

PAPER – 6: FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

Part I – Multiple Choice Questions

Case Scenario - I

RG Limited has estimated that number of operating cycle in year 2025-26 will be 3.

The amount of working capital required after taking an estimated 5% unforeseen contingency is ₹ 1,01,850. Other information is as under:

Opening stock of Finished goods is ₹ 31,100 and the closing stock will be lesser by ₹ 4,200 from the opening stock.

Opening stock of Raw Material is ₹ 24,450 and Closing stock of Raw material will be ₹ 28,200.

Opening stock of Work in Progress is ₹ 20,500 and Closing stock of Work in Progress will be more by ₹ 1,800 from the Opening stock.

Wages and Manufacturing expenses during the year will be ₹ 1,12,800.

Selling and Distribution expenses during the year will be ₹ 30,000.

Average Creditors for the year is ₹ 26,170.

All Purchases will be done on credit basis only.

Assume a 360 days year.

Using above information, you are required to answer the following questions 1 to 5:

1. *What will be the Total Operating Expenses and Cost of Goods Sold for the year?*

(A) ₹ 2,61,000 and ₹ 2,91,000

(B) ₹ 2,91,000 and ₹ 2,61,000

(C) ₹ 2,75,500 and ₹ 2,61,000

(D) ₹ 2,58,500 and ₹ 2,88,000

(2 Marks)

2. *What will be the Cost of Production and Finished Goods storage period?*
- (A) ₹ 2,58,600 and 45 Days
(B) ₹ 2,58,600 and 40 Days
(C) ₹ 2,56,800 and 45 Days
(D) ₹ 2,56,800 and 40 Days **(2 Marks)**
3. *What will be the Raw Material Consumed and Credit purchases?*
- (A) ₹ 1,52,500 and ₹ 1,50,550
(B) ₹ 1,49,500 and ₹ 1,52,500
(C) ₹ 1,45,800 and ₹ 1,49,550
(D) ₹ 1,52,000 and ₹ 1,45,800 **(2 Marks)**
4. *What will be the Raw material storage period and Work in Progress conversion period?*
- (A) 62 Days and 32 Days
(B) 65 Days and 30 Days
(C) 63 Days and 33 Days
(D) 63 Days and 45 Days **(2 Marks)**
5. *What will be the Creditors Payment period and Debtors Collection period?*
- (A) 60 Days and 50 Days
(B) 63 Days and 48 Days
(C) 62 Days and 45 Days
(D) 65 Days and 47 Days **(2 Marks)**
6. *PRAX Ltd. is an all-equity financed company, currently valued at ₹ 2,100 lakhs, with a cost of capital of 18%. The company is contemplating a strategic financial restructuring by:*
- (i) *Repurchasing ₹ 325 lakhs of equity shares.*
(ii) *Replacing the repurchased equity with 16% debentures.*
- The Company maintains constant Earnings Before Interest and Taxes (EBIT) and following a policy of distributing entire earnings as dividend.*

Corporate tax rate is 35%.

What would be the market value of Equity after structure modification as per Modigliani and Miller (MM) Approach?

- (A) ₹ 1,888.75 Lakh
- (B) ₹ 2,213.75 Lakh
- (C) ₹ 1,456.75 Lakh
- (D) ₹ 2,538.75 Lakh

(2 Marks)

7. KL Limited is replacing an existing machine. The replacement cost of the machine is ₹ 1,00,000 now and it requires maintenance of ₹ 20,000 at the end of every year for five years. At the end of Fifth year, it would have a salvage value of 10,000. The cost of capital is 14%.

$PVIFA_{0.14,5}$ is 3.433 and $PVIF_{0.14,5}$ is 0.519.

What will be the Equivalent Annual Cost (EAC) for the machine?

- (A) ₹ 57,617
- (B) ₹ 45,217
- (C) ₹ 47,617
- (D) ₹ 60,217

(2 Marks)

8. ABC Limited gives you the following information as on 31st March, 2025:

Current Liability : ₹ 1,60,000

Current ratio : 2.5

Liquid ratio (Quick ratio): 2

What will be the value of Stock?

- (A) ₹ 80,000
- (B) ₹ 1,20,000
- (C) ₹ 1,60,000
- (D) ₹ 64,000

(1 Mark)

Case Scenario - II

Solar Tech Innovation, a start-up specialization in next-generation solar panels entered the highly competitive renewable energy sector with a mission to make solar power more accessible and efficient. However, the company faced significant challenges, including high R&D costs, limited consumer awareness, regulatory compliance hurdles and stiff competition from established energy providers. To navigate these challenges, Solar Tech conducted an in-depth market analysis, identifying a strong demand for residential and commercial solar solution due to rising electricity cost and government incentives on green energy. However, it also noted threats from lower-cost alternatives and slow adoption in some regions.

