



TPE 2023 – Guide to Answer

Modni

The Test of Professional Expertise multi-discipline case study is designed to encourage you to provide alternative creative answers and there is no “right answer” at TPE level. This Guide to Answer illustrates the structure and the depth of analysis and explanation the examiners were seeking.

In assessing scripts, credit is always given for appropriate answers even if not contained in this published guide.

ICAS is providing this Guide to Answer to provide direction for your own learning. Do not use this example for any other purposes.

©ICAS 2023



Notes to students: this guide contains a number of tables which were copied from the question paper. These were included to assist markers, and students were **NOT** expected to include these. No marks were available for including these.

Morning Paper Requirements

Briefing notes for Jess

1. Evaluation of Modni's financial performance and position

The retail industry has experienced significant challenges in recent years. Firstly, the competition from challenger brands as consumers moved towards online shopping. Secondly, significant uncertainties in the UK due to Brexit and finally in 2020 the impact of the Covid-19 pandemic with global lockdowns, a slow recovery and changes in customer behaviour within fast fashion retail.

Modni's financial performance has been significantly affected by these factors suffering from declining revenue and reduced profit margins culminating in a net loss in 2020 and a forecast loss in 2021.

Financial performance

This document will consider four key aspects of financial performance:

- Revenue
- Gross profit
- Covid-19 impact
- Underlying operating profit

1.1 Revenue

Headline revenue has declined significantly in 2020 predominately as a result of the challenges faced in the fast fashion retail industry sector.

The forecast for 2021 shows some recovery in revenue though levels are not yet predicted to return to pre-2020 levels as shown below in Table 1.

Table 1 Historic revenue

	2021*	2020	2019	2018	2017
	£ mill	£ mill	£ mill	£ mill	£ mill
Retail revenue	464	190	550	542	479
Wholesale revenue	180	120	325	330	283
Total revenue	644	310	875	872	762
Index (2017 base year)	85	41	115	114	100

*Forecast

Retail revenue

Modni followed an expansive strategy increasing retail square footage by 28% in the two years to 2019.

However there has been a significant decline in square footage from 2020 following the closure of 60 own stores and 125 concession outlets, this is shown below in Table 2.

Table 2 Retail square footage

	2021*	2020	2019	2018	2017
	'000	'000	'000	'000	'000
Retail square footage	799	799	1,155	1,046	901
Index (2017 base year)	89	89	128	116	100

*Forecast

This closure of unprofitable stores has improved the revenue per square foot as shown in Table 3 with a five year high projected for 2021.

These are however forecast figures and as such are dependent on a successful final quarter including the expected seasonal Christmas sales.

It is worth noting that the revenue per square foot is still below that of similar competitor Joe Dexter (pre Covid-19), suggesting further improvements could still be made.

Table 3 Retail revenue per square foot

Revenue £ per square foot	2021*	2020	2019	2018	2017
Modni retail overall	581	238	476	518	532
Joe Dexter		425	798	792	801

*Forecast

Wholesale revenue

Wholesale revenue is forecast to be £180 million which is 55% of 2019 levels. There are two drivers of this change. Firstly, the number of partners has declined significantly in 2020 and 2021, this is expected given the difficult trading environment.

Secondly, the revenue per partner is significantly below the 2019 levels. An analysis of retail partners is shown below in Table 4.

Table 4 Analysis of retail partners

Number of partners	2021*	2020	2019	2018	2017
Key accounts	36	40	50	51	51
Independent retailers	2,300	2,500	2,750	2,797	2,846
	2,336	2,540	2,800	2,848	2,897

Average revenue per partner	£'000	£'000	£'000	£'000	£'000
Key accounts	1,000	600	1,300	1,294	1,118
Independent retailers	62	38	95	94	81

*Forecast

1.2 Gross profit

Modni's gross profit margin has been in decline since 2018 falling from 61% in 2017 down to 48% in 2020. The forecast for 2021 does show some improvement as illustrated below in Table 5.

Table 5 Gross profit margins by distribution channel

Channel	2021*	2020	2019	2018	2017
Retail - own store	58%	50%	57%	65%	68%
Retail - concession	43%	50%	52%	56%	56%
Wholesale - key clients	42%	42%	42%	42%	46%
Wholesale - independents	46%	46%	46%	47%	50%
Overall Modni	54%	48%	52%	57%	61%

*Forecast

Despite difficult trading conditions competitor firms have been able to maintain a higher gross margin as illustrated in Table 6 below.

