Business Management

Internal Assessment

Academic Year 2024

Research Question: Should Art Design Decor LLC improve their cash flow by strengthening its co-insurance system?

Key Concept: Change

Word Count: 1,712

Table Of Contents

Research Proposal (Rationale, Sources of data, Anticipated Difficulties & Potential Solutions, Action Solutions & Gantt Chart)

Rationale: Art Design Decor is a small, old interior design firm that is responsible for the design of several construction sites across Cairo, it is known for its unique design recommendations among its clients. I view the firm as motivational to myself as it is an example in my mind of how a company is supposed to run in the long-term. My father happens to have founded the company which acts as a part of my motivation in why I've chosen to analyze it. The main goal of this research paper is to evaluate whether or not a renewed co-insurance strategy would result in increased cash flow for the business.

Limitations: There are likely hidden point of views that I was not told about in the interview with the CEO and COO which might effect the outcome of this analysis.

Sources of data: The sources of data used in this research paper are combined with primary and secondary resources as will be displayed and mentioned concurrently.

Key areas of syllabus: Finance & Accounts and Operations Management

Tools: SWOT Analysis, FFA, Fishbone Diagram.

Primary Sources:

Interviews with the CEO and COO of Art Design Decor in order to provide insight into what their current co-insurance system is like, what problems it is causing, potential solutions and background information given on the topic from their respective points of views.

A survey to their management team (which consists of 4 members; CEO, COO, Head of operations, Head of Legal) asking whether or not they believe a strengthened co-insurance system would make their job easier and potentially fix the problems they're experiencing with cash-flow.

Secondary sources:

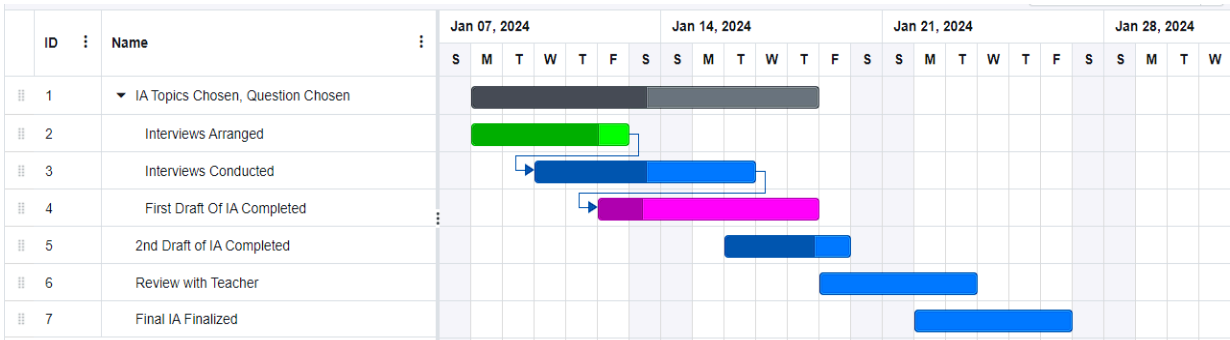
Academic Journals and business articles will be used as additional sources which should help pinpoint potential solutions and obstacles in strengthening ADD's cashflow.

Anticipated difficulties: While Art Design Decor (ADD) wishes to optimize and better its cash flow through a renewed co-insurance system, several roadblocks lie ahead of them. The primary hurdle lies in their existing relationships with current insurance providers, who aren't exactly known for embracing abrupt contractual shifts or proposals for any of their preexisting construction sites.

The insurance landscape in architecture is relatively rigid. Insurance companies are notoriously risk-averse, adhering to established protocols and meticulously assessing proposals before committing. ADD's desire for a swift co-insurance overhaul might not resonate with their providers, accustomed to a measured, step-by-step approach. Sudden changes, especially those impacting existing contracts or venturing into uncharted territory like new construction sites, could trigger hesitation and resistance not only from their insurance providers, but from their investors, financiers, and shareholders too. Building trust with insurance providers takes time and a proven track record. ADD's current co-insurance system might not yet inspire the level of confidence necessary for their providers to readily accept significant alterations. Demonstrating consistent profitability, transparent risk management practices, and a clear understanding of the proposed changes will be crucial in persuading them to come on board.

