Bumpy roads in the sky

By Grace Segran

Rapid economic growth and an increasing demand for travel should make it easy to make money in the airline business in India. But it's not. One private company explains how it's navigating through the clouds.

The paradox of India's airline sector is that it serves one of the world's fastest growing economies and is posting double-digit traffic growth, yet CAPA (Centre for Asia Pacific Aviation) estimates Indian carriers combined will lose over US$2 billion in the 12 months ending March 2012. Cut-throat competition, rising fuel costs, tight regulations and the depreciation of the rupee are making it difficult to operate an airline profitably in India. So says Nikos Kardassis, CEO of Jet Airways.

"High fuel prices are affecting our bottom line. We recently had a 20 percent depreciation of the rupee which makes everything more expensive for the airline. The Indian oil companies are buying in US dollars and they pass the depreciation of the rupee into the pricing and onto the airlines. In addition, the purchasing of heavy equipment such as engines, and the cost of services such as aircraft maintenance and ground handling are priced in dollars. The depreciation has made it very expensive for us to operate profitably," Kardassis told INSEAD Knowledge at his office in Mumbai recently. "We are also facing stiff competition from other airlines; there is a price war which started last year," he added. "We are operating at yields which are lower than 2007 and 2008."

If anyone can ride through these turbulent times, it's Kardassis. The man has over 25 years' service in aviation and financial services, beginning his aviation career with TWA, where he held various finance and operational positions. He became the first CEO of Jet Airways when it was founded by Naresh Goyal in 1993. In 1999, Kardassis left India's largest privatised airline to pursue a career at Merrill Lynch as managing director and head of business development and distribution for the Global Bank Group. He returned to Jet Airways in 2008 as senior advisor to the chairman for corporate strategy and finance when the company was in the midst of a massive global expansion, and was appointed CEO in 2009. This background gives him a perspective from which to assess what can be done to further the prospects of the airline industry in India.

Should the government do more?

Kardassis says that high aviation taxes, a lack of capacity (out of Mumbai airport, for example), and increasing infrastructure costs in metro cities such as Delhi are some of the things that are holding back the industry's potential to thrive. "What India needs is a policy framework that supports the industry's competitiveness. We need to remove negative frameworks such as excessive taxation on aviation fuel and regulatory barriers to efficient operations such as the right of first refusal which the flag carrier enjoys on applications for traffic rights between India and other countries."

Tony Tyler, the International Air Transport Association's (IATA) Director General and CEO, agrees, adding that Indian aviation has tremendous potential to drive economic growth in the sub-continent. But to realise this, India needs a common vision for aviation – "expressed in a National Aviation Policy strongly linked to an implementation plan. Such a policy would need to re-build competitiveness by addressing the difficult issues of tax, cost, investment and infrastructure." Tyler was speaking at the India Aviation 2012 conference held on 15 March 2012. He added that India should not settle for a bronze medal in the world of aviation. "It has pure gold potential."

Keeping costs under control

While that potential is being realised, Jet Airways started taking steps beginning in August 2011 to reduce its expenses considerably. “We looked through various expense elements and found we could reduce costs by US$180 million a year. We have renegotiated some of our maintenance and engineering contracts, gave up 50 percent of the spaces that we are occupying at the airports in engineering, security, customer service, sales and ticket offices. We have stopped hiring new employees into the company and through attrition, we are reducing payroll. Essentially, we have frozen all other spending,” Kardassis says.

He was quick to caution that all of those steps are not going to make the airline profitable, and is considering other peripheral ways to raise revenue: charging the customer for issuance of paper tickets, implementing transaction fees at call centres and becoming more diligent about charging customers for excess baggage. In addition, they will selectively increase fares, for example, on business class seats between Mumbai and Delhi, to try to bring the yields up.

To reduce distribution costs, Jet Airways is looking to sell more tickets directly to the customer on the Internet by offering special fares, so that travellers will go directly to the airline rather than through travel agents. The airline’s target is to achieve 30-35 percent revenue from web sales, and it has increased spending on Google and other online portals. But Kardassis says in India, there is a preference to go to the travel agent.

Leading position

The domestic market in India is projected to grow from 50 million to 150 million passengers - a significant three-fold increase - over the next eight years, and Jet is present in the key segments of air travel. Kardassis, claims Jet Airways is the leading airline in the full-service segment in India and from the Jet Airways group, Jet Konnect and Jet Lite are the dominant players in the low-cost segment of the market. Kardassis wants to maintain their leading positions.

“We expect both (full-service and low-cost) segments to grow over the next eight years. There are going to be customers who want to pay for full service: they appreciate the newspapers, the meals, the sitting arrangements. Then there is the leisure market – the young people who don't care too much about the newspaper but care about the fare; we are going to cater to this market too," Kardassis says. "By introducing our low-cost products about three years ago, we have been able to increase our overall domestic market share from 20 percent to 30 percent. Currently, 25 percent of total revenue is from full-service and 75 percent is from the low-cost service."

The same growth is expected for the international market. Kardassis says Jet Airways' fleet in the next three to four years has to double if it is to maintain its leadership position.

Remaining optimistic

Despite slim returns today, Kardassis remains optimistic. "Look at Europe – it's zero growth in the aviation market. When it goes up by one to three percent, people get all excited. Here in India, the market grew by 18.4 percent in 2011 which is the best year ever for the aviation industry. The Indian Ministry of Civil Aviation's Vision 2020 statement envisages a compound annual growth rate of 15 percent in the next five years with investment opportunities of US$120 billion up to 2020. With CAPA and IATA calling for aviation reforms, I see a serious upturn in the future - and we are going to be there," he says.

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