MAY 2021 PROFESSIONAL EXAMINATION
STRATEGIC CASE STUDY (PAPER 3.4)
CHIEF EXAMINER'S REPORT, QUESTIONS & MARKING SCHEME

EXAMINER'S GENERAL COMMENTS

This examination was based on a pre-seen scenario which described **Savior Box Limited (SBL)**, a pharmaceutical company. Started as a family business and has since grown into a pharmaceutical empire. Market leader in its home base Ghana with expansion into West African market with ambition to become a global organisation. SBL business model is operating three divisions: manufacturing, retailing and distribution and export. Decision making was rooted in its development history as a family business hence number of challenges. As a result of the challenges, the management board decision to hire a consulting firm Blessed Consulting and seconded a dedicated staff called Bismark with relevant experience for four months to support with transformational change management. The scenario was made available in advance of the exam. This is a very interesting industry and students are expected to be familiar as part of preparation toward the examination. The pre-seen was detailed and well-prepared candidates should have been able to give good answers in the context of the pharmaceutical industry. The unseen scenarios were interesting and presented some realistic questions on the industry. The standard of the paper was extremely good, and the questions were clear with preambles to assist candidates. The coverage was broad and in line with the syllabus the paper was heavy on the strategic application. All the questions were based on the recommended syllabus and study material of the Institute. The standard of the paper also shows remarkable improvement over the previous three exams diets since the Institute of Chartered Accountant (Ghana) introduced the Case Study in November 2019. Marks allocation followed the weightings in the syllabus and was fairly distributed to each question.

PERFORMANCE OF CANDIDATES

Again, the trend of performance did not change much with few candidates marginally performing well. Many appeared to be ill-prepared for this examination and did not demonstrate the required level of technical knowledge and application of knowledge to the case study. Overall, candidates performed well below average especially questions number one and two. There were a number of concerns relating to student performance in several other areas. This applies to most of the questions except question four (Balanced Scorecard critical success factor (CSF)) application question. In many cases candidates described wrong strategic models despite the fact that the questions required specific models. Model application to the case study remains a challenge to candidates resulting in losing valuable marks to achieve a pass. All answers must be applied to the case study and should bring in aspects of the pre-seen information as well as the information and appendices in the unseen additional information material. Answers which are purely rote learning were quite common in some requirements and this approach is awarded very low marks. There were also a number of candidates who gave very theoretical answers and did not apply them to the case study. Many candidates' answers lacked depth of development and therefore, although demonstrating a basic understanding and application of knowledge, they failed to accumulate sufficient marks due to not developing their answers sufficiently. Some answers were just short and incomplete.

NOTABLE STRENGTHS & WEAKNESSES OF CANDIDATES

Strengths

The candidates did well in the balanced scorecard's four perspectives requiring identification of critical success factor and outcome measurement. Most of the candidates answered the question and scored above 60% of the 20 marks allocated to the question. Number of candidates related their answers to the case study.

Weaknesses

Poor preparation by the students. The compelling evidence from the scripts points to poor preparation on the part of the candidates. The students scored very low marks because the answers provided were very shallow in terms of meeting the exact requirements. A good number of the students failed to answer all questions because they were not prepared, with over 80% of candidates not attempting all question.

Despite the fact that appendixes provided worked out financial ratios and vital industry statistics as part of the pre-seen material, candidates failed to apply them to the relevant questions and rather resorted to recalculating the same ratios and statistics again resulting in waste of precious exams time. About 75% of the candidates who attempted question one scored zero while a significant number did not answer them at all.

Poor or limited understanding of questions. The scripts revealed that students deviated in answering some of the questions. This problem was common with questions that demand application of some basic concepts. The questions that suffered most in this regard were question one, seven and eight which essentially required students to explain to SBL management board critical skills sets or business strategic models to support and facilitate analysis of competitive advantage of the organisation. Most students who attempted it deviated.

Most candidates ignored the allocation of marks to questions which resulted in poor time management especially question number five.

Poor use of language. The examination scripts were characterised by poor English language construction and avoidable spelling mistakes. This affects the quality of the answers provided by some candidates. The problem of poor use of English language has featured in the previous Chief Examiners' reports. The candidates are encouraged to use language appropriately.

LOOKING AHEAD OF FUTURE EXAMINATIONS

Candidates should read the pre-seen material carefully and come into the examination with understanding and mind map of the industry and the company which will be the focus of the exam. This will help candidates formulate good answers that relate to the tasks they are given. Candidates must manage their time well and make sure they do not run out of time on questions they know well at the expense of others. Candidates must answer what is being examined, read the questions very carefully, plan and answer what has been asked. Answers which are not applied to the case will not score high marks.

PRE-SEEN MATERIAL

INTRODUCTION

Savior Box Limited (SBL), a private limited liability company, was established in 1974 by James Mensah, a Chemist, who had spotted the opportunity to distribute Over the Counter (OTC) drugs in his local area. James had no ambition to extend the business, seeing it as a means of making enough money to enjoy life with his family. When James retired, his son Edwin Mensah who has been associated with the business since childhood, took over. Edwin has known most of the staff, suppliers and local customers for much of his life.

In the last ten years Edwin took over, the business has grown into a pharmaceutical empire with manufacturing, retailing & wholesale distribution and export. It still focuses on pharmaceutical products but now supply companies across the whole of West Africa and beyond. In recent years, he has appointed six directors, including his father, to help him run the increasingly complex organisation after retirement as a non-executive director.

SBL's BOARD OF DIRECTORS

James Mensah, Non-Executive Chairman
James is a retired business executive who established SBL and worked for many years before his retirement. James was appointed in 2018.

Edwin Mensah, Chief Executive Officer
Until he took over from his father in 2010, Edwin was in charge of the retail and wholesale distribution division of SBL.

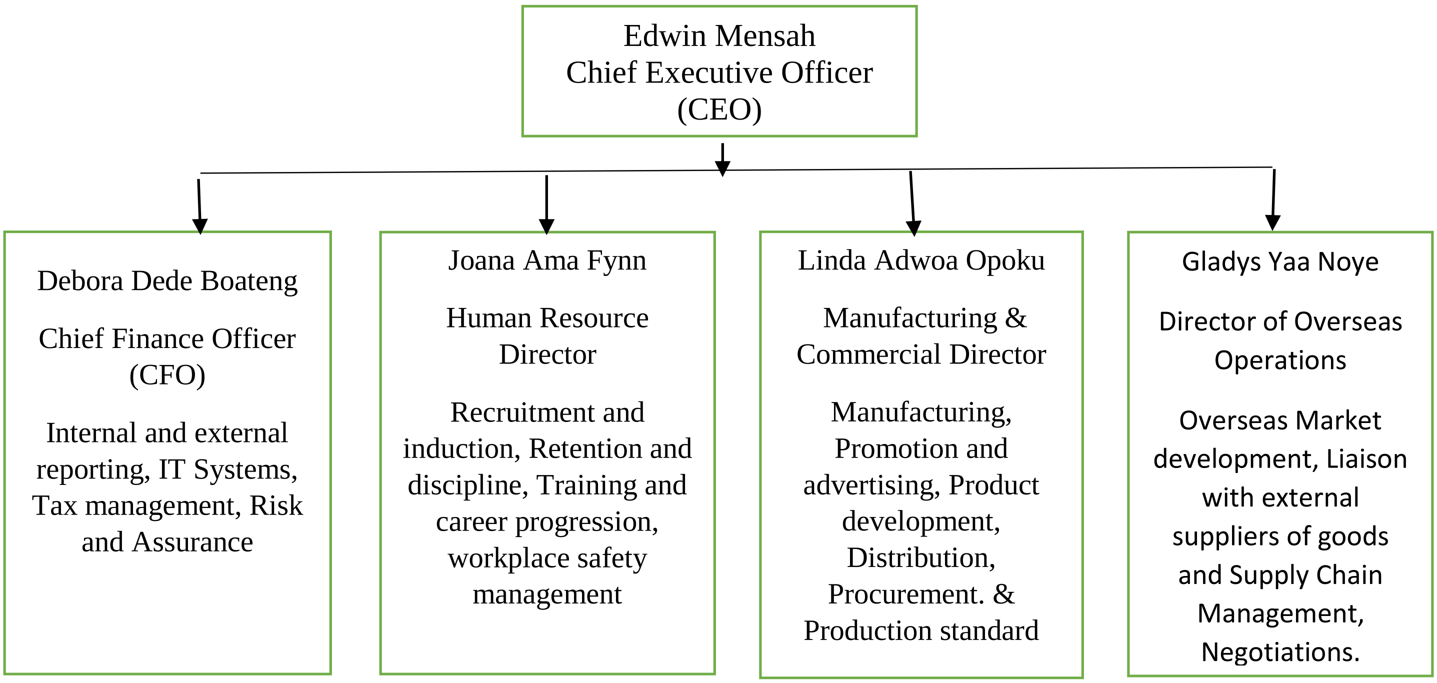
Debora Dede Boateng, Chief Financial Officer
Debora was a Senior Accountant with a large commercial food chain before she was appointed to SBL's Board. She is a qualified accountant. Debora was appointed in 2018.

