

Outlook: Global Re-balancing

2010 AAPA SHIFTING INTERNATIONAL TRADE ROUTES

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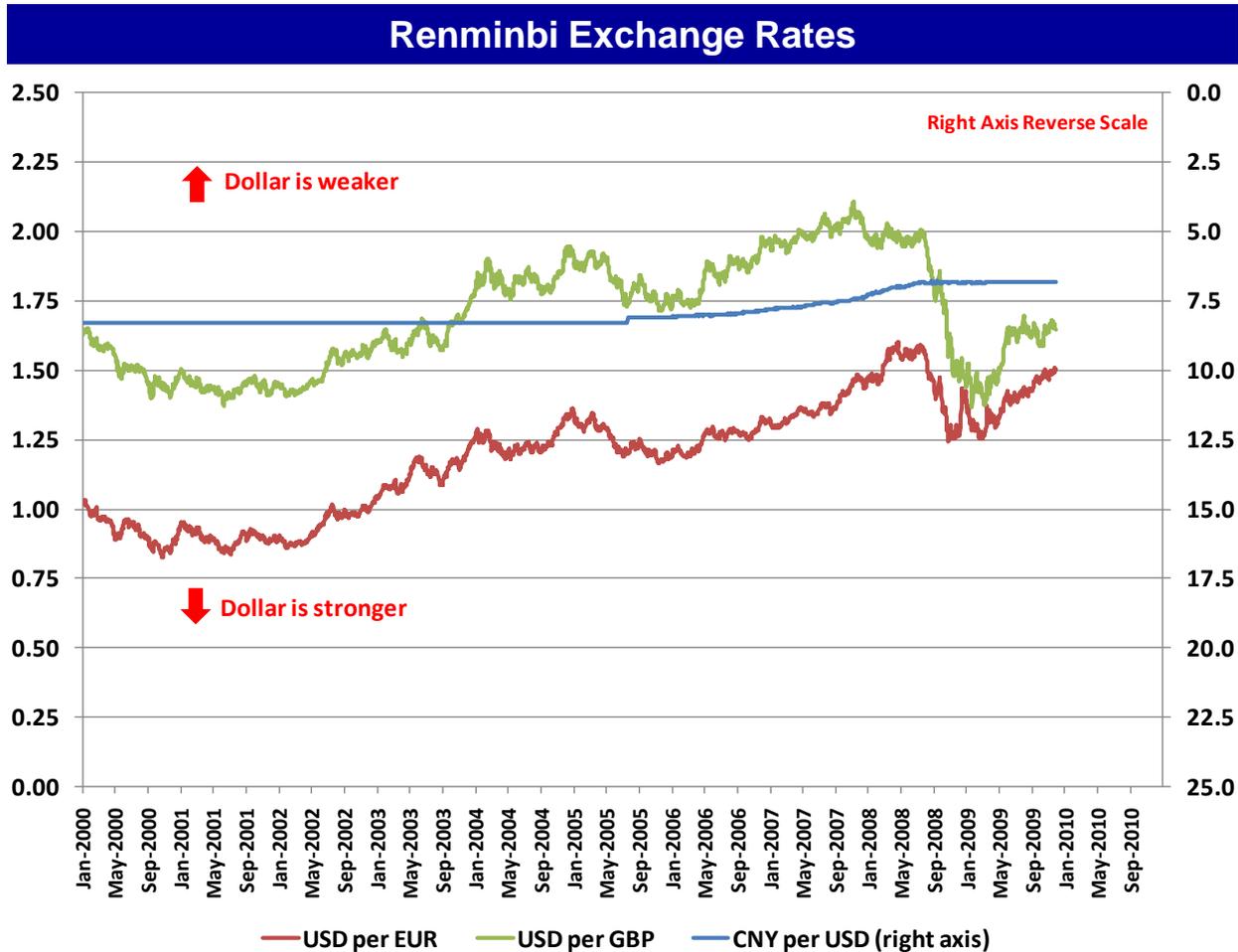


Major Themes

- ◆ **Recovering from Near Depression Experience is hampered by a weak financial system and global imbalances driven by China**
- ◆ **Long term trends remain intact for imports but the US needs to export more as trade cannot remain unbalanced indefinitely**
- ◆ **Bulk commodity trade could exceed container volume growth as emerging market economies mature**

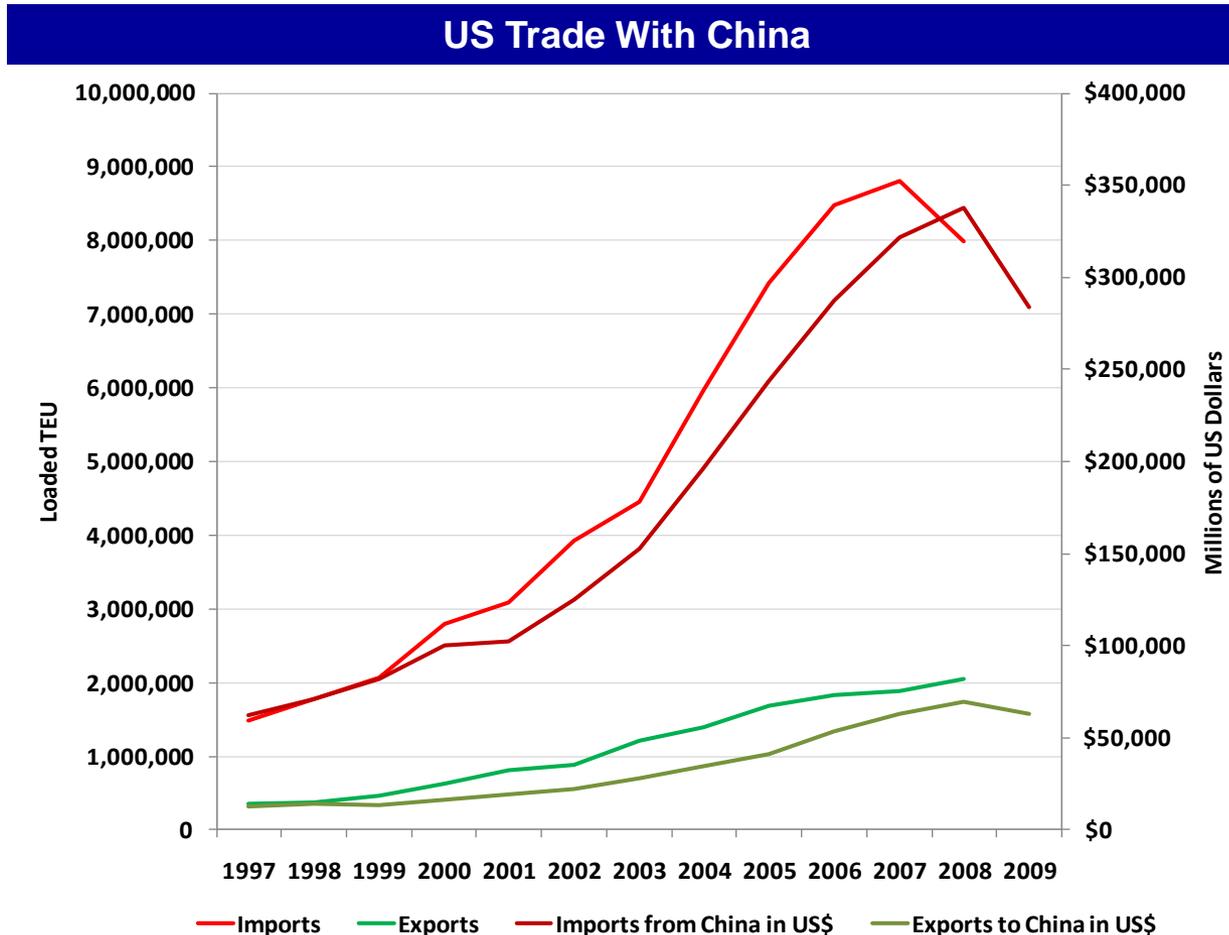
Macroeconomic Trends

Tampering With The Foreign Exchange Market



- ◆ In its biannual Currency Manipulators report, the US Treasury has never accused China of manipulating the renminbi's value against the US dollar.

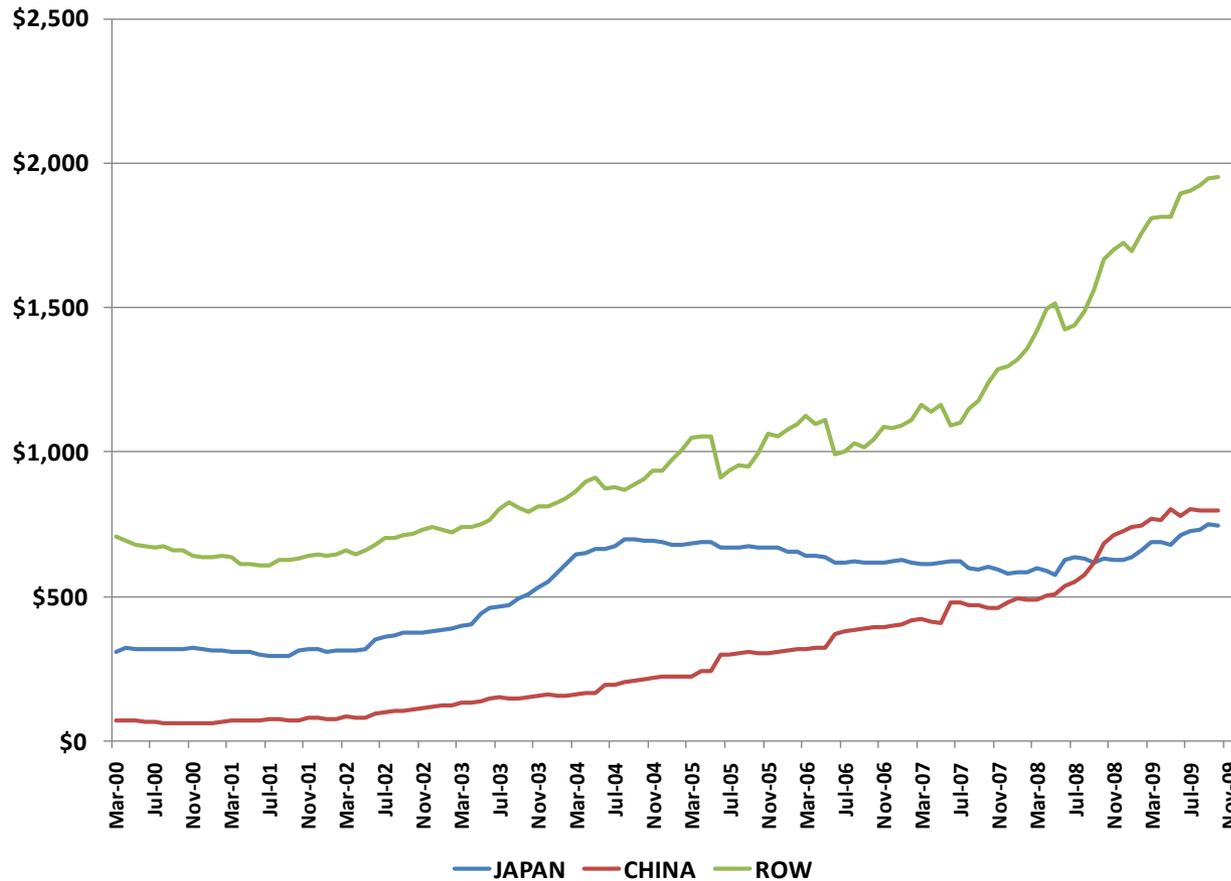
A Major Global Imbalance



- ◆ **China has become the largest source of US imports and the second largest destination of US exports**
- ◆ **To sustain this growth, China maintained a low exchange value of yuan for dollars by investing its trade revenue surplus in US treasuries**

