The story of the indian railways business essay

The story of the Indian Railways (IR) is truly a “ Turnaround”. After almost being declared bankrupt in 2001 according to the Expert Group, the Indian Railways is today, “ India’s second largest profit making Public Sector Undertaking, only next to ONGC” (Raghuram, 2007).

The Indian Railways in considered to be the country’s “ prime mover”, and boasts of having the largest network in Asia. The Indian Railways was first established in 1853 and travelled a distance of a mere 34 kilometers (kms) (Alivelu, 2012). The first ever train in India to use ‘ iron wheels’ was on 16th April, 1853 – the train has a capacity of 400 with fourteen carriages and travelled from Bombay to Thane, taking seventy-five minutes.[1]

A year after independence the Indian Railway system had already grown to consist of forty-two different railways systems “ consisting of 13 Class I Railways, 10 Class II Railways and 19 Class III Railways” (Alivelu, 2012). The various classes were segregated according to gross earnings and one of the biggest tasks the IR faced was in merging all the different railway systems of India into one – the princely state railways, the state owned railways.

In 1950 the Railway Board of India decided to “ regroup” the Indian Railways into six main zones namely, the Northern, the North Eastern, the Southern, the Central, the Eastern and the Western Railways[2]. In the following years seven more zones were created, like the South Central Railway, to aid in the better functioning of the railway system as a whole. This brought the total number of zones to sixteen.

Today, the Indian Railways operates more than 11, 000 trains in a single day, 7000 of which are passenger trains, making it the “ second largest rail network in the World", under a single management (Gupta & Bhat, 2007). The Indian Railways is essential for the growth of the country and it plays an important role in catalyzing the pace of economic and socio-economic development (Gupta & Bhat, 2007).

Nevertheless, the Indian Railways success story was inconsistent. To further prove my point, take for example the 1990s when the IR had financial troubles bringing questions of its ability (or inability) to provide for a competitive transport system of railways in the future. The reason for this was simple: the Indian Railways was always seen as public service, a service used by even the lower classes of Indian society and essential for all.

Over the past fifty years the Indian Railways not only played a major role in transporting passengers (PKM – passenger kilometers) but also freight (NTKM – net tonne kilometers)[3]. Soon enough, the Indian Railways was losing traffic to the roadways and in-passenger services were being subsidized for freight. The Indian Railways was faced by an imminent financial crisis.

Overview of Financial Performance of the IR

The Indian Railways is a department of the Government of India and is the largest organization in India (Gupta & Sathye, 2008). It has a capital investment of about Rs. 55, 000 crores and " has been pivotal to the developing economy of the country as a whole"[4]. The Indian Railways account for 1% of the county's GDP and is the largest employer with 1. 5 million staff in the organized sector (Gupta & Sathye, 2008). Its sheer size " and its mode of operation as a government department, present special challenges for the management of railways as a commercial enterprise. They also add to the difficulty of responding to both short and long-term changes in transport market conditions”[5]. Due to its size the government gives great importance to the Indian Railways and was undoubtedly concerned during its financial crisis in the 1990s. To help combat such a problem, the Government of India appointed the Rakesh Mohan Committee (RMC) to the probe the matter further. The Committee stated, “ IR is today on the verge of a financial crisis. Urgent action is needed to revitalize it so that it can continue to serve the nation”[6].

The RMC identified several factors that could have led to this financial decline. Some of the factors identified by them are inflexibility in pricing, loss of market share in freight business (that was profitable) and high cost of internally supplied products and services (Gupta & Sathye, 2008). Despite these problems, the RMC identified poor accountability as the prime reason for the financial decline. This was further exaggerated by rising labour (employee) costs and no productivity (Gupta & Sathye, 2008). However, an underlying factor is the fact that all major decisions in India are given much political emphasis, forgetting the public needs, choosing populist decisions over sounds business decisions.

This paper outlines various strategies used by the Indian Railways to improve its operations after the 1990s debacle. Some of the initiatives outlined here are its cost cutting measures, revenue raising initiatives and environmental factors. The turnaround story and the option of privatization of the Indian Railways are also describes and analyzed in this paper.

Cost Cutting Measures

Cost cutting or retrenchment as a strategy consists of several other sub-strategies that include: selling of assets, improving efficiency, outsourcing, withdrawing from areas in which it is underperforming, “ businesses that are not value added” and reducing its large scale of operations among others (Gupta & Sathye, 2008). However the key area of study and emphasis is on retrenchment and control of costs. Mr. Laloo Prasad Yadav, the Railway Minister in 2004, made a speech regarding the Railway Budget wherein he outlined his strategy. He said, “ Operating expenses will in no way be allowed to exceed the barest minimum require and cost effective use of assets will be ensured”[7].

