Skillshort

Self-Study Preparation Pack

CA INTERMEDIATE

Paper 6: Financial Management and Strategic Management

Chapter-wise Detailed Notes

For January 2027 attempt · ICAI BoS study material (new scheme) – Section A FM (50 marks) + Section B SM (50 marks) + RTP January 2027 · Every FM example verified in Python

100 marks · 3 hours | Two sections of 50 | 15 MCQ marks + 35 descriptive each | Q1/Q5 compulsory + any 2 of 3

Contents

How to use these notes	2
Chapter 1 (Section A – FM): Financial Management and Financial Analysis	3
Chapter 2: Financing Decisions and Cost of Capital	4
Chapter 3: Capital Investment and Dividend Decisions	6
Chapter 4: Management of Working Capital	8
Chapter 5 (Section B – SM): Introduction to Strategic Management	9
Chapter 6: Strategic Analysis – External Environment	10
Chapter 7: Strategic Analysis – Internal Environment	11
Chapter 8: Strategic Choices	12
Chapter 9: Strategy Implementation and Evaluation	13
Formula and framework sheet	15
Common mistakes in answers	16

This subject pack has 6 parts

1 Chapter-wise notes

2 Important topics & weightage

3 Past papers: trends & links

4 Mock tests + solutions

5 Chapter practice questions

6 Last-week plan & strategy

Prepared by Skillshort for self-study. Original explanations and questions; not an official ICAI/ICMAI/ICSI publication. Items marked VERIFY should be checked against the latest official material.

How to use these notes

Paper 6 has two independent sections: **Section A – Financial Management** (numerical-heavy) and **Section B – Strategic Management** (case-based theory). Each FM chapter gives the formulas in ICAI notation with a worked example (checked in Python), and each SM chapter gives the frameworks, the lists ICAI asks and how to apply them to a case. Items marked VERIFY should be checked against the latest study material.

File	Use it for
01 Chapter Notes (this file)	Concept building, formulas, frameworks
02 Important Topics & Weightage	What to study first; frequency across 4 recent attempts
03 Past Papers – Trend Analysis & Links	How ICAI asks; official download links
04 Mock Tests 1–2 with Solutions	Full 3-hour practice in the exam pattern
05 Chapter-wise Practice Questions	MCQs + descriptive practice
06 Last-Week Plan & Exam Strategy	Final revision and exam-day plan

Paper at a glance

Item	Section A – FM (50)	Section B – SM (50)
MCQs (15 marks)	8 MCQs (7 × 2 + 1 × 1): a 5-MCQ numerical case + 3 independent	8 MCQs (7 × 2 + 1 × 1): a 5-MCQ caselet + 3 independent
Compulsory	**Q1** – three numerical parts (5 + 5 + 5)	**Q5** – three case parts (5 + 5 + 5)
Choice	**Any 2 of Q2–Q4** (10 each); Q4 is usually **theory** (4 + 4 + 2, with an OR)	**Any 2 of Q6–Q8** (10 each: 5 + 5, sometimes with an OR)
ICAI weightage	I FM and financial analysis **10–15%** · II Financing decisions and cost of capital **45–50%** · III Capital investment and dividend decisions **20–25%** · IV Working capital management **15–20%** VERIFY	Five sections – introduction; external environment; internal environment; strategic choices; implementation and evaluation – **15–25% each**
Skill-wise	Knowledge 20–30%; application 70–80%	Knowledge 30–55%; application 45–70%

Chapter 1 (Section A – FM): Financial Management and Financial Analysis

1.1 Scope and objectives

- **Financial management** – planning, organising, directing and controlling the financial activities: **investment** (capital budgeting, working capital), **financing** (mix of debt and equity) and **dividend** decisions.
- **Objectives: wealth (value) maximisation** – maximising the market value of shares, considering risk and the time value of money – is preferred to **profit maximisation**. Limitations of profit maximisation: vague (which profit?), ignores the **timing** of returns and **risk**, and ignores social responsibility and the quality of earnings.
- **Basic functions:** estimating capital requirements, deciding the capital structure, choosing sources of finance, investing funds, disposal of surplus (dividend vs retention), cash management, financial controls. **Finance executive** today also handles treasury, risk management, investor relations, compliance and digital finance, and is a strategic partner to the CEO.
- **Financial manager vs financial controller:** the manager focuses on funds raising, investment and value creation (forward-looking). The controller focuses on accounting, reporting, internal control and compliance (stewardship).
- **Agency problem** – conflict between shareholders (principals) and managers (agents); reduced by performance-linked pay, ESOPs, monitoring and governance. **Agency costs:** monitoring, bonding, opportunity and structuring costs.

