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SMARTER PERSPECTIVE: CHASSIS INDUSTRY

Intermodal Chassis Market Demonstrates Pandemic Period Resilience

By Elbert Choi and Derek Brennan

In this article we take a look at the impact of diminished import/export volumes on the chassis segment of the intermodal industry, how providers and end-users have responded during the current crisis, and the likely path forward for industry recovery over the balance of the last two quarters of this year and into 2021.

Overview

On a global basis, 95% of all manufactured goods are at one point transported in a container. The intermodal industry connects a number of freight stakeholders, including third-party logistics providers, motor carriers, railroads, ocean carriers and container ports. According to the Intermodal Association of North America (IANA), annually, the $40 billion North American intermodal market, alone, moves 34.5 million domestic and international containers of consumer, industrial bulk, agricultural and other goods via a fleet of more than 700,000 chassis.

Chassis are the literal backbone of intermodal road transport, as they provide the framework on which shipping containers rest during their travels between intermodal terminals and shipping facilities. Owned by leasing companies, motor carriers, railroads, shippers and some steamship lines, chassis come in a variety of sizes and configurations, each designed to accommodate the size and weight of specific ocean/marine, domestic and specialty containers.

Durable and reliable, container chassis have an extensive life span. In fact, the average age of chassis in use within North America today is estimated at approximately 18 years, with the majority expected to provide a total useful service life of between 20-25 years or longer. Because a chassis is essentially a frame with suspension and axle systems, wheels and tires, brakes, and a lighting/electrical system, fleet upkeep for conventional and pool providers is relatively simple. Other than visible wear, new, used and rebuilt equipment often look much the same at a glance. Updated features such as LED lights replacing traditional bulbs, as well as upgraded tires with automatic tire inflation, ABS, weight sensors and GPS tracking systems, are often the key differentiators. While these enhancements clearly add to operational safety and efficiency, chassis at both the beginning and end of their useful lives serve a valuable role and can deliver excellent returns when properly managed and maintained.

To be certain, the real innovation taking place in the chassis market today is software-driven. Knowing precisely where the fleet is and how to pick it up efficiently, is becoming a critical aspect of overall fleet management as it empowers quicker action at lower cost during everyday business operations as well as in valuation/liquidation scenarios. We have seen increased receptivity among lenders to loan facilities associated with aging chassis fleets, particularly as they have observed key players investing significantly in their respective aging fleets. Two cases in point: 1) DCLI's recent investment of over $80 million in upgrading its chassis pools across the country with an emphasis on converting to radial tires and; 2) American Intermodal's (AIM) effort to enable all of its chassis with the latest GPS positioning technology.

Software-driven GPS innovation is being deployed to track and deliver real-time data, adding greater efficiency for managing new and retrofitted chassis fleet assets across their lengthy lifespan.

Source Image: CloudHawk®

Investments such as these make sense when considering that their lengthy life expectancy enables chassis owners to effectively amortize their investment over a period of many years, during which their fleets typically deliver a consistently healthy cash flow and maintain strong, tangible hard asset values. When not in use, many chassis are stored offsite and can be utilized as needed to cover peak holiday demand. Chassis are typically fully rebuilt to modern standards at end of their useful life, or when minor damage has occurred. Hilco values these renewed assets according to the rebuild date rather than their true historical age, and our accuracy in valuing and effectiveness in monetizing these unique assets is unsurpassed in the industry. In cases where disposition of either an entire fleet or large quantities of chassis assets are involved, Hilco leverages a "hybrid in-place" model to ensure maximum residual cash flows for current leases/contracts, while achieving strong market values for idle equipment via timely marketing and sale.

Historical Perspective

Steamship lines, themselves, had historically been the primary owners of container chassis since Intermodal's inception. The economic ramifications of the 2008 financial crisis changed that, however, leading to a renewed focus on core shipping services and divestiture of chassis assets by the lines, who no longer wanted responsibility for the associated investment, storage, repair, and logistic costs. With an annual expense of about $1,000 per chassis, these costs were quite significant based on the fleet size of most shipping lines. Over the past decade, this industry-changing shift has given rise to the predominant chassis lease and chassis pool system now in place in the U.S.

