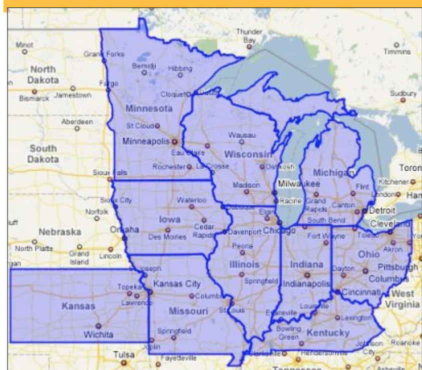
MISSISSIPPI VALLEY FREIGHT COALITION

Freight Notes

The Newsletter of the Mississippi Valley Freight Coalition

NATIONAL CENTER FOR FREIGHT & INFRASTRUCTURE RESEARCH & EDUCATION
CFIRE



From the Editor:

I am pleased to be back with the University of Wisconsin and the Mississippi Valley Freight Coalition. One of my goals is to improve the communications within the Coalition. This newsletter is one of the tools that I will use in that effort. It will be issued at least quarterly, or whenever something noteworthy occurs.

Ernie Wittwer

In This Issue:

Coalition Reauthorized

A their July meeting in Kansas City, the CEOs of the ten states of the Mississippi Valley Departments of Transportation unanimously voted to reauthorize the Mississippi Valley Freight Coalition (MVFC). The Coalition will continue as it has been for the past two years. Its two-year budget will be about $750,000, two-thirds provided by the states and one-third provided by the National Center for Freight and Infrastructure Research and Education (CFIRE).

The budget will support six projects:

Outreach Materials: This project will develop and disseminate outreach materials and media kits to promote awareness and understanding of freight operations and to communicate the importance of freight and multimodal networks for the economic competitiveness and well-being of the region.

Regional Recommendations for Reauthorization: In this project we will develop broad policy level recommendations on federal transportation reauthorization. The message will outline the uniqueness of the region and its transportation needs.

Transportation Profiles for MVC Commodities and Industries: Here we will focus on selected key agricultural and industrial products to demonstrate the flows of commodities in the region.

Performance measures for evaluating multi-state projects: Building upon measures being developed for other multi-state alliances and interstate corridors, this effort will develop measures related to freight that can be used to help evaluate regional efforts.

Resiliency of Freight Corridors in the MVFC: In this effort we will identify key nodes and sections on the MVFC freight network and then assess the impact of lost capacity of these key facilities.

Member Services for the MVFC Pooled Fund Activities: This project contains ongoing services to the Coalition: meetings, websites, newsletters, etc.

We welcome your involvement in the projects and other activities of the Coalition. One very good way to become involved is to volunteer to be a member of a project advisory committee. Each project will have such a committee, made up of knowledgeable people from states, MPOs, industry or academia. These committees provide ongoing guidance to the research teams, review draft materials and offer ideas. If you would like to be a part of a committee, please contact me (Ernie Wittwer) at the address on the last page.

Thank you for your support!

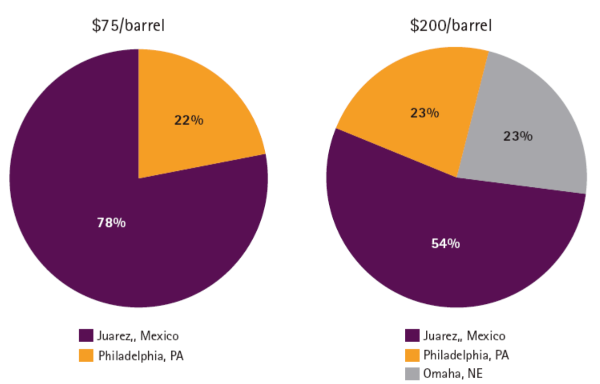
The Impact of Fuel Prices on Freight and Logistics

The price of crude oil has been bouncing between $120 and $150 per barrel for the past several months. Diesel fuel has followed, fluctuating between $4 and $5 per gallon. A $10 per barrel increase in the price of crude, results in about a $0.24 increase in the price of diesel. With the standard fuel surcharge, this in turn becomes a $20 increase in a five hundred mile shipment.

What effect will this huge increase in the cost of fuel have on freight transportation, logistics and manufacturing?

