Answer to Question One

Requirement (a)(i)

The style of strategy employed by Aybe is that of strategic planning. The case tells us that Aybe ‘applies a traditional rational model’. This approach has been employed to good effect in environments which are relatively stable and well understood by the organisation. However, the environments of the Asian markets, as described in the case, are fast-moving whereas rational strategic planning is not. The markets are ‘highly adaptive’ and strategic planning may not be able to cope with this. Furthermore, the market structures vary from entrepreneurial to those with state planning. In these conditions, the traditional rational approach would not be the most relevant one for Aybe to use.

Requirement (a)(ii)

Aybe could also use these approaches:

Opportunism or freewheeling opportunism: this would imply not preparing plans as such, but rather taking advantage of opportunities as they arise. This approach mirrors that of the Director of Operations and could be suitable in an environment subject to considerable, frequent and unforeseeable changes.

Incrementalism or logical incrementalism: this is an adaptive approach to strategy which involves making small changes to strategy in the light of changing conditions. It is a conservative, rather than a radical, approach; ‘Evolution not Revolution’. This approach might suit Aybe as a first move away from the constraints of strategic planning.

Emergent: this approach, after Mintzberg, regards strategy not as a mechanistic process but as an organic one. Instead of there being a top-down procedure for the development of strategy (i.e. as in Planning), the strategy is developed in response to environmental conditions and is highly adaptive. This could suit Aybe as it moves into an unfamiliar environment.

Answers based on positioning and resource based strategy also earned marks

Note: Only two approaches were required from candidates

Requirement (b)

In order to evaluate the suitability of Aybe’s current organisational structure for its proposed expansion into Asian markets, its salient features are described and compared to the environmental conditions which Aybe is likely to encounter in Asia.

Currently, Aybe has an organisational structure which ‘is organised along traditional functional lines’. This is similar to many companies and is reflected in the composition of the Board of
Directors, for example, there is a Finance Director and an Operations Director. It would be reasonable to expect that Aybe has departments corresponding to the different functions carried out within its business; for example, there will probably be a Marketing department and a Production department. These departments would have established zones of authority and responsibility and would benefit from periodic reporting of their results including performance against budget targets.

However, such a structure has disadvantages. Over time it can become stagnant and bureaucratic and it may be hard for enterprise to flourish in such a culture. This could be the situation within Aybe which has not engaged in re-organisation unlike many of its competitors: this could imply a resistance to change. There are other disadvantages in Aybe's structure. The functional departments do not necessarily reflect the value-creating processes within Aybe. Thus, the demarcation of the divisions by their products is necessarily an arbitrary one and, in practice, some products may overlap more than one division. The functional structure may also lead to a 'silo' mentality where employees only think and are concerned about their particular part of Aybe. This tendency could be to the detriment of Aybe's efficiency and profitability and lead to lower customer satisfaction. Aybe had maintained the same structure since 1990 although many of its competitors had reorganised since then. In 2008 consultants had suggested alternative structures for Aybe but it had still not changed. These factors strongly imply that by 2010 Aybe's organisational structures had become outdated.

The environment within Asia has some environmental conditions which throw into question the suitability of Aybe's current organisational structure for doing business there. These are:

*‘The markets are fast-moving and highly adaptive’.* If Aybe’s organisational structure has led to stagnation and bureaucracy, this may make the current structure unsuitable as it will not be able to respond speedily and flexibly to the business environment.

*‘Some countries in Asia are highly entrepreneurial’.* If Aybe's structure has led to a culture where enterprise does not flourish, Aybe may encounter difficulties in highly entrepreneurial countries as entrepreneurs do business in ways that Aybe may not be accustomed to; for example, entrepreneurs are often very decisive and expect this quality from others. Aybe may not be able to accommodate this.

*(In some countries)... ‘there is much involvement of the State in business’.* This may create problems for Aybe but they will not necessarily be ones to do with the organisational structure.

*‘In some countries there is a mixed economy’.* Aybe has a record of doing business in both America and Europe and should have experience of doing business where the Government is also involved in business; for example, in the UK the Government controls the nuclear power industry and some of the railways.

