Business Management HL Internal Assessment

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

Word Count: *1840*

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 was unlikely to be high due to the Covid-19 pandemic. He was also concerned about the lack of enough revenue generated. This led him to consider laying off certain employees and redesigning its organizational structure to control expenditure, to combat the issue of high operating costs low revenue. This leads to the question: "Should the company, DDE, consider outsourcing their labour demands ?".

Primary data was gathered from an interview with the owner and questionnaires sent to the employees, managers, and previous customers. This data was analyzed using Lewin's force field analysis, SWOT analysis and fishbone diagram. Secondary data was gathered from the Balance sheet, Profit-Loss account and Cash-Flow statements to produce a ratio analysis to gauge the company's financial position.

This report suggests that the company's financial & organizational structure is in a good position and is favourable for the plans that DDE wishes to employ (outsourcing labour). This would drastically increase its Net Profit Margin and reduce the operating costs. However, it's recommended to conduct further market research to test the report's validity on the recommendations provided.

Word Count: 200

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** (Interview with Owner & Questionnaire) and **three secondary** (Balance Sheet, Profit-Loss Account & Cash-Flow Statements) 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; Ratio analysis was used to calculate the current and future financial position of the company. Lastly a Fishbone diagram was used to evaluate 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.

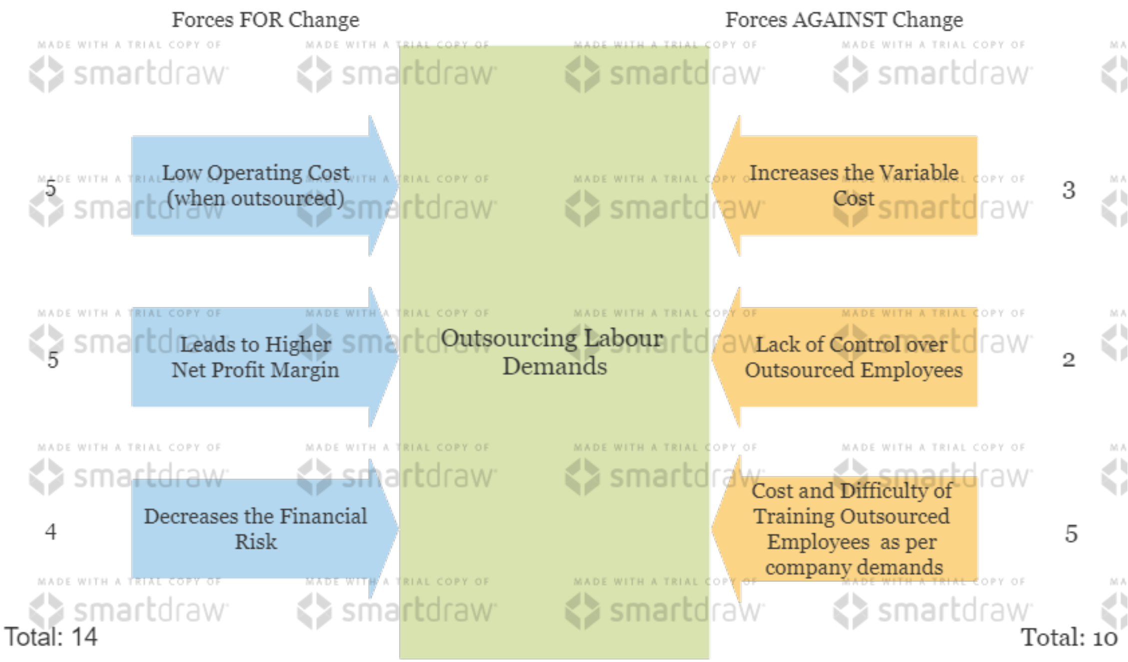
The owner states his reasoning to proceed on the initiative (outsourcing labour) as this would enable them to reduce their costs, as the workers (labourers) would be paid on a project basis instead of a monthly basis; also, this move would reduce their fixed cost per blue-collar employee, expenses like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



The owner states that, his primary reasons for opting to outsource labour is because it would drastically drop the operating costs and that this move would to higher net profit margin; both of which can be evidently seen from the force field analysis as both of them rank those parameters as 5/5. Besides these forces that drive for the change within DDE to outsource labour, an another factor is that it reduces the financial risk within the company.

