ICAP

Multi Subject Assessment Stage

3 June 2025
4 hours and 15 minutes – 100 marks

Management Professional Competence

CRN:

Name: ______________________________

INSTRUCTIONS

Please carefully read the following instructions:

1. You are required to access your answer working area by using your Student ID and Password as mentioned on your Admit Card.
2. The overall duration of the exam is 4 hours and 15 minutes, which includes the reading time and an extra 30 minutes of time that has been allocated due to the introduction of computer-based examinations.
3. All questions are compulsory.
4. Questions can be attempted in any sequence.
5. There is no specific time allocated for individual questions.
6. An auto-save function runs every minute. Further, your answers are saved automatically when you navigate between questions or click on the > **(NEXT)** or < **(BACK)** symbols.
7. Each question provides an answer area with a Rich Text Format (RTF) editor for writing your answers. Additionally, below the RTF editor, a spreadsheet is provided to facilitate examinees in doing rough calculations or other workings. **However, please note that any work performed in the spreadsheet will not be considered for marking. To ensure your work is considered, you must copy and paste it from the spreadsheet to the RTF editor.**
8. Work done in the spreadsheet of one question can also be copied into the RTF editor of the same or another question.
9. You may use Microsoft Office applications such as MS Word or MS Excel for rough working. However, please remember that any work performed in these applications cannot be copied into the examination software, and vice versa. Furthermore, any such work will not be uploaded with your exam for marking.
10. You may use pen and paper for rough work, but please note that pen and paper work should only be done on the last two pages of the question paper that are specifically allocated for this purpose. Remember that any rough work done on these pages will not be uploaded with your exam for marking.
11. In accordance with the open book policy of this paper, you are allowed to have a maximum of **FIVE** original books duly bound. Please ensure that the books or notes you bring are permissible under the open book policy. Keeping a book or notes that are not permissible will be considered a violation under the policy on the use of unfair means.
12. An external calculator can be used, provided it is included in the list of permissible calculators issued by ICAP.
13. During the exam, access to any website other than exam software website is strictly prohibited. Engaging in such activities will be considered a violation under the policy on the use of unfair means.

QUESTION 1

Dijkot footwear (DF) is based in Faisalabad and makes high quality sports footwear on behalf of several well-known global brands. Following the global trend in regular exercise post-pandemic, growth has been strong in recent years. As a result, DF is facing a capacity constraint as they are poised to take on new customers from overseas, but DF cannot immediately see how to fulfil the potential orders in an acceptable timeframe.

The board is therefore looking to expand by moving production overseas to a developing country to increase capacity and reduce labour costs. Following research and negotiations, DF have secured the option to buy an existing limited company in the overseas location – White Flash Footwear (WFF) that already makes sports footwear - for a price already agreed. WFF would then be a wholly owned subsidiary of DF. The current owners of WFF are looking to retire in the next 6 months.

Financing options for the acquisition need to be considered. Some directors favour equity as the investment is a permanent expansion, and is cheaper than debt as dividends don't necessarily have to be paid. Other directors disagree and believe debt is cheaper given the tax deductibility of interest payments. The board is evenly split on the decision to finance with debt or equity. Azlaan Sanghera, the professionally qualified Finance Director, has been asked to appraise the acquisition and financing options being considered, and is in the process of preparing analysis to form the basis of a briefing note to the board. Azlaan has prepared a memorandum collecting together relevant details for this exercise (see Appendix 1), and has a copy of the latest financial statements for DF to help examine the impact of different funding options (see Appendix 2).

At a recent board meeting, Azlaan also suggested that the Board could consider an alternative approach – 'we know the owners of WFF are looking to retire, so they are keen to sell. Wouldn't it just be simpler to buy the factory and machinery from them and take over the employment contracts we want to take over, and leave their corporate history behind? We could form a new company which would be a wholly owned subsidiary of DF to put the new business into'. After a lengthy discussion, Rohaan Khan, the Chief Executive Officer, deferred debate until the strategic, financial and taxation issues have been explored in detail.

The chosen country for expansion has a reputation for having lax labour laws, a poor health and safety record, and it is legal to employ children in that location. WFF has incredibly low labour costs, and 40% of the workforce is under the age of 13 years. The Human Resources director of DF objected to the chosen location on humanitarian grounds, but the Marketing Director responded 'we wouldn't be breaking any laws, and we would be providing an income to the families of the children working there. Plus, it maybe no-one even notices. I don't see a problem. Let's not forget the board's bonus depends on our ability to get this deal over the line.'

