

Predicting distress in Indian Aviation Industry: With reference to COVID-19

*** Dr. Nandita Mishra**

***Simrat Kaur**

ABSTRACT

Due to the major failures and bankruptcies, predicting financial distress set-out as a warning system which helps not only companies but also their creditors, investors, auditors and stock market regulators. Aviation market has already been facing a slowdown before COVID-19 hit the country. After COVID-19 the condition has become immensely problematic. Not only this has led to loss of jobs but overall impact on economy has been huge. Airlines constitute the heart of the aviation industry. Without airlines airports and other allied sectors cannot thrive

The main purpose of this paper is to analyze the current scenario of aviation industry with special focus on airlines distress in Indian aviation industry due to the virus (COVID-19) and the future of industry is impacted by it.

Keywords: Bankruptcies, Financial Distress, Aviation Industry, Stock Market Regulators

Introduction

India is ranked as world's third largest aviation market domestically. It is expected that India's overall aviation market will become 3rd largest globally by 2024. \$72 billion is currently contributed by Indian aviation sector to GDP. In respect of aircraft passengers, India is 5th largest market including both domestic and international passengers.

* **Dr.Nandita Mishra**, Associate Professor- Accounting & Finance Birla Institute of Management & Technology, Email: saanvinandita@gmail.com

****Simrat Kaur**, Research Scholar- Amity College of Commerce and Finance. Amity University Uttar Pradesh

Including 86 foreign carriers and 5 Indian carriers, India has total 91 international carriers with which major countries relate to India. Global RPK (Revenue Passenger Kilometer) growth was 6.5 % in 2018 whereas the domestic RPK, growth was 18.6%, three times of global RPK.

- By 2027, increase in fleet size of Indian carriers to 1100 aircraft, is predicted.
- By 2032, it is expected that freight traffic to cross 11.4 MT in Indian airports.
- By 2037, it is expected that Indian aviation market may cater to 520mn passengers as it is the fastest growing market.
- By 2037, it is expected that demand for aircraft will be 1,750.

