



Institute of Certified Management Accountants of Sri Lanka
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November 2020 Examination

Apex Level
ICS – 501 Integrative Case Study
Scenario I

No. of Pages: 11

Scenario I

WHOLESOME CAKES AND CONFECTIONARIES COMPANY LTD (WCCL)

Birth of an Entrepreneur

The origins of 'Wholesome Cakes and Confectionaries Ltd (WCCL)' can be traced back to 2006, when Sandra Madanayake, the daughter of a millionaire businessman Lucas Madanayake opened a small cake shop selling a limited, range of exclusive, homemade cakes.

Leaving school immediately after her advanced level, Sandra showed an acute interest in commencing a course in culinary education and was quick to discover her talent in this field with a special interest towards confectionaries. Having earned a higher diploma from a prestigious French culinary school with a distinction, she was determined to convert her talent and passion into entrepreneurship, a subject that also formed part of her curriculum. Since she is not interested to join her family business in transport, she persuaded her father to provide a pathway to a small business that became a reality with the opening of her own shop in 2006 at the tender age of twenty. Conveniently located, bordering Thurston Road, 'Wholesome Cakes', the cake shops of Sandra, offering homemade oven fresh cakes, soon became a popular destination, particularly for cake lovers. It also gained popularity for its 'take away' gift packs containing an assortment of four large pieces out of her then product range consisting of a piece each of Ribbon, Love, Juggery and Fruit and Nut cakes attractively packed for takeaway. The equipment for the cake shop comprised all brands of British origin that Sandra carefully selected while her visits to London during her stay in France and some of the main ingredients for cake making was also imported from reputed foreign suppliers.

Having started modestly by simply partitioning their large residence in 2006, with the growth of the business and increasing popularity, in 2010 the current place of business was newly constructed. The new design clearly separated segregating a part of their palatial residence that happens to be the ancestral home of Madanayake family. The shop was appended with an air-conditioned mini restaurant where customers can relax and enjoy some short eats (outsourced from Sandra's network of friends) and tea/coffee in an ambience of luxury and comfort. Sandra with an entrepreneurial passion and future ambitions, the business premises was well planned and constructed. It included space for future expansion in the form a larger cake making facility to house further equipment, some parking and storing capacity. Along with this expansion, a pastry chef of with foreign exposure and expertise was recruited as Sandra was planning for her

next phase of her life cycle both professionally and personally. The idea of this high-profile recruitment was not only the delegation of management of the WCCL but further expansion of the company's operations. In the year 2011 Sandra married Saman, an engineer by profession who was working as the factory manager in one of the large manufacturing companies. He also has adequate all-round exposure to business not only being born to a family engaged in construction but having pursued a post graduate diploma in Finance and Marketing from a recognized business school in USA.

Family dynamics in family businesses

Lucas the eldest of the Madanayake family, consisting of him and the two elder sisters enjoyed the control of finances of the Madanayake family. The sisters who are married to specialist medical Doctors have been abroad for some time working in Africa.

With the death of their father in 2016, arrival of the two sisters of Lucas to Sri Lanka for permanent settlement brought in an era of tension and anxiety in Madanayake family. As a result of this development in the family dynamics, family wealth ultimately had to be divided and was distributed. Even though Lucas Madanayake was entrusted with all family resources up to that point, his stake was restricted to the transport business including the fleet of vehicles plus that section of the ancestral residence (now converted to the business premises of WCCL) . It was compromised that one of the sisters was given the balance part of the ancestral home and also the sisters sharing the balance wealth. These developments severely restricted the spending power of Lucas's family as they had to invest in a residence for Sandra and the family, that also included a comfortable fully fledged annex for Lucas. A part of the money for this acquisition was financed out of a working capital loan for the transport business and for this purpose the vehicle fleet was revalued. To raise this loan the divided part of the ancestral home's business premises was also mortgaged. These unexpected hardships made Lucas to carefully evaluate the functioning of the two business ventures of his two children. By this time Sandra's elder brother also was running his shop of branded sports goods imported from two reputed principals, a venture that was also financed by his father. The financial analysis and appraisal of the functioning of these two ventures were carried out with the assistance of an accounting friend of Lucas. This examination clearly depicted losses in their respective business operations that were not quite evident as infusion of capital, whenever called for was not a problem for a man of Lucas's affluence who also adopted a carefree lifestyle. With the cycle of fortune taking an adverse turn of events it was very necessary some remedial measures were taken. Lucas decided to discuss his findings with his son-in law and seek his point of view and advice as well.

