PROFESSIONAL LEVEL EXAMINATION

DECEMBER 2016

Mock Exam 2

BUSINESS STRATEGY

ANSWERS

1

Marking guide

		Knowledge	Skill	Marks Maximum
1.1	Competitive forces in UK printing industry	3	8	10
1.2	Performance of PP	–	17	15
1.3	Draft letter	3	5	8
1.4	Strategic review			
	Break-even price	2	2	
	Factors in closing section	–	9	
				12
		8	41	45

1.1 **Power of suppliers**

Where suppliers are powerful then the prices of inputs can be forced upwards, thereby squeezing industry profits.

The key external suppliers to the printing industry are paper manufacturers as this makes up half of the variable operating costs (assuming that PP is typical of the industry).

The fact that paper manufacturers 'tend to be large, highly mechanised companies' means that the industry is concentrated, and that they have significant size and power by comparison to all but the largest printing companies (eg, the 'few very large printing companies [which] generate annual revenues in the range £100 million to £500 million').

This may indicate that paper manufacturers have significant power over smaller printing companies to negotiate high prices and extract profits from the printing industry. The fact that the increase in transportation and energy costs incurred by paper companies appears to have been passed on in full to printing companies in the form of a 15% increase in paper prices appears to support the proposition that paper companies supplying the print industry have significant power.

There are however other factors which would affect the power of the paper companies:

- Given the size of the European paper industry there is a sufficient number of suppliers, at over 50, for there to be competition, despite needing to export to the UK and incur distribution costs. However, they may act in unison to pass on cost increases, particularly where they are systemic across the paper industry (eg, energy costs)
- The paper manufacturers are reliant on the printing industry as a major customer group and thus their power is reduced as they may have few other industries to sell their output to other than print companies
- The suppliers' product is a major cost for printers. There may therefore be greater resistance to paper price increases by printers as paper costs are a significant factor in determining profitability

- There is low differentiation between different suppliers' paper products as it is like a commodity, so switching is fairly easy for printers, thereby lowering the power of suppliers
- In a recession, there may be surplus production capacity for paper producers, thereby increasing the power of printers
- Ecological concerns mean the overall level of demand for paper is contracting, thereby further increasing the power of printers

Other suppliers to the printing industry may also need to be considered (eg, machinery, land and buildings) but these are more generic and more information would be needed.

Threat of substitutes

Substitutes are alternative products that can perform similar functions to those supplied by the industry in question.

The ready availability of close substitutes limits the demand and the price for the outputs of the printing industry. This drives down industry profits.

The most obvious substitute for printed output is electronic communication which may be provided and distributed more easily than printed materials and can have additional features (eg, sound, real time updates, variations). This will limit the prices that consumers are willing to pay for traditional printed material, but may also increase the demands made from the format of printed output. It has been increasingly easy for consumers to switch to electronic communications as the internet has become more available in portable form, more sophisticated and more flexible. The variable cost of providing and distributing electronic communications is also extremely low.

Power of customers

The greater the power of customers the more they can put downward pressure on prices and reduce the UK printing industry's added value. The following factors are relevant:

- There are many printers in the industry (almost 14,000). While there may be differences of quality and service there are many choices available to customers so switching costs are likely to be low, giving customers' significant power over printers to negotiate price.
- There is significant variation in the size of printers (from very small to almost £500 million revenues) and in customers (from governments and large companies to individuals) so it is difficult to generalise about the effects of the relative size of customers on the printing industry other than to note that it is likely to vary significantly in various sectors of the industry.
- Purchases of printing services may represent a material part of some customers' costs (eg publishers) but a low proportion of other customers' costs. Again therefore there may be variation in resistance to industry price increases by customers.

Overall, industry profits are driven down by the power of some major customers and by their sensitivity to price increases.

Threat of entry

Threat of entry means that where companies can easily enter a profitable industry then high industry profitability can be competed away by increased supply and increased competitiveness.

A factor increasing the threat of entry is that the industry has relatively low differentiation of output and service (other than the digital or lithographic distinction) making switching to new entrants easier, as there may be little brand loyalty given the degree of commonality.

The low initial capital cost of digital printing makes the barriers to entry low in this sector, although they may be higher in the lithographic sector of the market where the costs of entry are greater. The required skills to operate the machinery are likely to provide some additional barriers initially.

