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CONSULTING DEPARTMENT RBC.RESEARCH

RUSSIAN TRANSPORT AND LOGISTICS SERVICES MARKET IN 2010-2011 AND FORECAST TO 2014

The size and structure of the logistics outsourcing market;
freight transportation, forwarding and warehousing services

Analytical Review
Sixth Edition



Demonstration version



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Moscow, 2011

ABSTRACT

This survey is devoted to the analysis of the latest development trends and prospects for the Russian transport and logistics services market. The survey on this subject was conducted for the sixth time.

The work provides a detailed review of the situation in the global and Russian logistics outsourcing markets, quotes the most important performance indicators of the sector in 2009-2010 and estimates for 2011, and contains a forecast for the development of major segments of the logistics market through 2014.

The survey presents, for the first time, comparative analysis between Russia and other countries with regard to such indicators as logistics costs, size of transport and logistics market, logistics outsourcing and 3PL segment.

The section "Global Transport and Logistics Market" contains an analysis of the post-crisis recovery process in major segments of the global logistics market. The markets in the U.S., EU countries and China are studied in more detail, giving a timeline of financial results reported by major 3PL providers in 2010.

The survey of the Russian transport and logistics services is comprehensive in nature and contains a detailed analysis describing the development of major segments such as freight transportation, forwarding (including international operations), warehousing and management services, in 2010 and the first half of 2011. The review provides estimates for the logistics market size, including 2PL and 3PL segments, in volume and value terms.

The section "International Freight Transportation in Russia" contains data on the dynamics and structure of foreign trade freight traffic in 2008-2010 and the first half of 2011. The changes that occurred in the Russian container transport market, including transshipment in ports and carriage by rail, are analyzed.

The section devoted to the Russian warehousing services market analyzes supply and demand in the commercial warehousing property market in 2010, dynamics and structure of the storage and distribution services market, and trends in the development of the logistics market in metropolitan regions and other constituent entities of the Russian Federation in 2011.

A separate section includes an analysis of competitive environment, financial performance of Russian and foreign transport and logistics companies in 2009-2010, as well the market consolidation and growth prospects in the post-crisis period.

The section "Potential for Growth of the Russian Transport and Logistics Services Market in 2011-2014" contains a forecast for the development of Russia's economy and foreign trade (baseline scenario of the RF Ministry of Economic Development) and RBC.research estimates for physical and value indicators of logistics market segments up to 2014.

The survey was conducted in Sept.-Oct. 2011.

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GLOBAL TRANSPORT AND LOGISTICS MARKET

Supply and demand determinants

The main factors that determine the demand for integrated transport and logistics services are dynamics of the global economy and international exchange of commodities, globalization of freight flows and sophistication of delivery schemes, as well as the need to optimize transportation, storage and distribution costs.

The 2009 financial crisis inevitably took a toll on the development of the global transport and logistics market. Some of the direct consequences of the crisis were a fall in production and consumption volumes in developed economies, a reduction in freight traffic and a decline in the demand for the entire range of transport and logistics services amid economic recession.

In 2010, Asian countries played the decisive role in a relatively rapid recovery of world trade following the global 2009 crisis, and it is this region that will determine the dynamics and structure of global freight flows and demand for transport and logistics services in the years immediately ahead. However, unlike in the previous period, the most important elements in the development of these countries will be focus on expanding their own markets and stimulating domestic demand and consumption.

Extraordinary measures taken by governments of developed and developing countries have allowed the global economy to overcome the recession, but the growth is not steady yet. In 2010, the growth rate was 5.1%, with advanced economies expanding by 3.1% and developing economies by 7.3%. 2011 and 2012 are expected to see “moderate growth” and exhaustion of the “post-crisis recovery” effect.

There are still high downside risks stemming from the following factors:

- Increased fiscal and financial uncertainty, growing government debt in the Euro Area.
- Downgrading of the U.S. sovereign credit rating.
- Low domestic demand in advanced economies.
- A danger of a new investment “bubble” and inflation growth in developing countries due to massive inflow of speculative capital; emerging market economies may well suffer more adverse export conditions and even more volatile capital flows.
- Events in North Africa and Japan...

