

The global aviation market economics essay

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Arindam Mallik[1]Surbhi Arora[2]Abstract: India's start in the last fiscal 2012-2013 was promising, with commendable achievements like maintaining 6.5% GDP growth rate and reducing fiscal deficit to 4.8% of GDP. An unavoidable pillar of this rise is constituted by the Indian aviation sector contributing around 0.5% (www.indianexpress.com, 2013) towards its GDP. But, this sector is still underperforming as per its potential and given the remarkable demography. Out of its total number of airports, 32 (Hindustan Times, 2013) are still lying unutilized. Only around 3% of the Indian population currently avail air travel. 93% of the total air traffic is contributed by just two major airports in India. All these figures indicate a dearth in the management of aviation business in India. In spite of some vital amendments made by the government towards the late 2012 by extending the FDI (Foreign Direct Investment) limit up to 49% and allowing foreign carriers to invest in domestic airlines, some key areas for improvement still remains, being the constant hike in the price of ATF (Aircraft Turbine Fuel) that constitutes 30-40% of an airline's operating expenses. India is aiming to achieve the 3rd rank among the global aviation market by 2020. But, with such figurative hurdles as stated above and many more like a 346% (Tony Tyler, June, 2011) hike in airport charges at New Delhi airport for example, could the path chosen by India to achieve its goal considered feasible? This paper would be highlighting the areas that are the focal points to drive growth in the Indian aviation sector. It would be stating the changes brought about by the government and what can still be done to achieve India's desired objective to rank 3rd in the global market. Key words: GDP, fiscal, foreign direct investment, Aircraft turbine fuel, demography. IntroductionThe year 2012 has seen a range of ups and downs in the Indian aviation sector. <https://assignbuster.com/the-global-aviation-market-economics-essay/>

In contrast to the 3.9% growth in the global aviation market, Indian domestic sector has contracted at the rate of 9% since February, 2012 (Times of India, 2013). But, if the overall trend is studied holistically, it has shown a positive inclination. Several changes have been noticed ranging from deregulation of FDI (Foreign Direct Investment), amendment of civil aviation policies, enhancement of safety and security issues, modifications in the MRO (Maintenance Repair and Overhaul) segment as per import of spare parts in the current budget and so on. All this occurred with the disheartening backdrop of the shutdown of Kingfisher airlines. Let us identify some of the key areas where the Indian aviation industry has dwelled in the last fiscal 2012-2013. Towards the end, the analysis would be highlighting some of the major scopes for improvement.

Analysis of impediments FDI (Foreign Direct Investment)

Before allowing FDI up to 49% in the domestic airlines sector, critical assessment has been made by the ministry on several angles. Earlier, such foreign investment benchmark has been laid with similar limits, but only, from foreign companies who were not into airline/aviation business. But now the debate was about full freedom of investment up to 49%. This was being considered because the majority of the Indian carriers were sinking into debts except IndiGo. Only further cash infusion seemed the solution to catalyze a turnaround. But, allowing FDI also meant risking ownership, extending bilateral and reciprocal agreements and liberalizing commercial security norms. So it required an accurate forecasted approach. Eventually in September, 2012 we noticed the government allowing FDI, even from foreign carriers, up to 49%. This had been opposed by a member of the UPA (United Progressive Alliance) government, from Mamata Banerjee (CM of West Bengal), following which she withdrew her

