



PAPER – 6:

FINANCIAL MANAGEMENT AND STRATEGIC MANAGEMENT

6A: FINANCIAL MANAGEMENT



QUESTIONS

PART I - Case Scenario based MCQs

1. ABC Ltd, a newly incorporated company, commenced its operations in 2024 by issuing equity shares at face value. The company follows a pure equity capital structure and has 10,000 equity shares outstanding.

During its first two years of operations, the company demonstrated stable financial performance. It earned a profit of ₹ 1,00,000 in 2024 and ₹ 1,04,000 in 2025, reflecting a consistent annual growth rate of 4%. The company's cost of equity (K_e) is estimated at 8%. Based on the Gordon Growth Model, the market price per share at the end of 2025 has been valued at ₹ 162.24.

Although the company has been following a traditional dividend payout policy, the management is now concerned about whether this policy maximizes shareholders' wealth. Specifically, the Board of Directors wants to assess whether the current dividend payout ratio is appropriate in light of the company's growth prospects and return on retained earnings.

To support this decision, the finance team has been instructed to evaluate the firm's dividend policy using both the Gordon Growth Model and Walter's Model. The objective is to determine the impact of the existing and alternative dividend payout strategies on the company's

market price per share, growth rate, capital employed, and overall shareholder wealth maximization.

You are required to answer the following requirements:

- (i) Based on the given information, what is the face value per share and the rate of return on retained earnings (r)?
 - (A) ₹ 10 and 8%
 - (B) ₹ 100 and 10%
 - (C) ₹ 100 and 8%
 - (D) ₹ 10 and 10%
- (ii) What is the market price per share in 2025 under Walter's Model?
 - (A) ₹ 162.24
 - (B) ₹ 150.00
 - (C) ₹ 143.00
 - (D) ₹ 170.00
- (iii) If the firm's return on retained earnings (10%) is greater than its cost of equity (8%), what is the optimum dividend payout ratio and corresponding market price per share?
 - (A) 60% payout; ₹ 143.00
 - (B) 40% payout; ₹ 150.00
 - (C) 0% payout; ₹ 162.50
 - (D) 100% payout; ₹ 130.00
- (iv) What is the capital employed at the beginning of 2026, growth rate and estimated earnings for 2026 if company continue the existing (traditional) dividend payout ratio in 2025?
 - (A) ₹ 11,24,864; 4%; ₹ 1,12,486
 - (B) ₹ 11,89,760; 10%; ₹ 1,18,976

- (C) ₹ 10,81,600; 4%; ₹ 1,08,160
- (D) ₹ 11,24,864; 10%; ₹ 1,18,976
- (v) What is the capital employed at the beginning of 2026, growth rate and estimated earnings for 2026 if company adopts optimum dividend payout ratio in 2025?
- (A) ₹ 11,24,864; 4%; ₹ 1,12,486
- (B) ₹ 11,89,760; 10%; ₹ 1,18,976
- (C) ₹ 10,40,000; 8%; ₹ 1,04,000
- (D) ₹ 11,44,000, 10%, ₹ 1,14,400
2. A firm's current liabilities comprise bank credit and other liabilities in the ratio of 2 : 1. The current liabilities of the firm are 3,00,000 and the current ratio is also 2 : 1. The quick ratio is 1 : 1. Thus, the amount of bank credit and inventory of the firm would be :
- (A) ₹ 3,00,000 and ₹ 1,00,000
- (B) ₹ 2,00,000 and ₹ 3,00,000
- (C) ₹ 3,00,000 and ₹ 2,00,000
- (D) ₹ 1,00,000 and ₹ 3,00,000
3. The capital structure of JKL Limited consists of 12% debentures of ₹ 50 lakhs, 10% preference shares of ₹ 25 lakhs, 14% term loan of ₹ 15 lakhs and equity share capital of ₹ 48 lakhs. Its reserves & surpluses are ₹ 24 lakhs. What would be the capital-gearing ratio?
- (A) 1.04
- (B) 1.25
- (C) 1.33
- (D) 1.56

PART - II Descriptive Questions**Ratio Analysis**

4. The following information pertains to P Limited for the year ended 31st March, 2025 :

Particulars	Amount / Ratio
Sales	₹ 3,60,00,000
Rate of Income Tax	40%
Return on Net Worth	30%
Share Capital to Reserves Ratio	6 : 4
Current Ratio	2 : 1
Percentage of Net Profit to Sales	8%
Inventory Turnover (based on cost of goods sold)	12
Cost of goods sold	₹ 1,44,00,000
Sundry Debtors	₹ 12,00,000
Sundry Creditors	₹ 16,00,000
Interest on 14% debentures	₹ 3,36,000

You are required to CALCULATE:

- (i) Operating Expenses
- (ii) Share Capital and Reserves
- (iii) Closing Stock
- (iv) Fixed Assets

Cost of Capital

5. Zebra Dynamics Ltd., a diversified engineering firm, is currently undergoing a strategic review of its capital financing. The Board of Directors has set strict hurdles for new project approvals. The Chief Financial Officer (CFO) has stated that the company's Cost of Capital based on Book Value weights is currently 11%, while the Cost of Capital based on Market Value weights is exactly 150 basis points higher.

Market Benchmarking Data

To determine the cost of equity, the finance team has gathered data on two comparable peers, A Ltd. and B Ltd, which operate in the same economic environment. Their returns are driven by the Capital Asset Pricing Model (CAPM):

Security	Beta	Expected CAPM Return
A Ltd.	1.2	15.20%
B Ltd.	0.8	12.80%

Capital Structure:

- Book Value Terms: The company maintains a traditional balance sheet with an equal ratio of Equity and Debt.
- Market Value Terms: Due to market optimism, the company's equity trades at a premium. The Market Value of Equity is 3 times its Book Value, while the debt trades at par (Market Value of Debt equals Book Value).

Debt Instrument Details

The company's debt capital is raised entirely through Debentures with the following characteristics:

- Coupon Rate: 7% per annum.
- Issue Details: The debentures were issued at a discount of ₹ 10 for ₹ 90.
- Redemption: They are redeemable at Par (₹ 100).
- Tenure: The debentures mature in 4 years.

You have been hired as a financial consultant to

- (i) PROVIDE a detailed breakdown of the component costs.
- (ii) CALCULATE the corporate tax rate applicable to the company assuming Discount on issue or premium on redemption are tax deductible.
- (iii) CALCULATE the Beta of the company.

Capital Structure

6. The following data relate to two companies belonging to the same risk class:

Particulars	A Ltd.	B Ltd.
Expected Net Operating Income	₹ 18,00,000	₹ 18,00,000
12% Debt	₹ 54,00,000	-
Equity Capitalization Rate	?	18

Required:

- DETERMINE the total market value, equity capitalization rate and weighted average cost of capital for each company assuming no taxes as per M.M. Approach.
- DETERMINE the total market value, equity capitalization rate and weighted average cost of capital for each company assuming 40% taxes as per M.M. Approach.

Leverage Analysis

7. ABC Manufacturing Limited produces industrial components with a well-established market presence. The company operates under a special tax-free status granted by the government, which exempts it from corporate income tax obligations.

