

**Industrial Research**  
February 2011

## Transportation & Logistics Baird's 2011 Outlook

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Please refer to Appendix – Important Disclosures and Analyst Certification



# Transport investment thesis

The logo for BAIRD, consisting of the word "BAIRD" in white, uppercase, sans-serif font, set against a blue parallelogram background.

## **Early-cycle rally has ended, but selective transport investment opportunity remains**

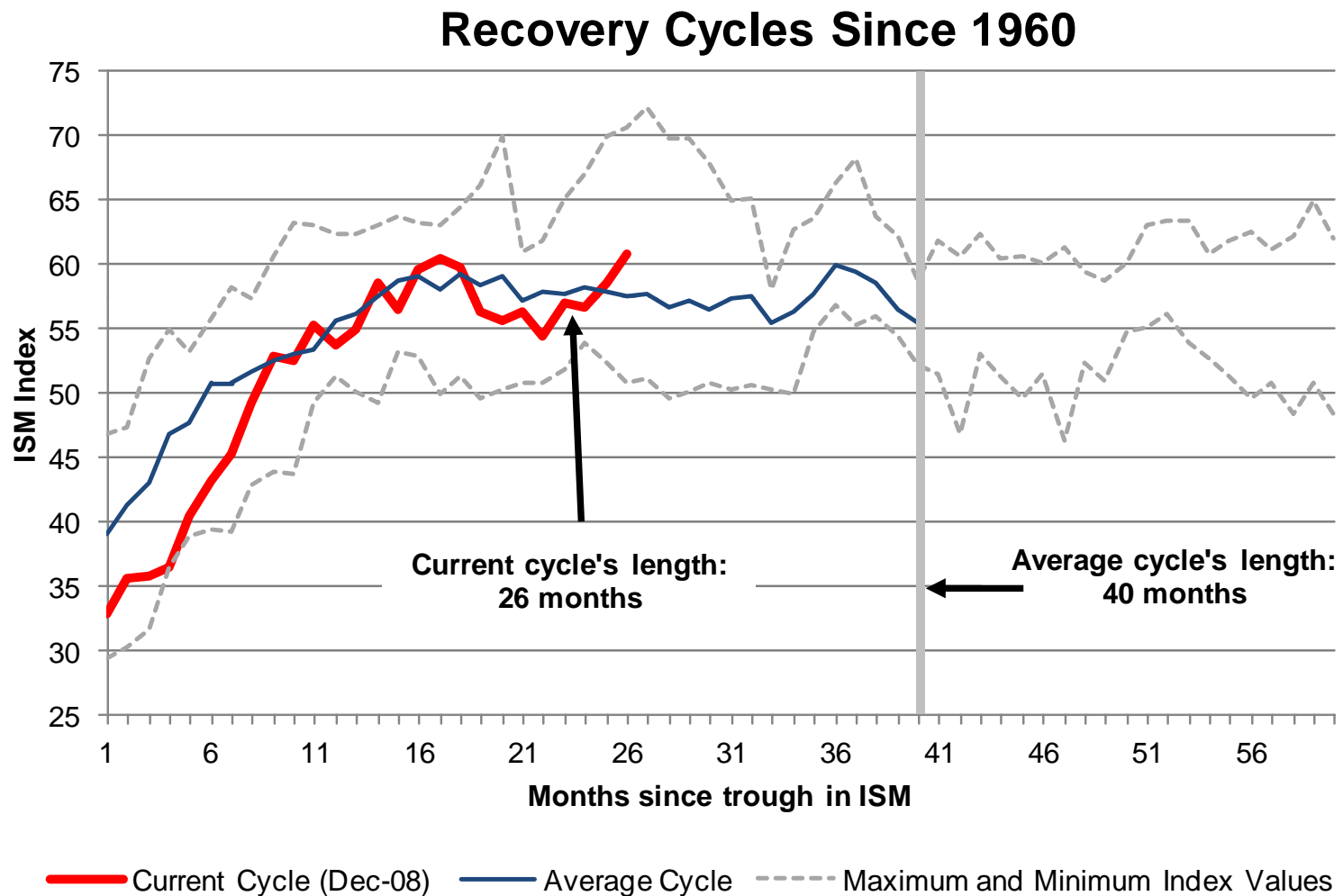
Prefer transports with industrial exposure, secular growth opportunity, pricing leverage

### **Key 2011 investment themes**

- Positive freight growth expected across modes
- Industrial recovery and lean inventories are key drivers of freight demand
- Strong pricing growth – truckers and rails; also domestic parcel
- Strength of international growth; fuel??

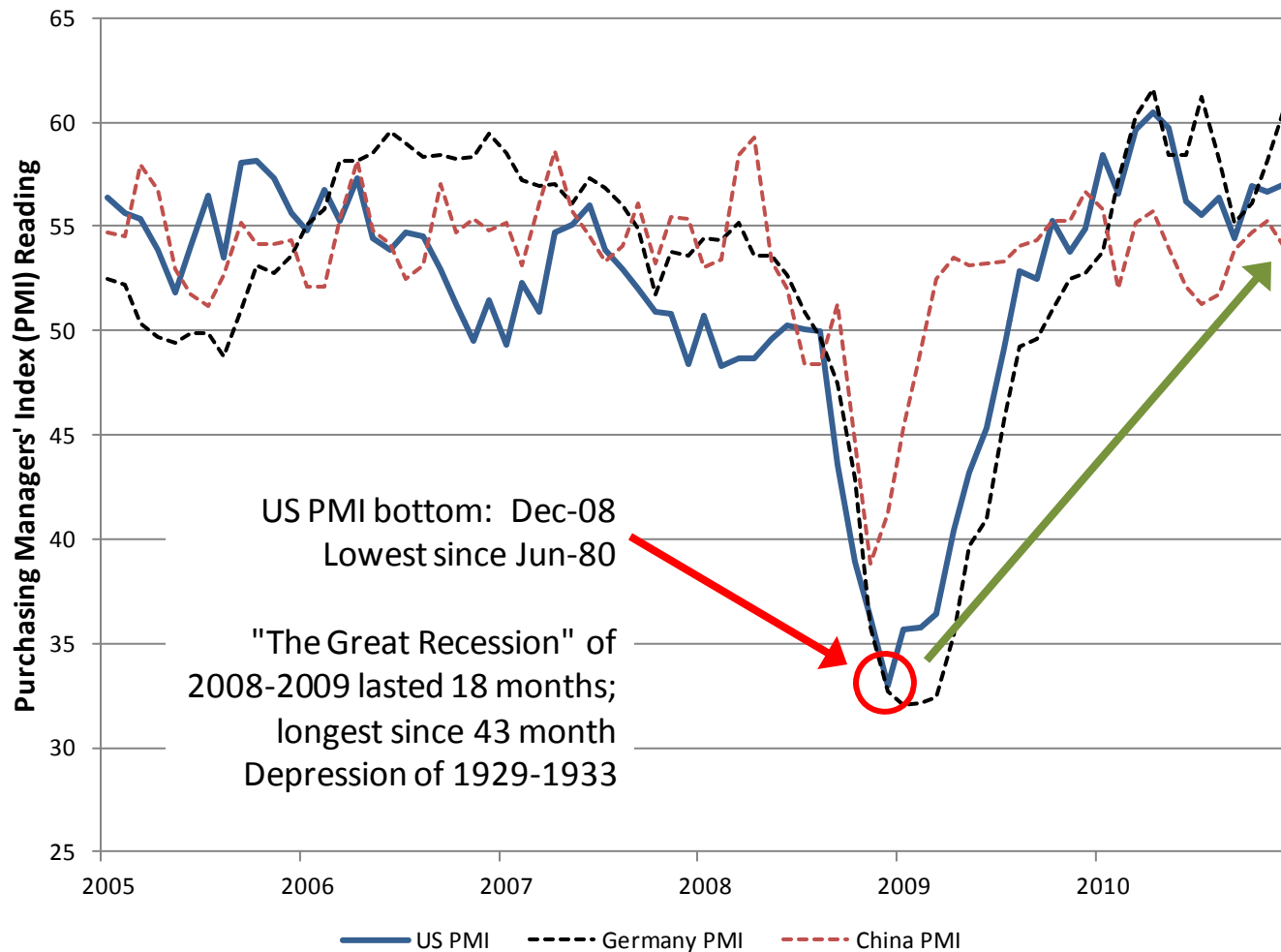
# Where are we in the cycle?

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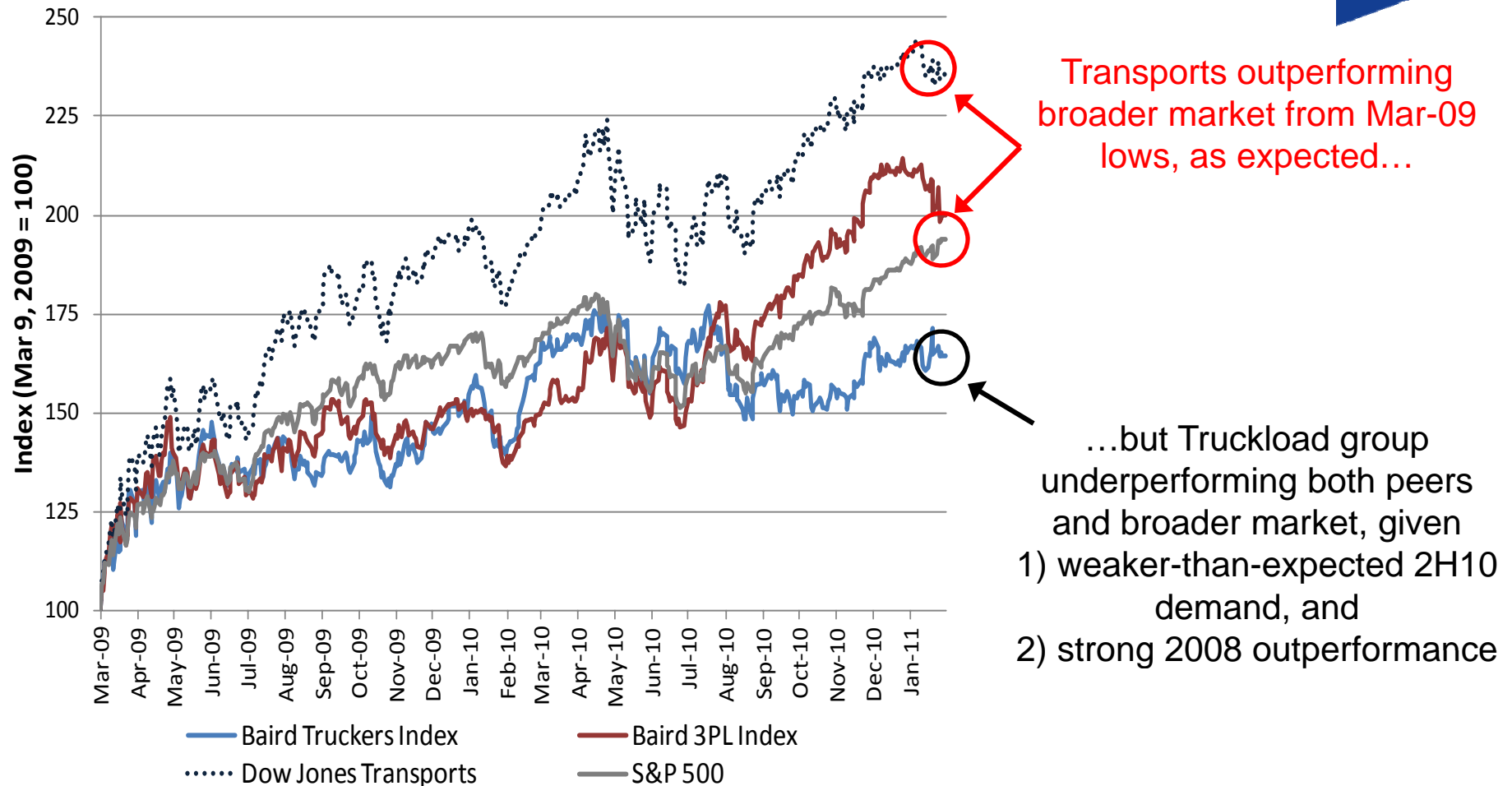
# Broad-based recovery from the depths of “The Great Recession”

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# Early-cycle Transport outperformance from March 2009 market lows

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# Early-cycle rally is over...

