FTR | State of Freight
INSIGHTS

Weekly Transportation Update

Market Updates for Transportation Professionals

March 17, 2023

HEADLINE

Manufacturing output and retail sales were lackluster in February.

- Retail inventories were leaner in January, reducing prospects for a stronger correction.
- Housing starts and permits see solid increases in February.
- Van segments' spot rates reverse their gains from the prior week.
- STB approves Canadian Pacific-Kansas City Southern merger.

Overview

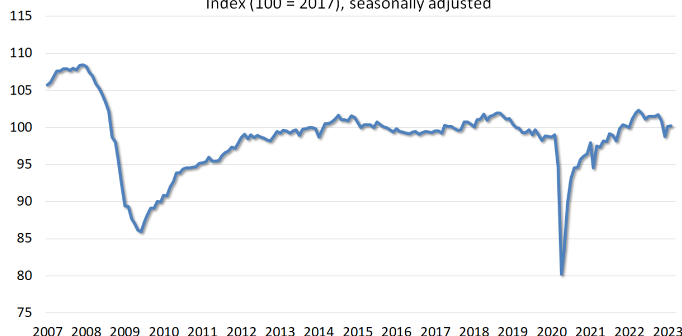
February is shaping up as a reversal of January in some respects with weak performance in the industrial and consumer sectors but strong gains in key residential construction metrics. Retail inventories were leaner in January, seasonally adjusted, reducing prospects for further correction.

Consumer inflation overall remained tamer than it had been in much of 2022, but falling energy prices were key. Meanwhile, pricing in key services like shelter continues to rise.

Economic indicators are not signaling any big near-term change in the status quo, but a potential banking crisis raises concerns over the economy and the Federal Reserve's monetary policy. A troubled financial sector could force the Fed to moderate its aggressive anti-inflation campaign.

Industrial production and manufacturing

Industrial production (IP) was flat m/m in February, but the Federal Reserve revised prior estimates slightly lower back to September. A 0.5% increase in utilities output largely offset a 0.6% decrease in mining. IP was down 0.2% y/y but remained 0.9% above the pre-pandemic month of February 2020.



Manufacturing output ticked up 0.1%, but performance was flat versus the initial January estimate due to a slight downward revision. Output was down 1% y/y but up 1.2% versus February 2020.

Motor vehicle and parts production edged down 0.3% in February but was up 10.8% y/y. Output was essentially even with February 2020.

IP figures could look significantly different soon. The Federal Reserve plans to issue its annual revision of IP indexes later this month.

Retail sales

Retail and food services sales in current dollars ticked down 0.4%, seasonally adjusted, in February after an upwardly adjusted 3.2% jump in January. With that upward revision, the small decline resulted

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Key Takeaways

- Manufacturing output was stable in February.
- Retail sales ease in February after January jump.
- The retail inventory correction might be ending.
- Housing starts and permits surged in February.
- Core CPI growth was a bit stronger in February.
- Producer-level inflation eased due to food, fuel.
- Revision shows record truckload PPI drop.
- Mortgage rates fall for the first time in six weeks.
- Diesel prices continued to fall in the latest week.
- Van spot rates give back the prior week's gains.
- CP-KCS merger wins STB approval as expected.
- Intermodal volumes take another step down.
- Rail carload volumes weaken due mainly to coal.

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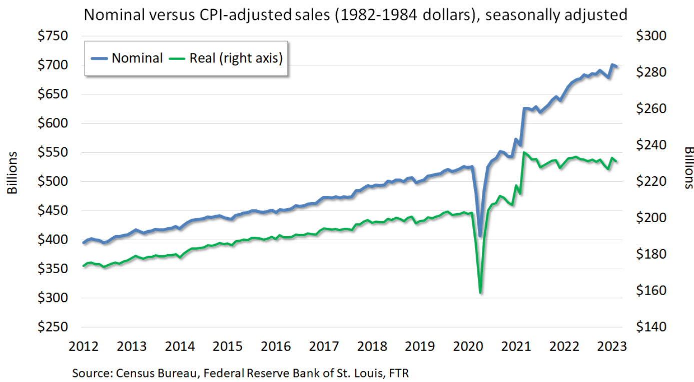


in a February sales level that was marginally higher than the initial January figure.