To differentiate itself, Solar Tech developed ultra-thin, high efficiency solar panels that could generate more power in less space. This innovation appealed to homeowners and businesses looking for cost-effective grand space-saving solutions. The company also adopted a strategic expansion model, first targeting urban centers with high energy consumption and gradually moving to rural areas. Internally, the leadership headed by CEO Mr. Rajiv, implemented structural changes to improve decision making. The company embraced a decentralized approach enabling regional teams adapt their sales and marketing strategies to local market conditions. Additionally, Solar Tech partnered with financial institutions to offer easy financing options, making solar energy more affordable.

To enhance operational efficiency, Solar Tech streamlined its supply chain and secured bulk raw material procurement deals, reducing cost without compromising quality. Simultaneously, the company focused on customer education through digital marketing and community outreach programs, increasing awareness and adoption. Over four years, these strategic initiatives led to Solar Tech's expansion across multiple states, partnerships with real estate developers, and a 60% increase in annual revenue. By aligning technological innovation, operational efficiency and market expansion, the company successfully positioned itself in the renewable energy sector.

Based on the above case scenario, choose the correct answer to Q. Nos. 9 to 13.

9. *A company's core values are essential for decision making and strategic alignment. Which of the following would be considered a violation of Solar Tech Innovation's values?*

(A) Investing in high-efficiency solar panels that reduce carbon emissions.

- (B) Partnering with fossil fuel companies to increase short term profitability.
- (C) Launching an initiative to make solar energy more affordable for rural areas.
- (D) Encouraging employees to participate in sustainability programs.

(2 Marks)

10. Solar Tech expands its distribution network by forming partnerships with retail chains. This directly affects which value chain activity?

- (A) Firms infrastructure
- (B) Inbound logistics
- (C) Outbound logistics
- (D) Technology development

(2 Marks)

11. Solar Tech innovation partnered with financial institutions to offer easy financing options to make solar energy more affordable.

This decision falls under which strategic level?

- (A) Corporate Level
- (B) Business Level
- (C) Functional Level
- (D) Operational Level

(2 Marks)

12. Solar Tech is considering expanding into a developing country where electricity access is low. Which external factor is the primary reason for this decision?

- (A) Low production costs in the target country
- (B) Strong competition from global solar brands
- (C) Availability of skilled solar engineers
- (D) High demand for alternative energy sources

(2 Marks)

13. A leading real estate developer, Green Habitat Constructions, wants to integrate Solar Tech's next-generation panels into its residential and commercial projects.

Where would Green Habitat Constructions fall in Mendelow Matrix?

- (A) High power, High interest (Key Players)
- (B) Low power, Low interest (Low Priority)
- (C) Low power, High interest (Keep informed)
- (D) High power, Low interest (Keep Satisfied)

(2 Marks)

14. Bio Cure is pioneer in low-cost rapid diagnostic kits and commands strong brand loyalty in Tier-2 and Tier-3 Indian cities. The company holds a leading competitive position, thanks to its proprietary technology and wide distribution network. However, the rapid diagnostic industry is maturing, with new regulations, consolidation, and slowing growth rates. Many firms are shifting their focus to AI-powered health platforms, making it harder for traditional players to innovate without high R&D spend.

Based on the ADL matrix, where is Bio Cure positioned?

- (A) Dominant position in a declining industry
- (B) Strong position in a mature industry
- (C) Tenable position in a growing industry
- (D) Weak position in an ageing industry

(2 Marks)

15. Edu Edge Learning a digital education start-up, struggled with inconsistent communication and poor integration across departments. Although the strategy and talent were in place, collaboration was ineffective. In order to resolve this issue, the leadership launched a centralized knowledge-sharing platform and defined clear internal communication protocols. Performance appraisal systems were linked to teamwork and collaboration goals, ensuring alignment of all the processes with strategic intent.

Which aspects of the McKinsey 7-S Framework is being strengthened at Edu Edge?

- (A) Strategy
- (B) Structure
- (C) System
- (D) Skills

(2 Marks)

16. In General Electric Matrix, what strategy is recommended for business units with high market attractiveness and strong business strength?

- (A) Invest/Expand
- (B) Select/Earn
- (C) Harvest/Divest
- (D) Liquidate

(1 Mark)

Answer Key

MCQ No.	Correct Option
1.	B
2.	D
3.	C
4.	B
5.	B
6.	A
7.	C
8.	A
9.	B
10.	C
11.	C
12.	D
13.	A
14.	B
15.	C
16.	A

Part II – Descriptive Questions

SECTION A: FINANCIAL MANAGEMENT

Question No. 1 is compulsory.

Attempt any **two** questions out of the remaining **three** questions.

In case, any candidate answers extra question(s)/ sub-question(s) over and above the required number, then only the requisite number of questions first answered in the answer book shall be valued and subsequent extra question(s) answered shall be ignored.

Working notes should form part of the answer.

