Aviation: Half-yearly Update

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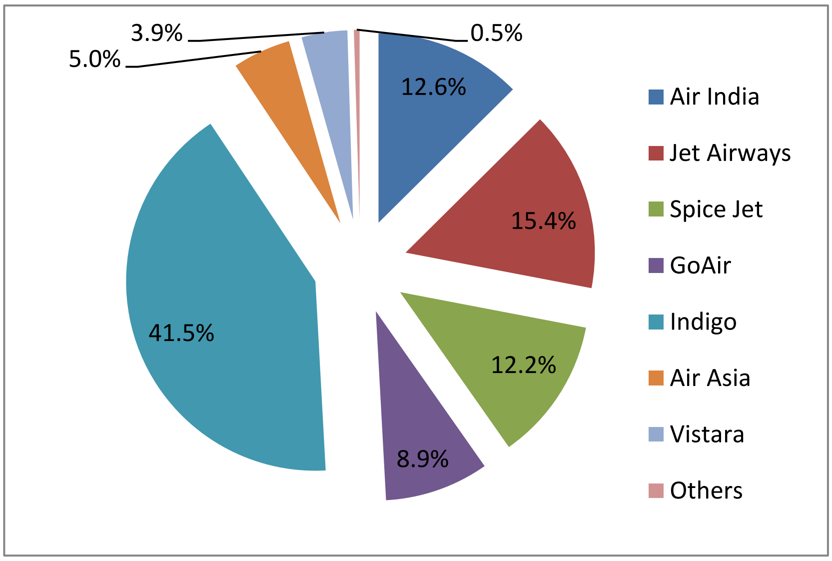
Strong passenger traffic growth

India's airline passenger traffic grew for the 49th consecutive month in September 2018.

- Total air-passenger traffic grew by 16.6% for April-September 2018 period y-o-y.
- The international and domestic passenger traffic grew 7.5% and 19.2% respectively during H1FY19 vs H1FY18.
- Total passenger traffic stood at 169.5 million during the 6-month period. Domestic traffic accounted for 80% of the total traffic.

Graph 1.Market Share of Airlines(All domestic airline companies)*



*Source: DGCA Others include all regional airlines *Market Share for H1FY19*

Airlines' performance hit by Fuel and Currency turbulence

- Total passengers carried by domestic airlines grew by 19.6% during the first 6 months of FY19. It stood at 6.9 crore during April-Sep 2018 vs. 5.77 crore for the corresponding period in FY18.
- Passenger load factor continued to remain above 80% for all domestic carriers.
- As per International Air Transport Association (IATA), Indian carriers incur 34% of operating costs on fuel which is well above the global average. With crude oil prices rising, the Indian carriers would be the most affected, compared with their global peers. Actual figures indicate fuel costs account for a much higher proportion of expenses for Indian airlines- roughly 40-45% of the total expenditure.

Traffic: Aided by Improved infrastructure and affordability

- Passenger traffic across airports in the country witnessed strong growth on the back of low fares and improvement in overall air-connectivity due to UDAN (Regional-connectivity) scheme.
- Delhi (35million), Mumbai (25million) and Bengaluru (16million) are the three largest airports and accounted for 44% of the total airline passenger traffic in the country.

