

Business Analysis Project

Session 8- Assignment Guidelines

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Assignment Criteria

1. Research on industry sector and selected organisation, referencing (10 marks)
2. Detailed financial analysis, including financial spreadsheet modelling of recommended strategy options (15 marks)
3. Analysis, interpretation and discussion of strategic issues (30 marks)
4. An appraisal of the limitations of financial models and conventional analysis (10 marks)
5. Conclusions and Recommendations (20 marks)
6. Quantitative Modelling Recommended Strategy (15 marks)

Report Structure

1. Introduction
2. Analysis of Current Financial Performance
3. Analysis of Strategic Issues
4. Conclusions
5. Recommendations
6. Limitations of financial models and conventional analysis

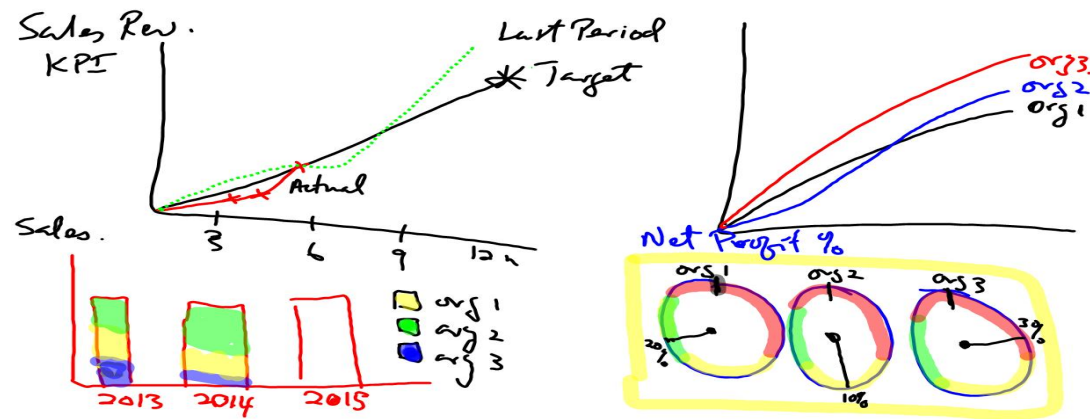
1. Introduction

- Give an introduction of industry of choice
- Give an overview of industry forecast, next 3 years, you can use expert reports e.g. Bloomberg, Yahoo finance, Marketline
- Choice of Organization- give brief overview of business, vision, mission, objectives and their current strategy
- Choice of Benchmarking Organization- state the 2 organization and justify why they were chosen e.g. similar or best in class

2. Analysis of Current Financial Performance

- Select Financial Indicator (Ratios) See next slide.
- Calculate for Focus Org and 2 Benchmark Org for a 3 year period
- Use an Excel Spreadsheet to do calculation. Place in appendix
- You can use sub sections for the discussion e.g. Profitability, Liquidity, Working Capital

- Present Ratios using a dashboard with graphs and charts



- Narrative analysis is needed, discuss performance over the last 3 years
 - Are we meeting targets?
 - What is the trend? Increasing/decreasing?
 - What is the % change? Positive/negative?
 - Make sure to include a comparison to the 2 Benchmark Org
- Summary of Key Financial Issues- here you present the gaps i.e. areas of weak performance.

Ellis, J and Williams D (1993), Competitive Strategy and Financial Analysis, Pitman , page 235

