FNBO TRANSPORTATION UPDATE

ECONOMIC UPDATE Q1 2023

In Q1 of 2023, Nominal and Real Gross Domestic Product (GDP) continued its third consecutive quarter of lower growth. Increases in activity were primarily from growth in consumer spending with goods driven by motor vehicle sales and services driven by health care and food service expenditures. Offsetting these increases were decreases in private inventory investment, mainly machinery and other transportation equipment as well as reduced residential investment in single family construction, according to the U.S. Bureau of Economic Analysis. The data shows that the economy is slowing and inflation, while persistently high, is subsiding.

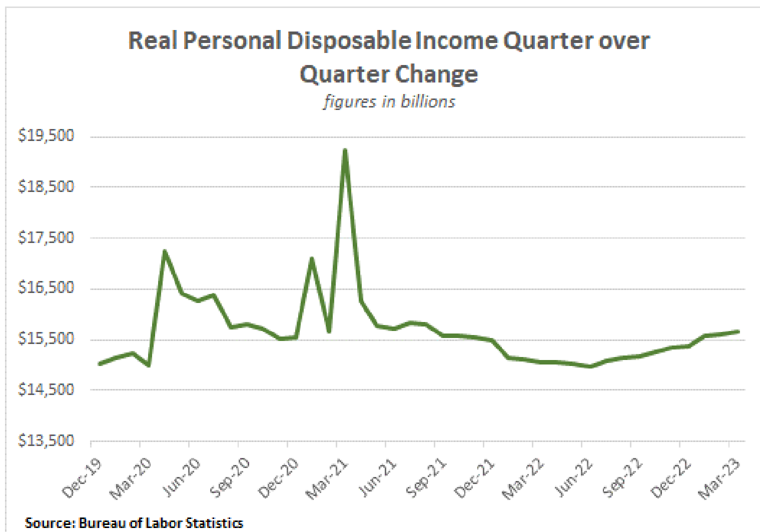
REAL GROSS DOMESTIC PRODUCT

Quarterly Percent Change from Preceding Period

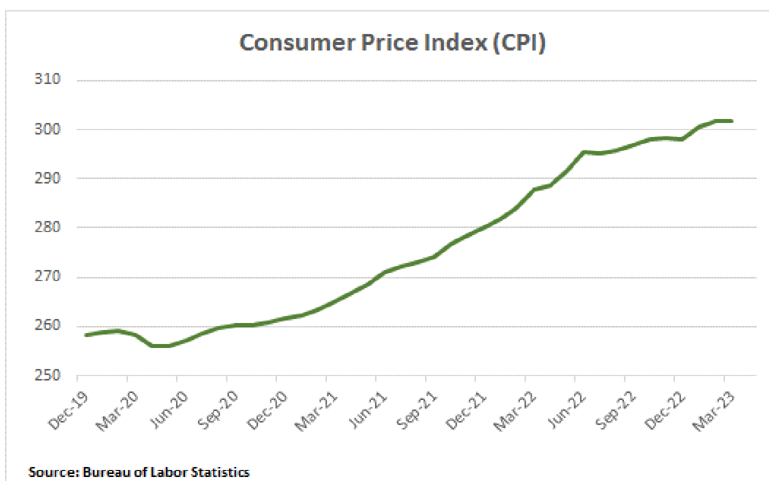
	Q1 2023	Q4 2022	Q3 2022
Nominal GDP	5.1%	6.6%	7.7%
Real GDP	1.1%	2.6%	3.2%
Personal consumption expenditures	3.7%	1.0%	2.3%
Goods	6.5%	-0.1%	-0.4%
Durable goods	16.9%	-1.3%	-0.8%
Nondurable goods	0.9%	0.6%	-0.1%
Services	2.3%	1.6%	3.7%
Gross private domestic investment	-12.5%	4.5%	-9.6%

Source: U.S. Bureau of Economic Analysis

Real disposable personal income, as shown in the chart, grew 8% in Q1, driven by increases in compensation and government social benefits, and a decrease in personal taxes. Personal savings were up slightly in Q1 at 4.8% compared to 4% in Q4 2022, per the Bureau of Economic Analysis. Total consumer debt was up 3% in Q1, which continues to trend with inflation, according to the Board of Governors of the Federal Reserve System. This shows that the underlying strength of the consumer as real income exceeded inflation with positive savings trends.

