2023 US TRANSPORTATION MARKET OUTLOOK

Helping you come through for your clients.

A ROUGH RIDE BACK TO NORMAL

As a leading indicator, the Transportation sector is generally considered a “canary in the coalmine” of the greater US economy. When the economy is expanding, freight carriers, less than truckload freight shipping (LTL), and other carriers are often the first to reflect that growth, as demand for their services ramp up. On the flipside, Transportation is also often the first place where slowdowns appear, as manufacturers and other shippers see sales dropping off and have less of a need for supply chain services.

This reality broadly explains what is happening in Transportation circa 2023.

Following an explosion in new demand in the wake of the 2020 COVID-19 pandemic, the Transportation sector has seen a significant number of challenges for the better part of the last 12-18 months. This is partially due to the sheer size of the demand spike which rocked the supply chain a few years ago and eventually led back to normal trends.

“If you look back on what happened during 2020, there was an all-time historical high in demand in the number of new entrants that were granted their trucking authority and entered the market,” says Mark Gallagher, Vice President of National Transportation at Risk Placement Services (RPS). “What has changed since that time is, certainly, we’ve seen things go the other way where the number of truck lines and transportation clients exiting the marketplace has exceeded the number of new entrants over the last couple years.”

In fact, many of the new industry players that jumped in after 2020 were the first to exit the marketplace as well, Gallagher adds.

Consumer demand following the pandemic was at an all-time high, as stimulus packages from the US federal government boosted buying power, and the result was a broad increase in the purchase of goods across the country. That time ushered in a change in the way we lived, worked and shopped, and the infusion of spending coupled with more and more people working from home meant that delivery services for things that many would otherwise go out for were greatly needed.

Now, things are different.

Stimulus has ended. Rent and student loan payment moratoriums have expired. And the many factors that drove increased demand for Transportation services over the last several years have effectively run out. Now, with inflation on the rise, the cost of goods across the board has increased.

As a result, the transportation industry has fallen back to a more normal state and corrected itself. Those clients that were in the industry or joined because of that spike in demand and the amount of freight rate that they would get for taking those loads have generally exited the marketplace or sat idle on the sidelines. The spot markets are down, costs are still rising and freight doesn't make financial sense for many participants right now.

"I'd say, in particular for non-fleet, the challenges from 2022 have bled over to 2023," explains Lorie Podolak, Transportation Underwriter and Broker at Risk Placement Services. "Some of the largest challenges that the industry is seeing have to do with operational costs, just the cost of doing business. That's mainly being driven by fuel prices, followed by the difficulty of obtaining parts to get vehicles repaired."

The many factors that drove increased demand for Transportation services over the last several years have effectively run out.

A COSTLY BUSINESS

Commercial transportation is, quite simply, a capital-intensive industry.

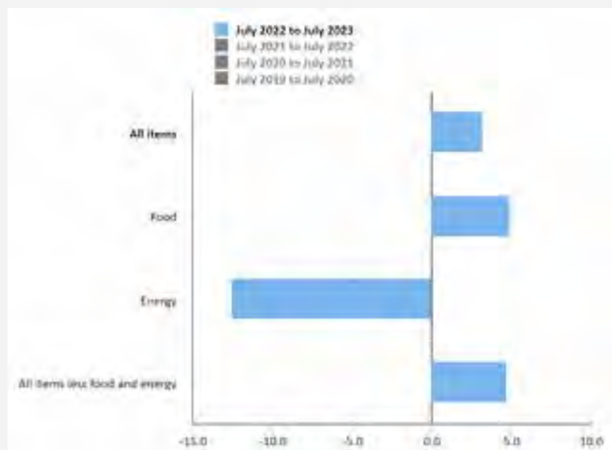
According to the American Transportation Research Institute's (ATRI) latest report on the trucking industry, total costs across the sector reached a new high in 2022 for the second year in a row. On the whole, transportation costs increased by 21.3% to $2.251 per mile last year, led by a 53% spike in fuel costs, a 15.5% increase in driver wages, and truck and trailer payments that were up 18.6% year over year. Even repair and maintenance costs were up 12% over the course of 2022.

