



Free Mock: Answer Plan

Strategic Case Study – May & August 2024

Answer Planning Technique

Please refer to the recorded version of Webinar “Answering Technique” for an in-depth guide on answer planning. Visit <https://www.studyattcs.com/product/scs> and check out the “Free Content” tab to access the video tutorial.

Replicate the same technique when practicing the five mock exams & in the real exam.

Steps to follow

1. Read the scenario & reference material: 5 minutes.
2. Reiterate each requirement in your own words. Keep it simple.
3. Develop headings and sub-headings.
 - a. Headings: Bold & Underlined format
 - b. Subheadings: Bold format
4. Develop each answer plan on the answer screen: 25 minutes.
5. Type the final answer. Simply expand the answer plan: 30 minutes.

Reiterating the Requirements

TASK 01

- FA’s comments: Introducing Eco-Intel services (30% = 15 marks)
- Director’s bonus (20% = 10 marks)
- Strategies to manage stakeholder pressure (50% = 25 marks)

TASK 02

- Ethics: Allowing competitors to license Eco-intel software. Alignment to vision, mission & values (50% = 25 marks)
- IA responsibilities: How to secure the source code (50% = 25 marks)

TASK 03

- How to finance IS investments (50% = 25 marks)
- Borrowing \$300m. How to deal with breach of debt covenants. (30% = 15 marks)
- How to manage currency risks (20% = 10 marks)

TASK 01

FA's comment (15 Marks)

- Introducing Eco-Intel services
 - Increased cashflows
 - High dividends can be paid
 - Increased profits
 - High share price
 - Initial cost of introducing EI: High
 - Long run: Costs will decrease
 - Operational efficiencies
 - Additional revs: new customer segment
 - Environmentally conscious customers
 - However, need to monitor additional operational costs: SW integration
 - Increased Beta
 - Current 0.88
 - Stock is relatively less risky at present
 - Attracts risk averse investors
 - Beta increasing: Volatility of shares increases (riskier)
 - Short term: share price might dip
 - Increased ke
 - Long run
 - Reduced risk due to better profits and cashflows
 - Increases market value of Saefwell
 - Eco-conscious appeal: Drives investor interest
 - Enhanced cashflows & profits
 - Risks
 - Systematic/ Market risk
 - Economic downturn, regulatory changes, tech disruptions, political issues, environmental concerns
 - Specific risk
 - Risks of designing, implementing & maintaining EI services
 - Should monitor & control each risk regularly

Director's Bonus (10 Marks)

- Paying Murat a bonus
 - Saefwell recognizes exemplary leadership
 - Handled by the RC
 - NEDs should dominate: we comply
 - Bonus's relevance will be evaluated
 - Increases transparency & fairness of exec. compensation
 - Aligns with SH interests
- Issues
 - Some SHs will question the bonus
 - Execs are already paid well
 - Discontent among other board members
 - Recognizing individual contributions overlooking collective effort
 - To fix issues
 - Develop a communication strategy
 - Explain the rationale behind individual bonuses
 - Explain alignment to corporate goals
 - Review the compensation structure to incentivize teamwork

Managing Stakeholders (25 Marks)

- Identify & manage main stakeholders
 - Advocacy groups
 - High interest low power
 - Can harness the power of the govt
 - Don't negotiate directly
 - Generates additional adverse publicity
 - Use media to engage: Saefwell's narrative
 - Govt
 - High power high interest
 - High interest as per the newspaper article
 - Explain that the law affects other stakeholders adversely as well
 - Engage directly
 - How to change?
 - Lobby
 - Change internal dynamics if needed to fall in line
 - Others: Suppliers & Clients
 - Collaborate to ensure their practices align with Saefwell's privacy standards
 - Ask them to support us change the law
 - Lobby
 - To save livelihoods of employees & investments of SHs
 - Should not be too excessive
 - Competitor (Brotto)
 - High interest. If both companies work together, power increases
 - General
 - Internal investigation: Is the article factual?
 - If yes,
 - Accept fault publicly
 - Inform about steps to mitigate
 - Media & our website

Ethics (25 Marks)

- Sharing source code: Ethical?
 - Source code: Digital asset which drives competitiveness
 - Sharing under controlled conditions
 - Fair & ethical
 - Leads to collective advancements within industry

- Ethical principles
 - Confidentiality
 - Safeguard data and competitive position
 - Releasing source code without safeguards: violates principle
 - To fulfill;
 - Sell IP at a fair price
 - Robust NDAs
 - Sound escrow arrangements
 - Objectivity
 - Fulfilling best interests of SHs & employees
 - Enabling clients to focus on core businesses, without sacrificing Saefwell's competitive edge
 - Higher potential revenues & profits
 - Integrity
 - Being truthful & honest
 - Ensure transparency in decision making
 - Seek inputs from SHs before finalizing contracts

- Mission Vs. Licensing
 - Mission: Provide tailored security solutions
 - Licensing: Aligned with mission
 - Offering operational efficiency
 - Offering a sustainable solution

