Examiner's report
Performance Management
September 2018

General comments

The Performance Management exam is offered in both computer-based (CBE) and paper formats. The structure is the same in both formats but our model of delivery for the CBE exam means that candidates do not all receive the same set of questions. In this report, the examining team share their observations from the marking process to highlight strengths and weaknesses in candidates' performance, and to offer constructive advice for future candidates.

- Section A objective test questions – we focus on two specific questions that caused difficulty in this sitting of the exam.
- Section B objective test case questions – here we look at the key challenge areas for this section in the exam.
- Section C constructed response questions - here we provide commentary around some of the main themes that have affected candidates' performance in this section of the exam, identifying common knowledge gaps and offering guidance on where exam technique could be improved, including in the use of the CBE functionality in answering these questions.

<u>Section A</u>

Sample Questions for Discussion

Here we take a look at **TWO Section A** questions which proved to be particularly difficult for candidates.

Example 1

Summary financial information for one of Damon Co's divisions for the last year is shown below:

	$'000
Revenue	18,000
Variable costs	(9,600)
Divisional fixed operating costs	(2,760)
Apportioned head office costs	(2,160)
Interest charges	(200)
Tax	(700)
Net profit	**2,580**

The average value of the division's total assets less current liabilities for the last year was $22.8m.

Damon Co assesses the return on investment of its divisions on the basis of controllable profit.

Based on this information, what is the division's return on investment for the last year?

A   11.3%
B   15.3%
C   20.8%
D   24.7%

What does this test?

✓ The calculation of a division's return on investment

What is the correct answer?

✓ The correct answer is **D**

- ROI is calculated as operating profit/capital employed. In this case, because the company measures the ROI on controllable costs, the figure for operating profit should exclude the apportioned head office costs.
- Therefore, ROI = ($18,000 - $9,600 - $2,760)/$22,800 = 24.7%
- Selecting option A, means that net profit was incorrectly used to calculate ROI
- Selecting option B, suggests that the operating profit figure was used without making an adjustment for head office costs
- Selecting option C, means that only the head office costs were added back to net profit and not the interest and tax figures ($2,580 + $2,160)/$22,800 = 20.8%

Example 2

Farry Co has recently decided to allow its employees to have unlimited access to the internet from their workplace computers using the company network. The reason for this decision is to allow employees to use external information so they can perform their duties more effectively.

Which of the following are direct costs of accessing external information for Farry Co?

(1)   Monetary cost of download fees
(2)   Time spent by employees using search engines
(3)   Payment for additional network security

A   1 and 2 only
B   1 and 3 only
C   1, 2 and 3
D   2 only

What does this test?

✓ The limitations of using externally generated information

What is the correct answer?

✓ The correct answer is **B**

- The question requires the distinction between direct and indirect costs of information.
- The time spent searching and analysing information on the internet has a cost but is not easily quantifiable and is often hidden amongst other costs and seen as sunk therefore it is indirect.
- The other two costs are easily identifiable with the decision and are quantifiable and so are direct costs.

Section B

Section B tests students' knowledge on a number of topics in more detail than section A, with three case questions containing 5 two-mark objective test questions. The range of topics covered in the September 2018 examination was:

- Decision making under uncertainty
- Target costing
- Activity based costing
- Learning curves
- Pricing
- Rolling budgets

A few key points that came out of section B were:

- Read the case scenario and requirements very carefully. This goes for the whole exam, but any objective test question is 'all or nothing' – if you misread the requirement or miss a vital piece of information from the scenario and get the answer incorrect you score zero for that question. This applies also to instructions on how to round your answers.
- Cover the whole syllabus. The list above should highlight this –PM has a large syllabus which can be daunting, but it is essential to have a broad knowledge. If, for example, a section B case covering variances comes up and you haven't covered this in your studies, the 10 marks available are left to chance.
- Be able to apply your knowledge of theories/techniques to the scenario given, as in the case questions these areas will often be examined in the context of the case. It is important that you are able to apply the logic of a concept or theory to a problem and so you need to understand the method and why you are doing the calculations, and not just focus on how to do the calculations.

Section C

Candidates were presented with questions drawn mainly from the areas of:

- Variances
- Performance measurement
- CVP analysis
- Limiting factor analysis

These will be discussed in turn. Although the specifics of individual questions will not be discussed, common areas candidates either performed well on or struggled with will be highlighted. Advice will be provided to improve exam performance.

Variances

This is usually an unpopular syllabus area, but answers were generally very strong. Longer variance questions usually involve calculation of some variances, and some discussion either about the variances, or issues surrounding their use. Candidates showed that they were able to use the information in the scenario to calculate the variances correctly, and apply their knowledge and understanding to discuss what was required.

It's possible that the change in the structure of the exam has encouraged candidates to spend more time practicing these calculations in order to make sections A and B more straightforward. Whatever the reason, it shows that spending time learning the techniques required certainly pays off.

