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Profitability analysis of air India limited: An empirical study

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Abstract
Airline service decisions are increasingly influenced by the new drivers of profitability. The fluctuating profitability must be better understood by the firm to make a better strategy. The Primary objective of a business undertaking is to earn profits. Profit earning is considered essential for the survival of the business. Profitability analysis measures how will a firm is performing in terms of its ability to generate profits. Profitability of the firm is highly influenced by internal and external variables, i.e., size of organizations, liquidity management, growth of organizations, component of costs and inflation rate. In this paper an attempt has been made to measure the profitability performance on the basis of selected profitability ratios. The present study is based on secondary data of last 6 years and covers the profitability performance of Air India. Air India experienced a strong 30-35% year-on-year improvement in revenue during the study period. Also Air India's domestic market share declined from 17.1% to 16.5%. During past five years Indian airline industry had witnessed major downturn on account of global economic crisis, lower passenger count, rising fuel prices, fluctuations in foreign exchange rate, all these external environmental factors along with internal environmental factors like operational inefficiency, non- strategic management decisions, higher overheads & financial charges influenced NPM negatively & resulted in greater losses.

Keywords: profitability, financial ratios, economic crisis, operational efficiency

Introduction

Air India is the national flag carrier airline of India with a network of passenger and cargo services worldwide. It is one of the two state-owned airlines in the country, the other being Indian Airlines. Its main base is Chatrapati Shivaji International Airport, Mumbai, with hubs at Indira Gandhi International Airport, New Delhi and Chennai International Airport. The airline operates flights that connect 39 destinations around the world including 12 gateways in India. Air India Limited is owned by the central government. The company was formerly known as National Aviation Company of India Ltd, which was incorporated to facilitate the merger of state-owned airlines, Air India and Indian Airlines. The company is headquartered at Mumbai and operates on both, domestic as well as international routes. Air India was founded as Tata Airlines in 1932 and became a public limited company in 1946 as Air India. Indian Airlines was established in 1953 through a merger of seven domestic airlines, following the passing of legislation, nationalising independent airlines in India. Considering that the airline is saddled with accumulated losses and debt, which are to be restructured, the civil aviation ministry prompted the company to go through the current financial and operational reengineering exercise. This resulted into a merger between Air India and Indian Airlines which got the cabinet clearance on March, 1 2007. Consequent to the above, a new company viz National Aviation Company of India Limited (NACIL) was incorporated under the Companies Act,1956 on 30th March, 2007. It was decided that post-merger, the new entity will be known as "Air India" while "Maharaja" will be retained as its mascot. Hence, on 27th February 2011, Air India and Indian airlines merged along with their subsidiaries to form Air India Limited.

Financial Tools and Methods

In order to evaluate financial condition and performance of a firm, the financial analyst needs certain tools to be applied on various financial aspects. One of the widely used and powerful tools is ratio or index. Ratios express the numerical relationship between two or more things. Accounting ratios are used to describe significant relationships, which exist between figures shown on a balance sheet, in a profit and loss account, in a budgetary control system or in any other part of the accounting organization.

Select Profitability Ratio's For Analysis

1. **Return on Investment:** This ratio is also called Return on Capital Employed. It measures the sufficiency or otherwise of profit in relation to capital employed. Return on Investment is used to measure the operational and managerial efficiency. Return on investment can be computed for measuring the return of various purposes.
2. **Gross Profit Ratio:** Gross profit ratio is also known as gross margin or trading margin ratio. Gross profit ratio indicates the difference between sales and direct costs. Gross profit ratio explains the relationship between sales and direct costs. Gross profit ratio explains the relationship between gross profit and net sales. The gross profit ratio is expected to be adequate to cover operating expenses, fixed interest charges, dividends and transfer to reserves.
3. **Operating Profit Ratio:** It is the ratio of profit made from operating sources to the sales, usually shown as a percentage. It shows the operational efficiency of the firm and is a measure of the management's efficiency in running the routine operations of the firm.

4. **Net Profit Ratio:** This ratio is also called net profit to sales ratio. It measure of management's efficiency in operating the business successfully from the owner's point of view. It indicates the return on shareholders' investments. Higher the ratio better is the operational efficiency of the business concern.
5. **Return on Net Worth:** This ratio signifies the return on equity shareholders funds. The profit considered for computing the ratio is taken after payment of preference dividend.

Statement of the Problem

Ratio analysis plays an important role in determining the financial strengths and weaknesses of a company relative to that of other companies in the same industry. The analysis also reveals whether the company's financial position has been improving or deteriorating over time. Profitability Ratios are used to evaluate management's ability to create earnings from revenue-generating bases within the organization. Profitability Ratios measure the earnings by dividing the earnings by a base, such as assets, sales or equity.

