

Jet Set Stop: RSTV – The Big Picture

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Larger Background:

- After flying for 25 years, Jet Airways on recently announced temporary grounding of operations after the lenders declined a 400-crore rupees lifeline, putting at stake around 20,000 jobs and thousands of crores in passenger refunds, dues to vendors and over 8,500 crore rupees to banks.
- Founded by Naresh Goyal, the full-service carrier served tens of millions of passengers for over two-and-half decades, before becoming the seventh domestic carrier to shutter operations in the past five years. However, the once-premier airline flew into deeper turbulence-second in its history after the 2010 crisis– after four back-to-back quarterly losses, leaving it gasping for financial breath and forcing it to default on payments to nearly all—from banks to lessors, to employees, and eventually leading to the shutdown.
- On this edition of the big picture we will analyse Jet's fall from grace and the implications for the aviation sector.

Analysis by the Experts:

How would you look at the Jet Airlines' fall from grace?

Ajay Dua, Former Secretary, Ministry of Commerce & Industry, weighed in with his arguments here.

This was something which was not unexpected, but that is only if you look at what had been happening for the last one year. However, around two years ago if someone had asked us the same question, one would have answered that the airline is going great and going from strength to strength. As a matter of fact, Jet Airways was operating in a market where the passenger traffic is growing in double digits CAGR for the last 7-8 years. Jet Airways had a huge fleet of its own; at its peak, it had around 124 aircrafts. Jet Airways also had international routes, and many well-paying routes within India, operating 600 flights a day. Thus, everything was going very well for the airline. However, there were considerable amount of illnesses within the airline. From what was apparent and coming out, it appeared to be a very rosy picture. The Government ultimately is the protector of the consumers, and at the end of the day, there are many entities at fault- for example, the airline, the lenders, the regulator and the Government.

Where did it all go wrong for the airline? Some analysts believe that post the acquisition of Air Sahara, Jet Airways has never really recovered. Other analysts say that it was the crisis later on. So, what is it really?

Dr. Sanat Kaul, Former Joint Secretary, Ministry of Civil Aviation, weighed in with his arguments here.

Well, if you look at it in a holistic way, the model of a full-service airline, and Jet Airways boasted of the best domestic full-service airline, is a model which was caught up by a disruptive business model of low-cost airlines. Now, low-cost airlines came 10-15 years back and they disrupted the whole market. The growth of double digits in Indian airline traffic, was due to the new model of low-cost airlines. Jet Airways was caught out and had to float its own low-cost airline (Jet Lite). In the domestic sector, people essentially

stopped buying business class tickets. Here, Jet Airways as a leader in the aviation industry suddenly found itself in the wrong place. Further, there was a lot of protest by the shareholders that Mr. Naresh Goyal needs to step down. There are many questions that arise: What is a management fault on his side? Was he interfering in the management in a manner detrimental to the company's interests? These are some of the factors where I would say that things have gone wrong. However, surely, the new model of low-cost airlines, did make a major dent into the concept of a full-service airline. People prefer to travel domestically using low cost airlines.

Ajay Dua, Former Secretary, Ministry of Commerce & Industry, weighed in with his arguments here.

I believe that if we feel that budget airlines in India have a future is akin to not capturing the entire picture. One should go by evidence. Jet Airways did not experience a competition from airlines like Indigo, etc. right from the beginning. This is because its capacity utilization continued to remain quite high until recently. The fact that Jet Airways loaded itself with too many frills, such as lounges, etc. is also a contributing factor. However, there are crucially several other factors which have led to what we are currently seeing in Jet Airways. The biggest factor to my mind is the debt which Jet Airways had to incur because it went in for an expansion- by virtue of which it acquired aircrafts from outside. This was probably done in a far more liberal manner than what ought to have been done.

Is there no room for full-service airlines in the country? There are a couple of them still in the market at the moment. Secondly, what happens to the around 20,000 employees of Jet Airways?

A.K. Bhattacharya, Editorial Director, Business Standard, weighed in with his arguments here.

I am of the view that this thesis which espouses that it is because of the entry of the low-cost carriers that Jet Airways faced a problem, probably needs to be tested. This is because in India, although a carrier may be low-cost, but you are not charging a low fare. The concept of a low-cost carrier is not getting translated into a fare that is cheaper than what the full-service carriers are offering. That is, the difference is very marginal. So, the real issue is the way Jet Airways was mismanaged, and in particular in the past 1.5 years to 2 years. The writing was on the wall. My broad understanding of why the Jet story has taken an ugly turn is for three basic reasons:

1. Failure at the management level itself
We all knew that there was a failure in terms of the management of the airlines (as this was out in the public domain itself); A KPMG auditor had raised questions on its auditing practices.
2. There was a company called Jet Air Trade. This company was receiving a commission. One doesn't know for what? 76 Crores worth of commission was being given by Jet Airways, which had already begun incurring losses to this company. Its promoter, Mr. Naresh Goyal was a majority shareholder of this company. Why was Jet Airways paying a selling and distribution cost of 12-15% compared to other airlines which was paying a cost of 2-3%?
3. Therefore, the questions about the management's inability to handle the situation comes to my mind as the first failure. The second failure to my mind is the banker's failure. The lenders completely failed to understand that this company has failed to submit its accounts and repay the dues by December 2018.
4. Also, the lessons learnt by SBI from what it did with Kingfisher has not been learnt. SBI was attempting to bail Jet Airways out through a negotiated settlement. This is a fit case to be referred to the Insolvency and Bankruptcy Court.
5. The next failure is that of the DGCA (Director General of Civil Aviation). The DGCA should have acted in advance. The problem was written on the wall at least 6-8 months ago. Why wasn't Jet Airways stopped? The DGCA in my opinion has failed to protect the interest of the consumers. The top management and the independent directors of Jet Airways have failed to protect the shareholders.

