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transaero: Turbulent times[[1]](#footnote-1)

Elena Senatorova, Grigori Erenburg, and Ruth Ann Strickland wrote this case solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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Max Feldman, a 39-year-old professor at Moscow State University, was looking forward to an upcoming trip to Canada. Feldman was going to visit Western University in London, Ontario, for four months to work on a collaborative research project in financial analysis. He had never been to Canada, and he had many plans and research ideas. The whole trip was planned with a departure in October 2015. Feldman had already purchased his tickets for a convenient non-stop flight from Moscow to Toronto with OJSC Transaero Airlines (Transaero).

In September 2015, news broke about the possible bankruptcy of Transaero, the safest and second-largest airline company in Russia, catching most people by surprise. In light of the news, with his flight already booked, Feldman needed to decide whether or not to cancel the tickets he had booked and fly with a different airline. He wondered what had gone wrong with the airline. How did this large, sustainable, and reliable company—one with a good reputation—get into such financial trouble? Could it have been foreseen and prevented? What would happen with Transaero in the near future? Feldman began to analyze Transaero’s financial data to gain a deeper understanding of the issues and to find possible solutions.

COMPANY BACKGROUND

Transaero, one of Russia’s largest private companies, was established in 1990 by Aleksandr Pleshakov and his mother, Tatiana Anodina. Anodina had been the head of the Interstate Aviation Committee, the supervisory body overseeing aviation in the Commonwealth of Independent States (CIS).[[2]](#footnote-2) Aleksandr’s father, Peter Pleshakov, was the Soviet Union’s minister of radio industry from 1974 until 1987. Aleksandr’s wife, Olga Pleshakova, was the chief executive officer (CEO) of Transaero from 2001 to 2015. Transaero’s official date of inception was November 5, 1991, the date of its first charter service.[[3]](#footnote-3)

Over time, Transaero had strengthened its position in different markets, especially in domestic and international flights, including routes with strategic importance such as from Moscow to Beijing, New York, and Toronto. Transaero focused on fleet renewal and increase of its efficiency. “During the period from 2010 to mid-2013 Transaero was expanding its fleet – the number of operated aircraft increased from 47 ones (01.01.2010) to 100 ones (01.01.2014)”.[[4]](#footnote-4)

As Feldman studied Transaero’s 2013 annual report, he noticed that Transaero had more than 200 routes (44 per cent were in Europe; 28 per cent were in Russia and CIS). That year, the airline and airport review website Skytrax had named Transaero among the World’s Top 100 Airlines.[[5]](#footnote-5) The number of passengers it had carried in 2013 totalled 12.5 million, an increase of 21.04 per cent from the total number of passengers in 2012, earning the airline a spot among the top 30 airlines in the world for flight volume. This was despite a crisis in the Egyptian travel market, which accounted for about 12 per cent of Transaero’s flights. Transaero’s total revenue in 2013 had increased by 14.81 per cent from its revenue in 2012 (see Exhibit 1). Aleksandr, who was the chairman of the board of directors, noted, “[F]rom 2003 to 2013, Transaero’s passenger turnover grew by 47 times... Air freight transportation went up by 25 times. The Company’s fleet expanded by 16 times… New partnerships with international airlines such as Virgin America, WestJet, JetBlue [Airways], and China Airlines were established.”[[6]](#footnote-6)

Olga, Transaero’s CEO, said:

Our company results under IFRS [International Financial Reporting Standards] and RAS [Russian accounting standards] prove the solid financial state of the airline and the sustainability of its development. In 2013, we continued to improve product quality by operating a broad route network, undertaking fleet modernization, and implementing new unique technologies. Our new approach to the airline’s business development strategy is in line with our mission statement “Rational growth, efficiency and strategic focus,” and aims to further increase financial efficiency. This strategy will continue to remain [a] priority for the airline.[[7]](#footnote-7)

SUSTAINABLE DEVELOPMENT

Transaero as a company, and its employees as individuals, believed in using the airline’s success to give back to society. According to the company’s 2013 annual report, Transaero was the only Russian airline company to achieve a Triple A (or “AAA”) rating[[8]](#footnote-8) for corporate social responsibility. The company’s charitable programs included social air transportation, children’s health care, and assistance for persons with disabilities. Three fundamental principles—consistency, partnership, and transparency—guided the company’s charitable programs. Company employees hosted over 30 charitable events in 2014 (see Exhibit 2).[[9]](#footnote-9)

THE SITUATION IN 2014 AND 2015

Transaero started 2014 in a strong position, with key positive events in the first half of the year including the following:[[10]](#footnote-10)

* *Air Transport World* ranked Transaero’s passenger traffic 27th in the world, placing it among Europe’s 10 largest airlines.
* The airline’s superior service for the 2014 Winter Olympics and 11th Paralympic Winter Games in Sochi earned it a Certificate of Merit from the Federal Air Transport Agency.
* Transaero’s policy of encouraging employees to become blood donors led to its receiving the Russian Souchastiye award for corporate involvement.
* A Flightfox[[11]](#footnote-11) survey determined that Transaero’s Imperial Class was among the world’s top 20 first-class cabins.

The situation changed for Transaero in the second half of 2014, making it a very difficult year for Transaero. In the company’s 2014 annual report, Aleksandr stated, “When adopting a new five-year strategy called ‘Balanced Growth, Focus and Efficiency’ in October 2013, the Board of Directors predicted a worsening in the operating environment, especially in market, financial, and economic conditions. However, the reality, which can be accurately described by the well-known term ‘a perfect storm,’ turned out to be much more difficult.”[[12]](#footnote-12)

Transaero’s 2014 financial statement data (see Exhibit 1), under IFRS, was influenced by three negative economic factors: (1) the acceleration in Transaero’s debt repayments at the time (when interest rates were rising), and banks responding to international sanctions by limiting their lending; (2) a decline in international travel due to a sharp decline in the value of the Russian ruble and aggravated by an increase in oil prices, prompted the need for the company to reduce prices and lower capacity expectations; and (3) restrictions imposed against flying over Ukraine, leading to a significant increase in the company’s operating expenses.[[13]](#footnote-13)

