ANSWERS OF MODEL TEST PAPER 2

INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

PART I – Case Scenario based MCQs

1. 1. (d) 14.99%

B = retention ratio=0.6, r=return on equity=20%, DPS=D0=20 x 0.4= 8,

MPS = P0 = EPS x PE = 20 x 15=300

G = b.r =0.6 x 20% = 12%

D1 = D0(1+g) = 8 (1.12) = 8.96

Ke = D1/P0 + g = 8.96/300 + 0.12 = 14.99%

2. (c) 90.58

Price of debentures= PV of future cash flows for investor discounted at their yield

= 8 x PVAF(9.5%,10 years)+ 100 x PVF(9.5%, 10 years)

= 8 x 6.2788 + 100 x 0.4035

=50.2304 + 40.35

=90.58

3. (a) 7.64%

NP = 90.58 x 96% = 86.96, RV = 100, Interest = 8, t = 0.27, n = 10

$$Kd = \frac{Int(1-t)+(RV-NP)/n}{(RV+NP)/2}$$

$$= \frac{8(1-0.27)+(100-86.96)/10}{(100+86.96)/2}$$

= 7.64%

4. (b) 9.77%

$$Kp = \frac{PD+(RV-NP)/n}{(RV+NP)/2}$$

$$= \frac{100+(1100-1050)/10}{(1100+1050)/2}$$

= 9.77%

5. (a) 10.52%

	Existing	Total	Additional	
Equity Funds	1,60,00,000	2,00,00,000	40,00,000	

Preference Shares		24,00,000	24,00,000	
Debt		56,00,000	56,00,000	
	1,60,00,000	2,80,00,000	1,20,00,000	
Capital gearing =	0.4			
(PSC + Debt)/Equity =	0.4			
(Total Funds -Equity)/ Equity = 0.4				
(2.8 crores-Equity)/ equity = 0.4				
Equity =	2 crores			
Weighted avg cost of marginal capital		**Weights**	**Cost**	**W.C**
Equity Funds	40,00,000	0.333333333	14.99%	5.00%
Preference Shares	24,00,000	0.2	9.77%	1.952%
Debt	56,00,000	0.466666667	7.64%	3.565%
Total	**1,20,00,000**			**10.52%**

2. (a) 9.74%

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

$$K_d = \left[\frac{10(0.7) + \frac{110 - 85}{10}}{97.5}\right]$$

= 9.50/97.5 = 9.74%

3. (c) 2.5

Margin of safety = (sales – BEP sales)/sales x 100

= 40%

Degree of operating leverage = 1/MOS

= 1/40% = 2.5

4. (a) 20%

$$\text{Payback Reciprocal} = \frac{\text{Average annual cash in flow}}{\text{Initial investment}}$$

$$= \frac{₹\,4,000 \times 100}{₹\,20,000} = 20\%$$

PART II – Descriptive Questions

1. (a) (i) Working Notes:

(i) Computation of Annual Cash Cost of Production	(₹)
Material consumed	12,00,000
Wages	9,60,000
Manufacturing expenses	12,00,000
Total cash cost of production	**33,60,000**
(ii) Computation of Annual Cash Cost of Sales:	**(₹)**
Total Cash cost of production as in (i) above	33,60,000
Administrative Expenses	3,60,000
Sales promotion expenses	1,20,000
Total cash cost of sales	**38,40,000**
Add: Gross Profit @ 20% on sales (25% on cost of sales)	9,60,000
Sales Value	**48,00,000**

Statement of Working Capital requirements (cash cost basis)

	(₹)	(₹)
A. Current Assets		
Inventory:		
- Raw materials $\left(\frac{₹12,00,000}{12 \text{ months}} \times 2 \text{ months}\right)$	2,00,000	
- Finished Goods $\left(\frac{₹33,60,000}{12 \text{ months}} \times 2 \text{ months}\right)$	5,60,000	
Receivables (Debtors) $\left(\frac{₹38,40,000}{12 \text{ months}} \times 3 \text{ months}\right)$	9,60,000	
Sales Promotion expenses paid in advance $\left(\frac{₹1,20,000}{12 \text{ months}} \times 1 \text{ month}\right)$	10,000	
Cash balance	1,00,000	18,30,000
Gross Working Capital		18,30,000