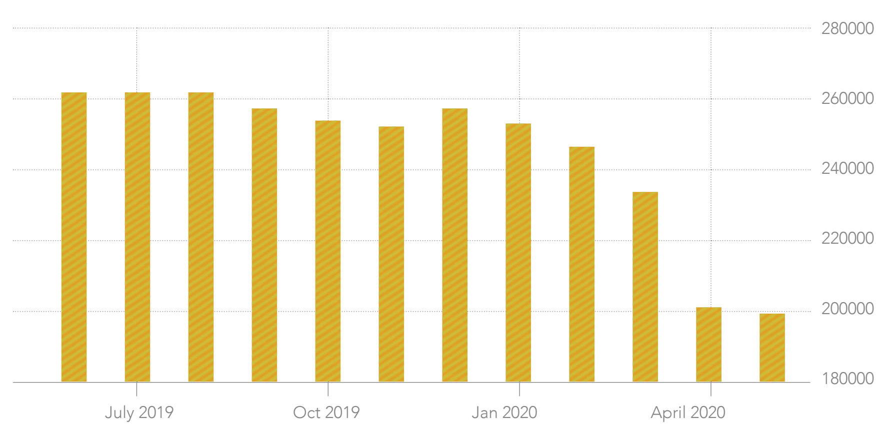
After faltering during 2016 in conjunction with the bankruptcy of shipping giant Hanjin - which threw ports and retailers around the world into turmoil as massive container ships were marooned and merchants worried whether goods would ever reach their shelves – the intermodal and chassis markets stood the course in 2017 and achieved record numbers in 2018, with inbound international and domestic container volumes rising by 6.5% and 5.5% respectively.

2019 was a year of modest growth in container trucking, with U.S. container imports increasing only 1% over 2018 levels and chassis volume falling slightly. Most chassis providers chose to refurbish existing assets rather than purchase new equipment in 2019, in large part because new chassis are primarily manufactured and sold by two providers located in China and would have been subject to the 25% tariffs imposed by the U.S. during the trade standoff at the time. Recognizing the pitfalls of such susceptibility to its business model, China's CIE Manufacturing (formerly CIMC), the world's largest producer of new chassis, relocated its production facility in Q1 2020 to the U.S. from China. Also, of note in 2019, DCLI purchased part of the domestic pool chassis business from TRAC International (TRAC), further solidifying its ability to provide the 53-foot chassis utilized exclusively in the U.S. Puerto Rico and Caribbean, per the Merchant Marine Act of 1920, which regulates commerce in U.S. waters and ports.

Current Market

As 2020 began and a U.S./China trade deal was signed, chassis providers were hopeful for a solid start to the year, but COVID-19 threatened to prevent that. While the domestic pool helped support the market early on, the onset of COVID 19 has certainly presented the industry with numerous challenges. To their credit, TRACS, DCLI, FLEXIVAN and other key industry players took proactive steps from the onset of the crisis to ensure that field maintenance and repair teams remained operational at rail, marine and other intermodal locations and that road service was readily available for any chassis equipment incidents that might occur during the unusual operating conditions.

