

# Trucking in TROUBLE



# *Are leasing and finance companies avoiding opportunities as well as risks?*

**By Susan L. Hodges**

**W**hen Jevic Transportation, Inc. announced its closure on May 19 after 27 years of business, CEO David Gorman cited the soaring cost of fuel, rising insurance

costs and fluctuating freight levels as culprits. In a letter to employees, Jevic's management said it had sought financing and other alternatives that would have allowed the company to continue. But apparently no one stepped forward with a solution broad enough to keep the company's trucks on the road, because Jevic filed for Chapter 11 bankruptcy the following day. With 1500 employees and 1,000 trucks, Jevic was a mid-size, for-hire carrier. Its closure adds to the 935 mid-size road carriers that closed their doors in the first quarter of 2008, and an as-yet unknown number that packed it in between April and July. According to a study by Avondale Partners LLC, a Nashville-based independent investment banking firm, the number of bankruptcies among trucking fleets with more than five units has reached its highest level since the 2001 recession, and is more than double the rate reported in the first quarter of 2007, during which 385 carriers ceased doing business.

Trucks are involved in the delivery of roughly 77 percent of goods purchased by U.S. consumers. The Federal Highway Administration puts the value of goods moved by truck between Mexico, the U.S. and Canada in 2006 at \$534 billion, while goods moved by rail during the same period were valued at \$129 billion.

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## Falling at Break-Neck Speed

Huge as it is, though, the trucking sector of transportation is now caught in a downward spiral, and experts in the sector say the decline is less a gentle creep down the mountain than a screaming free-fall to which the brakes may not be applied anytime soon. Observes Lee Wittmann, president of TQM Co., a transportation marketing service and used-truck seller in Banner Elk, North Carolina, “I’ve been in the business 45 years, and we go through this all the time—but not like this.”

Apparently not. According to the

American Trucking Association, acquisitions of new trucks were down by 38 percent for February, 2008, compared to the same month in 2007—and projections called for that rate to remain steady or drop even further for the first half of this year.

Many firms are returning their trucks at lease end, and others are calling to learn what would happen if they lengthened their trade cycle from three years to six. “What they’re weighing is the extra cost of maintenance as opposed to future residual value,” says Wittmann.

Another development in the ailing market: truck manufacturers are thinking about accepting trades. “For

years and years they refused to do this, saying it was the dealers’ responsibility,” says Wittmann. But at least one truck maker has chosen to do it in an attempt to bolster new-truck acquisitions, and Wittmann says the strategy is back-firing. “They’re so swamped with used trucks that they’re looking for ways to get rid of them.”

Not surprisingly, most equipment leasing and finance firms aren’t rushing to help financially strapped road carriers or truck manufacturers. As skyrocketing fuel bills eat into budgets dedicated to equipment maintenance, replacement and payments, delinquencies are climbing and credits are on the skid. “Everyone with subjective dollars to lend is turning their attention to other sectors that will provide more return with less risk,” says Brian DeRusha, director of asset management at AIG Commercial Equipment Finance, Inc., in Plano, Texas. Since the aim of banks and leasing companies is to generate a return on equity and capital, “They won’t concentrate on trying to lift up an industry that is suffering...because they have their own longevity to worry about.”

## Buy Low, Sell High?

Such logic is hard to dispute, but begs the question: if trucking is an integral part of the U.S. economy, do leasing and finance firms at least have an obligation to explore creative approaches that could help? Maybe not, but DeRusha believes opportunities exist for equipment leasing and finance companies to help trucking firms while helping themselves. “As crazy as it sounds, this is the absolute perfect time for companies to start investing in trucking,” he says. Why? “Because deals written in an adverse market should mature in a positive market,” he explains, “and leasing and finance firms will reap the benefits.”

But most credit departments don’t

see it that way. To credit experts, putting money into new deals while they're writing off old deals in the same industry is the definition of insanity. But DeRusha agrees that a similar argument could now be made in housing: it's a buyer's market, so now is the time to step in. Even so, "It takes a lot of courage to convince them that this is a good time to invest," says DeRusha.