Table 6 Gross profit margin of competitors

Gross profit margin	2021*	2020	2019	2018	2017
Modni	54%	48%	52%	57%	61%
Joe Dexter		56%	58%	58%	60%
kk girl		53%	55%	56%	55%

*Forecast

There are several reasons why Modni may have seen a large decline in gross margin.

- Change in strategic direction and product mix

The company introduced three new product streams namely 'KB Sportz', 'Junior' and 'At Home'. Lower margins on Junior and the clearance of the unsuccessful 'At Home' range have contributed to the lower margins.

- Flash sales

Modni's discounting policy changed in 2018, with frequent flash sales and high discounting early in the season

- Covid-19

The closure of retail outlets for part of 2020 and 2021 led to a significant amount of surplus seasonal inventory. The subsequent inventory impairment and discounted sale items have reduced gross margins.

- Exchange rate losses

Modni's inventory is sourced from outside the UK. The uncertainty surrounding Brexit and the global recession following Covid-19 have resulted in a fluctuating GBP and consequently a higher cost of sales. Modni does not currently hedge against exchange rate risk and as a result is exposed to currency movements.

- Distribution Channel

The forecast for 2021 show an improvement in the gross margin at 54%. This is likely to be driven by the change in sales mix as a higher proportion of sales are now retail - own store. An analysis of revenue by distribution channel is shown in Table 7 below.

Table 7 Distribution channels: Revenue

Distribution channel	2021*	2020	2019
Retail - own store	70%	59%	60%
Retail - concession	2%	2%	3%
Wholesale - key	6%	8%	7%
Wholesale - independents	22%	31%	30%
Overall	100%	100%	100%

*Forecast

1.3 Covid-19 impact

The lockdown periods in 2020 and 2021 caused significant problems for Modni. Modni's operating model of physical retail with no online presence exacerbated the financial impact of the lockdown period.

Research shows online shopping is currently favoured by the younger generations and is frequently used for clothing, shoes and accessories. This is Modni's target market and so it is surprising that Modni had not identified this aspect previously.

Lockdown meant the business was severely impacted with sales falling from an average of around £73 million per month to zero (based on 2019), whilst still incurring operating costs.

Operating costs relating to this period have been excluded for the purpose of analysing underlying operating profit as shown in Table 8. These figures have been provided by Modni and as such have not been verified.

Table 8 Extraordinary net costs arising from Covid-19

	2021 £ million	2020 £ million
Operating costs with closed stores	(120)	(200)
Supplier payment for worker wages	-	(30)
Key worker inventory donation	-	(30)
Government relief	30	40
Lease savings (revenue based leases)	10	30
Delivery costs saved	5	10
	(75)	(180)

The net effect of extraordinary costs attributed to Covid-19 is a reduction in operating profit of £180 million in 2020 and £75 million in 2021. This has caused significant problems for Modni. Unfortunately, the operational problems for Modni run deeper than this as covered in the next section.

1.4 Underlying Operating Profit

The true underlying operating profit is shown in Table 9 below. This excludes the 2020 and 2021 negative impact of Covid-19.

Table 9 Underlying operating profit

	2021*	2020	2019	2018	2017
Underlying operating profit £ mill	46	(61)	62	91	96
Revenue £ mill	644	310	875	872	762
Underlying profit margin	7%	(20%)	7%	10%	13%

*Forecast

Modni's underlying operating margin has deteriorated significantly since 2017 but is showing some projected improvement for 2021.

Over the same period competitor operating margins (without adjustment for Covid-19) have also seen a decline but not on the same scale as Modni as shown below in Table 10.

Table 10 Operating profit margin

	2021*	2020	2019	2018	2017
Modni	7%	(20%)	7%	10%	13%
Joe Dexter	NA	3%	12%	13%	12%
kk girl	NA	9%	7%	7%	10%

*Forecast

The decline in Modni's underlying operating profit margin is analysed further below.

Retail operating costs

Operating costs per square foot have increased in 2020 and 2021, as shown in Table 11 below.

The increased costs could be due to changes in the operational efficiency of the warehouses and in respect of the enhanced cleaning at all locations to ensure safer conditions for staff and customers.

This could however also indicate a failure to control rising costs or be driven by reductions in efficiency within retail outlets. If Modni are not able to pass rising costs on to customers profit margins will continue to decline.

Table 11 Retail operating costs per square foot

	2021*	2020	2019	2018	2017
Cost £ per sq. ft	305	314	220	271	280

*Forecast

Wholesale operating costs

Operating costs for wholesale have been largely consistent over the last few years indicating that many of the costs may be fixed in nature.

This is an area that could be improved, with less accounts to manage it may be possible to rationalise the business further and reduce these fixed costs.