Gladys Yaa Noye, Director of Overseas Operations
Gladys is a qualified Pharmacist and a Chartered Marketer with specialisation in pharmaceutical products, marketing and distribution. She has worked in several countries with extensive overseas experience. Gladys was appointed Director in 2018.

Linda Adwoa Opoku, Manufacturing & Commercial Director
Linda has held several senior positions in major quoted companies, including Director of Human Resources in one of SBL's competitors. Linda joined SBL's Board in 2018.

Joana Ama Fynn, Human Resource Director
Joana trained and practised as a human resource manager in a large production company before joining SBL as a senior HR Manager in 2014. She was promoted to HR Director in 2018.

SBL Directors



The Directors of SBL are having sleepless nights and wondering the best solution over the following issues, which they only provided as insight from the latest board minutes summarised below for reason of confidentiality:

- Board remit and effectiveness
- Evolutionary (not revolutionary) change
- The digital opportunity
- Greater need for hands-on pharma experience
- Winning in emerging market

Edwin is aware that the business world is changing rapidly around him, and he needs to be updating the culture, structure and technology used in the business. His decision to appoint the directors two years ago has resulted in a different approach to business and change in the business culture but unfortunately not improving the bottom line, profit. Edwin and the directors agreed at an earlier board meeting that some sort of strategic review was needed. Since none of them had any experience in structuring such an exercise, they decided to obtain an expert to help from outside the business. **Blessed Consulting** agreed and sent **Bismark Guy** to dedicate four months on a full time basis for the assignment effective February 2021.

Bismark Guy joined a large West Africa bank after graduation from University as a trainee Accountant. During his first eighteen months with the company, he completed his Institute of Chartered Accountant Ghana (ICAG) examination and, having worked on a variety of projects, was able to gain the experience necessary to award him the designation CA. Having qualified, Bismark was keen to develop his expertise in a wide range of businesses and so left the bank to join a management consultancy firm. Blessed Consulting is based in a country in West Africa but with clients all over the world. His work centred around short project re-imaging in a variety of

industries. He advised on best fit organisational structure, governance, improvement to planning and control processes, and was often involved in implementing organisational restructuring (re-imaging).
Bismark enjoyed the opportunity to work on a project that involved reviewing a whole business rather than just one department's system. During his time with SBL, he carried out a thorough review of the resources, the business development cycle, past business performance, and the business environment in which the company was operating. Recognising that the strategic process ought to be oriented to the future rather than the past, he spent some time talking to the directors, employees and external key stakeholders, including industry competitors.

BISMARK'S INTERNAL REVIEW NOTE OF SBL

SBL is the biggest pharmaceutical company in Ghana. The company is driven by a mission to provide a full range of quality pharmaceutical products at affordable prices and be the preferred supplier in Ghana. With many years of experience in the Pharmaceutical Industry operating as a manufacturer, retailer, and exporter to West Africa's sub-region.

SBL is a wholly-owned Ghanaian private company.It was founded by Mr. James Mensah as a family business. SBL has made giant strides since the retirement of the founder James Mensah in 2010 and has grown from a single retail outlet into a thriving business entity with its own office complex as headquarters in Ghana, retail & wholesale shops and warehouse facilities across West Africa. SBL also owns a manufacturing plant located in Ghana.

Edwin's deep insight, knowledge, and experience in the pharmaceutical industry have enabled SBL to continue providing quality and affordable pharmaceutical products to meet everyone's health needs in Ghana and beyond. SBL has consolidated its position as the biggest distributor of pharmaceutical products with a vast distribution network across Ghana and West Africa's sub-region. SBL has the largest retail chain of shops, with an ultra-modern pharmacy set up to bring products closer to customers, coupled with perceived exceptional customer service.

Besides the manufacturing of quality and affordable medicine, SBL also has the most prominent Agency representation for multinational pharmaceutical and consumer brands, enabling them to offer the widest range of pharmaceutical and consumer products in Ghana and the sub-region of West Africa.

SBL is made up of three main divisions- Manufacturing, Retailing & Wholesale Distribution and Exports. SBL goes beyond the offering of quality and affordable medicine to offer quality customer service. All SBL staff are trained to put the customer's needs first with the view of exceeding the expectations of customers. SBL has a staff strength of 500 with 54% in the manufacturing division and the remaining 46% in the other divisions at the end of 2020.

Vision

SBL's vision is to be a leading **pharmaceutical company** in Ghana and to become a significant global player by providing high quality, affordable and innovative solutions in medicine and treatment.

Mission

SBL’s mission is to be a globally admired **pharmaceutical company**, providing excellent quality products to its customers and people worldwide. To dedicate itself for humanity's quest for longer, healthier, happier lives through innovation.

Corporate Objectives

- Source products and raw materials from reputable organisations that will help the company offer top quality products at affordable prices.
- Engage in continuous improvement of customer service and internal processes through research and development.
- Make SBL products more available and accessible to all its stakeholders.
- Be among the largest indigenous African pharmaceutical companies by 2030.
- Treat the planet with respect.

Core Values:

- **Transparency**: Honest with their clients when examining the needs of the market with precision to meet all their customers' needs, provide the highest levels of quality for the company's services in the field of customer service.
- **Integrity**: Have a high level of ethics and integrity in the provision of everything they do, promote the principles and work ethics among the company's employees.
- **Quality**: Have a passion for excellence in quality products and services in every aspect of their business. Innovation and new features and constantly creating value for customers and employees through teamwork at the company.
- **Respect**: Have a good feeling of pride and high regard for all employees, attract top talent, and maintain a good continuity relationship.
- **Teamwork**: Encourage cooperation, advice and promote the spirit of teamwork. The company employees are familiar with the policy of total commitment to quality which will reflect the spirit necessarily when they are doing business.

SBL’s DEVELOPMENT AND GROWTH STRATEGY

In line with its vision, mission and corporate objective, SBL operates three divisions of ***Manufacturing, Retailing & Wholesale Distribution and Export*** to ensure efficient and effective operations. The divisions are headed by managers who provided goods and services to other divisions of the same organisation using transfer pricing. This ensures that SBL achieves goal congruence for the entity while not losing sight of each division’s autonomy.

Manufacturing Division

It was established six years ago to maintain a high standard of quality in manufacturing pharmaceutical products. Through the manufacturing division, SBL is able to meet the health needs of all segments of the market with affordable medicine. The manufacturing division of SBL started operation in the year, late 2015. The manufacturing plant is located in the Heavy Industrial area along the coast of Ghana to ensure access to cheap but skilled labour and easy logistics and supply chain management.

Following the report submitted by the consultant, the division noted that the plant is obsolete and not competitive, resulting in higher production cost and an increase in wastage. Additionally, the plant has higher setup cost with spare part not readily available on the local market to support its smooth operation. The plant was procured from a far Eastern country with no back up after-sales service support.