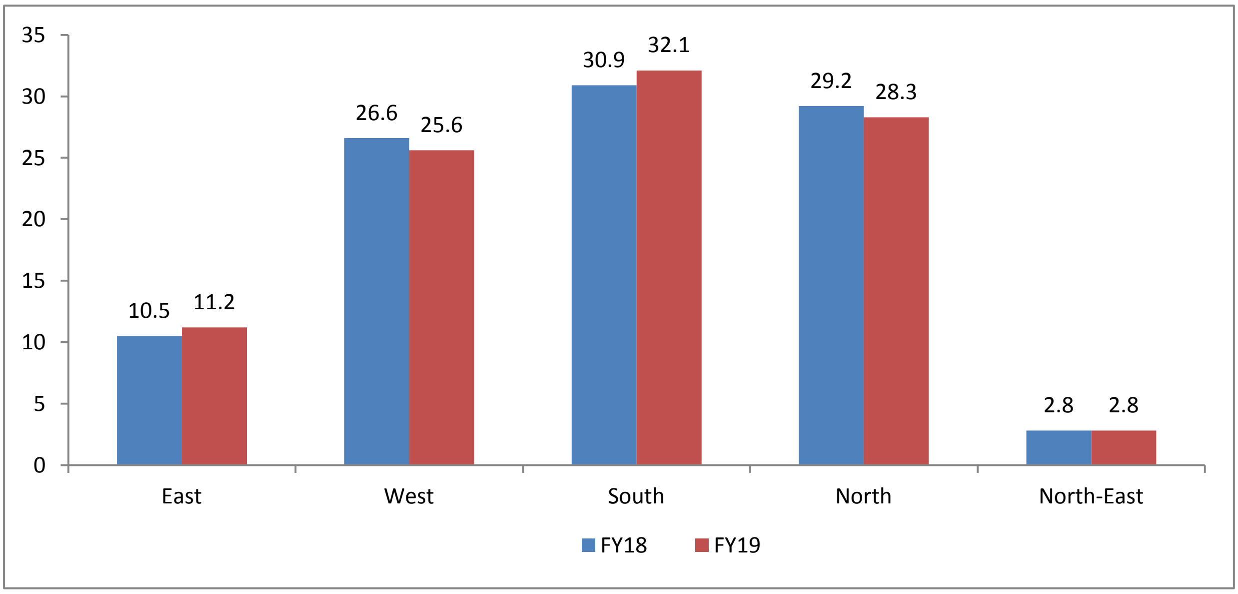
Table1. Passenger traffic across airports in India

	H1FY18	H1FY19	Growth (%)
	(In millions)		
International passengers	31.4	33.7	7.5
Domestic Passengers	113.9	135.7	19.2
Total passengers	145.3	169.5	16.6

**Data for April-September period Source: AAI*

- Southern region continued to account for largest share of passengers with 32%.
- Share of Northern and Western region stood at 28.3% and 25.6% respectively.

Graph 2. Regional passenger-traffic share (in %)



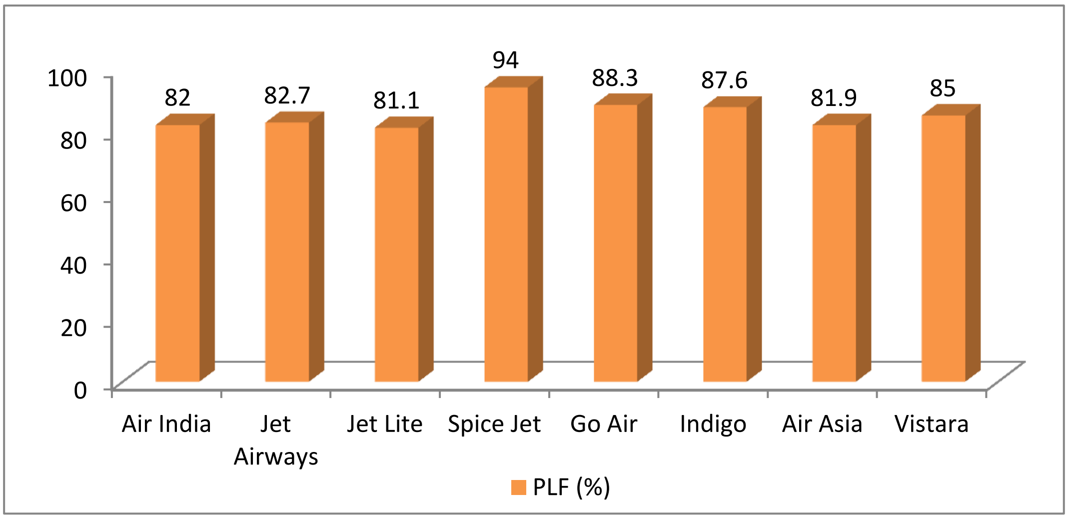
Source: DGCA

- Eastern and North-Eastern region had the lowest share at 11.2% and 2.8% respectively. With the UDAN scheme and modernization of existing air-strips, the combined share of the two regions is expected to grow to 15% by the end of 2019.
- Mumbai-Delhi, Bengaluru-Delhi, Bengaluru-Mumbai, Kolkata-Delhi and Delhi-Hyderabad are the top-5 busiest city-pairs in terms of passenger traffic.
- Pakyong Airport (Sikkim) and Kannur International Airport(Kerala) were new additions in India's aviation infrastructure.
- Pakyong Airport is a Greenfield airport and is expected to further boost connectivity and traffic to the North-Eastern region of India. Kannur International Airport is the 4th International airport in Kerala and is expected to operational by December 2018.