*‘Asia encourages free markets’.* This should not create difficulties for Aybe.

*(In some countries there is) ‘ a requirement ..for a local involvement in any business enterprise’.* In such a country, Aybe may be obliged to accommodate a local presence in ownership and possible local representation on its Board and in its workforce. In order to satisfy this requirement Aybe would have to change its organisational structure.

As Aybe will face a variety of new environmental conditions in Asia, its current organisational structure is likely to be unsuitable.

**Requirement (c)(i)**

If Aybe chooses to conduct its business in Asia using agents, this effectively represents a substantial degree of delegation. The agents will be independent businesses over which Aybe has no direct control. This gives rise to the following types of control problem:

**Probity**

The Asian customers will have a relationship directly with the agent and indirectly with Aybe. Thus, anything the agent does will reflect upon Aybe; for example, if an agent was to conduct dishonest advertising and make unrealistic claims about Aybe’s products, this could affect Aybe’s reputation.
Performance
If Aybe uses agents, it has delegated the responsibility for market development and profitability to an organisation over which it has no direct control. Aybe could find that the agent has different objectives to itself; the agent might want very rapid growth whereas Aybe might wish to grow more conservatively. The agent may have divided loyalties as it is likely to hold agencies from a number of clients and some of these may be competitors of Aybe. Agents, as independent organisations, have autonomy from Aybe and this must be respected. However, this autonomy does imply severe restrictions on Aybe’s ability to control.

Culture
In the agent’s country, business may be conducted differently to how it is carried out in Aybe’s home country; for example, the amount of time for which trade credit is extended may be shorter/longer than in Aybe’s home country. If Aybe tries to impose its usual trade credit terms upon its agents/customers, this could cause difficulties.

Communication
Although modern communications are very efficient there still remain difficulties for Aybe trying to control its agents in Asia. Time differences must be taken into account and Internet and telephone communication are not always reliable. In addition, language differences will also complicate communication.

Requirement (c)(ii)

Probity
Aybe should enquire into any potential agent’s background and trading record. It could utilise published financial statements, bankers’ references and specialist agencies such as D&B (Dun & Bradstreet). Requirements could be incorporated in the agency agreement to govern the agent’s behaviour.

Performance
Objectives and performance measures should be a part of the agency agreement and Aybe could require regular reports from the agent as well as the right to inspect its internal accounts.

Culture
Aybe may have to accept the different cultural practices that exist within the agent’s country. However, the agency agreement should delineate boundaries that are mutually acceptable.

Communication
As with culture, some of these problems are likely to be insoluble. However, Aybe might overcome some difficulties by requiring the agent to make periodic visits to Aybe’s offices and this could be supplemented by Aybe personnel making visits to the agent’s premises. Such visits could be carried out by Aybe’s internal auditors.

Note: The discussion under (C)(i) and (C)(ii) is not exhaustive but illustrative and whilst the question asks for two control problems, four have been given by way of example. Candidates are always given credit for appropriate answers.

Requirement (d)(i)

Director of Operations 5 year forecast

<table>
<thead>
<tr>
<th>Year ending 31/12</th>
<th>Actual 2009 C$m</th>
<th>Forecast 2010 C$m</th>
<th>Forecast 2011 C$m</th>
<th>Forecast 2012 C$m</th>
<th>Forecast 2013 C$m</th>
<th>Forecast 2014 C$m</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incremental revenue</td>
<td>5.00</td>
<td>6.25</td>
<td>7.81</td>
<td>9.77</td>
<td>12.21</td>
<td>15.26</td>
</tr>
<tr>
<td>Incremental costs</td>
<td>1.00</td>
<td>1.25</td>
<td>1.56</td>
<td>1.95</td>
<td>2.44</td>
<td>3.05</td>
</tr>
<tr>
<td>Incremental profit for the year</td>
<td>4.00</td>
<td>5.00</td>
<td>6.25</td>
<td>7.82</td>
<td>9.77</td>
<td>12.21</td>
</tr>
</tbody>
</table>
**Requirement (d)(ii)**

