Competition Reforms in the India: Exploring Options in Bus Transport

Policy Options Note

CREW Project

CUTS International

NATHAN

Competition Regulation and Law in India

In the mid-1950s, India adopted a policy of industrialization within a highly regulated economic structure, focusing on import substitution, heavy industries, a central role for the public sector, and price controls. The lack of competition resulted in an inefficient industrial structure with price and quality not being at par with international standards. This eventually led to the economic crisis of the early 1990s, after which reforms were introduced with a focus on liberalisation, privatisation, and globalisation. In 1969, India enacted the Monopolies and Restrictive Trade Practices (MRTP) Act, which prevented concentration of economic power, controlled monopolies, and prohibited monopolistic and restrictive trade practices. Thereafter, the MRTP Act was replaced with the Competition Act in 2002, which focused on prohibition of anti-competitive agreements and abuse of dominant position, regulation of combinations and promotion of competition advocacy. Further, India also has a draft National Competition Policy in place which is likely to be implemented soon. In addition to these regulations that relate to competition across sectors, there are also sector and state specific regulations with respect to bus transport and staple food (wheat) that influence competition in these markets.

Bus Transport in India

Of the various modes of transport, road transport is of utmost importance in India, especially given its significance to the poor and its reach throughout the country. The transport sector contributed 6.5 percent to India's GDP in 2011-12, with road transport comprising 74 percent of this (4.8 percent of GDP), followed by railways (1 percent of GDP).

This study addresses competition aspects of both inter-city and intra-city routes each in the states of **Gujarat** and **Madhya Pradesh**. These states were selected based on the demand for inter-city and intra-city travel, the growing economy in the states, the state of infrastructural facilities, the availability of substitute modes of transport, and contrasting policies.

Regulatory Evolution of the Bus Transport Market

The two key central laws governing the transport sector in India are the Road Transport Corporations (RTC) Act, 1950 and the Motor Vehicles (MV) Act, 1988. States enjoy considerable discretion in the transport sector, leading to wide variations in the bus transport market across the states. For instance, in 2005, the share of private buses was 7 percent in Maharashtra as compared to 97 percent in Orissa and 85 percent in West Bengal.

The MV Act also makes a strong distinction between two types of bus passenger transport segments – (i) Stage carriage - motor vehicles available for hire at separate fares paid by or for individual passengers either for the whole journey or for stage of the journey and (ii) Contract carriage - motor vehicles engaged as a whole under a contract for carrying passengers. A contract carriage permit holder cannot stop during the journey to pick up or set down passengers not included in the contract.

The scope of private participation and competition in the market can be restricted as a result of the above legislations permitting state governments to establish State Road Transport Undertakings (SRTU) to offer bus transport services, and to nationalize road transport services. This can be observed in the case of Gujarat, where the state has taken advantage of the power vested to states under the MV Act and has reserved the stage carriage routes for SRTUs. Both inter-city (stage carriage) and intra-city routes have been nationalized, creating a public monopoly for bus transport services.

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Despite performing well in the initial period, SRTUs have become inefficient (with deteriorating financial health, slowdown in fleet expansion despite a rise in demand, and increasing subsidies) due to factors including operational inefficiencies and political interference. Thus, in the early 1990s, although there was no regulatory change, private participation was encouraged in the market, resulting in the share of private buses in India increasing from 55% in the early 1990s to 92% by 2012.

Competition amongst Bus Operators (or lack of it) and its Impact

The Gujarat State Road Transport Corporation (GSRTC) enjoys a monopoly over the inter-city stage carriage segment in Gujarat, while the Ahmedabad Municipal Transport Corporation (AMTS) enjoys a monopoly over the intra-city bus transport systems in Ahmedabad. The lack of competition due to the legal barrier to entry due to State discretion as well as the assured availability of budgetary support irrespective of performance has resulted in inefficient performance by these undertakings, respectively. This is reflected in the ₹3 billion and ₹1.7 billion revenue deficit of GSRTC and AMTS respectively, in 2012-13.

