B. RILEY Advisory Services

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Monitor

Construction & Transportation

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TRANSPORTATION HOPES TO PICK UP SPEED IN 2021

EQUIPMENT DEMAND REMAINS SOFT

New construction equipment sales are down, while pricing for used equipment remains stable

CONSTRUCTION STARTS SLOW TO RECOVER

Total starts were 11% lower through October 2020 on a year-over-year basis

TRUCKS AND TRAILERS BEGIN UPWARD CLIMB

Truck orders in October spiked to their highest level in 24 months

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Overview

After a rocky start to 2020, there is some positivity to recent trends in the transportation and construction markets. Construction tied to residential housing continues its upward momentum, while nonresidential construction continues to display upward and downward trends on a month-to-month basis.

Crude oil demand increased over the summer in response to easing of COVID-19-related stay-at-home orders, as well as vacation and holiday travel, but has since slowed in response to a recent rise in cases and renewed restrictions. Therefore, activity in the oilfield sector, as well as demand for related support equipment, has declined. Consumer confidence has been on a continuous upward climb as of September; however, the recent uptick in COVID-19 cases has led to more uncertainty surrounding the job market and the overall health of the U.S. economy, and subsequently a decline in confidence as of October. These factors have contributed to the month-to-month decline of freight transportation figures.

The market for cranes and other lift equipment has remained stable through the third quarter of 2020 but continues to display signs of softened demand. Construction equipment manufacturers continue to report year-over-year sales declines; however, orders for new equipment are trending positively compared to 2019.

Retail truck sales in North America have increased in recent months but remain down on a year-to-date basis versus 2019. However, orders for new Class 8 truck tractors and trailers have displayed significant growth, as e-commerce continues to drive the industry.

Construction starts rebounded 12% in October after a steep decline in September, but remained 11% lower on a year-over-year basis. Mining equipment demand continues to trend along with demand for mined goods, which has realized some recent growth in the steel and aluminum markets.

Since the beginning of 2020, countries across the globe closed their borders and limited transportation and travel in order to contain the COVID-19 outbreak, creating obstacles for the intermodal and freight industry. While the sector continued to operate and deliver essential goods during shelter-in-place orders that began in March due to its critical infrastructure categorization, it was not immune to pandemic-related slowdowns, which resulted in an 11.8% decline in weekly rail traffic in March. However, the industry started to pick up speed and show signs of improvement in September as retailers restocked their inventories and prepared for the holiday season.

The COVID-19 pandemic has also caused substantial disruptions to the global maritime industry, particularly in the second quarter of 2020. However, with an increase in imports resulting from warehouses and retailers restocking their inventories, the sector started to exhibit record growth beginning in the summer and carrying into the fall.

Cranes & Lift Equipment

Activity in the secondary marketplace for cranes and lift equipment has remained relatively stable, with positive and negative trends throughout the second and third quarters of 2020, despite the effects of COVID-19, which have been felt worldwide. The anticipation is for this sector to return to patterns of growth in the coming months of the new year. Following the close of the third quarter of 2020, where September construction starts dipped 18% compared to August, construction starts realized a rebound of 12% in October to a seasonally adjusted annual rate of $787.9 billion, according to Dodge Data & Analytics ("Dodge").

While the positive momentum helped in the recovery of what was lost in September, it did not completely offset it. Total construction starts were 11% lower through October compared to the same time period in 2019. While residential starts displayed a 2% increase, nonresidential and nonbuilding starts were down 24% and 14%, respectively. While statistics continue to change on a month-to-month basis, Dodge predicts that although it may be slow, total construction starts will realize overall positive growth, with an anticipated 4% increase in 2021 to $771 billion. One of the drivers of this growth will be the booming e-commerce industry, as a significant increase in online sales has resulted in retailer demand for increased warehouse space. As warehouse construction is included in the commercial building vertical, Dodge anticpates that this sector will rebound by 5% to $113 billion in 2021.

