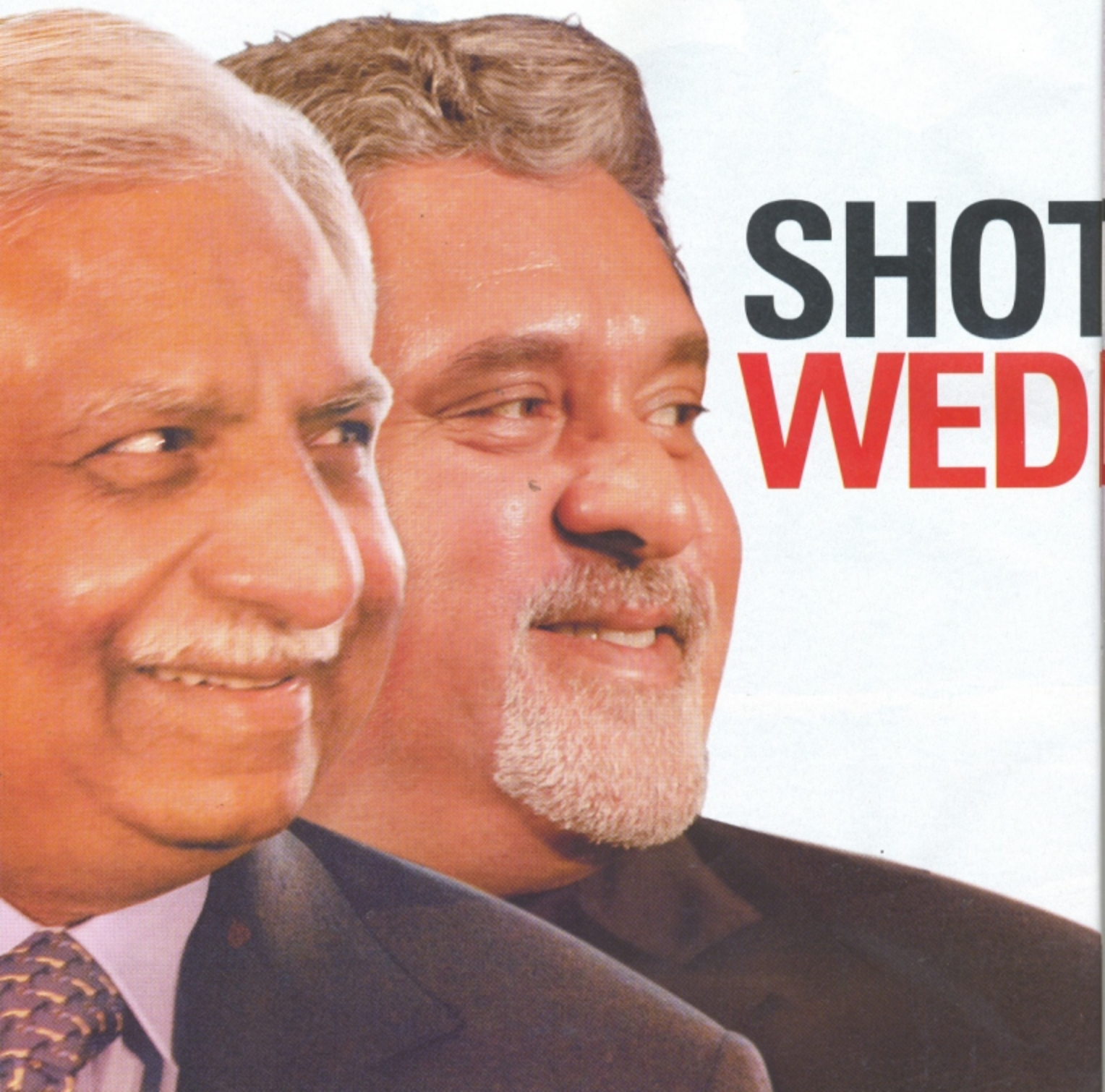


FEATURE JET-KINGFISHER



**SHOT**  
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IT WAS AN UNLIKELY SIGHT, ALMOST surreal. Vijay Mallya standing next to Naresh Goyal, at Kingfisher House, Vile Parle, Mumbai, hand around his rival's shoulder, calling him a friend and a new-found ally. The contrast between the two was as sharp as it is between the red uniforms of Kingfisher's crew and the bright yellow attire of the Jet Airways team. The two had just agreed to work together. The move took

most within the industry, and outside, completely by surprise.

