

CA



THE INSTITUTE OF
CHARTERED ACCOUNTANTS
OF SRI LANKA

SUGGESTED SOLUTIONS

KB5 – Business Value Creation

December 2016

Answer 01

Relevant Learning Outcome/s:

1.3 - Prioritise organizational stakeholders in terms of their impact on business (stakeholder mapping based on the power/interest matrix)

Study text Reference : pages 18/19

- (a) Stakeholder mapping is a method of understanding the interest and power of different stakeholders and indicating how management should respond to the concerns of each stakeholder group.

		Level of interest	
		Low	High
Level of Power	Low	A	B
	High	C	D

- (i) **Major shareholder/major customer**

High power, High interest (D)

They are the owners of the business who can make decisions. They can decide whether to go ahead with setting up the estate and factory, or not. They also have a high interest as this project will have an impact on profits, and the protests that are taking place can bring about disrepute to the business.

- (ii) **Citizens of Lakeside District/most of the employees**

Low power, High interest (B)

Given that the business will have an impact on their lives, they have a high interest. However they might not possess sufficient power to influence the decision.

- (iii) **Government**

High power, Low interest (C)

The government might decide to support the business and help them set up operations in Lakeside District. At the same time, given that protests have started they could reverse this. Thus they possess high power. In terms of interest, it might not be very high, as the government cannot only be interested in one business. However once the protests are over, the government might become interested in the project too, and make decisions accordingly.

- (iv) **Green Friends**

High Power, Low interest – (C)

Given that this is a global NGO they might have some power to influence the government and even the owners/managers of the business. However as of now, their interest is low but if citizens of Lakeside District are successful in getting their support, they might develop interest and thus influence stakeholders such as the government to act against setting up of the business in Lakeside District.

(6 marks)

(b)

- **Major shareholder/major customer** – key players as they have high interest and high power. Management has to consider their views when going ahead with the decision of setting up operations in Lakeside District.
- **Citizens of Lakeside District** – need to be kept informed as they have high interest and low power. Keeping them informed may help to reduce the protests against the business as these protests could be due to a lack of information. However if they do manage to obtain the support of Green Friends, they might have to be kept satisfied and could even become key players.
- **The government** – might have to be kept satisfied as they have high power but low interest. However with the protests, they might develop high interest, in which case they will become key players too.
- **Green Friends** – have the power to influence the public and other relevant authorities in relation to the environmental issues caused by the business. Therefore they should be satisfied by providing relevant information.

(4 marks)

(Total: 10 marks)

Answer 02

Relevant Learning Outcome/s: 2.2 Inventory management and warehousing
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Study text Reference : pages 42-48

(a)

Per the details given in the case, the main cause of customer complaints received by Goodies.lk seems to be stemming from an inadequate inventory management system. A good inventory management system would help Goodies.lk to overcome the current issues.

Costs of the current approach to inventory management adopted by Goodies.lk are given below.

- (i) High working capital investment resulting in high finance costs
- (ii) Cost of maintaining high inventory (e.g. storage, security, insurance)
- (iii) Quality of the product might be affected if it is in stores for a long period
- (iv) Creating customer dissatisfaction and developing a bad image for the company

(4 marks)

(b)

Goodies.lk can consider implementing a just-in-time (JIT) ordering system and a warehouse management system (WMS) to overcome prevailing problems.

JIT ordering system

A JIT system involves just-in-time purchasing, where items are purchased from suppliers and delivered at the exact time they are required to be sold to a customer.

In JIT the company will maintain minimum or no stocks, but arrange for the suppliers to deliver the goods once an order is placed. With the advancement in IT, Goodies.lk can place the order directly with the suppliers through an online portal and agree with them to deliver the goods to the warehouse within 24 hours. Then they can dispatch the goods by the second day so that it would reach the customer on the same day, or latest by the third day. This will enable Goodies.lk to reduce inventory holding costs, and the holding of non-moving inventory. Further by long-term agreements, the company can negotiate special discounts with the suppliers.

If the ideal situation can be achieved, it will be a core competence to the business and will help them to achieve a competitive advantage, as they are now able to operate with lower warehousing costs.