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In contrast to Gujarat, Madhya Pradesh, recognizing the inefficiencies of the SRTU, abolished the Madhya Pradesh State Road Transport Corporation (MPSRTC) in 2005. Before its abolishment, MPSRTC's fleet fell from 36,000 buses in the early 1990s to only 1,800 buses in 2000, while its staff remained disproportionately high at 13,000. In 2005 at the time of its abolishment, MPSTRC had a fleet of around 1,500 (of which only an average of 1,000 were on road) and 11,500 employee – implying more than 11 staff per operational bus. Its operation inefficiency is highlighted by its monthly losses of ₹50 million and accumulated salary backlog alone of ₹450 million. . In the inter-city bus transport market, the monopoly of MPSRTC was removed and private players were allowed to enter and compete in the market. For intracity markets, Special Purpose Vehicles in the cities of MP were established. Like for the city of Bhopal, Bhopal City Link Limited (BCLL), under the Bhopal Municipal Corporation, was set up as the public regulator in charge of operational decisions including fares, routes, schedules, and selection of operator – resulting in limited private participations

Intra-city Bus Transport

As mentioned, AMTS has been given monopoly status in providing Ahmedabad's intra-city stage carriage bus transport services. Being a legal monopoly, there is no threat of new entry, or competitive rivalry; and with no other significant alternative mode of mass public transport, there is no threat of substitution.

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Despite this, AMTS is unable to sustain itself and cater to the demand for bus transport in the city due to its limited fleet size and maintenance capabilities, which has resulted in the indirect entry of private bus operators. As of 2014, 170 AMTS buses were leased out for operation and maintenance and 210 private buses were hired by AMTS from private operators on an own-operate-maintain basis. These private buses are operated as AMTS buses (as per AMTS specified schedules and routes) in return for a fixed fee per kilometre. The private operators receive assured revenue and have no incentive to innovate or provide better service than others since they cannot use their brand name, and operate strictly under AMTS. Thus, all the inefficiencies of the public monopoly are retained and the operational cost efficiency of the private operators is lost to AMTS. AMTS's inefficiency is highlighted by the fact that fleet utilization decreased from 78 to 67 percent from March 2010 to March 2013 despite the overall fleet size increasing from 966 to 1120 buses over the same period. Cost overruns are creating a widening gap between costs and revenue (see below).

In Bhopal, with BCLL in charge of operational decisions including fares, routes, schedules, and selection of operator has restricted the role of private players in the market. Private players who are selected through open bidding operate buses through contractual agreements with BCLL, and enjoy monopoly rights in their specific routes, implying there is no direct competition between the operators.

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The operational inefficiencies among public operators adversely affect the quality of buses, number of routes operated, and frequency of service offered, while the monopoly itself limits the alternatives available to consumers. Private operators do not have a role in operational decision-making in either of the cities (Ahmedabad or Bhopal) such as route determination, bus schedule, frequency, type of service, or fare setting, which makes these decisions subject to bureaucratic inertia and political interference. In Bhopal, two private players operate the routes, but they only bid on routes every 8 years and there is still no direct competition between the operators.

The results of a perception survey carried out under CREW project indicate that greater private entry alone may not be sufficient for attaining higher consumer welfare unless factors such as spread of the network, frequency of service, timeliness of operation, etc. are also improved. This survey found that commuters in Ahmedabad were more satisfied than Bhopal, as indicated in Figure 2 below.