Between July and December 2014, Transaero repaid RUB9 billion.[[14]](#footnote-14) Then, banks began restricting lending, and the company was unable to obtain normal refinancing of its commercial loans. It applied for, and was granted, a state guarantee from the government of the Russian Federation for a RUB9 billion credit facility from VTB Bank, a global provider of financial services. This guarantee helped Transaero retain some financial stability despite the collapse of the ruble and the high volatility of domestic sales in Russia.[[15]](#footnote-15)

The company continued with its established focus on social air transportation, children’s health care programs, and corporate volunteering. The new credit guarantee allowed Transaero to add two additional social responsibilities: avoiding employee job loss and maintaining affordable domestic flights by freezing fares within Russia. Competitors viewed the latter action as “dumping.”[[16]](#footnote-16)

In 2015, customers began to purchase more tickets in advance, which resulted in an increase in unearned revenue.[[17]](#footnote-17) Feldman saw the unearned revenue from payments for future flights as a positive sign for Transaero. Also in 2015, Transaero was ranked among the top 20 safest airlines in the world according to JACDEC’s[[18]](#footnote-18) airline safety ranking for that year.[[19]](#footnote-19)

However, the weakening ruble at that time caused a significant increase in financing costs related to foreign currency loans (see Exhibit 3). Sanctions led to Russian bank losses and limited banks’ access to international capital markets. Transaero saw a significant shortening of the average loan maturity period, along with increased borrowing costs.[[20]](#footnote-20)

In response to these challenges, Transaero maintained its focus on reducing general operating expenses and costs related to fleet repairs and modifications. Attempts were made to optimize flight schedules. The company achieved a 4 per cent increase in customer volume in its unique Imperial Class and its business class. It completed modifications to its Boeing 747s, and a program to increase the seating capacity of its Boeing 767s was extended into 2015 to complete the last three planes. The company made significant improvements to its customer relationship management system and to its website to increase web sales. Global management consultants McKinsey & Company CIS assisted with the development and adoption of “Better and Cheaper” as a business improvement program for 2015. Transaero was also making preparations for the delivery of Airbus A321 aircraft, while delivery schedules were postponed for new Airbus A380 and Boeing 747-8 aircraft.[[21]](#footnote-21)

As Feldman conducted his analysis, he realized that despite the losses and challenges, Transaero had tried to survive. In 2014, the company achieved an increase both in number of passengers carried and in revenue, while total operating costs per flight decreased by 10.3 per cent. During 2011–2013, while the fleet was increasing every year and new routes were opening, Transaero’s seat occupancy rate was above 82 per cent, which was higher than PJSC Aeroflot Russian Airlines’ (Aeroflot’s) (77–79 per cent) and the rate for the industry as a whole (78–80 per cent). In 2014, load management at Transaero was equally efficient, with the load factor remaining at 84 per cent.[[22]](#footnote-22)

A serious problem emerged from Feldman’s analysis of Transaero’s statements: incorrect financial reporting data according to RAS. Also, the largest part of intangible assets—Transaero’s brand—was recognized in the financial statements under IFRS. However, the auditors noted in the auditor’s report in 2014 that they did not receive enough audit evidence that the 2014 financial report information complied with the requirements of International Accounting Standard 38, Intangible Assets.[[23]](#footnote-23) Transaero fixed this error only in its half-year financial report of 2015. The error created a very large but short-term bump in 2014 for the intangibles account. It also affected the dynamics of the deferred tax account on the balance sheet, causing a deferred tax liability in 2014 and a deferred tax asset in 2015.[[24]](#footnote-24) Feldman wondered if Transaero had deliberately manipulated its earlier financial reporting data to obtain loans and state guarantees.

Feldman examined the Russian airline industry’s data provided in Transaero’s 2014 annual report. Russia’s largest airlines, including Transaero, Aeroflot, OJSC S7 Airlines, and JSC UTair Aviation, accounted for 65 per cent of total passenger traffic, an increase from 53 per cent in 2010. Aeroflot (25 per cent in 2014) was Transaero’s most important competitor (14 per cent in 2014).[[25]](#footnote-25) Aeroflot was founded in 1923 and was one of the oldest airlines in the world.[[26]](#footnote-26) For many years, it was the only airline company in the Soviet Union. After the fall of the Soviet Union, Aeroflot became a public company, with the Russian government owning 51 per cent.[[27]](#footnote-27) Feldman compared data from Transaero’s financial reports with Aeroflot’s information, and noticed that Aeroflot’s financial position and financial results were much stronger than Transaero’s were. Part of Aeroflot’s revenue included royalties that foreign airlines had paid for flying through Russian airspace. Feldman was surprised to see these royalties in Aeroflot’s financial reports because they were supposed to be paid to the Russian government. He discovered that Aeroflot had historically received royalty payments from the Soviet Union.[[28]](#footnote-28) In the Soviet Union, Aeroflot had been a monopolist; it had been the only Russian carrier before becoming a public company. Feldman asked himself, were Aeroflot’s royalties the main reason for its stronger financial results? He wondered if Aeroflot could have played a role in Transaero’s problems.

The second half of 2015 brought some new and interesting events to Transaero: on August 31, Aleksandr, Olga, and Anodina all resigned.[[29]](#footnote-29) On September 1, Aeroflot attempted to acquire a controlling stake in Transaero for the symbolic price of RUB1.[[30]](#footnote-30) And on September 7, Aeroflot’s executive director, Dmitry Saprykin, was appointed CEO of Transaero.[[31]](#footnote-31)

Feldman looked through relevant online data and saw that Transaero’s most important debtholder was planning to ask the commercial court to initiate bankruptcy proceedings against the company. Moreover, top management of the third-largest Russian airline company, PJSC S7 Airlines, was interested in purchasing 51 per cent of Transaero’s shares.[[32]](#footnote-32)

OTHER AIRLINEs IN TROUBLE

The Demise of Pan Am[[33]](#footnote-33)

Feldman analyzed the experience of other airline companies that had been in trouble. He examined the tragic experience of Pan American World Airways (Pan Am), which had once been the largest U.S. airline. Pan Am was the first airline to carry passenger flights across the ocean (to the United Kingdom), and the first airline to purchase wide-bodied aircraft. In 1948, Pan Am launched the first ever economy-class flight. The legendary round terminal at John F. Kennedy International Airport in New York belonged to the airline and continued to carry its name.

