

# INVESTMENT IN AIR TRANSPORT

- Case Study of Precision Air

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## 1. **Air Transport Industry (briefly)**

Air Transport is one of the most highly regulated businesses. In addition, it is capital intensive, extremely risky, susceptible to many sensitivity tests and yet produces thin margins compared to other business sectors or investments.

The regulations on air services are international, having been formulated by the International Civil Aviation Organization (ICAO), which is a body of the United Nations. ICAO was established during the Chicago Convention in November 1944 for the purpose of regulating and harmonizing commercial Air Transport between states and establishing safety standards. This is achieved through Standard and Recommended Practices (SARPS) which are promulgated from time to time to contracting states.

Thus the regulations which are applied by the Tanzanian Civil Aviation Authority are according to SARPS and conform to practices by other states which are members of ICAO. Sometimes states may register a difference in application of the rules in order to suit their unique situation.

The difficult nature of aviation as a business was expressed by a previous Chairman of British Airways, one of the world's bigger airlines, when asked what he viewed as the success of his airline he replied, *"every day that the airline survives is a success"*. Yet another British airline tycoon said, *"in order to become a millionaire, start with a billion and invest in an airline."*

Warren Buffett, a billionaire investor in the USA commented, *"there is no worse business than the airline"*.

## 2. **Air Transport and Tourism**

Airlines are the engine for tourism. They facilitate fast, comfortable and safe means of arriving at the destination country through international airlines and point to point travel within the country through domestic air services. The dependence of tourism on air transport can be illustrated by the resultant acute depression of the sector after the tragic events in the USA on September 11, 2001 when large commercial aircraft were forced to fly onto the World Trade Centre, in New York and the Pentagon in Washington D.C. That horrendous event caused the loss of thousands of innocent lives and marked a historical moment for the airline industry and tourism.

The culture of traveling by air was soon afterwards changed and many would be tourists declined to travel. Due to the onset of Globalisation Tanzania like many countries outside the USA, was not spared in her infant but fast growing tourist industry. The effects linger on.

Therefore for tourism to thrive both international and domestic air transport must be adequately active, efficient and safe.

## 3. **Domestic Air Travel in Tanzania**

About two decades ago air transport was the domain of the state in many countries. Liberalisation started in the USA in late 1970s, spread over to Europe and gradually to other countries all over the world.

In Tanzania, the national carrier, Air Tanzania Corporation (ATC) was the sole provider, except for a few air charter companies, of domestic air travel. The government policy to liberalize the economy produced the opportunity for private domestic airlines to establish in Tanzania from early 1990s. Many of them sprang out fast but unfortunately they did not last for too long because of bad

preparations and a false expectation for quick wealth. In most cases, however the investors were foreign and left many debt problems behind in the wake of closing business.

During this period *Precisionair* got established and soon became second to ATC in the domestic market. *Precisionair* filled a void which ATC had made by stopping to operate the Twin Otter and Fokker Friendship aircraft to the small airports with unpaved short runways.

#### 4. **Precision Air Services Limited** (Trading as Precisionair)

*Precisionair* was formed as a logical development of an aerial crop spraying company namely, Precision Flight (Africa) Limited that was formed in 1986. At that time the economy in Tanzania was strictly state controlled and so it was a nightmare to get that company started. Uncompromising insistence and perseverance saw to its floatation and operation.

In early 1990s persistent drought rendered the agricultural sector unprofitable leave alone the looming famine. Therefore expensive aerial crop dusting became redundant and so Precision Flight Ltd.

It was then that Precisionair was conceived and came into effect operationally in 1993. The promoters saw opportunities in the growing tourist industry. Therefore the focus was to operate schedule and charter flights between Arusha, where the project was based, and the Northern safari areas of Serengeti, Ngorongoro, Lake Manyara and connecting to Zanzibar. The aircraft deployed to enter the market had to be reasonably affordable but capable safely and economically to meet that sector of travel. Thus piston engined Cessna aircraft from the second hand market were acquired and within two years of operation the results were tremendous. This was possible because of a sound management team armed with the requisite skills, full dedication and loyalty to the company. Those tenets still hold today and have made *Precisionair* to grow

efficiently, sometimes too fast, but with a good position in the market today. Within three years Precisionair grew from a small, modest air operator to a medium size airline. The route between Arusha and Zanzibar was the maker of the airline.

In 1996 the ATR 42 turbo-prop aircraft with capacity of 48 passengers was introduced. It is said, *"the aviation business is not for the faint hearted."* That explains the courage to leap from operating simple piston engine aircraft to a modern technology aircraft with five fold the capacity of passengers. In 1999 the whole fleet was made of turbo-prop aircraft consisting of two ATR 42, four LET 410 with a capacity of 19 passengers each and the small Grand Caravan for air charters and back up aircraft.

The journey has however been long and challenging. We started off in a completely disabling taxation system which was too restrictive compared to any country. That perhaps was the consequence of the state controlled economy practiced over a long period. Very often we came to the brink of closing business, not because the government was enforcing collection of due taxes, but their provision in the audited accounts and the qualifications noted by the auditors stopped refinancing which was necessary for survival. Fortunately the government recognized the contribution the company made to the development of the country and avoided to close it down by not enforcing collection of uncollectable taxes.