Reported utilization rates from many of the major rental equipment providers have displayed slight declines in all classes, including tower cranes. This is not only an effect of the cyclical nature of the construction industry, but more so that of the continuous effects of the pandemic. This, however, has not necessarily affected this type of equipment in the secondary marketplace.

Many companies are in a type of hold pattern as they wait for the economic impacts of the pandemic to subside. For this reason, used equipment demand is soft; however, pricing remains relatively stable as many companies are also not rushing to sell surplus equipment in the current market. Considering these factors, many major OEMs had scaled back production during this time to meet the decline in demand and manage existing inventory; however, a rebound in manufacturing may be on the horizon.

The Manitowoc Company reported a third-quarter decrease of 20.6% in year-over-year sales, while third quarter-orders for new equipment increased 10.5% to $389.9 million versus the same period in 2019.

Auction activity for cranes remains slow due to restrictions put in place by state governments prohibiting large gatherings, and all bidding remains online. Cranes in good condition, with relatively low hours, and of newer vintage, are the most sought after by potential buyers.

Trucks & Trailers

A decline in sales of new and used truck tractors and trailers, which started in late 2019 and trickled into 2020, was further exacerbated by the COVID-19 pandemic. Recent trends, however, have shown a positive recovery, in some cases, for the transportation industry. According to ACT Research ("ACT"), October 2020 Class 8 truck orders spiked at 38,900 units, the highest total in the past 24 months, which represents a 27% increase from the previous month and a 78% increase versus October 2019. Industry analysts anticipate that the upward trend will continue through mid-2021 and perhaps longer.

Additionally, total trailer orders for October were 54,691 units, an almost 7% increase from the prior month, and an 80% increase from October 2019. This increase is represented by a significant rise in dry van orders by large fleets, as a result of a growth in e-commerce. ACT reported that October 2020 trailer orders represented the third-highest in industry history.

Retail sales of new Class 8 tractors totaled 18,774 units, which represents the second-highest volume of the year after September, but an 18.4% decline from October 2019. On a year-to-date basis, sales have declined 34.9% to 152,695 units compared to the 234,721 units in 2019. According to the American Trucking Associations, the seasonally adjusted For-Hire Truck Tonnage Index decreased 6.3% in October, after a 5.7% increase in September, with the decrease largely attributed to seasonal fluctuations in combination with the global pandemic.

Following September, when used Class 8 tractor sales came in at 20,500 units, October sales totaled approximately 21,100 units, which represents a flat trend compared to October 2019. Year-to-date used sales rose to 204,800 units versus 197,400 units in 2019. The average price of a used Class 8 tractor in October rose to $41,812 per unit, an increase of 8% since October 2019, when the price averaged around $38,743 per unit. The average age of a used Class 8 sold was six years and six months, with mileage averaging around 450,000 miles.

Construction & Mining Equipment

As of October 2020, total construction spending increased 1.3% to $1.438 billion compared to the prior-month estimate of $1.420 billion. The private sector realized a total 1.4% increase in spending, with residential construction showing the largest month-to-month growth of 2.9% in October compared to September. As previously mentioned, larger construction companies have reported slight decreases in utilization, which is evidenced by the slight decrease in spending of 0.7% for nonresidential construction. It should be noted, however, that public construction fared somewhat more positively, where spending increased slightly to $344.8 billion, a 1% increase from the September estimate of $341.4 billion.

Consequently, construction equipment manufacturers and rental construction equipment companies are reporting year-over-year decreases in net sales. Construction equipment manufacturer Terex Corporation posted a decrease in net sales of 25.3% through the third quarter of 2020, while JLG, a division of Oshkosh Industries, posted a net sales decrease of 33.9% over the same period in 2019. Additionally, Caterpillar, a leading OEM in the industry, realized a sales decrease of 23% in the third quarter.

While the markets for this type of equipment remain low or absent of notable growth, many continue to be encouraged in regard to the long term. The secondary marketplace for construction equipment has softened throughout the course of the ongoing pandemic. Continuing economic uncertainty has driven down the current demand for used construction equipment. The need for and orders for new equipment have slowed following the contraction of the construction industry, yet pricing of equipment in the secondary marketplace remains relatively stable in some cases.