Product range and plant capacity

Currently, there are four product range in their plant, capable of producing on an annual basis and in a single shift the following dosage forms and their quantities as indicated below:

- Capsules - 37 million units: Optimal production capacity 84 million units annually.
- Liquids - 6 million units: Optimal production capacity 24 million units annually.
- Powders - 15 million units: optimal capacity 60 million units annually.
- Tablets - 450 million units: Optimal capacity 2 billion units annually.

Most of the product range are tropical medicine which is SBL's competitive advantage. SBL's manufacturing division produces about Two hundred (200) different Finished Pharmaceutical Products for the Ghanaian, West African and Africa markets.

SBL has initiated an ongoing investment program to build a new and fully Good Manufacturing Practice (GMP) compliant facility to complement their current output generation effort. This facility, upon completion, shall increase output generation by about 300 percent with a readily available market to absorb the products.

Quality Policy is also in place with a summary highlighted below:

- Produce safe, efficacious and affordable pharmaceuticals delivered as per agreed quality, agreed quantity and agreed time.
- Satisfy regulatory, statutory and current Good Manufacturing Practice requirements.
- Recruit qualified and experienced personnel and continuously develop their competence.
- Establish and implement quality objectives at all levels of the organisation.
- Institute and maintain a company-wide quality culture.

SBL is also committed to conducting its manufacturing processes to protect the health and safety of its employees, visitors, contractors, stakeholders, and the public. The aim is to remove or reduce the risks to the health, safety and welfare of all employees, contractors and visitors, and anyone else who may be affected by its operations.

Summary of industry best manufacturing practices standard committed below:

- Provide a safe working environment and safe systems of work.
- Ensure the plant and equipment are in a safe condition.
- Provide facilities for the welfare of all employees.
- Provide information, instruction, training and supervision that is reasonably necessary to ensure that each employee is safe from injury and risks to health.
- Have a commitment to consult and co-operate with workers in all matters relating to health and safety in the workplace.
- Commit to improving performance through effective safety management continually.

Retailing and Wholesale Distribution

SBL provides a full range of quality pharmaceutical products at affordable prices to all their customers. This philosophy allows them to contribute to the health needs of everyone in society. They are the largest pharmaceutical retailing and wholesale distribution company in Ghana, with their extensive distribution channels and warehouse facilities nationwide. Additionally, their fleet of over 160 trucks, vans and cars ensure that their products reach every corner of the country. This vital function is performed by its strong team of Medical and Sales Representatives. They work round the clock to ensure the delivery of quality and affordable medicines to every customer at a competitive price.

SBL uses prequalified independent pharmaceutical distributors, retail pharmacies, and chemical sellers to augment its warehouses, wholesales, and retails (pharmacies) to reach its customers/consumers. Government medical stores, hospitals, clinics and private health facilities are key partners to their business value chain.

The planned expansion programme is on course to add new wholesales and pharmacies to the network. Their objective is to get closer to the customer, thereby reducing the cost of doing business and increasing the bottom-line profit.

Export

SBL continue to extend their vast distribution network to provide quality and affordable medicines to other parts of West Africa and the rest of Africa. This is in line with their vision to be among the top ten indigenous African pharmaceutical companies.

Well planned export activities commenced within SBL since the establishment of the manufacturing plant in 2015. Before forming the Exports Division, they had already embarked on several prospective activities in West African countries. The cumulative effect of those activities is the leverage SBL has gained in some West African countries initiated by Edwin after his father's retirement.

SBL exports have mainly been pharmaceutical products manufactured locally in Ghana. They opened their first wholly-owned subsidiary in Freetown, the capital of Sierra Leone, in September 2017 known as GOOD HEALTH Pharma Limited. In addition, they also operate through accredited distributors in the under listed countries:

- Gambia-PK Pharmaceuticals, formerly OJAY Pharmacy
- Liberia-BEST Pharmacy and PAA Pharmacy Ltd

SBL is also gaining a foothold in the Nigerian market and has completed the registration of some of its brands in that country. Fortunately, Nigeria and Ghana Company laws are similar following the adoption of the ECOWAS market integration treaty. Plans are therefore afoot to establish a subsidiary of SBL in Nigeria. In addition to the above efforts to grow its distribution network across Africa, SBL has started making efforts to operate in Benin and Burkina Faso but their challenge is language and stringent French law.

To gain visibility and aid its mission to provide quality and affordable medicine to other parts of Africa, they participate in international trade exhibitions in several African countries, including South Africa, Morocco, Egypt, and Kenya.

With the results achieved so far, they are confident that SBL is poised to increase its reach and impact in West Africa and beyond. There are plans to enter other Africa countries in the near future, with the test market ongoing. They derive fulfilment from their growing capacity to bring quality and affordable medicines to other African countries.

MARKET POSITION REPORT

SBL is suffering due to the fragmented nature of the markets. Growth rates in most of the divisions served have fallen steadily over the last three years due to external competition from overseas rivals, and SBL is now facing a series of market that is stagnant or in decline. While SBL is still profitable due to substantial market shares, it is unreasonable to expect the situation to continue indefinitely. Zero growth is forecast in the SBL current market for the next four years due to overseas rival aggressive market penetration in Ghana and West Africa.

Over the last ten years, SBL has established itself as the market leader in manufacturing, retailing and wholesale distribution, but this has been hard work. The export has a lot of choices and strong market bargaining power. Margins are reasonable for the export division with growth potential but struggling to compete with the new entrant's rivals. This sector is encouraging, but the business model is not supporting leveraging the potential for growth since only 6% of the staff effort is directed toward this part of the business. Manufacturing is still causing major problems due to price competition from overseas rivals, making SBL a small fish in a big pond.

COMPETITORS ANALYSIS

Key Companies to Watch

YELLOW PLC
YELLOW PLC is the second-largest local manufacturer in the private sector and the second-largest supplier to the public sector in West Africa. It is among the few companies to supply a wide range of generic antiretrovirals (ARVs), including the triple therapy combination, to the public sector through a highly competitive tender system. Besides operating in Sub-Saharan Africa, the company has more recently ventured into the Indian market for an alternative supply source of cheaper generic drugs and expanding its geographic footprint.

GREEN PLC
GREEN PLC, one of the leading pharmaceutical companies in China, is one of the leading exporters of generics to West Africa. The company’s product range includes vitamins, antibiotics, analgesics, cardiovascular, respiratory, and cerebrovascular medicines. The company focuses primarily on the public sector and has recently won several tenders in teaching hospitals in Ghana.

RED LTD

RED Ltd, a subsidiary of Health Professional PLC., is one of the leading pharmaceutical distributors in Nigeria, handling about 30% of pharmaceuticals sold and distributed across the country. Entering Ghana a couple of years ago, RED Ltd is growing steadily in the Ghanaian pharmaceutical industry. Given the recently formed alliance with BOSTER Logistics (June 2020), the company plans to expand its coverage and further strengthen its distribution network.

SBL FINANCIAL STATEMENTS

Summary Statement of Financial Performance for the year ended 31 December 2020

	2020 GH¢million	**2019 GH¢million**
Turnover	120	140
Gross Profit	50	61
Operating Profit	12	21
Profit before Tax	9	15
Taxation	(4)	(7)
Profit after Tax	5	8
Dividend	(2)	(3)
Retained Profit for the financial Year	**3**	**5**

Statement of Financial Position as at 31 December 2020

	2020 GH¢million	**2019 GH¢million**
Non-Current Assets		
Intangible assets	6	2
Tangible assets	42	43
	48	**45**
Current assets		
Inventory	15	16
Trade Receivables	28	18
Cash at Bank and in Hand	4	6
	47	**40**
Current liabilities		
Payables: Amount falling due in one year	(15)	(10)
Net current assets	**32**	**30**
Total assets less current liabilities	80	75
Payables: Amounts falling due after one year	(40)	(38)
	40	**37**
Share capital	10	10
Retained Earnings	30	27
Shareholder’s funds	**40**	**37**

ANALYSIS OF TURNOVER BY PRODUCT GROUP AND AREA

	2020 GH¢million	2019 GH¢million
Branded Pharmaceuticals	55	80
Generic Pharmaceuticals	35	40
OTC Pharmaceuticals	30	20
	120	**140**
Ghana	65	120
Rest of West Africa	35	15
Rest of Africa	20	5
	120	**140**

BISMARK EXTERNAL REVIEW NOTE: PHARMACEUTICAL INDUSTRY IN GHANA

Executive Summary

In 2020, the pharmaceutical industry in Ghana was valued at GH¢1.15 billion. It is expected to witness a compound annual growth rate (CAGR) of 21.4% and generate a revenue of GH¢2.06 billion by the end of 2023.