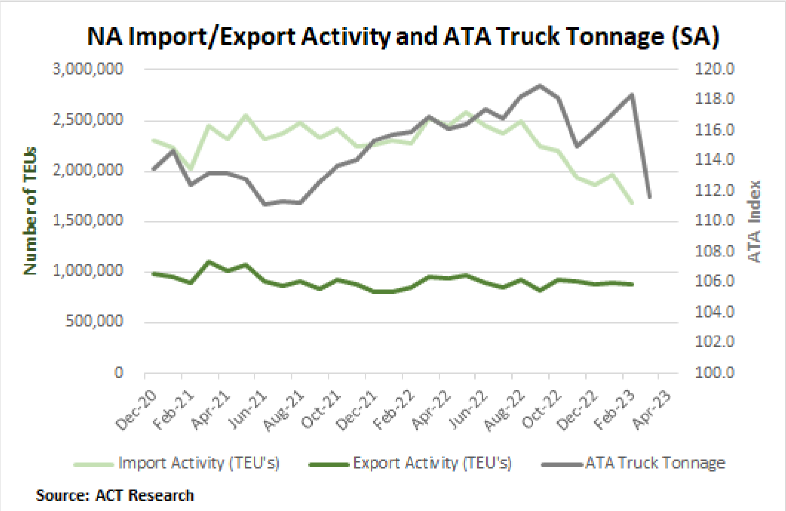


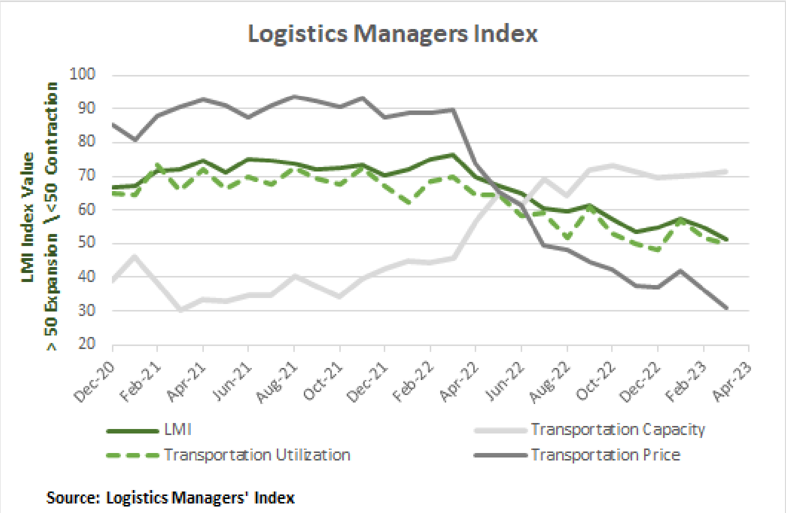
Inflation, measured by the Consumer Price Index (CPI), continued to decline in the first quarter, from 6.6% in January to 4.9% in March. Per the U.S. Bureau of Labor Statistics, the increase in CPI is mainly driven by shelter with energy costs decreasing. The index for all items excluding food and shelter continues to come down. The CPI was up 5% over the past 12 months, the smallest growth dating back to May 2021, per the U.S. Bureau of Labor Statistics.

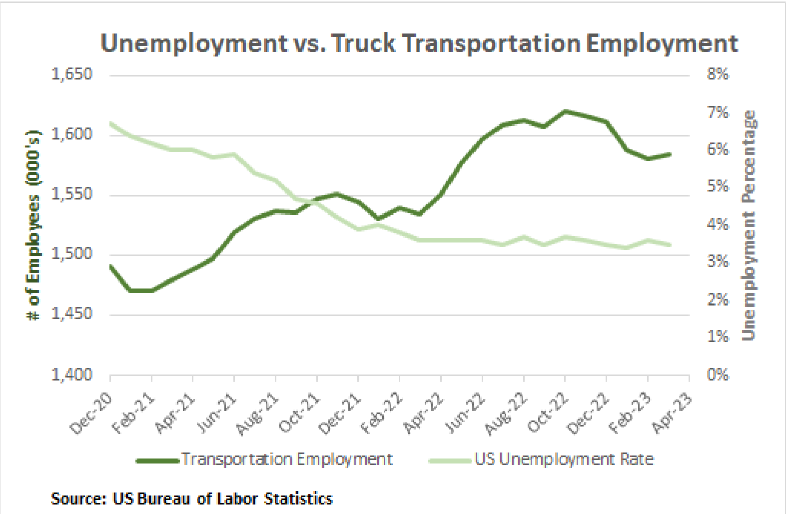


The labor market reported slower growth with a few large companies reporting mass layoffs. Most companies are using natural attrition to reduce employment levels. Companies reported the labor market becoming less tight with better employee retention, according to the Federal Reserve Beige Book.

