The Quarterly Forecast

ISSUE 2: JANUARY 2019

WORLDWIDE

Joe's View

Executive Summary by
Joseph Barry, President & Founder

SYNOPSIS

Tough questions still remain: Will we see a second front-loading push before the next round of tariffs? How will supply chains mitigate tariff-related pitfalls? Will the 25% duties on Chinese goods ever even come to fruition?

UNEMPLOYMENT IS DOWN, WAGES ARE ON THE UPTICK, AND CONSUMER SPENDING REFLECTS AN ECONOMY WITH AMPLE DISPOSABLE INCOME TO SPARE. Despite all signs pointing toward a happy, healthy economy, businesses and consumers alike would do well to brace for impact as an unpredictable trade war between China and the United States continues to churn.

In summary, Q4 2018 embodied the very essence of chaos, as impending tariff deadlines goaded panicked ordering decisions within global supply chains several months ahead of schedule. As supply chain professionals, we pride ourselves on our penchant for planning, but even the best-laid plans stand to be devastated by President Donald Trump's threat of 25% tariffs on all Chinese imports. To avoid paying unprecedented duties, many retailers rushed to collect their entire Q1 2019 inventories ahead of Trump's initial January 1 deadline (since delayed until March 1), which spurred a chain of events leading to sky-high spot rates and a severe bottleneck in trucking.

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These are the mysteries plaguing forwarders and the shipping industry at large. The truth is, we are just as much in the dark about the future of tariffs now as we were in October, and we can expect a lot of the same uncertainty in 2019.

We may not have all the answers, but what we do have is a wealth of strategic knowledge derived from decades of experience tackling every freight forwarding difficulty head-on, and a dedicated network of preferred partners who have our backs as staunchly as we have theirs.

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We will continue to monitor the situation, and continue to provide unprecedented freight forwarding and logistics services to our clients, no matter the seas ahead.

TARIFF UPDATE: A TALE OF TWO DEADLINES

At the start of the last quarter, businesses were told to prepare for the worst. July and September tariff adjustments were set to increase once again, this time from 10% to 25% at the start of the new year, January 1, 2019. On the same day, previously unaffected Chinese goods were also to be introduced to the tariff list.

News of the January 1 deadline helped fuel an importing boom, as supply chains were forced to make timely decisions regarding their inventories. For many businesses, this meant front-loading entire Q1 inventories ahead of January 1. In doing so, importers inadvertently intensified a persistent trucking shortage that seems guaranteed to worsen before improving.

Tensions spiked at the end of November during the G20 Summit in Buenos Aires, where talks between President Trump and China’s Xi Jinping resulted in a surprising 90-day tariff truce until roughly March 1. Suddenly, the dramatics of Q1 inventory acquisition—namely, strategic planning, financial gambling, warehousing turmoil, struggle for cargo capacity, driver scarcity, etc.—seemed all for naught.

A vague commitment to the 90-day pause is the only major detail of the three-hour meeting between the two leaders that’s been released to the public. The White House is keeping this one close to the vest, but Trump has suggested a favorable position for the United States in several tweets.

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The shipping industry’s fourth quarter reflected a healthy U.S. economy, albeit one that’s been kept on its toes as a touchy trade war with China continues to brew. The industry was taken by surprise when, on December 1, a so-called 90-day tariff “ceasefire” began, which leaves supply chains, once again, to make drastic ordering decisions based largely on indeterminate variables.

THE BREAKDOWN

90-Day Strategy:

- “People who are not way over inventory, who have cash, will buy. As we get closer to that deadline—60 days in or maybe 45 days in—we’ll see another push of people trying to get their goods in before the increase because that 15% increase (from 10% to 25%) is a big difference. The interesting thing is, when that happens, we’ll be at the beginning of the second quarter, so if people work through their first quarter inventories, they can do the same thing again. So, depending on how the talks go, we may see an uptick again toward the deadline.”

- The proposed 25% tariffs on the remaining $200+ billion in Chinese goods that are still in tariff limbo will be too hefty a burden for supply chains to absorb. The targeted products are more consumer-centric, so if the additional duties are implemented, consumers will experience the change in the form of inflated prices.

Oil:

- In an effort to reduce harmful shipping emissions, the International Maritime Organization (IMO) will lower the global sulfur cap on fuel content from 3.5% to .5% in 2020. Ahead of this mandate, all lines are said to be preparing to set low sulfur surcharges (also referred to as Green Fuel Surcharge, Emission Control Area Surcharge, and Low Sulfur Fuel Surcharge), beginning January 1, 2019.

- “Some carriers have already implemented their own mandatory low sulfur surcharges. As a result, forwarders aren’t necessarily experiencing the reduced cost of oil, because the mandates are increasing the actual cost of the bunker. They’re using cleaner burning fuel, so the actual cost is more, because the fuel has to be refined further.”

