



# ***CASE STUDY***

***NOVEMBER 2018***

## ***ADVANCE INFORMATION***

**This material is issued prior to the examination session on 7 November 2018.**

**Candidates MUST bring this material with them to the Examination Hall.**

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## **BESPOKE MONOGRAMMING LIMITED (BM): ADVANCE INFORMATION**

This Advance Information is issued prior to the examination session so as to allow you to familiarise yourself with the information provided and to undertake any other appropriate research and analysis. The Advance Information is also published on the website: [www.icaew.com/students](http://www.icaew.com/students).

**You MUST bring this Advance Information with you to the Examination Hall**, annotated if you wish, together with any other notes of your preparatory work. You must carry out sufficient and appropriate analysis work **of your own** in order to have a detailed understanding of the Advance Information. You should also undertake any additional research and analysis you feel necessary to enhance your awareness of the industry and market context and to enable you to clarify any technical terms or other issues of vocabulary. You will need to be able to refer back quickly to the Advance Information and your notes during the exam; you are therefore unlikely to benefit from taking large quantities of additional material with you into the Examination Hall.

At the start of the examination you will receive some additional material which will complete the description of the case scenario and state the Case Study requirements. Your answer must be submitted on the paper provided by the ICAEW in the Examination Hall. Any pre-prepared papers, or papers comprising annotated exhibits from the case material, included in your answer **WILL NOT** be marked.

### **Assessment of the Case Study**

The marks in the Case Study are awarded for professional skills, allocated broadly as follows:

- |  |     |
|--|-----|
| • Assimilating and using information                     | 20% |
| • Structuring problems and solutions                     | 25% |
| • Applying judgement                                     | 25% |
| • Drawing conclusions and making recommendations         | 20% |
| • Demonstrating integrative and multidisciplinary skills | 5%  |
| • Presenting appropriate appendices                      | 5%  |

Of the total marks available, 15% are awarded for the executive summary and approximately 10% for the relevant discussion of ethical issues within your answer to the requirements. Ethical issues do not form a specific requirement but, within a requirement, may cover such topics as:

- Lack of professional independence or objectivity
- Conflicts of interest among stakeholders
- Doubtful accounting or commercial practice
- Inappropriate pressure to achieve a reported result.

You should be clear that marks are awarded for demonstrating your professional skills, not for reproducing facts from the case. In order to be successful, you will need to:

- Demonstrate your knowledge of the case material and make use of your research;
- Carry out relevant analysis of the problems and structure your proposed solutions;
- Apply your judgement on the basis of the analysis that you have carried out; and
- Draw conclusions from your analysis and judgement, and develop them into practical commercial recommendations.

**Omitting any one of these elements will have a significantly detrimental effect on your chances of success.**

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## **November 2018 Case Study: Bespoke Monogramming Limited**

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**Who's who in the BM Case:**

**Borax Beadle (BB) Chartered Accountants**

Afon Crabbe (you)	Trainee ICAEW Chartered Accountant
Penny Price	Partner

**BM**

Gayle Harries	Managing Director
Mo Tenby	Director of Computer Aided Design and Production (CADP) and IT
Viv Baines	Director of supplier evaluation, purchases and inventory
Shelly Drapes	Director of customer evaluation and sales
Ffion Deans	Finance Director (an ICAEW Chartered Accountant)
Carl Morgan	Head of production workshop, warehouse and transport

**About you, Afon Crabbe; your employer, Borax Beadle ICAEW Chartered Accountants (BB); and your client, Bespoke Monogramming Limited (BM)**

You are Afon Crabbe, a final-year trainee ICAEW Chartered Accountant working at Borax Beadle (BB), a firm of ICAEW Chartered Accountants that has operations throughout the UK. You are based at Borax Beadle's office in Cardiff (the capital city of Wales) and work in the business advisory unit. You report to Penny Price, the partner responsible for client development in the business advisory unit.

One of the firm's new clients is Bespoke Monogramming Limited (BM), a company which designs and produces bespoke monogrammed products for supply to businesses in the luxury hotel and related hospitality industry. BB has extensive experience of working with other design organisations and many manufacturing clients, but this is its only design and production client. The BM site, which is based in a business and industrial park on the outskirts of Cardiff, comprises all the company's administrative offices, its design facilities and the monogramming workshop. The site has easy access to the UK motorway network, major rail services and Cardiff airport for domestic and international links.

Since you joined the business advisory unit, your work has included:

- Analysing and assessing clients' financial statements to understand their business and to identify financial issues and concerns relating to their financial activities, as well as providing clear advice to clients based on that analysis and assessment
- Assessing the market in which a client operates, identifying changes or trends in that market and any potential opportunities or threats by reference to the client's relevant strengths or weaknesses
- Performing additional financial data calculations and further financial analysis, to identify and evaluate financial strengths and weaknesses of clients and of their customers and suppliers
- Assessing financial and non-financial information provided by, or affecting, clients and their supply chains to perform a critical qualitative and quantitative review of the issues arising
- Providing clear opinions and reasoned judgements on issues relating to commercial activities – involving financial, operational and strategic considerations – presented by clients or matters which you consider important for any decisions facing those clients
- Drafting reports for clients on all the commercial aspects of their business, including business trust and ethical issues.

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**The design and related production industry**

Almost all organisations which produce goods would claim that they are also heavily involved in product design – which would mean that the design and related production industry covers a vast field. At one end of the spectrum of design and production there are the major manufacturing operations such as the automobile manufacturers. In that highly competitive industry the link between design and manufacture includes all aspects of engineering, including product performance, as well as appearance – and much more besides. At the other end of the spectrum, a marketing operation involved in packaging design might also include itself in the design and production industry – although its designers do not necessarily need to know much about engineering and may need a greater knowledge of artistic composition (together with original flair).

In between there is a vast array of businesses which combine the artistic skill of design with the practical skill of applying that design creation to the production of some final physical product. Many of these organisations are not involved in heavy manufacturing but could more aptly be described as design and production operations. These types of organisations frequently work with products that are partially or fully finished but to which value is added by the additional design work and processing which they provide. Businesses which offer a bespoke monogramming service are part of this industry.

**The bespoke monogramming industry**

Bespoke monogramming operates where companies and other commercial organisations require a corporate logo, or other unique design motif, to be created or adapted, and then monogrammed – by way of stitching or weaving – onto specific products to act as a form of decoration or advertising for the organisation.

In many of the world's luxury hotels, and other equivalent establishments, these specifically designed logos or motifs are monogrammed onto items such as bathrobes, towels and similar products. The effect of monogramming provides a heightened sense of occasion and opulence for their customers. The effect for the hotel is that it is perceived to be offering a higher value and more refined service to its eventual recipients – whether they are paying guests or important visitors. Such products also act as discreet and ongoing marketing.

The industry is characterised by many small businesses competing fiercely against each other. To succeed, an individual company must establish a competitive advantage over its rivals. This can be achieved by high-quality products, superior designs and consistently good customer service. Because the typical monogram design and embroidery businesses are relatively small in nature, they tend to be reliant on a small number of suppliers and a relatively small number of clients. The loss of a client, either because it has experienced hard times or because it has been poached by a rival, can be extremely damaging. Similarly, the fact that an individual monogram design and embroidery business cannot rely on a broad portfolio of suppliers means that operations would be severely disrupted if one of the suppliers increased its prices sharply or went out of business.

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## BM: history and overview

BM is a bespoke monogramming company which offers a design and production service for bathrobes and towels to business clients (such as luxury hotels, spas and exclusive cruise service providers). BM designs specific motifs based on a client's logo or emblems and can incorporate any other refinement according to need. These design refinements might include commemorative dates, events, locations or even relevant artwork related to the organisation. These designs are subject to initial approval by the client. They are then monogrammed and tested on a sample of products before final client approval and full monogramming production occurs.

BM has four key business operations:

- purchasing and inventory (**Exhibit 7**)
- computer aided design and production (CADP) (**Exhibit 8**)
- customer evaluation and making sales (**Exhibit 9**)
- supplier evaluation and contracting for supplies (**Exhibit 10**).

Gayle Harries is the Managing Director of BM. She has been an entrepreneur since her early twenties. Her mother was a needlework teacher in a secondary school, Gayle's grandmother had been a hat maker, and Gayle had inherited these family sewing and business skills. As an accomplished needleworker, after leaving school, Gayle was employed in the small, busy workshop of an upmarket, soft furnishings company called Cardiff Interiors Limited. Here she further developed her commercial machine needlework and workshop production skills.

An opportunity arose when the only daughter of a client was getting married and the honeymoon was to be spent in the UK at Wold Spa – an upmarket residential spa in the Cotswolds, an area beloved of wealthy overseas visitors because of the quintessential “Englishness” of the location. Gayle was asked privately to make the daughter and her new husband some special attire for use in the spa. Gayle agreed and made each of them a set of kimono-style thick linen and cotton luxury quality bathrobes. On each item she embroidered their intertwined initials and the date of their wedding. The personalised present was well-received by the couple but the impact at the spa was to prove even more rewarding. Other spa guests commented favourably on these items, and the spa manager was also impressed.

A few days later the spa manager, Joe Styles, contacted Gayle to discuss whether she would consider making more of these items of clothing for the Wold Spa itself. He outlined what the spa would require, including a special embroidered Wold Spa motif on each item. After discussing design ideas, negotiating delivery terms and agreeing prices and payment terms, the hotel placed an order for 200 sets of bathrobes. For Gayle it was the start of a venture into this monogramming market.

After another month, Joe Styles placed another order. When asked what led to the rapid re-ordering, Joe said: “Our spa customers liked these items and so we let them keep them as a souvenir when they left. We just charged them a nominal price. We have continued to do this: it is good publicity for us because our name and motif are on these products and we do not want old or worn-out items for subsequent customers; and, because we do not have to dispose of lots of old items, it solves a sustainability problem at the same time.”

