

ATA's Trucking Economic Review

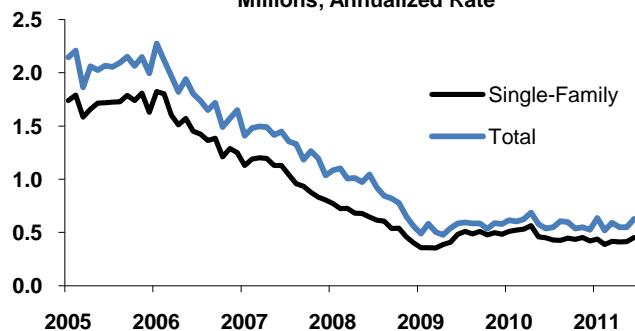
WHAT WILL HAPPEN IN THE 2ND HALF?

The economic outlook for the second half of the year is really up in the air at this point. Earlier this month, we were cautiously optimistic that real (i.e., inflation adjusted) gross domestic product (GDP) could grow approximately 3%, which would be much higher than the less than 2% we are expecting for the first half of the year. However, that cautious optimism is under threat as more recent economic data are suggesting sluggishness, not strength, will prevail. For example, we had a disappointing manufacturing number for June and there is still a lot of uncertainty related to the U.S. debt ceiling crisis and the European debt issue. To be certain, we are talking about sluggish growth for the rest of the year, not another recession.

THE ECONOMIC HEADWINDS

The U.S. economy is plagued with several headwinds, including the housing sector, a lackluster job market, accelerating inflation, indecision in Washington, D.C., and a lack of confidence. That doesn't mean all of the economic news is bad - quite the contrary; however, these are enough to keep a lid on growth for the time being.

Figure 1: Housing Starts Through June 2011
Millions; Annualized Rate

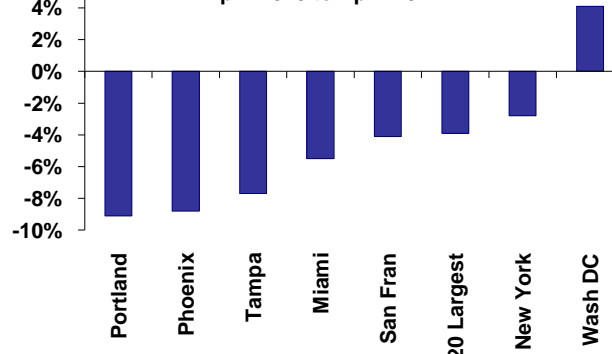


Sources: U.S. Census Bureau and ATA

Housing Still Lags

Housing continues to limit economic activity, although it is at such low levels, the importance to the economy has fallen over the last few years. Nevertheless, construction remains a large driver of trucking activity. In June, housing starts took a surprising leap, climbing to an annual rate of 629,000 from May's 549,000, but are still well below a "normal" 1.5 million rate.

Figure 2: Change in Home Prices
April 2010 to April 2011



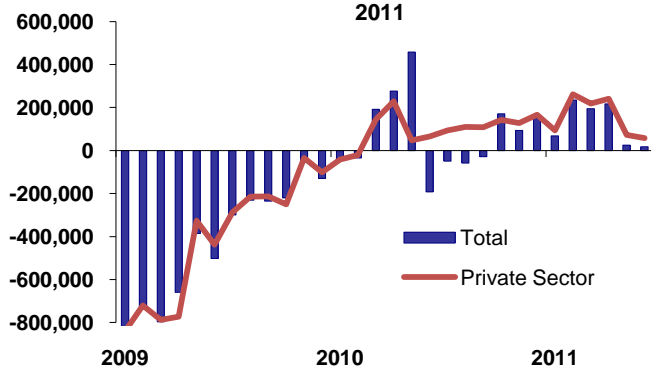
Sources: S&P/Case-Shiller Home Price Index and ATA

There are still too many factors holding down the residential construction industry, including falling home prices, relatively tight credit conditions, and low family formation.

