Centre for the Development of Enterprise

Integral Diagnostic Review

Final Report

White Angels
t/a Dream Flavours (Pty) Ltd

May 14 - 16, 2014, Gaborone-Botswana

Summary

- Background
- Diagnosis process
- Preliminary results
- Recommendations

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The Company's Diagnostic Process

- Company's background review
- Interview with the management and staff to understand the different elements of the company (14 May 2014)
- Co-construction (management validation of preliminary findings)(15 May 2014)
- Final reporting (16 May 2014)

Background

- White Angels t/a Dream Flavours Pty Ltd was registered in 2009 and started operations in 2010 in Molepolole, 45km from Gaborone.
- The company is owned by 5 shareholders, 3 of which double as employees while the other two are non-active directors
- The company specializes in production of Yoghurt, Sour Milk, Ice Pops, and Juices
- The company's vision is to be a leader in supply of yoghurt in the local market and to eventually participate in the export market
- The company procures raw materials from RSA and Botswana
- The company's main customers are hotels and general dealers
- The company was initially funded by Gender Affairs to the tune of P270, 000. The money was used to purchase machinery. A further P361,000 generated from sales has been ploughed back into the company from 2010 to 2014
- A loan of P200,000 was obtained in 2011 from FNB to fund purchase of refrigerated truck and working capital
- The company has 9 employees including the three shareholders
- The company's annual turnover has been going up and down: 2010 – P328, 465, 2011 – P700, 861, 2012 – P643, 852, 2013 – P323, 784.
- The company's main challenges are limited industry experience and shortage of working capital

Preliminary Findings

Preliminary Findings

Subareas Needing Improvement (Refer to co-construction report for justification)	
Strategic Management • Mission - Vision • Strategic Objectives	**Organizational Structure** • Decision Making Power
Marketing and Sales • Segmentation, Target Market, and • Price	**Quality Management** • Quality Control • Procedures • Product quality
Production and Operations • Suppliers • Planning • Plant Layout	**Human Resources** • Staff Performance • Personnel Policy
Finance • Cost Analysis	**Technological Innovation** • Execution of Innovation Projects

Results

The Company Strengths and Subareas of Intervention

Strengths	Subareas of Intervention
1. There shareholders are committed to achieving business success	1. Strategic Management – Strategic Objectives
2. The complies with necessary regulatory requirements	2. Marketing and Sales - Segmentation, Target Market, and Positioning
	3. Production and Operations - Providers
	4. Finance- Cost analysis
	5. Human Resources – Staff Performance
	6. Quality Management - Quality control
	7. Technological Innovation – Execution of Innovative Projects

Best Practices

Strategic Management – Strategic Objectives

Having strategic objectives and specific projects and action plans will enable the company to:

- Have a clear roadmap
- Develop and prioritize functions and activities
- Better planning (short and long term)
- Better allocation of resources
- Track operational performance
- Improve decision making across the company

The Strategic Process of Value Creation

Best Practices

Marketing and Sales – Segmentation, Target Market & Positioning

Benefits of a proper segmentation is the ability to adapt to the different needs and requirements of the different segments based on specific criteria. This enables informed marketing and positioning. Ultimately this results in:

- Effective focus especially on targets with potential for growth
- Improved inputs into customization for each segment resulting from interaction – product development
- Effective marketing, promotional and distribution plans
- Improved brand awareness and customer loyalty

Ultimately, improve market penetration and increase revenue

Best Practices

Production and Operations - Suppliers

A criteria for selecting and having adequate suppliers:

- Helps the company to identify qualified potential suppliers
- Helps to reduce supplier disruption risks
- Drives competition among suppliers
- Assists the business to achieve supplier diversity
- Culminates in supplier contracts

This ultimately helps the company to reduce procurement costs and increase profits

Best practices- Cont'd

Finance – Cost Analysis

Accurate costing of products:

- Ensures positive cash flows and non tying up of capital on products that are not profitable.
- Makes it easier to estimate the company's break even point (level of sales where all fixed costs are covered by revenue)
- Encourages good procurement methods
- Enables the company to appropriately price its products to secure the profit margin

Therefore contributes to reduce costs and improve profit margin

Best practices- Cont'd

Human Resources – Staff Performance

Documenting staff performance:

- Eliminates misunderstanding about company goals and objectives
- Makes it easy for the company to track employee performance
- Allows for employee growth
- Assists in operationalizing company strategies

This leads to improved company performance and ultimately contributes to profitability

Best practices- Cont'd

Quality Management – Quality Control

There is need for the company to have set documented quality control measures, with specific criteria used in maintaining quality. This will ensure:

- Systematic checks that will allow timely application of corrective measures.
- A clearly defined procedure for handling complaints.
- Less rejection of products.
- Consistency in products quality.
- Improved customer loyalty.
- More sales.

