TRADE FACILITATORS, INC.

We Can't Have Our Cake and Eat It, Too (Especially If It's Imported)

By

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Introduction

The supply chain disruptions caused by COVID-19 have introduced mainstream America to what trade professionals have known for years: The U.S. economy is over-reliant on imports and in particular, goods coming in from China. Whereas this weakness recently became news in the form of dozens of ships sitting outside the ports of Long Beach and Los Angeles, there's never been a shortage of statistics that show how precarious our trade imbalance really is.

Here are a few gems that shed light on the four-decade-long story of America's journey to import dependence:

- Over the course of the last fifteen years, the U.S. trade deficit in goods has averaged $750-$800 billion per year (we import $750b more than we export)
- Of that number, our trade deficit with China has averaged roughly $360 billion per year
- Historically, America's top exports to China (by volume) have been scrap metal and waste paper
- Ironically, none of the ships, containers or truck chassis used to import products into the United States are made here

While it is true that COVID-19 triggered the delays, cost increases and empty store shelves now hobbling America's import supply chain, what it really did was expose a fundamentally flawed system of international goods movement. Basically, factors like increased expenses, infrastructure constraints and driver shortages were around long before the Shutdown of early 2020; it just took the tragedy of Coronavirus to make these weaknesses too blatant to ignore.

Ironically, it's been cheap imports that (in part) have kept the U.S. inflation-free since the 1980's. Now, it will be supply chain price spikes that (also in part) drive inflation in 2022. Although we as shoppers have gorged ourselves on imported goods for four decades, it is the premise of this paper that when it comes to a consumption-oriented economy that doesn't manufacturer much anymore, we can no longer have our cake and it eat, too (especially if it's imported).

What does the above statement mean? It means that the U.S. should never have expected to enjoy the benefits of cheap imports without one day having our penchant for Retail Therapy come back to bite us in the behind. In the spirit of "never letting a crisis go to waste", we now have to figure out how to reap the economic advantages of importing while addressing our systemic weaknesses.

It is within the above framework that the balance of this article endeavors to a) shed light on our real supply chain flaws b) offer insights into the role that supply chains play in inflation and c) make some “Moon Shot” suggestions on how to fix a series of seemingly unrelated problems, all of which are way more important than little Johnny getting his PlayStation in time for Christmas.

A chain is only as strong as its weakest link, but what if all the links are weak?

As noted above, COVID-19 exposed a number of supply chain weaknesses that have been accumulating for decades. Whereas the average consumer wouldn’t necessarily know about these problems, folks that work in global trade have been well aware of them for a long time.

Here’s a quick summary of what those issues are:

- The absence of a national port, airport, rail & highway infrastructure strategy, along with minimal investment in said infrastructure over the last fifty years served as a slow-burning catalyst for the physical world constraints we’re experiencing now
- With the advent of Mega Ships that carry more than 20,000 containers, port congestion has been “a thing” for a good while now (especially when multiple ships berth all at once)
- The shortage of port and rail drayage drivers started two decades ago with the tightening of post 9/11 port security requirements (driver vetting reduced their numbers)
- Much needed thresholds that were placed on the emissions of older trucks (beginning in the early two thousands) restricted the number of tractors that provide port/rail trucking
- Container chassis imbalances started in the 2010 time frame when the ocean carriers stopped providing chassis for use by the import/export community
- In addition to trucker shortages, there has been a paucity of logistics workers entering the market for well over twenty years
- After 24 months of supply chain chaos, a number of seasoned logistics professionals are burned out and leaving the industry, thus weakening the logistics workforce even further
- Due to the ocean carriers’ reluctance to allow import containers to be transported to inland U.S. destinations, exporters in non-coastal areas have had major problems in securing containers for their exports
- A union-driven refusal to adopt port terminal automation in-line with the productivity of other nations hasn’t helped any
- The inability and/or unwillingness of the trade community to adopt technology standards that enhance supply chain visibility and goods flow has finally come home to roost

Inflation Nation, what’s the explanation?