When evaluating the forces that act against the change, it is evident from the force field analysis that the major force against the move is the high cost and difficulty in training outsourced labour as per company demands and standards; While also the increase in variable cost and lack of authority & control over the outsourced labour are also factors that are restraining the change.

While comparing both the forces for and against the change we see that the driving forces exceed the restraining forces by 4 points which is significant enough to favor the change within DDE to outsource labour.

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.

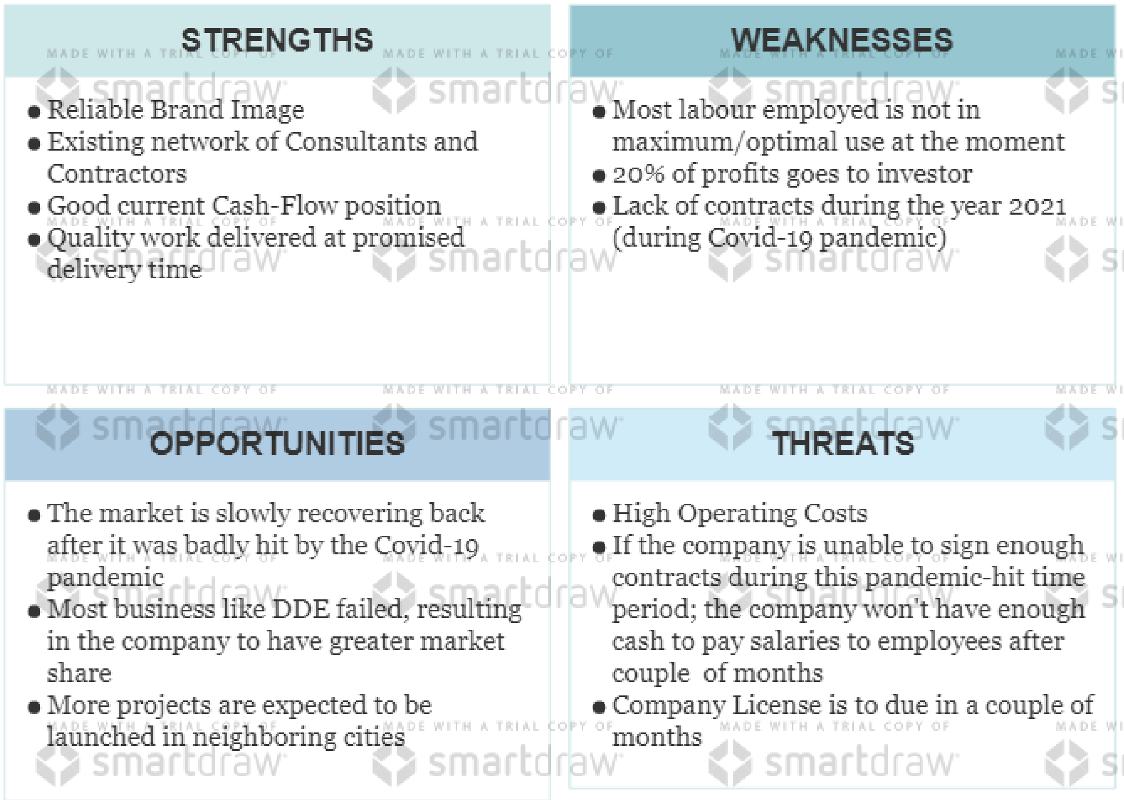
When analyzing the business Profit-Loss accounts, it is evident that other than the cost of revenue before outsourcing, the operating cost is relatively very high, whereas the operating cost after outsourcing is reduced significantly and is fraction of the original operating cost.

