BUSINESS PLAN TO STIFLE GROWTH?

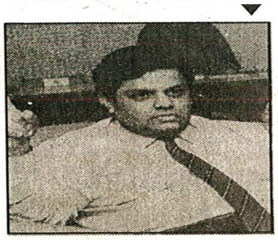
The Sunday Leader and/or the public is yet to receive from the Public Enterprise Reform Commission [PERC], clarifications and/or explanations and/or answers to the several queries posed and issues raised in the public interest on the privatisation of Air Lanka Ltd.

This has been so, notwithstanding PERC having published in the *Sunday Observer* of May 24, 1998 PERC's answers to summarised allegations made by the Opposition during the debate on the Air Lanka privatisation in Parliament on May 19, 1998 and Chairman PERC, Dr. P.B. Jayasundera and Director-General, PERC, Mano Tittawella having also endeavoured to meet public criticisms and proffer clarifications and explanations through an interview published in the May 1998 *Business Today*. In response thereto, *The Sunday Leader* last week raised several questions and issues that significantly remain unanswered.

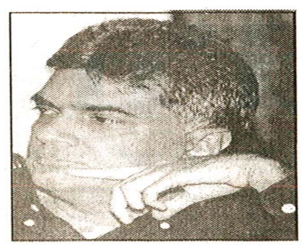
The Sunday Leader this week turns the focus on to some of the core issues, that need to be dealt with in the public interest, pertaining to this controversial privatisation of Air Lanka Ltd. Without any doubt, one of the corner stones of the privatisation of Air Lanka Ltd., has been the Business Plan formulated and forwarded by Emirates Airlines, with a *foreword* thereto by its Chief Director (Airline), T.C. Clark. The Business Plan presented is for a 10-year period, i.e. from the financial year 1998/99 up to the financial year 2007/08. Undisputedly, it is the Government's position, that the privatisation of Air Lanka Ltd., was carried out essentially on the basis of this 10-year Business Plan formulated by Emirates Airlines for Air Lanka Ltd.

BUSINESS PLAN NOT EXAMINED?

Director-General, PERC, Mano Tittawella – "The benefit (of the payment scheme) is fantastic"



Who were the competent experts who examined the 10-year business plan of the national airline of the country? Was the plan subjected to discussion and review by the senior managers and directors of AirLanka?



Opposition Leader Ranil Wickremesinghe – "Any 'clerk' could have prepared such a business plan"

Before dealing with some of the salient features of this 10-year Business Plan for Air Lanka Ltd. formulated and presented by Emirates Airlines, one of the major competitors of Air Lanka Ltd., itself, *The Sunday Leader* poses very primary and basic questions in relation thereto. One of them being, as to whether such Business Plan was critically examined and studied by competent independent experts in the airline business industry on behalf of the Government and/or Air Lanka Ltd.? If so, who were the competent experts, who carried out such examination and had they suggested any counter proposals and/or strategies on behalf of the Government and/or Air Lanka Ltd., in the formulation of the 10-year Business Plan for the national airline of this country?

Even more importantly, had such 10-year Business Plan been subjected to strategic discussions, deliberations and review by the management of Air Lanka Ltd., that ordinarily ought to have included the senior corporate managers and the Board of Directors of Air Lanka Ltd.? Accordingly, does such Business Plan comprise of strategies evolved, with the full involvement and concurrence of the corporate management of Air Lanka Ltd.,? If so, what proposals and/or strategies had the corporate management of Air Lanka Ltd., incorporated into such 10-year Business Plan? If not, how and why had the corporate management of Air Lanka Ltd., not been involved in the formulation of its own 10-year Business Plan?

On the contrary, is it the anomalous and incredible situation, that a 10-year Business Plan for Air Lanka Ltd., had been prepared by one of Air Lanka Ltd.'s major competitors in the very region and that such 10-year Business Plan had been accepted on mere face value, without any examination, whatsoever, by those competant and necessary? With no disrespect, *The Sunday Leader,* in the public interest, poses the pertinent question, as to what competence and expertise, the officials of PERC, including Chairman PERC, Dr. P.B. Jayasundera and Director-General PERC, Mano Tittawella, who apparently have carried out such privatisation of Air Lanka Ltd., and have been the Government spokesman thereon, have particularly in the airline business industry, to have dealt with such 10-year Business Plan?

NATIONAL INTERESTS ABANDONED?

Air Lanka Ltd., was not a mere Government owned business enterprise – it was and is the national airline of this country. A 10-year Business Plan ought to have taken into cognisance, various nationally important strategies, in addition to those commercial, particularly at this point of time, when the country has to prepare and gear itself to advent into the next millenium, taking cognisance also of the economic debacles that have befallen many a South East Asian countries, due to political regimes that had been seeped in corruption. Ought not such nationally important perspectives have been taken into reckoning, by those intimately knowledgeable and expertised in the airline business industry and accordingly, had PERC mobilised such expertise to have strategised the formulation of the 10-year Business Plan for the national airline of this country?

