THE FUTURE OF GLOBAL TRADE

JUNE 2020- The world is currently faced with a crisis of unprecedented proportions. Much of the pandemic is reflexively blamed on the interconnectivity of the world's nations. After all, with the virus thought to have emanated from a source in China and now affecting the entire globe, it is reasonable to speculate about the coming contraction of global trade. World Trade Center Chicago, to the contrary, firmly believes that the "hard goods" that underpin global trading activity are what dominate worldwide supply chains and the logistical elements of seaports, airports, railways, trucking and highways. Unlike the global provision of services, hard goods can't be moved between countries via Zoom or GoToMeeting. It is inevitable that global trade will continue to expand but there will be changes that address issues directly brought forth by this pandemic.

THE FACTS

- As World Trade Center Chicago has pointed out in prior discussions, the importance of expanding international trade in the U.S. is critical. It underpins most of its job growth over the last thirty years, since the fall of the USSR. One out of every 5 new jobs created in the U.S. has some connection to foreign trade. Equally important is the fact that these jobs are defined as "high value". This means that the equivalent job which is solely performed for domestic commercial purposes is 20% to 25% less in compensation. Most importantly, 85% of global business growth for the next ten years is projected to take place outside of the U.S.

- Even the disastrous results of the pandemic show how connected the world is. Not only has the trillions of dollars of the world's infrastructure been developed and positioned for efficient international trade, but the financial world has expanded to accommodate this, as well. Whereas only major international banks prior to 1965 had mechanisms such as foreign exchange trading and other methods of international finance to foster the financing of foreign trade, now a multitude of smaller, regional banks around the world do so as well. Additionally, every major market in the world experienced publicly traded equity values being reduced by 20% to 30%. In the past 15 years, American entities, including investors, individuals businesses and the Federal Reserve grew its foreign securities holdings from $6 trillion to more than $12 trillion

- China has been very attractive to the rest of the world as "the world's factory'". In a PricewaterhouseCoopers LLP survey for the American Chamber of Commerce in March of 2020, more than 70% of respondents had no plans to relocate production and supply chain operations outside of China due to the pandemic.

- But the pandemic has painted China as a somewhat unreliable trading partner in certain areas, and which uses tactics to pressure its partners. Despite their commitment to locating businesses in China, in April 2020 more than 75% of American companies have reported, since the start of the pandemic, supply chain disruptions in China as noted by the Institute of Supply Management.

- Further in this regard are efforts on the part of the Chinese to flex their muscles which have caused an examination on the part of the world community regarding its relationship to China. The "debt trap" diplomacy of China's effort to remake elements of the ancient Silk Road, currently referred to as its Belt and Road program, has resulted in financial stresses and distortions within important countries with emerging markets. The militarization of the South China Sea has caused great consternation on the part of other Asian countries and Western countries who use the heretofore open sea lane as one of the most important global trading highways. Recent crackdowns in Hong Kong are, at best, troubling and, at worst, a violation of an important international treaty.

- References to a global trade war recently have gained currency. WTCC believes that this will not result. Rather, what is being seen now is that the world is preparing for a process of careful "strategic de-linking". And this is quite natural. Just like businesses revise strategic plans due to "on the ground", real time, conditions, it should not be seen as an act of belligerence when countries do the same.

WHAT THIS MEANS: "DISRUPTIVE CHANGE"

- Not all disruptive change is the result of friction between "country partners" in the global trade system. Global trade, despite the many country-level players with a multitude of governmental systems, is capitalism. Disrupters to capitalism in search for better efficiencies and higher profits date back to ancient patterns of international trade. Disruption has accelerated over the last thirty years with the advent of the internet and the dot.com revolution. In fact, one glaring disruption has occurred over the last fifteen years outside of the view of the greater public, but very well known to the "inside baseball" community of global traders. The Panama Canal expansion is the most important recent, disruptive, infrastructural change affecting global trade. The expansion of the canal was undertaken to allow ships bearing cargo from Asia to directly access East Coast U.S. ports. The first direct shipments to East Coast ports commenced in 2016. Prior to the canal's expansion ships from Asia mostly unloaded cargo at the U.S. West Coast ports. This is no longer the case. The East Coast ports invested billions of dollars in infrastructural investment, assuring that they would be able to receive the bigger ships; dredging waterways to 45' depths, raising bridges to allow for larger cargo ships, improving street access for trucks to get to ports for the receipt of containers, and other actions to ready for this eventuality. The early disruption of this shift has already been revealed with the start of this activity. Containerized freight in the standard 20- and 40-foot boxes was up in east coast ports not previously known for spikes in cargo: 28 percent in the Philadelphia port in April 2017 compared with the same month a year earlier; Savannah reporting 19.4 percent growth compared to a year earlier; Norfolk up 14.6 percent in April 2017 from the prior year. The main losers: the Puget Sound ports of Seattle and Tacoma, whose cargo volumes fell 1 percent; New Orleans, which shrank by 21.3 percent. The canal's expansion disrupted other shipping infrastructure as well. Large segments of the rail/freight system in the U.S. have been irrevocably changed for generations. The long-time advantage of the International Longshoreman's Association to exploit the West Coast monopoly is gone.

