

MEMORANDUM TO CABINET BY THE
HONOURABLE THE PRIME MINISTER.

Establishment of a National Airline

BACKGROUND

Aero Technique Company Ltd., a United States corporation specializing in air transportation development and operations, was set up in California in August, 1967 with a capital of 400,000 dollars. The Company is principally owned by First California Co. of San Francisco.

Aero Technique obtained the services of Mr Joseph B. Mathis, an Airline consultant, to consider the possibility of developing a Malta-based international airline.

Preliminary studies indicated to the Company that Malta could profitably support one-carrier air services to major cities in Europe. Traffic would principally be made up of tourists from Northern Europe to Malta.

On the 12th September, 1967 Air Melita was registered as a local Company with its first object "to establish, develop, and operate an Airline and air transport services in general and to own, operate and manage all types of aircraft for the purpose of carrying passengers and freight, including mail" The Authorised Capital of the Company is £2.5 m. and the Issued Capital at the present stands at £1,000.

MARKET RESEARCH

In furtherance of the proposal, Aero Technique obtained the services of Checchi and Co., Aviation Market Research Consultants of Washington D.C., who drew up a comprehensive Report on "Passenger Projections for a New Airline to serve Malta". The Report, which does not go into the economics of the venture, concluded that the outlook for Air Melita to build traffic from Northern Europe is good. It projected that the total of passengers travelling to Malta from Continental European markets (excluding Italy) will rise from around 10,000 passengers in 1968 to between 146,000 and 265,000 in 1973. This

/assumed

assumed that the primary obstacles to the movement of this tourist traffic to Malta - the lack of direct air travel communication and the lack of travel promotion of Malta in Continental Europe - would be seriously and immediately taken up, the first by private enterprise and the second by the Malta Government Tourist Board.

The estimates of passengers given above would result in the Company deriving passenger revenues rising from about 20.5 m. in 1968 to 36.5 m. - 210.5 m. in 1973.

In this connection, it is relevant to draw attention to the following extract from the Robens Report:

"12. Communications with Europe.

If an investigation of the tourist market in Northern Europe reveals that there is a considerable potential for development..... then active steps should be taken to develop this potential, in particular by establishing an air service between one or more points in Northern Europe and Malta".

It would appear that the Checchi Report has established the existence of such a market.

FINANCIAL FORECASTS

On the basis of the Checchi Report and the revenues projected therein, Air Malta drew up pro forma financial statements for the pre-operating period and for the first three years of operation; on the results obtained therefrom, Air Malta decided to proceed with the project.

The forecasts are necessarily based on certain assumptions. The revenue rate per passenger mile, the amount of traffic which will be generated and its rate of growth, the load factors, the amount of intra-European traffic which will be carried by Air Malta and numerous other factors go to make the operations profitable or otherwise and a slight variation in any one of the assumptions would either agitate or disturb profitability. It could even make the Company a 'distinguished' operator or drive it to bankruptcy. The speculative nature of air transportation particularly in the field of new airlines opening up new routes, however, is such that forecasts must necessarily be accepted unless they are obviously unrealistic.

/CAPITAL FORMATION ...

CAPITAL FORMATION

Air Melita intend to raise the capital necessary for operations from the following sources:

Long-term debts

i.	British banks, 10-year 6½% loan, secured by aircraft	£ 11,500,000
ii.	7%, 15 year debentures from local sources and Aero Technique	£ 3,000,000
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		£ 14,500,000
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Equity

i.	Common Stock Government of Malta	£ 2,000,000
	Aero Technique	£ 2,000,000
ii.	Government of Malta non-interest bearing grant	£ 1,500,000
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		£ 5,500,000
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	TOTAL	£ 20,000,000
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The equity capital, as proposed, would be exclusively owned by the Government of Malta and Aero Technique in the ratio of 3.5 : 2.0; whatever variations are made in this ratio, it would be necessary for at least 51% of the capital to be held by the Government or by nationals of Malta if the Company is to qualify for recognition as a "designated airline" or a "National carrier".

with regard to the actual percentage of capital subscription from "official" sources, discussions with Air Melita representatives indicate that the Company is not deeply concerned about the form or the amount of the subscription so long as a minimum 51% holding by the Government and/or Corporation and/or Maltese Nationals is assured, so that an outright grant is not a sine qua non of the project. On the other hand, the Company feels that, without "official" participation, the Company would not be able to attract any substantial investment from local private or institutional sources.