What is likely to happen now especially when we consider that there are a few suitors for Jet

Airways?

Dr. Sanat Kaul, Former Joint Secretary, Ministry of Civil Aviation, weighed in with his arguments here.

Well, in my view, I don't see how anyone except a foreign airline would be interested in Jet Airways. If there is only Government pressure, then maybe SBI or Indian financial institutions might intervene. However, otherwise, it is not a case which is attractive at all. A foreign airline is allowed up to 49% equity in India. Further, an airline from the middle-east such as Etihad would certainly be attracted by that. This is because India has a very strong outbound traffic market for airlines. The future prospects of an airline owned by a foreign carrier which has a good hub would be attractive. However, no investor would be interested with the high costs of debt. There may be some other hidden costs also which may come about in terms of buying up the airline. The only party who would be interested is a foreign airline that has a good hub in their country to take Indian passengers out to their hub.

Jet Airways at the end of the day is a brand. Of course, that brand would have to be rebuilt now, but is anyone willing to take that risk?

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I believe that we are delaying the process of identifying a new buyer or a new investor. I believe that there would be a new investor. Jet Airways has a brand, and it still has a lot of bilateral routes on the international circuit. In the aviation industry these attributes carry a value. Further, Jet Airways has excesses at the airports. Thus, one must factor into the equation these other tangibles as well which should account for something. There are airport landing rights, there are access to routes, there is also the brand which Jet Airways carries. Plus, the airline still has a fleet of engineers to service the aircrafts; the airline also has pilots and a trained crew. What is needed now, and what the banks should have actually done, when they had found the signs last year (2018)- the first default actually had occurred in April 2018, after which the airline has only been going from bad to worse- the bankers should have got in then and should have insisted at that point of time, that Mr. Goyal would have to step down from the driving seat. Etihad was not willing to invest for a very simple reason in which they cited that Mr. Goyal could no longer continue as the chairman and his family could no longer continue to hold over 51% of the company. Even the Tata Group was at one time willing to invest in the company but hadn't gone ahead as Mr. Goyal was unwilling to step down. The Tata Group always had an urge to be in the Civil Aviation Industry, starting from the days of JRD Tata. Jet Airways is an airline with many more options than Vistara has. There is still time to revive Jet Airways. The longer the aircrafts remain grounded, the more difficult it would be to get them operational again. There would be a higher chance of employees walking away as well.

Can Jet Airways, although temporarily grounded for the time being, be turned around? And who would be in the best position to do that?

A.K. Bhattacharya , Editorial Director, Business Standard, weighed in with his arguments here.

Well, if SpiceJet could be turned around, by a man named Ajay Singh, then surely Jet Airways as well can be turned around many more times over. Let us not forget that Jet Airways is a first class airline. At a time when the Airline was running, it was probably the best private sector airline in the country. I believe that it has got a brand equity, which it can capitalize on- thus, I don't see, at least on paper, as to why the airline cannot be turned around or revived. However, ironically, the man who helped build this airline, is actually not wanted in the airline anymore. This is perhaps because of what I call, 'the promoters curse'.

When a promoter becomes too attached to his/her company, then problems arise. There are also all kinds of accusations and allegations that begin to go around.

Even in the case of Air India, there were initially no bidders. This was because, the bidders had raised

question marks on the Government of India being the largest shareholder. This was because they feared interference from the Government of India. Similarly, any serious bidder of Jet Airways would have a similar question about Mr. Goyal's interference if he continues to hold a 31% stake in the airline and remains as the Chairman of the airline. An assurance has to be given to the company that takes over. What I do know, is that for Jet Airways to be turned around, you need an airline and my sense is that the Tata Group is a good candidate. However, one needs to factor into the equation Mr. Ratan Tata's fraught relationship with Mr. Naresh Goyal- this was evident when the Tata's were about to enter into a major deal with Singapore International Airlines. The question is whether or not an assurance can be given to a potential bidder that the existing promoter would be hands-off, and that his shareholding would not be allowed to be translated into any kind of interference or intervention into the running of the company. Unless this is done in black and white, one wouldn't find a serious bidder and this company (Jet Airways) wouldn't be bailed out. What Jet Airways needs is a serious airline player which can come, take over and run things again.

Concluding Remarks:

- Currently, the slots and the routes that Jet Airways was operating are being allotted to other airlines temporarily. If Jet Airways is revived fast, then they would be able to retain it, otherwise, these slots would go. Thus, the airline is now working against time to resuscitate itself. Further, since India has a huge capacity for outbound traffic, the ideal investor would be a foreign airline. The Indian aviation sector is an attractive market for a foreign investor to enter into.
- Also, it is true that the Indian civil aviation industry is growing at double digit growth, however, in the last 5 years, we have had 7 airlines going under. However, having said this, we (India) shouldn't be too worried about consolidation. This doesn't mean that what is operating currently would get denuded, i.e. its capital gets denuded; its service gets denuded. etc.
- The fact of the matter is that our regulators have a responsibility. Merely, the DGCA working as a technical and an engineering agency, also has to look at the management of the airline. They have to look at the financials of the airlines. Also, being able to read and anticipate as to what is going on and be in a position where it can report to the Government.
- Another way forward is to make the DGCA truly independent. The DGCA should not be left as an appendage of the Ministry of Civil Aviation. The DGCA should be an independent autonomous regulator on paper as well as in practice.

