PAPER – 15 - BUSINESS STRATEGY & STRATEGIC COST MANAGEMENT

The following table lists the learning objectives and the verbs that appear in the syllabus learning aims and examination questions:

	Learning objectives	Verbs used	Definition
LEVEL C	KNOWLEDGE What you are expected to know	List	Make a list of
		State	Express, fully or clearly, the details/facts
		Define	Give the exact meaning of
	COMPREHENSION What you are expected to understand	Describe	Communicate the key features of
		Distinguish	Highlight the differences between
		Explain	Make clear or intelligible/ state the meaning or purpose of
		Identity	Recognize, establish or select after consideration
		Illustrate	Use an example to describe or explain something
	APPLICATION How you are expected to apply your knowledge	Apply	Put to practical use
		Calculate	Ascertain or reckon mathematically
		Demonstrate	Prove with certainty or exhibit by practical means
		Prepare	Make or get ready for use
		Reconcile	Make or prove consistent/ compatible
		Solve	Find an answer to
		Tabulate	Arrange in a table
	ANALYSIS How you are expected to analyse the detail of what you have learned	Analyse	Examine in detail the structure of
		Categorise	Place into a defined class or division
		Compare and contrast	Show the similarities and/or differences between
		Construct	Build up or compile
		Prioritise	Place in order of priority or sequence for action
		Produce	Create or bring into existence
	SYNTHESIS How you are expected to utilize the information gathered to reach an optimum conclusion by a process of reasoning	Discuss	Examine in detail by argument
		Interpret	Translate into intelligible or familiar terms
		Decide	To solve or conclude
	EVALUATION How you are expected to use your learning to evaluate, make decisions or recommendations	Advise	Counsel, inform or notify
		Evaluate	Appraise or asses the value of
		Recommend	Propose a course of action

Paper 15 - Business Strategy and Strategic Cost Management

This paper contains 4 questions. All questions are compulsory, subject to instruction provided against each questions. All workings must form part of your answer. Assumptions, if any, must be clearly indicated.

Full Marks: 100   **Time allowed: 3 hours**

1. **Read the case and answer the following questions**

In 2006-07 PTC Food division decided to enter the fast growing (20-30% annually) snacks segment, an altogether new to it. It had only one national competitor-Trepsico's Trito. After a year its wafer snack brand Ringo, fetched 20% market share across the country. Ringo's introduction coincided with the cricket world cup. The wafer snacks market is estimated to be around ₹ 250 crores.

The company could take the advantage of its existing-distribution network and also source potatoes from farmers easily. Before the PTC could enter the market a cross-functional team made a customer survey through a marketing research group in 14 cities of the country to know about the snacks eating habits of people. The result showed that the customers within the age-group of 15-24 years were the most promising for the product as they were quite enthusiastic about experimenting new snack taste. The company reported to its chefs and the chefs came out with 16 flavours with varying tastes suiting to the target age-group.

The company decided to target the youngsters as primary target on the assumption that once they are lured in, it was easier to reach the whole family.

Advertising in this category was extremely crowded. Every week two-three local products in new names were launched, sometimes with similar names. To break through this clutter the company decided to bank upon humour appeal.

The Industry sources reveal that PTC spent about ₹ 50 crores on advertisement and used all possible media print and electronic, both including the creation of its own website, Ringoringoyoungo.com with offers of online games, contests etc. Mobile phone tone downloading was also planned which proved very effective among teenagers. The site was advertised on all dotcom networks. Em TV, Shine TV, Bee TV and other important channels were also used for its advertisement along with FM radio channels in about 60 cities with large hoardings at strategic places.

Analysts believes that Ringo's success story owes a lot to PTC's widespread distribution channels and aggressive advertisements. Humour appeal was a big success. The 'Ringo' was made visible by painting the Railway bogies passing across the States. It has also been successful to induce Lovely Brothers' Future Group to replace Trito in their Big-Bazaar and chain of food Bazaars. PTC is paying 4% higher margin than Trepsico to Future group and other retailers.