Best practices- Cont'd

Technological Innovation- Corporate Culture for Innovation

Documenting and implementing a corporate culture for technological innovation, will enable the company to:

- Improve services and products to meet client preferences.
- Develop new products to meet clients requirements - product diversification
- Plan and carry out training technical programs for employees
- Introduce incentive system for employees
- Incorporate employees ideas in improving product and service delivery – increased motivation
- Budget for technical innovation

Best practices- Cont'd

Financial Analysis - Disclaimer

- **Disclaimer**

The strategic financial indicators are based on financial statements provided by the company.
The inclusion by the CDE consulting team of these figures and ratios in no way implies verification of the figures and ratios by the CDE consulting team.

The Company's financial year is from 1st August to 31st July of the following year.

Balance Sheet

	WHITE ANGELS BALANCE SHEET				
	ASSETS	**2012/2 013**	**2011/2 012**	**2010/2 011**	**Variation (%)**
1	Cash and cash equivalents	19 583	11 183	25 144	75%
2	Accounts receivable (debtors)	15 245	5 943	18 160	156%
3	Inventory	175 000	55 740	30 627	214%
5	Other Current Assets				
6	**TOTAL CURRENT ASSETS**	**209 828**	**72 866**	**73 931**	**187%**
7	Physical fixed assets	40 757	132 322	223 987	-69%
10	Other Assets				
11	**TOTAL FIXED ASSETS**	**40 757**	**132 322**	**223 987**	**-69%**
12	**TOTAL ASSETS**	**250 585**	**205 188**	**297 918**	**22%**

	LIABILITIES	**2 013**	**2 012**	**2 011**	**Variation (%)**
20	Account payable	344 286	34 229	85 776	905%
21	Short term portion of loans payables	40 000	40 000	20 000	0%
22	Taxes liabilities				
23	Short term provisions				
	Current liabilities				
25	**TOTAL CURRENT LIABILITIES**	**384 286**	**74 229**	**105 776**	**418%**
26	Long term debt to banks and fin. Inst.	100 000	140 000	180 000	-40%
27	Long term Provisions (deferred tax)				
28	Other Long term debt (shareholders loan)	284 217	284 217	284 217	0%
29	**TOTAL LONG TERM LIABILITIES**	**384 217**	**424 217**	**464 217**	**-9.4%**
30	**TOTAL PAYABLE LIABILITIES**	**768 503**	**498 446**	**569 993**	**54%**
31	Paid in Capital	100	100	100	0%
32	Reserves (Retained Earnings, other reserves)	-293 258	-272 175	-272 175	-7%
33	Current year net profit	-224 760	-21 183		961%
34	Other				
35	**EQUITY**	**-517 918**	**-293258**	**-272 075**	**-78%**
36	**TOTAL LIABILITIES**	**250 585**	**205188**	**297 918**	**-22%**

PROFIT AND LOSS ACCOUNT

	PROFIT/LOSS STATEMENT	2012/2 013	2011/2 012	2010/2 011	Variation (%)
37	Sales revenues	323 784	643 852	700 861	-50%
38	Cost of goods sold				
39	*Materials*	95 960	253 965	486 673	-62%
40	**GROSS PROFIT**	**227 824**	**389 887**	**214 188**	**-41%**
41	*Wages & salaries*	48 550	48 500	55 675	0%
42	*Other costs*				
43	**NET VALUE ADDED**	**179 274**	**341 387**	**158 513**	**-47%**
44	Depreciation	91 665	91 665	91 665	0%
45	Operating Expenses (G&A, selling, R&D)	293 325	240 903	282 406	22%
46	**OPERATING INCOME**	**-205 716**	**8 819**	**-215 558**	**-243%**
47	Financial income				
48	Financial expenses	19 044	30 002	12 308	37%
49	Other non-operating income				
50	Other non-operating expenses				
51	**INCOME BEFORE INCOME TAX**	**-224 760**	**-21 183**	**-227 866**	**-961%**
52	Income Tax Provision		0	0	
53	**NET INCOME**	**-224 760**	**-21 183**	**-227 866**	**-961%**

