

CA



THE INSTITUTE OF
CHARTERED ACCOUNTANTS
OF SRI LANKA

SUGGESTED SOLUTIONS

KE5 – Commercial Insight for Management

March 2016

SECTION 01

Answer 01

1.1

Learning Outcome/s:

1.3.1 Identify the types of resources used by the business organizations in creating value for customers (including the 7M's: money, men, material, method, machine, market and minutes)

Correct Answer B

1.2

Learning Outcome/s:

3.5.2 Explain how market equilibrium is achieved in competitive markets and its relevance for business

Correct Answer A

1.3

Learning Outcome/s:

3.3.1 Identify different types of customers

Correct Answer B

1.4

Learning Outcome/s:

3.6.2 Compute the different types of elasticities

Correct Answer B

1.5

Learning Outcome/s:

4.3.2 Define the concepts of national income (including GDP, nominal & real GNP and NNP)

Correct Answer A

1.6

Learning Outcome/s:

4.4.1 Explain demand-pull/cost-push inflation and identify the cost of inflation on business and the national economy

Correct Answer B

1.7

Learning Outcome/s:

4.5.1 Explain how exchange rates are determined and how changes in exchange rates affect businesses

Correct Answer A

1.8

Learning Outcome/s:

6.4.1 Identify the steps involved in production capacity planning

Correct Answer C

1.9

Learning Outcome/s:

6.8.1 Define marketing management and scope of marketing

Correct Answer C

1.10

Learning Outcome/s:

6.16.1 Identify the basic concepts of change management

Correct Answer B

(Total: 20 marks)

Answer 02

2.1

Learning Outcome/s: 1.4.1 Define 'vision', 'mission', 'goals' and 'objectives' of business organisations
Purpose – why does the organization exist and for whom Strategy – this provides the operational logic for the organization. Policies and Standards of behavior – mission should influence what people actually do and how they behave. Values – what the organisation believes to be important.

2.2

Learning Outcome/s: 2.7.1 Discuss the concept of opportunity cost and scarcity and their relevance to economy choice
All societies and organisations find that the resources available to them are <u>scarce</u> and these resources can be put <u>to alternative uses</u> . Hence, a <u>choice</u> has to be made as to the best use to which the resource should be put. Every time a choice is made between <u>alternatives</u> , one would select the “best” alternative which means that the “next best” alternative has to be sacrificed. Opportunity cost is the <u>cost or value of the “next best” alternative that was sacrificed</u> .

2.3

Learning Outcome/s: 3.4.1 Identify the behaviour of rational consumers using cardinal and ordinal utility
Cardinal utility theory suggests that consumers are able to measure absolutely the satisfaction that they derive from consumption of a given quantity of a commodity. For example the satisfaction derived from eating a piece of cake is 100 utils. Ordinal utility theory suggests that consumers cannot measure the utility absolutely. Instead they rank different commodities or different baskets of commodities to choose the best one. Example: orange juice is preferred to tea.

2.4

Learning Outcome/s: 3.7.1 Demonstrate the impact of government intervention on competitive markets and business activities through ceiling price, floor price, taxes, subsidies and quotas
A ceiling price or a maximum selling price is usually fixed on essential goods. (e.g. sugar). The price is set below the equilibrium price so that poor households would be able to buy these goods. At this price demand would exceed supply. Consumers will compete to buy the limited stock available, resulting in the emergence of “a black market”. To prevent this, Government <u>will adopt a rationing scheme</u> and the appointment of officials to supervise the rationing scheme. This means extra administrative costs to society. These are adverse consequences when government fixes maximum selling prices for goods.

2.5

Learning Outcome/s:

4.5.3 Discuss the factors affecting demand and supply of foreign currencies.

1. Devaluation of currency in the domestic country
2. Direct measures to restrict imports such as tariffs or import quotas or exchange control regulations
3. Domestic deflation to reduce aggregate demand in the domestic economy.
4. Measures to encourage exports and inward transfers

2.6

Learning Outcome/s:

4.5.3 Discuss the factors affecting demand and supply of foreign currencies

- The rate of inflation compared with the rate of inflation in other countries
- Interest rates compared with the interest rate in other countries
- The balance of payment
- Speculation
- Government policy on intervention to influence the exchange rate

2.7

Learning Outcome/s:

5.4.2 Discuss the main areas on leading

- Hygiene factors – company policy and administration/salary/working condition/job satisfaction/interpersonal relations/quality of supervision
- Motivator factors – status/advancement/challenging work/a senses of achievement/growth in the job/responsibilities/recognition

2.8

Learning Outcome/s:

6.6.1 Define main production methods (job production, batch production and flow production)

Job production is where the end product of a job is a single item made for a specific purpose.

Batch production is where products are produced in batches of some volume rather than as one-off items.

