

CIMA

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Pre-seen case study for Strategic level examinations – Papers E3, P3 and F3

For examinations in November 2011 and March 2012

PRE-SEEN MATERIAL, PROVIDED IN ADVANCE FOR PREPARATION AND STUDY FOR THE EXAMINATIONS IN NOVEMBER 2011 AND MARCH 2012.

INSTRUCTIONS FOR POTENTIAL CANDIDATES

This booklet contains the pre-seen material for the above examinations. It will provide you with the contextual information that will help you prepare yourself for the examinations.

You may not take this copy of the pre-seen material into the examination hall. A fresh copy will be provided on each of the examination days as part of the examination paper.

Section A of each of the three Strategic level papers (E3, P3 and F3) will be based on this material.

Unseen material will be provided on the examination day; this will comprise further context and the examination question requirements (a maximum of four compulsory questions, totalling 50 marks).

You will not be expected to have any knowledge of any other examination questions or unseen materials based on this pre-seen case study.

Section B of each of the three Strategic level papers (E3, P3 and F3) will **NOT** be based on this material.

The examination will last for three hours. You will be allowed 20 minutes reading time **before the examination begins** during which you should read the question paper and, if you wish, make annotations on the question paper. However, you will **not** be allowed, **under any circumstances**, to either begin writing or to use your calculator during the reading time.

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Pre-seen case study for Strategic level examinations

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Pre-seen case study

Introduction

Considers governance.

M plc is a long established publisher of newspapers and provider of web media. It is based in London and has had a full listing on the London Stock Exchange since 1983. The company has three operating divisions which are managed from the United Kingdom (UK). These are the Newspapers Division, the Web Division and the Advertising Division.

Newspapers Division

The Newspapers Division publishes three daily newspapers and one Sunday newspaper in the UK. The Division has three offices and two printing sites. Between them the three offices edit the three daily newspapers and the Sunday newspaper. The Newspaper Division has two subsidiary publishing companies, FR and N. FR is based in France within the Eurozone and N in an Eastern European country which is outside the Eurozone. Printing for all the Division's publications, except those produced by FR and N, is undertaken at the two printing sites. FR and N have their own printing sites.

*No Mags
No books*

News Intl do contract printing

Web Division

The Web Division maintains and develops 200 websites which it owns. Some of these websites are much more popular in terms of the number of "hits" they receive than others. Web material is an increasing part of M plc's business. In the last ten years, the Web Division has developed an online version of all the newspapers produced by the Newspapers Division.

Keep some, sell some?

"free" opportunity to charge e.g. Times

Advertising Division

The sale of advertising space is undertaken for the whole of M plc by the Advertising Division. Therefore, advertisements which appear in the print media and on the web pages produced by the Newspapers Division (including that produced by FR and N) and the Web Division respectively are all handled by the Advertising Division.

Problem selling space overseas.

response?

Adding or destroying value?

Group Headquarters

In addition to the three operating divisions, M plc also has a head office, based in the UK, which is the group's corporate headquarters where the Board of Directors is located. The main role of M plc's headquarters is to develop and administer its policies and procedures as well as to deal with its group corporate affairs.

€3 May 08 conglomerate value.

Mission statement

M plc established a simple mission statement in 2005. This drove the initiative to acquire FR in 2008 and remains a driving force for the company. M plc's mission is "to be the best news media organisation in Europe, providing quality reporting and information on European and world-wide events".

Before smartphones + tablets

*Expensive
clashes*

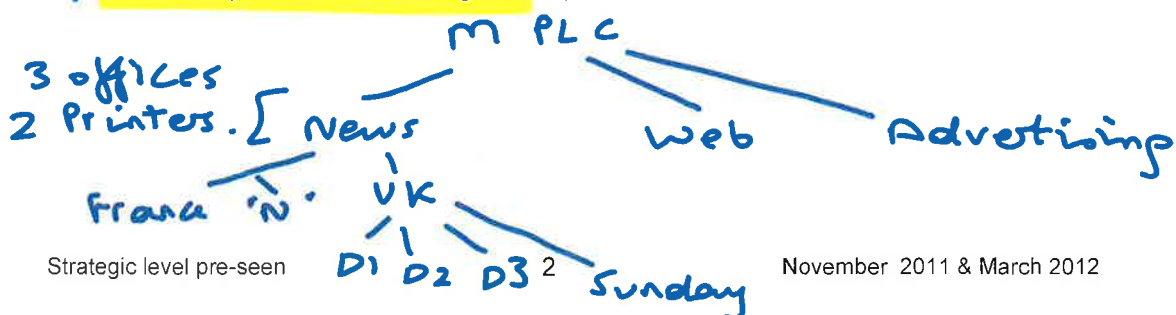
with strat. objective #4

Strategic objectives

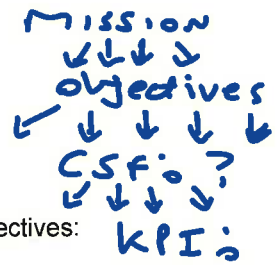
Four main strategic objectives were established in 2005 by M plc's Board of Directors. These are to:

1. Meet the needs of readers for reliable and well informed news.
2. Expand the geographical spread of M plc's output to reach as many potential newspaper and website readers as possible.
3. Publish some newspapers which help meet the needs of native English speakers who live in countries which do not have English as their first language.
4. Increase advertising income so that the group moves towards offering as many news titles as possible free of charge to the public.

