

THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD
A Committee of the Council of ICPAU

CPA (U) EXAMINATIONS

LEVEL THREE

BUSINESS POLICY AND STRATEGY - PAPER 14

MONDAY, 7 DECEMBER 2009

INSTRUCTIONS TO CANDIDATES

1. Time allowed: **3 hours 15 minutes**.
The first 15 minutes of this examination have been designated for reading time. You may not start to write your answer during this time.
2. Section **A** has **one** compulsory question carrying 50 marks.
3. Section **B** has **three** questions and only **two** questions are to be attempted. Each question carries 25 marks.
4. Please, read further instructions on the answer book.

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SECTION A

Question 1

Kikaaya Hospital is a national referral hospital located in Wakiso District. It is the oldest hospital in the district, and used to be the best hospital in the country. Back then, the hospital used to have modern facilities, and served a low population. Further referrals (cases which could not be handled at the hospital) were less than 7% of the general patient numbers attended to. A big portion of the revenue was from the central government in the form of grants through the Ministry of Health. Nominal fees were also charged based on actual surgical and medical services provided to the private patients. Central government grants accounted for about 80% of total revenue.

Lately, the hospital has been faced with financial difficulties. Senior management have, so far, failed to agree on a way forward. Operating costs have risen due to inflation, rising costs for medicines, salaries and medical equipment. Given the current global events, revenue from central government is under a lot of pressure as revenue authorities continue to declare shortfalls in revenue collection. As per the budget speech presented by the minister for finance on 11 June 2009, government priorities have shifted to a reduction in public expenditure, including health care. This is hitting the hospital hard.

To worsen matters, the hospital has failed to attract private patients. Corporate clients are opting for the up coming private clinics and hospitals to take care of their employees' health insurance. These private clinics generally have better reputation for patient care and more attractive "state of the art" facilities. Ironically, given the scarcity of medical doctors in Uganda, some of the staff at Kikaaya hospital are part-time employees in the competitor clinics. Consequently, private income for the hospital is forecast to drop even further. *(Selective financial and comparative performance data for the two hospital categories can be seen on page 4)*

As per the annual report for the year ended June 2009, the Board of Directors estimated that if the situation did not improve, Kikaaya Hospital would have a deficit of Shs 75 billion within three years. They therefore called for urgent action! Unfortunately, the board was divided on the way forward for the hospital. The two proposed options were:

- major capital investment to enhance the facilities.
- reduction in capacity so as to offer better services.

The board comprised of the powerful executive director (also Board Chairman), two representatives of the medical staff, two local councillors and a representative from the ministry of health. All these were split into a number of factions.

The first faction was led by Kibuuka Mohamed, the executive director of the hospital. He was an administrator and an accountant by training. His concern was that Kikaaya Hospital should be run efficiently. To him, and his fellow administrators, it was important that the hospital should be financially viable. However, efficiency and effectiveness are not always the same thing. In fact some of the actions taken may also lead to further ineffectiveness or inefficiencies elsewhere. An indication of this dilemma was the administrators' wish to reduce the length of time "in patients" spent in hospital so as to reduce costs, as well as a proposal to reduce hospital beds. However, sending patients home early could result in them requiring home visits from nursing staff for up to four or five extra days, and in some circumstances this early release could require re-admission to the hospital. Consequently initial savings might be eroded by further unanticipated costs. The administrators, according to most medical staff, were more concerned with short-term financial concerns than with medical ones.

The second and largest group was represented by Bukuku Ndungu, a consultant surgeon. This group wanted the introduction of modern surgery, just like in the private clinics. To them, the cause of the problems was the failure to match the facilities offered at competitor clinics and hospitals. However, substantial investments in equipment and other facilities would be required. These people also had hidden financial interests. All together as a unit, medical staff had been complaining about poor salaries for a long time, and had even threatened to go on strike on several occasions.

The third group was led by a local councilor in Wakiso District. The group comprised of other councilors who were not even board members. This group wanted the hospital to remain open for as long as possible, without any change in the pricing structure; in fact they advocated for price reductions! Ironically, these were the same councilors who had supported the government's decision to reduce funding for the hospital.

Naturally, the local population within Wakiso wanted the hospital to continue its function as a viable concern and even invest in more modern facilities. Unfortunately this stakeholder group had little power or influence. The residents of Wakiso were socially disadvantaged and were unable to bring any concerted pressure to bear fruit on the hospital's decision-makers.

As hinted on in the annual report 2009, the board of directors found it difficult to agree upon an acceptable strategy to solve the financial crisis. Commentators argue that the options on the table somewhat reflect the influence of the high ranking medical staff. Medical staff had even threatened to quit the hospital and

concentrate on their private clinics unless the board agreed to a capital investment programme designed to enhance the hospital's reputation.

It is argued that the second alternative (as proposed by the administrators) involving a reduction of hospital beds so as to offer better facilities for a lower number of patients is unacceptable. This option would greatly disadvantage the poor who cannot afford the private clinics, yet Kikaaya was a national referral hospital.

You have now been engaged as management consultant to advise on the way forward for Kikaaya Hospital. *"We work in a difficult environment where politics sometimes overrides objectivity..."* is a comment made by the Permanent Secretary, Ministry of Health, as he escorted you out of the ministry's boardroom. This was at the end of your entry meeting for the assignment.

