A STUDY OF MERGERS AND ACQUISITION IN THE INDIAN AIRLINE INDUSTRY: A CASE STUDY OF ACQUISITION OF AIR INDIA BY TATA SONS

Harsha Vispute, BA LLB, D.E.S. Shri Navalmal Firodia Law College, Pune

ABSTRACT

The Indian aviation market is growing rapidly, and M&As are a preferred method for entry into domestic markets. Domestic airlines also enter into M&As to increase their market share. Mergers and acquisitions aim to achieve greater financial strength for both companies involved. This leads to companies becoming financially stronger, more productive, and more efficient together. Businesses in the aviation sector consolidate to reap benefits such as increased access to capital, better bargaining power in the market, lower costs resulting from high-volume production, and more.

The civil aviation industry in India has emerged as one of the fastest-growing industries in the country during the last few years. It is also one of the most challenging sectors because it is very difficult to maintain a strong holding on a significant portion of the total market share, many big airline companies failed to do so. The Indian aviation industry has recovered fully from the covid-19 pandemic shock as indicated by the air traffic movement which stood at 327.28 million in FY23 compared to 188.89 million in FY22.

Air India was acquired by the Tatas in January 2022. It had last acquired aircraft in 2006. The airlines negotiated the deal for over one year and finally settled on an order that would cater to all segments.

The objective of this case study is to analyze the process of acquisition of Air India by Tata Sons and the strategic decision to acquire Air India, delving into the underlying motivations, the potential economic implications, and the broader impact on the Indian aviation industry.

Keywords: Mergers and Acquisitions, Profitability, Leverage, Liquidity, Capital Markets

INTRODUCTION

Air India, once celebrated as the nation's flagship carrier, encountered significant challenges during the 21st century. These included enduring financial losses, operational inefficiencies, and intense competition within the global aviation landscape. However, it has faced numerous challenges, including regulatory hurdles, intense competition, and the impact of global events such as the COVID-19 pandemic. Despite these hurdles, Air India has maintained a pivotal role in facilitating India's connectivity with the world, albeit grappling with operational inefficiencies and financial instability over recent years.

Tata Sons, a leading Indian conglomerate with historical ties to aviation through Tata Airlines (which later became Air India), saw an opportunity to revive the struggling airline.

Air India, an airline fully owned by Tata Sons, via its fully owned subsidiary, Talace Private Limited ("Talace)", had acquired 100% stake in Air India on 27th January 2022.

BACKGROUND

Jehangir Ratanji Dadabhoy Tata started Tata Air Services, which was eventually renamed Tata Airlines in 1932 and became a public limited company.

The Air Corporations Act was passed in 1953 by the Indian government in order to purchase a majority stake in the airline carrier from Tata Sons.

Later, when the aviation industry was opened up to private competition in 1994, six major private airlines entered the market: Jet Airways, Air Sahara, Modiluft, Damania Airways, NEPC Airlines, and East-West Airlines.

Frivolous attempts were made in 2000-01 to privatize Air India. Furthermore, these low-cost carriers began to eat into Air India's market share. To address this rivalry, the then UPA government chose to merge Air India and its domestic business, Indian Airlines, into a single entity which was accomplished in 2006. The plan was to use the assets and capital pooled together to accelerate expansion.

However, after merging with Indian Airlines in 2006, the company began to lose money. This is due to the fact that, prior to the merger, the ministry had spent close to 67,000 crore on 111 new wide-body planes, following the merger, the merged company employed about 30,000 people.

According to government estimates, the airline lost about 570 million (US$7.6 million) as a result of extra commissions approved by Michael Mascarenhas, the company's then-managing director. In 2006–07, Air India and Indian Airlines lost a total of $7.7 billion (US$100 million), which increased to 72 billion (US$960 million) after the merger in March 2009.

