ESlog - MODULE A :
BUSINESS PRINCIPLES

CONTENTS:

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ESlog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.01 *The financial impact of holding inventory*

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6.1.01.01 The financial impact of holding inventory

A. Inventory as financial asset

Inventories include value because we have spend money to build them. Also, because the inventory will create value (income) to the company after it is transferred to finished products ready to sell.

Also they create a cost which is the cost of money we invested and probably we borrowed by a bank at an interest rate

Inventory value = Quantity X Unit purchase price

Financial cost = Quantity X Unit purchase price X Time X Interest rate

6.1.01.01 The financial impact of holding inventory

A. Inventory as financial asset

B1. Financial cost of inventory

= **Inventory (value in E) * capital cost (%)**

It is the cost of the capital which we spend to buy the inventory and is blocked there until the inventory is sold as ready product

This cost depends on :

a. The **Quantity** of the stock
b. The **unit cost** of the inventory (the production cost – if produced internally or the purchase cost – if are procured from a supplier)
c. The **duration** the inventory is in the warehouse
d. The money borrowing **rate**

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory

B1. Stock financial cost

Exercise A:

A wine cellar has 1000 bottles of wine produced at a sale price of 4 E / bottle (with overhead costs of 10% and a profit of 20%) and 3000 bottles of juice purchased for resale purchased to resale, at a purchase price of 2 E / bottle. The average stay in the cellar is 4 months for wines while for juices only 20 days The company has an average borrowing cost of 5%

What is the cost of the committed capital for the stock?

1000X0.7X4X(4/12)X5%+3000X2X(20/30)X(1/12)X5%= 233+16 = 249 E

What steps would you take to reduce your financial costs?

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory

B1. Stock financial cost

Exercise B:

A company buys a bulk product and packages and markets it.
It has an average stock of raw material of 100 MT with an acquisition value of 5 E / Kgr which has an average renewal cycle of 50 days and an average stock of finished products of 60 MT with a sale price of 10 E / kgr, which remains on average 20 days in the Warehouse ready. Profit and overhead is 35%. The lending rate of the company is 9%.

α. What is the value of raw material stocks?

β. What is the value of stocks of finished products?

γ. How much is the cost of keeping stocks?

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory
B1. Stock financial cost

Exercise Γ:
The company trades 3 products with an acquisition value of 20, 50, 100 E per piece. The average stock is respectively 5000, 3000, 2000 pcs, with an average stay time in the warehouse ready 20, 15, 10 days. Borrowing costs 9%

α. How much is the total financial stock cost?

b. Which product would you start with to reduce costs?

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory
B2. Non-Financial stock cost
B2.1. Warehousing

Includes the costs of ownership and operation of the Warehouse.

Such costs are :
- Rents, leasing, depreciation
- Wages of storekeepers, dredgers, Clark drivers, workers, etc.
- Energy Costs (Heating, air conditioning, lighting, etc)
- Fuel costs Clark
- Warehouse maintenance costs, vehicles, equipment
- Municipal taxes
- Consumables, cleaners, packaging, etc.

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory

B2. Non-Financial stock cost

B2.2. Obsolescence

It is the state in which a product transitions the service is no longer requested even if it is in good working order.

B2.3. Pilferage

It is the theft of part of the contents of a package.

A special case is the replacement of the removed product with fake materials.

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6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS
B. Cost of capital associated with holding inventory

B2 . Non-Financial stock cost

B2.4. Damage

The value of the products destroyed

B2.5. Insurance

The cost of insuring the warehouse against the risks of fire, theft, earthquake, etc.

Also the cost of insurance of stored products

B2.6. Tax

Various taxes related to the ownership or operation of the Warehouse, such as: Property taxes, Municipal taxes, etc.

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6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

C. Inventory decrease

C1. Cash release

Reducing inventories releases cash thereby increasing the liquidity of the business.

Exercise :

The stocks of a business are:

a. Raw materials: 30000 Kgr unit cost 2 E

b. In production process: 5000 kgr unit cost 3 E

c. Finished products: 20000 kgr unit cost 4 E

d. In stock at dealers: 30000 kgr unit cost 5 E.

They are asking you to release 50000 E cash by reducing stocks. You are digging to ask all stages to reduce the quantities by the same percentage. What should this be?

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

C. Inventory decrease

C2. Revenue release

Reducing stocks that are tied to inventory creates available funds that can be allocated to promotion, sales network development, discounts, campaigns, etc. that will increase sales and revenue.

Exercise:

You are Warehouse Mgr. and ask you to reduce stocks of 100000 E by 20% to fund an annual promotion program for an existing product. Your own data show that with the reduction of inventories there is a possibility of losing sales of 50 pcs / month with a gross profit margin of 100 E. The cost of the campaign is estimated at 20000 E. The cost of borrowing is 9%. Calculate the percentage of sales growth that must be achieved for the next 12 months, to be the breakeven program

6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

D. Inventory increase

D1. Cash is tied up

An increase in stocks creates an increase in capital committed to stocks.

Exercise:

To cover a promotional plan, the Sales Manager asks you to increase your finished product inventory by 50%. The CFO asks you what additional impact this will have on the committed capital.

What data will you need and what calculations will you need to do?

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6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

E. Inventory write up

When can a stock be deleted:

1.When the product is damaged, its quality deteriorates

2.When the product is lost or stolen

3.When the sale price of the sale falls below the value entered in the stock account.

•In case of **sale the difference is deleted**

•Usually **a reserve** (contra account) account is created for the planned deletions. The amount is budgeted based on historical write-off data.

•Deletion is credited to the **"Inventories"** account and debited to the "Cost of Sales" account

•The deletion should be **done at once** when the need is identified and not partially or in different years.

•It may be **delayed for a short time** that the Procurement Department needs to do market research, find a sale price, tender, etc.

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6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

E. Inventory write up

E1. Impact on cash

Exercise:

Mention and explain if and what effect it has on cash:

a. The case of deletion

…………………………………………………………………………………….

β. The case of sale at a price

…………………………………………………………………………………….

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6.1.01.01 ECONOMIC IMPLICATIONS OF STOCKS

E. Inventory write up

E2. Impact on Profit & Loss

Cost of Sales = Opening stock + Purchases - Closing stock

Profit / loss = Revenue from sales - Cost of goods sold +/- ……

When inventory is deleted,

⇨ *the closing stock is reduced,*

⇨ *thus increasing the cost of sales,*

⇨ *so profits are reduced*

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ESlog - MODULE A :

BUSINESS PRINCIPLES

6.1.01.02 CASH TO CASH CYCLE

Understands cash to cash (C2C) cycle

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6.1.01.02 Cash to Cash Cycle

Balance sheet

Balance sheet example

TEDDY FAB INC.
BALANCE SHEET
December 31, 2100

ASSETS	
Current assets	
Cash and cash equivalents	$ 100,000
Accounts receivable	20,000
Inventory	15,000
Prepaid expense	4,000
Investments	10,000
Total current assets	149,000
Property and equipment	
Land	24,300
Buildings and improvements	250,000
Equipment	50,000
Less accumulated depreciation	(5,000)
Other assets	
Intangible assets	4,000
Less accumulated amortization	(200)
Total assets	$ 472,100

LIABILITIES AND SHAREHOLDERS' EQUITY	
Current liabilities	
Accounts payable	$ 30,000
Notes payable	10,000
Accrued expenses	5,000
Deferred revenue	2,000
Total current liabilities	47,000
Long-term debt	200,000
Total liabilities	247,000
Shareholders' Equity	
Common stock	10,000
Additional paid-in capital	20,000
Retained earnings	197,100
Treasury stock	(2,000)
Total liabilities and shareholders' equity	$ 472,100

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6.1.01.02 Cash to Cash Cycle

A. Working Capital or Net Working Capital

A1. Working Capital connect with Supply Chain

$$Net\ Working\ Capital = Current\ Assets - Current\ Liabilities$$

- Cash
- Demand deposits
- **Inventories**
- Bills Receivable
- Receivables from Sale

- **Debts to Prophets**
- Various Creditors
- Lines payable
- Debts in taxes, fees, liquidation funds

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6.1.01.02 Cash to Cash Cycle

A. Working Capital

A1. Working Capital connect with Supply Chain

Net working capital

They are the cash and items that can be converted into cash in the short term (one year) (eg, stocks, cash, bills receivable less short-term liabilities to suppliers). The Company uses its net working capital to measure cash flows and its ability to service its liabilities. A positive net working capital means that the company has money to maintain or expand its operations. The net working capital does not add to the assets of the company but supports its daily operation.

<u>QUESTION</u>: What components of the NWC are related to the supply chain?

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6.1.01.02 Cash to Cash Cycle

A. Working Capital

A1. Working Capital connect with Supply Chain

Current Ratio (CR)

Current Ratio = Current Assets / Current Liabilities

Av CR > 1 ⇨ Positive WC
Av CR < 1 ⇨ Negative WC

(The company will find it difficult to pay its suppliers, in the long run if low CR prices continue it may lead to bankruptcy)

Av CR > 2 ⇨ The company does not invest its funds
Av 1.2 < CR < 2 ⇨ It is considered satisfactory

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6.1.01.02 Cash to Cash Cycle

A. Working Capital

A1. Working Capital connect with Supply Chain

Quick ratio

Definition

- A measure of a company's liquidity and ability to meet its obligations.
- Quick ratio, often referred to as acid-test ratio, is obtained by subtracting inventories from current assets and then dividing by current liabilities.
- Quick ratio is viewed as a sign of company's financial strength or weakness (higher number means stronger, lower number means weaker).
- It means that for every dollar of current liabilities there are three dollars of easily convertible assets. In general, a quick ratio of 1 or more is accepted by most creditors; however, quick ratios vary greatly from industry to industry.

For example, *if current assets equal $15,000,000, current inventory equals $6,000,000, and current liabilities equal $3,000,000, then quick ratio amounts to: ($15,000,000 - $6,000,000)/$3,000,000 = 3.*

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6.1.01.02 Cash to Cash Cycle

A. Working Capital

A1. Working Capital connect with Supply Chain

Balance sheet example

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Less accumulated amortization		(200)
Total assets	$	472,100

LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
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Treasury stock		(2,000)
Total liabilities and shareholders' equity	$	472,100

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6.1.01.02 Cash to Cash Cycle

A. Working Capital

A2. Ways to Reduce Working Capital

- **a. More vendor payment days**
- **b. Stock management by Suppliers**
- **c. Decrease in stocks**
- **d. Simple Supply Chain**
- **e. Fewer customer credit days**

6.1.01.02 Financial terms

B. Results of the Year (Profit & Loss Statement)
It is the financial situation that dynamically and concisely shows the accounting result that the company realized during a period as well as its analysis.

Operating result = Gross result (sales - cost of goods sold) + Operating income - Operating expenses

Accounting period result = Operating result + Extraordinary and inorganic income / extraordinary profits - extraordinary and inorganic expenses / extraordinary losses

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6.1.01.02 Financial terms

C. Cash Flow

C1. Definition: Cash flows, or cash flows, are the amounts of money that enter (inflows) and outflows (outflows) from a business in a specific period of time. That is, they are all kinds of receipts and payments made by the company.
The income of a company is positive cash flows, while the expenses, respectively, are negative cash flows.
The difference between positive and negative customers reflects net cash flows.
C2. Data for the preparation of the Financial Statement
For the preparation of the cash flow statement it is necessary to know the following Sizes:
- The total investment capital
- Annual expenses (fixed and proportional operating expenses, interest, amortization, income tax, additional capital disbursements, etc)
- Annual revenue
- Annual depreciation

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6.1.01.02 Financial terms

C. Cash Flow

C3. Usefulness of the Financial Statement
Provides important and critical information for its short-term viability.
Such information is the following:
- The ability of the company to "produce" cash
- The ability to generate future cash flows or the possibility of the company experiencing cash shortages in the future.
- The use of cash made by the company during the period.
- The changes in the net assets and the financial structure of the company.
- The real financial performance of the company without the depreciation forecasts.
- The credit policy pursued by the company and what results it brings.
- The sources of funding it uses for its operation and investments.

