Executive Summary

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Background

Air India Limited (AIL), wholly owned by the Government of India (GoI), is engaged in Domestic as well as international air transport operations. The unfavorable industry scenario coupled with operational difficulties of the Company strained the financial position of Air India Limited. The high debt burden of the Company further contributed to liquidity stress and the Company lost significant market share in recent years.

The Company formulated a comprehensive Turnaround Plan (TAP) which was approved by the Cabinet Committee on Economic Affairs (12 April 2012). This Report examines the implementation of the Turnaround Plan. Report No. 18 of 2011 of the C&AG of India, had reviewed the Performance of Civil Aviation in India.

Financial Restructuring

Turnaround Plan/Financial Restructuring Plan (FRP) of AIL included infusion of equity of ₹42182 crore over the period from 2011-12 to 2031-32, restructuring of working capital of ₹22157 crore, earning of revenue of ₹5000 crore over ten years from 2012-13 to 2021-22 through monetisation of assets. The Company was expected to earn positive Earning before Interest Taxes Depreciation and Amortisation (EBITDA) from Financial Year (FY) 2012-13 and cash surplus from FY 2017-18.

AIL sold five B-777-200 Long Range (LR) aircraft during the period from 2013 to 2015. The sale proceeds were utilised to liquidate the outstanding loan amounting to ₹1804.96 crore. However, the equity commitment towards repayment of aircraft loans (during 2014-15) had not been adjusted to account for premature liquidation of aircraft loan taken for five aircraft.

(Para 3.3.1)

Equity commitment for Non-convertible debentures was worked out considering the interest rate at 9.50 *percent*. However the actual rate of interest payable was 9.08 *percent*. Considering this difference in rates, the equity sanctioned by GoI was higher by ₹521.53 crore over the entire repayment period (up to 2032).

(Para 3.3.2)

The working capital requirement of AIL exceeded the FRP limit which resulted in availing of additional short term loans. This increase in working capital requirements and consequent increase in short term loans was due to failure in generating projected revenue, mainly on account of non-achievement of asset monetisation target, increase in staff costs due to delay in operationalisation of subsidiaries and non-implementation of recommendations of Justice Dharmadhikari Committee (JDC), for harmonisation of wages and increase in interest charges.

(Para 3.4.1)

Monetisation of Assets

AIL failed to achieve the target mainly due to improper selection of properties not based on actual feasibility of monetisation.

Four properties viz. Plot at Vasant Vihar, Delhi, Plots in Nerul, Navi Mumbai, Buildings at Old Airport-Mumbai & Land at Baba Kharak Singh Marg, Delhi listed in the TAP could not be monetised due to various deficiencies in ownership and conditions attached to the ownership. Further, four properties identified in TAP for monetisation could not be monetised as the same were being utilized by the company for its own use.

(Para 3.5.1 and 3.5.2)

108 properties were given for valuation to M/s DTZ, out of which most of the properties had been given on lease by State Govt. / Airport Authority of India (AAI) / Govt. Agencies for specific purpose. Further, 18 properties did not have clear title. Hence, monetisation of these properties was uncertain. Only six properties had been put up for e-auction, out of which only two properties were sold till date.

(Para 3.5.3.1 and 3.5.3.3)

Due to non-achievement of yearly monetisation target of ₹500 crore, there was additional interest and debt burden on the Company.

(Para 3.5.4)

Availability of Aircraft

AIL executed purchase agreement with M/s. Boeing and M/s. GE for supply of fifty aircraft. Delivery of these aircraft started in 2007.

A month after the last B-777-200 LR aircraft was delivered to AIL, the company decided to lease out three B-777-200 LR aircraft as surplus capacity of wide body aircraft was likely after receipt of B-777-300 ER. This did not however materialise and led to operational losses of the airline. With the decision to utilise B-777-300 ER with re-despatch method for long haul operation, the B-777-200 LR aircraft, which were initially procured for long haul operation, were rendered redundant.

(Para 4.2.1)

Five B-777-200 LR aircraft were sold to Etihad Airways at significantly lower price than the indicative market price of USD 86 to 92 million per aircraft obtained by the company before initiating the sale process. Another valuation exercise was carried out after opening the financial bids and the market value of the aircraft could not be realised in the sale. AIL incurred a book loss of ₹671.07 crore on the sale of five aircraft and payment of ₹324.67 crore towards interest on loans availed for procurement of these aircraft.

