Business Management Pillar

Strategic Level Paper

P6 – Management Accounting – Business Strategy

20 May 2008 - Tuesday Morning Session

Instructions to candidates

You are allowed three hours to answer this question paper.
You are allowed 20 minutes reading time **before the examination begins** during which you should read the question paper and, if you wish, highlight and/or make notes on the question paper. However, you will **not** be allowed, **under any circumstances,** to open the answer book and start writing or use your calculator during this reading time.
You are strongly advised to carefully read ALL the question requirements before attempting the question concerned (that is, all parts and/or sub-questions). The question requirements are contained in a dotted box.
ALL answers must be written in the answer book. Answers or notes written on the question paper will **not** be marked.
Answer the ONE compulsory question in Section A on pages 2, 3 and 5. The question requirements are on page 5, which is detachable for ease of reference.
Answer TWO of the four questions in Section B on pages 8 to 12.
Maths Tables and Formulae are provided on pages 13 and 14. These pages are detachable for ease of reference.
The list of verbs as published in the syllabus is given for reference on the inside back cover of this question paper.
Write your candidate number, the paper number and examination subject title in the spaces provided on the front of the answer book. Also write your contact ID and name in the space provided in the right hand margin and seal to close.
Tick the appropriate boxes on the front of the answer book to indicate which questions you have answered.

P6 – Business Strategy

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SECTION A – 50 MARKS

[the indicative time for answering this section is 90 minutes]

ANSWER THIS QUESTION

Question One

Introduction

AAA is a small manufacturer of replacement machine components for machinery used in the mining and oil exploration industries. It is based in an African country. It was formed in 1952, as a partnership between two engineers, and incorporated in 1977. AAA now employs 120 staff, and has an annual turnover equivalent to one million US dollars. AAA is proud to offer the very highest levels of customer service. Much of the machinery used by AAA's customers is quite old and, as a result, components are no longer available from the original equipment manufacturers (OEMs), most of which are large multinational companies. AAA mostly supplies parts directly to the end-users but also receives a small but significant proportion of its business from OEMs, who then supply the components to their customers.

The current business model

AAA has always run its business in a very traditional way. The sales manager receives most orders by telephone or fax. The order specifies the OEM part number that the component is to replace. If AAA has previously supplied that component, the sales manager checks the price list and tells the customer the price. AAA holds very low levels of finished goods inventory, and then only of the most commonly ordered components.

Where AAA needs to make a component for the first time, an AAA 'estimator' (a qualified engineer, responsible for producing an estimate of the material and labour involved in manufacturing the item) obtains the original drawings of the component, either from AAA's extensive archives or from the OEM. The estimator then produces detailed engineering drawings, a list of materials and parts required, and an estimate of the labour hours likely to be used at each stage of the manufacturing process. The estimate is passed to a costing clerk in the accounts department who calculates the likely product cost (labour, materials and overheads), adds a 'mark-up' of 50%, and advises the sales manager of the price. If the customer accepts the price, an order is passed to the production department, which schedules and completes the work. If the actual cost of production is significantly different from that estimated, the price list is amended to reflect the actual manufacturing cost.

Very occasionally, a customer sends (or brings in) an old component, which cannot be traced back to an OEM. The sales manager gives the component to an estimator, who dismantles the component and produces the necessary engineering drawings and estimate. This process is called 'reverse engineering', and is common in the component manufacturing industry. Reverse engineering currently accounts for about 5% of AAA's business.

When an order is fulfilled, the component is delivered to the customer, together with an invoice. Most customers pay within 30 days, by cash or cheque. AAA does not have a problem with bad debts. An increasing proportion of AAA's business is now transacted in US dollars, as African currencies tend to be unstable.

AAA prides itself on the personal service it provides. The close contact it has with its customers means that AAA receives a significant amount of repeat business. AAA has never advertised its services, but grew significantly until 2005 as a result of 'word of mouth' recommendations by satisfied customers. AAA, however, has not experienced growth for the last two years, although turnover and profit have remained stable.

