Copenhagen Business School
Handelshøjskolen i København
Solbjerg Plads 3
2000 Frederiksberg

Master's Thesis

Valuation of IC Companys A/S

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Supervisor:

Peter Sehested

Made By:

Umar Sandhu, Cand Merc. FIR (Finance)

Mark Strøm, Cand Merc. IBS (International Business)

Copenhagen Business School
Handelshøjskolen i København
Solbjerg Plads 3
2000 Frederiksberg

Executive Summary

IC Companys A/S is a Danish fashion corporation, which produces 11 designer labels, which are exported to more than 40 countries all over the world. The company was founded in April 2001 through a merger of the clothing company InWear Group A/S and the fashion company Carli Gry International. The company is one of Northern Europe's largest fashion corporations. Their products target quality-conscious men and women, primarily in Scandinavia and EU. Each brand targets a special customer segment. The main part of their sale is via 10,500 wholesale distribution points in more than 40 countries. Furthermore, the company has 259 company-owned shops in 13 countries and 22 factory outlets.

IC Companys experienced a difficult period of time after the merger in 2001. Several years went by before a satisfying result was achieved. The difficulties consisted of managerial and economical challenges. The company has had changes in management and strategies throughout the last 8 years, which have been a contributing factor to the improved results. IC Companys is a cyclical company, which is relatively influenced by macro/micro-economic fluctuations. The company has had unsatisfactory results within the last 1-2 years, partly due to the downturn in both the economy and clothing industry.

The company is operating in a highly competitive market where differentiation is of outmost importance. Their brands are marketed in the mid and high-end price segment. IC Companys has developed a Multi-brand strategy, which in combination with a shared business platform are to increase focus on brand differentiation, customer loyalty, economies of scale and a reduction in costs.

The company has had difficulties in attaining their stated growth objectives. A stated growth objective in 2001 was not reached until 2005 and the growth objective for 2006 has not yet been reached. However, a positive and relatively satisfying development in the growth rate has been achieved in the period of 2004/05 to 2007/08.

The estimated value of IC Companys and its share price will be revealed in the latter part of the report. The estimates have been based on certain assumptions and through this a recommendation of whether or not to buy shares of IC Companys at the current share price will also be presented in the end of the report.

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1. Introduction

"The global financial downturn/crisis affects the fashion clothing company IC Companys – due to more and more limited personal finances the customers are falling away"[1].

"IC Companys again disappoints its investors and downgrades the expectations of the financial year 2007/2008"[2].

These are just some of many headlines, which have reached the media/public in 2008. The volatile situation of the market is expected to continue in the rest of 2009[3].

The fashion house IC Companys suffers from the declining retail sale. Within a year (2007/2008), the shares of IC Companys have decreased by 77%, which means that the market value of the company has diminished by 4,2 bn DKK. The company is now estimated to have a market value of only 1,2 bn DKK[4]. If comparing the development of the price per share from IC Companys to the index of the OMX Copenhagen 20, the negative development has been far more drastic for IC Companys than OMX Copenhagen 20 throughout 2008.

[1] http://finans.tv2.dk/nyheder/article.php?id=15675496 – translated to English
[2] http://finans.tv2.dk/nyheder/article.php?id=11578009 – translated to English
[3] http://www.business.dk/article/20081119/detail/81119023/
[4] http://www.business.dk/article/20081119/borsnyt/81119065/ & http://www.business.dk/article/20081002/borsnyt/81002142/
[5] http://borsen.dk/virksomhed/ic_companys

IC Companys is a relatively new company, which came into existence by a merger of the clothing company InWear Group A/S and the fashion company Carli Gry International in 2001[5]. Even though IC Companys only has existed for 8 years its historical roots go much deeper.

The company is one of Northern Europe's largest fashion corporations, which design, produce and offer fashion and leisurewear. It represents labels such as Peak Performance, InWear, Tiger of Sweden, Matinique, Jackpot, Cottonfield, Part Two and Soaked in Luxury[6].

We have found IC Companys to be an interesting company to analyze and to valuate due to its managerial and economical challenges. It will also be interesting to look into the line of business in which IC Companys operates, where it is crucial to constantly be in forefront with innovation, product development and branding. Due to the company's high quality products and line of business, in which it operates, IC Companys is very exposed to fluctuations in the economy. Since the merger in 2001, the company share has been rather volatile, partially attributable to the state of market. The price per share was 77 DKK in 2001 and declined to 23 DKK ultimo 2002. For 2003 and 2004 the value was

[5] http://finans.tv2.dk/nyheder/article.php?id=8456359

[6] http://www.business.dk/article/20080625/medier/80625032/ & homepage of IC Companys

approximately 30-40 DKK, per share, until it in June 2005 was traded at 275 DKK. The price increased to 345 DKK in 2006 and decreased to 318 DKK in 2007. Since then, the price per share has declined to a value of 46 DKK in February 2009[7]. Despite the effect of this historic development in market conditions/external factors, the company's performance has also been influenced by internal challenges/barriers[8], which is to be taken into consideration when analyzing/evaluating IC Companys. Both their strategic and financial situation has changed since the merger in 2001. It is therefore essential to look into the last 8 years of business in order to optimize the estimate of the valuation of IC Companys.

1.1 Problem Statement

The goal of this master thesis is to estimate the value of IC Companys. In order to make this possible, a strategic and financial analysis is to be made.

Strategic analysis:

The strategic analysis serves the purpose of analyzing the firm, its operations, its internal- and external environment and its strategy - how it creates value and how it plans to create value in the future. Elements, which have an impact on IC Companys current/future growth and earnings potential, will hereby be presented and evaluated. The strategic analysis is to answer following questions:

- What/How are the core competences of IC Companys? - define and evaluate IC Companys core competences.
- How will the internal- and external environment influence the ability of IC Companys to create value?
- How is IC Companys competitive situation?

[7] Annual Reports of IC Companys from 01/02 – 07/08, http://borsen.dk/virksomhed/ic_companys, homepage of IC Companys
[8] Annual Reports of IC Companys from 01/02 – 07/08

- How is the composition of the company's product portfolio in relation to future earnings and generation of liquidity?
- What/How are the historic and present growth- and earnings strategies of the company and are they to be followed in the future?

Financial analysis:

The financial analysis will look into the profitability, risk and growth of IC Companys. Further, an examination of the earnings capacity, liquidity and financing of the company will also be made. Historical financial information will be analyzed to be able to forecast the future financial performance of IC Companys. The financial information is collected from the annual reports of IC Companys with a time-span of 5 years, 2003/04 – 2007/08. The financial year of IC Companys is from 1st of July to 30th of June the following year.

The financial analysis is to answer following questions:

- Are the annual reports directly comparable for the chosen time-period, 2003/04 – 2007/08?
- Are the requirements of the accounting policies of IC Companys fulfilled for the purpose of analysis?
- How has the profitability of IC Companys developed through the period in question, 2003/04 – 2007/08?
- How have both the operating and financial risk of IC Companys developed through the given period?
- How has the development of growth of IC Companys been in this specific time-period?
- Focusing on 2003/04 – 2007/08, how can the results of IC Companys be categorized, as transitory or permanent profit?
- How has the development of liquidity and financing been in the period 2003/04 – 2007/08?

Valuation:

The strategic and financial analysis is used to forecast for the future and value IC Companys. Through the valuation certain questions are to be answered:

- Which required rate of return is expected by the owners?
- Which level of required rate of return should an investor of IC Companys expect?
- Which theoretical model is the most suitable/applicable for the valuation of IC Companys?
- What is the market value of IC Companys?
- How is the level of the estimated value in comparison to the actual market price?
- Which parameters in the applied model of valuation are the most significant and how price sensitive is the share of IC Companys if a parameter is changed/adjusted?

1.2 Methodology

The gathering of information/data will primarily be focused on sources, which are publicly available such as the Annual Reports of IC Companys 2001/02 – 2007/08, the homepage of IC Companys, different external articles, stock analyses and statistics. Theoretical articles and additional information concerning the industry, in which IC Companys operates, will be retrieved through the CBS Library. Further, the applied theory and models are taken from material used at lectures at Cand. Merc. FIR (Finance) and Cand. Merc IBS (International Business).

The theory and models applied in this dissertation will briefly be described in the following. A more profound evaluation of the models/theory will be presented in the sections, in which they are applied.

Apart from the Problem formulation, the report consists of 5 main parts. As introduction, a description of IC Companys will be made. Subsequently, the strategic and financial analysis will be presented, followed by a valuation and conclusion of the problem statement.

The introduction to IC Companys will include:

- A brief description of IC Companys and its business
- A chronological outlining of IC Companys strategic and financial highlights from the merger in 2001 to 2008.

This information will be used for the final part of the strategic analysis and the end conclusion for the report. An analysis/evaluation of the strategic initiatives compared to the financial performance will be conducted.

The purpose of the strategic analysis is to look into how certain factors affect the value creation of the company. The strategic analysis is divided in two parts, an internal and external. The internal part covers a description/analysis of IC Companys' line of business and the development of this. A Value Chain Analysis (Michael Porter) is applied to look into the value creation and internal competences of IC Companys. The chosen strategies of a company are based on the internal competences/processes.

The external part comprises a PEST and Porters Five Forces analysis. The PEST is a socio-economic analysis, which is used to establish and interpret the political, economic, social, technological, ecological and legal factors. These factors can influence the ability of a company to create value in the future. The model of Porter's Five Forces looks into the conditions of the industry, in which IC Companys operates and provides a perspective on IC Companys competitive situation. Further, a market segmentation of IC Companys' product portfolio will also be made. It will then be possible to classify the position of each brand/product in relation to target group, fashion and profit. In addition, a correspondingly market segmentation of the competitors brands will be made. This will substantiate the analysis of the competition between the separate brands.

To sum up on the strategic analysis the SWOT model will be applied. This will provide an overview of the strengths, weaknesses, opportunities and threats, which IC Companys is confronted by both internally as well as externally. Further, an evaluation of IC Companys strategies will end the strategic analysis. Here the idea or philosophy of the models of Porters Generic Strategies and Ansoffs Growth

Matrix will be borne in mind when evaluating the strategies (The models are presented in the appendix 1.11)[9].

The financial analysis will be based on the last 5 financial years, 2003/04 – 2007/08. The analysis will primarily be based on a group-level or if relevant/possible on a segment-level. As mentioned earlier, the analysis will consist of the following main parts; profitability, risk, growth and liquidity & financing.

To analyze the profitability of IC Companys, the focus will be on the earnings capacity compared with the development in activities/operations. Further, the return on equity and elements such as return on capital employed (ROCE), financial leverage and spread will be looked into.

The purpose of risk assessment is to estimate whether or not the earnings of IC Companys will end as expected. The analysis is conducted by evaluating the variability in the earnings of IC Companys. Since the total risk of IC Companys can be expressed through both the operating- and financial risk, these are the components, which will be focused on.

The growth aspect will be covered through an examination of the change in equity and the development of funds generated from operations and permanent profits.

The liquidity & financing section will concern the earnings-capability and here the reformulated cashflow statements will be used.

The strategic and financial analysis will be conducted in order to valuate IC Companys. The valuation will be based on the realized financial figures for the last 5 years, 2003/04 – 2007/08 and the expectations to the future development. Specific subjects and models will be looked into:

The required rate of return of the owners will be based on the CAPM-model. This is an economic model for valuing stocks, securities, derivatives and/or assets by relating risk and expected return. It is

[9] Source: ”The Strategy Process” – concepts, contexts & cases, Global 4th edition, Mintzberg, Lampel, Quinn & Ghoshal, 2003

based on the idea that investors demand additional expected return (risk premium) it they are asked to accept additional risk[10].

The Residual Income Model will also be applied to calculate the residual income. This refers to the abnormal earnings (economic profit), which is defined as profit after tax and interest less cost of capital (equity)[11]. The model will be used for the calculation of the value of IC Companys.

The valuation is primarily based on subjective evaluations and different parameters. To evaluate the significance of the parameters, a sensitivity analysis will be performed – if a parameter is changed how will it affect the price of the share?

Additionally, an analysis of other factors, which can have an effect on the value of the company and the future potential of IC Companys will be looked into.

To estimate the market value, an additional valuation model will be applied – multiples.

The partial conclusions for the strategic and financial analyses are made in the end of the report. In addition, the end conclusion will link the different analyses together and answer the Problem Statement of the report.

1.3 Delimitations

The target group of this report is set to being a potential investor of IC Companys. As mentioned earlier, the gathering of information/data will therefore primarily consist of material available to the public. Due to the chosen target group, interviews will not be conducted to retrieve further information.

The dissertation is based on the application of certain models/theories. This means that chosen/given parameters and subjective evaluations are used to determine the end results. Other possible models/theories are therefore neglected, which might have lead to a different conclusion of the report.

[10] http://www.valuebasedmanagement.net/methods_capm.html
[11] Regnskabsordbogen – Engelsk/Dansk – Sandro Nielsen, Lise Mourier, Henning Bergenholtz, 2007

This has been considered beforehand and the different models/theories have been thoroughly evaluated in order to find the most relevant and optimal method/solution.

The period before the merger of IC Companys in 2001, when the clothing company InWear Group A/S and the fashion company Carli Gry International were separate, will not be looked into. The focus will be on the period of 2001 – 2008 and on future forecasts/prospects of IC Companys.

2. Introduction to IC Companys

IC Companys A/S is a Danish fashion corporation, which produces 11 designer labels, which are exported to more than 40 countries all over the world. The company was founded in April 2001 through a merger of the clothing company InWear Group A/S and the fashion company Carli Gry International. The company is one of Northern Europe's largest fashion corporations with 16 subsidiaries in Denmark, Sweden, Norway, Finland, Great Britain, Ireland, Germany, Holland, Belgium, Austria, France, Poland, Czech Republic, Hungary, Canada and China. The head office is located in Copenhagen and in 2007/08 (financial year of IC Companys), the company attained revenue of DKK 3,737 million. IC Companys employs approximately 2,200 people (ultimo 2008). The corporation designs and sells a strong product portfolio of clothing targeting quality-conscious women and men under the brands/labels of Peak Performance, InWear, Tiger of Sweden, Matinique, Jackpot, Cottonfield, Part Two, Saint Tropez, By Malene Birger, Soaked in Luxury and Designers Remix Collection. Each brand targets a special customer segment. The main/key markets of IC Companys are Europe, Canada and Hong Kong. The company is listed on OMX Nordic Exchange Copenhagen and has been since primo May 2001. At 30th of June 2008 the ownership structure was as follows[12]:

Shareholders	Number of Shares	Capital & Votes
Friheden Invest A/S (Niels Martinsen)	6,983,892	39.0%
Danish Labour Market Capital Pension Fund (ATP)	2,000,788	11.2%
Other Danish Institutional Shareholders	2,908,314	16.2%
Danish Private Shareholders	2,578,468	14.4%
Foreign Institutional Shareholders	1,428,097	8.0%
Foreign Private Shareholders	143,543	0.8%
Treasury Shares	1,318,882	7.4%
Non Registered Shareholders	557,648	3.1%
Total	**17,919,632**	**100.0%**

The main part of the sale is via 10,500 wholesale distribution points in more than 40 countries. Furthermore, the company has 259 company-owned shops in 13 countries and 22 factory outlets.

[12] Annual Report 2007/08 page 88 – IC Companys

Wholesale revenue recorded DKK 2,497 million and retail (own shops) came in at DKK 1,092 million in revenue in 2007/08[13].

2.1 Strategic and financial highlights of IC Companys – financial year 2001/02

The merger was to create a foundation for profitable growth in a competitive and volatile market. The merger was to lead to significant positive cost-synergies. The intentions and background for a merger was also to have IC Companys become a strong international player. Compared to the two individual firms, InWear Group A/S and Carli Gry International, the merger of IC Companys was to result in:

- stronger product portfolio
- consolidated market position
- significant synergies and economies of scale
- create foundation for profitable growth
- a strong and more attractive organisation/workplace
- an interesting and attractive investment opportunity

The vision of the merger was to establish one of Europe's leading multibrand clothing/fashion companies and the strategy was to:

- Create a strong portfolio of designer clothes/labels through buying and own product development
- Strengthen Wholesale and Retail through separate divisionalization
- Close down non-profitable departments
- Create a more dynamic and decentralized organisational structure
- Attain significant efficiency-improvements especially for the Supply Chain and Administration departments
- Secure a top-position in all the main markets (Europe, Canada & Hong Kong) of IC Companys

[13] http://www.business.dk/article/20080625/medier/80625032/ , homepage of IC Companys, http://da.wikipedia.org/wiki/IC_Companys, IC Companys A/S Presse- & Analytikerpræsentation 12. marts 2001, Annual Report 2007/08 – IC Companys

At this point in time, 2001, certain trends were present in the market. Markets were stagnating and the dynamics of consumer behaviour were large. The competition was fierce - primarily driven by vertical integration, and in the Retail department an increasing consolidation was occurring. All this lead to a pressure on the earnings capacity/potential, which meant that economies of scale and strong well-positioned brands were of crucial importance[14].

IC Companys aggregated customer-base consisted of more than 4,500 customers and more than 400 concept stores. No customer accounted for more than 2% of the total revenue and the 10 largest customers represented less than 15% of the total revenue. IC Companys had 7,600 wholesale distribution points, 284 own stores in 17 countries and 25 factory outlets[15]. In this financial year (2001/02) of IC Companys, the total staff went from 2,500 to 2,100 employees, a decrease of 400 people.

IC Companys achieved total revenue of 2,915 mill. DKK (8% decline compared to the previous year) and an operating income of 134 mill. DKK (growth 32%), corresponding to an EBIT-margin of 4.6% (3.2% increase). Out of the total revenue approx. 90% came from outside of Denmark. The net income of the financial year 2001/02 was approximately 43 mill. DKK (-150 mill. DKK previous year). The financial expectations were realized in this period[16]. The total revenue can be divided between Wholesale, Retail and Factory Outlets. In 2001/02, the Wholesale revenue was 1,778 mill. DKK, which corresponded to a 6% decline in relation to the previous year. Despite the falling revenue, the Wholesale division had managed to maintain a satisfactory segment profit. The segment profit was 332 mill. DKK (359 mill. DKK previous year), corresponding to a profit-margin of 18.7% (19% previous year). The revenue of Retail experienced a decline of 10% to 1,137 mill. DKK. For this, the segment profit was 26 mill. DKK (71 mill. DKK previous year), corresponding to a segment profit margin of 2.6% (6.5% previous year), which were unsatisfactory. The Factory Outlets also had a 10% decline in revenue to 149 mill. DKK. Further, the segment profit was -32 mill. DKK (-47 mill. DKK previous year), which were characterized as unsatisfactory.

[14] IC Companys A/S Presse- & Analytikerpræsentation 12. marts 2001
[15] IC Companys A/S Presse- & Analytikerpræsentation 12. marts 2001 & Annual Report of IC Companys 2001/02
[16] Annual Report of IC Companys 2001/02

The decline in total revenue was caused by a consolidation and re-adjustment of IC Companys' organization, realization of merger synergies, closure of non-profitable Retail stores, termination of Wholesale customers, currency fluctuations and increased pressure on prices.

The goal of management was to have IC Companys achieve a more satisfactory profitability in 3-5 years. The profitability was to become equivalent to comparable companies in the industry[17].

Their mission stated: "We believe in the Scandinavian values of simplicity, honesty, functionality, and innovation as the guiding principle for the development of our activities"[18].

2.2 Strategic and financial highlights of IC Companys – financial year 2002/03[19]

Objectives/goals:

- Increase brand divisionalization to create a platform for profitable revenue growth for each key brand (InWear, Jackpot, Matinique, Cottonfield, Part Two – 5 key brands)
- Upgrade focus on renewed growth and development within IC Companys' key brands. The company has employed a new manager responsible for business development, whom is to continue the ongoing development and implementation of key brands strategies
- Expand the company's franchise function as a new, alternative operating system for third-party concept customers and for own retail stores
- Increase distribution and sales of the company's new and acquired brands (Saint Tropez, Designers Remix Collection, Tiger of Sweden and By Malene Birger)
- Develop and increase focus on the company's new own developed brands ("O by Isabell Kristensen", Edging by InWear and Error)
- Improvement of earnings in the retail-division - through a strengthening of management, store closures and a tightening of purchasing management, merchandising and the core store concept
- Plans to open 8-10 new factory outlets in the following year, 2003/04

[17] Annual Report of IC Companys 2001/02
[18] Annual Report of IC Companys 2001/02 page 9
[19] Annual Report of IC Companys 2002/03

- The development of the European market was still characterized by fierce competition
- Had total revenue of 2,706 mill. DKK (7% decline compared to the previous year) and an operating income of 129 mill. DKK, equivalent to an EBIT-margin of 4.8%, which were approximately the same levels as the previous year. Performance was in line with forecasts, although revenue fell slightly short of expectations. 82% of total revenue came from outside of Denmark. The net income was approximately 1 mill. DKK (43 mill. DKK previous year). The Wholesale revenue fell with 7% to 1,656 mill. DKK, while the segment profit increased from 332 mill. DKK to 395 mill. DKK, corresponding to a profit margin of 23.9% (18.7% previous year). The segment profit was highly satisfactory. The Retail revenue fell with 8% to 1,050 mill. DKK and the segment profit went down from 26 mill. DKK to -42 mill. DKK, which management found very unsatisfactory. In the Factory Outlet division a revenue of 117 mill. DKK (149 mill. DKK previous year) was realized. Further, a negative segment profit of -37 mill. DKK (-32 mill. DKK previous year) was achieved. This was unsatisfactory. The decline in total revenue of the Group was caused by closure of stores, currency fluctuations, weather conditions and loss of market share in a negative market
- The goal of management was still to have IC Companys achieve a more satisfactory profitability in 3-5 years. The profitability was to become equivalent to comparable companies in the industry
- The number of wholesale distribution points increased to 8,600 (previous year 7,600)
- The number of own stores went down to 263 from 284 previous year and factory outlets increased by 5 to 30
- Staff increased to approx. 2,350 employees from 2,100 the previous year
- Still focus on decentralizing the organisational structure where each brand is represented by individual management/control

Their mission stated: “We believe in the Scandinavian values of simplicity, honesty, functionality, and innovation as the guiding principle for the development of our activities as a multi-brand fashion company”[20].

[20] Annual Report of IC Companys 2002/03 page 11

2.3 Strategic and financial highlights of IC Companys – financial year 2003/04[21]

- Total revenue of 2,612 mill. DKK (3% decline from previous year) and a negative EBIT-margin – operating income was -275 mill. DKK. The performance was in accordance with previous stated expectations. The net income was -309 mill. DKK compared to 1 mill. DKK previous year. 82% of sales came from outside of Denmark. Wholesale revenue fell with 2% to 1,607 mill. DKK, while the revenue of Retail fell with 7% to 868 mill. DKK. Factory Outlets had an increase of revenue to 137 mill. DKK (16% increase). The Wholesale division had a segment profit of 166 mill. DKK compared to 377 mill. DKK the previous year. The segment profit for Retail was -71 mill. DKK compared to -51 mill. DKK previous year. The segment profit for Factory Outlets was improved from -32 mill. DKK to -7 mill. DKK, which was positive, but not sufficient. The total revenue of the Group was negatively influenced by store closures, price reductions and currency fluctuations.
- Due to the 2% decline in the wholesale division, a strengthening or improvement of efficiency for this department was decided upon. This was essential since wholesale represented approx. 60% of total revenue
- Improvement of the retail-division and factory outlets since they suffered an aggregated decline of 4% in revenue. Therefore, continue to reduce the number of loss-making stores through closure and conversion into franchise
- Peak Performance becomes a key brand in this period. Now the company has 6 key brands; InWear, Jackpot, Part Two, Cottonfield, Matinique and Peak Performance
- The management of IC Companys states that the increased investment in acquiring and own-developing of new brands the last couple of years has limited the development of 5 of their 6 key brands. Except from Peak Performance (32% increase in sales), all key brands have suffered significant losses in sales (20% decline in 2003/04). Therefore allocate attention to these key brands. Their aim was for the Group's product base to be brands of considerable size with distinctive international potential. Therefore, investments were made in the design and marketing of their key brands InWear, Jackpot, Matinique, Cottonfield and Part Two. IC

[21] Annual Report of IC Companys 2003/04

Companys intended that Peak Performance and Tiger (145% increase in sales for Tiger) was to retain their rate of expansion
- Purchasing- and inventory management was to be reorganized and made more efficient
- Production costs were to be reduced and sales and delivery were to become more efficient and precise.
- The organisational structure of the Group was made simpler in order to enhance performance, impact, dynamics and transparency.
- The number of wholesale distribution points increased from 8,600 to approx. 9,000
- The number of own stores (retail-division) went down from 263 to approx. 200
- Staff decreased from approx. 2,350 employees to 2,000
- Due to the ongoing restructuring of the company, both positive as well as negative deviations from expected results can occur. The management has therefore set a goal, to attain a satisfactory financial outcome within 3 years.