When Saman was called upon assist, advise and assume leadership of Sandra's business, he was quick to understand the symptoms of the problems confronting his wife's business venture. Saman's analysis showed that, simply Sandra was providing exquisite quality at a higher price compared to available competitive products of the competitive retail market. However due to high cost of genuine raw materials and inadequate volumes she was not able to achieve a break-even turnover of the ongoing business. It was also observed that the restaurant section was running at a loss due to a variety of reasons. The operational controls in form of efficient inventory and cost management practices too, were not considered adequate due to the absence of clearly defined responsibilities. He was also not fully impressed with the marketing proficiencies, especially in dealing with the institutional sales.

Market for Cakes in Sri Lanka

The pre 77 era of the Sri Lankan economy characterized with restrictive economic policies, meant lesser dynamism and competitive intensity in most industries. Apart from large expensive hotels that too were a mere handful, the two legendary upper middle class restaurants, namely 'Perera & Sons –Bakers to the nation' and 'Green Cabin/Pagoda' that is even currently popular were the two well-known places to buy good quality cakes in Colombo. There was other somewhat second tier Colombo based restaurants by the names 'Bakehouse', 'Isurudisi' etc that supplied cakes for domestic consumption and special events, apart from all wayside restaurants and hotels along main roads of the country where customers could purchase cakes of varying quality levels.

With the advent of the open economic landscape post 1977, the phenomenal growth of restaurant/hotel industry was no exception and hotels, and restaurants of different magnitude, positioning and opulence was quite evident in most parts of the country. By the mid-nineties, in Colombo, some major restaurant chains and cafes serving a range of cake options were in operation. A noteworthy competitor for the two established industry players mentioned in this case study, is FAB that has now become one of the prominent operators in this industry segment. This is another popular company with almost an island wide presence emulating the Perera & Sons, whilst 'Green Cabin' has opted to be a more Colombo and main suburb-based operator. When it comes to serving cakes of very good quality, the relatively late entrant 'Sponge' occupies a distinctive niche from the time it entered the Colombo market by the beginning of the century. Further, continuous emergence of new entrants into the market for cakes positioned towards the high end of the market in the Colombo city of varying levels of quality, has made the industry intensely competitive from the point of view of WCCL. Nevertheless, market for food was also growing with increasing tourism, customer preferences for high quality food items, and growth in white collar incomes and institutional sales.

The beginning of a new era for 'Wholesome Cakes'

Saman, wearing his business hat realized the enormous potential of his wife's competencies in the field of bakery products specializing in the area of 'cakes' embarked in preparing plans for the restructuring and expansion of his wife's family venture in early 2018. Given the enormity of the task at hand, Saman invited a management consultant owning a consulting company a colleague with particular specialty in strategic turnarounds to formally assist the family and bring a desired strategic change.

The concept of customer value and sustaining success

After an initial appraisal of the company affairs from its inception, amongst many discussions and training sessions to impart strategic knowledge by the Consultant to the top management of WCCL, given below is an interesting extract.

"In any successful competitive business, the concept of 'customer value' is at the heart of a company's strategy. Careful understanding and management of this variable is necessary for strategic success in the particular market segments that a company has opted to operate.

Competitively focused organizations always try to align and integrate customer value management with their strategy. Finance function, at the top level, as strategic partners in the company too must be conscious of such knowledge. Even under the popular Balanced Score Card (BSC) approach, customer value and its management is at the centre of the 'customer perspective'. We are well aware that the effective management of the 'customer perspective', is a powerful driver of the 'financial success' and 'shareholder wealth' in organizations.

Please also appreciate the strategic logic and benefits of the below diagram to sharpen your knowledge."

