



Strategy Case Study - Monic

Case study – Monic

About Monic:

Monic is an online organic clothing brand based in Phoenix, Arizona. The company was established in 2015 by a young entrepreneur, Marvis Carson, and the business has been growing rapidly in past few years.

The company uses fabrics 100% made from Global Organic Textile Standard (GOTS) certified organic cotton sourced from a local cotton farm. All of Monic's branding pieces on the clothing including woven labels, printed labels and hang tags are made of recycled materials. The whole process of fiber manufacturing, spinning, weaving, knitting, dyeing and product finishing is completed in U.S., where the workers are fairly paid and ensured a healthy and safe work environment.

Monic's products include T-shirts, sweaters and cardigans. Their prices range between \$30 to \$60.

Vision

To become one of the top online organic fashion brands

Mission

To provide premium U.S.-made organic apparel for anyone in the world

Values

- Quality – We believe our organic cotton products present high standard of quality to consumers
- Eco-friendly – We believe everyone has a responsibility to contribute to a greener planet
- Ethical – We believe being ethical is the key to success of our business

Monic's Income Statement

Income Statement			
US \$	2015	2016	2017
Sales	5,600	18,680	33,356
Cost of goods sold	(2,850)	(6,775)	(11,710)
Gross profit	2,750	11,905	21,646
<i>Gross margin</i>	49.1%	63.7%	64.9%
Selling and administrative expenses	(1,067)	(2,425)	(3,060)
Marketing expenses	0	(369)	(408)
Depreciation expenses	(1,050)	(1,050)	(1,903)
Operating profit	636	8,061	16,275
<i>Operating margin</i>	11.3%	43.2%	48.8%
Interest expense	(896)	(1,098)	(1,655)
Earnings before tax	(260)	6,963	14,620
Tax	-	(1,044)	(2,193)
Net income	(260)	5,919	12,427

Monic's Balance Sheet

Balance Sheet			
US \$	2015	2016	2017
Assets			
Current Assets			
Cash	7,438	15,402	31,460
Accounts receivable	940	5,600	14,790
Inventories	1,300	1,559	1,998
Total Current Assets	9,678	22,561	48,248
Fixed Assets			
Equipment	10,500	9,650	12,305
Capital expenditures	19,722	28,993	27,112
Total Fixed Assets	30,222	38,643	39,417
Total Assets	39,900	61,204	87,665

Balance Sheet			
US \$	2015	2016	2017
Liabilities			
Current Liabilities			
Accounts payable	2,205	4,190	6,960
Accrued expenses	638	1,688	3,883
Interests	560	1,070	3,395
Total Current Liabilities	3,403	6,948	14,238
Long-term debt	10,256	22,356	29,100
Total Liabilities	13,659	29,304	43,338
Owner's Equity			
Capital contributions	26,241	31,900	44,327
Total Liabilities and Owner's Equity	39,900	61,204	87,665

Monic's Cash Flow Statement

Cash Flow Statement			
US \$	2015	2016	2017
Operating Cash Flow			
Net Income	(260)	5,919	12,427
Plus: Depreciation & Amortization	1,050	1,050	1,336
Less: Changes in Working Capital	(1,163)	1,374	2,339
Cash from Operations	1,950	5,595	11,991
Investing Cash Flow			
Investments in Property & Equipment	(31,012)	(353)	(2,855)
Cash from Investing	(31,012)	(353)	(2,855)
Financing Cash Flow			
Owner's Capital Contribution	26,241	5,659	12,427
Changes in Long-Term Debt	10,259	(2,934)	(5,508)
Cash from Financing	36,497	1,559	7,700
Net Increase (decrease) in Cash	7,438	7,964	16,058
Opening Cash Balance	-	7,438	15,402
Closing Cash Balance	7,438	15,402	31,460

Monic's operations metrics and financial ratios

Operations Metrics			
US \$	2015	2016	2017
Number of products sold	102	460	782
Average order value	\$38.6	\$40.6	\$42.7
Material cost	\$890	\$1,959	\$3,206
Labor cost	\$1,670	\$4,040	\$6,538
Shipping cost	\$290	\$776	\$1,966
Total variable cost	\$2,850	\$6,775	\$11,710
Material cost/unit	\$8.7	\$4.3	\$4.1
Labor cost/unit	\$16.4	\$8.8	\$8.4
Shipping cost/unit	\$2.8	\$1.7	\$2.5
Variable cost/unit	\$27.9	\$14.7	\$15.0
Warehouse rent	\$400	\$400	\$460
Salaries and benefits	\$667	\$2,025	\$2,600
Marketing expenses	-	\$369	\$408
Total fixed cost	\$1,067	\$2,794	\$3,468

Financial Ratios			
	2015	2016	2017
Liquidity ratios			
Current ratio	2.84	3.25	3.39
Acid-test ratio	2.46	3.02	3.25
Leverage ratios			
Debt ratio	34.2%	47.9%	49.4%
Debt to equity ratio	52.1%	91.9%	97.8%
Efficiency ratios			
Asset turnover ratio	0.14	0.31	0.38
Inventory turnover ratio	2.19	4.35	5.86
Receivables turnover ratio	5.24	2.94	1.98
Days sales in inventory	166	84	62
Profitability ratios			
Return on assets ratio	-0.7%	9.7%	14.2%
Return on equity ratio	-1.0%	18.6%	28.0%
Labor cost ratio	29.8%	21.6%	19.6%
Material cost ratio	15.9%	10.5%	9.6%

Online organic clothing industry outlook

Industry Overview

The online organic clothing industry is growing as a result of increased public awareness of organic and ethical sources of clothing materials.

