

REVIEW OF CUSTOMER CHOICE IN THE FREIGHT LOGISTICS SECTOR BETWEEN THE UK AND THE CHANNEL ISLANDS

A report for CICRA

9 June 2017



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EXECUTIVE SUMMARY

Background and context

As both Jersey and Guernsey are island economies, they are heavily dependent on the transport of goods by sea. Goods are generally carried by road within the Channel Islands and then transported by sea to and from either France or the UK. In recent years, the market for freight logistics in the Channel Islands has seen a number of changes, including exit, entry and consolidation. CICRA has received concerns from market participants around how this sector is working. CICRA is therefore carrying out a market review of this sector, with the initial focus on the choices available to customers when selecting a freight transport provider. CICRA has engaged Frontier Economics and SYSTRA to assist in this review.

Objective of this report

The objective of this report is to understand if freight market customers are satisfied with current market outcomes on the following aspects, as outlined in CICRA's Terms of Reference:

- the factors customers take into account when selecting a freight transport provider (e.g. cost, resilience, reliability, etc.);
- customers' views on the adequacy of choice of freight transport providers when bringing goods into the Channel Islands; and
- the frequency of switching between freight transport services and any perceived barriers to such switching.

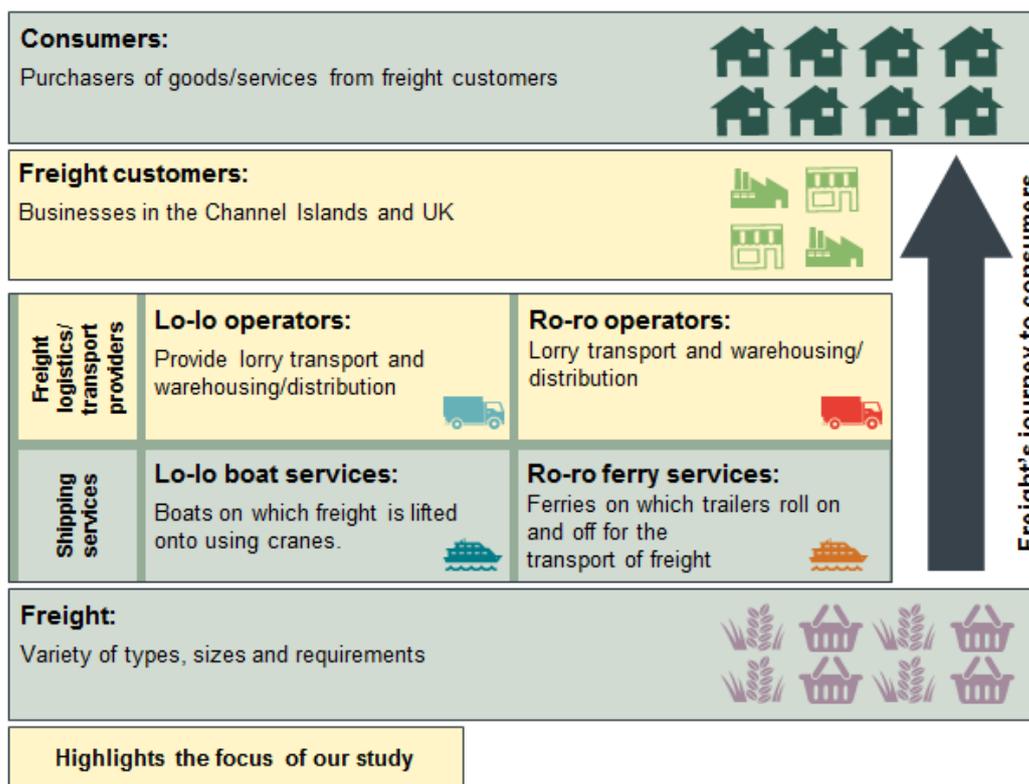
In addition, we consider the extent to which current outcomes are likely to be sustained in the future.

How is the market for freight structured?

Figure 1 provides a schematic overview of the supply chain for sea freight services¹ between the UK and the Channel Islands.

¹ In general, freight can be transported either by sea or by air. Air freight is a specialist service, with limited capacity and cost exceeding four times that of sea freight. Therefore it is not considered within the scope of the review. Furthermore, within sea freight, there exist three methods of shipping, these are: ro-ro, lo-lo, and bulk freight. Bulk freight involves the transportation of unpackaged, mainly commodity, goods, independently of logistics companies. As a result, it falls outside of the scope of this review.

Figure 1 Overview of supply chain for sea freight



Illustrative only

However, we discuss these stakeholders as well as the wider supply chain i.e. the shipping providers, in further detail below.

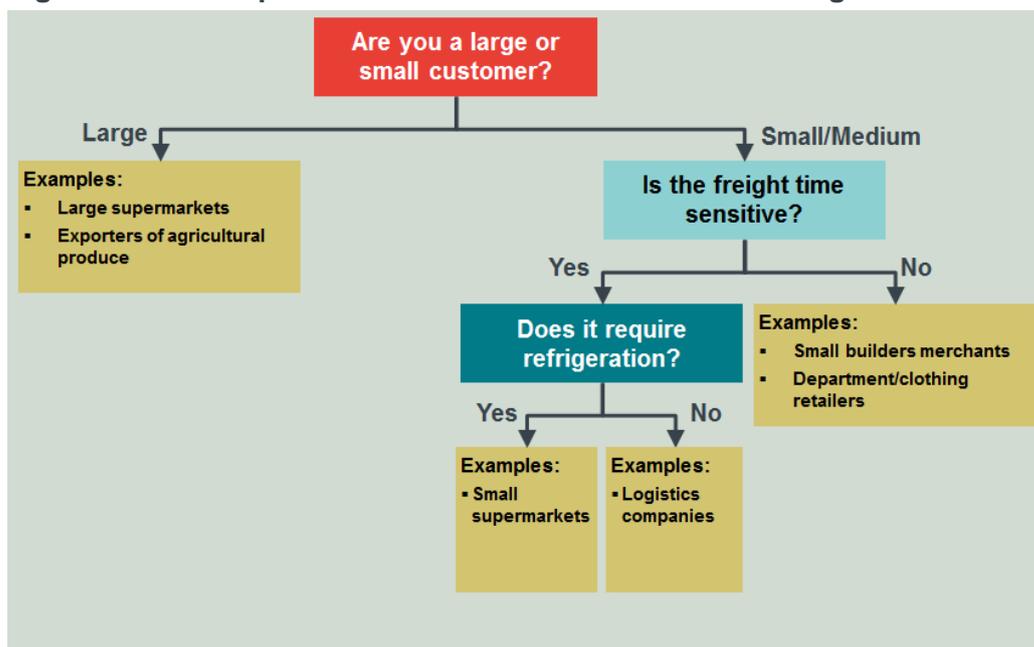
Freight customers

By virtue of being islands, the majority of businesses in the Channel Islands are freight customers (“customer”) as they will need to import/export freight. End-consumers purchase goods and services from these businesses. This means that there is a diverse range of different sized customers with a variety of requirements, including:

- **Large customers** are typically either large retailers such as supermarkets or large exporters of freight such as agriculture produce. They tend to require daily, refrigerated freight services.
- **Small or medium sized customers** include smaller supermarkets/wholesalers that will require refrigeration and possibly just-in-time delivery. It will also include a large number of retail and other businesses that only require ambient (i.e. non-refrigerated) services. This group also includes low volume customers who only ship occasionally. As a result, they are less likely to require speedy delivery.

Figure 2 summarises the different segments of the market and provides examples of the types of business in each segment.

Figure 2 Examples of customers in each market sub-segment



Source: Frontier Economics

Freight logistics/transport providers

There are two forms of this service, both of which deliver to customers' premises:

- **Roll-on, roll-off (ro-ro) operators:** They transport freight in trailers using lorries that are then rolled on and off ferries; and
- **Lift-on, lift-off (lo-lo) operators:** They transport predominantly containerised freight, which is lifted on to ships using cranes and then transported to its end destination via lorries.

They have been referred to as “freight logistics providers” and “freight transport providers” interchangeably in this report.

Shipping providers

There are two forms of this service:

- **Ro-ro ferry service providers,** these are separate entities from ro-ro operators who charge a fee to transport trailers on their boat. In the Channel Island, Condor Ferries (“Condor”) are the only provider of ro-ro ferry services; and
- **Lo-lo boat service providers,** which operate boats in which freight is transported, some/most of which can be their own freight from their freight logistics service. In the Channel Islands, there are only two lo-lo boat operators and they also offer freight logistics services, namely Channel Seaways and Channel Island Lines. They are included within the reference to “lo-lo operators” in this report.