Potential Solutions: The reason contracts are difficult to manipulate is due to how existing contracts with their insurance providers may contain clauses restricting flexibility or imposing hefty penalties for early termination as is required for a new co-insurance term. Modifying these contracts to accommodate the new co-insurance system could involve complex negotiations and potentially incur significant financial costs The need to balance potential gains with these upfront expenses adds another layer of complexity to the decision-making process. Expanding co-insurance to new construction sites introduces a whole new set of uncertainties. Insurance providers will likely scrutinize the risk profiles of these sites, factoring in factors like project complexity, location-specific hazards, and the track record of contractors involved. Convincing them of the viability and profitability of insuring these projects will require meticulous data analysis, comprehensive risk assessments, and a compelling presentation of the potential rewards and future obstacles.

Action plan displayed in a Gantt Chart:



Word Count: 560

Executive Summary

ADD is currently facing cash flow issues which effects their ability to properly purchase the necessary items needed to build what their clients have requested of them. This is effecting their ability to pay employees on time due to how cashflow affects everything inside of a business. Keep in mind, ADD is not struggling with finances, they're finding it difficult to keep track of how to cover damages given limited coverage by their current co-insurance system. I propose that with the strengthening of their weak co-insurance system, they'd be able to possibly soften these problems by having better access to liquid cash in the scenario of any damage to any of their construction sites as is common in their industry. ADD has experienced 2 major construction site damages this year which costed them $110,000 USD of which wasn't covered by insurance leading to projects being delayed and subsequently ending in a loss. Strengthening their co-insurance system will lead to less of these sorts of problems, leading to easier financing inside of their future and existing projects. The company currently employs 51-200 employees according to their linkedin profile.

Word Count: 188

Introduction

Art Design Decor is a small, multinational interior design firm that has been operating since the year 1996 across multiple continents, with their main offices being located in Dubai, the United Arab Emirates, and Cairo, Egypt. They've operated on construction sites across Europe and the middle east.

The most notable projects they've worked on include government buildings in dubai, restaurants in dubai festival city, and company employee offices for medium-sized businesses in Sharjah, a city located next to Dubai. They operate as a B2B (business to business) firm that searches for clients on the daily. They've recently come across a cash liquidity problem that's been effecting their cash flow due to alot of it being locked out in intangibles such as costs of materials that're used for construction and design. Ofcourse, having liquidity issues and cashflow issues are completely different things. But for ADD, they are intersected with one another as both of those problems link directly to the other, therefor solving either one of those issues would solve the issue as a whole. Cashflow issues stem from their clients and co-insurance agreement, while liquidity issues stem from their employees, sites, and co-insurance agreement.

Therefor, fixing their co-insurance agreement or atleast tweaking it to an advantage would heavily benefit them as a company as it'd fix all of the biggest issues they currently face as a small company with 51-200 employees.

Machinery in the industry is not very liquid, especially when they're used on a daily basis, which is why by restructuring and renegotiating their co-insurance systems with their insurance providers, they'll be able to likely have less money locked up and more given to them by clients without much issue. From what was said by the COO, they are not willing to push hard in this direction as they value their business connections with this insurance provider and their clients as it is one of the most competitive offers they've ever gotten in over 12 years (1 co-insurance clause is used across all of their clientele-deals).

The insurance provider would likely still be risk averse when it comes up to changing their agreement to advantage ADD which is one of the many obstacles that are acting as blockades in the advancement of this idea - the fact that it'd disadvantage their insurance provider and put more risk on their behalf, while subsequently reducing the risk from ADDs side of things.

Main Results and Findings

Brief Explanation of their Co-insurance deal is as follows (what their current deal offers):

- All risks insurance
- Professional indemnity insurance
- Public liability insurance
- Workers' compensation insurance
- Decennial Liability insurance
- Delay in start–up insurance

Defining all of these is crucial in understand why these cause problems. The figures below display the respective definitions as sourced in resource [4] "Insurance in Construction Contracts: A Few Things to Know." *Al Tamimi & Company*, 11 Mar. 2020, www.tamimi.com/law-update-articles/insurance-in-construction-contracts-a-few-things-to-know/. Accessed 11 Jan. 2024.

- All risks insurance – This insures against physical damage to the works (and usually materials on site). All risks insurance typically covers the full reinstatement value of the works plus a mark up for any ancillary costs (such as consultancy and professional fees) that are incurred.