- Vision Vs. Licensing
 - Vision: Be the most trusted service provider in the sector
 - Licensing: Aligned with vision
 - Establish trust through sharing
 - Responsible sharing of technology
 - Controlling the source code via escrow
 - Reenforce confidentiality via NDAs

- Values Vs. Licensing
 - Value: Responsiveness
 - Sharing tech
 - Sharing sustainability
 - Agile in meeting industry's needs
 - Value: Employee welfare
 - Sharing tech brings new business
 - Job security for staff
 - Opportunities for staff development
 - Upskilling to work with new clients
 - Value: Innovation
 - Sharing tech helps the industry's eco-system
 - Continuous innovations due to knowledge sharing

Internal Audit (25 Marks)

- Risk assessment: Check;
 - Potential vulnerabilities & threats of licensing
 - IP compromises
 - Strength of current security measures
 - Impact & probability of risk
- Review & verify effectiveness of the source code escrow arrangement
 - Credibility checks: escrow service provider
 - Alignment of escrow agreement 's terms with Saefwell's security objectives
 - Definition & enforceability: Source code release conditions
- Review NDAs
 - Structure, content & enforcement capabilities
 - Should cover
 - Confidentiality
 - Unauthorized usage
 - Penalties for breaches
 - Process for monitoring compliance
- Evaluate internal controls: Access to the source code within Saefwell
 - Access rights management
 - Change controls
 - Security of digital & physical storage
- Develop ongoing monitoring plan
 - Oversee security of code post-licensing
 - Regular audits
 - Escrow arrangements
 - Adherence to NDAs & Licensing agreements
 - Mechanisms for detecting unauthorized access/use of the source code
 - Ensure swift responses
 - Mitigate security breaches

TASK 03

Funding Options (25 Marks)

Total investment: C\$ 500 million or B\$ 1,500 million

Escrow Setup & Integration

- Investment: C\$ 300 million or B\$ 900 million
- Options:
 - Long term loan
 - Issuing equity

Raising loan finance

- Opting for loans: Effect on Gearing
 - Pre investment Gearing: 40%
 - Post investment Gearing: 49%
 - Gearing comes close to 50%
 - Saefwell is risky in the eyes of lenders
 - Lenders will charge higher interest rates: Increased finance costs
- Securing a loan of B\$ 900 m
 - Difficult due to the nature of assets acquired
 - Investing on intangible assets like software escrow services
 - Intangible assets cannot be appraised & liquidated easily
 - Bad collateral
 - Setup costs
 - No resale value
 - Bad collateral
- Current debt of Saefwell
 - Higher than PPE
 - Cannot secure additional debt against existing assets

Raising equity finance

- Opting for a rights issue
 - Raising money by selling shares at a discount to existing shareholders
 - Decreases Gearing
 - Success depends on how shareholders are convinced
 - Escrow service: significantly enhances credibility of licensing arrangement
 - Increased long-term value & positive NPVs
 - Easy to convince SHs
- Using retained earnings: B\$ 2,893m
 - No effect on gearing
 - Won't dilute SH's equity
 - Need not convince SHs or lenders

Annual Escrow Management Fee

- Investment: C\$ 200 million or B\$ 600 million
 - Recurring expense
- Financing via working capital
 - No impact on Gearing
 - Saefwell's Net Current Assets: B\$ 353 million
 - Not enough
- Financing via a short-term loan
 - No impact on Gearing
 - Can easily negotiate by presenting cashflow forecasts to lenders
 - Also, the interest cover is 13:1
 - Generates enough operating profits to cover loan interest

Debt Covenants (15 marks)

- Should not violate covenants without approval from creditors
 - Breach of covenants: Immediate return of funds
 - Asset seizures
 - Company dissolution
 - Saefwell can explain the issues of enforcing debt covenants
 - Negative publicity from shutting down the company
 - Liquidating assets might only cover a small portion of outstanding debts
- Borrowing B\$ 900 million: Seek approval from creditors
 - Sign new agreements: consent to modify the existing gearing threshold
 - Pre investment Gearing: 40%
 - Near the ceiling
 - Company has been successful in managing a gearing near the ceiling
- Persuade creditors to ease covenant terms
 - New investment leads to;
 - Increased equity and cashflows
 - Increased revenues
 - Reduced risk of defaults
 - Debt restructuring: Negotiating a loan with more favourable covenant terms
 - Reduced risk of covenant breach
 - Good for creditors
 - Won't lose interest income from early repayment
 - Good for Saefwell
 - No early repayment penalties

Currency Risk (10 Marks)

- Forward Contracts
 - Fixing exchange rates for future C\$ payments
 - Does not irradicate currency risk
 - Yet, offers certainty about future payments made in C\$
- Leading & lagging
 - Timing payments to capitalize on favourable forex movements
 - Paying an advance when the exchange rate is in Saefwell's favour
 - Cesco will prefer early settlements
 - However, Saefwell should consider the opportunity cost of early payments
 - Should monitor forex movements & forecasts to benefit from this strategy
- Communicate chosen plan to shareholders