Question 1 – Cavendish plc

(a) ***Statement of profit or loss and other comprehensive income for the year ended 30 June 2021***

		£000
Revenue		6,465
Cost of sales (4,165 + 196 depreciation)	(4,361)	
Gross profit		2,104
Distribution cost		(669)
Administration expense (1,126 + 31 depreciation + 415)	(1,572)	
Operating loss		(137)
Exceptional item:		
Gain on disposal of warehouse	**75**	
Dividend received		80
Profit before taxation		18
Taxation (122-26)		(96)
Loss for the year		(78)
Other comprehensive income		
Revaluation gain		700
Total comprehensive income for the year		**622**

(b) ***Balance Sheet as at 30 June 2021***

		£000
Property, plant and equipment	4,243	
Investment		365
Current assets		
Inventory	1,468	
Trade receivables	947	
Cash at bank	175	
Current liabilities	(868)	
Net current assets		1,722
		6,330
Share capital and reserves		
Share capital		4,500
Share premium	500	
Revaluation reserve		1,270
Retained earnings		60
		6,330

Statement of movement of property, plant and equipment

	L&B	P&M	F&F	Total
Balance b/f	2,400	1,800	620	4,820
Disposal	(150)			(150)
Revaluation reserve		160		160
Balance c/f	**2,250**	**1,960**	**620**	**4,830**
Accumulated depreciation				
Balance c/f		540	360	900
Revaluation reserve		(540)		(540)
P&L charge		**196**	**31**	**227**
Balance c/f		196	391	587
WDV at 30.6.2021	**2,250**	**1,764**	**229**	**4,243**

Current assets	**£**	
Trade receivables		947
Creditors		
Trade payables	566	
Taxation		122
Dividend proposed		180
		868

Balances in revaluation reserve and retained earnings are made up as follows:

	Revaluation reserve (£)	Retained earnings (£)
Balance b/f	600	488
Plant and machinery	700	
Transfer on disposal of warehouse	(30)	30
Loss for the year		(78)
Dividends (200+180)		(380)
Balance c/f	**1,270**	**60**

(c) Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life. Depreciable amount is the cost of an asset, or other amount substituted for cost, less its residual value.

The depreciation policy used has implications for the reported profit and the balance of the asset value on the balance sheet. These has implications for:

(1) Reported profits in a particular year
(2) The tax payable – the higher the depreciation charge the lower the profit and hence the lower the tax charge

However, the overall profits over the lifetime of a depreciable asset would be the same for different depreciation pollicises if the assets are held to their end of life).

Any changes in depreciation policies need to be justified and reported in the annual reports. Any changes in policy that are seen by investors to be arbitrary could be construed negatively by the market on the performance of the firm as well as the reliability of the management in reporting a true and fair view of the firm.

Question 2 – Nilgiris Ltd and Ooty Ltd

(a) Nilgiris Ltd

(i) Extract from statement of cash flows for the year ended 30 September 2024

Cash flow from operating activities

	£000
Cash received from customers (£316,000+£2,000)	318,000
Cash paid to suppliers (£100,400-£800-£2,400)	(107,200)
Cash paid for other expenses	(72,000)
Cash paid for rent (£14,400+£1,200)	(15,600)
Cash paid for advertising (£4,800-£400)	(4.400)
Cash paid for interest (£320-£40)	(280)
Cash flow from operating activities	**118,520**

(ii) Pro and cons of direct vs indirect methods of cash flow statement

Direct method:

Provides greater clarity by setting out operating cash receipts and payments

No accruals adjustments made, hence less susceptible to manipulation than the indirect method

Indirect method:

Sheds light on quality of reported earnings by reconciling earnings with net cash position

Reveals link between profits and cash, hence demonstrates ability to convert profits into cash

(b) Conoor Ltd

(i) Return on equity has seen a significant improvement from 12% to 18.5% in 2024 largely due to the improvement seen in the net income to sales revenue growing from 2.4% to 4%.

Earnings per share have followed return on equity with a significant rise in earnings per share from 2023.

Dividends per share was increased significantly in 2023 and this has been maintained in 2024.