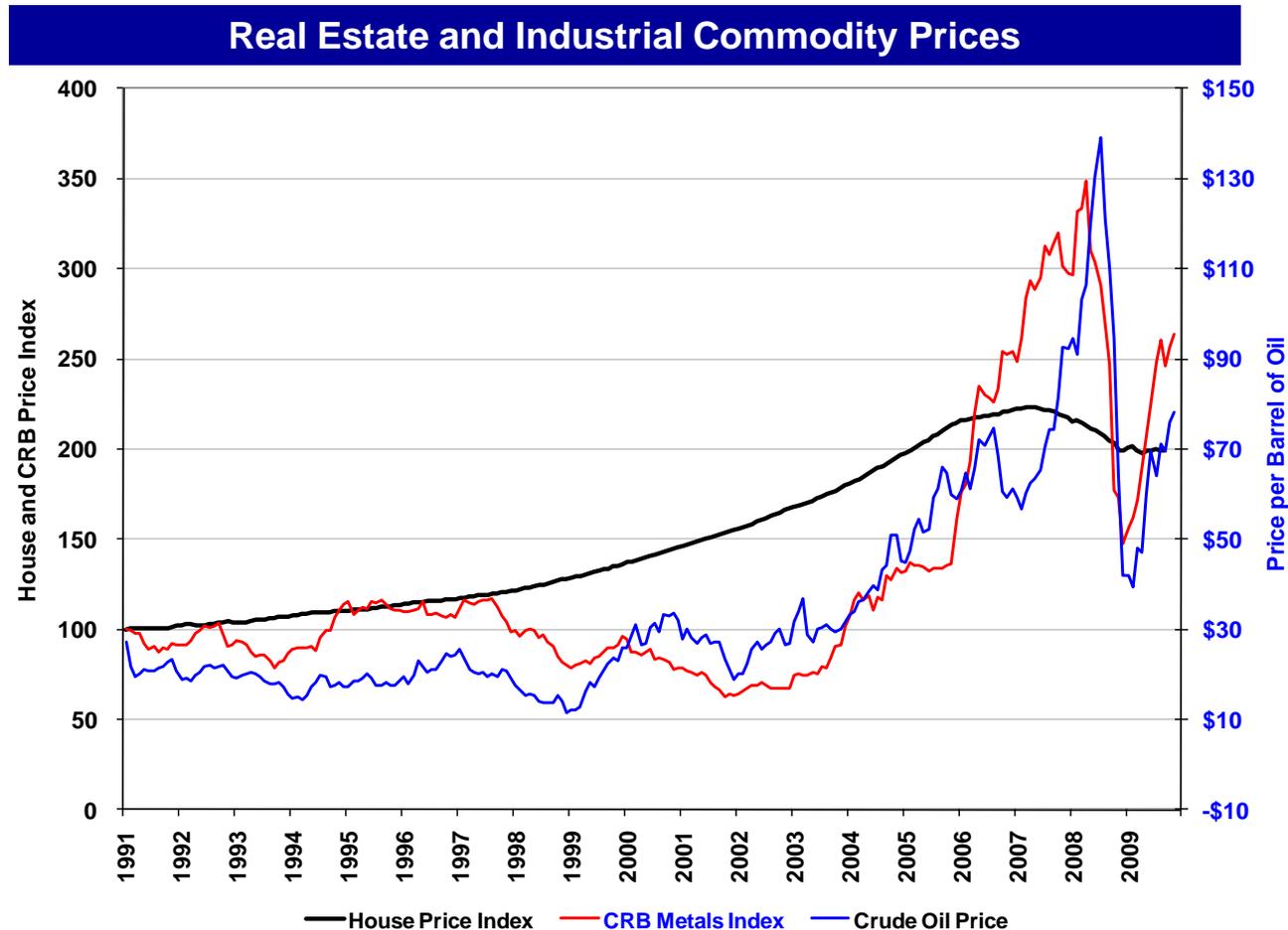
China Became The Largest Owner of US Debt

Treasury International Capital Reported Positions



- ◆ In October 2008 China became the largest foreign owner of US Treasury debt, surpassing Japan

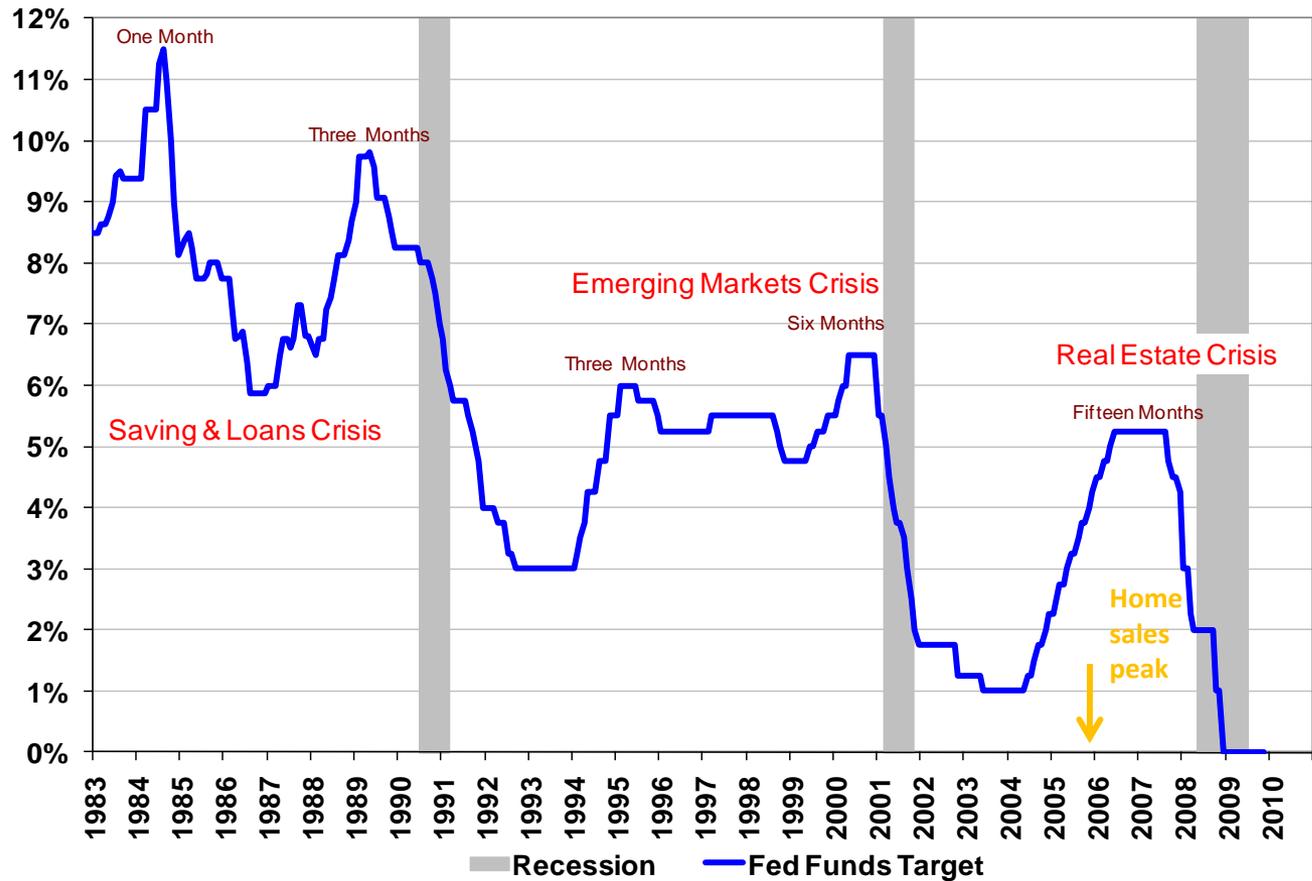
Twin Bubbles



- ◆ **China impacted the world and US economy in several ways**
 - ◆ Invested surplus trade revenues in US bonds, resulting in lower mortgage interest rates and therefore a housing boom
 - ◆ China's factory capacity and US real estate investment booms drove commodity prices up

Monetary Policy Response

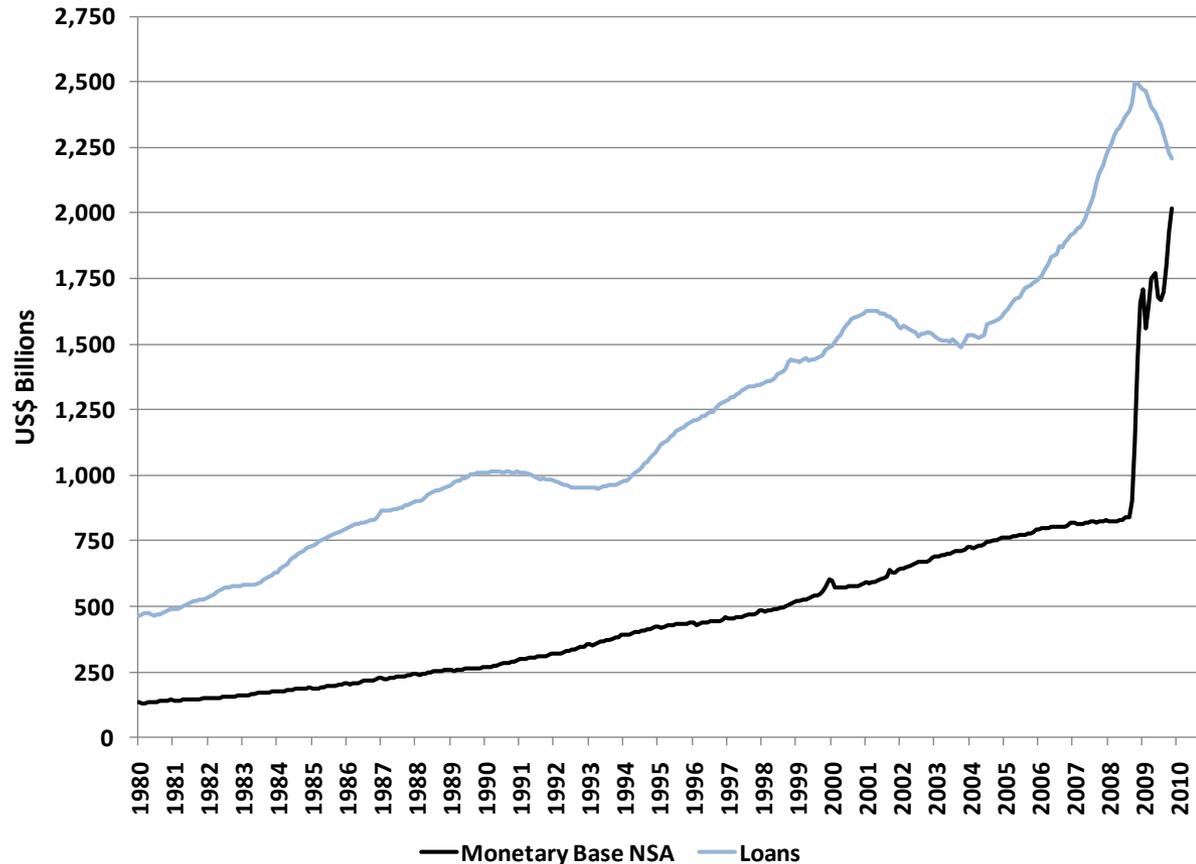
Federal Reserve Policy Interest Rate Target for Federal Funds



