

IS KINGFISHER BEING FISHED OUT ?

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Kingfisher chairman Vijay Mallya has faced rough situations earlier, but the chances that he will be able pull a rabbit out of the hat this time are slim. Only a stroke of financial genius and oodles of luck will save his cash-strapped airline with a debt of Rs 7,500 crore.

Vijay Mallya :

Born on 18 December 1955 is an Indian liquor and airline baron. The son of industrialist Vittal Mallya. He completed his degree at St. Xavier's College, Calcutta. He is the chairman of the United Breweries Group and Kingfisher Airlines. His United Spirits is world's second largest liquor maker, by volume. Mallya is also an MP in the Indian Rajya Sabha.

He also co-owns the Formula One team Force India, the Indian Premier League team Bangalore Royal Challengers and the I-League team East Bengal FC.

According to *Forbes*, his personal wealth is estimated to be \$1.4 billion. Mallya receives substantial press coverage that focuses on his lavish parties, villas, automobiles, Force India, Royal Challengers Bangalore and his yacht, the *Indian Empress*

Business

Breweries :

Mallya took over as Chairman of United Breweries Group in 1984 from his father Vittal Mallya. Since then, the group has grown into a multi-national conglomerate of over sixty companies, with an annual turnover which increased by 63.9% over 15 years to US\$11.2 billion in 1998–1999. The focal business areas of the group encompass alcoholic beverages, life sciences, engineering, agriculture, chemicals, information technology, aviation and leisure.

In May 2007, United Breweries Group announced the all-cash acquisition of scotch whisky maker Whyte & Mackay for £595 million (approximately Rs 3000 crore). In 2005 he took over Millennium Breweries Ltd (formerly known as Inertia Industries Ltd), which owned the two premium beer brands named *Sandpiper* and *Zingaro*.

Airlines :

In 2006, Mallya established Kingfisher Airlines. At present, the airline connects 32 cities. Kingfisher Airlines obtained a 26% stake in Air Deccan, a low cost Indian airline which Mallya later acquired fully and rebranded as Kingfishers Red. Vijay Mallya and his Jet Airways counterpart Naresh Goyal announced an alliance after a marathon meeting on 13 October 2008 at Mumbai, India.

* The winning case of Case Chase 2011 Competition for I Year MBA Students of KLS IMER, Belgaum.

Media :

Mallya owns the TATA industries Newspapers which serve Marin County, California where he maintains a home and stores a portion of his car collection

Corporate Sponsorship

UB Group sponsors many sports events and teams such as:

- Signature Golf Tournament - Indian Golf Tournament.
- Mohan Bagan A.C. - I league Team
- Kingfisher Derby Team - Horse Racing
- East Bengal Club - I league Team
- Royal Challengers Bangalore - IPL Team
- Force India - Formula One Team

Kingfisher Airlines :

Kingfisher Airlines is an airline group based in India. Kingfisher Airlines, through its parent company United Breweries Group, has a 50% stake in low-cost carrier Kingfisher Red. The airline has been facing financial issues for many years.

Kingfisher Airlines is one of the only seven airlines awarded 5-star rating by Skytrax along with Cathay Pacific, Qatar Airways, Asiana Airlines, Malaysia Airlines, Singapore Airlines, and Hainan Airlines. Kingfisher operates more than 375 daily flights to 71 destinations, with regional and long-haul international services. In May 2009, Kingfisher Airlines carried more than 1 million passengers, giving it the highest market share among airlines in India. Kingfisher also owns the skytrax award for India's best airliner of the year 2011.

Kingfisher Airlines is also the sponsor of F1 racing outfit, Force India, which Vijay Mallya also owns.

Emerging Problems [2009] :

Kingfisher Airlines appears to have hit turbulence. Mid-April, reports in the media point to a sudden exodus of Airbus Commanders from the airline. In just one week, as many as 26 are reported to have deserted their flamboyant employer and are believed to be headed for the Middle East. Despite the global economic downturn and clear signs of the Middle East economy slowing down, Qatar Airways is in the expansion mode and is prepared to offer as compensation a hefty tax free package to pilots qualified and experienced on Airbus family of aircraft. But the lure of money is perhaps unlikely to be the only provocation for this unusual and sudden migration of experienced pilots, some of whom are believed to be exploring opportunities to fly with any of the low cost airlines in the India.