Financial Information

The company's financial parameters for the current fiscal year are as follows:

Capital Structure Details

- Total Capital Invested: ₹ 20,00,000 (₹ 20 lakhs)
- Cost of Equity (K_e): 12% per annum
- Cost of Debt (K_d): 6% per annum
- Weighted Average Cost of Capital (WACC): 9% per annum

Operational Information

- Annual Sales Revenue: ₹ 24,00,000 (₹ 24 lakhs)

- Variable Costs: 50% of sales revenue
- Fixed Costs: ₹ 10,00,000 (₹ 10 lakhs) per annum

General corporate tax is 25%

As a financial analyst, you have been tasked with conducting a comprehensive financial analysis of ABC Manufacturing Limited. Specifically, you are required to:

- DETERMINE the optimal debt-equity composition that results in the given weighted average cost of capital of 9%.
- PREPARE a comprehensive Income Statement showing the company's profitability from operations through net income when the cost of debt is 6%, 10% & 12%.
- CALCULATE the Return on Investment (ROI) to assess how efficiently the company is utilizing its total capital invested.
- CALCULATE the Return on Equity (ROE) to evaluate the returns generated for equity shareholders.
- FIND the different leverages in the following format

Leverages	Computation	Dependent on	Indicates effect of ___ on
Leverages showing level of business risk			
Leverages showing level of finance risk			
Leverages showing level of combined risk			

- EXPLAIN the concept of Leverage as a double edged sword by explaining the Leverage Effect when $ROI > K_d$, $ROI = K_d$, $ROI < K_d$.
- DERIVE ROE from ROI in the following format –

Cost of debt =	6%	10%	12%
Return on Investment % of Equity			
Surplus / Deficit from debt payments in %			
Surplus / Deficit from debt payments in INR			
Return on Equity in INR=ROI + Surplus – Deficit			
Return on Equity in % = Return on Equity in INR/Equity			

Investment Decisions

8. EquipLease Financial Services Ltd. is a specialized equipment leasing company that has been operating in the industrial equipment financing space for over 15 years. The company's business model involves purchasing high-value machinery and leasing it to manufacturing companies, thereby earning returns through lease rentals while retaining ownership of the assets. The company has built a strong reputation for providing flexible financing solutions tailored to clients' cash flow patterns and business cycles. Their leasing arrangements help clients conserve capital while accessing state-of-the-art equipment.

EquipLease has recently purchased a specialized CNC precision machine with the following informations:

- **Purchase Cost:** ₹ 10,00,000 (paid upfront)
- **Expected Useful Life:** 4 years
- **Residual/Salvage Value:** Nil (technology becomes obsolete)
- **Depreciation for Tax Purposes:** Can be claimed by EquipLease under Straight line method (SLM) or Units of Production method(UOP)
- **Lease Rentals** earned by company is subject to tax.
- **EquipLease's Cost of Capital:** 10% per annum
- **Corporate Tax Rate:** 25%

TechManufacture Industries Ltd., a growing precision engineering company, has approached EquipLease expressing interest in leasing this

CNC machine. TechManufacture has provided detailed information about their expected utilization pattern:

The machine's usage will follow a graduated ramp-up pattern based on TechManufacture's order book projections:

Year	Production Capacity Utilization	Relative Units
1	Low (Initial phase)	1 unit
2	Medium	2 units
3	High	3 units
4	Peak	4 units

This pattern is typical for businesses scaling up production with new equipment - starting slow as operators are trained and processes are optimized, then ramping up to full capacity. The Client wants the company to charge lease rentals based on the client's utilization pattern 1:2:3:4.

Mr. Vikram Malhotra, the Chief Credit Officer at EquipLease, is tasked with structuring an appropriate lease arrangement. He faces several strategic decisions:

- i. HOW MUCH portion of the cost is recovered from tax savings on depreciation under both the methods viz. SLM & units of production method.
- ii. FIND the portion of investment to be recovered from lease rentals under both the assumptions i.e. Depreciation under both the methods viz. SLM & units of production method.
- iii. DETERMINE minimum lease rentals needed to recover the balance cost of investment after adjusting the Tax shields on the depreciation under both the depreciation methods if -
 - EquipLease charge uniform (equal) rentals over 4 years
 - Lease rentals follow the client's utilization pattern (1:2:3:4)

Working Capital

9. Following information is forecasted by the Puja Limited for the year ending 31st March, 2025:

	Balance as at 1st April, 20X6	Balance as at 31st March, 20X7
	(₹)	(₹)
Raw Material	45,000	65,356
Work-in-progress	35,000	51,300
Finished goods	60,181	70,175
Debtors	1,12,123	1,35,000
Creditors	50,079	70,469
Annual purchases of raw material (all credit)		4,00,000
Annual cost of production		7,50,000
Annual cost of goods sold		9,15,000
Annual operating cost		9,50,000
Annual sales (all credit)		11,00,000

You may take one year as equal to 365 days.

You are required to CALCULATE:

- Net operating cycle period.
- Number of operating cycles in the year.
- Amount of working capital requirement using operating cycles.

Miscellaneous

10. (a) DISCUSS the features of international funding and angel financing in the context of corporate financing.

- (b) "The treasury department of a business concern has evolved its importance over the years from being responsible for only cash handling issues to technical areas revolving around hedging forex risks and composition of capital structure." In the light of this statement, EXPLAIN briefly the fundamental tasks for which treasury department is responsible.
- (c) STATE the acceptance rule under Internal Rate of Return (IRR) method of capital budgeting.

**SUGGESTED ANSWERS**

1. (i) (B) ₹ 100 and 10%

Working Note 1: Earnings per Share (EPS) and Growth rate

$$\text{EPS}_{2025} = \frac{1,04,000}{10,000} = ₹ 10.40$$

$$\text{Growth rate (g)} = \frac{1,04,000 - 1,00,000}{1,00,000} = 4\%$$

Working Note 2: Dividend Payout Ratio & Retention Ratio

Using Gordon Growth Model:

$$P_0 = \frac{D_1}{K_e - g}$$

$$162.24 = \frac{D_1}{0.08 - 0.04} \Rightarrow D_1 = 6.4896$$

$$D_0 = \frac{6.4896}{1.04} = ₹ 6.24$$

Dividend Payout Ratio (DPR)

$$\text{DPR} = \frac{6.24}{10.40} = 60\%$$

Retention Ratio (b)

$$b = 1 - 0.60 = 40\%$$

Working Note 3: Rate of Return on Retained Earnings (r)

$$g = b \times r$$

$$0.04 = 0.40 \times r \Rightarrow r = 10\%$$

$$\text{Earnings in 2024} = 1,00,000$$

$$\text{Capital employed} = \frac{1,00,000}{10\%} = ₹ 10,00,000$$

$$\text{Face value per share} = \frac{10,00,000}{10,000} = ₹ 100$$

(ii) (C) ₹ 143.00

Market Price per Share under Walter's Model (2025)

