

# Examiner's report

## P5 Advanced Performance Management

### June 2014



#### Introduction

Firstly, we would like to offer our congratulations to all of those candidates who achieved a pass at this diet and our commiserations to those who did not.

In this report, our aim is to indicate areas of good and poor performance with the specific additional purpose of helping future candidates assess what is required of them. We have added comments about potential improvements to examination approach that could be made after the commentary on each specific question.

We will begin with general comments about the approach and then provide a commentary on the specific questions in the examination paper.

#### General Comments

The examination paper comprised two sections, A and B. Section A consisted of one compulsory question for 50 marks in total. Section B consisted of three optional questions for 25 marks each from which candidates were required to answer two questions. The vast majority of candidates attempted their allocation of three questions and there was little evidence of poor time management. There was no clear favourite amongst the section B questions with roughly equal proportions attempting each one.

The advice in past examiner's reports and approach articles does not seem to have been taken up by many candidates and we would strongly advise that candidates use these materials to ensure that they have the right overall attitude to P5, which is intended to lie at a post-graduate level.

As a result, we would offer similar broad comments to past reports. Most examinations require a balance of memory work and evaluation/analysis. As one goes through the levels (say from F2 to F5 to P5) this balance changes, from pure memory to more analysis. Good candidates distinguish themselves by being aware that if they come to this examination expecting to repeat memorised material, they will probably score only between 20% and 30%. However, in addition, at this diet, it was clear that many candidates lacked fundamental knowledge needed at P5. Most worryingly, basic management accounting concepts were clearly not well understood e.g. fixed and variable costs in question 1, comprehending an operating statement in question 4. These are gained at lower levels and must be carried forward into the more advanced levels. Also, there was evidence that many did not have basic knowledge of some of the methods in P5, e.g. value-based management in question 1. Without this knowledge, it is very difficult to score the analysis and evaluation marks since the candidate cannot understand the question subject.

The basis of this examination is analysis and application which then leads to evaluation. The candidate will need a foundation in the techniques of the syllabus but should focus more on evaluation of these techniques and consideration of their usefulness to the given scenario. This is a mindset that can easily be encouraged by attempting past papers as an integral part of the revision process. Candidates need to be aware that performance management is an area which, at an advanced level, is dependent upon situation and environment. A good, professional-level answer will go beyond the mere repetition of how a technique works and focus on relating it to the entity's specific environment. As in previous diets, it was very clear to the marking team that those candidates that had grasped the need for this went on to pass the paper. A common illustration of this fault was present in questions where 'justified recommendations' were sought. Those that chose to use points in the scenario to justify their recommendation scored the marks easily. Also, answers to question 4 on beyond budgeting at a sweet manufacturer (Godel) often seemed to demonstrate a pre-judgement that because going beyond budgeting is considered a 'new' idea that it must be the right one for Godel. They ignored the many indicators in the scenario which suggested that it was a very poor approach for such a company.

In contrast to the December 2013 diet, many candidates at this diet failed to read the requirement properly in some instances, for example; ,



- question 1 (i), asked candidates to ‘Evaluate the current performance report in Appendix 1’ not ‘Evaluate the current performance of Cantor using Appendix 1’; and
- question 1 (v), asked candidates ‘Using the information in the appendices, provide justified recommendations for suitable performance measures to reflect the proposed change in the company’s mission statement’ not ‘provide justified recommendations for suitable performance measures to reflect the company’s mission statement’.

The first of these examples was particularly surprising as this type of question has appeared in past papers such as Question 1 (June 2013, Kolmog) and Question 1 (June 2012, Metis). This issue was commented on in the examiner’s report to these papers. Additionally, the issue is discussed in an article on reading the requirement at P5 (‘Reading the question requirements at paper P5’). Finally, the scenario contained the clear instruction, ‘The CEO has advised you that the board does not require an evaluation of Cantor’s performance.’ This misinterpretation of requirements normally indicates a lack of preparation (practicing past papers, reading examiner’s reports and articles) and/or entering the examination room with an expectation of the questions in the paper. .

### Question One

This 50-mark question was based around a national, listed food and drink retailer, Cantor Group (Cantor). Cantor had two operating subsidiaries, Cafes and Juicey, which were at different stages of development (Cafes was mature and Juicey faster growing). The question began by requiring an evaluation of current reporting at Cantor then a specific question about the balance of fixed and variable elements of the property and staff costs within the group. Next, a move towards value-based management (VBM) was being contemplated and so consideration of the economic value-added of the group followed by an explanation of how VBM could be implemented and what its impact would be on the group. Finally, candidates were asked to recommend measures associated with a change in the company’s mission.

