Paper- 13: MANAGEMENT ACCOUNTING – STRATEGIC MANAGEMENT

Time Allowed: 3 Hours **Full Marks: 100**

The figures in the margin on the right side indicate full marks.
Answer Question No.1 and any other two more from the rest in this section.
(Please answer all part of the question at one place.)

Section -I (60 Marks)
(Strategic Management)

Question 1.

(a) In each of the cases/ statements given below, one of four alternatives is most appropriate. Indicate the correct answer: [1×10]

(i) For Cash Cow BCG Matrix analysis following is correct
(A) High market growth and high market share
(B) Low market growth and high market share
(C) High market growth and low market share
(D) Low market growth and low market share

(ii) Delphi Technique is used in
(A) Budgeting
(B) Projecting business
(C) Market Research Technique
(D) Technology Forecasting

(iii) World retailer Wal-Mart's entry into Indian market through Bharti Enterprises is an example of
(A) Merger
(B) Acquisition
(C) Joint venture
(D) Amalgamation

(iv) "Marketing mix" is a general phrase used to describe the different kinds of choices organizations have to make in the whole process of bringing a product or service to market. The 4Ps is one way—probably the best-known way—of defining the marketing mix, and was first expressed in 1960 by
(A) Boom and Bitner
(B) Lauterborn
(C) Borden
(D) McCarthy

(v) If suppliers are unreliable or too costly, which of the following strategies may be appropriate?
(A) Horizontal integration
(B) Backward integration
(C) Market penetration
(D) Forward integration.

(vi) BSNLs plan behind introduction of "Internet Plan 99", ISDN Virtual Private Network etc would be an example of:
(A) Utilization of newer technologies
(B) Portfolio generation
(C) Diversification of business
(D) Product development

(vii) SAIL's famous advertising campaign of "there is a bit of steel in everyone's life was meant to:
(A) Gain buyers awareness about its versatile product range
(B) Create an image of superior performance
(C) Inform new buyers about its special products
(D) Enhance product quality perception

(viii) Which one of the following is not a measure related to BSC?
(A) Financial
(B) Customer Satisfaction
(C) Innovation
(D) Gap Analysis

(ix) You engage a call taxi by dial-a taxi facility. This is an example of
(A) One Level marketing channel
(B) Zero Level marketing channel
(C) No marketing channel
(D) Two Level marketing channel

(x) The sale of tea through one-cup tea bag is an example of the following distinctive capability:
(A) Distribution
(B) Innovation
(C) Sales and marketing
(D) New services

Answer:

(i) (B) Low market growth and high market share
(ii) (D) Technology Forecasting
(iii) (C) Joint venture
(iv) (D) Mc Carthy
(v) (A)Horizontal integration
(vi) (D) Product Development.
(vii) (A) gain buyers awareness about its versatile product range
(viii) (D) Gap Analysis
(ix) (B) Zero Level marketing channel
(x) (B) Innovation

(b) Define the following terms (in not more than two sentences): [1x5]
(i) Transfer Price
(ii) EFT
(iii) Loss Leader
(iv) Value Engineering

(v) Conglomerate diversification

Answer:

(i) Transfer Price: Transfer pricing refers to the pricing of assets, tangible and intangible, services, and funds etc within an organization. The choice of the transfer price will affect the allocation of the total profit of the company.

(ii) EFT Electronic Funds Transfer: refers to a system whereby companies can transfer funds by means of electronic communication with their banks.

(iii) Loss Leader: A product or service sold at lower-than-normal margins (probably at a loss) in order to attract customers who might then buy other items at normal prices.

(iv) Value Engineering: Value Engineering is a systematic method to improve the 'value' of goods or products and services by using an examination of function. This is achieved by either improving the function or reducing the cost of the product simultaneously ensuring that basic functions of the product are preserved and not reduced as a consequence of pursuing /value improvements.

(v) Conglomerate Diversification: Conglomerate diversification consists of making entirely new products for new classes of customers. These new products have no relationship to the company's current technology, products or markets.

(c) State whether the following statements are 'True' or 'False' with justification for your answer: **[1x5]**

(i) "Management buy-out" refers to the purchase of all or any part of a business firm from its owners by new managers from outside the business firm.