Performance measurement

This is a broad and regularly examined area of the syllabus, and unfortunately performance in this key area was poor. The general structure of questions in this area is to present the candidate with information – words and numbers – about a business or possibly division(s) of a business. The main requirement will then be to discuss the performance of the business. In more recent exams, more guidance has been given as to which areas of performance should be discussed. This can be in the form of key headings, reference to the objectives of the business, or use of the models from the syllabus.

Whichever of these is the case, it's absolutely essential to read both the requirement and the scenario carefully. 'Assess the performance' can be quite a daunting prospect (where do I start?), but reading the requirement carefully can give big clues. The main reason candidates struggle to score well is that they do not address the requirement fully, missing out key instructions.

The other reason candidates struggle to score well on these questions is by not using the information in the scenario to give depth to their discussion.

Both of these problems can be explained using the March/June 2017 published sample questions. In The People's Bank question, a lot of information is given, which can also cause problems as candidates can spend too long reading this before knowing what they're trying to do, and end up re-reading it several times before they know what they're trying to do. To avoid falling into this trap, limit yourself to reading the first couple of lines of the scenario, to see what you're dealing with, and then move straight to the requirement(s).

The first requirement is a short, 4 mark question on why the balanced scorecard is more useful than just using financial measures. It is worth reading the suggested solution to see how it uses the information in the scenario, rather than generic answers like "financial doesn't show the whole picture."

Requirement (b) though, for 16 marks is worth spending more time reviewing. It's easy to look at a requirement like this and think "how am I going to write 16 marks' worth?" This is where taking an extra minute or so really pays off. The requirement reads:

"Using all of the information provided, including The People's Bank's vision and values, discuss the performance of The People's Bank in 20X6.

Note: Use each of the four headings of the balanced scorecard to structure your discussion."

Under exam conditions, it's easy to rush here and read "Using all of the information provided, discuss the performance of The People's Bank in 20X6," and dive into the question, but taking a little bit of extra time makes this a relatively easy task.

Firstly, the note underneath the requirement – use the four headings of the balanced scorecard. We now know that our answer will revolve around those four headings, making it easier to come up with points relevant to each one. It does also highlight the importance of knowing the models in the syllabus – if you

don't know the perspectives of the balanced scorecard; it's hard to structure your answer properly. You can still gain credit, but it's much harder to come up with valid points. As it happens, they are given in the scenario, but that's not always the case, so don't rely on it.

Secondly, the bank's vision and values are mentioned. We haven't read the scenario yet, but now we know that we need to look out for them, as they're clearly important. You can read the scenario and identify them quickly, but you must make sure that you use them. We're given several performance measures for each perspective, but the key thing here is addressing the requirement.

To give one example, under the 'Internal process' heading, we're told that the actual number of business processes within The People's Bank that were re-engineered and simplified was 110 compared to a target of 100. A generic answer would say "This is a good performance, as actual was 10% better than expected." It's very hard to give this any credit – to score marks in a PM question, you need to either give more depth to the discussion – why is something better or worse, or what does it mean to the business.

In this case, the second value listed is "Making business simple". This performance measure shows that they have met that value, so we could say "This is a good performance, as actual was 10% better than expected, showing that the bank has achieved its second value of making business simple." That little bit extra shows a full understanding of what the business is trying to do.

In summary, when asked to assess performance, don't just calculate every ratio or percentage movement you can find, and say "x is bigger than y" – spend a bit more time looking for what's important to the business, and explaining why things are better or worse.

CVP Analysis

Perhaps more regularly examined in sections A and B, CVP analysis is still an important syllabus area in PM, and candidates need to make sure they spend enough time studying it to gain a full understanding of what it offers.

While candidates had (on the whole) learned the relevant formulae to calculate important measures such as Weighted Average C/S ratio, Breakeven Revenue and Margin of Safety, when asked to discuss their answers there was a lack of depth. Common mistakes such as saying "If the breakeven point falls, then the margin of safety also falls," showed either a lack of care or a lack of understanding.

However, candidates generally picked up enough of the easy calculation marks to score a pass in this area. It should be noted though, that basic management accounting techniques are tested here, such as working out contribution, or total fixed costs. It was clear from many candidates' responses that although they understood the 'new' areas of the PM syllabus, their fundamental grasp of costing was lacking. Key errors such as not including non-production variable costs in contribution, or treating fixed costs as variable, meant that high scores were rare.

Limiting Factor Analysis

A popular topic in PM, dealing with limiting factors is an essential skill in decision making. Questions can either involve one limiting factor (Key Factor Analysis) or several, where Linear Programming techniques are required.

Performance in this area is usually quite good, as there is a well-defined list of steps to follow, however it is often clear that while the knowledge of the procedure is there, the understanding isn't. Looking at a situation with a single limiting factor, as this was the method primarily examined this sitting, it's important to understand the situation. We have a limiting factor – i.e. something that is limiting our output. As a result, we need to make the most of this limiting factor. Questions differ – we may be facing a make vs buy decision or a production levels decision, but the aim is the same – we need to get the most benefit per unit of the limiting factor. It is the last part – 'per unit of limiting factor' that is most often missed by candidates.

