South African Airways – born again?

"Warren Buffett's quip about how shooting down the Wright brothers would have been a great service to capitalism is backed up by ugly numbers. In the entire recorded history of the US airline industry, cumulative earnings have been negative $33bn".
(Lex, 2011)

In early 2021, Pravin Gordhan, minister of the Department of Public Enterprises, faced significant challenges in saving thousands of jobs by getting the national airline flying again. SAA, which had last made profits in 2011, had been burning R500[1]m a month and with liabilities significantly exceeding assets, had entered Business Rescue in December 2019. In the COVID decimated travel industry all the major airlines were facing bankruptcy, bailouts and restructuring, but many questioned the "SAA charade" (Theobald, 2020).

South African Airways

SAA commenced operations in 1934 as Union Airways, flying local routes (exhibit 1 and exhibit 2). Ten years later, the renamed airline opened three-day flights to a burgeoning European market and by 1970 had extended travel options to New York, Sydney and other international destinations – only to see many of these curtailed through economic sanctions against apartheid. Following Mandela's release in 1990, SAA enjoyed a revival through the inclusion of previously disadvantaged individuals as cabin crew and cadet pilots, and the resumption of flights to the US, Australia and elsewhere. An extensive fleet renewal programme followed, with a switch from Boeing to Airbus and an order of 41 new aircraft (SAA, 2021). By 2010, SAA was a member of the Star Alliance and the leading African carrier, boasting passenger numbers more than nine million, three-fold greater than competitors Ethiopian or Kenya Airways. Ten years later the status was reversed, with Ethiopian carrying 13.3m passengers, Kenya Airways 4.9m and SAA only 4.6m (Long Haul by Simple Flying, 2021).

Reasons for SAA's decade of poor performance were legion, with competition being but one. Africa's lucrative destinations had attracted all the major airlines, who carried an estimated 80% of overseas trade. Of the African carriers, Ethiopian was best graphically positioned as a "hub carrier", offering 127 destinations versus SAA's 57 and Kenya Airways' 44. With fuel costs being a major expense, SAA was further disadvantaged in its use of Airbus A340 quad jets versus the Boeing 767s used by Ethiopian, KLM and others. However, many commentators ascribed SAA's demise to poor management (Theobald, 2020), (Long Haul by Simple Flying, 2021).

SAA being a State-owned enterprise, was a creature of the South African Airways Act of 2007, reporting to Gordhan, and a "ghost being kept alive by ANC policy" (Bruce, 2020). As revealed in the Zondo commission into State-capture, malfeasance,

[1] The R/$ exchange rate in April 2021 was 14.3

politics and corruption had crippled and "brought to their knees" almost all State-owned enterprises, including SAA (Nyatsumba, 2021).

Business Rescue

The Companies Act of 2008 introduced Business Rescue as an option for South African companies in distress, who otherwise faced liquidation. In terms of the Act, a Business Rescue practitioner is appointed to replace the Board and must develop a plan which needs the support of at least 50% of creditors (Werksmans Attorneys, 2013). In December 2019, SAA made history as South Africa's biggest business rescue – this despite the more than R57bn in bailouts received from taxpayers since 1994 (BusinessTech, 2020). SAA's 2018/19 unpublished annual financial statements showed the group had accumulated R16bn in losses over the preceding three years and owed R26bn to creditors (including R9bn to the SA Government in guarantees, R4bn in "post-commencement" finance to the SA Government and SA banks, R600m to Comair to settle an "unfair competition" fine and various amounts owed to employees and SA Revenue Services) (Theobald, 2019).

Early in the process there were many questioning the rationale for resurrecting SAA. The government's National Development Plan listed 14 priority outcomes[2] including "infrastructure". Tourism had been a key argument for maintaining the State airline, but, prior to business rescue SAA had cut key routes and lost landing rights as it struggled to attract passengers (Theobald, 2020). Competition in logistics from companies such as global network operator DHL (who had invested billions in Johannesburg-based facilities) raised questions about SAA Cargo's viability. The more reasonable rationales for a further bail-out included SAA's role in supporting the training of black pilots, serving remote but necessary regional destinations, SAA's other subsidiaries (SAA Technical, Air Chefs) as well as SAA's symbiotic links with Navigation Services, Air Traffic, SA Weather Services and SA Civil Aviation. There was also the over-hanging issue of SAA's low-cost subsidiary Mango Airlines, already the substance of a R600m competition fine. How tolerable was it that shareholder-owned competitors SAFAIR and COMAIR should have to compete with Mango, a beneficiary of tax-payer support?

