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THE PRIVATIZATION OF MEXICANA (CMA)

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PREFACE

The objective of the Regional Project on Policy Reforms to Increase the Effectiveness of the State in Latin America and the Caribbean (HOL/90/S45), which ECLAC is executing with cooperation from the Government of the Netherlands, is to identify reforms that allow the States of the region to implement effective policies for pursuing the interrelated goals of macroeconomic stability, changing production patterns for attaining sustained growth, and social equity.

With this objective, the project seeks to analyze actual processes of public policy reform, from the perspective of an explicit view of State reform and how it relates to interest groups and social actors, in the context of the challenges facing the countries of the region during the current phase of their development, and the new functioning of their economies.

To achieve that objective, reform processes in different areas of public policy are analyzed in a number of countries in the region that have undertaken such reforms. The areas selected are: tax reforms, privatization of public enterprises, reform of trade regimes, labour reforms and reforms in areas of social policy. The countries chosen are: Argentina, Bolivia, Brazil, Colombia, Costa Rica, Chile and Mexico.

In turn, comparative analyses -between countries- are made of reforms carried out in each of the instrumental areas selected, for the purpose of drawing lessons applicable to each policy area, on the basis of the different national contexts.

Finally, analyses of reform processes in each country are integrated into a multidimensional view of the reform of the State taking place in each of them, in order to draw conclusions about the determinants and possibilities of State-reform strategies in Latin America and the Caribbean.

1. Introduction

Mexicana de Aviación is the most important airline in Mexico, it is the oldest airline in Latin America and the fourth oldest in the world. Its privatization in August 1989, represented the second privatization of an airline within a year.[1] The previous public airline to pass into the private sector was Aeroméxico (AM) via a bankruptcy (in 1988). CMA was, in 1990, the sixth largest (in terms of sales) firm in Mexico, but only the 47th. largest amongst world airlines. It is an example where privatization of a public firm did not result - unlike the privatization of Aeroméxico- in a efficient dynamic and solvent private company nor in government sale income. Poor performance as a private firm meant that it was effectively taken over by Aeroméxico after only three years after it was privatized.

2. History

CMA was created in july 1921 by H.Lawson and L Winship. In 1929 Pan AM bought the totality of the CMA shares. In that year, Pan AM obtained a concession from the USA Post Office for transporting post from/to USA - Mexico. In 1968 Cresencio Ballesteros (a Mexican construction industry leader) bought it from Pan Am. The carrier was revitalized improving services and profitability. However, the airline debts expanded faster than its fleet. In the economic crisis of 1982, a large devaluation of the peso, a recession of the Mexican international tourist market, a high foreign debt (of US$350 million), and with first quarter losses of US$127 million, the owner sold his leveraged holdings to the government under undisclosed terms. In 1986 the government decided to reduce its participation in the company. It was eventually transferred to the private sector -with government participation- in 1989.

3. The regulatory framework

The domestic airline service is subject to the General Law on Transport and Communications. A revision of the by-laws relevant for air transport was published in 1988 (Esquema Rector del Sistema Nacional de Transporte Aéreo). Essentially: a) for each route a concession has to be obtained from SCT -the Transport and Communications Secretariat; b) the tariff structure was controlled by SCT and the particular tariff for a given trip length determined by a loosely drawn formula (a regression of peso/kilometer on distance); c) there were no price controls on cargo. The international routes were subject to bilateral agreements between countries regarding Y class fares, but with discounts subject to the market. Hence, within Mexico, competition was via product differentiation (quality of service) rather than tariff discounts. Adjustments to fares lagged both in timing and magnitude from inflation. In April 1991 -just before deregulation- the government reduced fares by 5% when inflation was running at a 16% annual rate.

In July 1991, routes, tariffs, and the discount structure were liberalized except for routes with only one airline service.[2] The reforms were similar to the ones that had been adopted by the USA in 1978. The by-laws were published on the September 1991. The new regulatory framework consists of:

i) for national trunk line flights, operated by two or more airlines, the firms can determine their Y tariff, with monthly notification but not previous permission of SCT;

ii) the airlines can offer any discount structure, and cannot just offer the Y tariff;

iii) where only one airline operates, the existing tariff is taken as the Y tariff, and any change has to obtain SCT permission;

iv) applications by national airlines to operate in new routes or existing ones are to be granted immediately for indefinite time, but the airline has to start operating within 90 days, and operate that route at least for 6 months;

v) SCT is responsible to oversee if airlines fix tariffs under non-market agreements that are detrimental to competition, and the airlines have to provide analytical data for the determination of the Y and discount fares as well as provide information regarding occupation factors. This information has to be sent to SCT on a monthly basis.

vi) regional "feeder" airlines or local flights are not subject to iii) above, as alternative transport is considered sufficient competition; and,

vii) SCT will, in principle, have periodic meetings of representatives of the industry to obtain a continuous feedback regarding possible changes in the regulatory framework.

Further, in the beginning of 1989 the regulations and by-laws regarding foreign investment were modified. The new regulation allowed foreign participation in the airline business, but with a maximum of 49% ownership limit. This change was, as we will see, crucial for the privatization of CMA.

The new regulatory framework, could be seen as a preliminary step towards improving the performance of Mexican airlines in preparation for NAFTA (North American Free Trade Area between Mexico, USA, and Canada). Although the latter does not contain provisions for the airline business, it is expected to increase substantially traffic between Mexico and the USA, and increase competition from USA airlines. Further, the previous regulation prevented airlines from sufficiently exploiting their potential yield curve.

4. Financial performance

a) Revenue

In table 1 we summarize CMA's main sources of sale income. As can be seen, most of sales come from its passenger service, with an increasing proportion derived from its international flights. This reflects that firstly, the economic crisis starting in 1982 reduced substantially domestic passengers traffic and second, tariff differences for similar stage length (see table 2). Although nominal sales revenue grew spectacularly during the period 1981 to 1989, in real terms it was more or less stagnant until 1985, whence it grew until 1988, whereupon it fell.