With no inflation in the U.S. since the mid-to-late 1980s, it’s safe to say that the price hikes of 2021 are tied to COVID-19. With that said, and not unlike the aforementioned drivers of supply chain disruption, many of the ingredients for this inflationary recipe have been in play for a while now. Of equal importance, these are not independent variables; they interact to create a vicious cycle of cost increases that as of right now, show no sign of abating.

Here is a list of what those intertwined and mutually enabling inflationary causes are:

- Part of the U.S. inflationary tale can be attributed to increases in the money supply born of multiple Federal and state COVID-19 stimulus packages
- Tied to the above is the huge increase in demand for all types of goods during the Pandemic (most of which are imported from Asia)
- Ironically, the product scarcity caused by supply chain constraints and delays has driven up prices, as well
- While an old school explanation, there is a "Wage/Price Spiral" in the mix whereby the pay increases necessary to attract people back to work compel employers to raise prices for their goods and services, which in turn means that workers need another raise to keep pace with inflation…and so goes the upward spiral
- Due to increases in raw materials, labor and industrial real estate in China, the cost of importing goods from "The Middle Kingdom" has increased dramatically over the last fifteen years
- The Section 301 Tariffs of 2018, more commonly known as the "Trump Tariffs", made the importation of goods from China 25% more expensive (BTW, the Chinese NEVER paid these tariffs, it was always the U.S. importer picking up the tab)
- Consolidation in the ocean carrier business limited the number of service providers and as such, pricing options for shippers decreased (the Top 5 steamship lines have 65% global market share)
- Ocean transport from Asia to the U.S. spiked fifteen-fold in the last 18 months, often times making shipping costs more expensive than the value of the goods in a container
- The ocean carriers continue to (legally) maintain artificially high rates by manipulating the number of vessel sailings from Asia to the U.S. (via cancelled or "blanked" sailings)
- Ocean freight congestion has compelled importers to turn to air freight, which of course, also went up dramatically during COVID-19
- In addition to out-of-control air and ocean freight rates, rail and truck charges in the U.S. have seen similar increases
- In 2021, a "Me Too" mentality emerged in the logistics industry, where every service provider, from container stripping to warehousing and last mile delivery firms, raised their rates for the simple reason that they could

Supply Chain Disruption & Inflation: How Much Longer?

While nobody knows for sure, this author believes that there are five mutually enabling factors that indicate supply chain disruption and inflation will be around for all of 2022, and well into the foreseeable future. Consistent with a recurring theme throughout this paper, these are not stand-alone causes; they interact and conspire to perpetuate a self-fulfilling prophecy of ongoing disruption and increased costs. Here's what they are…

Supply chain disruption will be here for as a long as Coronavirus is. With over a dozen parties involved in an international transaction, supply chains depend on a reasonable flow of goods between those parties. Although there will always be some problem or delay to be fixed, supply chains were never meant to absorb the stops, starts, lulls and surges triggered by COVID-19. As such, supply chain disruptions will be around for as long as "COVID-X" is.

Climate Change. Incidents of supply chain disruption tied to Climate Change were happening years ahead of Coronavirus. Whether it was wild fires or massive snow storms shutting down highways, or an inordinate number of containers being lost at sea due to huge, wind-born waves, Climate Change is no stranger to supply chain disruption.

Fast forward to the COVID Era and just by looking at events like the vessel “Ever Given” being blown sideways into the banks of the Suez Canal, or the port of Vancouver being cut off from its rail connections due to flooding in November of 2021, it’s a lock that Mother Earth has a lot more high jinx in store for all of us.

As if Climate Change disruptions weren’t enough on their own, it will be when these events combine with COVID-born problems that things will really get tough. For example, a shut down in one country, when ill-timed and intertwined with an unforeseen Climate Change event in another, will twist things up in ways we’ve yet to envision.

