T4 – Part B Case Study Examination

For Examinations on 28 August and 21 November 2013

PRE-SEEN MATERIAL, PROVIDED IN ADVANCE FOR PREPARATION AND STUDY FOR THE EXAMINATIONS IN SEPTEMBER AND NOVEMBER 2013
INSTRUCTIONS FOR POTENTIAL CANDIDATES
This booklet contains the pre-seen case material for the above examinations. It will provide you with the contextual information that will help you prepare yourself for the examinations.
The Case Study Assessment Criteria, which your script will be marked against, is included on page 17.
You may not take this copy of the pre-seen material into the examination hall. A fresh copy will be provided on the examination day.
Unseen material will be provided on the examination day; this will comprise further context and the examination question.
The examination will last for three hours. You will be allowed 20 minutes reading time **before the examination begins** during which you should read the question paper and, if you wish, make annotations on the question paper. However, you will **not** be allowed, **under any circumstances**, to either begin writing or using your computer to produce your answer or to use your calculator during the reading time.
You will be required to answer ONE question which may contain more than one element.
For PC examinations only: Your computer will contain two blank files – a Word and an Excel file. Please ensure that you check that the file names for these two documents correspond with your candidate number.

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T4 Test of Professional Competence – Part B Case Study Examination

N – Multi-channel retailer case

N Company History

N Company (N) is a multi-channel retailer selling a wide range of goods through its online and bricks and mortar channels. It became a household name during the 1950's as a department store, so called because it was, and is, organised to sell a wide range of goods such as designer fashion, clothing, perfumes, furnishings, hardware, white goods, electronic products, computers, TVs etc. which are generally organised into departments within the store.

During its prime as a department store N had outlets in every large town and city of Country Z and was considered the leading retailer, being one of the first to develop a returns policy and to provide very good employment conditions for its front line staff.

Its strategy was one of differentiation through quality both in terms of the products it offered for sale and in the kind of service it offered to customers. Its target market was middle income customers who were prepared to pay a premium price for quality products and excellent service.

N's success in its home country Z, which is located in Europe (but outside the euro zone; the currency being the Z$), encouraged its management to extend its operations to markets abroad and it has established operations in countries across the world. During the late 1990's N became noted as one of the most profitable retailers in Country Z.

As N moved into the 21st Century it became clear that its once market dominance was over. A number of changes in the retailing environment occurred, most notably the growth of online retailing, (to which N responded much too slowly) and more dynamic competitors have quickly eroded N's market share.

The outcome of these changes was that N's revenues and profits fell significantly. In 2004, N's Directors bought out the Company. The Directors leading the buyout had to rely on support from the venture capitalist company 4J, and a number of other institutional investors which together took the majority of shares (80%) in the re-financed Company.

After a series of management changes and cost-cutting measures such as store closures and the sale and lease-back of stores, N's trading position was stabilised but with revenues and profits considerably below where they had been at their peak. During the years from 2005 to 2012, N attempted to keep pace with its competitors by introducing an online channel and bringing in new designers but it always seemed to be behind its major competitors.

Overview of N

N currently operates from a head office of about 2000 staff located in the north of Country Z. This is its main administration and distribution centre, which distributes to 6 regional distribution centres and then to the stores. It also has a small city office in the capital city of Country Z, which has been maintained as part of the Company's corporate image, dealing mainly with investor relations. An organisation chart is shown at Appendix 1.

Management information is provided by a variety of information systems. Sales information is provided by the bar-coding till systems which are directly connected to the head office and has for some time been the mainstay of management information. The daily sales have always formed an important part of the analysis of company performance.

Stock is controlled and issued through a separate system, with cost of goods being allocated to stores by category as and when delivered from the distribution centre. This is then held as store stock within the relevant department, until matched with sales by the till system. Payroll is operated by the HR function which also makes available relevant labour cost information for inclusion in the management and financial reports.

The compilation of the Store Performance Report (SPR) is achieved by consolidating the information from these systems. The SPR shows the sales per store and sales by product category within the store less the relevant direct costs, giving an indication of gross profit by category per store. After adding an apportionment for overhead costs, based on the floor area occupied by the departments, the overall performance of the departments and stores is measured. These reports are made available to store managers, forming an integral part of the management control process and are consolidated at product and regional level to enable both the individual store and the overall performance of the business to be assessed on a monthly basis.