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

Where:

$$E = 10.40$$

$$D = 6.24$$

$$r = 10\%$$

$$K_e = 8\%$$

$$\frac{r}{K_e} = 1.25$$

$$E - D = 4.16$$

$$P = \frac{6.24 + (1.25 \times 4.16)}{0.08}$$

$$P = ₹ 143.00$$

(iii) (C) 0% payout; ₹ 162.50

Optimum Dividend Policy and Optimum Price (Walter's Model)

When $r > K_e$, optimum dividend payout ratio = 0%

$$D = 0$$

$$P = \frac{\frac{r}{K_e} \times E}{K_e}$$

$$P = \frac{1.25 \times 10.40}{0.08} = ₹ 162.50$$

(iv) (C) ₹ 10,81,600; 4%; ₹ 1,08,160

Year	Capital Employed in Beginning (₹)	Retained Earning for the year (₹)
2024	₹ 10,00,000	1,00,000 × 40% = ₹ 40,000
2025	10,00,000 + 40,000 = ₹ 10,40,000	1,04,000 × 40% = ₹ 41,600
2026	10,40,000 + 41,600 = ₹ 10,81,600	-

Earnings 2026 = 10,81,600 × 10% = ₹ 1,08,160

Growth rate = 4%

(v) (D) ₹ 11,44,000, 10%, ₹ 1,14,400

Revised Growth rate under optimum dividend policy

$$G = b \times r$$

$$G = 100 \times 10\% \Rightarrow g = 10\%$$

$$\text{Capital employed (Beginning 2026)} = 10,40,000 + (1,04,00 \times 100\%)$$

$$= ₹ 11,44,000$$

$$\text{Earnings 2026} = 11,44,000 \times 10\% = ₹ 1,14,400$$

2. (B) ₹ 2,00,000 and ₹ 3,00,000

Calculation of Current Assets

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

$$\text{Current Assets} = \text{Current Ratio} \times \text{Current Liabilities}$$

$$= 2 \times ₹ 3,00,000 = ₹ 6,00,000$$

Calculation of Quick Assets

$$\text{Quick Ratio} = \frac{\text{Quick Assets}}{\text{Current Liabilities}}$$

$$\text{Quick Assets} = \text{Quick Ratio} \times \text{Current Liabilities}$$

$$= 1 \times ₹ 3,00,000 = ₹ 3,00,000$$

Inventory

$$\text{Inventory} = \text{Current Assets} - \text{Quick Assets}$$

$$= ₹ 6,00,000 - ₹ 3,00,000 = ₹ 3,00,000$$

Calculation of Bank Credit

$$\text{Bank Credit: Other Liabilities} = 2:1$$

$$\text{Total Current Liabilities} = ₹ 3,00,000$$

$$\text{Bank Credit} = ₹ 3,00,000 \times \frac{2}{3} = ₹ 2,00,000$$

3. (B) 1.25

Capital Gearing Ratio

$$= \frac{\text{Pref. Share Capital} + \text{Debentures} + \text{Other Borrowed Funds}}{\text{Equity Share Capital} + \text{Reserves and Surplus} - \text{Losses}}$$

$$= \frac{₹ 25 \text{ lakhs} + ₹ 50 \text{ lakhs} + ₹ 15 \text{ lakhs}}{₹ 48 \text{ lakhs} + ₹ 24 \text{ lakhs}}$$

$$= \frac{₹ 90 \text{ lakhs}}{₹ 72 \text{ lakhs}} = 1.25$$

4. (i) Operating Expenses

Net Profit = 8% on Sales = 8% x ₹ 3,60,00,000	₹ 28,80,000
Add: Income Tax = 40% x ₹ 28,80,000/60%	₹ 19,20,000
Profit Before tax	₹ 48,00,000
Add: Debenture Interest	₹ 3,36,000
Profit before interest and tax	₹ 51,36,000
Sales	₹ 3,60,00,000

Less:	
Cost of goods sold ₹ 1,44,00,000	
Profit before interest & tax ₹ 51,36,000	₹ 1,95,36,000
Operating Expenses	₹ 1,64,64,000

(ii) Share Capital and Reserves

Return on Net worth is 30%, hence profit after tax of ₹ 28,80,000 is equivalent to 30% of Net Worth.

$$\text{Net worth} \times 30/100 = ₹ 28,80,000$$

$$\text{Net Worth} = 28,80,000 \times 100/30 = ₹ 96,00,000$$

Ratio of Share Capital to Reserves = 6:4

$$\text{Share Capital} = ₹ 96,00,000 \times 6/10 = ₹ 57,60,000$$

$$\text{Reserves} = ₹ 96,00,000 \times 4/10 = ₹ 38,40,000$$

(iii) Closing Stock

Inventory Turnover (based on cost of goods sold) = 12

$$\text{Cost of goods sold} = ₹ 1,44,00,000$$

$$\text{Inventory Turnover Ratio} = \text{Cost of goods sold/Closing Stock} = 12$$

$$12 = ₹ 1,44,00,000/\text{Closing Stock}$$

$$\text{Therefore, Closing Stock} = ₹ 1,44,00,000/12$$

$$= ₹ 12,00,000$$

(iv) Fixed Assets

Calculation of Total liabilities

$$\text{Interest on 14 \% Debentures} = ₹ 3,36,000$$

$$\text{Therefore debentures} = \frac{₹ 3,36,000 \times 100}{14\%}$$

$$= ₹ 24,00,000$$

Total of Liabilities Side

Share Capital	₹ 57,60,000
Reserves	₹ 38,40,000
Debentures	₹ 24,00,000
Sundry Creditors	₹ 16,00,000
Total Liabilities	₹ 1,36,00,000

$$\text{Current Ratio} = 2:1$$

$$\text{Sundry Creditors} = ₹ 16,00,000$$

$$\frac{\text{Current Assets}}{\text{Current Liabilities}} = 2$$

$$\frac{\text{Current Assets}}{\text{Sundry Creditors}} = 2$$

$$\frac{\text{Current Assets}}{₹ 16,00,000} = 2$$

$$\text{Current Assets} = 2 \times ₹ 16,00,000$$

$$= ₹ 32,00,000$$

$$\text{Fixed Assets} = \text{Total Liabilities} - \text{Current Assets}$$

$$= ₹ 1,36,00,000 - ₹ 32,00,000$$

$$= ₹ 1,04,00,000$$

5. (i) **Let the cost of Equity be 'X' and Cost of Debt be 'Y'**

Calculation of WACC using Book value weights

Source of Capital	Cost of capital	Weights	WACC (K _o)
	(a)	(b)	(c) = (a) × (b)
Equity Share Capital	X	0.5	0.5X
Long term debts	Y	0.5	0.5Y
			11

Calculation of WACC using market value weights

Source of Capital	Cost of capital	MV Weights	WACC (K _o)
	(a)	(b)	(c) = (a) × (b)
Equity Share Capital	X	3/4 = 0.75	0.75X
Long term debts	Y	1/4 = 0.25	0.25Y
			11 + 1.5 = 12.5

$$0.5X + 0.5Y = 11 \quad \dots(1)$$

$$0.75X + 0.25Y = 12.5 \quad \dots(2)$$

Equating 1 & 2

$$K_e (X) = 14\%$$

Substituting X in Eqn. 1

$$0.5 \times 14 + 0.5Y = 11$$

$$7 + 0.5Y = 11$$

$$\text{Post tax } K_d (Y) = 8\%$$

$$(ii) \quad \text{Pre Tax Cost of Redeemable Debenture } (K_d) = \frac{I + \frac{(RV - NP)}{n}}{\frac{(RV + NP)}{2}}$$

