MARKET OVERVIEW

Global Container Shipping Market

The fundamentals determining the performance of the rail container transportation market include growth in freight volumes and growth in containerisation, i.e. reallocation of cargo traffic to container shipping from alternative transportation and railway rolling stock.

Assuming that the containerisation CAGR remains, and the average GDP growth is expected at 1.5– 2%, we could project the container market to show CAGR of 7– 8%.

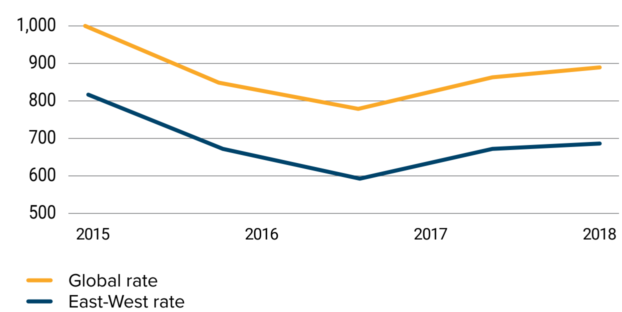
Due to sustainability on the market, the main focus remains on identifying the factors that would ensure greater containerisation of cargo flows and more volumes transported via railways. The key factor for attracting the cargo flows to the Russian Railway network is the development of transit traffic as it is least affected by domestic economic environment. According to the Company's estimates, the share of containerised cargo transported by the Russian Railway network increased from 6.6% to 7.2% year-on-year.

While the bulk of the Company's business revolves around land deliveries of containers along 1520 gauge railways, the state of the global sea shipping market is of essence to TransContainer, especially amid the rapid growth of intermodal volumes in international traffic.

On the one hand, the Company works with sea container carriers to organise export, import and transit shipments involving sea routes, therefore, the cost and availability of co-contractor services are the major drivers of the full price and quality of total logistic chain for the client.

At the same time, railway and sea shipping not only complement each other but also compete for a number of international routes. That is why changes in the sea freight market affect the competitiveness of railway transportation and require an adequate response from the Company.

Trends in Sea Freight Rates, USD per FEU



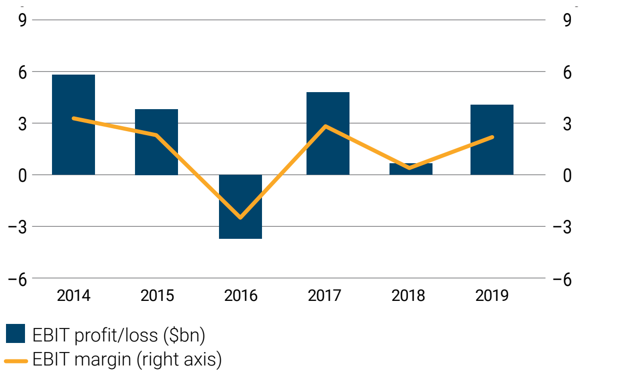
Source: Drewry Maritime Research

Overall, 2018 was as a successful year for the global container market. The recovery, which started in 2H 2016, continued into the reporting period.

In 2018, the global container traffic was up 4.7% compared to 2017 that is much lower than the 2017 (+6.3%) growth trend.

Still, the lower shipping volume growth rate yielded total operating profits of USD 1 billion for the industry in 2018 compared to USD 7 billion year-on-year.

Earnings Before Interest and Taxes, Industry Average (Drewry Maritime Research estimate)

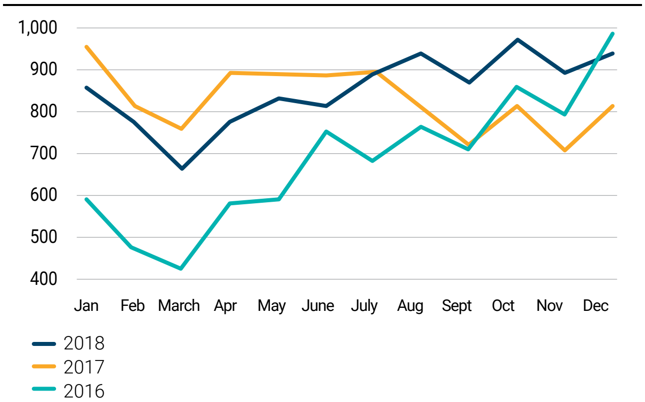


Source: Drewry Maritime Research

Trends in Sea Freight Rates

According to SCFI freight spot index, the average container transportation rate exceeded the previous year record by approximately 2.5%. However, with this respect the year is divided exactly into two parts: the rates were lower year-on-year until June, in June they were almost equal, and in H2 2018, the rate index went up by 15– 25% compared to the previous year.