Warehouse management system (WMS)

A WMS is an IT system for controlling the movement of stored goods within a warehouse and processing associated transactions such as receiving goods, putting them away, picking them for dispatch and shipping them. A WMS provides a standardised system for handling goods once they are received at the warehouse. There may be an independent handling system for each inventory type. An efficient WMS will help Goodies.lk to:

1. Minimise the cost of holding unnecessary inventory at the store. Goodies.lk has a lot of non-moving stock in the warehouse at present, and using a WMS can assist the company to make the best use of the storage space available
2. Model the physical storage facility that would enable them to store the goods in the most efficient way. For example, store the fast moving goods near the exit. Store goods that move together closer to each other. This would make the picking and packing process easier and more efficient. Goodes.lk currently has difficulty in locating goods in the warehouse, therefore by using a WMS they could improve their efficiency.
3. Have an automated link between order processing and logistics management. RFID or barcoding can be used to track the products in the warehouse so that Goodies.lk will be able to satisfy customer orders without any delay.

(6 marks)

(Total: 10 marks)

Answer 03

Relevant Learning Outcome/s:

3.2 Product design and process selection (new product development)

Study text Reference : pages 73-75

(a)

- By moving from a leader strategy to a follower strategy, Cooler can lower the product design and development costs. If not, they have to produce unique products to gain a competitive advantage.
- Leaders always need to invest heavily in R&D and as a result in the short-term their profitability is low. Followers on the other hand have less emphasis on R&D.
- Reduces uncertainty in relation to sales demand and market size, since they are providing their products to an existing market. Therefore, cost of sales promotion will be lower.
- Free from obtaining regulatory approval where required.

(3 marks)

(b)

1. Idea generation– the idea is suggested for a new product and it could be from anywhere in the organisation.
2. Idea screening– initial screening to decide whether the idea is a good one or not. This might involve identifying the target market, actual size of the market and its growth potential, technical feasibility, profits and so on.
3. Concept development and testing– the product concept is developed in more detail (cost of the product, prototype etc.), and is tested on a small group of prospective customers to see how they react to it (what features matter the most to them etc.)
4. Business analysis – carry out a financial analysis of the potential returns, decide on the sales price, estimate sales, revenue, profits and breakeven point.
5. Beta testing and market testing– produce a physical prototype and arrange private testing. Beta testing is where the new product is tested by real customers in a real user environment prior to a market launch. Interviews are then conducted to obtain customer views and make adjustments to the product if needed.
6. Technical implementation– plan and establish production and logistical arrangements.
7. Launch product– supported by an intense selling and marketing campaign. 8. Post launch review – review the price if needed.

(7 marks)

(Total: 10 marks)

Answer 04

Relevant Learning Outcome/s:

6.2 - Information technology infrastructure in organisations
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Study text Reference : pages 275-276

(a) Bestsellers can improve the value chain by adopting new technology as follows.

Improving value through primary activities

Inbound logistics – Bestsellers can use inventory control and systems such as material requirements planning (MRP), enterprise resource planning (ERP) and just-in-time purchasing. These make it easy to record and monitor movement of books and also order them. Further, suppliers could be given access to the inventory system so that they can themselves see if they need to bring in more stocks.

Operations – generally, organisations use IT for robots, process control, machine tool control, computer aided manufacturing (CAM), and computer integrated manufacturing (CIM) and enterprise resource planning (ERP). However as Bestsellers is involved in selling books, IT can be used to record all movements and transactions involving purchase, storage and sales of books, and to also easily obtain data on what books sell more (which could then be purchased).

Outbound logistics – can be improved by using a warehouse management system for the control of warehouse operations and technology such as RFID tagging. Even though Bestsellers does not have much involvement with outbound logistics, it can use an automated order processing system to increase the efficiency of delivering orders to customers.

Marketing and sales – Bestsellers can use an electronic point of sales system (EPOS) to record sales and update records. Further they can use technology for customer relationship management (CRM) and also introduce an online purchasing system.

