

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

A Committee of the Council of ICPAU

CPA(U) EXAMINATIONS

LEVEL FIVE

INTEGRATION OF KNOWLEDGE – PAPER 19

COMPREHENSIVE CASE STUDY

MORNING SESSION MATERIAL

THURSDAY, 21 JUNE 2007

INSTRUCTIONS TO CANDIDATES:

1. Time allowed: 5 hours 30 minutes.
9.00 – 11.00 a.m. (2 hours): Planning.
11.00 – 12.00 a.m. (1 hour): Break.
12.00 – 3.30 p.m. (3 hours 30 minutes): Writing.
2. The following pages contain case study materials.
3. The case study questions are contained in a separate paper marked Afternoon Session Material.
4. The completed answers and any working papers, clearly labelled working papers must be handed in at the end of the afternoon session. Where working papers form part of your answer, ensure that they are appropriately cross referenced.
5. It is in your interest that you hand in all written materials prepared during the examination.
6. Tables are provided on page 17.
7. Please read further instructions on the answer book.

STARGATE TELECOMS LTD

The Stargate Telecoms Ltd story was supposed to be a tale of huge success built from humble origins. Started 32 years ago, the company had reached UGX 1,000 billion in regional sales, building from its strengths in one of the most novel and competitive sectors in Eastern and Southern Africa. The firm was a typically African business family concern, with three brothers — **Samuel, Daniel and Peter Sembatya**. Samuel Sembatya was the original founder of the company. The eldest brother, Samuel was born in 1955, and spent his childhood through the harsh times that Africans suffered in the pre-independence boycotts in Central Buganda. On his father's death, he had to leave school at the age of 15 to take up a job in a radio repair shop. In 1975, Samuel, who had just turned 20, told his brother Peter he was convinced that the market for electronics gadgets could only grow as technology advanced. With UGX 300,000, obtained from the sale of Samuel's land which he inherited from his father, Samuel rented premises in Katwe, bought an electrical toolkit and set out in business making crude radio transmitters and telephone sets which they sold to locals in their home vicinity. Sales increased steadily over the next few years as their production and marketing skills improved.

In the early 1980s, the Sembatya Brothers put into practice several innovations that helped turn the business from a small enterprise into a giant regional corporation. At first they used to sell only to selected users because they could not meet demand, given the small size of their workshop. However, as revenues increased, they purchased a fully automated electronics assembly line from China and thus began mass producing their radios and telephone receiver sets. Samuel had another idea, unusual at that time: to offer retailers a 10 % discount paid in cash on delivery of their products. At that point, the electrical equipment did not carry the family name (they used foreign names, like 'Ladio' or 'Visioni') But they already had the characteristics of medium to high quality design at a very reasonable price. The electrical equipment (products) were also fully tropicalized and could withstand the effects of power surges and sudden outages. These positive characteristics were appreciated by the market and made the products highly favoured.

Two new ideas also emerged at the time of acquisition of the new assembly line. These included a novel technique for making electronics using robotic equipment. Samuel had observed, while visiting factories in India and China, that the use of robotic arms in certain processes increased quality because of their calibration precision and the need to solder parts in a dust free environment. Robotic arms could carry out this procedure in a vacuum space. The other idea was to recondition discarded electrical products imported from overseas to local

requirements and resell them in new covers/jackets with the Stargate label. The refurbished electricals were equally reliable and made a handsome profit for the company.

At about this time, the youngest brother Peter was graduating from University. Peter was placed in charge of warehousing and stores, while Daniel headed the production department. In 1985, the first electronics factory was built in the Kabusu Industrial Area, south west of Kampala. In 1988, the company opened the first independent outlet in the town of Ndeeba in the same locality as their factory, not far from Kabusu. With its appealing displays and customer oriented service, the shop was an immediate success as products included guarantees for repair or replacement. By 1998, approximately 200 Stargate Telecoms Ltd shops had opened in East and Central Africa; many of them franchised but all still bore the Stargate Telecoms Ltd name.

The idea of having other names with a different decoration and selection of electronics was at this point not found appealing and was abandoned. Production outside Uganda was also not started, not for economic and technical reasons, but to bypass protectionism in the COMESA Region countries, parts were imported into the various countries for assembly after manufacturing in Uganda. The complexity of handling an ever-expanding network of shops, production, materials' flows and employees kept increasing. By early 2000, everybody at company headquarters felt that something had to be done. The decision was made in 2001 to bring in professional managers.

