

Aviation: the death agonies of JAL

It's becoming boring for us, and agonising for JAL and its employees: the will it/ won't it fall into some form of administration or outright liquidation debate is not helping. The truth is simple: JAL is hopelessly insolvent and trading whilst insolvent is not generally allowed. So why are airlines seemingly protected against the corporate solvency laws that affect other businesses?

Ironically, when (daily, it come closer to when and further from if) the story of Asia's largest airline comes to a crash landing after almost 40 years (it was formed in 1951), it will not be the largest corporate failure in Japan. In fact, it won't even be close.

Japan Air Lines has been the recipient of vast amounts of government money in recent years: in fact, since the airline industry entered crisis after 11 September 2001, followed by SARS every one of the Japan's finance ministers has thrown money into the seemingly bottomless pit that is JAL. Every one, that is, except Yukio Hatoyama, the present incumbent of the post.

Hatoyama says that enough is enough: JAL may be the flag carrier but it is not a state owned business; and it is not the job of government support private enterprise without expectation or hope of reward.

And so he has ruthlessly overturned the policy of keeping JAL flying at the taxpayer's expense without regard to cost, saying that he is not convinced that whatever the government pumped in now would ensure the carrier's long term survival.

But Hatoyama is not pushing the airline towards liquidation: he wants to see a fundamental restructuring of the business and its capital base, its debt sorted out and rescheduled or waived and staff terms and conditions brought in line with regional norms. JAL is reported to provide pay and conditions far in excess of regional rivals such as Cathay Pacific and Singapore Airlines, resulting in rival carriers having to pay enhanced pay to native Japanese crew to attract equal quality with JAL.

Part of the problem is that no-one appears to know just how much debt JAL, with its complex business structure, is carrying. Estimates seem to centre around USD16,000 million. In the past week, its shares have fallen to their lowest ever in Tokyo in a decline that was not merely precipitous but seemingly more akin to the base-jumping antics of the succession of people throwing themselves off the top of the Burj Dubai / Khalifa - but without a landing softened by a parachute.

JAL has been in discussion with various airlines about various options, merging its cargo business with All Nippon, getting a cash-injection from Delta Airlines and American Airlines (themselves no strangers to, er, corporate restructuring). The US airlines may be playing a waiting game: with JAL's shares falling to just 67 yen last week - you'll need many shares to buy food at a Tokyo standing noodle bar - their money will buy a much greater proportion of the airline than it would have done when the discussions were started. In 2009, the shares fell almost 60%. Last week they fell almost 25% against the new year's opening. The catastrophic share plunge has led Japanese newspaper Asahi to speculate that the shares are now so close to valueless that one viable option is to form an entirely new company, transfer the assets to it and leave the debt behind with orphaned shareholders.

Watching closely will be Boeing: the collapse of JAL will make no difference to Boeing in the real world: there are orders galore. And JAL's 2005 order for 30 B787 "Dreamliners" and an option for 20 more will not be missed, at least not for several years. But it will be a major slap-in-the-face for the Japanese: the sale to All Nippon was part of a complex political / commercial deal that saw the production of the major components for the 787 being undertaken in Japan and a deal for both JAL and All Nippon to buy 787s was a part of the negotiation for Japanese companies to get access to the B787 development and production work.

Boeing have even decorated their second complete B787 in the livery of All Nippon - and that test-aircraft made its first test flight on 22 December last year, a week after the first.

JAL has resisted any form of restructuring, saying that it might affect passenger confidence. But history shows that troubled airlines often skimp on maintenance. Drawing out JAL's demise draws attention to that, and runs the risk that passengers will find an alternative anyway.

They have been doing so: within Japan, government figures show a swing from JAL's internal routes to high-speed trains, despite higher rail fares and even a recent "upgrade for 1000 yen" promotion, for economy to business on domestic flights. That's about a quarter of the price of a haircut at a men's barber.

Behind the scenes, though, the government is not leaving JAL entirely to fend for itself. There are reports that a rescue package, on the government's terms, is being prepared - with a government funded investment company set to take a major, perhaps controlling stake. Day to day running costs are being covered, in the short term, by Development Bank of Japan, a state owned bank. But that won't continue for long and JAL has to put up or shut up.

Whatever happens, it will need to further cut its routes: its domestic network, a legacy of being a state-owned carrier providing a public service, has many routes that don't come close to covering

costs. In Japan, air travel is vital because of the number of islands and mountainous terrain. Rail and road transport is not viable for much of the country.

But a final break with government money will put JAL in the position where it can argue for freedom from those obligations.

And, ultimately, that might be the only way that JAL can survive.