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Question Paper	
SCMPE	**Duration**: 110
Details: Test – 5	**Marks**: 60

Instructions:

- All the questions are compulsory
- Properly mention test number and page number on your answer sheet, Try to upload sheets in arranged manner.
- In case of multiple choice questions, mention option number only Working notes are compulsory wherever required in support of your solution
- Do not copy any solution from any material. Attempt as much as you know to fairly judge your performance.

Q 1: Sun Electronics manufactures and sells various electronic goods like mobile phones, laptops, televisions, refrigerators etc. The company sells these goods through the 30 stores situated in different parts of the country. The store managers place a request to the centralized team situated in Mumbai on a monthly basis. One store can send only one requisition per month.

The requirements of the stores are forwarded to the production planning team which is responsible for scheduling the manufacturing of these products. Once the goods are manufactured, the goods are sent to a central warehouse in Mumbai and are dispatched to different stores according to the store requirements. The time taken from placing a request from store to the delivery of product to the stores takes about 30-40 days on an average. In the process the company procures parts from more than 100 vendors. The company has faced quality related issues with many vendors leading to delay in production.

The average holding period of inventory in Sun Electronics is very high at 45 days as against an industry of 15 days. Since the order to delivery time at a store is very high, the company has traditionally allowed high inventory holding to reduce the stock outs at store level. The company is under severe pressure to improve its working capital cycle.

A high amount of inventory held at each store also means that the products become obsolete quickly. In case of products like mobile phones, new and upgraded versions are available in the market as early as six months from the date of initial launch of a particular model. A significant portion of inventory of mobile phones becomes obsolete every year. The company generally resorts to a discounted sale to liquidate such obsolete models.

The management at Sun Electronics has identified e-commerce as an opportunity for faster growth, both in terms of revenues and profitability. The company is considering launch of its own e-commerce website to sell all products which are currently being sold in physical stores. Depending upon the success of online sales, the company might choose to optimize and close certain physical stores in the next couple of years.

The management of the company is cognizant of the fact that existing inventory procurement and management system will not fit in the new e-commerce business. E-commerce works on a inventory light model and quick as well as on time delivery of products of the customers. The fact that customers could be from a location other than those where Sun Electronics has physical presence makes the matter complex.

The company is considering implementation of a supply chain management system. Will a supply chain management system be of use to Sun Electronics in light of the e-commerce venture? You are required to EXPLAIN the concept of Supply Chain Management and EVALUATE the applicability of in the current case.

(20 Marks)

Q 2: A company, which uses standard marginal costing, furnishes the following details relating to a single product manufacturing and sold in a quarter:

(Rs. '000)		
	Budget	**Actual**
Sale units	6,000	6,400
Sales	1500	1696
Direct materials	240	270
Direct labour	360	416
Variable overheads	600	648
Total variable costs	**1200**	**1,334**

The sales budget is based on the expectation of the company's estimate of market share of 12%. The market report reveals that the actual sales of the product in the whole country for the quarter is 60,000 units

Further data are given as under:

Particulars	Standard	Actual
Direct material price per Kg.	Rs.8	Rs.7.50
Direct labour rate per hour	Rs.6	Rs. 6.40

Required:

i) Compute the following variances for the quarter:

- Gross margin sales volume variance
- Market size variance
- Market share variance
- Sales price variance
- Direct materials usage and price variance
- Direct labour efficiency and rate variances
- Variable overheads efficiency and expense variances.

ii) Prepare an operating statement reconciling the budgeted contribution with actual contribution

(10 Marks)

Q 3:- JPY Limited produces a single product. It has recently automated part of its manufacturing plant and adopted Total Quality Management (TQM) and Just in Time manufacturing system. No inventories are held for material as well as for finished product. The company currently user's standard absorption costing system, Following are related to fourth quarter of 2018-19:

Particulars	Budget	Actual
Production and Sales	100,000 Units	110,000 Units
Direct Materials	200,000 Kg @ Rs. 30/Kg	250,000 Kg @ Rs. 31.20/Kg
Direct Labour Hours	25,000 hrs @ Rs. 300/hr	23,000 hrs @ Rs. 300/hr
Fixed Production Overhead	Rs. 320,000	Rs. 360,000

Production overheads are absorbed on the basis of direct labour hours.