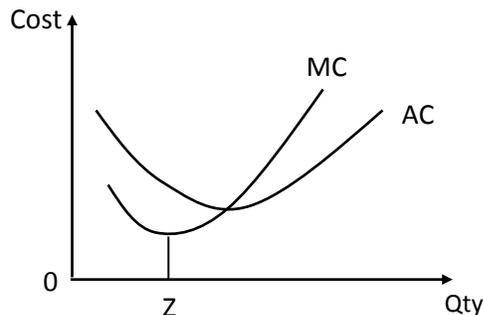
Continuous Flow production is where basic materials are produced through a succession of stages.

2.9

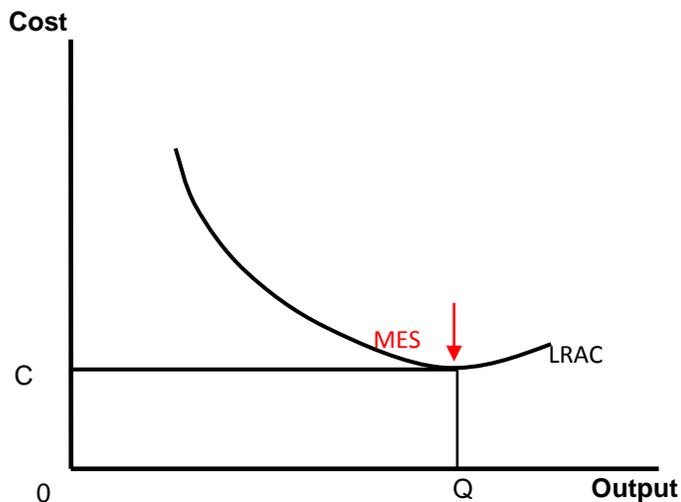
Learning Outcome/s:

6.3.1 Discuss the different cost concepts in short run and long run

In the short run (where one or more factors of production is fixed in supply), the average cost (AC) curve is typically U-shaped. Average costs fall up to a point with the spread of the fixed overhead. Beyond a point, (point Z), the law of diminishing returns will set in with the variable costs rising steeply. This explains the rising part of the AC curve.



In the long run, the AC curve (LRAC), will have a shallow U shape or L-shape. Average cost will decrease sharply with the factory moving to large scale production. However, beyond a point, diseconomies set in and the LRAC begins to rise.



2.10

Learning Outcome/s:

6.12.2 Identify the importance of HRM to a business

- It helps an organisation to have human resources of the right quantity and quality to meet the current requirements.
- It helps an organisation to have the required human resources to meet future demand.
- Increased motivation and productivity when HR with the right talent is selected to the company.
- Reduced staff turnover. This has implications for cost, operational efficiency and profitability.

(Total: 30 marks)

SECTION 2

Answer 03

Relevant Learning Outcome/s:
2.1 Introduction to management
2.3 Types of managers
2.5 Managerial skills

The four main tasks to be performed by managers in the management process can be listed as **Planning, Organising, Leading and Controlling**.

Planning involves setting performance goals and devising strategies to achieve them (i.e. what to achieve and how to achieve).

Organising follows planning and involves assigning tasks, grouping tasks into departments, and allocating resources.

Leading is the use of influence to motivate employees to achieve the organization's goals.

Controlling involves checking progress against plans. It is concerned with monitoring the progress of work, keeping the organization on track towards meeting its goals and making corrections, as necessary.

(b)

Senior management / top level management – they are responsible for overseeing the entire organization, developing its strategy and making decisions on the direction of the business.

Middle management – responsible for units within an organisation. They are accountable to senior management for their unit's functions.

Junior management / lower level management– responsible for controlling and directing of the employees and achieving the desired quality and quantity of production.

(c)

Technical Skills (Knowledge, competency, and proficiency in a specific activity)

Human Skills (Ability to work with people, communication and participate in teams)

Conceptual (Ability to work with ideas and concepts)

(Total 10 marks)

Answer 04

Relevant Learning Outcome/s:
4.6 Monetary policy and fiscal policy

(a)

Monetary policy is the macroeconomic policy implemented by the Central Bank.

It is the government policy on the **money supply, interest rates, exchange rates and the availability of credit.**

- Aggregate demand and the level of economic activity.
- Savings and investments in the economy.
- The distribution of income.

Government revenue collection is made through taxes. According to Keynesian economics, when the government changes the levels of taxation and governments spending, it influences aggregate demand and the level of economic activity. Fiscal policy can be used to stabilize the economy over the course of the business cycle.