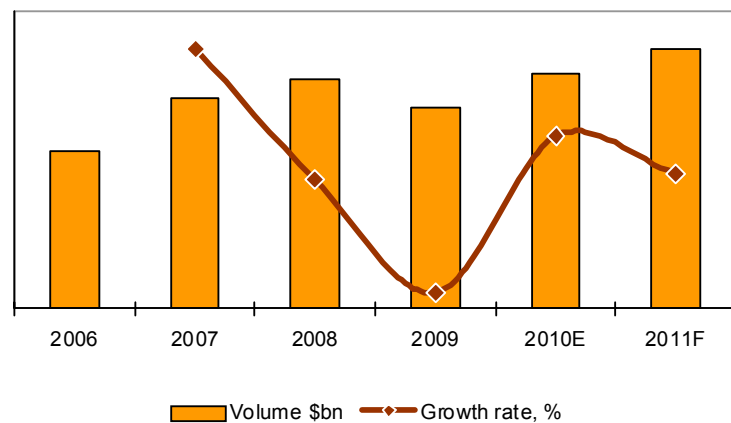
Market segments

Dynamics and structure of the global transport and logistics services market

The volume of the global transport and logistics market in 2010 is estimated at \$6.3 trillion with aggregate logistics costs of \$7.7 trillion (about 11% of global GDP)...

According to estimates by international research agencies, in the aftermath of the 2008 global crisis the growth rate of the global transport and logistics market slipped to 9% and its size shrank by 12% in 2009. In 2010, however, the market growth rate turned out to be twice as high as forecast and reached XX%...

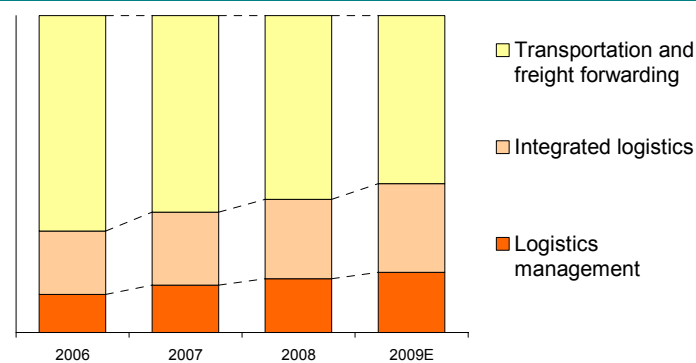
Global transport and logistics market, 2006-2011, \$ billion



Sources: Companies' data, RBC.research estimates

Logistics outsourcing (2PL, 3PL and 4PL)¹, estimated at \$XX trillion in 2010, accounts for about 55% of the world transport and logistics market volume, with 3PL and 4PL operators' services accounting... In 2010, freight transportation and warehousing services again became the key market growth driver...

Structure of the global transport and logistics services market, 2006-2010, %



Sources: Armstrong & Associates, RBC.research estimates

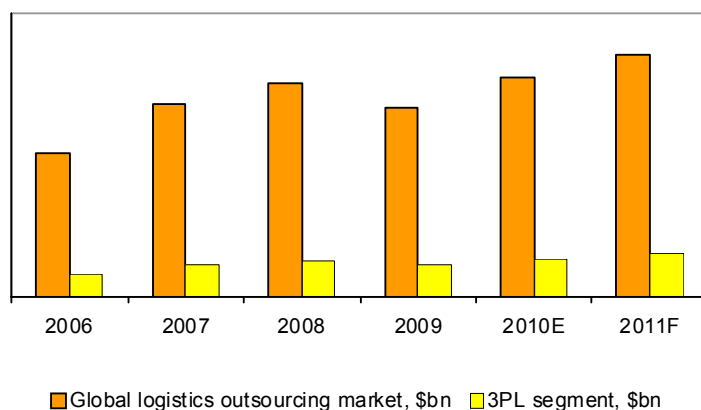
According to RBC's estimates based on operating results of major logistics providers, the decline in the 3PL market in 2009 was at least XX%... In 2010, the 3PL market grew by XX% in dollar terms, gaining back the losses incurred in the crisis year and exceeding the 2008 level. The market's growth in 2011 is expected to be...

¹2PL – Second Party Logistics (outsourcing). 2PL companies offer the traditional package of services including cargo transportation and simplest storage operation management.

