B | RILEY Advisory Services

DECEMBER 2022

# Monitor

## Construction & Transportation


# DELIVERY DELAYS RAISE PRICES

### EQUIPMENT PRICES BEGIN TO STABILIZE

As demand falls for newer equipment and availability of older equipment rises, prices have begun to stabilize

### CLASS 8 ORDERS SKYROCKET

September Class 8 truck orders skyrocketed as manufacturers fully opened order boards for 2023

### WEST COAST PORT CONGESTION FALLS

Rerouted shipping lines have caused East Coast port congestion to rise while falling on the West Coast

# In This Issue

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# Overview

Global supply chain issues have begun to ease compared to historical peaks experienced in 2020 and 2021. The global supply chain pressure index declined from 3.8 in November 2021 to 1.0 in October 2022, suggesting supply chain constraints are falling to historical norms.

Consumer demand and spending have also begun to fall, as evidenced by a decline in ocean and rail freight rates compared to 2021 levels.

Total construction starts increased 8% in October 2022 following a disappointing September, driven by increases in nonresidential and nonbuilding segments per Dodge Construction Network ("Dodge"). Residential construction starts declined, however, due to rising interest rates. Demand for new and used heavy equipment remains elevated as manufacturers work through historical backlogs. Recent price increases coupled with healthy demand benefited OEMs in the third-quarter of 2022. Moving forward, demand for heavy equipment is expected to be driven by increased infrastructure development and upgrades but may be tempered by increased energy costs, geopolitical conflicts, and rising interest rates.

Truck manufacturers have fully opened order boards for 2023 as supply chain constraints and component shortages begin to ease, causing orders for Class 8 trucks to skyrocket in September and October 2022. Although supply chain constraints are expected to continue easing into 2023, manufacturers have kept order goals conservative after having to scale back orders in 2022 due to component shortages.

Prices for used trucks have fallen in recent months as owner-operators that entered the freight trucking market amid record spot rate levels have begun exiting in droves, increasing the amount of used trucks available on the market.

Import container volume fell month-over-month and year-over-year in September 2022. Port congestion on the West Coast has significantly eased from the peaks experienced in the spring of 2022 as ocean freight carriers rerouted paths to East Coast ports due to a possible strike.

The Biden Administration attempted to broker a deal between railroad unions and management companies in September, which was widely rejected by unions, leading to weeks of unsuccessful negotiations and railroad unions declaring a deadline of December 9th to strike. Fearing the possibility of a strike, the Biden Administration passed a labor bill in late November and a second bill guaranteeing seven days of paid sick leave to rail workers, one of the biggest points of contention in negotiations. The bills are currently headed to the Senate; should they not pass ahead of December 9th, a strike may occur and severe economic turmoil would result.

# Cranes & Lift Equipment

Total construction starts increased 8% in October to a seasonally adjusted rate of $1.12 trillion per Dodge. Nonresidential starts increased 9% while nonbuilding starts increased 26%, driven by a 57% increase in highway and bridge starts. However, residential starts fell 3% in October. Total construction starts for the first 10 months of 2022 were 16% above the first 10 months of 2021; nonresidential and nonbuilding starts were 37% and 17% higher than the first 10 months of 2021, respectively, while residential starts remained flat.

The availability of new crane and lift equipment remains limited as manufacturers work through significant backlogs; price increases have also been implemented in recent months as input material prices have risen. Demand for newer and well-maintained equipment has fallen from previous peaks over the last 18 months but remains elevated compared to pre-pandemic levels. Equipment prices have begun to stabilize due to the increased availability of older equipment on the used and auction markets. Although infrastructure investments will keep projects in the pipeline for crane and lift equipment, price adjustments will be needed to factor in increased labor and fuel costs.

Despite rental firms experiencing increased utilization rates, increases in fuel and labor costs have reduced profits. The strong American dollar has also begun to impact OEMs due to significant fluctuations in foreign currency exchange rates. OEMs also continue to contend with supply chain constraints and inflationary pressures.

The Manitowoc Company, Inc. (“Manitowoc”), a leading global manufacturer of cranes and lift equipment, reported third quarter 2022 net sales of $454.7 million, a 12.4% year-over-year increase; however, third quarter orders fell 12.7% year-over-year to $472.0 million. Both third-quarter sales and orders were negatively impacted by changes in currency exchange rates. Manitowoc reported a backlog of $943.4 million for the third quarter, slightly below the second quarter backlog of $947.8 million.

Lower consumer confidence, geopolitical tensions, inflation, and rising interest rates are all expected to present challenges for OEMs in the coming months. However, increased construction spending, particularly in infrastructure and industrial construction, is expected to drive demand or utilization of cranes and lift equipment.