Expats



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Financial objectives

In meeting these strategic objectives, M plc has developed the following financial objectives:

Need Cash

- i. To ensure that revenue and operating profit grow by an average of 4% per year.
- ii. To achieve steady growth in dividend per share. *no info*
- iii. To maintain gearing below 40%, where gearing is calculated as debt/(debt plus equity) based on the market value of equity and the book value of debt.

not given unit share price > £2.68

Forecast revenue and operating profit

M plc's forecast revenue and net operating profit for the year ending 31 March 2012 are £280 million and £73 million respectively.

Actuals may be lower? ∴ GAP ANALYSIS

Extracts from M plc's forecast income statement for the year ending 31 March 2012 and forecast statement of financial position as at 31 March 2012 are shown in the appendix.

Gives projected P/E of 8.633

Comparative divisional performance and headquarters financial information

The following information is provided showing the revenue generated, the operating profit achieved and the capital employed for each division and the operating costs incurred and capital employed in M plc's headquarters. This information covers the last two years and also gives a forecast for the year ending 31 March 2012. All M plc's revenue is earned by the three divisions.

Mail = 168, News 142

News Intl 9% Margin

Newspapers Division

	Year ended 31.3.2010 £million	Year ended 31.3.2011 £million	Forecast for year ending 31.3.2012 £million
Revenue external	91	94	94
Revenue internal transfers	90	91	96
Net operating profit	45	46	48
Non-current assets	420	490	548
Net current assets	4	8	(10)
Margin	24.9%	24.9%	25.3%

Can't give up

Cover price Ads.

growth 4%

*Approx £94000 per title per day
44 / 170 = 26% Margin in UK*

Web Division

	Year ended 31.3.2010 £million	Year ended 31.3.2011 £million	Forecast for year ending 31.3.2012 £million
Revenue internal transfers	55	60	66
Net operating profit	10	13	16
Non-current assets	37	40	43
Net current assets	1	1	(2)

18% = (N+W)

25% N+W

Advertising Division

	Year ended 31.3.2010 £million	Year ended 31.3.2011 £million	Forecast for year ending 31.3.2012 £million
Revenue external	162	180	186
Internal transfers	(145)	(151)	(162)
Net operating profit	10	18	19
Non-current assets	3	6	7
Net current assets	1	1	(2)

from customer to News + web

Keep 29 costs 11

Keep 24 costs 5! Error?

Headquarters

	Year ended 31.3.2010 £million	Year ended 31.3.2011 £million	Forecast for year ending 31.3.2012 £million
Operating costs	8	9	10
Non-current assets	37	39	43
Net current assets	1	1	(1)

Total revenue

Op. profit Margin

	31.3.2010	31.3.2011	31.3.2012
Total revenue	253	274	280
Op. profit	57	68	73
Margin	22.5%	24.8%	26.1%
Head Office as % of profit	8/65 = 12.3%	9/77 = 11.7%	10/83 = 12%

*280 - 1 = 279
279 - 57 = 222
222 / 83 = 2.67
280 - 1 = 279
279 - 73 = 206
206 / 83 = 2.48*

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Notes:

1. The Advertising Division remits advertising revenue to both the Newspapers and Web Divisions after deducting its own commission.
2. The Web Division's entire revenue is generated from advertising.
3. The revenues and operating profits shown for the Newspapers Division include those earned by FR and N. The converted revenue and operating profit from N are forecast to be £20 million and £4 million respectively for the year ending 31 March 2012. FR is forecast to make a small operating profit in the year ending 31 March 2012. The Board of M plc is disappointed with the profit FR has achieved.

2012
 ...
 less than U.K. sell off? close?

Additional information on each of M plc's divisions

Newspapers Division

FR is wholly owned and was acquired in 2008. Its financial statements are translated into British pounds and consolidated into M plc's group accounts and included within the Newspaper Division's results for internal reporting purposes.

unlikely to succeed

Shortly after it was acquired by M plc, FR launched a pan-European weekly newspaper. This newspaper, which is written in English, is produced in France and then distributed throughout Europe. M plc's board thought that this newspaper would become very popular because it provides a snapshot of the week's news, focused particularly on European issues but viewed from a British perspective. Sales have, however, been disappointing.

