

THE LOGISTICS COUNCIL

Milwaukee Round Table

February 15, 2011

CSA and the State of Transportation



Steve Van Kirk
Vice President, Intermodal
Commercial Management

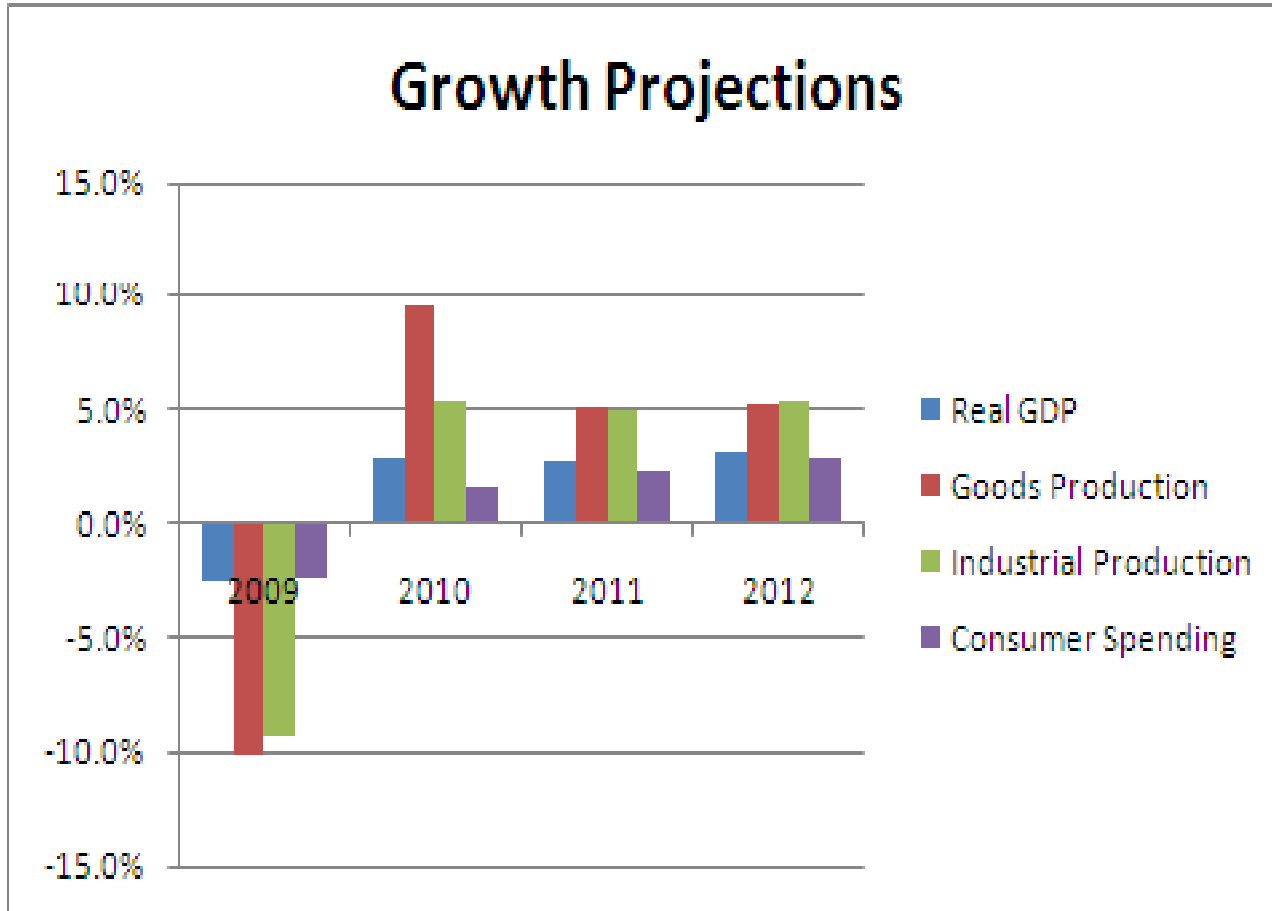
The State of Transportation

- Transportation Demand
- CSA
- Hours of Service Regulations
- Truckload Capacity
- Impact Upon Shippers

2011 Transportation Demand



MAJOR INDICATORS SHOW ECONOMIC GROWTH IN 2011

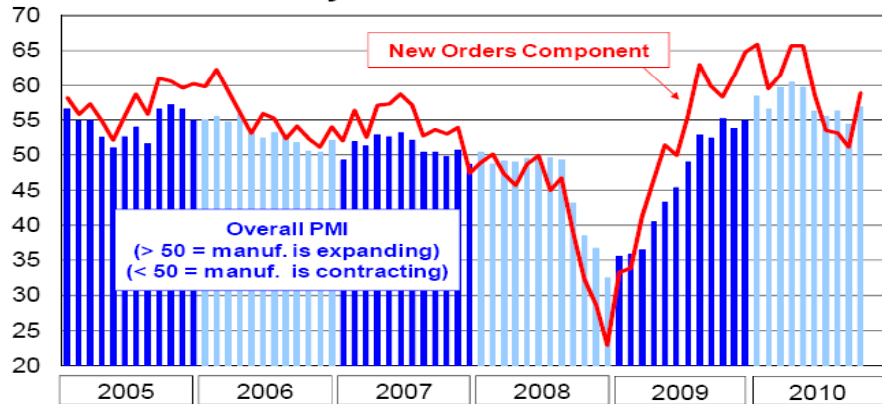


Continued growth in Goods Production, Industrial Production and Consumer Spending will lead to a substantial increase in the amount of freight that needs to move in the next few years.