FREIGHT DEMAND



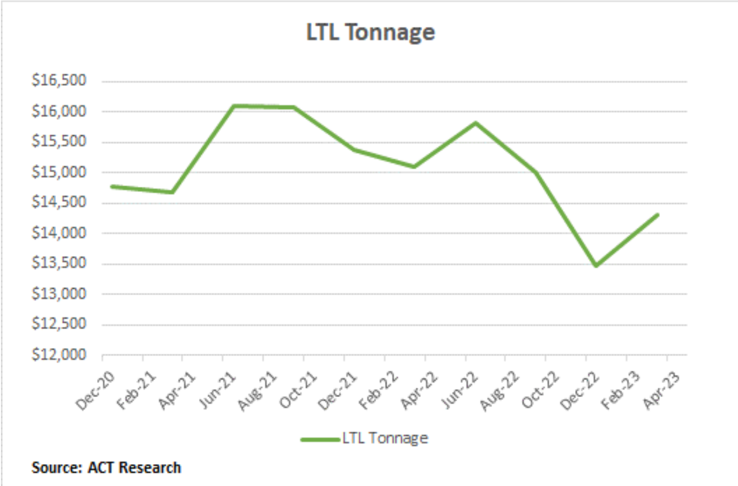




Trucking demand continued to fall off with truck tonnage now lower than pre-pandemic levels. Gains in January and February were attributed to volumes moving from the spot market. March data shows a decrease due to lower levels of home construction, manufacturing output and retail sales, per the ATA. Import activity continued to drop as companies look to reduce inventory levels and lower production due to Chinese New Year. The ACT expects import volumes to be down during most of the first half of 2023. Export container volumes decreased during the first two months of 2023; however, volumes are still up from 2022. ACT Research contributes this to a weakening of the dollar and likely some pickup as global trade lanes continue to get re-sorted due to the Russia/Ukraine conflict.

The Logistics Managers Index (LMI) highlights the inverse correlation between transportation capacity and prices with readings above 50 representing expansion in the industry. For March, the LMI was at 51.6, which indicates the industry is close to contraction, and is the lowest rating in the last 6.5 years. The decrease reflects the overall state of slower growth in the economy with increasing capacity driving prices lower.

Truck employment, in the bottom-left chart, is down from Q4 2022 as lower rates and decreasing volumes drive employees out of the industry. Per the U.S. Bureau of Labor Statistics, most of the employment decline has been in general freight trucking long distance employment. The national unemployment rate remained flat at 3.50%. LTL Tonnage improved in Q1 due to a weak market at the end of the year. Per ACT Research, LTL volumes are expected to decline through Q3 2023.



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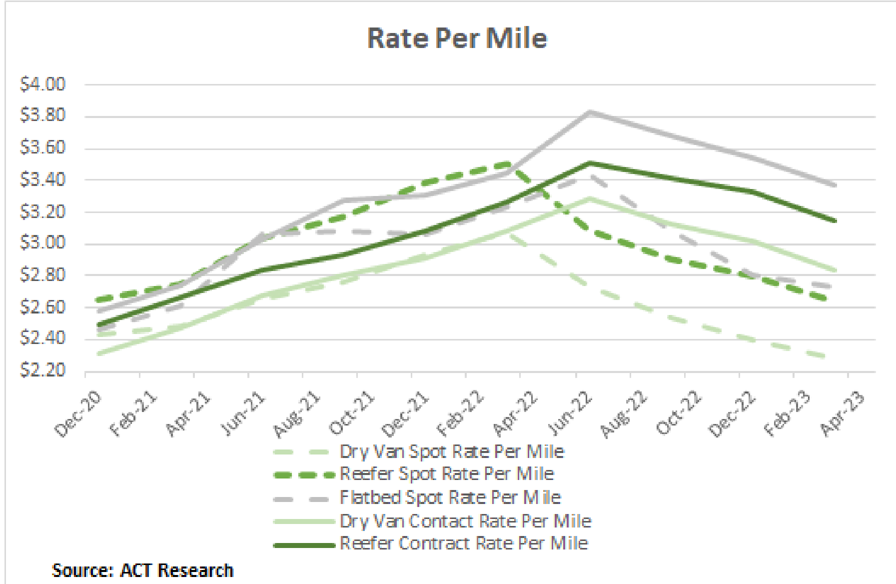
TRUCK RATES