1.2 Ratio analysis

Group	Ratio	Formula
Liquidity	Current ratio	Current assets ÷ current liabilities
	Quick ratio	(CA – inventories – prepaid expenses) ÷ CL
	Cash ratio	(Cash + marketable securities) ÷ CL
Leverage	Debt-equity	Long-term debt ÷ shareholders' equity
	Debt service coverage	Earnings available for debt service ÷ (interest + instalments)
	Interest coverage	EBIT ÷ interest
Activity	Inventory turnover	COGS ÷ average inventory
	Receivables turnover / ACP	Credit sales ÷ average receivables; 360 (or 365) ÷ turnover
	Payables turnover	Credit purchases ÷ average payables
	Fixed asset / capital turnover	Sales ÷ net fixed assets / Sales ÷ capital employed
Profitability	GP, NP, operating ratio	GP ÷ sales; NP ÷ sales; (COGS + operating expenses) ÷ sales
	ROCE	EBIT ÷ capital employed
	ROE	PAT (less preference dividend) ÷ equity shareholders' funds
Market	EPS, P/E, dividend yield, book value	PAT for equity ÷ shares; MPS ÷ EPS; DPS ÷ MPS

DuPont = ROE = Net profit margin × Asset turnover × Equity multiplier (Total assets ÷ Equity)

- **Effect of a transaction on the current ratio:** if the current ratio is **above 1**, paying a current liability **increases** the ratio, while borrowing short-term to buy current assets reduces it. If it is **below 1**, the effects are reversed. For example, at 2 : 1 (CA 4, CL 2), paying 1 of creditors gives 3 : 1, so the ratio improves.
- **Working back:** use the ratios as equations (e.g. CL ₹1,60,000, CR 2.5 → CA ₹4,00,000; QR 2 → quick assets ₹3,20,000 → inventory ₹80,000).
- **Limitations:** based on historical data; different accounting policies; window dressing; price-level changes; ratios are only indicators.

Chapter 2: Financing Decisions and Cost of Capital

2.1 Sources of finance

Type	Sources
Long-term	Equity shares; preference shares; debentures/bonds; term loans from banks and FIs; retained earnings; venture capital; **seed capital assistance**; lease financing; sale and leaseback
Medium/short-term	Working capital loans, cash credit, overdraft; trade credit; commercial paper; bill discounting; factoring; **packing credit** and post-shipment finance for exporters; inter-corporate deposits; public deposits
International	ECBs, ADR/GDR, foreign currency convertible bonds, **masala bonds** (rupee-denominated bonds issued abroad)
Contemporary	**P2P lending**, equity crowdfunding, start-up funding (angel investors, VC), green bonds

- **Seed capital assistance** – for entrepreneurs with technically viable projects but insufficient capital. It is a soft loan with low or no interest and a moratorium, given by IDBI/SIDBI and others for small projects VERIFY.
- **Bond types: callable** (issuer may redeem early – higher coupon), **puttable** (holder may sell back early – lower coupon), **drop-lock** (floating-rate bond that converts automatically to a fixed rate if the benchmark falls to a set level), **zero-coupon** (issued at a discount), **deep-discount**, **junk/high-yield** (low credit rating, so investors demand a higher yield), **green bonds** (proceeds for environmental projects).
- **Debentures are advantageous** when the company has stable earnings, a low existing debt level, a high tax rate (interest is deductible), wants to avoid dilution of control, and expects ROCE to exceed the cost of debt (trading on equity). They also suit inflationary periods, as the real burden falls.
- **Leasing:** operating vs finance lease; sale and leaseback; leveraged lease. Lessee evaluates the **PV of lease rentals (after tax)** against the PV of the cost of borrowing to buy.
- **Virtual banking** – banking through the internet and mobile without physical branches. It is popular for 24×7 access, lower costs, speed and convenience.