2.4 Strategic and financial highlights of IC Companys – financial year 2004/05[22]

- Revenue of 2,819 mill. DKK – 8% growth compared to previous year.
- EBIT was 158 mill. DKK - approximately 200% increase from previous year.
- Net income has increased from -309 mill. DKK 2003/04 to 172 mill. DKK this year.
- The situation has improved due to increased sales figures, higher gross profit across brands (lower purchasing costs) and advantageous purchasing-currencies.
- All sales channels, Wholesale, Retail and Outlets have realized a significant improvement of earnings.
- The decline in the original key brands, such as Jackpot, InWear, Part Two, Matinique and Cottonfield has stopped. Other brands (Peak Performance, Tiger of Sweden, Saint Tropez, Soaked in Luxury, Designers Remix Collection and By Malene Birger) have had a satisfactory progression with a combined growth of 22% and now makes 42% of total Group revenue and 80% of net profit. Therefore, IC Companys still has increased focus on their original key brands.

[22] Annual Report of IC Companys 2004/05

- A brand-oriented management structure has been implemented, which is different compared to previous functional focus.
- 50 own retail stores have been terminated and 20 converted into franchise.
- Sir of Sweden (Sub-label to Tiger of Sweden) has been sold and Error (own developed brand) has been liquidated in order to enhance focus on other profitable departments.
- Staff decreased by 100 employees to approximately 1.900.
- The Group’s total profit-level in 2004/05 is still slightly dissatisfying in relation to the potential of the industry.
- A new vision for IC Companys strategic foundation is introduced. The starting point is a Multibrand-strategy, which relates to a functional, management-based and commercial division of the Group´s brands at a common platform. It sets requirements in regards to an incremental updating of the brand portfolio for brands, which do not develop satisfactorily or due to other reasons do not fit the portfolio.
- Appointment of a new management and changes in the board.
- A new and more detailed 3-year financial plan is established – Attain a leading international position in the area of development, sales and marketing of fashion clothes and accessories through the Multibrand Strategy, where the customers are offered strong brands with a clear profile and personality.
- The financial goals are based on organic growth for a 3-year planning horizon.
- It is decided - No own developing or acquisition of new brands and no disposal of present brands.
- Wholesale revenue increased by 300 mill. DKK (19%)
- Wholesale now makes 68% of total revenue of the Group.
- The number of Wholesale distribution points increased from 9,000 to 9,173.
- Retail revenue fell by 93 mill. DKK (9%)
- Own stores (Retail) increased by 7 to 207.
- Factory Outlet revenue remained the same level as previous year, 138 mill. DKK.
- IC Companys business model are to generate a surplus of products, which are to be sold through Factory Outlets.

- 82% of total sales came from outside of Denmark.
- The Group´s 8 largest markets, except from Holland, have had a positive revenue development.

2.5 Strategic and financial highlights of IC Companys – financial year 2005/06[23]

- Revenue growth of 7% to 3.022 mill. DKK.
- Operating profit - realized an improvement of 55% to 323 mill. DKK
- Net profit – 224 mill. DKK compared to 203 mill. DKK previous year.
- The progression of IC Companys is primarily due to the growth of both Wholesale and the Retail-division combined with a continuous increase in gross profit.
- Still 82% of total revenue is from outside of Denmark.
- Wholesale revenue experienced 10% growth to 2,098 mill. DKK.
- Retail revenue increased by 3% to 798 mill. DKK. The improvement is due to:
    - More efficient purchasing- and stock management.
    - Overall improvement of operations
    - IC Companys has now achieved a sound state of store-portfolio after planned store closures and store-conversions (franchise)
- Factory Outlets revenue fell with 9% to 126 mill. DKK. – Satisfactory that the surplus of products after season has been diminished. This department is not expected to experience growth.
- The original key brands (InWear, Matinique, Jackpot, Cottonfield and Part Two) have had progress. The other brands (Peak Performance, Tiger of Sweden, Saint Tropez, Soaked in Luxury, Designer Remix Collection and By Malene Birger) have also had a significant improvement compared to previous year.
- The original key brands (see above) makes 54% of total revenue (previous year 58%) and 28% of profit (previous year 20%). The other brands (see above) makes 46% of total revenue (previous year 42%) and 72% of profit (previous year 80%) – thereby improved balance in earnings.

[23] Annual Report of IC Companys 2005/06

- IC Companys has acquired:
  - The distributor of Peak Performance in Norway, Adventure Sport & Leisure AS.
  - One of the Group´s sourcing agents in Turkey.
- The Multi brand strategy sets requirements in regards to an incremental updating of the brand portfolio for brands, which do not develop as expected or due to other reasons do not fit the portfolio any longer. This has lead to a closure of Part Two (Men´s line - PTM) in order to enhance focus on a profitable growth for Part Two Women.
- The shared platform is an essential element of the Group´s strategy. The platform has several central functions, such as sourcing, distribution, sales logistics, HR, IT, marketing, finance and administration. These shared functions enable the utilization of synergies across the different brands. Further, significant cost-advantages for the individual brand are hereby present and it is possible to secure a high product quality and minimize the risk of failure in deliveries to distributors and own stores.
- The sales and marketing department is brand-divided without synergies across brands. This is seen as strong contributor to the ongoing growth and brand-specific business development. The advantages in terms of increased sales, flexibility, ownership and pace are evaluated to exceed traditional cost-advantages of a shared sales force.
- The investments in marketing per brand have increased to 6% of total revenue against 3-4% earlier.
- Investments have been made in refurbishments of showrooms and own stores, sales training and upgrading of sales force, marketing and sales-development across brands and markets.
- Focus has been on the new management structure.
- The HR-department´s effort has increased and is to contribute even more to the development of IC Companys in the near future. The strategy of HR:
  - Organizational- and management development
  - Pre- and Post planning
  - Coaching of management and talents together with team building
  - Training of Sales personnel
  - These strategies are to match the need/competences of the business units and the shared platform. The HR-effort is labelled “IC Academy”.

- Goal – to create a portfolio of strong and independent brands with great personality. In other words, create an organization, which links the individual brands commercial focus with the Group´s costs- and quality advantages through shared operations of sourcing, distribution, sales logistics, HR, IT, marketing, finance and administration. IC Companys is labelled "Home of Fashion Brands".
- The Group´s total level of earnings is still less satisfying compared to the potential of the industry.
- Staff increased by approximately 100 to 2.032 employees.

2.6 Strategic and financial highlights of IC Companys – financial year 2006/07[24]

- Total revenue of 3,354 mill. DKK (14% increase)
- Operating profit – 12% growth to 340 mill. DKK
- All distribution channels have realized a growth in earnings.
- Retail have experienced highest growth in earnings (33%)
- Net profit was 241 mill. DKK, 8% increase.
- Wholesale revenue increased by 10% to 2,308 mill. DKK
- Retail revenue increased by 15% to 915 mill. DKK.
- Factory Outlets revenue grew 4% to 131 mill. DKK. – still focus on diminishing the surplus of products from season.
- Wholesale will continue to be the largest contributor to total revenue.
- Franchise makes 4% out of total revenue.
- The marketing-investments have increased by 10%.
- 81% of total revenue comes from outside of Denmark.
- New financial goals – in a period of 3-5 years, create a business with a yearly organic growth rate of minimum 15% and an earnings capacity (EBIT-margin) of minimum 15%.
- Staff increased by approximately 200 to 2,252 employees.

[24] Annual Report of IC Companys 2006/07

- First year after the merger in 2001, where IC Companys experienced a double-figured growth rate and where revenue exceeded the level from before the merger. IC Companys has achieved their best result so far. Focus is on growth creation and several growth initiatives have been implemented.
- Cottonfield Female has been introduced and the Men´s Line introduced in China.
- Established a customer loyalty programme to connect the customers even more to their brands and stores.
- Employed 132 people for the purpose of sales.
- "Retail Academy" was launched to train and educate the 900 store-employees.
- New financial and strategic objectives (Mission) – "We build successful international fashion brands". Their core competences are the ability to develop international brands.
- Vision – "We want to be the best owner and business support for international fashion brands". To be a competent and develop-oriented support combined with a quality-conscious and cost-focused platform in relation to their brands.
- A continuation of the Multibrand strategy, supported by the shared business-platform.
- Accelerate the growth for Peak Performance, InWear, Tiger of Sweden and By Malene Birger with the relative costs held constant.
- Create a "lever-effect" for Cottonfield, Matinique, Part Two, Soaked in Luxury and Designers Remix Collection by maintaining growth without increasing fixed costs.
- Follow through the re-establishment of Jackpot and re-create growth for Saint Tropez.
- To strengthen and make the shared business platform more efficient.
- To finish the implemented change of management and create a team-based performance culture.

2.7 Strategic and financial highlights of IC Companys – financial year 2007/08[25]

- Total revenue of 3,737 mill. DKK (11% increase).
- Operating profit (EBIT) increased by 3% to 349 mill. DKK.

[25] Annual Report of IC Companys 2007/08

- The result is affected by non-recurring costs amounting to 40 mill. DKK combined, of which writedowns of inventory and fixed assets in the fourth quarter account for 20 mill. DKK.
- Net Profit was 224 mill. DKK (7% decrease)
- Cost development in relation to revenue development did not progress as expected. Deterioration in cost efficiency was experienced.
- IC Companys was not satisfied with the financial performance, as both revenue and earnings in particular was less than expected. This was primarily due to insufficient sales efficiency in Group Wholesale operations, but also Group Retail operations.
- This year was also characterized by uncertainty in regard to the macroeconomic situation in Scandinavia and the rest of Europe.
- 80% of total revenue was generated outside of Denmark and 48% outside Scandinavia.
- Wholesale revenue recorded 2,497 mill. DKK (8% growth).
- Wholesale profit increased by 16% to 419 mill. DKK.
- Retail revenue came in at 1,092 mill. DKK (19% increase).
- Retail profit came to 78 mill. DKK, equivalent to previous year.
- Factory Outlet revenue reached 148 mill. DKK, a growth of 13% compared to previous year.
- Outlet profit came to 21 mill. DKK, approximately equivalent to previous year.
- IC Companys has launched a 3-year investment programme for Jackpot and Cottonfield and expects to open 15-20 new stores in 2008/2009 in Eastern Europe (Poland, the Czech Republic and Hungary).
- Changes in the Executive Board - Niels Mikkelsen was brought in as new CEO, while Chris Bigler, CFO, and subsequently Anders Cleemann, Executive Brand Officer, were appointed members of the Executive Board. The change in the Executive Board was based on the ambition to further strengthen the company's growth and earnings capacity. IC Companys still wants to build international fashion brands on a strong shared platform, but the manner in which the business model is executed will be subject to changes over the next years.
- New member of the Board of Directors was elected – Per Bank.
- The goal of IC Companys remains to create a group that annually achieves a minimum of 15% organic growth and an earnings capacity (EBIT-margin) of a minimum of 15%.

- Sales responsibility is now to a higher extent locally anchored. This is to ensure a clear division of work and inherently strengthen execution skills and ownership. The brand management remains globally responsible for sales performance and will focus on brand positioning, marketing, product development and strategic sales, whereas the operational sales responsibility is placed with the local sales companies.
- A continuation of the Multibrand strategy, supported by the shared business-platform.
- The Group's Leadership Academy was initiated this year. This aims at strengthening the Group's managers' competences, team building and execution skills. A total of 100 middle managers were trained in 2007/2008.
- Staff increased by approximately 200 people to 2,441 employees.
- The Mission, Vision and Values are presented below:

Mission & Vision[26]

- "We are people on a mission which is to build successful international fashion brands".
- "We strive to reach our vision which is to become the best owner and business support for international fashion brands".

Values[27]

"We believe in and support our 4 company values:

- Customer-Driven – Customers know us as proactive
- Reliable – You can count on us, a promise made, is a promise kept
- Ambitious – It's our passion to make fashion great business
- United – People working together, united in fashion

Through these values we will create growth and market value for the benefit of our stakeholders." To support the company vision, IC Companys has set certain objectives:

[26] Homepage of IC Companys – http://www.iccompanys.com/cds/showpage.asp?nodeid=2693&shownodeid=4632
[27] Homepage of IC Companys – http://www.iccompanys.com/cds/showpage.asp?nodeid=2693&shownodeid=4632

- Offer a solid base for brands to grow and expand from
- All brands must have international potential
- Each brand must establish a clear brand identity and earn money in the long term
- Work within the fashion industry

3. Strategic Analysis

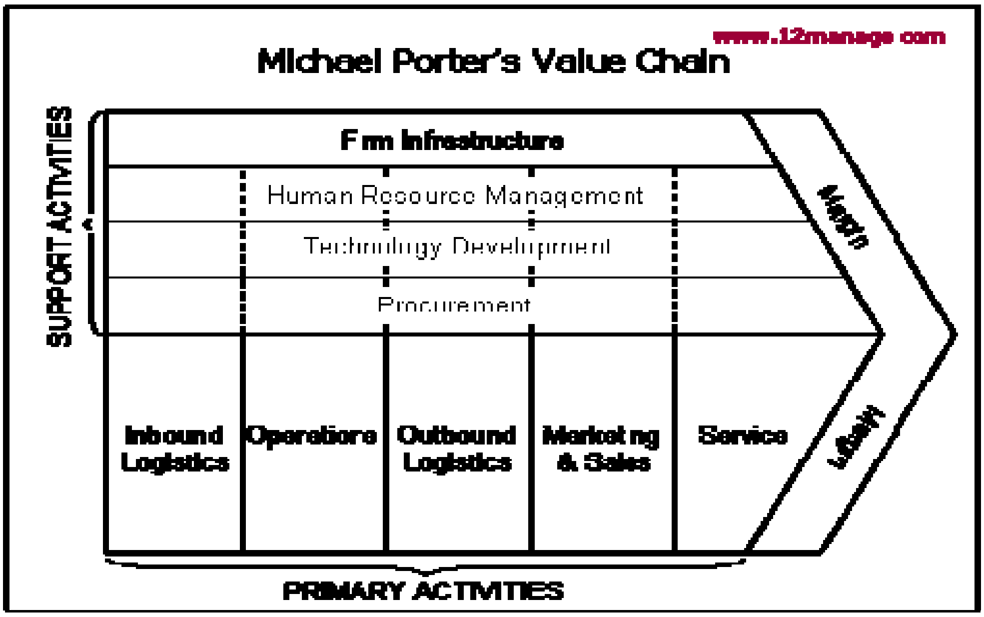
The industry in which IC Companys operates is exposed to customer preferences, why it is impossible to maintain a static strategy 5-10 years ahead. Brands are under a constant development due to the demand of the customers. Each clothes collection has a certain life cycle and has to be sold before it goes out of fashion. As alternative, the surplus can be sent to the Factory Outlets. Though, this will lead to an increase in the cost of logistics and a significant profit is lost, since the clothes will be sold at a discount.

3.1 Value Chain Analysis

The Value Chain Analysis is based on the information available as external analysts.

One of the reasons for a company to outperform its competitors or other comparable corporations can be found in the internal competencies. Here the focus is on the strengths and weaknesses of the Value Chain.

The purpose of the Value Chain Model is to describe the value creation in each link/operation and establish an overview of how the company allocates its resources to the different activities. The Value Chain Model can be divided into primary and support activities, which are illustrated below.



Source: http://www.learnmarketing.net/valuechain.htm and "The Strategy Process",4th ed.,Mintzberg, Lampel, Quinn, Ghoshal, 2003

The primary activities are essential for the firm to develop the competitive advantage. They consist of:

Inbound Logistics – refers to goods being obtained from the organizations suppliers ready to be used for producing the end product.

Operations – the raw materials and goods obtained are manufactured into the final product. Value is added to the product at this stage as it moves through the production line.

Outbound Logistics – once the products have been manufactured they are ready to be distributed to distribution centres, wholesalers, retailers or customers.

Marketing & Sales – Marketing must make sure that the product is targeted towards the correct customer group. The marketing mix is used to establish an effective strategy, any competitive advantage is clearly communicated to the target group by the use of the promotional mix.

Service – after the product/service has been sold what support services does the organization have to offer. This may come in the form of after sales training, guarantees and warranties.

The support activities assist the primary activities in helping the organization achieve its competitive advantage. They include:

Procurement – This department must source raw materials for the organization and obtain the best price for doing so. For the price they must obtain the best possible quality.

Technology Development – the use of technology to obtain a competitive advantage within the organization. This is very important in today's technological driven environment. Technology can be used in production to reduce cost thus add value, or in research and development to develop new products, or via the use of the internet so customers have access to online facilities.

Human Resource Management – the organization will have to recruit, train and develop the correct people for the organization if they are to succeed in their objectives. Staff will have to be motivated and paid the "market rate" if they are to stay with the organization and add value to it over their duration of employment. Within the service sector it is the "staff" who may offer the competitive advantage that is needed within the field.

Firm Infrastructure – every organization needs to ensure that their finances, legal structure and management structure works efficiently and helps drive the organization forward[28].

In regards to inbound logistics and procurement, suppliers have been evaluated and changed and production has been outsourced to more cost-efficient countries[29]. The total production has been outsourced to foreign countries due to several reasons. The main part has been moved to China (60%) and the sourcing of production is managed through independent sourcing offices. The rest of the sourcing is divided between Rumania (13%), Turkey (10%), India (5%) and other countries (12%). These sourcing offices are competing for the purchasing order of the brands of the company and production is thereby moved to where the combination of price, quality and security of delivery is optimal. The 10 largest suppliers represent 27% of the total production value of the company. The

[28] http://www.learnmarketing.net/valuechain.htm - (Michael Porter) Principles of Marketing by Philip Kotler
[29] IC Companys 3rd quarter reports for 2008/09

largest supplier represents 4% of the total production value[30]. This results in less dependency of each supplier and secures a higher level of delivery.

The tendency in cost of freight and raw materials (cotton, wool, polyester, etc.) has also been upward, but has had a minimal effect on cost of purchasing/procurement. (Cost of freight and raw materials represents a minor part of total cost of sales)[31]

In the operations department resources have been allocated to the development of the key brands. IC Companys has a brand portfolio consisting of 11 brands, where 5 five brands (key brands) are "inherited" from the merger. These brands are Jackpot, InWear, Matinique, Cottonfield and Part Two, which are highly concentrated in Scandinavia, Belgium and Holland. An ongoing focus on product development of these brands is present and necessary to, among other things, minimize the fashion risk. The other brands in the portfolio have either been acquired or own-developed. These are By Malene Birger, Peak Performance, Tiger of Sweden, Saint Tropez, Designers Remix Collection, Soaked in Luxury. The last 3 mentioned brands are familiar brands in Scandinavia, Belgium and Holland. For Peak Performance, By Malene Birger and Tiger of Sweden, the expansion is focused on UK, Canada and Southern Europe.

Since clothing collections change a minimum of 4 times a year and have a long lead time, there is a risk that the products will not match the customer preferences (fashion trends) when released in the market[32]. IC Companys has taken some precautions in regards to this. They have integrated a setup, OTB - Open To Buy Sales, which is seasonal sale of clothing with a short delivery time. Efforts will be focused on OTB sales and concerning pre-order sales; this is expected to have a lower growth compared to OTB sales[33].

Concerning outbound logistics, IC Companys has had difficulties in locating and finding local distributors for the continuation of the activities in China and Spain. Therefore, the management has terminated the sales activities in China, while a solution for Spain is still work in progress.

[30] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi
[31] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[32] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[33] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi

The overall distribution strategy is to expand the Retail and Franchise departments. In the future, this means that, these distribution channels will represent a larger part of the total distribution. For this purpose a complete franchise concept has been developed, which is actively applied to attract new franchise partners. Further, an expansion of own stores with specific concepts located in certain countries is prioritized. A new model of cooperation for the Wholesale department is also being implemented. In addition to secure an effective/efficient sale, the new model of cooperation will lower the amount of capital tied up for the Wholesalers as well as for IC Companys[34].

In the sales department IC Companys has developed the retail concepts. The stores are a significant link in the value chain, where the sale to the customers is executed. Therefore it is essential that the stores are presentable and the refurbishment is well-organized. Factors, which can make the buying process (point of sales – POS) a pleasant experience for the customers. Activities in regards to the refurbishment of stores have been outsourced. This is done to increase the company's execution-ability and flexibility for the future and the cost of opening new stores is diminished. Further, the staff/store-employees are educated through "IC Academy (Retail)" to increase sales in stores, loss-making stores has been sold or closed down, and franchising is an essential part of their strategy[35].

IC Companys also sends a message and creates a certain image for the company by preparing the "Code of Conduct", which is a set of rules/guidelines concerning corporate social responsibility (CSR) for their business operations. These considerations and responsibilities can be initiated by a demand from the customers and can contribute to change the perception of the customers and eventually influence the point of sale.

Sales through own stores and the need to carry inventory- and supplementary products for retailers involves a risk that products which, during the year, have been allocated for sale remain unsold at the end of the year. Here the company has the Factory Outlets for the continuous sale of such. Any products that cannot be sold through the Group's own outlets are sold to brokers for resale outside the

[34] IC Companys 3rd quarter reports for 2008/09
[35] IC Companys Annual Reports 2005/06 – 2007/08

Group's established markets. The inventory risk of the Group is reduced by the fact that a considerable part of the total order intake is pre-ordered by the Group's retailers[36].

The Group brands are sold by a total of 12,000 selling points, but no customer accounts for more than 5% of the Group wholesale revenue. (The Group's distributor in Russia is the single largest customer)[37]

Before a customer relationship commences, the Group's wholesale customers are credit rated according to the Group debtor policy and subsequently on a regular basis. Nevertheless, losses do occur. Credit insurance is typically only used in countries in which the credit risk is unusually high and where this is feasible. This primarily applies to export markets in which IC Companys is not represented through an independent sales company. In the past years, the Group had loss on bad debts which was less than 1% of wholesale revenue. In addition, in 2007/08 allowances for bad debts constitute DKK 37 million[38]. It appears that IC Companys has taken their precautions and to a certain extent has the credit aspect under control.

In regards to sale there is a factor, which IC Companys can not control or try to counteract. The weather conditions can affect sales – For example Peak Performance's winter collection will be affected negatively if the winter is mild and since Peak Performance is the largest brand[39], this will have a significant effect on the revenue/profit of the company.

IC Companys has a rather decentralized organizational structure to ease and increase the pace of decision-making in the different departments. Hopefully, this will also contribute to the motivation of the staff/managers, since they will be given a certain amount of trust and responsibility. In order for a decentralized organizational structure to function, the staff/managers have to be well-educated and possess the right competences. This is ensured through the Retail Academy (for the staff) and the Leadership Academy (for managers), where they are evaluated, trained and given the right qualifications for their employment, so they can help drive the organization forward. 900 store employees were trained and educated in 2006/07 and 100 middle managers in 2007/08[40].

[36] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[37] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[38] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[39] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08
[40] IC Companys Annual Reports 2005/06 – 2007/08

3.2 PEST Analysis

The purpose of the PEST Analysis is to investigate if IC Companys is capable of adapting to certain macro-economic factors. It will become clear, which opportunities and threats IC Companys is and will be confronted with, which in the end will have an effect on future profits. The PEST-model is illustrated below:

Source: http://www.mindtools.com/media/Diagrams/PEST.gif - Johnson & Scholes Exploring Corporate Strategy, 2002

The model determines the present and forecasts the future macro-economic situation based on historic factors and developments.

The PEST Analysis will be based on elements, which are essential to IC Companys business operations.

Political/Legal Factors

IC Companys is an international company, which means that political and legal issues are to be monitored nationally as well as internationally. Supply, distribution and sale can be affected by these issues in the countries in which IC Companys is conducting business operations. The main part of their sale is in western countries[41], which are subject to relatively same political factors as Denmark. Their main part of production is in China (60%) and the rest is divided between Rumania (13%), Turkey (10%), India (5%) and other countries (12%)[42]. Differences in culture and political aspects in foreign countries are important to IC Companys. Production has been outsourced due to the lower wages/salaries and some of these countries have specialized in production of clothing. The outsourcing can be connected with a certain commercial risk. Though, as mentioned in the Value Chain Analysis, the 10 largest suppliers represent 27% of the total production value and the largest supplier represents 4%. This is done in order to minimize the commercial risk by creating less dependency of each supplier and securing a higher level of delivery. Though, since 60% of production is outsourced to China, an increase in wages/salaries in China can be deterrent. The wages have increased steadily the last several years, but are still lower compared to Europe, where approximately 30% is produced[43]. Despite the precautions IC Companys has taken, they are still rather exposed to political risk factors in the form of possible regulatory amendments in China, which would affect their business operations severely.

To the advantage of IC Companys in regards to supply and competitiveness, the EU did not extend the quota system for products manufactured in China, which was introduced in the summer of 2005. The quota system has been replaced by a continuous supervision in 2008[44].

Corporations in the apparel industry are to pay attention to how, whom and where their products are being produced, since this industry is characterized by a large part of the products being fabricated in the East, where child labor is far more endemic compared to Europe. In IC Companys' "Code of Conduct" (CSR guidelines) they have among other things treated this issue and put emphasis in

[41] Annual Reports of IC Companys 2001/02 – 2007/08
[42] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2006/07 – 2007/08
[43] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2005/06 – 2007/08
[44] Annual Reports of IC Companys 2007/08

securing that their suppliers are abiding to the rules of child labor[45]. In an analysis of Dansk Erhverv 2007[46] it is stressed that, there is a tendency of more companies to engage in corporate social responsibility. This is both national and international companies. The motivation comes from a moral/ethical responsibility perspective and the fact that, this behaviour can contribute positively to the bottom line (net profit). In general, corporations are expecting this responsibility to become even more significant in the future. The analysis also states that, consumers are willing to pay a higher price for products, which have been produced by companies with focus on corporate social responsibility. It is therefore essential that IC Companys continues to follow their "Code of Conduct" and sends this message to the consumer. Further, IC Companys is a member of and active participant in FashionAid, an initiative started by Federation of Danish Textile & Clothing for the member companies. The initiative is a joint partnership with Danish Red Cross involving donations of garments to relevant areas worldwide. These are defective, though usable products and surplus production. IC Companys expects to donate between 8,000 and 12,000 garments per year through FashionAid[47]. Hopefully, these engagements will create positive PR and result in increased earnings.