Sources: FTR Associates, Witte Econometrics, Bureau of Economic Analysis

OTHER ECONOMIC INDICATORS OF FREIGHT VOLUMES ARE IMPROVING

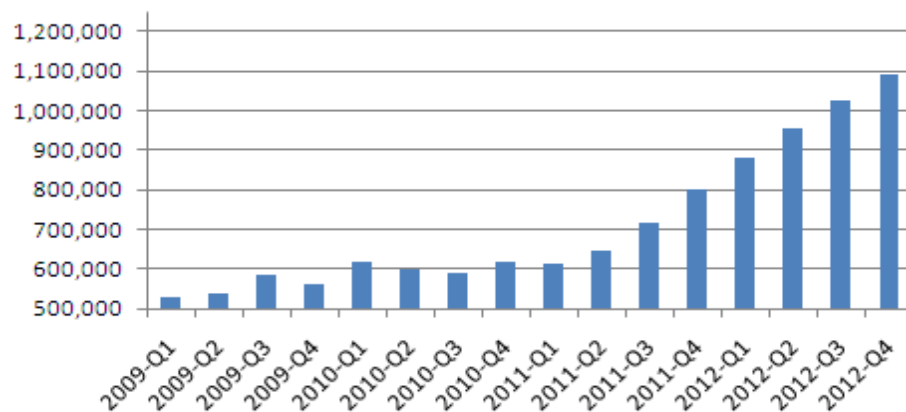
Purchasing Managers Index:
January 2005 - October 2010



Data are seasonally adjusted. Source: Institute for Supply Management

New orders are a leading indicator of industrial production, which drives shipping volumes. The Chicago regional PMI hit the highest level since 1988 in December!

Monthly Housing Starts

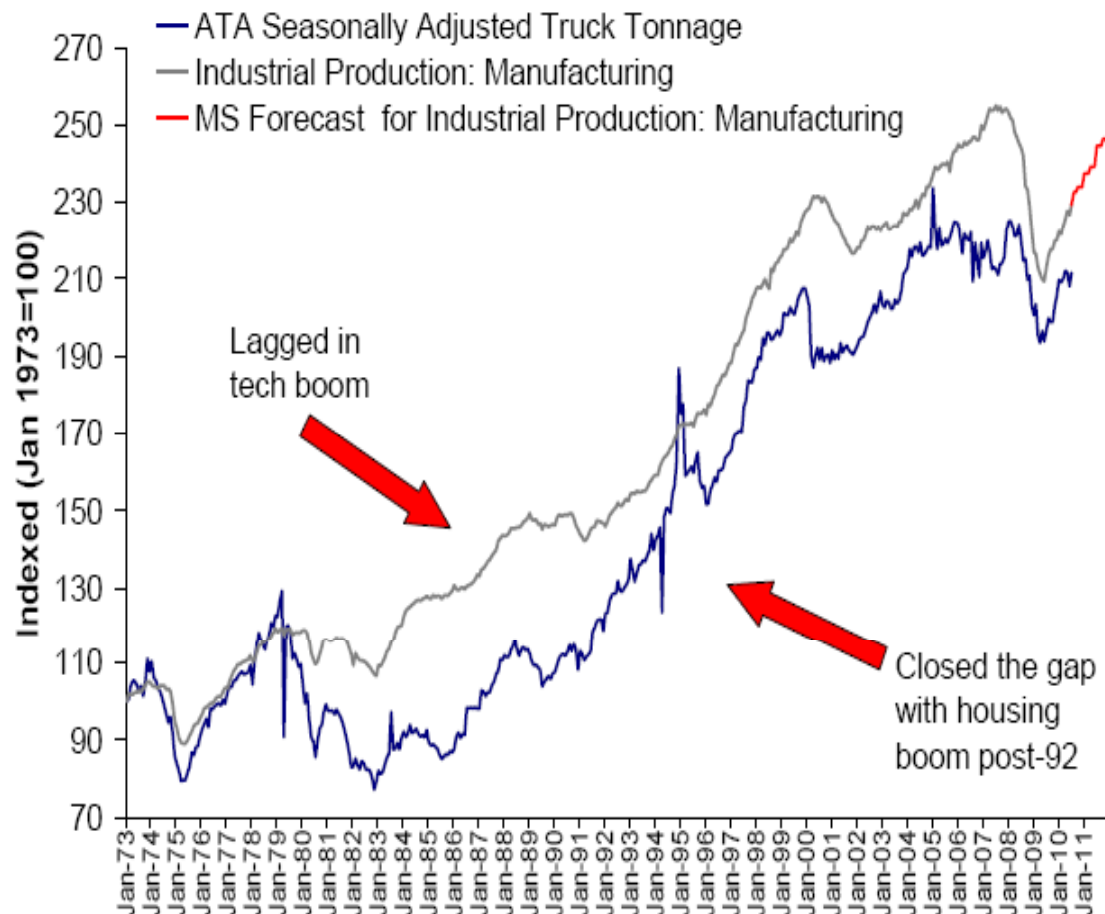


Sources: FTR Associates, Witte Econometrics

Housing starts not only create freight for the homes that are built, but are a corollary statistic for total home sales which creates freight through new home updates