Table 12 Wholesale operating costs per retail partner and as % of revenue

	2021*	2020	2019	2018	2017
Operating costs £'mill	43	47	47	46	45
Number of retail partners	2,336	2,540	2,800	2,848	2,897
Cost £ per retail partner	18,407	18,504	16,786	16,152	15,533

*Forecast

Central operating costs

Central operating costs have continued to increase reaching a peak of £90 million in 2019 a 40% increase compared to 2017. The projected costs for 2021 show a slight improvement at £86 million but this is an area of concern and requires attention.

Table 13 Central operating costs

	2021*	2020	2019	2018	2017
New design team	10	10	10	8	
KB Royalty	10	10	10	10	
Celebrity influencers	15	15	15		
Sponsorship	5	5	5		
Other	46	47	50	55	64
Operating costs £'mill	86	87	90	73	64
Index (2017 base year)	134	140	141	114	100

*Forecast

There has been continued reduction in the 'other' operating costs highlighting that there have been ongoing improvements to efficiency since 2017.

The increase in central costs has been driven by 4 main changes:

- Design Team

Modni incurs significant costs in maintaining its award-winning design team, it is important to continue investment here as this ultimately generates future products.

- KB Royalty

Since 2018 central costs include annual royalty payments of £10 million for the partnership with Kaity Brandon for the KB Sportz brand. An analysis of direct product profitability should be carried out to confirm that the partnership is profitable for Modni.

- Celebrity Influencers

In 2020 Modni engaged with a broad range of celebrity influencers to promote Modni clothing in their social media posts. The costs of partnering with the influencers has added a further £15 million per annum to central costs. The introduction of influencers does not appear to have led to an increase in revenue and so it is not clear if this is a justifiable expense.

- Sponsorship

Since 2019 Modni has invested £5 million per annum for the exclusive sponsorship of a reality TV programme called Island Romance. Analysis should be carried out to ascertain if there is a correlation between sales and when the show is being aired in different countries. The analysis will identify if the investment is justified for Modni.

Financial position

This section will consider:

- Liquidity
- Gearing

1.5 Liquidity

The company's liquidity position has deteriorated as cash reserves have fallen from £293 million at the end of 2019 to a forecast £67 million in December 2021.

This cash has been vital for the company's survival during 2020 and 2021 but cannot be relied upon to support an unprofitable business going forward.

Further analysis of the liquidity and working capital position for Modni is shown below in Table 14.

Table 14 Liquidity and working capital ratios

	2021*	2020 Modni	2019	2020 Joe Dexter	2019
Quick ratio	1.2	1.2	2.4	0.5	0.4
Receivable days retail partners	183	142	146		
Payable days	74	60	56	116	155
Inventory days	222	215	184	264	321
Bank and cash £'million	67	80	293	(75)	15

- Quick ratio

The quick ratio is 1.2 this has deteriorated significantly since 2019 but is still greater than 1 and considerably better than that of the competitor company Joe Dexter which by comparison is dangerously low.

Given the risk of inventory obsolescence and overvaluation of inventory it is more prudent to monitor the quick ratio rather than the current ratio.

- Trade Receivables

Retail partner receivable days are 183 days which suggest a significant failing in credit control.

It is very likely that the figure is overstated and should be reviewed for impairment. Modni should address this urgently.

The difficult trading conditions increase the risk of impairment and prompt collection will provide valuable cash flow.

- Trade Payables

Payable days have been increasing gradually, and this suggests that Modni are using trade creditors as a source of short term finance, though not to the extent that Joe Dexter does.

Care must be taken that this does not damage the relationship with suppliers. Modni has done much to support suppliers in 2020 and so this action, if deliberate, suggests it is driven by cash flow necessity.

- Inventory

Inventory days are very high with approximately seven months' worth of sales held in stock.

The position is clearly favourable compared to Joe Dexter however that company has recently been criticised for a suspected overvaluation of inventory in the 2020 accounts with a potential write down of up to £70 million.

It is worth noting that the shelf life for fast fashion is typically only a few weeks with many seasonal stock items. For Modni the valuation may still include unsold 2020 inventory that the company had hoped to repurpose to 2021 seasons. It would be useful to analyse the inventory carefully and ensure that inventory is not overstated in the 2021 accounts, it is quite possible that the value may be impaired.

1.6 Gearing

The company does not have any long-term loans, however incorporation of IFRS16 from 2019 has caused gearing to increase from 0% to 75% at the end of 2020.

This would have a detrimental impact if Modni were to seek new debt finance in the future.

Conclusion *(no additional technical marks as marks awarded above.)*

The company is loss making with declining margins and has only been able to continue trading by drawing on the company's large, accumulated cash balances.