Ringo to giving Trepsico a run for its money. Trito's share has already been reduced considerably. Retail tie-ups, regional flavours, regional humour appeals have helped PTC. But PTC still wants a bigger share in the market and in foreign markets also, if possible.

Answer the following questions:
a) What is SWOT Analysis?
b) What is the strength of PTC?
c) What are the weaknesses of PTC for entering into the branded snacks market?
d) What kind of marketing strategy was formulated and implemented for Ringo?

(4+6+6+4=20)

2. **Answer any two questions from (a), (b) and (c):** **[2 x 15 =30]**

(a) (i) What are the various steps required in contingency Planning? [7]

(ii) "Industry is a composite of competitive pressure in five area of the overall market". Explain briefly the competitive pressure. [6]

(iii) Distinguish between objectives and goals. [2]

(b) (i) Briefly Explain the effects of politics on organisation and employees. [7]

(ii) 'B' in BCG Matrix stands for Balance. Comment. [8]

(c) (i) What are the procedures followed for evaluating the decision for mergers and acquisitions? [4]

(ii) Discuss different types of Strategy alliance. [7]

(iii) "Profit may not be a universal objective, but business efficiency is definitely an objective common to all business" Comment. [4]

3. **Read the case and answer the following questions**

Polaris, a company engaged in Decision Support System (DSS) is examining the profitability and pricing policies of three of its recent engineering software packages:
• EE-46: package for electrical engineers
• ME-83: package for mechanical engineers
• IE-17: package for industrial engineers
Summary details on each package over their two-year "infancy-to-grave" product lives are as follows:

		Number of Units Sold	
Package	Selling Price	Year I	Year 2
EE-46	₹ 2,500	2,000	8,000
ME-83	3,000	2,000	3,000
IE-17	2,000	5,000	3,000

Assume that no inventory remains on hand at the end of Year 2.
Polaris is deciding which product lines to emphasize. In the past two years, profitability has been mediocre. Polaris is particularly concerned with the increase in R&D costs. An analyst pointed out that for one of its most recent packages (IE-17), major efforts had been made to reduce R&D costs.

Praveen, the engineering software manager, decides to collect the following life-cycle revenue and cost information for the EE-46, ME-83, and IE-17 packages:

	EE-46		ME-83		IE-17	
	Year 1	Year 2	Year 1	Year 2	Year 1	Year 2

Revenues (₹ 000s)	₹ 5,000	₹ 20,000	₹ 6,000	₹ 9,000	₹ 10,000	₹ 6,000
Costs (₹ 000s)						
R&D	7,000	0	4,500	0	2,400	0
Design of product	1,850	150	1,100	100	800	160
Manufacturing	750	2,250	1,050	1,050	1,430	650
Marketing	1,400	3,600	1,200	1,500	2,400	2,080
Distribution	150	600	240	360	600	360
Customer service	500	3,250	450	1,050	2,200	3,880

Required:

(i) How does a product life-cycle income statement differ from a conventional income statement? What are the benefits of using a product life-cycle reporting format?

[2+3]

(ii) Present a product life-cycle income statement for each software package. Which package is the most profitable and which is the least profitable? Ignore the time value of money. [3+1+1]

(iii) How do the three software packages differ in their cost structure (the percentage of total costs in each cost category)? [6]

(iv) State what do you mean by the term 'Life Cycle Costing' (LCC)? Write a few lines regarding LCC. [4]

4. Answer any two questions from (a), (b) and (c): [2 x 15 =30]

4(a) (i) ABC Limited uses a small casting in one of its finished products. The castings are purchased from a foundry. ABC Limited purchases 54,000 casting per year at a cost of ₹800 per casting.

The castings are used evenly throughout the year in production process on a 360 day per year basis. The company estimates that it costs ₹9,000 to place a single purchase order and about ₹300 to carry one casting in inventory for a year. The carrying costs result from the need to keep the castings in carefully controlled temperature and humidity conditions, and from the high cost of insurance.