Non-store retail saw the largest seasonally adjusted increase at 1.6% m/m, although sales were down 6.9% on a not seasonally adjusted basis. Other large retail sectors seeing gains included general merchandise stores and food and beverage stores, each of which rose 0.5%, seasonally adjusted.

Department stores saw the largest decrease at 4%, although that followed an upwardly revised 18.1% jump in January. All retail sectors that saw declines m/m during February had seen larger increases in January. For example, motor vehicle and parts sales were down 1.8% in February, but the upwardly revised January gain had been 7.1%.

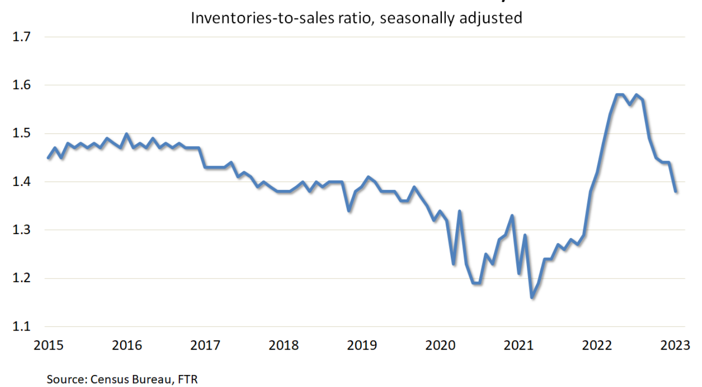
Inflation was a factor in keeping retail sales from falling more than they did. According to data from the St. Louis Federal Reserve, real retail and food service sales declined 0.8% in February. Sales in current dollars were 32.6% higher than February 2020. Sales adjusted for inflation were 14% higher.

Inventories

The upward revision in motor vehicle and parts sales in particular for January resulted in an even-leaner inventory situation for retail than FTR had estimated. Based on initial inventory and sales data for January, we had expected the total retail inventories-to-sales ratio to decline to 1.24 from 1.26 in December, seasonally adjusted. The formal initial release of the data showed the total retail ratio at 1.23. The ratio of inventories to sales in retail excluding automotive came in as expected at 1.15.

With weak inventory growth and strong retail sales in January, most retail sectors naturally saw declines in their seasonally adjusted inventories-to-sales ratio. The inventories-to-sales ratio for general merchandise has been falling since peaking in late summer and in January declined to 1.38, which is the leanest since late 2021 and in line with typical pre-pandemic ratios.

Barring a sharp decline in sales, the current ratio for general merchandise implies that any inventory correction is basically over, at least in that broad sector. One retail sector where inventories remain highly elevated relative to sales is building materials and garden supplies dealers, although the ratio ticked down slightly in January.



Residential construction

The housing sector in February showed further signs of possibly bottoming out. Housing starts rose 9.8%, seasonally adjusted, in February for their strongest m/m increase since March 2021, which had seen an abnormally large jump due to extremely cold weather the month before.

Starts of single-family homes moved up 1.1%, but the real strength was in starts of units in multi-family buildings with at least five units. Multi-family starts jumped 24.1%. Single-family starts were still 20% below the February 2020 rate, but multi-family starts were more than 18% higher.