A couple of days later, at an air show in Hyderabad, Goyal called the alliance "a new industrial model"; Mallya said it would lead to "a quantum leap forward in the evolution of Indian aviation".

Despite all the abrupt camaraderie that was deliberately on display, the world wasn't buying any of those glib lines. Two questions kept coming back. Will the two stick together? And, will this alliance pass regulatory scrutiny given its potent anti-competitive undertones?

"There has been no prior instance when the top airlines (in a country or region) have combined to form an alliance," says Ankur Bhatia, Executive Director, Bird Group, which manages airline-ticketing system Amadeus in India. "This will definitely lead to a monopoly of full-service airlines in India."

In one stroke, the combined entity—including Jet-owned JetLite and Mallya's Kingfisher Red (formerly Air Deccan)—control about 1,000 flights a day, both domestic and international, with a fleet of 189 aircraft. More importantly, it gives the alliance almost 60% share of the passenger market, handing it brute power in setting fares. In contrast, the nearest competitor, state-owned Air India, has just around 18% share of the market.

The second concern is that there is not enough glue to hold the alliance together. Both Mallya and Goyal are imposing and strong-willed personalities in their own way, just as Kingfisher and Jet are two very disparate organisations. They have different aircraft types and little room for real synergies. For example, Kingfisher has an entire Airbus fleet, whereas Jet Airways largely has Boeings, except for a few A320s. These are two different types of business models, operating styles and functionalities. "You need to give us time to operationalise the alliance. You will see the results of the association rolling out in the coming quarters," defends Mallya.

What's more, with large-scale route overlap between the two, there has to be a fair amount of give-and-take in deciding which airline will ground a flight and which will fly, in a given time slot. "Most global alliances work with 80% complementarity and 20% commonality in their networks. But in the case of Jet and Kingfisher, the ratio is just the reverse," points out Bhatia. So, to make this work, both have to be willing to give more than what they take. "When two principal competitors become collaborators, this can only be as a means to survive," says Kapil Kaul, CEO (India & Middle-East), Centre for Asia Pacific Aviation, a consultancy firm.

## Root Cause

The current economic situation is really the shotgun that's brought the two rivals together. The sharp rise in aviation jet fuel price for most part of this year, followed by the international liquidity squeeze, has taken a dramatic toll on the Indian airline industry, which is expected to tot up \$2 billion of losses in the current fiscal year.

Indian carriers experienced negative growth in passenger numbers for the first time in five years. For instance, the last four months till October this year, fewer passengers flew—the drop ranged anywhere between 11% and 22% month-on-month, compared to the same period last year.

Most carriers, including Jet and Kingfisher, have already effected a cut of 15-25% in their capacities in the last three months, putting on hold ambitious network expansion plans, both in domestic and international markets. Airline executives indicate that they may have to take out capacity by another 15-20% over the next six months if the downward trend in passenger numbers continues. This

## Marriage Of Equals

	Kingfisher, Kingfisher Red	Jet, JetLite
<b>Market share</b>		
Frequency share (%)	29.9	28.7
Capacity share (%)	24.0	27.9
<b>Service</b>		
Cities in India	64	44
Cities Overseas	1	20
Flights per day	479	530
Number of routes	139	136
<b>Fleet</b>		
No. of aircraft	81	108
Types of aircraft	Airbus 319, 320, 321	Boeing 737, Airbus 330, Airbus 72, CRJ200
<b>Valuation</b>		
Market cap (Rs cr)	862.9	1,479.3

Financials for 2007-08, market cap as on October 24  
Source: OAG Max Online, CMIE Prowess

# THE GUN DING

Arch-rivals Vijay Mallya and Naresh Goyal have come together, but only because they both have a gun to their heads. How long will the marriage last?