Figure 1: Annual Cost and Revenue of AMTS: 2002-03 to 2012-13

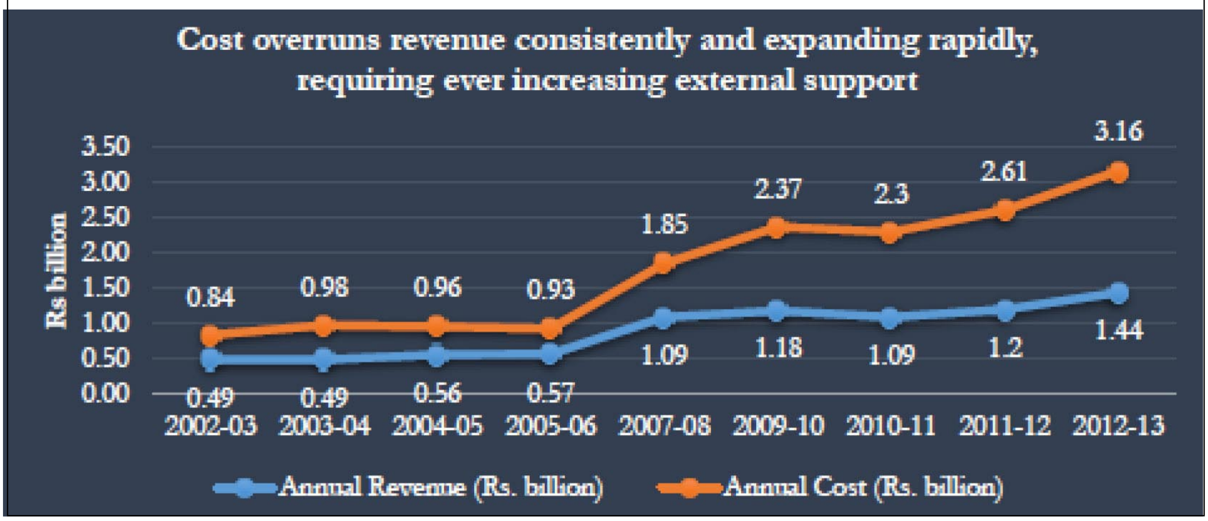

Figure 2: Access, Availability and Timeliness of Buses According to the Perception Survey

	Ahmadabad	Bhopal
Bus stop within 15 minutes walk	87%	52%
Time between buses less than 5 minutes	34%	17%
Time between buses - 6 to 15 minutes	51%	38%
Adherence to the time-table	45%	32%

Inter-city Bus Transport

In Gujarat, when GSRTC was formed in 1960, it competed with private operators. However, in 1994 Gujarat reserved inter-city stage carriage services for GSRTC (state owned unit), only permitting private operators to operate as contract carriages. Despite an initial good performance, GSRTC has run into operational losses and reduction in its fleet size. The fleet size declined over the years from around 7,800 buses in March 2003 to 6,700 buses in March 2013, and correspondingly, the passengers carried also declined from 1.27 billion to 0.84 billion (average annual passengers carried per bus also fell from 162,821 to 125,373). On the other hand, demand had been rising, creating a widening demand and supply gap. Consequently, to fill this need, private contract carriage operators started plying the inter-city routes 'illegally' as *de facto* stage carriages. According to the perception survey, there is considerable acceptance of private operators among passengers. Only a marginal proportion of respondents (ranging from 2 to 18 percent) rate the service of the public operator across different parameters to be significantly better than private competition. Moreover, two-thirds of the passengers are indifferent between private and public services even though 57 percent are aware that the private companies operate illegally.

In Madhya Pradesh, the market was liberalized with the abolishment of the MPSRTC in 2005. Operators have the freedom to choose their type of permit, with no restriction on the number of permits or fleet size available for private players, although fares are still regulated. The mode of registering a route of choice follows a formal procedure depending on the number of buses already plying on that route and the time of the scheduled bus. Though this is a positive process, most private operators apply for profitable routes and manage to get a permit despite many operators already servicing those routes. The promotion of entry by private players into the market has resulted in increased presence of private players in the market, - none of them however enjoy any significant market power. It is estimated that around 200 private operators are registered to ply intercity from Bhopal alone, with fleet size ranging from a single bus to up to 20-25 buses. However, these reforms have not necessarily led to improvements in passenger welfare. 59 percent of the surveyed respondents had to walk more than 15 minutes to reach the nearest inter-city bus network. These accessibility issues arise due to uncertainty in availability of buses. Interactions with local stakeholders in MP suggested that operators regularly ply on routes not allocated to them (practice of picking profitable routes even when an operator does not hold permit). Additionally, the infrastructural support from the government is limiting, thus raising the operational costs for operators, impacting important aspects of service delivery like safety. Only about 16 – 20 percent of commuters found the intercity bus service in MP to be safe.

