

SKYBUS SHUTDOWN

How could it happen?

Fuel prices, management woes jolted airline into sudden tailspin

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Beneath the thin veneer of perky ads and some upbeat news stories about the new airline there were signs of trouble at Skybus Airlines:

It dropped routes and discontinued flights.

Customers weren't snapping up tickets for the popular summer travel season.

And two top officials left the company in the last month.

At the same time, the economy continued to sour, fuel prices jumped and two other airlines went under.

Observers agree that fuel prices were perhaps the single biggest factor in Skybus' demise, but they disagree on some other points. Some say the company wasn't managed properly.

Things looked fine from the outside as recently as late February. Fox Business News did a mostly upbeat interview Skybus Chief Executive Bill Diffenderffer, wrapping up by praising the airline as a "success story."

By then, though, deep divisions were growing within Skybus. Although the news media often portrayed Diffenderffer as an innovative leader, some investors and board members felt he was more eager to spend time in front of the camera rather than tackle the tough day-to-day task of running an airline.

By his own admission, Diffenderffer is more of a creative "big-picture" type than a hands-on manager. The author of *The Samurai CEO*, he enjoyed being the face of Skybus on news shows and the speaker circuit in cities Skybus served as the airline was spending millions getting out of the gate and expanding quickly to new markets.

One of the people who was unhappy with Skybus' general direction at that point was Mike Hodge, then chief financial officer. The 35-year-old had come to Skybus from hedge-fund manager Tiger Management, which was a 4 percent investor in Skybus.

Hodge and Diffenderffer are very different animals. Diffenderffer is outgoing and likes to get along with people in power; Hodge is reserved and no-nonsense. He watched with the impatient, laserlike focus of a hedge-fund executive while Skybus lost money and customers because of operational inefficiencies through the winter.

At least one source said Hodge actually tendered his resignation in early March. In an interview last month, Hodge denied he'd actually resigned, but said he was definitely "frustrated" with the way things were going.

Meanwhile, the price of oil was reaching new heights almost daily and the credit markets were tightening. Airline stocks tumbled, and consolidation was seen as the key to survival for even the major carriers. Smaller airlines were threatened with extinction.

"When we started flying, oil was at \$62 a barrel. Now, it's \$106," said Charlie Clifton, vice chairman of Skybus, in an interview yesterday. "The West Coast routes worked, but not at those prices. We had to pull off them, which hurt our credibility. You need routes to mature, but you just don't have any room to maneuver at those costs."

Oil prices have made airlines such as Skybus endangered species.

"At this current level, there's no such thing as a low-cost carrier," said Darryl Jenkins, a Virginia-based airline expert and aviation professor at George Washington University. "There's currently no airline in the United States that has a viable long-term plan for survival. Jet fuel is a killer category, and it's a desperate time for the industry."

Although Skybus' investors didn't expect the airline to turn a profit within the first year, they were increasingly impatient with mounting losses and expenses. The \$160 million in startup capital that seemed ample at the outset was disappearing fast.

The airline also was courted with promises of \$57 million worth of incentives, most of that in tax breaks and improvements, some of them from Port Columbus.

The airport spent \$11.5 million on terminal improvements, \$2.6 million of that directly related to Skybus. It also waived \$2 million in fees.

Skybus also qualified for, but hadn't yet received, tens of thousands of dollars worth of bonuses for serving new markets from Port Columbus.

In return, Port Columbus received about \$2 million in lease fees from Skybus and millions more in parking and concession revenue generated by Skybus' presence at the airport, said David Whitaker, the airport's vice president of business development.

"Part of our mission is to create and improve space for airline use and passenger growth," Whitaker said. "There is some risk associated with that when you do a buildout and then you have a loss of service, but that's the nature of the business."

Immediate financial issues weren't the only things weighing heavily on Skybus. Labor problems were brewing. Pilots unhappy with working conditions, pay and a lack of communication with management started a drive to unionize under the Teamsters. The effort posed a direct threat to Skybus' plan of keeping labor costs well below industry averages.

The issue led to hands-on attention at the highest levels.

By early March, Skybus board Chairman C. Robert Kidder started coming into the Skybus offices near the airport several times a week, trying to figure out ways to staunch the bleeding. Kidder and Clifton reviewed expenses with the Skybus financial team, and decided a major, immediate overhaul was needed.

In mid-March, Diffenderffer signaled that major changes would be made to Skybus' routes that wouldn't necessarily be popular. They were necessary for the health of the airline. Several days later, Skybus cut flights and chopped destinations including Chattanooga, Tenn., and Niagara Falls, N.Y. -- the latter even before flights were set to begin.

Less than two weeks later, Diffenderffer stepped down to "return to the book-writing career he left in 2005," an explanation that was widely greeted with eye-rolling. Asked on the day of the announcement whether Diffenderffer had been shown the door, Kidder replied: "Bill understood what he was good at and what he wasn't good at."

Diffenderffer insists he didn't abandon a sinking ship.

"Two weeks ago when I left, it wasn't looking this way," Diffenderffer said yesterday. "Things got suddenly worse in the last two weeks. For one, bookings just fell off the cliff. Summer bookings that should've been coming in just weren't."

Though Diffenderffer blames a weak economy and housing market for a pullback in consumer demand, a loss of confidence in Skybus was a contributing factor. Online chat boards were filled with complaints about dropped routes and lack of customer service. It didn't help that Skybus never gained its desired foothold in the Greensboro, N.C., base it opened in January because the airline simply ran out of money to do much marketing.

In a memo to employees the day Diffenderffer left and Hodge took over as CEO, Hodge warned that Skybus was "behind plan" in its cash reserves. He said the airline would quickly try to renegotiate contracts with all its vendors to achieve cost savings, while getting a grip on increasing on-time performance and lowering the flight-cancellation rate.

Hodge never got a chance. A week later, one of Skybus' first employees, Vice President of Operations Bud Sittig, resigned. Although he urged employees to be loyal to Hodge, he said he was leaving because he was "out of step" with management.

That was four days ago. On Friday, the Skybus board held a special meeting and decided that Skybus would cease operations that evening.

Many observers have blamed the business model for Skybus' demise. Clifton, who spent 16 years at Ryanair, Europe's leading low-fare carrier, insists that Skybus' demise doesn't prove that the Ryanair model can't work in the U.S.

Ryanair took the Southwest Airlines model and stripped it of all the homespun niceties. Ryanair delivers on a simple promise: It will get you and your luggage from Point A to Point B for the cheapest fare possible. Skybus promised the same thing but didn't deliver consistently.

"I think the folks in the States demand more customer service than Europeans are used to, and I think that thinking impairs companies here from going after a simple, very low-cost model," Clifton said. "But I struggle with why it wouldn't work here if Wal-Mart works. I think the Ryanair model could work if it is implemented fully. You can't implement it a la carte."

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