The number of organic cotton farmers has been rising worldwide, leading to increased global organic cotton production volume (40% growth in 2017). This encourages more online apparel brands to begin producing clothing made of GOTS certified organic fabric or a mix of organic and non-organic materials.

The infographics summarize the important statistics about the online organic clothing sector in 2017.

Raw Material Cost

The average cost of raw organic cotton has been decreasing due to increased global production volume

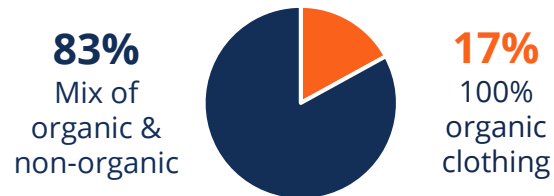
US\$1.25
per pound of organic cotton in 2016

VS

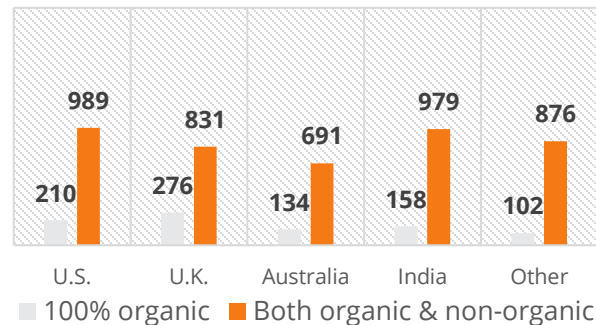
US\$1.04
per pound of organic cotton in 2017

Market Segmentation

There are two main types of organic clothing businesses: 100% organic and mix of both organic & non-organic



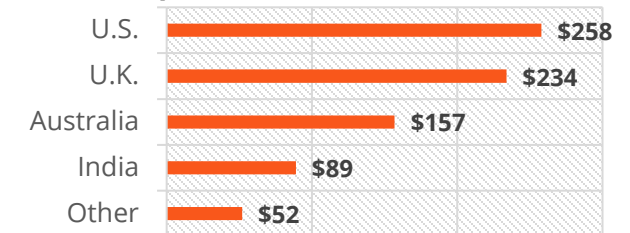
Number of online organic clothing stores in 2017



Market Growth

The global online organic clothing market is growing rapidly and consumer demand is also increasing

Top 5 markets in 2017 (US\$M)



