

INDIAN AVIATION INDUSTRY

Grounding of aircraft pose near-term challenges; large aircraft orders endorse long-term growth potential

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Although the aviation industry has witnessed healthy recovery in passenger traffic with better pricing discipline, supply-chain challenges and engine failure issues have emerged as headwinds for the sector as 24-26% of the industry fleet is likely to be grounded by March 2024.

Total current aircraft order book is close to double the current fleet in operations. However, ICRA expects the demand-supply balance to be maintained in the medium to long term.



▪ **The outlook for the Indian aviation industry remains Stable**, given the fast-paced recovery in domestic passenger traffic and relatively stable cost environment. At an estimated 150-155 million, ICRA expects the domestic air passenger traffic to surpass pre-Covid levels in FY2024. International air passenger traffic for Indian carriers had already exceeded pre-Covid levels in FY2023 and is likely to surpass the peak of FY2019 in the current fiscal.



▪ **The industry has witnessed improved pricing power**, as reflected in the improved yields and the spread between revenue per available seat kilometer – cost per available seat kilometer (RASK-CASK) for the airlines. The same is expected to remain favourable aided by the decline in aviation turbine fuel (ATF) prices (down 15% in YTD FY2024 on YoY basis) and the relatively stable foreign exchange rates.



▪ **However, the Indian aviation industry has lately been affected by engine failure issues and supply chain challenges**. This has resulted in the grounding of at least 154 aircraft for select airlines, thus impacting overall industry capacity (as measured by available seat kilometer or ASKMs), affecting nearly ~20-22% of the total industry fleet as on September 30, 2023. The recent powder-coating related concerns in engines are expected to result in additional grounding of aircraft in Q4 FY2024. This implies that ~24-26% of the industry capacity will be grounded by March 31, 2024, thus affecting the industry's ASKMs.



▪ **The grounding is likely to result in higher operating expenses**, attributed to increased charges and a surge in lease rentals due to substitute aircraft being taken on spot leases to offset the affected capacity. This, coupled with lower fuel efficiency (due to replacement with older generation aircraft), will adversely impact the airlines' cost structures and may result in an increase in air fares. However, mitigation in the form of healthy yields, high load factors and extent of compensation available from engine suppliers would help absorb the impact to an extent.



▪ **At present, the Indian aviation industry has a total order book of ~1,700 aircraft**, which is more than double the size of the current fleet in operation. The deliveries, however, are likely to be gradual, spanning over the next decade, and will also be impacted by the current supply chain challenges encountered by aircraft and engine OEMs. However, ICRA expects the demand-supply balance in the industry to be maintained in the medium to long term aided by improvement in air travel penetration levels.



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