In part (i) for 15 marks, most candidates performed reasonably well. As noted above, there was a number of candidates who provided an irrelevant evaluation of the performance of Cantor. Those that attempted the question asked scored most of the marks associated with such reports in general (e.g. data overload, rounding numbers, lack of narrative). However, fewer scored the marks that were present for appreciating the scenario surrounding Cantor. It was especially surprising that despite comments in previous examiner’s reports, candidates still seem reluctant to use the mission/strategy of the business to evaluate the report. There were many marks left unscored for analysing whether the report does actually report on the achievement of the mission/strategy. Those that scored well in this question considered this point. The other common fault in business reporting of ignoring the readers of the report was also present. The report had three groups of readers (the boards of the group and each subsidiary) and each of these would have different needs for summarisation and depth of detail in the report. Future candidates should be aware that the ability to evaluate the reporting of key management information in a business is an essential skill at P5.

Part (ii) of the question, worth 6 marks, required an assessment of the fixed and variable elements of property and staff costs at Cafes and Juicey and their performance management implications. Most (but unfortunately not all) candidates knew what fixed and variable costs were and had some ability in applying these to the scenario information, however very few showed sensitivity to the performance management aspects of operational gearing. As a result of this a recommendation from the examiner’s report for the last diet is worth repeating, ‘Future candidates should be aware that breakeven and the associated analysis is something that they will be considered to be expert in by the time they reach P5.’

Part (iii) for 9 marks requested an evaluation of the group's economic value-added and justification for any assumptions in the calculation. This question was generally well-done. Most candidates showed an understanding of the adjustments to profit and capital employed that are required for this performance metric. Two areas which demonstrated weak performance though were calculations of WACC, where many could not work out the weighting coefficients from the D/E ratio, nor did they read the question carefully to see that the cost of debt needed an adjustment to be post-tax, and in the selection of the capital employed where the year-end figure was used in error. Finally, another example of not reading the question was apparent as many candidates simply stated the assumptions rather than 'justifying' them as asked in the question.

In part (iv) for 10 marks, candidates were asked to explain how to implement value-based management (VBM) and its impact on the group. The problem for the majority of candidates was lack of knowledge with many vaguely talking of value without an understanding of it in the context of the scenario. The fact that the question had just considered economic value-added ought to have provided a memory jog. There were some candidates that seem to think incorrectly that VBM is ABM, possibly because the last two letters of the acronym are the same.. Those candidates that did show some understanding of VBM often did not apply it sufficiently to the management of Cantor where there were two businesses at different stages of development offering the opportunity to analyse the different drivers of value.

Part (v) considered issues around a proposed change in the mission statement to include the aim 'to provide a fair deal to our employees' and was worth 6 marks. There were a number of points about this requirement that were required to be understood:

1. the requirement asked about the 'change' to the mission statement and so comments about the existing mission statement were irrelevant (maximising shareholder value and customer appeal);
2. the requirement asked for 'justified' recommendations for suitable performance measures and so bullet point lists of every metric that a candidate could remember were of very limited value; and
3. the requirement stated that the answer should use 'the information in the appendices' and therefore, the aim of the question was to test if the candidate could identify suitable justified metrics from the information presented in the appendices. Candidates who just produced lists of employee satisfaction measures that they had come across in other scenarios were not answering the question and again, obtained limited credit.

As has become common, those candidates who had practised writing professional answers prior to the examination performed admirably in the presentation area (4 marks). The markers were looking for suitable report headings, an introduction, a logical structure, signposted by the good use of subheadings in the answer, and a clear, concise style. A conclusion was not required for the 4 marks but if a suitable and substantive one was offered then it was given additional credit.

As in the last diet, the advice to future candidates is to answer the question asked and in particular, that the examining team are trying to help by limiting the scope of a question requirement, so that candidates should look on its specifications as an opportunity to save time and write focussed answers.

## Section B

### Question Two

This 25-mark question covered the impact of a business process re-engineering (BPR) project and the performance management of staff at Booxe, a furniture manufacturer.

Part (a) was worth 6 marks and involved a simple cost-benefit analysis of the BPR project such as might be done in a post-implementation review. There were a number of possible approaches to this question that were given credit. This part was generally well done although many candidates muddled a per annum view of the



cost/benefit with a project lifetime view which left answers difficult to interpret for the markers and might have been confusing for the CEO who had asked such a question.

Part (b) for 11 marks then required that the candidate assess the impact of the BPR project on culture and management information systems. This part was again generally well done. Most candidates realised there were two areas to discuss and split their answers appropriately. It was gratifying to see that a large number took the hints in the scenario to consider how this might link to activity-based approaches and the introduction of an ERPS. The one weakness demonstrated was a simplistic grasp of what 'culture' might be such that many answers did not go beyond discussing the impact on employee motivation.