In April of this year, which is the latest data available, of the 20 largest metropolitan areas in the country, only one witnessed an increase in home prices compared with a year earlier (Washington, DC). For the group as a whole, prices were down 3.9% from April 2010. Housing starts are not going to increase significantly until home prices stabilize and begin to increase. At this point, we don't expect a return to 1.5 million starts until 2014.

In terms of family formation, this is one of the most important factors driving housing. During a recession, young people tend to put off marriage and starting a family, which reduces demand for housing.

Figure 3: Change in Employment Through June 2011



Sources: U.S. Department of Labor and ATA

Employment

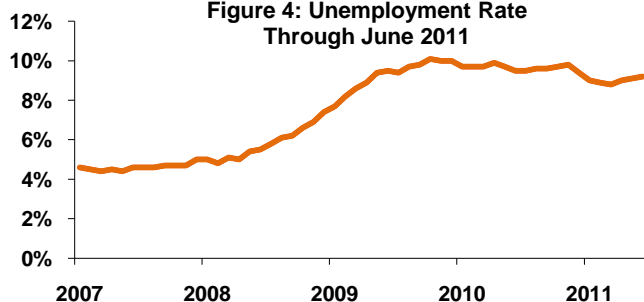
To say that the job numbers of late have been disappointing is quite an understatement. In May and June, total U.S. payrolls increased just a total of 43,000. At this stage in the recovery, we should be creating an average of 175,000 per month, or more. While the private sector is doing better than the overall economy, here too the number of jobs created are low – just 130,000 total in May and June.

The lack of job creation is a major reason why real GDP is likely to be muted in the second half of the year, unless things turn around quickly. In order to get to above 3% growth in the third quarter, we needed to create (net) at least 175,000 jobs per month.

Why are the job numbers so low? Several factors, including a lack of business confidence, the economic soft patch hit this spring, and bad weather during the first and second quarters of the year. These factors were expected to be temporary with stronger numbers starting already. Also, one other factor may be Washington, DC. With negotiations regarding the debt limit moving into the 11th hour, corporate America may be holding tight before hiring additional employees to see how everything plays out.

Bottom-line on employment: At some point, in order to increase output, businesses will have to increase employment levels. Productivity is high and output can't increase much without more labor. However, don't be surprised if the unemployment rate increases slightly before it falls again,

Figure 4: Unemployment Rate Through June 2011



Sources: US Department of Labor and ATA

which is currently at 9.2%. When the employment situation improves, more unemployed people are likely to enter the job market again, thus being counted as unemployed. Pay more attention to the number of jobs created in the near-term.

Government

There is no doubt that our public sector has to shrink in the future. And, while there is lots of debate in Washington, D.C. on how that will occur, the reality is that it will slow economic growth because the public sector is a major part of our economy, whether we like it or not. Last year, federal, state, and local government consumption and investment equaled about 20% of GDP.

As the public sector shrinks, that will be a drag on output. No doubt, in the longer term, less government spending can free up capital for the private sector, but that is unlikely to happen much in the near-term. Additionally, if taxes are increased, and there are very few economic forecasters that don't expect some form of tax increase, that will impact growth as well.

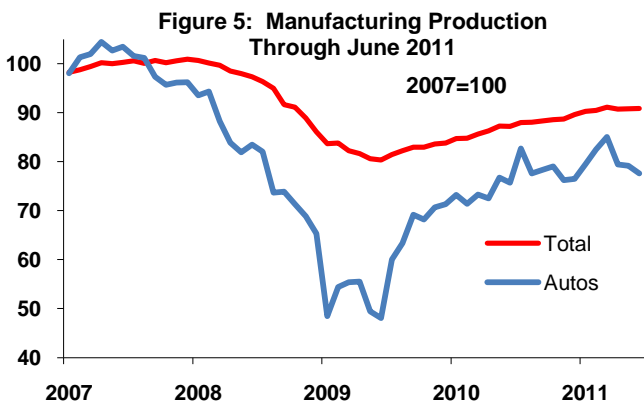
Bottom-line: The public sector needs to shrink, but the reductions in spending and/or tax increases will constrain growth in the near-term. Longer-term, we will be better off with a leaner, more efficient government.