US\$3.8B

Global organic clothing market sales 2017



+15%

Global organic clothing market sales growth from 2016



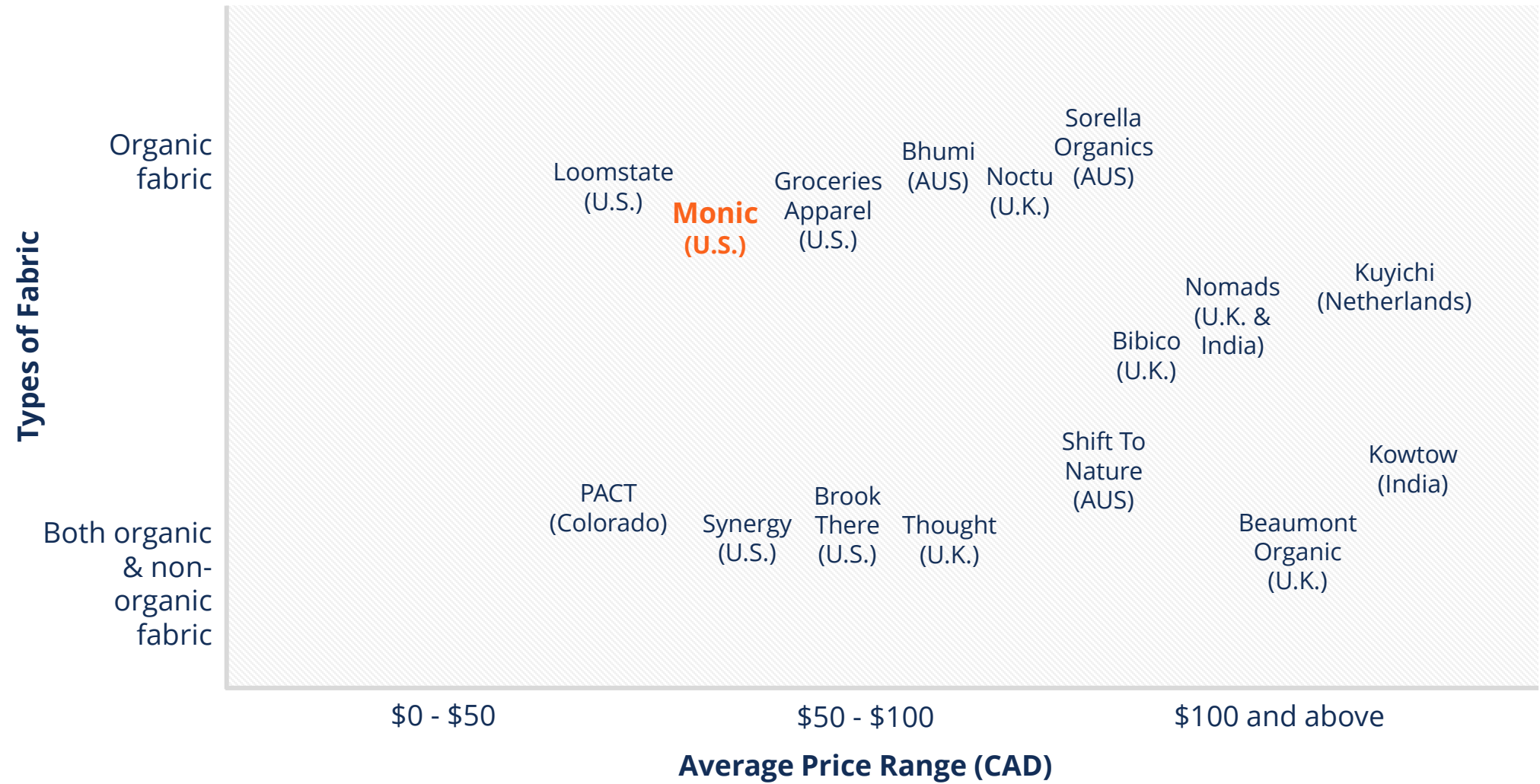
+28%

Total number of online organic clothing companies in the top 5 markets

Monic's supply chain



Strategic group map for online organic clothing industry



Competitive forces model

Intensity of industry rivalry

- Low concentration of rivals in the online organic clothing industry
- Low switching costs for customers
- Variety of organic apparel offerings

Power of complementary good/service providers

- Availability of other clothing products made of organic cotton such as pants, socks and hats might have an impact on the sales of organic cotton tops

Threat of substitute goods/services

- Small number of online organic clothing substitutes in the market, but switching costs are low for customers



Threat of potential entrants

- Low barriers to entry
- Sourcing organic and ethical cotton farmers could be a challenge to entrants
- No significant fixed costs or investment
- Low market penetration