High product demand and unstable supply chains don’t bode well for normal operations. Yet another irony of the COVID Era is that there has never been greater demand for imported goods, but the Asia-U.S. supply chain is at its most unstable point ever. When more and more goods continue to pour into a flawed system, instability is a guarantee, so expect this aspect of disruption to last throughout 2022. Even if consumer demand tanks in 2022, it will take six months to clear up the residual mess.

What the heck is “Front Loading”? When importers don’t trust their supply chains, they start to order merchandise from their overseas vendors sooner than needed, and in greater quantities (known as “Front Loading”). A classic case of Herd Behavior, when importers start to front load in mass, the pressure builds on the supply chain, thus perpetuating our now infamous vicious cycle of disruption and inflation. With retailers placing orders on Asian suppliers for Back-to-School 2022 in Q4 of 2021, front loading is in full swing, right now.

Manipulation of vessel supply by ocean carriers will keep rates high. After nearly two decades of billions of dollars in losses, the steamship lines have made the best use of their “Alliances” to band together and cut the supply of vessel sailings in the Asia-U.S. trade lane. Perfectly legal by Federal Maritime Commission rules, the alliances will continue to blank sailings throughout 2022 in order to control the supply of containers, thus maintaining rates at artificially high levels.

We can’t have our cake and eat it, too, so what can the U.S. possibly do?

As we begin to wind down this paper, it must be emphatically stated that in and of itself, access to cheap imports is not a bad thing. Quite the contrary, an advanced economy like the U.S. has to import goods that are too expensive to make domestically, while exporting technologically advanced products that can be sold at a premium (think Germany).

Our problem with imports is actually two-fold, a brief summary of which sets the stage for the solutions that will be presented in a moment. First, and as already stated, we’re too dependent on goods coming out of Asia and in particular, products of Chinese origin. Also, China has geo-political aspirations that aren’t exactly aligned with those of the U.S. and in the end, the importation of their products serves to fund those objectives.

Second, and beginning in the late seventies, the U.S. sent entire industries overseas without ever developing the above mentioned advanced export sectors. Actually, when one nets out recyclables, military hardware and agricultural commodities from trade statistics, we hardly export anything. This acute trade imbalance not only contributed to the disruption we see today, it has decimated high-end job creation and wage growth for the middle class.

With all that said, the remainder of this article is dedicated to presenting Moon Shot suggestions for how we can alleviate our import issues, all while addressing other problems that are of equal, if not greater consequence. By way of explanation, they're called "Moon Shots" because each of them is rife with complications of their own, they're generational in time span and require a level of resolve and collaboration that is in short supply here in the U.S.

Let's start off with a reiteration what's already been stated multiple times:

- The U.S. is over-reliant on imports from China
- China has geo-political aspirations that are not aligned with those of the U.S.
- The costs associated with importing from Asia are unsustainable
- Much of America's supply chain congestion is concentrated on the W. Coast, especially in the ports of Long Beach and Los Angeles
- There is a nation-wide labor shortage for truck drivers, as well as logistics workers of all kinds

Now, we're going to introduce some variables to the equation that at first glance, seem far removed from our supply chain challenges:

- Nobody knows the real number, but it can be said that there are millions of people living in the U.S. illegally, the majority of whom are our brothers and sisters from Latin America
- We have a humanitarian crisis at our southern border, with thousands of Latinos walking over 1,000 miles in the hopes of being allowed into the U.S.
- The U.S. has Free Trade Agreements (FTAs) with several countries in Latin America including Mexico, all of Central America, Dominican Republic, Colombia, Peru and Chile

Based on the above facts, what would happen if we did the following?

At the Community College level, create two-year apprenticeship programs in supply chain management & logistics. Although there are universities in the U.S. that offer four year degrees in supply chain & logistics, there aren't many two year programs for more operationally oriented positions. The U.S. should take a page out of Europe's book and fund a national Logistics Apprenticeship Program (run locally by community colleges) that not only provides academic training, but apprenticeships with established firms.