3PL – Third Party Logistics. 3PL providers offer a wide range of services with a considerable value added and possible subcontracting.

4PL – Fourth Party Logistics. The basic function of logistic system integrators is planning and coordination of client information flows and supply chain optimization, including integration of company's clients, customers and suppliers.

Volume of the global logistics outsourcing market and 3PL segment, 2006-2011, \$ billion



References: Gross revenue of 3PL providers

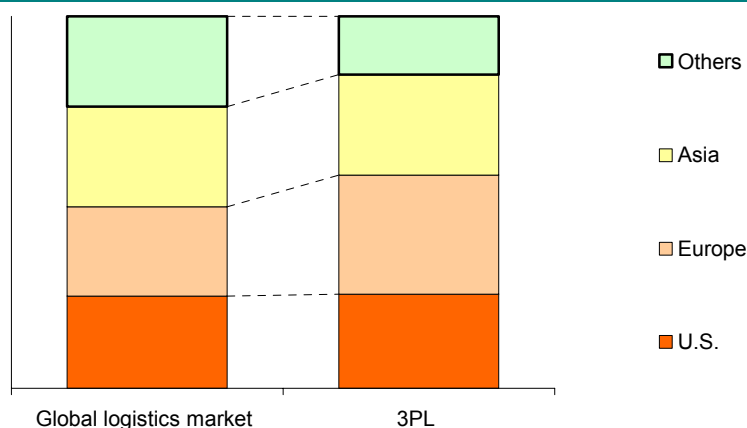
Sources: Armstrong & Associates, companies' data, RBC.research estimates

Geographical structure of the global 3PL market

According to an update from Armstrong & Associates, the most developed and mature transport and logistics market is in Europe. Ranking third in the world in the amount of logistics costs and the size of the transport and logistics market (24% in 2009), European countries contribute over 32% to global 3PL revenue...

The share of Asian countries (primarily, China) in the global 3PL market is growing. Total revenue of 3PL operators on the Asian market, including China, Japan and India, reached... The third position is held by the North American 3PL market with \$128.1 billion in 2009. However, at the country level the U.S. market remains the leader with...

Geographical structure of the global logistics market and 3PL services segment, 2009, %



Sources: Armstrong & Associates, RBC.research

RUSSIAN TRANSPORT AND LOGISTICS MARKET

The operation of Russia's transport industry in 2010 was characterized by transition from slump and stagnation to growth... In January - June 2011, the volume of commercial freight transportation by all modes of transport (excluding pipeline and non-public rail transport) and commercial turnover increased year-on-year by ...

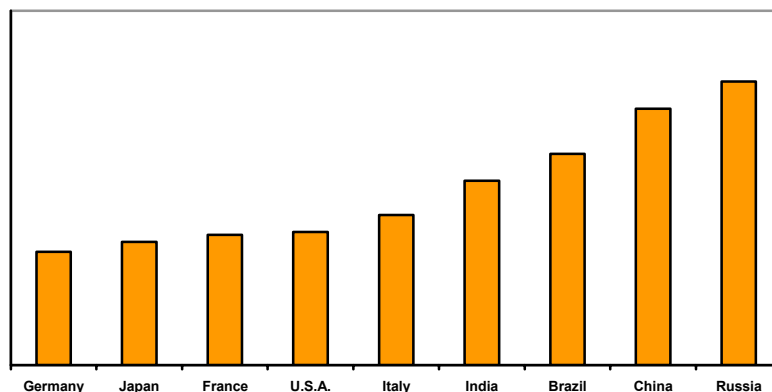
In general, the transport and logistics market managed to overcome the effects of the crisis, though the growth is not stable yet. The slow recovery of consumer and investment demand in Russia, the uncertain situation on global commodity markets, the general slowdown in growth rates of the global and Russian economy compared to 2010 will have a restraining effect on the market growth dynamics in 2011-2014...

Logistics costs, transport and logistics market, 3PL services: international comparisons

Russia stands among countries with a high level of logistics costs², which significantly impairs production and trade efficiency, negatively affects competitiveness of companies and of the country in general. The share of logistics costs in Russia's gross domestic product exceeds 20%, as compared to 18% in China, 13-15% in Brazil and India, 9.4% in the U.S., 10.6% in Italy, and 8.7% in Japan and Germany, respectively. The average global level is 11.4%.