AAA uses only very basic Information Systems (IS), and reports its performance using a simple comparison between budget and actual, which is produced using a spreadsheet package. AAA's accounting system is not automated, and transactions are recorded in traditional ledgers.

Project E: Computerised accounting and e-commerce systems

The sales manager of AAA has noticed that customers are increasingly mentioning that they would like to be able to order online. He knows that there has been a significant growth in business-to-business (B2B) e-commerce in recent years. The sales manager has recognised that in order to grow and to make a move into e-commerce possible, AAA's accounting system will have to be updated to a computerised one.

Having spoken to a number of potential suppliers, the sales manager has now received a proposal from SSS, a local company, to supply tailored 'off-the-shelf' systems for both accounting and e-commerce. SSS has provided a detailed breakdown of its proposal, to be known as Project E, which is summarised below.

The sales manager believes that, following implementation of the new systems (likely to be 12 months from contract agreement) e-commerce should lead to an increase in the company's turnover of 10% in its first year of operation. Thereafter, the turnover resulting from e-commerce should grow at a rate of 10% each year for the foreseeable future.

The sales manager also thinks that any increase in indirect costs as a result of this higher volume of business will be fully offset by a reduction in administration workload as a result of the new computerised accounting system. The gross margin earned from e-commerce business can therefore be used as the effective cash inflow for evaluation purposes. The current turnover of AAA is, as stated earlier, $1 million a year. The mark-up on products sold by e-commerce will be the same as at present (that is, 50%).

However, the sales manager thinks that a cautious approach should be taken to the evaluation of the proposal, and that any benefits after 5 years from implementation should be ignored. AAA has a weighted average cost of capital (WACC) of 15%.

The following information has been provided by SSS, the preferred systems supplier:

Project E

Item	**Timing**	**Cost US$**
"Mage Gold" accounting package	On agreement of contract	14,000
Tailoring of the above	During the first 6 months	20,000
"SellitOnline" e-commerce package	On agreement of contract	11,000
Tailoring of the above	During the first 6 months	8,000
Populating the e-commerce database	During the first 6 months	5,000
Training	During months 7 – 12	10,000
Support	Split over the five years following implementation	25,000
Hardware, networking and connection	During the first 12 months	40,000
Broadband service costs	Split over the five years following implementation	20,000
TOTAL COST		153,000

Note: You should assume that all cashflows arise at the end of the period to which they relate, for example 'Tailoring' at the end of 6 months, and 'Training' at the end of 12 months.

The requirement for this question is on page 5 which is detachable for ease of reference

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Required:

(a) Briefly explain how e-commerce has impacted on the way business is conducted.

(5 marks)

(b) Briefly discuss how a new Information Systems (IS) strategy might impact upon corporate, business and functional strategies.

(8 marks)

(c) Prepare a financial evaluation of Project E.

Note: You should ignore the effects of inflation and taxation.

(12 marks)

(d) Evaluate the strategic and competitive benefits to AAA of the proposed e-commerce system.

(15 marks)

(e) Advise AAA, based on your answers to parts *(a)* to *(d)* above, whether or not to invest in the proposed e-commerce and accounting project.

Note: You are not required to reproduce the detail of your arguments from earlier parts of this question.

(4 marks)

(f) Discuss how AAA might use its e-commerce system to increase the volume of business from 'reverse engineering' projects.

(6 marks)

(Total for Question One = 50 marks)

(Total for Section A = 50 marks)

End of Section A

Section B starts on page 8

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SECTION B – 50 MARKS

[the indicative time for answering this section is 90 minutes]

ANSWER *TWO* QUESTIONS FROM FOUR

Question Two

CCC is an established company in public ownership comprising the following divisions; construction and building, engineering and machinery, real estate. Although the company has traded profitably, its earnings have been subject to wide variations and some of the shareholders are concerned about the Board's policy of 'conglomerate diversification'

In the last year the company had the following earnings figures;

Division	**Earnings $ million**
Construction and building	50
Engineering and machinery	20
Real estate	30
Group	100

Note: It should be assumed that the above divisional earnings are stated after tax.