With the arrival of the second order, it became apparent to Gayle that there was a promising market for these monogrammed products. However, the potential size of this operation would require the setting up of a new business operation and the investment in a more automated production process. By using her personal savings and with financial help from her family, Gayle created a new company to develop this business opportunity.

## **BM overview**

BM was incorporated as a new monogramming company in 2009. In 2010 it leased offices and production space on a site in a business park on the outskirts of Cardiff. This location provides an efficient access to road, rail and air links, with direct routes for both suppliers and clients to keep transport costs to a minimum.

Gayle took advice from others in the trade, but also used her own experience and knowledge of machinery requirements, to make an investment in a computer aided design and production (CADP) monogramming workshop operation. The basis of any monogramming production process is that monogramming machines (which are effectively complex sewing machine workstations) are controlled by a computer program to perform an automated series of stitches, onto base products, using different coloured threads. This process produces the required final motif monogrammed onto the base product.

Initially, the monogramming workshop consisted of eight workstations, linked by computer which could work individually or simultaneously with minimal worker intervention. They are controlled and driven by an IT system in which the required approved design has been programmed. A series of machines select and position the products on which the designs are to be monogrammed. Using this equipment means that the complex embroidery stitching of the monogramming process can be done in minutes for each item. When set up in an appropriate production configuration, the eight workstations combined could monogram up to 100 items per hour (800 in a normal 8-hour shift in a day).

Together with the investment in equipment, Gayle also recruited key employees to assist in the production and other business processes. These included Mo Tenby, who was a specialist in CADP; and Carl Morgan, who had served an apprenticeship to become a specialist in sewing and embroidery machine operations.

Joe Styles proved to be an excellent contact and source of other business. He recommended BM as a supplier to the other hotel spas within his organisation – Boreal Spas – and he also helped to introduce Gayle to some similar organisations with which he had contact.

Gayle makes sure that BM only purchases the best-quality products for the monogramming process. These products are both base products (luxury quality bathrobes, and towels of various sizes) and monogramming materials (top-quality silk and cotton threads). By using only high-quality products and materials, the monogramming process suffers few production failures.

Since its creation, the business has grown strongly because of two main factors: the increasing skill and originality of the BM design team; and the quality of the base product and monogramming work. At the outset, BM took its clients' ideas for motifs, adapted them, and performed a monogramming service based on those (frequently simple) designs. Over time and with increasing experience and confidence, the design element was driven more by the BM design team, but the intellectual property (IP) for the final agreed designs remains with the client. The creative flair of the design team came from the inspirational leadership of Mo Tenby. The production expertise of the workshop team came from the ability of Carl Morgan, who gained confidence in what could be produced in the BM workshop.

There was an important feature of the business from the outset. As Gayle Harries has stated, "BM sells a luxury product, which because of the bespoke monogramming process becomes totally customised. Because of that process, there is then only one buyer for these finished goods. Customer satisfaction is therefore paramount." The combination of ensuring customer satisfaction by supplying a high-quality product combined with constant customer care is the basis for BM's success.

## EMAIL

**From:** Ffion Deans  
**To:** Penny Price  
**Subject:** BM financial and operational history and review of management accounts for the three years ended 30 September 2017  
**Date:** 7 December 2017

Further to your firm's appointment as our business adviser, please find attached a combined set of management accounts for the three years ended 30 September 2017, together with related notes (**Exhibit 5**). BM business activity has been on a steadily increasing basis each year but with occasional more intense one-off activity caused by a prominent anniversary or commemorative event. Revenue increases are a result primarily of increases in sales volume.

**Some general points**

- BM's revenue is from selling products (bathrobes and towels purchased as base products from suppliers) on which we have monogrammed a specific motif based on corporate logos and other emblems according to customer requirements. All sales are invoiced and paid in pounds sterling.
- Customers include luxury hotels and spas and related hospitality industry operations – such as upmarket cruise operators. These customers have their own different business patterns and levels of activity during the year. The overall effect for BM is that there is a constant stream of orders from existing customers throughout the year – both repeat orders and new requests – as well as business won from new customers. There can be surges of activity caused by special events.
- Inventory consists mainly of base products (bathrobes and towels) and monogramming materials – which comprises the embroidery silk and cotton threads used in monogramming. There is very little by way of finished goods or work-in-progress in inventory (see **Exhibit 7**).
- BM relies on prompt deliveries of materials purchased from suppliers. These suppliers are a mixture of UK-based and overseas-based companies. All purchases are made in pounds sterling.
- Non-current assets include property, plant and equipment (PPE):
  - The majority of IT and equipment is CADP equipment linked to the monogramming process. Depreciation rates for all items under this heading are 10-25% reducing balance. In the year ended 30 September 2014, BM upgraded and increased its production capacity to 12 monogramming machines
  - Vehicles include those vehicles used on-site to move inventory, together with vans and cars. Depreciation is 15-25% reducing balance
  - Leasehold improvements relate to the internal upgrading of the premises: depreciation is on a straight-line basis matching the 10-year property lease, which runs until 2020.
- In the management accounts, the relevant depreciation is included either in cost of sales as part of production overheads or in other operating costs, again as a component of overheads.
- In recent years, because of expansion, and working capital demands, BM has operated with a fluctuating bank balance which can change from positive to negative depending on timings of payments and receipts.

## Year ended 30 September 2015

- BM increased its revenue by more than 15% compared with the year to 30 September 2014, both because of increased sales orders from existing customers and through new customers.
- BM employed more skilled staff and apprentices from the local community. (Apprentices are workers – who are frequently school-leavers – given extensive training during their employment.)
- With increased competition between courier services, BM was able to maintain control over its transport costs during the year despite the increase in its sales volume.
- In August 2015, BM recognised a significant bad debt write-off because of the financial collapse of a major client, Majestic Hotels and Spas (Majestic). The collapse occurred with no prior indication of financial problems. At the time of its collapse, Majestic owed BM £222k. The full amount of this bad debt write-off (£222k) is included in other operating costs. The managing director of Majestic, Jan Roper, had provided verbal assurances concerning all its orders, which were completed by BM early in July 2015, but these assurances proved to be worthless when the company collapsed. BM annual sales to Majestic had been more than £600k for each of the previous two years.
- Majestic blamed its collapse on the failure of overseas construction companies to complete two new luxury hotels on time, resulting in complex litigation, substantial loss of business and a cash flow crisis, together with a demand for compensation from its disappointed customers.
- BM’s sales to Majestic had all been monogrammed with an ornate Majestic motif. This meant that any monogrammed products retrieved from the failed business had a £nil net realisable value.

The following schedule summarises the 2015 customer sales and year-end balances. Wold Spa is now represented under Boreal Spas and remains a loyal customer. There are approximately 30 customers under “All others”. Sales to most of these customers were one-off orders of less than £60k in the year.

Customers	2015	2015	
	Annual Revenue	Year-end Receivable	
	£000s	£000s	
Alphonse Hotels	891	32	International hotel group
Boreal Spas	517	22	Luxury spa operator
Cosset Hotels	336	16	UK luxury hotel operator
Deep Wave Cruises	603	28	Luxury cruise operator
Majestic	659	222	International hotel and spa group
Majestic write-off		(222)	
All others	1,789	31	Various
<b>Total</b>	<b>4,795</b>	<b>129</b>	

## Year ended 30 September 2016

- The collapse of Majestic meant that BM lost a significant element of its recurring annual revenue.
- BM had to meet with its bank at very short notice in October 2015 to negotiate a larger overdraft to enable the company to survive.
- Overdraft facilities were increased to £250k to cover the immediate BM financial deterioration and the impact and fluctuations in working capital.
- The detrimental effect in terms of operations and cash flow was particularly hard at the start of the financial year to 30 September 2016. BM had to review and reduce working time for its workforce.
- All other costs were evaluated and subject to tight controls.

- This incident caused Gayle Harries to initiate a review of all customers' creditworthiness. A new system of credit appraisal and control was put in place for all customers. The details of the credit appraisal are given in **Exhibit 9**, together with summaries of customer sales and year-end balances.
- Because of the suddenness and unpredictability of this incident, BM also decided to create a general allowance for the impairment of trade receivables in its management accounts. This allowance was to be calculated as 20% of closing trade receivable balances, for the year to 30 September 2016 and thereafter. An impairment charge, representing the movement in this allowance, is shown in other operating costs.
- Under the circumstances, BM made no new investment in non-current assets and there were no disposals. All non-essential investment activity was put on hold for the year.
- To spread business risk, and to recover from the loss of Majestic's business, Gayle Harries led a marketing and sales drive with a focus on smaller and medium-sized businesses.
- As a result, BM won new business customers including substantial new orders from two hotel and spa operators – one of which is also a luxury cruise operator.
- BM production was lower during the opening months of its financial year but, as a result of this successful marketing and sales drive and the positive determination of all staff to assist the recovery, revenues improved significantly, and production increased as the year progressed.
- Towards the end of this financial year, there were adverse changes in cost of sales caused by the decline in the value of sterling, which resulted in an increase in imported material costs.
- In line with the review of customer risk, a similar review was conducted relating to our suppliers to evaluate the risk to our supply chain (**Exhibit 10**).
- As part of cash management and working capital control, BM exercised tight control over its inventory and reduced the quantity and value held (**Exhibit 7**).
- The bank overdraft fluctuated but recovered from a peak of just over £200k during the year to end the year at £36k.

### **Year ended 30 September 2017**

There is a review of the year to 30 September 2017 and more detail on each of the main business operations following the management accounts.

