

## ASSIGNMENT COVER SHEET

### FINANCIAL RISK MANAGEMENT

Module Code : CIQGM719 Unit Number : 12

Course Level : Postgraduate (Level 7) Credit : 20

Valid for Academic Year 2019 - 20

### Applicable for the courses

- MBA in Accounting and Finance
- Postgraduate Diploma in Accounting and Finance

- |     |  |
|-----|--|
| LO1 | Understand the planning, budgeting and forecasting concepts of finance management                  |
| LO2 | Understand the control of performance management and internal control environment for risk control |
| LO3 | Understand the financial statement and decision analysis, including risk management                |
| LO4 | Know the shareholder/ corporate value creation, including M&A's and disposals                      |
| LO5 | Understand the control and management of operational and financial risk in a business              |

The following grading criteria will be applicable for this module :

Marks	Grade
70 to 100	A - Distinction
60 to 69	B - Merit
50 to 59	Pass
40 to 49	Fail with Resit
0 to 39	Fail with Retake

## General Guidelines

(Please read the instructions carefully)

1. Complete the title page with all necessary student details and ensure that the signature of the student is marked in the declaration form.
2. All assignments must be submitted as an electronic document in MS Word to the LMS (Use 12 Times New Roman Script).
3. Assignment that is not submitted to the LMS by the prescribed deadline will be accepted ONLY under the REDO and RESIT submission policy of EBS.
4. The results are declared only if the student has met the mandatory attendance requirement of 75% and/or minimum of 50% under extenuating circumstances approved and ratified by the Academic Director.
5. The assignment should not contain any contents including references cited from website like [www.ukessays.com](http://www.ukessays.com), [www.studymode.com](http://www.studymode.com), [www.slideshare.net](http://www.slideshare.net), [www.scribd.com](http://www.scribd.com).
6. Students can refer Wikipedia as a source of information, but the references cited in Wikipedia has to be mentioned.
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2. Original cover sheet and format retained.
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ASSIGNMENT INFORMATION	
Full/ Part Assignment	Full
Date Assignment Issued	02/08/2019
Date Assignment Due	
Assignment IV by	Dr. Vivek Mohan

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Course	MBA in Accounting and Finance
Date Submitted	18 <sup>th</sup> May, 2020

TO BE FILLED BY THE ASSESSOR		
Assessment types	Marks	Marks Awarded
Question 1	15	12
Question 2	20	15
Question 3	15	10
Question 4	20	15
Question 5	30	22
Overall Marks	100	74
Overall Grade	Distinction	
Assessor's Name	Linimol Ansalam	
Summative Feedback by Faculty for further improvement		
The candidate has exhibited a good presentation with proper alignment and answering. The candidate should include illustrations and examples while explaining the core concepts. The candidate should adhere to the Harvard reference system.		



## LO 1: Understand the planning, budgeting and forecasting concepts of finance management

*“A budget is a short-term plan of how an organization quantifies the operational activities required to achieve its long-term strategy.*

*It is a common mistake to assume that automation alone will bring necessary budget process improvements to an organization. Automating an inefficient or unintelligent budget process just makes the same process faster, not better.*

*The reality is traditional practices that govern budgeting, planning, forecasting, reporting and risk management are becoming obsolete in the context of a fast paced digital marketplace and a volatile and uncertain global economy. Long established budget practices provide a false sense of security and fail to cope with the speed and volatility of today's markets.*

*Additionally, the traditional budgeting process is widely decried, both by FP&A personnel—who must reconcile the requests from business managers with the targets handed down from the C-suite—and the business line managers they support—who view the budget process as a bureaucratic exercise, a distraction from their job, a drag on their time, and a purely finance-driven process.*

*As you consider a new budget system for your organization, remember this is the optimal time to evaluate the current strategies that can help your organization develop a more agile and intelligent budget and forecasting process, use this process as decision making tool rather than a negotiation, and positively change your organization's perception on budgeting, planning and forecasting techniques.”*

**Question 1:** *In reference to the above views on budget systems, explain relevant strategies and practices that you would consider for your chosen organization to improve its budgeting, planning and forecasting techniques. [15 marks]*

## LO 2: Understand the control of performance management and internal control environment for risk control



*In many smaller, unincorporated businesses such as sole traders and unlimited partnerships, the responsibility for internal controls often lies with the owners themselves. In most cases, the owners are fully engaged in the business itself, and if employees are engaged, it is usually within the capability of the owners to remain fully aware of transactions and the overall state of the business.*

*As organizations grow, the need for **internal controls** increases, as the degree of specialization increases and it becomes impossible to remain fully aware of what is going on in every part of the business.*

*In a limited company, the **board of directors** is responsible for ensuring that appropriate internal controls are in place. Their accountability is to the shareholders, as the directors act as their agents. In turn, the directors may consider it prudent to establish a dedicated internal control function. The point at which this decision is taken will depend on the extent to which the **benefits** of function will outweigh the **costs**.*

*The directors must pay due attention to the **control environment**. If internal controls are to be effective, it is necessary to create an **appropriate culture** and embed a **commitment to robust controls** throughout the organization.*

**Question 2:** Answer the following questions.

a] *In reference to the above given opinion, explain in your chosen organization, what are/could be the various factors that impact responsibility centers to clearly bring out the type of responsibility each of these centers have. Also analyze the performance measures established as controls which you believe would be appropriate to monitor and evaluate the performance of each of these responsibility centers.*

b] *Describe the business of your chosen organization. Briefly explain the various types of internal controls mechanism put in place to control the operational risks in your organization.*

c] *Explain the role and importance of Audits in your chosen organization. Also mention the different type of Audits that exist while describing the role of Internal Audit department towards assessing adequacy of accounting systems.*

[Total-20 marks]

**LO 3: Understand the financial statement and decision analysis, including risk management**

**What's keeping UAE businesses awake at night?**

*The Middle East encompasses a broad range of economic, financial, political, and social risks on a regional and country-specific basis. ICAEW's Economic Insight: Middle East is a quarterly economic forecast specifically for the finance profession, which has shared the following outlook as at Q4 2016:-*

- **Risks to an already-weak oil price.** *Even in a more positive scenario, oil prices will not return close to the \$100 per barrel (pb) averaged in 2010–2014. Our baseline forecast remains below \$60pb until 2019.*

• **Rising tax burden.** *Businesses are concerned about potential tax increases and spending cuts to shore up government finances. This could prompt lower demand, administrative burdens for businesses (a particular blow to small and medium-sized enterprises), or loss of retained earnings for future investment. Moves to boost employment of national born workers could also place a strain on the business.*

• **Exchange rate risk.** • *While pressure on exchange rate pegs has eased, businesses remain worried about the potential impact on costs if a move to more flexible exchange rates seems likely.*

• *These worries are keenest where set government budgets mean large deficits. Oman, Bahrain, and Saudi are most exposed with fiscal 'breakeven' oil prices \$30–\$50pb above current levels.*

*“A full implementation of President-elect Trump’s policy proposals would lower oil prices by \$10pb by 2020.”*

### **Question 3:**

*Evaluate the above-given information in terms of impact underpinning organizations in UAE required to embrace a long term effort by the government to close fiscal deficits and raise increased revenues from the non-oil economy. This could also place many pressures on businesses, particularly w.r.t higher labor costs, weaker consumer demand, and the loss of retained earnings for future investment strategies & better liquidity practices. [15 marks]*

### **LO 4: Know the shareholder/ corporate value creation, including M&As and disposals**

*Mergers and acquisitions (M&A) executed in UAE markets in 2016 highlight companies' well-implemented wealth management that contributes to the general economy and the private sector, analysts told Mubasher.*

*Statistics by Mubasher show that the top M&A deals carried out in the UAE totaled AED 657 billion (\$178.99 billion) in 2016 and involved 13 companies.*

*First Gulf Bank's (FGB) merger with the National Bank of Abu Dhabi (NBAD) led M&A deals in the Gulf country. The merger deal will result in creating the UAE's largest financial institution with total assets worth nearly AED 655 billion (\$178 billion).*

*Coming in second place on the list is AlSafwa Islamic Financial Services' merger with Mubasher Financial Services (MFS), which brought about Al Safwa Mubasher Financial Services as of 16 November 2016, with a capital of AED 563.88 million.*

*M&A deals carried out under the current difficult economic circumstances help companies boost their financial positions and their competitive edge as well as help reduce costs and operating risks, commented market analyst Mohamed Al-Azmy.*

*Market analyst Nawwaf El-Tayea noted that one of the main benefits of M&A deals is that they reduce the time needed to create a new company. He added that these deals often result in quick revenues for the companies.*

**Question 4:** Answer the following questions.

- a] Define the factors that will drive shareholder value in your organization. Also describe, giving reasons, if or if not a focus on shareholder value creation will lead to better decision making in your organization?*
- b] What is the meaning of Value-Based Management and evaluate the methods to measure achievements in an organization. Describe the key factors that drive corporates to undertake restructuring such as M&A etc.?*
- c] Explain the steps involved and describe the key steps followed in an M&A and divestment transaction. Analyze the following situation and provide your opinion.*

*Acme Engineering is evaluating options for its steel fabricating division. In 2013, the division has sales of \$ 400 million but reported an operating loss of \$ 35 million. The company believes that the division has potential to turn around but ACME's senior management has not been able to focus their attention on this division as it constitutes only 25% of its total sales with the balance coming from its heavy machinery division which had sales of \$ 1,200 million and an operating profit of \$ 150 million.*

*Describe, giving reasons, what should, in your view, be a possible restructuring option that the company could consider for its steel fabricating division assuming that division has a value of \$ 80 million. Also briefly outline the process that the company should follow to implement your suggested option.*

*[Total-20 marks]*

**LO 5: Understand the control and management of operational and financial risk in a business**

**Question 5:** Answer the following questions.



a] In your chosen organization, explain what are the different types of businesses and financial risks faced by it in the conduct of normal business operations and the decisions involved in it?

b] What is meant by internal risk environment in an organization? Analyze the given situation below and provide your opinion as to what led to the failure of the said institution.