Mr. James Pulunyi CPA, 36, a highly regarded executive formerly at Business Finance Bank (East and Central Africa's Premier Development Bank) in Kampala, was hired as a consultant and after some time became the new managing director. Although he had several ideas for the growth of the firm, his limited experience in industrial companies obliged him to hire experienced managers to put his ideas into practice. Mr. Pulunyi was a hardworking and energetic man who feared failure. As a result, he was reluctant to delegate and thus had to work late hours to keep up with the demands of work. Often times, he failed to follow through critical management decisions because of work overload. However, he was known for being forthright and honest

The man, in charge of personnel and organization, was Mr. Stone Ntambazi, who joined Stargate Telecoms Ltd in 2001 from a similar position at Game Electronics, a large South African multinational. They proceeded to recruit experienced managers from other large companies to form a 'professional team'. Mr. Ntambazi had to implement an organization development programme to bridge the old 'handshake management' culture with the new and more formal one. This process of creating new functions and written procedures lasted three

years, and finished in October 2003, far much longer than had been envisaged. Mr. Ntambazi was a high flier who enjoyed the corporate party circuit. As such he was always not abreast of his work and had a tendency to cronyism. He had recruited several old school pals of his in complete disregard of the company's human resources policy. Samuel and James were watching him and it was only a matter of time before the axe came down, contrary to Stargate's unwritten policy of running the business as a close knit family. Whoever was hired could consider theirs a job for life and could experience a fulfilling career at the firm. On several occasions James had scheduled early morning meetings with Mr. Ntambazi, only for the latter not to turn up. This was one of the reasons why the organizational development programme was lagging behind schedule.

As part of the new organizational development strategy, Mr. Ntambazi was supposed to introduce and fully implement a matrix organizational structure. This would replace the existing hierarchical structure which it was believed was no longer appropriate (see exhibit I). However his lifestyle and Mr. Pulunyi's reluctance to delegate responsibilities were affecting the pace of this programme and activities in other areas, especially product development. Delayed decision making was also responsible for the threat of industrial action by unionized staff, something never heard of in the Stargate business.

The Board of Directors was composed of the three members of the Sembatya family and Mr. Pulunyi. The Sembatya's did not play the conventional, distant role of members of the Board and took part in many day-to-day decisions. Although it did not appear in the organization chart, most of the senior functional managers had two reporting relationships: a formal one to James Pulunyi, and an informal one to a member of the Sembatya family.

Hence, there were two different groups of managers that had to coexist at the top: the self-made Sembatya siblings, and the well-educated ex-multinational executives. The main task of the organization development project was to join both cultures. According to Mr. Fulgence Mugabe, one of the managers of this project, there had been a lot of improvement in the mutual understanding process in the last three years, but the job was not finished yet because of the difficulty some people found in accepting change and new rules. Inevitably the new breed of managers was set on a collision course with the old guards.

Until July 1998, the three Sembatya siblings shared 100% of the company's equity. After reporting strong 1997 results, the company offered a total of 1.56 million common shares to the public. 7,000 shares were listed on the Uganda Securities Exchange, 448,000 shares on the Nairobi Stock Exchange, and the rest went to Stargate Telecoms Ltd's employees, dealers and clients. The total stock issue represented about 49% of the company. In addition, the company sold

UGX 40 billion and € 2 million denominated bonds with warrants. It was estimated that the whole financial operation represented about 20% of the company's equity, bringing in a minimum of UGX 330 billion of fresh capital.

The Company in 2004: An Overall Description

Stargate Telecoms Ltd was, by 2004 a vertically deintegrated company, not only in manufacturing, but also in the three other main activities that constituted its value chain: research and design, logistics and distribution, and sales. The company relied on external people and companies for the major part of its crucial activities. It employed some 400 people at the end of 2004. The research and design of new electronic equipment was done outside the company by a number of international freelance electronic engineers. Daniel Sembatya, with a staff of about 20 people in the Product Development Department, interpreted the 'look' created by the electronic engineers and performed the modelling phase. More than 80% of manufacturing was now done outside the company, by 35 sub-contractors that employed about 1,100 people. In-house production accounted for the remaining less than 20% (mainly sophisticated and proprietary processes which were critically quality sensitive) and was performed by 70–80 people.

