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Should the company, DDE, consider outsourcing their labour demands ?

***Word Count**: 2000*

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Batch of 2022

Contents

Executive Summary

The company owner has conveyed his scepticism about the growth potential and the company's current financial position, as the magnitude of new infrastructure projects to be launched in the local market were unlikely to be high due to the Covid-19 pandemic. The owner was concerned about the lack of enough projects to land with a contact of enough project value to make a significant profit and ways to maximize the potential profit made by the company without compromising the quality of the services offered by the company. This led the owner to consider laying off certain employees, shrinking the firm's activities, and redesigning its financial marketing strategies to control and manage expenditure to combat the issue of lack of projects and cash-flow issues. This leads to the question: "Should the company DDE redesign its financial and marketing strategies and consider changing its organization structure".

Following this, primary research was conducted in an interview with the owner and questionnaires sent to the company's employees, managers, and previous customers. This information and data were utilized and analyzed using Lewin's force field and fishbone diagram. Secondary data was gathered from a profit loss account and balance sheet to produce a ratio analysis to gauge the company's financial position.

1 Introduction

DDE is a private construction contracting company with one shareholder based in Dubai and operates on construction projects throughout the United Arab Emirates on a contract basis. It is involved in supplying and procuring labour, material, equipment, and general miscellaneous technical works related to the construction of general structures and buildings.

The company currently rents an office in Al Nahda, a district in Dubai, with a total of 3 employees. The primary customers of this firm are usually consultants or other bigger contractors (those who handle more extensive project/construction works). The company DDE receives payment of their work (per month) three months after they file for a payment (three months after work is done). This method of payment is generally accepted as an industry standard.

This negatively impacts the company when the company is to pay their monthly and quarterly expenses as the profit the company has in their books is still not in hand. This method of payment generally does not create cash flow issues. However, if the company is to invest their capital in procuring/advancing certain business segments, this method of advance payment creates a problem with respect to cash flow.

DDE intends to expand their market share and increase its revenue generated by outsourcing its labour demands to other small sub-contracting companies. When outsourcing labour in this regard, DDE needs to issue payments on a monthly basis without the 3-month delay. To effectively employ this new strategy, the company needs to have enough money in hand to issue payments to these outsourced companies before payments from the main companies are received.

If their plan is successful, it will help DDE have an extra, alternative source of revenue and enable them to undertake more construction projects as they would not need to use the company labour, rather, outsourced labour.

From this arises the research question, **"Should the company, DDE, consider outsourcing their labour demands ?"**

2 Methodology

This investigation combined and utilised two primary and three secondary sources of data. An interview was conducted with the founder of DDE, Mr. Farid Ahamad, seeking his views and goals off of his business; this provided a detailed outline of the goals and objectives of the corporation and their current standing and performance in the market. A questionnaire consisting of 10 questions was created and was conducted during four business days of the company, DDE. The questionnaire was aimed at the employees, managers and previous customers of the company. The questionnaire was an MCQ (Multiple choice) type.

The questionnaire aimed to gauge the employees, managers, and some other previous customer's opinions on the quality of the construction work the company has delivered to the project consultants, contractors and how they think about the company's organisational structure and work environment. These data sources shall be used to understand where and how the company can better use more efficient methods of Finance Accounting, Marketing, Human resource management and Operations management.

The IB Business Management textbook by Oxford University press was utilised as a secondary source to reference concepts mentioned and definitions.

Various business tools were employed to gather information to aid in the decision-making process. A SWOT analysis was employed as it analyses both the external and internal strengths and weaknesses and also analyses external threats and opportunities. Lewin's force field analysis was also used in to weigh the driving and the restraining forces for the start of the new initiative; Lastly, Ratio analysis was used to calculate the current and future financial position of the company if the company is to proceed with the initiative, which is to outsource its labour demands.

3 Main Results and Findings

The questionnaire displayed overall satisfaction amongst the previous customers and an excellent general opinion of the company amongst the employees. Approximately 65% of the previous customers are willing to sign a contract again with the company if they can. About 75% of the previous customers were satisfied with the quality of the company's work.

The interview with the company owner showed that the firm is able to meet its goals and objectives at the moment, which he largely gives credit to their small and simple organisational structure without much of a hierarchy in the organisation.