There is a significant risk regarding the valuation of inventory, and this requires urgent attention.

There is further risk regarding the recoverability of receivables with retail partners and this also requires urgent attention.

Supplier relationships are good but delays in paying suppliers may cause operational problems for Modni in the future.

To maintain the support of shareholders the directors need to present credible plans for improvements in performance beyond 2021.

Notes for phone call: Practical and operational factors for new distribution channel

The main considerations that the board will need to consider are as follows:

2.1 Functionality

Modni has already acquired the domain name and so it is a case of adding transactional functionality on to the existing website.

It is important that the website is simple to navigate ensuring that customers can search easily for products. This can be achieved by using drop down menus for categories and a search function that is able to identify products based on a range of different search criteria.

Customers should be able to reach their desired page with a minimal number of 'clicks'.

The website should be designed to operate on multiple browsers and on different smart devices, such as smart phones, tablets, and computers.

Modni may wish to consider launching their own app for even easier functionality. This would need to be functional for different operating systems.

2.2 Brand

Modni already manages a non-transactional website and so is familiar with the reflection of brand and image in the design, look and feel of the web pages.

This should be extended through the transactional aspects too, so the language should reflect that tailored to the target market of 16-25 year olds. This would typically be informal, relaxed and with humour.

2.3 Upsell and review

It will be useful to incorporate the ability to upsell

and rate the products, perhaps with the ability to add a review/customer feedback on products.

There may be the opportunity to engage with the audience further by analysing data and using this for targeted promotions to customers (see below).

2.4 Data Protection

The transactional websites will generate significant 'big data' for the company. Modni will use and process this personal data in multiple ways from the use of cookies for ease of navigation through websites, to analysis of customer buying habits for upselling, to potentially sharing with business partners such as wholesalers and suppliers.

Modni must ensure that the data is stored and processed securely and that there are suitable firewalls in place. In addition, Modni must ensure that it is processed and used in accordance with the relevant local laws such as GDPR (EU) and the UK Data Protection Act, failure to do so could lead to significant fines and a negative impact on reputation.

2.5 International aspects

As Modni operates across several European countries there will be multiple versions in different languages. Modni will need to comply with the different commercial legislation relating to sales transactions that applies in different countries.

2.6 Integration with the existing management information system

Online sales transactions will need to be integrated with the existing accounting system.

Inventory management will need to be on a real time basis to ensure that orders are only taken for in stock items and that payment is only taken once items have been despatched.

2.7 Investment in warehouse picking process

The volume of orders to be managed through the warehouses will increase significantly as multiple orders are taken for small volumes. Investment to enhance automated picking, with a focus on speed and accuracy, would be beneficial.

The introduction of quality control checks on sample dispatches could also be introduced.

2.8 Logistics for delivery

There will be significant level of dispatches from the distribution centres. Modni should consider whether this aspect of delivery should be outsourced or provided in-house. Given the pace of change this could be outsourced initially and the decision to bring in house delayed until a more stable time.

2.9 Returns process

Inevitably there will be a high level of returns. This could be for multiple reasons that are not linked to quality. For example, wrong size, not as expected, ordered more than needed with a view to return and so on.

The process for returns should be straightforward with a pre-populated returns label available for customers to print having processed the return online. This will enable simple and accurate management of real time inventory levels as bar codes are scanned on return to the warehouse.

A decision will need to be made regarding the cost of delivery and returns and whether this will be borne by the customer or Modni. A compromise could be reached by a free click and collect scheme and a charge for delivery.

There is an argument that free delivery and returns for purchases over a certain minimum value would encourage customers to purchase more items and enhance revenue.

2.10 Promotion

Modni will need to promote the online facility to customers. A quick and effective way to do this would be through the social media channels, using the social media influencers to promote this.

Promotion in retail stores would also be useful.

It is worth noting that retail partners may see the online presence as a threat to their own business, in particular some of the key accounts that have previously sold Modni branded products through their own websites. As Modni operates in multiple countries it would be sensible to launch online sales in one country initially and following the success of this roll out to other markets.

Note to students: markers were also advised to award marks for other relevant points not falling under those headings noted above.

CONFIDENTIAL

Report

Modni Plc

Prepared by Pemberton LLP

Date: November 2021

Contents

- 1 Introduction**
- 2 Executive summary**
- 3 Product and distribution channel strategies**
- 4 Review of investment opportunities**

1 Introduction

This report has been prepared for the directors of Modni to provide advice on two matters:

- Product and distribution channel strategies
- Investment opportunities

The contents of this report are intended for the sole use of the addressees and should not be disclosed to any third party without our express written permission. In producing this report, we have relied on the information provided to us to produce our advice and should any of this information be incorrect we are not responsible for any subsequent errors in our advice.