DF's current customers are internationally renowned brands, and have been reliable customers of DF for many years. Azlaan is concerned that if the acquisition of WFF goes ahead and orders from new customers are accepted, the new customers pose a liquidity and credit risk that DF hasn't been exposed to in many years, so care needs to be taken when offering them credit, balancing the needs of DF whilst also making the terms of trade acceptable to the new customers. Azlaan is considering how the current terms (see Appendix 3) should be amended to achieve this balance.

Requirements

(a) Assuming the acquisition is to be financed by debt, calculate the Adjusted Present Value of buying the WFF company shares. **(08 marks)**

(b) Recommend with justification how acquiring the WFF shares should be financed. **(08 marks)**

(c) Compare the option to expand overseas either by buying the shares of WFF, or by buying the factory, office premises and machinery from them, using the Suitability, Acceptability, Feasibility Framework. Make a reasoned recommendation as to which should be adopted. Further calculations are not required, and ignore taxation. **(14 marks)**

(d) Under the Income Tax Ordinance, 2001, discuss the tax implications of DF's expansion plan in the context of the requirements outlined in (b) and (c) above. **(07 marks)**

(e) Evaluate the ethical issues and implications of investing in the chosen overseas location. **(06 marks)**

(f) Recommend how the current customer credit terms should be changed for the new overseas customers. **(07 marks)**

Total: 50 marks

APPENDIX 1 – MEMO FROM AZLAAN

To: Acquisition task force team
From: Azlaan Sanghera
Subject: CONFIDENTIAL: White Flash Footwear

Dear team

The board are currently debating how to finance the potential acquisition of White Flash Footwear (WFF). In order to inform further discussion at board level, can you please prepare calculations appraising the acquisition of WFF assuming it is financed by debt for Rs. 6,000 million? This can then be used to demonstrate the impact of the debt-financing alternative in this board debate. To help with this I attach below some relevant information:

Business value
WFF is projected to generate incremental earnings of Rs. 950 million for the group in the first year, increasing by 5% per year indefinitely.

Finance
If financed by equity, then a right issue would be investigated. Horizon Holdings, our 65% shareholder, has indicated they would be willing to contribute further to finance their share of the acquisition.

If financed by debt, then more bonds would be issued on similar terms to currently. The current market price of these bonds is Rs. 80,000 per Rs. 100,000 (the nominal value). They would be issued for market price.

WFF's current equity beta is 1.5.

I look forward to receiving the first draft of your calculations this week please.

Best wishes

Azlaan

APPENDIX 2 – EXTRACT FROM LATEST DIJKOT FOOTWEAR FINANCIAL STATEMENTS AND MARKET INFORMATION

Statement of financial position

	Rs. in million
Long term liabilities	
8% irredeemable dentures	10,000
Equity	
Share capital (Rs. 100 each)	1,000
Retained earnings	13,950
	14,950
Total equity	**24,950**

Market information:

- Current share price: Rs. 2,500 per share
- Effective tax rate: 39% including super tax
- Risk free rate: 5% per year
- Market rate of return: 15% per annum
- Industry average gearing level (Debt/(debt + equity) using market values): 35%

APPENDIX 3 – DIJKOT FOOTWEAR RECEIVABLES POLICY

Credit control department policy: Credit accounts offered to customers

No customer can be offered credit unless they have been a cash customer of the company for at least 2 years.

After 2 years, and after receipt of a satisfactory bank reference and 2 trade references of our choosing, a credit limit of 10% of the previous 12 months sales can be offered on 30 day terms from the date of dispatch.

After a further period of 2 years, this can be extended to a limit of 25% of the previous 12 months sales on 45 day terms from the point of dispatch provided credit terms have been adhered to consistently.

Any variation from the above requires board majority approval.

QUESTION 2

Turbat Packaging (TP) manufactures commercial packaging and has two basic ranges – paper and plastic. For the first thirty years of operation, the company grew steadily and predictably in a stable environment. However, in recent times there has been increasing concern with the environmental impact of single use packaging. In response, the company made a decision a year ago to phase out the plastic range over a 3 year period, and increase the range of paper packaging. The current paper packaging is made from virgin pulp (from trees cut down for the purpose), but TP has recently set a target to source 75% of paper from recycled sources in 2 years' time.