...But transport outperformance potential given accelerating rates (particularly in truckload)

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\*Public TLs include HTLD, KNX

Source: FactSet, Baird estimates

# Primary 2011 freight demand drivers



- Healthy industrial production outlook
- Lean inventories
- Strength of international growth a key question

## Freight Demand Growth by Mode

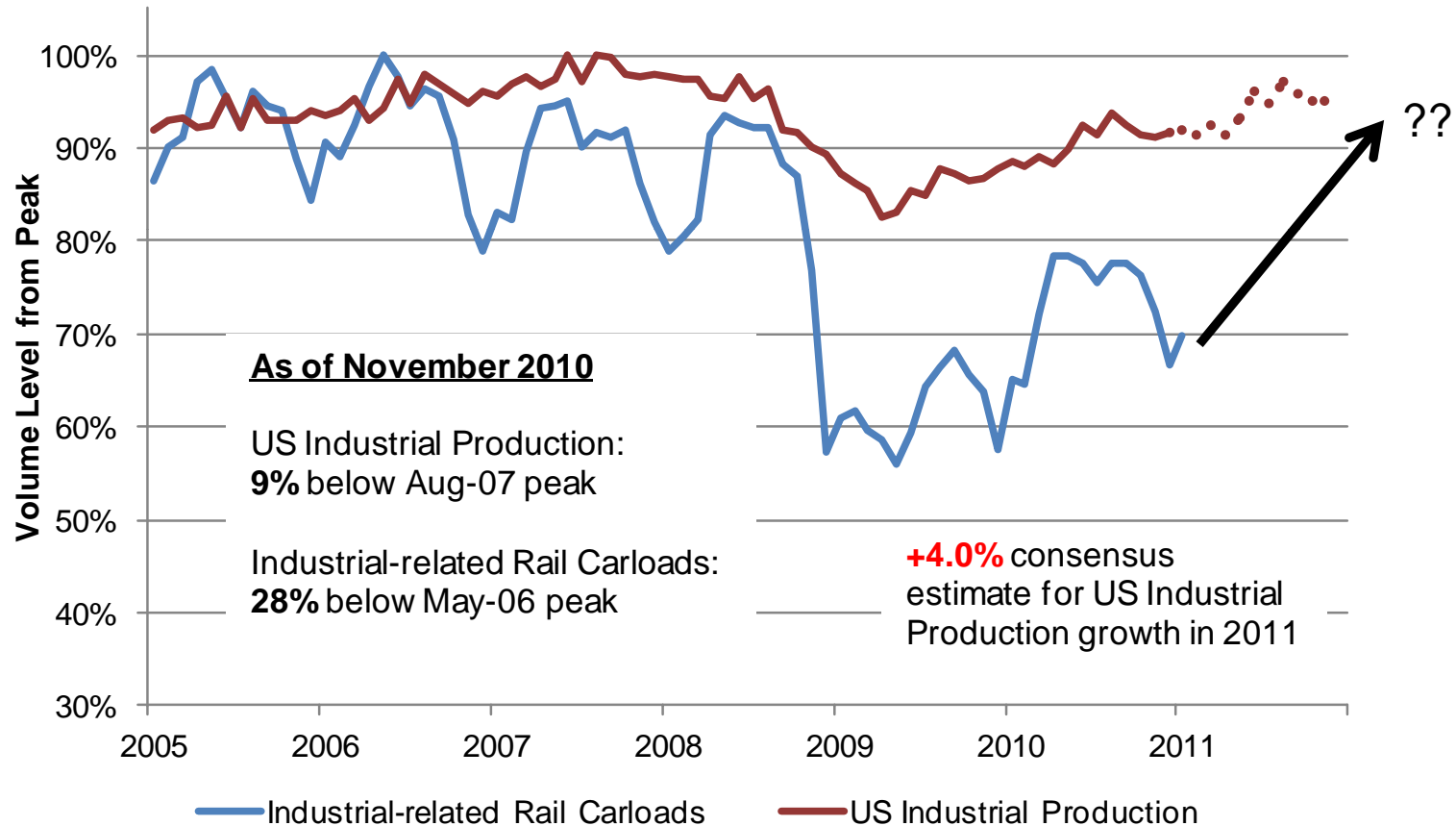
	2004	2005	2006	2007	2008	2009	2010	2011E
Truck	4%	4%	1%	-1%	-3%	-10%	5%	2-4%
Intermodal	10%	6%	5%	-1%	-3%	-15%	15%	5-6%
Rail	4%	1%	1%	0%	-3%	-16%	9%	3-5%
Airfreight	13%	5%	5%	4%	-4%	-10%	15%	0-5%
Ocean Freight	11%	10%	10%	9%	0%	-10%	12%	2-5%

# Industrial freight volumes well below peak

...supporting above-trend freight demand

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## Industrial Production Recovery Supports Industrial-related Volume Growth

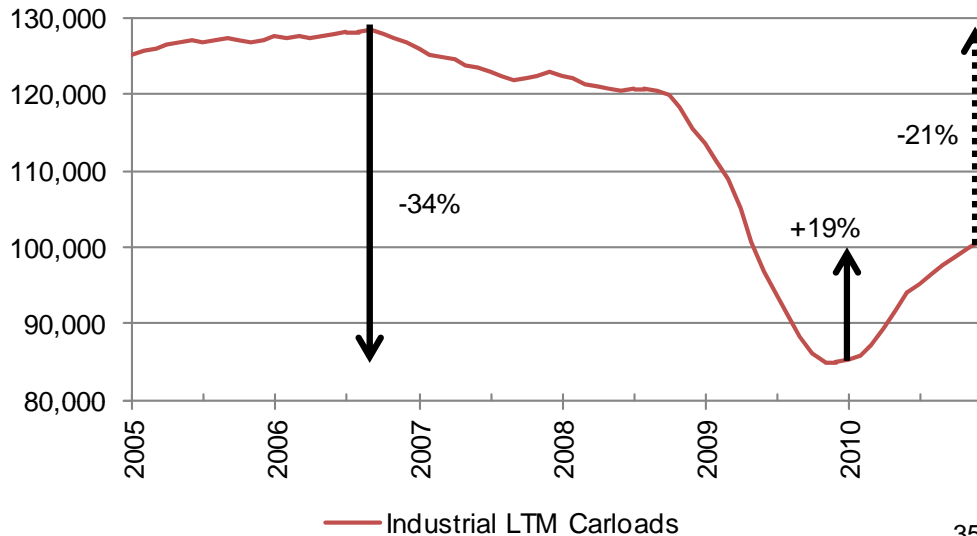




# Rails volumes remain well off peak levels

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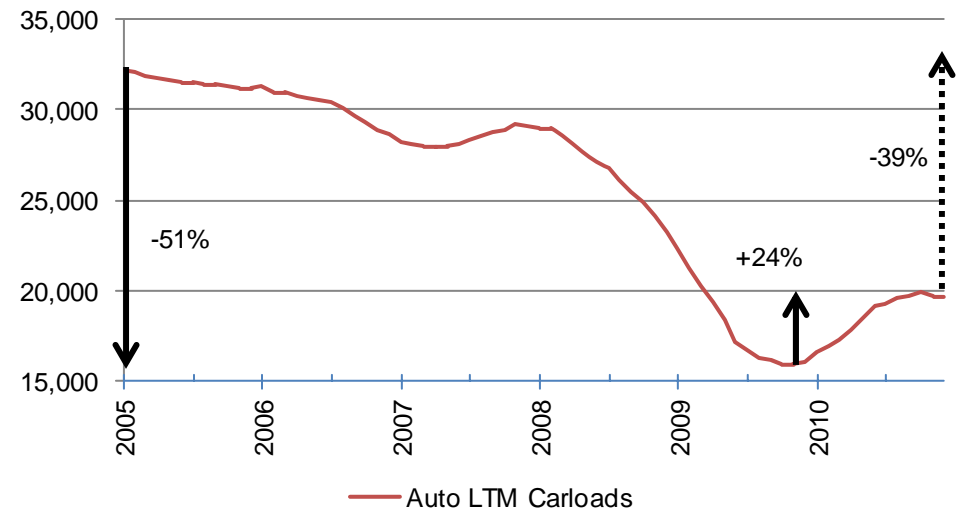
Industrial LTM Carloads



Industrial rail carloads  
over 20% off peak  
levels

Auto carloads nearly  
40% off 2005 levels; 8%  
production 2011 growth  
expected