2020 Import Volumes

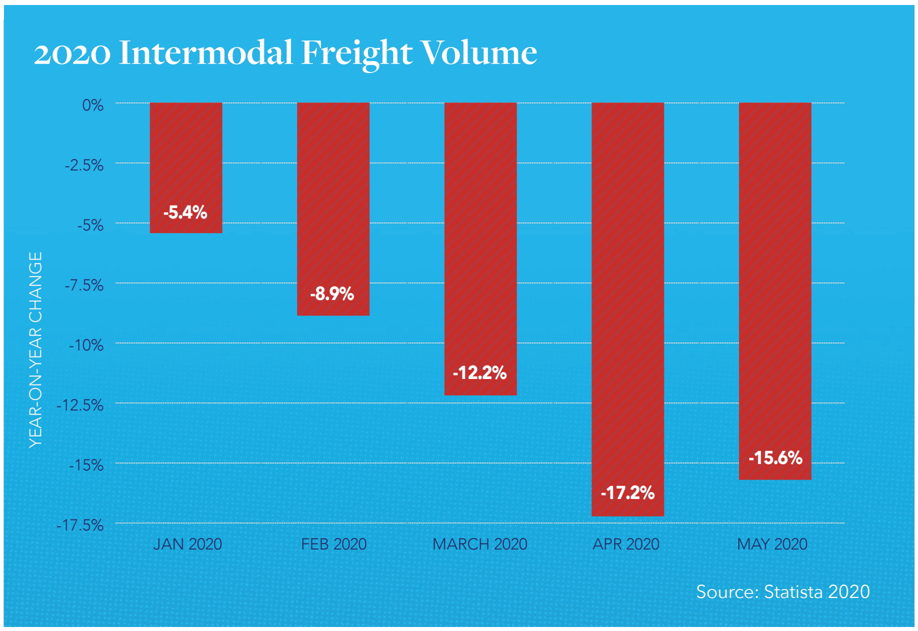


Import and export volumes are a key driver of intermodal volume and chassis use. Imports to the United States fell by USD 1.8 billion from the previous month to USD 199.1 billion in May 2020, the lowest level since July 2010, as the coronavirus pandemic led to a fall in domestic demand.

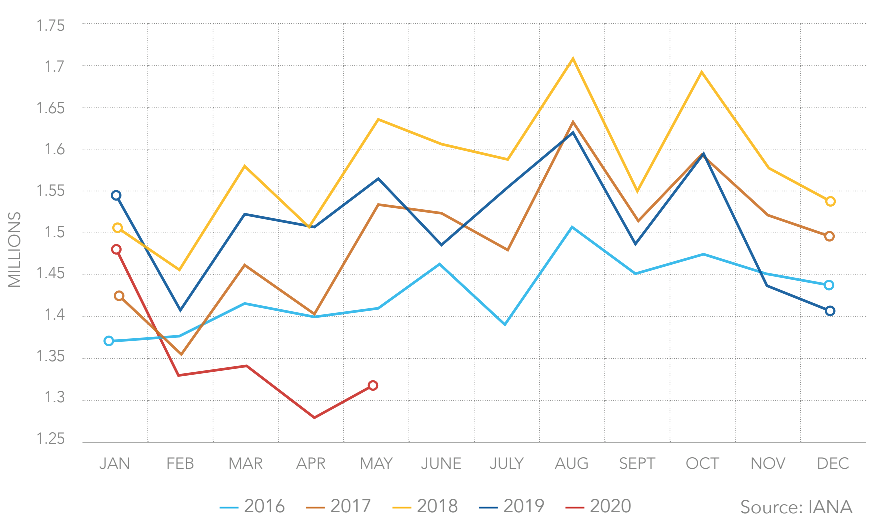
Source: TradingEconomics.com | U.S. Census Bureau

From a volume and operational standpoint, the decline in traffic based on the pandemic has been less significant than we had anticipated. While March through early May chassis market performance was down and shipping alliances, as reported by Container News in June, have announced some third quarter blank sails despite evidence that the U.S. economy is beginning to see demand recover- one major provider has informed Hilco that their last week of May was in line with the same week in 2019.

Given chassis' infrastructure-orientation, customers want and need to make sure they have chassis when and where they need them as markets recover. As a result, pool participants are continuing to make their monthly payments to ensure priority access, as are contract holders, who are keeping equipment on-hand so it is available as needed. We are hearing from providers that even customers who are having difficulty making payments have, for the most part, asked for some form of revised terms rather than terminating their relationship and their future access to those chassis assets altogether. We believe these actions strongly suggest that that those across the industry expect a return to more normalized volume in the months ahead. It bears noting that for some, such as UPS and USPS who have seen strong demand and associated volumes continuously through this period, maintaining those contracts has essentially been business as usual.



2016-2020 Monthly Volume Totals



As reported on June 22nd by Logistics Management, based on data provided by the Intermodal Association of North America, intermodal freight volume for the month of May 2020 was down 15.6% at 1,320,963 units as compared to the same month in 2019. This does, however, represent somewhat of a rebound from the April 2020 drop of 17.2%. On a year-to-date basis through May, total intermodal volume of 6,779,261 is down 10.2% annually.

Outlook

Based upon the above referenced feedback from the market, as well as our own and other market intelligence, Hilco expects chassis utilization to ramp-up in conjunction with consumer spending levels and the associated global and domestic movement of goods in Q3 and Q4. We see this likely resulting in performance for 2020 as a whole just slightly below 2019 levels. Since forecast volumes for 2020 were relatively flat, actual results may be in line with expectations, setting a pace for modest growth moving into 2021.

We expect strong interest in acquiring quality used chassis moving past the peak pandemic period. Much of this will likely be driven by a desire to add capacity to chassis pools in order to service existing customers while also being able to capture new, large accounts by guaranteeing volume access. Because chassis are rarely available on the used marketplace in bulk quantities, as growth returns, we see the potential for increased large-scale purchases of chassis via competitive acquisitions as well as a renewed interest in made-to-order, new chassis purchases directly from the manufacturers.