When the board made the decision to phase out plastic packaging, there was unanimous agreement at board level, and the individual directors resubmitted their departmental strategies with the new corporate goal in mind. Progress has been frustratingly negligible with rolling out the plan that was announced a year ago. In other words, TP is suffering from strategic drift – in practice it is continuing with its existing strategy even though the business environment is suggesting a change is needed.

Staff are generally happy in their roles, and like the stability and predictability of the working environment. Zara Mazari, the Human Resources director is proud of the high staff satisfaction rating and low staff turnover experienced in TP, and she puts this down to the simple yet effective appraisal system the company uses (Appendix 2).

The board prides itself on its informal approach to communications with staff. In the early days, board members knew every member of staff and their families. As the business has grown however, this approach has become increasingly difficult and impractical, so the board now sends out occasional emails to keep in touch with staff.

The board has now decided that a formal change programme is required to realise the new strategic goals of phasing out plastic packaging and ensuring 75% of paper packaging is sourced from recycled sources. The board met with the management committee recently to start this process (Appendix 1).

Requirements

(a) Evaluate and explain the cause of the strategic drift being suffered by TP. **(06 marks)**

(b) Recommend changes to the appraisal system required to remedy the issues identified in requirement (a). **(05 marks)**

(c) Recommend and justify steps to be taken in the initial 'unfreeze' stage of the change programme. **(10 marks)**

(d) Evaluate the ethical issues that would arise as a result of the operations manager's suggestion in the management committee meeting. **(04 marks)**

Total: 25 marks

APPENDIX 1 – NOTES OF MANAGEMENT MEETING

Chair: Zara Mazari, Director of Human Resources

Present: Zara Mazari, Naeem Dawood (operations manager), Danish Pasha (finance manager), Rahim Syed (marketing representative)

Apologies: All other board members, and the remaining 10 members of the management committee.

Zara Mazari (ZM) opened the meeting, and started by saying the Board has decided a change management subcommittee was needed to help ensure the successful roll out of two strategic initiatives over the next 2 years:

- Phase out of plastic packaging
- 75% of paper packaging to be manufactured from recycled sources

ZM explained that a recognised three stage change management process would be adopted:

- Unfreeze: Ensure the staff understand and accept the need for change.
- Change: Devise a new strategy and ways of working, and implement it.
- Refreeze: Ensure the new systems and processes are the 'new normal' and are adopted as standard routine.

There then ensued a detailed discussion about whether it was a good idea to phase out plastic packaging, and debates around why recycled paper was to be used, as it was felt by the management committee to cheapen the TP brand. The discussion was inconclusive, and ZM called the meeting back to order.

ZM noted that the phase out of plastic packaging had been announced at board level a year ago and built into departmental plans, but there had been negligible progress, hence ideas were needed to ensure the new strategy was rolled out successfully.

Naeem Dawood (ND) suggested taking a vocal opponent of the new approach from the workforce, and dismissing them publicly to make an example of them. ZM asked ND to speak to her after the meeting to explore the idea further.

The 30 minutes timeslot for the meeting drew to a close, so ZM asked for further ideas to be emailed to her over the coming week.

APPENDIX 2 – EMAIL FROM HR DIRECTOR: CURRENT APPRAISAL SYSTEM

To: Rehan Kashani, Finance Director
From: Zara Mazari, Human Resources Director
Subject: Summer staff satisfaction survey

Dear Rehan

Thank you for collating and presenting the data and analysis for the summer staff satisfaction survey. As requested I include my comments for inclusion in the final report:

'It is pleasing to see that staff satisfaction levels remain high, and staff turnover is at an all-time low in the company. As a board we pride ourselves on the quality of the relationship we have with our workforce.

In large part, this is due to the effectiveness of the appraisal system used by the business. It is designed to incentivise stable but continual improvement year-on-year. In essence, each member of staff has targets relevant to their role – some are financial, some non-financial. The higher of last year's target and actual performance is the basis for the current year assessment. Any improvements on this basis provides the starting point of a positive appraisal, pay rises and bonuses for the current year. This encourages a smooth, stable, consistent growth path that staff are clearly motivated by.'

Thank you once again Rehan. Any questions or clarifications needed, please let me know.