Review of Literature

Dr. A. Muthusamy and M. Muthumeena (2015) [1], made an analysis on "Financial Performance of Selected Private Airlines in India". The overall aviation industry has been flawed by cost inefficiencies and aggressive price cuts, rising cost, expensive jet fuel, dearth of experienced pilots, inflexible labour laws, higher cost of capital with a burden of interest payments, rising losses and working capital stretched balance sheet and tight liquidity profile of the most airlines. The financial performance has been analyzed with the help of some key measures relating to the performance in ratios on the overall financial performance of the selected private Airline companies in India.

Dr. R. Angayarkanni and Anand Shankar Raja. M (2015) [2], made an analysis on "Profitability Analysis of Select Indian Aviation Firms an Empirical Analysis". The fluctuating profitability must be better understood by the firm to make a better strategy. In this paper an attempt has made to measure the profitability performance and to analyze the impact of selected profitability ratios on ROCE of the company, for fulfilment of the objectives. The collected data is analyzed and computed to fit for drawing inferences.

DR. Vivek Singla (2013) [3], under took a study "A Comparative Study of Financial Performance of SIAL and Tata Steel Ltd". While analyzing the financial performance of the selected units, the analysis of working capital, analysis of fixed assets and analysis of profitability was included. SAIL and Tata Steel Ltd. both the companies are major players in steel manufacturing sector in India. After making the comparative analysis of both the firms we find that performance of Tata Steel Ltd. is better than the SAIL. It is so because the Net profit of Tata Steel Ltd. is greater than the SAIL similarly the inventory management of the Tata Steel Ltd. is better than the SAIL.

Research Methodology

The study is based on secondary data collected from the audited Profit & Loss A/c and Balance Sheet associated with schedules, annexure available in the published annual reports of Air India. The required information was also collected from Capitaline data base and also from PROWESS, which is the most reliable and authorized corporate database of CMIE.

Calculation of Profitability Ratios (I)

Profitability Ratios	2009-10	2010-11	2011-12
Return on Investments (%)	-87.38	-89.14	-91.96
Gross Profit Ratio (%)	-14.58	10.82	-29.84
Operating Profit Ratio (%)	-48.92	-34.06	-44.27
Net Profit Ratio (%)	-42.36	-48.82	-51.51
Return on Net Worth (%)	-91.55	-97.38	-94.04

***Source*:** Computed From Annual Reports of Ail

Interpretation and Discussion

The above table shows the calculation of profitability ratios from 2009-10 to 2011-12. In the table it is found out that the Return on Investments in 2009-10 is (-87.38 %), 2010-11 is (-89.14 %) and 2011-12 is (-91.96 %). The ROI ratio during 2009-10 and 2010-11 satisfies the norm level, as the long term funds and capital employed may be utilised more efficiently. Gross Profit Ratio was marked high (10.82%) in 2010-11, while as it was lowest (-14.58 %) in 2009-10 and (-29.84%) in 2011-12. The Gross Profit Ratio in the year 2010-11 shows that the sales mix were increased while in 20010 and 2011-12 it was observed that there is a higher proportion of low margin products in the sales mix. The Operating Profit Ratio shows a decreasing trend from bottom to top and it was highly decreased (-48.92%) in 2009-10 then (-34.06%) in 2010-11 and (-44.27%) in 2011-12. Operating Profit Ratio shows an inefficiency which is not enough to provide good return to the shareholders and investors. The Net Profit Ratio was marked as negative, (-42.36%) in 2009-10, (-48.82%) in 2010-11 and (-51.51%) in 2011-12. Return on Net Worth was proved negative in all the study period years, it was (-91.55%) in 2009-10, (-97.38%) in 2010-11 and was (-94.04%) in 2011-12. indicates that the funds from shareholders have not been efficiently utilised to generate the profit and decreased the growth of the company.

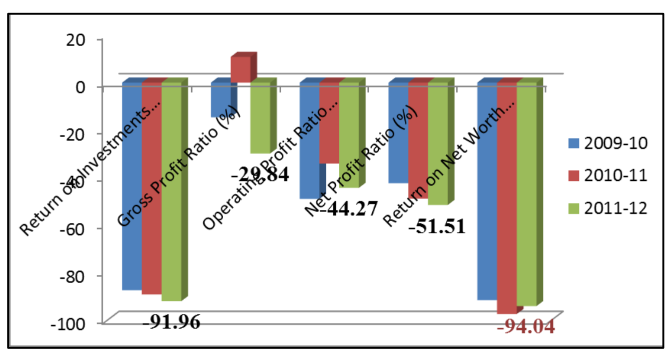

Fig 1: Representation of Gross Profit Ratio Values from 2009-10 to 2011-12.