- ◆ Fed Funds policy interest rate was kept at a high level for an unusually long period
- ◆ Inflation was considered a greater risk than mortgage finance

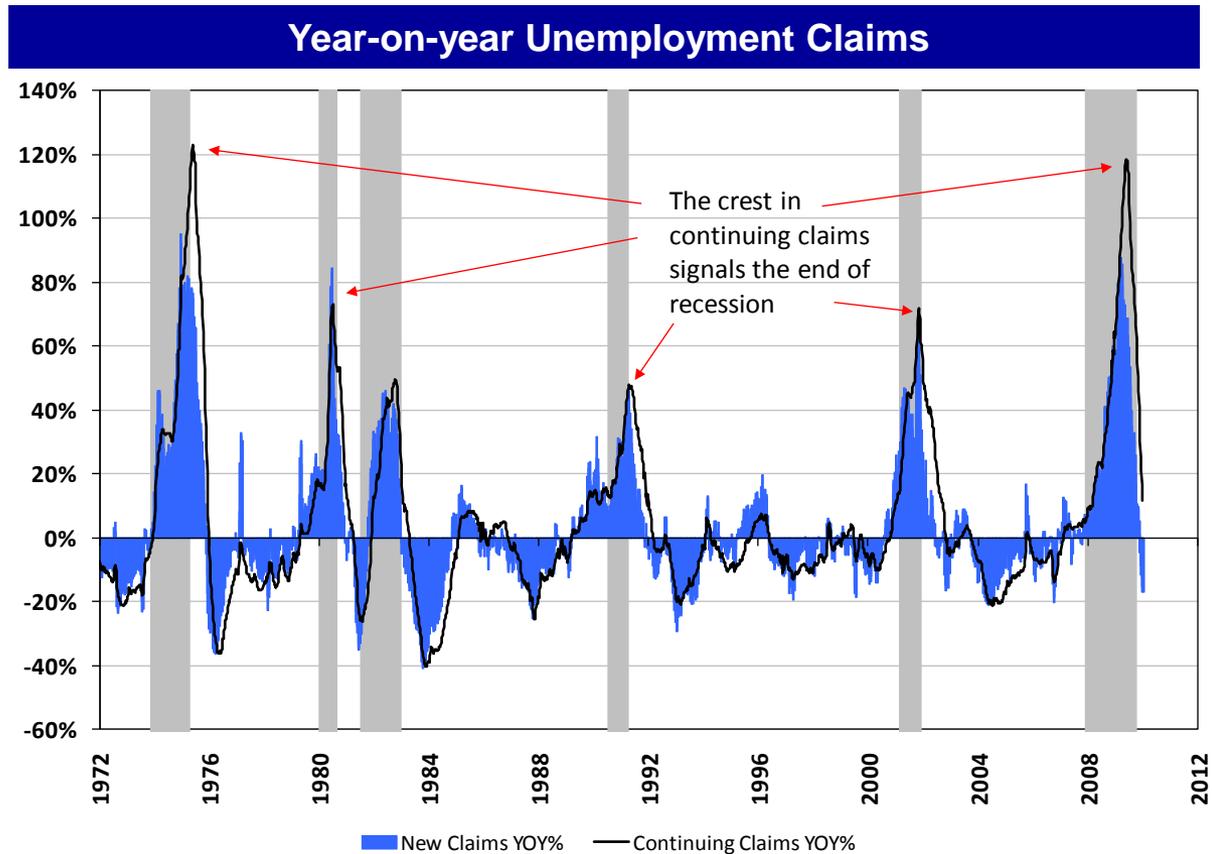
The Fed Made A Dramatic Effort As Liquidity Dried Up

Adjusted Monetary Base And Business & Consumer Loans



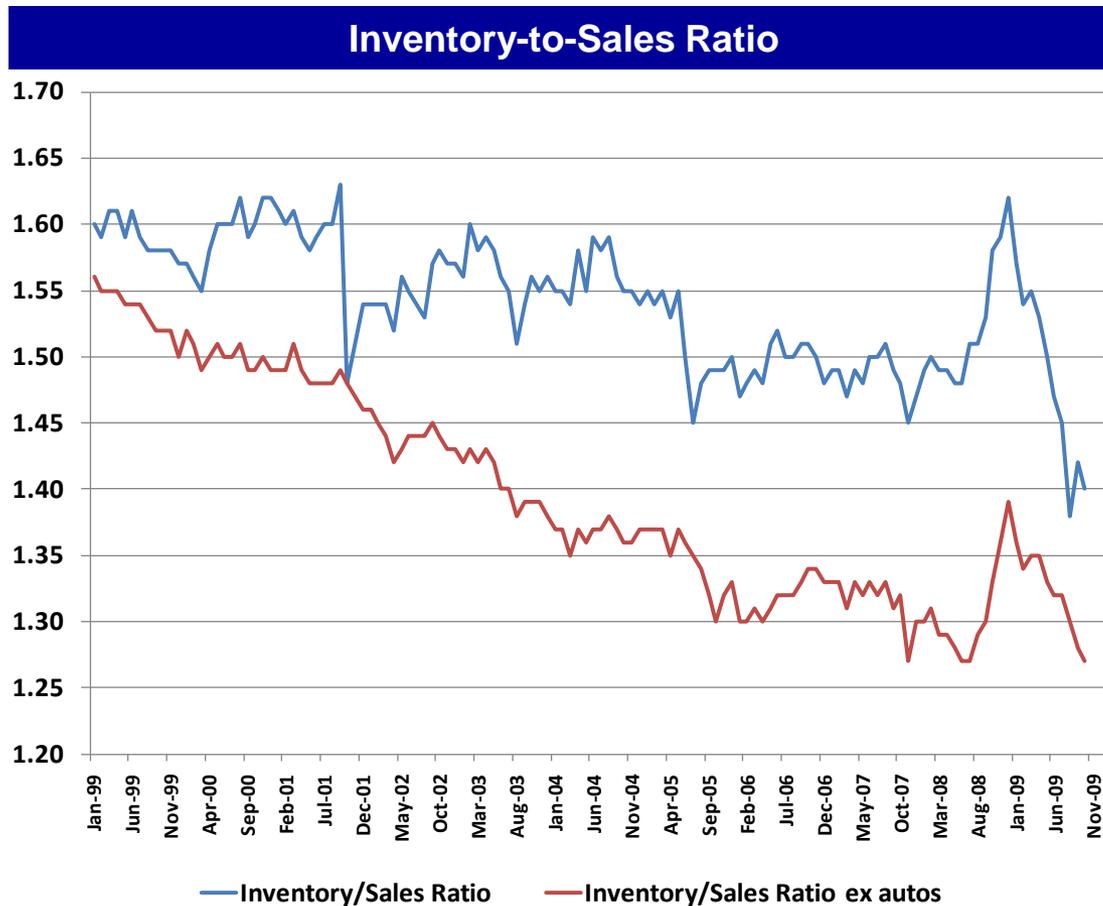
- ◆ The Fed's response has been in proportion to the magnitude of the crisis
- ◆ Bank loans could double overnight if the Fed doesn't pull back as the economy recovers
- ◆ Need to avoid too much money chasing too few goods

Early Signs of Recovery



- ◆ Unemployment insurance filings are declining and the unemployment rate will too
- ◆ Better labor market conditions will support growth in consumer spending and help the economy transition to self-sustaining growth
- ◆ The recovery will become self-sustaining when employment starts to increase, banks stabilize and if China cooperates

Excess Inventories Appear To Have Been Burned Off



- ◆ **Businesses had to reduce inventories dramatically due to tight credit conditions and rapidly declining consumer spending**
- ◆ **The inventory-to-sales ratio is closer to its trend level now than it was in Dec 2008**

