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JOURNAL OF THE INTERNATIONAL ACADEMY FOR CASE STUDIES

INSTRUCTORS' NOTES

Editors
Inge Nickerson, Barry University
Charles Rarick, Purdue University, Calumet

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JOURNAL OF THE INTERNATIONAL ACADEMY FOR CASE STUDIES

CONTENTS

LETTER FROM THE EDITORS

Welcome to the *Journal of the International Academy for Case Studies.* The editorial content of this journal is under the control of the Allied Academies, Inc., a non profit association of scholars whose purpose is to encourage and support the advancement and exchange of knowledge, understanding and teaching throughout the world. The purpose of the *JIACS* is to encourage the development and use of cases and the case method of teaching throughout higher education. Its editorial mission is to publish cases in a wide variety of disciplines which are of educational, pedagogic, and practical value to educators.

The cases contained in this volume have been double blind refereed, and each was required to have a complete teaching note before consideration. The acceptance rate for manuscripts in this issue, 25%, conforms to our editorial policies. The Instructor's Note for each case in this volume will be published in a separate issue of the *JIACS.*

If any reader is interested in obtaining a case, an instructor's note, permission to publish, or any other information about a case, the reader must correspond directly with the author(s) of the case.

We intend to foster a supportive, mentoring effort on the part of the referees which will result in encouraging and supporting writers. We welcome different viewpoints because in differences we find learning; in differences we develop understanding; in differences we gain knowledge and in differences we develop the discipline into a more comprehensive, less esoteric, and dynamic metier.

The Editorial Policy, background and history of the organization, and calls for conferences are published on our web site. In addition, we keep the web site updated with the latest activities of the organization. Please visit our site and know that we welcome hearing from you at any time.

Inge Nickerson, Barry University
Charles Rarick, Purdue University, Calumet

NOTES

PAROUT'S "BONE MARROW DRIVE" PROJECT MANAGEMENT

Sunaina Chugani, University of Texas at Austin
Joo Y. Jung, University of Texas-Pan American

CASE DESCRIPTION

The primary subject matter of this case is project scheduling and resource loading. Secondary issues examined include strategy and human resource management. This case study is appropriate for upper level undergraduate students and MBA students taking operations management related courses. The case is designed to be used in conjunction with two to three hours of in-class discussion followed by approximately three to four hours of outside classroom analysis and report writing. In class discussion topics may include project scheduling based on critical path method, resource loading using spread sheet and leadership issues.

CASE SYNOPSIS

Parout Stores, a chain of super centers known as one of the largest retailers in the nation, was struggling with its public image after bad press on its now improved labor practices. The national office instructed local branches to begin conspicuous local community service initiatives to help the company in rebuilding its reputation at the community level. Robert McClelland, the manager of a Parout branch in a small Texas border town with a largely Hispanic population, stumbled across an opportunity to serve the Hispanic community nation-wide. The idea evolved from a brief conversation between McClelland and the founder of MatchJulia.org, a non-profit organization dedicated to registering more minorities on the National Marrow Donor Registry so that minority cancer patients have a better chance of finding a match for marrow transplants. Villanueva, the founder of MatchJulia.org, was willing to fly to the community and publicly thank any organization that recruits over 1,000 donors. One major problem was that Villanueva was scheduled to travel abroad within four weeks. Hence, McClelland only had a month to achieve this feat. He needed to strategically plan a community outreach program to register 1,000 donors in less than a month as well as convince his team that this opportunity was worth all the extra hours needed to plan and execute this project on such short notice.

INSTRUCTORS' NOTES

Qualitative Aspects

Although the emphasis of this case study is largely on quantitative analysis, discussions on a qualitative side can benefit the students. Several different human resource management and strategic issues can be discussed in class in order to guide students in answering problem numbers 1, 7, and 8.

1) Gaining Acceptance from Stakeholders

Gaining the buy-in from various stakeholders will not be an easy task. Both in-house employees and community volunteers need to be approached with clear explanations of the project's goals. The importance of communicating and thus sharing the same project goal should be emphasized to students. Students should discuss methods of selling the project to stakeholders (for example, possible tactics may include using incentives and/or affective and motivational appeals),

7) Potential Problems

This project has very tight schedule and any slippage in schedule can delay the project completion. Class discussion can involve students about how to minimize the likelihood of delays. The importance of careful planning should be discussed. Signing up and keeping key players, especially the medical technicians, can pose a major challenge. How McClelland will persuade, lead and motivate all participants throughout the project should be discussed.

8) Creating Permanent Change

It should be debated whether this project is a permanent solution to the existing company image problem or the mere beginning of a longer process. Clearly, this project alone would not fix the damaged image. However, this project can be a good starting point for future projects to be built on for turning around the poor image.

Quantitative Aspects

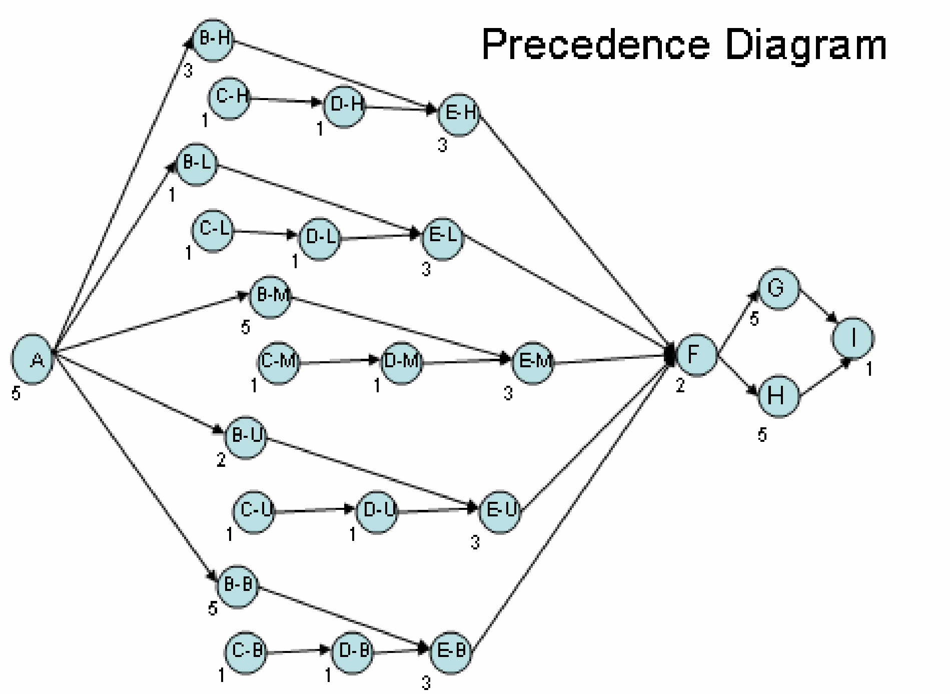
There are two spreadsheet files included with this case. The first spreadsheet, named "Parout Charts," is the file of charts that the instructor may present or withhold from students according to the level of difficulty desired. For example, for a more advanced class, the instructor may withhold all the charts in the file and require that the students come up with the precedence diagram and various matrices on their own. For a less advanced course, the instructor may choose to provide the students with the precedence diagram and require the students to produce the matrices on their own. For a more basic class, the instructor may even present the students with all the charts in the spreadsheet file to serve as a guide for the delaying and splitting activities and the subsequent charts.

The second spreadsheet, named "Parout Solutions" contains the solution that was developed by the authors of this case. This is just one way of leveling the resources and students will be allowed to develop their own unique solutions. The authors chose to utilize only delay/accelerate techniques, but students may also choose to split activities. Again, it is up to the instructor to set the difficulty level. In the solution provided, medical technician labor requirements vary between two and four medical technicians a day, with the gap on days 18 and 19 being unavoidable since no medical technicians are needed during the sorting activity. Employee labor requirements vary between two and seven employees a day, and PR personnel labor requirements vary between .25 and 3 PR personnel a day (again, with the gap on days 18 and 19 being unavoidable). The instructor can set more strict or more lax standards for the amount of variance, and can even shorten the amount of time Parout has to complete the whole project. In this way, the instructor can increase or decrease the level of difficulty to adjust to the students' capabilities.

CHARTS

PROJECT DURATION DETAILS			
Activity		**Predecessors**	**Duration (Days)**
A	Work with Cancer Societies to find local face for advertising	-	5
Highland Mall			
B-H	Advertise (Direct Marketing)	A	3
C-H	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-H	Train the people who will hold the drive.	C-H	1
E-H	Hold the drive and send the forms and cheek swabs to central location	B-H, D-H	3
Library			
B-L	Advertise (Direct Marketing)	A	1
C-L	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-L	Train the people who will hold the drive.	-	1
E-L	Hold the drive and send the forms and cheek swabs to central location	B-L, D-L	3
Medical Center			
B-M	Advertise (Direct Marketing)	A	5
C-M	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-M	Train the people who will hold the drive.	-	1
E-M	Hold the drive and sends the forms and cheek swabs to central location	B-M, D-M	3

PROJECT DURATION DETAILS			
Activity		Predecessors	Duration (Days)
University			
B-U	Advertise (Direct Marketing)	A	2
C-U	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-U	Train the people who will hold the drive.	-	1
E-U	Hold the drive and send the forms and cheek swabs to central location	B-U, D-U	3
Business District			
B-B	Advertise (Direct Marketing)	A	5
C-B	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-B	Train the people who will hold the drive.	-	1
E-B	Hold the drive and send the forms and cheek swabs to central location	B-B, D-B	3
F	Central Location sorts and ships forms and cheek swabs to lab	E-H, E-L, E-M, E-U, E-B	2
G	Takes 5 days to reach lab	F	5
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	F	5
I	Public Thank You Event	G, H	1



Labor Requirements (Worker-Days)					
Activity		Medical Tech.	Employees	Public Relations	Materials and Direct
A	Work with Cancer Societies to find local face for advertising	10	5	1	$0
B-H	Advertise (Direct Marketing)	3	3	3	$200
C-H	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-H	Train the people who will hold the drive.	1	2	0	$0
E-H	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-L	Advertise (Direct Marketing)	1	1	1	$50
C-L	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-L	Train the people who will hold the drive.	1	2	0	$0
E-L	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-M	Advertise (Direct Marketing)	5	5	5	$250
C-M	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-M	Train the people who will hold the drive.	1	2	0	$0
E-M	Hold the drive and sends the forms and cheek swabs to central location	6	9	3	$20
B-U	Advertise (Direct Marketing)	2	2	2	$80
C-U	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-U	Train the people who will hold the drive.	1	2	0	$0
E-U	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-B	Advertise (Direct Marketing)	5	5	5	$250
C-B	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-B	Train the people who will hold the drive.	1	2	0	$0
E-B	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
F	Central Location sorts and ships forms and cheek swabs to lab	0	8	0	$70
G	Takes 5 days to reach lab	0	0	0	$0
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	10	10	10	$0
I	Public Thank You Event	2	2	2	$0

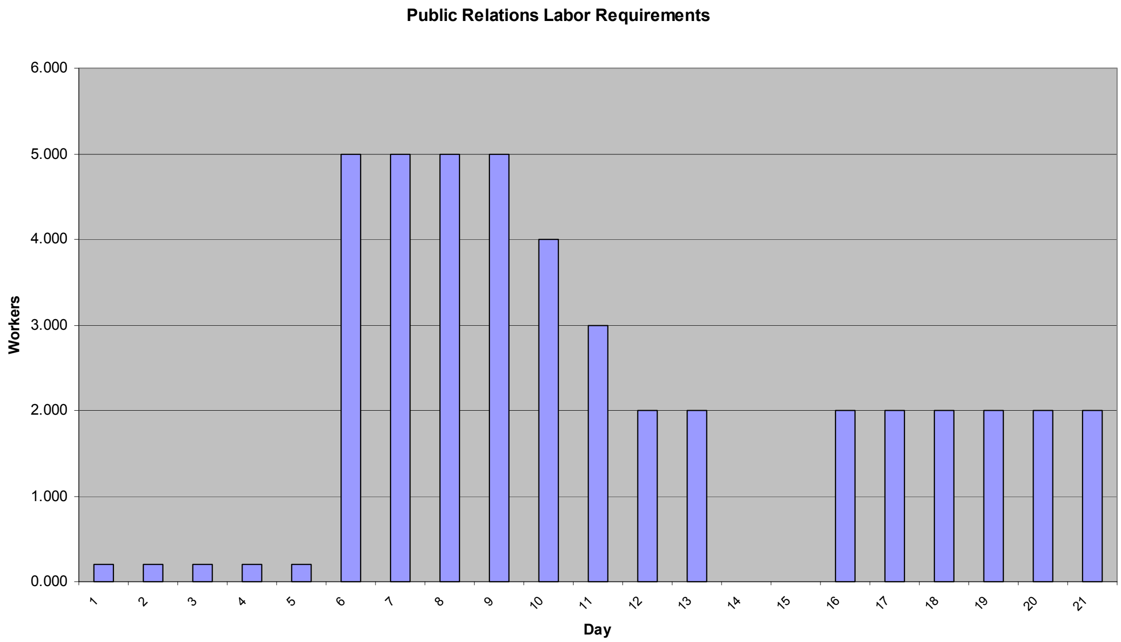
Original, Early-Start Schedule Matrix																									
	ACTIVITY																								
		Highland Mall				Library				Medical Center				University				Business Dist.				POST DRIVE			
	A	**b-h**	**c-h**	**d-h**	**e-h**	**b-l**	**c-l**	**d-l**	**e-l**	**b-m**	**c-m**	**d-m**	**e-m**	**b-u**	**c-u**	**d-u**	**e-u**	**b-b**	**c-b**	**d-b**	**e-b**	**f**	**g**	**h**	**i**
1	1	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	0	0	0
2	1	0	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	0	0
3	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
4	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
5	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
6	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	1	0	0	0	0	0	0	0
7	0	1	0	0	0	0	0	0	1	1	0	0	0	1	0	0	0	1	0	0	0	0	0	0	0
8	0	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0
9	0	0	0	0	1	0	0	0	1	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0
10	0	0	0	0	1	0	0	0	0	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0
11	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
12	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
13	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
14	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
15	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
16	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
17	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
18	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
19	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
20	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
21	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1
22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
23	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
24	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
25	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
26	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
27	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
28	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
29	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
30	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0

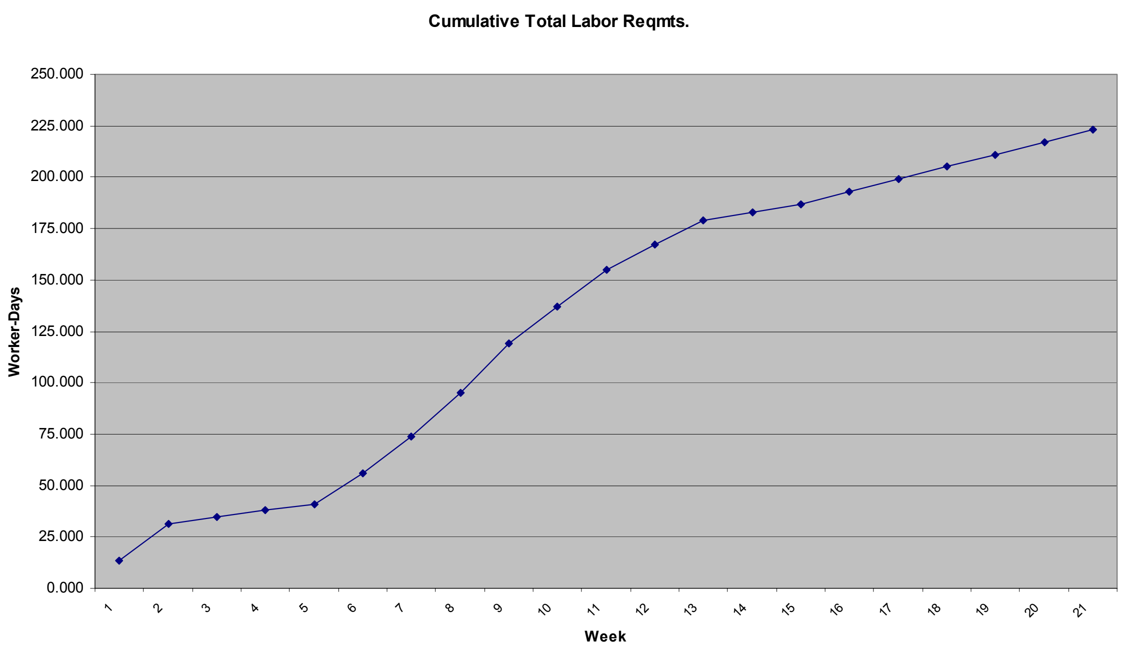
Parout / MatchJulia.com Project Resource Matrix					
Activity		**Med Tech.**	**Employees**	**Public Relations**	**Mtls.& Direct $**
A	Work with Cancer Societies to find local face for advertising	2	1	0.2	$0
B-H	Advertise (Direct Marketing)	1	1	1	$200
C-H	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-H	Train the people who will hold the drive.	1	2	0	$0
E-H	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-L	Advertise (Direct Marketing)	1	1	1	$50
C-L	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-L	Train the people who will hold the drive.	1	2	0	$0
E-L	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-M	Advertise (Direct Marketing)	1	1	1	$250
C-M	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-M	Train the people who will hold the drive.	1	2	0	$0
E-M	Hold the drive and sends the forms and cheek swabs to central location	2	3	1	$20
B-U	Advertise (Direct Marketing)	1	1	1	$80
C-U	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-U	Train the people who will hold the drive.	1	2	0	$0
E-U	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-B	Advertise (Direct Marketing)	1	1	1	$250
C-B	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-B	Train the people who will hold the drive.	1	2	0	$0
E-B	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
F	Central Location sorts and ships forms and cheek swabs to lab	0	4	0	$70
G	Takes 5 days to reach lab	0	0	0	$0
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	2	2	2	$0
I	Public Thank You Event	2	2	2	$0

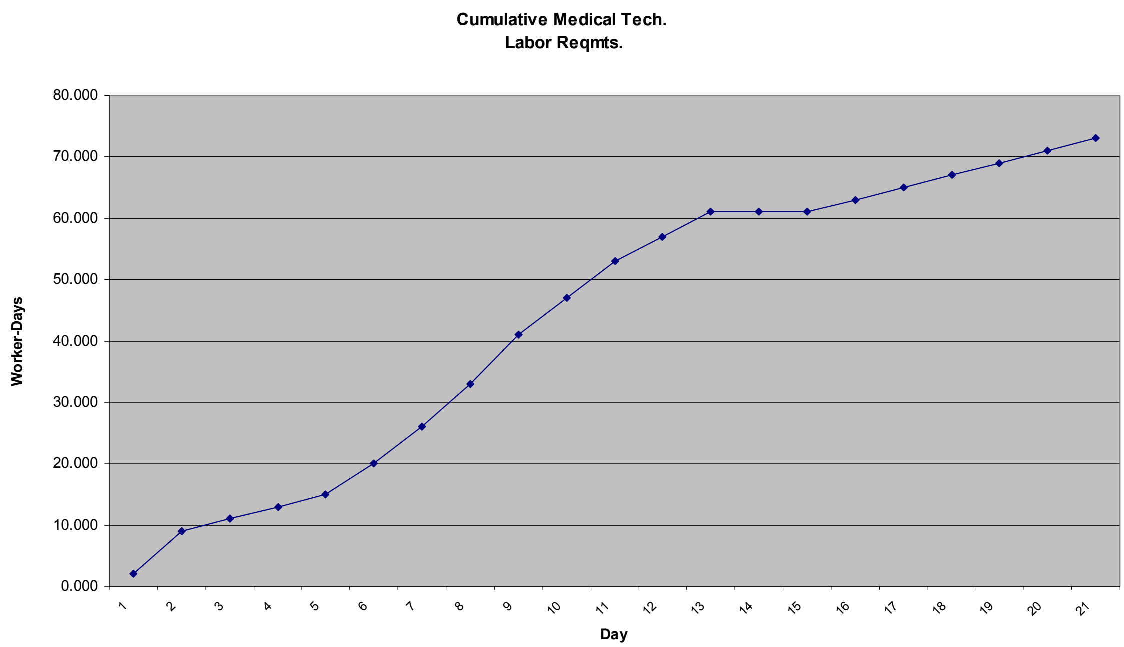
	Product of Original Schedule Matrix and Resource Matrix					Cumulative Labor and Total Project Labor							
Day	**Med Tech.**	**Employees**	**Public Relations**	**Mtls.& Direct $**	**Project**	**LABOR $**	**Total $**	**Cum. $**	**Med Tech.**	**Employees**	**Public Relations**	**Project**
1	2.000	11.000	0.200	250.000	13.200	1,584.000	1,834.000	1,834.000	2.000	11.000	0.200	13.200
2	7.000	11.000	0.200	0.000	18.200	2,184.000	2,184.000	4,018.000	9.000	22.000	0.400	31.400
3	2.000	1.000	0.200	0.000	3.200	384.000	384.000	4,402.000	11.000	23.000	0.600	34.600
4	2.000	1.000	0.200	0.000	3.200	384.000	384.000	4,786.000	13.000	24.000	0.800	37.800
5	2.000	1.000	0.200	0.000	3.200	384.000	384.000	5,170.000	15.000	25.000	1.000	41.000
6	5.000	5.000	5.000	830.000	15.000	1,800.000	2,630.000	7,800.000	20.000	30.000	6.000	56.000
7	6.000	7.000	5.000	800.000	18.000	2,160.000	2,960.000	10,760.000	26.000	37.000	11.000	74.000
8	7.000	9.000	5.000	740.000	21.000	2,520.000	3,260.000	14,020.000	33.000	46.000	16.000	95.000
9	8.000	11.000	5.000	560.000	24.000	2,880.000	3,440.000	17,460.000	41.000	57.000	21.000	119.000
10	6.000	8.000	4.000	540.000	18.000	2,160.000	2,700.000	20,160.000	47.000	65.000	25.000	137.000
11	6.000	9.000	3.000	60.000	18.000	2,160.000	2,220.000	22,380.000	53.000	74.000	28.000	155.000
12	4.000	6.000	2.000	40.000	12.000	1,440.000	1,480.000	23,860.000	57.000	80.000	30.000	167.000
13	4.000	6.000	2.000	40.000	12.000	1,440.000	1,480.000	25,340.000	61.000	86.000	32.000	179.000
14	0.000	4.000	0.000	70.000	4.000	480.000	550.000	25,890.000	61.000	90.000	32.000	183.000
15	0.000	4.000	0.000	70.000	4.000	480.000	550.000	26,440.000	61.000	94.000	32.000	187.000
16	2.000	2.000	2.000	0.000	6.000	720.000	720.000	27,160.000	63.000	96.000	34.000	193.000
17	2.000	2.000	2.000	0.000	6.000	720.000	720.000	27,880.000	65.000	98.000	36.000	199.000
18	2.000	2.000	2.000	0.000	6.000	720.000	720.000	28,600.000	67.000	100.000	38.000	205.000
19	2.000	2.000	2.000	0.000	6.000	720.000	720.000	29,320.000	69.000	102.000	40.000	211.000
20	2.000	2.000	2.000	0.000	6.000	720.000	720.000	30,040.000	71.000	104.000	42.000	217.000
21	2.000	2.000	2.000	0.000	6.000	720.000	720.000	30,760.000	73.000	106.000	44.000	223.000

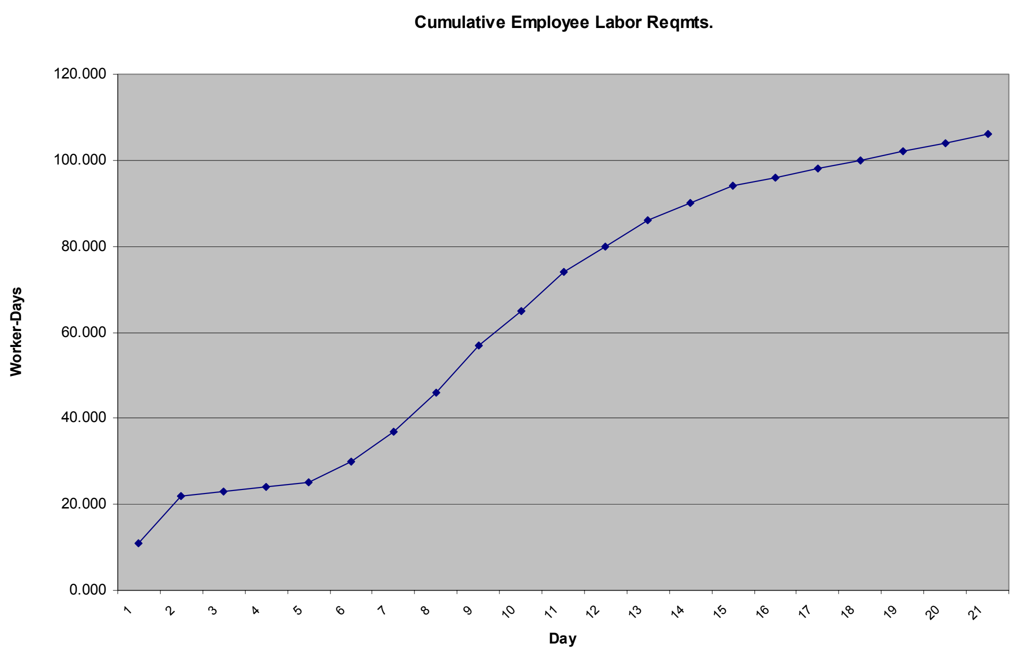

Medical Tech. Labor Requirements
Workers
Day
9.000
8.000
7.000
6.000
5.000
4.000
3.000
2.000
1.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21

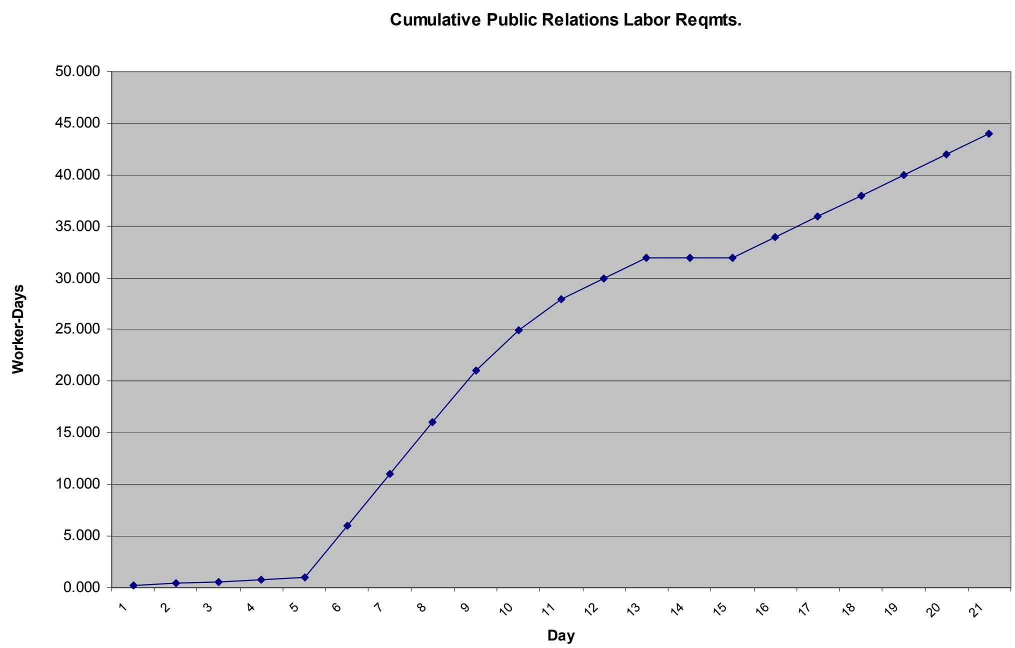

Employees Labor Requirements
Workers
Day
12.000
10.000
8.000
6.000
4.000
2.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21

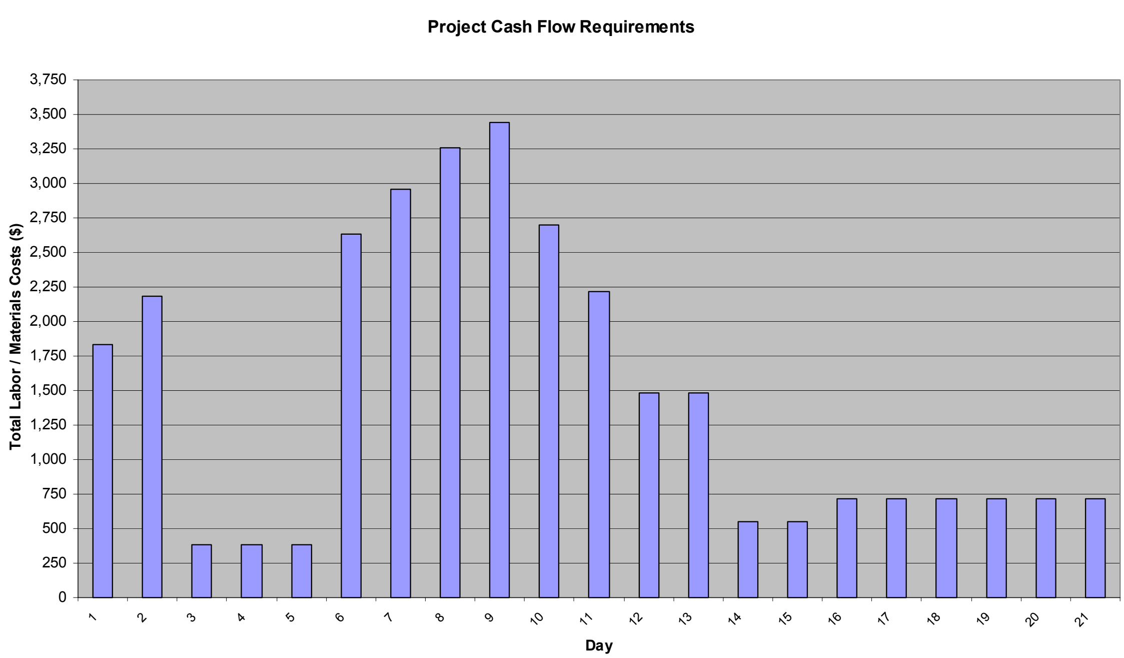

Public Relations Labor Requirements
Workers
Day
6.000
5.000
4.000
3.000
2.000
1.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21


Cumulative Total Labor Reqmts.
Worker-Days
Week
250.000
225.000
200.000
175.000
150.000
125.000
100.000
75.000
50.000
25.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21


Cumulative Medical Tech.
Labor Reqmts.
Worker-Days
80.000
70.000
60.000
50.000
40.000
30.000
20.000
10.000
0.000
1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
Day


Cumulative Employee Labor Reqmts.
Worker-Days
120.000
100.000
80.000
60.000
40.000
20.000
0.000
1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
Day

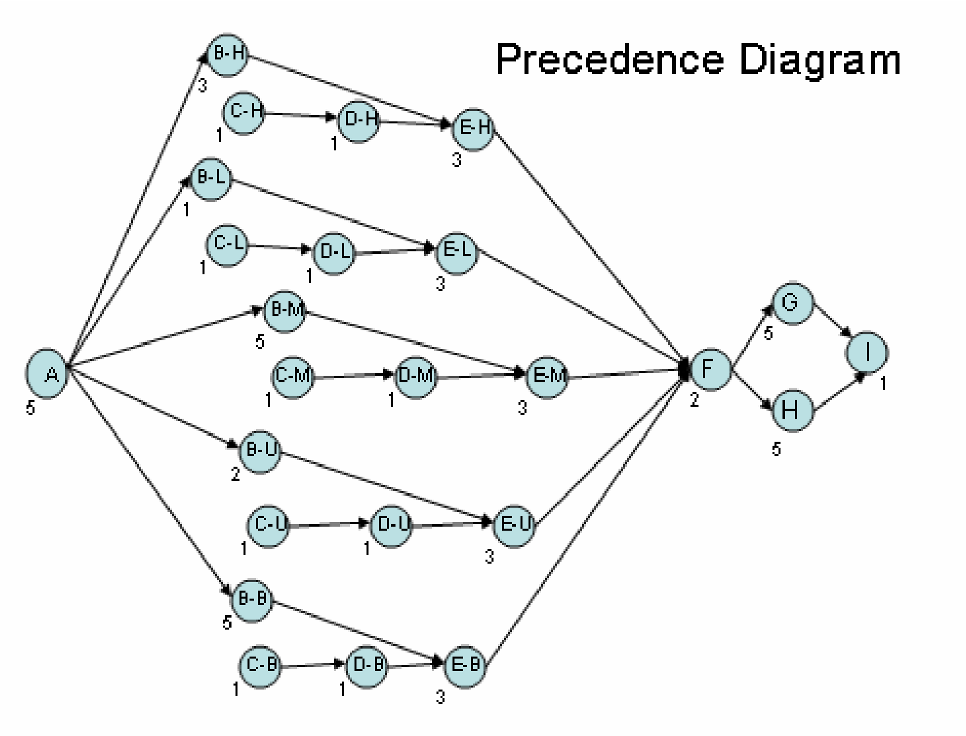

Cumulative Public Relations Labor Reqmts.
Worker-Days
50.000
45.000
40.000
35.000
30.000
25.000
20.000
15.000
10.000
5.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21
Day