Delivery from the foundry generally takes 6 days, but it can take as much as 10 days. The days of delivery time and percentage of their occurrence are shown in the following table-

Delivery Time (days)	6	7	8	9	10
Percentage of occurrence	75	10	5	5	5

  I. Compute the Economic Order Quantity. [1 ½]

  II. Assume that the company is willing to take a 15% risk of being out of a stock. What would be the safety stock and the Re-Order point? [3]

  III. Assume that the company is willing to take a 5% risk of being out of stock. What would be the safety stock and Re-Order point? [3]

  IV. Refer to the original data. Assume that using process re-engineering the company reduces its cost of placing a purchase of order to only ₹600. In addition, the company estimates that when the waste and in efficiency caused by inventories are

considered, the true cost of carrying a unit in stock is ₹720 per year. (a) Compute new EOQ and (b) How frequently would the company be placing an order, as compared to the old purchasing policy?   [1 ½ +2]

4(a) (ii) Quality Cost but poor Quality cost more. Discuss   [4]

4. (b)(i) An automobile production line turns out about 100 cars a day, but deviations occur owing to many causes. The production is more accurately described by the probability distribution given below:

Production per day	Probability	Production per day	Probability
95	0.03	101	0.15
96	0.05	102	0.10
97	0.07	103	0.07
98	0.10	104	0.05
99	0.15	105	0.03
100	0.20	Total	1.00

Finished cars are transported across the day, at the end of the each day; by ferry has space for only 101 cars.

Required:
(i) What will be the average number of cars waiting to be shipped?

(ii) What will be the average area of empty space on the boat?

The fifteen random numbers are given: 20, 63, 46, 16, 45, 41, 44, 66, 87, 26, 78, 40, 29, 92, & 21   [8]

4. (b)(ii) Heavens Ltd. has three divisions: Sun, Moon and Star. It also deals with two other outside companies: Mercury and Neptune.

Sun can buy a component from Moon or from Mercury, which will meet Moon's market price of ₹200 per unit. If Sun buys from Mercury, Mercury in turn will buy a component from Star for ₹40 per unit. The outlay costs to Star of supply this component are ₹20 per unit. In filling Sun's order, Moon would incur outlay costs of ₹165 per unit.

Assume that Moon is working at full capacity and can provide the component to Neptune at the same market price of ₹200 per unit and with the same outlay costs of ₹165 per unit.

I.   What alternative would be best for Heavens as a whole — Sun buying from Mercury or Moon? Show supporting calculations.   [4]

II. What Transfer Price should be used to guide the managers of Sun and Moon so as to maximize overall Company net inflow (cash inflow)?   [1]

III. Suppose that Moon has sufficient extra capacity to supply the component to both Sun and Neptune at the same time. How would this change your answers in parts (a) and (b) above? Show supporting calculations.   [2]

4. (c) (i) A Methods Engineer wants to assign four new methods to three work centres. The assignment of the new methods will increase production, details of which are given below. Determine the optimal assignment, if only one method can be assigned to each work centre.

Methods	Increase in production (units) in work centres		
	A	B	C
1	10	7	8
2	8	9	7
3	7	12	6
4	10	10	8

[8]

4. (c) (ii) A Company prepared the following budget for a year —

Item	Materials	Labour	Variable factory OH	Fixed Factory OH	Variable Selling OH	Fixed Selling OH	Profit	Sales Price
Percent	40%	20%	10%	10%	5%	12%	3%	100%

After evaluating the half-yearly performance, it was observed that the Company would be able to achieve only 80% of the original budgeted sales. The revised budgeted sales as envisaged above was estimated at ₹1,080 Lakhs after taking into account a reduction in the selling price by 10%. Prepare a statement showing the break-up of the original and revised budget for the year. [4]

4. (c) (iii) List any three common errors committed in drawing network diagrams. [3]