

CA



THE INSTITUTE OF
CHARTERED ACCOUNTANTS
OF SRI LANKA

SUGGESTED SOLUTIONS

KE5 – Commercial Insight for Management

September 2019

SECTION 1

Answer 01

1.1

Learning Outcome/s: 1.4.1

Define 'vision', 'mission', 'goals' and 'objectives' of business organisations

Study text reference: page 19

Correct Answer: D

1.2

Learning Outcome/s: 2.4.1

Identify the key roles played by a manager in an organisation including managerial roles by Mintzberg.

Study text reference: page 62

Correct Answer: A

1.3

Learning Outcome/s: 2.9.1

Identify the differences between economic profit and accounting profits

Study text reference: page 91

Correct Answer: C

1.4

Learning Outcome/s: 3.5.1

Identify the factors which influence market demand and supply

Study text reference: page 135

Correct Answer: B

1.5

Learning Outcome/s: 3.11.1

Explain characteristics of perfect competition, monopolistic competition, monopoly, oligopoly and their impact on businesses.

Study text reference: page 171

Correct Answer: D

1.6

Learning Outcome/s: 3.12.1

Explain how businesses determine the optimum output, price and profit in the short and long run in different markets

Study text reference: page 216

Correct Answer: A

1.7

Learning Outcome/s: 4.7.1

Identify financial markets, financial intermediation and the benefits to business

Study text reference: page 308/309

Correct Answer: B

1.8

Learning Outcome/s: 4.9.1

Discuss the nature of modern development and their impact on business

Study text reference: page 253

Correct Answer: A

1.9

Learning Outcome/s: 6.11.1

Identify the concepts of "Segmentation", "Targeting", and "Positioning" (STP) and the "Marketing Mix" (4Ps)

Study text reference: page 453

Correct Answer: C

1.10

Learning Outcome/s 6.16.1

Identify the basic concepts of change management

Study text reference: page 548

Correct Answer: D

(2 x 10 = Total: 20 marks)

Answer 02

2.1

Learning Outcome: 1.2.1 Identify the value offerings made by business organisations, in serving their customers (including goods, services, events, person, experience, place, properties, information, organisation and ideas)
Study text reference: page: 13
<ul style="list-style-type: none">• Tangible attributes: availability and delivery, performance, price, design, packaging, the range of complementary products in a line, availability of accessories and suppliers for product use or maintenance.• Intangible attributes: Image, perceived value, ease of use, convenient storage, product's aesthetic qualities, sentimental value, trendiness, impressiveness to friends, modern style.

2.2

Learning Outcome/s: 2.1.2 Explain the process of management
Study text reference: page : 72
Efficiency refers to getting the maximum output from the least amount of inputs or resources. Effectiveness is described as doing the work activities that will result in achieving goals. Efficiency is linked to resource usage while effectiveness is linked to high level of attainment of goals. Management process strives for low resource waste (High efficiency) and high goal attainment. (High effectiveness).

2.3

Learning Outcome/s: 2.6.2 Identify the scope of business economics.
Study text reference: page 82
<ul style="list-style-type: none">• Centrally planned economy – the decision and choices about resource allocation are made by the government.• Free market economy – the market forces of demand and supply and working of the price mechanism.• Mixed economy – both government (public sector) and market forces (private sector)

2.4

Learning Outcome/s: 3.3.2

Discuss the importance of customer value and customer satisfaction with special reference to the role of an accountant in the organisation.

Study text reference: page 187/188

- (i) CSFs :
- Quality of the foods
 - High level of customer service
- (ii) Appropriate KPI's may relate to:
- The speed of delivery. (Average time taken by one waiter to cater to a guest)
 - The number of repeat customer visits/ orders from the existing clientele
 - Scores achieved in customer satisfaction surveys
 - Number of customer complaints
 - Number of customer references in the social media platforms
 - Number of awards won in relation to hospitality management

2.5

Learning Outcome/s: 3.4.1

Identify the behaviour of rational consumers using cardinal and ordinal utility theories.

Study text reference: page: 110

- (a) The cardinal utility approach suggests that consumers are able to measure absolutely, the satisfaction that they derive from consumption of a given quantity of a commodity. The ordinal utility approach suggests that consumers cannot measure utility absolutely. Instead they rank different commodities or different baskets of commodities to choose the best one.
- (b) The ordinal approach is preferred in explaining consumer behaviour as it ranks the satisfaction by assigning numeral values to the level of satisfaction.

2.6

Learning Outcome/s: 4.1.1

Explain the main dimensions of the general environment (PEST factors) and their influence on business.