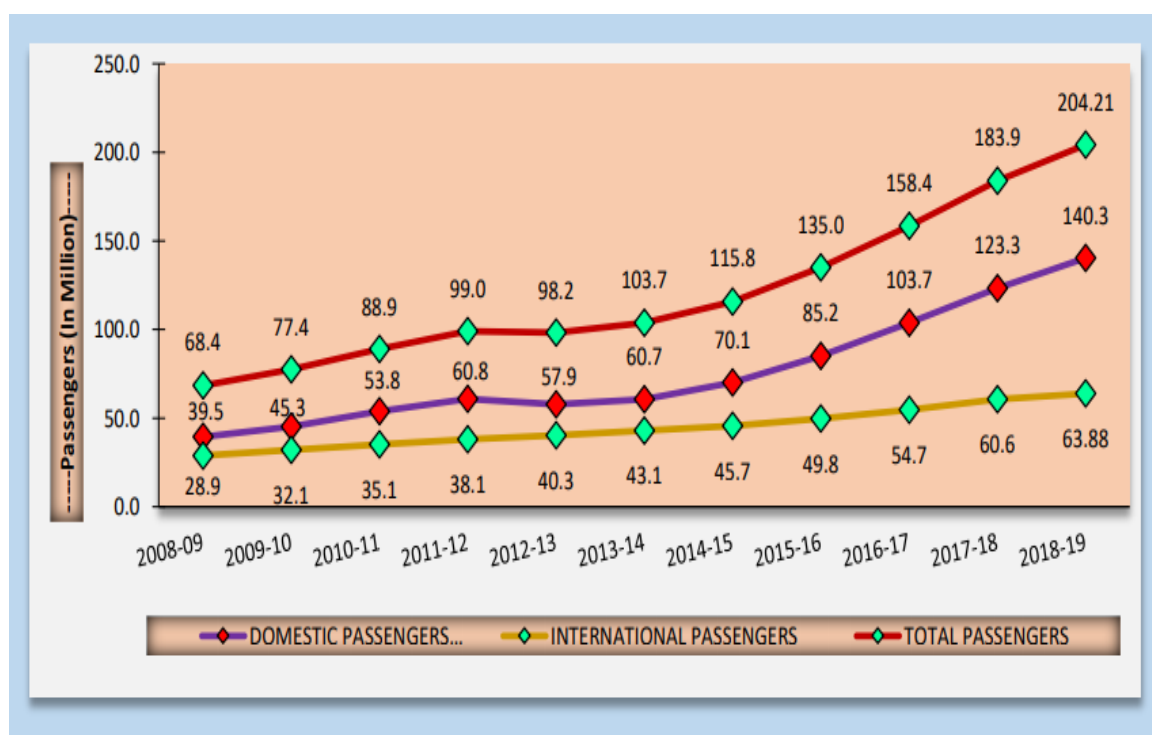


Figure 1: Passenger traffic carried by scheduled carriers over the last ten years, Source: (Directorate General of Civil Aviation, 2018-19)

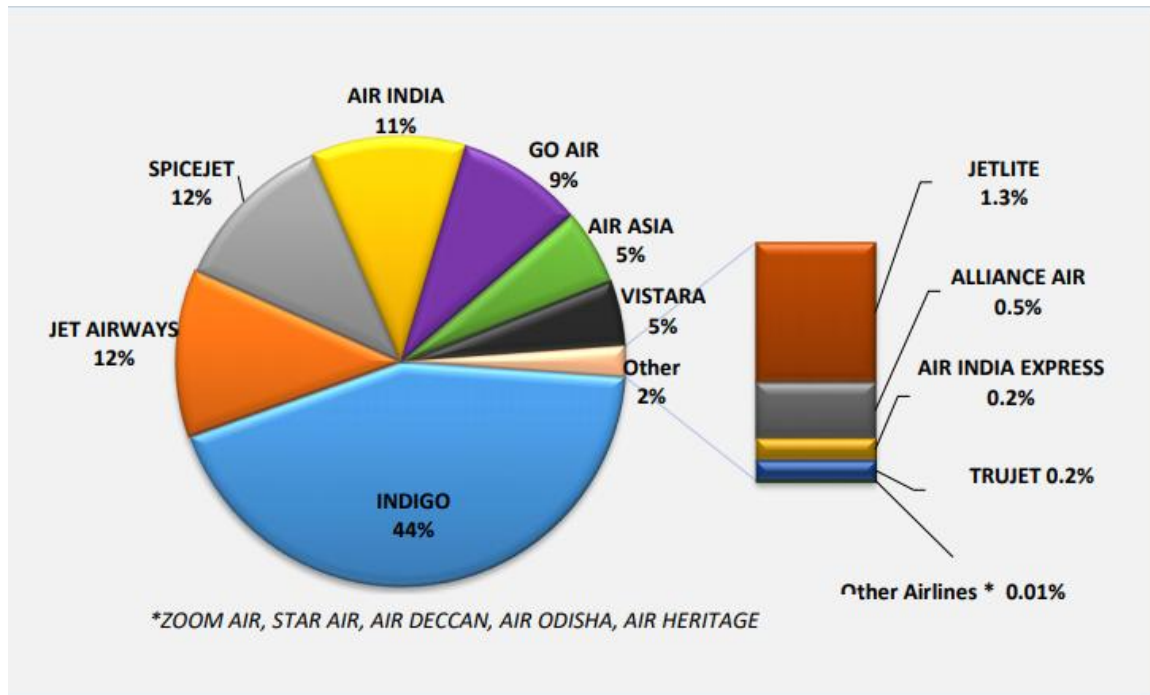


Figure 2: Market share (%) in terms of domestic market demand (RPK)- 2018-19, Source: (Directorate General of Civil Aviation, 2018-19)

Financial Distress

Financial distress is a stage before bankruptcy where the company is unable to generate profit, unable to pay its creditors or face lots of difficulties in paying the creditors.