The high level of logistics costs in Russia is mainly associated with inefficient internal logistics within companies and the national transport and logistics system in general, multiplied by huge distances and low quality of Russian roads, non-rational location of many manufacturing facilities, and archaic organization of cargo delivery from manufacturer to consumer...

Logistics costs in different countries of the world and Russia, 2009, % of GDP



Sources: *Armstrong & Associates Inc., RBC.research*

Logistics outsourcing in Russia (value of cargo transportation, forwarding, warehousing and handling services, plus management services) estimated at \$XX billion in 2009 accounts for some 30% of total transport and logistics market...

The bulk of freight transportation and warehousing services in Russia, and the more so of stock and supply chains management services, are performed by own transport and logistics units of manufacturing plants, distributors or retailers, which handle over XX% of total logistics operations.

Another peculiarity of Russia's transport and logistics market is a high share of oil and gas transportation by pipelines, with the increasing contribution of pipeline transport to market turnover. In 2010, the revenue earned by companies (predominantly by Transneft and Gazprom) from oil and gas transportation by pipelines totaled...

² Logistics costs are expenses related to logistics operations (placing purchase orders, procurement, warehousing of delivered products, in-plant transportation, interim storage, storage of finished products, shipment, outbound transportation, etc.).

Comparison of GDP, logistics costs and key indicators of transport and logistics markets in the U.S., Europe, China and Russia, 2009, \$ billion

Country	GDP	Logistics costs	Transport and logistics market volume	Logistics outsourcing	3PL services
U.S.A.
Europe
China
Russia
World

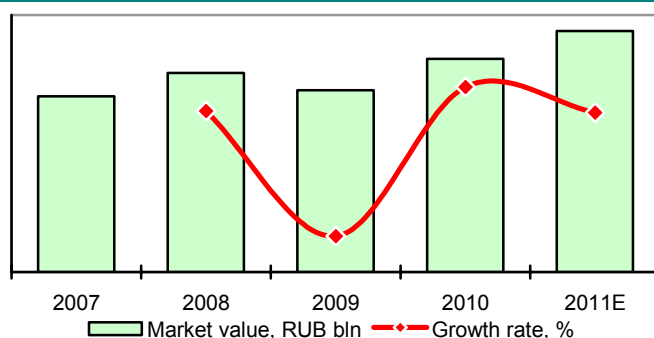
References: Transport and logistics market volume, incl. oil and gas transportation by pipelines.

Sources: Armstrong & Associates Inc., KPMG, RBC.research

Volume and structure of the logistics outsourcing market

The dynamics of physical indicators and turnover in general corresponded to trends on the global transport and logistics services market. The sharp decline in the market value measured in US dollars was caused by the fall of the ruble's exchange rate... In 2010, the market's volume not only recovered to the pre-crisis level, but even exceeded it by...

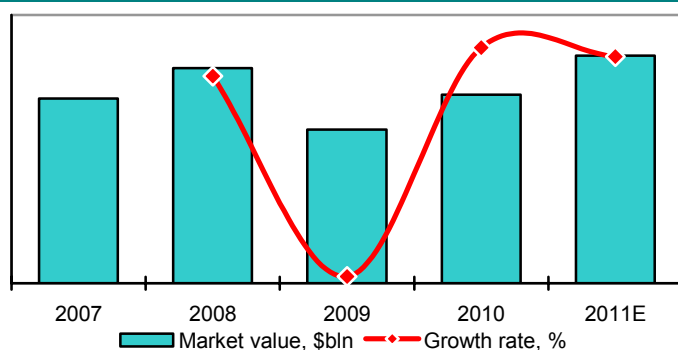
Dynamics of the Russian transport and logistics services market (logistics outsourcing), 2007-2011, RUB billion and %



References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

Sources: Rosstat, companies' data, RBC.research estimate

Dynamics of the Russian transport and logistics services market (logistics outsourcing), 2007-2011, US\$ billion and %



References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

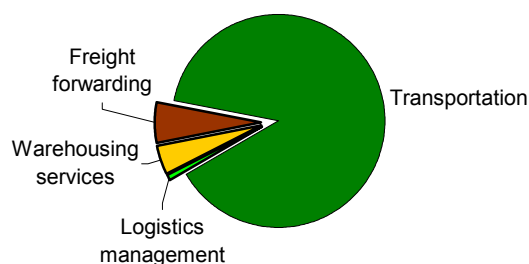
Sources: Rosstat, companies' data, RBC.research estimate

The main growth factor for the Russian transport and logistics services market in 2010 was an increase in freight transportation volume (primarily by rail) amid higher rates. The inflation component of the market growth rate in 2010 was no less than 10%...