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**Bespoke Monogramming Limited**  
**Management accounts for the three years ended 30 September 2017**

**Statement of profit or loss**

Year ended 30 September		2017 £000s	2016 £000s	2015 £000s
	Notes			
<b>Revenue</b>		<b>6,661</b>	<b>5,144</b>	<b>4,795</b>
Cost of sales	1	(5,297)	(3,954)	(3,597)
<b>Gross profit</b>		<b>1,364</b>	<b>1,190</b>	<b>1,198</b>
Other operating costs	2	(1,195)	(1,129)	(1,169)
<b>Operating profit</b>		<b>169</b>	<b>61</b>	<b>29</b>
Interest charges		(22)	(32)	(12)
<b>Profit before taxation</b>		<b>147</b>	<b>29</b>	<b>17</b>
Taxation		(29)	(6)	(2)
<b>Profit after taxation</b>		<b>118</b>	<b>23</b>	<b>15</b>

**Statement of financial position**

**As at 30 September**

	Notes	2017 £000s	2016 £000s	2015 £000s
<b>Non-current assets</b>				
Property, plant and equipment (PPE)	3	401	317	399
		401	317	399
<b>Current assets</b>				
Inventory	4	295	223	532
Trade and other receivables	5	1,087	652	216
Cash at bank		-	-	114
		1,382	875	862
<b>Total assets</b>		<b>1,783</b>	<b>1,192</b>	<b>1,261</b>
<b>Shareholders' equity</b>				
Ordinary share capital		200	200	200
Retained earnings		458	340	317
<b>Total shareholders' equity</b>		<b>658</b>	<b>540</b>	<b>517</b>
<b>Current liabilities</b>				
Trade and other payables	6	1,061	616	744
Bank overdraft		64	36	-
		1,125	652	744
<b>Total equity and liabilities</b>		<b>1,783</b>	<b>1,192</b>	<b>1,261</b>

## Statement of cash flows

Year ended 30 September

	2017	2016	2015
	£000s	£000s	£000s
Profit before tax	147	29	17
Adjustments for:			
Depreciation & loss on disposals	117	82	106
Interest charges	22	32	12
	<b>286</b>	<b>143</b>	<b>135</b>
Change in inventory	(72)	309	59
Change in trade and other receivables	(435)	(436)	280
Change in trade and other payables	422	(132)	(302)
<b>Cash generated from operations</b>	<b>201</b>	<b>(116)</b>	<b>172</b>
Taxation paid	(6)	(2)	(47)
Interest charges	(22)	(32)	(12)
<b>Net cash from operating activities</b>	<b>173</b>	<b>(150)</b>	<b>113</b>
<b>Investing activities</b>			
Purchase of PPE	(230)	-	(86)
Proceeds from disposal of PPE	29	-	16
<b>Net cash used in investing activities</b>	<b>(201)</b>	<b>-</b>	<b>(70)</b>
<b>Net change in cash and cash equivalents</b>	<b>(28)</b>	<b>(150)</b>	<b>43</b>
Cash and cash equivalents at start of year	(36)	114	71
<b>Cash and cash equivalents at end of year</b>	<b>(64)</b>	<b>(36)</b>	<b>114</b>

## Notes to the management accounts

### Note 1 Cost of sales

	2017	2016	2015
	£000s	£000s	£000s
Base products	2,895	2,064	1,871
Monogramming materials	1,450	1,027	937
Production labour	370	305	278
Production overheads	582	558	511
	<b>5,297</b>	<b>3,954</b>	<b>3,597</b>

### Note 2 Other operating costs

	2017	2016	2015
	£000s	£000s	£000s
Administrative staff and overheads	785	728	726
Marketing and distribution	303	262	221
Allowance for impairment of trade receivables	107	139	-
Trade receivables written off	-	-	222
	<b>1,195</b>	<b>1,129</b>	<b>1,169</b>

### Note 3 Property, plant and equipment (PPE)

	Leasehold Improvements	IT & Machinery	Vehicles	Total
<b>Cost</b>	£000s	£000s	£000s	£000s
At 1 October 2014	114	566	260	<b>940</b>
Additions	-	24	62	<b>86</b>
Disposals	-	-	(48)	<b>(48)</b>
<b>At 30 September 2015</b>	<b>114</b>	<b>590</b>	<b>274</b>	<b>978</b>
<b>Depreciation</b>				
At 1 October 2014	53	314	138	<b>505</b>
On disposals	-	-	(27)	<b>(27)</b>
Charge for the year	11	56	34	<b>101</b>
<b>At 30 September 2015</b>	<b>64</b>	<b>370</b>	<b>145</b>	<b>579</b>
<b>Carrying amount at 30 September 2015</b>	<b>50</b>	<b>220</b>	<b>129</b>	<b>399</b>
<b>Cost</b>				
At 1 October 2015	114	590	274	<b>978</b>
Additions	-	-	-	-
Disposals	-	-	-	-
<b>At 30 September 2016</b>	<b>114</b>	<b>590</b>	<b>274</b>	<b>978</b>
<b>Depreciation</b>				
At 1 October 2015	64	370	145	<b>579</b>
On disposals	-	-	-	-
Charge for the year	11	44	27	<b>82</b>
<b>At 30 September 2016</b>	<b>75</b>	<b>414</b>	<b>172</b>	<b>661</b>
<b>Carrying amount at 30 September 2016</b>	<b>39</b>	<b>176</b>	<b>102</b>	<b>317</b>
<b>Cost</b>				
At 1 October 2016	114	590	274	<b>978</b>
Additions	-	138	92	<b>230</b>
Disposals	-	(22)	(76)	<b>(98)</b>
<b>At 30 September 2017</b>	<b>114</b>	<b>706</b>	<b>290</b>	<b>1,110</b>
<b>Depreciation</b>				
At 1 October 2016	75	414	172	<b>661</b>
On disposals	-	(11)	(38)	<b>(49)</b>
Charge for the year	11	58	28	<b>97</b>
<b>At 30 September 2017</b>	<b>86</b>	<b>461</b>	<b>162</b>	<b>709</b>
<b>Carrying amount at 30 September 2017</b>	<b>28</b>	<b>245</b>	<b>128</b>	<b>401</b>

**Note 4 Inventory**

	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>£000s</b>	<b>£000s</b>	<b>£000s</b>
Base products	196	145	356
Monogramming materials	99	78	176
	<b>295</b>	<b>223</b>	<b>532</b>

**Note 5 Trade and other receivables**

	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>£000s</b>	<b>£000s</b>	<b>£000s</b>
Trade receivables	985	557	129
Other receivables	102	95	87
	<b>1,087</b>	<b>652</b>	<b>216</b>

**Note 6 Trade and other payables**

	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>£000s</b>	<b>£000s</b>	<b>£000s</b>
Trade payables	896	463	599
Other payables	165	153	145
	<b>1,061</b>	<b>616</b>	<b>744</b>

## EMAIL

**From:** Ffion Deans  
**To:** Penny Price  
**Subject:** Review of BM business operations for the year ended 30 September 2017  
**Date:** 8 November 2017

I am providing further information on the management accounts for the year ended 30 September 2017 and attaching a set of documents, written by members of the BM board, which provide an insight into the company's current business operations:

- purchasing and inventory (**Exhibit 7**)
- computer aided design and production (CADP) (**Exhibit 8**)
- customer evaluation and making sales (**Exhibit 9**)
- supplier evaluation and contracting for supplies (**Exhibit 10**).

**Year ended 30 September 2017**

- BM has continued to increase its revenue, both through increased orders from existing customers and through winning new business.
- Most of BM's customers operate in the luxury end of the hotel and leisure industry and, despite predictions of a possible decline, this sector – offering top-quality experiences to its customers – is continuing to prosper. As a result, BM's revenue is also growing and that is expected to continue.
- With the steady growth, the company maintained its need for bank overdraft facilities, both to continue to recover from the effects of the Majestic collapse and to fund an increasing working capital demand caused by expansion and rising prices for base products and monogramming materials.
- The full impact of the increase in these costs which started in 2016 was felt during the year to 30 September 2017. It was difficult to pass cost increases on, particularly to established customers for fear of losing their business, and this has caused BM's gross profit margin to fall.
- BM continued to exercise tight control over inventory.
- After a year of no investment, BM made some investment in non-current assets to upgrade production equipment and production IT. BM also part-exchanged and purchased some vehicles.
- The allowance of 20% of closing trade receivable balances was maintained in the management accounts. No trade receivables were written off during the year.
- Because of the success achieved over the previous twelve months, BM maintained its marketing and sales drive with a continued focus on the upmarket hotel industry but with an increased emphasis on the luxury cruise industry.
- Some customers placed orders very near the end of the trading year. As a result, there was an increased level of trade receivables in the statement of financial position. This increase in trade receivable balances also appears as a significant outflow in the statement of cash flows.
- A similar issue of timing (linked to increase in activity near BM's year-end) has occurred with purchases and trade payables, and these large outstanding balances have a prominent effect on the statement of financial position. They will affect cash flows after the year-end.
- The company operated with a bank overdraft throughout the year, but this was carefully controlled by management. The company remained below its agreed £250k overdraft limit at all times.

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**BM: purchasing and inventory – prepared by Carl Morgan**Purchasing

BM base products are bathrobes or towels in white or light beige towelling material, all of which have been made by and purchased from BM's approved suppliers. These are the colours of choice for many hotels, spas and cruise operators because they are the most adaptable of colours which match light bathroom furnishings and bed linen.