B. Current Liabilities:		
Payables:		
- Creditors for materials $\left(\frac{₹\,12,00,000}{12\,\text{months}} \times 2\ \text{months}\right)$	2,00,000	
Wages outstanding $\left(\frac{₹\,9,60,000}{12\,\text{months}} \times 1\ \text{month}\right)$	80,000	
Manufacturing expenses outstanding $\left(\frac{₹\,12,00,000}{12\,\text{months}} \times 1\ \text{month}\right)$	1,00,000	
Administrative expenses outstanding $\left(\frac{₹\,3,60,000}{12\,\text{months}} \times 1\ \text{month}\right)$	30,000	4,10,000
Net working capital (A - B)		14,20,000
Add: Safety margin @ 15%		2,13,000
Total Working Capital requirements		16,33,000

(b) (i) Calculation of market price per share

According to Miller – Modigliani (MM) Approach:

$$P_o = \frac{P_1 + D_1}{1 + K_e}$$

Where,

Existing market price (P_o) = ₹ 600

Expected dividend per share (D_1) = ₹ 40

Capitalization rate (k_e) = 0.20

Market price at year end (P_1) = ?

a. If expected dividends are declared, then

600=(P1+40)/(1+0.2)

600 x 1.2 = P1+40

P1 = 680

b. If expected dividends are not declared, then

600 = (P1+0)/(1 + 0.2)

600 x 1.2 = P1

P1= 720

(ii) Calculation of number of shares to be issued

	(a)	(b)
	Dividends are declared (₹ lakh)	**Dividends are not Declared (₹ lakh)**
Net income	1500	1500
Total dividends	(400)	-
Retained earnings	1100	1500
Investment budget	2000	2000
Amount to be raised by new issues	900	500
Relevant market price (₹ per share)	680	720
No. of new shares to be issued (in lakh) (₹ 900 ÷ 680; ₹ 500 ÷ 720)	1.3235	0.6944

(iii) Calculation of market value of the shares

	(a)	(b)
Particulars	**Dividends are declared**	**Dividends are not Declared**
Existing shares (in lakhs)	10.00	10.00
New shares (in lakhs)	1.3235	0.6944
Total shares (in lakhs)	11.3235	10.6944
Market price per share (₹)	680	720
Total market value of shares at the end of the year (₹ in lakh)	11.3235 × 680 = 7,700 (approx.)	10.6944 × 720 = 7,700 (approx.)

Hence, it is proved that the total market value of shares remains unchanged irrespective of whether dividends are declared, or not declared.

(c) Calculation of Cash Flow after Tax

	Year 1	Year 2	Year 3	Year 4	Year 5
Capacity	50%	65%	80%	100%	100%
Units	1,50,000	1,95,000	2,40,000	3,00,000	3,00,000
Contribution p.u.	360	360	360	360	360
(600 x 60%)					
Total Contribution	5,40,00,000	7,02,00,000	8,64,00,000	10,80,00,000	10,80,00,000
Less: Fixed Asset	2,00,00,000	3,50,00,000	5,00,00,000	5,00,00,000	5,00,00,000
Less: Depreciation (W.N.)	4,00,00,000	2,40,00,000	1,44,00,000	86,40,000	51,84,000

PBT	(60,00,000)	1,12,00,000	2,20,00,000	4,93,60,000	5,28,16,000
Less: Tax	(18,00,000)	33,60,000	66,00,000	1,48,08,000	1,58,44,800
PAT	(42,00,000)	78,40,000	1,54,00,000	3,45,52,000	3,69,71,200
Add: Depreciation	4,00,00,000	2,40,00,000	1,44,00,000	86,40,000	51,84,000
CFAT	3,58,00,000	3,18,40,000	2,98,00,000	4,31,92,000	4,21,55,200

