

Jetblue airway ipo valuation essay sample

[Environment](#), [Air](#)



1 Executive Summary

This report discusses whether and how JetBlue should list its shares on public from several angles. Two principal incentives prove that the IPO process could be inevitable, even without an optimal offering price, and valuation models including multiples comparison and income analysis imply the firm may be underpriced. Given the situation and all assumptions, an increment in either offering size or price is suggested.

2 SWOT and Background

JetBlue started by following Southwest's approach of offering low-cost travel, but sought to distinguish itself by its amenities, such as in-flight entertainment, TV on every seat and Satellite radio. Barely two years after its foundation had the company made profit and decided to raise money through IPO. The initial price for JetBlue shares, as by potential investors, was \$22 to \$24. While facing sizable excess demand for the 5.5 million shares, management was considering an increase in the offering's price range.

3 Listing Analysis

Theoretically, firms acquire liquidity, monitoring and credibility after going public, and at the same time undertake all costs of time, money or loss of control and any further obligations and responsibilities. The general pros and cons for listing is shown in the table below.

According to the case, the two main reason drove JetBlue going public are: a) Staying in expansion; and b) Bailing out venture-capital investors. These two

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needs can be both significant and urgent, which could be the causative reason of listing above all other incentives. General advantages of listing

General disadvantages of listing

The low-fare-low-cost business model of JetBlue is a kind of “small profit but great quality”. The hi-tech equipment, huge compensation and all new Airbus A320s would heavily rely on the capital basis and the size. In other words, the bigger this firm is, the greater the economies of scale. Unlike nowadays low-fare airlines e. g. Tiger and Jet Star that minimize fixed costs and lower service, JetBlue managed to rise the quality of service and to “fix the sucks”, which was also not in concert with Southwest and other low-fare business, and all these fixings needed money.

Airline industry is a typical case of cost management. JetBlue had done pretty well in cost controlling by a) Flying to secondary airports; b) Single type of airplane; c) Frequent short-haul point-to-point service; and d) Advanced technology. But the shortest plank is in 2001 the Board didn't fully realize the importance of fuel price.

Given JetBlue's “supreme” model was so attractive to creditors and institutional investors as well as mom-and-dad investors, was there any choice to acquire capital with lower costs or higher proceeds than IPO? Was there a secondary offering? The key is: to what extent do the management and WPCs want to adjust the control power and capital structure. A degree of control, a healthy DE ratio like Southwest and a stable dividend policy should

be desirable in 5 years when JetBlue is able to settle down. But back to 2002, all the Board knew about was expansion, expansion, expansion.

Appendix 1:

The number of shares is calculated by dividing profit attributed to common shareholders by the diluted EPS from financial statements in 2001. The reason why we use diluted EPS rather than basic EPS is: as a new public company convertible preferred stock holders would take their rights as soon as possible given it is not forbidden.

Based on this assumption, we assume that in the first day all preferred stocks, which is also implied by Exhibition 13 in which preferred stock dividend is not counted while projecting the future NOPAT.

Notably, a problem may have occurred as in the footnote it is said the number of pre-money shares outstanding was 35.1m which is different from the amount computed from the financial report. ($\$21,567,000 / \$1.14 = 18.918\text{m}$)

Considering there is a time span for convertible shares, say 2 years after IPO, the market price still would not act as if the 53m net income in 2002 would be entirely allocated to 5.5m shares outstanding because the firm is unlikely to pay any dividend before the preferred shares are converted.

Appendix 2:

Another important assumption we made in this case is: the forecasting Exhibition 13 is reasonable and reliable. The future of JetBlue is believed to

boost as in 2002 the inflation of revenue per aircraft is to be rise 16%, which seems not quite practical. Meanwhile, the projecting failed to reflect the risk of price of aviation oil, which in turn became a huge threats to JetBlue's business model in 2005.

Appendix 3:

PS ratio is calculated by Price/EBITDA. By PS ratio rather than EBITDA multiple we try to figure out the profitability represented by market price rather than profitability itself. The formula is [1/4] in Exhibition 7.

Appendix 4:

In order to ensure the comparableness and meaningfulness, this data in PB model is from the estimation of 2002 although the PB ratio is not forwarding. And the 98m is by adding 80m EBIT and 18m Depreciation in 2002 forecasting.

Appendix 5:

The risk premium we use here is a historical risk premium rather than required (or expected risk premium) according to Aswath Damodaran in his journal ' Equity Risk Premiums (ERP): Determinants, Estimation and Implications - The 2013 Edition'. The required premium was lower than historical premium in 2001 as a representative of enthusiasms by the whole public in stock market. However, a higher historical risk premium could perform better in long-term analysis because it's obsolete but stable.

Appendix 6□

Appendix 7:

As mentioned before, the first 5 FCFFs are negative - that makes TV to be the most contributive factor to FCFF model, as can be seen below, we divide the discount rate for calculating TV by 2 and the current value of the firm increase from 875m to 3869m. Therefore the result of FCFF model clearly depends on the infinite WACC rate, which means the FCFF model is not reliable anymore.