| | Ratio | How calculated | Interpretation |
|------------------|-------------------------------------|--|--|
| Operating ratios | Overall Performance | | |
| | Gross profit | Turnover minus direct costs of making product or providing a service | |
| | Operating Profit | Gross profit minus operating costs | Shows whether operation is financially sustainable |
| | Return on Capital Employed % | Operating profit / Average capital employed x 100 | Provides an overall measure of corporate performance |
| | Net Profit Margin % | Operating profit / Turnover x 100 | Describes the % profit for each £ turnover after direct & indirect expenses have been deducted |
| | Asset Turnover (X) | Turnover / Average capital employed | Shows how many times sales generated from the capital employed |
| | Working Capital | | |
| | Stock Turnover (X) | Cost of sales / Stocks | Indicates how many times stocks are being turned over in a year |
| | Debtor Turnover (X) | Turnover / Trade debtors | Number of times trade debtors are rotated in a year |
| | Working Capital to Turnover ratio % | (Stocks + trade debtors – trade creditors) / Turnover x 100 | Provides a measure of the overall working capital needs of the company. High ratios suggest working capital needs are greater. |
| Financial ratios | Debt Ratios | | |
| | Gearing Ratio % | Total borrowings / Capital employed x 100 | Measures extent of borrowings in relation to capital employed. |
| | Debt–equity ratio % | Total borrowings / Shareholders' funds x 100 | Relates total debt to shareholders' funds to indicate how company is financed. |
| | Interest Cover (X) | Profit on ordinary activities before interest / Interest paid | How many times profits cover interest payments. A measure of the ability to service debt. |
| | Liquidity Ratios | | |
| | Current Ratio (X) | Current assets / Current liabilities | How many times current assets cover current liabilities |
| | Acid test (X) | Current assets less stocks / Current liabilities | Current ratio less stocks. A more stringent test of liquidity |

3. Analysis of Strategic Issues

- Maximum 2 models
- **3.1 PESTLE Analysis**
 - **Discuss each factor individually**
 - Use evidence to support claims
 - Present summary table of PEST factors for Organization

| Political | Economic | Social | Technology |
|-----------|----------|--------|------------|
| • X | • X | • X | • X |
| • Y | • Y | • Y | • Y |

- **Identify the Key Driving Forces.** Use a diagram to present
- Must **discuss the impact and implications of the key driving forces** to the Organization and Industry
- Summarise using ETOP Analysis. See Next Slide for example.

Example ETOP analysis

| Macro-environmental factor Issues | Influential impact | | | | Conclusion Implication |
|--|--------------------|-------|---------|-------|--|
| | Opportunities | | Threats | | |
| | Major | Minor | Major | Minor | |
| <i>Political issues</i> | | | | | |
| Political climate | | | | | |
| A trend of political reform in pursuit of democracy | × | | | | Greater freedoms, security and a reduction of political risk |
| Legal system based on French civil and customary legal systems | | × | | | Standard practice throughout the region |
| Support to international business | | | | | |
| Investment codes in the region | × | | | | Secure environment for international investors |
| guarantee uniform rights for national and foreign businesses and the freedom to transfer capital, resources and salaries | | | | | |

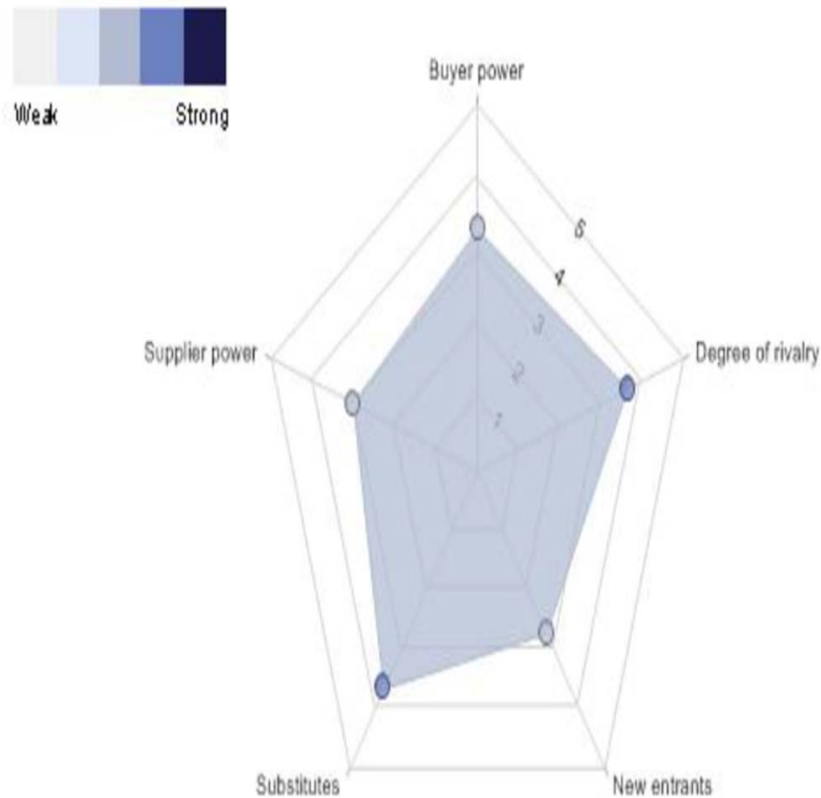
Instead of X you Could use a score -5 to 5 to represent Threat/Opportunity and its impact. – scores would be threat, + scores would be opportunity.