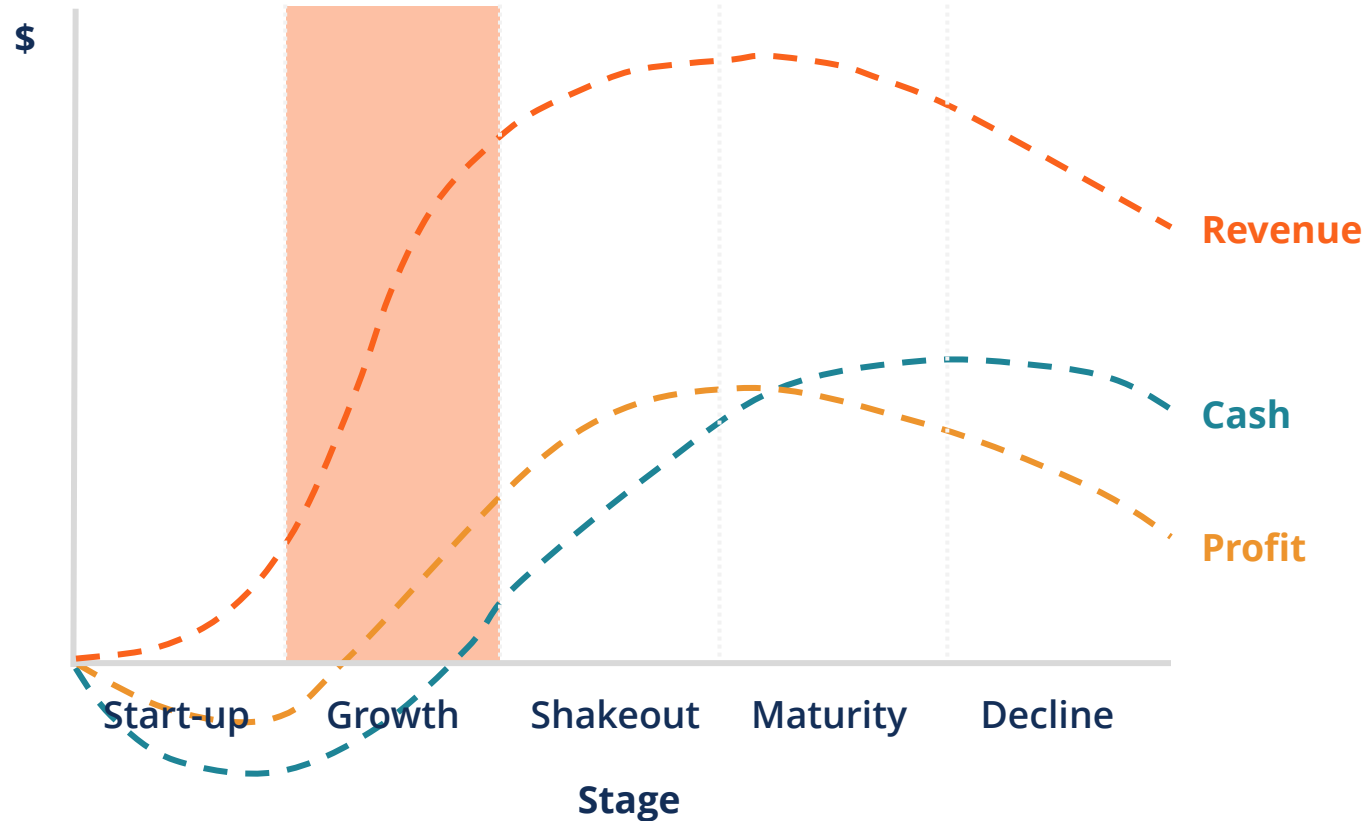
Bargaining power of buyers

- Low to medium buyers' price sensitivity
- Organic fabric are perceived as better product than non-organic fabric, thus allows companies to charge higher prices

Bargaining power of suppliers

- High suppliers' bargaining power because of limited supply of organic cotton
- GOTS implies high cotton quality, therefore allows suppliers to set higher costs

Industry life-cycle

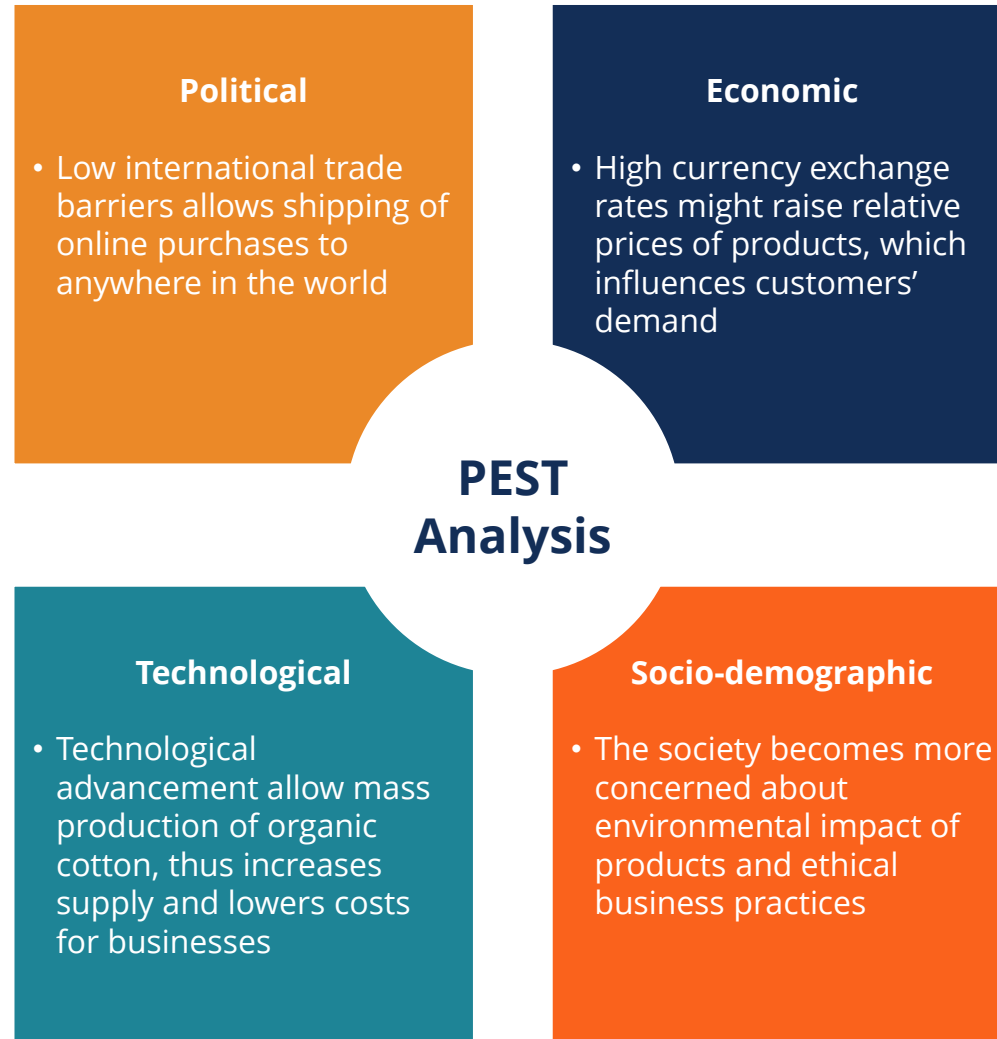


The online organic clothing industry is at the growth stage where the demand for ethically and organically made apparel is rapidly increasing. Monic is expected to face low threat from potential competitors due to low market penetration and excess production capacity.