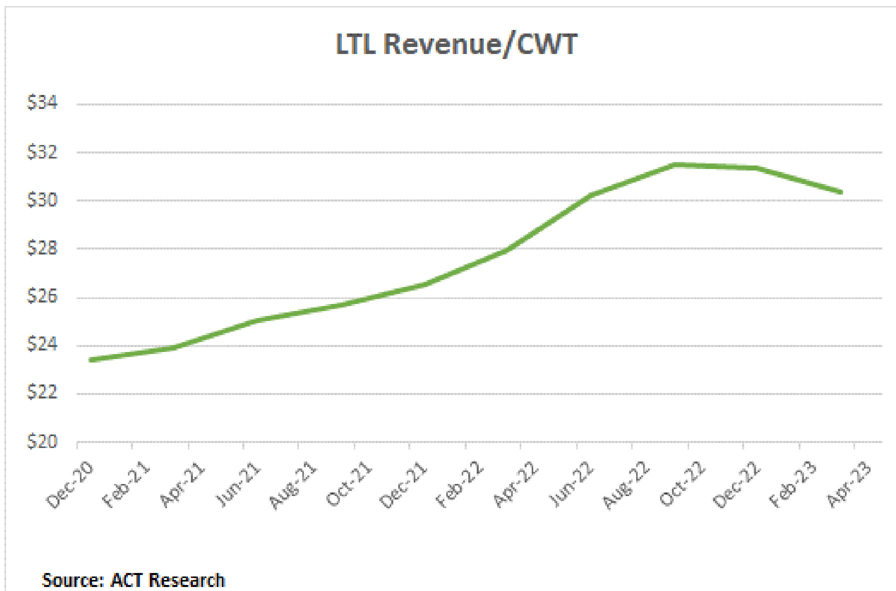
Shown on the right are contract and spot rates for dry van, reefer and flatbed. The decreases were driven by excess capacity and lower freight demands. Contract rate declines shown on the right averaged 5%. When netting fuel, that decrease dropped to 2% as fuel costs declined.

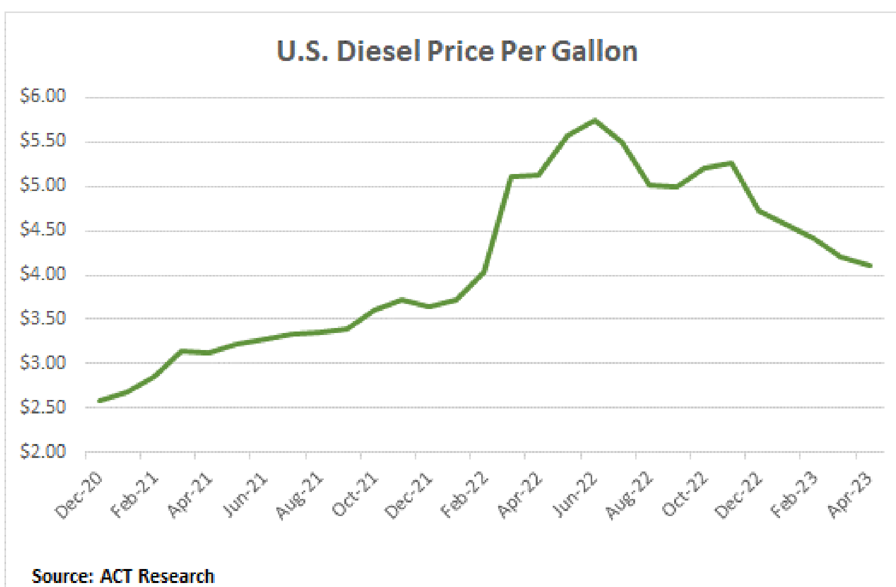
Spot rates continued to drop as import levels decreased and shippers optimized their freight. While both dry van and reefer rates reported decreases net of fuel, flatbed rates net of fuel were up 2%.

