European Foundation for the Improvement of Living and Working Conditions

EMCC company network

Managing change in EU cross-border mergers and acquisitions

Case example Air France-KLM: Combining strengths for sustainability

european monitoring centre on change

Wyattville Road, Loughlinstown, Dublin 18, Ireland. - Tel: (+353 1) 204 31 00 - Fax: 282 42 09 / 282 64 56
email: postmaster@eurofound.europa.eu - website: www.eurofound.europa.eu

The European Foundation for the Improvement of Living and Working Conditions organised a seminar for its company network on November 29–30, 2007, hosted by Santander at its corporate headquarters in Madrid, Spain. In intensive discussions over the two days, 32 representatives from companies, trade unions, universities, research organisations and the European Commission discussed the management of change in EU cross-border mergers and acquisitions (M&A). The Air France-KLM case was presented by Emmanuel Jahan, the company's director of EU Affairs.

The companies

Air France and KLM were two distinct national carriers before combining in 2004 to create the Air France-KLM group. Air France-KLM currently has an annual turnover of €23 billion, moving 73.5 million passengers per year. It employs 103,000 staff and owns a fleet of 569 aircraft. Passenger transport accounts for 80% of the group's turnover, and it now ranks first in the world for business volume, second in the world for the numbers of passengers carried and second in the world for numbers of international passengers carried.

Air France was formed in 1933 through a merger of four local airlines: Air Orient, Air Union, CIDNA and SGTA Farman. This gave the company its first experience with mergers. The company was enlarged in 1990 when it acquired UTA and Air Inter (subsequently merged by absorption in 1994). By contrast, KLM – the Dutch national carrier – had been completely independent since its foundation in 1919, and had only signed commercial agreements with other carriers. It had no historical experience with mergers or acquisitions.

Background to the merger

The Air France-KLM combination made sense on several levels. Although KLM was struggling financially before the takeover, the two airlines had very complementary networks: out of 106 long-haul destinations, only 36 were common to both networks. The merger therefore gave the new group a much larger pool of destinations that it could offer. KLM customers were offered 90 new destinations, while Air France customers were offered 40. The KLM hub of Amsterdam-Schiphol was a very important asset, both financially and strategically. The merger with KLM gave Air France the opportunity to link Schiphol with its own hub at Paris-Charles de Gaulle 2. In addition to the intrinsic advantages of these two bases, this combination also provided a strategic competitive advantage, by preventing British Airways (BA) from establishing a hub at Amsterdam to complement its London-Heathrow base. Air France-KLM is now in a position to maintain two large, important European hubs, an advantage few other airlines can match.

Air France's previous experiences with mergers and acquisitions greatly informed their attitude and approach when considering the acquisition of KLM. The company's mergers with Air Inter and UTA had not respected the corporate cultures of the acquired airlines and as a result were made more difficult. KLM had experience of a failed partnership with Alitalia, and its managers also wanted to have a productive transition during the merger with Air France, with as little insecurity as possible.

From the outset, Air France chose to take an original approach to their 'acquisition' of KLM, calling it a 'combination' and placing great emphasis on the ideas of cultural respect and complementary benefit. Major efforts were put into ensuring that the process was seen as a friendly 'acquisition by handshake' and not a predatory takeover. Air France felt that straightforward absorption of KLM would create useless conflict and thus set about creating two distinct airlines with a common base and shared core values.

The merger

The 'combination' approach was adopted to avoid merger by absorption and preserve the two national policies and cultures of the airlines.

Great care was taken in establishing the executive committee of the new group. It was recognised that the creation of an executive commitee might be perceived as an attempt to 'impose' the culture of one company upon the other, something both parties wanted to avoid. The integration process was taken one step at a time, with the aim of ensuring mutual trust and infusing cultural respect throughout the combination process. Functions were integrated selectively on the basis of operational efficiency. This meant that some functions, such as HR, which are strongly linked to the corporate cultures of the partner airlines, remained separate.

The combination process began in 2003, but is one of ongoing change and adjustment. Air France committed itself from the outset to ensuring that no staff were made redundant, but did reorganise, re-skill and redeploy its staff throughout both organisations to better facilitate joint working and to create synergies throughout the two groups. Collective agreements with the trade unions and a European works council were set up. As the combination proceeded, output increased by 16% despite negligible staff growth, ensuring that large-scale staff redundancies were unnecessary.

