

Light at the end of the tunnel: How far off is economic recovery for the American shipper?

"The gap in our economy is between what we have and what we think we ought to have."

- Paul Heyne, US economist-educator

"Globalization is a fact of life. But I believe we have underestimated its fragility."

- Kofi Annan, in 2001. Annan, a Ghanaian, was the 7th Secretary-General of the UN.

"It's a recession when your neighbor loses his job; it's a depression when you lose yours."

- former US President Harry Truman

By George Lauriat, AJOT

MIND THE GAP

For those who use the London underground, there is a familiar refrain heard when leaving or entering the train. The "mind the gap" announcement alerts passengers to the separation between the platform and the cars. In the US "mind the gap" could easily refer to the trade gap between the imports and exports of goods (exclusive of oil and services). The trade gap is nothing new. The United States has been running trade deficits for three decades plus. However, the trade deficits began to expand at an unprecedented rate in the late 1980s and continued to rise at a rapid clip until slamming into the barrier of economic recession in the fourth quarter of last year. For example, back in 1987 the goods deficit was just over \$152 billion, significant but with a booming economy, not a major concern. But by the 2001, economists were getting nervous about the rising trade deficit, coupled with strong dollar...and a suspiciously weak Chinese Yuan. In November of 2004, Federal Reserve Chairman Alan Greenspan jolted Wall Street when he commented that the US trade deficit "cannot continue to increase forever." This was economic vagrancy, an economy blissfully rolling along with no visible means of support. Still the trade deficits continued to increase and according to the recently released data from the US Census Bureau, the goods deficit in 2008 was \$821.2 billion, up over the \$819.4 billion in 2007.

GLOBALIZATION: SOURCING AND OUTSOURCING

Back in 2001, Greenspan had already believed that the US economy was in recession. Greenspan was probably right but the impact at the "Mall" level was minimal. High value consumer imports destined for US retailers like Wal-Mart, Target, Costco, Sears and Kohls continued to pour in from China. More importantly, the goods sold as fast as the shelves were stocked. The result was that the retailers posted record sales while China tallied record trade surpluses. In 2008, the US trade deficit with China hit a record \$266.3 billion as imports from that country rose to a record \$337.8 billion. Money is one thing but the physical impact is almost impossible to imagine. In 1997, China exported 1.48 million TEUs worth of goods to the US. By a decade later the total had risen to 8.8 million TEUs, which in terms of length would extend around the world one-and-third times. During the same span, US imports from Japan went from 721,000 TEUs to 783,000 import TEUs. Amazingly, China's numbers do not include Hong Kong, the United States' number three importer in terms of TEUs. Hong Kong sent 631,000 boxes to the US in 1997 and ten years later the number was 644,000 – albeit almost half of Hong Kong's exports to the US shifted to mainland ports over the period.

The reasons that the retail boom in the US continued were varied. Real estate and the housing market were white hot, with easy mortgages and low interest rates. Americans began using their ever increasingly higher valued homes like ATM machines, employing refinancing to generate disposable income. Although certain sectors would time to time be hit, the globalization of share markets seemed to act like a child's seesaw, when one segment was down another rose.

Another aspect to the period leading up to last year's crash was the invasive nature of globalization. The Internet was more than a worldwide people's movement it connected businesses in ways that had never been imagined. An ATM card in Boston, Massachusetts, dispenses cash just as well in Boston, United Kingdom. Equally, any IT service could be provided from any spot in the globe to any size company. Suddenly, global wasn't an exclusive enterprise of mega-companies but with in the reach of every company. There is an old saying that "bad news travel fast," and never has news bad (or good)

traveled faster than in today's global markets. Conversely, when the system breaks down, there is no place to run and no place to hide.

GREAT WAL OF CHINA

Unquestionably, the most influential company of the last two decades is Wal-Mart. In 2008, Wal-Mart is estimated to have accounted for nearly three percent (AJOT estimates that Wal-Mart imported over a million import TEUs annually; see US top importer chart). Beyond this figure are countless TEUS that suppliers import on their own accounts and later sell to Wal-Mart. A vast majority of these containers came from China (it is estimated that directly and indirectly Wal-Mart spends \$15 billion annually in China). Back in 2002, Wal-Mart shifted its global procurement operations to Shenzhen, just over the border from Hong Kong (formerly Wal-Mart used Pacific Resources for procurement). Many retailers followed the Wal-Mart lead in sourcing China products. It was said that in 1996 only six percent of Wal-Mart's products were sourced outside the US. Over the next decade Wal-Mart and other retailers did an about face. In Wal-Mart's case, the company had enough leverage (it's been said that Wal-Mart would be the 11th largest economy in the world if it was a nation) with suppliers to force them to shift operations from the US to China and other developing countries to keep costs low for American consumers...and provide a return for shareholders. This seemed to run counter to the avowed "Buy American" slogan of the time. Rightly or wrongly, the shift to outsourcing had already begun and what Wal-Mart did different was to take a holistic approach: factory floor-to-store shelf-to-consumer. Recently, Wal-Mart has been buying more products direct from the factory, rather than through the traditional brand names or middlemen. With the increased pressure on shareholder returns in a difficult market this process saves costs and shortens the supply chain.