The 10-year Business Plan essentially provides only for the replacement of 6 Aircrafts. Since 1995 Air Lanka Ltd., has been operating with a fleet of 9 Aircrafts and the 10-year Business Plan has envisaged the operation of a fleet configuration of only 9 Aircrafts up to the year 2008, demonstrating that there is no vision and strategy in the 10-year Business Plan for any growth of the Aircraft fleet over a horizon of a 10 year period. Is this an acceptable proposition for the national airline of this country, that is preparing and gearing itself to enter the next millenium, aspiring to be a financial and economic center in Asia? In the absence of such strategic foresight over a horizon of 10-years, the Business Plan is a mere financial document prepared to financially justify the acquisition of 6 Airbus Aircrafts from Airbus Industrie, France.

NO STRATEGY FOR GROWTH?

In no uncertain terms, admittedly the privatisation of Air Lanka Ltd., the national airline had been carried out by PERC and/or the Government essentially to purchase 6 new Airbus Aircrafts, replacing 6 existing Aircrafts. Ofcourse, the Business Plan provides for greater utilisation of the Aircrafts, greater penetration into markets, assurance of enhancement of quality of service and increase in levels of revenue over the 10-year period covered by the Business Plan. This is nothing exceptional. Surely, one would expect such factors to ordinarily grow and improve over a 10-year period and such strategies spelt out are mere operational strategies, that one would take into reckoning in the normal operational planning of the business operations of the airline.

The Sunday Leader publishes today the Income & Loss and Cash Flow Statements for the 10-year period 1998/99 to 2007/08 contained in the 10-year Business Plan for Air Lanka Ltd., formulated by Emirates Airlines. The Leader of the Opposition, Ranil Wickremesinghe has gone on record in Parliament, during the Air Lanka debate, opining that any clerk could have prepared such a Business Plan. He had pointed out that the Operating Income for the 10-year period was only US $ 188 million, whilst the bulk of the Net Income, the balance US $ 336 million is anticipated from ground handling and other non-operating revenue sources that arise from rights attached to the Airport. *The Sunday Leader* leaves it to the intelligent public of this country to review these Income and Cash Flow Statements in the context of the poignant observations made by the Leader of the Opposition, Ranil Wickremesinghe.

INCOME AND LOSS STATEMENT
US $ MILLIONS

	ACTUAL		BUDGET	PROJECTIONS										
	1995/96	1996/97	1997/98	1998/99	1999/2000	2000/01	2001/02	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08	Ten Year Total
Scheduled Services Revenue														
Passenger	209	204	208	239	272	330	391	392	398	406	408	431	418	3,668
Cargo	36	35	35	40	46	56	66	66	67	69	69	70	71	620
Excess Bagage	5	4	4	5	6	7	8	8	8	8	8	8	8	74
Mail	2	1	2	2	2	2	3	3	3	3	3	3	3	25
Total	251	245	248	285	325	395	468	469	476	486	488	494	500	4,387
Net Charter Revenue	2	3	0	0	0	0	0	0	0	0	0	0	0	1
Other Operating Revenue	2	1	2	2	2	2	2	2	2	2	2	2	2	17
Total Operating Revenue	254	248	250	287	327	397	470	471	478	488	490	[illegible]	502	4,404
Operating Cost														
Direct Operating Cost	153	155	157	189	195	205	241	252	263	271	278	284	291	2,469
Aircraft Related Cost	61	57	57	51	62	95	107	104	101	99	96	94	93	902
Overheads	89	76	66	70	73	80	84	86	88	90	91	92	93	845
Total Operating Revenue	302	288	280	310	333	380	432	441	451	460	465	470	476	4,217
Operating Income	(48)	(40)	(30)	(23)	(3)	17	38	30	27	28	24	25	25	188
Ground Handling Net Income	13	14	14	15	16	17	18	19	20	21	22	23	25	195
Duty Free Net Income	1	1	1	1	1	1	1	1	1	1	1	1	1	9
Non-Operating Revenue	13	18	15	8	8	8	11	12	14	15	16	19	21	131
Net Income/(Loss)	(21)	(8)	1	1	21	42	67	62	61	65	63	69	72	524
Taxation	1	0												
Net Income/(Loss) after Tax	(22)	(8)	1	1	21	42	67	62	61	65	63	69	72	524

CAPTURED BY A COMPETITOR?

