

Q4 2019 FREIGHT BROKER OUTLOOK: WHERE ARE WE IN THE FREIGHT CYCLE?

NOVEMBER 2019

FREIGHTWAVES FREIGHTINTEL RESEARCH






Key Highlights

- The freight recession of 2019 may have ended on July 24, when tendered load volumes (OTVI.USA) surpassed 2018 volumes for the first time. OTVI.USA remained above 2018 throughout the third quarter of 2019, ending on Sept. 30 up 7.14% year-over-year.

Figure 1 – Key Metrics for the 2019 Truckload Market

| Metric |  | Q1 2019 | Q2 2019 | Q3 2019 |
|--|---|---------|---------|---------|
| Tendered Load Volumes (OTVI.USA) y/y | | -0.5% | -5.7% | 7.1% |
| Tender Rejections (OTRI.USA) y/y | | -78% | -79% | -70% |
| DAT Spot Rates (DATVF.VNU) y/y | | -22% | -28% | -18% |
| Carrier Sentiment for Load Volumes % Change | | -22% | -5% | 34% |
| Carrier Sentiment for Line-Haul Rates % Change | | -23% | -21% | 105% |

*y/y is year-over-year

*Carrier Sentiment is % change from previous Quarter

Source: SONAR - OTVI.USA, OTRI.USA, FreightWaves Carrier Outlook Survey October 2019

- Truck capacity remained very loose in the third quarter as outbound tender rejections (OTRI.USA) remained in the 5% to 6% range. These levels were dramatically below tender rejections seen throughout 2018. OTRI.USA comparables should continue to be tough until the first quarter of 2019, when tender rejections were cut by almost two-thirds from 14.1% to 5.6%.
- DAT national dry van spot rates (DATVF.VNU) have recovered from second-quarter lows of \$1.28, though only marginally. At the end of the third quarter, this index of spot rates had only climbed up to \$1.43 per mile. These levels are still in the range of operating costs per mile for carriers and are in the range of a natural trough for line-haul rates.
- Paper (contract) rates continue to slide throughout 2019. The Producer Price Index for long-haul trucking (PPI.LDTL) posted its first year-over-year decline in paper rates in the third quarter. Indexes from Susquehanna Financial Group and Morgan Stanley also showed negative year-over-year paper rate renewals. And C.H. Robinson disclosed it is seeing severe downward pressure on contract renegotiations for 2020, running in the negative 12% range year-over-year.



- Carrier sentiment for loads and volumes over the next six months, which had been in a free fall for most of 2019, did receive a much-needed bounce. This is especially true for line-haul rates as positive sentiment more than doubled from our second-quarter survey. Now 42% of carriers have a positive outlook on line-haul rates going forward.¹

FreightWaves Freight Intel Contacts

Kevin Hill, Director of Research

(646) 731-4735, khill@freightwaves.com

Seth Holm, Senior Research Analyst

(404) 840-2064, sholm@freightwaves.com

Andrew Cox, Research Analyst

(615) 495-4507, acox@freightwaves.com

Alexandria Quevedo, Market Expert

(910) 783-4188, aquevedo@freightwaves.com

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¹ Q4 Carrier Outlook: Is this an end to the freight recession? can be accessed in the Research tab within SONAR.



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Where Are We in the Freight Brokerage Cycle?

The relationship between gross revenue and gross margins for freight brokerages are inversely related across much of the freight cycle. As spot market rates rise faster than paper (contract) rates, margins compress on higher load volumes. The opposite is true as spot rates fall faster than paper rates are rebid down as gross margins expand on flat and/or lower load volumes.

It is all part of the cyclical nature of supply and demand in trucking.

In our October white paper “Freight Broker Performance Across the Cycle,”² we examined this topic in detail. Part of our reference material was an excellent chart produced by Echo Global Logistics summarizing supply and demand in each part of the freight cycle.

According to Echo’s chart of freight cycles in Figure 2 below, we believe freight brokerages are in Stage C. This stage is the trough of the cycle, in which load volumes are flat or declining, spot rates have already fallen to their lows and paper rates are being rebid down by shippers to reflect the new macro environment for the freight market.

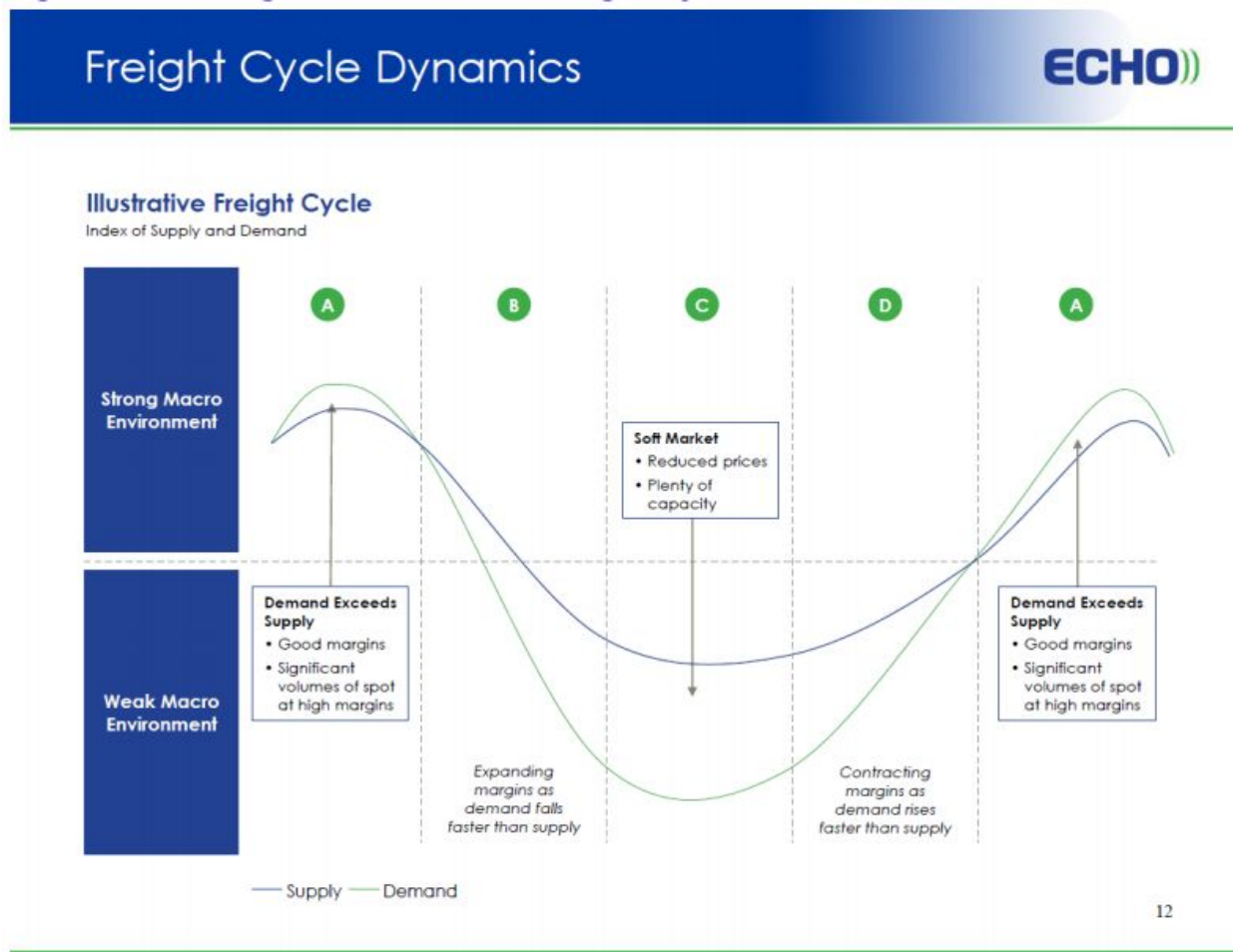
While no one can predict when the freight market will enter Stage D, we can identify its markers. The transition to the next stage should include spot rates rising as shippers continue to either rebid current paper rates and/or move more loads into the spot market to take advantage of lower rates in the spot market.