Project Cash Flow Requirements
Total Labor / Materials Costs ($)
3,750
3,500
3,250
3,000
2,750
2,500
2,250
2,000
1,750
1,500
1,250
1,000
750
500
250
0
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21
Day

SOLUTIONS

PROJECT ACCELERATION / DELAY STEPS		
Activity	DURATION (IN DAYS)	
	DELAY	ACCELERATE
A	-	
Highland Mall		
B-H	-	-
C-H	by 6 (From 1 to 7)	-
D-H	by 6 (From 2 to 8)	-
E-H	-	-
Library		
B-L	-	by 3 (From 6 to 3)
C-L	-	-
D-L	-	-
E-L	-	by 3 (From 7 to 4)
Medical Center		
B-M	by 4 (from 6 to 10)	-
C-M	-	-
D-M	-	-
E-M	by 4 (from 11 to 15)	-
University		-
B-U	by 1 (from 6 to 7)	-
C-U	by 1 (from 1 to 2)	-
D-U	by 1 (from 2 to 3)	-
E-U	by 4 (from 8 to 12)	-
Business District		
B-B	by 3 (from 6 to 9)	-
C-B	by 5 (from 1 to 6)	-
D-B	by 5 (from 2 to 7)	-
E-B	by 4 (from 11 to 15)	-
F	by 4 (from 14 to 18)	-
G	by 4 (from 16 to 20)	-
H	by 4 (from 16 to 20)	-
I	by 4 (from 21 to 25)	-

PROJECT DURATION DETAILS			
Activity		Predecessors	Duration (Days)
A	Work with Cancer Societies to find local face for advertising	-	5
Highland Mall			
B-H	Advertise (Direct Marketing)	A	3
C-H	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-H	Train the people who will hold the drive.	C-H	1
E-H	Hold the drive and send the forms and cheek swabs to central location	B-H, D-H	3
Library			
B-L	Advertise (Direct Marketing)	A	1
C-L	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-L	Train the people who will hold the drive.	-	1
E-L	Hold the drive and send the forms and cheek swabs to central location	B-L, D-L	3
Medical Center			
B-M	Advertise (Direct Marketing)	A	5
C-M	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-M	Train the people who will hold the drive.	-	1
E-M	Hold the drive and sends the forms and cheek swabs to central location	B-M, D-M	3
University			
B-U	Advertise (Direct Marketing)	A	2
C-U	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-U	Train the people who will hold the drive.	-	1
E-U	Hold the drive and send the forms and cheek swabs to central location	B-U, D-U	3
Business District			
B-B	Advertise (Direct Marketing)	A	5
C-B	Set up for Training: Equipment, Supplies, Refreshments	-	1
D-B	Train the people who will hold the drive.	-	1
E-B	Hold the drive and send the forms and cheek swabs to central location	B-B, D-B	3
F	Central Location sorts and ships forms and cheek swabs to lab	E-H, E-L, E-M, E-U, E-B	2
G	Takes 5 days to reach lab	F	5
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	F	5
I	Public Thank You Event	G, H	1


Precedence Diagram
A
5
B-H
3
C-H
1
D-H
1
E-H
3
B-L
1
C-L
1
D-L
1
E-L
3
B-M
5
C-M
1
D-M
1
E-M
3
B-U
2
C-U
1
D-U
1
E-U
3
B-B
5
C-B
1
D-B
1
E-B
3
F
2
G
5
H
5
I
1

Labor Requirements (Worker-Days)					
	Activity	Medical Tech.	Employees	Public Relations	Materials and Direct
A	Work with Cancer Societies to find local face for advertising	10	5	1	$0
B-H	Advertise (Direct Marketing)	3	3	3	$200
C-H	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-H	Train the people who will hold the drive.	1	2	0	$0
E-H	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-L	Advertise (Direct Marketing)	1	1	1	$50
C-L	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-L	Train the people who will hold the drive.	1	2	0	$0
E-L	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-M	Advertise (Direct Marketing)	5	5	5	$250
C-M	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-M	Train the people who will hold the drive.	1	2	0	$0
E-M	Hold the drive and sends the forms and cheek swabs to central location	6	9	3	$20
B-U	Advertise (Direct Marketing)	2	2	2	$80
C-U	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-U	Train the people who will hold the drive.	1	2	0	$0
E-U	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
B-B	Advertise (Direct Marketing)	5	5	5	$250
C-B	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-B	Train the people who will hold the drive.	1	2	0	$0
E-B	Hold the drive and send the forms and cheek swabs to central location	6	9	3	$20
F	Central Location sorts and ships forms and cheek swabs to lab	0	8	0	$70
G	Takes 5 days to reach lab	0	0	0	$0
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	10	10	10	$0
I	Public Thank You Event	2	2	2	$0

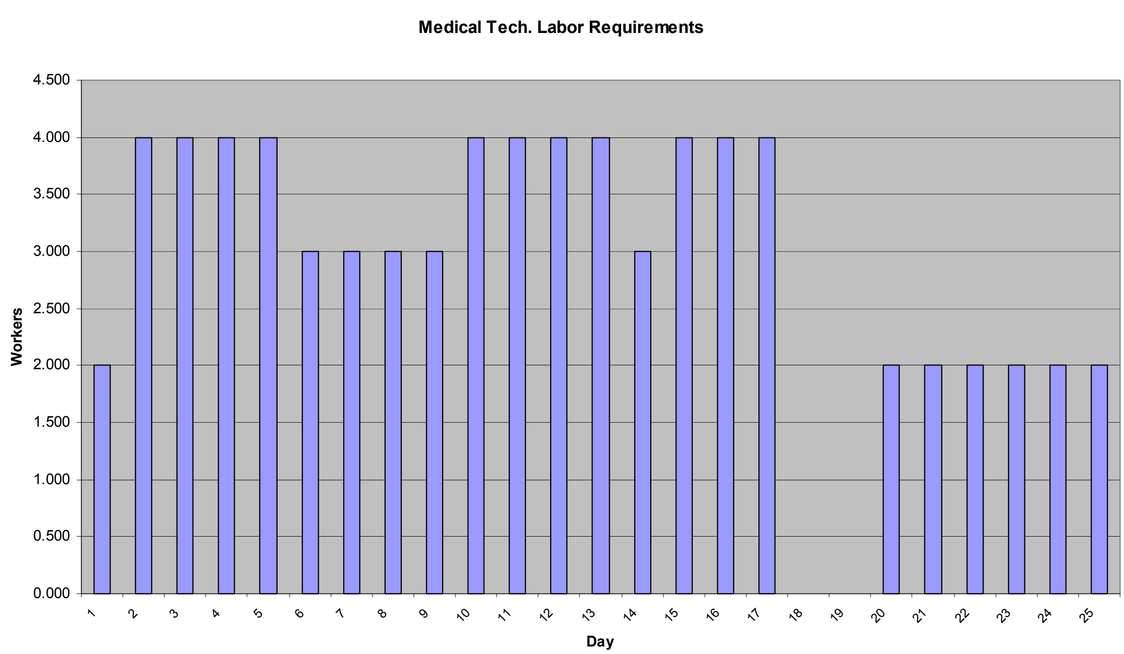
Resource leveled Schedule Matrix

DAY	ACTIVITY																								
		Highland Mall				Library				Medical Center				University				Business Dist.				POST DRIVE			
	A	b-h	c-h	d-h	e-h	b-l	c-l	d-l	e-l	b-m	c-m	d-m	e-m	b-u	c-u	d-u	e-u	b-b	c-b	d-b	e-b	f	g	h	i
1	1	0	0	0	0	0	1	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0
2	1	0	0	0	0	0	0	1	0	0	0	1	0	0	1	0	0	0	0	0	0	0	0	0	0
3	1	0	0	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0
4	1	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
5	1	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
6	0	1	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0
7	0	1	1	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	1	0	0	0	0	0
8	0	1	0	1	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0
9	0	0	0	0	1	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0
10	0	0	0	0	1	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0
11	0	0	0	0	1	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0
12	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0
13	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	1	1	0	0	0	0	0	0	0
14	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	1	0	0	0	0	0	0	0	0
15	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
16	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
17	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0	0	0	0	0	1	0	0	0	0
18	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
19	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	0	0	0
20	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
21	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
22	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
23	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
24	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1	1	0
25	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	1

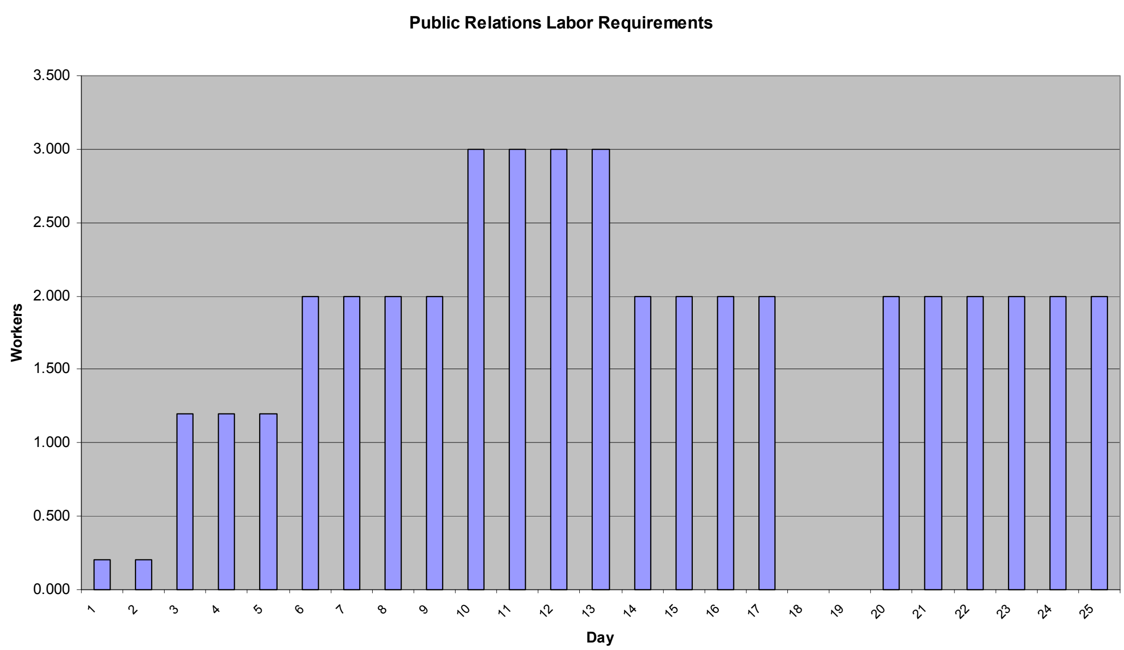
Parout / MatchJulia.com Project Resource Matrix					
Activity		Medical Tech.	Employees	Public Relations	Mtls.& Direct $
A	Work with Cancer Societies to find local face for advertising	2	1	0.2	$0
B-H	Advertise (Direct Marketing)	1	1	1	$200
C-H	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-H	Train the people who will hold the drive.	1	2	0	$0
E-H	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-L	Advertise (Direct Marketing)	1	1	1	$50
C-L	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-L	Train the people who will hold the drive.	1	2	0	$0
E-L	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-M	Advertise (Direct Marketing)	1	1	1	$250
C-M	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-M	Train the people who will hold the drive.	1	2	0	$0
E-M	Hold the drive and sends the forms and cheek swabs to central location	2	3	1	$20
B-U	Advertise (Direct Marketing)	1	1	1	$80
C-U	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-U	Train the people who will hold the drive.	1	2	0	$0
E-U	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
B-B	Advertise (Direct Marketing)	1	1	1	$250
C-B	Set up for Training: Equipment, Supplies, Refreshments	0	2	0	$50
D-B	Train the people who will hold the drive.	1	2	0	$0
E-B	Hold the drive and send the forms and cheek swabs to central location	2	3	1	$20
F	Central Location sorts and ships forms and cheek swabs to lab	0	4	0	$70
G	Takes 5 days to reach lab	0	0	0	$0
H	Alert the papers, Make arrangements for public appearances, Give Villanueva Time to Come down	2	2	2	$0
I	Public Thank You Event	2	2	2	$0

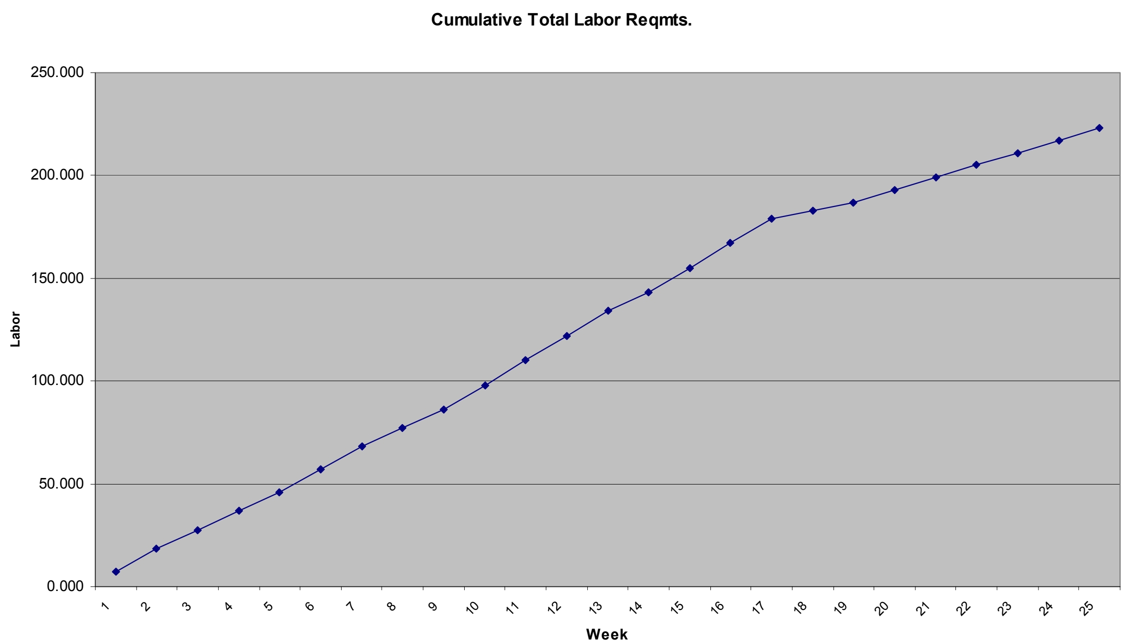
	Product of Schedule Matrix and Resource Matrix					Cumulative Labor and Total Project Labor							
Day	**Medical Tech.**	**Employees**	**Public Relations**	**Mtls.& Direct $**	**Project**	**LABOR $**	**Total $**	**Cum. $**	**Doctors**	**Employees**	**Public Relations**	**Project**
1	2.000	5.000	0.200	100.000	7.200	864.000	964.000	964.000	2.000	5.000	0.200	7.200
2	4.000	7.000	0.200	50.000	11.200	1,344.000	1,394.000	2,358.000	6.000	12.000	0.400	18.400
3	4.000	4.000	1.200	50.000	9.200	1,104.000	1,154.000	3,512.000	10.000	16.000	1.600	27.600
4	4.000	4.000	1.200	20.000	9.200	1,104.000	1,124.000	4,636.000	14.000	20.000	2.800	36.800
5	4.000	4.000	1.200	20.000	9.200	1,104.000	1,124.000	5,760.000	18.000	24.000	4.000	46.000
6	3.000	6.000	2.000	270.000	11.000	1,320.000	1,590.000	7,350.000	21.000	30.000	6.000	57.000
7	3.000	6.000	2.000	330.000	11.000	1,320.000	1,650.000	9,000.000	24.000	36.000	8.000	68.000
8	3.000	4.000	2.000	280.000	9.000	1,080.000	1,360.000	10,360.000	27.000	40.000	10.000	77.000
9	3.000	4.000	2.000	270.000	9.000	1,080.000	1,350.000	11,710.000	30.000	44.000	12.000	86.000
10	4.000	5.000	3.000	520.000	12.000	1,440.000	1,960.000	13,670.000	34.000	49.000	15.000	98.000
11	4.000	5.000	3.000	520.000	12.000	1,440.000	1,960.000	15,630.000	38.000	54.000	18.000	110.000
12	4.000	5.000	3.000	520.000	12.000	1,440.000	1,960.000	17,590.000	42.000	59.000	21.000	122.000
13	4.000	5.000	3.000	520.000	12.000	1,440.000	1,960.000	19,550.000	46.000	64.000	24.000	134.000
14	3.000	4.000	2.000	270.000	9.000	1,080.000	1,350.000	20,900.000	49.000	68.000	26.000	143.000
15	4.000	6.000	2.000	40.000	12.000	1,440.000	1,480.000	22,380.000	53.000	74.000	28.000	155.000
16	4.000	6.000	2.000	40.000	12.000	1,440.000	1,480.000	23,860.000	57.000	80.000	30.000	167.000
17	4.000	6.000	2.000	40.000	12.000	1,440.000	1,480.000	25,340.000	61.000	86.000	32.000	179.000
18	0.000	4.000	0.000	70.000	4.000	480.000	550.000	25,890.000	61.000	90.000	32.000	183.000
19	0.000	4.000	0.000	70.000	4.000	480.000	550.000	26,440.000	61.000	94.000	32.000	187.000
20	2.000	2.000	2.000	0.000	6.000	720.000	720.000	27,160.000	63.000	96.000	34.000	193.000
21	2.000	2.000	2.000	0.000	6.000	720.000	720.000	27,880.000	65.000	98.000	36.000	199.000
22	2.000	2.000	2.000	0.000	6.000	720.000	720.000	28,600.000	67.000	100.000	38.000	205.000
23	2.000	2.000	2.000	0.000	6.000	720.000	720.000	29,320.000	69.000	102.000	40.000	211.000
24	2.000	2.000	2.000	0.000	6.000	720.000	720.000	30,040.000	71.000	104.000	42.000	217.000
25	2.000	2.000	2.000	0.000	6.000	720.000	720.000	30,760.000	73.000	106.000	44.000	223.000

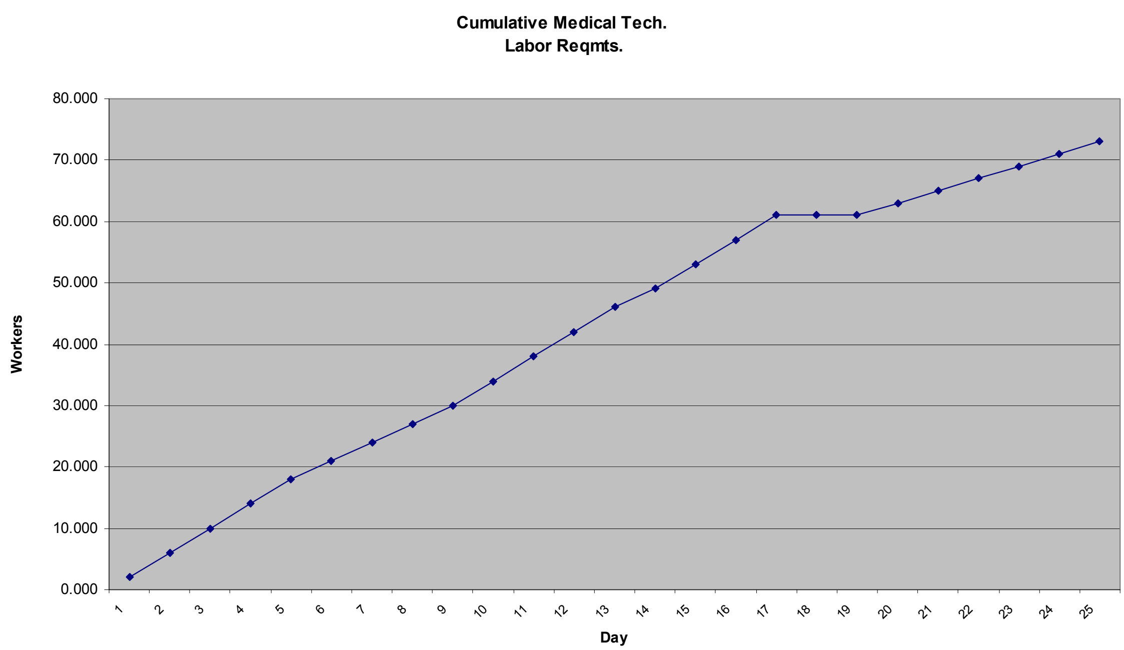

Total Project Labor Requirements
Workers
14.000
12.000
10.000
8.000
6.000
4.000
2.000
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day


Medical Tech. Labor Requirements
Workers
4.500
4.000
3.500
3.000
2.500
2.000
1.500
1.000
0.500
0.000
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day

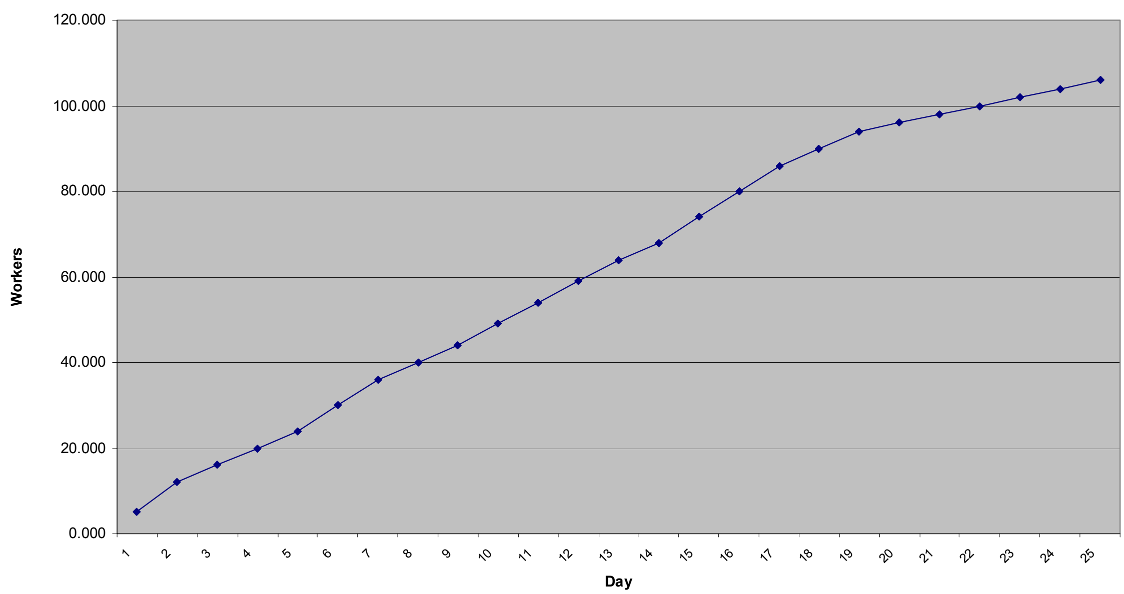

Employees Labor Requirements
8.000
7.000
6.000
5.000
4.000
3.000
2.000
1.000
0.000
Workers
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day


Public Relations Labor Requirements
3.500
3.000
2.500
2.000
1.500
1.000
0.500
0.000
Workers
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day

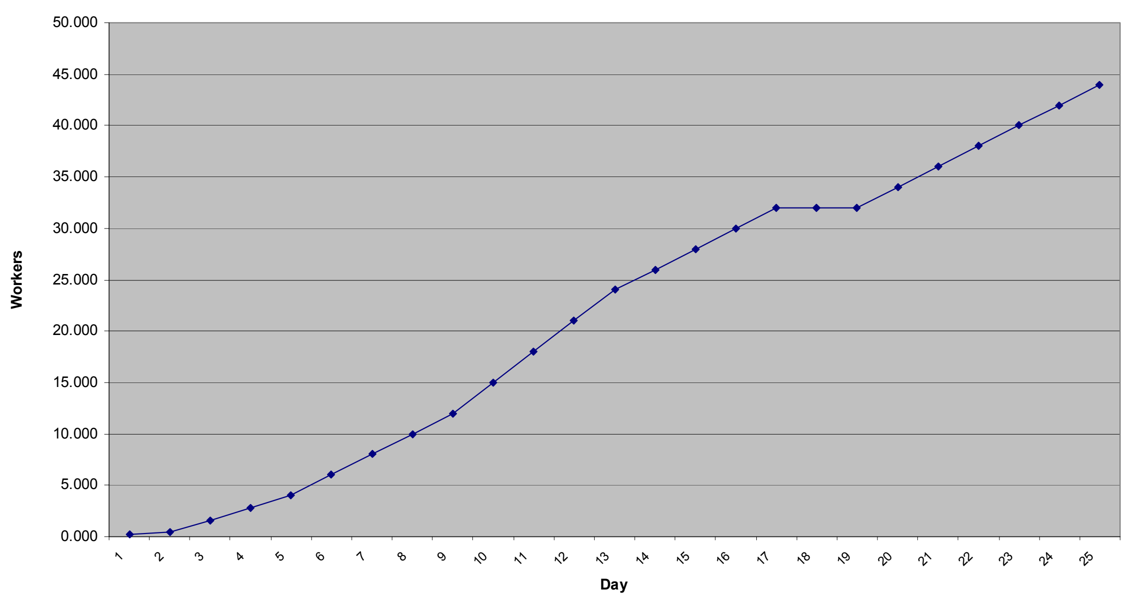

Cumulative Total Labor Reqmts.
250.000
200.000
150.000
100.000
50.000
0.000
Labor
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Week


Cumulative Medical Tech.
Labor Reqmts.
80.000
70.000
60.000
50.000
40.000
30.000
20.000
10.000
0.000
Workers
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day

Cumulative Employees Labor Reqmts.



Cumulative Public Relations Labor Reqmts.




Project Cash Flow Requirements
Total Labor and Materials
2,250
2,000
1,750
1,500
1,250
1,000
750
500
250
0
1 2 3 4 5 6 7 8 9 10 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25
Day

RENAULT YAHOO! ARGENTINA

D.K. (Skip) Smith, American University of Nigeria
Carlos A. Aimar, Centro Universitario San Isidro
Jorge Fajardo, Universidad de Palermo

CASE DESCRIPTION

This case challenges students to develop a strategy to grow Renault's business in Argentina, now that the economy is recovering from the severe economic disruptions caused by the fact that in 2002 Argentina defaulted on its debt and was declared bankrupt. The case is based on data collected by one of the authors in Argentina. The case is appropriate for senior-and level undergraduates as well as students in MBA and Executive Development programs. It is designed to be taught in a one hour and a half? class session, and is likely to require at least a couple hours of preparation by students.

CASE SYNOPSIS

Mr. Pedro Gouzou is Vice President of Marketing for Renault Argentina S.A., the Argentine subsidiary of the French automobile assembler and marketer, Renault S.A. Due to Argentina's default on its sovereign debt and the subsequent deterioration in the economic environment in Argentina, Renault's sales of new cars in Argentina fell dramatically. In 2003, for the entire country of nearly 40 million people, demand in Argentina for new Renault vehicles averaged slightly more than 40 vehicles per day. At the end of 2004, however, with the Argentine economy now recovering quite strongly, Renault is eager to rebuild sales. Additional data and information in the case include:

1. *For Argentina: Historical overview, a sample of recent statistics from the World Bank, and (for benchmarking purposes), comparable statistics for the United States.*
2. *For the company (at both local and global levels): Historical overview, current performance, and numerous factors impacting that performance.*
3. *Characteristics of the local company's current strategy, including descriptive information on the product line, characteristics of the distribution system, information on the promotion and pricing strategies the company is currently using, etc.*
4. *Characteristics of the current competitive situation.*
5. *Detailed data on the attitudes and behaviors of buyers of cars in Argentina.*

INSTRUCTORS' NOTES

As indicated in the case, the situation faced by Mr. Pedro Gouzou, Vice President of Marketing for Renault Argentina (hence, RA) is that he has been charged by his CEO to increase (within the next twelve months) sales of Renault cars in Argentina by 15%. As regards lessons and/or information which students should learn from this case, at least five points can be made:

1. At the beginning of the case, students will need to consider the extent to which developed-world models and conceptual frameworks can be applied to challenges and opportunities in the developing world. By the end of the case discussion, they will have discovered that some conceptual frameworks (for example, the development and use of "growth through innovation" strategies) can be useful guides to managerial action not only in the developed world but in the developing world as well.

2. Students will be able to compare their solutions to the one developed by the hero of the case, that is, Mr. Pedro Gouzou, Vice President of Renault Argentina.

3. Students will discover that a manager's conceptual framework (in this case, a "growth through innovation" strategy drawn from a set of alternatives suggested by Sawhney et al. (2006) and then fleshed out using a model very similar to one proposed by Urban and Hoffer (2003)) powerfully impacts the nature of the process and/or options used to turn a business around. Specifically, a Sawhney et al.-based approach to rebuilding revenues and profitability is likely to differ considerably from a plan to rebuild revenues and profitability based on alternative conceptual frameworks such as "turnaround strategy" or "marketing strategy."

4. As they work through the case, students are exposed not only to a bit of information on an important South American market (Argentina) but also to a bit of history on Renault Argentina, a company which has persevered for more than 50 years in Argentina, experiencing in some years huge profits, in some years huge losses, but currently enjoying (as the economy continues to recover from the bankruptcy of 2002) a high level of success.

5. Students may sometimes wonder about the extent to which technology-based tools such as the web can be used to develop and exploit business opportunities in the developing world. This case provides an interesting example of the extent to which technology-based tools such as the web are already being used not just in the developed world but in the developing world as well.

DISCUSSION QUESTIONS

We often select one student to lead the discussion. Another approach would be to solicit input from various students at various stages of the analysis. Either way, our usual approach to this case is threefold:

1. **Solicit from many students the details of the case, including information about the macroeconomic environment at the time of the case; information on the company; information on the competitive environment; information on customers, information on strategies the company has used over the years, and information on how those strategies have been implemented. Usually, we write much of this information on the board, so that if questions on "facts of the case" arise, we will have much of that information in front of us.**

2. **Ask an individual student or the class as a whole to address a very specific series of questions. Those questions, and comments relating to three possible solutions to the case, are as listed below:**

2.1. What is the main problem?

Students usually conclude that Vice President Gouzou must develop a plan to increase (within 12 months) the unit sales of Renault Argentina. We reinforce the idea that this is a reasonable statement of the challenge Mr. X faces.

2.2. What kind of problem is this?

Instructors should not be surprised if there are as many answers to this question as there are students in the class. Clearly, there is no one "right" answer. However, three alternative approaches, each of which seems quite relevant to the situation, are as indicated below:

- ♦ Marketing strategy.
- ♦ Turnaround strategy.
- ♦ Growth through innovation.