The 10-year Business Plan for Air Lanka Ltd., by Emirates Airlines stipulates that the 1st Class service will be eliminated, the total number of Aircrafts does not increase from the 9 in the Air Lanka fleet today, the number of stations served would fall from 28 today to 25, the yield and seat factor will increase moderately, supported by product improvement, 7 stations will be closed from November 1998, including Amsterdam and Zurich in Europe and Karachi, Bombay and Delhi in the SAARC countries. Such stipulations are from the 10-year Business Plan for Air Lanka Ltd., formulated by Emirates Airlines, one of Air Lanka's major competitors in the very region. *The Sunday Leader* leaves it to the public of this country to judge, the strategic growth envisaged in the 10-year Business Plan for this national airline of the country. Is this nationally acceptable? Is it the strategy to stifle the growth of Air Lanka Ltd., and make it a 2nd Class airline, subordinated to Emirates Airlines, the major regional competitor?

This is what Emirates Airlines, themselves, have admitted in the 10-year Business Plan – " As Emirates is a major player in Air Lanka's markets, commercial strategies will be harmonised between the two partners, including distribution. This will be particularly in the European and Pacific Rim markets. The airlines would thus complement each other's activities in all geographical spheres of operation. Sales offices will be co-ordinated in common stations to enhance the cross-selling of Air Lanka and Emirates, and to achieve cost savings through economies of scale."

INCOMPETENCY OF GOVERNMENT?

Amsterdam and Zurich are important strategic gateways to the American continents and other international destinations. Karachi, Bombay and Delhi would be strategically important in strengthening and developing business and economic activities and relations in the SAARC region, for which the SAARC countries have already mapped out strategies. How could national economic implications and national perspectives be considered and evaluated for a national airline, simply on the basis of Profit & Loss Statements? Ought not the correct professional approach have been to take into reckoning the national and socio-economic benefits for the country and its development and growth, through the processes of cost benefit analysis? When the Electricity Board is privatised are rural electrification programmes to be abandoned on the basis of narrow commercial considerations reflected in mere Profit & Loss Statements? Surely, Chairman PERC, Dr. P.B. Jayasundera being an economist, himself, atleast needs no enlightenment on this!

For the Deputy Minister of Finance, Prof. G.L. Peiris to have underscored and emphasised in Parliament, that Air Lanka Ltd., was privatised essentially to finance the re-fleeting of Aircraft, would it, in itself, not be an admission of bankruptcy in policy and strategies for the national development and growth of the country, which is the sole responsibility of any Government, and would this also not tantamount to an admission, that the Government has abdicated such national responsibility to provide for the country's future growth and development? How could the national airline of a country be handed over on a platter, that too to a major competitor in the very region, on the basic premise that the Government is unable to strategise and fund the country's own airline and its development and growth, that is vitally necessary to support national economic development and growth? What would then be next handed over to foreigners, reminiscent of the colonial regimes of the country?

PURCHASE DRIVEN PRIVATISATION?

What appears to have driven the privatisation of Air Lanka Ltd., has been the purchase of 6 Airbus Aircrafts. Curiously, PERC in its wisdom has not spelt out clearly and transparently the details pertaining to such major and core issue in the 10-year Business Plan. *The Sunday Leader* in the public interest brings into focus some of the salient and relevant features pertaining to such major public procurement, packaged and/or capsuled under the cover of privatisation, that had caused a public hue and cry, raising grave and serious questions on blatant transgression of procurement policies and procedures prevalent in the public sector, including the very procurement policies and procedures laid down in Air Lanka Ltd.'s manual of procedures, applicable to procurements of equipment and supplies of much less significance and of far less value!

Clause 3 of the Purchase Agreement between Airbus Industrie and Air Lanka Ltd., specifies the final price per Airbus Aircraft, as comprising of the sum of the Airframe price of US $ 85,315,000, Standard Specification Changes price of US $ 2,264,000, Buyer Furnished Equipment price of US $ 5,330,000 and Rolls-Royce Propulsion System price of US $ 23,975,000, thereby giving a total price US $ 116,884,000 per Aircraft. Curiously, such price has been defined as the price prevalent in January 1997 and Clause 3.2 of the Purchase Agreement provides that such basic price of January 1997 is subject to a price revision formula to determine the price of the Aircrafts at the time of delivery. By the Letter No.1 annexed to the Purchase Agreement, Airbus Industrie had agreed to give a credit of US $ 13,102,000 on each Aircraft and a credit of US $ 5,000,000 on each Rolls-Royce Propulsion System, thereby giving a net purchase price of US $ 98,782,000 per Aircraft. The said Letter also provides for a cap on the price revision formula on the January 1997 Air frame price at 3% p.a. compounded to the time of delivery of each Aircraft.