The CEO intends to introduce activity based costing system along with TQM and JIT for better cost management. A committee has been formed for this purpose. The committee has further analysed and classified the production overhead of fourth quarter as follows:

Particulars	Budget	Actual
Costs :		
Material Handling	Rs. 96,000	Rs. 124,000
Set Up	Rs. 224,000	Rs. 236,000
Activity:		
Material Handling (orders executed)	8,000	8,500
Set Up (Production runs)	2,000	2,100

Revisions of standards relating to fourth quarter were made as below:

Particulars	Original Standard	Revised Standard
Material Content per unit	2 Kg	2.25 kg
Cost of Material	Rs. 30 per Kg	Rs. 31 per Kg
Direct Labour Hours	15 Minutes	12 Minutes

Required

(i) CALCULATE Planning and Operational Variances relating to material price, material usage, labour efficiency and labour rate

(ii) CALCULATE overhead expenditure and efficiency variance using Activity Based Costing principles.

(10 Marks)

Q 4: The budgets for activity and cost of PQR Ltd. for the first three quarters of operation are shown below:

Period Covered Months	Budgets Quarters I-III		
	Q- I 1-3 ('000)	**Q -II 4-6 ('000)**	**Q-III 7-9 ('000)**
Activity :			
Sales (units)	9	17	15
Production (Units)	10	20	15
Costs (Rs.):			

Direct Material			
A	60	120	90
B	50	100	75
Production Labour	180	285	230
Manufacturing Overheads Excluding Depreciation	90	120	105
Depreciation of Production Machinery	20	20	20
Administration Expenses	25	25	25
Selling & Distribution Expenses	38	54	50

The figures shown above represent the costs structure of PQR Ltd., which have the following major features:

(i) Fixed element of any cost is completely independent of activity levels.

(ii) Any variable element of each cost displays a linear relationship with activity level, except that the variable labour cost become 50% higher for activity in excess of 19,000 units per quarter due to the necessity for overtime working.

(iii) The variable element of selling and distribution expenses is a function of sales. All other costs with a variable element are a function of production volume.

Activity for each quarter is spread evenly throughout that quarter.

In Quarter IV Production level will be set equal to sales level. Production and sales in this quarter is expected to range between 15,000 units and 21,000 units. The most likely volume is 18,000 units. In month 9 it will be possible to accurately estimate the sales for Quarter IV.

Cost structure will remain the same as in Quarters I to III accept the following:

(i) Labour wage rate will rise by 12 ½ %.

(ii) Variable labour input per unit of output will decrease, due to learning curve effect, such that 80% of the previous labour input per unit of output will be required in Quarter IV. The threshold for overtime working remains at 19,000 units per quarter.

(iii) Fixed factory overheads and the fixed element of selling and distribution costs will each rise by 20% (The variable element of selling and distribution costs will be unaltered)

Required:

(i) Prepare a Statement to show, under each cost classification given in the budgets, the variable cost per unit and fixed costs which will be effective in Quarter IV.

(ii) Prepare a flexible budget of production costs for the Quarter IV.

(10 Marks)

Q 5: Magical Stay is a hotel chain that has properties in popular tourist destinations. Each hotel is at least a 50 room's establishment that has standard, elite and luxury size suites. Currently, the chain has 9 properties spread across World. Magical Stay has its corporate headquarters in based out of each specific property that they cater to. Magical Stay is a public listed company, with majority of its shareholders being institutional investors like mutual funds, banks and insurance companies. Since these investors had a high stake in the company, they had representatives of the board of directors to govern strategic decisions. One of the strategic goals of the company for 2018, was to earn a profit of 1,500 million and keep increasing this target by 10% each year. Due to recessionary conditions, business has been volatile. Consequently, senior management is under pressure to meet the targets.

