Bombardier, Inc.: The 3 Biggest Obstacles to its Turnaround Plan

Description

On Tuesday senior executives at **Bombardier, Inc.** (TSX:BBD.B) laid out a comprehensive plan for the company's turnaround.

The targets are certainly ambitious: they are targeting US$25 billion in revenue, 7-8% EBIT margins, and free cash flow equal to 80% of net income, all within five years. If Bombardier is able to achieve such numbers, shareholders should see enormous returns.

But this is far from a sure thing. We look at the company's three biggest obstacles as it embarks on its turnaround plan.

1. The balance sheet

Bombardier has US$6.5 billion of liquidity (which includes undrawn credit lines) as it heads into next year, which should be plenty to ensure its survival in the short term.

But over the next two to three years, the story changes very rapidly. Bombardier has roughly US$9 billion in debt and doesn't expect positive free cash flow until 2018. That year, the company has US$1.4 billion of debt due, and in the five years thereafter, there are another US$5.2 billion of scheduled repayments.

So even if Bombardier executes its turnaround strategy perfectly, it may still face a cash crunch. If there are any hiccups over the next couple of years (and history suggests there will be), then the news will be even worse.

2. Government involvement

As we all know by now, the government of Quebec has invested US$1 billion for a 49.5% in Bombardier's CSeries jet program. And the province's largest pension fund has invested another US$1.5 billion for a 30% stake in Bombardier Transportation.

These measures will help Bombardier in the short run. But as the years progress, this cash could actually be a major hindrance in two ways. For starters, the company needs to cut costs, which, in normal circumstances, includes mass layoffs. But Bombardier will face political pressure to preserve as many jobs as possible after taking government money.

Secondly, Bombardier's bailed-out status is not good for the company's brand, which could significantly affect order totals.

3. Market forces

Bombardier is counting on robust growth from both its aerospace and train-making divisions. But the company is facing some severe headwinds.

Regarding the train business, competition is heating up, especially from the Chinese. The country's two state-owned train-makers–CNR Corp. and CSR Corp.–have merged into CRRC Corp., and this new giant will be aggressively pursuing market share. CRRC also has a significant cost advantages over Bombardier Transportation thanks to its scale and its access to cheap labour.

On the aerospace side, Bombardier again faces intense competition. Making matters worse, the business jet market has softened significantly, mainly in countries such as China and Russia. As a result, the industry is dealing with significant overcapacity, and there is no sign of this trend turning around.

To be clear, it is still too early to write Bombardier off. Yet the company's turnaround plans will be very difficult to execute. If you're looking for a predictable stock, or one that will deliver immediate results, you should look elsewhere.

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