Calculation of NPV

Year	Description	Cash Flow	PVF @12%	PV
0	Initial Investment	(10,00,00,000)	1	(10,00,00,000)
0	WC introduced	(1,50,00,000)	1	(1,50,00,000)
3	WC introduced	(2,00,00,000)	0.7118	(1,42,36,000)
1	CFAT	3,58,00,000	0.8929	3,19,65,820
2	CFAT	3,18,40,000	0.7972	2,53,82,848
3	CFAT	2,98,00,000	0.7118	2,12,11,640
4	CFAT	4,31,92,000	0.6355	2,74,48,516
5	CFAT	4,21,55,200	0.5674	2,39,18,860
5	WC released	3,50,00,000	0.5674	1,98,59,000
5	Scrap Sale	2,00,00,000	0.5674	1,13,48,000
	Net Present Value			**3,18,98,684**

Working Notes (W.N.)

Calculation of Depreciation

Year	Opening WDV	Depreciation	Closing WDV
1	10,00,00,000	4,00,00,000	6,00,00,000
2	6,00,00,000	2,40,00,000	3,60,00,000
3	3,60,00,000	1,44,00,000	2,16,00,000
4	2,16,00,000	86,40,000	1,29,60,000
5	1,29,60,000	51,84,000	77,76,000

2. (a) Income statement

Particulars		P	Q
		(₹)	(₹)
	Sales	50,00,000	48,00,000
(–)	Variable Cost	33,50,000	24,00,000
	Contribution	16,50,000	24,00,000
	Fixed Cost	8,25,000	16,00,000
	EBIT	8,25,000	8,00,000
(–)	Interest	5,50,000	6,00,000
	EBT	2,75,000	2,00,000

(–)	Tax	82,500	60,000
	EAT	1,92,500	1,40,000
(÷)	No. of Shares	1,00,000	70,000
	EPS	**₹ 1.93**	**₹ 2.00**

Working Note :

1. Financial Leverage	**=**	EBIT / EBT	**=**	EBIT / (EBIT – Int.)
Let the EBIT be X				
	P		**Q**	
	3 = X/(X – 5,50,000) 3(X – 5,50,000) = X 3X – 16,50,000 = X 2X = 16,50,000		4 = X/(X – 6,00,000) 4(X – 6,00,000) = X 4X – 24,00,000 = X 3X = 24,00,000	
	X = 8,25,000		**X = 8,00,000**	
2. Operating Leverage = Contribution/EBIT				
Let the Contribution be X				
	P		**Q**	
	2 = X/8,25,000 **X = 16,50,000**		3= X/8,00,000 **X = 24,00,000**	

3. Sales

Let the Sales be 100

Sales – Variable Cost = Contribution

		P		**Q**
Contribution	**=**	100 – 67	**=**	100 – 50
	=	33	**=**	50
Sales	**=**			
		P		**Q**
For 33		= 16,50,000	For 50	= 24,00,000
For 100		**= 50,00,000**	For 100	**= 48,00,000**

(b) Expected return on capital employed

Capital Employed = Debt + Equity

= (₹ 63,00,000 + ₹ 54,00,000) + (₹ 70,00,000 + ₹ 1,30,00,000)

= ₹ 3,17,00,000

Return on capital employed/ROI = $\left(\frac{\text{EBIT}}{\text{Capital employed}}\right)$ x 100

At present:

$= \left(\frac{54,00,000}{3,17,00,000} \right) \times 100$

= 17.03%

Now company expects 2% more as ROI

So, Expected ROI = 17.03% + 2%

= 19.03%

Proposed EBIT = Proposed Capital Employed x Return on capital employed

= (₹ 3,17,00,000 + ₹ 50,00,000) x 19.03% = ₹ 69,84,010

(i) Market Price per Share:

Particular	**Financial Options**	
	Option – I 12% term loan of ₹ 50,00,000	**Option II 1,00,000 equity shares @ ₹ 20 and 11% debentures of ₹ 30,00,000**
	(₹)	**(₹)**
EBIT	69,84,010	69,84,010
Less: Interest		
- 10% on old debentures	6,30,000	6,30,000
- 11% on new debentures	-	3,30,000
- 12% on old term loan	6,48,000	6,48,000
- 12% on new term loan	6,00,000	
Total Interest	18,78,000	16,08,000
EBT	51,06,010	53,76,010
Less Tax @ 30%	15,31,803	16,12,803
EAT	35,74,207	37,63,207
No. of equity shares	7,00,000	8,00,000
Earnings per share	**5.11**	**4.70**
P/E ratio	10	10
Market Price per Share = EPS x P/E ratio	**51.06**	**47.04**

(ii) Recommendation:

The option I is better and may be opted as both EPS and MPS are higher.

3. (a) Inventory Turnover = $\frac{\text{Inventory}}{\text{COGS}} \times 365 = \frac{38,60,000 \times 365}{76,40,000} = 184.41$ days = 185 days (apx)

Receivables Turnover = $\frac{\text{Receivables}}{\text{Sales}} \times 365 = \frac{39,97,000 \times 365}{1,25,00,000} = 116.71$ = 117 days (apx)

Equity to Reserves = 1

Reserves = 1 x 30,00,000 = 30,00,000

Projected profit = 30,00,000 - 18,00,000 = 12,00,000

Net Profit Margin = 15%

12,00,000/ Sales = 0.15

Sales = 80,00,000

Gross Profit = 80,00,000 x 50% = 40,00,000

COGS = 80,00,000 - 40,00,000 = 40,00,000

Projected Debtors Turnover = 100 days = $\frac{\text{Closing Receivables}}{\text{Sales}}$ x 365

$$100 = \frac{\text{Closing Receivables}}{80,00,000} \text{ x } 365$$

$$\text{Closing Receivables} = \frac{80,00,000 \text{ x } 100}{365} = 21,91,781$$

Projected Closing Inventory = 70% of opening inventory = 70% of 38,60,000 = 27,02,000

Projected Creditor Turnover= 100 days = $\frac{\text{Closing Creditors}}{\text{COGS}} \text{x} 365$

Closing Creditors = $\frac{\text{COGS}}{365} \text{x} 100$

Closing Creditor = $\frac{40,00,000}{365} \text{x} 100 = 10,95,890$

Equity Share Capital + Reserves = 30,00,000 + 30,00,000 = 60,00,000

Long Term Debt to Equity = 0.5

$\frac{\text{LTD}}{60,00,000} = 0.5$

Long Term Debt = 0.5 x 60,00,000

Long Term Debt = 30,00,000

(b) Financial Instruments in the International Market

Some of the various financial instruments dealt with in the international market are:

(a) Euro Bonds

(b) Foreign Bonds

(c) Fully Hedged Bonds

(d) Medium Term Notes

(e) Floating Rate Notes

(f) External Commercial Borrowings

(g) Foreign Currency Futures

(h) Foreign Currency Option

(i) Euro Commercial Papers.

4. (a) Inter-relationship between Investment, Financing and Dividend Decisions: The finance functions are divided into three major decisions, viz., investment, financing and dividend decisions. It is correct to say that these decisions are inter-related because the underlying objective of these three decisions is the same, i.e. maximisation of shareholders' wealth. Since investment, financing and dividend decisions are all interrelated, one has to consider the joint impact of these decisions on the market price of the company's shares and these decisions should also be solved jointly. The decision to invest in a new project needs the finance for the investment. The financing decision, in turn, is influenced by and influences dividend decision because retained earnings used in internal financing deprive shareholders of their dividends. An efficient financial management can ensure optimal joint decisions. This is possible by evaluating each decision in relation to its effect on the shareholders' wealth.

The above three decisions are briefly examined below in the light of their inter-relationship and to see how they can help in maximising the shareholders' wealth i.e. market price of the company's shares.

Investment decision*:* The investment of long term funds is made after a careful assessment of the various projects through capital budgeting and uncertainty analysis. However, only that investment proposal is to be accepted which is expected to yield at least so much return as is adequate to meet its cost of financing. This have an influence on the profitability of the company and ultimately on its wealth.