AIG Commercial Equipment Finance hasn't left the truck market, lending instead to what DeRusha calls "the right transactions." These include deals for trucks to be shipped to Canada and Eastern Europe. "You may want to look at availability in international markets," he advises other ELFA members with a stake in trucking.

Chris Condon, president of Dover Management Group, Inc., in Dover, Massachusetts, agrees, particularly when it comes to used trucks. Many

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U.S. trucking firms are holding on to their vehicles as long as possible to avoid purchasing new models that comply with EPA requirements for lower emissions. This is because new units, with sophisticated technology that performs multiple tasks to produce cleaner exhaust, cost \$5,000 to \$10,000 more than units made before 2008. And when used trucks do come off market, vast quantities are being acquired by overseas buyers.

## After-Market Management

“Equipment isn’t being produced locally in developing economies in Europe, and with the falling [U.S.] dollar, our used equipment is very attractive,” explains Condon. According to a report from the U.S. Department of Commerce, Russia’s demand for used U.S. trucks has grown annually since 2000, and is expected to keep growing “into the foreseeable future” as that nation’s economy continues to expand and its own manufacturers fail to produce high-quality vehicles. One U.S. Department of Commerce spokesman estimated Russian acquisitions of used U.S. trucks at 2,500 units per month. Observes Condon, “Europe has propped up values for us on used trucks. Otherwise, they’d be in the tank.”

But TQM Co.’s Wittmann says one reason residual truck values are low in the U.S. is that some leasing and finance companies are mishandling the after-market. “I’ve seen companies get a [returned truck] worth \$50,000 and try to sell it for \$100,000,” he says. Then, after six months without a bite, these firms apparently become impatient and sell the unit for \$20,000. “It’s ridiculous,” says Wittmann, whose former business is liquidating portfolios for leasing companies. “At some point the leasing company decides it needs more dollars in the till and gets rid of the truck immediately,” and almost always at a

## EPA Reaches Out to Lenders, Fleets

The U.S. EPA has come up with a way to help trucking firms obtain financing: it has launched a web site that connects carriers belonging to its SmartWay Transport Partnership with private lenders who compete for loans to purchase fuel-saving trucks and technologies.

The SmartWay Transport Partnership is a voluntary alliance between freight industry sectors and the EPA that establishes incentives for fuel efficiency improvements and greenhouse gas emissions reductions. By 2012, SmartWay hopes to remove between 33 million and 66 million metric tons of carbon dioxide (CO2) emissions and up to 200,000 tons of nitrogen oxide (NOx) emissions per year. At the same time, the initiative will save of up to 150 million barrels of oil annually.

The SmartWay Finance Center web site ([www.smartwayfinancecenter.com](http://www.smartwayfinancecenter.com)) allows members to submit an application that lenders then respond to in an effort to win the business. Loans are provided for equipment from SmartWay vendors that range from SmartWay-certified tractors and trailers to tires and idle-reduction systems.

Since the web site was announced in mid-March, trucking firms have submitted more than 300 applications for loans and leases of environmentally friendly equipment, with about 75 percent resulting in offers from lenders. For information about registering as a lender, visit <http://www.smartwayfinancecenter.com/lenders.cfm>.



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many of these companies [have left the market],” he notes, naming ORIX, Merrill Lynch, and most recently, CIT.

Unless other leasing and finance firms come forward with innovative approaches, Forbes thinks trucking companies may have to turn to the hedge-fund market. “But they’ll see junior mezzanine debt prices,” he warns. “It’s just a matter of how much they want to pay [for money], and how long they can take the pain.”

There lies the rub, because trucking companies can’t take much more pain. With the price of diesel fuel hovering around \$4.70 a gallon, only the largest carriers are able to pass through part of the expense to their shippers. Mid-size and smaller fleets are often at the mercy of brokers who compete on price.

### **Captive Capacity**

Still committed to financing the trucking industry are captives such as Volvo Financial Services North America (VFSNA). In a creative move in April, Mack Financial Services and Mack Financial of Canada, both divisions of VFSNA, announced six fourth-quarter winners of free payments. Each winner had financed a new Mack highway truck with Mack Financial Services, and was thus entered into a drawing for free payments. Two winners received free payments for one year, while two others received free payments for six months, and the final two, free payments for three months. In 2007, 24 customers won three or more free payments each.