This movement of loads into the spot market will increase demand and spot rates as paper rates find a bottom. This movement of paper vs. spot rates will continue to compress gross margins until demand and supply are relatively even again.

² Freight Broker Performance Across the Cycle can be accessed in the Research tab within SONAR.



Figure 2 – ECHO’s Four Stages of a Freight Cycle



Source: Echo Investor Relations

Gross Margins - Theory vs. Practice

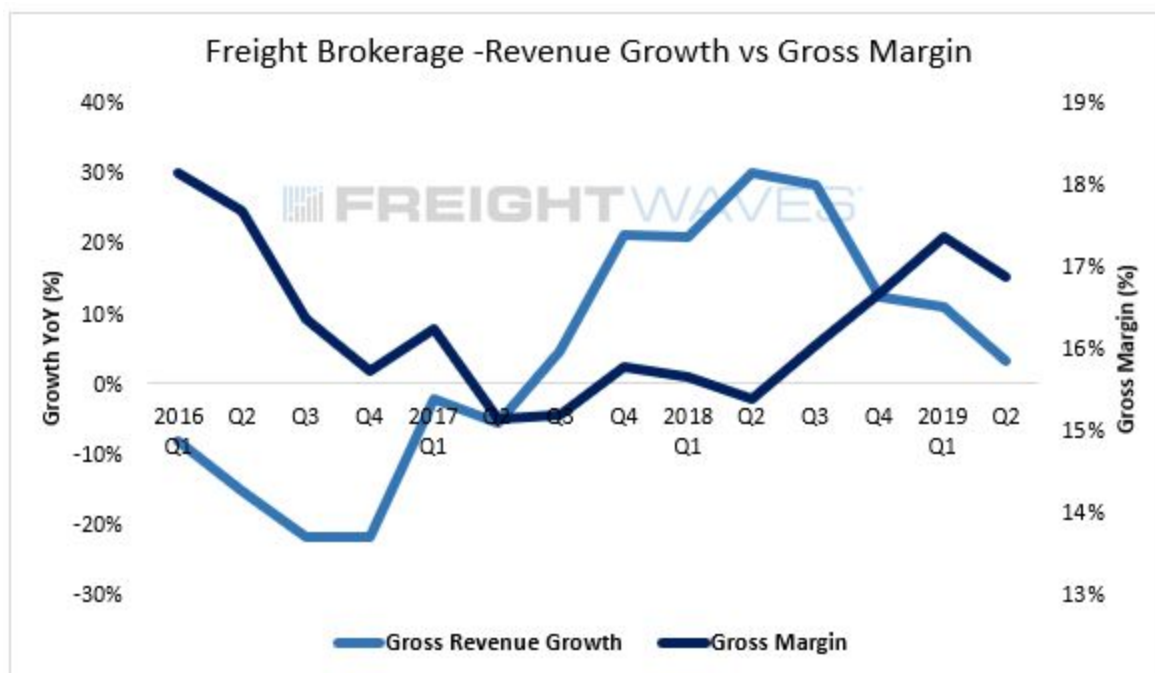
The stages of the freight cycle from Echo in Figure 2 is great in theory, but how well does it describe the real world?

Figure 3 below is a chart of gross revenues and gross margins as measured by the top five publicly traded freight brokers (CHRW, JBH, ECHO, LSTR, XPO). As one can see, gross revenues peaked in the second quarter of 2018. During this time, gross margins were contracting as spot rates rose much faster than paper rates could be rebid higher by freight brokerages. This is consistent with Stage A in the Echo model when demand outstrips supply. Margins contract on higher gross revenue and load volumes.



In the second half of 2018, gross revenues fell along with spot rates and load volumes. During this time though, gross margins expanded as spot rates began to fall even as paper rates were still being rebid higher to reflect the volatility in rates seen in the first half of 2018. This correlates quite nicely with Echo’s Stage B in the freight cycle.

Figure 3 – Public Freight Brokerages’ Gross Revenues and Margin Across the Freight Cycle



Source: FreightWaves White Paper - Freight Broker Performance Across the Cycle October 2019

The first half of 2019 has been stuck in Stage C of the freight cycle. Gross revenue, gross margin, as well as load volumes, have been on the decline. Spot rates have declined and are still holding flat, while paper rates have been under rebidding pressure by shippers that are actively clawing back rate increases given up at the height of the 2018 capacity crunch.

The next stage in the cycle should see more shippers moving loads into the spot market to cash in on lower spot rates as they continue to rebid paper rates lower. This will move freight brokerages into the most difficult part of the cycle in which gross revenues and gross margins contract as spot rates begin to climb, even as paper rates continue to be rebid down. On the bright side, load volumes should increase as another cycle begins in the freight markets.



