
Read the Case Study and answer all the questions that follow.

JETSAVE SPREADS ITS WINGS

Established in 1996, Jetsave Ltd is one of the new generation of UK based commercial airlines offering low cost flights to several European destinations. The business has grown rapidly during a period of rising consumer incomes, but further expansion into new routes is becoming more difficult due to lack of runway capacity in some major airports. The Chief Executive, Mike Parker, is considering diversifying into other travel-related operations. One plan is already well advanced – to offer car hire to air travellers. To save on costs only one model of car would be offered – a medium-sized vehicle. Bookings would be made only via the Internet or, if cars were available, on arrival at the airport.

Important issues still need to be resolved before the plan can be submitted to the other directors. Should the vehicles be leased or purchased? Which airports should be used as the first locations? How can the excellent staff-management relationships be maintained as the business expands into new areas of operation? Will the proposed marketing expenditure budget prove to be adequate?

Jetsave leases all of the aircraft in its fleet. However, the option of purchasing the 100 cars needed to set up the hire service is a real possibility. The manufacturer preferred by Jetsave as the sole car supplier is offering a 40% reduction off the list price per car of £15 000 if they are purchased outright. The vehicles will be retained by Jetsave for at least one year. Mike had calculated that 10% of the cost could be met from cash in the bank and the remainder would be borrowed.

The service will have to be popular and generate funds quickly. Further expansion will depend on a good public response and positive cash flows. The selection of the first airports for the new operation is therefore crucial. The busiest airports are the most expensive to set up a new office in. There is also more competition from other car hire companies. Due to the capital costs of establishing branches, it is possible that car hire will not be offered at all of the airports used by Jetsave.

Mike is concerned about the impact of the expansion on certain aspects of human resource management. His predictions, based on early sales forecasts for car hire, suggest that within two years the total workforce of the business could be doubled to 500. The excellent informal links that exist between management and staff, that make the entire workforce feel involved and important, might be lost with expansion through diversification. Currently, managers hold informal discussions with staff when an issue arises. Staff feel involved in issues that directly affect them as they are able to express their views freely to any of the managers. Perhaps a more formal system of participation will be required in the expanded business.

The car hire section of the business will be operated separately by a new division of the business with its own management structure. However, good communication between airline ticket sales, check-in desks and car hire will be essential to ensure a complete customer service. The staff at all airports in all divisions need to be seen to be working as a team to retain customer confidence.

Careful planning of the whole operation such as arranging office space, recruiting and training staff and preparing promotional material will be crucial, especially as the project will have to start by 1st April next year in order to attract the lucrative summer market.

Appendix A :

Forecast Balance Sheet for Jetsave before purchase of vehicles

| | (£000s) |
|--------------------------------|-------------|
| Non-Current Assets | 3000 |
| | |
| Current Assets | |
| Inventories | 100 |
| Trade receivables | 200 |
| Cash and cash equivalents | 120 |
| | 420 |
| | |
| Current Liabilities | |
| Trade payables | (400) |
| | |
| Net Current Assets | 20 |
| | |
| Non-Current Liabilities | |
| Loan capital | (1000) |
| | |
| Net Assets | 2020 |
| | |
| Equity | |
| Share Capital | 1520 |
| Reserves | 500 |
| | 2020 |

Appendix B

Estimated Annual Marketing Expenditure Budget of car hire companies

| | |
|------------|------------------------|
| Avon | £6 million |
| Hersch | £5 million |
| Betterhire | £2 million |
| Jetsave | £0.5million (proposed) |

Appendix C

Price Comparison of car hire – daily rate for medium sized car

| | |
|------------|--|
| Avon | £75 |
| Hersch | £74 |
| Betterhire | £65 (offices not open at all airports) |
| Jetsave | £60 (proposed) |

What does Jetsave's balance sheet tell us about the financial health of the business?

(5 marks)

Assuming the vehicles are purchased using the sources of finance suggested by Mike, How would this affect the balance sheet. Make sure you show all workings.

(8 marks)

Using the new balance sheet advise Jetsave on the suitability of these proposed sources of finance.

(12 marks)

Jetsave Ltd has set a marketing expenditure budget of £0.5million for the car hire division (Appendix B). To what extent might the success of Jetsave's car hire division be dependent on the level of its marketing expenditure budget?

(20 marks)