(ii) 'CVP model' is a simple break-even model.

(iii) 'Acquisition' is nothing but the joining of two separate firms to form a single firm.

(iv) 'Stars' are the products in a high-growth market but where they have a low-market share.

(v) Time value' refers to the difference between the market value of an option and its intrinsic value.

Answer:

(i) False: The correct statement is: Management buy-in (not Management buy-out) refers to the purchase of all or any part of a business firm from its owners by new managers from outside the business firm.

(ii) True: Break Even Analysis is based on cost-volume-profit (CVP) of a firm.

(iii) False: The correct statement is: 'Merger' is nothing but the joining of two separate firms to form a single firm.

(iv) False: The correct statement is: 'Question Marks' are the products in a high-growth market but where they have a low-market share. 'Question Mark', being a problem child has a low market share whereas 'Star' has a high-market share.

(v) True: Difference in value, positive/negative arises over a period of time. Hence the statement is true.

Question 2.

(a) Define a PPP in the context of developmental efforts in infrastructure in India.

(b) Explain the linkage between environmental analysis and strategic management. Accountant should associate himself in the implementation of Strategic TCM in an organization.

(c) What are the strategies adopted to combat hostile takeover?

[3+5+12]

Answer:

(a) Public-Private Partnership (PPP or P3) involves a long-term contractual agreement between a public sector authority and a private party. According to the Viability Gap Funding (VGF) scheme and guidelines for the India Infrastructure Development Fund, issued by the Ministry of Finance, GoI, a public-private partnership occurs when government agencies share resources and revenue with a non-government company. These partnership arrangements are used to meet specific niche requirements and are legally binding.

According to the Asian Development Bank, PPP is a range of possible relationship between public entity and the private party in the context of infrastructure and core services. This partnership is a mutually beneficial long-term relationship between the public and private sectors, which are an effective way to bridge gaps between demand and available resources, quality and accessibility, and risk and benefit.

(b) Environmental analysis has three basic goals.

(i) The analysis should provide an understanding of current and potential changes taking place in the environment. It is important that one must be aware of the existing environment and at the same time have a long-term perspective too.

(ii) Environmental analysis should provide inputs for strategic decision-making. Mere collection of data is not enough. The information collected must be used in strategic decision-making.

(iii) Environmental analysis should facilitate and foster strategic thinking in organization, typically, a rich source of ideas and understanding of the context within which a firm operates. It should challenge the current wisdom bringing fresh viewpoints into the organization.

The following are the specific benefits of environmental study:

(i) Development of broad strategies and long-term policies of the firm.

(ii) Development of action plans to deal with development of technological advancements.

(iii) To foresee the impact of socio-economic changes at the national and international levels on the firm's stability.

(iv) Analysis of competitor's strategies and formulation of effective counter measures,

(v) To keep oneself dynamic.

(c) A target company which faces the threat of a hostile takeover, would adopt the following Strategies:

Poison pill tactics: This strategy aims at initiating action against the predator by destroying the attractiveness of the firm. The following are few methods:

The acquiring company may issue substantial amount of convertible debentures to its existing shareholders which would make it difficult for the potential acquirer as there is a danger of considerable increase in the voting power of the company.

- The target firm either sells or mortgages or leases or otherwise disposes off some of its precious assets.
- The target firm can defend itself from the onslaught of the potential bidder is to dispose of its liquidity by acquiring some asset or other firm.
- The target grants its employees stock options that immediately vest if the company is taken over. This is intended to give employees an incentive to continue working for the target company at least until a merger is completed instead of looking for a new job as soon as takeover discussions begin. However, with the release of the "golden handcuffs", many discontented employees may quit immediately after they've cashed in their stock options. The poison pill may create an exodus of talented employees. In many high-tech businesses, attrition of talented human resources often means an empty shell is left behind for the new owner.
- The target company issues rights to existing shareholders to acquire a large number of new securities, usually common stock or preferred stock. These new rights usually allow holders (other than an acquirer) to convert the right into a large number of common shares if anyone acquires more than a set amount of the target's stock (typically 10-20%). This immediately dilutes the percentage of the target owned by the acquirer, and makes it more expensive to acquire control of the target.

