

Paper 15 - Business Strategy & Strategic Cost Management

Whenever necessary, suitable assumptions should be made and indicate in answer by the candidates.

Working Notes should be form part of your answer

Section A

Question No. 1 & 2 are compulsory. Answer any two questions from the rest.

- 1 In 2002, the Florida Turnpike became the first governmental toll agency to be given the ability to function as a private enterprise. The Florida's Turnpike Enterprise's goal was to become an innovative operation built on providing value at every part of the customer experience. As part of the "We Drive Smiles" initiative, a series of awareness and skill-building service training sessions were delivered to all 1,400 team members across the entire state of Florida.

Within one year, this ground-breaking effort resulted in many impressive operational improvements, including:

- Dramatic improvement of employee morale (up 18%) and customer satisfaction (92% would recommend to family/friends).
- has expanded and increased revenue, improved efficiency, cost-effectiveness and timely project delivery.
- has leveraged resulting additional revenue to make substantial improvements to the existing road system, delivered six expansion projects, contracted most in-house functions to the private sector, promoted customer service, maintained financial stability and improved bond rating.
- expanded responsibility for all operations on every FDOT-owned and operated toll road and bridge. This represents about 600 miles of roadway and 80 percent of all toll facilities in Florida.

Based on the amazing success of this service transformation, Florida's Turnpike Enterprise was awarded the prestigious international President's Award for Innovation and Excellence in 2003 and later won the JD Powers Seal of Approval for Excellence in 2005.

Required:

- (a) What are the impressive outcomes of adopting the strategies by Florida Turnpike?
- (b) State the merits and demerits of Benchmarking.
- (c) List the types of Benchmarking.

[4+5+6]

2. IKEA's goals of sustainability and environmental design are central to its business strategy. It has launched a new sustainability plan to take the company through to 2015. This will combine social, environmental and economic issues.

IKEA uses SWOT analysis to help it reach its objectives. This is a strategic planning tool. It helps the business to focus on key issues. SWOT is the first stage of planning and looks at the Strengths, Weaknesses, Opportunities and Threats involved in a project or business venture.

Strengths and weaknesses are internal aspects. This means that they are within the control of the business. They may refer to aspects of marketing, finance, manufacturing or organization.

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Opportunities and threats are external factors. This means that they are outside the control of the business. These may include the environment, the economic situation, social changes or technological advances, such as the internet.

A business can create opportunities and counter threats by making the most of its strengths and addressing its weaknesses. For example, one of IKEA's key strengths is its strategic aim to use no more material than necessary in the production of each item. In addition, it develops its product plans to increase its use of waste or recycled materials.

- One particular table, the NORDEN table, uses knotty birch wood. The knots in this wood usually mean it is rejected by other retailers and manufacturers as unsuitable for use. However, IKEA has made the knots part of its design feature.
- OGLA chairs are made using wood waste from saw mills and LACK tables use a 'sandwich' of stiff card between wood sheets to reduce the amount of solid wood needed.

IKEA is a well-known global brand with hundreds of stores across the world. In order to improve performance, it must assess its external and competitive environment. This will reveal the key opportunities it can take advantage of and the threats it must deal with. IKEA responds to both internal and external issues in a proactive and dynamic manner by using its strengths and reducing its weaknesses. Through this, IKEA is able to generate the strong growth it needs to retain a strong identity in the market.

IKEA's passion combines design, low prices, economical use of resources, and responsibility for people and the environment. The company's products, processes and systems all demonstrate its environmental stance. For example, clever use of packaging and design means more items can fit into a crate, which means fewer delivery journeys. This in turn reduces IKEA's carbon footprint.

IKEA believes that there is no compromise between doing good business and being a good business. It aims to go beyond profitability and reputation. IKEA is intent on becoming a leading example in developing a sustainable business. This will create a better everyday life for its customers. IKEA has discovered a business truth being sustainable and responsible is not just good for customers and the planet; it is also good for business.

Required:

(i) Explain the meaning of strengths in the context of SWOT Analysis.

(ii) Describe the advantages of SWOT Analysis.

(iii) Mention the basic objectives of SWOT Analysis

(iv) What are the advantages of IKEA after adopting the SWOT Analysis?

[3+3+4+5]

3. Contingency Planning. Enumerate the steps involved in it. List the benefits of Contingency Planning. **[2+4+4=10]**

4. How social analysis is conducted as a part of PEST Analysis? List the Drawbacks of PEST Analysis. **[4+6=10]**

5. (a) Discuss what is Retrenchment Strategies and why it is adopted? **[6]**

(b) List the factors that affect the choice of a strategy. **[4]**

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Section B

Question No.6 is Compulsory. Answer any two questions from the rest.

