

Postgraduate Diploma in Accounting and Finance

Management Accounting

Assignment

Instruction:

- 1. Assignment Due Date: 12 November 2016, Friday before 18:30**
- 2. No plagiarism is allowed**
- 3. Show all workings**
- 4. Required number of words: 2,000 – 2,500
(Excluding references/bibliography, tables, footnotes, etc.)**

Case Study - Good Foods Limited

Good Foods Limited (GF) is a food manufacturer and distributor whose shares are listed on the Hong Kong Stock Exchange's Main Board. One of the operating divisions of GF is the Good Juices (GJ) division, which makes and distributes orange juice. GJ has developed a strong reputation for premium orange juice, having won numerous awards in Hong Kong and throughout Asia. GJ currently produces two brands of orange juice:

| Brand | Principal ingredients | Selling price | Principal customers | Retail Price |
|---------|---|------------------|---|------------------------------------|
| Premium | Squeezed juice from fresh oranges | HK\$10 per litre | Supermarkets, restaurants, bars | 150% to 300% of GJ's selling price |
| Organic | Squeezed juice from fresh organic oranges | HK\$20 per litre | Department stores, hotels, luxury restaurants | 200% to 400% of GJ's selling price |

The original GJ division was a separate company founded by Geoffrey Jin and his family in 1975. In 1991 Geoffrey sold the company to GF. Since 1991 the GJ Division has continued to expand steadily at an average annual growth rate of 5% in revenue.

Geoffrey Jin remained the chairman and managing director of GJ after the acquisition in 1991. Geoffrey has also been an executive director of GF since 1996. In early 2011, Geoffrey entered into his fifth four-year service contract with GJ. It was understood that Geoffrey would retire on 31 December 2015. To recognise his long term service to the company, the directors of GF agreed to award Geoffrey a special bonus of HK\$5,000,000 if GJ is able to maintain the average 5% annual growth rate in revenue and a minimum net profit margin of 12% over the four year period ending 31 December 2015.

Geoffrey Jin has always insisted on using high-quality fresh oranges in the juice products. GJ now sources its oranges from orchards in Guangxi, Jiangxi, Hubei, Hunan and Sichuan provinces. GJ's packaging plant is located in South Mainland China near Hong Kong. GJ's principal market is in Hong Kong.

The management of GF estimates that in the year 2013, GJ will achieve a growth in sales of 4.5% only, although GJ was able to maintain a net profit margin above 12%. After steady growth over the last few years, the management of GF has begun to expect a slowdown in the premium juice market, and is concerned about the achievement of steady growth in the long term.

The management team of GF has put forward a proposal to introduce a high volume, lower cost range of orange juice, the Quality brand, in the selling price range of HK\$5 per litre in the Mainland. The lower cost product will use orange juice concentrate imported from the USA. The new product will be promoted as pure orange juice. Although it is not made by squeezing fresh oranges, the management of GF considers that the Quality brand is a relatively high value added product in the Mainland compared with orange juices supplemented with artificial ingredients. As living standards continue to improve, the management of GF believes that the Quality brand will become attractive to customers in the Mainland.

However, when this proposal was first communicated to Geoffrey in a regular management meeting he had expressed overwhelming concern. He said "This new range has the potential to damage the business and the company's brand name. Moreover, if our products are able to achieve an average net profit margin of 12%, why should we market a product with such a low profit margin? Yes, I agree that the market is already saturated, but why cannot we change the pricing of our more profitable existing products to attract higher sales volume at a lower price, for example by cutting the price of Premium (Family) by 5%. Why do we have to enter into the low-end market in the Mainland and take the risks?"

For the year ending 31 December 2013, the latest estimates for the operating results are as follows:

| | HK\$ |
|----------------------------------|-------------------|
| Sales revenue | 57,600,000 |
| Raw material | 18,240,000 |
| Overhead -wages | 2,000,000 |
| Overhead -depreciation | 3,000,000 |
| Packing costs | 9,450,000 |
| Delivery costs | 2,200,000 |
| Selling costs | 2,880,000 |
| Marketing and promotion expenses | 1,152,000 |
| Administration costs | <u>10,000,000</u> |
| Profit before taxation | 8,678,000 |
| Taxation | <u>1,735,600</u> |
| Net profit | <u>6,942,400</u> |

The latest estimate of the operational data of the existing brands for the year ending 31 December 2013 and operational data for the proposed new brand are as follows:

| | | Organic (Regular) | Premium (Regular) | Premium (Family) | Quality (Family) |
|-------------------------------------|-------------|----------------------|----------------------|---------------------|---------------------|
| Volume per pack | Litre | 0.5 | 0.5 | 1 | 1 |
| Pack per case | Number | 24 | 24 | 12 | 12 |
| Volume per case | Litre | 12 | 12 | 12 | 12 |
| Cases sold in 2013 | | 40,000 | 150,000 | 250,000 | - |
| Selling price in HK\$ | per case | 240 | 120 | 120 | 60 |
| Raw material in HK\$ | per case | 96 | 36 | 36 | 20 |
| Packing costs in HK\$ | per case | 30 | 30 | 15 | 12 |
| Delivery costs in HK\$ | per case | 5 | 5 | 5 | 1 |
| Selling costs in HK\$ | % of sales | 5% | 5% | 5% | 5% |
| Marketing and promotion expenses | % of sales | 2% | 2% | 2% | 2% |
| Taxation | % of profit | 20% | 20% | 20% | 20% |

The production overheads and administration costs are relatively fixed. For financial reporting purposes, the costs are allocated to products on the basis of material costs and revenue respectively. After adjustment for inflation and other factors, the management of GF expects the existing estimated operational data of the products to remain stable for a considerable period.