Services – customer databases allow organisations to sell aftersales services and deal with customer complaints and queries. Accordingly customers can easily give comments and even place orders for other books using Internet facilities. If payments could be made online it would further add value. Use of email would ease communication within the organisation as well as with outside parties such as suppliers and customers.

Improve the value through secondary activities

Firm's infrastructure – includes activities relating to general management, accounting, finance and strategic planning. Therefore by using accounting systems and network technology (e.g. intranet) Bestsellers can maintain accurate records. Additionally, they can trace debtors and creditors easily. General management could also become more efficient due to proper coordination through integrated systems such as Enterprise Resource Planning (ERP).

HRM – includes all activities relating to attracting and retaining an appropriate workforce. Bestsellers can maintain a skills database by using IT facilities and use IT application for staff planning. Further they can get an IT system to maintain automated personnel scheduling.

Technology development – includes all activities relating to R&D, product and process improvements. Bestsellers can carry out electronic market research using advanced IT applications to decide the trends of demand for different categories of books.

Procurement – includes all activities relating to purchasing of RM, machineries and supplies. Bestsellers can use IT to make automated purchasing decisions and link suppliers with EDI. Ultimately they can go for an e-procurement system.

(7 marks)

(b) In order to improve the value chain of Bestsellers using IT application, the following IT infrastructure will be needed.

Standalone computers – used on their own or connected to other devices such as printers, scanners (without connection to other computers).

Networks – a network is a number of computers linked to each other so that they can communicate with each other and share the same files, software and peripheral equipment (such as printers). Local area networks link computers together with local cabling. Wide area networks cover a wider geographical area and link computers through either dedicated lines or via the Internet.

Connected devices – include connecting dumb terminals, computers and printers. A network may also use other devices for input and output of data, such as barcode readers, plastic swipe cards etc.

Internet, intranets and extranets – intranets are within the organisation, whilst extranet access can be given to selected people outside the organisation.

Centralised and decentralised processing – depending on the degree of IT adoption by Bestsellers, it can apply a centralised or decentralised processing system on one of the network's larger computers. It would then be possible to access processed data from any part of the network when required.

(3 marks)

(Total: 10 marks)

Answer 05

Relevant Learning Outcome/s:

5.3 Talent attraction and retention

Study text Reference : pages 198/205

(a)

Advantages of interviews

- **Adaptability** – interviews can be adapted to the situation of candidate. Therefore, based on the background of the candidate, the interviewer can change the questions, interview style and atmosphere.
- **Face to face discussion** – interviews provide the opportunity to exchange information with candidates to assess their suitability for the job.
- **Two-way communication** – in the interview, it is possible to provide the opportunity to candidates to ask any questions to clarify the job and its responsibilities.
- **Ability to test proficiency** – interviews allow to test the proficiency of spoken English.
- **Test culture and discipline** – interviews allow to test the cultural background and discipline of the candidates.

Disadvantages of interviews

- **Scope** – interviews may be too brief to get to know the candidate in depth and make an accurate prediction of work performance.
- **Artificial situation** – candidates may be on their best behaviour and not show their true personality. Or on the other hand, they might be too nervous and not perform to their true potential.
- **Halo effect** – interviewers can make a general judgment on a single obvious attribute (e.g. being well dressed or well spoken)
- **Contagious bias** – the interviewer may change the behaviour of the applicant by unintended suggestions (the applicant might be led by the wording of the question or non-verbal cues).
- **Incorrect assessment** – qualitative factors such as motivation, honesty or integrity are very difficult to define and assess objectively at an interview.
- **Inexperienced interviewers** – if interviewers lack experience with selection, they may fail to reach a good decision about which applicant to select for the job.

(6 marks)

(b)

Hygiene factors – these relate to conditions at work, such as working conditions, job security, and interpersonal relations at work, supervision, company policies and pay. Hygiene factors cause dissatisfaction in the individual if his/her needs are not met. They do not motivate the individual to perform better.

Motivator factors – these satisfy the needs for fulfilment at work, and include factors such as challenging work, career advancement (or the prospects of it), a sense of achievement, recognition from bosses and colleagues, responsibility, and additional pay. Employees may not be satisfied only with motivator factors. First they will eliminate the dissatisfaction based on hygiene factors and then they may be satisfied with motivator factors.