2. Executive Summary

Product and distribution channel strategies

Product

- Focus on core product areas for the Modni and Angelo Dimitri brands.
- Delay promotional discounts to later in the season.

Distribution Channels

Retail

- Continue to review and subsequently close underperforming stores.
- Consider expansion to new concession areas such as airport and train stations.

New channels

- Launch the online channel for both the Modni and Angelo Dimitri brand.
- Investigate revenue opportunities through licence income for the Angelo Dimitri brand.
- Identify and launch outlets stores as a new retail distribution channel.

Investment opportunities

- The board should focus on returning the current operations to profit and launching the transactional website as such, this report recommends that the board should not embark on any additional investment opportunities at the current time.

3 Product and distribution channel strategies

The strategies in this report address product and distribution channels for both Modni and the recently acquired Angelo Dimitri brand.

3.1 Product

Modni should review the profitability of all inventory on an ongoing basis. This will identify underperforming product lines that should be discontinued.

Discounting

The practice of discounting early in the season cycle has eroded margins and should be stopped, with discounting left to later in the cycle where possible. For example, reducing prices after the Christmas peak rather than in the run up to it.

Core brand

Modni should undertake market research and pilot launches for new product lines to test the market prior to a full launch. This could have prevented the mistakes made with the Junior and At Home ranges.

The company should stay close to its core brand and focus on the needs of its target market, age 16-25 years.

KB Sportz

The KB Sportz brand has proved successful and generates high gross margins, typically around 60%. Modni has confirmed that this brand is profitable after additional central costs and so the board should ensure that the partnership is continued.

It is noted that the alleged behaviour of Teddy Lotz has been a concern for Kaity and his departure will ease this.

Angelo Dimitri

The continuation of this brand will represent diversification for Modni with a new direction for the design team and potential changes to the supply chain given the premium nature of the product.

The board should analyse the performance of this premium product regularly and divest if suitable returns are not achieved.

The brand is well regarded, and the board should continue to focus on the target market of this luxury brand. Any changes in direction must be market tested before any new products are launched.

3.2 Distribution channels: Modni

Retail – Own store

Modni should continue to operate through their own retail stores, however the viability of each store should be reviewed on an ongoing basis.

It may be appropriate to relocate and or downsize stores in certain areas to maximise on passing footfall and shopping convenience such as out of town retail parks.

The board should be mindful of lease obligations and look for natural end points if early termination of leases is not financially viable. With difficult trading circumstances the ability to sublet retail outlets is minimal.

It may be prudent to engage professional assistance to manage lease negotiations with a view to agreeing lower rental payments for the duration of leases and or lower exit charges. For stores that will remain open it would be advantageous to move leases to revenue based leases where possible.

Retail – Concessions

The advantage of retail through concession outlets is that it extends the reach to many bricks and mortar locations with minimal investment.

Despite higher margins the absolute contribution generated by concession outlets is low as forecast concession contribution is £2 million compared to £17 million from own store.

The board should look for further opportunities here such as small concessions within airports and other transport stations.

Wholesale

This distribution channel has lower gross margins, but the operating costs are significantly lower such that the contribution towards central costs is double that of retail outlets. (Appendix 1).

Modni should consider ways to increase retail partners, particularly those that would be classed as key based on their size. Key partners do have lower gross margins but would benefit from economies of scale when compared to smaller independent partners.

It is worth noting that there may be a detrimental impact on key partners as Modni will now compete directly with some retail partners through the new online channel.

3.3 Distribution channels: Angelo Dimitri

Modni will need to consider the distribution channels open for the Angelo Dimitri brand. Given the exclusive nature of the brand the current distribution channels are unlikely to provide a suitable outlet as the brand focus is quite different to Modni.

New distribution channels for Angelo Dimitri are discussed in the next section.

3.4 New distribution Channels: Modni and Angelo Dimitri

Online

As acknowledged by the board, Modni is to prioritise the development of its online distribution channel. Industry trends indicate that consumer preference for online shopping will continue, it is likely that the bricks and mortar presence will decline further as growth in online sales continues.

The level of decline will depend on the importance that is attributed to having some physical presence on the high street. The success of challenger brands such as kk girl would suggest that such presence is no longer a prerequisite for success.

This channel will also provide an efficient way to sell discounted inventory items for both Modni and Angelo Dimitri without taking up valuable retail space in stores.

Retail outlets can then focus on increasing revenue per square foot by prioritising full price items.

