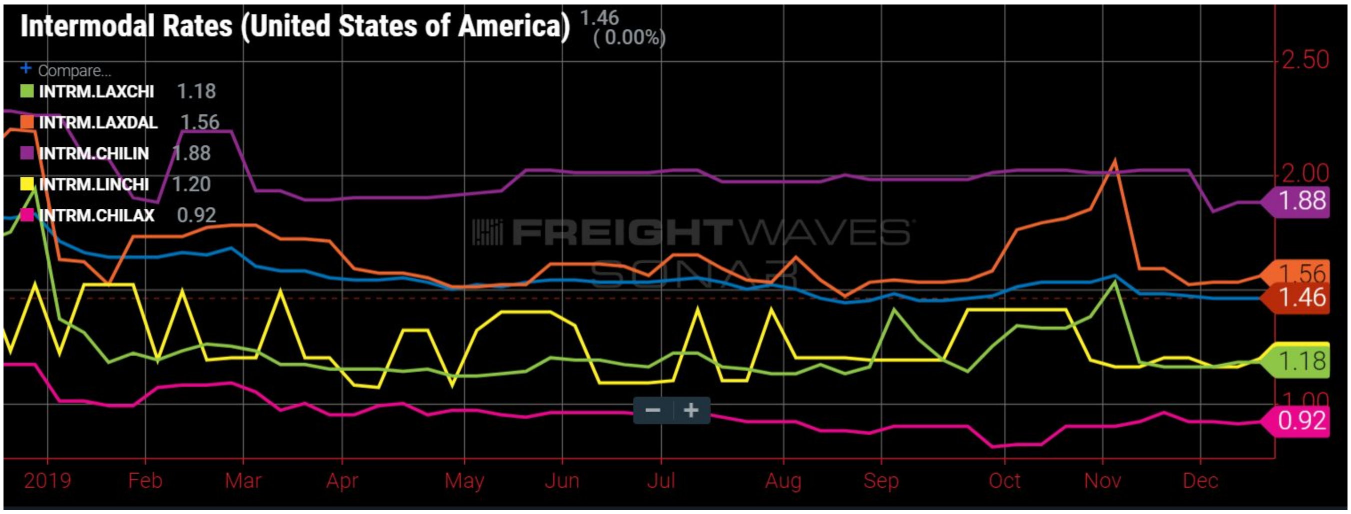
Intermodal spot rates



(Chart: FreightWaves SONAR)

Intermodal rates continue to walk along the x-axis. This has essentially been the case throughout the year. Overall, four major lanes' rates remained the same. The three major lanes that saw movement in rates are: Chicago-Los Angeles (+1.1%), Los Angeles-Dallas (+2.0%), and Linden-Chicago (+3.4%).

We have not changed our base-case thesis that rates will likely remain steady with a bias toward upward movement. This is due to our belief that railroads will attempt to narrow the gap in rates between rail and truck.

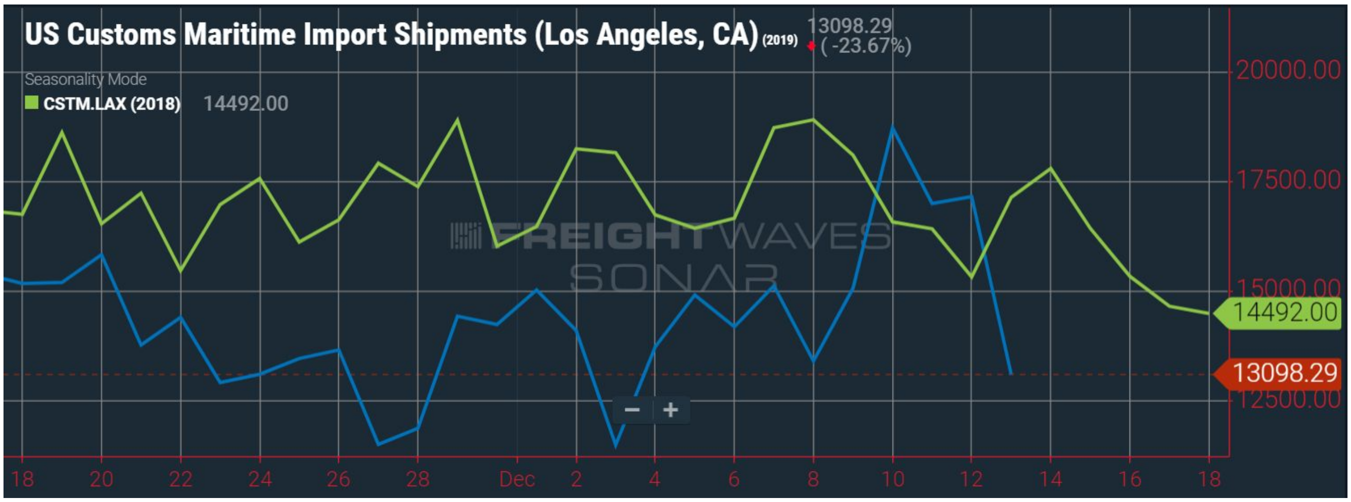
"One of the major themes in the railroad industry in 2019 has been the unusually high degree of competition from trucks; that's due to a combination of a weak truck market and ever-rising railroad rates," wrote FreightWaves intermodal expert Michael Baudendistel in a December 16 customer note.

