MENZIES AVIATION

18th August 2023

Director (P&S, Tariff)
Airports Economic Regulatory Authority of India (AERA)
AERA Administrative Complex
Safdarjung Airports
New Delhi - 110003.

Dear Sir,

Sub: Submission of responses on Consultation Paper No. 06/2023-24 dated 28 July 2023

Kind reference is invited to the Consultation Paper No. 06/2023-24 dated 28 July 2023 in the matter of determination of tariffs for Cargo Handling Services for Menzies Aviation (Bengaluru) Private Limited (MABPL) at Kempegowda International Airport (KIA), Bengaluru for the first control period beginning from FY 2023-24 to FY 2027-28.

We thank the Authority for finalizing the Consultation Paper of Cargo Handling Services for Menzies Aviation (Bengaluru) Private Limited for the first control period.

As part of the stakeholder consultation process for the referenced consultation paper, we are sharing with you our responses for the kind consideration of the Authority.

The tariff determination exercise is vital for the viability of MABPL operations in a competitive cargo market at BIAL. MABPL humbly requests the Authority to apply a consistent regulatory framework for its cargo tariffs.

It is requested that the Authority may determine the final tariffs of the first control period only after taking into consideration our above submission on the Consultation Paper, as there are considerable market dynamic changes post of our MYTP Submission.

Committing to the continued support and cooperation with the Authority,

Thanking you.

Yours faithfully,

Venkata Reddy Kunam

Head of Projects – India

Menzies Aviation (Bengaluru) Pvt. Ltd. ★

Enclosures:

1. MABPL's response to the Consultation Paper
2. Menzies Aviation response to the Consultation Paper
3. **Menzies Aviation letter on the CHQ expenses of MABPL (Confidential)**

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Submission of MABPL's responses on Consultation Paper No. 06/2023-24 dated 28 July 2023

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As part of the stakeholder consultation process for the referenced consultation paper, please find below the comments of MABPL for the kind consideration of the Authority:

1) Traffic forecast for the first control period

A. Proposal of AERA:

Para 3.3.1 of the CP no. 06/ 2023-24 for the first control period of MABPL – Chapter 3: *"Cargo Volume Projections:*
Based on the material before it and its analysis, the Authority proposes to consider the Cargo Volume projections for the MABPL for the First Control Period as per Table 4.

B. MABPL's proposal:

i. MABPL thanks the Authority for considering and approving our proposal with respect to Cargo Volume Projections.

Traffic forecast methodology as per MYTP

ii. At the time of submission of the cargo forecast for international traffic, MABPL had based its cargo volume forecast on the following:

a) Assumption of 50% market share for MABPL in international cargo traffic, excluding cold chain and express/ courier cargo.

b) Historical trends in traffic handled by the incumbent cargo operators (AISATS and MABB)

Revised traffic forecast based on actual volumes.

iii. After submission of the MYTP in March 2023, both cargo operators started their operations from 24th May 2023 onwards. MABPL had approached the international airlines to enter into the SGHA cargo services contracts. As per the competitive market for cargo services at KIA, all the international airlines have chosen between the two cargo operators.

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iv. MABPL would highlight to the Authority that the term of SGHA contract for cargo handling services is a minimum of 3 years while in some cases, the term can be up to 5 years (MABPL has submitted to the Authority the SGHAs it has signed with the international airlines as part of its responses to Authority's queries). Therefore, the airlines have a fixed contract for 3-5 years for their cargo operations at BIAL. Thus, the market share of MABPL as of date in the international cargo traffic, excluding cold chain and express/ courier cargo, will not change substantially during the control period.

Hence, MABPL humbly requests the Authority that the cargo traffic forecast should be based on the actual market share of MABPL as of today. This approach will ensure an accurate estimation of the traffic forecast for MABPL.

v. Further, the MYTP forecast was based on the historical trends in traffic of the incumbent cargo operators (AISATS and MABB), which is no longer relevant since the actual traffic for the initial months with the respective market share is available to determine the future traffic forecast.

Revised traffic forecast of MABPL for the first control period

vi. The actual traffic of MABPL for the first two months of the operations is given in the table below:

Particulars	June 2023	July 2023
International cargo traffic handled by MABPL (MT) (A)	**9,602**	**8,359**
Percentage change (Drop) from June 2023	**-**	**-13%**
Annualised traffic based on this monthly international cargo traffic (MT) (A*12)	**1,15,224**	**1,00,308**

vii. As can be seen from the table above, the traffic has reduced by ~13% in the month of July when compared to the month of June. The decrease in international traffic is due to a large international carrier shifting its cargo handling operator from MABPL to its competitor from 1st July 2023 onwards. The share of the cargo carried by this international carrier in total international traffic of MABPL was ~19% (~21,600 MT annually).

viii. We have attached a regret letter issued from the large customer for the consideration of the Authority (confidential letter and request the authority not to be disclosed in the public domain).

ix. For MABPL, the loss of this key customer has resulted in a significant impact in terms of its traffic handled. Further, MABPL has limited opportunity to grow its international airline customer base during the control period as all the international airlines have entered long-term SGHA's with either of the two cargo operators, as stated earlier.

x. Therefore, based on the actuals, MABPL proposes the following traffic forecast for the first control period:

Particulars	FY24*	FY24 (annual)	FY25	FY26	FY27	FY28
International cargo traffic handled by MABPL (MT)	84,833	100,308	106,326	112,706	119,468	126,637
Growth rate (%)			6%	6%	6%	6%

** for the period from 24 May 2023 (COD) till 31 March 2024*

xi. MABPL would highlight that its traffic forecast proposed for the first control period is still higher than the traffic forecast approved for its competitor, which had also assumed a 50% market share as stated in para 3.5.2, implying that the traffic assumptions of MABPL are more pragmatic for the same cargo market.

xii. This revision in the international cargo traffic forecast is critical for MABPL as the existing traffic forecast will result in the Authority's assumption of high revenue and lower tariff increase, translating into a significant reduction in profitability for MABPL.

xiii. Accordingly, MABPL requests the Authority to revise the cargo traffic forecast of MABPL for the first control period as per the table above.