Question 1

(a) The capital structure of RSA Limited is as under:

	(₹)
Equity Shares (₹ 10 per share)	1,00,00,000
8% Irredeemable Preference Shares (₹100 per share)	5,00,00,000

Additional Information:

- (i) Equity shares are quoted at ₹ 60 each and a new issue priced at ₹ 60 will be fully subscribed; flotation cost will be ₹ 4 per share.
- (ii) Issue price of the 8% Irredeemable preference shares was ₹ 45.
- (iii) Current market price of the 8% irredeemable preference shares is ₹ 55.

RSA Limited has been paying dividend to its equity shareholders at a constant growth rate of 5% per year and the dividend paid this year was ₹ 2 per equity share.

You are required to calculate:

- (i) The cost of equity using Gordon's model
- (ii) The cost of the irredeemable preference share
- (iii) The weighted average cost of capital using market value weights.

(2 + 1 + 2 = 5 Marks)

(b) Diwan Limited has outlined its financial projections for the fiscal year 2025-26. The company plans to utilize total assets amounting to

₹ 50,00,000, with 35% of assets financed through debt at interest rate of 10.50% per annum. Projected sales revenue is ₹ 55,00,000. Direct costs are estimated at ₹ 30,00,000 and other operating expenses are estimated at ₹ 4,80,000. The applicable tax rate is 33%

You are required to calculate:

- (i) Profit After Tax (PAT)
- (ii) Net profit margin (After tax)
- (iii) Return on Assets (After tax)
- (iv) Asset turnover ratio
- (v) Return on Equity

(1 x 5 = 5 Marks)

- (c) Global Beverage Corporation is considering replacing one of its bottling machines with a newer and more efficient model. The existing machine was purchased five years ago for ₹ 16,00,000 and has a total useful life of ten years. Currently, the company can sell this machine for ₹ 9,60,000. The new machine costs ₹ 32,00,000 having an estimated salvage value of ₹ 3,20,000 and a useful life of five years. With the new machine, annual contribution margin is projected to increase from ₹ 16,00,000 to ₹ 18,40,000 and operating efficiencies are expected to yield further annual savings of ₹ 3,20,000. Depreciation is calculated on a straight-line method over the machine's five-year life. The company's cost of capital is 12% and corporate tax rate is 33%.

You are required to calculate the Net Present Value of new machine.

Given: $PVIFA_{0.12,5}$ is 3.605 and $PVIF_{0.12,5}$ is 0.567

(5 Marks)

Answer

$$\begin{aligned}
 \text{(a) (i) } K_e &= \frac{D_1}{P_0 - F} + g \\
 &= \frac{2(1+0.05)}{60-4} + 5 \\
 &= 8.75\% \\
 \text{(ii) } K_p &= \frac{PD}{P_0}
 \end{aligned}$$

$$= \frac{8}{45}$$

$$= 17.78\%$$

(iii) Calculation of WACC using market value weights

Source of capital	Market Value	Weights	Cost of capital	WACC (K _o)
	(₹)	(a)	(b)	(c) = (a) × (b)
Equity shares	6,00,00,000	0.6857	0.0875	0.0600
Preference shares	2,75,00,000	0.3143	0.1778	0.0559
	8,75,00,000	1		0.1159

WACC (K_o) = 0.1159% or 11.59%

If P₀ is taken as current market price for calculation of preference share

$$(ii) K_p = \frac{PD}{P_0}$$

$$= \frac{8}{55}$$

$$= 14.55\%$$

(iii) Calculation of WACC using market value weights

Source of capital	Market Value	Weights	Cost of capital	WACC (K _o)
	(₹)	(a)	(b)	(c) = (a) × (b)
Equity shares	6,00,00,000	0.6857	0.0875	0.06
Preference shares	2,75,00,000	0.3143	0.1455	0.0457
	8,75,00,000	1		0.1057

WACC (K_o) = 0.1057% or 10.57%

(b) (i) Income Statement

Particulars	(₹)
Sales	55,00,000
Less: Direct Cost	30,00,000
Gross Profit	25,00,000
Less: Operating Expenses	4,80,000
EBIT	20,20,000
Less: Interest (50,00,000 x 35% x 10.5%)	1,83,750
Profit Before Tax	18,36,250
Less: Tax @ 33%	6,05,963
Profit After Tax	12,30,287

$$\begin{aligned} \text{(ii) Net Profit Margin after tax} &= \frac{\text{Net Profit after taxes}}{\text{Sales}} \\ &= \frac{12,30,287}{55,00,000} = 22.37\% \end{aligned}$$