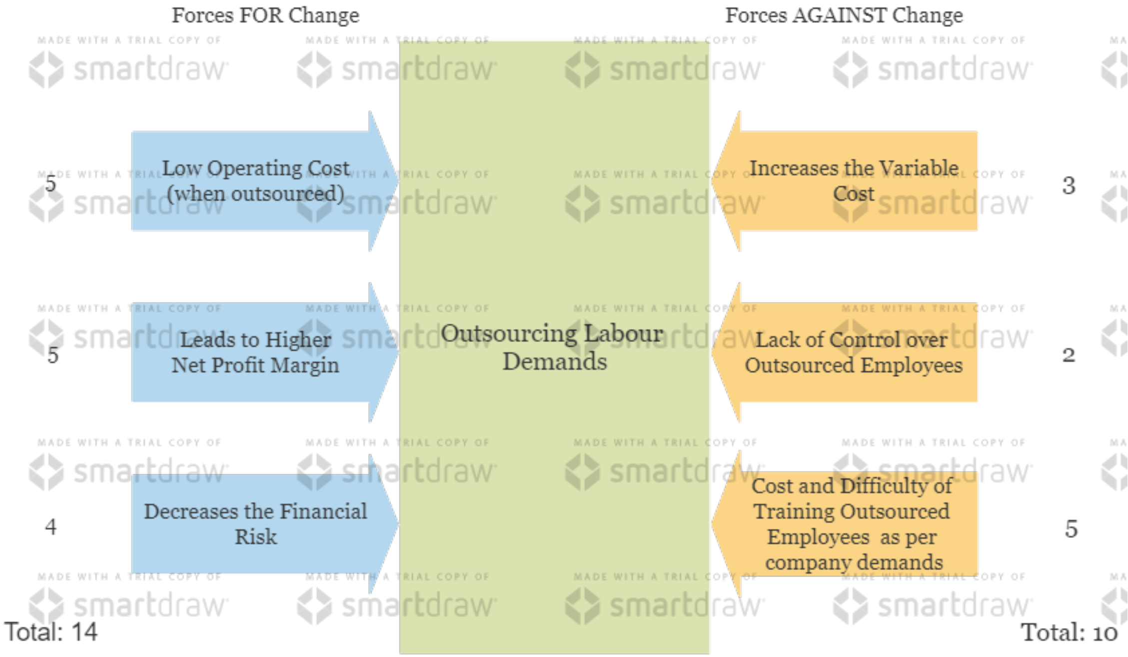
The owner states his reasoning to proceed on the initiative (outsourcing labour) as this would enable them to reduce their costs, as the workers (labourers) would be paid on a project basis instead of a monthly basis; also, this move would reduce their fixed cost per blue-collar employee, expenses like health insurance, visas, accommodation etc.

This move would also enable them to offer consultants and contractors more competitive prices and possibly lead to more contracts being signed, eventually leading to "wider margins" or "higher profits".

4 Analysis and Discussion

4.1 Lewin's Force Field Analysis

A force field analysis was used to analyze the driving and restraining forces so as to decide whether DDE should consider outsourcing. Each force factor is ranked out of 5 in terms of significance and net sums of both the forces are calculated and compared to determine whether the change should occur.



4.2 Ratio Analysis

Ratio Analysis is a numerical and qualitative financial tool that can be used to determine the current and future financial position of DDE for if the company can consider outsourcing its labour demands.

$$\text{Gross Profit Margin (Current)} = \frac{\text{Current Gross Proft}}{\text{Current Revenue}} \times 100\% = \frac{\$1296000}{\$2160000} \times 100\% = 60\%$$

$$\text{Gross Profit Margin (Future)} = \frac{\text{Predicted Gross Proft}}{\text{Predicted Revenue}} \times 100\% = \frac{\$2333000}{\$3888000} \times 100\% \approx 60.2\%$$

$$\text{Net Profit Margin (Current)} = \frac{\text{Current Net Profit}}{\text{Current Revenue}} \times 100\% = \frac{\$705375}{\$2160000} \times 100\% \approx 32.7\%$$

$$\text{Net Profit Margin (Future)} = \frac{\text{Predicted Net Profit}}{\text{Predicted Revenue}} \times 100\% = \frac{\$1995000}{\$3888000} \times 100\% \approx 51.3\%$$