Gujarat and Madhya Pradesh present two contrasting pictures highlighting greater open private participation and competition introduced in the MP inter-city market by abolishing the SRTUs. However, the benefits of competition cannot be realized by liberalisation alone – the government needs to create the enabling environment by providing the required infrastructure and regulatory oversight in the market. There are issues related to accessibility and availability of buses for commuters especially on non-profitable routes. Adherence to schedule is poor with instances of bus trips being cancelled or reschedules due to non-availability of passengers in the respective trip have been reported. This is where the presence of an SRTU in Gujarat (GSRTC) may have its benefit as the government is more motivated than the private sector to service less popular or profitable routes. But the public transport system in Gujarat is not able to meet the demand by itself or turn a profit, indicating the need for private sector participation. In fact, the private sector is operating—though illegally—without regulated fares or set schedules. The state needs to abolish its public sector monopoly and find a way to legally incorporate these private sector operators into the market while balancing the need for good regulations to ensure that consumers in all areas are still served.

Potential for Reform

Both states have much potential for reforms that can promote competition and increase welfare in the bus transport market. A key finding in both states is that weak regulatory systems are diminishing consumer and producer welfare, and that the presence of government as a monitoring and evaluation authority is imperative for ensuring sustainability and a level playing field. The draft Road Transport and Safety Bill, 2014 also proposes the development of such an authority in the states that can act as a regulator in the transport sector. Public Private Partnership (through a process of competitive public procurement) may be a promising approach for introducing private competition in the bus transport sector, especially to ensure that private sector providers are easily able to attach their fleet to government operated services.

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About the CREW Project

The Competition Reforms in Key Markets for Enhancing Social and Economic Benefits in Developing Countries project ("CREW") is being implemented over three years in four countries (India, Ghana, the Philippines and Zambia) to develop an approach for assessing the impacts of competition enhancing (or reducing) reforms on consumers and producers in two selected markets (staple food and bus transport). Supported by DFID (UK), BMZ (Germany) and facilitated by GIZ (Germany), CREW aims to demonstrate to policymakers and development partners the impacts of competitive markets on consumers and producers to garner greater attention and support to this issue and motivate the allocation of resources for implementing competition reforms in developing countries. For more information see www.cuts-ccier.org/CREW.

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Policy Options Note

Competition Reforms in the India: Exploring Options in Wheat

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Procurement should be opened up to the private sector and reforms should be undertaken to reduce the distortionary effects of the MSP and buffer stock

Wheat Market in India

Wheat was chosen as the staple food in India due to its widespread cultivation and popularity in the Indian diet. As a result of lifestyle changes, it has become the preferred staple in much of India. Given India's size, the project focuses on two top-producing states with varying market characteristics and agricultural policies – **Bihar** and **Rajasthan**.

In the wheat supply chain in India, there are 5 nodes: production; agricultural marketing of the produce; procurement; warehousing; and distribution to the retail consumer. There are 9 intermediaries involved in the wheat supply chain in India, and has significant impact on the price mark-up from the farmer to the end consumer. Although the project analyzed reforms in all the nodes of wheat supply chain, in this note, we discuss the state-specific reforms and their impact in the following key areas:

- Seed sector
- Agricultural marketing
- Procurement

Seed Sector

At the national level, liberalization since the mid-1980s has largely abolished entry barriers and has facilitated vibrant private participation in the seed sector. Nationally, the private sector is estimated to account for 80% of seed sector. However, agriculture is jointly governed by the central and state governments, and so the benefits of policy liberalization at the national level vary considerably across states due to differences in state-level policies as well as administrative efficiency.

Before 2008, the amount of certified/quality seed distributed in Bihar on subsidy was low (only 6200 quintals) as was the seed replacement rate (the percentage of area sown out of total area of crop planted in a particular season using certified/quality seeds) at only 11 percent. This was because the requisite amount of quality seeds was not available from the State Seed Corporation and the Bihar Rajya Beej Nigam (BRBN) was not participating in the central sector scheme for strengthening seed infrastructure. There was only one private sector seed company in Bihar. In 2006, reforms were undertaken to strengthen the BRBN and enhance the seed production capacity of the farmers. The reforms were supplemented by the implementation of the Bihar Agricultural Road Map (BARM) 2008-12, which involved various reforms including subsidized seeds, training of farmers, and increase private participation in the seed market.