OR

$$\begin{aligned} &= \frac{\text{EBIT}(1-t)}{\text{Sales}} \\ &= \frac{20,20,000(1-0.33)}{55,00,000} = 24.61\% \end{aligned}$$

$$\begin{aligned} \text{(iii) Return on Assets (ROA)} &= \frac{\text{EBIT}(1-t)}{\text{Average total assets}} \\ &= \frac{20,20,000(1-0.33)}{50,00,000} = 27.07\% \end{aligned}$$

$$\text{(iv) Asset turnover} = \frac{\text{Sales}}{\text{Assets}} = \frac{55,00,000}{50,00,000} = 1.1 \text{ times}$$

$$\text{(v) Return on equity} = \frac{\text{Net Profit after taxes}}{\text{Owners' equity}}$$

$$= \frac{₹ 12,30,287}{65\% \text{ of } ₹ 50,00,000}$$

$$= \frac{12,30,287}{32,50,000} = 37.85\%$$

(c) Calculation of Net Initial Cash Outflows:

Particulars	₹
Cost of new machine	32,00,000
Less: Sale proceeds of existing machine	(9,60,000)
Add: Tax paid on sale of existing machine {(9,60,000 – 8,00,000) x 33%}	52,800
Net initial cash outflows	22,92,800

Calculation of Net Present Value of new machine

Particulars	₹
Incremental Contribution	2,40,000
Add: Cost saving	3,20,000
Savings	5,60,000
Less: Incremental Depreciation {5,76,000-1,60,000}	4,16,000
Incremental Profit Before Tax	1,44,000
Less: Tax @ 33%	47,520
Profit After Tax	96,480
Add: Depreciation	4,16,000
Cash Inflow	5,12,480
PVIFA	3.605
PV of Cash Inflow	18,47,490
Add: PV of Salvage Value of new machine (₹ 3,20,000 x 0.567)	1,81,440
Total PV of Cash Inflow	20,28,930
Less: Initial Cash Outflow	22,92,800
NPV	(2,63,870)

If Tax on sale of existing machine is not taken**Calculation of Net Initial Cash Outflows:**

Particulars	₹
Cost of new machine	32,00,000
Less: Sale proceeds of existing machine	(9,60,000)
Net initial cash outflows	22,40,000

Accordingly, NPV Will be ₹ 20,28,930 - ₹ 22,40,000 = (₹ 2,11,070)

Question 2

- (a) *M/s KRY Limited is a mid-sized company engaged in manufacturing and sales of Industrial equipment. The capital structure of the company is as under:*

<i>Equity Share Capital (12,500 Shares of ₹100 each)</i>	<i>₹12,50,000</i>
<i>6% Debentures</i>	<i>₹ 50,00,000</i>
<i>8% Bank of Loan</i>	<i>XXXXX</i>
<i>Other information are as under:</i>	
<i>Total Sales</i>	<i>₹ 75,00,000</i>
<i>P/V Ratio</i>	<i>40%</i>
<i>Operating Leverage</i>	<i>2.4</i>
<i>Corporate Tax Rate</i>	<i>3.84</i>
<i>Corporate Tax Rate</i>	<i>30%</i>
<i>P/E Ratio</i>	<i>8</i>

You are required to calculate following:

- (i) *Earnings Before Interest and Tax*
(ii) *Fixed Cost excluding interest*
(iii) *Amount of Bank Loan and Bank Interest* (iv) *Earning Per Share*
(v) *Market Price Per Share* **(1 + 1 + 2 + 2 + 1 = 7 Marks)**
- (b) *Saraswati Ltd. has started its business a year back with a paid-up equity capital of ₹ 50,00,000. The other details are as under:*

<i>Earnings of company</i>	₹ 5,00,000
<i>Cost of Capital</i>	₹ 159.09
<i>Market price per share using Gordon's Model</i>	8%
<i>Internal rate of return on investment</i>	12%
<i>Number of shares</i>	50,000

You are required to:

- (i) Calculate the Dividend paid per share using Gordon's Model.
- (ii) What will be Optimum dividend pay-out ratio according to Gordon's Model when $r = K_e$? **(2 + 1 = 3 Marks)**

Answer

(a) (i) Operating Leverage = $\frac{\text{Contribution}}{\text{EBIT}}$

2.4 = $\frac{75,00,000 \times 0.40}{\text{EBIT}}$

EBIT = 12,50,000

(ii) Fixed Cost excluding interest = Contribution – EBIT

= 30,00,000 – 12,50,000 = 17,50,000

(iii) Combined Leverage = $\frac{\text{Contribution}}{\text{EBT}}$

3.84 = $\frac{30,00,000}{\text{EBT}}$

EBT = 7,81,250

Total Interest = EBIT – EBT = 4,68,750

Interest on bank loan = Total Interest – Interest on debentures

= 4,68,750 – 3,00,000 = 1,68,750

Amount of bank loan = 1,68,750/8%

= 21,09,375

(iv)