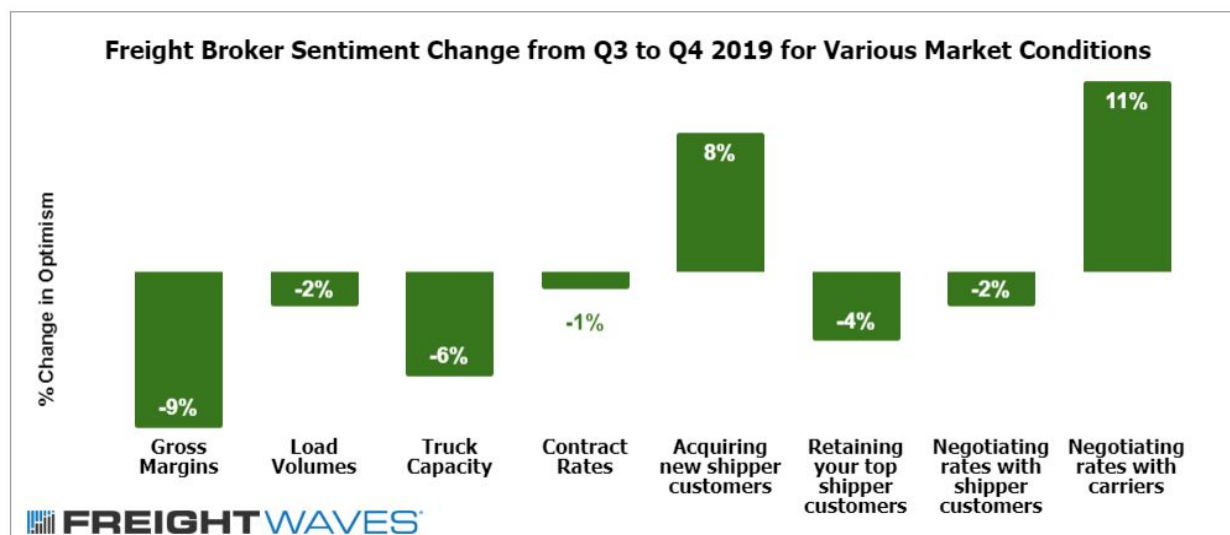
Fourth Quarter 2019 Freight Brokerage Outlook Survey Results

In early November, FreightWaves surveyed 405 freight brokers via email to get a sense of their expectations for several freight market indicators for the next three to six months.

This is the second quarterly survey of brokers. The first survey was conducted in August and included 160 respondents.

Figure 4 below represents the change in optimism between the third-quarter and fourth-quarter surveys for the expectations of a series of market conditions. Figure 5 shows the changes in optimism along with negative and neutral sentiment.

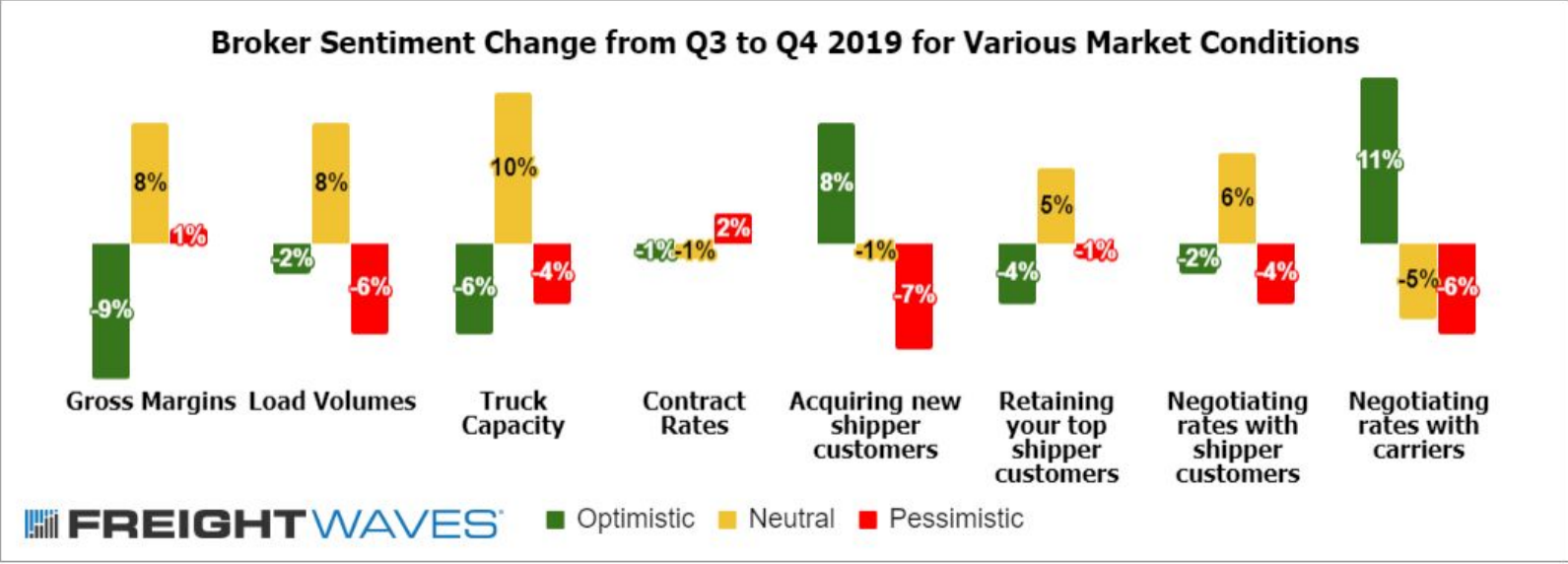
Figure 4 – Freight Broker Change in Positive Sentiment from Q3 to Q4 2019



Source: FreightWaves Q4 Freight Broker Survey - October 2019

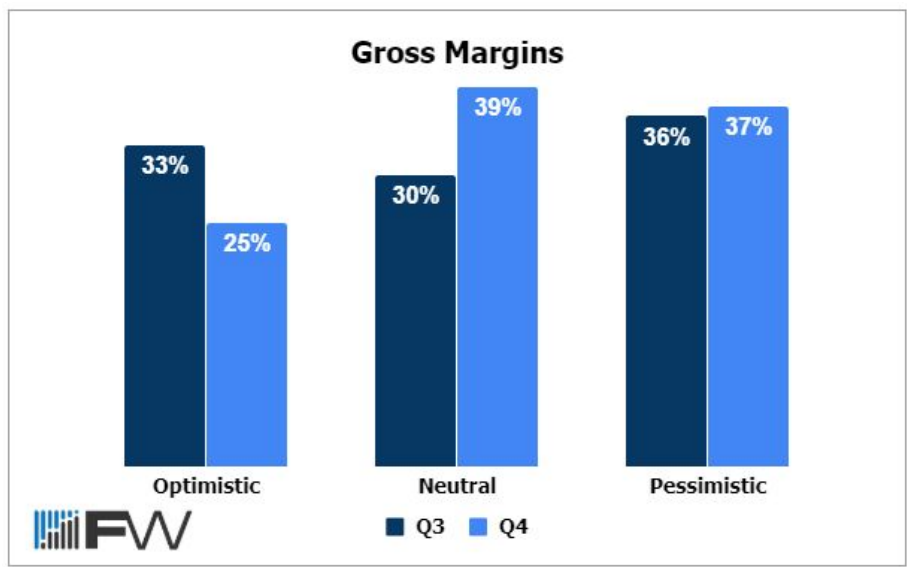


Figure 5 – Freight Broker Change in Sentiment from Q3 to Q4 2019 — Positive, Negative and Neutral Readings