#### **Case Study 1: Washington Mutual**

- 2004: Embarked upon a lending strategy to pursue higher profits by emphasizing high-risk loans
- 2006: High-risk loans began incurring high rates of delinquency and default,
- 2007: Mortgage-backed securities began incurring rating downgrades and began incurring losses due to a portfolio that contained poor quality and questionable customers. (Source: Wall Street and the Financial Crisis: Anatomy of a financial collapse began incurring losses due to a portfolio that contained poor quality and fraudulent loans and securities. Its stock price dropped as shareholders lost confidence and depositors began withdrawing funds, eventually causing a liquidity crisis at the bank)
- 2008: Seized by its regulator, the Office of Thrift Supervision (OTS) Placed in receivership with the Federal Deposit Insurance Corporation (FDIC) Sold to JPMorgan Chase for \$1.9 billion.

#### **Case Study 2 – Barings Bank**

On February 26, 1995, Barings Bank (Barings) - the United Kingdom's (UK) oldest and one of its most reputed banks - declared it was bankrupt. The bank with a total net worth of \$900 mn had suffered losses above \$1 bn.

These losses were the result of the gross mismanagement of the bank's derivatives trading operations by Nicholas William Leeson (Leeson), the General Manager of Barings Future in Singapore (BFS).

BFS had been established to look after the bank's Singapore International Monetary Exchange (SIMEX) trading operations. Leeson's job was to make arbitrage profits by taking advantage of price differences of similar contracts on the SIMEX (Singapore) and Osaka stock exchanges. Despite not having the authority, he traded in options and maintained an un-hedged position. He acted beyond the scope of his job and was able to conceal his unauthorized derivatives trading activities.

Due to the senior management's carelessness and lack of knowledge of derivatives trading, the bank landed up in a major financial mess.

When Barings finally went into receivership on February 27, 1995, it had an outstanding notional futures position on Japanese equities and bonds of US\$ 27 bn (US\$ 7 bn on Nikkei 225 equity contracts and US\$ 20 bn on Japanese government bond (JGB) and Euro yen contracts).

*Analysts said that the situation demanded that banks the world over must tighten their internal control procedures.*

*c) Based on the above case study explain in your opinion the risk management instruments that could have been applied for avoiding a financial risk situation.*

*[Total-30 marks]*

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## Question 1

### INTRODUCTION

Etisalat Telecommunications Group Co PJSC was the world's 14<sup>th</sup> ranked mobile operator in the year 2014 and 140<sup>th</sup> in the world as per Financial Times Global 500 ranking in terms of market capitalization is one of the biggest and leading telecommunication services. As of today, Etisalat service subscriptions exceed 167 million. It was also the only mobile operator until 2006, in the United Arab Emirates. After which Du operator who entered the market and now owns 37% of local market share.

The head-office of Etisalat is based in the emirates of Abu Dhabi. It was inaugurated in 1976 by the British company International Aeradio Ltd and the local partners. Later in the year, 1983 ownership changed when the UAE Government acquired 60% and the remaining shares were sold at public auction.

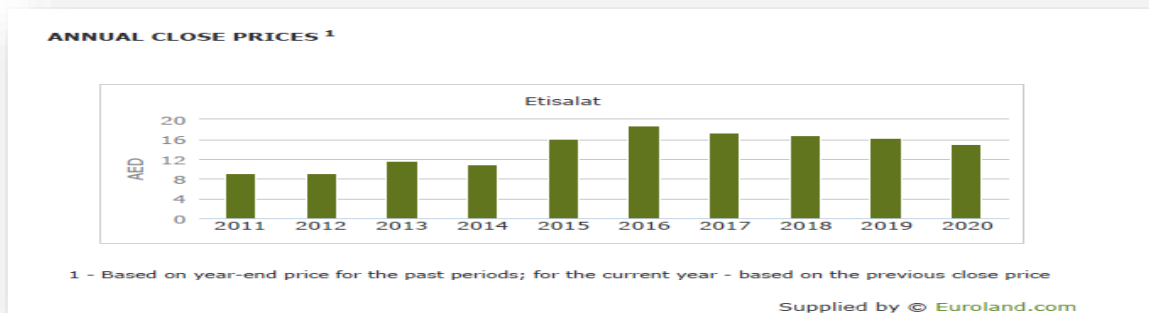
The historic development of this telecommunication goes back to 1991 when the UAE government permitted the wired and wireless telecommunications services is when the Etisalat became the monopolist in the industry for UAE. Later in 1994 they introduced GSM and was the first internet service provider. In 2002, GPRS was introduced and two years down they managed to unveil 3G networks in the Middle East. It was in 2010 when Etisalat successfully implemented the fiber-optic networks and launched 3DTV and became one of the only 5 countries around the world with the service. In 2018 was a disruptive technological achievement as the first telecom operator in the MENA region when the first 5G wireless network was presented.

Chairman Obeid Al Tayer stressed the importance of the futuristic solutions from Etisalat moving towards 5G in the current Covid-19 pandemic. Which can serve remote businesses, entertainment, education and have the potentials of clients present and future needs? It positioned itself to bring futuristic solutions to government, businesses and the public having re-emphasized their efforts in digital innovation and leadership as telecom brands regionally and globally.

Etisalat has a rich history of innovation and technological feat. The telecommunication giant blue-chip offered innovative solutions to 148 million subscribers these services in 18 nations across Africa, Middle East & Asia. With its broad variety of services from voice and data services through mobile, fixed landline services, internet access, and wholesale network

services to other carriers. The E-vision department provides digital cable tv's and installs and E-Marine maintains submarine communications cables in the Mediterranean Sea.

There are representative branches located in New York, Paris, London, Frankfurt, Amsterdam, and Singapore, and Etisalat has over 10,000 employees of the team.



[Etisalat, 2020], [Dubai-Freezone, 2020], [D&B Hoovers, 2020], [Issac John, 2020]

Its present market value is AED148 billion. The consolidated net revenues at AED 52.2 billion and profit of AED8.7 billion in the year 2019. It has high credit ratings showing a strong balance sheet and assured long-term achievement. Etisalat went public in 2002 in Abu Dhabi Securities Exchange, with a share price of AED 15.36 with net income growth of 0.89%.



[Bloomberg, 2020]

The vision of Etisalat is its strategic plan. It identifies the future goals to promote its strategic, leadership, and other decision processes. And the mission is to focus the committed and



talented workforce to seek to expand contributors' values and to give innovative services, from the beginning to facilitate customers to face their strategic ambitions.

[[www.etisalat.com](http://www.etisalat.com)]

## **Budgeting, Planning & Forecasting Techniques**

Budgeting, planning, and forecasting is generally a 3-step process for shaping and arranging out an organization's short and long -term financial goals.

**Budgeting** is the process of producing comprehensive projections of future cash flows. It is an annual practice for every company. Including several variables in the operating environment and concentrating entity's strategic objectives is how the budgets are prepared. Organizations involve mainly in two categories of budgeting:

- **Operating budgeting**

Projections of sales, productions, departmental expenses, etc. once prepared and authorized will project the next financial year's guidelines controlling the business activities.

- **Capital budgeting**

Cash budgeting engages future projects over many accounting periods. It is used to detail each project along with its fund expenditures and expected cash inflows for each year. It must also be discounted to their current worth and arranged by priority and advantageousness.

## **Elements of a Master Budget**

An organization consists of several departments hence budgeting for each department is relating to its requirements. When all the budgets from each division are incorporated, it is known as the "Master Budget".