The first step leading to the collapse of Pan Am was in 1969, when the company received a large shipment of Boeing 747s that had been commissioned three years earlier. In that year, the economy experienced a downturn, which reduced demand for passenger flights and made carrying a large number of aircraft commercially unviable. The 1973 oil crisis brought another challenge for the “most experienced airline in the world,” as Pan Am’s slogan of those years proclaimed. Soaring fuel prices, along with sharply reduced demand for air travel delivered a significant blow to the air giant. The company’s losses for the years 1969–1976 amounted to US$364 million, and its debt grew to a billion dollars.

In 1985, Pan Am’s main competitor, United Airlines, acquired all of Pan Am’s routes to the Asia-Pacific region. After two terrorist attacks on board Pan Am flights in 1986 and 1988, fewer people were choosing the company’s flights. The carrier’s insurance company for a long time refused to reimburse the hundreds of millions of dollars that Pan Am owed to the relatives of terrorist attack victims. The fuel crisis that ensued from the Gulf War in 1990–1991 brought the final blow to the company, and in December 1991, the legendary Pan Am declared bankruptcy and ceased to exist. The carrier’s debt at that time amounted to US$9 billion. Delta Air Lines Inc. (Delta) acquired the remaining profitable assets. Subsequent attempts to revive the brand ended in failure.

The Bankruptcy of Delta[[34]](#footnote-34)

Feldman learned that the rights to fly the European routes, the largest trans-Atlantic destinations, inherited from Pan Am by Delta brought the latter to a leadership position in terms of the number of passengers and the number of flights carried across the Atlantic. It did not, however, save Delta from the crisis that began in the airline industry following the attacks of September 11, 2001.

The drop in demand, a further increase in oil prices, and the emergence of low-cost competitors caused Delta to lose US$10 billion over 2001–2005. In 2004, the company attempted to evade bankruptcy by conducting mass layoffs and reducing the salaries of the remaining employees. The airline’s pilots agreed to work for approximately 70 per cent of their initial rate. At the same time, the airline introduced new flights.

The measures did not work: on September 14, 2005, the company was forced to declare bankruptcy. At that time, this third-largest U.S. carrier had US$20.5 billion in debt. Fortunately, two years later, the company managed to overcome the crisis. On April 25, 2007, the court approved the carrier’s plan to exit bankruptcy. Old shares of Delta were cancelled, and new ones began trading on the New York Stock Exchange at US$20 per share.

**European Experience: Swissair[[35]](#footnote-35)**

As part of his analysis, Feldman looked at the history of airline business collapses in Europe. In 2001, the main Swiss airline, Swissair, declared itself bankrupt after 70 years in business.

Many analysts believed that the “beginning of the end” for Swissair had been the airline’s decision to create a new air alliance. The first step in doing so had been the purchase of a controlling stake in Crossair, followed by the acquisition of Belgian airline Sabena. The main idea was to secure the shares of small and not-well-known European carriers. Only the upper management of the carrier seemed to understand why this was necessary for Swissair.

In 1998, the airline extended the “Qualiflyer” alliance, bringing together more than 20 airlines, most of which were experiencing financial difficulties. However, constant subsidizing of the less-fortunate partners depleted Swissair’s resources, and the crisis in the aviation world following the September 11 attacks in the United States ultimately finished the company. The carrier’s debt at the time of bankruptcy exceeded CHF38 billion.[[36]](#footnote-36)

According to the conclusions of the auditors, it was “management errors, dubious methods of accounting, and lack of control” that contributed to the bankruptcy of Swissair. A few months after the collapse, the airline arranged for the sale of its property; among the lot were the ski suits of the top managers, silver trays and ice buckets, and plush toy planes with the Swiss flag. According to experts, the sale brought in about CHF10 million, which was only a drop in the ocean of Swissair’s debt.

Officially, the company ceased to exist on March 31, 2002, and a new carrier, Swiss International Air Lines (Swiss), was created in its place. In June of the same year, the Zurich prosecutor’s office launched an investigation into the cause of the bankruptcy and initiated lawsuits against the three top managers of the company.

Another European Experience: Great Expectationsof Alitalia in 2017[[37]](#footnote-37)

Italy’s national carrier, Alitalia, declared bankruptcy in 2008. In the same year, the authorities agreed to sell it to French airline Air France, Dutch airline KLM Royal Dutch Airlines, and German airline Lufthansa. However, upon being elected prime minister, Silvio Berlusconi interrupted the deal, arguing that the company must remain national. Under Berlusconi’s leadership, the Italian Parliament adopted a law on the bankruptcy of state companies that cost the country €5–6 billion.[[38]](#footnote-38)

Alitalia’s losses were written off. But these measures did not help. In 2013, Alitalia was on the threshold of a new bankruptcy, with debt of approximately €1 billion. The company was hoping for a partnership with the Franco–Dutch group Air France–KLM, which owned a 25-per-cent stake in Alitalia, but the alliance refused to participate in the further capital increase. Help came from the United Arab Emirates: Etihad Airways acquired a 49.9-per-cent stake in the Italian carrier for €1.75 billion.

CONCLUSION

From his academic and practical experience, Feldman knew that it was common for airline companies to have high financial leverage. Most aircraft were financed through financial leasing. The airline industry typically had high operating leverage, with a lot of fixed costs. The combination of high financial and high operating leverage created enormous risks, especially during macroeconomic crises.

Feldman tried to identify an acceptable level for financial leverage and other ratios in the airline industry (see Exhibit 4). Information that Feldman obtained on European emerging markets included the financial data of Transaero, Aeroflot, JSC UTair Aviation, and Croatia Airlines Ltd. Feldman tried to answer the question of whether it was possible for Transaero to avoid problems in 2015 without support from the Russian government.

Feldman knew that, according to IFRS, leases were classified into capital leases and operating leases. He suspected that Transaero carried considerable operating leases. While economically a part of a company’s liability, operating leases were not reflected on the balance sheet. Unfortunately, there was no information availablein Transaero’s reportsabout operating leases. To get an idea of the size of operating leases, Feldman looked at data on the number of aircraft the airline had in 2013–2014 (seeExhibit 5).

Feldman tried to analyze the decisions made by top management, including the extremely high financial leverage, alleged dumping, and alleged manipulation of financial reports. He was impressed by the role of Olga in the development of the company; she was the first woman to assume the position of head of a Russian airline company. She was also the only Russian among the 50 “Most Powerful Women in Business” according to *Fortune’s* annual ranking in 2012 and 2013.