2.2 Cost of capital

Cost of irredeemable debt = $K_d = I(1 - t) \div NP$

Cost of redeemable debt = $K_d = [I(1 - t) + (RV - NP) \div n] \div [(RV + NP) \div 2]$

Cost of preference shares = $K_p = [PD + (RV - NP) \div n] \div [(RV + NP) \div 2]$ (irredeemable: $PD \div NP$)

Cost of equity – dividend growth = $K_e = D_1 \div P_0 + g$, where $D_1 = D_0(1 + g)$ and $g = b \times r$

Cost of equity – CAPM = $K_e = R_f + \beta(R_m - R_f)$

Earnings yield method = $K_e = EPS \div MPS$

Cost of retained earnings = $K_r = K_e$ (ignoring flotation cost and personal taxes)

WACC = Σ (weight × specific cost) – weights at book value or market value

WORKED EXAMPLE **Specific costs and WACC (verified in Python)**

10% debentures of ₹100 issued at ₹96, redeemable at ₹105 after 5 years, tax 25%: $K_d = [10 \times 0.75 + (105 - 96)/5] \div [(105 + 96)/2] = (7.50 + 1.80) \div 100.50 =$ **9.25%**.

Equity: D_0 ₹4, g 6%, P_0 ₹50 → $K_e = 4.24/50 + 6\% =$ **14.48%**. CAPM: R_f 7%, β 1.2, R_m 12% → **13%**.

9% preference ₹100 issued at ₹95, redeemable at par in 5 years: $K_p = (9 + 1) \div 97.5 =$ **10.26%**.

WACC with weights equity 50% (15%), preference 10% (10%), debt 40% (7.5%) = 7.5 + 1.0 + 3.0 = **11.5%**.

- **Marginal cost of capital** – the WACC of additional funds raised, often in steps as cheaper sources are used up (break points).

2.3 Capital structure

- **Theories: Net income (NI)** – more debt lowers WACC and raises value (Ke and Kd constant). **Net operating income (NOI)** – WACC and value are independent of leverage (Ke rises linearly). **Traditional** – an optimal structure exists, where WACC is minimum. **Modigliani–Miller** – without taxes, value is independent of capital structure (arbitrage); with taxes, Vl = Vu + Dt (tax shield).

MM with taxes = Value of levered firm = Value of unlevered firm + Debt × tax rate

- **EBIT–EPS (indifference point)** – the EBIT at which EPS is the same under two financing plans:

Indifference point = (EBIT − I1)(1 − t) ÷ N1 = (EBIT − I2)(1 − t) ÷ N2 (deduct preference dividend where present)

WORKED EXAMPLE Indifference point (verified)

Plan A: issue 2,00,000 equity shares. Plan B: issue 1,00,000 shares + ₹10 lakh 10% debt (interest ₹1,00,000). Tax 25%. EBIT × 0.75 ÷ 2,00,000 = (EBIT − 1,00,000) × 0.75 ÷ 1,00,000 → **EBIT = ₹2,00,000**; EPS at that level = ₹0.75 under both plans. Above ₹2,00,000 EBIT, the debt plan gives higher EPS.

- **Factors in capital structure:** financial leverage/trading on equity, cost of capital, risk and cash-flow ability, control, flexibility, market conditions, tax, and the **pecking order** (internal funds → debt → equity).
- **Over- and under-capitalisation** and their remedies.

2.4 Leverages

Degree of operating leverage = DOL = Contribution ÷ EBIT = % change in EBIT ÷ % change in sales

Degree of financial leverage = DFL = EBIT ÷ EBT (with preference dividend: EBIT ÷ [EBT − PD ÷ (1 − t)]) = % change in EPS ÷ % change in EBIT

Degree of combined leverage = DCL = DOL × DFL = Contribution ÷ EBT

WORKED EXAMPLE Leverages (verified)

Sales ₹10,00,000; variable cost ₹6,00,000; fixed cost ₹1,50,000; interest ₹50,000. Contribution 4,00,000; EBIT 2,50,000; EBT 2,00,000. **DOL = 1.6; DFL = 1.25; DCL = 2.0**. A 10% rise in sales raises EBIT by 16% and EPS by 20%.