Industry	**Current average market sector PE**
Construction and building	8
Engineering and machinery	13
Real Estate	23

CCC is currently valued on the stock market at $1,000 million, and proposed / current dividends are approximately half analysts' expectations.

Construction and building
This activity represents the original business before CCC started to make acquisitions. The divisional management has described the business as 'mature, stable, offering the prospect of modest but sustained growth'.

Engineering and machinery
This activity represents the first acquisitions made by CCC whereby a number of small companies were bought and consolidated into one division. The divisional management has described the business as 'mature but offering the prospect of profit growth of 10% per annum'. Additionally the division has a broad customer base servicing a number of government agencies – minimising the risk of cash flow problems.

Real estate
This division represents the most recent acquisition made by CCC and has provided profit growth of over 20% per annum in the three years since it was formed. The divisional management, which is recognised as the most dynamic management team within CCC, feels that this rate of growth can be continued or surpassed.

HQ Organisation
Each division has its own headquarters office in a different town and the group headquarters, which has the responsibility for raising capital and operating a group treasury function is also separately located. The group headquarters is located in the capital, is quite luxurious and has a staff of 50 including the main board directors. Group headquarters, and the staff, is funded by a management charge on the divisions.

The remainder of this question and the requirement are on the page opposite

Investors
An informal group of institutional shareholders, which holds approximately 20% of CCC's equity has requested a review of the Board's strategy and a rationalisation of the company's portfolio. These shareholders feel that the Board of Directors has destroyed value and that the company should take the opportunity to dispose of the real estate division, reduce costs by closing the group headquarters and relocate the board and treasury functions to one of the divisional headquarters. This, they have said, would allow the company to pay a large, one off, dividend to reward shareholders for their tolerance of poor past performance.

The Board of Directors feels that the suggestions are unreasonable and that its strategy has served the best interests of all shareholders.

Required:

(a) Explain the term 'conglomerate diversification'.

(3 marks)

(b) *(i)* Evaluate the comments made by the institutional investors that the Board 'has destroyed value'.

(3 marks)

(ii) Evaluate the suggestions made by the institutional investors that

> "the company should take the opportunity to dispose of the real estate division, reduce costs by closing the group headquarters and relocate the board and treasury functions to one of the divisional headquarters".

(7 marks)

(c) Identify and evaluate alternative methods available to the Board for the disposal of the real estate division, should it decide to do so, and recommend the method of disposal most appropriate to CCC.

(12 marks)

(Total for Question Two = 25 marks)

Section B continues over the page

Question Three

Based in a European country, BBB is a charity which raises funds to provide portable equipment to remove the poison arsenic from drinking water in villages, in less developed countries. Run by a Board of Trustees, the organisation operates on laissez faire management principles. There are few full-time paid employees and BBB is heavily dependent upon the work of volunteers. Although these volunteers are dedicated, many have said that they do not feel the organisation knows where it is going and have said that they are not confident about the future of BBB.

Funding comes from appeals to the general population, which are made through newspaper advertisements. BBB does not use the Internet to promote or raise donations and, generally, does not use available technology to any extent in its organisation. Additionally, BBB receives corporate donations, most of which come from old school friends of the trustees. There is no government funding.

Recently BBB has had difficulty in attracting donations and is at risk of not being able to carry on its work. The charity industry has become more competitive and many other organisations within it have become more aggressive in their marketing and promotion.

None of the Board of Trustees has a commercial background. The Chairman of Trustees has recently been to a number of conferences where the value of foresight and the need to conduct a frequent and thorough 'environmental analysis' have been discussed.

The Chairman has accepted that there is a serious gap in the knowledge that the trustees have about the environment in which BBB operates. Recognising that BBB needs a more proactive approach to the environment in which it operates, your help as a management accountant has been sought.