How did we carry out the market research?

To establish customers' views on the functioning of the freight market, Frontier Economics partnered with SYSTRA, a specialist in market research, to interview freight customers in the Channel Islands. In total, we held 20 in-depth interviews with customers, either over the phone or face-to-face. Our aim was to obtain perspectives from a wide-range of customers, who were drawn from multiple sources:

- customer information from freight transport providers that responded to our request for customer details;
- a sample of customers provided by CICRA; and
- Protel, an independent recruitment agency, were asked to recruit a sample of customers. Using an independent agency allowed us to remove any threat of sample bias from over-representing the views of one freight transport provider's customers.

In addition, to ensure we had a complete picture of the freight market, we also conducted interviews with a number of freight transport providers and the ro-ro ferry operator. Because these interviews were primarily for context, they are not directly relevant to the Terms of Reference (which focus on customers' views on choice in the market). These interviews provided useful context and we are very grateful to those we spoke to for being generous with their time.

A report prepared by SYSTRA which includes the content from these discussions has been shared with CICRA separately; it has not been included here as the focus of this report is customer choice, as per the Terms of Reference.

What were our findings?

Overall, we found that customers are generally satisfied with the freight market.

Quality of service is a key consideration for customers when considering switching. Large customers acknowledge that they have little choice of provider as only Ferryspeed are credibly able to offer the services they require. However, all of the customers are broadly satisfied with the level of service and price. Also, there are potentially other options (such as self-supply) available if customers were no longer content with the current providers.

Our key findings are summarised in Figure 3.

Figure 3 Summary of findings

Key questions	General conclusions
Drivers of choice	<ul style="list-style-type: none"> For most customers, quality of service (defined in a variety of ways including reliability, professionalism and quality of infrastructure) is a key consideration when choosing a freight transport provider, more so than price.
Adequacy of choice	<ul style="list-style-type: none"> There is a mixed view on the adequacy of choice. The larger the customer, the less choice they are likely to have. While some expressed a desire for more choice, others were content with the current level of service and did not express any preference for more options.
Ability and willingness to switch	<ul style="list-style-type: none"> Contractually, customers would be able to switch providers because the vast majority operate on an account basis. However, the willingness to switch was mixed. For some, the lack of willingness stemmed from a lack of choice, for others it came from satisfaction with the current provider and the service level offered.

Source: Frontier Economics

We provide further detail on our findings below.

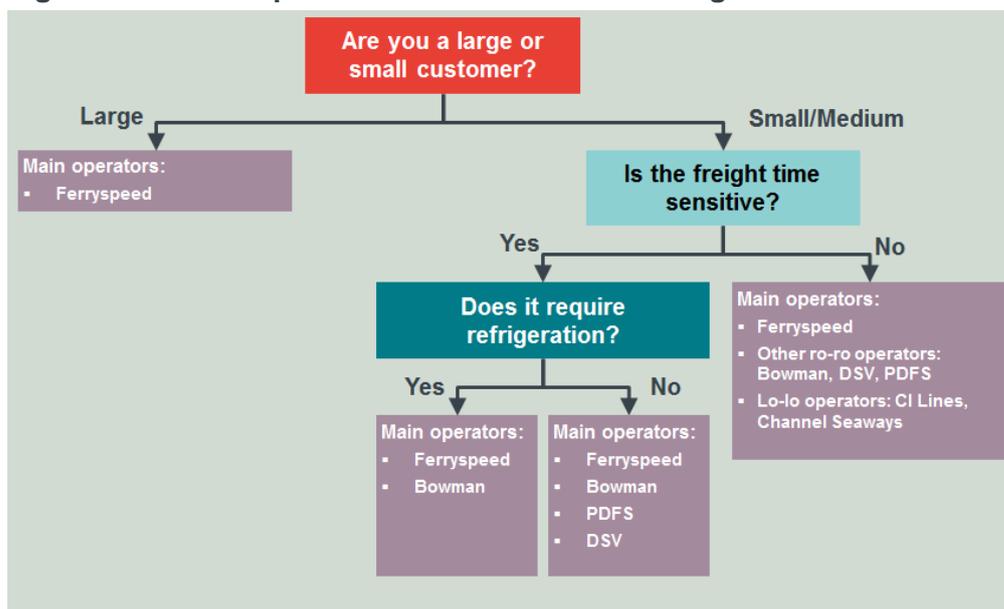
What drives customers' choice of freight transport provider?

The vast majority of customers indicated that qualities such as reliability, professionalism and quality of infrastructure were more of a driver of choice than price. This led customers, particularly large customers, to use Ferryspeed. However, it also led some small/medium customers to use smaller providers as they felt they received better service as they were “priority” for that provider.

Do customers feel they have adequate choice?

In general, the larger the customer, the smaller the choice-set of providers they appeared to have. Also, the need for refrigeration also tended to reduce the choice set. Figure 4 summarises the options available to customers dependent on their freight requirements.

Figure 4 Main operators in each market sub-segment



Source: Frontier Economics

Customers in different segments had different perspectives on the choices available to them:

- some small/medium customers, particularly those with non-time-sensitive, ambient freight, indicated that they had a range of providers to choose from;
- some small/medium customers, particularly those with time-sensitive refrigerated freight, indicated that, while they theoretically had a choice, they would be reluctant to switch as they felt that they would receive a worse price or level of service from another provider;
- the larger of the small/medium customers (those with time-sensitive refrigerated freight), indicated that they felt they had no credible alternative to their current provider; and
- large customers indicated that they had no choice other than Ferryspeed.

Amongst customers who indicated they had no credible alternative, there was a difference in opinion as to whether they wanted more choice. Some indicated that while they would welcome more choice, it might not be necessary as they feared it would lead to excessive focus on price which would come at the cost of a reduction in quality of service. It appeared that a small number would benefit from more choice; they suggested that Condor's rate card may be a barrier to growth and entry.²

Are customers willing and able to switch away from their current providers?

The interviews suggested that contractual barriers to switching were low. The majority of customers operated on an account basis and large customers who

² Condor's rates are inversely related to volume shipped. Thus, those shipping lower volumes face higher charges per metre than those shipping higher volumes

tendered contracts did so regularly. However, either as a result of their satisfaction with the levels of service or through lack of choice, the majority of customers had not recently switched provider.

The vast majority of customers indicated that self-supply was either impossible or extremely difficult. Larger customers were more likely to indicate that it was theoretically possible for them to switch to supplying themselves, however none indicated that this was something they would wish to do.

What do customers think can be improved in the market?

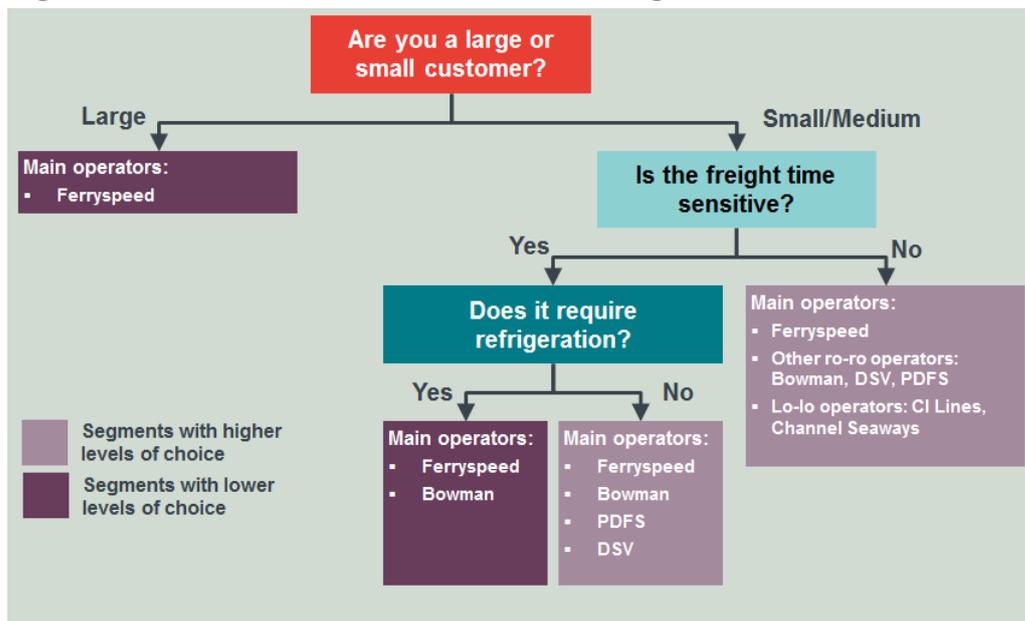
Outside of the points discussed in earlier sections around competition, although customers were broadly satisfied with the service from Condor, some suggested that both the management of ro-ro ferry services and the level of competition in the market for ro-ro ferry services could be improved.

