An Overview of Commercial Vehicle Demand in the NA Market

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What is Wrong With NA Market?

• We have been in a deep correction, rather than a fundamental shift in the relationship between freight and the trucks needed to haul it.

  – The economy of the coming decade will look a lot different than that of previous decades, but the relationship between population and consumption is unchanged.

  – There is no substitute for Class 8 trucks and tractors in getting the freight to market.
Flexibility is the Key

![Diagram showing the relationship between Cost and Flexibility for different modes of transport: Air, Rail, Water & Pipeline, and Truck. The diagram indicates that as flexibility increases, cost decreases.](image)
U.S. Logistics Spend
as a Percentage of GDP
1980 - 2008

Transportation Spending
Inventory Carrying Costs
Total Logistics Bill
This Cycle Will be Different

• U.S. economic growth will be slower
  • With property and equity prices under pressure, debt, rising taxes etc., U.S. consumers will have less discretionary income
    – House and personal use vehicles won’t be supersized

• Mexico, Canada will experience stronger growth
  • Demand for commodities, healthy banking system, strong loonie will boost discretionary incomes
  • Cheap peso and rising energy costs will accelerate manufacturing repatriation, large population

  – There is a strong relationship between manufacturing and heavy truck demand
Real Gross Domestic Product
Q/Q at SAAR
Q1'96 - Q4'11

Source: BEA, ACT Research Co., LLC: Copyright 2010

ACT U.S. Freight Composite
Q/Q at SAAR, Y/Y
Q1'97 - Q4'11(Actual through Q1'10)

Source: ACT Research Co., LLC: Copyright 2010
Fleet Profile

• Chronologically, the fleet has never been older
  • With many of the trucks in the market having gone through both 2001-2002 and 2008-2009, we believe that consumed age is below average

• By the end of 2010, the Class 8 population will have fallen further than freight, setting the stage for a rebound

• Country models indicate growing replacement demand in all three NAFTA markets
AVERAGE AGE:
U.S. Class 8 Active Population
1979 - 2015

AVERAGE AGE:
Canada Class 8 Active Population
1979 - 2015
REPLACEMENT:

NA Class 8 Active Stock

1990 - 2017

Units (000s)

- Exports
- Mexico
- Canada
- US

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Excess Capacity Heading to Shortage

U.S. C8 Pop. Relative to Economic Activity: Export Adjusted
1997 - 2011
Class 8 Population: Freight per Unit
1980 - 2015e

US$ Millions per Class 8


Periods of C8-Freight Equilibrium

Deregulation

+51% productivity in 5 years

44% in 13 yrs

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Used Truck Valuations

• Used truck values will be a key determinant of future fleet age profile

  – New truck values up $22k from EPA’04 to EPA’10 – Excluding taxes!
    • If used truck values do not rise to compensate for higher prices, truckers will have to keep trucks longer

  – Since the end of 2006 overcapacity has been a constant issue, thereby depressing used pricing
    • No guidance as to how pricing will react when capacity glut goes away
Used Class 8 Sales Gap: Average Selling Price vs. Estimated New Class 8 Price
January '03 - March '10  (Not Seasonally Adjusted)

$000s/Unit

New Price Estimate (Tractor Sleeper)

$95K
$100K
$108K
$117K

$ GAP: New - Used

Average Used Class 8 Price

Target $ Gap
Other Factors

• Trucker profitability
  – Tightening capacity in 2010 sets the stage for very strong profit recovery 2011-2013
    • Truckers reporting rapidly diminishing overcapacity
    • Credit availability should follow revenue & margin expansion
  – Depreciation allowance becoming a factor

• Exports & Mexico
  – Weak US$, will support exports above 92-03 avg.
  – Mexico: In addition to manufacturing boost, on track for emissions prebuy (EPA’07) in late 2011
TL Carrier Database:
Net Profit Margin
Q1 '97 - Preliminary Q1 '10
When Carriers Make Money…

TL Carrier Database:
Carrier Net Income & US Trailer Orders
Year over Year Percent Change
Q1'95 - Q1 '10
Depreciation

- Truckers depreciate tractors 6 or 7 years, with plans to sell at 4 or 5 years
  - Many truckers who thought they would be trading in 2008 and 2009 are still driving the same trucks
  - In 2010 and 2011, depreciation tax allowance runs out for older trucks.

- Back of the envelope math suggests replacing an out of depreciation truck with a new truck would generate ~$5k in tax savings
  - (((120k/6years)*60% depreciation rate)*40% tax rate)
Current Environment: Class 8

• Indicators all pointing in right direction in April
  
  • Orders: Surprise on high side in March and April
    » Reports that most of industry is building premandate deep into/through Q2
    » Trucker comments indicate rapid capacity tightening
    » Orders coming ahead of schedule for EPA’10 units

  • Backlog: Maintained in very tight band since early 2009
    » BL up 3.5k in April to 46.9k

  • Build: April UPD lowest in seven months
    » Ahead of previous expectations
    » Based on BL fill, Q2 build likely to fall between 34k-35k

  • Retail Sales: Seasonally strongest period of the year
    » Inventory still composed of premandate units

• Inventory: Units and INRS both fall in April
TOTAL CLASS 8: N.A. NET ORDERS
January '02 - April '10 (Not Seasonally Adjusted)
TOTAL TRAILERS: NET ORDERS
Year over Year Percent Change
January '02 - April '10

Units (000s)

Y/Y % Change

NET ORDERS: Monthly & 6 Mo. Avg.

Y/Y % Change (Right Axis)
TOTAL CLASSES 5-7: N.A. NET ORDERS
January '02 - April '10  (Not Seasonally Adjusted)
TOTAL CLASS 8 NA:
NET ORDERS (Trailing 12 Months) & BUILD

January '02 - April '10 (Not Seasonally Adjusted)
Medium Duty Trucks & Buses

• For trucks, it is all about housing
  • Site preparation companies & utilities
  • House building materials & contractors
  • Making a house a home

  • Most MD trucks stay within 50 miles of home
    – Relatively easy to defer replacement

  • MD truck market subject to right-sizing pressures
    – From above in ‘90s, from below in ‘00s

• Buses

  • School boards squeezed by diminished tax collection & higher fuel costs

  • School bus age maximums are mandated in all states
New Home Sales vs. CI 5-7 Truck Sales
Y/Y % Change of SAAR

Source: ACT Research Co., LLC, US DOC Census Bureau

Legend:
- NEWHOUS
- CI 5-7 TRUCK RS
- Poly. (NEWHOUS)
- Poly. (CI 5-7 TRUCK RS)
Forecasts

• Ramp-up to 2011
  • Lingering overcapacity dries up in mid 2010
  • Used truck prices rise rapidly through mid 2010
  • Credit log-jam eases as asset values & profits rise

• Forecast risks appears tilted to the upside
  • Above trend orders may be explained by continued premandate availability, but…
    • Economy continues to surprise on high-side
    • Truckers indicate rapid capacity tightening since February
    • Press releases for EPA’10 orders are becoming a common occurrence
N.A. Class 8 Production
1998-2015

Units (Thousands)
N.A. Classes 5-7 Production

1998 - 2015

Units (Thousands)