

Brother Can You Spare a Loan?

Finding capital may ultimately determine success or failure in trucking

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Substitute the words “trucking company” for “railroad” and “dime” for “loan,” and that 1932 Depression-era song popularized by Bing Crosby could be about today’s credit-starved trucking companies.

It’s been a rough year for most Americans, and for trucking companies seeking financing, it’s been even rougher as they wait for the economy to pick up steam, inventories to be reduced, and lending institutions to release their grip on desperately needed capital.

Trucking executives are accustomed to hearing bad news lately, so before going any further, let’s interrupt the doom-and-gloom with this: The recession is over, according to American Trucking Associations economist Tavio Headley, though it won’t be declared so for a while. Headley said in a recent interview that the economy has bottomed out and is slowly growing, with future growth to be muted and choppy for some time. “Trucking,” he said, “is just barely making the turn to recovery ...”

No one who saw Headley’s sobering presentation before the Arkansas Trucking Association’s annual conference earlier this year would describe him as a wild-eyed optimist, so it’s a hopeful sign that he’s using the words “trucking” and “recovery” in the same sentence. According to Headley, the industry has been dealing with a nationwide inventory glut that must be reduced before trucks can be hired to haul more newly-produced goods.

Headley said that inventory reduction is about 75 percent complete, and while boom times won’t necessarily fol-

ONCE I BUILT A RAILROAD, I MADE IT RUN,
MADE IT RACE AGAINST TIME..
ONCE I BUILT A RAILROAD; NOW IT’S DONE.
BROTHER, CAN YOU SPARE A DIME?



low, empty warehouses undoubtedly will help the industry. "It's going to be better than what it was, but what your readers have to understand is, it's not going to surge," he said. "It's going to improve, but it's not going to surge."

Headley said the outlook won't get much brighter for trucking during the next six months. There are still "way too many trucks chasing too little freight," he said. But he expects the outlook to be better in a year. Eventually, of course, the economy will gain momentum and so will the industry. "In the real long term, I'm very bullish on trucking," he said.

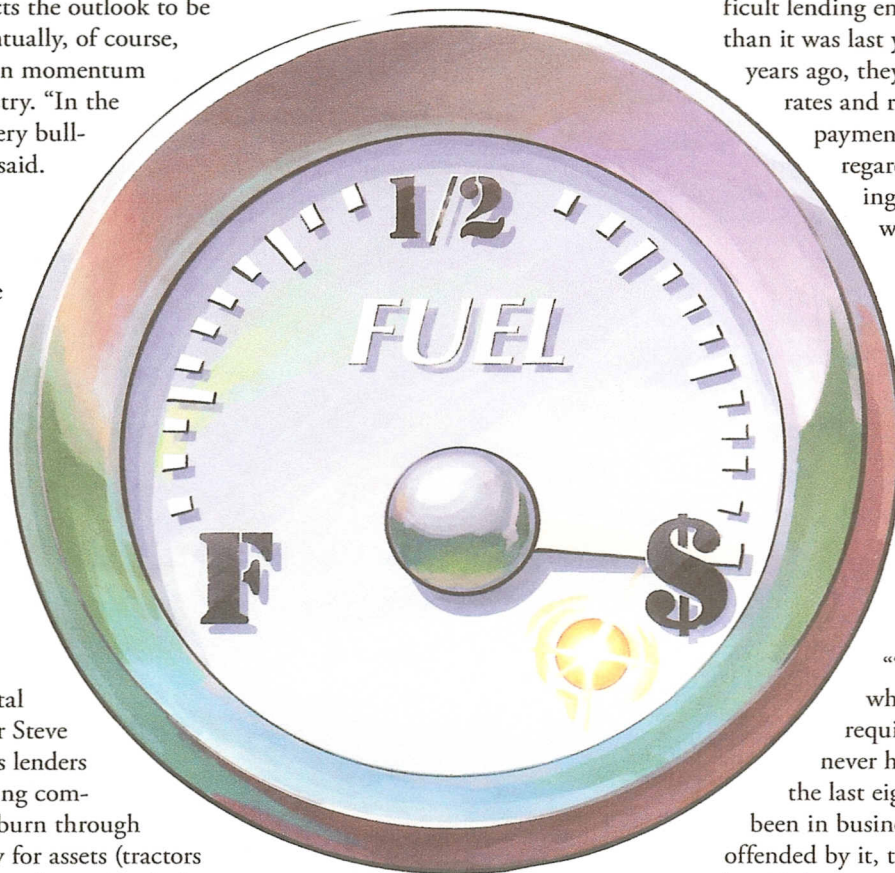
Survival tips

But to get to the long term, trucking companies must survive now, and that is easier said than done in a lending environment that doesn't see the industry as a good credit risk. According to Jim Schnoes, director of the advisory firm Transport Capital Partners, and partner Steve Dutro, in good times lenders like to loan to trucking companies because they burn through a lot of capital to pay for assets (tractors in particular) that must be replaced after only a few years, often with more borrowed capital. But in bad times, lenders are reluctant to do business with trucking companies because of the industry's thin profit margins.

