# Aviation stocks face turbulence

## Costlier crude oil & weak rupee may offset a recovery in volumes

RAM PRASAD SAHU
Mumbai, 12 July

Since their lows in April, aviation stocks InterGlobe Aviation (IndiGo) and SpiceJet have gained 18-32 per cent on expectations of an improvement in passenger traffic and regulatory relief in the form of higher fares and expansion in capacity.

The government had increased the domestic fare by 5 per cent (at the lower band) in April and further by 13-15 per cent in June. This followed a fare increase of 10-30 per cent in the upper and lower bands in February this year. The hikes were prompted by a surge in the price of aviation turbine fuel, which jumped 81 per cent YoY in Q1FY22 (12 per cent QoQ) and a rise in the Brent crude oil prices by 13 per cent QoQ.

Ashish Shah and Vaibhav Shah of Centrum Research believe that the upward fare revisions will provide interim relief to airline companies amid falling traffic and rising crude environment. They expect ticket yields of IndiGo and SpiceJet to increase 7 per cent sequentially in the June (Q1FY22) quarter.

The other trigger for aviation stocks is the rise in passenger traffic. From its lows in May when the average daily passenger traffic stood at 63,000, the number more than doubled to 150,000 for the week ended July 10. Similarly, the numbers of daily departures and flyers per flight also increased 50-67 per cent over their lows in May. What may help airline companies is the Ministry of Civil Aviation's decision to increase flying capacity from 50 per cent to 65 per cent of pre-Covid levels from July 5.

The shift from the international leisure market to the domestic market may also aid volumes of domestic players. Aditya Mongia and Teena Virmani of Kotak Institutional Equities say: "A recovery in demand for Indian carriers can receive a major boost if international travellers swap prospects of international travel from domestic, as has happened in the case of China. Among Indian carriers, IndiGo is the one that continues to add capacities and may have a disproportionate share in the swap volumes." Given this shift in January and February, select base airports (Jammu, Chandigarh) for tourist destinations had breached pre-Covid levels of demand.

On the other hand, the sector faces multiple headwinds in the form of rising crude oil prices and a depreciating rupee. From sub-$60 per barrel levels in March, crude oil prices are up 25 per cent and hovering around $75 per barrel. Similarly, the rupee has depreciated 3 per cent against the dollar from the end of May to over ₹74.5 currently.

While crude oil prices remain the single biggest cost, a weak rupee will increase maintenance and leasing costs. Losses at the operating profit level can thus continue despite the volume improvement. Analysts expect volumes to reach February 2021 levels only by the end of the current year.

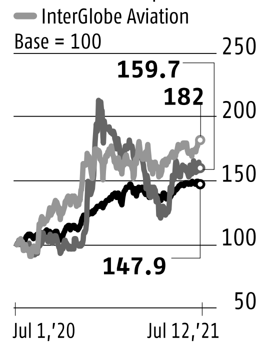
Given the multiple headwinds, investors should avoid airline stocks for now, unless there is a clear indication of pricing power, lower costs, and stable profitability.

### LOSSES RISE IN Q1FY22 (In ₹cr)

| | InterGlobe Aviation | SpiceJet |
|---|---|---|
| Net sales | 2,647 | 1,034 |
| % change YoY | 245 | 101 |
| % change QoQ | −57.5 | −45 |
| Ebitda | −963 | −259 |
| Loss Q1FY22 | −2,203 | −706 |
| Loss Q4FY21 | −1,147 | −235 |
| P/E (x) FY23E | 21 | 7 |

P/E: Price to earnings ratio; Ebitda : Earnings before interest, taxes, depreciation, and amortisation
E: Estimates
Source: Elara Capital

### HIGH-FLYING




# IFSCA issues norms for setting up, operating ITFS

PRESS TRUST OF INDIA
New Delhi, 12 July

The International Financial Services Centres Authority (IFSCA) on Monday released a framework for setting up and operating an international trade finance services platform (ITFS) to provide trade finance services at international financial services centres (IFSCs).

The framework will enable exporters and importers to avail various types of trade finance facilities at competitive terms, for their international trade transactions through a dedicated electronic platform ITFS, an official statement said.

This will help in their ability to convert their trade receivables into liquid funds and to obtain short-term funding, IFSCA said.

"This framework will provide an opportunity to the participants to avail trade finance facilities for trade transactions such as export invoice trade financing, reverse trade financing, bill discounting under letter of credit, supply chain finance for exporters, export credit (packing credit), insurance/ credit guarantee, factoring and any other eligible product, on the ITFS platform," it said.

