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THE CHINESE GAZETTE

Raza Khan wrote this case under the supervision of Professor Julie Gosse solely to provide material for class discussion. The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The authors may have disguised certain names and other identifying information to protect confidentiality.

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In December 2016, Aroma Adeel, manager of Commercial Banking at International Bank of Business (IBoB) was reviewing her notes after speaking with Josh Li, owner, founder, and president of The Chinese Gazette (TCG). Li’s organization published newspapers that were targeted toward the Chinese community in Toronto, Canada. Li was requesting a long-term loan of CA$100,000[[1]](#footnote-1) so his company could fund a salary for a new, full-time journalist. Adeel knew this loan would be the first long-term loan to TCG in over 15 years. Scrutiny from her superiors would be high, so she had to make the appropriate recommendations for IBoB.

TORONTO, ONTARIO[[2]](#footnote-2)

With a population of 2.8 million, Toronto was the largest city in Canada and was well known as the country’s centre for financial services. However, with nearly 90,000 businesses in Toronto that provided jobs for over 1.4 million people, Toronto was also a technological, tourism, and media hub for all of Canada. Toronto was home to nine post-secondary institutions, including five universities and four colleges, and was considered one of the top 10 most liveable cities in the world. Toronto and the Greater Toronto Area were also known worldwide for their multiculturalism and diversity. Almost half the city’s population included residents who self-identified as visible minorities and approximately 50 per cent of Toronto’s population originated from a foreign country. People came to Toronto for many reasons, including access to jobs, education, and the lifestyle the city provided. In particular, Toronto was a preferred destination for Chinese immigrants. The Chinese community comprised over 12 per cent of the city’s population and represented the second largest ethnic group.

THE CANADIAN NEWSPAPER PUBLISHING INDUSTRY[[3]](#footnote-3)

The Canadian newspaper publishing industry was made up of large, national companies that owned local and national brands, and small community print newspapers that operated in niche markets. Canadian newspaper publishers differed by type of reported news and frequency of published papers. In addition to print, online content was a differentiator, and publishers provided access to this content in different ways. Some offered free online availability; others required subscriptions. The industry produced $3.6 billion in sales in 2016 with an average profit margin of 10 per cent and had over 28,000 employees nationwide, including publishers, editors, and journalists.

Canadians read news for two main reasons: to stay informed and reading for leisure. Although the number of Canadians who read newspapers was difficult to track, the circulation of printed papers decreased from 35.6 million to 30.4 million between 2011 and 2015. The industry was struggling and expected to decline in revenue by a yearly average of 4.4 per cent between 2016 and 2021. Increasing online readership was the biggest driver of these trends. Newspaper publishers were now making approximately $15 less for every traditional print advertisement they replaced with an online advertisement.

The news industry in general was also extremely competitive and had seen tremendous proliferation in content media, such as blogs, YouTube channels, podcasts, and other social media platforms that were replacing traditional outlets as sources for news. Moreover, the trend toward online consumption lowered barriers to entry and caused the industry to become even more competitive, resulting in the onset of new foreign competition to the Canadian market. In order to remain competitive in this challenging environment, publishers had to cultivate a credible brand and attract good journalists who were capable of delivering high-quality material.

THE CHINESE GAZETTE

History

Li immigrated to Toronto from China with his wife, Nancy, in 1989 and started a newspaper in 1992. Although Li had no previous business, publishing, or writing experience, he believed his passion for current affairs and his sense of civic duty to make wrongdoers accountable would help him succeed as a publisher. Li was forced to shut down his business in 1994 after being unable to produce profits. He took this time to read, meditate, and reflect on what he had learned from this failure.

Two years later, Li gave the newspaper business another try. With no employees, Nancy and Li did all the writing, publishing, and marketing of the newspaper. Revenues grew every year until the global recession of 2008, when TCG once again was on the brink of bankruptcy. However, Li’s financial savvy carried TCG through these tough economic times and revenues eventually returned to pre-recession levels.