Required:

(a) Discuss how conducting a frequent and thorough environmental analysis would help the Board of Trustees of BBB.

(14 marks)

(b) Explain the concept of foresight and two techniques for the development of foresight.

(5 marks)

(c) Discuss the difficulties that BBB might, as an organisation, experience in developing a process of environmental analysis.

(6 marks)

(Total for Question Three = 25 marks)

Section B continues on the page opposite

Question Four

DDD is a biotechnology company which develops drugs. It was founded seven years ago by three scientists when they left the university medical school, where they had been senior researchers. The Company employs 10 other scientists who joined from different universities. All of these employees are receiving relatively low salaries but participate in a share option scheme. This means that when DDD is successfully floated on the stock exchange they will receive shares in the company.

DDD currently has a number of new, innovative drugs in development, but the earliest any of these drugs might come to market is two years from now. It is expected that there would be one successful drug launched in most years after that for at least six years. However, successful drug launches are never guaranteed, due to the speculative nature of biotechnology and the long period of clinical trials through which any new drug must pass. DDD has to invest a significant amount of resources into the development of each potential drug, whether they are successfully launched or not. Currently, it has 12 drugs in development, a number of which may not be successfully launched. Due to the speculative nature of the industry, companies such as DDD are unable to obtain bank loans on commercial terms.

DDD is funded by an exclusive arrangement with a venture capital company. However, there is only sufficient cash in place to maintain the present level of activity for a further nine months. The venture capital company owns 15% of the equity of the company. The rest is owned by the three founders. It has always been the intention of the venture capital company and the founders that, once the company has a sufficient number of drugs in production and on the market, the company would be floated on the stock exchange. This is expected to happen in five years' time.

Recently there have been a number of approaches to DDD which might solve its cash flow problems. The three founders have identified the following options:

1. The venture capital company has suggested that it will guarantee the cash flow until the first drug is successfully launched in commercial quantities. However, it would expect its equity holding to rise to 60% once this offer is accepted.
2. A large pharmaceutical company has offered to buy DDD outright and retain the services of the three founders (in research roles) and a few of the staff.
3. Another biotechnology company has offered to enter into a merger with DDD. This company has also been established for seven years and has one drug which will be launched in six months. However, of the four other potential drugs it has in development, none are likely to be commercially viable for 5 years. This company would expect the three founders to stay with the newly merged company but feels a rationalisation of the combined staff would be needed.

As the financial advisor to the three founders you have been asked to comment on the approaches that have been made.

Required:

(a) Describe the 'Suitability, Feasibility and Acceptability (SFA) framework as used for evaluating strategic options.

(6 marks)

(b) Using the SFA framework, evaluate the strategic options identified by the founders.

(12 marks)

(c) Identify and evaluate one other strategic option that the founders might pursue.

(5 marks)

(d) Recommend the most appropriate strategic option based on your analysis above.

(2 marks)

(Total for Question Four = 25 marks)

Section B continues over the page

Question Five

EEE is a divisionalised company, based in F, where it is quoted on the stock exchange. EEE manufactures and sells small electrical equipment products. As a country, F is more highly developed than the neighbouring countries. EEE has enjoyed a strong home market and has exported to the neighbouring countries.

EEE has had a reputation for producing high quality products. Recently, it has come under increasing competitive pressure from new, privately held, companies based in the neighbouring countries.

It appears that competitors based in these neighbouring countries have been selling lower quality products than EEE and have been undercutting it quite significantly in terms of price. Sales in both EEE's home and export markets have been badly affected by the actions of these competitors in the neighbouring countries.

EEE has looked at a number of possible solutions to this situation and has decided to acquire a manufacturing company in one of the neighbouring countries and move all of its production there, completely closing the manufacturing division in F. This would mean that EEE would purchase one of the companies that has recently become a competitor. EEE would maintain its present divisionalised structure within its home country F and treat the acquired company as a new division.