Study text reference: page 235

- To achieve flexibility in business planning: Have a simple management structure that drives immediate communication of change.
- Awareness of risks inherent in dynamic environmental conditions: importance of conducting a proper risk analysis, have a Business Continuity planning (BCP) and contingency plans built into the future business strategy.

2.7

Learning Outcome/s: 4.5.3

Discuss the factors affecting demand and supply of foreign currencies.

Study text reference: page: 303

Expenditure switching policy

- A depreciation of the domestic currency/ devaluation of the domestic currency
- Direct measures to restrict imports such as tariffs or impose import quotas or tightening of exchange control regulations

Expenditure reducing policy

- Domestic deflation to reduce aggregate demand in the domestic economy – reduction of government expenditure, curtailment of government investments etc.

2.8

Learning Outcome/s: 4.6.2

Discuss the impact of monetary and fiscal policies on business

Study text reference: page : 294

Expenditure decisions by the government will affect suppliers to the government (e.g. suppliers of machinery).

The taxation policy determines consumer purchasing power which affects sales revenue also. Taxes on company profits and tax allowances affect the after tax returns on investments.

If the government kept its own spending at the same level, but reduced level of taxation, it would stimulate demand in the economy, firms and households would have more of their own money, after tax for consumption or saving/investing.

2.9

Learning Outcome/s: 5.1.1

Identify the planning process and advantages of planning to an organisation

Study text reference: page: 324

- The future is unknown and surprises could always occur and if plans are too detailed might not be able to cope with uncertainties
- Lack of creativity can prevent identification of opportunities
- Fear of possible adverse consequences of taking decisions can lead to the management avoiding planning
- Inertia caused by excessive bureaucracy hindering change
- Focus on current developments
- Negativity
- Insufficient resources
- Poor communication
- Resistance

Learning Outcome/s: 6.4.1

Identify the steps involved in production capacity planning.

Study text reference: page : 409

There are different ways of planning for capacity.

- **A level capacity plan** – is a plan to maintain activity at a constant level over the planning period and to ignore fluctuations in forecasted demand. Staffing and other resource level are kept at a constant.
- **A chase capacity plan** - The plan is the opposite to a level capacity plan. It aims to match capacity to forecasted fluctuations in demand.
- **A demand management plan** – the aim is to reduce peak demand by switching to off-peak periods.
- **A mix of the above three types of plan (mixed plans)**- planning is often a mixture of level capacity planning, chase demand planning and demand management planning.

SECTION 02

Answer 03

Learning outcome : 4.4

Role of inflation

Study text reference: page: 278/283/285

(a) The high rate of price inflation considered to be harmful and undesirable in relation to the following macroeconomic variables.

(i) **Balance of payments**

- The transaction with other countries, which are recorded in the balance of payments (BOPs), get adversely affected if there is a high inflation rate.
- A high rate of inflation in the domestic market makes domestic goods unattractive to the foreign buyers and therefore, reduces the demand for exports.
- Due to high domestic prices, residents prefer to buy foreign goods which results in an increase in imports.
- The results of falling exports and increasing imports will cause an adverse disequilibrium in the BOP.
- This adverse situation may lead to a steep decline foreign exchange reserves and possibility of default on the external payment front.

(ii) **Economic Growth**

- Higher inflation means lower consumption. There is lesser demand for goods and services. This negatively affects production and slows down economic growth.
- When there is high inflation, the cost of production goes up and it discourages production in the economy. Therefore economic growth will slow down.
- When there is high inflation, interest rates will go up and people will be encouraged to save more and more. This will discourage investment and as a result it will have an impact on economic growth.

(b) Negative consequences of unemployment are,

- Loss of output- if labour is unemployed, the economy is not producing the optimum output. Thus, the total national production is less than it could be.
- Loss of human capital – the unemployed labour will gradually lose its skills, because skills can only be maintained while working.
- Increasing inequalities in the distribution of income – the poor get poorer and there might be political instability.
- Social costs – unemployment brings social problems of personal suffering and distress, frauds etc.
- Increasing burden of welfare payments.

(c) The policies should be focusing on training the labour force to enhance labour productivity. The government can establish various training centers to provide training to enhance the skills and competencies of its labour force. So, that they can contribute to increase the production in various sectors and this in turn helps to create more job opportunities.:

- Introduction of new technology
- Encourage research and development
- Provide incentives for innovation, granting loans for self-employment.
- Offering grant assistance to employees in key regional areas
- Encouraging labour mobility- reimbursement of relocation expenses, improving the flow of information on vacancies.
- Abolishing minimum wage regulations, where such regulations exist.
- Abolishing closed shop agreements

(Total: 10 marks)

Answer 04

Learning Outcome/s : 5.4/5.5

5.4 Nature and scope of leading as a management function

5.5 Nature and scope of control

Study text reference: page 368/372-374,375

- (a) Factors which might motivate employees of any business organization, according to Herzberg's two factor theory are,

Hygiene factors – company policy and administration, salary, the quality of supervision, interpersonal relations, working conditions, job security etc.