• 3.2 Five Forces Analysis

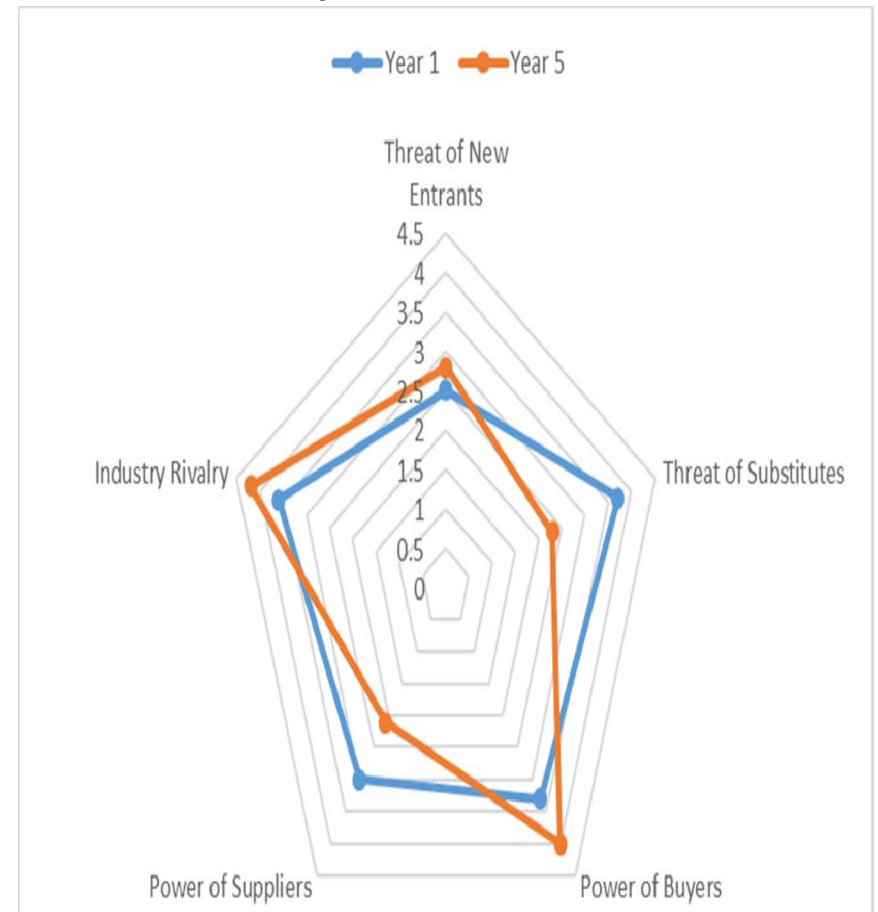
- Use a Quantitative analysis
- Discuss each factor individually
- For each Force identify the key influencing factors
- Use Radar Chart for each Force. See example below
- Must **discuss the impact and implications of the key influencing factors** to the Organization and Industry



