

Airbus case summary

Business



**ASSIGN
BUSTER**

In the Airbus case we are faced with a capital budgeting decision. It is the planning process used to determine whether a firm's long term investments such as new machinery, replacement machinery, new plants, new products, and research development projects are worth pursuing. It is budget for major capital, or investment, expenditures.

Capital budgeting decisions are crucial to a firm's success for several reasons. First, capital expenditures typically require large outlays of funds. Second, firms must ascertain the best way to raise and repay these funds.

Third, most capital budgeting decisions require a long-term commitment. Finally, the timing of capital budgeting decisions is important. When large amounts of funds are raised, firms must pay close attention to the financial markets because the cost of capital is directly related to the current interest rate.

In the case of Airbus the company is facing the decision of developing the world's largest commercial Jet in order to compete on the very large aircraft market with Boeing 747. In order to calculate whether the investment is worth taking, a discounted cash flow analysis is used.

How many aircraft does Airbus need to sell in order to break even on its investment? After making some assumption and calculation of the Net Present Value, Airbus would need to sell about 45 aircrafts in order to break even. (Please see excel file).

If the Net present value is negative, then the investment is not worth taking and the project is not able to cover its investment. When the NPV is equal to

zero, it is the point at which the project will break-even. If the NPV is positive, the project is worth taking and it is able to cover all the investment costs and make a profit.

What is Airbus' maximum exposure in taking on the A3XX project?

Undertaking this project has very high risk, since the investment made by the company is very high. The maximum exposure that the company is taking on the project is to lose all the investments made up to now, which is approximately \$13 billion. This may lead to jeopardizing the future of the company and even bankruptcy.

Other problems that they might face are during the manufacturing process, they may have difficulty keeping up with the deadlines and thus this may lead to penalty fees for late deliveries of aircrafts.

This may cause a reduction in orders and customers turning to the competitors. Since there are significant risks involved in the situation, discuss at least 5 risk mitigation strategies that Airbus could undertake?

Developing the world's largest commercial jet may face significant risks, and for this reason Airbus should undertake mitigation strategies to cope with the risks. Some of those risks include: if Airbus is not being able to meet manufacturing deadlines, low demand for the aircrafts due to high prices and problems with suppliers.

What can Airbus do, well they could impose strict regulations on controlling the manufacturing process.

Airbus could make some discount for advance orders in order to stimulate demand. Establishment of good relationships with suppliers by trying to negotiate long-term contracts on prices and delivery. How do you expect Boeing to respond to a decision by Airbus to proceed with its It is very unlikely that Boeing will invest in the development of a competing aircraft since this decision is related to huge investments.

If Boeing wanted to make this nvestment they would not have withdrawn from the project in 1995, when Airbus and Boeing were working together on a feasibility study for the plane. It is possible that Boeing might take a decision to cut its prices on the Boeing 747 and compete with its existing plane, while for Airbus would be difficult to compete with the low prices since they have other cost to cover such as development, marketing, etc. This strategy may divert sales from the A3XX.

Ignoring the threat from the new Airbus aircraft would be also a possible solution for

Boeing since they have the power to compete with its existing planes and they can concentrate on the production of its existing product line. The development of a stretch version of the 747, was also a solution for Boeing, which is what they actually did. Boeing 747 got an efficient make over to challenge A3XX. The new 747-8 may look like Just another 747, but in addition to the new engines and swept wings, the new airplane is stretched more than 18 feet, increasing the volume by 16 percent. With the extra size and most importantly, extra efficiency Boeing may attract customers way from the Airbus A3XX.

But with a first flight still ahead of them, Boeing has some catching up to do.

In an effort to bring down those seat per-mile costs, and offer the maximum number of routes for the airlines, Boeing opted not to challenge the Airbus A3XX directly with a new super Jumbo. Instead, the company opted for the smaller, point-to-point efficiency with the 787 Dreamliner. But the company didn't want to give away the Jumbo Jet crown without a fight. So instead of developing an all-new airplane to compete in the relatively small Jumbo Jet market, the company decided to give the iconic 747 a makeover.

The new 747-8 is a stretched version of the most recent 747 model, the -400.

The extra space can accommodate 51 more seats than the -400. Though even with the new room, the new Boeing airplane still won't be able to carry as many passengers as the A3XX. So the A3XX will remain the king of the Jumbos for the foreseeable future. It will be the biggest airliner, carrying the most passengers of any airplane in the world. But when the new 747-8 lifts off the runway sometime soon, it might just demonstrate that you don't have to be the biggest to win the fight.