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Mexicana Airlines to be Sold to Mexican Investor Grupo Posadas

by LADB Staff
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President Vicente Fox's administration has agreed to sell Mexicana airlines to hotel chain Grupo Posadas for US$165.5 million. The transaction is part of the government's efforts to sell off its shares in airline holding company Corporacion Internacional de Transporte Aereo (CINTRA) to private investors. The government also placed Mexico's other flagship airline Aeromexico on the auction block, but the sale was postponed because the lone bid submitted by Grupo Xtra was deemed inadequate.

The government assumed majority control of CINTRA in 1994, when the savings protection agency (Fondo Bancario de Proteccion al Ahorro, FOBAPROA) acquired Aeromexico and Mexicana to prevent them from falling into serious financial difficulty (see SourceMex, 1995-01-18). In late 2004, the government's anti-trust agency (Comision Federal de Competencia, CFC) approved a plan to merge Mexicana and Aeromexico into a single company (see SourceMex, 2004-11-03 and 2005-02-29). The government reversed its stance in early 2005 and decided to sell Mexicana and Aeromexico as separate entities.

CINTRA officials said the scheme approved last year left the process open to anti-trust actions because Aeromexico and Mexicana control two-thirds of Mexico's domestic market. The government's plan to sell the two airlines and their respective subsidiaries, Click Mexicana and Aerolitoral, initially attracted scant interest (see SourceMex, 2005-07-27). By August 2005, however, as many as 11 partnerships or companies had submitted bids or expressed serious interest in submitting bids. This included foreign airline companies Iberia and Icelandair, the pilots union (Asociacion Sindical de Pilotos Aviadores, ASPA), and Mexico's Grupo Angeles, which manages a network of hospitals.

Grupo Posadas only viable bidder at deadline

The situation changed again by the Nov. 21 deadline, when Grupo Posadas remained the only party with an active bid for Mexicana. The case was similar for Aeromexico, where the only remaining bid was submitted by industrial conglomerate Grupo Xtra, owned by Mexican entrepreneur Isaac Saba and family.

The lack of viable bids at the deadline raised some questions about the financial health of Mexicana and Aeromexico, which have suffered the same economic woes as the global aviation industry. "The aviation industry has faced its worst financial crisis in the last five years," said syndicated columnist Sergio Sarmiento. "In 2005 alone, global commercial aviation, hampered by the high cost of fuel, will suffer a loss of US$7.5 billion. Accumulated losses since 2001 amount to US$40 billion."

The potential buyers cited a variety of reasons for withdrawing. Iberia and Icelandair, for example, cited the government's regulations requiring a majority Mexican ownership in the two airlines.
Grupo Angeles, a major hospital group in Mexico, was disqualified because the company failed to turn in a letter of credit by a specified deadline. ASPA, which represents just over 2,000 pilots at Aeromexico, Mexicana, Click, and Aerolitoral, dropped its bid after negotiating an agreement with the government by which the union would receive 5% percent stakes in each of the privatized airlines in exchange for meeting productivity goals.

Sarmiento said the Mexican aviation industry showed some signs of recovery last year. "In 2004, CINTRA actually made a profit," said the columnist. "This situation is not as good in 2005 because of fuel costs, but the return to financial health is what prompted the government to finally proceed with the sale of the airlines."

Another concern is the increased competition from discount airlines, many of which have come on the scene just this year (see SourceMex, 2005-07-27). Mexican officials said this was not a hindrance in the privatization of CINTRA. "There is strong potential for growth in the Mexican airline industry, so the market should be ample for all the players," said deputy transportation secretary Aaron Dychter. Grupo Posadas paid US$165.5 million for Mexicana, but the total cost will rise to US$1.45 billion after the new owner and its partners factor in Mexicana debts of US$294 million and the US $997 million cost of aircraft leases.