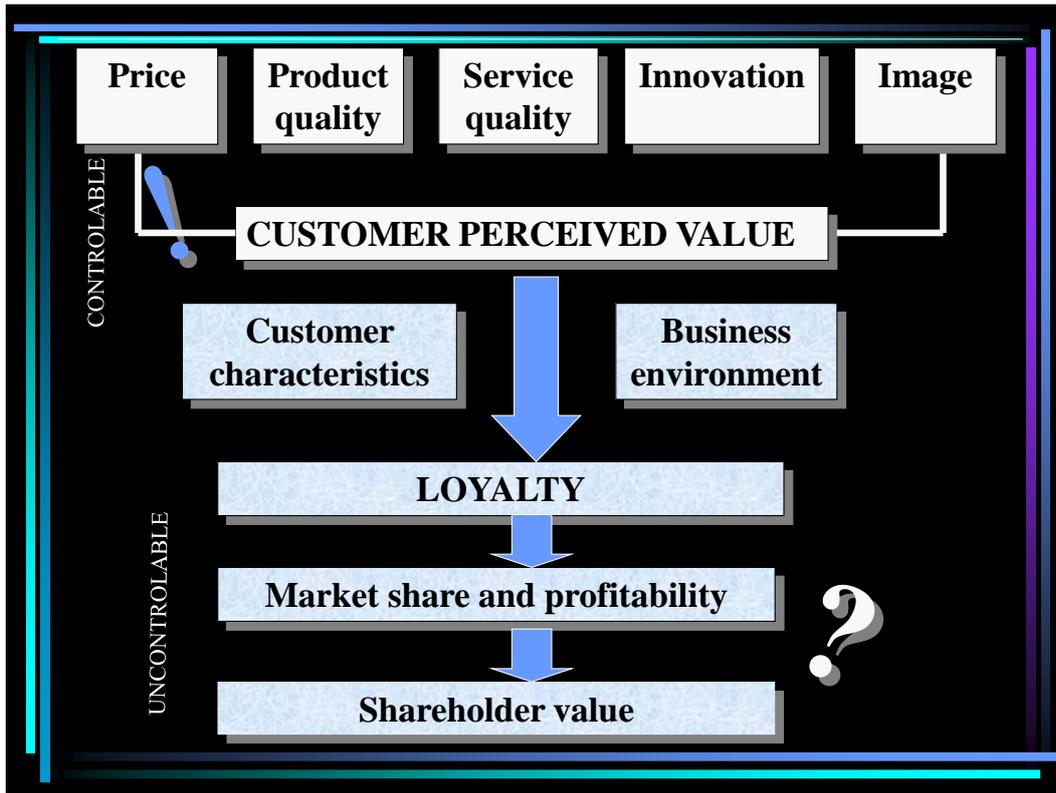


Figure 1 Link between 'Customer Value' and 'Shareholder Value'

(Adapted from: Gale, Bradley T. Managing Customer Value, 1994)

Customer Value is simply the key attributes of quality according to the way the customers in a market segment define it as offered at the right price. Quality includes all non-price attributes that can be conveniently categorized under 'product', 'service' and 'emotional quality'. Quality, value and price are relative. A typical, generic customer value map is given below:

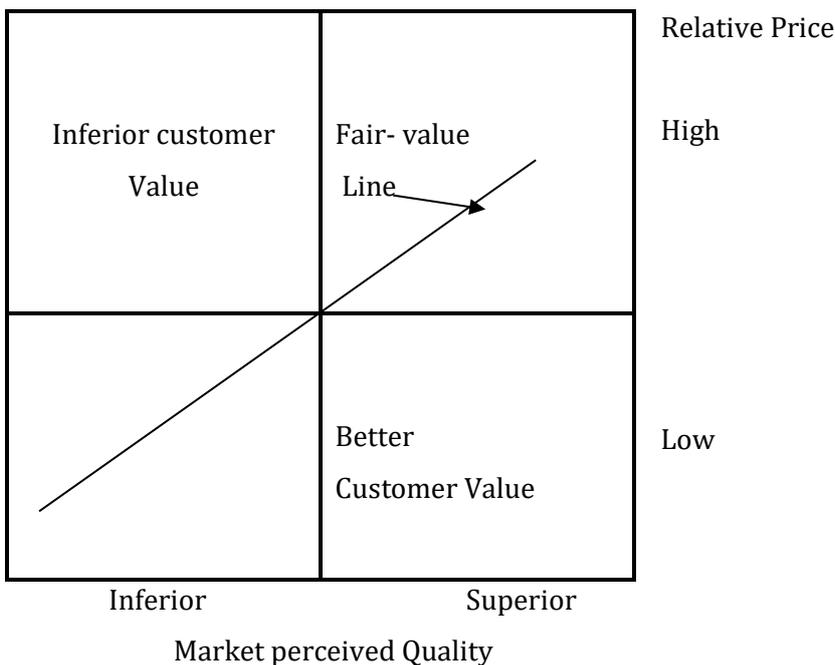


Figure 2- The structure of a typical Customer Value map

Certain Changes/Reorganization decisions

Following were agreed by the top management of WCCL to be included as and included as initiatives of organizational change to be implemented.