INDUSTRIAL PRODUCTION IS A STRONG INDICATOR OF TRUCK TONNAGE

ATA Truck Tonnage vs. Industrial Production: Manufacturing



Source: ATA, Morgan Stanley Research

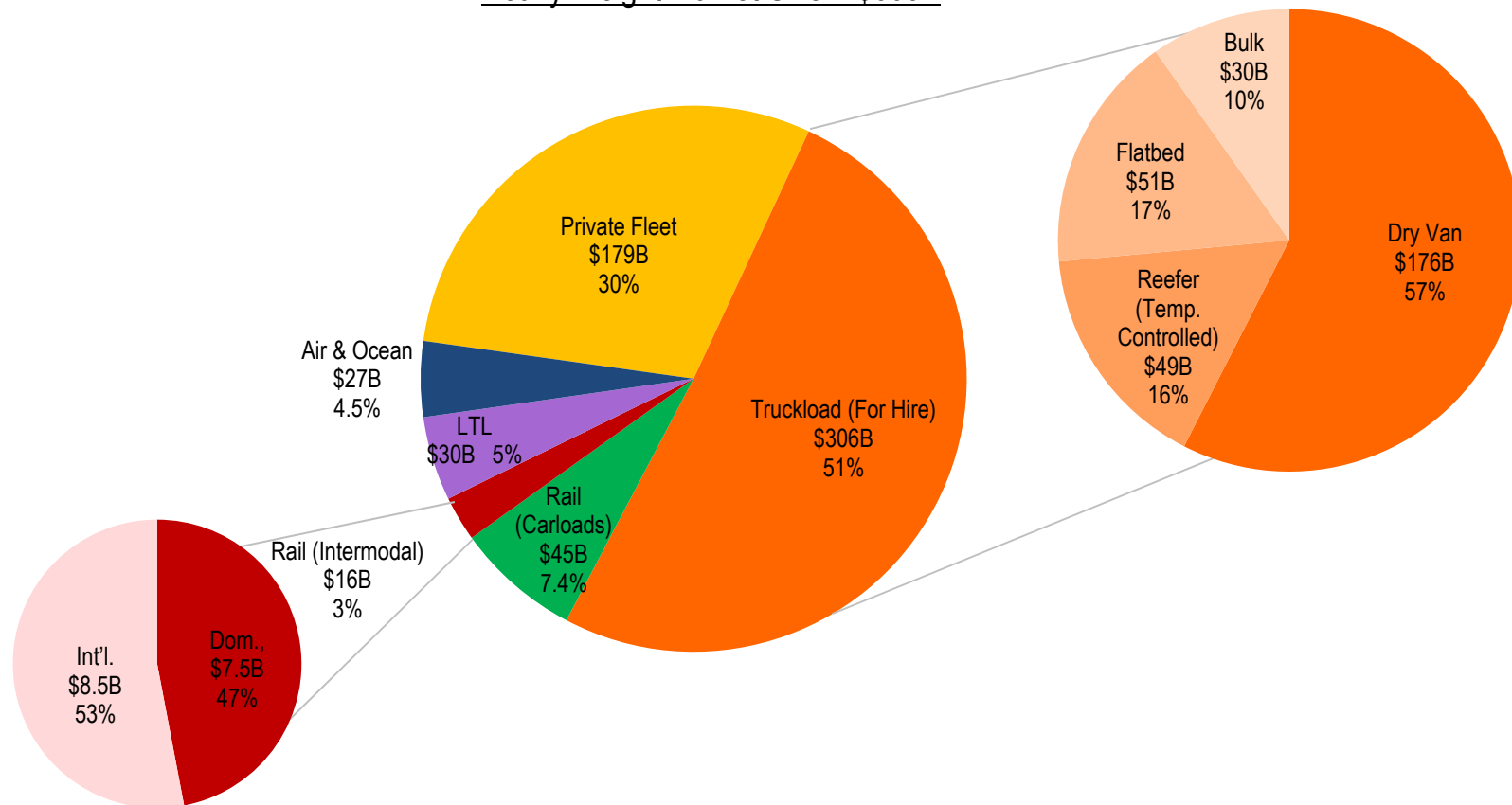
With the growth in goods and industrial production outpacing consumer spending, the average American will be spending more on products and less on services – this equates to freight volumes growing faster than the overall economy.

Industrial Production Growth	
2010 Q2	7.0%
2010 Q3	4.8%
2010 Q4	5.2%
2010 - Annual	5.6%
2011 - Forecast	5.4%
2012 Forecast	5.0%

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THE U.S. HEAVY FREIGHT MARKET IS LARGE AND IS FORECAST TO GROW AT 10% CAGR THROUGH 2013 DURING THE CYCLE.

Heavy Freight Market Size = \$603B



► *Tighter supply conditions are anticipated creating an environment of rising rates.*

Source: FTR Associates, Transport Fundamentals, ATA, Baird, Council of Supply Chain Management

CSA IMPLEMENTATION



CSA BASICS

Unsafe Driving

- Safe Driving & Hazardous Materials
 - *Speeding, Following Too Closely, Improper Lane Change*

Fatigued Driving

- Hours of Service Compliance

Driver Fitness

- Driver Qualification, Licensing & Training
 - *Expired Med Card, Improper Endorsements, Driving While Disqualified*

Drugs/Alcohol

- Drug and Alcohol Violations
 - *Use or Possession of Drugs/Alcohol (as detected at roadside)*

Vehicle Maintenance

- Vehicle/Mechanical Violations
 - *Tire Tread Depth, Lights, Brakes*

Cargo Related

- Load Securement and HM
 - *Improper Placarding, Overweight, Securement*

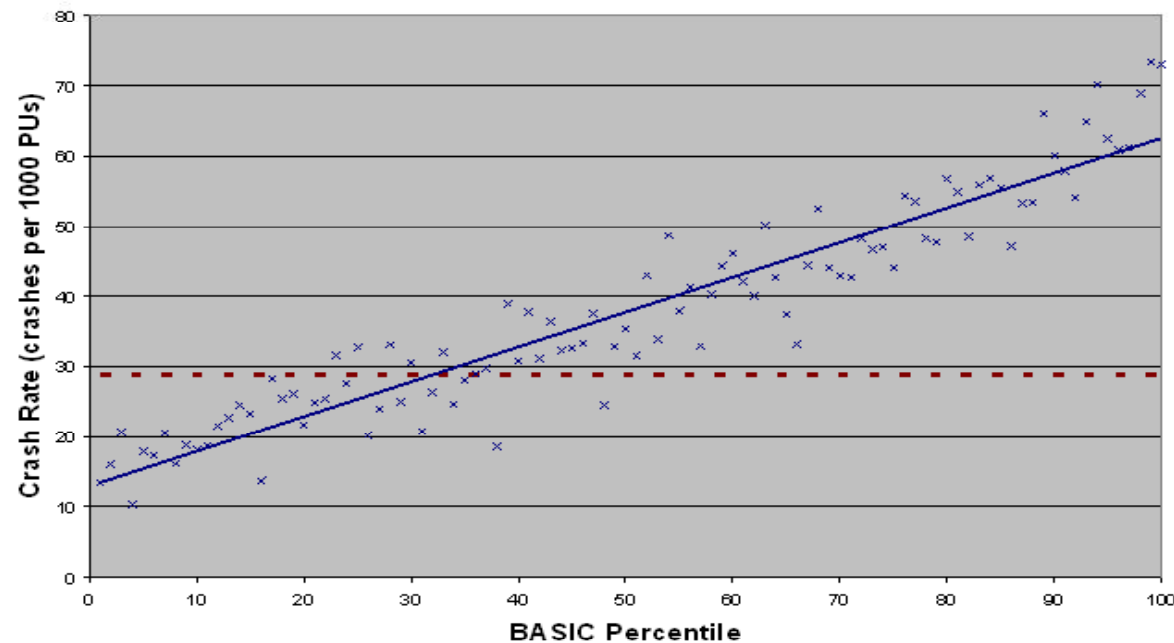
Crash Indicator

- DOT Recordable Crash Rate

INTERESTING FACTS...