- Professional indemnity insurance – This insures contractors with design responsibility (i.e. under design and build contracts) against liability arising out of professional negligence and will respond if, for example, designs do not comply with the requirements of the underlying construction contract (although it is not uncommon for professional indemnity insurance to exclude cover for "fitness for purpose" warranties).

- Public liability insurance – This provides cover for liability arising out of death or personal injury to third parties (but not the contractor's employees, who should be covered by worker's compensation insurance) or damage to property belonging to third parties (but not the works, which is covered by the all risks insurance) prior to the works being taken over.
- Workers' compensation insurance – This insures the contractor against liability for the death or personal injury to its employees (usually on site) when performing the works.

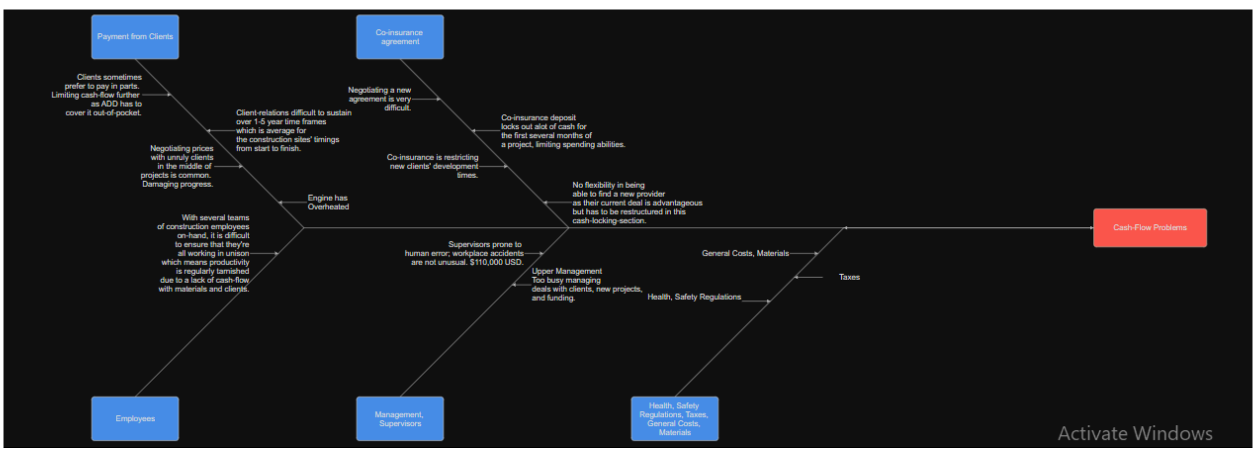
> - Decennial liability insurance – Under Articles 880 to 883 of the UAE Civil Code the contractor (and supervising architect) are jointly liable to the employer for a period of 10 years (from the date the works are taken over) for any defect that threatens the safety or stability of the building or if the building suffers a total or partial collapse. Decennial liability cannot be contractually excluded and contractors often take out insurance against this liability. Similar decennial liability regimes apply in most other Middle Eastern jurisdictions.
> - Delay in start-up insurance (DSU) – Unless the contractor is entitled to relief under the contract, contractors are customarily required to pay liquidated damages to the employer if the works are not taken over by the date for completion or, depending on the nature of the works, fail to satisfy specified output criteria.

As shown above, this is enough to cover everything that could possibly go wrong in one of ADDs' projects. ADD has never experienced issues in what the insurance actually covers, it's mostly experienced problems in the amount of money locked in the first several months of a project. This ends up forcing ADD to dig into personal finances of the board members such as the COO, CEO, and CFO. The CFO isn't sure on what to do or how to approach this problem, but he said they've got bigger problems and that this issue does not deserve the management teams' attention. They've been working fine with the current system in place so he sees no reason to introduce change. Surprisingly enough, all of the executives (besides the CFO) all have the shared belief that they'd love for this change to take place, but nobody is actively choosing to take action on it.