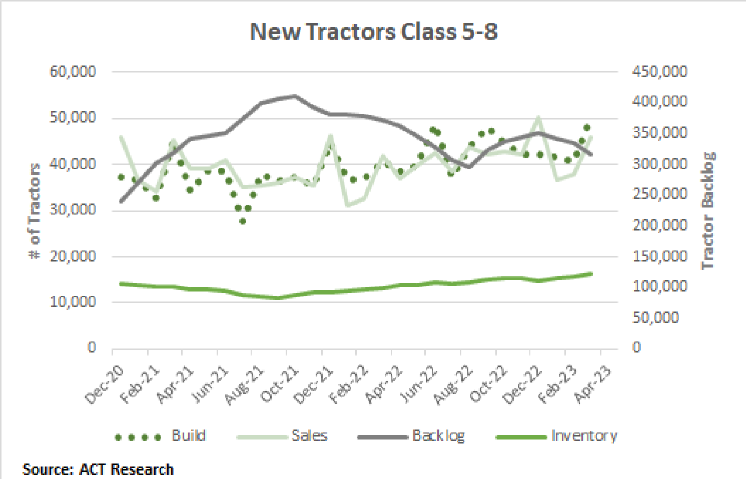
LTL costs were down 3%, as shown on the right, when netting fuel rates were up less than 1%. This is due to the high barriers to entry that allow LTL providers to hold prices as they invest in real estate, technology and equipment. Per ACT, LTL rates are expected to remain positive despite TL rate declines.

Diesel prices are down 13% in the first quarter with April data showing continued declines. However average prices for the quarter were up 2.7% when compared to Q1 of 2022. The decline in diesel prices is a result of lower demand domestically and internationally because of a slowing economy.

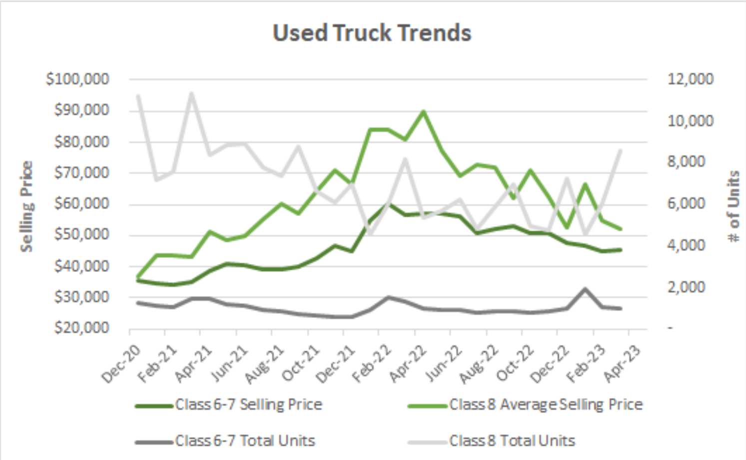




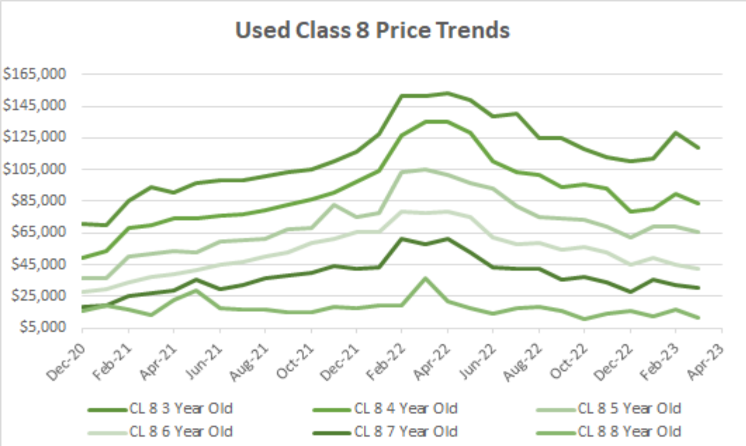




Source: ACT Research



Source: ACT Research



Source: ACT Research

TRACTOR TRENDS

Demand for new trucks is still strong, while backlog is down 4% from Q4 2022 due to the lack of available build slots, per ACT Research. Build levels were up 3% quarter over quarter and 16% year over year. Most of the gains took place in class 8 build levels that were up 4.3%, while class 5-7 were up less than 1%. Sales continue to follow build levels as there is little stock inventory being allocated.