Logistics and distribution activities were also performed mainly by outsiders. The company, however, managed the storage phase by using a single, huge warehouse for finished products. In addition, the Logistics Department at Stargate Telecoms Ltd was in charge of delivering the finished electronic equipment to the stores all over the region. Finally, the company utilized an external sales organization of almost 80 dealers which took care of a retailing system of the nearly 200 shops spread all over the region. The internal part of this activity was performed by seven area managers, who coordinated the selling system as a whole divided by territories. The large volume of business done by the company required that production planning for telecommunications and computer items were carried out in advance of delivery to the stores. Roughly, 21 months elapsed from the research and design of electronic items for a particular selling season to the delivery on the shop shelf of a particular item.

Basic steps in the production cycle were: preparation of final designs; assembly of a few samples of each of the 60 electronic items in the total collection; a 'pre-presentation' seminar was then held between Daniel Sembatya and manufacturing managers and some of the company's 80 dealers, which eliminated about a fourth of the models. The remaining models were then produced in small quantities for presentation by area managers to dealers and by dealers to store owners. Upon receipt of the first orders, the planning department 'exploded' a rough production plan for the year. Purchases were

made according to this plan, and capacity with the sub-contractors negotiated. Finally, production was started and deliveries begun just in time for the sales launch. Sales were scheduled so that each store could present up to 70 per cent of all items in its stock display to its customers at the outset of the launch of each batch of new products.

As Stargate Telecoms Ltd moved into new geographic areas the complexity of operations grew incessantly, because the best dealers for different areas tended to carry out many other businesses which were not related to Stargate's main business line. The company was now divided into three major divisions: home electronics, telecommunications and computers. In 1993, Stargate Telecoms Ltd had seven plants in East and Central Africa. In 1995, the number of plants decreased to four and in 2004 the company owned just three production units, one for each major business line. The reason for this reduction was simply a matter of the company's philosophy of vertical deintegration and external production as a mode of organization. All those divested plants acted in 2004 as Stargate Telecoms Ltd sub-contractors.

The early 1980s had seen the development of Stargate Telecoms Ltd's perhaps most widely publicized production technique: the robotic assembly of electronic equipment rather than human soldering and joining. Up to then, it was the electronic parts that were delivered to the factory and then assembled by workers. Stargate Telecoms Ltd discovered that, to a large extent, the critical factor was quality and durability and decided, therefore, to assemble a large part of their production using vacuum contained robots. They thus avoided poor quality production and ensured they could meet demand for the 'best hits' of the season. The process was socially undesirable but had the advantage of allowing production to respond quickly to public demand on reliability and price. It also allowed the company to maintain almost no inventory, and to produce mainly to order. The company kept 100% of the packaging and quality control phase internally.

In addition, quality control and packaging was both the most complex and the most upfront process in the business to leave it to risky external sub-contractors. Before the packing phase, every electronic item had to pass through a testing process to ensure that it was working. This phase was also a labour-intensive but, technically speaking, was not as sophisticated as research and design. This phase did require particular machinery for diagnosing failed parts in each component in case there were defects. It was split in two parts: quality control of each single electronic item and packaging.

Some Problems in the Stargate Telecoms Ltd-Subcontractors Relationship

Mr. David Luggya, the managing director of one of the largest external firms which Stargate Telecoms Ltd subcontracted and an important equity position holder commented;

"The main problem in working for Stargate Telecoms Ltd is the great number of changes in electronic items etc. they produce in a very short time. We have to adjust the machines weekly or even nightly to follow all these changes. This means a large number of different electronic items produced in small batches each, which, from a manufacturing point of view, is very inefficient."

This sub-contractor also complained about the machinery suggested by Stargate Telecoms Ltd. In his opinion, they had a **product orientation** instead of a **'process orientation'**, not taking into account the productivity or the suitability of the machinery available to the sub-contractors. Thus, he maintained, that the machinery suggested by the company was often more suitable to a 'craftsman making designer gadgets rather than to an industrial concern mass producing the electronic equipment'. Sub-contractors ran a big risk when they decide on the purchase of a certain type of machine. The key factor that determines the usefulness of the production machines is the versatility with which they could be adjusted to assemble different parts/products.

Indeed Stargate had experienced some problems of this type in the past because some sub-contractors had been stuck with machines that were useless for the current electronic production trends. The firm had facilitated the change of the machines either by buying them or by allowing the contractors wide margins so they could reinvest this money in new machinery.