COST OF AIRBUS AIRCRAFT

Clause 9.1 of the Purchase Agreement between Airbus Industrie and Air Lanka Ltd., stipulates the delivery of the 6 Airbus Aircraft as follows – Aircraft No. 1 – October 1999; Aircraft No. 2 – November 1999; Aircraft No. 3 – December 1999; Aircraft No. 4 – January 2000; Aircraft No. 5 – July 2000; Aircraft No. 6 – August 2000. On the basis of the price revision cap of 3% p.a. on the January 1997 net purchase price, would not the respective prices for the Airbus Aircrafts be as follows. – Aircraft No. 1 – US $ 107,417,769; Aircraft No. 2 – US $ 107,679,763; Aircraft No. 3 – US $ 107,941,758; Aircraft No. 4 – US $ 108,211,612; Aircraft No. 5 – US $ 109,830,739; Aircraft No. 6 – US $ 110,100,593 thereby giving a total of US $ 651,182,234 *[could be more since the cap of 3% applies only to the Airframe price and not to the Rolls-Royce Propulsion System, Buyer Furnished Equipment and Standard specification changes]*. In such context how did the PERC's official statement in the *Sunday Observer* May 24, 1998 stipulate that – "Therefore, the total cost of the Aircraft purchased is given at between US $ 550 million and US $ 600 million for six Aircrafts to be delivered in 1999 and 2000."?

Furthermore, Clause 5.2.1.2 of the said Agreement provides the pre-delivery payment terms in respect of each Aircraft to be as follows:- Upon signature of the Purchase Agreement – 2% – On the first day of each of the following months prior to the scheduled month of delivery; – prior to 24 months – 5%; – prior to 12 months – 5%; – prior to 6 months – 4%. The balance payment is to be made concurrently with the delivery of each Aircraft.

The Board of Directors of Air Lanka Ltd., had adopted, inter-alia, the following Resolution on March 31, 1998 – "The payment by wire transfer by the Company to Airbus Industrie G.I.E ("Airbus") of United States Dollars of Twenty Six Million Eight Hundred Eighty Thousand (US $ 26,880,000) pursuant to Section 5.2.1.2 of the Purchase Agreement (the "A330 Agreement") between the Company and Airbus (listed as item to Annex 1 hereto), which represents the first instalment of pre-delivery payments for the six Airbus A330-200 aircraft to be purchased by the Company under the A330 Agreement be and hereby is authorized. Such payment shall be made by the Company promptly upon execution and delivery by the Company and Airbus of the A330 Agreement." – Could PERC clarify the reconciliation of the said pre-delivery payment to Airbus Industrie in terms of Clause 5.2.1.2 of the Purchase Agreement?

UNEXPLAINABLE ISSUES

The above two Clauses by themselves, no doubt, appear to be of some queer significance, in that, the pre-delivery payment stipulated of 5% prior to 24 months to the scheduled month of delivery of each of the Aircrafts, would mean that in respect of Aircraft Nos. 1, 2, 3 and 4, that such pre-delivery payments ought to have been paid in October 1997, November 1997, December 1997 and January 1998, respectively, whereas the very Purchase Agreement has been signed on March 31, 1998. How could one explain such glaring discrepancy? Could PERC, who handled these Agreements clarify and explain?

PERC's official statement in *The Sunday Observer* of May 24, 1998 also stated – "The Airbuses will cost about US $ 600 million, but Air Lanka will have 10 to 15 years to pay for them. Spread over a 10 year period, this is not such a substantial amount as made out by the Opposition." – In the interview given to *Business Today* Chairman PERC, Dr. P.B. Jayasundera and Director-General PERC, Mano Tittawella emphatically underscored in their own words – ".... the long-term funding is basically available at 6.68%... 6.68% long-term money is excellent. Anybody who understands money market would tell you that. The benefit is fantastic, both in terms of financing this, and also the purchase price of this Aircraft." The Purchase Agreement between Airbus Industrie and Air Lanka Ltd. has annexed to such Agreement the Letter No. 4 on the subject of financing, which, inter-alia, refers to long-term loan facilities of 10 and 12 years.

Ironically, however, the privatisation of Air Lanka Ltd., with Emirates Airlines has provided for the sale and lease-back of the 6 new Airbus Aircraft at the rate of US $ 900,000 per month as disclosed in the 10-year Business Plan, presumably that is US $ 64.8 million per annum for the 6 Airbus Aircraft, which is given under Aircraft Related Costs in the Income and Loss Statement, included in a total of US $ 902 million for the 10-year period of the Business Plan. The underscoring of the long-term interest rates as excellent and the sale and lease-back of the 6 Airbus Aircraft is not compatible and comprehensible. Ought not the actual financing costs of such arrangements, including the interest costs and charges embedded in the Airbus Aircraft leasing terms, being the major component of the 10-year Business Plan, have been explicitly and transparency explained, more so PERC having so described the deal, as excellent and of fantastic benefit?

Such incompatible strategy is even more confounded, when the Cash Flow Statement of the 10-year Business Plan, has shown a Cash Balance of US $ 501.8 million at the end of the 10th year ! What Business Planning is this?

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