# Trucks & Trailers

Preliminary Class 8 truck orders reached 42,500 units in October 2022, an increase from 23,391 units in October 2021 but below the historical record of 53,700 units in September 2022, which was 97.8% above September 2021 per ACT Research ("ACT"). The skyrocketing increase in orders is the result of manufacturers fully opening order boards for 2023 as visibility for the price and availability of materials has improved. Demand for new trucks remains significantly elevated as manufacturing has been limited over the past two years due to supply chain constraints and component shortages, both of which have eased in recent months. The August 2022 backlog for Class 8 orders totaled 197,000 units with only 8,000 units slated for delivery in the second quarter of 2023. Net trailer orders for September reached 26,086 units, a 47% month-over-month increase but 8% below September 2021 orders.

Class 8 truck retail sales totaled 22,863 units in October, 34.5% above October 2021, and relatively in-line with September 2022 sales. For the 10 months ended October 2022, retail sales of Class 8 trucks have increased 11.8% to 202,088 units. ACT anticipates Class 8 retail sales to total 259,000 units in 2022 versus 221,889 units in 2021. As the supply chain continues improving into 2023, production levels are expected to begin approaching pre-pandemic norms for the first time since 2020. The current production backlog and average age of trucks currently in use is expected to drive strong demand in 2023. Although manufacturers have opened order boards for 2023, their goals remain conservative following cancelled orders in 2022 related to component shortages.

The American Trucking Association's ("ATA") seasonally adjusted for-hire truck tonnage index fell 2.3% month-over-month in October 2022, the largest monthly decline since March 2020 but 2.8% above October 2021, marking the 14th consecutive year-over-year gain but the smallest increase since April. The month-over-month decline occurred alongside a slightly depressed fall freight season and slowing economy.

The average retail price for used Class 8 trucks was $86,732 in August 2022, 6.4% below July prices and 28.5% above August 2021 per ACT. Used Class 8 truck prices are approximately 40% below peak prices in the spring of 2022 and are falling an average of 8% per month. The price decline comes as owner-operators, who entered the market amid record spot rates in 2021, have begun exiting just as quickly as spot rates fell, putting their trucks back onto the resale market. Despite recent declines, used Class 8 prices still remain elevated compared to pre-pandemic levels as OEMs were forced to reduce 2022 build plans and set modest goals for 2023. Used Class 8 truck prices are expected to continue declining into 2023 as demand for heavy-duty equipment begins to return to pre-pandemic norms.

# Construction & Mining Equipment

As of September 2022, total construction spending reached an annual adjusted rate $1,811.1 billion, a 0.2% increase from August and 10.9% above September 2021. For the first nine months of 2022, total construction spending amounted to $1,353.7 billion, an 11.4% increase above the same period in 2021. Private sector expenditure totaled $1,450.3 billion, 0.4% above August; residential construction spending totaled $918.0 billion in September, equivalent to August. Nonresidential construction spending totaled $532.3 billion, 1.0% above August. Public construction spending totaled $360.9 billion in September, 0.4% below August. Educational spending totaled $78.2 billion, unchanged from August while highway construction spending increased 1.7% to $108.4 billion.

According to a recent survey conducted by the Association of Equipment Manufacturers, 44% of respondents report supply chain constraints have eased in 2022 versus 2021. Demand for both new and used equipment remains elevated while record backlogs continue. The Terex Corporation reported sales of $457.9 million for the third quarter of 2022, a 9.4% year-over-year increase. Caterpillar, Inc. reported sales of $15.0 billion for the third quarter of 2022, a 21% increase from the third quarter of 2021. Both companies attributed the increase in sales to favorable price realizations and healthy demand. Moving forward, equipment demand is expected to be driven by increased infrastructure development and upgrades funded by government and private investment, but growth may be tempered by rising energy costs due to the ongoing Russia-Ukraine conflict and rising interest rates.

Building material prices declined 0.3% month-over-month in September; material prices have declined 2.3% since June, the largest quarterly drop since April 2022 in-line with the overall economy and slowing housing market, driven by a 2.9% drop in September lumber prices and a 6.7% decline in steel mill prices per the Producer Price Index. Although prices have been declining in recent months, building material prices still remain elevated compared to pre-pandemic levels.

The Energy Information Administration estimates U.S. coal production to reach 598 million short tons (“MMst”) in 2022, a 20 MMst increase over 2021. Worldwide consumption is expected to increase 0.7% to 8 billion tonnes in 2022, following a 6% increase in 2021; the increases in coal consumption have been driven by rising natural gas prices due to the ongoing Russia-Ukraine conflict. Rising natural gas prices have made coal more competitive, causing international coal prices to rise, hitting three historical peaks between October 2021 and May 2022. Sanctions and bans on Russian coal have caused market disruptions, contributing to coal shortages, driving prices. Moving forward, international coal prices are expected to remain elevated as tight market conditions continue.