6. Boraco Ltd. has been offered supplies of special ingredients S at a transfer price of ₹15 per kg by Chhotaco Ltd. which is part of the same group of companies. Chhotaco Ltd processes and sells S to customers external to the group at ₹15 per kg. Chhotaco Ltd. bases its transfer price on cost plus 25% profit mark-up. Total cost has been estimated as 75% variable and 25% fixed.

You are required to:

Discuss the Transfer prices at which Chhotaco Ltd. should offer to transfer special ingredient S to Boraco Ltd. in order that group profit maximizing decisions may be taken on financial ground in each of the following situations:-

- (i) Chhotaco Ltd. has an external market for all of its production of S at a selling price of ₹15 per kg. Internal transfers to Boraco Ltd. would enable ₹1.50 per kg of variable packing cost to be avoided.
- (ii) Conditions are as per (i) but Chhotaco Ltd has production capacity for 3,000 kg of S for which no external market is available.
- (iii) Conditions are as per (ii) but Chhotaco Ltd has an alternative use for some of its spare production capacity. This alternative use is equivalent to 2,000 kg of S and would earn a contribution of ₹6,000. **[4+3+3]**

7.

(a) A Multinational Company runs a public Medical Health Centre. For this purpose, it has hired a building at a rent of ₹10,000 per month with 5% of total taking. The Health Centre has 3 types of wards for its patients namely- General ward, Cottage ward, and Deluxe ward. State the rent to be charged to each bed-day for different type of ward on the basis of the following information.

- (i) The number of beds of each type is general ward 100, Cottage ward 50, Deluxe ward 30.
- (ii) The rent of cottage ward bed is to be fixed at 2.5 times of the general ward bed and that of Deluxe ward bed as twice of the Cottage ward bed.
- (iii) The Occupancy of each type of ward is as follows-
General ward 100%, Cottage ward 80% and Deluxe ward 60%. But, in General ward, there were occasions when beds are full, extra beds were hired at charges of ₹20 per bed. The total hire charges for the extra beds incurred for the whole year amount to ₹12,000.
- (iv) The Health Centre engaged a Heart Specialist from outside and on an average fees paid to him was ₹15,000 per trip. He makes three trips in the whole year.
- (v) The other expenses for the year were as under-

Salary of Supervisors, Nurses, Ward Boys	4,25,000
Repairs and maintenance	90,000
Salary of Doctors	13,50,000
Food supplied to patients	40,000
Laundry charges for their bed linens	80,500
Medicines supplied	74,000
Cost of Oxygen, X-ray etc. other than directly borne for treatment of patients	49,500
General Administration Charges	63,000

- (vi) Provide profit at 20% on total taking.
- (vii) The Health Centre imposes 8% Service Tax on rent received.
- (viii) 360 days may be taken in a year. **[4+4+4]**

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(b) Write down the role of a Firm's suppliers in its Value Engineering or Cost Reduction drive. [4]

(c) "Kaizen Costing is an approach that explicitly incorporates continuous improvement during the budget period" Discuss the statement. [4]

8.

(a) 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, viable 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.

(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+8]

(b) List out the assumptions on which cost-volume profit analysis is based? [4]

9.

(a) What is Product Life Cycle Costing? State its characteristics and benefits. [1+2+2]

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(b) Whirlpool India Ltd. assembles washing machines at its Auburn plant. In December 2013, 60 tumbler units that cost ₹ 44 each (from a new supplier who subsequently went bankrupt) were defective and had to be disposed of at zero disposal value. Whirlpool India Limited was able to rework all 60 washing machines by substituting new tumbler units purchased from one of its existing suppliers. Each replacement tumbler cost ₹ 50.

Required

- (i)** What alternative approaches are there to account for the material costs of reworked units?
- (ii)** Should Whirlpool India Limited use the ₹ 44 tumbler or ₹ 50 tumbler to calculate the costs of materials reworked? Explain.
- (iii)** What other costs might Whirlpool India Limited include in its analysis of the total costs of rework due to the tumbler units purchased from the (now) bankrupt supplier? **[2+1+2]**

(c) Four Products A, B, C and D have ₹5, ₹7, ₹3 and ₹9 profitability respectively.

First type of material (limited supply of 800 kgs.) is required by A, B, C and D at 4 kgs., 3 kgs., 8 kgs., and 2 kgs., respectively per unit.

Second type of material has a limited supply of 300 kgs., and is for A, B, C and D at 1 kgs., 2 kgs., 0 kgs and 1 kg. per unit. Supply of other type of materials consumed is not limited. Machine hrs. available are 500 hrs and the requirement are 8, 5, 0, 4 hours for A, B, C and D each per unit.

Labour hours are limited to 900 hours and requirements are 3, 2, 1 and 5 hours for A, B, C and D respectively.

Formulate this as a linear programming problem. You are not required to solve the LPP. **[5]**

(d) List out ten steps of quality improvement as has been conceptualized by Philip Crosby. **[5]**