Source: FreightWaves Q4 Freight Broker Survey - October 2019

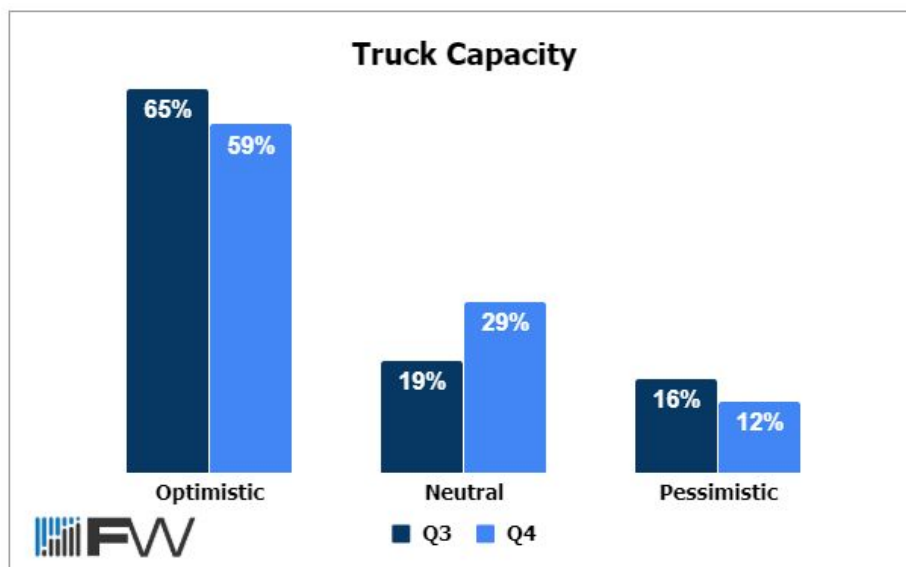
Figure 6 – Freight Broker Sentiment for Gross Margins



Source: FreightWaves Q4 Freight Broker Survey - October 2019

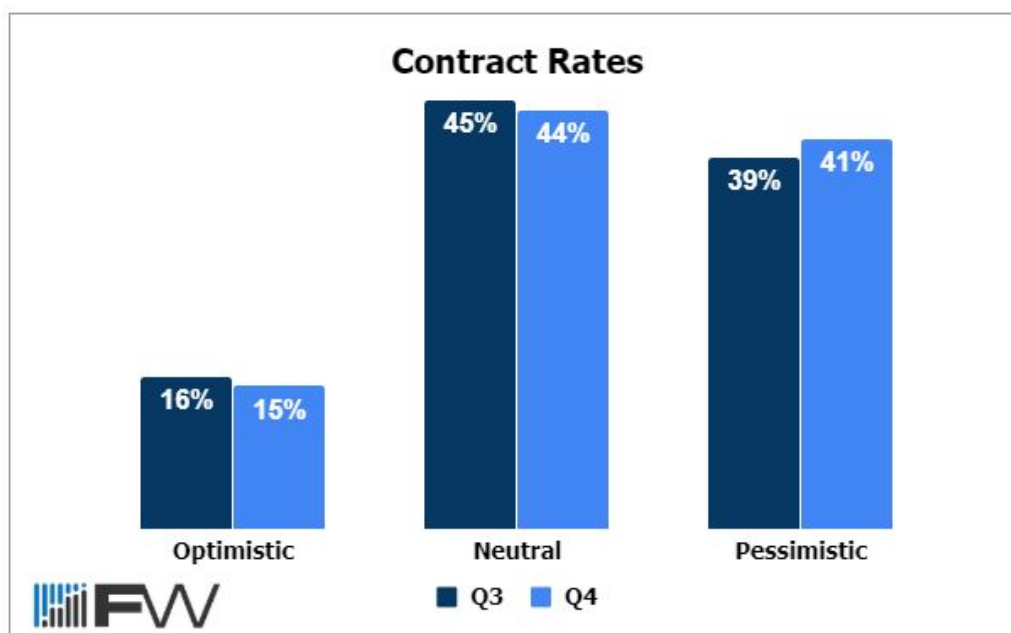


Figure 7 – Freight Broker Sentiment for Truck Capacity



Source: FreightWaves Q4 Freight Broker Survey - October 2019

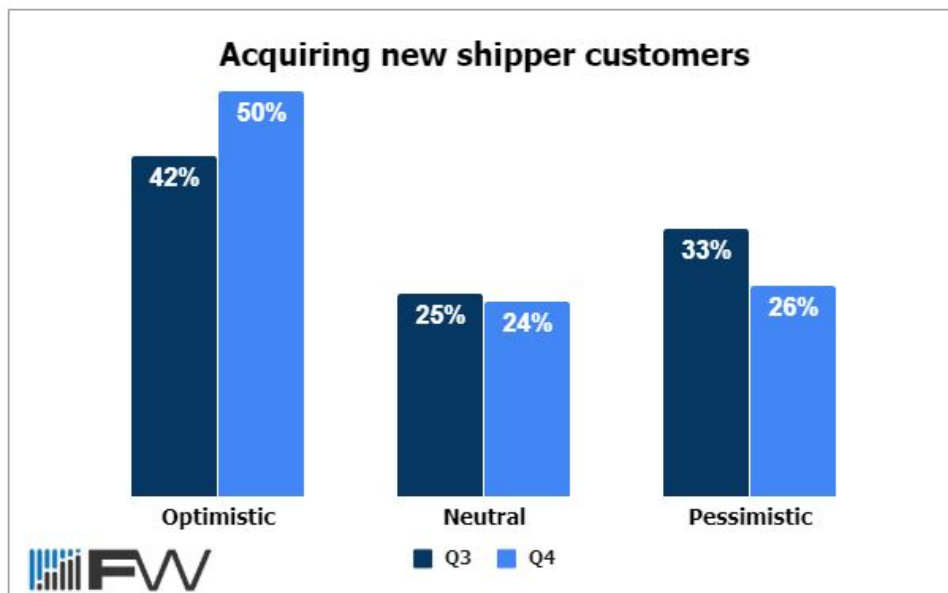
Figure 8 – Freight Broker Sentiment for Paper (Contract) Rates



