PAPER 15 - Business Strategy and Strategic Cost Management

Full Marks: 100 **Time allowed: 3 hours**

This paper contains 4 questions. All questions are compulsory, subject to instruction provided against each question. All working must form part of your answer. Assumptions, if any, must be clearly indicated.

1. Read the Case and Answer the following Questions. **[20 marks]**

DD is the India's premier public service broadcaster with more than 1,000 transmitters covering 90% of the country's population across an estimated 70 million homes. It has more than 20,000 employees managing its metro and regional channels. Recent years have seen growing competition from many private channels numbering more than 65, and the cable and satellite operators (C & S). The C & S network reaches nearly 30 million homes and is growing at a very fast rate.

DD's business model is based on selling half-hour slots of commercial time to the programme producers and charging them a minimum guarantee. For instance, the present tariff for the first 20 episodes of a programme is ₹30 lakhs plus the cost of production of the programme. In exchange the producers get 780 seconds of commercial time that he can sell to advertisers and can generate revenue. Break-even point for producers, at the present rates, thus is ₹ 75,000 for a 10 second advertising spot. Beyond 20 episodes, the minimum guarantee is ₹65 lakhs for which the producer has to charge ₹1,15,000 for a 10 second spot in order to break-even. It is at this point the advertisers face a problem - the competitive rates for a 10 second spot is ₹50,000. Producers are possessive about buying commercial time on DD. As a result the DD's projected growth of revenue is only 6-10% as against 50-60% for the private sector channels. Software suppliers, advertisers and audiences are deserting DD owing to its unrealistic pricing policy. DD has three options before it. First, it should privatize, second, it should remain purely public service broadcaster and third, a middle path. The challenge seems to be to exploit DD's immense potential and emerge as a formidable player in the mass media.

Required:

(i) Discuss the best option, in your view, for DD.
(ii) Analyze the SWOT factors the DD has.
(iii) Explain the proposed alternatives which you suggested.
(iv) State the basic objectives for conducting SWOT analysis. [6+6+4+4]

2. Answer any two questions from a, b and c. **[2×15=30 marks]**

(a)
(i) Distinguish between 'Strategy' and 'Policy'. [3]
(ii) Explain the significance of Strategy Evaluation. [3]
(iii) Discuss the problems of strategy evaluation. [4]
(iv) "Discuss how a firm can create and sustain 'Competitive Advantage'. [5]

(b)
(i) Describe about "Corporate Restructuring". Discuss different Corporate Level Restructuring Strategies. [5]
(ii) "Differentiation Strategy is not without pitfalls". — Identify the common pitfalls. [5]
(iii) Explain about the 'synergy'. Discuss its significance in strategy making [5]

(c) Hassan is one of the India's leading detergent manufacturing companies. 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 the Product manager has prepared as input into his paper to the Board.

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

(ii) Explain what strategic options are available to Hassan in accordance to the BCG Matrix.

(iii) Outline what limitations the model poses to the Product Manager as he prepares his paper to the Board. [10+2+3]

3. Read the case and answer the following questions. [20 marks]

Rizwan, the general manager of Infosys, is to decide when to release the new version of Infosys's spreadsheet package, Easyspread 2.0. Development of Easyspread 2.0 is complete. However, the diskettes, compact discs, and user manuals have not yet been produced. The product can be shipped starting 2014.

The key problem is that Infosys has overstocked the previous version of its spreadsheet package, Easyspread 1.0. Rizwan knows that once Easyspread 2.0 is introduced, Infosys will not be able to sell any more units of Easyspread 1.0. Rather than just throwing away the inventory of Easyspread 1.0, Rizwan is wondering if it might be better to continue to sell Easyspread 1.0 for next three months and introduce Easyspread 2.0 on April 1,2014, when the inventory of Easyspread 1.0 will be sold out.

The following information is available:

	Easyspread 1.0	**Easyspread 2.0**
Selling price	₹1,500	₹1,850
Variable cost per unit of diskettes, compact discs, user manuals	200	250
Development cost per unit	650	950
Marketing and administrative cost per unit	350	400
Total cost per unit Operating income per unit	1,200	1,600
Operating income per unit	300	250

Development cost per unit for each product equals the total costs of developing the software product divided by the anticipated unit sales over the life of the product. Marketing and administrative costs are fixed costs in 2014, incurred to support all marketing and administrative activities of Infosys. Marketing and administrative costs are allocated to products on the basis of the budgeted revenues of each product. The preceding unit costs assume Easyspread 2.0 will be introduced on April, 2014.

