

REASON BEHIND KINGFISHER AIRLINE'S FAILURE: "AN EYE OPENING CASE STUDY REVEALING THREE KEY WORDS FOR AVIATION INDUSTRY SUCCESS: COSTS, COSTS, COSTS"

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ABSTRACT: Our research paper try to throw lights on some major reasons which were somehow responsible for the current crisis going inside the kingfisher Airlines which can be realized by the press statement from KFA, on 12 March 2012, highlights the challenges:

"The flight loads have reduced because of our limited distribution ability caused by IATA suspension. We are therefore combining some of our flights. Also, some of the flights are being cancelled as a result of employee agitation on account of delayed salaries. This situation has arisen as a consequence of our bank accounts having been frozen by the tax authorities. We are making all possible efforts to remedy this temporary situation."

RESEARCH OBJECTIVE:

The key objective of this research study is to investigate the reasons behind the failure of the Kingfisher airline in the year 2012.

To investigate the government policies and the various steps taken to fix the current crisis.

To investigate the reasons due to which the whole Aviation Industry is suffering from higher operating losses.

What went so terribly wrong with Kingfisher when rival Jet Airways has comparatively much higher debt?

INTRODUCTION:

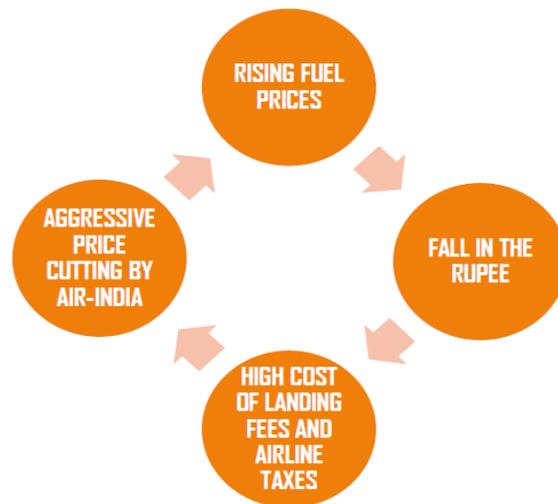
Global aviation industry is passing through challenging times due to unprecedented fuel price hike during the last 4 years, turbulent financial markets and economic recession. Vijay Malaya's dream bird, **Kingfisher Airlines** - popularly known as **The King of Good Times** - is witnessing its worst phase. Indian domestic aviation is suffering from a serious market failure, caused by misguided government policy and ministers need to step in quickly to fix it. In India, most of the upcoming airlines added a large number of aircraft since 2006 and deployed them mostly on metro sectors resulting into suicidal price war among all the airlines. Every airline in India is currently suffering from operating losses.

RESEARCH METHODOLOGY:

The data for the current study are collected from secondary sources such as annual reports, news papers (Economic Times, Business Standards, TOI, etc), and Aviation industry analysis report. In analyzing various parameters, last one year data is collected. The study has been confined to study only the various reasons behind the failure of Kingfisher airlines.

FINDINGS:

- While doing the research, we find that there are four main reasons why Indian Aviation Industry is in so much pain, which can be reviewed as given below:



- Kingfisher's net worth has been completely eroded, while its auditors had raised several questions about its accounting practices in its annual report.
- Kingfisher Airlines Ltd's loan funds stand at Rs7, 543 crore (debt-to-equity ratio of about 3.2) & that of Jet Airways (India) Ltd's is Rs14, 123 crore (debt-to-equity about 4.2).
- Spice jet Ltd, on the other hand, has lowest debt at Rs712 crore (debt-to-equity about 0.7).
- Kingfisher's fixed assets stand at Rs2, 286 crore, but it has a negative net working capital (excluding cash and bank balance) of Rs1, 970 crore. Jet Airways has a much stronger asset base with the value of its fixed assets at Rs14,417 crore; its negative net working capital (excluding cash and bank balances) is relatively much lower at Rs560 crore. Spice Jet has a total fixed asset base of Rs1, 115 crore.

- Kingfisher could not deliver on profitability even last year when the going was considered to be good. According to analysts, the sector experienced its best returns in the quarter ended December 2010. Even during such times, Kingfisher's net loss for fiscal 2011 stood at Rs1,027 crore. That's when Jet had managed a net profit of Rs9.69 crore—on a stand-alone basis—and Spice Jet posted a net profit of Rs101 crore. Spice Jet's net profitability, of course, was also supported by relatively lower interest expenses.
- Kingfisher Airlines share price: Sep-2010 to Sep-2011

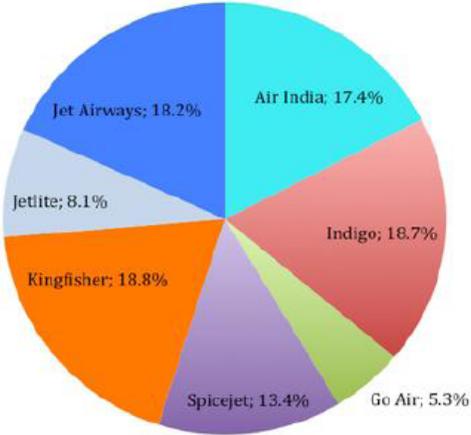


- For the September quarter, Kingfisher's operating losses are higher than the other two, with Jet's operating loss being far lower. Kingfisher's fuel and interest expense (Kingfisher's debt is also probably costlier than that of Jet Airways) as a percentage of revenue is higher than that of Jet.
- A higher interest cost, coupled with higher operating losses, has led to pressure on Kingfisher's ability to service its interest and debt obligations. Further, Kingfisher's current liabilities have increased by 23% in September from March (an indication that it may be
- Stretching payments to suppliers). Naturally, Kingfisher seems to be the worst affected of all the three.
- Revenue growth for Kingfisher domestically was very weak, falling 3% to Rs. 1,184 Crore from Rs. 1,227 Crore