TCG became a leading newspaper for Toronto’s Chinese readers. The company was the third largest Chinese newspaper in Toronto with a weekly circulation of 26,000 newspapers. Although Li was content with the business and proud that it had supported his wife and two children, he believed he could make the newspaper even more successful. At 55 years of age, Li wanted to improve the business so that one day his children would have the opportunity to take it over and provide for their own families.

Operations

TCG’s headquarters were located in Scarborough, a sub-riding within Toronto. The company acquired six employees who were dispersed across sales, writing and editing, graphic design, and distribution. Li and his wife managed the business together and split the functional workload. Li oversaw sales. Nancy was the paper’s editor. Twenty per cent of TCG’s news was on China, 50 per cent on local news, 20 per cent on editorial columns, and 10 per cent on investigative journalism. The newspaper was published three times a week and distributed at Chinese grocery stores throughout Toronto, free of charge. TCG also maintained a website and a social media account on the popular Chinese platform, WeChat.[[4]](#footnote-4) Readers could access TCG’s articles through both online sources. The company earned revenues primarily by charging businesses for advertisements, but Li found that classified ads were also a strong source of cash for the business.

Competition

Li considered the publications *51.Canada* and *YorkBBS* to be TCG’s main competitors. He believed both organizations attracted a growing reader base because they responded quickly to customers’ changing tastes for online content. While TCG remained focused on print newspapers, *51.Canada* and *YorkBBS* won market share as the first Chinese publishers to provide online news in the Toronto market. However, neither competitor offered English translations of their Chinese-language articles, which Li believed was a key differentiator. Providing articles in two languages—English and Mandarin—allowed TCG to give newly immigrated families the comfort of their native language, while practising reading and understanding English.

THE PROPOSED EXPANSION

Li also believed his newspaper was different from competitors because he encouraged TCG journalists to write about controversial topics and use their platform to hold public figures accountable, which was a journalistic value that he felt other newspapers did not uphold. He told Adeel, “I am constantly on the side of my readers. I have a passion for delivery and want them to know the truth.”

With sales in 2016 of almost $500,000 and strong cash reserves, Li’s business was running well, but he wanted to increase readership. He felt that several controversial topics went unreported; because he was occupied with operating the business, he was unable to write about them himself. Li planned to expand by hiring a young, ambitious journalist with a desire to change the status quo, a willingness to ask hard questions, and the drive to uncover the truth. A fresh journalist on the writing team with a mandate to exclusively report controversial topics could further differentiate TCG from competitors and ultimately attract more readers.

With his daughter in university and his son working full time, Li felt that their independence gave him freedom to take on more financial risk to support his goals for TCG. Bank funding would allow Li to continue growing the business and pursue his initial vision of TCG as a trustworthy, investigative newspaper for the Chinese community. Li also wanted to move away from daily operations by starting and hosting a YouTube extension of the newspaper. He was well respected in the Chinese community and was regularly asked to be a guest speaker on local television news stations. However, because of the operational demands of the paper, he had to turn down these invitations. With a bank loan to fund a new journalist, Li would have time to accept and attend these media appearances.

Historically, Li preferred to fund operations with cash generated from the business and personal savings. After a bad experience with a bank when he first started up, Li pledged to finance as much of the newspaper as possible with non-bank sources. He eventually took out a mortgage through a bank to fund the purchase of company headquarters but paid it off soon after. Although Li preferred to finance assets with in-house sources, he recognized that in order to expand, he would again need the bank’s help and was willing to take on debt.

Li expected that it would take three months to find a suitable journalist upon approval of the loan. Although he was unsure exactly how much the journalist would increase TCG’s revenues, Li estimated that annual sales would increase by 5 per cent (conservatively) to 15 per cent (optimistically). In line with industry trends, Li believed that business was moving toward more online publication and expected gross margins to increase to 41 per cent of revenues the next year. He credited this subsequent decrease in cost of goods to reduced variable costs associated with online distribution, which was typically less capital-intensive than publishing print newspapers. Li also anticipated delivery and freight to decrease to 3.5 per cent of revenues and utilities to decrease to 0.35 per cent of revenues because of reduced printing and distribution activities. He also expected professional fees to increase by 0.17 per cent of revenue to help make the online publication more reader-friendly and visually appealing. Li wanted to drive growth in readership; therefore, he expected to increase the advertising and promotion budget to 0.25 per cent of revenue. If approved, the $100,000 loan would be paid back over six years, with annual principal payments and interest charges of prime plus 2 per cent.[[5]](#footnote-5) Li planned to use the entire $100,000 over the next two years to fund the new journalist’s salary, with a planned annualized rate of $47,500 for the first year (see Exhibits 1 to 5).

