PHD CHAMBER

PROGRESS HARMONY DEVELOPMENT

Estd. - 1905

Saurabh Sanyal
Secretary General

FT-15-CA
Dated: May 23, 2016

Secretary
Airports Economic Regulatory Authority of India,
AERA Building, Administrative Complex,
Safdarjung Airport,
New Delhi- 110 003

25/5 O.I.D. AGM(RKG) 25/5

Subject: Consultation Paper No. 10/2015-16 dated 16th March 2016 issued by Airports Economic Regulatory Authority of India (AERA) for Determination of Aeronautical Tariff in respect of Chhatrapati Shivaji International Airport Mumbai, for the second Regulatory Period (01.04.2014 - 31.03.2019).

Respected Madam,

May I take this opportunity to briefly introduce PHD Chamber of Commerce and Industry, a proactive and dynamic multi-State 111 year old apex organization Chamber, working at the grass-root level and with strong national and international linkages. The chamber's members constitutes of over 1800 corporates, comprising of Large, medium and small scale enterprises as its direct members and around 200 associations as indirect members serving around 45,000 members.

We are constantly in touch with the policy makers and regulators across the country and are extensively involved in the recommendations for policy formulations of the country and our views are best sought after by various ministries and policy makers in the country. The private airports sector in India is in its nascent stage and requires consistent and forward looking regulatory decisions to enable airports to grow, develop and be economically viable. The Tariff should therefore be adequate to enable airport operator become viable and be able to generate sufficient funds that would be required for future expansion and modernization.

Accordingly, we wish to submit the following issues to the Authority for their consideration on behalf of our members.

1. **Cost of Equity:**

AERA has proposed return on equity at the rate of 16% which is significantly lower than what was sought by MIAL i.e. 23% for the second control period and needs to be revisited by AERA considering the following facts.

a. It is understood the Authority had engaged NIPFP to estimate the cost of equity for Airports in India. We understand the methodology adopted by NIPFP for determination of cost of equity for Airports has several flaws. These methodologies have been criticized by many experts. Considering such a flawed report for determination of cost of equity may not be giving a positive signal for the potential investors in the sector apart from negative impact on all Major Airports.

b. It would be important to consider that studies done by various other experts and agencies including Government appointed agency SBI Capital Market have given a range of 18.5% to 24% for return on equity for Airport sector.

PHD CHAMBER OF COMMERCE AND INDUSTRY
PHD House, 4/2 Siri Institutional Area, August Kranti Marg, New Delhi - 110 016 (India)
Tel. : +91-11-2686 3801-04, 49545454, 49545400 • Fax : +91-11-2685 5450
E-mail : saurabh.sanyal@phdcci.in • Website : www.phdcci.in • CIN NO :- U74899DL1951GAP001947

c. Risk profile and traffic volatility is much higher for the Airport sector compared to other similar infrastructure sectors. Return on equity in other sectors such as power, port, roads etc. is ranging between 15.5 to 18%. However, the difference between these sectors and the Airport is that in these sectors return is given on the amount of equity infused by the investors while in the case of Airports the return is given on the value of asset base (RAB) which is subject to depreciation every year.
In effect this means that 16% return proposed by AERA will be decreasing every year as RAB depreciates every year and for a concession period of 30 years 16% return on equity proposed by AERA would translate to a return far below 16% which is grossly inadequate and will discourage any further investment in the sector by the prospective investors.

d. DIAL & MIAL are liable to pay AAI a huge revenue share (46% & 38.7% respectively) of its gross revenues including a return on equity and therefore a 16% return on equity proposed by AERA will in effect result in a return which is much below the reasonable return expectation of the investors.

e. Authority may kindly consider a cost of equity of 18.5 % to 24 % as submitted by SBI Caps in their study, as they are a reputed Govt. entity with specialized knowledge and vast experience on the subject matter.

2. **<u>Return on Real Estate Deposits used for Project Funding:</u>**

AERA has proposed Zero return on real estate deposits proposed to be utilized for project funding by MIAL which according to us needs reconsideration by the Authority on account of the following:

a. While structuring the transaction for lease of commercial land airport operators forgo a part of annual lease rentals in favor of upfront RSD. These funds have an inbuilt opportunity cost since if deposits are not to be collected for project, it would result in lease rental becoming high.

b. These funds have all characteristics similar to that of equity considering very long tenure of these deposits and taking into account the fact that lenders have considered these deposits as quasi equity. For all purposes, these deposits should be considered similar to equity and accordingly appropriate return should be given.

c. We understand that private Airports utilize the security deposit as a means of finance since no other sources were available. For funds available through other sources such as debt or equity AERA would have given cost of debt or equity and therefore assuming that these deposits have zero cost is not in line with international practices as these funds have implicit cost.

d. Tariff Authority for Major Ports (TAMP) and Petroleum and Natural Gas Regulatory Board (PNGRB) sets tariff following the cost + return on capital employed approach. Capital employed is calculated by adding net fixed assets and working capital. These regulators do not consider the source of funding of the project while calculating return and allows return on all kind of capital employed including security deposits at a uniform rate of 14 to 16%. We are of the opinion that it will be completely unfair to Airports if no return is provided on these deposits.

e. Authority to kindly consider providing return on RSD commensurate with the return on equity.

We thank the Authority for providing us this opportunity to highlight our key concerns in the Consultation Paper. We expect that the Authority will consider our concerns highlighted above while determining the aeronautical tariff for all major private Airport.
We hope our suggestions will be considered favorably in the interest of the long-term viability of the airport sector, incentivizing the private investors to invest into the sector and being able to offer world class services to passengers.

Yours Sincerely

Sanyal

Saurabh Sanyal
Secretary General