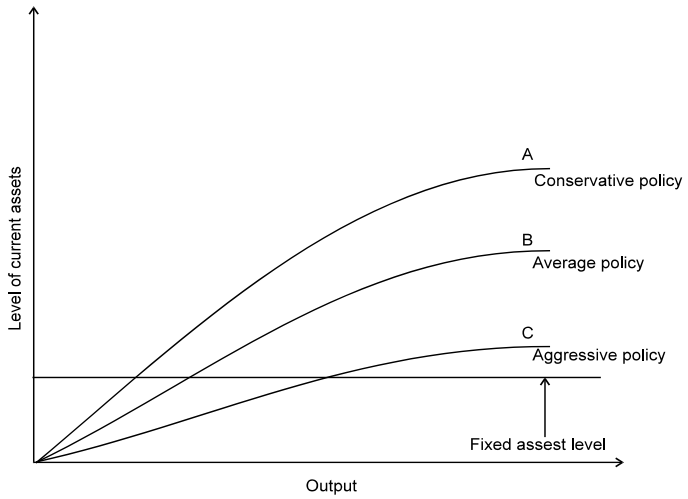
Financing decision*:* Funds can be raised from various sources. Each source of funds involves different issues. The finance manager has to maintain a proper balance between long-term and short-term funds. With the total volume of long-term funds, he has to ensure a proper mix of loan funds and owner's funds. The optimum financing mix will increase return to equity shareholders and thus maximise their wealth.

***Dividend decision**:* The finance manager is also concerned with the decision to pay or declare dividend. He assists the top management in deciding as to what portion of the profit should be paid to the shareholders by way of dividends and what portion should be retained in the business. An optimal dividend pay-out ratio maximises shareholders' wealth.

The above discussion makes it clear that investment, financing and dividend decisions are interrelated and are to be taken jointly keeping in view their joint effect on the shareholders' wealth.

(b) Liquidity versus Profitability Issue in Management of Working Capital

Working capital management entails the control and monitoring of all components of working capital i.e. cash, marketable securities, debtors, creditors etc. Finance manager has to pay particular attention to the levels of current assets and their financing. To decide the level of financing of current assets, the risk return trade off must be taken into account. The level of current assets can be measured by creating a relationship between current assets and fixed assets. A firm may follow a conservative, aggressive or moderate policy.



A conservative policy means lower return and risk while an aggressive policy produces higher return and risk. The two important aims of the working capital management are profitability and solvency. A liquid firm has less risk of insolvency i.e. it will hardly experience a cash shortage or a stock out situation. However, there is a cost associated with maintaining a sound liquidity position. So, to have a higher profitability the firm may have to sacrifice solvency and maintain a relatively low level of current assets.

(c) Concept of Discounted Payback Period

Payback period is time taken to recover the original investment from project cash flows. It is also termed as break even period. The focus of the analysis is on liquidity aspect and it suffers from the limitation of ignoring time value of money and profitability. Discounted payback

period considers present value of cash flows, discounted at company's cost of capital to estimate breakeven period i.e. it is that period in which future discounted cash flows equal the initial outflow. The shorter the period, better it is. It also ignores post discounted payback period cash flows.

OR

(c) Concept of Indian Depository Receipts: The concept of the depository receipt mechanism which is used to raise funds in foreign currency has been applied in the Indian capital market through the issue of Indian Depository Receipts (IDRs). Foreign companies can issue IDRs to raise funds from Indian market on the same lines as an Indian company uses ADRs/GDRs to raise foreign capital. The IDRs are listed and traded in India in the same way as other Indian securities are traded.