2021—2022 ANNUAL CHANGE OF AVERAGE COSTS PER MILE

MOTOR CARRIER COSTS	PERCENTAGE CHANGE
Vehicle-based	
Fuel Costs	53.7%
Truck/Trailer Lease or Purchase Payments	18.6%
Repair & Maintenance	12.0%
Truck Insurance Premiums	2.3%
Permits & Licenses	-6.3%
Tires	9.8%
Tolls	-12.5%
Driver-based	
Driver Wages	15.5%
Driver Benefits	.05%
Total	**21.3%**

Source: American Truck Research Institute; An Analysis of the Operational Costs of Trucking 2023

12-MONTH PERCENT CHANGE FROM JULY 2022 TO JULY 2023



Source: US Bureau of Labor Statistics

"Inflation is causing all kinds of interesting problems," Gallagher says. "When you look at what Transportation clients get paid to haul loads and what they used to be able to afford with that just two or three years ago to what their margins are now, the difference is striking."

After peaking at 9.1% in June 2022 following more than two years of pandemic-induced growth, the inflation rate has settled back down to 3.7% as of August 2023, up slightly from the month prior. The Bureau of Labor Statistics reported that the consumer price index increased 3.2% from July 2022 to July 2023, compared to an increase of 8.5% during that same period a year ago.

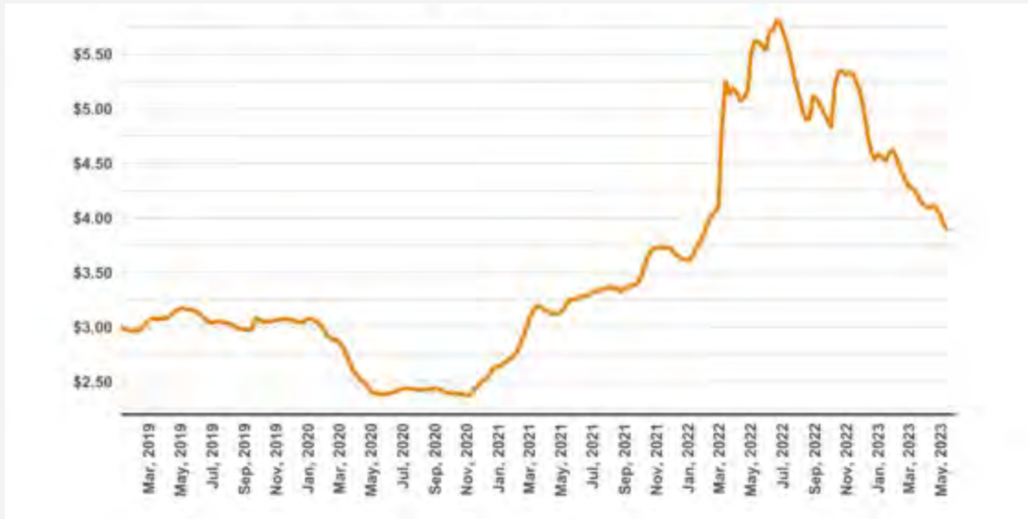
But it's not just inflation and payroll costs that are impacting costs in commercial transportation.

The Bureau of Labor Statistics reported that the consumer price index increased 3.2% from July 2022 to July 2023.

Just as has been happening in passenger cars, demand has been outstripping supply in commercial equipment, delaying deliveries of new trucks and boosting prices for vehicles, trailers and other equipment. According to trucking research firm ACT Research, new trailer orders in the US reached a record of more than 47,000 during just the month of October 2022, and remained up by more than 20% for the year even after dipping down during subsequent months. Pent-up demand paired with backlog-to-build ratios that remain as much as seven months out mean that fleets that need trucks, trailers and other equipment still need to wait or pay a premium on the used market, despite the fact that new trucks can cost in excess of $200,000 or more.