Feldman identified the most important events that influenced Transaero’s problems: an increase in oil prices, the introduction of international sanctions, and the decline in the exchange rate of the ruble against the U.S. dollar.

Transaero’s auditor was the well-known RSM RUS.[[39]](#footnote-39) Feldman carefully read the auditor’s reports, considering it strange that the auditors had not considered the errors in the 2012–2014 financial statements as significant. Next, Feldman went through online articles about Transaero. He tried to gain a broader picture by assessing how Transaero’s possible bankruptcy could affect the entire Russian airline industry and its main stakeholders.

Feldman knew that the Russian government could support Transaero to avoid cutting jobs and prevent problems for large tour companies. Many of Russia’s largest tour operators had already booked tickets through Transaero. Feldman understood that such cases should motivate regulators to change legislation. He wondered if, according to international practice, a new company would eventually arise from the debris of Transaero.

Feldman knew that customers were rarely protected against bankruptcies in Russia. It would be impossible to refund tickets that had already been sold to customers if the company was dissolved. Feldman needed to quickly decide whether to cancel his flights and re-book with another airline. He would not be able to get the convenient direct flights that Transaero had offered, but if he waited he might lose both his flight and his money.

Feldman looked through Transaero’s reports and online data again. Was it possible for Transaero to avoid bankruptcy or, if it could not, to recover from it? What lessons must be learned by the main stakeholders?

Exhibit 1: TRANSAERO Financial Statements

(A) Transaero Income Statement (in RUB millions)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **For the Fiscal Period Ending** | **12 months Dec. 31, 2011** | **12 months Dec. 31, 2012** | **12 months Dec. 31, 2013** | **12 months Dec. 31, 2014** | **12 months Jun. 30, 2015\*** |
| Revenue | 68,226.0 | 91,843.5 | 105,449.3 | 113,761.5 | 116,258.9 |
| Cost of Goods Sold | 62,244.9 | 75,918.6 | 104,963.7 | 102,629.4 | 100,063.5 |
| **Gross Profit** | 5,981.1 | 15,925.0 | 485.7 | 11,132.0 | 16,195.4 |
| Selling, General, & Admin Expenses | 3,605.5 | 5,095.5 | 3,655.4 | 3,773.4 | 4,421.5 |
| Depreciation & Amortization | 1,632.3 | 2,637.1 | 3,289.4 | 2,819.7 | 3,088.4 |
| Other Operating Expenses/(Income) | 159.8 | 139.0 | - | - | (25.1) |
| Operating Expenses, Total | 5,397.6 | 7,871.5 | 6,944.7 | 6,593.1 | 7,484.8 |
| **Operating Income** | 583.5 | 8,053.4 | (6,459.0) | 4,539.0 | 8,710.7 |
| Interest Expense | (6,215.3) | (8,509.3) | (10,627.5) | (13,762.3) | (18,844.0) |
| Currency Exchange Gains (Loss) | (283.2) | (1,025.5) | (984.5) | (9,484.0) | (4,226.1) |
| Other Non-Operating Income (Expenses) | 3,728.3 | 1,137.8 | 1,693.0 | 334.1 | 5,104.4 |
| Gain (Loss) on Sale of Investments | - | (355.5) | - | - | - |
| Gain (Loss) on Sale of Assets | 4,379.1 | 975.2 | 402.5 | 51.4 | 419.8 |
| **Earnings Before Tax** | 2,192.4 | 276.1 | (15,975.6) | (18,321.8) | (8,835.2) |
| Income Tax Expense | 0.3 | 504.1 | (2,634.5) | (3,858.8) | (1,643.1) |
| **Net Income** | 2,192.1 | (228.0) | (13,341.1) | (14,463.0) | (7,192.1) |

(B) Transaero Balance Sheet (in RUB millions)

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Balance Sheet as of:** | **Dec. 31, 2011** | **Dec. 31, 2012** | **Dec. 31, 2013** | **Dec. 31, 2014** | **Jun. 30, 2015** |
| **ASSETS** |  |  |  |  |  |
| Cash & Equivalents | 3,203.3 | 518.2 | 1,360.0 | 461.6 | 1,012.6 |
| Short-Term Investments | 12.1 | 10.9 | 2,055.4 | 246.9 | 695.9 |
| Accounts Receivable | 1,735.0 | 2,654.7 | 3,198.3 | 3,518.6 | 3,722.7 |
| Other Receivables | 4,510.2 | 3,399.0 | 979.1 | 989.5 | 822.6 |
| Inventory | 1,443.2 | 1,995.0 | 4,502.7 | 5,786.9 | 6,011.8 |
| Prepaid Expenses | - | - | 1,873.8 | 3,450.7 | 2,568.2 |
| Restricted Cash | 3.2 | 22.2 | 25.1 | 56.0 | 55.2 |
| Other Current Assets | 5,031.1 | 9,919.6 | 667.1 | 215.9 | 803.9 |
| **Total Current Assets** | 15,938.2 | 18,519.6 | 14,661.6 | 14,726.1 | 15,692.8 |
| Property, Plant, & Equipment | 72,800.9 | 74,464.0 | 75,794.0 | 107,865.0 | 105,034.9 |
| Long-Term Investments | 1.7 | 194.9 | 216.6 | 7.1 | 7.1 |
| Intangible Assets | 2,292.9 | 2,220.1 | 2,169.9 | 61,390.4 | 7,240.6 |
| Deferred Tax Assets | - | - | 2,025.4 | - | 10,949.5 |
| Other Long-Term Assets | 2,824.5 | 3,696.4 | 6,604.2 | 8,865.5 | 16,586.4 |
| **Total Assets** | 93,858.3 | 99,094.9 | 101,471.6 | 192,854.2 | 155,511.2 |