The airline ushered in a refreshing five-star culture in domestic air travel that was laced with innovative features to provide the customer-referred to as 'guest' by the airline-excellent value for money and the unforgettable "Kingfisher Experience". On account of a powerful image projection blitz with its catchy slogan "Fly the Good Times", very soon Kingfisher became the airline of choice for the sophisticated and choosey segment of society. Not before long, Kingfisher Airlines emerged the acknowledged market leader in the industry.

The airline inducted a fleet of brand new aircraft of the Airbus 320 family, Airbus 330, ATR 72 and placed orders for more in accordance with their long term plans for expansion. Kingfisher was the first airline in India that had, and perhaps still has, plans to induct the giant Airbus 380 due for delivery in 2012. The airline was staffed and in some areas overstaffed with the best available in the market. Employees spoke with immense pride about the airline and appeared to be happily reveling in the glamorous world of

Kingfisher. The airline even bought over Deccan in the middle of 2007 with the triple objective of killing competition, enlarging operational network and commencing services on international routes in August 2008 using Deccan's operating license. The aim was to beat the other Indian carriers of Kingfisher's vintage.

DREAMS HIT WALL OF DUES :

By the end of 2007, hopes of breaking even after three years of operation began to fade. Under the dual onslaught of skyrocketing prices of Aviation Turbine Fuel (ATF) and declining load factor owing to global economic downturn that had the inevitable impact on the Indian economy, the year 2008 proved to be a nightmare not only for Kingfisher but the airline industry as a whole. Both these factors played havoc with the balance sheet of the airline which was perpetually in a state of imbalance since inception on account of extended operation of the airline at a high threshold of input costs.

Between April and September of 2008, Kingfisher reported a loss of Rs 641 crore. In the last quarter of 2008, that is, October to December 2008, finances of the airline were down by another Rs 626 crore. Bills started to pile up of substantial sums owed to the various agencies, such as oil firms for ATF already drawn, five star hotels utilised by crew, simulator training conducted at establishments abroad, local transport companies for services provided and Airport Authority of India in respect of the various charges. All together the cumulative arrears were reported to be over Rs 1,000 crore. Financial woes of the airline were compounded by the fact it was unable to obtain fuel and other services on credit till such time the dues were cleared.

While lower prices of ATF provided some relief, to redeem the grievous state, the airline set in motion a number of emergency measures to reign in expenditure. These included trimming capacity through withdrawal or reduction in the number of flights on unprofitable routes; shelving of expansion plans; deferment of delivery schedules of new Airbus 320 class aircraft; lease or sale of aircraft already with the airline rendered surplus; modification of orders for the long-haul A340-500 aircraft and the smaller A333-200s; strategic operational alliance with Jet Airways to pool resources and optimise capacity utilisation; review and rescheduling of some international routes, notably to the US, and so on. The airline was in desperate need for funding and was lobbying with the government for investment by foreign airlines, which was not permitted under the existing regulations.

Unfortunately, even the latest regulations put in place by the government a month ago have dashed hopes of domestic airlines seeking foreign airline equity. The new regulations pertain to investments and operations of scheduled airlines which set a minimum paid up capital of Rs 50 crore with five large aircraft. For regional carriers, the entry barriers are lower at a minimum equity of Rs 20 crore and five aircraft. The regulations permit foreign equity up to 49 per cent and NRI investment up to 100 per cent but continue to prohibit investment by foreign carriers.

PILOTS BEAR THE BRUNT :

For Kingfisher, the situation worsened through 2008 as the economy continued the downslide. Following year, it became precarious and presented a serious threat to the survival of the airline. The situation called for further urgent action. Attention then turned to trimming cost of human resource, especially pilots, which accounts for a substantial portion of operating cost and is invariably a sensitive issue. In fact, the exercise had begun in a discrete manner in September 2008 when some 300 low ranking employees were laid off. In the following month, salaries of a small group of 50 trainee pilots recruited as First Officers, was reduced drastically to a paltry stipend. At that time, Commanders and other senior pilots were spared. Vulnerable, the trainee pilots were really not in a position to resist this "take it or leave it" disposal by the airline management.