N sells a wide variety of goods which are split into various product groupings. It has a total of 160 stores with a customer facing sales area of 1,114,800 square metres. A detailed analysis of the sales categories and the margins associated with them together with an analysis of current and forecast company performance can be found in the Finance Director's report to the Board (Appendix 2).

The majority of goods sold, 80%, are 'own bought', but like many department stores, N also welcomes concessionaires into its stores because they are another attraction that increases footfall. Concessionaires operate like shops within shops. These specialist retailers offer attractive goods such as high quality jewellery, expensive exclusive clothing and other desirable goods not stocked by the department store itself. They are usually granted the concession to sell within the store paying a fixed rental per square metre of space occupied or a percentage commission on the value of business generated.

On the retirement of the existing Chief Executive Officer (CEO) in late 2012 the Board, under the direction of 4J, agreed that it should seek out a chief executive who could take decisive steps to put N back amongst the leading competitors in the retailing industry. The Chairman of N welcomed Ms. Bilder as CEO. She came with a reputation as someone well known for her record in turning companies around.

Ms. Bilder found on her appointment that N faced a series of formidable challenges. Some of these challenges came from the changing retail environment, others derived from problems and weaknesses within N itself.

The developing industry context

Like other department stores which originated in the early twentieth century, N located its main stores in the central shopping areas of major towns and cities. This was advantageous at the time when railway lines, tram and bus routes converged on the city or town centre but became a disadvantage with the growth of car ownership, the increasing congestion in cities and the need for convenient car parking space.

The subsequent growth of out-of-town shopping centres with ease of access for cars and spacious car parking has led to the relative decline of many high street stores located in town centres as shoppers have preferred the convenience of shopping in the out-of-town stores. In order to compete therefore, N is faced with the problem of store relocation and the financial problems of coping with this change.

The growth of competition from other retail formats is one of the biggest challenges facing department stores like N. Once thriving and profitable, many are now struggling to compete with supermarkets and specialty shops. At the lower end of the market, the main threat is from supermarkets and hypermarkets while at the higher end of the market, specialty stores are significant competitors for N. New entrants from abroad, including companies from the USA as well as from Country Z's European neighbours provide an increasing international challenge.

One of the problems for department stores like N concerns the strategies that each company might adopt to fend off this twin group of rivals, one of which erodes its customer base with the offer of low prices, while the other out-competes them by offering fashionable specialty products.

It is important to note in this context that the room for manoeuvre for large retailers like N is limited by the competition policy of Country Z which seeks to prevent takeovers that might reduce competition between retailers in the same industry sector.

Faced with the saturation of their home market and the expansion restriction imposed on buying the market share of a competitor, large retailers like N have sought to expand their operations by moving into overseas markets. In some cases such moves have been successful but in others less so.

The key to successful overseas expansion seems to be in how to take advantage of the economies of scale that a multinational organisation enjoys while at the same time adapting to a different retail environment and customising the offer to consumers of a different cultural background.

Department stores are also challenged by shifting demographic structures especially in their own domestic markets. Senior age consumers with large disposable incomes are not only increasing their savings rates but are also shifting their spending towards goods and services not traditionally offered by department stores, such as health and well-being, home-improvement and entertainment products outside the home.

As this post Second World War generation of the customer population grows older, it is not being replaced by younger customers because this younger segment have developed different buying habits. Analysts claim there is a growing psychological disconnect among young shoppers who consider department stores to be old-fashioned and outdated. Today's younger generation shop at a mix of stores ranging from online, to discount, to niche specialty shops; all of which appear able to react faster to the latest trends and fashions in shopping.

The challenge for N and other department stores is to maintain their appeal to older affluent customers while improving their attractiveness to the younger generation of shoppers.

One of the most important changes in retailing in the last two decades has been the emergence of online retailing. Its impact, until quite recently, has been limited and some retailers have chosen to ignore it assuming that their existing strategy of providing the right products and good service in-store would allow them to continue much as they have always done.

Recent changes

During the festive season between the end of 2012 and the start of 2013 however, two developments occurred that signalled significant change in the retailing industry. One of these was the collapse of a number of bricks and mortar-only retail chains that specialised in the sale of particular categories of goods such as music, cameras and electrical goods. These retailers were unable to compete with Web-only retailers that did not have the expense of staffing, running and maintaining bricks and mortar stores.