Motivator factors – status, advancement, recognition, responsibility, challenging work, a sense of achievement, growth in the job

- (b) Advantages of having an effective communication system in the organization:

- Communication is required for planning, co-ordination and control of business organizations.
- Communication is fundamentally linked to managerial performance.
- Management decision making requires data/ information. That information has to be communicated. Managers are at the hub of a communication system.
- Interdepartmental co-ordination depends on information flows.
- Individual motivation and effectiveness depends on communication.
- Best ideas/ creative suggestions or the best plans can't take shape without communication.

- (c) Steps that a company could take to clear up the misunderstandings are,

- Use feedback/ Confirmation- managers should get feedback/ confirmation both verbal and non-verbal
- Issuing a message in more than one form
- Reporting by exception should operate to prevent information overload on managers
- Train managers to express themselves clearly and concisely
- Build up interpersonal trust between managers and direct subordinates
- Use simple language whenever possible.
- Create an active listening culture/ working environment

(Total: 10 marks)

Answer 05

Learning Outcome/s: 6.7.1/6.7.2/3.12.1

6.7.1 Define short run and long run production concepts and related production measurements (total production, average production, marginal production), using graphical means.

6.7.2 Explain the "Law of Diminishing marginal Returns" and its impact on businesses.

3.12.1 Define Human Resource Management (HRM)

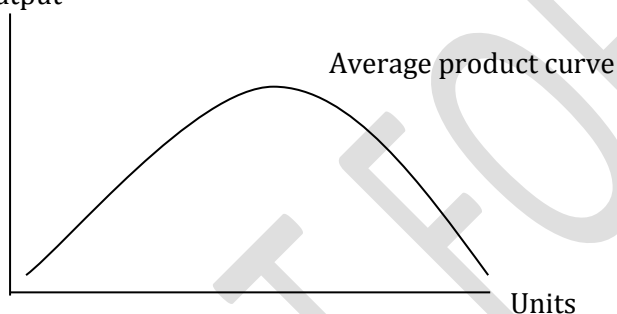
Study text reference: page 425,427,211

(a)

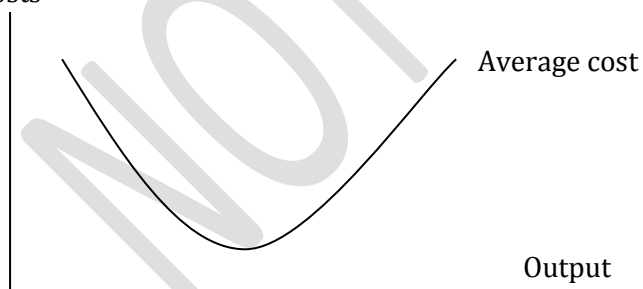
Workers	Average Product	Total product	Marginal Product
1	9	9	-
2	10.5	21	12
3	10.67	32	11
4	10.5	42	10
5	10.2	51	9

(b)

Output



Costs



- Rising productive efficiency leads to falling unit costs
- On the other hand, diminishing productive efficiency leads to rising unit costs.
- The law of diminishing marginal returns implies that productive efficiency initially rises and then falls in the short run.

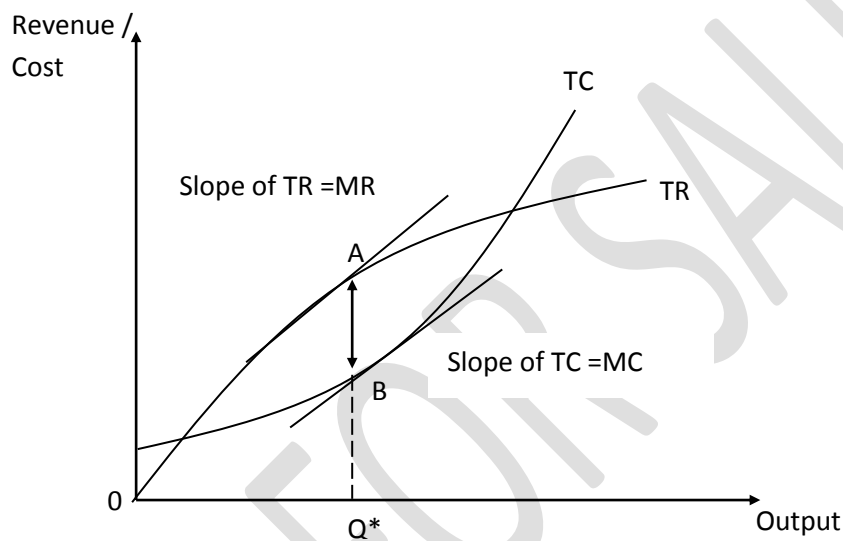
- (c) There are two approaches in determining the profit maximizing output level; namely;
- 1) Total Approach
 - 2) Marginal Approach

The profit maximizing output level where the total revenue exceeds the total costs by the greatest amount.