- **Financial leverage as a "double-edged sword":** when ROI exceeds the cost of debt, leverage **magnifies** EPS (favourable). When ROI falls below the cost of debt, it **magnifies losses** to shareholders and raises the risk of insolvency.
- **Financial distress** – inability to meet obligations; prolonged distress leads to loss of customers and suppliers, higher borrowing cost, employee attrition, forced asset sales and eventually bankruptcy.

Chapter 3: Capital Investment and Dividend Decisions

3.1 Capital budgeting – cash flows

- Use **incremental, after-tax cash flows**; ignore sunk costs and allocated overheads; include opportunity costs, working capital (released at the end) and salvage value (with the tax effect).

Annual cash inflow = (Revenue − cash cost − depreciation)(1 − t) + depreciation = EBIT(1 − t) + depreciation

- **Replacement decisions:** incremental investment = cost of new − sale value of old (tax adjusted); incremental depreciation; incremental savings.

3.2 Techniques

Technique	Rule	Note
Payback period	Years to recover the initial outlay	Ignores the time value of money and post-payback flows; **discounted payback** fixes the first
ARR	Average profit after tax ÷ average (or initial) investment	Accounting profits; ignores the time value of money
NPV	PV of inflows − PV of outflows; accept if > 0	Best measure of value creation
IRR	Rate at which NPV = 0; accept if IRR > cost of capital	Interpolate: L + NPV_L ÷ (NPV_L − NPV_H) × (H − L)
PI	PV of inflows ÷ PV of outflows; accept if > 1	Useful under **capital rationing**
MIRR	Reinvests inflows at the cost of capital	Avoids the multiple-IRR problem
Equivalent annual cost/benefit	NPV ÷ annuity factor	Compares projects or machines with **unequal lives**

WORKED EXAMPLE NPV, IRR, PI and payback (verified)

Outlay ₹5,00,000; inflows years 1–5: 1,50,000; 1,80,000; 2,00,000; 1,60,000; 1,20,000; cost of capital 10% (PVF 0.909, 0.826, 0.751, 0.683, 0.621).

NPV = ₹1,19,180 (approx.); **PI = 1.24**; **IRR ≈ 19.2%**; **payback = 2.85 years** (1,50,000 + 1,80,000 = 3,30,000 in two years; 1,70,000/2,00,000 = 0.85 of year 3).

- **NPV vs IRR conflicts** arise from size disparity, timing of cash flows and unequal lives. **NPV is preferred** because it assumes reinvestment at the cost of capital and measures absolute wealth.
- **Risk analysis** (overview): risk-adjusted discount rate, certainty equivalents, sensitivity and scenario analysis.

3.3 Dividend decisions

Walter model = $P = [D + (r \div Ke)(E - D)] \div Ke$

Gordon model = $P0 = E(1 - b) \div (Ke - br) = D1 \div (Ke - g)$

MM model = $P0 = (D1 + P1) \div (1 + Ke)$; new shares $\Delta n = (I - (E - nD1)) \div P1$

WORKED EXAMPLE Dividend models (verified)

Walter: E ₹10, D ₹4, r 15%, Ke 12% → P = [4 + (0.15/0.12) × 6] ÷ 0.12 = **₹95.83**. Since r > Ke, retaining more increases the price (optimal payout: zero).

Gordon: E ₹10, b 60%, r 15% → g 9%; D1 = ₹4; P0 = 4 ÷ (0.12 − 0.09) = **₹133.33**.

MM: P0 ₹100, Ke 10%, D1 ₹5 → P1 = **₹105** if the dividend is paid and **₹110** if not – the shareholder's wealth is the same.

- **MM assumptions:** perfect capital markets; no taxes (or no difference between dividend and capital gains tax); fixed investment policy; no risk or uncertainty (investors can forecast prices and dividends); no flotation or transaction costs.
- **Relevance theories:** Walter, Gordon ("bird in hand"); **irrelevance:** MM. Practical: stable dividend policy, Lintner model, residual policy.
- **Stock split** – reduces the face value and raises the number of shares. **Advantages:** makes shares affordable and more liquid; signals growth. **Limitations:** extra cost; no real change in value; may attract speculation. **Bonus shares** – capitalisation of reserves.

Chapter 4: Management of Working Capital

4.1 Concepts and estimation

- **Gross WC** = current assets; **net WC** = CA − CL. Permanent vs temporary WC. **Financing approaches:** matching (hedging), conservative, aggressive.

