Container Rail Volumes to Surge at 16% CAGR by FY25

October 28, 2022 l Ratings

Synopsis

In this report, CareEdge Ratings has analysed the imminent shift in the mode of freight movements from roadways to railways and the underlying factors facilitating the transition.

- CareEdge Ratings expects container rail volumes to grow at a healthy compounded annual growth rate (CAGR) of 15.60% for FY2022 to FY2025 with steady improvement in rail-coefficient to 31%.
- Slated completion of the prestigious Dedicated Freight Corridor (DFC) project by June 2023, increased trips of cost-effective double-stack container trains and incremental volumes of cement cargo through railways are prominent factors influencing the switch from roads to rail.
- CareEdge Ratings believes that transit assurance under DFC aiming to squeeze the travel period by 40-50% for some of the major routes shall accelerate this transition. This shall help in achieving 'Just in Time' inventory management and hence improve cost competitiveness.
- Nevertheless, higher haulage rates for freight traffic due to extensive cross-subsidization of passenger traffic and the absence of a regulatory body for the railways are the underlying key challenges for the modal shift.

A dedicated freight corridor boosts the modal shift from road to rail

Container cargo transported through railways (Rail volumes) grew by a healthy year-over-year rate of 17.63% to 74.38 million metric tonne (MMT) during FY22 as compared to 12.51% growth in overall container cargo volumes. The rail co-efficient also expanded by 115 bps to 26.70% during FY22, mainly supported by partial connectivity of the dedicated freight corridor (DFC) with Mundra and Pipavav ports on the western coast. This marks the beginning of the modal shift from roads to rail.

Slated completion of the prestigious DFC project by June 2023, a growing movement of cost-effective double-stack container trains and incremental volumes of cement cargo through railways are prominent factors for the switch from roads to rail.

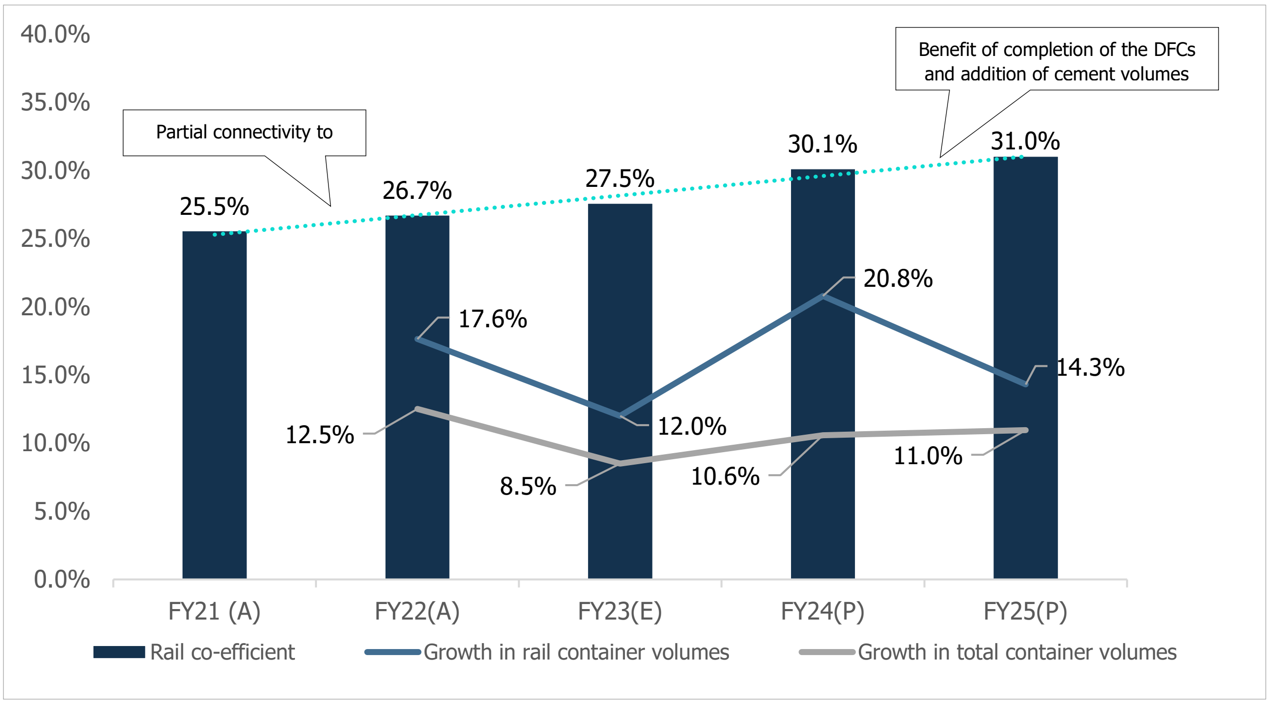
CareEdge Ratings believes that transit assurance under DFC with a reduction in transit period by 40-50% for some of the routes shall accelerate this transition. Based on estimates, inventory carrying cost constitutes 43% of the overall cost of logistics. Thus, a significant reduction in transit duration is expected to help in achieving Just-In-Time based inventory management thereby boosting the cost competitiveness of domestic goods. Nevertheless, establishing end-to-end connectivity through the electrification of feeder routes, container freight terminal and warehousing capacities are crucial for achieving the envisaged modal shift.