/FISCAL

FISCAL AND OTHER AIDS

The Company is also seeking the usual fiscal aids: exemption from Customs duty on equipment and spares, exemption from income tax for 10 years and other aids in the establishment of ground facilities and in the training of personnel.

The project, however, would not seem to qualify for assistance under the Aids to Industry Ordinance as it is not directly or indirectly an industrial activity. A minor amendment to the Ordinance would remove this difficulty out of the way.

AIR TRANSPORT LICENSING AUTHORITY

Air Melita have already applied under the provisions of the Air Transport (Licensing of Air Services) Regulations, 1949 to the Air Transport Licensing Authority for licences to operate scheduled services to various points in Europe.

The applications have yet to be considered by the Authority.

In connection with the applications made to A.T.L.A., Director of Civil Aviation has commented in extenso on the broader features of the project and a copy of his communication is at Appendix A.

LETTER OF INTENT

Aero Technique is seeking the issue of a Letter of Intent by the Government, a draft of which, prepared by the Company itself, is at Appendix B.

The terms of the draft include, by reference or by implication, the following points:

- a) recognition of Air Melita as the National Carrier (para. 1);
- b) the intention of the Government to grant the necessary permission to operate (para. 2); this presumably is meant to include the necessary A.T.L.A. licensing;
- c) £1,605,000 of the financing will be provided by Government and/or Maltese institutions and individuals or a combination of these (para. 3);
- d) Government will endeavour to conclude bi-lateral air services agreements with the countries to

/which

which Air Melita will be establishing routes (para. 4);

- e) Government (presumably through the Tourist Board) will embark upon a programme promoting tourism to Malta in North European countries (para. 4);
- f) Government will assist in the Company's negotiations to acquire the necessary operating equipment (para. 5);
- g) within the framework of the Aids to Industry Ordinance and other legislation, Government will make available certain tax and other incentives, will help in the establishment of ground facilities and assist in the training of personnel (para. 6).

It is undeniable that without a Letter of Intent, Aero Technique cannot be expected to pursue the matter; nor would it be able to secure a commitment from overseas financial institutions to participate in the venture.

If it is the intention of the Government to "encourage" the formation and operation of Air Melita, a Letter of Intent seems to be called for. Such a letter would be suitably worded to permit freedom of action by both A.T.L.A. and the Aids to Industries Board.

Hon. Ministers are invited to consider and decide on the following points:

If Air Melita were to be allowed to operate:

- i) does Government propose to make Air Melita its National Carrier?

It has been made clear by the promoters of Air Melita that the Company should be the National Carrier. The project is sizeable and the market primarily limited to travel originating from outside Malta and National Carrier status would enable the Company to plan ahead on a sound footing of "exclusivity".

- ii) does Government propose to invest capital in Air Melita?

Air Melita must have at least 51% of its capital subscribed from Malta sources to be in a position to be appointed a "designated airline" or a "National Carrier".

/Moreover

Moreover, Aero Technique anticipate that, if Government does not make a grant to or take up shares in Air Melita, the greatest difficulty would be experienced in raising capital from other sources.

- iii) does Government propose to see fiscal aids being granted to the Company?

This is a matter for the Aids to Industry Board but Government's favourable inclination would permit the amendment of the Ordinance which alone would allow the Board to consider granting aids.

- iv) does Government propose to issue a Letter of Intent to the Company?

This could be limited to a declaration of acceptance in principle which would incorporate the Government's stand on the National Carrier issue and its intentions with regard to capital participation. Such a letter could also incorporate reservations with regard to operating licences which are A.T.L.A.'s responsibility and the aids which fail to be considered by the Aids to Industry Board.