The core of the logistics outsourcing market is formed by freight transportation and forwarding services (about 95% in 2010). Compared to 2008, the market structure experienced certain changes related to an increase in the share of freight transportation in the market volume and a reduction in value-added services...

The value of the transportation services market is defined as the total revenue derived by carriers from cargo transportation. The "forwarding surcharge" for cargo transportation varies between 5% and 15% and may reach 18 to 20% in international traffic.

Structure of the Russian transport and logistics market by type of services, 2010, %



Source: RBC.research

The growth of freight revenues (in current rubles) in 2010, including transshipment in ports and airports, is estimated at about XX%. The highest year-on-year growth rates were recorded in rail, road and air transport. Revenues in the forwarding services segment grew by XX% on average.

Volume of Russian transport and logistics services market segments, 2008-2010, RUB billion



References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

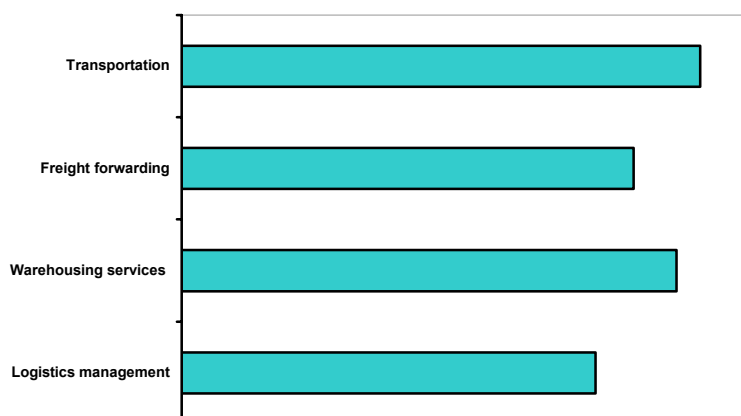
Sources: Rosstat, companies' data, RBC.research estimate

According to RBC's estimates, the growth in the warehousing services segment in ruble terms in 2010 was about XX%. This growth mainly came from rises in rental rates and a decrease in vacancy rates in Class A and B warehouses amid slack growth of supply of high quality warehouse facilities for commercial use.

The volume of the warehousing services market in value terms includes: cost of lease of storage space in commercial use, operating expenses and cost of safekeeping services. Safekeeping in quality warehouses is regarded as an integrated logistics service – from acceptance of cargo in the warehouse through to its dispatch to the client.

The total volume of the transport and logistic services market grew by XX% in 2010 compared to 2009...and value-adding segments such as forwarding and management logistics failed to overcome the effects of the crisis and restore their volumes.

Growth of Russian transport and logistics services market segments, 2010 versus 2008, %



References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

Sources: Rosstat, companies' data, RBC.research estimate

According to RBC's estimates, in 2011 the growth rate of the transport and logistics services market is expected to fall to XX%... Freight turnover of transportation companies will increase by X%; as a result of rises in cargo transportation rates, revenue generated by transportation companies may grow by XX%. Approximately the same growth rates can be expected for companies providing forwarding services. Revenue in the segments of warehousing services provided in quality warehouses and management services might grow by...

The structure of the Russian logistics outsourcing market is dominated by 2PL services; the share of value added 3PL services does not exceed X%, and the share of gross revenue of logistics providers in market turnover is...

Volume of 2PL and 3PL segments of the Russian transport and logistics services market, 2010, \$ billion, %

Market segment	Total	2PL	3PL	Share 3PL, %
Freight transportation
Freight forwarding
Warehousing services
Logistics management
Total

Source: RBC.research

The low share of 3PL services in the turnover of the logistics outsourcing market is largely attributable to the existing structure of production and, accordingly, freight flows in Russia, which are characterized by domination of raw materials and semi-finished goods – hydrocarbons, ore, coal, mineral fertilizers, timber and sawn lumber. Their delivery from manufacturer to consumer (within the country or to the border) is mainly provided by rail transport under contracts with transportation and forwarding companies or carrier companies

(primarily with JSCo RZD and its subsidiaries, and independent rolling stock operators) with a minimal forwarding surcharge...