Source: FreightWaves Q4 Freight Broker Survey - October 2019

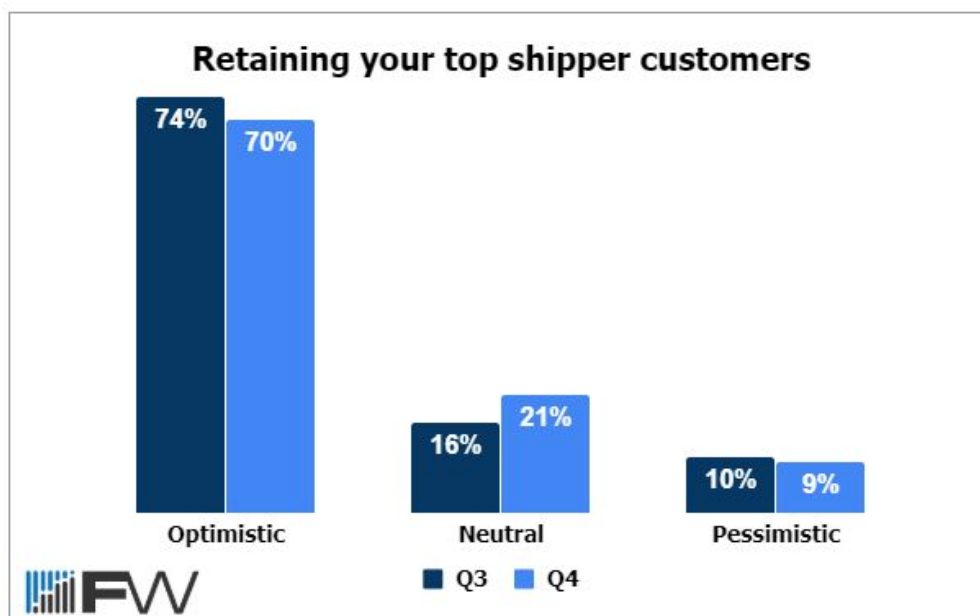


Figure 9 – Freight Broker Sentiment for Acquiring New Shipper Customers



Source: FreightWaves Q4 Freight Broker Survey - October 2019

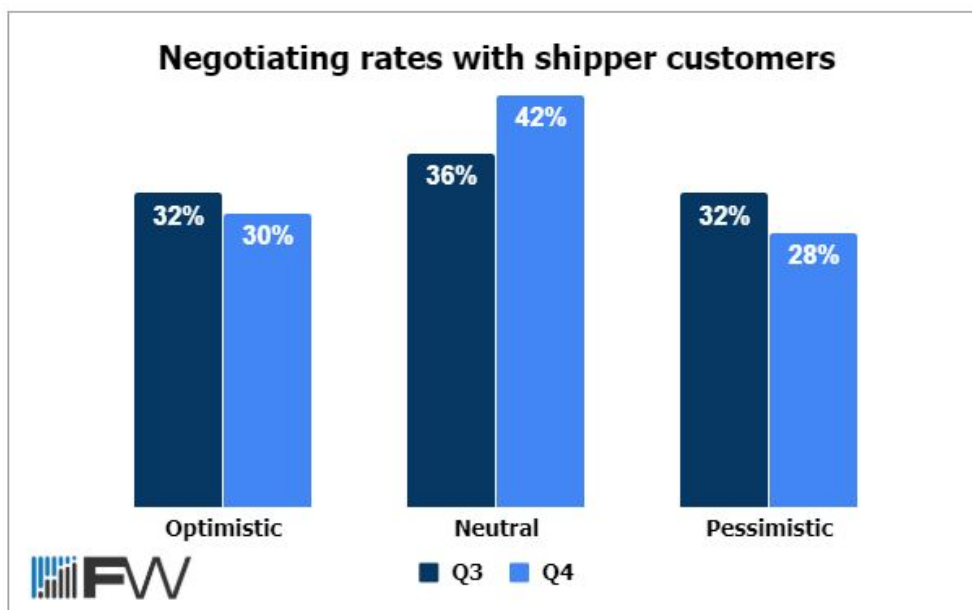
Figure 10 – Freight Broker Sentiment for Retaining New Shipper Customers



Source: FreightWaves Q4 Freight Broker Survey - October 2019

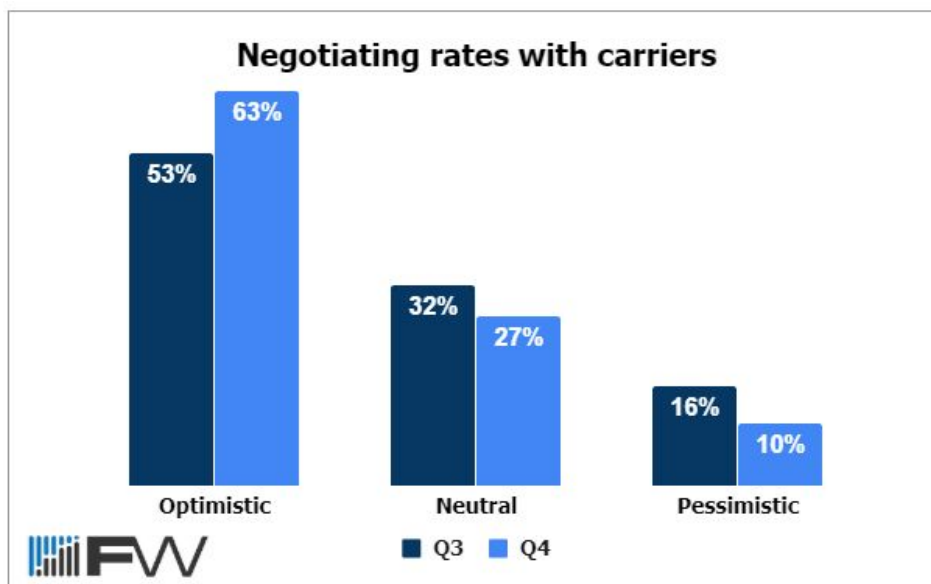


Figure 11 – Freight Broker Sentiment for Negotiating Rates with Shipper Customers



Source: FreightWaves Q4 Freight Broker Survey - October 2019

Figure 12 - Freight Broker Sentiment for Negotiating Rates with Carriers



Source: FreightWaves Q4 Freight Broker Survey - October 2019



Key Freight Market Trends in Q4 2019 and Q1 2020

The following SONAR data reflect market conditions as of Nov. 20.