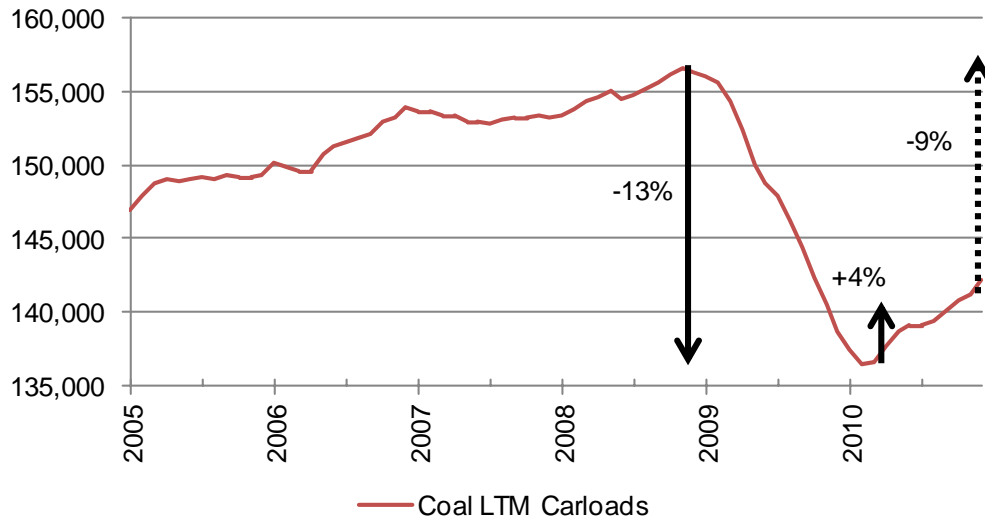
Auto LTM Carloads



# Rails volumes remain well off peak levels

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Coal LTM Carloads

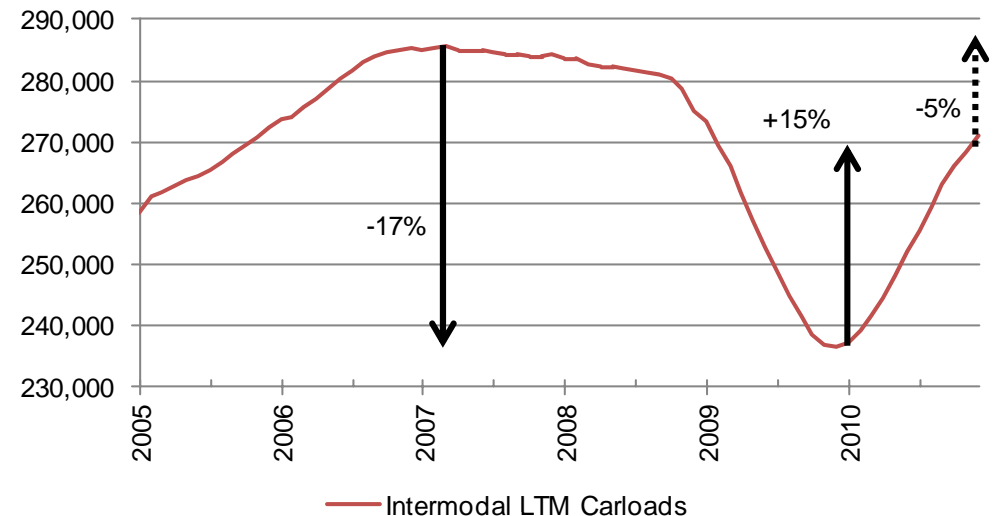


**Coal 9% off peak,  
despite expanding  
Export opportunities**

**Overall intermodal off  
peak levels due mostly  
to international**

**Domestic intermodal  
expected to be strong  
again in 2011**

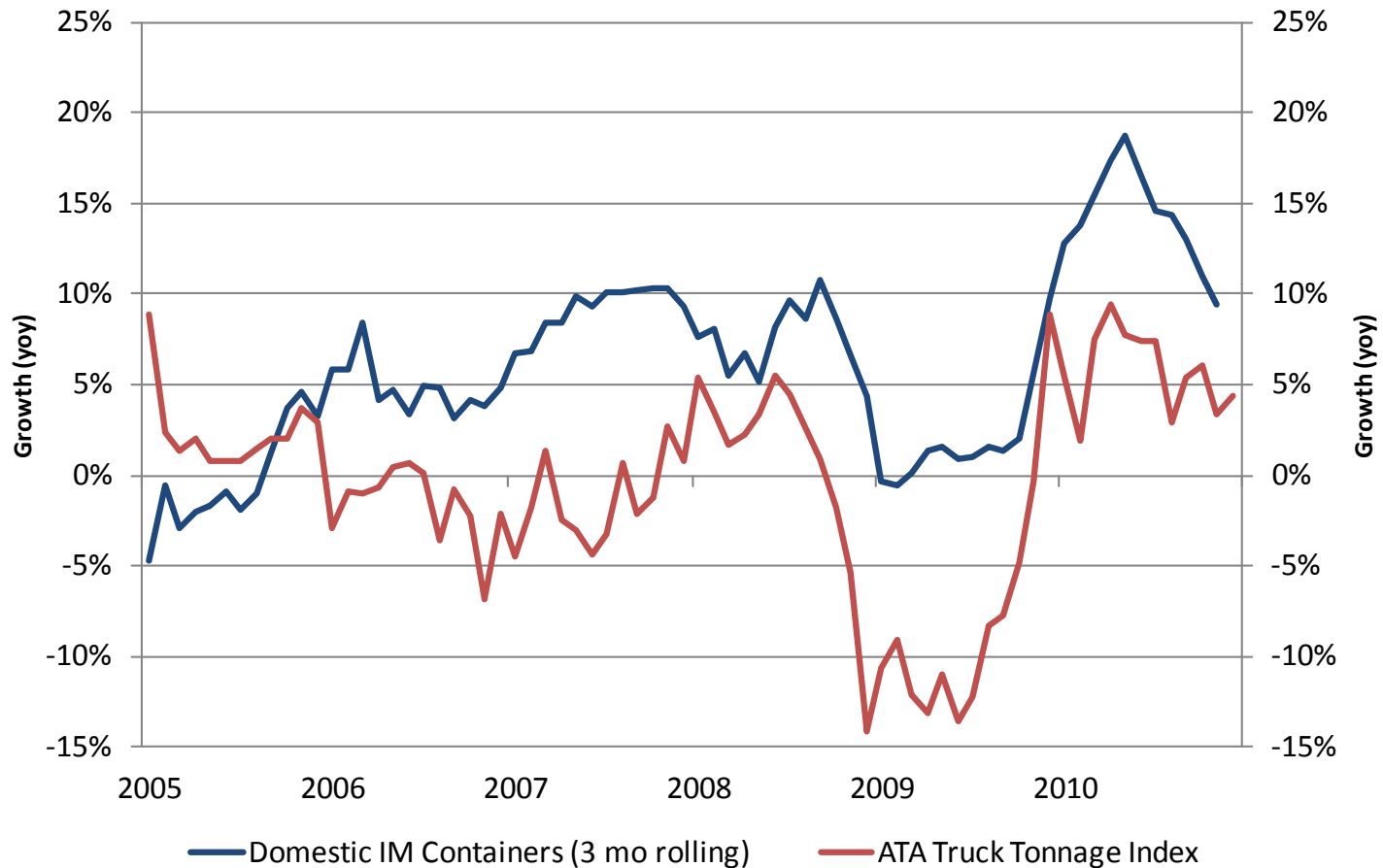
Intermodal LTM Carloads



# Intermodal: the secular growth story

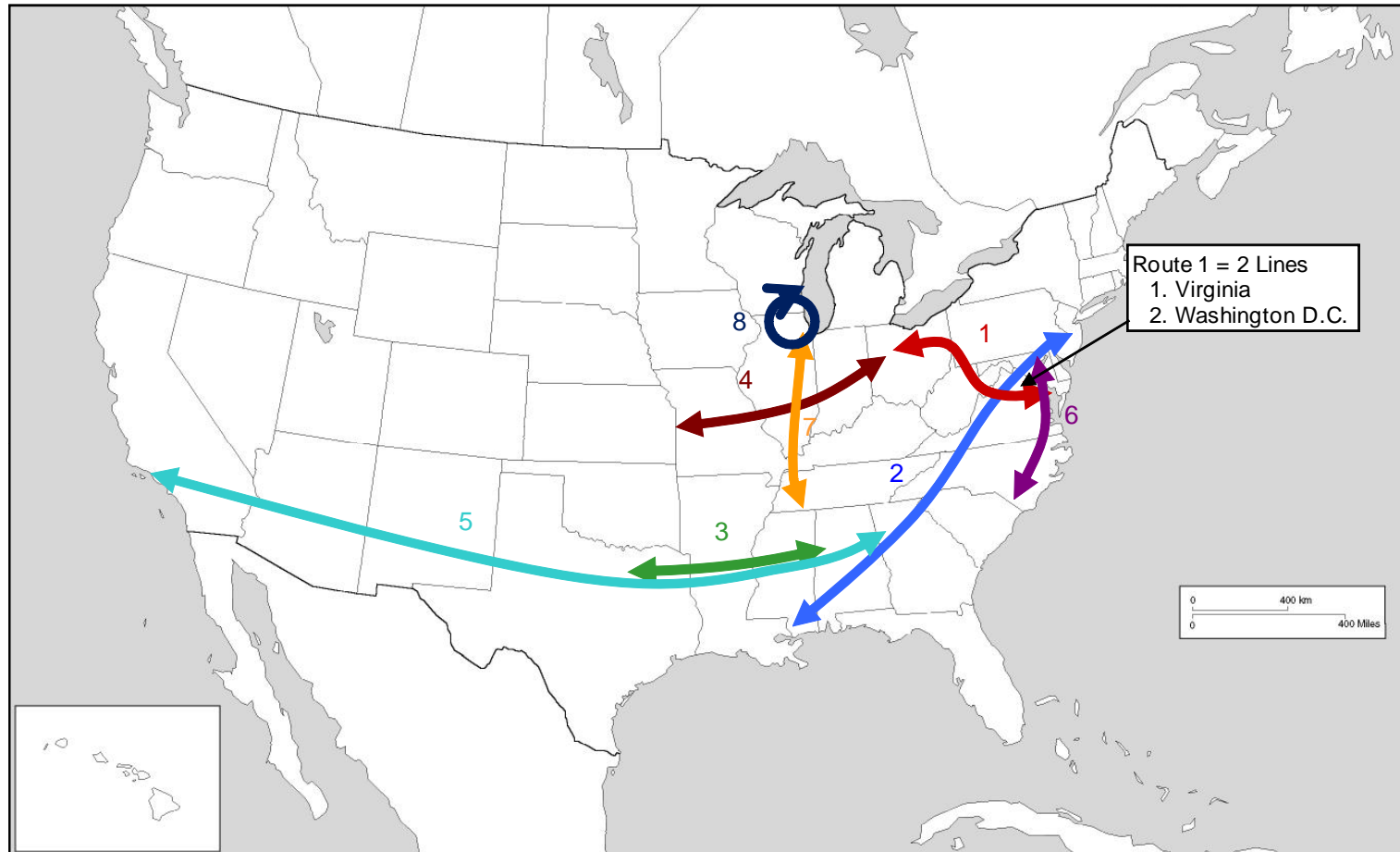
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## Domestic Intermodal A Secular Share Gainer



# Intermodal infrastructure investment

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**Route 1:** NSC Heartland Corridor (2010) and CSX National Gateway (2015):  
DC/ Virginia to Columbus, OH

**Route 2:** NSC Crescent Corridor (2013)  
Newark, NJ to New Orleans, LA

**Route 3:** KCS and NSC Meridian Speedway (2006)  
Meridian, MS to Shreveport, LA

**Route 4:** Schneider, CSX, KCS Intermodal (2006)  
Marion, OH to Kansas City

**Route 5:** UNP and NSC enhanced Sunset Corridor (2007) Source: Baird  
Southwest to Los Angeles, CA

**Route 6:** CSX I-95 Corridor  
Baltimore, MD to North Carolina

**Route 7:** MidAmerica Corridor  
Chicago to Memphis

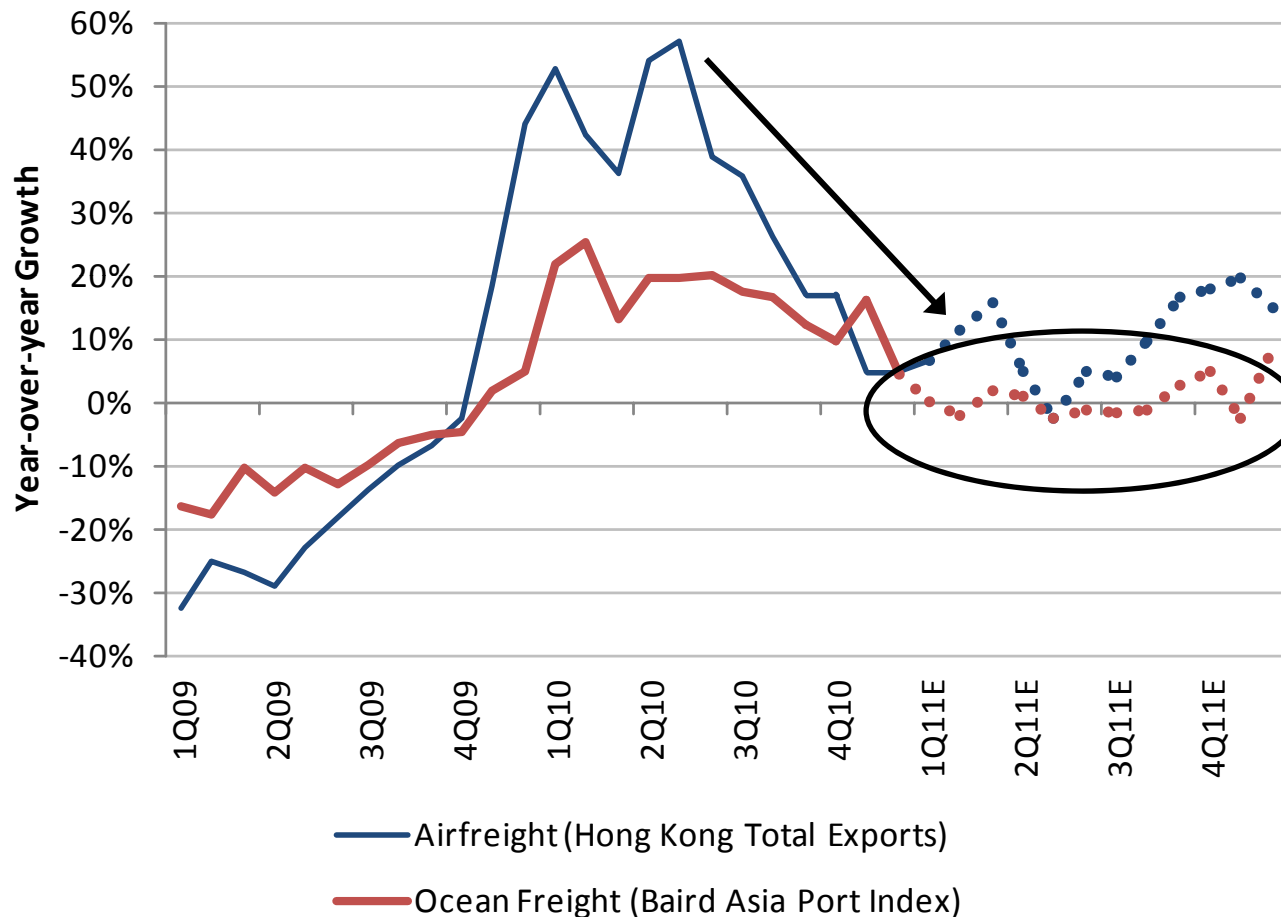
**Route 8:** Centerpoint Intermodal  
Chicago inland port