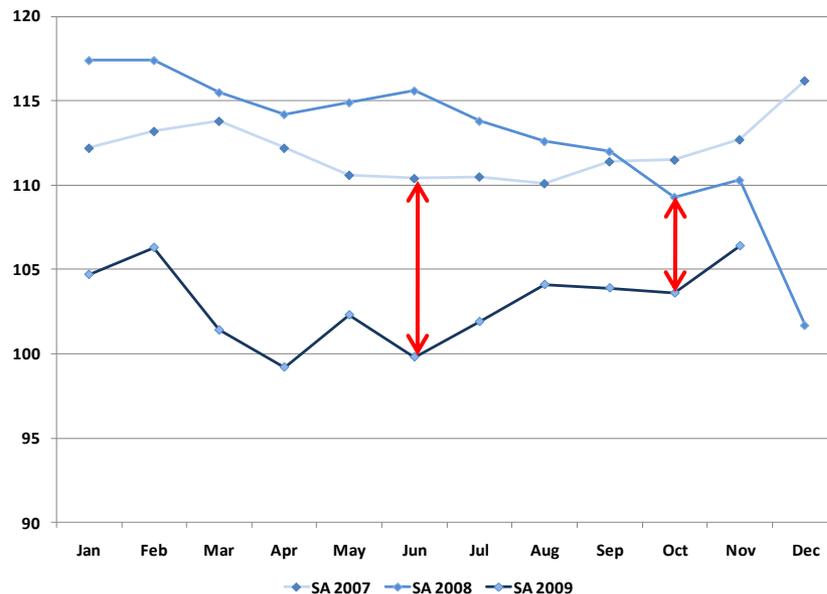


Rail and Truck Volumes Are Recovering

Intermodal Rail Volumes



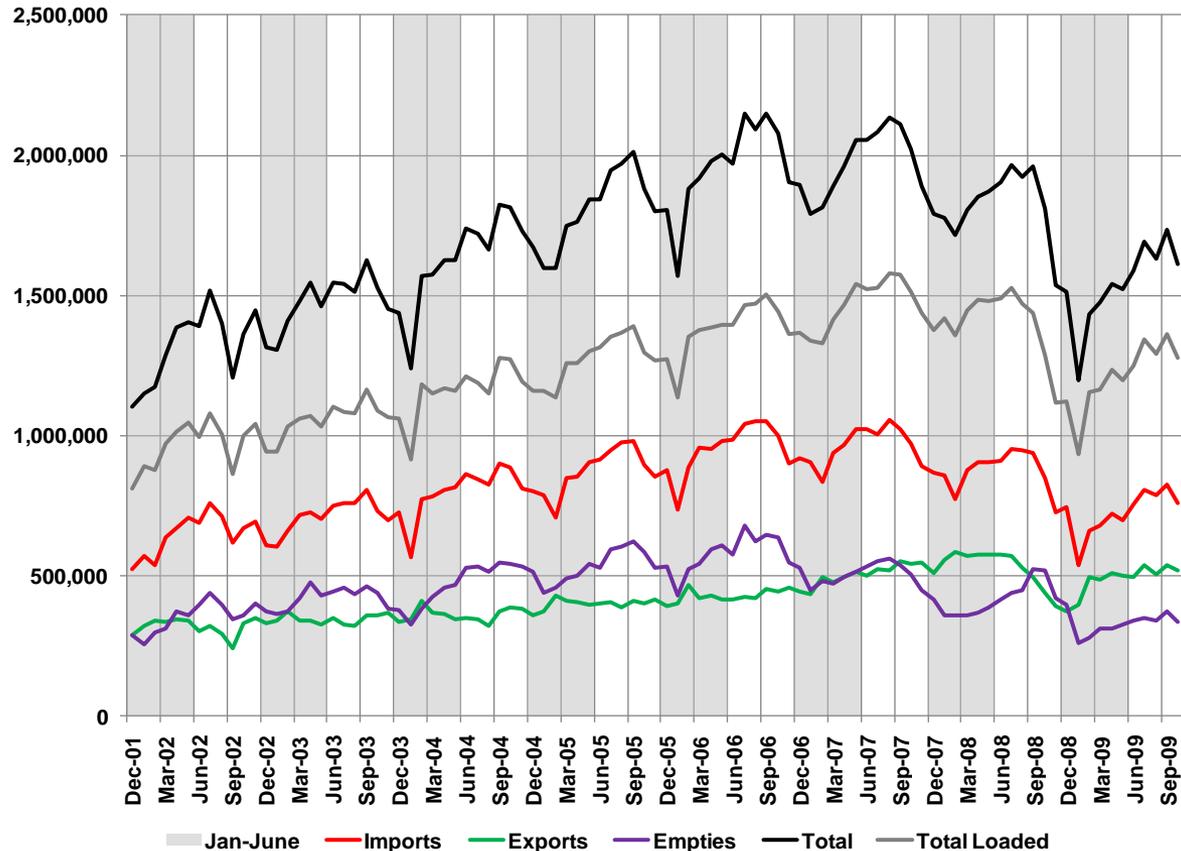
Seasonally Adjusted ATA Truck Tonnage Index



- ◆ Rail volumes bottomed in the second quarter of 2009. In the week ending December 19, total volumes were 3.8% higher than the same week in 2008; intermodal volumes were 8.7% higher.
- ◆ Year to date total volumes for the seven Class I North American railroads and KCS Mexico are down 15.8% compared to the same period in 2008 and 18.1% compared to 2007.
- ◆ Truck volumes also bottomed in the second quarter of 2009 but remain well below year ago levels

Container Volumes Recovering From A 7-year Low

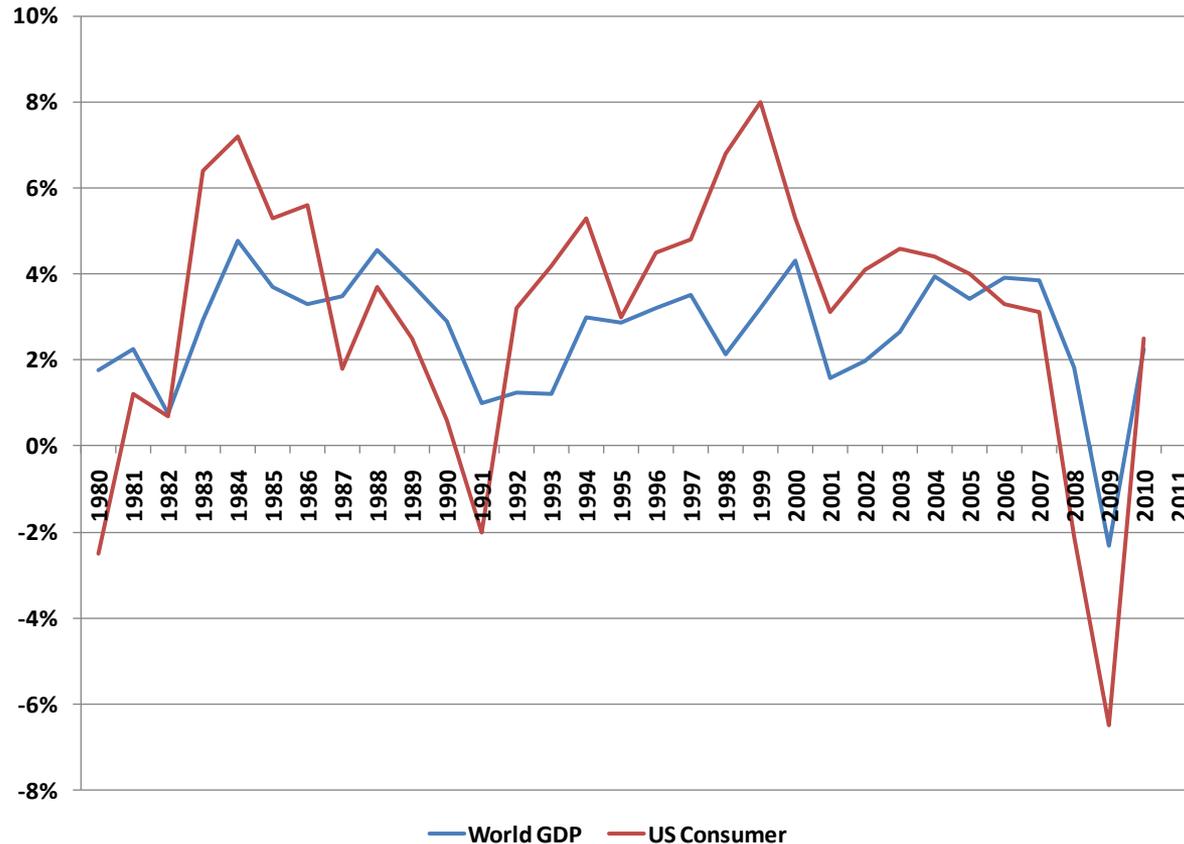
Monthly Int'l Container Volumes (in TEUs) For 6 Of The Largest US Ports



- ◆ Volumes increased 46% from the February trough through the October peak.
- ◆ Through November volumes were 15.5% below the same period in 2009 and 37% above the February trough

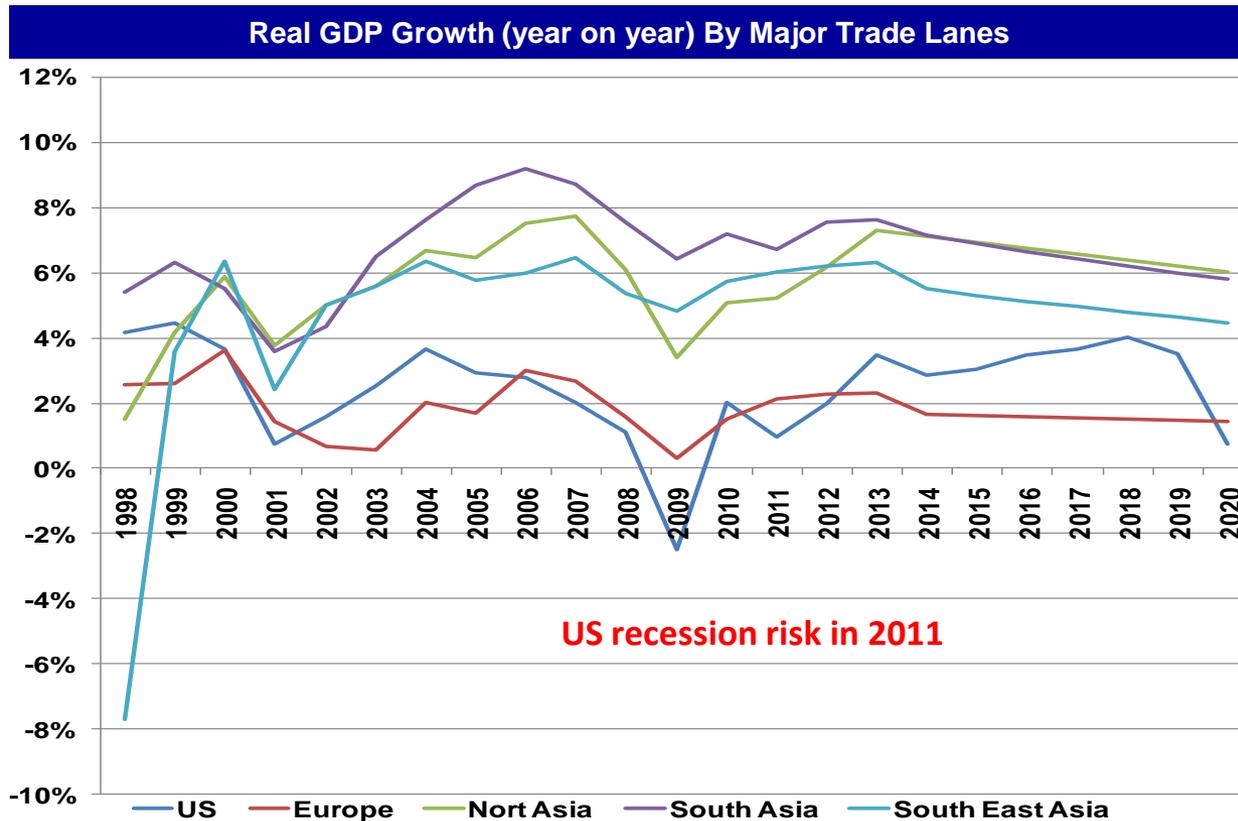
World Economy Struggles To Recover Without the US

US Consumer Spending and Global Real GDP Growth



- ◆ **The US economy accounts for 25% of World GDP, US consumers account for 17.5% of World GDP – weak US outlook underlies the below average global growth forecast**
- ◆ **In 2010 the process of weaning the global economy off policy support will begin**