- Present overall Radar chart for Five Forces

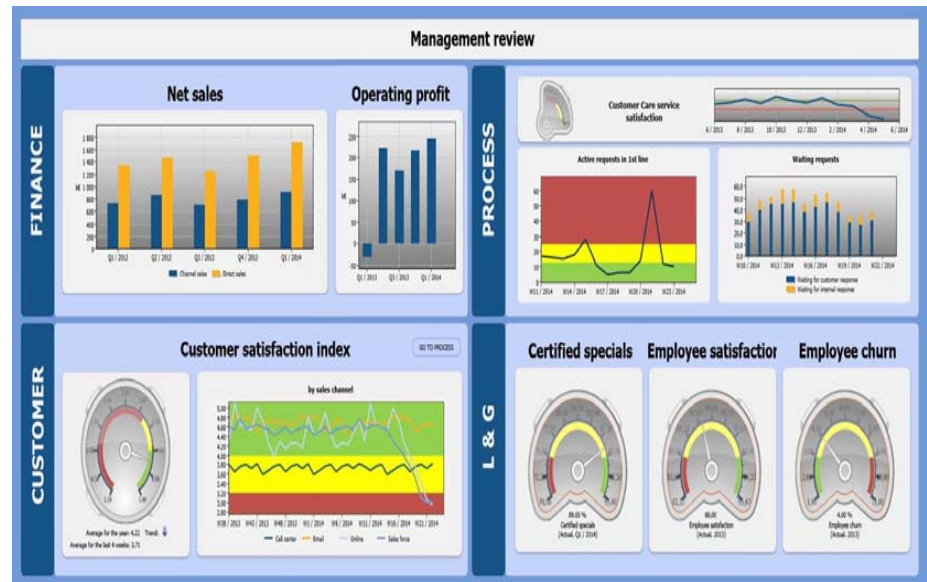


- Present Radar chart for next 3-5 years



Must provide a discussion of the key driving forces of competition and its impact on the organization

- **3.3 Balance Scorecard**
 - Select industry specific KPI
 - Present dashboard of KPI's
 - Benchmark if possible
 - **Write discussions on the performance of the organization**
 - Are we meeting targets?
 - What is the trend? Increasing/decreasing?
 - RAG Status?



- **3.4 Summary of Strategic Issues**

- Provide a brief discussion of the key issues arising out of the PEST, Five Forces, Balance Scorecard analysis
- Use:
 - ETOP analysis and Key Driving Forces Diagram
 - Five Forces Overall and next 3-5 years Radar Chart
 - Balance Scorecard dashboard
 - to get the key points

4. Conclusions

- must link strongly with the earlier parts of the report and **pull together your findings**
- **restate the key issues** that you have identified and your major findings
- **Use the summary of Key Financial Issues**
- **Use the summary of key Strategic Issues**

5. Recommendations

- Based on the analysis and conclusions, you must now **recommend an appropriate Strategic Option** for the Focus Organization
- It must address these key issues and major findings
- **5.1 Strategic Choice**
 - Present the Strategic Options- using appropriate models e.g. Porter's Competitive Strategy, Bowman's Strategic Clock, Ansoff Matrix, BCG Matrix etc.
 - Narrow down to 2 or 3 options
 - Evaluate and **Choose ONE**
 - Could use a **Decision Tree Analysis** or **Weighted Rank Analysis** for the selection

- **5.2 Modelling of Strategic Choice**

- You must model your recommendations in the financial spreadsheet model from section 2
- make some assumptions on costs, sales etc. and input these to the model
- State these assumptions
- Add the prediction for the next 3 years (Sensitivity Analysis)
- Calculate new financial ratios for the next 3 years
- Print spreadsheet in body

