



# From IPO to T/O

2006

The story of Jazeera Airways, the airline that broke Middle East governments' monopoly of the aviation industry by being the first private airline in the region.

**Wings of Freedom**

A National Carrier of Kuwait.

**jazeera AIRWAYS**  
طيران الجزيرة



From IPO to T/O

**Introduction by Marwan Boodaj** ..... 1

**Before Jazeera Airways** ..... 2

    Government controlled industry ..... 2

    Kuwait spearheads the change ..... 3

**The conception of Jazeera Airways and the challenges that came with it** ... 3

    Convincing investors and bankers: Jazeera Airways will succeed! ..... 3

    Convincing the market: low cost does not mean low quality ..... 5

    Convincing travelers: book directly, its easier and cheaper ..... 6

    Convincing governments: Jazeera Airways is a partner ..... 6

**From IPO to T/O** ..... 8





From IPO to T/O  
P.1

## Introduction by Marwan Boodai

Jazeera Airways first came to life on June 12, 2004 with the completion of its Initial Public Offering (IPO). A little over a year later, we took flight with a brand new fleet of Airbus A320s, effectively launching Jazeera Airways as the first private airline in the Middle East.

A total of 15 months have elapsed from IPO to take-off (T/O). During this period we have faced one existential threat after another... from convincing investors and financial institutions that a private airline will succeed in the Middle East, to convincing governments that Jazeera Airways' low-cost business model can help them grow their primary and secondary travel industries. This document takes a close look into the challenges Jazeera Airways faced, and how our team overcame them. Today, one of every 25 Kuwaitis is a shareholder in Jazeera Airways.

Ultimately, the objective of this case study is to provide the observer, the analyst, and the industry professional with insight into airline and the challenges it faced. Having said that, this document is not about other airlines, it is about Jazeera Airways, Kuwait and the history we made together. It is about the freedom we brought to our travelers by empowering them and making them more independent through cutting-edge technology and low fares.

Sincerely,

Marwan Boodai,  
Chairman and CEO  
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## Before Jazeera Airways

Jazeera Airways Kuwait Shareholding Company (K.S.C) first came to life on June 12, 2004 with the completion of its Initial Public Offering (IPO). In November of 2004, less than a year later, it received the Air Operator's Certificate (AOC). On October 24, 2005, with USD 34 million in capital and a highly motivated team, the airline took delivery of a brand new Airbus A320 fitted with 165 leather seats. It was the first of a 10-aircraft order of the same type from Airbus. Six days later, Jazeera Airways took to the skies on its first commercial flight to Dubai. Fifteen months have passed from IPO to T/O (take-off) and despite the heavy skepticism, the industry has been keeping a close eye on Jazeera Airways ever since.

"Jazeera Airways set to shake-up Kuwait status quo" was how the European Editor of Air Transport World, Cathy Buyck, referred to the launch of Jazeera Airways. Over the past 10 months Jazeera Airways has not only challenged the status quo in Kuwait but also raised the bar in regards to on-time performance and operational efficiency, and shook-up the aviation sector with its low-fares. But launching a private airline in the Middle East, the only

remaining region in the world that still has a government owned and controlled aviation industry, was not an easy task.

Jazeera Airways faced challenges that ranged from raising capital, securing traffic rights, offsetting negative perceptions of the low-cost business model, to convincing regional authorities that Jazeera Airways was a friend, not a foe. This case study looks at the environment Jazeera Airways was born into and the obstacles it overcame in its first ten months of operations.

## Government controlled industry

Registering an average traffic growth of 10.7% per year from 1995 to 2004, the Middle East has captured the attention of the global aviation industry with its potential<sup>1</sup>. The industry itself, however, is a lot older than that. Airlines in the Middle East have been operating for 60 years in countries like Egypt, Kuwait, Saudi Arabia and Lebanon. Yet, regardless of its history, the progress of the Middle East aviation industry did not grow the same way it did in Europe and America. Rather, it grew in the opposite direction, towards government control!