- Mini restaurant to be discontinued
- Instead, the space was used to expand the cake sales showroom and cake making facilities, the product range was increased, standardized and rationalized.
- To Critically examine the inventory management function including material planning, stock holding policies and controls
- The following three product groups were created:
 - Group A – (Basic range) Butter, Chocolate, Vanilla, Lemon, and Ribbon
 - Group B – (Value added range) Love, Juggery, Fruit and Nut, Chocolate Fudge
 - Group C - (Special Orders) (for ceremonies such as cakes for Birthdays, Office parties and weddings etc)
- To improve the marketing activities which will increase sales of the company and strengthen the brand image.
- Product Positioning with a strategic emphasis
- Better management of customer value
- To find appropriate strategies for financial restructuring
- Explore creative ways of expanding the business scope

Consulting Company Research of the product positioning of WCCL

As per a research study carried out by the Consulting company of the WCCL’s product offerings, the following ‘customer value map’ was generated.

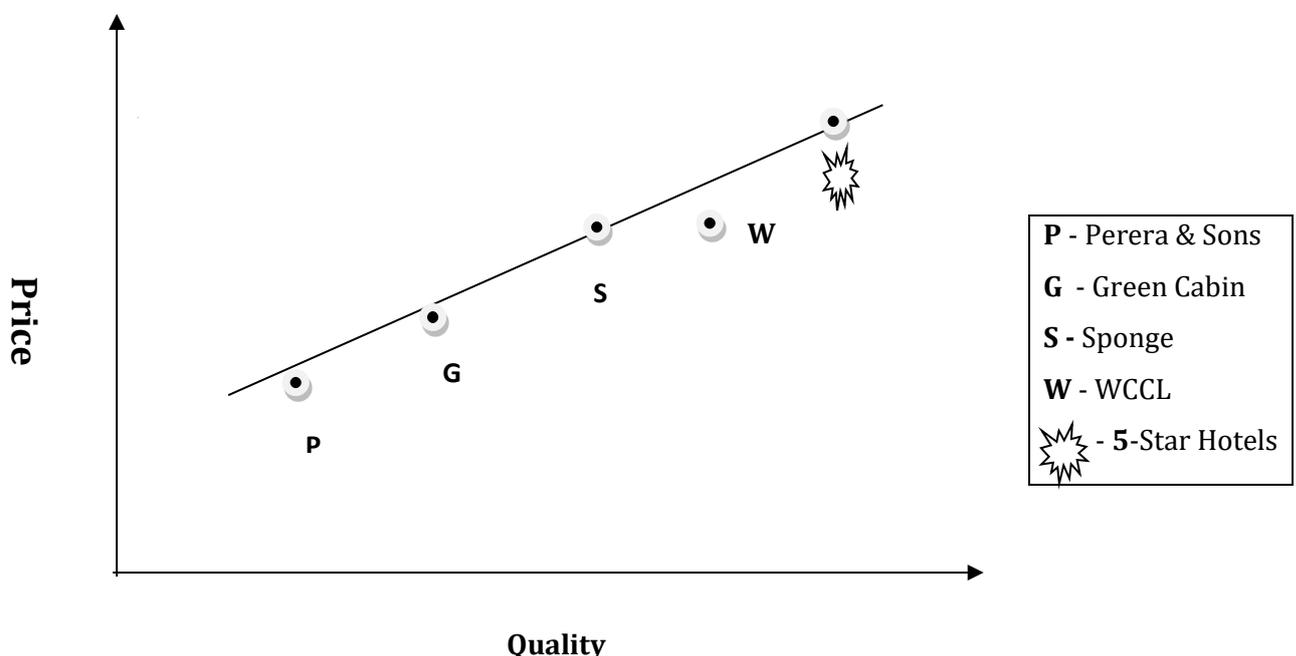


Figure 3 – Consulting Co’s Research finding of the collective Product range, of WCCL ‘s - Customer Value Map

Selected Financial/Cost management information of WCCL

In the field of Finance, the consultant also studied and analyzed the financial accounts, cost management and pricing mechanisms adopted by the company. In particular he was concerned of the cost allocations that have resulted the reported profitability of different product groupings. Accordingly working with the company officials, they arrived at a more realistic basis of allocating costs into different product groupings of WCCL, as depicted under Appendix 2.

