Table of Contents

1. Background

- Crisis after crisis – since early 2020 we have seen:
    - Low and very unpredictable volumes
    - Absence of forecasts due to this unpredictability
    - Consequent low efficiency in operations
    - Significant financial losses by most LSPs
    - Reduction in capacity and resources generally
    - Labour shortages
    - Material shortages
    - Significant cost increases in many areas, especially raw materials such as steel driving asset costs up
    - Consequent halt in most investments

  And so to war…
    - Massive cost increases - not just in fuel and energy
    - Inflation, and now interest rates, rising fast
    - Costs in FVL mostly rising far faster than headline inflation rates in the press
    - Driver shortage hugely exacerbated by Ukrainians and others leaving – many trucks are parked up
    - Any contract signed before the war is certainly now loss making
- Despite this background and the risk of recession, volumes are expected to start slowly recovering – but confidence in the market is extremely low

2. Mode by mode

2.1. Road Transport

- Most large fleets have disposed of hundreds of trucks since 2020
    - A straw poll of 6 larger operators shows that between them they have reduced by **1,500** trucks which equates to a **27%** loss of capacity
    - In most cases these transporters have been scrapped and not sold, so the capacity is lost completely
- An additional 5-10% of trucks are now parked up on any given day due to the driver shortage
- Many small operators that historically worked as sub-contractors have exited the market and turned to general haulage – an undocumented capacity loss
- Driver shortage is global and has existed for decades but is now becoming truly critical
    - FVL finding it harder than ever to persuade drivers to drive transporters – in comparison with general haulage the job is hard, dangerous, thankless and, for many, involves extensive roaming in trucks with small cabs
    - According to the IRU, up to 425,000 truck driver positions in Europe, 10% of the total, remained unfilled in 2021, forecast to jump to 14% by the end of 2022 – 600,000 jobs!
- OEMs have disrupted the market in trying to secure capacity
- Some have contracted dedicated trucks which reduces industry efficiency and further reduces capacity

- Some have turned directly to the spot market which has vastly inflated rates and disrupted the normal working of the industry - larger LSPs contracted to OEMs can no longer get sub-contractors and operate their networks efficiently
- Some have changed their distribution networks and contributed to less efficient operations in the sector

2.2. Short Sea Shipping

- Capacity has been reduced generally
- Older vessels scrapped or sold to the Far East – more will follow
- Many ships deployed outside Europe (Asia) to meet demand - **estimates put this at more than 15 vessels!**
- Order book for new vessels at a historic low – last mid-size vessel on order will deliver soon, though deep sea ships are being built
- Lead times are at historic highs – order now for 2026/27 delivery!
- Shortage of dock labour persists
- Congestion in some key ports continues to significantly impact on efficiency with thousands of 'lost' days in the first half of 2022 equating to 10-15% of capacity

2.3. Rail Transport

- Some older wagons have been scrapped
- Capacity in traction has also reduced
- Plus - huge infrastructure problems, especially in Germany
    - More than 1,000 major construction works
    - Many other smaller ones that result in short notice track closures
    - Track closures mean diversion over longer routes which effectively means more resource is needed. On average 20-30% more!
    - Disruption will last a <u>minimum</u> of 10 years
- Combination of these 2 factors means 35-40% shortage of capacity – at least for the German market
- Traction does not want to work for FVL – unpredictable sector
- Train driver shortage – full employment
- In Germany shipments of war materiel and energy (e.g. coal) are prioritised over other freight
- Shortages equate to hundreds of trains per day across the industry, estimated at 500+
- FVL has become much less reliable as a result

3. How do we rebuild the industry?

3.1 General

- Restore confidence
    - Long-term partnership approach with more balanced contracts and sharing of risk
        - Change is already being seen but needs to be industry wide
        - Contractual relationships need to address issues such as:
            - Minimum volume guarantees
            - Better planning/forecasting/communication

- Respecting payment terms (especially as interest rates rise)

3.2 Road and shipping

- Investment is needed but no-one will invest without confidence in future volumes and the reasonable expectation of profitability
- Unpredictability remains with material and supply chain shortages
- Factors impacting confidence include:
    - Ongoing war
    - Looming recession
    - Continuing semi-conductor shortage (VDA quotes “at least 2025”)
    - Potential closure of German plants due to gas shortages (warned by VDA)
    - China/Taiwan situation could have enormous impact on semi-conductor supply
- Even if confidence returns today it will take:
    - 15 months to put a new transporter on the road – and you will still have to find a driver for it!
    - 4-5 years (!) to put a new vessel on the water

3.3 Rail

- Will not be solved by investment from LSPs
- Issues are mostly a result of (very) long-term lack of investment in rail infrastructure across Europe
- European Commission very good at promoting use of rail / modal shift e.g. Shift2Rail but have almost completely failed to deliver on infrastructure and progress towards a single market for rail
  There is not even light at the end of the tunnel!

3.4 And do it sustainably……

Against this challenging background the industry still needs to decarbonise

- This again is largely an issue of investment
- Some shipping lines investing heavily in greener assets
- Some OEMs already pushing hard for ‘green’ road transport, but….
    - Electric trucks are 3^{+} x price of ICE
    - There is no infrastructure in place…
    - …. and no green power to charge/fuel them

4. Summary

This is not a short-term problem, and potential solutions are few.

Some, such as the driver shortage, will require political and social change that will take many years.

ECG predicts that demand in the FVL sector will exceed capacity in Europe for a minimum of 5 years, even if action is taken today.