Financial distress also imposes negative impact; large number of bankruptcies lead to depression or recession. It affects the consumers and companies before spending or lending as they become more conscious. Journey of bankruptcy starts when there is a reduction in company's profit because consumers stop spending when they become conscious.

It is difficult to secure financing when a company is under financial distress. It may lead to orders cutting back by customers, significant drop in its market value or terms of delivery changing by its suppliers. Businesses which have a possibility in experiencing financial distress in future can take help from predicting bankruptcy or financial distress. To avoid

bankruptcy in future prior warnings may help businesses to take some appropriate changes. Business failure or cost of financial distress can be mitigated with the help of prior warnings.

When a company is unable to generate income or revenue and is not able to pay its financial obligation, that state is known as financial distress (FD). It can be because of non-assets or high fixed costs. It is a major concern if a firm goes through failure. FD prediction set out as effective warning system i.e., it is significantly important for companies.

Top companies of airline industry

IndiGo

With a largest market share of 46.9 % as of March 2019, IndiGo is biggest passenger airline in India. Company is based on three main pillars which are being on time, offering low fares and delivering a courteous experience. It mainly operates in India's domestic airline market. From 2006 a carrier with one plane to fleet of 255 aircrafts today. Currently it operates flights to 89 destinations including 24 internationals and 63 domestics.

Jet Airways

On 1st April 1992, Jet Airways India Limited (JAIL) was incorporated. It has headquarters in Mumbai. Main hubs of Jet Airways are at Chennai, Delhi, Amsterdam and Mumbai airports. It has served services previously to The Middle East, North America, Europe and North America. All operations are suspended from 17th April 2019 and internationally on 12th April 2019.

SpiceJet

In 1984 SpiceJet Ltd was incorporated. It is an Indian carrier based at New Delhi (Indira Gandhi International Airport). It is one of the largest airlines in India serving domestic destinations all over the country. In October 2010, the airline started operations internationally. Currently it operates flights to 62 destinations including 9 internationals and 53 domestics.

- Daily around 53,000 passengers are carried.
- Among domestic airlines, highest passenger load factor scheduled as of 2018-19.

Air India

State-owned carrier, Air India has its main hubs at Mumbai and Delhi airports. In august 2007, Indian Airlines merged with Air India. Domestic as well as international destinations are covered by Air India's network including Asia, Europe, North America and The Middle East. Air India Express is also operated by the carrier. On 11 July 2014, it became the member of Star Alliance.

Go Air

Go Airlines (India) Ltd is a part of Wadia Group. It runs under the Go Air brand. Operations started by Go Air in November 2005. Currently 330 daily flights are operated by the airline across 36 destinations including 9 international and 27 domestics.

Go Air is positioned as '**the Smart People's Airline**'. It's theme of '**Fly Smart**' aims to offer time efficiency, consistency and quality assurance to the passengers through cost friendly fares.

Air Asia

On June 12, 2014, Air Asia India started its operations and it plans to increase its route network to provide services to all Indian metro cities with a selection of some tier-II cities.

As by January 2020, 21 destinations are covered by Air Asia. Air Asia India has secondary hubs in Kolkata and Delhi and is based at Bangalore Kempegowda International Airport.

Vistara

Vistara is a joint venture of Singapore Airlines limited (SIA), and Tata Sons Private Limited in which 49% stake is owned by Singapore Airlines and 51% stake in partnership is hold by Tata Sons. Vistara is derived from Sanskrit word ‘**Vistaar**’ which means ‘**a limitless expanse**’. An inspiration is drawn by Vistara from the world as Vistara occupies the ‘limitless’ sky.

Vistara started its operations on January 9, 2015 with a flight from Delhi to Mumbai. Currently Vistara serves 35 destination with over 200 flights daily. More than 15 million customers have been flown by Vistara since it started operations.