Domestic and transborder yields are low in comparison with those of the USA with similar stage length (see table 3).[3] Both passenger revenue per available seat kilometer (ASK), with and without adjusting for trip length, and passenger revenue per RPK (adjusted for stage length, hence taking into consideration load factors) are lower than AM and other comparable carriers.[4] With respect to non-Mexican carriers this reflects that tariff regulation allows USA carriers to price segment the market, thereby maximizing income without impairing traffic volume. Mexican regulation prohibited this until late 1991.

b) Costs

A global indicator of cost efficiency is operating costs per available seat kilometer. In graph 1 and table 4 we show that: i) over time CMA's real operating cost rose from 1984 until 1987 and since then has fallen below the levels recorded in the early eighties; ii) its ratio was amongst the lowest of North American carriers, including AM, in 1989.

There are five main cost areas: ticketing, sales and reservations, maintenance, station charges, fuel, crew (see table 5). The ticketing, sales and reservation costs per ASK for CMA are in the middle range while as a percentage of total operating costs are in the high end (see table 6). This area covers diverse items but is essentially labour-intensive hence its expensiveness is due to low labour productivity. Crew costs of CMA per ASK are at the lower end of comparative carriers. Furthermore, pilot productivity has improved in 1990: average monthly flight hours changed from 35 hrs. to over 45 hrs. in 1990; the addition of A320-200 planes will be flown with existing pilot staff, therefore further improvement is expected. Maintenance costs per ASK for CMA are significantly above North American carriers. With a lower wage in CMA compared to USA carriers the high ratio can be attributed to: a) restrictive productivity reducing work provisions in CMA's labour contracts; b) high outhouse maintenance -mainly USA firms- although with the acquisition of Turborrectores this should be reduced. The major area of increase for CMA has been station charges. Station charges, both per ASK and as a percentage of total operating costs, are higher than other LA carriers but lower than USA flag carriers (see table 6). This reflects, on the one hand, relatively low labour productivity but, on the other, high increases of charges by airport authorities in Mexico (see table 7). Fuel costs is the second major operating cost item. Although these are higher in comparison with North American carriers, they are lower than South American ones (see table 6). The sharp increase in 1990-91 was due to the Gulf War however, while in USA prices have fallen in 1991, in Mexico these government controlled prices have not done so.

c) Profits

In table 8 we summarize the profit and loss statement of CMA. During the 1981-89 period the company had negative operating profits in 1982 and 1986, two macroeconomic crisis years. However, after tax profits were consistently negative after 1985, although after reaching a peak in 1987 negative profits were reduced.

5. Economic performance

In this section we describe CMA's economic performance, both over time as well as in comparison with its main competitors, using key indicators normally used in the airline business. In table 9 we summarize the main economic data for CMA, over the 1980-1992 period.

i) Capital Productivity (see table 10): CMA's aircraft utilization (hours per day) is (depending upon the type of aircraft) within the range of USA carriers but lower than AM for comparable aircraft.

ii) The load factor of CMA has ranged from a low of 58% (in 1986) to a high of 62.7% (in 1989). However, there is a significant negative gap between CMA and AM, to CMA disadvantage (see table 11).

iii) Labour productivity ASKs per employee, (adjusted for stage length) is, with respect to other carriers, extremely low. This reinforces the conclusion derived in the comparison of costs per ASK (differentiated between station, maintenance, and ticketing/sales) discussed above (see table 10).

a) Market share

In an analysis of the market share we can distinguish between the domestic market and the international (USA to/from Mexico) market.

Domestic passenger traffic, with the exception of 1985, declined from 1983 to 1988. Since then, there has been a positive trend, although by 1990 total traffic was still below the 1983 figure. CMA share of the domestic passenger market exhibit a sustained yearly growth up to 1988. Much of the gain reflected the problems of Aeroméxico (bankruptcy in 1988). Since Aeroméxico reorganized it has moved quickly to recapture a large part of market share it had lost (see table 13). For most of the period both CMA and AM were increasing their market shares at the expense of regional operators. However, due to the growth of the latter (although CMA has in 1990 regional carriers as subsidiaries, see below) this trend has been reversed somewhat. The differential in market share gap and seat share gap (see table 14) shows that the differential has been to the advantage of CMAs main competitors and is reflected in AM's higher load factor.

Table 15 shows transborder traffic by USA and Mexican flag carriers. There are three central features:

i) The transborder market even grew significantly in the 1983-1990 period, a trend that is expected to continue, and accelerate due to the North American Free Trade Agreement, and tourist promotion by the Mexican government;

ii) the growth rate for USA flag carriers was much higher than for Mexican ones, despite that Mexican domestic resident traveler traffic grew at a higher rate.

iii) CMA is historically the dominant Mexican carrier (see table 16), but is gradually losing out to Aeroméxico. Furthermore, the interruption of operations of the latter company left a void in the transborder market that was filled by USA flag carriers, although it must be noted that CMA was in the midst of privatization and reorganization.

This trend will be difficult to reverse, given that USA carriers have inherent advantages; first, they have larger route structures allowing them to feed traffic to their gateways, thus facilitating on line transfers to and from interior cities (on average, 50% of traffic through hubs are connecting or through traffic). Second, between 80% of USA flag carriers is through travel agency network. The latter work mainly on the basis of commissions that are pegged to their sales to a specific carrier. With USA flag carriers more extensive domestic and to some extent international networks agencies can build up higher sales with USA carriers rather than with foreign ones.