- Sales budget
- Production budget
- Cash budget
- Direct material purchase budget
- Labor budget
- Overhead budget
- Selling, general & administrative budget

[Harold Averkamp, 2020]

## **Approaches to the budgeting process**

There are many ways to approach budgeting. Amongst two main approaches to budgeting process are;

- **Top-Down Budget** – essential input is finished by the c-suite of the business. Lower level management is associated in executing these guidelines on i.e. sales, compensation for the achievement of financial goals.
- **Bottom-Up Budget** – it is more of an umbrella approach to budgeting. Despite upper management providing general instructions, but lower management developing the budgets.

Etisalat can use more of a top-down approach given it can look at more of the big picture and macro variables. It will analyze how systematically each factor will fall into place to achieve the desired outcomes.

## **Steps in the Budgeting Process**

It is an exhaustive process with sophisticated steps opening to recognize the overall picture.

### **○ Budget hypothesis**

To do a budget, there will always be assumptions for examples of sales trends, cost trends, etc. Before commencing on creating a budget, these guesses must be carefully reviewed according to the recent environmental conditions.

### **○ Availability of funds**

Constraints of capital can severely cripple the growth project of the business. As the available investable funds will govern the inception of feasible projects.

### **○ Analyze costing factors**

Every business expects to face changes. There could be exposed daily to challenges that demand a complete change in the cost structure. Therefore, before a budget, we must carefully consider all the points that could affect the costing for the budget to be practical.

### **○ Budget standards**

The standards used in previous budgeting must be modified according to more up to date environmental conditions.

### **○ Gain revenue forecast**

The sales budget is vital for all budgets. As it also decides if the business is making enough profits for survival. Therefore, sufficient attention should be focused on preparing the sales budget by proper demand forecasted.

### **○ Justify remuneration**

It is a huge part of the budget as annually there will be increments. Therefore, approvals must be granted from executive management, hence added to the budget plan.

### **○ Attain capital budget**

Growth of business depends on how many capital expenses incurred as it aids to seize opportunities required to develop. Therefore, any plans on Capex should be added to the budget.

- **Check the budget**

An intensive review must take place to eradicate any errors to avoid unbalance in the budget sheet.

- **Approvals**

It must be forwarded to the top management for the appraisal to assure the budget is following the company's goals and make final changes if any before approval.

- **Budget issue**

Once approved by the top management it will formally issue so the operations take place accordingly.

## **4 Types of Budgeting Techniques**

### **a) Incremental Budgeting**

Based on the previous year's actual figures, adding and deducting a % to achieve the present year's budget is incremental budgeting.

**Pros:** due to its clear and easy to understand it is the most common type of budgeting given the main cost factors do not change yearly.

**Cons:** it can preserve inefficiencies e.g. knowing the increased 10% annually to spend on the department the manager can take bigger budgets unjustified. Budgetary slacks and can overlook the external factors i.e. inflations.

### **b) Activity-based budgeting**

It is a top-down reach that regulates the number of inputs needed to aid the aimed outputs goals of the company e.g. the number of activities required to achieve a targeted sale, accordingly, find out the cost involved in achieving the targeted outputs.

**Pros:** considers each cost driver, it gives a competitive edge by removing all unrequired activities, looks at the business at a unit, eradicates barriers.

**Cons:** it demands a sound understanding of different activities, research & analysis recommended for factors, therefore, needing to assign officers to engage in this activity which gives rise to cost involved and short-termed.

This technique seems to best suit Etisalat given all different telecommunication service variety provided. Hence, they can calculate for each activity the cost and use it for budgeting purposes to allocate resources or compare the expenses against its activities achieved.

### c) Proportion Budgeting

This looks at the budget in an angle to ensure that every aspect is taken into consideration in the budget must have a value to the business. Therefore, zero allowance of unnecessary spending, however not as much as zero budgeting.

**Pros:** clarity by quantifying targets, prioritize essential activities that are critical.

**Cons:** engagement of both top & bottom employees can create chaos, being subjective, and having the autonomy to the management to decide on their instincts can be irrational.

### d) Zero-based budgeting

The specialty in this technique is that is assuming all department budgets are zero and every single expense must be justified nothing is irrelevant or automatically approved. The aim is to cut down all expenses that are not essential to profit and mostly used for when the budget is very low, or the organization is having tough times.

**Pros:** it is a perfect match for looking into unrestricted expenses more than a compulsory operating expense.

**Cons:** having to check each expense can be time-consuming

[CFI, 2015], [Rick Yvanovich, 2019]

**Planning** furnishes a structure for a business's financial objectives for the coming 3 to 5 years.

It is the process of thinking with regards to the future action plan vital to achieving a goal. It provides answers to how, when, and what is to be executed with best, worst & most case scenarios. Therefore, it is a target-oriented activity that creates future development of actions and gives the future atmosphere of the company.

### Planning Types

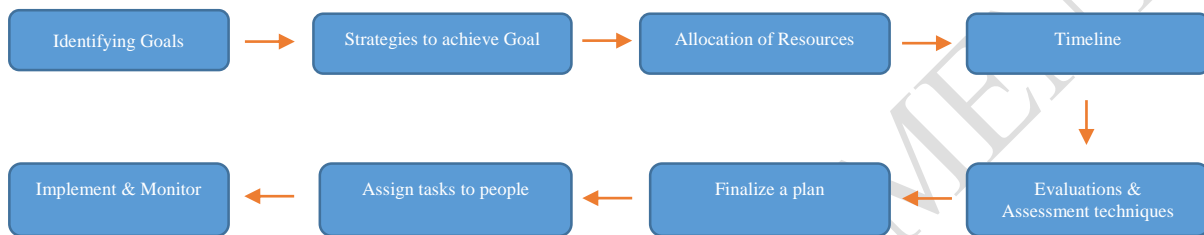
- **Operational planning** – done by lower-level managers for daily operations.
- **Tactical planning** – strategic planning relating to different parts of the organization.
- **Strategic planning** – done by top management i.e. CEO for the long term 2 to 5 years goals of the organization.



## The advantages of planning:

- Growth of productivity
- Profitability
- Rise of customer relation
- Surge the return on investment

## Steps in Planning



As the future is ambiguous, planning is pushed to have certain guesses. These guesses belonging to the future are forecasting, which is founded on past trend, economic condition, and information.

**Forecasting** takes past data and present market situations and then forms prophecies as to the amount of revenue a firm can predict for the coming few months or years. With every new information available it will be altered to mitigate future uncertainties.

## Type of Forecasting

- **Quantitative & qualitative forecast** – past figures data is quantitative & personalized attitudes is qualitative forecasting.
- **Time series forecast** – a club of data is accumulated over a distinct period. It believes trends repeat over a long period of 5, 10, 15 years. Examples of the method are moving average, exponential smoothing, trend analysis.
- **Judgmental forecast** – established on subjective measures and instinct.

## Steps in forecasting



## **How Technology can make the process easy**

Technology itself can't replace the planning, forecasting & budgeting process. However, it can help incorporate corporate performance management solutions through purchasing as an off-the set-shelf solution provided.

Planning is simpler and more effective. It helps practices augment periods and security of information and develop involvement by the main people of the organization, especially at the front lines.

### **Advantages**

- customized user-friendly interfaces to measure and monitor performance through interaction, self-service dashboards, and graphical visualizations.
- Check deep causes with utmost devotion scrutiny of structurally rich data.
- Calculate trends and make forecasting automatically from both internal & external data.
- Execute speedy what-if scenario demonstrating and create well-timed, stable, plans, and predictions.

[Madhuri Ma, 2018]

## **Etisalat Financial Planning Strategies**

As the leading telecommunication provider, they seize every opportunity that comes their way to maximize profit potentials. With the international investments aiding the long-term development strategies. Financial planning and budgeting are as per current trends and conditions. Below are strategies forested and implemented in Etisalat to future proof itself in the market and to increase its share value.

Analyzing the growth in the population in the UAE was taken into consideration to capture the more users to their services. Hence in 2009, they reduced the internet broadband charges by 40% to increase the subscribers to their services.

In 2008 Etisalat signed a contract with the Ministry of Education to provide UAE government schools with IP/MPLS internet connectivity and technical support service give them a stable business and entering the education sector.

In 2010 Etisalat planned to increase its market share with a margin of 15%. Focusing on marketing operations, to cater to a massive number of subscribers around the country to experience modern telecommunication technologies.

Until 2015 foreign direct investments in UAE's telecommunication industry were not allowed. However, after the negotiations with the World Trade Organizations in 2015 for allowing foreign competition to touch the market Etisalat will have to focus on how to tackle not just the internal competitor DU but as well as multinational competitions from giving intense competition.

With the continuous profits and market share acquired by Etisalat, they have enough cash flow to provide investments in together contiguous product categories. It also helps the organization is investing in new technologies and new products.