The other development was a sudden increase in the rate of growth of online shopping. This was of particular relevance to N because although it registered an increase in online sales of 10 per cent over that enjoyed in the same period in 2011/2012, some of N’s department store competitors experienced increases in excess of 40 per cent with online sales making up to a quarter of their total sales. Even taking into account this exceptional seasonal effect on sales, such a rate of increase in growth was unexpected. The conjunction of these two developments provided a stark warning to bricks and mortar retailers which had not developed an online channel or had such a channel but which lacked the latest refinements.

These developments also led some retail analysts to forecast major changes in the retail landscape. In particular, the increased rate of growth of online retailing, has led to the claim that the purpose of the conventional retail store will need to be rethought, perhaps with some of the stores acting primarily as showrooms for online buyers. One implication of this, it is argued, will be the need for conventional retailers to reassess their store portfolios, both in terms of the number of stores and in the location of their stores. Predictions to date suggest a decline in the number of store outlets and a concentration of stores where footfall is greatest.

Mobile devices

One impetus for the recent growth in online shopping has been the increasing availability of affordable mobile devices such as the smart phone and the tablet that provide access to the internet. The improvement in the functionality and power of these devices has led to an upsurge in their purchase and use.

Aside from the many benefits of these devices for personal communication, social media, photography, direction finding and other benefits, these mobile devices are now increasingly used by shoppers whilst at home or in-store for a variety of shopping tasks. These include activities such as: browsing for goods other than the ones on showroom display, receiving promotional offers and other marketing material, viewing product reviews from other customers, searching online for lower prices elsewhere and using mobile devices made available by store personnel to pay for goods.

These benefits for customers, it is predicted, will lead to an even greater increase in the use of mobile devices whilst shopping and will require significant investment by retailers if they are to maintain their competitiveness. In particular retailers will need to ensure that wireless connectivity is available throughout their stores as a lack of the ability to use their mobiles in-store has been shown to lead to frustration for consumers and a loss of some sales. Such retailers will also need to make sure that their web pages are configured in such a way that they are as easily available to the mobile phone-user as they are for the conventional computer-user. Retailers will also have to ensure that their delivery of online purchases is as good, if not better, than that of competitors.

In this context it is also worth noting that the increase in mobile shopping is a global phenomenon not confined to the mature economies but is fast growing in emerging economies as the preferred way of online shopping. For multinational retailers the development of mobile devices that have wireless connection to the internet has enabled them to develop online channels in their overseas businesses more quickly and at lower cost than previously. With wireless technology, retailers no longer have the expense of cabling for internet connection but can install private Wi Fi (wireless) systems that allow wireless connectivity relatively quickly. Indeed the evidence is that major retailers are now investing large sums on bringing themselves up to date with best mobile technology practices in the industry both at home and abroad.

Challenge for retailers

There is however a particular challenge for retailers to ensure that their online channel, mobile channel and bricks and mortar channels are well integrated with each other so that customers who want to use a mix of channels can do so in a seamless manner. So whether customers order goods by their mobile, online from their computer or in person at the store, he or she can have goods delivered or collect them in-store at his or her convenience.

Other associated problems of adopting an online channel include questions of customer security and protecting the integrity of the customer’s personal information during the online transaction process. Another problem for retailers is how to ensure continuation of service if a technical problem occurs in the retailer’s computer systems.

Finally it is important to note that the on-going economic recession in Country Z and the associated squeeze on family budgets is a major problem for retailers like N. The eurozone problems inevitably have a depressing impact on Country Z’s economy and this together with the fierce competition N is experiencing in its home market is another reason for it to consider the expansion of its international business.

Review of N’s operational activities.

Soon after her appointment as CEO, Ms. Bilder gathered the executive team of N together in order to conduct a review of N’s current activities.

Ms. Bilder introduced the review with a description of her previous record in helping the turnaround of several companies, one of which had been a large retail organisation, before proceeding with an outline of what she perceived to be the existing position of N while listing some of its key problems and the challenges it faces.

Drawing on her experience of turning companies around, Ms. Bilder felt that one of the weaknesses, common to all these companies, had been their inadequate management of risk. Few of them had had contingency plans in place and when the economic downturn came along they were completely unprepared for it. She added that she did not intend N to be unprepared for future risks.

Her own view, based largely on the financial statements and Finance Director's report (Appendix 2) was that although the decline in the Company's performance had slowed down, and that N remained profitable, the current performance was a long way below that of the 1990's when profitability outperformed that being presently achieved.