Where,

I = Interest payment

NP = Net proceeds

RV = Redemption value of debentures

n = Remaining life of debentures

$$k_d = \frac{7 + \frac{(100 - 90)}{4}}{\frac{(100 + 90)}{2}}$$

$$k_d = \frac{7+2.5}{95}$$

$$\text{Pre Tax } K_d = 10\%$$

$$\text{Post tax } K_d = \text{Pre tax } K_d (1-T)$$

$$8\% = 10\%(1-T)$$

$$\text{Tax rate (T)} = 20\%$$

(iii) According to CAPM

$$\text{Cost of Equity (K}_e\text{)} = R_f + \beta (R_m - R_f)$$

Where,

$$K_e = \text{Cost of equity capital}$$

$$R_f = \text{Risk free rate of return}$$

$$\beta = \text{Beta coefficient}$$

$$R_m = \text{Rate of return on market portfolio}$$

$$(R_m - R_f) = \text{Market risk premium}$$

$$14\% = 8\% + \beta \times 6\%$$

$$\text{Beta coefficient} = 1$$

Working Note:

A Ltd

$$15.20 = R_f + 1.2R_p \quad \dots\dots(1)$$

B Ltd

$$12.80 = R_f + 0.8R_p \quad \dots\dots(2)$$

By solving Eqn. 1 & 2,

$$R_p = 6$$

$$\text{So Risk Premium} = 6\%$$

Substituting $R_p = 6$ in Eqn 1

$$15.20 = R_f + 1.2 \times 6\%$$

$$R_f = 15.20 - 7.20 = 8\%$$

Hence, Risk Free Return = 8%

$$R_p = R_m - R_f$$

$$6 = R_m - 8\%$$

$$R_m = 14\%$$

6. (a) Assuming no tax as per MM Approach.

Calculation of Value of Firms 'A Ltd.' and 'B Ltd' according to MM Hypothesis

Market Value of 'B Ltd' [Unlevered(u)]

$$\begin{aligned} \text{Total Value of Unlevered Firm (V}_u) &= [\text{NOI}/k_e] \\ &= 18,00,000/0.18 \\ &= ₹ 1,00,00,000 \end{aligned}$$

$$K_e \text{ of Unlevered Firm (given)} = 0.18$$

$$\begin{aligned} K_o \text{ of Unlevered Firm (Same as above)} &= k_e \text{ (as there is no debt)} \\ &= 0.18 \end{aligned}$$

Market Value of 'A Ltd' [Levered Firm (l)]

$$\begin{aligned} \text{Total Value of Levered Firm (V}_l) &= V_u + (\text{Debt} \times \text{Nil}) \\ &= ₹ 1,00,00,000 + (54,00,000 \times \text{nil}) \\ &= ₹ 1,00,00,000 \end{aligned}$$

**Computation of Equity Capitalization Rate and
Weighted Average Cost of Capital (WACC)**

	Particulars	A Ltd.	B Ltd.
A	Net Operating Income (NOI)	18,00,000	18,00,000
B	Less: Interest on Debt (I)	6,48,000	-
C	Earnings of Equity Shareholders (NI)	11,52,000	18,00,000
D	Overall Capitalization Rate (k_o)	0.18	0.18
E	Total Value of Firm ($V = \text{NOI}/k_o$)	1,00,00,000	1,00,00,000
F	Less: Market Value of Debt	54,00,000	-

G	Market Value of Equity (S)	46,00,000	1,00,00,000
H	Equity Capitalization Rate [$k_e = NI / S$]	0.2504	0.18
I	Weighted Average Cost of Capital [WACC] (k_o)	0.18	0.18

Assuming 40% taxes as per MM Approach

Calculation of Value of Firms 'A Ltd.' and 'B Ltd' according to MM Hypothesis Approach

Market Value of 'B Ltd' [Unlevered(u)]

$$\begin{aligned} \text{Total Value of unlevered Firm } (V_u) &= [NOI (1 - t) / k_e] \\ &= 18,00,000(1 - 0.40) / 0.18 \\ &= ₹ 60,00,000 \end{aligned}$$

$$K_e \text{ of unlevered Firm (given)} = 0.18$$

$$\begin{aligned} K_o \text{ of unlevered Firm (Same as above} &= k_e \text{ as there is no debt)} \\ &= 0.18 \end{aligned}$$

Market Value of 'A Ltd' [Levered Firm (l)]

$$\begin{aligned} \text{Total Value of Levered Firm } (V_L) &= V_u + (\text{Debt} \times \text{Tax}) \\ &= ₹ 60,00,000 + (54,00,000 \times 0.40) \\ &= ₹ 81,60,000 \end{aligned}$$

Computation of Weighted Average Cost of Capital (WACC) of 'B Ltd.'

$$= 18\% \text{ (i.e. } K_e = K_o \text{)}$$

Computation of Equity Capitalization Rate and Weighted Average Cost of Capital (WACC) of A Ltd

Particulars	A Ltd.
Net Operating Income (NOI)	18,00,000
Less: Interest on Debt (I)	6,48,000

Earnings Before Tax (EBT)	11,52,000
Less: Tax @ 40%	4,60,800
Earnings for equity shareholders (NI)	6,91,200
Total Value of Firm (V) as calculated above	81,60,000
Less: Market Value of Debt	54,00,000
Market Value of Equity (S)	27,60,000
Equity Capitalization Rate [$k_e = NI/S$]	0.2504
Weighted Average Cost of Capital (k_o)*	13.23

*Computation of WACC A Ltd.

Component of Capital	Amount	Weight	Cost of Capital	WACC
Equity	27,60,000	0.338	0.2504	0.0846
Debt	54,00,000	0.662	0.072*	0.0477
Total	81,60,000			0.1323

$$*K_d = 12\% (1 - 0.4) = 12\% \times 0.6 = 7.2\%$$

$$WACC = 13.23\%$$

7. Optimal debt-equity composition

Let the weight of equity be W

Item	Cost	Weight	Product
Equity	12	W	12W
Debt	6	1 – W	6 – 6W
		1	9%

$$9 = 12W + 6 - 6W$$

$$3 = 6W$$

$$W = 0.5.$$

So, Weight of Equity is 0.50

So, Weight of Debt is $1 - 0.50 = 0.50$

Total Capital = 20 Lakhs. Hence, Debt and equity 10 Lakhs each.