Decision

Although Adeel had met Li only a few times, she could tell he was a passionate and charismatic business owner, who needed IBoB’s funding support to realize his company’s vision and expansion plans. However, she was still concerned about the risks associated with issuing a loan to a company that was in a struggling industry. She also worried about conducting business with a client that had no prior relationship with the bank. Did this $100,000 loan request deserve to be approved? Adeel settled in to review TCG’s file.

**EXHIBIT 1: STATEMENT OF EARNINGS (UNAUDITED) for the years 2014–2016,   
ending December 31 (in CA$)**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2016** | **2015** | **2014** |
|  |  |  |  |
| **Revenue** | $ 478,284 | $ 483,235 | $ 505,449 |
| Less: Cost of goods sold | 289,204 | 294,755 | 318,342 |
|  |  |  |  |
| **Gross profit** | 189,080 | 188,480 | 187,107 |
|  |  |  |  |
| **Operating expenses** |  |  |  |
| Salaries and wages | 36,614 | 39,283 | 56,972 |
| Delivery and freight | 19,461 | 20,873 | 13,132 |
| Subcontract | 17,074 | 20,853 | 42,714 |
| Vehicle | 17,274 | 15,317 | 16,122 |
| Supplies | — | 13,224 | 8,590 |
| Depreciation | 12,435 | 9,813 | 12,794 |
| Occupancy | 11,399 | 9,500 | 10,303 |
| Telecommunications | 7,612 | 7,641 | 5,879 |
| Meals and entertainment | 7,050 | 6,885 | 7,976 |
| Utilities | 2,108 | 6,046 | 5,767 |
| Travel | 6,231 | 4,976 | 3,268 |
| Office and general | 2,500 | 3,235 | 3,102 |
| Professional fees | 1,300 | 1,300 | 1,950 |
| Repairs and maintenance | 478 | 1,184 | 3,259 |
| Interest expense | 721 | 1,038 | 1,389 |
| Insurance | 927 | 956 | 931 |
| Advertising and promotion | 842 | 249 | 8,886 |
|  |  |  |  |
| **Total operating expenses** | 144,026 | 162,373 | 203,034 |
|  |  |  |  |
| Net earnings (loss) before tax | 45,054 | 26,107 | (15,927) |
| Less: Income tax | 10,691 | 4,421 | 0 |
|  |  |  |  |
| **Net income after taxes** | $ 34,363 | $ 21,686 | $ (15,927) |
|  |  |  |  |

Source: Company files.

**EXHIBIT 2: STATEMENT OF RETAINED EARNINGS (UNAUDITED) for the years 2014–2016, ending December 31 (in CA$)**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2016** | **2015** | **2014** |
|  |  |  |  |
| Beginning retained earnings | $ 441,049 | $ 419,363 | $ 435,290 |
| Add: Net income | 34,363 | 21,686 | (15,927) |
| Less: Dividends | 0 | 0 | 0 |
|  |  |  |  |
| Ending retained earnings | $ 475,412 | $ 441,049 | $ 419,363 |
|  |  |  |  |

Source: Company files.