Distress in industry before COVID-19

Cases of financial distress have been reported by airline companies in India. In 2016, Air Asia faced a cash crunch and its expansion plans were forced to be kept on hold as per the report of (Livemint, 2016). Huge losses were reported by SpiceJet in 2014 and by the end of the year it cancelled about 2000 flights forcefully according to (Economic Time, 2014). Over the last ten years various bankruptcies are led by similar situations of financial distress. In April 2017, Air carnival stopped operations (focused routes in southern part of the country). Same year Air Pegasus went bankrupt and in October 2012, Kingfisher Airlines stopped operations due to failure of paying liabilities and loans. These examples show the seriousness of financial distress in this sector as it can lead to huge losses and bankruptcies (Mahtani & Garg, 2018).

Jet Airways in distress:

Jet Airways owes more than 8000 crores to banks, thousands of crores more in arrears to vendors, lessors and employees. The airline formally stopped flying on 17th April 2019.

It is seen as the end of Jet Airways as to save the airline no plans are submitting by the bidders. Creditors are planning to meet and deciding the liquidation of assets and shut down of the company. Airline has used 270 days out of 330 days as according to Indian bankruptcy law, to submit a resolution plan an airline has 330 days. According to law only 60 days are left so for 90-day extension NCLT's (National Company Law Tribunal) approval is required.

Mistakes done by big airline companies which leads to financial distress:

Airlines like Jet Airways and in 2014, SpiceJet went under distress because of having load factor of about 78%. Lower load factor with low passenger demand can lead to financial distress. Buying aircrafts directly from the manufactures by airlines like Jet Airways and Air India can increase leverage which is one of the major factors of financial distress. Now instead of buying, SLB (sale and leaseback) mechanism is followed by the companies which helped them to save huge outflow.

Covid-19 - Affecting the global economy?

COVID-19 (coronavirus) is an infectious disease in which most infected people feel mild to moderate respiratory illness and no special treatment is required to recover. Those people which have major medical problems like diabetes, cancer, cardiovascular disease and those who are old are likely to have serious illness.

There is no such treatment or vaccines for COVID-19 currently. An outbreak of coronavirus started on February 17 in China, but less than 1000 people were affected outside the country. Over the next 30 days, investors didn't know that coronavirus burst out of china and major outbreaks seen in Italy, South Korea then in Spain, Germany. The UK, The United States and in France.

Businesses suddenly stopped, stock market start dropping, and sudden emergency actions taken by central governments even bigger than the financial crisis happened in 2008.

As per Johns Hopkins University, more than 3,00,00 people are affected by coronavirus and at least 12,944 have died till March 22, 2020 (CNN, 2020).

Covid-19 – Impact in India

341 active covid-19 cases and 5 death were reported till 22nd March 2020. Necessary steps were taken by Govt. of India to ensure the people are prepared to face this disease and threat created by the pandemic.

Health emergency as well as financial crisis is created by COVID-19. Coronavirus came at a worse time as Indian economy was already facing slowdown. 25 million jobs are about to abolish due to coronavirus as estimated by the International Labour Organization. In 2020, global economy can be cost by coronavirus between \$1 trillion and \$2 trillion according to UNCTAD (United Nations Conference on Trade and Development).

Impact on India could be \$348 million though it has affected only 30 people in early March in India.

Impact of COVID-19 on Indian aviation industry

If corona virus contains at current level and does not spread continuously the about \$63 billion loss would be seen in passenger's revenue as said by the airline companies.

Situation of Indian airline industry on 20th February 2020:

\$29.3 billion loss in revenues is analyzed by IATA (International Air Transport Association) due to the impact of COVID-19 on markets associated with China.

12-15% dip in demand is seen by Indian carriers during the first 2 weeks of March which make the situation worse. There can be fall of 25 % or more in the coming period which is said by CAPA (Corrective and Preventive Action) in its first update given on the impact of COVID-29 on Indian aviation industry. 30% down is seen in upcoming bookings which shows a dark period in Indian aviation market.

During the last one month till March 18, 2020, shares of SpiceJet crashed 55% to Rs. 37.80 and IndiGo slipped to 35%.

