

Troubled airline faces 'critical year'

Q&A / GERALD GRINSTEIN, CEO OF DELTA AIR LINES

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When Delta Air Lines was pushed into bankruptcy court last September by soaring fuel costs and shrinking cash reserves, it had little left but a plan to get out of trouble, said its chief executive.

"We had consumed all of our assets," Delta CEO Gerald Grinstein said. "All we had to offer was a business plan."

Four months into Delta's Chapter 11 bankruptcy case, Grinstein believes that plan will still lead the ailing airline and local corporate icon back to financial viability.

Grinstein met last week with The Atlanta Journal-Constitution for his first extended interview since Delta filed. He said the company's plan is on track and should start to reverse a tide of red ink later this year. Grinstein thinks Delta can emerge from Chapter 11 by mid-2007, which would make its trip much swifter than that of United Airlines, which has spent more than three years in court.

But he also said Delta's course is far from certain. The company faces a March 1 deadline for a permanent cost-cutting deal with pilots, and jet fuel costs remain above projections. Delta is still working on what Grinstein calls the "most aggressive stretch of all" — a \$1.1 billion bet on retooling its fares and flight network. It faces tough internal issues, including retention of talented managers.

This will be a "critical year" for Delta, Grinstein said. Here is an edited account of the interview:

Q: When do you expect to come out of Chapter 11?

A: My aspiration would be to come out in the spring or summer of '07. Certainly [we] don't want to stay in as long as United. ... We're right on the plan that we laid out ... [but] fuel is now more costly than we projected.

Q: Does your plan have the flexibility to handle the higher fuel costs?

A: Yes, we believe it does. I mean, if it stays at [current levels] through the course of the year, there are going to have to be combinations of things that we would do. Among those is you have to plan on some fare increases.

Q: Since filing, you've reported \$1.3 billion in losses. How soon do the changes you've made start to reverse that?

A: We expect it to be about the third quarter of '06. I would expect us to be better than break even by the fourth quarter. ... The plan does have some points where we're fairly close in terms of liquidity to some of our covenants [financial restrictions in Delta's debtor-in-possession loans]. ... April is a point in time where the projected performance is above, better than covenant, but we don't have the same margin as we otherwise would have. But as long as we're staying on plan, I think we're OK.

Q: Two years ago, you indicated you expected to be CEO three years or less. Has Chapter 11 changed your view? How long do you want to be CEO of this company?

A: [Laughs] I want to stay long enough ... so that I know we're going to achieve what I believe we will achieve, which is the certainty of life, and not mere survival but vitality. Second, I want to make sure that we have the right people succeeding me. I think those two can come together, because this team is now ... reasonably well-seasoned.

Q: Do you feel a responsibility to stay CEO until the company is out of Chapter 11?

A: No. I feel responsible to stay until I know that it's going to emerge and be healthy.

Q: A downside of bankruptcy from management's perspective is a loss of control. How much control have the creditors and debtor-in-possession [DIP] lenders had in setting your course?

A: As long as we report to the [DIP lenders] regularly and as long as we are on plan, there is no problem. ... In terms of the creditors' committee ... everything that we've tried to work through with them ... has all been fine.

Q: Judge Prudence Beatty recently gave up the Delta case to take a medical leave. Are you happy that a new judge, Adlai Hardin, has taken the case?

A: You know I'm not going to answer that question.

Q: How much are all the lawyers, financial advisers and others working on the bankruptcy costing Delta?

A: I bet we're paying in the neighborhood of \$14 million or \$15 million a month.

Q: Continental Airlines CEO Larry Kellner recently complained about Delta's competitive advantages from bankruptcy. What are those advantages?

A: [Laughs] The advantages of bankruptcy are the same ones that Kellner's company took advantage of. [Continental made two trips through Chapter 11.] They got rid of their pension costs. Scrubbed all of their labor costs down. ... They completely remodeled their fleet and modernized it. They did a very good job, particularly the second time through, of scrubbing out all of the different costs so that they were much lower-cost than any of the other network carriers.

... They were also able, as we are now able, to redirect some of their resources, because they got rid of things that they didn't want.

... We were paying \$65 million a year for MD-11s [aircraft rent] that we weren't using. MD-88s, we were paying \$225,000 a month [per aircraft]. Now we're paying \$75,000 a month. It's a huge change in the cost structure.

Q: You said pilot costs are a big pending issue. Are you still seeking \$325 million in concessions?

A: The number hasn't changed. ... We've been in contact [with the union], but I can't tell you that negotiations have started. Time is running out. The end date for an agreement is March 1.

Q: When will Delta make a decision on whether to terminate the pensions?

