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THE INSTITUTE OF  
**CHARTERED** ACCOUNTANTS  
OF SRI LANKA

# **SUGGESTED SOLUTIONS**

**KB 5- Business Value Creation**

**June 2015**

# SECTION 1

## Answer 01

Relevant Learning Outcome/s: 1.1/1.2
1.1 Nature of business value
1.2 Value creation process

- (a) In a typical value chain, there are two types of activities namely primary activities and secondary activities. Those activities relevant to the Comnet Bank (Pvt) Limited are given below.

### Primary activities

As Comnet Bank (Pvt) Limited is a service organization inbound and outbound logistics are not important primary activities of the value chain. However following primary activities are important for the value creation process.

1. **Operation:** operation means all activities cost and assets associated with converting input into output. In the given scenario, operation activities include all banking and non-banking activities of the organization. Specially accepting deposits, providing loan facilities, providing facilities to settle payments and money transfers etc. can be considered as core banking activities. Providing leasing, credit card services, and bank assurance etc. can be considered as non-banking operations.
2. **Marketing and Sales:** means activities, cost and assets dealing with advertising, promotion, pricing and channel relations. In this situation all advertising such as TV, press, radio or any other commercial media adopted for promoting Comnet Bank and all the point of sales materials such as posters and banners display in the bank premises can be considered as belonging to this category. Further special sales promotions like mobile banking and offering competitive interest rate etc. can be considered as activities of marketing and sales.
3. **Services:** means the activities, cost and assets relating to providing assistance to buyers. Therefore all the services provided within the bank premises to help their customers and all the after sales services such as providing business consulting to borrowers, issuing recommendations about client background, providing necessary information (e.g. checking balance of their accounts, due dates of installment of loans, cheques in the float etc.) and assisting client businesses in different perspectives can be considered as the activities associated with the service component.

Main supportive activities are given below

- **Firm's Infrastructures:** includes all activities, cost and assets relating to the general management, accounting, finance, and strategic planning etc. Therefore day to day administration work, office management activities, handling transportation for banking activities, recording the transactions and preparing final accounts etc can be considered as each activities.
- **HRM:** includes all activities, cost and assets relating to staffing, training and development etc. Therefore staffing process such as job designing, recruitment, selection and hiring as well as all the staff training programs adopted by Comnet Bank can be considered in this category.

- **Technology development** : means all activities , cost and assets relating to R&D , product and process improvements. If Comnet Bank has undertaken research for developing new products or technology and any other activity involved in improving the productivity of the operation process by adopting new technology, these can be considered as activities associated with technology development.
- **Procurement:** means all activities , cost and assets relating to purchasing of RM , machinery and supplies. Therefore purchasing machinery such as computers and other tools for banking operations, purchasing stationery and obtaining other supportive services can be considered as procurement related activities of Comnet Bank.

(b) Being a service company, the value chain model may not be applicable in its entirety to Comnet bank. However, in their attempt to enhance value creation for their customers, the value chain model could be beneficial in many ways.

1. Identify sources of value. Since the net profit of Comnet is reducing, they can use the value chain to identify non value adding activities that can be eliminated or done more cheaply. As much as the value chain shows how the value is created, it also shows how the costs are added. Hence understanding these costs would enable Comnet to reduce or eliminate them.
2. See the business as a whole. Rather than viewing business functions in isolation, the value chain would enable Comnet to understand how the overall value is being created by the combination of all activities. Hence this would provide a better overall view of the company's total value proposition.
3. Identify potential sources of competitive advantage. The value chain can support Comnet to identify and develop a clear competitive strategy. Whether Comnet decides to follow a cost leadership strategy or a differentiation strategy, understanding and aligning the value creation activities to suit the selected strategy is important. The value chain could act as a very important tool in this exercise.

**(Total: 10 marks)**

## Answer 02

Relevant Learning Outcome/s: 2.2
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2.2 'Inventory management and warehousing
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(a) Value is created in warehousing through efficient planning, operations and control. These are required in all the following aspects of operations (functions):

1. Handling goods received from suppliers: checking that the supplier has delivered them as specified in the purchase order, and in good condition; transferring the purchased items into a storage location
2. Handling, recording and storing finished goods as they come out of production
3. Protection of items during the time they are held in store
4. Efficient location of items within store, so that physical movements of items are minimised – this speeds up the despatch process
5. Despatching orders
6. Monitoring and controlling inventory levels, to minimise stock-outs but also to avoid excessive levels of inventory: limiting costs of losses due to damaged and stolen inventory

(b) Warehouse Management System (WMS) is an IT system for controlling the movement and storage of goods within a warehouse and processing associated transactions such as receiving goods, putting them away, picking goods for shipment and shipping them. A WMS monitors the progress of products through the warehouse.

