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

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.

Section A

1. Hassan Ltd. is one of the India's leading detergent manufacturing company. The firm has more than twenty-five product types. These have been developed over a period of its ten year existence. Some products are very successful while others have not performed well. The challenge for the board has been the formulation of strategy & policy in the way the company manages the portfolio of products.

As a newly recruited qualified Cost Accountant, your advice is being sought to address the following questions which the Product manager has prepared as input into his paper to the Board.

(a) Describe the Boston Consulting Group (BCG) growth vector matrix.

(b) Explain the strategic options which are available to Hassan in accordance to the BCG Matrix.

(c) State the limitations the model poses to the Product Manager as he prepares his paper to the Board.

(d) There are some products, which have high market growth rate but have low market share, produced by the Hassan Ltd. In the time of inevitably slow industry growth rate their market can be reduced. In this circumstances, state those strategies which are to be followed by Hassan Ltd. **(10+2+3+5=20)**

2. Answer any two questions **[2×15 =30 marks]**

(a) (i) "Choice of strategy is influenced by some factors"- State the factors that influence the choice of strategy.

(ii) Discuss about the Organizational Development and its characteristics.

(iii) Distinction between Strategic Management and Strategic Planning **[5+5+5]**

(b) (i) Enumerate the advantages of Strategic Planning.

(ii) Discuss the benefits of Strategic Alliance.

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

(c) (i) State the industry characteristics which influence the intensity of rivalry among the firms.

(ii) State the drawbacks of Vertical Integration. **[10+5]**

Question.3 (Compulsory) **[20 marks]**

Gujarat Mineral Development Corporation (GMDC) has two divisions. The Mining Division makes toldine, which is then transferred to the Metals Division. The toldine is further processed by the Metals Division and is sold to customers at a price of Rs 1,500 per unit. The Mining Division is currently required by GMDC to transfer its total yearly output of 4,00,000 units of toldine to the Metals Division at 110% of full manufacturing cost. Unlimited quantities of toldine can be purchased and sold on the outside market at ₹ 900 per unit.

The following table gives the manufacturing costs per unit in the Mining and Metals divisions for 2014-15:

	Mining Division	Metals Division
Direct materials	₹ 120	₹ 60
Direct manufacturing labour costs	₹ 160	₹ 200
Manufacturing overhead costs	₹ 320[a]	₹ 250[b]
Total manufacturing costs per unit	₹ 600	₹ 510

[a]Manufacturing overhead costs in the Mining Division are 25% fixed and 75% variable.
[b]Manufacturing overhead costs in the Metals Division are 60% fixed and 40% variable.

1. Calculate the operating incomes for the Mining and Metals divisions for the 4,00,000 units of toldine transferred under the following transfer-pricing methods: (A) market price and (B) 110% of full manufacturing costs.
2. Suppose GMDC rewards each division manager with a bonus, calculated as 1% of division operating income (if positive). What is the amount of bonus that will be paid to each division manager under the transfer-pricing methods in requirement 1? Which transfer-pricing method will each division manager prefer to use?
3. State the arguments would Amit, manager of the Mining Division, makes to support the transfer-pricing method that he prefers? **[(6+6)+5+3]**

Question.4 Answer any two questions **[2×15 =30 marks]**

(a) (i) A company produces two products X and Y, the production cost of which are show below:

	X (₹)	Y (₹)
Direct material cost	47.50	47.50
Direct labour cost	23.75	42.75
Variable overhead	23.75	42.75
Fixed overhead	23.75	42.75
	118.75	175.75

Fixed overhead is absorbed on the basis of direct labour cost.

The product passes through two processes, Assembly and Painting. The associated labour cost is ₹ 47.50 per direct labour hour in each. The direct labour associated with the two products for these processes are shown below:

Process	Time taken	
	Product X	Product Y
Assembly	10 minutes	40 minute
Painting	20 minutes	15 minutes

The current market price for X is ₹ 308.75 and for Y it is ₹ 247. At these prices, the market will absorb as many units of X and Y as the company can produce. The capacity of the company to produce X and Y is limited by the available capacity of the two processes. The company operates two shifts of 8 hours each. Painting is a single process line and two hours in each shift will be down time. Assembly can process two units simultaneously, although this will double the requirement of direct labour. Painting can operate for full 16 working hours each day.

What production plan should the company follow in order to maximize profit under (I) Traditional Costing System and (II) Throughput Accounting System? **[3+3]**

4(a) (ii)

A company has developed a special purpose Electronic Security Device and once introduced in the market, the same expected to have a life cycle of 3 years from the time of its introduction in the market before the device becomes obsolete due to technological advancement of other competitive products.

You have been asked by the company to prepare a product life cycle budget.

The following information is available:

	Year I	Year II	Year III
No. of units to be manufactured and sold	50,000	2,00,000	1,50,000
Price per device (₹)	500	400	350
R & D and Design cost (₹)	9,00,000	1,00,000	Nil
Production cost:			
Variable cost per device(₹)	200	150	150
Fixed cost(₹)	70,00,000	70,00,000	70,00,000
Marketing cost:			
Variable cost per device(₹)	100	70	60
Fixed cost(₹)	30,00,000	25,00,000	25,00,000
Distribution cost:			
Variable cost per device(₹)	50	50	50
Fixed cost(₹)	10,00,000	10,00,000	10,00,000

Prepare the budgeted life cycle operating profit.

It has been further indicated that if a discount of 10% is given to customer, the unit to be sold per year will increased by 5%. Would you recommend introduction of such discount? **[3+6]**

4(b).(i)

Explain the theory of constraints? **[5]**

4(b).(ii)

Apollo Company prepares its budgeted output and sales at its maximum capacity of 50,000 units for 2014. However, due to efficiency improvements, Apollo was able to sell 55,000 units for the year. Other data for 2014 follows as:

Budgeted fixed overhead costs	₹ 41,25,000
Budgeted selling price	₹ 825
Budgeted variable cost per unit	₹ 330

I. Calculate the budgeted profit per unit, the operating income based on the budgeted profit per unit, and the flexible-budget operating income.

II. Compute sales-volume variance and production-volume variance. What do each of these variance measures? **[4+6]**

Question.4 (c) (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

[3+3]

4 (c).(ii)

Two similar products A and B, manufactured by a company for a production period have the following data:

Particulars	Product A	Product B
Selling price (₹/unit)	142.50	199.50
Variable cost (₹/unit)	85.50	114.00
Labour hours per unit	2	6

Total fixed costs that have to be incurred irrespective of the type of product amounts to ₹ 5,13,000. Besides, there are specific fixed costs of ₹ 1,71,000 to be incurred only if A is produced and ₹ 2,05,200 to be incurred only if B is produced. Assume no inventory. At present, 7,500 units of A and 7,500 units of B are sold.

Required:

I. What is the current Break-Even Point (BEP)?
II. What is the minimum number of units to achieve BEP?
III. If there are only 10,000 labour hours possible in production period, what would be the optimum product-mix? **[2×3=6]**

4 (c).(iii) "Kaizen Costing is an approach that explicitly incorporates continuous improvement during the budget period" Discuss the statement. **[3]**