

Mock Test Paper - Series II: August, 2026

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INTERMEDIATE: GROUP – II

PAPER – 6: FINANCIAL MANAGEMENT & STRATEGIC MANAGEMENT

PAPER 6A : FINANCIAL MANAGEMENT

Suggested Answers/ Hints

PART I – Case Scenario based MCQs

1. (A) Current Assets (2025–26) = Cash & Cash Equivalents + Accounts Receivable + Inventories
 $= 212 + 4,200 + 4,500 = ₹ 8,912$ thousand
Current Ratio = Current Assets ÷ Current Liabilities = $8,912 ÷ 5,560 = 1.60: 1$
Quick Assets = Current Assets – Inventories = $8,912 - 4,500 = ₹ 4,412$ thousand
Quick (Acid-test) Ratio = Quick Assets ÷ Current Liabilities = $4,412 ÷ 5,560 = 0.79: 1$
2. (C) Receivable Turnover Ratio = Credit Sales ÷ Average Accounts Receivable
Average Accounts Receivable = (Opening + Closing) ÷ 2 = $(3,000 + 4,200) ÷ 2 = ₹ 3,600$ thousand
 $= 14,400 ÷ 3,600 = 4.00$ times
Inventory Turnover Ratio = COGS ÷ Average Inventory
Average Inventory = $(3,000 + 4,500) ÷ 2 = ₹ 3,750$ thousand
 $= 9,600 ÷ 3,750 = 2.56$ times
3. (D) Long-term Debt = Non-Current Borrowings = ₹ 5,000 thousand
Total Debt = Non-Current Borrowings + Current Liabilities = $5,000 + 5,560 = ₹ 10,560$ thousand
Long-term Debt to Total Debt = $(5,000 ÷ 10,560) × 100 = 47.35\%$
Shareholders' Equity = Equity Share Capital + Other Equity = $4,000 + 3,752 = ₹ 7,752$ thousand

$$\begin{aligned}\text{Debt-to-Equity Ratio} &= (\text{Long-term Debt} \div \text{Shareholders' Equity}) \times 100 \\ &= (5,000 \div 7,752) \times 100 = 64.50\%\end{aligned}$$

4. (D) $\text{Net Profit Ratio} = \text{Profit After Tax} \div \text{Sales} \times 100 = 1,680 \div 16,000 \times 100 = 10.5\%$
 $\text{Return on Total Assets} = \text{Profit After Tax} \div \text{Total Assets} \times 100 = 1,680 \div 18,312 \times 100 = 9.17\%$

5. (B) $\text{Interest Coverage Ratio} = \text{EBIT} \div \text{Interest} = (\text{PBT} + \text{Interest}) \div \text{Interest}$
 $= (2,400 + 680) \div 680 = 3,080 \div 680 = 4.53 \text{ times}$. A ratio of 4.53 times, well below the industry norm of 10 times, means earnings cover interest obligations with a much thinner margin than peers. Combined with a Debt-to-Equity Ratio of 64.50% (industry average 35%), the company is both more leveraged than its peers and less able to comfortably service that debt from operating earnings. For a loan officer, this combination rising leverage and weakening debt-servicing capacity is the key red flag in the proposal, not a reason for automatic approval.

6. (A) ₹ 11,20,000
 $\text{Incremental Initial Cash Outlay} = \text{Cost of machine} + \text{Shipping \& Installation}$
 $= ₹ 10,95,000 + ₹ 25,000$
 $= ₹ 11,20,000$

7. (C) 9.533%
 $\text{Weighted Average Cost of Capital (WACC)}$
 $\text{After-tax Cost of Debt:}$
 $10\% \times (1 - 0.32) = 6.8\%$
 $\text{WACC} = \frac{1}{3} (15\%) + \frac{2}{3} (6.8\%)$
 $= 5\% + 4.533\% = 9.533\%$

8. (D) Generally lower than the before-tax cost of debt.