2.3. **For the kind of problem selected, what are the key variables and which expert says so?**

For students concluding that the main problem is "marketing strategy," Perreault and McCarthy (2002) suggest that the key marketing strategy variables are: 1) Target market; and 2) The marketing mix (that is, place, price, product, and promotion). For students concluding that the main problem is the need for a "turnaround strategy," Sheth (1985) suggests there are nine strategies which can be considered: 1) Entrenchment (that is, fight for a larger share of existing uses of products in existing markets); 2) Consider selling to intermediaries; 3) Mandatory consumption (that is, ask government to pass a law requiring the use of a product or service); 4) Go international; 5) Broaden product horizons (that is, don't sell just the computer; rather, sell the computer plus a full set of ancillary products and services); 6) In existing markets, identify new applications for products; 7) In existing markets, identify new usage situations; 8) Repositioning (that is, in new markets, identify new uses for products by changing the image of the product); and 9) Redefining markets (that is, in new markets, identify new uses for products by making functional changes in those products. For students concluding that the main problem is "growth through innovation," Sawhney et al (2006) identify the following twelve approaches to innovation which can be used to create growth: 1) Offerings (i.e., create new products); 2) platform (that is, create new offerings by combining common components in different ways; 3) solutions (that is, offer integrated solutions to customer problems, not products); 4) customers (identify new segments); 5) customer experience (redesign the overall experience of customers); 6) value capture (create new ways for the company to generate revenue); 7) processes (that is, redesign core processes to increase efficiency and/or effectiveness); 8) organization (change the firm's form, function, or activity scope); 9) supply chain (redesign the firm's sourcing and/or fulfillment activities); 10) presence (create new distribution channels); 11) networking (create network-based intelligent products/services); and 12) brand (leverage a brand into new domains).

2.4. What data from the case relate to the key variables?

As Implied above (and this is one of the key learning points of the case), the data students present will depend on the main problem they identify. Students believing the main problem is "marketing strategy" will focus on the two key variables identified earlier, that is, the target market and the marketing mix. Appendix 1 identifies data from the case which relate to each of these key variables. Students believing the main problem is the need for a turnaround strategy will focus on the nine alternative strategies identified by Sheth; Appendix 2 identifies data from the case which relate to each of those alternatives. Students believing the main problem is a need to identify and exploit "growth through innovation" opportunities will focus on one or more of the twelve alternatives suggested by Sawhney et al.

2.5. What alternative solutions can be identified?

Because research suggests we make better decisions if we identify alternatives and then chose one, we require students to identify at least two alternatives. Of course, students having difficulties coming up with a second alternative can be reminded that one possible solution is to "change nothing."

2.6. Which one alternative does the class/student recommend, and why?

"Changing nothing" is unlikely to help Mr. Gouzou achieve his objective, that is, to increase (within the next 12 months) units sales of Renault Argentina by 15%. Thus, students believing the main problem is the need for a new marketing strategy will recommend an approach which focuses (or re-focuses) on the target market and the "4Ps" (that is, price, product, promotion, and place/distribution). Students believing the main problem is the need for a "turnaround strategy" are likely to recommend consideration of one or more of the alternatives identified by Sheth. Students believing the main problem is the need to identify and exploit one or more "growth through innovation" options are likely to recommend consideration of one or more of the options suggested by Sawhney et. al.

The approach used successfully by Mr. Gouzou was a "growth through innovation" remarkably similar to one of those suggested by Sawhney et al. (2006). For additional information on what happened, please see the epilogue.

2.7. What negatives are associated with the alternative selected by the class leader and/or other members of the class?

Very few solutions are risk and/or problem-free. Negatives associated with the solution proposed by the class leader and/or other members of the class could include the following: The chosen alternative, if it requires Renault Argentina to acquire specialized equipment and/or skills which the organization doesn't currently possess, could be expensive both in terms of time and money. Also, because the case probably doesn't provide all the data a decisionmaker would need (in other words, it is likely that some important data is missing), it is possible that assumptions made by the class leader regarding the actual situation faced by Renault Argentina are incorrect. If so, the proposed solution might be inappropriate.

3. **The third and final step in discussing a case with students is to share with them what actually happened (that is, to provide them with an epilogue to the case) and to discuss with them the implications of that outcome. In this case, as he thought about how to tackle the challenge of increasing the number of units sold by 15% within 12 months, Mr. Gouzou and his team identified and then evaluated a number of "growth through innovation" related approaches, including many of the sorts of options identified by Sawhney et al. (2006). The conclusions reached by Gouzou and his team included the following:**

   a. Given his need to increase the number of units sold and to do so quite quickly (that is, within 12 months), several of the sorts of "growth through innovation" options suggested by experts including Sawhney et. al. (for example, the development of innovative products and/or services, the development of integrated solutions, the re-design of core operating procedures, changing the form/function and/or activity scope of the firm, creating network-centric product offerings, etc.) did not appear relevant to Mr. Gouzou.

   b. Of the "growth through innovation" options which did (because they could be actioned relatively quickly) look interesting, Mr. Gouzou found himself drawn to the dimension of "presence," that is, the creation of "new distribution channels or innovative points of presence, where offerings can be bought or used by customers."

   c. Based on his knowledge of the fact that nearly 40% of Argentina's population lives in the area of greater Buenos Aires and does therefore have access to cell phones, computers, and the internet, Gouzou found himself wondering whether it would be possible to achieve the objective set by the CEO (that is, to increase RA unit sales by 15% within the next 12 months) simply by making it possible for customers to buy a Renault vehicle over the internet. Ultimately, Gouzou and his team decided that selling on the web (that is, the sort of "new distribution channels or innovative points of presence, where offerings can be bought or used by customers" option) not only had the potential to achieve the desired results but also was very appropriate to Renault's existing situation and aspirations. The advantages of launching an initiative to offer vehicles on the web perceived by Mr. Gouzou and his team included:

1). While RA's dealer network in cities like Buenos Aires and Mendoza is strong, the dealer network does not provide strong coverage in rural areas. For its vehicles, web-based selling should enhance RA's ability to increase levels of awareness, interest, desire, and action (that is, purchase) in rural areas. In short, this web-based initiative should improve RA's geographic coverage.

2). For many years, RA has cultivated a high technology image for its vehicles. Launching a web-based selling initiative is consistent with (and will contribute to) the company's high tech image. Furthermore, making a web-based selling initiative at this time gives RA a "first mover" advantage, that is, the additional prestige and visibility associated with being the first local automobile company to launch such an initiative.

3). Moving on-line should allow RA to strengthen its relationships not only with customers but also with its dealers and their salespeople. Moving on-line also provides a way for RA to update very quickly its messages to members of each of the above groups, that is, customers, dealers, and salespeople.

4). Moving on-line offers the possibility that RA will be able (after the web-based initiative is up and running) to reduce its expenditures on traditional media (print, electronic, billboard, etc.).

5). The web-based selling initiative means that RA will have a 24/7 sales and information presence, not a sales and information presence limited to the number of hours per week that dealerships are open.

6). Moving on-line offers the possibility that by selling out of inventory, RA will be able to reduce both its finished-goods inventory and the financial costs associated with holding that finished goods inventory.

d. As he thought further about the idea of meeting the CEO's objective by starting to sell Renault vehicles over the internet, Mr. Gouzou realized that he and his team would have to make decisions regarding every element of Renault's marketing strategy, including the following:

1). TARGET MARKET: What group of consumers should be targeted, if Renault decides to make a vehicle available for sale on the internet?

2). PRODUCT: Should the specific product (that is, the vehicle or vehicles) sold over the internet be available only over the internet? After thinking about this issue, Mr. Gouzou and his team concluded that the vehicle sold over the internet should be unique to the channel, that is, that it should be available to consumers only over the internet.

3). PROMOTION: How should Renault communicate to customers the fact that a vehicle was now available to them over (and only over) the internet? Also, what should the steps in the selling process be, for customers purchasing a new vehicle on the internet?

4). PRICE: Should there be one single price for all customers buying the Renault vehicle being promoted on the internet? How should financing be handled? What about shipping charges?

5). PLACE (that is, distribution): How will vehicles sold on the internet be delivered to customers? Will they be delivered through the dealership closest to the location of the customer? If so, how quickly will the vehicle be available for the customer to pick up from his/her dealer?

e. Regarding the above questions, Mr. Gouzou and his team reached the following conclusions:

1). TARGET MARKET: The target market most likely to be interested in purchasing a new car on the internet would be young, technologically savvy consumers. Mr. Gouzou and his team concluded that the type of car this group would most likely be able to afford would be a compact car like the Renault Clio. In the initial stage of the project, Mr. Gouzou and his team decided to offer on the web the following two versions of the Clio: the Clio Authentique (this version of the Clio has a 1.2 liter engine) and the Clio Expression (this version has a 1.6 liter engine).

2). PRODUCT: Mr. Gouzou and his team considered at length the question of how to differentiate a Clio purchased over the internet from a Clio purchased in the traditional fashion, that is, by a consumer going to a dealership and making the purchase there. Ultimately, Gouzou and his team decided that the way to differentiate the Clio purchased over the internet was to co-brand it with the name of a well-known and well-regarded e-business. When Gouzou approached Yahoo! Argentina with the idea of creating a co-branded car (that is, the Clio Yahoo!), Yahoo! Argentina agreed to allow its name to be used in this way.

3). PROMOTION: One of the key challenges faced by Gouzou and his colleagues was the issue of how to make target market consumers aware of the fact that the Clio Yahoo! did exist but could be purchased only on the internet. Ultimately, Gouzou and his team decided on an intense local and national advertising campaign using billboards, posters at shopping malls, announcements on buses, posters at sports events and concerts, and so on.

Regarding the web-based selling process for purchasing a Clio Yahoo!, Gouzou and his team decided that customers purchasing a Clio Yahoo! on the web would need to go through the following sequence of steps:

a). Customer goes to RA's web page and clicks on "Direct Click."

b). Customer chooses the desired product; at first, (and as indicated above) the options were the 1.2 and the 1.6 liter versions of the Clio Yahoo!

c). Customer chooses the color he/she desires.

d). Customer indicates the dealer to whom their vehicle should be delivered.

e). Customer indicates how they will pay for the vehicle. The options include 1) pay cash; or 2) select from a variety of financing plans provided on the website.

f). Customer confirms the payment option he/she has selected.

g). Customer receives confirmation of the payment option he/she has selected.

h). If the desired colors are not available, the customer is offered alternatives which are available.

i). Customer inputs their personal data on a form called "Purchase Conditions."

j). Customer clicks on "Purchase Confirmation."

k). Once confirmed and accepted, the customer is invited to print the bank forms and other documents relating to the transaction.

4). PRICE: Gouzou and his marketing team decided that there would be one (and only one) price for each of the two models of the Clio Yahoo! purchased on the web. Freight charges would be included in the one price offered to all customers; this means that purchasers in areas located near the factory are subsidizing the freight-related costs of customers located far from the factory.

For customers needing to finance their purchase of a Clio Yahoo!, Gouzou and his team decided that a variety of financing alternatives would be offered on the RA website.

5). DISTRIBUTION: Gouzou and his team decided that customers purchasing a Clio Yahoo! could indicate (as they completed their web-based purchase) where they would like to pick up their car.

f. While Mr. Gouzou was not aware of the research by Urban and Hoffer (2003) in their study of virtual (that is, web-based) automobile dealerships, it turns out that the decisions he and his team reached on the marketing strategy-related issues set forth above are very consistent with the recommendations made by the authors in their research report. For example, Urban and Hoffer (like Mr. Gouzou and his team, as explained earlier) recommended that the target market be young, tech-savvy customers; that the website should (in the beginning) be intensively promoted using billboards, transit advertising, posters at sports events and concerts, etc.; that a "one-price" policy should be used; that a variety of financing options should be offered on the web-page; that vehicles purchased on the web should be delivered within a fixed period of time to a dealer or non-dealer location convenient to the customer; etc..

CONCLUDING COMMENTS

While the above comments describe the program initiated by Mr. Pedro Gouzou and his team to achieve the objectives set by the CEO, readers may also be interested in learning the answers to the following two questions:

1). Did RA's web-based selling initiative allow Mr. Gouzou to achieve the objective (that is, to increase unit sales by 15% within the next 12 months) set by his CEO? The answer is "Yes."

2). Are there other implications flowing from this analysis of the case which might be of interest to readers and/or of great use to Renault Argentina as well? The authors of this case believe that once again, the answer is "Yes." Points we would like to offer in support of our viewpoint include the following:

a). While the web-based initiative has helped RA grow its business in Argentina, RA's total business in Argentina is still very small. Given the indication in the case that RA currently accounts for approximately 5% of new car sales in Argentina, there is a huge opportunity to grow the company's presence in the automobile industry back toward levels achieved during the days when RA accounted for 1/3 (that is, 33%) of all new vehicles sold in Argentina.

b). As always, the question is exactly what actions to take and/or initiatives to launch, so as to grow RA's business in Argentina back to the levels achieved by the company in the past.

c). Interestingly enough, the "growth through innovation" typology suggested by Sawhney et al. (2006) may provide the answers the company needs. As mentioned earlier in this note, because of very short timeframe on the objective given him by his CEO, Mr. Gouzou discounted several of the Sawhney et al. suggestions regarding ways to grow through innovation. Given more time, however, it seems quite likely that if RA has (or can develop) deep knowledge of their customers' vehicle-related attitudes, behaviors, and experiences, it should be able to use that information to select the Sawhney et al. (2006) "growth through innovation" dimensions which are most promising and then develop programs to grow back toward historic levels, by exploiting those "growth through innovation" opportunities. If RA needs a model to facilitate their development of deep knowledge of their customers, the article by Arken (2002) suggests a series of questions which may be useful to them.

APPENDIX 1
CASE DATA RELATING TO MARKETING STRATEGY MODEL

TARGET MARKET: The case indicates that one possible target market would be teenagers, single persons, young couples, and people who are entering the new car market for the first time.

PRODUCT: The case indicates that "small cars" account for more than 90% of the new cars sold in Argentina each of the last couple of years. Additional information about two of the primary car types available in Argentina is as indicated below:

> HATCHBACKS: these are small cars with three to five doors. They tend to be used for personal transportation. They appeal to teenagers, single persons, young couples, and people who are entering the new car market for the first time. They have a modern style and a modern image, and easy handling is likely to be especially important to buyers.
>
> SEDANS: these are medium-size, fast and comfortable, and tend to have four doors plus a trunk. The size of the trunk can be important to buyers. These cars tend to be of special interest to users in search of status; for this reason elegance and comfort (particularly back seat comfort) are likely to be especially important. These vehicles are of interest to users both in urban settings and to those who use interstate highways.

PRICE: The case indicates that data from Brazil suggests that a high percentage of new car purchases are financed, rather than paid for in cash. As indicated below, this is especially true in the case of "small cars." Industry experts believe that the new car financing patterns in Argentina are quite similar to those found in Brazil.

	%FINANCED	%PURCHASED FOR CASH
Small cars	87%	13%
Midsized cars	58%	42%
All other categories	57%	43%

PROMOTION: As in the United States, in Argentina new cars have traditionally been advertised using a variety of media including billboards, print media (including newspapers and magazines), radio, television, and so on. As in the United States, the increased power and market penetration (especially with younger consumers) of the Internet is leading manufacturers of consumer products in Argentina (including the car companies) to re-examine and reevaluate their expenditures on traditional media.

Regarding the internet and its usage by consumers in Argentina, the case indicates that "more than 40% population lives in Buenos Aires and its suburbs; one of the implications is that quite a large percentage of the population has access to modern telecommunications products and services including computers, cell phones, and internet access. Research conducted in Argentina indicates that approximately 9 million citizens of Argentina use the internet when making purchases, and at least 5 million have actually purchased something online."

DISTRIBUTION: As in the United States, in Argentina new cars have traditionally been sold through dealerships. In Argentina, this has led to a situation where urban buyers (especially those located in Buenos Aires) are well served and are offered a wide variety of different makes and models of new cars; however, consumers interested in buying a new vehicle but living in rural areas may not have very many makes and models of new cars from which to choose.

APPENDIX 2
CASE DATA RELATING TO THE "TURNAROUND STRATEGIES" MODEL

1. ENTRENCHMENT. This approach, according to Sheth, involves taking market share away from competitors. He suggests four alternatives which firms may be able to use: 1) Segment the market (and introduce different products, flavors, or brand names for each segment); 2) Identify specialty markets; 3) Go after heavy users of the product; and 4) Seek multiple channels of distribution. As to data relating to the above alternatives, the case indicates that small cars accounted for a very large percentage of total sales, that the "hatchback" format appears to appeal to quite a number of consumers (teenagers, young singles, couples entering the new car market for the first time, and so on), and that an Internet-based channel of distribution might not only be a very appropriate approach to this particular segment of the market, but that it might also be very cost effective in terms of promotion and helpful in dealing with distribution related challenges (for example, creating a strong presence in rural markets) as well.

2. SWITCH TO INTERMEDIARIES. If getting products into the hands of consumers is difficult for some reason, Sheth suggests that marketers may be able to succeed by selling to intermediaries (wholesalers, processors of agricultural products, etc.) instead. There is very little data in the case suggesting that this turnaround strategy would be useful to Renault Argentina.

3. MANDATORY CONSUMPTION. Sheth indicates that sometimes it is possible to revive a business by getting government (state, local, or federal) to pass a law making in mandatory for consumers to purchase certain categories of products. In the U.S., for example, infants

traveling in cars must be strapped into a car seat. It seems very unlikely that the company will be able to get the government to pass a law mandating that consumers in Argentina must purchase their vehicles from Renault Argentina.

4. GO INTERNATIONAL. Sheth indicates that sometimes it is possible to revive a business by beginning to sell the product in markets outside the home market. The case indicates indicate that Renault Argentina is already exporting vehicles. In short, it seems unlikely that this turnaround strategy will achieve the results Renault Argentina is seeking to achieve.

5. BROADEN THE PRODUCT HORIZON. Sheth indicates that this approach often involves focusing on the function that a product performs and then thinking of the product as a component in a system. There is no data in the case supporting the idea that within the next 12 months, this turnaround strategy could deliver the results Renault Argentina hopes to achieve.

6. NEW APPLICATIONS. According to Sheth, new applications usually involve some sort of functional change in the product. He indicates that a good way to search for new applications is to ask consumers how they actually use the product. An example from the U.S. would be the introduction by a raisin growing cooperative from California, of very small boxes of raisins which mothers could give their children as a snack. In this way, raisins (traditionally sold in the U.S. in one pound boxes, for use by cooks) suddenly became a snack food as well. There is no data in the case supporting the idea that a “new applications” based turnaround strategy will achieve (within the next 12 months) the results Renault Argentina desires.

7. NEW SITUATIONS. Sheth indicates that this strategy requires marketers to seek out different times, places, and/or positioning for product usage. A U.S. example is Sunkist, which has been working for many years (with very limited success, unfortunately) to convince consumers that orange juice is not just a breakfast drink. Again, there is no data in the case supporting the idea that a “new situations” based turnaround strategy will achieve (within the next 12 months) the results Renault Argentina desires.

8. REPOSITIONING. According to Sheth, this strategy involves redefining a product’s image into new usage situations within the same general application context. For example, when Marlboro cigarettes (the first full-length cigarette with a filter) failed to appeal to women (the original target market), Marlboro was repositioned to be the cigarette of choice for rugged, outdoor, male smokers. There is no data in the case supporting the idea that within

the next 12 months a "repositioning" based turnaround strategy will achieve the results Renault Argentina desires.

9. REDEFINE MARKETS. Sheth identifies four alternative approaches to using this strategy: 1) Generic to specialty products; 2) Primary to secondary products; 3) Industrial to consumer products; and 4) Consumer to industrial products. Again, there is no data in the case supporting the idea that a "redefine markets" based turnaround strategy will achieve (within the next 12 months) the results Renault Argentina desires.

APPENDIX 3
CASE DATA RELATING TO THE "GROWTH THROUGH INNOVATION" OPTIONS IDENTIFIED BY SAWHNEY ET AL. (2006)

1) Offerings (i.e., create new products): there is no data in the case to suggest that Renault Argentina is financially strong enough to create new products. Furthermore, the case indicates that the Vice President of marketing is expected to increase sales by 15% within the next 12 months. It seems very unlikely that a new vehicle could be developed and marketed within that time period.

2) Platform (that is, create new offerings by combining common components in different ways): again, it seems unlikely that Renault Argentina would be able to create new offerings within the next 12 months.

3) Solutions (that is, offer integrated solutions to customer problems, not products): there is no data in the case supporting the idea that buyers of new vehicles in Argentina are looking for integrated solutions of some sort.

4) Customers (identify new segments): there is no data in the case supporting the idea that there is suddenly a new segment of vehicle buyers in Argentina.

5) Customer experience (redesign the overall experience of customers): there is no data in the case supporting the idea that redesigning the customer experience is likely to provide the desired 15% increase in sales within the next 12 months.

6) Value capture (create new ways for the company to generate revenue): there is no data in the case supporting the idea that there may be new and different ways for Renault Argentina to generate substantial amounts of additional revenue. Furthermore, and as indicated in the

case, the objective given to the Vice President of marketing is that he should increase sales of vehicles by 15% within the next 12 months.

7) Processes (that is, redesign core processes to increase efficiency and/or effectiveness): again, it seems unlikely that redesigning core processes will allow the Vice President of marketing to achieve this objective, that is, to increase sales of vehicles by 15% within the next 12 months.

8) Organization (change the firm's form, function, or activity scope): there is no data in the case supporting the idea that changing the firms organization is likely to increase sales by 15% within the next 12 months.

9) Supply chain (redesign the firm's sourcing and/or fulfillment activities): there is no data in the case supporting the idea that reworking the supply chain will allow Renault Argentina to increase its sales by 15% within the next 12 months.

10) Presence (create new distribution channels): the case indicates that 9 million consumers in Argentina go to the Internet for information when they are purchasing products, and 5 million consumers in Argentina have actually purchased a product on the Internet. In other words, the data in the case suggest that if Renault Argentina could create a strong presence on the Internet (that is, use the internet as a distribution channel), this might make it possible for the Vice President of sales to achieve the objective (a 15% increase in sales within the next 12 months) which his CEO has articulated.

11) Networking (create network-based intelligent products/services): there is no data in the case supporting the idea that a network-based intelligent products-based turnaround strategy will make it possible for Renault Argentina to increase sales by 15% within the next 12 months.

12) Brand (leverage a brand into new domains): the case provides no data to support the idea that there are new domains into which the Renault brand could be leveraged quickly enough so as to achieve the desired 15% increase in sales within the next 12 months.

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MISSOURI SOLVENTS: MANAGING CASH FLOW

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CASE DESCRIPTION

The primary subject matter of this case concerns managing a firm's cash flow. Case asks students to evaluate a number of proposed alternatives to address a projected cash shortfall as well as develop additional courses of action. A secondary task is an examination of ethical issues associated with managing accounts payable. The case requires students to have an introductory knowledge of general business issues thus the case has a difficulty level of three (junior level) or higher. The case is designed to be taught in one class session of approximately 1.25 hours and is expected to require 1-2 hours of preparation time from the students.

CASE SYNOPSIS

Missouri Solvents is a regional distributor of liquid and dry chemicals. Revenues and profits have grown steadily. The sales growth has required the acquisition of additional fixed assets and current assets. Financing the additional assets has placed a strain on the firm's ability to raise capital. While the company ended last year with a healthy cash balance, there were many occasions during the year that it was necessary to obtain short-term bank loans in order to keep the company operating. As part of the firm's annual planning process, the finance and accounting staff prepare a projected income statement and balance sheet for the coming year. This year, Allen David, the company's chief financial officer, directed Fletcher Scott, the firm's budget analyst, to also develop a monthly cash budget in an effort to identify potential cash flow problems. The cash budget indicated that the company would need additional cash during the second quarter of approximately $2,000,000. Scott reviewed the cash budget with David and since the company's board of directors had expressed concern with the company's increasing use of debt financing, David was reluctant to increase the firm's bank borrowing even for a short period of time. Other alternatives for covering the projected cash shortfall must be evaluated.

INSTRUCTORS' NOTES

Case Overview

Missouri Solvents is a regional distributor of liquid and dry chemicals, headquartered in St. Louis. Growth has been steady with sales and profits have been growing. The sales growth has required the acquisition of additional fixed assets and current assets. Financing the additional assets placed a strain on the firm's ability to raise capital. There were many occasions during the prior year that it was necessary to obtain short-term bank loans in order to keep the company operating. To improve the firm's ability to manage its cash flow, Allen David, the company's chief financial officer, directed Fletcher Scott, the firm's budget, analyst to also develop a monthly cash budget.

The cash budget indicated that the company would need additional cash (additional financing) during the second quarter (April, May and June) of approximately $2,000,000.

Scott reviewed the cash budget with David. The company's board of directors had expressed concern with the company's increasing use of debt financing, thus David was reluctant to increase the firm's bank borrowing even for a short period of time. Other alternatives considered were:

1. Reducing inventory levels.
2. Attempting to collect accounts receivables faster.
3. Delay capital expenditures scheduled for the first half of the year to the second half.
4. Delay paying finance charges or tax payments.
5. Slow payments to vendors (accounts payable).

Income Statements and Balance Sheets for Missouri Solvents (historic and projected) are provided in Appendix 1. Ratios for Missouri Solvents and industry average ratios are provided in Appendix 2.

Case Use

This case may be used in a number of business courses and may be particularly appropriate for accounting and finance courses. Students are asked to evaluate the alternatives considered by David and Scott to handle the cash shortfall. A secondary issue is the ethics associated with delaying payments to vendors.

DISCUSSION QUESTIONS

1. **Assume you are Fletcher Scott. Prepare the report evaluating the alternatives and a recommended course of action. Use ratio analysis to support your evaluations and recommendation.**

Increasing Missouri Solvents' bank debt was not considered an option since the company's board of directors had expressed concern with the company's increasing use debt financing. To effectively evaluate the other options, student must calculate the firm's historic and projected ratios using the financial statements provided as well as the industry average ratios.

Reduce inventory levels. David and Scott both thought this might be possible but David noted the firm already had an ongoing program to systematically review the inventory levels of all items and levels were slowly being reduced.

	2005 Actual	2006 Actual	2007 Actual	2008 Projected	2007 Industry Average
Inventory turnover (times)*	7.67	7.93	8.05	9.02	8.33
Days Invested in Inventory (360 days)**	46.93	45.37	44.73	39.89	43.20
* Sales/360 ** 360/inventory turnover					

Ratios indicate the firm is currently turning its inventory 8 times a year or is carrying about 45 days of inventory and the plan for next year already includes increasing the inventory turns to 9 or reducing the investment in inventory to about 40 days. The three-year trend confirms the statement of David that inventory levels are slowly decreasing. The company's ratios also indicate that Missouri Solvent is turning its inventory more frequently than the industry average. While reducing inventory levels may be possible, the firm does appear to have an effective inventory control system in place. To cover the necessary $2,000,000 short fall, the firm would need to increase its turns to 11 or reduce its days invested in inventory to 33 days. Reducing inventories to this level would most likely be difficult without jeopardizing sales.

Another point against this alternative is that changing a firm's inventory policy will have long-term ramifications and the projected cash shortfall is for only three months.

Attempt to collect accounts receivables faster. David thought it might be possible to increase credit standards and collection effort but it could not be accomplished without a major confrontation with the sales staff. The sales force already feels that they are losing sales because of a conservative approach to granting credit and an overly aggressive collection effort.

	2005 Actual	2006 Actual	2007 Actual	2008 Projected	2007 Industry Average
Average Collection Period (360 days)***	40.17	38.98	38.80	37.29	43.20
***360/(sales/accounts receivables)					

Ratios indicate Missouri Solvent is doing a good job of collecting its receivables. Selling terms are net 30 and average collection period or days sales outstanding is 39 days, below the industry average of 43 days. The plan for next year calls for an additional reduction to 37 days. As with the suggestion of reducing inventory levels, this does not appear to be a likely alternative. Reducing receivables would most likely jeopardize sales.

Changing a firm's credit policy and collection effort will have a long-term impact on sales while the projected cash shortfall is for only three months.

Delay capital expenditures. David felt delaying capital expenditures scheduled for the first half of the year to the second half was not a viable action without reworking the entire financial plan. The projected benefits of the capital expenditures for the first half of the year were included in the sales forecast for the last six months of the year.

Although a total for planned capital expenditures is not given in the case, the actual balance sheet for 2007 and the projected balance sheet for 2008 indicate capital expenditures of $7,700,000. Although David did not think delaying some capital expenditures was workable, this alternative should be given serious consideration. Not all projects are directly related to sales activity or cost reductions, and there is a high likelihood that some projects may be able to be postponed for a few months without serious consequences to the firm's projected results.

This option also had the advantage of not requiring a major change in the firm's current asset investment (accounts receivables and inventories) policy. This alternative would provide a short-term solution to a short-term problem.

Delay paying finance charges or tax payments. The case states that David thought delaying payments to the bank could be arranged but he was reluctant to approach the bank about rescheduling payments. He felt that approaching the bank could cause the bank to be concerned about the firm's ability to manage its cash. The case provides no information regarding Missouri Solvents' relationship with its bank or banks but the case did indicate that the Board is concerned with the firm's increasing debt ratio.

	2005 Actual	2006 Actual	2007 Actual	2008 Projected	2007 Industry Average
Debt Ratio	51.09%	52.66%	56.88%	60.00%	50.48%

David's reluctance to approach the bank may be an indication that the bank may also be concerned with the firm's increasing debt ratio. In either case, this may not be an area that would solve the firm's problem. Total projected interest expense for 2008 is slightly over $1,000,000. The case does not indicate if principal payments are to be made during the year. In either case, this does not appear an alternative that would solve the firm's problem.

Both David and Scott agreed that delaying tax payments was not an option that should be pursued at this time. Delaying tax payments is <u>never</u> a good idea.

<u>Slow payments to vendors (accounts payable)</u>. During the early years of operation, the company was not always able to pay its vendors according to terms. The paying of invoice after the due date resulted in some vendors threatening to stop extending credit to Missouri Solvents. This never happened but the lack of vendor credit would have caused substantial problems. Since that period, a concerted effort has been made to avoid late payments to vendors.

	2005 Actual	2006 Actual	2007 Actual	2008 Projected	2007 Industry Average
AP Deferral Period (days)****	31.09	31.33	29.58	26.68	35.17
****Accounts payables/(cost of goods sold/360)					

The company's current accounts payable deferral period is 27 days, compared to an industry average of 35 days.

To cover the necessary $2,000,000 shortfall, the firm would need to increase its AP Deferral Period to approximately 35 days. David thought slowing vendor payment by 10 days for a few months was possible. He thought it was likely the vendors wouldn't notice a change in Missouri Solvents payment pattern. Temporarily delaying payments to 35 days would the advantage of not requiring a major change in the firm's current asset investment policy and have no impact on sales. This alternative would provide a short-term solution to a short-term problem.

Another option not mentioned in the case and associated with accounts payable is to meet with key vendors and request extended payments terms for 3-4 months. This would allow the firm to handle its short-term cash problem without delaying payments and risking irritating the firm's suppliers.

Recommendation: The first option would be to delay those capital expenditures that will have minimal impact on sales and operating expenses, but this action alone may not provide the cash necessary to bridge the shortfall. The second option would be to approach selected suppliers to request temporary extended credit terms. As mentioned previously, this approach would allow the firm to handle its short-term cash problem without delaying payments and risking irritating the firm's suppliers.

An argument could be made to temporarily slow the payments of vendor invoice without asking for extended credit terms. This alternative would risk upsetting vendors, but, based on comments from David, the risk would be small.

Changing the firms inventory or credit management policies would not be an attractive solution because the change would have a long-term impact on the firm's sales. Missouri Solvents is facing a short-term problem.

2. Would your recommendation change if the projected cash shortfall was for six or nine rather than three months?

If the projected shortfall was for six or nine months rather than three month, the recommended course of action could change, but probably not much. Delaying capital expenditures would still be an option but given the time period of the shortfall (six to nine months), it would essentially be delaying some projects for most of the year. Suppliers would be less likely to agree to extended credit terms for six to nine months than three months.

Slowing payments with permission from vendors would become a more viable option. As stated previously, to cover the necessary $2,000,000 shortfall, the firm would need to increase its AP Deferral Period to approximately 35 days. This would match the industry average. David thought it was likely the vendors wouldn't notice a change in Missouri Solvents payment pattern. He is probably correct. Delaying payments to 35 days would have the advantage of not requiring a major change in the firm's current asset investment policy and have no impact on sales. This alternative would provide a short-term solution to a short-term problem.