Certain Environmental trends

Given the current situation where government has enforced certain restrictions and also increased the tariff of various items of imported raw materials, the board of directors of WCCL is concerned whether such impositions could affect the competitiveness of their product offerings. Another concern in the current environment is corona virus pandemic (Covid-19) and its possible impact on the Bakery industry.

Some of the directors have even expressed concerns and interest over the growing societal trends in health consciousness and growth in incomes of certain customer groups beyond the Western Province. Digital marketing too, seems to be yet another field of contemporary development.

-End of Scenario I-

Appendix 1 - Draft financial results of WCCL for the year ended 31st March 2020

(In regard to the 'product prices' and 'product quantities' given, please note that they are for equivalent 1kg prices and quantities)

Appendix 1

WHOLESOME CAKES AND CONFECTIONARIES COMPANY LTD				
<u>Draft Profit and Loss Statment for the year ended 31st March 2020</u>				
Product Lines /Categories				
	Group A	Group B	Goup C	Total
	(in Rs 000,s)			
Sales	60,000	36,000	20,000	116,000
Cost of Sales				
Raw Materials	30,000	18,000	8,000	56,000
Labour	6,000	3,600	2,000	11,600
Factory Overheads	18,000	9,000	6,000	33,000
	<u>54,000</u>	<u>30,600</u>	<u>16,000</u>	<u>100,600</u>
Gross Profit	6,000	5,400	4,000	15,400
GP Percentages	10%	15%	20%	13%
Administartion Expenses				4,675
Marketing Expenses				400
Finance Expenses				9,800
Net Profit				<u>525</u>

	Group A	Group B	Goup C	Total
	in Rs 000,s			
Sales	60,000	36,000	20,000	116,000
Selling Price	1000/=	2000/=	4000/=	
Quantity Units	60,000	18,000	5,000	

Draft Statement of Financial Position as on 31st March 2020

(in Rs 000,s)

Fixed Assets

Land and Buildings	56,025
Machinery and Equipment	30,100
Furntiure and Fittings	15
	<u>86,140</u>

Current Assets

Raw materials	28,310
Works In Progress	1,803
Finished Goods	1,749
	<u>31,862</u>
	<u>118,002</u>

Current Liabilities

Bank Overdraft	14,500
Private overdraft	9,800
Creditors	4,150
	<u>28,450</u>

Long Term Loan (Private loan)	20,000
Share capital & Reserves	<u>69,552</u>
	<u>118,002</u>

Appendix 2

Factory OH Cost allocations, based on relationships that best represent equitable distribution of effort of activites within different functions , among the three Product categories (expressed as percentages)

Organisational Functions	Value (in Rs 000's)	A %	B %	C %
Material Planning, Ordering,Importing/Purchasing and Store keeping	5,925	20	40	40
Cake factory machinery depreciation and manitenance	3,025	40	30	30
Factory electricity,cleaning and other expenses etc	6,025	40	40	20
Factory Management salaries and benefits	<u>18,025</u>	25	45	30
Total	<u>33,000</u>			

Note 1

-Distribution of the cost behavior of Factory overheads -Fixed and Variable.

-25% of the Factory management salaries and benefits , 25% Cake factory machinery depreciation and maintenance and 75% of Factory electricity,cleaning and other expenses etc -Fixed.

ICS -November - 2020 Examination- Marking Grid					
Evaluation		Weightage	Competency assessment (Marks)		
			High level of application	Middle level of application	Low level of application
Knowledge	Technical knowledge (On Management Accounting, Financial Accounting & Business Management.	30	24-30	8-23	1-7
Application	Application of practical solutions based on the knowledge and skills gained through synthesis, analysis and calculative practices.	20	16-20	6-15	1-5
Integration	Examine a problem/ issue in a holistic sense through drawing from diverse functional disciplines.	15	12-15	4-11	1-3
Prioritization	Demonstrate a rational, balanced outlook supported with evidence to unearth issues and rank them in the order of priority.	15	12-15	4-11	1-3
Decision	Present viable decisions and implementable recommendations.	10	8-10	4-7	1-3
Presentation	Ability to structure answer clearly and legibly in a most appropriate logical sequence. With recommendations and relevant references clearly.	10	8-10	4-7	1-3
TOTAL		100			