The density of cotton is measured in “gsm” (grams per square metre) – the higher the number, the better the quality of the product. To ensure the best-quality base products for the BM production process, BM aims to buy base products which have a gsm of 600 or above. This rating means that the base product not only has a feeling of luxury and quality but that it is also capable of having a monogram added to it without suffering any distortion. This ensures almost no imperfections or rejections in the monogramming production process. BM selects its base product suppliers mainly on the quality of the product. Increasingly, the carbon footprint of the supply is taken into consideration.

The monogramming process requires a multitude of different silk and cotton threads covering the whole spectrum of colours. These threads must also be of the requisite industrial production strength. The production of intricate motif designs on the base products can use substantial quantities of these (often expensive) threads. BM purchases these threads from a variety of suppliers, both in the UK and abroad. Particular threads are only available from specialist suppliers, many of whom are located outside the UK.

BM's policy is to ensure that it purchases regularly from its range of suppliers. By doing this, it is attempting to obtain the best-quality purchases from its suppliers at the best price and is also reducing the inherent risk of being dependent on any single supplier. The reality is that most base products and monogramming materials originate outside the UK. This means that even where BM buys from a UK supplier, it is almost certain that the UK supplier is in a supply chain which includes a manufacturer based outside the UK (see **Exhibit 10**).

Inventory

What makes each BM product unique and only of use to a specific customer is the exclusive monogrammed logo or emblem on each item supplied to it. This is both the unique selling point for BM and its business weakness.

Immediately prior to production, the inventory of base products has a value which could, in the event of those items not being required, be used in other manufacturing processes, or even sold to other users and manufacturers. As soon as the monogramming is applied, the product has a full sale value only to the specific customer. It instantly becomes totally valueless to any other customer, and therefore to BM. The time and effort which would have to be spent by BM employees in unpicking any unwanted motifs by hand, and the damaging impact on the product itself, makes such a process commercially worthless.

Because goods are monogrammed to order for immediate despatch and not for inventory, it is the purchased base products and the cotton and silk thread monogramming materials which make up the physical inventory. All inventory is valued at the lower of cost and net realisable value.

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**BM: computer aided design and production (CADP) – prepared by Mo Tenby**Overview

BM is a company which designs motifs in conjunction with its customers and then, using a monogramming process, stitches the designs, by way of embroidery or a form of weaving, onto the base products. The designs and monogramming are commissioned by corporate customers such as luxury hotels and related organisations. The monogramming process is performed in the workshop by a combination of the twelve computer-linked workbench machines – which can work independently or simultaneously on an order.

BM's design and logo processing team is led by design graduate Mo Tenby. Mo specialises in design creation and works closely with Shelly Drapes and the clients on agreeing the final designs.

The day-to-day management and control of the production in the monogramming workshop is led by Carl Morgan. He has worked with BM since completing a CADP apprenticeship. Carl is now a fully-qualified CADP specialist engineer and, as well as managing the monogramming process, he also oversees all aspects of distribution.

BM design process

The design team works in conjunction with the sales team (which is led by Shelly Drapes). This is particularly important in the initial discussions with clients. A crucial part of winning corporate business is to understand the client brief in terms of motif design: especially exact colours, fonts, dates and images to be used.

An agreement to submit a bid for work, or supply a design proposal, is initially a combined design and sales process. The two teams then diverge. The design team presents its ideas based either on precise client criteria or on original designs created by the BM team for client review – in both cases seeking client approval. This creative process can take a number of iterations, spread over a week or even months, before full agreement is reached, and the client signs off on the designs. Occasionally, an inspirational design idea is accepted almost immediately. As part of most agreements, the customer keeps the IP of the designed motif.

The design team works using the most up-to-date design technology. In many cases, designs include or are based around the corporate logos of the organisation. These can feature emblems such as crowns; coats of arms, or other identifiable symbols of an organisation – but for special events these are often amended to incorporate specific details such as a commemorative occasion or date, a special location, a significant event, or the hosting of an important group of visitors. These changing design details provide a sense of uniqueness to those using the products on which the design is monogrammed.

As in all design work, it is the visual flair and creativeness of the designers which can be crucial in any successful proposal. The BM design team comprises a small number of young design graduates as well as employing school-leavers on training schemes which combine the practical work of the BM design studio with local training at college. BM designs have won many creative awards, and there is fierce competition for any employment vacancies.

One aspect of the approval process is that clients are shown these designs monogrammed onto actual samples of bathrobes and towels as a physical prototype. This physical presentation, rather than an electronic transfer, is part of a careful BM policy of keeping close to clients as well as protecting all BM design work, until client approval is obtained. BM treats all design and prototype creation costs and the time the team spends on this work as part of the production overhead in cost of sales. Apart from those instances where a design concept is created and accepted instantly, it is rare for this iterative design and consultative process to take less than two weeks.

If it is successful in its negotiation on the designs (and eventual price), a signed agreement is obtained. BM then conducts trial production, which, if there are no problems, can be finalised in hours. Where there are problems, it can be several days of additional testing before BM can begin the full production process. The approved final client designs are dated and stored on BM's integrated CADP system with all previous versions stored on separate password-controlled files to minimise the risk of the wrong versions being used in full manufacturing.

### BM production (monogramming) process

The monogramming team becomes involved from an early stage in winning client business. A team led by Carl Morgan is responsible for ensuring that the ideas designed by the BM designers can be presented as an actual finished item to the client. To that end, there is a small dedicated section of the workshop – known as the “solver section” or “solvers” – engaged in producing these prototype items for consideration and client approval. This team combines artistic and production engineering skills.

Many complex processing problems have to be overcome at this stage by the solvers. Simple logos involving mainly word designs pose few problems. Other designs which can appear beautifully balanced and appropriate on the computer screen, or when printed on paper, fail to live up to expectation when being woven onto a product. Some designs end up being too bulky for the fabric. Others cause awkward bunching or gathering of the background material. In some cases, the colours cannot be matched exactly; and in others, details are not significant or bold enough.

It is the solvers' function to create an appropriate prototype of each design motif. They do this by using the customer-selected base products and then monogramming the design motif onto the product using the workshop equipment. The output from this process is then subject to detailed review and evaluation to ensure that the output meets all specifications. If there are any production problems at this stage, the solvers try to find the necessary solutions. The solutions, or the lack of them, are then fed back to the main design team for amendments to design proposals and, if appropriate, the customers are also consulted. This loop avoids the problem of providing an impractical and ultimately undeliverable design to a client.

As soon as a prototype has been successfully accepted by the client, a small sample of products is produced which then undergo certain resilience testing by BM. This involves a series of high temperature washes and drying processes to check for any colour distortions, shrinkages, fading or weakening. If any problems occur, it is again the solvers' job to sort them out. Only when all tests are completed satisfactorily can the full monogramming production process be approved and then programmed into the system for production.

All monogramming processes occur in BM's large production workshop. This has a series of computer-linked monogramming workstations – which are elaborate stitching and weaving machines – through which products pass in a process which can be performed in minutes for

each product. BM's production system can run all machines in parallel producing one customer order, or individual machines can operate separately. The monogramming process is usually identical between products within production batches, provided that they all require the same motif.

If necessary, it is possible for BM to monogram 1,200 standard items of an uncomplicated design in a single day. This would assume using the full capacity of 12 machines working constantly, with no glitches and all products and materials and labour available throughout.

Finished monogrammed products are folded, bundled and packed immediately ready for imminent despatch. No monogramming of products is ever undertaken to be stored as inventory on behalf of a customer. All monogrammed items are subject to immediate delivery to the customer.

## **BM production costs**

Most of the production costs are linked to volumes of products being made. However, component costs can vary over time caused by price changes – for example, increases in product materials caused by exchange rate changes, and increases in labour costs through higher wages. Efficiencies (and inefficiencies) in the production process can affect both materials usage and labour time spent on a customer order.

### Production overheads

As in many design and production organisations, the full labour cost of Mo Tenby's design team, plus any related initial material costs associated with the design and testing of prototypes for any BM customer, are included as part of the production overheads.

This is because new techniques are constantly being developed and considered in new projects for customers, but all innovations are built on the experience of previous positive or negative trials. Previous failures are eliminated, and previous successes are incorporated further in new projects. This accumulated expertise is the starting point for new designs. Treating these development costs as part of overheads to be spread amongst the projects in any year avoids the cost of failure in design or prototype being charged, unnecessarily harshly, on individual specific projects.

Also included in the production overheads is the cost of power, proportions of rent, location taxes, as well as workshop and CADP depreciation charges.

In the past three years, there have been steady changes in average production costs against a constant average selling price, and these changes have squeezed margins. The averages (rounded) for a typical single BM product are shown below:

<b>Average production costs</b>	<b>Notes</b>	<b>2017</b> <b>£</b>	<b>2016</b> <b>£</b>	<b>2015</b> <b>£</b>
Base product	<b>1</b>	22.0	20.5	19.0
Monogramming materials	<b>2</b>	11.0	10.5	9.5
Production labour	<b>3</b>	3.0	3.0	3.0
Production overheads	<b>4</b>	4.0	5.0	6.0
<b>Total production cost</b>		<b>40.0</b>	<b>39.0</b>	<b>37.5</b>
Average selling price	<b>5</b>	50.0	50.0	50.0
<b>Contribution</b>	<b>6</b>	<b>10.0</b>	<b>11.0</b>	<b>12.5</b>

### Notes

1. A base product is the item on which the motif is monogrammed.
2. Monogramming materials comprise the silk and cotton embroidery threads which are used in creating the design motifs being monogrammed.
3. Labour is the cost of the workshop labour used in all aspects of receipt of products and materials, the monogramming process, inventory work and packaging for despatch.
4. Production overheads – as discussed above.
5. As stated, the average selling price for a BM product has remained at £50 for the past three years mainly because of resistance by customers to any price increases.
6. The contribution made by a product is the difference between the selling price and production costs – and may be considered as either the mark-up on cost or the margin on selling price.