A WMS would improve the operation of Tradestar in the following ways,

1. Minimise cost - A WMS could enable Tradestar to minimise cost. Since WMS is usually an automated system, the documentation cost and people cost could be minimised by implementing a WMS.
2. Reduce service time - Since the employees will be able to easily identify the goods and their location, the goods can be located much faster reducing service time and improving service to the customer.
3. Inventory Control - A WMS could help Tradestar to track where products are held, which supplier they come from, and the length of time they are stored. This could provide an analysis of data to improve inventory control.
4. Maximise the usage of space - WMS can be used for modelling the physical storage facilities such as racking and location of racks. This could enable Tradestar to reduce storage space utilised and maximise the available space more efficiently.

**(Total: 10 marks)**

### Answer 03

Relevant Learning Outcome/s: 3.2.

3.2. Product design and process selection (new product development)

- (a) Womack and Jones (*Lean Thinking*) define five principles for improving lean manufacturing by lean thinking
1. Specific value - The critical starting point for lean manufacturing is value that the customers want. Value can only be defined by the customers. Therefore the first principle is to specify what creates value from the customer's perspective.
  2. Value stream - For each product, identify the 'value stream'. These are the activities in the production process that create the value that customers want.
  3. Flow - Make the production process flow in response to demand, without interruptions such as breakdowns or defective output
  4. Pull - Let the customer 'pull' value from the producer. The producer should only make what is valued (pulled) by the customer, and make it just in time to satisfy customer demand. Lean manufacturing is associated with just-in-time purchasing and production methods.
  5. Perfection - Strive for perfection (zero defects) by constantly removing layers of waste, and by removing delays and discontinuities in the supply chain and manufacturing process
- (b) As explained in the scenario, lean manufacturing would enable a business to reduce the non value adding activities in the manufacturing process. It is an approach to manufacturing or a 'philosophy of manufacturing'. The aim of lean manufacturing is to increase value and minimise the amount of resources used in the manufacturing operations.

Lean manufacturing can be used to minimize cost, improve liquidity and reduce cycle time.

**Minimize cost :** By understanding the non value adding activities and value adding activities of a business operation, the management can take action to eliminate or reduce the amount of non value adding activities. When the non value adding activities are reduced or eliminated, the businesses will be able to reduce their cost of operations. Also by striving for excellence to reduce defects by constantly removing the layers of waste, lean manufacturing would enable the business to reduce quality rejects and cost of quality.

**Improve liquidity :** Liquidity is the amount of cash or easily cashable assets available to a business. Lean manufacturing is based on a 'pull system' where the goods are only produced when there is a demand from a customer. This would enable the business to avoid holding inventories and holding valuable resources in the business in stocks which customers never want to buy. At the same time, the raw material will be purchased 'Just in Time' and minimum work in progress will be maintained between operations. This would enable the business to reduce the amount of cash tied up in inventories.

**Reduce cycle time :** The cycle time is the time taken to complete an activity. In a business, time taken by each activity will add up to the total cycle time of the operation. Lean manufacturing by identifying and eliminating or reducing non value added activities will reduce the activities carried out by a business. When the amount of activities is reduced, the cycle time of the overall operation will reduce.

