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DELHI INDIRA GANDHI INTERNATIONAL AIRPORT

Delhi International Airport Limited
(Formerly known as Delhi International Airport (P) Limited)

Registered Office: New Udaan Bhawan,
Opp. Terminal 3, IGI Airport,
New Delhi 110037, India
T +91 11 47197000
F +91 11 47197181
CIN No. U63033DL2006PLC146936
W www.newdelhiairport.in

Letter No: DIAL/2017-18/FIN/377
Date: 12th Jun'2017

To,

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

Subject: Consultation Paper for determination of tariff for aeronautical services in respect of Cochin International Airport, Cochin for the second control period

Reference: Consultation Paper No. 06/2017-18 dtd 12th May'2017

Dear Sir,

With reference to above consultation paper, please find below our response:

As per proposal 10, Authority proposes to consider cost of equity at 14% for computation of Fair Rate of Return.

DIAL Submission:

The Indian civil aviation industry in particular is on a high growth trajectory as India aims to become the third largest aviation market by 2022. Indian growth story is going to even continue in the future which requires substantial investment. Regulatory environment is a major driver in providing congenial environment for such investments and at the same time attract private investment into airport development. Despite the highest growth rate globally in the aviation sector, private capital is shying away from India. This is despite 100% FDI being allowed.

The prime mover for the airport development is the policy and regulatory environment. The Regulatory environment ideally should be a combination of cost recovery, **fair rate of return** and efficient methodology for incentivisation and dis-incentivisation. Investments in the airport sector largely depend on the Government policy and the Regulatory environment. Our experience would indicate that the Regulatory risk is placed amongst the top while evaluating a project in Indian context amongst other financial and commercial risk matrices.

It may also be seen that the Airports are operating in such a complicated environment where there is a perennial need for capital; raising funds is difficult; the cost of capital and risk-premiums are high; dispute resolution mechanisms are almost non-existent; and policy and regulatory uncertainty prevails.

Given the above facts the rate of return offered to private operators appears unfair and not commensurate with the associated risks and the complex ground realities. The infrastructure projects as the airports are back ended in terms of the return to the investor. In such a scenario returns not commensurate with the risks involved would further deteriorate the financial position of the Airports.

The Authority in clause 12.2.1 of the subject consultation paper has stated following:

"The Authority noted the request for a higher % of cost of equity to be considered while calculating the FRoR. The Authority also noted that CIAL has been established and running the airport for over 15 years with consistent trend of profits and dividends. Considering the past operations, profitability and established traffic base, the Authority proposes to consider return on equity at 14% for CIAL for the second control period."

From above it is evident that Authority has determined the rate of return based on historical financial performance of the company and not considered the methodology defined under the airport operator guidelines 2011 for determination of cost of equity.

As per airport operator guideline for tariff computation, the cost of equity shall be determined by applying Capital Asset Pricing Model (CAPM). Accordingly, Authority should determine cost of equity for Cochin Airport using CAPM method.

Also, authority should consider SBI Cap report on "Fair Rate of Return of Equity for Indian Airport Sector". SBI Capital was appointed by MoCA to carry out this study. In its study, SBI Caps has recommended that a return of 18.5% to 20.5% is fair rate of return for private airports and has enumerated certain risk factors for airport sector in India in general.

For Delhi International Airport Ltd.

K Narayana Rao
Director