Customers perceived that better management of the ro-ro ferry through improved communication of expected delays, cancellations, etc. would help them with inventory management. A variety of views were expressed regarding Condor, the ferry operator. Some perceived that an increase in competition would improve reliability of service and lower the costs of shipping for their provider, which they hoped would be passed on to them. However, others were less convinced, as they were concerned that an increase in competition could lead to there being two loss-making ferry operators, neither of which was sustainable.

How might the choice of freight providers change moving forward?

Focussing specifically on the adequacy of choice, we saw that while some segments are served by a range of providers, others have a limited choice of providers. This can be seen in Figure 5, where the segments for large customers and small/medium customers of refrigerated freight have been highlighted as having less choice relative to other sub-segments.

Figure 5 Choice-set in each market sub-segment



Source: Frontier Economics

However, as was outlined in Figure 3, customers are content with prices and service levels offered, even in these market segments. We did not find substantive evidence that inertia is a barrier to switching for customers; customers were aware of the offers available to them and indeed, those that were unhappy with quality of service did switch providers. Given this, there appear to be constraints on players in those markets which could stem from a combination of the threat of regulation, other providers and/or self-supply.

We do not have evidence to suggest that these constraints will be substantially weakened moving forward, which means that current outcomes are likely to be sustained in the future. However, there are actions that could be taken to lower barriers to entry and expansion in the market and thereby, increase competition and choice. This would require further and more detailed analysis.

1 INTRODUCTION

1.1 Background and context

As both Jersey and Guernsey are island economies, they are heavily dependent on the transport of goods by sea. Goods are generally carried by road within the Channel Islands and then transported by sea to and from either France or the UK. The market for freight logistics in the Channel Islands has seen a number of changes in recent years, ranging from exit to entry and consolidation.

CICRA has received concerns from market participants around how this sector is working. CICRA is therefore carrying out a market review of this sector, with the initial focus being on the choices available to customers when selecting a freight transport provider.

CICRA has engaged Frontier Economics and SYSTRA to assist in this review.

1.2 Objective of this report

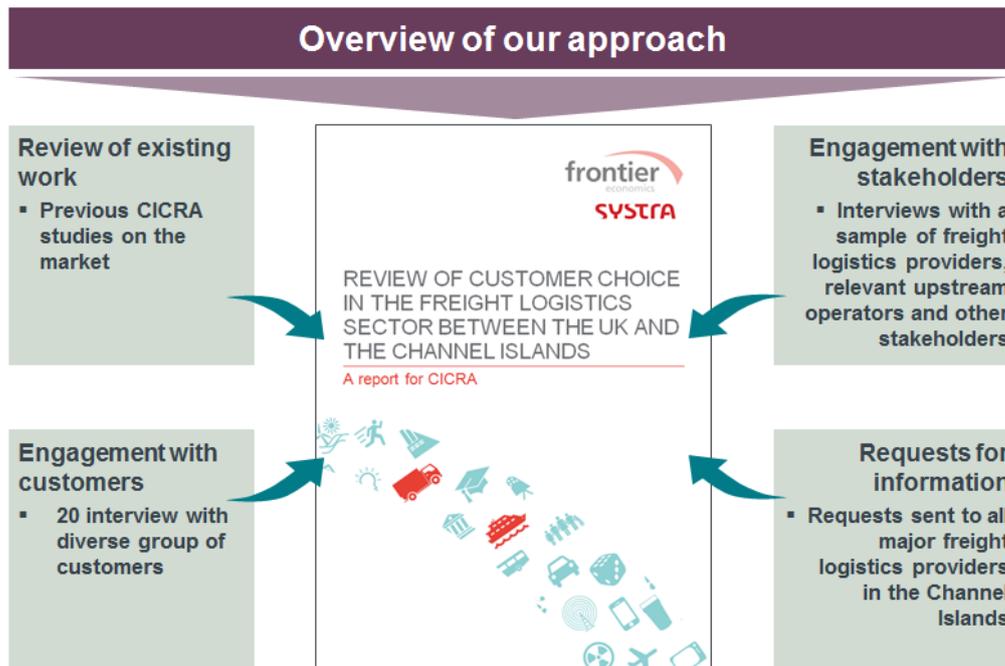
The objective of this report is to understand if freight customers are satisfied with current market outcomes on the following aspects, as outlined in CICRA's Terms of Reference:

- the factors customers take into account when selecting a freight transport provider (e.g. cost; resilience; reliability);
- customers' views on the adequacy of choice of freight transport providers when bringing goods into the Channel Islands; and
- the frequency of switching between freight transport services and any perceived barriers to such switching.

In addition, we consider the extent to which the current outcomes are likely to be sustained in the future.

We used a range of methods and information sources to determine customers' views and develop an in-depth understanding of the choices in the Channel Island freight logistics market. Figure 6 provides an overview of our approach.

Figure 6 Overview of our approach



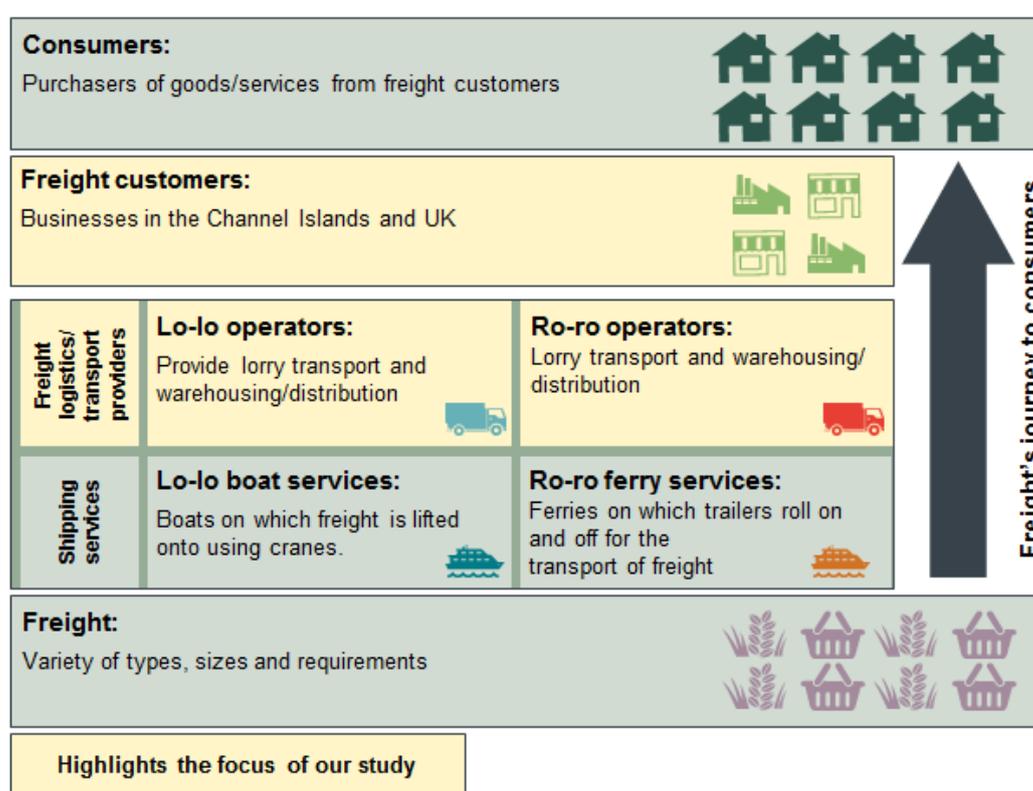
Source: Frontier Economics

2 HOW IS THE MARKET FOR FREIGHT STRUCTURED?

2.1 Who are the participants in this market?

Figure 7 provides a schematic overview of the supply chain for sea freight services³ between the UK and the Channel Islands.