**(Total: 10 marks)**

## Answer 04

Relevant Learning Outcome/s: 6.3.
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6.3. E-business
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- (a) B2B (Business to Business) involves companies doing business with each other using internet as platform, as when manufacturers sell to distributors and wholesalers to retailers.
- B2C (Business to Consumer) involves the business using the internet to deal with consumers and sales to the general public. A large part of B2C takes the form of buying and selling online and online marketing.
- (b) Internet has provided a whole new platform for businesses to operate and has changed radically the way a traditional business would interact with the customers. This radical change can be analysed as follows.
1. Direct contact with the customer - B2C platforms provided by the internet has enabled businesses to interact directly with their customers. Now businesses can establish direct relationship with their customers without going through other intermediaries and middlemen. This also enables the businesses to cut down on operating cost and provide goods and services to customers at much lower cost. A business like Savari.lk can hence provide a much more competitive cost service to customers when compared to traditional travel agents with physical office spaces.
  2. Convenience for the consumer - The consumers can now interact with their sellers from anywhere at any given time at their convenience. This has changed the conventional buying habits of the consumer. The businesses have to now adapt to the new buying behaviours of consumers who make their purchases on the internet and provide them with the necessary platform and support to make their interactions as convenient as possible.
  3. Small companies can succeed - Given the ease of setting up and operating on the internet, not only large corporations, but even small businesses can easily move in to the global market place. All they need to have is a B2C e-commerce platform and they can overcome the heavy burden of owning or renting physical store locations and the cost of operating such locations.
  4. Virtual businesses - Businesses like Savari.lk are completely new business models enabled purely because of the e-commerce platforms facilitated by the internet. In some cases these virtual businesses can be operated from home, using a network of subcontractors to provide services to customers.
  5. New economics of information - With the availability of internet now most of the information is free. Hence customers can easily access product options, compare them, understand product reviews made by other customers and make informed product selection decisions.
  6. Speed of transaction - The internet provides the capacity to conduct and complete business transactions in a very fast manner. Unlike the traditional store locations, the customer now does not have to make a special visit, but can look at options, select and purchase at a much faster speed. Hence the businesses need to ensure that their e-commerce B2C platforms are convenient to use and faster to operate and complete transactions.

**(Total: 10 marks)**

## Answer 05

Relevant Learning Outcome/s: 7.3.
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7.3. Strategic purpose of an organization
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- (a) Critical success factors (CSFs) are those actions that must be performed well in order for the goals and objectives established by an organisation to be met successfully. By using CSFs organizations can excel to outperform competition. These are underpinned by competences which ensure this success'.

When considering the present scenario of mobile communication market in Sri Lanka, it is noted that the entire market is dominated by two leading operators who together control 80% of the market. Two other players also operating a big catering to niche markets. Therefore following CSFs are the more relevant factors to success in the Sri Lankan Market.

- i) Brand awareness and preference – In the mobile telecommunication market most of the customers like to maintain strong brand loyalty with features of definite identification. Therefore MobCom should develop brand awareness and create brand preference through unique brand personality to succeed in the market.
  - ii) Perceived service quality – As mobile telecommunication is a service, most customers expect high service quality such as reliability, assurance, responsiveness, empathy as well as tangibles from their mobile service provider.
  - iii) Area Coverage – Area coverage is a key determinant in the mobile telecommunication industry. Some service providers in the industry need to expand their coverage. Therefore some customers may not buy their services.
  - iv) Cost of services – As per capita income in Sri Lanka is relatively low, customers are highly concerned about the price of their mobile communication network.
  - v) Differentiated features of the services – Most small companies become successful by providing differentiated services and features of this market. Therefore they are able to succeed with specialized niche markets.
- (b) KPIs set to achieve the objectives of an organization have to be SMART i.e. specific, measurable, attainable, realistic and time bound. Following are some of the KPIs MobCom can set to measure the achievement of the organization in connection with different CSFs;
- Increasing brand awareness by 90% and brand preference by 20% during first five years (CSF - Brand awareness and preference)
  - Maintaining higher service quality in handling customer complaints, bill settlement and other technical supports compared to major competitors during first five years (CSF - Perceived service quality) – customer survey results.
  - Cover more than 75% of geographical areas of the country during first five years (CSF – Area coverage)
  - Offer cheaper packages than competitors without violating regulations of TRC during first five years (CFS - Cost of services) e.g. service cost per subscriber
  - Offer differentiated and customized packages for different purposes such as calling, data, video conferencing etc. during first five years (CSF - Differentiated features of the services). A no of new features offered compared to competitors.

**(Total: 10 marks)**

## SECTION 2

### Answer 06

Relevant Learning Outcome/s: 7.3/4.1/4.2
7.3 Strategic purpose of an organisation
4.1 Role of marketing strategies
4.2 Segmentation, targeting and positioning

- (a) Competitiveness of the fairness cream industry in Sri Lanka can be analyzed by using the Porter's Five Forces model. According to the model, industry competitiveness is decided based on five forces.

