Conch republic electronics

Over the years, the company expanded into manufacturing and is now a reputable manufacturer of various electronic Items. Jay Manacles. A recent MBA graduate. Has been hired by the company's finance department. One of the major revenue-producing items manufactured by Conch Republic is a personal digital assistant (PDA). Conch Republic currently has one PDA model on the market, and sales have been excellent. The PDA Is a unique item In that it comes In a variety of tropical colors and Is preprogrammed to play Jimmy Buffet music.

However, as with any electronic Item, technology changes rapidly, and the current PDA has limited features in comparison with newer models. Conch Republic are now considering very seriously the development of a more sophisticated PADS which loud have all the features of the existing PDA but with additional features including cell phone capability and the ability to run different forms of productivity software desired by business, and other users including university students. The capital requirement to develop this new sophisticated PDA was going to be quite significant.

Management has accepted the fact that the financing of this new project would have to be made from existing cash resources and outside finance. Consideration had also to be given in terms of the more appropriate business model to apply. Could the manufacturing of the new unit be made by an out source manufacturing capability to do so. The key issues facing management for this project may be summed up as follows: 1. The Corporate financing risks involved 2. The rate of return expected for the project 3. The rate of return expected by outside investors 4.

The decision making complexities for a project of this nature Without having any specific figures or information to hand you Cay Manacles) are however required to lay out the issues in an informative manner for the Board, who are not well versed in Corporate Finance, but who are required to make a presentation to their shareholders on their future plans. This assignment may require you to make certain assumptions. Please state these assumptions. You should also consider the value of any Corporate Finance techniques or theories that may be applicable in your paper to the Board.

Please DO NOT explains these techniques or theories as you will be assessed on how well you understand and Judge the applicability of these theories. Students who copy from their Finance Text books will fail this assignment Contents 1. 0 Introduction 7 digital assistant (PDA). With fierce competition from other digital manufacturer, it is important that the company to develop a more sophisticated PADS which would have all the features of the existing PDA but with additional features including cell phone capability and the ability to run different forms of productivity software desired by users.

Before launching a new series, the company need to go through the following steps as to ensure a smooth production of this new series. 1. 1 10 steps before launching new products (Brady, 2010) As a business grows the question of the introducing new products/services arises. Launching new products/services means taking risks and managing change. Growth ND change must be managed at the same time as on-going business operations. Maintaining momentum is challenging for small businesses with limited resources.

The business owner looking to introduce new products/services should carefully consider: I. What is the market demand? It. Do customers need the new products/services? Iii. Does the business have manufacturing/servicing, production, storage and distribution capacity and capability? Lb. Can warranty and service requirements be met? V. What is the competition in equivalent products/services? When new product/services are being considered, a business case should be repaper in order to weigh up the pros and cons of the new venture.

Importantly, as well, the return on investment to the business must be calculated. 1. 2 Factors to consider before production The business case should include, but is not limited to: Confirm customer needs and requirements - understand the market 2. Define the product/service and its unique selling point(s) 3. Design (conceptual) or detail the product/service - including quality, safety, compliance and functionality 4. Identify suppliers and understand material supply issues 5. Decide whether to manufacture, assembly or purchase 6.

Calculate the cost of manufacture - including procurement, materials, labor and plant 7. Calculate your price for the product/service - what will the market bears? Is the new product/service commercially viable? 8. Evaluate storage and distribution capacity and capability 9. Calculate lead times to get the product/service to market 10. Identify risks associated with launching a new product 11. Consider internal impacts including staff, financial, other constraints 12. Calculate total cost to the business and expected ROI. (NEWS, 2010) 2. Corporate Financing risks involved 2. 1 Insufficient Capital When launching a new product, it is wise for the company to split the whole project budget and progress. When starting a new division, it is natural impulse to ask for as little as possible in order to avoid an excessive debt load. While it is wise to minimize the risk of debilitating loan payments, insufficient funding creates its own risks for a start-up project. Without adequate capital, a project cannot market its offerings to a sufficiently large customer base.

The owner of a fledgling business also needs to have enough hands to cover the project's expenses until the business generates enough money to support itself. Failure to do so can cause this new business unit / project to prematurely fail. 2. 2 Projection Errors When leasing equipment or borrowing funds, a new start up project must make projections about how much revenue this division is expects to generate. This is a tricky endeavourer because the business unit has not yet started to operate. In addition, business loan proposals must include projections about anticipated expenses.

It may be possible to project the cost of rent and materials with some degree of accuracy, but labor costs are harder to pinpoint, especially with a new Taft. In addition, every new business makes mistakes and deals with unanticipated difficulties. It is impossible to account for all of these possibilities when signing a lease or applying for a loan. 2. 3 Secured Debt Starting up new business unit often uses their own property and assets as collateral when applying for business loans or signing business leases.

Secured debt is easier to obtain and also carries lower interest rates than debt with no assets to guarantee it. However secured debt presents the risk of an entrepreneur losing the assets that the division has agreed to use as collateral. Such situations can be financially catastrophic for an unlucky business owner who runs the risk of losing the entire capital for this project. (Guaranteeing, 2011) As an investor, the required rate of return is one of the factors to consider when selecting securities for your share portfolio.