Green mail tactics: The target firm can purchase its own stocks at a premium to avert a takeover bid. The incentive is offered by management of the target company to the potential bidder for not pursuing the takeover bid.

White Knight tactics: The target company's management may seek out a friendlier potential acquiring company who could offer a higher offer price which would eventually drive away the original bidder. The purpose of 'white knight strategy' is to seek to find a bidder. The objective is to make the takeover exercise as much unviable and unprofitable as possible for the original bidder. Such a strategy will help get the target firm a better deal. There are cases where a white knight has later been aggressive with the target company and consummated the deal at better terms.

Golden Parachutes tactics: Adopted by the target company by offering hefty compensations to its managers if they manage to get ousted due to takeover; this is pursued to reduce their resistance to takeover. This was also mentioned among one of the strategies of poison pill. This is mainly initiated because soft target firms who are managed by professional managers may fear shifting of loyalty by professional managers and to avoid any such attempts set up golden parachutes so that predators may not have incentive to deal with the agents for consummating the deal.

Divestiture tactics: Whereby target the company arranges to divest or spin off some of its businesses in the form of an independent, subsidiary company thus reducing the attractiveness of the existing business to the predator. This clearly changes the valuation of the company and many a times the multiples of valuation for multi divisional businesses would encourage such moves by target companies.

Crown Jewel tactics: Whereby the target company arranges to sell its crown jewel namely highly profitable part of the business or ones which market values better in order to dissuade the predator. However, such strategic initiative requires clear understanding of predators target businesses and valuation guidelines to be effective.

Legal tactics: A target firm can forestall the possible takeover bid through legal mode. It takes the form of 'legal strategy' for guarding against hostile takeovers. In this case, it is possible for the target firm to move a court of law for obtaining injunction against the offer. For this purpose, relevant provisions exist in the Securities Contracts (Regulations) Act, 1956 and the Companies Act, 1956. This strategy is resorted to either to block or delay the tender offer in circumstances where the shares are lodged for the transfer by the bidder. SEBI has come with clear guidelines to discourage hostile takeovers in India.

Question 3.

A mobile phone company which was already in the business of laptops and portable computing devices to capture a wide range of customers. It took the following steps:

(i) It adopted a technology where mobile phones could be simply used as phones or connected to the laptop using a hardware device or use wireless connection to the internet. Printing could also be done directly from the mobile through a printing device. The technology allowed transfer of selected contents of SIM/ mobile phone memory into memory cards which were also sold by the company as accessories in small quantities of 5 cards per packet.

(ii) It introduced a wide range of products – from the basic key punch to a touch pad and even voice recognition system. It also introduced landline models which were bigger devices and could be used in a fixed location by multiple users (as in households or offices) using the same mobile numbers, by using a wireless connector between the portable model and landline model.

(iii) It entered into tie-up arrangements with financial institutions having numerous service outlets in metros, similar towns and rural areas and provided a scheme where buyers could play in easy installments, while making an interest- fetching fixed deposit with the respective outlets. This scheme would psychologically aid the buyers while safe guarding the seller against potential bad – debts in case the product becomes obsolete.

(a) Classify the above measures into the marketing mix strategy as defined Mc. Carthy.

(b) What are the market segments that the company is trying to reach out to?

(c) It is criticized that while (iii) above provides access to a large number of customers, the scheme entails customers" outlay of the cost of the phone as fixed deposit as well as the first installment. Could you suggest other schemes to aid customers in buying higher models even if they do not have enough cash, while keeping in mind the possibility of obsolescence, bad – debts and recovery costs?

(d) What are the parameters in which you could effectively use the analysis for the information given in (i) to (iii) above? [4+6+5+5]

Answer:

(a) Mc Carthy"s Marketing Mix Strategy:

- **(i) Product:** Innovative – using laptop connection, wireless connection to internet, printing from mobile, memory cards-accessories, land line interchange, voice recognition.
- **(ii) Place:** Wide reach through urban and rural outlets.
- **(iii) Price:** attractive price for affordability and credit price
- **(iv) Promotion:** It entered into tie-up arrangements with financial institutions having numerous service outlets in metros, similar towns and rural areas and provided a scheme where buyers could play in easy installments, while making an interest-fetching fixed deposit with the respective outlets.