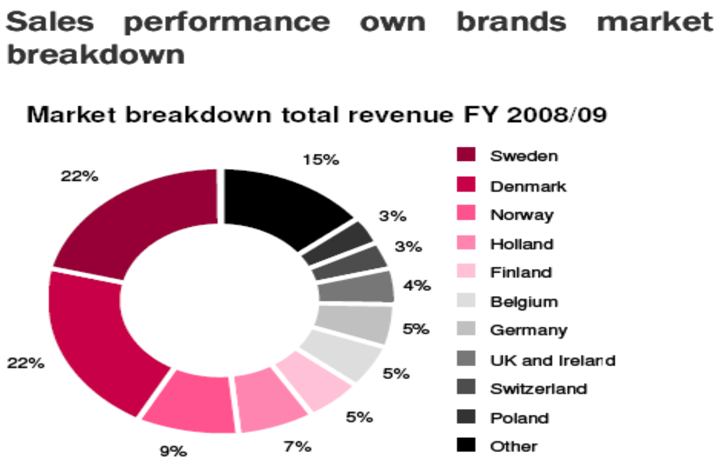
Economic Factors

The sale of IC Companys products is dependent on the development of both the national and international market conditions, of whether or not; the specific countries are experiencing an economic boom or recession. The brands/collections of IC Companys are products, which to a certain extent are characterized as "luxury products" (designer labels), where the sale of these will be affected in a period of growth or recession. In a period of recession, a decline in private consumption in the main markets will impede sales.

IC Companys main market is the European market. Approximately 85% of the total revenue is from countries in Europe. Denmark and Sweden represents 44% of the total revenue combined. The other

[45] Annual Reports of IC Companys 2006/07 – 2007/08
[46] Dansk Erhverv Analyse – Dansk Erhverv undersøgelse 2007, "Forbrugertendens: Stort potentiale for etisk forsvarlige produkter"
[47] Annual Reports of IC Companys 2007/08

markets in Europe are Norway, Holland, Belgium, Finland, Germany, UK & Ireland, Switzerland and Poland[48].



Source: Annual Report of IC Companys 2008/09

This means that, the current state and outlook of the general economy in Europe is crucial to IC Companys. Historically speaking, it has shown that the US economy affects the European economy. Therefore, both the US and Euroland growth forecasts are looked into. Globally, both Japan and China play a part too in regards to the economy. The table below indicates that, global growth rates will improve from 2009 to 2010. Danske Bank Analysis expects the next two to three quarters to be particularly strong. The main factors behind the rapid recovery in the coming quarters are: 1) A very strong inventory cycle; 2) Record stimulus starting to feed through to demand; and 3) Substantial easing of headwinds witnessed by a strong reversal in credit markets. Further, they are cautiously optimistic that the recovery will prove sustainable and expect the job creation to return and hence for consumers to revive[49]. This can be fortuitous circumstances to the business operations of IC Companys. Hopefully, this will result in an increased private spending/consumption of clothing. Though, there are some risk factors to this positive global growth scenario. These mainly stem from higher oil prices, a jobless recovery, renewed financial turmoil or a new sharp rise in the US savings ratio[50].

[48] Annual Report of IC Companys 2008/09
[49] http://www-2.danskebank.dk/danskeanalyse - "Global Scenarios - Rising from the ashes", September 2009
[50] http://www-2.danskebank.dk/danskeanalyse - "Global Scenarios - Rising from the ashes", September 2009

Global growth forecasts

% y/y	2009 Danske Bank	2009 Consensus	2009 IMF	2009 OECD	2010 Danske Bank	2010 Consensus	2010 IMF	2010 OECD
USA	-2.3	-2.6	-2.6	-2.8	3.2	2.3	0.8	0.9
Euroland	-3.7	-4.0	-4.8	-3.9	2.2	0.9	-0.3	0.0
Japan	-5.3	-6.0	-6.0	-5.6	3.0	0.8	1.7	0.7
China	8.5	8.0	7.5	7.7	9.5	8.5	8.5	9.3
Change from previous fcst								
USA	+0.1				+0.5			
Euroland	+0.2				+0.2			
Japan	+0.9				-0.2			
China	+0.0				+0.0			

Source: Danske Markets, Bloomberg, OECD, IMF

Source: http://www-2.danskebank.dk/danskeanalyse - "Global Scenarios - Rising from the ashes", September 2009

The following tables substantiates above forecast. In general, the economy for Euroland and US are going in the right direction. Though, the unemployment rate could be lower.

Macro forecast, Euroland

% Change q/q AR	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	2010 Q2	2010 Q3	2010 Q4	Calendar year average 2008	Calendar year average 2009	Calendar year average 2010
GDP	-9.5	-0.5	1.9	3.1	2.8	1.9	2.0	2.1	0.6	-3.7	2.2
Private Consumption	-2.0	0.7	0.1	0.4	0.6	0.7	0.9	1.1	0.3	-0.3	0.6
Private Fixed Investments	-19.5	-5.0	-1.1	3.2	6.2	3.8	4.5	4.7	-0.7	-9.5	3.2
Change in inventories [1]	-2.7	-3.0	0.9	1.1	0.5	0.1	0.1	0.0	0.1	-0.7	0.3
Public Consumption	2.6	1.8	2.3	2.3	2.1	2.1	2.0	2.0	2.2	2.3	2.1
Exports	-31.0	-4.3	8.0	11.2	6.5	4.2	4.8	5.1	1.1	-13.5	6.1
Imports	-27.8	-10.9	6.2	9.7	6.0	3.8	4.8	5.0	1.1	-11.9	4.9
Net exports [1]	-1.8	2.8	0.7	0.7	0.3	0.2	0.1	0.1	0.0	-1.0	0.5
Unemployment rate (%)	8.8	9.3	9.6	9.9	10.1	10.1	10.0	9.9	7.6	9.4	10.0
CPI (y/y)	1.0	0.2	-0.4	0.3	0.9	1.0	1.3	1.4	3.3	0.3	1.2
Core CPI (y/y)	1.6	1.6	1.2	0.8	0.8	0.8	1.0	1.2	1.8	1.3	1.0
Public Budget [2]									-1.9	-4.7	-5.2
Public Gross Debt [2]									69.3	77.1	82.1
Current Account [2]									-0.8	-1.7	-1.5
ECB refi rate [2]	1.50	1.00	1.00	1.00	1.00	1.25	1.50	2.00	2.50	1.00	2.00

1: Contribution to GDP growth, 2: Pct. of GDP, 3: End of period

Source: Ecowin and Danske Bank projections

Source: http://www-2.danskebank.dk/danskeanalyse

US macro forecast

% Change q/q AR	2009 Q1	2009 Q2	2009 Q3	2009 Q4	2010 Q1	2010 Q2	2010 Q3	2010 Q4	Calendar year average 2008	2009	2010
GDP	-6.4	-1.0	4.6	4.1	4.0	2.2	2.8	3.4	0.4	-2.3	3.2
Private Consumption	0.6	-1.0	2.5	0.0	1.5	2.0	2.5	2.5	-0.2	-0.8	1.5
Private Fixed Investments	-39.0	-13.5	0.4	11.7	15.4	8.1	8.4	10.1	-5.1	-18.0	8.2
Residential	-38.2	-22.8	8.2	36.0	36.0	26.2	21.6	21.6	-22.9	-20.0	23.3
Non-residential	-39.2	-10.9	-1.6	5.6	9.7	2.8	4.4	6.5	1.6	-17.5	3.9
Change in inventories ($bn, rea	-113.9	-159.2	-100.0	-30.0	0.0	0.0	0.0	0.0	-25.9	-100.8	0.0
Change in inventories [1]	-2.3	-1.4	1.8	2.2	0.9	0.0	0.0	0.0	-0.3	-0.6	0.8
Public Consumption	-2.6	6.4	4.1	2.8	1.9	1.9	3.1	2.6	3.1	2.2	2.8
Exports	-29.9	-5.0	4.1	8.2	8.2	4.1	4.1	8.2	5.4	-11.9	5.5
Imports	-36.4	-15.0	3.0	7.2	8.8	8.0	8.0	8.0	-3.2	-16.1	5.8
Net exports [1]	2.6	1.7	0.0	-0.1	-0.3	-0.6	-0.6	-0.2	1.2	1.1	-0.2
Unemployment rate (%)	8.1	9.2	9.6	10.0	9.9	9.6	9.5	9.3	5.8	9.2	9.6
CPI (y/y)	-0.2	-0.9	-1.6	1.6	2.7	2.4	2.1	1.8	3.8	-0.3	2.2
Core CPI (y/y)	1.7	1.8	1.5	1.5	1.3	1.0	0.9	1.1	2.3	1.6	1.1
Public Budget [2]									-3.2	-11.2	-9.6
Public Gross Debt [2]									68	81	87
Current Account [2]									-4.9	-2.7	-2.9
Fed funds rate [3]	0-0.25	0-0.25	0-0.25	0-0.25	0-0.25	0-0.25	0-0.25	0.75			

1: Contribution to GDP growth, 2: Pct. of GDP, 3:End of period

Source: Reuters Ecowin and Danske Markets

Source: http://www-2.danskebank.dk/danskeanalyse

As mentioned, Denmark and Sweden are IC Companys two key markets and represent 44% of total revenue. Norway represents 9% of total revenue. In the table below, a macroeconomic forecast is shown for these three countries. Overall, the scenario looks positive and hopefully this will improve even further in the years to come.

Makroprognose

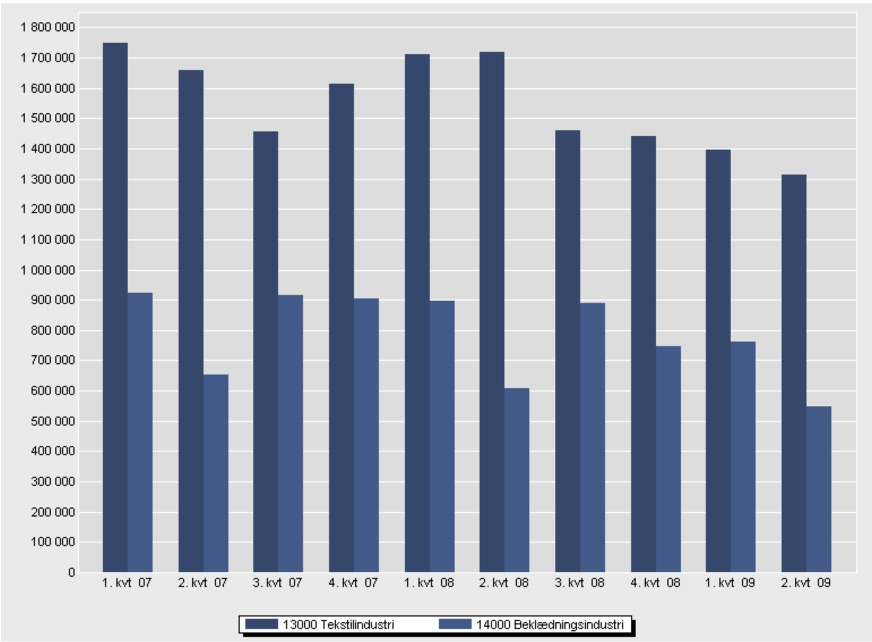
Makroprognose, Skandinavien

	år	BNP[1]	Privat-forb.[1]	Off. forb.[1]	Faste inv.[1]	Lager-inv.[2]	Eks-port[1]	Import[1]	Infla-tion[1]	Ledig-hed[3]	Off. budget[4]	Off. gæld[4]	Betal. bal[4]
Danmark	2008	-1,2	-0,1	1,5	-5,0	0,2	2,3	3,5	3,4	1,8	3,6	33,3	2,2
	2009	-3,5	-3,7	1,7	-11,1	-1,5	-6,1	-9,0	1,3	3,6	-1,5	38,4	1,8
	2010	0,8	2,7	1,6	-2,6	0,2	2,1	3,7	1,9	5,0	-3,8	43,2	1,7
Sverige	2008	-0,8	-0,2	1,5	2,7	-0,6	1,9	3,0	2,2	4,6	2,5	37,5	8,3
	2009	-6,1	-6,1	0,9	-16,9	-1,2	-15,7	-16,1	-0,2	6,2	-1,3	39,6	6,3
	2010	1,1	1,1	1,5	-5,7	0,0	1,8	-0,3	1,3	10,0	-2,7	43,5	6,4
Norge	2008	2.1	1.2	3.8	3.8	0.7	1.3	4.4	3.8	2.6	8.0	26.0	19.0
	2009	-0,3	0,5	5,9	-6,7	-0,1	-5,8	-8,0	2,2	3,5	12,0	26,0	24,9
	2010	2,5	3,6	5,1	2,8	-0,2	0,7	2,3	2,3	4,0	13,9	26,0	24,8

Source: http://www-2.danskebank.dk/danskeanalyse

Below is shown a graph, which illustrates that the revenue of the textile/clothing industry in Denmark has followed the economic downturn in Denmark from 2nd half of 2008. This is where the economical crisis accelerated[51].

This supports the argument, that the textile/clothing industry is a sector, which in general is influenced by the state of the economy.



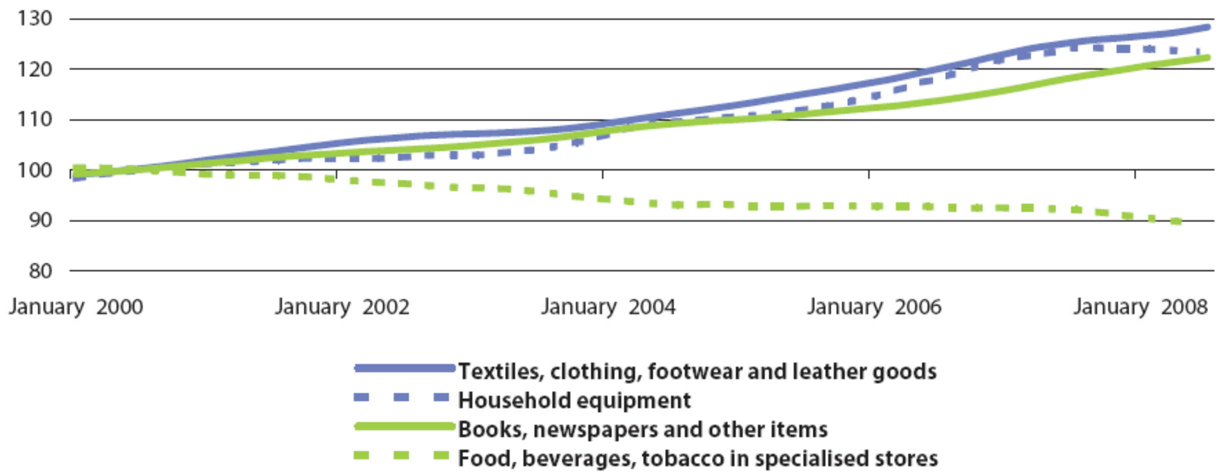
Source: Danmarks Statistik – www.statistikbanken.dk

Since IC Companys is an international company and operates outside of Denmark, especially in Europe, it would be essential to look into the following – is the revenue of the European textile/clothing industry also affected by the economic situation in Europe as well as Denmark? Illustrations have been made below, which indicates that volume of sales has increased from January 2000 to January 2008 for textiles, clothing, footwear and leather goods for EU27 (figure 8.18). The table for the Retail Trade Turnover shows that, the level of turnover from September 2008 to July 2009 has remained almost the

[51] http://www-2.danskebank.dk/danskeanalyse

same. It is to be noted that, the indexes are different in the two scenarios. Figure 8.18 has year 2000 to index 100, whereas the table has year 2005 to index 100. However, if the table is compared to the graph (figure 8.18) and the indexes are recalculated, the volume of sales in the given industry has decreased from January 2008 to July 2009. The downturn in the European economy, in a part of the same period (2008/09), has definitely been a contributing factor to this negative development in the clothing/textile industry.

Figure 8.18: Volume of sales index, selected retail trade activities, EU-27 (1)
(2000=100)



(1) Trend cycle; estimates, June and July 2008.

Source: Eurostat (sts_trtu_m)

Retail Trade Turnover – textiles	**2008**				**2009**						
Index, 2005 = 100	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**Apr**	**May**	**Jun**	**Jul**
European Union (27 countries)	112	109	108	107	112	108	109	109	108	109	111

Source: Eurostat - retail trade turnover, textiles

If the development in the clothing/textile industry (Figure 8.18 and Table for Retail Trade Turnover) is compared to the real GDP growth rate for the European Union (27 countries) in below table, following interpretations can be made. From year 2000 to 2008, the clothing industry experiences growth as does the GDP of EU27. From 2008 through 2009, the development becomes negative for both the clothing industry and GDP of EU27(forecast). An additional scenario, which indicates that, the clothing/textile industry is affected by the state of the economy/private consumption.

Below table, “Revenue of IC Companys”, is presented in order to find out if IC Companys follows these aforementioned tendencies. If real GDP growth rates are compared to the development in revenue of IC Companys, following statements can be made. The real GDP growth rates for EU27, Denmark and Sweden have a lower increase in the period 2001-2003 compared to 2004-2007. From 2008/09 the rates become negative. The total revenue of IC Companys declines in the period 2001/02 to 2003/04. This is the period where EU27, Sweden and especially Denmark have lower growth rates of GDP volume compared to 2004-2007. You can argue that, since the European economy in general is progressing in the years 2001-2003, where IC Companys total revenue is declining, the sale of clothing for this company does not follow the state of economy/private consumption. However, IC Companys was experiencing start-up problems after the merger in 2001. From 2004 IC Companys had restructured their business and made it more efficient, which lead to an increase in total revenue until 2007/08. In this period, the real GDP growth rates increased even further. At the downturn in the economy in 2008/09, IC Companys experiences a negative development in their total revenue. The overall development of the clothing sale of IC Companys seems to follow or be dependent on the state of the economy/private consumption.

Real GDP growth rate											
Growth rate of GDP volume - percentage change on previous year											**Forecast**
	1999	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**
European Union (27 countries)	3.0	3.9	2.0	1.2	1.3	2.5	2.0	3.2	2.9	0.8	-4.0
Denmark	2.6	3.5	0.7	0.5	0.4	2.3	2.4	3.3	1.6	-1.2	-3.3
Sweden	4.6	4.4	1.1	2.4	1.9	4.1	3.3	4.2	2.6	-0.2	-4.0

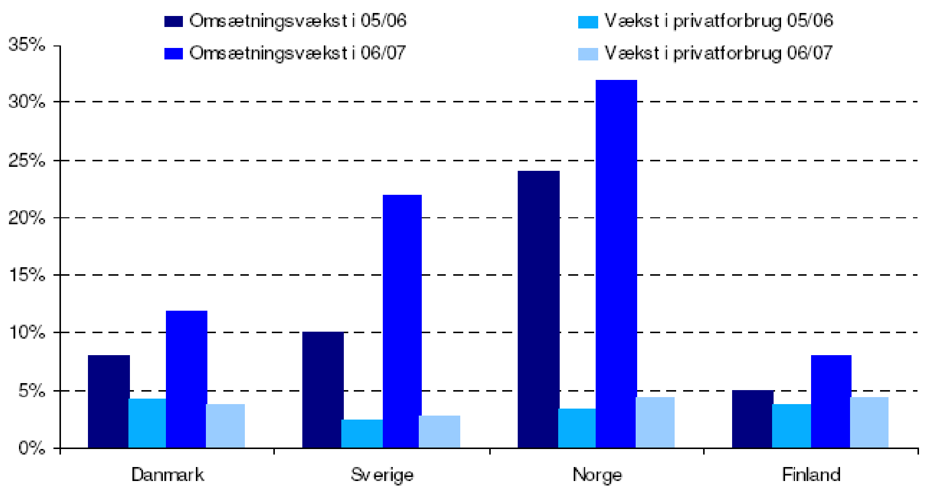
Source: Eurostat

Revenue of IC Companys	Financial year of IC Companys									**Forecast**
Percentage change on previous year		**2000/01**	**01/02**	**02/03**	**03/04**	**04/05**	**05/06**	**06/07**	**07/08**	**08/09**	**09/10**
Total revenue		-	-8.0	-7.0	-3.0	8.0	7.0	14.0	11.0	-4.0	-5.5

Source: Annual Reports of IC Companys 2001/02 - 2008/09

To support the postulate that, the condition of the economy and private income/spending relates to sales in the clothing/fashion industry, a graph[52] for the Scandinavian countries is shown below. The graph illustrates the growth in revenue versus growth in private consumption in the Scandinavian markets for IC Companys.

Figur 9. Udviklingen i privatforbrug og omsætningsvækst i Skandinavien



Kilde: Danmarks statistik, Statistiska Centralbyrån, Statistisk Sentralbyrå, Tilastokeskus, IC Companys og Capinordic Markets.

[52] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi

This graph substantiates the fact, that the revenue growth of IC Companys is severely dependent on the growth in private spending/consumption. Sales in Sweden and Denmark combined represent 44% of the total revenue, so if the economic growth decreases in these markets, the impact will be significant.

Despite the negative market conditions the last years, IC Companys has experienced some positive developments. Sales in January 2009 went relatively satisfying, which indicates that the average consumer still has funds to spend. Though, the consumers have become more careful/considerate and critical in their choice of clothing and more sensitive towards the price. IC Companys is convinced that, the gains of making the company more efficient combined with the right clothing-collections will exceed the macroeconomic tendencies. In total revenue, the brands of IC Companys have experienced a 9% decline in the 3rd Quarter 2008/09. Brands such as Tiger of Sweden, InWear, Jackpot, Matinique and Cottonfield have had a two-digit decline. However, Part Two, By Malene Birger, Saint Tropez, Soaked in Luxury and Designers Remix Collection have had a two-digit increase/progression. The development within the separate brands are neither to be explained by price nor fashion-degree. Therefore it can be concluded, that the possibilities of creating growth irrespective price-segment are completely present despite the disadvantageous economic conditions[53].

The international trade of IC Companys makes them exposed to currency fluctuations/risk. Almost 70% of purchasing is performed in USD-related currencies and Chinese Renminbi, while sales is in DKK, SEK, EUR and other European currencies. However, the Group monitors and manages all its financial risks by the use of financial instruments, thus there are limits to this[54].

Socio-Cultural Factors

The customer loyalty towards fashion clothing/brands can change within different periods. Trends, fashion and taste will change and customers will switch to other brands if a given brand does not meet these requirements. It is therefore necessary and of outmost importance that IC Companys continues to focus on innovation and develop their brands, being both own-developed and acquired brands. Usually when a product is being launched in a market, the company will have determined a specific target

[53] IC Companys report 3rd quarter 2008/09 – 20th of May 2009
[54] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi and Annual Reports of IC Companys 2007/08

group for this product. Though, in the clothing industry it can be difficult to aim for a specific target group. The behaviour of certain target groups are not always as expected. Some target groups do not behave according to their profile and “category”. The different categories sometimes overlap. The division of target groups into certain categories can also prove difficult in regards to price-segment. A brand will either be sold as a high-, mid or low-end product, but the behaviour of consumers can also be unpredictable in this scenario. A consumer’s decision of how to spend or allocate their private income will vary between each individual. However, consumers with high private disposable income will be more willing to buy clothing in the mid and high-end price segment than consumers with low private disposable income. These are elements, which IC Companys has taken into consideration. This is done through their Multi-brand strategy, which was developed in 2003/04 - 2004/05. Besides focusing on potential, growth, profitability and obsolescence of the different brands in their portfolio, the Multi-brand strategy leads to an incremental updating and managing of their brand portfolio in relation to trends, fashion, taste, price and buying behaviour.

Unforeseeable events such as unusual weather conditions can not be controlled and can have an effect on the clothing industry as well[55].

Technological Factors

In 2000 Carli Gry launched an online-based Business-to-Business “distribution/sales channel” for their Wholesale markets in EU. This has been developed through the years and makes it possible for Wholesale to place orders directly via the internet. Thereby, Wholesale has easy access to the manufacturers’ inventories and can respond more rapidly to changes and the given demand of the consumer[56].

E-trade/business is something that has increased the last couple of years. Last year 58% of people in the age-group 15-29 had used some form of E-trade. This year the amount has increased to 83%. This is a tendency, which will continue – even though the rate of increase will become more moderate than before, states CEO Morten Kamper from Foreningen for Distance- og Internethandel. Despite the

[55] Annual Reports of IC Companys 2003/04 – 2008/09
[56] Merger prospect 2001 and Annual Reports of IC Companys 2001/02 – 2008/09

financial crisis, the online retail trade has shown growth, which is contrary to the physical retail trade. Clothing is one of the absolute top contributors[57]. However, the financial crisis has still affected the online retail trade, since the increase in growth has declined compared to previous years[58]. Eurostat has published figures for E-trade in EU from 2008, which states that 59% of Danish adults have conducted E-trade. This places Denmark at the top of the list followed by Great Britain and Holland. The average of E-trade in EU is 3 out of 10 EU-citizens (32%) in the age-group 16-74. Again clothing is one of the top ranks among EU-citizens[59].