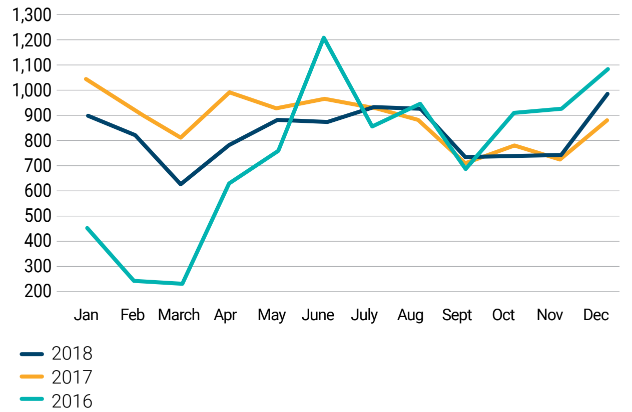
Trends in the Weighted Average Freight Spot Index (SCFI)



Source: InfraNews

Notably, the rates at Trans-Pacific shipping routes exceeded their 2017 level well in advance (in May), i.e. immediately after the imposition of extra duties on steel and aluminium by the US and announcement of planning the first package of anti-China duties with a total value of USD 50 billion per annum. From this point on, the Asia - US shipping market has experienced rapid growth. It should be noted that those trends were different for two main corridors between Asia and Europe (the Northern Europe ports and the Mediterranean ports). The rates in the Northern corridor were down as compared to 2017 through much of the year, except for several peak season months. The diagram illustrating the rates on the routes to the Mediterranean ports is approximately the same as the overall industry diagram with a distinct trend reversal in July.

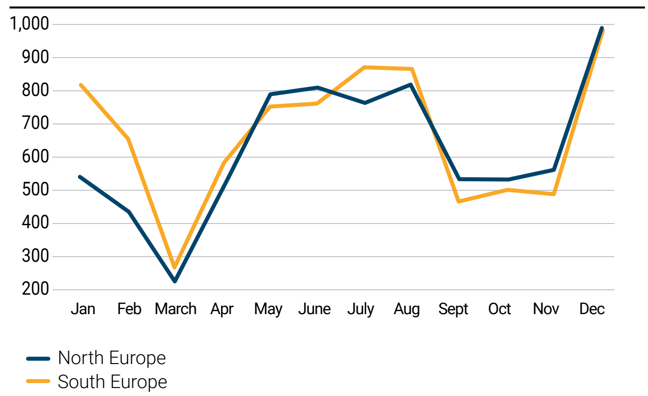
Trends in SCFI Index for the Mediterranean Ports



Source: InfraNews

One more significant change should be mentioned. The route to the Northern Europe ports has been traditionally the main corridor between Asia and Europe, and the rates there have always been higher. In 2018 the rates for the Mediterranean trade routes were staying higher than those for the Northern ports within six months.

Trends in SCFI Index for the Northern Europe Ports

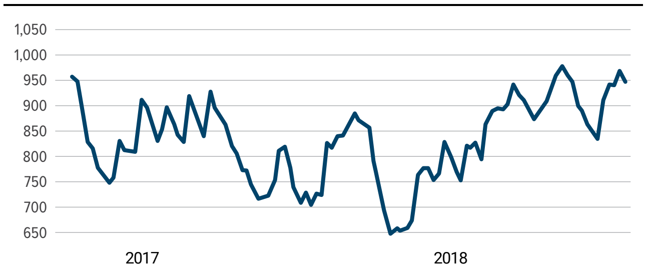


Source: InfraNews

This situation reveals a sustainable demand. Not surprisingly, the container ports of Southern Europe continued to grow at a faster rate than the traditional leaders of the European market (the Northwestern ports). Barcelona being the fastest growing container port in 2017 with 32% growth has lost its leadership in this category, but has increased its volumes by 16% in 11 months and apparently now ranks seven in the European port ranking, ahead of Felixstowe and the Maltese port of Marsaxlokk. Piraeus has become the leader with regard to growth rate. The container turnover of the largest port in Greece rose by 20% last year and amounted to 4.4 mln TEUs. The container turnover of Rotterdam (the largest port in Europe, with almost a third of all containers shipped via the Northern Europe ports) increased by 5.7% and reached 10.8 mln TEUs in the first three quarters of 2018. The quarterly growth rate in H1 was about 6%. The turnover growth acceleration both for Rotterdam and Antwerp in the summer peak season was most likely due to reorientation of cargo flows from the British ports of Felixstowe and Southampton, after that it slowed down in Q3. Considering the overall slow-down in the market by the end of the year, we could expect that Rotterdam's turnover would not exceed 5% throughout 2018.

