

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA (U) EXAMINATIONS

LEVEL FOUR

BUSINESS POLICY - PAPER 17

TUESDAY, 17 JUNE 2003

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. Mathematical tables are provided at the end of the question paper.
5. Please, read further instructions on the answer book.

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SECTION A

Question 1

Ziphom (U) Ltd (ZUL) is a fast growing company specializing in the design, artwork, copywriting and production of high quality catalogues and brochures. The company was formed only ten years ago by *Hussein Kyalo*, a charismatic art and design graduate, and has grown largely as a direct result of his personal leadership. The business focus at ZUL has been constant throughout this period – quality, client responsiveness and innovation in both design and use of associated information technology. When asked for his view on the mission of ZUL, Hussein simply replied, “to win”.

ZUL has a staff of about 40, most of whom are graduates, and with an average age of about 30 years. The company operates through a very loose management structure, which is essentially based on project design teams forming and reforming in response to the nature and flow of work received from clients. There are some dedicated functions, namely, the sales account executives who manage a portfolio of clients, and the buyers who commission print production when design has been completed.

ZUL's growth to date has been entirely organic, making use of high levels of profitability, high levels of retained earnings and extensive use of operating leases for design technology equipment from DFCU Leasing Ltd. A summary of the 2002 financial results of ZUL is shown at the end of this scenario.

About 70 % of the turnover arises from sub-contracting out printing work, which arises as a result of design, and about 30% for the design work itself. ZUL aims to make about 5% operating profit on clients' print production. Print production is sub-contracted to a number of printing businesses based usually on the lowest tender price, subject to clear-cut quality and delivery guidelines.

Hussein is of the view that the next stage in ZUL's development must be to move into the actual printing business itself, so integrating design and production completely and maximizing value chain profitability. He believes that this process of vertical integration should be carried out by acquisition and has targeted Quick Printing Factory Ltd (QPF Ltd), a family run business, as a prime candidate for takeover.

QPF has been in existence for over 40 years and the present managing director and majority shareholder has for some time been wishing to sell the business and retire. QPF has some 250 employees, mainly in operational areas such as stores, job layout and machine set-up, print machine operation, maintenance, packaging and dispatch. Employees are all trade union members. Current financial data for QPF is shown in the table below together with average results for similar printing businesses. These results are typical of performance in recent years for this sector of the printing industry, although QPF's results have shown a

steady deterioration over the last few years. About 5% of QPF's turnover arises from print jobs already sub-contracted from ZUL.

A preliminary acquisition agreement has been reached which values QPF basing on a Price Earnings Ratio (PE) of 6:1 on current pre-tax profits. QPF's balance sheet values are viewed as broadly realistic, if not a little over optimistic, and reflect a going concern situation. The non-current assets are largely represented by printing machinery, much of which was acquired some years ago. The acquisition price is to be paid as to 40 % on takeover and the remaining 60% in equal installments over the next six years. ZUL plans to meet 10% of the initial 40% payment through existing cash resources, and to raise the remaining 30% through a medium-term bank loan secured against the assets of both ZUL and QPF. The remaining balance of the purchase price will be paid through operating cash flows generated by the amalgamated business.

Summary financial data (all figures in Shs millions)

	ZUL	QPF	Printing Industry Average
Sales	10.5	20.3	30.5
Cost of sales	7.2	14.6	19.6
Gross profits	3.3	5.7	10.9
Expenses	2.2	4.9	7.5
Net profits	1.1	0.8	3.4
Non-current assets	1.2	8.4	17.2
Current assets	3.6	5.3	6.3
Current liabilities	1.3	2.2	3.3
Net Assets	3.5	11.5	20.2

Required:

- (a) It is fairly obvious from Hussein's mission statement ('to win') that he is interested in the company becoming successful, and will be interested in some kind of 'growth strategy'.
 - (i) Using the PEST model as the starting point, discuss the key issues which should be considered by ZUL in developing its business. (20 marks)
 - (ii) Identify the forces, which affect the level of competition in the printing industry using Porter's Five Forces Analysis Tool. (20 marks)
 - (b) Using the data provided and any other relevant arguments or non-financial information comment on the growth strategy of ZUL Ltd. Advise whether ZUL should go or not go ahead to acquire QPF. (10 marks)
- (Total 50 marks)**

SECTION B

Question 2

Marketing has been defined as identifying customer needs and wants and finding ways to satisfy them profitably. Understanding and crafting an appropriate "marketing mix" is essential when developing a winning marketing strategy for a service based business.

Required:

Describe how the marketing mix model could assist in the process of strategy formulation for a service-based business.

(25 marks)

Question 3

Human Resource Planning, Recruitment and Training are key elements of any Human Resource Management strategy.

Required:

Explain why proper and adequate consideration of the elements of human resource planning, recruitment and training are an important feature of the strategic management of organizations that employ significant numbers of accountants and other professionally qualified staff.

(25 marks)

Question 4

The Boston Consulting Group (BCG) growth share matrix is a model, which identifies the positioning of a strategic business unit (SBU), indicating its market growth rate and relative market share. It has been stated that the matrix is useful as it illustrates a portfolio's strength and helps in providing a guide for the strategic direction of each SBU.

Required:

Explain the contents and the main uses of the BCG matrix in strategic planning.

(25 marks)