The company has increased its margin over the 3 year period with a fall in the % cost of sale but increases in operating expenses (operating expenses to sales revenue) need to be investigated. *Indicates need for better control of operating expenses.*

However, it can be seen that the improvement in efficiency fell in 2024 when the return on equity fell to 18.5% from the 21% achieved in 2023 due to a significant decline in assets turnover when the sales to total assets fell from 2.7 to 2.0.

One reason could be the increase in non-current assets as shown by the increasing net assets per share. *Indicates need to concentrate on increasing sales to benefit from this increase in the asset base.*

There are also concerns about the control over working capital.

The current and acid test ratios have fluctuated falling to their lowest for the three years in 2024.

Stock turnover has been falling for the past three years and the period of credit taken by customers has increased significantly. This suggests possible liquidity problems and there seems to have been a significant overdraft at the end of 2023 and 2024.

The period of credit taken by suppliers has increased significantly in 2024 and, as it is now an average over two months, suppliers might become restive and press for faster payment. *Indicates a need for improvement in cash flow management.*

Further investigation of Conoor Ltd should include among others:

(i) who are the customers of Conoor (how concentrated are they, how reliable and stable are these customers, have there been many new customer acquisitions, what is the churn among customers etc)
(ii) what are the product lines that Conoor is involved in and whether there are any major new product lines and their performance
(iii) who are the key suppliers to Conoor Ltd and if they are reliable
(iv) what was the performance of the business before 2022
(v) What is the breakdown of the operating expenses and the trends and why
(vi) How is the sales broken down by stores or geographical areas and the trends behind them
(vii) The proportion of debt and equity
(viii) The number of employees

Question 3 – Caledonian Electronics Ltd

(a) Option 1

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
	£m	£m	£m	£m	£m	£m
Plan and equipment	(9.0)					1.0
Sales revenue		24.0	30,8	39,6	26.4	10.0
Variable cost		(11.2)	(19.6)	(25.2)	(16.8)	(7.0)
Fixed cost (excluding depreciation)		(0.8)	(0.8)	(0.8)	(0.8)	(0.8)
Working capital	(3.0)					3.0
Marketing cost		(2.0)	(2.0)	(2.0)	(2.0)	(2.0)
Lease		(0.1)	(0.1)	(0.1)	(0.1)	(0.1)
Total cash flow	(12.0)	9.9	8.3	11.5	6.7	4.1
Discount factor	1.000	0.909	0.826	0.751	0.683	0.621
Present value	(12.0)	9.0	6.9	8.6	4.6	2.5
Net present value	**19.6**					

Option 2

	Year 0	Year 1	Year 2	Year 3	Year 4	Year 5
	£m	£m	£m	£m	£m	£m
Royalties	-	4.4	7.7	9.9	6.6	2.8
Discount factor	1.000	0.909	0.826	0.751	0.683	0.621
Present value	0.0	4.0	6.4	7.4	4.5	1.7
Net present value	**24.0**					

Option 3

	Year 0	Year 2
	12.0	12.0
	1.000	0.826
Present Value	12.0	9.9
Net present value	**21.9**	

(b) Before making a final decision, the board should consider the following factors:

- The long-term competitiveness of the business may be affected by the sale of the patents.
- At present, the business is not involved in manufacturing and marketing products. Would a change in direction be desirable?
- The business will probably have to buy in the skills necessary to produce the product itself. This will involve costs and problems may be encountered. Has this been taken into account?
- How accurate are the forecasts made and how valid are the assumptions on which they are based?

(b) Option 2 has the highest net present value and is therefore the most attractive to shareholders. However, the accuracy of the forecasts should be checked before a final decision is made. Moreover, a discussion of the benefits of examining other forms of investment appraisal should also be considered e.g., Payback method (simple and examines when the investment payback, Internal rate of return etc as they provide alternative information).

Question 4 – Clarendon Ltd

(a) Business model is the customer value proposition, method of value creation and the approach to value capture. A business model innovation involves systemic changes to the value proposition (such as the marketing mix e.g., product, price, promotion and place (distribution)), value creation (manufacturing, operations and distribution), the approach to value capture (revenue and cost architectures) and the value network (i.e partners). A product innovation on the other hand might involve changes to the product but not necessarily all elements of the value proposition, value creation, value capture and value network. A process innovation involves changes in the process (e.g., manufacturing method) but not all elements of the value proposition, value creation, value capture and value network.