The management of GF estimates sales of 200,000 cases of the Quality brand in the year ending 31 December 2014 and that the brand can achieve an increase of 20% per annum in sales volume for the years 2015 to 2017 and 10% per annum for 2018 and after. To produce the Quality brand, GJ has to purchase a new mixing and packing system at a cost of HK\$12,000,000 on 1 January 2014. The new machinery should last for 6 years. Both the tax and accounting depreciation are on a straight line basis. Additional promotion expenses for the new brand of HK\$2 million will be incurred in each of the years 2014 and 2015.

Required:**Question 1**

You are a Finance manager at GF. Write a report to the management of GF regarding the new Quality brand. Your report should:

- a) **Identify the type of generic strategy option adopted by GF when it launches the new Quality brand in the Mainland, using any appropriate strategy model and compare it with the existing strategies adopted by GF;**
- b) **Evaluate the appropriateness of the strategy to launch the new Quality brand in the Mainland, using a product life cycle model;**
- c) **Based on 2013's operational estimates, calculate the contribution margins and profitability of the existing brands (Le. Organic, Premium (Regular) and Premium (Family). Explain your calculation where necessary;**
- d) **Evaluate Geoffrey's suggestion to change the pricing of the existing brands;**
- e) **Your calculation of the net present value (some of figures are included in Table) and the payback period of the investment in the new mixing and packaging machine; and**
- f) **Explain your recommendation on the proposed launching of the new Quality brand and the matters to which you would alert the management.**

Table A

| | <u>2014</u> | <u>2015</u> | <u>2016</u> | <u>2017</u> | <u>2018</u> | <u>2019</u> |
|-------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|
| | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 | \$'000 |
| Sales revenue | 12,000 | 14,400 | 17,280 | 20,736 | 22,810 | 25,091 |
| Production costs | 6,600 | 7,920 | 9,504 | 11,405 | 12,545 | 13,800 |
| Additional wages | 500 | 500 | 500 | 500 | 500 | 500 |
| Selling and marketing costs | 840 | 1,008 | 1,210 | 1,452 | 1,597 | 1,756 |
| Additional promotion expenses | 2,000 | 2,000 | - | - | - | - |
| Discount factor | 0.870 | 0.757 | 0.658 | 0.572 | 0.497 | 0.432 |

GF is subject to income tax at a rate of 20%, payable at year end, and is entitled to tax depreciation allowance.

Question 2

Based on the new Quality brand's contribution to GJ's net profit for 2014 and 2015, explain your views on the principal reason for Geoffrey's strong reaction to the introduction of the new brand. From the perspective of professional ethics, do you consider Geoffrey's reaction appropriate? How would you advise the management of GF to resolve this issue?

Report Format:Title Page

Include a title page that provides the title of the report, the author's name, the date it was written or presented, and the organisation or department for which it was written.

Table of Contents

Create a table of contents that gives page numbers for the different sections of your report. Include page numbers for subheadings of main sections as well. Table of contents is optional and could be used for a longer report.

Summary

Summarise your report. This will be the first main section of your report. It is an executive summary or abstract that highlights the problem and steps to solve it. Summaries are generally about a page in length, and they give the reader a general overview of what is in the report. If you conducted a survey or experiment, include your research questions, methods, and outcomes.

Introduction

Write an introduction. The introduction demonstrates to your audience why the problem is important. It presents the problem or situation in clear, concise language. The introduction also includes a short statement on how the problem should be solved, or why or how the problem was created. It quickly conveys the crux of the report in one to two sentences.

Fact Findings and Analysis

Divide the body of the report into sections. The body of the report offers greater detail of the problem, and it provides some background to it. It also gives some in-depth analysis that goes beyond merely describing the problem to identifying different aspects of the problem and drawing connections between them.

Divide the body of the report into headings and subheadings to help the reader understand the flow of the report. Keep the headlines short, capitalizing the first letter of each main word in the headline. For example, you could divide the body into "Problem," "Background," and "Analysis" sections.

Conclusion and Recommendations

Draw conclusions at the end of the report. Your conclusion section is where you will offer suggestions of how to solve the problem or answer the questions posed in the report. You can create a separate "Action Steps" or "Suggestions" section. Provide ideas of how to move forward with the problem, and help the reader understand why it is important in a broader sense. Make your audience members care about the problem on a wider scale by telling them how this problem relates to them personally and why your solutions are the best way to solve it.

