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Indian Port Logistics Industry – CFS/ICD/CTOs

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Direct Port Delivery (DPD) volumes at JNPT have stabilised; CFSs continue to handle similar volumes but at reduced margins

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Overview

DPD volumes at JNPT have stabilised; CFSs continue to handle similar volumes but at reduced margins

DPD continues to be a long-term concern for the CFS model;

Data for Q3FY2019 from JNPT and for January-February 2019 indicates that over the last 6 months, the proportion of DPD volumes has seen a modest increase from 41% to 43%. While there has not been a major increase in the absolute volumes imported through DPD, which hover around ~130,000 to 140,000 containers on a monthly basis, the impact on realisations of CFS players and consequently their profit margin is beginning to become more pronounced. Many CFS players had been reporting pressure on operating margins since the start of DPD in February 2017, however, in Q1-Q3FY2019, some CFS players have reported a sharp drop in performance. Other CFS players who are generally end-to-end logistics players and have a competitive advantage over others have been able to retain volumes along with some moderation in profitability as a significant proportion of the DPD cargo is still being routed through the CFSs. Going forward, ICRA believes that unless the CFS players tweak their business models to offer an alternate value-addition to their customers, it is unlikely for them to deliver their earlier EBITDA margins from their businesses. While ICRA believes that there could be limitations to possibilities for DPD proportion moving above a certain level as all importers may not be positioned to transition to it, going forward, given the continued push for more DPD and possibilities of introduction of Direct Inland Delivery (DID), there could be increased pressure on average realisations of integrated port logistics players. Trade continues to be a beneficiary of the scheme as users have witnessed a decline in logistics cost.

Direct Inland delivery (DID) to further improve the ease of business

Implementation of DID could put pressure on margins of ICDs

The government of India plans another reform - a new import handling plan to supplement the DPD program. Authorities have called on various stakeholders to examine the last touch logistics plan for inland container depots (ICDs) - Direct Inland Delivery (DID). This should be another positive for hinterland shippers striving to reduce logistics costs in a hyper-competitive market environment. This is largely on the back of the success achieved by DPD which has reduced the dwell times and overall cost for importers in order to extend the same benefit to users of ICDs. The same is being implemented by the Central Board of Indirect Taxes & Customs (CBIC). The board has suggested that importers registered under DID will have to complete documentation and duty payments prior to goods arrival at their designated ICDs and that stakeholders should consider offering tariff incentives for DID containers, in lieu of free storage days that apply under the normal delivery practice. There will be a need to devise a tariff structure [which acts as a financial incentive] where importers voluntarily opt for DID clearance for pre-identified containers, rather than avail the free period at ICD as non-DID containers. Further, the board has asked stakeholders to take into account cases where all containers manifested on the bill of lading do not arrive in a single shipment, which happens frequently at ICDs, and suggested that custodians extend DID to all manifested containers, including those yet to arrive, subject to other compliances.

At this point, the actual savings that can be achieved, the extent to which the importers are willing to accept this program and the real advantage of DID remain to be seen. ICRA believes, that while this is a positive development for importers and could help in reducing the transit time, thereby easing business, similar to the impact on CFS players on account of DPD, there could be an impact on the business model of ICDs. There would be an impact on the overall revenues earned from imported containers thereby affecting margins.

Rail volumes witness sequential decline during Q3 FY2019

Rail volumes witness sequential decline during Q3 FY2019, timely implementation of DFC projects will be crucial to drive growth in the medium term: After witnessing moderate growth in volumes during FY2017 due to some pick-up in EXIM traffic as well as some pick up in domestic traffic due to introduction of services like time table-based trains, the growth accelerated during FY2018, driven by traction in both EXIM and domestic volumes. However, during 9m FY2019, while there has been yoy growth, during Q1 FY2019 and Q3 FY2019, some sequential decline in volumes have been witnessed due to moderation in exim volumes. The timely completion of infrastructure projects like dedicated freight corridor in a timely manner will also be crucial to drive growth in this segment in the medium term.

Stable outlook in the near term as trade volume growth revives; favourable growth outlook over the medium term, driven by increasing containerisation, new terminals/ ports, DFC and DMIC

Stable near-term outlook; favourable long-term prospects: In terms of the near-term outlook for the container logistics sector – the CFS, ICDs and CTOs segments are expected to display moderate growth in the current fiscal and FY 2019 as the international trade volumes have shown a revival. Notwithstanding the moderation in economic growth, the industry's long-term prospects remain highly favourable as containerisation witnesses a renewed focus with new capacities coming up online and providing the necessary environment for increased usage of containers. On account of the country's growing external trade and increased orientation towards containerisation, container traffic volumes should grow at a 10-12% CAGR over the next decade. The growth in the port logistics segment is expected to be mainly led by benefits arising out of GST implementation and volume growth in containerisation/new terminals at ports leading to incremental growth in volumes. Besides, the port logistics industry should benefit from a favourable demand environment over the long term due to ongoing projects such as a dedicated freight corridor (DFC) and the Delhi-Mumbai industrial Corridor (DMIC), as well as the opening up of new business segments like 3PL and cold chains.

Credit issues for the CFS/CTO operators

ICRA Research believes that CFS players at JNPT could face pressure on margins in the near term on account of diversion of volumes to DPD and lower storage incomes resulting from it. Players who are able to retain volumes and offer value added services may stand to fare better than other players. At all ports handling containers, large number of CFS operators results in high competition for incremental volumes and could result in some consolidation going forward. Credit profiles of CTO players are susceptible to increase in haulage charges and also face competition from road carriers. Further, the business remains highly capital intensive as players have to set up new terminals in order to expand operations.

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