Schnoes (pronounced "Schnays") and Dutro compare today's climate to the nation's anemic housing market. In 2007, home buyers could obtain low-interest loans with no down payment, and the credit market was similar for trucking. Today, some potential home buyers cannot get loans, and the same is true for weaker trucking firms. Though they might be able to limp through the next few years, they will be in trouble when they are forced to replace their aging fleets with new tractors that, because of higher emissions standards, will be more expensive than they other-

wise would have been.

Schnoes and Dutro said this is the third boom-bust cycle since 1981. During bad times, the number of available lenders falls, some never to return. In 1981, Citibank disbanded its transportation group, and the same is happening with many regional lenders today. Wausau Bank had an excellent transportation group based in Chicago that was



shut down last year after the bank was bought by Bank of America. "Bank of America obviously still lends to trucking, but you don't get the same kind of depth of knowledge from the bankers that you work with," Dutro said. "That's unfortunately been a trend for some years in banking."

So where can trucking companies get loans? According to Schnoes and Dutro, the most common methods are through vendor credits followed by banks and then securitization or factoring of receivables. According to Schnoes, vendors don't particularly like providing credit to trucking companies, but not doing so hurts themselves and their sister companies who need somebody to move their freight.

Still, like other lenders, they're more

tight-fisted than they were a couple of years ago. "I will say across the board, all credit has tightened, all covenants and credit agreements are much more difficult than they used to be, and that includes the vendor guys, which historically used to run loose when there was a little bit rosier credit market," he said.

Banks will loan money to stronger trucking companies, and while it's a difficult lending environment, it's better than it was last year. Compared to two years ago, they are charging higher rates and requiring higher down payments and better collateral regardless of where a trucking company is based or what kind of carrier it is.

(Those that specialize in automotive parts have a higher hurdle to jump than others, for obvious reasons.)

According to Dutro, companies that have been out of the credit market for several years will be surprised at the environment when they try to borrow again. "There will be truckers who get offended at being required to do things they never had to do, at least not in the last eight to 10 years they've been in business," he said. "They'll be offended by it, they'll be shocked by it, but it's because that whole credit world has changed underneath us."

Who will be favored? Stronger companies, naturally, but those that have had open, transparent relationships with their banks will have a particular advantage, according to Schnoes and Dutro. Personal relationships help a little. Meanwhile, it pays dividends to have relationships with more than one bank, though that's not always possible for smaller firms.

Desperate measures

Trucking companies sometimes must make difficult decisions to get loans. Jack Waldo, a research analyst at Stephens Inc. who writes recommendations for trucking stocks, said one method is engaging in a sale-leaseback

transaction, usually involving selling real estate and then leasing it from the buyer.

That means renting what you used to own, and Waldo said that while some companies consider that a better use of their capital, "At this point, many people are doing that in a move of desperation."

Desperation is a reality for some trucking companies, and there is no more desperate time than when a lending institution forecloses on their most important assets – tractors and trailers. Thankfully, banks are reluctant to do that now because they can't do anything with the assets. Not only has the domestic market for used trucks dried up, but so have overseas markets where ready buyers were available a few years ago. "A banker's worst day is the day he (forecloses) and the guy throws the keys across the desk," said Schnoes, a former banker.

Another avenue for obtaining capital is factoring, in which outside financing companies pay the invoice due to a trucking company, minus a fee, and then bill the shipper. The practice has a repu-

tation in the trucking industry as being tainted with desperation, but Schnoes and Dutro say it's a stable environment in which to do business these days.

John Downing, owner of Freight Capital, the exclusive factoring partner of the American Trucking Associations, defends it as being similar to a low-

"TRUCKING IS JUST BARELY MAKING THE TURN TO RECOVERY."

—TAVID HEADLEY
ECONOMIST, AMERICAN TRUCKING ASSOCIATIONS

fee credit card that is much easier for trucking companies to establish than a bank line of credit. According to Downing, Freight Capital practices "nonrecourse factoring," meaning it assures that the trucking company gets paid very quickly for a small fee and then assumes the risk that the shipper might never pay. "When we buy an invoice, we're buying that invoice," he said. "We're taking it on, and if a carrier's customer ends up filing bankruptcy for whatever

the reason, then we take all the risk so that they don't have to."

As the economy improves and the trucking industry becomes more profitable, credit standards will loosen. And as always happens, companies that survive the bust will be well positioned for the boom. ATA's Headley said that fewer than expected trucking companies have gone out of business. But more will undoubtedly follow.

When the economy picks up steam, the law of supply and demand that has been the enemy of good trucking companies will become their friend.

Fewer trucks available to haul freight will equate to higher rates. Despite all the bad news, Schnoes and Dutro expect things to be better in a year. Waldo said Stephens is selectively overweight on certain trucking stocks. And Headley points out that as bad as things are, it wasn't long ago that they were much worse. "There are bluer skies ahead in general now," he said. "A year ago, things were really bad. We were dropping off a cliff. We're not doing that anymore."