- 758,682 carriers in DOT database
- 3.6M commercial drivers
- Only 92,184 carriers have sufficient data to have a CSA score (12.15%)
 - Those 92,184 carriers have 2.7M drivers (75% of 3.6M total)
- 52,967 carriers (of the 92+K with a CSA score) have at least one *alert-level CSA BASIC score* (57%)
- Those 52,967 carriers employ 1,539,000 drivers ($1,539,000 / 3,600,000 = 42.75\%$)
- FMCSA says “don’t worry, we are only seeing ~10% of carriers over the threshold...” The truth is that represents nearly 50% of the capacity that is under DOT scrutiny...

★ Analysis Results - Unsafe Driving BASIC



U.S. Department of Transportation
Federal Motor Carrier Safety Administration



October 22nd, 2009

So what? The linkage between SAFESTAT scores and crash risk was abstract and plaintiff's attorneys struggled to link the two. There will be no such struggle with CSA. Shippers will need to select carriers carefully.

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THE CARRIER AND DRIVER PERSPECTIVE

1. Drivers will be held accountable for their performance from the carrier and indirectly by the FMCSA
2. Those with excessive violations will find it hard to find employment
3. The pre-screening program (PSP)
 - Providing visibility to roadside inspections and crashes
 - Non-preventable crashes will have a negative impact
 - Further iteration required
 - **A credible estimate is that ~280,000 drivers will have at least one deficient CSA BASIC score** using the 90% threshold originally projected by the FMCSA
 - Will create operational issues and will affect driver capacity and freight movement

HOW WILL THIS EFFECT SUPPLY CHAINS?


1. CSA will purge bad commercial drivers from the industry (that's a good thing—we shouldn't apologize, but, it will tighten capacity).
2. Carriers who continue to hire or retain "un-fit" drivers will face litigation exposure for negligent hiring/retention.
3. Shippers and freight brokers will use CSA as a tool in selecting qualified carriers. Some carriers will fail under the weight/scrutiny. Shippers will be exposed in truck litigation based upon carrier qualification & selection.
4. Insurance providers will use CSA to determine rates. *[Combined with pressure to increase minimum insurance levels; this becomes challenging]*

WHAT TO DO....

Shippers:

- Educate your transportation managers on CSA
- Solicit/Research carriers' CSA scores
- Ask if carriers are using PSP
- Tender freight to carriers with compliant scores
- Develop the capability to monitor CSA scores once public, and tender freight accordingly
- Engage your legal counsel to ensure defensibility of the approach you choose...

SCHNEIDER NATIONAL IS COMPLIANT IN ALL CSA BASICS

Schneider National Carriers - 9/25/2010			
Behavior Analysis and Safety Improvement Categories (BASICS)			
			Compliant
	<u>Unsafe Driving</u>	=	
	<u>Fatigued Driving (HOS)</u>	=	
	<u>Driver Fitness</u>	=	
	<u>Drugs/Alcohol</u>	=	
	<u>Vehicle Maintenance</u>	=	
	<u>Cargo-Related</u>	=	
	<u>Crash Indicator</u>	=	

SUMMARY:

- CSA is much better than SafeStat and will serve to improve safety.
- While not perfect, good work has been done to make CSA more fair and equitable.
- More work needs to be done:
 - Crash Accountability
 - Severity weights modified to more closely match crash causation
- Public safety stands to be the biggest winner, which is a win for all of us!

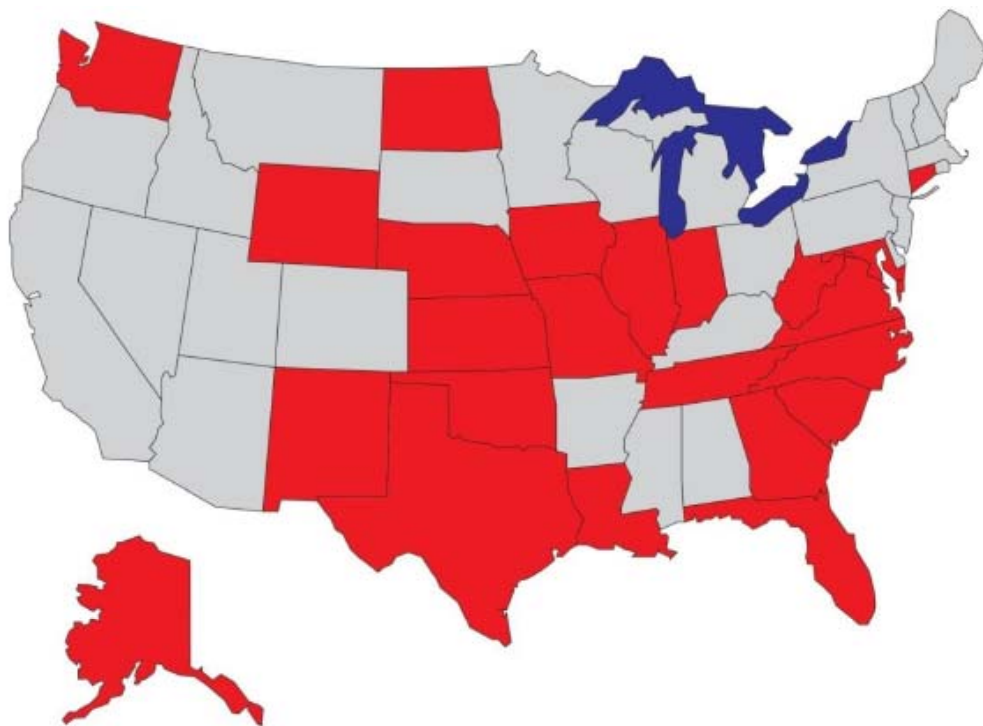
CSA - SHIPPER LIABILITY EXPOSURE



SHIPPER EXPOSURE IN LITIGATION

- *“Shipper exposure in trucking litigation is inevitable”*
- *“CSA will accelerate shipper liability in trucking litigation”*
- *“Increasingly, state laws are prohibiting transportation indemnity agreements which purport to indemnify the shipper for its own negligence.”* Clay Porter, Dennis, Corry, Porter, & Smith Law Firm (noted trucking industry defense attorney)
- 25 States have anti-indemnifications laws on the books:
 - Sec. 45.45.905. Indemnification prohibited. (a) A motor carrier and a shipping person may not, with regard to a transportation services contract, agree that (1) the motor carrier will indemnify, defend, or hold the shipping person harmless, or agree to a provision that has the effect of indemnifying, defending, or holding a shipping person harmless, from claims or liability for the negligence, intentional acts, or intentional omissions of the shipping person
- Plaintiff’s attorneys have political influence and that want access to your deep pockets...