Inflation

Inflation measures have accelerated over the last year. For example, in June, the consumer price index (CPI) was up 3.4% compared with a year earlier. This tied May 2011 as the fastest year-over-year clip since late 2008. The "core" CPI, which excludes food and energy prices, was up 1.6% from a year earlier, the fastest pace since December 2009, although the Federal Reserve likes to see the core rate between 1% and 2%, so we are right in the middle of that range now.

Wholesale inflation is rising too. The producer price index (PPI) was 7% higher in June of this year than the same month last year, which was the largest gain since late 2008. The same is true for the core PPI, which increased 2.3% from June 2010.

Bottom-line on inflation: While inflation has accelerated in the U.S., it is nearly all commodities driven. We are more concerned about inflation outside the U.S. in emerging economies than in the developed world. In the U.S., with more than 14 million people still unemployed, wage inflation is unlikely; and without wage inflation, it will be difficult for headline inflation to increase too fast. After increasing 1.6% last year, we expect the CPI to jump 3% this year and then rise a smaller 1.8% next year.



Sources: Federal Reserve and ATA

Confidence

Finally, households and businesses are suffering from a lack of confidence. A recent poll reported that a majority of households still believe we are in a recession. At the end of the day, we don't put too much stock in these confidence indexes as they are subject to the news of the day. Nevertheless, it is not good to have a lack of confidence during this soft recovery either.

THE ECONOMIC TAILWINDS

From reading the news print, one might think that there are few, if any, bright spots in this economy. However, that is not the truth. Up until recently, we were expecting a very solid second half of the year because of these economic strengths. Unfortunately, the headwinds increased in recent months and the tailwinds decreased slightly, but the economy is still more likely to grow going forward than fall back into a recession.

Manufacturing Output

The industrial sector has been a very bright spot in the U.S. economy this year. Through June, manufacturing production was up 5.3% compared with the same period last year. Growth would have been even better if it were not for an 8.8% drop in auto production this spring, in part, from Japanese supply problems stemming from the earthquake.

While manufacturing output hit a soft patch in the spring like most sectors, there is evidence that activity could accelerate again. Specifically, the Purchasing Manager's Index increased to 55.3% in June from 53.5% in May, which was the largest increase since January of this year. The PMI is a good leading economic indicator and typically tracks very well with truck tonnage.

Goods Exports

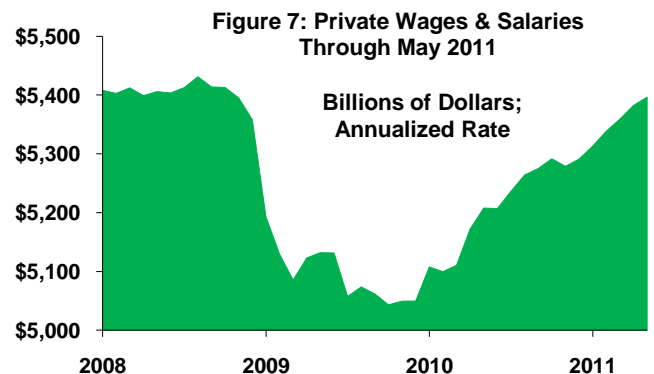
U.S. goods exports have been one of the reasons why manufacturing activity is increasing nicely. As Figure 6 shows, exports have fully recovered and are now above pre-recession levels. A relatively weak dollar is helping, but so is robust growth in the emerging world. While the U.S. is not going to become a net exporter, these trends will help production and truck freight volumes domestically.