Equipment in good condition with low hours tends to bring in premium prices; however, the value of equipment in less-than-good condition, with higher hours, has continued to decline. As the economy begins its road to recovery and construction starts and spending continue to stabilize, equipment related to infrastructure and nonresidential construction, such as excavators, wheel loaders, bulldozers, motor graders, and other similar equipment, are expected to return to more steady demand levels.

Despite the impacts seen across other verticals, the steel and aluminum industries were considered essential during the outbreak of COVID-19, and demand and market prices for flat rolled steel, copper, and aluminum have more recently rebounded strongly in the months of October and November. Steel mill utilization is over 71% and mill lead times have stretched to seven to nine weeks. The three-month London Metal Exchange (“LME”) copper price of $3.48 per pound has not been seen since December 2013, while the three-month LME aluminum pricing spiked to its highest point in 2020 at $0.91 per pound.

In late October 2020, China blacklisted a wide range of Australian commodities, including thermal and met coal, due to Australia’s decision to bar Huawei Technology Co., Ltd. from building Australia’s 5G cellular network in 2018. Chinese power stations and steel mills were told to stop using Australian coal and Chinese ports were instructed not to offload the fuel. As a result, there is a flotilla of more than 50 ships that have been waiting over a month to offload at the Chinese ports. The ban is easing somewhat as the first cargo of Australian coal, weighing 135,000 tons, was expected to clear customs in the second week of December.

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Intermodal & Freight Rail

As retailers restocked their shelves in preparation for the holiday season, the intermodal and freight sector showed signs of recovery in September 2020 after solid pandemic-related declines through July, with the month representing the fourth-strongest intermodal month in history. According to the Association of American Railroads ("AAR"), while combined U.S. carload and intermodal originations in September 2020 were 2.4 million, down 1%, or 25,558 carloads and intermodal units versus September 2019, the decline marked improvement compared to a few months ago.

U.S. railroads originated 912,772 carloads in October 2020, down 6.6%, or 64,634 carloads, from October 2019, while containers and trailers for the month increased 10%, or 105,966 units, to 1.2 million containers and trailers versus the same month last year. Combined U.S. carload and intermodal originations in October 2020 were 2.1 million, up 2%, or 41, 332 carloads and intermodal units from October 2019.

Per the AAR, 10 out of the 20 carload commodity categories tracked each month experienced carload gains compared with the previous year, including grain, up 21,66 carloads or 25.5%; iron and steel scrap, up 3,579 carloads or 29.1%; and waste and nonferrous scrap, up 1,527 carloads or 11.2%. The increase in the 10 carload categories represented the most since the pandemic began. Carloads of grain for October were their highest in 13 years, while carloads of motor vehicles and parts have recovered after falling close to 90% earlier this year. Commodities that saw declines during the same period included coal, down 56,343 carloads or 19.1%; crushed stone, sand, and gravel, down 14,275 carloads or 16.0%; and petroleum and petroleum products, down 10,199 carloads or 20.0%.

According to the AAR's senior vice president John T. Gray, October represented the best month ever for U.S. rail intermodal, with volumes up by a third from April of this year, primarily due to rising imports and inventory restocking in preparation for the holidays.

Industrial Marine

Container trade grew moderately in 2019 due to a slowdown in manufacturing and export orders worldwide, while the COVID-19 pandemic further impacted global demand in 2020. At the peak of the pandemic, when cargo volumes were declining, the container shipping industry cut capacity and reduced costs in order to maintain profitability instead of market share. Additionally, several governments, through their border agencies, port authorities, and customs administrations, made reforms to keep trade flowing while adhering to health and safety protocols. As a result, freight rates remained at stable levels despite a decline in demand, with ports on both U.S. coasts reporting volume surges in October 2020.

