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The Chartered **Governance** Institute

ICSA Qualifying Programme

Development of Strategy

Sample assessment material 2019

Time allowed: 3 hours (plus 15 minutes reading time)

Do not open this examination paper until the presiding officer or an invigilator tells you to.

You must not take this paper out of the examination room.

The examination paper contains **6** questions of which you must attempt **4.** You must attempt **3 questions** in Section A and **1 question** in Section B. The questions in Section A are based on the pre-released case study whereas the questions in Section B are not based on the pre-released case study.

Each question is allocated 25 marks. There are **100 marks** available in total for the paper.

Note: Unless otherwise specified, you should assume that an Act or an organisation referred to in the questions is a UK Act or organisation.

Case study

CHEMSHOP plc

Strategy and structure

CHEMSHIP plc (CHEM)ownsand operatesa chain of 320 pharmacy shops, located in towns within a 150-mile radius of London. The shops are of varying size but employ a consistent business model with each shop having a Manager, who is a qualified pharmacist, one or twoadditional qualified or trainee pharmacists and five to ten shop assistants, as required. In addition to dealing with National Health Service (NHS) prescriptions, the shops stock the normally expected range of health-related items; in a number of the shops the opportunity has been taken in recent years to bring additional facilities to the local community. The group head-office is in Reading (40 miles from London).

The strategy has been to grow the group organically (exploiting opportunities in the communities that it serves). It has grown through further acquisition to the point where the businesshas become a potential target acquisition for a national plc pharmacy group and an initial approach has been made by this group to the Executive Directors of CHEM.

The growth of the group and the core financial performance is illustrated in the graphs below. Competitive advantage has been built through finding and acquiring shop locations where CHEM is the only pharmacy in that area.

CHEM was started privately 25 years ago by eight shareholders, each of whom ran apharmacy. Initial funding was a mixture of equity, shareholder loans and long-term bank debt,with banks also providing working capital facilities as required. Six years ago, the group floated 52% of the shares on the Alternative Investment Market (AIM), each of the eight original shareholders earning equal capital from the sale and each retaining a 6% stake. The ‘market’ shares are held by ten different institutional investor groups, with no dominant holder.

The current Board comprises:

- two non-executive directors (NEDs) appointed by the original shareholders;
- three independent non-executive directors (INEDs), one of whom is the Chair, and;
- two executive directors: the Chief Finance Officer (CFO), Barun Bhatia, and the Chief Executive (CEO), Jen Simpson.

The executive directors, Barun and Jen, have worked well together since the initial public offering(IPO), their different capabilities (finance and leadership respectively) complementing each other well. Head Office staff have noticed a recent increase in tension between them.Governance is seen as a tick-box exercise to satisfy the expectations of AIM market regulations. Board meetings are held quarterly and consist of reports from the CFO and CEO to the other directors. The reports are rarely challenged.

The figures keep moving in the right direction, the group is profitable, and dividends are paid regularly, so the directors believe they are fulfilling their stakeholder accountabilities. The Chair has only infrequent discussions with Jen and has a relaxed attitude at Board meetings.He meets shareholders twice a year and after his latest such meeting commented “the shareholders are happy, there is no need for me tointerfere in the business when all is going so well”.

Operation

The stock held by the shops is controlled from HeadOffice through use of an Electronic Point Of Sale(EPOS) system with daily updates; central ordering from suppliers is automated based upon estimated stock level requirements, but the turnaround time is sometimes slow and deliveries inaccurate with shops receiving the wrong stock. There is very little opportunity for the individual shops to influence day-to-day stockholdings, although they can recommend new items/lines to head office (the time cycle from suggestion to approval and stock-in-shop averages at 12 weeks). Full financial detail is only held by Head Office and basic monthly reports, including only shop volume, turnover and profitability, are issued to the shop managers, despite frequent requests for more detailed weekly reports. The only performance indicators are those included in the annual report and accounts at group level.

Two years ago, following a proposal by Jen, it was agreed that each shop manager could influence their personal earnings by retaining a 10% share of any additional profit or loss that is made in comparison to the standard costing/profitability model issued by Head Office. This has proved highly beneficial to the more competent shop managers within the group but is resented by others. All negotiation with suppliers is theoretically handled by Head Office; shop-floor pricing is guided by Head Office but with the opportunity for the local managers to use their initiative to increase sales of high volume stock and seize other economic opportunities.

The shop managers have started to find different methodsto increase theirproduct offering through local sourcing, entering product as 'goods received' on the EPOS system, often with a lack of clarity, and leaving the administration team at Head Office to sort out the errors in the system. This can raiseprofitability at an individual shop level but causes chaos within the IT system.Barun is concerned about loss of control and visibility.