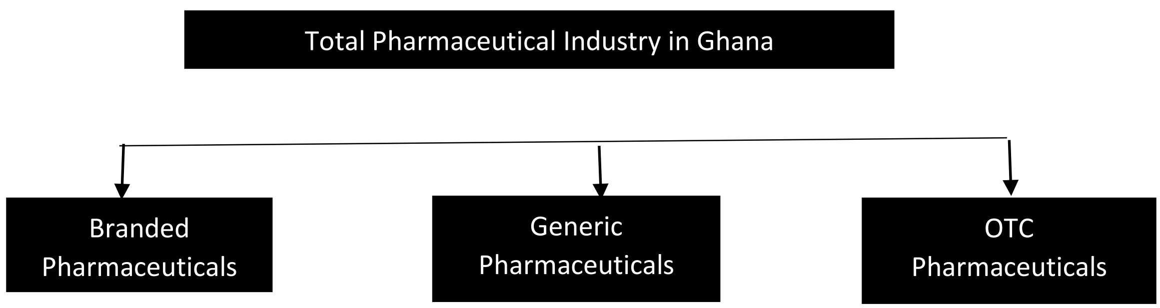
SBL accounted for 5.65% of the total Ghanaian pharmaceutical industry's revenue in 2020 because of its large size, while others accounted for the remaining 94.35%. The pharmaceutical industry in Ghana is fragmented. In 2020, the generic pharmaceutical segment represented the highest revenue share of 51%, while the branded pharmaceutical segment represented the least. The over-the-counter (OTC) pharmaceutical segment is considerably large in Ghana, constituting 59.34% of the total pharmaceutical industry, attributable to a large number of local manufacturers, particularly in the anti-infectives, analgesics, and multivitamins product segments.

In 2020, the anti-infectives therapeutic segment accounted for the highest revenue share of 30.02% of the total pharmaceutical industry in Ghana. It is expected to witness a high CAGR from 2021 to 2024 and remain the largest therapeutic segment during the forecast period. Although the oncology therapeutic segment accounted for the smallest revenue share in 2020, it is expected to be the fastest-growing segment during the forecast period, given the increasing awareness about cancer in Ghana.

The recent achievement of 84% National Health Insurance Scheme (NHIS) coverage in Ghana in 2020 is expected to result in high growth of the pharmaceutical industry, particularly the prescription pharmaceutical (generic and branded) segment, because of easy accessibility and affordability of medicines. The judicious efforts of the Food and Drugs Authority (FDA) in Ghana to control parallel trading and imports of counterfeit drugs are expected to contribute to the growth of Ghana's legitimate pharmaceutical industry. Furthermore, the government is also encouraging the local production of essential medicines to improve capacity utilisation and reduce imports.

Market Segment

The Ghanaian pharmaceutical industry can be broadly divided into three main segments: branded, generic, and over-the-counter (OTC) pharmaceuticals. Branded pharmaceuticals include research and patented prescription drugs sold by innovator companies, particularly multinationals, through local distributors in Ghana. Generic pharmaceuticals include prescription drugs produced and imported into Ghana by generic companies from India and China and sold through local distributors. OTC pharmaceuticals include drugs sold directly to consumers without a healthcare professional's prescription by local pharmacists and chemists.



APPENDICES (a to f)

Bismark's Strategic Review- Summary data notes

a. Financial Health (Based upon the accounts to 31 December 2020)
Appendix I

Profit before Tax	40% down on last year	16% down over the last 3 years
Sales	14.28% down on last year	30% down over the last 3 years
Net current assets	3.33% up on last year	2% down over 3 year
Trade receivables	55.55% up on last year	35% up over 3 years
Trade payables-due less than a year	50% up on last year	40% up over 3 years
Trade payables-due more than a year	5.26% up on last year	10% up over 3 years
Cash at bank and in hand	50% down on last year	30% down over 3 years
Intangible assets	200% up on last year	10% up over 3 years
Dividend	33.33% down on last year	25% down over 3 years
Retained Earnings	11.11% up on last year	20% up over 3 years
Shareholders fund	8.11% up on last year	15% up over 3 years

b. Customers who had been with SBL for more than ten years
Appendix II

How do you rate SBL for Product quality and brand reliability?	Excellent 30% Good 40% Fair 20% Poor 10%
How do you rate SBL on price?	Excellent 10% Good 20% Fair 60% Poor 10%
How do you rate SBL on service	Excellent 70% Good 15%

	Fair 10% Poor 5%

c. Customers who had been with SBL for less than ten years
Appendix III

How do you rate SBL for Product quality and brand reliability?	Excellent 10% Good 40% Fair 40% Poor 10%
How do you rate SBL on price?	Excellent 5% Good 10% Fair 40% Poor 45%
How do you rate SBL on service	Excellent 50% Good 20% Fair 10% Poor 20%

d. Analysis of market position
Appendix IV

Division	**Turnover % 2020**	**Turnover % 2019**	**Market share% 2020**	**Market share % 2019**
Manufacturing	55	57	12	14
Retailing & Distribution	25	29	22	30
Export	20	14	18	7
Total	**100**	**100**		

e. The average number of persons employed by SBL (including directors) during the year 2020 was as follows:
Appendix V

Division	**2020 Headcount**	**2020 %**	**2019 Headcount**	**2019 %**
Manufacturing	270	54	295	52
Retailing & Distribution	200	40	250	44
Export	30	6	25	4
Total	**500**	**100**	**570**	**100**

f. Intangible Assets: research and development cost

Intangible assets relate to the development of new products. Since the products are not yet on the market, no amortisation has been recorded.

Appendix VI

	GH¢m
At the beginning of the year 2020	2
Additions	4
At end of year 2020	**6**

ADDITIONAL INFORMATION

Final Bismark Note for SBL Directors discussion

The note below was obtained as part of Bismark's engagement with Directors of *SBL's competitors* in other to help SBL formulate a sustainable growth strategy. The West Africa region currently enjoys a stable political, legal and economic system. Recent attempts to improve the economy have been largely successful, with inflation projected between 5% - 10% in the past two years. Business taxation is likely to remain at an average of 40%. Government payment shall continue to be the main challenge with the associated negative impact on the businesses' cash flow since it is the industry's largest customer.

Summary of Chief Executives Officers (CEO's) Perspective

- Pharmaceutical companies must understand the similarities and differences in market optimisation strategies to ensure maximum profit and product accessibility by patients.
- GREEN PLC and RED Ltd are the leading Multinational Companies (MNCs) in Ghana because of their decentralised decision-making system and strategic relationship with stakeholders.
- Public tenders are attractive target segments for large revenues and long-term commitment, especially MNCs and foreign market participants.
- Urban centres are expected to be responsible for about 75% of Ghana's growth over the next 15 years. Thus the regional capital contributed 64% of Ghana's overall share of the market in 2020.
- Government procurement through competitive tenders is the cheapest despite the process bottlenecks but contributes significantly to the Pharmaceutical Industry's bottom line.
- Government is the main contributor to the industry's cash flow problems due to delays in payments after supplies to central medical stores.

Summary of Chief Finance Officer's (CFO's) Predictions

- Branded pharmaceuticals are expected to adopt a differential pricing strategy specific to patient segments and geographies in West Africa to make treatment affordable to a large group of patients, thereby significantly expanding their customer base.
- Foreign traders in West Africa are expected to bolster their distribution channels by engaging in strategic partnerships with trustworthy local stakeholders.
- Given the immense growth potential and business opportunities, it is expected that companies would invest significantly in their marketing capabilities, patient awareness programmes, and treatment support services to enhance brand loyalty.

