

## The State of Logistics

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We see the economy slowing down on some fronts and the stock market sinking with loses in six out of the past seven weeks. The Greek debt crisis has pushed some in the US to think, "Here comes the summer of 2008 all over again". But before those who see the glass as half empty all of the time or rain on the country's economics parade, let's just pause for a moment and see how last year may impact what is happening this year.

In CSCMP's 22<sup>nd</sup> Annual State of Logistics report released this month, the report paints an interesting picture about the changes that took place in 2010 and makes one stop to think: has the economy just paused to catch our breath, or are we about to begin the backward slide again? Here are some highlights.

When we look at logistics costs in 2010 as a percent of GDP, they increased by 8.3%. Transportation costs were up by more than 10% ahead of 2009 for all modes. When you break this down, all sectors other than trucking improved by 15.5% while trucking, the largest component of transportation, improved by only 9.3%. Much of the trucking increase came from increased fuel surcharges, despite the fact that trucking capacity permanently decreased by more than 16% since 2006. Employment in the sector did increase by a meager 1.4% in 2010 after losing 13.4 % of its employees from the previous four years.

We see that supply and demand have begun to equalize as volume increased and then began to falter a bit in the second half. After an 11% decline in 2009 last year's, Industrial Production increased by 5.3 %. There were frequent peaks and valleys in freight volumes which disguised the fact that they actually grew year over year.

Although the cost of carrying inventory was low in 2010 and continues to remain low this year, we see that manufacturers have kept inventory levels very lean as a precautionary measure. Warehousing costs dropped 6% as companies chose to optimize their distribution patterns and reduce the number of warehouses they maintained. This took place as all business inventories increased all quarters except for Q2. The lack of a consistent trend here brings into focus the lack of consistent economic progress on the inventory front.

We saw a steep 21% increase in rail costs last year. US railroads have recovered some lost ground, but not all of it. Since the recovery started much of the idled equipment and employees have been put back to work, Intermodal has been the shining star in this area. Ocean saw a weak patch in the second half of last year with some surprised to see lower spots offered as ship owners were looking for more containers to fill their vessels after significant increases in 2009.

As we look out to the current and future market place we must proceed with caution. Pressure will continue to be felt by shippers from the decrease in drivers, the reduction of capacity and government regulations. Building sound relationships by shippers is a must. As shippers continue to control costs, air costs which have not rebounded will continue to be weak. Ocean shippers will benefit from excess vessel capacity for the foreseeable future, although there will be some imbalances (higher costs) on certain lane segments.

Air freight revenue increased by more than 11% in 2010. But in the second half of the year air carriers realized that their customers were not willing to pay for this premium service. This in turn moved many companies' freight back into the ocean vessels.

It looks like growth will now remain weak for the second half of 2011. New orders have begun to drop and consumer sentiment is falling. Improvements in unemployment have begun to reverse themselves. The only thing we can predict with certainty is that those who manage transportation will have a number of challenges to deal with for the remainder of this year.