She went on to acknowledge the profound changes that had taken place in the retail industry since the 1990s, many of which had made competition in the industry fiercer than ever. She ended on the optimistic note that N had a great past as one of the founding giants of retailing in Country Z and was capable of seizing leadership in the industry once more.

She then invited the directors comprising the executive team to provide an update on how their particular area of responsibility was performing. Ms. Bilder made it clear that she was interested in how N stood in relation to its competition and in particular the strengths and weaknesses of the Company as compared with its key competitors.

Updating from senior executives

Sales and Marketing

The Sales & Marketing Director opened the presentations with an apology for some mistakes, most notably certain sales which had fallen short of expectations in the recent past. Ms. Bilder quickly set the tone for the meeting by stating that she was looking for analysis not excuses.

He quickly recovered and gave a polished PowerPoint presentation of how his team had performed in the recent past together with its main successes and occasional failures. In particular he emphasised N's success with own brand products, adding that this was partly due to recessionary times as consumers struggled to meet the rising cost of living, particularly for transport and winter heating.

N already had a fairly high proportion of own brands (60%) and he felt that this was a good time to increase the number of N's own brands since there was a higher margin on these than on the sale of branded goods.

He also noted that some of N's competitors who were selling white and electrical goods had managed to persuade manufacturers to produce own brand goods for them and wondered if N should do the same.

The Sales and Marketing Director emphasised the importance of maintaining and possibly increasing the marketing budget in order to maintain the Company image and the constant requirement to remain ahead of the competition, particularly in relation to clothing sales which accounted for 45% of total sales in the year to 31 March 2013.

Also of major concern is the rapid increase in the industry of online business, and the fact that the Company is not well equipped to take advantage of this ever increasing trend. Many of the store managers are reporting customers browsing and inspecting goods in the stores, but not buying. A rapid and effective expansion of this aspect of the business is urgently required, in terms of improvements in the online order processing systems and improvements in the online customer interface. Marketing campaigns will be needed to improve customer awareness of the enhanced multi-channel experience.

IT and Logistics

The IT and Logistics Director was the next to speak. His was a dazzling performance illustrated with a range of charts and diagrams. Much of what he had to say went over the heads of his audience but the following important points emerged from his presentation.

First he explained some of the problems that had arisen from the way in which N managed its multi-channels. Customer surveys clearly indicated that the present structure of N in which the online channel, the mobile channel and the bricks and mortar channel all operated independently did not provide the desired customer experience.

Customers ordering online were unable to pick up products from many of the bricks and mortar outlets or return unwanted goods to them. Also the system allowing customers to use their smart-phones to order products while on the move was not yet up and running and younger consumers in particular found this irritating.

By contrast, several of N's major competitors had seamlessly integrated the management of their channels so that customers could order online and collect in-store, (click and collect). They could order using their internet based devices, tablets and smartphones at their convenience and arrange for delivery direct to their home or collect from a store of their choice.

The competitors' integrated multichannel structure and technology also allowed any returns to be collected by courier or to be returned to a store. One of the advantages of customers being allowed to pick up and make returns to stores was that customers were often attracted to purchase other products while visiting the store.

Other problems noted during the IT and Logistics Director's presentation included those relating to the back office logistical problems involved in ensuring smooth and reliable delivery of products from manufacturer and supplier to N's central and regional warehouses and then to their stores on time and in the required quantity. A number of stock-outs during the periods running up to seasonal national celebrations had proved financially damaging and embarrassing for N and highlighted the urgent need for modernisation of the product ordering and communication system.

Although the introduction of N's online channel had gone smoothly and online sales achieved 3.2% of total revenue in the year to 31 March 2013, competitors' online sales were increasing far more rapidly with comparable figures of typically 8-10% of their total revenue and with plans to double this in the medium term.

Human Resources

The HR Director believed that the excellent customer service which had formed one of the cornerstones of N's competitive strategy had continued to be a differentiating factor but competitors were catching up fast. She also believed that it was as essential to train local managers and corporate staff working in overseas subsidiaries as comprehensively as staff in the home country if N's corporate brand was to be successful in its international businesses.

Estates Management

The Estates Management Director was pleased to report that the modernisation programme for existing stores was going well and he expected that the timetable as set out two years ago would be met for all refurbishment completions. On the matter of store closures he expressed regret that a number of stores in the smaller towns of Country Z had been closed because sales had been falling year-on-year. A study of the demographics suggested there was no realistic possibility of such stores returning to profit.

