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Growth derailed

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Overview

A growing imbalance between rapid growth in Indian ports and flagging investment in rail and road connections to those ports is hindering the country's ability to fully benefit from port development. From a micro perspective, this imbalance creates uncertainties for importers and exporters over the availability and price of their goods. This picture will change only gradually as public-private partnerships in port connectivity projects begin to flower and infrastructure planning becomes more integrated. Substantial investments are being made in small and large ports across India, and major firms such as Gateway Terminal India in Navi Mumbai are on target to meet their container traffic projections five years ahead of schedule. However, given the likelihood that port congestion and bottlenecks will worsen in the short to medium term despite the port investment surge, we see opportunities for logistics firms that can work to ensure quicker delivery of raw materials and finished products.

Context

Strong demand is driving port development, but infrastructure bottlenecks still plague Indian industry

Wrap

Infrastructure bottlenecks will persist in the near term

Trusted Judgements

Connectivity is lagging port development; the involvement of economic stake holders can help alleviate the problems

- > **Suresh Joseph**, general manager, DP World Cochin

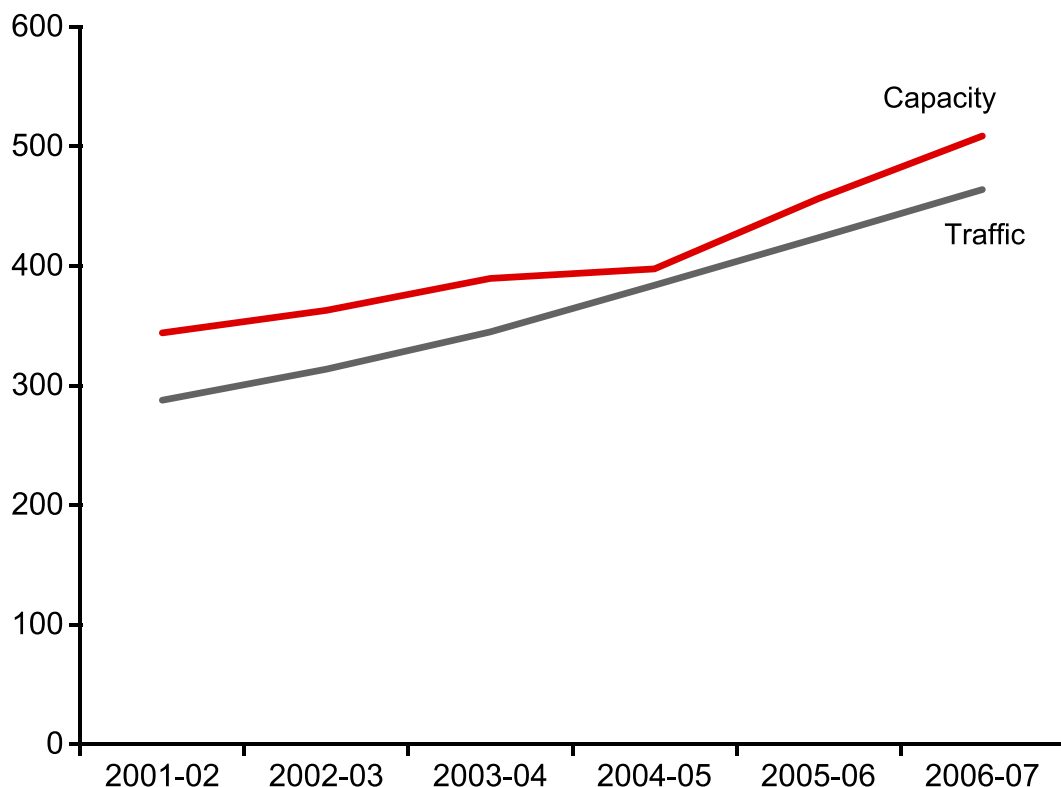
Context

Rapid growth in port traffic

Rapid economic growth in India is driving demand for imports of commodities such as coal and wheat, causing most of the country's ports to operate at full capacity. This has led to an emphasis in recent years on capacity expansion at major ports, increasingly via the public-private partnership (PPP) route. In the Tenth Five-year Plan period, an investment of Rs 53.9 billion (US\$1.3 billion) was made in ports, including Rs 19.1 billion from the private sector. Smaller ports that fall under state government jurisdiction have also succeeded in attracting investor attention, and private sector operators are developing greenfield projects along India's coastline, map [here](#).