The barriers to entry for litho printing are much greater partly because of the high initial capital cost but also because of the ongoing fixed operating costs arising from long print runs.

Other factors decreasing the threat of entry:

- Low prices and losses in the market at the moment provide disincentives to entry
- Customer loyalty reduces switching

Overall, the entry barriers might appear to be low as there are disincentives to entry. Indeed the key question currently appears to be barriers to exit, rather than barriers to entry.

There is, however, a key distinction between the UK industry and the UK market. There may be low barriers to entry into the UK industry, but the barriers to the UK market are even lower when there can be imports from low-cost overseas producers, particularly the large scale, efficient printing companies located in developing economies.

Competitive rivalry

Factors increasing competition:

- There are exit barriers where fixed costs are high or machinery is highly specialised. This may be true of the lithographic sector of the industry, but the fact that 'approximately 16% of UK printing companies ceased to trade in 20X1' and that these were small companies is indicative that exit barriers are low for smaller digital printers.
- Industry demand has fallen, which means there is slack capacity, thereby increasing competition amongst existing companies for a reduced total market.
- Some of the printing companies are large, with economies of scale enabling them to compete strongly compared to smaller companies.

1.2

	20X0	20X1	20X2 (6 months)
Increase in printing revenue (annualised)		4.07%	6.25%
Change in variable operating costs (annualised)		7.0%	8.9%
Increase/(Decrease) in op profit (annualised)		(12.5%)	14.3%
Op profit %	3.3%	2.7%	2.9%
Revenue per print run £	2,050	1,969	1,700
Op profit per print run £	66.7	53.8	50.0
Revenue per million pages £	37,846	37,647	32,381
Op profit per million pages £	1,231	1,029	952
Paper cost per million pages £	12,154	12,426	10,952
Pages per print run	54,167	52,308	52,500
Revenue per employee (annualised)	82,000	85,333	90,667
Op profit per employee (annualised)	2,667	2,333	2,667
Increase in print runs (annualised)		8.3%	23.0%
Increase in pages (annualised)		4.6%	23.5%
Increase/(decrease) in paper cost per million pages		2.2%	(11.9%)

Overall performance

In assessing performance over the period of 2.5 years there are a number of factors to consider in the case of PP and the information available:

(1) In comparing the reporting periods the final period is only six months so the data needs to be annualised to make valid comparisons. The processes of annualisation makes no assumption about what will actually happen in the second half of 20X2, it is merely an arithmetic adjustment of a short accounting period in order to make a like-for-like comparison with an annual accounting period.

(2) There have been two random and exogenous events in the final two periods – one favourable and the other unfavourable – being the Anniversary Games and the increase in paper prices. In order to assess underlying performance it is necessary to attempt to view the performance in the absence of these events, or at least separately identify the contribution of these events, so a better notion of sustainable performance can be ascertained.

Tutorial note

Performance appraisal involves not just explaining what has happened, but how it has happened and why it has occurred. A fuller explanation may also require identification of when events occurred in order to isolate their effect to sub-periods.

Printing revenues

Annualised printing revenues were £2.4 million in 20X0, a period during which there was no benefit from the Anniversary Games. These revenues increased by 4.07% in 20X1 and 6.25% (annualised) in the half year to 30 June 20X2.

The increases may have been due to increases in sales volumes, perhaps in part arising from the Anniversary Games which will not be sustained. Similarly the additional temporary demand in the industry may have meant that sales prices could be increased.

An alternative explanation for possible sales price increases is that there was a common increase in costs in the industry from increases in paper prices and some, or all, of this has been passed on to customers in the same way as paper manufacturers have passed on their cost increases to their customers in the printing industry. This explanation is consistent with the increase in variable costs and the decrease (from 20X0 though not 20X1) in net margin for PP despite the increased revenue.

In testing these propositions, the data indicates that there has been an increase in volumes both in terms of the number of print runs (8.3% in 20X1 and 23% in 20X2 annualised) and the number of pages printed (4.6% in 20X1 and 23.5% in 20X2 annualised).

As the increase in volumes exceeds the increase in revenue we see that revenue per print run and revenue per million pages have fallen. This may imply decreasing sales prices, but as the number of pages per print run has fallen in 20X1 compared to 20X0, it could also imply a change in product mix with a higher proportion of small print runs being taken on.