**EXHIBIT 3: BALANCE SHEETS (UNAUDITED) as at December 31 (In Ca$)**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2016** | **2015** | **2014** |
| **ASSETS** |  |  |  |
| Current assets |  |  |  |
| Cash | $ 110,985 | $ 15,293 | $ 41,654 |
| Short-term investments | 703,723 | 695,736 | 470,835 |
| Due from government agencies | 0 | 0 | 7,412 |
| Income tax recoverable | 0 | 3,349 | 0 |
| Prepaid expenses | 500 | 500 | 0 |
| **Total current assets** | 815,208 | 714,878 | 519,901 |
|  |  |  |  |
| Fixed assets |  |  |  |
| Long-term investments | 32,279 | 32,279 | 32,279 |
| Property, plant, and equipment | 185,378 | 155,153 | 150,000 |
| Less: Accumulated depreciation | 139,135 | 126,700 | 116,887 |
| Property, plant, and equipment, net | 46,243 | 28,453 | 33,113 |
|  |  |  |  |
| Total fixed assets, net | 78,522 | 60,732 | 65,392 |
|  |  |  |  |
| **Total assets** | $ 893,730 | $ 775,610 | $ 585,293 |
|  |  |  |  |
| **LIABILITIES** |  |  |  |
| Current liabilities |  |  |  |
| Accounts payable & accrued liabilities | $ 46,967 | $ 38,976 | $ 54,379 |
| Due to government agencies | 19,055 | 10,932 | 0 |
| Income tax payable | 7,404 | 0 | 3,893 |
| **Total current liabilities** | 73,426 | 49,908 | 58,272 |
|  |  |  |  |
| Long-term liabilities |  |  |  |
| Due to shareholder | 329,055 | 268,816 | 91,821 |
|  |  |  |  |
| **EQUITY** |  |  |  |
| Share capital | 15,837 | 15,837 | 15,837 |
| Retained earnings | 475,412 | 441,049 | 419,363 |
| **Total equity** | 491,249 | 456,886 | 435,200 |
|  |  |  |  |
| **TOTAL LIABILITIES AND EQUITY** | $ 893,730 | $ 775,610 | $ 585,293 |
|  |  |  |  |

Source: Company files.

**EXHIBIT 4: FINANCIAL RATIOS (IN CA$)**

|  |  |  |  |
| --- | --- | --- | --- |
|  | **2016** | **2015** | **2014** |
| **PROFITABILITY** | % | % | % |
| Revenue | 100.00 | 100.00 | 100.00 |
| Less: Cost of goods sold | 60.47 | 61.00 | 62.98 |
| Gross profit | 39.53 | 39.00 | 37.02 |
|  |  |  |  |
| **Operating expenses** |  |  |  |
| Salaries and wages | 7.66 | 8.13 | 11.27 |
| Delivery and freight | 4.07 | 4.32 | 2.60 |
| Subcontract | 3.57 | 4.32 | 8.45 |
| Vehicle | 3.61 | 3.17 | 3.19 |
| Supplies | 0.00 | 2.74 | 1.70 |
| Depreciation | 2.60 | 2.03 | 2.53 |
| Occupancy | 2.38 | 1.97 | 2.04 |
| Telecommunications | 1.59 | 1.58 | 1.16 |
| Meals and entertainment | 1.47 | 1.42 | 1.58 |
| Utilities | 0.44 | 1.25 | 1.14 |
| Travel | 1.30 | 1.03 | 0.65 |
| Office and general | 0.52 | 0.67 | 0.61 |
| Professional fees | 0.27 | 0.27 | 0.39 |
| Repairs and maintenance | 0.10 | 0.25 | 0.64 |
| Expense interest | 0.15 | 0.21 | 0.27 |
| Insurance | 0.19 | 0.20 | 0.18 |
| Advertising and promotion | 0.18 | 0.05 | 1.76 |
| Total operating expenses | 30.11 | 33.60 | 40.17 |
|  |  |  |  |
| Net earnings (loss) before tax | 9.42 | 5.40 | –3.15 |
| Less: Income tax | 2.24 | 0.91 | 0.00 |
| **Net income after taxes** | 7.18 | 4.49 | –3.15 |
|  |  |  |  |
| Return on average equity | 7.25 | 4.86 | n/a |

|  |  |  |  |
| --- | --- | --- | --- |
| **LIQUIDITY** |  |  |  |
| Current ratio | 11.10:1 | 14.32:1 | 8.92:1 |
| Acid test | 11.10:1 | 14.25:1 | 8.79:1 |
| Working capital | $ 741,782 | $ 664,970 | $ 461,629 |
|  |  |  |  |
| **EFFICIENCY** |  |  |  |
| Age of payables | 59 days | 48 days | 62 days |
|  |  |  |  |
| **STABILITY** |  |  |  |
| Net worth to total assets (%) | 55 | 59 | 74 |
| Interest coverage | 63.49 x | 26.15 x | n/a |

|  |  |  |
| --- | --- | --- |
|  | **2015–2016** | **2014–2015** |
| **GROWTH** | % | % |
| Sales | –1.0 | –4.4 |
| Net income | 58.5 | –236.2 |
| Total assets | 15.2 | 32.5 |
| Equity | 7.5 | 5.0 |

Source: Company files.