6. CMA just before privatization

Just before privatization, CMA flew to about 44 cities (28 in Mexico and 16 abroad) with a total of 114 routes, and a daily average of 218 flights. Its fleet (see table 17) was composed of 37 Boeing 727 - 200 A planes with an average age of 10.3 years, 7 of which were rented, and 5 Douglas DC-10/15 (four rented) with an average age of 7.5 years.[5]

The company had two maintenance bases, one in Mexico City and the other in Guadalajara. Further, the company provided reservation services with other airlines through the SERTEL system. CMA had holdings in a number of companies: i) 5% of Turborrectores -a turbine engine reparation company; ii) 100 of ATS, a real state firm; iii) 50% of DATATRONIC (jointly owned with Aeroméxico) which provides computers and computing services.

CMA share ownership just before privatization -detailed in table 18- was: i) 50.1% government owned; and ii) a significant proportion of the shares were held by stockbrokers and commercial banks, including Banamex.

The company's workers were organized in 4 unions: i) the pilots union, Asociación Sindical de Pilotos y Aviadores (ASPA); ii) the air staff union, Asociación Sindical de Sobrecargos de Aviación (ASSA); iii) the ground staff union, Sindicato Nacional de Trabajadores de Aviación y Similares (SNTAS); and iv) workers in the United States, in the International Association of Machinists and Aerospace Workers, (IAMA). In 1988 the company employed 13,027 persons. In October of that year, major changes were obtained in the negotiations with the unions. The new contract reflected: i) a reduction in a number of privileges of the workers; ii) a change in working practices to increase efficiency; iii) an agreement that, if necessary, the number of employees could be reduced by 20%.

The new agreement with ASPA included an increase of 5.8 hours of flight time for the pilots. The new contract with SNTAS, included: i) a reduction of non-penalized lateness from 30 to 15 minutes; ii) a reduction in the number of holidays for the first five years of work; iii) a reduction of the length of permissions for ill health of family members and also of the right for paid days due to illness from 300 to 180. The agreement with ASSA allowed CMA to: i) increase the working day in a way that the company avoided that cancelling flights due to flight delays resulted in the working day being used up; ii) a reduction in rest periods, thereby increasing effective service; iii) use less than the total number of flight crew when it was not necessary.

7. Privatization: Why, How, and to Whom

a) Why to privatize

In May 1988, a government policy document on airline business pointed out that: i) there was a generalized worldwide movement of a reduction of state participation in the airline business; ii) the existing two national airlines and concession titles had prevented the growth of regional airlines; iii) since the beginning of the eighties the service provided by both national airlines had deteriorated due to bad management, operating procedures, as well as labour relations; iv) it would be convenient to have (at least two) private firms that operated in the major trunk routes.

The Information Prospectus of the International Bank -the government's financial agent in the privatization of CMA- stated that, given the demand for air transport, for the rest of this century domestic routes would require about 120 planes by the year 2000. Of the existing fleet of the two national airlines, by that year there would only be between 20 and 30 still operating. Therefore, a massive investment in this industry was required. The implied increase in government expenditure/indebtedness was contrary to the established budgetary policy of the government. Thus, it was argued, that it was imperative to have the private sector operating the airlines.

b) <u>How privatization was carried out</u>

The first attempt to privatize CMA, in 1986, with Banamex as the financial agent, backfired. There were very few sufficiently capitalized offers. Most investors complained that CMA: i) had an excessive debt; ii) was bound by overgenerous pilot contracts; iii) was forced to cover unprofitable routes. The government, therefore, had to revamp the company by means of debt restructuring, elimination of marginal routes, tourist promotion, and other measures.

The second, and this time successful attempt, was in 1989. The privatization calendar was:

23-25 May 1989

The public announcement of the privatization of CMA under a new scheme. Essentially, the government would not sell its participation, but it would manage it in a joint venture with the private sector. The latter would be the majority owner of a new company which would hold the shares of CMA and new effective resources of the buying group. Thus, the process was essentially oriented towards increasing the capital of the firm, incorporating management experience in order to achieve growth and a greater efficiency.

The main conditions set by the government were:

- the buying Group had to buy at least 25% of the social capital;
- foreign participation would be limited to 49% of the group;
- the group could not sell controlling shares for a minimum of five years;
- the federal government would maintain its participation in the new company for at least three years. To this end the government set up a controlling firm, "Corporación Mexicana de Aviación" (COMA), in which the government deposited 49.9% of its shares in a proportion of one to one (see table 19).

9-22 June

The receipt of deposits (10 thousand million pesos) with which potential buyers were given the details and the official prospects produced by BI, the government's financial agent in the sale.

June to 6 August

This period was given to potential investors to have the opportunity to evaluate the company, make on site visits, have interviews with management and workers.

7 August

The acceptance of formal offers. Seven offers were received.

22 August

The public announcement of the winning offer -by Grupo Falcon. The group offered:

- US$140 million in new capital;
- Grupo Falcon would have 25%, Federal government 40.1% and minority shareholders 34.9% of the shares;
- the new capital book value of the new firm was set at US$550 million, equivalent to 1.07 of the accounting value of its shares, a price above the stock market valuation which was about 50% below the accounting value;
- an investment program (not legally binding) of US$3,000 million in the next 10 years, about 1,100 of which would be invested in Mexico, and the creation of about 21,500 new jobs. The investment program included the intention of increasing the fleet with 47 airplanes and substituting the 6 oldest units in the company's fleet.

The share structure of COMA, in the first step, was 49.9% government-owned and 50.1% owned by the new investors -The Falcon Group (see table 19). COMA owned 40% of CMA shares. Given that the government still owned the majority of CMA's shares, it created a trust in which it put its remaining shares (20.1) with voting rights given to the Grupo Falcon, the latter thus having a majority voting right. The sale contract, however, specifies that under certain conditions the government has veto right. Furthermore, the existing CMA shareholders were given the option (completely taken up) of swapping their CMA shares for COMA shares one for one. In addition, in order to meet the 25% share condition, Grupo Falcon had to buy additional shares from the stock market such that it owned 34.9%.

8. The changing value of CMA/COMA

The issue of whether the government sold the company at a "fair price" does not, of course, strictly arise in this case.

