Sri Dharmasthala Manjunatheshwara
College of Business Management, Mangalore
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MBAH 502

Third Semester M.B.A. Degree Examination, April/May 2024
BUSINESS ADMINISTRATION
Strategic Cost Management

Time : 3 Hours Max. Marks : 70

SECTION – A

Answer **any two** questions. **Each** question carries **10** marks. Answer to the questions should **not** exceed **six** pages. **(2×10=20)**

1. What is meant by Strategic Cost Analysis ? Explain how it is prepared, implemented and monitored.
2. What is Transfer Price ? Explain the benefits and the methods of fixing transfer price.
3. Describe the concept of Responsibility Centre ? Explain the importance of different types of Responsibility Centres.

SECTION – B

Answer **any three** questions. **Each** question carries **12** marks. Answer to the questions should **not** exceed **six** pages. **(3×12=36)**

4. A company manufactures MP3 players. It is planning to introduce a new model and development will begin very soon. The new product is expected to have a life of 3 years. You are given the following data.

	Year 0	Year 1	Year 2	Year 3
Units Manufactured and sold		25,000	1,00,000	75,000
Price per unit (₹)		90	80	70
R & D costs (₹)	8,50,000	90,000	–	–
Production Costs (₹)				
Variable cost per unit		30	25	25
Fixed costs		5,00,000	5,00,000	5,00,000
Marketing Costs (₹)				
Variable cost per unit		5	4	3
Fixed costs		3,00,000	2,00,000	2,00,000
Distribution Costs (₹)				
Variable cost per unit		1	1	1
Fixed costs		1,90,000	1,90,000	1,90,000

a) Calculate the Life-Cycle Operating profit of the firm.

b) The company plans to offer a discount of 10% to the customer which is expected to increase the sales by 5%. Would you recommend the introduction of such discount ? Give reasons.

P.T.O.

5. X Ltd. has decided to analyse the profitability of its five new customers. It buys bottled water at ₹ 90 per case and sells to retail customers at a list price of ₹ 105 per case. The data pertaining to five customers are :

	Customers				
	A	B	C	D	E
Cases sold	4000	20000	136000	72000	90000
List selling price (₹)	105	105	105	105	105
Actual selling price (₹)	105	104.50	99	102.40	95.20
No. of purchase orders	15	20	30	25	35
No. of customer visits	2	3	6	2	4
No. of deliveries	10	30	60	40	20
Kilometers travelled per delivery	20	6	5	10	30
No. of expedited deliveries	0	0	0	0	1

Its five activities and their cost drivers are

Activity	**Cost Driver Rate**
Order taking	₹ 750 per purchase order
Customer visits	₹ 600 per customer visits
Deliveries	₹ 5.75 per delivery Km travelled
Product handing	₹ 3.75 per case sold
Expedited deliveries	₹ 2250 per expedited delivery

Required :

a) Compute the customer-level operating income of each office retail customers now being examined. Comment on the results.

b) What insights are gained by reporting both the list selling price and the actual selling price for each customer ?

c) What factors X Ltd. should consider in deciding whether to drop one or more of the five customers ?

6. What is meant by Balanced Score Card ? Explain the benefits and different perspectives of Balanced Score Card.

7. AML Ltd. is engaged in production of 3 types of ice cream products - Coco, Strawberry and Vanilla. The company presently sells 50,000 units of Coco @ ₹ 25 per unit, strawberry 20,000 units @ ₹ 20 per unit and vanilla 60,000 units @ ₹ 15 per unit. The demand is sensitive to selling price and it has been observed that every reduction of ₹ 1 per unit in selling price, increases the demand for each product by 10% to the previous levels. The company has the production capacity of 60,500 units of Coco, 24,200 units of strawberry and 72,600 units of vanilla. The company marks up 25% on cost of the product. The company management decides to apply ABC Analysis. For this purpose it identifies 4 activities and rates as follows.

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Activity	**Cost Rate**
Ordering	₹ 800 per purchase order
Delivery	₹ 700 per delivery
Shelf-stocking	₹ 199 per hour
Customer support and assistance	₹ 1.1 per unit sold

The other relevant information for the products is as follows.

Particulars	**Coco**	**Strawberry**	**Vanilla**
Direct material per unit (₹)	8	6	5
Direct labour per unit (₹)	5	4	3
No. of purchase orders	35	30	15
No. of deliveries	12	66	48
Shelf stocking hours	130	150	160

a) Calculate target cost for each product after a reduction of selling price required to achieve the sales equal to the production capacity.

b) Calculate the unit cost of each product at the maximum level using ABC.

c) Compare the cost of each product and comment on it.

8. ABC Ltd. has prepared a flexible budget for the coming quarter. The following information is provided from the same.

Production Capacity	40%	60%	80%	100%
Direct Wages	24,000	32,000	40,000	48,000
Direct Materials	12,000	18,000	24,000	30,000
Production Overhead (fixed & variable)	12,600	13,800	15,000	16,200
Administrative overheads (fixed & variable)	6,200	6,600	7,000	7,200
Selling & Distribution Overheads (fixed & variable)	6,800	7,400	8,000	8,600
Total cost	**61,600**	**77,800**	**94,000**	**1,10,200**

However, due to recession, the company will have to operate at 50% capacity in the coming quarter. Selling price has to be lowered to an uneconomical level, and the expected sales revenue for the coming quarter will be ₹ 49,500. But it is projected that in the next quarter, following the coming quarter, the concern will operate at 70% capacity and generate a sales revenue of ₹ 90,000.

The management is considering a suggestion to keep the operation suspended in the coming quarter and restart operation from the next quarter when it is expecting to operate at 70% capacity. If the operation is suspended, it is estimated that :

a) The present fixed cost for the quarter would be reduced to ₹ 11,000.

b) There will be a cost of ₹ 7,500 for closing down the operations.

c) There will be an additional maintenance cost of ₹ 24,000 for quarter.

d) There would be an one time cost of ₹ 20,000 in reopening the plant. You are required to advise whether the factory should be kept operational during the coming quarter and also what will be the profit at 70% capacity utilization level ?

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SECTION – C
(Compulsory) **(1×14=14)**

9. Bombay Steel Ltd. manufactures 4 products, namely A, B, C and D using the same plant and process. The following information relates to a particular period.

Product	Volume	Material Cost per unit (₹)	Direct Labour per unit	Machine Time per unit	Labour Cost per unit (₹)
A	500	5	1/2 hour	1/4 hour	3
B	5000	5	1/2 hour	1/4 hour	3
C	600	16	2 hours	1 hour	12
D	7000	17	1½ hour	1½ hour	9

Total production overhead recovered by the cost accounting system is analyzed under the following headings.

Factory overhead applicable to machine-oriented activity	₹ 7,424
Set up cost	₹ 4,355
Cost of ordering materials	₹ 1,920
Handling materials	₹ 7,580
Administration for spare parts	₹ 8,600

These overhead costs are absorbed by products on a machine hour rate of 4.80 per hour giving an overhead cost per product of :

A) ₹ 1.20 B) ₹ 1.20 C) ₹ 4.80 D) ₹ 7.20

However, investigation into the production overhead activities for the period reveals the following totals.

Product	No. of set ups	No. of material orders	No. of times material was handled	No. of spare parts
A	1	1	2	2
B	6	4	10	5
C	2	1	3	1
D	8	4	12	4

You are required :

i. To compute an overhead cost per product using ABC, tracing overheads to production units by means of cost drivers.

ii. To comment briefly on the differences disclosed between overheads traced by the present system and those traced by ABC.