Modal shift expected in some of the bulk cargo categories

Indian railway's freight is dominated by a few bulk commodities like Coal, Fertilizer, Iron-ore and other raw material for steel. The government of India allowed transportation of bulk cement through containers in FY22, which shall boost rail volume growth for containers and could add incremental annual volumes of 10-12 MMT by FY25. Thus rail volumes are expected to be buoyant due to DFC benefits and cargo diversification in container volumes**.**

CareEdge Ratings estimates container rail volumes to grow at a healthy compounded annual growth rate (CAGR) of 15.60% for FY2022 to FY2025 with steady improvement of rail-coefficient to 31% and incremental volumes from cement.

Chart 1: Growth in rail container volume Vs overall container volume and Rail-Coefficient



Source: CareEdge Ratings

Land lease policy to improve privatization prospects and aid multimodal logistics

Higher land lease payment to Railways is one of the hurdles for the rail logistics segment. However, in September 2022, the Union cabinet approved a reduction in the railway land lease fee from 6% of the market rate of land per acre to 1.5%. The lease period has also been extended from the prevailing period of five years to 35 years. The new railways land lease policy is also a positive catalyst for the privatisation of the rail logistics sector and the development of 300 cargo terminals (in line with PM Gati Shakti framework).

National Logistics Policy to integrate data exchange among stakeholders

National Logistics Policy (NLP) aims to bring down the logistics cost of India to less than 10% of Gross Domestic Product (GDP), in line with other developed countries from the existing level of 14%.

The development of the Unified Logistics Interface Platform (ULIP) allows data exchange among stakeholders, which will improve work efficiency in the logistics sector by providing real-time information to all stakeholders and thus strengthen India's international competitiveness.

Higher haulage rates and the need for a regulator for railways are underlying challenges

The haulage rates are periodically notified by the Indian Railways and the charges paid by container train operators form 65-75% of their total operating expenses. As per a World Bank report, while ~60% of the capacity of the rail network is deployed for passenger transport, the segment contributes only ~30% to Indian Railway's freight revenue. This translates into extensive cross-subsidisation of passenger fares with freight fares reducing the competitiveness of rail freight over roads.

CareEdge Ratings opines the need for an independent regulator in railways from three key perspectives: (i) rationalising the freight tariff by determining the optimum level of cross-subsidisation of the passenger segment with the freight segment (ii) facilitating private participation by ensuring the protection of their interests, and (iii) transparent dispute resolution mechanism.

CareEdge Ratings View

The rail co-efficient expanded by 115 bps to 26.70% during FY22, mainly supported by partial connectivity of the dedicated freight corridor (DFC) with Mundra and Pipavav ports on the western coast.

"CareEdge Ratings expects container rail volumes to grow at a healthy CAGR of 15.60% for FY2022 to FY2025 with a steady improvement of rail-coefficient by 430 bps to 31% and incremental freight volumes primarily cement. CareEdge Ratings believes that transit assurance under DFC aiming to squeeze the travel period by 40-50% for some of the major routes and over 3x growth in the movement of cost-effective double stacker container trains by FY25 shall accelerate this transition. The new railways land lease policy acts as a catalyst for the privatization of the rail logistics sector and the development of 300 cargo terminals.

Nevertheless, prevailing high haulage rates for operating container trains due to extensive cross-subsidization with passenger freight, challenges in establishing end-to-end connectivity and the absence of regulator in Railways unlike other key infrastructure segments are impeding the modal shift of cargo from roads to rail." said Ms. Rajashree Murkute, Senior Director – Corporate Ratings.

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