He was happy to report however, that two out-of-town flagship stores had recently opened on time and early indications suggested that shoppers found them to be very attractive. Sales were going very well and this was an encouraging development especially as another similar flagship store was due to open in City T in the west of Country Z in the coming months.

Prompted as to what other formats N might adopt other than flagship stores and the existing smaller department stores in major towns, the Estates Management Director suggested that N might consider opening convenience stores of the type already offered by some of its competitors. Some of the present department stores, in the smaller towns for example, might be downsized to become convenience stores stocking food and other everyday requirements while others might be opened on the auto-routes that cross Country Z.

His final point however, was the most important. He had been in discussion with the IT and Logistics Director and they had agreed that N's coverage of the country was limited if the trend for the 'Click and Collect' multi-channel activity continued to grow. Compared with competitors, they felt N had too few stores on the perimeter of big towns and cities where parking facilities were more readily available and where out-of-town retail parks already attracted an increasing volume of shoppers each week.

International Operations

The International Operations Director began with an overview of N’s performance in overseas markets. This presented a mixed performance: N’s priority markets of Asia and the Middle East are performing well. In North America and Europe trading conditions were more challenging and performance was less positive. He noted with regret the closure of some stores in Europe.

He then went on to remind his colleagues that N had recently introduced a new structure for the management of its global operations in which the business had been divided into four regions; Europe, Asia, North America and the Middle East. A general manager had been appointed to lead each region together with a head of business development to drive growth. He felt that this new structure would enable greater focus on emerging markets, and whilst there were considerable up-front costs associated with these developments he felt that this would be well worth the investment in the longer term.

Looking to the future he confirmed that N was seeking to expand its international business especially in emerging markets as these showed the greatest potential for future growth. Its principal mode of entry would be by a series of franchises with suitable partners but he noted that in some cases, N would look at the acquisition of existing retail stores and even build new stores. He added that an investigation into the best strategy for competing in particular foreign markets would be necessary as a means of assessing advantages and possible risks.

Procurement

The Procurement Director began by making clear that the updating of N’s procurement policies, procedures and technology while making progress had still some way to go and that in some respects was less effective and efficient than that of its main competitors.

With regard to commodity prices, the price of cotton was a major concern as this had more than doubled in recent years as a result of poor harvests and rising demand from the Chinese domestic market. This had also resulted in increases in wool and polyester prices.

He also noted that procurement policy in N had swung back and forth between that of fostering good and long standing relationships with a few large suppliers and the alternative of shifting between large numbers of different suppliers according to what N considered was the best offer at a particular point in time.

The Procurement Director agreed with his colleague in IT and Logistics that N’s information and communications systems needed urgent attention if merchandise was to be shipped to distribution centres and stores as efficiently as its leading competitors.

Merchandising

The recently appointed Merchandising Director began by thanking her colleagues for the warm welcome she had received from members of the executive team on taking up her appointment. Her brief on appointment had been to review all of the merchandising activities but with a particular focus on women’s clothing. She was in the early stages of her review but had already come to a number of conclusions. She welcomed the exciting new look of the modernised stores and felt that the atmospherics ideally suited the kind of clientele N was seeking to attract.

She also felt that N was targeting the right market segment and felt that it had most of the skills and competences to meet the fashion aspirations of the women in the age range 25-45 which N targets. She was disappointed however, with the existing product assortment and pointed out that the racks of unsold garments in the recent seasonal collection demonstrated clearly that N was not meeting the expectations of even its most loyal customers. On inspection, she had found huge gaps in the range of clothing offered. In particular there were no petite sizes, no larger sizes and the clothing offered did not look fashionable.

She was also surprised by the differences in average lead time between N and its leading competitors in delivery of garments from manufacturer to distribution centre and then on to stores. It took N's suppliers 20 weeks to manufacture and deliver fashion items to stores as compared with a lead time of 12 weeks for N's main competitor. She had already been given the go ahead to make drastic changes including a training programme for all of N's buyers and faster overnight deliveries of fashion garments from distribution centres to stores to speed up delivery. In addition, she also proposed to the Procurement Director that a switch be made to new suppliers.

Finance

The Finance Director gave the last presentation summing up the observations of all her colleagues, explaining how these were reflected in the financial performance of the company.