From the incremental profit forecast it is possible to derive the following forecasts:

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Earnings per share</td>
<td>0.022</td>
<td>0.028</td>
<td>0.035</td>
<td>0.043</td>
<td>0.054</td>
<td>0.068</td>
</tr>
<tr>
<td>Dividend per share</td>
<td>0.011</td>
<td>0.014</td>
<td>0.017</td>
<td>0.022</td>
<td>0.027</td>
<td>0.034</td>
</tr>
</tbody>
</table>

The Director of Operations’ assumptions about the future are much more optimistic than those of the Management Accountant and this is reflected in both the Earnings per share and the Dividend forecasts. By 2014, for example, the Director of Operations’ Dividend forecast is 262% of that of the Management Accountant (C$ 0.034 c.f. C$ 0.013). It is not clear what the source of the Director of Operations’ assumptions is. If they are based on expert knowledge of the market, then the shareholders should benefit from the proposed expansion. Has the Director got access to other relevant information that he has not disclosed to the Management Accountant? If the assumptions are not based on expert knowledge, then the prospects for Aybe’s expansion are not so bright.

**Requirement (d)(iii)**

The Management Accountant has prepared a profit forecast according to Aybe’s normal procedures. The Director of Operations believes that this forecast is ‘totally unrealistic’. At this point, there is clearly a conflict, which is not unusual, but this does not necessarily constitute an ethical dilemma. However, the Director of Operations explains that a management accountant should not ‘question a director’s professional expertise’ and that ‘a good management accountant should help him by carrying out his requests’. The Director of Operations further instructs the Management Accountant to prepare a new profit forecast, based on the Director of Operations’ assumptions, for presentation to the Board of Aybe and that the Management Accountant should destroy her original profit forecast.

The Management Accountant is now in a difficult position. One of the roles of a management accountant is to assist decision-makers and the Director of Operations is asking for such assistance. The Management Accountant should also recognise that the Director of Operations has expertise outside the Management Accountant’s experience and should, within limits, defer to the Director of Operations’ greater knowledge.

However, the Management Accountant has followed the normal procedure within Aybe for preparing such a forecast and has consulted both with board members and operational managers. The assumptions within the Management Accountant’s profit forecast reflect not just her own views but also those of her colleagues. Just as she owes a duty to the Director of Operations to assist him in his decision-making, she owes a similar duty to Aybe and those who are involved with the decision to transact business in Asia. The Chartered Institute of Management Accountants (CIMA) has adopted a Code of Ethics (hereafter the Code) to give guidance to its members with regard to their behaviour when faced with situations such as these.

CIMA has established fundamental principles of professional ethics for professional accountants and these include the following:

**Integrity** ‘A professional accountant should be straightforward and honest in all professional and business relationships’.

CIMA further states that ‘A professional accountant should not be associated with reports etc. where they believe that the information:

‘Omits or obscures information required to be included where such omission or obscurity would be misleading’.

It is arguable that if the Management Accountant carried out the Director of Operations’ instruction she would be in conflict with the principle of integrity described above in that her own more conservative forecast would not be placed before the Board. It is arguable that such behaviour is not ‘straightforward and honest’.
CIMA has also defined a further principle, that of **Objectivity**: ‘A professional accountant should not allow bias, conflict of interest or undue influence of others to override professional or business judgements’.

The principle of objectivity imposes an obligation on all professional accountants not to compromise their professional or business judgement because of bias, conflict of interest or the undue influence of others.’

It is arguable that the Director of Operations is using his position and personality to make the Management Accountant suppress her conservative profit forecast in favour of his more optimistic one.

If the Management Accountant were to be given the opportunity to present both profit forecasts to the Board with both her and the Director of Operations given the opportunity to explain their differing points of view, there would not be an ethical dilemma.

However, because the Director of Operations has instructed the Management Accountant to destroy her forecast, such behaviour would conflict with the principles of Integrity and Objectivity. Therefore, an ethical dilemma exists.