EXHIBIT 1 (B) continued

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **Balance Sheet as of:** | **Dec. 31, 2011** | **Dec. 31, 2012** | **Dec. 31, 2013** | **Dec. 31, 2014** | **Jun. 30, 2015** |
| **LIABILITIES & EQUITY** |  |  |  |  |  |
| Accounts Payable | 9,077.7 | 9,421.6 | 17,870.1 | 26,549.2 | 28,677.2 |
| Short-Term Borrowings | 16,407.8 | 22,011.9 | 24,516.8 | 30,313.7 | 47,595.3 |
| Current Portion of Capital Leases | 4,230.0 | 5,392.8 | 7,506.9 | 10,116.7 | 20,467.6 |
| Current Income Taxes Payable | 133.3 | 211.7 | - | - | - |
| Current Unearned Revenue | - | - | 7,972.9 | 4,649.2 | 17,674.2 |
| Other Current Liabilities | 9,260.1 | 8,521.6 | 3,509.7 | 9,612.3 | 11,838.0 |
| **Total Current Liabilities** | 39,108.9 | 45,559.7 | 61,376.4 | 81,241.1 | 126,252.3 |
| Long-Term Debt | 8,249.2 | 12,727.8 | 25,542.9 | 34,503.8 | 30,928.7 |
| Capital Leases | 35,234.2 | 37,155.1 | 34,295.0 | 32,098.2 | 50,917.0 |
| Non-Current Deferred Tax Liability | - | - | - | 11,578.1 | - |
| **Total Liabilities** | 82,592.3 | 95,442.5 | 121,214.3 | 159,421.1 | 208,098.0 |
| Common Stock | 7.6 | 7.6 | 7.6 | 7.6 | 7.6 |
| Additional Paid in Capital | 2,476.6 | 2,480.3 | 2,393.3 | 2,334.8 | 1,798.8 |
| Retained Earnings | (2,565.4) | (2,852.1) | (29,547.8) | −43,996.9 | (89,979.2) |
| Treasury Stock | (2,360.2) | (2,767.5) | (1,023.4) | −3,059.2 | (3,142.8) |
| Comprehensive Income and Other | 13,707.4 | 6,784.2 | 8,427.6 | 78,146.8 | 38,728.9 |
| Total Common Equity | 11,265.9 | 3,652.4 | (19,742.7) | 33,433.1 | (52,586.8) |
| **Total Equity** | 11,265.9 | 3,652.4 | (19,742.7) | 33,433.1 | (52,586.8) |
| **Total Liabilities & Equity** | 93,858.3 | 99,094.9 | 101,471.6 | 192,854.2 | 155,511.2 |

EXHIBIT 1 (B) continued

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
| **For the Fiscal Period Ending** | **12 months Dec. 31, 2011** | **12 months Dec. 31, 2012** | **12 months Dec. 31, 2013** | **12 months Dec. 31, 2014** | **12 months Jun. 30, 2015** |
| Net Income | 2,192.1 | (228.0) | (13,341.1) | (14,463.0) | (7,192.1) |
| Depreciation & Amortization | 1,632.3 | 2,637.1 | 3,289.4 | 2,819.7 | 3,088.4 |
| (Gain) Loss from Sale of Assets | - | - | (1,835.3) | (1,452.1) | (1,452.1) |
| Provision & Write-Off of Bad Debts | - | - | (82.6) | (167.7) | (167.7) |
| Other Operating Activities | (3,314.5) | 893.1 | 8,530.5 | 20,284.2 | 16,004.4 |
| Change in Accounts Receivable | - | - | 16,389.2 | (11,207.5) | (11,207.5) |
| Change in Inventories | - | - | (2,507.7) | (1,284.2) | (1,284.2) |
| Change in Accounts Payable | - | - | (197.7) | 14,277.9 | 14,277.9 |
| Change in Other Net Operating Assets | - | - | (1,817.8) | (2,238.7) | (2,238.7) |
| **Cash from Operations** | 509.9 | 3,302.2 | 8,426.9 | 6,568.6 | 9,828.4 |
| Capital Expenditure | (18,059.8) | (6,751.2) | (11,941.0) | (2,731.8) | (1,177.2) |
| Sale of Property, Plant, & Equipment | 9.2 | 251.0 | 1,406.5 | 4.9 | (57.5) |
| Cash Acquisitions | - | 87.9 | - | - | - |
| Divestitures | - | - | - | - | (126.1) |
| Investments in Marketable & Equity Securities | 2.0 | (65.6) | (18.8) | 2.3 | (1,978.8) |
| Other Investing Activities | 65.5 | 46.8 | (2,007.6) | 1,551.1 | 1,554.6 |
| **Cash from Investing** | (17,983.2) | (6,431.2) | (12,561.0) | (1,173.5) | (1,785.0) |
| Long-Term Debt Issued | 50,772.0 | 49,022.1 | 77,172.1 | 78,053.6 | - |
| Total Debt Issued | 50,772.0 | 49,022.1 | 77,172.1 | 78,053.6 | 54,121.4 |
| Long-Term Debt Repaid | (28,129.7) | (39,593.0) | (64,188.9) | (68,668.7) | - |
| Total Debt Repaid | (28,129.7) | (39,593.0) | (64,188.9) | (68,668.7) | (46,842.0) |
| Issuance of Common Stock | 2,885.4 | 700.0 | 4,798.6 | 4,044.8 | 1,806.2 |
| Repurchase of Common Stock | (1,150.7) | (1,303.5) | (2,926.1) | (5,979.0) | (2,631.2) |
| Common Dividends Paid | (24.1) | (57.7) | (69.6) | (106.5) | (106.5) |
| Other Financing Activities | (6,118.4) | (8,324.0) | (9,810.3) | (13,637.6) | (14,822.0) |
| **Cash from Financing** | 18,234.5 | 443.9 | 4,975.8 | (6,293.5) | (8,474.0) |
| **Net Change in Cash** | 761.2 | (2,685.1) | 841.8 | (898.4) | (430.7) |

Note: \* The half-year financial report from 2015 was the last available financial statement for Transaero. In the S&P Capital IQ database, this information is reported for the last twelve months, for the period July 1, 2014 to June 30, 2015, not for the last half-year; RUB = Russian ruble; RUB1 = US$0.02 on December 31, 2014.

Source: Transaero Airlines, “Open Joint-stock company Transaero Airlines (MISX:TAER) > Financials,” S&P Capital IQ, accessed February 16, 2017.