2) Base Personnel Cost excluding Corporate HQ cost for FY24 and annual escalation in personnel cost proposed by the Authority.

A. Proposal of AERA:

Para 5.4.1 of the CP no. 06/ 2023-24 for the first control period of Menzies Aviation – Chapter 5: *"Operating & Maintenance Expenditure:*
However, as the ISP is operating in a competitive environment and to attract new customers, ISP must exercise cost controls in all of its operating expenditures, including payroll costs, to maintain viable operations. In this regard, the Authority notes that though as per the ISP, its payroll cost structure is based on the erstwhile operators' payroll structure; however, onetime upliftment in the salaries of all employees up to 25% proposed during the first tariff year and higher Y-o-Y % increase in payroll (16%) considered by the ISP for the first Control Period will increase the payroll expenses significantly.
The Authority, while working out payroll expenses for the first tariff year as per the above table, has considered normal annual escalations in payroll expenses @ 10% p.a. for FY 2021-22 & FY 2022-23. In respect of the FY 2023-24 (first tariff year), the Authority has considered 35% overall increase in the payroll costs over the previous year, which has been worked out considering 10% increase for annual
increments in salaries, 10% towards one time upliftment in the average salaries (as against 25% proposed by the ISP) for all employees and 15% increase in the payroll expenses due to the projected increase in number of manpower on account of commissioning of new domestic cargo terminal building & increase in the projected cargo volumes.

B. MABPL's proposal:

i. The payroll expenses need to provide fair compensation to various personnel that handle the day-to-day operations at the cargo terminal.

ii. The annualized base cost of INR, 57.60 cr. for FY24 estimated by MABPL, was done so while keeping in mind the hyper-inflationary environment between FY21-FY23, market standards, the zero-compensation growth in FY20 and the competitive talent market.

iii. MABPL firmly believes in delivering quality service and hires the workforce with the right skill set to maintain its operations. The one-time upliftment of 10% provided by the Authority needs to be revised to compensate the employees for zero appraisal in the Covid year and to retain and maintain the region/industry salary standards to ensure the optimum functioning of the cargo terminal.

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MABPL submits that due to the unique set-up of their Cargo Terminals at the Bengaluru Airport, wherein the international and domestic cargo terminal operations would be divided between two terminals located 2 km apart, MABPL would require dedicated staff at each terminal for efficient functioning as cross-utilization of manpower and equipment is not practically feasible. Therefore, MABPL would request the Authority to allow the annualized base cost of INR 57.60 cr. for FY24.

iv. Further, MABPL would highlight to the Authority that MABPL's average salary per employee is lower than the market average. The table below shows a comparison between expenses per employee at MABPL and GHAC, Hyderabad:

GHAC	Ref. (Order no. 04/ 2023-24)	2024	2025	2026
Payroll cost (INR cr.)	**Table 16**	**36.63**	**41.99**	**48.05**
Employees	Table 14	710	750	790
Average salaries (INR lakhs)		**5.16**	**5.60**	**6.08**

MABPL	Ref.	2024 (annualized)	2025	2026
Payroll cost (INR cr.) (Excluding CHQ Cost)	Table 14 of MYTP document	57.6	66.7	77.4
Total payroll cost (INR cr.)		**57.6**	**66.7**	**77.4**
Employees	Table 13 of MYTP document	1487	1569	1659
Average salaries (INR lakhs) (Excl CHQ cost)		**3.87**	**4.25**	**4.66**
% difference from GHAC		-25%	-24%	-23%

v. MABPL would also like to point out that the personnel cost has been considered by the Authority for the period from 24 May 2023 (which represents the actual date of handover of operations from MABB to MABPL) to 31 March 2024. However, MABPL would highlight to the Authority that for a smooth handover and transition, it would require adequate advance planning and preparation. Accordingly, MABPL had proposed that around 110 employees will be on its roll from 1st April 2023 onwards instead of 24 May 2023. Accordingly, MABPL would request the Authority to consider the payroll costs from 1st April 2023 onwards.

vi. MABPL would also like to draw Authority's attention to clause 5.7.5 of Order No. 13/2023-24 released on 09/08/2023 in the matter of 'Determination of Tariff for WFS Private Limited providing Cargo Handling Services at Kempegowda International Airport, Bengaluru for the First Control Period'. The Authority has analyzed and noted that despite considering an annualized payroll expenses of INR 67.6 cr for FY24 inclusive of the INR 10 cr. for the intercompany expenses, MABPL's employee expenses per MT of cargo handled is almost 19% lower than that of its competitor. This shows the level of efficiency with which MABPL has built its workforce and also the cost-cutting measures that are a result of having a centralised support system (discussed in the next point).