These investments are starting to pay off. A case in point is Gateway Terminals India (GTI), a joint venture between the Netherlands-based APM Terminals (the world's second-largest container terminal operator) and the state-owned Container Corporation of India. GTI, in which APM Terminals has a 74 per cent stake, has been the "build-own-transfer" (BOT) contractor for one of three container terminals in the Jawaharlal Nehru Port Trust, Navi Mumbai, since October 2006. The venture originally had a targeted capacity of 1.3 million 20-foot equivalent units (TEU) by 2013, but had already attained more than 1 million TEU by November 2007. At this pace it will achieve its designated capacity later this year, five years ahead of schedule. Port developers from all over the world are vying for a fourth terminal at the Jawaharlal Nehru Port.

Traffic vis-a-vis capacity at major ports (million tonnes)



Source : National Advisory Council, Government of India.

The government is targeting substantial investment in ports in the Eleventh Five-year Plan (2007-12). India's port capacity is scheduled to rise from 737 million tonnes in 2007 to 1,500 million t in

2012. Investment of Rs 553 billion in major ports is envisaged. Smaller ports are expected to attract investment of some Rs 317 billion.

Connectivity lags port development

A combination of factors is responsible for lagging rail connectivity in India:

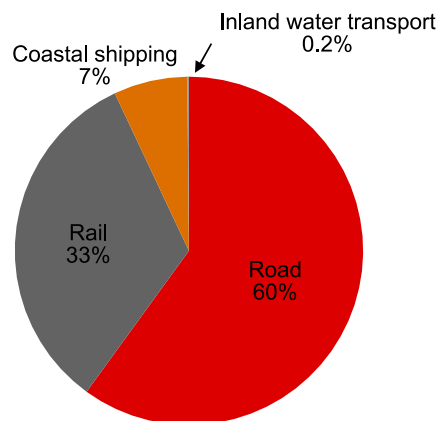
1) Inadequate investment

Connectivity projects have been unable to keep up with the fast pace of port development. In the Eleventh Plan period, the government plans investment of Rs 30 billion in 53 road and rail connectivity projects, equal to just 3 per cent of projected port investments, despite the fact that connectivity projects are more capital-intensive.

2) High rail freight tariffs

Excessively high rail freight charges have long sustained a preference for moving cargo by road, discouraging investment in railways aimed at port connectivity. This is attributable to cross-subsidisation of rail passenger fares by higher freight tariffs, which has restricted the market share of railways in freight traffic. Roads account for 60-65 per cent of freight traffic in India, compared with railways' share of only 30-32 per cent.

Modal share in freight transport, 2005



Source: National Maritime Development Programme.

This pattern has begun to reverse. Decisions by the railways to selectively increase the carrying capacity of rail wagons, reduce freight tariffs and offer incentives for the use of railway capacity during lean periods have helped win back market share from road transport. Compared with a target of 396 billion tonne kilometres in the financial year ending March 2007 (the final year of the Tenth Five-year Plan), the railways moved 475 billion t/km of freight.

3) Lack of integrated approach to infrastructure development

The railways are also finally concentrating on port connectivity projects, and the Ministry of Railways has set up a dedicated enterprise, the Rail Vikas Nigam (Rail Development Corporation)

to undertake port connectivity projects. The government is looking at PPPs to supplement its own resources by involving port developers and other stakeholders.

PPP in port connectivity projects

Project	Private sector partners	Public sector partners	Project description
Pipavav Rail Corporation, Gujarat	Gujarat Pipavav Port Limited	Ministry of Railways	33-year BOT concession for gauge conversion, operation and maintenance of 271 km rail link between Surendranagar and Pipavav port at an investment of Rs 3.35 billion
Kutch Railway Company, Gujarat	Gujarat Adani Port Limited (Mundra)	Rail Vikas Nigam, Government of Gujarat	Gauge conversion of the 301 km Gandhidham - Palanpur range in Gujarat, providing connectivity to Kandla and Mundra ports at an investment of Rs 5 billion
Hassan Mangalore Rail Development Company, Karnataka	Mineral Enterprises Limited	Ministry of Railways, Government of Karnataka, New Mangalore Port Trust, Rail Infrastructure Development Company (Karnataka)	33-year concession agreement for gauge conversion, operation and maintenance of 183 km rail line between Hassan and Mangalore at an estimated investment of Rs 2.75 billion
Haridaspur-Paradip Rail Link, Orissa	Essel Mining and Industries, Posco India, Jindal Steel and Power, MSPL, Rungta Mines	Rail Vikas Nigam, Steel Authority of India, Infrastructure Development Corporation of Orissa, Paradip Port Trust	Constructing 82 km long Haridaspur-Paradip rail link at an estimated investment of Rs 5.9 billion
Obulavaripalle-Krishnapatnam railway line, Andhra Pradesh	Krishnapatnam Port Company	Rail Vikas Nigam, Government of Andhra Pradesh, National Mineral Development Corporation	Construction of 113 km long broad gauge line at an investment of Rs 5.8 billion