[1] Dr. Muthusamy. A and Muthumeena. M, "Financial Performance of Selected Private Airlines in India", ZENITH *International Journal of Business Economics & Management Research*, Vol. 5, Issue 5, May 2015, pp. 11-26.

[2] Dr. Angayarkanni R and Shankar Raja. M Anand, "Profitability Analysis of Selected Indian Aviation Firms: An Empirical Analysis". IRACT – *International Journal of Commerce, Business and Management*, Vol. 4, Issue 2, April 2015, pp. 1018-1028.

[3] Dr. Singla Vevik. "A Comparative Study of Financial Performance of SAIL and Tata Steel Ltd". *International Refereed and Indexed Journal for Research Scholars and Practitioners* (IJRSR), Vol. 2, Issue 1, 2013, pp 2321-3280.

The above Fig is based on the profitability ratios pertaining from 2009-10 to 2011-12. The Fig represents the analysed data for above table in bars inorder to make it convenient for better understanding the position of changing ratios calculated in the table.

Calculation of Profitability Ratios (II)

Profitability Ratios	2012-13	2013-14	2014-15
Return on Investments (%)	-90.40	-84.01	-82.92
Gross Profit Ratio (%)	-16.12	-14.36	-9.23
Operating Profit Ratio (%)	-47.77	-38.21	-38.15
Net Profit Ratio (%)	-34.25	-34.18	-34.08
Return on Net Worth (%)	-83.88	-84.54	-86.99

Source: Computed From Annual Reports of Ail

Interpretation and Discussion

The above table shows the analysis of profitability ratios ranging from 2012-13 to 2014-15. The above table holds Return on Investments Ratio, Gross Profit Ratio, Operating Profit Ratio, Net Profit Ratio and Return on Net worth Ratio. The ROI ratio during the study period was observed as negative. This indicates that the ratios did not satisfy the standard norm. So the long term funds and capital employed cannot be utilised efficiently. The GPR also didn't qualifies the standard norm as there was a highly proportion of low margin products in the sales mix. The OPR was (-16.12%) in 2012-13, (-14.36%) in 2013-14 and (-9.23%) in 2014-15. Here, Operating Profit Ratio also shows an inefficiency which is fails to provide good return to the shareholders and investors and also was not good for running business of the company. The NPR was found negative in the select period of study, it was (-34.25%) in 2012-13, (-34.18%) in 2013-14 and (-34.08%) in 2014-15 The NPR indicates that the operational efficiency of the business concern was highly effected during the period of study because such condition was not in favour for the betterment of shareholders investments. The RONW ratio was observed negative during the study period, it was (-83.88%) in 2012-13, (-84.54%) in 2013-14 and (-86.99%) in 2014-15. The ratio shows that the funds from shareholders have not been efficiently utilised during the study period to generate the profit and failed to increase the growth of the company.

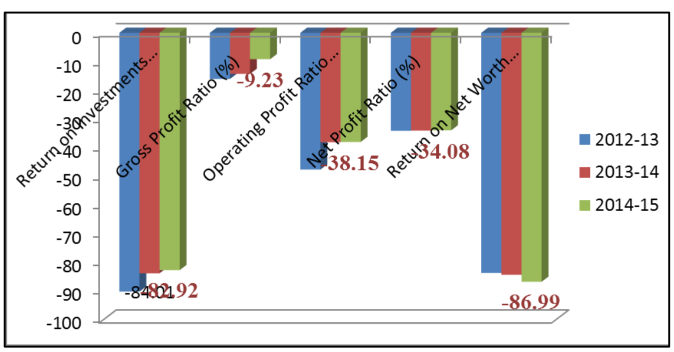

Fig 2: Representation of Gross Profit Ratio Values from 2012-13 to 2014-15.

The above Fig highlights the graphical representation of calculated ratios of the above table ranging from 201-13 to 2014-15. The Fig also represents the profitability ratio of air India limited. The calculated ratios in the above graph were deviated downwards to make better understood the efficiency of the sample company during the sample period.

Conclusion

The airline business is a highly dynamic business. The time is not fixed for the airline to become profitable. The present condition and the challenges that airline is facing and the advantages that airline is having in future timeline can be known by observing this analysis. The main objective behind the airline analysis is that to reveal the actual technique that airline practices to drive away the competition in order to achieve high end profits. This is also benefited to the investors both from inside as well as outside to invest funds in the company. After analysing the select Profitability Ratios, it was found out that the Profitability more or less depends upon the efficient utilization of resources, sales and quality management. For better performance, the cost reduction should be avoided by using advanced technologies inorder to increase the profitability position of the company.

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