ANSWERS OF MODEL TEST PAPER 2

PAPER 6B: STRATEGIC MANAGEMENT

PART I - Case Scenario based MCQs

1. (A) (i) (b) (ii) (c) (iii) (b) (iv) (b) (v) (b)

(B) (i) (c) (ii) (b) (iii) (b)

PART II - Descriptive Questions

1. (a) The retail chain is employing a strategy that combines both proactive and reactive elements. Monitoring consumer trends and adjusting product offerings accordingly demonstrates a proactive approach to anticipate and meet customer needs. On the other hand, maintaining a flexible supply chain to respond quickly to changes in demand reflects a reactive strategy to address unforeseen shifts in the market.

This combination allows the retail chain to both anticipate future trends and react effectively to immediate market changes, making its strategy partly proactive and partly reactive. This dual strategy of proactive trend monitoring and reactive supply chain flexibility enables the retail chain to anticipate market shifts and adapt to them effectively, ensuring its competitiveness and customer satisfaction.

(b) PQR Ltd. has planned to implement the Strategic Business Unit (SBU) structure. Very large organisations, particularly those running into several products, or operating at distant geographical locations that are extremely diverse in terms of environmental factors, can be better managed by creating strategic business units. SBU structure becomes imperative in an organisation with increase in number, size and diversity.

The attributes of an SBU and the benefits a firm may derive by using the SBU Structure are as follows:

- A scientific method of grouping the businesses of a multi – business corporation which helps the firm in strategic planning.
- An improvement over the territorial grouping of businesses and strategic planning based on territorial units.
- Strategic planning for SBU is distinct from rest of businesses. Products/ businesses within an SBU receive same strategic planning treatment and priorities.
- Each SBU will have its own distinct set of competitors and its own distinct strategy.
- The CEO of SBU will be responsible for strategic planning for SBU and its profit performance.

- Products/businesses that are related from the standpoint of function are assembled together as a distinct SBU.
- Unrelated products/ businesses in any group are separated into separate SBUs.
- Grouping the businesses on SBU lines helps in strategic planning by removing the vagueness and confusion.
- Each SBU is a separate business and will be distinct from one another on the basis of mission, objectives etc.

(c) Competition from new sustainable fashion brands falls under the "Threat of New Entrants" category of Porter's Five Forces Model for Competitive Analysis. These new entrants pose a threat to existing sustainable clothing retailers like *GreenThrift Inc.* by increasing competition and potentially eroding market share. The emergence of these brands, focusing on using organic and recycled materials along with ethical manufacturing practices, aligns with the values of environmentally conscious consumers, making them strong competitors in the sustainable fashion market.

2. (a) Each organization has to build its competitive advantage over the competitors in the business warfare in order to win. This can be done only by following the process of strategic management. Strategic Management is very important for the survival and growth of business organizations in dynamic business environments. Other major benefits of strategic management are as follows:

- Strategic management helps organizations to be more proactive rather than reactive in dealing with its future. It facilitates to work within vagaries of environment and remains adaptable with the turbulence or uncertain future. Therefore, they are able to control their own destiny in a better way.
- It provides better guidance to entire organization on the crucial point – what it is trying to do. Also provides frameworks for all major business decisions of an enterprise such as on businesses, products, markets, organizational structures, etc.
- It facilitates to prepare the organization to face the future and act as pathfinder to various business opportunities. Organizations are able to identify the available opportunities and identify ways and means as how to reach them.
- It serves as a corporate defence mechanism against mistakes and pitfalls. It helps organizations to avoid costly mistakes in product market choices or investments.

- ♦ Over a period of time strategic management helps organization to evolve certain core competencies and competitive advantages that assist in the fight for survival and growth.

(b) To maintain a competitive edge in the face of increased competition, *Reshuffle Corp* can differentiate its products in several ways:

- **Tangible and Intangible Aspects:** *Reshuffle Corp* can focus on the tangible aspects of its products, such as using high-quality materials and innovative designs to create furniture that is both functional and aesthetically pleasing. Additionally, they can emphasize the intangible aspects of their products, such as excellent customer service and a strong brand reputation for reliability and durability.
- **Pricing Strategies:** While market prices are often dictated by competition, *Reshuffle Corp* can work on cost optimization to maintain profitability. They can also consider offering value-added services, such as free installation or extended warranties, to justify a higher price point.
- **Product Features:** By continually optimizing their product features based on customer feedback and market trends, *Reshuffle Corp* can ensure that their products deliver maximum satisfaction to their target customers. This may include features that enhance functionality, design, quality, and overall user experience.
- **Product Centric Approach:** *Reshuffle Corp* should keep their products at the center of their strategic activities, ensuring that all business processes, from production to sales and marketing, are aligned to meet customer needs and expectations.
- **Product Life Cycle Management:** *Reshuffle Corp* should be aware of the life cycle of their products and plan for reinvention or replacement accordingly. They can introduce new product lines or upgrade existing ones to keep up with changing customer preferences and market trends.

3. (a) SWOT Analysis for *EasyLife Corporation's* New Smart Home Devices Venture:

Strengths	**Weaknesses**
• Strong brand reputation in consumer electronics. • Established distribution network. • Access to technological expertise for product development.	• Limited experience in the smart home devices market. • May require additional investments in research and development.

• Financial resources to support product launch and marketing.	• Potential challenges in integrating a new product line with existing offerings. • Lack of established customer base for smart home devices.
Opportunities • Growing market for smart home devices due to increasing consumer interest in home automation. • Possibility of partnering with existing smart home platform providers. • Potential to leverage brand loyalty from existing customers. • Ability to differentiate through innovative features and design.	**Threats** • Intense competition from established players in the smart home devices market. • Rapid technological advancements lead to short product life cycles. • Potential for cybersecurity threats in connected devices. • Economic factors impacting consumer spending on discretionary items.

The SWOT analysis highlights that while *EasyLife Corporation* has several strengths that can support the launch of a new smart home devices line, there are also significant weaknesses and threats to consider. To maximize the chances of success, *EasyLife Corporation* should focus on leveraging its brand reputation and distribution network while carefully addressing the weaknesses and threats identified. Additionally, staying informed about technological developments and consumer trends will be essential for maintaining competitiveness in the dynamic smart home devices market.

(b) The concept of forward and backward linkages between strategy formulation and implementation in strategic management highlights the interconnected nature of these two phases and their impact on the overall strategic decision-making process of an organization.

Forward Linkages: Forward linkages refer to the impact of strategy formulation on strategy implementation. When an organization formulates a new strategy or revises an existing one, it sets the direction for the organization's future actions. For example, if a company decides to expand its product line to target a new market segment, this decision will require changes in the organization's structure, resources allocation, and possibly its leadership style. These changes are necessary to align the organization's operations with the new strategic direction. Thus, the formulation of strategies has forward linkages with their implementation, as it sets the stage for how the strategy will be executed.

Backward Linkages: Backward linkages, on the other hand, refer to the impact of implementation on strategy formulation. As an organization implements its strategies, it gains valuable insights and feedback from the implementation process. This feedback can influence future strategic decisions. For example, if a company faces unexpected challenges or discovers new opportunities during the implementation of a strategy, it may need to reevaluate its strategic choices. Similarly, past strategic actions and their outcomes can also influence the formulation of future strategies. Over time, these incremental changes in strategy and implementation take the organization from its current state to where it aims to be, reflecting the dynamic nature of strategic management.

In conclusion, the forward and backward linkages between strategy formulation and implementation highlight the iterative and interconnected nature of strategic management. By understanding and leveraging these linkages, organizations can enhance their strategic decision-making process and improve their overall performance.

4. (a) Strategic Performance Measures (SPM) are metrics used by organizations to evaluate and track the effectiveness of their strategies in achieving strategic goals and objectives. SPM provides a framework for measuring the performance of key areas critical to the success of the organization's strategy. These measures help in assessing whether the organization is progressing towards its desired outcomes and allow for adjustments to be made to improve performance.