PART II – Descriptive Questions

1. (a) Evaluation of Credit Policies

Particulars	Present Policy (₹)	Proposed Policy (₹)
Credit Sales	20,00,000	23,00,000 (115% of 20,00,000)
Variable Cost (75%)	(15,00,000)	(17,25,000)
Contribution	5,00,000	5,75,000
Bad Debts	(30,000) (20,00,000 × 1.5%)	(57,500) (23,00,000 × 2.5%)
Profit Before Tax (PBT)	4,70,000	5,17,500
Tax @ 30%	(1,41,000)	(1,55,250)
Profit After Tax (PAT)	3,29,000	3,62,250
Opportunity Cost (Refer working note)	(22,500)	(34,500)
Net Profit	3,06,500	3,27,750

In the proposed scheme the net profit is more by ₹ 21,250 i.e. (₹ 3,27,750 – ₹ 3,06,500), hence, the company should change the credit policy.

Working Note:

Opportunity Cost on Investment in Debtors:

Present policy = Variable Cost × (Collection period / 360) × Required rate of return

$$= 15,00,000 \times \frac{45}{360} \times 12\% = ₹ 22,500$$

$$\text{Proposed policy} = 17,25,000 \times \frac{60}{360} \times 12\% = ₹ 34,500$$

Assumptions:

- (i) Cash discount is not availed by the debtors.
- (ii) Debtors are utilising the full credit period for payment.
- (iii) Number of days in a year is 360 days.

(b)

Number of equity shares ($\text{₹ } 40,00,000 \div \text{₹ } 100$)	40,000 shares
Earnings per share, EPS ($\text{₹ } 8,00,000 \div 40,000$)	₹ 20.00
Dividend per share, DPS ($\text{₹ } 4,80,000 \div 40,000$)	₹ 12.00
Rate of return, r ($\text{₹ } 8,00,000 \div \text{₹ } 40,00,000$)	20%
Cost of equity, K_e (inverse of P/E ratio = $1 \div 10$)	10%

(i) **Is the Dividend Policy Optimal?**

Walter's Model values a share as:

$$P = \frac{D + \frac{r}{K_e}(E - D)}{K_e}$$

Substituting the values ($D = \text{₹ } 12$, $E = \text{₹ } 20$, $r = 20\%$, $K_e = 10\%$):

$$P = \frac{12 + \frac{0.20}{0.10}(20 - 12)}{0.10} = \text{₹ } 280.00$$

Since the firm's rate of return, r (20%), is greater than its cost of equity, K_e (10%), it is a growth firm. For a growth firm, Walter's Model prescribes a zero payout as the optimal policy. By retaining 100% of earnings, the value of the share would be:

$$P = \frac{0 + \frac{0.20}{0.10}(20 - 0)}{0.10} = \text{₹ } 400.00$$

Conclusion: Since $r > K_e$, the company is NOT following an optimal dividend policy. Retaining the entire earnings (zero payout) would raise the share value from ₹ 280 to ₹ 400.

(ii) **P/E Ratio at which Dividend Policy Has No Effect**

Dividend policy becomes irrelevant to value only when K_e equals r , i.e. $K_e = 20\%$. The corresponding P/E ratio is:

$$P/E = \frac{1}{k_e} = \frac{1}{0.20} = 5$$

Conclusion: At a P/E ratio of 5 ($K_e = r = 20\%$), dividend policy will have no effect on the value of the share.

(iii) Effect of a Lower P/E Ratio (P/E = 4)

If the P/E ratio is 4, the cost of equity becomes:

$$K_e = \frac{1}{4} = 25\%$$

Recomputing the share value with $r = 20\%$, $K_e = 25\%$, $D = ₹ 12$, $E = ₹ 20$

$$P = \frac{D + \frac{r}{K_e}(E - D)}{K_e}$$

$$P = \frac{12 + \frac{0.20}{0.25}(20 - 12)}{0.25} = ₹ 73.60$$

Here, r (20%) is now less than K_e (25%) the firm has become a declining firm. For a declining firm, Walter's Model prescribes a 100% payout as the optimal policy, the opposite of the conclusion in part (i).

Conclusion: YES, the decision changes. With $P/E = 4$ ($r < K_e$), the optimal policy reverses to full (100%) payout, instead of zero payout.