Permits authorized for future construction saw even stronger growth than did starts, soaring 13.8% – the largest m/m gain since July 2020. Single-family permits saw their first increase in a year and remain 22% below February 2020. Multi-family starts, which

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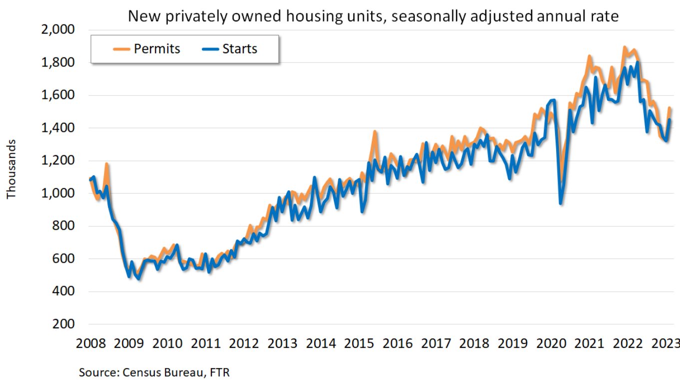

have been more volatile, jumped more than 24% and are nearly 69% above February 2020.

Housing completions rose more than 12%. The number of homes under construction has clearly peaked, although multi-family units under construction continue to rise steadily while single-family homes under construction continue to fall steadily.

Consumer inflation

A decline in energy prices and a deceleration in food price increases resulted in slightly tamer consumer inflation during February. The Consumer Price Index for all items rose 0.4%, down from a 0.5% gain in January. The 12-month change in the all-items CPI was 6%, down from 6.4% in January.

A decline in utility prices helped keep prices for services in check, but services inflation otherwise accelerated slightly due to prices for shelter and transportation services. The 0.8% increase in shelter matches December and two months in 1990 for the strongest m/m increase since 1985.

With food and energy moderating February's all-items inflation, CPI less food and energy accelerated a bit, ticking up 0.5% for the largest m/m gain since September. The 12-month change was 5.5%, down from 5.6% in in January.

Although the monthly increase in the CPI excluding the volatile food and energy sectors is still higher than it was before the pandemic, services are the real issue. The 12-month change in services excluding energy has been rising steadily since the fall of 2021 and is now 7.3%. Conversely, the 12-month change for commodities less food and energy has been declining mostly steadily for a year and is now down to just 1%.

Producer inflation

Drops in final demand pricing for food and energy were largely responsible for a 0.1% decrease in the Producer Price Index for final demand in February. The 2.2% drop in final demand foods is the largest since June 2020 and the third largest in the data, which goes back to late 2009.

Producer-level inflation was mild in February even excluding volatile sectors. The PPI for final demand less food, energy, and trade services ticked up just 0.2%, which matches several months in the second half of 2022 as the smallest gain since May 2020.

Within freight transportation services, the most notable development was a major downward revision in the PPI for general freight truckload in January. The initial estimate had been a 3.3% decrease from December. With the revision, the January drop was a record 8.2%. The general freight truckload PPI declined another 1.3% in February.

The PPIs for other trucking segments also were down in February but by smaller degrees. The PPI for long-distance specialized trucking declined 0.4%. The LTL PPI was down 0.7%. Neither sector saw the sharp decline general freight truckload had seen in January. Long-distance specialized eased 0.8% in January while the LTL PPI had risen 3%.

February's decrease in the rail intermodal PPI was more in line with that of general freight truckload at 1.5%. After falling in only two months between July 2020 and July 2022, the rail intermodal PPI has fallen in five of the past seven months.

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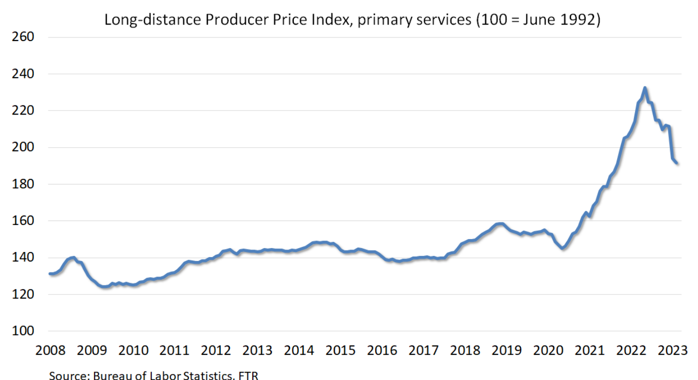

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The trailer PPI eased 0.6% in February following a 1.4% decline in January. However, trailer pricing might not continue to fall if the PPIs for key materials are any guide. After steady decreases recently, the PPIs for steel mill products and lumber increased in February, and the aluminum PPI rose for the third straight month.

