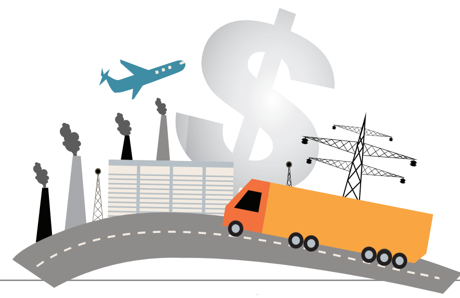
THE NEW ECONOMIC PARADIGM OF FREIGHT TRANSPORTATION



The US Economy and the US Dollar

The US economy provided a number of mixed signals in December of 2015. Unemployment is at only five percent. Economic growth, while sluggish, has been able to generate a consistent 200,000 new jobs a month. But some other indices don't look so good.

The Institute for Supply Management (ISM) PMI Index of economic activity in the manufacturing sector contracted in November for the first time in 36 months, since November 2012, while the overall economy grew for the 78th consecutive month. The November PMI registered 48.6 percent, a decrease of 1.5 percentage points from the October reading of 50.1 percent and below the 50 percent mark that signals growth. The New Orders Index registered 48.9 percent, a decrease of 4 percentage points from the reading of 52.9 percent in October. The Production Index registered 49.2 percent, 3.7 percentage points below the October reading of 52.9 percent. Ten out of 18 manufacturing industries reported contraction in November, with lower new orders, production and raw materials inventories accounting for the overall softness in November.

The US dollar, despite the pre-election buzz and the recent terrorist activity, continues to soar against other currencies. While good when it comes to the cost of imports, the high greenback slows exports and tourist visits to America.

Other countries (e.g. Canada) are not achieving the same level of economic success as the US. In a speech given on Dec. 8, Stephen Poloz, the Governor of the Bank of Canada, mused that Canada may have to adopt some stimulative measures (e.g. negative interest rates) to spur economic growth. Certainly any combination of US interest rate hikes combined with inaction or opposite action in Canada, can only serve to decrease the value of the Canadian dollar that has been dropping in recent days. Is a $0.65 to $0.70 Canadian dollar on the horizon? These changes have profound effects on freight transportation.

As the currency of the United States moves in an opposite direction, the low Canadian dollar (and the currency of other countries), will change the flow of goods between the United States and its second largest trading partner, Canada. There will also be a reduction in exports of US goods to Canada and other markets, thus injuring the American economy. Canadians are already feeling the pinch at the grocery store and in the malls of the large upswing in the American dollar.

The rise in the value of the US dollar raises questions about the reshoring movement. How long will the US dollar remain high against other currencies? Will some companies halt or revisit their reshoring initiatives? Will some sectors rethink where they locate their plants to improve the price competitiveness of their products? To balance their lanes and make money, how much will freight carriers adjust their north and southbound rates to compensate for these forces? Stay tuned in 2016.

Climate Change

News reports today are indicating that many countries will dedicate themselves to reducing their carbon emissions so as to limit the temperature increase on our planet over the balance of this century. What are the implications for the freight industry? Certainly trucks, one of the biggest emitters of carbon, will have to utilize much more energy efficient engines. This will certainly raise the cost of buying a truck and thereby raise freight rates.

Achieving reductions in fossil fuel emissions will also lead to carbon taxes and cap and trade initiatives. These will also increase shipping costs. There will be much more pressure to not just have more energy efficient engines, but to use other types of fuels that are less harmful to the environment.

The Cost of Crude Oil

The changes outlined above are taking place at a time when the cost of crude oil is below $40 a barrel and drifting downward. While very disadvantageous to North American based producers, these low costs that are partially passed on to consumers at the retail level are great for carriers and shippers. Unless OPEC changes course, we will likely continue to see low prices at the pump.

The Trans Pacific Partnership Agreement (TPPA)

Following nearly eight years of negotiations, 12 Pacific Rim countries – Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States and Vietnam – have agreed to take part in the Trans-Pacific Partnership Agreement (TPPA), a sweeping trade deal that affects some 40 percent of the global economy. The TPPA is a fundamental aspect of Washington's pivot-to-Asia policy, involving the large-scale refocusing of American corporate and military muscle within the heart of the ASEAN region. The deal aims at formulating new rules for international trade around core US strategic interests, and in the process overshadowing key functions of the World Trade Organization (WTO), a comparatively more even platform for discussing issue of global trade.

Roughly three quarters of Canada's exports are destined for the US, and the preferential relationship with its largest trading partner that was established by the North American Free Trade Agreement (NAFTA) could be lost. This deal is larger and deeper than NAFTA both in terms of the number of countries involved, as well as the range of tariff and non-tariff barriers addressed. The TPP deal must still be ratified in each member country. In Canada, the Liberal government is generally in favour of free trade but has said they need to review the details before making a decision.

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