Because of this dissatisfaction and criticism, Stargate Telecoms Ltd tried to retain in-house the most expensive and technology-dependent activities. Mr. David Luggya on the other hand realized that working exclusively for Stargate Telecoms Ltd involved a risk, but on the other hand it had the advantage of allowing them to dispense with a sales and marketing department:

"The constant work provided by Stargate Telecoms Ltd enables my company to concentrate on manufacturing, with just a few people in charge of administrative and financial tasks. Working only for Stargate Telecoms Ltd means one invoice per month, fixed payment conditions, etc. We often receive requests from potential clients, but I'd rather work this way."

But some Stargate executives did not share the sub-contractors point of view. This lack of empathy was best illustrated in the person of Mr. Muhangi, head of the telecommunications division. He pointed out that:

"one of the main problems in working with external firms is to achieve the flexibility in them. They have to completely adapt to Stargate Telecoms Ltd demands in terms of working periods, designs and quality demands etc."

Another Stargate Telecoms Ltd executive voiced this concern: that this was neither a 'just in time' system nor a very scheduled one.' Sub-contractors normally worked 8 hours a day, but when the company was in a hurry they had to work over the weekend, and 12 or more hours a day. One of the highlights of the company's network of sub-contractors was described by Mr. David Luggya as follows:

"Stargate Telecoms Ltd maintains a sort of "umbilical cord" with external contractors. They are considered part of our family, and feel confident in telling us their problems. Plant managers knew personally each sub-contractor and some of them even became friends, to the point that they talked about their personal problems and sought advice from the company."

Manufacturing people visited sub-contractors very often. In addition, they were permanently in touch by phone. This daily communication allowed them to work in real-time, solving little problems and making production adjustments. According to the firm, the less experienced the sub-contractor in the electronic industry, the better it would adjust to Stargate Telecoms Ltd's philosophy. It was more difficult to create this 'umbilical cord' with people that had previously worked for other big firms. An experienced contractor tried to impose its conditions before starting the relationship. Finally, there was a strong identification with Stargate Telecoms Ltd, not only within the company but also among sub contractors' employees.

High-tech Production Processes

Many experts in the electronics industry agreed that the Stargate Telecoms Ltd success formula was based on the company's ability to combine cutting edge research with advanced technology. Samuel Sembatya confirmed this in an article that appeared in the Uganda Investment Authority magazine, the 'Investor':

"There are many elements to our success, but the real point is that we have kept the same strategy all along to put quality and reliability on an industrial level. Most of the rest of African electronic design is still at an

artisan level. We are at the leading edge of technology and our aim is to stay there."

For production, Stargate Telecoms Ltd used numeric control processing machines linked to DELL computer-aided-design (CAD) personal computer terminals. Designers using the ten CAD terminals could play around with electronic designs on a video screen. Once a designer decided on a particular design, the computer prepared a JPG image that was saved and could direct the robotic production line to produce the parts, in an easy-to-assemble form of cojoinable parts. Since 1999, they had also used a FOTOGENIX CAM system which they had connected to an Indian-made auto-cam recorder, turning the system into a CAD—CAM unit. The FOTOGENIX CAD—CAM system's automatic design camcorder followed design pieces stored in the software architect's computer memory, which could record up to 1,500 design processes in various stages and also produce images for production.

The quality control phase was a high-tech process too. At the factory, workers would test the prepacking electronic equipment in about five different diagnostic systems for any problems before dispatch to the warehouse. This process was critical because it prevented having many sales returns resulting from defects. Stargate also had a zero defect tolerance policy.

Logistics

Logistics played an important role in the Stargate Telecoms Ltd strategy. Stores carrying Stargate Telecoms Ltd products were designed with limited storage space for back-up stocks. Upon arrival at the store direct from the company, merchandise often was checked and directly placed on the display shelves. This required both a carefully prepared schedule of deliveries to stores, and a large and efficient warehouse to store finished product at headquarters. The new robotized warehouse in the Namanve Industrial Area, the main symbol of Stargate Telecoms Ltd's high technology, became fully operational in February 2003. At a cost of over UGX 420 million to build and outfit, the warehouse was a huge automatic box run by an IBM minicomputer which directed several robots via remote control. The robots could read bar codes on boxes, and then sort and store them. The operation of the warehouse was totally automated and there was no human handling in the whole process. A staff of five specialists monitored the movements via computer screen.

