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The Fall of King of Good Times: Reasons behind Kingfisher Crisis

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Abstract:
Kingfisher airline was a former airline group headquarter in India. From a distant view, with growing market share in aviation sector, increasing number of destinations and a series of awards showed a very glamorous picture for the company. However by the end of 2011, a huge financial crises was uncovered from the books of the organisation. Starting in 2005, Kingfisher airlines had a short but lasting imprint in the history of Indian aviation sector. Debates followed of another case of window dressing to wrong strategic moves adopted by its overly ambitious owner Vijay Mallya. This paper is an attempt to highlight the reasons behind the financial debacle of kingfisher airlines from the point of view of mistakes in strategic decision making. The research methodology has largely been secondary in nature. After collection of factual data and the strategic decisions that followed since its inception, a methodological analysis revealed several strategic mistakes in the financial as well as managerial structure of the kingfisher airlines. The paper also discusses the significance of this particular case study for the aviation sector and proposes future scope of actions and learnings for the management.

Keywords*: Kingfisher airlines, aviation sector, financial crisis, strategic decision making*

1. Introduction

Right from its inception days since 2003, Kingfisher Airlines has promised to be an innovative and customer oriented company. Its strategies could be rightly termed as market firsts and was a pioneer of revolutionary flying experience in the Indian aviation industry. From treating its customers as guests and not passenger kingfisher airlines was a hit with people. In 2007, just couple of years into operation the over ambitious owner of Kingfisher Airlines, Vijay Mallya decided to merge with Air Deccan a pioneer low cost flying company. With its brilliant customer attracting and glamorous communication strategies and service of competition to five star flights, Kingfisher Airline climbed the charts fast and was first Indian flying company to win several international flying awards. As on 2011 kingfisher had the largest market share of 20% of the entire domestic aviation industry (see Figure 1). It also had highest number of passengers.

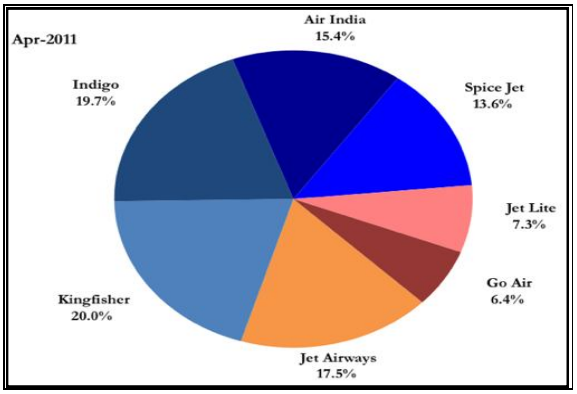

Figure 1 : Market share of Aviation sector as on April 2011

Within 5 years since it came into operation, Kingfisher airlines bagged series of aviation awards including 5 star airlines award by Skytrax for 3 years in a row. However, there was a dark side to this glory. Since it came into operation, Kingfisher Airlines hasn't pulled up to post profits. Following is a summary of financial results of Kingfisher Airlines (see Table 1):

#	From	To	Months	Total Income	Cost	Net Profit	EPS
01	Apr-05	Jun-06	15	1,352	1,689	-337	-68
02	Jul-06	Jun-07	12	2,142	2,562	-420	-42
03	Jul-07	Mar-08	09	1,546	1,734	-188	-11
04	Apr-08	Mar-09	12	5,577	7,186	-1,609	-55
05	Apr-09	Mar-10	12	5,271	6,918	-1,647	-54
06	Apr-10	Mar-11	12	6,496	7,523	-1,027	-16
07	Apr-11	Sep-11	06	3,410	4,142	-732	n/a
Total			78	25,793	31,754	-5,960	

Table 1: YoY financial results of Kingfisher Airlines

Kingfisher airlines in many instances in the years followed by its inception had shown signs of its liquidity vulnerability. In the past several years, Kingfisher airline has had trouble paying their fuel bills. The oil companies allege that Kingfisher owes them almost Rs 200 crores in dues. Cases were also filed against Kingfisher airlines by GE commercial aviation services and DVB Aviation Finance Asia Ltd in 2011 for not paying aircraft lease rentals on time. Adding to it was the news of its bank accounts being frozen for non payment of taxes and strikes by staffs for non payment of salaries. Kingfisher red, the low cost carrier of KFA was shut down in Sept 2011.Over 100 pilots had resigned by November 2011 for non payment of salaries and over 50 flights were being cancelled daily till 19th November 2011. It was announced that company has incurred substantial losses that have accumulated over the years and that the company's net worth has eroded. The financial reports released in the last quarter showed companies terrifying financial health with high interest dues on debt and liquidity crunch. In Jan 2012, several group of bank creditors lead by SBI declared kingfisher airlines a Non Performing Asset. In 2012, the aviation authorities refused to renew its license till existing dues are paid by the company. In July 2014, it was listed as countries highest NPA.