The above information provides a detailed and accurate picture of the past, present and future - at least in the short term - of a business.
In many cases, highly profitable companies went so far as to go bankrupt. This was because although they had profits, they had a liquidity problem (cash) and were unable to service their liabilities.
Therefore, the examination of the viability of a company must be done in terms of liquidity and not only in terms of profitability. For this reason, the role of the Financial Statement is now very important.

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6.1.01.02 Financial terms

C. Cash Flow

C4. Discrimination of cashiers
Cash flows are divided into three categories of flows:
A. Operating flows
Operating flows are related to the production and sale of products, as well as the provision of business services.
Operating stream inputs include:
- Sale of goods or provision of services,
- Various other income such as renting extra space
- Refunds from the government
- Returns on shares
- Yields on interest-bearing securities (government or corporate bonds)

Operating flow outputs include:
- Production of products or services (payments for raw materials and auxiliary materials, payments for labor, rent, insurance, payments to suppliers, etc.)
- Merchandise market
- Payments for taxes to the government
- Interest payments

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6.1.01.02 Financial terms

C. Cash Flow

C4. Discrimination of cashiers

B. Investment flows

Investment flows are cash flows that relate to the buying and selling of fixed assets and securities of other companies for long-term investments.

Investment inflows include:

- Proceeds from the sale of fixed assets

Receipts of interest-bearing securities or shares of other companies held for investment purposes.

Outflows of investment flows include:

- Payments for the purchase of fixed assets
- Payments for the purchase of interest-bearing securities held for investment purposes
- Issuance of a loan

C. Financial flows

Cash flows include the acquisition of cash from the issue of shares, the outflow of cash, the repurchase of shares already issued, etc.

Cash flow inputs include:

- Capital derived from the sale of shares of the company
- Funds derived from the creation of debts

Cash flow outputs include:

- Redemption of shares, Payment of dividends, Repayment of debts

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ESlog - MODULE A :

BUSINESS PRINCIPLES

6.1.01.03 Calculates the Net Present Value NPV

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6.1.01.03 Net present value

Is the **Net** (namely after taking into account all income and expenses) **Present** (namely after future cash flows are reduced to current prices) **Value** of an Investment.

Used as an indicator to measure the profitability of a potential investment or to compare potential investments to select the most profitable

$$\boxed{NPV = \sum_{t=1}^{T} \frac{C_t}{(1+r)^t} - C_o}$$

Which:

- C_t = net cash inflow during the period t
- C_o = total initial investment costs
- r = discount rate
- t = number of time periods

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6.1.01.03 Net present value

$$\boxed{NPV = \sum_{t=1}^{T} \frac{C_t}{(1+r)^t} - C_o}$$

An amount today has more value than an amount in the future for two reasons:

1. **Inflation**

   That is, a product now costs 100 E but after a few years it will cost 110 E

2. **Profitability**

   That is, if I invest 100 E today they will bring profits after some 50 E years so the 100 E have the same value as 150 E after some years.

The above is expressed by the **discount rate (r)** with which we convert future values into current ones

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6.1.01.03 Net present value

Related methods of measuring profitability:

1. **Payback period**

   It is the time period in which the original invested capital is expected to be returned.

   With a simple approach:

   If we invest today 100000 E and every year from now on we earn (inputs - outputs) 20000 E, then the investment returns in 5 years (here of course we consider discount rate zero)

   This method has the weakness that it can not measure the profitability of the investment throughout its life, which is what is required, because it does not take into account the inflows - outflows after the payback period.

   That is, an investment may have a discouragingly long payback period of, say, 10 years, but its profitability may be very high in years 12, 12, 13 and beyond. Conversely, it may have a small payback, eg 2 years, but in the following years it may have losses.

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6.1.01.03 Net present value

Related methods of measuring profitability:

2. **Internal Rate of Return - IRR**

   This method uses the same formula as the NPV. The IRR is the discount rate value for which the NPV becomes zero.

   Because IRR refers to one year, it can be used to compare two investments that have higher profitability.

   It can also be used, because it is annual, to compare two different investments. The NPV method does not help this because it gives the net present value of the two investments, regardless of their duration. But the investor is interested to know the amount of NPV in how long it will collect, it is different if it happens in 3 years and different if it happens in 8 years. He obviously prefers the 3 years investment because he has the ability to reinvest the funds in the next 6 years

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6.1.01.03 Net present value

A. Present value of inputs

$$\boxed{NPV = \sum_{t=1}^{T} \frac{C_t}{(1+r)^t}}$$

which:
C_t = cash inflow during the period t
r = discount rate
t = number of time periods

6.1.01.03 Net present value

B. Present value of outputs

$$\boxed{NPV = \sum_{t=1}^{T} \frac{C_t}{(1+r)^t} - C_o}$$

Which:
C_t = cash outflow during the period t
C_o = total initial investment costs
r = discount rate
t = number of time periods

6.1.01.03 Net present value

Γ. Capital budgeting to analyze profitability of investment or project

- We have a profitable investment when the NPV> 0
- The most profitable investment is the one with the highest IRR
- Among 2 investments with the same NPV, the one with the highest IRR is the most prevalent
- Among 2 investments with the same IRR, the one with the highest NPV is the most prevalent
- Among 2 investments with the same IRR, the one with the shortest lifespan is predominant

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Slog - MODULE A :

BUSINESS PRINCIPLES

6.1.01.04 Expenditures incurred - Budgeted expenditures

Monitors actual costs versus budgeted costs

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6.1.01.04 Expenditures incurred - Budgeted expenditures

A. Budget

It is useful because:

1. I better understand what **activities my income comes** from and how it is distributed
2. I better understand what **activities I spend** my money on
3. I identify **expenses that are unnecessary** or do not contribute to revenue
4. I know **where to cut spending** if the financial situation changes
5. I understand how **to achieve my financial goals**
6. I remove unpleasant **surprises and stress**

6.1.01.04 Expenditures incurred - Budgeted expenditures

A.Budget

The steps to create a budget

1. **Which are my Goals?**
2. **Where does my money come from (Revenue)**
3. **Where I spend my money (Expenses)**
4. **I make arrangements where needed**

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6.1.01.04 Expenditures incurred - Budgeted expenditures

A. Budget

How we estimate the amounts of the budget:

A. Last year base

We rely as a basis on the actual LY data and make adjustments according to the estimated increases / decreases in the cost parameters (labor, transport, raw materials, production costs, index, etc.) and in the quantities

B. Zero base

We do not take into account last year's data and we build the budget from scratch.

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6.1.01.04 Expenditures incurred - Budgeted expenditures

A. Budget

Advantages and disadvantages of the methods :

A. Last year base

- \+ Writing speed
- \+ Small risk of omissions
- \- Trend for growth forecasts
- \- Revenues and expenses are not analyzed in their components but the final amount is fluctuated adhoc
- \- Risk of forecasting amounts from one-off income - expenses of last year, which will not occur in the estimated year

LY actual X % adjustment = CY plan

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6.1.01.04 Expenditures incurred - Budgeted expenditures

A. Budget

Advantages and disadvantages of the methods :

B. Zero base

+ Revenues are analyzed in depth, opportunity for strategy modification, marketing plan, product range, etc.
+ Expenses are analyzed at their root and we are given the opportunity to assess whether they are needed and to what extent
+ Staff are trained to understand the cost structure
- Time consuming
- Risk of receiving expenses

CYc1+ CYc2+….. = CY Plan

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6.1.01.04 Expenditures incurred - Budgeted expenditures

B. Actual expenditure to date

Expenditure incurred goes through a series of phases:

1. Committed

Orders or contracts with suppliers have been signed and payment is expected within the current year. There may be some margin for cancellation or postponement of delivery and / or payment

2. Delivered

The products or services are delivered by the suppliers and payment is provided within the year. There may be little possibility of returning part of the products or deferring payment

3. Invoiced

The Suppliers have invoiced the products and the invoice is on its way, either in the hands of the inclusive service, the way to the Accounting Office, or in its hands

4. Payable

Registered in the system (ERP, etc), appear as a liability to suppliers

5. Paid

They have been paid and are displayed in the system as Actual expenses.

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6.1.01.04 Monitors actual costs versus budgeted costs

B. Actual expenditures to date

The actual expenses can be analyzed through there phase there are processed:

1. **Committed**

The orders or contracts have been signed and the payment is expected. There might be an option for cancelling the order or delay the delivery and payment.

2. **Delivered**

The products have been delivered and the payment is expected. There might be an option of returning part of the order or delay of payment.

3. **Invoiced**

The providers have processed and invoiced the order. The invoice is in the hands of the responsible department.

4. **Payable**

They have been processed through the system (ERP, etc.), and they show up as an obligation to the provider

5. **Paid**

They have been paid and they show up on the system as Actual expenses.

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6.1.01.04 Monitors actual costs versus budgeted costs

Exercise

Budget Monitoring

Line: Staff Overtime

LY Plan	LY Actual	CY Plan	YTD Plan	YTD Actual	% vs YTD Plan	Projected Plan	Revised Plan
25000	26700	22000	12000	14200	118.3%	26033	?????

You are hired as the new Supply & Logistics Director in the middle of the year aiming at controlling the expesnses, that they are said to be extensive for the last year. You ask for the line by line analysis as shown above:

1. What are the 3 most important conclusions you draw from the table above?
2. What other information do you need to base your investigation?
3. What amount would you suggest as a revised plan ?
4. What measures would you take in order to assure your revised plan succeeds?

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6.1.01.04 Monitors actual costs versus budgeted costs

C. Future expenditure commitments

They are the obligations that we have to our providers under the form of:

1. Contract
2. Assignment order - Order
3. Other form of assignment (email)
4. Other verbal agreement that confirms the order or assignment

The commitments have **great importance** because, even though they do not show up in the progress report of the actual budget, they will show up in the near future and if we do not account for them they might jeopardize the budget.

Commitments must be made only by those who have the right authorization while the Financial Director is fully aware. This process is better completed if it goes through the system (ERP).

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6.1.01.04 Monitors actual costs versus budgeted costs

D. Balance of annual budget remaining

It is the remaining of the annual budget minus the annual total expenses as to the point in time we calculate the balance (Year-To-Date)

Balance = Plan - YTD spend

It is important to track the balance especially during the last months of the year, so as not to cross and go over the budget.

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6.1.01.04 Monitors actual costs versus budgeted costs

D. Balance of annual budget remaining

Balance = Plan - YTD spend

Management options of remaining expense budget

The **options** of managing a situation whereby the remaining is less than the budget are:

a. Cancellation or delay of sourcing until the new fiscal year
b. Delay payables until new fiscal year
c. Reevaluate the plan with (or without) integration of other cost units and/or revenue streams

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ESlog - MODULE A : BUSINESS PRINCIPLES

6.1.01.05 Business Plan

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6.1.01.05 Business Plan

What is a Business Plan

A Business Plan is a written proposal that aims at:

- describes and explains the business idea,
- estimates the future course of the business,
- forecasts the financial aspects of the business – necessary initial capital and the return on the investment,
- proves whether it is beneficiary to develop your business idea

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6.1.01.05 Business Plan

Why do we need a Business Plan

- To decide to move forward or not with the investment
- Clears the image of the business idea
- Minimizes the risk which puts you in the path of success
- Helps you attract investors, lenders, co-founders and partners, banks, etc.
- Creates a path of constant acting
- Creates the point of reference when evaluating the progress of implementation

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6.1.01.05 Business Plan

Contents of Business Plan

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

6.1.01.05 Business Plan

Contents of Business Plan

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

A short summary of the Business Plan which highlights the business idea and how will it succeed.
It must help the reader in **just 1 or 2 pages** to understand the business idea, be convinced of its financial viability and its implementation plan.