With a surge in imports, the nation's ports are reporting record or near-record activity as warehouses and stores restock eight-plus months into the COVID-19 pandemic. The global outbreak resulted in a significant economic disruption in the second quarter, only to be followed by record growth beginning in the summer and carrying into the fall.

The Port of Los Angeles, the nation's largest, reported on November 18, 2020 that it processed 980,729 20-Foot-Equivant Units ("TEUs") in October, an 18% increase year-over-year from 770,289 TEUs. "Marine terminals are getting squeezed from both sides. Vessels are coming in very full and at a faster pace, and they're also looking to turn back to Asia as quickly as possible," said Gene Seroka, the port's executive director. "We see trucking and railroad resources that are stretched thin and local warehouses that are at, or near capacity." Seroka estimates that container numbers will remain strong through February 2021.

The Port of Long Beach also reported a record month in October, with 806,603 TEUs processed, representing an increase of 17.2% from the previous year. The volume represents the first time in the port's history it has topped 800,000 containers and compares with 688,425 TEUs handled in the 2019 period.

The Port of Oakland reported a 5.8% year-over-year increase in container volume, moving 216,686 units in October, compared with 204,880 in 2019. The only West Coast port to report a year-over-year decline was the Northwest Seaport Alliance, which operates facilities in Seattle and Tacoma, Washington. Those ports moved 296,892 TEUs in October, a 4.2% decline compared with 310,066 containers the previous year. East Coast ports also reported record numbers.

However, while domestic ports are experiencing an increase in demand, pandemic-induced container shortages in major export ports are leading to higher freight rates from Asia. The shortage is largely caused by companies that had stopped purchasing at the start of the pandemic ramping up inventory, which resulted in a significant increase in demand for container shipments from Asia. Additionally, some U.S. companies that shut down operations during the stay-at-home orders stopped shipping goods in containers back to Asia, which also contributed to the shortage. Market participants said they have seen container rates from Southeast Asia to the U.S. increase to as high as $4,500 per 20-foot container TEU. The supply crunch is disrupting delivery times and forcing buyers to look for domestic supply or other alternatives.

Overall, with a new surge in COVID-19 cases and an ongoing trade dispute between the U.S. and China, the maritime sector is bracing for shockwaves that are still to come.

Monitor Information

B. Riley Advisory Services' *Construction & Transportation Monitor* relates information covering most transportation sectors, including industry trends and their relation to our valuation process.

B. Riley Advisory Services strives to contextualize important indicators in order to provide a more in-depth perspective of the market as a whole. B. Riley Advisory Services welcomes the opportunity to make our expertise available to you in every possible way. Should you need any further information or wish to discuss recovery ranges for a particular segment, please feel free to contact your B. Riley Advisory Services Business Development Officer.

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Experience

B. Riley Advisory Services' has worked with and appraised a number of companies within the construction and transportation industry, including industry leaders in heavy mobile equipment, freight rail, marine, and aerospace. B. Riley Advisory Services's extensive record of transportation inventory and machinery and equipment valuations also features appraisals for companies throughout the entire supply chain, including manufacturers and distributors, maintenance and repair companies, and freight rail refurbishing companies.

B. Riley Advisory Services' extensive experience includes valuations of major businesses in the construction and transportation industry such as:

- One of the largest providers of crane rental services in all sizes and varieties in North America.
- Long-standing providers of truckload shipping services for chemicals, petroleum, and energy sector products.
- A heavy civil construction company specializing in building and reconstruction of transportation/water infrastructure projects.
- A leading miner and explorer of coal properties.
- Providers of locomotives supplying more than 50 railroads including Class I and commuter rail systems.
- Manufacturers and distributors of inland and ocean-service vessels and equipment, as well as OEM and aftermarket marine components and accessories, for the industrial marine and recreational boating industry.
- Manufacturers and distributors of OEM components and parts for aircraft, helicopters, ships, submarines, ground systems, avionics, and other commercial airline and defense applications.

Moreover, B. Riley Advisory Services has liquidated and been involved in the asset disposition of many companies in the construction and transportation industry.

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