Technology has traditionally been seen as key to the efficient running of the 'group' and initial investment in this was high relative to income. As shops are acquired or converted, the identical system is implemented to maintain the group system and operational culture. In recent years there has been lack of expenditure on technology and the current system is no longer fit for purpose, with the relatively new customer online ordering system being separate from the main shop EPOS system. Barun has undertaken a review of the options available, has identified a better system, and is finalising a formal proposal for the Board with a substantial up-front cost to the group. He believes the group will start to suffer problems if this is not actioned rapidly.

The major 'cultural' issue at each shop is the control being exerted by Head Office with very rare face-to-face contact; with an annual conference in Reading, attended by the shop managers, the CEO and the CFO. The eightoriginal shareholders no longer have any active role in the business or the shops but expresstheir strong opinions forcefully at shareholder meetings.

Opportunities

The UK government has increased the potential range of services that a qualified UK pharmacist is able to offer to encourage treatment of 'minor' issues outside the NHS. This is seen by Head Office as an opportunity to expand the business model further and they are expecting shop managers to develop this potential. A group of 100 of these managers met recently (without any Head Office involvement) and are preparing a proposal to be presented to the directors that removes control from Head Office and allows more local autonomy.

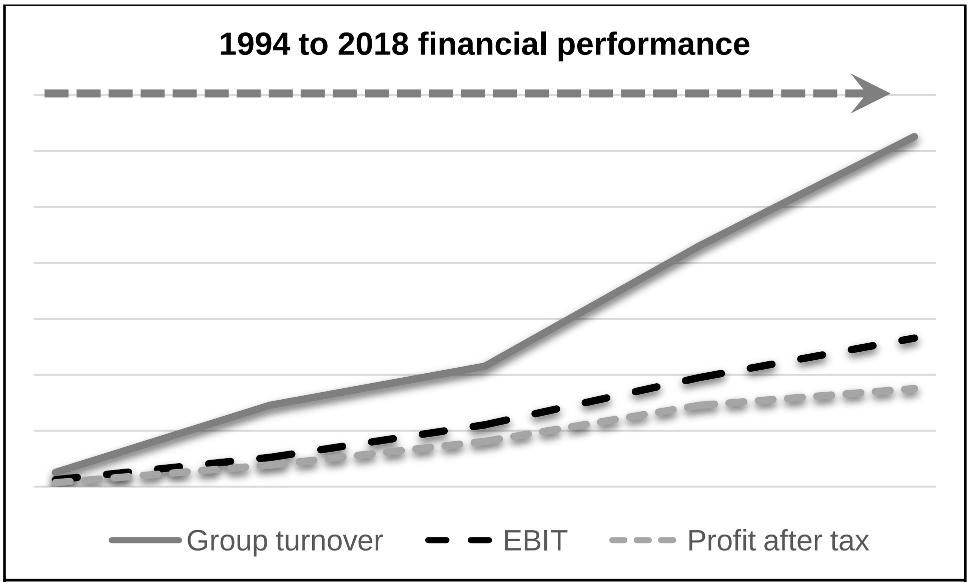
Although she has no experience of overseas operations, Jen has the vision of expanding CHEM internationally. She has identified an opportunity to acquire a private company (MEDI) operating80similar pharmacy shops in Northern France. This group operates a different business model with each shop taking individual responsibility for itsentire business operation, but with the MEDI name being used for funding and marketing of the brand and the shops. MEDI has reached the point where further expansion will require a more uniform supply-chain approach, such as that used by CHEM.

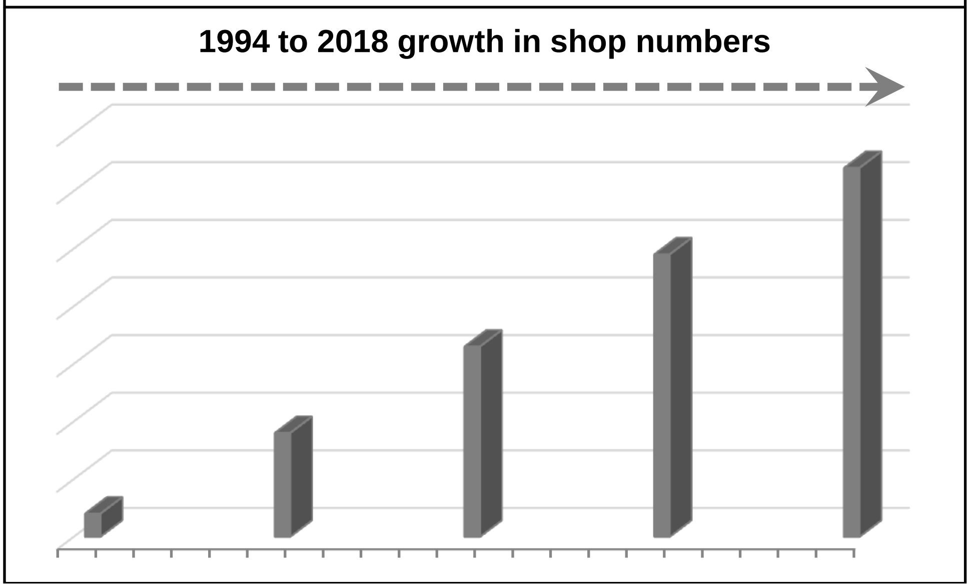
At the CHEM Board meeting last week:

- Jen presented a confidential outline proposal to acquire MEDI through long-term debt (the banks are very supportive).
- The CHEM NEDs were concerned that this was the first they had heard of the plan and at the impact on cashflow, the likely reduction of group dividend payments, and the reaction of the shareholders. Jen suggested that meetings should be set-up to discuss the situation with shop managers and with investors.

- Barun supported the acquisition but stated that cashflow would be managed through a wholesale price increase in each shop, greater central control and removal of the bonus potential from the shop managers.
- The NEDs expressed serious concern at the likely reaction from the existing shop managers, and the potential for reputational damage. They would prefer to maintain the current gradual organic growth of the group within the UK.
- Barun and Jen reveal that they have separately been involved in private conversations with the national plc pharmacy group which is interested in acquiring the CHEM group. It is clear from the discussion that Barun has been encouraging the approach, but that Jen has shown no interest. The NEDs have asked for further details.
- The meeting ended in disagreement, and some acrimony, with an additional Board meeting being called for ten days' time.

Performance





For the financial year ending 31/12/2018:
- Turnover was £625million
- Earnings before Interest and Tax was £265million
- Profit after tax was £175million
- 320 pharmacy shops were operated within the CHEM group

Section A

*Answer**three** questions in this section.*

1. Discuss the difference between organic growth, acquisition, and strategic alliance as alternative strategic pathways, stating the appropriateness of each for the strategic development of CHEM.

[Total for Question 1 = 25 marks]

2. (a) Discuss the relationship between rational and emergent strategy, using the case study to illustrate how and why both are needed.

(15 marks)

(b) Assess how the 'Johari' window could be used to illustrate the communication impact of the strategic changes that are emerging at CHEM.

(10marks)

[Total for Question 2 = 25 marks]

3. Assess the appropriateness of the current organisational structure of CHEM. Recommend to the directors any alternative structures that would align with the evolving strategy of the group.

[Total for Question 3 = 25 marks]

4. The additional CHEM Board meeting has taken place and there is now serious disagreement between Barun, Jen and the NEDs.

- Jen is committed to pursuing the acquisition (of MEDI) despite the lack of overseas knowledge and experience.

- Barun has formally proposed that the IT system be replaced in its entirety as it is causing increasing issues, Jen has argued the money would be better spent on the acquisition.

- The NEDs are concerned at the apparent internal conflicts and why they were not aware of such differences sooner. They are also concerned to keep both of the subjects confidential to avoid any impact upon reputation and share price.

Prepare a paper for the directors analysing the capabilities and competences of CHEM, considering how and why the business appears to have lost strategic focus, including a proposal for a more effective method of control and oversight of the business.

[Total for Question 4 = 25 marks]

TOTAL FOR SECTION A = 75 MARKS

Section B

*Answer **one** question only.Questions 5 and 6 do not relate to the pre-released case study.*

5. (a) Explain why effective leadership is essential to the delivery of strategy.

(13marks)

(b) Assess the strategic role of company directors from the differing perspectives of leadership and governance.

(12marks)

[Total for Question 5 = 25 marks]

6. A large electronic games company has recently established a national charity that collects and redistributes unwanted children's toys and games (physical and electronic). The strategic ethos is that children learn to cope with today's society better through the playing of games. It has established distribution centres alongside existing foodbanks*. Whilst the development is welcome, there is some concern as to the motives of the company.

Evaluate the different stakeholder perspectives for the charity.
Include in your answer, an assessment ofthe benefits that 'stakeholder interaction' can bring to the development of a strategy of Corporate Social Responsibility (CSR), and compare this to the alternative perspectives of 'laissez-faire', 'enlightened self-interest', and 'shaper of society'.

*Foodbanks: places where stocks of food, typically basic provisions and non-perishable items, are supplied free of charge to people in need of assistance.

[Total for Question 6 = 25 marks]

TOTAL FOR SECTION B = 25 MARKS

TOTAL FOR PAPER = 100 MARKS

The scenarios included here are entirely fictional. Any resemblance of the information in the scenarios to real persons or organisations, actual or perceived, is purely coincidental.