

2.2. Fixed Costs

McPhee Distillers has fixed costs that are slightly higher in the first year due to the incorporation, which carries a Marketing expense for \$50,000 for the creating of the corporate branding and logo.

Next to this extraordinary expense, the Distillery has eight different expense categories that we need to analyze separately.

2.2.1. Advertising & Promotion

In 2015, the company sold 150 barrels on the general market, and one year later, only 100. Elsa clearly states that the regular sales in the first year were below expectations. This puts an even more dramatic light on the further decrease in sales in 2016.

While we know that there is significant demand in the market, McPhee's Advertising & Promotion efforts do not seem to show success when it comes to materializing in actual sales revenue. As McPhee is still a very young company, it needs Marketing exposure to build brand reputation and to appeal to potential customers.

Advertising and Promotion costs should not be cut. They should be further increased. However, McPhee Distillers needs to tailor-make their marketing collateral around the purpose of the company and clearly state the claim to increase sales and efficiency of the Advertising & Promotion expenses.

2.2.2. Lease

McPhee Distillery has signed a 5-year contract for a disused shipyard for \$5,000 per month. The contract runs from January 1, 2015 until the end of 2019. It is

It is also important to calculate the actual cost of the equipment during the lifetime to compare it with alternative investments. Given the initial purchase price of \$500,000, the expected lifetime of 10 years, and annual expenses for Repairs and Maintenance of \$75,000, McPhee will have spent €1,250,000 on the equipment after ten years.

If McPhee was to take out a loan for the purchase of new equipment, with a longer expected lifetime and fewer expenses on Repairs & Maintenance, it would be more effective.

Considering an investment of new equipment for \$1m, Elsa could sell the current used equipment for the market value of \$400,000. This would leave her with a loan of \$600,000, and Repairs & Maintenance costs reducing significantly. Elsa should invest in new equipment and sell the current set-up. This would enable her to decrease the expenses for repairs & maintenance significantly. It will also enable her to scale up production in the future.

2.2.6. *Supplies / Utilities*

These expenses can be analyzed together.

McPhee claims that the quality of their product is their distinguishing factor. Therefore the costs for supplies and utilities are high due to the strict production process. Once these expenses are reduced, the product quality and company positioning is challenged significantly. This should be avoided. Supplies and Utilities should not be reduced.

2.2.7. *Warehousing*

The significant expenses for Warehousing are because McPhee is holding inventory that is not sold and that the finished and sold barrels are stored for 12