In order to have a defined plan for operations, Magical Stay prepares an annual budget for each of the properties as well as one master budget that consolidate at a company level. There is a separate financial and business analysis team that is in charge of this exercise. Key assumptions and future expected trends are discussed at with the operations management of each property. After incorporating the corporate headquarters numbers, the consolidated budget is presented to the senior management for approval. In order to have a uniform policy across locations, key metrics like room rent per day, material procurement for kitchen and rooms, employee hiring, capital investments at each property, advertising and promotional activities are handled directly by the corporate headquarters.

The management at each location is responsible to ensure smooth operations of the hotel chain by implementing these policies. The manager of each hotel property is given a target in terms of revenue to be generated, room occupancy and profit to be achieved. Therefore, the management at each location is also under pressure to perform and meet the target set by the senior management, In the past, if the target had not been met for couple of years, the senior management had closed down the hotel and exited the property. At the same time, best performers are given more liberal budgets to operate on. Hence, competition between various locations has always been fierce. There are constant negotiations for been given a "reasonable / practical target" that has to be achieved.

Monthly meetings are scheduled with the corporate office to explain variance of results from the budget. The recent monthly results have shown that 7 of the 9 properties have consistently not been able to meet the targets in the past six months. The situation is confounded because the tourism industry has been affected greatly by recessionary trends in the global economy. Therefore, the footfalls at the regular tourist places, where the hotel has properties, have reduced considerably. In some places occupancy during peak season has only been 60%. Therefore, operations are bleak and uncertain. At these meetings, the operations management argue that due to this dynamic scenario, the budgeted targets set become obscure since they are not based on the current circumstances.

The corporate office has met with the operations management at each of these properties in order to understand the situation better. Discussions have taken place about how the business can be improved. Few of the suggestions to improve performance are:

a. When the hotel is not fully booked, especially during off-season, give manager at each quickly, therefore the decision about the rate would be better handled by the personnel at the authority to rent out rooms at an attractive discount. These opportunities have to encase quickly, therefore the decision about the rate would be better handled by the personnel at the hotel. A guideline on the discount policy can be worked out with the corporate office. This will ensure that room occupancy rates increase, while earning reasonable return.

b. Allow for procurement of kitchen supplies locally, rather than buying it only from specified authorized vendors. Not only will this be cheaper , it also allows for moderate flexibility with the kitchen menu that can cater to customer demands based on current availability of supplies. Prior approvals can be taken by the management from the quality control department to ensure that customer satisfaction does not suffer.

c. A monthly reward and recognition program for employees, based on their service record for the month. Recommendations can be from fellow employees or the location manager.

d. Allow the location management autonomy, with a reasonable budget to cater to purchasing equipment. In order to address certain urgent requirements or repairs, quick response from the operations management is needed. The current process of getting approval the corporate office is cumbersome since it takes a longer time. Autonomy can help address these issues quickly without much damage done to customer satisfaction. Funding can be quickly procured from banks if required.

Based on these discussions, the senior management has decided to decentralize all of the above decisions. As a pilot project, they have decided against preparing a line-wise detailed budget (sales budgets, operations cost budgets, advertising etc.) for each location. Instead the operations management will be given clear targets at each of the locations regarding the key profitability ratios, liquidity ratios and leverage ratios, as also guidelines on market share, quality and customer satisfaction. These benchmarks have been finalized based on industry research of peer group companies. However, the managers have the autonomy to achieve the expected target based on their individual business scenarios at each location. The focus is therefore not on achieving budget numbers that have been finalized. Instead management gets growth targets to achieve.

One year after implementing this decision, it was found that company was able to meet the shareholders' expectations, have a robust growth and energetic employee morale.

Required

i. DISCUSS the traditional budgeting process had a negative impact on Magical Stay's operations.

ii. EXPLAIN the philosophy behind "growth-based targets" instead of "budget based targets.

(10 Marks)