PAPER 15 – BUSINESS STRATEGY AND 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

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

This paper contains 4 questions, representing two separate sections as prescribed under syllabus 2012. All questions are compulsory, subject to the specific guidance/ instructions stated against each question. All workings, wherever necessary, must form a part of your answer. Assumptions, if any, should be clearly stated.

Question No. 1. (Read the Case and Answer the following Questions)

1. DD is the India's premier public service broadcaster with more than 1,000 transmitters covering 90% of the country's population across an estimated 70 million homes. It has more than 20,000 employees managing its metro and regional channels. Recent years have seen growing competition from many private channels numbering more than 65, and the cable and satellite operators (C & S). The C & S network reaches nearly 30 million homes and is growing at a very fast rate.

DD's business model is based on selling half-hour slots of commercial time to the programme producers and charging them a minimum guarantee. For instance, the present tariff for the first 20 episodes of a programme is ₹30 lakhs plus the cost of production of the programme. In exchange the producers get 780 seconds of commercial time that he can sell to advertisers and can generate revenue. Break-even point for producers, at the present rates, thus is ₹ 75,000 for a 10 second advertising spot. Beyond 20 episodes, the minimum guarantee is ₹65 lakhs for which the producer has to charge ₹1,15,000 for a 10 second spot in order to break-even. It is at this point the advertisers face a problem - the competitive rates for a 10 second spot is ₹50,000. Producers are possessive about buying commercial time on DD. As a result the DD's projected growth of revenue is only 6-10% as against 50-60% for the private sector channels. Software suppliers, advertisers and audiences are deserting DD owing to its unrealistic pricing policy. DD has three options before it. First, it should privatize, second, it should remain purely public service broadcaster and third, a middle path. The challenge seems to be to exploit DD's immense potential and emerge as a formidable player in the mass media.

Required:

(a) Discuss the best option, in your view, for DD.

(b) Analyze the SWOT factors the DD has.

(c) Explain the proposed alternatives which you suggested.

(d) State the basic objectives for conducting SWOT analysis. [6+6+4+4]

Question No. 2. (Answer **any two** questions. Each question carries **15 marks**)

2. (a)

(i) State the drawbacks of Vertical Integration. [5]

(ii) Enumerate the advantages of Strategic Planning. [5]

(iii) Describe about the Internal and Competitive Benchmarking. [5]

2.(b)

(i) Discuss about the Organizational Development and its characteristics. [5]

(ii) Explain about the BCG Matrix. [10]

2.(c)

(i) "In maturity stage of product life cycle the market becomes saturated, price competition intensifies, and the rate of sales growth slows down." — Suggest strategic choices in such situations. [8]

(ii) Discuss how 'Gap Analysis' might be applied to a product/market situation. [7]

Question No. 3. (Read the Case and Answer the following Questions)

3. Medical Instruments uses a manufacturing costing system with one direct-cost category (direct materials) and three indirect-cost categories:

- Setup, production order, and materials-handling costs that vary with the number of batches
- Manufacturing operations costs that vary with machine-hours
- Costs of engineering changes that vary with the number of engineering changes made

In response to competitive pressures at the end of 2013, Medical Instruments employed value engineering techniques to reduce manufacturing costs. Actual information for 2013 and 2014 are:

	2013	2014
Setup, production-order, and materials-handling cost per batch	₹8,000	₹7,500
Total manufacturing operating cost per machine-hour	55	50
Cost per engineering change	12,000	10,000

The management of Medical Instruments wants to evaluate whether value engineering has succeeded in reducing the target manufacturing cost per unit of one of its products, HJ6, by 10%. Actual results for 2013 and 2014 for HJ6 are

	Actual Result for 2013	Actual Result for 2014
Units of HJ6 produced	3,500	4,000
Direct material cost per unit of HJ6	₹1,200	₹1,100
Total number of batches required to produce H J6	70	80
Total machine- hours required to produce HJ6	21,000	22,000
Number of engineering changes made	14	10

Required:

(a) Calculate the manufacturing cost per unit of HJ6 in 2013.

(b) Calculate the manufacturing cost per unit of HJ6 in 2014.

(c) Did Medical Instruments achieve the target manufacturing cost per unit for HJ6 in 2014 Explain?

(d) Explain how Medical Instruments reduced the manufacturing cost per unit of HJ6 in 2014.

(e) List out the steps involved in implementing a Target Costing.

(f) State the role of Cost Accountant to be assigned to a Target Costing Team.