The data on revenue per employee reflects the fact that the increases in volumes and in sales revenues have been achieved with a workforce of constant size, thus demonstrating improved efficiency per employee.

Operating profit and costs

Operating profit fell in 20X1 compared to 20X0 (down 12.5%) but then recovered substantially in 20X2 (up 14.3%) when the data is annualised.

In 20X1 variable operating costs increased by 7% which is higher than the increase in revenue and, as a consequence, operating profit fell, despite the increase in revenue. To explain this increase, there are two key factors: the increase in volumes produced and the significant increase in paper prices. The price increase occurred 'at the beginning of 20X1' so in identifying when this factor occurred it can be assumed that the cost of paper was higher for almost all the year.

Despite the increase in paper costs of 15% by suppliers, the cost of paper used only increased by 2.2% per million pages in 20X1 compared to 20X0. In the six months to the end of June 20X2 the cost of paper per million pages actually decreased by 11.9%. This needs further investigation but possible reasons might be: purchasing poorer quality paper, less wastage, reduction in average size per page.

Estimating the impact of the paper cost increase, in order to isolate the effect, the following calculation can be carried out which takes into account (1) that paper is only 50% of variable costs and (2) that paper rose in price by 15% at the start of 20X1:

	20X0	20X1	20X2 (6 months)
Total revenue	2,460,000	2,560,000	1,360,000
Fixed operating costs	800,000	800,000	400,000
Variable op cost without paper price increase (W)	1,580,000	1,580,000	860,000
Op profit ignoring paper price increase	80,000	180,000	100,000
Annualising 20X2			200,000
% change		125%	11.1%

WORKING

20X0 Unchanged

20X1(£845/1.15) + (£845k) = £1,580,000 (rounded)

20X2(£460k/1.15) + (£460k) = £860,000

Once the paper price increase effect has been stripped out, there is a 125% increase in underlying operating profit in 20X1. Possible explanations are:

- Variable costs have decreased despite increases in volumes. This may be due to:
  - Smaller print runs (eg Anniversary Games) or increased efficiency
  - Paper cost increases for PP may have been lower than the industry average
  - Use of opening inventory (eg if paper cost increase had been foreseen by PP and inventories accumulated at the previous cost levels then, particularly on a FIFO basis, this would lower cost of sales in the period)
- Increased revenues

  Excluding the paper price increase (which is uncontrollable) then, subject to the above factors, there has been a significant increase in performance in 20X1 compared to 20X0. The temporary nature of the impact of the Anniversary Games may however mean that this improvement is unsustainable, but no data is available to quantify this effect.

  The improved performance in 20X1 has been sustained in the first half year of 20X2. After eliminating the paper price change, and annualising the 20X2 data, profit improved by 11.1% in 20X2 compared to 20X1. Operating profit increased by 14.3% if there is no adjustment for paper prices.

  Looking at the underlying causes of the improvement in 20X2 there has been an increase in printing revenues of 6.25%, but also an increase in variable costs of 8.9%. The improvement in operating profit therefore means the company has benefited from a reduction in operating gearing. As a consequence, increasing sales volumes generated a high additional contribution and fixed costs remained constant.

  While the Anniversary Games affected both 20X1 and 20X2, it could be an explanation for the improvement in 20X2, as there may have been a greater

impact as the Games approached. However, any improvement in operating profit may have been temporary and unsustainable in the period after the Anniversary Games, when there will be no further exogenous boost to demand.

1.3 Palladium Printing Ltd

Address

11 June 20X2

Dear Admissions Service

PP is pleased to make available to its clients the benefits of the latest variable data printing (VDP) software. We believe that Southern University will benefit particularly from this technology in the printing and distribution of its prospectuses to applicants.

Cost benefits

As you will be aware, your current printing suppliers use large scale lithographic printing. In the past, such a choice has been understandable as this delivered low cost per unit of output for large volume print runs compared to digital printing for comparable output.