Reference, Bibliography and Appendices

Cite your sources. External references and bibliography and internal produced appendices used to support ideas should be cited at the end of your report.

House style

Reports are required...

- To be in black ink on white
- To be in **Times New Roman** typeface, point size 12 for the text
- To be in size 16 in **bold** for the title
- To have line spacing of 1 line
- To use no other fonts or font sizes
- Not to employ clipart or similar illustrations
- To include a central header to show the title 'Narrative Reporting'
- To have headers and footers in Times New Roman typeface, size point 8
- To show the word count as Appendix 1
- To be fully referenced, including full web browser addresses used and other information of sources
- To use hanging indent for the references list (in MS Office - Paragraph/indents/special/hanging, similar in other applications)

Some basics

Structuring your essay

Use sub-headings based on a few themes. This will help you to organise your work while you are working, enabling you to produce a better structure and logical flow to your argument.

Students who do well in the essay...

- *Read LOTS of articles!*
- *Start writing EARLY, organising their work into different themes as they go along*
- *THE AREA OF YOUR ESSAY must follow the requirements given, not a different one! A good test is to ask a friend if he or she can guess the title/topic of your work after reading any page*
- *Re-read and edit their work on a regular basis to ensure the work is well structured and not repetitive*
- *Avoid using double citations (Smith, 2000; cited in Brown, 1997) as a way of getting round the number of articles to be used. Students should generally aim to use only the primary source of information in an article, rather than other references found by the author.*

This coursework is designed to be an extended independent research based essay equating to a mini-dissertation. It is therefore expected that you will evaluate your own work over the months in order to improve it. This means **reading, re-reading, and revising your work**. Your ideas and your writing will be much better if you work on your assignment for a short time each week rather than work for long periods of time towards the end of term. This is because you will unconsciously think about your work in between sessions, so that each time you come back to it you will be able to look at your work with a fresh pair of eyes.

Submission Guidelines

- Wordcount excludes references (bibliography), footnotes, appendices and diagrams. There will be a 10% penalty for work that over- or under-exceeds the limit by 10% (wordcount to be included as Appendix 1).
- A good answer will...
 - *Take a mainly analytical approach to the material (i.e. a largely descriptive piece of work will not receive good marks)*
 - *Produce a meaningful and valid conclusion based on the evidence you have evaluated*
- You will lose marks for the following reasons...
 - *The requirements are not addressed properly or in full*
 - *Reliance on textbooks or too many references from the same article*
 - *Insufficient use of good-quality journals (at least 10)*
 - *Poorly thought out arguments, badly presented and, or structured*
 - *Limited conclusions*

Tips for success

- You will need to write and re-write. Your first few drafts will almost certainly not be of a sufficiently high standard to pass. Be prepared to write more than you will end up using in order to end up with a good quality piece of work
- **Do not use the first person ('I')** - This is an exercise in your ability to synthesise material from various sources and evaluate them in relation to the requirements. Your personal opinion is not required!
- **Use the spell-checker and grammar-checker before you submit, or ask someone to proof-read your work.**
- Do not waste time using fancy graphics. They will not earn you any additional marks, and will not compensate for a poorly drafted essay.
- Finally, before submitting your work you should read carefully the marking criteria shown on the next page in order to satisfy yourself that you have done everything necessary to obtain the mark that you require.

Indicative Marking Criteria

| | |
|------------|---|
| 80% + | <p>Clear structure, and critical analysis and evaluation. A thorough understanding of the key concepts in the study. Address the questions directly.</p> <p>Good flow and clear writing style</p> <p>Excellent communication</p> |
| 70% - 79% | <p>Sound structure, critical analysis and evaluation</p> <p>Fluent use of concepts</p> <p>Address the question</p> <p>Evidence of background reading</p> <p>Clear communication</p> |
| 60% - 69% | <p>Structured and evidence of understanding</p> <p>Address most aspects of the question</p> <p>Some evidence of background reading fully referenced</p> <p>Most material relevant to the question</p> <p>Communicate in a satisfactory manner</p> |
| 50% - 59% | <p>Poor structure but an understanding of the basics is evident</p> <p>Too descriptive to approach, lacking relevant analysis</p> <p>Too little evidence of background research</p> <p>Communication meets assessment requirements</p> |
| Fail – 49% | <p>Lacking structure</p> <p>Does not address the assignment's requirements</p> <p>Little evidence of reading</p> |

Sources of Reference:

Reference Books

- Kaplan Publishing - ACCA F5 Performance Management Complete Text
- BPP Publishing - ACCA F5 Performance Management Complete Text
- Management Accounting for Business, Colin Drury, South-Western Cengage Learning
- Cost and Management Accounting: an introduction, Colin Drury, Thomson
- Management and Cost Accounting, Charles T. Horngren, Prentice Hall
- Cost Accounting: a managerial emphasis, Charles T. Horngren, Prentice Hall

Professional Journals

- The Association of Chartered Certified Accountants
- Chartered Institute of Management Accountants