Required

(i) On the basis of financial considerations alone, should Rizwan introduce Easyspread 2.0 on 2014, or wait until April 1, 2014? Show your calculations, clearly identifying relevant and irrelevant revenues and costs. [5]

(ii) What other factors might Rizwan consider in making a decision? [6]

(iii) Fixed Costs are irrelevant in decision making. List out the exceptions. [5]

(iv) State the term Opportunity Cost. [4]

4. Answer any two questions from a, b and c. [2×15=30 marks]

(a)

(i) The monthly budgets for manufacturing overhead of a concern for two levels of activity were as follows :

Capacity	60%	100%
Budgeted production (units)	600	1,000
Wages	₹ 1,200	₹ 2,000
Consumable stores	900	1,500
Maintenance	1,100	1,500
Power and fuel	1,600	2,000
Depreciation	4,000	4,000
Insurance	1,000	1,000
	9,800	12,000

You are required to:

I. Indicate which of the items are fixed, variable and semi variable

II. Prepare a budget for 80% capacity; and

III. Find the total cost, both fixed and variable, per unit of output at 60%, 80% and 100% capacity. [3+4+3]

(ii) Explain the concept of learning curve and state how relevant is the same in managing costing? [1+4]

(b) An agriculturist has 480 hectares of land on which he grows Onion, tomatoes, Cabbage and carrots. Out of the total area of land, 340 hectares are suitable for all the four vegetables but the remaining 140 hectares of land are suitable only for growing Cabbage and carrots. Labour for all kinds of farm work is available in plenty.

The market requirement is that all the four types of vegetables must be produced with a minimum of 5,000 boxes of any one variety. The farmer has decided that the area devoted to any crop should be in terms of complete hectares and not in fractions of a hectare. The only other limitation is that not more than 1,13,750 boxes of any one vegetable should be produced.

The relevant data concerning production, market prices and costs are as under:

	Onion	**Cabbage**	**Carrots**	**Tomatoes**
Annual yield:				
Boxes per hectare	350	100	70	180
	₹	₹	₹	₹
Costs:				
Direct material per hectare	952	432	384	624
Direct Labour:				
Growing per hectare	1792	1216	744	1056
Harvesting and packing per box	7.20	6.56	8.80	10.40
Transport per box	10.40	10.40	8.00	19.20
Market price per box	30.76	31.74	36.80	44.55

Fixed expenses per annum:	₹
Growing	1,24,000
Harvesting	75,000
Transport	75,000
General administration	1,50,000

It is possible to make the land presently suitable for Cabbage and carrots, vegetable for growing Onion and tomatoes if certain land development work is undertaken. This work will involve a capital expenditure of ₹6,000 per hectare which a bank is prepared to finance at the rate of interest of 20% p.a. If such improvement is undertaken, the harvesting cost of the entire crop of tomatoes will decrease on an average by ₹2.60 per box.

Required:

I. Calculate, within the given constraint, the area to be cultivated in respect of each crop to achieve the largest total profit and the amount of such total profit before land development work is undertaken. [7]

II. Assuming that the other constraints continue, advice the grower whether the land development schemes should be undertaken and if so the maximum total profit that would be achieved after the said development schemes is undertaken. [8]

(c)

(i) Difference in operating speeds of machines may lead to higher WIP inventory. How does a JIT system resolve this issue? [5]

(ii) State how the PRAISE process can be smoothly implemented. [3]

(iii) A Company using a detailed system of standard costing finds that the cost of investigation of variances is ₹ 20,000. If after investigation an out of control situation is discovered, the cost of correction is ₹ 30,000. If no investigation is made, the present value of extra cost involved is ₹ 1,50,000. The probability of the process being in control is 0.82 and the probability of the processes being out of control is 0.18. You are required to advice:

I. Whether investigation of the variances should be undertaken or not;

II. The probability at which it is desirable to institute investigation into variances. [3+4]