“Joining Jet and Kingfisher would depend on what value it brings us. We will wait for the alliance to get operational first

— M Thiagarajan  
Managing Director, Paramount Airways



There are payment issues that have resulted from the financial crisis, but nothing to be too scared about really

— Kiran Rao  
Executive Vice-President, Marketing & Contracts, Airbus



“Code-share agreements would hold the key to success or failure of the alliance

— Dinesh Keskar  
Vice-President (Commercial), Boeing India



There has been no prior instance when the top airlines in a country or region have come together to form an alliance

— Ankur Bhatia  
Executive Director, Bird Group



essentially means that many more aircraft would be grounded, along with pilots and crew. “It is much cheaper to keep aircraft on the ground than fly them,” says a senior Kingfisher executive.

Rival airline companies too are keeping a close watch on how the alliance shapes up, though most term it as a ‘marriage of convenience’. Some industry sources, in private, confide that they have received feelers to join the bandwagon. After a lot of cajoling, M Thiagarajan, Managing Director, Paramount Airways, concedes that he is open to the idea. “It all depends on what value it brings to Paramount. We will wait for the alliance to get operational,” he says.

The industry is also desperately short of cash and recently pleaded with the government for a \$1 billion bailout package. “There are payment issues due to the financial crisis, but nothing to be too scared about,” says Kiran Rao, Executive Vice-President, Marketing and Contracts, Airbus. He has supplied aircraft to both Kingfisher and Jet. “The alliance will make them stronger. It is better for us to see healthy airlines.” This bleak scenario will

force the two to work together for the time being. But what happens when things start improving?

### Rules Of Engagement

Alliances are fairly common among global airlines. Star Alliance is the world’s largest, with 21 full and three regional members. Sky Team has 11 members and three associate airlines, and One World Alliance comprises of 10 airline members.

But there hasn’t been a monopolistic scenario emerging from any of these. That’s because the members come from different markets. When the Star Alliance was created, the idea was that the strengths of United Airlines in the US would become accessible to German Lufthansa, and the advantage that, say, Singapore Airlines has

in Asia would become advantageous to another carrier in the alliance.

Moreover, each carrier did not have to invest and develop a base, facility, terminal area and lounge in every geography; it could access those of a partner that had already invested in these facilities there. “Most of these alliances feature the biggest American airline with the biggest European one, or the biggest European with the biggest Latin American or African carrier,” says Mark Martin, Senior Advisor, KPMG India.

But what Jet and Kingfisher are proposing to do just can’t be compared with such alliances. “The concept and purpose of the alliance between Jet and Kingfisher is very different from the above alliances,” says Bhatia. “In a growing market, chances are this alliance could be viewed as anti-competitive and would come under the scrutiny of regulators,” warns Kaul.

### Where Is The Flight Plan?

Although the two companies are yet to spell out the finer details, the broad contours of the alliance have been disclosed. It includes joint marketing through code-share agreements, both on domestic and international flights, interline agreements that allow the airlines to pick up each other’s passengers, network rationalisation to cut unviable routes and frequencies, sharing of infrastructure facilities and recognition to each other’s frequent-flier programmes. But there is no equity participation. “Code share would be the key to success of the alliance,” says Dinesh Keskar, Vice-President (Commercial), Boeing India.