(b) The market segments that the company is trying to reach are:

- **Based on users:** Various age groups use the different models (from school children to the elderly.)
- **Based on geographical access to funding:** highly placed officials use all the accessories and facilities, while even the lower economic range would use the lower end model.

- **Based on affordability and use of facilities:** highly placed officials use all the accessories and facilities, while even the lower economic range would use the lower end model.
- **Based on attraction to non-existing segments which are only using landlines:** these users will gradually convert to this new facility.
- **Based on ancillary product"s usage:** users of printers, laptops, landlines, internet etc.
- **Based on financial tie-ups:** persons may be induced to make the FDs for availing credit. This may be psychological boost while spending on consumable goods.

(c)

(i) There could be a tie-up arrangement with the existing credit card/debit card banker for easy building and collection, so that the credit worthiness is monitored by the existing set up.

(ii) For the salaried class, a direct collection from the employer may be availed, so that default is lesser.

(iii) The number of installments or period of credit could be made lesser to take care of the obsolescence.

(iv) Instead of fresh FD, a takeover of the deposit may be considered without having to pass the penalty of foreclosure to the customer.

(v) Readily marketable value of other idle assets like gold could be taken as a safety mechanism in lieu of FD.

(d) Pareto analysis could be used in the given scenario in the following ways:

Concentrate on:

- 80% of the profit making product models and induce customers to buy.
- 80% of the non-defaulting customers try to retain them and repeat buying by offering more schemes.
- 80% of the market segment and bring better models/after sale service etc.
- 80% of the sales value generating products and strengthen tie-ups with the allied products like laptops etc.
- 80% of the geographical location buying the products and offer more value addition to those segments.

Question 4

(a) Explain strategic implications of BCG matrix model.

(b) Write a short note on

(i) Role of brands in the construction of barriers to entry

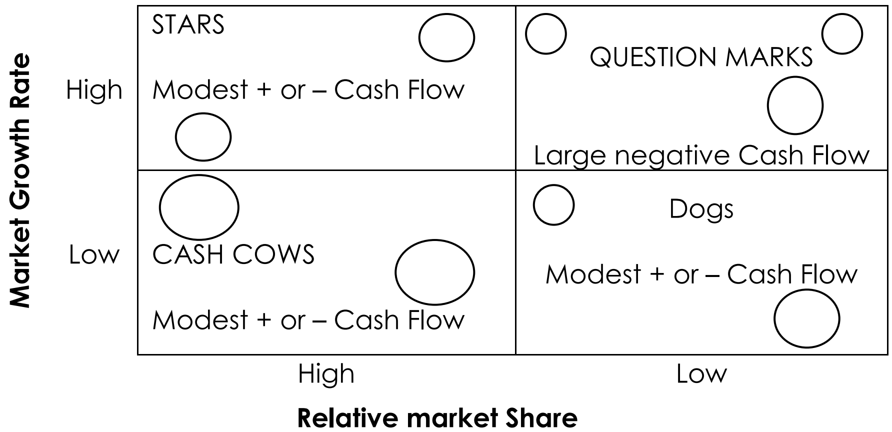
(ii) J. Strauss and R. Frost's E-marketing model

(iii) Kaizen Costing **[8+(4+4+4)]**

Answer

(a) In general, for large companies, there is always a problem of allocating resources amongst its business units in some logical/rational ways. To overcome such problems, Boston Consulting Group (BCG) has developed a model, which has been termed as the "BCG Matrix".

A simple pictorial depiction of the BCG matrix is as below:



The model uses the Market Growth (vertical axis) as the indicator of the industry's attractiveness and a typical marketer's market share(horizontal axis) as its competitive position. This sort of analysis enables a company to assess its competitive position. This sort of analysis enables a company to assess its competitive standing and enables to decide future resources allocation for its product portfolio.

Boston Classification	**Strategic Implication**
Question Marks	- High Market growth rate but low market share - Must decide whether to try for a star-hold or divest.
Stars	- Since the stars are growing rapidly and have the advantage of already having achieved a high share of the market, they provide the firms best profit and growth opportunities. - The firm should hold and build even though additional investment may be required.
Dogs	- Low market share and low market growth rate. - Dogs hold little promise for the future and may not even pay their own way, they are prime candidates for divesture
Cash cows	- Because of their high share positions in a low growth area. Cash cows are ideal for providing the funds needed to pay dividends and debts, recover overheads and supply the funds for investment in other growth areas.