- International Revenue growth was even worse, falling 9% to Rs. 363 Crore from Rs. 398 Crore
- Passengers carried fell 15% to 2.63 million; antithetical to general market trends.
- Domestic Passenger Yield fell 3% to Rs. 3,804 despite capacity discipline.
- International Passenger Yield rose 5% to Rs. 10, 864.
- EBTIDAR Profit (which measures operating results before taxes, interest, depreciation , loan amortization, and rents) of Rs. 125 Crore (Rs. 284 Crore in Q3 10-11), EBITDAR profit of Rs. 161 Crore on Domestic (Profit of Rs. 225 Crore in Q3 10-11), and EBITDAR loss of Rs. 36 Crore on International (Rs. 59 Crore profit in Q3 10-11)
- Kingfisher deferred almost 213.4 Crores worth of losses into future taxes under “Deferred Tax Asset”
- There was a onetime special item of almost Rs. 79.25 crore that contributed to the loss.

RISK MANAGEMENT FAILURES IN KINGFISHER AIRLINES



STRATEGIC RISK – MARKET ANALYSIS	<ul style="list-style-type: none"> ✓ KFA was launched as a premium business class airline. ✓ A lack of understanding of customer requirements and basing a decision that luxury sells in airlines. ✓ Mr. Mallya, highly successful in liquor business, didn't comprehend the differences in customer preferences within the two industries. 																
STRATEGIC RISK – MERGER WITH AIR DECCAN	<ul style="list-style-type: none"> ✓ KFA acquired Air Deccan's international flying rights and simultaneously entered the cheaper market segment. ✓ It became the largest Indian airline with 27.5% market share, and domestic travel increased by 30%, however it didn't make profits. Despite the fact the it's main rival – Jet Airways – continuously showed profitable quarters. <div style="text-align: center;">  <table border="1" style="margin: 10px auto; border-collapse: collapse;"> <caption>Market Share of Indian Airlines</caption> <thead> <tr> <th>Airline</th> <th>Market Share (%)</th> </tr> </thead> <tbody> <tr> <td>Jet Airways</td> <td>18.2%</td> </tr> <tr> <td>Air India</td> <td>17.4%</td> </tr> <tr> <td>Indigo</td> <td>18.7%</td> </tr> <tr> <td>Kingfisher</td> <td>18.8%</td> </tr> <tr> <td>Spicejet</td> <td>13.4%</td> </tr> <tr> <td>Go Air</td> <td>5.3%</td> </tr> <tr> <td>Jetlite</td> <td>8.1%</td> </tr> </tbody> </table> </div> <ul style="list-style-type: none"> ✓ With the merger, it lost its brand image of a premium business class airline. 	Airline	Market Share (%)	Jet Airways	18.2%	Air India	17.4%	Indigo	18.7%	Kingfisher	18.8%	Spicejet	13.4%	Go Air	5.3%	Jetlite	8.1%
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STRATEGIC RISK - INVESTMENT IN PLANES	<ul style="list-style-type: none"> ✓ According to 31 March 2011 ending annual report, KFA flew 366 domestic flights and 28 international flights. It owned 67 aircraft. ✓ Aircraft/engine lease rentals stood at Rs. 984 crore (USD 197 million) during the twelve month period from April 2010 to March 2011. 																
FINANCIAL RISK - EXCESSIVE DEBT	<ul style="list-style-type: none"> ✓ KFA posted a loss of Rs 1027.39 crore (USD 205.95 million) in December 2011 quarter. ✓ As of 31 March 2011, its net worth was negative at Rs 3633.08 crore (USD 728.29 million). ✓ Presently, KFA has a total debt of Rs 7057.08 crore (USD 1414 million) and total accumulated losses of Rs 6000 crore (USD 1202 million). 																
OPERATIONAL RISK – FUEL COSTS	<ul style="list-style-type: none"> ✓ Expenditure on fuel stood at Rs. 2274 crore (USD 456 million) during the twelve month period from April 2010 to March 2011 accounting to 28% of the total costs. ✓ The Indian industry was hit more adversely due to the cumulative impact of Customs Duty and Sales Tax on account of this sharp increase in international fuel prices. 																

All the full-service boys messed up their mergers. Coincidentally, all three – Jet, Kingfisher and Air India – went in for acquisitions and mergers in 2007-08. While Jet bought Sahara, Kingfisher bought Air Deccan and Air India merged with Indian Airlines. The traditional logic of mergers is cost savings and synergy, where two and two equals five. The management ignored the warning signs of stormy weather and failed to navigate the company into safety.

CONCLUSION:

Running an airline in India is a mugs' game. Once defined as the simple business of “getting bums on seats” – more “bums” means better bottom line – the way the Indian industry is being run, one wonders if the “bums” are paying enough for the seats they sit on. Almost paradoxically despite their continual shrinkage in the domestic market, Kingfisher has continued to post solid, if unspectacular operating figures in the domestic market. Kingfisher plans to increase revenues through more efficient operations, while simultaneously controlling costs by shedding some realty assets (including its Mumbai corporate office), entering sale and leasebacks for some Airbus aircraft, and switching some high-cost rupee loans into low-cost foreign currency loans. There has also been speculation the carrier will permanently reduce its fleet of 66 aircraft (the same level as Jun-2010) to 35 aircraft. Kingfisher Airlines is also working “aggressively” with a consortium of banks, which hold a 23% stake in the company, to further reduce interest costs and raise working capital.

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