Best wishes

Zara

QUESTION 3

Karachi Storage Solutions (KSS) provides warehouse services for clients. It uses diesel powered forklift trucks extensively for heavy lifting in well ventilated areas. Some members of the board are increasingly concerned about the impact the use of diesel powered forklifts could have on KSS Corporate Social Responsibility credentials because the warehousing industry is very dynamic – fast moving and unpredictable - as clients push hard for a greener, more efficient and effective service and increasingly complex and global supply chain management models. Other directors however don't even acknowledge the environmental factors of using diesel as an issue, and fail to see any benefits in doing, measuring or reporting on such things.

The Operations Director has suggested that many of the forklifts currently in service are close to the end of their useful economic lives, and that they could be replaced with electric forklifts to improve the environmental sustainability of the company's operations. Manufacturers of electric forklifts are keen to increase the sales volume of their products to promote their brands, so they are offering the option to lease the forklifts as opposed to buying them. The Finance Director (Sameer Jalbani) has agreed to prepare the financial and non-financial case comparing the lease option compared to buying (see Appendix 1).

KSS has been approached by a tech start-up business looking to sell KSS software to automate forklift driving. The software should reduce labour costs as drivers will not be needed, and should reduce running costs as the software will continuously optimise truck speed and direction to balance the time taken to move inventory with the cost. A price of Rs. 500 million has been quoted by the tech start-up company for the software. The board would like to understand the financial value of the software to the company to help them appraise this offer (see Appendix 2).

Changes to KSS warehouse systems are required to facilitate the new forklifts to accommodate a different pallet size and charging requirements. Some of this investment can be financed from existing reserves, however costs savings are required elsewhere in order to fully finance the investment required. The financial controller has targeted a 15% reduction in administration costs per year (marketing, finance, human resources and IT) compared to the prior year over each of the coming 3 years, but is facing an aggressive backlash from department heads as they have no idea if this is achievable.

Requirements

(a) Evaluate the case for updating the Corporate Social Responsibility policies to improve the economic performance of the business. **(05 marks)**

(b) Recommend, with reasons, whether the new electric forklift trucks should be leased as opposed to purchased outright. Include supporting calculations. **(10 marks)**

(c) Estimate the value of the automation software using the Calculated Intangible Value approach. **(05 marks)**

(d) Evaluate the appropriateness of the current cost reduction plans for KSS, and recommend any changes required to the proposed approach. **(05 marks)**

Total: 25 marks

APPENDIX 1 – EMAIL: LEASE OR BUY ELECTRIC FORKLIFTS

To: Financial analysis team
From: Sameer Jalbani
Subject: Electric forklifts – lease or buy

Hi

I hope you are well. As you are aware, we are looking to replace our aged fleet of diesel forklifts with electric ones, and we are tasked with examining the case for leasing as opposed to buying the trucks – both the financial and non-financial aspects. Can you please draft the case for me, using the following background information:

Ownership

- Period of ownership: 4 years
- Cost of purchasing a truck: Rs. 12.5 million
- Residual value after 4 years: Rs. 2 million (Note: the operations manager tells us 4 years is the least expensive and best period of ownership.)
- Tax allowable depreciation can be ignored
- Quarterly maintenance costs (included in the lease cost if leased): Rs. 245,902 per quarter, tax deductible
- Pre-tax cost of borrowing for KSS: 12.55% per year

Leasing

- Lease term: 3 years
- Lease payments: Rs. 1,639,344 per quarter in arrears for 3 years. This is allowable for tax purposes
- The assets remain the property of the leasing company for the whole lease.

The rate of tax on corporate income is 39%.

I look forward to receiving your draft analysis. Any questions, please ask.

Best wishes

Sameer

APPENDIX 2 – MEMORANDUM: THE FINANCIAL IMPACT OF AUTOMATION SOFTWARE

To: Sameer Jalbani, Finance director
From: Danish Jalbani, CEO
Subject: Value of automation software

Dear Sameer

I hope you are well. As you know we have been approached by Warehouse Automation Software (WAS), who have offered to supply us with automation software for the new range of electric forklifts. The price they have asked for is Rs. 500 million. We need to understand the value of this software to us, and as discussed can you please supply the board with your Calculated Intangible Value for this software?

I include a note of the assumptions we agreed around the boardroom table which I believe may be relevant in your calculations:

- Our forecast profit after tax for next year is Rs. 2,000 million, excluding the impact of the software. We make a net margin of 20%, and a gross profit margin of 40%
- We pay tax at a rate of 39%
- Impact of the software: a reduction in costs of sale by 5% per year, indefinitely
- Our cost of capital is 20% per year

I look forward to hearing from you.

Thanks and regards

Danish

(THE END)

Rough Sheet

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