In February this year it came to light that while the airline had promoted as many as 21 of the management executives to high positions, it had tinkered with the terms of contract which had been entered into with senior pilots at the time of employment. As a part of the process of merger with Deccan, Kingfisher implemented a 'productivity-linked compensation structure' ostensibly under some sort of compulsion of the new Deccan-Kingfisher package structure in which emoluments of the original Kingfisher pilots had to be reduced to achieve parity with erstwhile Deccan pilots. In the face of falling demand, the total flying hours of the airline had come down by 21 per cent with corresponding reduction of monthly flying hours for each pilot. Owing to the new link with 'productivity', in which emoluments were related to the number of flying hours per month, from a figure of Rs 4.30 lakh, salaries of senior pilots were trimmed by as much as Rs 80,000 per month.

In addition, there has been considerable scaling down of some peripheral perks and privileges such as downgrading entitlement of hotel accommodation from the luxurious five-star to three-star or even guest house accommodation and so on. But perhaps, senior pilots were irked not so much with monetary stratagems but with the manner in which their terms of employment were altered unilaterally. Pilots have even petitioned the court seeking waiver of the mandatory six-month notice period prior to resigning to join another domestic carrier on the grounds that the airline had failed to fulfill contractual obligations. Viewed from the airline's point of view, these measures, unpalatable as they may be, were necessary for the survival of the airline.

HARD CHOICES :

The second issue that could have been a bone of contention was modification in the procedure for First Officers to upgrade to Command status on the Airbus type of aircraft. Under the new dispensation, senior First Officers with adequate experience to be eligible for Command on Airbus-narrow or wide body jets-were compulsorily required to first go through tenure in Command on ATR 42 or ATR 72 turboprop aircraft. The requisite downgrade from jet to turboprop would have in all likelihood dented their professional ego. But the airline had no option if the prohibitively expensive 140-odd expatriate Commanders were to be progressively replaced not only under orders of the Ministry of Civil Aviation but more importantly to cut cost.

Global economic crisis has had a debilitating impact on the Indian airline industry which has been engaged in a desperate struggle to establish a foothold in the erstwhile public sector dominated activity. With the rate of growth of passenger traffic dropping by 10 per cent in the financial year 2008-09 and economic revival not yet in sight, prospects for the industry look far from inspiring.

March 2011 :

In March 2011, the consortium of 13 banks led by sbi and icici agreed to convert Rs 1,300 crore of Kingfisher's debt into equity at a price of Rs 64 per share. The price was calculated in compliance with a SEBI rule which requires all conversion of debt into equity to take place at a six-month weighted average of the share price. Mallya got lucky. The six month price of Rs 64 was a 61 per cent premium over the prevailing share price of Rs 40 at the time the debt was converted into equity. The banks could have still said no to the deal but they went ahead with the conversion of debt into equity. The share price has sunk further to around Rs 20 eight months later, exacerbating the losses suffered by the banks. The perception in UB City is that Mallya will not sell his yachts and horses or the Royal Challengers IPL team to shore up the airline.

The six top banks in the consortium forked out Rs 596 crore for shares worth Rs 195 crore at current prices. The banks suffered a double whammy because in addition to equity they have also financed Kingfisher through loans. Their total exposure is around Rs 7,000 crore.

The D-Month [Nov 2011] – The Fall Begins :

News Headline – “Kingfisher Airlines crisis: 130 pilots quit, 149 flights cancelled”

While Kingfisher claimed it was cancelling 50 flights every day till November 19, in reality, it operated only 269 flights of its allocated winter schedule of 418 daily flights on Thursday. A shocking 149 flights - 36% of its daily allocated schedule - were not operated. Officially, Kingfisher has said that it has cancelled flights to reconfigure its Airbus A-320 aircraft. However, it is learnt that around 130 pilots have quit the cash-strapped carrier in the past few weeks. Also, airport operators, oil companies and vendors of all imaginable items have massive dues running with Kingfisher and are demanding that owner Vijay Mallya pay up. Given the shortage of crew and funds, the airline has truncated its schedule, perhaps opting to “fly less and spend less”.