Grupo Posadas' strong connection to the tourism industry raised some concerns that the purchase of Mexicana might open the door for the company to engage in some monopolistic practices. Tourism Secretary Rodolfo Elizondo countered that the move could actually have the opposite effect, since Posadas would be very interested in attracting more clients to its hotels. "Grupo Posadas is the largest hotel group in our country," said Elizondo. "The link of the hospitality industry and aviation could actually result in lower air fares, which is what we all want."

Some concerns raised about transaction
Critics also raised concerns about the privatization process, including charges that the sale price for Mexicana was too low and that Posadas was not in a strong financial position to acquire the airline. There were also questions about whether there was some insider information used in a separate but related transaction.

One of the minority holders in Mexicana, the giant financial institution Grupo BBVA-Bancomer, had advance access to privileged information from the savings protection institute (Instituto de Proteccion al Ahorro Bancario, IPAB), which was handling the sale of CINTRA. BBVA-Bancomer is accused of benefiting from the process to the detriment of taxpayers, who fund IPAB.

Concerns were especially strong about the liquidity of Grupo Posadas, with the paying price of US$165.5 million taking up much of the company's available cash. This led some critics to raise suspicions that the sale might have involved illegal or irregular financial transactions to benefit the buyer. Several financial-rating companies, including Standard & Poor's (S&P), Moody Investor Services, and Fitch Ratings, issued cautionary assessments for Grupo Posadas debt. The concerns about Grupo Posadas' financial health led the Chamber of Deputies to ask the congressional audit agency (Auditoria Superior de la Federacion, ASF) to conduct a comprehensive audit of the sale. "In the initial analysis, something does not seem right about this sale," said Deputy Jesus
Gonzalez Schmal, a member of the Partido Convergencia por la Democracia (PCD) and chair of the subcommittee on airports (Subcomision de Aeropuertos) in the lower house. "The value of the building owned by Mexicana is US$75 million, and the company paid US$165 million for the airline."

**Congress seeks information on Aeromexico bids**

The Chamber of Deputies has also asked ASF to examine the circumstances surrounding the bidding process for Aeromexico in conjunction with the investigation of the Mexicana sale. Grupo Xtra submitted the only bid, which was rejected. Gonzalez Schmal noted that neither Grupo Posadas nor Grupo Xtra had any experience in the aviation industry. "We want to know whether the government engaged in a process by which the two airlines were given or sold at a very low prices to these two bidders," said the PCD legislator.

CINTRA chairman Andres Conesa Labastida denied any irregularities in the privatization of the two airlines. He said the offers by the two companies were viable, except that Grupo Posadas bid was very close to the government's asking price, especially with the strong participation of some minority partners. "I wouldn't say [Grupo Posadas] paid too much or that it went for less than it is worth. I'd call it a fair price," Conesa told Reuters.

In contrast, Grupo Xtra's bid was only 75% of the real value of Aeromexico. "It would have been more difficult to raise the additional 25%," said Conesa. Some private analysts agreed with this assessment. "There is not much appetite out there for Aeromexico," said stock analyst Jaime Aguilera of the Mexico City office of HSBC. Conesa said the privatization of Aeromexico would be reopened sometime in early 2006, either through another direct bidding process, a sale of shares on the Mexican stock exchange (Bolsa Mexicana de Valores, BMV), or a combination of the two. (Sources: Associated Press, 11/22/05; Radio Formula, 11/25/05; The Herald-Mexico City, 11/29/05; Reuters, 11/30/05; El Financiero, 11/21/05, 11/30/05, 12/01/05; La Cronica de Hoy, 11/22/05, 11/29/05, 12/01/05; La Jornada, 11/30/05, 12/01/05, 12/02/05; Reforma, 11/29/05, 11/30/05, 12/01/05, 12/05/05; El Universal, 11/29/05, 11/30/05, 12/01/05, 12/02/05, 12/05/05; El Economista, 11/30/05, 12/05/05)

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