Figure 13 – Tender Load Volumes Are Now Slightly Below 2018 Levels



SONAR: OTVIY.USA – Annual percentage change in outbound tendered load volumes between 2019 and 2018

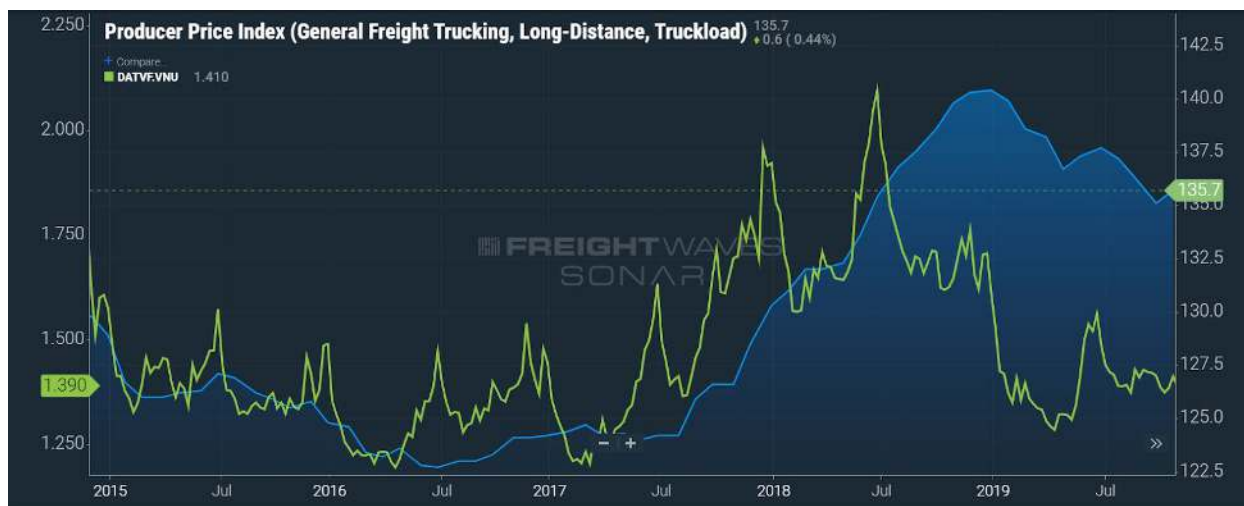
Figure 14 – Outbound Tender Rejection Rates Are Above 6% for the First Time Since July 2019



SONAR: OTRI.USA - One year change

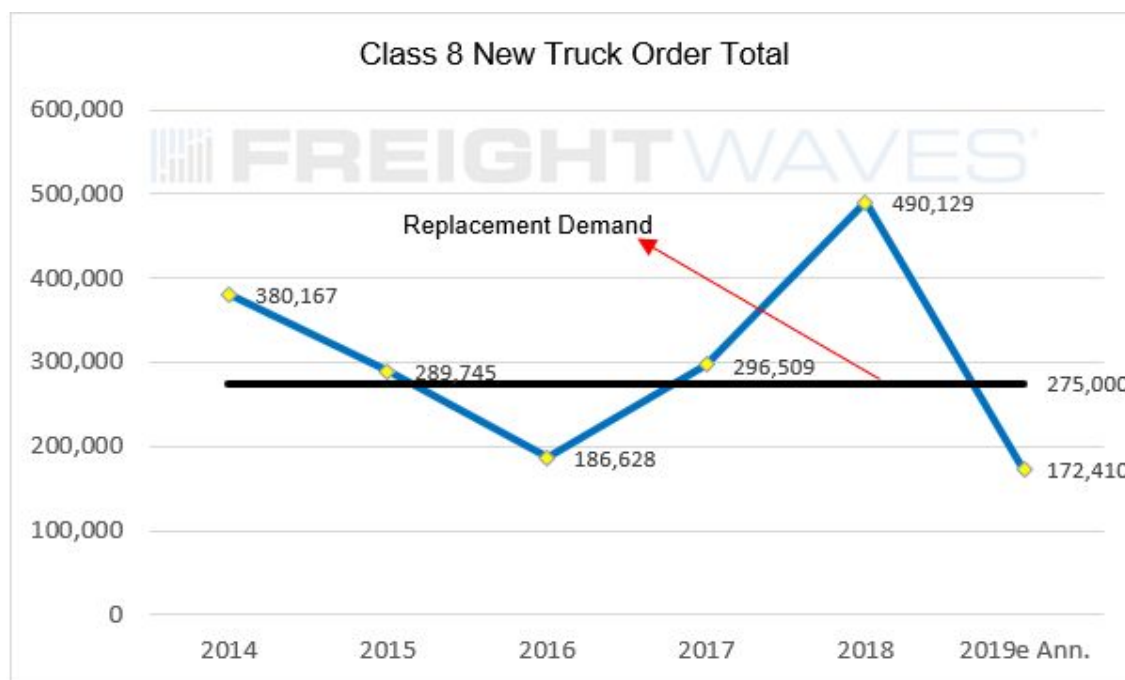


Figure 15 – Contract Rates Post First Year-Over-Year Declines in Growth in This Cycle



Source: PPI.LDTL (Blue) and DATF.VNU (Green)

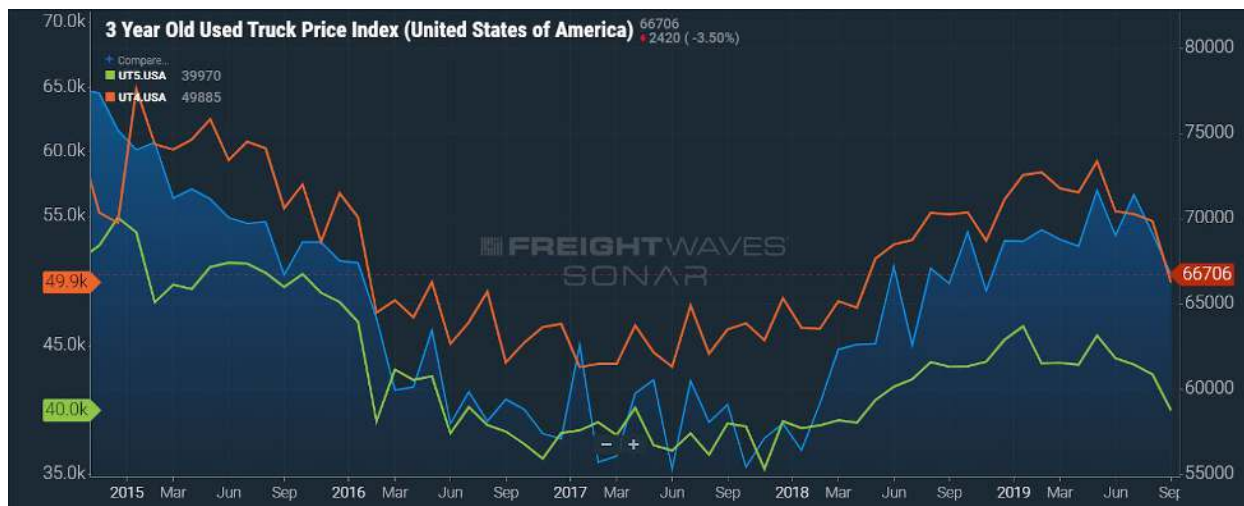
Figure 16 – 2019 New Truck Orders Are Still Running Well Below Replacement Levels



