Privatization is the way forward for AI

According to recent Government data, nearly 17 per cent of the total routes operated by Air India are loss-making. What led the national carrier to become a perennially loss-making airline. A ***Bureaucracy Today*** analysis.

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Recently Finance Minister Arun Jaitley in a veiled statement raised a question mark over the desirability of the Government continuing to run Air India (AI) with a meagre 13% share when the private sector occupies an overwhelming 87% of the space. The statement lent credence to a possibility that the recommendation of NITI Aayog for the privatization of Air India could be taken on board.

However, the Ministry of Civil Aviation was not too enthusiastic about outright privatization. Instead, it mooted bringing in a "strategic"partner even while retaining majority control in Air India. It believes that the Government on its own is capable of turning around AI if only the airline is unshackled from its huge debt (currently, about Rs 52,000 crore plus another Rs 8,000 crore it owes to oil PSUs).

Staying clear (at least for now) from the differences between the two, on June 28, 2017, Jaitley informed the nation about the "in-principle" decision of the Union Cabinet for strategic divestment of AI and five of its subsidiaries. A Group of Ministers (GoM) under him has also been constituted to work out the modalities of divestment.

Within a few months, the country will know which way things move. But it is important to analyze as to what led the *Maharaja* to its present state. That will also help in looking for the right solutions.

At the outset, it is worth taking note of the "generic" factors applicable to any Government undertaking – which are generally responsible for its downfall. These are the lack of autonomy to its management in taking decisions, constant interference by the political establishment not only in its policy matters but also in its day-to-day functioning, the load of operating airlines in financially unviable areas (**example**, the Northeast region), excessive manpower and the inflated overheads cost (for AI this includes the cost of generous freebies granted to the political class).

AN ADDITIONAL FACTOR

In the AI case, however, there was an additional factor that overshadowed all the aforementioned causes. This one relates to a seriously flawed decision by the then political establishment – about a decade ago – to procure 111 aircraft for Rs 70,000 crore which was about four times the requirement of only 28. This by itself was bound to give a crippling blow to the financials of the airline.

When a company creates a huge liability (aircraft purchases were funded by borrowings from a consortium of banks) with no matching business to put its assets to use, it inevitably leads to an unsustainable situation. The cash generation is bound to be too little vis-à-vis the requirement to amortize the loans. The irony is that the then Government did nothing to boost the utilization of the aircraft. Far from that, it gave away excessive bilateral seats and profitable routes to foreign/private airlines thereby ensuring that most of these aircraft sit idle.

The other flawed decision was the merger of Indian Airlines with Air India in 2007. Even as there was little to gain by way of synergies (mergers are normally driven by this logic), the vast differences in the work culture ethos, compensation packages and the age profiles of employees of the two entities led to operational inefficiencies thereby compounding the losses and increasing the debt of the combined entity.

The outcome of all this is pathetic as Air India is saddled with a debt of about Rs 52,000 crore. This includes Rs 22,000 crore due to the acquisition of aircraft and Rs 30,000 crore as a

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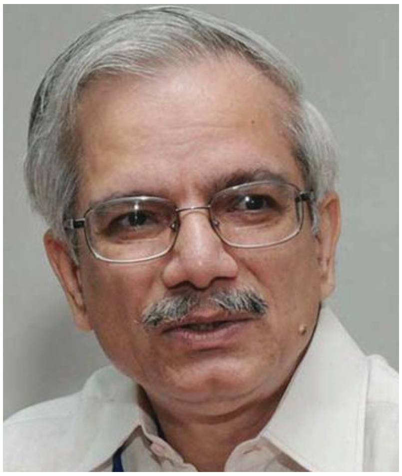

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working capital loan. This is despite the erstwhile UPA dispensation sanctioning a bail-out package of Rs 30,000 crore in 2012; of this, about Rs 24,000 crore has already been given (most of it has been used to fund operational losses even as the mountain of debt remains intact).

In retrospect, it is now amusing to hear that "it makes no sense for the Government to be running an airline as it cannot withstand competition from no-frills private airlines". What a joke! First, the powers that be make deliberate moves to incapacitate AI and concurrently boost private airlines resulting in a steep decline in its share from 35% in 2007 to 13% currently and then bemoan it cannot compete.

THE WAY FORWARD?

What is the way forward? Broadly, there are three approaches to address the issue. First, continue the status quo but with more "efficient" and "transparent"governance a la Modi style. **Second**, retain majority control (>50%) with the Government but induct a "strategic" partner (domestic or foreign who is already in airline business) and **third**, shed majority control – either 100% upfront or keeping some residual shares (**example**, on the lines of divestment in Maruti Udyog).

The **first** is clearly unworkable. Modi's dictum of "minimum government and maximum governance" may be good administrative reforms and has indeed delivered in terms of efficient services and no corruption. But this won't work in the context of a commercial enterprise. The proof of pudding is in eating. Already three years under his regime, we have not seen any significant improvement except that AI's losses have come down somewhat (things could be much worse if those who incapacitated Air India in the first place were to come to power again, say, in 2019 or 2024).

The **second** approach carries an instinctive appeal as divestment of a good chunk of AI shares say, 26%. A "strategic" partner can bring in new technologies, innovations and management practices besides help in extinguishing a portion of the debt. But why would Modi give so much when the Government continues to be in the driver's seat? Add to this accountability and continuous surveillance by statutory bodies such as the Comptroller and Auditor General, the Central Vigilance Commissioner and the Central Bureau of Investigation. All of this is sufficient ammunition to scare him away.

There is a view that the Government should sell the airline only after it has erased the debt from its books. This is a bad idea. AI has huge assets, including land and real estate, most of it in prime locations, and intangibles such as bilateral and landing rights which command a huge premium. Besides, one cannot ignore the value of its aircraft. In short, all assets with right valuations should more than pay for the debt plus generate good value for the buyer.

A GOOD OPTION

The third one is a good option. While divesting majority control to a private player, the Government may retain some residual AI shares to keep a tab on how a new owner will be handling things (those may be offloaded at an opportune time to fetch a good price). Being in the driver's seat and free from surveillance by three watchdogs (the CAG, the CVC and the CBI), a private player will have strong incentive to buy the airline which will get all that is needed to give it the required boost.

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Hopefully, Team Modi will fully leverage the inherent strength of the *Maharaja* while negotiating a deal and not get carried away by numbers on the balance sheet *per se*. ■

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