Marketing, Retailing and Advertising

There were three groups of actors involved in selling activities: the company, the dealers and the shop owners and managers. Although nominally a member of the Board, the real Marketing Manager was Samuel Sembatya, who in the past

had formally occupied this position many times. Under him, the Commercial Director and Area Managers composed the marketing department. Nearly all the members of the commercial organization had been hired by him, and were used to working directly with him. Area managers were company employees in charge of territories run by a number of dealers. There were seven areas for the nearly 80 dealers. Richard Mwami, the Area Manager in charge of the Rwanda, Congo and Burundi once described one of the tasks of an area manager in the following disparaging terms:

"He does every month what dealers do every day: have a look at each shop and its problems. We are always watching the movement store by store. Sometimes we talk directly with shop owners, although dealers don't like that. But they need to hear the voice of the company from time to time."

Mr. Mwami went to the Western region of the Stargate operations once a month and talked almost daily with every dealer on phone. Another important task an area manager performed was the collection of the money from the shops. On average, an area manager devoted 40% of his time to following up payment problems. His rush periods were March to April in the Easter Season and November to December in the Christmas season.

Mr. Manuelli Opoka was the super dealer for the north-east region of East and Central Africa. He had joined the company in 1989 as the manager of the second shop opened by the company in Bakuli. He had worked with Samuel Sembatya in a car repair shop when they were teenagers. Mr. Opoka explained the criteria for selecting a person as a dealer in the following terms:

"The candidate had to have an enthusiastic predisposition towards the work itself. The boss was looking for people who could be potential consumers rather than dealers, who could understand the product and its quality, and believe in it."

The main responsibilities of the super dealers were:

1. To select the location of new shops.
2. To find and select potential investors for new shops.
3. To help new clients in starting shops and train them, usually in the dealer's stores.
4. To look at the shops and help owners to manage and control their shops.
5. To present the collection to shop managers and help them in choosing goods.
6. To collect orders and transmit them to headquarters.
7. To encourage image competition among shops.

Dealers were also encouraged to reinvest part of their commissions in opening new shops, thus becoming clients themselves. This mechanism produced a 'self multiplying effect' in the retailing network. This policy of encouraging dealers to have and run their own shops helped them to get first-hand knowledge of the retail business and its problems in practice. For instance, Mr. Opoka owned 12 shops out the 40 he supervised in the north-east of the region. More than competitors, the shops owned by him served as examples to the shops recently opened in such things as products display, overall image, etc. Besides this, according to Mr. Opoka, the concentration of shops in an area of a town, instead of reducing the sales of each one, tended to increase them. What was not clear was how Mr. Opoka's other business interests conflicted with his role as super dealer and agent.

Fewer than fifteen of the Stargate Telecoms Ltd stores region wide were owned and operated by the company. These were located in key cities such as Kampala, Nairobi, Dar es Salaam, Kigali, and other big urban cities. The rest were set up by independent entrepreneurs, some of whom often owned several shops in the same area. Stargate Telecoms Ltd approved location of the shops and Samuel personally oversaw the more strategic sites. Shop owners were not retail experts. As Samuel Sembatya put it:

"We have caused a new type of retailer to become important who until the day before was perhaps a takeaway or salon operator. Their prior career is of no importance but they must have the right spirit to work in a Stargate Telecoms Ltd shop."

Mr. James Muwalimu, Area Manager for the North East region, commented: "Experts in retailing are not good shop owners (and managers) because they don't understand very well the particular Stargate Telecoms Ltd system." When asked about this 'system', he mentioned the following characteristics:

1. a new window display every week,
2. good sales people in stores, good service,
3. competition of image among shops (window decoration, gadgets, diversity and display),
4. no price competition (initial prices set at factory or strongly suggested) and
5. all markdowns discussed with dealers before being offered.

Turnover among shop owners was low. For example, of the 40 shops controlled by Mr. Opoka in the northeast of the operating region, only 3 shop owners had been replaced in a period of 10 years.

Retailers/dealers originally did not sign franchise agreements as Samuel Sembatya, the founder, hated bureaucracy. Also, they were neither required to pay Stargate Telecoms Ltd a fee for use of its name nor a royalty based on a percentage of sales or profits. Therefore, the term 'franchising' in describing the Stargate Telecoms Ltd retailing network was a misnomer.