Since the executive team was unwilling to handover a comprehensive record of their financial performance, this analysis is limited to the information we did receive. Such as their revenue (which is 57,000,000 EGP Last fiscal year, 2023). We can tell, using their revenue and egypt's construction industry size that they control roughly 0.00282005954% of the egyptian construction industry market share. This proves their status as a small company. Their yearly revenue was roughly 1,847,139$ USD. Applying the standard profit margin according to their revenue, we can estimate that they've profited roughly $369,400 USD last year which is likely on the lower side of business income due to the fact that they're a small company. In previous years, ADD was making around 3,600,000 AED In the United Arab Emirates, back in 2017. This is equivalent to around $1,000,000 USD or 0.00001111111% of the UAEs construction industry at their peak before relocating their Headquarters to Cairo. Here, we can tell that the decision to move to Cairo was not a good one. This ofcourse varies since they might anticipate that they'd be able to garner more revenue in comparison to the UAE in 5 years from now which might've aided in their decision to move to Cairo. The only downside being that it had created a whole host of problems, most notably being their cashflow problems which is still mainly caused by the reasons aforementioned.

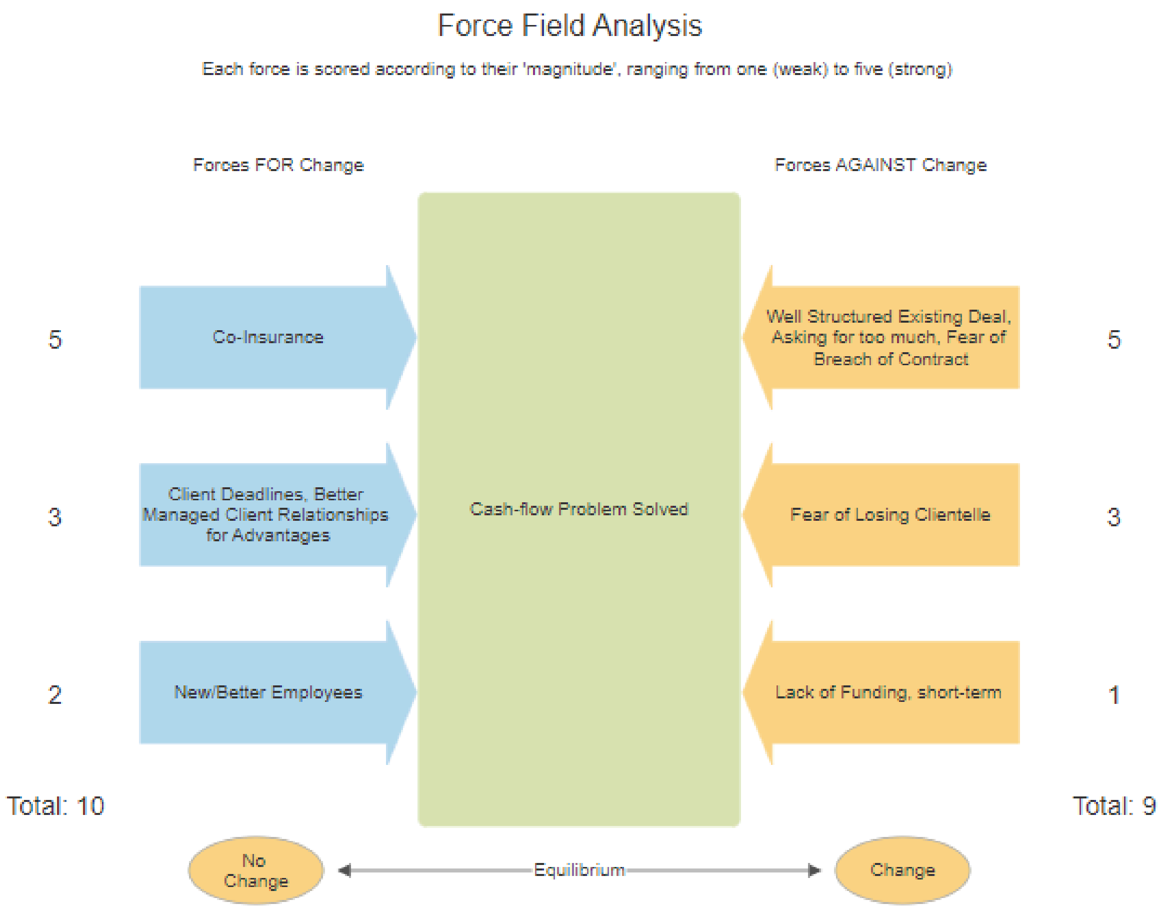
<u>Analysis and Discussion</u>

Fishbone Diagram



Since ADD is facing problems with cash-flow and sustainability, a fishbone diagram should aid in the identification of potential issues with their structured spending systems and cash distribution which should assist in convincing their insurers that they'll be safer in a better-suited co-insurance agreement. The fact that one agreement is causing this many problems hints at a lack of long-term thinking in the companies' management team. The CEO infact points this out as a "Missed Oppurtunity", a somewhat optimistic outlook to the situation considering the fact that they'd grown to see more problems arise out of this 1 problem. A lack of decisiveness had led to the cashflow problem as up to this day, no management member had contacted the insurance provider with their supposed concerns.

Field Analysis



If we take a look at the Force Field analysis above, co-insurance plays the most crucial role in the advancement of the cash-flow problems' solution. The fact that it plays a crucial role means that it'd have the most power in the fixing of this problem. The lack of motivation/and/or resistance to change in the executive management team is a main reason behind the current cash-flow problem.

Liquidity vs. Cash Flow: While liquidity and cash flow are distinct issues, they are interconnected for ADD. The liquidity problem, related to employees, sites, and the co-insurance agreement, affects cash flow. Addressing the co-insurance agreement could potentially release funds tied up in the early stages of projects, alleviating the liquidity issue and positively influencing cash flow.

Management Perspective: The executive team's reluctance to take decisive action and the CFO's perception that the issue is not critical highlight a lack of urgency in addressing the financial challenges. A more proactive approach, especially regarding the co-insurance agreement, could demonstrate a commitment to long-term financial stability.