Economic Outlook for Major Trade Lane Economies

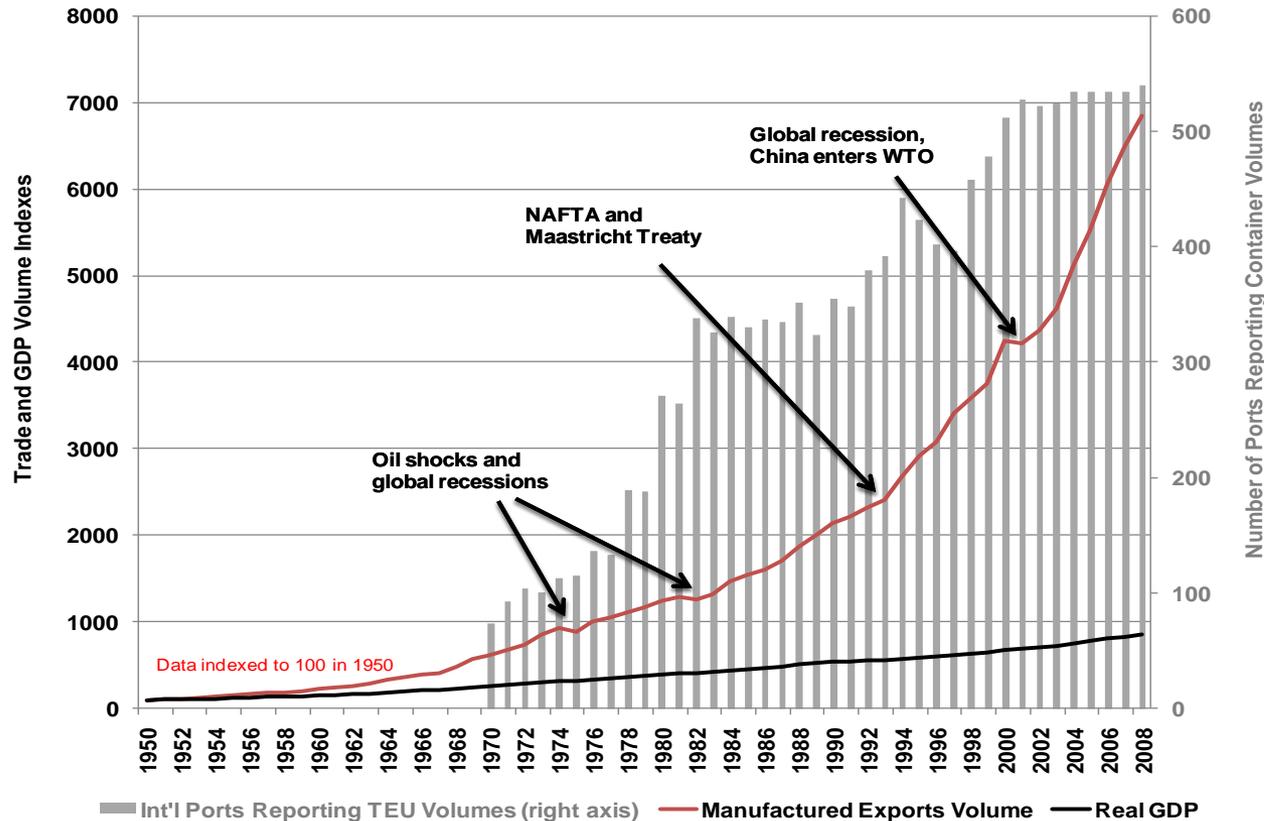


- ◆ Near term is weak due to mature economies
- ◆ Policy withdrawal creates uncertainty - look for “all clear” in 2011
- ◆ Long term outlook is more robust due to Emerging Markets trends
- ◆ World trade patterns will change due to the changing relative size of emerging and mature economies over the forecast horizon

Long Term Trends

Global Trade Has Exceeded GDP Growth

World Trade and GDP Volume Indexes



◆ **Cyclical Drivers**

Trade has grown faster than GDP

Macro shocks have not impacted trends

◆ **Structural Drivers**

Containerization; lowers freight cost

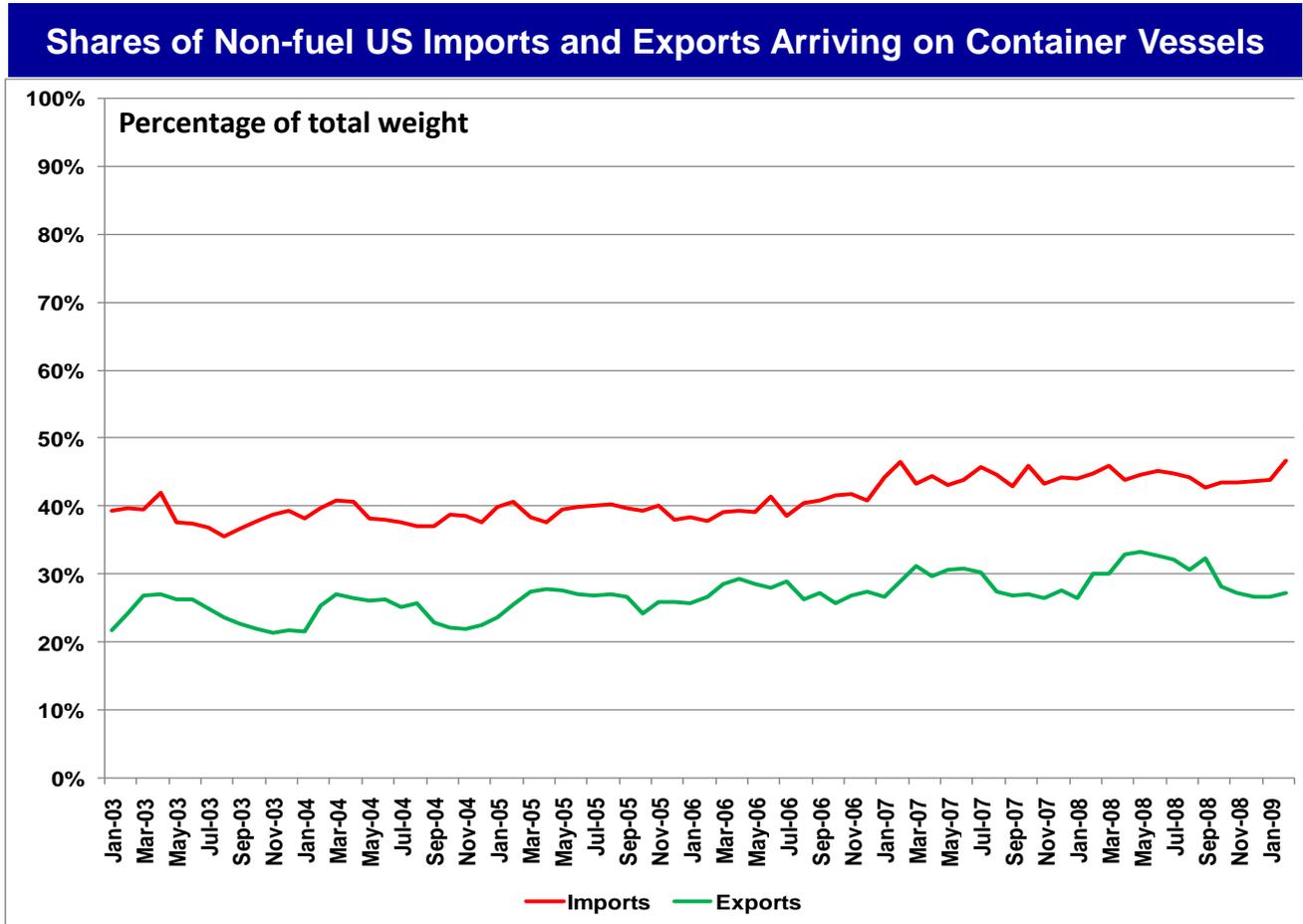
Trade Agreements; lowers trade costs

World Wide Web; allows “globalization”

Demographics; drives off-shoring/import substitution

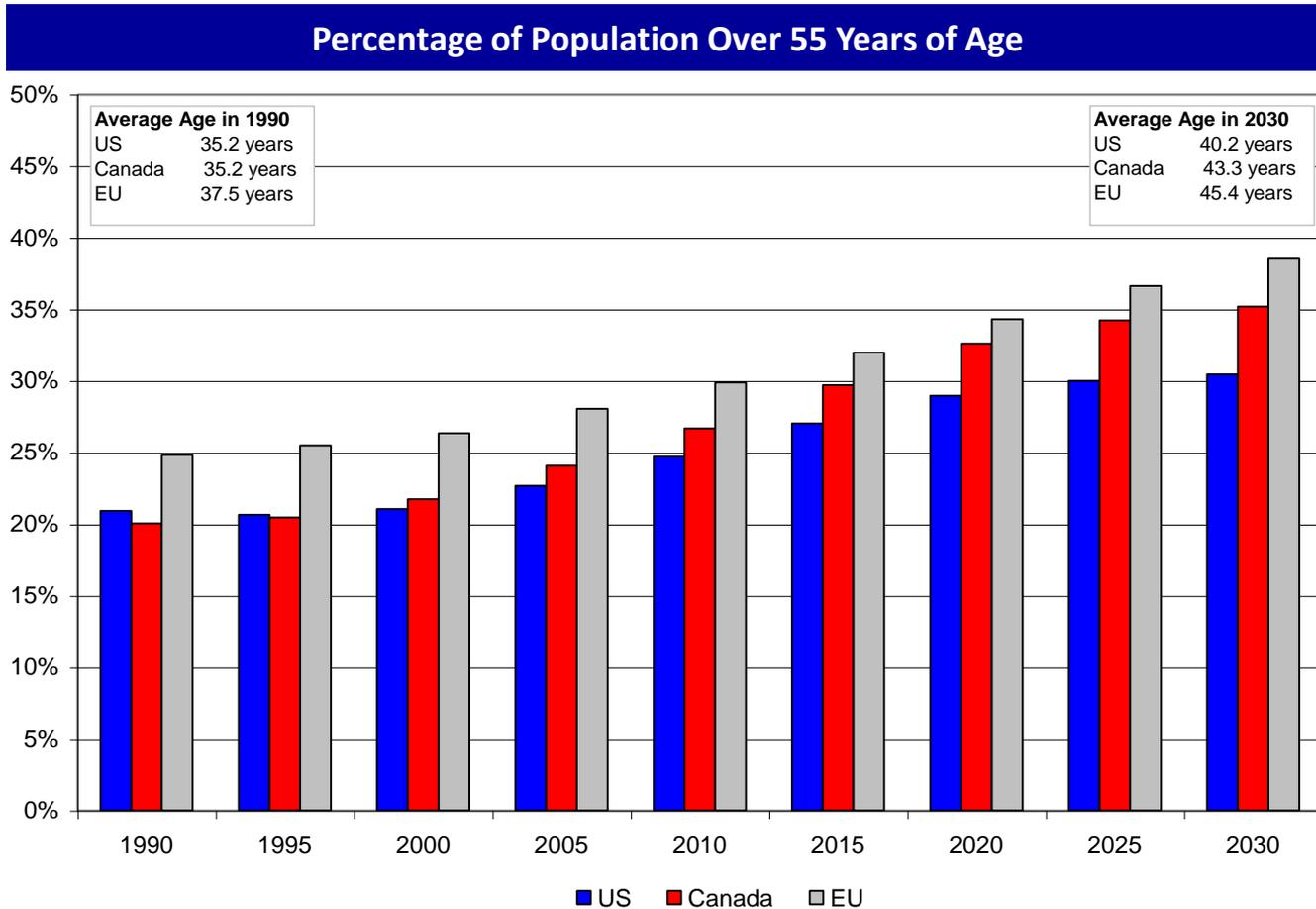
| Period | Real Exports CAGR | Real GDP CAGR | Export to GDP Growth Ratio |
|-------------|-------------------|---------------|----------------------------|
| 1950 - 2008 | 7.6% | 3.8% | 2.0 |
| 1980 - 2008 | 6.3% | 2.8% | 2.3 |
| 1998 - 2008 | 6.7% | 3.0% | 2.2 |