On account of this development, IC Companys has increased focus on this realm of business. They have recently made an agreement with GSI Commerce Inc., which Niels Mikkelsen (CEO of IC Companys) has labelled one of the world's leading e-commerce-partners. Niels Mikkelsen states that IC Companys has several distribution channels – Retail, Franchise, Wholesale and Outlets. Though, e-commerce is something, which deserves attention as well. Currently, the agreement comprises 9 out of their 11 brands – Designers Remix Collection and Saint Tropez are not included at present time[60]. However, Peak Performance is soon to be acquired online and within 18 months the rest of IC Companys products will be available as well[61].

The idea is that a company website is used for both sale and display/showroom, where customers find information, inspiration, compare prices and trade when the time and desire is right. Many clothes are actually sold in lunch-breaks and after the children have been put to bed. To neglect internet-sales will be irrational and a great mistake. The customers expect to find the company and its products via the internet[62]. It appears that IC Companys is going in the right direction in regards to online sale.

The technological factor is also essential concerning the manufacturing phase. Time/security of delivery, price and quality of the clothing are imperative elements. China has long been known for their inexpensive labor and their ability to produce clothing. China is expected to increase their global share

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57 "Alle unge shopper nu på nettet", Ekstra Bladet 11. aug. 2009, Gitte Hejbjerg, http://ekstrabladet.dk/kup/elektronik/article1204780.ece?service

58 http://borsen.dk/it/nyhed/163253/email_finans/ (11-08-2009) "Nethandel trodser nedturen"

59 "Danskere handler mest på nettet", Mads Bindesbøll Ohsten (1/4-2009) – http://www.erhvervsbladet.dk/erhvervsklima/danskerne-handler-mest-paa-nettet

60 http://www.e-handel.dk/uploaded_images/borsen_091109_nethandel2-734943.png "Store forventninger til nethandel"

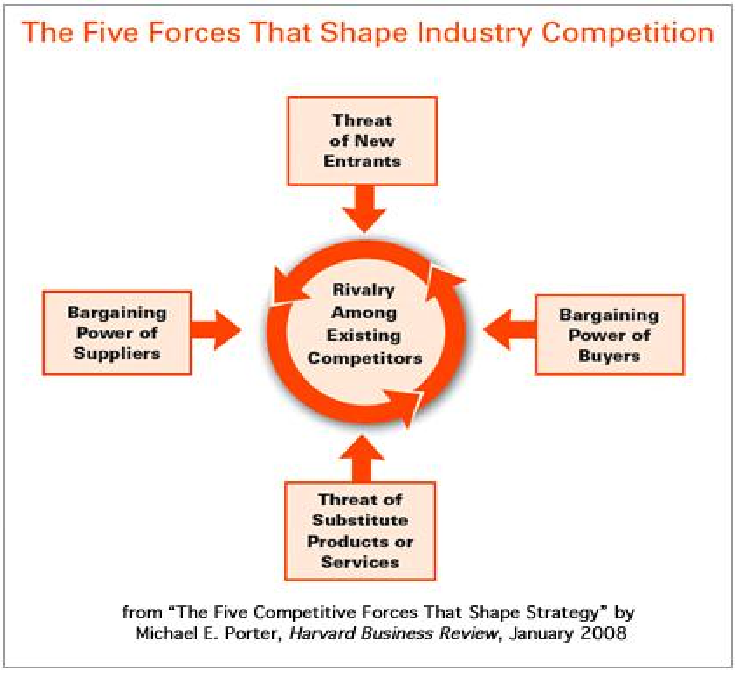
61 "IC Companys: Øger satsning på detailbutikker", 10/9-09, http://finans.tv2.dk/nyheder/article.php

62 "Nethandel er i fremgang", Morten Kamper, Direktør for Foreningen for Distance- og Internethandel – http://www.e-handel.dk/uploaded_images/nethandel-715787.png

of manufacturing in the clothing industry in the future due to their ultra modern, minimum-wage industry. It is to assume that IC Companys has had these deliberations, since China represents approximately 60% of IC Companys manufacturing. The rest is manufactured in Rumania (13%), Turkey (10%), India (5%) and other countries (12%). Eastern Europe has in the last years also shown progress within technological development and has low cost in the labor-market for clothing, which supports IC Companys decision to integrate these countries in their manufacturing portfolio[63].

3.3 Porters Five Forces Analysis

This analysis will be conducted by using the model of Porters Five Forces. The model looks into the conditions of the industry, in which IC Companys operates and provides a perspective on IC Companys competitive situation. According to Michael Porter, growth and earnings potential in an industry depend on five central forces.



Source: "The Strategy Process", 4th edition, Mintzberg, Lampel, Quinn & Ghoshal, 2003

[63] http://www.information.dk/print/95982 - "Kina sætter sig på tøjproduktion", Kathy Marks, 29/5-07

It has to be noted that, the model provides a static overview of the industry and lacks the dynamic perspective. Though, the model will still give a relatively clear picture of the industry and the competitive situation within this.

Threat of New Entrants

Brand/Trademark, capital, access to production/manufacturing- and distribution/sales channels are factors, which are essential in relation to a start-up in the clothing industry. The brand/trademark is of significant importance, since it is to create awareness, brand identity and customer loyalty. This is usually something that requires a certain amount of time, this is not done overnight. To increase brand awareness demands a heavy marketing effort and a lot of capital.

The establishment of production/manufacturing- and distribution/sales channels also has certain capital requirements. However, a company does not necessarily have to own the manufacturing machinery. It is possible to use suppliers for the production/manufacturing of clothing and thereby minimize the capital tied up in non-current assets.

The entry barriers are evaluated as being relatively high concerning the brand. To establish brand awareness, identity and customer loyalty demand considerable resources and is rather time-consuming. Even though there is an indication of the loyalty towards a brand is not as important for the consumer, who mixes different brands, it still requires that the consumer has knowledge of the brand.

In the clothing industry it has become practice to outsource or establish production/manufacturing in the East, especially in China where among other things, the cost of production is low. If an outsourcing strategy is chosen, the amount of capital employed is limited. The entry barriers in relation to this are more modest compared to the establishment of production/manufacturing sites.

An additional business strategy for new entrants could be to sell/distribute their product/brand through already existing 3. party stores or via the Internet (e-commerce) and avoid capital tied up in new stores, which would lower the entry barriers.

Bargaining Power of Suppliers

The total production of IC Companys has been outsourced to foreign countries. The main part has been moved to China (60%) and the rest is divided between Rumania (13%), Turkey (10%), India (5%) and other countries (12%). The 10 largest suppliers represent 27% of the total production value of the company. The largest supplier represents 4% of the total production value. This results in less dependency of each supplier, the possibility to put pressure on prices and secures a higher level of delivery. China has many clothing manufacturers, which makes it rather easy for IC Companys to switch to other suppliers if not satisfied with the current ones. However, this can have an effect on quality, price and security of delivery.

The independence of each supplier lowers the bargaining power of IC Companys in relation to achieving volume discounts, improved credit terms, etc. Though, the overall bargaining power of suppliers is relatively limited.

Seen from a different perspective, the employees of IC Companys are suppliers of knowledge and "know-how" and could therefore also possess some bargaining power. In this case, the key employees are the designers and the ones, who develop and have the responsibility of the different product lines. It is essential for IC Companys to try to maintain this workforce or be able to attract new competent employees if necessary. IC Companys is to some extent dependent on these employees.

Threat of Substitute Products or Services

The main focus and product portfolio of IC Companys are aimed towards the mid and high-end price-segment. They have 4 brands in the high-end price-segment (Peak Performance, Tiger of Sweden, Designers Remix Collection and By Malene Birger) and 7 brands in the mid price-segment (Part Two, InWear, Cottonfield, Jackpot, Matinique, Saint Tropez and Soaked in Luxury)[64]. Other competing brands can be mentioned as substitute products and/or services. The different brands of IC Companys have competitors in their respective categories. However, this will be described in the section "Rivalry among Existing Competitors". If the main brands of IC Companys are classified as "luxury products",

[64] Annual Reports of IC Companys 2006/07 – 2008/09

a substitute could be inexpensive basic clothing. As an example, this would be clothing sold in supermarkets or via mail order. Here the clothing is to fulfil the basic need of having to wear clothes. The products of IC Companys and of other fashion houses serve an additional purpose. They are also to represent a certain image, lifestyle, personality, identity, etc. The brands/products of IC Companys are therefore not in direct competition with inexpensive basic clothing.

The level of service in clothing stores can also differ. If customers are not satisfied with a given service when buying clothes, they might substitute the service by visiting another store in the future. If a customer's intention is to buy clothes, a high level of service by itself can not substitute the act. Service is to be seen as a complementary product/service to the act of buying clothing. It is therefore essential to maintain a high level of service in the stores. IC Companys is through their Retail Academy (for staff) and Leadership Academy (for managers) trying to educate and develop their employees to, among other things, attain an optimal service-level in their own stores.

Bargaining Power of Buyers

The bargaining power of buyers can be seen from different perspectives and divided into two categories. One category is the wholesale distribution points (stores owned by 3. parties) and the other category is the end-consumer of IC Companys' products. IC Companys sells clothing via 12,000 wholesale distribution points located in more than 40 countries all over the world. Wholesale revenue equals approximately 60% of IC Companys total revenue. Though, no customer accounts for more than 5% of the Group wholesale revenue. The impact of losing a customer will be relatively limited. If the criteria for buying the products of IC Companys are not in line with the business philosophy of the wholesale customers, they have the option to find another supplier of clothing. This they can do rather easy as the supply of clothing is abundant and the share of supply from IC Companys to each wholesale customer is minimal. However, it can be argued that IC Companys has renowned well-established brands/trademarks, which will make it difficult for wholesale customers to find substitutes. The bargaining power of wholesale customers is only in some degree present.

The end-consumer of IC Companys' products also has some form of bargaining power. If they are not satisfied with the characteristics of IC Companys' brands, it is possible to substitute with brands of competitors. The willingness to switch to the competitors' brands will depend on the end-consumer's relation to and identification with brands of IC Companys.

Rivalry among Existing Competitors

Last year the total revenue of the Danish clothing companies reached DKK 23.6 billion. It is expected to decline 7-10% and exports, which makes 90% of total revenue is to decline equivalently. More than half of the companies have experienced setbacks in 1st half 2009 and the tendency is expected to continue correspondingly the rest of the year. It is especially the small- and large-scale enterprises, states Export Director Michael Hillmose from DM&T (Dansk Mode & Textil - formerly known as Dansk Textil & Beklædning – DTB). The Danish clothing industry is characterized by 3 large corporations, Bestseller, IC Companys and BTX Group, which represents a significant share of the total revenue in the industry[65]. In general, IC Companys has many competitors in the Danish as well as the international market. Many players in the markets have their own individual concept and collections and aim towards several segments. In these markets, IC Companys would either have to conquer market share from the competitors or expand through other and/or new geographical markets if growth is desired. Another model or combination in achieving growth in this industry would be to evaluate and reduce the level of costs.

The mid-price segment has attained great attention in the apparel industry. The segment makes the largest part of the total fashion market and the growth in the segment is estimated to become 3-4% p.a. The competition is severely intensive and more suppliers are starting to enter the segment[66].

The main part of IC Companys' brands is categorized in the mid-price segment (Jackpot, Cottonfield, Part Two, InWear, Matinique, Saint Tropez and Soaked in Luxury). The company has always had a strong foothold in this segment and will continue to focus at this. Their other brands are categorized in the high-end price segment, such as Peak Performance, Tiger of Sweden, Designers Remix Collection

[65] "Den danske tøjbranche dykker", Jesper Olesen, 5/8-09 – http://epn.dk/brancher/mode/toj/article1771871.ece
[66] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi

and By Malene Birger, which are the most sensitive to market fluctuations. Every brand in the portfolio has a unique profile and is therefore competing with different brands in the market[67].

Due to the fierce competition in the market, it is essential to have a strong focus on brand profiling and brand positioning, which are to create brand loyalty. The Multibrand strategy of IC Companys is specifically to improve the brand identity towards the consumers. Additionally, the development of fashion is to be carefully monitored to meet the requirements of the consumers.

The mid-price segment for fashion clothing is generally fragmented and therefore no brands have a dominant position. This means that there is a great potential in this segment and IC Companys therefore plans to operate and strengthen sales within this[68].

Each of IC Companys' brands target a special customer segment. Below, 3 tables[69] are presented, which illustrates the brand portfolio of IC Companys, their individual profile, separate growth strategies of each brand and competitors in their respective segments.

[67] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi
[68] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi
[69] Annual Reports of IC Companys 2007/08

3.4 SWOT Analysis

The SWOT model is applied to sum up on the strategic analysis. Strengths, weaknesses, opportunities and threats, which IC Companys is confronted by both internally as well as externally, are presented.

Strengths

- Well-established large international company
- Several products – 11 designer labels
- Diversified Product Portfolio – Each product/brand has a unique profile and targets a special customer segment. Targets two price segments, mid and high-end price segments.
- Well-positioned brands
- Industry experience
- Consolidated market position
- Dynamic and decentralized organizational structure
- Expansion of the Franchise function
- Several distribution/sales channels – Wholesale, Retail, Factory Outlets and Franchise
- Closure of non-profitable stores
- Multi-brand strategy
- The shared business platform – several central functions, such as sourcing, distribution, sales logistics, HR, IT, marketing, finance and administration. Enables the utilization of synergies across the different brands. Leads to significant cost-advantages, secures a high product quality and minimizes the risk of failure in deliveries to distributors and own stores.
- Sales and marketing departments are brand-divided – Advantages in terms of increased sales, flexibility, ownership and pace are evaluated to exceed traditional cost-advantages of a shared sales force.
- Sales responsibility is to a higher extent locally anchored – to ensure a clear division of work and inherently strengthen execution skills and ownership. The brand management remains globally responsible for sales performance and will focus on brand positioning, marketing,

product development and strategic sales, whereas the operational sales responsibility is placed with the local sales companies.

- Training of employees and managers (IC Academy – Retail Academy & Leadership Academy)
- Established a customer loyalty programme – to connect the customers even more to their brands and stores
- Production/Manufacturing outsourced to cost-efficient countries
- Low dependency of each supplier of clothing
- OTB (Open To Buy) – seasonal sale of clothing with a short delivery time
- New model of cooperation for the Wholesale department is being implemented – secure effective/efficient sale and lower amount of capital tied up for Wholesalers as well as IC Companys
- Refurbishment of retail stores have been outsourced – increases execution-ability, flexibility and diminishes costs
- "Code of Conduct" (guidelines CSR) – contribute to a positive perception of the customers and eventually influence the point of sale
- Factory Outlets – clothing, which remains unsold the end of the year/season can be sold here
- No Wholesale customer accounts for more than 5% of the Group wholesale revenue
- Online-based business-to-business "distribution/sales channel" for Wholesale markets in EU – wholesale can place orders directly via the Internet (easy access to manufacturers' inventories and can respond more rapidly to changes and the given demand of the consumer)

Weaknesses

- Lacks experience in selling clothing online and is not as up to date in this realm of business
- Dependent on their designers and the ones, who develop and have the responsibility of the different product lines – suppliers of knowledge and "know-how"
- No products in their portfolio, which are aimed toward the low-end price segment – would possibly contribute to sales both during a state of growth and recession in the economy
- Heavy marketing expenses to promote a brand

- Fixed costs related to the Retail department (own stores)

Opportunities

- Implementation and development of e-commerce – selling clothes via the Internet
- Develop or acquire new brands
- Gain market share nationally as well as internationally
- Expand to new markets
- Fluctuations in the economy – positive direction
- Currency fluctuations – positive direction
- Exploit that the mid-price segment for fashion clothing is generally fragmented and therefore no brands have a dominant position

Threats

- Currency fluctuations – negative direction
- Fierce competition in the clothing industry
- Weather conditions
- Fluctuations in the economy – negative direction
- Price increases on manufacturing and supply of clothing
- Fashion Risk – their products might not live up to customer preferences (fashion trends)
- A decrease in brand loyalty
- Political/legal issues (regulatory amendments) in the countries, in which IC Companys operates
- Threat of new entrants

3.5 Strategies of IC Companys

To assess and achieve its goals in terms of growth, earnings and other objectives, a company has to choose one or several strategies to pursuit. The strategic situation is looked into in order to find out if the company is strategically fit – is the strategy viable in relation to IC Companys' strengths, weaknesses and the opportunities and threats the company is confronted by.

IC Companys mission and vision are to build successful international fashion brands and to become the best owner and business support for international fashion brands. They expect to create growth and market value for the benefit of its stakeholders through different values:

- Customer-Driven – Customers know us as proactive
- Reliable – You can count on us, a promise made, is a promise kept
- Ambitious – It's our passion to make fashion great business
- United – People working together, united in fashion

To support the company vision, IC Companys has set certain objectives:

- Offer a solid base for brands to grow and expand from
- All brands must have international potential
- Each brand must establish a clear brand identity and earn money in the long term
- Work within the fashion industry

This set of values is based on placing the customer/stakeholder in the centre and to constantly develop and offer better brands to the customer. This is both for the general product portfolio and on an individual basis for each collection of the separate brands. The most paramount intangible resource of IC Companys is definitely the brands of the company. These are both the own-developed and acquired brands. IC Companys brands are coherent with their portfolio and thereby make a significant strategic parameter[70].

IC Companys will continue to operate with a portfolio of brands for different price-segments in order to meet various preferences of the consumer and to minimize loss in sales caused by an economic downturn. The philosophy of the Multibrand Strategy substantiates this scenario. Further, the competition is fierce in the mid-price segment (the largest segment), which makes it essential to have diverse products and market them in several price-segments. This will provide IC Companys with a competitive advantage.

[70] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi

The organizational structure and the Multi-brand strategy account for both the individual brand and create synergies within the shared business functions/platforms.

IC Companys overall goal is to achieve a yearly organic growth of minimum 15% and an EBIT-margin of minimum 15% in a 3-5 years time-horizon.

The growth objective is divided between the different distribution channels. Franchise is expected to grow relatively strong and the growth potential in Retail is to be utilized. Sales through Outlet Factories is anticipated to be modest due to an improved purchasing- and inventory management. Efforts will be focused on OTB[71] sales and in regards to pre-order sales; this is expected to have a lower growth compared to OTB sales.

IC Companys intends to operate from a growth aspect. The strategy is to expand business operations within retail and franchise. The last several months IC Companys has been working on introducing a new franchise concept. The Group will from a tailor-made and professional concept provide assistance to independent store-owners in establishing and running a business. The purpose is to secure a reduced or minimal level of capital tied up. Negotiations with potential franchise-owners have already proved successful. Several agreements/contracts have been made in Denmark and Sweden[72].

IC Companys has in the budget for 2009/10 allocated DKK 100-120 mill. to invest in sales-supportive precautions. Approximately DKK 80-100 mill. will be used for the opening of new and own retail stores. With the right design and concept supported by the right marketing strategy it will be possible to increase the growth of their brand portfolio.

Further, to grow a focus on e-commerce for clothing is an evident step in the right direction. Peak Performance is soon to be acquired online and within 18 months the rest of IC Companys products are available as well[73].

IC Companys sells its brands in several markets (more than 40 countries) and approximately 80% of revenue is generated outside of Denmark. Though, it is only in 8 of the largest markets (Sweden, Denmark, Holland, Norway, UK & Ireland, Belgium, Finland and Germany) where all of the

[71] Open To Buy Sales – seasonal sale of clothing with a short delivery time.
[72] Annual Reports of IC Companys 2008/09
[73] "IC Companys: Øger satsningen på detailbutikker", 10/9-09, http://finans.tv2.dk/nyheder/article.php

company's brands have been introduced[74]. Therefore, a significant unexploited growth potential is present in the other markets, in which the company already operates and possesses competences and market experience. Focus is directed towards growth markets, internationalization of brand portfolio, to increase efficiency in sales and expansion of the store concepts via Franchise and distributors in new markets such as Russia, Eastern Europe and the Middle East. The Russian market has a certain potential, which in 2005-2007 showed a high growth progression of 44%[75].

Despite the negative market conditions the last years, IC Companys is convinced that, the gains of making the company more efficient combined with the right clothing-collections will exceed the macroeconomic tendencies. As mentioned earlier (Economic Factors – PEST Analysis), the total revenue of the brands of IC Companys have experienced a 9% decline in the 3rd Quarter 2008/09. Brands such as Tiger of Sweden, InWear, Jackpot, Matinique and Cottonfield have had a two-digit decline. However, Part Two, By Malene Birger, Saint Tropez, Soaked in Luxury and Designers Remix Collection have had a two-digit increase/progression. The development within the separate brands are neither to be explained by price nor fashion-degree. Therefore it can be concluded, that the possibilities of creating growth irrespective price-segment are completely present despite the disadvantageous economic conditions[76].

The choice to outsource production/manufacturing to mainly China and Eastern Europe and make use of a shared business platform is a strategy to minimize costs, which in the end can contribute to the objective of achieving growth.

As mentioned in the PEST analysis (Economical Factors), IC Companys has 85% of its sales in the European market, which means that the company is rather dependent on the economic situation/outlook in Europe. To minimize this business risk, a strategy to expand its operations and enter new markets would be something to consider. As illustrated in table "Global Growth Forecasts" (PEST analysis – Economical Factors), China has experienced growth rates of approximately 8%, while USA, Euroland and Japan has suffered during the global economic downturn. Due to the large size of the Chinese market and current/forecasted growth rates, this is an attractive market to look into. Even though IC

[74] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi
[75] Capinordic bank – IC Companys A/S, 6 November 2007, Samarah Shafi
[76] IC Companys report 3rd quarter 2008/09 – 20th of May 2009

Companys recently has had logistical difficulties and terminated their sales activities in China, this could be a market, which deserved renewed attention. As a first step, the sales potential is to be explored and find out if the demand/requirements of the Chinese consumer in terms of fashion, price, socio-cultural elements, etc. are consistent with the supply of IC Companys. The advantages of penetrating this market is that, IC Companys already has the experience of the Chinese market through their former presence and there might exist unexploited opportunities.

Another initiative/strategy for IC Companys would be to increase focus on export to Germany. According to figure “Sales performance own brands market breakdown” shown in the PEST-analysis (Economical Factors), Germany represents 5% of IC Companys total sales. The organization DTB (Dansk Textil & Beklædning) will implement new value-adding activities and increase its export efforts in Scandinavia and Europe. They will especially direct attention to the German market. A conducted survey, performed by DTB, indicates that the German market is a market with relatively low risk and a latent potential. Due to the economic situation, Germany would not be a poor choice. Several analysts state that Germany is a country where the retail trade will remain relatively stable and the risk of currency fluctuation is minimal contrary to other countries. Danish products and Danish values are also perceived positively in Germany, but the competition has become more intense. DTB has also directed attention towards other interesting markets; China, the Emirates and Canada[77]. Therefore - another reason for IC Companys to re-establish their business operations in the Chinese market and increase efforts in Canada, where they are already present.

[77] DTB´s årsberetning 2008

4. Financial Analysis

The annual report is an important tool to examine how well a company has been doing historically. The annual report does not only give a picture of the company's current situation but it can furthermore be used to describe the past and gives information about the future operating profit, and analyze the risk connected with the cash flow. It can be said that the annual report is used as a measure instrument to get an insight into the chosen and followed strategies.

The financial analysis is not just used to measure and explain how the previous financial years have been, but furthermore it is used to create a foundation for budget the forthcoming comprehensive income. The historical development is also an important tool when you have to estimate the value of the firm. By looking at the historical data very closely you might be able to explain why things went the way they did. The result would be a more valid estimation of the forthcoming earnings and financial analysis.

4.1 Analysis of accounting policies

The starting point for a meaningful financial analysis over time is that the financial material is suitable for the purpose of analysis. This entails that there are some invariably demands that must be fulfilled as these:

Comprehensibility: Information that is incomprehensible is mostly useless but the degree of comprehensibility depends of the receiver and it is assumed that the receiver possesses the necessary knowledge concerning business related factors and accounting, etc. Comprehensibility is therefore accepted as a precondition to the annual report.

Relevance: Is there a connection between the information the financial statement user need and the information which has been given in the annual report. Information is accepted to be relevant when it affects the user's economic dispositions and is a precondition to the annual report.

Reliability: Can the financial statement user trust the accounting material meaning is it neutral without bias, have the assets and liabilities been recognized correctly.

Comparability: Is it possible to compare the information through years and benchmark with other companies.

The Danish accounting policies have been under significant change. The reason has been the implementation of Årsregnskabsloven af 7. Juni 2001 (ÅRL) and the transition to the international standards IAS/IFRS. These changes have had an effect on recognize, measurement, level of information, disclosure in the notes and the management´s review.

Evaluation of the accounting policies and the accounting material

The analysis of the accounting statement of IC Companys has the aim to disclose whether IC Companys accounting policies gives a fair presentation and comparability of annual reports of different financial years.