Beginning in the late 70s and

**"The [Middle East] aviation system remains heavily regulated by government airport and airline ownership, restricted traffic rights, selected traffic right allocation, and price restrictions."**

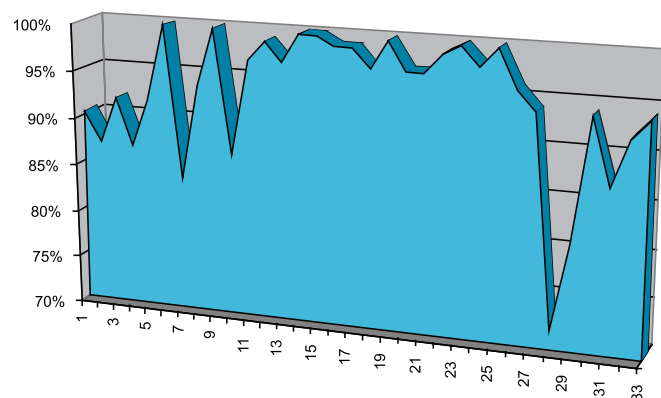
-Booz Allen

Source: *Mastering the Challenges of the Middle East Aviation System*

followed up in the 80s and 90s, the U.S, European, and Asian civil aviation authorities moved to deregulate the sector and pursue free market policies based on ethical competition, transparent financial reporting, and open markets. At the same time, Middle Eastern governments continued to reinforce their grip on the industry. This created an environment that is "heavily regulated by government airport and airline ownership, restricted traffic rights, selected traffic right allocation, and price restrictions" as described in a report by Booz Allen (a global consultancy for business and government) in a 2006 report entitled "Mastering the Challenges of the Middle East Aviation System".

## EXHIBIT A

**Jazeera Airways on-time performance average: 94%**  
Global industry average: 85%



<sup>1</sup> Source: Booz Allen, citing World Tourism Organization. 2006

## Kuwait Growth Key figures:

- Population growth 7.7%
  - GDP growth 19.4%
  - Kuwait stock exchange index growth 106%
  - Air traffic growth 4%
  - Passenger traffic growth 8.8%
- (All figures based on 2005 data vs 2004 data)

## Kuwait spearheads the change

In 2003 the Kuwaiti government began considering freeing-up its hold on Kuwait's aviation sector to help the country cope with the unprecedented growth it was witnessing (see left). The move was part of a greater deregulation plan that was kicked off several years earlier when companies were allowed to enter the public transportation sector and the management of free trade zones and sea ports. This time however, it was considering breaking its own monopoly in the aviation sector, which was trailing behind global industry standards in services and innovation.

In fact, Kuwait travelers were lagging so far behind, that until the launch of Jazeera Airways in late 2005, the only way customers could purchase tickets were in person, either at the travel agent or the airline's office. Furthermore, travelers had to reconfirm their paid ticket 72 hours before their flight or they were guaranteed to lose their paid seat. When they did reconfirm, they still risked being downgraded or worse: losing the seat because of overbooking - a policy pursued to cope with the increase in demand resulting from the country's growth. All these factors combined led Kuwait to move towards deregulation.

**"We are determined to bring in the private sector and giving it priority."**

- H.H the Emir of Kuwait Sheikh Sabah Al Ahmed Al Sabah during the Jazeera Airways launch ceremony on October 29, 2005

## The conception of Jazeera Airways and the challenges that came with it

The historic moment came in late 2003 when the government announced that it will gradually deregulate the transportation sector and offered three licenses (two passenger airlines and one freight airline) to be won. H.H. the Emir of Kuwait, then Prime Minister, Sheikh Sabah Al Sabah's progressive government was the impetus behind the move, realizing that new players were required to not only boost but also enhance Kuwait's transportation sector. Jazeera Airways founders seized the opportunity and presented the authorities with a feasibility study on Jazeera Airways, and how it can help reinvigorate the sector. Eventually Jazeera Airways received the Kuwaiti Cabinet's approval, and on October 30th, 2005, became the Middle East's first private airline.

**Jazeera Airways set to shake-up Kuwait status quo"**

-European Editor of Air Transport World

## Convincing investors and bankers: Jazeera Airways will succeed!

The first challenge faced by Jazeera Airways' startup team was to generate \$34m in capital to commence operations. Interested private equity investors and banks willing to supply debt capital had to be convinced that Jazeera Airways would be a commercial success, before parting with their money. But from the very beginning questions were raised about the likelihood of Jazeera Airways surviving in a government-monopolized industry. After all, the plan was to be the first privately owned airline operating in a region full of government owned airlines... in other words, airlines with open credit lines supplied by their governments.

From IPO to T/O  
P.4

Key to gaining the trust, belief and support of the investment community was to establish a clear vision of the business model that would work in the Middle East market, to gain the support of the Kuwaiti Government, and to recruit an experienced and professional management team that were capable of delivering the business plan over the next five years.

