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Dynamics of governance and ethics (Swissair – Airline Sector)

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ABSTRACT

Students were to research on a particular industry sector, study their governance and point out the good, bad and ugly practices of their governance. Here, in this report, I have selected Swissair airline sector for my study. Swissair, considering their dramatic fall (it used to be one of the best airlines and nation's pride that apparently got market failure, gone under debt in 2002 and the government had to bail it out) was a very good choice for this report. The structure of this report is very simple since the scope was just to point out governance and ethics practices of this company. In my report, I have given a little background information about the company that is followed by the bad governance and ethics practices in Swissair. These bad points are followed by the ugly practices. Now when Swissair saw itself failing they started taking steps that included some governance and ethical changes as well. I have tried to include them in the good points. Overall, my report is a short paper describing governance in Swissair, where I have tried my best to include all major and critically important points.

Introduction

Introduction / Background

Swissair was started in 1931 by the merger of two main Swiss airlines and it was in the market till 2002. In its total span of market presence - total 71years - it has been the national airline. Swissair was ''renowned as a flying bank and it came to be regarded as a Switzerland's national symbol'' (Steger and Krapf, 2002) due to its strong financial position.

In the 2002 the economical and political changes in Europe started affecting Swissair and causing its downfall. Swissair also tried to integrate into these changes (Steger and Krapf 2002).

Swissair, was considered as a source of national pride, and it had a great deal of government control (owning 30 percent of the stock) over certain aspects of the decision making process (Steger and Krapf, 2002).

Two companies' merger formed Swissair with 13 aircraft, 64 employees that had flights from Zurich to four domestic and 14 European destinations. In its later time (By early 2001) it had 72,000 employees worldwide with 21,000 local employees. That time Swissair had 75 aircraft that served 210 destinations in 75 countries.

Swissair was formed by a merger between two local carriers. The new company had 13 aircraft, 64 employees, and flew from Zurich to 4 domestic and 14 European destinations. By early 2001 Swissair Group had 72,000 employees worldwide including 21,000 working in Switzerland. It had 75 aircraft, and served 210 destinations in 75 countries. In 1997, the Swissair Group was renamed SAirGroup, with four Subdivisions SAirlines (to which Swissair and Crossair belonged), SAirServices, SAirLogistics and SAirRelations.(Source : wikipedia)

The Bad

- In 1990s, Airline industry as a whole was experiencing changes. Airlines started alliances/partnership/joint venture relationships to expand routes for firms and to insure its passengers' easy access to destinations (Domke-Damonte, 2000).
- With this changing time, Swissair, instead of partnering or making alliance with other airlines choose a strategy of acquisition in order to growth. This strategy was called as "Hunter Strategy". This strategy was mainly a result of government influence in decision making. (Steger and Krapf 2002).
- Swissair's decision to acquire airlines instead of partnering with them was taken under political pressure as it was considered national pride. Social and political pressures on decision making didnot consider and acknowledge the changes in economy in the airline sector itself or European Union at that time. This led managers to make poor decisions and managers also were mostly political appointees with little or no experience in airline industry which made decision making process even worst (Teahan, 2002).
- For example, while making decision, Swissair CEO at the time, Philippe Bruggisser, emphasized a strategy of acquisition of (rather than partnership) stakes in different airlines; and outsiders questioned this decision. But even though the members thought CEO is playing power game, board was unable to stop this (Steger and Krapf 2002).
- Swissair's board membership, instead of reflecting competence and experience, reflected political affiliation due to the dominance of political norms in Swiss business

In a study done in the 1980s, the conclusion data shows that Switzerland was run by elite of 300 people from industry, banks, and trade associations (Steger and Krapf (2002).

- And, these members are selected mostly by their friends who were already in. In addition, Swiss law required the majority of board members to be Swiss nationals or residents.
- Labor unions and the companies' management often have a cooperative relationship in Switzerland. This is not the case in

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many other European countries. European airlines are not able to quickly cut labor costs in response to a downturn, as e.g. US companies can do. Swissair executives had little experience dealing with European unions.

- In Switzerland, management of companies and labor unions often have a cooperative relationship which is not normally the scenario of European countries. Also European unions does not let airlines to cut labor cost quickly as suppose to American airlines does. Their little experience of dealing with European unions made Swissair executives job more difficult.