The above model is a very handy tool for the management in resource allocation decisions.

(b) (i) Role of brands in the construction of barriers to entry

A barrier of entry makes it difficult for a new entrant to gain a foothold in a market. Barriers to entry include economies of scale, product differentiation, capital requirements, switching costs, access to distribution, and other cost advantages. Brands function as entry barrier in the following ways:

- **Product differentiation -** Porter discusses two criteria. Brand image is built up through advertising and other special features are reflects both use and signaling criteria.
  - Existing firms in an industry may have built up a good brand image and strong customer loyalty over a long period of time, through advertising, product quality, etc.
  - A firm might develop a variety of brands to crowd out the competition. Some firms own many brands to make it harder for competitors to get noticed by

consumers, as there are so many alternatives. This creates a barrier of entry, because new entrants would have to spend heavily to overcome the existing brand loyalties and to build up a brand image of their own.

- With some brands, there are also quite high **switching costs**, which is why many people are unwilling to change bank account because of the inconvenience of so doing.
- **Economies of scale** are also relevant. A certain amount of volume may be necessary to justify the promotion of the brand. Existing producers may already have built up a distribution network which functions best at this level.

(ii) J. Strauss and R. Frost's E-marketing model

E-marketing is the result of information technology applied to traditional marketing. It evolves from the company's overall E-business strategies and selected business models. It's application of a broad range of information technologies in marketing functions, to achieve the following:

(i) Transform marketing strategies to create more customer value.

(ii) More efficient planning and execution of conception, distribution, promotion, and pricing of goods/services.

iii) Create exchanges that satisfy individual consumer and business customer's needs and wants.

Judy Strauss and Raymond Frost's E-marketing model defines E-business as a continuous optimization of a firm's business through digital technology.

$$EB = EC+BI+CRM+SCM+ERP$$

Where, EB is electronic business, EC is electronic commerce (to enable buying/selling through digital technology), BI is business intelligence (for collecting primary/secondary data or information), CRM is customer relationship manager (to satisfy customers and build long lasting relationship), SCM is supply chain management (to delivery of products/services efficiently and effectively) and ERP is enterprise resource planning (optimization of business process and lowering costs, application of EDI, i.e. electronic data interface).

E-marketing is normally carried out in the following types:

a. **B2B**–This involves business-to-business marketing of inter-company business done online.
b. **B2C**–This involves business-to-consumer marketing, where goods/services are directly marketed by business organizations directly to the ultimate consumers using the Internet.
c. **C2C**–This involves consumer-to-consumer marketing, where consumers directly sell the goods/services to other consumers, using the Internet system.

Among these types, the maximum E-marketing activities take place, and the maximum online marketing opportunities lie in B2C where marketers sell directly to ultimate consumers.

(iii) **Kaizen Costing:**

The word **"Kaizen"** has originated from a Japanese word meaning continuous improvement or enhancement estimation during production. This involves setting up annual targets for improvement in elements of costs in conversion as part of production.

Kaizen costing is a costing technique to reflect continuous improvement efforts in small steps to the following;

(i) Control, reduce and eliminate various elements of costs in conversion as part of production. Each element of this cost is subject to continuous improvement.

(ii) Improve with quality assurance technology,

(iii) The effective responsiveness to the target customers
(iv) Improve the production process after manufacturing activities have begun (i.e., optimization of production by reducing the wasteful activities), and
(v) Financial endurance of business enterprises.

Any continuous improvement project in a Shop-Floor is known as Gemba Kaizen where Gemba refers shop-floor and Kaizen refers continuous improvement. Japanese expert Yashuhiro **Monden** defines Kaizen costing as the maintenance of present cost levels for the products currently being manufactured through systematic structured efforts to achieve the desired cost level. For example, optimization of total cycle cost is a typical Kaizen attempt. (Total cycle time cost = Set up time cost + Process time cost +Move time cost + Delay time cost).