All of these costs are having a direct impact on insurance rates for commercial Transportation. What's more, diesel prices remain near all-time highs at $4.50 per gallon and are volatile on a month-to-month basis.

MONTHLY US ON-HIGHWAY DIESEL PRICES, 2019—2023



Source: American Truck Research Institute; An Analysis of the Operational Costs of Trucking 2023 Update

ATRI found that the insurance premium cost per mile increased 47% over the 10-year period between 2010 and 2020, from $0.59 per mile up to $0.87 per mile for truckers. Though 2020 provided something of a reprieve across the industry—in decreased fuel costs for truckers and reduced loss frequency for insurance carriers—since that time, and certainly this year in particular, the frequency and severity of losses have continued to climb for insurance carriers, along with loss reserves for past losses. There has also been a spike in the costs associated with Transportation-related litigation due to things like social inflation and nuclear verdicts, so insurance costs will likely continue to rise.

One bright spot, explains Mike Mitchell, Area President with RPS Charlotte, is that equipment prices—both new and used—are starting to edge down as of the end of 2023. However, that trend has a dark side: Falling freight rates.

“A big part of the cost in Transportation is supplying demand for the truck,” Mitchell says, “and that accompanies freight rates. There’s less demand right now, so that’s why freight rates are lower. Therefore, people are selling their equipment because there’s not as much freight work available as there was coming out of the pandemic when the supply chain issues were really at their peak.”

As a result, the market for new and used equipment is starting to even out, albeit at a lower level than before.

“If you look at the overall economy for truckers right now, it’s in a freight recession,” he says. “Truck drivers are really struggling to find loads that enable them to make money and be profitable. The marketplace is all about supply and demand, and there are more trucks out there than there is work.”

DRIVERS IN SHORT SUPPLY

The freight shortage is largely due to three primary factors: The lingering effects of the pandemic on global supply chains, continued backups in US ports due to staffing shortages, and an ongoing shortage of truck drivers to transport goods overland. Together, these factors are impacting the entire freight ecosystem, from shippers, to buyers, to end users around the world.

> **The driver shortage is having a particularly outsized impact on independent truckers working in the non-fleet segment of the market.**

The American Trucking Association has estimated that the industry was short as many as 80,000 drivers as of 2021. Although the pandemic years helped alleviate that shortage somewhat—bringing ACT Research's Driver Availability Index to 44 in January 2022, indicating a near balance in driver supply and demand—the trend has ticked down since then, suggesting further driver shortages are on the horizon.

In particular, the portion of the existing workforce approaching retirement is set to start rising by 2025 as today's drivers age out, with the pool of prime-age drivers dropping significantly through 2029 if younger workers don't start entering the field.

As ACT Research President and Senior Analyst Kenny Vieth told Commercial Carrier Journal in January 2023: "It's going to be even more difficult to find drivers as we move into the recovery period (2024 and 2025)."

The driver shortage is having a particularly outsized impact on independent truckers working in the non-fleet segment of the market. In addition to the rising operational costs facing the entire industry, those working at the smaller end of the business have been dealing with driver shortage issues for the last five or more years in ways that their larger competitors have been able to largely sidestep.

"Historically speaking, most of our insurance carriers are looking for drivers with some sort of experience," explains Lorie Podolak, a Transportation Underwriter with RPS. "In the large fleet space, there are different concessions that can be made for inexperienced drivers to train them up in partnership with senior drivers and a good onboarding program. Those larger fleets have the flexibility to widen their net when it comes to hiring new drivers to overcome those shortages. But the

one- and two-unit operators don't often have that luxury because they're working in a smaller space and need drivers who are ready to hit the road immediately."