Is the information in the annual report applicable concerning the company's assets, liability, equity, financial position, income and cash flow. The assessment will cover IC Companys accounting policies for the financial years 2003/04-2007/08.

The annual report of IC Companys A/S has been prepared in accordance with the International Financial Reporting Standards (IFRS) throughout the analytical period. IC Companys changed to IFRS July 1, 2005.

The independent auditor's of IC Companys has not found any deviations and has found the material to fulfill the requirements of accounting throughout the analytical period. The first 2 financial years it has been the same auditors but in 2007/08 Kirsten Mikkelsen has been replaced by Henrik Hansen.

On behalf of the above details we conclude that, IC Companys has followed standards according to IFRS. The accounting records have been evaluated as comprehensible, relevant, reliable and comparable.

4.2 Change of policies

The accounting policies of IC Companys have only been changed once. The change occurred in 2005/06 where the company transitioned to IFRS. This transition has necessitated several changes. The changes are as follows:

- Business combinations and goodwill
- Share-based payment
- Intangible leasehold right
- Pension obligations
- The Parent Company´s measurement of investment in subsidiaries

The changes have resulted in an adjustment of 30.5 DKK mill for the yearly profit and the equity have been adjusted with 43.2 DKK mill.

Share-based payment must be settled when the company receives the goods or when the service has been provided. The set-off must reflect the intensification in the equity or the liability if the share-base payment has been purchased by cash payment. The share-based payment must be settled to current cost. IC Companys has due to the transitional provisions of IFRS 1 and IFRS 2 not applied stock options and warrants granted before and after November 7, 2002 in the equity because they have been fully exercised at January 1, 2005.

Exchange adjustment of foreign currencies

On translation of foreign enterprises, IAS 21 prescribes that exchange adjustments must be recognised as separate line items directly in equity. Upon a subsequent disposal of the enterprise, any accumulated translation differences must be recognised in the income statement. According to IFRS 1 it is now possible to reset the exchange adjustment to zero the day before the interim. Any future translation differences must be settled in equity.

This is exactly what IC Companys has done. July 1, 2004 they reset their exchange adjustment to zero. Any future translation differences will be recognized in equity. Any future exchange adjustment concerning disposal of a firm which have been recognised in equity will be settled in the income statement.

Business combinations and goodwill

All business combinations must apply the purchase method. Assets and liabilities must be settled to currents cost and not as carrying amount. IC Companys has applied the purchase method to account for acquisition. The Group has decided to apply the exemption in IFRS 1, to the effect that IFRS 3 has been implemented with effect from July 1, 2004.

According to IFRS it is not possible to depreciate goodwill anymore. Instead there must be made a yearly impairment test. IC Companys will from July 1, 2004 apply this by making yearly impairment test. Any impairment will be set off in the income statement.

Pension obligations

In accordance to IAS 19 a firm must measure and settle defined benefit liability in the income statement and liability concerning actuarial measurement. IC Companys has adjusted the annual report in accordance with this.

In Connection with the transition to IFRS the layout of the income statement has been changed so that it is classified as type instead of by function.

In addition to the change in the accounting policies there have been made some reclassification and layout changes. These are as follows:

Provisions are no longer presented as a separate group of liabilities termed provision. They are instead incorporated in the short and long termed liabilities.

Accordance with IAS 18 license income is now settled in the revenue compared to previous where it was recognized as operation income.

Commission income is settled as net amount under revenue in accordance to IAS 18

Minority interests are presented as a separate item under consolidated equity.

Asset under construction are presented separately in the balance sheet.

The financial years for 2006/07 and 2007/08 have not led to any change in the accounting policies. As mentioned the only change in accounting policies has been made 2005/06 because of the transition to IFRS, which also led to a change in layout of the income statement.

4.3 Correction for analytical use

The value creating economic activities in a company can be divided into two parts, operating and financial activities. The international and the Danish accounting regulation do not have clear guidelines regarding the division of respectively operating- and financial activities. This means that it is up to the individual external analyst to make a reclassification of the public annual report into both operating and financial activities so that it can be used for further analysis on both operating and financial activities.

A company´s capability to create return on assets in the long run will in most cases be driven by its operating activities or the so called main activities. Therefore it is very important to analyze this specific value driver to measure the company´s existence in the long run and that's why it must be "cleaned" for financial activities.

On behalf of the above mentioned it is clear that one must make reclassification of a company's annual reports before an accounting analysis can be made. The classification must be made for the balance sheet, the movement in equity, income statement and the cash flow statement.

A company can besides the actual distribution of operating and financial activities make entries direct on the equity regarding both the national- and international regulations and standards. It is therefore possible to recognize as a part of the value creation in the movement of equity. Entries made direct on the equity will be reclassified so it will make it possible to distinguish between the transaction with the owners from the comprehensive income. In connection with the visibility of the total value creation a reclassification of the statement of change in equity must be made so that the item concerning the comprehensive income is included.

The official annual report is in lack of complete information and adequate toward the external investor therefore some of the reclassification and corrections have been made by us based on some estimates.

The estimates mostly concern distribution circumstances and in those circumstances where it has not been possible to find any information in the annual statement.
In the appendix is the official balance sheet, movement in equity, income statement and cash flow shown. Furthermore is the reformulated balance sheet, movement in equity, income statement and cash flow shown in the appendix.

The whole procedure regarding the reformulation of the above mentioned is treated in the appendix where each reclassified items have been reviewed. This review consist of both a reclassification of financial and operating items and take a stand to make correction on some items as accurate as possible so that the analytical motive has been fulfilled.

4.3.1 Important points concerning the balance sheet

Other provisions

In the year 03/04, 04/05 and 05/06 IC Company has made provisions on “Rent for loss generating stores to be closed”, ”provisions for rent” and restructuring of acquired enterprise”. Taking the analysis into account we have moved these items from the balance sheet to the accounting period they concern. From IC Companys point of view the reason is that these provisions are an estimate for a prudence concept. In an analysis point of view these items have no eligibility in the provision.
In an accounting point of view one must expect that these costs must have been devoted on behalf of a justified expectation to the forthcoming cost. But taking the analysis perspective into account these cost should be recognized to the periods they concern. That is why we have made an adjustment to this according to the appendix. The reclassification (reversal of these costs) will appear within the appendix.

We refer to appendix 1.1 where the treatment of the balance sheet has been made in detail.

Other payables:

In the annual report other payables are typically not “closely” specified. In this case though there have been some specification on some of the main items but there is still some items as “other cost payable” that have remained unspecified.
It is necessary to comment on classification of these items.

Accrued interest has been classified as an interest-bearing liability why it must be assumed that these must be related to financial liability.

We have classified unrealized loss on financial contracts as an operating liability. This we have done by looking at the accounting policies. We believe that the cash flow hedging must be referred to sales of goods and purchased supplies. It is mentioned in IC Companys accounting policies that forward exchange contract is only used regarding the hedging of sales of goods and purchased supplies. It is however possible that unrealized capital loss on interest rate swaps, etc. is included in this amount. But because neither the accounting policies nor the company do specify this item it has not been possible to comment any further on this topic.

4.3.2 Important points concerning movement in the income statement

Concerning the correction and reformulation of the income statement the items have been divided into two main groups, which are operating and financial relating components. By doing this we will be able to recognize whether IC Companys gets their earnings from operating activities or financial relating activities. Operating related items have furthermore been divided into "operating profit from sale" and "other operating profit". The purpose of this division is to make it easier for the reader(analyst) to identify whether the company gets its earnings from its main activities that can be considered as recurrent(operating profit from sale) or is it from some secondary, one-off items or from other profit components that cannot be considered as being recurring(other operating profit).

Unusual items:

In the accounting year 03/04 some items such as "provision for loss on account receivable", "impairment of inventory" and "correction of goodwill" with the amount 20 mill DKK, 57 mill DKK and 58 mill DKK respectively, have been reclassified from "operating profit from sale" to "other operating sale". The same has been the case for the accounting year 07/08 where the reclassification concern "Provision for loss on account receivable" with 7 mill DKK and "provisions for severance pay to the Group's Chief Executive Officer" with 13 mill DKK.

Distributing the tax costs:

We have distributed the tax costs for all the accounting years on the operating result and the financial results. This allocation has been made on behalf of the published annual reports. There will though be some part of it that has been made by using estimate. But we do not believe that this will have an effect on the fair presentation or the analysis.

Determination of the comprehensive income has also led to correction of some items that has been recognized directly on the equity regarding the published annual report. The reason for the change is that we want to express IC Companys total value creation with the comprehensive income.

We refer to the appendix where the income statement has been looked into.

The official and reformulated annual statements are given in the appendix.

4.4 Analysis of the profitability

This section will take point in the reformulated annual reports. As introduction the activity (revenue) of IC Companys will be looked into.

The profitability will be based upon the return on equity decomposed to operating profit compared to the net operating asset ($ROIC_{noa}$) and the asset turnover.

The structure that will be used in the profitability analysis is shown in appendix 1.4. The analysis will concern the return on equity and is divided into three levels where the level that is higher will be analyzed by decomposing and analyzing the level before.

The levels are as follows:

Level 1: Decomposing the return on equity(ROE)

Level 2: Decomposing the return on capital employed, ($ROCE_{noa}$)

Level 3: Analyze the underlying drivers

4.4.1 Activity (the development in the revenue)

As it appears from figure 4.4 IC Companys has experienced a constant rise in the revenue throughout the analytical period. Looking at the first 4 years one will be able to see that there has been a rise of approximately 200 mill DKK yearly. But the greatest rise appeared in 2008 where the revenue exceeded a level of 3.7 billion DKK, which was a rise of 350 mill DKK.

The rise in the revenue is basically due to the rise in the wholesale. Throughout the whole period IC Companys has experienced a rise in this segment. If you compare the wholesale revenue from 2004 with 2008 one will see that it has increased with an index of 55 to a level of 155.

Figure 4.4 furthermore shows that the segment that contributed most to the revenue is the wholesale. Wholesale contribute about 2/3 of the entire revenue. As mentioned before wholesale has been increasing throughout the whole period whereas retail experienced a fall in 05. This can be seen in light of closure of own retail shops that has been onerous. Sometimes it can be more profitable to close a shop that has a negative effect on the total result even though that it might be on the expense of the revenue.

When the merger between Inwear and Carli Gry took place in 2001 IC Companys formulated a goal where they had to have a 5- 10% organic growth yearly in revenue. This goal has been reviewed in 2007 to reach a level of 15%. In regards to the first goal, IC Companys was not able to reach this goal in the first 3 years after the merger. IC Companys have not stated any specific revenue growth in between 2001 and 2007. The first time they actually reached a growth objective stated in 2001 was in 2005. 4 years after the merger. From 2005 to 2007 they were able to attain the growth level stated in 2001. In 2007 and 2008 the growth level almost reached the stated goal of 2007 (15%).

In the presentation of annual report 2008/09 IC Companys states that they expect a negative development in revenue. So far they have experienced a decline in revenue of 9% to a level of 1.003 mill DKK for the 3rd quarter of 2008/09. This point will be discussed in the valuation section where we will discuss the estimate for the growth.

There have been several reasons for the growing revenue. Based upon the annual report we have found following points to be of crucial character:

- As mentioned, the revenue for retail business has been increasing from 2005. This is among other things due to the change of strategy and macro-economic upturn/growth. From the merger in 2001 until 2005, the revenue from Retail was declining. To turn the development it was decided to close own shops that were onerous and convert some of them into franchise. In 2006 the Retail focus was increased. They established a customer loyalty programme to connect the customers even more to their brands and stores. Diversification also played an important role.
- The growth is also due to IC Companys Retail Academy which objective is to train and educate the company's shop employees (900 people were trained).
- There have been some structural changes as well, which have led to a multibrand strategy that also has contributed to a rise in revenue.

Figure 4.4 developments in revenue both total and at a segment level

	2004	2005	2006	2007	2008	04	05	06	07	08
Total Index	2.612.204 100	2.820.600 108	3.022.000 116	3.353.800 128	3.737.200 143	100%	100%	100%	100%	100%
Wholesale Index	1.607.000 100	1.906.000 119	2.098.000 131	2.308.000 144	2.497.000 155	61,5%	67,6%	69,4%	68,8%	66,8
Retail Index	868.000 100	777.000 90	798.000 92	915.000 96	1.092.000 126	33,2%	27,5%	26,4%	27,3%	29,2
Outlet Index	137.000 100	138.000 101	126.000 92	131.000 96	148.000 108	5,2%	4,9%	4,2%	3,9%	4,0%
Not allocated	204	-400	0	-200	200	0%	0%	0%	0%	0%

On behalf of the above mentioned, it can be said that IC Company has been able to reach the target that was set in 2001 in 2005. The target was not reached until then. The target of an organic growth (15%) that was formulated in 2007 has on the other hand not been reached yet. Even though they have experienced a two-figured growth rate, it has still not been at the level of their target. 2008/09 3rd quarter report shows a decline in the growth and therefore they will not reach the estimated goal from

2007. One must assume that this might indicate a turnaround in the forthcoming revenue from positive to negative growth.

The market IC Companys is operating in is relatively sensitive towards the macro-economic fluctuations. There has been an economic upturn in many parts of the world through the last 4-5 years. Besides their change of strategy, this upturn has also contributed to the increase in revenue.

4.4.2 Decomposing the return on equity, ROE

This section will be looking into the problem within level 1. We will decompose the return on equity by analyzing the operating activities as well as the financial activities through a deeper analysis of $ROCE_{noa}$ and FGEAR*SPREAD.

Figure 4.5 Decomposing the return on equity, ROE

			2004	2005	2006	2007	2008
$CI/EQ_{average}$	ROE	Return on equity	-55,3%	46,7%	36,4%	48,3%	40,4%
OP*100/NOA	$ROCE_{noa}$	Return on capital employed	-21,6%	31,4%	22,7%	25,4%	19,0%
NID/EQ	FGEAR	Financial gear	1,4	0,6	0,7	1,0	1,4
NIC*100/NID	IR	Net interest rate	2,8%	5,7%	3,2%	2,4%	3,3%
$ROCE_{noa}$-ir	SPREAD	Spread	-24,4%	25,7%	19,5%	23,0%	15,7%
FGEAR*SPREAD	$FGEAR_{contrib}$	Financial gear contribution to the ROE	-33,6%	15,2%	13,7%	22,9%	21,3%

As it appears from figure 4.5 the ROE has been at a more or less steady level from 2005 until 2008. But looking at the basis year 2004 we can see a dramatic change. IC Companys has been able to convert a negative ROE into a positive ROE with 101,9 percentage point. The main reason for the low ROE in 2004 is the contribution of $ROCE_{noa}$. The borrowing rate is almost at the lowest level throughout the analytical period but still we get a negative SPREAD. The end result is that the financial gearing will have a negative effect on the equity so IC Companys is not able to earn on loan capital, actually they are losing on it.

The following year IC Companys suffers of both ascent and descent. In 2006 ROE falls with approximately 10% point and then it rises in 2007 with 12% point and then it falls in 2008 with 8% points. $ROCE_{noa}$ is the main cause for this development but it should be mentioned that IC Companys has been able to adapt the borrowing rate so it follows the development in ROE.

4.4.3 Decomposing the return on capital employed, $ROCE_{noa}$

The return on capital employed is an individual driver compared to ROE, but it has 2 underlying drivers on its own. The driver that affects ROCE is the profit margin (PM) and assets turnover (AT) regarding appendix 1.4.

PM measures the profit for each sold kroner from the company´s operating activities and can be said to be a tool that measure IC Companys ability to adapt the income and cost.

The asset turnover describes the funds tied up in a company and tells how heavy it is in capital. It also measures each kroner from the revenue invested in net operating assets.

Figure 4.6 development and decomposing the $ROCE_{noa}$

			2004	2005	2006	2007	2008
OP*100/NOA	$ROCE_{noa}$	Return on capital employed	-21,6%	31,4%	22,7%	25,4%	19,0%
OP*100/sale	PM	Profit margin	-8,6%	9,6%	7,0%	8,0%	5,7%
Sale/NOA	AT	Asset turnover	2,52	3,27	3,25	3,16	3,33
I/AT	Inversion		0,39	0,31	0,31	0,32	0,30

Looking at these values it is very clear that the problem IC Companys had in 2004 was to adapt the cost to the income because the profit margin is at a very low level. Asset turnover on the other hand is at very satisfying level.

If we compare the development in the profit margin with the development in ROCE we can see many similarities. Every time ROCE rise, profit margin rises as well and when ROCE falls, profit margin falls as well.

Asset turnover on the other hand has been quite steady but we can still see an improvement from 2004 to 2005. From then on it has been at a relatively steady level with small changes. When we take the inversion of the assets turnover we will be able to calculate how many “øre” IC Companys bind in net operating assets for creating “one krone” of revenue. The inversion of the asset turnover has improved in 2005 where only 31 cent of the net operating assets is acquired to create “one kroner” revenue. Otherwise it has been at a steady level since then.

In the following section we will go into further details and move to level 3 were we will analyze the underlying drivers to PM and AT to get a closer explanation for why these drivers have developed as they have.

Comparing IC Companys profit margin with some of its main competitors we can without any doubt say that IC Companys has a profit margin that is at a lower lever compared to the competitors.

	2004	2005	2006	2007
Revenue				
IC Company	2.612	2.821	3.022	3.354
H&M	62.986	71.886	80.081	92.123
Bestseller	741	997	1279	1486
Profit for the year				
IC Company	-309	201	224	241
H&M	7.275	9.247	10.797	13.588
Bestseller	86	138	154	193
Profit margin, %				
IC Company	-11,8%	7,1%	7,4%	7,2%
H&M	11,6%	12,9%	13,4%	14,7%
Bestseller	11,6%	13,8%	12,9%	12,9%

Especially in 2004 IC Companys has a profit margin that is at a very low level. The profit margin for the 2 other competitors is basically at the same level with small deviations. For Bestseller it is more than 11 % throughout the whole period and for H&M it is more than 12%.

On behalf of the above mentioned it is obvious that IC Companys has a problem with the profit margin. They have to improve this financial ratio to get to a level that equals the competitors. This indicates that IC Companys has to concentrate within the adjustment of the income and cost because the asset turnover is at an acceptable level. Our recommendation concerning the strategies of IC Companys is described in section 3.5 (strategies of IC Companys).

4.4.4 Analyzing the underlying drivers PM and AT

	2004	2005	2006	2007	2008
$PM_{gross\ margin}$	52,4%	56,5%	58,5%	59,1%	60,6%
$PM_{staffcost}$	-24,5%	-24%	-23,5%	-24,1%	-24,9%
$PM_{capacitycost}$	-56,5%	-50,1%	-48,5%	-49%	-51,1%
$PM_{beforetax}$	22,5%	29,9%	32,3%	32,2%	33%
$PM_{taxcost}$					
$PM_{sale\ after\ tax}$	12,7%	23,6%	23%	23%	23,3%
PM_{other} operating profit, after tax	-21,3%	-14%	-16%	-15%	-17,6%
PM	-8,6%	9,6%	7,0%	8,0%	5,7%

Figure 4.7

The underlying drivers to the profit margin

Figure 4.7 shows the underlying drivers to the profit margin. The profit margin has been decomposed into sole components so that we can be able to make a more thorough analysis of the profit margin. By doing this it will help us to identify those components that affect the profit margin into a positive or a negative direction.

During the analysis of the underlying components the $PM_{\text{other operating profit after tax}}$ has likewise been individually calculated. The reason is that we would like to “clean” the main profit margin from that part that cannot be expected to be continuous. The focus should be on the part that is from the core business activity which is equal to the operating profit from sale.

The above shown profit margins have some interesting characteristics.

PM_{gm} has throughout the accounting period been increasing constantly. In 2008 it reached the top point with a value of 60,6%. The growth has been greatest in 2005 and since then the increase in growth rate has diminished. Focusing on the total growth from 2004 till 2008 it has been about 16% point which point in the right direction.

The $PM_{\text{staff cost}}$ has been at a steady level. From 2004 and until 2006 they fell a bit, but then they started to increase and got up to a level that is greater than the value in 2004. The same can be said about the $PM_{\text{capacity cost}}$. They too started off with a fall and then they again started to increase, but this time the value in 2008 did not exceed the value in 2004.

Changes in financial ratios: It seems like that there have been some periods, especially 2005 and 2006, where IC Companys has been able to reduce the cost used to create one krone of income. But then again they have not been able to keep this at a long term level. But some of the change in the cost pattern can be explained in the strategy formulation. As mentioned earlier, IC Companys has from 2006/07 been focusing on own retail shops, which includes more employees and then results in increasing staff and capacity costs. Furthermore can the increasing use of promotion also be one of the causes.
The $PM_{\text{sale after tax}}$ has been constant from 2005. The only time it was low was in 2004 were it only was 12,7%. This improvement is caused by better cost structure were both the staff and capacity cost have been reduced and because there has been a huge improvement in the revenue.

$PM_{\text{other operating}}$ profit effects the main PM in a negative direction. Even though it has been improved through the years it still has a negative impact because of these “other items”.

Given an overall picture it indicates that IC Companys has been able to maintain a balance between the cost and income. 2004 is the only year where the cost was at a high level and the income at a low level. But the development does indicate that IC Companys is moving towards the wrong end because of the increasing cost. If IC Companys is able to maintain a high level of revenue in the future it will lead to a greater potential in achieving a high level of profit margin.

Underlying drivers to asset turnover (AT)

Asset turnover has further been decomposed for the sole operating assets and debt. Figure 4.8 Shows this decomposing

Figure 4.8

	2004	2005	2006	2007	2008
$AT_{mat\ assets}$	0,11	0,07	0,07	0,07	0,07
$AT_{immat\ assets}$	0,07	0,08	0,09	0,11	0,11
$AT_{fin\ assets}$	0,05	0,06	0,07	0,05	0,04
$AT_{inventory}$	0,16	0,13	0,12	0,13	0,13
$AT_{receivable}$	0,09	0,07	0,07	0,07	0,08
$AT_{trade\ payable}$	-0,08	-0,08	-0,09	-0,09	-0,08
1/AT	0,40	0,31	0,31	0,32	0,30
AT	2,52	3,27	3,25	3,16	3,33

IC Companys can increase the ROCE by keeping the operating assets at a minimum and increase the revenue. The overall AT has in average been increasing throughout the analytical period because of a fall in the trade receivable and an increase in the trade payable.

Overall the AT has been increasing and has been improved by almost 1 from 03/04 - 07/08

4.5 Trend analysis

A trend analysis illustrates how each accounting item has been developing throughout the analytical period compared to a basis year.

Appendix 1.5 shows the indexed income statement and balance sheet for IC Companys where 2004 is the basis year. Looking at the income statement one will realize that there is a lot of items that are detached and/or deviate compared to the basis year. But we have found that Revenue, operating income from sale, operating income and the comprehensive income are those items that are most interesting to comment on.

The revenue has already been discussed in section 4.4.1 and will not be further commented on in this section. The indexed operating income from sale has experienced a huge positive development compared to the basis year. Each of the years has an index that is more than 200 and ends at a level of 262 in 2008. This is more than a doubling. The same cannot be said about the operating sale. In this case IC Companys experienced a small rise that again fell in 2006 and kept falling until 2008 were it actually reached a level that was lower than the basis year. The development in the comprehensive income is similar to the development in the operating income from sale. It has been positive developments compared to the basis year even though there have been ups and downs in the analytical period. But still we have an index that is more than doubling in 2008 compared to the basis year.

The indexed material fluctuates, why it makes it difficult to look for a specific pattern. Because of the fluctuations, the trend analysis cannot be used to conclude something specific about the development and it will therefore not be examined further.

4.6 Risk analysis

The risk in IC Companys is based upon both the operating and financial relating risk. Furthermore the line of business also reflects the risk profile. In the following, we will discuss the first two types of risk in IC Companys throughout the analytical period.

The analysis will enlighten the variability risk which shows why the company has not been able to reach the earning that was expected.

An investor has in general aversion towards risk. This mean that the required rate of return must reflect the risk an investor undertake by investing in a particular company or share. When the risk in a company or share increases the investor must be compensated for it by demanding a higher required rate of return.

As mentioned, the rate of equity depends on the rate of capital employed the financial gearing FGEAR and the SPREAD.

The total risk in a company comprises both the operating and financial risk and is given by the equation:

Total risk = operating risk * financial risk

In the following sections we will treat these risk objects.

Operating risk

The main purpose of analyzing the operating risk is to get a view into IC Companys proportion of fixed and variable cost. This will make it easier for us to understand how a change in the company´s revenue will affect its earnings. This analysis will furthermore enlighten IC Companys ability to adapt to the macro and micro economic circumstances that can cause a change in the revenue as well the earnings. Some of these factors could be falling sales prices, increasing cost price and the general demand for some specific brands.

The operating risk reflects the variance in the return of capital employed. By that we mean it shows the fluctuations and changes in the earnings.

Before we are able to evaluate the relationships between the fixed and variable cost one must analyze the cost structure in order to determine how a change in the revenue will affect IC Companys earnings.

Operating gearing and cost structure

The external analyst is not able to make a “perfect” classification of IC Companys cost structure regarding the fixed and variable cost on behalf of the published annual reports. Because of that one must assume that the calculated financial ratios are based upon IC Companys ability to make a correct break down of the cost into fixed and variable cost.