As we can see from Monic's financial statements, the company has been earning low profits in the past three years and has low cash balances on its account. This is due to the amount of capital initially invested in the business, including the cost of purchasing equipment, finding an ethical and organic cotton source, production costs, etc.

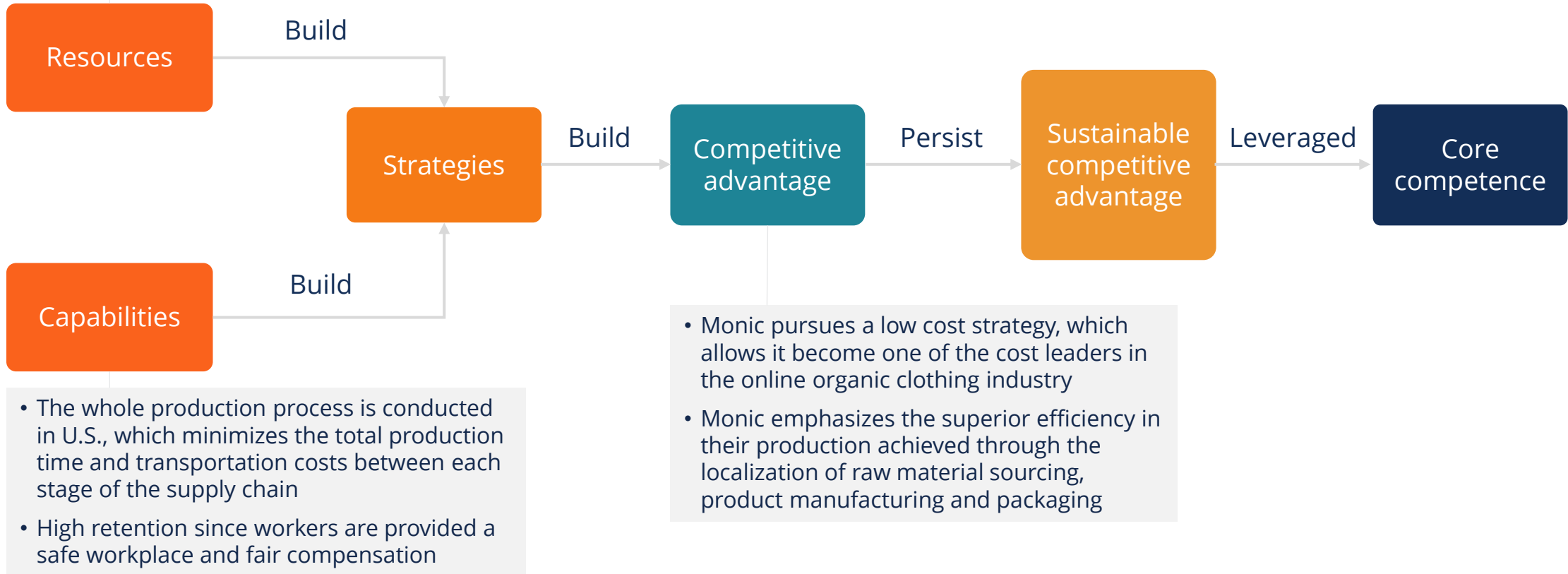
The revenue for Monic has grown dramatically, increasing by 234% and 79% in 2016 and 2017 respectively. This is a typical scenario for company in a growing industry since there are many opportunities to expand its business.

Broad factors analysis (PEST)