SECTION A

1) Edwin is concerned that the current skills set of his directors are not sufficient to drive any change management in SBL. At a discussion during a board meeting, the directors vehemently disagreed.

   Required:
   Explain to SBL board using ***the Rosabeth Moss Kanter theory***, suggested skill that managers should have in other to change-adept to help improve profit. **(10 marks)**

2) Edwin is keen that the change in SBL should be transformational. Explain to the board of SBL using ***the Gemini 4Rs model*** the element of transformational change by relating it to the above case. **(10 marks)**

3) Bismark is proposing that he would be using the "***Strategic Clock***" to assess competitors' business strategies.

   Required:

a) Explain to the board of SBL the purpose of the 'S***trategic Clock'*** as proposed by Bismark. **(3 marks)**

b) Draw a strategic clock and explain using the **FIVE (5)** broad groups of business strategy to help SBL gain a competitive advantage. **(7 marks)**

4) The board is concerned that currently there is no formalised method to evaluate the strategic performance of SBL. At a board meeting to brainstorm, Bismark suggested the use of a ***Balanced Scorecard*** but his only concerned was that it applies to the service industry. Debora Dede Boateng disagrees.

   Required:

a) Explain to the board why Balanced Scorecard can be used or otherwise as a Critical Success Factor (CSF) when measuring the performance of SBL. **(8 marks)**

b) In a table format with the heading ***"Perspective" and "Outcome measures"***, identify the Balanced Scorecard **FOUR (4)** aspects of performance using the information provided from the SBL case study. **(12 marks)**

(Total: 50 marks)

SECTION B

5) Bismark's four months consultancy service contract was running out of time with so much yet to be done. He then contracted you as a Consultancy Business Support Advisor to **summarise** his work to enable him meet with the Directors of SBL. He provided you with the following format to use to ensure that all issues reviewed are covered:
   i. Title page
   ii. Table of contents
   iii. Introduction
   iv. Executive Summary
   v. Body of the report
      - Business environment analysis
      - Industry background
      - Competitor analysis
      - Market Analysis
      - Operations analysis
      - Management Summary
      - Financial Performance
   vi. Conclusions and recommendations **(20 marks)**

6) James Mensah and Edwin Mensah are concerned that SBL is not strictly adhering to concepts of good governance. They want to see SBL as a well governed company.

   Required:
   As a Business Development Advisor, explain to the board what ***"concepts of good governance"*** is. **(10 marks)**

7) Debora Dede Boateng is having sleepless nights due to the level of SBL's risk in relation to ongoing investment. She had a discussion with Bismark which centered on *"**International Organization for Standardisation's ISO 31000**"*.

   Required:
   Explain the process of risk management that you will recommend that should be adopted by SBL's board in line with ISO 31000. **(10 marks)**

8) Divisional managers are concerned about SBL's objective of transfer pricing. As a Business Advisor, explain to the divisional managers the transfer pricing objective of SBL as it is often in conflict: *"**entity goal congruence' and "division autonomy**"*. **(10 marks)**

(Total: 50 marks)

SOLUTION TO QUESTIONS

SECTION A

QUESTION ONE

Rosabeth Moss Kanter suggested that managers in a change-adept entity such as SBL directors should have the following skills:

- **Turning in to the environment**: SBL directors need to be aware of changes in their environment to make change by the entity necessary. Kanter suggested that managers leading change create a ***"listening post"*** network that they should use to monitor their environment change. She commented "Pay special attention to customer complaints, which are best source of information about an operational weakness or unmet need. Also search out broader signs of change- competitors such as Yellow PLC, Green PLC and Red LTD doing something differently or a customer using a product or service in unexpected ways.

- **Challenging the prevailing organisational wisdom**; Change managers should be prepared to challenge the ***'conventional wisdom'*** and question accepted views about what is necessary or the way things should be done, including taking the opportunity to win in the emerging market rather than keeping directors awake or take advantage of the digital opportunity.

- **Communicating a compelling aspiration**. Leaders driving change should have a clear idea of what they want to achieve and share this ***'vision'*** with everyone they deal with. In addition, the managers must have personal courage of conviction that the change is necessary. Without this sense of purpose, managers will not be able to ***'sell'*** the need for change to others in SBL.

- **Building coalitions**. Managers cannot make change happen through personal effort alone. They need to win the support and co-operation of all the individuals with the knowledge, influence or resources to make change happen. Making change happen is, therefore a process of building alliances and support.

- **Learning to persevere**. Managers of change should continue with the process of change even though there are likely to be setbacks and ***'defeats'*** on the way.

- **Making everyone a hero.** The manager should give full credit to everyone who helps to introduce change successfully and should make team members feel their efforts are fully appreciated. If possible, individuals who help to introduce the changes successfully should be rewarded.

(Any five points @2 marks each = 10 marks)

QUESTION TWO

Transformational change within an organisation can be challenging to achieve successfully, and the role of managers or team leaders are critically important. Managers lead the change process, and it is their responsibility to bring their team members along in accepting and welcoming the change. In particular, SBL managers as team leaders should communicate the reasons for the change, such as reduction in profit before tax for the past three down by 16% and 2020 down by 40% over 2019. Reduction in profit before tax is a sustainability challenge that can be a reason for a change in the current business operating model. This would also ensure the team members' trust so that they are willing to believe and accept what the team leaders say and follow where the team leader takes them. It is also important that SBL allow team members to participate in the planning and implementation of the change as reflected in the business meeting minutes evolutionary (not revolutionary) change to identify with the change more readily to make team members change agents.
The ***Gemini 4Rs model was introduced by Gemini Consultants*** to support managers such as SBL directors when dealing with transformational change. The 4Rs elements are ***Re-frame, Re-structure, Revitalise and Renew.***

Re-frame

- Create the desire for change example, reduction in sales by 30 % over the last three years 2020 made performance reduced by14.28% over 2019.
- Create a vision of what the entity is trying to achieve. For example, SBL's vision is to be a leading pharmaceutical company in Ghana and become a significant global player by providing high-quality, affordable and innovative solutions in medicine and treatment appealing to stakeholders?
- Create a measurement system to set targets for change example, which is the optimal plant operational level that should be satisfactory to the market and management to ensure adequate, timely and quality supply of products
- Measure performance, for example, by clearly defining the target market share of each division of manufacturing, retailing & distribution and export to allow for actual performance against the target by SBL.

Re-structure

Examine the organisation structure, and create an economic model showing how value can be created by the entity and where resources should be used. Then, re-design the processes so that they work better to create more value. For example, SBL needs, as part of restructuring need to review staff deployment.

Revitalise

- This is SBL commitment to the future. Fund new products and new markets that fit well with the entity environment, such as a clear strategy to expand its footprint in

Africa. SBL directors need a deliberate strategy with backup resources deployment to achieve that vision and to grow profit.

- Inventing new businesses should be the responsibility of all directors. Currently, the SBL structure appears to be the responsibility of Gladys Yaa Noye, director of overseas operations, and to some limited extend Linda Adwoa Opoku, manufacturing and commercial operations director.
- Chane the rule of competition by making use of new technology, including digital opportunities.

- **Renew**.
- SBL need to develop individuals within the organisation beyond the directors' level as per the current structure. Make sure employees have the skills that are required and that they support the change process.
- SBL need to create a reward system to motivate individuals to seek change.
- SBL need to develop individual learning and creativity within the organisation to be spearheaded by Joana Ama Fynn, human resources director, to include organisational development of SBL.