L-ARKIVJI NAZZJONALI TA' MALTA

14th December, 1967.

DOA/332/10

OPM/553/67

DEPARTMENT OF CIVIL AVIATION
CIVIL AIRPORT BUILDINGS
LU, A.
MALTA, G.C.

4th December, 1967.

Confidential

Administrative Secretary

Air Melita

With further reference to your letter of the 21st November and with reference to mine of the 22nd November, Mr Mathis has now submitted in terms of the Air Transport (Licensing of Air Services) Regulations, 1949, six applications for the operation of scheduled services on the following routes:-

- (a) Malta - Paris - Brussels - Oslo
- (b) Malta - Nice - Amsterdam - Helsinki
- (c) Malta - Tunis - Lisbon
- (d) Malta - Athens - Beirut
- (e) Malta - Cologne/Dusseldorf - Copenhagen
- (f) Malta - Zurich - Stockholm

2. I enclose a copy of each of the applications together with its relative schedule as well as Annexures as follows:-

- (a) a complete schedule of all services to be operated by the Company
- (b) list of proposed fares
- (c) Information on the aircraft proposed to be used
- (d) The aircraft proposed to be employed
- (e) The Insurance proposed to be taken
- (f) Information on "Air Melita Ltd"
- (g) Map of the Air Routes proposed to be operated.

3. I have asked Mr Mathis to furnish me with information on his operational practices and his maintenance practices and I enclose a copy of his letter dated 28th November. The pro-forma balance sheets which should be attached to this letter were not in fact attached but are stated to be on the way from California together with a statement and proof of the financial resources of Mr Mathis which I have also asked him to furnish.

4. I understand that a copy of the study made by Checchi and Company of Washington, D.C. on "Passenger projections for a new airline to serve Malta" and prepared for Aero Technique Co. Ltd has been supplied to you direct and a further copy is not therefore enclosed.

5. Mr Mathis has registered "Air Melita Ltd" in terms of the Commercial Partnerships Ordinance, 1962. The Memorandum of Association follows the usual lines with the Authorized Capital being set at £2,500,000 the Issued Capital being £1,000,000, 50% of which is paid up. The Issued Capital is owned by two shareholders

i.e. Prof. Jos. M. Ganado	950 Ordinary Shares
Francis Abela	50 " "

The Directors of the Company may consist of not less than two but not more than seven, the first Directors being Mr Joseph B. Mathis and Prof. Jos. M. Ganado. The Company Secretary is Mr Francis Abela. The Company was originally registered as a private company but it is proposed to turn it to a public company.

Exchange Control to transfer 40% of the shareholding to Aero Technique and that Mr Edward Bolton of 161 Constitution Drive, Hemet Park, California, is being appointed another Director.

7. The aircraft which Mr Mathis states he will use are B.C-111 twin-jet aircraft. From information I have checked with the manufacturers, these aeroplanes are in use apart from British airlines, also by American Airlines such as T. The B.C-111 has proved itself to be a very economical aircraft with Direct Operating Costs of 2.0 U.S. cents per seat mile on stage lengths of 250 statute miles. Mr Mathis originally mentioned that he would be purchasing three of these aircraft from the Irish Airline Aer Lingus who have decided to standardise their fleet with the long-term objective of only operating Boeing aircraft. I have confirmed this through contacts I have with Aer Lingus and that they have four aircraft for sale. Mr Mathis is now saying that he will purchase new aircraft and I have checked that he has been in touch with both the British Aircraft Corporation who manufacture the B.C 1-11 and also with Hawker Siddeley Aviation who manufacture the Trident. While both, of course, are willing to sell to him, the difficulty is that the American Government may not allow him to use loan funds obtained from American sources for the purchase of British aircraft.

8. On the subject of maintenance of the aircraft and the training of the crews, Mr Mathis has said that he will enter into an agreement with British United Airways. BUA are the largest of the British Independents and have three VC-10s and ten B.C 1-11s. I have confirmed that they are prepared in principle to offer Mr Mathis maintenance facilities for his aircraft at Gatwick and to undertake training of aircrew, Cabin staff and engineers. They make technical facilities available for the staff of other airlines and they can make arrangements on a similar basis.