Part (c) for 8 marks looked for advice on the appraisal system at Booxe. Candidates who performed well in this question usually discussed the purpose of an appraisal system, considered the issues at Booxe and then suggested solutions to the problems identified. Again, those candidates that used the information in the final paragraph of the scenario found some easy marks to score. Those candidates who gave text-book answers to what an ideal appraisal system should be did not score marks as efficiently. Very few candidates seemed to comprehend what the 'balance between control and staff development' might mean in this context. Those candidates that made an effort to analyse these concepts usually picked up the marks available.

Future candidates should prepare to answer questions on the impact of management consultancy techniques mentioned in the P5 syllabus (such as BPR) on other areas of their P5 (such as culture, information systems, control) and not only the strategy of the business.

### **Question Three**

This 25-mark question was based on a joint venture (TandR) between two different companies, Turing and Riemann, for the design and manufacture of wind turbines for electricity generation. The question considered the decision under uncertainty of choosing a design for a new wind turbine and then looked at the performance management issues associated with a joint venture.

Part (a) for 9 marks asked for an analysis of the risk appetites of the two JV partners and then, justified recommendations of the method of choosing between the three design types. This part was generally well done with 8 or 9 marks often scored. It was especially cheering to note that most candidates understood that decision making 'under uncertainty' is different from 'under risk' or else, they realised that the lack of information on probabilities meant that expected values were not an optimal approach. One area for future candidates to note is that the answer needed to be a single recommendation of the method to use not a list of the available ones and they should read the model solution closely to see why the methods were chosen.

Part (b) for 8 marks required the candidates to use the methods recommended in part (a) to evaluate the design choices. Again, this part was usually well done with many candidates scoring full marks. One point for future candidates to note is that the companies involved cannot choose to produce a certain number of units as this is the uncertain factor, so conclusions such as 'Turing should make 2,000 units of the 8MW in order to gain a profit of \$13,300m' are misleading. Tutors may also want to note that although minimax regret was not an optimal choice for method, the correct calculation was given full credit in part (b).

Part (c) for 8 marks required a discussion of problems in managing in a joint venture such as TandR. This part was adequately attempted with many candidates able to identify the problem areas but few could discuss the causes and impacts of these problems in anything other than vague terms. The question called for a 'discussion' which implies that some depth of development of points is expected.

Future candidates should prepare to be examined on scenarios based around the complex structures mentioned in the syllabus.

#### Question Four

This 25-mark question was based on the current and possibly future budgeting systems at a sweet manufacturer, Godel. The candidates were supplied with information about the company and its business environment and also, its operating statement. The company was in a mature market with long-term contracts with its two main customers and very limited scope for innovation or market growth. The strategy therefore was one of cost leadership driven by a command-and-control style of management. Staff were loyal and unambitious for change.

Part (a) for 6 marks required an assessment of the information provided in the operating statement and detailed variances of Godel. Specifically, it called for a comprehension of the operating and planning variances within this context. Most candidates did not know the definitions of operating and planning variances and so those that attempted an answer talked about all the other variances in the Appendix thus avoiding answering the question. The question was a reading and comprehension exercise of one of the basic types of management accounting report and it required no calculations.

Part (b) for 11 marks required an evaluation of the current budgeting system at Godel. Like part a, this part was also inadequately attempted. As in the past, too many candidates only saw the negatives of the existing system and few identified its positives for a traditional company like Godel in a mature market. This then led to a failure to grasp that the budgeting system at Godel was in fact well-fitted to its needs.

Part (c) was worth 8 marks and requested an evaluation of a proposal to move to beyond budgeting at Godel. Most candidates picked up the few marks on offer for a description of the beyond budgeting style. However, many candidates seemed to assume because beyond budgeting was 'new' and the existing approach was 'old/traditional' that the correct answer was to recommend a move to beyond budgeting. This kind of pre-judged answer is a classic mistake in papers at this level. It is vital that candidates can demonstrate their ability to perform an objective evaluation of a situation. Only once this is done should a conclusion be formed. The scenario was loaded to be very much in favour of a simple, traditional approach and the beyond budgeting one would have probably been more time-consuming, more expensive and have generated little value in the circumstances in which Godel found itself.

There are two important lessons for future candidates from this question. They should ensure that they have a working grasp of concepts from F2 and F5. They should not assume that because a technique is new that it is suitable and they must appreciate the particular business scenario of the question.

#### Conclusion

In conclusion, the main messages from this paper for future candidates are:

- Read the question carefully and answer the question requirement that has been set
- Learn the models, theories and terminology including those assumed from previous levels
- Practice application of this knowledge in scenario contexts
- Be prepared to justify all your suggestions using evidence from the scenario - don't just state them