The average single BM product detailed above is one item in a set of items all of which are monogrammed (a set normally comprises six items: four towels of different sizes and two bathrobes).

Customers place their orders on the basis of one set for each pair of guests and then multiply the order to ensure that they can replace sets during a guest's normal stay. This may mean ordering two or three sets of items for each pair of guests.

The number of individual items monogrammed reached over 100,000 for the first time in the year ended 30 September 2016. In the year to 30 September 2017, BM exceeded its monogramming target of 125,000 items.

**BM: customer evaluation and making sales – prepared by Shelly Drapes****Context**

The collapse of a business customer, and its failure to pay the amount it owes, is not just a number. The immediate impact in financial terms is on cash flow, bank overdraft requirements, ongoing revenue, purchases from suppliers, investment in PPE and staff levels. This can affect the morale of staff throughout the business, who may feel threatened by a possible loss of future employment. It can also have a negative impact in terms of the futility of having previously worked on any order made by a customer that subsequently failed. It may be seen as an indicator of poor management and judgement and a lack of commercial awareness. Where the collapse is sudden and unexpected, it can result in a loss of business trust towards all other customers. This was the effect of the financial collapse of Majestic for BM.

Majestic was a prestigious international hotel and spa operator, which had been a customer of BM for several years. From an initial order in 2010, BM's sales to Majestic had increased steadily and it became a significant customer in terms of both revenue and its prestige. Because of the high value of the orders being processed immediately prior to its collapse, BM had sought specific assurances from Majestic concerning payment. Majestic had provided verbal assurances before the completion and despatch of the last orders in July 2015. Even with those assurances, when it collapsed a short time later Majestic was unable to pay the amounts it owed to BM and to its other trade creditors. In addition, although BM had a 'retention of title' clause in the contract (which was also displayed prominently on each invoice), any retrieval of the goods sold was a valueless exercise. The whole of the outstanding receivable had to be written off. Majestic's default caused lasting damage.

**Customer summary**

The following is a summary of BM's annual revenue and amounts receivable per major customer at 30 September:

<b>Customers</b>	<b>2017</b>	<b>2017</b>	<b>2016</b>	<b>2016</b>	
	Annual Revenue <b>£000s</b>	Year-end Receivable <b>£000s</b>	Annual Revenue <b>£000s</b>	Year-end Receivable <b>£000s</b>	
Alphonse Hotels	1,452	152	1,196	143	International hotel group
Boreal Spas	664	91	641	66	Luxury spa operator
Cosset Hotels	864	107	917	109	UK luxury hotel operator
Deep Wave Cruises	674	129	522	84	Luxury cruise operator
Falconer Leisure	326	83	291	49	Hotel and cruise operator
Henry Six	254	177	184	66	Hotel and spa group
Indulge Hotels	174	97	-	-	Hotel group
Titanic Cruises	78	78	-	-	Cruise operator
All others	2,175	317	1,393	179	Various
<b>Total</b>	<b>6,661</b>	<b>1,231</b>	<b>5,144</b>	<b>696</b>	

BM has set in place a process for evaluating customers in terms of creditworthiness and other commercial and operational factors, from initial contact through to collection of outstanding balances. BM has reviewed its existing customers and evaluates all new customers using the following process. This is an ongoing process, set within the context of the need to win new business and then retain customer loyalty.

## **Evaluation of customers**

### Customer appraisal

If BM can meet the quality and quantity supply requirements for a customer – which primarily depend on CADP and purchases analysis – then the detailed appraisal of the customer covers the factors below.

There are no strict rules or weightings against the following criteria, apart from an overall assessment of the creditworthiness of a customer – the ability to pay for products ordered and delivered – and whether trading with this customer may result in any potential negative implications for BM's business reputation.

### Key questions and criteria for new and existing customers

1. What is known about this customer in terms of:

- History – how long has the customer existed or been in business?
- Location – where is this business based and who are its owners?
- Public profile – how well-known is this customer?
- Reputation – any details which may indicate a risk in trading with this customer?

What BM is seeking here, at the outset, is whether the customer is a dependable, well-established organisation or a recently set-up operation, which might be riskier.

2. What will be the value of the initial order; what are the potential annual sales; what is the probable profitability?

These are obvious commercial criteria, which are assessed against average BM trading statistics to evaluate customer size and its benefit/risk to BM in both the immediate and longer term.

3. Are BM normal credit terms the acceptable credit terms for this customer?

Any adverse deviation by a new customer requesting an extension to normal credit terms has to be evaluated carefully and authorised. (Standard terms: Payment due within 30 days from the month end following the date of invoice – which would normally average 45 days' credit.)

4. Is BM selling at an appropriate price?

The following detailed factors are relevant and are important in winning a customer's business:

- Are BM's prices/margins acceptable to our customer – does an initial discount have to be offered to win an order from a potentially good customer?

- Is BM offering a high-quality deal, which is attractive to the customer, when considering: price; quality of product; and delivery timescales?
- Are the margins negotiated acceptable to BM?
- Can BM determine or estimate what any competitors are offering (and does it matter)?

BM is looking to determine what is necessary to win the immediate order using appropriate commercial criteria, but also considering the longer-term implications.

5. Can BM establish a good, confident working relationship with this customer?

This appraisal considers the business trust element – it is affected by, and dependent on, the individuals conducting the negotiations on behalf of the customer and does it need careful evaluation?

6. How important is BM as a supplier to the customer under review?

Does the order being placed represent a significant proportion of a customer's monthly or, in particular, annual spending (or of the customer's annual revenue)?

7. Are positive references available?

- Can the customer provide appropriate positive commercial references, at the outset – provided by any of their current suppliers?
- Are there positive credit reference agency ratings available?
- Are there positive bank references available?

These references are essential external (objective) pieces of evidence for a customer evaluation.

### **Customer case studies and evaluations**

Set out below are evaluations relating to two customers. The first was conducted retrospectively on an existing customer, Alphonse Hotels, as part of the new evaluation process introduced in October 2015 after the collapse of Majestic. The second, Falconer Leisure, was conducted before trading with this customer started.

## Alphonse Hotels

Alphonse is a luxury international hotel chain, established in 1902, with its head office in London. BM negotiated its first contract, worth £215,000, with Alphonse in April 2012 when its London hotel was chosen to host a VIP 5-day event in August 2012, for representatives of the countries attending the 2012 London Olympics and their partners. BM contracted to supply all the towels and bathrobes with a unique motif which combined the hotel's logo of a golden and maroon "A H" with the hotel location and date. With over 250 rooms and daily changes of towels, this initial order was for over 5,000 items.

BM priced this prestigious order keenly not only to win it, but also because it hoped that other orders for similar events might follow. BM's assessment was that there might be as many as four other important events for Alphonse in London each year as well as a multitude of other events in Alphonse hotels elsewhere in the UK and abroad.

The motif and prototype were agreed within one month of the start of detailed considerations. Alphonse accepted all of BM's credit terms and production was scheduled and completed in the following two weeks. The finished goods were immediately despatched, and the invoice raised simultaneously. It was paid within 30 days of being presented.

The initial feedback by the hotel on the appearance and quality of the BM products was very favourable. The final feedback, after the event, was also positive. The purchasing manager from Alphonse wrote: "Most guests wanted to keep one or two of these items as souvenirs of a great time at our hotel during such a special event. All surplus items were presented to the staff and others who worked on the event. Everything was highly sought after. We regard the distribution of these items as being great publicity and a good marketing device and we will certainly be asking your company to submit designs and products for future events".

Despite being a small supplier to Alphonse at the outset, BM is now the main supplier of similar products with standard monogrammed Alphonse Hotel emblems as well as its supplier of choice for more elaborately designed products for all special events.

Since then the Alphonse hotel chain has hosted many other events from culture to sports, politics and economics. Its key hotels from throughout Europe have acted as the locations for major conferences on key issues and high-profile social occasions. Since 2012, BM has provided products for many of these events.

### Summary of Alphonse (2015) based on above key questions and criteria:

1. This was a well-established UK-based business with a high profile and a strong reputation.
2. Regular order value £120,000; annual sales potential over £1,000,000.
3. BM credit terms accepted and adhered to for all orders.
4. Initial contract mark-up on production cost of 15% (selling price discounted after negotiation) to win order; subsequently the target mark-up has been 25%.
5. Good clear professional working relationship established directly with key personnel.
6. Order from Alphonse represents an immaterial fraction of its annual revenue.
7. All references excellent – bank followed up with Alphonse approved phone call to BM.

This indicates that Alphonse would have met the critical criteria had they been applied in 2012. There has been no subsequent indication of insolvency and no adverse financial media commentary.



## Falconer Leisure

Falconer, an AIM listed company established in 1994, is an upmarket hospitality organisation with a head office based in the UK and a variety of luxury spa centres and medium-sized exclusive hotels throughout the UK and Europe. It also runs a series of exotic and unique cruise operations taking guests on charter cruises to off-the-beaten-track locations. Falconer was one of the first cruise companies to take passengers on the North West Passage route from Greenland to the Bering Sea. A special environmentally-friendly Norwegian cruise ship was the luxury 400-berth vessel equipped for all the possible uncertainties to be faced on such a cruise. As part of the cruise experience, Falconer wanted to have a special logo designed and monogrammed onto the bathrobes and towels for the guests.

Boreal Spas had recommended BM to Falconer. Similarly, Boreal had introduced Falconer to BM as a new worthwhile customer. Falconer's director of marketing made the initial contact with BM. From its initial discussions, BM confirmed Falconer's history and size. From a credit company's evaluation, BM established that Falconer's annual revenue was above £160 million – the majority of which came from the spa and hotel operations. The cruise operations accounted for less than 30% of that total.