*All the quotations in this section are from the CIMA Code of Ethics for Professional Accountants, October 2007.*
SECTION B

Answer to Question Two

Requirement (a)

Using the categories of Porter’s value chain the business has the following strengths and weaknesses:

Primary activities

Inbound logistics
No information given, so unable to classify this.

Operations
The business has outgrown the need for shop premises. The owners are unable to attend antiques fairs which have very good business potential. WEAKNESS.

Outbound logistics
The assumption is that storage and distribution is carried out at the shop premises. Mention was made in the case of the increasing cost of security, as the antiques require protection from theft. It could be that the shop premises are no longer the best place to store and distribute antiques. Possible WEAKNESS.

Marketing & Sales
The owners used to gain their business because of their location, but this is no longer as important. Latterly, they have built up a reputation and have many repeat customers. However, their use of the Internet is primitive and does not contribute to their business. This was a strength now turning into a WEAKNESS.

Service
As the owners have a national reputation and many repeat customers, this is classified as a STRENGTH.

Support Activities

Firm infrastructure
The owners have had a long history of profitable trading. However, recently they have made losses. WEAKNESS.

The owners’ premises, if sold, would enable them to realise ‘a substantial capital gain’. STRENGTH.

Human Resource Management
The owners work in the business and there are no employees. Their long survival in the business and their reputation as experts are STRENGTHS.

However, the people are the business and there is little possibility of succession. Further if the owners have been in business since 1980 they may be approaching retirement age. WEAKNESS.

Technology development
This seems to have been neglected. See Marketing & Sales.

Procurement
No direct evidence of this but longevity of business suggest that this has been a STRENGTH.

Requirement (b)

The owners have recently set up a website but this only has some basic information about their business. Although the website has received many hits, it hasn’t led to any increase in business. This suggests there is a wide degree of interest in their business but the website does not enable anyone who is remote from the town where JGS is based to do any business
with the owners. The obvious inference is that if they converted their website to facilitate e-commerce their business would increase in both turnover and profit.

Initial steps to take in the introduction of e-commerce would include preparing a project plan and also identifying the level and source of funds which would be required. If the owners are to set up a website with e-commerce capability they will need to catalogue, photograph and enter their stock onto the website. The website would need continual updating as stock is sold and new stock acquired. They would have to ensure that their server had adequate capacity to cope with the forecast level of traffic. The website would need to have good security to protect against viruses and fraud, and the owners would need to have a secure method of receiving payments to facilitate their customers’ transactions. If the owners do not have the requisite expertise, they will need to employ a consultant to help them establish the website, to give them some training and to be available to help with website modifications and emergencies.

All of the above will require a significant financial investment.

**Requirement (c)**

A move to e-commerce for the owners would affect the value chain of the owners in the following ways. If trading via the website takes off, the owners do not need to keep their shop. They will no longer be tied to a specific location and they could move their business. They will also save money on the shop’s fixed costs if they relocate to a cheaper area. Thus, their **Operations** will have altered.

The **Outbound logistics** of the business will be affected in a similar way to Operations.

**Marketing & Sales:** e-commerce represents a new way of doing business. It should lead to increased business as the owners are no longer subject to geographical boundaries and their antiques will be displayed on the web.

**Firm infrastructure:** the change to e-commerce could mean that the owners could return to profitability. They will also be able to realise their inherent capital gain on disposal of the shop and should benefit from an injection of cash.

**Human Resource Management:** e-commerce implies a new way of working for the owners. They can now attend fairs and travel which they have not been able to do previously as they will no longer be tied to their shop.

**Technology development:** with the adaption of e-commerce this aspect of the value chain will now be an important part of the business.

**Procurement:** the owner’s new website will put them in touch with a greater number of customers. This could give them access to new sources of supply of antiques.
Answer to Question Three

Requirement (a)

Implementation has been defined as: ‘the conversion of the strategy into detailed plans or objectives for operational units’. Implementation is an essential part of the model because no matter how good the strategic analysis and strategic choice have been, unless a proposed strategy is capable of being put into action there will be no benefit to the organisation.