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alliance from UPA. I have a partially positive opinion about this. It could have been taken at a later stage after certain modified restructuring had been made in the civil aviation policy as the loop holes are still causing hurdles in implementing the required benefits. One of such could be seen in the case of the South Asian budget carrier, Air Asia. The FIPB (Foreign Investment Promotion Board) is unable to give it clearance because its Indian partners Tata sons and Telestra, are currently not operating any airline in India. ATF (Aircraft Turbine Fuel) Surging ATF prices have by far been the major hurdle faced by the domestic carriers in curtailing their operating costs that comprises of 30-40%. In India the taxes on ATF are much higher than their global counterparts. This factor in itself is a big drawback surmounting the debts. Over the past few years ATF prices have compounded immensely owing to a weakening rupee against the USD. After the import-parity add-ons from the refiners, the carriers have to pay 30% state taxes varying from state to state. India has allowed direct import of ATF that could bring down the tax burden down to a flat 4%, but due to the lack of infrastructure to facilitate storage is withholding the carriers to take this advantage. Currently the storage mechanisms are owned by refineries like BPCL, HPCL, IOCL, RIL, etc. for a 15 days delivery basis which is in talks to be increased to a month's stretch for crude. Unavailability of such facilities at the airports, would make the strategy to directly import fuel instead of manufacturing, useless. The airlines are not even implementing defense mechanisms like fuel hedging to safeguard themselves from fluctuating foreign exchange prices. In order to utilize this opportunity it's important to declare airports with an infrastructure status. In the 12th five year plan (2012-2017), Rs. 1 trillion has been allocated to infrastructure development, in which aviation <https://assignbuster.com/the-global-aviation-market-economics-essay/>

sector comprises of a mere 0.5%. This share should be increased in proportion as the aviation sector contributes 1.5% towards GDP (www.iata.org, 2013). Even in the recent budget the overburdened price of ATF has been ignored, though some amendment has been made after that. A joint venture between Air India and the OMCs (Oil Manufacturing Company) has curtailed the prices by 10% followed by a price cut by 5%. Management Concerns This is a vital role to be played by the top brass of the airline companies which requires immense capability of decision making. The context can be explained through the sufferings of Kingfisher that had caused their shutdown. Unpaid salaries of employees have been one of the lingering concerns for the carrier. It had been in the news for a long time that the management failed to keep their word in spite of repeated promises. The resulting factors have been misallocation of resources. Kingfisher had set a benchmark in glamorous aviation from the time they acquired Air Deccan in 2003-2004. In order to maintain this image they had to incur several extra costs. We also saw Kingfisher starting their low-cost wing Kingfisher Red to recapture their market share. But they lacked in establishing an efficient low cost model. Neither were they able to identify their loopholes and at a time when all the airline companies were running to grab the low cost model, we see Kingfisher withdrawing Kingfisher Red. Many other failures to take feasible decisions led to frequent strikes by employees. Eventually, its license got suspended in October 2012 followed by cancellation by DGCA (Directorate General of Civil Aviation) on 31st December, 2012. Regulatory framework Along with mismanagement, the shutdown of Kingfisher was even caused due to over ambition and unplanned fleet acquisition. These factors operated under an infeasible policy framework. Soaring ATF prices and the <https://assignbuster.com/the-global-aviation-market-economics-essay/>

falling value of rupee also played an important role. Due to surmounting debts the lessors wanted to cease the aircrafts from the operating carrier, but AAI (Airport Authority of India) didn't allow them to do so. This had two fold reasons. Withdrawal of the aircrafts would have resulted in reduced seat capacity in the market leading to inflated airfares through discriminatory pricing strategy. Secondly, it highlights the gaps in government policies. The current policy involves a tedious and cumbersome documentation system, due to which in spite of having the right the lessors found it difficult to reclaim their fleet. Another dimension to this issue is that the carrier accumulated huge losses when it was grounded for prolonged period. So AAI cling on to the fleet in order to secure their grounds for claiming their landing and parking charges. Human Resource problem Likewise Kingfisher, Air India faced some major constraints in their HR management except it enjoying the status of being a national carrier, repeatedly funded by public money. Strikes occurred over disputes between the pilots of its two distinct wings, Air India and Indian Airlines, over modification of its pay structure. The Air India pilots opposed to be paid under the same pay scale as Indian Airlines as they considered themselves employed under the international pay structure. Unrest even occurred when the aviation ministry wanted to re-evaluate their FDTL (Flight Duty Time Limitations) as per ICAO (International Civil Aviation Organization) standards. Strikes made the carrier, already overburdened with debt further bleed for money. An airline only earns money when it flies. These strikes not only catalyzed the losses but also disrupted the brand image of Air India and Kingfisher. Recent Highlights Price wars Of late domestic airlines are seen competing over airfares. Spice jet initiated the offer by offering 2 lakh seats at Rs. 2013 this year around <https://assignbuster.com/the-global-aviation-market-economics-essay/>

