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IFC

International
Finance Corporation

MIGA

Multilateral Investment
Guarantee Agency

PUBLIC-PRIVATE PARTNERSHIPS BRIEFS

Kenya: Kenya Airways Privatization



Overview

In 1995, IFC successfully advised the Government of Kenya on the privatization of Kenya Airways. After selling 26 percent of the airline to a strategic partner, the frequency of the airline's flights grew by 61 percent in six years, developing Nairobi into a regional hub. The sale was completed in December 1995 and the public offering in April 1996. The airline has been profitable ever since.

A strong alliance partner, KLM Royal Dutch Airlines, purchased 26 percent of the equity and the Kenyan Treasury received over \$70 million from the sale. Over 113,000 Kenyans were able to buy 22 percent of the shares in the airline (the vast majority bought the equivalent of about \$200 worth). Kenyan financial institutions bought 12 percent, international financial investors 14 percent, and employees of the airline acquired 3 percent. As the public offering was over-subscribed, IFC devised an allocation policy that favored smaller investors and airline employees. The sequencing of getting the strategic investor on board first was crucial to building public confidence in the transaction and the future of the airline.

Despite the current financial and economic turmoil, Kenya Airways maintained its profitability during the six months that ended on September 30, 2008. In 2008, Travel News & Lifestyle Magazine voted Kenya Airways as the African Airline of Choice, and in 2006 Kenya Airways won the prestigious African Aviation Award awarded by African Aviation Magazine.

This series showcases how the World Bank Group supports the development and implementation of public-private partnerships. This support comes in the form of public sector loans, private sector finance, sector and transaction advice, guarantees, and output-based aid.

Background

Kenya Airways was incorporated in 1977 as the country's national flag carrier and was fully owned by the Government. Over the next 15 years, the airline accumulated massive financial losses, along with crippling debt arrears from its failure to service its loans. The basis for a nationwide privatization program was laid out in 1992, and Kenya Airways was one of the 45 companies to be privatized in the first stage of the process. Concurrently, a new board of directors was appointed and a high caliber management team was recruited. Under its leadership the company underwent a process of restructuring and commercialization: routes, fares and fleets were rationalized, management was overhauled and the entire staff was put through training.

The next step was to help bring about private ownership of Kenya Airways. The Government's main objectives were to ensure the continued operation of Kenya Airways as the country's national airline, to transfer the bulk of ownership of the airline to the private sector, and to allow the airline to build on its improved operating performance and profitability with support from the private sector.

Project Description

To secure an alliance with an international airline, the Government and IFC agreed that an equity partnership was the best option, which resulted in a multitranche privatization, starting with the sale of a minority stake to a strategic partner followed by a public offering. As a result:

- The Government sold 26 percent of the company to KLM and offered the remaining 51 percent to the public (non-Kenyans were limited to a maximum of 49 percent of the total equity).
- Kenya Airways and KLM signed a cooperation agreement whereby they agreed to pool their strengths and achieve economies of scale by sharing resources, combining route networks, and assessing new markets in Sub-Saharan Africa.

IFC approached a total of 154 airlines, resulting in 4 major international airlines showing serious interest: British Airways, KLM, Lufthansa, and South African Airways, but only KLM and South African Airways submitted business plans and financial offers. The Government awarded the privatization to KLM through a process of sequential negotiations. KLM was chosen because of its record as a

pioneer in the development of airline alliances and in the creation of a global network of cooperative services, its flight connections to Kenya since 1969, and its valuation of the airline at \$100 million as opposed to South African Airways' valuation of \$89 million.

In addition to the joint venture agreements, Kenya Airways and KLM signed a cooperation agreement whereby they agreed to pool their strengths and achieve economies of scale by sharing resources, combining route networks and assessing new markets in Sub-Saharan Africa.

World Bank Group Role

The Government believed that IFC had the requisite combination of technical expertise, political sensitivity, and credibility required for the difficult environment surrounding the privatization. Consequently, in April 1994, it hired IFC to prepare a strategic review and options report and to develop and implement a privatization action plan. IFC's undertakings included the following:

- Conducting a strategic review of the airline's operations and financial condition.
- Producing a detailed action plan to reconcile the Government's objectives and practical constraints with the commercial realities of the industry.
- Identifying the characteristics of potential investors.
- Determining financing needs as well as legal and regulatory requirements.
- Designing an equity structure.
- Evaluating the bids and negotiating with prospective partners.
- Recommending a preferred partner.
- Designing the public offer.

Outcomes

- The success of this joint venture led to the doubling of passenger traffic and cargo between 1995 and 2003 and a boost to tourism. In addition:
- The Government received more than \$70 million from the sales and saw its remaining 23 percent minority stake increase in value.
- The service standards and reliability of Kenya Airways improved dramatically.
- The airline received a \$15million loan from IFC to modernize its fleet.
- The airline has been profitable ever since the transaction closed.

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