As a Capex expense, Etisalat forecasted and planned on spending on turning to fiber optic cable, which increased the international data service access.

As the new technologies adopted also allow them to price differentiation in the market. Facilitating to keep their existing customers and attract new customers.

The economic hike after the previous recession from 2008 onwards helps them to increase their market share with slow growth in the industry.

At present in collaboration with Noor bank, they launch a digital financial services e-Wallet for international remittance service letting financial transactions between UAE residence and around 200 countries.

The sustainable reason behind their success is also the continuous investments in the latest technologies, network infrastructure, and spectrum license targeting empowering shareholders, clients, and society.

In 2019 Etisalat's other strategic plan is executed when they enter the 5G network in the UAE and allowing its penetration in Africa.

The organization also preserve exercise of large cash forming to reach to benefit the shareholders and growth in business.

Etisalat is also leveraging its cloud computing promotions, to add big data, applications, and vertical-specific with services such as cloud hosting, cybersecurity services, email solutions & mobile device management relating to health, education, and government sectors.

[Etisalat, 2020], [Mark Sutton, 2014]

## **Importance of Budgeting to Etisalat**

- ❖ Deliver as a tool to administer and audit the targets for revenues, expenses, and goals to be achieved.
- ❖ Capital expenditure for strategies can be formulated in this stage of planning budgets for the growth of the company.
- ❖ It manifests the priorities and urgencies of the business through the distribution of funds to different divisions and what is expected of them.

- ❖ It is a great way of controlling spending and eliminating unnecessary resource allocation to less important aspects.
- ❖ It helps with the proforma financial statements by forecasting so the business can track its profit margins.
- ❖ Rectify and examine the impact of changes as they occur.
- ❖ Heighten the relationship between the operational and financial plan
- ❖ Evaluate variances and detours from the plans therefore quickly take measures.

[Martin Luenendonk, 2015]

## Question 2

### A. Identity Responsibility Centers

It is a sub-unit of an organization in which centers can be categorized by the outlook of obligation appointed and decision-making authority given to separate managers.

#### Types of responsibility centers

##### a) Cost Center

Expenditure or cost-related section of an entity in that the managers are accounted responsible for only the expenses incurred. Cost center managers have handled over all or some costs in their division, but not over revenues. The managers are responsible only with regards to the controllable costs involved in such as front desk operations.

Examples of cost centers:

- Maintenance department
- Manufacturing divisions or businesses
- Product and service divisions
- Administrative, accounting, and human resource department, etc.

Etisalat has its cost centers such as managing contracts, customer service, manage carrier interactions, work orders of maintenance and disputes, maintaining telecom inventories of assets and services, etc. incurring costs.

##### b) Revenue Center

They mainly focused on attaining sales incomes. The manger is not responsible for the cost, investment aspects to improve market shares. However certain expenses such as sales and marketing costs can be controlled. Revenue centers will control the price, promotional activities, etc.

Examples of revenue center:

- Regional sales office in a national or multinational corporation
- The Marketing-manager of a product line



- Individual sales representative
- a book shop in a department store

In Etisalat, the revenue centers associated with the Etisalat service centers or workshops selling all types of telecommunication services they pose (postpaid & prepaid mobile call plans, eLife home entertainment plans, Wi-Fi internet connections, 5G services, etc.) and the sales promoters are revenue centers for Etisalat.

### c) **Profit Center**

A profit center section of a business is responsible for both expenses and revenues. The manager is responsible and has the authority to make decisions and choices that can influence both controllable costs and revenues of the department and control them.

It is involved in seeking ways to expand income by increasing production or advance distribution methods. The managers are enthused to decide concerning the activities and operations of the department. They are usually created in product or process and given full freedom of obtaining supplies and making sales.

Examples of profit center:

- Supermarket profit center departments: men's clothing, women's clothing, toy, shoes
- Product or an industrial division responsible for sales and expenses
- The manager of one of the outlets in a chain of stores responsible for pricing, product range, purchasing and promotion

### d) **Investment Center**

Investment centers are responsible for investments as well as profits. The investment manager has supervision over expenses, revenues, and the invested capital in the center's assets. He will devise the credit policy which has a direct effect on debt recovery, and the inventory policy will control the investment in inventory.

Therefore, it is visible the investment center manager has more authority and responsibility than other types of responsibility center managers. Through which he can invest in correct assets, enhance the organizations' vision and mission, guide the team for recommended mergers & acquisitions, transit to e-commerce, etc.

Examples of investment center:

- Giant corporation with several subsidiaries, giving authority to the subsidiary president to make decisions regarding investments, who will be held responsible.

i.e. CEO of Etisalat Al Abdooli for UAE is responsible for its research development, innovative new technological infrastructural transitions with the cost involved to implement, and to forecast the profits they could generate.

[Lie Dharma Putra, 2012],

### **Performance measures established as controls to monitor and evaluate the Performance**

- **Cost center**
  - i. Short-term performance measures budgets are the expense assessments for controlling, it is evaluated by cross-checking the actual variance in the cost against the budgeted standard cost of the projected period.
  - ii. Long-term efficiency is achieved through benchmarking a range of activities and processes against top performers in the industry.
  - iii. Non-financial measures evaluate the quality aspects of the center by achieving timely production goals, employee health & safety measures, response time, etc. to evaluate performance.
- **Revenue Center**
  - i. Analyze budgeted revenues against actual revenues.
  - ii. Direct expenses of the revenue centers i.e. advertising, salaries, selling costs will be minus from the sales revenue.
- **Profit Center**
  - i. It is correlated to the results if the center has accomplished the budgeted profit.
  - ii. Unit basis profitability study using ratio techniques to find more specific profit.
  - iii. Compare with past performance, industry performance.
- **Investment Center**
  - i. Use of calculations such as return on investment.
  - ii. Residual income rates.
  - iii. Economic value added by the investment.

[Ebrary, 2014], [Etisalat Services Holding, 2020]

### **Factors impact responsibility centers**

#### **○ Shareholders**

They are the owners of a company. By selling shares of the asset, or partial holding in the business, in change for equity investment to function the organization. They typically impact organization operations and various decisions differently to other stakeholders' interests with

the business. In Etisalat 60% of its ownership belongs to Emirates Investment Authority and 40% free float.

**How these shareholders can affect the responsibility centers through:**

**i. Profits**

- Every shareholder ultimate objective is to maximize profit.
- Therefore, they will be extra keen on the performance of the profit centers.
- However, organizations try to strike a balance between the shareholders and other related parties' interests.

**ii. Short-Term focused**

- Generally, their ambition is instant results oriented.
- Therefore, listed companies like Etisalat the executive management will have immense pressure to achieve revenues putting pressure on revenue centers to bring profit rapidly.
- This conflicts with the long-term entrepreneurs who don't want to compromise the stable vision just for short-term ambitions.

**iii. Strategic Planning**

- In some instances, top management oversight philanthropic hunts to alleviate shareholders' financial goals.
- Some shareholders focus on financial benefits and social & environmental responsibility.
- While others might overly stress on cost controls with labor involving cost centers to diminish business costs.

○ **Senior Management**

Senior management is responsible for developing individual and corporate values along with behavioral expectations for the company to aid the application of the management system.

**i. Set Objectives**

- setting goals, strategies, plans, and objectives by company objectives.
- It must be measurable objectives to direct towards goals.
- Establish the enforced plans that are frequently examined against the objectives and take necessary action plans to alter any deviations.
- Approving seeking investment to a certain level.

**ii. Organize**

- Senior management will regulate the number of resources dedicated to carry out the activities of the entity and to authorize, complete, evaluate, and continuously develop the management system.
- Manage the information and knowledge as a resource.
- Make sure the employees are skilled to perform assigned tasks.

### iii. Measure

- Authorize correct measures and targets, and check and clarify performance.

[James Foster, 2017]

## Recommendations

### Decentralization

- ❖ It will help make better decisions as the local managers know better the market conditions in which they operate hence creating more precise decisions.
- ❖ Decisions can be prompt as it will involve the lease of the top management and it allows the top management at the same time to focus on strategic planning.

[Chris Joseph, 2019]

### Departmental financial report

- ❖ Having a departmental gross profit method helps control the gross profit and gives a proper idea of the return on investment etc.
- ❖ It will rectify separately itemized losses and raise the manager's attention on the cost. It will motivate the employees as well as showcase the contribution of each department.

## Conclusion

Having a manager in each responsibility center allows accomplishing authorization and control aside from evaluating the performance that acts as an encouragement factor.

It is important to do efficiently the analyzing and evaluation of the performance without getting too focused on process-oriented as that might lose the bigger picture of fundamental objectives to be achieved.