Licencing

A new distribution channel to consider would be a licensing agreement using the Modni, KB Sportz and Angelo Dimitri brands. Examples include perfume, footwear, fashion watches and wearable tech.

Outlet store

Modni should also consider opening several outlet stores as an alternative way to retail slow moving/obsolete inventory.

This will be particularly useful for Angelo Dimitri as this will enable some control over pricing and the brand.

Conclusions and recommendations *(marks awarded in the main body of the report)*

Modni should focus on its target market of 16-25 year olds, which includes continuing the successful partnership with KB.

Angelo Dimitri presents an opportunity for diversification; the performance of the brand should be monitored and if a satisfactory profit margins are not achieved Modni should divest the brand.

Modni should continue to review the performance of retail outlets and divest if performance is not satisfactory. Consultants should be engaged to negotiate lower revenue based rents and early exits for store selected for closure.

Modni should consider options for expansion to new concession areas such as airport and train stations.

Modni should proceed as soon as possible with the launch of the online sales channel using this for both the Modni and Angelo Dimitri brand.

There may be opportunities for new revenue streams through licencing income, with the Angelo Dimitri brand in particular and through the launch of outlets stores in suitable locations.

3.5 Appendix

Operating profit by distribution channel	Forecast 2021	2020	2019
Retail - Own store	£ million	£ million	£ million
Revenue	450	184	525
Gross profit	261	92	299
Operating costs	(244)	(251)	(245)
Contribution towards central costs	17	(157)	45
Contribution/sales %	4%	(85%)	9%
Retail - Concession	£ million	£ million	£ million
Revenue	14	6	25
Gross profit	6	3	13
Operating costs	(4)	(5)	(6)
Contribution towards central costs	2	(2)	7
Contribution/sales %	12%	(39%)	27%
Wholesale	£ million	£ million	£ million
Revenue	180	120	325
Gross profit	81	54	147
Operating costs	(43)	(47)	(47)
Contribution towards central costs	38	7	100
Contribution/sales %	21%	5%	31%
Overall	£ million	£ million	£ million
Retail contribution	19	(161)	52
Wholesale contribution	38	6	100
Central costs	(86)	(87)	(90)
Operating (loss)/profit	(29)	(242)	62

4 Investment Opportunities

This section of the report considers two potential investments currently under consideration. The board have already received detailed financial analysis regarding the payback and NPV of each investment. All opportunities are financially viable, and the board do not see them as mutually exclusive.

This report considers the risks, rewards, and other considerations of each opportunity.

Summary

	Concept Store in Birmingham	Japanese Expansion 10 stores
Initial Investment	£40 million	£50 million
Square ft	100,000	100,000

4.1 Financial investment

Modni has a forecast year end cash balance of £67 million, Modni has recently committed £20 million for the purchase of Angelo Dimitri and is investing in a new transactional website.

The launch of online sales is likely to require additional investment in the warehouse with improvements needed in operations such as warehouse picking and logistics for despatch and returns.

It is not clear if these investments have been reflected in the forecast and so the available funds could be considerably lower.

The board would need additional long term finance to pursue both options. The level of new finance required will depend on the levels of cash required to manage working capital requirements.

Modni's current position and recent financial performance suggest that the board may find it difficult to raise further finance at this time.

Concept Store in Birmingham

4.2 Rewards

The investment in a concept store in Birmingham would also raise the profile for Modni. This would be an opportunity to shape the customer experience in physical retail bringing shoppers back from the online world.

Modni would be able to showcase not only the Modni brand but also have designated areas for the KB sportswear, Angelo Dimitri, and any other new launches or acquisitions in the future.

New store design concepts could also be tested at the store. This could include the use of plus size, gender neutral and para sports mannequins, the latter for the KB sportswear range.

In addition, the innovative modern designs, out of town location, free parking, and regular entertainment events for children, arts demonstrations and craft stalls are likely to attract visitors and hence increase footfall indicating that this would be more successful than some of the older city centre locations.

Modni would be able to work with a variety of other businesses incorporating leisure services such as bowling, cinema and food and beverage. In addition to generating rental income this business ecosystem is likely to benefit from a further increase in footfall leading to increased revenues and profits.

By combining leisure as well as retail experiences there may be opportunities for new business areas for Modni themselves such as their own café, bar, or restaurant.

Alternatively, Modni could seek to identify suitable businesses that would be willing to work in partnership with Modni, this would reduce the risk but would of course reduce the returns too.

4.3 Risks

There are those that consider the future of retail to be online, reflecting a cultural shift that was accelerated due to Covid-19 in 2020. The return to the large store experience is seen as outdated and unprofitable. Many retailers are focusing on trying to reinvent the physical shopping experience with false expectations of likely revenue and profit. Put simply, the concept may fail.