Containerization of Trade



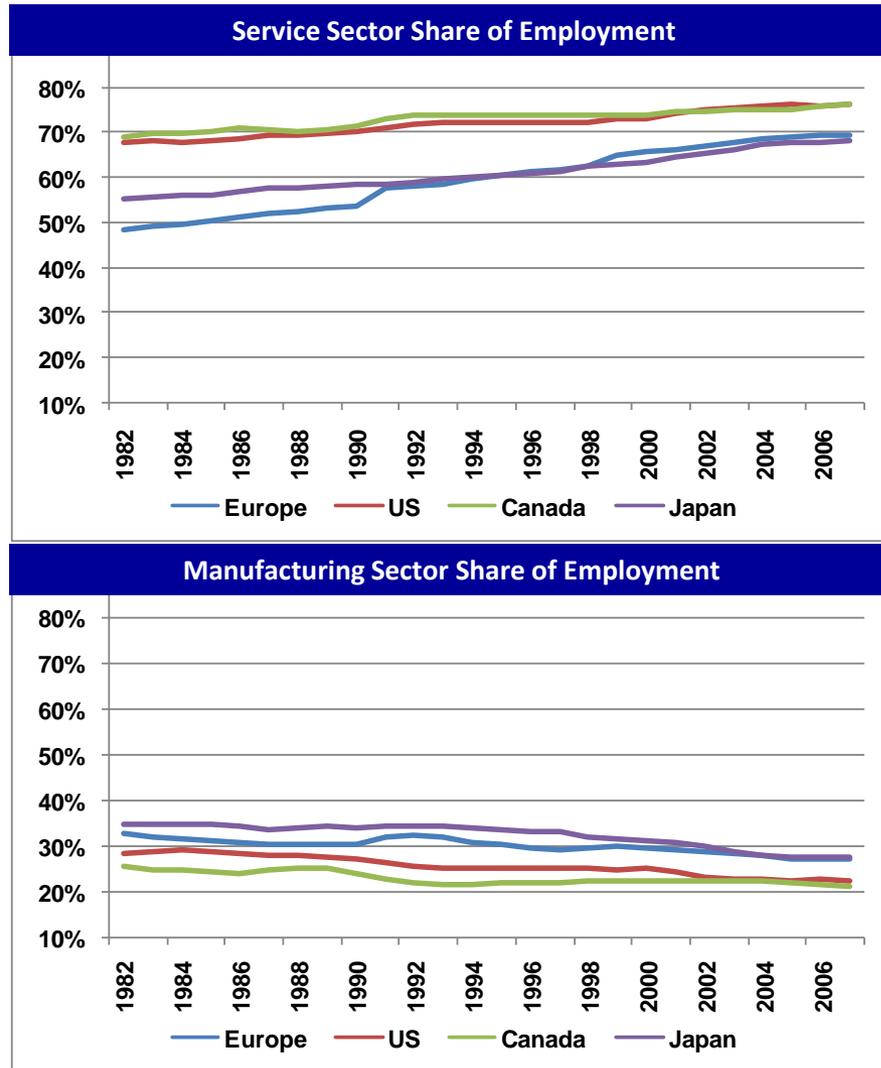
- ◆ The 8% increase in the share of imported and exported goods moving on container vessels between 2002 and 2008 represents 2.6 million additional loaded TEUs flowing through US ports
- ◆ Both import and export goods could see further containerization

Demographics



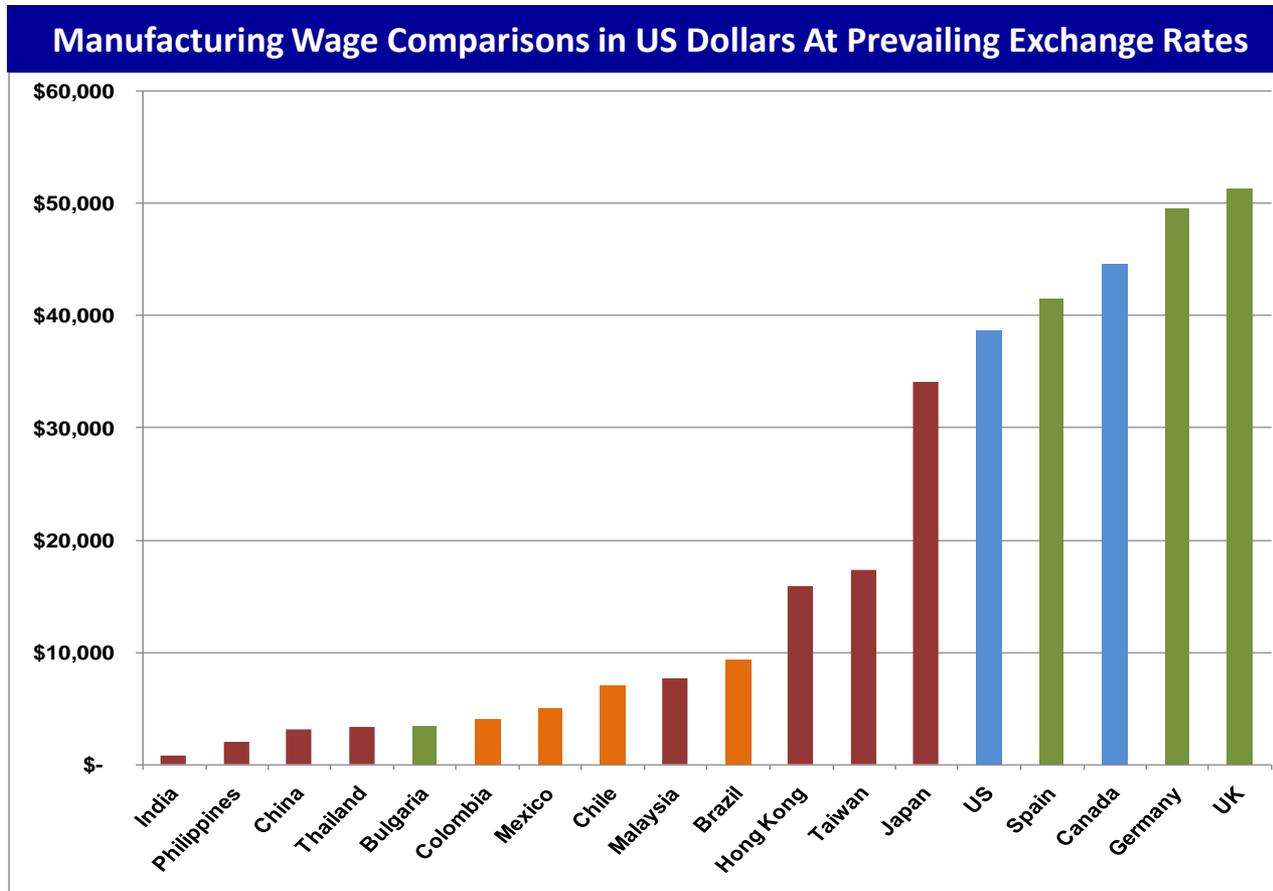
- ◆ **That industrialized nations' populations are aging is not news, but the significant rise in their elderly populations over the next 20 years will reinforce the consequences already evident in the structure of their economies.**
- ◆ **Without immigration and trade, these economies face an output shortfall**

Mature Industrialized Economies Are Increasingly Service Intensive



- ◆ Developed economies are becoming more service-intensive and less manufacturing-intensive, as a function of domestic and international demographic change

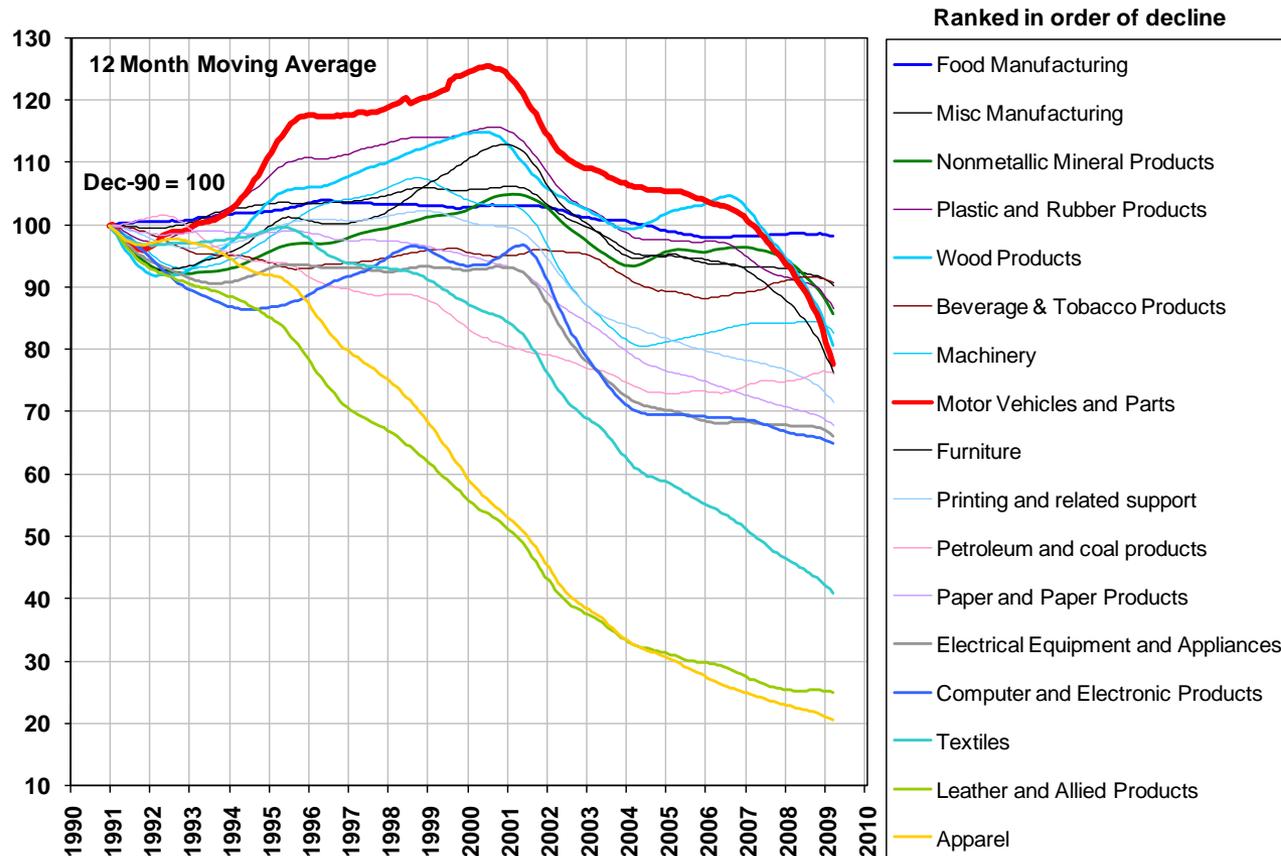
Manufacturing Industry Wage Comparisons



- ◆ **Low wages in emerging markets are partly due to their younger populations**
- ◆ **Outsourcing services maturing markets more cheaply and accesses growing markets**
- ◆ **Low wages in Latin America indicate they are prime locations for manufacturing “near-sourcing”**