By March 2011, Air India had a debt of 426 billion rupees (US$5.7 billion) and an operational deficit of 220 billion rupees (US$2.9 billion) by March 2011. The government was being sued for $429 billion (US$5.7 billion). The government decided to offer Air India approximately Rs 30,000 crores in equity capital over ten years. Lately, Air India had a total debt of 61,562 crores as of August 31.

In 2017, the government announced its plans to sell the national carrier after it suffered recurring losses, particularly following a gigantic cash crunch. The airline hasn’t made a profit since its merger with Indian Airlines in 2007. For the financial year ended on March 31, 2017, it reported a net loss of around Rs10,000 crore.

MOTIVATIONS BEHIND THE ACQUISITION

1. **Strategic Re-entry:** The acquisition allowed Tata Sons to re-enter the aviation market after having lost control of Air India nearly 70 years prior. This move holds sentimental value and strategic significance for the Tata Group, which already has stakes in other airlines like Vistara and AirAsia India.

2. **Market Positioning**: By acquiring Air India, Tata Sons aimed to strengthen its position in the Indian aviation sector, making it the second-largest domestic airline operator in the country. This acquisition provides access to a significant number of aircraft, trained personnel, and valuable airport slots, enhancing Tata's operational capabilities.

3. **Revitalization Potential**: Tata Sons has a reputation for successfully turning around struggling enterprises. The group’s commitment to improving Air India’s service quality and operational efficiency is seen as a critical factor in the airline’s potential revival.

PROCESS OF ACQUISITION OF AIR INDIA BY TATA SONS

1) As part of the acquisition agreement, the Tata Group has assumed responsibility for approximately 25% of Air India's total debt. Additionally, Tata has committed to maintaining at least a 51% stake in the airline and retaining its 12,000 employees for one year. The agreement also includes a business continuity clause, which requires Tata to adhere to certain operational standards for a period of three years. Furthermore, Tata has the right to use the Air India brand for five years as part of the deal.

2) Air India has been sold to Tata Sons for ₹18,000 crore as the conglomerate outbid the consortium led by SpiceJet's chief Ajay Singh. Tata Sons will now pay ₹2,700 crore in cash to the government and take over the remaining debt of ₹15,300 crore. The reserve price first set by the government at ₹12,906 crore was calculated as a weighted average of the business valuation and asset valuation.

3) Air India's debt had swelled to a huge Rs 61,562 crore as of August 31, 2021, mostly funded by sovereign guarantees to cover its losses. As of March 31, 2021, the airline had accrued losses of Rs 70,820 crore.

4) Following the agreement, The Tata Sons holding company Talace Pvt Ltd will take over ₹15,300 crore and the remaining ₹46,262 crore will be transferred to Air India Assets Holding Limited (AIAHL).

5) The VVIP planes that carry the President and Prime Minister will retain their Air India One call sign but their management and maintenance will be handed over to the Indian Air Force.

6) Air India employs a total of 12,085 people. There are 8,084 regular employees and 4,001 contract employees. Air India Express employs 1,434 people.

   They have to stay with the Tatas for a year. They must be retrenched through a voluntary retirement arrangement if they are retrenched. In the next five years, almost 5,000 people will be forced to retire. Employees may be fired for poor performance or part of a disciplinary procedure.

7) While the Tatas have complete control over Air India, they must adhere to a business continuity clause.

8) They will also be required to keep the brand for a period of five years. They can sell it after that, but not to a foreign corporation.

STRATEGIES TATA SONS IMPLEMENT POST-ACQUISITION TO IMPROVE AIR INDIA'S SERVICES

Tata Sons implemented several strategic initiatives post-acquisition to enhance Air India's services and operational efficiency. These strategies focus on restructuring the airline's operations, improving customer experience, and integrating it with existing Tata aviation ventures.

1. **Fleet Modernization**:
   Tata Sons prioritized upgrading Air India's fleet to improve service reliability and efficiency. They negotiated a significant order for 470 aircraft, including wide-body and narrow-body planes, to cater to both domestic and international markets. This modernization aims to enhance fuel efficiency and reduce operational costs, addressing the challenges posed by Air India's aging fleet.