Talking through her report (shown in Appendix 2) which had been circulated to the board, the essential points were that while N remained profitable, it was not keeping up with competitors in terms of sales growth, particularly in the more recent on-line order and collect business. Cost pressures continued in all areas but particularly in distribution as a result of increased fuel and road usage charges and in the administration of the business as warehouse distribution management became increasingly expensive. She went on to emphasise that with the sales figures as described it was essential that the forecast costs be kept to plan.

Also with regard to the financing of the business, the original buyout agreement envisaged that the venture capitalists and all other shareholders would forgo dividends for a period in order that profits were reinvested in the business. This period had now come to an end with the payment of a dividend of Z$ 50.0 million in the current year. Similar dividend pay-outs are expected in future years.

She also pointed out that the revolving bank finance agreement of Z$ 600.0 million will require renegotiation in 2016. Care will need to be taken with cash forecasting and investment decisions.

Glossary for N Case

Atmospherics/ambience - store factors such as display, design, fixtures, flooring, smell, sound, lighting, temperature, wall coverings, which can be controlled by a retailer to influence the consumer's buying mood.

Bricks and mortar - businesses that have a physical (rather than virtual or online) presence - in other words, stores (built of physical material such as bricks and mortar).

Concession - the right granted to a retail business to sell goods within another establishment. The owner of the concession - the *concessionaire* - pays either a fixed sum or a percentage of revenue for the rights to do so.

Flagship store - a large store in a prominent location, (often a major city) that holds or sells the highest volume of merchandise in the chain.

Footfall - the number of people visiting a shop or a chain of shops in a period of time.

Mobile channel – refers to the use of mobile devices such as Smart Phones, Tablets and the like to investigate availability of goods, to compare prices, view promotions, order and pay for goods and arrange delivery whenever and wherever the customer happens to be, at home or on the move.

Own-bought goods – goods purchased by the company for resale, maybe branded or own label.

Own-label goods – goods manufactured by the original manufacturer but sold under the N company label.

Retail format - refers to the retail mix in terms of range of products and services, pricing policy, promotion, operating style or store design and visual merchandising.

Returns policy - a policy which allows the customer to return a product if not satisfied with it within a certain period of time, subject to the policy of the retailer.

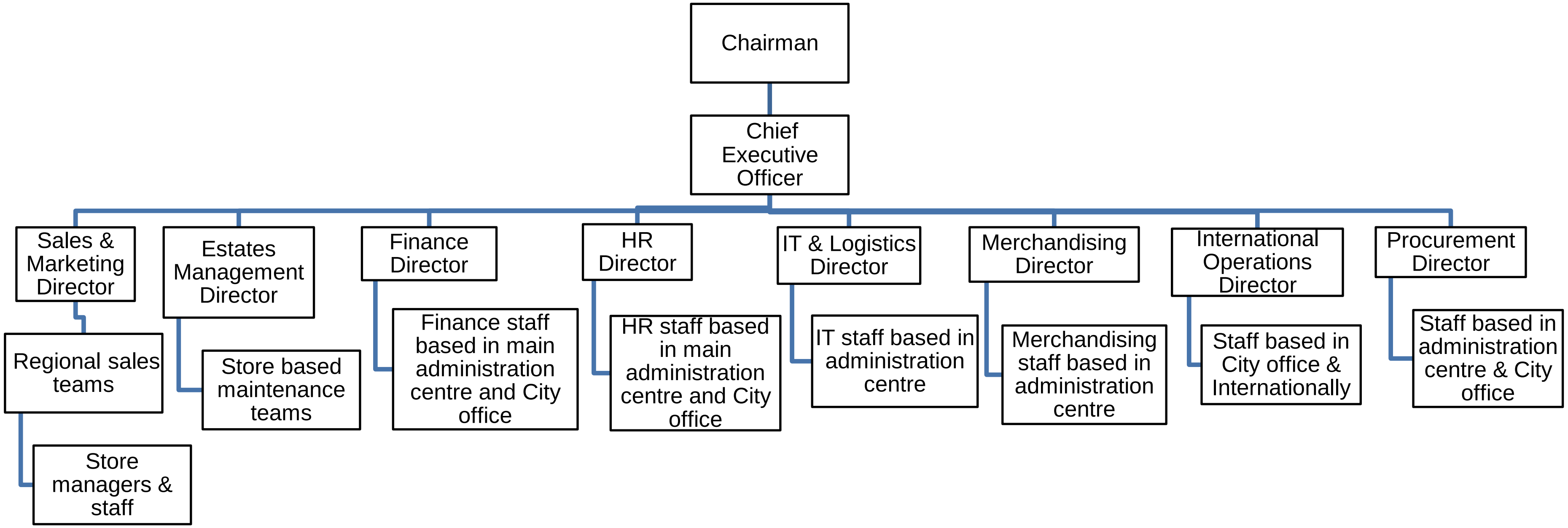
Revolving credit facility – a credit facility which has an agreed upper limit available for an agreed time period and which will fluctuate with the cash requirements of the company. An arrangement fee is usually charged and incorporated in the balance due.