CAPA-Centre for Aviation March 18 report:

"In the absence of serious and meaningful government intervention, such an outcome could lead to several Indian airlines shutting down operations by May or June due to a lack of cash".

If we look at the situation of Indian airline industry on 20th March 2020, shares of airline companies jumped up to 10%. ICRA rating agency said that in the coronavirus outbreak, aspect for airline industry remains negative which resulted in cancellation of travel by many international passengers to South East Asian countries.

As per CAPA, 150 planes might be grounded initially by Indian airlines because of situation created by COVID-19. If there will be continuous decline in the demand, by April they may ground forcefully most of their fleet.

Consolidated losses in Q1 except Air India are expected at \$500-\$600 million as per initial estimates but if the situation remain same it may be revised downwards lately. As per CAPA, it is expected that most of the airlines will be bankrupt by the end of May 2020. To control the situation coordinated industry and government action is needed immediately.

Due to the impact of COVID-19 and because of various travel restrictions by multiple governments in the world, many airlines technically in the stage of bankruptcy or on the way of breach of debt contracts. Due to the fleets grounded by the companies, cash reserves are decreasing, and flights are operating even lesser than half.

Forward bookings are far greater by cancellations. Any new recommendation by government is to stop flying. Demand is continuously decreasing and whole airline industry is far away from the normality. Aviation industry is not only about airline health, but it is more than that. It is important for global trade and communication.

There can be impact of Air India privatization on to the distressed situation. To maintain the state airline running, Govt. may provide interim funding of \$300-400 million immediately.

Government Initiatives

As suggested by CAPA, Government should:

- Bring ATF (aviation turbine fuel) under the GST regime.
- On a weekly basis, jet fuel prices should be revised.
- Short-term suspension should be implemented.
- Credit terms for payments should extend.
- Working capital loans should be extended by banks which are secured against sales-and-leaseback incentives or future sales.

Relief measure proposed by the Government:

- Fuel credit line for two months
- Waiver of VAT on jet fuel, excise duty.
- Easy loan at 1% rate.
- Waiver of parking charges and landing charges.

Rescue package by the Government

Proposal by Finance Minister includes:

- Taxes levied on the aviation sector is suspended temporary including suspension of aviation fuel tax. Rescue package is worth of 100-120 billion rupees (\$1.3-\$1.6 billion) which is proposed by India's civil aviation ministry.

Major decisions taken by Airline Companies

On 18th March 2020, all international flights are cancelled by Vistara after following Go Air as all international operations have been grounded by it already. Around 65%-70% overseas flights suspended by IndiGo and Air India and several planes grounded already. 25% of domestic operations are going to be trimmed by IndiGo as the travel demand reduced because of COVID-19 said by the airline on 20th March 2020.

Stock view of listed companies of Indian aviation industry

Table 1: Stock prices of listed Indian aviation companies on NSE, Source: (NSE, 2020)

Date	IndiGo (InterGlobe Aviation Limited)	SpiceJet Ltd	Jet Airways (India) Ltd
20-Feb	1464.85	92.85	27.9
24-Feb	1444.5	86.6	27.15
25-Feb	1376.9	87.7	28.2
26-Feb	1391.45	89.05	27.25
27-Feb	1366.5	87.45	25.95
28-Feb	1300.05	83.35	25.1
02-Mar	1239.05	75.8	23.9
03-Mar	1228.45	74.35	22.75
04-Mar	1201.05	70.9	21.65
05-Mar	1211.1	69.5	22.7
06-Mar	1176.9	63.2	21.6
09-Mar	1213.2	63.7	20.55
11-Mar	1160.25	60.35	19.55
12-Mar	1018.4	48.6	18.6
13-Mar	998.8	43.75	17.7
16-Mar	978.4	42.6	16.85
17-Mar	976.7	42	16.1
18-Mar	949.9	37.8	15.85
19-Mar	909.2	34.05	15.9
20-Mar	871.7	35.5	15.85