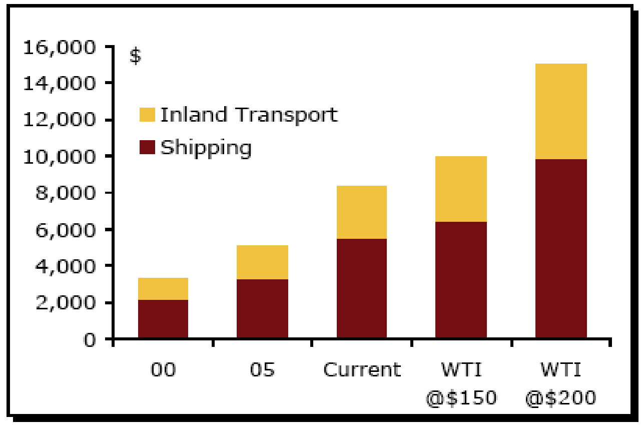
Two articles, *Past the Tipping Point* (Gosier) and *Will Soaring Transport Cost reverse Globalization?* (Rubin), offer some insights into the potential effects. (Both articles can be found on the MVFC website.)

Gosier illustrates the impact of increased fuel prices on the location of manufacturing with a case study of a company with facilities in Juarez, Mexico; Philadelphia, PA; and Omaha, NE. With fuel prices at $75 per barrel most production comes from the

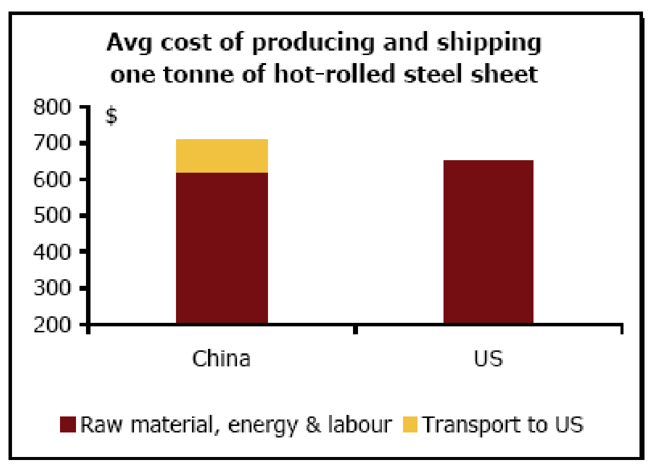


Juarez plant; but at $200 per barrel nearly half of the production would move to the US facilities. It is more economical to locate production closer to the customer.

Rubin makes the case somewhat differently. He notes that over the past three years, every one dollar increase in world oil prices has lead to a 1% rise in transport costs. He notes that at current oil prices (May 2008), every 10% increase in distance translates into a 4.5% increase in shipping costs. The 40-foot container that cost $3,000 to ship from Shanghai to the East Coast of the US in 2000, now costs more than $8,000 and would cost more than $15,000 if oil prices hit $200.



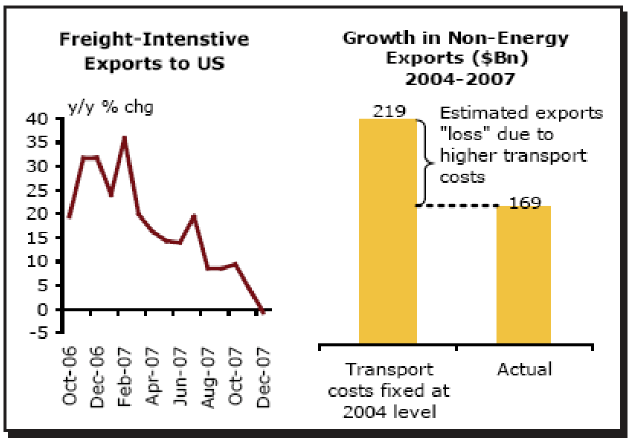
Rubin uses steel to illustrate the importance of this change. A ton of steel requires about one and one-half hours of labor. While China still has a major advantage in labor costs, they import nearly all the ore used in steel production. With those transport costs and the cost of shipping the final product to the US, it now costs less to buy US steel than Chinese steel.



This cost structure is reflected in today's trading patterns. Chinese steel exports to the US have fallen by 20% when compared to last year. At the same time, US steel production has grown by about 10%.

Fuel Prices (continued)

Steel is one of those freight intensive commodities, that is a commodity with relatively high transportation cost because weight or bulk and relatively low value. Shoes, apparel, and furniture are also in this category. A fair amount of the total Chinese exports to the US are freight intensive. The following illustrates the impact of increased transportation costs on Chinese exports to the US.