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

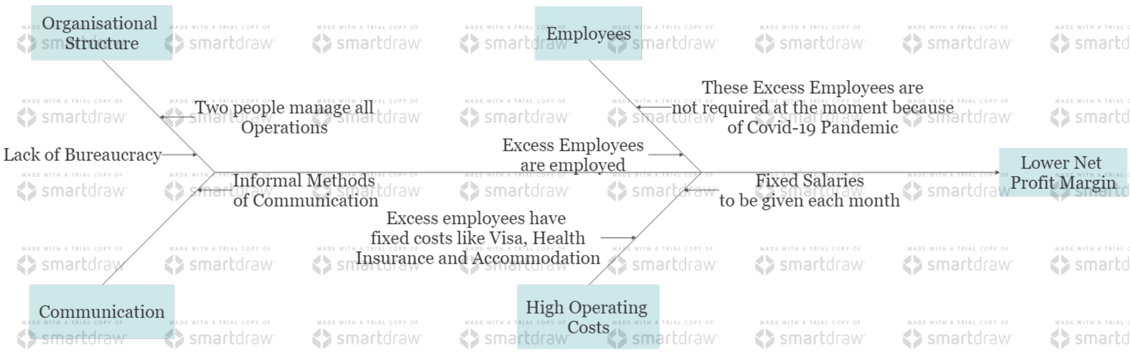
The internal strengths, weakness, opportunities as well as threats of the business were discussed with the owner and are included in the below SWOT analysis, which could help and aid us to decide if outsourcing labour is worth implementing.



The strengths of DDE are that it has a reliable brand image and has a good cash-flow position, whereas the major weakness of the business is that there is an insufficiency of projects in the year 2021 due the Covid-19 pandemic. The possible opportunities that the company can exploit are that market is slowly recovering from the economic backlash and current trends show that many projects are expected to be launched in neighboring cities, which DDE could possibly get contracts for, whereas the current threats that DDE encounters are the high operating costs and possible future issues related to cash-flow if future payments are not processed on time, as the company has enough money to sustain only a few months, without incoming payments.

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.



The major issue of Lower Net Profit Margin that the company is facing is mainly High operating costs and Employees; both of which are due to the excess employees not required as the Covid-19 Pandemic hit the market. These employees are paid fixed salaries that increase fixed costs for the business.

Other than these issues, the company has some serious internal issues regarding the organisational structure and communication within the company. This is because three people manage all company operations, and no supervisor/manager exists to overlook them. The employees use a very informal method of communication, namely, instant messaging over SMS or messaging apps like WhatsApp.

All the above factors add up and result in causing the issue of reducing the company's Net Profit Margin drastically.

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: Interview with Company Owner

1) What type of business is DDE? How big is the business? What sort of business structure is employed ?

DDE is a small company with mainly one shareholder (plus an investor/sleeping partner with 20% share). The company provides material, equipment, labour, and various general miscellaneous technical works related to the construction of general structures and buildings. The company has one office in Al Nahda area of Dubai, where the company's two white-collar employees manage the day-to-day business affairs.

DDE can be largely classified as a construction company. The company makes about an average of USD 50k ($50,000) per project in revenue; DDE undertakes about three projects per month on an average. Resulting in about USD 150k in monthly revenue. The business employs a very simple business structure. I, the owner, instruct my three main employees at my office. They pass those instructions to other blue-collar employees and supervise them. This business is a profit entity.

2) How exactly has the business progressed and developed from the time you have started this business venture? How has your business growth been over the years ?

The growth in the business has been mainly for two reasons, recognition in the market amongst various contractors and consultants and marketing through multiple means of advertisements. The business has been steadily growing at a rate of approximately 20% annually. Due to current market conditions due to the Covid-19 pandemic, the growth rate has decreased but has not stopped. To counter this, we have increased the budgets on the HR and marketing segments of the business. After some initial years after setting up the business, the company has shown a steady, consistent improvement from the time I have started this venture.