Operating cycle = RM storage period + WIP conversion period + FG storage period + receivables collection period − payables deferral period

- Example: 45 + 15 + 30 + 60 − 40 = **110 days** (verified).
- **Estimation of working capital (cash-cost basis):** raw materials (months × RM consumed), WIP (months × cost of production, adjusted for degree of completion), finished goods (months × cost of production/sales), debtors (at **cost of sales** excluding depreciation, or at sales value, as per the question), cash, less creditors (months × purchases) and outstanding wages/overheads; add a contingency margin.

4.2 Receivables management

- Evaluate a credit policy by **incremental analysis**: incremental contribution − cost of funds in additional receivables (at cost) − incremental bad debts − incremental collection/administration cost.

WORKED EXAMPLE Liberalising credit (verified)

Sales ₹30 lakh → ₹35 lakh if the credit period is extended from 30 to 60 days; variable cost 70%; bad debts 1% → 2%; cost of funds 15% p.a.; 360-day year.

Incremental contribution = 5,00,000 × 30% = **1,50,000**. Investment in receivables at variable cost: before 30,00,000 × 70% × 30/360 = 1,75,000; after 35,00,000 × 70% × 60/360 = 4,08,333; extra 2,33,333 × 15% = **35,000**. Extra bad debts = 70,000 − 30,000 = **40,000**. Net gain = **₹75,000** → liberalise.

- **Factoring** – sale of receivables to a factor (with or without recourse) for immediate cash plus services (collection, ledger management, credit protection). Compare the factoring cost with savings in administration, bad debts and interest.

4.3 Cash management

Baumol model = Optimum cash = √(2 × T × b ÷ i) (T = annual cash need, b = cost per conversion, i = interest rate)

- Example: T ₹10,00,000, b ₹320, i 10% → √(64,00,00,000) = **₹80,000** (verified).
- **Miller–Orr model:** cash balances fluctuate randomly between an **upper limit** and a **lower limit**. When cash touches the upper limit, securities are bought to bring it back to the **return point**; when it touches the lower limit, securities are sold. Spread = 3 × (¾ × transaction cost × variance ÷ interest rate per day)^⅓; return point = lower limit + spread ÷ 3.
- **Cash budget** – receipts and payments by month; identifies surplus or deficit. Also **float** management (collection and disbursement float), concentration banking, lock-box.

4.4 Payables, inventory and WC finance

- **Cost of forgoing a cash discount** = [d ÷ (100 − d)] × [365 ÷ (credit days − discount days)]. Trade credit is not free when the discount is forgone.
- **Bank finance:** cash credit, overdraft, bill discounting, working capital demand loans; **commercial paper**; **packing credit** (pre-shipment) and **post-shipment** finance (e.g. negotiation or purchase of export bills) for exporters.

Chapter 5 (Section B – SM): Introduction to Strategic Management

5.1 Business policy, strategy and strategic management

- **Strategy** – a long-term plan of action designed to achieve the organisation's objectives and competitive advantage; it is partly **proactive** (planned) and partly **reactive** (adaptive). **Strategic management** – formulating, implementing and evaluating cross-functional decisions that enable an organisation to achieve its objectives.
- **Strategic intent** = vision + mission + business definition + business model + goals and objectives.

Element	Meaning	Features
Vision	What the organisation **wants to become** – the future picture	Inspiring, long-term, clear
Mission	**Why it exists** – purpose, customers, products and philosophy	Broad, enduring, distinguishes the firm
Values	Core beliefs guiding behaviour and decisions	Ethical anchor
Goals / objectives	Specific, measurable targets for results	SMART, time-bound, consistent

- **Significance of vision and mission:** give direction and purpose; unify effort and culture; guide resource allocation; communicate identity to stakeholders; serve as a basis for objectives and for evaluating performance.
- **Objectives with a strategic focus** aim at outcomes that strengthen the **overall business position and competitive strength** (market share, quality, customer satisfaction, technology leadership). **Financial objectives** concern financial outcomes (profit, ROI, cash flows). Both are needed.
- **Levels of strategy: corporate** (what businesses to be in – board and top management), **business** (how to compete in each business – SBU heads), **functional** (how each function supports the business strategy – marketing, finance, HR, operations).
- **Importance:** proactive orientation; direction; better allocation of resources; anticipating opportunities and threats; competitive advantage; long-term survival. **Limitations:** a complex and uncertain environment; time-consuming and costly; difficult to forecast; rigidity; competitors may also plan; benefits are hard to measure.
- **Strategic management process:** (1) strategic intent; (2) environmental and organisational analysis; (3) strategy formulation; (4) strategy implementation; (5) strategy evaluation and control – a continuous loop.
- **Strategic decision makers:** board, CEO, top management, SBU and functional managers. **Strategic uncertainty** – unpredictability of future events (technology, regulation, competition, customer behaviour) affecting the strategy; managed by scenario planning, strategic flexibility, monitoring of signals and building options.