Throughout the accounting period the production cost will be analyzed to find out if these costs include fixed costs to be able to distinguish between fixed and variable costs. Our examination of the published annual report has though not given any concern for that and therefore we have maintained the distribution of the fixed and variable cost.

Another uncertainty dilemma that occurs is whether “other types of cost” is including some variable costs. But it is not possible for us to isolate the variable cost.

The cost structure could also be affected by some varying cost which would have an impact on the operating gearing. This would be the case where IC Companys activity would achieve a specific level. Because these items have also not been identified it cannot be analyzed.

The analyst should be cautious with the interpretation of the operating risk. But the calculations can though be used to identify the level of the gearing.

		2004	2005	2006	2007	2008
Fixed cost/total cost	OGEAR^1	0,49	0,52	0,53	0,53	0,55
Fixed assets/operating assets total	OGEAR^2		0,46	0,50	0,48	0,46
Operating debt total/net operating assets	OGEAR^3	0,50	0,54	0,58	0,51	0,61

The leverage has been calculated in figure 4.9. As an alternative to the calculation of OGEAR we have calculated the leverage between the fixed assets and operating assets (OGEAR^2) and the operating debt compared to the net operating assets (OGEAR^3).

As it is shown in figure 4.9 the “leverage values” for the operating gearing has been at a constant level without huge fluctuations. OGEAR^1 shows mostly an increasing tendency but this might be because of the change in the strategy where they have a greater focus at own retail shops. OGEAR^2 on the other hand has been at a very steady level. But the development seems to go in the right direction. The only significant fluctuation we see is in OGEAR^3 where the value gets to 0,61 in 2008 from 0,51 in 2007.

But the fact that OGEAR[1] is greater than OGEAR[2] could be found in the uncertainty there is with the distribution of the cost in fixed and variable cost.

Break-even sale and safety margin

When analyzing the break-even sale and the safety margin will still assume that IC Companys has made a proper distribution of the fixed and variable cost.

		2004	2005	2006	2007	2008
Revenue		2.612,2	2.820,6	3.022	3.353,8	3.737,2
Fixed cost/Gross $margin_{reformulated}$	Break-even sale	2.466,4	2.373,6	2.384,8	2.643,1	2.972,5
(Revenue-breakeven)/revenue	Safety margin	5,6%	15,8%	21,1%	21,2%	20,5%

Figure 4.10 shows the safety margin for IC Companys. The development has been positive. Looking at 2004 we can see that the safety margin is at a very low level. That means IC Companys can only afford to have a decrease of 5,6% in the revenue before the profit will turn into loss. The reason for the low safety margin in 2004 is the high rate of fixed cost. But from then on the safety margin has had a huge rise. It grew to a level of 15,8% in 2005 to a end result in 2008 20,5%. This means that even though IC Companys has had an increasing fixed cost rate it has been able to have a greater increase in the revenue. Though, as mentioned, IC Companys has announced a fall in the revenue and growth rate in the future. They could get into a difficult situation with at falling growth rate and revenue whereas the fixed cost is rising. They should already at this particular moment try to reduce the fixed cost. Another reason for why IC Company should be focusing on minimizing the fixed cost is there historical development. It is noticed, that when the macro and micro economic development is positive then IC Companys is able to get high revenue as well a high profit. But as soon there is a negative development in the macro and micro economic factors it will affect IC Companys and the profit would decrease significantly. To avoid this they have to adjust to the environment by reducing the fixed cost so that they can be more competitive.

The operating risk is besides, the above mentioned, also affected by the volatility in the demand. In this case IC Companys has an advantage of being a company with a high level of diversification. Being a multi brand company they can compensate the fall in one brand with the rise in another brand. Other operating risk factors could be sales prices, discounts, cost prices, fluctuations in the exchange rate and so on.

The operating leverage is at a middle level. This means that IC Companys would attain a relative high profit by growth in the earnings compared to an increase in costs. An increase in earnings will surpass an increase in costs.

Financial risk

The financial risk is calculated on behalf of the financial leverage and distribution in SPREAD(interest margin ~ $ROCE_{noa}$- r). The interest margin depends upon the net interest rate and the return on capital employed.

When the SPREAD gives a positive value it can be said that the company earns on the loan capital. On the other hand when SPREAD gives a negative value it means that the company loses money on the loan capital. This refers to the “lever-effect” where a rise in the SPREAD leads to a rise in the total sale.

Figure 4.5 shows that except from 2005/06, the financial leverage has been at an overall constant level throughout the analytical period.

When we look at the SPREAD for IC Companys we will notice that they had a huge negative SPREAD in 2004. But in 2005 the development turned around. From having a SPREAD of -24,4% in 2004 it rose to 25,7% in 2005 and now have a positive leverage. The following year the SPREAD has been both decreasing and increasing. But in 2008 it fell to 15,7%, which is a huge fall compared to 2005. But as a general overview, one can say that IC Companys has had positive leverage where it has been able to raise the return on equity towards the return on the operation ($ROCE_{noa}$) ~ lever-effect.

Another important factor when looking at the financial risk is the borrowing rate. If the borrowing rate increases it can have a negative effect on IC Companys. There have been periods where the $ROCE_{noa}$ has been at a low level and contributed negatively to the financial risk. The borrowing rate (net interest rate cost/net interest bearing debt) has been at a reasonable level throughout the period. In 2004 it was 2,8% but rose to 5,7% and fell again until 2008 where it got to 3,3%.

It is important for IC Companys that $ROCE_{noa}$ increases. The main reason is that the borrowing rate is at a reasonable level where the probability for lowering it further is small. If we look at IC Companys $ROCE_{noa}$ in 2004 we can see it is negative and is the main reason for the negative SPREAD. But when the $ROCE_{noa}$ has developed into positive figures we get huge positive SPREADS. Because the positive ROCE leads to a positive SPREAD, the leverage will contribute to the lever-effect where it will affect both ROE and the owners return into positive. If the SPREAD is negative it will lead to what is called "the opposite lever-effect").

From an overall perspective the financial risk seems to be at a middle/good level. The reason is that the SPREAD is at a good level as well. But what might be a bit of concern is the development for the coming year 2009. But at this particular moment it seems to be at a good level.

4.7 Analyzing the growth

The growth potential in IC Companys depends on the company's ability to use the necessary financial resources to create and finance the forthcoming growth whether this is organic growth, purchase of brand, joint venture etc.

Before we are able to budget the prospective growth rate we must analyze IC Companys historical and present growth. It's important to determine whether the present development is a good indicator for the expected prospective development in the profitability by looking at ROE and its underlying drivers.

In this connection it is important to determine whether the profitability is affected by extraordinary items that cannot be expected in the future. By this we mean the transitory profit components.

We will in the following sections compute IC Companys permanent profit where the transitory will be excluded. By doing this we will only have profit components that has been gained from the companys permanent profit the so called core operating profit.

Permanent profit:

As mentioned in the above section will the historical and present growth rate "blaze the trail" for budgeting the prospective growth.

In appendix 1.7.5 is IC Companys profit divided into permanent and transitory items.

This statement shows that the calculated permanent profit is more or less equal to the operating profit from sale in the last two years of the analytical period. But for the first three accounting years the differences are huge. The difference in the permanent profit compared to the reformulated income statement is caused by the transitory tax components that now has been both calculated and separated to get the tax effect.

The distribution between the permanent and transitory profit has been thoroughly examined in appendix 1.7 and therefore it will not be discussed here. We refer to appendix 1.7.

Figure 4.11 shows the decomposing of $ROCE_{noa}$. The financial ratios have first been decomposed into the part that comes from the transitory items and the permanent (core) profit. On behalf of this distribution it is obvious that the transitory items on the net operating assets have a huge impact on $ROCE_{noa}$. Especially in the year 2003/04 IC Companys gets a negative $ROCE_{noa}$ because of the deficit in the transitory items. The remaining years IC Companys is able to maintain a positive $ROCE_{noa}$ but the transitory items still have a negative effect on $ROCE_{noa}$.

Figure 4.11

		2004	2005	2006	2007	2008
TI/NOA		-61,6%	-38,8%	-60,7%	-44,6%	-59,4%
$_{Core}$ OP/NOA	$_{Core}$ $ROCE_{noa}$	40,0%	70,2%	83,3%	70,1%	78,4%
OP*100/NOA	$ROCE_{noa}$	-21,6%	31,4%	22,7%	25,4%	19,0%
$OP_{after\ tax}$ *100/sale	$PM_{sale\ after\ tax}$	12,7%	23,6%	23%	23%	23,3%
$OO_{after\ tax}$ *100/sale	$PM_{other\ op\ profit\ after\ tax}$	-23,3%	-14,0%	-16,0%	-15,0%	-17,6%
OP *100/sale	PM	-8,6%	9,6%	7,0%	8,0%	5,7%
$_{Core}$ OP_{sale} *100/sale	$_{Core}$ PM_{sale}	15,8%	21,5%	25,6%	22,2%	23,6%
SALE/NOA	AT	2,52	3,27	3,25	3,16	3,33

We have furthermore made a decomposing of PM into $PM_{sale\ after\ tax}$, $PM_{other\ op\ profit\ after\ tax}$ and $_{Core}$ PM_{sale}.

From this decomposing of PM we can see that both $_{Core}$ PM_{sale} and $_{Core}$ PM_{sale} are actually more or less at the same level throughout the whole accounting period. But we are still able to see a specific pattern in the development of these two financial ratios. The difference between these two financial ratios is greatest in the first 3 years of the analytical period compared to the last 2 years. The reason for this is that, the first three years has a relative high adjustment of the tax component compared to the last two accounting years. Therefore the effect is greatest in the first three years.

We see here that there is a huge difference. One of the reason is that sales and administration cost has not been included in the core profit but is a part of the transitory item. The reason for that is that we as an external analyst are not able to identify the size of these cost. IC Company has put these cost in “other operating profit”. But when you look at the note for this particular item it will not clarify anything. Therefore we have been forced to recognize these costs as transitory cost and not as a part of the permanent cost.

Regarding the budgeting and valuation of IC Companys we can make use of the calculated financial ratios. Though, we have to be careful of using the core PM_{sale} specially the first three accounting years because of the huge tax adjustment.

But as it has been mentioned in previous section, IC Companys is going through a turnaround process where there has been change in the strategy. This makes it even more important that we use this historical development with cautiousness. Even though these values indicate a high growth rate we have to keep in mind that the upcoming annual report states that a negative growth is expected. This and some assumptions concerning the core PM_{sale} and other important financial ratios will be used in the final valuation of IC Companys.

4.8 Growth in funds generated from operations

A growing sale mostly requires a growth in the net operating assets. This means that before one can finance the growth the financial resources have to be available. The growth can be achieved in several ways. It can be achieved by financing its own operations or turn to loan capital. However, the last option will only increase IC Companys financial risk. The last way of achieving this, is by contribute additional capital by carry out a share issue for new or present shareholders.

By contributing additional capital we will be able to increase the debt-equity ratio without affecting the financial risk. On the other, if we choose to achieve growth through enhanced borrowing it will result in an increased financial leverage and risk.

	2004	2005	2006	2007	2008
$g^* = (PM*AT)+[FGEAR*(ROCE_{noa} - ir)] * (1-d)$	-55,3%	46,7%	36,5%	41,9%	33,3%
$g^{**} = (PM_{pp}*AT)+[FGEAR*(ROCE_{noapp} - ir)] * (1-d)$	91,1%	108,5%	139,9%	118,4%	147%

Figure 4.12

Figure 4.12 shows the growth rate for funds generated from operations for IC Companys calculated on behalf of the original financial ratios(g*) and by using the items from the permanent profit(g**) so that we can be able to see the growth rate cleared for transitory items.

Looking at the calculated growth rate for funds generated from operations (g*) one will notice that it equals the ROE that has been calculated in one of the previous sections. But this will only be the case for the first three years. That's because IC Companys did not pay any dividend throughout these years. This is different in 2007 and 2008 due to the paid dividend. G* is negative in 2004 due to the negative PM.

If we look at the growth rate for funds generated from operations where only the permanent profit has been taken into consideration one will see there are huge differences. Before commenting on this we have to keep in mind what has been said about the PM from core operating. In this case is the growth rate for all the accounting years not only positive but almost 100% or more. The main reason for exactly this development is the PM. We see that core PM is positive trough out the analytical period. But the main reason for why it has such a high PM is due to the lack of information about the sales and administration cost that has not been included in the core profit. But still these financial ratios can be used to guide us in the right direction for what IC Companys must improve.

What IC Companys should keep doing is to increase ROCE through PM to a level that is greater than the borrowing rate, which will lead to a positive growth rate. In this way it will not be necessary to get some external funding through the equity. This might be illogical because IC Companys financial ratios actually show a good result. But we have to keep in mind that IC Companys has been through a very difficult period. When the macro and/or micro economic factors are heading towards a positive direction IC Companys will come out with a terrific result. But as soon the macro/micro economic factors are heading in a negative direction the result will be the exact opposite. They need to be on the leading edge. That's why we believe that they must improve their PM by firstly reducing the fixed costs. Other initiatives could be better sales prices etc.

4.9 Liquidity and finance

From having focused on IC Companys profitability, risk and growth we now move our focus towards IC Companys cash flow statement, its liquidity and finance. The cash flow statement can be a useful tool to evaluate the quality of the result IC Companys has achieved at the specific accounting year. It can furthermore be used to evaluate whether the operating income has been based upon real cash flow movements or is it based upon calculatorial items.

We will in this section compare the free cash flow (FCF) that has been calculated on basis of the reformulated cash flow statement with the theoretical calculation of FCF. Our main concern is to identify whether there is a reasonable difference between the calculation of the cash flow from the operation and investment. This is done by subtracting the change in net operating assets from operating profit, and the difference (FCF) is to be compared the FCF from the reformulated cash flow statement.

Figure 4.13 shows the calculation of the free cash flow (FCF)

Figure 4.13

	2004	2005	2006	2007	2008
Cashflow from operating activity corrected	142.955	291.670	335.877	306.200	364.305
Cashflow from investing activities corrected	-77.038	-82.600	-141.800	-186.400	-138.400
FCF	65.917	209.070	194.077	119.800	225.905
Operating profit	-224.083	271.165	210.430	269.590	213.730
Change in net operating assets	-351.883	6.583	124.900	138.100	-11.100
FCF	127.800	264.582	85.530	131.490	224.830
DIFFERENCE	61.883	55.512	-108.547	11.690	-1.076

When calculating the theoretical FCF it can be done by using 2 methods. Figure 4.13 only shows one of the methods whereas the other method is available in appendix 1.9.3. But the end result is the same for both methods. When we look at figure 4.13 we can see that there is huge deviation between FCF from the reformulated cash flow statement and the theoretical calculated FCF.

We can see that there are huge differences in the two calculated FCF for the first three years. In 2004 the difference is 61,9 mill DKK whereas the difference diminishes in 2005 to 55,5 mill DKK and

reaches a level of -108,5 mill DKK in 2006. The differences in 2007 and 2008 are 11,7 mill DKK and -1,1 mill DKK respectively, which is acceptable.
The differences that appear in 2004 and 2005, which have a positive effect can be due to a lots of things. But we believe that the primary cause is that IC Companys closed loss-making shops and converted some of them into franchise. In 2005, 50 shops were terminated and 20 of them were converted into franchise. IC Companys has furthermore sold Sir of Sweden and liquidated the self owned brand Error. In 2006 IC Companys acquires the distributor of Peak Performance in Norway, Adventure Sport & Leisure AS and One of the Group´s sourcing agents in Turkey. When acquiring these companies IC Companys also acquires there interest bearing debt. This interest bearing debt has not been stated in the published annual reports and therefore it is not possible for us to identify the size of the part that originates from the acquired companies. The debt has an impact on FCF and it might be one of the reasons for the huge differences.

On behalf of the above mentioned and the lack of exact information regarding the huge differences in FCF it can be said that, the external analyst don't have the possibility to declare the differences in FCF compared to the realized results because of some main missing parameters. Evaluations will be made in regards to this in the conclusion. The conclusion of the financial analysis will be made in the end of the report.

5. Valuation

The purpose of this section is to estimate the value of IC Companys. This valuation will be made by using the historical financial analysis and the knowledge we have attained from the strategic analysis of IC Companys to determine different drivers, among these the budget as reference to the valuation.

IC Companys portfolio consists of key brands as well as portfolio brands, which are distributed through the 3 segments, wholesale, retail and outlet. The segments operate under at least 2 different markets - and competitive terms where wholesale is directed towards approximately 12.000 customers including franchise partners who run concept stores. Retail and outlets is on the other hand IC Companys own shops. In the analytical period the degree of earnings has been different for the three segments. All three segments have though been able to produce positive values through the whole analytical period. When taking the valuation into consideration it would be sufficient to make a budgeting on these three segments.

The information that has been given in the published annual reports is not sufficient enough to make budgeting at a lower level than the revenue. When looking at the analytical period from 2004 until 2008 it appears that wholesale represents approximately 70% of the revenue, retail 27% and outlet approximately 3%. The numbers vary a bit from year to year but looking as a whole it gives a fair presentation.

Regarding IAS 14 a company does not have to show level of earning and invested capital for each brand and segments. The only asset turnover that we can make use of is the one that has been used in section 4.4.4 where the net operating assets show that IC Companys bind 0,40 DKK for each sales kroner for the accounting year 2004. This gives an asset turnover of 2,52. In the budgeting we will only make use of asset turnover at this overall level and not at segment level.

5.1 Estimating the operating assets cost of capital (WACC)

Both the lender and the shareholder have demanded a minimum return on their investment. The weighted average cost of capital (WACC) express this return that IC Companys has to be able to achieve by the invested capital so that both the lender and the shareholder can be satisfied. When evaluating the company the cost of capital is the factor that is used to discount the residual income that has been calculated on behalf of the budgeted period. The weighted average cost of capital is expressed by the equation:

$$WACC = \frac{E}{V} * Re + \frac{D}{V} * Rd * (1 - Tc$$

Where:
Re = cost of equity
Rd = cost of debt
E = market value of the firm's equity
D = market value of the firm's debt
V = E + D
E/V = percentage of financing that is equity
D/V = percentage of financing that is debt
Tc = corporate tax rate

Estimating the weighted average cost of capital depends on the capital structure (the relationship between the market value of the equity and the market value of the net interest bearing debt), the cost of equity, the average borrowing rate on the debt and then finally it depends on the corporate tax.

Estimating the shareholders required rate of return

As it appears from the above, one of the most essential factors concerning an investment is the shareholders required rate of return. In the following we will estimate this required rate of return by making use of the CAPM- model. CAPM-model describes the relationship between the expected return and the risk for each company compared to the whole stock market. Assuming that an investor would require a higher expected return as compensation for the higher risk that will be involved.

Estimating the shareholders required rate of return by using the CAPM-model

CAPM (capital asset pricing model) divides the risk into a systematic and an unsystematic risk. The systematic risk can be explained by the general movements in the markets and can therefore not be diversified. This is the part of risk that CAPM-model tries to price. The unsystematic risk on the other hand is the part of the risk that is diversifiable. This risk occurs as a result of some company related factors that can be diversified if the investor decided to place its capital in a portfolio of shares where he can make use of all diversifiable advantages of a portfolio consisting of about 15-20 different shares.

The CAPM model consists of the risk-free interest rate, beta, the expected return by investing in the market portfolio and finally the market risk-free premium.

$$\overline{r_a} = r_f + \beta_a(\overline{r_m} - r_f)$$

Where:

r_f = Risk free rate

β_a = Beta of the security

$\overline{r_m}$ = Expected market return

We have decided to determine the rate of a risk-free investment by using leading treasury bond that is used as a risk-free investment.

The leading treasury bond with 4% nominal expiration to 2019 is set to an effective payment of interest to 3,8677 % at august 31, 2009.

The beta can be explained as a securities relative risk compared to the market risk. Securities with a beta value greater than 1 is assumed to be aggressive, because the increase in a security's expected return would be greater than increase in the market portfolio expected return. On the other is security with a beta value less than 1 called defensive securities.

The beta value will be determined by valuing IC Company's operating and financial risk. Our valuation will be based upon analysis and circumstances of IC Companys present and forthcoming accounting risk, the strategic position etc. and will be compared with an external share analysts opinion. In section 4.6 of the analysis of the profitability we saw that IC Companys total operating and financial risk is at middle/high level. Combining this with the line of business IC Companys is operating within where you must be quick to reorganize (the fashion business) and that the safety margin is expected to get worse we have decided it to be at a level above 1.

In September 2008 Spar Nord made an analysis of IC Companys. This was at a time where IC Companys had not announced the predictions for the forthcoming years. If we look at the beta values Spar Nord has predicted for IC Companys for the three last years it has been at a steady level of 1,10. In the forthcoming year IC Companys has made some reduction in the fixed cost, as a result of the falling growth rate. "Danish share analysis" has set the three year beta value to 1,19. On behalf of the above we have decided to estimate the beta value to 1,15.
The premium for the market risk (r_m-r_r) can be estimated on behalf of some prior analysis where the movements in the markets including inflation and other social changes will be included in the final estimate. The purpose of this estimation is to avoid temporarily random effects. As an alternative the premium can be estimated by valuing present share prices through for instance the residual income model. The third option is to make an enquiry about how different investors valuate the market risk premium.

The premium for the market risk has been set to 5% on behalf of some analysis that indicate that the investors expect a premium of 3-7%. We have decided to use the estimate of 5% because it does not deviate that much from the analysis that has been made in 2007 by KPMG where they indicated the estimate to a steady level of 4,5% since 2002.

The last factor we have to include before we can estimate shareholders rate of return is the percentage supplement that has to be added because of the shares illiquidity. We have set this rate to be 1,4% because Niels Martinsen owns 39% of IC Companys shares through the company Friheden Invest.

There is a lot of criticism about the CAPM model but we will only highlight some of them. One of the criticisms is that it is considered as a one-period model under the assumption that the premium for risk is constant over time. One could imagine that the premium of risk is different for different periods. As another critical point is that CAPM is a model where the expectation to the future is based upon the historical data where you assume that these expected events will occur over a longer period of time.

The model furthermore assumes that no investors can affect the price of a security or a share. This assumption secures that the price of a security is decided by the demand of all the investor. But in the practical life many of the shares are traded by institutional investors who can affect the market price of the security. This can also be used in our case where Niels Martinsen owns 39% of the capital and will be able to affect the price of an IC Companys share and will make the share illiquid.

The assumption about homogenous expectation, where all the investors have kept identical market portfolio and have the same view on the expected return and risk is over a period of time practical unrealistic.

Despite the fact that CAPM- model possess some weaknesses we will still be using this model to estimate shareholders required rate of return because this model is the most useful model in practical life.

$$\overline{r_a} = r_f + \beta_a(\overline{r_m} - r_f)$$

Where:

r_f = Risk free rate

β_a = Beta of the security

$\overline{r_m}$ = Expected market return

= 3,8677% + (1,15*4,5%) + 1,5% = **10,54%**

Estimating the capital structure

The shareholders required rate of return has now been calculated and we only need to calculate the capital structure before we can estimate the WACC. The purpose of projecting the capital structure is because the cost of equity that is related to the shareholders and the cost of debt that the lenders require are different. These costs of capital of IC Companys will be included in the weighted average cost of capital.

In connection with the profitability analysis and the decomposing of the financial ratios in figure 4.5 we showed the calculated net interest bearing cost to be 3,2% in 2006, 2,4% in 2007 and 3,3% in 2008.

When we have to estimate the required rate of return for the debt we will add a greater risk supplement than is already included in the calculation of the interest rate. The macro economic system is in recession and that's our argument for the risk supplement. There will the cost of capital for the debt be a bit higher than the rate that was calculated in the profitability analysis. It will though not impair the historical accounting analysis because the valuation is based on ex ante values.

	2004	2005	2006	2007	2008
Equity	290.242	538.500	579.500	566.600	473.500
Net interestbearing debt	498.000	322.700	410.200	562.700	644.700
Share of equity	36,8%	62,5%	58,6%	50,2%	42,3%
Share of NID	63,2%	37,5%	41,4%	49,8%	57,7%

Figure 5.1

As it appears from figure 5.1 the capital structure has been quite unstable. In 2004 and 2008 IC Companys had a greater share of debt compared to equity. And in the three middle accounting years has the share of Equity been greater than the share of debt but this share has been decreasing. If we look at the forthcoming accounting year 2009 we would see that IC Companys still has a greater share of debt compared to equity. Therefore we have decided to use an equity/net interest bearing debt to be 47/53 and are estimated as the long term capital structure.

We do not have any long term budget of IC Companys that can support this (above-mentioned - capital structure). Vice versa, we also do not have any material that contradicts what has been stated above.

Calculating the cost of capital for the lender finance:

The capital cost of the lender financing (k_d) should basically be based upon the current market interest. This is the interest rate that IC Companys would be able to borrow at. This interest rate can be estimated by using the equation for k_d. The risk-free rate, the company specified risk supplement and the corporate tax are all included in the calculation of k_d. The corporate tax has been reduced from 28% to 25% and has therefore been recognized with 25%. The corporate tax-rate for all of IC Companys subsidiaries is unknown and therefore we have chosen to use the Danish corporate tax-rate.