The Board of Directors recognises the need to carefully select a suitable acquisition target company. The Board also recognises that careful consideration will need to be given to the most suitable approach to performance management once the acquisition has been made. The Board is considering an approach based on either Return On Investment (ROI) or Residual Income (RI).

Required

(a) Advise the Board on what information would be required to assess the suitability of an acquisition target.

(15 marks)

(b) *(i)* Discuss the difficulties that EEE may experience with the performance measurement of its divisions, post acquisition.

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(6 marks)

(ii) Discuss the disadvantages that EEE may experience if it chooses to use ROI as its primary performance measure.

(4 marks)

(Total for Question Five = 25 marks)

(Total for Section B = 50 marks)

End of Question Paper

Maths Tables and Formulae follow on pages 13 and 14 which are detachable

Present value table

Present value of $1, that is $(1 + r)^{-n}$ where r = interest rate; n = number of periods until payment or receipt.

Periods (n)	Interest rates (r)									
	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909
2	0.980	0.961	0.943	0.925	0.907	0.890	0.873	0.857	0.842	0.826
3	0.971	0.942	0.915	0.889	0.864	0.840	0.816	0.794	0.772	0.751
4	0.961	0.924	0.888	0.855	0.823	0.792	0.763	0.735	0.708	0.683
5	0.951	0.906	0.863	0.822	0.784	0.747	0.713	0.681	0.650	0.621
6	0.942	0.888	0.837	0.790	0.746	0705	0.666	0.630	0.596	0.564
7	0.933	0.871	0.813	0.760	0.711	0.665	0.623	0.583	0.547	0.513
8	0.923	0.853	0.789	0.731	0.677	0.627	0.582	0.540	0.502	0.467
9	0.914	0.837	0.766	0.703	0.645	0.592	0.544	0.500	0.460	0.424
10	0.905	0.820	0.744	0.676	0.614	0.558	0.508	0.463	0.422	0.386
11	0.896	0.804	0.722	0.650	0.585	0.527	0.475	0.429	0.388	0.350
12	0.887	0.788	0.701	0.625	0.557	0.497	0.444	0.397	0.356	0.319
13	0.879	0.773	0.681	0.601	0.530	0.469	0.415	0.368	0.326	0.290
14	0.870	0.758	0.661	0.577	0.505	0.442	0.388	0.340	0.299	0.263
15	0.861	0.743	0.642	0.555	0.481	0.417	0.362	0.315	0.275	0.239
16	0.853	0.728	0.623	0.534	0.458	0.394	0.339	0.292	0.252	0.218
17	0.844	0.714	0.605	0.513	0.436	0.371	0.317	0.270	0.231	0.198
18	0.836	0.700	0.587	0.494	0.416	0.350	0.296	0.250	0.212	0.180
19	0.828	0.686	0.570	0.475	0.396	0.331	0.277	0.232	0.194	0.164
20	0.820	0.673	0.554	0.456	0.377	0.312	0.258	0.215	0.178	0.149

Periods *(n)*	Interest rates (r)									
	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833
2	0.812	0.797	0.783	0.769	0.756	0.743	0.731	0.718	0.706	0.694
3	0.731	0.712	0.693	0.675	0.658	0.641	0.624	0.609	0.593	0.579
4	0.659	0.636	0.613	0.592	0.572	0.552	0.534	0.516	0.499	0.482
5	0.593	0.567	0.543	0.519	0.497	0.476	0.456	0.437	0.419	0.402
6	0.535	0.507	0.480	0.456	0.432	0.410	0.390	0.370	0.352	0.335
7	0.482	0.452	0.425	0.400	0.376	0.354	0.333	0.314	0.296	0.279
8	0.434	0.404	0.376	0.351	0.327	0.305	0.285	0.266	0.249	0.233
9	0.391	0.361	0.333	0.308	0.284	0.263	0.243	0.225	0.209	0.194
10	0.352	0.322	0.295	0.270	0.247	0.227	0.208	0.191	0.176	0.162
11	0.317	0.287	0.261	0.237	0.215	0.195	0.178	0.162	0.148	0.135
12	0.286	0.257	0.231	0.208	0.187	0.168	0.152	0.137	0.124	0.112
13	0.258	0.229	0.204	0.182	0.163	0.145	0.130	0.116	0.104	0.093
14	0.232	0.205	0.181	0.160	0.141	0.125	0.111	0.099	0.088	0.078
15	0.209	0.183	0.160	0.140	0.123	0.108	0.095	0.084	0.079	0.065
16	0.188	0.163	0.141	0.123	0.107	0.093	0.081	0.071	0.062	0.054
17	0.170	0.146	0.125	0.108	0.093	0.080	0.069	0.060	0.052	0.045
18	0.153	0.130	0.111	0.095	0.081	0.069	0.059	0.051	0.044	0.038
19	0.138	0.116	0.098	0.083	0.070	0.060	0.051	0.043	0.037	0.031
20	0.124	0.104	0.087	0.073	0.061	0.051	0.043	0.037	0.031	0.026