For Etisalat which is into telecommunications and digital technology which constantly faces rapid changes identifying and evaluating the performance measures can help stay in objectives and eradicate unwanted spending, support sustainable required investments to be taken responsibly by the respective managers and also analyze the growth of the business and to make forecast potentials opportunity decisions on time.



## **B. Business operations involved in Etisalat**

Etisalat is the largest telecommunication service provider in the UAE. Having individual and corporate clients they provide service operations ranging from online payment portals, customer loyalty benefits mobile apps, mobile online registration renewals, postpaid and prepaid calling packages, eLife home entertainment packages, speed Wi-Fi connections over fiber optics, 4G & 5G. It also has produced such a smart device that could be purchased through packages of postpaid plans on an installment basis.

They provide strategic and operational backing to all their operating firms to sustain and grow market values by safeguarding and increasing the business important areas boosting digital potentials.

Etisalat is stressing on enhancing invading packages, such as switching prepaid consumers to postpaid and enlarging value from customer base over customer value management operations.

Determined to become more rapid, digital, and productive they are the first in the Middle East & North Africa is the 4<sup>th</sup> to launch 5G with attempts to increase shareholder value.

The company is extremely focused to obtain digital reconstruct by attaining exceptional digital customer experience, being super-fast, creating greater digital income platforms, and heightening the competence.

With the implementation of 5G, they also plan to achieve network virtualization and endorsement of cloud on the route to programmable and software directed networks.

Involvement in remodeling IT architectures founded on open APIs together with DevOps techniques are some of its IT operations.

[Etisalat Annual Report, 2020]

## **Responsibilities of Internal Control**

Internal controls are the mechanism, policies, procedures, guidelines, and actions instrumented by a firm to mitigate asset lost, establish accounting data is accurate and escalate the efficiency of the operation and encourage an environment of compliance among the people working to make sure the plan information is thorough and precise.

Adequate internal control systems will cater to a fair assertion regarding the ability of recognized objectives.

❖ **Productive management of business**

Structure in position to assure that all activities are documented through internal policies.

❖ **Preserving assets**

Taking care of the properties from thievery and other physically dangerous situations which may inflict damage to workers. As well as intangible assets such as intellectual rights that must be patent protected.

❖ **Prevention & detection of hoax and error**

it will have the fraud and blunders at operational capacity to a strategic level.

[Dico, 2005]

### **Types of internal controls**

▪ **Detective**

These controls are in place to rectify inaccuracies post happened. It supports to review and balances procedures and regulate how productive protocols are. Detective controls benefit safeguard assets and will take place irregularly.

e.g.

- a) Conducting inventory counting checks
- b) Internal audits
- c) Past performance review of different divisions and budget variance analysis
- d) Peer reviews
- e) Enforce job requirements and anticipations.

▪ **Preventive**

The purpose of preventive internal controls is to avoid blunders from happening. They take place on a frequent base. It is the most cost-effective control as it helps prevent the loss of assets before it takes place.

e.g.

- a) Password-protected access to asset store locations
- b) Physical locks on stock warehouses
- c) CCTV security camera systems
- d) Taking backups of computer data

- e) Physical and drug tests for staff
- f) Setting passwords to each user and system users.
- g) Employee background check
- h) Employee monitoring and skill upgrading programs
- i) Segregation of duties
- j) Entitled vacations

#### ▪ **Corrective**

Corrective internal controls exist to correct the errors rectified in detective internal controls. When a mistake happens, the staff must take any measures in place to correct it.

e.g.

- a) Training programs can prevent future errors
- b) Progressive discipline for faults
- c) Data backups to restore if the loss of data in a natural disaster
- d) Insurance can aid if assets damaged or stole

[Michelle Furlong, 2019]

### **Etisalat internal controls in place to evaluate and monitor operational risks**

#### ❖ **Physical Controls**

These are the measures and systems to secure assets against thievery and illegal break-in and use.

- Security camera installation
- Installing security entry to the building
- Double safekeeping of valuable assets, hence the access will require both to authorize.
- Stock counts of inventory

#### ❖ **Management Controls**

- Top management reviews on performance reports related to the organizational objectives.
- Address the lower management of control activities in place.
- Horizontal department wise reports on performance reviews.
- Operational functional reviews.

#### ❖ **Supervision**

- There must be one team-leaders maintenance workshop to direct the rest to get the work done and to have responsibility for the tasks to be achieved.

#### ❖ Enterprise risk management and compliance exercise

- Audit committee authorized actions in place to add security exercises and correlative with compliance tasks across the group.
- Scrutinizing each area of work and rectifying risks involved in that area in line with international ERM adoption methods.

#### ❖ Cyber Security

The outside threatens over the internet is always there for a telecommunication giant like Etisalat. However, they have controls such as:

- Dedicated Network & its security members aggressively supervising activities on their network.
- Work on reducing existing cyber threats and personal data privacy cracks.

#### ❖ Continuous service

the preserving success of their services is because of the continuous effort to excel in their operations. They need to overcome intimidations of interruptions, faults, losses caused by natural calamities, and unexpected impediments.

- Launch a business continuity management team to establish and scrutinize these plans and crisis management preparations.
- Having proper insurance schemes to provide for infrastructure asset harms.

[Etisalat, 2016]

### C. Importance of Audit to Etisalat

Etisalat Group has built an excellent control environment for its service fields and exercises by carrying out itself to the top-notch governance regulations throughout its operations.

#### **External audit**

They also have set a foundation for participation with external auditors to consistent reports in line with IFRS (International Financial Reporting Standards). The external audit is considered as one of the basic control facets for the work atmosphere that assures the integrity of operations and secures the passion of its shareholders. Thus, making sure both UAE corporate standards and accounting standards are met in the policies set by the organization.

#### **External audit policies**

- Structure of its obligation.
- Dismissal
- Resignation

- Necessary qualities
- Duties
- Permitted work scope

### **Crucial duties of the audit committee**

- Oversee the quality and integrity of company financials.
- Establishing and carrying out a policy for contracting with the external auditor.

### **Internal audit**

In 2016 Etisalat won the Best Practice Award in Internal Audit for the sector over the 5<sup>th</sup> Chief Audit Executive Conference arranged by the UAE Internal Auditor's Association in Dubai, UAE.

The internal audit activities must furnish independent and unbiased pledge and consulting services, adding value and advance the operations of the group. It supports Etisalat to achieve its goals by;

- Building an extensive path to forecast
- Analyze
- Prioritize
- Review
- Promote the application of cost-efficient internal regulation and conformity.

### **Crucial internal controls**

- Assure the formation of indemnity or reaction plan for essential risks and conformance violations if any.
- Observing furtherance in fulfilling agreed accomplishments with constant coverage on their position to the Audit Committee.
- Executing follow-up analysis.

[Etisalat, 2018]

### **Different Type of Audits**

#### **❖ External Audit**

In other words, financial audit or statutory audit pertains to the investigation of the fact and fairness of the financial statements of a company by an external auditor who is independent of the entity by a reporting framework i.e. IFRS. Most countries or jurisdictions demand an external audit on at least a yearly base.

#### **❖ Compliance Audit**

In numerous nations, organizations are required to carry out particular audit engagements in addition to the statutory audit to conform with the obligations of specific laws and regulations.

### ❖ Forensic Audit

It refers to the practice of auditing and fact-finding skills to affairs that might include statutory indications. For examples:

- Fraud investigations: stealing of money, tax slacking, money laundering, insider trading
- Appraisal of loss for insurance claims.
- Discovering of claims of professional evasion concerning to the accountancy profession.

### ❖ Tax Audit

Handled to evaluate the exactness of the tax returns filed by the entity and are hence utilized to rectify the numbers of any above or below the valuation of taxability against the tax authorities.

### ❖ Public Sector Audit

It comprises the investigation of the financial concerns of the government-owned business activities to appraise if they have been functioned in the way that is in the foremost concern of the public.

### ❖ Internal Audit

In other words, an operational audit is a freewill reassessment act initiated by a company to guarantee the efficacy of internal controls, risk management, and administration to alleviate the reaching of the firm's goals.

It doesn't limit financial statements like in financial audits, rather the range of procedures is far and wide that comprehend any issues that can influence the accomplishment of organizational goals.

[iEduNote,2017]

### **Role of Internal Audit department towards assessing the adequacy of accounting systems**

Carrying out an internal audit is intrinsic to frequently supervise and safeguard the organization's assets. It always supports the management to be in charge of all the procedures. Additionally, examine the problem and then arrange a business resolution for such difficulty.

### ❖ Enhance the performance of accounting processes by ensuring:

- i. No deceitful transaction occurs.
- ii. Prudent utilization of assets

### ❖ Serve important intuition by:



- i. The auditor does an extensive investigation of the procedures and discovers all the crucial information about the process.  
For example, if there is inconsistency in the report produced by the accountant, an auditor will figure it out.
- ii. That inclusive observation will permit the management to act for the perspective of the organization.

