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Flying Through a Storm

Buffeted by an ailing economy and a major shareholder, Aer Lingus's CEO says constant change is key to survival

By DAN MICHAELS

Nobody can accuse Christoph Mueller of shying away from a challenge.

A decade ago, the German airline executive stepped in to run Belgium's ailing national airline, Sabena. His scramble to save it was cut short by the terrorist attacks of Sept. 11, 2001, which drove Sabena into liquidation.

Mr. Mueller, who had cut his teeth at German aviation powerhouse Deutsche Lufthansa AG, then moved to corners of the industry the many executives from big-name carriers scorn: the cost-focused air-cargo business and hyper-competitive charter operations. But Mr. Mueller, 48, says he chalked up valuable experience that prepared him for his current challenge: turning round Ireland's struggling national carrier, Aer Lingus Group PLC.

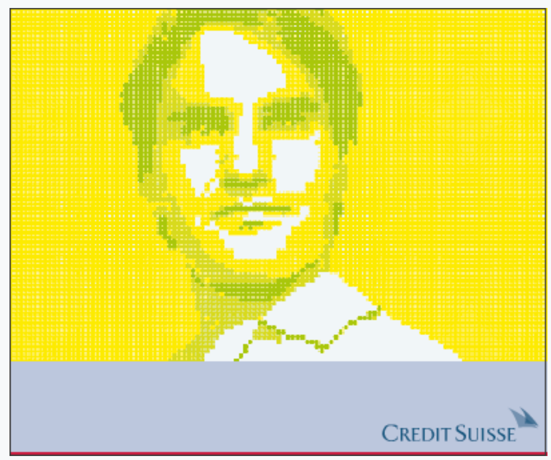
"If you study medicine, at some point in your career you have to decide whether you want to opt for the emergency room or cosmetic surgery," says Mr. Mueller to explain his career choices. "I gravitate towards the emergency room."

Aer Lingus flirted with insolvency after 9/11 but snapped back smartly and was successfully floated on the Dublin and London stock exchanges in 2006. It then over-expanded and tried unsuccessfully to go up-market. When Mr. Mueller arrive at the airline in September 2009, "not even our employees were sure what we stood for," he said soon after.

Today, thanks largely to a recovery plan Mr. Mueller launched late last year, Aer Lingus is sitting on more than €900 million ($1.91 billion) of cash, with a strong balance sheet, and even posted an operating profit of €60 million for the first nine months of the year, compared to an operating loss of €34 million for the same period in 2009, despite Ireland's deepening financial troubles.

Following the Irish government's announcement this month that it had turned to the European Union and the International Monetary Fund for a bailout, Aer Lingus officials say they will stay focused on cutting costs, limiting capacity and building their Dublin hub for traffic between Europe and the U.S.

Still, the carrier faces daunting obstacles. Ireland's economy is shrinking under the weight of massive bank problems and a collapsed construction sector. Personal incomes have fallen



and business spending has been slashed.

Mr. Mueller highlights the positives: Ireland runs a big trade surplus and, being an island, its population travels incessantly. But to adapt to Ireland's harsh new reality, in December he launched a restructuring program dubbed Greenfield. Its goal is to cut costs, make the operation more nimble and position it for an eventual upturn. A cornerstone has been to shake the carrier's legacy of its days as a state enterprise.

"Change is painful and we have to respond to that in a humane way," he said in an interview. "The desperate situation in Ireland has created solidarity."

Niall Shanahan, spokesman for Irish public sector trade union Impact, said staff generally agree. "Nobody takes anything for granted," Mr. Shanahan said. Despite some difficult moments with Mr. Mueller during five months of negotiations over Greenfield, "he seems to have a very pragmatic approach," Mr. Shanahan said.

Aer Lingus Chairman Colm Barrington said that pragmatism was one reason he wanted Mr. Mueller for the job. Another plus was that Mr. Mueller isn't Irish. "Aer Lingus seemed very Irish-centric," said Mr. Barrington, who joined the airline one year before Mr. Mueller. "A foreigner wouldn't understand the way things work in Ireland, and that would be great."

Mr. Mueller had used his outsider status and pragmatism effectively at Sabena before time ran out, say former colleagues.

"A lot of executives came from big carriers and would walk around with their nose in the air, but he was utterly unpretentious," says Hubert Horan, a American airline veteran who worked with Mr. Mueller at Sabena. "He can be the person with nothing to lose, and he can tell people the truth."

Mr. Mueller says that his job before Aer Lingus, as aviation director of leisure group TUI Travel PLC and as a member of the executive committee of Deutsche Post AG, reminded him not to consider one market superior to another. Old-style "legacy" airlines such as Sabena and Aer Lingus are often weighted with the pride and baggage of being national carriers, which can complicate restructuring.

"Sometimes what is declared impossible in legacy carriers is possible," he said.

Cost-cutting has opened new possibilities for Aer Lingus, Mr. Mueller said. In March, the Irish carrier launched an unusual joint venture with United Continental Holding's United Airlines to fly between United's hub at Dulles Airport outside Washington, DC, and Madrid—a market neither of them could serve profitably alone. Aer Lingus supplies the plane and crew at low cost, while United markets the tickets. The pair spit income from this entirely new revenue stream. Mr. Mueller said he sees the project as a model for more deals.

Mr. Mueller said that Aer Lingus's other partnerships, with JetBlue Airways Corp. and British Airways PLC, are also boosting its business and offer a way for it to grow without getting swallowed up. The carrier avoided that fate following two takeover attempts by Irish rival Ryanair Holdings PLC.

Ryanair now owns almost 30% of Aer Lingus after being blocked from taking it over by the European Union. The Irish government still holds 25%, staff own an additional 12.5%, and the rest is listed in Dublin and London. Aer Lingus is pushing regulators to force Ryanair to divest its stake, arguing that having a rival as its biggest shareholder complicates strategic planning.

For now, Ryanair and its voluble chief executive Michael O'Leary have stayed out of Aer Lingus' board of directors, whose policies they prefer to criticize from the sidelines.

Two months after Mr. Mueller's arrival, Ryanair's boss said the newcomer was taking appropriate steps to return the carrier to profitability, but added, "You could put a potato into Aer Lingus and it would come up with the same decision."

Mr. Mueller has defied Mr. O'Leary's frequent predictions that Aer Lingus is headed for imminent doom, and increased revenue even as traffic drops. But Mr. O'Leary has still criticized Aer Lingus's retrenchment and dismissed its profits because these have been gained by shrinking the carrier.

Mr. O'Leary says he expects the cash-strapped Irish government will eventually ask Ryanair to take Aer Lingus off its hands, but outside observers say that's unlikely to happen because the EU has objected to the carriers merging. Whether Ryanair holds or divests its stake could ultimately be decided in courts.

Despite those fights, Mr. Mueller said relentless competition with Ryanair for more than a decade has brought discipline. "Aer Lingus would not have survived in the absence of Ryanair," Mr. Mueller said.

To keep Aer Lingus on course, Mr. Mueller is trying to shape it up for constant change, which he admits is tough on staff.

"The problem is, once you rest on your laurels for a second, it's almost game over," Mr. Mueller said.

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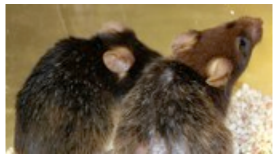

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