European folded very quickly

N, which publishes local newspapers in its home Eastern European country, is also treated as part of the Newspapers Division. M plc acquired 80% of its equity in 2010. At that time, M plc's board thought that Eastern Europe was a growing market for newspapers. The subsidiary has proved to be profitable mainly because local production costs are lower than those in the UK relative to the selling prices.

Print more in N?

Buy NCI? Value N?

Ethics? Control?

The Newspapers Division's journalists incur a high level of expenses in order to carry out their duties. The overall level of expenses claimed by the journalists has been ignored by M plc in previous years because it has been viewed as a necessary cost of running the business. However, these expenses have risen significantly in recent years and have attracted the attention of M plc's internal audit department.

There has been significant capital investment in the Newspapers Division since 2009/10. The printing press facilities at each of the two printing sites have been modernised. These modernisations have improved the quality of output and have enabled improved levels of efficiency to be achieved in order to meet the increasing workloads demanded in the last two years. Surveys carried out before and after the modernisation have indicated higher levels of customer satisfaction with the improved quality of printing.

All done?

The increased mechanisation and efficiency has reduced costs and led to a reduction in the number of employees required to operate the printing presses. This has led to some dissatisfaction among the divisional staff. Staff in the other divisions have been unaffected by the discontent in the Newspapers Division. Staff turnover has been relatively static across the three divisions, with the exception of the department which operates the printing presses in the Newspapers Division where some redundancies have occurred due to fewer staff being required since the modernisation.

Margins only up very slightly
 Journalism other cards

Web Division

The web versions of the newspapers are shorter versions of the printed ones. There is currently no charge for access to the web versions of the newspapers. Revenues are generated from sales by the Advertising Division of advertising space on the web pages. Some of the websites permit unsolicited comments from the public to be posted on them and they have proved to be very popular. The Web Division is undertaking a review of all its costs, particularly those relating to energy, employees and website development.

Opportunity: full versions + charge

Opportunity 'top table' type site

Ethicality, Legality Govt. reputation of press.

sell off some? Change Management?

Payback

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NPV on new system?

full e-commerce ability to take Mico payments secretly + easily

May be given BCG?

The Web Division's management accounting is not sophisticated: for example, although it reports monthly on the Division's revenue and profitability, it cannot disaggregate costs so as to produce monthly results for each of the 200 websites. The Division is at a similar disadvantage as regards strategic management accounting as it lacks information about the websites' market share and growth rates. This has not mattered in the past as M plc was content that the Web Division has always been profitable. However, one of M plc's directors, the Business Development Director (see below under The Board of Directors and group shareholding) thinks that the Web Division could increase its profitability considerably and wants to undertake a review of its 200 websites.

Mail group do this.

Advertising Division

The Advertising Division remits advertising revenue to both the Newspapers and Web Divisions after deducting its own commission. In addition, the Advertising Division offers an advertising service to corporate clients. Such services include television and radio advertising and poster campaigns on bill boards. Advertisements are also placed in newspapers and magazines which are not produced by M plc, if the client so wishes. An increasing element of the work undertaken by the Advertising Division is in providing pop-up advertisements on websites.

May need Strat. control or Strat. planning

Planning process

Financial control, may not be appropriate given interdependency of divisions

Each division carries out its own planning process. The Newspapers Division operates a rational model and prepares annual plans which it presents to M plc's board for approval. The Web Division takes advantage of opportunities as they arise and is operating in a growth market, unlike the other two divisions. Its planning approach might best be described as one of logical incrementalism. Increased capital expenditure in 2010/11 helped the Advertising Division to achieve an 11% increase in revenue in that year. The Divisional Managers of both the Web Division and the Advertising Division are keen to develop their businesses and are considering growth options including converting their businesses into outsource service providers to M plc.

May not be best at reading

No I.T No Mktg.

The Board of Directors and group shareholding

Free wheeling opportunism. Need dissection?

M plc's Board of Directors comprises six executive directors and six non-executive directors, one of whom is the Non-executive Chairman. The executive directors are the Chief Executive, and the Directors of Strategy, Corporate Affairs, Finance, Human Resources and Business Development. The Business Development Director did not work for M plc in 2005 and so had no part in drafting the strategic objectives. She thinks that objective number four has become outdated as it does not reflect current day practice. The Business Development Director has a great deal of experience working with subscription-based websites and this was one of the main reasons M plc recruited her in March 2011. Her previous experience also incorporated the management of product portfolios including product development and portfolio rationalisation.

Break up group?

Need to keep her

There are divisional managing directors for each of the three divisions who are not board members but report directly to the Chief Executive.

How do board keep tabs on these people? Too many reports to CEO?

