**LATAM Airlines and COVID-19**

a.) What is Latam's strategy? What is Latam doing well?

* LATAM’s strategy is to maximize the use of the cargo holds on passenger planes and complement its offer with its freighter planes. LATAM was the largest freighter airline with 145 destinations in 26 countries. LATAM also offered flights to exotic destinations, with unique connections. (pg. 4)
* One initiative that LATAM executed well, which significantly helped the company, was its deep restructuring process in 2016. The restructuring reduced operational costs and improved efficiencies by utilizing significant employee layoffs, deep cuts to top executive positions and optimization of fleet size. It was at this point that Akbar Al Baker, CEO of Qatar Airlines decided to invest in LATAM to develop a long-term relationship. (pg. 3).

b.) How did Latam get into this situation? Is their distress primarily the result of poor operating decisions, poor financial decisions, or bad luck?

* In 2019, the growth potential for aviation in the region was expected to be high. LATAM chose to bet on this growth and increased their leverage, which placed the company in a financially vulnerable position entering the pandemic.
  + LATAM had $10.4 billion in financial debt, which amounted to a debt-to-asset ratio of 85% (compared to Delta at 76% and Southwest at 62%). (pg 4).
* This distress was a result of all three: operating decisions, poor financial decisions and bad luck:
  + *Operating Decisions:* In 2012, the merger between Lan and Tam did not go as smoothly as anticipated. The expected $200 million in synergies did not materialize and the companies experienced difficulties in coming together. (pg. 3)
  + *Poor Financial Decisions:* LATAM was already significantly levered going into the pandemic and did not have much cushion for any kind of unforeseen event. (pg. 4).
  + *Bad Luck:* There was no way for LATAM to predict the COVID-19 pandemic and a -96.7% year over year drop in passengers. (Exhibit 12) In 2012 and 2013, the Brazilian currency was sharply devalued and international oil prices increased substantially, greatly impacting the operating expense. Thes macroeconomic factors are out of LATAM’s control. (pg. 3)

c.) How levered is Latam? Does this amount of leverage make sense for them? Why or why not?

* LATAM has a debt-to-asset ratio of 85%. (Exhibit 7)
* This amount of leverage makes sense as the airline industry is highly competitive and airlines need large amounts of cash to lease aircrafts.
* This amount of leverage does not make sense as LATAM should have been more prepared and financially stable. The airline industry is known to be volatile, for example, Delta and American Airline, two of the largest American airlines, went through Chapter 11 during 2005-2007, and 2011-2013, respectively. (pg. 7)

d.) How serious is the situation? Why?

* This situation is very serious and will not only impact LATAM, but may also have a significant impact on the airline industry, investors, and the entire country of Chile. A study by Oxford Economics showed that LATAM contributed $6.2 billion in 2019 to Child’s GDP through its operations (2.5% of GDP), generated a total of $600 million in tax revenue, and contributed $2.5 billion to national labor income. (pg. 9).

e.) What are Latam's alternatives for raising external capital, and what are the advantages and disadvantages of these alternatives?

* Debt, Equity, Private Equity???
* LATAM already has a pretty complicated ownership structure, so issuing more equity would cause dilution. (Exhibit 2)
* Other considerations: US vs Chile vs other countries
  + Value of different currencies? Inflation? Interest Rates?
* Chilean government funding challenges: social unrest, the President of Chile, Sebastian Pinera, used to own 20% equity stake in the company, so it appears as a ‘Conflict of Interest,’ and typically governments usually require companies to maintain jobs in exchange for fiscal assistance, but LATAM has already announced massive layoff. (pg. 9)

| Tranches DIP | Interest | Conditions |
| --- | --- | --- |
| Tranche A | Interest 12-14% | Payment preference over tranche C |
| Tranche B | Reserved for government aid | To be defined |
| Tranche C | Interest 14.5% | Interest paid at the end of the process, and option to convert shares into equity |

f.) How should Latam raise the needed funding?

g.) Will Latam be able to reorganize in such a way to survive the pandemic and emerge from Chapter 11? If so, what do they need to do?

* Even if LATAM secures the additional funding and continues on financially, it must learn to adapt to a different way of flying post-COVID. The world and airline industry is rapidly changing and LATAM must develop a deeper sense of trust with customers if they want to be successful in the future.