(4 marks)

(Total: 10 marks)

SECTION 02

Answer 06

Relevant Learning Outcome/s:

- 4.3 Managing Products and brands.
- 4.4 Pricing strategies
- 4.5 Distribution and channel management

Study text Reference : pages: 133-145

- (a) Sunshine is a strong detergent and is low priced. It appears to be positioned based on the fact that it addresses the needs of a strong cleaning liquid, which is also very affordable. Thus the present positioning is based on strength and low cost.

However, the new product is not focused on strength nor price, but on the fact that it is safe for users and is a green product. Thus the values of the Sunshine brand do not match this new product. Therefore this product could have a different brand name. This new brand should be positioned in a way that highlights its benefits (e.g. health and safety, environmentally friendly), which are not offered by other products.

Accordingly, Sunshine can hold their present customer base in rural areas and attract urban customers to the new brand. Thus they can manage the declining trend of their present brand in urban areas.

(6 marks)

- (b)

Requirements for successful brand positioning	
Relevance	The branded products should be positioned in a way that has meaning for consumers and meets their needs.
Clarity	The 'meaning' of the brand should be distinct, easy to communicate to consumers and easy for them to understand.
Coherence	The same 'image' of the brand should be promoted consistently through all aspects of the marketing mix. For example, a high-quality brand needs to be supported with high-quality products and high prices, and possibly exclusive distribution.
Patience	It can take a long time to establish a successful brand.

(4 marks)

- (c) The promotional mix is the combination of activities used by marketing managers to promote a product or service. Sunshine can apply the following elements of the promotional mix to promote the new product line.

Advertising – this is a well-established method of marketing products. There are different advertising media: television, cinema, radio, newspapers, magazines, billboards, posters, website advertising etc. which could be applicable to the new brand.

Sales promotion – could be used to stimulate purchasing and sales. The objectives are to increase sales, inform potential customers about new products, and create a positive business or corporate image. The company can offer coupons, special discounts, free samples, organise contest etc.

Public relations – PR activities enable an organisation to influence a target audience to create a favourable image of the company and its brands. The company can organise press conferences and send press releases regarding the specialties of the new product range. At the same time, they can become involved in different CSR programmes.

Direct marketing – involves sending sales promotion material (such as brochures), directly to potential customers. The marketing material may be sent by post or by email.

Personal selling – by sales representatives (“salesmen”), either through face-to-face meetings with potential customers or by telephone. In this situation, personal selling can convince dealers about the new brand.

Sponsorship – involves providing financial support for sporting or other events. The association of a sponsor's name with an event will be help to promote the brand. The company can sponsor a national level sporting or education event during the introduction stage.

Point-of-sale displays – refer to displays of a firm's products at a place, usually within a retail store, where customers are likely to see them. They often involve a special price promotion, with the intention of tempting shoppers to buy the product.

(6 marks)

- (d)

Pricing strategy is concerned with deciding the price level at which a company should try to sell its products. There are various pricing strategies that a company may select for its product. A price skimming strategy is more suitable for this new product line, as it is a green product which has minimum harm for users and the environment and is also made from internationally approved ingredients. The product is focused on health and safety of professional consumers too. Therefore the company can charge a high price for it.

Method of distributions

A manufacturer can choose to distribute products using one of the following ways:

1. Extensive distribution

2. Selective distribution
3. Exclusive distribution
4. Direct distribution

Extensive distribution – The manufacturer seeks to sell the goods through as many retailers as possible in order to obtain 'saturation coverage' of the market. For this method of distribution, it is necessary to use a large number of wholesalers and retailers; otherwise the costs of distribution may become excessive.

Following extensive distribution could harm the new brand image as it will be available with many retailers that would restrict the ability of sleek to communicate its new brand position adequately.

Exclusive distribution – The manufacturer gives exclusive distribution and selling rights to one organisation, possibly globally, but more usually within a specified geographical area.

Exclusive distribution with a limited number of intermediaries could limit the ability to maximise the sales potential and not suitable for the company.