Particulars	(₹)
EBT (Earnings before tax)	7,81,250
Less: Tax @ 30%	2,34,375
PAT (Profit after tax)	5,46,875
No. of shares	12,500
Earnings per share (EPS)	43.75

$$(v) \text{ Market price per share} = \text{EPS} \times \text{PE Ratio}$$

$$= 43.75 \times 8 = 350$$

$$(b) (i) P_0 = \frac{E(1-b)}{K_e - br}$$

$$159.09 = \frac{10(1-b)}{0.08 - 0.12b}$$

$$159.09(0.08 - 0.12b) = 10(1-b)$$

$$12.7272 - 10 = 19.0908b - 10b$$

$$2.7272 = 9.0908b$$

$$B \text{ (retained earning ratio)} = 0.30$$

$$\text{Dividend payout ratio} = (1-b) = 0.70$$

$$\text{Dividend per share} = \text{EPS} \times (1-b) = 10 \times 0.70 = ₹ 7$$

(ii) When $r = K_e$, There is no optimum ratio**Question 3**

(a) AVS Limited is planning to diversify its cotton manufacturing business. The Chief Financial Officer (CFO) intends to raise fund of ₹ 22,00,000 for this project. The current estimates of Earnings Before Interest and Taxes (EBIT) from the new project are ₹ 5,00,000 per annum. The company's share is currently selling at ₹ 120 and is expected to decline to ₹ 110, in case the funds are borrowed more than ₹ 10,00,000. It is stated that the cost of debt will be 14% up to ₹ 8,00,000, 16% for additional amount of ₹ 2,00,000 above ₹ 8,00,000 and 18% for additional amount above ₹ 10,00,000. The tax rate

applicable to the company is 30%. the following options are in consideration of the company.

Option	Debt	Equity
I	60%	40%
II	50%	50%
III	40%	60%

Considering the objective of maximising Earning Per Share (EPS), which option of financing should the company choose? **(7 Marks)**

- (b) A company issues 20,000, 18% Debentures of ₹100 each. The debentures are redeemable after a period of 8 years. The cost of debentures using approximation method is 14.58%. The corporate tax rate is 30%. You are required to calculate:
- (i) Issue price of the Debentures, if redeemable at par.
- (ii) Revised Cost of Debentures using approximation method, if redeemable at 10% Premium after 8 years. **(2 + 1 = 3 Marks)**

Answer

(a)

Particulars	Options		
	Option-I: 60% Debt	Option-II: 50% Debt	Option-III: 40% Debt
	₹	₹	₹
Debt	13,20,000	11,00,000	8,80,000
Equity	8,80,000	11,00,000	13,20,000
EBIT	5,00,000	5,00,000	5,00,000
Interest on Debts:			
- on debt upto ₹ 8 lacs @14%	(1,12,000)	(1,12,000)	(1,12,000)
- on debt above 8 lacs and upto 10 lacs @ 16%	(32,000)	(32,000)	(12,800)
- on debt above 10 lacs @ 18%	(57,600)	(18,000)	---

Profit before taxes	2,98,400	3,38,000	3,75,200
Taxes @ 40%	(89,520)	(1,01,400)	(1,12,560)
Profit after taxes	2,08,880	2,36,600	2,62,640
Number of shares	8,000	10,000	11,000
Earnings per share	26.11	23.66	23.88

Since Option 1 i.e 60% debt provide the maximum EPS, company should choose Option 1 (60% debt and 40% equity) for financing.

(b) (i) Cost of Redeemable Debenture (K_d)

$$= \frac{I(1-t) + \frac{(RV-NP)}{n}}{(RV+NP) \times \frac{1}{2}}$$

$$0.1458 = \frac{18(1-0.3) + \frac{(100-NP)}{8}}{(100+NP) \times \frac{1}{2}}$$

$$0.1458 = \frac{(100.8 + 100 - NP) \times 2}{800 + 8NP}$$

$$116.64 + 1.166NP = 401.6 - 2NP$$

$$3.166 NP = 284.96$$

$$NP = 90$$

(ii) Revised Cost of Redeemable Debenture (K_d)

$$= \frac{I(1-t) + \frac{(RV-NP)}{n}}{(RV+NP) \times \frac{1}{2}}$$

$$= \frac{18(1-0.3) + \frac{(110-90)}{8}}{(110+90) \times \frac{1}{2}}$$

$$= 15.1\%$$

Question 4

Answer the following:

- (a) Discuss any 2 advantages and limitations of Stock Splits. **(4 Marks)**
- (b) Explain in brief the following types of bonds:
- (i) Callable Bonds
 - (ii) Puttable Bonds
 - (iii) Masala Bonds
 - (iv) Drop Lock Bonds **(4 Marks)**
- (c) Explain two basic functions of Financial Management. **(2 Marks)**

OR

- (c) Explain any two limitations of profit maximization objective of Financial Management. **(2 Marks)**

Answer**(a) Advantages of Stock Splits**

1. It makes the share affordable to small investors.
2. Number of shares may increase the number of shareholders; hence the potential of investment may increase.