BROAD INDEMNITY FOR SHIPPER CONDUCT IS UNENFORCEABLE – 25 STATES CURRENTLY WITH ANTI- INDEMNIFICATION LAWS



RECENT SETTLEMENTS / VERDICTS IN TRUCK LITIGATION

Carrier	Damages
Carrier A	\$36.5M
Carrier A	\$23.5M (reduced to \$15.2M on appeal)
Carrier B	\$49.1M
Carrier C	\$62.7M
Carrier D	\$24.0M
Carrier E	\$31.5M
Carrier F	\$23.5M

HOURS OF SERVICE



HOURS OF SERVICE (HOS)

	Current	Proposed by Public Citizens	Expected
Daily Work	14	12	14
7 Days Work	60	60	60
Daily Driving	11	8	10
Rest / Break	10	12	10 + break
Restart	34	48	Variable

There is a strong movement to amend the current HOS regulations which will likely go into effect in mid-2011. When these laws are changed, the amount of miles that can be driven in a day will be reduced. Based on preliminary modeling, this will impact capacity by 3% to 6%.

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ELECTRONIC ON-BOARD RECORDERS

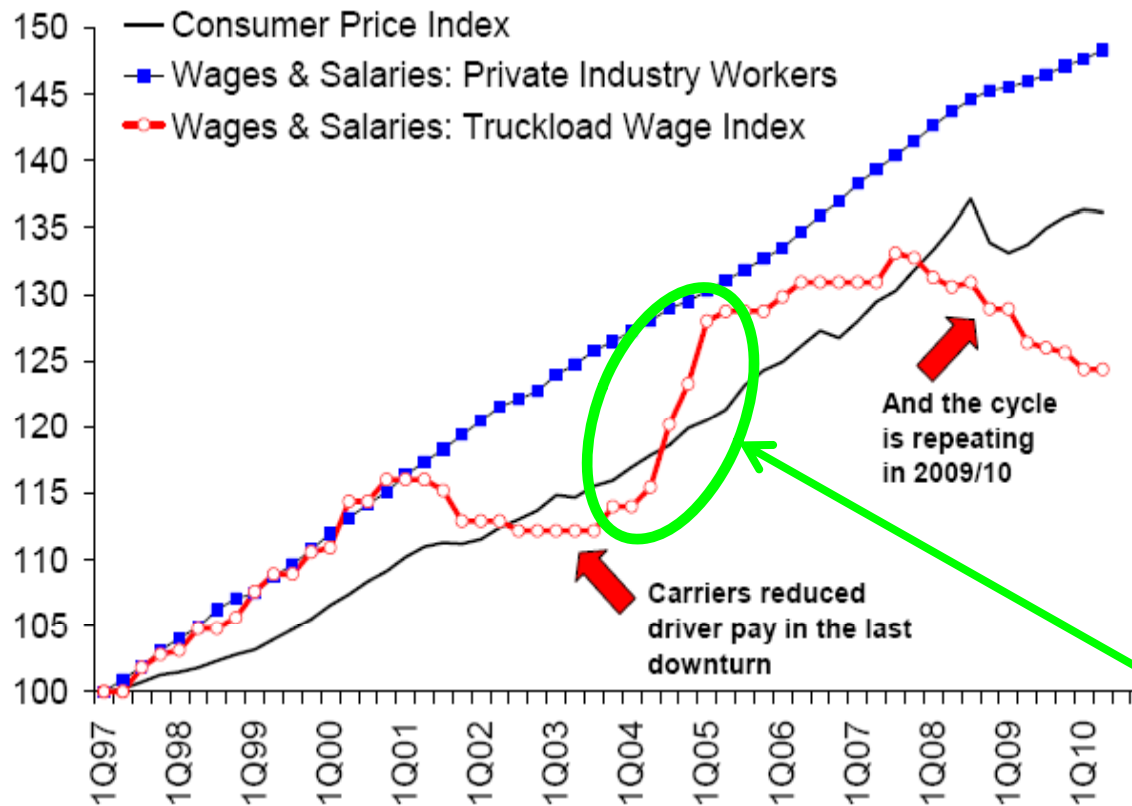
- One of the seven CSA categories is “Fatigued Driving”
- Compliance to this metric is measured through the drivers/carriers compliance to the HOS regulations
- Some carriers with poor scores in this area are being mandated to convert their fleet to electronic logging
- Others are voluntarily converting to increase the safety of their fleet
- Miles driven per day are hampered by EORs by approximately 5%
- According to the Institute of Highway Safety, 55% of all long-distance trucks will need EOBRs

TRUCKLOAD CAPACITY IMPACTS



DRIVER PAY

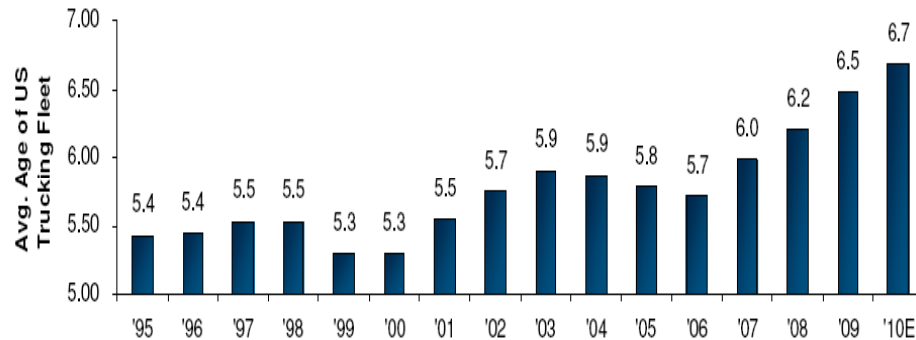
Starting Driver Pay (Per Mile) for Drivers with 3 Years Experience vs. Inflation



Source: National Survey of Driver Wages and Morgan Stanley Research

With increasing levels of freight demand and capacity leaving the industry, to retain and recruit quality drivers, providers will need to increase driver pay.