Specialty store - refers to a retail store that offers specific and specialised types of item. These stores focus on selling a particular brand, or a particular type of item, for example, one that sells only smart phones. Sometimes it includes chain retail stores that sell a specific brand of clothing.

Web-only retailers - use the Internet as their primary means of retailing as contrasted with bricks and mortar retailers which use the Internet to promote goods or services but also have the traditional physical stores available to customers.

Appendix 1

Organisation Chart of N as at 31 March 2013



Appendix 2

Finance Director's report to the Board for the year ended 31 March 2013.

The business has faced another challenging year. Revenue has increased by Z$ 49.5 million or 2.5% on the year, to Z$ 2,029.9 million (2012: Z$ 1,980.4) which takes into account the new stores opened but it is not keeping pace with competitors which are achieving increased revenues of almost 4.0%. N has sales per square metre (sq. m.) of customer-facing floor area of Z$ 1,820.86, (total floor area 1,114,800 sq. m.) which is considerably less than our major competitors, which are achieving over Z$ 1,900 per sq. m. Cost of sales including purchases, employee and other operating costs are 86.7% of sales resulting in a gross profit for the year of Z$ 270.0 million, 13.3% of sales value (2012: Z$ 263.4 million, also 13.3% of sales value). Extracts from the current year, and forecast are attached.

Distribution costs of Z$ 64.9 million increased by 13% over the year (2012: Z$ 57.4 million) as a result of increased fuel and transport operating costs. Administrative expenses increased by 2.5% to Z$ 40.6 million for the year (2012: Z$ 39.6 million). This has resulted in a lower operating profit in 2013 of Z$ 164.5 million (8.1% of sales as compared to 8.4% in 2012.)

Finance costs of Z$ 15.0 million have reduced slightly (2012: Z$ 16.0 million) as the business has reduced the loan finance position net of cash from Z$ 665.5 million to Z$ 592.9 million. After some lengthy discussions with 4J and other institutional shareholders it was agreed that a dividend be paid of Z$ 0.50 per share totalling Z$ 50.0 million.

The revolving credit facility with the bank of Z$ 600 million, excluding the arrangement fee, will require renegotiation in 2016. Accurate cash monitoring and planning and backing from shareholders will be vital to a successful outcome.

The enclosed forecast for 2014-2016 is based on current performance and cost relationships continuing into the immediate future with distribution costs increasing by 10% year-on-year and finance costs remaining static.

Because of this and sluggish sales growth, the forecast indicates that N will experience declining profitability over the 3 year period. It is essential that there is further investment in areas such as on-line sales channels, with customers able to easily pick up or return goods. Also an improvement in margins through increasing own branding and a thorough administrative review are required to improve on the forecast position.

While the operational cash position remains manageable, the funding of investments required to develop the business will require careful planning and consideration.

Extract from Published Statement of Profit or Loss for N for the year ended 31 March

	2013 Z$ million	2012 Z$ million
Revenue	2,029.9	1,980.4
Cost of sales	1,759.9	1,717.0
Gross profit	270.0	263.4
Distribution costs	64.9	57.4
Administrative expenses	40.6	39.6
Profit from operations	164.5	166.4
Finance costs	15.0	16.0
Profit before tax	149.5	150.4
Tax	41.9	42.1
Profit for the year	107.6	108.3

Statement of Financial Position of N as at:

		31 March 2013		31 March 2012	
	Note		**Z$ million**		**Z$ million**
Assets					
Non-current assets					
Property, plant and equipment	1		**941.2**		**935.5**
Current assets					
Inventories	2	461.7		455.2	
Trade and other receivables		101.3		90.5	
Cash and cash equivalents		147.2		61.7	
			710.2		**607.4**
Total assets			**1,651.4**		**1,542.9**
Equity and liabilities					
Ordinary share capital issued		100.0		100.0	
Share premium		250.0		250.0	
Retained earnings		232.6		175.0	
Total equity			**582.6**		**525.0**
Non-current liabilities					
Loans and borrowings	3	530.1		605.6	
Total non-current liabilities			**530.1**		**605.6**
Current liabilities					
Loans and borrowings		210.0		121.6	
Trade and other payables		286.8		248.6	
Tax payable	4	41.9		42.1	
Total current liabilities			**538.7**		**412.3**
Total equity and liabilities			**1,651.4**		**1,542.9**