Wal-Mart was ahead of the curve, or it can be argued created the curve. And it maybe is happening again. In late October 2008 Wal-Mart's CEO Lee Scott, while in China, announced a sweeping initiative to create a more transparent and greener supply-chain. This initiative includes new supplier commitments, more surprise audits, greater energy efficiencies, significant reduction in plant pollution, zero product defect by 2012 and the demand that all factories must give the name and location of their suppliers. Wal-Mart also made it

clear that those suppliers that don't comply within a reasonable time frame will be dropped. It's an ambitious overhaul. It won't be easy to create transparency throughout the supply-chain. Scott's address came less than a month after Sweatfree Communities, an anti-sweatshop activist group, issued a report documenting abuses of a Bangladesh-based factory supplying apparel to Wal-Mart. The report contained testimony by factory workers on deliberate attempts to cover up working conditions from Wal-Mart audits. With the increased pressure over "outsourced" US jobs coming from Congress all retailers will be compelled to follow Wal-Mart's lead to greater supply chain transparency or else fuel the fires of protectionism. Among those issues that might light the fuse is press reports that the mega-retailer intends to outsource its US based IT operations to India – a contract estimated to be worth \$300-\$500 million. Recently President Obama, in a televised address, said American companies shouldn't outsource US-based IT jobs overseas, arguing that this creates more unemployment and hurts the already damaged economy. The President had already said he wanted "Buy American" part of the stimulus package. Undoubtedly, outsourcing of jobs will be under greater scrutiny than any time in the past three decades.

...continued on page 2

Year	1st	2nd	3rd	4th	Total
2009	2,238,183	NA	NA	NA	2,238,183
2008	6,753,999	6,874,409	7,173,035	7,599,455	28,400,898
2007	7,006,112	7,421,112	7,519,347	8,002,891	29,949,793
2006	6,354,449	7,192,465	7,836,001	7,730,283	29,107,198
2005	5,778,965	6,247,634	6,497,759	6,742,847	25,267,305
2004	5,132,831	6,038,327	5,804,144	6,140,617	23,115,919
2003	3,821,074	4,289,819	4,259,802	4,507,797	16,878,492

Source Zepol (based on AMS data)

...continued from page 1

FOUR CORNERS OF THE BOX

In 2008, the US imported 29 million containers, continuing to land boxes (7.6 million TEUs - see Quarterly Chart) deep into the fourth quarter, well after the economic crisis had hit. With retail sales in December off, inventories are high and 2009 looks weak. In 2008, a number of big name retailers went out of business, such as Circuit City and Linen 'n Things, while a number of others were merged or acquired. The impact on the retail sector has yet to filter fully through to bottom line statistics but heavy layoffs are well underway. In 2008, the retail sector is said to have laid off 500,000 of the 2.6 million layoffs nationwide.

Through February 11th, the US had imported just over 2.3 million TEUs, around half the number tallied the first quarters of the last few years. China's Customs recently reported that trade with the US was off 15.2% and year-to-year figures showed a 17% decline in foreign trade overall. However, China also reported that foreign trade in January is up 102% over January 2008. The mixed numbers indicate a slowdown in China, Inc. (that and the thousands of migrant factory workers that have returned home after factory layoffs) but to what extent is still unclear.

Already we are seeing some big names in retail posting big declines in same-store-sales (often considered the best way to analyze performance). Retailers like Dillard (-12%), JC Penney (-16.4%), Gap (-23%), Saks (-24%), Talbot's (-24.6) are all down big when compared to January 2008. Still there is a little glimmer of light in the tunnel (if not at the end). Wal-Mart's own same-store-sales are up 2.1%, and others like Costco (4%), BJ Wholesale (7.6%), Gottschalk's (8.8%) and Walgreens (0.1%) managed to beat the odds and post gains.

Ultimately the "bailout" for retailers and the steamship lines and ports and other links in the supporting supply chain will depend on the American consumer. If imports fall to around 28 million TEUs or less (compared to the near 30 million posted in 2007), even with cutbacks, layoffs and vessel lay ups, bankruptcies and acquisitions and mergers will happen and the business landscape will be much changed. Anan Kofi, former Secretary General of the United Nations, made the prescient comment in 2001, "Globalization is a fact of life. But I believe we have underestimated its fragility." With the global recession the 'fragility' and interdependence of markets and economies has never been clearer. The beginning of the end to recession may have already started with that simple recognition.