The first group of private equity investors that were convinced by the potential for Jazeera Airways provided \$10m to take a 30% stake in the airline. The other 70% was open to an Initial Public Offering (IPO), as per government law, in June of 2004. The IPO, led by the National Bank of Kuwait acting as both the placement manager and the sole sales agent, was oversubscribed 12 times and generated \$288m. It was by far the most successful IPO in Kuwait's history. Confident in its business plan, the startup team only accepted the \$24m they initially sought, and refunded the rest. The shares were distributed on a pro-rata

basis and thus created a group of shareholders totaling 36,500, or 1 in every 25 Kuwaitis.

The equity raised through the IPO helped the start-up team finance the initial investments in setting up a head office and the commercial and operational systems required to start flying, plus some working capital. It also provided the funding for aircraft deposits. The start-up team then set about raising the \$119m required to purchase the four aircraft required for the first year of operation.

At all times it has been essential to keep purchase, acquisition and financing costs as low as possible. The fixed overhead, including aircraft ownership costs, would ultimately total more than 20% of total costs and it was therefore critical to secure the most cost effective asset base possible to maximize the future return on assets.

The choice of aircraft type was the Airbus A320, which provided

the lowest aircraft purchase cost. In conjunction with its banking partners, Jazeera Airways then worked with financial and legal advisors to secure loan structures that would provide the lowest cost of long-term debt capital.

**"Few people have given Jazeera Airways a chance; it has proven all critics wrong".**

*-Arabian Business, May 2006*

**Structure of the main financing deals**

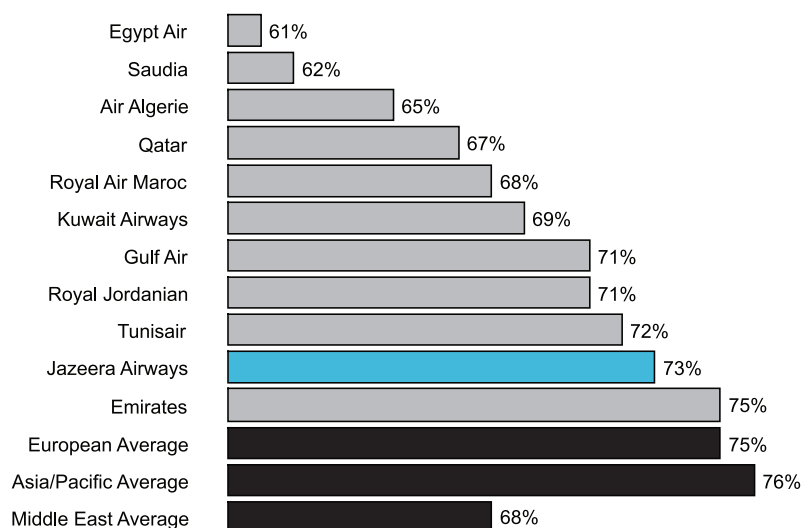
To date, \$181m of long-term debt has been arranged, together with \$40m of pre-delivery payment (PDP) financing for the first six aircraft, all in partnership with leading international banks such as Natexis Banques Populaires (NBP), DVB, National Bank of Kuwait and Kuwait Finance House.

**EXHIBIT B**

**Load Factor (RPK/ASK):  
73%**

Source: Booz Allen (based on Air Traffic Intelligence and Booz Allen analysis) and Jazeera Airways.

Note: Due to lack of continuous reliable statistical information in the Middle East, chart uses 2004 data for all airlines except for Jazeera Airways, which is based on Jan-Aug 2006 data. The purpose of this chart is not to compare airlines' performance, but to put Jazeera Airways' performance in perspective.



With the delivery of the first four aircraft, \$119m of senior debt has been raised and secured on the assets. The PDP commitments to Airbus (totaling approximately \$13m per aircraft) were part financed by loans that were arranged with Kuwait Finance House (KFH) and Natexis Banques Populaires (NBP) on three of the first four aircraft totaling \$22m. All of these loans were forms of Islamic financing in structure, and Jazeera Airways' dogged pursuit of the lowest cost financing solution was rewarded in April 2006 with an Air Finance Journal Annual Award for the "Most innovative deal of the year for 2005".