Direct distribution – The manufacturer sells directly to consumers through online sales and the Internet. But online marketing may not be successful with a detergent product range.

Selective distribution – The manufacturer uses a limited number of intermediaries to distribute the goods and sell them to the end customer.

Therefore following a selective distribution method using leading supermarket chains such as Keells, Cargills, Arpico, Laugfs and other modern trade outlets may be more suitable for the new product line. It will be able to reach selected customers in urban areas.

(Total: 25 marks)

Answer 07

Relevant Learning Outcome/s:

5.7 Managing culture and change
7.4 Formulation of business level strategy
7.7 Monitoring and control

Study pack reference: pages 249/351/365

(a) Lewin's Three-Stage Model

Kurt Lewin, a psychologist, developed a model for change management in the 1940s. He suggested that successful change can be done using a three-stage process.

Unfreeze – this is the process of finding a way to get people (both individuals and groups) to end their resistance to change. This is achieved by finding ways to strengthen the driving forces for change or to weaken the restraining forces that resist change. Therefore the top management should explain the benefits of change, pointing out the negative consequences of not changing and make staff understand the need for change.

Movement – This stage involves making the change. It includes not just making the changes to operations and activities, but making changes to the thoughts, feelings and behaviour of the people affected. This could be done by giving clear instructions to staff about the new patterns of behaviour and providing training in the new procedures. Clear communication is necessary so that the staff understand what needs to be done.

Re-freeze – After the change has occurred, there may be a tendency for people to revert to 'old ways' after a while, and for the changes to become lost and forgotten. If employees have any problems, the management must quickly sort them out, so that staff is encouraged to follow the new system. The organisation should provide additional rewards to encourage staff to follow the new procedures.

(6 marks)

(b)

Kim and Mauborgne proposed 4 steps to implement the blue ocean strategy in an organisation using the “four action framework”.

Reduce: *Which factors should be reduced below the industry standard? Which factors yield little or no competitive advantage?*

Plastex can reduce the cost of packaging as it seems to be above the industry standard and does not seem to provide a competitive advantage.

Create: *Which factors should be created? (i.e. the ones that industry has not offered before)*

Recycled products could be a new feature created by Plastex, which the industry doesn't offer at the moment. Since there is great awareness about sustainability and the importance of recycling among the general public now, this can be seen as a valued innovation.

Raise: Which factors should be raised above industry standard?

Plastex can increase their spending on R&D and provide new products continuously to the market, creating the brand image of an innovative company. Local companies such as Ceylon Biscuits have done this quite successfully.

Eliminate: Which factors, taken for granted, should be eliminated because they add little or no value.

Plastex can perhaps eliminate the internal transport fleet and use a third party transport provider to manage their transport fleet. This may reduce the cost as they are clearly spending more than the industry average on transportation.

(9 marks)

(c)

When strategies have been selected and implemented, their progress and performance should be monitored. In this regard, the organisation can measure financial performance as well as non-financial performance.

Financial performance is a measure of what has happened in the past, but past financial performance is not necessarily a good guide to financial performance in the future. It is important to measure financial performance of a given strategic plan as it enables the management to:

- Compare actual financial performance of the previous year with the targets for performance in the new business plan.
- Produce new forecasts for the remainder of the business plan period, and assess whether the organisation still expects to achieve its financial objects by the end of the period.

At the same time, non-financial performance such as the achievement of targets for customer satisfaction, quality, product innovation and so on, are often a guide to the future. Last year's non-financial performance may be a good indicator of what is likely to happen in the future, and how this will affect the organisation's long-term objectives.

(6 marks)

(d) **Indicators of financial performance**

- Cost of goods sold as a percentage of sales
- Sales and distribution overheads as a percentage of sales
- GP margin
- NP margin

Indicators of non-financial performance

- Percentage of products made using recycled plastics (this is an important indication of whether the company is moving towards the new direction set)
- Amount of new products introduced during the year (since Plastex is on a journey to create a reputation for being an innovative company, it is important to measure the same)
- Degree of customer awareness about the new concept (this is an important indication of whether customers are educated about the new concept)

(4 marks)

(Total: 25 marks)



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