

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA (U) EXAMINATIONS

LEVEL FOUR

BUSINESS POLICY - PAPER 17

TUESDAY, 17 DECEMBER, 2002

INSTRUCTIONS TO CANDIDATES

1. Time Allowed: 3 Hours
2. Section **A** has **one** compulsory question carrying 50 Marks
3. Section **B** has **three** questions and only **two** are to be attempted. Each question carries 25 Marks.
4. Please, read further instructions on the answer book.

SECTION A

Question 1

Uganda Telecom International Ltd (UTIL) is a well-established company providing telecommunications services both nationally and within the COMESA [Common Market for Eastern and Southern Africa] region. Its business has been concerned with telephone calls, the provision of telephone lines and equipment, and private telecommunications networks. UTIL has recently supplemented these services by offering mobile phones, which is an expanding market locally and in the region.

The company maintains a diverse customer base, including residential users, regional companies, government agencies and public-sector organizations. The company handles approximately 10 million calls each working day, and employs nearly 5,000 personnel.

Strategic development

The chairman of UTIL stated in the latest annual report that there are 3 (three) main areas in which the company aims to develop in order to remain a regional leader in the telecommunications market. He believes that the three main growth areas reflect the evolving nature of the telecommunications market and will provide scope for development.

The areas in which development is planned are:

1. Expansion of the telecommunications business in the national and regional markets, both by the company acting on its own and through partnership arrangements with other suppliers.
2. Diversification into electronic media services – TV, Radio etc, providing the hardware to permit electronic shopping from home / office and broadcasting services.
3. Extension of the joint ventures and strategic alliances which have already been established with companies in Rwanda, Tanzania, Zimbabwe, Kenya, DRC, Sudan, Ethiopia and South Africa.

The chairman explained that the company is intent on becoming the regional leader in communications. This will be achieved through maintaining its focus on long-term development by improving its services to customers, developing high-quality, up-to-date products and being innovative, flexible and market-driven. His aim is to deliver to the region a world-class service at competitive prices.

Financial Information

Extracts from the company's financial records for the last two years indicate the following figures of its performance in the national telecommunications market:

	Last Year US\$,000	Previous Year U\$ '000
Turnover	16,613	15,977
Profit (EBIT)	3,323	2,876
Capital Employed	22,150	21,300

UTIL estimates its cost of capital to be approximately 11 %.

The Chairman expressed satisfaction with the increase in turnover and stated that cost efficiencies were now being generated following completion of a staff reduction programme. This would assist the company in achieving a target return on capital employed (ROCE) in this market of 20% over the next three years.

Business Opportunities

According to the Chief Executive Officer of UTIL, major opportunities for the company lie in the following areas:

- Encouraging greater use of the telephone;
- Provision of advanced services, and research and development into new technologies, including internet and systems integration.
- The increasing freedom from government control of telecommunication services in the region.

The company has used an extensive advertising Television and Poster campaign. This was in order to penetrate further the residential market by encouraging greater use of the telephone, with varying charging incentives being offered to residential customers.

To further the objective of increasing long-term shareholder value, the company is actively considering investment of US\$ 200 Million in each of the next three years in new technology and quality improvements in its national market. This investment is not expected to have any residual value at the end of three years.

Following the investment the Directors of UTIL believe that its rate of earnings before interest and tax (EBIT) to turnover in its national telecommunications market will remain constant. This rate will be at the same level as last year for each of the three years of the investment.

Market and Competition

UTIL is currently experiencing an erosion of its market share and faces increasingly strong competition in the mobile phone market. While UTIL is the leader in its national market, with an 85% share of the telecommunications business, it has experienced a reduced demand for the supply of residential lines in the last five years as competition has increased.

The market for supply of equipment in the national telecommunications market is perceived to be static. The investment of US \$ 200 million in each of the next

three years is estimated to increase UTIL's share of this market to a level of 95%. The full improvement of 10% is expected to be received by UTIL next year, and its market share will then remain at this level for the full three-year period. It is anticipated that unless further investment is made after the three-year period, UTIL's market share will revert to its current level as a consequence of the expected competitive response.

Industry regulation

The Government of Uganda has established the Uganda Communications Commission (UCC) as a regulatory body to promote competition and deter anti-competitive behaviour in the sector. As a result of the activities of the UCC (the regulator) and aggressive pricing strategies, it is anticipated that charges to customers will remain constant for the full three-year period of the new investment. All cash flows can be assumed to occur at the end of the year to which they relate. The cash flows and discount rate are in real terms.

Required:

- (a) Explain the nature of political, economic, social, and technical forces, which influence UTIL in developing its business and increasing its market share.
(10 marks)
 - (b) Apply **Ansoff's** product/market growth vector matrix to assess the extent of the potential market development opportunities available to UTIL.
(10 marks)
 - (c) Evaluate and comment on UTIL's proposed investment in the new technology and quality improvements in its national telecommunications market. Assume that variable costs are 80% of the incremental revenue, and that fixed costs will not increase. Ignore working capital and taxation.
(15 marks)
 - (d) Assess to what extent the investment in new technology and quality improvements in UTIL's national telecommunications market contributes towards the closure of the company's planning gap in respect of its target ROCE.
NB: You may assume that the entire capital investment is written off at the end of the three-year period.
(5 marks)
 - (e) Recommend a strategy, which UTIL could employ to close the gap and achieve the strategic development aims identified by the chairman.
(10 marks)
- (Total 50 marks)**

SECTION B**Question 2**

Organizations have what are termed as “*core / primary*” activities as well as “*support activities*”. Analysing the **value added** achieved by an organization will reveal how much has been contributed by each of its primary and support activities. The object of the analysis is to identify those activities undertaken by the organization, which contribute the most to the total value added. This is so that strategies may be established to increase their contribution still further in order to meet organizational objectives.

Required:

Explain how value chain analysis may help a company:

- (a) to assess the value added by each of its primary activities and support activities.
- (b) to determine its priorities for strategic resource allocation.

(25 marks)

Question 3

Financial accounting is mainly geared towards the provision of information to external decision makers. For this reason management accounting evolved to serve the needs of the internal decision makers and cost control. In concentrating on the internal environment, the management accounting function has been criticised for not addressing the needs of senior management to enable effective strategic planning. In particular, the criticism has focused on inadequate provision of information, which analyses the organisation’s exposure to environmental change and its progress towards the achievement of corporate objectives.

Required:

Explain how strategic management accounting can provide information that meets the requirements of senior managers in seeking to realize corporate objectives

(25 marks)

Question 4

Both academic theory and the practice of strategic planning agree that it refers to the task of choosing directions and areas of concentration for an organization and that the strategic planning process is affected by the nature of the environment.

Required:

- (a) Identify the five competitive forces in the environment of a firm and discuss the threat posed to the firm by each of these forces.
(15 marks)
- (b) Discuss the nature and effect of significant 'entry barriers' on the formulation of a strategic plan for a business which is already established in the industry.

(10 marks)
(Total 25 marks)