The merging of the two corporate cultures was achieved through a comprehensive programme aimed both at developing mutual awareness between the two corporate cultures and at enabling hands-on knowledge to filter throughout both organisations, while simultaneously extending greater security throughout the group. Some key ingredients of this programme included:

- optimising teamwork, achieved by means of a major intercultural training programme involving 70 two-day seminars attended jointly by mixed Air France and KLM teams; so far 1,000 employees have participated in these events;
- a short-term exchange programme (STEP), achieved through a series of short-term missions varying from one day to a month in length and aimed at developing a greater understanding of the other airline; over 50 employees have participated in these exchanges;
- a longer-term exchange programme, entitled 'Connecting our Talents', in which 18 young managers have transferred to the partner airline; this is facilitating the development of in-depth knowledge and understanding of the partner airlines;
- a training programme for the social partners of the European works council;
- English courses for all staff, to ensure that communication does not become a barrier to the development of further vocational skills or to general advancement within the Air France-KLM group.

Challenges and how they were overcome

From the beginning, the Dutch government expressed fears that Air France would absorb the most profitable KLM routes and simply dismantle the company. Air France's experience with the absorption of Air Inter and UTA had convinced the company that it needed to ensure that the experience of combination remained friendly and full of mutual respect, and that it kept the two companies as distinct, complementary entities. To address this fear, Air France embarked on awareness activities and training seminars, relocated some of its employees to Amsterdam and emphasised the importance of joint working, learning exchange and experimentation within the arrangement.

In addition, Air France and KLM signed a social agreement committing themselves to retaining all core business activities within the group, even those which could be outsourced. This included information and communications technologies, maintenance, training and freight. However, across both airlines, these departments are subject to economies of scale. In certain instances, differences between the companies could not coexist and the practices of one had to replace the other; this was done only when it was logical to do so, with all parties understanding the mutual benefits of the change. For example, KLM had developed in-house information and communications systems based on substantial research and development, while Air France used global information and communications systems. While the KLM system had its advantages, it was not logical or beneficial to continue using the KLM system, so it was replaced with the global system.

In relation to staffing and union relationships, there were some very real differences between the demands and priorities of Air France employees, and those of KLM. For example, in the Netherlands, there has been a strong tradition of part-time working, while in France, part-time working was seen as an unfavourable option by the trade unions when proposed by Air France management. These differences were successfully resolved and the union representatives from both airlines are now on the same track.

Although Air France had committed itself to no collective redundancies among the staff at KLM, it did state that it would restructure, re-skill and reorganise the company and that employees must be prepared to participate in this restructuring. Staff were given assurances that they would remain in employment, but they also had to accept changes and be prepared to re-skill or move within the company as necessary. For example, 50% of staff turnover takes place in crews, so Air France-KLM invested in better crew training; in addition, the company also re-trained potentially redundant employees from other departments to join this sector. The security that this gave to employees allowed for greater staff retention and the development of positive relationships with those involved in the change process who might otherwise have felt very insecure.

Finally, Air France-KLM developed three-year strategic plans for their airlines with clearly defined commitments to ensure that future profitable growth be accompanied by social progress. The group also commissioned an external quarterly survey called the *Internal Perception Monitor* to measure employee satisfaction and to monitor how perceptions and understandings of the company are evolving. This helps it to understand how the process has unfolded over time as well as plan for the future.

Outcomes and lessons learned

Air France and KLM characterise themselves as two airlines with operational autonomy but a common executive committee management, which directs the development and reorganisation of the new joint enterprise. It is a group that has chosen a unique route in its acquisition strategy – focused not on absorption but on values of mutual respect for differences and diverse context-specific solutions together with a common operational core. The group characterises its ‘combination’ as an ongoing process centred on mutual understanding, operational autonomy and cooperative benefit. Company representatives emphasise the critical importance of mutual cultural understanding to this process, pointing to the learning experiences that resulted from direct first-hand encounters between the French and Dutch employees. These range from the apparently trivial, such as the discovery that Dutch workers prefer to drink milk with a sandwich at lunchtime, while their French counterparts expect to sit down to a full meal in a restaurant, to much deeper aspects of management practice.

All parties remain convinced that this ‘combination’ has been a success, bringing into being one of the largest and most successful airline groups currently operating, and enabling Air France-KLM to use this combination as a tool to grow in the future in a range of different airline markets.

A motivating factor in Air France's unique approach in this case was the fact that the costs of a true merger could not be economically justified. The company sought to create a situation where the mutual benefit of the two complementary networks could be capitalised upon without accruing additional unnecessary costs by trying to integrate and homogenise all operational aspects. The aim was simply to find the optimal combination of the two airlines, since undertaking a merger for the sake of a merger was not logical. By developing a culture of commitment to compromise, Air France and KLM ensured that their combination was as mutually beneficial to both companies as possible.

Ursula Huws and **Brie O' Keefe**, Analytica Social and Economic Research Ltd

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