Figure 7 Overview of supply chain for sea freight



Illustrative only

Our study focuses on freight customers and freight logistics/transport providers i.e. ro-ro and lo-lo operators. However, we discuss these stakeholders as well as the wider supply chain i.e. the shipping providers, in further detail below.

2.1.1 Freight customers

As a result of being on an island, the vast majority of businesses in the Channel Islands interact with the freight market in some form. Freight customer and freight

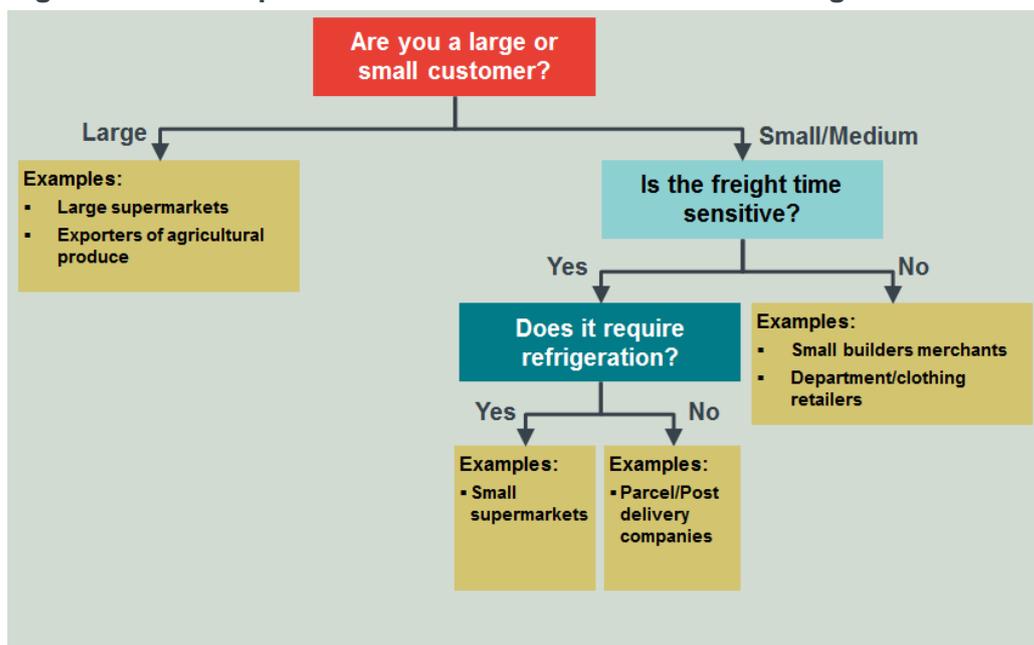
³ In general, freight can be transported either by sea or by air. Air freight is a specialist service, with limited capacity and cost exceeding four times that of sea freight. Therefore it is not considered within the scope of the review. Furthermore, within sea freight, there exist three methods of shipping, these are: ro-ro, lo-lo, and bulk freight. Bulk freight involves the transportation of unpackaged, mainly commodity, goods, independently of logistics/shipping companies. As a result, it falls outside of the scope of this review.

transport provider interviews indicated that the majority of goods sold on the islands are imported either via the UK or France. The majority of the islands production is exported to the same destinations, meaning that very few goods are both produced and consumed on the island. As a result, there exists a diverse range of different-sized freight customers (“customers”) with a variety of requirements.

- **Large customers** are typically either large retailers or large exporters (such as supermarkets and exporters of produce) that require refrigerated freight services. These customers generally operate on a contract basis which is either reviewed or tendered regularly. They require a daily service, either due to volumes or the need for just-in-time delivery.
- **Small or medium sized customers** include:
 - smaller supermarkets/wholesalers that will require refrigeration and possibly just-in-time delivery. They tend to operate on an account basis with many having accounts with multiple providers. As a result of this, they can change provider easily;
 - retail and other businesses that only require ambient (i.e. non-refrigerated) services. These customers either ship low volumes daily or more sizeable volumes a small number of times a week. They also tend to operate on an account basis with many having accounts with multiple providers; and
 - even smaller customers who ship only occasionally and in low volumes, making them less likely to require speedy delivery. A small proportion requires refrigerated or specialised freight services, but the majority will only ship ambient freight. These customers also tend to operate on an account basis but are generally less likely to have accounts with multiple providers.

Figure 10 summarises the market structure and provides relevant examples in each segment.

Figure 8 Examples of customers in each market sub-segment



Source: Frontier Economics

2.1.2 Freight logistics/transport providers

Types of freight logistics/transport providers

There are two types of freight logistics/transport providers (referred to as “freight logistics providers” and “freight transport providers” interchangeably in this report), both of which deliver to customers’ premises.

Roll-on, roll-off services (“ro-ro”)

Providers of ro-ro services (“ro-ro operators”) transport lorries containing trailered freight, which is ‘rolled’ on to/off a ferry at the departure/arrival destination and then transported to the customer’s premises. There are four major ro-ro operators:

- Ferryspeed, the largest operator;
- Paul Davis Freight, who was recently acquired by lo-lo operator, Channel Island Lines (“CI Lines”);
- DSV; and
- Bowman.

These operators offer a six day a week service to customers with ambient freight in both Jersey and Guernsey.

Ferryspeed and Bowman are the key providers of refrigerated services.

[8]

Ro-ro operators do not own their own ferries but instead use ferry services operated by Condor Ferries (“Condor”). Condor is currently the only ro-ro ferry operator based in the Channel Islands (discussed in more detail in the section on “Shipping services”).

Lift-on, lift-off services (“lo-lo”)

Providers of lo-lo services (“lo-lo operators”) transport predominantly containerised freight to and from the lo-lo boat using lorries. The containers are lifted on or off the lo-lo vessel using purpose-built cranes located at the quay.

There are two lo-lo operators in the Channel Islands, namely Channel Island Lines (“CI Lines”) and Channel Seaways. They ship container-freight to and from the islands on their own lo-lo boats before transporting it to customers via lorries. CI Lines sails three times a week and Channel Seaways sails twice a week.

Relative size and suitability of ro-ro and lo-lo

[X] presents a schematic description of the players, channels and their relative size within the market for freight in the Channel Islands.

[X]
[X]
[X]

Interviews with both freight logistics providers and customers suggested that lo-lo is more suited to non-time sensitive, ambient freight. They indicated that the infrequency of the service compared to ro-ro made it a less attractive option for customers who required daily delivery. And, while they acknowledged it was possible, it was difficult for lo-lo operators to provide a refrigerated offering comparable to ro-ro.

However, previous analysis by CICRA as well as evidence from the customer interviews suggested that certain forms of freight can be shipped using either method. The figure below presents market shares when the market is defined as all freight logistics services.

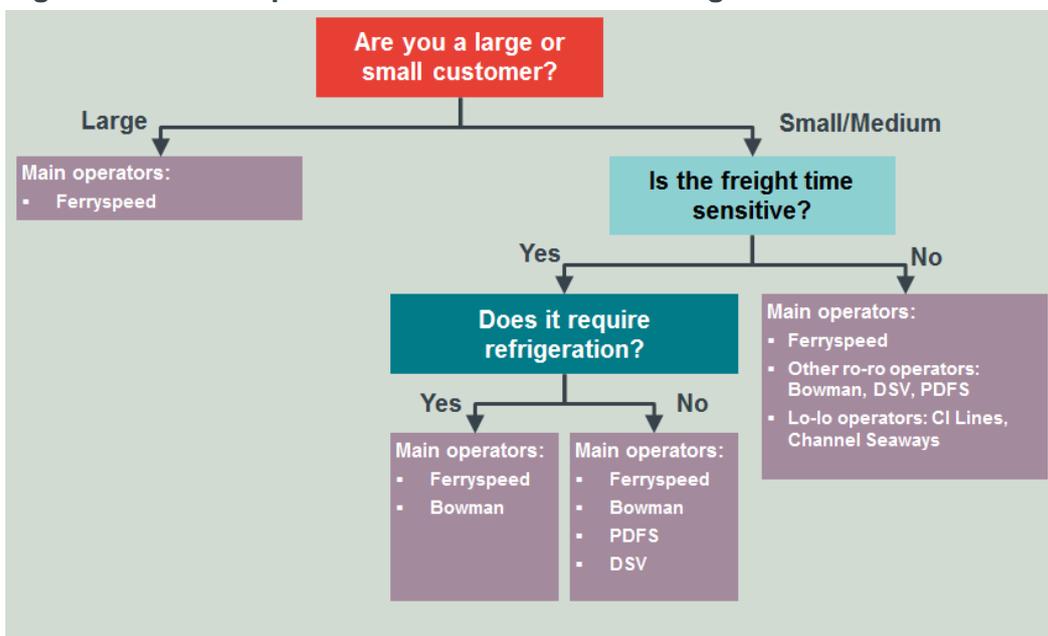
[X]

[X]

[X]

Figure 9 summarises the options available to customers based on their freight requirements.