**EXHIBIT 5: STATEMENT OF CASH FLOWS (for the years ending December 31) (IN cA$)**

|  |  |  |
| --- | --- | --- |
|  | **2016** | **2015** |
| **OPERATIONS** |  |  |
| Net income | $ 34,363 | $ 21,686 |
|  |  |  |
| Adjustments to cash basis |  |  |
| Depreciation | 12,435 | 9,813 |
| Due from government agencies | – | 7,412 |
| Prepaid expenses | – | (500) |
| Income tax recoverable | 3,349 | (3,349) |
| Income tax payable | 7,404 | (3,893) |
| Accounts payable and accrued liabilities | 7,991 | (15,403) |
| Due to government agencies | 8,123 | 10,932 |
|  |  |  |
| Net cash flow from operations | 73,665 | 26,698 |
|  |  |  |
| **FINANCING ACTIVITIES** |  |  |
| Due to shareholder | 60,239 | 176,995 |
|  |  |  |
| Net cash flow from financing activities | 60,239 | 176,995 |
|  |  |  |
| **INVESTING ACTIVITIES** |  |  |
| Property, plant, and equipment | (30,225) | (5,153) |
| Short-term investments | (7,987) | (224,901) |
|  |  |  |
| Net cash flow from investing activities | (38,212) | (230,054) |
|  |  |  |
| Net cash flow | 95,692 | (26,361) |
| Beginning cash | 15,293 | 41,654 |
| Ending cash | $ 110,985 | $ 15,293 |
|  |  |  |

Source: Company files.

1. All currency amounts are in CA$ unless otherwise specified. [↑](#footnote-ref-1)
2. “Labour Force Characteristics, Seasonally Adjusted, by Province (Monthly) (Quebec, Ontario, Manitoba),” Government of Canada: Statistics Canada, April 6, 2018, accessed June 14, 2018, www.statcan.gc.ca/tables-tableaux/sum-som/l01/cst01/lfss01b-eng.htm; “Tourism,” Toronto, accessed June 14, 2018, https://www.toronto.ca/business-economy/industry-sector-support/tourism/; “World Rankings for Toronto,” Toronto, accessed June 14, 2018, https://www.toronto.ca/city-government/data-research-maps/toronto-progress-portal/world-rankings-for-toronto/; “NHS Profile, Toronto, C, Ontario, 2011: NHS Data,” Statistics Canada, November 27, 2015, accessed July 10, 2017, www12.statcan.gc.ca/nhs-enm/2011/dp-pd/prof/details/page.cfm?Lang=E&Geo1=CSD&Code1=3520005&Data=Count&SearchText=Toronto&SearchType=Begins&SearchPR=01&A1=Ethnic%20origin&B1=All&Custom=&TABID=1. [↑](#footnote-ref-2)
3. Steve Ladurantaye, “Five Things about the Canadian Newspaper Industry,” The Globe and Mail: Media, updated March 26, 2017, accessed https://www.theglobeandmail.com/report-on-business/five-things-about-the-canadian-newspaper-industry/article11121196/; “Newspaper Publishing—Canada Market Research Report,” IBISWorld: Where Knowledge Is Power, December 2017, accessed July 10, 2017, https://www.ibisworld.ca/industry-trends/market-research-reports/information/newspaper-publishing.html. [↑](#footnote-ref-3)
4. WeChat was a Chinese mobile application that consisted of a messenger, marketplace, and other social media products. The purpose of WeChat was to aggregate all major social media platforms and provide them in one mobile application. [↑](#footnote-ref-4)
5. Prime was 2.7 per cent. Interest would be charged on the original $100,000 loan balance. [↑](#footnote-ref-5)