3. Is it ethical to delay payments to vendors beyond the agreed upon terms?

One way to approach an analysis of the ethics of this decision is to utilize ethical theories. Teleological and deontological are the most common categories of ethical theories used to analyze the ethics of conduct. Teleological ethics is concerned with outcome; an action is right if it promotes the best consequences. Utilitarian theory, where costs and benefits are compared in order to arrive at the optimal solution, is the most often used teleological theory in business ethics. Deontologist are concerned with motive, not outcome, and judge an action according to whether or not it is the right thing to do. An action is right if it is in accordance with a moral rule or principle.

Using utilitarian theory may be difficult in practice because of the difficulty of measuring costs and benefits. In this case, a Utilitarian analysis has been conducted in a general sense, as the costs and benefits of each alternative have been considered, although actual dollar costs and benefits are not assigned. The benefits of each alternative (that is, covering the projected cash shortfall) seem to be approximately equal, except for the delay in capital expenditures, which may not be sufficient to cover the shortfall. If benefits are approximately equal, then utilitarian analysis will be based on differences in costs. The costs of reducing inventories or a faster collection of accounts receivable include possible loss of sales, and the use of a long term solution for a short term problem. A delay in capital expenditures carries the cost of reworking the entire financial plan, but it does provide a short –term solution to a short-term problem. A delay in paying finance charges carries with it the cost of a loss in bank confidence, especially since there has been a significant increase in the firm's debt ratio since 2005. Delaying tax payments is not an option; costs are prohibitively high. This leaves the final alternative, which is to slow payments to vendors for a few months. The cost of doing so would be to irritate the vendors, but the risk appears to be small. From a Utilitarian perspective, weighing costs against benefits, this would be the optimal solution.

For Immanuel Kant, the most well-known deontologist, an action is ethical if it is done for the sake of duty. According to Kant's First Categorical Imperative, one must "act as if the maxim of your action were to secure through your will a universal law of nature." In order for an action to be ethical, it must past the "universalizability" test; that is, the action must be one that we would want everyone to do. According to deontologists, deferring payments to vendors beyond agreed upon terms would be unethical. Promises must be kept because a world in which no one kept promises would be unacceptable. Kant's Second Categorical Imperative states that one must "always act so as to treat humanity, whether in your own person or that of another, as an end in itself, never as a means only." One must treat others with respect. A deontologist would find meetings with key vendors to ask for an extension of payment terms to be a more ethical solution to the cash flow problem.

Another way to analyze the ethics of this case is with the Stockholder v. Stakeholder models of corporate social responsibility. According to the Stockholder model, the most important consideration is return to the owners of Missouri Solvents. Managers have a moral obligation to maximize the return to the shareholders. Therefore, deferring payments to vendors would be acceptable as long as the vendors did not respond by cutting off supplies of vital products. Again, David believes the risk of this is small.

In the Stakeholder model, suppliers are one of six stakeholders that have an interest in the operations of the corporation. In a socially responsible corporation, the goal of managers is to harmonize the interests of these stakeholders. Advocates of the stakeholder model would be more likely to favor the deontological alternative, that is, to meet with key vendors to ask for an extension of payment terms as a solution to the cash flow problem.

Appendix 1

Missouri Solvents
Income Statement ($000)

For the Year Ended December 31, 2007

	2005	2006	2007	Projected 2008	Industry Average 2007
	$	$	$	$	$
Sales revenue	67,700,000	79,200,000	89,200,000	99,200,000	100,000,000
Less: Cost of goods sold	59,400,000	70,100,000	79,100,000	87,700,000	87,000,000
Gross profits	8,300,000	9,100,000	10,100,000	11,500,000	13,000,000
Less: Operating expenses					
Selling expense	3,100,000	3,280,000	3,480,000	3,880,000	3,500,000
General and administrative expenses	1,700,000	1,825,000	2,025,000	2,325,000	2,400,000
Depreciation expense	1,150,000	1,550,000	1,750,000	2,050,000	2,000,000
Total operating expense	5,950,000	6,655,000	7,255,000	8,255,000	7,900,000
Operating profits	2,350,000	2,445,000	2,845,000	3,245,000	5,100,000
Less: Interest expense	855,000	895,000	925,000	1,025,000	700,000
Net profits before taxes	1,495,000	1,550,000	1,920,000	2,220,000	4,400,000
Less: Taxes (rate = 40%)	598,000	620,000	768,000	888,000	1,760,000
Net profits after taxes	897,000	930,000	1,152,000	1,332,000	2,640,000
Dividends	100,000	100,000	100,000	100,000	400,000

Balance Sheet ($000)
As of December 31

Assets	2005	2006	2007	Projected 2008	Industry Average 2007
	$	$	$	$	$
Current assets					
Cash	220,000	215,000	265,000	190,000	400,000
Accounts receivable	7,555,000	8,575,000	9,615,000	10,275,000	12,000,000
Inventories	8,825,000	9,982,000	11,082,000	10,992,000	12,000,000
Total current assets	16,600,000	18,772,000	20,962,000	21,457,000	24,400,000
Gross fixed assets	32,650,000	34,800,000	40,100,000	47,800,000	35,000,000
Less: Accumulated depreciation	18,375,000	19,925,000	21,675,000	23,725,000	18,000,000
Net fixed assets	14,275,000	14,875,000	18,425,000	24,075,000	17,000,000
Total assets	30,875,000	33,647,000	39,387,000	45,532,000	41,400,000

Liabilities and Stockholders' Equity	2005	2006	2007	Projected 2008	Industry Average 2007
	$	$	$	$	$
Current liabilities					
Accounts payable	5,130,000	6,100,000	6,500,000	6,500,000	8,500,000
Notes payable	2,210,000	2,270,000	2,870,000	2,070,000	2,700,000
Accruals	560,000	412,000	470,000	666,000	700,000
Total current liabilities	7,900,000	8,782,000	9,840,000	9,236,000	11,900,000
Long-term debts	7,875,000	8,935,000	12,565,000	18,082,000	9,000,000
Total liabilities	15,775,000	17,717,000	22,405,000	27,318,000	20,900,000
Stockholders' equity					
Common stock (at par)	7,200,000	7,200,000	7,200,000	7,200,000	8,500,000
Retained earnings	7,900,000	8,730,000	9,782,000	11,014,000	12,000,000
Total stockholders' equity	15,100,000	15,930,000	16,982,000	18,214,000	20,500,000
Total liabilities and stockholders' equity	30,875,000	33,647,000	39,387,000	45,532,000	41,400,000

Appendix 2					
Historical Ratios Missouri Solvents					
	Actual	**Actual**	**Actual**	**Projected**	**Industry Average**
Ratio	**2005**	**2006**	**2007**	**2008**	**2007**
Current ratio	2.10	2.14	2.13	2.32	2.05
Quick ratio	0.98	1.00	1.00	1.13	1.04
Inventory turnover (times)	7.67	7.93	8.05	9.02	8.33
Days Invested in Inventory (360)	46.93	45.37	44.73	39.89	43.20
Average collection period (360 days)	40.17	38.98	38.80	37.29	43.20
Fixed (net) asset turnover (times)	4.74	5.32	4.84	4.12	5.88
Total asset turnover (times)	2.19	2.35	2.26	2.18	2.42
AP deferral period (days)	31.09	31.33	29.58	26.68	35.17
Debt ratio	51.09%	52.66%	56.88%	60.00%	50.48%
Times interest earned ratio	2.75	2.73	3.08	3.17	7.29
Gross profit margin	12.26%	11.49%	11.32%	11.59%	13.00%
Net profit margin	1.32%	1.17%	1.29%	1.34%	2.64%
Return on total assets (ROA)	2.91%	2.76%	2.92%	2.93%	6.38%
Return on equity (ROE)	5.94%	5.84%	6.78%	7.31%	12.88%

HRM CASE STUDY: DIVERSITY MANAGEMENT: FACILITATING DIVERSITY THROUGH THE RECRUITMENT, SELECTION AND INTEGRATION OF DIVERSE EMPLOYEES IN A QUEBEC BANK

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CASE DESCRIPTION

This case focuses on the illustration and application of HRM workplace diversity management concepts. First, students will have to discuss the advantages of a diverse workforce and the steps involved in diversity management. Next, they must critique the HRM director's diversity plan. They will then be required to design and implement HRM practices in order to facilitate the recruitment, selection, integration and development of diverse employees. Finally, students will propose measures that evaluate the effectiveness of these HRM diversity practices.

The case has a difficulty level of 4 to 6: it is appropriate for HRM courses from senior level to second year graduate level (M.Sc. and MBA courses in HRM, staffing). Students are expected to prepare the case before coming to class. The case is designed to be discussed in one class of 3 hours. This fictitious pedagogical case was inspired in part by the real-life experiences of HR and employment equity managers in various Canadian organizations. The authors interviewed or met these individuals during the second author's seminars on diversity.

CASE SYNOPSIS

In this case, participants will examine the situation of Françoise Roy, HRM manager of a bank in Quebec, Canada. Françoise had only been director of human resources at the People's Bank of Quebec (PBQ) for a little over a year when she undertook a huge project This effort entailed encouraging diversity in the bank by increasing ethnic and cultural minority representation and by eliminating discrimination among the workforce. The Human Rights Committee had approved her action plan regarding employment equal opportunity. In order to achieve her goals, Françoise must now design and implement a workforce diversity action plan.

In this case study, students will first discuss the advantages of a diverse workforce and the steps in diversity management. Next, they must critique the HRM director's diversity action plan. They will then have to design and implement HRM practices in order to facilitate the recruitment, *selection, integration and development of a diverse workforce. Finally, students will be required to propose measures used to evaluate the effectiveness of these HRM diversity practices.*

INSTRUCTOR'S NOTES

Questions and Discussion

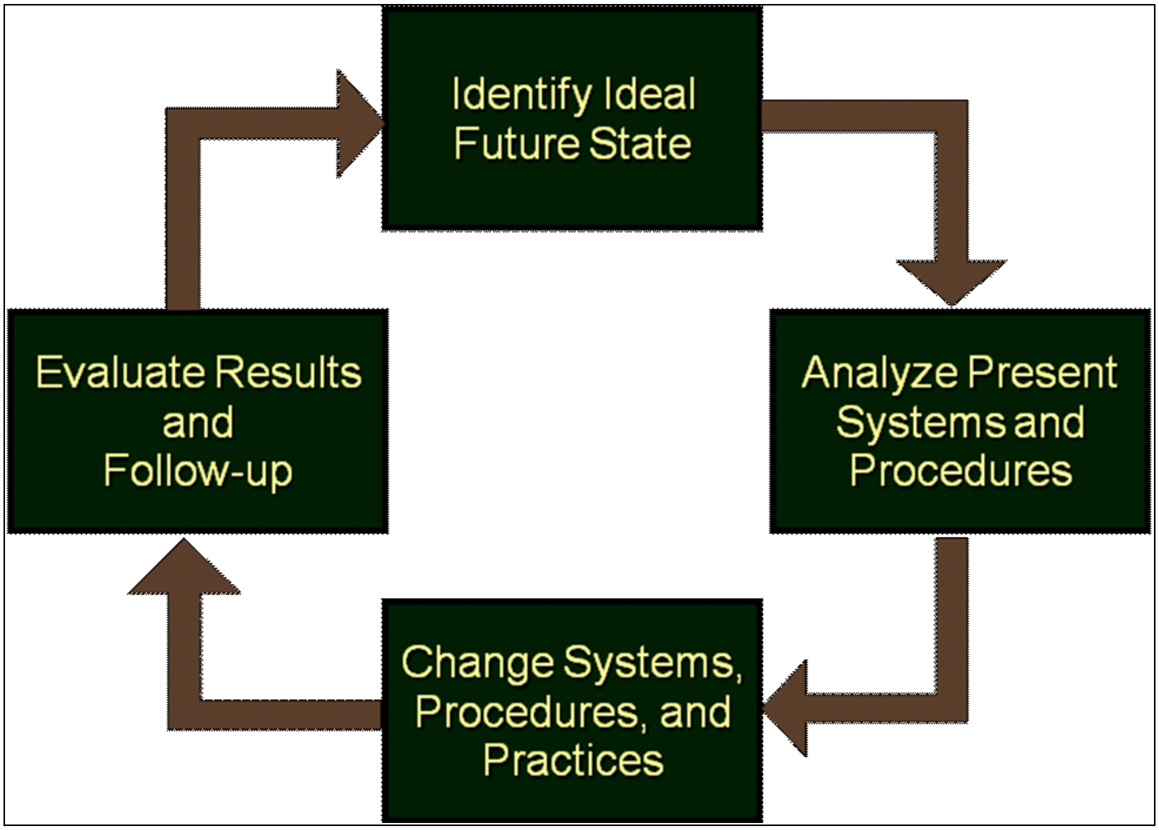
1. What are the advantages of a diverse workforce?

In business terms, diversity can be defined as a set of differences of individual traits including socio demographic variables and professional variables, which can be found in an organization's various levels (Thomas, 1991; Cox, 1991). Core dimensions of diversity include age, ethnicity and culture, gender, race, religion, sexual orientation, and capabilities (Schwind, Das, and Wagar, 2007). Secondary dimensions include education, status, language, income levels, etc.

Many North American companies take measures to better handle diversity, seeing an opportunity to enhance their future growth and to develop a competitive advantage (Roberson & Park, 2007; Thomas & Wetlaufer, 1997; Wentling & Palma Rivas, 1998). The advantages of a diverse workforce, representative of today's society, are numerous. First of all, a diverse workforce allows better service to customers, who are diverse as well, and it enhances the image and the credibility of the organization (Thomas & Ely, 1996). In addition, a diverse workforce increases productivity, facilitates innovation, and enables resolution of problems (Davis, 2000). Furthermore, hiring a workforce that doesn't represent society will lead to repercussions that are harmful to the social and economic plans of that society (Samuel et al.,. 1997). In any case, understanding and managing diversity is crucial for organizations, given the current changes in the cultural and ethnic attributes of the workforce (Richard, Murthi, & Ismail, 2007).

2. What are the steps in managing diversity?

Das (1998) identifies four steps in managing diversity, explained below.



1. Identify current and ideal future state. This step begins with the identification of current workforce composition i.e. age, gender, ethnicity, education, and disability (may also include language, race, parental status, marital status, etc.). Surveys, focus groups, and employee interviews are then conducted to identify present and ideal future states at work.

2. Analyze present systems and procedures. Examine current policies, systems, practices, rules and procedures to determine their validity and fairness for a diverse workforce (e.g., work assignments, recruitment and selection, orientation, performance management, etc.).

3. Change policies, procedures, and practices. Important elements at this step are the four following points:

   -*Senior management commitment*, one of the most important elements for ensuring the success of diversity efforts.

-*Establishment of a diversity committee* to oversee diversity efforts, design and implement diversity management practices, and serve as a communication link. This committee should represent all employee groups, i.e., occupational groups, geographic locations, age, etc.

-*Education and training*. Training and education on the importance of diversity needs to be provided to all employees at all levels in the organization. A variety of training techniques can be used to sensitize workers to varying cultural values and norms.

-*Wide communication of changes*. Information, changes in internal systems and procedures must be communicated to all employees.

4. Evaluate results and follow-up. This step involves monitoring progress on a systematic basis and communicating quantitative (e.g. number of hires, promotions, absenteeism, turnover, grievances, etc.) and qualitative (e.g. work climate feedback) indices.

3. Critique Françoise' S Diversity Action Plan.

Certain elements of Françoise's plan do not seem to be in a logical order, while others are missing. The following issues need to be addressed:

An information campaign targeting all managers and employees should be launched very early in the process. This campaign would focus on the importance of diversity, on the Bank's intentions, on the current situation in terms of diversity and on the Bank's objectives (this element is present in Françoise's plan, but is chronologically misplaced). This campaign would illustrate the Bank's commitment to change. For instance, the CEO could address employees directly, giving a talk on the importance of diversity, its advantages, the importance for the Bank of establishing and implementing diversity policies and objectives, the launch of a survey to assess the current situation and the upcoming development of a program for promoting diversity. It is crucial that the communication of policy to employees and managers be implemented at the beginning of the process, rather than at the end.

Current and future desired states should then be identified. The current situation should be assessed in terms of diversity and organizational culture. This assessment could include a survey among employees to measure their attitudes toward diversity and their satisfaction regarding the current situation, in terms of diversity, at the Bank. The desired state and the diversity objectives would then be determined, taking into consideration the « starting point » revealed by this assessment.

Current HRM policies, practices and procedures should be analyzed to determine their validity and fairness for a diverse workforce (e.g., work assignments, recruitment and selection, orientation, performance management, etc.).

A Diversity Committee should be formed, and a diversity manager - which could be the HR Director herself - should be appointed (missing elements). This diversity director and diversity committee would be responsible for the direction and coordination of all the diversity efforts and changes.

The HRM policies and programs should then be (re)defined, and developed/modified in collaboration with the line managers and employees (missing element). Indeed, in a context where the organizational culture is not particularly favorable to the proposed changes, communication, consultation and involvement of employees and managers are key. In this design and development step, the diversity committee (in collaboration with the banks' employees and managers) should also decide which indicators will be measured to evaluate the implementation and effectiveness of the diversity policies and practices.

Once the policies have been developed, managers will have to be trained (this element is present in the plan, but is chronologically misplaced) as well as employees (missing element), prior to implementation.

The following step is the implementation of the diversity policies and programs throughout the organization (this element is present in the plan, but is chronologically misplaced).

Finally, progress and results will be measured (missing element). After a reasonable delay - from a few months to a year, depending on the programs or policies - employees and managers should be asked to provide feedback, show cognitive increase, behavior change and effective practical results. Programs and policies may then be adapted and modified accordingly.

Throughout the change process, it will be crucial to emphasize bidirectional, open and transparent communication, with all employees (not emphasized enough in Françoise's plan).

For a conceptual overview, see Shen, Chanda, D'Netto, & Monga's (2009) diversity management framework.

Topic 1: The Recruitment of a Diverse Workforce

4. What recruitment practices would you introduce to facilitate the internal and external recruitment of a diverse workforce?

5. What measures/indicators would you use to evaluate the progress and effectiveness of these practices?

During recruitment of minority employees, organizations face two major challenges. The first one is to reach the minority group members who meet the position's selection criteria. Often, these minority groups don't use the same networks as the majority groups. The second challenge is to get those potential candidates to submit their applications. Unfortunately, many companies are unaware that they are reflecting an image of homogeneity, while other companies must deal with the fact that, in certain spheres, their industry is poorly perceived. (Waxin, Panaccio, 2004; Waxin, 2008).

FACILITATING INTERNAL RECRUITMENT OF A DIVERSE WORKFORCE

To facilitate the internal recruitment of diverse employees, Waxin, Panaccio (2004) and Waxin (2008) propose three useful practices:

The systematic use of internal job postings, for all job openings. The diversity team should establish a clear job posting policy and explain to managers and recruiters the importance of posting job openings internally first. Possible evaluation measures could be: 1) the ratio of job openings posted internally and externally, 2) the numbers of internal applicants per internal job posting, and 3) the number of internal applicants effectively hired based on internal job posting, per year. Line managers and recruiting officers should be evaluated on their proper use of the new job posting policy.

The creation of an internal database/skills inventory. The bank can create an internal database or skills inventory that could be used to identify the internal candidates for promotion or advancement. This database should contain information on employee qualifications, competencies, skills, experiences, performance records and motivations. It will help recruiters identify internal candidates who best fit the job specification to fill the vacancies, including those who were not considering applying for the job. If necessary, the bank can also train previously pre-selected candidates in order to develop them for their next career move.

The implementation of this internal skills inventory requires the establishment, in collaboration with line managers, of the list of variables/data that will be included in this database. It also requires training line managers and recruiters on the importance and use of this internal data bank, and giving recruiters and managers access to this database. Regular update to this database will be necessary. Finally, the use of this database for any future recruitment should be mandatory.

Possible evaluation measures could be the number of minority applicants in the database, and the number of employees recruited internally using this database (for the company as a whole and for individual departments separately). Recruiters should be evaluated on the proper use of this data base.

Redesign of the referral system. If the bank is already using a reference and recommendation system, it's important to make sure that these systems are not discriminatory. In fact, referral systems can easily lead to direct or indirect discrimination. If the bank doesn't have a referral policy yet, one can be introduced, while making sure it's not discriminatory.

Implementation would require defining the referral policy, informing managers and employees on the objectives, importance and use of this policy, restating the organization's commitment towards equality in all the company's calls for referrals, and approaching employees that are members of minority groups for referrals.

Possible evaluation measures could be the number of minority candidates received following a call for referral, and the number of minority candidates hired through referrals (for the company as a whole and for departments individually). Recruiters should be evaluated on the proper use of this policy.

FACILITATING EXTERNAL RECRUITMENT OF A DIVERSE WORKFORCE

To facilitate the external recruitment of diverse employees, Waxin, Panaccio (2004) and Waxin (2008) propose four useful practices:

Analyzing and improving the image/reputation of the company. The reputation of the bank as an equal opportunity employer will help the bank attract highly qualified candidates. The bank should then advertise their plan to increase minority representation among its employees, and outside the organization, to change the misconception of homogeneity.

The implementation of this initiative would require the formation of discussion groups to better understand the image the bank is currently projecting, to include members of minority groups in promotional documents, to involve these individuals in social events, to train and send them to recruiting events, and to invite representatives of external minority groups to visit the offices and meet the bank directors.

To measure the effectiveness of this initiative, the bank could measure the image it projects as a minority employer by conducting surveys among the clients or applicants during job interviews, follow up regularly and compare the yearly results.

Orienting external advertising campaigns towards the targeted communities. Implementation of this initiative would require a review of all advertisements in order to eliminate all signs of ethnic or cultural discrimination, to add a statement confirming that the company supports equal opportunity in employment., to publish the advertisement in media available to minority groups (magazines, radio, television, Internet sites, etc..), and include minority members in advertisements, flyers, films, etc.

Possible evaluation measures could be the number and quality of such initiatives, the number of applications received per advertising campaign, and the number of employees hired through the different types of media.

Developing relationships with communities of minority members. Direct contact with minority communities is an effective way of delivering the job posting information to them. The implementation of this initiative would require 1) developing a network of connections with diverse groups and targeted communities, 2) broadcasting employment opportunities through these communities, and 3) organizing various activities along with those community groups, like the mentoring of students or trainees by bank managers. On a regular basis, the bank could also organize conferences and meetings with members of these community groups, or join radio and television shows that are popular among minorities.

Possible evaluation measures could be the number and quality of the relationships developed or maintained each year, the number of applications received through this network, and the number of minority members who were hired through this network.

Developing strong relationships with educational institutions having high ratios of minority student enrollment. The implementation of this initiative would require developing relationships with certain educational institutions, sending minority representatives to these schools during career fairs, training all bank employees involved in these events, and organizing internships and summer jobs for minority group members.

Possible evaluation measures could be the number of educational institutions involved, the number of applications received through this program, as well as the number of minority candidates effectively employed through this program.

Topic 2. The Selection of Employees to Promote Diversity

6. What selection practices would you introduce to facilitate the selection of minority employees?

7. What measures/indicators would you use to measure the progress and effectiveness of these practices?

Follow-up questions: What are the key elements of a standard selection process? What new ideas should the bank adopt and what should managers pay close attention to in order to facilitate the selection of minority employees?

The main diversity challenge at the selection stage is the elimination of the discriminatory factors that may affect the selection process: these factors are related to conscious and unconscious stereotypes held by those evaluating the candidates, and to the structural elements of the selection process (selection criteria, selection interviews and tests). Based on a literature review, Waxin, Panaccio (2004) and Waxin (2008) list best the practices that support the selection of diverse employees.

Composition of the selection panel. The selection panel responsible for identifying the best candidates should include representatives of minority groups (Thomas & Wetlaufer, 1997). The implementation of this initiative would require setting goals for the representation of minority groups in the selection panels, identifying members of minority groups among current employees, approaching and training them to become members of the selection panel. If the organization doesn't have enough minority employees willing to serve as members of a selection panel, the company could invite minority members from external organizations.

Possible evaluation measures could include the number of members of the selection panel that are also members of minority groups.

Training the selectors on diversity. The staff involved in the selection process should be educated or trained on the diversity related legislation, human rights and the importance of workforce diversity. They should be made aware of the cultural differences and the best ways to handle those differences, the existence and effects of stereotypes and the ways to avoid them.

To evaluate the effectiveness of such a program, the training team could measure the satisfaction of the trainees, their increase in cognition on diversity related issues (quiz), the change in their behavior, the number of selectors trained in diversity, and the numbers of minority employees employed by those trained selectors.

Identifying non discriminatory selection criteria. The bank must ensure that for each job opening, there is a clear and non-discriminatory job description and job specification, and that the selectors are made aware of the technical and managerial skills required for each position to be filled. The selection criteria for each job opening must be fair, valid, relevant and job-specific.

Possible evaluation measures could be the percentage or number of positions for which the job description and specifications have been checked by the diversity specialists and found consistent.

Using selection methods that enhance diversity. The North-American private sector has set innovative techniques regarding selection methods that enhance diversity. Before proceeding to interviews, selectors could make sure that they have at least one candidate from a minority group (Thomas & Wetlaufer, 1997). Well-structured interviews offer the most objective comparison means possible. One Canadian bank that has been successful with its selection methods uses situational and behavioral interviews instead of asking questions related to typical Canadian work experiences (Samuel et al. 1997). That way, even if the candidates have no previous work experience, they are questioned on how they would handle certain difficult situations, thus giving selectors a clear idea of their behaviors and problem solving techniques.

Possible evaluation measures could be the number of minority candidates interviewed; and the number of minority candidates hired (by job category, by department and for the entire company).

The difficulty of recognizing past achievements of foreign applicants (experience and skills). Members of minority groups and ethno-cultural communities are more likely to be under-employed or over-qualified for the positions they hold (Iverson, 2000). Their capabilities and skills are more likely to be under-used and their achievements, unappreciated, because their employers tend to underestimate foreign academic programs and accomplishments realized in their home country. In order to get around the difficulties of evaluating the validity of work experience in a foreign country for a certain position, emphasis must be put on evaluation of skills using other means, whether it be competency, behavior-based interviews or tests (job samples, performance, simulation tests). The implementation of this initiative would require the development of a policy for recognition of foreign achievements and experience for minority employees. This policy should be applied to all internal and external applicants.

The effectiveness of this initiative could be measured by surveying employees from minority groups and measuring their perceptions that past achievements and experiences have been recognized for their true value.

It is important that the recruitment-selection team reports to the diversity manager and those in charge of diversity management, and that the evaluation of their performance is based on taking the right measures to meet the diversity goals.

Topic 3. The Integration and Development of a Diverse Workforce

8. What HRM practices would you introduce to facilitate the integration and development of diverse employees?

9. What measures/indicators would you use to measure the progress and effectiveness of these practices?

Designing and implementing an orientation program. The bank must put together an orientation program for all employees. The program will cover areas such as the organization's mission, vision, values, code of conduct, diversity management practices, etc. This program must also include the introduction of new employees to their supervisors, co-workers, and people they need to work with. To make the orientation of minority employees easier, the following information must be provided to all new employees: company policies regarding diversity, zero discrimination tolerance, legislation regarding equity and discrimination at the workplace, rights of employees who believe themselves to be victims of discrimination or harassment due to being members of a minority group, and the way to report any misconduct. It is also important to include a follow-up "integration meeting", for example three months after the initial orientation program, so they can discuss the difficulties encountered and find solutions. An "orientation kit" should be handed out to all new employees.

To evaluate the effectiveness of this initiative, one could use a satisfaction survey to be filled by all new employees just after the orientation program and then six months after hiring, comparing satisfaction rates across time and across employee categories. Retention rates of minority employees relative to all employees, one year and two years after hiring (by department and for the entire organization) should also be examined.

Designing and implementing a mentoring system. A mentoring program will facilitate the integration and development of all employees. Mentors must be selected based on their responsibilities and interest in mentoring, and must be trained on the importance of diversity.

The implementation of this initiative would require designing a mentoring policy, identifying and soliciting potential mentors, evaluating the records of volunteering mentors, training the selected mentors, matching them with mentees, and organizing the follow-up activities.

Possible evaluation measures could be the number of pairs of mentor/mentees, satisfaction rates of the mentors and mentees, and the performance records of the mentees.
Training the supervisors. Supervisor support is significantly related to the development and vertical mobility of their subordinates. In addition to dealing with the issue of diversity, the supervisor training must include the following aspects (Deslandes, 2002).

Giving feedback. Feedback has great impact on the satisfaction, motivation and performance of employees. Members of minority groups tend to receive less feedback than members of majority groups. Supervisors must be trained to give constructive, continuous feedback.

Suggesting interesting tasks as sources of personal development. Employees who are members of minority groups may receive unfair access to training courses, due to the lack of support from their superiors. Supervisors must be encouraged to use the skills of all their employees in optimum ways.

Advising employees on their career. Members of minority groups receive less guidance from their supervisors than their colleagues who are members of majority groups. Supervisors have a tendency to not support the promotion of members of minority groups for fear that it might weaken their own credibility.

Implementation of this initiative would require designing and implementing a training program and establishing a formal evaluation and rewards policy for the supervisors. The supervisors should be evaluated by their employees on several points: quality and frequency of feedback received, optimal utilization of the employees' skills and competencies, quality of their advice on training, development and career management issues. The level of satisfaction among diverse employees regarding the support offered to them by their supervisors should also be assessed.

Eliminating the discriminatory biases in the performance management process. Performance appraisal is a key factor for determining salary increases in many organizations. According to the *self-categorization* theory, supervisors tend to support members of their own group rather than those of other groups. Performance objectives must be specific, clear, realistic, relevant, measurable, and well communicated. The biases which may influence yearly performance evaluation interviews are the same as those at work during the selection interviews. Implementation of this initiative would require designing and implementing a training program for managers on performance evaluation and management.

Possible evaluation measures would include surveying employees on their satisfaction regarding the evaluation process and comparing performance levels/records of minority group employees to the rest of the employees (for each department and for the company as a whole).

To conclude, the professor can ask the students to develop a new diversity plan, which would include the practices discussed above.

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WAL-MART: GETTING BACK TO GROWTH OLD GUARD VS. CHANGE AGENT CONFLICT AND THE IMPACT ON GROWTH

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CASE DESCRIPTION

The primary subject of the case is the development of a marketing strategy for Wal-Mart to improve "same store" U.S. sales growth during 2006-07. Wal-Mart must identify new growth opportunities and develop strategies to attract those consumer groups to Wal-Mart. Complications arise when Wal-Mart goes outside the retail industry for its marketing talent, resulting in a clash of values. There are conflicting managerial views of strategy implementation. The proposed strategy of upgraded merchandise and value pricing is resisted by the "old guard" strategy of selling large quantities of average merchandise at low everyday pricing. In addition, continual negative press presents additional marketing challenges to overcome.

The case has a difficulty level of undergraduate seniors in marketing strategy, retailing, market research, and master's level course in managerial marketing or business strategy. The case is designed to be taught in one class and can be taught in one of two ways. Students can be divided into teams of four students to prepare a case analysis defining the problem, developing alternative solutions, and providing a recommended solution and course of action. A second method is to use the end questions as a springboard for the case class discussion. For either alternative, the case can be taught in one and a half hours. Student preparation time should be expected to be eight hours in total for the group, about two hours per student. On an individual basis, a student should be able to read the case and complete the case questions in three hours.

CASE SYNOPSIS

Wal-Mart has been successful in opening retail discount mass merchandising stores across the United States, mainly in smaller, rural cities, where limited competition exists from small mom and pop retailers. As part of growth plans, Wal-Mart began opening stores in larger, suburban and urban areas and now faced competition from Target and other specialty retailers. Soon, same stores sales growth slowed and growth from new stores was limited by many communities objecting to Wal-Mart locating stores in their town.