Volume of the Russian 3PL market (gross and net revenue of 3PL providers), 2007-2011, \$ billion and %

Parameter	2007	2008	2009	2010	2011E
Gross revenue, \$bn
Growth rate, %
Net revenue, \$bn
Growth rate, %

Source: RBC.research

A more detailed analysis of the trends in the development of key segments of the transport and logistics market in 2009-2010 and estimates for 2011 as well as a forecast to 2014 are provided in the sections dedicated to freight transportation, warehousing logistics and market growth potential.

Competitive environment

The competitive environment in the Russian transport and logistics services market is generally determined by activities of Russian companies. However, key players in the 3PL services segment are commonly considered to be western logistics providers that have wide experience in servicing major manufacturing and trading companies on a global scale. As a rule, the scope of operations of western logistics providers on the Russian market depends on the activity of their regular customers in Russia...

According to RBC's estimates based on data of companies and National Credit Bureau, the revenues of TOP 30 transportation and logistics companies (excluding JSCo RZD) in 2010 amounted to about \$X billion³.

In terms of turnover, the leaders are Russian transport holdings that include carrier companies and port operators, which possess considerable assets in the form of vehicles, terminals, warehousing complexes and expand their business by creating (or acquiring) specialized logistics divisions operating in the 3PL segment.

The first two positions in the list of largest transportation and logistics companies (with a turnover in excess of \$950 million) are occupied by diversified transport holdings N-Trans Group and Universal Cargo Logistics Holding. The third position is held by Sovfracht-Sovtmortrans Group, which increased its turnover by nearly 30% in 2010.

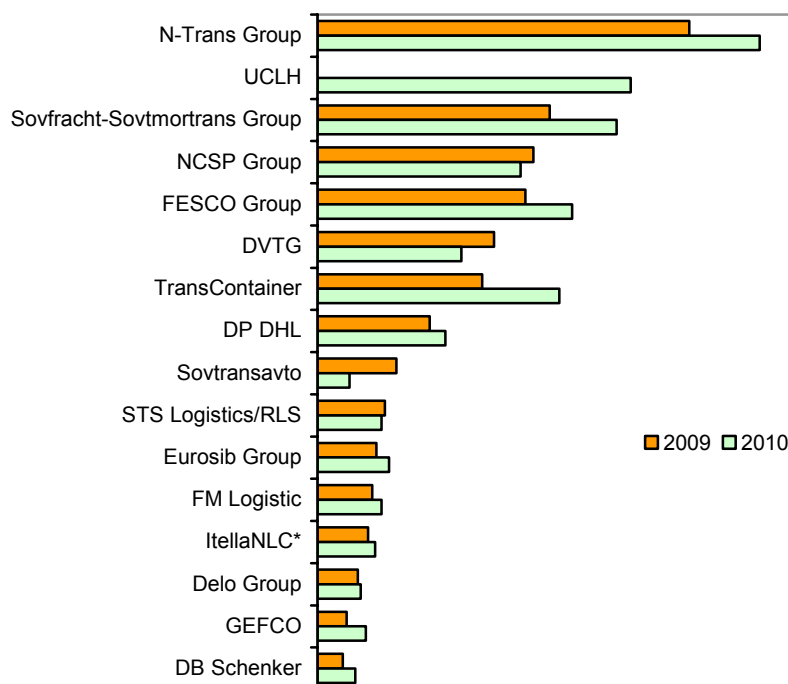
The aggregate turnover of the other three leading transport holdings (FESCO Transportation Group, DVTG and NCSP) is estimated to be within ...

The group of companies with revenues from \$100 million to \$400 million is headed by DP DHL, which managed to increase the volume of operations in Russia after a fall in turnover in 2009. Here also belong...

Most of the TOP 30 logistics companies have a turnover between \$30 million and \$100 million. According to RBC's estimates, this group also includes western 3PL providers...