## Convincing the market: low cost does not mean low quality

Jazeera Airways is built on a business model that works to maximize efficiency in day-to-day operations, enabling it to generate daily cost savings that are relayed to travelers in the form of low fares; otherwise known as the low-cost model. Kuwait did not have much exposure to low cost carriers as other parts of the world did. Jazeera Airways recognized that launching low fares without preparing the market might cause skepticism, and that it will have an adverse effect on its revenue. This posed a challenge for the airline: how to tell the market it was low-cost without a market response of "oh, so low-quality"?

To avoid a long lasting effect on the airline, Jazeera Airways made sure that every media communication, every advertisement, and every marketing initiative communicated that Jazeera Airways had some

## INSIGHT

### The deal that won Air Finance Journal's "Most Innovative deal of the year for 2005"

The Islamic finance structure worked on the principle that no loan takes place but that a real commodity is traded and the bank makes a profit on the transaction as reward for the use of its money. In practice, Jazeera Airways placed orders to buy oil from the vendor (the bank) with full transfer of ownership. At the same time, acting as the airline's agent, the vendor (via a commodity broker) placed an order to sell the oil on the aircraft delivery date. The vendor then forwarded the sale proceeds for the oil to Jazeera Airways in order to meet the pre-delivery commitments to Airbus, who in turn periodically paid the vendor their profit on the transaction. On delivery of the aircraft the (deferred) payment for the oil purchase was settled in full.

or all of the following factual messages to prove that low cost does not mean low quality:

- Jazeera Airways employs well experienced captains with a minimum of 5,000 flying hours that are recruited from leading international airlines
- Jazeera Airways flies a brand new fleet of Airbus A320s powered by brand new engines and fitted with leather seats,
- Jazeera Airways had contracted Lufthansa Technik, a leading global engineering services provider, to service the aircraft engines.

When Jazeera Airways announced it was accepting bookings on Sept 12, 2005 - six weeks before its first flight to Dubai - its fares made first-page headlines and bookings quickly picked up. As expected, questions about how Jazeera

Airways was able to offer low fares also picked up through word of mouth, and eventually reached the airline's head office. The buzz on Jazeera Airways continued to spread and by the second quarter, skepticism subsided as reflected by the numbers (see Exhibit B). In fact, while only operating point-to-point with two aircraft from one hub, Jazeera Airways had sold 55,686 seats by January 1st, and had flown more than 100,000 travelers by March 4, 2006.

## INSIGHT

### How does Jazeera Airways keep operational cost low?

- Continues to build a fleet comprising single-type of aircraft, the Airbus A320
- Outsourced engineering and services of engines to Lufthansa Technik
- Invested in a strong IT base built on Navitaire Reservation and Revenue Management system and Nortel communication platform, enabling it to electronically streamline commercial operations
- Introduced cost efficient sales channels: Internet and Call center
- Offers ticketless travel, saving costs associated with issuing conventional tickets
- Quick turnarounds
- High aircraft utilization: 13 block hours per day
- Continuous sales and marketing initiatives to secure high load factors at lower fares
- Highly skilled and self motivated team
- Strong commitment to lowering cost every day

## Convincing travelers: book directly, its easier and cheaper

During the startup phase, Jazeera Airways knew that it needed to keep seat cost as low as possible to meet its business plan targets, but the savings it planned from having a high aircraft utilization rate, outsourcing engine engineering services to Lufthansa Technik, and other strategies were not enough. The airline had to avoid paying the high travel agent commissions or the overheads caused by having a network of offices if it wanted to meet its business plan projections. The airline had no alternative; it had to drive travelers towards booking

directly without high operational costs. The obvious solution was to invest in both an online booking engine and a call center, and then drive people to book directly. Essentially, whether the airline would be successful or not boiled down to whether it was able to change a 50-year old habit.