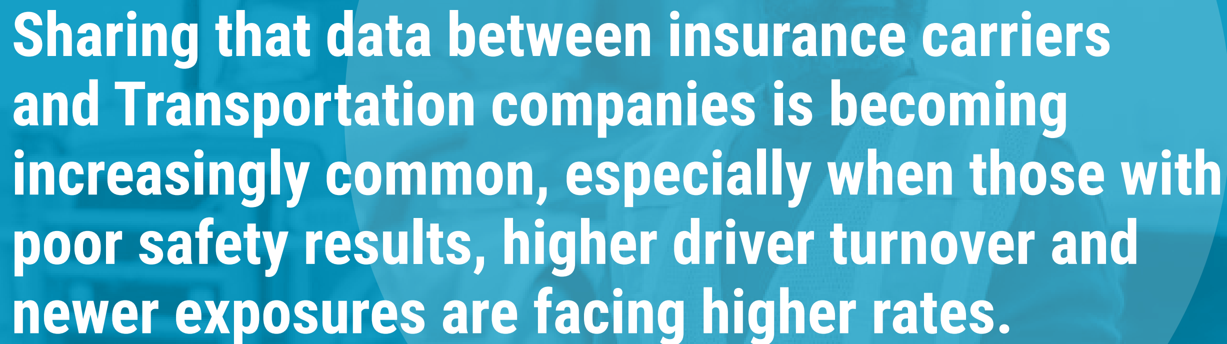
To combat these shortages, a number of state and federal government programs have been created to connect high school students with trucking co-ops, taking an inexperienced driver at 18 and training them so that they are ready for a job at graduation. Other programs—such as sign-on bonuses, late career training and even ownership opportunities—are working toward the same goal of increasing the pool of experienced drivers, though progress has been slow and availability remains a key constraint for operators.

TECHNOLOGY CONTROLLING COSTS

According to some estimates, as much as 40% of the cost of a new truck in 2023 goes toward technological enhancements. Technology such as electronic logging devices (ELD), which automatically record driving time to more accurately record hours of service (HOS). That's in addition to driver safety and loss prevention measures that have emerged over the last decade, such as lane departure warning systems, backup sensors, inward and outward facing cameras and more. (Of course, these advanced systems have also added to operational and maintenance costs as well, increasing repair bills, service time and replacement costs for these functions.)

Every truck since 2000 has been able to capture data via ELD—where you drive, how you drive, when you drive, how fast you drive, who is driving, etc. And sharing that data between insurance carriers and Transportation companies is becoming increasingly common, especially when those with poor safety results, higher driver turnover and newer exposures are facing higher rates. In those tougher segments, carriers are already tightening restrictions, particularly among those that are new to the Transportation industry, and it's opening the rest of the industry up to just what they have access to in that data.

"One of the biggest questions we face is, with all the costs surrounding the trucking industry, how can businesses keep their insurance costs in check?," Gallagher says. "One ask that we do have of clients that's relatively free of charge is that they share their ELD data. And virtually every new insurance carrier or program that is entering the marketplace is asking for this data. It's a great way for insurance providers to adjust and create better rating offerings in states, territories, by class, by commodity, time of day, etc, by quantifying and capturing the information that's available from ELDs."



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A growing group of insurance carriers are offering discounts when that data is shared, reducing costs for Transportation clients simply because carriers want that data and companies have access to it already. It helps in rate-making and in finding new solutions for Transportation clients.

“We can’t, as an industry, continue to raise rates just because losses are climbing,” says Gallagher. “We have to find new ways to offset those losses. Data collection can help us better understand driving patterns and behaviors so that we can find new ways for Transportation clients to reduce their costs.”

The use of this technology isn’t quite as clear-cut on the non-fleet side, however, due to the more personal nature of the business at that level. Not surprisingly, among owner-operators, the idea of in-cab surveillance or mileage tracking might be less appealing when the business owner themselves will be one of the drivers being monitored.

“Even with offerings like discounts or programs where you only pay for the mileage you drive, my agents have been getting resistance from insureds not wanting anyone else watching what they do,” says Podolak. “They sometimes feel like they’re being overly monitored by this technology when, historically speaking, one of the reasons that many people got into trucking was the freedom of being your own boss and being on your own.”

