LLC SpecTransContainer offers integrated services to a wide range of clients in the 1520 gauge market, focusing on petrochemical producers. The main strategic goal of the new company is to become a Top 3 market player in its segment in the next five years.

The outcomes of year 2018 confirmed correctness of the decision to allocate the specialised container transportation segment to a separate legal entity. The volume of specialised cargo transported with the equipment of LLC SpecTransContainer amounted to 15,000 TEU by the end of the year, that is 36% above the target value of the approved business-plan.

Terminal Business

In 2018, the works on the Company's terminal network upgrading were continued, including maintenance of lifting machinery, trucks, and equipment.

To retain and strengthen the position of TransContainer at the containers terminal handling market, the purchase and sale of 100% CJSC Logistics-Terminal (on 3 September 2018, TransContainer and JSC First Container Terminal, a subsidiary of Global Ports Investments Plc, completed a deal to acquire 100% shares of CJSC Logistics-Terminal) shares were transacted at the St. Petersburg transport hub.

CJSC Logistics-Terminal owns and manages a multifunctional terminal logistics complex linked to Shushary Station (close to St Petersburg) by railway. The complex, which was put into operation in 2010 and which offers a wide range of services on container and general cargo handling, comprises a container terminal, warehouses of class A and C, a permanent zone of customs clearance with a temporary warehouse and other facilities of terminal logistics infrastructure. In 2018, the volumes of CJSC Logistics-Terminal handling amounted to 179,000 TEU, while the volumes of general cargo handling equalled 339,000 tonnes.

Geographic Priorities

Priorities for the international sales network development are set based on the existing and potential container flows between countries across the 1520 mm gauge network. The Company considers the following regions as lucrative for its international expansion: the Asia Pacific, India, the Middle East, Central and Eastern Europe.

In 2018, the use of Mongolia as a transit route for transportation was a new focus area for the Company. The region has a favourable geographical location, which enables us to choose an optimal route from the Chinese key freight traffic clusters to Russia and Europe.

To develop the transit route through Mongolia, in September 2018 the Company registered its subsidiary - Chinese Joint Venture TransContainer-Mongolia in Ulaanbaatar. This decision was taken as a part of the China–Mongolia–Russia corridor development initiative.

Chinese Joint Venture TransContainer-Mongolia is planned to deal with forwarding the container cargo on the territory of Mongolia, managing and monitoring the TransContainer's flatcar and container fleets on the territory of Mongolia and at the key border crossings, as well as arranging a technical interaction with the Mongolian forwarding agencies.

Strategic Risks

Our strategic development priorities are exposed to a number of key risks that may adversely affect delivery on the Company's strategic goals and financial and operational targets[1].

Deterioration of Global Economic Environment

Actual macroeconomic performance depends on a number of external interrelated factors, specifically:

- decreasing prices of oil and other commodities;
- China's economic slowdown;
- trade war between China and the United States;
- UK exit from the EU;
- risks related to the EU abandoning its ultra-low interest rates policy.

Materialisation of these risks may slow down the global economy, which would have a negative knock-on effect on Russia's GDP, national currency and international transportation volumes.

Should any of such risks crystallise, the Company would consider a review of its investment programme to factor in the new demand patterns, while also adjusting its pricing policy and implementing a cost optimisation programme along with other measures to improve its competitive position in the domestic and global markets.

Geopolitical Issues

Since 2014, Russian entities and individuals have been subject to both individual and sectoral sanctions imposed by the US, the EU and a number of other countries, with effects including limited access to debt and equity capital markets, and restricted technology transfers.

In August 2017, the US Congress passed the Countering America's Adversaries Through Sanctions Act, which identifies state-owned entities operating in the railway or metals and mining sector as potential subjects of US sectoral sanctions and provides for potential sanctions against Russian sovereign debt, public officials, and business persons.

1. For the details of Risks Report see TransContainer's Corporate Risk section on page 191.

On 27 August 2018, new US sanctions came into effect, but they do not directly concern Russian individuals or legal entities. Goods and technologies considered by the American authorities as relating to national security were forbidden for export to Russia (for example, avionics, submersible vessels, some kinds of gas turbines, gaging equipment, etc.). The only exclusions were the goods and technologies required for security of civil aviation.

New sanctions against Russia's economy or transportation companies also cannot be excluded, with the Company and the industry at risk of being severely affected, should it materialise.

To manage the risk, the Company monitors the sanctions environment and adjusts its debt and financial policy to factor in potential adverse effects from new or revised sanctions.

Deterioration of Railway Operating Environment

In recent years, increasing containerisation has been the key driver behind the growth of the rail container transportation market, which has also been supported by a prudent tariff policy for container shipments, easier access to the rail infrastructure, developing technology for high-speed container trains, etc.

Infrastructure fees for container transportation growing at above-average rates, additional limitations introduced for container trains, shutdown of terminal capacities used for container processing, as well as other restrictive technical measures may have a material adverse effect on the competitiveness of the entire railway industry and, therefore, on the performance of the railway container transportation market.

The Company will continue working together with Russian Railways and other railway administrations to promote further development of containerisation processes and container shipment practices.

Chinese Government Reducing or Terminating Support for Rail Container Transportation

The Chinese government supports international rail transportation, including transit routes. Government subsidies are a strong driver of the pricing attractiveness of rail shipments from China in comparison to sea freight. Cancellation of, or reductions in the government support may have an adverse effect on rail container transportation on relevant routes. To minimise the impact, the Company takes measures to bolster the competitive edge of existing services, expand the network of international routes, and optimise its logistics.

Competition from Alternative Transportation

The rail container transportation market strongly depends on the alternative transportation markets. Overall, the pricing environment in rival transportation segments has been favourable for the rail container business.

The sea freight market after its recovery in 2016–2017 shows the 2018 average container transportation rates corresponding to SCFI freight index approximately 2.5% higher year-on-year. It should be noted that up to July 2018 the rates were lower than in 2017. In July they became almost equal to the previous year, and in 2H 2018 the rates index raised 15–25% year-on-year due to negative news background relating to the trade war between the US and China.

However, long-term sea freight trends associated with a sustained supply-and-demand imbalance; a shift towards super-large container ships, and decreased per unit costs of a TEU container cargo are creating a systemic risk of a renewed decline in freight rates, which may have an adverse impact on the competitive strength of international rail container transportation.

To minimise the impact, the Company takes measures to bolster the competitive edge of existing services, expand the network of international routes, and optimise its logistics.

Stronger Competition in the Rail Container Transportation Market

Increase in the market demand usually leads to a mid-term competition growth driven by existing companies actively purchasing rolling stock and potential new players entering into the market. In the near term, it may push rolling stock prices significantly higher, while putting them under a mid- or long-term downward pressure from the growing supply-and-demand imbalance. A particularly severe impact may be felt at the cyclical downturn. The Company plans to minimise the impact of this risk by taking measures to improve the price competitiveness, client service, and rolling stock efficiency, as well as by a prudent flatcar purchasing policy ensuring an adequate supply-and-demand balance.

Risks Related to Rolling Stock Procurement

With the rail shipment market rapidly growing and the 2016–2018 rolling stock renewal underinvested, we face a growing short- and mid-term risk of having insufficient active rolling stock to meet the needs of shippers.

There might be delays and shortages in flatcar supply, along with rapidly growing flatcar prices triggered by growing demand and key components prices.

To mitigate the impact, the Company establishes long-term partnerships with key manufacturers and optimises the rolling stock purchase schedule.