Railroads are responding to this renewed competition by trying to improve service. Recently, train velocity has been trending upward; terminal dwell times have contracted for most of the year. The true test will be when railroads start increasing volume, which will likely occur only when industrial production in the United States fully recovers.

Freight demand

Intermodal volumes are still negative compared to last year, but are inflecting upward against 2018 comps, at least compared to where they were last week. U.S. Class I intermodal volumes were down 8.0% last week Y/Y, slightly better than last week's comparison, which saw intermodal units down 11.30% Y/Y. As we noted last week, it is unlikely that comps get much better going into the year as there was a surge in volumes late last year due to the pull-forward of freight volumes ahead of tariffs. We mentioned previously a potential increase in volumes ahead of this year's Dec. 15 tariff in our weekly trucking report. We have not seen a substantial increase in import data.

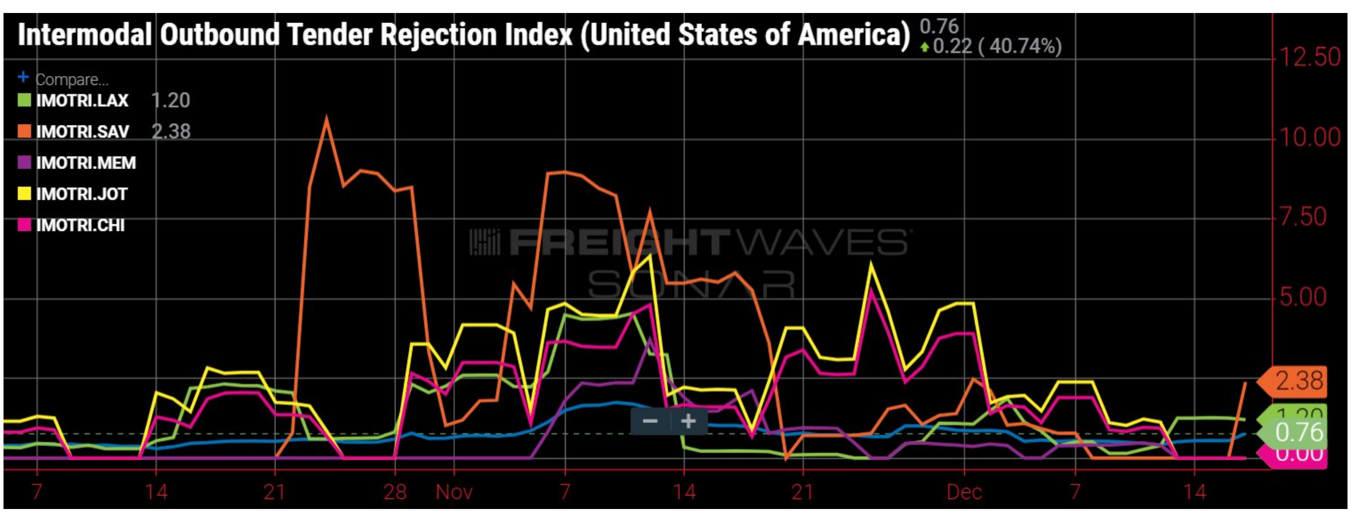
The railroad that saw the biggest year-over-year drop in weekly intermodal volume was once again Union Pacific, with a decline of 14.0% Y/Y. As seen in U.S. customs data, maritime imports into the Los Angeles market have consistently been below last year's levels.