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6.1.01.05 Business Plan

A. Business Concept

A1. The enterprise

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

- Describe :
  - the scope and goal of the enterprise,
  - type of legal entity (Ltd, etc.),
  - the major shareholders,
  - the invested capital,
  - the strengths of the business

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6.1.01.05 Business Plan

A. Business Concept

A2. The Product

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

Describes :

- The product or service of the business,
- the customer needs that it satisfies,
- the technical characteristics,
- the competitive properties (sources of competitive advantage)

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6.1.01.05 Business Plan

A. Business Concept

A3. The Market

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

- Defines :
  - who is our audience (target group),
  - who is our major competitors
  - the size and distribution of the market, and the one we tend to acquire
  - entry barriers and ways to mitigate

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6.1.01.05 Business Plan

A. Business Concept

A4. To marketing Plan

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

- Describes :
  - the business's positioning in the market,
  - how the product is differentiated (4P's model):
    - Product
    - Place
    - Price
    - Promotion

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6.1.01.05 Business Plan

A. Business Concept

A5. Management & Organization

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

- Describes the ability of running the business examining:
  - The people,
  - The production process
  - The premises
  - The tools, equipment, infrastructure and systems

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6.1.01.05 Business Plan

B. Financial Forecasting

B1. Sales

Introduction
The Business
The product/service
The Market
Marketing Plan
Management & Organization
Financial Forecasting
Financial Requirement
Indices

- We estimate the volume of sales using the following formula:

$$\sum_{i=1}^{n} V_i \times P_i$$

where :

Σ = Sum of all products
n = Number of products
V = Sales Volume
P = Selling Price

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6.1.01.05 Business Plan

B. Financial Forecasting

B2. Profits

- We calculate profits by the following formula:

Profit/Loss=
Total Revenues– Total Costs

Where :

Total Revenues = Sales Revenues+ Other Revenues

Total Costs= Fixed Costs+ Variable Costs

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6.1.01.05 Business Plan

B. Financial Forecasting

B2. Profits

Costs

- Is the total amount of money spent or the cost that is created because of any business activity aiming at realizing revenues.
- Costs can be:
  a. Payments,
     e.g., salaries
  b. Λογιστική εκπνοή μέρους ενός περιουσιακού στοιχείου??
     e.g., depreciation
  c. Amounts that are deducted from profits
     e.g., bad debts
- The costs are then summed up, showed up in the profit/loss account and deducted from the profit before tax.
- All expenses are costs, but costs are not expense (*can you think of any examples?*)

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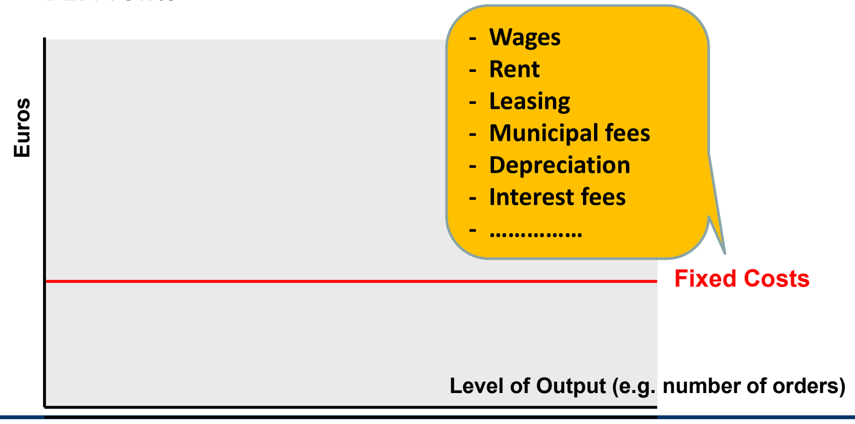
B. Financial Forecasting

B2. Profits



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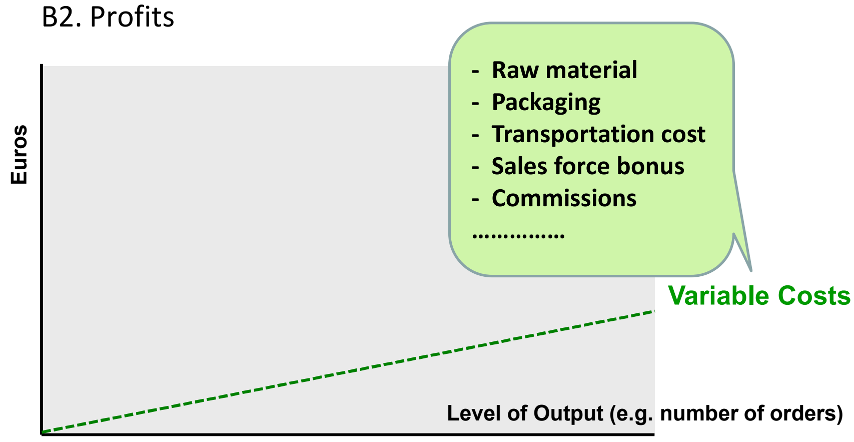
B. Financial Forecasting

B2. Profits



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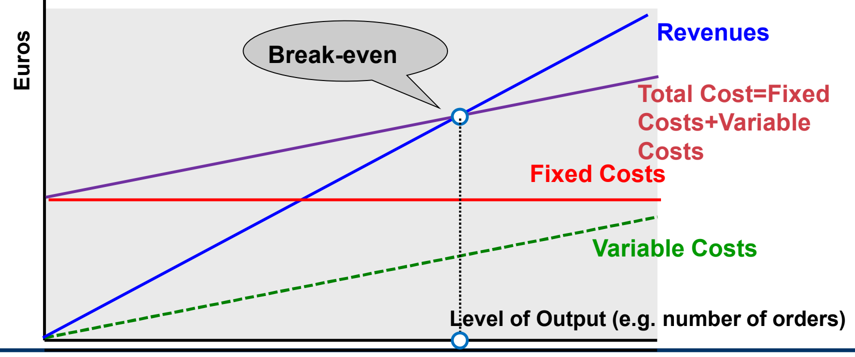
B. Financial Forecasting

B2. Profits

Break even is the level of output at which the revenues are **equal** to total cost.



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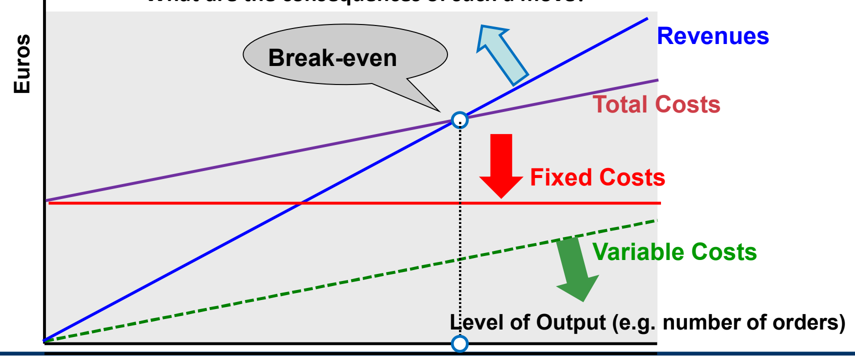
B. Financial Forecasting

B2. Profits

Exercise : **How can we move the level of output right of the Break Even Point? What are the consequences of such a move?**



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B. Financial Forecasting

B2. Profits

Exercise : A dairy company examines the selling of milk through automated selling points. Fixed costs are 300,000€ per annum, while variable costs are 0.40 €/kg. 1.50 €/kg is suggested as the selling price. For that price, it is estimated 200,000kg for the annual sales volume. The marketing director suggest an alternative; 1.60€/kg as the selling price which is forecast to realize 180,000 kg per annum.

A. What is the breakeven for each scenario?
B. Which scenario is more beneficiary?

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B. Financial Forecasting

B2. Profits

Exercise: How can we move the level of output right of the Break Even Point? What are the consequences of such a move?

	Action	Consequence
↑	**Increase Selling Price** **Increase Sales Volume** **Increase other sources of revenues**	**Decrease Sales Volume** **Increase Marketing Cost** **Small to none consequences**
↘	**Decrease Variable Costs**	**Decreased level of quality, decrease Selling Price and Sales Volume**
↓	**Decrease Fixed Costs**	**Decrease Sales Volume**

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B. Financial Forecasting

B3. Cashflow

Are the in-flow and out-flow cash that are resulted from business activities:

Cash Flow				
Money Received	Start	Month 1	Month 2	Month 3
Cash Sales	$0	$0	$0	$0
Payments Received	$0	$0	$75	$188
New Loans	$200	$0	$0	$0
New Investment	$300	$0	$0	$0
Total Received	$500	$0	$75	$188
Money Spent				
Cash Spending	$0	$0	$25	$50
Bill Payment	$0	$0	$300	$250
Repay Loans	$0	$0	$0	$0
Purchase Assets	$0	$0	$0	$0
Total Spent	$0	$0	$325	$300
Cash Flow	$500	$0	($250)	($113)
Cash Balance	$500	$500	$250	$138

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6.1.01.05 Business Plan

B. Financial Forecasting

B3. Cash flow

Cash flow Statement

It is one of the most important statement:

(balance sheet, Income statement, Stockholders equity, Cash Flow statement)

Involves the cash that are realized and used during a period of time. They are represented under these 4 categories:

1.Operating activities	- converts the items reported on the income statement from the accrual basis of accounting to cash.
2. Investing activities	- reports the purchase and sale of long-term investments and property, plant and equipment.
3. Financing activities	- reports the issuance and repurchase of the company's own bonds and stock and the payment of dividends.
4. Supplemental information	- reports the exchange of significant items that did not involve cash and reports the amount of income taxes paid and interest paid.

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B. Financial Forecasting

B3. Cash Flow

Cash Flow Statement

How can it be interpreted :

1. The cash that is generated by operating activities is compared with the profit of the business. If they are consistently higher than the profit, we conclude that the Profit is of **"High Quality".** But if it is lower, then it raises questions as to why profits are not converted into cash.

2. If a business creates cash that are consistently higher than the cash it uses, then the business is able to issue more shares, buy shares, decrease debt, acquire other businesses. This situation is desirable by any shareholder of such business.

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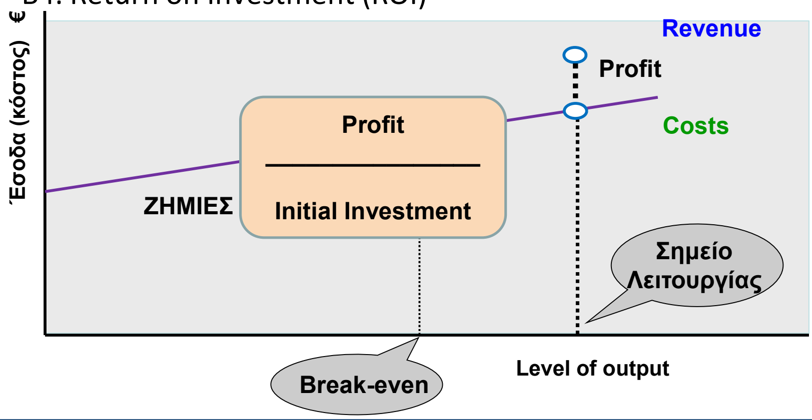
B. Financial Forecasting

B4. Return on Investment (ROI)



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B. Financial Forecasting

B4. Return on Investment

Return on Investment (ROI) is an indicator used to evaluate the returns of an investment or to compare the returns amongst investments

How do we use ROI?

A. ROI calculates how effectively a business used its capitals to realize profits. If the investment does not result into something positive or other investments seem more favorable, then you should not move forward.

Example:
If the long term ROI is less than the cost of capital, it is favorable for the business to liquidate its assets and increase its cash.

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B. Financial Forecasting

B4. Return on Investment

B. ROI is also used by the bank, investor and analysts to assess the economic robustness and effective use of resources of the business.

It is said that businesses need at least 10-14% ROI in order to be able to finance their future endeavors.

- If ROI is low, the administration is not effective or the style of the business is too conservative,
- If ROI is high, the administration is doing a good job or the business does not possess the necessary capitals for the fiscal year.

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6.1.01.05 Business Plan

B. Financial Forecasting

B4. Return on Investment

C. ROI can also be used to evaluate an **proposed investment in new equipment,** by dividing the increase in profits created by the new equipment by the increase in costs of the equipment.