Without a doubt, this is a great avenue for getting more people into the logistics industry with good paying jobs. As a result, the productivity gains from having professionally trained people in the transportation & logistics workforce would help speed up the flow of goods, both internationally and domestically.

Offer amnesty to people that are in the country illegally in exchange for working in trucking & logistics. With an estimated shortage of 80,000 truck drivers and thousands of open positions in the broader logistics industry, why not offer immigration amnesty to folks here illegally, in exchange for a commitment to work in the logistics space?

Of course, there would have to be a rigorous vetting/training program that includes ESL certification (English as a Second Language), qualification for a CDL (Commercial Driver's License) and TWIC (Transportation Worker's Identification Card), but this type of program would get many people out of the Shadow Economy and convert them into tax paying citizens.

One might imagine that the trucking & logistics industries would be more than happy to participate in some type of Sponsorship Program, potentially paying any "amnesty tax" levied against participants to account for their prior illegal status.

Encourage U.S. importers to take advantage of existing Free Trade Agreements with countries in Latin America. The U.S. will never solve its crisis on the southern border by turning people away once they show up in places like Nogales and Reynosa. We would be much better served if we helped to create a safe environment in their home countries where they didn't feel forced to leave. In other words, if people felt safe, had a decent job and a modicum of hope for a better future, they'd be more likely to stay home.

Stated above, the U.S. has FTAs in place with Mexico, all of Central America, Dominican Republic, Colombia, Peru and Chile, which means that there is reciprocal duty free treatment on goods imported and exported to/from all of these countries. If U.S. importers were able to shift their sourcing of goods to these countries, there would be no import duties, transportation costs would be less than half of those from Asia and transit time would be reduced by 60%.

In what would clearly be a virtuous cycle, not only would U.S. importers (and ultimately U.S. consumers) enjoy all of these benefits, but over time, job creation would compel folks to forego the walk to the U.S. border and gladly stay put in their home country.

Further incentivize U.S. importers to source products in Latin America. Free Trade Agreements with countries like Mexico and Guatemala have been in place for years and admittedly, FTAs (by themselves), have not created the number of jobs needed for people to remain in their countries. For reasons that include limited production capacity, shoddy infrastructure, organized crime and bad education systems, many importers simply don't feel confident in sourcing product from these nations.

With the U.S. government already pouring billions per year in aid to countries in Latin America, we might consider redirecting those funds to areas that help to build an industrial base and strong workforce. Also, we could further incentivize U.S. businesses to invest in Latin America by offering companies tax credits from the IRS. While it might sound like yet another corporate give-away program, the net effect would actually benefit us.

After reading the above suggestions, it should be clear to the reader why they're called Moon Shots. Unrealistic? Yes. Likelihood of being implemented? Low. But here's the deal…if we think that our supply chain woes will go away by ocean ports charging importers a penalty for leaving containers on a terminal for too long, or by having the Federal Maritime Commission "investigate" unreasonable charges by the container lines, it's already game over.

So, why not shoot for the moon? Why not think big and try to kill two (or more) birds with one stone? As it stand today, we're attempting to address the *symptoms* of an illness, as opposed to the *sickness* itself, and it's high time we made some bold moves to deal with our underlying systemic troubles.

Closing Comments

Hopefully, this article has made it clear that our supply chain maladies have been brewing for decades, but that it took a Black Swan event like Coronavirus to expose and amplify those flaws. While these disruption and inflation-causing factors are real and have to be dealt with in the short term, the underlying issue is that the U.S. is over-reliant on imports from Asia, with nearly 50% of those goods coming from China.