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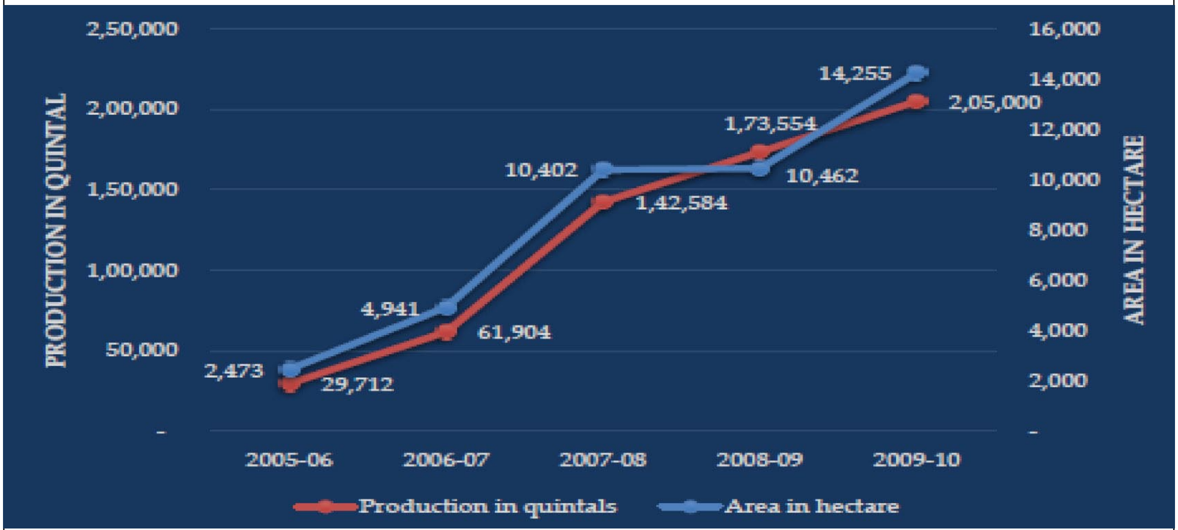
The BARM set a 35% seed replacement rate target for wheat and encouraged seed production and marketing by private players. The following changes were observed in the seed market after BARM (however given the various simultaneous schemes in this market and the lack of information we could not ascertain whether these changes are a result of increased private participation or other schemes):

- The number of private players in Bihar increased from 1 in 2006 to over 10 in 2013
- Seed production increased seven fold between 2005-06 and 2009-10
- Yield of wheat increased from 18-20 quintal/hectare in 2008 to 38-40 quintal/ hectare in 2013
- Most respondents of the survey undertaken for this project noted an improvement in access, reliability of supply and purchase, quality, and affordability of seeds.

Figure 3: Seed Production in Bihar: 2005-06 to 2009-10



Source: Department of Agriculture, Government of Bihar

In contrast to Bihar, in Rajasthan, the state of the seed market has not changed significantly - the seed replacement rate was similar in 2008-09 and 2011-12. While Rajasthan also attempted reforms in the sector and set targets on seed production and seed replacement rates, the Rajasthan Seed Plan did not have a holistic approach as followed by Bihar and lacked proper direction and resources. With Rajasthan being fairly self-sufficient in seed production and large number of private players already present in the market, the Rajasthan Seed Plan had set a higher target of a 50% seed replacement rate by 2011-12. However, in the absence of micro level planning, the target remained unmet and SRR in Rajasthan actually fell from 33% in 2008-09 to 30% in 2011-12.

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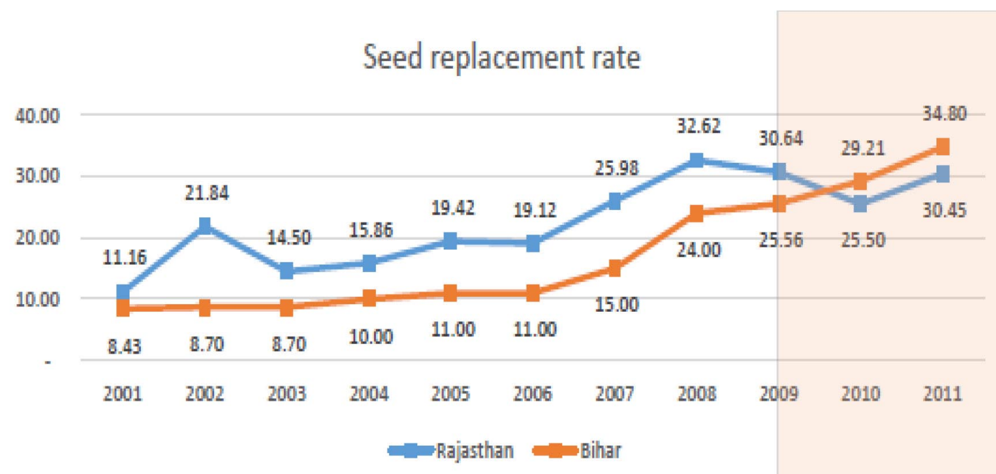
The figure below compares the seed replacement rate in the two states. Bihar overtook Rajasthan in seed replacement rate by 2010-11 from a 9 percentage point deficit in 2007-08.