Example:

A small business can invest in new equipment that costs *5.000€, which* increases the income by *1.000€.*

This creates a ROI of 1.000 / 5.000 or 20%. If this ROI is higher of the ***opportunity cost*** *and there are no other better investments, then the investment is favorable..*

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6.1.01.05 Business Plan

B. Financial Forecasting

B4. Return on Investment

Differences between ROI and RONA

RONA = Return on Net Assets (Indicator of the financial performance).
Calculates how effectively a business uses its net assets to create profit.
It is calculated by using the following formula:

RONA = Return on Net Assets $= \dfrac{\text{Net Income}}{\text{Fixed Assets+Net Working Capital}}$

ROI = Return on Investment $= \dfrac{\text{Net Income}}{\text{Fixed Assets}}$

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6.1.01.05 Business Plan

C. Financial Requirements

C1. Initial Capital and Capital Extension

Includes the expense associated with founding the business but also operating it:

- Buying land, building infrastructure
- Analysis, building licenses
- Buying equipment
- Buying Licenses, patents, etc.

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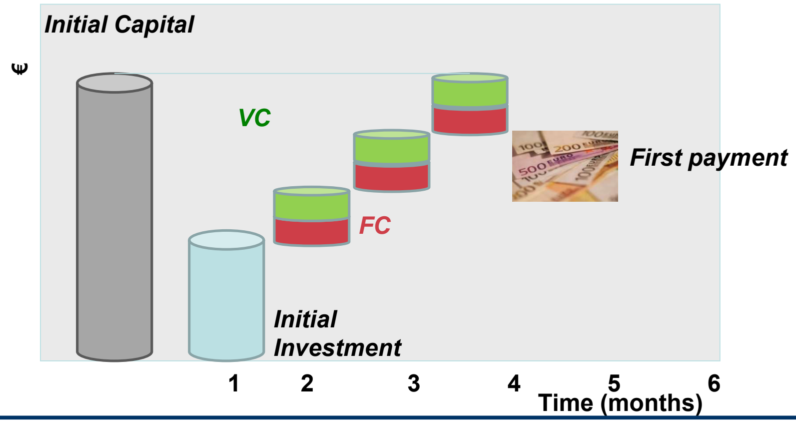
C. Financial Requirements

C1. Initial Capital and Capital Extension



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C. Financial Requirements

C1. Initial Capital and Capital Extension

Attracting Investors

An investors is attracted to a business if:

- It has a high ROI
- Escape option
- The business plan is viable and sustainable and has a small risk attached
- The business has an experience management team
- The business has guaranteed clients and contracts
- The major shareholders believe in the scope of the business

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6.1.01.05 Business plan

C. Financial requirements

C1. Initial and expansion investment capital

Venture Capital

- How to finance the establishment, development or acquisition of a company
- The investor acquires a portion of the company's share capital in exchange for financing
- It is often used in the case of transfer of corporate ownership either to minority shareholders or to groups of company executives (management buy-outs)
- It is usually done through a share capital increase, in which the existing shareholders do not participate in order for the venture capital company to participate.
- For the most part, the major shareholder still retains control of his company

Examples :
Goody's, Chipita, Microsoft, Amazon.com and Yahoo!

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C. Financial requirements

C1. Initial and expansion investment capital

Seed Capital

The initial capital to start the business. It is available to either the founders or friends to start the company and attract the interest of venture capital.

Angel Investors

They offer more favorable terms than other financiers, they invest mainly in individuals and secondarily in the idea. They are interested in the success of their venture and less in the return on their investment

Love Money

Initial capital offered by family or friends, based on quality factors and relationships rather than a standard cost-benefit analysis.

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D. Current business position

D1. Current state of the company

In order to prepare a Business expansion plan for the addition or modification of a product or the infrastructure of a company, it is necessary to properly record the current situation in order to correctly calculate the ROI performance of the addition

EXCERCISE :

When implementing an agricultural machinery production investment, a new proposal is made for expansion with an additional production line for an innovative product. The additional investment will cost 100000 E and is expected to contribute 9000 E / year profits (before depreciation). How do you evaluate this investment proposal?

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6.1.01.05 Business plan

E. Major Achievements

E1. Success Factors

Frequent reasons for failure

1. They are trying to become a big business very early

- spend a lot of money on marketing without investigating whether Customers really want the products or have to modify them to want them
- add properties that can be "nice to have"
- hire a lot of staff to promote the product
- ignore other opportunities that arise

2. They underestimate the time it takes to place the product

- usually needs 2.5 times more than they calculated

3. They do not seek expert opinion and help

- Mentors, peer assist

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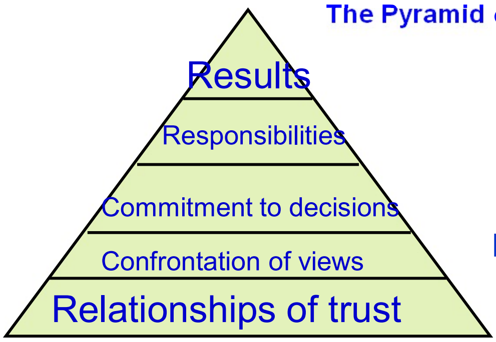
E. Major Achievements

E1. Success Factors

The Pyramid of Performance :



From

Trust

to

Performance

Do not proceed further unless you have established trust in your team

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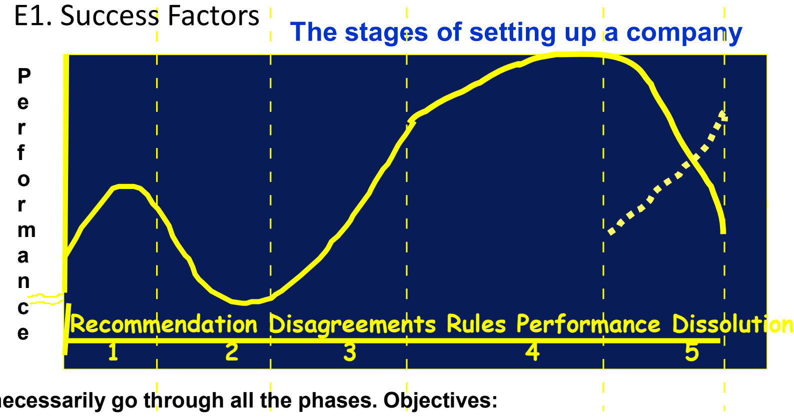
E. Major Achievements

E1. Success Factors



We will necessarily go through all the phases. Objectives:

a. Pass phase 2 b. quickly with the least wear. Phase 4 should last longer and the rest less
c. Launch phase 1 of the next action when phase 5 starts

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6.1.01.05 Business plan

E. Major Achievements

E1. Success Factors

Characteristics of a Successful Entrepreneur

- **Vision - Goals - Strategy**
- **Faith - Commitment - Perseverance**
- **Risk taking – No fear**
- **Team - Atmosphere**
- **Passion- Humor**

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E. Major Achievements

E1. Success Factors

Conditions for a strong team

- **integrity - creativity - judgment**
- **trust relationships**
- **enlignment in the vision**
- **goals - incentives**
- **roles - responsibilities**

6.1.01.05 Business plan

E. Major Achievements

E1. Success Factors

Focus on essential achievements

In a business plan there are many objectives, deliverables, key milestones, secondary timelines, actions critical to the implementation of the plan, non-critical actions, actions that are financial commitments, others that are not, assumptions critical to the viability of the investment, etc.

When implementing the Business Plan, we should focus as a priority on:

- **Critical milestones (eg, licensing, prototype testing, loan approval, etc.)**
- **In actions that involve large financial commitments (eg real estate purchase, recruitment, etc.)**
- **In cases where sustainability is based (eg, competing products, economic environment**, etc.)

ESlog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.06 Pricing Strategy

Understands how a pricing strategy is defined

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing targets that the company can choose - 1

- **Price stability in the Market**
- **Determination of fair prices**
- **Prices similar to Competitors**
- **Avoid price war** *(status qvo)*
- **Survival**
- **Cost coverage** *(cost plus)*
- **Coverage of part of the costs** *(partial cost recovery)*

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing targets that the company can choose - 2

- **Maximizing the profit margin**
- **Profit maximization**
- **Revenue maximization**
- **Quality leadership**
- **Quantity maximization**

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Factors influencing pricing

- **Related to Organizational Characteristics** (goals, strategies, culture, structure, market position, size, marketing strategies, etc)
- **Related to Quality Characteristics** (product type, cost, quality, Life Cycle stage, Innovation, differentiation, etc)

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing Strategies -1

- **Competitive pricing**
  Useful when the product can not be differentiated from the Competition. It applies when the pricing target is either Survival or Avoidance of War
- **Good-better-best pricing**
  Higher prices for products that have received better processing, packaging or attention. It applies when the goal is Maximizing Turnover or Quantity
- **Loss leader**
  A product is selected to be sold at a low price to attract customers who will buy other products.
  Applies when the goal is Maximizing Turnover or Quantity.
- **Multiple pricing**
  The unit price is lower when the customer buys more than one item. It applies when the goal is Maximizing Profit or Quantity

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing Strategies-2

- **Optional product pricing**
  A product is offered with special specifications at a higher price. Applies when the pricing goal is Maximizing Turnover or Quality Leadership
- **Penetration pricing**
  A product is offered at a lower price than the competition, when it is in the phase of entering the market or increasing the share. It applies when the goal is Maximizing Turnover or Quantity
- **Premium pricing**
  When a high quality or luxury product with low expected sales is sold at a high price. Applies when the goal is Maximizing Profit Margin Quality Leadership.
- **Product bundle pricing**
  Many products are grouped in one sales package. Useful for getting rid of stocks. Applies when the goal is Maximizing Turnover or Quantity

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing Strategies -3

- **Product line pricing**
  Products that are usually used together are offered in a package at a price lower than the sum of the individuals. Applies when the pricing goal is Profit Maximization Quality Leadership
- **Skim pricing**
  A new product, without high competition, is offered at a high price which later decreases when the competition is activated. Applies when the goal is Profit Maximization, Profit Margin Maximization or Turnover Maximization

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Invoicing methods

- **Cost based pricing**
  a fixed profit margin is added to the production cost (markup)
- **Break even pricing**
  the company designates a point of sale where it covers its costs
- **Rate of return pricing**
  the company sets a product price that in combination with its sales volume yields a satisfactory return on its investment (ROI) or asset (ROA)
- **Perceived value pricing**
  The price is determined based on buyers' perceptions of the value of the product and not on its actual cost.

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing methods - Especially for new products:

- **Penetration price**
  set a lower price than the competition to facilitate market penetration
- **Skimming price**
  a price higher than the competition is set to facilitate market penetration
- **Market driven price**
  a price is set in the context of competition

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

Pricing Objectives

Pricing Strategies	Profit Max	Revenue Max	Quantity Max	Profit Margin Max	Quality Leader ship	Partial Cost recovery	Survival	Status Quo
Multiple	■		■					
Product line	■				■			
Skim	■	■		■				
Good, better,best		■	■					
Product bundle		■	■		■	■	■	
Optional product		■			■			
Premium				■	■			
Loss leader			■			■	■	
Penetration		■	■					
Competitive							■	■

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

A1. Survival

When the goal is the survival of the company then the pricing policy is formulated to ensure sales revenue as needed to cover costs and the company survives by postponing for later when conditions are more favorable the implementation of other strategies and profit.

In addition to the pricing policy part, the company can implement policies to reduce operating costs or a combination of both to achieve the goal of survival.

In these situations it is possible that issues such as quality, safety, education, advertising, interest in the environment, etc. are likely to take second place.

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

A1. Survival

This Strategy is implemented with the pricing methods:

- **Loss Leader Pricing**
- **Competitive pricing**
- **product bundle pricing**

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

*A*2. Current profit maximization

The aim is to maximize Profit.

This goal is different from the profit margin maximization strategy in which the goal is to maximize the profit margin per unit.

Exercise :

A company has estimated that it can sell 10,000 units at a price of 10 E or 15000 at a price of 8 E. The product cost will be 5 E and 4.5 E respectively. Which scenario fits with profit maximization and which with profit margin maximization?