Although Mallya touts a figure of Rs 1,500 crore in cost savings each year through the alliance with Jet, he does not explain how they plan to reach the mark. A senior Kingfisher executive indicates that around 50% of that figure would be accounted for through rationalisation of existing routes. None of them just seem ready to answer how they plan to share the gains from this alliance among themselves. “We have deliberately kept the scope of the alliance flexible. It will gain shape as we go forward,” explains a senior Kingfisher executive.

But the biggest gains will perhaps be on international routes. Goyal highlights the need for Indian carriers to have a common

**Both Vijay Mallya and Naresh Goyal are imposing and strong-willed personalities. Kingfisher and Jet are two disparate organisations—they have little room for real synergies**

# “We want to cut costs”

Jaen Albrecht, CEO, STAR Alliance, explains how the world's largest alliance works without ruffling feathers

## How does STAR help members handle cyclical fluctuations in the sector?

The Alliance can help carriers cut cost without reducing the quality of the product. Our important projects include moving members together in the same terminals, building common lounges, helping the carriers build efficient hubs to reduce costs. Also, we work with the carriers to maintain network coverage. When a member carrier opts to reduce routes and frequencies, another may step in by flying its own aircraft or by providing the withdrawing carrier a 'piggyback' ride through code-sharing so that the portfolio of destinations the first carrier can sell under its code remains intact despite the physical schedule cutback. Also, the alliance has developed new technologies to help carriers evaluate the benefits of code-sharing, and determine what

works best for them. Other areas of the alliance—IT, sourcing, fleet, marketing—all work with carriers to find ways to save costs and increase revenues through common purchasing, improving fuel-efficiency and technology. We work on two fronts: saving money and producing products that build revenue. Both are important, especially in today's economic climate.

## Are more airlines inclined to join global alliances in downturns?

We don't see any such link, as new carriers need to bring benefits for the alliance and the other member-carriers also need to benefit from a new member joining—it needs to be a win-win situation. If you look at the recent joiners—Air China, EgyptAir, Shanghai Airlines and Turkish—all four carriers operate in emerging markets, where the alliance needs to be present and from which the respective carriers need to provide global air transportation.

## When will Air-India join the alliance?

The integration process is on and is expected to be over in 2009.



front against foreign carriers flying in and out of the country. “Foreign airlines have been dumping capacity, as they know we don't have the resources to fight them,” he says. Currently, foreign carriers command almost 80% of traffic to and from India. “Indian carriers can together bring a lot of revenue back into India—instead of losing it to foreign carriers,” says KPMG's Martin. “It has the potential of becoming an India

Alliance—that can go into the world to bring in revenue and foreign exchange.”

## Own Making

But, if Jet and Kingfisher have come to record such big losses (each reportedly losing Rs 8-10 crore every day), part of the blame rests with them. Over the last two years, riding on profitless growth in passenger numbers—driven by cheap tickets—the

carriers expanded rapidly in their fight for market share, raising the cost of scarce manpower: pilots, cabin crew, engineers.

The two desperately need the benefits they believe will come from the alliance. But those may not be so easy to reap. Theoretically, consolidation through alliances should lead to better pricing power. But Jet and Kingfisher may not find it easy to force a fare hike in the face of dropping passenger demand. Even valuations are unlikely to improve much.

“Any assumptions that the alliance may help improve the valuations of Jet and Kingfisher are flawed,” says an airline analyst in a Mumbai-based broking firm. In fact, since the deal was announced, Jet's share price has fallen 41% and Kingfisher's 37% (as on October 24); much more than the 23% drop in the BSE Sensex. And if they were looking for savings in manpower costs (there will be excess staff in both carriers when they rationalise their flights), that too has been stymied. Jet recently took back all the employees it laid off.

For Mallya and Goel, working together may well turn out to be as difficult as sparing with each other was. ■

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— Mark Martin  
Senior Advisor, KPMG India



When two principal competitors become collaborators, it can mean only one thing—they're looking to survive

— Kapil Kaul  
CEO (India & Middle-East), Centre for Asia Pacific Aviation