Management was concerned whether the low price strategy could sustain growth. Several managers were hired to craft a new strategy moving away from price into more stylish fashion and "value propositions." The fashion initiative failed and management brought in outside marketing people to select a new advertising agency to attract upper income shoppers to Wal-Mart, a difficult strategy given the current Wal-Mart customer was lower income. Conflicts soon arose within Wal-Mart on strategy changes with merchandising and marketing departments having different views on products and pricing. Complicating the problem was the fact new marketing people were culturally different than the old time Wal-Mart staff. Wal-Mart's negative imagine in the community presented additional marketing challenges. After conducting market research on current and potential customers, management faced product, pricing, and customer target decisions in a new competitive environment.

This case was prepared solely to provide material for class discussion. The authors did not intend to illustrate either effective or ineffective handling of a managerial situation.

INSTRUCTORS' NOTES

Case Objectives

The objectives of this case include:

- ♦ To have students understand the capabilities and strategies leading to a firms' success can be vulnerable to a changing competition and business environment.
- ♦ To have students learn that a firms' marketing strategy of expanding beyond its core customer base to a different or additional customer base is challenging and can conflict with existing customers.
- ♦ To have students appreciate that company culture and organizational structure can enhance marketing plans and strategies or possibly stand in the way of accomplishing change.
- ♦ To have students recognize that competing marketing ideas within a firm are useful in debating strategy and plans, but once a plan is decided, all functional areas must support and execute it without reservation.
- ♦ To have students realize that a highly integrated price proposition alone may not be sufficient to sustain growth and that not every customer responds to price alone.

- ♦ To have students recognize that a firms' corporate citizen image can negatively impact sales growth.

Assignment Questions

1. What were the critical factors that led to the early success and growth of Wal-Mart?
2. Why did Wal-Mart see the need to change strategy?
3. How has Wal-Mart's negative image affected the business? Should this be a concern for the marketing department or public relations department?
4. Wal-Mart attempted to attract higher income customers with its Metro 7 line, upgraded televisions, and adding more stylish merchandise. Do you agree with this change? What are the risks to current customers?
5. Describe Wal-Mart's relationship with its current suppliers. If Wal-Mart wants to upgrade its image by sourcing product from major name brands in fashion, what might Wal-Mart face in trying to do business with these suppliers?
6. How well did Roehm and Womack fit into the Wal-Mart culture? How did Wal-Mart culture and organizational structure influence marketing and merchandising decisions?
7. Describe how you might go about selecting a new ad agency. How would you have conducted the selection process? What was the rationale for selecting DraftFCB? Why might the "old guard" at Wal-Mart be resistant to Draft?
8. Going forward, what can Wal-Mart do to improve same store sales?

Teaching the Case

Since most students will have experience in shopping in Wal-Mart, instructors might find it interesting to start the case asking students to compare shopping at Target versus Wal-Mart. Students will probably offer comments on the Wal-Mart pricing but then the differences in look, feel, and merchandise mix will probably surface. This could be followed by the question, "What types of merchandise would you not expect to find at Wal-Mart?" Then move into the assigned questions.

1. What were the critical factors that led to the early success and growth of Wal-Mart?

Wal-Mart built a strategy around low cost so as to provide low price and wide selection to customers.

- ♦ Stores were located in rural areas where real estate was relatively inexpensive and competition weak. There were no large retailers, only small, local mom and pop stores that could not compete on price or assortment.
- ♦ Products were sourced in China and other low cost countries to keep Wal-Mart prices low. Major name brand fashion items were not sold by Wal-Mart.
- ♦ Wal-Mart put enormous pressure on US suppliers, squeezing them for low prices.
- ♦ The company built a sophisticated computer based logistics and distribution system to efficiently move goods and reduce costs. These cost reductions enabled Wal-Mart to successfully balance both a low price strategy and a fair return on investment to the shareholders.
- ♦ Wal-Mart kept wages and benefits low primarily using part-time help in the stores. Health and other benefits were limited and part-time employees did not qualify for benefits.

2. Why did Wal-Mart see the need to change strategy?

- ♦ Same stores sales have matured and are flat and achieving same store growth has become increasingly difficult. The lower income Wal-Mart customer was unable to take the store to the next level by buying more expensive merchandise.
- ♦ New stores in urban areas are more expensive to start-up with higher real estate costs, taxes, and other retailers willing to bid high for scarce, quality retail space. Target was also established in many of the suburban communities Wal-Mart sought to enter.
- ♦ Local communities fought against the opening of Wal-Mart stores trying to protect local retailers. This caused negative publicity against Wal-Mart and increased costs in legal fees to try to locate stores.
- ♦ Wal-Mart came under intense criticism from labor unions and other organizations tarnishing the image of the retailer and causing some consumers to avoid buying in Wal-Mart.
- ♦ Competition heated up.
    - o Target combined low prices with more fashionable merchandise and a better shopping experience drawing potential middle and upper income customers from going to Wal-Mart.
    - o Other retailers learned to compete with Wal-Mart by offering competitive prices with additional services not matched by Wal-Mart.
    - o The "stack-em high, sell-em cheap" unsegmented message may have lost its saliency in light of competitors selling name brand assortments and shopping experiences.

3. How has Wal-Mart's negative image affected the business? Should this be a concern for the marketing department or public relations department?

- ♦ Depending on the research, up to 14% of the population has negative feelings about Wal-Mart which translates into lost business. Perhaps if Wal-Mart did not have such bad publicity, these lost customers might have increased same store sales. Wal-Mart's reaction to the negative publicity by mounting the economic conference and other activities clearly indicate a concern that negative publicity is hurting sales.
- ♦ The marketing and public relations department should both be concerned about Wal-Mart's image. Marketing is responsible for linking the customer to the company and negative publicity inhibits that ability. Marketing should work with the public relations department to develop community based marketing programs to help improve the company's image. Marketing should also conduct market research among Wal-Mart customers, as well as those aware of Wal-Mart but not shopping in the stores to assess the influence of attitudes towards the company on purchasing habits and purchase intent.

4. Wal-Mart attempted to attract higher income customers with its Metro 7 line, upgraded televisions, adding more stylish merchandise, and advertising in Vogue magazine. Do you agree with this change? What are the risks to current customers?

- ♦ Wal-Mart's attempt to upgrade its merchandise and its appeal to upper income shoppers including the Metro 7 line raises several concerns.
  - o The Metro 7 line was a Wal-Mart store brand, not available in any other retailer. Thus, those potential higher income shoppers who are name brand conscious would not see Metro 7 clothing as an addition to their wardrobe, and might be reluctant to wear a clothing label associated with Wal-Mart.
  - o While upgrading styles can be seen as an important strategy component, upgraded styles without the associated brand names would likely be insufficient to attract higher income buyers as well as Target customers.
  - o Upgraded televisions at competitive prices might be an attraction to higher income customers, but Wal-Mart does not have knowledgeable sales associates to answer questions about the features and benefits of these more expensive televisions. If Wal-Mart wanted to move into more

technically complex products and compete with the major electronics retailers their sales and service expenses would have to increase.

- o The ads in Vogue magazine are questionable. The Vogue reader has a high fashion orientation and probably would not consider the Metro 7 line in her wardrobe. If Wal-Mart advertised the Metro 7 line in Vogue to impress Wall Street that a fundamental shift in marketing and merchandising at Wal-Mart had taken place, a better way to impress Wall Street is with a successful Metro 7 line.

♦ Any effort to change the merchandise mix runs the risk of confusing and alienating current customers.

- o The core Wal-Mart shopper is interested in low price first, brands and fashion may come later. If current customers sense the merchandise and marketing direction has changed, this may increase concerns about Wal-Mart low pricing.
- o Historically there has been a good fit between the Wal-Mart low price strategy and the demographics and psychographics of its current customers. Any radical change could sever that loyalty bond between Wal-Mart and its current customer base. Wal-Mart runs the risk of not attracting the higher income shopper and also alienating its core customer base.

5. Describe Wal-Mart's relationship with its current suppliers. If Wal-Mart wants to upgrade its image by sourcing product from major name brands in fashion, what might Wal-Mart face in trying to do business with these suppliers?

♦ Wal-Mart historically has squeezed its suppliers for favorable treatment (within the law) and for low prices. While Wal-Mart can give a vendor substantial national and international sales volume, this may come at a price--limited vendor profitability.

♦ Name brand fashion suppliers may be reluctant to do business with Wal-Mart for several reasons.

- o If the fashion supplier has a presence in major department and fashion retailers, the presence of their brand in Wal-Mart could dilute the image of their brand.
- o Wal-Mart is known for setting low prices to consumers. Some of the name brand fashion suppliers prefer to have retailers sell their products at a suggested list price. This enables the retailers to achieve a higher profit margin and allows the retailer to stock a broader array of merchandise and

offer services associated with the product. These name brand fashion marketers will be reluctant to sell to Wal-Mart for the fear that their current retailers will drop their products if they sell to Wal-Mart and if Wal-Mart discounts the products.

6. How well did Roehm and Womack fit into the Wal-Mart culture? How did Wal-Mart culture and organizational structure influence marketing and merchandising decisions?

- ♦ Roehm and Womack were outsiders to the Wal-Mart culture and had a difficult time fitting in. Neither had retail experience which made them "outsiders" to the way things were done in the retail industry.
  - o Roehm's style was to push the edge of advertising, introduce sex into advertising, something just the opposite of the Wal-Mart conservative culture.
  - o Her failure to attend staff meetings, redecorating her office, her efforts to move Wal-Mart from price to branding, value, segmentation, and accountability led to further alienation from the Wal-Mart management team, many of whom wanted status quo.
  - o Her inability to develop a working relationship with Quinn hampered her ability to fully understand the market research and Wal-Mart customer dynamics.
  - o Her alleged violations of Wal-Mart policy regarding relationships with other employees and taking gifts from Wal-Mart suppliers further separated her from the Wal-Mart culture and management team.
- ♦ Wal-Mart's culture and organizational structure had significant impact on marketing and merchandising decisions
  - o There was a lack of strategic cohesiveness across functional areas in Wal-Mart. Merchandising focused the stores on price, the prevailing "old guard" strategy, while marketing featured style. Moreover, customer insights were ignored. This lack of an integrated marketing and merchandising strategy confuses consumers and dilutes brand image.
  - o There was indecisiveness about the overall business strategy with many stops and starts, leading to confusion across departments. Whether the strategy was to seek new customers and minimize the impact on existing customers or stay with the price/smiley face strategy of the past and market to existing customers, leadership in overall strategy was missing.

- o Management was unclear who Wal-Mart was competing with for new customers and what points of differentiation are important to these customers. The "old guard" continued to believe low price alone was a sustainable competitive advantage but failed to realize competitors were offering more than price and keeping customers from Wal-Mart.

♦ The new organizational structure following the departure of Roehm was clearly a step in the right direction to integrate marketing and merchandising decision making across functional areas. Fleming gained control over pricing and the customer experience. Yet the issue of price, market segments, target customers, and overall strategy remained unclear.

7. Describe how you might go about selecting a new ad agency. How would you have conducted the selection process? What was the rationale for selecting DraftFCB? Why might the "old guard" at Wal-Mart be resistant to Draft?

♦ Spending over 100 days out of the office and visiting 30 advertising agencies is not an effective use of time. These trips caused Roehm to miss important meetings at Wal-Mart. Roehm, based on her extensive experience and contacts in the business, could have identified and screened at least 10 agencies with the potential to handle the large Wal-Mart advertising account. These agencies could be invited to Bentonville to make a capabilities presentation to management. From the ten, three to five agencies could be invited to prepare specific recommendations as to how they would advertise Wal-Mart. The Wal-Mart team would then visit the agencies, hear the agency presentations, and make a selection of the final agency. This would cut the travel time and focus the decision making on a select number of qualified agencies.

♦ The rationale for selecting DraftFCB was based on the agency's approach to marketing using segmentation, targeting, and accountability. DraftFCB's experience in direct marketing with its return on investment mentality and local area marketing was a departure from Wal-Mart's mass market philosophy. Roehm believed DraftFCB could position Wal-Mart to compete against Target for the same customer.

♦ DraftFCB's approach to marketing was consistent with the new marketing staff hired by Wal-Mart who focused on branding and customer segmentation but foreign to the long time merchandisers who focused on low cost merchandise sold at a low price to the mass market. Moreover, the notion of accountability, that is, measuring return on marketing investment, could reflect negatively on current managers who spent marketing money apparently without accountability. Hence, DraftFCB approach represented a threat to current management.

8. Going forward, what strategy changes can be implemented to improve same store sales?

- ♦ Wal-Mart needs to decide on an overall marketing and merchandising strategy, validate that strategy, and stay with it. The company has moved back and forth between price, value, fashion, mass marketing, segmented targets, and back to low price. This has the potential to confuse the consumer and has failed to attract the higher income customer.
- ♦ The future strategy has to be carefully crafted to attract new customers and yet not alienate current customers.
  - o A two level, fashion merchandise strategy could be considered: 1) basic quality at low price, consistent with current customer needs and 2) medium quality and slightly better fashion brands at competitive department store prices for more upscale customers. Wal-Mart could ask branded fashion companies to develop select merchandise just for Wal-Mart under the fashion brand name but in styles and price points not available in other stores. In this way the branded fashion companies might sell to Wal-Mart without brand dilution.
  - o Adequate customer service is the challenge Wal-Mart faces in upgrading electronic offerings such as flat screen televisions. Adding knowledgeable sales help will add cost. A telephone hotline in the television department linked to a central office manned by television experts could provide live answers to customer questions without adding to individual store personnel. For the lower income customers, less costly flat screen televisions with fewer features and favorable financing can possibly satisfy this segment.
  - o Overall, Wal-Mart must move from price alone to a value proposition that includes quality merchandise, better fashion, and wider selection at competitive pricing. The buying habits of Target and other department store customers need to be identified and strategies developed to attract those customers without alienating the core Wal-Mart customer. However, it should be recognized the pure price shopper has limited options beyond Wal-Mart.
  - o The public image of Wal-Mart needs to be improved even at increased costs to the company for employee benefits and corporate citizenship.

This has to be weighed against the up to 14% of the population not shopping in Wal-Mart because of its poor public image.

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WAL-MART IS COMING TO INDIA -THE CASE

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CASE DESCRIPTION

Wal-Mart, which employs more than a million people, is under intense scrutiny for its policies and practices in the U.S. In spite of all its might and contributions, it is regularly under attack for treatment of its employees-for their low wages, lack of medical and dental plans, and lack of pension benefits-and for the decimation of small entrepreneurs in the community wherever it establishes its mega stores. So it is no surprise that Wal-Mart's coming to India, through a partnership with Bharti Group, is being opposed by many.

The primary purpose of this study is to analyze the ethical aspects of the largest international retailer, Walmart, coming to India where millions of people depend upon small businesses for their livelihood. The other important topics to be researched include: (a) The reasons why Wal-Mart wants to enter the Indian market; (b) Why its entry is opposed by some people; and (c) Why some others want the retailing giant to come to India.

This is a practice oriented case study (versus academic) appropriate for both undergraduate (junior and senior levels) and graduate level students. A teacher would require about an hour to explain the case contents and its significance to students. Similarly, a student would need about 2-3 hours to prepare the case and about half an hour to present it to the class, if so required. Time would vary depending on whether the case is analyzed and presented using a team approach or otherwise. However, because of the multidimensional nature of the case, a team approach may be more meaningful in its analysis.

CASE SYNOPSIS

This case would be very helpful to students, teachers, advisors, and policy makers who are interested in subject areas such as, international retailing, retailing in India, infrastructural development in India, and the effects of a giant multinational retailer's coming to India on its millions of kirana stores (small businesses) and the millions of people who depend upon these kirana stores for their livelihood.

INSTRUCTORS' NOTES

Questions and Answers

1. Why Wal-mart wants to enter the Indian market?

India is a large, diverse, technologically advancing, and poor country. Its population of more than one billion is only second to China. Its networks of roads, railroads, waterways, and airways are quite deficient. The airport at New Delhi, capital of India, is often closed because of fog. It is quite common to find cows sitting in the middle of the roads and highways-slowing down or stopping streams of trucks, auto-rickshaws, cars, and hand-carts going in different directions. Pedestrians walk on the road, or on the heavily crowded sidewalks if available.

Electric power supplied by the local governments is available but only for a few hours a day. Power outages happen frequently, with or without advance notice. The commercial refrigeration of perishable products is in its infancy stage. A large number of people, particularly women, are illiterate. Air and water pollution is widespread. The real estate prices are skyrocketing. It is very difficult to find sufficient space for locating superstores or malls on or near the main streets of India.

India has received worldwide attention for its technological excellence and exports and the millions of jobs it has created in these areas. However, its retail trade industry has not benefited much from these opportunities. The large-chain retail stores, which are benefiting from technological tools, make up only about 3 percent of the retail sales in India. Neighborhood stores and kirana shops (small stores) make up the rest (Institute for Local Self-Reliance, July 21, 2005). Large supermarkets are few and far in-between. Most Indians continue to shop at the neighborhood stores and the kirana shops for their requirements.

The retailing business in India is unorganized. Most of the millions of kirana shops are very small, have very little space (500 sq. feet or less) to operate, very few items to sell, and very little capital for growth (Swamy 2005).

So why does Wal-Mart want to enter the Indian market? No, Wal-Mart is not crazy. It has many compelling reasons to go to India. With all its problems and limitations, the country offers a number of opportunities, such as follows, to Wal-Mart and other retailers to establish large chain stores in the country.

To Diversify Supply Sources

While it is to the credit of both Wal-Mart and China to have developed the kind of close relationship that they have, the retailer's dependence on a single country as its primary supplier of products (about 90% of its needs) could be very risky. Wal-Mart, therefore, is trying to increase its merchandise sourcing from other countries, including India.

International trade is very competitive and mobile. Over the decades, the international buyers have been purchasing merchandise from several countries such as, Mexico, Korea, Japan, China, Hong Kong, India, and the Philippines. It is a virtual world where buyers can easily and quickly move from a higher cost country to a lower cost country. And because Wal-Mart does not own any factories, it's even easier for it to switch its sources of supplies from one country to another and from one company to another.

To Participate in a Huge Market

The current retail industry in India is dominated by the millions of small and entrepreneurial 'kirana' shops, vendors, and mobile hawkers selling all kinds of daily needs-including the milk, vegetables, and fruits. Refrigerating perishables is rare. Customers find retail shopping frustrating, time consuming, inefficient, and expensive. India is decades behind several other countries where the retailing business is dominated by supermarkets and shopping malls and the convenience and pleasure of shopping that they provide.

According to a study, India's retail industry is estimated at about $300 billion-which is expected to grow to about $427 billion by 2010 and about $637 billion by 2015 (Epstein Nov. 27, 2006).

India's growing middle class citizens are earning and spending more. Their centuries old tradition of self-denial and saving for the future is giving way to their appetite to consume and enjoy here and now. Its exploding younger generation is in the forefront of this transformation-65% of its people are under 35.

According to Jeff Immelt, chief executive of General Electric, GE India's parent, "We believe that India is a rising star at the beginning of a growth cycle, with consumer spending increasing at a strong rate, and people seeking and demanding a better quality of life" (Reddy 2005).

Many large international retailers like Carrefour SA of France, Metro AG of Germany, Tesco and Marks & Spencer Group of England, and Lifestyle International of Dubai already have their offices in India, both to source products from India and also lobby the Indian government to allow them to establish their retail stores in the country. The internationally known fashion retailer, Saks Fifth Avenue of New York, and the apparels retailer, Tommy Hilfiger, are also planning to set shops in India. Clearly, Wal-Mart cannot afford not to be among the first group of foreign retailers allowed to open large chain stores in India.

Finally, for a variety of reason, Wal-Mart had to close its operations in Germany and South Korea in 2006. Stores, Inc., its Asda grocery chain in the United Kingdom, which it purchased in 1999, has not yet become the dominant player in the field-it is behind the retailing giants Tesco and J. Sainsbury (White 2008). The Indian and the Chinese markets offer tremendous opportunities.

2. Why some people and organizations are against Wal-Mart coming to India?

There are several reasons, some fundamental and some superfluous, against Wal-Mart and other large international retailers establishing shops in India.

Calamity for Kirana Merchants

One might wonder why, on the one hand, India is very receptive to the foreign direct investment (FDI) in its manufacturing, information technology, and financial services sectors, but, on the other hand, quite hesitant to encourage the same in its retailing industry?

There are about 12 million retail outlets in India which account for 97% of its about $258 billion in annual retail sales (Elliott 2006). About 70 million Indians depend upon these small kirana (grocery) stores, mom and pop shops, and mobile handcart businesses for their livelihood (Institute for Local Self-Reliance, July. 21, 2005). These retailers exist at the end of the distribution chain, selling to the ultimate consumers. Millions of others work as intermediaries between the manufacturers, growers, wholesalers, and the retailers. (Note: the estimated size of the Indian retail industry, although quite large, may differ from one source to another).

Wal-Mart's coming to India, endowed with an array of modern equipment, methods, and management expertise will make these intermediaries, retailers, farmers, and manufacturers lose their jobs. According to Mohan Guruswamy, eight million people would lose jobs if Wal-Mart or similar stores captured just 20 percent of the retail trade in India (Elliott 2006). These statistics are frightening for a country which is already suffering from high rates of unemployment and poverty.

A paper by Andrew Shepard (2004), an economist with the UN Food and Agriculture Organisation, confirmed that large supermarkets often push small farmers out of business. The paper cited, among other examples, the development of the Giant retail chain in Malaysia which slashed the number of vegetable suppliers from 200 in 2001 to just 30 in 2003.

Threat to Large Indian Retail Firms

Pantaloon, Shoppers' Stop, and Westside are among a very small number of large chain retailers which already operate in different parts of India. The Pantaloon group, the largest discount retailer in India, includes Pantaloon apparel stores, Big Bazaar hypermarkets; and Food Bazaar. They Indian mega-retailers feel threatened by the entry of Wal-Mart and other global retailers who want to start their operations in India. An average-sized Wal-Mart store operates with 200,000 square feet of space. Pantaloon's flagship Big Bazaar operates with only about 50,000 square feet of space (Reddy 2005). It would be like David versus Goliath.

It may be noted that Bata, Godrej, Hero, Malhotras, Raymond, Reliance, Shopper's Stop, and Tata companies are among the other growing native large retail chains in India.

Unions Oppose the Anti-Union Retailer

The Indian labor unions are against Wal-Mart coming to India because Wal-Mart is against unionization. In the U.S., its home country, it has prevented its employees to form any union. It, however, is unionized at one of its stores in Canada. In China, under pressure from the All-China Federation of Trade Unions and the Chinese government, Wal-Mart agreed to allow unions if the Chinese workers would request to join one (BBC News 2004).

However, unlike Canada, workers are much poorer in India; and unlike China, India is a democracy. Labor in India is more organized and powerful as compared to its counterpart in many other countries. For example, according to the Indian labor laws, any company employing more than 100 workers cannot fire employees without first obtaining government permission to do so. Likewise, no worker can be made to work more than 75 hours of overtime a quarter (Rai 2006).

It is not uncommon for labor unions to go on strike when it has not been able to reach an accord with the management over the issues under dispute between them. At times, there are country-wide labor strikes involving millions of workers. Workers also resort to slowdowns, dharnas (sit downs), walkouts, and strikes. Most labor activities against management relate to the issues of wages, benefits, pension, fair-treatment, and job security. Generally, these activities are peaceful. Occasionally, however, they do become violent and destructive.

Likewise, the management may also resort to plant closeouts to contain its costs and protect its property.

It may be pointed out that while the foreign companies in India are struck less often than their Indian counterpart, they do get their share of the labor unrest. The two-week strike by workers at the Toyota Motors plant in Bangalore and another strike by workers at the Honda Motorcycles & Scooters' plant in Gurgaon, near New Delhi, are just two examples of labor problems at foreign companies in India.

Opposition from American Workers

In its home country, the American employees are concerned with the possibility that once in India, Wal-Mart would increase its merchandise sourcing from India-from about $1.5 billion worth in 2005 to about $10 billion worth in the next few years. This would mean more job losses in the U.S.

3. Why India wants to invite Wal-Mart to India?

Not everyone subscribes to the notion that Wal-Mart coming to India would only have negative consequences for its people. Many of them, on the other hand, argue that the international mega-retailer would have several positive effects on India's economy and infrastructure-as discussed below.

Economic Advantages

Foreign Direct Investment (FDI) in retail sector has been a key driver of increased productivity and economic growth in many countries. For example, in Brazil, Poland and Thailand, it has motivated wholesalers and food processors to improve operations and raise exports. Its emphasis on standardized products has boosted tourism. Consumers enjoy the lower prices as producers make higher profits (Swamy 2005).

According to the World Bank, the organized retailing has tended to control inflation because these retailers can buy directly from manufacturers at most competitive prices. For example, prices in real terms at Wal-Mart have not increased for almost a decade (Naik 2005).

In September 2006, Wal-Mart announced that it will drastically cut prices of 300 generic prescription drugs to as low as $4 for a month's supply. Needless to say, it was a result of its bargaining might it uses in negotiating prices with the corporate giants in the pharmaceutical industry. By using a similar policy in India, Wal-Mart can make drugs affordable to millions of people there.

Finally, Wal-Mart will increase the availability of standardized products in India, which in turn would help boost tourism (Swamy 2005).

Waste Reduction

Wal-Mart would be able to work directly with farmers and food-processing companies and help them reduce waste and enhance the quality of their products. Farmers can bypass an inefficient and often corrupt government-controlled distribution chain. In a country where some 40 percent of farm produce is spoiled before it reaches consumers, these improvements would be very beneficial to all. Consumers would get improved quality at better prices.

Infrastructural Development

Wal-Mart, like other firms, would require a much more efficient and modern network of infrastructure to survive and grow in India. While the Government of India is making efforts to establish such facilities, it will take them years to do so. Therefore, Wal-Mart, like some of its Indian competitors, would also have to invest in building some of its own modern infrastructure (Moreau and Mazumdar 2006).

For example, Mukesh Ambani (of the Reliance Retail Group) is planning to build two modern cities-one outside Mumbai and another outside New Delhi. The ten year master plan includes modernization of farms, building of warehouses and distribution centers, and opening up retail stores. It plans to build 1,600 farm-supply hubs across the country to provide farmers with various types of financial, technical, procurement, and marketing support and training. Similarly, 85 logistics centers would be established to help transport farm products between various destinations such as, fields, retail stores, seaports, and airports (Moreau and Mazumdar 2006).

Ambani plans to create a seamlessly effective and efficient network of infrastructure (communication, roads, power generation, water purification, railroads, bridges, etc.) to connect and move, goods, services, and information from one point to another-farmers, manufacturers, financiers, supplies, distributors, and consumers. The $11 billion project, when materialized, would help create 1 million jobs and $20 billion worth of agricultural surplus for exports per year by 2011 (Moreau and Mazumdar 2006).

Some of the other private entities involved in improving infrastructure in India include auto manufacturers that generate electricity, Irb corporation that is building roads, and Anil Ambani, Mukeh's brother, who is building a $4 billion suburban railway system in Mumbai, (Knowledge@Wharton Dec. 14, 2006).

Naturally, Wal-Mart will also have to help India improve its infrastructure-as it helps itself prosper in this country.

Culture and Ethnocentrism

Finally, and probably the most important reason for India to allow Wal-Mart and other large international retailers to come to India is cultural. For decades, the Indian economy has been constrained by the philosophies of socialism, swadeshi (India made) production, cottage industries, and the government controlled economy. The use of modern equipment and technology has been limited in order to protect jobs. This logic, with all its noble intention, is fundamentally misguided. Denying Wal-Mart and other international retailers to help India modernize its retailing industry and infrastructure would be like denying Caterpillar to do business in heavy equipment in India. It's not a question of whether India can take care of its retail business on its own; it is more a question of how efficiently it can do so.

The Indians are very proud of their ethnicity and illustrious cultural history. However, they are also interested in shopping at places that are clean and organized. Buying foreign products, eating at international restaurants, and watching films and shows made in the U.S. are considered as status symbols. No wonder, they have fancy for the Japanese cars, McDonald's, Starbucks, and the Baywatch, starring David Hasselhoff.

No, the Indian ethnicity and traditions should not be of major concern for Wal-Mart in India.

4. It is argued that Wal-Mart's coming to India would be unethical since it would cause unemployment and displacement of millions of people and their families. What is your opinion?

Let me discuss this complex and multisided question as follows:

Unemployment

It is true that Wal-Mart's coming to India would have a negative effect on the survival of the kirana industry and the millions of entrepreneurs and employees whose livelihood depends on it.

While the introduction of large international retail chains would hurt many people in India in many different ways, this is not the whole story. The kirana shops continue to be replaced by the Indian chain retail stores such as Pantaloon-with or without Wal-Mart. Admittedly, the entry of Wal-Mart and other international retailers would accelerate the replacement process. Either way, it will take years before the kirana shops become a thing of the past.

Secondly, it is argued that because the type of consumers who shop at the large chain stores are often different than those who patronize the kirana shops; and that because the overall retail industry will continue to grow, the entry and expansion of the large retail chains, including the multinationals, would not have much negative impact on the traditional retailers for years to come. And if and when that happens, Wal-Mart would have a very small role in it.

Harmful Ingredients and Misinformation

The multinational companies in India have been criticized for some questionable practices. For example, it has been alleged that products manufactured in India by Coke and Pepsi contain unacceptable levels of pesticides and cancer-causing benzene (The New York Times August 23, 2006).

Likewise, some multinational pharmaceutical and drug companies have been accused of providing insufficient and/or inaccurate information about their products to the doctors in India as compared to their counterparts working in the advanced countries. The list of uses of their drugs they provide to the former is at times larger than what they make available to the latter. Likewise, the range of adverse effects that they provide to the Indian doctors is narrower than what they share with their counterparts in the advanced countries (Rane 1998).

So it is argued that Wal-Mart, widely known for its alleged unethical practices in the U.S., would resort to similar practices in India.

The use of unacceptable levels of pesticides and cancer causing benzene in making soft drinks and providing incomplete/inaccurate information to doctors about drugs is certainly unethical and/or illegal. If Wal-Mart would use similar practices in India, it likewise would be responsible for them.

On the other hand, it is not proper to argue that if certain foreign companies were engaged in some questionable practices in India, that all foreign companies would also do likewise. Let us hope that Wal-Mart would stay away from such practices.

The State of Business Ethics in India

The Lord Acton's (1834-1902) famous quote "Power corrupts, and absolute power corrupts absolutely," applies too well to India. Not everyone, but many, many people, with power or opportunity, won't hesitate to take advantage of the situation. Corruption is rampant in India, as it is in several other nations such as, Brazil, China, Mexico, and Russia. The U.S. business and government, once a beacon of hope of ethical dealings, with its own problems of corruption and dishonesty, is not helping much either.

At the same time, India has enacted several laws to fight corruption. They deal with people's right to information, government procurement, human rights, right to education, and contracts, among others. Internet is playing a major role in bringing problems to public attention. However, clearly, it is an uphill fight.

CONCLUDING THOUGHTS

Opposition by people adversely affected by modern technology and equipment is nothing new. The Industrial Revolution which is credited for increasing wealth and the standard of living of the average person was also blamed for the wage decline and distress it caused to many. In 1811, in Nottingham, England, some of these impoverished workers, called Luddities, stormed into factories and destroyed the machines responsible for shattering their means of living (McCullough 2007). Imagine the consequences of stopping the industrial revolution at that time in the history, on people and society today.

Investment in modern technology and equipment is a pre-requisite of economic progress. Use of these resources also reduces the need for human labor. The resulting unemployment causes a gamut of personal, social, and political problems. Unemployment shatters personal lives, increases unrest, and creates political upheavals.

The society can help minimize these problems and pains by helping the unemployed and displaced people with unemployment benefits, counseling, education, and training for new job opportunities. Economic progress and economic justice should go hand in hand.

According to the WTO guidelines, India is required to lift its ban on the foreign direct investment, such as from Wal-Mart, in its retail industry. The failure to do so may cause the developing nation to lose the tariff and trade privileges it enjoys from other countries. This loss can have a very negative effect on its production, productivity, exports, and employment.