9. With regard to Administration, Mr Mathis proposes to be himself Managing Director of the airline with the following personnel:

Mr T.M. Peck (U.S.)	Deputy Managing Director
Mr Kenneth Barnes (Australian)	General Manager Technical Services
Mr William M. Hordenstine (U.S.)	General Manager Sales
Mr C.W. Petrich (Australian)	General Manager Operations
Mr Donald Ingalls (U.S.)	General Manager Finance
Mr Charles Quantz (U.S.)	Secretary and Legal Counsel

with a General Manager, Services, (U.S. or European) yet to be selected.

All these people are stated to have extensive experience in aviation and to average in excess of 18 years with other international airlines.

In the world Aviation Directory I have been able to trace Mr Peck who is employed in the Special Services Division of Trans World Airlines as Director of Associated Airline Affairs. In the same Directory, a Mr Donald Ingalls is listed as Controller with Slick Airways.

As regards Joseph Berwise Mathis himself, he was born on the 1st July, 1926. In 1948 he became Clerk in the Inspection Department of Trans Texas Airlines. On the 8th November, 1952, he was issued by the Civil Aeronautics Board with licence No. 125 1595 as an Aircraft Dispatcher. On the 18th November, 1952, the FCC issued to him Restricted Radio Telephone Operator Permit No. 9-24414. His status that in 1957 he was still with Trans Texas and had become manager of scheduling of flight crews and aircraft. In 1958 he went to Alaska Airlines and worked as aircraft dispatcher. In 1961 he transferred to Air America and worked as manager of Air Transport Operations Group on a contract flying passengers and cargo within Laos. In 1962 he worked for Slick Airways in flight planning and in scheduling crews and aircraft. He further states that in 1964 he started working on the Malta project on which about £107,000 have already been spent (in the financing estimates produced by Mr Mathis, Pre Operating Costs are given at £521,570).

Transiff International, Monark Airlines, American Airlines
and Slick Airlines.

10. Financing may, of course, prove to be a stumbling block. As you are aware, when we come to designate an airline in terms of an Air Services Agreement, the State who will be the other party to the agreement will want to be satisfied that the airline designated by the Maltese Government is substantially owned and effectively controlled by the Maltese Government or by Maltese Nationals. On the assumption for the moment that the appointment of a majority of Maltese directors on the Board counter-balances the all-foreign administration to be employed by the airline (see para 9 above) Mr Mathis will have to raise the majority of his equity in Malta. Mr Mathis proposes to raise £1,609,000 from Maltese sources, £4,107,000 from British Banks as a ten year loan at 6 1/2% interest and £1,425,000 to be subscribed by Aero Technique. Mr Mathis is aiming at obtaining a grant of between £720,000 and £359,000 from the Malta Development Corporation, the Government of Malta making a loan or taking equity of between £359,000 and £720,000 and other Maltese financial or business sources providing between £720,000 and £359,000 on subordinated debt or preferred basis.

Quite a large proportion of Mr Mathis's financing is going to be debt. In the United States there has been a fourfold increase in the industry's total investment in 1966 as compared with 1955, with debt exceeding equity for the first time in 1959. This tendency has continued since. A decided swing for the reverse is showing now, however, with the acquisition of the next generation of aircraft equipment by the U.S. Scheduled airlines. Whereas in 1961 long-term debt stood at 1.75 billion dollars and stockholders equity stood at 0.96 billion dollars, the figures for 1966 were 2.21 and 1.83 respectively. The greatly increased market prices of airline stocks is reckoned to be one of the factors that have brought this about.

11. With regard to traffic, there is no doubt that before the routes start being flown and services are available, traffic is not just being moved. There is certainly no doubt here as to what comes first. On the other hand, one cannot be dogmatic as to what traffic will be available or at what rate that traffic will build up. Even accepting as Mr Mathis is doing, that the airline will make a heavy loss of between £400,000 and £500,000 in the first year of operation, the risk that is being taken consists in whether the traffic will build up at a rate which will make operations profitable from the second year and which will not send the airline on the rocks as has unfortunately happened to many airlines in other countries.