Used class 8 trucks for sale increased 13% from Q4 2022 with the average price down 6%, mileage up 2% and age down 4%. This shows the number of trucks being turned in as operators exit the industry. The increased supply of used units drove prices down despite the average unit being newer.

Class 6-7 units were up 51% due to the seasonal spike, with units down 28% year over year. The selling price date for class 6-7 was mixed as prices were down 19% year over year with a 13% increase in average age. Class 3-5 units were up 7% year over year with selling price, mileage and average age relatively flat.

Used values of class 8 trucks decreased across most ages with the exception of 3-year-old trucks, which were up 5% per ACT Research. This gain can be attributed to continued shortages of new trucks driving demand for the gently used. The declines no longer appear to correlate with age as each category continues to find the bottom of the market.

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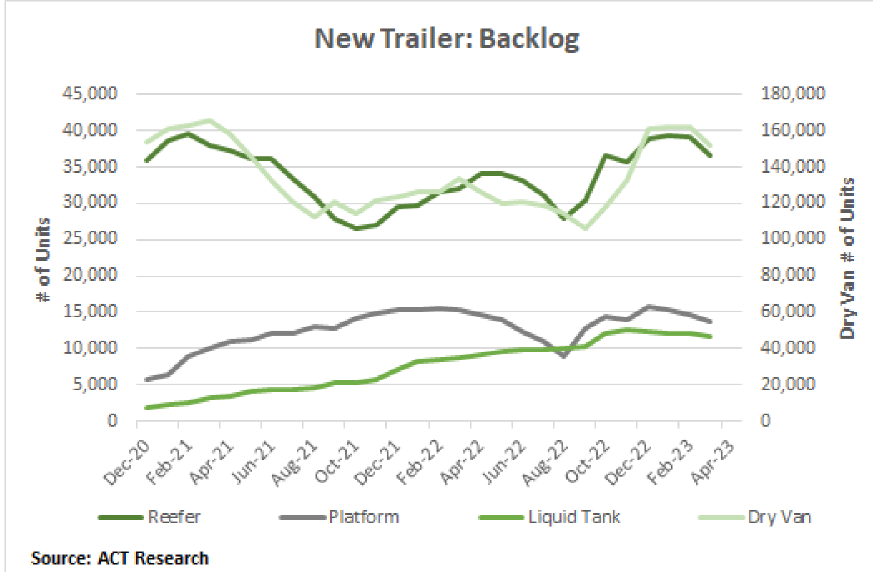
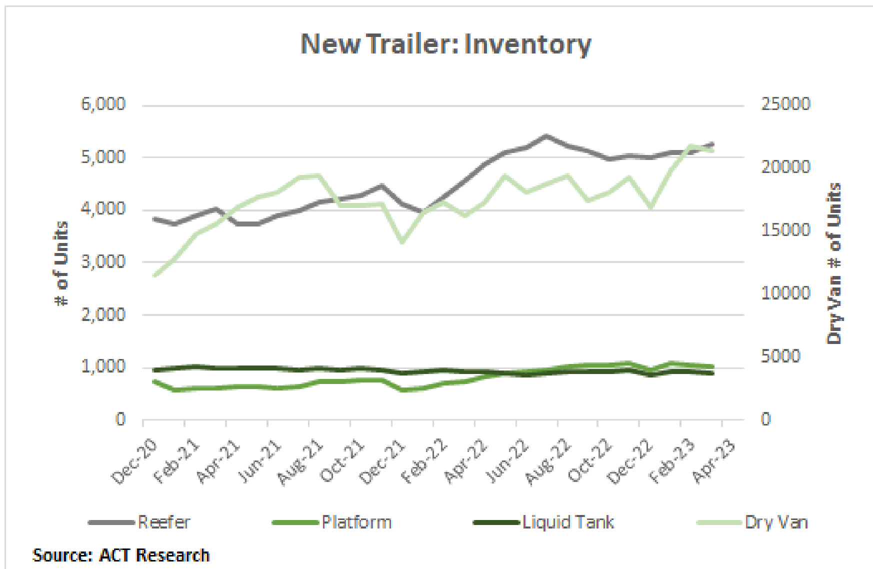
TRAILER TRENDS