# Intermodal & Freight Rail

North American rail volume decreased 0.7% to 334,731 carloads for the week ended November 12, 2022 as reported by the Association of American Railroads. Intermodal units fell 4.9% to 335,949 units for the same week.

U.S. rail traffic totaled 490,350 carloads and intermodal units for the week ended November 12, 2022, a 2.5% decline from the same week in 2021. Carloads fell 0.2% to 235,474 units while containers and trailers fell 4.5% to 254,876 units. For the first 45 weeks of 2022, total U.S. combined rail traffic was 22,285,808 carloads and intermodal units, a 2.5% decrease from the same period in 2021. Carloads increased 0.2% to 10,450,126 carloads while intermodal units declined 4.7% to 11,835,682 units.

Four out of 10 commodity groups posted increases for the week ended November 12, 2022 compared to the same week in 2021. Motor vehicles and parts increased 9.3% to 23,283 carloads; farm products excluding grains and food increased 4.9% to 27,058 carloads; nonmetallic minerals increased 3.3% to 42,490 carloads; and grain increased 0.2% to 36,869 carloads.

Combined North American rail volume, on 12 reporting U.S., Canadian, and Mexican railways, for the first 45 weeks of 2022 totaled 30,550,437 carloads and intermodal units, a 2% decrease from the same period in 2021. Canadian railroads reported combined traffic of 6,567,421 carloads and intermodal units for the first 45 weeks of 2022, a 1.8% decrease compared to the same timeframe in 2021. Mexican railroads reported a total of 1,697,208 carloads and intermodal units, a 3.5% increase compared to the same period in 2021.

In September, the Biden Administration brokered an agreement between railroad unions and freight management companies, which was ultimately rejected by the unions. This led to weeks of unsuccessful negotiations, causing unions to set a deadline of December 9th to strike should an agreement not made. In order to avoid a strike, the Biden Administration passed a labor bill in late November. A second bill was also passed, guaranteeing rail workers seven days of sick leave, one of the biggest points of contention in negotiations. The bill is currently headed to the Senate; should it not be passed ahead of December 9th, a strike may occur, leading to widespread, severe economic turmoil.

# Industrial Marine

Lower consumer demand is being reflected in import levels as import container volume declined to 2,215,731 containers in September 2022, 12.4% below August and 11.0% below September 2021. All 10 U.S. ports experienced a decline in import volume in September. The Port of New York and New Jersey experienced a lower 2.3% month-over-month decline while volumes fell 17.6% and 17.3% at the Ports of Long Beach and Los Angeles, respectively. Import volume at the Port of Savannah fell 21.5% month-over-month due to the impact of Hurricane Ian.

Imports continue to route to East Coast ports as West Coast logistics managers fear a possible strike while unions and port management negotiate new contracts. The top five East Coast ports handled 48.2% of total import container volume in September 2022, up from 4.1% in August while the top five ports on the West Coast decreased from 41.9% in August to 37.0% in September. The International Longshore & Warehouse Union and Pacific Maritime Association have been negotiating new contracts since July 2022.

Port congestion has also begun to ease from peaks experienced earlier in 2022 as delays at the Ports of Long Beach and Los Angeles fell below seven days in September. Despite declining from August, East Coast port delays remained above 10 days in September with the Port of Savannah reaching 14.2 days. Since the beginning of the year, the number of ships waiting to make berth off the coasts of North America have declined from 150 to less than 100 as of October, primarily on the East and Gulf Coasts.

Logistics managers reported declines in September and October ocean freight orders, signaling lower consumer demand. Empty containers have begun to increase as a result, causing container prices to drop. Container prices fell for 38 consecutive weeks, averaging $2,591.41 as of November 17, 2022, 72% below the same week in 2021 and a 9% week-over-week decrease per the Drewery World Container Index.

Container prices have fallen over 75% since reaching the peak average of $10,377 in September 2021 but are still 82% higher compared to pre-pandemic 2019 prices.

Despite the recent decline in ocean freight orders and container prices, ship owners have increased container ship orders. As of October 2022, the orderbook for container ships reached a record 7.1 million twenty-foot equivalent unit ("TEU"); the previous record was 6.6 million TEUs in 2008. However, it is unclear whether the ocean freight market can absorb these new ships as freight is falling as consumer demand and spending declines.

Falling consumer demand and spending is expected to continue into 2023, negatively impacting the ocean freight market. Drewry, an independent maritime research company, anticipates market earnings before interest and taxes to decline over 64% from 2022 levels but will remain above pre-pandemic earnings. Supply is expected to outpace demand, which has caused ocean carriers to resort to blank (cancelled) sailings in recent weeks in order to soften the decline. Fleet capacity management will also help carrier performance in 2023 by selling older ships for demolition, delaying the deliveries of new ships, and idling vessels.

# 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.

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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’ 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:**

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- 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 Wholesale & Industrial Solutions has liquidated and been involved in the asset disposition of many companies in the construction and transportation industry.

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