In Johnson, Scholes and Whittington’s model, each of the three aspects are given equal weighting. The model represents these aspects as being inter-dependent; that is, they all inform each other. Thus, for example, Strategic Implementation is inter-linked with both Strategic Analysis and Strategic Choice. The elements affect each other and overlap. The model is not linear; i.e. there is not a definite pathway through the model. Strategy can start and end with any one of the aspects because it should be a dynamic process.

Requirement (b)(i)

Critical Success Factors (CSFs) are ‘those components of strategy where the organisation must excel to outperform competition’ (Johnson, Scholes and Whittington). It is implicit in the definition that any organisation will not have a great number of CSFs: six or fewer CSFs have been suggested as an appropriate number.

In the case of TDM, CSFs have to be identified which are specific to it and which are crucial for its success. The following CSFs are recommended:

**CSF: Customer satisfaction**

This CSF could be supported by such KPIs as:

*Student satisfaction:* most UK universities now carry out such surveys into this area and TDM could imitate this practice.

*Rate of repeat business:* many of TDM’s students will be sponsored by their employers. This KPI will measure if employers continue to use TDM.

**CSF: Employee attitudes**

This CSF could be supported by such KPIs as:

*Rate of staff turnover:* a high rate of staff turnover is suggestive of dissatisfaction, a low rate of contentment.

*Rate of staff absence:* a high rate indicates poor staff morale; a low rate suggests staff that are happy to come to work.

**CSF: Product quality**

This CSF could be supported by such KPI’s as:

*Market share:* TDM has consistently had the largest market share in its sector and both its absolute market share and trends in market share (Is it increasing? Is it decreasing?) are strongly indicative of success.

*Accreditations:* TDM’s courses are open to scrutiny by professional and academic bodies. TDM could measure the accreditations it receives which reflect outside opinion as to the level of quality it is achieving.

**CSF: Brand image**

This CSF could be supported by such KPIs as:

*Brand recognition:* this KPI could be assessed by means of survey with its customers, past, present and potential. This KPI would indicate the proportion of customers who are aware of TDM’s brand.

*Brand reputation:* as in the case of brand recognition, brand repute could be investigated to discover customers’ feelings about TDM’s brand. It could be that recognition and repute are contrary. It is possible for many people to know about your brand but not to like it. Alternatively, few people may know about a brand but those that do like it very much.

Candidates who suggested market leadership as a CSF also earned marks
Requirement (b)(ii)

Customer satisfaction
It is important that RCH knows how its customers feel about its services. As the CEO of RCH commented ‘...success is built on happy customers: we give them what they want’. TDM has to ensure that it is getting this aspect right if it is to continue to be successful. It is a truism that without customers TDM will not have a business. However, it appears to have had a production focus rather than a customer focus and has neglected this area in the past. One important indicator of customer satisfaction will be the students’ pass rates.

Employee attitudes
Employees are important in every business but this is particularly the case for TDM where its employees come into contact with its customers. It is vital that TDM’s employees continue to perform at a high level and so TDM should monitor their morale and the KPIs above will give an indication of this.

Product quality
Customers will only continue to use TDM’s services if it can demonstrate it is providing courses of a high quality. This can be measured, to an extent, by the endorsement of external bodies in the form of accreditations. It can also be tracked more immediately by the market share which TDM has gained. This KPI can be routinely calculated, perhaps at monthly intervals, unlike accreditations which will be granted intermittently.

Brand image
TDM does not have a strong customer focus and it is in a market where there are continually new entrants. Although it has had satisfactory performance in the past, ‘it has constantly achieved its sales targets and its students achieve passes on a par with the national average’ it seems to be an introspective organisation. It may not be performing to the best of its ability. In order to counteract these tendencies, TDM could benefit from an awareness of how it appears to the outside world.

The answer in this section is not exhaustive, other CSFs and KPIs could be discussed. However, candidates will always be given credit for appropriate contributions,
Answer to Question Four

Requirement (a)

Ansoff has four cells in his matrix which is formulated with axes based on:

- present and new products
- present and new markets

The CEO has described XZY’s strategy as being based on ‘selling what we know to who we know’. Although this has been a successful strategy in the past in terms of profitability and share price, XZY is now finding growth difficult to sustain.