However, with the Falcon Group's offer, the governments capital became US$220.3 million, with an implicit price accounting value relation of 1.07, resulting from dividing the government's equity in COMA (220.3) by the government's equity in CMA (205.85), which in turn was above the stock market valuation, which in the months just before privatization was about 50% below book value.

One method for determining the accuracy of the implied sale price is by comparing it to other recent privatizations. In tables 20 and 21 we summarize the central features and market price/value of other recent privatizations.

9. Fiscal impact

Since the government did not sell any of its shares of the company, there was no direct effect on fiscal balances during the first step of privatization of Mexicana. This was reinforced by the fact that the company did not receive recent transfers nor did the government lose any dividend income stream, given the company policy of increasing its capital instead of distributing dividends.

However, the government increased prices and tariffs and prices of goods and services provided to CMA by other public enterprises, including ASA's tariffs and turbine gasoline price (which had been about 4 times less than the price in the USA in 1988). Although CMA had been subject to the existing tax laws, union members of the company did not pay income tax. After privatization, they were obliged to pay it.

10. CMA - A private firm

CMA is controlled by the holding company COMA, a joint venture of the government (49.9%) and a newly created Corporación Falcon (50.1%). The government, in principle, will retain equity interest in Mexicana for at least three years, but later on, it may be cashed out in full.[6]

The Corporación Falcon is made up by 54% of Mexican partners and 46% of a foreign investor group (see table 22). The dominant figure amongst the Mexican partners is P. Brennner, leader of the Xabre Group. The latter is a well capitalized Mexican conglomerate that has expanded aggressively during the eighties. Amongst the public enterprises the Group bought there were those in textile mills, sugar refineries, resort hotels and a 40% share in Nacobre -a copper company. A number were restructured and resold for a profit, however, Xabre's Real Turismo division retained the Camino Real and Calinda chains of luxury hotels plus other tourism properties. The next largest Mexican investor is the Saba family with 6.9%, followed by C. Abendrop with 4.9%. The latter, former owner of Banco del Atlántico that was nationalized in 1982, became CMA's chairman on privatization until 1990. The leading foreign investor, with an equal equity participation, is Chase Manhattan, followed by D. Burnham Lamberts's DBL Americas Fund, a vehicle for 40 USA corporate investors, with 7% (US$10 million), and Sir James Goldsmith, an Anglo-French corporate raider and a friend of Brenner, with a 6% participation (US$8.6 million).

11. Performance

The new management has undertaken a number of steps to capture market growth and improve efficiency. Amongst the measures taken are:

First, an increase in vertical integration. CMA has formed or acquired a number of subsidiaries since it was privatized in 1989. One of these subsidiaries is Turborrectores, a jet engine overhaul facility based in Querétaro, owned by CMA on a 98.4%. SERTAL, a computerized reservations system, is owned 50% by CMA and the rest by Aeroméxico. CMA also owns DATATRONICS, a subsidiary on data processing; Aeropuertos y Terrenos, that leases commercial property, and a number of regional airlines (see table 23).

Second, the acquisition of regional carriers (Aerocaribe, AeroMonterrey, AeroCozumal, Aeropacífico). The company also plans to establish hubbing operations in Guadalajara, Monterrey, Cancún, Tijuana, thus capturing a fast growing east-west market as well as the traditional north-south one.

Third, the establishment of a number of own tour operators' subsidiaries in the US and Mexico, including a wholesale one in the USA, the introduction of business-class cabins, and plans for the Air-bus.

Fourth, plans for the refurbishment of its B727-200 fleet with 22 A320 -200, at an anticipated cost of one million ASTUTE per plane. The original delivery dates and expenditure implied are shown in table 24. The new fleet will not only increase its current capacity, but it will also update it for the January 2000 USA "phase III" legislation regarding aircrafts (existing planes are of stage II type).

Fifth, a number of marketing and operational improvements, in line with the purchase of the program PROS yield management system. CMA is still in the process of implementing software and reforming the processes of management structure, control, and interdepartmental cooperation. The regulatory framework will allow full utilization of this program that permits price segmentation of the market, thus increasing revenue without impairing traffic.

Sixth, an increase in cargo capacity, which implies an investment in handselling facilities in Mexico City (with an expenditure of 1.5 mp and estimated capacity increase of 6 to 10%, and planned expenditure of Mex$30 billion in other Mexican airports). In 1990 CMA signed an agreement with KLM regarding technical, commercial and operational cooperation.

Seventh, invoking the new labor contract signed in 1988, the company decided to reduce its labour force. The latter has been reduced from a peak of 14,052 in 1987 to 11,681 by 1991, and will radically decrease to 8,433 by the end of 1992.[7]

In 1990 there were some indications of improvement: for example, passenger revenue per RDK improved 4.9% (to $0.043) compared to 1989, and there was a smaller profit loss. However, maintenance costs per ASK increase 3.4% (to $.0086); crew cost per ASK rose 3.8% (to $0.0027); fuel costs and stationary charges per ASK rose in 1990 with respect to 1989 (46.5% and 9.4%, respectively); and load factors fell 4.5 percentage points from 62.7% in 1989. The 13.8% increase in capacity (ASK) was not matched by an increase in traffic. Furthermore, there is substandard time performance in contrast with AM (66% against 98%), combined with high lost\damaged luggage. Punctuality declined from 75.4% in 1990 to 82.5% in 1991. This has lead to a negative image of CMA vis à vis AM, particularly, in the domestic market. Thus, in 1990, although both nominal and real revenue increased, tax profits net fell.

Performance worsened in 1991 and 1992. Real operating income fell, while operating expenditure rose in 1992 (after falling the year before), allowing the company to generate greater operating profits but producing losses after tax profits. Economic indicators also declined; real revenue per kilometer declined dramatically together with the number of passengers per ASK, reflecting the falling market share combined with increasing capacity. The company was moving fast towards insolvency.