ENDNOTE

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FINANCIAL ANALYSIS OF WRONGFUL TERMINATION: JOSEPH KIDWELL

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CASE DESCRIPTION

The primary subject matter of this case concerns the valuation of economic damages incurred by Mr. Joseph Kidwell upon his wrongful termination from Gilad Lexus of Billings, Montana. A secondary issue examined involves brand specific knowledge which is not transferable to the selling of other automobiles. The course has a difficulty level appropriate for the advanced undergraduate or first year masters students, practicing HR managers or those seeking to become forensic economists. The case is designed to be taught in one and a half class hours and is expected to require two hours of outside preparation by students.

CASE SYNOPSIS

Joseph Kidwell, a talented sales manager for a Lexus dealership, was terminated for refusing to call the police and report a car as being stolen. It was later found that an employee had borrowed the car without permission, but Joseph had already been terminated. Joseph brought a lawsuit against the dealership for wrongful termination, the details of which are presented in this case. The reader is tasked with analyzing the economic loss suffered by Joseph due to the termination.

INSTRUCTORS' NOTES

Suggested Teaching Approach

This case is useful for teaching the application of economic and finance principals in a real world setting. The estimation of economic loss requires the idea of opportunity cost and forecasting what the plaintiff's economic picture would be if the damage had not occurred and the future economic picture after the damage has occurred. The use of present value techniques should be employed to compute the value at the time of the trial of losses which will be experienced by Joseph after the trial has taken place.

Suggested Questions for Students Needing Structured Guidance

1. **What are the major components of Joseph's economic damages?**

   The major components of Joseph's economic damages are lost earnings, lost 401k contributions, and additional health insurance costs. These losses should be determined for the time period between the time of dismissal and the date of the trial (June 3, 2006 - August 1, 2007). These are termed Past Losses since they occur prior to the trial. Similarly, estimates of these costs for some time period after the trial date are termed Future Losses.

2. **What role does future inflation play in estimating future damages?**

   What Joseph's future earnings would have been at Gilad Lexus are unknown. Since his compensation was tied to gross sales, anything which affected the sale of Lexus automobiles would also affect his income. Without building an econometric model of Lexus sales, the conservative approach is to assume that Joseph's earnings would have kept up with the rate of inflation. But that raises the question of what will be the future rate of inflation? Estimate the rate of inflation by use of a geometric mean of the Consumer Price Index (CPI) for the same number of years used in computing the discount rate.

3. **What discount rate should be used to calculate the present value of future damages?**

   Future Losses should be discounted to the date of the trial by use of a suitable discount rate. The choice of an appropriate discount rate arouses considerable debate among economists. The student should have a sound logic to back-up the choice of discount rate regardless of the rate chosen. The geometric mean for the last fifteen years of the constant maturity 3-month Treasury bill is often used as a discount rate. The justification for this rate is that it reacts more quickly to changing inflation expectations. Since the past is being used to predict the future, the more variable short-term rate is seen as being a better predictor.

4. **How many years will it take Joseph to attain his previous level of earnings? How does Joseph's level of education and geographic location figure in the damage calculations?**

The number of years into the future to compute damages is unclear. A low skilled individual earning a low wage should be able to find equivalent employment in less time than an individual with highly specialized training who earns a high income. The less transferable a person's skill set, the longer it will take to regain the same level of earnings. Joseph's value in the marketplace rests upon his knowledge of Lexus automobiles and the Lexus way of doing things. This specialization will make it more difficult for him to recover. If he is lucky enough to find a position with another Lexus dealership, his recovery time will be shorter. If he is forced to take a position selling another brand of automobile or perhaps an entirely different product, his recovery time will be longer. There are numerous academic papers which suggest that the average length of time to recover from an involuntary dismissal is 5 years.

Possible Solution to the Case

One possible solution is summarized in the tables which follow. Other solutions could certainly result. Typically, expert witnesses are hired by attorneys to support the particular lawsuit, so in reality, the analysis is usually substantially biased. The lesson here, though, is to present a plausible solution. Attorneys and courts have a strict preference for 'the right number.' A range of outcomes may be a desirable exercise for forensic economics; however, the particular methods and assumptions are left to the professor.

Table TN1: Summary of Economic Damages (detailed in table TN 2).	
Summary of Economic Damages	
Past Damages	
Earnings	$212,800
401k Contributions	$19,152
Insurance Costs	$6,970
Total Past Damages	$238,922
Future Damages	
Earnings	$308,570
401k Contributions	$27,771
Total Future Damages	$336,341
Total Damages	$575,263

Table TN2. Detailed Analysis.

Joseph Kidwell

trial date	08/01/07						
inflation	3.0%						
discount rt	3.5%						
recovery rt	33.3%						
Year	Earnings w/o Dismissal	Earnings with Dismissal	Lost Earnings	Growth Factor	Discount Factor	Economic Value	Cumulative
2006	$221,868	$137,934	$83,934	1.000	1.000	$83,934	$83,934
2007	$128,866	$0	$128,866	1.000	1.000	$128,866	$212,800
2007	$93,002	$68,967	$24,035	1.000	0.986	$23,687	$23,687
2008	$221,868	$91,933	$129,935	1.030	0.952	$127,355	$151,042
2009	$221,868	$122,547	$99,321	1.060	0.919	$96,824	$247,866
2010	$221,868	$163,355	$58,513	1.092	0.888	$56,734	$304,600
2011	$221,868	$217,752	$4,116	1.125	0.858	$3,970	$308,570
Year	401k Contributions w/o Dismissal	401k Contributions with Dismissal	Lost Contributions	Growth Factor	Discount Factor	Economic Value	Cumulative
2006	$19,968	$12,414	$7,554	1.000	1.000	$7,554	$7,554
2007	$11,598	$0	$11,598	1.000	1.000	$11,598	$19,152
2007	$8,370	$6,207	$2,163	1.000	0.986	$2,132	$2,132
2008	$19,968	$8,274	$11,694	1.030	0.952	$11,462	$13,594
2009	$19,968	$11,029	$8,939	1.060	0.919	$8,714	$22,308
2010	$19,968	$14,702	$5,266	1.092	0.888	$5,106	$27,414
2011	$19,968	$19,598	$370	1.125	0.858	$357	$27,771
Year	Insurance Costs w/o Dismissal	Insurance Costs with Dismissal	Insurance Damages	Growth Factor	Discount Factor	Economic Value	Cumulative
2006	$2,787.95	$6,272.88	$3,484.93	1.000	1.000	$3,484.93	$3,484.93
2007	$2,787.95	$6,272.88	$3,484.93	1.000	1.000	$3,484.93	$6,969.86
2007	$2,012.05	$2,012.05	$0.00	1.000	0.986	$0.00	$0.00
2008	$4,800.00	$4,800.00	$0.00	1.030	0.952	$0.00	$0.00
2009	$4,800.00	$4,800.00	$0.00	1.060	0.919	$0.00	$0.00
2010	$4,800.00	$4,800.00	$0.00	1.092	0.888	$0.00	$0.00
2011	$4,800.00	$4,800.00	$0.00	1.125	0.858	$0.00	$0.00

Note: Economic value is the present value of lost earnings, lost contributions, and insurance damages (first, second, and third panels of exhibit TN2).

EPILOGUE

The case was settled out of court for $400,000. Joseph and his family moved to Minneapolis, Minnesota where he was able to obtain a sales position at another Lexus dealership. It took 6.5 years for his earnings to reach the same level as his inflation adjusted earnings at Gilad. He still misses his family and friends in Billings.

SIERRA PACIFIC RESOURCES IMPLEMENTS A MERGER

Ruth Clarke, Nova Southeastern University
David Cohen, Nova Southeastern University

CASE DESCRIPTION

The primary subject matter of this case concerns the development of a staffing plan for the merger of two companies. Secondary issues examined include;

How can the staffing plan be modified to save time and money and still meet legal guidelines?
How can the process be accelerated and still allow for a cascade approach to staffing?
What elements of the plan are crucial to ensure legal defensibility of the process?
Who is included in the phrase "protected class?"
What is a role profile?
How do you create role profiles for existing positions and for new positions?
Who is a job content expert?
What information do employees need to know in order to make an informed decision about their future with the company?
What role does a job fair serve?
What is the role of training in a staffing process?
Why is it so important to involve attorneys in the process?
Why can't existing performance appraisal data from the two companies be used to make selection decisions?
What are the benefits of designing a voluntary severance package? What are the disadvantages of such a package?
How do you prevent managers from preselecting their candidate of choice?
What role do senior officers play in the staffing process?
How do you estimate of the cost of a staffing process?
How do you estimate the time involved to design a staffing process?
How do you estimate the time involved to implement a staffing process?

The case has a difficulty level of level 5, appropriate for first year graduate level; six, appropriate for second year graduate level; seven, appropriate for doctoral level).

The case is designed to be taught in 2 classes where it is overviewed in one class and the questions are discussed in a second class. It requires 2 - 3 hours of outside preparation by students.

CASE SYNOPSIS

What happens when the real world and the academic world collide? In a perfect world a legally defensible staffing plan for the merger of two companies requires a detailed step by step process as well as sufficient time and money to execute the process. In the imperfect, real world, designing a legally defensible staffing plan when money is tight, time is of the essence, and managers don't have the patience to go through a detailed, labor intensive process before making their selection decisions is another matter altogether. This case describes a detailed, step by step and by-the-book staffing process to create a legally defensible staffing plan. It is designed by someone who is known for creating expensive, thorough and time consuming processes that have never lost a challenge in court. When client concerns and constraints challenge that perfect plan the perfect world clashes with the imperfect world and students are caught in the middle.

Their task is to modify the perfect staffing plan in a way that satisfies the attorneys who are looking out for the company's best interests and the management team who want to staff the new organization as quickly and as economically as possible so they can get on with the business of running the new business. Although not detailed in the case, instructors can incorporate the selection and design of behavioral competencies, role profiles and critical incident (behavioral) interview questionnaires and interviewing techniques into the case.

INSTRUCTORS' NOTES

Recommendations for Teaching Approaches

Use the following case questions for class discussion.

What are the strengths and weaknesses of the selection process?
What needs to be considered and who needs to be involved in the determination of requirements for a position in the merged organization?
Why is the selection of officers so critical to the process and what does it communicate to employees even before the remainder of the selection process begins?
What information needs to be made available to all employees to ensure that they have what they need to know in order to make an informed decision about their future?
Why current performance data are not used to make selection decisions instead of a lengthy and labor intensive process?

What changes, if any, would you make to the staffing plan and how would you ensure that those changes do not compromise the integrity of the process?
What are the hard and soft expenses associated with the merger staffing plan?

Additional questions if time permits a more extensive classroom discussion

Who should a voluntary severance package target?
What additional support elements will help employees through the process?
What does the merger integration staffing plan communicate to employees?

We discuss each of these questions in detail in the following section to guide instructors.

1. What are the strengths and weaknesses of the selection process?

The overall strength of the selection process is in its detail and thoroughness. It involves input from job content experts (supervisors and managers) in the identification of job requirements which is crucial for a legally defensible process. It treats each employee equally in that no prior performance data are included in the information used for a hiring decision since this information would not be consistent across the two legacy organizations. It requires each employee to go through the entire selection process for a desired position. It ensures that hiring managers, once in place, select their direct reports and it has an oversight committee to ensure that the process is adhered to and executed fairly and objectively. The process also provides all the information an employee needs to know before he or she is required to make a decision to apply for a position in the new organization or seek employment elsewhere. While the detail and thoroughness are strengths, they may also be considered weaknesses in that they increase the length of time necessary to design and implement the process. This also increases the expenses associated with the staffing process. This same level of detail can be seen by hiring managers as a nuisance especially if they have prematurely and inappropriately decided which employee(s) they want to hire.

In the event of a lawsuit by a member of a protected class, ask students how they would defend the process in court. What do they see as the most important steps to ensure the legal defensibility of the selection process?

Students need to compare and contrast the cost of the process with the cost of defending the process in court if it is not done well. Impress on them that without the extensive nature of a thoroughly designed selection process, the possibility of legal challenges increases.

If a member of a protected class were to successfully sue the company for discrimination based on the design, implementation or results of the selection process, the cost to the company in both out of pocket costs and damaged image would be extensive. For this reason, managers and supervisors (the job content experts) must be involved in every step of the process, and the process itself needs to be extensive in order to ensure fairness for everyone seeking a position in the merged organization.

2. What needs to be considered and who needs to be involved in the determination of requirements for a position in the merged organization?

A well designed process includes the hiring managers' input in the creation of job specifications as well as the competencies and traits that are necessary for success in those positions. These are known by the acronym KSA (knowledge, skills and abilities.). The process by which these are identified and the recommended individuals involved is described in detail in the staffing plan component of the case. Without the involvement of these job content experts, it would not be possible to defend the process in a court of law.

Information is collected from candidates through a process called critical incident or behavioral interviewing. Here is a brief explanation of the technique which the instructor may wish to share with the students.

Critical Incident Interviews

An essential part of the role of an interviewer is to determine the presence of critical competencies in candidates for a particular position. This cannot be done by reviewing experience and education, but can be done by interviewing the applicant and asking questions designed to elicit how the interviewee behaved or what the interviewee did in certain situations. Interviewers need to function as investigative reporters or courtroom attorneys and seek specific examples of behavior in the applicant's past.

It has long been established that the best predictor of a person's future behavior is his or her past behavior. Since it is neither practical nor possible to observe everything that a person does or says, the next best thing is to seek information from the applicant through a process known as a Critical Incident Interview.

Standard job interviews often involve questions or statements such as, "Tell me about your strengths and weaknesses (developmental needs)," or "What would you do?" questions that describe a particular situation. Critical Incident Interviews, on the other hand, focus on specific situations in which the candidate has been involved in the past. Therefore, the interviewer can ask the candidate to describe real situations and what they actually said or did in those situations. It is up to the interviewer to collect enough information about the candidate to be able to describe to a third party why he, the interviewer believes that the candidate does or does not possess sufficient proficiency in a competency necessary for success on the job.

This type of interview needs to identify three pieces of information in order to evaluate a behavioral example. First, under what conditions did the candidate act or react? This could be a standard job responsibility or it could be in reaction to an event or someone else's action. Second, what specifically did the person say or do in response? The interviewer should always be seeking "I" statements from the applicant and all verbs that follow "I" must be in the past tense. Third, it is important to know if what the person did had the intended outcome. Did their actions work or not? Were they successful or not? Did others respond as they wanted them to or not? It is the interviewer's task to identify what the person did, why the person did it, and how it turned out?

It is not the purpose of this case to teach Critical Incident Interviewing. However, the instructor may wish to introduce specific behavioral interviewing techniques and have the students practice this type of interviewing on each other.

3. Why is the selection of officers critical to the process and what does it communicate to employees even before the remainder of the selection process begins?

The first official communication in a merger situation is the selection of officers; therefore, the process must be transparent. What gets communicated by actions is more meaningful than what is communicated by words. Based on their experience, employees know what each officer stands for their selection (the action) must be in sync with and show support for the values of the new organization. Officer selection communicates not only the "winning" organization it also sends a message to all employees about the culture of the new organization. Employees will look for every conceivable inconsistency between what is communicated about the new culture and the selection of officers to help create it.

The selection of officers communicates which of the two merged organizations is going to exercise the most control in the merged organization. Fortunately or unfortunately, employees always think in terms of winners and losers in mergers, even if the merger is positioned as a merger of equals. Second, it communicates the values that will guide the new organization because employees know, explicitly or implicitly, what values each officer stands for. If the merger is all about change and only the oldest members of the officer team are going to be a part of the merged organization, then employees will doubt that change is going to be a real value. If the merger touts a new era of open communication and the officers selected are the most formal and least approachable, again a conflict in what is said and what is done will occur. In these cases the intent of the merger may be doomed from the start. A survey conducted by New Dawn Consulting (a well known but disguised management consulting firm) and the Society for Human Resource Management (2000) found that 6 out of the 10 top reasons why mergers fail are related to human resources issues.

4. What information needs to be made available to all employees to ensure that they have what they need to know in order to make an informed decision about their future?

Employees need and have the right to know what happens if they want to stay and what happens if they choose to leave the organization voluntarily. Obviously employees need to know the vision, mission and values of the merged organization as well as details about the specific jobs for which they want to apply. This would include, but not be limited to salary, location, level, responsibilities and when known, their immediate supervisor/manager. Employees also need to know what the company will do for them if they do not choose to seek a position in the merged organization. All employees have the right to choose not to be a part of the merged organization and in such cases they are entitled to a voluntary severance package.

When you have more employees to choose from than you have positions to fill, a voluntary severance package helps reduce the pool of available employees in a positive manner, and maintains any goodwill the company has established in the past.

It is often the case that many employees don't like the idea of change and almost all employees want options when it comes to personal decisions relating to their jobs and their careers. A voluntary severance package allows employees to opt out of the process altogether if they don't like the change they foresee with the merger. For some employees, a voluntary severance package can be a financial windfall that enables them to start a new career. For long service employees it can provide the incentive they need to retire. (The student must interpret these last two sentences in light of current economic conditions.)

Typically long-term employees are the most vulnerable in a merger situation. Younger employees can view a merger as an opportunity to change careers and be paid for doing so. Employees in the prime of their careers and those on an upwardly mobile career path rarely have anything to worry about. Long-term employees, not yet ready to retire but feeling too old to change careers or jobs are typically targeted for voluntary severance and often feel forced to leave, whether that feeling is perceived or based in fact. They need to be treated with respect and provided with support throughout the merger process.

This discussion provides a good opportunity to highlight components of a voluntary severance package. Typically these consist of fixed dollar amounts multiplied by a factor comprised of age, length of service and level within the organization, as well as continuation of health benefits or an artificial bridge to extend health benefits for those employees who are below normal retirement age. Many organizations base the eligibility for this bridge on what they term a "magic" number which equals age and years of service. It is specifically designed to ensure that employees who are close to retirement age do not lose out on retirement benefits due to the merger or acquisition.

5. **Why current performance data are not used to make selection decisions instead of a lengthy and labor intensive process?**

Legacy performance management information cannot be used for selection purposes because there is no commonality of process or content between legacy companies. Only the fact that an employee is in good standing and therefore eligible for a position in the merged organization is legally permissible. Beyond that, all employees are on equal footing for the selection process. Employees can point to the use of past performance data as discriminating against them in the new organization. Ignoring legacy performance management may be a tricky concept for students; but this leads to possible legal action. It is also something that hiring managers do not like ignoring even though they know that they are required not to use it.

6. **What change, if any, would you make to the staffing plan and how would you ensure that those changes do not compromise the integrity of the process?**

There is no right or wrong response to this question. Students should be encouraged to determine what would be lost from a validity standpoint if certain elements are removed from the process. One area that should be discussed is the cascade approach. This approach dictates that nothing can happen at a particular level until the level above has been selected. The assumption here is that newly placed managers and supervisors implement the selection process for their direct reports. This can be changed with skilled interviewers conducting screening interviews and then recommending who the hiring manager should interview. This can save considerable time and expense in the process and is conducted much like HR departments or personnel agencies operate. When this type of prescreening is done by HR professionals, the process moves more quickly because final candidates are presumable ready to be interviewed once the hiring manager is in place.

Students should note that while a generic set of competencies is sometimes used in a merger/acquisition staffing situation, this approach is not as legally defensible as the process described in this case.

7. **What are the hard and soft expenses associated with a merger staffing plan?**

Hard expenses: Professional consultant fees, development costs, materials out of pocket expenses (travel, meals), salaries, etc.

Soft expenses: Time away from regular responsibilities for those involved in the process; regular work that is not getting done on time or not getting done at all, clerical/administrative, follow-up activities, training and development time.

Additional questions if time permits a more extensive classroom discussion

8. Who should a voluntary severance package target?

The most likely group to accept a voluntary severance package needs to be identified so the package can be geared toward their needs and designed to entice them to accept. This group is different in every merger and acquisition situation. When this is done well, it can get the merger off to a positive start in the eyes of employees when they feel they are being treated fairly and with respect for their length of service to the legacy companies.

Ask the students if they would take a voluntary severance package. Some of them will think this is a great idea and enable them to achieve goals, while others will focus on the instability associated with no job. Young students should be encouraged to be more aggressive in taking on new challenges and career development. Older students should see this as an opportunity to start something new with a capital infusion from the severance package.

9. What additional support elements will help employees through the process?

One other support area includes an Ombudsman. An ombudsman needs to be set up so employees feel that they have recourse should there be concerns on their part at any time during the merger selection process. Outplacement support should be provided for anyone not selected for a position, at no cost to the employee. This should include all the peripheral support one might need such as fax, phone, office, etc., in order to facilitate their job search. Many US students will not be familiar with the ombudsman concept. Ombudsmen are more common in European countries. Let them search the web for information on this or locate an actual ombudsman for class.

10. What does the merger integration staffing plan need to communicate to employees?

The most important statement that the staffing plan needs to communicate is the fairness and relevance of the process. This begins with a voluntary severance package, which, if structured appropriately and communicated clearly will start the entire process off on a positive note. The severance package needs to be targeted to a particular group and designed in such a way as to encourage that group to take advantage of the package. While most changes in an M & A situation bring concerns, a well designed voluntary severance package will say to employees that the company cares about them.

The staffing plan needs to communicate the same sense of caring. It needs to show employees that they will not have to make any decisions about what they want to do until they have all the information they need in order to make an informed decision. Students should be encouraged to detail a list of questions that an employee might have when facing an M & A question and then compare those questions to which steps in the plan are designed to answer them. In this way they can determine if anything has been omitted and if, in fact, all employees have the information they need in order to make personal decisions.

EPILOGUE

David and Jean agreed on a price of $2,150,000. The merger process was implemented successfully and completed in the first week of December. The following goals were met:

Sierra Pacific Resources Achieved Goals

- 500 positions were filled, approximately 300 located in Las Vegas, and 200 in Reno.
- 175 employees took voluntary severance packages (100 from Nevada Power) and 25 (18 from Nevada Power) needed help in locating another position.
- There were no legal actions taken against the company.
- There were no process violations; all hiring managers implemented the process as intended.
- There were many positive comments about the process from participants, both hired and not hired.
- There was representative distribution of staffing selections from both legacy companies.
- A positive image was created within the communities served because of the way employees were treated during the merger staffing process.
- There was no disruption or decline in level of services provided to customers.
- The company realized dollar savings through eliminating redundancies in staff positions.
- The new name was posted over the Nevada Power name on banners before the staffing process was complete.

This material was collected by one of the authors during a consulting project with the two companies as they went through the merger and reorganization. The data consist of interviews with key players and information drawn from the material designed to guide the process of integration. Sierra Pacific Resources has graciously consented to the public dissemination of this case.

The following suggested references are a first step towards understanding the nature of merger success or failure, and also behavioral interviewing. Interested instructors can find material in these references to support the fact that most merger failures are related to people and cultural issues. A New Dawn Consulting and SHRM internal report on Integration Challenges, 2000, collected data which also supports this finding; however this report is not publicly available.

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AMOS HILL ASSOCIATES, INC.

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CASE DESCRIPTION

The primary subject matter of this case concerns a capital costing decision relating to a new equipment purchase. Secondary issues examined include production possibilities and the effect and timing of a major equipment purchase. The case has a difficulty level of three (appropriate for junior level) to five (appropriate for first year graduate level). The case is designed to be taught in two class hours and is expected to require two to six hours of outside preparation by students.

CASE SYNOPSIS

Amos-Hill Associates, Inc. is a veneer manufacturer in Indiana, specializing in the production of premium quality American hardwood veneers for international architectural and furniture markets. Veneer is a decorative wood product created by slicing logs into thin sheets (1/20 to 1/50 of an inch) to maximize the yield of natural wood grain material for applications in architectural and furniture products. Recently, Amos-Hill Associates acquired a new veneer slicing system which uses a new technology, a vacuum table, to hold the flitches (half-logs) from which veneer is sliced from the log. John Chiarotti, the vice-president and general manager of Amos-Hill has requested an analysis of the benefits of purchasing an additional vacuum table for the second production line. The improvement must be significant enough to justify the cost of the new vacuum table.

INSTRUCTORS' NOTES

Topical Coverage and Intended Courses

This case is designed to illustrate factors that must be considered in a capital-costing decision. The relatively small size of the organization allows for the reader to connect the importance of expenditures on equipment to the strategic intent of management. In addition, the case illustrates the essential operational processes of the hardwood veneer industry.

The topics presented in this case make it appropriate for graduate or undergraduate classes in financial management, management accounting, or entrepreneurship. The strategic implications of production gains utilizing new technology allow it to be a suitable case for discussion in strategy classes. The case can be covered in thirty to seventy five minutes, depending on the depth and breadth of the discussion.

Discussion Questions:

The following questions are suggested for discussion:

1. **Assuming a 14% cost of capital, should Amos-Hill Associates, Inc. invest $180,000 in a new vacuum table for their second vertical slicer line?**

   This very broad question does not provide the student very much in the way of structure or guidance. The instructor may prefer to direct the student further by asking for the following:

   A. Begin by determining which logs will be cut on the second vacuum slicer, assuming that the highest quality (most expensive per Veneer Price per 1,000 sq. ft. column in Table 1) logs will continue to be processed on the first table;
   B. Calculate the additional ¼" of veneer per flitch with the new table;
   C. Calculate the associated gross profit generated from the additional veneer computed in B above;
   D. Compute the additional flitches per shift that can be processed;
   E. Compute the resulting additional gross profit from the additional flitches calculated in D above;
   F. Using the above information, compute the payback period, net present value and internal rate of return of the capital investment of the second vacuum table.

2. **Explain the potential benefits beyond any tangible financial benefits to Amos-Hill that can be achieved by replacing the current slicer with the newer technology. Are there disadvantages, as well?**

Key Issues:

The overriding decision presented in this case is a major equipment purchase. Financial justification must be made for this significant expenditure through an analysis of the costs to be incurred and the benefits returned by the change. As such, return on investment, breakeven, and cash flow analyses are each appropriate investigation techniques.

The effect and timing of introducing new technology into the production process is also an important topic illustrated in this case. The benefits of production gains, issues with change management, determining the timing and extent of technology adoption, and the effect of new technology on competency and competition can be discussed using this case as an illustration.

Answers to Discussion Questions:

1. **Assuming a 14% cost of capital, should Amos-Hill Associates, Inc. invest $180,000 in a new vacuum table for their second vertical slicer line?**

1A The Total Production by Output Line column in Table Two of the attached Excel workbook computes how many flitches are processed on each of the three production lines -Production by Output Line column. Table Three shows production not done on the vacuum line. (See column 7) The most expensive (column 6) species were removed as those are sliced on the present vacuum slicer. Overall amounts from Table One would skew the results because they would include more expensive (profitable) species.

1B The additional veneer cut is computed 2 ways. The first method uses the average yield over all veneer not done on the first vacuum table (Table 3). The second method computes the additional veneer on a species by species basis.

1C Two methods of computing the additional gross profit from the extra ¼ inch sliced from the backer board are shown. The first method uses averages over all the species. The second method computes on a species by species basis. The results are within $1500 of each other.

1D The extra flitches done per shift are computed using the extra flitches per day and 240 working days per year. The 240 working days is per Amos-Hill. The difference of 20 days between 52 weeks * 5 days per week or 260 and the 240 are holidays and vacation.

1E The next computation is the gross profit from the extra flitches sliced. Only one method is computed here, as the previous gross profit computations were so close.

1F Lastly, the payback (Part 1), net present value (Part 2) and internal rate of return (Part 3) are computed using the additional gross profit from the two previous computations, veneer from the extra ¼ inch of backer board and the extra flitches sliced.

2. **Explain the potential benefits beyond any tangible financial benefits to Amos-Hill that can be achieved by replacing the current slicer with the newer technology. Are there disadvantages, as well?**

Any number of considerations may be discussed here. Certainly, there are other issues besides the dollars-and-cents calculations that must be thought through before the decision is made. While some of these qualitative issues may be quantified, the intent of this question is to have the students look at the larger picture associated with a significant capital. Among these issues are: 1) the veneer quality improvement associated with no "wobble" of the flitch when using the vacuum system as opposed to the hydraulic system, 2) improved safety for the associates as a result of not having to use the knife to steady the flitch during mounting, and 3) the adoption of state-of-the-art technology and its effect on competition and competitiveness.

A potential drawback to the purchase of the new vacuum table relates to the increased production capacity allowed by the upgrade. It is possible that the additional production may overburden other parts of the operation. For example, if production increases dramatically, will the dryer's capacity be exceeded? Or, could the additional trimming and quality inspection cause the need for additional associates? Is there room in the facility for additional finished product?

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Table 1: Previous Year Veneer Processing Data
Amos-Hill Associates, Inc.

Market	Species	Thickness (slices/inch)	Veneer per log foot (sq ft)	Doyle Yield (log ft)	Log Count*	Log Cost $/log ft	Raw Material Cost ($)**	Veneer Price ($/1000 sq ft)
US	Walnut	42	78	110,484	1,132	5.50	607,662	135
Foreign	Walnut	50	85	175,366	2,468	5.50	964,513	135
US	White Oak	42	77	1,123,355	10,141	2.50	2,808,388	104
Foreign	White Oak	43	78	112,875	1,804	2.50	282,188	104
Foreign	Red Oak	42	70	377,106	3,090	1.70	641,080	91
Foreign	Red Oak	43	71	30,190	410	1.70	51,323	91
US	Maple	42	75	99,709	1,649	4.50	448,691	120
Foreign	Maple	50	85	210,583	1,820	4.50	947,624	120
Foreign	Maple	51	85	318,327	5,197	4.50	1,432,472	120
US	Cherry	36	72	147,909	2,037	5.50	813,500	140
Foreign	Cherry	45	80	272,431	2,984	5.50	1,498,371	140
Foreign	Cherry	46	80	306,362	2,934	5.50	1,684,991	140
Foreign	Cherry	50	82	96,451	729	5.50	530,481	140
SUMS				**3,381,148**	**36,395**		**$12,711,280**	
Data provided by Amos Hill, 2005 production metrics								
* Average log = 10 ft long by 16 inches diameter					** Doyle yield * Log cost/log foot			

AN IN-SOURCING DECISION IN THE HEALTH CARE INDUSTRY: SHOULD AN ORTHOPEDIC PRACTICE BUY AN MRI?: A CASE STUDY

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CASE DESCRIPTION

The primary subject matter of this case is a capital budgeting decision. Capital budgeting issues are appropriately discussed in accounting and/or finance disciplines, as well as healthcare management courses. The case and teaching note support the discussion and analysis of several secondary issues, in addition to the quantitative and qualitative factors incorporated in capital budgeting decisions. These issues include, but are not limited to, ethical issues, government policy practices, and sensitivity analysis. The quantitative analysis requires the student to demonstrate an understanding of the complexity that may be involved in determining relevant factors included in a capital budgeting decision, as contrasted with the simplicity of most textbook capital budgeting problems. The case is appropriate for use in junior level classes (level three) and above. There is a great deal of flexibility incorporated in the case, dependent on the instructor's desire to pursue, or not pursue, discussion of the secondary issues. This flexibility makes the case suitable for advanced analysis and discussions at higher course levels, up to and including first year graduate levels (level five). The number of class hours required to teach the case is dependent on the depth explored by the individual professor. However, class hours would be expected to range from one to two hours; preferably over two class meetings. Preparation hours required of the student are expected to average two to four hours.

CASE SYNOPSIS

This case considers the dilemma being confronted by an orthopedic physicians group. The practice is facing shrinking revenues driven by government plans to reduce Medicare reimbursements. In an effort to avoid salary cuts to physicians that appear imminent, members of the practice suggest raising rates to private payers. When this alternative is ruled out, it is decided that an expansion of ancillary services may provide a solution to the dilemma. The primary decision is whether to expand services by in-sourcing the Magnetic Resonance Imaging (MRI) diagnostic tool. Quantitative analysis of this decision requires the student to identify and determine the *projected cash flows, associated with acquiring the MRI, over a twelve year period using net present value analysis. The realism of this decision problem is enhanced due to the fact that the physician's group serves several different classes of customers as well as using the MRI as a diagnostic tool for a variety of ailments/injuries. Each patient group and procedure results in a different reimbursement amount. This analysis is then expanded with two potential alternatives; a ten percent increase in prescribed MRIs or elimination of service to Medicare/Medicaid patients. Students should identify the quantitative impact of acquiring the MRI versus the status quo, as well as the ethical considerations associated with eliminating services to Medicare/Medicaid patients. This addition invites the discussion of business ethics from a stakeholder perspective.*

INSTRUCTORS' NOTES

Recommendations for Teaching Approaches

In the following sections we propose questions to be used in conjunction with the case and offer solutions and suggestions for stimulating classroom discussion.