**Exhibit 2: CORPORATE SOCIAL RESPONSIBILITY**

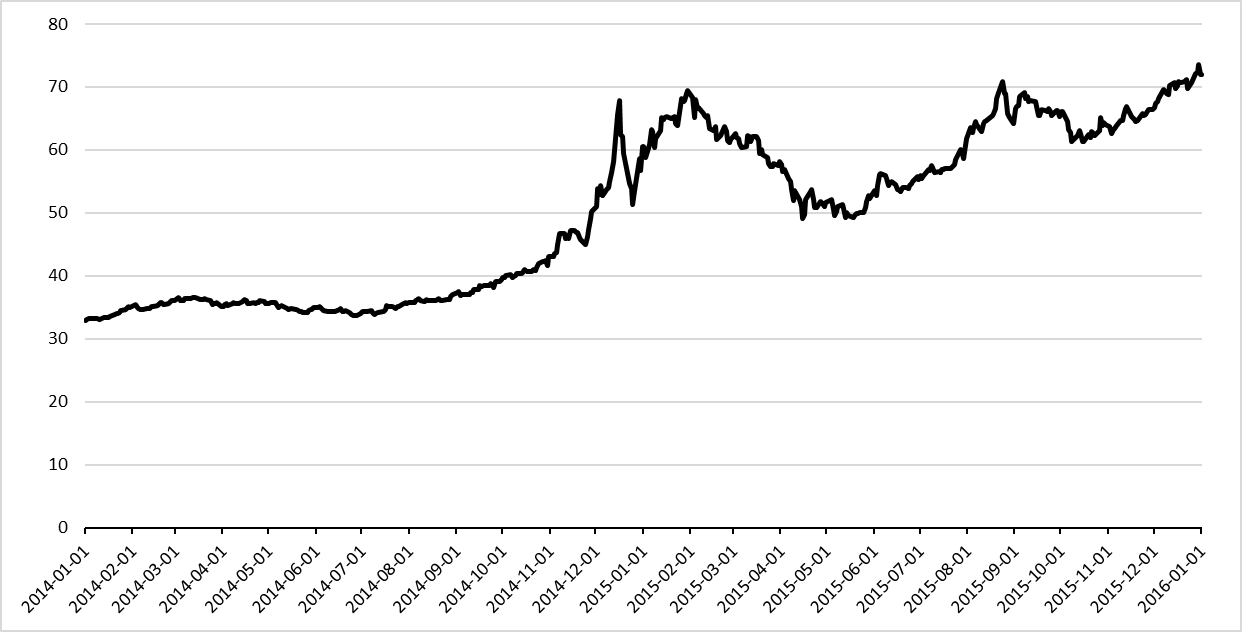
All charitable programs were comprehensive in nature and were implemented following three fundamental principles: consistency, partnership, and transparency.

* Back to the Future: Throughout its years of operation, this program assisted approximately 3,500 children with serious illnesses at all stages—from diagnostics and treatment to rehabilitation. In 2014, Transaero partnered with major Russian charity foundations to carry more than 600 ill children from Russian regions and CIS countries to leading clinics in Moscow and Saint Petersburg, as well as to institutions in the United Kingdom, the United States, Israel, and Germany.
* Flight of Hope: Implemented in November 2013, this project become very popular with passengers by enabling them to make donations during flights for the treatment of children suffering from serious illnesses. More than US$100,000 was raised through this program, making it possible to fund critical surgeries for 21 children. Olga Pleshakova, chief executive officer of Transaero, said: “I am proud that the Flight of Hope passengers are the first in Russia to be able to help children suffering from serious diseases during their flights by making their personal donations. Transaero demonstrates to passengers that helping is simple and one does not even have to leave a seat to do this!”
* Flying with Disabilities: Transaero continued a series of training sessions for its own employees and for employees from airports in Moscow and other cities in Russia that provided theoretical and practical training in how to accommodate and communicate with disabled passengers. In 2014, Transaero carried 100 sports fans with disabilities, including 20 people using wheelchairs, to the world’s largest winter Paralympic competition, on board a Boeing 777 wide-body aircraft. In addition, in partnership with the Sledge Hockey Federation, Transaero organized a flight for Ladoga, Europe’s only junior sledge hockey team, to the United States, where young athletes took part in friendly matches with their U.S. peers. In providing these services, Transaero leveraged its great experience in dealing with persons with disabilities and in understanding the importance of the social function performed by Transaero as one of the largest companies in the industry.
* Flying without Fear: Striving to make the flight experience comfortable for all passengers, Transaero, together with the Flying without Fear Centre, created an in-flight video-based course specially designed for those who experienced aerophobia, or anxiety and fear during flight.
* Travelling to the Transaero Country: This program organized charity events to support the rehabilitation of disabled children, social adaptation of orphaned children, and awareness campaigns to promote charitable ideas among employees and educational projects for Transaero corporate volunteers. Company employees held more than 30 charitable events in 2014, including regular Transaero Days in a rehabilitation camp for disabled children; creative master classes; work by volunteers at paediatric oncology departments of cancer clinics in Moscow and Saint Petersburg; and cultural, educational, and career guidance activities for orphaned children.
* Veterans: Every year, Transaero provided air transportation services to veterans on Victory Day. In 2014, more than 1,000 World War II veterans, survivors of the Leningrad siege, prisoners of fascist concentration camps, and rear workers eligible for benefits took advantage of Transaero’s tickets with a 100 per cent discount.

Note: CIS = Commonwealth of Independent States.

Source: Transaero Airlines, *Transaero Annual Report* 2013, Bloomberg LP, accessed August 1, 2017; Transaero Airlines, *Transaero Annual Report 2014*, Bloomberg LP, accessed August 1, 2017.

Exhibit 3: U.S. DOLLAR VERSUS RUSSIAN RUBLE\*



Note:\* Reported as US$1 in Rubles.

Source: “Historical Quotes for Russian Ruble,” Wall Street Journal online, accessed April 26, 2018, https://quotes.wsj.com/fx/USDRUB/historical-prices.