**Not Pictured:** Patriot Corridor  
Albany, NY to Boston, MA

# Decelerating international growth a potential headwind...

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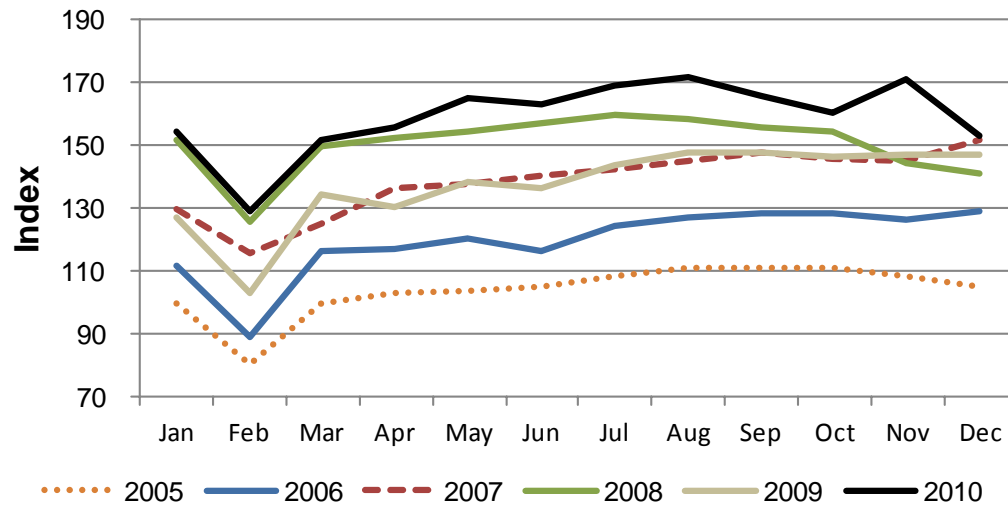
## Tough Comparisons Pressure International Growth



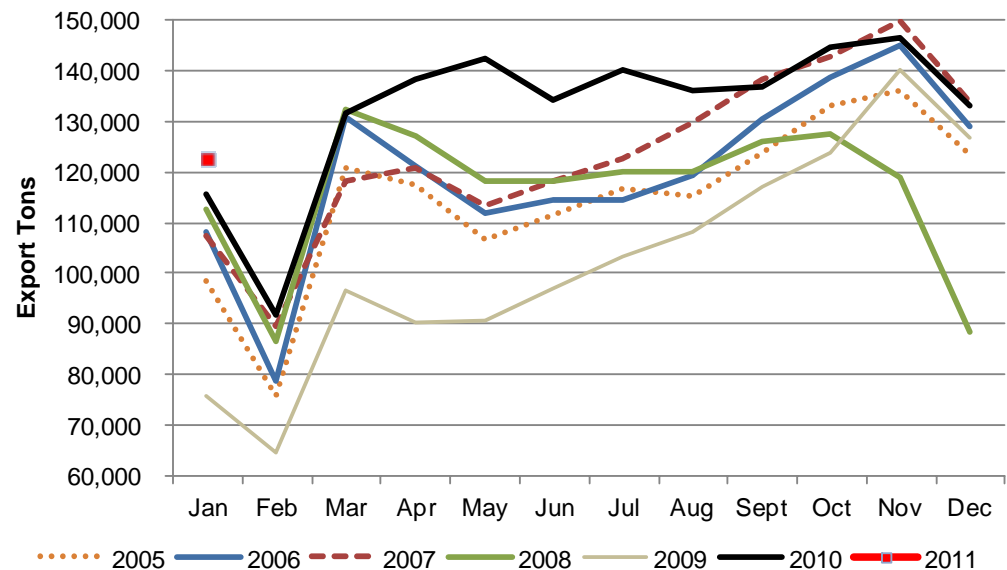
# ...However, absolute international volumes at record levels

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Baird Asia Port Index



Hong Kong Airfreight Export Tonnage

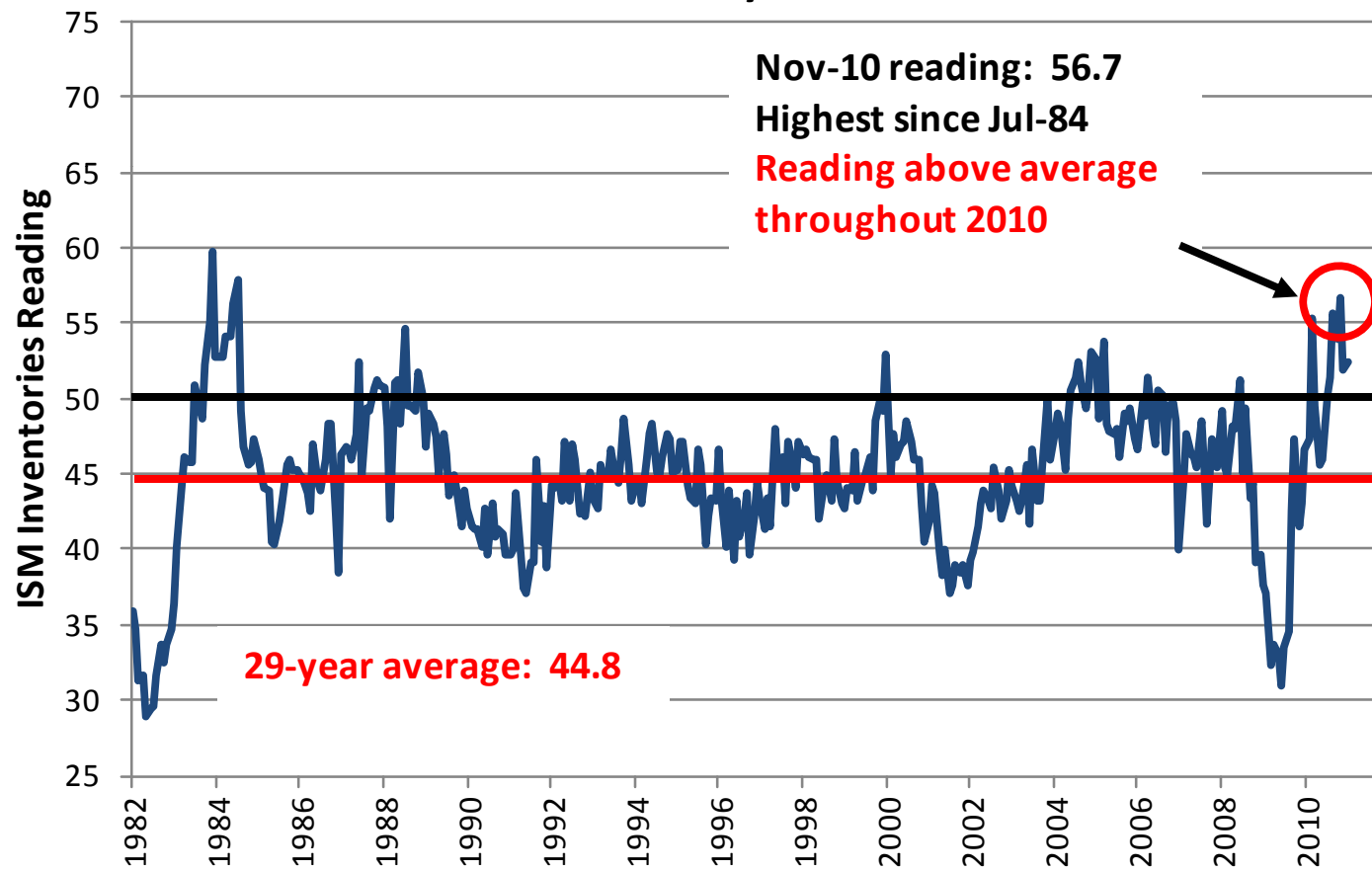


Source: HACTL, industry data, Baird estimates

# Pace of recent inventory restocking is unsustainable

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## 2010's Inventory Restocking Unlikely To Remain a Catalyst in 2011...

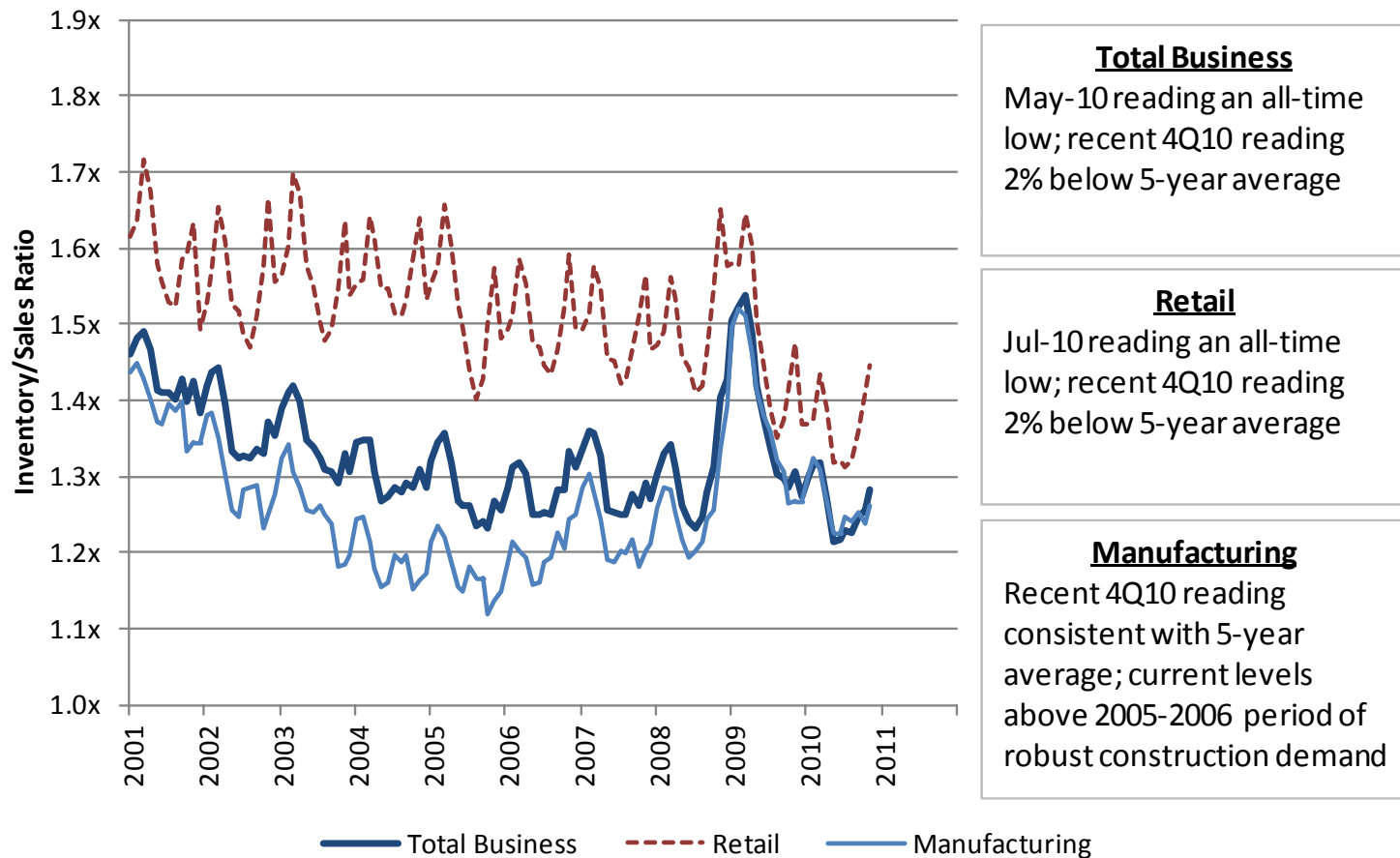


# Inventories lean across channels

Making freight demand very sensitive to economic activity

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## ...But Inventories Remain Lean Across Channels