Source: US Census Bureau, Golisticsmgnt, De 2007, CIBCWM

The trend also seems to be borne out by the drop in traffic at LA/Long Beach, the principle port of entry for Chinese imports. June 2008 traffic was down 12.5% from the same month of 2007. The first six months of 2008 were down nearly 7% from the previous year.

Mexico may be the beneficiary of the rise in oil prices. It has a significant labor cost advantage over the US and a major transport cost advantage over China. Non-energy exports from Mexico to the US continue to grow at the rate of 7% annually. Much of that growth is in the freight-intensive sector and much of it competes directly with China.

Gosier sees a much greater emphasis on capacity utilization and sourcing strategies as ways to reduce transportation costs. Companies may want to rethink that logistics strategies of Just-in-Time and Pull Logistics in favor of slower speed, but higher volume approaches. These changes are illustrated in the following:

All of this depends on the future price of oil and the strength of the US and global economies. Some speakers at Congressional hearings earlier this summer argued that as much as 70% of the current price of oil can be attributed to speculators. If a speculative bubble exists and if it bursts, it will probably be a temporary correction in the general upper trend. Oil is a finite resource for which worldwide demand is increasing. A number of things pressure the price of oil, some positively and some negatively.

Positive	Negative
Demand in China and India is growing.	Demand in the US and Europe is stable or falling
Political unrest in the Middle East and Nigeria	China has raised the price of gasoline
OPEC seems able to maintain price control	Major new reserves have been found off Brazil
The weak dollar drives up the price	Iraqi production should be increasing, contributing to world oil supplies
Russian production seems to have peaked	Alternative energy sources are growing in importance
When prices fall American consumers tend to go back to old habits	Strategies to counter global warming are being taken somewhat seriously

Where does this leave us? It seem unlikely that we will have oil prices at $20 per barrel in the future. Therefore, the freight transportation strategies that worked well when energy was cheap will have to be rethought. This probably means more production and distribution facilities closer to markets and much more emphasis on managing transportation to maximize utilization.

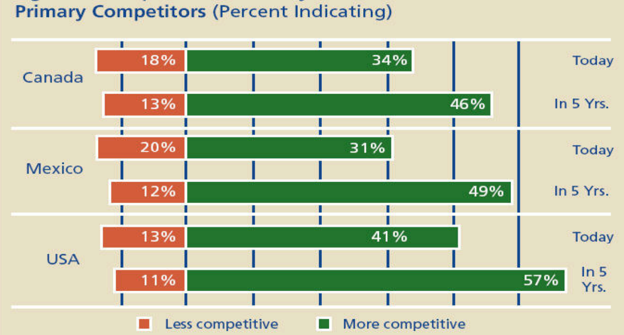
The Great Lakes Manufacturing Council

In July the Great Lakes Manufacturing Council held its annual meeting in Cleveland. People from private industry, government and academia from all the Great Lakes states and provinces attended. Speakers included Joe Loughrey, President and COO, Cummins, Inc.; Jane Warner, Executive Vice President, Global Finishing and Software Businesses, Illinois Tool Company; and Donald McCabe, Senior Vice President, Manufacturing and Performance Excellence, Corning, Inc. Many other speakers took part in panels or break out sessions.

While all the sessions were excellent, I want to focus on one report given by Craig Giffi of Deloitte Consulting. Giffi gave an overview of a report that Deloitte had prepared for the National Association of Manufacturers. The report was of a survey of manufacturers in North America. In many ways the survey results tend to reinforce the views presented in the last article on fuel costs. North American manufacturers are quite optimistic about the future of manufacturing in the US and North America.

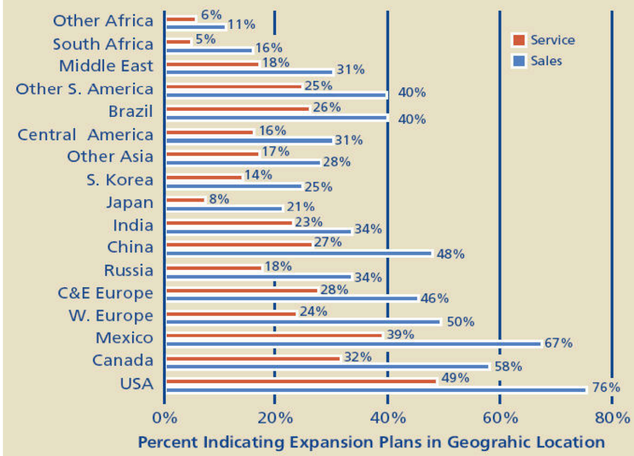
As the following illustrates manufacturers in Canada, Mexico and the US all see themselves as becoming more competitive over the next five years:

Figure 1. Competitveness Today and in 5 Years Relative to Primary Competitors (Percent Indicating)



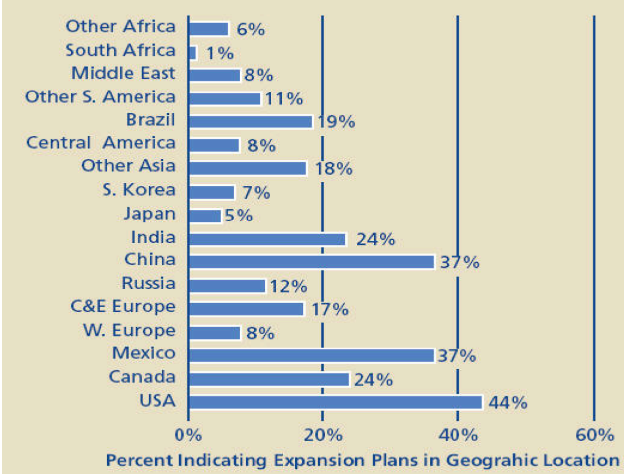
Most respondents also saw a greater expansion in their sales and service operations in North America than in other parts of the world.

3b. Where Will You Be Expanding Sales and Services?



Even production will be expanded in North America, based on the views expressed in the survey. Only China and India were estimate to grow at rates comparable to the three countries of North America. None rated as high as the US.

3a. Where Will You Be Expanding Production?



Another set of questions that got much of the press coverage dealt with the impact of NAFTA. Forty-nine percent rated its impact as positive, while only 10% saw it as negative; the balance said it was neutral.

You can find all the presentations from the conference at: http://greatlakesmanufacturing.org/glmc_forum_2008.cfm

Grain Bottlenecks

The Seattle Times reports on the problem of bottlenecks in the shipment of grains for export. According to the article, which can be found at http://seattletimes.nwsource.com/html/nationworld/2008136169_bottleneck25.html, grains intended for export are piling up near terminals waiting for rail cars or barges.

In 2007 similar delays forced grains to be stored in the open or in improvised shelters. The USDA estimated that the need to store added $107 million to the $160 million cost of transporting the grains. This amounts to nearly one percent of the market value of those grains.

Some producers have raised concern over the US's position in the global food market. Noting that other countries such as Brazil and Argentina are moving into that market very aggressively. In a cost competitive world, increased transport cost could be a hinderance to US farmers.

Comment

As the article on fuel prices demonstrates, the situation facing freight movement in the region and the nation is changing. Less than a year ago, our primary concern was capacity. We saw our major highway routes congested and growing more congested. Many of our rail corridors were also operating at capacity. Fuel prices seem to have changed the nature of the problem, at least for a little while. Overall vehicle miles of travel have fallen by as much as 3.6%, depending on which report you read. Imports are down and export are up. We have some reasons to be optimistic about manufacturing in North America and the US.

We still have challenges. The impact of the price of fuel underscores the importance of efficient transportation. Our region has many advantages in transportation and natural resources. We are the hub of the rail and freeway networks. We have incredible resources in our rivers and lakes. We have the coal and iron ore that made our region and industrial powerhouse in the late Nineteenth Century. We still have to make our transportation network as efficient as possible. We have to capitalize on the strange benefit that high oil prices have given us: We are now more competitive with foreign producers because it costs so much to move the products over long distances. We have to maintain our historic advantage in transportation to be competitive with manufacturers in other parts of the US or Mexico.

Give Us Feedback

Newsletters are fun to write and read, but they are a one-way communications device. In the sidebar, you will find contact information for all of us at CFIRE. Please give us your comments and ideas.

The Mississippi Valley Freight Coalition and the Center for Freight and Infrastructure Research and Education

CFIRE Director, Teresa Adams
adams@engr.wisc.edu or
608-263-3175

Deputy Director, Jason Bittner
bittner@engr.wisc.edu or
608-262-7246

Research Manager, Greg Waidley
gwaidley@engr.wisc.edu or
608-262-2013

Coalition Facilitator and Editor, Ernie Wittwer
wittwer@engr.wisc.edu or
608-890-2310

www.mississippivalleyfreight.org

cfire.wistrans.org

Mailing Address:

Wisconsin Transportation Center

1415 Engineering Drive

2205 Engineering Hall

Madison, WI 53706-1691