At the beginning of 1993, control effectively passed onto Aeroméxico. The latter had been buying CMA shares in the stock market and by March held 11% of CMA's shares. During that month, an agreement for transferring 43.7% of CMA shares to Aeroméxico, in principle, was signed by the two companies.[8] In exchange, CMA shareholders obtained 50 warrants of five years term. However, presumably to avoid regulatory problems, the two companies will continue to operate under their respective commercial names.

CMA downfall contrasts sharply with the performance of Aeroméxico, even though the latter had a poorer performance than Mexicana when both were public enterprises. The different performance can be partly explained by the difference in the mode of privatization as well as the dissimilar strategies adopted. First, Aeroméxico was privatized through bankruptcy. This allowed Aeroméxico to dramatically reduce its labour force without incurring up front costs of severance payments, and to obtain more flexible labor contracts. Aeroméxico reduced its labour force from 12,584 in 1987 to 3,752 in 1988, and only reached 6,169 by 1992. CMA, on the other hand, reduced the number of employees from 13,003 in 1989 to 11,681 by 1991, and the dramatic reduction to 8,433 by the end of 1992 was too late and also implied higher financial costs. Second, while Aeroméxico's fleet expansion was based on leasing -under favorable renegotiation of existing leases, given its bankruptcy, and new leasing in the context of an international oversupply of planes- CMA embarked on a costly acquisition of aircraft. Third, Aeroméxico had no government participation while CMA continued to have government participation in the company.[9]

12. Conclusion

The privatization of CMA was via capital dilution, a mechanism that ensured transferring control to the Mexican private sector for relatively small investment (relative to the value of the firm). Thus, it became an example where fiscal income was not an important factor in the privatization. In the process of privatization priority was given to capital infusion and managerial experience, so that the company could expand to meet expected growth in air travel. Since privatization was by capital dilution, the government did not obtain any sale income and with the fall of CMA's share prices, the expected capital gains of shares were diluted.

Although the company took a series of measures that could have borne fruit in a few years, its ambitious expansion program -without the necessary adjustment to improve performance- meant that losses increased dramatically. CMA was taken over by its Mexican competitor company in 1993, only three years after it was privatized.

This case also illustrates what may happen when deregulation and privatization do not go hand in hand. On the one hand, its costs were raised by tariff and price increases (to international levels) of government companies that provided inputs to CMA; but at the same time, airline tariffs remained controlled, thus generating financial problems to the company. However, much could be made of this, since airline tariffs were liberalized and discounts allowed in order that the company could exploit the potential yield curve within two years of privatization. Furthermore, Aeroméxico -whose performance did improve- was subject to the same regulatory framework and changes. The fact that the two companies are effectively one since 1993 does, however, reopen the question of the design and effectiveness of the regulatory framework.

Notes

[1] For the privatization of Aeroméxico see I. Ruprah (1993b), for an overview of the Mexican divestiture program see also I. Ruprah (1993a), and for an evaluation of divestiture in Latin America see R. Devlin (1993).

[2] During the first three months after deregulation, both Mexicana and Aeroméxico increased three times their fares in matching amounts, with an accumulative increase of 30%. By late 1991 fares caught up with inflation.

[3] Unless otherwise indicated, international comparisons include for Latin American airlines: Avianca, AeroPerú, Lan Chile, Viasa, Mexicana, and Aeroméxico; while for USA airlines: USAIR, Southwest, Alaska, Delta, American, Continental, Northwest, United, Trans World, and Pan American.

[4] In this document we define comparable carriers as AM and other North American airlines.

[5] This contrasts with Aeroméxico which had less owned aircraft and a significantly lower average age of its fleet (self owned and leased).

[6] Like the TELMEX case, the government was expecting large capital gains. However, the continuing poor performance and the fall of stock market shares indicate that the government has not sold the shares it still holds.

[7] We note that the reduction in the number of employees is small in comparison to Aeroméxico. However, the reduction in the latter company occurred when it was on strike, so there was no disbursement of severance payments. In the case of CMA, the reduction of employees was costly due to generous severance payments' legislation in Mexico.

[8] Conditioned by authorization from SCT and financial restructuring of CMA.

[9] Government involvement in the privatized CMA is demonstrated by the election of García Sáinz as replacement of the Director General in June 1991. The latter had a high public sector profile: Director of IMSS (Social Security Institute); Secretary of SPP (Programming and Expenditure Ministry).

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STATISTICAL TABLES

Table 1
CMA Sales of goods and services produced
(millions of new pesos)

	1981	1982	1983	1984	1985	1986	1987	1988	1989	1990
1. Domestic	5.79	8.79	24.43	38.90	63.97	116.56	287.01	632.27	741.05	1.126.6
2. International	7.68	11.65	32.39	50.30	85.60	190.18	505.83	929.20	965.00	1.467.1
3. Freight	0.91	1.31	3.04	5.99	10.44	21.85	53.62	102.36	102.67	146.66
4. Others	0.32	0.60	1.32	0.92	1.59	5.62	20.49	38.84	72.39	104.98

Source: Company Profits, SCT.

Table 2
Fare distance comparison
(1989)

City	Carrier	Fare (US$)	Distance (miles)	Fare/mile (US$)
Boston/Newark	CO	178.00	206	.864
Mexico City/Acapulco	MX	52.20	191	.273
New York/Cleveland	CO	296.00	417	.710
Chicago/Nashville	AA	364.00	441	.825
Guadalajara/Monterrey	MX	74.60	410	.182
New York/Miami	DL	432.00	1,098	.393
Seattle/Los Angeles	AS	472.00	1,133	.417
Chicago/Dallas	AA	459.00	918	.500
Mexicali/Guadalajara	MX	142.00	1,113	.128
Atlanta/Los Angeles	DK	620.00	2,153	.288
New York/Mexico City	MX	307.00	2,090	.147

Source: Directly from the airlines.

Note: Non-discount Y class fares.

