

Maharaja Returns to the Tata Group: Disinvestment of Air India

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Summary

In a landmark decision announced by the Indian government on 8 October 2021, the Tata Group's bid for the state carrier Air India has been approved. Though there were attempts to privatise the airline since 2001, none met with any success. The merger of Air India and Indian Airlines in 2007 complicated issues further with the merged entity running up losses and a huge volume of debt. Faced with mounting demands on the state exchequer and dissatisfaction in the functioning of the airline, the government decided to finally bite the bullet and divest its entire stake in a flexible and well-structured deal. The success of this deal will infuse great confidence among bidders in the ability of the government to deliver clean and timely contracts in other divestment proposals.

Introduction

On 8 October 2021, the Indian government announced a landmark decision to sell its entire stake in Air India as well as Air India's stake in two other businesses – Air India Express and Air India SATS Airport Services. The scope of the sale includes 100 per cent of the government's stake in Air India, 100 per cent of the airline's shareholding in low-cost airline Air India Express Limited and 50 per cent in Air India SATS Airport Services Private Ltd. The monetisation of the other state-owned regional carrier, Alliance Air, a fully-owned regional subsidiary, which is a part of the Air India Asset Holdings, is also on the anvil as a part of the government's asset disposal programme. Alliance Air was carved out of Air India after government decided to divest Air India's stake. The Letter of Intent has been issued and the Share Purchase Agreement is expected to be signed by 20 October 2021.

Remarkable Political Will

The disinvestment of Air India was a huge challenge. The fact that disinvestment has been achieved when the sector is going through severe COVID-19 pandemic related issues, is a sign of the strong political will and single-minded dedication of the government to see the process through. The **privatisation of Air India** is a message from the government to the markets and global investors that it has the political will to bite the reform bullet. Its demonstrative effect gets amplified because Air India was always a hard sell, given its colossal losses and debt despite continuous infusion of funds.

This marks the first major outright privatisation of a public sector company in almost two decades. The encouraging feature of this process has been the realisation among employees and political parties that Air India, as a public sector entity, was no longer sustainable. The cost of keeping the entity operational was costing the exchequer far too much and the

treasury could no longer sustain that cost. On the other hand, the pragmatism shown by the government this time in tweaking the modalities of the divestment process to make it attractive for bidders, sends an unambiguous message, of its determination to push forward with the privatisation agenda.

Tata Sons back in the Cockpit

Tata Sons will regain control of Air India as it takes over 100 per cent of the government's stake in the national carrier, marking the end of a protracted struggle to sell the airline and the first step in the Centre's mega privatisation push. The former owner of Air India placed a winning bid of ₹18,000 crore (S\$3.39 billion), of which ₹2,700 crore (S\$1.83 billion) will be paid in cash and the remaining ₹15,300 crore (S\$3.12 billion) will be absorbed from the over ₹60,000 crore (S\$12.21 billion) debt the airline had as of 31 August 2021. The transaction is expected to close by the end of December 2021.

Ratan Tata, Chairman Emeritus of the Tata Group, has been bold in his acquisitions. He has been aggressive in acquiring high profile global brands despite the challenges involved in those acquisitions. The bidding process and competition for brands such as Corus Steel and Jaguar Land Rover were rather intrepid calls in the face of global competition. Acquiring Air India has also been an emotional call for the Tata's since the airline was so rudely taken away from them 68 years ago. The acquisition was all the more daunting in the face of the challenges facing the aviation sector today. However, it is widely believed that a professionally run organisation like the Tata Group will be able to turn around the ailing airline and help it establish its brand among global airlines.

Nationalisation of Air India

Air India owes its birth to the Tata Group in 1932. In 1947, as India gained Independence, the government bought 49 per cent stake in the company. In 1953, in what was termed as a cruel blow to J R D Tata since he had so carefully nurtured Air India, the government nationalised the company. In recognition of his expertise of the aviation sector and close association with the airline, J R D Tata was appointed Chairperson of Air India. However, in yet another blow to the ageing Tata patriarch, in 1977, the-then Janata Party government dropped him from the boards of both Air India and Indian Airlines. Despite the shake-up, the nationalised Air India was professionally run and soon established itself as a leading carrier in the field of aviation. It was in 2001 that the-then government decided against state participation in civil aviation. It tried to reduce the government's stake by 40 per cent in the airline. However, for varying reasons that attempt could not be successfully executed.