3) Why do you think this move to outsource labour would be beneficial for your company ?

I think this decision to outsource labour would be beneficial for the further growth of DDE as it would significantly reduce DDE's operating costs, increase the revenue generated and would lead DDE to undertake multiple projects than it can currently undertake as we would not need to depend on the company's labour. Therefore, it enables DDE to undertake as many projects as possible without the constraints of how to supply that much labour.

B 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**
Opening Balance	240	656.375	629	601.625	1050.5	1023.125
Cash Inflows						
Cash Revenue	540	0	0	540	0	0
Total Cash Inflows	540	0	0	540	0	0
Cash Outflows						
Office Rent	5	0	0	5	0	0
Wages	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
Transportation	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0
Visa Renewal	25	0	0	0	0	0
License Renewal	7.5	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0
Total Cash Outflows	123.625	27.375	27.375	91.125	27.375	27.375
Net Cash Flow	416.375	-27.375	-27.375	448.875	-27.375	-27.375
Closing Balance	656.375	629	601.625	1050.5	1023.125	995.75

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

All figures in *$* 000's	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
Opening Balance	995.75	1444.625	1417.25	1389.875	1838.75	1811.375
Cash Inflows						
Cash Revenue	540	0	0	540	0	0
Total Cash Inflows	540	0	0	540	0	0
Cash Outflows						
Office Rent	5	0	0	5	0	0
Wages	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
Transportation	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0
Visa Renewal	0	0	0	0	0	0
License Renewal	0	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0
Total Cash Outflows	91.125	27.375	27.375	91.125	27.375	27.375
Net Cash Flow	448.875	-27.375	-27.375	448.875	-27.375	-27.375
Closing Balance	1444.625	1417.25	1389.875	1838.75	1811.375	1784

Table 5: Cash-Flow Statement of the company as of 31 December 2021

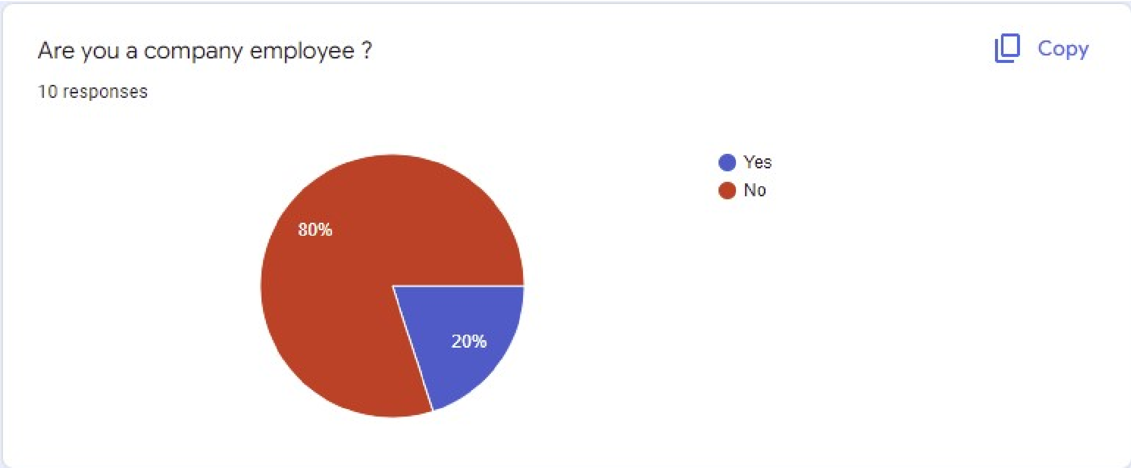
All figures in $ 000's	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**
Opening Balance	240	958.775	801.8	644.825	1396.1	1239.125
Cash Inflows						
Cash Revenue	972	0	0	972	0	0
Total Cash Inflows	972	0	0	972	0	0
Cash Outflows						
Office Rent	5	0	0	5	0	0
Wages	26.25	26.25	26.25	26.25	26.25	26.25
Telephone	0.125	0.125	0.125	0.125	0.125	0.125
Transportation	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0
Visa Renewal	25	0	0	0	0	0
License Renewal	7.5	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0
Outsourcing Costs	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
Net Cash Flow	718.775	-156.975	-156.975	751.275	-156.975	-156.975
Closing Balance	958.775	801.8	644.825	1396.1	1239.125	1082.15