Income Statement

Cost of debt =	6%	10%	12%
Sales	24,00,000	24,00,000	24,00,000
Less: Variable Costs (50%)	12,00,000	12,00,000	12,00,000
Contribution	12,00,000	12,00,000	12,00,000
Less: Fixed Costs (Given)	10,00,000	10,00,000	10,00,000
EBIT	2,00,000	2,00,000	2,00,000
Less: Interest	60,000	1,00,000	1,20,000
EBT / PAT	1,40,000	1,00,000	80,000
Return on Investment = EBIT/ Capital employed	10%	10%	10%
Return on equity = PAT / Equity Capital	14%	10%	8%

Leverages showing level of different risk

Leverages showing level of	Leverages	Computation	Dependent on	Indicates effect of ... on ...
Business risk	Operating Leverage (DOL)	$\text{Contribution} \div \text{EBIT}$ $= 12,00,000 \div 2,00,000$ $= 6$	Fixed Operating Costs	Sales on EBIT
Financial Risk	Financial Leverage (DFL)	$\text{EBIT} \div \text{EBT}$ $= 2,00,000 \div 1,40,000$ $= 1.43$	Fixed Financial Costs	EBIT on EPS
Combined Risk	Combined Leverage (DCL)	$\text{Contribution} \div \text{EBT}$ or $\text{DOL} \times \text{DFL} = 6 \times 1.43$ $= 8.58$	Both Fixed Operating & Fixed Financial Costs	Sales on EPS

$$\begin{aligned}\text{Return on Investment} &= \text{EBIT} / \text{Capital employed} \\ &= 2,00,000 / 20,00,000 = 10\%\end{aligned}$$

When the cost of 'fixed cost fund' is less than the return on investment, financial leverage will help to increase return on equity and EPS. The firm will also benefit from the saving of tax on interest on debts etc. However, when cost of debt will be more than the return it will affect return of equity and EPS unfavourably and as a result firm can be under financial distress. Therefore, financial leverage is also known as "**double edged sword**".

Effect on EPS and ROE:

When, ROI (10%) > Interest (6%) – Favourable – Advantage

When, ROI (10%) < Interest (12%) – Unfavourable – Disadvantage

When, ROI (10%) = Interest (10%) – Neutral – Neither advantage nor disadvantage

Income Statement

Cost of debt =	6%	10%	12%
Return on Investment = 10% of Equity	1,00,000	1,00,000	1,00,000
Surplus / Deficit from debt payments in %	10 – 6 = 4%	10 – 10 = 0	10 – 12 = - 2%
Surplus / Deficit from debt payments in INR = % of Debt	40,000	Nil	(20,000)
Return on Equity in INR = ROI + Surplus – Deficit	1,40,000	1,00,000	80,000
Return on Equity in % = Return on Equity in INR / Equity	14%	10%	8%

8. Calculation of PV of Tax savings under Straight line method (SLM)

Particulars	Result
Annual Depreciation	10 Lakhs / 4 Years = 2,50,000
PV of Tax savings on above	2,50,000 Lakhs x 25% x PVAF @ 10% i.e. 3.170 = 1,98,125

Calculation of PV of Tax savings under Units of Production (UOP)

Year	Depreciation	Tax savings	PVF @ 10%	PV of Tax Savings
1	1,00,000	25,000	0.909	22,725
2	2,00,000	50,000	0.826	41,300
3	3,00,000	75,000	0.751	56,325
4	4,00,000	1,00,000	0.683	<u>68,300</u>
				1,88,650

Let lease rental of 1st year be X

PV of after tax Lease rentals charged as per client's utilization pattern

Year	Lease rentals	After Tax Lease Rentals	PVF @ 10%	PV of Lease Rentals
1	X	0.75X	0.909	0.682X
2	2X	1.5X	0.826	1.239X
3	3X	2.25X	0.751	1.690X
4	4X	3X	0.683	<u>2.049X</u>
				5.660X

PV of after tax Lease rentals charged equally

Let annual lease rental be X

$$X \times (1 - 25\%) \times 3.17(\text{PVAF @ } 10\%) = 2.378X$$

Investment to be recovered from lease rentals

Particulars	In UOP Ratio		Equally	
	SLM	UOP	SLM	UOP
Investment	10,00,000	10,00,000	10,00,000	10,00,000
PV of Tax savings on Depreciation	1,98,125	1,88,650	1,98,125	1,88,650
Investment to be recovered	8,01,875	8,11,350	8,01,875	8,11,350
PV of after-tax Lease rentals	5.660X	5.660X	2.378X	2.378X
Lease rentals = X	1,41,674	1,43,348	3,37,206	3,41,190

Statement Showing PV of yearly lease rentals when charged in UOP Ratio

Year	Particulars	SLM	UOP
	Lease rentals = X	1,41,674	1,43,348
1	0.682X	96,622	97,763
2	1.239X	1,75,534	1,77,608
3	1.690X	2,39,429	2,42,258
4	<u>2.049X</u>	2,90,290	2,93,720
	PV of Total after tax lease rental	8,01,875	8,11,350

Statement Showing PV of yearly lease rentals when charged Equally

Year	Particulars	SLM	UOP
	Lease rentals = X	3,37,206	3,41,190
1	0.682X (0.909 x 0.75)	2,29,974	2,32,692
2	0.620X (0.826 x 0.75)	2,09,068	2,11,538
3	0.563X (0.751 x 0.75)	1,89,847	1,92,090
4	<u>0.512X (0.683 x 0.75)</u>	1,72,649	1,74,689
	PV of Total after tax lease rental	8,01,539*	8,11,009*

* Difference is due to rounding off in PVAF

9. Working Notes:

1. Raw Material Storage Period (R)

$$\begin{aligned}
 &= \frac{\text{Average Stock of Raw Material}}{\text{Annual Consumption of Raw Material}} \times 365 \\
 &= \frac{\text{₹ 45,000} + \text{₹ 65,356}}{2} \times 365 \\
 &= \frac{\text{₹ 3,79,644}}{\text{₹ 3,79,644}} \times 365 \\
 &= 53 \text{ days.}
 \end{aligned}$$

Annual Consumption of Raw Material

$$\begin{aligned} &= \text{Opening Stock} + \text{Purchases} - \text{Closing Stock} \\ &= ₹ 45,000 + ₹ 4,00,000 - ₹ 65,356 \\ &= ₹ 3,79,644 \end{aligned}$$

2. Work-in-Progress (WIP) Conversion Period (W)

$$\begin{aligned} \text{WIP Conversion Period} &= \frac{\text{Average Stock of WIP}}{\text{Annual Cost of Production}} \times 365 \\ &= \frac{\frac{₹ 35,000 + ₹ 51,300}{2}}{₹ 7,50,000} \times 365 \\ &= 21 \text{ days} \end{aligned}$$

3. Finished Stock Storage Period (F)

$$\begin{aligned} &= \frac{\text{Average Stock of Finished Goods}}{\text{Cost of Goods Sold}} \times 365 \\ &= \frac{₹ 65,178}{₹ 9,15,000} \times 365 = 26 \text{ days.} \\ \text{Average Stock} &= \frac{₹ 60,181 + ₹ 70,175}{2} \\ &= ₹ 65,178. \end{aligned}$$

4. Debtors Collection Period (D)

$$\begin{aligned} &= \frac{\text{Average Debtors}}{\text{Annual Credit Sales}} \times 365 \\ &= \frac{₹ 1,23,561.50}{₹ 11,00,000} \times 365 \\ &= 41 \text{ days} \\ \text{Average debtors} &= \frac{₹ 1,12,123 + ₹ 1,35,000}{2} = ₹ 1,23,561.50 \end{aligned}$$