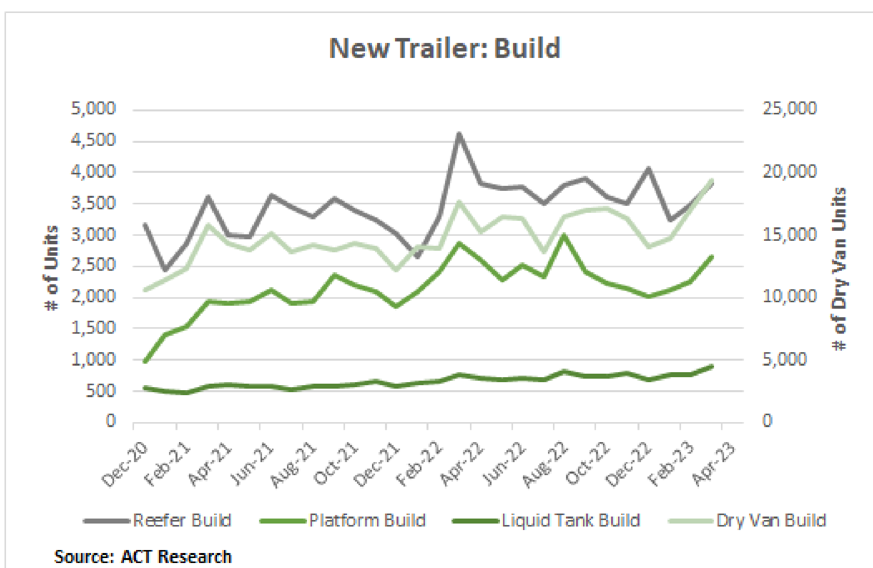
Trailer backlogs were up 10% in Q1 and up 20% year over year. Dry van and reefer reported increases while platform and liquid trailers reported decreases. According to ACT Research, cancellations were up 14% in Q1 and 188% year over year, but as a percentage of backlog are still only 1.24%. Per ACT Research, some 2023 order boards remain partially closed as OEMs try to control orders to avoid under delivery.

Inventory numbers were up 12% quarter over quarter and up 24% year over year for Q1, according to ACT Research. Dry van inventories reported the largest increase, up 16% and 26% respectively. Platform and liquid trailer inventories were up just slightly.

New trailer builds were up 6% in Q1 and up 7.5% year over year. Dry van, platform and liquid tank all reported increased quarter over quarter build levels. Reefer builds were down 6% in Q1 and flat over last year. ACT Research shows OEMs reported labor shortages are easing with some OEMs expecting improvement in material and parts availability.







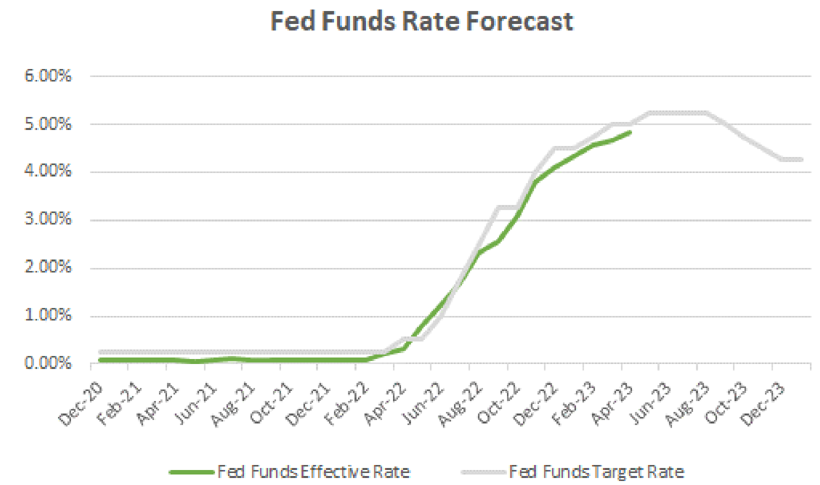
INTEREST RATE OUTLOOK

With signs of inflation easing and concerns about the lagging impact from monetary policy, the Fed reduced the level of rate increases with 25 bps adjustments in February, March and May 2023. This brings the total increase to 500 bps over the past 14 months. The central bank signaled that it may pause with the tightening cycle for interest rates while commenting that additional policy firming could be appropriate to achieve 2% inflation.