2. **Integration with Existing Airlines:**

   The consolidation of Air India with Vistara, a joint venture between Tata Sons and Singapore Airlines, is a critical strategy. This merger aims to create a robust airline capable of competing effectively in both domestic and international markets. The combined fleet of 218 aircraft positions the new entity as a leading carrier, enhancing operational synergies and expanding market reach.

3. **Service Quality Improvement**:
   Tata Sons launched a comprehensive 100-day improvement plan focusing on enhancing service standards. This includes revamping customer service protocols, improving on-time performance, and ensuring a consistent and high-quality passenger experience. The goal is to restore Air India's reputation as a premium airline and attract a loyal customer base.

4. **Operational Efficiency**:
   The management has implemented measures to streamline operations, including optimizing crew scheduling and improving aircraft utilization. These initiatives aim to reduce operational costs and increase profitability, addressing the historical inefficiencies that plagued Air India.

5. **Customer Experience Enhancement**:
   Tata Sons is committed to transforming Air India's customer proposition. This involves revamping the in-flight experience, enhancing safety measures, and improving overall customer engagement. The focus is on delivering a world-class experience to passengers, which is crucial for regaining market share.

6. **Financial Restructuring**:
   Addressing Air India's substantial debt is a priority. Tata Sons is working on a financial restructuring plan that includes leveraging existing assets and seeking strategic partnerships to stabilize the airline's finances. This approach aims to create a sustainable business model for the future.

AIR INDIA'S 100-DAY IMPROVEMENT PLAN

The Tata Group's 100-day improvement plan for Air India focuses on overhauling service standards and enhancing operational efficiency. Key aspects include:

- Service Overhaul: A complete revamp of Air India's service standards is essential, with significant investments planned to elevate the brand's reputation.

- Immediate Concerns: The plan addresses critical areas such as on-time performance, call center efficiency, and the swift resolution of passenger complaints.

- Organizational Changes: A large committee has been formed to enhance services, alongside senior-level hiring in human resources to foster synergies within the airline.

- Leveraging Experience: Tata's partnership with Singapore Airlines through Vistara provides valuable experience in delivering premium services, which will be applied to Air India.

- Financial Commitment: The Tata Group will manage ₹15,300 crore of Air India's ₹61,562 crore debt and pay an additional ₹2,700 crore in cash to the government, although the overall disinvestment does not significantly advance the government's financial goals.

- Long-term Investment: The acquisition is viewed as a long-term investment by Tata, driven by both emotional ties and the potential for profitability through improved management.

Overall, the plan aims to restore Air India's standing in the aviation market while minimizing the government's role in its operations.

ANALYSIS OF THE FINANCIAL/PHYSICAL PERFORMANCE REVENUE:

1)Total Revenue declined from Rs.134,793.8 million last year to Rs.134,022.7 million (reduction of Rs.771.1million).

ii) Operating Revenue for the year was Rs.131,086.2 million against previous year's revenue of Rs.132.245.2 million (reduction of Rs.1,159.0 million). The reduction in the revenue was on account of

a) Drop in yields coupled with global recession;

b) Reduction in other revenue due to policy on bi-lateral and ground handling.

REVENUE BREAKDOWN 2019-20

EXPENDITURE BREAKDOWN EXPENDITURE:

i) The total expenditure incurred during the year was Rs,190,358.3 million as compared to the previous year's figure of Rs.206,680.1 million (a reduction of Rs.16,321.8 million).

ii) Operating Expenses declined by Rs.23,157.8 million mainly due to the following: Decrease in fuel price by Rs.19060 million i.e. 29% Reduction in leasing charges due to return of leased fleet by Rs.2072.9 million i.e. 15% Savings on account of implementation of fuel gap efficiency analysis by Rs.1100 million,

iii) Reduction in booking agency commission by Rs.276.8 million: Reduction in aircraft maintenance cost by Rs.177.1 million However, the above reduction in expenditure was offset by increase in other costs

iv) viz.: Increase in depreciation, obsolescence and amortization charges by Rs.1115.9 million i.e. by 9% due to induction of new aircraft; Increase in interest on aircraft loans by Rs.2420.4 million Le. by 63% due to induction of new aircraft Increase in interest on working capital borrowings by Rs.5220.3 million Le. by 43% due to increase in borrowing rates and working capital limit; Increase in handling charges by Rs.754.9 million due to cost of operations via Frankfurt.