IFSCA was established in April last year under the International Financial Services Centres Authority Act, 2019. It is headquartered at GIFT City, Gandhinagar. IFSCA is a unified authority for the development and regulation of financial products, financial services and financial institutions in the International Financial Services Centre (IFSC) in India. Currently, GIFT IFSC is the maiden international financial services centre in India.

# Avoid locking into corporate FDs of longer tenures

## Deterioration risk in credit profile increases, and better rates may become available a year later

BINDISHA SARANG

Bank fixed deposit (FD) rates have come down over the past few years. State Bank of India, for instance, offers rates of 2.9-5.4 per cent (3.4-6.2 per cent to senior citizens) for tenures ranging between 7 days and 10 years. With returns from bank FDs failing to beat inflation, investors are looking for better alternatives. Currently, several AAA-rated company FDs are available that offer returns of up to 8.25 per cent.

**Higher returns**

Company FDs are popular among many fixed-income investors because they offer better rates.

Sahil Arora, senior director, PaisaBazaar, says, "They usually offer higher interest rates than bank FDs." They also offer a number of payout options that investors can choose from — monthly, quarterly, half-yearly, and yearly. Ratings from credit rating agencies provide investors a reasonable estimate of the quality of the FD.

Corporate FDs offer higher certainty than debt mutual funds (MFs) as their interest rates remain fixed during their tenures and don't fluctuate with changes in policy and market rates.

**Default risk**

Their higher returns, however, come with higher risks. Adhil Shetty, chief executive officer (CEO), BankBazaar, says, "The biggest risk they carry is credit risk — the uncertainty that the company may not be able to pay back either the interest or the principal."

Remember that credit ratings provide an idea of only the probability of default. A highly rated corporate FD is safer, but there are no assurances. Shetty says, "In the past, even highly rated corporate FDs have defaulted. They failed to either pay interest or return the principal on time to depositors."

Company FDs are not backed by an insurance cover.

Arora says, "Bank deposits — including current, fixed, and recurring of up to ₹5 lakh in each scheduled bank — are covered by the depositor insurance programme offered by the Deposit Insurance and Credit Guarantee Corporation, a Reserve Bank of India subsidiary."

**Should you invest?**

Before investing in a company FD, check whether the company's financial and other parameters are sound. Shetty says, "Spend some time in trying to understand the company's management and business model before investing. After all, by investing in a corporate FD, you are lending money to the corporate."

### PAY HEED TO BOTH RETURNS AND RATINGS

| Company | Highest interest rate offered (%) | Rating |
|---|---|---|
| Shriram Transport Finance | 8.25 | MAA+/Stable by ICRA |
| PNB Housing Finance | 6.7 | FAA+/negative |
| Bajaj Finance | 6.75 | FAAA/Stable by CRISIL MAAA/Stable by ICRA |
| ICICI Home Finance | 6.9 | FAAA/Stable by CRISIL MAAA/Stable by ICRA |
| Mahindra & Mahindra Finance | 6.45 | FAAA/Stable by CRISIL |
| HDFC Limited | 6.65 | FAAA/Stable by CRISIL MAAA/Stable by ICRA |

Source: Bankbazaar

In the current environment, retail investors should stick to AAA-rated corporate FDs.

As for who should invest, Arora says, "Investors having higher risk appetite and seeking higher returns than bank FDs, or those seeking higher income certainty than they would get in debt funds, can opt for corporate FDs."

According to Tarun Birani, founder and CEO, TBNG Capital Advisors, "These are large, credible groups. Park a portion of your debt allocation into these FDs for the short term."

YOUR MONEY

Some experts are of the view that you should invest in them for only one year.

Jharna Agarwal, head, Anand Rathi Preferred, says, "Check the liquidity position of these high-rated companies and then go for a one-year deposit. The markets will price in rate-hike expectations over the next year. After a year, the maturity proceeds can be moved back to MFs."

Avoid committing money for the longer term for two reasons. One, after a year, there could be opportunities to deploy funds at better rates. Two, it is difficult to predict the stability of companies with which deposits are made over the longer term.

Investors in the higher tax brackets should avoid company FDs and stick to debt MFs.

Birani says, "Interest income from company FDs will get added to the investor's income. Even if you earn 7 per cent interest and pay 40 per cent tax, you will end up with only around 4 percent. Debt MFs are far more tax efficient."