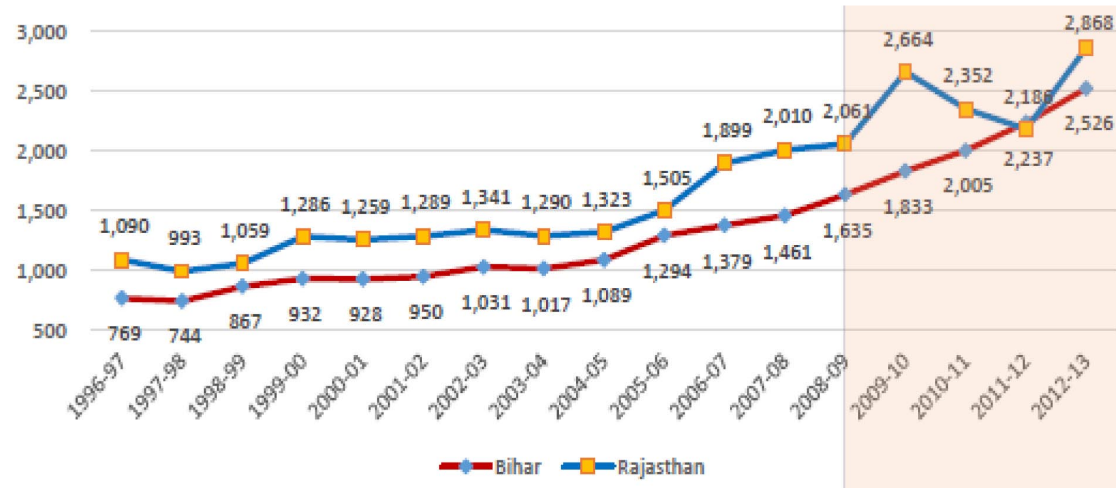
Despite Bihar's success in raising local seed production, expenditures on seed per hectare increased in both the states (see figure below). This indicates a continued local

Figure 4: Seed Replacement Rate in Bihar and Rajasthan: 2001 to 2011



Source: http://seednet.gov.in/Material/SRR-13.pdf

Figure 5: Expenditure on seed per hectare (in ₹)



Source: Commission for Agriculture Costs and Prices

demand-supply gap despite the recent improvement in the seed sector, especially considering the low base from which Bihar started.

Agricultural Marketing

Organized agriculture markets were introduced under the Agriculture Produce Market Committees (APMCs) in the 1970s with the objective of protecting farmers from exploitation by intermediaries and traders. However, instead of improving efficiency, the policy denied private investment, invited corruption, and artificially restricted the number of market players. Over time, these regulated markets degenerated into restrictive and monopolistic markets with high transaction costs.

Bihar completely repealed the APMC Act in 2006, which freed the market for private participation but with little success. However, due to the absence of government support in infrastructure development, private markets ('mandi',) contract farming or direct marketing has not increased significantly. Thus, the marketing setup has remained underdeveloped with limited private mandis and some proliferation of informal mandis. The market infrastructure created under APMC continues to operate, but with their operations now unregulated.

In Bihar, due to the absence of government support in infrastructure development, private markets ('mandis'), contract farming or direct marketing has not increased significantly

Notwithstanding some cost gains reported by farmers post abolishment of APMC (86% respondents in Saran district and 70% in Vaishali district stated that they benefited) particularly due to removal of the transaction cost - mandi fee, farmers continue to depend on local traders (and/or village assemblers) for sales and remain vulnerable to the price fluctuations.