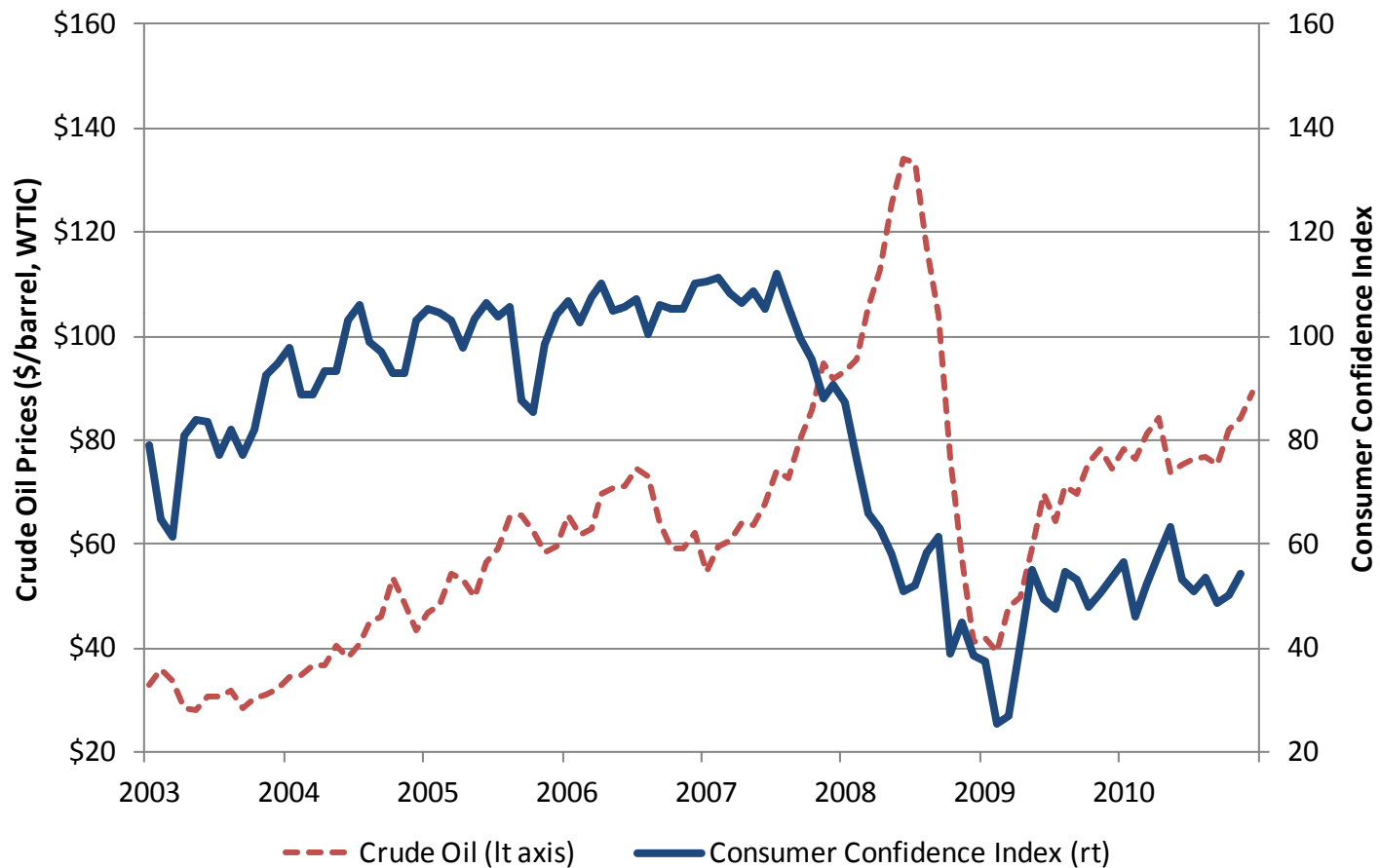




# Rising fuel prices a wildcard

Recent rise in fuel a(nother) headwind for consumers

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# Positive outlook for freight pricing

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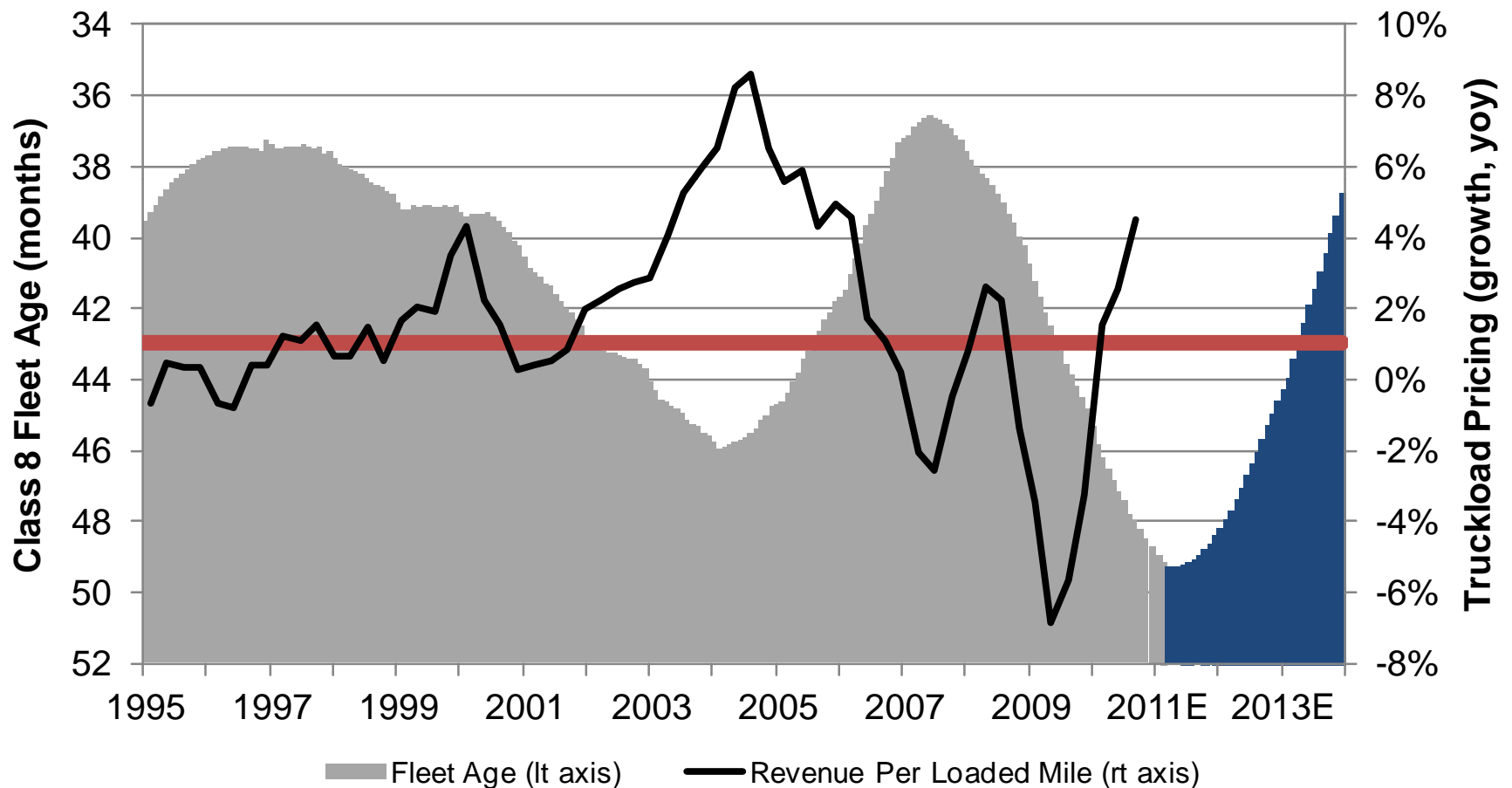
- **2011: further freight rate improvements**
- **Normal seasonality supports strong 2Q spot market**
- **Upside potential in a more robust demand environment**

<b>Freight Rate Growth by Mode</b>								
	2004	2005	2006	2007	2008	2009	2010	2011E
Truckload	6%	5%	2%	-2%	-3%	-6%	1%	4-8%
Less-Than-Truckload	3%	3%	6%	-1%	-2%	-10%	-2%	4-5%
Rail	5%	6%	6%	6%	7%	5%	5%	4-5%
Domestic Intermodal	3%	4%	3%	1%	0%	-5%	0%	3-5%

# Accelerating 2011 truckload pricing

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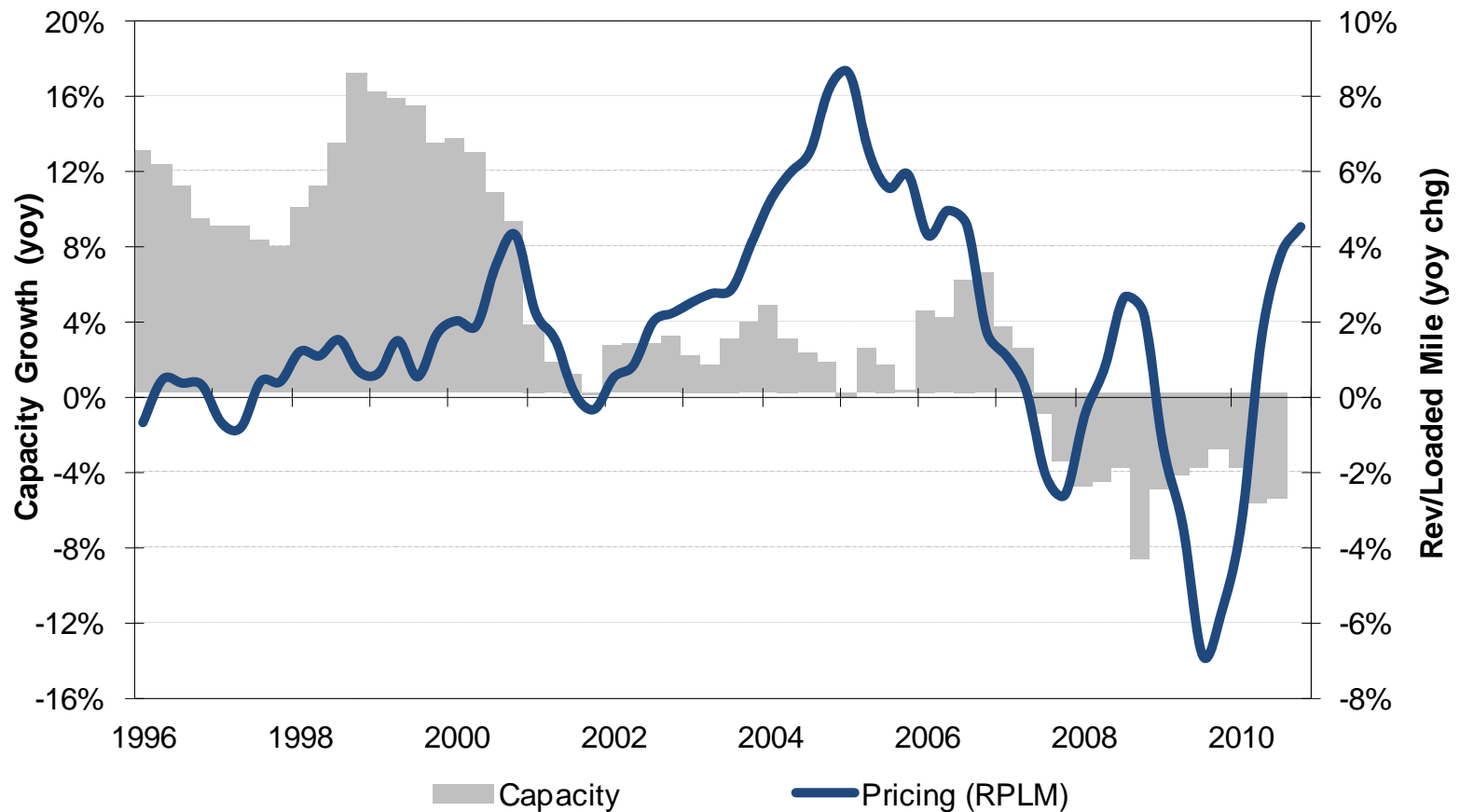
**Truckload Fleet At A Generational High, and Still Aging;  
Supportive of Accelerating Truckload Rates**