In spite of the above, it was NEVER the intention of this article to state that the U.S. should stop doing business with China. An entirely absurd notion, the fact is that we need China for its ability to manufacturer a broad range of increasingly complex products at a competitive price. Also, the relatively few U.S. companies that do export to China need access to the market, so let's just say that China should stay in the game, but that its playing time needs to be cut.

What this article unapologetically states is that the U.S. needs to DIVERSIFY its sources of imported products. There's a reason why most of America's import delays are found on the West Coast, and that is because the majority of our consumer goods come from Asia. For anyone that doesn't believe that statement, think about it this way…

The ports of Los Angeles and Long Beach rank worldwide as the 17th and 22nd largest ports, respectively. As America's #1 maritime complex, LA/LB has ships coming in from nine of the ten biggest ports in the world (seven are in China, the other two are Singapore and Busan). With that level of activity, LA/LB is really a giant funnel that, on its best day, has trouble handling so many containers. Throw COVID-X into the mix and we've all seen how that story goes.

If importers source more goods from Latin American nations that have FTAs with the U.S., a couple of things can happen. First, and most obviously, we'll reduce our reliance on Asian imports and as a result, costs will go down. Next, we'll take pressure off the W. Coast by utilizing ports like Laredo, Tijuana, Houston and Miami. Finally, and here's the Moon Shot, there is an opportunity to at least partially stem America's immigration disaster by building supply chains that will keep people at home.

When John F. Kennedy challenged America with his "Moon Shot" speech of May 5, 1961, the goal was to put a man on the moon by the end of the decade. While certainly a more terrestrial matter, we should now challenge ourselves to design supply chains that facilitate both imports and exports, all while helping our brethren in Latin America. After all, let's not forget what JFK said in his Inaugural Address of January 20, 1961…

"…To our sister republics south of our border, we offer a special pledge to convert our good words into good deeds, in a new alliance for progress, to assist free men and free governments in casting off their chains of poverty…"

If we live up to JFK's pledge, we just might be able to have our cake and it eat, too, and when that cake is imported from Latin America, let's hope it's a giant "Tres Leches"!

Dan Gardner Profile

Dan Gardner is president of Trade Facilitators, Inc. (TFI), a Los Angeles based consulting firm dedicated to the fields of global supply chain management, logistics and trade compliance. Prior to founding TFI, Dan worked in the 3rd Party Logistics industry where he held senior roles that include President of Latin America for Exel Global Logistics, President of Ocean World Lines and SVP USA with DHL Global Forwarding.

Over the course of his career in 3rd Party Logistics Dan was directly involved in twelve acquisitions, the largest of which was the $7b sale of Exel Global Logistics to the parent company of DHL, Deutsche Post. Dan was also part of the management team that sold ATC Logistics & Electronics to Genco (later acquired by FedEx).

Mr. Gardner's activities at TFI focus on consulting with Beneficial Cargo Owners, as well as providing strategic, operational and commercial advice to technology startups in the logistics and supply chain space. Dan also serves as Chairman of the Advisory Board for STG Logistics, the largest bonded Container Freight Station operator in the U.S.

In addition to his professional experience, Dan has been an adjunct professor of supply chain management his entire career. In 2002, Mr. Gardner was selected as the Professor of the Year in the Masters of International Business Program at Florida International University and in 2014 he earned the "Top Instructor" distinction at the California State University Long Beach Center for International Trade & Transportation. Dan remains on the faculties of CSULB, Georgia Tech and Long Beach City College.

A native of Lynn, Massachusetts, Mr. Gardner holds an MBA from the University of Miami and is a licensed U.S. Customs Broker. Dan has also been certified in Production & Inventory Management (CPIM) by The American Production & Inventory Control Society (APICS), holds a Black Belt in Six Sigma and earned a certification by the American Society for Industrial Security (ASIS) as a Physical Security Professional.

During his career, Dan has travelled to over fifty countries, having lived in Colombia and Mexico for a total of five years. He can be reached at dgardner@tradefacil.com.