Additionally the government did not stop to listen to our petitions and, although it took a long long time, the taxation in the industry is now manageable after some amendment to the Regulations. The country is competitive compared to the neighbours. It is only a mop up that is now required. The partnership between the government and the private sector was evident during this process.

Different kinds of challenges have been addressed continuously as new ones arise. Inadequate airport facilities and navigation aids, monopolies of ground

handling companies, insufficient skilled staff are problems that are regularly dealt with. Occasionally there comes up the kind of investors who focus on quick returns or something else not related to the core business. These are usually short lived but while they survive they stir up quite a commotion in the market and have caused us a lot of problems. Natural occurrences like unpredictable severe weather patterns often cause disruptions to flight schedules and extra demand from the skills of our flight crew. Bird strikes and foreign object damages bring about huge unscheduled expenses.

Simply, the business is full of challenges and the only explanation to venture into it may be classified as, passion, adventure, lack of awareness or prestige. Wealth is rare.

Having grown so dramatically fast, Precisionair is presently in the consolidation phase. The airline has embarked on measures which will ensure sustainability. These include, improvement of staff skills by training in and outside the country, cut back on costs, embracing information technology, improvement of services through on-time-performance, good public relations and to strengthen the balance sheet. These will create a base for the development of the airline to a regional or even an international carrier which is the vision.

The survival has been through keen perseverance, using high skills, staff loyalty and prayer. Yes, prayer.

## **5. How to Establish an Air Service Business in Tanzania**

As earlier mentioned the prerequisites to establish an air service company are similar between countries because of the standards set by the ICAO.

The basic requirements are the Air Service Licence and the Air Operator Certificate both of which are issued by the Tanzania Civil Aviation Authority (TCAA) to which body the applications are made. The authority issues special

forms on which to make the application. The TCAA will require together with the application:

- (i) The registration of the company with the Registrar of Companies according to CAP 212
- (ii) A business plan to indicate the viability and sustainability of the project and the ownership structure. Usually there is a requirement for local participation in ownership but this has often been conveniently overlooked in order to attract foreign investment.

Nevertheless, in order for an operator to be eligible for the Bilateral Air Service Agreements (BASA) with other countries, the following conditions in addition will strictly apply as a requirement of the other country:

- (a) the central administration and principal place of business has to be in Tanzania
- (b) the effective control is by nationals of this country which means a controlling vote of the board of directors
- (c) the majority of share holding must be vested in the country
- (d) the majority of profits are retained in the country

These conditions have become a problem to some local investors perhaps due to their lack of awareness or deliberately trying to go round the rules.

It is always much simpler to follow the rules!

- iii) in order to apply for the AOC the aircraft of intended operation have to be identified and inspected by officials of the TCAA to ascertain their compatibility with a safe operation. The plan for maintenance is approved along with the aircraft.

## 6. **Business Opportunities**

Tanzania is known as the land of many opportunities.

This is true to the air transport business. Being a very large country with an area of 945,234 sq.km and inadequate infrastructure for surface transport, Tanzania needs more than anything air transport for her development. Whereas road transport requires thousands of kilometers of construction, the basic for air transport is a runway which may be only one kilometer. The aeroplane and its operation is expensive but not necessary for the cost of whoever constructs the runway and the airport.

The rapidly growing sectors of economy namely tourism, manufacturing, agriculture and trading rely on air transport. All these are located over the country. No one air service is presently able to provide the network required to cover the demand. Concentration has been on the tourist destinations of the North, Zanzibar and parts of the South. But even in those areas, the demand is not yet fully met. The more the operators competing the more the market is stimulated to incite extra demand.

Therefore serious and genuine investors who are well prepared to face the challenges will find a lot of scope to satisfy their ambitions in aviation. While it is not possible to create profits in the short term, the long term opportunity of creating a good company stock is certainly available in Tanzania.

The Tanzania Investment Centre (TIC) is a proven investor friendly and in a special way recognizes the significance of air transport in the overall development of the country. Precisionair as well as other local operators have benefited from the unfailing goodwill of the TIC.

## 7. **Finally**

About 80% of a tourist's expenditure is on airline travel. Therefore countries which have their own international air carriers are able to stimulate tourism much better and earn more than the rest. For that reason small nations in Africa like the Seychelles and Mauritius have developed a vibrant tourism industry. Egypt, South Africa and Kenya are similarly great tourist destinations.

Unfortunately Tanzania is missing this link and the future does not indicate a lot of hope for an own international airline. Certainly not at these times of severe 'turbulence' in the industry where many a giant airlines have become bankrupt while others are following.

The country however, should not lose focus in establishing her own airline, through private investment. In the interim, possibilities to co operate with existing airlines in a special arrangement could be explored. This is necessary in order to vigorously promote the wonderful destination that Tanzania is and retain some of the 80% that is expensed in air travel by tourists.

To quote Andrew Young the renown diplomat and once Mayor of Atlanta, Georgia in the USA, he said, *"Any country will earn much interest free money more from tourism than they can ever get from the IMF, World Bank and other financial institutions."*

Tanzania has what it takes to be a giant in tourism. *'It can be done, play your part,'* the Father of the Nation the Late Mwalimu Julius K. Nyerere, said.

*30<sup>th</sup> September, 2002*