Too often also, customers are sharing data and not seeing much of a premium reduction on their bill. Or, they are getting detailed reports back from the carrier or the telematics provider and they don’t know what to do with it. Even if you’re noticing trends in what’s being recorded, if you aren’t able to act on those insights, you aren’t going to get much use out of that data in the long run.

Simply put, in some situations, discounts aren’t enough. Either the discounts on the equipment need to be better or the bottom line rate reductions need to be richer in order to get the industry as a whole—from the large carriers all the way down to solo shops—to fully jump on board with telematics as an industry practice.

Adds Podolak: “Particularly on the non-fleet side, there is an opportunity to explain the advantages of telematics products to clients. So, we at the wholesale level need to do a better job educating our customers on the advantages that their customers could see, both financially and operationally, by embracing telematics.”

THE COURT OF PUBLIC OPINION ISN’T GOING AWAY

The average temperature in most parts of east and central Texas is around 67°F in February, according to the National Weather Service, but that wasn’t the case in 2021, when the state was hit with a historic winter storm over Valentine’s Week, bringing snow, sleet and freezing rain to much of the eastern portion of the state. It was one of the most impactful weather events in US history—knocking out most of the region’s power and resulting in days of road closures, business shutdowns and more—causing more than $1 billion in property damage.

In the midst of all that chaos, a young trucker was slowly working his way through his route outside of Houston. He was fairly new to the industry but still experienced enough to meet acceptable standards for the carrier and was driving below the speed limit, being cautious as one would expect given the conditions.

Still, despite his best efforts, an SUV carrying a family traveling the other way on the highway lost control on the ice, crossed over into his lane and hit the truck head-on. As a result, several of the family members were gravely injured. There was effectively nothing the truck driver could have done to avoid the crash, as without the SUV traveling unsafely, the crash never would have occurred.

In the resulting court case, however, the jury found for the family, awarding them more than $10 million in damages.

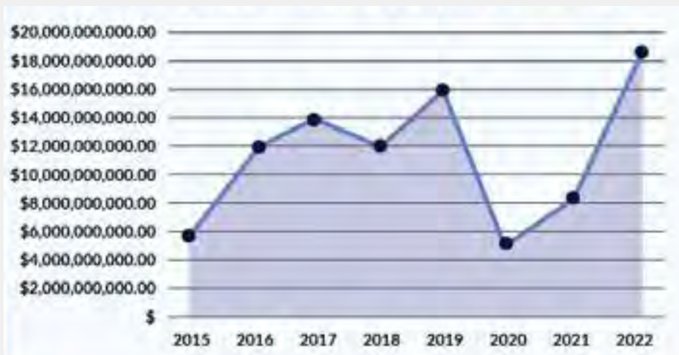
It was just another example of the so-called "nuclear verdicts" that are impacting the Transportation sector, leading to higher insurance costs and potential for large losses on the carrier side. And it is happening beyond just trucking to include any aspect of the sector where there is potential for injury or casualty. According to a March 2023 report from Marathon Strategies, the median verdict greater than $10 million against corporate defendants is up 55% since 2010. The COVID-19 pandemic shutdowns in 2020 slowed this trend, but it has only accelerated since the world got back to normal. Total corporate nuclear verdicts spiked sharply, from $4.9 billion in 2020 to over $18.9 billion in 2022. The mean verdict also nearly doubled in that time to $41.1 million.

Not surprisingly, these larger and larger judgments are impacting Transportation premiums and driving loss rates as claims and defense costs continue to rise. This is creating a ripple effect across the industry, impacting rates for everyone from large fleet clients to single-unit trucks. As Podolak explains, both the cost to defend claims as well as claims payouts have both increased exponentially over the last three to five years.

States including Texas, Iowa, and Florida have taken steps to address the rise of these judgments through early tort reform efforts, though the results have so far been limited. In the Lone Star State, for example, a nuclear verdict was challenged on appeal earlier this year, but the verdict was upheld despite the state's efforts to reform the process.