(Chart: FreightWaves SONAR)

Los Angeles is the most important intermodal origin in the Union Pacific network. Based on the plunging customs volumes, we are not surprised that Union Pacific suffered a more severe decline in intermodal volumes relative to other railroads. We expect that Union Pacific will continue to manage through tough comps into the end of the year.

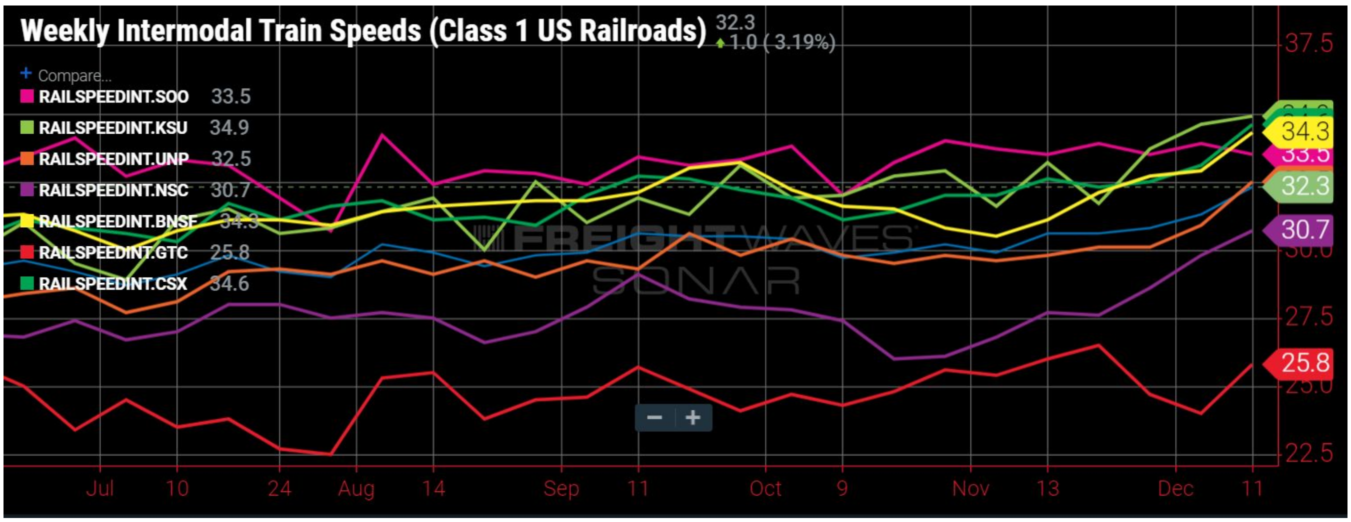
Intermodal capacity



(Chart: FreightWaves SONAR)

Intermodal capacity remains extremely loose heading to the end of the holiday season. Intermodal Outbound Tender Rejections (IMOTRI.x) measure contracted loads rejected by IMCs. IMOTRI has stayed stable right around 1%, showing that railroads are not willing to turn away any of the contracted loads. Over the past week, national intermodal rejections have climbed over 50% from

0.49 to 0.76. Two important markets tightened slightly: Savannah, GA and Los Angeles, CA. In Los Angeles, intermodal tender rejections rose 106 basis points from 0.14% to 1.20%. Savannah, which tightened more than any other intermodal market, went from zero to 2.38%. Intermodal shippers will start to see a rebound in rejections as truckload turndowns have climbed to their highest point in more than 10 months. If trucking rates climb as a result of the higher rejections, intermodal will have a chance to capitalize in Q1 2020.



(Chart: FreightWaves SONAR)

Intermodal Railroad Speeds (RAILSPEEDINT.x) is the average speed at which an intermodal train moves across the railroad's network. The data point is a service metric that the railroads are trying to improve with the implementation of precision scheduled railroading (PSR). The higher the rail speed, the faster assets are moving across the network, thus the better – and more 'truck-like' – service that the rails are providing to their customers.

The average speed across all Class I intermodal traffic increased by 3.19%, from 31.3 mph to 32.3 mph. Faster trains shows that the implementation of PSR is making the rails more efficient across all Class I railroads, at least during a low-volume environment. All of the Class I railroads moved their trains faster over the past week, except for Canadian Pacific. Canadian National has the most improvement to make in train speeds; it's the only railroad that has a weekly average speed under 30 mph. Ultimately, as long as railroads continue to make improvements to their service, either by terminal dwell times or rail speeds, their offering will be more attractive to customers and they will again be able to compete with the highway.