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Financial

CIA-IV

The Certified Internal Auditor Part 4

QUESTION: 180
The managerial factor that may lead to overbuilding in an industry is

A. Management's belief that the career consequences of overcapacity appear to be more serious than those of under capacity.
B. Management's production orientation.
C. Inflation of expectations by industry buzz.
D. Uncertainty caused by changes in industry structure.

Answer: B
Management that is production-oriented may be more likely to overbuild than marketing-or finance- oriented management.

QUESTION: 181
What governmental factor most likely will lead to overbuilding in a global industry?

A. Tax incentives are given to local subsidiaries of foreign firms.
B. The government favors an indigenous industry that has a small minimum efficient scale.
C. Environmental regulations are imposed on domestic firms.
D. Anti-bribery laws impede domestic firms from competing globally.

Answer: A
Governmental factors may lead to overbuilding. For example, tax incentives may promote excess capacity by permitting foreign subsidiaries to pay no tax on earnings retained in the business. A nation also may wish to create an indigenous industry. When the minimum efficient scale is great in relation to world demand, the excess production in the country may contribute to global overcapacity. Furthermore, governmental employment pressures may result in overbuilding to create jobs or avoid job loss.

QUESTION: 182
Which factor is most likely to limit expansion of a firm's productive capacity?

A. Senior managers have production backgrounds.
B. The firm operates in one industry.
C. Current technology will soon be obsolete.
D. Demand uncertainty is low.

Answer: C
A firm's behavior may send signals to competitors that building is unwise. For example, it may announce an expansion project or indicate in some way that forecasts of demand are unfavorable or that current technology will soon be obsolete.

QUESTION: 183
What condition is most likely necessary to the success of a strategy of preemptive expansion?

A. Competitors believe that the move is preemptive.
B. The result is intense industry conflict.
C. The firm does not know the expectations of competitors about the market.
D. The learning-curve effect is small.

Answer: A
Competitors must believe that the move is preemptive. Hence, the firm should know competitors' expectations about the market or be able to influence them favorably. Moreover, the preempting firm must have credibility, such as resources, technology, and a history of credibility, to support its statements and moves.

QUESTION: 184
Entry into a new business may be made by internal development or acquisition. Entry through internal development usually involves creation of a full-fledged new business entity. The costs likely to be incurred by an internal entrant include
II. nvestments to overcome entry barriers
II. Change in the equilibrium level of supply and demand
III. Lower prices charged by competitors
IV. Higher marketing costs

A. I and II only.
B. I and IV only.
C. II, Ill, and IV only.
D. I, II, Ill, and IV.

Answer: D
An internal entrant must cope with structural barriers and retaliation by existing firms. Costs incurred by the internal entrant include initial investments to overcome entry barriers (facilities, inventory, branding, technology, distribution channels, sources of materials, etc.), operating losses in the start-up phase, and the effects of retaliation (e.g., higher marketing

costs, capacity expansion, or lower prices). Other costs include the price increases for factors of production that may result because of the new entry. Also, the capacity added to the industry by the entrant may affect the equilibrium level of supply and demand. The result may be additional competitive costs as firms with excess capacity cut prices.

QUESTION: 185

Entry into a new business may be made by acquisition. The analysis differs from that for entry by internal development. A key point is that prices are set in the market for acquisitions. Accordingly, a buyer should most likely expect to make above- average profits when the

A. Market is active and well organized.
B. Seller can choose to continue operating the business.
C. Market for acquisitions is imperfect.
D. Buyer adopts a sequential entry strategy.

Answer: C

Acquisitions are more likely to earn above-average profits when the expected present value to the seller of continuing operations is low, e.g., because the seller needs funds, has capital limits, or has management weaknesses. Above-average profits also are more likely when the market for acquisitions is imperfect. For example, (1) the buyer may have better information, (2) there are few bidders, (3) the economy is weak, (4) the seller is weak, or (5) the seller has reasons to sell other than profit maximization. Moreover, the buyer may have a unique ability to operate the seller.

QUESTION: 186

A firm enters a new business by creating a full-fledged new entity (an internal entrant). The internal entrant is least likely to cause disruption and retaliation in a

A. Slow-growth industry.
B. Fragmented industry.
C. Commodity-producing industry.
D. Highly-concentrated industry.

Answer: B

In a fragmented industry, many firms might be affected but not significantly. These firms also might have no ability to retaliate. Firms in a fragmented industry have insignificant market shares and little influence on industry outcomes.

QUESTION: 187
Entry by a firm into a new business may be through the creation of a full-fledged new business entity. The new entrant is most likely to cause industry disruption and retaliation when

A. The industry is fast-growing.
B. The industry is highly concentrated.
C. Fixed costs are low.
D. The market is segmented.

Answer: B
In a highly concentrated industry, the internal entrant is more likely to have a significant and noticeable effect on particular firms with the ability to retaliate. In a fragmented industry, many firms might be affected but not significantly. These firms also might have no ability to retaliate.

QUESTION: 188
A firm may decide to enter a new business by creating a new entity. After undertaking a structural analysis, the internal entrant chooses an appropriate target industry. The most likely target is an industry in which the entrant

A. Will have to develop its own distribution network.
B. Can raise mobility barriers after entry.
C. Will not have to compete with a dominant firm that seeks to protect the industry.
D. Calculates that the costs of retaliation to existing firms are less than the benefits.

Answer: B
A distinctive ability to influence industry structure is another basis for earning above-average profits. Thus, an ability to raise mobility barriers after the firm has entered the industry is a reason to target that industry. Moreover, a firm may be able to recognize that entering a fragmented industry will start a process of consolidation and increased entry barriers.

QUESTION: 189
A firm wishes to enter a new business by creating a new entity (an internal entrant). The internal entrant is most likely to achieve above-average profits by targeting which industry?

A. An industry with high entry costs.
B. An industry with a stabilized structure.
C. A new industry.

D. An industry in equilibrium if entry positively affects the firm's existing businesses.

Answer: C

A firm may be able to achieve above-average profits by choosing appropriate targets. For example, an industry may be in disequilibrium because it is new, entry barriers are rising, or firms have poor information. In a new industry,
(1) the structure is not established,
(2) entry barriers are low, (3) retaliation is unlikely,
(4) resource supplies have not been locked up, and
(5) brands are not well developed.
However, initial firms may have greater costs than later entrants. Rising entry barriers favor an early entrant whose subsequent competitors will face higher costs. The early entrant also may have an edge in product differentiation. Poor information may perpetuate disequilibrium because firms that might enter the industry may not be aware of its potential.

QUESTION: 190

According to the behavioral theory of management.

A. Employees are motivated to fulfill needs.
B. Morale problems are not goal related.
C. Compensation is a universal motivator.
D. Productivity is not correlated with job satisfaction.

Answer: A

The behavioral theory of management holds that all people including employees) have complex needs, desires, and attitudes. The fulfillment of needs is the goal toward which employees are motivated. Effective leadership matches need-fulfillment rewards with desired behavior tasks) that accomplishes organizational goals.