Selected financial and performance data from Kikaaya Hospital and Karen Hospital, a leading private hospital in Wakiso for the year 2008:

	Kikaaya	Karen
Income from government (Shs billion)	24	-
Income from private patients (Shs billion)	1	2.5
Income from corporate clients - medical insurance (Shs billion)	<u>2</u>	<u>73</u>
Total income (Shs billion)	27	75.5
Labour costs (Shs billion)	15	20
Medical equipment (Shs billion)	10	18
Drugs (Shs billion)	2.5	5.5
Other variable costs (Shs billion)	10	13
Fixed costs (Shs billion)	15	17
Total costs (Shs billion)	<u>52.5</u>	<u>73.5</u>
(Deficit)/Surplus (Shs billion)	<u>(25.5)</u>	<u>2</u>
Further referrals (% of referral cases)	13	4
Average no of staff	900	700
No of beds	350	450
Average waiting time (days)	66	28
Readmission rates (% of inpatients)	7	1

Required:

- Identify the major problems facing Kikaaya Hospital, and discuss the extent to which the proposed solutions would address these problems.
(25 marks)
- Propose and assess any other strategic options that the board of directors could have considered.
(10 marks)

- (c) What factors would enable the medical staff to push through their desired course of action?

(5 marks)

- (d) To what extent could the other stakeholders have argued against the chosen strategy of the medical staff and pushed through their own objectives?

(10 marks)

(Total 50 marks)

SECTION B

Question 2

When Mpiima, 30, a mid career professional quit his marketing job at a multinational company, he knew he was about to start living his dream. This was in 1990 when he opened the first ever advertising agency in Uganda. Eighteen years down the road, all his efforts seem to have been worthless unless something is done. Mpiima was a daring guy who opened up a small office on Kampala road, where he initially conducted his business with just one administrative assistant. Over the years, however, he had built Mpex Advertising into a force to reckon with. At its peak, Mpex Advertising was operating under a franchise arrangement with Mpex International, a seasoned European marketing / public relations company. This arrangement enabled Mpex Advertising to win over multinational clients. Mpiima had also created a small but very innovative team of staff, some of them expatriates from his European business counterparts. These were the people behind market conquering campaigns like the revival of Coka (U) Ltd (a soft drinks company), launch of a communications company as well as a beer campaign in the mid 1990's. Mpex Advertising was dictating the tunes as far as advertising was concerned and there were no complaints from their corporate clientele.

The liberalisation of the radio airwaves in the mid 1990's set in motion an unbelievable wave that swept the FM airwaves in Uganda. Several FM stations opened, and with them came the music revolution. In the words of one music producer, "*Uganda virtually kicked out Congolese music.....*" With the increasing production of Ugandan music, and the media's "creation" of Ugandan celebrities, Mpex Advertising's position started to be threatened. What started as informal arrangements between musicians and corporate companies now turned into formal advertising contracts. Subsequently, the musicians, as well as other Ugandans set up advertising/media companies bypassing Mpex Advertising in the process. Their biggest competitive strength was the fact that they used local celebrities to endorse their customers' products, while the more expensive Mpex Advertising relied on studio generated adverts. Among the new companies were a few big players that did a lot more than just advertising. Their product range

went as far as public relations management, social responsibility and branding support.

In 2004 Mpex Advertising lost its franchise with Mpex International amid accusations of unpaid royalties and unethical practices of soliciting government business. Around the same time, they lost most of the core creative staff to a local competitor, and with them went the only remaining corporate clients; Meembo Mobiles Ltd and Seelo Uganda, a leading fuel company.

It is now evident that Mpex Advertising is on its knees and it is just a matter of time before its doors are closed for the last time.

Required:

- (a) What factors could explain the fall of Mpex Advertising?
(9 marks)
- (b) Using the five forces model, comment on the status of competition in the advertising industry.
(12 marks)
- (c) What were the advantages and disadvantages of the growth strategy used by Mpex Advertising?
(4 marks)

Total 25 marks

Question 3

Kampala Furniture Mart is a leading maker of furniture in Kampala. Most of its furniture is customized according to customer requirements. For the past five years, company records show that 70% of the furniture sales are customized items. However, some standard items are made with a few of them displayed in the showroom, the rest kept in the store. On average, standard items spend up to 6 months in the stores. This practice has constrained the company's storage facilities because the storeroom has to be used for timber and other supplies.

There is a reasonable degree of automation in the furniture making process, even though manual intervention is common. A new managing director took over recently but is not sure about the ideal production system at Kampala Furniture Mart. He is torn between implementing a wholly product focused system and a wholly process oriented system. He has now approached you for your opinion as the production manager.

Required:

- (a) Distinguish between a product focused and a process oriented production system, clearly showing which option is appropriate for Kampala Furniture Mart.

(7 marks)

- (b) Under what circumstances is it ideal to implement a:

- (i) product focused productive system?

(9 marks)

- (ii) process oriented productive system?

(9 marks)**(Total 25 marks)****Question 4**

Carol Nabunya is the managing director of Abby Micro-finance Ltd, a company specializing in financial services. The company has had five offices in different geographical locations within Uganda, and is a popular source of finance for small and medium-size enterprises. Its major products range from short to medium-term loans. In a bid to increase market share, the company recently tookover another micro-finance company; Back Page Micro-finance Ltd. Since then, it has been able to tremendously expand its branch network to over 30 branches. According to the Uganda Micro-finance Union, Abby Micro-finance Ltd is now the second largest micro-finance institution in the country, in terms of branch network and customer base. The management style and work culture in Back Page Micro-finance Ltd was different from that in Abby Micro-finance Ltd. Therefore, there has been a clash of cultures after the acquisition.

Staff in the acquired company are also low on motivation with rumours that they are going to be retrenched, despite assurances from management. There are also reports that some of the recent system malfunctions are a result of sabotage from former staff of Back Page Micro-finance Ltd.

Carol is naturally concerned that the acquired company might not be successfully integrated.

Required:

- (a) Assess the factors which need to be taken into consideration if a newly acquired company is to be successfully incorporated into the group.

(15 marks)

- (b) What synergies could have driven the above acquisition?

(10 marks)**Total 25 marks**