“Captives tend to have a more consistent approach to lending and leasing throughout a business cycle,” says Martin Weissburg, president and CEO of VFSNA. Despite what Weissburg called “some industry softness,” financial institutions that are serious about the transportation industry “remain interested in providing capital to well established transportation companies

significant loss.

Chris Condon says that if used-truck values were higher, it could make sense to require additional collateral for financing a new truck. “This happens with marginal credits all the time,” he says. “We’d lease you a truck, but you’d have to pledge two of your existing trucks as collateral.” Since used-truck values are on the fence, another option could be to

require trucking customers to put up other collateral with a liquid market, such as trailers or maintenance machinery.

Tom Forbes, an industry consultant in Alpharetta, Georgia, believes specialty finance companies could profit by cementing transactions now with cash-strapped trucking firms that could be paid later at a premium when the market returns. “But so

with strong credit profiles,” he added. Yet, strong credit profiles are getting harder to find as owner-operators and fleet managers take longer to pay their bills, just to keep their trucks on the road.

Ken Kremar, principal of the Industry Practices Group at Global Insight USA, Brooklyn, New York, is collaborating with Global Insight's Marc Lauritano in Washington, D.C. to produce a study on trucks and trailers for the Equipment Leasing & Finance Foundation. To be completed in mid-August, the study will present a micro-economic picture of the truck and trailer market, market forecasts and interviews with several members of the trucking industry.

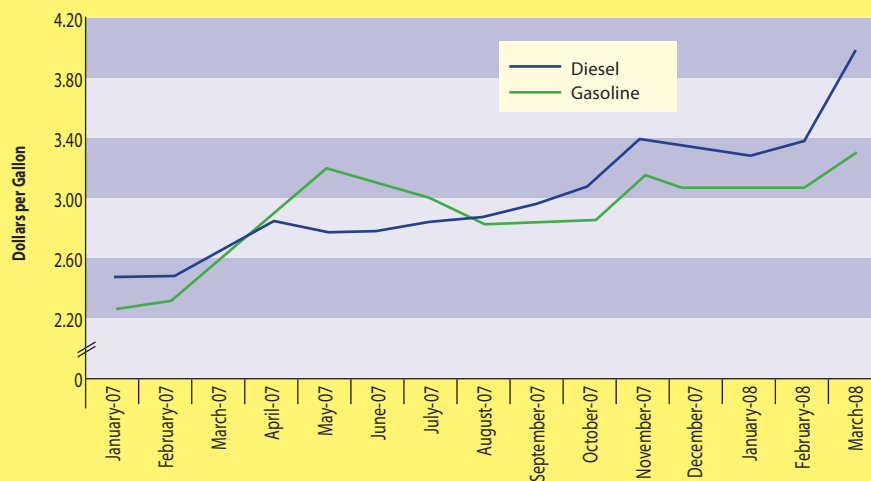
Working on the demand side of the study, Kremar says a cloud will continue to hang over the U.S. economy into 2009. But he foresees an uptick in truck acquisitions, at least, as some carriers invest in '09 models to avoid acquiring 2010 models with still more emissions equipment. “Nobody wants to be the first to wrestle with the new technology,” he says. Kremar further expects another decrease in truck financing in 2010, but looks for demand to stabilize soon afterward.

In the meantime, he thinks a creative approach to financing may be the best approach for trucking and the equipment finance industry. “And maybe some companies will jump on it,” he says. After all, trucking may slip and slide, and even plunge from the cliff. But it won't go away, because, in the words of Brian DeRusha, “People need transportation. It's just a reality now of paying the price of fuel to put food on the table.” Let's see who delivers the bacon. ■

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## Monthly Retail Sales Price of Diesel and Gasoline, Jan. 07-Mar. 08



Graph courtesy of U.S. Department of Energy, Energy Efficiency and Renewable Energy

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