A new large store would also increase the operating gearing as this would involve increased operating space.

4.4 Other factors to consider

Strategically the store could help strengthen Modni's brand, differentiating Modni from the challenger online brands. The store could be used to showcase Modni's CSR initiatives.

Public relations events at the store could be used to promote partnerships with celebrities such as KB and Bella Blue. This could improve the reputation of Modni showing that the partnership with KB will continue despite the allegations against with the former CEO, Teddy Lotz.

Modni has no experience of working with other business partners or in areas outside fashion. Modni would need to engage suitable skilled personnel to manage and lead this initiative.

If the concept store is successful there may be opportunities to replicate this model in other locations.

If the investment were not successful Modni would find it difficult to let or sell the store.

Launch in Japan

4.5 Rewards

Modni has some experience of operating on a global platform but this is restricted to operations of the Modni brand within Europe.

Japan was identified as a region where the brand is popular and so initial market research indicates that establishing a sales network would be beneficial.

This can be done with relatively low levels of investment and presents a scalable opportunity for Modni to grow through investment in new own stores.

4.6 Risks

The brand may not be successful in Japan.

There would be exchange rate risks relating to both transactions and translation of overseas assets and liabilities.

There would be exposure to political and legal risks.

4.7 Other factors to consider

There would be practical issues re the logistics of supplying stores.

Time and language differences would also need to be managed.

It is likely that there would be additional costs to develop an appropriate local website.

This venture is for short term leases and so would be relatively easy to withdraw from if not successful.

4.8 Conclusion and recommendation

Modni's recent financial performance and current position indicate that the current board should prioritise improving the performance of the current operations and focusing on the existing projects namely launching the transactional website and developing the newly acquired Angelo Dimitri brand, consequently undertaking any new investments at the current time is not recommended.

Once Modni has returned to a profitable position the new board can consider strategies for expansion.

Email To: Nick Purcell

From: Jess Sharp

Subject: The Post News and background information

Date: 9 November 2021

Hi Nick

Thank you for the phone call this morning. Here are my thoughts regarding actions with The Post News, options for obsolete inventory and some relevant industry background information that should be helpful.

5.1 Short term response

Modni should issue a press statement confirming that:

- The company's policy is to ensure that the company has high standards and suppliers must pass rigorous checks before being approved as a supplier.
- Supplier factories are visited on a regular basis and there has been no indication of improper behaviour.
- Modni will conduct an internal enquiry regarding the allegation but are confident that current processes are sufficient and in line with Modni's stated policy. Once the enquiry is complete Modni will publish the findings.

5.2 Actions

- Conduct an enquiry and publish the findings and response
- If the claim is incorrect
 - Consider legal action against the newspaper for false allegations
- If the claim is correct there are several possible longer term solutions
 - Cease to use the supplier at the earliest opportunity
 - Improve the supplier vetting process to avoid future incidents occurring
 - Continue to use the supplier but work with them to ensure a fair wage is paid enabling adults to be able to support families and thus avoid the need for child labour
 - Support local education projects where the suppliers are based raising the standard of education for workers families
 - Conduct wider investigation of other factories within the supply chain including work subcontracted by suppliers

5.3 Options for disposal of obsolete inventory

Ordinarily a retailer has the following options regarding the sale of obsolete inventory:

- End of season sales
- Sale via outlets stores
- Donate to charity

Such practices would usually be acceptable for Modni however as Angelo Dimitri is a premium brand the above actions could be detrimental to the brand value.

This places Modni in a difficult position if it transpires that there is surplus overvalued inventory. Other high end brands have been criticised in the past for burning or landfilling inventory as a way of solving such a problem.

To maintain the exclusivity of the brand and protect Modni's reputation it is recommended that surplus inventory is sold through a limited number of controlled channels such as selective retail partners and online. Discounting levels can be controlled to minimise the impact on the brand.

Wider stakeholder concerns

Recent media reports have addressed several areas that raise concerns for various stakeholder groups. These can be categorised as environmental and social concerns.

5.4 Environment

The fast fashion industry produces seasonal items that are often worn only a handful of times before becoming out of date. Filled with good intentions, many consumers give these now unwanted clothes to charity shops for resale. The scale of this is such that most of the clothing is not resold and instead ends up in landfill. This cycle is promoted by the fast fashion industry through the short life cycles of products and many believe there should be more accountability for this.