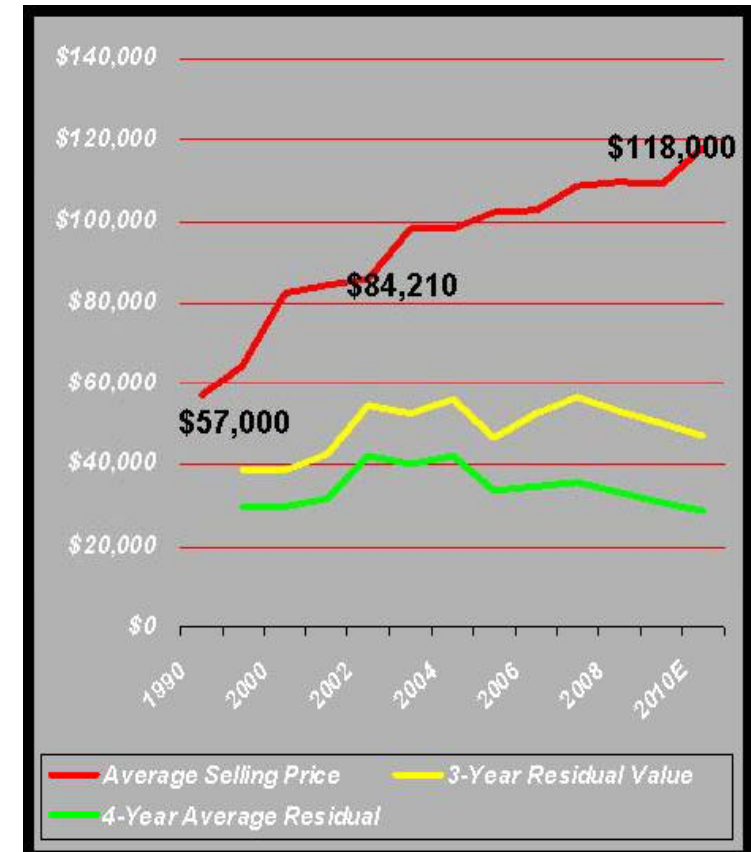
TRUCK COSTS - MAINTENANCE - 2010 ENGINES



Source: ACT Research.

Miles	Maint. Exp / Mile	Growth
<= 175k	\$0.031	
250k	\$0.037	22.0%
350k	\$0.046	24.1%
500k	\$0.060	29.1%
> 550k	\$0.149	148.7%

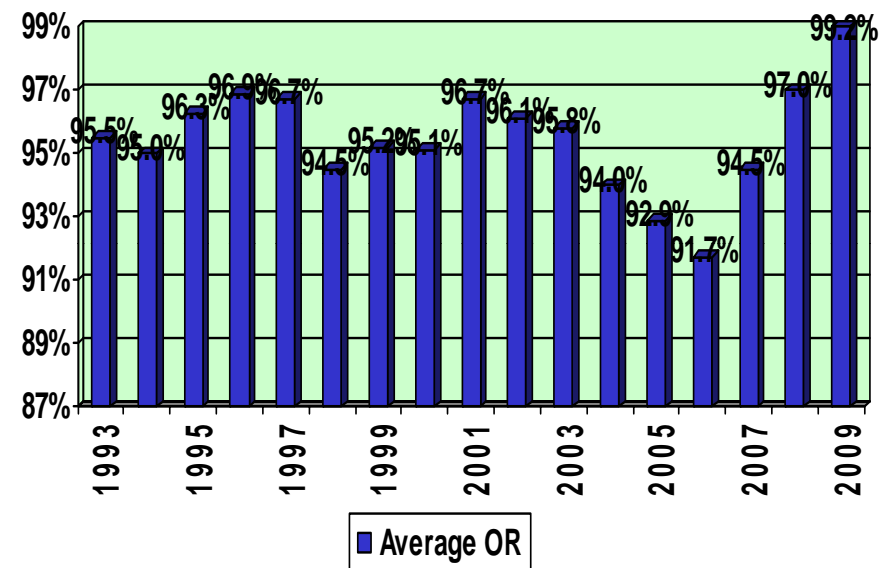
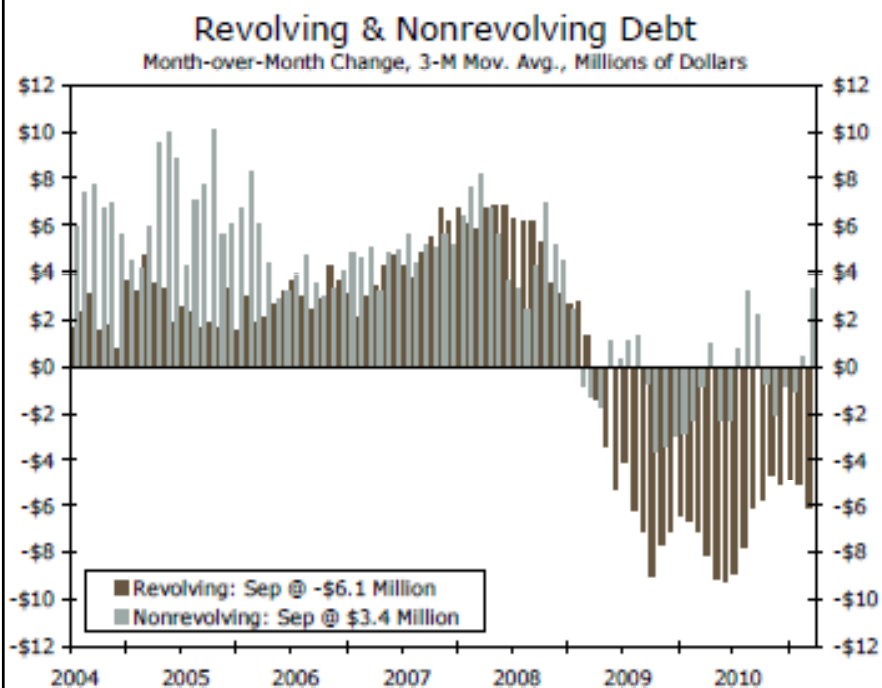
Source: Stephens Inc. estimates using industry channel checks.



During the downturn, fleets suspended the purchases of new tractors. Now, carriers are forced to deal with higher maintenance costs or higher truck costs (with worse fuel efficiency...)