Finding the money

For the SAA rescue plan to be viable, about R26bn was required. In January 2021, the Development Bank (DBSA) had agreed an "equity bridge facility" of R3.5bn. Finance minister Tito Mboweni's February 2021 budget speech re-allocated billions of rands from other departments to fund COVID-19 related costs (Mboweni, 2021). With South Africa's debt-to-GDP ratio at 82%, the government was borrowing at a rate of more than R2bn per day and servicing costs and wages amounted to 79c in every rand of tax income (Quintal, 2020) (Leon, 2021). Other suggested sources of bail-out funds were a "possible" strategic equity partner, an amendment to Regulation 28 of the Pension Fund Act to further access private retirement funds or that the Reserve Bank (SARB) should simply "print money" (Bruce, 2020). There was universal agreement on two issues: the SA government could not continue to indefinitely bail-

[2] The focus areas identified in the NDP: education, health, safety and security, economic growth and employment, skills development, infrastructure, rural development, human settlements, local government, environment, international relations, public sector, social protection, nation-building and social cohesion.

out SAA and that SAA should not revert to a zombie company, merely able to service loans (Smith, 2021).

On 2nd May 2021 the business rescue practitioners (Matuson & Associates and Adamantem) handed SAA back to the interim board, extracting a fee of R36m for their efforts[3]. They noted that SAA was "solvent and liquid" and that "a significant portion of the debt that had hamstrung SAA" had been transferred to a "receivership vehicle" to be repaid to creditors over the next three years. They also observed that R3.5m of the required R10.3bn was still outstanding to complete the rescue plan but were "hopeful that this would be forthcoming from the Treasury" and that additional working capital was expected from an unnamed "strategic equity partner" (Paton, 2021).

On 20th May 2021, the SAA Pilots association headed to court claiming, "irreparable harm" to its members and accusing SAA of "scab-labour" in an attempt to "permanently neutralise" union members (Smith, 2021). This had followed union action over the failure to pay wages at SAA Technical, where management had commenced a retrenchment process to cut 1200 employees (Mkentane, 2021), (Phakathi, 2021). Mango too, faced several issues including "exploitative" lease contracts, technical and maintenance issues of a grounded fleet, an operating loss and no cash. Its survival dependant on an anticipated R819m Special Appropriation from the Treasury (Paton, 2021).

On 3rd June 2021, as a largely unvaccinated South Africa approached the start of its third COVID wave and re-entered "lock-down", Gordhan announced a 'born-again' SAA, "almost ready to take off" and promised "no more bailouts" (Smith, 2021).

But, given SAA's history, the lack of a detailed rescue plan, the uncertainties of a COVID future and all the other priorities of a developing country, was it even ethical to think about bailing-out an airline? And what were the chances of success?

References

Bruce, P. (2020, June 17). *No way can this SAA rescue plan work*. Retrieved from BusinessLive: https://www.businesslive.co.za/bd/opinion/columnists/2020-06-17-peter-bruce-no-way-can-this-saa-rescue-plan-work/

BusinessTech. (2020, May 15). *SAA counts R16 billion in losses over three years*. Retrieved from BusinessTech: https://businesstech.co.za/news/government/398403/saa-counts-r16-billion-in-losses-over-three-years/

Leon, T. (2021, May 27). *The president loves big numbers and big talk but it's all fantasy economics*. Retrieved from Business Live: https://www.businesslive.co.za/bd/opinion/columnists/2021-05-27-tony-leon-the-president-loves-big-numbers-and-big-talk-but-its-all-fantasy-economics/

Lex. (2011, November 29). *US airlines: crash and burn economics*. Retrieved from Financial Times: https://www.ft.com/content/6f2278bc-1aaa-11e1-bc34-00144feabdc0#axzz1fC6UupDx

[3] The total cost of Business Rescue was estimated in excess of R220m (Smith, 2021).

Long Haul by Simple Flying. (2021, April 15). The Battle For Africa: Ethiopian Airlines vs Kenya Airways vs SAA. Retrieved April 15, 2021, from Simple Flying: https://www.youtube.com/watch?v=14ByYjS6iE4

Mboweni, T. (2021, Feb 24). *Minister Tito Mboweni: 2021 Budget Speech.* Retrieved from www.gov.za: https://www.gov.za/speeches/minister-tito-mboweni-2021-budget-speech-24-feb-2021-0000

Mkentane, L. (2021, April 5). *Numsa to take legal action over failure to pay wages at SAA subsidiaries*. Retrieved from Business Live: https://www.businesslive.co.za/bd/national/2021-04-05-numsa-to-take-legal-action-over-failure-to-pay-wages-at-saa-subsidiaries/

Nyatsumba, K. (2021, February 28). *Why SAA won't fly: not just state capture, the government is also to blame*. Retrieved from TimesAlive: https://www.timeslive.co.za/sunday-times/opinion-and-analysis/2021-02-28-why-saa-wont-fly-not-just-state-capture-the-government-is-also-to-blame/