5. Creditors Payment Period (C)

$$\begin{aligned}
 &= \frac{\text{Average Creditors}}{\text{Annual Net Credit Purchases}} \times 365 \\
 &= \frac{\left(\frac{\text{₹ } 50,079 + \text{₹ } 70,469}{2} \right)}{\text{₹ } 4,00,000} \times 365 \\
 &= 55 \text{ days}
 \end{aligned}$$

(i) Operating Cycle Period

$$\begin{aligned}
 &= R + W + F + D - C \\
 &= 53 + 21 + 26 + 41 - 55 \\
 &= 86 \text{ days}
 \end{aligned}$$

(ii) Number of Operating Cycles in the Year

$$= \frac{365}{\text{Operating Cycle Period}} = \frac{365}{86} = 4.244$$

(iii) Amount of Working Capital Required

$$= \frac{\text{Annual Operating Cost}}{\text{Number of Operating Cycles}} = \frac{\text{₹ } 9,50,000}{4.244} = \text{₹ } 2, 23,845.42$$

- 10. (a) International Funding:** With liberalization and globalization a business enterprise has options to raise capital from International markets also. Foreign Direct Investment (FDI) and Foreign Institutional Investors (FII) are two major routes for raising funds from foreign sources besides ADR's (American depository receipts) and GDR's (Global depository receipts). Obviously, the mechanism of procurement of funds has to be modified in the light of the requirements of foreign investors.

Angel Financing: Angel Financing is a form of an equity-financing where an angel investor is a wealthy individual who provides capital for start-up or expansion, in exchange for an ownership/equity in the company. Typically, angels, as they are known as, will invest around 25 to 60 per cent to help a company

get started. This source of finance sometimes is the last option for startups which doesn't qualify for bank funding and are too small for venture capital financing.

(b) The fundamental tasks for which treasury department of any enterprise is responsible are:

1. **Cash Management:** It involves efficient cash collection process and managing payment of cash both inside the organisation and to third parties.

Treasury will also manage surplus funds in an investment portfolio. Investment policy will consider future needs for liquid funds and acceptable levels of risk as determined by company policy.

2. **Currency Management:** The treasury department manages the foreign currency risk exposure of the company. In a large multinational company (MNC) the first step will usually be to set off intra-group indebtedness. The use of matching receipts and payments in the same currency will save transaction costs and also will save the organization from any unfavorable exchange movements.

The treasury will manage any net exchange exposures in accordance with company policy. If risks are to be minimized then forward contracts can be used either to buy or sell currency forward.

3. **Fund Management:** Treasury department is responsible for planning and sourcing the company's short, medium and long-term cash needs. They also facilitate temporary investment of surplus funds by mapping the time gap between funds inflow and outflow.

4. **Banking:** It is important that a company maintains a good relationship with its bankers. Treasury department carry out negotiations with bankers with respect to interest rates, foreign exchange rates etc. and act as the initial point of contact with them.

5. **Corporate Finance:** Treasury department is involved with both acquisition and divestment activities within the group. In addition, it will often have responsibility for investor relations.

(c) **Acceptance Rule of IRR method.**

The use of IRR, as a criterion to accept capital investment decision involves a comparison of IRR with the required rate of return known as cut-off rate.

If $IRR \geq$ Cut-off Rate or WACC	Accept the Proposal
If $IRR <$ Cut-off Rate or WACC	Reject the Proposal

6B: STRATEGIC MANAGEMENT



QUESTIONS

Multiple Choice Questions

1. EcoRide Motors, founded in Chennai in 2017, started as a small manufacturer of electric scooters targeted at environmentally conscious urban commuters. The company gained momentum when the government introduced FAME subsidies for EV adoption and rising fuel costs made electric mobility more attractive. Initially, EcoRide differentiated itself with sleek designs and strong battery life, which appealed to young professionals in metro cities.

As the EV industry became more competitive, EcoRide realized that success depended not only on product quality but also on an efficient value chain. The company focused on building close partnerships with battery suppliers, invested in efficient assembly lines, and created a network of after-sales service centers. This integrated approach gave EcoRide an edge in reliability and customer satisfaction.

In 2021, EcoRide attempted to enter the budget scooter market to expand its customer base. However, the move backfired as cost pressures affected margins, and established players already had stronghold in the low-price segment. Internally, this failure led to debates within the management team. The CEO adopted a transformational leadership style, motivating employees to view challenges as opportunities and encouraging cross-functional collaboration for innovation.

To restructure its portfolio, EcoRide introduced high-performance e-bikes for premium customers while continuing scooters for the mass market. Management positioned scooters as a potential Cash Cow in the

BCG matrix due to steady demand but low growth, whereas the e-bikes were considered Stars, expected to drive future growth in the expanding premium EV segment.

Recently, when the government announced stricter battery recycling norms, EcoRide faced resistance from dealers who feared higher compliance costs. At the same time, an environmental NGO emerged as a powerful stakeholder, urging EcoRide to adopt greener supply chain practices. The company recognized that managing stakeholder expectations would be critical for long-term sustainability.

Based on the above Case Scenario, answer the Multiple Choice Questions.

- (i) EcoRide's initial success was supported by external factors such as EV subsidies and rising fuel costs. Which specific environmental analysis tool should EcoRide use to systematically assess these factors, and why would it be more suitable than SWOT in this context?
 - (a) BCG Matrix
 - (b) PESTLE Analysis
 - (c) Porter's Five Forces
 - (d) Strategic Group Mapping
- (ii) By partnering with battery suppliers, improving assembly lines, and investing in service centers, EcoRide focused on strengthening its entire chain of operations. Which framework does this reflect and how does it add competitive advantage to the EV industry?
 - (a) Value Chain Analysis
 - (b) Experience Curve
 - (c) Ansoff's Growth Matrix
 - (d) McKinsey 7S Framework

- (iii) When EcoRide attempted to enter the budget scooter market but failed due to intense competition and thin margins, which of Porter's Five Forces best explains the challenge, and how did it affect profitability?
 - (a) Threat of Substitutes
 - (b) Bargaining Power of Suppliers
 - (c) Competitive Rivalry among Existing Firms
 - (d) Bargaining Power of Buyers
 - (iv) EcoRide categorized scooters as Cash Cows and e-bikes as Stars in its portfolio planning. According to the BCG Matrix, what does this imply about the resource allocation strategy the company should follow for each product?
 - (a) Harvest scooters & divest e-bikes
 - (b) Invest in scooters & maintain e-bikes
 - (c) Harvest scooters & invest in e-bikes
 - (d) Divest scooters & harvest e-bikes
 - (v) The rise of environmental NGOs and stricter recycling regulations highlight the importance of stakeholder management. Using Mendelow's Matrix, how should EcoRide position NGOs as stakeholders, and what type of engagement strategy would be most appropriate?
 - (a) Minimal Effort – monitor occasionally
 - (b) Keep Informed – provide regular updates
 - (c) Keep Satisfied – manage but not deeply involve
 - (d) Key Players – actively engage and collaborate
2. Rohan is a manager at "Z-Foods." His primary responsibility is to develop specific tactics for the marketing department to ensure that the "Quick-Snack" division achieves its market share targets. At which level of strategic management is Rohan functioning?
- (a) Corporate Level

