

# JESA INVESTMENT & MANAGEMENT CO., LTD.

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## Our Solution to the Alitalia's never-ending crisis

By Saro Capozzoli, Antonio De Castro – Jesa

Since 2010, Alitalia is going bankruptcy for the third time. The first collapse happened in 2008, after the block of a sales plan; the second one, in 2014, when the company was again on the verge of bankruptcy and the Italian government had helped negotiate an agreement with Etihad, the great Middle Eastern carrier, which accounted for 49% of the shares. Anyway, this did not give Ethiad the right to impose its strategy and rules. The project to bring Alitalia into operation by 2017, however, proved to be optimistic. According to Bloomberg, the Italian carrier's market share dropped to 18% in 2015 (from 23% in 2008), and the number of passengers dropped in a decade from 30 to 23 million. In 2016, Alitalia lost around EUR 400 million.



On April 25<sup>th</sup> Alitalia's employees were requested to vote to accept pay cuts and redundancies. As expected, they did not approve the proposal. Now, almost 12 thousand employees are at stake. Even banks refused to finance the company, which was forced to apply for pre-bankruptcy procedures. The Italian government should again help Alitalia. Options are two: to sell the company; or to sell its goods in order to pay back its debt.

The company's main strategy in the last years focused on Italian and European routes, where it had to not only to face the competition of low cost airlines, such as Ryanair or EasyJet, but also the one of high-speed trains. Trains, indeed, improved its routes over the years. As an example, in the Rome-Milan route, which was very important to Alitalia, customers' prefer to take the high-speed train rather than a flight as it is fast, cheaper, and connected right to the city center.

Moreover, as shown by McKinsey's research, the short flights represent the less profitable segment in the industry. Since Alitalia it is not a low-cost airline, it has to maintain "costly standards". For example, landing in principal airports reduces profits made by the company.

Despite Alitalia offers a few intercontinental flights, the main focus remains the U.S.A. (where the company has to compete with Emirates). Alitalia offers weekly flights to New York, Miami, and Boston and seasonal flights to Chicago, and Los Angeles. Even if connections to the U.S.A. are quite developed, Alitalia offers only four weekly flights from Italy to China. All of them connect Rome to Beijing, while China

Eastern and Air China supply the rest, connecting Rome and Milan to Shanghai.

Wouldn't have been a great opportunity to boost flights from/to China?

Chinese middle class reached 200 million people and, according to Eurostat, Italy has been elected the favorite European destination for Chinese tourists in 2015. Alitalia should have provided people with connections not only to Shanghai and Beijing, but also with "smaller" cities, such as Chengdu, Chongqing, Guangzhou, Nanjing, and Xiamen.

Moreover, Chinese people could have benefited from Italy's strategic position that is considered an ideal hub for Chinese relations with Africa. Italy is deemed as a "safe country" close to the African continent. Also, Italy is an ideal point to fly to North and South America.

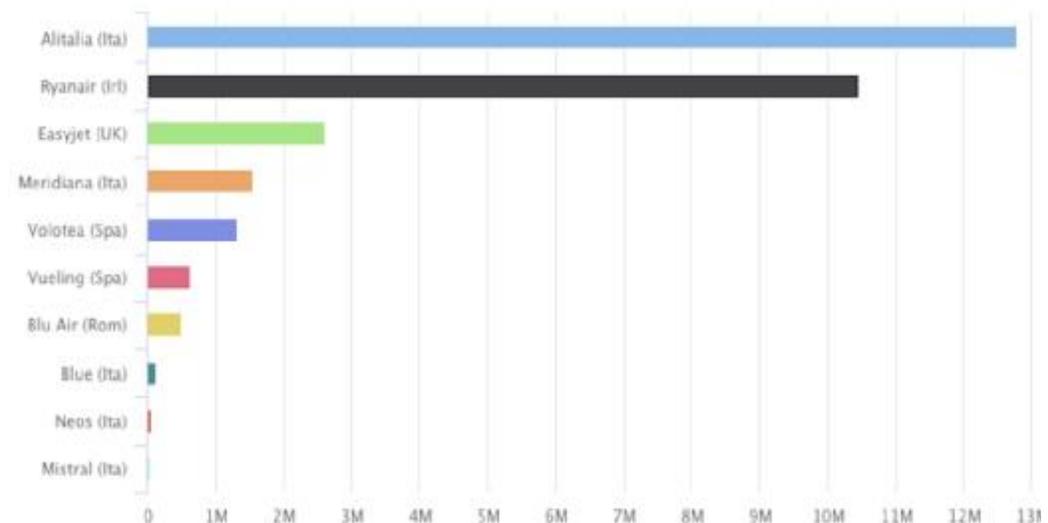
Furthermore, it is possible to highlight that Alitalia concentrated its flight in Milano Malpensa and Rome Fiumicino airports. The company might have overvalued these airports location. For instance, Veneto region's (located in the East part of Italy) passengers won't choose to travel from Milano Malpensa as it is far away and badly connected with the highway. Until important hubs like Malpensa and Linate will not be easily reachable from the Eastern part of Italy they won't be the customers' first choice. In this case, Verona and Venice airports offer good and fast connections through Frankfurt, Munich, Amsterdam and Vienna to the rest of the world. Alitalia might have lost a slice of customers just for bad decisions in terms of airports.