One of M plc's non-executive directors was appointed at the insistence of the bank which holds 10% of M plc's shares. Another was appointed by a private charity which owns a further 10% of the shares in M plc. The charity represents the interests of print workers and provides long-term care to retired print workers and their dependents. Two other non-executive directors were appointed by a financial institution which owns 20% of the shares in M plc. The remaining 60% of shares are held by private investors. The board members between them hold 5% of the shares in issue. None of the other private investors holds more than 70,000 of the total 140 million shares in issue.

40%

It has become clear that there is some tension between the board members. Four of the non-executive directors, those appointed by the bank, the charity and the financial institution, have had disagreements with the other board members. They are dissatisfied with the rate of growth and profitability of the company and wish to see more positive action to secure M plc's financial objectives.

Some board members feel that the newspapers market is declining because fewer people can make time to read printed publications. Some of the non-executive directors think that many people are more likely to watch a television news channel than read a newspaper.

Diversify into buying TV channel

Govt may not allow it ← e.g. FOX?

Compliance based = Do Minimum

Lack of control Govt regulation?

Editorial policy

M plc's board applies a policy of editorial freedom provided that the published material is within the law and is accurate. The editors of each of the publications printed in the UK and France and of the websites have complete autonomy over what is published. They are also responsible for adhering to regulatory constraints and voluntary industry codes of practice relating to articles and photographs which might be considered offensive by some readers.

Lead To Greiner's summary N of W Crisis ceased to exist

There is less scrutiny of the accuracy of the reporting in N's home country than in other countries. The Eastern European country in which N is situated has become politically unstable in the last two years. Much of this unrest is fuelled by the public distaste for the perceived blatant corruption and bribery which is endemic within the country's Government and business community. It is well known that journalists have accepted bribes to present only the

Ethics.

Government's version of events, rather than a balanced view. There is also widespread plagiarism of published material by the country's newspapers and copyright laws are simply ignored.

Corporate Social Responsibility

Too Old Too little

A policy is in place throughout M plc in order to eliminate bribery and corruption among staff especially those who have front line responsibility for obtaining business. This policy was established 15 years ago. All new employees are made aware of the policy and other staff policies and procedures during their induction. The Director of Human Resources has confidence in the procedures applied by his staff at induction and is proud that no action has ever been brought against an employee of M plc for breach of the bribery and corruption policy.

Luck?

M plc is trying to reduce its carbon footprint and is in the process of developing policies to limit its energy consumption, reduce the mileage travelled by its staff and source environmentally friendly supplies of paper for its printing presses. The Newspapers Division purchases the paper it uses for printing newspapers from a supplier in a Scandinavian country. This paper is purchased because it provides a satisfactory level of quality at a relatively cheap price. The Scandinavian country from which the paper is sourced is not the same country in which N is situated.

Not doing enough

No clear Strategy

Strategic Development

The Board of Directors is now reviewing M plc's competitive position. The Board of Directors is under pressure from the non-executive directors appointed by the bank, the charity and the financial institution (which between them own 40% of the shares in M plc), to devise a strategic plan before June 2012 which is aimed at achieving M plc's stated financial objectives.

Dividends? Gearing? News growth < 4% revenue + op. margin Less concerned with strat. objectives.

Extracts from M plc's forecast group income statement and forecast statement of financial position

Forecast income statement for the group for the year ending 31 March 2012

	Notes	£ million (GBP million)
Revenue		280
Operating costs		(207)
Net operating profit		73
Interest income		1
Finance costs		(11)
Corporate income tax	1	(19)
FORECAST PROFIT FOR THE YEAR		44

Interest cover 6.7x
 where from?
 4.42 x 250m
 Mail div, = 328 + P.A.T.

Forecast statement of the group financial position as at 31 March 2012

	£ million (GBP million)
ASSETS	
Non-current assets	641
Current assets	
Inventories	2
Trade and other receivables	27
Cash and cash equivalents	2
Total current assets	31
Total assets	672

Deprn going forward may exceed capex
 ∴ Cash generation exceeds profit
 rec. days = 35

EQUITY AND LIABILITIES

Equity		
Share capital	2	140
Share premium		35
Retained earnings		185
Non-controlling interest		16
Total equity		376

Non-current liabilities		
Long term borrowings		250
Current liabilities		
Trade and other payables		46
Total current liabilities		46
Total liabilities		296
Total equity and liabilities		672

C.R = 0.75
 ∴ Need cash
 payable days = $\frac{46}{207} \times 365 = 81$ days high?
 Ratio of 0.4
 Need Equity of 375
 ∴ Share price = £2.68

Notes:

- The corporate income tax rate can be assumed to be 30%.
- There are 140 million £1 shares currently in issue.
- The long-term borrowings include £83 million of loan capital which is due for repayment on 1 May 2013 and the remainder is due for repayment on 1 April 2019.

Re-registered: should be easy
 End of Pre-seen Material
 May cost 4.42