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}} = \frac{\$600000}{\$245000} \approx 2.45$$

$$\text{Return on Capital Employed (Current)} = \frac{\text{NPBIT}}{\text{Capital Employed}} \times 100\% = \frac{\$897500}{\$699300} \times 100\% \approx 128\%$$

$$\text{Return on Capital Employed (Future)} = \frac{\text{NPBIT}}{\text{Capital Employed}} \times 100\% = \frac{\$2256000}{\$1731000} \times 100\% \approx 130\%$$

The Gross Profit Margin for both the company's current and predicted financial state (if the company is to decide to outsource its labour) are both relatively healthy and above the optimal 50% range. This shows the company is profitable and has no issues with the lack of profitability. This statement is further supported by a very good Net Profit Margin of 32.7% before considering outsourcing and an excellent predicted Net Profit Margin of 51.3% after outsourcing.

When analyzing the business Profit-Loss accounts, it is evident that other than the cost of revenue before outsourcing, the operating cost is relatively very high, whereas the operating cost after outsourcing is reduced significantly and is fraction of the original operating cost.

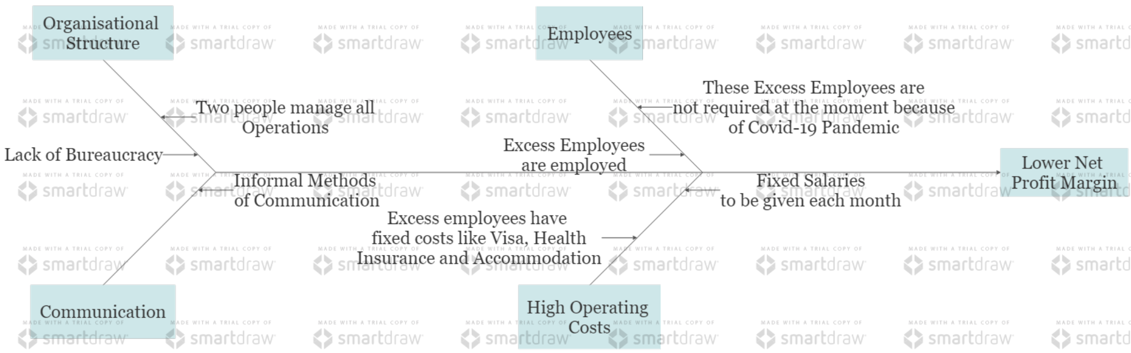
The current ratio is largely positive, demonstrating that the company is in a healthy and stable Cash-Flow position and would not be at a financial risk if the company is to start outsourcing their labour demands.

We can confidently say from the above conclusions that the company can increase their firm's growth and profit margin by outsourcing labour.

4.3 SWOT Analysis

4.4 Fishbone Diagram

The Fishbone diagram finds and analyses the root issue/problem faced within a business. This business tool shall determine the underlying problems/reasons faced by DDE causing the company to consider outsourcing. The main concern from the owner of the firm is Lower Profit Margin.



4.5 PEST Analysis

5 Limitations of Study

There are limitations in both the primary and secondary data collected from the business to use for the various business tools. The results from the questionnaire could be not correct as the respondents might not have been completely honest, affect our conclusions. Also the Ratio Analysis done was based on the current and future (predicted) Profit-Loss Accounts. The predicted Profit-Loss Account is susceptible from bias, resulting in an overestimation or and underestimation.

6 Conclusion and Recommendations

In conclusion, the company "DDE" outsourcing their labour demands would bring the firm a number of benefits, providing an extra stream of revenue, thereby increasing the profit, which then increases the Net Profit Margin. The predicted and the current Profit-Loss Account shows that the Net Profit Margin is 51.3% and 32.7% respectively. The predicted figures are taken in consideration that the company would outsource their labour demands.

With the use of all the four tools, there are significant indications that point out and shows that it is highly beneficial and profitable for the company to start outsourcing labour to increase the profits generated and sustain well in this pandemic-hit industry.

To conclude, based on present and predicted findings, it is highly recommended that the company, DDE should:

- Consider outsourcing their labour demands

- Consider setting competitive prices, so as to attain more contracts, thus a means of increasing revenue
- Utilize intensive marketing strategies to increase their market share

References

[1] Muchena, Martin Mwenda, et al. *IB Business Management Course Book 2014 Edition*. Oxford University Press, 2014.

