

Road freight IMPACT ANALYSIS

Increase in road freight rates to offset hike in diesel prices

Summary

Diesel prices, which account for 55-60 per cent of the total cost for a transporter, are a key determinant of road freight rates. CRISIL Research expects truck freight rates to increase by 3-4 per cent, in the light of Rs 2 per litre diesel price hike.

Contents

Section

Diesel prices head North, road freight rates to follow 1

Figure

Freight rates Vs Diesel prices 1



About CRISIL Limited

CRISIL is India's leading Ratings, Research, Risk and Policy Advisory Company.

CRISIL offers domestic and international customers a unique combination of local insights and global perspectives, delivering independent information, opinions and solutions that help them make better informed business and investment decisions, improve the efficiency of markets and market participants, and help shape infrastructure policy and projects. Its integrated range of capabilities includes credit ratings and risk assessment; research on India's economy, industries and companies; global equity research; fund services; risk management and infrastructure advisory services.

About CRISIL Research

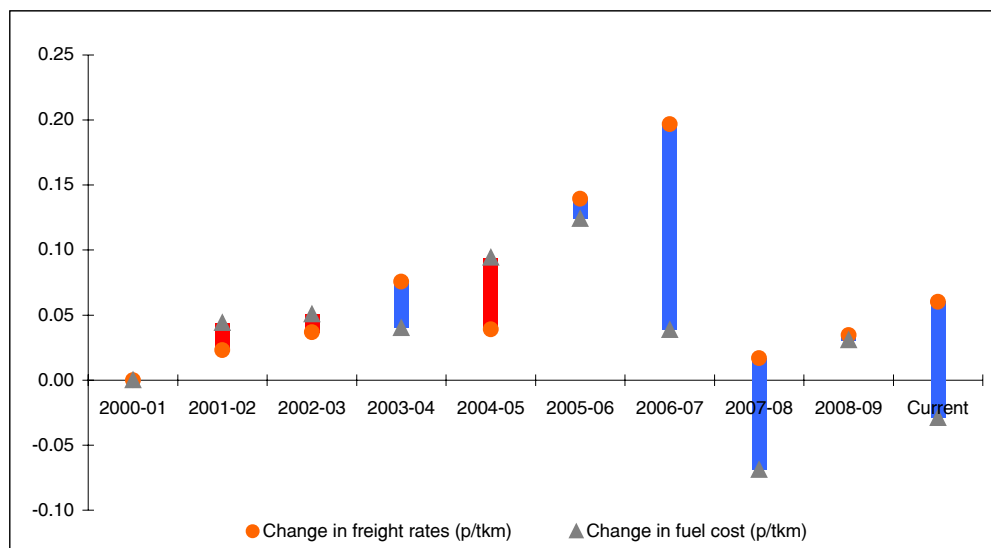
CRISIL Research is India's largest independent, integrated research house. We leverage our unique, integrated research platform and capabilities spanning the entire economy-industry-company spectrum to deliver superior perspectives and insights to over 600 domestic and global clients, through a range of subscription products and customised solutions.

Disclaimer

CRISIL Research, a Division of CRISIL Limited has taken due care and caution in preparing this Report. Information has been obtained by CRISIL from sources which it considers reliable. However, CRISIL does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. CRISIL is not liable for investment decisions which may be based on the views expressed in this Report. CRISIL especially states that it has no financial liability whatsoever to the subscribers/ users/ transmitters/ distributors of this Report. CRISIL Research operates independently of, and does not have access to information obtained by CRISIL's Ratings Division, which may, in its regular operations, obtain information of a confidential nature which is not available to CRISIL Research. No part of this Report may be published/reproduced in any form without CRISIL's prior written approval.

Diesel prices head North, road freight rates to follow

Freight Rates v.s. Diesel prices



Current: as on July 2009; tkm: Tonnes-kilometres; P: Paise

Source: CRISIL Research

The hike in petrol and diesel prices effective from July 2, 2009 is unlikely to have a substantial impact on the transportation sector. Transporters are expected to pass on the -- Rs 2 per litre -- hike in diesel prices to consumers. We believe that transporters will not be in a position to absorb the cost increase as their cash flows are already at near break-even levels.

The hike in diesel prices is expected to result in a 3-4 per cent increase in the freight rates on contractual fleet. Spot transactions are however likely to have varied increases depending on the route. Industry interactions indicate that, on some routes, transporters may increase rates by as much as 6-8 per cent initially, which may eventually stabilise at lower levels depending on market dynamics. At present, the freight movement is almost equally divided between spot and contractual arrangements.

The operating costs for transporters are estimated to increase by 5 paise per tkm (tonne-kilometre) from July 2009; on account of the hike in fuel costs. Post the cut in diesel prices in January 2009, truck freight rates remained almost stable. However with signs of marginal improvement in freight movement, we expect the hike in diesel prices to be passed on to the end-users.

The above analysis takes into consideration the two factors that determine the pricing flexibility of road transporters viz, competition from railways and the demand-supply scenario of trucks. Since there is no indication of increase in rail freight rates so far, the cost competitiveness of road freight will reduce further. However, the inter-modal shifts will continue to be driven largely by structural advantages and the impact of relative pricing on growth in road freight is expected to be marginal.

The demand-supply scenario for mid-sized and heavy goods vehicles has been unfavourable from the second half of 2008-09, the period which coincides with the slowdown in growth of index of industrial production (IIP), thereby indicating lower freight availability. The sharp drop in truck purchases in 2008-09, due to higher interest costs as well as unavailability of freight have resulted in a 41.3 per cent y-o-y decline in incremental tonnage capacity of mid-sized and heavy trucks, as compared with a 2.6 per cent increase in the IIP. Consequently, obtaining freight contracts was easy till September 2008, post which there has been a reduction in freight availability thereby leading to a slowdown in contract renewals even for large fleet operators. Spot operators have been facing huge losses since September 2008.

Transporters' cash flows are already under immense pressure. CRISIL Research therefore estimates that transporters would have to increase freight rates in line with the hike in diesel prices in order to maintain their current cash flow position; else their profitability is likely to be hit. CRISIL Research also believes that this diesel price hike further reduces the possibility of revival in commercial vehicle sales, which have been subdued due to slowdown in freight availability.

**Mumbai**

1061, Solitaire Corporate Park,
151, Andheri-Kurla Road, Andheri (E),
Mumbai - 400 093, India.
Phone +91 (22) 6758 8035/ 36
Fax +91 (22) 6758 8088

New Delhi

The Mira,
G-1 (FF), 1st Floor, Plot No. 1&2,
Ishwar Nagar, Near Okhla Crossing,
New Delhi -110 065, India.
Phone +91 (11) 4250 5100, 2693 0117-21
Fax +91 (11) 2684 2212/ 13

E-mail: research@crisil.com

Bengaluru

W-101, Sunrise Chambers,
22, Ulsoor Road,
Bengaluru - 560 042, India.
Phone +91 (80) 4117 0622
Fax +91 (80) 2559 4801

Kolkata

'Horizon', Block 'B', 4th floor,
57 Chowringhee Road,
Kolkata - 700 071, India.
Phone +91 (33) 2283 0595
Fax +91 (33) 2283 0597

www.crisil.com