³Gross revenue of transportation and logistics companies can generally include the cost of services provided by third-party carriers, including carriage by rail, which leads to double-counting of market turnover.

Revenues of the largest transportation and logistics companies operating in Russia, 2009-2010, \$ million



References: The data for foreign logistics operators include the revenues of companies registered in Russia and filing financial statements under Russian standards, translated into US dollars at the annual average exchange rate.

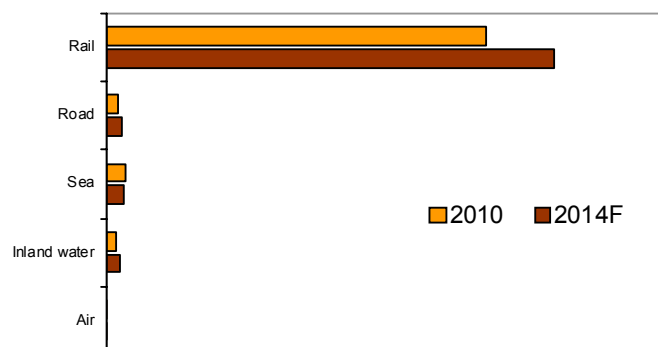
Sources: Companies' data, National Credit Bureau, RBC.research estimate

GROWTH POTENTIAL OF THE RUSSIAN TRANSPORTATION AND LOGISTIC SERVICES MARKET IN 2011-2014

Freight transportation market

The development of freight transportation market in 2011- 2014 is projected to take place amid the gradual recovery of growth rates of the economy, industrial production and physical volume of exports and relatively more dynamic growth of imports. In 2011, commercial transport will exhibit relatively high growth rates as the process of recovery of freight traffic after the crisis of 2009 is completed, but in 2012-2014 average year dynamics are projected to slow down...As before, overall dynamics of the industry will be determined by rail transport, where freight turnover growth rates, after some reduction in 2012, will reach...

Forecast for growth of freight turnover of transportation companies by mode of transport, 2010-2014, billion t-km



Sources: RF MED (September 2011 forecast), RBC.research

According to forecast by RBC.research, in 2011-2014 the value of the freight transportation market in current prices may grow from RUB X billion to RUB X billion. With revenues from cargo transshipment in ports and airports, the turnover in the Russian transportation services market in 2014 may exceed...

Forecast for changes in the volume and structure of the Russian transportation services market (including revenues from cargo transshipment in ports and airports), 2010-2014, RUB billion, %

Mode of transport	Volume, RUB bn, 2010	Share, 2010, %	Volume, RUB bn, 2014F	Share, 2014, %	2014/2010, %
Rail
Road
Sea
Inland water
Air
Cargo transshipment at air and water ports
Total
Freight transportation

Source: RBC.research

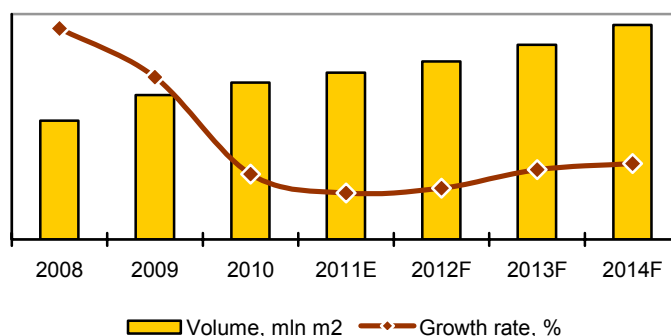
Warehousing services market

The development of the Russian market of quality warehouse property and storage and warehousing and distribution services in 2011-2014 will be determined by the following factors:

- ✓ In spite of the fact that the market was showing stable growth throughout 2010, developers started to display activity only in the second half, when it became clear that rental rates had approached a level that could ensure an acceptable payback period for new properties. As a result..
- ✓ The outrunning growth of absorption volume alongside the low rate of commissioning of new projects will lead to further reduction of vacancy and rise of rental rates...
- ✓ A relatively slow growth in the amount of new warehouse completions in 2012-2013 will be associated with the long cycle of creation of new warehousing complexes (14-18 months). Since there was no new construction almost in all regions except the metropolitan area, significant growth of supply on the lease market can be expected only...

