PPP Initiatives and Indian Railways – Creating an agenda for Inclusive Economic Growth

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As an environmentally sustainable and economically efficient mover of goods and passengers, the Indian Railways functions as a pivotal organization in promoting economic growth and social integration in the country. In order to achieve double digit GDP growth levels, the Railways needs to act as a force multiplier and provide the engine that can pull growth to consistently higher levels. The Vision 2020 document of the Indian Railways spells out that "Indian Railways shall provide efficient, affordable, customer-focused and environmentally sustainable integrated transportation solutions. It shall be a vehicle of inclusive growth…"

In this article, we seek to highlight some key areas of concern for Industry with respect to PPP initiatives vis-à-vis the Indian Railways.

During last year's budget speech Honorable Minister of Railways had made a statement that "The time has come for **the business community to come and join hands to build partnerships with the Railways".** In creating infrastructure with private capital, the Indian Railways can create wealth, unlock efficiencies, and keeping in view the need for better utilization of national resources, build a strong, responsive and vibrant Railways organization with higher levels of capability.

The figures for the growth in traffic show that between 2004-05 and 2009-10, growth in traffic has been from a level of 602 million tonnes to 890 million tonnes at a CAGR of 8.13% per annum. At the same time, freight earnings have also grown from Rs 31,000 Crore to Rs 58,700 Crore during the period in review.

There have been two primary factors that contributed to the performance of the IR in the previous 5-6 years. On the one hand, the economic boom prior to the crash of 2007-08 fuelled transportation demand and generated growth for the Railways. Second, the IR followed a strategy of reducing the slack on infrastructure and capacity by following strategies both at the operational as well as the commercial levels that sought to intensify asset use and rationalize commercial working. Besides the obvious short/medium term benefits that have been witnessed as a result, one of the outcomes of this strategy has also been to generate a need for development of further infrastructure and capacity to deal with growth in demand that inevitably follows any industrial or economic resurgence.

Besides substantial increases in track capacity, the Indian Railways needs three times as many locomotives, wagons, and coaches and an almost entirely new/upgraded terminal network if it has to meet the likely demand for services. Therefore, the plans for setting up modern rolling stock manufacturing units to handle current and projected demand must be accelerated and the

Railway Board should be empowered and be held accountable to implement these projects on a defined time line. Rapidly increasing traffic demand has made some sectors highly capacity constrained. While building the Dedicated Freight Corridors (DFC) will be necessary, while DFC implementation is underway, Railways should also consider deploying modern technology to improve safety and increase throughput in existing capacity constrained segments especially those in the South Eastern, East Coast and South East Central railways that are carrying the maximum bulk volumes, and along the Northern, Western and North Western routes that are dominated by container volumes.

The key challenges faced by the Railways will emerge from the growing demand and the limitations on existing infrastructure and capacity to deal with this growth. Infrastructure investments and enhancing capacity with the introduction of new technologies will need to be the combined strategies to meet this challenge.

Expansion and Investments in Infrastructure – PPP initiatives

As the IR embarks on a process for growing its infrastructure and assets to deal with emerging demand growth, an opportunity automatically presents itself for attracting investment partnerships in this endeavor. Such investment, which is usually seen in the form of various PPP initiatives, is meant to invite interested bidders from the private space to participate in rail projects in what ideally should be mutually beneficial or **"win-win"** arrangements.

PPP engagements need to be clearly segregated from outsourcing of various rail tasks. To this end, it is imperative that the IR appreciate that PPP initiatives must be those where there is a **sharing of both risk and reward** of investment by both partners in the process. It is a matter of some concern for industry that the Railway sector which forms the very backbone of land based transport in the country has seen extremely limited PPP initiatives for participation of the private sector in Rail related investments.

Some suggestions to improve the working of the PPP initiative as well as promote development of infrastructure on the IR system are indicated below:

1. **The approvals process and closure of projects has been delayed in almost all initiatives.** Repeated postponement of bids for major projects such as the locomotive factory at Madhepura in Bihar, an engine-component unit at Dankuni and a coach plant at Kanchrapara in West Bengal have severely impacted plans of industries seeking participation in such projects and also acted as a dis-incentive for others from entering into territories where many have had to suffer financial and time delays of their investment plans.

2. **Wagon leasing options:** The Rail Minister's commitment to announce a Modified Wagon Investment Scheme is still unmet, and the existing wagon leasing policy has seen limited response. **The primary issue related to these policies relates to the linking of freight rebates with a fixed time frame for reimbursing returns on capital employed.**

There is also a restriction on both the type of wagons that are covered as well as commodities that can be carried. This further restricts the market and has resulted in a situation where the very sectors like coal and ores that would see the maximum potential from investment in ownership or leasing of wagons find themselves excluded. Similarly, only special type and high capacity wagons are included in the wagon leasing policy. These restrictions need to be removed so that a wider participation is possible in the space and the overall availability of available rolling stock can be enhanced from various sources.

3. **PPP and IR Terminals:** Terminals are the gateways into the Indian Railway network and it is only through the development of better terminals that incremental cargo volumes can be attracted to the rail mode. The existing framework of private sector participation in the terminal space was expanded in the past year with the announcement of the PFT (private freight terminal) and Auto Hub Policies, which created a potential for expanding the terminal network beyond existing goods sheds, ICDs and private sidings. These policies have however some key flaws that have restricted the interest shown in development of terminals on the PPP model envisaged.