Review: Businesses that are not value added

The first service that was leased out under Mr. Yadav’s time was its catering service to IRCTC. This was done after a thorough review of its business. The catering facility is essential for both static and mobile passengers. By static I refer to passengers on the stations and by mobile I talk of passengers on trains. The outsourcing of the catering business to IRCTC took place by an open bidding system to beat political pressures (Raghuram, 2007). Mr. Yadav stated in the 2007 Railway Budget that the IR has reduced its losses by more than Rs. 1000 crores by simply leasing its catering and parceling services (Gupta & Sathye, 2008). Likewise by “ attracting private investment under the wagon investment schemes”, the Indian Railways could channelize its resources elsewhere.

Year

2001-02

2002-03

2003-04

2004-05

Total no of pairs of trains catered

228

231

234

250

Pairs of trains continuing as departmental

43

39

38

12

Static catering units

3152 stations

3152 stations

3152 stations

9270 units

Sales turnover of departmental units (Rs cr)

196

202

172

191

License fee(Rs cr)

23

26

29

59

IRCTC income (Rs cr)

37

42

76

Source: (Raghuram, 2007)

Efficiency Improvements

The Indian Railways operating ratio (which is considered a key indicator to measure financial performance) was drastically reducing from 2001 to 2007. Take these figures into consideration to demonstrate the point mentioned above: from 98. 8% in March 2001 to 83. 2% in 2006 to a significantly lower 78. 7% in 2007. A lower operating ratio is better than a higher one. The Indian Railways operating ratio can easily be compared to China Rail’s (60. 7% in 2006) and even Canadian Pacific Railway’s score of 75. 4% in the same year. According to the Business Standard, the Indian Railways Minister, Dinesh Trivedi, 2012 released a statement in the Lok Sabha with the IR’s Budget proposal for the fiscal year 2012-13 stating, “ I expect to achieve an Operating Ratio of 84. 9% in 2012-13 as compared to 95% in the current year. If this trend continues, I have no doubt that my Operating Ratio will improve upon even the best ever of 74. 7% within the 12th Plan” (Business Standard, 2012).

A few of the strategies employed by the Indian Railways to improve its efficiency are in two broad fields, “ modernization” and “ technology up gradation”. Under these fall, firstly, improving its operating mechanism for freight transportation with the help and introduction of the Freight Operating Information System. Secondly, to improve safety and line capacity the IR introduced modern signaling and telecommunication technology. Thirdly, it computerized its control offices and Coaching Operations Information Systems completely with the help of National Train Enquiry System. The introduction of better technology into the Indian Railways greatly benefitted its passengers and efficiency of the system.

Downsizing

The Indian Railways Minister made harsh decisions to downsize the railways. The initial plan of downsizing began when Mr. Nitish Kumar was in power and continued when Mr. Yadav took office. The plan adopted by the Indian Railways was not to fill any vacancies created in employment due to retirement or any other reason. Although the number of workers employed is still over a million, the numbers reduced from 1. 472 million in 2003 to 1. 412 million in 2006. Even the staff on payroll was drastically reduced by 10% from 1. 58 million in 1999 to 1. 41 million in 2006 (Gupta & Sathye, 2008). All of the above measures resulted in a decline in expenditure.

Outsourcing

As mentioned earlier the Indian Railways had leased out its catering and parceling services. Apart from this it also outsourced its advertising campaigns. They used a public-private partnership strategy instead of the traditional retailing (Gupta & Sathye, 2008). By outsourcing their advertising they hoped various zones within the railways would become more proactive (Raghuram, 2007). " The overall IR earnings had gone up from Rs 50. 2 crores in 2004-05 to Rs 78. 1 crores in 2005-06" (Raghuram, 2007). These figures are evidence and give weight to the Indian Railway's ' turnaround' story.

Repositioning

Repositioning includes product innovation, rebranding, and product differentiation. This section will outline the above mentioned strategies and the measures that were taken by the Indian Railways.

Focus on growth

The Indian Railway’s main aim and primary focus was on meeting the requirements of its passengers. Freight users and passengers are the two main customers of the Indian Railways and the majority of their revenue comes from them. Their revenues make up a total of “ two-third and one-third of total railway revenue” (Gupta & Sathye, 2008).

Freight

In 2004 there was a steep growth in the freight revenue and this was one of the main reasons for the turnaround of the Indian Railways (Gupta & Sathye, 2008). Two factors have been identified for the reason of the turnaround Mr. Raghuram highlights this in his paper – “ The essence of the turnaround was in fact that (i) total revenues increased by a significant percentage in the last two years and (ii) the net revenues continued a robust upward trend” (Raghuram, 2007). The various measures helped the Indian Railways in two ways; firstly, in increasing the amount of goods that could be transported and secondly, in increasing the revenue earned per unit for freight.