All Stargate Telecoms Ltd outlets were required to follow basic merchandising concepts. The most important among them being that all merchandise must be displayed on open shelves accessible to customers, who could touch it and switch it on. The open displays in an otherwise undecorated space created an impression of great freedom to the window-shopping customer. Important also was the selection of adequate salespeople; they must be young and very customer-oriented. They had to be able to advise the customer on which electronic equipment best suited their needs. Stargate Telecoms Ltd used five mechanisms to control its 'identity' in spite of the dramatic increase in the number of shops:

1. Standardization of the shop image. Retailers had to choose among 12 basic layouts and fixture selections. This furniture must be provided by only one of three contracted suppliers, located near headquarters.
2. Central supply of advertising material, which was produced at headquarters and shipped to the shops all over the region. Shops were allowed to do some advertising in local media (mainly newspapers) after the company had checked the advertisement.
3. A strict pricing policy. The marketing people back at Stargate printed the price in local currencies in each country to attach to every item.
4. Stargate Telecoms Ltd shops could only sell Stargate Telecoms Ltd products.
5. Assistance to new clients.

Employing one advertising agency in each country, the company had coordinated its advertising region wide. Since the products were all from one source, there was consistency in character all over the region. The company was therefore able to maintain the consistency and international character of its advertisements. About 4% of Stargate Telecoms Ltd's revenues were spent on direct advertising. Additionally the company sponsored sports events, including football, rugby and golf.

Information Systems (IS)

The Information Systems Department had committed itself to using the best IS available but had not focussed on the sub-contractors' network. The IT department had a huge demand from its resources and had not been able to focus outwards to its external customers as opposed to internal customers.

Because of rapid growth, the IS systems required restructuring to cope with new demands and this was straining its capacity to add value to the business. Thus while there was good internal connectivity, the policy on a business wide intranet seemed to be undefined. The IT Manager claimed that he was waiting for the moment when the company would decide which of the stakeholders in its huge network were strategic for connectivity purposes. His argument was that there were too many satisfactorily and most of them were too small for the IT Department to connect and service stakeholders. There was just no way to satisfy everybody and if IT focussed on external customers, it would have no specific objectives. Therefore, Stargate Telecoms Ltd did not know the exact IT requirements of each sub-contractor at any given moment and support was slow. With changes in the Sub-contractors' Network, Stargate Telecoms Ltd hoped it would help improve service levels and the IT Department was considering installing a network for a limited constellation of sub-contractors if a policy position was defined. The idea was to simplify the complex problem of being in touch with so many external firms, and deal only with the 9 or 10 largest sub-contractors. These in turn would be in touch with all the medium-sized and small contractors. To control those contractors better, Stargate Telecoms Ltd would still own all the proprietary rights relating to the software and also spend a considerable amount of money on software development. The decision facing management was whether to purchase outright or lease the software (Exhibit II).

Financial Matters

The company, which had now been publicly traded for a while, had been performing well. Newcomers to the industry, especially i-Tel, had been gobbling up its stock for a while, unbeknown to the Board. Because the industry was becoming more and more lucrative, i-Tel Ltd which quickly wanted to reinforce its international position in the industry had adopted a predatory position. One of the problems Stargate was facing was that the founders had not put in place a good succession plan for the Board despite their tremendous success. Thus as more business savvy investors were entering the market, the older Sembatya brothers were not able to keep apace. Yet the structure of the Board had remained unchanged for the last, ten years with no new fundamentally business shaking ideas being introduced. The abridged financial statements of the company for the last two years are attached as exhibit III.