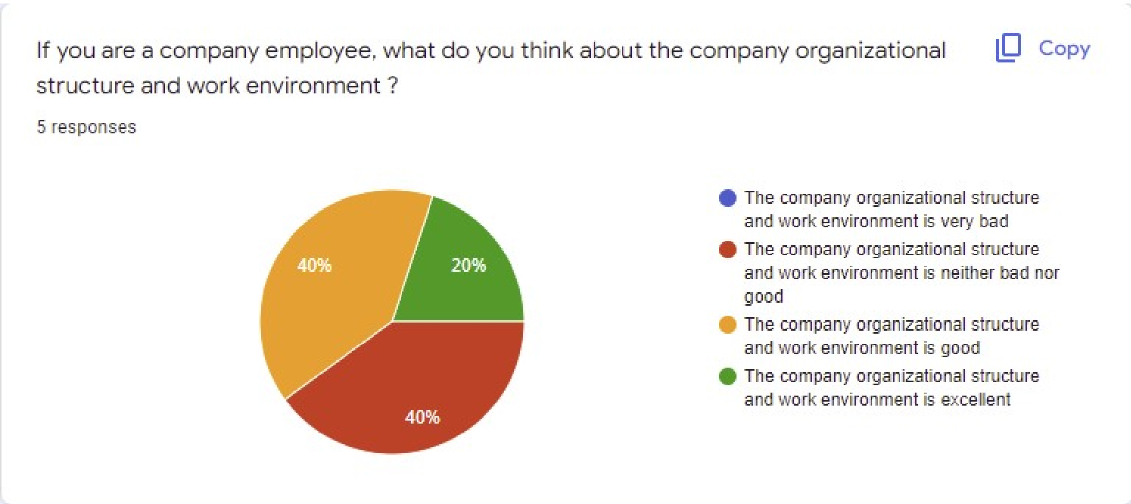
Table 6: Predicted Cash-Flow Statement of the company from 1st January to 31st June 2022