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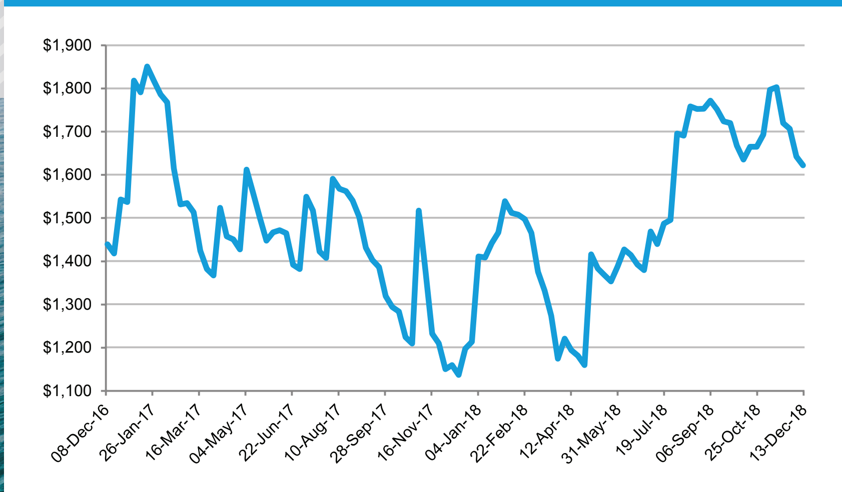
Trucking Shortage:

- The main issue facing importers right now is an intensifying trucking shortage. There are simply not enough trucks/drivers to keep up with booming consumer/importer demand.
- Drayage providers have been hit hardest by the shortage, especially in L.A. and New York, where container traffic is very high. Some carriers are even pulling back on their door-to-door services because they know they will be faced with unfavorable drayage handling timeline when they arrive in terminal.
- One way trucking companies are combating the driver shortage is by raising wages to attract new drivers and improve current driver retention rates. There are also talent acquisition initiatives in place that target the industry's most underrepresented demographics; namely, young women.
- In December 2017, truckers were introduced to what's known as the electronic logging device mandate. The rule is meant to improve driver safety by limiting the number of hours spent on the road daily, in accordance with labor laws. Despite the admirable intentions of the rule, many truckers cite reduced salaries, loss of freedom, and insufficient parking capacity at truck stops in their arguments against it.

Trade Lane Notes

Insights from **Torie Coleman,**
Director of Operations

World Container Index: Assessed by Drewry, $/40ft container



Source: The World Container Index assessed by Drewry, a composite of container freight rates on eight major routes to/from the United States, Europe, and Asia

SYNOPSIS

The China-USA trade war has been a boon for carriers, who were able to demand lofty surcharges in exchange for precious cargo space amid the influx of panicked front-loading that took place ahead of supposed January 1 tariff updates.

THE BREAKDOWN

- As the timeline for meeting the January 1 deadline narrowed to a close, volumes dropped, along with shipping rates. The result is available cargo space, and subsequently, some leverage in pricing negotiations has transferred to importers and forwarders.

- Q1 capacity will rely on a confluence of factors:

    1. As it is, warehouse vacancy is so scarce that some importers are holding containers and chassis for up to 30 days. Warehouse scarcity is due at least in part to front-loading associated with the initial threat of January 1 tariffs. If Trump moves forward with additional duties, more front-loading is in store, and with it, hiked rates and tightened capacity.

    2. How many businesses have exhausted their ordering power or storage options? If a business has front-loaded their spring stock already, they may not have the resources to do it again.

    3. If a deal is successfully negotiated and new tariffs are taken off the menu, the recent volatility of rates and capacity should stabilize.

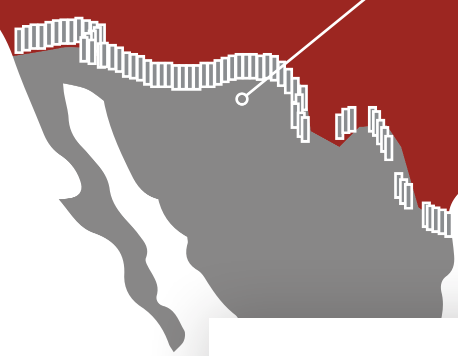
    4. Q4 saw a lot of capacity control in the form of blank sailings (26 on the Trans-Pacific lane, alone). Carriers will likely plan blank sailings in January to capitalize on the two-week shutdown of Chinese shops beginning February 5.