5. Updates

5.1 March 2023 update

Four months on from when this report was first published much has changed and there is evidence of confidence returning to the market. Many problems also remain of course, and the FVL industry remains heavily impacted by lack of capacity. What is now becoming a major factor in the overall situation is a fragmenting of the market with shippers taking control of dedicated resource that reduces the efficient use of assets even more.

5.2 Mode by mode

5.2.1 Road transport

Since December 2022 significant orders have been placed for car transporters. Lead times for trucks remain long, typically around 15 months, but with the economic downturn there are cancelled orders from the general haulage industry that have freed up some spots for delivery this year. The trailer manufacturers are scrambling to build back capacity having scaled back massively and, as with many sectors, staff are hard to find. As a result, lead times now extend well into 2024 and there is no possibility to increase the asset base any faster in the current year. In fact, current production rates are really only renewing the fleet and not expanding it.

The downturn in general haulage is also freeing up some truck drivers which is offsetting the driver shortage in the short-term. However, the efficiency of the overall fleet is now being severely impacted by several factors.

- Transporters being leased for dedicated use by a few customers are very inefficient to operate.
- Port congestion has led to changes in networks and the use of new ports as well as restrictions on access to port terminals due to congestion.

Both of these factors have dramatically impacted efficiency with increased levels of empty running and have reduced the overall capacity of the market.

Underlying this, of course, the driver shortage remains and is the subject of a Dinner Debate that ECG will host in the European Parliament on 21st March. We are pleased to see that that European Commission is, at last, proposing to allow licences to be issued at the age of 18, which is a big step forward, but much more action is required.

Sadly, new laws frequently have unintended consequences, and we see this with the recent Mobility Package which changed the rules, amongst other things, on cabotage. We now see instances of networks being changed so that a single long national trip (e.g. from South to North Germany) is made into two international trips with a stop in another country. The result is more kilometres driven and consequent inefficiency. More worrying is the new requirement for trucks to return to the country where they are registered at least every 8 weeks. For many trucks from countries in Eastern Europe this means running empty back, especially while market demand in these countries is very low, and being unproductive for a number of days. This crazy situation is increasing emissions and costs significantly, as well as further compounding the capacity problem.

Another factor having a negative impact is the increasing weight of the vehicles being carried as electrification gathers pace. We are seeing reducing load factors which again requires more transporters to move the same volume.

5.2.2 Shipping

Here too we see confidence returning with increasing order books for ro-ro vessels. The following quote from VesselsValue provides a good summary:

"Marginal improvement to Vehicle Carrier (LCTC, PCTC) supply is expected this year based on 12 vessel deliveries, compared to ultra-low demolition activity predicted at 4 vessel removals by VV averaging 5,205 CEU per ship. This is because shipowners are likely to keep vintage units trading for longer in order to capitalise from a highly lucrative charter market rolled over from 2022.

However, 45 vessels are scheduled for delivery in both 2024 and 2025, compared to vessel removals at less than half the delivery rate. Firming net fleet growth by c.+7% in 2024, and c.+8% in 2025, adding half a million CEU to the sector's total capacity of 4m CEU based on 782 live ships today.

A narrowing of the supply-demand imbalance is therefore expected in 2024, followed by a balanced market in 2025 after new increased sized ships begin trading regularly in deepsea liner services. Creating a cascading effect as smaller, midsize tonnage returns to minor deepsea and intraregional shortsea routes, rebalancing capacity across all liner services.

The orderbook has swelled over the last 12 months which is positive for OEMs. No midsize or small PCTCs were ordered last year which is ominous for shortsea LV trade. OEMs …have increased their chartering activity of late taking deepsea tonnage on 5-year deals. An interesting trend to watch, along with LV trade volumes flowing into Containers."

Worryingly, 5 or 6 more vessels are expected to leave European waters this year for the Asian market which, combined with the lack of any new short-sea tonnage, causes further concern. While VesselsValue expect global capacity to catch up with demand in 2025 the short-term offers few solutions. The dramatic shift to containerization in recent months being driven by this as well as the huge fall in container rates as ro-ro rates have risen.

Port congestion also continues, with vessels either being forced to wait for extended periods or to add additional ports to their rotations to unload vehicles in places not normally used for automotive. This again is an issue that impacts the overall capacity of the total fleet.

Terminal operations are also impacted with many close to gridlock. The reduced number of vessels means that, on some routes, the frequency has reduced and the numbers on each vessel are higher with more space then needed to operate. Some terminals are restricting port calls, either reducing the numbers of vehicles or sometimes closing completely to ships. The space issues in terminals are also causing limitations for trucks with numbers being restricted in various different ways. Again the reduced sailings affect this as dwell times have increased so export cargoes are controlled resulting in restrictions on the trucks and trains delivering them.

5.2.3 Rail

Little has changed here and the reduction in capacity stemming from the infrastructure problems, principally in Germany, continues to put increased pressure on other modes, mostly road. Over the winter of 2022/23 things have improved, with lower volumes than expected and improved circulation times, but even so wagons remain in tight supply. However, coming into Spring the infrastructure works ramp up again and there is also a likelihood of industrial action in Germany in the months ahead.

Looking ahead there are few new wagons on order and anyway production capacity is limited with current lead times into 2025.

5.2.4 Summary

Overall there remains little positive news in the short term simply because assets cannot be created overnight. Capacity everywhere in the FVL sector remains exceptionally tight with efficiency of assets and other operations all negatively impacted by the situation. Looking further ahead things look more positive with investments being made, but 2023 will be a challenging year for the industry across Europe.