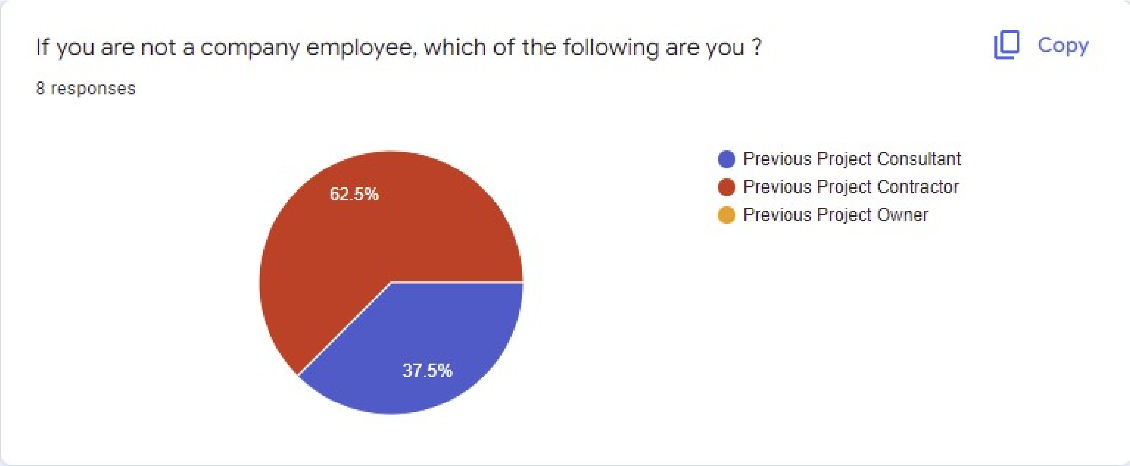
All figures in $ 000's	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**
Opening Balance	1082.15	1833.425	1676.45	1519.475	2270.75	2113.775
Cash Inflows						
Cash Revenue	972	0	0	972	0	0
Total Cash Inflows	972	0	0	972	0	0
Cash Outflows						
Office Rent	5	0	0	5	0	0
Wages	26.25	26.25	26.25	26.25	26.25	26.25
Telephone	0.125	0.125	0.125	0.125	0.125	0.125
Transportation	1	1	1	1	1	1
Employee Accomodation	3.75	0	0	3.75	0	0
Visa Renewal	0	0	0	0	0	0
License Renewal	0	0	0	0	0	0
Loan Repayments	55	0	0	55	0	0
Outsourcing Costs	129.6	129.6	129.6	129.6	129.6	129.6
Total Cash Outflows	220.725	156.975	156.975	220.725	156.975	156.975
Net Cash Flow	751.275	-156.975	-156.975	751.275	-156.975	-156.975
Closing Balance	1833.425	1676.45	1519.475	2270.75	2113.775	1956.8

Table 7: Predicted Cash-Flow Statement of the company from 1st July to 31st December 2022

C Appendix: Questionnaire






If you are not a company employee, which of the following are you ?
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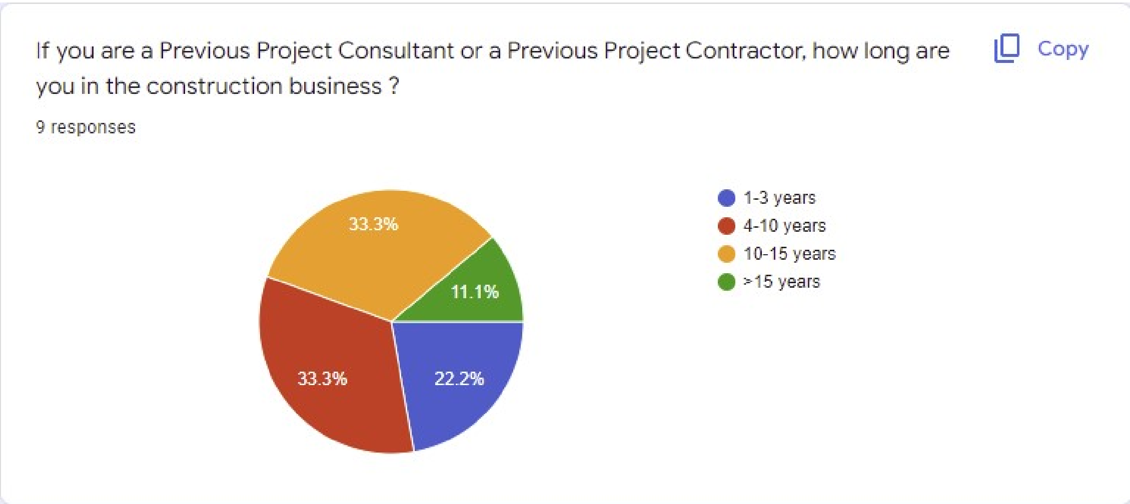
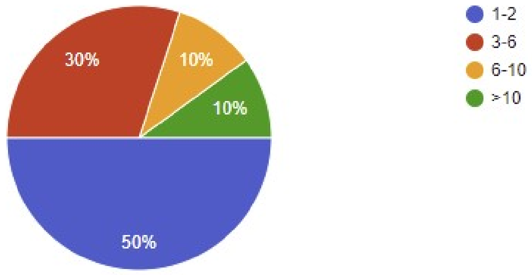
8 responses
62.5%
37.5%
Previous Project Consultant
Previous Project Contractor
Previous Project Owner


If you are a Previous Project Consultant or a Previous Project Contractor, how long are you in the construction business ?
Copy
9 responses
33.3%
11.1%
33.3%
22.2%
1-3 years
4-10 years
10-15 years
>15 years

If you are a Previous Project Consultant or a Previous Project Contractor, how many projects do you undertake in a month ?