- ✓ The share of logistics operators in the structure of demand on the lease market is expected to continue its...
- ✓ The bulk of the supply in 2012-2014 will remain concentrated in the Moscow Region, given the high potential of the metropolitan market where the demand for warehouse property and 3PL services, including storage, distribution and supply chain management, is concentrated...

Forecast for dynamics of the amount of high quality warehousing space in Russia, 2008-2014, million m²

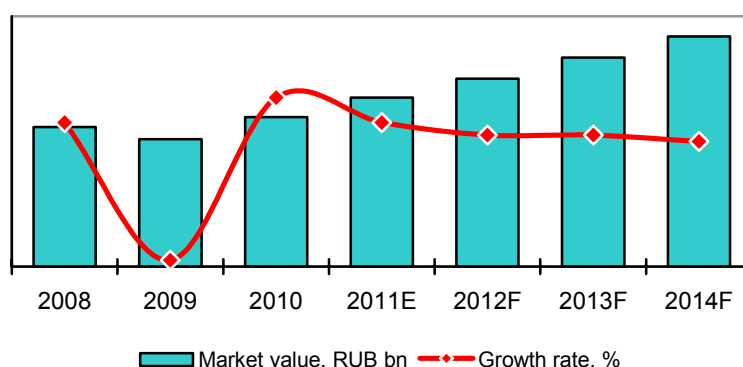


Source: RBC.research

Forecast for dynamics of the transportation and logistics services market

According to estimates by RBC.research, taking account dynamics of freight turnover and tariff component of freight transport as well as changes in the demand and rental rates in the warehousing segment, the growth rate of the transport and logistics market in 2012-2014 may amount to 10-11% per year, and in 2014 the market volume will exceed the 2010 level by 54%.

Figure 1. Forecast for dynamics of the Russian market of transportation and logistics services, 2008-2014, RUB billion and %

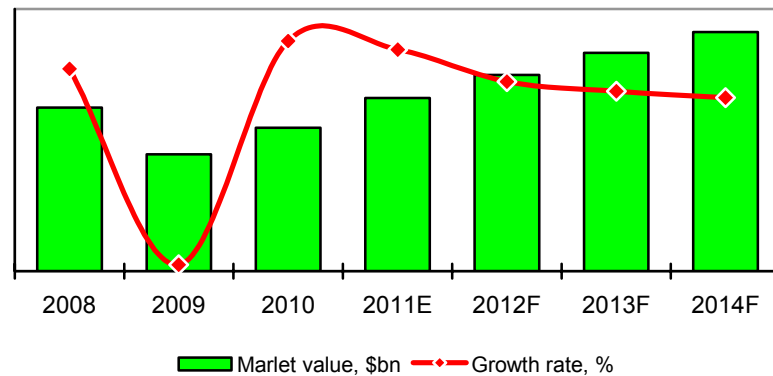


References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

Source: RBC.research estimate

According to the calculated average annual exchange rate of the ruble against the dollar for the forthcoming years (forecast by the RF MED), in 2014 the volume of the market of transportation and logistics services in dollar units may increase by...

Forecast for dynamics of the Russian market of transportation and logistics services, 2008-2014, \$ billion and %



References: Including revenues of cargo handling at airports and ports, and independent private rail operators, in current market prices.

Source: RBC.research estimate

Forecast for dynamics of the value of Russian transportation and logistics services market segments, 2008-2014, RUB billion, %

Market segment	Parameter	2008	2009	2010	2011E	2012F	2013F	2014	2014/2010, %
Cargo transportation	RUB billion	...	...	...	...	...	...	...	...
	Index, %	...	...	...	...	...	...	...	...
Freight forwarding	RUB billion	...	...	...	...	...	...	...	...
	Index, %	...	...	...	...	...	...	...	...
Warehousing and distribution services	RUB billion	...	...	...	...	...	...	...	...
	Index, %	...	...	...	...	...	...	...	...
Logistics management	RUB billion	...	...	...	...	...	...	...	...
	Index, %	...	...	...	...	...	...	...	...
Russian transport and logistics services market	RUB billion	...	...	...	...	...	...	...	...
	Index, %	...	...	...	...	...	...	...	...

References: Cargo transportation incl. transshipment at air and water ports, in current prices

Source: RBC.research estimate