ANALYSIS OF REMARKABLE OUTCOMES OF THE ACQUISITION:-

1. **Return of the prodigal son:** The airliner returns to its original owners after 90 years. It holds a great sentimental value for Ratan Tata, who believes that this acquisition will help the group strengthen its hold on the industry and it will bring back the glory of its past.

2. **Leaders in domestic space:** On the business front, the Tata group already has a strong presence in the industry, with a majority stake in AirAsia India and a joint venture with Singapore Airlines named Vistara Airlines. This deal will make it the second largest domestic carrier in India.

3. **Lucrative airline real estate:** The Tatas will further have access to over hundred planes, thousands of trained pilots and crew. Plus it will get 4400 domestic and 1800 international landing and parking slots in India apart from the 900 lucrative parking slots worldwide (including Heathrow).

4. **Substantial Overlaps:** The transaction will result in significant overlaps in horizontal, and non-horizontal relevant markets. Vistara and AirAsia, subsidiaries of Tata Sons, operate in international and domestic passenger air transport on nine and ninety-one overlapping origin-destination routes respectively with the Target. After the fruition of the transaction, Vistara and AirAsia will also share business with the Target in international and domestic cargo services, charter flight services and ground and cargo handling services. With respect to vertical/complementary relationships, AISATS provides ground handling services to airlines at the Bengaluru, Hyderabad, Delhi, Thiruvananthapuram and Mangalore airports, while AirAsia India provides passenger air transport services in all these airports and Vistara provides passenger air transport services at all these airports except Mangalore airport. AISATS provides cargo handling services to airlines at the Bengaluru airport, while Vistara and AirAsia India provide passenger air transport services at the Bengaluru airport. Taj SATS and its wholly-owned subsidiary Taj Madras provide in-flight catering services to airlines in India, while Air India and AIXL provide passenger air transport services in India.

5. **Plummeting Competition in the Aviation Industry:** S20(4) lays down the factors, which the

CCI shall have due regard while determining whether a combination would have an AAEC in the relevant market. This section seeks to analyse the Tata- Air India combination through the lens of the factors mentioned in s20(4) of the Act.

6. **Changing Market Composition in the domestic market:** In 2021, the domestic passenger air traffic market share for Air Asia and Vistara was 13.2% and for the Target was 12%. The total market share of Tata-Air India enterprise will be 25.2% [in reference to s20(4)(h)]. The combination along with the three major competitors [Indigo (54.8%), Spice Jet (10.5%) and Go Air (8.8%)] occupies more than 99% of the market share. The current composition indicates a highly concentrated market, which becomes more obvious in a comprehensive HHI analysis. An HHI of 2500 or greater is indicative of highly concentrated market. In this market, even before acquisition, the HHI was of 3509, which implies very low competition. As a general rule, mergers or acquisitions that increase the HHI between 100- 200 points in highly concentrated markets raise antitrust concerns, as they are assumed to create barriers to entry for potential competitors [s20(4)(b)] and to increase the likelihood drive out the existing competitors [s20(4)(c)]. Hence, this acquisition will exacerbate anti-competitiveness in the market and will drive the market towards a more oligopolistic structure.

