29 . Aer Lingus is a small airline which must reconcile itself to becoming smaller

£500m fleet that landed Aer Lingus in a crisis

Persistent losses in air travel operations have undermined the financial stability of Aer Lingus, and today's board meeting faces its grimmest agenda in years. Jim Dunne reports

AER LINGUS has one of the most modern fleets of short-haul aircraft in the world — and therein lies the root of its current financial crisis.

The airline implemented a spending programme in 1987, paying more than £500 million for 28 new aircraft, and total debt now stands at £580 million. Net debt as a percentage of shareholders' funds is 133 per cent, a level at which Aer Lingus could be fairly described as working for the banks; the interest bill last year was £58 million.

Today's board meeting will consider a demoralising combination of cuts and asset sales. Aer Lingus is a small airline by world standards and must now reconcile itself to becoming smaller.

The objective for the air transport side of the business is to become profitable or at worst break even. The persistent losses in the basic role of flying people from A to B has undermined the financial stability of the group despite the profits earned elsewhere in the group (see accompanying graphic).

The Minister for Transport, Tourism and Communications, Mrs Geoghegan-Quinn, will attend today's board meeting. She will hear details, *The Irish Times* has learned, of an interim report prepared by the management to deal with the deteriorating financial position.

The proposed measures include a significantly smaller presence for Aer Lingus in continental Europe and a corresponding decrease in personnel. The report does not specify job cuts by numbers, but suggests that the slimmed-down Aer Lingus will require 1,000 fewer man-years.

The cuts will be across the board, from pilots and cabin crews to support staff in all areas, including sales and marketing and ground personnel. However, payroll costs may be reduced by means other than straightforward redundancies. For example, Aer Lingus's newest batch of entrants have written into their contracts of employment the acceptance of compulsory or voluntary leave at times of financial difficulty for the airline.

The report points out that Aer Lingus is in no position to fund an expensive redundancy package. It also firmly states that the winter schedule on the Atlantic route will remain in place, with two jumbo jets allocated to this sector. Aer Lingus is seeking a lease customer for the third jumbo jet in the fleet.

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fortably into the strategic vision of the group.

The simplest assets to dispose of would be hotels. Aer Lingus owns the Copthorne chain in Britain and properties in France and Belgium. It is an investor in Irish hotels, including the International Hotel at Dublin Airport.

Aer Lingus plans to spend £20 million over the next five years on a chain of budget hotels in Ireland with a joint-venture partner, Forte. The current thinking of Aer Lingus management is that the sale of hotels would be a poor strategic move — unless they were offered an exceptional price for a particular property.

Today's report to the board is an Action Plan Mark Two. The first was introduced in August following the annual general meeting, when a loss of £11.8 million was revealed. What Aer Lingus discovered to its alarm in September was that the first action plan was inadequate to cope with deteriorating market conditions.

A fares war on the routes to London has turned a once-profitable route into a serious loss-maker. A different fares war, from the United States into London has drained away business from Aer Lingus on the Atlantic route, since it is cheaper for an American tourist to reach Ireland via London. It is estimated that over 60 per cent of all US visitors to Ireland now "backtrack" from Britain.

A measure of the growing seriousness of the problem was the abandoning of the so-called fifth- freedom rights over Manchester and Bristol. Aer Lingus scrapped its services on the Dublin-Manchester-Amsterdam, Dublin-Manchester-Paris and Dublin-Bristol-Düsseldorf routes.

Earlier this month, the airline announced it was reducing its Dublin-Gatwick service from three flights a day to one a day. Within a week, this decision was revoked and Aer Lingus will now leave Gatwick altogether.