A draft proposal for the logo for the Falconer cruise was submitted which, with a series of detailed amendments, gained Falconer board approval. The ship had on-board laundry facilities, which meant that it could launder most passenger towels and bathrobes as necessary. As a result, the initial order was for eight items per room and the total order was worth £160,000 and this provided a contribution for BM of £35,000. The main credit terms were agreed in accordance with BM terms and conditions and Falconer took possession of the goods ordered at an agreed collection point at Cardiff airport, ready to be transported by air to its cruise ship, within three weeks of agreeing the order. The balance outstanding was paid within 30 days.

As Falconer later stated about this special first order, "As passengers were paying more than £30,000 each for the 25-day cruise, we wanted everything to be as exclusive and memorable as possible – but in keeping with our corporate ethos. BM's products were high-quality in all respects: functional and memorable – most guests were delighted to be able to use and to keep them as a souvenir."

## Initial evaluation of Falconer

1. A well-established UK business with a high public profile and a strong reputation.
2. Initial order value £160,000; good contract; annual sales potential over £480,000.
3. BM credit terms accepted.
4. Initial contract gross margin of around 22% (selling price not discounted).
5. Good clear professional working relationship established.
6. Order from Falconer for this cruise represented an immaterial fraction of its revenue.
7. All references excellent – the recommendation from Boreal (a trusted customer) concerning Falconer is highly valued.

BM's initial evaluation of Falconer was positive. Subsequent re-evaluations have remained positive. Further orders have followed from Falconer on a regular basis for its various spa and hotel operations with other regular orders for its cruise ships.

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**BM: supplier evaluation and contracting for supplies – prepared by Viv Baines**Context

The impact of losing a major customer without warning – and the knock-on effect that might easily have included BM – has meant that BM is aware that it is also the subject of financial evaluation by its suppliers, who want to be sure that they will be paid for the goods and services which are supplied to BM.

As part of a strengthening of the evaluation of its supply chain, BM has implemented a detailed review of existing and potential suppliers which applies if a supplier is contracted to supply a critical volume of quality products over a sustained period. The analysis comprises reviewing a series of key operational and financial factors to identify areas of risk as well as being reassured about a supplier's strengths.

BM has tried to ensure that it has a UK supplier which supplies the same production items as any non-UK supplier. Almost all UK operators in this industry have to import most of these products – all supply chains have an import element to them.

The following table shows the details of our main suppliers for base products (towels and bathrobes) and monogramming materials (silk and cotton threads). "Others" represents those organisations that supply services such as utilities, transport or marketing.

Suppliers	2017	2017	2016	2016	
	Annual	Year-end	Annual	Year-end	
	Purchases	Payable	Purchases	Payable	
	£000s	£000s	£000s	£000s	
Cassio	696	124	491	73	Italy: silk & cotton threads
Fomenta	1,479	224	962	126	Egypt: base products
Hardy	1,284	287	891	132	UK: base products
Prospectus	775	122	438	41	UK: silk & cotton threads
Tooley	183	24	-	-	Ireland: base products
Others	-	115	-	91	Other suppliers (not products)
	<u>4,417</u>	<u>896</u>	<u>2,782</u>	<u>463</u>	

**Evaluation of suppliers**Key operational factors

1. Can the supplier meet the quality and quantity supply requirements for the product which BM wants to order:
  - from its inventory?
  - from its own manufacturing?
  - for standard products and regular quantities ordered?
  - for one-offs or significant urgent orders?
2. Where is the supplier and its supply chain based? How well established?
  - Is it a UK-based operation?
  - If based abroad what is the mode of transport and timings for delivery to Cardiff?
  - Is it dependent on another key supplier and, if so, where is that key supplier based?
  - Is it a start-up, well-established or is it a business in decline?

3. What is the importance of this order to the supplier and to BM?
  - What is the BM negotiating position: are we 1% or 25% of its business?
  - Are there any alternative suppliers for BM for this product?
  - Does this supplier have any alternative higher-priority customers?
4. Does this supplier have a similar corporate ethos to BM?
  - Does it have clear and fair employment practices?
  - Does it participate in good employee training programmes?
  - Does it support its local community?
  - Are its goods produced from sustainable sources?

### Key financial factors

5. Is the price for these supplies a reasonable price?
  - Might the price be too high? Is BM being overcharged? Can BM negotiate?
  - Might the price be too low? Was the price offered in order to win the business, but it is probably unsustainable over the longer term and higher prices will follow?
6. What is the financial viability of this supplier in relation to this order?
  - Are there any obvious evidence of solvency issues? Does it chase BM for payment?
  - Who are the suppliers to this business?
  - Who and where is the supplier's bank – will BM be making payments to a recognised commercial bank?
7. What is the profitability of the supplier?
  - Is the supplier business generating sufficient operating profit to survive?
  - Is the operating profit increasing or declining? What is the trend?
  - If margins can be analysed, is BM obtaining good value from the supplier?

### **Supplier case studies and evaluations**

Set out below are evaluations relating to two suppliers. Fomenta's was a retrospective evaluation as part of the new process carried out in November 2015. Tooley's evaluation was conducted in October 2016 before trading with this supplier started.

#### Fomenta: evaluation November 2015

Fomenta is one of BM's original and most important suppliers of base products. Fomenta was introduced to BM in 2010, through a small BM customer at that time. Since then it has supplied towels and bathrobes to BM. All Fomenta goods are of Egyptian cotton – which, at 700 gsm, is one of the highest-quality absorbent cottons in the world. These products are of a sufficient weight to provide a superb base for monogramming work and the finished product has excellent moisture-absorbing qualities and great strength when wet.

Fomenta has been a manufacturer of cotton products from raw cotton grown in Egypt for more than 50 years. It is an established and highly successful business (revenue approximately £15 million), which exports over 90% of the goods it manufactures. The locally grown Egyptian cotton ('white gold', as it is known in Egypt) has a longer staple (or fibre) than cotton produced from most other sources. This longer staple means that a more luxurious and stronger end-product can be manufactured. "Egyptian" cotton is now grown worldwide, and it is used as a term to describe long-fibre cotton with a high gsm. Prices charged by

Fomenta are higher than those of most other manufacturers, but BM is paying these prices for a known quality product which meets its standards and has BM customer approval.

Normally Fomenta goods are sent by ship from Egypt to Cardiff docks and can take up to three weeks to arrive. This is not usually a problem because BM holds sufficient base product inventory to cover that period. On occasions, where there has been difficulty with transport, or a need by BM for additional base products to be delivered more rapidly, these problems have been resolved by Fomenta agreeing to air-freight urgent orders to avoid delays.

Gayle has visited the Fomenta factory on several occasions and has always said that the manufacturing working conditions are impeccable and that Fomenta's supply chain is also excellent. Wages paid to workers are above the local average and workers are given training and encouraged to take up formal educational opportunities. The raw material used by Fomenta in its manufacturing process is grown within 50 kilometres of the Fomenta factory on established farms with apparently good working conditions.

Fomenta participates in different European Trade Fairs each year and its Managing Director, Omar Gamal, regularly visits BM in Cardiff to discuss BM's requirements and product criteria.

#### Summary of evaluation of Fomenta (November 2015) based on above criteria:

1. A manufacturer of high-quality base products which meet BM's and its customers' standards.
2. Based in Egypt but with good well-established transport links to Cardiff – has always supplied on time.
3. BM purchases less than 10% of Fomenta's output. It supplies 50% of BM's base product – but any risk of failure in this supply chain is covered because BM has other base product suppliers.
4. Ethos: well-established company with good employee conditions and sustainable sources of its raw materials. Its locally-based supply chain appears free from problems.
5. Usual order value £50k - £60k every three weeks; annual purchases (2015) under £1 million – easily managed. Prices are above other suppliers but the 700 gsm base products are acclaimed for quality.
6. The whole system of imports from Fomenta follows a traditional pattern: product order followed by delivery and then payment by credit transfer directly to Fomenta's bank. There have never been any issues.
7. Fomenta has a track record of good profits even during difficult years of cotton production. It is a healthy business financially and trades fairly with BM. The upward movement in prices for Fomenta products has been caused by exchange rate changes which BM expected to be reversed (and so had not hedged).

For both BM and Fomenta it is a good, equal and durable trading relationship in which clear professional working practices have been established directly with key personnel. Prices paid and trading terms suit both parties – the goods supplied are of excellent quality and value. There is no indication of any financial issues and there has never been any adverse financial or other media commentary.

#### Tooley: evaluation October 2016

BM was introduced to Tooley and its products, by an existing UK company known to BM, at an established Trade Fair in Brussels in August 2016. Tooley had been attending this Trade Fair for each of the past five years. Tooley is a manufacturer and supplier of luxury white and

off-white (light beige) bathrobes and towels made from a linen-cotton mix (70:30). Linen is a yarn derived from the cultivated flax plant which is grown in Ireland, and elsewhere, which increases in strength by about 20% when it is wet.

Tooley has a large manufacturing facility just outside Dublin where it produces and sells the equivalent of over £5 million worth of goods every year. It was set up and has operated in Ireland for over 15 years and supplies both domestic and export markets. Its products are tried and tested in a competitive market. It has generated and reported audited profits in each year since its creation. BM staff visited the Tooley factory in October 2016 to assess Tooley's base products. These cotton-linen products are ideal as the base product for BM's production process and these product materials are of the highest quality. Tooley's prices reflect the quality of its products and are 10% above the prices of other BM base product suppliers.