Figure 9 Main operators in each market sub-segment



Source: Frontier Economics

2.1.3 Shipping services

Ro-ro ferry services

Condor is the sole provider of ro-ro shipping services and passenger movements between the UK and the Channel Islands. It has a fleet of four ships:

REVIEW OF CUSTOMER CHOICE IN THE FREIGHT LOGISTICS SECTOR BETWEEN THE UK AND THE CHANNEL ISLANDS

- two carry foot passengers and a small amount of light freight;
- one vessel carries foot passengers and freight; and
- one carries only freight.

Condor operates two services, six days a week on the route between Portsmouth, UK and the Channel Islands (“the Northern Route”) as a morning and evening service.

Its pricing is based on a rate card where ro-ro operators are charged per metre shipped based on volumes shipped over the last six months/year. [X]

[X]

[X]

[X]

Lo-lo boat services

This refers to the boat used by lo-lo operators to transport freight. Since the lo-lo operators in the Channel Islands use their own boats, lo-lo boat services are not considered separately. They are instead considered within the discussion of providers of freight logistic services hereafter.

2.2 What is the size of the relevant freight market?

How much freight is transported between the Channel Islands and the UK?

595,000 tonnes*

In 2015, 595,000 tonnes of sea freight were transported between the Channel Islands and the UK using either ro-ro or lo-lo. Around two-thirds (397,000 tonnes) were transported to/from Jersey while one-third (198,000 tonnes) was transported to/from Guernsey.⁴

of sea freight transported between the Channel Islands and the UK in 2015.

67% of this related to Jersey and 33% to Guernsey.

**Bulk freight excluded.*

What is the split between exports and imports?

85%

of freight is imported to the islands, 15% is exported*

**Based on total freight volumes with bulk freight included.*

Data on exports and imports are only available for all types of freight including bulk freight (the transportation of unpackaged, mainly commodity, goods, independently of logistics/shipping companies). Across the two islands, 85% of total freight was imported and 15% was exported.

Due to changing trends and external developments, the total amount of freight imported/exported into the islands has fluctuated over time. The most significant development was the ending of Low Value Consignment Relief (LVCR) between the UK and the Channel Islands in 2012. This was a VAT exemption designed to speed up the transit of low value (up to £18) goods through mail. The removal of this relief reduced total freight volumes in 2012, which can be seen in Figure 10 below.

What is the split between ro-ro and lo-lo?

Data on the split between ro-ro and lo-lo is only available for Jersey.⁵ In Jersey, 73% of freight volumes are transported using ro-ro, with 27% using lo-lo. Stakeholders have suggested that ro-ro is also the most popular method of transporting freight in Guernsey.

73%

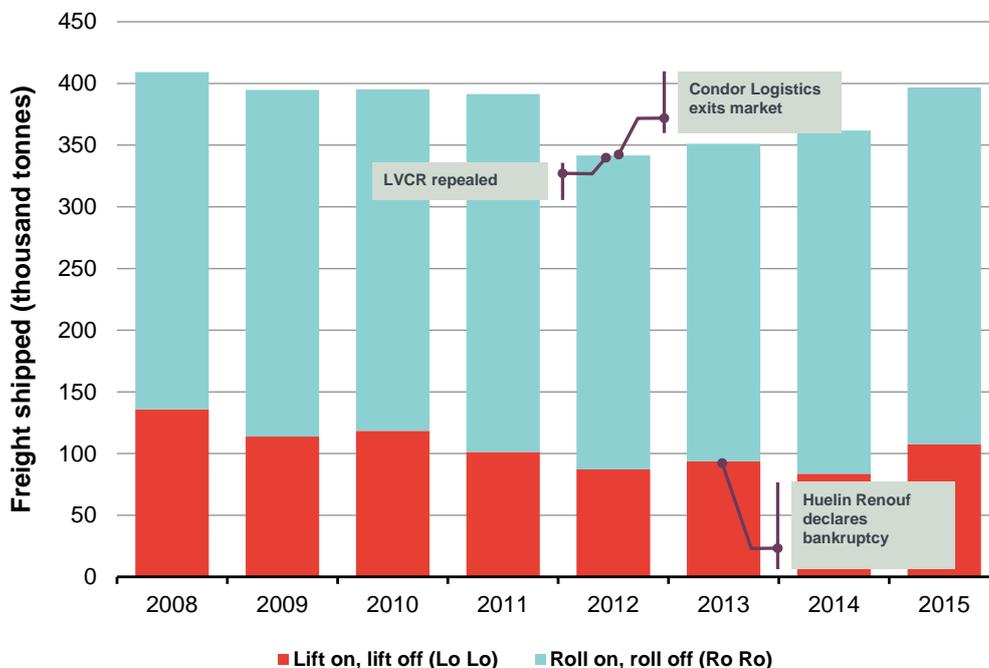
of freight is transported using ro-ro, 27% using lo-lo

⁴ Jersey/Guernsey in figures 2015

⁵ The Ports of Jersey publish the split of sea freight by ro-ro and lo-lo but Guernsey Ports only publish the total volume of sea freight shipped.

The relative proportions shipped using ro-ro and lo-lo has not fluctuated considerably over this time period, as seen in Figure 10. However, changes in the freight market, such as the exit of ro-ro operator Condor Logistics and lo-lo operator Huelin Renouf have had some impact on the volumes shipped on each type of service.

Figure 10 Volumes of ro-ro and lo-lo in Jersey, 2008-2015



Source: Jersey in Figures 2009 – 2015
Note: Figures split by type of freight is not available for Guernsey

2.3 How is the market regulated?

Figure 11 provides an overview of the regulation of players in the Channel Islands freight market.

Figure 11 Existing economic regulation in the freight supply chain



Source: Frontier Economics, Customer interviews, Operating agreement between the Harbour Master or

Jersey and Condor Limited, 2014.

This is discussed in further detail next.

2.3.1 How are the providers of freight logistics services regulated?

The market for freight logistics services is not currently regulated. As seen above, the market consists of multiple ro-ro and lo-lo operators and the competitive constraints in the market could stem from any or all of:

- constraint from other operators or entry from new operators- existing operators could be constrained in their activities by competitive pressure from each other. They may also be constrained by the threat of new entry;
- constraint from self-supply- the operators could be concerned that if they exercise any market power, their customers could switch away from them, acquire their own trucks and trailers, and begin transporting their own freight; and
- constraint from the threat of regulation- larger players could be concerned about regulatory intervention if they exercise any market power through price increases or reductions in service quality

2.3.2 How is the provider of ro-ro ferry services regulated?

Condor is regulated via its ramp license which was signed with the States of Jersey in 2014. A Memorandum of Understanding exists with the States of Guernsey in keeping with the agreement with the States of Jersey.

The licence/MoU requires that any operator, Condor included, that wishes to service the market:⁶

- shall provide the “designated services”, which include both passenger and freight services on both the Northern and Southern routes in all seasons;⁷
- shall undertake periodic service reviews;
- shall measure profitability and efficiency by reference to Return On Average Capital Employed (ROACE); and
- shall ensure that ROACE remains within a lower and upper tramline. In the event that ROACE falls below or above the tramlines the operator should meet with a Ferry Service Steering Group within two weeks with written recommendations on how to remedy the situations including reducing/increasing prices or increasing/reducing scheduling.

2.4 What are the recent developments in the market?

Over the past 12 years the freight market in the Channel Islands has been characterised by consolidation, exit and entry. There have been two major

⁶ Operating agreement between the Harbour Master or Jersey and Condor Limited, 2014. Available at: <http://www.ports.je/SiteCollectionDocuments/ID%20Agreement%20Condor%20Operating%20Agreement%2020140715%20KW.pdf>

⁷ The “Southern Route” is the route between the Channel Islands and France.

mergers over this period and considerable amount of entry/exit, with exit slightly outweighing entry. The following section chronologically describes the major development in the freight market over the past 12 years with Figure 12 highlighting the major developments in this period.