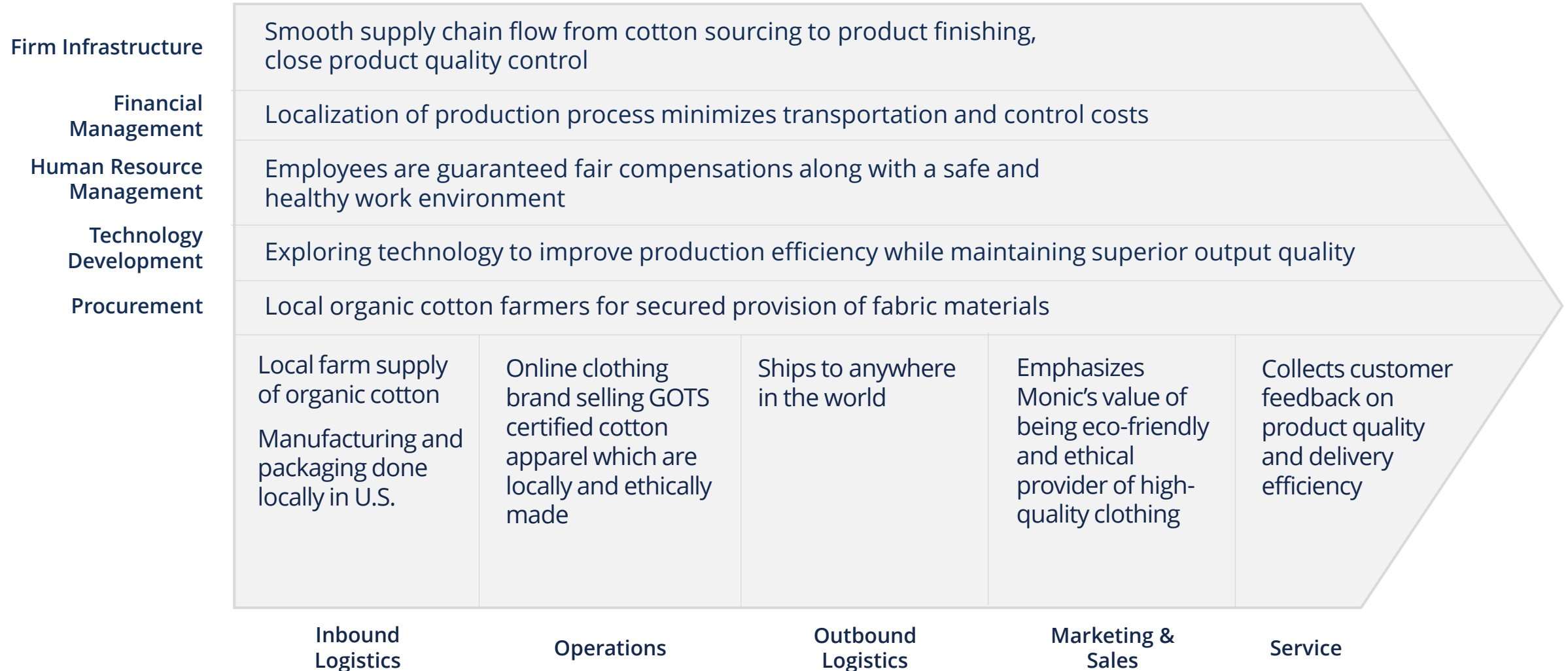


Monic's competitive advantage

- Monic has a secured source of organic cotton provided by a local farm
- Monic hires workers who have over ten years of experience in manufacturing cotton apparel, enhancing efficiency and productivity



Monic's value chain example



Product-market segments

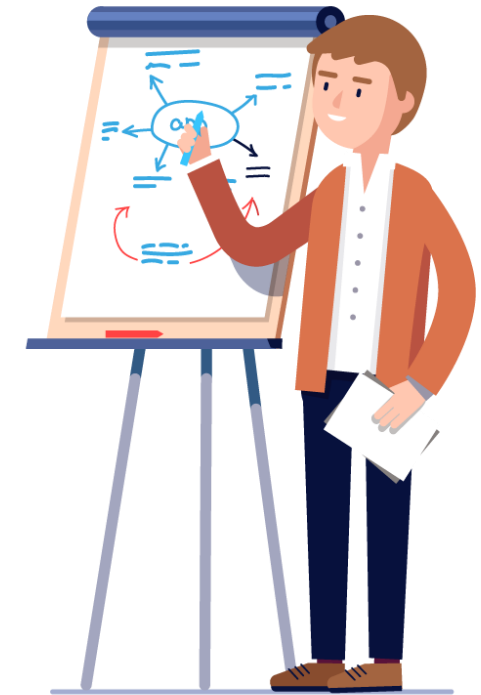
Product	Customer		
	General public	Awareness of purchasing organic clothing	Organic clothing supporters
	T-shirts, sweaters and cardigans	✓	✓
	Bottoms		
	Footwear		
	Hats, caps and beanies		

Monic's current focus is selling organic cotton tops including T-shirts, sweaters and cardigans. It targets a broad customer segment and sells to anyone who are generally interested in fashion or organic products.

In response to the growing market size of the industry and increasing customer demand, Monic plans to enter into selling of other organic cotton products such as pants, socks, hats and beanies. These products are expected to attract increasing number of customers, comprised of mainly organic clothing supporters or consumers who would prefer to purchase organic clothing if available.

Monic's closer focus in these market segments will allow the company to produce superior clothing matched to the needs of these customers.

Monic's current strategies



Strategic alternatives

After performing the external and internal analysis and reviewing its current strategies, Monic is considering these three strategic alternatives to expand its product collections and attract more customers:

A. Selling organic cotton pants

B. Selling organic cotton beanies

C. Selling organic cotton shoes

The table on the right summarizes the production capacity and financial details of each of the alternatives.