"Clearly, we're still far away from a solution," Podolak says. "I think the only hope for the insurance carriers is going to be boots on the ground and trying to get this done from a regulatory standpoint."

SUM OF CORPORATE NUCLEAR VERDICTS 2015—2022



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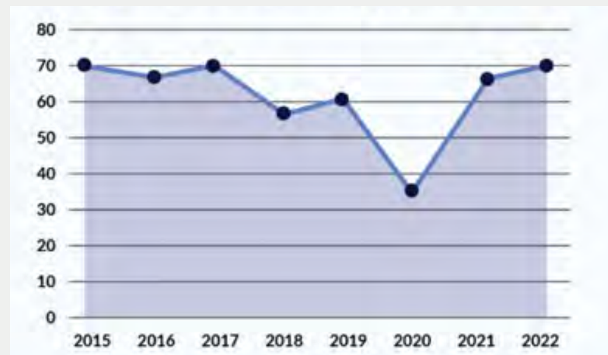

Source: Marathon Strategies; Corporate Verdicts Go Thermonuclear

PRICES UNDER PRESSURE

Not surprisingly, given all of these operational costs and risk factors, Transportation insurance carriers are facing downward pricing pressure because of the competition, despite the ongoing push for higher rates on their existing books of business.

“It’s kind of counterintuitive,” explains Mitchell. “Transportation is not for the faint of heart. It can be very volatile, and if you’re not careful, the losses can add up quickly. Some companies simply lose their comfort level with it and exit.”

But, despite those exits, new carriers are jumping into Transportation and keeping capacity at near record highs. With those new participants come new approaches to the market, from a focus on telematics and tracking to lower rates. Time will tell how successful these carriers are in Transportation, but in the short term, having more insurance companies in market should be good news for clients by reducing rates to help mitigate both increased operating costs as well as today’s lower freight rates. But legacy carriers who would prefer to raise premiums to compete might not agree.

“There’s so much capacity, so many players, so many different programs that, if you’re an insurance carrier and if you don’t lower your prices, there is another carrier waiting to underbid you,” says Niko Matic, Senior Commercial Auto Underwriter at Risk Placement Services.

As in all insurance markets, more capacity makes for lower rates and a more competitive market, and Transportation in 2023 is no exception. In addition to incumbent players, more and more insurtech firms have arrived in Transportation as well, further boosting capacity and leading more customers to shop around at renewal time.

On the whole, the downward pricing pressure for Transportation insurance is greater this year than it has been since COVID. In the boom times for Transportation, 5%–10% increases were easier for agents to sell since truckers were making record profits and weren’t struggling to stay in the black. Now agents have to dig deeper to explain individual premiums and more fully justify any increases.

“Now clients are expecting you to come in and give them a rate decrease because of the way they’re struggling financially right now,” says Matic. “It’s making things more difficult at a time when insurance companies themselves are needing higher rates on renewals as their loss costs continue to rise.”

Certainly, carriers are working to retain business while still maintaining a healthy pipeline of new business and market share. But we're also seeing more and more difficult places to place exposures and carriers continuing to restrict coverage in them. This includes segments of the Transportation industry such as cross-docking in Mexico from the US, garbage and refuse haulers, residential delivery, towing, dump haulers, public automotive, and more. In some of the business auto segments, for instance, standard line carriers are placing exposures in package policies that can be priced more efficiently than by breaking them out into their own self-contained policies.

Agents would do well to get specific at renewal time in this type of market. Compared to a year ago, risks that have performed well and have long tenure with a carrier can still see between flat and 5% increases at renewal, though decreases are not unheard of. For risks that have not performed as well, 15-20% increases are possible, which is emerging as a particularly competitive space where risks have had a more challenging history.

The reason? That is where most of the capacity is.

Explains Mitchell: "A lot of times that new capacity is coming in and offering some technology or for those types of risks to help almost rehab themselves, saying we can help save you some insurance money by implementing this technology. In turn, it makes them a better risk, which brings down their insurance costs."