7. **Explicating Ripple Effect:** The incident of Tata-Air India enterprise occupying a share of more than 25% in the domestic passenger traffic market, has consequences and ramifications beyond this market. A larger share enables the combination to exercise significant influence in other relevant markets. For instance, it enables Tata Sons to secure favourable ground handling and in-flight catering service contracts. Another relevant example is that the transaction will provide Tata Sons control over 22% share in the domestic cargo air transport market instead of the previous acquisition share of 13%. This will provide Tata Sons an upper-hand in the cargo handling services, thereby creating unfair hardships for existing enterprises providing similar services.

8. **Aggravating factors:** The dominance in market share will enable Tata Sons to acquire the benefits of economies of scale. However, the anti-competitive impact of the transaction does not stop at the effects of the increased market share. The peculiar features of the aviation industry enable the acquisition to be an extremely powerful tool for driving out potential competitors. Consequent to the transaction, Tata Sons will enjoy the benefits of 'grandfathering rights' in slot allocation and public barriers to entry in the aviation sector.

In the aviation industry, time slots allotted to airlines to take off and land from an airport, while also granting access to other airport infrastructure and traffic rights or travel routes between destinations, constitute critical assets. In India, the Airports Authority of India and the DGCA allot slots in accordance with the IATA guidelines. Under the policy of grandfathering rights, the historical precedence of the allocated slots is maintained, if the slots in question have been utilised by the passenger airliner to whom they were allocated at least 80% of the time during the last season. This deprives the new airlines of securing slots during peak times in prestigious airports, which in turn, reduces the outreach of their services. By the virtue of 'grandfathering rights', when airlines merge, the merged entity retains all the slots that the airlines had access to before the merger. Consequently, Tata Sons will gain access to Air India's over 4,400 domestic slots and 1,800 international slots, which will enable it to expand its service base exponentially.

India's Civil Aviation Requirement (CAR) Section 3, in Parts II and III, mandates that a scheduled service operator that applies to provide services using aircraft with a takeoff mass of 40,000 kg or more must purchase or lease a minimum of five aircraft with start-up equity requirement of Rs. 50 crores. Additionally, as an airline's fleet grows in increments of up to five planes, equity requirements grow by Rs. 20 crores. These requirements are aimed at ensuring that the new entrants to the airlines market are financially viable, but they impose very high burdens on potential entrants who already have to incur huge fixed costs. These public barriers to entry provide additional leverage to Tata Sons to operate independently of competitive forces prevailing in the relevant market.

CONCLUSION:

Tata Sons' acquisition of Air India represents a historic reconnection to India's aviation legacy and a strategic move to expand its presence in the industry. While offering advantages like potential synergies, increased market presence, and global reach, the deal also presents substantial financial, operational, and regulatory challenges. Tata's success will depend on effectively addressing these issues, streamlining the airline's economy, and positioning it competitively in the dynamic aviation landscape.

This case study provides insights into strategies employed by key players to navigate market complexities, offering valuable lessons for the broader aviation industry and businesses facing similar global challenges.

Tata Sons has initiated consolidation of its airline entities Vistara, AirAsia India, and Air India Express under Air India, following discussions with Singapore Airlines (SIA), its Vistara joint venture partner. The move will make Air India the country's second-largest airline by fleet and market share. The group will have a low-cost carrier and a full-service airline under Air India, which will be the sole airline brand post-merger.

REFERENCES:

1. Tata Sons. Tata Sons Acquires Air India. Press Release. (November 19, 2022 10.30 AM), https://www.tata.com/press-releases

2. Air India Acquisition by Tata Sons. BusinessNews.com. (November 19, 2022 11.32 AM). https://www.businessnews.com/air-india-tata-acquisition.

3. Air India - Tata Sons Deal. (n.d.). FinancialReview.com. (November 19, 2022 11.00 AM). https://www.financialreview.com/air-india-tata-deal

4. Tata Group regains Air India's ownership after seven decades. Hindustan times. (November 19, 2022 9.30AM) https://www.hindustantimes.com/india-news/tata-group-finalisesdeal-to-regain-air-india-s-ownership-after-seven-decades-101643283895717.html