Limitations of Stock Splits

1. Additional expenditure needs to be incurred on the process of stock split.
2. Low share price may attract speculators or short term investors, which are generally not preferred by any company

- (b) (i) Callable bonds:** A callable bond has a call option which gives the issuer the right to redeem the bond before maturity at a predetermined price known as the call price (Generally at a premium).
- (ii) Puttable bonds:** Puttable bonds give the investor a put option (i.e. the right to sell the bond) back to the company before maturity.

(iii) Masala Bonds: Masala (means spice) bond is an Indian name used for Rupee denominated bond that Indian corporate borrowers can sell to investors in overseas markets.

(iv) Drop Lock Bond: It is a Floating Rate Note with a normal floating rate. The floating rate bond would be automatically converted into fixed rate bond if interest rate falls below a predetermined level. The new fixed rate stays till the drop lock bond reaches its maturity.

(c) Basic function of financial management:

(a) Investment decisions (I): These decisions relate to the selection of assets in which funds will be invested by a firm.

(b) Financing decisions (F): These decisions relate to acquiring the optimum finance to meet financial objectives and seeing that fixed and working capital are effectively managed.

(c) Dividend decisions (D): These decisions relate to the determination as to how much and how frequently cash can be paid out of the profits of an organisation as income for its owners/shareholders.

(d) Working Capital Management (WCM): Generally short term decision are reduced to management of current asset and current liability

OR

(c) Limitations of profit maximisation objective:

(i) The term profit is vague. It does not clarify what exactly it means.

(ii) Profit maximisation has to be attempted with a realisation of risks involved.

(iii) Profit maximisation as an objective does not take into account the time pattern of returns.

(iv) Profit maximisation as an objective is too narrow.

SECTION – B: STRATEGIC MANAGEMENT**Part II**

Question paper comprises of **4** questions, Answer Question No. **5** which is compulsory and any **2** out of the remaining **3** questions.

Question 5

- (a) ARP Motors, an automobile company, was struggling in the competitive SUV market in India. As a business strategist, you recommended that ARP launch a compact SUV that balances affordability with premium features. In response, ARP developed and introduced FLEXON, strategically pricing it and incorporating high-end features such as a 5-star Global NCAP safety rating, a modern design and an advanced technology. Furthermore, the company expanded into the electric vehicle segment with FLEXON EV, positioning it as one of the most affordable yet feature-rich electric SUVs in India.

Which strategy did you recommend to ARP Motors to achieve a competitive advantage? Explain the strategy briefly and enumerate the key ways ARP Motors implemented it. **(5 Marks)**

- (b) You are the CFO of a multinational corporation that has been facing declining profitability in one of its business units for the past three years. It has been struggling with negative cash flows and intense competition. Significant investment would be needed for technological upgrades. You are not interested in investing in restructuring and revitalizing. A more promising investment opportunity is available elsewhere. As CFO, what step would you take in response to this situation? How would you justify your decision? **(5 Marks)**
- (c) XYZ Ltd. recently formulated an international expansion strategy and implemented the new market expansion strategy with the aim of increasing its presence in international markets. However, six months into the implementation, sales figures are not meeting projections. Improper use of resources, undesirable tendencies of the workers, non-conformance to norms and standards and unforeseen regulatory challenges have emerged. Additionally, competitor activity has intensified, affecting market share. As a strategic decision-maker, which function of strategic management process would you perform? What specific elements of that function would

you implement to overcome these issues and ensure that planned actions translate into successful achievement of goals and results? (5 Marks)

Answer

- (a) The strategy recommended to ARP Motors is the **Best-Cost Provider Strategy**.

Best-cost provider strategy is directed towards **giving customers more value for their money** by emphasizing both **low cost and premium features**. The objective is to keep costs and prices lower than those of other sellers of comparable products while offering better quality and superior features.

Application in ARP Motors Case:

- **Launch of FLEXON (Compact SUV):** ARP priced FLEXON strategically at an affordable level, while at the same time incorporating **premium features** such as a 5-star Global NCAP safety rating, advanced technology and a modern design. This reflects the approach of offering **better quality at lower or comparable prices**.
 - **Introduction of FLEXON EV:** By entering the electric vehicle market, ARP positioned FLEXON EV as one of the **most affordable yet feature-rich electric SUVs in India**. This aligns with the principle of **charging lower prices for comparable products or offering higher quality for similar prices** thereby giving customers **more value for money**.
- (b) As CFO, the appropriate step would be to adopt a **Divestment Strategy** for the business unit.

Divestment strategy involves the **sale or liquidation of a portion of business, a major division, profit centre or SBU**. It is usually adopted when a turnaround has been attempted but has proved unsuccessful or when it is obvious that divestment is the only answer.

The decision is further justified because:

- **Persistent negative cash flows** from this unit are creating financial strain.
- **Intensity of competition** makes survival difficult.

- **Technological up gradation is not feasible** for the company at this stage.
- **A better alternative investment opportunity is available elsewhere** making it preferable to release resources from the loss-making unit.