Figure 12 Timeline of major developments in the Channel Islands freight market, 2005-2017



Source: JCRA, Condor Group, BBC, CICRA

Ferryspeed acquiring Channel Express

A significant market structure change occurred in 2005 when Ferryspeed, the largest operator in the ro-ro market, acquired Channel Express, another operator in the market.⁸ This increased Ferryspeed's market share by 10-20% with the new entity estimated to have 70-80% market share in the "sea-borne temperature controlled freight" market.

As a condition for this merger, Ferryspeed offered not to acquire the Channel Express warehouse, instead surrendering it to the Port of Jersey. They also voluntarily stopped acting as a sub-contractual distributor for DSV (then known as DFDS), who then took over the warehouse.

[✂]

Events between 2012 and 2014

A second series of events which had a significant impact on the market occurred between 2012 and 2014.

In 2012, Condor Logistics ceased trading. Frontier understands that this was, in part, due to the ending of the VAT exemption for low-value goods imported to the

⁸ <http://cicra.gg/files/060711%20FINAL%20PUBLIC%20VERSION%20DECISION%20FERRYSPEED.pdf>

UK from the Channel Islands (the LVCR).⁹ This policy change also significantly reduced total freight volume. Their exit left Ferryspeed, PDFS, DSV and Bowman as the only four major ro-ro operators.

A year later, in August 2013, Huelin Renouf Shipping, a lo-lo operator, went into liquidation.¹⁰ After a period in which a number of bids for their assets were submitted they were purchased by a consortium of investors and Channel Island Lines was created.

[<]

Finally, in 2014 Condor signed a 7 year (later extended to 10) ramp license with the States of Jersey (discussed in Section 2.3.2). This set out the terms that all ro-ro ferry providers wishing to operate in the Channel Islands must commit to; specifically, it requires each operator to commit to providing a six day a week, year round, freight and foot transport on both the Northern and Southern route.¹¹

Events since 2014

In recent years, there have been two examples of small-scale market entry as well as some consolidation.

[<]

Also in 2016, Jersey Post acquired the UK Company Fraser Freight. Interviews with freight logistics operators and customers indicate that this has not had a significant impact on the market as the majority of Fraser Freight's business takes place in continental Europe.¹²

Most recently, Paul Davis Freight Services, a ro-ro operator, and Channel Island Lines, a lo-lo operator, announced their intention to merge. This transaction was approved by CICRA in March 2017, creating an integrated ro-ro/lo-lo operator.¹³

⁹ Condor Group, "Following loss of LVCR, Condor Group to close logistics business", 4 Oct 2012, link: http://www.condorferries.co.uk/Documents/12_10_04%20GannouncementLVCRImpact_Jerseyfinal.pdf

¹⁰ BBC, "Shipping company Huelin-Renouf stops trading", 20 Aug 2013, link: <http://www.bbc.co.uk/news/world-europe-jersey-23766025>

¹¹ BBC, "Condor Ferries gets 10-year licence application approval", 14 Jul 2014, link: <http://www.bbc.co.uk/news/world-europe-jersey-28300584>

¹² Jersey Post, "Jersey Post to acquire Fraser Freight", 14 Jul 2016, link: <http://www.jerseypost.com/fraserfreight/>

¹³ CICRA, "Case M1280J – Proposed Acquisition of Paul Davis Freight Services Limited by Rockayne (Jersey) Limited t/a Channel Island Lines", 29 Mar 2017, link: [http://www.cicra.gg/_files/170403%20PDFS,%20Rockayne%20\(CIL\)%20-%20Redacted%20Decision.pdf](http://www.cicra.gg/_files/170403%20PDFS,%20Rockayne%20(CIL)%20-%20Redacted%20Decision.pdf)

3 WHAT ARE CUSTOMERS' VIEWS ON CHOICE?

In this section, we summarise consumers' views on the three key questions as set out in CICRA's Terms of Reference:

- the factors customers take into account when selecting a freight transport provider;
- the adequacy of choice of freight transport providers when bringing goods into the Channel Islands; and
- the willingness and ability to switch between freight transport services.

We also asked customers about the improvements they would like to see in the market. These aspects are discussed in more detail below.

3.1 What drives customers' choice of freight transport provider?

Overall, the majority of customers said they felt that they received a good service from their freight transport provider ("provider"). The majority of customers, regardless of size, indicated that quality of service was a more important factor than price when choosing a provider. Quality of service is defined across a wide range of metrics which are presented in Figure 13.

Figure 13 Considerations of customers when choosing a provider



Source: Customer interviews

The requirements of their freight influenced customers' choice of provider. For instance,

- those with ambient and non-time sensitive customers were able to choose from all ro-ro and lo-lo operators;
- those that needed a daily/quick service could only use ro-ro operators; and
- those that had special requirements (e.g. fragile, hazardous, legal requirements) were limited to fewer providers.

The majority of customers used a sole provider. The main reasons given for this were:

- it is easier to deal with just one primary provider;
- they receive volume discounts for increased quantities transported; and/or
- they have only one credible option.

However, a small number of customers used multiple providers, usually to handle different types of goods and services. In some cases this was due to their preferred provider being unable to handle certain types of freight.

What drives large customers' choice of freight transport provider?

Given the importance of service, large customers almost exclusively chose Ferryspeed. All large customers indicated that Ferryspeed had invested significantly in infrastructure, and a number indicated that they had seen noticeable improvements in Ferryspeed's service over a five year period. Moreover, none perceived excessive price increases in this time.

In addition to a reliable and professional service, examples of the service offered by Ferryspeed for larger customers include:

[&<]

What drives small/medium customers' choice of freight transport provider?

Small/medium customers were served by a variety of providers. These included Ferryspeed, as well as other such as Bowman Haulage, DSV and CI Lines.

While two small/medium customers suggested that they were predominantly price-driven, the majority of these customers indicated that their choice was more dependent on quality than price. This was because a poor quality service from a provider would be reflected in their own business' performance, which might then result in lost contracts with their end-consumers.

The most common reason for using providers other than Ferryspeed was that customers wished to feel like a priority for their provider. Therefore, while they did not transport significant enough volumes to feel like a priority for Ferryspeed, their volumes were large enough for them to be considered a big customer by a smaller operator. They felt this impacted on the service they received.



“[With our previous provider] I felt like we were at the back of the queue.”

Small customer

Nevertheless, the small/medium customers who did use Ferryspeed indicated they were happy with the service they received.

[X]

3.2 Do customers feel they have adequate choice?

There is a significant difference in the level of choice customers face depending on their size. Small/medium customers indicated that they had a good amount of choice in the market while large customers had one credible option, Ferryspeed.

Do large customers feel they have adequate choice?

Large customers, in particular those that required refrigeration, indicated that they had no choice other than Ferryspeed. This was due to no other provider being able to handle the volumes that they needed to ship, and no other provider having made the investment in infrastructure that they require.



“I don’t see the need for anyone else really. I think we get a very fair, competitive service from Ferryspeed.”

Large customer

However, while being open to the idea of increased competition in this market, these customers were confident that they were receiving a satisfactory deal from their provider in terms of price, and were happy with the quality of service they were receiving. Some suggested that while a second provider could improve competition, they would be concerned that too much price competition may lead to under-investment or reductions in service quality (to offset any price reductions).

Do small/medium customers feel they have adequate choice?

There were a range of views expressed by businesses in the small/medium customer segment.

Some felt that they had a good choice of providers. This was particularly the case if the freight was not time-sensitive as this increased the pool of potential

providers to include lo-lo operators. Many felt that they would be able to find an acceptable alternative provider if necessary, even if they were not able to offer the same level of service as their current provider.

Another group felt that they had a choice, however that they would be reluctant to exercise that choice. This was due to their belief that, while switching was theoretically possible, they would not receive the same price or level of service from a rival provider. This view was prevalent amongst larger small/medium customers, particularly those who required refrigerated services.

Finally, there was a group of small/medium customers who felt that it was difficult to switch because they did not have confidence in other operators to provide the service they required. Some customers in this segment indicated that they did not see this as a problem. It appeared that some felt they would benefit from more choice, pointing to the rate card as a barrier to rival providers gaining scale.