Source: FreightWaves analysis of ACT Research



Figure 17 – Used Truck Values Have Now Declined for Three Consecutive Months



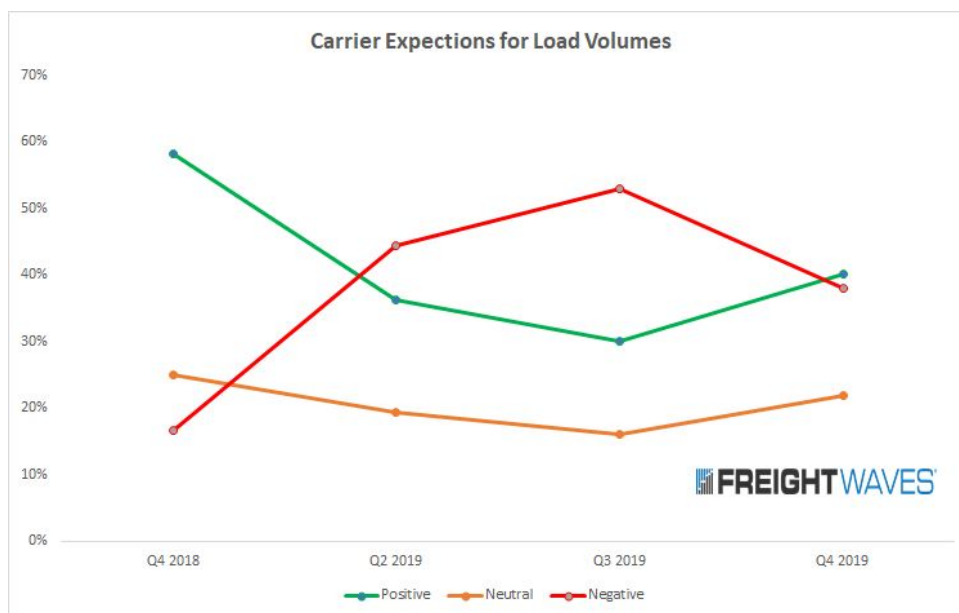


Fourth Quarter Carrier Outlook Survey Results

In October, FreightWaves surveyed 137 small and midsize carriers (fleets with five to 100 trucks) to gauge their current sentiment on a number of market conditions compared to those experienced in 2018.

This survey is a continuation of quarterly carrier outlook survey FreightWaves has conducted since the fourth quarter of 2018. The results are presented below to provide a historical look at carrier sentiment.

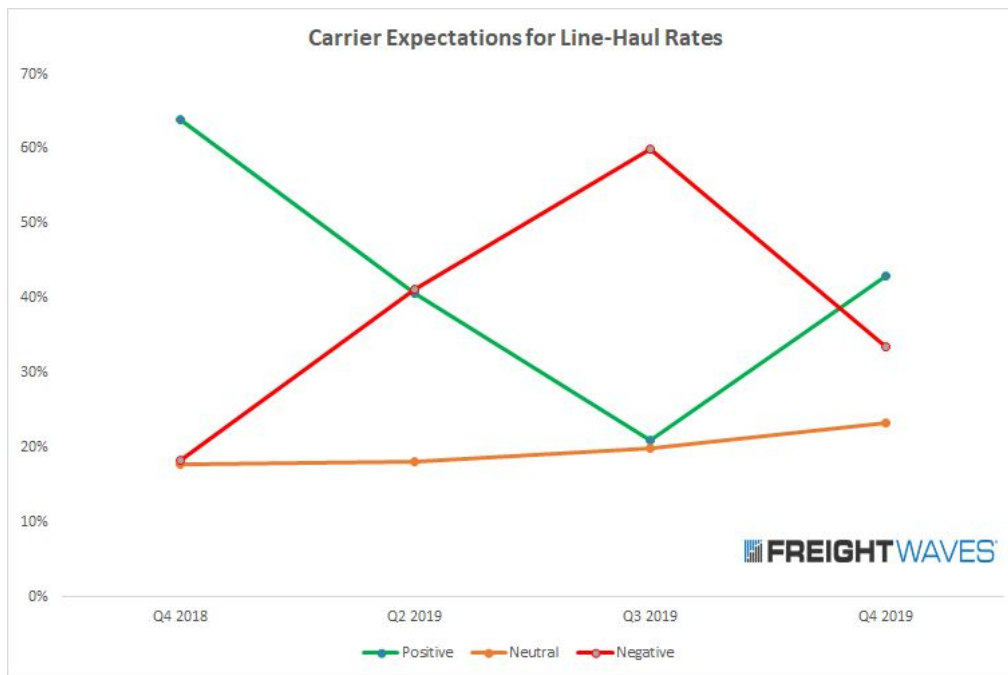
Figure 18 – Carrier Outlook for Load Volumes Rebounds for Q4 2019