5.7.5 Notwithstanding the above, if payroll costs of the service providers is to be compared, then the comparison should be between the services providers in the comparable situation, for instance ISPs operating at same airport, under the similar terms & conditions as per the similar concession agreements. Accordingly, the Authority has compared the payroll costs of the WFSBPL with the other cargo service provider at the Bengaluru airport namely MABPL, who has also been awarded cargo handling concession by the same

airport operator (BIAL) at Bengaluru airport. Further, both cargo terminal operators have commenced their commercial operations at Bengaluru airport on the same date i.e., 24.05.2023. The Authority, from its comparative analysis notes that WFSBPL's projected payroll cost per MT of cargo in FY 2023-24 is much higher when compared with its peer at Bengaluru airport, as tabulated below:

Particulars	WFSBPL	MABPL#
Cargo Volumes (MT)	119587	246875
Total Projected Annualized Payroll Costs by the ISP (₹ in crores) for FY 2023-24	40.12	67.60
Employee cost per MT of Cargo (in ₹/ MT)	**3354.88**	**2738.23**

Figures as per CP no. 06/2023-24 dt. 28.07.2023 for MABPL

The payroll cost pertaining to other service provider in the above table includes their corporate headquarters' cost allocation. The Authority, based on the above comparative analysis draw inference that the other service provider is operating with higher employee productivity as compared to WFSBPL. The Authority expects ISPs to optimize and bring efficiency in their operating costs, so as to maintain a competitive edge.

vii. Based on the rationale provided above, MABPL requests the Authority to allow the annualized base cost of INR 57.6 cr. for FY24 and, consider the payroll cost from 1 May 2023 onwards.

3) Personnel CHQ cost of the Third Control Period

A. Proposal of AERA:

Para 5.4.1: *"The Authority notes that MABPL has projected a CHQ' cost allocation at ₹ 10.00 crores in FY 2023-24, thereafter an increase of 5% Y-o-Y basis. In this regard, the Authority observes that ISP has not submitted calculations for the allocation of CHQ cost for the MABPL and basis for the proposed YoY escalation therein. Further, it is observed that ISP has made CHQ's cost allocation a part of its projected payroll expenses, where normal annual escalation is 10%, as against 5% in HQ's cost proposed by the ISP.*

Considering the above, the Authority has segregated the MABPL's CHQ's costs allocation from its projected Payroll costs and proposes to rationalize it at ₹ 3 crores in FY 2023-24. However, the Authority proposes the consider the annual escalation in the CHQ's costs allocation @5%, as proposed by the ISP."

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B. MABPL's proposal:

i. MABPL strongly recommends the Authority revisit its treatment of the CHQ costs.

ii. Menzies group operates cargo stations in more than 60+ Countries and serves more than 250+ airports globally. To ensure efficiency, quality, and consistent global policy at each of these 250+ airports globally in a highly cost-effective manner, Menzies Group has formed a centralised support system. That's because deploying a local support team at each airport that performs the same functions would obviously result in a higher overall cost when all airport stations across the globe are combined. However, the central spine of all the operations needs to compensate through a reasonable fee from the subsidiaries for providing these services. The CHQ costs are allocated on an equitable basis across all airport stations.

iii. For MABPL to work efficiently, the CHQ provides services with respect to its employees with subject matter expertise, Enterprise Resource Planning (ERP) software, a global reporting system - OneStream, cargo handling manuals and other standard operating procedures. In addition to these, the CHQ provides cargo training modules relating to AvSec, dangerous goods, valuable cargo etc., for the on-site staff whose certification is required as per aviation regulatory agencies.

iv. The CHQ provides these services as a package to MABPL, and thus, it is very difficult to provide the break-up of the cost for each of the services. However, MABPL has undertaken an exercise to determine the cost it will incur if it procures these services individually to determine the cost savings on an overall basis to compare it with the CHQ costs.

S. No.	Cost Heads	Resulting Cost Savings per year
1	ERP	INR 4.0 cr. One-time implementation cost and recurring/license fee of 50 Lakhs per annum if procured locally, resulting in cost savings of INR 1.3 cr. Per year with amortized ERP cost
2	IT related expenses/Time and Attendance software	INR 1.5 cr., if procured locally
3	Staff with subject matter expertise, key accounts managers,	INR 4 cr. consultancy/ new employees cost for the subject matter expertise provided by CHQ
4	Global reporting system Onestream	INR 0.5 cr. if procured individually
5	Training Modules/Trainers/SOPs	INR 1.5 cr., if procured locally
6	Cargo Manuals, Corporate Training Modules,	INR 1.5 cr., if procured locally

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S. No.	Cost Heads	Resulting Cost Savings per year
	Total	**INR 10.30 cr per annum (After amortizing one time cost of ERP)**

v. As seen from the table above, the cost savings for MABPL with respect to these services, if procured locally/ individually, is more than the cost charged by CHQ, justifying the cost-effective nature of the CHQ services.

vi. MABPL submits to the Authority that the proposed CHQ costs charged by the parent company will be on an arms-length basis in compliance with the transfer pricing regulations in relation to such transactions. Therefore, the CHQ costs proposed by MABPL are reasonable.

vii. Further, MABPL has submitted a letter from the headquarters (confidential and not to be shared in the public domain) justifying the CHQ cost and providing the benchmarks across its subsidiaries in India. MABPL would highlight that the CHQ cost proposed is in line with its subsidiaries.

viii. On the comparison of the payroll cost with its competitor, the Authority has itself established that even after considering a cost of INR 10 cr., the total payroll expenses, including CHQ costs, are significantly lower than that of its competitor per ton basis showing efficiency in MABPL's payroll costs (refer 'Point iv of MABPL's Proposal on Payroll Expenses').

ix. MABPL would also request the Authority to allow an annual increment of 10% instead of the 5% for the CHQ cost considering the annual escalation, payroll revision and cost of inflation.

x. Based on the above, MABPL requests the Authority to allow the annualised CHQ costs at INR 10 cr. in FY24 with annual increment of 10% over the control period.