EXHIBIT I: The Stargate Conceptual Business Flow Chart

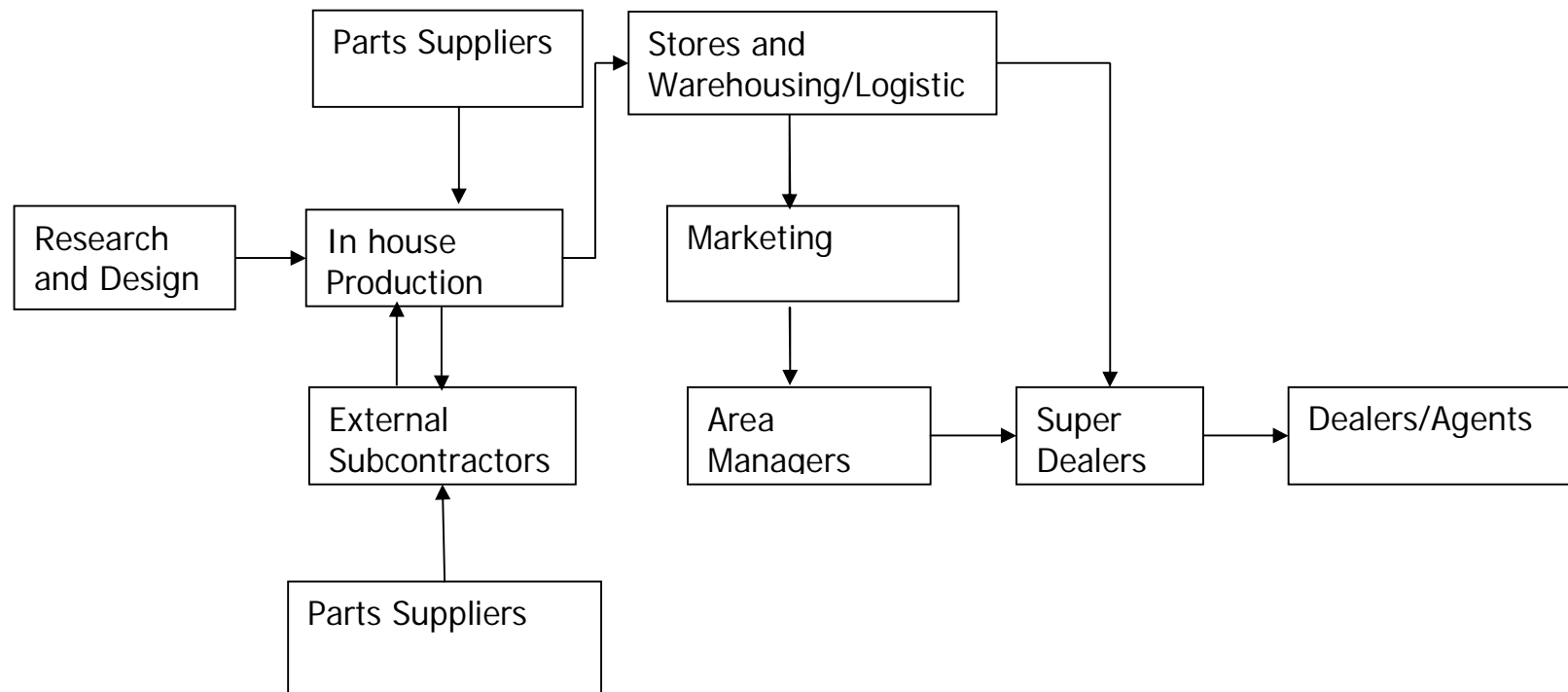


EXHIBIT II: Buy or Lease?

Management of Stargate Telecoms Ltd obtained details with the regards to the software decision. The software would cost Ushs 6.4 Billion and would have an economic life of five years. It is envisaged that with this software installed the operating costs of the company will reduce by UGX 2.1 billion per annum. There are new liberal Capital allowances of 25% per annum on declining balance basis claimable for investments in software of such a type. Taxation of 30%, however, will be payable on operating cash flows one year in arrears. It is considered that a discount rate of 20% would reflect the risk of this kind of project's operating cash flows.

Stargate intends to finance the new software by means of a five-year fixed interest loan at 18% per annum repayable in five years time. As an alternative DFCU Leasing Ltd has proposed a finance lease over five years at UGX 1.5 billion per year payable in advance. It is anticipated that the scrap value under each of the financing alternatives will be zero.

EXHIBIT III: Financial Highlights**Consolidated Balance Sheet as of 31 December 2006**

Assets	2006	2005
	UGX '00,000	UGX '00,000
Current Assets	833,192	494,891
Investments	5,431	6,372
Non-Current Assets (net)	134,636	80,335
Intangible Assets	<u>15,548</u>	<u>10,215</u>
TOTAL ASSETS	<u>988,807</u>	<u>591,813</u>
Liabilities and Share Capital		
Current Liabilities	373,663	317,203
Long-term Liabilities	251,148	76,730
Capital Gains Roll-over Reserve		130
Minority Interest in Consolidated Subsidiaries	2,437	4,742
Share Capital and Reserves	<u>361,559</u>	<u>193,008</u>
TOTAL Capital & Liabilities	<u>988,807</u>	<u>591,813</u>