Source: FreightWaves Carrier Outlook Surveys – Q4 2018, Q2-Q4 2019

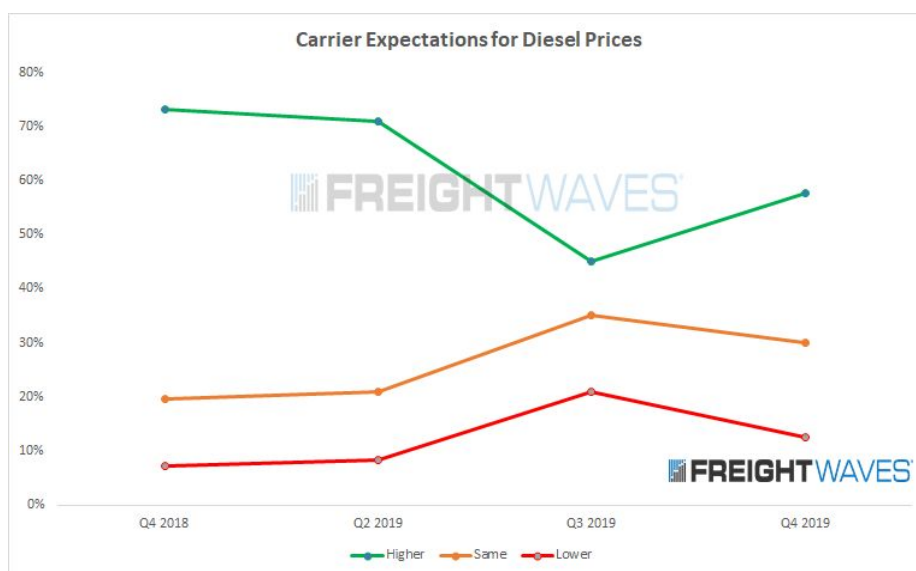


Figure 19 – Carrier Optimism for Line-haul Rates Double from Q3 to Q4 2019



Source: FreightWaves Carrier Outlook Surveys – Q4 2018, Q2-Q4 2019

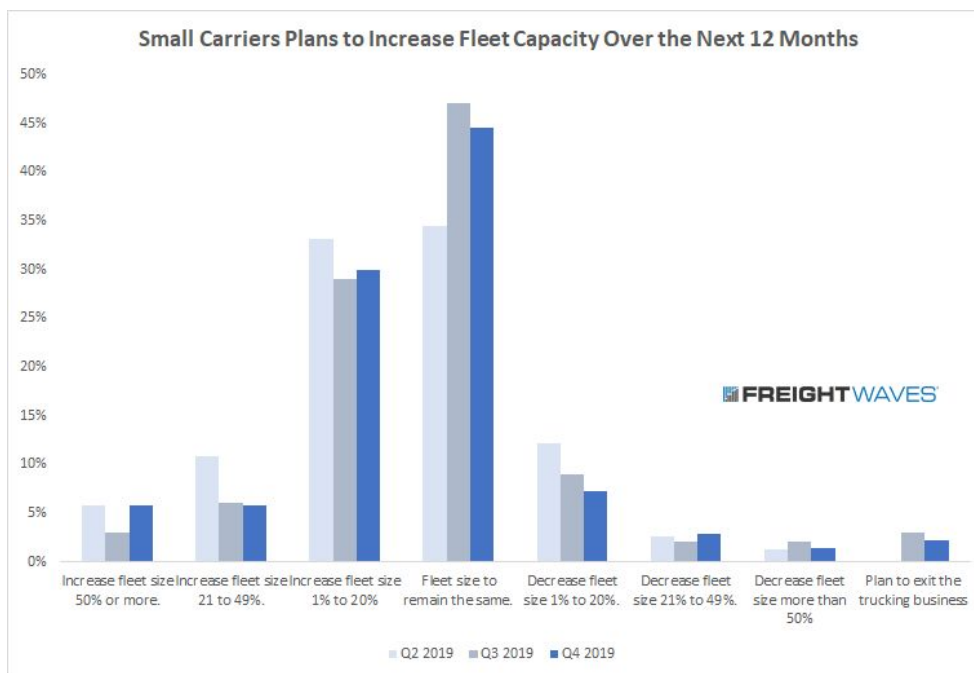
Figure 20 – Where is Diesel Heading Over the Next Six Months?



Source: FreightWaves Carrier Outlook Surveys – Q4 2018, Q2-Q4 2019

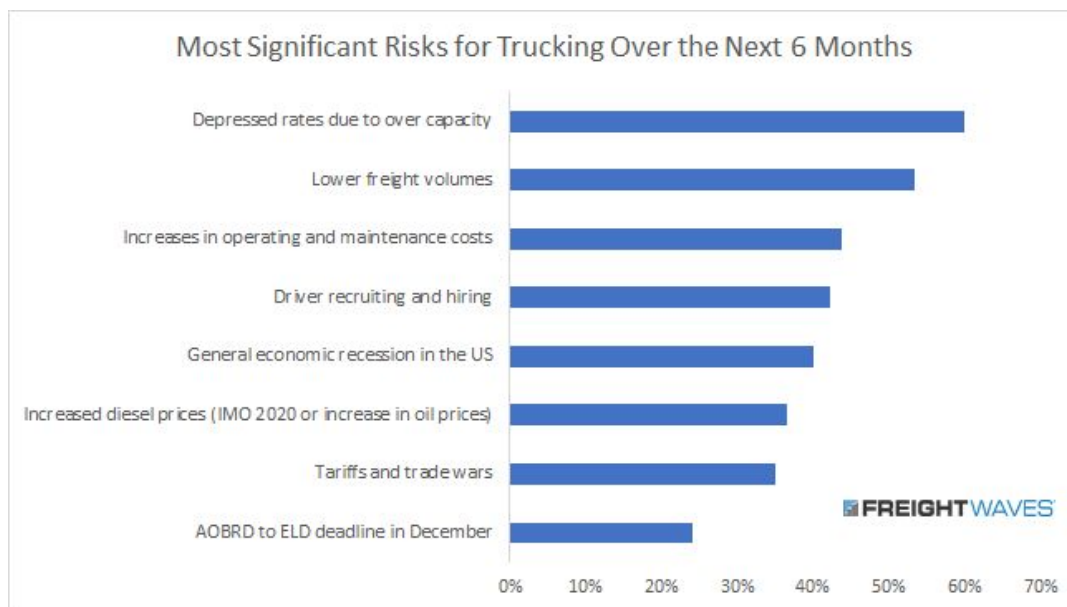


Figure 21 – Are Carriers Expanding or Contracting Trucks in Their Fleets?



Source: FreightWaves Carrier Outlook Surveys – Q2-Q4 2019

Figure 22 – Where is the Risk to a Trucking Recovery?



Source: FreightWaves Carrier Outlook Surveys – Q4 2019



FreightWaves

FreightWaves is one of the fastest-growing enterprise software-as-a-service (SaaS) companies in the world. In less than three years, FreightWaves has become the leading provider of data and analytics for the global freight market. FreightWaves' full-time team of 150 captures, models and interprets near-time data from more than 1,000 sources to provide participants with the fastest insights into the global freight market. The company offers the fastest data in the industry and the most complete view across all modes of freight transportation. SONAR, the company's SaaS offering, is a market dashboard that provides companies involved in transportation with access to data sets that can help them optimize their routing, pricing and planning decisions.

FreightWaves is also the largest publisher of freight news and data in the world. FreightWaves.com publishes more than 40 news articles per day, providing commentary and analysis for freight transportation, while FreightWaves TV is the first and only streaming TV network for the transport and logistics industry.

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FreightWaves Freight Intel Contacts

Kevin Hill, Director of Research

(646) 731-4735, khill@freightwaves.com

Seth Holm, Senior Research Analyst

(404) 840-2064, sholm@freightwaves.com

Andrew Cox, Research Analyst

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