

AMADEUS MAKES AN OFFER FOR NAVITAIRE AND PLANS AN ALLIANCE WITH ACCENTURE

T2RL Staff

THE FACTS

Amadeus announced their intention to acquire Navitaire for 830M USD. The deal is expected to close in the fourth quarter of 2015. Amadeus and Accenture also announced a strategic partnership to focus on digital services for Amadeus' airline customers.

THE ANALYSIS

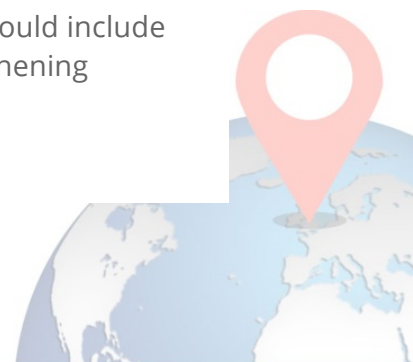
Should the deal obtain the relevant regulatory approvals it will change the structure of the market for the PSS business. Looking at the global market place this would give Amadeus a global share of some 36% as measured by revenue passengers boarded.

Current Migrations by Revenue Passengers Boarded in Millions (full year 2014) by Airline HQ Location

PSS Supply	Europe	North America	Asia Pacific	ROW	Global
Amadeus	417	1	198	170	786
Navitaire	186	38	165	89	478
Others / In-House	386	807	775	255	2,223
Total	989	846	1,138	514	3,487
% Share	61%	5%	32%	50%	36%

Source: T2RL Research

The volumes do not include future contracted implementations which would include Japan Airlines and Southwest and the loss of TAM and Air Berlin, strengthening Amadeus' position in North America and weakening it slightly in Europe.



Current Migrations by Revenue Passengers Boarded in Millions (full year 2014) by Business Model

PSS Supply	Full Service Carrer	Hybrid Carrier	Low-Cost Carrier	Other Business Model	Total
Amadeus	724	35	2	25	786
Navitaire	2	201	241	34	478
Others / In-House	1,553	316	231	121	2,221
Total	2,279	552	474	182	3,487
% Share	32%	43%	32%	32%	36%

Source: T2RL Research

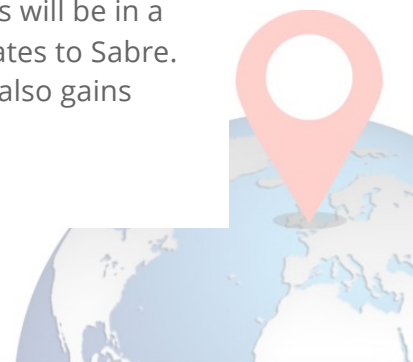
Amadeus' current customer portfolio is very different to that of Navitaire. The acquisition, if successful, will balance the portfolio in two customer segments where they are weakest, although Southwest is still the World's largest hybrid carrier and yet to cutover to Amadeus.

Furthermore, T2RL's research suggests that Amadeus have targeted the two fastest growing market segments in this deal.

Business Model	CAGR '10-'19	CAGR '15-'19
Charter Carrier	6.1%	4.2%
Charter/Scheduled Airline	2.7%	4.0%
Franchise Carrier	3.6%	4.1%
Hybrid Carrier	7.8%	8.3%
Low-Cost Carrier	13.6%	11.9%
Network Airline	5.3%	5.7%
Total Market	6.0%	6.9%

Source: T2RL Research

The addition of Navitaire's Gol Airlines and Azul in Brazil means Amadeus will be in a better position to maintain a presence in South America after TAM migrates to Sabre. Although Gol may currently be looking at market alternatives, Amadeus also gains Indigo and SpiceJet in India.



For Amadeus, there are other reasons to be excited about this deal.

If Amadeus can establish a logical upgrade path from the Navitaire solution to Amadeus' Altea for those low-cost airlines who grow to a hybrid / full-service carrier, then it could conceivably prevent that airline from considering other options. This capability could lock in significant revenue. However there is a volume shift risk as Lufthansa's Germanwings, IAG's Vueling and Air France/KLM's Transavia have all been growing faster than the rest of their group bringing some risk of dilution in total revenues over time.

The new, larger Amadeus also has the potential to re-use technology between the solution sets thus improving both product offerings and reducing total costs. For example, Altea has significant customer management capabilities that could be of interest to Navitaire customers. Navitaire customers would have access to these functions sometime after the deal closes.