(c) Statement Showing Computation of Cash Flow After Tax (CFAT)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Capacity Utilisation	50%	65%	80%	100%	100%
Units Produced	1,50,000	1,95,000	2,40,000	3,00,000	3,00,000
Contribution per Unit (₹ 600 × 60%)	360	360	360	360	360
Total Contribution (₹)	5,40,00,000	7,02,00,000	8,64,00,000	10,80,00,000	10,80,00,000
Less: Fixed Cost (₹)	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
Profit Before Tax (₹)	(60,00,000)	1,12,00,000	2,20,00,000	4,93,60,000	5,28,16,000
Less: Tax @ 30% (₹)	(18,00,000)	33,60,000	66,00,000	1,48,08,000	1,58,44,800
Profit After Tax (₹)	(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
Cash Flow After Tax (₹)	3,58,00,000	3,18,40,000	2,98,00,000	4,31,92,000	4,21,55,200

Statement Showing Computation of Net Present Value

Year	Description	Cash Flow (₹)	PVF @12%	Present Value (₹)
0	Initial Investment	(10,00,00,000)	1.000	(10,00,00,000)
0	Working Capital Introduced	(1,50,00,000)	1.000	(1,50,00,000)
3	Additional Working Capital	(2,00,00,000)	0.7118	(1,42,36,000)
1	Cash Flow After Tax	3,58,00,000	0.8929	3,19,65,820
2	Cash Flow After Tax	3,18,40,000	0.7972	2,53,82,848
3	Cash Flow After Tax	2,98,00,000	0.7118	2,12,11,640
4	Cash Flow After Tax	4,31,92,000	0.6355	2,74,48,516
5	Cash Flow After Tax	4,21,55,200	0.5674	2,39,18,860
5	Working Capital Released	3,50,00,000	0.5674	1,98,59,000
5	Sale of Scrap	2,00,00,000	0.5674	<u>1,13,48,000</u>
	Net Present Value			3,18,98,684

Working Note: Computation of Depreciation (WDV Method @ 40% p.a.)

Year	Opening WDV (₹)	Depreciation @ 40% (₹)	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

The Net Present Value of the project works out to ₹ 3,18,98,684 (approximately ₹ 319 lakhs), which is positive and exceeds the ₹ 100 lakhs threshold set by Secure Venture Capital Firm. Nova Green Mobility Ltd. is therefore in a position to secure funding from Secure Venture Capital Firm for this project.

2. (a) Cost of equity for Vertex Industries Ltd.

Given: $R_f = 5\%$, $R_m = 10\%$, $\beta = 2.0$

$$K_e = R_f + \beta (R_m - R_f)$$

$$K_e = 5\% + 2.0 \times (10\% - 5\%)$$

$$K_e = 5\% + 2.0 \times 5\%$$

$$K_e = 5\% + 10\% = 15\%$$

(b) Cost of equity for Competitor A and Competitor B

$$\text{Competitor A } (\beta = 1.2): K_e = 5\% + 1.2 \times (10\% - 5\%) = 5\% + 6\%$$

$$K_e = 11\%$$

$$\text{Competitor B } (\beta = 0.8): K_e = 5\% + 0.8 \times (10\% - 5\%) = 5\% + 4\%$$

$$K_e = 9\%$$

Company	Beta (β)	Cost of Equity (K_e)
Vertex Industries Ltd.	2.0	15%
Competitor A	1.2	11%
Competitor B	0.8	9%

Vertex Industries ($\beta = 2.0$) has the highest cost of equity at 15%, indicating the highest systematic (market-related) risk among the three firms.