(Para 4.2.2 and 4.2.3)

Delay in induction of the B-787-800 aircraft led to AIL operating existing inefficient aircraft on the routes earmarked for B-787-800 aircraft. AIL lodged an initial claim of USD 710 million against which the company received only USD 328 million for compensation from M/s Boeing.

(Para 4.2.6)

The Company, though aware of the shortage of narrow body aircraft as early as May 2010, delayed leasing of A-320 aircraft. This resulted in non-availability of aircraft as targeted. Against the requirement of 19 aircraft, the Company inducted only five aircraft till March 2016.

(Para 4.3 and 4.3.1)

Deployment and utilisation of Aircraft

Deployment of aircraft remained low as they were grounded for considerable period. The main cause of grounding of AIL aircraft was non-availability of spares, leading to cannibalisation of spares from one aircraft to another, compounding the grounding period and loss of flying hours. In case of some aircraft, the initial provisioning of spares was lower compared to that recommended by manufacturers/ suppliers. Orders for spares were placed only as and when the need arose. There was excess grounding due to delay in completion of regular scheduled checks. Further, there were instances of prolonged grounding exceeding six months where the aircraft were cannibalised. For the period the aircraft was grounded, the Company continued to pay finance charges and lease rent.

(Para 5.1 and 5.2)

Six B-787-800 aircraft had to be grounded soon after induction for over four months on account of reported malfunctioning of Lithium-ion-Battery. The purchase agreement did not contain any provision for levying penalty on the manufacturer in case of inherent technical fault. In the absence of specific provision in the agreement, AIL failed to recover claim of USD 50 million, preferred on M/s Boeing in full. As against AIL's claim M/s. Boeing agreed to pay USD 24 million in cash and USD 3.4 million towards waiver of late fee on AIL's spare account. In the meanwhile, AIL incurred substantial expenditure due to unplanned grounding on account of mechanical defect in the aircraft which was a design deficiency attributable to M/s Boeing. Further, the Dreamliner (B787-800) which had been identified as the workhorse of AIL suffered continuous technical snags since its introduction in AILs fleet.

(Para 5.2.2.1 and 5.2.2.2)

TAP had set targets for utilisation of aircraft in terms of hours to be flown. The utilisation of the aircraft were, however, below the target in TAP. The aircraft were grounded for prolonged periods leading to low utilisation. The Available Seat Kilometer (ASKM) of the newly acquired B-777-200 LR, B-777-300 ER and B-787-800 aircraft had been lower than the targets fixed for the period from 2010 to 2016.

(Para 5.3)

The empty weight of the B-787-800 aircraft was observed to be higher than the prescribed weight by ten tons. The increased weight of the aircraft would result in additional fuel consumption. M/s Boeing however, admitted that performance of B-787-800 aircraft had been below what has been promised and AIL would be compensated by providing suitable discount in future delivery of three B-777-300 ER aircraft. The procurement contract did not have adequate safeguards to enforce compensation and as such the company had to resort to negotiation. M/s Boeing refused to negotiate the ceiling on compensation but offered negotiation in good faith.

(Para 5.3.1)

The Company could not achieve the TAP targets for utilisation of available fleet in respect of narrow body aircraft.

(Para 5.5.2 and 5.5.3)

Aircraft grounded for routine checks remained grounded for prolonged periods owing to non-availability of components, serviceable engines and other parts which led to cannibalisation of parts.

(Para 5.4.2, 5.4.3, 5.4.4 and 5.4.5)

Considerable delays in operationalising the CFM engine facility led to engines being sent abroad for repair and maintenance.

(Para 5.4.5.1)

Inefficiency of maintenance of aircraft also resulted in compensations that the airline had to pay to lessors for non-fulfilment of re-delivery conditions of the aircraft.

(Para 5.4.5.3)

Management of bilateral agreements and slot management

Enhancement in bilateral entitlement between India and foreign countries resulted in seat capacity allowed in the bilateral far exceeding the genuine passenger traffic requirements between two destinations leading to its use for 6^{th} freedom traffic by foreign airlines impacting the interest of AIL. Enhancement of bilateral entitlements had greater impact on operations in gulf sector particularly Dubai and Abu Dhabi.