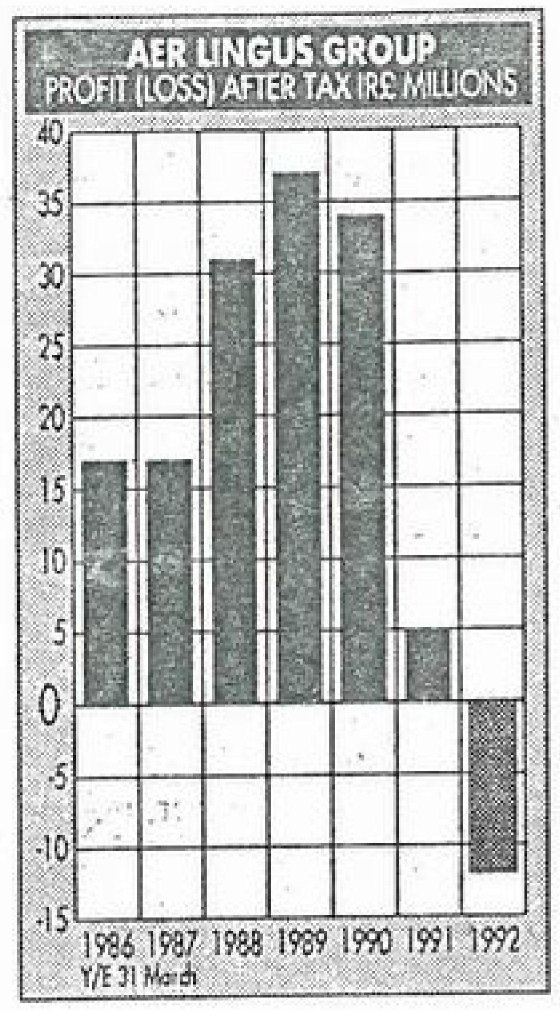
The question of an equity injection by the sole shareholder — the State — is not likely to be raised with Mrs Geoghegan-Quinn today, but the thought will be on everybody's mind. Both SIPTU and the Irish Airline Pilots' Association have been canvassing that solution to Aer Lingus's debt problem.

SIPTU argues that over the years the shareholder has invested £68.6 million and now owns a company which is valued at £600 million at least.

"The State borrows the money to invest in many areas which generate no financial return," SIPTU says. "But the investment in Aer Lingus yields a clearly measurable return in capital growth, dividends and especially jobs." (Aer Lingus employs a total of [illegible] people, 7,600 of them in Ireland. It has added nearly 2,000 new jobs in Ireland since 1987.)

Apart from the current debt burden, exacerbated by recession in the principal markets, Aer Lingus needs urgently to replace its elderly fleet of jumbo jets. All three are over 20 years old and maintaining them becomes more expensive by the year. A new Boeing 747 costs about $100 million, a sum out of reach for Aer Lingus under its present capital structure.

Even if Mrs Geoghegan-Quinn is receptive to the unspoken request for capital, her colleague, the Minister for Finance, Mr Ahern, will not be



RESULTS BY DIVISION

	1991/92 IR£ million	1990/91 IR£ million
Air Transport		
Turnover	499.2	499.6
Loss before interest	(8.8)	(19.6)
Interest	(29.1)	(22.9)
Loss before tax	(37.9)	(42.5)
Airline Services (including maintenance)		
Turnover	158.7	158.9
Profit before interest	17.8	21.0
Interest	(3.2)	(0.3)
Profit before tax	14.6	20.7
Hotels		
Turnover	94.3	78.5
Profit before interest	20.6	17.4
Interest	(8.6)	(5.0)
Profit before tax	12.0	12.4
Commercial Holdings		
Turnover	96.8	76.2
Profit before interest	7.0	12.8
Interest	1.2	3.2
Profit before tax	8.2	16.0
Group		
Turnover	849.0	786.2
Profit (loss) before tax	(3.1)	6.6
Taxation	(8.6)	(1.6)
Minority Interests	(0.6)	0.9
Extraordinary Items	0.5	2.4
Profit (loss) for the year	(11.8)	8.3

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On the issue of asset sales, the management is desperately trying to avoid strategic mistakes which, for example, saw the demise of one of the pioneers of civil aviation, Pan American.

