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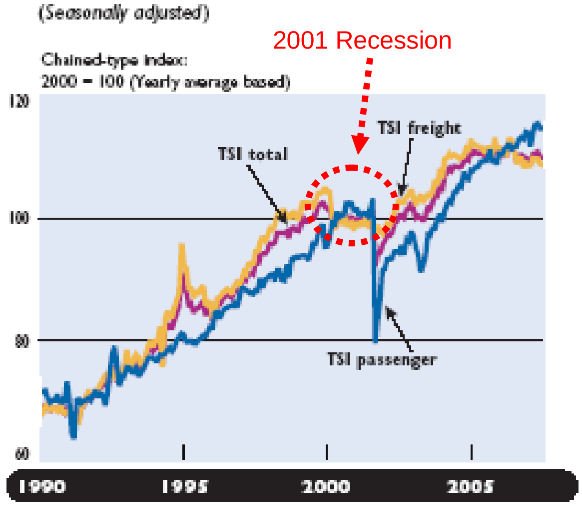
Learn From The Past - Don't Get Caught With High Rates & No Carriers

As we enter the rough waters of financial uncertainty, it is important that we don't take issues like carrier capacity and the financial condition of our service providers for granted. Many of the indicators of the last recession are similar to today's conditions; periods of rising diesel fuel prices, financial market indices dropping, and downward pressure on used truck pricing. With these factors in mind, prudent executives in firms that move goods will take steps to make sure that they are on the winning end of these turbulent times for the transportation industry.

What happened the last time?

Preceding the 2001 recession, several factors conspired to impact the trucking industry and its customers in a negative way. Pressure on the trucking industry began in the fall of 1999 with falling used truck prices that threatened the financial viability of the nation's truck fleets, truck and trailer manufacturers and truck equipment finance companies. Following several strong years for new truck sales and two years of record economic expansion, a glut of low mileage tractors in very good condition filled the used truck market. This depressed truck prices to the lowest levels seen in many years.

Transportation Services Index (TSI): 1990–2007
(Seasonally adjusted)



Notes: 2007 data are through July. May–July 2007 data are preliminary. The TSI total is a single index measure of monthly output of for-hire transportation services in the United States using 2000 as the base year.

Source: Compiled by U.S. Department of Transportation, Research and Innovative Technology Administration, Bureau of Transportation Statistics, special calculation, September 2007, available at: http://www.bts.gov/xml/tsi/src/index.xml.

The falling value of many major carrier investments in fleet assets left about two-thirds of trucking companies in North America nearly bankrupt as the value of their assets declined dramatically. This threatened more trucking concerns than the combination of escalating fuel prices and the ongoing driver shortage. And the three together formed a perfect storm many would not survive and the sharp increase in bankruptcy filings during the period bears witness to this effect.

In March, 2001, the U.S. economy entered a recession followed almost immediately by the events of September 11, 2001. The DJIA plummeted, causing the economy to sink further into decline. The result was layoffs and surging defense spending, putting more pressure on the economy.

The recession's toll on the transportation industry was high; hundreds of thousands of drivers out of work, as even stalwarts fail. Consolidated Freightways became the largest motor carrier to declare bankruptcy. This failure alone cost 15,000 drivers their jobs. At the end of 2001, there are 330,000 fewer trucks operating than there were two years prior. During this recessionary period and slow recovery, from 2001 to early 2003, 11,500 motor carriers went out of business. The resulting decline in industry capacity, allowed the surviving carriers to raise rates as shippers jockeyed to find available capacity. Industry consolidation, rather than a surge in demand, led to the eventual rebound. For customers, freight flowed, rates began getting higher and carriers began reporting higher profits.

Financial performance for the carriers who ran tight operations (Top 100 Carriers – Bureau of Transportation Statistics) through the 2001 recession saw a minor shift in operating ratios (OR)[Is that correct? OR = operating ratio? In any case, let's define it. –Ed.]:

1994 Average OR for Top 100 – 94.2
1999 Average OR for Top 100 – 94.6
2000 Average OR for Top 100 – 94.9
2001 Average OR for Top 100 – 95.4
2002 Average OR for Top 100 – 95.5

How were the customers affected?

Companies with significant transportation requirements felt downstream effects from all the carrier failures and the resultant consolidation; shipping delays, cost increases from surviving carriers and asset write offs for private fleet operators.

What should I do today?

If shipping is a fundamental part of your supply chain, it makes sense to take stock of your situation and take action to ensure your goods continue to flow to your customers on a timely and predictable basis. Here are 5 things to do now:

1. Review the condition of your carriers. This includes the usual key performance indicators for transportation like on-time performance, damaged items per 1000, deliver time, freight as a percent of sales, etc. But at times like this, financial stability, credit worthiness and other business fundamentals of carriers should be reviewed.

2. Take immediate action on urgent exposures and low hanging fruit. The carrier review will yield results in the form of low hanging fruit opportunities for improvement in cost and performance, long term initiatives and potentially some urgent issues that need to be dealt with immediately before they become problems. Begin work immediately on the low hanging fruits ideas and any urgencies that are discovered such as pending failures etc.
3. Plan for the long term and for nimbleness in the near term. Once the low hanging fruit project have been started (and are generating benefits that can pay for longer term initiatives) and the urgencies are satisfied, planning can begin on long term initiatives, and contingencies. Longer term initiatives might include contracting with a third party logistics (3PL), or instituting a core carrier program. These are projects intended to keep shipping costs low as a percentage of sales over the long run. Planning for contingencies means simply that it may not be time to replace a weak carrier, but perhaps it's time to allocate some capacity on another carrier so that in the event of a problem (with either carrier), the company already has relationships established with alternate carriers that can step up and carry the load.

Situation: we are on the verge of economic conditions similar to 2001

Challenge: carriers and OO's went out of business in 2001 and if that happens again, it could impact your business if you rely on them.

Solution: 1) understand the condition of your carriers; their credit worthiness and cash position, their ability to flex to take on capacity should you need to consolidate on fewer providers, 2) Make any immediate changes needed, and 3) plan for contingencies and nimbleness by always have a secondary provider in case of needs.

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