



Strategy Case Study - Monic

This document contains extracts from Monic's annual report for 2017

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Company overview

Monic is an online organic clothing brand based in Phoenix, Arizona. The company was established in 2015 by a young entrepreneur, the CEO Marvis Carson, and our business has been growing rapidly in past few years. Our product collections include T-shirts, sweaters and cardigans. Our prices range between \$30 to \$60.

At Monic, we aim at becoming one of the top online organic fashion brands. We are committed to provide premium U.S.-made organic apparel for anyone in the world. We use 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, product finishing, packaging and storing is completed in U.S., where the workers are fairly paid and ensured a healthy and safe work environment.

Our core values are simple and consistent – quality, eco-friendly and ethical. We believe that our organic cotton products present high standard of quality to our customers. We strongly believe that everyone has a responsibility to contribute to a greener planet, and Monic achieves this by providing purely organic cotton products. We also believe that being ethical is the key to success of our business.



Quality

Eco-
friendly

Ethical

Message from the CEO

Dear friends,

2017 has been an important year for Monic, as we continued to grow our business in order to better satisfy the growing demand for high-quality organic clothing globally. The key factors leading to our sustained success are well reflected in our supply chain model – secured local source of raw organic cotton which meets the GOTS requirements and our team of talents with over ten years of on-hands experience in cotton apparel manufacturing. As we highly value the hard work of our people, we have always been committed to provide them with a safe workplace and competitive compensations. The combination of valuable resources and outstanding team of professionals enables our products to be created and delivered to customers in the most timely and cost-efficient manner.

Thanks to the team's dedication, we recorded a significant sales growth and doubled profits in the past year. As result of raw material unit cost reduction, rising demand and product price raise, Monic achieved a gross margin of 64.9% and an operating margin of 48.8% in 2017, increasing by 1.2% and 5.6% respectively compared to 2016.

In response to the increasing competition in the online organic clothing industry, we strive to continuously improve our product quality and offer the most affordable options to potential customers. As we did in 2017, we'll continue to focus on our core business of ethical organic cotton apparel and remain a low-cost leader within the industry. We also hope to receive ongoing support from our loyal customers and reach out to the bigger group of green product supporters and those who hold the same values as Monic by providing expanded collection of superior organic cotton products.

Looking forward, we believe our financial growth will continue in 2018 and we expect to achieve a better market position as organic clothing products become more prevalent.

Marvis Carson
CEO

Marvis Carson

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

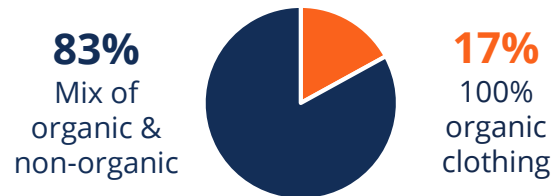
US\$1.25
per pound of organic cotton in 2016

VS

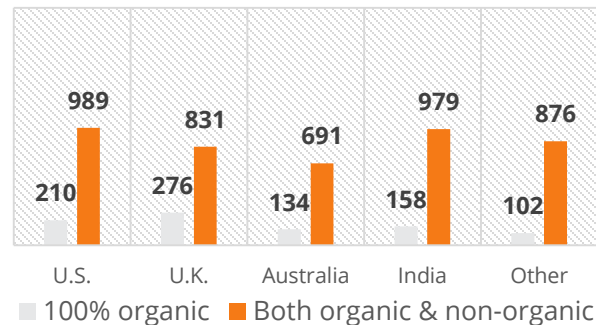
US\$1.04
per pound of organic cotton in 2017

Market Segmentation

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



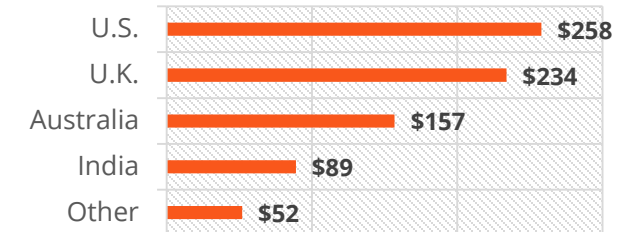
Number of online organic clothing stores in 2017



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

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

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

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

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%

Market research summary report

Our marketing team took the initiative to research on trends in the online organic clothing industry and conducted quarterly customer surveys to collect information about popularity of various organic cotton products available in the market. The summary of the industry research can be found on page 5 of this document.

We have seen a good opportunity in the organic clothing industry as there was a 15% sales growth in 2017 globally while U.S. was the top market amongst all countries (US\$258 million total sales). In response to the growing market size of the industry and increasing customer demand for 100% organic clothing, we plan 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. Monic's closer focus in these market segments will allow the company to produce superior clothing matched to the needs of these customers.

We have identified three most feasible options for product expansion: organic cotton pants, organic cotton beanies and organic cotton shoes. Our estimated retail price is \$55 for pants, \$30 for beanies, and \$75 for shoes. The estimated annual production capacity for the three products are 600, 520 and 300 respectively, while the expected units of sale are 550, 360, 320 respectively. The pants will be available in three sizes (small, medium, large); the beanies are one-sized; and the shoes will be available in sizes 5 to 10 (no half sizes). We have a marketing expense budget of \$1,000 for the new product line which will be launched in 2018. Below are the cost structures for each of the three product lines:

Estimated Costs	Pants	Beanies	Shoes
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
Inventory storage cost	\$560	\$180	\$600
Salaries and benefits	\$7,000	\$3,100	\$8,600
One-time capital expenditure	\$10,000	\$5,000	\$16,000

Our team also performed durability testing on the three products to assess how long-lasting they are, and we assigned scores on a scale of 5 based on the amount of surface abrasion, colorfastness, stain release and odor resistance. Out of the three products, shoes scored the highest (5/5), pants ranked second (4/5) and beanies ranked third (3.5/5). On the other hand, more advanced machines and equipment are required for the production of shoes compared to the other two options.

Decision scorecard

Monic uses the following scorecard to evaluate the attractiveness of a potential project:

		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