[2] Hoang, Paul. International Baccalaureate Business and Management. IBID Press, 2014.

A Appendix: Company Financials

Particular's	$ 000's
Assets	
Fixed Assets	
Furniture & Equipment	10
Net Fixed Assets	10
Current Assets	
Cash	240
Payments to be recieved	360
Net Current Assets	600
Current Liabilities	
Payments to be given	160
Short-term loans	85
Net Current Laibilities	245
Working Capital	355
Long-Term loans	220
Net Assets:	135
Financed by:	
Capital & Reserves	85
Retained Profits	50
Total Equity	135

Table 1: Balance Sheet of the company as of 31 December 2021

Particular's	**$ 000's**
Revenue	2160
Cost of Revenue	864
Gross Profit	1296
Expenses	
Payroll	315
Transportation	12
Visa	25
License Renewal	7.5
Office Rent	20
Employee Health Insurance	4
Employee Accomodation	15
Net Expenses	398.5
NPBIT (Net Profit Before Interest and Tax)	897.5
Interest	155
NPBT (Net Profit Before Tax)	742.5
Tax	37.125
NPAIT (Net Profit After Interest and Tax)	705.375
Investor Share	141.075
Retained Profit	564.3

Table 2: Profit-Loss Account of the company as of 31 December 2021

Particular's	**$ 000's**
Revenue	3888
Cost of Outsourcing	1555
Gross Profit	2333
Expenses	
Payroll	42
Transportation	2
Visa	3.2
License Renewal	7.5
Office Rent	20
Employee Health Insurance	0.6
Employee Accomodation	2
Net Expenses	77.3
NPBIT (Net Profit Before Interest and Tax)	2256
Interest	155
NPBT (Net Profit Before Tax)	2101
Tax	105
NPAIT (Net Profit After Interest and Tax)	1995
Investor Share	399.1
Retained Profit	1596

Table 3: Predicted Profit-Loss Account of the company for the year 2022

All figures in $ 000's	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**	**Aug**
Opening Balance	240	656.38	629	601.63	1050.5	1023.1	995.75	1444.6
Cash Inflows								
Cash Revenue	540	0	0	540	0	0	540	0
Total Cash Inflows	540	0	0	540	0	0	540	0
Cash Outflows								
Office Rent	5	0	0	5	0	0	5	0
Wages	26.25	26.25	26.25	26.25	26.25	26.25	26.25	26.25
Telephone	0.125	0.125	0.125	0.125	0.125	0.125	0.125	0.125
Transportation	1	1	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0	3.75	0
Visa Renewal	25	0	0	0	0	0	0	0
License Renewal	7.5	0	0	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0	55	0
Total Cash Outflows	123.63	27.375	27.375	91.125	27.375	27.375	91.125	27.375
Net Cash Flow	416.38	-27.38	-27.38	448.88	-27.38	-27.38	448.88	-27.38
Closing Balance	656.38	629	601.63	1050.5	1023.1	995.75	1444.6	1417.3

Table 4: Cash-Flow Statement of the company as of 31 December 2021

All figures in $ 000's	Jan	Feb	Mar	Apr	May	Jun	Jul
Opening Balance	240	958.775	801.8	644.825	1396.1	1239.13	1082.15
Cash Inflows							
Cash Revenue	972	0	0	972	0	0	972
Total Cash Inflows	972	0	0	972	0	0	972
Cash Outflows							
Office Rent	5	0	0	5	0	0	5
Wages	26.25	26.25	26.25	26.25	26.25	26.25	26.25
Telephone	0.125	0.125	0.125	0.125	0.125	0.125	0.125
Transportation	1	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0	3.75
Visa Renewal	25	0	0	0	0	0	0
License Renewal	7.5	0	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0	55
Outsourcing Costs	129.6	129.6	129.6	129.6	129.6	129.6	129.6
Total Cash Outflows	253.225	156.975	156.975	220.725	156.975	156.975	220.725
Net Cash Flow	718.775	-156.98	-156.98	751.275	-156.98	-156.98	751.275
Closing Balance	958.775	801.8	644.825	1396.1	1239.13	1082.15	1833.425

Table 5: Predicted Cash-Flow Statement of the company for the 2022