The growth in online sales has led to reduced efficiency in outbound logistics and higher emissions from 'white van' drivers. To protect bricks and mortar businesses and to reduce environmental concerns, governments are considering the introduction of a sales tax for online sales, depending on the level of tax this may reduce the growth of this distribution channel.

5.5 Social

The industry has been criticised for the oversexualisation of young girls and the consequential impact on the mental health on what is part of Modni's target market. Many retailers are tackling this through promotion of body positivity throughout stores and embedded within advertising campaigns.

Modni needs to keep up to date with social issues and adapt stores and products accordingly. Recent examples of social change include the use of gender neutral changing rooms, and mannequins and models that are representative of society.

Please do not hesitate to get in touch if there is anything else we can help with.

Kind regards

Jess Sharp

Email for ethics partner

To: Ethics partner
 From: Charlie Tarazi
 Subject: Matters for attention
 Date: Today

A number of matters have come to my attention during my assignment work on Modni. I have separated these into concerns within Pemberton and concerns within Modni.

Pemberton

Lack of due care and attention

(Ethical principle: Professional competence and due care)

Due to the illness of a manager within the firm there has been an increase in workloads for other managers, resulting in excessive levels of overtime. This is not sustainable and is damaging for the wellbeing of staff. It is also likely to have a knock on effect as overworked staff are likely to make mistakes, with potential longer term implications for the firm.

A further example of this was that I was asked to rely on client figures without any validation in order to perform the work quicker. This would breach the principle of **professional competence and due care**.

The firm should ensure that future work is only accepted if there are sufficient resources available. It may be appropriate to recruit a manager on a temporary contract to cover for the manager currently absent on long term sick leave.

Bias in reporting

(Ethical principle: Objectivity)

Jess Sharp indicated that the documents I produce for the board should show Teddy Lotz in a positive light. Clearly this is bias and would be a breach of the **objectivity** principle.

The firm should ensure that managers are aware of their responsibility to report in an objective manner. This could be addressed through ongoing formal training or through the firm's appraisal process.

Bribery

(Ethical principles: Professional behaviour, Integrity and Objectivity)

During the course of my work, I have been offered store vouchers as a 'thank you' for the work that I have completed. It appears that Jess Sharp has also received vouchers and it may not be a one off event. The firm's policy is that we cannot accept gifts from clients as this is a breach of the objectivity principle it also raises concerns regarding whether there has been a breach of The Bribery Act with potential criminal implications for the firm.

Inappropriate reference to Modni's chairman

(Ethical principle: Professional behaviour)

Some may feel that comments regarding a client's visual appearance good or bad are harmless however I consider the behaviour to be unprofessional and inappropriate. Jess Sharp made an inappropriate reference regarding Nick Purcell, Modni's chairman. This would breach the principle of **professional behaviour**.

In this instance Jess should be advised that her comments were inappropriate, and she should maintain her professionalism with colleagues and clients.

Modni

Culture

(Ethical principles: Professional competence and due care and professional behaviour)

I am concerned that there may be weaknesses within the control environment of Modni. The company is now being led by a dominant CEO that was instrumental in the departure of Teddy Lotz. This weakness would challenge the **professional competence** of the board.

The allegations against Teddy Lotz may prove to be true, indicating a culture where inappropriate behaviour was acceptable and promoted. This would not be **professional behaviour**.

The company engages with celebrity influencers and does not monitor disclosure of paid advertising, which is likely to be harmful to Modni's reputation if this was later revealed. This may challenge the principle of **professional behaviour**.

Board

(Ethical principle: Professional competence and due care)

The board currently comprises three directors, whilst this is an interim position the current leadership is far below the requirements of good corporate governance. Failure to abide by the Code implies lack of **professional competence and due care** though this may be short term concern caused by the recent board changes.

Risk management

(Ethical principle: Professional competence and due care)

I was concerned at the lack of risk management within the company. The company sources all products from outside the UK and consequently is exposed to significant foreign exchange risk. It is surprising that a company of this size has deemed it acceptable to accept this risk. The weakness in risk management suggests a lack of **professional competence and due care**.

The company may suffer from reputational risk through the allegations regarding Teddy Lotz and claims of inappropriate behaviour with a supplier.

Going concern

(Ethical principle: Integrity and objectivity)

Our work has shown that the company had seen a continued decline in performance and a weakened liquidity position. There is a real concern regarding the going concern status of the company.

As Modni is not an audit client we are not under obligation to report on the going concern status of the company. We should share our concerns with the board and make further recommendations for improvement. Failure to share our concerns

There may be fee recovery implications for Pemberton if Modni does encounter going concern and liquidity problems.

Please contact me if you would like to discuss any matters further.

Kind regards

Charlie