Note:
1. Assets are at net values after charging depreciation.
2. Consists of items held for resale.
3. Represents the outstanding balance of the revolving credit facility, including the arrangement fee.
4. The tax rate is 28%.

Note: Paid in share capital represents 100,000,000 shares of Z$ 1.00 each at 31 March 2013

Statement of Changes in Equity For the year ended 31 March 2013	**Share capital**	**Share premium**	**Retained earnings**	**Total**
	Z$ million	**Z$ million**	**Z$ million**	**Z$ million**
Balance at 31 March 2012	100.0	250.0	175.0	525.0
Profit for the year	-	-	107.6	107.6
Dividends paid	-	-	(50.0)	(50.0)
Balance at 31 March 2013	**100.0**	**250.0**	**232.6**	**582.6**

Statement of Cash Flows for N for year ended 31 March 2013

Cash flows from operating activities	Z$ million	Z$ million
Profit before tax		149.5
Adjustments		
Depreciation	88.0	
Finance costs	15.0	103.0
Movements in working capital		
(Increase)/decrease in inventories	(6.5)	
(Increase)/decrease in trade receivables	(10.8)	
Increase/(decrease) in trade payables	38.2	20.9
Cash generated from operations		273.4
Finance costs (net paid)	(15.0)	
Tax paid	(42.1)	(57.1)
Net cash from operating activities		216.3
Cash flows from investing activities		
Purchase of non-current assets	(93.7)	(93.7)
Cash flows from financing activities		
Dividend paid	(50.0)	
Increase in loans and borrowings	12.9	(37.1)
(Decrease)/increase in cash and cash equivalents		85.5
Cash and cash equivalents at the beginning of the year		61.7
Cash and cash equivalents at the end of the year		147.2

N: Product Sales and Profitability Analysis for the year ended 31 March 2013

		Sales	Cost of Inventory	Gross Margin
	% Sales	Z$ million	Z$ million	Z$ million
Womenswear	22.5	456.7	174.3	282.4
Menswear	14.0	284.2	88.1	196.1
Childrenswear	8.5	172.5	66.3	106.2
Health & Beauty	24.0	487.3	299.1	188.2
Accessories	10.5	213.1	85.2	127.9
Home (Household)	20.5	416.1	312.1	104.0
Total	100.0	2029.9	1025.1	1004.8

The following costs have been included in arriving at cost of sales:

	2012/ 2013 Z$ million	2011/2012 Z$ million
Cost of inventory	1025.1	1010.0
Employee costs	308.0	305.6
Staff development and training	25.0	25.0
Depreciation	88.0	85.0
Maintenance	35.2	34.0
Rental charges	90.2	86.8
Energy costs	38.4	35.6
Advertising and promotion	150.0	135.0
	1759.9	1717.0

Forecast Statement of Profit or Loss for N for 2014-2016

Year to 31 March	**2014** **Z$ million**	**2015** **Z$ million**	**2016** **Z$ million**
Revenue	**2,080.6**	**2,132.6**	**2,185.9**
Cost of sales	1,803.9	1,849.0	1,895.2
Gross Profit	**276.7**	**283.6**	**290.7**
Distribution costs	71.4	78.5	86.4
Administrative expenses	41.6	42.6	43.7
Profit from operations	163.7	162.5	160.6
Finance costs	15.0	15.0	15.0
Profit before tax	**148.7**	**147.5**	**145.6**
Tax	41.6	41.3	40.8
Profit for the year	**107.1**	**106.2**	**104.8**

Assessment Criteria

Your script will be marked against the T4 Part B Case Study Assessment Criteria shown below.

Criterion	**Maximum marks available**
Analysis of issues (25 marks)	
Technical	5
Application	15
Diversity	5
Strategic choices (35 marks)	
Focus	5
Prioritisation	5
Judgement	20
Ethics	5
Recommendations (40 marks)	
Logic	30
Integration	5
Ethics	5
Total	**100**

End of Pre-seen material