However, lithographic printing is inflexible and can only print identical prospectuses, without tailor making to individuals' needs. If a student is only considering two or three courses then he/she only needs a small proportion of the total prospectus. PP's VDP technology enables only the relevant pages to be printed for each student and thus significantly fewer pages can be printed. As a consequence, there are significant cost savings for your university as:

- Paper cost savings enable competitive pricing for our clients
- Recent increased costs of paper magnify this effect
- There will be lower storage and handling costs at the university with smaller physical volumes
- Lower postage costs in sending prospectuses to student applicants
- Lower wastage as there are no unused prospectuses
- No need for short print runs after August to make up for poor initial estimation of quantities each year

Marketing benefits

Our VDP technology enables us to print a different prospectus for every individual applicant. This enables your university to market itself to particular students to maximise the probability that they will select your institution for their future education. The marketing benefits for your university include:

- No irrelevant materials describing courses or issues that the applicant is not interested in.
- Given the reduced size of the prospectus, there is opportunity to provide more detail on relevant courses which would not be practical in a single prospectus covering all courses.

- An opportunity to tailor-make other aspects of the prospectus. For example: highlight selected social activities where the applicant has already indicated that he/she has an interest; overseas or home-based student fees and concerns; accommodation details for non-local students only; gender specific issues.
- Opportunity to personalise each prospectus for each applicant (eg, with their name or some other personal details declared on their application).

Environmental benefits

Many of the university's stakeholders will be aware of environmental issues and the carbon footprint involved in producing large quantities of printed paper. The scaled-down prospectus that could be produced by PP compared to lithograph printing would be a significant response to this concern given the large volumes of paper necessary in producing a prospectus.

Client service benefits

The use of PP's digital printing enables quick turnaround for urgent work and production of supplementary publications to applicants, which is not offered by lithographic printing. If small print runs are required for a small sub-set of applicants, this is also possible using digital printing.

Also, in the past, all prospectuses were printed in one print run. In future, the smaller monthly print runs lend themselves to digital printing, rather than lithographic printing, as the set-up time is lower and short-term adjustments can be made.

Conclusion

PP's digital printing using VDP technology offers a flexible product that can be tailor-made to your needs and avoids producing irrelevant material, thereby reducing paper costs and protecting the environment.

Yours sincerely,

Haraj Harris

H Harris

Marketing Director

Palladium Printing Ltd

1.4 (a) **Price**

The total incremental cost of the contract would be:

[(20,000 +32,000 + 35,000) × £1.60] + (3 × £11,600)	= (87,000 × £1.60) + £34,800
	= £174,000
The average incremental cost per prospectus	= break-even price to the university
	= £174,000/87,000
	= £2

(b) **Graphic design proposed closure**

A firm decision on proposed closure seems difficult to make given the poor financial information available which appears to trace neither costs nor benefits directly to the graphic design function.

In terms of revenues, there appears to be interdependency between graphic design revenues and printing revenues as these services are supplied jointly on all graphic design contracts. PP appears to use an arbitrary rule of thumb of 10% of total contract price. This seems unlikely to be universally applicable and fails to discern a cause and effect relationship.

However, to the extent that revenues, as recognised, are valid, then the graphic design function only appears to be just covering its employee costs (assuming graphic design employees are paid the average for the company) ie:

Average salary	= £600,000/30	= £20,000 pa
Graphic design wages	= 3 × £20,000	= £60,000 pa
Graphic design revenue	= £60,000 pa	

The financial viability of graphic design also depends on the other variable costs created by this function. This excludes the major variable costs of paper (solely used in printing) and wages (already considered) but other variable costs generated by graphic design need to be reviewed.

Even if graphic design does make a loss, there may still be reason to keep it open if other printing work is won based on PP's ability to deliver printing and graphic design together. The closure of graphic design may therefore lead to a lost contribution from printing.

As graphic design is 10% of joint revenues, then the printing revenues generated on joint contracts is £540,000 (9 × £60,000), so joint contract value is £600,000. This is a substantial proportion (23.4% in 20X1) of total revenue which may be put at risk if graphic design is closed.

Conclusion

A better accounting system to identify costs and revenues with the graphic design function is required in order to make a more informed choice on closure. Even then, a good understanding of customer requirements is needed. It may well be that graphic design should remain open as a loss leader given the dependence of a significant amount of printing revenue on contracts requiring graphic design input.