A: Well, I don't know whether Delta would ever make a decision on that. If I recall correctly at United, it was the [Pension Benefit Guaranty Corp.] that made the decision to terminate the pension plan.

Q: But do you still hold out hope for any legislative relief from Washington [where Congress is considering measures to allow Delta to stretch out payments into its pension funds and ease the cost of keeping them]?

A: Well I don't want to say that I think Washington is going to be the end all, be all, but I do think I'd like to see what the legislation is. ... We don't have a plan to ask the court to terminate their pension.

Q: Do you think companies have a moral obligation to fulfill their pension obligations and to pay them?

A: Sure, but I want to balance that against the moral obligation that I think companies have to try and preserve as many jobs as they possibly can. ... If what you're looking at is a world where you're canceling their pensions and it's going in my pocket, then it's a pretty clear moral situation. But the contrast is, between trying to preserve, as we are at Delta ... 50,000 careers, and we can't do it if we have to pay those [pension plan contributions]. Then you've got two moral issues right in square conflict with each other.

Q: How has Chapter 11 affected customer service?

A: I think there are two factors. One is, we always wanted to be able to make that investment [to improve service], but we were so thin that we couldn't do as much of it as we wanted. ... The second one is, I think our people want to prove that [the Chapter 11 filing is] ... not because of anything they did, and they're working even harder to prove to passengers that they can do a good job.

Q: How do you plan to maintain employees' spirit long term?

A: I see our job as reassuring people that Delta is going to survive, and that it will only really get a chance to grow and expand the way we think it should if we have superior passenger service. ... And it's got to be part of your ethic going ahead. Delta is ... an echo of the past. We were there and we've lost some of that and now we're trying to recoup something we had, and I think it may be a better situation here. But I will not tell you that I think it's easy.

Q: As Delta is cutting bene – fits, pay, etc., how much are you worried that's driving good employees from the company?

A: We're losing good people. We're losing them at every level of the company. We're losing them at Delta Technology [a subsidiary]. We're losing them in management. We've had 1,200 pilots go out in the last 11 months. We've had trouble attracting people at some of our [jobs] over at Hartsfield/Jackson. This is not everyone's cup of tea, and so we are going to lose a lot of people.

Q: Is it something you guys have figured out how to deal with?

A: No, we have not figured out a way to deal with it. We will deal with it ... in unfortunately a patchwork way, because as somebody said the other day, bankruptcy is a process where everyone has to feel the pain. We're going to push that pain as far as we can, unfortunately. I don't want to wind up like United or American, complaining why \$500 million was given to executives when everyone else is taking a cut. We just can't do that.

Q: Is that a promise? A lot of the times when companies exit from bankruptcy, there usually is some sort of package that has equity, incentives, etc. specifically targeted to the management.

A: No, I'm not making a promise. But the new owners of the company are going to have to face up to whether they want to hold these executives, and what they have to do to hold them.

Q: On another matter, the retiree committee alleges that Delta is raiding a trust that was set up to pay monthly incomes to widows and disabled employees, in order to pay other employee-related expenses. How do you feel about that?

A: Well, when I first heard about it, I went to some people here that I trust and said, 'Tell me, are we right or are we wrong? Did we do something that was inappropriate, or did we act appropriately?' ... Three of them came back to me and said, 'We may not have handled all the paperwork right, but everything we did was appropriate.' My due diligence satisfies me that — while I might have preferred that the paperwork had been done more carefully — that the use of the funds was an appropriate use of the funds.

Q: Why do you think the rumor [about merger discussions with Northwest Airlines] persists?

A: Well, I think it started with the simultaneous filing of Chapter 11 [by Delta and Northwest]. ... We are not in merger discussions with anybody. Our belief is that we are going to aim at an independent, stand-alone airline. If you were going to merge, this would be the time to lay the groundwork for it, because you'd shape your fleet to add somebody else's, and it would be the ideal time to match it. We aren't doing that.

Q: You're making a substantial bet on expanding international service. Some experts say you're late to the party and may face over-capacity, price cuts and eventually competition from discount carriers.

A: Well, [we've] got some protections. One is ... bilateral agreements in certain markets [that prevent competitors from entering]. Secondly, a large source of your traffic is likely to come from European carriers. ... They are all significantly higher-cost ... so I think we have a real edge in that market. Thirdly, there is no question that there are going to be low-cost carriers [trying to fly international routes, but] ... the track record of companies that have tried that has not been all that great.

Q: Do you plan to book a seat on AirTran's new flights to Seattle this summer?
(Grinstein has a home there.)

A: [Laughs heartily] I don't want to be uncomfortable that long.