In 2007, in what was ostensibly mooted as an attempt to reduce the losses of the domestic carrier, Indian Airlines, it was merged with Air India. That merger was most unprofessionally executed, with both airlines in the red. The merged entity remained constantly in financial difficulty and had to be supported from the national exchequer as it continuously made losses. Since 2009-10, the government has spent over ₹1 trillion (S\$20.34 billion) to bridge the losses. As of August 2021, Air India's debt was ₹61,562 crore (about S\$13.56 billion).

The next attempt to divest the entity was made in 2018. Under false notions of continuing its hold in the organisation, the government's proposal was to divest only 76 per cent of its stake. Naturally, there was no buyer since bidders were wary of the government continuing to have its finger in the pie. It was finally in 2020 that government took a pragmatic and flexible approach in deciding to divest the entity fully. The government agreed to retain part of the debt, since in all previous attempts prospective bidders were discouraged by the huge debt burden that the airline had built up.

The Sale Arrangement Now

In the present sale arrangement, of the total debt of ₹ 61,562 crore (S\$13.56 billion), the Tatas will take over a debt of ₹15,300 crore (about S\$2.71 billion). The remaining ₹46,262 crore (S\$17.63 billion) will be transferred to a Special Purpose Vehicle (SPV), Air India Assets Holding Ltd. The SPV houses Air India's assets and liabilities. The assets include office space and ground handling and engineering arms and Alliance Air, the regional arm. The sale of building and other assets is expected to fetch around ₹14,000 crore (S\$2.58 billion).¹

Air India has 12,085 employees of which 8,084 are permanent, and 4,001 contractual. In addition, Air India Express has 1,434 staffers. In the next five years, about 5,000 permanent employees will be retiring. After one year of takeover by the Tata's, employees of Air India can be offered a voluntary retirement scheme (VRS). The VRS liability will be funded by the Tata Group. The government will pay ₹1,300 crore (about S\$2.44 billion) towards clearing the dues of employees.² As a part of the sale condition, the Tata Group cannot transfer the Air India brand or logo for five years and, thereafter, can do so only to an Indian entity.

The Tata Group had evinced interest in acquiring the airline on several occasions earlier, including partnering with Singapore Airlines (SIA) in 2001, but the bid was withdrawn. In 2015, the Tata Group launched an airline in a 51:49 joint venture with SIA. The Tata Group also holds 83.67 per cent stake in the low-cost airline AirAsia India. Industry sources believe that with Air India under its umbrella again, the Tata Group could consolidate its airline operations.

Revenue Realised from the Disinvestment

Looked at from the standpoint of revenues gained by government in the disinvestment, the deal does not contribute anything substantial. However, it is an important landmark in the evolution of the country's economic policy, as it was a complex exercise which has been managed as an open, transparent and competitive bidding process. The decision will be a fillip for future privatisation proposals because bidders will get more confidence in the government's capacity to close complex transactions. The process was carried out over a nine-month period, despite multiple obstacles, with the bureaucracy showing uncharacteristic alacrity in decision making.

¹ "Ready for take off: Tata Group retakes Air India, makes Rs 18,000-crore winning bid for national carrier", *Financial Express*, 9 October 2021, <https://www.financialexpress.com/industry/ready-for-take-off-tata-group-retakes-air-india-makes-rs-18000-crore-winning-bid-for-national-carrier/2346763/>.

² Ibid.

The fact that the Tata Group has credibility in the industry and an otherwise clean reputation seems to have helped in the processing of its bid. It was also a very decisive and bold decision by government to divest its stake totally and not to try and retain partial stake holding as had been done in its previous attempts. It is natural for any private entity to have reservations in taking on the government as a partner specially with the entity having a huge overhang of debt and the typical employee culture of a public sector enterprise. It was also very practical on the part of government to realise that bidders in the past had been daunted by the debt-ridden company and unless the government was willing to meet part of that debt, the proposal would have not attracted genuine bidders. While working on the Air India deal, the government must have finally realised that shutting down the airline was the only option if the current bid failed.