(b) Total Assets = ₹ 50 crores

$$\text{Total Assets Turnover Ratio} = \text{Sales} \div \text{Total Assets} = 3$$

$$\text{Hence, Total Sales} = 50 \times 3 = ₹ 150 \text{ crores}$$

Computation of Profit after Tax (PAT)

Particulars	₹ in crores
Sales	150.00
Less: Variable operating cost @ 60%	90.00
Contribution	60.00
Less: Fixed cost (other than interest)	10.00
EBIT (Earnings before interest and tax)	50.00
Less: Interest on debentures (12% × 25)	3.00
EBT (Earnings before tax)	47.00
Less: Tax @ 30%	14.10
EAT (Earnings after tax)	32.90

(i) Earnings per Share

$$\text{EPS} = \text{Earnings available to equity shareholders} \div \text{Number of equity shares}$$

$$\text{EPS} = 32.90 \text{ crores} \div 1.20 \text{ crore shares} = ₹ 27.42$$

(ii) Operating Leverage

$$\text{Operating Leverage} = \text{Contribution} \div \text{EBIT} = 60 \div 50 = 1.20$$

An operating leverage of 1.20 shows that fixed costs form a modest part of Sunrise Foods' cost structure. A 1% change in sales would change EBIT by about 1.20%, so the company's operating profit is only mildly sensitive to swings in sales volume.

(iii) Financial Leverage

$$\text{Financial Leverage} = \text{EBIT} \div \text{EBT} = 50 \div 47 = 1.06$$

The financial leverage is quite low, indicating that Sunrise Foods' interest burden is small compared to its operating profit, the debenture obligation is well covered by EBIT, leaving the company financially comfortable.

(iv) Combined Leverage

$$\text{Combined Leverage} = \text{Operating Leverage} \times \text{Financial Leverage} = 1.20 \times 1.06 = 1.28$$

A combined leverage of 1.28 means a 1% increase in sales would raise EPS by roughly 1.28%, Sunrise Foods carries a moderate overall risk from the combination of its fixed operating costs and its use of debt.

Together, the operating, financial and combined leverages give the board a quick read on how sensitive the company's profits and shareholder earnings are to changes in sales, which is useful context before deciding on any further borrowing or capacity expansion.

3. (a) 1. The Debt option yields the higher EPS. Although the interest rate on debt (8%) equals the dividend rate on preference shares (8%), and both raise the identical amount of additional capital, the two are treated differently for tax purposes:

- Interest on debt is a charge against profit, it is deducted before computing tax, so it earns a tax shield of $(\text{Interest} \times \text{Tax Rate})$.
- Preference dividend is an appropriation of profit, it is paid out of profit after tax, so it earns no tax shield.

Because of this tax shield, the after-tax cost of debt is lower than the after-tax cost of preference capital, so more residual earning is left for equity shareholders under the Debt optio, producing a higher EPS.

2. Existing Equity Share Capital (= Capital Employed) is taken as ₹ 10,00,000, with 1,00,000 shares in issue.

The EPS gap between Debt and Preference arises purely from the tax shield on interest, and this relationship holds regardless of the size of the existing equity base:

- Incremental earnings from choosing Debt over Preference = Tax shield on interest = $X \times 8\% \times 50\% = 0.04X$
- Spread over the unchanged 1,00,000 shares: $\frac{0.04x}{1,00,000} = 0.10$
 $\Rightarrow 0.04X = ₹ 10,000$
 $\Rightarrow X = ₹ \frac{10,000}{0.04} = ₹ 2,50,000$
- EBIT = ROCE $\times$ Capital Employed = $31.25\% \times ₹ 10,00,000 = ₹ 3,12,500$
- Revenue = EBIT $\div$ Operating Margin = $₹ 3,12,500 \div 31.25\% = ₹ 10,00,000$

3. New shares = Additional Funds $\div$ Face Value = $₹ 2,50,000 \div ₹ 10 = 25,000$ shares

Total shares after issue = 1,00,000 (existing) + 25,000 (new) = 1,25,000 shares

4. **Evaluation of alternative options**

Particulars	Option 1 (Equity)	Option 2 (Debt)	Option 3 (Pref. Shares)
Revenue (₹)	10,00,000	10,00,000	10,00,000
EBIT (31.25% of Capital Employed) (₹)	3,12,500	3,12,500	3,12,500
Less: Interest (8% of ₹ 2,50,000) (₹)	Nil	20,000	Nil
Earnings Before Tax (₹)	3,12,500	2,92,500	3,12,500
Less: Tax @ 50% (₹)	1,56,250	1,46,250	1,56,250
Earnings After Tax (₹)	1,56,250	1,46,250	1,56,250
Less: Preference Dividend (8% of ₹ 2,50,000) (₹)	—	—	20,000