# Constrained truck capacity supports rates

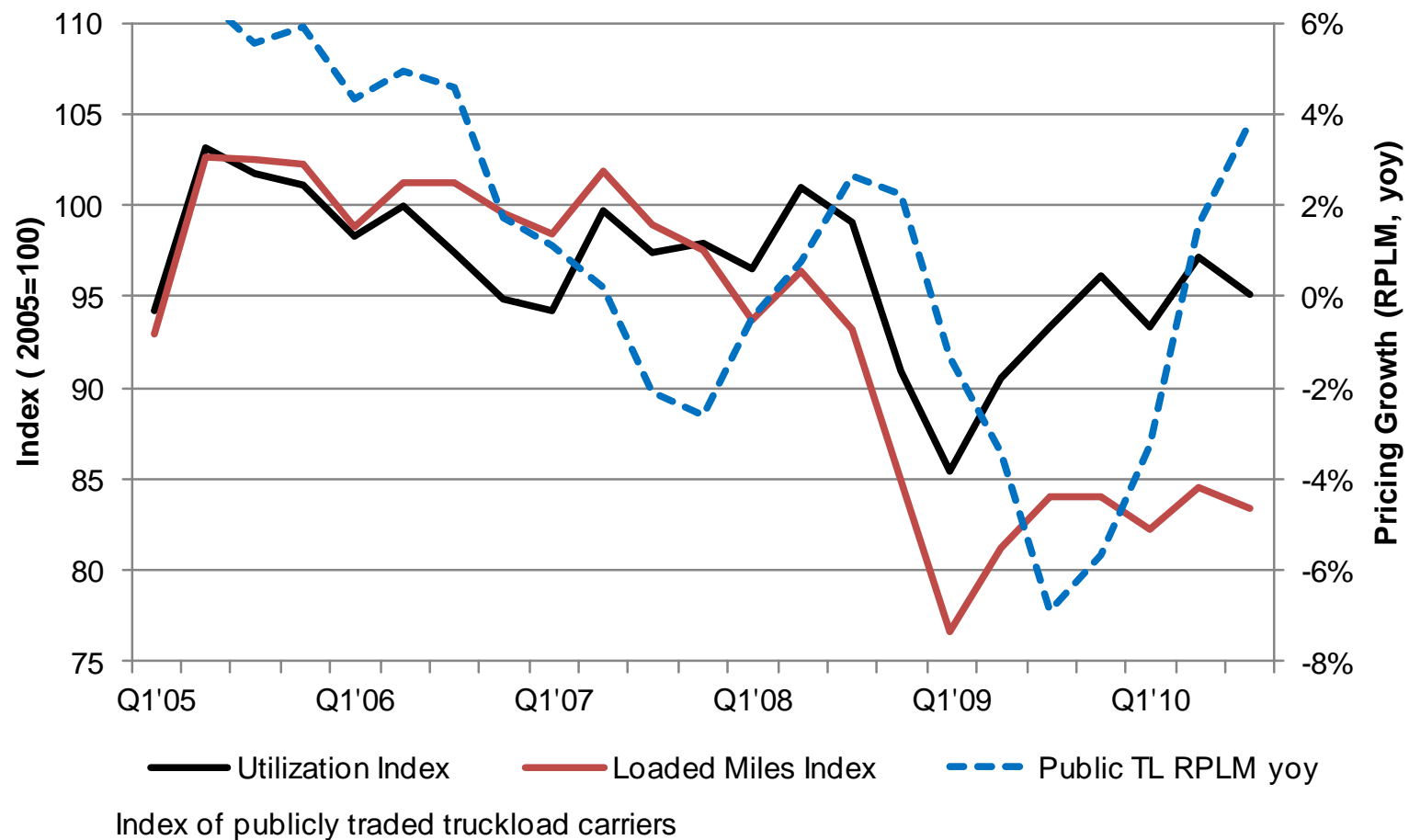
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Truckload Pricing vs. Capacity



# Truck utilization outpacing volumes

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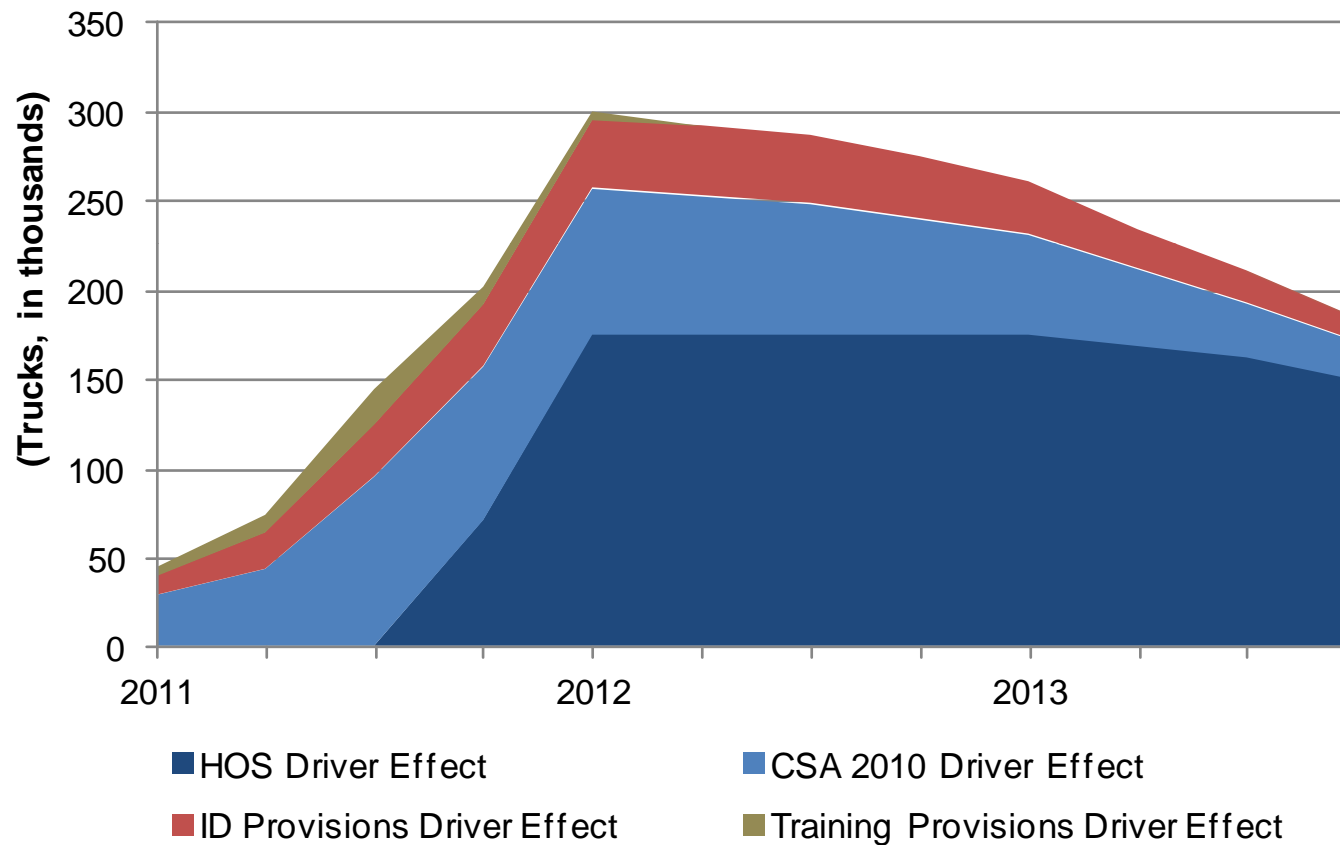


# Numerous constraints to truck capacity

Regulatory, credit, operating costs

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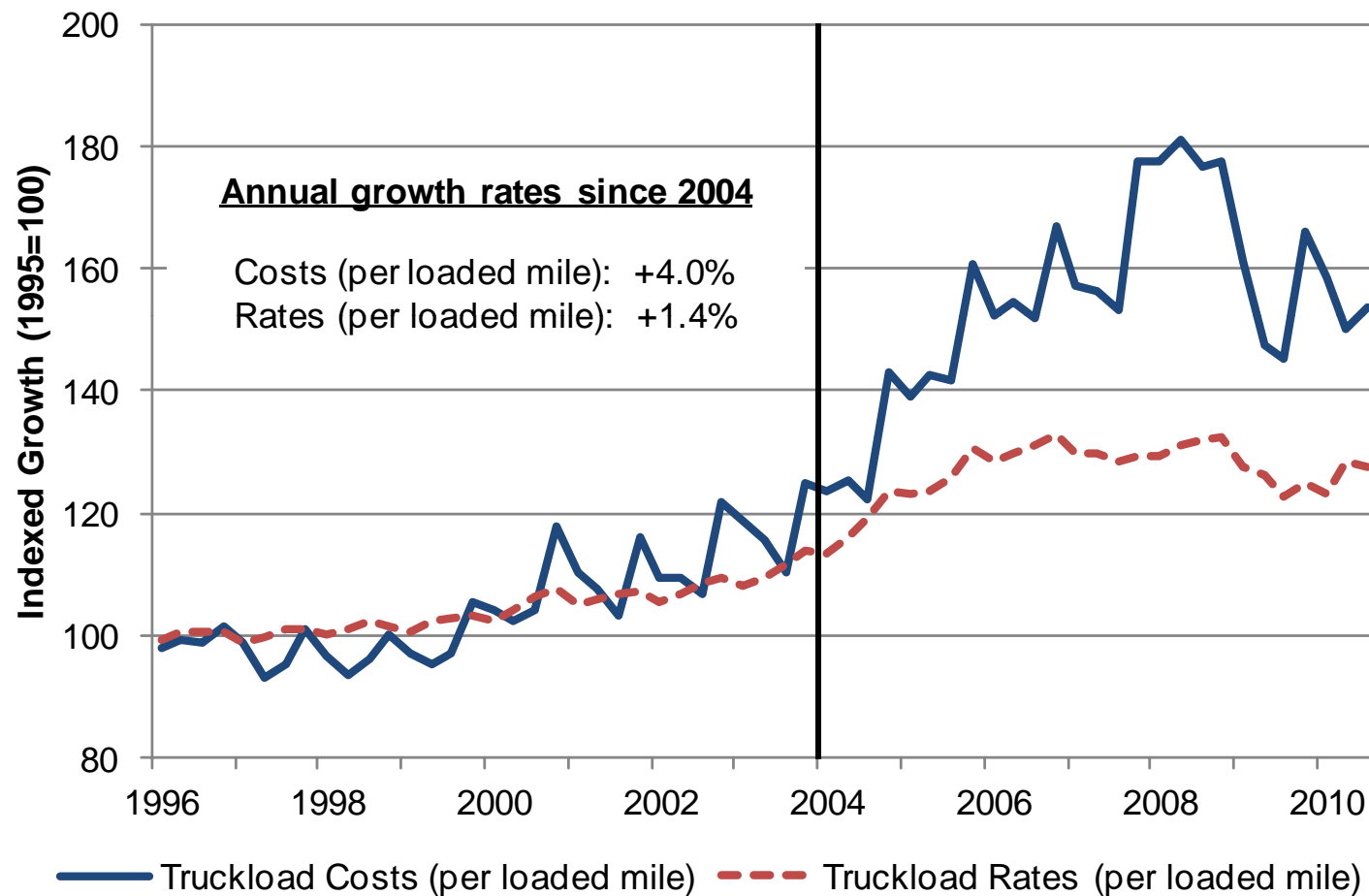
## Cumulative Regulatory Drag