Benefits to the Tata Group

The Tata Group has a wide global net of operations. Its software and information technology (IT) solutions are functional in about 100 countries around the world. After its acquisition of Jaguar Land Rover and Corus Steel, its footprint has been established in sectors other than IT. The group has also set up a defence manufacturing facility in which it has international collaborations with aircraft and defence hardware producing companies in the United States and Europe. With the addition of Air India, its portfolio will be enhanced. The acquisition gives the Tata Group access to 1,800 international landing and parking slots at domestic airports and 900 slots at airports overseas. This is in addition to 4,400 domestic slots and 141 aircrafts. Air India has in its fold over three million frequent fliers.³ The acquisition of Air India will thus give the Tata conglomerate a very substantial boost to its national and international network of operations.

In its earlier bid for acquisition of the airline, its overseas partner, SIA had expressed reservations. In the present bid by the Tata, SIA appears to have cooperated which may just be an indication that the two airlines may merge their Indian operations to further enhance their reach.⁴ This will provide Air India and the Tata Group a major upgrade in their portfolio. Air India's market share as in August 2021 was 13.2 per cent.⁵ If Air Asia, Vistara and Air India were to merge, they would get 26.7 per cent of the domestic passenger market, thereby offering stiff competition to the domestic market leader, Indigo Airlines.

Way Forward for the Government

Purely in terms of meeting its disinvestment revenue target for the current year, the Air India divestment deal does not contribute a substantial amount. As of 7 October 2021, against a target of ₹175,000 crore (S\$36.62 billion), the achievement was only ₹9,111 crore (S\$1.63 billion). Last year too, the divestment target could not be met. As against the ambitious target of ₹210,000 crore (S\$42.04 billion), the realisation was only ₹32,847 crore

³ Press Trust of India, "Government issues LoI to Tatas for sale of Air India", *The Indian Express*, 11 October 2021, <https://indianexpress.com/article/india/govt-issues-loi-to-tatas-for-sale-of-air-india-7566645/>.

⁴ Pranav Mukul, "Tata Sons wins bid for acquiring national carrier Air India", *The Indian Express*, 9 October 2021, <https://indianexpress.com/article/business/aviation/tata-sons-wins-bid-for-air-india-government-7545472/>.

⁵ Ibid.

(\$5.42 billion).⁶ The low realisation in the previous year could be attributable to the COVID-19 pandemic. However, the present deal serves as a huge confidence booster to the officials of the Department of Investment and Public Asset Management (DIPAM) and the government.

The department has learnt a great deal from the Air India sale and can confidently complete divestment of other companies. In future deals, both the bidder and the government will derive confidence since an interest from many bidders will result in increased competition. Bidders will be attracted by the fact that the government has been able to deliver along the timelines, a complex deal as that of Air India. While there can be no standard template for a divestment process; yet having successfully concluded this deal will send a very positive signal to investors seeking to participate in other such disinvestment proposals. It is also encouraging to see government officials not being deterred by the fear of investigative agencies reopening the deals for later scrutiny. Quite often, the fear of the auditor or the Central Bureau of Investigation has been trotted as a proxy for non- performance. The present team has set to rest any such bogey by ensuring a transparent process which has been scrutinised and validated by multiple agencies.

The DIPAM has a challenging agenda before it for the balance of the current fiscal as it has multiple programmes for divestment running concurrently. Financial bids are slated to be invited soon for Bharat Petroleum Corporation Ltd, Pawan Hans, Bharat Earth Movers Ltd and Shipping Corporation of India. Much to its credit, the government has, in the last few months, taken several bold decisions such as corporatising the ordnance factories, providing guarantee to the bad bank⁷ and shown willingness to convert its revenues receivable from telecommunication companies into equity, which indicate to its resolve to meet with all the policy pronouncements made by it.

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⁶ Union Budget, Department of Investment and Public Asset management, <https://dipam.gov.in/>.

⁷ “Explained: The arguments for and against a bad bank”, Sunny Verma and George Mathew, *The Indian Express*, 14 October 2021, <https://indianexpress.com/article/explained/npa-bad-bank-balance-sheet-loan-rbi-shaktikanta-das-7151841/>.