   The PFT policy does not effectively invite investment in a true PPP framework as the IR is not actually providing a concession to the private terminal developer. What is being provided is a permission/license to undertake a new activity, i.e. goods shed operation, which has erstwhile been under the exclusive rights of the Indian Railway as a Monopoly rail service provider. In exchange for this not only is a onetime fee being expected, but a long term revenue share too is expected to be paid even though the IR does not have any opportunity loss of income or gives up in any way its own rights as a terminal or rail service provider. For a true PPP model to be developed, the IR must offer its own land if its wants to earn a revenue share. Such land would have to be bid out on a competitive basis, and only then would a concession agreement with a revenue sharing agreement be actually warranted. Other aspects in the policy that need to be addressed include matters like limiting the time period of the agreement to 20 years even though the land is to be privately owned.

   In the Auto-Hub policy, the list of eligible agencies that can apply is too limited. Also, since the list specifies only manufacturers, logistics players sponsored by manufacturers or registered SFTOs, a contradiction develops at a later stage in the policy, where the idea of a common user facility with no exclusive rights is talked about. Seven years is too short a period for any kind of an infrastructure project to yield returns. Also, if licensee is not allowed to sub-let, it would become practically difficult to implement a common user solution. Finally, the concept of prior approval of Railway administration for maximum charges that can be levied must be removed. The nature of services provided in an auto hub is of a specialized type in which IR has no expertise. Once a facility has been handed over to an operator/developer, and he is being charged a commercial lease for use of the land, price regulation is best left to market forces.

Within the terminal space, the Railways should also look at leveraging its available land at existing as well as underused facilities for up gradations through private sector participation. While much attention has already been given to the development of mega-terminals, multi-modal hubs etc., it is equally important to develop a larger network of small and medium terminals (ranging from 5 Acres to 20 Acres) that improve quality of access to the Railway system.

4. **PPP and Container Rail Operations-** A major initiative taken for private sector participation in the Rail sector came in 2007, with the signing of the concession agreement for container rail operations with 15 operators. As perhaps the biggest PPP initiative taken by the Railways, this effort has received a lot of attention both from the Railways as well as the Trade. However, three years into the effort, many gaps still remain that need to be urgently addressed. The agreement is not in effect a concession at all, as it provides no benefit of asset or infrastructure transfer to the operators. Operators are captive customers and need to be given the rights of customers rather than concessionaires

   Some Recommendations for the container rail sector:

   a. IR needs to be more liberal in granting permissions on use of Railway owned goods sheds (CRTs) for container handling. They should also actively encourage co-user access in private sidings to provide a wider terminal access for container operations.

   b. Maintenance of wagons is currently done only by IR. There should be a provision for wagon owners to maintain their own wagons as is the global practice in this regard.

   c. IR needs to consider providing reasonable transit commitments, and following an equitable reward and penalty regimen for charging in case of delays, stabling of trains etc.

   d. IR needs to provide some commitments on stable rail haulage rates, provide adequate notice for increase, and ensure competitive advantage over road to ensure that the sector is able to attract the road based cargo.

   e. The previous year has seen the introduction of an extremely restrictive pricing policy that has identified 9 important commodities and raised their container haulage charges to levels where their containerised transport is effectively priced out. Such restrictive practices need to be rolled back as not only do they give the wrong signal to potential investors, but also add to the already increasing logistics cost and inefficiencies in the overall system of cargo movement.

5. **SFTO and AFTO policies:** These two policies were also introduced in the previous year but are yet to attract any takers. Both policies suffer from similar problems though the final policies have been considerably modified from their original draft versions. The concept of high entry fee to be paid merely for the right to own one's own assets does not appeal to most potential investors as it is an unnecessary cost increase for most investors. The permission and scrutiny mechanisms are long-winded and a lack of any time commitments have tended to put many expressions of interest or even firm applications in bureaucratic loops. Private maintenance is not provided for even though new technology is expected to be brought in for specialised and heavy load movements. Finally, the concession agreement that is to serve as the legal contract between IR and potential investors has still to be provided and it is un-reasonable to expect investment from the industry unless the legal and contractual obligations that would govern the process are defined in the first place.

6. **Improved Project Management:** Most of the private investment policies that have been announced seem to lack the "**will to implement**". To improve and facilitate efficient project management practices, Railways should expedite & streamline various approval processes with a view to providing time bound clearances which are required for various Rail connectivity projects. Railway should create a dedicated cell for such approvals and ideally have a single window policy. At present, all core sector Railway siding projects are suffering due to time taken in various approvals and the uncertainties associated with un-met timelines, last minute change requirements etc.

7. **Modern fitted Coaches:** Permitting private agencies to enter into the field of furnishing the interiors and fittings for passenger coaches is also a possible area of private investment or participation that needs to be looked at by the IR. Private investment working with creatively designed revenue share models for such a space could go a long way in not just improving the quality but also the overall customer experience and leave IR customers with much greater feeling of satisfaction from their rail interaction.