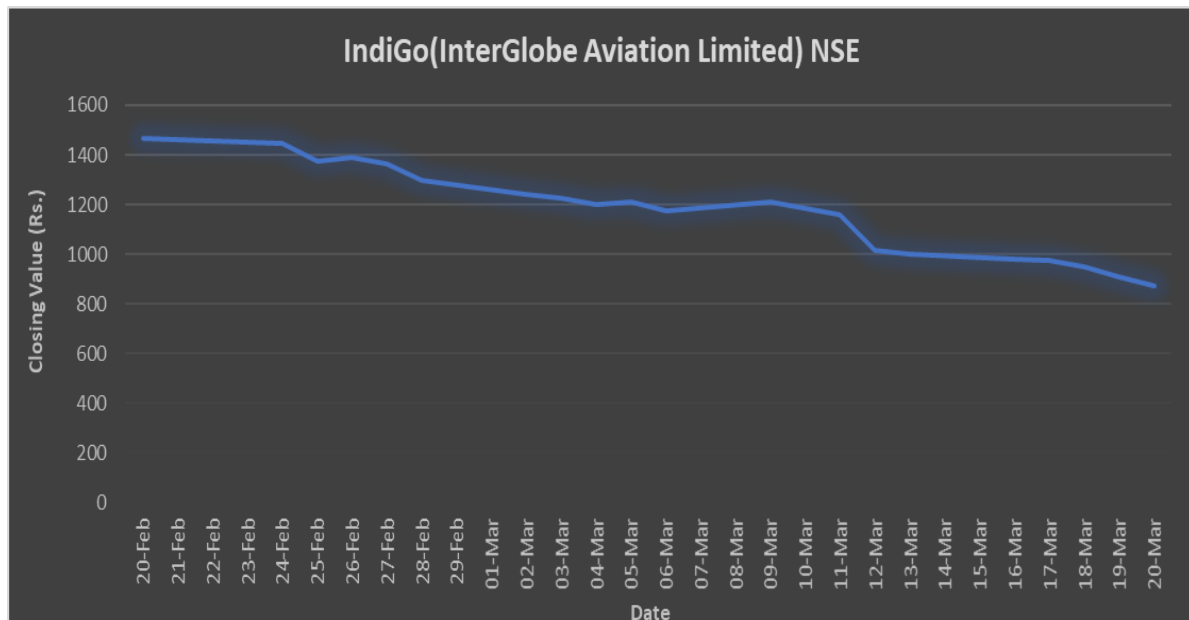


Figure 3: Change in the NSE stock price of IndiGo



Figure 4: Change in the NSE stock price of Jet Airways

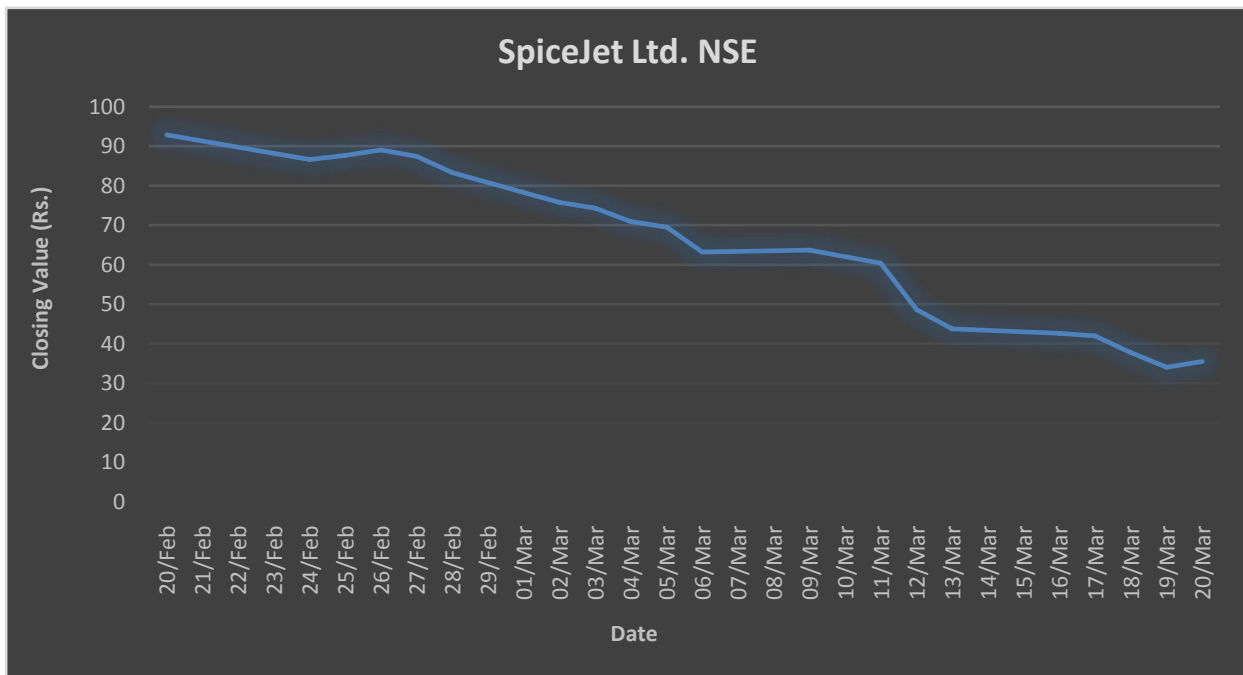


Figure 5: Change in the NSE stock price of SpiceJet

From the above table and figures we can see that there was a drastic change in the stock prices of all three Indian aviation companies. One of the main reasons could be the increase of COVID-19 in the country. About 10% decrease is seen in last few days.

As comparing to the prices of last month, stock prices of all the companies have reduced to its half of the value or less. Passengers are avoiding travelling in the current situation and restrictions by various governments due to COVID-19 is another big reason for the drop in price.

Future of Indian airline industry

The world governments are climbing to rescue airlines which have been forced to cut jobs and to park planes because of the virus which set a slowdown on travel. IATA (International Air Transport Association) estimated need of more than \$200 billion bailout by the airlines.

Earlier various airline failures have been seen from the first swing of airline deregulation in 1990s, but they were relatively small. Two crucial airline closure (Jet Airways) since 2012 have been seen which had a major impact on aviation system of \$ 6 billion, SpiceJet was also rescued last minute by Ajay Singh which may have converted into the third failure.

COVID-19 hit the Indian Aviation System even more badly than the above stated failures. Around 68% of aircraft being grounded by Indian Airlines due to the coronavirus outbreak over the next 2 months as calculated by the India government.