6.1.01.06 Pricing Strategy

A. Price relative to business strategy

*A*2. Current profit maximization

This strategy is implemented by one of the following methods:

- **multiple pricing**
- **product line pricing**
- **skim pricing**

6.1.01.06 Pricing Strategy

A. Price relative to business strategy

A3. Market share leadership

With this strategy we seek the company to have the largest market share. This is measured either in product volume (eg, pieces, kilos, etc.) or in sales value (in E)

O Steve Jobs (Apple) suggests how a company can become a market leader:

1. Possession and Control of market related technology
2. Immediate adoption of better technologies as soon as they appear regardless of what others are doing

Creating a category for a product, its evolution into an industry standard

This strategy is particularly relevant in the age of the Internet where first movers in new markets can quickly gain a monopoly position.

6.1.01.06 Pricing Strategy

A. Price relative to business strategy

A3. Market share leadership

This pricing strategy seeks to increase market share and is applied when the product is introduced to the market. This strategy uses the following pricing methods:

- **multiple pricing**
- **good-better-best pricing**
- **product bundle pricing**
- **loss leader pricing**
- **penetration pricing**

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6.1.01.06 Pricing Strategy

A. Price relative to business strategy

A4. Product quality leadership

The pricing strategy seeks to highlight the high quality of the product. This strategy uses the following pricing methods:

- **premium pricing**
- **optional product pricing**
- **product bundle pricing**
- **product line pricing**

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6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Price elasticity of Demand –PED or $e_{\{p\}}$

It gives the percentage change in demand that causes a percentage change in price. It is usually negative, ie an increase in price causes a decrease in demand. Excludes products that do not obey the law of supply and demand

$$e_{\{p\}} = \frac{dQ / Q}{dP / P}$$

Example: If the price increases by 5% and therefore the demand decreases by 5%, then the Elasticity is (-5) / (5) = -1

Point - Price elasticity of Demand = $$Ed = \frac{P}{Q_d} \times \frac{dQ_d}{dP}$$

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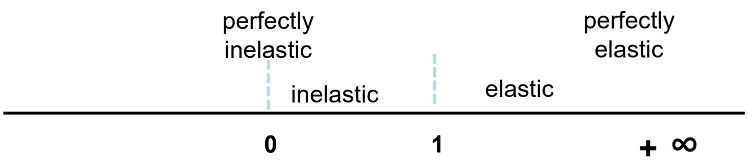
6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Value	PED
< 1	inelastic
> 1	elastic
0	perfectly inelastic
∞	perfectly elastic



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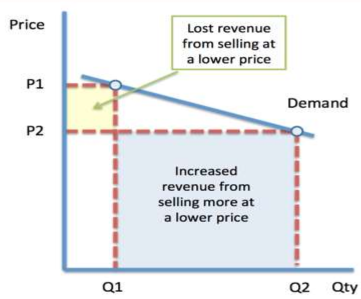
6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Elastic Demand (Ped > 1)

If the co-efficient of price elasticity of demand >1, then demand is said to be price elastic i.e. highly responsive to a change in price

- If demand for a product is price elastic, a supplier stands to gain extra revenue if they reduce their prices.
- The change in quantity demanded will be proportionately higher than the reduction in price. This is shown in the diagram opposite.



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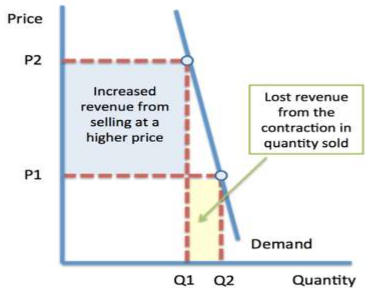
6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Inelastic Demand (Ped < 1)

If the co-efficient of price elasticity of demand <1, then demand is said to be price inelastic i.e. unresponsive to a change in price

- Following a change in price, the total revenue earned by the producing firm will depend on the PED for its product
- If the coefficient of PED is <1, a rise in market price (e.g. from P1 to P2) will lead to an increase in total revenue



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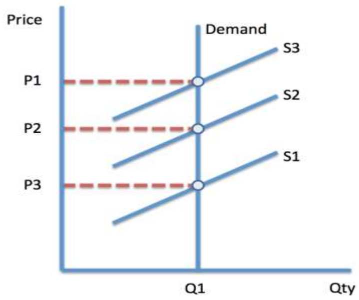
6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Perfectly Inelastic Demand (Ped = 0)

If the co-efficient of price elasticity of demand = zero, demand is perfectly inelastic i.e. demand does not vary with a change in price

- A perfectly inelastic demand curve is an extreme case for it implies that consumers are willing and able to pay any price for the product. If supply falls, equilibrium market price can rise without any contraction in the quantity demanded



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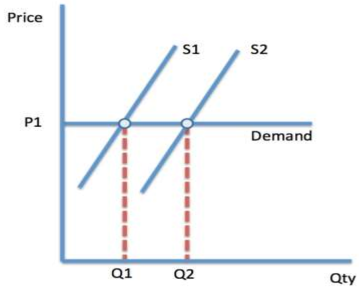
6.1.01.06 Pricing Strategy

B. Price elasticity of Demand -PED

Perfectly Elastic Demand (Ped = infinity)

If the co-efficient of PED = infinity, then demand is perfectly elastic – there is one price at which consumers are prepared to pay

- If demand for a product is **perfectly elastic**, a change in market supply (shown on the right as an outward shift of supply) will not lead to any change in the equilibrium price. This demand curve applies to highly **competitive markets** where no supplier has any "pricing power"



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6.1.01.06 Pricing Strategy

Γ. Cost related

The product price must cover:

- the variable part of the cost (cost of sales)
- fixed and overheads divided by quantity
- a realistic profit

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6.1.01.06 Pricing Strategy

Δ. Related to Competition prices

Competitive pricing

The price is determined according to the competition prices and is placed in the upper, middle or lower zone depending on the parameters:

1. How fast does the company want to market it?
2. How much market share does he want to gain?
3. Whether the product is of better quality or inferior to the competition products

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6.1.01.06 Pricing Strategy

E. Pricing Methods

E1. Cost plus

This method determines the price based on the cost of the product (which includes all production, distribution, advertising costs, overheads, etc.) and by adding a percentage of profit.

Παράδειγμα :

- Κόστος πωληθέντων		:	1000 E	
- Συμμετοχή στα γενικά έξοδα	40%	:	400 E	
Κόστος προϊόντος		:		1400 E
- Κέρδος	30%	:		420 E
ΤΙΜΗ ΠΩΛΗΣΗΣ		:		1820 E

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6.1.01.06 Pricing Strategy

E. Pricing Methods

E2. Target profit pricing

The Seller sets the price in order to achieve a certain amount of profit.

When using this method it is very important to consider the Product Demand Curve. Because any change in price affects product demand, it is not enough to multiply the unit Contribution by the quantity of the product. Instead, the profit for a given price must be calculated by the formula:

Expected Profit = Unit Contribution*Demand Function{Price} - - Fixed Costs

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6.1.01.06 Pricing Strategy

E. Pricing Methods

E2. Target profit pricing

Example :

Fixed Costs : 200000 E

Target profit : 100000 E

Unit price : 75 E /unit

Variable unit cost : 45 E / unit

Contribution margin : 30 E / unit

The amount of sales that will bring this profit is determined as follows:

Sales X contribution margin = Fixed costs + Target profit

Sales = (200000 + 100000)/30 = 10000 pieces

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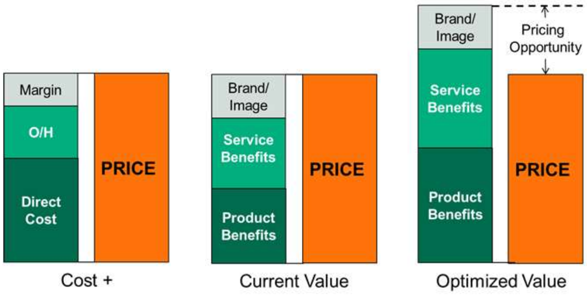
6.1.01.06 Pricing Strategy

E. Pricing Methods

E1. Perceived value pricing



To pricing opportunity is quantified through a better understanding of the value of the product, service and brand

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6.1.01.06 Pricing Strategy

E. Pricing Methods

E1. Perceived value pricing

Actual value

Corresponds to the cost of production and sale of the product for a profit, without brand name. No other expectations are met by the seller or the buyer.

Perceived value

Completely different from the actual value. It is the value that the customer believes the product has. This belief is formed by the opinion of the market and by the benefits that the customer expects to have if he buys the product.

Usually: **perceived value > actual value**

In some cases, however, it can: ***perceived value < actual value***

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ESlog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.07 Assess Business Performance

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6.1.01.07 Assess Business Performance

A. Review Activities

Important step for assessing business performance is to review activities under the following scopes:

1. Is this activity **necessary**? (must, nice to have, worthless)
2. Does it add to **perceived value,** or does it create only additional cost?
3. Is there the option of abolishing it, reducing it, simplifying it, replacing it with a more innovative activity or **automate** it?
4. How does the **added value** it creates to the company's products or services in relation to the costs it creates?

Streamlining activities is called reengineering, restructuring, process simplification, lean approach, etc.

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6.1.01.07 Assess Business Performance

A. Review Activities

Exercise:

Explain the difference between **reengineering** and continuous **improvement**:

Reengineering :

- Radical changes in operations and way of working
- Aim at high percentage at savings
- When there is a merger or acquisition, before the application of ERP system, etc.
- In cases of emergency
- Ever few years, not constant
- Aim at being sustainable for the years to come

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6.1.01.07 Assess Business Performance

B. Evaluate products or services

The reason for products or services to exist is to satisfy the customers' needs, while realizing profit for the provider. Every product or service must be evaluated through the following scopes:

1. Does the customers' need still exist or did it transform into something that other products cater to now?
2. Are technological advancements making your production methods ore even your product or services obsolete?
3. How is the competition transforming their products?
4. Is profitability of the product in the wanted levels?
5. Are the pricing strategy and pricing methods suitable?

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6.1.01.07 Assess Business Performance

C. Review Financial Performance

The review of financial performance aims at assuring the sustainability and profitability of the company.

The method that we use to review financial performance is the comparison between the **actual** figures with the **planned** figures:

- Sales (units)
- Prices
- Revenues
- Costs
- Profits
- etc.

6.1.01.07 Assess Business Performance

D. Financial and Operational Ratios

The comparison of financial and operational performance between two companies at two different points or periods in time must use the suitable ratios.

I. ACTIVITY ratios

- **a. Inventory turnover** (= cost of products sold/ average inventory)
- **b. Receivables turnover** (= net revenue / average receivables)
- **c. Payables turnover** (= purchases (on credit) / average payables)
- **d. Asset turnover** (= net revenues divided by average total assets)

6.1.01.07 Assess Business Performance

D. Financial and Operational Ratios

II. LIQUIDITY ratios

- **a. Current** ratio (= current assets / current liabilities)
- **b. Quick** ratio (= accounts receivable / current liabilities)
- **c. Cash** ratio (= cash + short-term marketable securities / current liabilities)

III. SOLVENCY ratios

- **a. Debt-to-assets** ratio (= total liabilities / total assets)
- **b. Debt-to-capital** ratio (= total debt / (total debt + total shareholder's equity))
- **c. Debt-to-equity** ratio (= total debt / total shareholder's equity)
- **d. Interest coverage** ratio (=earnings before interest and taxes / interest payments)

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6.1.01.07 Assess Business Performance

D. Financial and Operational Ratios

IV. PROFITABILITY ratios

- **a. Gross profit margin** (= gross income ÷ net revenue)
- **b. Operating profit margin** (= operating income ÷ net revenue)
- **c. Net profit margin** (= net income ÷ net revenue)
- **d. Return on assets (ROA)** (= net income ÷ total assets)
- **e. Return on equity (ROE)** (= net income ÷ total stockholder's equity)

(See attached document for further explanation)

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Slog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.08 Outsourcing

make outsourcing decisions

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6.1.01.08 Outsourcing

A. What can we get outsourced

A1. Core Competence

Core competences is strong points (strengths) or strategic advantages of a company. Is the combination of the **pooled knowledge** and the **technical capabilities** which allows the company to be competitive in the market.