Airlines: Amid strong demand, crude and currency drags

- Out of the 8 airlines, 3 full-service airlines and 1 low cost-carrier reported PLF of 80-85%.

Graph 3. Passenger Load factor of airlines (excl. regional airlines)



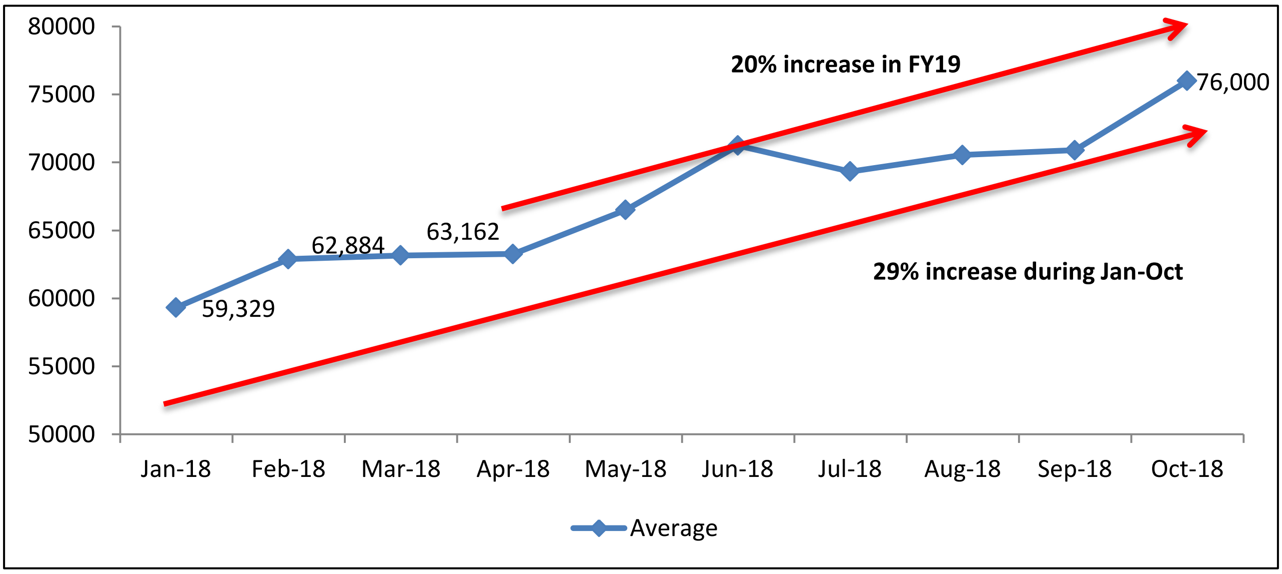
Source:DGCA *excludes regional airlines

- The remaining airlines reported PLF between 85-94%. The largest airline company in the country by market share reported PLF of 87.6% for H1FY19.
- Among the 7 major airlines (Jet and Jetlite taken together), barring Indigo, all other airlines reported fall in market share. The national carrier reported the highest decline in market share Q-o-Q. Air India accounted for 12.6% of the market share in H1FY19 vs 13.3% in H1FY18.

Crude and Currency:

- The Indian airline industry continues to be the fastest growing globally, having reported double-digit growth over the past 4years. The growth has been stymied owing to global crude oil price and falling rupee w.r.t. dollar which has led to an increase in the input cost for airline operators.

