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Flagging out in road freight transport: a strategy to reduce corporate costs in a competitive environment
Results from a longitudinal study in Austria

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ABSTRACT

Following the example of maritime transport, the relocation of fleets abroad – referred to as flagging out – has become an important cost reduction strategy for road freight transport companies. Particularly after the EU Eastern Enlargement in 2004, many Austrian road freight transport companies took advantage of both the freedom of services and the lower costs in New Member States. This paper shows the results of four waves of surveys of Austrian road hauliers, describing developments, attitudes, motives and impacts of the phenomenon. There is also a discussion about the significance of the problem, which was seldom referred to in the scientific literature.

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1. Introduction

In highly competitive markets with many small and medium firms, an individual company has little influence on market prices but always needs to strive for efficiency. This holds particularly true for the domain of road freight transport in Central Europe, where any strategies leading to cost reductions are likely to be implemented (Hilal, 2008). Flagging out – i.e. the re-location of fleets – is one possible way of doing this. This paper discusses this phenomenon and presents results from a longitudinal study based upon four individual waves of empirical surveys in Austria. It begins by discussing the strategy of flagging out in general, drawing on the existing body of research. Next, the methods used to conduct the survey and the data collected are outlined and the results presented. Finally, the findings are discussed and conclusions are drawn.

2. Background

As transport services are ‘produced’ by geographical relations and not at a facility or production site, Krink (1971) famously argues that a transport company has no location in the strict sense of the term. The administrative building serves as head office only, and is of course not equivalent to a production site. Taking advantage of this fact, ship-owners have often registered their fleet in other countries with more liberal regimes with less strictly defined rules in order to overcome trade restrictions (Thuong, 1987; Toh and Susilowidjojo, 1987); to avoid legal restrictions (Llàcer, 2003; Metaxas, 1981); and to profit from lower standards and therefore lower costs ‘flag of convenience’ – ‘foc’; (Alderton and Winchester, 2002; Rodrigue et al., 1997; Rowlinson and Leek, 1997). Later, the air transport industry also followed the maritime example. In both industries, which are traditionally oriented towards international transport, the means of transport (ship, vessel, aircraft) is directly linked to the medium of transport (water, air) and no further basic infrastructure (streets, rail tracks) is needed. Access is technically easy and flexible and not restricted to set routes, while business is global. It is thus easier to register a fleet abroad in these domains than in the domains of road and rail transport (Sampson and Bloor, 2007).

Indeed, compared to air and maritime transport, road freight transport – though it does have an important international component – has to be regarded as a rather local business (Hesse and Rodrigue, 2004), and most journeys are short-haul services (Allen et al., 2012; Fürst, 2010). Nevertheless, although flagging out was introduced significantly later than in other transport sectors, operating non-national vehicles on an international as well as national scale is not new to the European road freight industry (as the example of Luxembourg shows (Freudmann, 1999)). During the last decades, and particularly after the fall of the iron curtain in

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Central Eastern Europe/CEE (AT, BG, CR, CZ, HU, PL, RO, SI, SK), the road freight transport market has undergone substantial changes. For example, new organisational and management structures have arisen; new linkages and routes have been developed; new equipment and technology have been transferred to the region; and a quantitative and qualitative upgrading of infrastructure and services has taken place (Hall, 1993; Kummer, 2010; Kummer et al., 2009a,b). First, the rise in liberalisation and deregulation in the Common Market offers more or less free access to the entire EU area for all companies operating under a Community License (Hilal, 2008). Second, most countries in the CEE region, which were formerly separated by the iron curtain, have now become full members of the EU. Only some minor transitional regulations delaying full access to all national markets has hindered the market access of companies from the new Member States. Previous research shows that the importance of flagging out grows with the opportunities to do so which are available at the respective point in time. This can be clearly seen in the case of the EU, where the introduction of favourable conditions due to the EU enlargement to CEE countries resulted in an increase in flagging out to these countries. If an area with harmonized legal conditions (and a lack of legal and administrative barriers) is enlarged to include countries or regions with divergences in the relevant economic conditions, e.g. labour costs in road freight transport, the use of these opportunities tends to increase. For example, Fig. 1 shows that labour costs in the new CEE Member States are significantly lower than in Austria, leading to a massive increase in flagging out to these countries.

