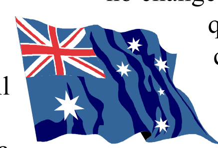
CII

APRIL 2004

Australia-U.S. Free Trade Agreement; Plenty of Jokers:

With much of CII's activities geared to the South Pacific, we naturally take a great interest in new developments there. The recent Australian-U.S. Free Trade Agreement is a major evolution in the business and commercial relationship between the two countries. From the U.S. standpoint, the Agreement is a win-win situation. More than 99 per cent of American manufactured exports to Australia now will be free of all import duties. As an air cargo wholesaler overwhelmingly moving finished manufactured goods as well as spare parts and components for our forwarder customers to Australia, CII expects to benefit from this new trade agreement.

From the Aussie side, the picture is far less rosy. So one sided is the agreement favoring the U.S., many in the Australian public and Parliament protested the new accord. For an advanced nation with a very high standard of living, Australia surprisingly has little industry. Its exports are almost wholly agricultural and raw material products. It is just these products that the U.S. Trade Commission refused to consider for duty elimination. Beef, for example, the largest single export to the U.S., will retain its high tariffs because of objections from U.S. cattle ranchers who complained that "cheap" Australian beef would cost thousands of U.S. jobs. Perhaps the most egregious example of U.S. lobbying muscle was the sugar industry. Sugar was taken off the table during negotiations, with U.S. trade representatives insisting there was to be no change in the tiny Australian sugar



quota. If changes were even contemplated, the entire Trade Agreement would be scuttled. The sugar lobby is a disgrace to the United States. Here is a minuscule group of sugar growers in politically powerful states throughout the South and Southwest making policy for the $1 trillion generated by U.S. trade with the rest of the world. Speaking as a freight forwarder whose customers will benefit, I applaud the new Australian-U.S. trade agreement. Speaking as a new American, I am ashamed at the enormous pressures placed on the Australians epitomized by a personal telephone call from President Bush to Australian Prime Minister John Howard, urging adoption of the agreement

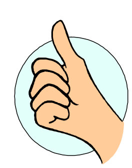
Inside This Issue:

Another Loader Becomes A Co-Loader!

Keith Loader, our Chicago representative, convinced still another member of his family to get into the co-loading business, better known as whole-saling. Last February, his nephew, Ian Loader, joined CII as Vice President, Eastern Region, with headquarters at New York's JFK. Before venturing out to the big airport in Queens, Ian spent the previous three months being tutored by the best teacher in the business—his uncle Keith! From driving a forklift to pallet building, to mastering the paperwork, to negotiating with the airlines, to looking after customers, Ian had to learn fast or he would have been cut up by the great white sharks in our business!

When Ian joined CII in February, it was sink or swim. We threw him into the deep end of the pool, knowing his three month stint with Keith would stand him in good stead. The results? Uncle Keith would be proud of his nephew's progress and achievements in that snake pit called JFK cargo. It's one of the toughest freight environments in the world, especially for a non-New Yorker. Here we are, headquarters in Los Angeles with a mid-westerner heading our N.Y. operations. Yet, our business is growing by leaps and bounds.

Keep up the excellent work, Ian. We're not the only ones who think so. Feedback from customers and airlines is, they think you are number one in their books.

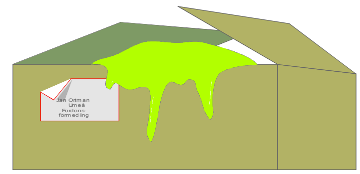


Airline Security Gets Tighter Because Of Stowaways:

Last autumn, Kitty Hawk received a great deal of unwanted attention when it was discovered that a man "shipped" himself in a box from New York to Dallas on one of the cargo carrier's airplanes. Far less publicity was given to a more recent incident involving three men from the Dominican Republic. They shrink wrapped themselves in a pallet on a Capital Cargo International flight and were discovered when they attempted to tear themselves out at Miami International Airport. This incident seems to have galvanized a number of U.S. carriers to step up security procedures, particularly Northwest Airlines.

Northwest has put forwarders on notice that it will start random inspection of freight, including opening packages it considers "suspicious." This new action will pose a serious dilemma for all forwarders, particularly those who handle customers' shipments from Asia. Northwest, of course, is the largest combination carrier in terms of cargo and is the only American passenger airline with all freighter service out of the ever-increasingly important Asian market. Once again, forwarders are faced with an almost insoluble problem; making sure cargo coming into the U.S. is properly screened and inspected yet making money from time definite transportation.

As Yul Bryner sang in "The King & I," is a puzzlement. That "puzzlement must be solved if air freight can continue serving customers with the speed and preciseness of delivery they expect, while obeying tougher security rules.



GM's J-I-T Strategy Backfires:

Readers of our Newsletter will remember my criticism of the "gung ho" just-in-timers; those ideologues who proclaimed that anyone who didn't believe in the J-I-T mantra were hopeless fuddy-duddies, 100 years behind the times and should be drummed out of the air freight business. My criticism of J-I-T was based on thirty years experience in cargo; that no one system or methodology answers the very many different needs of shippers. The latest event, involving General Motors and Just-In-Time delivery of raw steel for GM's assembly lines, illustrates my contention.