Thus, adopting **Divestment Strategy** will allow the company to stop financial losses, free resources and reallocate them to more promising opportunities, thereby ensuring long-term value creation.

- (c) In the given case, XYZ Ltd. should perform the **Strategic Control function** of the strategic management process.

Strategic control ensures that what is planned is translated into results by regulating behaviour, placing curbs on undesirable tendencies, ensuring conformance to norms and standards, monitoring proper use of resources, and coping with changes in the environment.

The **process of control** involves the following elements:

1. **Objectives** of the business system operationalized into measurable and controllable standards.
2. **Monitoring and measuring performance** of the system.
3. **Comparison of results** with standards, detecting deviations and gaining insights on standards themselves.
4. **Feedback and corrective action** to make desired changes and keep the system on course.

By applying strategic control and its elements XYZ Ltd. can overcome deviations and ensure successful achievement of its international expansion goals.

Question 6

- (a) "A well-defined vision and mission statement provide direction and purpose to an organization." Explain the significance of vision and mission statements in strategic planning. **(5 Marks)**
- (b) Which concept explains the efficiency increase gained by worker through repetitive production work, leading to cost reduction and competitive advantage? List down its relevance features in strategic management.

(5 Marks)

Answer

- (a) Strategic Management is a dynamic process of formulation, implementation, evaluation and control of strategies to realise the organisation's **strategic intent**. Strategic intent clarifies *what the organisation wants to do and why it wants to do it*, which forms the basis of **vision and mission statements**.

A **vision statement** describes the organisation's future aspirations and desired position while a **mission statement** explains its present business scope, purpose, goals and the means to achieve them. Together, they provide **direction and purpose** in strategic planning.

Significance of Vision in Strategic Planning:

- Provides a blueprint of where the organisation wants to be.
- Aligns organisational efforts on a chosen path.
- Creates enthusiasm and mould's identity.
- Clarifies aspirations in products, markets, customers and technology.

Significance of Mission in Strategic Planning:

- Explains the reason for the firm's existence.
- Ensures unanimity of purpose and efficient resource use.
- Standard for allocation and goal translation.
- Gives distinct identity and direction.
- Reflects present activities and ensures legitimacy.

Thus, a well-defined vision and mission provide clarity of purpose, direction for growth and a framework for decision-making. Vision answers, *"where we want to go,"* and mission answers *"what business we are in and why we exist."* Together, they form the philosophical base of strategy and guide the organisation toward long-term success.

- (b) The concept is **Experience Curve**. The experience curve, akin to a learning curve, explains the efficiency increase gained by workers through repetitive productive work. It is based on the phenomenon that unit costs decline as a firm accumulates experience in terms of a cumulative volume of production – the idea being, *"we learn as we grow."*

Relevant Features of Experience Curve in Strategic Management

- As business organisations grow, they gain experience which enables cost efficiencies.
- Experience may provide an advantage over competition as lower costs create a barrier for new entrants.
- Experience is considered a key barrier to entry for new firms contemplating industry entry.
- Large and successful organisations possess stronger experience effect, helping in leadership and cost advantage.

Thus, the experience curve is a critical concept in strategic management as it links growth with learning, cost reduction and competitive advantage, making it a strong determinant of industry positioning and entry barriers.

Question 7

- (a) *"The primary objective of SWOT analysis is to help organizations develop a full awareness of all factor involved in making a business decision."*

In the light of the above statement, explain why is it necessary to do SWOT analysis for business organization before using the strategy. (5 Marks)

- (b) *"In a dynamic business environment, merger serves as a critical tool for companies seeking expansion, synergy creation and competitive advantage." Discuss the concept of mergers, their classifications and their impact on business performance. (5 Marks)*

Answer

- (a) The **primary objective of SWOT analysis** is to help organizations develop a full awareness of all the factors (internal as well as external) involved in making a business decision. Hence, it becomes necessary to conduct SWOT analysis before strategy formulation for the following reasons:

- SWOT analysis identifies the **Strengths and Weaknesses (internal factors) and Opportunities and Threats (external factors)**. This ensures that management considers all aspects before deciding on a strategic move.

- It helps in discovering recommendations and strategies with a focus on **leveraging strengths and opportunities** while working to **overcome weaknesses and threats**. This lays the base for realistic and practical strategies.
- SWOT highlights both – the areas where the business is **performing well** and the **areas which need improvement**. This helps organizations to **align resources efficiently to achieve objectives**.
- Periodic SWOT analysis helps organizations to check the **current landscape** of their business and to **make necessary improvements** in operations, thus keeping **strategies relevant to changing circumstances**.
- It places complex internal and external issues into a **simple framework**, making it **easier** for managers **to identify challenges, opportunities, and competitive factors** before finalizing a strategy.

Thus, SWOT analysis is a necessary step before using any strategy, as it ensures that decisions are based on both **internal capabilities** and **external realities**, thereby increasing the chances of success in achieving organizational objectives.