Table 3
Revenue: an international comparison
(1990)

	C. M. A.		AM	LATIN AMERICA			U. S. A.		
	1989	1990		MIN.	AVG.	MAX.	MIN.	AVG.	MAX.
Passenger revenue per ASK ratio	0.041	0.0432	0.0488	0.0205	0.052	0.0715	0.0403	0.04843	0.0601
Passenger load factor (%)	62.9	59.9	64.4	53.4	62.45	67.6	55.2	62.05	67.0

Source: ICAO Financial Data and Mexicana.

Table 4
Operating cost per ASK, a comparison
(1989)

Carrier	Operating cost per ASK (US$)	Ratio to MX
Mexicana (MX)	0.044	---
Aeroméxico	0.050	114
Alaska	0.062	141
American	0.050	114
Continental	0.047	107
Delta	0.053	120
Northwest	0.055	125
Pan American	0.052	118
Trans World	0.049	111
United	0.055	125
USAir	0.067	152

Source: ICAO - 1989 Financial Statistics.

Table 5
Major CMA's expenditure areas
(000 US$)

	1 9 8 9		1 9 9 0		
Expense	Amount	% of total	Amount	% of total	% change in amounts
Ticket/sales reservations	150,068	20.3	163,758	18,3	90.1
Fuel	119,434	16.1	199,411	22.3	67.0
Maintenance	117,454	15.9	132,883	14.9	13.1
Station charges	107,111	14.5	158,214	17.7	42.7
Crew	43,408	5.9	50,911	5.7	17.3
Total:	$537,475	72.7	705,147	78.9	31.2

Source: Company Reports.

Table 6
Differentiated costs: a comparison
(1989)

	C. M. A.		AM	LATIN AMERICA			U. S. A.		
	1989	1990		MIN	AVG	MAX	MIN	AVG	MAX
Crew cost (ASK)	0.00255	0.00268	0.00473	0.00128	0.002412	0.00288	0.00262	0.004693	0.00793
Crew cost (% OC)	5.76	5.95	9.41	3.07	4.03	4.8	6.05	8.641	11.19
Maintenance expense (ASK)	0.00692	0.00685	0.00564	0.00321	0.006137	0.00828	0.00828	0.00573	0.00857
Maint. expense (% OC)	15.76	15.51	11.41	8.07	10.41	12.56	12.56	11.019	13.84
Ticket/sales (ASK)	0.009	0.0085	0.00625	0.0046	0.011325	0.0219	0.0219	0.00981	0.0133
Ticket sales (%PR)	21.7	20	13	6.7	24.825	38.3	38.3	20.07	27
Station charges (ASK)	0.0065	0.007	0.0048	0.0011	0.002975	0.0049	0.0049	0.00812	0.0112
Station charges (% OC)	13.7	15.3	9.4	3.4	4.5	5.6	5.6	14.63	16.8
Fuel cost (ASK)	0.0072	0.0105	0.007	0.013	0.021875	0.04	0.04	0.01497	0.084
Fuel cost as a (% OC)	16.1	23.2	13.2	13.2	18.875	23.8	23.8	14.152	15.8

Source: Mexicana: Situation Audit, SH&E, 1991.

Note: ASK per available seat kilometre; % OC percent of operating costs; % PR percent of passenger revenue.

Table 7
Mexican airport charges

a) Charges for equipment	1/89	5/90	% increase	11/90	% increase [a]
Aircraft push-out tractor	395 000	630 890	59.7	757 070	91.7
Ground equipment tractor	73 000	106 340	45.2	140 360	91.7
Motorized passenger loader	93 050	148 620	59.7	178 340	91.7
Auxiliary power unit	142 210	227 140	59.7	272 570	91.7
b) Charges for personnel	**1/89**	**5/90**	**% increase**	**11/90**	**% increase [b]**
Ramp supervisor	28 230	45 100	59.7	54 120	91.7
Operator/driver	14 750	23 560	59.7	28 270	91.7
Police/security	12 890	20 590	59.7	24 710	91.7

Source: Mexicana documents.

a Increase over 1/89.
b Increase over 1/89; hourly peso charges.

Table 8
CMA financial performance
(thousands of new pesos)

	Thousands of new pesos						Percentage growth (Real 1980 new pesos)	
Year	Sales	Operating costs	Operating profit	Other net income	Profit before tax [a]	Profits after tax	Operating expenditure	Operating income
1981	15	13	2	0.5	1.5	1.5	6.7	3.9
1982	22	24	-1	-1.6	-2.6	-2.7	10.5	-4.2
1983	61	53	8	-7.2	0.8	0.8	16.6	3.5
1984	96	83	13	9.0	4.0	4.0	-7.9	-5.1
1985	162	157	5	-11.9	-6.9	-6.9	19.7	6.6
1986	334	349	-15	-55.1	-40.1	-40.1	19.4	11.0
1987	867	855	12	-93.6	-81.6	-83.8	5.7	11.9
1988	1 703	1 538	165	-116.6	48.4	-42.6	-16.9	-9.4
1989	1 881	1 856	26	-5.4	20.12	-8.9	1.6	-6.8
1990	2 845	3 079	-234	98.4	-135.6	-164.8	2.8	18.3
1991	3 384	3 504	-116	10.8	-105.2	-130.4	-16.7	-22.3
1992	3 307	3 852	-545	80.9	-464.1	-497.7	4.3	-2.0

Source: Company Annual Reports.

a Before corporate tax, asset tax, provisions, and labour profit sharing.

Table 9
CMA economic indicators

Year	Passengers (thousands)	Kilometers flown (millions)	ASKs (millions)	Employees	Fleet	Cities served
1980	7 571	78	11 078	10 560	44	41
1981	8 152	80	12 110	12 105	45	39
1982	7 623	75	12 035	12 391	41	39
1983	8 095	83	13 932	12 475	43	40
1984	8 414	91	15 679	12 973	44	40
1985	8 954	94	16 219	12 896	46	41
1986	8 072	95	16 205	13 759	45	44
1987	7 857	95	16 146	14 052	45	46
1988	8 439	93	15 927	13 027	42	43
1989	8 502	96	16 793	13 003	44	44
1990	9 062	108	19 117	11 409	50	48
1991	8 549	104	17 977	11 681	58	42
1992	7 991	109	18 596	8 433	64	45

Source: Company Reports.