Consolidated Income Statement for the Year Ended 31 December 2006

	2006	2005
	UGX '00,000	UGX '00,000
Revenue	1,079,060	879,535
Cost of sales	<u>701,818</u>	<u>558,501</u>
Gross profit	<u>377,242</u>	<u>321,034</u>
Selling, general and administrative expenses	169,303	150,653
Income from operations	207,939	170,381
Other (income) expenses	1,878	6,368
Gain from Disposal of Investments		3,198
Income taxes	(87,008)	(69,788)
Deferred income taxes	<u>(5,468)</u>	<u>-</u>
Income before minority interest	113,585	97,423
Income to minority interest	<u>(556)</u>	<u>(1,226)</u>
NET INCOME FOR THE YEAR	<u>113,029</u>	<u>96,197</u>

Table 1: PVIF- Present Value of Shs 1 Due at the End of n Periods

Period	9%	10%	11%	12%	13%	14%	15%	16%	18%	20%
1	0.917	0.909	0.901	0.893	0.885	0.877	0.870	0.862	0.847	0.833
2	0.842	0.826	0.812	0.797	0.783	0.769	0.756	0.743	0.718	0.694
3	0.772	0.751	0.731	0.712	0.693	0.675	0.658	0.641	0.609	0.579
4	0.708	0.683	0.659	0.636	0.613	0.592	0.572	0.552	0.516	0.482
5	0.650	0.621	0.593	0.567	0.543	0.519	0.497	0.476	0.437	0.402
6	0.596	0.564	0.535	0.507	0.480	0.456	0.432	0.410	0.370	0.335
7	0.547	0.513	0.482	0.452	0.425	0.400	0.376	0.354	0.314	0.279
8	0.502	0.467	0.434	0.404	0.376	0.351	0.327	0.305	0.266	0.233
9	0.460	0.424	0.391	0.361	0.333	0.308	0.284	0.263	0.225	0.194
10	0.422	0.386	0.352	0.322	0.295	0.270	0.247	0.227	0.191	0.162
11	0.388	0.350	0.317	0.287	0.261	0.237	0.215	0.195	0.162	0.135
12	0.356	0.319	0.286	0.257	0.231	0.208	0.187	0.168	0.137	0.112
13	0.326	0.290	0.258	0.229	0.204	0.182	0.163	0.145	0.116	0.093
14	0.299	0.263	0.232	0.205	0.181	0.160	0.141	0.125	0.099	0.078
15	0.275	0.239	0.209	0.183	0.160	0.140	0.123	0.108	0.084	0.065

TABLE 2: PVAF - Present Value of an Annuity of Shs 1 per Period for n Periods

Period	9%	10%	11%	12%	13%	14%	15%	16%	18%	20%
1	0.917	0.909	0.901	0.893	0.885	0.877	0.870	0.862	0.847	0.833
2	1.759	1.736	1.713	1.690	1.668	1.647	1.626	1.605	1.566	1.528
3	2.531	2.487	2.444	2.402	2.361	2.322	2.283	2.246	2.174	2.106
4	3.240	3.170	3.102	3.037	2.974	2.914	2.855	2.798	2.690	2.589
5	3.890	3.791	3.696	3.605	3.517	3.433	3.352	3.274	3.127	2.991
6	4.486	4.355	4.231	4.111	3.998	3.889	3.784	3.685	3.498	3.326
7	5.033	4.868	4.712	4.564	4.423	4.288	4.160	4.039	3.812	3.605
8	5.535	5.335	5.146	4.968	4.799	4.639	4.487	4.344	4.078	3.837
9	5.995	5.759	5.537	5.328	5.132	4.946	4.772	4.607	4.303	4.031
10	6.418	6.145	5.889	5.650	5.426	5.216	5.019	4.833	4.494	4.192
11	6.805	6.495	6.207	5.938	5.687	5.453	5.234	5.029	4.656	4.327
12	7.161	6.814	6.492	6.194	5.918	5.660	5.421	5.197	4.793	4.439
13	7.487	7.103	6.750	6.424	6.122	5.842	5.583	5.342	4.910	4.533
14	7.786	7.367	6.982	6.628	6.302	6.002	5.724	5.468	5.008	4.611
15	8.061	7.606	7.191	6.811	6.462	6.142	5.847	5.575	5.092	4.675