# Numerous constraints to truck capacity

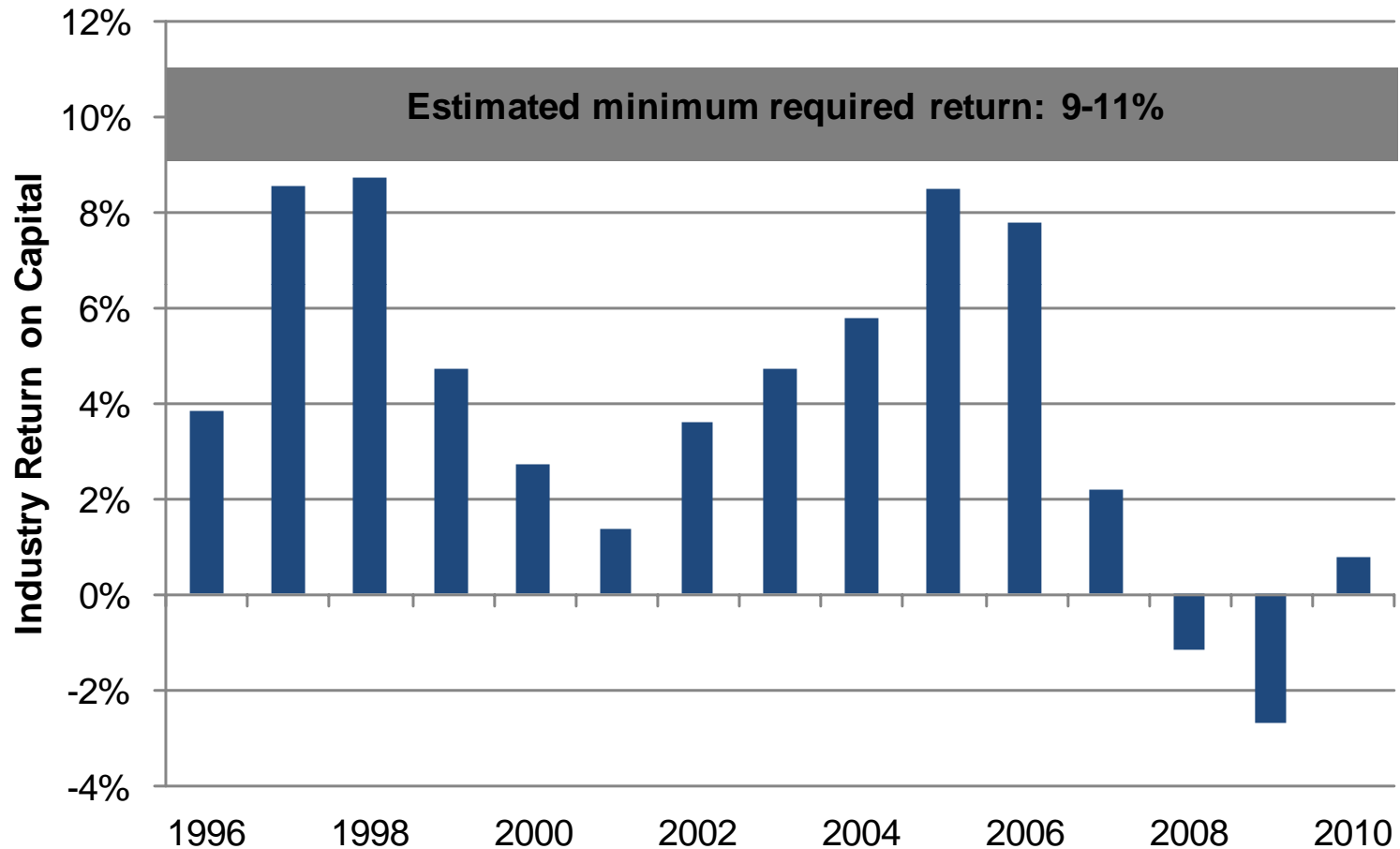
Operating costs continue to rise

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# Inadequate industry capital returns requires higher prices

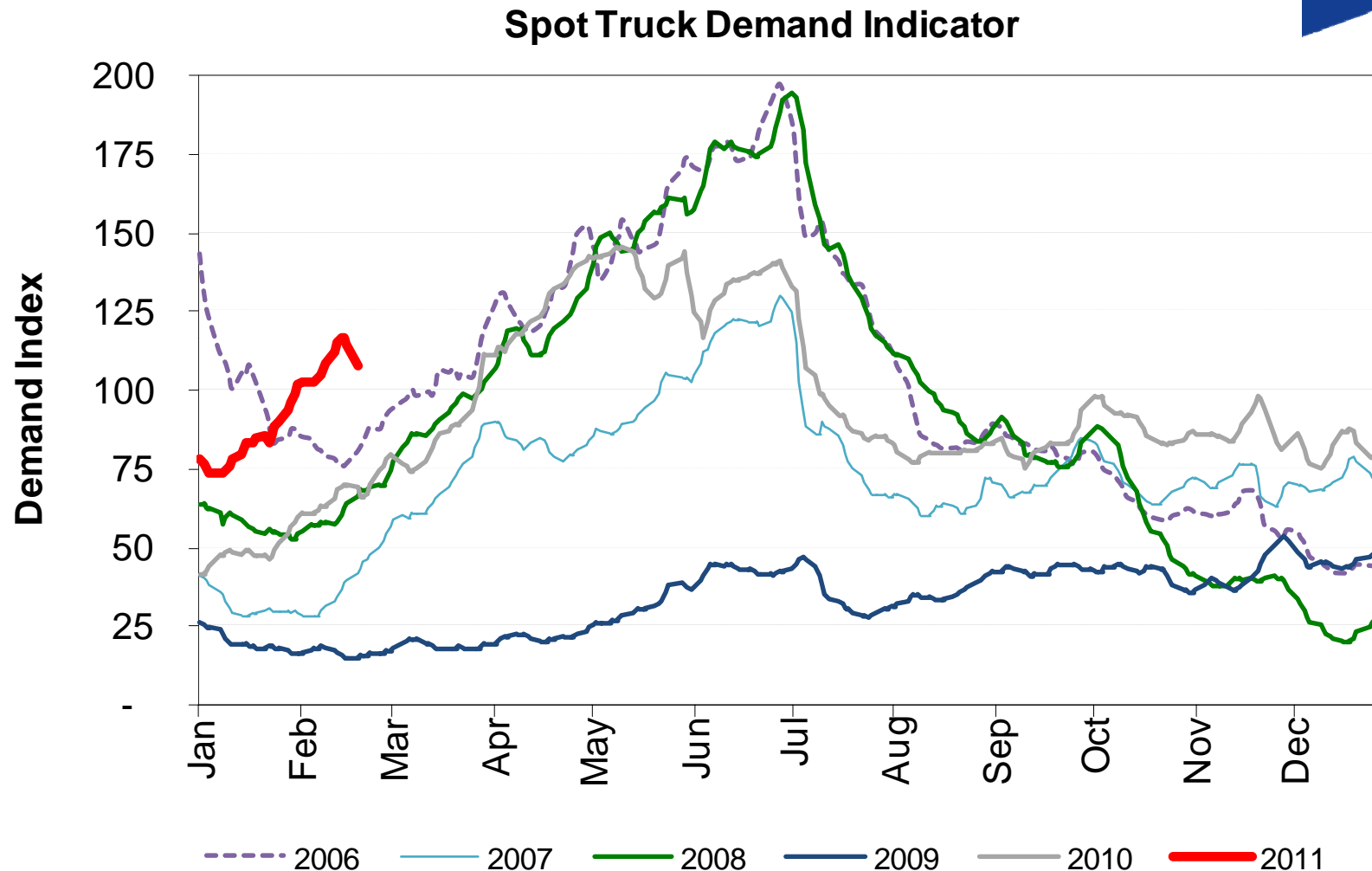
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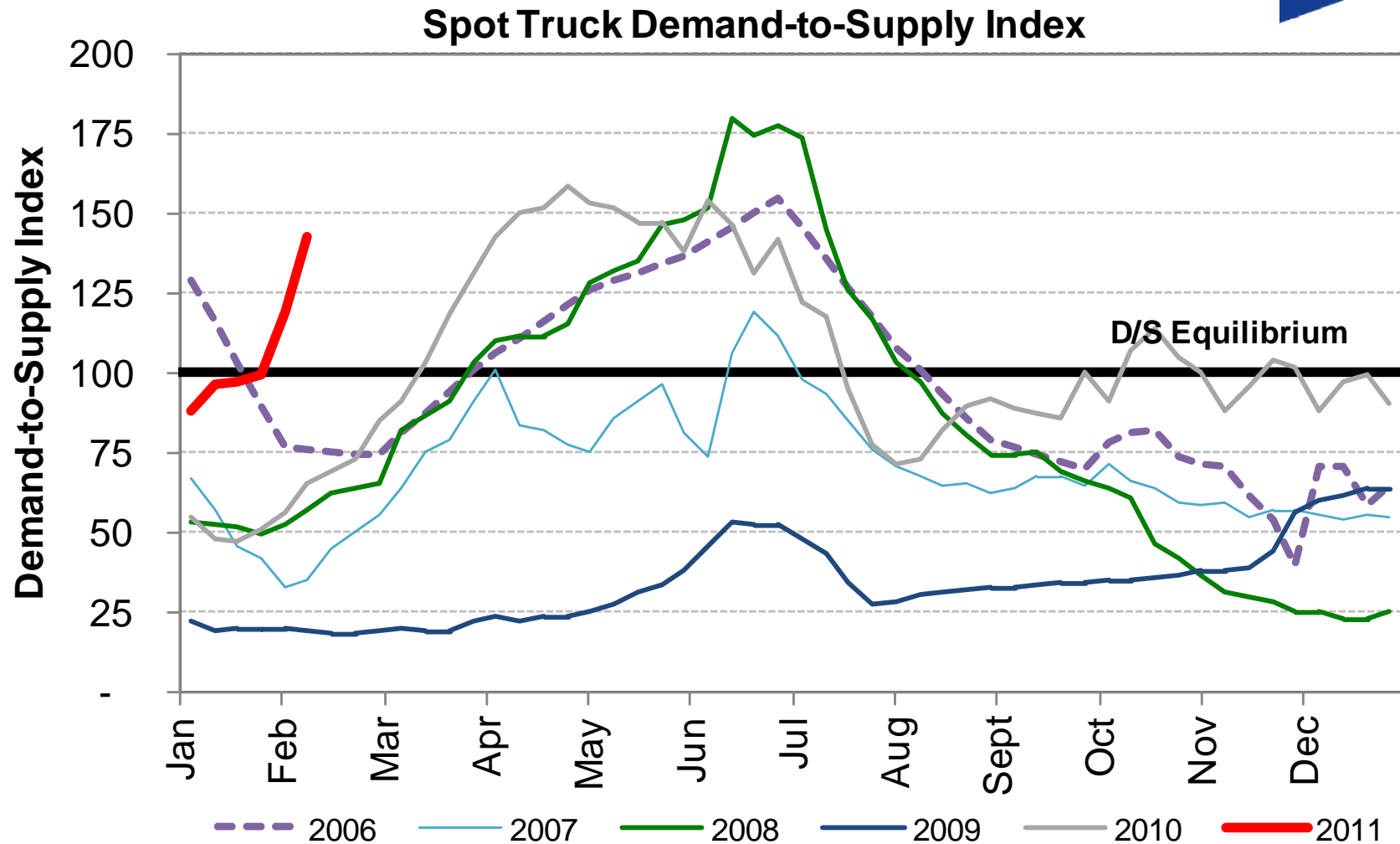
# Spot market demand unseasonably strong