Core Competence:

- allows the company to penetrate to new markets
- provides many advantages to customers
- it is not easily imitable (the competition cannot imitate it)
- Assists at creating the brand

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6.1.01.08 Outsourcing

A. What can we get outsourced

A1. Core Competence

What activities can we outsource:

1. Not the activities related with the core competencies
2. Key activities (with some reservations)
3. Non key activities
4. When the **technology advances** and the in-house production is not able to catch up.
5. Activities requiring **huge investment** in infrastructure
6. When sales volume is low and in-house production is not financially viable/justified
7. When there is a plethora of high-quality providers
8. When the **cost** of in-house is greater than outsourcing

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6.1.01.08 Outsourcing

A. What can we get outsourced

A2. Requires specific expertise

For products or services that require a specific expertise to produce, it is preferably to get it outsourced for the following reasons:

1. It requires specialized staff, specialized technology and informed management structure. All of those result to high cost, especially when the level of production is less than the necessary to achieve break-even
2. A service provider that specializes in service of a unique know-how and/or technology might be able monitor the tech sector for improvements, focus on high productivity and invest in R&D. And because of the high number of customers it can cover its costs
3. Greece lacks of outsourcing services because there are not enough companies with a proven record of consistency and performance that specialize in something.

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6.1.01.08 Outsourcing

A. What can we get outsourced

A3. Financially attractive

In order to decide whether to outsource part of our business, we must assure that the outsourcing option is more financially attractive than the in-house option.

It is important to also consider in our calculations the following aspects about costs :

1. Not only the costs of the operations but also the cost of management of those operations (e.g. driver+ fleet mgr + %Transport Mgr + %Auditor+….)
2. Revenues of selling company's assets (e.g. vehicles, real estate, etc.)
3. Expenses must be considered with the estimation for the future conditions (e.g. while drivers and warehouse employees' wages increase, 3PL fee might decrease)
4. We must consider the necessary future investments for expanding and/or replacing infrastructure (e.g. vehicles, Clark, shelves, software, etc.)

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6.1.01.08 Outsourcing

A. What can we get outsourced

A3. Financially Attractive

Exercise:

A retail company that owns its fleet considers the option of outsourcing. The annual expenses for wages (drivers, τεχνιτών, δρομολογητών) is 2,500,000 €, while expenses for rent for parking spaces, synergies, office of supportive staff, insurance fees, depreciation etc. are 1,500,000 €. Variable costs (fuel, maintenance , tires, etc.) is 2€/unit of product

The annual volume of transport is 1,000,000 units, but the predictions for the futures estimate that is going to drop to 800,000 units.

Having asked for offers from transporting companies (in €/units),what is the max price that would be financially attractive for an outsourcing option?

P x 800,000 units < 2,500,000€ + 1,500,000€ + 2€ x 800,000 units

therefore **T < 7 €**

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6.1.01.08 Outsourcing

B. Process of outsourcing

B1. Plan Initiative

In order to plan outsourcing an activity we must consider the following:

1. Identify the activity that **can** be outsourced
2. Study of financial benefit – NPV
3. Approval of business case
4. Market research for providers
5. Express clearly the responsibilities of the potential provider and publish a notice of tender
7. Selection of provider
8. Transition plan
9. Training
10. Change implementation
11. Corrective actions

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6.1.01.08 Outsourcing

B. Process of outsourcing

B2. Explore Strategic Implications

A decision to follow the outsourcing option should not only consider the short term economic criteria but also the positive implications in the strategic level, such as:

1. Work hand-in-hand with the retail/commercial strategy of the company
2. Better position in the market
3. Ease to enter or exit in the industry, ease of merge and buy outs
4. Maintain or upgrade the status of the brand
5. Improve profitability and performance (POI)
6. Positive feedback from the market and stock market
7. Ability to expand to new geographic areas
8. Ability to outsource more activities

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6.1.01.08 Outsourcing

B. Process of outsourcing

B3. Analyze costs and performance

The contractor's Perspective

The costs of the new model must be analyzed in detail and assure that they are realistic. A low offer from a contractor is not enough, because if that contractor is not able to carry out our business activity we will be faced with a huge cost of ending our contract with them and urged to return to the old model (if that is even technically possible) or switch contractors.

Assuring of a realistic cost analysis, we can follow the **open book approach**, which means the cost analysis of the contractor can be openly inspected by both parties. This open book approach guarantees total transparency and can help both parties to agree on a **fair price** that includes all costs and a realistic profit margin.

Furthermore, we must assure that the contractor will realize **realistic return** on the investment, which means realistic profits compare to the initial investment and the capital they will employ.

6.1.01.08 Outsourcing

B. Process of outsourcing

B3. Analyze costs and performance

The Business Perspective

The costs of the new model for the business must be analyzed in detail and be assured that they are realistic.

Each cost must be recorded as it is shown in a specific moment in time ("AS IS") and how it is predicted to be with the new model ("TO BE"). Be aware of the costs that do not exist but are introduced with the new model. We need to check also if the hypothesis on which we base our decision are viable (e.g. price of selling owned equipment and assets).

The change has an **one off implementation cost** (e.g. training, transportation of stock, infrastructure, etc.) and a **constant operating cost**.

We must secure the **realistic return** of this investment, in other words realistic savings compared to the initial investment of in-house model.

6.1.01.08 Outsourcing

B. Process of outsourcing

B4. Select Providers

The Methodology of selecting a provider follows these steps :

1. Stating the criteria that the potential provider must satisfy (size, experience, clientele, infrastructure, geographic coverage, synergy, financially robust)
2. After research the potential providers are selected
3. A Request for Information (RFI) is sent
4. Selection of those who satisfy the criteria
5. Request for proposal (RFP), meetings to enrich the new model with provider's ideas
6. Request for Quotation (RFQ)- Evaluation with criteria and weighting factors
7. Post tender negotiation (PTN)
8. Contract

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6.1.01.08 Outsourcing

B. Process of outsourcing

B4. Select Providers

Sources of Information on providers:

- **Website, prospectus**
- **Newspapers, Industry's magazines**
- **Stock Market**
- **Commercial catalogs**
- **Chambers**
- **Certifying institutions**
- **Credit control institutions**
- **Other buyers, competitors**
- **Surveys, meetings**

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Managing conflicts

Cooperation	*win – win*
Compromise	*balance*
Retreat	*lose – win*
Compete	*win – lose*
Avoid	*no winners – no losers*

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Negotiation Tactics

1. Separate the problem from the people
2. Focus on the interest and not the positions
3. Insist on using subjective criteria
4. Find options for achieving a win-win case.

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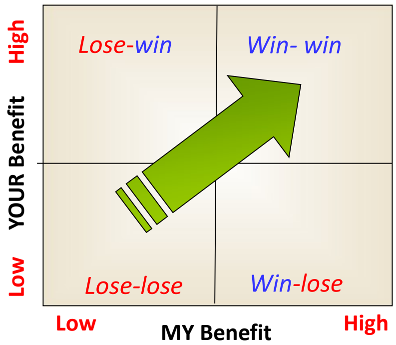
6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Negotiation tactics

4. Find options for achieving a win-win case



In effective negotiations, each side tries to move the negotiations from a win-lose situation or a lose-win to a win-win situation.

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Negotiation tactics

	Strengths	Weaknesses
OUR	Highlight 1 - I am their best client - We have tenders in progress or under preparation	Hide 2 - We need the contract - No one else can satisfy our criteria - We must keep them as a secondary provider
THEIRS	3 - They hold a patent - No competition - They have orders to sell production Undervalue	4 - The prices will decline in the future - New competitors will enter the market - Customers' complaints Expose

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Style of negotiation:

The hard negotiator beats the soft

***SOFT*:**
- Focus on building and maintaining a relationship
- Focus on agreement
- Avoid conflicts
- Trust others
- Make offers

***HARD*:**
- Set the deal as a condition for a relationship
- Aim at winning
- Apply pressure
- Don't trust others
- Threat

If you are in the soft side or if you feel that you are in the wick side, then you may switch the negotiation from the *"object"* of the negotiation (eg, the price of the product) to the *"process" of the negotiation (eg, negotiate the process to organize a market research about a fair price)*

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

Negotiation tactics

Before Negotiation

1. Study the commercial and sourcing strategy
2. Study the market analysis
3. Evaluate the dynamics of the competition
4. Be informed about historic details
5. Confirm that the demands of the business are met

Set Negotiation Strategy

1. Set goals
2. Make a negotiation plan
3. Prepare
4. Guarantee the agreement of all stakehodlders

Negotiation

1. Approaches
2. Tactics
3. «Tricks»
4. Cultural Differences

After Negotiation

1. Conclusions and agreements
2. Contract
3. Lessons for the future

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6.1.01.08 Outsourcing

B. Process of outsourcing

B5. Negotiating the Terms

The negotiating of the terms can follow these steps:

1. During setting the demands and **RFI** for the agreement of the parameters (e.g. number of vehicles, timetable of deliveries and ordering)
2. After opening all offers, the PTN are declared. PTN should be declared the first 2-3 applicants and not with the first applicant or best offer.
3. Be able to renegotiate terms of the contract during the cooperation of the two sides

- There should be a price-goal or term-goal before the negotiation
- The spirit of the negotiation should be win-win (not win-lose)

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6.1.01.08 Outsourcing

B. Process of outsourcing

B6. Transition Resources

For the transition from the "AS IS" situation to the "TO BE" situation, we need resources. We consider resource:

1. **Capital for Fixed Assets**

   For the initial investment in equipment and infrastructure, even if those things are usually the provider's responsibilities.

2. **Working Capital**

   For high stock levels during the transition phase, or for increased credit limits to customers to build stocks, etc

3. **Down payment/Deposit**

   A down payment to the provider for the purchase of the necessary infrastructure.

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6.1.01.08 Outsourcing

B. Process of outsourcing

B6. Transition Resources

4. **Equipment – Machinery**

   that will be used for the transition, such as trucks, forklifts, etc.

5. **Staff**

   for planning and implementing the transition. It can be people form within the organization, specialized consultants, external project management teams or even the provider. Staff is translated as a cost in this case.

6. **Time**

   needed to complete the transition. The longer it takes to transition, the more costly it will be to the company. A transition plan must aim at the least amount of time for the transition.

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6.1.01.08 Outsourcing

B. Process of outsourcing

B7. Managing Relationships

	TRADITIONAL	MODERN
• Access to information	Restricted, access only to necessary info	"Open book"
• Pursuit of profit • Remuneration	Win – lose Fixed cost	Win – win Cost plus, incentivized fee
• Goal	Costs minimization Separate goals	Value Maximization Common goals
• Meeting frequency • Relationships	Low Confrontation	High Cooperation
• Who evaluates • Dispute resolution	The client evaluates the provider Legal	Both-ways evaluation Internal and consensually
• Duration	Short-term	Long-term

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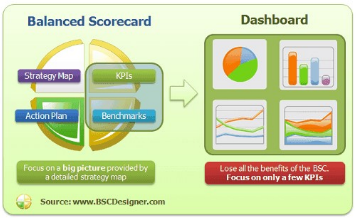
ESlog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.09 Performance Scorecard

Defines and implements a performance scorecard

KPIs of the Balanced Scorecard on the Dashboard



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6.1.01.09 Performance Scorecard

A. What is a Performance Scorecard?

A1. Translating Strategy into indicators

a. Goals

In order to achieve the Goals of a company through the Strategy chosen, individual Objectives must be defined. Those objectives will be fulfilled by the various departments of the internal organization as well as the outsourced services.

Exercise:

If the Strategy of a company is to increase its market share, how would it affect the Logistics Department's goals?

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-
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6.1.01.09 Performance Scorecard

A. What is a Performance Scorecard?

A2. Performance Measures/Indicators

b. Weighting factors

In order to prioritize the goals of a company and be able to measure the total performance, we need to set weighting factors for each goal:

Example:

The company sets goals for the Logistics Department as shown below:

● Decrease of operating costs by 15%	WF : 40%
● Reducing Warehousing facilities (from 3 to 2)	WF : 35%
● Integrating an ERP System	WF : 25%

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6.1.01.09 Performance Scorecard

A. What is a Performance Scorecard?

A3. Focus on a number of Domains

Each year and depending on the company's strategy, the management chooses the number of domains on which wish to focus on. Such domains might be:

- Economic Performance
- Development of new products or services
- Increasing market share
- Enhancing infrastructure
- Environment – Security – Quality
- etc.