As shown in the diagram the profit maximizing output level occurred at Q^* where the gap between TR and TC is the largest.

Under the marginal approach the profit maximizing condition is; $MR = MC$
The first derivative of TR is MR and the first derivative of TC is MC.

The diagram;



(Total: 10 marks)

Answer 06

Learning Outcome/s: 6.12

Nature and scope of human resource management

Study text reference: page 503/504/511

(a) Advantages of having a performance based incentive scheme

- Employees' efforts and attention are directed to where it is most needed – performance.
- Commitment and motivation are enhanced. This is particularly important when there are cultural obstacles to improvement.
- Achievement can be rewarded separately from effort, resulting in the recruitment and retention of high quality employees.
- Labour costs are linked to organizational performance.

(b)

- Flexible working hours
- Training
- Working at home/ Virtual office facilities
- Career progression
- The pursuit of green or ethical policies by the company

(c)

Labour preference for leisure (Labour Leisure Model)

Substitution effect: A rise in the wage rate increases the opportunity cost of leisure, as each hour spent not working involves a greater sacrifice in terms of the amount of income foregone. The substitution effect hence leads the individual to substitute work for leisure.

Income effect: the higher wage rate increases the individual's real income, leading the individual to consume more hours. Increased income means that higher income earners can afford to consume more hours of leisure by working less.

(Total: 10 marks)

SECTION 3

Answer 07

Learning Outcome: 3.5/3.6/3.7/3.8

3.5 Demand, supply and market equilibrium in a competitive market

3.6 The concept of elasticity

3.7 Impact of government intervention on competitive markets

3.8 Competitors and their impact on organisations

Study text reference: 124/160/161/179

(a)

Factors affecting the demand function

- Income level of consumers in Country Y
- Price level of other substitutes of sugar in country Y
- Increase in population

Factors affecting the supply function

- Level of wages of the employees in industry
- Price of inputs
- Weather conditions
- Expected rise in the price of sugar
- Changes in technology

(b)

(i) At the market equilibrium, $Q_d = Q_s$

$$200 - 4P = -160P + 8P$$

$$P = 30$$

Equilibrium price is Y dollar 30.00

$$Q_d = 200 - 4P$$

$$= 200 - 4(30)$$

$$= 80$$

Equilibrium quantity is 80 Kg

(ii) The price elasticity of demand at the equilibrium price:

$$\Delta Q / \Delta P * P / Q$$

$$= -16/4 * 30/80$$

$$\underline{= -1.5}$$

(c) At the price of Y\$ 25

$$Q_d = 200 - 4P$$

$$Q_d = 100$$

$$Q_s = -160 + 8(25)$$

$$Q_s = 40$$

$$\text{Excess demand} = 100 - 40 = 60$$

$$\text{Import cost} = 60 * 25 = \text{Y\$ } 1,500$$

(d) (i) **Excess supply = Supply at the Y dollar 40 – Demand at the Y dollar 40**

$$Q_s = -160 + 8(40)$$

$$Q_s = 160 \text{ Kg}$$

$$Q_d = 200 - 4(40)$$

$$Q_d = 40 \text{ Kg}$$

Accordingly, $160 - 40 = 120 \text{ Kg}$

The total cost of the government is: $120 * 40 = \underline{\text{Y dollar 4,800}}$

(ii)

- When the guaranteed price is set above the equilibrium price, quantity supplied will exceed quantity demanded.
- Producer surplus is much higher than the consumer surplus, dead weight loss.

(e)

(i) Key factors to be considered when undertaking competitor analysis are:

- Competitor's goals- the firm as a whole and the business unit. What are the competitor's stated financial goals? The organizational structure and their management styles etc.
- The competitor's assumptions about the industry- what does the competitor believe to be its relative market share etc.
- The competitor's current and potential situation and existing business strategy. – Distribution strategy, products, marketing and selling etc.
- Competitor's capability- core competence and ability to expand.

(ii) Information for strategic uses can be gathered from the following sources:

- Competitor's financial statements
- Information from common customers and suppliers
- Inspection of a competitor's products
- Information from former employers
- Job advertisements

(Total: 20 marks)

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