- (b) Business Level
 - (c) Functional Level
 - (d) Administrative Level
3. In the smartphone industry, if a few large component manufacturers control the supply of specialized OLED screens and there are no viable alternative suppliers, the smartphone brands face high pressure from:
- (a) Bargaining power of buyers
 - (b) Threat of substitutes
 - (c) Bargaining power of suppliers
 - (d) Industry rivalry
4. Jayant oversees the 'Consumer Goods' segment of a large conglomerate. This specific segment has its own dedicated legal and finance heads who operate semi-autonomously from other segments like 'Industrial Parts'. This structure is an example of:
- (a) Simple Structure
 - (b) Matrix Structure
 - (c) Strategic Business Unit (SBU)
 - (d) Functional Structure
5. VitaGlow Naturals Ltd., a personal care company, launches a new herbal shampoo "HerbaSilk" that is sulphate-free, prevents hair fall and contains rare botanical extracts sourced from the Himalayas. Customers perceive it as superior to ordinary shampoos. The company prices HerbaSilk 25% higher than its regular shampoo range and sales rise strongly due to its perceived uniqueness. Identify the strategy adopted by VitaGlow Naturals Ltd.:
- (a) Cost leadership strategy
 - (b) Focus strategy
 - (c) Differentiation strategy
 - (d) Best-cost provider strategy

6. Rajesh Textiles Ltd., a leading fabric manufacturer, establishes MedCare Hospitals to enter the healthcare services industry, which has no technological or market linkage with its existing textile business. The management expects growth through sectoral expansion and risk spreading. This move represents which type of diversification?
- Concentric diversification
 - Conglomerate diversification
 - Horizontal diversification
 - Vertical diversification

Descriptive Questions

Chapter 1-Introduction to Strategic Management

7. Ms. Kavya has been appointed as the CEO of GreenHarvest Foods Ltd., an organic food company that has diversified into plant-based nutrition products. The company plans to launch the NutriPure brand of plant-based protein foods. GreenHarvest aims to promote healthy lifestyles through nutritious, sustainable, and ethically sourced food products. Draft a suitable vision and mission statement that Kavya may formulate for NutriPure.
8. Mr. Vikram Patel owns a chain of ten bookstores across the Mumbai region. Three of these stores were launched in the past two years. He has always believed in strategic management and enjoyed robust sales of books, magazines, and educational materials until about five years ago. However, with the increasing preference for online shopping, the sales at his physical stores have declined by approximately sixty percent over the last five years. Analyze Vikram Patel's current position in light of the limitations of strategic management.

Chapter 2-Strategic Analysis: External Environment

9. Riya, the strategy manager of FreshSip Beverages Ltd., was studying the packaged fruit juice market in India before launching a new preservative-free juice brand. She observed that several established brands, low-priced local players, and substitute drinks like smoothies and flavored milk were competing intensely. Which aspect of external environment analysis is reflected in this situation?

10. How does the PESTLE framework assist in analyzing the macro-environment?

Chapter 3-Strategic Analysis: Internal Environment

11. Neha, the strategy head of UrbanRide Motors Ltd., was analysing the two-wheeler industry before launching a new premium electric scooter. She observed that firms in the market could be grouped based on price range (economy–premium) and technology (petrol–electric). She decided to position UrbanRide among premium electric brands. Which strategic analysis tool is reflected in this situation?
12. Write a short note on the key strategic drivers of an organization.

Chapter 4-Strategic Choices

13. Arvind, CEO of Stellar Electronics Ltd., decided that instead of depending only on consumer appliances, the company should enter the renewable energy equipment business to achieve long-term growth and reduce business risk. He proposed establishing a new division for solar panels and batteries. Which corporate strategy is reflected in this decision?
14. Explain the strategic implications of each of the following types of business in a corporate portfolio:
- (a) Stars, (b) Question Marks, (c) Cash Cows, (d) Dogs

Chapter 5-Strategy Implementation and Evaluation

15. FinEdge Services Ltd., a financial consulting firm, initiated a digital transformation programme to modernise its services. The management defined clear digital objectives, assessed existing manual processes and capability gaps, prepared a phased digital roadmap and implemented new technologies and work practices across all levels of the organization. Which concept of strategy implementation is reflected?
16. Write a short note on Matrix Structure.



SUGGESTED ANSWERS/HINTS

1. (i) (b) (ii) (a) (iii) (c) (iv) (c) (v) (d)

2. (c)

3. (c)

4. (c)

5. (c)

6. (b)

7. The **NutriPure** brand of plant-based nutrition products may have the following vision and mission:

Vision: Vision implies the blueprint of the company's future position. It describes where the organization wants to land.

Ms. Kavya should aim to position **NutriPure** as a trusted leader in plant-based nutrition. The vision may be "To be a leading plant-based nutrition brand that nourishes lives, supports holistic well-being, and inspires sustainable living."

Mission: Mission defines the firm's business purpose, goals, and approach to achieving them. It explains the reason for the company's existence. Ms. Kavya may articulate the mission as:

- To develop plant-based nutrition products that enhance health and vitality.
- To promote sustainable food choices through ethically sourced and natural ingredients.
- To support healthier communities by providing safe, nutritious and environmentally responsible food solutions.

8. Vikram Patel is facing declining sales due to a significant shift in customers toward online platforms. Although he employs strategic management tools, they cannot always overcome every obstacle or guarantee success. The limitations of strategic management in Vikram's situation include:
- The environment in which strategies are developed is highly complex and unpredictable. The entry of online bookstores, a new type of competitor, introduced a different dynamic to the book retail industry. These online platforms, with their extensive reach and pricing power, have dominated the market, posing a formidable challenge to traditional bookstores.
 - Another limitation of strategic management is the difficulty in forecasting future developments. Despite his strategic management efforts, Vikram Patel did not anticipate the extent to which online bookstores would impact his sales.
 - While strategic management is a time-consuming process, it is crucial for Vikram to continue managing strategically. These challenging times demand increased effort and adaptability on his part.
 - Strategic management can be costly. Vikram Patel might consider hiring experts to understand customer preferences better and adjust his strategies to offer more personalized services. These customized offerings could be difficult for online stores to replicate, giving him a competitive edge.
 - The bookstores owned by Vikram Patel are much smaller in scale compared to online stores. This makes it challenging for him to predict how online platforms will manoeuvre strategically.
9. The situation reflects the **competitive environment (industry environment)** aspect of external environment analysis.

The competitive environment consists of factors within the industry that influence a firm's competitive position, such as existing competitors, new entrants, substitutes, and pricing rivalry. As per strategic analysis, firms must evaluate industry structure and competitive forces before entering or expanding in a market.

In the given case, Riya observed the presence of many established brands, low-cost local players, and substitute beverages like smoothies and flavored milk. This indicates intense industry rivalry and strong threat from substitutes. Such conditions affect profitability and market entry decisions.