For each domain, there are specific quantifiable goals which the various departments of the company are responsible to realize.

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6.1.01.09 Performance Scorecard

A. What is a Performance Scorecard?

A3. Focus on a number of Domains

ΑΜΟΙΒΗ ΜΕ ΒΑΣΗ SCORECARD

Παραδειγμα

Α/Α	ΣΤΟΧΟΙ	ΣΥΝΤ. ΒΑΡΥΤΗΤΑΣ	ΕΠΕΞΗΓΗΣΗ ΒΑΘΜΟΛΟΓΙΑΣ	SCORE	Τελικη βαθμολογια
1	Μειωση κοστους μεταφορας	40%	Πρωτοβουλιες για μειωση κοστους	3	1,2
			0 - 10000 E : 1		
			10001 - 20000 E : 2		
			20001 - 25000 E : 3		
			25001 - 30000 E : 4		
			30000 - E : 5		
2	Μειωση ατυχηματων	20%	Ατυχηματα με θανατο η τραυματισμο	4	0,8
			0 ατυχ : 5		
			1 ατυχ : 4		
			2 - 3 ατυχ : 3		
			4 - 5 ατυχ : 2		
			> 6 ατυχ : 0		
3	Μειωση επιστροφων	16%	Επιστροφες ως % επι ογκου παραδοσεων	3	0,46
			< 1% 5		
			1% 2% 4		
			2% 3% 3		
			3% 5% 2		
			5% 7% 1		
			> 7% 0		
4	Μειωση παραπονων πελατων	16%	Παραπονα ως % επι αριθ. Παραδοσεων	2	0,3
			< 1% 5		
			1% 2% 4		
			2% 3% 3		
			3% 5% 2		
			5% 7% 1		
			> 7% 0		
6	Μειωση απωλειων	10%	Ελλειμματα, απωλειες, κλπ σε ΜΤ	4	0,4
			0 5		
			0 - 2 MT 4		
			2 - 4 MT 3		
			4 - 7 MT 2		
			7 - 10 MT 1		
			> 10 MT 0		
	ΣΥΝΟΛΟ	100%			3,15

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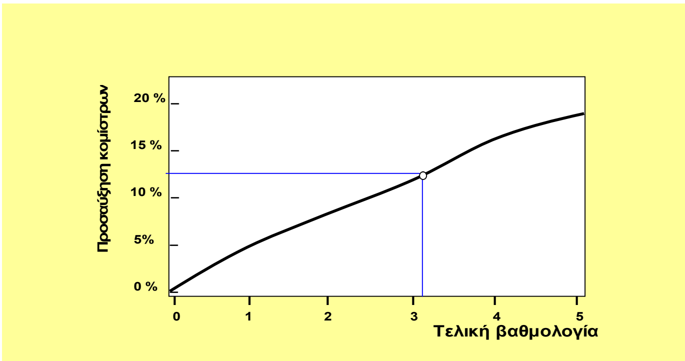
6.1.01.09 Performance Scorecard

A. What is a Performance Scorecard?

A3. Focus on a number of Domains

Performance-based Remuneration



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6.1.01.09 Performance Scorecard

B. Implementation

B1. Project Management Approach

The implementation of each goal follows the “project management approach”, which suggests:

1. Clarifying the objectives *(Objective)*
2. Identifying the necessary actions to accomplish the goal *(WBS)*
3. Time Plan *(Time plan)*
4. Implementation Cost Plan *(Cost Plan)*
5. Risk Identification/Management *(Risk Plan)*
6. Stakeholder(s) Identification/Management *(Stakeholders mgmt)*
7. Communication Plan *(Communication Plan)*
8. Organizational Plan *(Organization Plan)*

6.1.01.09 Performance Scorecard

B. Implementation

B2. Employees’ Involvement

The goals are not achieved by themselves, but it is the outcome of people’s efforts. In order to guarantee that people’s involvement is effective, there need to be:

- an understanding that they are a part of the company’s strategy and vision
- capable staff (competence, Knowledge, capabilities, etc.)
- coordination from higher deputy person and resolution of conflicting goals
- frequent progress monitoring περιοδική
- motivation, reward, bonus

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6.1.01.09 Performance Scorecard

B. Implementation

B3. Pilot Implementation

Before we start pursuing a goal, we need to test whether that goal is attainable to the extent that has been estimated, the estimated time and the unpredictable consequences that it might have, etc

The conclusions from the implementation testing will be used to form the final company's goals of the and organize its implementation plan.

It is usually tested upon a sub-set of the market that represents its entirety. A failure of such a testing can be manageable.

The implementation testing can be categorized:

- by geographical location
- by consumer category
- by a specific product or service

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard

It was first introduced by Robert S. Kaplan and David P. Norton.

Apart from goals related with financial performance, there are additional goals concerning:

- Process Efficiency
- Customer Satisfaction
- Organizational Capacity

aiming at achieving a balanced organizational performance

The goals related with Financial performance are reflected on the outcomes of the effort, whereas the rest of the goals focus on realizing future value for the company by investing on clients, suppliers, staff, operations, technologies and innovation.

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard - Examples of Goals

FINANCIAL

1. Reduction of operating cost of transportation (salaries, fuel, maintenance)
2. Reduction of inventory financial cost
3. Reduction of warehousing cost
4. Increase the transported volume
5. Increase the average order volume
6. Increase driver's productivity
7. Increase usage of tonnage
8. Reduction of accidents
9. ……………………………………
10. ……………………………………

(Complete the list)

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard - Example of Goals

PROCESS EFFICIENCY

1. Automated ordering system
2. Optimizing routing
3. Increase drop size
4. Overnight deliveries
5. ABC approach for inventory analysis
6. Direct deliveries
7. Optimized picking methods
8. Groupage with collaborating companies
9. …………………………
10. …………………………

(Complete the list)

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard - Examples of Goals

CUSTOMER SATISFACTION

1. **Reduction of clients' complaints**
2. **Clients Rating**
3. **Reduction of damaged products due to storing and transport**
4. **SLA Rating (Service level Agreement)**
5. **Delivery time**
6. **Repairs and maintenance network**
7. **Response time of repairs and maintenance**
8. **Reduction of back orders**
9. **…………………………..**
10. **……………………………**

(Complete the list)

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard - Example of Goals

ORGANIZATIONAL CAPACITY

1. **Innovative Ideas**
2. **Inclusion and Diversity**
3. **Learning hours**
4. **Employee turnover**
5. **Employees' Morale**
6. **Knowledge management systems**
7. **Rotation programmed**
8. **Talent Acquisition**
9. **………………………………**
10. **……………………………….**

(Complete the list)

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard

Robert S. Kaplan and David P. Norton

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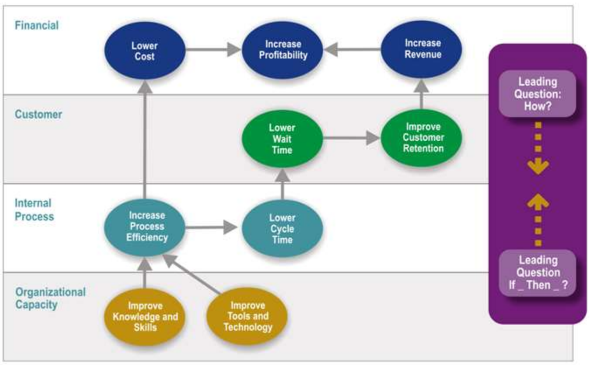
6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard



The non financial goals interact and, in the end, optimize the financial goals

The Strategy Map illustrates how value is created within the organization

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard

a. The Learning & Growth Perspective

- Very important to company with intense knowledge
- Good for individual and company's improvement
- Education and training should be prioritized and specific
- **Learning is more than training**.
- Learning involves mentors, tutors, ease of communications between co-workers, technological education tools

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard

b. The Business Process Perspective

- Refers to the internal business operations
- The performance indicators of which assist managers to assess their department's performance and the extent to which their products or services satisfy the customer's expectations
- Operations exist to ensure the achieving of goals
- Operations should always cost less than the value they create
- The performance indicators should be created by those who have a deep understanding of how the operations work

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6.1.01.09 Performance Scorecard

C. Models

C1. Balanced Scorecard

c. The Customer Perspective

- Frequently, we are reminded how important customer focus and customer satisfaction is.
- Even if the company's current economic performance is satisfactory, we should always be alert for signs of underperforming in these areas (customer satisfaction), because our customers might switch to competitors. Subsequently, worsening the company's economic performance.
- The customer's satisfaction indicators should be made for each consumer category and for the consumer need the company's product or service caters to

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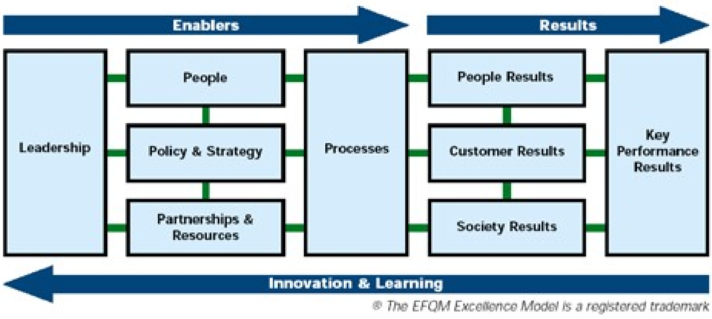
C. Models

C2. EFQM

European **F**oundation for **Q**uality **M**anagement
established in 1989 by 67 leading companies



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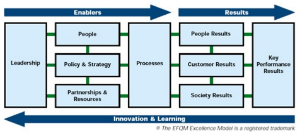
6.1.01.09 Performance Scorecard

C. Models

C2. EFQM



EFQM Excellence Model gives the ability to understand the relationship between the reasons and consequences of the action that the organization takes and assess the success

The EFQM model consists of:

The Fundamental Concepts of Excellence : Determines the fundamentals which constitute the framework for achieving excellence

The Criteria : Provide the frame for putting the Fundamental concepts and the RADAR logic into practice

The RADAR : Tool used for the systemic improvement in all departments and operations of the company

The model can be used in any type of organization

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6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

"All European organizations, both in the public and private sectors, are facing new challenges. The increasing pressure to compete on a global stage with limited resources means we all have to work together to secure our future prosperity, and that of generations to come. The EFQM Excellence Model provides a framework that encourages the cooperation, collaboration and innovation that we will need to ensure this goal is achieved."

Herman van Rompuy, President of the European Council

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6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

The Fundamental Concepts of Excellence :

- Adding Value for Customers
- Creating a Sustainable Future
- Developing Organizational Capability
- Harvesting Creativity & Innovation
- Leading with Vision, Inspiration & Integrity
- Managing with Agility
- Succeeding through the Talent of People
- Sustaining outstanding Results

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6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

The Criteria

Enable Criterion :

What a company must do to implement its strategy

- Leadership
- Strategy
- People
- Partnership and Resources
- Processes, Products and Services

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6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

The Criteria

Results Criterion :

The results that will be achieve simultaneously with strategic goals

- Customer results
- People results
- Society results
- Business results

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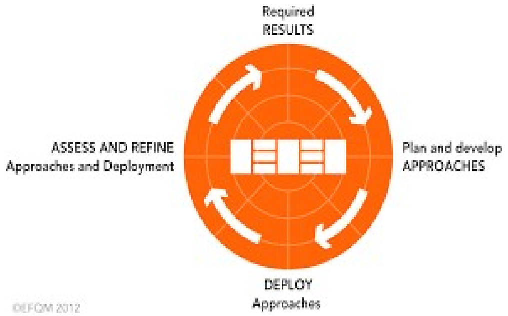
6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

Radar logic (**R**esults, **A**pproaches, **D**eployment, **A**ssess, **R**efine)

It is a dynamic framework used as a tool for assessment and management



Provides a structured approach to reflect on the company's performance

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6.1.01.09 Performance Scorecard

C. Models

C2. EFQM

Radar logic

A company must:

- Determine the **results** that it pursues as part of its strategy
- Organize the **approach** of getting results
- **Deploy** its approach systematically to ensure implementation
- **Assess and refine** the approach the was chosen based on the results and conclusions

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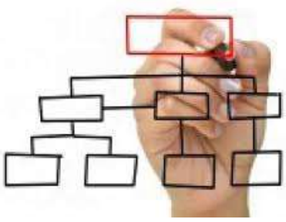
Slog - MODULE A :
BUSINESS PRINCIPLES

6.1.01.10 Organizational Structure

Designs an appropriate organization structure



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6.1.01.10 Organizational Structure

A. Specialization

A1. Types and number of specialization

Specialization

It is a method of production that focuses on a limited amount of products or services aiming at higher productivity.