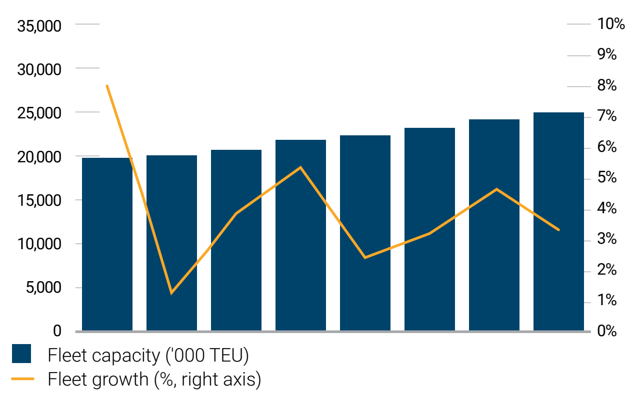
According to preliminary reports, the container turnover of Antwerp, the second largest port in Europe, increased by 5.5% in 2018 and amounted to 11 mln TEUs. However, except for a severe drop in turnover and rating of Felixstowe due to failure in introducing a new IT-system of the port, the rating of European ports has not changed significantly in the past year. At the same time, in Asia where the world's largest operating ports are located, the top-5 rating has been transformed considerably. Shanghai is still the world's biggest container port: it tops the rating for nine years in a row. The leader's container turnover grew by 4.4% and exceeded 42 mln TEUs. Singapore is still ranked second: its volumes increased by 8.7% last year and amounted to 36.6 mln TEUs. The Chinese port of Ningbo-Zhoushan is for the first time among the world's three major container ports by transshipping 26 mln TEUs in 2018 against 24.64 mln TEUs year-on-year. With the turnover of 26 mln TEUs, Ningbo-Zhoushan has got ahead of Shenzhen port (25.74 mln TEUs) that was previously ranked third. Traffic via Guangzhou port (Nansha) amounted to 22 mln TEUs in 2018 that is 8% up year-on-year. As a result, the port moved to rank 5, while Hong Kong with its turnover decreased by 5.4% dropped to rank 7. The port of Busan in South Korea has retained its rank 6. According to the preliminary estimates of BPA Port administration, its container turnover amounted to 21.67 mln TEUs last year. Despite the transshipment growth by 11.5%, the total volume increased by only 5.8% because of the zero growth of foreign trade turnover volumes under a stagnant economy.

Trends in Shanghai Containerized Freight Index



Fleet

The capacity of global container fleet grew by 5.1% in the first three quarters of 2018. For reference, the growth amounted to only 3.8% in 2017. ULCS container ships with the capacity of 12,000 TEUs and more accounted for about 80% of the total growth. According to shipbroker Clarkson, the global capacity increased by 1.3 mln TEUs over the past year, and in 2017 – by 1.1 mln TEUs. At the same time, the retirement rates of old fleet remained very low: only 54 container ships were withdrawn from use. The freight rate growth owing to a rising demand drove the shipowners to postpone ship decommissioning. This was particularly apparent in Panamax segment with a capacity from 4,000 to 5,300 TEUs, as its lease price was doubled and reached almost USD 10,000 per day. The market started slowing down by the end of the year. According to the latest Alphaliner data, early in 2019, about 20 Panamax type vessels had been already idle. In the first three weeks of the year, 10 vessels were decommissioned.



Source: Drewry Maritime Research

Outlook for 2019

According to Drewry Maritime Research estimates, in 2019 the container transportation growth rate decreased to 4.1– 4.4% due to a worldwide economic slowdown linked with potential rise of protectionism and economic deceleration of China being the main driver of container shipping.

