U.S. XPRESS

COVID-19 IMPACT

Forecast Update

06/15/20

PERSEVERANCE AMIDST ADVERSITY

On April 21st, the leadership team at U.S. Xpress released a forecast exploring the potential impact of COVID-19 on freight markets, truckload capacity, and the overall economy. The first section of that forecast was subtitled: "Optimism is Allowed." As several states and municipalities commence the phased reopening process, we see plenty of things to be hopeful about for the future. The re-openings across the country are welcome news for those who are weary from uncertainty. While the long-term repercussions of COVID-19 are still somewhat murky, the trajectory of freight markets in Q2 is becoming clearer.

Without a doubt, the past several months will be remembered as one of the most trying times in modern history. The pandemic has taken a remarkable toll on the health and economic wellbeing of so many of our neighbors and friends. However, as we expressed before, we've never been prouder of the courage and resiliency on display in the trucking industry. When this pandemic has passed, we'll have truckers to thank for keeping our shelves stocked and our economy afloat. Their contributions have literally saved lives. They've been truly relentless.

Our April 21st whitepaper forecast took the position that this pandemic has the potential to cull truckload capacity unlike any event in recent memory. Here's an excerpt from our forecast:

> "Just as we expect the industry to experience unprecedented weak demand in the second quarter, we believe that will give way to a sharp increase in demand on a level we've never before seen. Even more impactful will be the fact that we will see this heightened demand concurrent with supply levels decimated in the wake of a rough second quarter. By that time, fleet counts will have retracted across the board. Bankruptcies could remove more capacity in a single quarter or two than any previous cycle we have ever experienced, including the 'Great Recession' of 2008.
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> Here's the near-term future we envision: when we go in to a full recovery, spot rates will run to historical highs; but the bigger story will be the amount of freight that will have to be deprioritized and sit on docks because there isn't enough capacity to handle all of the demand."

Several weeks have elapsed since we shared our perspective. In the items below, we've tabulated some of the data that's been reported since our initial forecast. **Our hope is that the worst is behind us: not only with respect to the public health repercussions of the virus but in terms of the deterioration of our economy, as well.** Of course, the degree to which policy makers and the business community can turn their focus to recovery will hinge on how smoothly we reopen and whether we see a resurgence in cases.

WHAT'S HAPPENED SINCE OUR INITIAL FORECAST?

The past several weeks have revealed several data points that reinforced our earlier viewpoint with regards to the impact of COVID-19 on the freight market as well as the economy in the broad. It's worth reiterating that, in trying to understand the impact of COVID-19 on the freight industry, U.S. Xpress is staying mindful of the trade-offs between fast data, which tends to be noisy, and slow data, which tends to be slightly more longitudinal in nature and thus somewhat more reliable.

With that caveat in mind, here are some numbers that have gotten our attention since the release of our initial forecast:

- On May 28th, the Bureau of Economic Analysis released its second estimate of Q1 GDP calculating a 5.0% decrease. Now, this estimate is subject to further revision as Q2 GDP reporting is released. However, the repercussions of COVID-19 for 2Q GDP aren't much of a mystery. The only question is just how steep the decline will be.

- After 10 weeks of jobless claims totaling more than 40 million, the most recent two weeks of Department of Labor data have brought better news. Initial jobless claims fell by 249,000 during the week ending May 30th from the prior weeks' total of 2.13 million. Moreover, "continuing claims" – those who have been collecting unemployment for at least two weeks – are now at 19.3 million; down from a peak of nearly 23 million.

- On June 5th, the Bureau of Labor Statistics released its monthly non-farm payroll survey data. The report indicated that the economy added 2.5 million jobs in May: the largest one month increase in the history of the series (seasonally adjusted data is available back to January of 1948). This was a welcome sight considering the fact that the labor market not only beat the consensus of dour expectations of an additional 8 million jobs lost but also showed signs of recovery after a very rough April. May's unemployment rate dropped to 13.3% from 14.7% in April.

  The jobless claims and non-farm payroll data are encouraging signals that jobs are indeed returning as state economies begin to reopen.

- On April 28th, the Conference Board released their monthly Consumer Confidence Index. The index declined from 118.8 in March to 86.9 in April.

Consumer Confidence Index
(March-April)

- A transportation research firm released a report indicating that April yielded the lowest number of Class 8 truck orders in the modern era. Their study remarked that May orders will be critical for not just the commercial industry, but the overall economy altogether. This transportation research firm anticipates the recovery to take a gradual trajectory with characteristics of both "L" and "V"-shaped curves. They also forecast 2021 as a recovery year, 2022 as a growth year and 2023 as a banner year.

- The non-partisan Congressional Budget Office is presently forecasting Q2 GDP to decline by 38.7% followed by subsequent rebounds of 22% and 11% for the quarters to follow in 2020. As of June 9th, the Atlanta Branch of the Federal Reserve Bank's "GDP Now" tracker projects a -48.5% drop in GDP during Q2.