These comments were consistent with the views expressed by larger customers and suggested that as companies get bigger, their choice in the market is restricted to fewer players.

3.3 Are customers willing and able to switch away from their current providers?

3.3.1 Would customers be able to switch away from current providers?

Evidence from customer interviews suggests that it is contractually possible for all types of customer to switch between suppliers.

Would large customers be able to switch?

Larger companies tended to operate on a contract basis. These are typically multi-year contracts, subject to periodic break clauses and often service level agreements (covering aspects such as delivery schedules, volume of damages and claims against lost stock etc.).

However, large customers indicated that when they did tender contracts they were not satisfied with the response as often only a small number of companies place bids.

[&<]



“I don’t know of any [other] provider out there that has this facility [warehousing], that could hold volume like that for us and pick it”

Large customer

Would small/medium customers be able to switch?

The majority of small/medium customers appeared to operate on an account basis, and many had accounts with multiple, or all, providers. These accounts

were usually negotiated annually for the year ahead. Customers generally suggested that they would be able to switch easily.

3.3.2 Would customers be willing to switch?

Customers, both large and small/medium, tended not to switch because they are content with current providers. The vast majority of customers indicated they had not seen excessive price rises and that they were satisfied with the quality of service they received. Similarly, many indicated they had experienced improvements in quality of service over five years.

While a number indicated that they were sensitive to price, a similar number indicated that they would not switch when faced with a large price increase because they valued quality of service.

A number of customers indicated they had:

- tendered contracts;
- considered switching; or
- switched provider in the past 5 years.

However, of these three types of customer, those who had actually switched were the minority. Furthermore, amongst the customers who did not switch, none indicated that they were dissatisfied.



“If I had to pay £5, £10 a pallet more for the service I’m having, I’d do it. It’s not all about cost.”

Small customer

3.3.3 Could customers switch to self-supply?



“Too expensive, too complex.”

Large customer

Nearly all customers indicated that they were unlikely to consider self-supply. No large customer indicated that they had given serious thought to self-supply. However, when pressed, some indicated that it would theoretically be possible, but challenging.

[X]

Small and medium sized customers generally indicated that self-supply would be very difficult or impossible for them. The most common reasons for this were:

- lack of scale;
- lack of knowledge and expertise in running a freight logistics operation;
- seasonal operation and fluctuating volumes which would leave capital equipment unutilised and losing money for parts of the year; and
- restrictions on employment, which mean potentially diverting staff from core operations.

Some customers stated that, while they would like to self-supply, the price they would face from Condor as a small operator would make such a venture unviable.



“We would never get the rates on the ferry that some of the haulage companies get... we’d be [self-supplying] but to no gain. If I could get the same rates then I’d seriously consider it.”

Small customer

REQUIREMENTS FOR SELF-SUPPLY

Based on our interviews, it appears that self-supply is most viable if the business has the following characteristics:

- It already owns infrastructure needed, or are able to secure capital to invest;
- It transports significant volumes (more than 5,000 metres a year), or able to sustain losses while volumes build up;
- It is able to utilise both legs of the route;
- It has a credible plan to manage logistics and warehousing; and
- It transports constant volumes, all year-round.

Any individual customer’s business may only meet some of the characteristics above and the viability of self-supply will depend on the specific characteristics of the business

3.4 What do customers think can be improved in the market?

Having gathered views on the questions on choice and acknowledging that interviewees appeared to be largely content with choice, we also asked customers about improvements they would like to see in the market. The suggestions from customers were:

- improved management of the ferry service; and
- increased competition in ferry service.

Management of ferry services



“There should be a second ferry company serving the islands, someone else to give Condor competition that might make Condor service the Islands better than they do... [Condor] should have a spare boat, and more of a backup plan”

Customer

Customers were broadly satisfied with the service from Condor. However, some indicated they would like to see:

- More information from Condor to support business management – for instance details on the arrival times of ferries, warnings of projected bad tides, alerts to future risks and upcoming maintenance etc.;
- earlier arrival of the ferry in the Islands;
- improved reliability of ferries; and
- transparency on the fuel surcharge/reduction in costs of operation to enable lower prices for products for end users.

Competition in ro-ro ferry services

Customers had contrasting views on the viability and value of introducing competition for Condor in the ferry market.

Some customers, including large customers, welcomed it because they considered that it would:

- motivate Condor to improve the quality of its service;
- create a downward pressure on costs for providers, which could then be passed on to customers and ultimately end consumers; and
- provide customers with a second option and therefore increased flexibility and resilience should services be disrupted for any reason.

However, others were less convinced, and raised concerns about how much competition for ferry services the Islands could support. Caution was urged to ensure that the viability of a vital service was not threatened, and an attempt to increase competition did not lead to there being two loss-making ferry operators, neither of which was sustainable.



“That would be difficult. To have two ferry services, I don’t think there’s enough business in the islands to support it.”

Customer

Other suggestions

Customers also proposed that the States of Jersey make more land available for warehousing, and to make it easier for freight operators to expand and consolidate warehousing.

COMPARISON WITH OTHER FREIGHT MARKETS

Most customers had little or no experience in other freight markets from which to draw comparisons with the Channel Islands.

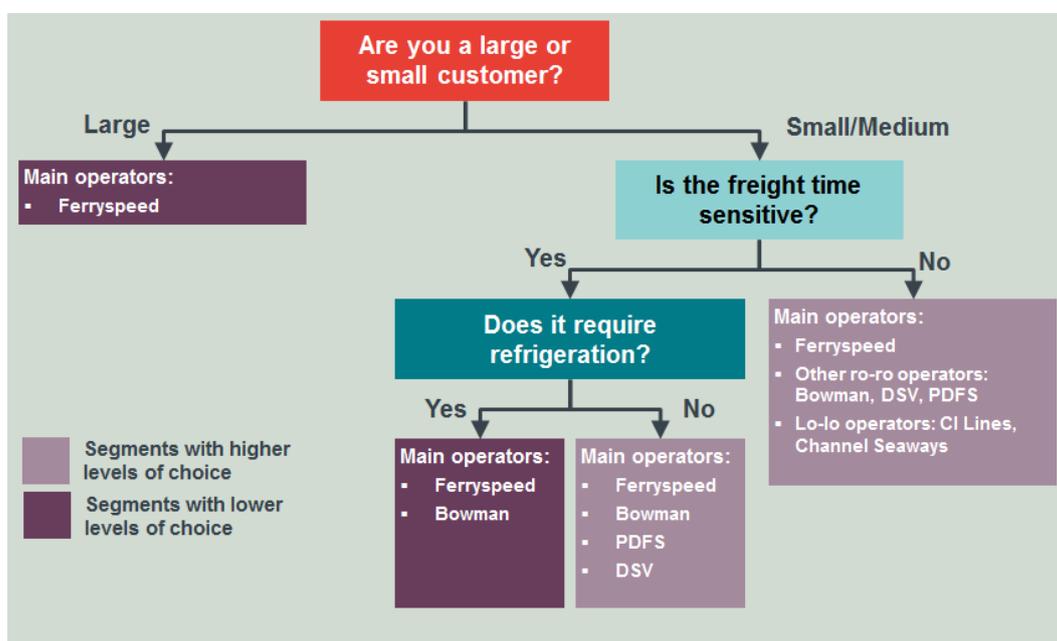
However, those that did often referred to experience in the Isle of Man freight market and agreed that it shared many commonalities with the market in the Channel Islands. These were:

- similar limited nature of freight transport providers, including existence of one large player;
- comparable cost of freight transport services; and
- comparable natural limitations resulting from a small population, including its ability to support competition in both freight transport provider and freight shipping services markets.

3.5 What is our conclusion on choice in the market?

Figure 14 below outlines the choice available to various customer segments.

Figure 14 Choice-set in each market sub-segment



Source: Frontier Economics

As can be seen, there are segments of the market where there is less choice than others. These are the segments for large customers and small/medium customers of refrigerated services. However, across segments, customers appear to be largely content with the level of service received. Furthermore, customers did not perceive that their prices had increased significantly over time.

On the whole, the general conclusions from the interviews to the questions set out in Terms of Reference are summarised in Figure 15.