Wages Are Rising

Private industry wages and salary disbursements are nearly back to pre-recession levels. Incomes are not growing at a pace that alarms us about inflation, but it is good that they are rising again. Couple in the fact that the stock market is healing, savings are rising, debt loads are falling, and net worth has grown, consumer finances have improved significantly. This is a very positive trend going forward and one that will help consumer spending. Don't expect a return to the pre-recession heyday, but most consumers are in a better position today than before.



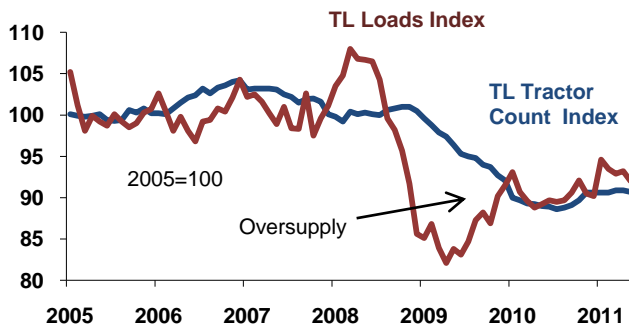
Sources: US Census Bureau and ATA



Source: Bureau of Economic Analysis

at this point. Figure 10 shows ATA's large TL tractor count has been flat this year (blue line), so despite a small drop in volumes, supply and demand are close to being in balance. While the freight market is not really tight currently, considering the sluggish economy, it is better than one might expect.

Figure 10: For-Hire TL Supply vs Demand



Source: ATA's *Trucking Activity Report*

Through May of this year, the small TL tractor fleet count is down 7.2% from the same period last year. Over the same period, the LTL's reported 7.4% fewer trucks operated. In other words, the number of trucks operated by most sectors is either flat or down significantly.

The bottom-line on capacity: Little, if any, capacity is coming on-line, a trend that is likely to continue in the foreseeable future. The driver shortage is quickly returning, which will limit capacity. Government regulations are limiting and could reduce further the amount of capacity. Finally, the much higher equipment prices are likely to limit the amount of tractors fleets can buy, thus limiting capacity. At this point, nothing suggests that a large amount of supply will come on-line in the quarters ahead.

Costs

While carriers should be pleased that supply and demand are relatively in balance, they cannot ignore the cost side of their business during this sluggish economy. In fact, motor carriers are seeing much higher inflation rates than the economy overall. Everything from diesel fuel prices, which, for most TL carriers, has caught or surpassed labor as their largest expense, to tires to tractors to driver wages seem to be going up.

Summary

Chances of a better second half of the year are falling as most economic data suggest sluggish growth going forward. However, that doesn't mean that all of the economic news is bad and that a recession is imminent.

In fact, the likelihood of a recession is still fairly low. Nevertheless, it will be slow going for awhile, which means that truck freight volumes will show lackluster growth, at best.

Luckily, our industry has been disciplined and supply has grown little, if any, over the last year, which means supply and demand are fairly balanced. However, carrier bottom-lines are under pressure as most costs are rising significantly. This is a trend that isn't likely to go away anytime soon.



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ATA's Driver Compensation Study Now Available!

In June 2011, ATA published its latest Driver Compensation Study (DCS). The last time ATA published this study was in 2009. The results were based on surveys of 155 motor carriers.

- Employee Driver Data (e.g., years of experience required, training required, minimum age required, bonuses offered, holidays and vacation time offered, retirement plans and other benefits offered, and how often drivers get home)
- Employee National and Regional Driver Wage Data (e.g., average annual driver salary by carrier revenue size, by nationwide and regional, by carrier type)
- Hiring and Retention Data (e.g., sources for recruiting new drivers and average recruitment costs per driver)
- Independent Contractor Data (e.g., how carriers pay independent contractors and if cash advances are provided)
- Technician Data (e.g., how much technicians are paid and benefits provided)

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