(Transformational change = 2 marks and 2 marks each of the Gemini 4Rs elements = 10 marks)

QUESTION THREE

a) **Purpose of the "strategic clock"**

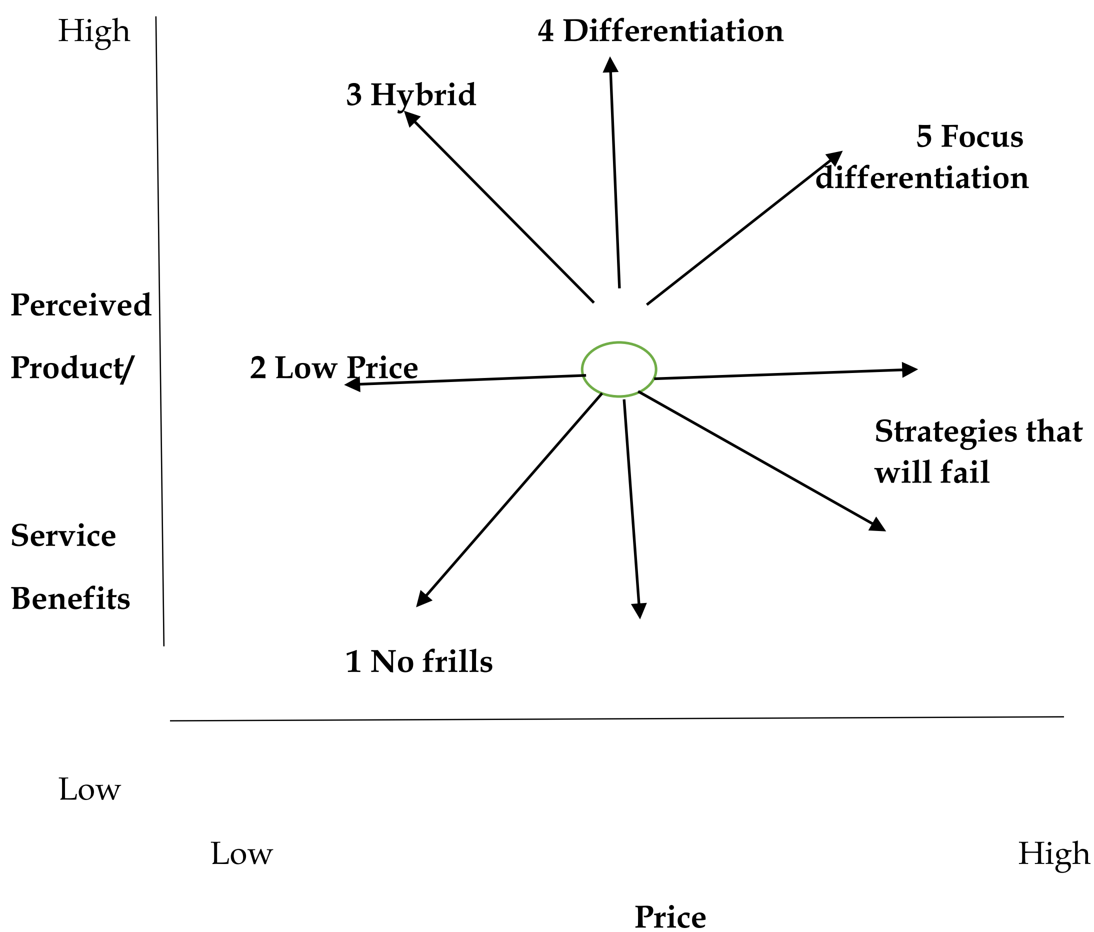
The strategic clock was suggested by Bowman (1996) as a way of looking at combinations of price and perceived benefits. Companies such as SBL can also use the strategic clock to assess the business strategies of competitors and the combination of prices and benefits they may be offering. SBL should consider which combination of the two they should try to provide, although to do this, they must also understand customers' perception about the benefits that the product or the service provides.

The two factors in providing value to customers are the price of the product or the service and the benefits that the customers believe the product or service offers. Competitive advantage comes from offering an attractive combination of price and perceived benefits. SBL, as provided in appendixes II and III (b & c), further analysed customers with SBL over 10 years and below 10 years. Performance is not good but SBL does not have target to help conclude with internal benchmark targets and also with competitors. This data needs to be improved to support management decision making.

(3 marks when well explained and related with the case study) (3 marks)

b) The strategic clock has two dimensions: price and perceived benefits. Price can be shown on a scale ranging from 'low' to 'high'. Similarly, perceived benefits can be shown as a scale from 'low' to 'high'. The 'clock' consists of series of business strategies. Each business strategy is shown as the hand of a clock, pointing to a combination of price and perceived benefits. This is because customers have different requirements in terms of value for money.

Five business strategies might enable a firm to gain a competitive advantage and strategies that will fail because they cannot provide a competitive advantage.



The five broad groups of business strategy that might succeed are:

1. a 'no trills' strategy (position 1 on the clock)
2. a low-price strategy (position 2)
3. a hybrid strategy (position 3)
4. a differentiation strategy (position 4)
5. a focused differentiation strategy (position 5)

No frills strategy; Position 1

A no frills strategy is to offer a product at a low price with low perceived benefits. It should attract customers who are price conscious and are happy to buy a basic product at the lowest possible cost. SBL might use this strategy to target over the counter generic products. With no frills' strategy, customers understand that they are buying products that give them lower benefits and might be difficult to apply to a pharmaceutical product in practice.

Low price strategy: Position 2

With a low-price strategy, customers perceive that the product or service gives average or normal benefits. However, it is not regarded as a low-quality product. The price is low. However, it is low compared with similar products in the market. Only the lowest-cost producer in the market can implement this business strategy successfully. SBL might explore the generic products manufactured directly by them with a tropical brand competitive advantage to create a market niche over its business competitors such as a multinational, through optimising plant production capacity to lower price remains a challenge. At the end of 2020, manufacturing production capacities are as follows: Capsules 44.05%, liquid 25%, Powders 25% and Tablets 22.5% using an obsolete plant with challenging stat uptime and no after sales backup support.

Hybrid strategy: Position 3

A hybrid strategy involves selling a product or service that combines: Higher than average befits to customers and a below-average selling price. To be successful, the business requires low-cost production and also the ability to provide more enormous benefits. Thus, it tries to achieve a mix between a low-price strategy and a differentiation strategy. The hybrid strategy can be used for the selling & distribution division where SBL provide a full range of products at affordable prices to all customers.

Differentiation strategy: Position 4

A differentiation strategy is based on making a product or a service appear to officer more benefits than rival products or services. In the strategic clock, a differentiation strategy involves charging average prices for a product or service or price that are perhaps only slightly higher than the average. However, the strategy does not include charging prices that are very much higher than average. Customers, therefore, believe that they are getting more benefit for every value they spend. SBL can explore this strategy to support its competitor analysis for the export market as the Ghana market is fragmented.

Focus differentiation strategy: Position 5

Focus differentiation strategy is to sell a product that offers above-average benefits for a higher-than-average price. Products in this category are often strong branded as premium products. Therefore, their higher price can be justified, for example, tropical pharmaceutical products branded by SBL and patented.

Business strategy on the clock that will fail

The diagram of the strategic clock shown above indicates some business strategies that will not succeed because they do not enable the company to gain a competitive advantage. Higher price and low quality.

(Diagram 2marks and the five strategies 1 mark each with explanation that relate to case study) (7 marks)

QUESTION FOUR

a) The balanced scorecard can be used to measure performance in relation to long-term business objectives. For a commercial business such as SBL, the most important objective is a financial objective. However, to achieve the financial objectives in the long-term, it is necessary to achieve goals and targets that are non-financial in nature as well as financial and therefore can be used for any business industry when performance objectives are clearly defined to suit the inductor and can be measure realistically and objectively.

The balanced scorecard, critical success factors are identified for ***'four' aspects of performance or 'four' perspectives:***

- Customer perspective
- Internal perspective
- Innovation and learning perspective
- Financial perspective

Of the four perspectives, three are non-financial. For each perspective, Kaplan and Norton argued that an entity key performance measurements and key performance targets. The four perspectives provide a framework for identifying what those measures should be. However, each entity's specific measures, including SBL, will vary according to the nature of the entity's business. With that flexibility, Debora is right by disagreeing that the model can only be applied to the service industry, raised by Bismark.