February. It was followed by similar endeavors by Jet Airways and Air India. The point is such practices cannot derive long term benefits. Instead of competing over price only, the carriers should have innovation in their service through product differentiation. Nevertheless Air India's current efforts are commendable. Just like advertising spaces at the airports are a major source of non-aeronautical revenue, similar strategies would now be applied to aircrafts as well. They might sell the hull space of the aircraft's tail, in-flight bins, pillow, seat covers and even allow consumer durables. Similar way outs can be designated to diversify the dependence precisely on aeronautical revenues. Boeing's Dreamliner

In order to curtail fuel consumption, the carriers are including various fuel efficient aircrafts in their fleet. Such incursions have been even implemented by our national carrier. These Boeing 787s are regarded to be 20% fuel efficient and can travel 16000 kilometers nonstop with a full tank (The Economic Times, 2012) with the latest contemporary state of the art in flight services and designs in the industry. But, the delivery of these machines was delayed by 3 years. It even faced some technical glitches when fire broke out in the cockpit due to overheating of the battery cells.

Budget 2013 Expectations were high regarding this fiscal budget 2013. But the results were disheartening. Ever increasing ATF prices and airport charges needed an immediate addressing. But the finance ministry haven't paid heeds to the issues commendably. In spite of contributing over 1.5% towards the national GDP, the aviation sector is still viewed as a mere tax creator and not an economic generator. Some amendments that took place are fuel surcharge hiked from 5% to 10%, income tax limit raised to Rs. 2 lakhs, amendment of U/S 29 of Custom Act 1962, amendments in baggage rules and basic custom duty exemption on <https://assignbuster.com/the-global-aviation-market-economics-essay/>

aircraft parts and maintenance equipment. Trends for the future Customer Relationship Management (CRM) Due to immense competition in the current business market the implementation of CRM is an ultimate necessity to culture product differentiation. Otherwise we have seen that due to lack of differentiated services in a highly competitive market, most of the carriers are engaging in price war which is nothing but disruptive. Aviation being a customer centric industry, CRM would enable the airlines to catalyze customer loyalty. This would initiate long term viability of the respective companies. Many of the airline companies have lost track of the true needs of the passengers and are sticking to the outdated view of what airline services are all about. The application of CRM is a long term investment with lifelong benefits. It comprises acquisition and deployment of knowledge about customers to enable the airlines to sell their product and services efficiently. (Pawar, 2012) Gagan GAGAN is a satellite based navigation system which is a part of Global Positioning System (GPS). Implementation of GAGAN would provide augmentation service for GPS over India, Bay of Bengal, South East Asia, and Middle East extending up to Africa. It will be compatible with other System Based Augmentation Systems (SBAS) like the Wide Area Augmentation System (WAAS) of USA, the European Geostationary Navigation Overlay Service (EGNOS) of the European Union and the Multi-functional Satellite Augmentation System (MSAS) of Japan. It will bridge the gap between EGNOS and MSAS, providing seamless air navigation service across regional boundaries. GAGAN would result in improved efficiency, direct routes, increased fuel saving, approach with vertical guidance at all runways, significant savings due to removal of ground aids, reduced workload of flight crew and air traffic controllers, improved airspace capacity

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due to reduced aircraft separation, reduce the risk of controlled flight into terrain, enhanced Air-to-Air surveillance, availability of minimum safe altitude warning and reduce noise pollution. (India)

Conclusion

India can achieve 9-10% annual GDP only if the populous states like Bihar and Uttar Pradesh start performing strongly. Orissa is another state which has huge untapped economic potential. But, for this to happen they would require to enhance their air capacity. Despite having 25% of India's population residing in Bihar and Uttar Pradesh, their airports accounted for only 2% of air traffic in the last fiscal year 2011-2012. Kanpur, India's largest city in the largest state, with a population of 3 million, has limited air connectivity and is being served by not more than two departures per day, for regional aircrafts. Thus, we have encountered a number of areas through this paper that would help us to introspect through the nerve of the aviation industry. Though the current picture does not coincide with our optimistic outlook towards the sector due to the accumulated debt crisis, there is enough potential in the domestic aviation sector to make a turnaround.