(Para 6.1)

Enhancements in bilateral entitlements between India and foreign countries had resulted in seat capacity allowed in the bilateral agreements significantly exceeding the “point-to-point” passenger traffic requirements between the two destinations. The sixth freedom traffic carried by the 17 foreign airlines continued to significantly exceed the point-to-point traffic between the countries during the years 2014-15 and 2015-16. During 2014-15, 6^{th} freedom traffic constituted 59.15 *percent* of the total carriage. This increased to 61.14 *percent* during 2015-16

(Para 6.1.1)

AIL had been granted 5^{th} freedom rights in a majority of the bilateral agreements. Out of the 50 MoUs reviewed, Audit noticed that designated carriers of India had clear intermediate/beyond 5^{th} freedom rights in 28 agreements. In 41 out of 50 countries reviewed, AIL had the option of utilising 5^{th} freedom rights. However, Audit observed limited utilisation of 5^{th} freedom rights by AIL

(Para 6.1.3.1)

AIL had utilised 100 *percent* of the allocated capacity of bilateral entitlements *vis-a-vis* 13 countries. Yet the company made no efforts to enhance these allocations or to provide for future enhancements in capacity, despite increase in fleet size following procurement of aircraft. In India-Oman sector and in India-Qatar sector MoCA withdrew seats allocated to AIL and transferred it to Indigo airlines, due to non-utilisation of allocated seats by AIL.

(Para 6.1.3.2)

Network and Route Strategy

AIL was able to operate only a single hub at Delhi as against the envisaged hubs at Delhi and Mumbai, even after four years of approval of TAP. AIL had also moved away from the TAP strategy of launching of 'Indian Shuttle Service' to utilise all economy narrow body aircraft to target new passenger segment and taken a conscious decision to adopt hybrid model of Full service carrier and Low cost carrier.

(Para 7.1 and 7.2)

While the Company envisioned re-emergence of Air India as the market leader in Indian aviation sector by providing seamless travel within India and the world with the introduction of appropriate network model, the Company failed to utilise its available resources optimally, particularly for the narrow body fleet of A-319 and A-321.

(Para 7.3)

All international services and domestic services of AIL recovered their fuel cost during 2012-13 and 2014-15 respectively. AIL achieved surplus over variable cost in 2012-13. This surplus over variable cost increased from ₹686 crore in 2012-13 to ₹4103 crore in 2015-16. AIL however failed to generate surplus to meet the total cost, the deficit over total cost being ₹5514 crore in 2015-16. Operations in International sector was the major contributor to the overall deficit.

(Para7.4)

Human Resource Management Initiatives

Milestones that AIL had to achieve for release of equity included ceasing of payment of Productivity Linked Incentive (PLI) till the achievement of Profit Before Tax by AIL and working out VRS package by December 2011. Report of Group of Officers, approved by CCEA, also included need for rationalising of costs, trimming of management and employee groups to drive the productivity of airline.

Despite direction of CCEA to stop payment of PLI till the time AIL could generate profit before tax, AIL made payment of ₹734 crore being 75 *percent* of PLI to the employees as adhoc pay. Further, one step-up benefit given to the Aircraft Maintenance Engineers and Technical Officers in contravention of the recommendation of JDC report resulted in annual expenditure of ₹13.92 crore.

(Para 8.1.A and 8.2.1)

In contravention of the recommendation of JDC report, AIL approved promotion of 2482 managerial employees, allowed accommodation of crew in five star hotels leading to excess expenditure and extended free passage to family members.

(Para 8.2.2 to 8.2.4)

AIL had excess manpower compared to the approved standard force. However AIL hired consultants, temporary and casual employees, etc. which added to staff expenses.

(Para 8.3)

The crew of AIL has not been optimally utilised which resulted in additional payment of ₹48.89 crore. The existing Cabin crew were also underutilised.

(Para 8.5 and 8.5.1)

Hiving off of Maintenance Repair and Overhaul and ground handling business to subsidiaries

TAP envisaged the hiving off activities of Maintenance Repair & Overhaul (MRO) services and Ground Handling services to subsidiaries by January 2012.

Hiving off activities of MRO to Air India Engineering Services Limited (AIESL) and Ground Handling to Air India Air Transport Services (AIATSL) were achieved only on 1 January 2015 and 1 April 2014 respectively, after considerable delay.