When Just-In-Time first made its appearance about fifteen years ago, the car companies were among its earliest and most fervent apostles. "We're going to save millions by moving parts and supplies at the last minute to avoid excess inventory costs," said the auto makers. "We're also going to cut down on the number of suppliers so that we can better monitor the flow of auto parts," they continued.

Yes, the auto makers saved millions but it seems they will be losing hundreds of millions of dollars to cover rising steel costs. Rather than risk cutting off its supply of parts since inventory deliberately was cut to next to nothing according to the gospel of J-I-T, GM reluctantly will pay its suppliers the higher cost of steel to ensure on-time delivery. This incident illustrates once again how vulnerable companies have become after years of streamlining their supply chains and relying on a smaller number of suppliers. GM admitted that without paying the higher steel prices for its purchases, "our plants would have to shut down." Here is another example of Just-In-Time ideology swamping common sense. J-I-T, in many cases, does save on inventory costs but a careful eye should be kept to ensure that the shipper doesn't save a penny to lose a pound.

Arrow Air; More Lives Than The Proverbial Cat:

Arrow Air is a melancholy example of why cargo airlines seem to possess the nine lives of proverbial cats. They never seem to go out business. Here is an airline with a long history of inept management, shaky financial base, miserable service and maintenance performance, and even a fatal crash which took the lives of more than 200 U.S. servicemen on the snowy fields of Newfoundland. Yet, it continues to fly with some equipment more than forty years old. Perhaps even more amazing is the willingness of investor groups to keep funding this poor excuse of an airline. Despite our year being only three months old, Arrow already has been sold twice in 2004 to different investment groups after filing for bankruptcy in January.

Arrow's situation is very similar to that of freight forwarder GeoLogistics, another loser, in which Arrow has had an almost incestuous relationship. Arrow was the principal carrier for Geo's previous

incarnation, LEP Profit out of Puerto Rico to the U.S. Mainland primarily carrying pharmaceuticals for the forwarder's customers. That service generated a chorus of complaints from the likes of Pfizer, Schering Plough, Bristol Myers Squibb and other drug makers about miserable service.

What is there about the airline and air freight business that makes normally hard-headed businessmen turn into wild-eyed romantics? GeoLogistics and its predecessor companies have lost millions of dollars during the past decade, yet continues to be funded by investor groups who seemingly believe miracles will happen. Arrow is but one example of how cargo airlines keep flying through clouds of red ink. Kitty Hawk only recently came out of bankruptcy. Ditto with Connie Kallita's stable of airlines. Even a much stronger BAX Global finally recorded a profit last year after fifteen years of flying as an all-cargo carrier.

Asian Air Freight; Too Much Of A Good Thing?

The current Asian air freight market is the latest example of why freight forwarders increasingly grow old before their time. What some commentators are calling "an early spring," Asian-U.S. air freight volume is spiking to all time highs. Yet, for our industry, these huge volumes of cargo ex-Asia, particularly China, is turning into one big headache. What's causing this migraine? No big mystery. Asian cargo gateways are flooded with freight and lift capacity can't keep up with demand. Backlog at Seoul's airport alone is approaching 500 tons. With this huge increase in volume, as surely as night follows day, airlines are raising their rates. Ad hoc booking tariffs have jumped 40 per cent more than rates quoted last year. Spot kilo rates have jumped 50 per cent in many cases; from $2 to $ per kilo. More insidiously, a number of airlines is insisting forwarders upgrade to premium or express service to ensure space—often at rates two and three times consol tariffs. What's a forwarder to do? Even the famed flexibility of forwarders can't overcome fully the extraordinarily tight space between Asia and the U.S.. We're moving cargo from Asia to North America via Europe and Australia. We're persuading carriers to move more freighters into northern Asia where demand is greatest. CII is particularly fortunate in that we have live wire agents in China and Hong Kong who are moving our cargo on time and at realistic rates. It will be interesting to see if these huge amounts of cargo will continue as the year progresses. Or will it slacken as the U.S. economy slows down with a continuing dearth of jobs and less consumer spending.

U.S. Claims China Hampers Trade:

The White House recently filed a claim with the WTO alleging China tax policies hurt American chip makers. In response, Beijing calls it a "misunderstanding." What misunderstanding? As our trade deficit continues to balloon with China (the greatest of any nation), this champion of "rogue" nations is continuing scurrilously upon a path that makes it impossible for America to derive any trade benefit from China's growing prosperity. At every turn, Beijing erects road blocks to U.S. imports. We can't even get these people to combat rampant abuse of international copyright laws, let alone address the lack of ethics and integrity of their government-owned joint venture companies. The chip issue revolves around a 17% value-added tax that China levies on semi-conductors. Since the year 2000, chips produced in China have been eligible for rebates of up to 14%. U.S. chip industry executives say the rebate policy is part of an aggressive attempt by the Asian country to become a major player quickly in semi-conductors. The Chinese government insists its tax policies don't violate WTO rules. The semi-conductor case is based on a "misunderstanding." The Chinese are masters at clouding an issue. When is the world going to wake up and realize China has no intention of allowing its trading partners to play on a level field? The quicker we treat China with the same amount of contempt they obviously treat us, the better off we will be. I hope we succeed with the WTO complaint. I won't be holding my breath, however. The WTO, like the U.N., is bogged down in bureaucracy. It could take years to reach a decision. In the meantime, if I were President Bush, I would be considering seriously a retaliatory action.

Sincerely,

Julian A. Keeling