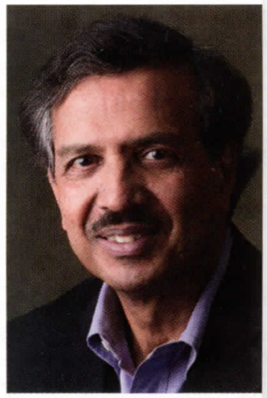
Commentary

Time for truck shippers to rethink practices



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2018 PROMISES TO be a great year for truckers. The demand and supply imbalance is shaping up to be of the kind not seen in last 20-plus years, and spot market rates are up high double digits, even exceeding 20 percent over just a few months ago.

It's no surprise, then, that shippers are complaining and fearing a huge increase in transportation costs. For those who keep informed of developments impacting this spike in prices, this should not have come as a shock.

The factors impacting the hikes are outside the control of the industry. Trucking capacity reduction results from factors such as: the declining appeal of driver jobs among young people; the poor quality of life for drivers away from home for several days week after week; crumbling infrastructure causing delays on roads; and the Dec. 18 rollout of the ELD mandate.

Simultaneously, demand has increased rapidly because of the national focus on America First efforts by large corporations to expand manufacturing activity in the US, which has increased industrial production index by 3.5 percent; and greater demand for faster delivery by consumers driven by free shipping promotions by online retailers.

The carriers, no doubt, are viewing this as an opportunity to price their capacity at the highest level the market will support, to the chagrin of many shippers. The shippers fail to realize that the for-hire trucking industry with $300 billion in revenue generates less than $25 billion in operating income.

This 8 percent profit margin pales in comparison to other suppliers shippers utilize. The top three technology companies (Apple, Google and Microsoft) generate more than $400 billion in revenue per year, but in excess of $100 billion in profit, or a profit margin of more than 25 percent. And the two largest US telecommunications companies (Verizon and AT&T) generate nearly $300 billion in revenue at a 20 percent profit margin. Even the railroads operate at a 30 percent margin.

Furthermore, the shippers overlook that the trucking industry is very capital- and labor-intensive. It has to generate free cash to purchase tractors that have increased in cost from $100,000 in 2010 to more than $140,000 now. In addition, the industry is very labor-intensive and has to pay higher wages to drivers, which are still only $44,000 per year in spite of recent wage increases.

This may not appease the shippers who are accustomed to having very low rates. Such low margin for truckers has resulted in transportation being less than 4 percent of total cost of the products moved. So, even with a high double-digit increase in truck rates, trucking still will result in a less than 1 percent increase in total cost of the products for shippers.

Furthermore, in spite of all the progress to improve utilization of trucking capacity, about 15 percent of the capacity is still wasted for reasons including factors that are within the control of the shippers, such as: elimination of air from the trailers with better packing and palletizing of freight; keeping drivers and trucks waiting to deliver freight to a consignee or to pick up freight from a shipper; more deliveries and pickups from facilities without a freight dock or with a very tight maneuvering yard; and keeping a driver waiting to obtain confirmation of delivery.

ShipMatrix data on billions of parcels and LTL shipments show that even with new dimensional charges, there are still many parcels that are shipped with excessive cube. This problem is not limited to parcel shipments, but gets manifested in higher cube in less-than-truckload shipments and in truckload shipments, thereby adding to higher transportation cost.

There is at least one large trucking and intermodal company that alerted its customers last year to budget for a 10 percent increase in 2018. In making such suggestion, the company went to great length to explain the various factors that were contributing to such a projection.

Do shippers receive explanation from Apple for charging more than $1,000 for its new 10x iPhone? And when have these shippers received any explanation from Microsoft for major increases in prices for its software and hardware products?

As expected, this change in demand and supply for trucking capacity is impacting the LTL industry. The LTL industry has operated at a single-digit operating margin since deregulation in 1980. Given that shippers have many ways to reduce their transportation cost with better shipping practices, the LTL carriers should feel justified to increase their margins and generate more free cash for investment in new model tractors and higher wages for drivers.

The shippers would like to see the carriers add capacity to avoid rate increases in this tight market. However, when the trucking industry had excess capacity in the past, the shippers were quick to demand lower prices and squeeze carrier margins.

In this market, the carriers should not feel bad about increasing their profit margins. The higher income will still fall short of recovering the decline experienced in last several years when they had single-digit profit margins. This supply and demand imbalance offers an opportunity for shippers to assess their shipping practices. They will find their inefficiencies are responsible for more cost in absolute dollars than the increase that will result from higher rates. JOC

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