Strategic alternatives	A. Selling organic cotton pants	B. Selling organic cotton beanies	C. Selling organic cotton shoes
Sizes	S, M, L	One size	Size 5 – 10
Annual production	600	520	300
Expected units of sale	550	360	320
Average product price	\$55	\$30	\$76
Revenue	\$30,250	\$10,800	\$24,320
Material cost/unit	\$5.7	\$2.4	\$6.8
Labor cost/unit	\$10.2	\$5.5	\$12.5
Shipping cost/unit	\$2.8	\$1.1	\$3.1
Variable cost/unit	\$18.7	\$9.0	\$22.4
Total variable cost	\$10,285	\$3,240	\$7,168
Inventory storage cost	\$560	\$180	\$600
Additional workers	2	1	2
Salaries and benefits	\$7,000	\$3,100	\$8,600
Marketing expenses	\$1,000	\$1,000	\$1,000
Total fixed cost	\$8,560	\$4,280	\$10,200
Operating profit	\$11,405	\$3,280	\$6,952
Operating margin	37.7%	30.4%	28.6%
Capex (one-time expense)	\$10,000	\$5,000	\$16,000
Product durability (out of 5)	4	3.5	5

Multi-criteria analysis (criteria)

To determine the optimal strategic alternative, Monic uses the following scorecard to evaluate the attractiveness of each alternative:

		Decision Rule			Score
Pillar	Attributes	Attractive	Moderate	Unattractive	Weight
Financial	Revenue	>\$30,000	>\$20,000	<\$20,000	+2
	Operating margin	>30.0%	>25.0%	<25.0%	+1
	Labor cost ratio	<18.3%	<18.5%	>18.5%	+1
Customers	Product durability	5/5	>4/5	<4/5	+2
	Demand	>400	>300	<300	+1
Operations	Annual production	>500	>400	<300	+1
	# product size	1	2 – 3	>3	+1
Human Resources	Additional workers	1 or less	2	>2	+1

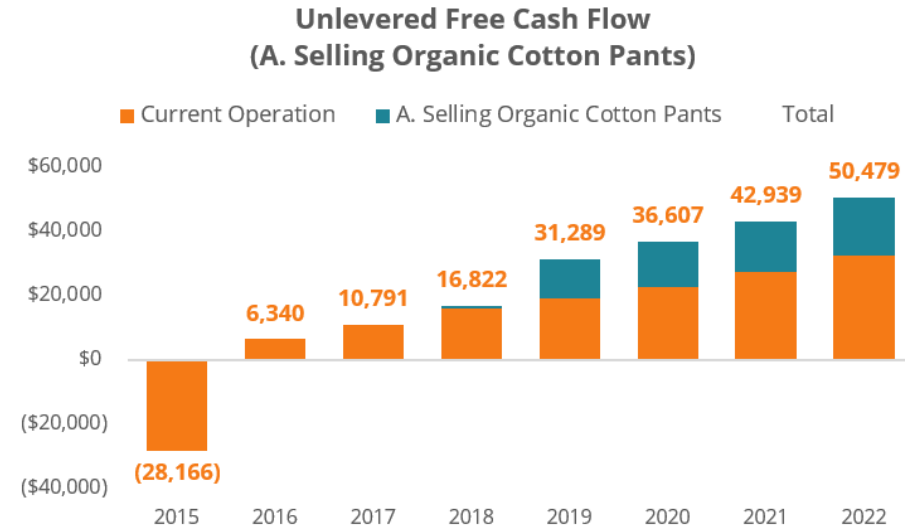
Multi-criteria analysis (results)

Pillar	Attributes	A. Selling organic cotton pants	B. Selling organic cotton beanies	C. Selling organic cotton shoes	Score	
					Winner	Weight
Financial	Revenue	\$30,250	\$10,800	\$24,320	A	+2
	Operating margin	37.7%	30.4%	28.6%	A	+1
	Labor cost ratio	18.5%	18.3%	16.4%	C	+1
Customers	Product durability	4/5	3.5/5	5/5	C	+2
	Demand (Based on survey results)	486	452	270	A	+1
Operations	Annual production	600	520	300	A	+1
	# product sizes	3	1	6	B	+1
Human Resources	Additional workers	2	1	2	B	+1
Total Points Scored		5	2	3	A	

Based on the result of the multi-criteria analysis, Monic should ideally pursue the strategy of **selling organic cotton pants** in addition to its existing products. This will allow Monic to increase both revenue, operating margin and annual production.

DCF analysis

Case Study - Monic	2015	2016	2017	2018	2019	2020	2021	2022
DCF Valuation (A. Selling Organic Cotton Pants)								
Free Cash Flow								
EBIT				11,405	13,116	15,083	17,346	19,947
Less Taxes				1,711	1,967	2,262	2,602	2,992
Less Capex				10,000	-	-	-	-
Plus Depreciation				1,800	1,800	1,800	1,800	1,800
Less Changes in Working Capital				500	550	605	666	732
Unlevered Free Cash Flow				994	12,398	14,016	15,878	18,023
Total FCF (Current Operation + Alternative A)	(28,166)	6,340	10,791	16,822	31,289	36,607	42,939	50,479
DCF Valuation								
NPV	122,767							
Cost of Capital	15%							
Perpetual Growth Rate	2%							
Terminal Value	396,067							
NPV of Terminal Value	171,230							
Total Enterprise Value	\$293,997							