In contrast to abolishment of APMC by Bihar, Rajasthan ushered in reforms in 2005 in line with the Model APMC Act to enable private engagement in developing agriculture markets, direct marketing and contract farming. However, despite the contrasting approach, Rajasthan also failed to see any noticeable ground-level progress. There is no operational farmer-consumer market in the state, only 2 licenses have been issued for private markets, only 1 license has been issued for trading in more than one market, and no registration for contract farming.

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The reason behind this was the absence of parallel policy reforms in related areas like public investment in infrastructure, credit policy, and land policy. Although 76 direct marketing licenses have been issued for direct sourcing from farmers by private entrepreneurs, the fine print in the rule books has limited any progress.

Thus, the experience of the two states show that reforms limited to the APMC Act allowing private entry will not automatically translate into private investment. Instead, there needs to be a harmonized, multi-pronged policy approach encompassing land, infrastructure, connectivity, administrative reform, credit, and investment in order to address the multi-faceted problem of agricultural marketing.

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Procurement

The Agricultural Pricing Policy (APP) emerged in India to address food scarcity on the one hand and to protect farmers from price fluctuations caused by bumper crops, international price movements as well as scrupulous practices by market players on the other. This led to the buffer stock maintenance norms and procurement at government initiative at Minimum Support price (MSP) for farmers. On the procedural side, procurement involves only public agencies, with the number of such agencies active in a particular region limited by government regulation. This limits farmers' options when selling to the government, who purchases 1/4 to 1/3 of total production. On the price side, MSP has a distortionary effect on market price discovery. Considering the volume of government purchases, the declared MSP considerably impacts the open market price discovery mechanism. Moreover, recent hikes in MSP have altered it into an instrument of subsidy from its originally designed function of acting as a price floor. Even this 'subsidy' is highly inefficient since the marginal and small farmers generate little marketable surplus and generally remain outside the outreach of the procurement network.

The MSP policy is also distortionary in its indirect impact on crop selection by farmers – the series of hikes under political patronage has generated a sense of assured profitability in sowing MSP covered crops.

Since 2013-14, the procurement of wheat from farmers in Bihar is being undertaken by Primary Agriculture Cooperative Societies (PACS). With a wide network of about 8,500 centres at the village panchayat level, this reform was expected to bring significant welfare gain for the wheat farmers. However, the move failed to have much impact due to inherent institutional failure in PACS like documentary requirements (such as land records), refusal to purchase citing low quality, and political influence. PACS have considerable potential to benefit small farmers – as they had been conceived as institutions 'of the farmers, for the farmers, by the farmers' – however, their effectiveness in benefitting ordinary farmers has diminished over time due to social and political undercurrents.

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Another issue with procurement in Bihar is that a state monopoly has been created (replacing 7 procurement agencies with just one) resulting in no/limited cross agency competition. According to the perception survey, only about 30 per cent of the farmers surveyed in Vaishali and Saran districts, on an average, opine that market access and price realization increased because of PACS – with about 75% of the marginal/small farmers not perceiving any such benefit from PACS.

Procurement in Rajasthan continues to be done through the APMC recognized markets ('mandi'), and as such the farmers remain exposed to the negativities associated with APMC system including licensing rules, infrastructural bottlenecks, intermediation cost, lack of market integration, refusal citing quality issues, delay in payment, etc. This affects farmers interested in selling to the government procurement agencies at MSP. Here again there is a public monopoly in government procurement at a price (MSP) that is not market determined.

Given the varying policy stance in the two states of the government across the wheat supply chain, the market environment in these states is also considerably different. However, a common observation from the two states is that the impact on competition and welfare is a joint culmination of the various policy measures and factors influencing their implementation including government actions and institutional factors. While strong state involvement in procurement activity to support food security or stabilize prices may not be abolished at the present stage of economic development, overall welfare may be enhanced by doing away with the public monopoly in procurement. The sector may be opened for private entry, allowing a larger number of procurement agencies to develop closer to the centres of production. Improved accessibility, with potential for better price realization, is likely to be considerably beneficial for marginal and small farmers. The buffer stock policy also should be reconsidered as the stock is sometimes double the stipulated minimum holding norm, which distorts the market.

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