Mortgage rates

Mortgage rates eased for the first time in six weeks. The average rate on a 30-year fixed-rate mortgage fell to 6.6% from 6.73% in the prior week. Freddie Mac attributed the decline primarily to turbulence in the financial markets.

Diesel and petroleum prices

The national average price of diesel fell 3.5 cents to $4.247 a gallon during the week ended March 13. Diesel prices have fallen nearly 38 cents in the past six weeks and were exactly $1 lower than they were a year ago. Prices in the latest week were down in all regions except for the West Coast where they moved up very slightly.

One notable milestone is that the average price of diesel in the Gulf Coast region has now dipped below $4 a gallon for the first time since the end of February last year immediately before the historic $1.15 surge in the first two weeks of March.

At least in the near term, diesel prices do not seem to face significant upside pressure. Distillate production and inventories declined a bit in the latest week, but so did crude prices. On March 15, West Texas Intermediate closed at $67.61 a barrel, which is the lowest price since early December 2021.

Trucking

A week after posting their strongest gains of the year, broker-posted dry van and refrigerated spot rates in the Truckstop system fell by about the same amount during the week ended March 10 (week 10) that they had increased the week before. Meanwhile, the flatbed segment recorded its largest single-week drop in rates since August.

The total broker-posted spot market rate declined just over 5 cents. Total rates were about 20% below the same 2022 week but more than 2% above the five-year average.

Dry van spot rates decreased about 5 cents. Rates were almost 27% below the same 2022 week and nearly 8% below the five-year average.

Refrigerated spot rates declined about 4 cents. Rates were about 25% below the same 2022 week and nearly 6% below the five-year average.

Flatbed spot rates fell nearly 8 cents for the largest weekly decline since week 33 of last year. Rates were about 19% below the same 2022 week but 5% above the five-year average for the week.

Spot volume

Spot load activity fell more than 5% after surging nearly 17% during the prior week. Volume was almost 57% below the same week last year and about 30% below the five-year average. Volume in the van segments was the lowest since June 2020 except for Thanksgiving week last year.

Dry van loads decreased nearly 11%. Volume was almost 56% below the same week last year and about 34% below the five-year average for the week.

Refrigerated loads fell 11%. Volume was about 59% below the same week last year and nearly 36% below the five-year average for the week.

Flatbed loads dipped more than 1% after surging more than 27% in the previous week. Volume was nearly 60% below the same week last year and more than 31% below the five-year average.

For more on week 10 spot metrics for truck freight, visit https://www.ftrintel.com/spotmarketinsights.

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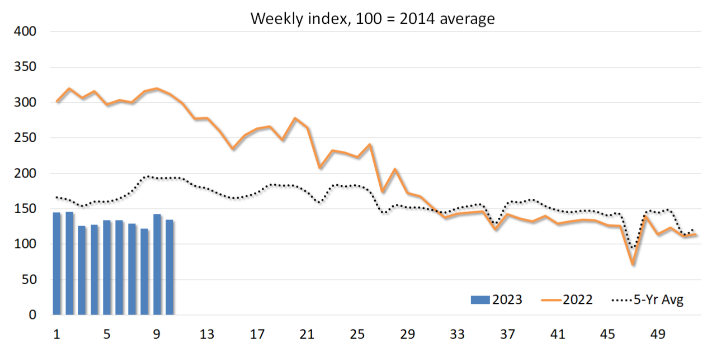