Strategic & Financial Indicators

Strategic Indicators	2012-2013	2011-2012	2010-2011
Local sales per employee (Pula)	35,976	71,539	77,873
Exports as a percent of total sales	N/A	N/A	N/A
Variation of local sales (%)	-50%	-8%	N/A
Net value added, NVA	179,274	341,387	214,188
Productivity (Pula)	19,919	37,932	23,798
Gross profit margin(%)	29.6	60.1	30.6
Net profit margin(%)	-69%	-3%	-33%
Net worth (Pula)	-517,918	-293,258	-272,075
Number of managers to employees	0.11	0.11	0.11

Strategic & Financial Indicators

Financial Indicators	2012-2013	2011-2012	2010-2013
Current Ratio	0,55	0,98	0,70
Acid test (Quick ratio)	0,09	0,23	0,41
Average collection period (days)	17	3	9,46
Average payment period (days)	870	41	57,73
Inventory conversion period (day)	442	67	20.6
Debt to equity ratio	-1,48	-1,70	-2,09
Times interest earned	-10,80	0,29	-17,51
% Over (Under) Break-even point	-53%	3%	-0,58

Best practices- Cont'd

Financial Analysis

Sales and profitability

- Sales continue to decline from 2010/2011 to 2011/2012 by 8% and between 2011/2012 and 2012/2013 from P643,582 to P323, 784 which represents a decline of 50%. The gross profit margin declined by approximately 50% from 60.1% to 29.6% during 2011/2012 and 2012/2013 financial year periods. This points to deficiencies in the management of purchase and inventory system .
- While sales decreased by 50% in 2012/2013, operating expenses have increased by 20%, resulting in a record level of loss for the year 2012/2013 (-P224 760)
- Company has operated below break-even point in 2012/2013, reaching a record low (-53%).
- Sales decline has mainly been due to the low product quality which led to loss of major clients

Best practices- Cont'd

Financial Analysis

Working capital

- Average debt collection period has increased from 3 to 17 days.
- The average supplier payment period increased from 41 days to 807 days .This has affected the credit worthiness and goodwill of the company.
- The net working capital became more negative -P1,343 to -P174,458 in the period indicating that the firm does not have sufficient funds to satisfy both maturing short term debt and operational expenses.
- The inventory conversion period increased from 67 to 442 days which implies that the period taken to convert stock into cash has drastically increased. This also indicates that the company's cash is tied up in low moving stock.

Best practices- Cont'd

Financial Analysis

Solvency

• The current ratio has dropped from 0.98 in 2011/2012 to 0.55 in 2012/2013. The desired figure is 2, indicating that the company will not easily meet its current obligations.

•The acid test ratio has worsened from 0.23 in 2013 to 0.09 in 2012/2013. This indicates that the company's state of solvency has declined.1 is a healthy level .

•The net profit margin has improved from -33% to-3.0% between the 2010/2011 and 2011 /2012 financial year. However it declined to -69% during the 2012/2013 financial year.

•The company's debt/equity ratio has improved slightly from -1.7 to – 1.48 during the period. This points negatively to its ability to source external finance; bank loans etc . However this remains negative and is related to negative equity.

•Times Interest Earned ratios declined from 0.29 to -10.8 .This is an indication that the company currently does not have the ability to meet its interest commitments.

Best practices- Cont'd

Financial Analysis

Conclusion :

- The company is not financially sound. They are operating at 53% below break even point. The operating expenses have increased and sales have declined resulting in significant loss for year 2013. Company's equity base is completed depleted reflecting accumulated losses over the last three years. (-517,918 for 2012/2013 financial year). Similarly, net working capital has been negative for the 2 to 3 consecutive years indicating that the firm does not have sufficient funds to satisfy both maturing short term debt and operating expenses.
- The company is facing bankruptcy and very exposed to closure risk.
- The company will need to be recapitalized .