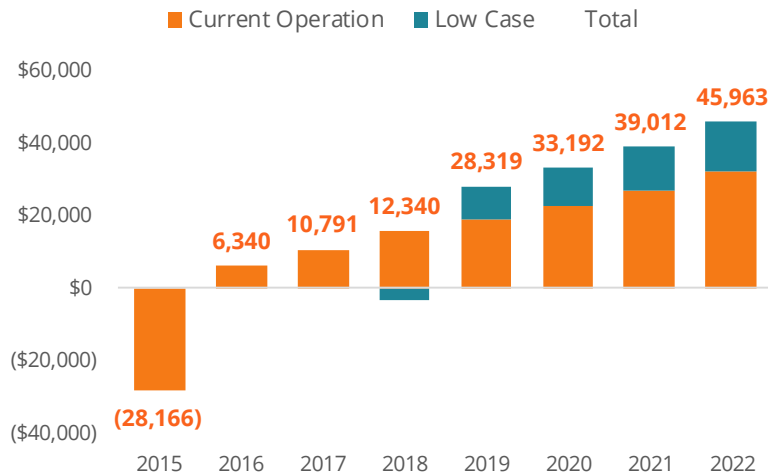


Forecast scenarios for strategic alternative

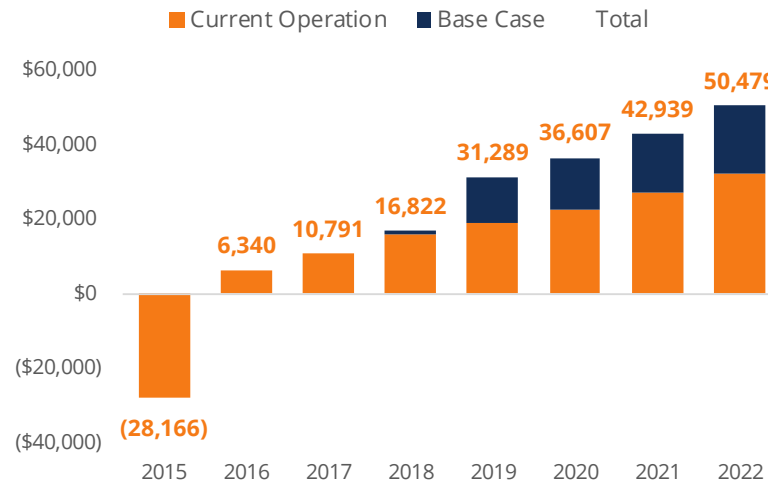
Scenario Analysis	Alternative A. Selling organic cotton pants		
	Forecast Scenarios		
	Low Case	Base Case	High Case
Expected units of sale	470	550	630
Average product price	\$55	\$55	\$55
Revenue	\$25,850	\$30,250	\$34,650
Material cost/unit	\$5.8	\$5.7	\$5.6
Labor cost/unit	\$10.2	\$10.2	\$10.2
Shipping cost/unit	\$2.9	\$2.8	\$2.7
Variable cost/unit	\$18.9	\$18.7	\$18.5
Total variable cost	\$8,883	\$10,285	\$11,655
Inventory storage cost	\$600	\$560	\$540
Additional workers	2	2	2
Salaries and benefits	\$7,000	\$7,000	\$7,000
Marketing expenses	\$1,000	\$1,000	\$1,000
Total fixed cost	\$8,600	\$8,560	\$8,540
Operating profit	\$8,367	\$11,405	\$14,455
Operating margin	32.4%	37.7%	41.7%
Capex (one-time expense)	\$11,900	\$10,000	\$8,800

Forecast scenarios - DCF analysis

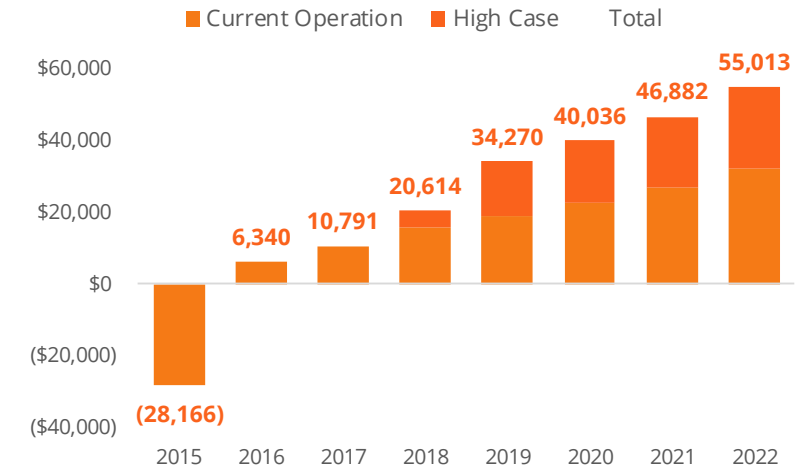
Unlevered Free Cash Flow (Low Case)



Unlevered Free Cash Flow (Base Case)



Unlevered Free Cash Flow (High Case)



Monic's strategic pillars



• Current strategies

• Strategic alternatives