2. Reasons for financial turmoil

A systematic study of the economic environment during the period and several wrong strategic moves of Kingfisher Airlines highlight the reasons that culminated into one of the biggest financial debacles aviation industry has ever witnessed. The critical reasons are:

2.1. Cannibalization by Kingfisher Red

Vijay Mallya assumed that he could succeed by his old tactics of stylising and glamorising the services offered by Deccan and adding extra services and frills. For instance, meals, newspaper and other entertainment services that were available with other full service fleets were introduced. Mallya thought that by providing more facilities he will be able to extract more money. However, it was in contradiction to the very core low cost operating structure and philosophy of Air Deccan.

What followed was a rebranding exercise under which the Deccan brand was brought under the parent brand name and introduced as Kingfisher Red. This led to a blurring of the brands as there was hardly any distinction between the full service (represented by Kingfisher) and the low-cost brand (Deccan/Kingfisher Red). Both brands looked similar and had a similar service. Kingfisher Red became neither full service nor low cost. It was floating somewhere in the middle of the two classes. This blurring eventually led to cannibalisation of parent company brand name as Kingfisher's full-service economy passengers were left wondering why they should be paying extra when they could fly cheaper on the Kingfisher Red service.

2.2. Flawed Strategies after Merger

Mallya assumed that his market leader concept will succeed in the aviation sector just as it did in the breweries business. However, it proved to be a costly mistake with the cost of acquiring Air deccan and a quick expansion into full fleet airline expanded the liquidity crunch in the financial statements.

As Kingfisher Red became slightly costlier thanks to Mallya 's desire to make it "stylish", passengers migrated to other LCCs such as Spice Jet and Indigo, thereby hitting the occupancy of the mother brand as well as the subsidiary stepchild, adding to Kingfisher's woes. The very core competitive edge with lost cost airlines is that without meals, entertainment stations and luxury seats, aircraft becomes light and more fuel efficient. Vijay Mallya and his team overlooked this. Another reason for the crisis was Mallya's decision to go international even before his domestic operations became profitable.

It cannot be said the Merger with Air Deccan was fully a wrong decision. Kingfisher Airlines had got an opportunity to achieve economies of scale by expanding its operations in terms of routes and passengers. The merger provided cost synergies up to the value of 300 crores. It was also a boost in kingfisher earning a major chunk of market share. However, the major issue with the merger was that kingfisher airlines and Air Deccan were both structurally and philosophically different airlines. There were conflicting clues and ideologies in terms of services, business model and target market. Kingfisher airlines also didn't practice fair role of parent brand and suppressed value of Air Deccan in its operating model. Whenever there was schedule class of kingfisher with Air Deccan, Kingfisher got an upper hand. Vijay Mallya known for his flashy style seemed uncomfortable managing a budget oriented business. Mallya tried to persuade customers to try its premium brand at cost of Kingfisher red, but the customers instead switched to other low cost companies. Such policy errors led to complete shutdown of the low cost carrier.

2.3. Low Customer Base for Premium Class

Vijay Mallya went wrong in perceiving the price market trends for Indians. Unlike in U.S.A and other countries Indian consumers are not mature enough to compare the high pricing with quality. They would rather prefer a low cost carrier despite of fewer luxuries. The Kingfisher brand was strong. The product was good. But the strategy Mallya used was wrong. Kingfisher is not only a full service but a full service premium brand. You cannot expand premium market beyond a limit because people who can afford it are a limited number. Kingfisher only targeted top of the pyramid to succeed while the real potential market was at bottom where there is an inexhaustible customer pipeline.