Paton, C. (2021, June 2). *Mango's financial difficulties multiply*. Retrieved from Business Live: https://www.businesslive.co.za/bd/companies/transport-and-tourism/2021-06-02-mangos-financial-difficulties-multiply/

Paton, C. (2021, May 2). *SAA business rescue finally over*. Retrieved from Businesslive: https://www.businesslive.co.za/bd/national/2021-05-02-saa-business-rescue-finally-over/

Phakathi, B. (2021, April 28). *SAA Technical starts retrenchment process to cut up to 60% of jobs*. Retrieved from Business Live: https://www.salabournews.co.za/56208-saa-technical-starts-retrenchment-process-to-cut-at-least-60-of-its-2-000-jobs

Quintal, G. (2020, October 28). *Political parties criticise SAA bailout and SA's rising debt*. Retrieved from Business Live: https://www.businesslive.co.za/bd/national/2020-10-28-political-parties-criticise-saa-bailout-and-sas-rising-debt/

SAA. (2021, April 2). *Brief History.* Retrieved from FlySAA: https://www.flysaa.com/about-us/leading-carrier/about-saa/brief-history

Smith, C. (2021, June 3). *No more bailouts' - Gordhan says 'born-again' SAA almost ready for take off*. Retrieved from Fin24: https://www.news24.com/fin24/companies/no-more-bailouts-gordhan-says-born-again-saa-almost-ready-to-take-off-20210602?utm_source=24.com&utm_medium=email&utm_campaign=3989+23804718+61605&utm_term=https%3A%2F%2Fwww.news24.com%2Ffin24%2Fcompanies%2Fno-more-b

Smith, C. (2021, May 20). *SAA pilots head back to court to stop 'irreparable harm'*. Retrieved from Fin24: https://www.news24.com/fin24/companies/industrial/saa-pilots-head-back-to-court-to-stop-irreparable-harm-20210520?utm_source=24.com&utm_medium=email&utm_campaign=3989+23804718+61181&utm_term=https%3A%2F%2Fwww.news24.com%2Ffin24%2Fcompanies%2Findustrial%2F

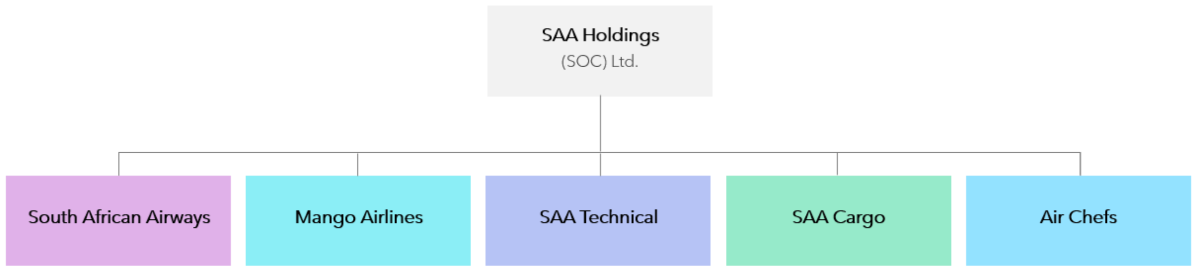
Theobald, S. (2019, December 8). *SAA business rescue takes SA into uncharted territory*. Retrieved from Intellidex: https://www.intellidex.co.za/insights/stuart-theobald-saa-business-rescue-takes-sa-into-uncharted-territory/

Theobald, S. (2020, August 11). *Why keep up the SAA charade*. Retrieved May 27, 2021, from Business Live Premium: https://www.businesslive.co.za/bd/opinion/columnists/2020-08-11-stuart-theobald-why-keep-up-the-saa-charade/

Werksmans Attorneys. (2013, April). *Basics of Business Rescue*. Retrieved from Werksmans.com: https://www.werksmans.com/wp-content/uploads/2013/04/Werksmans-Basics-of-Business-Rescue.pdf

Exhibit 1

SAA Group Structure



Source: Author's construction from SAA Integrated Report 2017 (latest published).

Exhibit 2

SAA Key Facts

Founded	1934
Main Hub	Johannesburg
Alliance	Star Alliance
Frequent Flyer Programme	Voyager
Fleet	64 aircraft (SAA 52, Mango 10, SAA Cargo 2)
Domestic destinations	8
Regional destinations	25
International destinations	8
Passengers	SAA 6.8m Mango 2.9m
Cargo	111000 tonnes
Revenue	R30.7bn
Operating profit	-R 2.7bn
Employees (Group)	10071
Employees (SAA)	5752

Source: Author's construction from SAA Integrated Report 2017 (latest published).