Customer perspective

What do customers value? By recognising what customers value most, a company can focus its performance targets on satisfying customers more effectively. For example, target might be developed for several aspects of performance such as value for money, quality, place of delivery etc.

Internal perspective
To achieve its financial and customer objectives, what processes must SBL perform with excellence? Management should identify the key aspects of operational performance and achieve excellence in these areas. For example, SBL might consider customers value the quality of its products and services using effective operational controls in preventing the error from happening considering the sensitive nature of its products and services as pharmaceutical industry.

Innovation and learning perspective
How can the SBL continue to improve and create value? The focus here should be SBL ability to maintain its competitive position through the skills and knowledge of its workforce and developing new products or making use of new technology as it develops.

Financial perspective
How does SBL create value for its owners? Financial measures in the balanced scorecard system might include share price growth, profitability and return on investment, including dividend payment trend and growth in shareholders' funds.

SBL board to note:
Several measures of performance may be selected for each perspective or just one. However, SBL consultant Bismark and Debora should note that using a large number of different measurements for each perspective adds to the complexity of the performance measurement system hence should focus on critical success factors that relate to SBL.

(Explanation of Balanced Scorecard and relevant to SBL 2marks: Explanation of the four perspectives in relation to SBL 1.5 marks each) (8 marks)

b) Examples of measurement performance for each of the four perspectives are as follows in the table below in relation to SBL.

Perspective	**Outcome measurement**
Critical financial measures (***What do SBL owners' value?)***	✓ Return on investment target (plant investment decision target) ✓ Profitability and profitability growth such as profit before tax target ✓ Profitability analysis by market segment ✓ Sales target by division to support transfer pricing decision ✓ SBL growth target to benchmark with industry CAGR 21.4% ✓ Debtors and creditors ratio and impact on cash flow and adequate liquidity target
Critical customer measures ***(What dose customers want?)***	✓ Percentage of delivery on time target ✓ Quality of product and service target ✓ Benefits derived from projects and services target ✓ Accessibility of product and services target ✓ Customer's complaints targets ✓ Percentage of products or services rejected target.
Critical internal measures ***(What internal activities does SBL need to excel at to succeed at its business?)***	✓ The success rate in winning contract orders from government ✓ Set-up times (Production change over time) ✓ Percentage of plant capacity utilisation ✓ Product cost reduction ✓ Percentage reduction in the amount re-working of defective units ✓ Cash flow negotiation targets with government, suppliers and debtors

Critical innovation and learning measures ***(What SBL need to be good at now to excel in the long-term?)***	✓ Revenue per employee ratio ✓ Employee productivity ratio ✓ Employee satisfaction ratio ✓ Percentage of turnover from new customers ✓ Employee retention and turnover rate ✓ Percentage of total revenue earned from sales of new products ✓ Time to develop new products from design to completion of development and introduction to the market ✓ Percentage of Investment at research and development as compared with the total investment

(3marks for each of the four perspectives and outcome suggested measurement)
(12 marks)

(Total: 50 marks)

SECTION B

QUESTION FIVE

i. **Title page**
The title page is there to attract readers to the report and assist them in finding the report later. The following should be covered:
- Title (any sub-titles) should distinguish the report and ensure it is easily identifiable from others.
- Author since the report is for internal use only
- Degree of confidentiality
- Date

(1mark)

ii. **Table of contents**
The table of contents is a list of all the sections that are included in the report (in the same order in which they appear plus relevant page numbers, for example
SBL internal review summary report
SBL external review with a focus on the pharmaceutical industry in Ghana
SBL competitor analysis with an emphasis on directors and Chief Finance Officers perspectives and predictions

(2 marks)

iii. **Introduction**

The introduction prepares the reader (Bismark Guy) for the report itself by reminding him of what he already knows for example why the report has been written and the question that the report answers by

Make the subject of the report clear, i.e. support of Bismark Guy extract notes summary.

State the purpose of the report, i.e. to be presented to SBL directors

(1mark)

iv. Executive Summary

The benefit of including an executive summary is for senior management with little time to go through or read. Therefore, a concise, clear, and well written executive summary should include the following:

- What the report is about
- What the problems are
- The conclusions the writer arrived at
- What the writer recommendation

The skill in writing the executive summary is to give the overall picture without including too many details.

(4 marks)

v. Body of the report

The body of the report heading provided by the Bismark. The headings are essential 'signposts' that allow Bismark to navigate to the relevant details of the report in a logical fashion to further investigate when he read the executive summary:

- Business environment analysis- Brief SWOT analysis:
  - ***Strength****:* business employs a high skill and dedicated staff
  - ***Weakness***: Obsolete plant with no after sales service producing well below capacity, challenging start time etc.
  - ***Opportunity***: Huge demand for the business products overseas with potential to increase export market share in West Africa and beyond
  - ***Threat:*** A large number of new competitors forming strategic alliances to dominate and government procurement and payment delays
- **Industry background**-pharmaceutical industry which provides both product and service
- **Competitor analysis**- who are the main competitors?
- **Market Analysis**- Size, segmentation and potential growth and challenges
- **Operations analysis**- operations challenges
- **Management Summary**- who the management personnel are and their background.

- **Financial Performance** -Summary of financial information, income statement, statement of financial position and highlight performance challenges based on the ratios provided in the case study appendices.

(9 marks)

vi. Conclusions and recommendations

- Do the conclusion and recommendations follow logically from the rest of the report (draw out the main points of the report and present a considered judgement to support Bismark discussion with the SBL board of directors: only draw conclusions that are justified by the evidence and facts contained in the body of the summary report: make recommendations based only on discussion and conclusions: No now line of argument or material in the conclusions and recommendations that is not part of the body of the summary report
- Check conclusions and recommendations against the original objective (summary Bismark work for discussion with the board of SBL)
- Ensure the conclusions and recommendations answer the reader (Bismark) key questions to facilitate his engagement with the board of SBL.

(3 marks)

QUESTION SIX

A well-governed company is one in which the board acts in the best interests of shareholders and other stakeholders such as employees and in accordance with the law. In doing so, the board should apply a number of broad concepts. Failure to apply these concepts in practice is likely to mean bad governance, with the board or its leaders governing the company in their self-interest. These include ***fairness, transparency, independence, honesty and integrity, responsibility and accountability and reputation***

Generally, the concepts seem 'obvious". However, it is useful for the board of SBL to think about what might happen if these concepts are not strictly applied and enforced as a board.

Fairness

In corporate governance, fairness refers to the principle that all shareholders should receive fair treatment from the directors. At the basic level, all the entity shareholders in the company should be entitled to equal treatment, such as one vote per share at a general meeting of the company and the right to have the same dividend per share.

Transparency (openness)

Transparency means ***'not hiding anything***. Intentions should be clear, and information should not be withheld from those individuals who ought to have a right

to receive it. Transparency also means clarity. In corporate governance, it should refer not only to the ability of shareholders to see what the directors are trying to achieve. It also refers to the ease with which an ***'outsiders'***, such as a potential investor or aoutsidere, can make a meaningful analysis of the company and its intentions.
Therefore, transparency means providing information about what the company has done, what it intends to do in the future, and what risk it is facing, such as the SBL director's intention to acquire a new plant.

Independence
Independence means freedom from the influence of someone else. For example, a principle of good corporate governance is that a substantial number of the board of directors of a company should be independent, which means they can make a judgment and give an opinion in the company's best interest without bias or preconceived ideas.
The independence of a director is threatened by having a connection to a particular interest group, for example, Edwin and the father, James. Executive directors can never be independent because their views will represent the opinions of the management team. Similarly, a retired formal executive such as James might still be influenced by the views of management because he shares the ***'management culture'***. Directors who represent the interest of majority shareholders are also incapable of being independent—similarly, professional advisors such as Bismark to SBL. External auditors, solicitors should be independent of the company and should give honest and professional opinions and advice.