Therefore, FreshSip must assess competitive forces and develop appropriate strategies such as differentiation or cost competitiveness to succeed. Hence, the aspect reflected is the competitive (industry) environment of external analysis.

10. The PESTLE framework assists in analyzing the macro-environment by systematically evaluating six external factors that impact an organization's operations and strategy.
1. **Political Factors:** This includes government policies, regulations, political stability, and taxation. Understanding these factors helps organizations anticipate regulatory changes and government interventions that could affect their business environment.
 2. **Economic Factors:** This involves assessing economic conditions such as interest rates, inflation, exchange rates, and economic growth. These factors influence business costs, consumer purchasing power, and overall market conditions.
 3. **Social Factors:** This examines demographic trends, lifestyle changes, cultural norms, and consumer attitudes. Insights into social factors help businesses align their products and services with evolving consumer preferences and societal trends.
 4. **Technological Factors:** This includes technological advancements, innovation rates, and technological infrastructure. These factors impact production processes, product development, and competitive positioning.
 5. **Legal Factors:** This involves understanding business laws, employment regulations, health and safety standards, and compliance requirements. Legal factors are crucial for ensuring regulatory compliance and avoiding legal risks.

6. **Environmental Factors:** This covers ecological issues, sustainability practices, and environmental regulations. Awareness of environmental factors helps businesses adapt to climate change and meet sustainability goals.

By analyzing these factors, the PESTLE framework provides a comprehensive understanding of the macro-environment, helping organizations anticipate changes, adapt strategies, and make informed decisions.

11. The situation reflects the use of **Strategic Group Mapping**, an important tool of industry (competitive) environment analysis.

Strategic group mapping identifies clusters of firms within an industry that follow similar strategies or have similar characteristics, such as price level, quality, technology, distribution, or product range. Firms within the same strategic group compete more directly with each other than with firms in other groups.

In the given case, Neha classified two-wheeler firms based on price (economy to premium) and technology (petrol to electric). This classification creates distinct strategic groups such as economy petrol, premium petrol, economy electric, and premium electric. UrbanRide plans to position itself in the premium electric group.

Such mapping helps identify close competitors, market gaps, and positioning opportunities before strategic decisions. Hence, the strategic analysis tool reflected is Strategic Group Mapping.

12. **Key Strategic Drivers of an Organization**

Strategic drivers are essential elements that influence an organization's ability to differentiate itself from its competitors and achieve competitive advantage. These drivers assess the current performance of the business and provide insights into areas that need focus.

The key strategic drivers include:

1. **Industry and Markets:** Understanding the industry and markets is crucial for identifying the organization's relative position. Industries group similar companies based on their primary products, while markets are defined by the buyers and sellers of

these products. Analyzing industry and market dynamics, often through tools like strategic group mapping, helps organizations evaluate competition and refine strategies.

2. **Customers:** Identifying and understanding customers is a critical driver. Customers are segmented based on their needs and spending capacity, which guides product development and marketing strategies. Differentiating between customers (buyers) and consumers (users) is vital to tailoring pricing, design, and usability strategies effectively.
3. **Products and Services:** Products and services are central to defining the business. Organizations must assess their offerings, classify products, and devise strategies for differentiation, branding, and pricing. Product innovation and marketing are key to maintaining competitiveness.
4. **Channels:** The channels through which products and services are delivered impact on accessibility and customer satisfaction. Strategies related to direct, digital, or relationship-based marketing ensure the efficient distribution of offerings to target customers.

By aligning these drivers with organizational goals, businesses can achieve sustained growth and maintain a competitive edge.

13. The decision taken by Arvind reflects the **diversification strategy**, which is a corporate-level strategy.

Corporate level strategy is concerned with the choice of business, direction and scope of the organization as a whole. It addresses the fundamental issue of what businesses the organization should be in and how the overall business portfolio should be managed to achieve growth and stability.

Diversification strategy involves entry into new products or businesses that are different from the firm's existing operations. It is adopted to achieve growth, reduce risk arising from dependence on a single business and exploit new opportunities in the environment.

In the given case, Stellar Electronics Ltd., which was earlier operating in consumer appliances, proposes to enter the renewable energy equipment business such as solar panels and batteries by creating a new division. This represents expansion into a new business area beyond its present product line with the objective of long-term growth and risk reduction. Thus, the company is broadening its business portfolio by adding a new business, which is characteristic of diversification at the corporate level. Hence, the corporate strategy reflected is diversification strategy.

14. In the BCG growth-share matrix portfolio of investments are represented in two-dimensional space. The vertical axis represents market growth rate, and the horizontal axis represents relative market share. The strategic implications for various business types under BCG in the corporate portfolio are:

Stars are products or businesses that are growing rapidly and are the best opportunity for expansion. *Stars may follow the Build strategy.* They need heavy investments to maintain their position and finance their rapid growth potential.

Cash Cows are low-growth, high market share businesses or products. They generate cash and have low costs. They are established, successful, and need less investment to maintain their market share. *A strategic alternative advocated for cash cows is Harvest.*

Question Marks are low market share businesses in high-growth markets. *A strategic option for them is Hold for which they need heavy investments.* Question marks if left unattended are capable of becoming cash traps.

Dogs are low-growth, low-share businesses and products. *The relevant strategy is Divest.* Dogs may generate enough cash to maintain themselves, but do not have much future. Dogs should be minimized by means of divestment or liquidation.

15. The situation reflects **digital transformation supported by change management**, an aspect of strategy implementation.

Digital transformation refers to the use of digital technologies to develop new or improved business processes, services or operating models. Such transformation requires planned organizational change, which is enabled through change management.

Change management in the digital transition consists of four essential elements:

1. Defining the goals and objectives of the transformation
2. Assessing the current state of the organization and identifying gaps
3. Creating a roadmap for change that outlines the steps needed to reach the desired state
4. Implementing and managing the change at every level of the organization

In the given case, FinEdge defined digital objectives, assessed manual processes and capability gaps, created a phased roadmap and implemented new technologies and practices across all levels. These actions correspond to all four elements of digital transformation change management. Hence, the concept reflected is digital transformation through change management in strategy implementation.

- 16.** In matrix structure, functional and product forms are combined simultaneously at the same level of the organization. Employees have two superiors, a product/project manager and a functional manager. The "home" department - that is, engineering, manufacturing, or marketing - is usually functional and is reasonably permanent. People from these functional units are often assigned temporarily to one or more product units or projects.

The product units / projects are usually temporary and act like divisions in that they are differentiated on a product-market basis. The matrix structure may be very appropriate when organizations conclude that neither functional nor divisional forms, even when combined with horizontal linking mechanisms like strategic business units, are right for the implementation of their strategies. Matrix structure was developed to combine the stability of the functional structure with flexibility of the

product form. It is very useful when the external environment (especially its technological and market aspects) is very complex and changeable.

A matrix structure is most complex of all designs because it depends upon both vertical and horizontal flows of authority and communication. It may result in higher overhead costs due to more management positions.

The matrix structure is often found in an organization when the following three conditions exist:

1. Ideas need to be cross-fertilized across projects or products;
2. Resources are scarce; and
3. Abilities to process information and to make decisions need to be improved.