4) Repairs & Maintenance expenditure

A. Proposal of AERA:

Para 5.4.3: *"Further, the Authority has included the all-inclusive, comprehensive maintenance charges (AICMC) for five years costing around ₹ 5.15 crores in respect of the International Material Handling System under the Repair and Maintenance costs from FY 2025-26 onwards (after two years of defect liability period), which the ISP has considered as CAPEX for FY 2023-24. The Authority has spread ₹ 5.15 crores AICMC in the five tariff years, starting from FY 2025-26, at an annual charge of ₹ 1.03 crores. This is resulting in a steep increase in R&M Costs in FY 2025-26 by @ 30%.*
In view of the above, in order to rationalise R &M Costs of the ISP, the Authority proposes normal annual escalation in R&M Expenses @ 7% p.a. as against the 15% YoY increase proposed by the ISP for the First Control Period."

B. MABPL's proposal:

i. MABPL has proposed the escalation in the R&M expenses based on the following:

   a. We are in an inflationary phase globally. Hence, the cost of parts of the equipment sourced from India as well as imported from other countries, are expected to increase on account of the inflation in addition to the labour and service costs.

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b. Due to the rapidly changing technology landscape and cybersecurity concerns, MABPL anticipates changes to the security requirement from BCAS from time to time and has assumed the same in the proposed escalation in the R&M costs.

c. MABPL believes in thorough preventive maintenance, which is cost-effective in the long term from savings in the capital expenditure or high R&M cost in one year. This cost has been considered while proposing the escalation in R&M costs.

d. MABPL would also highlight that in addition to the above factors, the equipment will be catering to a year-on-year increase in the cargo traffic, which will result in additional R&M cost.

ii. Furthermore, if viewed from the perspective of total RAB (after excluding the security deposit), the total R&M cost is much lower than the 6% benchmark the Authority has approved for other airports. This is, in part, attributed to the newness of the equipment, as rightly pointed out by the Authority, but also is accredited to the standard operating procedures and manuals created by the MABPL CHQ, which, through the rigorous experience of multiple airports, has been able to devise workflows in a way to maximize the utility of each equipment and component of the Cargo Terminal's infrastructure.

iii. Reducing the R&M costs to a 7% YoY escalation effectively reduces it to a real increase of less than 2% YoY as the Authority has cited an inflation of 5.1% in its recent orders. As the control period progresses, the real increase of ~1.9% in R&M costs will be unreasonable, especially considering the base figure of INR 3.50 cr. in FY24 to be so low (on account of new infrastructure).

iv. MABPL would also like to draw the Authority's attention to the fact that while a large chunk of infrastructure is new, certain assets are being inherited from the previous cargo operator. At this point, the valuation of assets is underway, and the same will be submitted in due course of time. It is essential that this factor must not be ignored that old / existing asset will demand a higher R&M cost, and normalizing it with the supposed R&M cost on new assets is unfair.

v. MABPL would further like to point out clause 5.7.8 of Order No. 13/2023-24 released on 09/08/2023 in the matter of 'Determination of Tariff for WFS Private Limited providing Cargo Handling Services at Kempegowda International Airport, Bengaluru for the First Control Period'. While being on a similar scale and level as MABPL in terms of the newness of assets, the Authority has approved a higher (11%) R&M cost escalation in the second half of the control period.

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5.7.8 The Authority notes the comments of M/s SpiceJet regarding Repair & Maintenance costs and the response thereon by the ISP. The Authority observes that the WFSBPL has proposed major CAPEX on the refurbishment of International Cargo Terminal (CT2), Cold Chain Facility (CCF) and on the procurement of new cargo handling equipment/systems. Considering that the major renovation & restoration of the cargo infrastructure at a significant CAPEX is already being undertaken by the service provider. In addition, new equipment/ systems are also being procured by the ISP.

The Authority feels that as the new equipment & material handling systems etc. are generally under the warranty for first few years; similarly, cargo infrastructure which is being renovated/ restored must also be under the defect liability period/ warranty period. Hence, the R&M costs are expected to be comparatively lower during the initial tariff years of the Control Period. Though, as the equipment ages, due to higher wear & tear, R&M expenses during the later part of the Control Period may be higher. Therefore, the Authority decides to consider Y-o-Y increase in R&M Expenses @ 7% for initial two tariff years (FY 2024-25 and FY 2025-26) and @ 11% p.a. from FY 2026-27 onward.

Accordingly, the Authority has computed the revised R&M Expenses for the First Control Period of ISP as tabulated below:

Table 21: Revised Repair & Maintenance Costs considered by the Authority for the ISP in respect of the First Control Period

(₹ in crores)

Particulars	FY 2023-24 (10 months only)	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28	Total
R & M Cost (ii)	6.77	8.69	9.30	10.32	11.46	46.55
YoY% Increase	-	7%	7%	11%	11%	

vi. Accordingly, MABPL requests Authority to consider 15% y-o-y escalation in the R&M cost.