12. Enquiries I made with our Embassy in Washington did not elicit much information except that the opinion was that Mr Mathis does not have a very good grasp of the intricacies involved in the setting up of such projects; that a similar project accepted by the Luxembourg Government did not materialize; and that Aero Technique Co. Ltd was set up in California in August last with a capital of 400,000 dollars.

13. The salient points that strike me in this proposal are:-

- (a) This airline is starting from scratch. It is not being mothered in its teething troubles by a long established airline nor is it drawing on its experience obtained over the years. Mr Mathis is bringing together men of different nationalities and experience who have never worked together as a team. He may and he may not succeed in forming a working team. Mr Mathis himself has no experience managing an airline.
- (b) Mr Mathis does not propose to invest any money of his own in the Company. If Government does not make a grant to the Company or take shares in it, it is anticipated that the greatest difficulty will be experienced by Mr Mathis in raising his capital in Malta. Considering that Government has been reluctant to take shares in Maltese airlines which has been consistently making money, is it going to take shares and make a substantial grant to a company which may lose money or at best whose operations are uncertain? On the other hand as explained above, the participation of Maltese Capital is an indispensable requirement.

L-ARKIVI NAZZJONALI TA' MALTA

14. The first step to be taken, however, is for the Air Transport Licensing Authority to consider the six applications and have them published in the Government Gazette in terms of Regulation 7 of the Air Transport (Licensing of Air Services) Regulations, 1949. You may wish in the first instance to fix a date when the Authority can hold a meeting unless you consider that the Authority need not be convened just for the purpose of deciding on publication, in view of the fact that Regulation 7 makes publication mandatory. If you decide not to convene the Authority, I propose that we stipulate the full 28 days as the period during which representations or objections may be received.

Sgd. (G.H. Perro)

Director of Civil Aviation

Aero Technique Company Ltd.,
300 Russ Building,
San Francisco,
California,
U.S.A.

Gentlemen:

This letter expresses the present intention of the Government of Malta concerning the establishment of a Maltese International Flag Airline to be based upon and operate from the territory of Malta.

2. The understanding and intention of the Government is that the necessary permission to operate such an airline will be granted with the following understandings:

3. The Government approves the principle and plan of the proposed airline, with the understanding that you will provide approximately £5,536,000 toward the financing; it is contemplated that approximately £1,605,000 toward the said financing will be furnished by the Government and/or Maltese institutions and individuals or a combination of these.

4. It is further understood that you will, upon the completion of the financing of approximately £7,141,000, embark upon an extensive programme of advertising in the territories included in the proposed operation submitted by you; it is the Government's intention to exert all necessary effort to expedite the completion of the necessary bilateral agreements with the countries projected in your stated plan of operation, and further to embark upon a continuing programme toward stimulating and promoting tourism to Malta from those countries.

5. It is the Government's understanding that you have commenced negotiations with British aircraft manufacturers toward the acquisition of the aircraft equipment proposed in your projected operations and have arranged financing accordingly; it is the intention of the Government to assist you by all useful means in your negotiations for the acquisition of this equipment.

6. The Government is informed in your operations projection that within 12 months of your becoming operational you will employ approximately 400 to 500 Maltese individuals; accordingly, the Government will offer all possible support, within the framework of its Aids to Industries Programme, toward establishing the necessary ground facilities and assisting in the training of these individuals. The Government will also make available to you certain tax and business incentives.

7. It is our understanding that you have commenced a market study, through the facilities of Messrs Checchi and Busuttill, for the purpose of determining the market

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potential and feasibility of your projected operation and that this study should be completed approximately October 1st, 1967. It is further our understanding that within a reasonable time of your receipt of the necessary Government approvals, bilateral agreements and commitments on the financing from Maltese sources, you will have completed all necessary arrangements toward financing and aircraft availability.

Government of Malta

By: _____

Affirmed:
Aero Technique Company Ltd.,

By: _____