Looking at the equation we can see that the only element that is missing is the corporate risk supplement to calculate the k_d. When a company grant this risk supplement it can be seen as a type of compensation for the lender to grant the company with a loan, when the lender assumes the company as being more risky than the market portfolio. This supplement is most commonly calculated by different finance houses where they credit rate the company. At this particularly moment is has not been possible for us to find a finance house who have made a credit rating of IC Companys. We have therefore decided to make use of risk supplement of 4% which is a bit higher than the supplement that is used in different credit ratings.

The reason for why we have decided to use a supplement that is higher than used normally is because Niels Martinsen has an indirect influence on the price and especially in this case where he has chosen to keep his stock of shares in IC Companys. Besides that, IC Companys has experienced a change in the management and the fact that IC Companys is a company who will be affected by the financial crisis/economic fluctuations, which also affects the result. All of this is the basis for the higher rate of the supplement.

$$\text{Cost of capital}_{\text{for debt}} = (IR_{\text{risk-free}} + IR_{\text{supplement}}) * (1-Tax_c) = (3{,}8677\% + 4\%) * (1-0{,}25) = 5{,}9\%$$

Where

$IR_{riskfree}$ = risk-free interest rate

$IR_{supplement}$ = risk supplement

Tax_c = corporate tax

As mentioned earlier we have calculated the net interest cost which can be said to be equal to the required rate of return for the investors. The calculated interest rate in 2008 was 3,3%. If we compare this calculated interest rate with the calculated 5,9% from above we can see that the difference mainly is the risk supplement. If we adjust this supplement for the tax we will get a value of 4% * (1- 0,25) = 3,0% and adding it with the net interest cost of 3,3% we get (3,3% + 3,0%) = 6,3% which is more or less the same as the calculated above.

Calculating the weighted average cost of capital WACC

When we have calculated the required rate of return for the shareholders and the share of the equity to be 47% and that the cost for the borrower finance is set to 5,9% we can then calculate the cost of capital to be 8,1%.

$$WACC = E/V * Re + D/V * Rd \quad C_{WACC} = 0{,}47*10{,}54\% + 0{,}53*5{,}9\% = \mathbf{8{,}1\%}$$

Where:
Re = cost of equity
Rd = cost of debt
E = market value of the firm's equity
D = market value of the firm's debt
V = E + D
E/V = percentage of financing that is equity
D/V = percentage of financing that is debt
Tc = corporate tax rate

SparNord uses a WACC of 7,92%. The calculated WACC is a bit higher than the WACC that has been estimated by a professional analyst. This can be caused by the degree of subjective estimation there is combined with calculating the WACC and its components.

5.3 Budgeting

The budgeting will be based upon some of those value drivers that can express the forthcoming expectation to the financial ratios in the profitability analysis. In a perfect world would the sole value drivers be calculated by using historical financial ratios that has been calculated in the profitability analysis and combine it with the future prospect that has been drawn from the strategic analysis. IC Companys has furthermore been through some turbulent years which the analysis shows and the valuation will mostly be based upon the realized values from the 3rd quarter of 2009 and from the statement from the management concerning the future prospects.
The key value drivers and budgeting items are the revenue, turnovers, earnings contribution and the operating profit before tax. But because IC Companys is a cyclical company we will budget the company by best and worst case scenario. We will then rate/weigh these two scenarios in regards to their respective probability in order to calculate the value of IC Company.

Determining the budgeting period

When determining the budgeting period there is several factors that has to be taken into account such as the company's existence in the market, the sole brands life cycle, possession of new production technology and especially for IC Companys they must have a competent and competitive designer team or some advantageous distribution channels.

Since the merger In 2001 IC Company has been through some changes. Today it is 8 years after the merger. Within the first 4 years IC Companys went through lots of changes within the strategies and the turnaround process. The last 4 years they actually have managed to have a more sorted product portfolio, have more clear strategies and has some good results. But still there is not consistency in IC Companys. They have had very fluctuating results throughout its life. This and some of the calculated financial ratios are a valid foundation you can base your valuation upon. Because there is such an uncertainty combined with IC Companys, it is difficult for us to clarify when IC Companys will reach a stable stage, but an estimate would be within 4-7 years.

We have set the budget period to be 10 years because a period longer than that will be connected to lots of uncertainty. The budget period would be from 1/7- 2009 to 30/6- 2019. It should be noted that the budget starts with the current accounting year 2008/09 where they have published the announcement for 3rd quarter and the expectations to the revenue and result before tax. We have evaluated 2009 of being the best starting point because the budget period is the extension of the analytical period. The budget period will be followed up by the terminal period that will be starting at 1/7-2019 and continue forward.

Budgeting the revenue and the gross margin

The starting point for the budgeting and one of the most important items to forecast is the revenue and its development throughout the budget period. The portfolio is no longer divided into main brands and portfolio brands but in a multi brand strategy. The growth rates of revenue are estimated for each brand in the portfolio in regards to their expected sales development. This requires that we can achieve knowledge about how the development is in each brand and the proportion they are contributing to the revenue and the valuation. This will also make it possible to determine the prospective potential for IC Companys.

We believe that in connection with the turnaround process IC Companys is confronting they will surely make use of the revenue and the bottom line as their performance indicator and they will also be important in the forecast. The turnaround process implies that IC Company must increase the sales on its main brands and at the same time be focusing on the bottom line by reducing the cost and achieving synergy.

Concerning the development in the revenue, we expect the Retail and Leadership Academy to contribute positively to this development. The staff and managers are trained, educated and given the right competences to make the firm more efficient.

Our main focus has as well been on the revenue and the bottom line in connection with the budgeting.

Revenue of the brands:

Peak performance and Tiger of Sweden represent approximately 40% of the whole revenue whereas InWear, Jackpot, Matinique, Cottonfield, Part two and by Malene Birger represents approximately 55%

of the revenue. It is stated in the announcement of 08/09 that the brand Inwear, Matinique, Cottonfield, Tiger of Sweden and Jackpot has experienced a two-digit decrease in revenue whereas Part two and some other brands have had a two-digit improvement in revenue. We will budget with the same development throughout the whole 2008/09. In The best case scenario we will budget some of IC Companys main brands such as Matinique, Jacpot and Cottonfield with a fall of each 5% until 2010/11. But we believe that from then on the growth will be improved with a growth rate of 3% to the rest of the budget period. This is due to several reasons. First of all IC Companys has got a new management who entered IC Companys 2007/08. The new management’s forthcoming plans are to have a high priority on the cost reduction instead of a middle/moderate approach. Another thing is that the whole world is going through a financial crisis. This has an impact on all major line of business. As it seems this crisis will be solved within a couple of years. As mentioned before IC Companys is a company that follows the market conditions. When the economy is booming then IC Companys will get a very satisfied result.

In the worst case scenario these brands are set to have a decrease of 9%, 6% and 10% for respectively Jackpot, Matinique and Cottonfield. These are the same percentages that these brands have declined compared to last year. This has been chosen in the case if IC Companys fails to adapt to the market. These percentages will be set to 2010/11 and from then on we believe in a slight increase of the brands of respectively 2%, 3% and 2%

InWear has experienced a decrease of 23%. We have again decided to have a decrease in this segment until 2010/11 of 15% and from then on we believe it might turn into a 3% growth until the terminal period where the growth rate will be set to 2%.

If IC Company fails to adapt to the market conditions in same extent then we believe that the decrease in the first 2 years would be 20% and from 2010/11 until the end of the budgeting period the growth rate will be set to 2%. In the terminal period it has been set to 1%. This would be the worst case.

Part two, By Malene Birger, Soaked in luxury, Saint Tropez and Designers Remix Collection on the other hand have experienced a growth of approximately 15% in average. We have estimated that these brands will continue with this development because they have been successful in meeting the requirements of the market. We have estimated a growth rate of respectively 7%, 13%, 15%, 9% and

15% until 2011/12 and from then on the estimates will be 5%, 7%, 9%, 5% and 9% until the terminal period. In the terminal period they will be set to 5% all of them besides Soaked in luxury and Part Two, which will be set to 3%. The reason why we are being a bit optimistic here is that these brands have done very well in a period of recession.
In a worst case scenario they will be estimated to a lower growth rate due to the difficulties in maintaining high growth rates. In this case the estimates would be 5%, 10%, 10%, 8% and 10% until 2011/12. From then on it would be estimated to 3%,5%, 5%, 3% and 5%. In the terminal period they would be 2% for all of them.

If we look at some of the main brands, Peak performance and Tiger of Sweden, the development has been in complete contrast. Tiger of Sweden has been declining with 11% whereas Peak Performance has increased with 5%. These two brands generate 37% of the revenue where Peak Performance has 25% and tiger of Sweden 12%. If IC Companys predictions will be fulfilled regarding their strategies then we will project Tiger of Sweden with a declining rate of 5% until 2010/11 and from then on it will grow with 3%. In the terminal period it will be a more moderate growth rate of 2%. Peak performance on the other hand will grow throughout the whole period. In the first 3 years the growth would be 5% and decline to 4% until the terminal period where it would be 3%.

If we believe the worst case scenario where IC Company will not be able to adjust the cost and to the market condition then we will see a decline of Tiger of Sweden of 8% in the first 3 years and from then on it would grow at a moderate level of 2% and growth rate of 1% in the terminal period. Peak Performance has been the key brand and it will grow at a more decent growth rate compared to the best case scenario. Our estimate is 3% for the whole period and in the terminal period it would be 2%.

The revenue in general

Looking at the announcement for 2008/09 IC Companys states that they expect a small decline in 2008/09 compared to 2007/08. On behalf of the announcement and the development in the market we have budget the revenue for 2008/09 to 3.599 mil DKK. This is a decline of 3% compared to the revenue of 2007/08. Peak Performance, Soaked in Luxury, Saint Tropez, By Malene Birger and

Designers Remix Collection are expected to maintain a progression whereas Jackpot, InWear, Cottonfield and Tiger of Sweden are expected to decline.

We expect that the revenue will decline with respectively 3% and 2% in 2009/10 and 2010/2011. In 2011/12 we believe that the turnaround process will take place so that they can expect a growth of 1%. From that point we have estimated a growth rate of 3% until the last of the budget years. The reason for why we believe that IC Companys will experience fall in the first 3 years is that IC Company is in an unfavorable situation with financial crisis and high cost. But when we believe the turnaround process will take place we have estimated the growth to be just 3%. That's not high. There are some reasons for that. IC Company has so far not been able to adjust to the market conditions. The big question is whether IC Company will be better to adjust to the market conditions. In the announcement for 2009 they have higher priority on cost reduction than before. This may indicate a positive development in the future.

Nothing in the strategic analysis indicate that IC Companys is considering to acquire external brands. Their main focus has been and is still to keep concentrating on the existing brands. We have therefore not included any merger or acquisition of new brands in the budget period. We have though distinguished between different brands when budgeting. We believe that some brands will perform better than others. Even though IC Companys in 2008/09 states that the focus will be on existing brands, we expect them to develop new brands in the near future, why we are estimating a small grow in "other brands" from 2013/14 and to rest of the budget period.

We refer to appendix 1.10 for a closer examination of the revenue distribution for the different brands.

The development in the exchange rate

IC Company sells most of its brands in Scandinavia, North and Central Europe. Because a big part of the capacity cost is held in Euros it is limited how much one can hedge the risk. An unfavorable exchange rate development will affect the revenue and the result in a negative way. 01-01-2009 the EURO was 745,10 and on 04-09-09 it was 744,36 compared to 100 DKK. It is difficult to predict the development in the EURO throughout the budget period but we think that the exchange rate will not differ significantly and will not have an impact on the revenue throughout the budget period.

Gross result

We believe that IC Company will experience a decrease in the gross result. In the announcement IC Company states that the gross result has been 10% below last year. This is mainly due to the discounts. They have been necessitated to give greater discount on each of the segment which has resulted in a negative gross margin in each segment as well. We believe that even though the earnings have been affected negative it will be positive in the later part of the budget period. But with improving market conditions it will be less necessary to give great discount and the earnings will be improved.

Another reason for some optimism is that the announcement has stated that 16 shops has been closed that generated negative results. Further, 76 new stores has been developed where the main part is concessions. Of course IC Companys will miss the earnings from these shops but the end result would be positive due to their generation of loss. This is something that will have an impact on the earnings within a few years of the budget period. Earnings contributions percentages of 59% have been used in the budget period until 2012/13 and from then on we will budget the earnings contribution to 61% until the end of the budget period. We believe that IC Companys will already at an early stage reduce its cost and when the revenue will start growing it will achieve a greater earnings contribution.

If we say that IC Companys will not be able to meet the expectations both now and in the future we will calculate with a smaller margin of earnings. In 2008/09 the gross margin was 59%. We will use an estimate of 57% until 2012/13 and from then on 59% will be used.

Exchange rate fluctuations

IC Companys makes most of its purchased supplies in the east in USD or in USD related exchange rates. Because of that IC Companys would be sensitive towards an unfavorable development in the exchange rate that can affect the earning in a negative direction. USD has been through turbulent changes throughout a period of time. In march 2009 the USD was set at a price of 592,5 DKK / 100 but on September 7, 2009 it was down to 518 DKK/100. We do expect that USD will experience a rise in the price in the future and that is one of the reasons for why we have set the gross margin to 54% and not 55% in the start of the budgeting period. We anticipate IC Companys to monitor and manage these financial risks as they do now, by use of financial instruments. Thus there are limits to this.

Budget for the capacity cost

Capacity cost consist of employee cost, depreciation and other external cost such as marketing cost, administrative cost and rental of shops etc. We have divided the capacity cost into employee cost and other operating expenses. The reason is that IC Companys has not made a more detailed division of the capacity cost. In 2007/08 the employee cost counted for 24,9% of the revenue. In the annual report of 2008/09 the employee cost was calculated to 25,8% of the revenue. If we look at the historical values from the accounting period we would see that it basically has been increasing. In 2005/06 it was at 23,5% until it reached 24,9% in 2007/08. When the revenue increases we assume that IC Companys will invest in expansion of the retail shops which will result in an increase in staff cost. We believe that until 2012/13 the cost will be at the same level as in 2008/09. From then on the cost will be reduced a bit to 24,5%.

If we look at the other operating expenses they account for 25% of the revenue according to the annual report 2008/09 . This is an increase compared to 2007/08 where other operating expenses was 23,2%. These proportions have throughout the accounting period been fluctuating. Since 2005/06 the costs have been increasing, which continued in 2008/09. This is not a good sign. The annual report does not give us any information about which items have been placed under “other operating expenses”. But we believe that it must be the cost relating to marketing, sales and administrative cost.

Even though the costs have increased within the period of 2007/08 – 2008/09, IC Companys has had focus on minimizing the costs. The newly entered management has set an objective - a basis cost reduction of 200-250 mill DKK in 2008/09. This will be achieved by introducing organizational structural adjustment programs. One of these programs is, IC Companys has outsourced the refurbishment and interior design of stores. This has resulted in a dismissal of a lot of employees. So this is one of the reasons for the reduction in the cost. Furthermore IC Companys has decided to stop the sales activities in China.

During the accounting period IC Companys has been focusing on the company structure. This decentralization has among other things the aim to increase the pace of decision-making and hopefully result in an increased performance. On behalf of these actions and with the aim to reduce the cost as a high priority we will estimate the other operating expenses lower compared to previous years.

In the best case scenario we believe that IC Companys will be able to reduce its operating expenses such as sales, administration cost and employee cost. In the first 3 years of the budget period we will project with a share of 25% and from then on it will be set to a level of 23,5% because IC Companys would be able to adjust to the market and implement its strategies.

In the worst scenario we believe that the reduction in the other operating expenses will be less. In this case will the projected proportion be set to 25,8% meaning at the same level as it was set in the first 9 months of 2008/09. This has been based upon the hypothesis that IC Companys will not be able to reduce the cost more compared to the revenue. The same can be said about the staff cost. If the loss making retail shops are not closed, the fixed cost will be at the same level. These costs have been set to 25,8% until 2012/13 and from then on it will be set to 24% of the revenue.

Budgeting goodwill

If we look at the historical accounting period we would see that the only time IC Companys has included the amortization of goodwill was in 2003/04. From then on it has been almost equal to zero. The reason was that in 2003/04 IC Companys followed the Danish Share regulations but from 2004/05 it changed to IFRS where amortization of goodwill is not allowed but only an impairment test.

On behalf of that it is difficult for us to predict the impairment of goodwill. Another reason is that it can be said that the brands IC Companys have purchased so far, can be said to be successful purchases, especially the latest purchased brands as Tiger of Sweden, Peak Performance and Saint Tropez. Furthermore we believe that most of IC Companys brands have a long life-cycle.

For both the best case and worst case we will estimate the amortization of goodwill to zero.

Budget the transitory items.

In connection with the preparation of the accounting analysis we reformulated the published annual reports with the aim to identify the permanent profit. This was done by "cleaning" other operating profit from transitory items. Regarding the identification of the permanent profit that was done in section 4.7, we saw a great amount of transitory items. But you might recall that we mentioned that in the item "other operating expenses" there were included the sales and administration cost. This was the reason for the huge amount of transitory cost. Besides that, the transitory items consisted of some non-recurring items such as change of accounting policies, depreciation of goodwill and "special items".

Exchange rates regulation of foreign subsidiaries is also included in other operating profit. As it was the case of the revenue and the gross margin we believe it is difficult to estimate the development in the exchange rate and because of that we have decided not to include the revaluation of the subsidiaries in the budget.

In the annual report for 2008/09 IC Companys had 10,5 mill DKK included in the item "other gain and losses". Looking at the previous accounting years we can see that it has been fluctuating. But by taking the average of the historical accounting period we will estimate this item with a value of 10 mill. DKK. This will be the case for both the best case scenario and the worst case scenario.

IC Companys has not had any values recognized in "special items" since 2007 and up to the latest annual report 2008/09. Even though we believe that IC Companys would be necessitated to close some of it shops we will not budget any value in this item because it is difficult to predict.

We have furthermore not chosen to include any of the other transitory items such as change of accounting policies and amortization of goodwill because these cost are one-off cost that we believe will not be returning and concerning goodwill it is not possible anymore because of the regulation in IFRS.

Tax budget

In appendix 1.7.5 is the effective tax percentage calculated to be -9%, -15%, 34%, 23% and 30% for the year 2003/04, 2004/05, 2005/06, 2006/07 and 2007/08 respectively. Looking at these values we might be able to identify a pattern. The two first years IC Companys had a negative tax rate, which might be due to the turnaround process. Since then it has been fluctuating until it ended at 30%. The effective tax rate for 2008/09 is 28%. The level has been somewhere in between 23 and 34% since 2006, which might be explained by the fact that IC Companys is an international player where the effective tax rate is not only affected by the Danish corporate tax but also by other countries tax rates. Another reason might be the part of the unused tax relating loss that has not been recognized. Because calculation of the tax rate cannot be made in the budget period we will determine the tax rate to be 29%. As an alternative we might use the Danish corporate tax rate of 25% but looking at the three previous years and the tax rate for 2009 we see that it is about the 30%, therefore we have decided to set the tax rate to 29%.

Summary of budget the operating profit

As mentioned before when making budget we will usually take the realized values for the forthcoming annual report or announcement 2008/09 into account and we assume that the operating profit can be equated with the permanent profit that has been calculated in the accounting analysis. Though, there is one more thing we have to take into consideration and that is that IC Companys is a cyclical company.

If we look at the just realized annual report for 2008/09 we can see that IC Companys had a profit of 109,2 mill. DKK compared to 224 mill DKK in 2007/08. This decrease in profit is partly due to the economic downturn.

Budget the net operating assets

Net operating assets were in 2007/08 measured to a value of 1.118 mill DKK. The asset turnover has throughout the analytical period been increasing. In 2003/04 the asset turnover was 2,52 and ended in 2007/08 at 3,33. Though, in 2005/06 and 2006/07 the asset turnover slightly decreased. This was rather insignificant. We have calculated the average asset turnover to be 3,11.

We believe that IC Companys has been able to improve the asset turnover throughout the analytical period by reducing some of its cost, getting better sales prices and cutting of the discounts.

Looking at the operating assets for the whole analytical period we can see they have increased from 1292 mill DKK in 2003/04 to 1800 mill DKK in 2007/08. However, the revenue has been increasing as well from 2003/04 to 2007/08. The inventory has increased with approximately 200 mill DKK from the beginning to the end of the accounting period. This is an acceptable increase because increased revenue will result in increased inventory. Tangible fixed assets have increased from 176 to 424 mill DKK within the same period. This must again be looked at, with an increase in revenue and the need/opening of new stores, etc. Trade payable income has also increased from 235 to 314 mill DKK within the same period, which is a good sign to a certain extent.

IC Companys has not signaled any significant new investments or other major initiatives that may give any indication concerning change in the net operating assets. A change might occur if IC Companys purchased a new brand but no announcements in regards to this has been made. The revenue has furthermore been budget on behalf of organic growth. On behalf of the above we have decided to set the asset turnover to 3,10 throughout the whole budget period including the terminal period. We will not distinguish between best/worst case here.

Budget the share- based payment and options program

Throughout the recent years it has been more and more widespread in some line of business and some specific groups of employees to add share-based payment to the fixed salary with the main purpose to make the employee a part of the company in the long run.

One of the main reasons for introduction of share based payment is the motivation of staff, which will positively contribute to the efficiency in the company. The company’s overall goal must be aligned with the goals of the employees

The advantage of the employee is that the given options or warrants gives the employee a right but not an obligation to buy a specific amount of shares, either new or existing shares. The allotment price is always lower than the market price so it can be considered a bonus element to purchase these shares.

The bonus element will only by taxed the day the employee chooses to exercise the right of the option or warrant.

It is not irrelevant to look at this kind of payment of the employee from the already existing shareholders point of view, because these shareholders would suffer a depreciation of its shares because of the favorable price. The depreciation consists of the spread from the difference in the market price and the favorable price. This is also the spread that the employee will be taxed.

In most cases it is the leading employee who will be offered these kinds of bonus payments. This is also the case in IC Companys. By using the Black-Scholes model the share options and warrants consist of 2,3 mio DKK the 30 June 2008 according to the annual report for 2007/08.

In relation to the subsequent valuation we must take the present options program into consideration. Lately IC Companys has assigned 173.500 shares in 2009 in connection with an employee share emission. Looking at the annual report for 2007/08 we can see that stock options counted for 2 mill DKK and warrants counted for 0,1 mill DKK. This should be included in the valuation. But before we correct the equity for this amount we have to regulate for the tax credit IC Companys achieve for these options liabilities, which is 25% of the liability. The equity will therefore only be adjusted for the value of 1,58 mill DKK.

The size of these stock options programs is so insignificant that it will not have great impact in calculating the estimated stock price.

Budget the dividend

Since the merger of InWear and Carli Gry, IC companys has had a dividend policy which is to distribute 30% of the profit of the year. This policy will only come into force if IC Companys has the liquidity to implement the dividend policy and for new investments. IC Companys has not distributed dividend in 2008/09 even though they had a profit.

We will not estimate with any dividend in the first 5 years of the budget period but from then on we will estimate with a dividend of 30% of the profit also in the terminal period. This will be the case for both the best and worst case.

Budget the yearly depreciations

Since IC Companys transferred to IFRS they have had a special item in the annual report that is "depreciation". In this item is included the yearly depreciation of tangible and non tangible assets. If we look at the accounting period we can see that this item represents almost 3% of the revenue. Leasehold improvement and "equipment and furniture" represents almost 90% of this item. In the best case scenario we will estimate with 3% until 2012/13 and from then on we will estimate with 3,5%. The reason is that, in line with the revenue is growing then the assets will also grow and therefore we have estimated with a higher ratio. In the worst case scenario we will still use 3% until 2012/13 and from then on we will estimate with a ratio of 4%. This is if IC Companys won't be able to adjust the operating assets with the revenue.

5.3 Budgeting in the terminal period.

IC Companys will be valuated under the prerequisite that IC Companys is a going concern and therefore we should make an infinite budget. This is obvious impossible we have therefore as a starting point made a budget period of 10 years with varying revenues, EBIT margin and other value drivers. After this period of 10 years we expect a terminal period that is a steady state.

The terminal value is calculated from the terminal period and this shows the value that is added to the equity in the remaining life of the company after the budget period.

When to determine the terminal period and calculate the terminal value it can be done by one of these two assumptions:

1. Investments made after the budget period will generate a return. The market forces provide the return that has been generated to be exactly at the same level as the capital cost.

2. Investments made after the budget period will generate a return that is at a higher level than the capital cost. This profit is a result of the continuous growth in IC Companys cash flow.

Companies that generate a return that is at a higher level than the cost of capital will attract competitors and this return will be diluted until it ends at the same level as the cost of capital.

The strategic analysis shows that IC Companys is one of the largest providers of cloth in Northern Europe. Despite the fact that this line of business has a great amount of competition we still believe that IC Companys continuously will create growth regarding the growth potential in section 4.7. But we believe that the growth rate would be at a more moderate level compared to what has been stated in the investor meetings.

The key figures in budgeting the terminal period is the revenue growth and the earnings contribution in percentages. In the following sections we will estimate the different value drivers and justify them.

