THE INSTITUTE OF CHARTERED ACCOUNTANTS OF PAKISTAN

Final Examinations Winter 2003

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Business Management **(MARKS 100)**
Module E **(3 hours)**

Q.1 Sportsballs dominate Pakistan's Sporting Goods export category since the mid-1970s. Sialkot, the hub of this industry, has over 300 registered exporters out of which only around 150 own their production facilities. Fewer than 20% of exporters maintain complete vertical production units and stitcher networks. They export 80% of the approximately 35 million hand-stitched balls exported every year. Raw materials such as PVC artificial leather, cloth, rubber latex, and rubber air-bladders, are typically purchased from local suppliers upon receipt of orders and processed into ready-cut panels for hand-stitching. These panels are delivered to sub-contractors, called "makers" who have them stitched by village-based "stitchers". Upon return, these stitched balls are inspected to buyer's order specifications and packaged for shipment. One ball takes an average of 23-30 days from order to shipment.

Figure 1- **Sportsball Exports from Pakistan***

#	PRODUCT CATEGORY (hand-stitched inflatable balls)	% -age	UNITS (million)	USD VALUE (million)	PKR VALUE (million)
1	Professional soccer-balls	3	1.05	6.56	380.48
2	Match-grade soccer-balls	22	7.70	48.13	2,791.54
3	Mass-market soccer-balls	46	16.10	100.63	5,836.54
4	Others, i.e. volleyball, rugby etc.	11	3.85	24.06	1,395.48
5	Promotional balls	18	6.30	39.38	2,284.04
		100	**35**	**218.76**	**12,688.08**

*Estimated from consolidated industry figures.

Record Sports Private Limited was formed in 1981. By 2002 it had become a front-runner in the sporting goods industry, exporting 100% of its products under the logos of leading world brands. It was recognized by a number of national awards including the FPCCI Export Trophy. Competitors and customers both agree that Record's success was due to its founder's personal dynamism, his willingness to challenge traditional business models and his ability to select and groom professionals into decision-making positions.

By early 2002, Record's annual revenues stood at just under Rs. 600 million through an average daily output of about 9,000 units and an annual production capacity of just over two million units. This had already placed Record among the industry's top tier of exporters, in a market characterized by seasonality, low product innovation and stable global demand. Record's present client portfolio contained mid-level regional brands that sold high volumes of the mass-market category, matched by a healthy mix of match-grade balls. So far, Record had successfully avoided getting involved in the promotional category, but it was finding it tough to break into the professional category because of low volumes and highly entrenched competition. Record was recognized for its consistent quality and customer claims were within the 2% allowed. In-house reject rates, at almost 8%, were lower than the industry average of 10-11% because of selective automation of the quality inspection function. However, stitching rejects had to be sent back to the maker for repairs adding days to production time. It was usual practice to commission 10-12% more than the production order to ensure on-time customer shipments.

Financially, Record showed healthy cash-flows and minimal borrowings against credit facilities, fixed assets estimated at over 165 million including almost 100,000 square feet of newly constructed factory floor-space that is under-utilized. Yet, despite its brand new factory outside the city, Record still operated within the traditional cottage-industry model, which helped maintain low overheads and indirect labour costs.

Figure 2- **Production Cost of Typical Sportsball**

#	Item	PKR	USD
A	**RAW MATERIALS**	**116.58**	**2.01**
	Artificial Leather	34.22	0.59
	Natural Latex	10.44	0.18
	Lining cloth	13.92	0.24
	Rubber bladder	10.44	0.18
	Accessories	5.80	0.10
	Screen Printing	9.86	0.17
	Packaging	25.52	0.44
	Miscellaneous	6.38	0.11
B	**CONTRACT LABOUR**	**37.12**	**0.64**
	Maker	7.54	0.13
	Stitcher	23.78	0.41
	Screen Printer	5.80	0.10
C	**FACTORY OVERHEADS**	**132.24**	**2.28**
	Salaries	16.24	0.28
	Utilities	13.34	0.23
	Communication	24.36	0.42
	Facilities Management	8.12	0.14
	Marketing & Travel	69.60	1.20
	Sampling & Testing	0.58	0.01
D	**TAXES & DUTIES**	**21.46**	**0.37**
	Tax @ 5%	14.50	0.25
	Surcharges etc @ 2.5%	6.96	0.12
E	**COST OF SALE**	**307.40**	**5.30**
F	**F.O.B. SALE PRICE**	**362.50**	**6.25**
G	**PROFIT**	**55.10**	**0.95**

* USD 1 = PKR 58

However, things were beginning to change. Global brands were pushing for lower prices in all categories of balls. Forecasts by industry analysts predicted a price compression of 5-8% in the coming 3 years due to new production facilities opening up in China, where local raw materials were cheaper, utilities were less costly, worker efficiency was demonstrably higher, and shipment processing and time-to-market were faster than in Pakistan.