2.4. Flawed Financial Model

Money managers have also found fault with Mallya's financial model of having one of his businesses to guarantee another. Many of his holding companies have already been pledged as collateral for loans. Also, with Indian stock markets being the worst performers in Asia this year, selling equity at home would be counterproductive. Raising debt at home would be equally hurtful since the borrowing costs in India are the second highest in the region. The fall in the value of the rupee – down to its lowest level in 32 months and faring the worst among Asian currencies – has only made matters worse.

Analysts say Mallya could have easily raised funds through equity when his airline merged with Air Deccan in April 2008. Kingfisher's stocks were high and its debt levels were still low at the time, but Mallya chose not to do so as he was reluctant to accept terms of private equity investors. This was a mistake. Besides bringing funds, private equity participation would have ensured some discipline in the airline.

2.5 High Fuel Prices

Indian carriers operate at cost levels that are probably the highest in the world. In India, jet fuel costs 50 per cent more than the global price. Fuel cost can be as much as half of the total operating costs of an aircraft. With the government of India's high taxation policies, Jet fuel costs 40 times more expensive in India than other Asian cities. With jet fuel prices rising further, domestic airlines are expected to lose thousands of crores every quarter.

2.6 Policy Issues

Adding to the poor plight of domestic airlines are the rigid and unproductive policy issues. For instance many leaders and experts have expressed concerns over having to fly unprofitable routes in order to maintain connectivity in the nation. Vijay Mallya in a press conference said it's our duty to fly loss making routes which adds to the miseries of income statements. Add to it the higher sales tax intensifying their hardship

2.7 Price Wars

The airline industry has been engaged in a price war for years, in the absence of a regulatory mechanism that prevents predatory pricing. That's a double whammy – while fuel costs are among the highest in the world, the fares in India are among the lowest in the world. The intensified competition with more and more flash sales have made Indian domestic airlines virtually handicapped in rising travel prices. Vijay Mallaya himself favoured the idea of raising prices to improve the plight of his company but he knows it's not going to work in the price intensive Indian market.

The price wars aren't helping anyone but the ultimate customers. No airline has a significant share of the market so that it could act as a price leader and affect prices. Rather all airlines act like rats in the race to attract passengers cutting each other's business at the cost of their own margins. So until there is a larger consolidation of firms, stabilisation of the price in the airline industry is of serious concern for future.

2.8. Over ambition

Mallya perhaps wanted to be Rinchard Branson of India to quickly. With heavy losses mounting already and firm failing to break even domestically, Mallya decided to expand its fleet in international skies. This further added burden on the red line in the balance sheet.

3. Conclusion

Vijay Mallya tried to apply his drinks business model of glamour and frills in the management and operation of his new airline business. There was no doubt from the beginning that its services were in line with international standards. It was popular with the passengers with most customers giving a positive review, but that does not cover the economic vulnerability of the brand.

Indian aviation sector has seen impeccable growth and revolution which will go on in coming years. Many airlines have come and gone while others have come and acquired a strong foothold in the business. Kingfisher started on a good note. An ambitious project by a well known brand fell flat due to mismanagement and wrong strategic decisions by Kingfisher group. Vijay Mallya can be criticised for it seems entered into the business to acquire a glamorous status rather than trying to exploit the business opportunity that it brought along. There are larger lessons to be learnt from this case. It highlights the need to understand each sector's market dynamics in a isolated view and by strongly understanding consumer behaviour of a particular market segment. This is where companies like spice jet, and indigo are earning advantage.

One main factor that tied the hands of kingfisher in coming up the drowning boat is the price war. The greediness of competitors has created unhealthy competitive environment even if it created problems for themselves too. This strategy cannot sustain for long and is a threat to sustainability and stabilisation of the aviation sector at large. With FDI at doorstep and many international brands entering the focus should be on creating a healthy competitive environment, improving quality of service and coming in unity to find solutions to problems manning aviation sector such as security, fuel prices etc.

Mallya who owns business from breweries, cricket team to F1 team did a mistake of neglecting one of most sensitive and competitive business segment : aviation sector. As of now Mallya is the only board member left holding on to the brand. Kingfisher still has over eight billion in dues and creditors do not seem to be getting them any time soon. Jet Airways and Spice Jet are likely to reap some benefit out of Kingfisher's plight for a long time. Having said that, higher fuel prices, a weak rupee, growing competition with entry of Air Asia and policy rigidness will continue to remain a concern for the old players in the near future.

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