Bharuch-Dahej Railway Company, Gujarat	Dahej SEZ Limited, Adani Petronet (Dahej) Port, Gujarat Narmada Valley Fertilisers	Rail, Vikas Nigam, Gujarat Maritime Board	Implementation of gauge conversion on the 63 km long Bharuch-Samni-Dahej rail line at an investment of Rs 3.5 billion
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Each connectivity project is undertaken by a Special Purpose Vehicle (SPV), a joint venture bringing together Indian Railways and various stakeholders. The Ministry of Railways generally awards a concession to the SPV to finance and construct the project, while land acquisition is undertaken by the railways with funds provided by the SPV. Revenues are collected by the railways and shared with the SPV on a predetermined basis. A potential risk to the PPP is that the railways sometimes tend to reroute traffic away from the SPV-financed line, depriving it of its legitimate share of traffic, but this is unlikely to be a significant problem in the future, given rapid growth in freight traffic.

The Ministry of Railways has also completed connectivity projects to the Haldia Port in West Bengal and Jawaharlal Nehru Port in Navi Mumbai, but even these are likely to find it difficult to handle the increasing traffic at ports. Increasing imports of coal and food grains will put further pressure on the already strained rail system in India as the railways account for 100 per cent of coal traffic and 70 per cent of food grain movement. The Indian railways also face a shortage of rolling stock which is being addressed by encouraging private sector investors to purchase rail wagons.

Eventually, the proposed Rs 280 billion Dedicated Railway Freight Corridor, financed by a Japanese government loan, will facilitate the movement of freight between Delhi-Mumbai (western corridor) and Delhi-Kolkata (eastern corridor). The Dedicated Freight Corridor India SPV has been formed to operate double-stacked container trains at a maximum speed of 100 km/hour along these corridors. However, this project will take at least five years to become operational. By this time the pressure of freight traffic to and from ports will have increased even further.

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Involvement of economic stake holders will help alleviate problems

Suresh Joseph, general manager, DP World Cochin

An integrated approach to planning and development of infrastructure in India is lacking. An apex body which ensures a concerted and integrated approach to development of infrastructure is absent. This is compounded by lack of coordination among government agencies and departments. Therefore the development of ports is not simultaneously accompanied by the development of other modes of transport to move cargo out of these ports.

Ports have shorter gestation periods and require less investment than road and rail projects, which creates a disjuncture between the development of ports and hinterland connectivity projects. Land acquisition problems also plague road and rail projects, but are less of an issue for ports as the land is already in the possession of the port trusts in the case of major ports. It is also necessary in some cases to develop road and rail connectivity across a wide variety of terrain en route to the port which can cause unforeseen engineering bottlenecks and lead to delays.

Added to this, connectivity projects are almost always unable to keep pace with growth in traffic at the ports once completed. Many connectivity projects also focus solely on linking ports to local rail or road networks and do not consider integrating other industries in the region.

Political incentives favour investment in populist schemes rather than in long-gestation infrastructure projects that do not bring a political payoff. Inadequate spending also paves the way for delays. Investments in rail and road connectivity projects by the relevant central ministries are often made with political considerations, resulting in poor allocation of resources.

PPPs are a step in the right direction, as stakeholders have the right economic incentive to invest and ensure timely completion of the project. Involving port operators and local industries in connectivity projects will aid in the timely completion of projects since they will demand transparency in bidding and awarding projects, bring in adequate funds and have an incentive to complete projects on time and on budget.

Wrap

Infrastructure bottlenecks will persist in the near term

As our trusted source points out, there is a growing mismatch between rapidly expanding port traffic and lagging connectivity due to a lack of integrated infrastructure planning. The Ministry of Railways has realised the importance of port connectivity, but faces implementation bottlenecks in the short term. Over time, PPPs involving local industries should help to alleviate the problem, as will the planned development of dedicated freight corridors.

In the short term, suboptimal rail connectivity will force Indian companies to hold larger than desired inventories. While this may impede manufacturing growth, it conversely provides a business opportunity for logistics companies that manage warehouses and can ensure on-time delivery using multimodal linkages. Firms that invest in connectivity projects and railway wagons such as Jindal Steel and Posco will also gain a strategic advantage as they will be able to ensure efficiency in production and supply finished products to their buyers more quickly.

Infrastructure bottleneck-linked commodity price volatility is likely to persist in the near term, as artificial scarcity is created by raw materials failing to reach their destinations on time. Given poor connectivity, port congestion is likely to increase in the short and medium term and reduce the absorption capacity for further investments in ports. It therefore seems quite likely that the envisaged investment in ports will not fully materialise in the absence of adequate connectivity.