Exhibit 4: FINANCIAL RATIOS

|  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- |
|  | **Aeroflot** | | **European Emerging Markets** | | **Global Airline Industry** | |
| **2013** | **2014** | **2013** | **2014** | **2013** | **2014** |
| **LIQUIDITY RATIOS** |  |  |  |  |  |  |
| Current Ratio | 1.2x | 0.7x | 1.3x | 0.7x | 0.7x | 0.6x |
| Quick Ratio | 0.8x | 0.5x | 1.5x | 1.3x | 1.2x | 1.2x |
| Cash from Operations to Current Liabilities | 0.4x | 0.3x | 0.7x | 0.3x | 0.3x | 0.2x |
| **EFFICIENCY** |  |  |  |  |  |  |
| Total Asset Turnover | 1.4x | 1.3x | 1.4x | 1.1x | 0.8x | 0.8x |
| Fixed Asset Turnover | 3.4x | 3.1x | 3.2x | 2.7x | 1.5x | 1.4x |
| Average Days Sales Outstanding | 28.1 | 31.3 | 28.7 | 31.2 | 22.8 | 21.9 |
| Average Days Inventory Outstanding | 6.8 | 7.2 | 7.1 | 7.6 | 10.4 | 9.9 |
| Average Days Payable Outstanding | 24.4 | 28.8 | 0.1 | 0.2 | 32.0 | 31.9 |
| Average Cash Conversion Cycle | 10.5 | 9.7 | 7.0 | 10.4 | 10.3 | 10.0 |
| **FINANCIAL LEVERAGE** |  |  |  |  |  |  |
| Total Liabilities/Total Assets | 74.0% | 104.9% | 54.2% | 101.6% | 81.7% | 83.5% |
| Total Debt/Equity | 156.8% | NM | 83.1% | NM | NM | NM |
| Long-Term Debt/Equity | 131.7% | NM | 55.4% | NM | 135.0% | 165.7% |
| EBIT/Interest Expenses | 6.1x | 1.9x | 2.9x | 2.0x | 0.9x | 1.4x |
| **PROFITABILITY** |  |  |  |  |  |  |
| Return on Equity | 13.6% | (83.7%) | 13.1% | NM | 10.5% | 11.0% |
| Return on Assets | 6.1% | 2.4% | 5.9% | 2.1% | 2.3% | 3.3% |
| Return on Sales | 2.8% | (4.8%) | 7.1% | (4.4%) | 0.1% | (0.6%) |
| Gross Margin | 12.1% | 9.3% | 23.1% | 10.0% | 17.5% | 18.2% |

Note: EBIT = earnings before interest and tax. If the denominator is less than or equal to zero, the ratio was shown as NM (not meaningful).

Source: Aeroflot – Russian Airlines, “Public Joint Stock Company Aeroflot - Russian Airlines (MISX:AFLT) > Financials > Ratios,” S&P Capital IQ, accessed February 16, 2017; Airlines, “Airlines > Key Stats & Ratios,” S&P Capital IQ, accessed February 16, 2017; Airlines, “European Emerging Markets > Key Stats & Ratios,” S&P Capital IQ, accessed February 16, 2017.

**EXHIBIT 5: AIRCRAFT INFORMATION**

|  |  |  |
| --- | --- | --- |
| **For the Fiscal Period Ending** | **12 months Dec. 31, 2013** | **12 months**  **Dec. 31, 2014** |
| Total Number of Aircraft | 100 | 104 |
| Aircraft Owned | 9 | 9 |
| Aircraft—Capital Lease | 59 | 59 |
| Aircraft—Operating Lease | 32 | 36 |

Source: Transaero Airlines, “Open Joint-stock company Transaero Airlines (MISX:TAER) > Financials > Industry Specific,” S&P Capital IQ, accessed February 16, 2017.