5) Total Operating Expenses

A. Proposal of AERA:

Para 5.4.7: *"Based on the review and analysis of Operating Costs projected by the ISP, the Authority proposes to consider OPEX for the First Control Period as per Table given below:"*

The table below illustrates the operating expenses for FY24 (annualized base year) as submitted by MABPL and as proposed by the Authority:

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Particulars (INR cr)	First Control Period Total as submitted by MABPL	First Control Period Total as proposed by the Authority	Difference (INR cr)
Payroll and Other Staff Expenditure	390.63	348.60	42.03
Corporate HQ Cost	55.30	16.14	39.16
Administrative & General expenses	286.80	286.80	0.00
Repairs and Maintenance	26.98	26.02	0.96
Utilities cost	24.89	24.89	0.00
General Expenses	0.00	1.50	-1.50
Revenue Share payable to Airport Operator	335.75	313.83	21.92
Total O&M expenses	**1120.35**	**1017.77**	**102.58**

B. MABPL's proposal:

i. MABPL would like to draw Authority's attention to clause 8.5.5 of Order No. 13/2023-24 released on 09/08/2023 in the matter of 'Determination of Tariff for WFS Private Limited providing Cargo Handling Services at Kempegowda International Airport, Bengaluru for the First Control Period. The Authority has stated that the two operators – MABPL and WFSBPL have been awarded similar concessions by the same airport operator (on similar conditions) and hence, MABPL would like to cite the comparison between the two as stated by the Authority since the two are comparable.

ii. MABPL's opex per MT, when considered as is (as per the MYTP submission) is substantially lower (~56%) as compared to its counterpart WFSBPL. The comparison between the proposed expenses by MABPL and those approved for WSFBPL show that the proposed structure by MABPL is competent, efficient and best in the market. Since the Authority verifies WFSBPL's costs, MABPL will therefore like to reiterate its request of allowing the proposed expenses by MABPL:

   a. Base Personnel Cost for FY24 at INR 57.6 cr.
   b. CHQ cost at INR 10 cr
   c. Payroll costs being approved from 1 May 2023
   d. CHQ costs annual growth rate at 10%
   e. Escalation in R&M costs of 15% y-o-y

6) Treatment of Security Deposit by the Authority

A. Proposal of AERA:

Para 5.4.5: *"The Authority notes that as per SPRHA, ISP is required to pay ₹ 50 crores of interest-free refundable Security Deposit to the Airport Operator for the concession period. In its MYTP submission, ISP has proposed a Security deposit as a part of its RAB. As regards to Return on Interest-Free Security Deposit, the Authority proposes to consider 5% Return per annum, as per the AERA's consistent*

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approach in this regard. Accordingly, the Authority proposes excluding SD from the RAB of the ISP for Aggregate Revenue Requirement (ARR) Calculations."

B. MABPL's proposal:

i. MABPL would highlight to the Authority that the funds infused in the project for security deposit have been raised at a much higher rate than 5%.

ii. In an ideal scenario where funds for any purpose have been raised at the Fair Rate of Return (FRoR) determined by the Authority, the return on those funds should match the same.

iii. In the event of funds that are raised at FRoR, which generate an annual return of 5%, it would be a net loss-making proposition for MABPL.

iv. Therefore, we request the Authority to provide a return on the security deposit in line with the FRoR so as to fairly compensate the shareholders of MABPL.

7) Cost of Equity and Impact on Fair Rate of Return as computed by the Authority

A. Proposal of AERA:

Para 7.3.3: *"The Authority notes that ISP has considered a cost of equity at 21%. However, the ISP hasn't submitted proper justifications thereof. The Authority, following its consistent approach regarding the Cost of Equity for ISPs, proposes to consider the Cost of Equity @ 14% for the First Control Period. As regard to cost of debt, the Authority proposes to consider the cost of debt at 9.5% p.a., as proposed by the ISP. However, the Authority will revisit the issue of the cost of debt at the time of finalising the Tariff Order for the ISP, considering the actual debt availed etc. and other relevant information.*

In view of the foregoing, the Authority proposes to consider FRoR @ 12.01% for the computation of ARR in respect of MABPL for the First Control Period.

B. MABPL's proposal:

i. MABPL has noted that the Authority has treated MABPL's cost of equity while maintaining consistency across cargo operators.

ii. However, MABPL's case cannot be treated similarly to other cargo operators.

iii. The Authority itself has deemed cargo operations at BIAL to be 'Competitive'. The Authority has also acknowledged the need for caution and cost-cutting measures in order to sustain. These factors combined inculcate a higher degree of risk for MABPL, thereby warranting a higher project beta and subsequently, higher cost of equity, as investors would seek a higher return to compensate for the additional risk.

iv. Therefore, normalizing MABPL's cost of equity with other cargo operators is not ideal. Instead, compensating investors with a higher rate of return – to the tune of 21% would be apt. This has been arrived at using the standard CAPM method as illustrated below:

$$CoE = R_f + \beta \times ERP$$

Where Rf denotes the risk-free rate, ERP denotes the country-specific equity risk premium (net of risk-free return), beta denotes the project risk and any other associated risks (such as liquidity risk, risk of default etc.).