Cumulative present value of $1 per annum, Receivable or Payable at the end of each year for *n* years

$$\frac{1-(1+r)^{-n}}{r}$$

Periods	Interest rates (*r*)									
(n)	1%	2%	3%	4%	5%	6%	7%	8%	9%	10%
1	0.990	0.980	0.971	0.962	0.952	0.943	0.935	0.926	0.917	0.909
2	1.970	1.942	1.913	1.886	1.859	1.833	1.808	1.783	1.759	1.736
3	2.941	2.884	2.829	2.775	2.723	2.673	2.624	2.577	2.531	2.487
4	3.902	3.808	3.717	3.630	3.546	3.465	3.387	3.312	3.240	3.170
5	4.853	4.713	4.580	4.452	4.329	4.212	4.100	3.993	3.890	3.791
6	5.795	5.601	5.417	5.242	5.076	4.917	4.767	4.623	4.486	4.355
7	6.728	6.472	6.230	6.002	5.786	5.582	5.389	5.206	5.033	4.868
8	7.652	7.325	7.020	6.733	6.463	6.210	5.971	5.747	5.535	5.335
9	8.566	8.162	7.786	7.435	7.108	6.802	6.515	6.247	5.995	5.759
10	9.471	8.983	8.530	8.111	7.722	7.360	7.024	6.710	6.418	6.145
11	10.368	9.787	9.253	8.760	8.306	7.887	7.499	7.139	6.805	6.495
12	11.255	10.575	9.954	9.385	8.863	8.384	7.943	7.536	7.161	6.814
13	12.134	11.348	10.635	9.986	9.394	8.853	8.358	7.904	7.487	7.103
14	13.004	12.106	11.296	10.563	9.899	9.295	8.745	8.244	7.786	7.367
15	13.865	12.849	11.938	11.118	10.380	9.712	9.108	8.559	8.061	7.606
16	14.718	13.578	12.561	11.652	10.838	10.106	9.447	8.851	8.313	7.824
17	15.562	14.292	13.166	12.166	11.274	10.477	9.763	9.122	8.544	8.022
18	16.398	14.992	13.754	12.659	11.690	10.828	10.059	9.372	8.756	8.201
19	17.226	15.679	14.324	13.134	12.085	11.158	10.336	9.604	8.950	8.365
20	18.046	16.351	14.878	13.590	12.462	11.470	10.594	9.818	9.129	8.514