For example, in a factory, specialization can be seen when the production line uses a work station for a specific task, e.g. car seat assembling at car factory

The exact opposite approach is called **group production**, where a group of employees are responsible for all the tasks necessary.

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6.1.01.10 Organizational Structure

A. Specialization

A1. Types and number of specialization

Exercise :

1. **What are the advantages of specialization?**

2. **What are the advantages of not specializing?**

3. **Under what condition it is beneficiary to use specialized staff?**

4. **Under what condition it is beneficiary to use unspecialized staff?**

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6.1.01.10 Organizational Structure

A. Specialization

A1. Types and number of specialization – SWOT Method

Strengths: 1. What I am good at? What are my strengths? How can I improve my strengths even more? 2. What unique resources can I employ or attract? 3. What strengths other people perceive you possess?	**Weaknesses:** 1. What weaknesses can I improve upon? 2. Where do you lack from your competition? 3. What weaknesses other people perceive you have?
Action Plan (what, how, when, who)	**Action Plan (what, how, when, who)**
Opportunities: 1. What opportunities are accessible to you? 2. Could you take advantage of any changes? 3. What opportunities can you build upon your strengths?	**Threats :** 1. What is the competition doing? 2. What changes might impose a threat? 3. What threats are your weaknesses imposing you to?
Action Plan (what, how, when, who)	**Action Plan (what, how, when, who)**

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6.1.01.10 Organizational Structure

A. Specialization

A1. Types and number of specialization – SWOT Method

- With this methods we can examine:
- the **Strengths** and **Weaknesses** of the organization
- The **Opportunities** and **Threats** that can arise

- In order to choose the necessary actions to:
- Utilize our **strengths**
- Improve on our **weaknesses**
- Exploit any **opportunities**
- While, minimizing the **threats**

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4.1.01.05 Comparative assessment and performance management

B. Steps for Improvement

SWOT Exercise - Individual Professional Assessment

Strengths: 1. What I am good at? What are my strengths? How can I improve my strengths even more? 2. What unique resources can I employ or attract? 3. What strengths other people perceive you possess?	**Weaknesses:** 1. What weaknesses can I improve upon? 2. Where do you lack from your competition? 3. What weaknesses other people perceive you have?
Action Plan (what, how, when, who)	**Action Plan (what, how, when, who)**

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4.1.01.05 Comparative assessment and performance management

B. Steps for Improvement

SWOT Exercise - Individual Professional Assessment

Opportunities: 1. What opportunities are accessible to you? 2. Could you take advantage of any changes? 3. What opportunities can you build upon your strengths?	**Threats :** 1. What is the competition doing? 2. What changes might impose a threat? 3. What threats are your weaknesses imposing you to?
Action Plan (what, how, when, who)	**Action Plan (what, how, when, who)**

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6.1.01.10 Organizational Structure

B. Organizational Shape

B1. Number of Staff

The number of staff under a specialty is determined by:

1. The total annual output (W) (e.g. no of trips)
2. The output (w) that an employee can achieve in a day
3. Utilization factor (u) of the employee's output deducting the non working hours (leaves, days-off, accidents, equipment maintenance, non smoothed demand, etc.). Due to these reasons the employee cannot can not produce the output expected from his position

The formula that can calculate the number of staff required is :

Number of staff: $\boldsymbol{N = W / w * u}$

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6.1.01.10 Organizational Structure

B. Organizational Shape

The organizational shape must be formed in such way to be dynamic to implement the strategy of the Organization

When the strategy is changed or evolved, the shape must adapt to such changes.

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6.1.01.10 Organizational Structure

C. Distribution of Power

C1. Centralized

- **Power** and **decision making** is concentrated to the Central Structure
- Local organizations have little ability to make decisions
- Usually decisions delay due to luck of knowledge on the issues, to lack of information, to overloading of the central structure with issues of all the local organizations, to distancing from the problems
- Decisions are more **objective** because they are not biased by the relationship of the local organizations with the problem environment and because they are assessed using the same criteria applied everywhere
- **Central consulting and administrative** teams are utilized better
- **Tighter control** of operations
- **Unified and standardized** operations, policies, systems

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6.1.01.10 Organizational Structure

C. Distribution of Power

C2. Decentralized

- Part of **power and decision making** is given to decentralized structures.
- The decision making process is **speeded up** because of the awareness of issues, close proximity to the problems, better risk identification.
- Decisions are less objective because they are biased by the relationship of the local organizations and because they are not assessed with the application of the same criteria. Usually, decentralized structures decline from the Central structure directions
- Perfect environment for training and exposure to new issues for new employees
- Filtering and adaptation of decisions to local conditions
- ……………………………
- ……………………………

c

6.1.01.10 Organizational Structure

C. Distribution of Power

Other Forms

Globalized

Investments are decided without the influence of the local or national environment. The power consequently is distributed in the same pattern.

«Glocalized» – Matrix

Distribution of power follows a mixed structure. In some issues power remains in global level while in other in the local level. For this type of distribution of power, it is usually used the term "glocal" structure, defined by the mindset: globally think – locally act. Strategic, marketing and reporting issues are decided by the central structure, while operational issues (e.g. storing, transportation, maintenance, customer crelations, etc.) are decided by the local structures.
In turn, the reporting lines of the organization are prepared accordingly.

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6.1.01.10 Organizational Structure

D. Departmentalization

Departmentalization is the grouping of similar tasks and operations in departmental units in order to achieve the company's goals in the most efficient and effective way possible

Departmentalization can be done according to:

- ***Function***
- ***Process***
- ***Product***
- ***Market***
- ***Customer***
- ***Geographic Area***
- ***Matrix – Project organization***
- ***Combination of the above***

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6.1.01.10 Organizational Structure

D. Departmentalization

D1. Functions

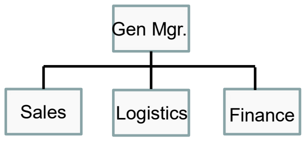
Departmentalization by function is one of the oldest and common types of departmentalization.

Advantages: specialization by function (operations, marketing, finance, etc.) leads to focused and efficient operations.

Disadvantages : each department focuses on its goals risking to distance itself from the goals of other department and the entire organization's. In some cases, departments risk working against some other department's interests in order to achieve their own goals.

Critical Parameter: Perfect (horizontal) information and strong acts of coordination by the general manager are required.

Example (Disadvantage):



The administration of the Logistics department is under pressure by the Finance department, the logistics department cuts down on stock significantly and as a consequence the company faces a decrease in sales

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6.1.01.10 Organizational Structure

D. Departmentalization

D2. Products

Departmentalization by product is used when deep understanding of the products is required. It is usually used by big companies (e.g. petroleum, chemical companies)

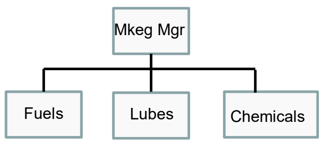
Advantage : constant product improvement, focused on profitability by product, employees' specialization

Disadvantage : each department focuses on the its goals while the customer is visited by different sales people that might give the impression of conflicting goals

Critical Parameter: Perfect (horizontal) information and strong acts of coordination by the marketing manager are required.

Example (Disadvantage):

The marketing manager working in the fuel industry has little interest in chemical products, that the business starts to shrink.



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6.1.01.10 Organizational Structure

D. Departmentalization

D2. Workflow/Process

Departmentalization by process helps with the concluding of workload, avoiding mistakes and delays. It is usually used for big transporting volume. (e.g. Courier company)

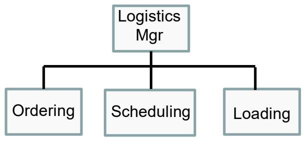
Advantages : Smooth workflow, control and monitoring of the status of a transport, software integration, etc.

Disadvantages : Lack of flexibility, unresponsive to unpredictable situatuins, low employees' satisfaction, delays cause more delays further down the line

Critical Parameter: Reorganizing of processes, automation and flexibility are required

Example (Disadvantage):

The ordering department is in office 9am to 5pm, as a result orders that come through after 5pm will be processed from 9am the next day.



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6.1.01.10 Organizational Structure

D. Departmentalization

D4. Markets

Departmentalization by market is useful when high quality of services needed to be provided to different types of markets.

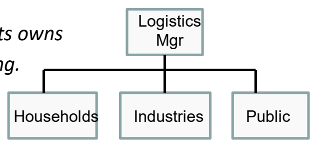
Advantages : Focused on different markets, specialization, better understanding of customers' needs.

Disadvantages : Unable to transfer employees among departments, risk of losing a clear brand image when the markets are not similar, underuse of equipment

Critical Parameter: Resources must be constantly used effectively regardless the fluctuations of the tasks for the different markets

Example (Disadvantage):

A moving company operating in three different markets owns small vans for households, for which demand is growing. On the other hand, they own big trucks for their industrial clients, for which demand is declining.



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6.1.01.10 Organizational Structure

D. Departmentalization

D5. Geography

Departmentalization by market is useful when high quality of services needed to be provided to different geographic areas.

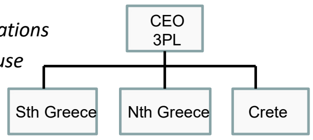
Advantages : Focus on different geographic areas, specialization, better understanding of customers' needs by geographic areas, lower transport costs, better customer relations

Disadvantages: Unable to transfer employees among geographic areas, tendency of "running independently" from the other areas, high costs of middle management

Critical Parameter: Unified processes, central system, inspections

Example (Disadvantage):

A 3PL company with warehouses in 3 different locations and faces a problem with convincing all 3 warehouse managers to use the same system and policies



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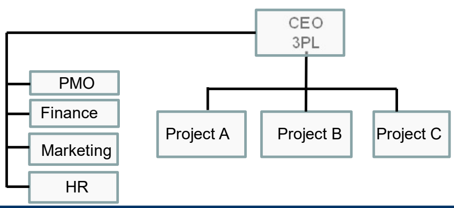
6.1.01.10 Organizational Structure

D. Departmentalization

D6. Projects

Departmentalization by project is useful for companies that are responsible for carrying out big projects. The staff is distributed to project teams and when the project is completed they return to their initial responsibilities, until they are called upon for a new project.

It is also called matrix, because while there is a departmentalization by project, there is simultaneously one by function. Usually, certain authorities and common tasks *(procurement, reporting, Safety, design, etc.)* consist the PMO *(Project Management Office)*



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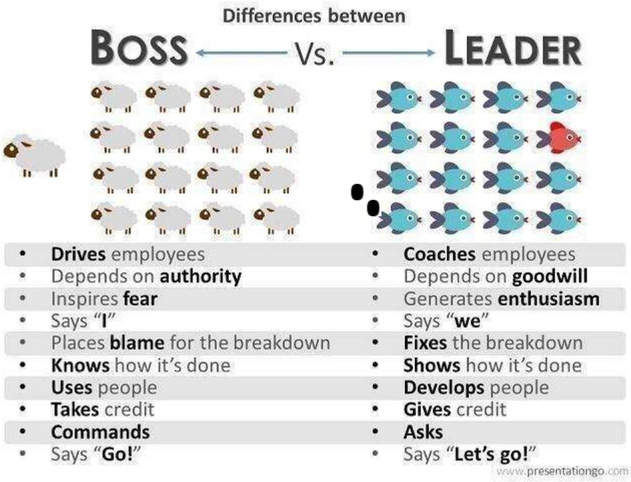
6.1.01.11 Various



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