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Will Rising Logistics Costs Finally Reverse Trend of Offshore Production?

"Mini-Trend Seems to be Underway; DESA Moves All Heater Production back from China to Kentucky; Reverse Globalization?

SCDigest Editorial Staff

Is it possible that rising fuel and transportation costs will put the brakes on – and possibly even reverse – the trends in globalization?

Both the math and the anecdotal evidence seem to say that is just might happen, at least for awhile.

Rising logistics costs are a global phenomenon, and depending on where and how you are shipping, the cost of moving containers from China to the US might have double or tripled over the past few years. For some products, especially those with low margins, or where the economics behind the offshoring decisions were marginal, that can mean rising logistics costs can erode the savings that the offshore supply chain initially delivered.

The cost of shipping a forty-foot container for some companies, especially those on the east coast, has risen from $3000 to as much as $8000 since the beginning of the decade. That's a huge increase in total supply chain costs for which lower production costs overseas may not compensate.

Some Companies Moving Production Back

DESA LLC, which makes a variety of heating products such as those used on the sidelines during cold football games, recently announced it was moving all of its production back from China to a factory in Bowling Green, KY. There are numerous reports of furniture factories in the Carolina's, which were devastated by imports from China, revving up again. Even one now Chinese-owned company, Craftsman Furniture, has halted plans to move more production back to China. Hair case products maker Farouk Systems, also plans to bring all its production – and about 1000 jobs – back from China later this year. "My cost of getting a shipping container here from China just keeps going up -- and I don't see any end in sight," **Claude Hayes**, president of the retail heating division at DESA, told the Wall Street Journal last month.

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The New Tariff

Rising transportation costs are a new type of "tariff" on imported goods, and by some estimates that logistics tariff versus the state of affairs just 2-3 years ago has increased from 3 to 9 percent – a change that can totally alter the economics of the offshoring decision.

Currency valuation swings and rising labor costs in China may also be fueling some of this reverse thinking.

"I rather suspect that the close to 20% rise in the Chinese renminbi against the dollar (together with higher inflation in China than in the US) has also

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played a role in these decisions," says **Brad Setser** of the Asia EconMonitor. "A rise in the renminbi has the same effect as a rise in the cost of shipping. Production in the US starts to look more attractive if the costs of producing goods in China goes up."

Economist **Jeff Rubin** thinks the situation is likely to also help US steel makers.

"It's not just about labor costs anymore," says Rubin. "Distance costs money, and when you have to shift iron ore from Brazil to China and then ship it back to Pittsburgh, Pittsburgh is looking pretty good at 40 bucks an hour."

The big question for manufacturers and supply chain strategists, of course, is whether the current logistics situation is permanent – or whether after this current spike, fuel costs will come back to levels seem 3-4 years ago.

The key, most agree, is being able to quickly and accurately measure total supply chain costs, and build flexibility into the supply chain to be able to make and execute sourcing decisions rapidly.