Copy

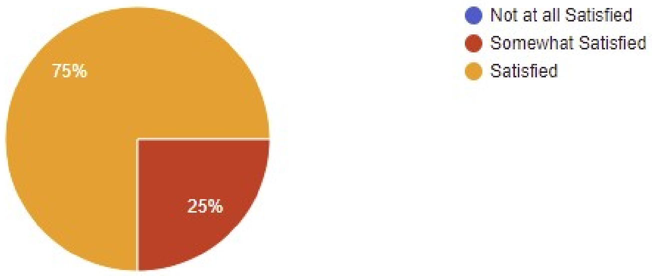
10 responses



If you are a Previous Project Consultant or a Previous Project Contractor, are you satisfied with DDE's quality of work ?

Copy

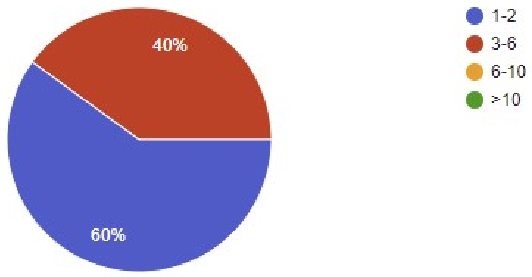
8 responses



If you are a Previous Project Consultant or a Previous Project Contractor, how many projects did you work with DDE ?

Copy

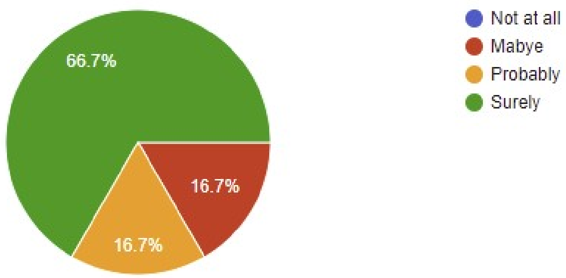
5 responses



If you are a Previous Project Consultant or a Previous Project Contractor, would you wish to work and sigh a contract with DDE again ?

Copy

12 responses



If you are a Previous Project Consultant or a Previous Project Contractor, are you happy with the current quotations that DDE offers to you ?

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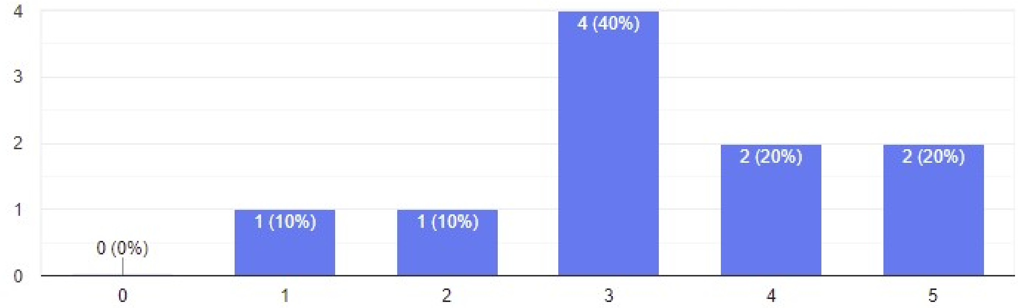
10 responses



If you are a Previous Project Consultant or a Previous Project Contractor, if you could issue tenders/payments on a monthly basis, would you issue it ?

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10 responses