If any kind of meaningful support by government is not given to the airline industry, there can be lack of cash in some local airlines and could shut their operation by May or June.

It is said by the political agreement that the impact of COVID-19 could extend for up to 6 months or more than that as it is not a short-lived disturbance.

Conclusion

Indian aviation industry plays a vital role in contributing to the GDP of the country. Aviation industry is very important as it helps in communicating with the other countries and in increasing trade with them but due to the outbreak of this pandemic disease a financial distress can be seen in the industry.

Travel avoided by people and increase in restrictions made more difficult to the industry to suffer. Major drop is seen in the stock prices of the top Indian aviation companies. Privatization of Air India is put on hold. It is predicted that if any major steps would not be taken by the government then top Indian companies can lead to bankruptcies.

As of now many proposals are proposed by the government to rescue the aviation industry as due to COVID-19 slowdown in the industry lead to financial distress.

Proposals like waiver of parking charges & landing charges, easy loan at 1% rate and some of the suggestions are given by CAPA to Indian government too like extending of working capital loan by banks, bringing ATF under GST regime.

If the effect of COVID-19 decrease, in next few months and government make major steps and follow the proposals made by them to decrease the slowdown and distress in the industry, then there are chances of handling the current situation and upcoming bankruptcies of various Indian aviation companies.

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