Chapter 6: Strategic Analysis – External Environment

6.1 Macro environment – PESTLE

Factor	Examples
Political	Government stability, trade policy, subsidies, tax policy
Economic	GDP growth, inflation, interest rates, exchange rates, income levels, electricity access in developing countries
Social	Demographics, lifestyle, education, preferences (e.g. Generation Z wanting personalisation)
Technological	Automation, AI, digital platforms, R&D
Legal	Consumer protection, labour, competition and data-protection laws
Environmental	Climate change, pollution norms, sustainability expectations

- **Micro environment:** customers, suppliers, competitors, intermediaries, public. **Demand and supply** interact to set price in competitive markets. Firms analyse demand elasticity, supply constraints and substitutes to set price and capacity.
- **Close and continuous interaction with the environment** helps a firm to identify opportunities and threats early, adapt products, use resources effectively, and build legitimacy.

6.2 Industry and competitive analysis

- **Key questions:** dominant economic features of the industry; competitive forces and their strength; drivers of change; strongest and weakest competitors (strategic group mapping); likely moves of rivals; **key success factors**; whether the industry is attractive.
- **Porter's five forces:** (1) **threat of new entrants** (barriers – economies of scale, capital, brand, access to channels, regulation); (2) **bargaining power of buyers**; (3) **bargaining power of suppliers**; (4) **threat of substitutes**; (5) **rivalry among existing firms**. The state of competition is a composite of these forces. Collectively strong forces mean low industry profitability.
- **Strategic group mapping** – plotting rivals on two key competitive characteristics (price/quality, geographic coverage) to identify the closest competitors.
- **Industry life cycle / PLC:** introduction → growth → maturity → decline. Strategy differs by stage (heavy promotion in introduction; capacity expansion in growth; cost efficiency and differentiation in maturity; harvest or divest in decline).
- **Globalisation – reasons to go global:** market inadequacy at home, resource needs (raw materials, talent, technology), lower costs, collapse of trade barriers, spreading risk, following customers, and economies of scale.

Chapter 7: Strategic Analysis – Internal Environment

7.1 Resources, capabilities and competitive advantage

- **Competitive advantage** – a position that lets a firm earn higher returns than rivals, through **lower cost** or **differentiation**. It is sustainable if it is hard to imitate.
- **Core competencies** (Prahalad and Hamel) – a combination of skills and technologies that **provides access to a wide variety of markets**, makes a **significant contribution to customer benefits**, and is **difficult to imitate**. **VRIO test:** valuable, rare, inimitable, organised to capture value.
- **Value chain (Porter): primary activities** – inbound logistics, operations, outbound logistics, **marketing and sales** (e.g. partnerships with retail chains expand distribution, which is outbound logistics/marketing), service; **support activities** – firm infrastructure, HR management, technology development, procurement.
- **Experience curve / learning curve** – unit costs fall as cumulative output rises because workers become more efficient through repetition, processes improve, and economies of scale arise. It gives a cost advantage to the market leader; firms pursuing cost leadership use it.

7.2 SWOT and TOWS

- **SWOT** – internal **strengths and weaknesses**, external **opportunities and threats**. It helps an organisation develop a full awareness of all factors in a decision, build on strengths, minimise weaknesses, seize opportunities and counter threats.
- **TOWS matrix: SO** (use strengths to exploit opportunities – maxi-maxi), **ST** (use strengths to counter threats), **WO** (overcome weaknesses using opportunities), **WT** (defensive – minimise weaknesses and avoid threats).