The Key Factors that Continue to Affect the Global Container Shipping Market in 2019

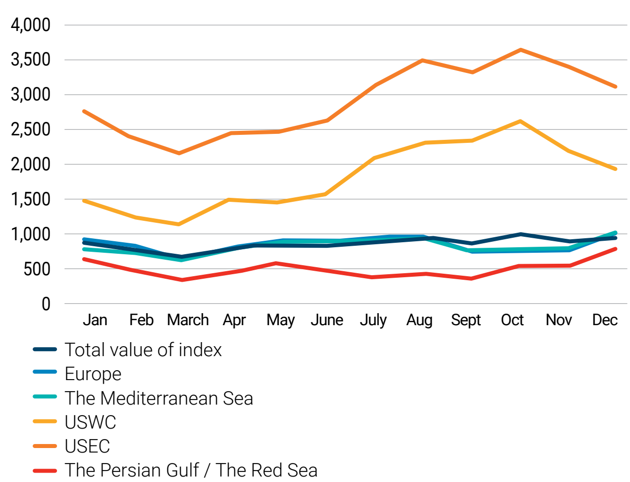
1. The continuing rise of oil price that might have a negative impact on the maritime carriers profitability and overall trends in global demands; risks associated with the sustained transportation supply-and-demand imbalance, as well as risks of aggressive pricing policies of major alliances and independent players for ensuring the market share.

2. Introducing new environmental restrictions on sulphur content in the marine fuel since the beginning of 2020 (so-called IMO-2020 regulations) accelerated the process of fleet modernization and investments in marine emission purification systems.

3. Revising the strategy by terminal and linear operators and shifting priorities to the adjacent segment – Logistics (Maersk, DP World, Cosco, Contship Italia). This trend resulted in an upsurge of interest in feeder operations, and therefore, growing demand for construction of small-size container ships. Eventually, a wave of consolidation in the industry hit the feeder market. In 2018, the Danish feeder operator Unifeeder was purchased by DP World, and CMA-CGM acquired the Finnish operator Containerships. On the other hand, London analysts from Drewry have thus concluded that the industry demand for extra large container ships is satisfied, no big orders are expected, and the market is nearly balanced. However, as early as January 2019, new orders by OOCL and CMA CGM were reported.

4. Political Factor. The previous year clearly demonstrated that the container market is directly dependent on policy. We suggest to take another look at trends in SCFI container index. The rate index for the ports in North America exceeded the 2017 level in May, immediately after the beginning of the trade war between the US and China. And in the last quarter, when the market is always rapidly growing in anticipation of the holidays - and it was so, except for the Trans-Pacific segment - the rates started to drop dramatically as the possibilities of stocking up Chinese goods had been exhausted, while there was again a hope that the conflict could be finally resolved.

SCFI Index for Different Geographical Market Segments



Source: InfraNews

Relatively unfavourable conditions in Asia-Europe shipping market were caused to a large extent by political instability in Europe. First, we should point out the prospect of a UK exit from the EU. Analysts' negative outlook had a significant impact on the market. Also, the adverse political factors include unsafe conditions and escalating separatist sentiment in southern Europe, "anti-European" plans of Italy, crisis in Turkey, etc.

5. The majority of market players recognise that Asia–Europe railway corridor has become a full-fledged shipping alternative that is preferable for specific cargo owner categories. Moreover, this corridor is developing politically, as it is strategically important for Asian countries as a shipping alternative via the Suez Canal in case of rising geopolitical tensions in the Middle East. Thus, the Japanese and Chinese logistics companies have been actively cooperating in establishing a multimode corridor for Japanese goods delivery to Europe. By the estimates of the Eurasian Development Bank, the rail container transportation volumes between China and the EU will reach 1 mln TEUs by 2020, while China expects it to be 2 mln.

6. Integration of container carriers in larger alliances enhanced their negotiating positions. The operators in other market segments are trying to adopt this strategy. Thus, for example, in autumn 2018, ONE and Hapag-Lloyd reached a partnership and vessel sharing agreement (VSA) in relation to feeder operations. In January 2019, four out of the five operators of Hong Kong Port that kept losing its positions announced the establishment of a strategic alliance. They are planning to hand over 23 berths and eight terminals of the deep water area of the Kwai Tsing Port for joint operations. These factors will continue to affect the market in 2019.

The base case scenario for 2019 does not forecast significant changes in the market environment compared to 2018, which bodes well for the Russian container market.