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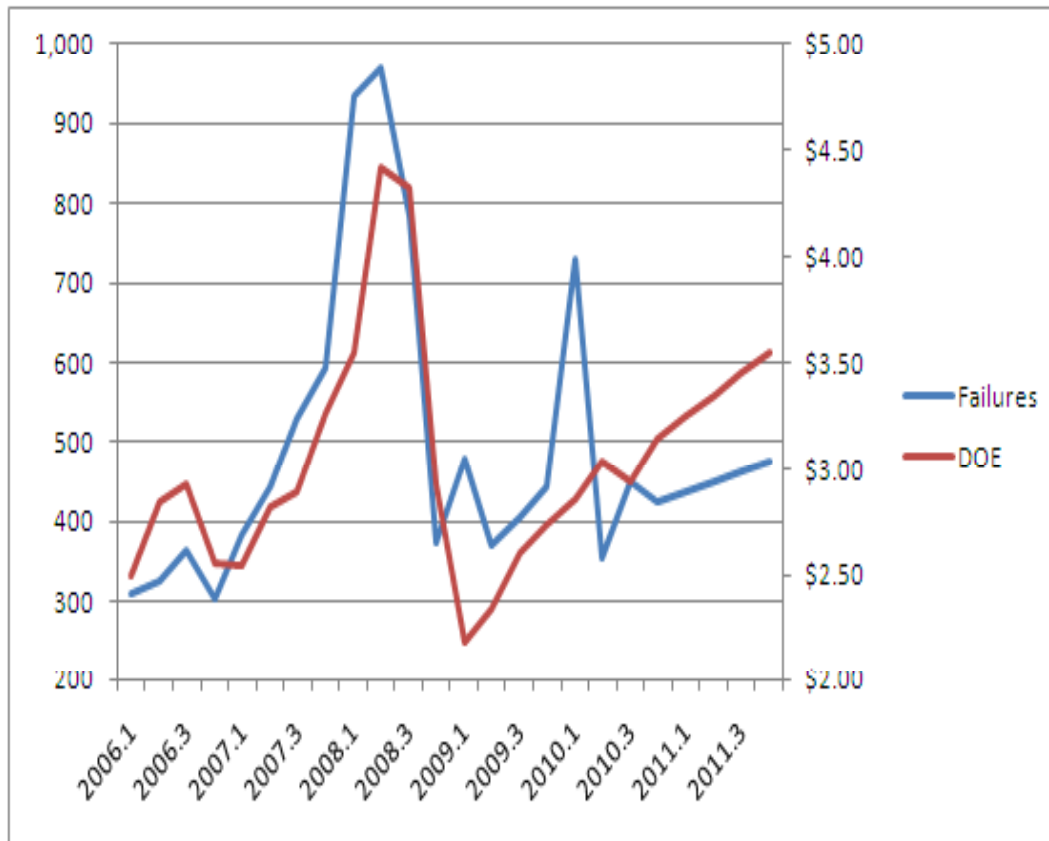
NOT ALL CARRIERS ARE IN A POSITION TO BE ABLE TO AFFORD REPLACEMENT TRUCKS



Due to the economic downturn, carriers' profits collapsed and their balance sheets worsened. Combine this with tighter lending and many carriers do not have the cash or the ability to borrow to upgrade or expand their fleet.

Sources: Bureau of Economic Statistics, ATA

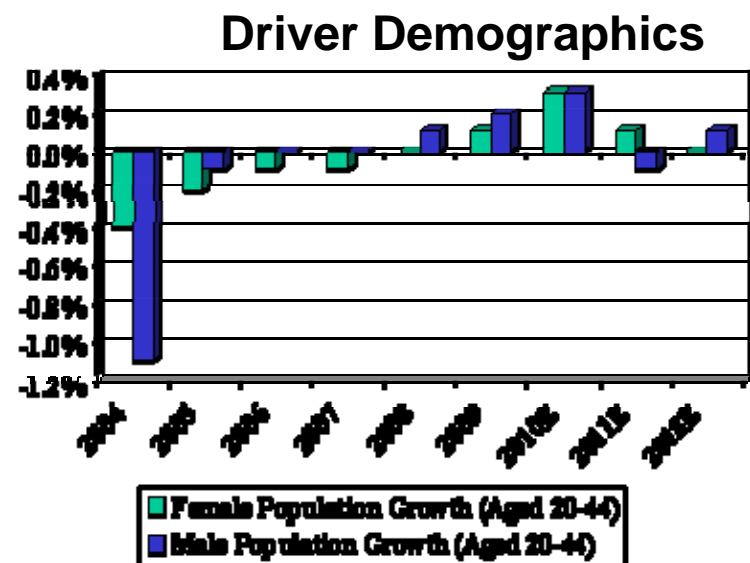
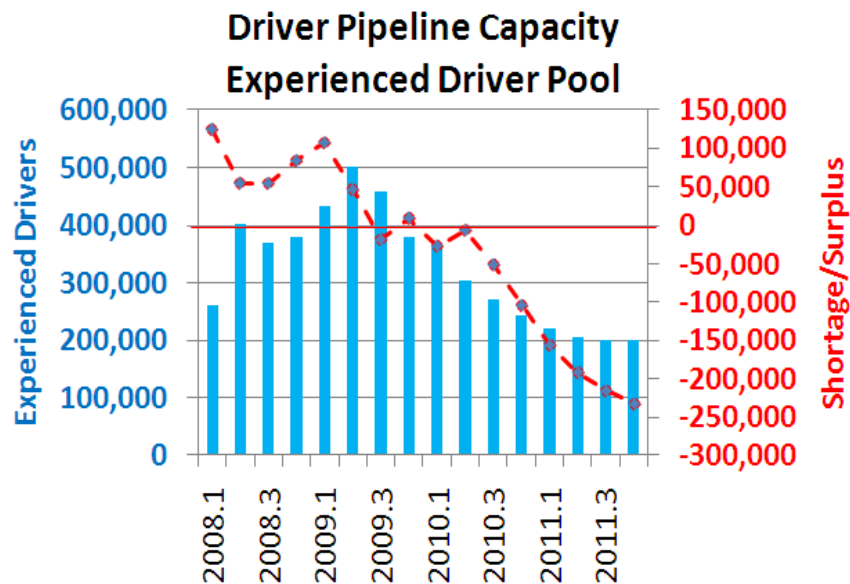
FUEL PRICES DRIVE TRUCKING BANKRUPTCIES