(Para 9.1)

AIL inaccurately reported to the Oversight Committee (August 2013) that employees of AIL performing ground handling activities had been transferred to AIATSL, even though, all staff continued to be on the rolls of AIL with actual transfer of payrolls for AIATSL taking place w.e.f. April 2014. Similarly AIL informed (August 2014), that both AIESL and AIATSL had been operationalised by February 2013 even though, AIATSL could be operationalised only by April 2014 and AIESL by January 2015.

(Para 9.2)

AIL was to provide a total equity of ₹375 crore to AIESL during the first three years commencing from the date of operationalisation of AIESL. Likewise, AIATSL was to be provided an equity of ₹393 crore, of which ₹150 crore was to be infused in the first year. However, AIL did not infuse this equity towards capital expenditure in AIESL and AIATSL (March 2016).

(Para 9.3)

M/s Boeing had committed to invest upto USD 100 million for establishing and operating a facility in India dedicated to provide maintenance and logistics services as a part of the purchase agreement signed in December 2005. As per the original agreement, the MRO facility was to be operational by August 2009. However the facility was completed only in January 2014 and operationalised in August 2015.

(Para 9.4)

Consequent to the purchase of new Boeing aircraft fitted with GE engines, AIL decided to set up GE branded GEnx and GE 90 overhaul facility at Nagpur. The facility was to be operational by 2013. The facility was still under construction and was expected to be fully operationalised only by December 2017. Due to delay in completion of overhaul facility, AIL had to pay higher amounts to GE for engine overhaul services. The avoidable amount incurred by AIL over January 2013 to March 2016 on this account was ₹ 64.75 crore.

(Para 9.4)

Integration of IT Systems

TAP had envisaged integration of Central Planning and Control System (CPCS) and Flight Planning System (FPS) with the existing Passenger Service System (PSS) and RAMCO Systems. The CPCS, comprising Network Planning and Control System (NP&S), System for Operations and Hub Control (HCC-OCC) and Crew Management System (CMS) were to be procured and implemented before Commonwealth Games beginning in October 2010.

AIL was not utilising three out of the five modules of NP&S (a component of CPCS) despite their implementation as early as in May 2010-July 2010 though, it was paying the monthly recurring System Usage and Support fee for these. AIL failed to arrange for vital input data and skilled man-power necessary for optimum utilisation of Profit Manager, in time. AIL also failed to calibrate the Profit Manager System necessary for a meaningful output. This rendered the expenditure incurred on the procurement of input data, infructuous**.**

(Para 10.4 - A and B)

AIL did not insist on Performance Bank Guarantee (PBG) in the contract for Data Services, Sales and Network Analyzer Module required for utilisation of Profit Manager. Therefore, no penalty could be imposed on the service provider for non-performance, eventually leading to the termination of the contract. AIL also did not make adequate efforts to develop and retain trained manpower for complete utilisation of the sophisticated NP&S Tools.

(Para 10.4 - C)

The Crew Management System (CMS), a key component of CPCS, to be implemented by Commonwealth Games October 2010, was yet to be implemented by the contracted solution provider forcing AIL to adopt an alternate inferior solution as an interim measure. The delays were attributable to absence of timely follow-up by AIL and penalty clause for delays in the Contract.

(Para 10.5)

There had been a significant delay in the implementation of FPS and a corresponding delay in accrual of substantial savings in terms of fuel cost.

(Para 10.6)

Operational Performance

Cabinet Committee on Economic Affairs (CCEA), as well as Master Restructuring Agreement (MRA) had fixed milestones for operational efficiencies to be achieved by AIL by 2015.

Though AIL achieved the overall milestone for Passenger Load factor and network Yield, it did not meet individual target in respect of B-777-200 LR and B-787-800 fleet.

(Para 11.1 and 11.2)

AIL was to achieve an overall On Time Performance (OTP) of 85 *percent* in 2012-13 and 90 *percent* by 2013-14. However till 2015-16, the target of 85-90 *percent* in OTP had not been achieved. Moreover, OTP of AIL had been lower as compared to the other domestic carriers at Delhi and Mumbai airports both in 2014-15 and 2015-16. While AIL had recorded the lowest OTP for Mumbai, it was the second lowest performer for Delhi.