Top US Importers

Name	Business	Headquarters	2007	2008
Wal Mart Stores	Retailer	Bentonville, Arkansas	776,695	1,013,458
Target Stores	Retailer	Minneapolis, Minnesota	545,350	550,000
LG Electronics	Electronics	Englewood Cliffs, New Jersey	251,339	446,341
(Lowes) L G Sourcing	Specialty Retailer	Wilkesboro, North Carolina	518,189	257,173
Adidas America (Taylor Golf/Rockport)	Footwear/Apparel Retailer	Portland, Oregon	428,315	255,994
Costco	Retailer	Issaquah, Washington	444,467	248,246
Fisher Price (Mattel, AB Brands)	Toys	East Aurora, New York	353,765	240,075
Dole Fresh Fruit	Food Distributor	Westlake Village, CA	279,149	216,228
Sears Merchandising Services/KMART	Retailer	Chicago, Illinois	269,869	216,228
Nestle	Food Distributor	Glendale, California	342,400	204,974
Ikea	Furniture	Mount Holly, New Jersey	313,004	201,858
Red Bull	Beverage Distributor	Santa Monica, California	116,138	169,725
Jarden	Niche Retailer	Rye, New York	153,723	159,741
Nike/Reebok	Shoes/Apparel	Beaverton, Oregon	139,076	153,789
American Honda (Honda)	Auto Parts/RV/engine related	Torrance, California	33,893	133,493
JCPenney	Retailer	Plano, Texas	160,333	133,118
Big Lots Stores	Retailer	Columbus, Ohio	196,095	126,009
Altria (PhilipMorris)	Food/tobacco conglomerate	Richmond,VA	NA	121,181
Pier 1 Imports	Retailer	Savannah, Georgia	67,050	118,412
Kohls Department Stores	Retailer	Menomonee Falls, Wisconsin	175,601	116,868
TJX, Newton Buyer (TJ Maxx) Marshalls	Apparel Retailer	Framingham, Massachusetts	98,869	116,593
Samsung (ADC)	Electronics	San Diego, California	151,770	109,241
Heineken USA	Beverage Distributor	White Plains, New York	134,629	95,643
Best Buy	Retailer	Minneapolis, Minnesota	72,014	87,720
Kroger/Fred Myer	Retailer	Cincinnati, Ohio	73,631	87,091
Diageo	Beverage Distributor	London, UK	NA	80,754
Canon USA	Electronics	Lake Success, New York	127,675	77,657
Coaster	Furniture distributor	Bensenville, Illinois	130,650	68,556
Arauco Wood	Lumber, wood products	Atlanta, Georgia	48,042	66,446
Michaels	Arts and Crafts Retailer	Irving, Texas	89,931	65,183
Walgreens	Retailer	Deerfield, Illinois	70,109	64,364
Family Dollar Stores	Retailer	Matthews, North Carolina	34,111	59,668
Dollar General	Retailer	Goodlettsville, Tennessee	62,663	58,069
Xerox	Electronics/imaging	Norwalk, Connecticut	76,230	57,354
Marubeni USA	Trading House	New York, New York	54,062	57,076
Gap Stores	Apparel Retailer	San Francisco, California	73,965	57,044
Federated Dept/Macys/Bloomingdale	Retailer	New York, New York	62,751	51,476
Bridgestone	Tires	Nashville, Tennessee	99,452	46,120
General Electric	Conglomerate	Stamford, CT	104,661	46,050
Home Depot	Specialty Retailer	Atlanta, Georgia	253,519	41,366
RTG	Furniture	Seffner, Florida	44,719	38,915
Toyo Tire	Tires	Cypress, California	68,958	37,211
Lite-On IT	Computer Peripherals	Whittier, California	79,103	35,784
Nissan Motors	Auto	Smyrna, Tennessee	91,894	32,798
GEA Products	Engineering Systems	Bochum, Germany	49,526	32,303
Newell/Rubbermaid	plastic containers	Atlanta, Georgia	NA	27,067
Sketchers USA	Footwear/Apparel Retailer	Manhattan Beach, California	29,116	25,752
General Motors	Auto	Detroit, Michigan	44,831	24,855

Source: Zepol

Zepol is a privately held Minneapolis-based corporation that provides an innovative, online trade database. Co-founders Paul Rasmussen and Jeff Wilson launched Zepol in 2002. TradeIQ™ offers subscribers access to vital import data-developed entirely from US import Bills of Ladings.