SECTION-II (40 Marks)
(Risk Management)

Answer Question No. 5 and any other two from the rest in this section.
(Please answer all parts of the question at one place.)

Question 5.
(a) In each of the cases/statements given below, one of four alternatives is correct. Indicate the correct answer: [1x5]

(i) Portfolio Managements reduces
(A) Systematic risk
(B) Unsystematic risk
(C) Inflation risk
(D) Interest rate risk

(ii) Subrogation means
(A) Utmost good faith
(B) The active efficient case that sets in motion a chain of events which brings about a result
(C) The transfer of all rights and remedies available to the insured after indemnity has been effected
(D) Mitigation of loss

(iii) EPD in risk management means
(A) Economic policy holder deficit
(B) Expected probability of holder deficit
(C) Expected policy holder deficit
(D) Expected policy holder default

(iv) Instruments that hedge against risk do not include
(A) Letter of credit
(B) Underwriting
(C) Factoring
(D) Rights issues

(v) Value migration suggests the needs to monitor on continuous basis to detect and measure the changes happening in value flows
(A) Between the industries

(B) Between the companies
(C) Between the divisions of a company
(D) All of the above

Answer:

(i) A – Systematic risk (ii) C – The transfer of all the rights and remedies available to the insured after indemnity has been affected. (iii) C – Expected Policy Holder Deficit (iv) D – Rights Issues (v) D– All of the above

(b) State whether the following statements, based on the quoted terms, are 'True' or 'False' with justifications for your answer. If any statement is false, you are required to give the correct terms, duly quoted: [1x5]

(i) "Loss Control" is a method of risk financing for managing pure risk.
(ii) There is no distinction between risk and uncertainty in the business filed.
(iii) "Knock- for-Knock" agreement in a motor insurance provides that in the event of damage caused by collision, each owner will bear his own loss irrespective of legal liability.
(iv) The individual insurers or professional rate making organization may determine insurance rates are called profit loaders.
(v) Risk management is the process used to systematically manage exposures to both pure risks and speculative risks.

Answer:

(i) **False:** "Loss Control aims at controlling the occurrences of losses, while risk financing aims to fund the risk that may arise".
(ii) **False:** "Former implies that chances of each outcome occurring is known and latter implies that odds can only be guessed".
(iii) **False:** "It is an agreement between the insurers writing motor insurance. The respective insurers and not the owners bear the loss".
(iv) **False**: Actuaries are individual insurer or professional rate making organization may determine insurance rates.
(v) **False:** Risk management is the process used to systematically manage exposures to pure risks.

Question 6.

(a) What are the basic parts of an Insurance contract?
(b) How do you embrace project risk management and what are the strategies to be adopted?
(c) A businessman wants to decide whether to stock commodity A or commodity B. He can stock either but not both. If he stocks A, if it is a success, he feels that he can make ₹200 but if it is failure, he will loose ₹500. If he chooses A, there is an 80% chance of making ₹200. If he stocks B and if it is success, he feels that he can make ₹400 but if it is a failure, he would loose ₹300. If he chooses B, there is 60% chance of making ₹400 but if it is a failure, he would loose ₹300. If he chooses B, there is 60% chance of making ₹400. The question is: which commodity A or B should the businessman stock? [4+3+8]

Answer:

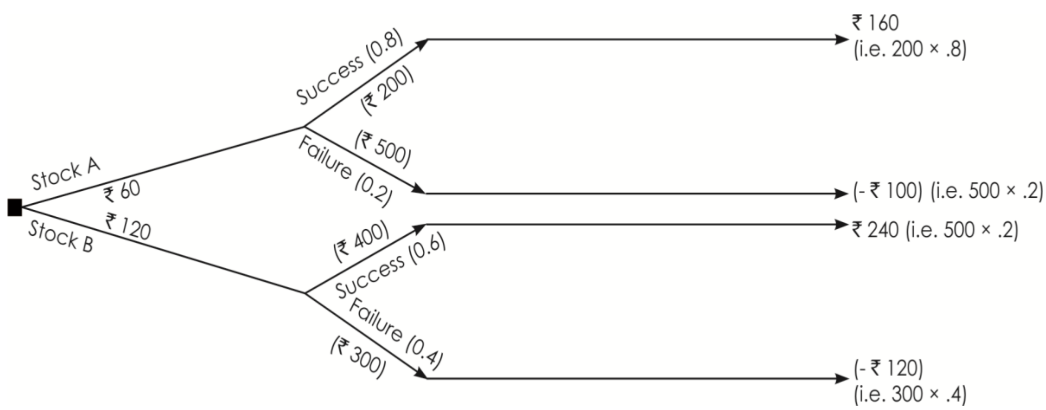
(a) The basic parts of an insurance contract – are as follows:

(i) Declaration – are the statements that provide information about the property or activity to be insured.
(ii) Definitions – clear the meaning of key words or phrases.
(iii) Insuring agreement – summarizes the major promises of the insurer.

(iv) Exclusions – three major types of excluded perils, excluded losses, and excluded property.
(v) Conditions – rules specific to a geographic location.
(vi) Miscellaneous provisions – situation or purpose specific.

(b) Project risk can be embraced through comprehension of residual risk. This risk could be retained by developing a proper information system regarding the residual risks, commercial aspects and developing a clear sense in bearing various risks, then understanding of particular risk domains to develop ability to bear commercial risks. This risk could be transferred through Develop information system regarding financial institutions, capital markets and special vehicle applications identification local industrialists who are ready to partner for sharing risks through a portfolio of investment, identification of international partners for sharing investments through a portfolio of investment, identification of financial institutions locally like commercial banks, identification of international financial institutions.

(c) Adopting the "**Rolling back"** technique, the problem may be solved through simple "Decision Tree Model".



At stock A, the expected pay-off would be : ₹ (200 x 0.8) – (500 x 0.2) = ₹ 60
At stock B, the expected pay-off would be : ₹ (400 x 0.6) – (300 x 0.4) = ₹ 120
Therefore, as the expected pay-off at stock B (₹ 120) is better than the expected pay-off of stock A (₹ 60), we should stock commodity B, if we can have a stock of only one commodity.

Question 7:

The Indian Umbrella market can be classified as, single umbrellas, single to triple fold umbrellas, spring action 'Piano' type umbrella, fancy umbrellas and specialized large golf and garden umbrellas. The sales of golf and garden umbrellas are limited and are sold through exclusive retail shops. Also there is a large institutional sale and cut-throat promotional and gift offers in the market in this category. Modern umbrellas are as old as 125 years in India. Mohendra Lal Dutta (MD) and K.C. Paul are the pioneers of this industry.

Companies and Police departments provide their outdoor staff with umbrellas on their own cost. Mohendra Lal Dutta and K.C Paul are well-known names in East-India's brand like SUN, STAG, EBRAHIM CURRIM is popular in the West. North has brands like CHANDNI, CAMPUS, while St. GEORGE, POPY are famous in South-India especially in the more rain affected Kerala. Till the fifties, there were two kinds of umbrellas in the country, the Bengali ones, popular in the East and the COLOMBO umbrella assembled in Konkan and Malabar also popular in the South-India and West-India. Cane and bamboo staves are used in all these

umbrellas.
During the sixties, the steel tube umbrella was introduced and instantly became popular because it was lighter and less bulky, Mohendra Lal Dutta working on a brand strategy, has created and floated his own brand called "MD" and hoped to take foreign brands when they would get the benefit of the Indian liberalization policy for export.
Questions:
(i) Is there any scope for a national brand for umbrellas? As a product manager of such a company, how would you prepare a product policy?
(ii) Will "MD" brands umbrellas succeed? What brand strategy the company will have to adopt?

(1+6)+(3+5)

Answer:

(i) Indians prefer brands which are very popular at the national level. At present most of the brands in umbrellas are regional in nature. Hence, there is an ample scope for a national brand for umbrellas.

The product manager should:

- ✓ Develop a long-range and competitive strategy for the product
- ✓ Prepare annual marketing plan and sales forecast planning
- ✓ Work closely with advertising agencies to develop programmes and campaigns at the national level to take on foreign brands when they come to India.

(ii) While choosing a brand the company should ensure that:

- ✓ It suggests something about the product
- ✓ It should suggest product quality
- ✓ It should be easy to pronounce.