Figure 15 Summary of findings

Key questions	General conclusions
Drivers of choice	<ul style="list-style-type: none"> ▪ For most customers, quality of service (defined in a variety of ways including reliability, professionalism and quality of infrastructure) is a key consideration when choosing a haulier, more so than price
Adequacy of choice	<ul style="list-style-type: none"> ▪ There is a mixed view on the adequacy of choice. ▪ The larger the customer, the less choice they are likely to have. ▪ While some expressed a desire for more choice, others were content with the current level of service and did not express any preference for more options
Ability and willingness to switch	<ul style="list-style-type: none"> ▪ Contractually, customers would be able to switch hauliers because the vast majority operate on an account basis. ▪ However, the willingness to switch was mixed. For some, the lack of willingness stemmed from a lack of choice, for others it came from satisfaction with the current provider and the service level offered.

Source: *Frontier Economics*

4 HOW MIGHT THE CHOICE OF FREIGHT PROVIDERS CHANGE GOING FORWARD?

In this section, we focus on the market segments where there appear to be less choice, namely the market for large customers and the market for small/medium customers of refrigerated goods, relative to the other segments. Acknowledging that consumers appear not to be discontent with prices, for each segment we explore:

- the factors that may be driving these outcomes today; and
- whether these factors are likely to remain in place in the future.

POSSIBLE DRIVERS OF OUTCOMES

As has been discussed in Section 2.3.1, the market for freight logistics services is not currently regulated. However, the pricing behaviour of freight logistics providers could be driven by any or all of:

- threat of regulatory intervention from CICRA;
- constraint from customers switching to self-supply; and
- constraint from other providers or threat of entry from new providers.

We discuss the extent to which they are likely to apply in the two customer segments now and in the future.

4.1 Market for large customers

4.1.1 What is driving today's outcome?

[X]

[X]

[✂]

4.1.2 Could these drivers continue to exist in the future?

[✂]

4.2 Market for small/medium customers of refrigerated freight

[✂]

4.2.1 What are the drivers of today's outcomes?

[✂]

4.2.2 Could these drivers continue to exist in the future?

[✂]

[✂]

[✂]

[✂]

4.3 What could facilitate a widening of the choice-set?

In general, a widening of the choice set to include more providers and improved ability to self-supply would increase competition in the market for freight logistics services. One way to increase choice is to lower barriers to entry and expansion in a market.

[✂]

5 CONCLUSION

The objective of this report has been to understand if freight customers are satisfied with current market outcomes on the following aspects, as outlined in CICRA’s Terms of Reference:

- the factors customers take into account when selecting a freight transport provider (e.g. cost; resilience; reliability);
- customers’ views on the adequacy of choice of freight transport providers when bringing goods into the Channel Islands; and
- the frequency of switching between freight transport services and any perceived barriers to such switching.

On the whole, the general conclusions from the interviews to these questions are summarised in Figure 16.

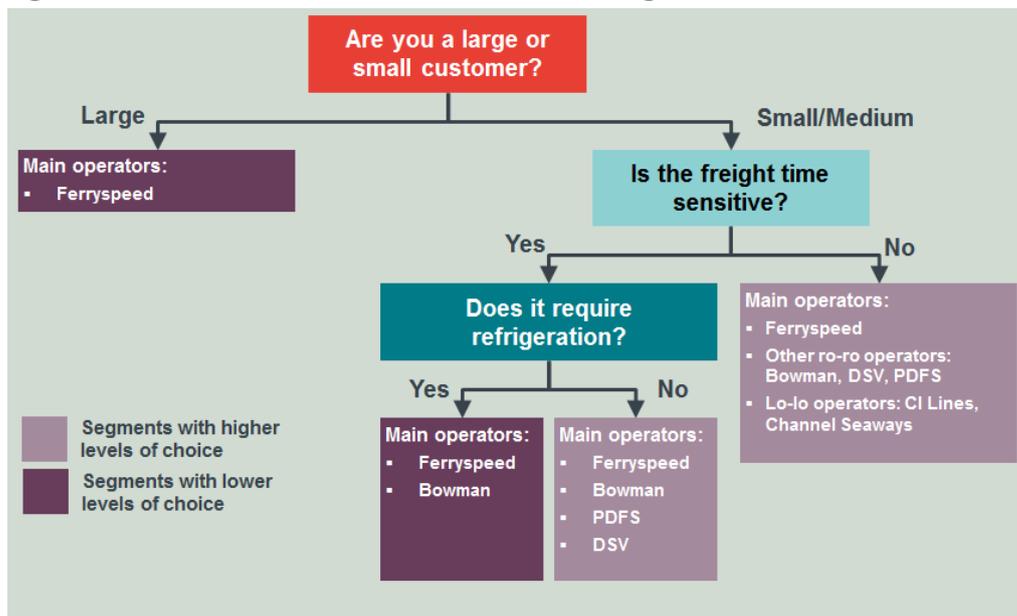
Figure 16 Summary of findings

Key questions	General conclusions
Drivers of choice	<ul style="list-style-type: none"> ▪ For most customers, quality of service (defined in a variety of ways including reliability, professionalism and quality of infrastructure) is a key consideration when choosing a freight transport provider, more so than price.
Adequacy of choice	<ul style="list-style-type: none"> ▪ There is a mixed view on the adequacy of choice. ▪ The larger the customer, the less choice they are likely to have. ▪ While some expressed a desire for more choice, others were content with the current level of service and did not express any preference for more options.
Ability and willingness to switch	<ul style="list-style-type: none"> ▪ Contractually, customers would be able to switch providers because the vast majority operate on an account basis. ▪ However, the willingness to switch was mixed. For some, the lack of willingness stemmed from a lack of choice, for others it came from satisfaction with the current provider and the service level offered.

Source: *Frontier Economics*

Focussing specifically on the adequacy of choice, we saw that while some segments are served by a range of providers, others have a limited choice of providers. This can be seen in Figure 17, where the segments for large customers and small/medium customers of refrigerated freight have been highlighted as having less choice relative to other sub-segments.

Figure 17 Choice-set in each market sub-segment



Source: Frontier Economics

However, as was outlined in Figure 16, customers are content with prices and service levels offered, even in these market segments. Thus, there appear to be constraints on players in those markets which could stem from a combination of the threat of regulation, other providers and/or self-supply.

We do not have evidence to suggest that these constraints will be substantially weakened moving forward, which means that current outcomes are likely to be sustained in the future. However, there are actions that could be taken to lower barriers to entry and expansion in the market and thereby, increase competition and choice. This would require further and more detailed analysis.

ANNEX A HOW WE CONDUCTED THE MARKET RESEARCH

A.1 Interviews with consumers of freight logistics services

To establish customers' views on the functioning of the freight logistics market, Frontier Economics partnered with SYSTRA, a specialist in market research, to interview freight market customers in the Channel Islands. In total we held 20 in-depth interviews with customers, either over the phone or face-to-face. Our aim was to obtain the perspective of the market from a wide-range of market participants, who were drawn from multiple sources:

- customer information from providers that responded to our request for customer details;
- a sample of customers provided by CICRA; and
- Protel, an independent recruitment agency, were asked to recruit a sample of customers. Using an independent agency allowed us to remove any threat of sample bias from over representing the views of one provider's customers.

We sought to obtain the views of a wide range of customer types to see how the market is working for organisations with different circumstances - e.g. importing/exporting, large/small volume of transported goods, ambient or refrigeration requirements, and need or not for fast delivery. Further to this, customers needing hazardous, specialised and fragile services were all considered within the sample. Thus, we sought to obtain deep insights of different customers through detailed, in-depth one-to-one discussions rather than obtain quick responses to a list of structured questions that would typically form a quantitative survey.

A.2 Interviews with other market participants

Before meeting with customers, we met/spoke with a sample of other market participants including current freight transport providers and Condor to understand the market structure from their perspective as context for the customer interviews.

The contact details for relevant stakeholders were submitted by CICRA and included ro-ro, lo-lo and other relevant stakeholders.

Because these interviews were primarily for context, they are not directly relevant to the Terms of Reference (which focus on customers' views on choice in the market). These interviews provided useful context and we are very grateful to those we spoke to for being generous with their time. A report prepared by SYSTRA which includes the content from these discussions¹⁴ has been shared

¹⁴ Please note that all information shared with us on these calls/meetings has been anonymised as per Market Research Society Guidelines, as had been discussed at the start of the interviews.

REVIEW OF CUSTOMER CHOICE IN THE FREIGHT LOGISTICS SECTOR
BETWEEN THE UK AND THE CHANNEL ISLANDS

with CICRA separately; it has not been included here as the focus of this report is customer choice, as per the Terms of Reference.