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v. These numbers have been estimated/calculated as follows:

a. **Risk-free Rate in India:** In line with the standard approach in the Indian capital markets, the yield of a 30-year bond has been used to estimate the risk-free rate. The current yield of the 30-year sovereign bond is approximately 7.33%, and the same has been considered by MABPL to estimate the risk-free rate in India.

b. **Global Equity Risk Premium:** In order to understand the risk premium of India, we first need to estimate the global risk premium of the market that is considered the least risky/most developed. For this purpose, we have considered the stock markets of United States of America, as it has the highest rating (lowest risk), largest market capitalisation and significant history with ease of data availability. In the last 95 years (1928-2022), US equity markets have returned 11.51% against 4.87% for treasury bonds. Therefore, the global equity risk premium is estimated at 6.64%*.

c. **Country Risk Premium:** The global equity risk premia needs to be adjusted for the Indian markets, as an emerging market has inherently higher risk than a developed market. To estimate this, we have adopted the standard approach of using Sovereign Credit Spread or Credit Default Swap (CDS) as a proxy. This comes out at 3.79%, bringing the total equity risk premium to 10.43%.

d. **Project Beta:** Estimating the project beta accurately requires stock price data. However, since MABPL is not a listed company, the second approach would be to look at the market average of similar operators from around the world. After rigorous analysis, MABPL has arrived at the conclusion that the cargo operations business carries a higher risk than the broader market average. Therefore, consider the project beta of such cargo operators to be in the range of 1.25 to 1.40 as compared to the broader markets. Accordingly, an average equity beta of 1.31 is considered for computation purposes.

vi. The table below illustrates the calculation of cost of equity as per the estimates above:

Particulars	**Value**
Risk-Free Rate in India (A):	7.33%
Global Equity Risk Premium (B):	6.64%
Country Risk Premium (C):	3.79%
India's Equity Risk Premium (D = B+C):	10.43%
Project Beta estimate (E):	1.31
Cost of equity for the project (A+(E*D)):	21%

vii. With the cost of equity at 21%, and the cost of debt and gearing ratio proposed by the Authority, we arrive at the Fair Rate of Return of 16%.

**Source: pages.stern.nyu.edu/~adamodar/New_Home_Page/datafile/histretSP.html. On an annualised basis, the mean difference in annual returns comes out to be 6.64% over the last 95 years.*

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8) **Valuation of Transfer Assets**

A. **Proposal of AERA:**

Para 4.2.17: *"Considering that ISP is contractually bound to accept the old assets which are transferred by the AO, the Authority proposes to consider the valuation of old assets as proposed by the ISP. However, the aspect of valuation of transfer assets will be revisited by the Authority at the time of finalisation of Tariff Order for the ISP."*

B. **MABPL's proposal:**

BIAL has appointed a certified valuer, which will submit its report within 4 weeks. MABPL will submit the report once the valuation activity is complete. In the meantime, MABPL would request the Authority to consider a tentative valuation (based on an initial assessment) of INR 11 cr.

9) **Domestic Tariff card proposed by the Authority**

A. **Proposal of AERA:**

Para 7.3.8: *"Accordingly, the Authority proposes following an increase in the Tariff rates for the Cargo Handling Services provided by the MABPL at KIA, Bengaluru, over the tariff applicable to the previous cargo operator, for the First Control Period as under:*

Particulars	***FY24***	***FY25***	***FY26***	***FY27***	***FY28***
Domestic cargo Handling Services	*21%*	*21%*	*21%*	*14%*	*14%*

B. **MABPL's proposal:**

i. Before filing the tariffs to the Authority, MABPL had undertaken several stakeholder consultation meetings to understand the market acceptability and address the industry's concerns.

ii. Based on the stakeholder consultation and requirement of sustainable operations, MABPL submitted the proposed tariffs for the first control period.

iii. MABPL would also highlight that several airlines have agreed to the proposed domestic rate card and entered into agreements with MABPL subject to the Authority's approval (signed SGHA's submitted to the Authority as part of the MYTP review process).

iv. The domestic tariffs were proposed to compensate for the investment undertaken by MABPL in developing the new greenfield cargo terminal.

v. **Accordingly, MABPL submits to the Authority that the domestic tariffs in the initial years be increased to at least 35% in FY24 and 32% in FY25 to address the above concerns.**

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10) International Tariff card proposed by the Authority

A. Proposal of AERA: *'Tariff increase proposed to be considered by the Authority for the First Control Period.'*

Particulars	*FY24*	*FY25*	*FY26*	*FY27*	*FY28*
International cargo Handling Services	*15%*	*15%*	*13%*	*10%*	*10%*

B. MABPL's proposal:

i. After thorough evaluation of the Authority's proposed Tariff Rate hike for international cargo handling services, MABPL would like to cite clause 8.5.4 of Order No. 13/2023-24 released on 09/08/2023 in the matter of 'Determination of Tariff for WFS Private Limited providing Cargo Handling Services at Kempegowda International Airport, Bengaluru for the First Control Period'.

Table 36: Percentage increase in tariff considered by the Authority for WFSBPL in respect of the First Control Period

Particulars	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
TSPs (incl. Demurrage Charges)	30%	17%	17%	17%	17%
Airline Fees	15%	8%	8%	8%	8%

ii. MABPL has noted that the Authority has approved different tariff increases for TSPs and Airline fees for the competitor, which is a change of position of the Authority from the consultation paper and other cargo ISPs.

iii. It is imperative to highlight that MABPL and WFSBPL are competitors for International Cargo Operations at KIA.

iv. Airlines negotiate contracts with the cargo operators for the provision of cargo services. There is intense competition between the cargo operators to attract the airlines, and one of the major negotiation points is with respect to the rates offered by the cargo operators. Thus, there is a difference between the Authority's approved rates for airlines and rates charged to the airlines by the cargo operators.

v. Since the Authority has approved a significantly lower rate increase for airline fees for its competitor, MABPL is of the view that the airlines will negotiate with MABPL to offer similar or lower rate as offered by its competitors. In order to attract cargo traffic and survive in the intense competition, MABPL expects that it will be forced to offer similar or lower rates as offered by its competitors to its customer airlines. In case MABPL continues with its uniform tariff increase approach for TSPs and airline fees, then such arrangement will result in significant losses wherein MABPL will not realise the revenue projected by the Authority from airline customers in actuals.