Conclusions of the Diagnosis

Conclusion

Conclusion

- White Angels t/a Dream Flavours is a propriety limited company located in Molepolole, 45km from Gaborone. The company is owned by 5 shareholders, 3 of which double as employees while the other two are non-active directors.
- The company turnover for the year ended 2013 is P323, 784, a decline of almost 50% from the previous year. The company has been running at a loss for the past three years.
- The main challenges facing the company has been product quality issues, lack of skills and lack of industry experience. The company has since purchased a tool for checking milk quality upon receipt.

Conclusion

Conclusion

- The company is at growth stage where issues of cash flow and profitability are critical. White Angels has been running at a loss mainly because of low sales associated with product quality issues and inability to compete with imported product
- Our assessment have revealed that the subareas that require interventions are: strategic objectives, marketing and sales, production and operations, quality control, cost analysis, staff performance and execution on innovation projects.
- The company has been struggling to service its debt and is also facing working capital challenges
- The company needs to close the gaps in the above indicated subareas in order to regain its competitiveness in target markets.

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Recommendations For Improvement

SUB-AREAS	RECOMMENDATIONS	
	INTERNALLY	WITH SUPPORT OF EXTERNAL RESOURCES
STRATEGIC MANAGEMENT - STRATEGIC OBJECTIVES	➢ Formulate and document company mission and vision ➢ Formulate and document company objectives and strategies.	➢ Assistance with the formulation and development of strategic objectives and plan
SEGMENTATION, TARGET MARKET & POSITIONING	➢ Update customer database with description of specifications ➢ Develop criteria for segmenting customers ➢ Target groups with growth potential where the company has competitive advantage ➢ Clearly identify the needs of each category	➢ Support to undertake a light market research to understand market dynamics

SUB-AREAS	RECOMMENDATIONS	
	INTERNALLY	WITH SUPPORT OF EXTERNAL RESOURCES
PRODUCTION AND OPERATIONS – SUPPLIERS	➢ Develop selection criteria for suppliers ➢ Conduct supplier research with a view to select the most reliable suppliers that offer favourable payment terms and quality raw materials ➢ Diversify supplier base ➢ Formulate guidelines for procuring and receiving materials	➢ Enlist help of industry expert in the field of business
FINANCE COST ANALYSIS	➢ Clearly identify all fixed and variable costs ➢ Update the existing pricing to ensure all costs are captured ➢ Constantly reconcile the costing with financial records ➢ Explore possible cost saving areas that could lower input costs	➢ Enlist the help of a cost accountant to develop an effective cost structure and implement a costing system

SUB-AREAS	RECOMMENDATIONS	
	INTERNALLY	**WITH SUPPORT OF EXTERNAL RESOURCES**
HUMAN RESOURCES – STAFF PERFORMANCE	➢ Develop performance targets ➢ Implement performance monitoring system ➢ Enhance the skill and competency of staff	➢ Enlist assistance to develop and implement PMS system ➢ Engage business oriented manager
QUALITY MANAGEMENT – QUALITY CONTROL	➢ Establish clientele preference ➢ Implement and document recognized standards such as BOBS ➢ Identify and document critical control points which should be adhered to ➢ Implement quality check procedures ➢ Formulate and implement pest control policy ➢ Bench marking with factories producing similar products	➢ Enlist the assistance of experts in this field of business

SUB-AREAS	RECOMMENDATIONS	
	INTERNALLY	WITH SUPPORT OF EXTERNAL RESOURCES
EXECUTION OF INNOVATION PROJECTS	➢ Set up innovation process ➢ Allocate budget for innovation projects ➢ Recognize and reward employees for innovation	➢ Assistance with setting up an innovation scheme

Priority Intervention

To improve growth and profit margins, the company should develop and implement a turnaround strategy. This implies the following.

- **Improve staff performance**
  - Enhance technical skills of staff especially about the industry that the company is operating in
  - Set up performance targets for employees
  - Set up performance management system
- **Improve on Quality Management**
  - Establish clientele preference
  - Implement and document recognized standards such as BOBS
  - Identify and document critical control points which should be adhered to
  - Implement quality check procedures
  - Formulate and implement pest control policy
  - Bench marking with factories producing similar products
- **Market segmentation and differentiated marketing**
  - Further investigation of the market to determine the targets and where the company has competitive advantage.
  - For each segment to develop product pricing and communication appropriately
  - Established a sales force in order to generate new business

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Thank You