Market Position: ADD's market share in the Egyptian construction industry is relatively small, indicating its status as a small company. The decision to relocate headquarters to Cairo has raised questions about its overall impact on the company's financial health. Revisiting the co-insurance system might be crucial in mitigating the adverse effects of the relocation.

Limitations and Difficulties

Using tools like fishbone diagrams and force field analysis is helpful but has downsides. Relying on limited data makes these challenges more pronounced,especially considering how ADDs' management were reluctant to hand out information. Fishbone diagrams, made for brainstorming and visualization, might make complex issues too simple, lacking the depth needed for a full analysis. The subjective nature of interpreting causes introduces biases, as people might prioritize causes differently. Also, the lack of clear numbers in fishbone diagrams makes it hard to prioritize and solve critical issues. Force field analysis, while useful, has its own limits. The subjective assessment of forces for and against a situation can vary, and assuming static forces may not catch the dynamic nature of factors and how they change over time. The absence of clear numbers in force field analysis makes it hard to compare forces and fully assess their impact.

Limited data means not fully understanding the research problem and possibly missing important variables. Conclusions from a small dataset might not apply to a larger group, hurting the external validity of the research findings. The increased chance of error in statistical analyses from limited data weakens the reliability and strength of the research. Researchers need to be aware of biases and assumptions when using these tools, making sure these don't affect the outcomes. The tools' relevance in a particular context is crucial, and using them in the wrong way might give less meaningful results. In conclusion, while fishbone diagrams and force field analysis offer good insights, carefully managing their limits is crucial. Using a broad research approach with different methods and considering the situation is essential to improve the credibility and usefulness of research findings. Researchers need to aim for clear analyses, recognize how factors change in complex systems, and be watchful for biases to produce strong and reliable research results.

<u>Conclusion</u>

According to the explanation above, it is reasonable for us to assume that ADD’s problems could hypothetically be solved by fixing its co-insurance plan and thereby fixing its material and employee problems that’re caused by the lack of cash flow in the first place. As covered throughout the majority of this Research paper, it is concluded that ADDs management is the main obstacle in the proceedings of these possible solutions due to their beliefs and resistances against ‘unneccessary’ change.

In conclusion, fixing ADD's co-insurance system has the potential to address both liquidity and cash flow problems. By renegotiating the agreement to unlock funds tied up in the initial stages of projects, the company could improve its financial flexibility. However, the success of this strategy depends on effective communication with the insurance provider, strategic decision-making, and a proactive approach from the executive team. The analysis suggests that addressing the co-insurance issue is a key step towards resolving ADD's financial challenges.

Resources

To be inserted…