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NEW INTEREST IN PROGRAMS

The same forces are impacting the Transportations Programs space, though in slightly different ways, according to Jeffrey Marks, Transportation Program Manager at Risk Placement Services. In fact, more and more players have been entering the program space in Transportation over the last five years and that trend doesn't look to be slowing down.

"There are programs being created for everything you could possibly imagine," he says, "and that is putting a lot of pressure on traditional insurers. They're feeling a lot of pressure and their results are showing it; they need to be more aggressive to retain that business instead of letting it go to the program space."

One problem is that the market for programs isn't necessarily getting any bigger. The pie is only so big, and every entity that jumps in is trying to get a little bit more profit out of the same piece of the pie as everyone else. So, what's happening is it's squeezing out some of the traditional insurers.

Not surprisingly, this is altering the competitive balance.

"Over the past decade, the competition for the insurance for the actual companies that are paying the bills has ramped up exponentially year over year. As the trucking industry is on the precipice of a major change—depending on how many years you believe it is going to take for self-driving technology to replace a lot of drivers—there's a bit of a fever pitch to make the most out of the market while it still exists in its current form."

This is happening alongside a reappraisal of where programs fits in the broader insurance industry.

"Programs requires a lot of partnerships, and you can't have a good partnership if at the end of the day one of the partners is holding a combined ratio above 100," Marks says. "Everybody has to be profitable and equitable in the sharing of those profits. So, as we build on our programs hopefully we'll prove that out and be able to get better terms and open up more RPS-exclusive programs that will make us more competitive in the wholesale space."

Whether or not the pace of growth in programs continues remains to be seen. Marks expects to see the interest from new entrants decelerate based on, if nothing else, the restrictive capital that's already in the market as well as new scrutiny from the capital that remains on the sidelines. But that's a good thing, he says. "In business, you succeed or fail typically off of merit. And I like to think that's what will happen here."

WHAT'S NEXT FOR TRANSPORTATION?

Transportation is in an interesting place at the moment, with a lot of unknowns surrounding both the state of the US economy and the outline for freight overall in 2024 and beyond. One broader force that could impact Transportation as well is the state of the banking system.

"I spoke to a client recently who brought something up that I had never considered before," says Matic. "If you're a bank right now and you've financed the purchase of a brand new tractor trailer for $300,000, would you

repossess that truck if your client can't make their payments? Of course not, because as soon as you repossess that truck, it's worth half of what you paid for it."

This is not just hypothetical, either. Some trucking companies are deferring their loan payments—still paying, but delaying them or negotiating more flexible terms—in hopes that freight rates and the market at large will turn around before the banks are forced to act. They are running on very thin margins at the moment, serving their debts in order to keep things going as long as possible. If and when banks start repossessing trucks that will lower the supply of Transportation infrastructure in the market, which would theoretically increase freight rates for those carriers that remain.

"Looking at the big picture about how everything is glued together right now, I think the biggest variable is the banks," Matic says. "They're essentially continuing the party by not making any big changes. But that approach could shift at any time and have major implications for Transportation overall."

In the short term, most expect the trucking and transport insurance market to remain largely unchanged in the year ahead, though it remains to be seen how the recent bankruptcy filing by Yellow—the third-largest freight carrier in the US that accounts for roughly 10% of all LTL transport capacity—could impact the broader Transportation market.

"It will be interesting to see if this becomes a short-term opportunity for some of our clients," Mitchell says, "but I expect to see that continue to play out in 2024. Hopefully, early on next year, we'll start to see the freight recession ease off and start to see freight rates go back to where these truckers have more healthy margins."

One thing that is and always will be true of our industry, no matter the challenges, the transportation industry is resilient. "So many transportation clients, carriers, and providers have been in business for decades as most all of them can weather the storms of our industry," Gallagher noted. "2024 may be the year where we are back on the upswing at some point, and if it is, our industry will respond and deliver."

One thing is and will always be true of our industry, no matter what the challenges, the transportation industry is resilient.

CONTRIBUTORS

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