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vi. Being mindful of the above challenges and to survive in the competitive market, MABPL is compelled to request the Authority to offer consistent treatment with respect to the tariff determination approach adopted by the Authority for its competitors.

vii. In that regard, MABPL would request the Authority to allow a lower increase in the airline fees and a higher increase in the TSP charges w.r.t. the tariff increase proposed in the consultation paper such that the international revenues remain the same as shown in the table below:

Tariff increase w.r.t. international cargo fees	FY24	FY25	FY26	FY27	FY28
Proposed by the Authority in consultation paper					
Airline fees and TSPs	15%	15%	13%	10%	10%
Proposed by MABPL					
Airline fees	15%	8%	8%	8%	8%
TSPs	Due to a reduction in the quantum of tariff increase in airline fees, the revenues from airlines will be lower than that assumed in the consultation paper resulting in a shortfall in international revenues. This shortfall in airline revenues is requested to be recovered from an adjustment in the tariff increase for TSPs*. which will be higher than that proposed by the Authority during the consultation paper.				

* *as per the assumptions on ARR finalized by AERA as part of the order*

viii. The same has been done for its competitor, which would reflect consistency on the part of the Authority and the two cargo operators operating at the same airport under similar concession agreements.

11) Tariff rates proposed by the Authority

A. Proposal of AERA: *'Annexure IV: TARIFF PROPOSED BY THE AUTHORITY FOR CARGO HANDLING SERVICES IN RESPECT OF MABPL AT KIA, BENGALURU FOR THE FIRST CONTROL PERIOD FOR STAKEHOLDERS' CONSULTATION'*

B. MABPL's proposal:

After a thorough evaluation of the Authority's proposed Tariff Rates, MABPL would like the Authority to reconsider the following:

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Int / Dom	Import/ Export/ In/Out/ Notes	Airlines/ FF/A/S#	Service	Ref. Page No.	Proposed by the Authority	Proposed by MABPL	Remarks
Int	Import	FF/A/S	Demurrage Charges (General, Special, Valuable/ dangerous)	72	Free period to 120 hours	Free period to 96 hours	Storage for 48 hours Free period prescribed as per Ministry of Civil Aviation and subsequent 48 hours
Int	Import	FF/A/S	Demurrage Charges (General, Special, Valuable/ dangerous)	72	120 hours to 720 hours	96 hours to 696 hours	Period prescribed as per Ministry of Civil Aviation
Int	Import	FF/A/S	Demurrage Charges (General, Special, Valuable/ dangerous)	72	Beyond 720 hours	Beyond 696 hours	Period prescribed as per Ministry of Civil Aviation
Int	Notes	FF/A/S	Point 3	73	'Cross Weight'	'Gross Weight'	Spelling Error
Int	Export	Airlines	PER/ PIL/ TCR	74	3.78*	4.35*	As the existing charge is INR 3.78 per kg, with 15% increase the rate proposed by MABPL was INR 4.35 per kg. Also, SGHA with customer is also signed with the proposed rates (submitted to the Authority). Therefore, MABPL requests the Authority to provide the proposed rate of INR 4.35 per kg in FY24 and adjust the future

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Int / Dom	Import/ Export/ In/Out/ Notes	Airlines/ FF/A/S#	Service	Ref. Page No.	Proposed by the Authority	Proposed by MABPL	Remarks
							year tariffs as per the applicable tariff increase.
Int	Import	Airlines	PER/ PIL/ TCR	75	3.78*	4.35*	As the existing charge is INR 3.78 per kg, with 15% increase the rate proposed by MABPL was INR 4.35 per kg. Also, SGHA with a customer is also signed with the proposed rates (submitted to the Authority). Therefore, MABPL requests the Authority to provide the proposed rate of INR 4.35 per kg in FY24 and adjust the future year tariffs as per the applicable tariff increase.
Dom	Outbound Inbound	FF/A/S	Terminal, Storage and Processing	76	Special Special - AVI	Special/ AVI Special/AVI	Change in both outbound and inbound.
Dom	Notes	FF/A/S	Point 1	77	Export/ Import	Outbound/ Inbound	Export/Import not applicable on domestic routes
Dom	Notes	FF/A/S	Point 1	77	'Cross Weight'	'Gross Weight'	Spelling Error
Dom	Notes	FF/A/S	Point 1 Point 4	77	Export Cargo/ Import Cargo	Replace with Outbound Cargo/ Inbound cargo	Export/Import not applicable on domestic routes

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Int / Dom	Import/ Export/ In/Out/ Notes	Airlines/ FF/A/S#	Service	Ref. Page No.	Proposed by the Authority	Proposed by MABPL	Remarks
Dom	Notes	FF/A/S	Point 4	77	-	Replace with points in remarks.	Storage charges: a. Outbound Cargo-Free period shall be 24 hours from the time shipment deposited by the forwarder/agent/shipper on 'Per Kg Per day'. b. Inbound Cargo-Free period shall be 24 hours from the actual time of flight arrival at 'Per Kg Per Day" basis.
Dom	Transshipment	Airlines	Domestic to Domestic (General/ Special)	79	General: Per kg - 2.54* Min – 204* Special: Per kg - 2.54* Min – 204*	General: Per kg - 3.34* Min – 229* Special: Per kg - 3.34* Min – 441*	Existing charge for INR 2.76 per kg and minimum fee of INR 189/ 364 (General/ Special) (for transshipment) with 21% increase will be INR 3.34 per kg and INR 229/ 441 (General/ Special).