The Ugly

- To make the situation worst, corporate governance of Swissair was divided as per Swiss law in which dad to day operations were done by executive management and board with the members of powerful political persons had ultimate responsibility for leading the company (Steger and Krapf 2002).
- In Swissair governance, 30 percent government ownership decided the CEO and also provided the CEO with instructions on conducting the business of congruent with the political agenda of the Swiss government and people. As a result of the compliance with political and social norms, economic norms and ethical norms were ignored, and thus, the corporation failed. (Nwabueze and Mileski)
- In Swissair one of the stakeholders – the government - dominated decision making and that was done completely based on national pride. This made the government regulation role get confused with the board of director oversight role. This created a conflict in the corporate governance since the out come of government regulation was that the board and management were not independent of each other.
- If Swissair was having an independent structure the board would have been able to check and balance structure for management.
- Since, Swiss law required the majority of board members to be Swiss nationals or residents, directors end up having so many positions at a time. Also, due to the split in corporate governance structure required under Swiss law, the board and management behaved as if there were a split in responsibility further ‘‘muddied’’ by the difference between the business operations at Swissair and the clear functioning of the Swiss government.(Nwabueze and Mileski)
- At Swissair Philippe Bruggisser, - a COO that was promoted as CEO – did not effectively communicate to the government, board of directors and the public the risk of their acquisition policy instead of partnering. This led company a debt which was unpaid until the government bailed it out (Steger and Krapf, 2002).
- In addition to that individual level, there was also a corporate level example of governance system failure at Swissair. The main auditors PricewaterhouseCoopers lacked the accuracy in the auditing of Swissair’s finances by led to four years of identical accounting statements which never reported the risk associated with the different holdings (Steger and Krapf, 2002). The auditors (PricewaterhouseCoopers) continued to issue and certify the same opinion for four consecutive years without any questions from the board of directors of the company. The political norm of Swissair as a national airline representing the pride of Swiss people, pressured auditors to fail to use due care in auditing financial statements. Further, the lack of questioning from the board confirmed that politics outweighed any other consideration.
- Swiss had the same issue and certification from auditors (PricewaterhouseCoopers) for four consecutive years. This was happened without asking a single question to the board of directors because of political power. Also, since Swissair was considered as a national airline representing the pride of Swiss people, auditors were pressured to fail to use due care in auditing financial statements.

The Good

- Swissair tried to improve the governance by taking several steps. Some of them are as below
- In February 2001, management took serious steps to save Swissair. They cancelled several follow-up investments and other investment decisions. It also included 34% stake in TAP Air Portugal, and 51% of Turkish Airlines that they plannedpreviously.
- New Chief Executive Officer was appointed in march 2001 for Swissair. Mario Corti, the new Chief Executive Office was also the chairman of Swissair’s parent company SAirGroup. Corti had lot of public support and trust. People believed in him that he could save Swissair. He was as popular as he started being called as “Super Mario” and a general belief existed that the company would again become profitable within 3-5 years.
- Swissair started cost cutting measures according to which they sold their hotel chain Swissôtel to Raffles Hotel Group for SFr520 million. The cost cutting measures also initiated the internal corporate magazine named “Voice” that encouraged cost saving measures by employees. Swissair pilots also contributed in cost cutting approaches by accepting a 5% pay cut for 2 years.
- The new Chief Executive Officer Mario Corti started taking serious actions. In this the first step was to announce a major restructuring plan on September 24. According to which Swissair and Crossair would merge, and would create a new firm called Swiss Air Lines, but they would at the same time maintain each airline's individual brand. This consolidation has an impact of 10,000 jobs lost, including 3000 at Swissair's catering company, Gate Gourmet.
- Although Mario Corti was having so many difficulties and was having a very tough job he did show some progress in 2001 during summer and spring for cost cutting. When a popular belief was that Mario Corti should have drop the airline business concentrating on their big business of catering, airport-retail and baggage handling operations. While it could have been a cost effective and profitable step, the cut out airline would most likely reduce Zurich’s traffic for larger European airports. This could be very shocking incident for Swiss people and their pride. Also there was a possibility for Switzerland to lose their position as an attractive business and tourism location without high quality air service.

Conclusion

- The high fuel prices in 2000, slow US economy during the same time and then USA attack September 11, 2001 these are the factors that affected mostly all airlines but Swissair was affected by its own governance more than it was affected by these factors One of the greatest failures of Swissair governance was its Hunter Strategy. SAirGroup invested heavily in second-tier, unprofitable companies, many of whom were in serious trouble, with big debt, low revenue and large losses. In many cases acquisitions were overpriced. (Vardan Seven)
- Greater political influence on company governance was the major factor for Swissair’s failure.

- Swissair's strategy, management and corporate governance were fundamentally weak. This leaded bad decisions of shareholders, insufficient openness that resulted in a failure

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