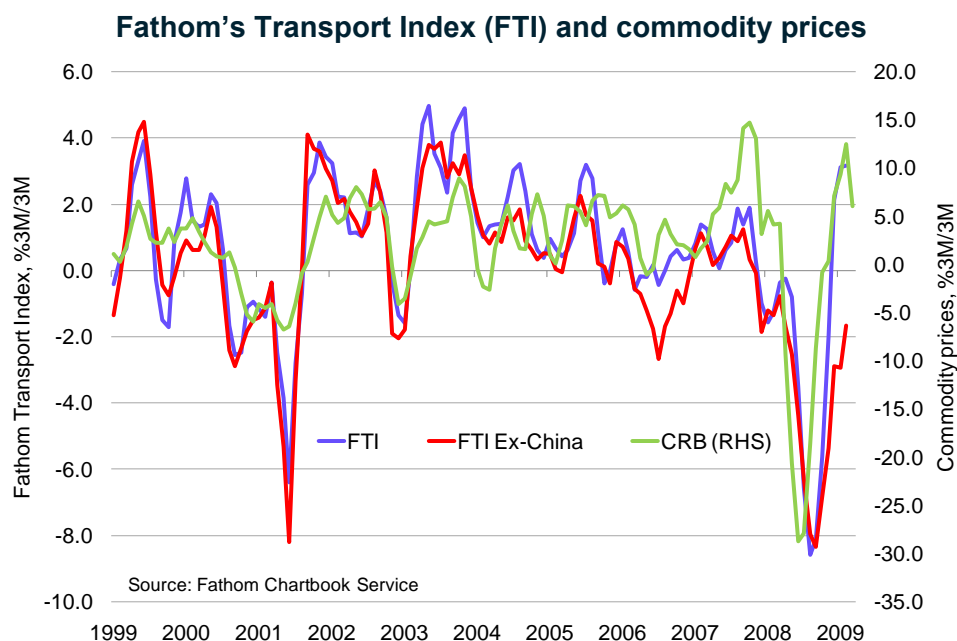


WE'RE GETTING THERE

In the late 1980s the UK's nationalised rail network was decrepit to say the least, but to persuade us that things were getting better those crafty ad men came up with the following slogan: "*British Rail, we're getting there*". Just where they were getting to was a mystery to most of Britain's long suffering rail commuters. Although we did find out in the end. It turned out to be privatisation. The privatisation of the rail service was pushed through presumably because it was believed that privatised train delays were more efficient than nationalised ones!

At Fathom we have been monitoring the transport industry very closely, searching for signs of a sustainable upturn in the global economy. For example, one could interpret the recent upturn in commodity prices as an early sign that global industrial production is likely to pick up. We know that commodity prices can be chased up by speculative demand, but if the volumes of goods being shipped around the world have risen too, then the price rises might indicate an increase in real demand and might therefore be interpreted as evidence that the global economy is "getting there", unlike British Rail which never did.



The green line in this week's chart shows the three month on three month percentage change in the prices of a broad index of commodities. It has risen rapidly recently. So too has Fathom's Transport Index (FTI) shown by the blue line. We have constructed this index to reflect the changes in the quantities of goods transported by road, rail, air and water around the world. By calculating this index we can monitor the quantity of goods that have been produced and sent onwards. We believe this index is a more useful indicator of future activity than the usual economic surveys, or the costs of transport services that can often be very distorted by shortages in the supply of, for example, vessels.



The FTI shows not only that the recent rise in commodity prices has been accompanied by an increase in the volume of goods that have been transported, but also that the commodity price increases between 2006 and 2007 were not accompanied by an associated increase in transport activity. In other words, it was a commodity price bubble, although you probably didn't need us tell you that today!

However, when we exclude Chinese freight activity from our index, the picture looks less positive. The FTI excluding Chinese freight activity is represented by the red line in the chart. It shows that outside China, freight volumes are still falling. This sort of information is now frequently interpreted optimistically as evidence that China is "leading *the global economy out of recession*".

According to official statistics China is growing at around 8% per annum. There are many reasons to be suspicious about these numbers, but it is not these figures that should lead us to be wary of this decoupling story. If China is to lead the global economy out of recession and back to trend growth, then its imports need to rise. This is not happening. Trade data is data that we can trust, since it is the rest of the world that is either selling to or, more frequently, buying from China. And this data shows that China's current account is expanding not shrinking. In other words China is still a net saver, and savers do not power economic recoveries.

So why the increase in freight activity, particularly Chinese freight activity, and the (seemingly) associated rise in commodity prices? One explanation is that China is simply stock piling commodities for the future, pushing their prices up today. And who could blame them when the other option is to purchase yet more IOUs issued by Uncle Sam? But an increase in commodity stock piles is not much of a harbinger of economic recovery, it's just another form of saving. In our view then, the recent strength of commodity prices and freight activity is not a portent of a return to normal, or at least not any time soon.

Instead the global trade figures and other evidence suggests to us that rather than attaining the speed of an unstoppable freight train once again, global growth is only likely to reach the "break neck" speed of a British Rail train. In other words, sustainable trend growth will get here, but it will probably be much later than the markets currently expect.