Tooley is one of the leading exporters in its region and has won Ireland's Small Business Exporter of the Year twice since 2010. It normally holds almost £300,000 worth of its base product inventory at any point in time. Tooley guarantees that any export order will be despatched within 7 days of receipt of order provided that the export order is backed by a certified bank guarantee or an Irrevocable 60-day Letter of Credit drawn on one of the major UK clearing banks (BM's bank is one such bank). Specifically, Tooley has a 48-hour guaranteed truck and ferry delivery service for goods to UK customers. It also has other customers in the UK and Tooley staff make frequent visits to the UK to liaise with customers.

Tooley has a policy of purchasing local linen from producers close to its Dublin base. Its cotton is imported. It has a workforce of 40 staff, of which 10% are on youth work-based training programmes. Its Managing Director, Raymond Tooley, sits on the board of the Dublin Chamber of Commerce. He is also a frequent speaker at European business conferences.

#### Summary of evaluation of Tooley (October 2016) based on above criteria:

1. This is a new supplier which manufactures a unique (linen and cotton mix) range of high-quality base products. These are expected to meet BM requirements for both production purposes and customers' final usage standards.
2. Based in Ireland, so import arrangements apply, but with excellent (48-hour delivery) and established transport links to UK – its physical location is not seen as a problem.
3. BM proposes to purchase approximately £200k worth of goods from Tooley in the next trading year (only 4% of Tooley's output; less than 5% of BM's base product purchases). BM will evaluate these products during production and by monitoring performance after sales.
4. Ethos: this is small but highly-regarded company, with excellent staff conditions, sustainable sources of raw materials and strong commercial connections. It has a positive public profile.
5. BM's initial order value would be £15k monthly; annual purchases under £200k.
6. Tooley's trading terms are accepted; bank arrangements are confirmed for initial orders.
7. Tooley operates with a minimum mark-up on its production cost of 25% (similar to BM's aims). It does not offer any discounts to win orders.

From the initial visit to Dublin and the subsequent reciprocal visit made by Raymond Tooley to BM's workshop, a professional working relationship has been established. Although the price to be paid is higher than from other suppliers, BM is confident that the products will provide it with a trouble-free production process. BM will discuss possible sales price increases with its customers. (Subsequent review is that these goods are of exceptional quality and suit BM production requirements and final customer needs perfectly.)

## EMAIL

**From:** Gayle Harries  
**To:** BM board cc: Penny Price  
**Subject:** Review of management accounts, corporate responsibility, commercial review  
**Date:** 7 November 2017

Following the recent board meeting, I am summarising the outcome of the discussions held on the review of the 30 September 2017 management accounts.

**2017 management accounts**

- The board considered that the financial performance of BM as shown by its statement of profit or loss to 30 September 2017 showed some good progress with a substantial increase in revenue by comparison with 2016 of almost 30%. BM aims to maintain this new level and has a revenue target of £8 million for the year to 30 September 2018.
- That positive picture also shows that the CADP team has been able to increase the efficiency of the way it operates. The investment by BM in new CADP systems and new equipment has helped to achieve that efficiency, by shortening production times and reducing wastage. The CADP team is confident that it can deliver 160,000 monogrammed items in the year to 30 September 2018.
- However, there has been a relentless increase in BM's cost of sales – particularly product materials – which impacts the whole business, affecting not only profitability but also cash flow. We face a constant struggle to negotiate better prices from suppliers – whilst pursuing our key goal of maintaining product standards.
- Despite having a very strong network of loyal customers and full confidence in the monogrammed products we create, we continue to meet strong resistance from customers to any price increases.
- BM has remained in fluctuating overdraft during this financial year but has always kept below its agreed maximum. BM has set itself the target of keeping its overdraft below £150,000 for the year to 30 September 2018 – after which date it will re-negotiate a lower maximum (and hopes to reduce its finance expenses).

**Corporate responsibility**

BM has continued its corporate responsibility approach to both employees and product selection with two major projects:

- BM has received continuing benefit from employing young people who have completed workplace apprenticeships with other employers. As a result, BM will in future increase the number of its own workplace apprenticeships to be offered to 10% of the workforce. By doing this, it will be participating in a national scheme to enhance the initial work experience and training opportunities available to young people seeking meaningful employment from our locality. Any financial incentives or subsidies (for training) provided by Local or National Government will be offset against payroll costs.
- BM is actively supporting the attempts being made by some organisations, both in the UK and abroad, which are seeking to find a method and a commercial market for the re-use of cotton products. BM has been working with different organisations testing their products for free in its own process to determine suitability and the economic viability of using re-shredded cotton. BM intends to continue this co-operation and will engage with its customers to identify those who may want to consider being part of a sustainability chain. BM will be looking to make commercial purchases of appropriate base products which meet its gsm and other quality standards, as and when they become available.

## **Commercial review: financial, operational and strategic risks**

As part of our annual review of BM's commercial environment, the following are identified as areas which might pose a risk to the organisation:

### Financial

- The impact of any major one-off production requirement which would initially have a negative cash flow impact.
- Any significant increase in the cost of imported base products or monogramming materials.
- The negative cash flow impact of any significant bad debt.
- Any costly litigation caused by the unauthorised use of a logo or motif in our production (see below).
- Any major increase in power or transport costs.

### Operational and strategic

- A failure of the CADP system – BM has a back-up of all the software, but production would stop and with the loss of production there would be a loss of revenue, or increased costs until recovery occurred, but probably no permanent long-term damage.
- The CADP system being hacked and disrupted – this is potentially quite serious and expensive, particularly if any disruptive program is not detected during a long run of production. It would be particularly troublesome if any glitches in monogramming were not spotted before despatch to customers. Reinstating the system would be expensive. As well as a strong IT system security, which should prevent hacking and corruption, there is a continuous visual check throughout all production runs.
- Encroaching or using another organisation's registered logo or emblem in a BM motif design by mistake. This could be the cause of commercial embarrassment as a minimum, and expensive and time-consuming remedial action to retrieve the situation in a worst case – as well as the problem of dealing with any litigation that might arise. BM conducts extensive research to try to identify any possible duplication of emblems or motifs – and always seeks full approval from any appropriate authority.
- The sudden departure of a key employee – BM conducts frequent reviews of all employees and is as confident as any employer can be that its working conditions and remuneration packages are sufficiently attractive and contribute to employee loyalty.
- A change in government policy away from sustainable production.
- Sudden supplier failure which will disrupt our established supply chain.
- Major equipment failure during a critical production operation. The disruption would cause delay and deadlines would be missed.
- BM always faces the ongoing problem of fierce competition and major customer retention. We try to address this by supplying high-quality goods at equivalent or lower prices than competitors and by attempting to make our motif designs original and inspiring. So far, we have achieved both.



## EMAIL

**From:** Shelly Drapes  
**To:** BM board cc Penny Price  
**Subject:** Customer review for the year ended 30 September 2017  
**Date:** 20 November 2017

Alphonse Hotels: this remains BM's largest customer in terms of revenue. We have had numerous re-orders of our products on behalf of individual Alphonse hotels, as well as a series of special orders for specific events in the UK and abroad. It continues to pay promptly and remains an excellent customer. It regularly recommends us to other organisations.

Boreal Spas: this long-established customer has continued to provide BM with just over £50,000 of work each month. It is in the process of purchasing a series of similar operations in Europe which will increase the number of its spa locations by 40%. BM expects to benefit from this expansion in the year to 30 September 2018.

Cosset Hotels: this is an excellent customer. Each hotel renews the products we supply on an annual basis. Our products are mentioned in Cosset publicity material and favourably reviewed by their guests. There was a small decline in annual revenue during this year, but we expect revenue from Cosset to increase by 15% in the year to 30 September 2018.

Deep Wave Cruises: this UK-based luxury cruise operator has a fleet of nine cruise ships of varying sizes. It operates all year round from a base in the Caribbean and specialises in island and South American cruises. All cruise ships have specially monogrammed products which are re-ordered regularly. BM arranges for orders to be delivered to the cruise ships. BM expects annual revenue from this customer to increase at its current rate of 30%.

Falconer Leisure: revenue from this customer has expanded steadily since its first order. It has become an excellent customer and a great advertisement for our products. BM supplies an increasing number of the spas and hotels in this organisation as well as the cruise ships.

Henry Six: this luxury hotel and spa organisation has large hotels and spa facilities in all the major cities and warm water spa locations in Europe. It has a head office near Harrogate in the north of England where it has a major spa centre. We started by bidding for a contract with the spa business in the UK. Our evaluation was that this would be a good customer with real potential for us to be able to increase our sales to other businesses in this organisation.

Indulge Hotels: this is a new customer which BM evaluated positively in March 2017. We have supplied goods to four of its eight hotels and are hoping for repeat orders and further equivalent business from the other hotels in the year to 30 September 2018.

Titanic Crises: a small cruise operator, which is a new customer. It has operated since 2015 from Edinburgh, taking wealthy passengers on ecological cruises to islands around the UK and Europe. It specialises in Northern Lights cruises. Following our usual vetting process and agreement on motif design, we started to supply it with our products in August 2017.

Others: most of these customers are leisure industry organisations who have commissioned single orders from us. Our monogramming work for them tends to be to commemorate events such as anniversaries or single special occasions. All of them are subject to rigorous creditworthiness checks.

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## EMAIL

**From:** Viv Baines  
**To:** BM board cc: Penny Price  
**Subject:** Supplier review for the year ended 30 September 2017  
**Date:** 20 November 2017

Cassio: this is a long-established family-owned company which supplies Italian silk and cotton threads to customers all over the world. It is based in Milan at the heart of the Italian clothing industry. It has annual sales of £10 million. During this past year, Cassio has developed a new range of silk cotton threads in its factory which include a special gold thread that retains its colour despite repeated washes. For BM this has proved to be an excellent innovation which BM customers request in new designs.