Furthermore, several examples of similar instances in the European context can be found. In Denmark, there has been a significant increase in vehicles which were registered abroad. As well as labour costs, the administrative burden in Denmark played an important role (Anon., 2011). High labour costs in Finland also made Finnish companies flag out their fleets to Russia (Anon., 2003). In the past, the Benelux countries – Belgium, Netherlands and Luxembourg – used to be a popular intra-EU destination for flagging out, particularly for neighbouring countries (Freudmann, 1999). Luxembourg offered substantial advantages like lower corporate taxes, government investment subsidies, low payroll taxes and low social expenses for employees registered there. However, nowadays, these countries are rapidly losing ground to new Member States such as Slovakia, Hungary and Romania. As conditions evolve over time, the practices and destinations of flagging out also change with them. (Dieplinger et al., 2010; Freudmann, 1999; Anon., 2002, 2003, 2011)

As a result, the market has essentially become fully liberalised and deregulated. A Common Market for road freight transport has finally been established (Hilal, 2008) and almost all Central and Eastern European companies have been able to enter the market, leading to a significant increase in competition on the services and labour markets. Furthermore, it is also easy for companies from the former EU-15 to open a subsidiary in the new Member States.

Due to the growing cost pressures over the past years (Hilal, 2008), the flagging out of Heavy Goods Vehicles (HGVs) has become a popular strategy in the transport industry, and particularly in Austria. At this point, it is important to distinguish between the two different kinds of flagging out (Kummer et al., 2009a, 2003, 2006). First, 'direct flagging out' means that a national haulier relocates a Heavy Goods Vehicle that had already been registered in the home/original country to a new location abroad, while 'indirect flagging out' refers to new investments into HGVs which are registered abroad from the beginning. Both forms of flagging out increased considerably after the EU enlargement of 2004 (Bergrath, 2000; Butzke, 1999; CNT, 2003; Cordes et al., 2006; International Road Transport Union (IRU), 2001; Kummer et al., 2006).

As a country at the 'heart of Europe', Austria is particularly exposed to Central and Eastern European competitors, since it has borders to Slovakia, Hungary and Slovenia, and distances to other

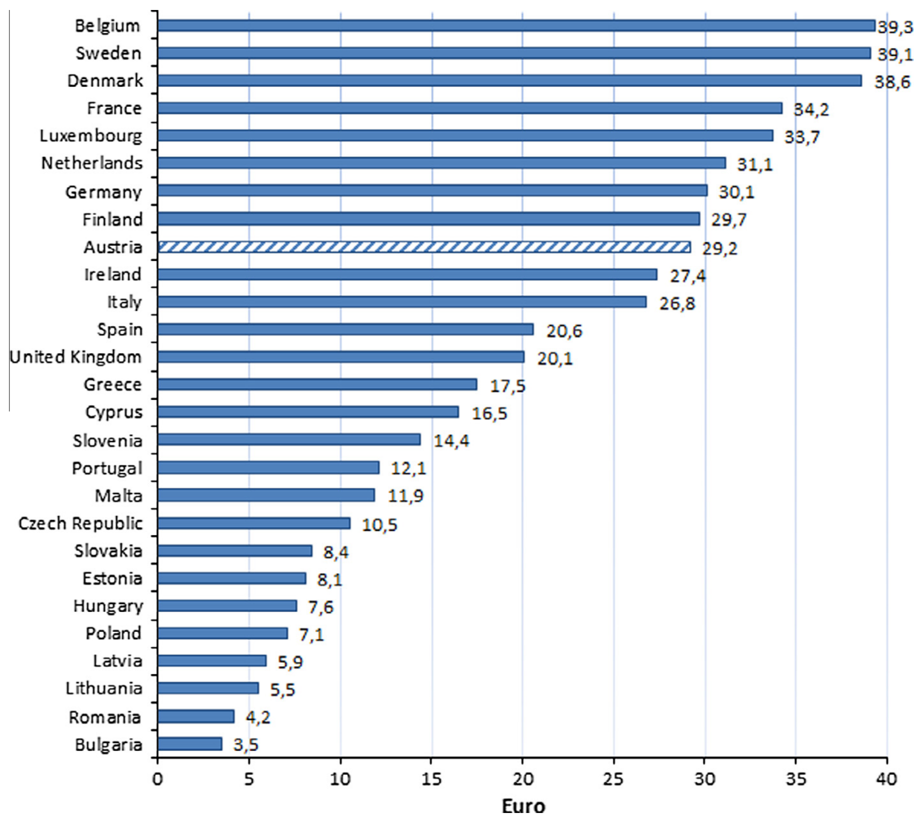

Fig. 1. Labour cost in euro per hour 2011.

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