Table 10
Capital productivity: a comparison
(hours per day 1989)

Fleet	CMA	Aeroméxico	Alaska	American	Continental	Delta
B727-200	9.39	---	9.93	9.30	8.55	10.96
DCP	---	7.62	---	---	6.52	7.03
DC10	8.54	10.11	---	10.83	9.43	---
LOAD FACTOR						
%	---	---	54.3	61.8	60.0	59.1
RATIO TO CMA	59.9	NA	91	103	100	99

Table 11
Domestic passenger load factor
(CMA and AM)

	CMA	Aeroméxico	Load Factor Gap
1983	59.5%	63.3%	(3.8)
1984	59.4	61.0	(1.6)
1985	60.2	62.0	(1.8)
1986	58.3	61.9	(3.6)
1987	62.0	62.6	(0.6)
1988	70.7	65.1	5.6
1989	62.7	69.2	(6.5)

Source: Report of the Secretary of Communications and Transport.

Table 12
ASK per employee and load factor: comparison
(1989)

Carrier	Load factor	Ratio to CMA	Ratio ASK: per employee
CMA [a]	59.9	---	0.0012
Alaska [b]	54.3	91	0.0023
American [b]	61.8	103	0.0019
Continental [b]	60.0	100	0.0025
Delta [b]	59.1	99	0.0024
Northwest [b]	61.5	103	0.0023
United [b]	64.5	108	0.0016

[a] Year ending December 31, 1990.
[b] Year ending September 30, 1990.

Table 13
CMA and AM domestic passengers boarded

	Mexicana	%	Aeroméxico	%	Others	%	Total	%	Growth
1983	6 003	43.3	4 915	35.5	2 936	21.2	13 854	100	4.1
1984	5 961	44.0	4 915	36.3	2 664	19.7	13 540	100	-2.3
1985	6 448	44.5	5 527	38.2	2 509	17.3	14 484	100	7.0
1986	5 459	47.2	5 004	43.3	1 100	9,5	11 563	100	-20.2
1987	4 761	47.3	4 407	43.8	900	8.9	10 068	100	-12.9
1988	5 072	57.4	2 715	30.7	1 053	11.9	8 840	100	-12.2
1989	5 436	50.8	3 790	35.4	1 455	13.6	10 681	100	20.8
1990	---	50.8	---	41.0	---	---	---	100	---

Source: Report of the Secretary of Communications and Transport.

Table 14
Market share - Seat shares gaps[a]

	Market share			Seat share [b]			
	CMA	AM	Gap	CMA	AM	Gap	Gap Differential
1987	51.9%	48.1%	3.8	55.8%	44.2%	11.6	7.8
1988[c]	65.1	34.9	30.2	74.9	25.1	49.8	19.6
1989	58.9	41.1	17.8	59.8	40.2	19.6	1.8
1990	55.4	44.6	10.8	57.2	42.8	14.4	3.6

Source: Report of the Secretary of Communications and Transport (1987-89); Mexicana documents (1990) and Official Airline Guide on I.P. Sharp.

a Shares are based on MX and AM only; other carriers are excluded.

b Based on summer schedules for each year.

c Distorted by AM bankruptcy.

Table 15
U.S.-Mexico capacity and transborder traffic scheduled seats

Carrier	1984	1985	1986	1987	1988	1989	1990	1990 Capacity (%)
CMA	1 921	2 051	2 116	2 267	2 357	2 429	2 592	
Continental	426	478	526	779	1 205	1 194	988	14.2
American	433	425	475	494	630	875	898	12.9
Aeroméxico	1 120	1 059	1 003	1 151	520	591	859	12.4
Delta	421	377	353	395	429	713	727	10.5
Pan American	368	341	308	321	246	357	358	5.2
Alaska	0	0	0	0	5	132	283	4.1
United	56	50	56	73	69	101	194	2.7
Northwest	0	0	2	42	42	35	48	0.7
Passengers (000)	5 707	5 384	5 681	6 912	7 050	7 467	8 434	---
% of U.S. citizens	74.4	73.0	75.9	77.1	74.7	72.0	71.1	

Source: Official Airline Guide from I.P. Sharp.

Table 16
U.S. - Mexico capacity: CMA and AM schedules seats
(000)

	Mexicana	Aeroméxico	% of MX
1984	1 921	1 120	63.2
1985	2 051	1 059	65.9
1986	2 116	1 003	67.8
1987	2 267	1 151	66.3
1988	2 357	520	81.9
1989	2 429	591	80.4
1990	2 592	859	75.1

Source: Official Airline Guide on I.P. Sharp.

Table 17
CMA's fleet

	1984	1985	1986	1987	1888
Boeing 727-200 (TAA-TAB-TAC)	3	3	3	3	...
Boeing 727-200 A	31	31	30	30	30
Boeing 727-200 A (rented)	5	7	7	7	7
Douglas DC-10/15	2	1	1	1	1
Douglas DC-10/15 (rented)	3	4	4	4	4
Total					
	12,973	12,986	13,759	14,052	13,027
Employees					

Table 18
Share structure
(as of 28 April 1989)