❖ **Risk Estimates by:**

- i. Judgments at frequent cycles spike the synchronizing of the entity and make it more reliable
- ii. A cycle assessment and communication of the outcome facts and numbers can attract the faith in shareholders and potential investors.

❖ **Compliance by:**

- i. The internal auditors can review the accounting systems if in order with the laws of the state.
- ii. If the policies, actions, processes are compiled by the rules of the region.

[JaxaAuditors, 2020]

## QUESTION 3

### Probing the risks afflicted in UAE

#### ❖ Falling oil prices

Striking fall in oil prices globally after its highest in 2014 of \$115 per barrel declining 2015 onwards triggering GCC states to examine expenditure to safeguard public projects are essential, economical, and effective and to broaden the economies. Reasons behind this are;

- i. The oversupply of oil in the market. One of the prominent oil reserves in the world is facing issues with storage who can hold over 700million barrels.
- ii. The decline in the Chinese economy since 2015, with profits decreasing over \$100 billion in compared with 2014. Indicating further stagnant in growth in 2016.
- iii. In 2016 the remarkable nuclear agreement between Iran and world-leading superpowers. It removed the trading prohibitions with Iran thus adding up to 800,000 barrels per day to the market over the year 2016 alone.
- iv. Additionally, the oil-rich Kingdom of Saudi Arabia turns down to reduce oil production. As a result of all these in 2016 daily excess of 1 million barrels were being produced.

### Impact of volatile oil prices affecting higher labor costs in the UAE

The attitude Dubai has in 2016 for the impact is vigilantly positive. Limiting its oil income to 6% of total revenue and diversifying the Dubai economy. UAE is one of the leaders in diversifying the economy with its peer GCC members, the government took measures such as:

- Increasing public spending by 12% as compared to the previous year \$12 billion.
- Focused on preserving the amount of leverage in infrastructure for long term planning for over 5 years.
- Weighing the expenditures by 37% to coeducation, healthcare, housing development, and neighborhood development.
- Furthermore, investing in Dubai Metro lines infrastructure which is to connect to Expo2020. As well as other projects such as Museum of the Future, Zabeel One and Abu Dhabi on Reem mall.

#### Impact on Etisalat

Amongst the contribution of GDP in 2017 oil stood at 29.5% and amongst the other sectors such as wholesale & retail, construction, Real estate, etc. information and communication sector in which Etisalat operates had a 2.90% displaying the growth in UAE's economic diversification.

Due to this diversification of drive-in UAE, these sectors other than oil show cast a demand for manpower, in return increasing the remunerations of the professionals. Impacting in higher labor costs.

[Linesight, 2020], [The Work Bank, 2020]

#### ❖ **Increasing Tax burden**

UAE and GCC nations presented value-added tax (VAT) from January 2018. It is critical to governmental progression centered on reducing subsidies, raising more income, and bringing down expenditures. It is a constructive growth decreasing dependence on oil revenues. With the continuous irrecoverable decline of the oil prices is it an important move. Tax can help in spending on medical aptitudes, transport infrastructure, public schools, community service, etc.

### **Impact of VAT implementation affecting weaker consumer demand & loss of retained earnings in UAE**

As a result of this short-term inflation would go high far as a residence in UAE are concerned, it will alter their living by way of increment in living cost. It involves spiking consumer inflation, as a result, weakening consumer demand. The decrease in consumer spending will contain the demand, might even result back in deflation. Thus, the final impact on inflation will depend on other drivers such as economic growth interest rates.

However, the creating of new job opportunities to the local-born citizens of the country through tax administration work might also support the boosting employment and to ironically increase the purchasing power. It will also open private sector additional revenues by providing advisory specialize, consulting services to vast companies.

#### **Impact on Etisalat**

As Etisalat is operating in one of the high-powered industries in UAE, it's also a base for the technology, innovation, and development of the economy. Their services in wired and wireless telecommunication leased line services will all be subject to standard vat applied to them.

As far as the demand is concerned there might be an extra burden on the consumers of the services for the groups GCC regional consumers. However, in the long run, people will be adjusted to the expense inclusive of the vat.

lowering demands and incurring implementation and unavoidable related admin expenses such as claiming of accurate Vat, compliance, quarterly returning submissions, updating systems, training staff in VAT processes plus a huge organization like Etisalat will need to appoint dedicated team or consultants specialist to transit and maintain requirements of vat burdens which can cut investments and retained earnings. They must make sure whichever expenses are recoverable to be claimed.

The SME businesses might also have to absorb vat costs to keep their products or services attractive. As it is being small businesses, they wouldn't have economies of scale as much

compared to big giants in the field which might still give competitive prices on their products even after the vat minimizing their costs.

[ADCB, 2019], [Andrew Torchia, 2018]

### ❖ Exchange rate risk

The trend in present-day capital markets lets investors possess securities in foreign markets, generally done through foreign currencies. It allows expansion and yield returns internationally, especially when the local market might not be doing so well.

However, in the process of denominating through currencies might lose the whole effect of reaps of appreciation of asset prices if one of the currencies fluctuates adversely. The reason being the future returns on investment depends on two things; the assets value and exchange rate back to your home currency i.e., if the foreign invested currency appreciates value, rises versus if the foreign-invested currency depreciates the invested value decreases.

### Dirhams peg to US\$

UAE has its currency dirhams pegged to USD on the outlook is one dollar fixed at with the value of the dirham of 3.672 almost always. However, if the US resolves to increase its interest rates they will appreciate the dollar. Which will result in 3 outcomes;

- Increasing the buying power of the dollar
- Discouraging exports of US-based firms
- Higher rates if to borrow or refinancing in dollars.

### Lowering currency risk

- **Invest in nations in which their currencies are pegged to the dollar**  
This is a benefit to the UAE as it will encourage foreign investors to invest more in the emirates. As the value of dirhams will mirror the value of dollars in the international market.
- **Forward Contracts**  
By agreeing on the rate of the transaction for the future date. It supports to manage risks.
- **Option Contract**  
Allowing contract to a fixed rate over a period.
- **Hedge foreign assets**  
Balance the losses arising from the foreign currency, by investing in the equal opposite lead in another.

## **Impact of rate risks affecting lower consumer demands in the UAE**

Due to the fluctuations of the oil prices in the region, adding with sluggish salaries, with the tax application reduced retained earning with the uncertainty in the international market and the complications in getting exchange rates fixed rates for SME companies, etc. can impact adversely to the buying power of the UAE.

[Yazad Darasha, 2019], [Abdulnasser Alshaali, 2018]

### **❖ Better Liquid practices**

Dubai is known for ambitious as growing diversification aids the economy to be more volatile. UAE is placed 17<sup>th</sup> internationally as its competitiveness.

UAE had in 2014 the vision for 2021 inclined to change into a knowledge-based economy. The government aims at 80% GDP to come from non-oil sectors. The vision 2030 of Abu Dhabi recognizes healthcare infrastructure and aerospace as the engines for tomorrow's growth along with service and manufacturing industries.

Their travel to economic broadening has a long way to go. They need to exhaust in industrial expansions which the leaders have identified. The government alone can't, however, achieve this target, with the same ambition and dedication from the private sector is required. With greater coordination, they can bring the change to reality for a better strategically planned future which is more sustainable and reliable.

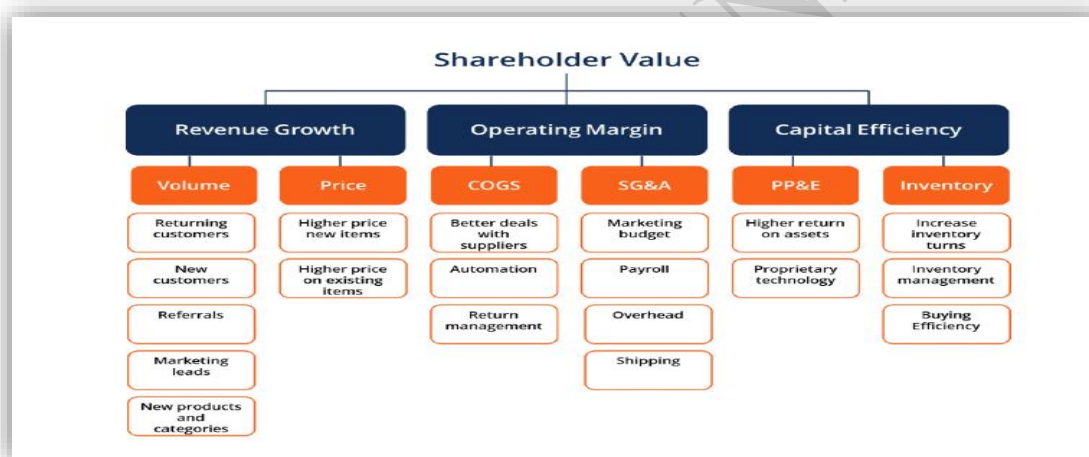
[Issac John, 2018], [UAE Gov, 2020]

## QUESTION 4

### A. Shareholder value in Etisalat

Shareholder value is the commercial value owners received in return for their ownership in the business. In simple when the prospers more than expected it will give worth to it.