When the airline opened for booking on September 12, 2005 it had a running Navitaire-based website<sup>2</sup> and a manned Nortel Systems-based call center. In the following months Jazeera Airways actively marketed both, and employed interactive tactics to deliver their benefits. These tactics included placing internet connected laptops in shopping malls with a host to guide the user, launching special

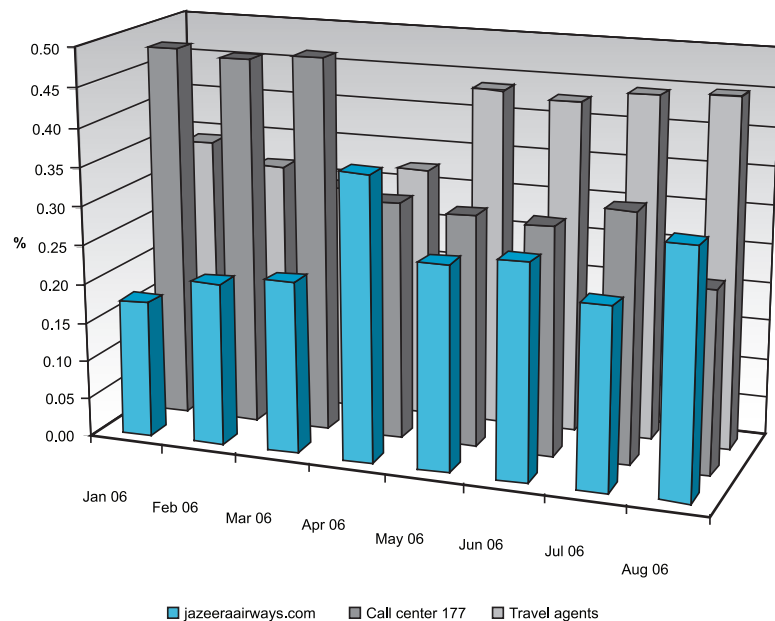
promotions for students on college campuses, and giving talks in college classrooms. Gradually the market began to react and Jazeera Airways was able to convert travelers.

When this case study was written, 62% of all ticket sales<sup>3</sup> were directly booked and paid, either through jazeeraairways.com or the airline's call center 177. In August 2006, (the last available statistic at the time of writing this document) 32% of all ticket sales were made online. The strengths of these numbers prove that traveler habits can change if travelers are presented with a more empowering proposition. In this case, Jazeera Airways has been able to overcome an age-old habit with great success.

### EXHIBIT C

#### Sales Channel Split

Jazeeraairways.com	28%
Call Center 177	34%
Travel Agents	38%



Source: Jazeera Airways

## Convincing governments: Jazeera Airways is a partner

With the exception of Kuwait, which not only allowed but championed the establishment of private airlines in 2003, and later opened its skies in 2006, countries in the Middle East were cautious of a new private and low cost airline. This posed a challenge for Jazeera Airways during

the start-up phase as it had to convince Middle East countries that Jazeera Airways was not a foe, but a friend who was here to help by increasing traffic to their cities through market stimulation. However, without a track record and previous examples, the task was difficult.

<sup>2</sup> Navitaire is a global provider of revenue management systems and online booking engines for airlines. Jazeera Airways is the first airline in the Middle East to use Navitaire.  
<sup>3</sup> This figure covers all bookings made from September 12, 2005 to August 31, 2006.

From IPO to T/O  
P.7

Through continuous visits and persistence by the Jazeera Airways' start-up team, five countries believed in Jazeera Airways' potential and opened up their airports, solely based on faith in the airline and its management team. By October 30th, 2005, the airline was able to secure five key launch routes, namely Dubai, Beirut, Damascus, Bahrain, and Amman. Over the coming months Egypt too became part of history by granting Jazeera Airways rights to three Egyptians cities, namely Alexandria, Luxor and Assiut. India, not a Middle Eastern country of course, also followed suit and granted Jazeera Airways rights to operate to New Delhi, Mumbai and Cochin. So did Iran.

Today all cities have witnessed the positive impact of Jazeera Airways traffic and airport revenue, except for the Indian cities which were newly launched routes at the time of writing this document. Lebanon, which supported Jazeera Airways from the very beginning, is good example of that.

Traffic between Kuwait and Beirut was always healthy, and was even

healthier with Jazeera Airways. Traffic increased to Lebanon's only civilian airport by 33% during the period of January to May of 2006 (compared to the average of January to May traffic between 2003, 2004, and 2005). To be precise, that's 30,726 additional travelers that flew between Kuwait and Beirut on Jazeera Airways during that period.

With success examples like these, it is clear that the industry is

changing to a region led by market factors that ultimately benefit cities and travelers.