Earnings available to equity shareholders (₹)	1,56,250	1,46,250	1,36,250
Number of Equity Shares	1,25,000	1,00,000	1,00,000
Earnings Per Share (EPS)	₹ 1.25	₹ 1.46	₹ 1.36

(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

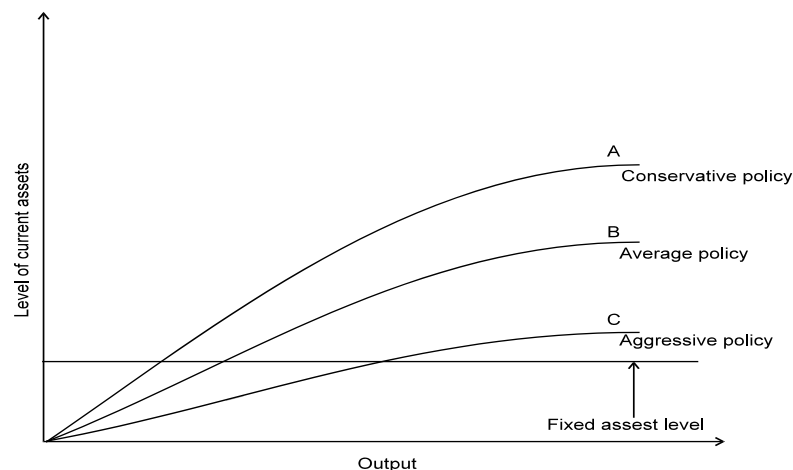
financing. This have an influence on the profitability of the company and ultimately on its wealth.

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) (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.

OR

- (c) Bridge Finance: Bridge finance refers to loans taken by a company normally from commercial banks for a short period because of pending disbursement of loans sanctioned by financial institutions. Though it is of short-term nature but since it is an important step in the facilitation of long-term loan, therefore it is being discussed along with the long term sources of funds. Normally, it takes time for financial institutions to disburse loans to companies. However, once the loans are approved by the term lending institutions, companies, in order not to lose further time in starting their projects, arrange short term loans from commercial banks. The bridge loans are repaid/ adjusted out of the term loans as and when disbursed by the concerned institutions. Bridge loans are normally secured by hypothecating movable assets, personal guarantees and demand promissory notes. Generally, the rate of interest on bridge finance is higher as compared with that on term loans.

PAPER 6B: STRATEGIC MANAGEMENT

ANSWERS

PART I

- | | | | | | | | | | | |
|--------|-----|-----|------|-----|-------|-----|------|-----|-----|-----|
| 1. (A) | (i) | (c) | (ii) | (b) | (iii) | (c) | (iv) | (a) | (v) | (d) |
| (B) | (i) | (d) | (ii) | (a) | (iii) | (b) | | | | |

PART II – Descriptive Questions

1. (a) Ecro Ltd. employs both **proactive** and **reactive** strategic approaches to stay competitive in a dynamic market.

Initially, the company was proactive in its approach by adopting the features of proactive strategies:

- **Strengthening Brand Identity:** Proactively building a strong eco-friendly image to appeal to environmentally conscious consumers.
- **Innovative Marketing Campaigns:** Crafting impactful and creative campaigns to enhance market visibility and differentiate its products.
- **Product Innovation:** Consistently introducing new and innovative eco-friendly products to meet evolving customer demands and maintain a competitive edge.

These proactive strategies are deliberate, reflecting planned actions to improve market position and financial performance.

However, when the company started facing competition from large retailers, it forced the company to quickly adapt to the changing market conditions by following the features of reactive strategies:

- **Adapting to Market Changes:** Responding to the entry of large retailers in the eco-friendly segment by quickly adjusting strategies.
- **Competitor Analysis:** Studying competitors' strategies to counteract their actions effectively.
- **Dynamic Marketing:** Implementing varied marketing techniques to respond to competitors' campaigns.
- **Pricing Adjustments:** Adopting counter-pricing strategies to remain competitive without compromising profitability.