Rivalry – There are several strong players in the market and some local competitors are trying to establish themselves in the market. Therefore rivalry among the existing competitors in the market is high.

Threat of new entrants – Fairness cream industry has very few barriers to entry. Therefore it is possible for most of the small players to enter into the market by introducing local products or importing reputed brands in small quantities. Therefore threat of new entrants is high.

Threat of substitutes – According to the given details, there are many alternative products available in the fairness cream market. Specially herbal products and some products using hormones etc. have a big threat to the fairness cream market. Therefore threat of substitutes is high.

Bargaining power of buyers – Buyers have high bargaining power because they have opportunity to select a suitable product from the wide range of brands available in the market.

Bargaining power of suppliers – In this industry source materials are readily available. Therefore suppliers cannot have a big influence on manufacturers. Further imported products are also introduced to the local market with their own names. Therefore foreign suppliers don't have much control over local distributors. Therefore bargaining power of suppliers is relatively low.

- (b) Mainly in consumer markets, companies such as Beauty Pharma do not attempt to appeal to every customer, but rather would select one or more market segments they would cater to. The purpose of market segmentation is to identify the segment or segments each companies would target with their marketing activities.

According to the findings of consumer survey conducted by the independent research firm, products for whitening have been particularly successful in villages. Rural markets have contributed a significant share of this market and are an important factor in driving growth. Therefore they can adopt to several segmentation variables in proposing the target market for Soft Petal. Possible segments under selected variables are given below.

- Geographical Segmentation (Density and Location) –Rural Areas and Urban Areas
- Demographic Segmentation
  - o Age – Below 16 years, 16 years – 36 years, 37 years – 60 years etc.
  - o Gender – Male , Female
  - o Income – Low , Middle and High
- Behavioural Segmentation (Benefit sought)– Fairness and Beauty, Skin Care, Nutrition etc.



- (c) Based on above segments under each variable, suggested target market can be selected for the new product. Accordingly following target market can be proposed for Soft Petal.

“Young middle income female customers who are located in rural areas and who equate fairness with beauty and expect both from the cosmetic products” .

Based on this target market, company can develop comprehensive profile of target customers.

- (d) Marketing mix is the combination of factors that a company puts together to make products meet the needs of the different customers. A typical marketing mix would include the basic attributes of the product, how the company would price the products, promotional method and how the product would be distributed to the end consumer. This combination of factors is known as the 4Ps.

Beauty Pharma could use the marketing mix as follows in developing the marketing strategy for Soft Petal.

### **Product**

Since Soft Petal is a fairness cream, it first needs to be established as a product that delivers the core attribute that it promises to deliver. The design of the product, features and modifications to meet the different needs of the consumers may be important. For example, Soft Petal can introduce different variations to suit different skin conditions of consumers like a product variety to cover oily skin, dry skin and normal skin. In addition it should include the ingredient for fast whitening. Further packaging branding and other features of the product should be considered in designing the product. Especially sachets of Soft Petal will be very popular among rural customers.

### **Price**

Given the low income of the target market, it is important for Beauty Pharma to make Soft Petal an affordable product to its customers. They (Beauty pharma) can assess the market price of other competitor products to have an initial understanding of the price they may be able to charge. Price discounts can also be proposed in the initial stage.

### **Place**

Place is where the customers are able to buy the product. A company must provide a distribution channel so that the customers could buy the product. In the case of Soft Petal, Beauty Pharma may benefit by distributing them through retail outlets rather than specialized stores such as pharmacies. In this way the female consumer will find it more convenient and comfortable to purchase the product than going to a pharmacy to purchase it as a special item. Opportunities of modern trade are limited due to target customers being in rural markets. They can consider appointing distributors for geographic segments for larger coverage.

### **Promotion**

This is how the company would communicate its marketing proposition to its potential customers. This could include direct selling, advertising, sales promotion, e-communications, public relations and direct marketing etc. For example, Beauty Pharma may be able to provide a sachet of Soft Petal free along with one of its other famous cosmetic products to introduce it to the market as a sales promotion strategy. They can also use advertising mass media. Specially, TVC can be used in the commercial break of Hindi movies, Sinhala tele dramas and music programs. Press advertisement can be used in female targeted papers and magazines. Social media can also be used but only for selected customers.