**Note: Charges for base year (FY24). To increase throughout the control period in line with the hikes decided by the Authority.*

Below note to be included in the tariff table and notes

All Export charges for Freight forwards/shippers/agents shall be on per shipping bill/AWB basis

All Import charges for Freight forwards/consignees/agents shall be on per bill of Entry/AWB basis

Menzies Aviation (Bengaluru) Pvt. Ltd.

Thanking you.

Yours faithfully,

Venkata Reddy Kunam

Head of Projects – India

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14th August 2023

Director (P&S, Tariff)
Airports Economic Regulatory Authority of India ("AERA" or "the Authority")
AERA Administrative Complex,
Safdarjung Airport, New Delhi -110 003

Sub: Response to Consultation Paper No. 06/2023-24 dated 28th July 2023

Ref: Determination of tariff for Cargo Handling Services for Menzies Aviation (Bengaluru) Private Limited (MABPL) at Kempegowda International Airport (KIA), Bengaluru for the First Control Period (FY 2023-24 to FY 2027-28)

Dear Sir,

Menzies Aviation Limited (Menzies) has 74% stake in Menzies Aviation (Bengaluru) Private Limited, herein after referred as "MABPL", a joint venture company formed in August 2022 between Menzies Aviation Limited and Bangalore International Airport Limited (BIAL) to provide cargo services at KIAB. MABPL has entered into Service Provider Right Holder ("SPRH") agreement with BIAL on 26th December 2022 to design, build, finance, develop, operate, undertake refurbishment activities, maintain, and transfer the International Cargo Terminal 1 and design, build, finance, develop, operate, maintain and transfer the Domestic Cargo Terminal at BIAL.

Menzies Group is renowned global provider of aviation services, including ground handling and cargo operations. The group's operations span across 60+ countries in 6 continents, serving more than 250+ airports, offering a comprehensive range of service to efficiently manage the movement of goods through air transportation. Menzies group has leveraged upon its strengths with respect to its global network, expertise in cargo operations, efficiency, stringent safety processes, and state of the art technology in the operationalization of MABPL.

Investment of Menzies in MABPL is one of prominence given the large scale of operations and the significant investment committed by it for the facility expansion. The tariff determination exercise undertaken by the Authority is very critical for the business viability of the JV in an intensely competitive market. A fair and consistent regulatory framework is required for the sustainability of the JV. It will also build confidence among the global investors to undertake significant capital expenditure in India while feeling secure regarding the tariff determination framework. Certain proposals in the consultation paper as given below are urged to be revisited by the Authority as these are critical to the financial viability and sustainability of the JV:

1. Uniform rate increases for airlines and freight forwarders.

It has been observed that the Authority has amended its proposal in the final Order no. 13/ 2023-24 dated 9th August 2023, regarding the uniform tariff increase for its competitor and allowed different percentage tariff increase for freight forwarders and airlines. Menzies would highlight that the cargo tariff rates levied to airlines in a competitive market are determined based on RFP/Tender process with each of the airlines subject to cap set by the Authority. Thus, the airline tariff rates are discounted to attract or retain an airline customer. Thus, in a competitive market, we will not be able to charge the airline tariffs rates proposed by the Authority in the consultation paper given that there is significant difference between competitor and our rates. In these circumstances MABPL will not realize the revenues projected by the Authority from the airline rates resulting in lower ROI. Therefore, to accurately estimate the revenues and maintain sustainable operations, MABPL urges and requests the Authority to allow different percentage increase for freight forwarders and airlines (as detailed in the revised proposal submitted by MABPL).

2. Cost of equity

From a global investor's perspective, Menzies would stress upon allowing reasonable cost of equity on its investment to maintain sustainable operations for MABPL. The Authority's proposal of allowing 14% cost of equity on the cargo investment is inadequate for the Indian market. Such low cost of equity will affect the influx of investment in cargo business in India from global large investors. Menzies has taken inherent risks when investing in any of its subsidiaries, especially after COVID-19. A reasonable rate of return compensates investors for these risks encouraging them to invest in these projects. This balance between risk and reward is fundamental to maintaining robust and sustainable investment ecosystem. Allowing a reasonable cost of equity for global investors is not only in best interest of the investors but is also essential for promoting economic growth, job creation, innovation, and sustainability. Therefore, Menzies requests the Authority to allow cost of equity of 21% as per the detailed submission of MABPL.

3. Cost of Personnel

Menzies would highlight to the Authority that, based on Authority's analysis itself, MABPL's personnel costs are significantly lower than our competitor when considered on a per MT basis. Further, rationalizing the costs is not possible on account of the highly skilled work force that MABPL relies upon to perform the required services and maintain adequate service quality. Therefore, Menzies request the Authority to allow INR 57.6 cr. as the annualized base personnel cost for FY24 for MABPL.

Menzies would reiterate the importance of the tariff order from the perspective of MABPL's sustainability and reasonable rate of return to the shareholders who have committed significant investment. The decisions of the Authority are important from the perspective of the attractiveness of India's cargo business to the global cargo players such as Menzies. Therefore, we request the Authority to consider the above aspects while finalizing the final tariff order. The fair and consistent treatment of the Authority to the cargo operators will allow Menzies to build a viable and sustainable business that not only meets the market expectations, but also set a new bar of service quality and business integrity.

Thanking you,

Yours faithfully,

………………………………………………

John Geddes
Director and Secretary
For and on behalf of:
Menzies Aviation Limited