This suggests that one of the cells of the matrix, Market Penetration, is approaching the point where it cannot offer any further growth to XZY.

In the context of Ansoff’s matrix the remaining options are:

Product development: this implies the launch of new products to existing markets. XZY would need to analyse the cause of its reduced growth. If it is because its existing products are coming to the end of their life-cycles, then launching new products in its existing markets could be an appropriate way forward.

If the slow-down in growth is due to some structural problem with Asian markets, for example recession, then offering new products to existing markets may not restore growth.

Market development: this option would mean that XZY would offer its existing products to new markets, for example Australia and Europe. This would be appropriate if the products were still vibrant and the reason for the slow-down in growth was that the Asian markets had become saturated or were suffering from structural problems.

Diversification: according to Ansoff’s matrix XZY’s remaining option would be to diversify which would commit XZY to making new products for new markets which could restore growth; for example, XYZ could offer a business service within Europe.

Each of the options above implies moving into new areas, to a greater or lesser extent, and so represents increased risk for XZY with diversification being the riskiest.

The CEO, who has a fiduciary duty to act in the best interest of XZY’s shareholders, should examine whether it is necessarily a bad thing if the company’s growth rate slows down. It could be better from the shareholders’ viewpoint than the endless pursuit of growth which, in the long-term, is an unrealistic aspiration.

Requirement (b)

The CEO will have the following difficulties to deal with:

- As the reorganisation is aimed at reducing headcount, staff will resist change either informally by negotiation and lobbying or perhaps formally by recourse to legal action.
- Many reorganisations do not fulfil their objectives and the new structure may damage XZY’s profit. This may occur as the workload may not reduce but will have to be carried out by fewer staff and this could result in poorer quality. This could adversely affect XZY’s share price.
- The reorganisation and its attendant difficulties may distract XZY’s management from its normal business and its customers might suffer as a result.
- The reorganisation may not be tackling XZY’s underlying problems, for example, that its products are at the end of their life-cycles or that the Asian market has structural problems. Thus, the CEO might be misled into putting his attention in the wrong areas.
- Although the reorganisation is designed to save money, in the short term it will cost money and the financial benefits may take longer to emerge. There is a possibility that the reorganisation might, in the short term, produce the opposite result to that which is intended.
Requirement (c)

A number of writers have suggested models or procedures to deal with change. One well-known model was proposed by Kurt Lewin and this would be appropriate for XZY to use. Lewin suggested that successful change could be achieved by the following three steps.

- **Unfreezing**: at this stage the CEO and his team would need to make the organisation aware of the need for change and its necessary preparations.
- **Change (Move)**: the organisation will have to understand its new structure and learn to function. It will involve people in learning new ideas and approaches, particularly about their own jobs. At this stage, XZY would be in a state of transition as it moves towards its final desired, post-reorganisation form.
- **Freeze (Refreeze)**: when this stage is reached, the changes have to become embedded in the organisation. All the staff remaining after the reorganisation and the headcount reduction must understand their new role and put this into practice. Therefore, it is at this point that the changes must be consolidated.

There are many other models and approaches to change that are available. *Candidates are given credit for any suitable model used appropriately.*

**Tactics**

In addition to the use of a model to structure the reorganisation and headcount reduction, the CEO needs to consider tactics that would contribute towards making this change successful. It would be helpful if XZY had a person identified as being the champion of the change. This needs to be an influential person and the most obvious person in this case would be the CEO who would be able to demonstrate that there was top-level support for the change. However, this role might be delegated to another Board member if the CEO has too many calls on his time.

The change champion could be supported by a project team who would be involved in the operational aspects of effecting the change.

The motivation of XZY employees could be influenced by providing incentives and disincentives to participants in the change. As well as incentives, or inducements, people could be encouraged/pressured to accept change if there are disincentives; for example, their promotion could be blocked for those who resist change.

It would be important throughout the three stage process that XZY emphasised good communications about the change with its staff. It would also assist motivation and embedding of the change if staff were allowed to contribute to the change process and its outcomes rather than simply being told what will happen to them.