An OTP analysis (as per delay codes) for 50 *percent* of the domestic AIL flights in the Delhi-Mumbai-Delhi (domestic) sector (2014-15), revealed that 23 *percent* of the delay in Delhi and 26 *percent* of the delay in Mumbai airport was entirely attributable to AIL. Another 20 *percent* to 30 *percent* of the delay could also have been partially controlled by AIL. Further OTP analysis of 50 *percent* of flights with lower OTP operating to major international destinations from Delhi and Mumbai airports, revealed that nearly half the delays were within the control of AIL. Similarly for 2015-16, 19 *percent* of the delays in Delhi and 23 *percent* of the delays in Mumbai were entirely attributable to AIL. In addition 26 to 38 *percent* of the delays could have been partially controlled by AIL. Further in International sector (Ex-Delhi and Ex-Mumbai) nearly one-third of the delays were entirely within the control of AIL alongwith another one third of the delays which were partially controllable. Action by the airline could, thus, improve the OTP significantly.

(Para 11.3)

The percentage of rescheduling of flights within three days of flights increased after 2013-14. In significant number of cases the reason recorded for rescheduling was "Miscellaneous". Audit studied the actual reasons for rescheduling in case of Ex-Delhi flights and Ex-Mumbai flights. In respect of Ex-Delhi flights 59.78 *percent* and 65.66 *percent* of the reason for 2014-15 and 2015-16 respectively were within the control of AIL. In respect of Ex-Mumbai flights 62.65 *percent* and 67.28 *percent* of the reasons for 2014-15 and 2015-16 respectively were within the control of AIL. Moreover no mechanism existed in AIL to monitor/control rescheduling of flights.

(Para 11.5)

Recommendations:

(i) As a result of the considerable erosion of the benefits of financial restructuring due to high volume of short term loans of AIL, the value of which was nearly four times the cash credit limits laid down in the Turnaround Plan–Financial Restructuring Plan (TAP-FRP), the Company and the Ministry may need to reassess the requirement of fund envisaged in the Plan.

(ii) Monetisation of assets which failed to take off in the four years ended 31 March 2016 should be fast tracked. Efforts should be taken to ensure that assets identified for monetisation had proper title deeds and the lease agreements did not contain any limiting provision/conditions impacting their monetisation.

(iii) Considering the acute shortage of narrow body aircraft faced by the Company, the process of leasing additional A-320 aircraft should be expedited. All efforts should be made to eliminate abnormal grounding of aircraft. Considering the significant expenditure of the airline on lease rent (for leased aircraft) and finance cost (for owned aircraft) for the period the aircraft were grounded, effective action should be taken for optimising the stock of spares, parts, components and serviceable engines required for repair and maintenance of the acquired fleet. Utilisation of aircraft, particularly the narrow body aircraft should also be improved to meet targets prescribed in TAP and contribute to higher revenues for the airline.

(iv) The Company should focus on recovery of total cost of operation rather than variable cost alone for an effective turnaround for the airline. Rationalisation of routes should be continued. Concerted efforts should be made for maintaining and improving the market share of the airline, particularly on routes where the presence of AIL has been traditionally strong.

(v) The recommendations of Justice Dharmadhikari Committee on harmonisation and rationalisation of staff costs should be implemented by AIL in letter and spirit. The excess manpower compared to the standard force fixed by the Company needed to be

rationalised and the practice of hiring of temporary manpower should be reviewed. The crew should be optimally utilised and their availability should be aligned to the station of their operation to address crew shortages leading to poor On Time Performance, re-scheduling, cancellation of flights. AIL should also rationalise costs on Staff on Duty travel, related allowances and hotel expenses in positioning the staff.

(vi) The IT application Central Planning and Control System, should be fully implemented expeditiously. Efforts should be made for development and retention of trained manpower for operating these sophisticated IT systems.

(vii) Systems should be put in place for better coordination of crew and more efficient maintenance of aircraft so that delays, re-scheduling and cancellation of flights were minimised.

(viii) Since equity commitment of Government of India (GoI) is specific to identified purposes, equity releases of GoI should be adjusted to match the reduction of loans of AIL guaranteed by GoI and the lower interest liability on non-convertible debentures issued by AIL.

(ix) Considering the significant equity funds committed by GoI to AIL, a decision regarding grant of additional bilateral rights to foreign carriers should take into consideration its impact on AIL, as recommended by the Public Accounts Committee of Parliament in its 93rd report (2013-14).


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