A number of measures were carried out by the Indian Railways with regards to wagon turnarounds and freeing of wagons. For example, customers were being given incentives to free wagon spaces faster and were constantly encouraged to free up wagon space and round the clock loading and unloading systems were introduced. There was better connectivity to ports and refrigerated vans were introduced to transport perishable goods like food products. “ All these measures put together resulted in raising the percentage of average annual growth rate in freight volume from 2. 34

(2001) to 7. 90 (2006) and freight revenue from 6. 31 (2001) to 17. 90 (2006) and to 14. 96 (2007)” (Gupta & Sathye, 2008).

Passenger Revenue:

The two schemes adopted by the Indian Railways to improve and capitalize on passenger revenue are: 1) an increase in the passengers comfort and providing better amenities for them and 2) make pricing competitive (competitive pricing). The Indian Railways added many new coaches (bogies) to trains where there was high demand. Mr. Yadav also improved safety on bridges, tunnels and areas of common mishap along with safety of passengers on running trains. In terms of competitive pricing, they reduced air-conditioned train ticket fares in response to the numerous low-budget airlines that sprouted in the last couple of years.

Product innovation

Most of the product innovation that took place in the Indian Railways revolved around freight. “ Double stack container” trains were introduced, increasing line capacity, and many new stations were added to handle the overload of freight (Gupta & Sathye, 2008). All of these measures according to economist Das have “ led to saving of about seven percent on capital cost and 25 percent in operating expense”[8]. Lastly, “ it introduced new design of wagons with higher pay load (carrying capacity) but lower tare weight (weight of the empty wagon) that improved safety features” (Gupta & Sathye, 2008).

Product differentiation

Unlike previously, the Indian Railways is constantly competing with the aviation sector after the introduction of low-budget airlines. It is also directly competing with roadways as many passengers may chose to drive down after the betterment of our national highways. The Indian Railways therefore had to improve on its product and improve and provide for better amenities for its passengers. One of its most groundbreaking innovations has been the introduction of e-ticketing where passengers can directly book their tickets online from the comfort of their homes through the Indian Railways official IRCTC website. Apart from this, IR has also introduced new bogeys that are more spacious and can accommodate more passengers.

Environmental Factors

Macroeconomic conditions

What proved crucial for the Indian Railways was the fact that the Indian economy was doing very well during its turnaround. The Indian economy was growing at an average pace of 8. 5% at the time when Laloo Prasad Yadav was sworn in as Minister (Gupta & Sathye, 2008). " This growth environment offered an opportunity for the IR and had a significant impact on the turnaround" (Raghuram, 2007). Undoubtedly this increased the demand for not freight but also passenger travel simultaneously and seamlessly helping IR.

Rise in demand

The Indian Railways success is mirrored by India's economic activity at the time. There was an increase in the demand for pig iron used in steel plants, for coal used for electricity, and for cement that is used for construction. All of these increased freight. And to add to IR benefits, India was exporting 84% of its iron ore to China and to reap from these benefits it increased the freight on iron ore.[9]

Legal position

The Supreme Court's ruling in November 2005 came as a blessing in disguise for the Indian Railways. The Court " banned overloading of road transport vehicles" (Gupta & Sathye, 2008). This meant only one thing for the IR – an increase in freight and therefore an increase in revenue. It is said that " The average road freight rate for transportation shot up by about 25 to 30 percent in the short run increasing the difference between road and rail freight cost"[10].

Pay Commission

In India, the Pay Commission appointed by the Government of India determines the pay of its Ministers and civil servants. A hike or reduction in pay does not necessarily translate to the same effect on pensions. The Pay Commission is said to have increased the pay of all IR employees by 34% in 1997 (Gupta & Sathye, 2008). However, by 2003 the pay rise rose to almost 14% of what it was in the 1980s. According to Gupta et al, " By the time the present Railway Minister took over, the impact of this pay rise and pension liabilities had been absorbed by the system through increased redundancies" (Gupta & Sathye, 2008).

Decline in financial costs

The last area to be analyzed is the decline in financial costs. In terms of the Government of India's rules and regulations the Indian Railways is given an unfair advantage as compared to the roadways of India. For example, the interest rates are lower and IR is requisite to give 6. 5% in dividends, a reduction from 7% in 2004-2005 (Yadav, 2005). This dividend is paid only on the Government's investment in the Indian Railways. I say that the Indian Railways is at unfair advantage to the roadways simply because the latter has " to borrow at commercial rates" (Gupta & Sathye, 2008).