Creating value for the shareholders is one of the primary aims for Etisalat. Projects such as the



launch of 5G as the 4<sup>th</sup> in the world attempt to increase the value of its shareholders. It the consistent effort Etisalat is keen on discovering possibilities to perfect its platforms to strike the balance in development and shareholder. Generating strong cash availability and sound debt ratios are ways used to intensify the shareholders' value further. The capital structure itself of the company is in line to sustainably support create value for its owners. Furthermore, assurance is given by their highest credit ratings achieved to solidify their position to the existing and potential investors.

### Factors that will drive Shareholder value in Etisalat

[CFI, 2015]

- **Increase in the number of sales units**  
Create strategies to promote, market, and introduce new services to increase sales units of the services and products offered to its existing customers and to pull new potential customers.
- **Increasing of the selling price**



the company can use strategies to inflate the prices over the periods moderately. It can use enhancement in the products and better qualities to justify more expensive prices.

- **Cost efficiency**

Analyze appropriate ways to cut the expenses in selling, general and administrative costs to effectively administer and reduce costs.

- **Earnings per Capital**

It is to try to increase the return on the capital employed, earnings before interest, and tax. It demonstrates how effective a company is in using funds in operation.

- **Fixed cost optimization**

Increasing the usage of the fixed costs will reduce the per cost unit. Etisalat can use this strategy in their service workshops and branches or in customer service call centers to maximize the customers served within the stipulated period.

- **Consider making acquisitions**

Besides the normal operational profit makings of the organization, acquiring a well-researched and analyzed profit-making prospects can not only increase the profitability in the long run as well as make the company more competitive and recognized in the international context if it's a foreign merger or an acquisition. Example Etisalat acquired Tigo, Hutchison, etc.

- **Dividend**

In the short-term profits for the investment is calculated by the dividends paid. It is a huge deal for the investors, and it gives a view about the management's efficiency to the stakeholders. Therefore, dividend distribution is a very crucial variance to add value.

[Alfred Rappaport, 2006]

### **How to focus on shareholder value creation lead to better decision making**

It is crucial to take the shareholder's interest seriously as they are the owners and the investors who aid the business to sustain and grow. Therefore, maximizing their profitability should be of utmost importance. The organization must know how to increase the value to the shareholder at the same time with short term profitability's at the same time stay focused on the long-term growth of the business.

Shareholders can be the key measurement to evaluate the effectiveness of the management's long-term results. It keeps the business result centric and focused to innovate, research, and add value overall which makes it competitive amongst its competitors. It helps achieve;

- Operational effectiveness highlighted
- Attempt to focus on generating profits
- cut costs and streamline every aspect of the business
- Result oriented and quantitative accomplishment
- Benefits in pulling new investors
- Achieved efficiencies will increase the market value of the business

[Megan Lambert, 2017]

### **Limitation of being shareholder-oriented**

- Profit focus is short term result oriented which is limit the long-term capital investments of growth
- It can lead to stock price influence
- It can discourage the employees with the cost reductions approaches which might lead to the loss of job
- Might lead to less competitiveness globally due to the overspending of dividends and benefits to the shareholders in the short run which compromises by limiting the retained earnings that could have spent to acquire new markets internationally.

[Steve Denning, 2018]

### **Conclusion**

Therefore, bottom-line Etisalat must understand to increase the value for the shareholder is being of utmost importance however striking the balance considering the other stakeholders such as the employees and customers are to be in the equation when pursuing success, especially in the long term. Thus, prepared to be more organized and prioritized when to focus on which party most without hurting the sentiments of the other stakeholders which help better achieve the vision and missions of the company.

## **B. Value-Based Management**

VBM pursues to amend the detach between performance goals and value creation. It helps companies to operate with persistently on value. It caters to accurate and distinct measure value on an entire organization level. In financial decision making it is used to achieve ambition maximizing shareholder value or for some stakeholder value. It empowers and aids the process of creating, managing, and value.

### **How it works**

The value of a firm is rectified by the discounted future cash flows. It creates value when capital is invested to reap more than the capital. Value-based management does is concentrating on how to plan on strategic and operational decisions. The approach involves ambition, analytical techniques, and management processes to target management decision making on value creation.

[Timothy Koller, 1994]

Examples of VBM impact in telecom for Etisalat

- **Creating designs for value creation**
  - i. New service 5G gave the potential to increase profits by \$1.2 billion.
  - ii. A slight cost reduction in a landline telephone device can create a reduction in unit price.
  - iii. Salesforce development plans revised on analyzing value would be eliminated.
  - iv. No value-adding projects can be discontinued.

### **Benefits of VBM**

- Increases the value of the corporate persistently
- Appreciates clarity
- Aligns organizations to operate in globalized markets.
- Avoids low estimates of inventory
- Enhances the distribution of resources

### **Evaluate how VBM methods facilitate performance achievements**

This stage includes a critical analysis of the organization's targets and aims. It can be done on a quarterly, bi-annual, or annual basis. It is important as we are living in an ever-changing

dynamic modern environment. It will help the entity to update to the latest in the industry, preserve market share, and have a competitive advantage.

- ❖ Operational efficiency
  - i. Increased pace
  - ii. Cost-effective
  - iii. Outcome and capacity
  - iv. Swift and agile
- ❖ Investment and projects
  - i. Increase monetary yields
  - ii. Better project outcomes
  - iii. Project efficiency
  - iv. Projection cost favorable variance
- ❖ Market performance measures
  - i. increasing market price
  - ii. more innovations
  - iii. developments
  - iv. profit increments

[Chirstopher Smith, 2019]

## RESTRUCTURING

Restructuring is a way for the companies to lead the execution and optimize the business. Usually, companies take advantage of restructuring in the course of a downtrend to avail future economic development benefits. It could support an external asset purchase or an internal operational cost efficiency or improve productivity.

[Nicholette Brown & Martin Skanberg, 2017]

### Types of restructuring and the factors for investing in restructuring

#### ▪ Joint Ventures

It is the combination of two or more parties for a task-specific duration business purpose. The partners stand alone as firms as creating the new venture together anticipating benefit for the joint offering.

e.g. DCM group and Daewoo motors joined to create DCM Daewoo Ltd to produce automobiles in India.

#### ▪ Mergers

It is the legal merger into one entity of two companies with a newly created ownership and management structure. A merger is a more friendly approach and involves no cash transactions but weakens the individual share unit power. It surrenders existing stocks and creates new under the freshly created business organization.

e.g. UAE's two major banks FGB and NBAD merger.

- **Acquisitions**

In this, the smaller company is purchased by the bigger company and stops existing and all its assets become a part of the bigger company. The management structure now will be of the company which consumed the other. It involves huge cash figures to purchase.

e.g. Disney acquired Pixar and Marvel. Google acquiring Android. Etisalat has acquired Help AG, Yahsat & Maroc Telecom as their acquisitions.

- **Divestment**

It is one of the significant tools in restructuring. It constantly analyses purchased assets and divisions under management to urge if the assets are in line with the strategic value creation and the prospects of the company. If it failed to uphold the purpose the divisions or assets will be disposed of.

e.g. Google selling its acquisition of Motorola to Lenovo for \$3 billion, after purchasing for \$12.5 billion.

- **Management Buy-Out**

The company management of directors and employees buys its shares when the shareholders try to sell it out to other parties due to stagnant growth or lack of management skills perceived on the business. It could be the management decide to purchase in full or part buyouts. It could also happen if the owners are incapable of running the business deemed by the management and attempts to save the company which is at risk.

e.g. UNS Holdings management buyout syndicate.

[Abey Francis, 2014]

### **Reasons for the Restructuring**

- ❖ **Growth**

Internal augmentation might not suffice to grow as a business. M&A's enacts adequate and balanced development of the organization.

- ❖ **Scale economies**

The company will have more resources in a merger or acquisition. Therefore, increase the levels of operation and achieve economies of scale.

- ❖ **Revenue & cost synergies**

It is the larger integrated value of individual units. These are the advantages availed from operating economies, increased income as a result and improved management competence, etc.

- ❖ **Buy out the competition**

Elimination of the competition by the M&A's. it will save on having to bear any extra cost to advertise their products with the competition. Which will have a positive effect of having cost saved and reducing the operating costs.

- ❖ **Diversification**

Companies operating in different aspects will be diversified and cost less to do so by cutting off the extra complication a company might have to face trying to enter a new industry.