These reactive strategies demonstrate Ecro Ltd.'s ability to adapt to unforeseen developments and changing market conditions.

Future Strategy for Competitive Advantage

To remain competitive and gain a sustainable edge, Ecro Ltd. should adopt a **blended approach** of proactive and reactive strategies:

1. **Sustainable Differentiation:** Focus on continuous innovation and exclusive eco-friendly product lines to strengthen its unique position.
2. **Customer-Centric Approach:** Use data analytics to understand consumer preferences and tailor offerings.
3. **Operational Efficiency:** Optimize supply chain and reduce costs to balance affordability and quality.
4. **Strategic Alliances:** Partner with eco-certification organizations to build credibility and trust.

By crafting a strategy that integrates **planned proactive initiatives** with **adaptive responses**, Ecro Ltd. can navigate uncertainty, tackle competition, and ensure long-term success.

- (b) To enable successful digital transformation, the appropriate strategy for 'Twaran' is a Change Management Strategy. It is essential to effectively manage the organizational, procedural and cultural changes brought about by the adoption of new digital technologies.

Following are the five best practices for managing change in small and medium-sized businesses:

1. **Begin at the top:** Change should be initiated and driven by unified, focused leadership. A committed top management can create and promote a culture that inspires the organization to embrace change.
2. **Ensure that the change is both necessary and desired:** Before initiating digital transformation, decision-makers must understand its necessity and long-term impact. Without a proper strategy, introducing too much change too quickly can be counterproductive.
3. **Reduce disruption:** It is essential to minimize employee disruption during transformation. This can be done by:
 - Communicating changes early.
 - Equipping employees with tools and training.

- Empowering change agents like project managers.
 - Involving IT teams proactively.
 - Creating an environment conducive to change.
4. **Encourage communication:** Promote open and continuous two-way communication. This ensures that employees feel heard and involved and that concerns are addressed timely. Effective communication also promotes innovation and collaboration across departments.
 5. **Recognize that change is the norm, not the exception:** Businesses must treat change as a continuous process, not a one-time project. Being change ready helps the organization to adapt, sustain performance and stay aligned with evolving customer expectations.
- (c) 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**.
2. (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) A tool to identify the market positions of rival companies by grouping them into like positions is **Strategic Group Mapping**. A strategic group consists of those rival firms which have similar competitive approaches and positions in the market.

The procedure for constructing a strategic group map and deciding which firms belong in which strategic group are as follows:

1. Identify the competitive characteristics that differentiate firms in the industry typical variables that are price/quality range (high, medium, low); geographic coverage (local, regional, national, global); degree of vertical integration (none, partial, full); product-line breadth (wide, narrow); use of distribution channels (one, some, all); and degree of service offered (no-frills, limited, full).
2. Plot the firms on a two-variable map using pairs of these differentiating characteristics.
3. Assign firms that fall into about the same strategy space to the same strategic group.
4. Draw circles around each strategic group making the circles proportional to the size of the group's respective share of total industry sales revenues.

3. (a) Strategic performance measures should be **carefully selected** so that they are aligned with organisational goals and provide **relevant, reliable and actionable information**. In selecting the right measures, organizations should consider the following factors:

- ◆ **Relevance:** The measure should be relevant to the organization's goals and objectives and provide information that is actionable and meaningful.
- ◆ **Data Availability:** The measure should be based on data that is readily available and can be collected and analyzed in a timely manner.
- ◆ **Data Quality:** The measure should be based on high-quality data that is accurate and reliable.
- ◆ **Data Timeliness:** The measure should be based on data that is current and up to date, enabling organizations to make informed decisions in a timely manner.

These **factors are important** because they provide a way for organizations to **assess the success of their strategies, identify areas for improvement, and make informed decisions about how to allocate resources and adjust their strategies to achieve their desired outcomes**. Effective strategic performance measures should be relevant, meaningful, and easy to understand and should be regularly reviewed and updated to ensure their continued alignment with the organization's goals and objectives.