2

Marking guide

		Knowledge	Skill	Marks Maximum
2.1	(a) Value chain diagram	4	3	
	(b) FF value chain and value creation	1	7	
				14
2.2	Factors for FF board consideration	3	8	10
2.3	Market research	3	6	8
		11	24	32

2.1 (a)

Firm infrastructure	One factory, freezer warehouse, 200 shops, founder/main shareholder on board, tight operational and financial controls, low cost minimalist culture				
Technology development	Simple ordering systems, limited inventory control and payables management	Basic, technology, simple automated systems	Own lorries used 24 hours per day		
Human resource management	Limited training (unskilled); employees replaced; minimum wage, strict rules	Limited training; employees replaced; minimum wage, strict rules	Limited training; employees replaced; minimum wage, strict rules		Own staff in shops
Procurement	Bulk buying, low quality, managing supplier relationships, simple payables management	Machines: automated but simple processes	Purchased own lorries		Few receivables (cash sales) so no admin for credit control
Primary activity	Constant amounts delivered, organised by suppliers, simple delivery systems	Simple automated machinery, low cost unskilled labour, small product range	Direct delivery to own shops by own fleet	Collected by customers; no advertising	Health and safety
	Inbound logistics	**Operations**	**Outbound logistics**	**Marketing and sales**	**Service**

(b) A value chain identifies the relationships between the company's resources, activities, functions and processes that link the business together and which create a profit margin. In essence it combines the firm's functional strategies necessary to achieve a business' overall strategy in order to create value.

The value chain can be used to examine linkages between functions and processes, where value can be created using the resources of a business to generate strategic options. Non added value activities can be identified and reduced or eliminated. It can also help identify the cost drivers behind FF's least cost strategy.

The primary activities and functions are those that create value and are directly concerned with providing the product/service. The support activities do not create value of themselves, but they enable the primary activities to take place with maximum efficiency.

FF is pursuing a least cost strategy within Porter's generic activities and should thus focus upon low cost resources to produce a low cost product. This is reflected in the low labour and materials costs on the supply side and operating activities of the value chain and the delivery chain to customers via FF's own shops.

Low cost features are built in throughout the value chain including:

- Automated but simple production processes
- Low cost labour at the minimum wage for production and support staff
- Low cost produce which is mainly imported from Eastern Europe
- Costs of inbound logistics shifted to suppliers
- Small product range so longer production runs
- Efficient distribution system

FF can use the value chain to examine whether all activities (primary and supporting) are contributing to its least cost strategy and hence identify inconsistencies eg if the machinery is old and necessitating increased repair costs with production disruption, thereby reducing margins. In so doing it helps identify FF's source of competitive advantage.

The value chain can also be extended to the whole supply chain to ensure suppliers also contribute to the least cost strategy.

The value chain can assist in identifying further scope for cost reduction eg increase the number of potential suppliers so the company can shop around for the best price or to invest in technology to make for more efficient production.

2.2 Within the Ansoff matrix, the proposed commencement of production and sale of chilled meals is product development (ie same market but a different product).

Favourable factors

- **Higher margins** – chilled foods have higher margins than frozen foods so a similar level of sales will generate more profit.
- **Growing market** – chilled foods is a growing market in the UK, while frozen foods is a declining market. With a small market share, frozen foods could be

seen as a 'dog' product in the BCG matrix, being in the declining phase of the product life cycle. Conversely chilled foods could be seen as a 'question mark' or 'problem child' in the expansion phase of the product life cycle.

- **Common suppliers** – there may be cost savings as the food needed for chilled and frozen meals is similar and thus there are common suppliers and efficiencies.
- **Common customers** – if chilled meals are to be sold through FF shops then there are likely to be common customers and thus common marketing opportunities built on access and reputation.
- **Common production** facilities prior to chilling/freezing are likely to lead to some cost savings through economies of scale.
- **Distribution** – the distribution network from factory to shop is common for frozen and chilled meals. This generates economies of scope. This is particularly the case if FF lorries can be adapted to take both chilled and frozen meals.