1. This case has been written on the basis of published sources only. Consequently, the interpretation and perspectives presented in this case are not necessarily those of OJSC Transaero Airlines or any of its employees. [↑](#footnote-ref-1)
2. The Commonwealth of Independent States, also called the Russian Commonwealth, was a regional organization formed during the dissolution of the Soviet Union. Nine out of the 15 former Soviet Republics were member states, and two were associate members. [↑](#footnote-ref-2)
3. Artem Solodkov, Dada Lindell, “The dream of heaven: how Transaero is trying to return to the market [in Russian],” RBK Group, November 14, 2016, accessed June 20, 2017, https://www.rbc.ru/business/14/11/2016/5829a4109a7947623927c0be. [↑](#footnote-ref-3)
4. “The Fleet of Transaero Will Comprise 109 Aircraft by 2018,” Russian Aviation, April 30, 2014, accessed July 20, 2017, www.ruaviation.com/news/2014/4/30/2301. [↑](#footnote-ref-4)
5. Skytrax, “The World’s Top 100 Airlines—2013,” World Airline Awards, accessed July 15, 2017, www.worldairlineawards.com/awards/world\_airline\_rating\_2013.html. [↑](#footnote-ref-5)
6. Transaero Airlines, Transaero Annual Report 2013, Disclosure Center, Corporate Information, accessed April 26, 2018,e-disclosure.ru/portal/FileLoad.ashx?Fileid=895115. [↑](#footnote-ref-6)
7. Transaero Airlines, “Transaero Airlines Announces IFRS Results for 2013,” press release, April 30, 2014, accessed July 15, 2017, https://aviator.aero/press\_releases/17213. [↑](#footnote-ref-7)
8. A Triple A rating was the highest rating assigned to an issuer's bonds by credit rating agencies. [↑](#footnote-ref-8)
9. Transaero Airlines, Transaero Annual Report 2013, Disclosure Center, Corporate Information, accessed April 26, 2018,e-disclosure.ru/portal/FileLoad.ashx?Fileid=895115. [↑](#footnote-ref-9)
10. Transaero Airlines, *Transaero Annual Report 2014*, Bloomberg LP, accessed August 1, 2017. [↑](#footnote-ref-10)
11. Flightfox was a website offering a consultative flight searching ability to help customers find the best fares and construct optimal itineraries. [↑](#footnote-ref-11)
12. Transaero Airlines, Transaero Annual Report 2014, Disclosure Center, Corporate Information, accessed April 20, 2017, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-12)
13. Transaero Airlines, Transaero Annual Report 2014, Disclosure Center, Corporate Information, accessed April 20, 2017, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-13)
14. RUB = Russian ruble; RUB1 = US$0.02 on December 31, 2014. [↑](#footnote-ref-14)
15. Anne Paylor, “Russian Government Agrees to Bail out Transaero Airlines,” *Air Transport World*, December 29, 2014, accessed June 23, 2017, http://atwonline.com/daily-news/russian-government-agrees-bail-out-transaero-airlines. [↑](#footnote-ref-15)
16. Transaero Airlines, Transaero Annual Report 2014, Disclosure Center, Corporate Information, accessed April 20, 2017, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-16)
17. Transaero Airlines, Transaero Annual Report 2015, Disclosure Center, Corporate Information, accessed April 26, 2018, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-17)
18. JADEC = Jet Airliner Crash Data Evaluation Centre [↑](#footnote-ref-18)
19. Transaero Airlines, *Transaero Annual Report 2014*, Disclosure Center, Corporate Information, accessed April 26, 2018, http://e-disclosure.ru/portal/files.aspx?id=12696&type=4. [↑](#footnote-ref-19)
20. Transaero Airlines, Transaero Annual Report 2015, Disclosure Center, Corporate Information, accessed April 26, 2018, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-20)
21. “Transaero clarified the delivery time for new Airbus and Boeing”, ATO, October 8, 2014, accessed March 20, 2017, http://www.ato.ru/content/aviakompaniya-transaero-utochnila-sroki-postavok-novyh-airbus-i-boeing?sea=20069. [↑](#footnote-ref-21)
22. Transaero Airlines, *Transaero Annual Report 2014*, op. cit.; “JSC ‘TRANSAERO Airlines [in Russian],’” Disclosure Center, Corporate Information, accessed November 10, 2017, www.e-disclosure.ru/portal/files.aspx?id=12696&type=4. [↑](#footnote-ref-22)
23. Transaero Airlines, Transaero Annual Report 2014, page 3, Disclosure Center, Corporate Information, accessed April 26, 2018, http://e-disclosure.ru/portal/files.aspx?id=12696&type=4. [↑](#footnote-ref-23)
24. Transaero Airlines, “Open Joint-stock company Transaero Airlines (MISX:TAER) > Financials,” Financial Statements for 2014, 2015,” S&P Capital IQ, accessed November 20, 2017, www.capitaliq.com. [↑](#footnote-ref-24)
25. Transaero Airlines, Transaero Annual Report 2014, Disclosure Center, Corporate Information, accessed April 20, 2017, http://e-disclosure.ru/portal/files.aspx?id=12696&type=2. [↑](#footnote-ref-25)
26. Oliver Smith, “Aeroflot: from world's deadliest airline to one of the safest in the sky”, The Telegraph, February 9,2016, accessed March 15, 2017, https://www.telegraph.co.uk/travel/news/Aeroflot-from-worlds-deadliest-airline-to-one-of-the-safest-in-the-sky/. [↑](#footnote-ref-26)
27. “Aeroflot--Russian International Airlines History”, Fundinguniverse, accessed March 20, 2017, http://www.fundinguniverse.com/company-histories/aeroflot-russian-international-airlines-history/. [↑](#footnote-ref-27)
28. JSC Aeroflot Russian Airlines, IFRS Consolidated Financial Statements for the year ended 31 December 2014, accessed March 20, 2017, http://ir.aeroflot.com/fileadmin/user\_upload/files/eng/companys\_reporting/financial\_statements/fy2014.pdf. [↑](#footnote-ref-28)
29. Kathrin Hille, “High drama as Russia’s Transaero edges towards bankruptcy”, Financial Times, November 8, 2015, accessed July 20, 2017, https://www.ft.com/content/8cb09032-84ad-11e5-8095-ed1a37d1e096. [↑](#footnote-ref-29)
30. Maksim Blinov, “Russia’s Biggest Private Airline Bought for a Ruble,” RT, September 2, 2015, accessed March 15, 2017, www.rt.com/business/314101-transaero-aeroflot-airlines-russia. [↑](#footnote-ref-30)
31. Kathrin Hille, “High drama as Russia’s Transaero edges towards bankruptcy”, Financial Times, November 8, 2015, accessed July 20, 2017, https://www.ft.com/content/8cb09032-84ad-11e5-8095-ed1a37d1e096. [↑](#footnote-ref-31)
32. Kathrin Hille, “High drama as Russia’s Transaero edges towards bankruptcy”, Financial Times, November 8, 2015, accessed July 20, 2017, https://www.ft.com/content/8cb09032-84ad-11e5-8095-ed1a37d1e096. [↑](#footnote-ref-32)
33. Maria Fedorishina, “Not Only Transaero: Why the Largest Air Carriers Go Bankrupt [in Russian],” VC, October 7, 2015, accessed June 23, 2017, https://vc.ru/p/aircrash; and Luis Linares, “25 Years Ago: Pan Am Ceases Operations,” *Airways*, December 2, 2016, accessed June 23, 2017, https://airwaysmag.com/airchive/pan-am-ceases-operations. [↑](#footnote-ref-33)
34. Dean Foust, “How Delta Climbed Out of Bankruptcy,” Bloomberg, May 14, 2009, accessed June 23, 2017, www.bloomberg.com/news/articles/2009-05-14/how-delta-climbed-out-of-bankruptcy; and Maria Fedorishina, “Not Only Transaero: Why the Largest Air Carriers Go Bankrupt [in Russian],” VC, October 7, 2015, accessed June 23, 2017, https://vc.ru/p/aircrash. [↑](#footnote-ref-34)
35. Maria Fedorishina, “Not Only Transaero: Why the Largest Air Carriers Go Bankrupt [in Russian],” VC, October 7, 2015, accessed June 23, 2017, https://vc.ru/p/aircrash. [↑](#footnote-ref-35)
36. CHF = Swiss franc; CHF1 = US$0.61 on March 31, 2001. [↑](#footnote-ref-36)
37. Tommaso Ebhardt, Chiara Albanese, and Deena Kamel, “Alitalia Starts Bankruptcy Process as Etihad Cuts Off Funds,” Bloomberg, May 2, 2017, accessed June 23, 2017, www.bloomberg.com /news/articles/2017-05-02/alitalia-starts-bankruptcy-proceedings-after-turnaround-fails; and Maria Fedorishina, “Not Only Transaero: Why the Largest Air Carriers Go Bankrupt [in Russian],” VC, October 7, 2015, accessed June 23, 2017, https://vc.ru/p/aircrash. [↑](#footnote-ref-37)
38. € = EUR = Euro; €1 = US$1.55 on March 31, 2008. [↑](#footnote-ref-38)
39. RSM is a powerful network of audit, tax and consulting experts with offices all over the world. RSM RUS is a full member of RSM in Russia. Historically, RSM was derived from the initials of three of the original founding member firms of the organization: Robson Rhodes, Salustro Reydel, and McGladrey. [↑](#footnote-ref-39)