The required rate of return is the minimum rate of return an investor could accept from an investment, in order to compensate the investor for not investing something today. In other words, an investor invests in an investment today in order to enjoy the benefits and rewards at a later stage. The components of an investor's required rate of return that will compensate the investor for the risk taken are: I. The time value of money during the investment period it. The expected rate of inflation during the investment period iii. The risk involved Risk premium and the associated fundamental sources of risk 3. Risk premium Risk Premium the excess return required by an investor over and above the risk free rate (risk free is risk free because it is backed by the government who is unlikely to ever go bankrupt) earned in a bank or with a government bond as a result of the uncertainty about the expected rate of return. In other words, if there were no required rate of return would equal the risk free rate. 3. 2 Business risk A business does not always have a guarantee of steady income or cash flow and when there is income and cash flow it can fluctuate quite a bit. This makes investing in shares a riskier option than simply putting money in the bank.

But as we have said before, a higher risk means a higher return. For example, Conch Republic Electronics will be launching the new electronics models. Such new electronics may have seasonal highs and lows, but will still receive steady flow of income over any particular business cycle. On the other hand, the microchips supplier company may experience spurts of income on a less frequent basis, and thus its earnings will fluctuate more dramatically over a year. In the latter instance, the business risk is substantially higher for the investor than the former. . 3 Financial risk Financial risk is the uncertainty that relates to how a firm finances its investments. If Conch Republic Electronics uses ordinary shares to finance the company, then this company will be subject to business risk only. Borrowing money from a bank or other inciters involves interest charges being paid by the company before providing income or returns back to the shareholders, thereby increasing the uncertainty of the return to investors. The use of debt creates a fixed financing cost for the company, as interest has to be paid.

The company is therefore exposed to greater risk, as it has to pay its interest. This risk is known as financial risk. 3. 4 Liquidity risk Liquidity risk refers to the uncertainty or ability of the investor to be able to convert an investment into cash in the secondary market, in order to use that cash for other purposes. In other words it's how easy for the investors to sell Conch RepublicElectronics' shares 3. 5 Exchange Rate risk Exchange rate risk is the uncertainty that investors experience when they purchase securities in a currency other than their own domestic currency.

For example, if an investor invests in a Conch Republic Electronics, they will experience exchange rate risk because the stock price for Conch Republic Electronics is link to exchange rate. The more volatile the exchange rate between two countries, the less certain an investor would be regarding the exchange rate, the greater the exchange rate risk, ND therefore the larger the exchange rate risk premium required. 3. 6 Country Risk Country risk or political risk relates to the uncertainty of returns as a result of political issues or changes in a country that may impact upon the economy.

Developed countries such as the USA, I-J and Germany are believed to have relative stability in the political environment and hence are regarded as low risk countries to invest in. However, countries like Zombie and Argentina are developing countries with an unstable political environment and therefore present a high country risk for the potential investor. 3. 7 Risk Premium The risk premium is a composite of all the risk factors mentioned above. Therefore, investors should take all of these issues into consideration when making an liquidity risk within the share market of that country may present a high risk. . 0 Rate of return expected for the project As Conch Republic Electronics is launching new product within the new division, such business environment that causes the division weighted cost of capital (rate of return expected from the project) to be high or low can be effected by four factors namely: general economic conditions, the marketability of the firm's securities (market notations), operating and financing conditions within the company, and the amount of financing needed for new investments. 4. Factor 1: General Economic Conditions General economic conditions determine the demand for and supply of capital within the economy, as well as the level of expected inflation. This economic variable is reflected in the risk less rate of return. This rate represents the rate of return on risk- free investments, such as the interest rate on short-term government securities. In principle, as the demand for money in the economy changes relative to the supply, investors alter their required rate of return.

For example, if the demand for money increases without an equivalent increase in the supply, lenders will raise their required interest rate. At the same time, if inflation is expected to deteriorate the purchasing power of the Euro, investors require a higher rate of return to compensate for this anticipated loss. 4. 2 Factor 2: Market Conditions When an investor purchases a security with significant risk, an opportunity for additional returns is necessary to make the investment attractive. Essentially, as risk increases, the investor requires a higher rate of return. This increase is called a risk remit.

When investors increase the is required rate of return, the cost of capital rises simultaneously. Remember we have defined risk as the potential variability of returns. If the security is not readily marketable when the investor wants to sell, or even if a continuous demand for the security exists but the price varies significantly, an investor will require a relatively high rate of return. Conversely, if a security is readily marketable and its price is reasonably stable, the investor will require a lower rate of return and the company's cost of capital will be lower. 4. Factor 3: Operating ND Financing Decisions Risk, or the variability of returns, also results from decisions made within the company. Risk resulting from these decisions is generally divided into two types: business risk and financial risk. Business risk is the variability in returns on assets and is affected by the company's investment decisions. Financial risk is the increased variability in returns to common stockholders as a result of financing with debt or preferred stock. As business risk and financial risk increase or decrease, the investor's required rate of return (and the cost of capital) will move in the same erection. . 4 Factor 4: Amount of Financing The last factor determining the corporation's cost of funds is the level of financing that the firm requires. As the financing requirements of the firm become larger, the weighted cost of capital increases for several reasons. For instance, as more securities are issued, additional flotation costs, or the cost incurred by the firm from issuing securities, will affect the percentage cost of the funds to the firm. Also, as management approaches the market for large amounts of capital relative to the firm's size, the investors' required rate of return may rise.

Suppliers of capital become to absorb this capital into the business. This is typically " too much too soon". Also, as the size of the issue increases, there is greater difficulty in placing it in the market without reducing the price of the security, which also increases the firm's cost of capital.