Graph 4. Average-monthly ATF Prices (In Rupees/KL)



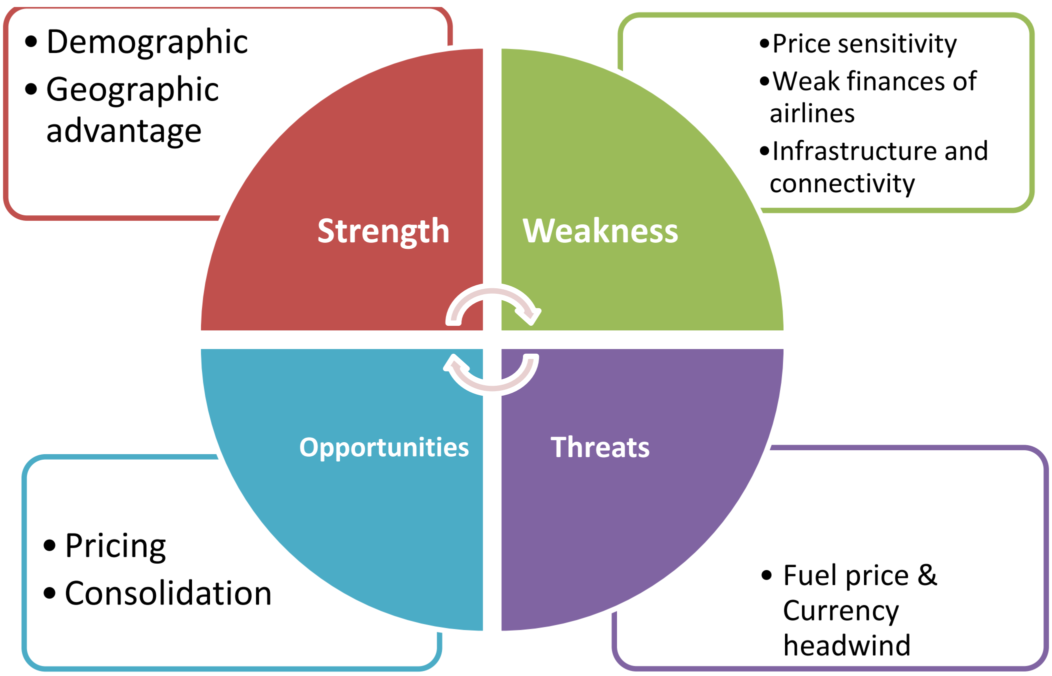
Source: IOCL

- ATF prices have increased 20% during FY19 and 29% in YTD. This has led to substantial increase in the operating expense of airlines.
- ATF accounted for 25-30% of the total expense of airline companies between FY15-17. The same has increased to above 40% for the sole airline company which reported financials for H1FY19.
- The rupee has depreciated in the range of 11-13% YTD vs dollar. A large proportion of airline costs are denominated in US dollars (fuel, spares and repairs) which in turn drive up operating expenses.

Financial performance:

- Revenue per Available Seat Kilometre (RASK) has remained stable during the year due to heightened competition. Costs on the other hand are expected to increase by over 40-50% as a result of fuel and currency impact which will lead to substantial increase in Cost per Available Seat Km (CASK).
- The key to improvement in the financial performance of airline companies would hinge on improvement in passenger fares. Crude-oil prices have evidently positioned at a new normal ($70-80 per barrel), and dollar-rupee movement too has stabilised at a 11% higher level (₹72 & above/$) from the previous year. Costs would remain at the escalated levels.
- Other revenue sources like freight, baggage and comfort/seating/Value Added services would continue to add marginally to the overall revenue.

Figure 1. SWOT (Analyst View for Current Business Environment)



- Analysing performance of global airline companies, in developed markets, especially US, they have been able to remain profitable during the current financial year (2018).
- More importantly, airlines like Delta, United, American Airlines and Southwest have been passing on the fuel-cost impact by increasing passenger fares, inducting and flying more fuel efficient planes and hiked baggage fares. They have also kept their non-fuel costs under control which further aided their financial performance.

Outlook:

- We expect the airline fares to increase by an average 8-10% over the next two quarters. During the peak season (October-December), airlines would aim at improving realisations on the back of peak PLFs.
- We continue to expect the airlines to witness financial headwinds, given heightened competition. We maintain our earlier estimate of operational margins (OPM) to remain at 4-6% levels or lower for FY19 for the airline sector. Airlines will have to pass on fuel and currency impact to consumers to remain viable.
- Overall capacity addition (Available Seat Km/ASK) is estimated to grow by 12-14% in FY19, mostly by a handful of airline companies. The new-capacity supply would be adequate to meet passenger traffic growth of 15-18% in FY19.