DISCUSSION QUESTIONS

1. **Calculate the NPV of the project given the current patient mix of POGI and the proposed 800 MRI procedures per year.**

Table 3: Projected MRI Revenue by Procedure Type and Patient Group
(Percentages reflect the proportion of the 800 expected MRIs per year for each procedure and patient type)

		Spines	Knees	Hips	Shoulders	Wrist/arm	C-spine/head	Bi-lateral Knee
Procedure Mix		20%	30%	25%	5%	5%	10%	5%
Patient Mix								
Medicare	25%	$850	$400	$750	$440	$325	$700	$770
Private Pay	40%	$1,084	$538	$918	$640	$452	$1,116	$985
Workers' Comp	20%	$1,020	$480	$900	$528	$390	$840	$924
Medicaid	10%	$550	$285	$475	$350	$225	$225	$550
Uninsured	5%	$434	$215	$367	$256	$181	$446	$394

This table projects the revenue from the 800 expected MRIs by type of MRI and by type of patient. For example, 20% of the MRIs (160) will be of the spine. Of those 160 spine MRIs, 25% (40) will be provided to Medicare patients. The projected reimbursement for a spine MRI for a Medicare patient is $850.

Table 4: Annual Revenue Generated by Procedure and by Patient Group							
Procedure	**Number of Mris**	**Medicare**	**Private Pay**	**Workers' Comp**	**Medicaid**	**Unisured**	**Revenue**
Spines	160	40	64	32	16	8	
Revenue		$34,000	$69,376	$32,640	$8,800	$3,469	$148,285
Knees	240	60	96	48	24	12	
Revenue		$24,000	$51,648	$23,040	$6,840	$2,582	$108,110
Hips	200	50	80	40	20	10	
Revenue		$37,500	$73,440	$36,000	$9,500	$3,672	$160,112
Shoulders	40	10	16	8	4	2	
Revenue		$4,400	$10,240	$4,224	$1,400	$512	$20,776
Wrist/arm	40	10	16	8	4	2	
Revenue		$3,250	$7,232	$3,120	$900	$362	$14,864
C-spine/head	80	20	32	16	8	4	
Revenue		$14,000	$35,712	$13,440	$1,800	$1,786	$66,738
Bi-lateral Knee	40	10	16	8	4	2	
Revenue		$7,700	$15,760	$7,392	$2,200	$788	$33,840
Total Number of Mris	800	200	320	160	80	40	
Total Revenue		$124,850	$263,408	$119,856	$31,440	$13,170	$552,724

This table develops the total annual revenue from each procedure by patient type. The table is developed by multiplying the reimbursement by patient type and procedure in Table 3 for the number of MRIs for each procedure and patient type. For example, the reimbursement rate for a Medicare patient that receives a spine MRI is $850. Forty Medicare patients are projected to receive spine MRIs. Therefore, projected revenue for this procedure and patient type is $850*40 = $34,000

Table 5: Projected Cash Expenses												
Incremental Expenses	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
Tech (full time) wages	$37,440	$38,938	$40,495	$42,115	$43,800	$45,551	$47,374	$49,268	$51,239	$53,289	$55,420	$57,637
Tech (full time) tax and fringe	10,109	10,513	10,934	11,371	11,826	12,299	12,791	13,302	13,835	14,388	14,963	15,562
Malpractice	25,000	26,250	27,563	28,941	30,388	31,907	33,502	35,178	36,936	38,783	40,722	42,758
Film	24,000	24,480	24,970	25,469	25,978	26,498	27,028	27,568	28,120	28,682	29,256	29,841
Maintenance contract / warranty		16,000	16,000	16,000	16,000	20,000	20,000	20,000	20,000	20,000	25,000	25,000
Property Insurance	8,000	8,160	8,323	8,490	8,659	8,833	9,009	9,189	9,373	9,561	9,752	9,947
Training and Cert (average)	2,500	2,600	2,704	2,812	2,925	3,042	3,163	3,290	3,421	3,558	3,701	3,849
Total Incremental Cash Expenses	$107,049	$126,941	$130,988	$135,197	$139,576	$148,130	$152,867	$157,796	$162,925	$168,261	$178,815	$184,594

This table presents the annual operating expenses associated with the acquisition of an MRI. The expenses are determined from the information provided in Table 2 of the case.

Table 6: Projected Before Tax Cash Flows												
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
Projected Revenue	$552,724[a]	$580,360	$609,378	$639,847	$671,839	$705,431	$740,703	$777,738	$816,625	$857,456	$900,329	$945,346
Projected Expenses	$107,049[b]	$126,941	$130,988	$135,197	$139,576	$148,130	$152,867	$157,796	$162,925	$168,261	$178,815	$184,594
Projected Cash Flow	$445,675	$453,419	$478,390	$504,650	$532,264	$557,302	$587,836	$619,942	$653,700	$689,195	$721,515	$760,751

This table provides the projected cash flows associated with acquiring the MRI machine and serving 800 patients annually.
[a] Year 1 projected revenue is determined in Table 4. Revenue (reimbursement) is expected to increase 1.5% per year.
[b] Projected expenses were determined in Table 5.

Table 7: Net Present Value Analysis							
Year	Before Tax Cash Flow	Depreciation	Taxable Income	Tax Expense	After Tax Cash Flow	Pv Factor	Discounted after Tax Cash Flow
0	($1,375,000)					1	($1,375,000)
1	445,675	$275,000	$170,675	$59,736	$385,939		
2	453,419	$440,000	13,419	$4,697	448,722		
3	478,390	$264,000	214,390	$75,037	403,354		
4	504,650	$158,400	346,250	$121,188	383,463		
5	532,264	$158,400	373,864	$130,852	401,412		
6	557,302	$79,200	478,102	$167,336	389,966		
7	587,836	$0	587,836	$205,743	382,093		
8	619,942	$0	619,942	$216,980	402,962		
9	653,700	$0	653,700	$228,795	424,905		
10	689,195	$0	689,195	$241,218	447,977		
11	721,515	$0	721,515	$252,530	468,985		
12	760,751	$0	760,751	$266,263	494,488		
							$3,121,269.68
						NPV =	$1,746,269.68

This table provides the net present value analysis associated with the acquisition of the MRI machine, using a discount rate of 8%.

2. Which of the following would have a more significant impact on the NPV of the project?

a) a ten percent increase in the number of MRI s performed?

The only variable cost associated with the increased number of procedures is the cost of film. The NPV increases by $330,610.

Table 3A: Projected MRI Revenue by Procedure Type and Patient Group (Percentages reflect the proportion of the 880 expected MRIs per year for each procedure and patient type)								
		Spines	Knees	Hips	Shoulders	Wrist/arm	C-spine/head	Bi-lateral Knee
Procedure Mix		20%	30%	25%	5%	5%	10%	5%
Patient Mix								
Medicare	25%	$850	$400	$750	$440	$325	$700	$770
Private Pay	40%	$1,084	$538	$918	$640	$452	$1,116	$985
Workers' Comp	20%	$1,020	$480	$900	$528	$390	$840	$924
Medicaid	10%	$550	$285	$475	$350	$225	$225	$550
Uninsured	5%	$434	$215	$367	$256	$181	$446	$394

This table projects the revenue from the 880 expected MRIs by type of MRI and by type of patient. For example, 20% of the MRIs (176) will be of the spine. Of those 176 spine MRIs , 25% (44) will be provided to Medicare patients. The projected reimbursement for a spine MRI for a Medicare patient is $850.

Table 4A: Revenue Generated by Procedure and by Patient Group [a]

Procedure	Number of MRIs	Medicare	Private Pay	Workers' Comp	Medicaid	Uninsured	Revenue
Spines	176	44	70	35	18	9	
Revenue		$37,400	$76,314	$35,904	$9,680	$3,816	$163,113
Knees	264	66	106	53	26	13	
Revenue		$26,400	$56,813	$25,344	$7,524	$2,841	$118,921
Hips	220	55	88	44	22	11	
Revenue		$41,250	$80,784	$39,600	$10,450	$4,039	$176,123
Shoulders	44	11	18	9	4	2	
Revenue		$4,840	$11,264	$4,646	$1,540	$563	$22,854
Wrist/arm	44	11	18	9	4	2	
Revenue		$3,575	$7,955	$3,432	$990	$398	$16,350
C-spine/head	88	22	35	18	9	4	
Revenue		$15,400	$39,283	$14,784	$1,980	$1,964	$73,411
Bi-lateral Knee	44	11	18	9	4	2	
Revenue		$8,470	$17,336	$8,131	$2,420	$867	$37,224
Total Number of Mris	880	220	352	176	88	44	
Total Revenue		$137,335	$289,749	$131,842	$34,584	$14,487	$607,997

[a] Some revenue amounts are rounded due to truncating.
This table develops the total annual revenue from each procedure by patient type. The table is developed by multiplying the reimbursement by patient type and procedure in Table 3-A for the number of MRIs for each procedure and patient type. For example, the reimbursement rate for a Medicare patient that receives a spine MRI is $850. Forty four Medicare patients are projected to receive spine MRIs. Therefore projected revenue for this procedure and patient type is $850*44 = $37,400

Table 5A: Projected Cash Expenses												
Incremental Expenses	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
Tech (full time) wages	37440	38938	40495	42115	43800	45551	47374	49268	51239	53289	55420	57637
Tech (full time) tax and fringe	10109	10513	10934	11371	11826	12299	12791	13302	13835	14388	14963	15562
Mal-practice	25000	26250	27563	28941	30388	31907	33502	35178	36936	38783	40722	42758
Film	26400	26928	27467	28016	28576	29148	29731	30325	30932	31550	32181	32825
Main-tenance contract / warranty		16000	16000	16000	16000	20000	20000	20000	20000	20000	25000	25000
Property Insurance	8000	8160	8323	8490	8659	8833	9009	9189	9373	9561	9752	9947
Training and Cert (average)	2500	2600	2704	2812	2925	3042	3163	3290	3421	3558	3701	3849
Total Incremental Cash Expenses	109,449	129,389	133,485	137,744	142,173	150,779	155,570	160,553	165,737	171,129	181,740	187,578

This table provides the annual operating expenses associated with the acquisition of an MRI. The expenses are determined from the information provided in Table 2 of the case and applied to the patient/procedure mix in Table 4-A.

Table 6A: Projected Before Tax Cash Flows												
	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
Projected Revenue	607,997[a]	638,397	670,317	703,833	739,024	775,975	814,774	855,513	898,288	943,203	990,363	1,039,881
Projected Expenses	109,449[b]	129,389	133,485	137,744	142,173	150,779	155,570	160,553	165,737	171,129	181,740	187,578
Projected Cash Flow	498,548	509,008	536,832	566,088	596,851	625,196	659,204	694,960	732,552	772,073	808,623	852,303

This table presents the projected cash flows associated with acquiring the MRI machine and serving 880 patients annually.
[a] Year 1 projected revenue is determined in Table 4-A. Revenue (reimbursement) is expected to increase 1.5% per year.

TABLE 7-A
NET PRESENT VALUE ANALYSIS

YEAR	BEFORE TAX CASH FLOW	DEPRECIATION	TAXABLE INCOME	TAX EXPENSE	AFTER TAX CASH FLOW	PV FACTOR	DISCOUNTED AFTER TAX CASH FLOW
0	($1,375,000)					1	($1,375,000)
1	498,548	$275,000	$223,548	$78,242	$420,306		
2	509,008	$440,000	69,008	$24,153	484,855		
3	536,832	$264,000	272,832	$95,491	441,341		
4	566,088	$158,400	407,688	$142,691	423,397		
5	596,851	$158,400	438,451	$153,458	443,393		
6	625,196	$79,200	545,996	$191,099	434,097		
7	659,204	$0	659,204	$230,721	428,483		
8	694,960	$0	694,960	$243,236	451,724		
9	732,552	$0	732,552	$256,393	476,159		
10	772,073	$0	772,073	$270,226	501,847		
11	808,623	$0	808,623	$283,018	525,605		
12	852,303	$0	852,303	$298,306	553,997		

TABLE 7-A NET PRESENT VALUE ANALYSIS							
							$3,451,879.74
					NPV =		$2,076,879.74
This table provides the net present value associated with the acquisition of the MRI machine when 880 patients are served, using a discount rate of 8%.							

b) the elimination of Medicare and Medicaid patients while maintaining the 800 projected MRI procedures per year?

(Assume the 280 MRIs ordered for Medicare and Medicaid patients are replaced by Private Pay patients - 75%, Worker's Comp patients - 20%, and Uninsured patients - 5%.) The NPV increases by $392,352; the 280 Medicare and Medicaid patients are distributed as follows: 210 to private pay, 56 to workers' comp, and 14 to uninsured.

TABLE 3-B
PROJECTED MRI REVENUE BY PROCEDURE TYPE AND PATIENT GROUP
(Percentages reflect the proportion of the 800 expected MRIs per year for each procedure and patient type)

	800	SPINES	KNEES	HIPS	SHOULDERS	WRIST/ARM	C-SPINE/HEAD	BI-LATERAL KNEE
PROCEDURE MIX		20%	30%	25%	5%	5%	10%	5%
PATIENT MIX								
PRIVATE PAY	66%	$1,084	$538	$918	$640	$452	$1,116	$985
WORKERS' COMP	27%	$1,020	$480	$900	$528	$390	$840	$924
UNINSURED	7%	$434	$215	$367	$256	$181	$446	$394

This table projects the revenue from the 800 expected MRIs by type of MRI and by type of patient when Medicare and Medicaid patients are eliminated from the mix. For example, 20% of the MRIs (160) will be of the spine. Of those 160 spine MRIs , 66% (106) will be provided to Private Pay patients. The projected reimbursement for a spine MRI for a Private Pay patient is $1,084.

TABLE 4-B
REVENUE GENERATED BY PROCEDURE AND BY PATIENT GROUP [a]

PROCEDURE	NUMBER OF MRIs	PRIVATE PAY	WORKERS' COMP	UNINSURED	REVENUE
SPINES	160	**106**	**43**	**11**	
REVENUE		$114,904	$44,064	$4,683	$163,651
KNEES	240	159	65	16	
REVENUE		$85,542	$31,104	$3,486	$120,132
HIPS	200	133	54	14	
REVENUE		$121,635	$48,600	$4,957	$175,192
SHOULDERS	40	27	11	3	
REVENUE		$16,960	$5,702	$691	$23,354
WRIST/ARM	40	27	11	3	
REVENUE		$11,978	$4,212	$488	$16,678
C-SPINE/HEAD	80	53	22	5	
REVENUE		$59,148	$18,144	$2,411	$79,703

TABLE 4-B
REVENUE GENERATED BY PROCEDURE AND BY PATIENT GROUP [a]

PROCEDURE	NUMBER OF MRIs	PRIVATE PAY	WORKERS' COMP	UNINSURED	REVENUE
BI-LATERAL KNEE	40	27	11	3	
REVENUE		$26,103	$9,979	$1,064	$37,146
TOTAL NUMBER OF MRIs	800	530	216	54	
TOTAL REVENUE		$436,270	$161,806	$17,780	$615,855

[a] Some revenue amounts are rounded due to truncating.
This table develops the total annual revenue from each procedure by patient type. The table is developed by multiplying the reimbursement by patient type and procedure in Table 3 for the number of MRIs for each procedure and patient type. For example, the reimbursement rate for a Private Pay patient that receives a spine MRI is $1,084. One hundred and six Private Pay patients are projected to receive spine MRIs. Therefore projected revenue for this procedure and patient type is $1,084*106 = $114,904

TABLE 5-B
PROJECTED CASH EXPENSES

Incremental Expenses	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
Tech (full time) wages	$37,440	$38,938	$40,495	$42,115	$43,800	$45,551	$47,374	$49,268	$51,239	$53,289	$55,420	$57,637
Tech (full time) tax and Fringe benefits	10,109	10,513	10,934	11,371	11,826	12,299	12,791	13,302	13,835	14,388	14,963	15,562
Malpractice	25,000	26,250	27,563	28,941	30,388	31,907	33,502	35,178	36,936	38,783	40,722	42,758
Film	24,000	24,480	24,970	25,469	25,978	26,498	27,028	27,568	28,120	28,682	29,256	29,841
Maintenance contract/Warranty		16,000	16,000	16,000	16,000	20,000	20,000	20,000	20,000	20,000	25,000	25,000
Property Insurance	8,000	8,160	8,323	8,490	8,659	8,833	9,009	9,189	9,373	9,561	9,752	9,947
Training and Cert (average)	2,500	2,600	2,704	2,812	2,925	3,042	3,163	3,290	3,421	3,558	3,701	3,849
Total Incremental Cash Expenses	$107,049	$126,941	$130,988	$135,197	$139,576	$148,130	$152,867	$157,796	$162,925	$168,261	$178,815	$184,594

This table presents the annual operating expenses associated with the acquisition of an MRI to serve 800 patients. The expenses are determined from the information provided in Table 2 of the case and applied to the patient/procedure mix in Table 4-B.

TABLE 6-B
PROJECTED BEFORE TAX CASH FLOWS

	Year 1	Year 2	Year 3	Year 4	Year 5	Year 6	Year 7	Year 8	Year 9	Year 10	Year 11	Year 12
PROJECTED REVENUE	615,855[a]	646,648	678,980	712,929	748,576	786,004	825,305	866,570	909,898	955,393	1,003,163	1,053,321
PROJECTED EXPENSES	107,049[b]	126,941	130,988	135,197	139,576	148,130	152,867	157,796	162,925	168,261	178,815	184,594
PROJECTED CASH FLOW	508,806	519,707	547,992	577,732	609,000	637,875	672,437	708,774	746,974	787,132	824,348	868,727

This table provides the projected cash flows associated with acquiring the MRI machine and serving 800 patients annually. In this scenario the patient mix consists of private pay, workers' comp and uninsured patients only.
[a] Year 1 projected revenue is determined in Table 4-B. Revenue (reimbursement) is expected to increase 1.5% per year.
[b] Projected expenses were determined in Table 5-B.

TABLE 7-B NET PRESENT VALUE ANALYSIS							
YEAR	BEFORE TAX CASH FLOW	DEPRECIATION	TAXABLE INCOME	TAX EXPENSE	AFTER TAX CASH FLOW	PV FACTOR	DISCOUNTED AFTER TAX CASH FLOW
0	($1,375,000)					1	($1,375,000)
1	508,806	$275,000	$233,806	$81,832	$426,974		
2	519,707	$440,000	79,707	$27,897	491,810		
3	547,992	$264,000	283,992	$99,397	448,595		
4	577,732	$158,400	419,332	$146,766	430,966		
5	609,000	$158,400	450,600	$157,710	451,290		
6	637,875	$79,200	558,675	$195,536	442,339		
7	672,437	$0	672,437	$235,353	437,084		
8	708,774	$0	708,774	$248,071	460,703		
9	746,974	$0	746,974	$261,441	485,533		
10	787,132	$0	787,132	$275,496	511,636		
11	824,348	$0	824,348	$288,522	535,826		
12	868,727	$0	868,727	$304,054	564,673		
							$3,513,621.81
						NPV =	$2,138,622
					IRR = 31.8%		
						NPV TABLE 7-A	$2,076,880
						DIFFERENCE	$61,742

This table provides the net present value associated with the acquisition of the MRI machine when services are provided to private pay, workers' comp and uninsured patients only. The difference between this second alternative and the first alternative (a 10% increase in MRIs) is also noted.

3. Would the profitability of the investment be significantly impacted if there were a change in cost of capital for the physicians' group?

NPV of the project has been calculated under each scenario using a discount rate of 8%. The Internal Rate of Return (IRR) under each scenario is between 28% and 32%. It would appear that any reasonable discount rate would result in a positive NPV making the analysis insensitive to minor fluctuations in cost of capital. (See Tables 7, 7-A, and 7-B)

4. Will the opportunity to provide "one stop" services improve the quality of care for the patients?

If patients are relieved of the "hassle" of scheduling an MRI appointment at the hospital and having to travel to another facility to receive the diagnostic treatment, patient (customer) satisfaction should increase. Offering the imaging service "in house" could reduce the time usually required to schedule at another facility as well as relieve the patient from providing another medical history at the MRI facility. In addition, the "turn around time" in obtaining readings could be reduced. Each of these factors should enhance the quality of diagnostic treatment as well as the overall patient experience.

5. What do you think that the impact will be on hospitals that provide MRIs at significantly higher prices than that charged by POGI if they acquire a magnet? Is there any potential impact on the long-term quality of care for patients of these hospitals?

Magnetic Resonance Imaging is generally considered to be a profitable service. Hospitals that are burdened with significant overhead costs in addition to the responsibility to provide quality care to indigent patients will resent physicians' groups "pirating" this profitable service. Although hospitals may be unhappy with this situation they are not likely to be in a position to retaliate specifically against this physicians group or patients, thereof. However, if profitable offerings are diminished at the local hospital, the local hospital may have to rethink indigent care, staffing levels, and consider other "cuts" in services in order to remain financially viable. Decisions such as these could, in fact, have a long term impact on the quality of care provided by the affected hospitals.

6. What, if any, ethical issues do you see surrounding the potential acquisition of MRI capabilities by POGI?

One significant ethical issue looming is the potential to "over-prescribe". This may be kept "in check" from at least two different directions. One, private pay insurance company regulation may deter unnecessary MRI orders. Two, most doctors are, in fact, ethical and would not choose to intentionally prescribe unwarranted testing or procedures. A further ethical issue is the long term impact on quality of care provided by the local hospital, as referenced above.

Another ethical issue to consider is with respect to "dropping" Medicare/Medicaid patients from the patient mix. How difficult will it be for these patients to secure alternative care? Recent surveys regarding physicians providing care to the poor report mixed results. Modern Healthcare (Jan. 9, 2006) reports that, in spite of deep cuts in Medicare reimbursement that occurred four years ago and stagnant increases since, the physician in America are not closing doors to Medicare patients. About 73% in 2004-2205 accepted new Medicare patients, a two percentage point increase since the steep cut. The Associated Press reported on March 23, 2006, that the percentage of physicians who serve the poor has dropped to about 67%. As physicians leave solo practices to join large groups they lose control over patient mix and the larger the group the less likely that the poor (Medicaid patients) will be served. The report released by the Center for Studying Health System

Change disclosed that only 62% of physician groups with more than 50 physicians accept Medicare patients.

A proposed cut in Medicare reimbursements of 10.1% was scheduled to be implemented in 2008. In light of proposed cuts, a more recent survey was conducted by the American Medical Association (AMA). They received responses from 2,216 members and nearly 56% of the respondents indicated they would stop accepting any new Medicare patients while 32.8% reported that they were unsure as to whether they could continue seeing their current Medicare patients (Champlin, 2006). A similar survey in Minnesota conducted by the Minnesota Medical Association reported that 53% of the physicians would reduce the number of Medicare patients they treat if a smaller (4.4%) Medicare reimbursement cut went through (Minnesota Medicine, 2007). In addition, the American Academy of Family Physicians reported that 30.5% of internists took no new Medicaid patients in 2005 (Finkelstein, 2006).

Congress passed a "stop gap" measure in December 2007, allowing payments to increase 0.5% and agreed to revisit the issue in June. This is the sixth year in a row that congress has acted to not implement cuts that are required by the sustained growth rate formula (Family Practice Management, 2008). On July 15, 2008, Congress voted to override President Bush's veto of another "stop gap" bill. The 10.1% cut in Medicare reimbursements has been delayed for 18 months with a 0.1% increase allowed for 2008 and 1.1% for 2009 (Cardiology Today). Physicians are subject to the formula-derived cuts but hospitals, insurance companies, and other entities are not, leading practitioners to believe they are being treated unfairly.

Nelson (2005) provides guidance to healthcare professionals when faced with difficult ethical decisions. His decision model is rooted in the concept of procedural justice and suggests the organization's mission and value statements may assist the organization when prioritizing and ranking the cost/benefit to stakeholders. The stakeholder theory advanced in business ethics would suggest that the rights, values, and interests of the individuals and groups affected by the decision must be considered (Mintz and Morris, 2008). In this case the predominant stakeholders are the physicians, the Medicare/Medicaid patients that may be "dropped", the local hospital, and the insurers. Asking students to address the potential issues from the perspectives of these stakeholders will likely result in a lively discussion about the complexity of decisions related to healthcare.

Capital budgeting decisions in the healthcare industry have more recently focused on investment in information systems, particularly in integrated networks (Morrissey, 1997). Morrissey contends that a healthcare facility manager's decision to invest in facilities or services previously focused on the issue of "impact on bottom line". Although profitability is still an important factor, a non economic question is typically included in the decision process; "How will this investment provide a continuum of quality care?" (Addressed in Question 3, above.)

Weiss (2005) offers a number of additional factors to be considered when making a decision to expand services. She suggests that, first, a real need should be identified. Second, a sound cost analysis is required. Hire a consultant to assist not only in identifying the expenses but also to provide input to a lease versus buy decision. (Note that in the quantitative analysis of cash flows, an interest expense is not calculated in determining before tax cash flows associated with the investment. The interest expense is related to the financing decision not the capital budgeting decision. Likewise, evaluating lease versus buy would be the financing decision, not acquisition decision.) Investigate any restrictions from private payer insurance groups; are their patients required to go elsewhere. Assess the additional risk that you are adding by offering the service. The manner in which the new service will be marketed must be considered. And, finally, consult a healthcare attorney prior to adding the service. The Stark II ban prohibits self-referral. (O'Sullivan, 2004.) Noncompliance with the law, particularly with respect to referrals of Medicare/Medicaid patients, whether intentional or not, can result in fines, denial of reimbursements, or both. There are exceptions to the "self-referral" ban and those exceptions are met in this case. The only factor not specifically addressed in the case is that, to meet the provisions of the "exception" requirements, physician compensation cannot be tied to the service, i.e., the number of referrals.

With increasing revenue compression, physicians' groups are seeking alternative means to combat shrinking revenues and increasing costs. This case explores the alternative of expanding ancillary services to include offering MRI diagnostic procedures "in house". The financial issues to be evaluated in this decision, as well as qualitative factors including ethical issues, are considered in this case analysis.

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GETTING FROM A TO B: A CASE STUDY OF HE DELIVERS UNLIMITED, INC.

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CASE DESCRIPTION

The primary subject matter of this case is entrepreneurship. Secondary issues examined include female leadership, the impact of FICO credit scores on interest rates, and for-profit versus non-profit organizational status. The case has a difficulty level of four and is appropriate for senior level courses. The case is designed to be taught in one to two class hours and is expected to require two hours of outside preparation by students.

CASE SYNOPSIS

"I need that money today. No I needed that money yesterday," stated Lisa Smith. Lisa Smith, founder, president, and CEO of HE Delivers Unlimited, Inc. is struggling to make ends meet. The company is beginning its third year of operations and is experiencing financial difficulties. Smith is faced with trying to turn around the company and eradicate its financial woes. Its largest customer is delinquent in submitting payments; and without the timely receipt of these payments, the company does not have enough cash to maintain operations. Smith is attempting to operate the company from owner financed funds and cash from operations. Due to personal financial circumstances in the past, Smith is trying to improve her credit score and does not want to incur additional debt. Accordingly, she has not obtained any external funding and has used cash to make major asset purchases. Furthermore, Smith began operating her company without a business plan. Without timely prepared financial statements, she does not know the financial position of the company and is unable to make sound financial business decisions. Smith has dreams of expanding the company. However, she knows that this will not be possible unless she can improve the company's financial position.

INSTRUCTORS' NOTES

Recommendations for Teaching Approaches

The purpose of this case is to expose students to some of the challenges facing new business owners. This is particularly important since most new ventures fail within their first few years of business. It is recommended that the instructor start the discussion with a clear understanding of why the main issue arose (i.e., "where did things go wrong"?). After addressing the lack of business planning, the instructor could lead the students into discussions about issues that the owner should have focused on in planning that could have eradicated some of her problems. Such discussions could center around resources available (especially to women) to help raise operating capital, debt versus equity financing, the impact of the owner's FICO score on obtaining financing and for-profit vs. non-profit organizational status. Instructors could discuss these issues with the class as a whole or arrange students in groups to research, analyze and present possible solutions to the above issues. In order to effectively analyze this case, students should have background knowledge of entrepreneurship, debt versus equity financing, and forms of business organizations.

Case Overview

This case presents several issues that entrepreneurs may face in starting a new business venture. Exposing students to these situations will make them aware of the challenges they may face when starting businesses in the future, strategies they could use to overcome these challenges and the overall importance of business planning. The case could be used to require students to research funding sources and ways to raise capital, along with organizations that provide support for entrepreneurs. In doing so, students can further discuss the use of debt and equity financing in starting and operating a business. The case also provides a platform to discuss the credit crisis that occurred in 2008, and the significance of having a good FICO credit score for acquiring debt financing. Good credit is a meaningful topic to discuss with college students since credit card companies are active in soliciting them for credit cards. Many students obtain these credit cards without full knowledge of interest rates, payment terms and FICO scores, and consequently end up with bad credit before they graduate from college. Amortization schedules are included in the instructors' note to illustrate the impact that FICO scores and related interest rates can have on interest paid over the life of a loan. The case also discusses steps that should be followed when deciding whether to continue or terminate a failing business.

Learning Objectives

[LO1] *To present challenges facing entrepreneurs and new business ventures.*

[LO2] *To identify funding sources that may be available to entrepreneurs (especially female entrepreneurs).*

[LO3] *To discuss the impact of an entrepreneur's personal credit rating in obtaining debt financing.*

[LO4] *To provide an understanding of the importance of planning before launching a business.*

[LO5] To discuss options for entrepreneurs who want to be a service to the community.

Discussion Questions

1. What are some of the challenges facing entrepreneurs and how can they get help to overcome these challenges? [LO1]

Entrepreneurship is often a very difficult undertaking, and the majority of new businesses fail within the first four years. Starting a new business involves a great deal of risk and sacrifice. Entrepreneurs must decide whether to leave their current career or lifestyle. Many entrepreneurs are knowledgeable about their service or product but lack the skills necessary to operate their business. Challenges facing entrepreneurs include lack of (1) managerial skills necessary to manage employees and the business overall; (2) marketing skills necessary to advertise and promote their business; and (3) financial resources necessary to operate and grow the business.

To help overcome the above challenges and the rapidly growing number of new businesses in the U.S., entrepreneurship education has become a fast growing discipline in colleges and universities in the U.S., and throughout the world. Most business schools offer a course in entrepreneurship while others offer major and minor concentrations in entrepreneurship. Agencies like the U.S. Small Business Administration aid, counsel and assist Americans start, build and grow businesses. Entrepreneurs can also seek help from Small Business Development Centers (SBDC), which are administered by the U.S. Small Business Administration. They provide management assistance and counseling to small business owners. Most SBDCs are located on university campuses and receive a portion of their funding from the university.

2. What are two of the main challenges faced by Smith in this case? [LO1]

(1) The company has a cash flow problem. HE Delivers does not have the financial resources necessary to operate and grow the business (# 3 above). The problem is exasperated by the fact that their largest customer is delinquent in making payments. If the owners are not able to improve the company's cash flow, they may have to terminate the business. The cash flow problem is an underlying result of the lack of business planning.

(2) The company lacks planning. Smith launched the business before developing a business plan and obtaining essential resources. Essential resources for a new venture include basic information about the market and industry, human resources and financial resources; all of which would be included in a business plan.

Furthermore, there are no budgets or timely prepared financial statements. Without timely prepared financial statements, Smith is unable to determine the financial position of the company nor prepare monthly budgets or analyses. Accordingly, she does not know whether rates are sufficient to generate an appropriate amount of revenue or whether expenses are too high. Also, the fact that HE Delivers does not have financial statements could hinder the company from getting a loan. Lenders and potential investors are interested in knowing the financial position of a company before providing funding. They may be interested in knowing the financial position of the company for the past calendar years and also the year-to-date financial position at the loan application date.