Unfavourable factors

- **Capital investment** – there is a risk that, if the venture fails, the realisable value of assets purchased will be low and therefore there is a risk of high exit costs.
- **Core competences** – it is questionable whether the core competences established in frozen meals will be appropriate for the manufacture, distribution, storage and marketing of chilled meals.
- There may be **brand confusion** between a least cost product in frozen food and a high margin chilled product in chilled meals.
- The new storage and distribution technology may not easily transfer to chilled food and it may **displace capacity** for frozen meals whose operating efficiency may suffer.
- **Sales displacement** – if customers buy FF chilled meals, these sales may displace sales of FF frozen meals thereby limiting the benefit of market entry.
- **Competitive market** – although chilled meals is a growing, high margin business at the moment, there is evidence that it is increasingly competitive, with low cost offers available from existing market participants.
- **Floor space displacement** – space in the FF factory and shops, currently occupied for the benefit of frozen foods, may be displaced by chilled meals. This may reduce frozen meals' operating efficiency.
- **Inventory management** may be a much more complex issue given the disparity in shelf life of frozen and chilled products.

2.3 Market research is the systematic gathering, recording and analysing of information about problems relating to marketing of goods and services. Market research therefore involves gathering information about the 4Ps of marketing.

The particular focus of market research for FF is whether there is a demand for the three particular types of ethnic cuisines proposed (ie Polish, Lebanese and Vietnamese cuisines).

In particular, the key objective for market research in this case is to determine the likely volume of customers and the most appropriate prices. Relevant to this objective are the following:

Place: There may be varying demand for the three cuisines in different parts of the UK eg where there is a high Polish population then this type of cuisine may be more popular. This means that any market research is only likely to be valid with respect to a particular location. The idea of assessing a national demand may be too abstract without specific locations and therefore is likely to be largely invalid.

Price: The price that potential customers are willing to pay is clearly a specific objective of the exercise of assessing viability. Again this may vary throughout the UK according to demand and income levels.

Product/service: In this case, there are three separate products so they need to be evaluated separately not as a composite whole. It needs to be considered in terms of the attributes that are likely to generate demand (eg convenience, taste, shelf life, volume). This may vary not just between the three cuisines, but within them, according to cooking styles and regional variations with the three countries.

Promotion: As a new venture, the initial impact of advertising and other promotion on price and demand should be considered.

Market research types

The two broad areas of market research are:

- Desk research
- Field research

Desk research

Desk research is the gathering and analysis of existing or secondary data. This is likely to be of background significance in establishing the characteristics of the potential market identified, but is nevertheless important.

In particular, this might relate to the total size of the market: for the UK; for a particular city; or for the region around a specific FF shop.

Data sources for total market size may include:

- Industry publication of market size and growth of similar ethnic cuisines including prices
- Data on popularity of restaurants selling each of these cuisines (trade magazines). Reviewing comments and discussions made on social media about the different types of cuisine.
- Existence and extent of market for these three cuisines by supermarkets already selling these meals
- Ethnic population and distribution statistics for three relevant groups (government statistical sources)

Field research

Field research involves the collection of new (primary) information direct from respondents. As such it is usually more expensive than desk research and so is only performed if desk research fails to answer all questions asked.

Data sources may include:

- Surveying local supermarkets for volume of sales of ethnic food of these three types or similar types
- Observing prices of ethnic ready made chilled meals
- Questionnaires of existing customers (tastes, volumes, price resistance)
- Questionnaires of local potential customers (tastes, volumes, price resistance)
- Sample tastings for existing customers
- Sample tastings for local potential customers

3

Marking guide

		Knowledge	Skill	Marks Maximum
3.1	Balanced scorecard for KK	4	6	
	Importance of four perspectives	–	4	
	Importance of key performance indicators	–	4	
				16
3.2	Ethical implications	3	4	7
		7	18	23

3.1 **Financial perspective (how does the company look to shareholders?)**

CSF/goals	KPIs
Operating losses (stability)	Changes in operating losses
Revenue (growth)	Revenue growth Revenue from each product
Shareholder value (added value)	Return of capital employed Share price changes
Liquidity (survival)	Operating cash flows Projected cash balances

The recognition that losses will be made in the next few years does not prevent an assessment of the financial perspective in terms of the scale of the losses and how they are changing over time.

For a loss-making company, liquidity is an important financial measure. Liquidity needs to be controlled if the company is to survive a difficult period and return to profitability in the longer run with the new strategy.

Customer perspective (how do customers see the company?)