Kingfisher also faces the threat of unpaid aircraft leasing companies seeking the return of their planes. Spare part vendors too - like other creditors - want their past dues to be cleared along with current ones.

Kingfisher Problem Overview :

Kingfisher may be a victim of its business model which focuses on the upper-end flier. The slowdown of 2008-2009 decimated the high-end market. There is evidence that price matters most to the Indian consumer. But Vijay Mallya is determined to stick to his model. In September, he announced closure of Kingfisher Red, the low-cost arm which emerged after his takeover of Air Deccan in 2007-08.

Unlike other airlines, which have had ups and downs, Kingfisher has never recorded a profit since it began operations in 2005. In 2010-11, when crude prices were moderate and the rupee strong, Kingfisher recorded losses of Rs 1,027 crore. In comparison, Jet’s loss was Rs 86 crore.

#	From	To	Months	Total Income	Cost	Net Profit	EPS
1	Apr-05	Jun-06	15	1,352	1,689	-337	-68
2	Jul-06	Jun-07	12	2,142	2,562	-420	-42
3	Jul-07	Mar-08	09	1,546	1,734	-188	-11
4	Apr-08	Mar-09	12	5,577	7,186	-1,609	-55
5	Apr-09	Mar-10	12	5,271	6,918	-1,647	-54
6	Apr-10	Mar-11	12	6,496	7,523	-1,027	-16
7	Apr-11	Sep-11	06	3,410	4,142	-732	n/a

Once upon a time Vijay Mallya believed his dream business, an airline, would catapult him from tycoon to trillionaire. Six years after he launched Kingfisher Airlines in 2005, its troubles have become a virus that could infect the entire UB Group. Mallya’s cash-rich liquor business has been drained before for glamorous acquisitions and lifestyle needs. But that was a manageable burden. An airline is too heavy a load. Mallya is eloquent in his litany of reasons for the crisis.

He blames everyone and everything-bar himself.

His foray into the airline business has cost the shareholders of Ub’s holding company, shares of which are currently trading at Rs 82, almost four times lower than their 52-week high of Rs 315. This is the price paid for vanity management.

Mallya needs someone to rescue him urgently. **By how much? For how long?** His pride has stopped him from asking the Government for a bailout. Banks are reluctant, having already offered him a generous package in March 2011, when they converted a substantial portion of debt into equity at a premium that raised more than one question. But there are potential saviours. The Tatas have reportedly made an offer, valuing the company at Rs 30 a share. That is a 50 per cent premium on Kingfisher's share price in the second week of November but is well below the Rs 81 mark that Kingfisher recorded in November 2010. Mallya has spoken to Reliance boss Mukesh Ambani to explore his interest. So far, Ambani has formally denied any inclination to buy into the struggling airline. India today reported that the white knight may well be an Indian business group flush with cash which also owns a private equity fund of substantial size. Mallya has someone lined up. He told India today after his press conference in Mumbai on November 15 that "if I was asked a direct question-have you received a direct offer from an Indian investor-the honest answer is yes."

There is speculation that Sahara promoter Subrata Roy, who bought into Mallya's Formula One team earlier this year, may be interested in making a comeback to aviation after selling out to Jet Airways in January 2006.

Over the last six years, he has leveraged personal equity of Rs 3,593 crore in the airline with banks who have committed Rs 7,057 crore in loans. In the last 12 months alone, Mallya has put in Rs 780 crore of his own or associates, of which Rs 150 crore came in the last month.

The UB Group is suffering. The performance of six of its listed companies has been seriously impaired by the focus on Kingfisher. Its market capitalisation has halved from Rs 45,134 crore to Rs 21,308 crore.

Questions for Discussion :

1. What were the reasons for Kingfisher being unable to earn profit from its date of inception?
2. Will Kingfisher sell its Assets to meet its debts?
3. What can save Vijay Mallya's Kingfisher Airlines?
4. Do you think Kingfisher Airlines is draining the resources of the UB Group?

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