We have been working closely with leading providers and communicating regularly with numerous stakeholders across the industry throughout the current crisis. For ABLs with questions or concerns regarding specific exposure within their portfolio at this time, we are here to help and encourage you to reach out to us for any perspective and guidance pertaining to chassis fleet valuation considerations, acquisition, disposition and other matters.

Hilco Global is one of the world's largest and most diversified business asset appraisers, valuation advisors, and monetization experts.

A trusted resource to companies, their lenders and professional services advisors, Hilco Valuation Services provides value opinions across virtually every asset category. Our extensive experience in valuing and monetizing chassis assets is unsurpassed in the industry, with our valuation and M&E teams working closely together to deliver maximum accuracy and efficiency on behalf of our clients. With a dedicated team focusing on truck, trailer and chassis fleets, we have performed valuations on well over 1 million assets across transportation and logistics, covering $2 billion in deployed capital. Hilco's track record in the liquidation of fleet assets for maximum valuation based on its understanding of realistic value and real challenges to an actual orderly liquidation process, is highly regarded across the industry. Hilco Valuation Services has the ability to affirm asset values via proprietary market data and direct worldwide asset disposition and acquisition experiences. Access to this real-time information, in contrast with the aged data relied upon by others, ensures our clients more reliable valuations, which is crucial when financial and strategic decisions are being made.

DEREK BRENNAN, CEA IS SENIOR VICE PRESIDENT, FINANCIAL REPORTING AT HILCO VALUATION SERVICES

Derek joined Hilco in 2003 and has been in the auction, liquidation, and appraisal industry since 1996. Throughout his career, Derek has served as a valued consultant and advisor to financial institutions on hundreds of asset-based loan and recovery assignments. He is a recognized leader within the industry with extensive experience in transportation/logistics and expertise in specialty areas including: computers, construction, corrugating equipment, electronics, food and chemical processing, foundry and primary metals, metal working, metal forming, metal scrap handling equipment, mining, oil drilling equipment, packaging, plastics and rubber molding, textiles and woodworking. Previously, Derek served as an appraiser at DoveBid, which was later acquired by Liquidity Services, Inc.

Derek is a Certified Equipment Appraiser (CEA) and a member of the Association of Machinery and Equipment Appraisers (AMEA). He has completed both the American Society of Appraisers (ASA) Performing Machinery and Equipment Valuations for Financial Reporting Purposes and the Uniform Standards of Professional Appraisal Practice (USPAP) courses. He received his Bachelor of Science degree in Business Management from the University of Phoenix.
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ELBERT S. CHOI, CVA IS SENIOR VICE PRESIDENT AT HILCO ENTERPRISE VALUATION SERVICES

Elbert has been with the company since early 2008. He has completed or managed hundreds of valuation engagements and related financial analyses for organizations ranging from small, closely held companies with about $1 million of revenue to very large organizations with revenues up to several billions of dollars. Elbert's work has included business and stock valuations, debt valuations, cost of capital analyses, valuations of patents, unpatented early stage technologies, trademarks, proprietary processes, illiquid investments, options, notes and restricted stock, damages calculations, purchase price allocations, and litigation support services. Clients have included hedge funds, private equity groups, commercial banks, accounting firms, BDC's, venture capital funds and a variety of other niche financial institutions. These engagements span a multitude of different industries and have been performed for a range of purposes including: asset based lending, estate and gift taxation, income taxation, buy/sell agreements, shareholder buyouts, management buyouts, leveraged buyouts, S Corporation conversions, financial reporting, collateralization, collateral monitoring, marital dissolution, dispute resolution, mergers and acquisitions, strategic planning, and others.

Prior to joining Hilco Enterprise Valuation Services, LLC, Elbert founded the Business Valuation department for a midsize public accounting firm located in Schaumburg, IL. During his tenure there, he performed valuations for the purposes of partnership dissolution, marital dissolution, estate/gift tax, estate planning, mergers and acquisitions, funding scenarios, and a variety of other purposes.

Elbert is a Certified Valuation Analyst and a member of the National Association of Certified Valuation Analysts (NACVA). In addition to undergraduate degrees in Finance and Computer Engineering, he received his MBA in Finance from DePaul University. Contact Elbert at: 847.800.4260
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