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# Spot market demand per unit of supply

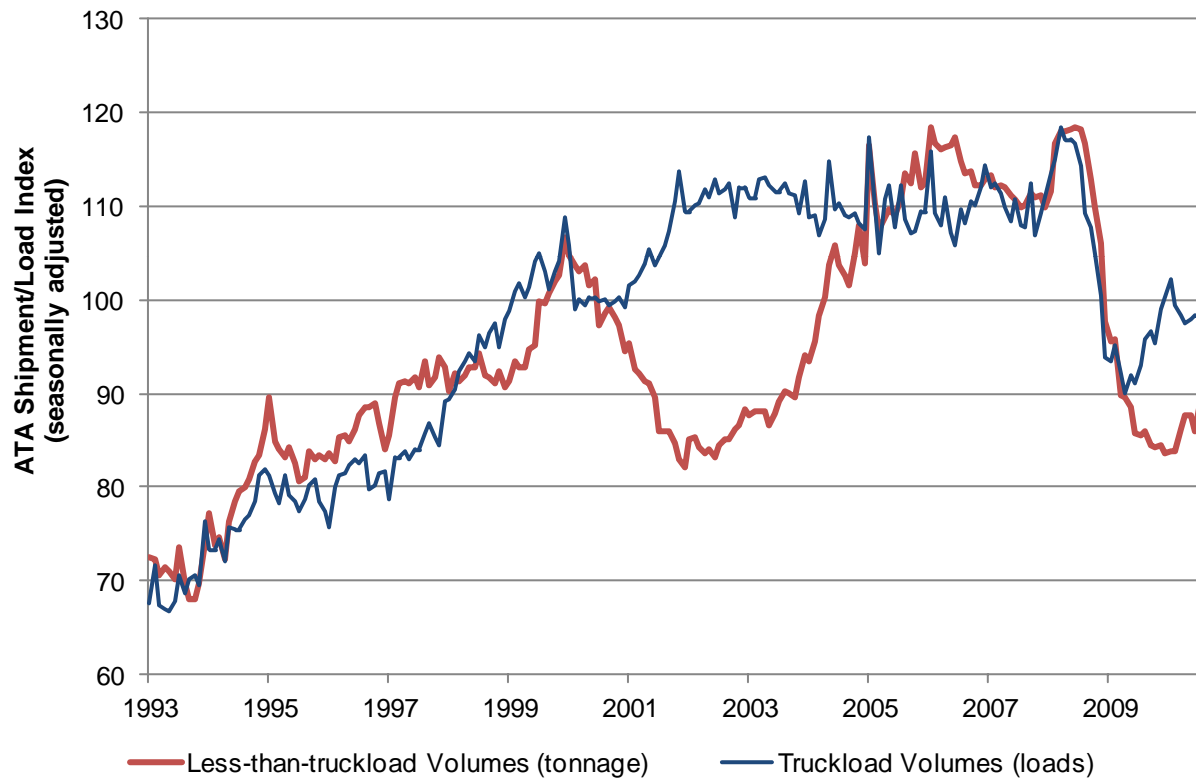
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# LTL volumes lag TL, as expected...

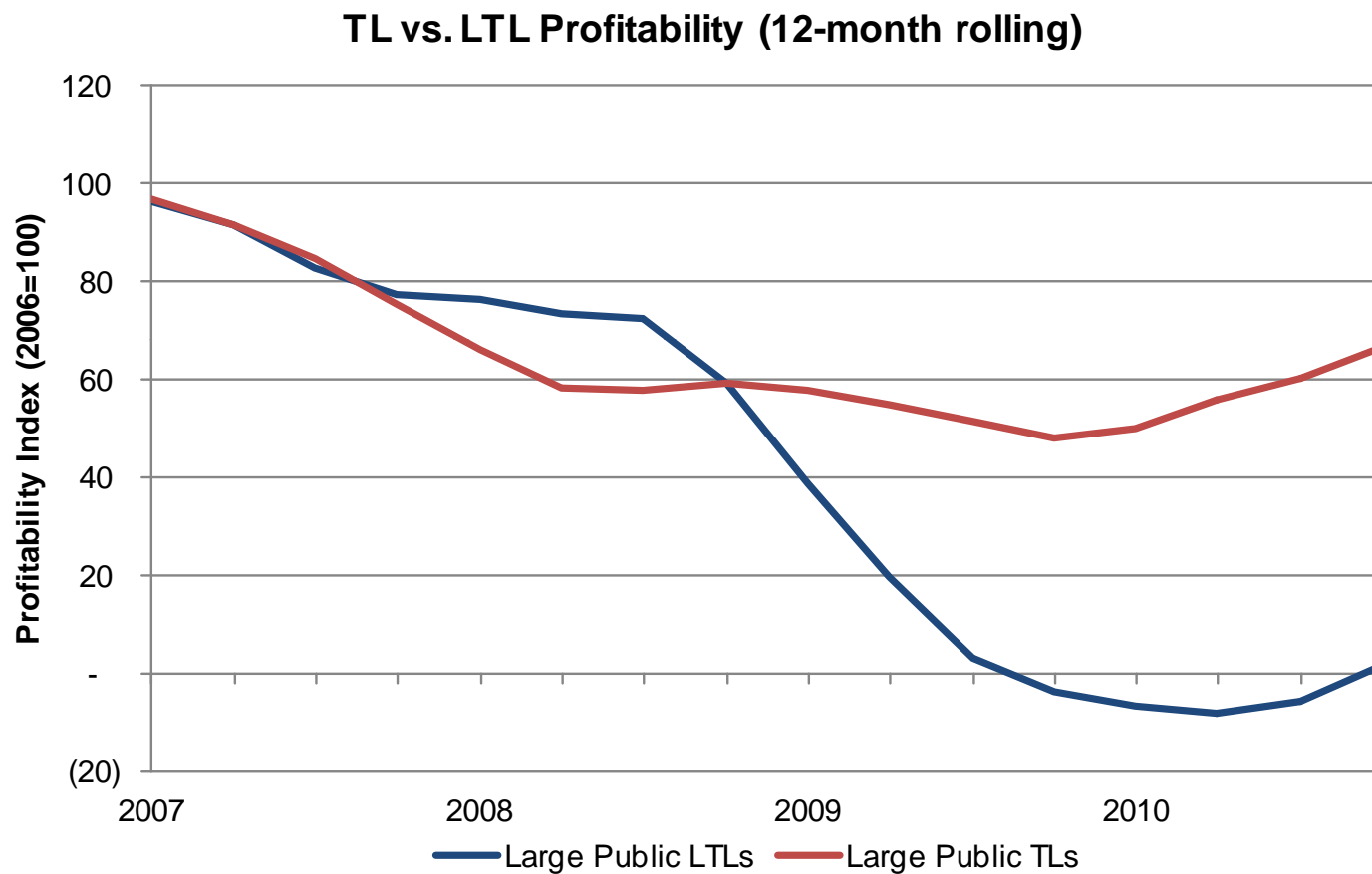
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**Early-Cycle Truckload Volumes Outpace LTL**



...However, LTL profit lag was much more severe

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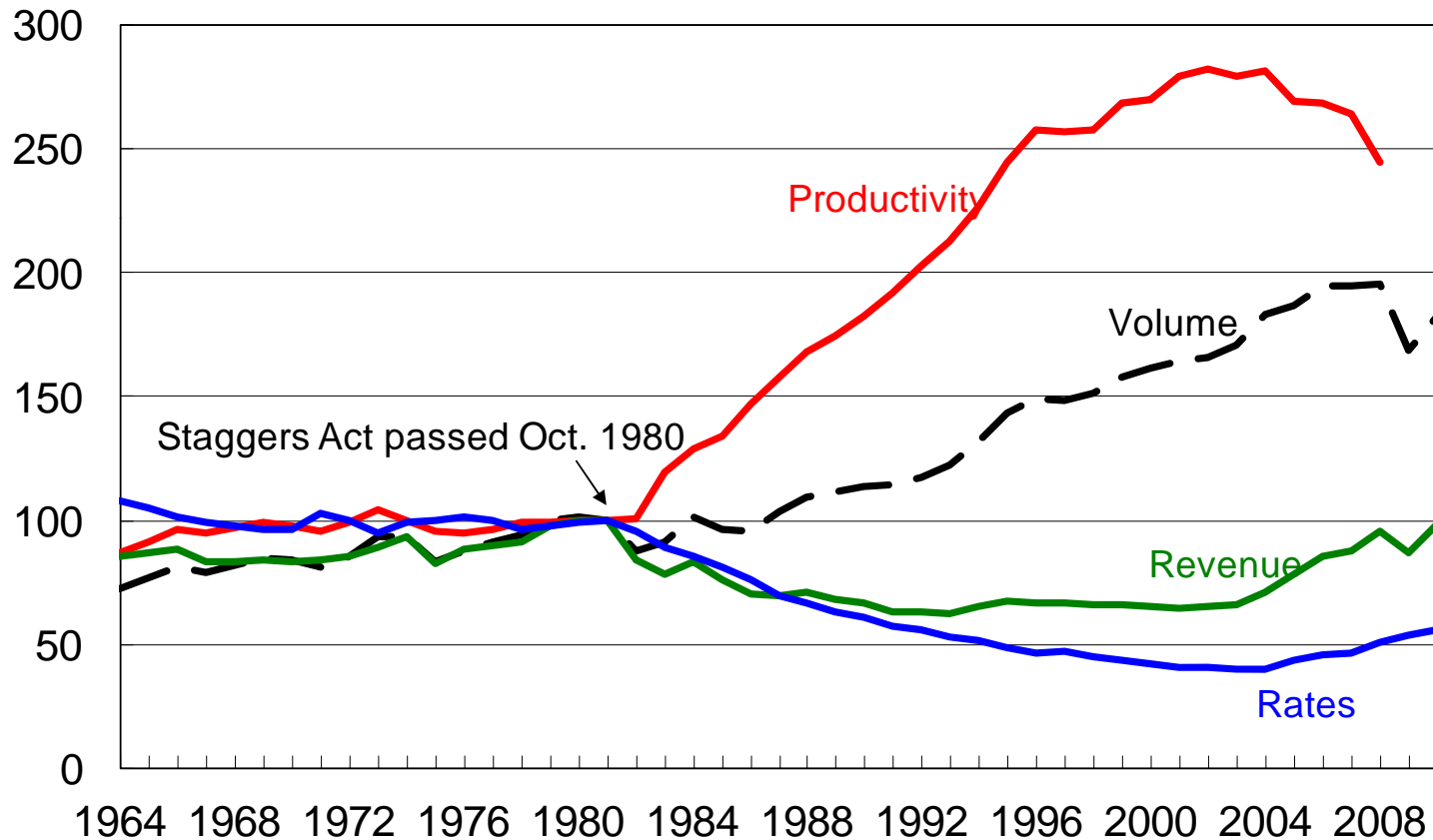


TLs: J.B. Hunt, Knight Transportation, Werner, Heartland Express  
LTLs: Con-way, Old Dominion, FedEx, Arkansas Best

# Rail Pricing Renaissance should continue

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## U.S. Freight Railroad Performance Since Staggers (1981 = 100)



p - preliminary Rates are revenue per ton-mile; volume is ton-miles.

# What did we see from 4Q results?



- Accelerating domestic freight pricing across modes
- Moderating, but positive, freight demand
- Rising costs pressuring earnings
- 1Q outlooks guarded...
- ...but 2011 expectations remain constructive

# 2011 implications for the industry



- Asset owners recouping inadequate capital returns through pricing
- Accelerating truckload pricing, with upside if stronger demand; positive pricing to continue into 2012
- Bid negotiations favoring carriers
- Positive freight growth across modes; deceleration from 2010 levels
- Industrial freight trends stronger than retail given “catch-up”
- 2010’s inventory restocking phase should subside; but lean inventories support future freight growth
- “Easy” freight growth opportunities have passed; providers must refocus on sustainability of growth

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