(b)

- Both monetary and fiscal policies attempt to attain the macroeconomic policy objectives by influencing aggregate demand.
- In order to stimulate economic growth it is important to ensure that expansionary fiscal and monetary policies are implemented.
- Expansionary fiscal policy refers to the reduction of taxes and increasing government expenditure which would lead to an increase in aggregate demand and thereby an increase in rate of economic growth.
- To reinforce the impact of expansionary fiscal policy, expansionary monetary policy should be implemented.
- Expansionary monetary policy refers to reduction of interest rates and expansion of money supply to increase the aggregate demand in the economy.

(Total 10 marks)

Answer 05

Relevant Learning Outcome/s:
5.2. Organisation and organisation structure

(a) Functional Form

Merits	Demerits
<ul style="list-style-type: none">• Clear division of work - avoids duplication• Responsibility is clear cut• Specialization enhances efficiency• Functional expertise	<ul style="list-style-type: none">• Sub-optimisation – Each manager is concerned only about his dept. goals & not about corporate goals• Unhealthy competition• Narrow specialization

Geographic Departmentation

Merits	Demerits
<ul style="list-style-type: none">• Local decision making – closer contact between co. & its customers and suppliers• It may be easier to set up area offices than to service markets from one location• It may be more cost effective to manufacture in the regional centres	<ul style="list-style-type: none">• Duplication & possible loss of economies of scale• Inconsistency in standards may develop across different areas• Inconsistency in methods may develop across different areas.

(b)

- There is physical and mental limitation in terms of the workload that could be handled by Suresh as an owner of the company.
- Suresh will save a lot of time after delegation of his work to managers and he can concentrate more on planning and taking strategic decisions to develop his business.
- Delegated authority contributes to job satisfaction and development of lower level employees. (delegates)
- The increasing size and complexity of Extra (Pvt) limited calls for both managerial and technical specialization.
- Delegation shortens the chain of decision making and brings decisions closer to the situation that requires them.

(Total: 10 marks)

Answer 06

Learning Outcome 6.7 Production concepts in businesses

(a)

No. of Workers (1).	Total Prod. in Units (2).	Average Production in Units. (3) = (2) ÷ (1)	Marginal Prod. In units (4) = (ΔP/ΔW)
1	10	10	
2	22	11	12
3	36	12	14
4	44	11	08
5	50	10	06
6	54	9	04
7	52	7.4	-2

- (b) The law of diminishing marginal returns states that “when equal units of a variable factor are added in succession to a fixed factor, then beyond a point, the returns to that factor will begin to diminish.”
- (c) Diminishing returns set in after the 3rd worker is employed.
- (d) Marginal product will be less than the average product when average product is falling and greater than average product when average product is rising. It intersects the average product at the point of maximum output.

(Total 10 marks)

SECTION 3

Answer 07

Learning Outcome :

3.9 – competitive forces

3.11- Theoretical dimensions of market structures

Number of firms - There are a few large mutually interdependent firms in the industry. More specifically there are only 5 firms with significant market shares in the industry.

Nature of the product – The firms in the industry differentiate their products by offering various types of products and services under different product packages such as postpaid, pre-paid, etc as well as through pricing (i.e. monthly rental) and the features that are provided.

Barriers to entry – There are significant barriers to entry in the mobile telecommunication industry such as regulatory barriers, need of a high investment, significant switching costs and absence of telephone number portability.

Price– It is possible to see price rigidity in the mobile telecommunication industry meaning the prices are stable for a long period of time. As a result they mainly compete through non-price strategies.

(b) (i)

Barriers to entry refer to anything that prevents new firms entering an industry.

These can take several forms, ranging from legal/regulatory barriers to technological and economic barriers as well as barriers caused by existing players in the industry.

(ii)

- Legal/regulatory barriers - It is mandatory to obtain a license in order to operate as a mobile telecommunication service provider.
- Economic barriers - It is required to have a significant investment in order to initiate and operate as a mobile telecommunication service provider in the industry.
- Technological barriers - Significant switching costs that have to be incurred by consumers moving from one operator to another
- Technological barriers - Absence of telephone number portability across service providers also act as an entry barrier.

(c)

(i) If price is the basis of competition, it is known as price competition and if the basis is anything other than price it is known as non-price competition. E.g. Differentiation, advertising etc.

- Differentiation of the product or service offered
- Heavy advertising
- Sales promotion
- Creating brand loyalty

(d)

- The threat of new entrants – company Y needs to critically consider the facts that act as barriers to entry and the possible response of existing competitors to the new entrant to fully understand the threat to new entrants.
- The threat of substitute products or services – this is the threat coming from similar products which satisfy the same customer needs.
- The bargaining power of customers – customers want better quality products at lower price. Satisfying this want might force down the profitability of suppliers in the industry.
- The bargaining power of suppliers - suppliers can exert pressure for higher prices.
- The rivalry amongst current competition in the industry – the intensity of competitive rivalry within an industry will affect the profitability of the industry as a whole.

(Total: 20 marks)

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