Periods	Interest rates (*r*)									
(n)	11%	12%	13%	14%	15%	16%	17%	18%	19%	20%
1	0.901	0.893	0.885	0.877	0.870	0.862	0.855	0.847	0.840	0.833
2	1.713	1.690	1.668	1.647	1.626	1.605	1.585	1.566	1.547	1.528
3	2.444	2.402	2.361	2.322	2.283	2.246	2.210	2.174	2.140	2.106
4	3.102	3.037	2.974	2.914	2.855	2.798	2.743	2.690	2.639	2.589
5	3.696	3.605	3.517	3.433	3.352	3.274	3.199	3.127	3.058	2.991
6	4.231	4.111	3.998	3.889	3.784	3.685	3.589	3.498	3.410	3.326
7	4.712	4.564	4.423	4.288	4.160	4.039	3.922	3.812	3.706	3.605
8	5.146	4.968	4.799	4.639	4.487	4.344	4.207	4.078	3.954	3.837
9	5.537	5.328	5.132	4.946	4.772	4.607	4.451	4.303	4.163	4.031
10	5.889	5.650	5.426	5.216	5.019	4.833	4.659	4.494	4.339	4.192
11	6.207	5.938	5.687	5.453	5.234	5.029	4.836	4.656	4.486	4.327
12	6.492	6.194	5.918	5.660	5.421	5.197	4.988	7.793	4.611	4.439
13	6.750	6.424	6.122	5.842	5.583	5.342	5.118	4.910	4.715	4.533
14	6.982	6.628	6.302	6.002	5.724	5.468	5.229	5.008	4.802	4.611
15	7.191	6.811	6.462	6.142	5.847	5.575	5.324	5.092	4.876	4.675
16	7.379	6.974	6.604	6.265	5.954	5.668	5.405	5.162	4.938	4.730
17	7.549	7.120	6.729	6.373	6.047	5.749	5.475	5.222	4.990	4.775
18	7.702	7.250	6.840	6.467	6.128	5.818	5.534	5.273	5.033	4.812
19	7.839	7.366	6.938	6.550	6.198	5.877	5.584	5.316	5.070	4.843
20	7.963	7.469	7.025	6.623	6.259	5.929	5.628	5.353	5.101	4.870

FORMULAE

Annuity

Present value of an annuity of $1 per annum, receivable or payable for *n* years, commencing in one year, discounted at *r*% per annum:

$$PV = \frac{1}{r}\left[1 - \frac{1}{[1+r]^n}\right]$$

Perpetuity

Present value of $1 per annum, payable or receivable in perpetuity, commencing in one year, discounted at *r*% per annum:

$$PV = \frac{1}{r}$$

LIST OF VERBS USED IN THE QUESTION REQUIREMENTS

A list of the learning objectives and verbs that appear in the syllabus and in the question requirements for each question in this paper.

It is important that you answer the question according to the definition of the verb.

LEARNING OBJECTIVE	VERBS USED	DEFINITION
1 KNOWLEDGE		
What you are expected to know.	List	Make a list of
	State	Express, fully or clearly, the details of/facts of
	Define	Give the exact meaning of
2 COMPREHENSION		
What you are expected to understand.	Describe	Communicate the key features
	Distinguish	Highlight the differences between
	Explain	Make clear or intelligible/State the meaning of
	Identify	Recognise, establish or select after consideration
	Illustrate	Use an example to describe or explain something
3 APPLICATION		
How you are expected to apply your knowledge.	Apply	To put to practical use
	Calculate/compute	To ascertain or reckon mathematically
	Demonstrate	To prove with certainty or to exhibit by practical means
	Prepare	To make or get ready for use
	Reconcile	To make or prove consistent/compatible
	Solve	Find an answer to
	Tabulate	Arrange in a table
4 ANALYSIS		
How you are expected to analyse the detail of what you have learned.	Analyse	Examine in detail the structure of
	Categorise	Place into a defined class or division
	Compare and contrast	Show the similarities and/or differences between
	Construct	To build up or compile
	Discuss	To examine in detail by argument
	Interpret	To translate into intelligible or familiar terms
	Produce	To create or bring into existence
5 EVALUATION		
How you are expected to use your learning to evaluate, make decisions or recommendations.	Advise	To counsel, inform or notify
	Evaluate	To appraise or assess the value of
	Recommend	To advise on a course of action

Business Management Pillar

Strategic Level Paper

P6 – Management Accounting – Business Strategy

May 2008

Tuesday Morning Session