7.3 Portfolio analysis

Model	Dimensions	Strategies
BCG growth-share matrix	Market growth rate × relative market share	**Stars** (invest), **cash cows** (milk, fund others), **question marks** (invest selectively or divest), **dogs** (harvest/divest)
GE nine-cell matrix	**Industry (market) attractiveness × business strength (competitive position)**	High-high cells: **invest/grow** (green); middle: selective/hold (yellow); low-low: harvest/divest (red)
Ansoff product-market growth matrix	Existing/new products × existing/new markets	**Market penetration**, **market development** (existing product, new market/segment), **product development**, **diversification**
ADL matrix VERIFY	Competitive position × industry maturity	Natural development to withdrawal

7.4 Strategic drivers

- Industry and markets, customers, channels, products and services, and **competitive advantage** – the forces that shape strategy and that management must understand to choose the right direction.

Chapter 8: Strategic Choices

8.1 Business-level (Porter's generic) strategies

Strategy	Means	Conditions for success
Cost leadership	Lowest cost producer; standard product; price advantage	Economies of scale, experience curve, efficient processes, tight cost control, access to cheap inputs, price-sensitive buyers
Differentiation	Unique features valued by customers; premium price	Strong R&D, brand, quality, customer service; buyers value uniqueness
Focus (cost or differentiation)	A narrow segment, niche or locality	Segment distinct and big enough; rivals not serving it well (e.g. a neighbourhood store with personalised delivery)
Best-cost provider	Good features at a lower price than rivals	Buyers want value

- **Risks:** cost leaders – technological change, imitation, lost focus on customer needs. Differentiators – imitation, price premium too high. Focusers – segment erosion, broad competitors entering.
- **Cost leadership – key resources and capabilities:** sustained capital investment and access to capital; process engineering skills; intense supervision of labour; products designed for ease of manufacture; low-cost distribution; tight cost control with frequent reports; structured organisation and responsibilities; incentives based on quantitative targets.

8.2 Corporate-level (grand) strategies

Strategy	Forms
Stability	Continue the current business with incremental improvement
Growth/expansion	**Intensification** (market penetration, market development, product development); **diversification** – related/concentric, unrelated/conglomerate; **vertical integration** (backward/forward); **horizontal integration**; mergers and acquisitions; strategic alliances; joint ventures; internationalisation
Retrenchment	**Turnaround** (fix a declining business), **divestment** (sell a unit), **liquidation** (close down)
Combination	Different strategies for different units at the same time

- **Turnaround – danger signs:** persistent negative cash flows, declining market share, falling sales, high employee turnover and low morale, uncompetitive products, mismanagement. **Action plan:** assess the situation; diagnose root causes; set a turnaround plan (cost cutting, asset sales, revenue generation, product repositioning); implement; return to normal growth and profitability.
- **Divestment** – when a unit consistently performs below expectations, does not fit, needs too many resources, or the money is better used elsewhere. **Liquidation** – last resort; selling all assets.
- **Mergers and acquisitions:** horizontal, vertical, concentric, conglomerate; **reasons:** synergy, growth, market power, diversification, tax benefits, acquiring technology or brands. Risks: integration problems, overpaying, culture clash.
- **Strategic alliances** – cooperation between firms while remaining independent (e.g. partnering with financial institutions to offer customer financing).

Chapter 9: Strategy Implementation and Evaluation

9.1 Formulation vs implementation

Formulation	Implementation
Positioning forces before action	Managing forces during action
Focus on **effectiveness**	Focus on **efficiency**
Mainly an **intellectual** process	Mainly an **operational** process
Needs intuitive and analytical skills	Needs motivation and leadership skills
Coordination among a few people at the top	Coordination among many people

- **Strategy formulation vs implementation matrix:** sound formulation + good implementation = **success**; sound formulation + poor implementation = **trouble**; poor formulation + good implementation = **roulette**; poor formulation + poor implementation = **bad**. The two are linked: a strategy is only as good as its execution.