[2+2+2+4+6+4]

Question No. 4. (Answer **any two** questions. Each question carries **15 marks**)

4.(a)

(i) Difference in operating speeds of machines may lead to higher WIP inventory. How does a JIT system resolve this issue? Explain. [4]

(ii) A single product company prepares quarterly budgets. Budgeted variable costs per unit are as under:

	₹
Direct materials	24
Direct labour 8 hours (₹ 6 per hour)	48
Factory overheads	16
Selling price	180

Administration overhead is ₹1,00,000 per month and fixed factory overhead is ₹ 90,000 per month including ₹ 20,000 depreciation. The normal capacity of the factory is 3,000 units per month. Finished goods stocks are valued at full factory cost of production and the budgeted opening stock on 1st July 2014 is estimated at 2,400 units valued at ₹ 2,66,000. It is the policy of the company to keep the opening finished stock of each month at a constant ratio to the budgeted unit sales of that month. Extra production in excess of the capacity of 3,000 units per month can be achieved by working overtime at double the labour hour rate.

Estimated sales are as under:

Month	Units
June 2014	2,600
July 2014	2,000
August 2014	2,800
September 2014	3,200
October 2014	3,600

The direct material costs relating to the production of each month are paid for in the succeeding month. The patterns of collection of sales are as under:

30% in the same month

70% in the next month

All other costs are paid in the month in which they are incurred. An installment of deferred payment of ₹14,000 in respect of the purchase of machinery is due for payment

in July 2014. The company has to pay dividend amount to ₹15,000 in September 2014. The projected cash balance on 1st July, 2014 is ₹1,00,000.

Required:

I. Prepare a combined budgeted Profit & Loss Statement for the quarter ended 30th September, 2014.

II. Prepare a cash budget for each of the three months of the quarter ended 30th September, 2014 *viz.* July, August and September 2014. [5+6]

4.(b)

(i) A book store wishes to carry 'Ramayana' in stock. Demand is probabilistic and replenishment of stock takes 2 days (i.e. if an order is placed on March 1, it will be delivered at the end of the day on March 3). The probabilities of demand are given below:

Demand(daily)	0	1	2	3	4
Probability	0.05	0.10	0.30	0.45	0.10

Each time an order is placed, the store incurs an ordering cost of ₹ 10 per order. The store also incurs a carrying cost of ₹ 0.50 per book per day. The inventory carrying cost is calculated on the basis of stock at the end of each day.

The manager of the bookstore wishes to order 5 books when the inventory at the beginning of the day plus order outstanding is less than 8 books.

Currently (beginning 1st day) the store has a stock of 8 books plus 6 books ordered two days ago and expected to arrive next day.

Use Monte-Carlo Simulation for 10 cycles.

The two digits random numbers are given below:

89	34	78	63	61	81	39	16	13	73

[10]

(ii) A firm has received an order from customer 'X' to be executed for ₹1,800 (all inclusive). The order requires the following materials, labour etc.:

Materials	Requirements	In stock	Book value	Replacement cost per kg.	Realisable value per kg.
Material 'A'	100 kg.	50kg.	₹250	₹7	₹3
Material 'B'	300 kg.	140 kg.	₹280	₹3	₹1

Labour:

Department I : 10 hrs @ ₹15
Department II : 8 hrs @ ₹12
Variable Overhead : ₹150

Materials 'A' is one that is regularly used by the firm and if used on this order has to be replaced for the use of other orders – Materials 'B' has no use and the result of excessive purchase made for an order executed two years ago.

Labour in department I is available for this order but labour in department II is fully engaged on another order which is earning a contribution of ₹20 per hour and if the order from 'X' is to be executed, labour in department II has to be diverted from current operations.

State whether the order received from customer 'X' has to be accepted. Show workings. [5]

4.(c)

(i) A city hospital has the following minimal daily requirement for nurses:

Period	Clock time (24 hours day)	Minimal number of nurses required
1	6AM - 10AM	2
2	10AM – 2PM	7
3	2PM – 6PM	15
4	6PM – 10PM	8
5	10PM – 2AM	20
6	2AM – 6AM	6

Nurses report to the hospital at the beginning of each period and work for consecutive 8 hours. The hospital wants to determine the minimal number of nurses to be employed so that there will be sufficient number of nurses available for each period. Formulate LPP. Do not solve. [5]

(ii) A company has 4 Zones and 4 Marketing Managers available for Assignment. The zones are not equal in sales potentials. It is estimated that a typical marketing Manager operating in each zone would bring in the following Annual sales –

Zones	East	West	North	South
₹	2,40,000	1,92,000	1,44,000	1,20,000

The four Marketing managers are also different in ability. It is estimated that working under the same conditions, their yearly sales would be proportionately as under:

Manager	M	N	O	P
Proportion	8	7	5	4

If the criterion is Maximum Expected Total sales, find the optimum Assignment and the Maximum sales. [10]