- (b) **Innovation** refers to the creation and implementation of **new or significantly improved products, services, processes or business models**. Innovation acts as a key driver of **growth, competitiveness and long-term sustainability**.

Innovation refers to the upgradation of existing products, services or processes, which leads to **higher market share, revenues, profitability and customer satisfaction**. For long-term business growth, innovation plays a crucial strategic role.

What Innovation Offers to an Organisation

1. **Helps Solve Complex Problems:** Innovation enables businesses to identify opportunities in societal and business problems and develop **customer-centric and sustainable solutions**. Though initial costs may be high, innovation ensures long-term economic and environmental sustainability.

2. **Increases Productivity:** Innovation simplifies and automates tasks, reduces manual effort and improves efficiency. Automation and digital tools enhance productivity at both process and organisational levels, creating a ripple effect across industries.
3. **Gives Competitive Advantage:** Faster innovation helps firms move ahead of competitors. Innovative products offer greater customer satisfaction, require less marketing effort, help retain existing customers and attract new ones.

Risks Involved in Innovation

1. **High Cost and Financial Risk:** Innovation involves significant investment and returns may not be immediate or assured.
2. **Uncertain Returns:** Some innovations may not deliver expected benefits, making them appear as unnecessary expenses in the short run.
3. **Technological Uncertainty:** Rapid technological changes may make existing innovations obsolete.
4. **Implementation Risk:** Poor execution or lack of organisational capability can lead to failure of innovative initiatives.

Thus, while **innovation is a powerful driver of growth, productivity and competitive advantage**, it also involves risks that must be carefully managed to achieve **long-term sustainability and success**.

4. (a) Ansoff's Product Market Growth Matrix, developed by Igor Ansoff, is a strategic tool that helps businesses identify growth opportunities by analyzing the interplay between products and markets.

It offers four distinct strategies based on whether the products and markets exist or are new. These strategies are:

1. **Market Penetration:** Focuses on selling existing products in existing markets. This involves increasing market share by enhancing sales through advertising, promotions, competitive pricing, or encouraging higher usage among current customers.
2. **Market Development:** Entails selling existing products in new markets. This could involve exploring new geographical regions, utilizing alternative distribution channels, or creating new market segments.
3. **Product Development:** Involves introducing new or modified products into existing markets. This strategy often requires innovation and developing products that meet current market needs.

4. **Diversification:** Refers to marketing new products in new markets. It is a high-risk strategy as the business ventures into unfamiliar products and markets.

As market dynamics evolve, companies may transition between these strategies to adapt and sustain growth. The matrix provides a structured framework for businesses to align their growth strategies with their capabilities and market conditions.

- (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.

OR

In light of Michael Porter's Five Forces, new entrepreneurs often face significant barriers that restrain their keenness to enter an industry. These barriers increase the competitiveness of existing firms and discourage new entrants, impacting industry profitability.

Common barriers that may restrain new entrepreneurs include:

- (i) **Capital Requirements:** When a large amount of capital is required to enter an industry, firms lacking funds are effectively barred from the industry, thus enhancing the profitability of existing firms in the industry.
- (ii) **Economies of Scale:** Many industries are characterized by economic activities driven by economies of scale. Economies of scale refer to the

decline in the per-unit cost of production (or other activity) as volume grows.

- (iii) **Product Differentiation:** Product differentiation refers to the physical or perceptual differences, or enhancements, that make a product special or unique in the eyes of customers.
- (iv) **Switching Costs:** To succeed in an industry, new entrant must be able to persuade existing customers of other companies to switch to its products. When such switching costs are high, buyers are often reluctant to change.
- (v) **Brand Identity:** The brand identity of products or services offered by existing firms can serve as another entry barrier. Brand identity is particularly important for infrequently purchased products that carry a high unit cost to the buyer.
- (vi) **Access to Distribution Channels:** The unavailability of distribution channels for new entrants poses another significant entry barrier. Despite the growing power of the internet, many firms may continue to rely on their control of physical distribution channels to sustain a barrier to entry to rivals.
- (vii) **Possibility of Aggressive Retaliation:** Sometimes the mere threat of aggressive retaliation by incumbents can deter entry by other firms into an existing industry.