Meanwhile, the world was waking up to labour practice and workplace standards because of revealing press coverage of sweatshop conditions in many factories in developing countries producing for major brand names. Bonded child labour in Pakistan's carpet industry had already caused a major loss of confidence among buyers who were abandoning their Pakistani suppliers and moving to other places such as China and India. The cottage industry model was vulnerable because of its obvious dependence upon home-based cheap labour where there was no way of monitoring conditions of employment, such as voluntary adult workers, their human rights such as fair wages, legal working hours, occupational health & safety and freedom of association. It was quite clear that many customers who had traditionally ordered sportsballs from Pakistan were considering other sourcing options.

Record had the resources to double its infrastructure and the coordination capacity to expand its home-based stitcher workforce accordingly. Moreover, there was opportunity to diversify into allied product ranges like uniforms, goalie gloves and shin-pads at minimal investment. But buyers typically required a supplier to first show what it was capable of before considering any orders. For Record the question was whether buyers would approve of any new investment in allied product manufacturing by Record and whether its new products would be able to compete in price and quality.

The challenge for the CEO was how to attract more business and break ahead of the competition in an environment where volume demand was unlikely to rise beyond the present level, selling prices were sure to decline, the cost of raw material and overheads were continuing to grow, more competitive suppliers in other countries were beginning to look attractive to buyers, and for the first time, workplace standards and workers' rights were becoming important in customers' buying decisions.

The situation clearly called for a new business strategy. Consider yourself in the position of the consultant hired to help the CEO decide on the most appropriate action plan.

(a) What is Record's market share in national sportsballs exports? In the given context, at whose expense would Record strive to gain market share? Explain to the CEO the concept of "entry barriers" and how he would create and sustain competitive advantage by employing it. **(05)**

(b) Within the market segmentation of product categories, which type of balls should Record focus on if it has to become most profitable? Why? List for the CEO all the possible sources of competitor information that can help him determine exact costs and quality levels of the competition. **(05)**

(c) What element of the traditional sub-contracted stitching business model poses the highest risk in terms of managing product quality, turn-around time, resource optimization and human rights & workplace conditions? Knowing what you do about managing risk and establishing direct control, what will you say in response to the CEO's argument that sub-contracting stitching is 10-15% cheaper than stitching all balls in factory controlled workshops? **(06)**

(d) If forecasts about 5-8% price compression prove true over the next year, would Record still be able to retain profitability? Looking at the calculations for the cost of production, under which cost head do you see most potential for saving resources? Make a convincing case for the CEO to re-organize the pricing calculations to create a healthier profit margin. **(04)**

(e) List the key strategy issues that the CEO must consider when developing a business strategy for Record. Conduct a quick SWOT analysis of the situation at Record, keeping in mind the CEO's aim of breaking ahead of the competition through innovations and diversification, but mindful of the local systems, external competition and buyer's emerging attitudes.

Internal	S	W
External	O	T

(10)

Q.2 What is meant by the term "stakeholder"? List or draw a diagram of the possible stakeholders for a large national publicly listed company. How do these stakeholders impact business strategies? What must a business do to maintain a balance between the relative powers and conflicting interests of its stakeholders? **(15)**

Q.3 Human Resource Management is a strategic approach to acquiring, developing, managing and motivating an organization's people. How does it differ from the traditional "personnel" function? Compare the two approaches to prove which is more appropriate to modern business. **(11)**

Q.4 Can the efficiency of an organization be measured in non-financial ways? If yes, how can this be done? Describe what you understand by "key limiting factor" and how you would employ it as a technique to measure efficiency? Explain through a suitable example from the non-profit sector. **(11)**

Q.5 Explain the following terms:

(i) Downsizing
(ii) Total Quality Management
(iii) Empowerment **(09)**

Q.6 In today's shrinking world many businesses consider the possibility of launching operations in a new country. Give an example of a company you know of that has managed to compete successfully in a number of diverse cultures. What are some of the factors that can be considered as opportunities for global competition in the case of such a company? Likewise, what factors could be considered threats to global competition? What would you recommend to a company that wishes to compete globally? **(12)**

Q.7 Do you agree that "international business is really a collection of domestic industries"? Argue for or against the idea, keeping in mind the five factors that influence strategy for a company competing globally as compared to a national one. Draw Porter's "diamond" of determinants of national competitive advantage and explain each segment briefly. **(12)**

(THE END)