- **5.3 Suitability, Acceptability and Feasibility**

- discuss and interpret the financial and other outcomes of your recommendations

5.3.1 Suitability

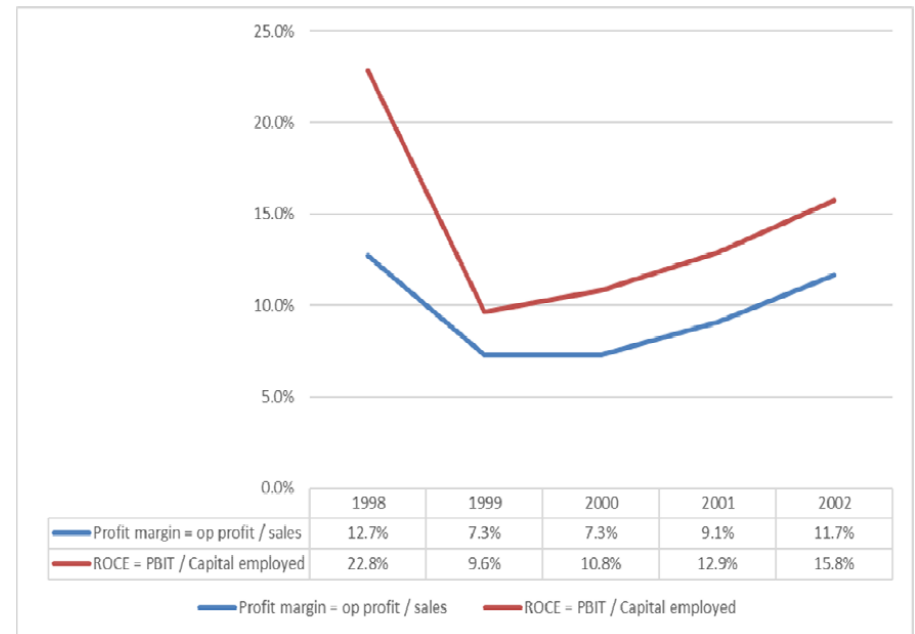
- Assess strategic fit. Discuss whether or not the new strategy:
- Will exploit the opportunities in the environment and avoid the threats?
- Will capitalise on the organisation's strengths and strategic capabilities and avoid or remedy the weaknesses?
- Use Ranking to demonstrate suitability against key strategic factors. See example below.

Score: 0-5

| Strategic options | Take Adv | | mitigate | | Total Score |
|--------------------|----------|---|-----------|---------|-------------|
| | S | O | Strengths | Threats | |
| 1. Mkt Penetration | 2 | 4 | 1 | 5 | 12 |
| 2. Prod Dev | 4 | 3 | 5 | 4 | 16 |

• 5.3.2 Acceptability

- Conduct a Cost Benefit Analysis- Spreadsheet
- Calculate: Payback period, Net Present Value, Internal Rate of Return
- Place CBA spreadsheet in appendix- showing above calculations
- **Discuss Payback period, NPV, IRR results in body**
- Use the new financial ratios from modelling spreadsheet
- **Present new Ratios using a new dashboard with graphs and charts for the next 3 years in body**
- Narrative analysis is needed, discuss projected performance for the next 3 years
 - What is the trend?
Increasing/decreasing?
 - What is the % change?
Positive/negative?
- Is the new strategy Acceptable?



Summary- Criteria for Acceptability

| Criteria | To Understand | Examples | Limitations |
|------------------------------|--|--|--|
| Return | | | |
| Profitability | Financial return on investments | ROCE Payback period DCF | Apply to discrete projects Only tangible costs/benefits |
| Cost-benefit | Wider costs/benefits (incl. intangibles) | Major infrastructure projects | Difficulties of quantification |
| Real options | Sequence of decisions | Real options analysis | Quantification |
| Shareholder value analysis | Impact on shareholder value | Mergers and acquisitions | Technical detail often difficult |
| Risk | | | |
| Financial ratio projections | Robustness of strategy | Break-even analysis Impact on gearing/liquidity | |
| Sensitivity analysis | Test assumptions/robustness | What if? analysis | Tests factors separately |
| Stakeholder reactions | | | |
| | Political dimension | Stakeholder mapping Game theory | Largely qualitative |

- **5.3.3 Feasibility**

- Do the resources and competences currently exist to implement the strategy effectively?
- If not, can they be obtained?
- Need to consider:
 - The funding required.
 - Cash flow analysis and forecasting.
 - Financial strategies needed for the different 'phases' of the life cycle of a business.

6. Limitations of financial models and conventional analysis

- You need to critique the PEST and Five Forces model
- Please see:
 - Lynch- Strategic Management
 - Johnson and Scholes et al – Exploring Corporate Strategy
- **6.1 Critique of PEST**
- **6.2 Critique of Five Forces**