- (b) **Merger** is a process when two or more companies come together to expand their business operations. In such a case the deal gets finalized on friendly terms and both the organizations share profits in the newly created entity. In a merger two organizations combine to increase their strength and financial gains along with breaking of the trade barriers.

Types of Mergers and their impact on business performance

- (a) **Horizontal Merger:** A horizontal merger occurs when two firms in the same industry and direct competitors combine. Its objective is to achieve economies of scale by eliminating duplication, widening product lines, reducing investment in working capital and fixed assets and removing competition, thereby strengthening market position and efficiency.
- (b) **Vertical Merger:** A vertical merger occurs between firms in the same industry at different production or distribution stages. It may involve backward integration (taking over suppliers) or forward integration

(acquiring buyers/distributors). Such mergers create synergies, cost efficiencies and advantages by controlling inputs, reducing dependence and enhancing overall operational and financial performance.

- (c) **Co-generic Merger:** A co-generic merger takes place between firms related through production processes, markets, or technologies. It allows product line extension or acquisition of components essential for operations. Such mergers enable businesses to diversify around common resources and strategic needs, creating opportunities for growth, synergy and better utilization of existing capabilities.
- (d) **Conglomerate Merger:** A conglomerate merger involves firms from unrelated industries with no direct linkages in customers, functions or technologies. It helps companies diversify risk, enter new markets and expand business portfolios. Though largely unrelated, some overlap in production, marketing or R&D may exist, offering opportunities for growth and financial stability.

Question 8

(a) *"A close and continuous interaction between a business and its environment helps in strengthening the business firm and using its resources more effectively." Explain Business environment and discuss how does the interaction between a business and its environment helps the business firm. (5 Marks)*

(b) *"Many managers fail to distinguish between strategy formulation and strategy implementation. Yet, it is crucial to realize the difference between the two because they both require very different skills."*

On the basis of this statement, outline the key distinctions between strategy formulation and strategy implementation. (5 Marks)

OR

(b) *Write a short note on the hourglass organizational structure. (5 Marks)*

Answer

- (a) The term **business environment** refers to all **external factors, influences, or situations that** in some way **affect business decisions, plans, and operations**. It is highly dynamic and continuously evolving. Organizational success depends not only on its internal abilities but also on its relationship with the external environment.

Interaction between Business and Environment: A close and continuous interaction strengthens the business firm and enables effective utilization of resources in the following ways:

- i. **Determine opportunities and threats:** The interaction between the business and its environment would explain opportunities and threats to the business. It helps to find new needs and wants of the consumers, changes in laws, changes in social behaviours and tells what new products the competitors are bringing in the market to attract consumers.
- ii. **Give direction for growth:** The interaction with the environment enables the business to identify the areas for growth and expansion of their activities. Once the business is aware and understands the changes happening around, it can plan and strategies to have successful business.
- iii. **Continuous Learning:** The managers are motivated to continuously update their knowledge, understanding and skills to meet the predicted changes in the realm of business.
- iv. **Image Building:** Environmental understanding helps the business organizations to improve their image by showing their sensitivity to the environment in which they operate.
- v. **Meeting Competition:** It helps the businesses to analyse the competitors' strategies and formulate their own strategies accordingly. The idea is to flourish and beat competition for its products and services.

(b) Difference between Strategy Formulation and Implementation

Strategy Formulation	Strategy Implementation
Strategy Formulation includes planning and decision-making involved in developing organization's strategic goals and plans.	Strategy Implementation involves all those means related to executing the strategic plans.
In short, Strategy Formulation is placing the Forces before the action.	In short, Strategy Implementation is managing forces during the action.

An Entrepreneurial Activity based on strategic decision-making.	An Administrative Task based on strategic and operational decisions.
Emphasizes on effectiveness .	Emphasizes on efficiency .
Primarily an intellectual and rational process .	Primarily an operational process .
Requires co-ordination among few individuals at the top level .	Requires co-ordination among many individuals at the middle and lower levels .
Requires a great deal of initiative, logical skills, conceptual intuitive and analytical skills .	Requires specific motivational and leadership traits .
Strategic Formulation precedes Strategy Implementation.	Strategy Implementation follows Strategy Formulation.

OR

In recent years information technology and communications have significantly altered the functioning of organizations. **The role played by middle management is diminishing** as the tasks performed by them are increasingly being **replaced by the technological tools**. Hourglass organization **structure consists of three layers** in an organization structure **with constricted middle layer**. The structure has a short and narrow middle management level.

Information technology links the top and bottom levels in the organization reducing away many tasks that are performed by the middle level managers. A shrunken middle layer coordinates diverse lower-level activities.

Hourglass structure has obvious benefits from reduced costs. It also helps in **enhancing responsiveness by simplifying decision making**. Decision making authorities are shifted close to the source of information, so **decision making is faster**. However, with the reduced size of middle management, **the promotion opportunities for the lower levels diminish significantly**.