**“The recent establishment of low-cost services in regional airports has contributed (remarkably so, in certain cases) to an increase in peripheral accessibility and the boosting of the catalytic effect of airports on their local economies, something that can be vouched for by key sectors such as trade, construction and industry.”**

*Source: Study of The Impact of Low-Cost services in the Regions of the Atlantic Arc presented in the Atlantic Arc Transport Group Meeting / Vitoria, 21 February 2005. The Atlantic Arc covers Portugal, Spain, Western France, U.K., and Ireland*

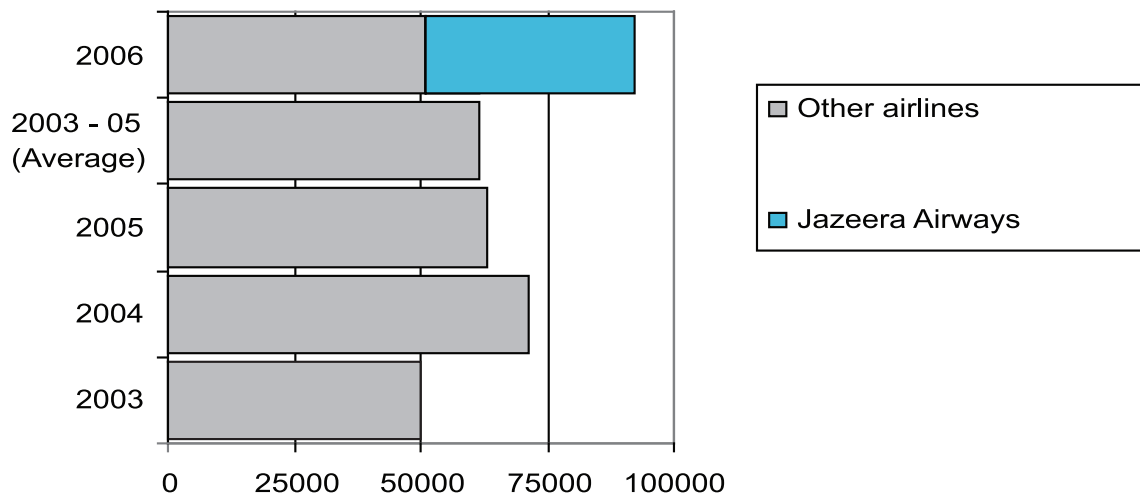
**“It is also important to note that, contrary to common belief, low cost carriers actually grow the entire air passenger market, rather than “cannibalizing” from traditional airlines.”**

*-KPMG*

*Source: Survey report on the Impact of low-cost airlines on Central and Eastern Europe using Hungary as a case study. Survey was conducted by the Travel and Tourism Group of KPMG in Central and Eastern Europe. Published in March 2005*

**EXHIBIT D**

**33% increase in Kuwait – Beirut Traffic**



Source: Beirut Rafic Hariri International Airport

Note: All represented data for all the referenced years is for the months of January to May, for two reasons: 1, Jazeera Airways started on October 30 2005, and has not operated for full year by the time of writing this study and 2, Beirut airport was shutdown on July 13 following the Israeli attack on the city and had not yet resumed operations at the time of writing this document. As a result, the only applicable data for 2006 was from January to May, and in an effort to avoid skewed analysis, this data was compared to the same period of previous years.

## From IPO to T/O

It was a 15 months process from IPO to take off. Few believed Jazeera Airways would come to life, but it did. Few believed Jazeera Airways would be able to attract investors and banks, but it did. Few believed Jazeera Airways would be able to implement its low-cost business model, but it did. Then, few people believed Jazeera Airways would be able change travelers' habits, but again it did.

More than two years have passed since the government's decision to deregulate the market. Since then more Middle Eastern governments have showed interest in both private and semi-private airlines. Following in the foot steps of Kuwait and Jazeera Airways, Saudi Arabia has announced that it will issue private licenses. At the time of writing this story they were accepting bids from investors. This is the future of Middle East aviation, heralded by Jazeera Airways.

### INSIGHT

A look into Jazeera Airways' operations and safety standards

- Brand new fleet of Airbus A320s
- Fleet power by brand new CFM 56-B engines, producing less CO<sub>2</sub> emissions for a better environment with cleaner air
- Fleet engine maintenance by Lufthansa Technik
- Day-to-day operations streamline by a strong IT backbone based on world-leading systems, such as Navitaire, Jeppesen, and Geneva systems
- Organizational structure in compliance with to international recognized standards (JAR OPS standard)
- Team and crew train with well reputed companies, Lufthansa, Airbus Training, Gulf Air and Kuwait Airways



From IPO to T/O  
P.9

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