Currently, the hope is to find another company that can "save" Alitalia.

But, should a company invest in Alitalia?

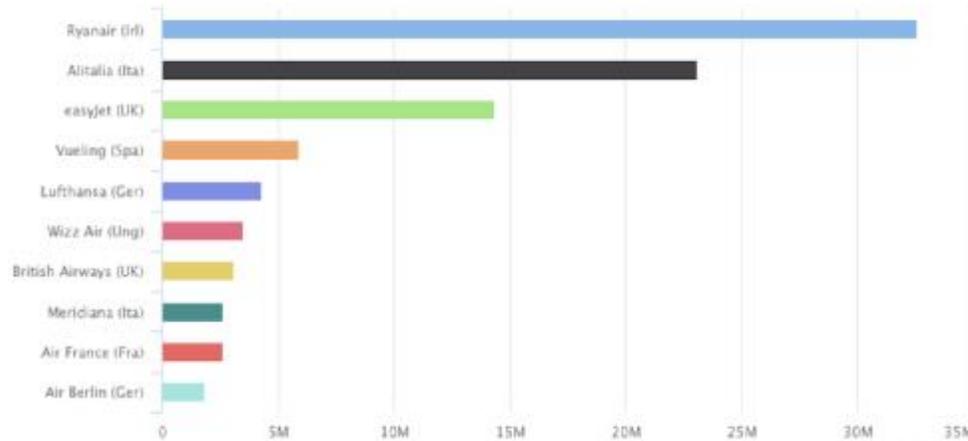
In Italy, many customers prefer to buy an Alitalia flight rather than a low-cost one, as it has several agreements with companies and institutions. Moreover, the flag company is one of the few companies that connect small Italian airports with Milano Linate, which is the closest airport to the center of Milan. Nevertheless, Alitalia flights are the most expensive throughout Europe and the biggest market share in the Italian market is held by Ryanair.

Top 10 airlines in Italy for passengers transported within the country in 2016



Source: ENAC data, made by FON

Top 10 airlines in Italy for passengers transported in 2016



Source: ENAC data, made by FON

our analysis we can see it would be worth it to make a strategic alliance between Ryanair and Alitalia. The latter can specialize in long routes, such as to the U.S.A. and Asia, while the former could manage the national and European ones. The aim, anyway, should be to keep a focus on Africa e Asia as they might become the biggest markets in the world in a few years. For the record, Ryanair and Norwegian Airline are already discussing to create a low-cost route from Europe to the U.S.A. and Canada at just 198EUR (apparently) for the round trip. This is the tendency aircraft should follow: to merge or to die.

We strongly believe that a way for making profits again could be to open to new intercontinental routes. To do so, Alitalia should change its fleet, which can currently count mostly on small planes. This will be for sure a very expensive investment for the potential buyer, but it could open new markets. As the "strategic" changes made by the management team over the last years were unsuccessful, Alitalia has not been able to benefit from diverse opportunities.

Alitalia main drivers are political and social goals, which in a way reflect the Italian way of doing business at the public level. This could not fit an industry open to the global market.

We think that it will be hard to find a new potential buyer for Alitalia, but whether it happens we believe that it is necessary to completely change the strategy to make it profitable and competitive. Thanks to

## Europe it's Hopefully Safe

By Saro Capozzoli, Tristan Gonnord - Jesa

In recent years, Europe has had a lot of internal troubles. From the debt crisis to the migrant's one, the EU came to a breaking point with France President's election.

Fortunately, Mr. Macron, from the centrist party, was elected president. He will promote European oriented ideas contrarily to Marine Le Pen whose election would have blown up the European Union. Mr. Macron is a convinced pro-Europe politician: the visit in Germany in his first day of presidency can remind us that one of France's goals will be to reinforce Europe. The new French President outlined a few points that he wants to reform. The first one was about creating joint European military structures. Then, he also insisted on the fact that Europe has to be strong against Brexit in order to show that there are more advantages to be in the EU rather than to leave it. Also, to allow for fairer economic competition between companies that want to work in other countries, Macron proposes to harmonize tax policies in 19 countries. The main proposition is to create a shared budget for all the countries using the euro currency that would be managed by a newly created joint finance minister for the Eurozone. The new euro-zone finance minister would also oversee this, which Macron calls an effort to fight "social dumping," when companies move work or workers to countries with lower taxes. Macron says such a budget would allow for joint investments, provide emergency financial help, and help the euro-zone better react to a financial crisis.



These propositions are all aimed at strengthen cooperation among the EU members, that's why Mr. Macron can be seen as a symbol of the new orientation that EU wants to follow in order to become strong again.

Even more importantly, the election of a pro-European president in France carries a message of great hope. Now that the protectionist spectrum seems to be moved away, it's time to show that all the EU countries are able to work together to improve their model and remain powerful in today's globalized world. A united Europe means strong economic relations. Countries can bond to be seen as a unique front by the rest of the world, to be ready when facing international competition, and to improve local economic conditions.

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