KK's new business model attempts to present a changed product and a changed brand image. KPIs need to measure whether the company is being successful, over time, in changing customers' perceptions of the company/brand/products. This is particularly the case as the same brand name is being retained. A favourable brand image will lay the foundation for future profitability and sustainable competitive advantage.

Internal business process perspective (what must the company excel at?)

CSF/goals	KPIs
Quality of service	Delivery lead times
Employee utilisation	Productivity per employee
Quality of staff	Training course (number, type) Results from training courses (qualifications, skills attained, new procedures introduced)
Quality of product	Number of returns inward Number of claims on guarantees

Reliance on design does not mean that technology can be ignored. Customers are likely to require acceptable levels of technology (including reliability, quality and durability) even if they do not need the latest features.

Similarly production efficiency is important in terms of labour productivity particularly if cost control is a key element in returning to profit as suggested by the CEO.

Innovation and learning perspective (how to continue to improve and create value?)

CSF/goals	KPIs
Design leadership	Number of design awards Time to develop next generation of design Market recognition (surveys, industry articles, questionnaires)
Employee satisfaction	Staff turnover Staff complaints Employee ideas used
Impact of innovation	% of sales from new designs or products
Technology capability	New features on products – time lag behind first introduction by market leader (compare to two-year target)

The new business model no longer requires the company to achieve technology leadership in the market place. Design leadership is however essential if products are to appeal to customers above rival products. The response to, and consequences of, new designs are therefore vital (financial and non-financial) as this is the new core competence to give competitive advantage.

3.2 Ethics can be viewed at the individual level (Jack) and the corporate level (KK). The consideration here is with respect to KK.

A key ethical issue is that of legality.

This relates not just to whether KK is acting legally, but whether Jack has acted illegally and whether KK will knowingly take advantage of Jack's actions. KK therefore has an ethical obligation to make itself aware of the legality of the actions of its employee, albeit that they occurred before he became an employee.

If Jack has been an independent adviser then he will have been acting under a series of consultancy contracts. Almost certainly these will have contained confidentiality clauses.

Copying of company data therefore seems likely to be in breach of the contract (a civil transgression) but may also be criminal act.

The use of wider knowledge gained seems less likely to be an issue in terms of KPIs, as this is general industry knowledge. Company data is more of an issue as it is specific but probably cannot be remembered without reference to the copied files.

Legal advice should be taken but, if Jack has acted illegally, KK should not benefit from those actions and may consider dismissing Jack.

To the extent that Jack has acted legally, then additional ethical considerations apply. The key ethical principle here is confidentiality and whether, even if there is no legal duty of confidentiality, there is an ethical duty to keep confidential information obtained as part of a private agreement.

In making a decision as to how to act, KK may refer to the Institute of Business Ethics three tests:

- Transparency
- Effect
- Fairness

Transparency – would Jack's consultancy clients mind other people knowing the details of their KPIs and data of achievement? In this case, if the information is private and confidential then transparency may not be appropriate in terms of making files available. General unattributable use of knowledge by Jack however seems implicit and acceptable in any contract.

The other issue of transparency was whether it was known and acceptable to Jack's clients that he copied and retained the files and whether Jack has, or could obtain, any evidence of permission.

Effect – who does the decision affect/hurt?

In this case, the rival companies whose data has been extracted may suffered a comparative disadvantage if Jack reveals not just the data itself but the source of the data. Moreover, it could be argued that KK will obtain an unfair competitive advantage over all rivals by illicitly obtaining better measures of strategic control.

It should be noted that Jack is not asking to benefit by direct payment, but he may hope to benefit indirectly as a more effective employee.

Fairness – would the decision be considered fair by those affected?

The issue for KK is that they are being asked to benefit from confidential information. In the context of business ethics, KK's behaviour, if they accept the information, is to gain an unfair advantage over rivals.

Conclusion

What Jack is offering KK to his employers is access to information that is not otherwise readily available in the public domain and was gained by virtue of confidential agreements.

KK might want to seek advice regarding the legality of such an action.

There does however appear to be a difference between (1) detailed copied file information being made available which appears, without evidence to the contrary, to be a breach of confidentiality and (2) general use of knowledge and experience acquired as an adviser which clients would have perceived Jack would probably use in general terms on other advisory clients.

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