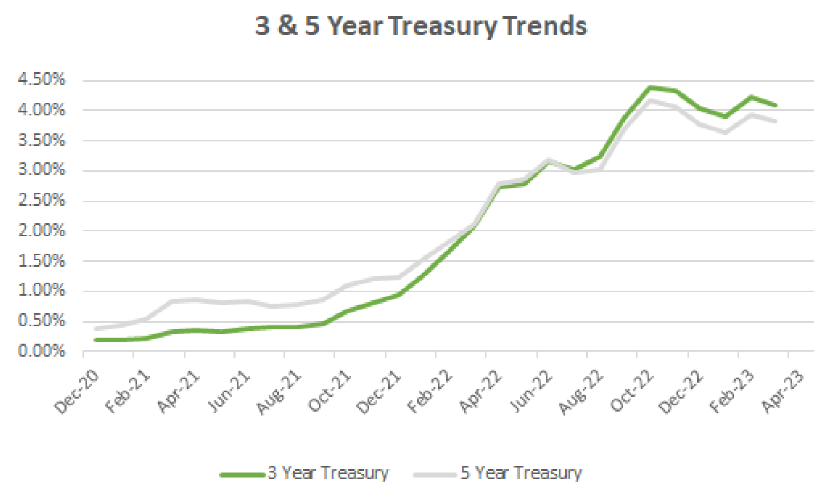
This is illustrated in the Fed Funds Rate Forecast chart that predicts the Fed will shortly pause in monetary policy and then pivot to rate decreases in the second half of 2023. The central bank is expected to continue to reduce its holding of securities, otherwise referred to as quantitative tightening, by reducing its holding of Treasury securities and agency debt.

The second chart shows the three- and five-year Treasury yields. Treasuries are a commonly used index for fixed rate loans. This index has been impacted by concern over the financial strength of banks as investors have moved cash to securities which has driven the yields lower. We would expect in response to this the spread over Treasuries will increase to adjust until the market corrects itself.

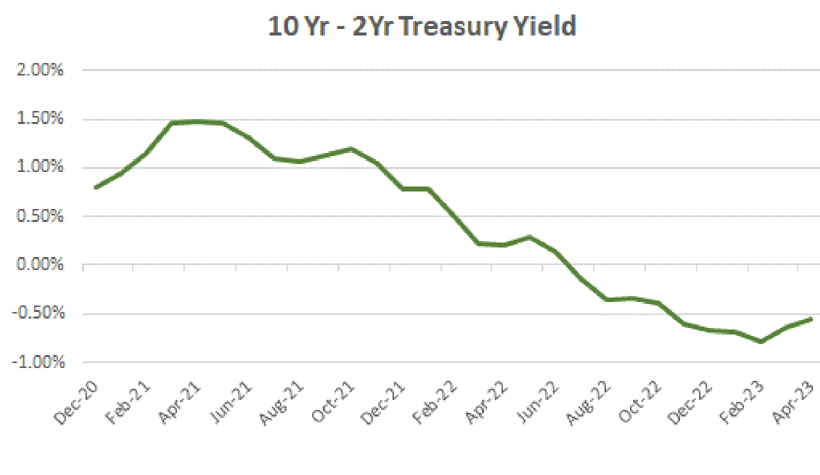
The last chart is the yield curve for Treasuries. Any value above 0% indicates it is more costly to borrow money for a longer term than a shorter term. Currently the yield curve is inverted averaging -0.7% for Q1 but is starting to flatten out with two consecutive months of improvement. This indicates the gap between short- and long-term borrowing rates is starting to decline. A yield curve inversion is historically a predictor of recessions.



Source Bloomberg Financial



Source: Federal Reserve Bank of St. Louis



Source: Federal Reserve Bank of St. Louis

Connect with the Expert, Aaron Martens

Aaron Martens is the Vice President of Transportation Banking for FNBO. In this role, Aaron supports closely held and family-owned businesses with comprehensive banking services. Aaron has been with the bank for over 15 years, with the majority of his experience in commercial banking. Aaron received a BSBA from the University of Nebraska Lincoln and an MBA from the University of Nebraska Omaha.

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