**(Total: 25 marks)**

## Answer 07

Relevant Learning Outcome/s: 5.1/5.2/5.3/5.4
5.1 Role of human resource management in value creation
5.2 HR planning
5.3 Talent attraction and retention
5.4 Performance management

- (a) According to the given scenario, JH Holdings is a medium scale company and offers quality electrical items to the local market under its own brand names. Even though company has high growth potential, it has difficulty in developing due to some internal issues of the company. Most of those issues relate to HRM.

Most important issues can be summarized as follows.

- Lack of job designing  
There is no proper job designing adopted by the company. According to the details, most of the duties of employees are decided by Admin Manager.
  - No job description and specification  
As most of the employee conflicts are created through overlapping duties, it is noted that JH Holdings does not have proper job descriptions for some positions. Further there is no evidence to say that they are using job specification to identify the right persons for the jobs.
  - Inefficient recruitment and selection process  
According to the given details, there is no proper recruitment or selection process. Applications are generated from both internal and external sources and the candidate is selected without following acceptable procedures.
  - Lack of formal induction  
According to the given details most new employees are leaving the company before completing their probationary period due the difficulties of adapting to the prevailing culture of the organization. Therefore prevailing symptoms indicate lack of formal induction.
  - No proper performance appraisal method  
Salary increments are decided by CEO and he does not disclose the mechanism of evaluating employees. This means there is no proper performance evaluation at the company.
- (b) With the purpose of solving above issues, top management should take necessary action to establish a separate HR department and assign a separate manager for the HR function. As they have already make this decision, top management of JH Holdings should new provide facilities to formalize HRM practices within the company in order to creat value for the business through people.

After establishing the separate HR department the following actions are to be taken immediately.

- Analyse current positions and re-design the jobs. New positions should be created based on the requirements of the Company.
- Prepare proper job descriptions and specifications specifying the duties attached to each job and select the best people for the respective positions. Through this procedure the unnecessary involvement of Admin Manager can be limited.
- Plan HR for the future  
The company can determine future HR needs and compare such needs with the available man power to identify potential labour shortage or surplus. They can then utilize the existing man power more effectively and efficiently.
- Establish formal recruiting and selection process  
JH Holdings should establish a formal process for recruiting potential candidates and selecting the most suitable individuals for the different jobs. It helps to acquire best talent from the competitive labour market.
- Introduce proper induction  
HR department should established a formal procedure for orientation of new employees. The purpose and content of the induction program should be clearly set out by the department.
- Establish performance appraisal system.

HR department should initiate a formal performance evaluation scheme for employees. Based on the results they can decide salary increments, promotions and training needs etc.

In addition to the above, HR manager is responsible for implementing other HRM functions such as training and development, pay and welfare management and grievance handling etc. within the company to further increase business value through people.

- (c) As Company does not have a formal recruitment and selection procedure, HR manager should adopt the following steps.
- Determine tasks, duties and responsibilities relevant to the post of Accountant- This can be done by HR manager based on the job description of Accountant developed after the job analysis process.
  - Deciding job requirements – Based on the job analysis information, HR manager should prepare job specification specifying qualifications, experience, and any special (mental or physical) requirement for the post of Accountant.

- Deciding recruitment method – Recruitment method should be decided based on the recruitment policy of the Company. As the proposed position is that of Accountant it is better to go for paper advertisements in popular week-end English newspapers.
- Collecting applications and creating a pool of qualified candidates – After the advertisement, HR department should have the mechanism to collect applications from candidates and arrange their details into standard format.
- Short listing candidates - As the job requirement is to hire a Chartered Accountant, all the candidates should be short listed based on education qualifications and past experience.
- Selecting suitable candidate – Selecting can be done based on several techniques such as selection examinations, interviews, background investigations etc. However, in the given situation, it can be recommended to use several selection interviews. Accordingly, first interview can be conducted jointly by HR and Admin managers and second interview can be conducted by CEO.
- Formal hiring and signing of contract – After selecting a suitable candidate, HR manager should prepare appointment letter and job contract and inform candidate. Selected candidate and the CEO should sign the contract to confirm formal appointment.

**(Total: 25 marks)**

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