- A Wall Street research firm recently forecasted a 27.3% decline in Q2 GDP followed by subsequent quarters of growth at 9% and 6.4% respectively. That same firm's six-month trucking pricing outlook survey revealed that sentiment around rate expectations are at a low not seen since 2015. They also see similar trends on the demand side of the equation, as well: the pandemic has diminished demand expectations to lows never seen in the history of the firm's survey (which commenced in 2013). Moreover, that same study has found that truckload spot rates have fallen 17% in Q2 thus far and are down 8% on average in 2020. Weaker truckload spot pricing continued to bleed into the contractual market – average truckload revenue per mile declined at a rate of 1.9% in March and 2.3% in Q1.

- The Cass Truckload Linehaul Index, a measure of per-mile linehaul rates, declined 7% year-over-year in April: the worst drop in the last 15 years.

- However, a June 8th market update from a national bank's analysis of the trucking sector revealed some signs of recovery in freight markets. Their tracking of weekly indicators in trucking (e.g. spot rates) showed that momentum has been positive for five consecutive weeks. Moreover, spot freight loadings have increased over the past six weeks as spot rates have recovered gradually from multi-year lows across trailer types. They expect April to be the bottom of the truck and trailer order cycle.

OUR OUTLOOK

Before the onset of the pandemic, some industry forecasts predicted an inflationary spot market entering 2020 due to a slump in truckload capacity resulting from carrier exits. As we observed in our initial forecast, the COVID-19 economy will most likely exacerbate those anticipated carrier bankruptcies. **We suspect that "slow data" (released in July) in the form of monthly and quarterly reporting around consumption, industrial production, truckload volumes, and carrier bankruptcies will soothe much of the anxiety resulting from the rapid volatility in "fast data" – the daily reporting of spot rates, shipper and carrier sentiment, and so on.** Notwithstanding any flare-ups of cases and hospitalizations, Q3 of 2020 will usher in a sense of relief and resolve as the country focuses on recovery – confident that the worst very well may have passed.

Once months of plummeting industrial activity give way to an intentional, but moderate recovery, another round of freight market volatility will occur as the country tilts back toward consumption patterns observed before the pandemic; albeit at a diminished degree of spending. For example, consumers will have to make their own case-by-case appraisals of how often to dine in restaurants versus continuing to rely on groceries or home delivery.

A reopened economy with bolstered industrial activity means an ever-growing volume of freight that has to be moved. The degree to which the preceding months of declining freight volumes and compressed freight rates has winnowed carrier capacity will ultimately determine just how inflationary freight rates will become. **We agree with those who predict a slow-but-potent recovery for the remainder of the year – something that lays the foundation for unbridled growth in 2021. However, we do believe that even the steadiest recovery will have stark ripple effects for shippers and carriers alike.**

Here's one other critical data point that reinforces our view. The operator of one of the trucking industry's largest network of load boards, DAT Solutions, reported that for the week ending May 24th, the number of posted loads declined by 16.5% (from the week before) while truck posts, a proxy for truckload capacity, dropped by 29%. Consequently, shippers and brokers paid a premium to secure truckload capacity prior to Memorial Day weekend.

-16.5% Posted loads declined for the week.

-29% Truckload capacity declined with rates increasing by a premium.

That's a good indicator that the loads-per-truck ratio is beginning to build due to capacity coming out of the market. Moreover, a 4,000-truck holding company (Comcar Industries) filed for bankruptcy recently. A handful of other small carriers have also exited recently. We still anticipate many more bankruptcies to come however we are confident that the Paycheck Protection Program portion of the CARES Act passed in April has provided a lifeline to carriers who otherwise would have filed for bankruptcy by now.

The coming reduction of capacity at carriers that are still operating will also be impactful in the near term, as well. Involuntary reductions in fleets through bankruptcies will be compounded by voluntary truck reductions at those carriers that are able to maintain operations through this time.

Just as in our prior forecast, we do expect to see a fair amount of capacity come out over the next couple of quarters.

BETTER DAYS ARE AHEAD

At the conclusion of our prior forecast, we observed that the ultimate impact of COVID-19 will be driven, greatly, by psychological factors – how consumers (and purchasing managers) “feel” once we’re on the other side of this. Even the most rational decisions in this era will be tinged with a bit of anxiety. Moreover, several months of economic uncertainty can be wearying for even the most resilient people. These are trying times for all of us. It’s worth reinforcing that better days are ahead, and perhaps even sooner than we anticipate. Again, the current economic climate isn’t a result of structural flaws due to fiscal or regulatory policy. Our country has asked each and every one of us to make extraordinary sacrifices in order to preserve the health of our communities. The time will come when we’ve beaten this pandemic and can turn all of our energy to rebuilding our economy and restoring what was lost.

COVID-19 is a story of valleys – but there will also be peaks. As you stay safe, stay calm and make the best decisions possible in the midst of unprecedented uncertainty, do remember that you’re not alone in any of this. There are a great many people who appreciate you and your colleagues’ diligence and strength throughout this crisis. Logistics and transportation professionals across the country have contributed greatly to the preservation of our health and quality of life; and we have all done this difficult work with minimal rest and comfort.

We’re grateful for the privilege to work together amidst one of the most difficult times in our nation’s history. We’re looking forward to being right there with you during one of the greatest recoveries in our history, as well.

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