PAPER 15 - Business Strategy and Strategic Cost Management

Working Notes should form part of the answer
"Wherever necessary, suitable assumptions should be made and indicated in answer by the candidates."

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

1. From peak sales of over 27,000 units in the January-March 2012 quarter to under 4,000 in the three months to December 2013, Tata Motors' Nano hasn't quite lived up to the hype and expectations built up since its launch in mid-2009. To combat with the situation now it launched Nano Twist, a 'smart city car' costing just under Rs. 2.36 lakhs.
Answer the following questions :

(a) What is strategic decision? What are its characteristics? **[5]**
(b) Strategic decisions are complex in nature – explain. **[5]**
(c) Explain how this strategic decision will help Tata Motors to repositioning themselves in the market . **[5]**

2. Hero Honda joint venture formed in 1984 is a classic case of strategic alliance involving the Indian company Hero Group and Japanese automobile major Honda Motorcycle. The alliance has been terminated with the entire 26% stake of Honda Motorcycle in the venture bought by the Hero Group. Selling out of the venture gives the Japanese company the freedom to go it alone in the world's second largest market for two-wheelers.

(a) Is joint venture the only way to enter into strategic alliance? **[5]**
(b) Alliances are not new, but in the competitive landscape, distinguishing features are emerging. Identify these features. **[5]**
(c) What are the key success factors for managing an alliance? In the light of these key success factors, identify the reasons for the termination of this successful joint venture. **[5]**

3. It has been known for many years that the returns from diversification are often poor. Why do managers still persist with it as a strategy? **[10]**

4. Discuss how competitive forces shape strategy? **[10]**

5. Explain the concept of 'value-chain' and discuss the advantages of value-chain analysis to-any organisation. **[10]**

Section B
Question No. 6 is compulsory. Answer any two questions from the rest.

6. After observing heavy congestion of customers over a period of time in a petrol station, Mr. Anup has decided to set up a petrol pump facility on his own in his nearby site. He has complied

statistics relating to the potential customer arrival pattern and service pattern as given below. He has also decided to evaluate the operations by using the simulation technique.

Arrivals		Services	
Inter-arrival time (minutes)	**Probability**	**Inter-arrival time (minutes)**	**Probability**
2	0.22	4	0.28
4	0.30	6	0.40
6	0.24	8	0.22
8	0.14	10	0.10
10	0.10		

Assume:

(i) The clock starts at 8.00 hours

(ii) Only one pump is set-up

(iii) The following 12 Random Nos. are to be used to depict the customer arrival pattern

78	26	94	08	46	63	18	35	59	12	97	82

(iv) The following 12 Random Nos. are to be used to depict the service pattern

44	21	73	96	63	35	57	31	84	24	05	37

You are required to find out the

(i) Probability of the pump being idle

(ii) Average time spent by a customer waiting in queue. **[8+2=10]**

7.

(a) Fit straight line by the least square method to the following figures of production of Sugar Factory. Estimate the production for the year 2013.

Year	2007	2008	2009	2010	2011	2012	2013
Production(in Lakh tons)	76	87	95	81	91	96	90

[3+2=5]

(b) State the assumptions on which cost-volume profit analysis is based. **[5]**

(c) Hardware Ltd manufactures computer hardware products in different divisions which operate as profit centres. Printer Division makes and sells printers. The Printer Division's Budgeted Income Statement, based on a sales volume of 15,000 units which is given below. The Printer Division's Manager believes that sales can be increased by 2,400 units, if the Selling Price is reduced by ₹20 per unit from the present price of ₹400 per unit, and that, for this additional volume, no additional fixed costs will be incurred.

Printer Division presently uses a component purchased from an outside supplier at ₹70 per unit. A similar component is being produced by the Components Division of Hardware Ltd and sold outside at a price of ₹100 per unit. Components Division can make this component for the Printer Division with a small modification in the specification, which would mean a reduction in the Direct Material Cost for the Components Division by ₹1.5 per unit. Further, the Component Division will not incur variable selling cost on units transferred to the Printer Division. The Printer Division's Manager has offered the Component Division's Manager a price of ₹50 per unit of the component.

The Component Division has the capacity to produce 75,000 units, of which only 64,000 can be absorbed by the outside market.

The current Budgeted Income Statement for Components Division is based on a volume of 64,000 units considering all of it as sold outside.