Of course, this news also means that Amadeus will immediately develop many more airline customer relationships. These relationships could have significant benefits to the extent that Amadeus is able to cross-sell its components to Navitaire customers, and Navitaire components to existing Amadeus customers. T2RL's research suggests that Amadeus has enough confidence in its components such as its Revenue Management, Revenue Accounting, and Loyalty Solutions to value these synergies. With a price of some 14 times earnings, Amadeus may not have shared much of these synergies with Navitaire but product portfolio rationalisation especially in revenue accounting will be likely post the closing of the deal. Travelport will suffer as a result of the agreement, although this is unlikely to be material. Currently Travelport handle other airline availability, bookings and interline tickets and electronic tickets together with some pricing functions for some Navitaire customers.

With any large deal such as this one comes some amount of risk. Today, the low-cost and full-service customer bases are distinct, but the line between them is becoming more blurred. As some low-cost carriers require more capabilities, and full-service carriers desire simplicity and lower costs, Amadeus could eventually find itself offering two solutions to one customer base.

For airline customers, on a nominal basis this deal means that they would have less choice between vendors.



For other PSS vendors, this news means their strongest competitor will become even stronger. While the deal will close in the fourth quarter of 2015, T2RL estimates that it will take Amadeus more than a year to effectively integrate Navitaire into their company. Current vendors will thus have a short window of time while Amadeus management's attention is diverted on integration. After that, it will be "game on".

T2RL's research indicates that roughly 50% of Navitaire's customers will be re-competing or re-contracting their PSS services between now and the end of 2018. As a result, other PSS vendors will need to ensure they have a fair hearing and can participate in a competitive tender process before Amadeus moves to lock these customers up. It will be interesting to see how many of Navitaire's customers, who usually take pride in defining themselves through direct distribution, will be comfortable with their provider also being a GDS, although the largest airline by passengers boarded, Ryanair, now provides some of its content to the GDSs.

Regarding the Amadeus – Accenture alliance, T2RL's research indicates that there is a significant services opportunity in and around PSS. It is difficult for PSS vendors to address this need themselves as they are oriented around building products and not performing consulting and support. A company with a services culture and subject matter expertise around a specific PSS solution, especially the leading one, could and should serve this market need well. However, Accenture will need to meet the appropriate price points to be successful. In addition, the track record of such strategic partnerships is poor, providing reasons to be sceptical about the eventual success of this new strategic alliance. T2RL see the Accenture alliance as an easy means for Amadeus to pass on some additional benefits to Accenture by buying services that they would consume anyway without overpaying on the earnings multiple. Such a premium could lead to a discount on the current stock price. The non-exclusive partnership deal also provides Accenture access some of Amadeus' larger customers. This represents a direct attack on HP's and IBM's services divisions.

THE SPECULATION

The dominant position in Europe in particular could create some regulatory challenges for Amadeus. T2RL believe most customers will not oppose the transaction and Accenture contracts are particularly unlikely to have change of control clauses that would support a mass exodus post transaction. A few commercially savvy and disruptive customers may seek to exploit the opportunity to lower their costs further and to obtain contractual improvements in their own Navitaire terms but this is unlikely to have a material effect on the outcome.

Amadeus will definitely be concerned about the regulators in Europe but will have looked at the Amadeus and Navitaire solutions as covering different markets.

The news of this acquisition also begs the question whether there will be further consolidation in the PSS provider market. After this deal is consummated, Amadeus and Sabre will have a 53% share of the market. Whilst such a total is high for the top two suppliers in any industry, the market is relatively fragmented thereafter, especially in the small- to medium-sized airline market. T2RL believe it is quite likely there will be further consolidation in the industry.

Smaller providers such as Hitit, Radixx, ISA, KIU and Intellisys will all become much more interesting for those looking to enter new segments or buy their way into the PSS market place, especially if prices are likely to rise in the longer term.

Undoubtedly T2RL believe there will be an impact on pricing in the longer term. In other industries, consolidation of the key suppliers is often followed by increased pricing, or less flexibility on key contractual terms. As an example from the airline industry itself, the U.S. Justice Department is currently investigating whether some of the USA's biggest airlines have colluded to keep airfares high. The Justice Department is specifically concerned that recent merger activity among USA airlines has led to less price competition. Regardless of whether the investigation finds any wrongdoing, the fact such questions are raised shows the level of concern where and when there is too much market power. It will be important for all market participants to determine, after this deal is closed, that there is still significant price competition in the PSS market.



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