- There is a strong link between the cost of fuel and the number of trucking companies that close their doors
- The DOE is forecasted to increase 8% to 12% in 2011 - expect more truckers to fold
- Historical correlation would indicate this could be 5.5% to 8.5% of capacity
- Shippers who take action to reduce their fuel spend will amplify this problem

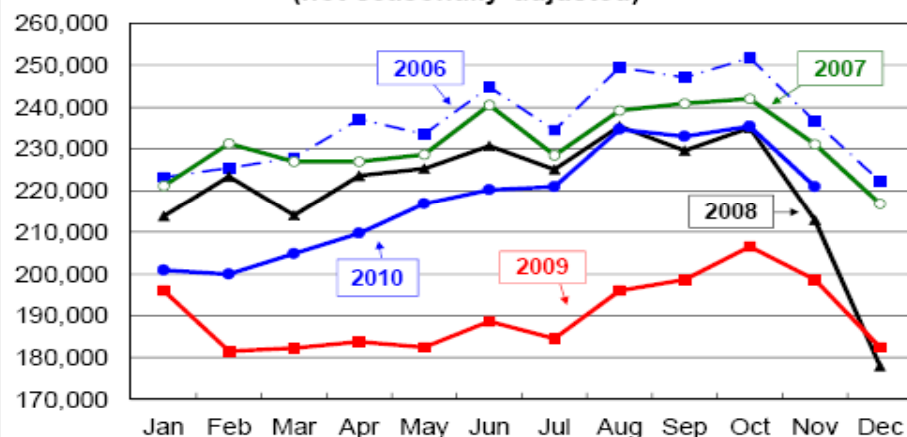
Sources: FTR Associates, DOE

EVEN IF CARRIERS WERE ADDING TRUCKS, DEMOGRAPHICS ARE HURTING RECRUITING



Experienced drivers are leaving the industry and retiring and the amount of people who have historically filled these openings are diminishing.

Average Weekly U.S. Rail Intermodal Traffic
(not seasonally adjusted)



Data are weekly average originations for each month, exclude U.S. operations of CN and CP, and reflect revisions from original reporting. Source: AAR Weekly Railroad Traffic

Intermodal volumes in 2010 have regained 2008 levels and forecasted increases will put 2011 volumes at the highest levels on record.

N.A. INTERMODAL OUTLOOK

Description	QUARTER			YEAR		
	2010*Q3	2010*Q4	2011*Q1	2010	2011	2012
U.S. Imports of Goods ¹	18.1%	1.4%	2.2%	16.1%	6.7%	6.0%
U.S. Exports of Goods ¹	3.4%	7.0%	8.4%	14.0%	7.2%	6.3%
Truck Loads ²	4.6%	0.2%	2.2%	5.3%	3.3%	4.7%
Class 8 Capacity In Use	79.1%	78.8%	79.6%	78.5%	81.0%	85.2%
Intermodal Loads ²	20.3%	11.5%	10.7%	14.4%	7.0%	6.9%
-International ²	28.1%	16.0%	13.2%	18.3%	6.3%	7.3%
-Domestic ²	11.7%	6.8%	8.0%	10.1%	7.9%	6.5%

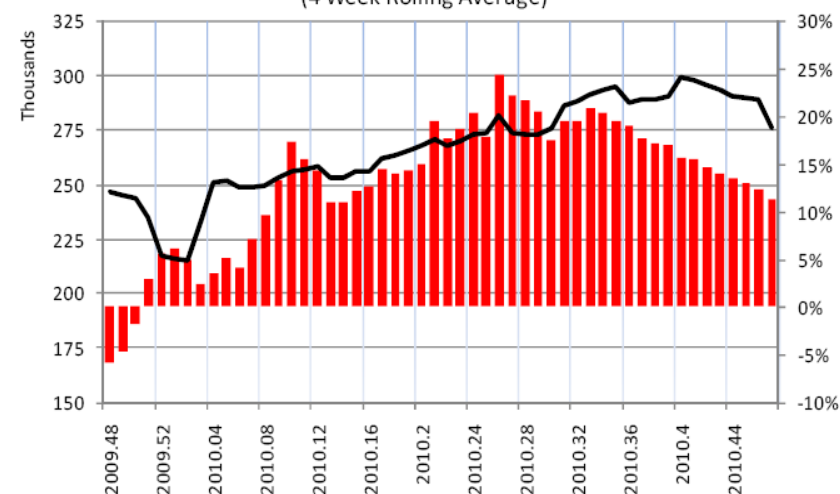
Notes:

¹ SAAR Q/Q % Change ² Y/Y % Change

Sources: GTC, FTR, IANA

AAR Weekly Intermodal Loadings

(4 Week Rolling Average)



Sources: GTC, FTR, AAR; Copyright 2010

■ Y/Y % Change — 4 Week Rolling Average

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DRIVER IMPACTS WILL AFFECT DRAY CAPACITY

- All of the issues that will affect trucking will also affect drayage capacity
- Drayage capacity will be negatively affected by CSA, Hours of Service, On-board Recorders, and DOE Costs
 - Since the regulatory measures are done in miles, drayage will be impacted by these laws more than long-haul truck
- Drayage costs will be affected by the needed changes in driver pay as well as the increasing costs of tractor ownership
- In addition to these costs, the State of California has mandated that all trucks entering ports or intermodal rail yards comply with 2010 emissions standards - using older, cost effective trucks is no longer an option

HOW SHOULD A SHIPPER RESPOND TO THE 2011 TRANSPORTATION ENVIRONMENT?



SUGGESTED SHIPPER ACTIONS

- Capacity will be harder to find in 2011 than it was in 2010 - 2012 will be even worse! Align yourself with those who control the capacity - *asset based carriers*.
- Shippers will become liable for the carriers they select. Align yourself with safe, reputable providers.
- Transportation providers' costs have been steadily increasing, while revenues have not kept up. This is not sustainable, prices will increase.
- Fuel prices will continue to rise. Fuel surcharge programs should align with incremental carrier fuel cost increases. Utilizing sub-standard programs will exacerbate capacity challenges.
- Purchasing behavior - commodity based procurement tactics will not gain capacity when choices exist in the market. Develop a strategic approach to procurement with key transportation providers.

THANK YOU!