(b) Business model innovation typically creates superior competitive advantage compared to product and process innovations because:

i. For competitors it is difficult to identify (as one cannot understand easily what components have been changed and how they have been put together) – systemic nature of change

ii. It is difficult for competitors to replicate even if they were able to identify the components of change

The means for Clarendon Ltd to be able to innovate their business model is to move to a personalisation based product offerings (e.g. Zara) where they are able to meet specific customer requirements based on personal need. However, this would require a major reorganization of its activities and process to cater for cush a need and also changes in its manufacturing strategy.

(c) Challenges typically faced by firms include

i. Cognitive biases (due to dominant designs) by senior management (e.g., Xerox, Polaroid)

ii. Inability to reconfigure competencies

iii. Inability to coordinate change

iv. Political factions within a firm

The above answers need to be discussed with examples of firms from either the academic literature or other sources (e.g., business press etc). In this case of Clarendon, a discussion of how the firms might face similar challenges and what are the possibilities of overcoming them might provide an excellent answer.

Question 5 – Perfect competition and coopetition

(a) Discuss the assumptions behind a perfectly competitive market

- Large (theoretically infinite) number of consumers and suppliers each with an insignificant share of market

- Each firm is too small to affect price via a change in market supply – each individual firm is assumed to be a price taker

- Identical output produced by each firm – homogeneous products that are perfect substitutes for each other (Consumers perceive the products to be identical)

- Consumers have perfect information about the prices all sellers in the market charge

- All firms (industry participants and new entrants) have equal access to resources (technology, other factor inputs)

- No barriers to entry & exit of firms

- The model provides a theoretical benchmark against which we compare and contrast imperfectly competitive markets - point of reference.

Good answers will reflect on the desire of all businesses to move from the assumptions of perfectly competitive markets. In particular, the discussion should focus on the perfectly competitive market acting as a benchmark and then for firms to see how much the assumptions in the industry context vary from the perfectly competitive market model. This provides a means to strategies and seek opportunities to supply at a higher price. Techniques for managing differentiation and information are key, but other valid approaches should be rewarded.

(b) Firms often cooperate and compete at the same time in order to create and capture value. The emergence of shorter product lifecycle, convergence of multiple technologies and increasing costs of conducting R&D require firms to have multiple resources in order to improve continuously on delivering the existing value proposition, while exploring new opportunities to enhance innovation. Such multiple resource requirements often do not reside within a single firm and, hence, firms in the same industry often cooperate in order to share such resources and then go on to compete to divide the created value jointly. Such collaborative activity has been called coopetition.

Coopetition is the concept that the forces that shape industry profits are to a great extent the result of choices made by the individual firms within the industry. As these firms become savvier regarding the reaction of rivals to their own actions, they will choose actions that reduce the likelihood of losing industry profits to price wars, consumer surplus, and/or ineffective negotiations with

suppliers. As each firm comprehends its own role within the industry, firms can collectively fashion strategies that "cause" a force to have only a limited effect. If firms ignore the concept of coopetition, they must resign themselves to simply reacting to the industry forces.

Hence, coopetition could be helpful in formulating competitive strategy by examining the complementary nature of resources between firms and how they might be able to jointly create value and then what are the unique assets of each firm to be able to capture some of the value that is created.

Question 6 – Rutherford Ltd

(a) Two-sided markets are markets where two different types of users may realise gains by interacting with each other through a common platform. For example, Adobe Acrobat, Ebay etc

(b) In two-sided markets because of the interconnected nature of the market the number of customers on one side effects the number of customers on the other side. Demand side network externality is where the addition of a customer adds value to other customers. Many industries such as telecommunications and financial services among others tend to display demand side externalities. Cross-price elasticity is a measure of the sensitivity of the price on one side of the market affecting the number of customers/users on the other side of the market.

(c) Rutherford Ltd needs to study and estimate the effects of this cross-price elasticity in order to develop a pricing strategy. In extreme cases, it might be appropriate to give away for free the proposition to one side of the market in order to generate users on the other side that could be charged. For example, Rutherford might consider giving away its software solution for free as it enables users to use them to create certain designs which if they need to be improved would require further purchase of software services to edit and enhance the key design.