Types of Strategic Performance Measures

There are various types of strategic performance measures, including:

- **Financial Measures**: Financial measures, such as revenue growth, return on investment (ROI), and profit margins, provide an understanding of the organization's financial performance and its ability to generate profit.
- **Customer Satisfaction Measures**: Customer measures, such as customer satisfaction, customer retention, and customer loyalty, provide insight into the organization's ability to meet customer needs and provide high-quality products and services.
- **Market Measures**: Market measures, such as market share, customer acquisition, and customer referrals, provide information about the organization's competitiveness in the marketplace and its ability to attract and retain customers.
- **Employee Measures**: Employee measures, such as employee satisfaction, turnover rate, and employee engagement, provide insight into the organization's ability to attract and retain talented employees and create a positive work environment.

- ♦ **Innovation Measures:** Innovation measures, such as research and development (R&D) spending, patent applications, and new product launches, provide insight into the organization's ability to innovate and create new products and services that meet customer needs.
- ♦ **Environmental Measures:** Environmental measures, such as energy consumption, waste reduction, and carbon emissions, provide insight into the organization's impact on the environment and its efforts to operate in a sustainable manner.

(b) The strategy adopted by *StarTech Solutions* is Focused differentiation. This strategy involves targeting a specific segment of the market with unique products or services that are perceived as valuable by customers in that segment. By specializing in serving unique, high-end clients, *StarTech* is able to differentiate itself from competitors and create a competitive advantage.

Advantages of Focused Differentiation:

- **Strong Customer Loyalty:** By catering to a specific niche market, *StarTech* can build strong relationships with its customers, leading to higher customer loyalty and retention.
- **Higher Profit Margins:** Serving a niche market allows *StarTech* to command higher prices for its specialized products or services, leading to higher profit margins.
- **Reduced Competition:** By focusing on a niche market that other firms are not targeting, *StarTech* faces less competition, allowing it to establish itself as a leader in that segment.
- **Better Resource Allocation:** Focusing on a specific market segment allows *StarTech* to allocate its resources more efficiently, concentrating on areas that will provide the greatest return on investment.

Disadvantages of Focused Differentiation:

- **Limited Market Size:** The niche market that StarTech is targeting may be limited in size, restricting the company's potential for growth.
- **Risk of Market Changes:** Changes in the market or customer preferences could impact on the demand for *StarTech's* specialized products or services, leading to potential revenue loss.
- **Higher Costs:** Serving a niche market may require specialized resources and expertise, leading to higher costs of operation.
- **Imitation by Competitors:** If *StarTech's* success in the niche market attracts competitors, they may attempt to imitate its strategy, eroding its competitive advantage.

Overall, the focused differentiation strategy adopted by *StarTech Solutions* has allowed it to differentiate itself in a competitive industry and build a strong position in the market. However, the company must be aware of the potential challenges and risks associated with this strategy and continue to innovate and adapt to maintain its competitive edge.

OR

Strategic alliances are formed if they provide an advantage to all the parties in the alliance. These advantages can be broadly categorised as follows:

(i) **Organizational:** Strategic alliances may be formed to learn necessary skills and obtain certain capabilities from the strategic partner. Strategic partners may also help to enhance productive capacity, provide a distribution system, or extend supply chain. A strategic partner may provide a good or service that complements each other, thereby creating a synergy. If one partner is relatively new or untried in a certain industry, having a strategic partner who is well-known and respected will help add legitimacy and creditability to the venture.

(ii) **Economic:** Alliances can reduce costs and risks by distributing them across the members of the alliance. Partners can obtain greater economies of scale in an alliance, as production volume increase, causing the cost per unit to decline. Finally, partners can take advantage of co-specialization, where specializations are bundled together, creating additional value.

(iii) **Strategic:** Organizations may join to cooperate instead of compete. Alliances may also create vertical integration where partners are part of supply chain. Strategic alliances may also be useful to create a competitive advantage by the pooling of resources and skills. This may also help with future business opportunities and the development of new products and technologies. Strategic alliances may also be used to get access to new technologies or to pursue joint research and development.

(iv) **Political:** Sometimes there is need to form a strategic alliance with a local foreign business to gain entry into a foreign market either because of local prejudices or legal barriers to entry. Forming strategic alliances with politically-influential partners may also help improve overall influence and position.