3. What are some other problems that the company is experiencing? [LO1]

- The company has not raised/obtained any outside funding.
- Cash is used to make major purchases.
- The owner is hesitant about raising prices to a more reasonable level.
- The company needs a more experienced accountant (internal or external) involved in the organization.
- The company is not using the expertise and skills of the board of directors in the operation of the company (i.e., the CPA on the board of directors should prepare or ensure that financial statements are prepared, the board members should require/prepare a business plan).

4. What financing sources are available to Smith? [LO2]

Entrepreneurs can consider two types of financing: debt financing and equity financing. They can also consider using internal or external funding to operate the business. Debt financing includes interest bearing instruments, which usually require collateral. Equity financing does not require repayment or collateral, rather it allows one to purchase ownership in the company. Internally generated funds can result from profits, the collection of accounts receivable (more quickly), sale of assets, etc. External funds include family, friends, banks, government loan programs and grants, and venture capital.

New ventures usually operate on equity financing. Most new ventures have negative cash flows in the early years of the business and, accordingly, have difficulty obtaining debt financing. Smith has operated the company through self-financing and revenues generated from the operation of the company. In self-financing the company, however, she has increased her personal debt (i.e., refinancing her home).

When attempting to raise money, potential investors want to see that the owners have invested in the business. Owners do not want to lose their money. Investing in the business reflects that they believe in their venture and that they are willing to take the risk to start the business. Due to Smith's limited resources, however, she does not have ample funds to effectively operate and grow the business. In Smith's case, she should research programs that are designed to assist women, minorities and small disadvantaged businesses, such as the Small Business Administration (www.sba.gov), Innovation Research Program (www.sbir.com), SCORE (www.score.com), the Office of Women's Business Ownership (www.sba.gov/aboutsba/sbaprograms/onlinewbc), 8(a) Business Development Program (www.8-a.com), and Women-21.gov (www.women-21.gov). The internet is a valuable tool for obtaining information and finding possible resources.

5. What are Smith's other options for financing until she is able to receive outside funding? [LO2]

- Smith could consider establishing a line of credit and/or overdraft protection at her bank. This would be advantageous because additional funds would be there if she needed it for payroll or other expenses. The money could be repaid when payments are received from customers.
- Other sources of funds Smith might consider include family and friends. Once cash on hand has increased to a reasonable balance, the funds can be repaid.
- Smith can either give Simmeons incentives to pay on time (sales discounts) or she can increase the penalties for late payments. The healthcare customer could be given a discount if they pay within the original 15-day period. The $250 late payment could be increased to motivate the customer to pay on time, and offset the cost for bounced checks. Simmeons is the company's largest customer and Smith does not want to 'rock the boat' and lose them. This company, however, is causing Smith to incur additional expenses and stress.
- Smith can bill parents monthly instead of quarterly for the home-to-school transportation service.
- Smith should consider increasing her rates. Smith is losing money and making her cash flow problem worse if she is charging below market rates. The company will not generate a profit if her revenues are not covering her expenses. Perhaps she can seek to compare her rates with her competitors on a periodic basis.

6. How does Smith's credit rating affect her getting a loan? How would you rank her credit rating, assuming it is 624? [LO3]

Credit ratings have become a prominent issue in the current economy. People with average and below average credit ratings are having difficulties obtaining loans, and when they do, it can be costly. The FICO score, developed by the Fair-Isaac Corporation, is a statistical analysis of different credit data in one's credit files. Such data includes payment history, amounts owed, length of credit history, new credit and types of credit used. The score represents one's creditworthiness, and the likelihood that they will repay their debt. The FICO credit score range is between 300 and 850. While it is difficult to increase FICO scores in the short-term, they can be increased over time by paying bills on time, reducing debt balances, not applying for debt frequently and obtaining additional credit if one has limited credit (not having significant credit can have a negative impact on a FICO score).

The owner did not reveal her exact credit score. Assume, however, that her credit score is 624. Smith has developed a less than average credit rating, which means in the current economy (recession) it may be difficult for her to obtain loans for the business. If she does obtain loans, they will be at a higher interest rate, and will cost the company more money. The impact of a FICO score on interest charges is illustrated below.

For example, a score of 624 would likely qualify for a 30-year fixed-rate mortgage of 7.774 percent. If you increased your score by 51 points to 675 your interest rate would drop to 6.624. Over the life of the loan those 51 points would save you $42,026 in interest charges on a $150,000 mortgage (Bucci, 2002).

Credit card companies are becoming more active in soliciting college students for credit cards. Before graduation, many students will accumulate thousands of dollars of debt and incur bad credit which will follow them for years. A credit score can affect one's car payment, car insurance, house payment and even whether one gets a job. It has become common practice for employers to run credit checks on potential employees. A credit score may reflect to an employer whether you are trustworthy, dependable, can manage a department or handle money reliably.

Students, who have credit cards and/or loans, are encouraged to get copies of their credit reports and credit scores. Individuals are allowed one free credit report from each credit agency a year. Credit scores are available for a nominal fee. The three credit agencies are as follows:

Equifax - www.equifax.com
Experian - www.experian.com
TransUnion - www.transunion.com

All three credit reports can be obtained from the website, www.annualcreditreport.com.

Current U.S. credit score rankings are as follows per www.freecreditscore.com:

Table	
Excellent	750 and up
Good	720 – 749
Fair	660 – 719
Uncertain	620 – 659
Poor	619 or lower

7. Was it wise for Smith to pay additional money monthly in order to repay the company's auto loan quicker? [LO3]

By making additional payments each month, Smith was able to reduce the amount of interest the company paid over the life of the loan. This is the case since all additional amounts, above the scheduled monthly payments, go directly toward the principal. For example, if the company pays an extra $200 per month, the loan can be paid off 12 months earlier, and save $484.80 in interest (see loan amortization schedules at Exhibit 2 and Exhibit 3). Since the second largest factor in determining a FICO score is the amount of debt one owes, lowering the loan balance can help to improve Smith's credit score. The largest factor in determining a FICO score is making payments on time.

On the other hand, by making extra loan payments each month, Smith had less cash to use to pay operating expenses. Even if a company has extra cash on hand in a given month, it is important that owner's establish budgets and consider expenses due in future months. Doing so, could have helped to reduce the company's future cash flow problems. In this case, however, it appears that Smith's fear of not being able to repay the loan caused her to pay additional money per month in order to pay off the loan faster.

8. What type of planning should Smith have engaged in before launching her business? [LO4]

Careful planning is essential to success. Extensive research and planning should occur before launching a new business. Entrepreneurs need marketing information about their product, target group and the geographical area where the business will be located. They should also become familiar with laws, government regulations and taxes to which they will be subject. It is also pertinent that they explore programs that encourage innovation and entrepreneurship.

Once extensive research is performed, a business plan should be developed. Baron and Shane (2005) note that the components of a business plan should include the following basic requirements:

- *What is the basic idea for the new product or service?*
- *Why is the new product useful or appealing – and to whom?*
- *How will the idea for the new venture be realized – what is the overall plan for producing the product, for marketing it, for dealing with existing and future competition?*
- *Who are the entrepreneurs – do they have the required knowledge, experience, and skills to develop this idea and to run a new company?*
- *If the plan is designed to raise money, how much funding is needed, what type of financing is needed, how will it be used, and how will both the entrepreneurs and other persons realize a return on their investment?*

Improving the business venture is a continuous process. After the company begins operations, the owners should redefine their business plan and establish policies and procedures to improve operations and profitability. Owners should periodically analyze and review the financial position of the company, reassess growth and marketing strategies, and reestablish company goals. Exhibit 1 presents a business planning model established by Baron and Shane (2005).

9. Should Smith reconsider her organizational status? [LO5]

Perhaps Smith should reconsider the company's organizational status. A portion of HE Delivers is operating in a charitable capacity by serving a social need. Smith originally established HE Delivers to provide reasonable and dependable transportation to disabled, needy and underprivileged persons. Special (low) rates are given to the disabled as well as to charitable organizations. Smith may find it advantageous to consult with a lawyer and CPA about making the segment of the company that provides transportation to the disabled, low income and underprivileged persons a separate not-for-profit entity. The other segments would remain as a for-profit entity and charge higher/market rates. It is important to realize, however, that even a not-for-profit entity must have positive cash flow to operate effectively.

10. How could Smith benefit from such a change? [LO5]

By establishing a not-for-profit entity to provide transportation service to low income and underprivileged persons, HE Delivers can apply for grants and other sources from foundations, and state and federal governments. These funds would help to provide a service to these persons by subsidizing the reduced rates that are offered them.

11. Should Smith continue the operation of HE Delivers or terminate the business?

In deciding whether to continue or terminate the business, Smith should follow the steps in the business turnaround process.

- First, Smith must detect and analyze her warning signs of trouble and potential bankruptcy. Detecting these signs early and making immediate changes can help improve the operations and cash flow of the company. HE Delivers' warning signs include not having the cash to pay creditors on time, struggling to pay employees on time, bounced checks and charges, and their continued distressed relationship with Simmeons. Other general warning signs of a troubled company include management of finances becomes so lax that no one can explain how money is spent, customers are given large discounts to enhance payments because of poor cash flow, directors cannot document or explain major transactions, key personnel leave the company, suppliers demand payment in cash, payroll taxes are not paid and contracts are accepted below standard amounts to generate cash (Hisrich, Peters & Shepherd 2005, p. 545).
- Second, Smith should seek outside assistance from professional organizations that are established to assist small businesses, such as the Small Business Administration (SBA), Small Business Development Centers, and SCORE. There are also turnaround management consulting firms, such as The Business Finance Turnaround Association, that provide support for struggling companies in hopes of turning them around.
- Third, Smith should consult with an attorney and CPA regarding the business. Many small businesses do not seek the advice of professionals due to the associated high costs. Obtaining professional advice, however, can be instrumental in whether or not a business becomes successful. Smith should take advantage of the attorney and CPA who are on the board of directors for advice on the company.
- Based on the above, Smith has to decide whether the business is worth saving or if it should be terminated. It is pertinent that entrepreneurs not hang on to a company that is going to continuously drain resources with no turnaround in sight. If a turnaround is possible based on gathered advice and information, it is pertinent that Smith establish a plan and a time frame for doing so. If a turnaround does not occur within the established time frame, she should terminate the business.

Failure of a business venture should not be the end for an entrepreneur. History is full of entrepreneurs who failed at numerous ventures before establishing a successful business. Generally, after failing at a business venture, entrepreneurs have a better understanding of the need for planning, research and capital. They can use these lessons to improve their next venture. Possible investors and venture capitalists will not necessarily disregard someone who has failed at a business venture in the past. With a solid business plan, potential investors may assume that the entrepreneur learned from his/her mistakes.

EPILOGUE

At the end of year 3, Smith and Jones decided to terminate HE Delivers, and return to the workforce. They were unable to make ends meet, cash flow was a constant problem, bills were piling up and the days had become too stressful. Smith had refinanced her house and continued to put money into a company that was not profitable. Smith finally decided to throw in the towel and liquidate the business.

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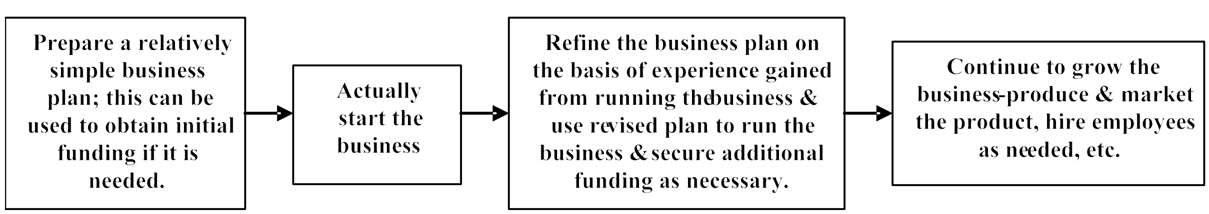
Exhibit 1: A Model of Business Planning Used by Many Successful Entrepreneurs



Source: Baron, R. & S Shane (2005). *Entrepreneurship: A Process Perspective*. Mason, OH: South Western, p.166.

Exhibit 2: Loan Amortization Schedule

$13,750 loan, 6.5% interest, no extra payments

Pymt No.	Payment Date	Beginning Balance	Payment	Extra Payment	Total Payment	Principal	Interest	Ending Balance
1	2/1/2009	$ 13,750.00	$ 421.42	$ -	$ 421.42	$ 346.94	$ 74.48	$ 13,403.06
2	3/1/2009	13,403.06	$ 421.42	-	$ 421.42	348.82	72.60	13,054.24
3	4/1/2009	13,054.24	$ 421.42	-	$ 421.42	350.71	70.71	12,703.53
4	5/1/2009	12,703.53	$ 421.42	-	$ 421.42	352.61	68.81	12,350.92
5	6/1/2009	12,350.92	$ 421.42	-	$ 421.42	354.52	66.90	11,996.40
6	7/1/2009	11,996.40	$ 421.42	-	$ 421.42	356.44	64.98	11,639.96
7	8/1/2009	11,639.96	$ 421.42	-	$ 421.42	358.37	63.05	11,281.59
8	9/1/2009	11,281.59	$ 421.42	-	$ 421.42	360.31	61.11	10,921.28
9	10/1/2009	10,921.28	$ 421.42	-	$ 421.42	362.26	59.16	10,559.02
10	11/1/2009	10,559.02	$ 421.42	-	$ 421.42	364.23	57.19	10,194.79
11	12/1/2009	10,194.79	$ 421.42	-	$ 421.42	366.20	55.22	9,828.59
12	1/1/2010	9,828.59	$ 421.42	-	$ 421.42	368.18	53.24	9,460.41
13	2/1/2010	9,460.41	$ 421.42	-	$ 421.42	370.18	51.24	9,090.23
14	3/1/2010	9,090.23	$ 421.42	-	$ 421.42	372.18	49.24	8,718.05
15	4/1/2010	8,718.05	$ 421.42	-	$ 421.42	374.20	47.22	8,343.85
16	5/1/2010	8,343.85	$ 421.42	-	$ 421.42	376.22	45.20	7,967.63
17	6/1/2010	7,967.63	$ 421.42	-	$ 421.42	378.26	43.16	7,589.37
18	7/1/2010	7,589.37	$ 421.42	-	$ 421.42	380.31	41.11	7,209.06
19	8/1/2010	7,209.06	$ 421.42	-	$ 421.42	382.37	39.05	6,826.69
20	9/1/2010	6,826.69	$ 421.42	-	$ 421.42	384.44	36.98	6,442.25
21	10/1/2010	6,442.25	$ 421.42	-	$ 421.42	386.52	34.90	6,055.73
22	11/1/2010	6,055.73	$ 421.42	-	$ 421.42	388.62	32.80	5,667.11
23	12/1/2010	5,667.11	$ 421.42	-	$ 421.42	390.72	30.70	5,276.39
24	1/1/2011	5,276.39	$ 421.42	-	$ 421.42	392.84	28.58	4,883.55
25	2/1/2011	4,883.55	$ 421.42	-	$ 421.42	394.97	26.45	4,488.58
26	3/1/2011	4,488.58	$ 421.42	-	$ 421.42	397.11	24.31	4,091.47
27	4/1/2011	4,091.47	$ 421.42	-	$ 421.42	399.26	22.16	3,692.21
28	5/1/2011	3,692.21	$ 421.42	-	$ 421.42	401.42	20.00	3,290.79
29	6/1/2011	3,290.79	$ 421.42	-	$ 421.42	403.59	17.83	2,887.20
30	7/1/2011	2,887.20	$ 421.42	-	$ 421.42	405.78	15.64	2,481.42
31	8/1/2011	2,481.42	$ 421.42	-	$ 421.42	407.98	13.44	2,073.44
32	9/1/2011	2,073.44	$ 421.42	-	$ 421.42	410.19	11.23	1,663.25
33	10/1/2011	1,663.25	$ 421.42	-	$ 421.42	412.41	9.01	1,250.84
34	11/1/2011	1,250.84	$ 421.42	-	$ 421.42	414.64	6.78	836.20
35	12/1/2011	836.20	$ 421.42	-	$ 421.42	416.89	4.53	419.31
36	1/1/2012	419.31	$ 421.42	-	$ 421.42	419.31	2.11	0.00
Totals			$ 15,171.12		$ 15,171.12	$ 13,750.00	$ 1,421.12	

Exhibit 3: Loan Amortization Schedule

$13,750 loan, 6.5% interest, $200 extra paid per month

Pymt No.	Payment Date	Beginning Balance	Payment	Extra Payment	Total Payment	Principal	Interest	Ending Balance
1	2/1/2009	$ 13,750.00	$ 421.42	$ 200.00	$ 621.42	$ 546.94	$ 74.48	$ 13,203.06
2	3/1/2009	13,203.06	421.42	200.00	621.42	549.91	71.52	12,653.15
3	4/1/2009	12,653.15	421.42	200.00	621.42	552.89	68.53	12,100.26
4	5/1/2009	12,100.26	421.42	200.00	621.42	555.88	65.54	11,544.38
5	6/1/2009	11,544.38	421.42	200.00	621.42	558.89	62.53	10,985.49
6	7/1/2009	10,985.49	421.42	200.00	621.42	561.92	59.50	10,423.57
7	8/1/2009	10,423.57	421.42	200.00	621.42	564.96	56.45	9,858.61
8	9/1/2009	9,858.61	421.42	200.00	621.42	568.02	53.40	9,290.59
9	10/1/2009	9,290.59	421.42	200.00	621.42	571.10	50.32	8,719.49
10	11/1/2009	8,719.49	421.42	200.00	621.42	574.19	47.22	8,145.30
11	12/1/2009	8,145.30	421.42	200.00	621.42	577.30	44.12	7,568.00
12	1/1/2010	7,568.00	421.42	200.00	621.42	580.43	40.99	6,987.57
13	2/1/2010	6,987.57	421.42	200.00	621.42	583.57	37.85	6,404.00
14	3/1/2010	6,404.00	421.42	200.00	621.42	586.74	34.68	5,817.26
15	4/1/2010	5,817.26	421.42	200.00	621.42	589.91	31.51	5,227.35
16	5/1/2010	5,227.35	421.42	200.00	621.42	593.11	28.31	4,634.24
17	6/1/2010	4,634.24	421.42	200.00	621.42	596.32	25.10	4,037.92
18	7/1/2010	4,037.92	421.42	200.00	621.42	599.55	21.86	3,438.37
19	8/1/2010	3,438.37	421.42	200.00	621.42	602.80	18.62	2,835.57
20	9/1/2010	2,835.57	421.42	200.00	621.42	606.06	15.36	2,229.51
21	10/1/2010	2,229.51	421.42	200.00	621.42	609.35	12.08	1,620.16
22	11/1/2010	1,620.16	421.42	200.00	621.42	612.65	8.77	1,007.51
23	12/1/2010	1,007.51	421.42	200.00	621.42	615.97	5.46	391.54
24	1/1/2011	391.54	393.66	0.00	393.66	391.54	2.12	0.00
Totals			$ 10,086.32	$ 4,600.00	$ 14,686.32	$ 13,750.00	$ 936.32	

ACCESSING INTERNATIONAL CAPITAL MARKETS AT SLC

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CASE DESCRIPTION

The primary subject matter of this case is the cost of raising capital internationally. Secondary issues examined include assessing exchange rate exposure and computing the conditional cost of an international debt issue. The case requires students to have an introductory knowledge of accounting, statistics, finance and international business thus the case has a difficulty level of four (senior level) or higher. The case is designed to be taught in one class session of approximately 3 hours and is expected to require 3-4 hours of preparation time from the students.

CASE SYNOPSIS

St. Louis Chemical (SLC) is a regional chemical distributor, headquartered in St. Louis. Don Williams, the President and primary owner, began SLC ten years ago after a successful career in chemical sales and marketing. The company has gradually expanded it product line and network of manufactures. A recent economic downturn in Europe combined with the strengthening of the US dollar has presented an opportunity for SLC to participate in a joint venture with a German Chemical distributor. In order to raise capital for the venture, SLC will need to borrow about $50 million and has an opportunity to issue bonds denominated in US dollars, Euros or Euro/US dollar dual currencies.

INSTRUCTORS' NOTES

Tasks to Be Performed

1. **Williams has asked Thorton to first prepare a series of spreadsheets showing the cash flows associated with each of the three bond issues expressed in terms of US dollars where applicable (using the forward rates provided by Zeutsche Bank). Both investment banks had explained that the up-front fees are deducted from the par value of the bonds. For the US dollar bond, a 1.25% up-front fee totals $625,000 (1.25% of**

the $50 million Par Value). If the bonds are sold at par value, SLC will only receive $49,375,000.

The first bond offering is a $50 million 8.25% semi-annual coupon bond with 5 years to maturity. There is a 1.25% up-front fee and the bond is expected to sell at Par Value. The initial cash received by SLC would be $49.375 million ($50 million minus the up-front fee of $625,000). The semi-annual interest payments are $2.0625 million (calculated as $50 million*8.25% / 2). The repayment at maturity is equal to the $50 million par value of the bond.

US$ Bond Offering	
Year	US$ Cash Flow (millions)
0	49.3750
0.5	-2.0625
1	-2.0625
1.5	-2.0625
2	-2.0625
2.5	-2.0625
3	-2.0625
3.5	-2.0625
4	-2.0625
4.5	-2.0625
5	-52.0625

The second bond offering is a €40 million 7.0% annual coupon Euro denominated Eurobond with a five year maturity. There is a 0.90% up-front fee and the bonds are expected to sell at 101% of Par Value. The up-front fees will total €360,000 (€40 million * 0.009) and the bonds are expected to sell for €40.40 million (€40 million * 1.01). Using an exchange rate of $1.25/Euro, the Euro denominated Eurobond is expected to generate €40.04 million (net of fees) or the equivalent of $50.05 million today. The annual interest payments are €2.8 million. To convert the annual coupon payments into US dollars, the €2.8 million are multiplied by the forward exchange rate provided by Zeutsche Bank. For year 1 the US dollar equivalent would be $3.53416 million (€2.8 million * $1.2622/1EUR). At maturity, the €40 million par value repayment in terms of US dollars would be $53.644 million (€40 million * $1.3411/1EUR).

Straight Euro Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	40.04	1.2500	50.05000
1	-2.80	1.2622	-3.53416
2	-2.80	1.2775	-3.57700
3	-2.80	1.2921	-3.61788
4	-2.80	1.3186	-3.69208
5	-42.80	1.3411	-57.39908

The third bond offering is a €40 million 7.5% annual coupon Euro/US dollar dual-currency Eurobond with a five year maturity. There is a 0.90% up-front fee and the bonds are expected to sell at 99% of Par Value. The up-front fees will total €360,000 (€40 million * 0.009) and the bonds are expected to sell for €39.60 million (€40 million * 0.99). Using an exchange rate of $1.25/Euro, the Euro denominated Eurobond is expected to generate €39.24 million (net of fees) or the equivalent of $49.05 million today. The annual interest payments are €3.0 million. To convert the annual coupon payments into US dollars, the €3.0 million are multiplied by the forward exchange rate provided by Zeutsche Bank. For year 1 the US dollar equivalent would be $3.7866 million (€3.0 million * $1.2622/1EUR). Because of the dual-currency arrangement, $50 million is repaid at maturity.

Euro-USDollar Dual Currency Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	39.24	1.25	49.0500
1	-3.00	1.2622	-3.7866
2	-3.00	1.2775	-3.8325
3	-3.00	1.2921	-3.8763
4	-3.00	1.3186	-3.9558
5	-3.00	1.3411	-54.0233

2. Explain to Williams the primary factors influencing the differences among the initial cash flows for each proposed bond offering (in terms of US dollars) received by SLC.

The primary factors influencing the differences among the initial cash flows for each bond are the up-front fees charges by each investment bank and whether or not the bond is expected to be a premium, discount, or par value bond. The size of all three bond offerings are the same ($50 million is equivalent to €40 million at the stated exchange rate of $1.25/1EUR). However, the straight Euro denominated Eurobond has the largest initial cash flow as the up-front fee is low (0.90%) and the bond is expected to sell at a premium (101% or Par Value). The second largest initial cash flow is generated by the US dollar bond. Although it has a higher up-front fee (1.25% versus 0.90%) compared to the Euro/US dollar dual currency bond, it is expected to sell at Par while the dual currency bond is expected to sell at a discount.

3. Discuss the primary factors influencing the interest (coupon) payments and principle repayment in terms of US dollars made by SLC over the five year life of each bond.

Interest payments are made semi-annually for the US dollar denominated bond versus annually for the Eurobond offerings, but the primary difference would be the coupon rate (7% for the straight Eurobond, 7.5% for the dual currency Eurobond, and 8% for the US dollar bond) and corresponding forward exchange rate. Both Eurobond offerings would have lower annual coupon payments relative to the US dollar bond which has a constant annual payment of $4.125 million. However, the annual coupons payments of the Eurobonds expressed in US dollars are increasing due to the forward rate premiums. For example, the straight Eurobond pays €2.8 million in interest per year and dual-currency Eurobond pays €3.0 million. In year 1, the forward rate is given as $1.2622/1EUR corresponding to payments by SLC of $3.53416 million and $3.7866 million respectively. In year 5, the forward rate is $1.3411/1EUR and the US dollars needed to make the €2.8 million coupon payment and €3.0 million coupon payment increase to $3.75508 million and $4.0233 million respectively.

The principle repayment at maturity is fairly straight-forward for the US bond and the dual-currency Eurobond at $50 million. The straight Euro Eurobond requires a principle repayment of €40 million. When converted into US dollars at a 5-year forward rate of $1.3411/1EUR, the principle repayment on the straight Euro Eurobond issue is $53.644 million.

4. Compare the annualized all-in cost of each bond issue assuming exchange rate risk for the Eurobond issues is hedged using the forward rates provided by Zeutsche Bank. (The annualized all-in cost is the internal rate of return that equates the present value of the future US dollar outlays with today's US dollars received, net of fees.)

The US dollar bond has a periodic Internal Rate of Return of 4.28% per 6-months, so the nominal annual percentage rate (APR) is 8.56% (4.28%*2 = 8.56%). However, an effective annual rate comparison relative to the Eurobond issues would be more appropriate as both Eurobonds are annual coupon bonds. The effective annual rate (or annual percentage yield) is calculated as:

$$\text{Annual Percentage Yield} = (1 + APR/2)^2 - 1.$$

The annual percentage yield of the US bond is 8.74%. Therefore, the appropriate all-in cost of the US bond issue would be 8.74%.

The straight Euro Eurobond issue has an internal rate of return of 8.46%. No adjustment is needed as the coupons are paid annually; therefore the annualized all-in cost of the straight Eurobond is 8.46%.

The Euro/US dollar dual currency Eurobond has an internal rate of return of 8.25%. No adjustment is needed as the coupons are paid annually; therefore the annualized all-in cost of the straight Eurobond is 8.25%.

5. Make a recommendation to Williams assuming the exchange rate risk for the Eurobond issues is hedged using the forward rates provided by Zeutsche Bank.

Both the straight Euro and the Euro/US dollar dual currency bonds are cheaper than the US dollar alternative. The Euro/US dollar dual currency bond offers the lowest all-in annualized cost at 8.25%. The exchange rate risk associated with the interest payments are hedged using the forward rates provided by Zeutsche Bank. The lower up-front fees and the fact that the principle repayment is in US dollars (and not adversely affected by the Euro trading at a forward rate premium) make the dual currency Eurobond the most attractive option.

6. Discuss possible explanations for the difference in fees between the two investment banks.

The lower up-front fees charged by Zeutsche Bank may be part of a relationship banking strategy. Zeutsche Bank may be looking to establish a relationship with SLC via an attractive bond offering in an effort to do other more profitable business with SLC once the joint venture is completed.

7. Discuss the primary differences in the straight Euro Eurobond and Euro/US dollar dual currency Eurobond relative to the US dollar denominated bond from a European investor's point of view.

The relatively lower coupon rate offered on the Eurobond is expected, primarily due to the Euro trading at a forward premium relative to the US dollar. The 28 basis point difference between the US dollar and straight Euro Eurobond issue might be due to credit perceptions between European investors and US investors. The lower coupon rate on the Eurobond issue most likely reflects the Euro trading at a forward premium relative to the US dollar. However, the 49 basis point difference between the US dollar and Euro/US dollar dual currency Eurobond may reflect both differences in credit perspectives between US and European investors and the fact that European investors may want exposure to long-term US dollar risk. A European investor may be speculating that principal repayment in dollars may be worth more Euros than the forward rate implies. If the spot rate on the Euro does not strengthen by as much as the forward rate implies, the European investor's return will exceed the yield implied from the forward rate all-in cost. In exchange for the additional risk, the European investor is receiving a higher coupon relative to the straight Euro Eurobond issue.

8. Assume that Williams decided not to hedge the exchange rate risk with forward rate contracts, but left the Eurobond exposure un-hedged. Use the following exchange rate scenarios:

Scenario A: The Euro is currently trading at \$1.25/1EUR but strengthens relative to the dollar by 3.75% each year for the next 5 years.

Scenario B: The Euro is currently trading at \$1.25/1EUR but weakens by 3.75% each year for the next 5 years

Calculate the all-in cost of each bond issue under each scenario and describe the impact of un-hedged currency exposure on the all-in cost of the US dollar denominated bond, Euro denominated Eurobond and Euro/US dollar dual currency Eurobond.

Scenario A:

US$ Bond Offering	
Year	US$ Cash Flow (millions)
0	49.375
0.5	-2.0625
1	-2.0625
1.5	-2.0625
2	-2.0625
2.5	-2.0625
3	-2.0625
3.5	-2.0625
4	-2.0625
4.5	-2.0625
5	-52.0625

All in cost of the US dollar bond issue is unaffected and remains at 8.75%

Straight Euro Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	40.04	1.2500	50.0500
1	-2.80	1.2969	-3.63125
2	-2.80	1.3455	-3.76742
3	-2.80	1.3960	-3.90870
4	-2.80	1.4483	-4.05528
5	-42.80	1.5026	-64.31234

All in cost increases to 10.99% as the Euro strengthens and requires more US dollars to purchase Euro necessary to repay the bond issue.

Euro-USDollar Dual Currency Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	39.24	1.2500	49.0500
1	-3.00	1.2969	-3.8906
2	-3.00	1.3455	-4.0365
3	-3.00	1.3960	-4.1879
4	-3.00	1.4483	-4.3449
5	-3.00	1.5026	-54.5079

All in cost of the Euro/US dollar dual currency Eurobond increases to 8.82% as the coupon payments are adversely affected by the strengthening of the Euro (the principle repayment is unaffected).

The US dollar bond issue is the most attractive under Scenario A

Scenario B:

US$ Bond Offering	
Year	US$ Cash Flow (millions)
0	49.375
0.5	-2.0625
1	-2.0625
1.5	-2.0625
2	-2.0625
2.5	-2.0625
3	-2.0625
3.5	-2.0625
4	-2.0625
4.5	-2.0625
5	-52.0625

All in cost of the US dollar bond issue is unaffected and remains at 8.75%

Straight Euro Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	40.04	1.2500	50.0500
1	-2.80	1.2031	-3.36875
2	-2.80	1.1580	-3.24242
3	-2.80	1.1146	-3.12083
4	-2.80	1.0728	-3.00380
5	-42.80	1.0326	-44.19341

All in cost decreases to 2.96% as the Euro weakens and requires fewer US dollars to purchase Euro necessary to repay the bond issue.

Euro-USDollar Dual Currency Eurobond			
Year	Euro Cash Flows (millions)	Exchange Rate (US$/1 EUR)	US$ Cash Flow (millions)
0	39.24	1.25	49.0500
1	-3.00	1.2031	-3.6094
2	-3.00	1.1580	-3.4740
3	-3.00	1.1146	-3.3437
4	-3.00	1.0728	-3.2184
5	-3.00	1.0326	-53.0977

All in cost of the Euro/US dollar dual currency Eurobond decreases to 7.20% as the coupon payments are reduced by the weakening of the Euro (the principle repayment is unaffected).

The straight Euro Eurobond issue is the most attractive under Scenario B.

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