

## Taking the Long View



■ Trade and Transportation

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If nothing else, a global recession gives us all an opportunity to brush up on our economic history. When times are bad, there is at least some comfort in knowing that previous recessions led to recoveries which led to further economic growth. Taking the long view gives us some perspective and reminds us that what appears to be a dramatic shift in the economy might very well be a blip on the radar screen, a brief departure from our normal trajectory.

The same is true of global trade. These days, it's not uncommon to hear people talk about major shifts in global trade lanes brought about by things like the expansion of the Panama Canal and the shift of Asian trading activity south and west to Vietnam and India. And while there is no doubt that changes are occurring, it's also true that we have short memories.

The rise of China as the lynchpin of global trade is a relatively recent phenomenon. China only became the top nation in containerized trade in 1998. Today, the portion of China's economic output attributable to international trade is greater than 80 percent, but in 1980 it was a mere 15

percent. While the rising cost of doing business in China may make Vietnam and India more attractive centers of production and shipping, and while the expansion of the Panama Canal may create new opportunities for some ports to lure traffic away from others, history tells us that what we are experiencing now should be considered in light of much longer term trends. Predicting winners and losers from recent events means understanding what has shaped trade in the past. It means taking the longer view.

The growth of global trade has always paralleled the growth of cities and the increasing use of technology to solve the complex problems confronting humans. From about 800 A.D., when early Europeans discovered the benefits of water navigation - particularly along rivers - as a means of exchanging goods, up until the late 18<sup>th</sup> century, trade was characterized by an emphasis on the pursuit of goods needed for basic survival, including agricultural products and textiles. These were relatively low value commodities that could be carried in bulk on vessels made out of wood and traveling along coasts or on rivers. Most processing of materials was local in nature.

Rapid changes began to occur in the late 18<sup>th</sup> century however. This was the first stage of the industrial revolution when steam power replaced falling water as the principal means of driving industry. Factories were no longer limited to locations immediately adjacent to rivers. This facilitated the growth of cities which became home to industrial centers. At the same time, steel and iron replaced wood as the primary structural materials. The combination of larger, sturdier

vessels and steam power meant that goods and people could penetrate the interior of entire continents in a way that had never occurred before. Nations gained global dominance through trade and through military might. The first great trading vessels were also designed as defensible ships to protect cargo and crew as well as the interests of the nation.

Since the early 20<sup>th</sup> century, global trade has been marked by an even more rapid movement of goods. This stage has involved an increased reliance on technical skills to make trading systems more efficient. For example, the increased use of information tools to generate real-time data means that just-in-time delivery is now possible. This approach to managing the global supply chain has reduced costs in areas like warehousing and inventory, integrating the various components of the chain into a more seamless flow of goods and services. New technology tools have also facilitated information flows around the globe. This makes it easier to identify lower cost sources for various goods (and their components) that are far removed from the end user. The combination of reduced costs and integrated supply chains results in trade that occurs over greater distances.

As was the case in the earliest days of trade, some of the advances in 20<sup>th</sup> century technology particularly in the shipping sector, were the result of improvements in military technology that found commercial outlets. Take the diesel engine. After World War I, the excess capacity of diesel power plants built for submarines was put to use in the commercial shipping sector. And modern shipping benefited from a series of occurrences that resulted from the closing of the Suez Canal in 1956. When Egypt closed the Canal, it restricted the flow of oil to Europe. As a consequence ship owners began investing in bulk carriers that could carry oil from the Middle East to Europe around Africa. Without the limitations on ship size imposed by the Canal, investments were made in larger and larger vessels which reduced operating costs. This approach to trade, focusing on economies of scale, would find its greatest outlet in the container ship.

So, like in real estate, location matters. But determining future winners and losers in the “trade game” will depend upon much more than proximity to a canal or access to Asian labor. It

will depend upon a combination of factors, some of which may not even be apparent to us yet, including technologies we can’t yet imagine. There is also the human factor. Our demand for goods and services sets in motion complex supply chains. And if there is such a thing as human nature, then here in particular, the long view is advisable.