Fomenta: as in all previous years, this company has supplied consistently high-quality base products. As well as these being excellent products for our monogramming process we are constantly sending Fomenta the positive feedback we receive from BM customers – which in turn cite their guests favourable comments – concerning the luxurious quality of these items. During the year Fomenta has delivered all of our orders on time. The one major concern for us has been the steady increase in its base product prices.

Hardy: is a UK company based in South Wales. It is an established supplier of base products to BM – having started supplying these products when BM was first created. Helen Hardy, the current managing director of Hardy, took over the running of this family business in 2012. She has become a close friend of Gayle Harries and as a result the two businesses work in close co-operation. The company obtains most of its base products as finished goods from a supplier in Turkey. These products are made from 700 gsm cotton and, because of this, Hardy's prices for base products match those of Fomenta very closely.

Prospectus: is based in London and supplies BM with silk and cotton threads from a variety of sources – both UK and imported. Many of its cotton threads are used as the basis for the BM monogramming process. It is a reliable supplier with a very short delivery time on all its monogramming materials.

Tooley: this company only started to supply BM with base product goods during the year ended 30 September 2017. BM contacted Tooley through its spa customer, Boreal Spas. Tooley has proved to be both a totally reliable and very high-quality supplier. The linen-cotton mix in its products has proved to be a very good base on which to monogram customer logos and the products are proving to be ideal for use in spas and on cruises because of the strengthening quality which occurs when the products are wet. Although it does not initially have the absolute feel of luxury of Fomenta products, its quality when being used has been superb. Even though Tooley's prices for equivalent base products are about 10% higher than those of either Fomenta or Hardy, we expect to increase our orders from Tooley during the next twelve months.

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**International Travel News**

**March 2018**

**Been there, done that, got the bathrobe and the towel ... at a cost**

For many top hotels and luxury cruise liners, the monogrammed bathrobes, towels and bedclothes that greet a guest as they enter the bedrooms are a carefully constructed part of the image and aura of luxurious quality which these organisations aspire to create for their guests. There is one dilemma which these establishments are reluctant to discuss. That is the “disappearance” of enormous quantities of these monogrammed items along with the guests.

Guests, who have frequently paid very large sums of money for their time at these establishments, expect the very best in all aspects of their treatment during their stay. They also believe that given the sums involved, they are not simply renting the towels, bathrobes and bedclothes— they are buying them, and deserve to take them home as a visible part of the experience. Possession of a bathrobe with the monogram of a top-class hotel, and its exotic city crest, to be worn at home later can be too much to resist – even for the wealthy and famous. As a result, luxury hotels with a real cachet – be they in London, Paris, New York or elsewhere – find their inventory depleted at a steady pace.

As Monsieur Eduard Gillet of the Henry Six Hotel in Paris said, “It is always difficult to confront someone who has paid one thousand euros for a night’s stay, as to whether they have mistakenly packed two of our monogrammed towels and bathrobes into their bulging suitcases – because, although we know that the answer is almost certainly ‘yes’, they are going to say ‘no’”. He added: “Of course on the one hand it is flattering to think that our products are so good, and the memory of the stay so unique, that guests want to keep these items as a reminder, but on the other hand there is a not insignificant cost to this activity”.

The numbers are indeed unbelievable. From its 200+ rooms and apartments, an average of 20 monogrammed items disappear from the Paris hotel every day – with the rate being much higher at weekends, when different guests are in residence. However, to avert some very ugly and unwanted scenes in the palatial hotel lobby, particularly when the guests are famous or fabulously wealthy – and the hotel would welcome their future return – hotel staff are told to avoid the issue.

The solution for many such hotels regarding these wealthy souvenir hunters is that they are charged for the monogrammed products as part of the room price anyway. As a result, the guest goes home happy with his or her “captured” souvenir bathrobe or towel and the hotel covers its costs – and nobody notices or complains.

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### The cachet of the unique souvenir

Within hours of the close of the celebrations for the Royal Wedding in Windsor, adverts began to appear on many websites offering to sell the official gifts given to the 2,640 guests who were fortunate enough to attend the event as invited guests in the grounds of Windsor estate. Simple canvas shopping bags monogrammed with the approved royal blue logo and the date of the occasion were being offered for sale by auction with bids reaching amounts in excess of £1,000.

The exclusive Windsor and London hotels and residences, which had been used by the famous invited guests, experienced a similar surge in demand for any products which depicted this special occasion. A spokesperson for Alphonse Hotels said: "After we were notified of the date of the event, we contacted our usual company, BM, and it designed an appropriately tasteful, fully approved logo for our bathrobes and towels. This combined the event logo and date together with a much smaller discreet hotel logo – our guests were suitably impressed. However, I would not expect to see these items, which our distinguished guests could retain, on eBay at any time soon".

### Follow the money ... UK companies fail to identify financial sources

Within a short period of time, the directors of all commercial organisations based in the UK who are responsible for monitoring financial transactions may be held personally liable for any failure to identify the legitimate sources of receipts or transfers of funds passing through their organisations.

Within this context, a UK television documentary, which tracked the movement of large sums of cash – passing through identifiable bank accounts located in known offshore tax havens – to purchase UK assets, has provoked a storm of public concern.

The programme identified very easily that a series of these companies were merely shells set up in offshore locations to protect the anonymity of the source of finance (and the ultimate financier) from the financial transaction. Often by making just two telephone calls it was easy for the programme to identify that the companies making large payments for purchases of a range of UK assets were not who they stated they were.

The purchases made by these organisations ranged from houses and boats, to large stocks of fine whiskies and expensive *objets d'art*. The purchase of these luxury items is seen as an easy way to "launder" (make legitimate) money from doubtful sources, such as fraud or other criminal activity. To summarise: they could be seen as somewhat shady deals from somewhat sunny places.

The reaction from viewers of the programme made it clear that the general public expect a more responsible approach from those within an organisation, when reviewing these financial transactions. The view is that despite the commercial impact it may have on the potential recipient, the leaders of these organisations have a legal and an ethical responsibility to identify the sources of financial transactions or face the consequences.

### **“Shoddy” now seen as having a proud history**

If you ever wondered what the famous “rag and bone” man actually did (or does), the answer is that his trade is that of recycling unwanted goods, and in particular old clothes – a career that is currently seeing something of a resurgence.

For years, this recycler would traipse the streets of the UK crying out to house dwellers, to bring out any unwanted items. Paying minimal prices, he would collect and buy bags of old clothes. Beyond that, most people did not know or care what happened next. In fact, the rag dealer was a key element in turning rags back into riches – or at least into something called “shoddy”, an economically important form of recycled cotton. The collected rags would be sorted and sifted before passing through an industrial shoddy process which created this recycled product. These days the word “shoddy” is more frequently used to describe work of an inferior nature.

But fashion and public opinion change. Internationally there is an increasing demand for products of all kinds to be re-used as far as possible – and this is especially true of old clothes made from natural cotton or wool: “shoddy” and its equivalents are now back in vogue. In particular, much attention and research has been undertaken to find different ways of recycling cotton – by far the world’s most popular natural fibre.

Currently the recycling of cotton is in transition but according to most experts it will follow the same path as paper recycling. A few years ago, only a small percentage of paper was recycled; today, most paper is recycled, and cotton looks set to follow that trajectory. Some clothing manufacturers, including Levi’s, are already including recycled clothing into new items. Cotton “shoddy” may soon become the new cotton “chic”.

### **The price of working to the (unreasonable) deadline**

In many organisations, working to a customer’s requirements is the key to success. The ability to match or exceed a customer’s expectations brings an initial external reward such as the successful sale, or the satisfactory completion of a project. However, the price paid within the organisation may be more difficult to assess or value.

Most production deadline solutions dealing with speeding up manufacturing and deliveries would involve a higher charge to the client – which would normally be resisted by the client. In attempting to satisfy a client’s sometimes extreme or very specific demands, a company can find itself not just working outside its own – and, more particularly, its employees’ – zone of comfort, but also outside what is economically achievable or sensible.

There is also considerable evidence that stress in the workplace has a hugely detrimental impact on the lives of the employees who experience it and on the business itself – in both the short and the longer term. The effect on the business can manifest itself in low staff morale, poor-quality work and staff absenteeism. This in turn can lead to goods or services being supplied to a customer which reflect that work situation. Organisations which fail to consider the impact of stress on employees, when they are striving to win or complete contracts, risk losing the effectiveness and loyalty of their most important asset.

### **UK bad debts in 2018**

Well-known UK high street companies such as Toys R Us, Maplin and House of Fraser have followed the corporate collapse of construction giant Carillion into financial failure in 2018. As well as making this year one of the worst for large-scale collapses, the effect in all cases is the ensuing huge number of failures by small and medium-sized enterprises which fall into financial hardship and ruin in the wake of these large company disasters.

In the case of Carillion, small businesses are owed an average of £141,000. Insurers have said that they will be paying more than £30 million to businesses owed money by Carillion. Sums ranging from £5,000 to several million pounds are being paid to firms which had insurance policies against bad debts. However, most of Carillion's suppliers risk getting little or nothing back, as only a minority of firms had the necessary trade credit insurance – which covers firms against the risk of not being paid if a company with which they do business then collapses.

Furthermore, as one business analyst summarised: “Given that Carillion, which was the UK's second biggest construction firm and a major service provider for the government, went into liquidation with a £900 million debt pile to its suppliers and £600 million pension deficit, the fact that only £30 million will be paid out in insurance speaks for itself”. Very few small businesses think about this type of insurance – which in any case is not cheap.

As can be seen all too frequently, one major and unexpected insolvency can risk a knock-on effect to hundreds of innocent firms in the supply chain.

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