Revenue and earnings contribution

The growth in the revenue has been estimated to 2% for the best case scenario and approximately 1% for the bad case scenario. These growth rates are less than the growth rate in the budget period. Even though IC Companys are heading towards a time with falling rates we believe that they will maintain a growth rate in the future because of different strategic implementations. The earnings contribution has been set to 61% for the best case and 59% for the worst case scenario. These percentages are the same as the budget percentages in 2012/13. Because of the competition we think it would be difficult to have a higher earnings contribution. But still IC Companys has been able to reduce these costs throughout its lifetime by changing distributors, move production to countries with cheaper labour and they still are focusing toward minimizing the cost as one of the highest priorities in the announcement for 2008/09.

Capacity cost in the terminal period.

There is no doubt that IC Companys will go through a turnaround process in the coming time. From a historical perspective, through the period of 2004/05 – 2007/08, IC Companys has had good results in relation to revenue and profit. However, this development has recently gone in the wrong direction. We predict this negative development to continue within the next year or so. But in the future we again expect a turnaround process that will result in positive development. In the worst case scenario we have estimated the staff cost and sales administrations cost to 25% and 24% respectively. For the best case the staff cost and sales and administration 24,5% and 23,5%. These percentages are the same percentages that have been used in the budget period from 2012/13. We believe that IC Company will not be able to reduce these costs more than they already will do until 2012/13 and therefore we have estimated with a constant rate.

Tax in the terminal period

We have the expectation that there will not be any regulatory intervention or greater change regarding the corporate tax and therefore we will calculate with a corporate tax of 25% in the terminal period. In the section “budget the tax” you will find some comments regarding the international tax.

Dividend policy in the terminal period

As mentioned earlier we expect that IC Companys will distribute dividend to its shareholders in the later part of the budget period. We are convinced that IC Companys will be consolidated and will be able to pay dividend in the terminal period as well.

Net operating assets in the terminal period.

When estimating the net operating assets there is specially one thing that must be taken into consideration. That’s the amortization of goodwill. But as it has been mentioned above, IC Companys follows IFRS that does not allow amortizing the goodwill. Furthermore has IC Companys not proclaimed that it will acquire any new brands or similar but because the terminal period is relatively long we believe that the goodwill they have at this moment will last and therefore we have not decided to make any changes in the turnover for net operating assets from the budget period.

5.4 Valuation

In connection with the valuation of IC Companys we have chosen to use the residual income model and by using multiples. The essential part of the residual income model is the key figures and value drivers that was analyzed and identified in the profitability and the strategic analysis. For instance is Return on capital employed($ROCE_{noa}$) and net operating assets a part of the model.

To mention one of the residual income models weaknesses it can be said that it does not take the strategic opportunities into consideration that IC Companys has, which may affect the valuation of this company.

The residual income model for a going concern, which IC Companys is assumed to be, can be inferred by the following equation:

Figure 5.3 Residual income model

As it appears from the equation, the valuation is divided into two portions. Firstly we have to find the real earning which is the value of the net operating asset to time 0. In the second portion we have to discount the expected operational residual income to time t which is the present value of the residual income over the budget period.

Valuation by using the residual income model.

In appendix 1.10 you will find the prerequisites for budgeting the income statement, net operating assets and other value drivers which is used for the below mentioned valuation.

September 24, 2009 was the value of one IC Companys share 133 DKK. At this moment they had 16.9 million shares issued. This gives a market value of IC Companys shares to be 2253.4 million DKK. We have calculated a market value of IC Company to be 3599.4 million DKK and with the present amount of shares it give a solely share price of 233 DKK.

We can see from our calculation that there is a huge difference in between the market value of the equity from the Copenhagen Stock Exchange and the value we have calculated by using the above mentioned equation. But we have to remember that approximately 60% of this market value of 3599.4 million DKK consists of the discounted value of terminal period.

5.5 Sensitivity analysis of the discounted cash flow valuation

Forecasting the budget period from 2008/09 – 2018/19 and estimating the capital required rate of return has been made by using the financial analysis and the outcome of the strategic analysis. Therefore there are a lot of value drivers that have either a direct or an indirect effect in the valuation of IC Companys. Furthermore we have to recall what has already been mentioned earlier that IC Companys is considered as a cyclical company. This means we have to face other challenges as well. In the following sections we will start out with the complications that are related to valuating a cyclical company and thereafter we will discuss other value drivers.

There is different ways of valuating a cyclical company. The method we have used is by calculating the market value of IC Companys from a best case scenario and a worst case scenario and weigh them in regards to probability. In appendix 1.10 and 1.10.1 we have the best- and worst case budget. In giving these scenarios probabilities we had two major considerations. Due to this, it is decided to valuate IC Companys by giving the best case scenario a probability of 35% and the worst case scenario a probability of 65%. The first thought regarding the valuation has been how much a buyer would be willing to pay for IC Companys and how much a seller would expect to gain from a possible sale. The second thought is our expectations to the future growth.

We do not believe that is fair to valuate IC Companys by using the value drivers in a time where the development for the company is going in a negative direction. At the same it would also be misleading to estimate a market value of IC Companys by just making use of values that has been generated from an upwards going development. When to valuate the company one must take both the good and bad time into consideration.

Our estimation of IC Companys is that each share is more valuable than 133 DKK. Therefore this is not the price, which should be used. 233 DKK is a more appropriate price that would be acceptable for both the seller and buyer. Even though there will always be conflicts of interest between the buyer and seller.

Another reason why we have estimated the best case to 35% and worst case to 65% is our expectations to the future growth. We believe that IC Companys will manage to turn their performance in a positive direction. But our estimation is that it would be with a more moderate development in the future. The growth rate has been based on the information we got from the strategic analysis concerning the planned future implementations and the ability of the company to change this development. Further, the macro/micro economic factors are expected to improve, which will influence the growth rate of IC Companys in a positive direction.

In spite of some of the values have been conservatively estimated, there is some factors in the valuation that have been estimated on subjective and critical valuations. These factors will affect the valuation with separately weight and therefore should the valuation be complemented with a sensitivity analysis to identify how sensitive the valuation is towards these factors.

For instance we have estimated the risk-free rate under the assumption that we make an investment that has a long term and that the investment is risk-free. We have made use of a 10 yearly treasury bond with an effective rate of 3.87%. A growth in the interest level will result in a higher required rate of capital and "all other things equal" will result in a lower market value of IC Companys.

In the below mentioned matrix we have WACC at the horizontal axis and the growth rate in the vertical axis for the worst and best case scenarios. These are the factors that we think has a great impact in valuing the market value of IC Companys.

Figure 5.4

WACC	Revenue growth rates				
	0%/3%	0,5%/3,5%	1%/4%	1,5%/4,5%	2%/5%
7,1%	257	274	297	328	374
7,6%	232	245	261	283	313
8,1%	211	221	233	249	269
8,6%	194	201	210	222	237
9,1%	180	185	192	200	211

The figure above clearly shows how sensitive the market value of IC Companys is towards changes in its main parameters. This shows that the stock price is more sensitive towards a change in the WACC compared to a change in the growth rate. If the calculated WACC of 8,1% is decreased with half a percentage point it will result in an increased stock price of 28 point to 261. Whereas if only the growth rate will be changed from 1%/4% to 1,5%/4,5% the price will only increase by 16 point to 249 DKK. Furthermore this clearly indicates when the WACC is at a high level the change in the revenue has less effect on the market value of IC Companys. With a WACC of 8,1% and a growth rate of respectively of 1%/4% we have calculated the stock price to be 232,9 DKK. We believe that one should invest in IC Companys because the firm is undervalued.

The estimated value of 232,9 DKK partly prerequisites, that IC Company will be able to keep a growth rate of approximately 2% after the budget period. In the making of the budget and terminal period we have included the expected synergy effects and cost reductions in our deliberations, which hopefully will result in improved earning and profit margin. These factors are mainly based on the strategic analysis. Further, IC Companys is expected to continuously focusing on development and efficiency of the company. Their quarterly report also states a positive announcement and expectation to the future. All this supports our estimate of 232,9 DKK. Though, there is always some form of uncertainty in relation to this scenario.

Finally it has to be said that the above mentioned valuation has been made basically by discounting the residual income where the terminal period consists of about 60% of the residual income.

We have valuated the growth and the ability to adjust to the cost as the most essential elements of IC Companys. As mentioned, the valuated share price is set to 233 DKK. Further, we don't believe that IC Companys would have a growth below 2% in the future.

Areas to be focused on for the management:

- The management must perform and make sure of growth in the revenue.
- The cost must be adjusted
- More detailed strategic and economic budgets must be made.

To control the credibility of the residual income model valuation we have calculated the value of IC Companys by using the discounted cash flow model, which is stated in appendix 1.10 and 1.10.1. The free cash flow model is one of the most detailed models used for valuation. Budgeting the operating profit prerequisites a thorough knowledge of IC Companys. By using the estimated forthcoming cash flows we will be able to avoid those implications that occur only by using the annual statement such as problems concerning recognition- and measuring-criteria.

5.6 IC Companys - by using multiples

In practical life most of valuation is made by using multiples. Price Earning ratio (P/E) is an example of a multiple. The key figures is always possible to find at the price list for instance in Børsen. The P/E is calculated by measuring the stock price relative to the annual net income or profit by the firm per share. P/E ratio means how much an investor is willing to pay for each unit of net income. When making comment on the P/E one should compare the P/E for a particular company with other companies that operate in the same line of business.

We have made a comparison between IC Companys P/E and H&M and not Bestseller due to lack of information.

Accounting period	30.06.04	30.06.05	30.06.06	30.06.07	30.06.08	Terminal period
Market value	780	5.005	6.424	5.764	2.717	3398.4
Price	42,5	275	344,5	318	156	200
Number of shares	18.351.650	18.201.623	18.648.400	18.126.800	17.415.800	16.942.807
Realized result	-308,8	203	224,4	240,6	224	170,2
PE value, IC Companys	-2,53	24,7	28,6	24	12,1	20,0
PE value, H&M	21,8	19,7	25,3	24,3	17,3	-

Table 5.1

As it appears from table 5.1 we can see that the P/E-ratio for IC Companys has been varying a lot. The P/E ratio has been at a more constant level in the financial years 2005-2007 compared to the accounting year of 2004 and 2008. The main reason for this is that IC Companys had a loss in 2004 whereas they achieved profits in the three following years. Futhermore IC Companys experienced a decreased result and stock price. However comparing the P/E for IC Companys with H&M we see that in the year 2004, 2007 and 2008 the P/E has been at a lower rate than H&M. in 2005 and 2006 it has been at a higher level. Based on our calculation the overall picture shows that IC Companys has been underestimated. IC Company can make use of this in the future. If they fulfill the requirements demanded by the market in the future they can achieve a higher P/E.

5.7 Rate triggers - what can increase the price.

- An increased information flow would be a factor that could lead to a higher price. If IC Companys presents a more structured information flow where they present the forthcoming strategy plans, which brands, markets and collections they will be focusing on in the future and is considered as a part of the long-term strategy. All of this are some factors that analyst will make use of in the valuation of the company because these factors are essential for IC Companys survival. Presentation of positive actions will lead to positive activity concerning the price.

- A successful turn-around process will also lead to a higher positive activity regarding the price. If IC Companys will be able to adapt to the environment by living up to its expectation by reducing the cost and be able to turn the negative growth rate to a positive growth rate it will lead to a higher price. It is also important that the management of IC Companys will be able to keep the level of trustworthiness in the forthcoming years in order to maintain the high price level by producing positive announcements.
- Purchase of shares from hedging or investment funds. IC Companys is a cyclical corporation, and the future development of the economy and the firm is expected to go in a positive direction, which could make it an interesting investment opportunity. This will make the price increase.

Though, investment funds can be deterred to invest in IC Companys and acquire shares due to below-mentioned cause.

1. Niels Martinsen possesses 40% of the shares in IC Companys which makes it very obvious that he has a lot to say and therefore has an impact on the price of the share. He would like to demand a price that might be favorable from his point of view but might be a high price for the investment fund.

If the investment funds have similar perception of our estimate of the share in relation to the actual market price, this could trigger an investment in IC Companys, which again would lead to an increased share price.

- Positive macro/micro-economic developments and forecasts can increase the price.

5.8 What can make the price fall.

- Negative macro/micro-economic developments and forecasts can decrease the price

- An unsuccessful turnaround process. There is a risk for an unsuccessful turnaround process. If IC Companys does not live up to the expectation to its future growth and strategies the result might be that the investors will lose trust in the management and it will be reflected in a declining price.

- The fashion. One of the major factors that will lead to a declining revenue/sale is the fashion. If IC Companys designer team fails to live up to the fashionable trend for the coming year it will lead to a falling stock price.

- Lawsuits. A lawsuit against IC Companys will truly have a negative effect on the stock price due to negative publicity.

6. Conclusion

IC Companys A/S is a Danish fashion corporation, which produces 11 designer labels, which are exported to more than 40 countries all over the world. The clothing industry, in which it operates, comprises many companies/suppliers. IC Companys is present in the mid and high-end price segment and has different competitors within these. The main part of their brands is marketed in the mid-price segment, which is particularly competitive. Though this segment is generally fragmented and no brands have a dominant position. This means there is a great potential in this segment, which IC Companys intends to focus on and strengthen their position within this. Every brand in their portfolio has a unique profile and is therefore competing with different brands in the market. All their brands are coherent with their portfolio and thereby make a significant strategic parameter. Due to the fierce competition in the market, it is essential to have a strong focus on brand profiling and brand positioning, which are to create brand loyalty. The Multibrand strategy of IC Companys is specifically to improve the brand identity towards the consumers. Additionally, the development of fashion is carefully monitored to meet the requirements of the consumers. IC Companys decision to operate with a portfolio of diverse brands for different price-segments will contribute to meet various customer preferences and possibly minimize loss in sales caused by an economic downturn. This provides IC Companys with a competitive advantage.

In several years, IC Companys has sold or closed down many loss-making stores to minimize costs and create value for the company. Increased focus has been directed towards the development of their existing brands. Presently, they have no intentions to diminish or increase the product portfolio. It could be argued, that a strategy to acquire or develop products for the low-end price segment is worth considering - would possibly contribute to sales both during a state of growth and recession in the economy.

The strategic internal analysis indicates the core competencies of IC Companys. The production is outsourced to cost-efficient countries and no supplier represents more than 4% of the total production value in order to diminish the dependency and bargaining power of each supplier and minimize the commercial risk. Since clothing collections change a minimum of 4 times a year and have a long lead time, there is a risk that the products will not match the customer preferences (fashion trends) when released in the market. IC Companys has taken some precautions in regards to this, by integrating the OTB-setup (Open To Buy – seasonal sale of clothing with a short delivery time). Activities in regards to the refurbishment of stores have been outsourced to increase execution-ability, flexibility and to diminish costs of opening new stores.

Through IC Academy, the employees and managers of the organization is trained, educated and given the right qualifications for their employment to help drive the organization forward, make the company more efficient and in the end provide better services to the customer. Efforts have been put in corporate social responsibility activities, IC Companys "Code of Conduct", to create a positive image of the company and hopefully influence the perception of the customers in a positive direction towards buying their clothes.

If their clothes are not sold through the Retail department, IC Companys has Factory Outlets for the continuous sale of such. Products, which can not be sold through the Factory Outlets are sold to brokers for resale outside established markets. All this contributes to the total revenue of the company. The Group's brands are sold by a total of 12.000 selling points, but no customer accounts for more than 5% of the Group Wholesale revenue. The impact of losing a customer will be relatively limited. A new model of cooperation for the Wholesale department is being implemented. In addition to secure an effective/efficient sale, the new model of cooperation will lower the amount of capital tied up for Wholesalers as well as for IC Companys.

IC Companys has a rather decentralized organizational structure to ease and increase the pace of decision-making in the different departments. Combined with the Multi-brand strategy it creates synergies within the shared business functions/platforms and minimizes costs.

The strategic external analysis shows how external factors can influence IC Companys ability to create value in the future. IC Companys can be rather exposed to both price increases and regulatory amendments in China, where approximately 60% of production is taking place.

85% of IC Companys total revenue is generated in Europe and 44% in Denmark and Sweden, which means that they are rather dependent on the sale within these regions. The company is affected by macro-economic fluctuations as is the rest of the clothing industry. Despite the negative market conditions the last years, IC Companys is convinced that, the gains of making the company more efficient combined with the right clothing-collections will exceed the macroeconomic tendencies. The development in revenue in 3rd quarter 2008/09 within the separate brands were neither to be explained by price nor fashion-degree. IC Companys believes that, the possibilities of creating growth irrespective price-segment are completely present despite the disadvantageous economic conditions. The macro-economic forecast seems positive in the years to come, which can contribute to an increased sales-level of IC Companys and the clothing industry in general.

The international trade makes the company exposed to currency fluctuations/risk. The Group monitors and manages all its financial risk by the use of financial instruments, thus there are limits to this.

Socio-cultural factors such as fashion trends, taste, price and buying behaviour changes incrementally. IC Companys is aware of this and has focus on adapting to these changes through their Multi-brand strategy. On a continuous basis, the focus is on innovation and development of their brands.

Their internet-based Business-to-Business “distribution/sales channel” for their Wholesale market in EU eases the access to manufacturers’ inventories and leads to a more rapid response-time for changes in demand of the consumer. E-trade/commerce has increased the last couple of years. To follow the development, be competitive and increase sales, IC Companys has engaged in a co-operation with one of the world’s leading e-commerce partners, GSI Commerce Inc. Within 18 months the total product portfolio is to be acquired online.

IC Companys has their products manufactured, primarily in China and Eastern Europe. In addition to the cost-efficiencies, the technological development within the manufacturing of clothing in these countries will improve the quality of IC Companys products and in the end assist in offering a better product.

The threat of new firms entering the clothing industry is present. To prevent from disappearing in the highly competitive market it is essential to create a differentiated brand or trademark. IC Companys has through the Multi-brand strategy focus on this realm and is trying to establish brand awareness, brand identity and in the end customer loyalty. Marketing and other sales-supportive efforts have been increased to support this strategy. It will also become more difficult for the Wholesale distribution points to substitute a differentiated brand/trademark as IC Companys with brands of competitors. The bargaining power of the buyers (Wholesale) will be diminished.

IC Companys overall goal is to achieve a yearly organic growth of minimum 15% and an EBIT-margin of minimum 15% in a 3-5 years time-horizon. The growth objective is divided between the different distribution channels. Franchise is expected to grow relatively strong and the growth potential in Retail is to be utilized. Sales through Outlet Factories is anticipated to be modest due to an improved purchasing- and inventory management. Efforts will be focused on OTB sales and in regards to pre-order sales; this is expected to have a lower growth compared to OTB sales.

The growth potential of IC Companies is present. They export to more than 40 countries. Though, it is only in 8 of their largest markets where all of their brands have been introduced. Here they already have the market experience, hence a great potential in gaining market share. Focus is directed towards this to grow and increase sales.

An overall evaluation of IC Companys accounting policies has been made, which indicates that IC Companys mainly has followed IFRS (International Financing Reporting Standards) and to some extent the Danish Financial Statements Act. It can thereby be concluded that the accounting material completely fulfill the requirements of comprehensiveness, relevance, reliability and comparability. Though, it has been necessary to make some corrections to the published annual reports for the purpose of analysis.

A reformulation and a reclassification of IC Companys balance sheet, movements in equity, income statement and cash flow statement have been made in order to be able to make an individual analysis on operating and financial activities respectively, comprehensive income, permanent profit, etc.

As an introduction to the profitability, IC Companys activity was examined, by looking at the revenue. The growth objective, which was set in 2001, was not reached until 2005. A new target was set in 2006 and has not yet been reached. Even though their growth objective has not been reached, they have still managed to increase the revenue. However, IC Companys is not expected to reach its goals within the near future.

The profitability has mainly been explained by looking at ROE. IC Companys has managed to turn a negative ROE into a positive two value figure. Since 2004/05 the ROE has been kept at an overall positive satisfying level. The ROE has been decomposed, which showed that $ROCE_{noa}$ was the primarily cause to the fluctuations in the ROE. The development in ROCE has been similar to the development in ROE. ROCE was negative in 2004 and turned positive in the following years, which was the same for ROE.

Furthermore, $ROCE_{noa}$ has been decomposed into its underlying drivers, PM and AT. This decomposing has shown that the main reason for the fluctuations in ROCE is caused by the profit margin (PM). IC Companys has had some problems to adjust the cost and income. Their profit margin was transformed into positive figures from 2004 until 2008 and was at a satisfactory level. But in the time of recession in the economy, the fixed cost might be a problem. On the other hand, AT has been at a constant level that means IC Companys has been good in distributing the capital.

The decomposing of PM has shown that fixed costs have been fluctuating, but IC Companys has been able to reduce some of them. In the end of the analytical period IC Companys had rising fixed costs as the revenue also has been rising. Though, they have to improve the adjustment of fixed costs to become more competitive. A further decomposing of the profit margin has been made, where the transitory items have been separated from the core profit. This has shown that the transitory items are contributory to the lowering of PM. Looking at the financial ratios one will see significant differences in the PM, where transitory items have been included in comparison to where transitory items have been excluded. However, sales and administrations costs have not been included in the core PM due to lack of information. Especially 2004 have been affected by the transitory items. A negative PM of 8% has been converted into a positive 15% core PM. The remaining accounting years have experienced a positive rise of 13% in average as well.

We have evaluated the operating and financial risk of IC Companys. The operating risk has mainly been increasing throughout the analytical period. With the growing revenue borne in mind, the risk is evaluated as an average level. The costs have also been growing, but will not affect them negatively at this particular moment.

The financial leverage has also mainly been increasing throughout the accounting period. The financial leverage contributed to a negative result to ROE because of a negative SPREAD in 2004. The following years a positive SPREAD was achieved and contributed positively to ROE. The financial

risk has remained at a high middle level. The overall operating and financial risk of IC Companys can be estimated to an average level.
Some uncertainty can be related to the future risk. Is it going to increase or decrease? The development in the operating risk will be affected by IC Companys ability to complete the turn-around process. With a forecasted falling growth rate in 2009/10, IC Companys has to reorganize rapidly to, among other things, minimize their fixed costs.
The development in the growth rate of funds generated from operations has been identical with the development in ROE for the first three financial years, because dividend was not paid. If the growth rate of funds generated from operations is corrected for transitory items a significant change in the growing rate appears. A 100 % rate will be attained in the first financial year and exceed 100 % in the following years. It has to be pointed out that, sales and administration costs have not been included, which explains the high growth rate. However, this still indicates that IC Companys has to improve the ROCE to a level that is higher than the borrowing rate, which will increase the growth rate of funds generated from operations.
Due to lack of information concerning the acquisitions, made in 2005/06, we have not been able to identify the size of interest bearing debt this has lead to. A comparison between the FCF and the realized results is therefore not possible.

IC Companys has basically been valuated by using the residual income model and by using multiples, which has been benchmarked with Hennes & Mauritz.

We have chosen the residual income model as we believe is the most suitable to valuate IC Companys. This model is comprehensive in investment theory and many of the main financial ratios have already been described in the financial analysis. The residual income model furthermore has an ex-ante approach.

A best case and worst case scenario have been added to the residual income model. This has been made because IC Companys is a cyclical company. For this we have distributed a probability of 65% for the worst case scenario and a probability of 35% for the best case scenario to valuate IC Companys.

The residual income model consists of a 10-yearly budget period followed by a terminal period. In the budget period we have included all the information gathered from the strategic analysis, financial analysis and the information given in the announcement for the forthcoming financial year 2008/09. We have made a very detailed budget for the revenue by going into depth with the sole brand and looked at its potential from the information given and what our expectation is. The cost has furthermore been divided into different items such as staff costs and sale & administration costs. It has not been possible to make a further division of the sales & administration cost because lack of information.

Initially, the shareholders rate of return has been calculated, which is an essential parameter in the residual income model. Shareholders rate of return has been estimated by using the CAPM-model and calculated to 10,54%. The cost of capital for debt on the other hand has been estimated to 5,9%. Using these values with their respectively weighted capital structure we get a WACC of 8,1%.

With the information above we have calculated a theoretical price of IC Companys. Some of its main uncertainties is the estimated growth rate in the terminal period of 1,5% and 4% and the probabilities of 65% and 35% that has been used for the worst-and best case scenario. Other factors have been estimated with reasonable assurance. We believe that these growth rates are very realistic. IC Companys has a vision to achieve a growth rate of 15%. We are of that thought this might be optimistic. Even though the downturn in the economy and clothing industry might be temporary, the growth rate of 15% is set to high. Due to our analysis and information gathered, we find it unrealistic to attain a growth rate of 15%.

The valuation is followed by a sensitivity analysis. This sensitivity analysis has been focusing on two sensitivity parameters, WACC and the growth rate. This analysis has shown that the valuation is more sensitive towards the change in WACC than change in the revenue.

We have primarily based the valuation of IC Companys on the residual income model. This has resulted in a theoretical price of one IC Company share of 232,9 DKK with a market value of 3,599 billion DKK.

This price of 232,9 DKK is much higher than the published stock price September 24th, 2009 of 133 DKK. An estimated share price of 232,9 DKK must be viewed with some reservations. When valuating, prerequisites is made, which are based upon our own subjective views specifically in the operating budget and the terminal period. The sensitivity analysis also indicates a value of IC Companys somewhere in between 180 DKK and 374 DKK depending on the growth rate and WACC.

The price of IC Companys is under-valued. We recommend investing in this share due to the difference between the actual market price and our calculated price.

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