	Shares	%
Gobierno Federal	57,364,748	50.83
Probursa	4,519,511	4.01
Operadora de Bolsa	3,860,794	3.42
Grupo Mexicano de Desarrollo	3,829,799	3.39
Familia Sáenz	3,749,751	3.32
C.B.I.	3,439,055	3.05
Vector Casa de Bolsa	2,298,095	2.04
Valores Bursátiles	1,968,279	1.74
Inverlat	1,846,967	1.64
Arka	1,729,356	1.53
Abaco	1,491,543	1.32
Estrategia Bursátil	1,348,439	1.20
Prime	1,131,439	1.00
Banamex	1,028,138	0.91
Afin	963,147	0.85
Invermexico	962,396	0.85
Familia Bailleres	958,764	0.85
Acciones Bursátiles	781,345	0.69
Maxival	574,588	0.59
Comercial Casa de Bolsa	562,625	0.50
Casa de Bolsa Cremi	469,185	0.42
Casa de Bolsa México	355,919	0.32
Other	17,621,407	15.61
TOTAL:	112,855,290	100.00

Table 19
Changing share structure

	Compañía Mexicana de Aviación (thousands of shares)	(%)	Corporación Mexicana de Aviación (thousands of shares)	(%)
Before Privt.				
Government	113,119.2	50.1	---	---
Pvt. shareholders	112,591.4	49.9	---	---
Total:	225,710.6	100.0		
First step				
Government	56,691.5	20.1	56,427.6	49.9
Pvt. shareholders	112,591.4	39.9	---	---
New investors	---	---	56,653.3	50.1
Corp. M.A.	113,081.0	40.0	---	---
Total:	282,363.9	100.0	282,359.9	100.0
Second step				
Government	---	---	113,119.1	40.1
Shareholders	---	---	98,653.8	34.9
New investors	---	---	70,590.9	25.0
Corp. M.A.	282,363.9	100.0	---	---
Total:	282,363.9	100.0	282,363.9	100.0

Table 20
Recent Airline Privatization Transactions

Privatized entity	Acquiring entity	Year of transaction	General terms of transaction	Shares issued	Price per share (US$)	Mkt. price of equity (US$)	Mkt. price of equity (US$)
Aeroméxico	Dictum Corp.	1988 (Nov)	Sale of 75% of Aerovías stock to Dictum	NA	NA	350,000	466,700
Air Canada	Publicly issued stock	1988	43% of govt. stock sold	30.8 Mil.	$6.59	202,000	469,767
		1989	Remaining 57% sold	41.1 Mil.	9.70	398,500	699,123
British Airways	Publicly issued stock	1987 (2/11/87)	Sales of 720.2 Mil. common shares (equal to 72.02 Mil. American Depositary Receipts) in the U.K., U.S., Japan and Canada	720.2 Mil.	125 p/shares or $19.69 per ADR	1,428,070	1,418,070
Mexicana	Xabre Group & foreign investors	1989 (Aug)	Sale of 25% of airline by the Mexican government	NA	NA	140,000	560,000
VASP	Canhedo and VASP employees (VOE)	1990 (9/4/90)	Sale of 48% of VASP stock to Canhedo (local transport company) and 12% to VOE	15.9 Mil.	0.003	43,700	91,000

NA = not available.

Table 21
Market value and price of company indexes of comparable transactions
(based on fiscal year prior to the transaction)

Privatized entity	Value of company (thousands of US$)	Price of equity (thousands of US$)	Market Value/price Ratios: Value/price of total revenues		Value/price of operating income		Value/price of net income		Value/price of cash flow		Value/price of book value	
Aeroméxico	$627,000	$466,700	1.40	1.04	NM	NM	NM	NM	NM	NM	4.97	3.70
Air Canada '88	1,313,964	469,767	0.55	0.20	16.47	5.89	37.38	13.36	7.18	2.57	2.85	1.02
Air Canada '89	1,567,993	699,123	0.54	0.24	14.93	6.66	19.44	8.67	8.21	3.66	2.01	0.90
British Airways	1,821,720	1,418,070	0.37	0.29	7.04	5.48	9.99	7.77	4.57	3.56	2.01	1.57
Mexicana	725,500	560,000	0.97	0.75	10.03	7.75	5.37	4.15	3.69	2.85	1.84	1.42
VASP	601,200	91,000	1.65	0.25	35.36	5.35	NM	NM	30.52	4.62	NM	NM

Note: Market value of company = (Market value of equity) + (Debt + Capital leases). The market values used to determine the ratios above assume 100% onwnership and are derived from the actual transaction. NM = not meaningful.

Table 22
Composition of Group Falcon

	Investment (thousands of US$)	Share % (%)
Xabre	46.00	32.9
Elías Sacal	15.0	10.7
Carlos Adendnp	7.0	5.0
Fam. Name Yapur	2.0	1.4
R. Cenizzo	1.4	1.0
Mexican Sub-total	71.4	51.0
Chase Manhattan Bank	50.0	35.7
DBL American Dev. Assoc.	10.0	7.1
J. Goldsmith	8.5	6.1
Foreign	68.6	49.0
Total	140.0	100.0

Table 23
CMA's acquisitions

			Millions of US$		
Subsidiary	Acquisition date	% owned by CMA	Acquisition price (SM)	Acquisition basis (SM)	CMA book value
Turborreactores	Aug. 10, 1990	99.04	18.83	20.00[a]	36.98
SERTEL	July 1990	50	24.00	12.00	12.00
Datatronics	Sept.20, 1990	100	1.10	1.10	0.66
AeroCaribe	Aug. 24, 1990	100	3.62	3.62	2.49
AeroCozumel	Aug. 24, 1990	100	0.91	0.91	2.07
AeroMonterrey	Start-up 1990	100	7.50[b]	7.50	7.50[c]
Aeropuertos y terrenos	Sept.19, 1990	100	9.16	9.16	20.17
				50.94	81.87

a CMA purchased 94.15% of Turborreactores for US$18.83 million. It already owned 5%.
b Estimated.
c Estimated. AeroMonterrey's aircraft are actually owned by another CMA subsidiary.

Table 24
CMA's fleet acquisition plans and expenditure

	1990	1991	1992	1993	1994	1995
Expenditure (millions of US$)	68.1	156.7	214.1	158.3	173.7	855.7
Delivery (No.)	-	4	6	4	4	4

Source: CMA Annual Report and documents.

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