Particulars	Printer Division ₹'000	Component Division ₹"000
1. Sales Revenue	6,000	6,400
2. Manufacturing Cost:		
Component	1,050	-
Other Direct Materials, Direct Labour & Variable OH	1,680	1,920
Fixed OH	480	704
Total Manufacturing Cost	3,210	2,624
3. Gross Margin (1 - 2)	2,790	3,776
Variable Marketing Costs	270	384
Fixed Marketing and Admn. OH	855	704
4. Non-Manufacturing Cost	1,125	1,088
5. Operating Profit (3 - 4)	1,665	2,688

1. Should the Printer Division reduce the price by ₹ 20 per unit even if it is not able to procure the components from the Component Division at ₹50 per unit?
2. Without prejudice to your answer to part (1) above, assume that Printer Division needs 17,400 units and that, either it takes all its requirements from Component Division or all of it from outside source. Should the Component Division be willing to supply the Printer Division at ₹ 50 per unit?
3. Without prejudice to your answer to part (1) above, assume that Printer Division needs 17,400 units. Would it be in the best interest of Hardware Ltd, for the Components Division to supply the components to the Printer Division at ₹50?

Support each of your conclusions with appropriate calculations. **[4+3+3=10]**

8.

(a) A company has just completed the manufacture of 40 units of a new product. The manufacturing costs are:-

Direct materials	2,00,000
Direct labour: 8000 hours at ₹20 per hour	1,60,000
Variable overheads	80,000
Special tools (re-usable)	10,000
Fixed overhead apportioned	1,00,000
Total	5,50,000

The Company policy is to add a profit of 12% on selling price.

The Company received another order for 120 units of this product for which the company quoted, based on its policy on absorption cost basis, a price of ₹15,625 per unit. The customer struck the order to ₹11,000 per unit. The Company is short of work and so is keen to take up more orders but it is reluctant to accept this order price because it is against the policy to accept any price below its cost. The Company experiences a learning curve of 90%.

(i) Compute the gain or loss arising from acceptance of the order of ₹11,000 per unit.

(ii) Advice whether the company should accept this order for 120 units or not. **[3+5=8]**

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

(c) A Company manufactures a single product, which requires two components. The company purchases one of the components from two suppliers: X Ltd. and Y Ltd. The price quoted by X Ltd is ₹180 per hundred units of the component and it is found that on an average

3% of the total receipt from this supplier is defective. The corresponding quotation from Y Ltd is ₹174 per hundred units, but the defective would go up to 5%. If the defectives are not detected, they are utilized in production causing a damage of ₹180 per 100 units of the component.
The Company intends to introduce a system of inspection for the components on receipt. The inspection cost is estimated at ₹24 per 100 units of the component. Such as inspection will be able to detect only 90% of the defective components received. No payment will be made for components found to be defective in inspection.

(i) Advise whether inspection at the point of receipt is justified?
(ii) Which of the 2 suppliers should be asked to supply?
Assume total requirement is 10,000 units of the component. **[3+4=7]**

9.

(a) Why is Traditional Accounting not needed? **[4]**

(b) Citizen Company produces Mathematical and Financial Calculators. Data related to the products is presented below.

Particulars	Mathematical	Financial
Annual production in units	50,000	1,00,000
Direct materials costs	₹1,50,000	₹3,00,000
Direct manufacturing labour costs	₹50,000	₹1,00,000
Diorect manufacturing labour hours	2,500	5,000
Machine hours	25,000	50,000
Number of production runs	50	50
Inspection hours	1,000	500

Both products pass through Department 1 and Department 2. The departments combined manufacturing overhead costs are

	Total
Machining costs	₹3,75,000
Setup costs	1,20,000
Inspection costs	1,05,000

Required:-

(i) Compute the manufacturing overhead cost per unit for each product.
(ii) Compute the manufacturing cost per unit for each product. **[3+3=6]**

(c) Standard cost specification for a product are as follows:

Time 15 hours per unit		
Cost ₹3 per hour		
Actual performance in a cost period is as follows:		
Production 500 units		
Hours taken	Production	7,800 hours
	Idle time	200 hours
Total time		8,000 hours

Payment made ₹24,800 (average per hour ₹3.10).
Calculate Labour variances. **[10]**