The company should first test the market of the product to study the response of customers. Only when the brand evokes good feeling among the customers it should think of continuing with the brand name. Umbrellas are low priced items. Hence, the cost involved in promoting the brand should be reasonable. Umbrellas are a necessity. Hence, the brand strategy should be to promote it as national brand fulfilling a necessity. By ensuring good quality, it can be promoted as a product with durability.

Question 8.

Write short notes on the following: **[5×3]**
(a) CAPM
(b) Corporate Risk Governance
(c) Re – Insurance

Answer:

(a) CAPM

This model developed by William F. Sharpe and John Linter in the 1960s, wants to show a relationship between the unavoidable risks and expected return from a security. The CAPM model is based on the risk-averse behaviour of an investor.

It is concerned with two key questions:

(i) What is the relationship between risk and return for an efficient portfolio?
(ii) What is the relationship between risk and return for an individual security?

The CAPM, in essence, predicts the relationship between the risk of an asset and its expected return. This relationship is very useful in two important ways. First, it produces a benchmark for evaluating various investments. For example, when we are analyzing a security we are interested in knowing whether the expected return from it is in line with its fair return as per the CAPM. Second, it helps us to make an informed guess about the return that can be expected from an asset that has not yet been traded in the market. For example, how should a firm price its initial public offering of stock?

Although the empirical evidence on the CAPM is mixed, it is widely used because of the valuable insight it offers and its accuracy is deemed satisfactory for most practical applications.
CAPM is based on the following assumptions:

- Investors are risk averse
- Security returns are normally distributed
- The utility function of investors is quadratic,
- Investors have homogeneous expectations – they have identical subjective estimates of the means, variances and co-variances among returns,
- The market is perfect: there are no taxes; there are no transactions costs; securities are completely divisible; the market is competitive,
- The quantity of risky securities in the market is given.

Looking at these assumptions, one may feel that the CAPM is unrealistic. However, the value of a model depends not on the realism of its assumptions, but on the validity of its conclusions. Extensive empirical analysis suggests that there is a lot of merit in the CAPM.

(b) Corporate Risk Governance

Responsibility of a corporate body encompasses

- Identifying the organization's appetite for risk in the areas of capital leverage, credit rating, etc;
- The capability of the organization to manage risk and support its business strategy;
- Establishing the structural relationship between the roles and responsibilities for risk management;
- Pooling of risk and develop such integrated risk measures encompassing the various spheres of activity like finance, marketing, human resources and operations;
- Establishing proper tools for risk assessment, measurement and analysis;
- Developing a proper culture and awareness in the organization through leadership;
- Educating the various layers of organization about risks absorption and management through case studies. Corporate governance has become a buzzword in Indian corporate world and SEBI has laid down guidelines in this regard. Every annual report contains a section on corporate governance along with management's discussion on performance and future outlook.

(c) Re – Insurance

All insurance companies have a risk appetite i.e. a limit on the amounts that they can settle for any given claim that is made by the Insured. Any claims made beyond this specified limit by the insured is settled by another company referred to as a Reinsurance company.
Thus, Reinsurance is insurance for insurance companies. Reinsurance is the transfer of part of the risk that a direct insurer assumes by way of an insurance contract on behalf of the insured, to a second insurance carrier, the Re-insurer who has no direct contractual relationship with the insured. Direct insurers need reinsurance to limit annual fluctuations in the losses they must bear on their accounts and to protect the assets of the company

in the event of a catastrophe. Direct insurers take on hazards and risks from the policy holders. Re-insurers take on hazards and risks from the direct insurer.

Insurance companies typically enter into an agreement with the Re-insurer and sign a Reinsurance Treaty which states all the terms and conditions of the agreement. The Re-insurer agrees to accept a certain fixed share of risk upon terms as set in the agreement. The well known Reinsurance companies in the world are Swiss Re, Munich Re, and Zurich Re. For example, an Insurance company has a risk appetite of ₹1 million. But has issued a general insurance policy for an engineering project where the sum insured is ₹4 million. If a claim is made on this particular policy, the claim will be settled for ₹4 million. ₹1 million will be paid by the Insurance Company that issued the policy and the remaining 3 million will be paid by the Reinsurer.