Aer Lingus has quietly sold the Canadian ATS company, which manufactured automated systems for US$10 million to a consortium led by the existing staff. That sale, Aer Lingus says, was because the business did not fit com-


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Bord Failte was dismayed yesterday at the prospect of Aer Lingus reducing further its capacity to bring tourists into Ireland. In 1991, according to SIPTU, 58 per cent of visitors arrived by air and Aer Lingus carried 75 per cent of the total. Wearing another hat, Mrs Geoghegan-Quinn will be concerned about this, but her capacity to give the Aer Lingus board any support other than moral is severely limited.

War and currency turbulence buffet Europe's carriers

The international airlines have lost a total of $6 billion in recent years, **Paul Duffy reports.**

FOR EUROPE'S airline industry the heady profits of the late 1980s vanished as the 1990s started. 1990 was a particularly difficult year for the industry as the war clouds began to gather over Iraq and the Middle East.

Oil prices rose rapidly, which greatly increased operating costs, and passenger numbers and fare yields fell just as quickly, squeezing the carriers from both sides simultaneously.

Thus, the authoritative American journal *Air Transport World* calculated that industry losses worldwide for 1990 came to $3.9 billion. For 1991 it eased to a still substantial $2.1 billion.

High interest rates and heavy fluctuations of the hard international currencies have also hit the industry, coming at a time when there is mounting pressure — instigated initially by the manufacturers in the early 1980s — on airlines to replace their fleets (many still with worthwhile economic life) with quieter jets.

These aircraft enjoy perhaps a 10 per cent reduction in operating costs, which makes little impression on the lease or capital costs of a new generation jetliner, which will have a price tag ranging from $25 million (for a Boeing 737-500) to $125 million for a 747-400.

Traffic is only now returning to pre-Gulf War levels on many international routes, where predictions of a sustained annual growth of six per cent had enticed carriers into contracts for new fleets of aircraft.

Europe has had its own difficulties. As EC policy moved inexorably towards deregulation (due to start in January 1993) the giant carriers in Europe — Lufthansa, Air France and British Airways — moved quickly to secure new routes and take over smaller companies, or to start new associate companies.

In Germany, Lufthansa now controls 97 per cent of all national commercial aviation and it seems set to expand eastwards into the former USSR at a quickening pace. It came as a considerable shock to Lufthansa after more than 30 years of net profits to report a 1991 loss of $288 million.

Air France has in the last few years increased its control over the country's commercial aviation by taking majority holdings in all its major national competitors. In the last two years it has recorded losses — $162 million in 1990 and $107 million in 1991. But it has consolidated itself into a strong position to benefit from the open skies policy in the next few years.

British Airways has become the outstanding commercial success in European aviation. For many years it enjoyed the support and privileges of state ownership. When Mrs Thatcher mandated Lord King to privatise the airline, he set about converting it into an outstanding capitalist model, and in the last few years it has become one of the world's most profitable operators.

Only Hong Kong's Cathay Pacific and Singapore Airlines have earned more; both enjoy a high percentage of profitable business class passengers.

But substantial bail-outs were needed for Belgium's Sabena and Spain Iberia airlines and even Air France needed a helping hand. This was frowned upon by the supporters of the open market but quickly ignored.

Aer Lingus also suffered from the recessionary effects of the Gulf War. Its Atlantic services were hard-hit by the consequent reluctance of Americans to leave their country, and particularly to head in the direction of the conflict.

Its fleet of Boeing 737s dated mostly from the late 1960s and early 1970s and were due to be replaced. So in the last few years the essentially unprofitable airline division of the Aer Lingus group has found it necessary to add new aircraft, some bought, some leased.

The interest and lease charges alone resulting from these are quoted in the group's annual accounts at £29 million for 1991/2, but total interest paid by the group in that year amounted to no less than £57.9 million.

And although increased competition on the London route has resulted in Aer Lingus holding its market share of passenger numbers, there has been a price to pay in substantially lower fares. Today, the airline loses at least £8 for every passenger it carries on this route. Many of these fares are paid in sterling and the recent fall has contributed to the airline's problems.

Paul Duffy is an aviation industry analyst.