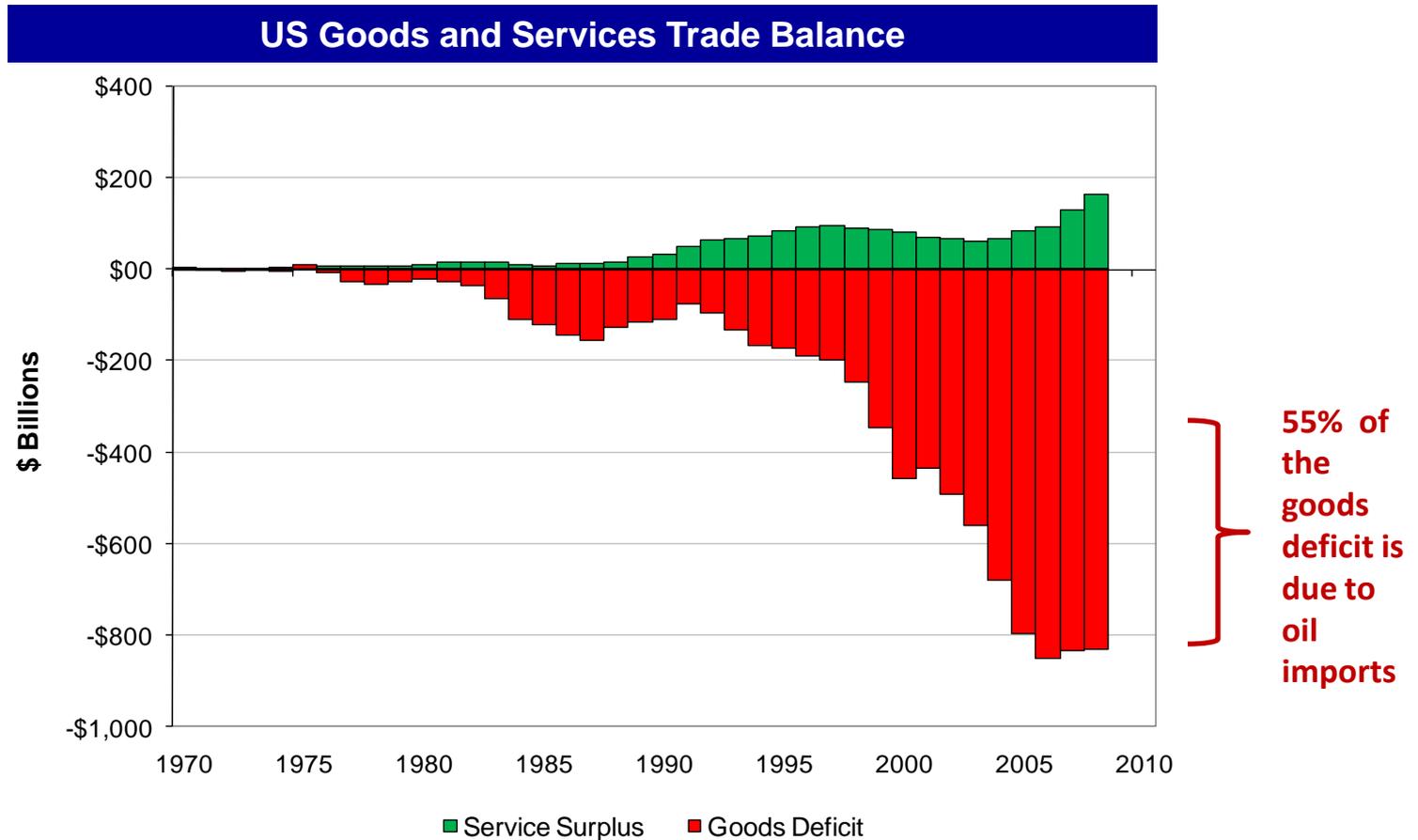
Plenty of Outsourcing Left

US Manufacturing Employment Trends By Industry



- ◆ Autos and housing-related sectors lagged other industries in terms of outsourcing due to strong demand for their products until recently
- ◆ A lot of outsourcing still to come – many industries lag the leaders
- ◆ Similar expectations have been expressed by analysts at the US Dept of Labor

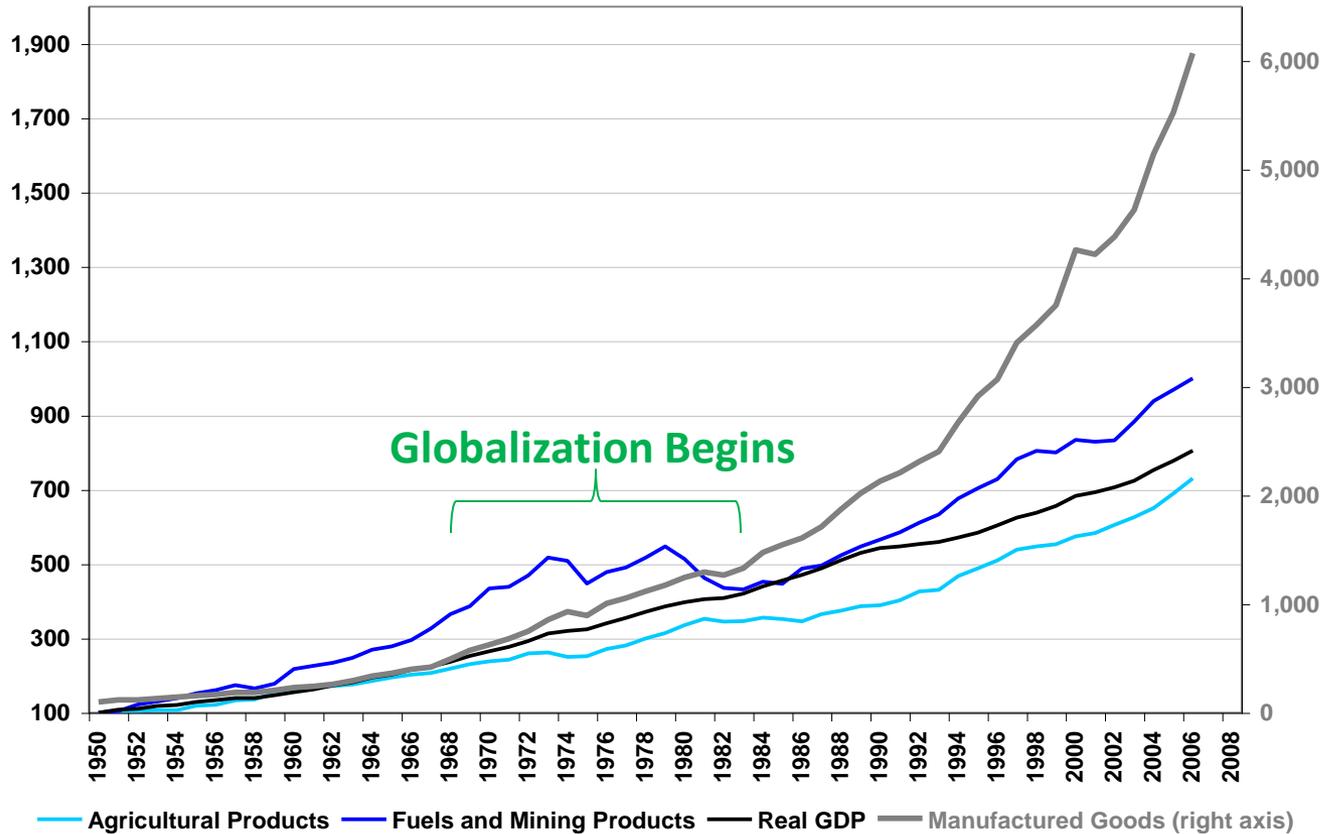
Eventually The US Will Have To Balance Its Trade



- ◆ It is unlikely that the service sector will ever offset the goods trade deficit
- ◆ The US will have to reduce dependency on fuel imports and start selling goods, or the dollar will have to decline a lot

Global Trade: Commodities Lag Manufactured Goods

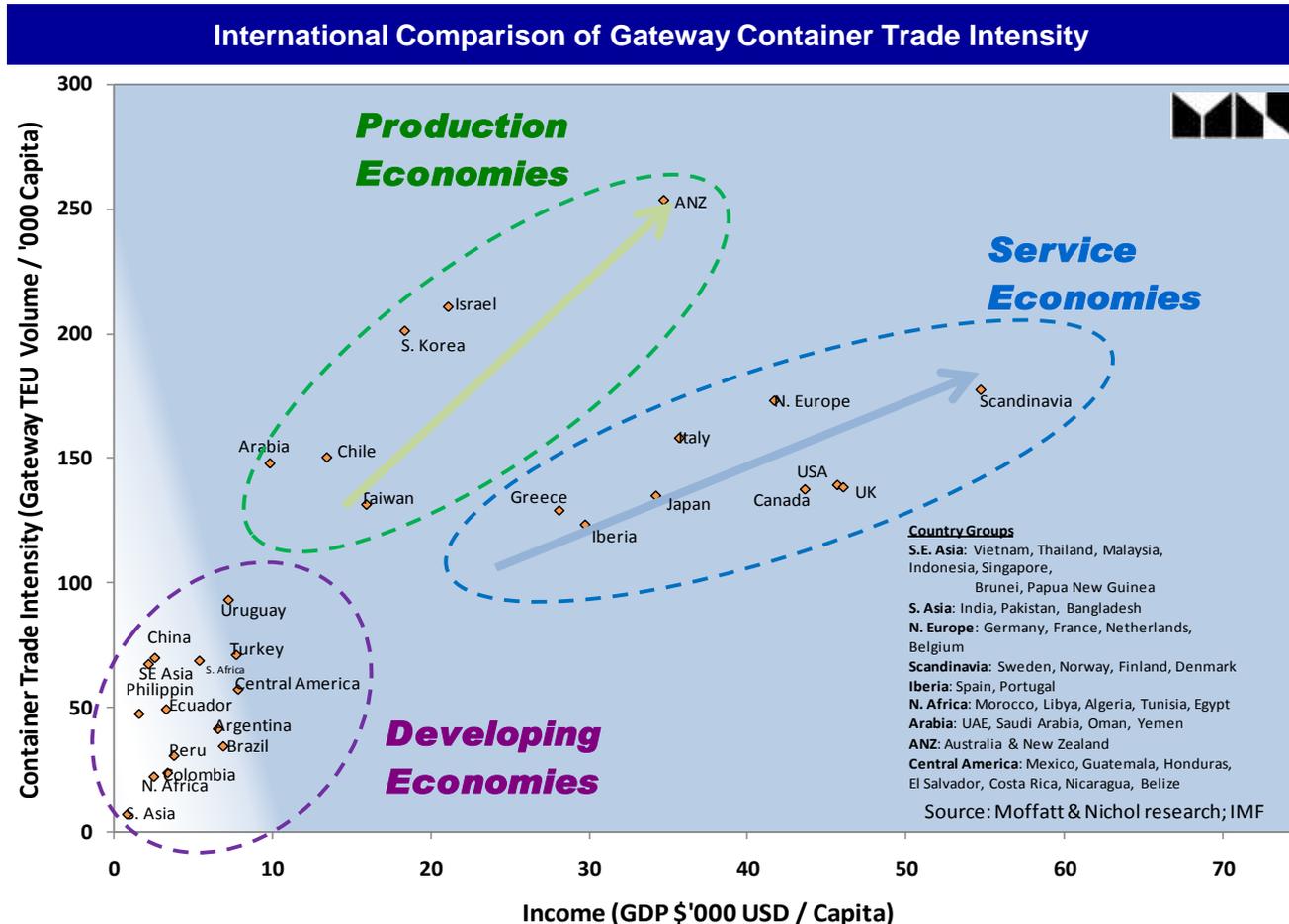
World Trade and GDP Volume Indexes



- ◆ Manufactured goods and non-agricultural products trade have grown faster than GDP
- ◆ Agricultural products trade has lagged GDP and other products
- ◆ Gap between manufactured goods and other products trade must narrow
- ◆ Bulk commodity trade depends on manufactured goods trade and other structural factors

| CAGRs Period | Manufactured Goods | Agricultural Products | Fuels and Mining Products | Real GDP |
|--------------|--------------------|-----------------------|---------------------------|----------|
| 1950-2006 | 7.6% | 3.6% | 4.2% | 3.8% |
| 1980-2006 | 6.3% | 3.0% | 2.6% | 2.8% |
| 1995-2006 | 6.9% | 3.7% | 3.2% | 3.0% |