- Shipping rates from China to the United States have increased more than 100% from 2017 levels (China-West Coast: 128%, China-East Coast: 123%). However, since the tariff deadline has been extended, we have seen a downward trend in Trans-Pacific shipping rates. ■

CAF WORLDWIDE

Global Economic Forecast

Trump's threat of a multi-year government shutdown is his response to congressional resistance a federally subsidized of a 2,000-mile-long U.S.-Mexico border wall. A prolonged shutdown could disrupt the trade of up to $821 million in goods per day at the Southern border.



Economic Recession

The synchronized economic growth that defined 2017-18 appears to be in peril as trade growth is slowing and in some cases, shrinking. Some analysts have gone so far as to call for an economic recession to ensue as soon as this year. U.S. economic growth has decelerated quarter-to-quarter in 2018.

- Q2 2018: 4.2% growth (actual)
- Q3 2018: 3.5% growth (actual)
- Q4 2018: 2.9% growth (projection)
- Q1 2019: 2.5% growth (projection)

Container Trade

According to Maersk, the world's biggest container ship operator, global container trade growth slowed between 2017 and 2018.

- 2017: 5.8% growth
- 2018: 4.2% growth

Global Trade

According to data provided by Trading Economics, a trade data publication, global trade has already been negatively affected by tariff updates.

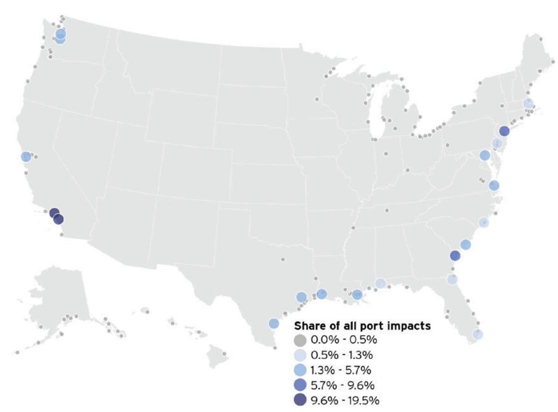
- GDP growth rate December 2017: 4.2%
- GDP growth rate December 2018: 3.4%

DOMESTIC IMPACT

According to a report by Brookings, 94% of tariff impacts are distributed among just 20 United States seaports.

Tariffs could result in 10% to 20% less product being moved per port in the United States, which may reduce or eliminate the need for many port workers.

Tariff impact exposure by seaport, individual totals and U.S. shares, 2017



Source: Brookings analysis of PIERS data

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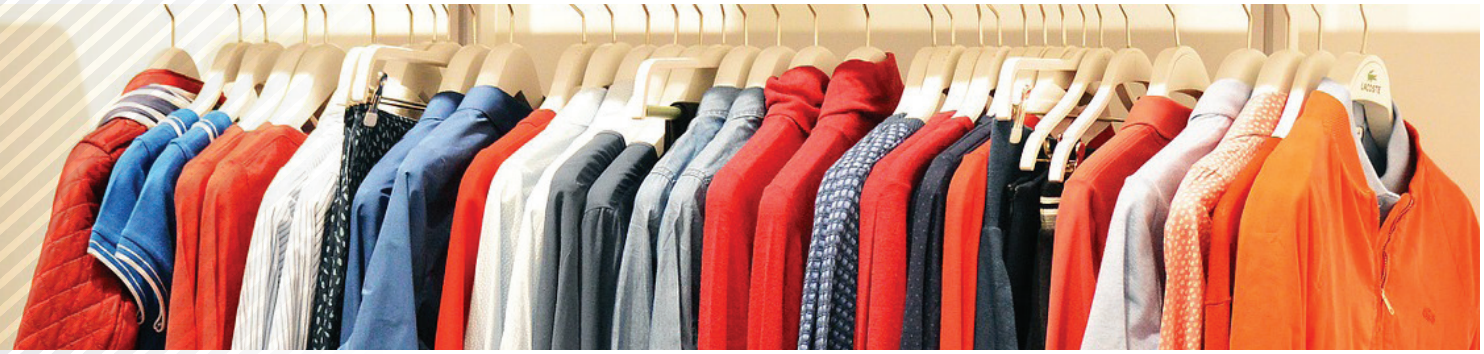
Global Economic Forecast



WHAT'S NEXT FOR APPAREL?

Trump tariffs and sanctions on Chinese goods have emboldened apparel manufacturing markets to shift away from China in favor of neighboring countries with lower labor costs. Thus far, Vietnam and Bangladesh are the two prime benefactors.

- Bangladesh is the second-largest exporter of apparel, claiming 6.4% of global share.
- Vietnam is the third-largest, with 5.8%.
- The minimum wage rate in Vietnam is $122–$176 per month.

Per the Commerce Department's GDP data released on October 26, consumer spending on clothing and footwear rose 11.7% year-over-year last quarter. This marked its biggest increase since 2005. We believe growth in consumer demand to be organic. ■