Honesty and integrity (probity)
Honesty is an essential quality for directors and their advisors. An individual who is honest and who is known to be honest, is believed by others and is therefore likely to be trusted. However, in business practice, honesty is not a widespread as it might be. Business leaders may prefer to ***'put a spin'*** on the fact and manipulate facts to present a more favourable impression.
Integrity is similar to honesty, but it also means behaving in accordance with a high standard of behaviour and a strict moral or ethical code of conduct. Professional accountants, for example, are expected to act with integrity by being honest and acting in accordance with their professional code of ethics.
If shareholders in the company suspect that the directors are not acting honestly or with integrity, there can be no trust, and good corporate governance is impossible.

Responsibility and accountability
The directors of a company are given most of the powers for running the company. Many of these powers are delegated to executive managers, but the directors remain responsible for how those powers are used.
An important role of the board of directors is to monitor executive management decisions and satisfy themselves that the decisions taken by management are in the

best interest of the company and its shareholders. The board should also retain the responsibility for certain key decisions, such as setting strategic objectives for their company and approving major capital investments. The board of directors should not ignore their responsibility by delegating too many powers to executive management. With responsibility, there should also be accountability. In a company, the board of directors should be accountable to the shareholders. Shareholders should consider the reports from the directors about what they have done and approve or disapprove. The reports include annual reports and accounts to the shareholders to consider and discuss with the board of directors at an annual general meeting. If shareholders do not approve directors, they have the right to remove them from office.

Reputation
The reputation of a company might be good or bad. That is the character of the organisation as perceived by stakeholders. A reputation may be based on a combination of several qualities, including success and management competence. However, a company might earn a good reputation with investors, employees, customers and other stakeholders in other ways. A concern of the environment or eco-friendliness and responsiveness through its corporate social responsibilities such as SBL corporate objective of treating the planet with respect.
Companies that are badly governed can be at risk of losing goodwill from investors, employees and customers.

(Any five points @ 2 marks each) **(10 marks)**

QUESTION SEVEN

Risk is usually associated with the possibility that things might go wrong. Debora's concern is rightly so since the existing plant is not currently operating at the optimal capacity yet seems obsolete. Hence, replacing it with a cutting-edge modern facility with higher output capacity, for example, 300% capered with the current output.
However, risk has a broader meaning. Risk exists whenever a future or future event cannot be predicted with certainty, and a range of different possible outcomes or events can recur. Risk can be divided into two categories pure and speculative risks.
SBL management should have considered risk when making the plant investment decisions. Management should have chosen investments that are expected to increase the value of SBL but at a level of risk that it considers acceptable.
An organisation including SBL attitude towards risk influences whether or not risks are **taken, tolerated, retained, shared, reduced or avoided**, and whether or not the treatments are implemented or postponed ***(International Organisation for Standardization's ISO 31000).*** The investment in plant decisions is a financial risk and a significant component of business risk.

Debora needs to know that risk management is a corporate governance issue hence a shared responsibility with her colleague's board of directors. The board of directors is responsible for safeguarding the assets of SBL and protecting investment in the plant from loss of value.

Risk management is a process of managing both downside risks and business risks. It can be defined as the culture, structures and processes that are focused on achieving possible opportunities yet at the same time control unwanted result.

SBL should adopt the following process of risk management in line with ISO 3100 standard recommendation:

- Identification of risks
- Assessment of risks
- Risk control measures
-

Risk identification

Risk identification is the initial stage in a system of risk management. SBL board needs to understand what risk it faces. For example, the plant is obsolete, both in its environment and markets (strategic risk) or internally (operational risk).

The risk identified by SBL will vary in importance. Some risks might be unimportant or easily controlled. On the other hand, some risks might be very significant. Therefore, it is necessary to assess the importance of each risk to rank the risk in order of significance or priority so that appropriate control measures are urgently through the process of assessing the risks.

Assessing the risk

The assessment of risk is sometimes called ***'risk profiling' or 'risk mapping'***. To assess the investment risk, it is necessary to consider the likelihood that loss will occur due to the risk, and the size of the loss when this happens. A simple approach to risk mapping involves taking each risk identified and placing it on a map. The map is a 2X2 matrix with one representing the frequency of the adverse events or the probability that the risk will materialise and the adverse outcome when it occurs. The other side representing the impact (loss) if the adverse event occurs, or adverse circumstances arise since the inability of the plant to produce to meet market demand and the associated negative impact on SBL, including customers order delays and further loss of market share to competitors.

The risk map can help management identify risks where immediate control measure is required. For example "high impact, low probability. All key risk should be "owned' by specific individual managers who should be required to take the necessary control measures.

Difference approaches to controlling risk

The decision about suitable control measures depends on the significance of the risk and the cost of taking the control measures. With the case of SBL, it appears management is considering the acquisition of a new plant; however, it is not clear

whether the old plan would be disposed of. Therefore, further discussion is required for SBL management and board to be clear about their decision.
Control measure can only be justified if the cost of control is less than the benefits obtained from reducing the risks. There are several different approaches, including risk transfer, hedging the risks and diversification of risks.
In the case of SBL, risk transfer is one option by insuring the plant. By purchasing insurance, some of the risks can be transferred to the insurance company.

(ISO 31000 explanation and relate to SBL 4marks. Process of risk management 3 points of 2 marks each) (10 marks)

QUESTION EIGHT

To: Divisional Managers of SBL
From: Business Advisor (Consultant)
Subject: **Objective of Transfer Pricing and potential conflict-Entity goal congruence and divisional autonomy**.

This brief report is to advise SBL divisional managers decisions that have to be made about what transfer price should be for performance management and performance evaluation in a divisional organisation of SBL. It is appropriate that:

- The selling division should earn profit or return on sales or services that it buys from other divisions, for example manufacturing division should make a profit when it sells to the retail and distribution division.
- The buying division should pay a fair price for the goods and services that it buys from the other divisions.

Transfer prices are decided by management. The objectives of transfer prices should be to achieve the following:

- achieve goal congruence for the entity as a whole
- give autonomy (freedom to make decisions) to the managers of the profit centres or investment centres

These two objectives are often in conflict with each other, and unless the transfer prices are set at a suitable level, it might be impossible to achieve both objectives.

The motivation of divisional managers

An assumption is that the managers of every profit centre will take a decision that maximises the profit of the division. If every division maximises its profit, the profit of SBL as a whole will also be maximised. However, a division might take an action that maximises its profit but reduce the profit of another division. As a result, the entity's profit as a whole might also be reduced, for example, between the manufacturing division of SBL and the selling and distribution division.

Goal congruence

Every divisional manager should work towards the maximisation of the profit and returns of the entity as a whole. Therefore, when every divisional manager has the same aim or goal, there is a goal congruence.

- Transfer prices should therefore encourage divisional managers to take decisions that are in the best interests of the entity as a whole to support the competitive advantage of SBL as highlighted in the Chief Finance Officers summary production report during Bismark engagement.
- Transfer prices should not encourage a divisional manager to take decisions against the interests of the entity as a whole that would reduce the profit of SBL or impede its pricing competitiveness.

Divisional autonomy

Autonomy is the freedom of action and the freedom to make decisions. Divisional managers should be free to make their own decisions. Autonomy should improve the motivation of divisional managers. For example, when the transfer price is set or decided, the managers of all divisions within SBL should be free to choose.

- Whether to sell their output to other divisions (internal transfer) or sell to an external customer if an external market exists for the output
- whether to buy their goods from another division (internal transfer) or buy them from external suppliers if the external market exists for the output.

Divisional managers should be allowed to make their own choices. They should not have to be told what to do by senior management at the head office.

Conflict

If there is a conflict between the objective of goal congruence and divisional autonomy, goal congruence should have priority. If SBL divisional managers cannot agree to do what is best for the entity as a whole, they should be instructed about what to do by SBL senior management.

Ideally, transfer prices should be set so that divisional managers can agree on selling and buying between each other in a way that is in the best interests of all the divisions and the entity as a whole. Overall transfer pricing decision to be adopted by SBL is to gain a competitive advantage over its competitors.

(Objective of transfer pricing 2 marks: goal congruence 3 marks; divisional autonomy 3; decision conflict 2 marks) (10 marks)

(Total: 50 marks)