Low Container Trade Intensity in Emerging Markets

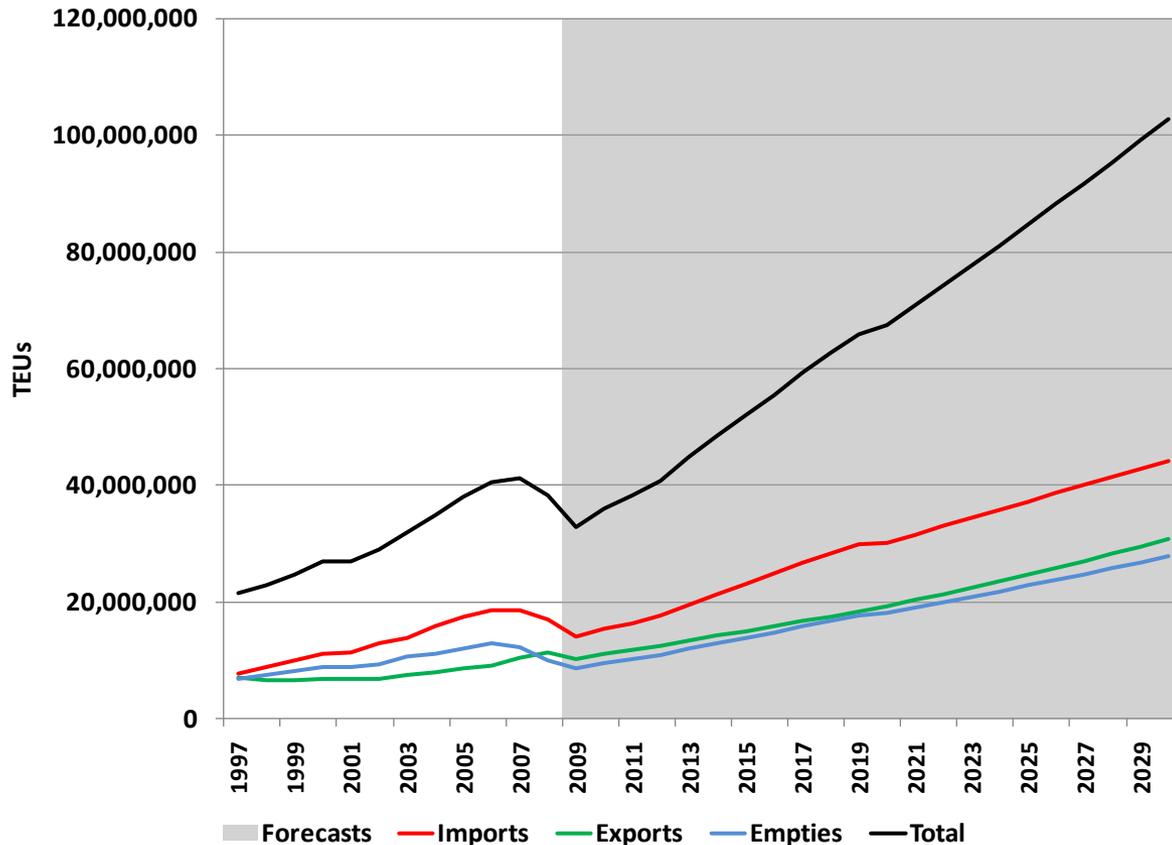


- As per capita incomes rise in developing economies and they invest in transportation infrastructure, the trade intensity of these economies will catch up with those of more developed economies
- For countries like Peru, with about 30 containers of foreign trade per 1,000 people, to close the gap with the US, which has 140 containers per 1,000 people, its volumes would have to grow 20% for the better part of a decade.

Container Trade Forecasts

Long Term Outlook For US Container Volume Trade

US International Maritime Container Volume Trade



- ◆ Global macroeconomic trends remain supportive of trade growing faster than GDP
- ◆ China is expected to moderate its currency stance and increase the consumer's share of GDP
- ◆ International policy is expected to further remove trade barriers and gradually reduce the environmental impact of economic activity

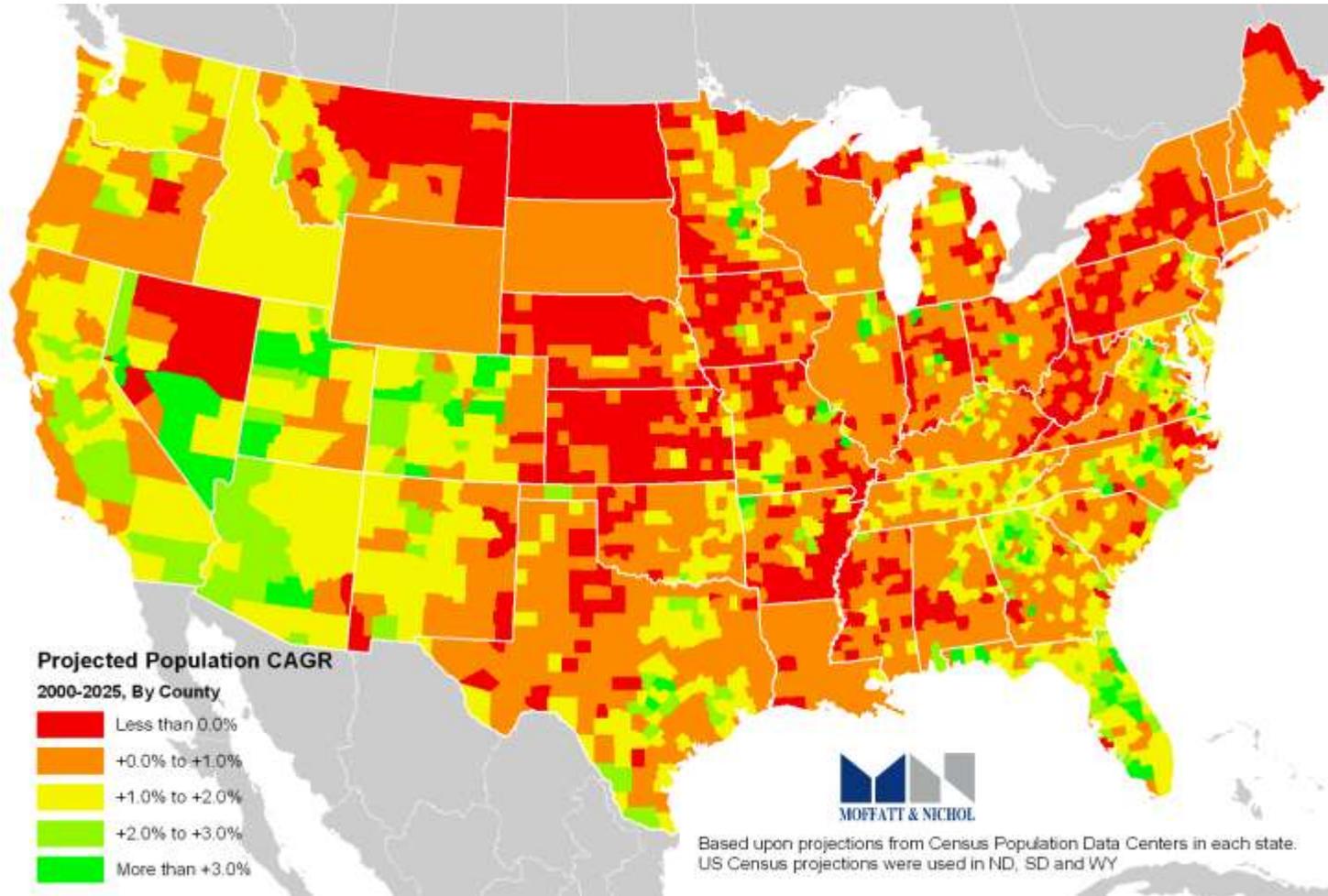
US Container Volume Trade Outlook By Trade Lane

| 2008 TRADE ROUTE | US IMPORTS | | US EXPORTS | |
|---------------------|-------------------|-------------|-------------------|-------------|
| | TEUS | SHARE | TEUS | SHARE |
| North Asia | 11,542,916 | 64% | 4,355,308 | 39% |
| South Asia | 575,977 | 4% | 298,761 | 2% |
| SE Asia | 1,600,483 | 10% | 788,903 | 9% |
| EU | 1,701,699 | 7% | 1,477,121 | 13% |
| Mediterranean | 852,215 | 9% | 687,011 | 18% |
| Middle East | 38,080 | 0% | 260,027 | 4% |
| EC S America | 417,802 | 3% | 313,498 | 3% |
| WC S America | 282,773 | 1% | 206,014 | 1% |
| Australia-NZ | 130,936 | 1% | 200,732 | 4% |
| Caribbean | 374,172 | 0% | 1,213,130 | 4% |
| Cent America | 569,303 | 0% | 530,210 | 1% |
| Canada | 6,228 | 0% | 5,960 | 0% |
| Mexico | 56,715 | 0% | 50,040 | 0% |
| WC Africa | 16,761 | 0% | 89,494 | 1% |
| S Africa | 44,175 | 0% | 55,615 | 0% |
| EC Africa | 8,627 | 0% | 21,184 | 0% |
| Other Regions | 30,951 | 0% | 62,598 | 0% |
| TOTAL | 18,249,813 | 100% | 10,615,606 | 100% |

| 2020 TRADE ROUTE | US IMPORTS | | US EXPORTS | |
|---------------------|-------------------|-------------|-------------------|-------------|
| | TEUS | SHARE | TEUS | SHARE |
| North Asia | 21,664,763 | 65% | 8,586,494 | 43% |
| South Asia | 1,329,121 | 5% | 870,992 | 3% |
| SE Asia | 3,070,658 | 12% | 1,658,495 | 9% |
| EU | 2,244,643 | 6% | 2,031,015 | 9% |
| Mediterranean | 1,176,380 | 7% | 1,182,633 | 19% |
| Middle East | 86,871 | 0% | 516,232 | 5% |
| EC S America | 826,412 | 3% | 452,912 | 2% |
| WC S America | 444,920 | 1% | 528,272 | 1% |
| Australia-NZ | 264,052 | 1% | 270,531 | 3% |
| Caribbean | 528,335 | 0% | 1,630,191 | 3% |
| Cent America | 841,942 | 0% | 780,177 | 1% |
| Canada | 12,240 | 0% | 10,074 | 0% |
| Mexico | 92,585 | 0% | 108,271 | 0% |
| WC Africa | 25,611 | 0% | 332,160 | 2% |
| S Africa | 67,109 | 0% | 125,063 | 0% |
| EC Africa | 14,906 | 0% | 73,987 | 0% |
| Other Regions | 55,808 | 0% | 79,607 | 0% |
| TOTAL | 32,746,356 | 100% | 19,237,105 | 100% |

- ◆ Latin America and South Asia have the greatest potential to surprise positively

Demographic Trends Are Changing The Economy's Structure



- ◆ **US population is moving to urban, coastal and Southern locations**
- ◆ **National container forecasts do not apply uniformly across US transportation infrastructure due to regional population and international trade lane growth differentials**

Takeaways

- ◆ **Self-sustaining recovery requires financial system stabilization and adjustment of China's policies**
- ◆ **Long term trends remain intact for imports – demographics matter more than balance sheets**
- ◆ **Bulk commodity trade could exceed container volume growth as the global economy rebalances**

***Now is the time to make investment decisions -
transportation is a “first mover advantage” industry***