Is the Freight Slowdown Signaling Recession?

Fewer goods being shipped could indicate a recession on the horizon.

September 24, 2019 8 min read

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Over the past year, several analysts and experts in economic trends have flashed warning signs about the U.S. economy. Not waving a red flag of concern would be a challenge in today's somewhat chaotic environment, with discussions of trade wars, tariffs and an impending downturn in economic activity across the board. Although it is impossible to predict when the next recession may strike, freight — one of the broadest indicators of economic movement — has been sending mixed signals throughout most of 2019.

Many believe that after the most recent data published on industry trends, the downturn in freight over the last six months shows a clear sign of a recession on the horizon.

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The signals of a freight recession.

Several driving forces point to a recession in freight, impacting nearly all parties involved in the process. From freight brokers to truckers, shippers and carriers, a slowdown in the freight industry has far-reaching implications for many. However, not all signals of a downturn warrant fear. Two main aspects of the freight environment foreshadow a recession

in freight: a decrease in rates and growth in stockpiles.

A decrease in freight rates

Compared to the impressive numbers in the summer of 2018, this year has shown a clear decline in freight rates. According to recent data, spot load posts, van load-to-truck and flatbed load-to-truck rates are all down compared to August 2018. A reduction in freight rates is a response to supply and demand. As capacity grows tighter, meaning there is a small gap between carriers and shippers, freight rates tend to tick up. When the opposite takes place, rates drop, often significantly. The year-over-year decline in freight rates can be a signal of a longer-term economic slowdown.

A growth in stockpiles

In addition to declining freight rates, an increase in stockpiles across manufacturers and retailers is a sign of a recession in the industry. From nearly all sources, including DAT, ACT research and the Cass Freight Index, volumes of loads in freight have experienced decreasing numbers for a significant portion of 2019. Businesses, particularly those in industrial categories, not necessarily consumer-focused merchants, rushed to get inventory stockpiled before the implementation of tariffs threatened last year. Now, those stockpiles are not moving nearly as fast as some might hope, and so there is less of a need for freight services. These indicators signal a downturn in the freight industry as much if not more than falling freight rates.

Turmoil in trucking, rail and air freight industries.

The whole of the freight industry, including trucking, rail, and airfreight companies large and small comprise more than $800 billion in economic contribution. Although 2018 was a

fast and furious year for most freight companies, alongside successful freight brokers and independent carriers, 2019 has been a different story altogether. As freight rates dropped with loosened capacity, freight businesses felt the pinch and responded accordingly.

Big players cut growth outlooks.

Major contributors to the freight industry have recently reduced their projections for growth given the decline in freight trends. For instance, J.B. Hunt, Knight-Swift and Schneider — all large companies in the freight industry — slashed earnings outlooks for the remainder of 2019. Part of these declines can be related to the fact that a decline in spot market loads fell 37 percent from July 2018 to July 2019, highlighting a reduction in the need for moving goods among manufacturers and retailers. As significant players cut growth outlooks, they may also be inclined to cut jobs, leaving truckers and other operational staff seeking out new opportunities.

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Small players forced to go bankrupt.

While larger companies in the freight business have experienced adverse outcomes due to recession signals firing in the last few months, small freight businesses have felt the pressure to a greater extent. Small companies in freight, including owner-operator truckers, are more prone to work on an as-needed basis through one-off contractors. During the height of the freight boom in 2018, tight capacity meant nearly everyone was being called to the table for work. Now, as freight needs decline, smaller companies are hurt more, with some filing bankruptcy or closing up shop altogether.

Larger freight operations may have more access to capital to keep the doors open during a recession; small and independent businesses may not have the same luxury.

U.S.-China trade war intensifies the situation.

Experts suggest that the increase in freight volume that spread throughout 2018 was the result of fear for the future economic state. Talk of trade wars was ever-present, but the implementation of tariffs on both Mexico and China had yet to come to fruition. To get ahead of the potential downturn that a newly imposed tariff would cause, freight companies rushed to meet the demands of business around the world. Stockpiling inventory, from consumer goods to industrial and raw materials, was the norm last year.

Now, however, the freight world has experienced a significant changing of the tides. Trade war talks have become a reality, with new tariffs imposed as recent as the beginning of September. With an increased cost of doing business due to tariffs, manufacturers and retailers are forced to slow down procuring inventory to then ship to businesses and consumers, or they must increase prices to ensure financial stability into the future. These changes have a drastic impact on shipping by truck, rail and air. There is less of a need for freight services as trade war tactics continue, creating more of a slow down in the industry overall.

The Cass Freight Index and what it means for the economy.

The Cass Freight Index has received quite a bit of attention over the course of 2019, and it should, given its purpose. The Index, published by Cass Information Systems, is a measurement of monthly aggregate deliveries of freight within the United

States. Each month, data is published on more than 1,200 divisions of unique companies and manufacturers, providing a picture of freight volumes and historical trends in the industry.

In December 2018, the Cass Shipments Index was negative for the first time in two years, but this was quickly brushed off as a one-time decline. However, since that time, the Index has shown steady decreases each month, compared to the previous year's data. When these figures are trending downward for several months, analysts share that an economic contraction may be on the way. When goods aren't being shipped as often or with as much volume as the Index suggests, the freight industry is taking a turn. In many instances, the economy follows suit, albeit not always immediately or to the same extent.

When freight is in a recession, does the economy follow?

Going back to the most recent recession, data shows that freight slow down can be an early indicator of a broader decline in economic activity. Freight experienced a downturn in 2006, nearly two years before the Great Recession began in January 2008. However, the freight industry falls into recessionary levels twice as often as the economy at large, and declines in freight volume and rates do not always signal a recession for the masses.

The Shipment Index vs. GDP

A critical aspect of a recession that is necessary to note is the reality that the signals showing a decline in freight movement do not necessarily mean a recession is looming. For the first quarter of 2019, GDP, a leading indicator of economic activity, was up more than three percent. In the

second quarter, positive growth continued, but at a slower rate of 1.8 percent. Trends in GDP, unlike the shipping index, include several facets of the economy, such as wages, employment and consumer spending. Each has continued to post relatively strong gains over the last several quarters, but analysts suggest, based partially on the slump in freight trends, that this growth may soon come to an end.

Should these forces behind economic health and stability continue to shrink in the coming months, a recession is likely to follow closely. Other broad warning signs have also appeared in recent months, including an inverted yield curve which is a telling sign of recessionary trends. Furthermore, economic growth and contraction are cyclical, historically moving in eight to ten year periods. As an economy, the United States is past due for a downturn by more than one year.

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Fewer goods are being shipped. What does it mean?

Overall, a recession in freight due to lower shipping volumes and decreased rates does not mean indefinitely that an economic slowdown is taking place. However, fewer goods being shipped can be a clear indicator that a recessionary environment is on the cusp. From an industrial standpoint, declining shipments can be connected to lower housing starts, increased costs of doing business due to tariffs, and lower business investments in economic forces like increased infrastructure. On the consumer side of the line, fewer goods being shipped boils down to decreases in consumer spending – yet another telling sign of an economic downturn. All in all, the signals coming from the freight sector highlight what is on the horizon for the broad economy at some point soon.

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