In a simple example, where we have a limit on material and make two products, most candidates will calculate the contribution per unit of each (or saving per unit in a make vs buy question). Answers such as this are common:

	Product A	Product B
Selling Price ($)	20	100
Variable Costs ($)	15	85
Contribution ($)	5	15
Rank	2	1

This is then followed by a production plan making product B first. This misses the key point that we're limited by material – we don't know which product requires more material. In an extreme example, if product A requires 1kg of material and product B 15kg then despite its higher contribution, Product B will use up our scarce resource quickly, and provide less benefit. The correct approach would be:

	Product A	Product B
Selling Price ($)	20	100
Variable Costs ($)	15	85
Contribution ($)	5	15
Material/unit (kg)	1	15
Contribution/kg ($)	5	1
Rank	1	2

This shows the importance of the limiting factor – using 1kg of materials to make Product A will generate $5 of contribution, whereas making Product B will only give us $1 of contribution per kg used – so we must make Product A first to maximise our contribution, and any leftover material can be used to make Product B.

There are of course other factors to consider – if we only focus on one product then customers may be unhappy with the lack of availability of the other(s). Candidates seemed comfortable identifying these non-financial factors in the context of limiting factors – perhaps more so than other syllabus areas. Practical issues regarding make vs buy decisions such as effect on quality, customer reaction and delivery lead times were quickly identified.

Exam technique on PM exams

Exam technique is important at any level, but especially in PM as it is often the first exam that candidates attempt at the Applied Skills level. The style of questions is different and the time available feels tight. It does

seem that in recent sittings candidates have concentrated on scoring well in Sections A and B at the expense of Section C, with some written answers being very brief or rushed. I would strongly recommend managing your time carefully to allow enough (about 40%) of the available time to make a good attempt at Section C.

There are a couple of strong arguments for this. Firstly, answers to Sections A and B are either right or wrong. This means that a silly mistake, or misreading the question, can mean missing out on 2 marks. In Section C, assuming that you show your workings, you can still score most of the marks if you make a mistake.

Secondly, there are many 'easy' marks available on Section C. For calculations, many smaller calculations are awarded credit as they are required to get to the final answer. A ten mark calculation question might only have one mark allocated to the 'final' answer, with the rest for the working required to get there. Looking at past exam questions can help explain this – Q31 from the Sep/Dec 2017 published sample questions is a good example. Part (a), for 12 marks, is to calculate an optimum selling price and resulting profit using the MR=MC method.

A quick look at the mark allocations in the suggested answers shows the level of detail this is split into. For example, 1.5 marks for finding the demand function. So even if you struggle with later parts of the method, you'll get credit for this part. This is why it's important to attempt all parts of the exam, and explain to your marker what it is that you're trying to do – credit will be given where possible. Also remember that follow-on marks are given. In this question, if you get the demand function wrong, none of your later answers will be 'correct', but as long as your method is correct, you will be awarded the marks – in short, don't give up!

Other easy marks can be picked up on the discussion questions. On the same question, part (b) requires a discussion around two pricing methods, market penetration and market skimming, for 8 marks. You may look at that and struggle to come up with 8 marks' worth, but a couple of good points can soon boost you over the pass mark. If all that you can remember about market skimming is that it involves charging a high price and is suitable for unique products, write that down, and see if it applies to our product – a quick read of the scenario will show that in this case, it is a new, eagerly anticipated product, which is an argument in favour of market skimming. Candidates are not expected to reproduce the suggested solution in their answers, but showing understanding of the syllabus and using the scenario will gain a lot of credit.

Most candidates are now using the CBE software to sit the exam. Unfortunately it does seem that many are unprepared for the experience. While the word processing software is relatively straightforward to use, it is strongly recommended using the ACCAs practice resources at https://www.accaglobal.com/gb/en/student/exam-support-resources/fundamentals-exams-study-resources/f5/cbe-specimen-exams.html to get used to the spreadsheet software.

More specifically, the spreadsheet should be used to perform your calculations. A significant number of candidates are working out numbers on a calculator and then typing them into the spreadsheet. This is problematic for a number of reasons. Firstly, it's easy to type them in incorrectly. Secondly, if you've made a mistake in your calculation it is hard to award partial credit, as markers can't see where the calculations have come from. Thirdly, it's slow! The spreadsheet software should make calculations easier, not harder, allowing more time to focus on the written requirements and making the best use of the scenario.

Guidance and Learning Support resources to help you succeed in your exam

Preparing for the PM exam may appear daunting but there are many resources available to help you. There are many technical articles available on the topics in this report. In addition all the past exams referred to are available for your use. You should refer to these throughout your studies. Please make sure that you visit the ACCA's website and look at everything available to you. There are also plenty of support materials to help you feel confident about taking your exams on CBE.

http://www.accaglobal.com/uk/en/student/exam-support-resources/fundamentals-exams-study-resources/f5.html