- Frankly, the global trade system before the advent of the pandemic was due for a disruption. As mentioned, a system based on capitalist principles is always in motion. But as in any other crisis which the world has faced in the last eighty years since the global trade structure began to be formed after WWII, global trade will continue to expand. This is because the global trade culture and the nature of global trade infrastructure is so pervasive that the system is now organic. The sheer numbers are themselves compelling enough to hammer home this point. In a recent Wall Street Journal piece concerning the "awkward" position that the European Union and the, now independent, UK find themselves in between the U.S. and China, the interconnectivity of the four largest international trading partners through the perspective of the EU tells the story. The EU exports approximately $400 billion annually to the U.S. and imports approximately $300 billion. The EU exports nearly $375 billion annually to the UK and imports approximately $200 billion. The EU exports approximately $250 billion annually to the China and imports around $375 billion. Other reasons for expansion are apparent such as the multitude of countries who have not yet reached their "global trading maturity" in places such as Africa, South Asia, and parts of Latin America. But it is clear as a modern day fact that increased trade and increases in GDP go hand-in-hand.

- The most visible element where changes will take place in this next generation of disruption will, largely, be apparent in the supply chain structure. Some manufacturing will likely move from China to the South Asian region (India, Sri Lanka, Bangladesh) and Southeast Asia (notably Vietnam and Thailand), but trade will remain global. On-shoring has already begun in the United States as exemplified by the recent decision of Taiwan Semiconductor and Manufacturing Company's announcement to build in Arizona and the effort underway by the Administration and Congress to create a fund to pay for the on-shoring of critical electrical components industry. No better example of the new emphasis on "strategic" trade is the effort to reign in Huawei, the Chinese electronic components manufacturer. Another example of how "country partners" act similarly to private business partners when de-linking is commercially necessary is the drama over rare earth minerals. During the height of the 2019 trade war between the U.S. and China, President Xi toured a region of China that is noted for its richness in rare earth minerals. The trip was interpreted as a message to the U.S. that the Chinese government has leverage as a result of this condition. The Chinese government has been funding the mining of rare earth minerals at a rapid pace as they see this as a strategic advantage over Western nations. The problem for China in sending the message is that the United States got it. It galvanized bi-partisan support in Congress to take action. The Defense Production Act was invoked to help pay for the start of a processing facility for rare earth minerals in a remote section of California, called Mountain Pass.

- The pandemic has exposed the vulnerability of a vast, geographic expansion of the manufacturing supply chain. The deep-tiering and verticality of the many subcontractors and suppliers in the final assembly of a product, and the confinement of this system to a single location exposes manufacturers to several risks. One risk is that the further the supply chain exists down in the assembly process, the smaller the suppliers get and the more invisible the suppliers become to the final assembler. With many small businesses dominating global supply chains, and the recognition that the average small business maintains less than thirty days of working capital, current press announcements are replete with the glaring gaps which have developed in manufacturing and final assembly as a result of the pandemic. The frailty of the system and oftentimes obscurity of its members are no better exemplified by the Weekend Wall Street Journal of June 13th. A headline article reported that 1,300 Chinese manufacturers of N95 masks have named their required "representative office" in the U.S. as a residence in Wilmington, DE where the occupants know nothing about the relationship. Lastly, another vulnerability in global supply chains which has been revealed is that a political, civil or geological disruption in a geographical location where this vertical system exists can be catastrophic. This is what the world faces today, and the changes are underway.

THE FUTURE

The U.S. can be an even bigger player on the international trading stage than it has been. WTCC has recently written about the importance of the SME's (small-to-medium size businesses) in U.S. growth and, given the manner in which small business has been crushed by the pandemic and the recent political upheavals in U.S. cities, it is more important at this time to revisit this phenomenon. Fully 90% of all businesses in the U.S. are private, with less than 500 employees. But 88% of this community has less than 20 employees. Further, it is in the 88% that a woman or member of a racial minority might appear most frequently as the prime owner or CEO of such a company. But, with most international job growth of the last thirty years heavily dependent on the growth of foreign trade, only 1% of these companies trade internationally. The importance of SME growth is not unique to the U.S. It is estimated that there are approximately 150 million such businesses around the globe. And the explosive growth in large technology companies, contrary to popular commentary, is contributing to the growth of this phenomenon. AIRBNB, the U.S. company which formed around the concept of lodging in facilities other than the formal hotel community, is responsible for the creation of 600,000 small independent businesses around the world to support its reservation system. The World Trade Centers Association makes its most important inroads in the expansion of jobs by getting more of the SMEs to trade internationally. It has programs which are targeted towards this objective and works with national organizations to grow these businesses through increased foreign trade, which helps to grow the job base in the regions in which World Trade Centers operate. Entrepreneurs will be the solution to this pandemic and most growth will come from SME's and international trade. Of critical importance to the future of global trade will be supporting SME trade flow in the U.S. as a foundation for job growth. The unprecedented impact of the current pandemic further exemplifies the paramount importance of job creation. This is where World Trade Center Chicago can help.

WTCC is one of 330 World Trade Centers (WTCs) around the world. All are members of the World Trade Centers Association (WTCA), which is the largest, private, global trade organization in the world work under a credo to be apolitical. It is why the WTCA is the only international organization in which China and Taiwan serve as members of equal footing.

WTCC strives to be a good partner with business operatives dedicated to global trade in Chicago and throughout Illinois. It can achieve this by providing access to its network of WTCs throughout the world.

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