

BY: DR A. THILAGARAJ

AVIATION INDUSTRY: LOW-COST CARRIERS DRIVING THE GROWTH

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Legacy carriers are being forced to match LCC fares, in the times of escalating costs

India is one of the fastest growing aviation markets in the world. The Airport Authority of India (AAI) manages a total of 127 airports in the country, which include 13 international airports, seven custom airports, 80 domestic airports and 28 civil enclaves. There are over 450 airports and 1091 registered aircrafts in the country.

The genesis of civil aviation in India goes back to December 1912 when the first domestic air route

between Karachi and Delhi became operational. In the early fifties, all airlines operating in the country were merged into either Indian Airlines or Air India, and, by virtue of the Air Corporations Act 1953, this monopoly continued for the next 40 years. The Directorate General of Civil Aviation (DGCA) controlled every aspect of aviation, including granting flying licences to pilots, certifying aircrafts for flight and issuing all rules and procedures governing Indian airports and airspace.

Finally, the Airports Authority of India (AAI) was assigned the responsibility of managing all national and international airports and administering every aspect of air transport operation through the Air Traffic Control.

Challenges

The growth in the aviation sector and capacity expansion by carriers have posed challenges to the aviation industry on several fronts. These include shortage of workers and professionals, safety concerns, declining returns and the lack of accompanying capacity and infrastructure. Moreover, stiff competition and rising fuel costs are also negatively impacting the industry.

Employee shortage. There is a shortage of trained and skilled manpower in the aviation industry. As a consequence, there is cut-throat competition for hiring employees, which, in turn, is driving wages to unsustainable levels. Moreover, the industry is unable to retain talented employees.

Regional connectivity. One of the biggest challenges facing the aviation industry in India is to provide regional connectivity. The lack of airports is hampering regional connectivity.

Passengers' Status in Aviation

Year	International		Domestic		Total	
	Number in millions	Percentage growth	Number in millions	Percentage growth	Number in millions	Percentage growth
1999-2000	13.29	2.90	25.74	6.90	39.04	5.50
2000-01	14	5.40	28.01	8.80	42.02	7.70
2001-02	13.63	-2.70	26.36	-5.90	39.98	-4.90
2002-03	14.82	8.80	28.90	9.60	43.72	9.40
2003-04	16.65	12.30	32.04	10.09	48.69	11.40
2004-05	19.45	17.00	40.10	25.00	59.54	22.30
2005-06	22.36	15.10	50.98	27.90	73.34	23.70

Rising fuel prices. As fuel prices have climbed up, the inverse relationship between fuel prices and airline stock prices has been demonstrated. Moreover, the rising fuel prices have led to an increase in the air fares.

Declining yields. Low-cost carriers (LCCs) and other entrants together now command a market share of around 46 per cent. Legacy carriers are being forced to match LCC fares, in the times of escalating costs. Increasing growth prospects

have attracted and are likely to attract more players, which will lead to more competition. All this has resulted in lower returns for all operators.

Gaps in infrastructure. Airport and air traffic control (ATC) infrastructure is inadequate to support growth. While a start has been made to upgrade the infrastructure, the results will be visible only after two-three years.

Trunk routes. At present, trunk routes are not fully exploited. One of

the reasons for inability to realise the full potential of trunk routes is the lack of genuine competition. The entry of new players would ensure that air fares are brought to realistic levels, as it will lead to better cost and revenue management, increased productivity and better services. This, in turn, would stimulate demand and lead to growth.

High input costs. The input costs are also high. Some of the reasons for high input costs are withholding tax on interest repayments on foreign currency loans for aircraft acquisition and increasing manpower costs due to shortage of technical personnel.

Growth prospects

The Indian aviation industry has witnessed remarkable growth in recent years, with key drivers being positive economic factors, including high GDP growth, good industrial performance, and corporate profitability and expansion. Other factors

SWOT Analysis of the Aviation Industry

Strengths

- Growing tourism.** Due to growth in tourism, there has been an increase in the number of international and domestic passengers. Growth in the number of domestic passengers is estimated at 50 per cent per annum, while growth for international passengers is 25 per cent.
- Rising income levels.** The rise in disposable income is expected to increase the number of flyers.

Weaknesses

- Under-penetrated market.** The total passenger traffic was only 50 million as on Dec. 31, 2005, amounting to only 0.05 trip per annum compared to 2.02 trips per annum in developed nations like the United States.
- Untapped air cargo market.** The air cargo market has not been fully tapped in India and in the coming years, a large number of players are expected to have dedicated fleets.
- Infrastructural constraints.** Infrastructure development has not kept pace with growth in the aviation services sector. Huge investment is required for development of physical infrastructure for airports.

Opportunities

- Investments.** Huge investments are expected to take place in the aviation sector in the near future.
- Growth in market size.** Growth in the aviation sector is 25-30 per cent.

Threats

- Shortage of trained pilots.** There is a shortage of trained pilots, co-pilots and ground staff, which is severely limiting growth prospects.
- Shortage of airports.** There is a shortage of airport facilities, parking bays, air-traffic control facilities, and takeoff and landing slots.
- High prices.** Though a good enough number of low-cost carriers already operates in the industry, majority of the population still can't afford air fares.

include higher disposable incomes, growth in consumer spending and low fares. As of May 2006, private carriers accounted for around 75 per cent share of the domestic aviation market. During April-September 2006, the total aircraft movements witnessed an increase of 29.6 per cent year on year to 494.92 thousand aircraft movements, compared to 318.89 thousand during April-September 2005. The total air passenger traffic in September 2006 showed an increase of 31.1 per cent, compared to 2005.

The Centre for Asia Pacific Aviation (CAPA) had predicted that the domestic traffic would grow at 25 per cent to 30 per cent a year until 2010 and international traffic would grow by 15 per cent, taking the overall market to more than 100 million passengers by the end of the decade. Indian carriers have 480 aircrafts on order for delivery by 2012, which compares with a fleet size of 310 air-

Recent Developments

1. Modernisation of airports
2. Policy on merchant airports
3. Growth in MRO segment
4. Airport security policy
5. Augmentation of fleet by various airlines
6. Foreign equity participation in air transport services

crafts operating in the country today.

Top players

The players in the Indian aviation industry can be categorised into three groups: public, private and startup. Public players include Air India, Indian Airlines and Alliance Air. Private players include Jet Airways, Air Sahara, Paramount airways, Go Air Airlines, Kingfisher Airlines, Spice Jet, Air Deccan and many more. Startup players are those which are planning to enter

the markets. Some of them are Omega Air, Magic Air, Premier Star Air and MDLR Airlines.

Future scenario

Indian airports are handling between 90 and 100 million passengers per year. Nearly 80 per cent of this growth is driven by LCCs.

According to the Ministry of Civil Aviation, India will need 1500 to 2000 passenger planes in the next ten years. Over 135 aircrafts have already been added in the last two years alone. India's fleet strength is estimated at 500-550. The domestic market size is estimated to have crossed 60 million, with international traffic of 20 million. By 2020, Indian airports are estimated to handle 100 million passengers, including 60 million domestic passengers. ■

The author is a lecturer in Department of Commerce, Sri S.R.N.M. College, Sattur

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