9.2 Organisational structure

Structure	Features
Functional	Grouped by functions; suits single-product firms
Divisional	By product, geography or customer; suits diversified firms
SBU	Groups of related businesses as strategic business units
Matrix	Dual reporting – functional and project; for complex projects
Network / virtual	Outsourcing of most functions; coordination through IT
Hourglass	**Middle management levels compressed** (technology and empowerment replace coordinating roles); a broad top and a broad, multi-skilled lower level. Faster decisions and lower cost, but fewer promotion paths

9.3 Leadership, culture and change

- **Strategic leadership** – managing through others: setting direction, building culture, motivating. **Transformational** leaders inspire change through charisma and vision; **transactional** leaders rely on rewards and procedures to maintain stability.
- **Corporate culture** – the shared beliefs, values and practices of an organisation. **Sources:** the founders' vision and values; history and past successes; the leadership's behaviour; the industry and the environment; rewards and HR practices; rituals, stories and symbols. Culture can be a strength (alignment) or a weakness (resistance to change).
- **McKinsey 7S framework: hard S** – strategy, structure, systems; **soft S** – **shared values**, **style**, **staff**, **skills**. All seven must be aligned. Failures often come from misaligned soft elements, e.g. poor communication and integration despite a good strategy and talent.
- **Strategic change – Kurt Lewin: unfreezing** (create awareness of the need to change), **changing/moving** (new behaviours, processes, structure), **refreezing** (institutionalise the change).
- **Digital transformation** – integrating digital technology into all areas (cloud, AI, analytics, e-commerce), changing how the business operates and delivers value. Success requires leadership commitment, a customer focus, data capability, change management and culture.
- **Innovation** – a catalyst for growth: new products, processes and business models; it improves customer satisfaction and creates competitive advantage. It needs an innovation culture, R&D, collaboration and tolerance of failure.

9.4 Strategic control and performance measures

Type	Purpose
Premise control	Checks whether the **assumptions** on which the strategy was based remain valid

Type	Purpose
Implementation control	Monitors milestones and projects to see whether the strategy is being implemented as planned and remains appropriate
Strategic surveillance	A broad, unfocused scan of the environment for events that may affect the strategy
Special alert control	Rapid reassessment after a sudden, unexpected event (disaster, takeover bid)

- **Operational control** – short-term budgets and schedules; **management control** – resource use against targets.
- **Strategic performance measures:** financial (profitability, ROI, EVA), customer (satisfaction, retention, market share), internal processes (quality, cycle time), learning and growth (employee skills, innovation) – the **balanced scorecard** links them to strategy. Good measures are **aligned with goals**, relevant, actionable, balanced between leading and lagging indicators, and few in number. **Benchmarking** compares performance with the best in the industry.

Formula and framework sheet

Topic	Remember
Kd (redeemable)	[I(1 – t) + (RV – NP)/n] ÷ [(RV + NP)/2]
Ke	D1/P0 + g; CAPM Rf + β(Rm – Rf); g = br
Leverage	DOL = C/EBIT; DFL = EBIT/EBT; DCL = C/EBT
Indifference point	(EBIT – I1)(1 – t)/N1 = (EBIT – I2)(1 – t)/N2
Capital budgeting	Cash flow = EBIT(1 – t) + depreciation; IRR interpolation; PI = PV inflow/PV outflow; EAC = NPV/annuity factor
Dividend	Walter; Gordon P = E(1 – b)/(Ke – br); MM P0 = (D1 + P1)/(1 + Ke)
WC	Operating cycle = RM + WIP + FG + debtors – creditors; Baumol √(2Tb/i); discount cost = d/(100 – d) × 365/(N – D)
SM frameworks	PESTLE; Porter 5 forces; value chain; SWOT/TOWS; BCG; GE 9-cell; Ansoff; generic strategies; grand strategies; 7S; Lewin; strategic control types; balanced scorecard

Common mistakes in answers

1. FM: using pre-tax cost of debt in WACC, or forgetting to deduct tax on interest.
2. FM: including depreciation (non-cash) as an outflow, or forgetting its tax shield.
3. FM: mixing book and market value weights; not stating the assumption used.
4. FM: in credit-policy questions, computing the investment in receivables at sales value when the question says "at cost".
5. FM: treating sunk costs or allocated overheads as relevant cash flows.
6. FM: computing EPS without deducting preference dividend.
7. SM: listing theory without **applying it to the case** – ICAI asks you to identify the strategy, explain why, and recommend.
8. SM: confusing **market development** with **product development** in Ansoff questions.
9. SM: confusing BCG dimensions (growth × share) with GE dimensions (attractiveness × strength).
10. SM: writing generic points on culture or leadership without the specific framework the question names (7S, Lewin, generic strategies).