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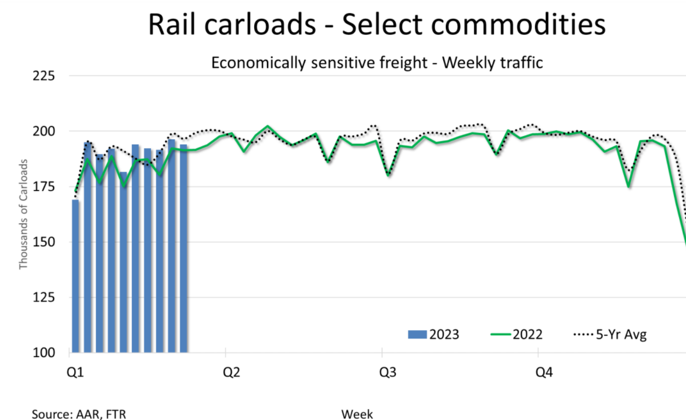
Rail/Intermodal

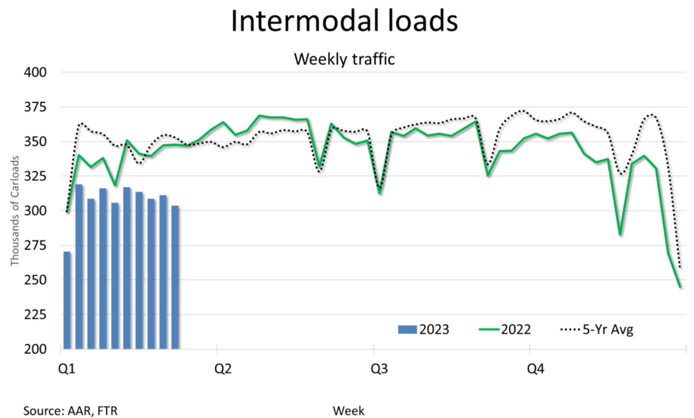
The Surface Transportation Board this week approved the combination of Canadian Pacific and Kansas City Southern after a two-year regulatory review and consultation process that included significant environmental review. The transaction will become effective on April 14, at which point CP will control the operations and lines of Kansas City Southern and Kansas City Southern de Mexico.

The board imposed relatively few conditions on the transaction aside from what CP itself agreed to in private settlements and in its application. The board did, however, impose a record seven-year oversight period on the combined carrier to ensure that representations it made about truck-to-rail conversions, rail service, and train counts all come to fruition.

One condition STB imposed that could prove meaningful is that the combined carrier must produce upon request by a shipper a justification for any rate increase higher than inflation at open interchange points on the day of approval. The board believes this is a concrete way to hold CP to its pledge to keep gateways open on commercially reasonable terms going forward.

The lack of any of the conditions requested by the Class I carriers means that Union Pacific and the newly combined carrier would need to collaborate to solve problems in the Houston terminal area if train counts increase significantly. Houston proved to be one of the major pain points in the UP-SP merger of the 1990s and it could prove significant in this transaction as well given the nature of KCS' operations over UP tracks in this region.





Automotive, intermodal, and agriculture are the three commodity groups that are expected to see the biggest potential gains from the transaction, but time will tell how real those gains prove to be. Chemicals traffic could also benefit from the transaction, but how much they benefit will be more dependent on the political climate in Mexico than the merger transaction itself.

Intermodal and carload volumes

Overall intermodal volumes took another step down in the latest week, to end just above 300,000 units in the week ended March 10. The segment continues to be battered by a combination of lower import levels, port shifts toward east and Gulf coast ports, and weak active truck utilization. Unfortunately for the intermodal space, there appears to be no end in sight for any of those headwinds. There remains no discernable progress on a west coast port labor contract, retailers said in recent conversations with investors that they expect a downshift in consumer spending, and the truck market shows no signs of increasing in the near future.

Carload volumes declined in the latest week as coal traffic gave back its gains from two weeks ago. Coal declined significantly in the latest week as low natural gas prices and export coal prices weigh on the sector. Coal volumes likely will be sharply weaker in 2023 than they were over the last two years.

Other sectors largely held steady or moved weaker. One of the few bright spots in carload in the latest week's numbers include pulp and paper, where volumes ticked up for the second week in a row and are now at their historical five-year average. This is a good sign for the pulp and paper business that has struggled to post volume stability, let alone growth, over the last year.

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