- ❖ Layout expenses and risks
- ❖ Increasing financial assets
- ❖ The synergy of new technology, innovation, and customers
- ❖ Entry to new products and markets

[Links Financial, 2016]

### **C. Divestment transaction process**

As per the details given Acme engineering's main revenue streams are coming from 75% of the heavy machinery division with a total operating profit of \$150 million. The steel fabricating division only caters to the balance 25% of sales which is \$400 million and had generated an operating loss of 35million in the year 2013. Given the situation, it seems disposal of the division is an option they must consider.

#### **Reasons for recommendation**

- To avoid all the additional costs accumulating further in other expenses and taxes after already the operating loss of \$30 million.
- Senior management's focal attention is on the mainstream heavy machinery division that can totally focus on that to increase the efficiencies and productivities without having to waste more time on smaller 25% which is making losses.
- Selling is off for \$80 million of its worth will open opportunities in supplying capital to invest further in the profit-making primary division's expansions and growth.
- Therefore, creating to optimize shareholders value.

### **Steps by step approach process for divestment**

#### **STEP-1 Strategic Assessment**

##### **❖ Scrutinize commercial functions**

Check if the decision of disposal is in line with the long-term goals of the company and increasing share value etc.

##### **❖ Rectify divestment applicants**

Independently review the market the business portfolio is conducting if expanding or shrinking. Check-in a macro level if there are indications for growth or contraction in the future. Analyze if the competition will further consumer the market value of the business. The trends and signals from these aspects will give a sense of how the division



is compatible with the firm's goals and why it's best to get rid without further incurring costs and losses.

#### ❖ **Endorse decision on divestment**

Lack of performance might not necessarily mean strategic conflict. Drivers such as ill-management, lower investments, or market disturbance could influence the division's performance. Therefore, strong proofs are required to back up a divestment decision along with investigations based on strategic and financial suggestions.

#### ❖ **Construct the transaction**

Once an initial decision is made to divestment, it must be regulated the formation and structure of the deal that is the most likely outcome to be of the potential divestment.

### **STEP-2 Disposal planning**

#### ❖ **Acquire corporate consent**

The consent to proceed will be a documentation present comprising thorough examined strategic rationales such as market, estimates of value, alternative transaction approaches, etc. being the basic recommendation to the board of directors and the CEO. It will also discuss the process, durations for planning with preparing and carrying out of the affair.

#### ❖ **Build an organization plan**

Commonly the divisions under divestment will be a part of the greater parent company's financial asset for a long time. Therefore, creating a correlation and sharing operational foundation. Thus, it is required to straighten out the divestment unit to a stand-alone company to the best possible extend so selling opportunities increased.

#### ❖ **Produce withholding plan**

To make sure the mitigating of the negative impact of the selling, the important employees must be recognized at the early stages and plan to compensate them for staying with the division until the selling is done.

#### ❖ **Gather a team to process divestment**

It is important to form a team to plan, process, and align the divestment. Senior executives, consultants, and advisors and managers guided by the CEO of the parent company ideally will comprise in this team. For example legal, HR, finance, banks, accounting firms, and other specialists.

#### ❖ **Start the disposal plan**

Once the team is in a position to execute the plan under the supervision of the team leader it must carry out considering factors such as key activities in the transaction,

material duties, outcomes, deadlines, milestones, rectify the key decision points, and any threats.

### **STEP-3 Preparation**

#### **❖ Selling preparation**

Occupy outside resources such as banks, financial advisors, regulatory and consultants' advice, and the thorough checking and policies. Govern the selling proceedings etc.

### **STEP-4 Performance of the disposal**

#### **❖ Execution operations**

once the preparation is in position, next is for the team to inaugurate the disposal attempts by declaring purpose to sell, administer the selling, negotiate agreements, and close the deal.

### **STEP-5 Retrospective study**

This step is vital to institutionalize to learn the moral of the experience. Humble financing in time will let the company realize profits and lessons learned from the deal.

[William J. Gole, 2018]

## QUESTION 5

### **A. Businesses & Financial risks in Etisalat**

Evolving in business requires dedication and risks. However, certain risks are far greater than others. Managing a business working hard will earn the winning of clients, revenues, and shareholder pleasure. While success is the supreme objective, the business risk may come in the way of achieving it. Hence comes the risk management, to manage these situations.

Etisalat Group is in the frontline in rectifying and the bold management of threats is vital to reach their ultimate goals. Understanding that risk is part and parcel of doing business the ERM enterprise risk management system is set as a control to consistently monitor, rectify, evaluate, and manage any potential internal principal risks and unpredictable.

They regularly evaluate the risks that can make a substantial impact on the business through various methods and proactively make decisions to manage them. Below are examples of how Etisalat assesses and manages risks in various business and financial areas.

#### **❖ Economic Risk**

##### **Macroeconomic conditions**

Dynamic regional and global commercial circumstances in a number of the markets in which Etisalat functions unceasingly represent challenges to the Group.

Management decisions:

- Annual financial budgeting & planning processes examine these shifting economic drivers.
- Researches are in progress and the study of market states is frequently appraised within essential markets.

##### **Geopolitical Threats**

Current political and geographical unpredictability present continuous challenges over several countries in which Etisalat operates.

Management decisions:

- They work firmly with the related operating companies' management to support local knowledge to fight back these challenges.
- As a side effect, the security of the local staff is dedicatedly managed by the operating company provisions.

### **OTT Operators**

Over-the-top operators are a popular threat for the telecommunication in grabbing the mobile voice incomes even with Etisalat's established markets. The growth in VoIP applications consuming the old telecom operators' profits.

Management decisions:

- Have different approaches in reply to these threats.
- The device is in the respective commercial teams across the influenced operating companies.

## **❖ Operational Risk**

### **Cyber Security**

The danger of outside cyber-attacks across the Etisalat network and IT system is incurable.

Management decisions:

- Network and IT security teams dedicatedly investigating activities across the Group's networks to find out and reduce potential cybersecurity threats and data privacy violations.

### **Competition & Pricing Pressures**

The markets in which Etisalat functions are identified by soaring levels of entrants existing and new, pricing pressure, technology replacements, market, and product cross intersecting and customers are confused about what to go ahead with.

Management decisions:

- Etisalat intently studies and detect trends within the markets and fund its networks, products, and service to compete successfully.
- The development of cyber products & services is an additional way of managing manifold rivalry risks.

## ❖ Compliance Risk

### Litigation

Etisalat is just like any other company exposed to the risk of legal actions by competitors, clients, governments, and other stakeholders. It will impact the financial profitability and prestige of the Group's operating companies.

Management decisions:

- Legal guidance within every operating company supervises & effectively conducts such legal cases.
- Their internal legal team also shares progressive assistance to the operating companies where needed.

## ❖ Financial Risk

### Foreign Exchange exposure

Like any other organization which has an international business is exposed to fluctuations in the foreign currency rate in some of the countries in which they operate. It will particularly the uncertainty will impact the consolidated results and the overall worth of investment in foreign operations.

Management decisions:

- Launched strategies, systems, and techniques to detect, manage, and state any such exposures.

### ❖ Other Financial exposure

The interest rates, liquidity, and credit risks are other financial risks exposed by Etisalat's assets and liabilities.

Management decisions:

- Studies the market for the interest rate in contrast to the present lending rates and analyze it or not to act in the current rates i.e. to borrow further or not.

[Etisalat, 2018]

## **QUESTION - 5**

### **Internal Risk Environment**

Internal dangers are encountered by an organization within the firm and come to light at times of general operations of the organization. These risks can be foreseen up to a certain extent, hence an organization has the potentials to mitigate the internal risks.

- **Human factor risk**

An Individual's problems might present operational threats. Such as union strikes, cheating employees, inefficient leadership, negligence on the external manufacturers and vendors, and wrongdoing of outright unsuccessful in payments by the customers, etc.

- **Technological risk**

These risks involve unexpected swifts in the production, distribution of a company's service. Such as obsolete computer operating systems can slower the functions of production, stocks, etc. Its server's system downs can lower the production resulting in idle times and revenue loss.

- **Physical Risk**

Tangible assets loss or impairment risks include a company's physical risk. To avoid such losses the company can avail credit insurance to save against customer's debt defaults etc.

### **Case Study 1: Washington Mutual**

Washington Mutual (WaMu) in 1917 with its head office in Seattle was a savings and loan bank with profitable investments. It had firm and secure savings in the state. Technology embracing innovations in the finance institution helped them further flourish. In 1983 WaMu became a public listed company and further grew to double the assets within 6 years and acquired 16 smaller financial institutions. Around 2008 almost 60% of its operating profits were from retail banking and 20% were from the credit cards and 14% from home loans.

### **What led to the failure of the bank?**



- 1) To enhance the slow growth one of the financial institutions called Long Beach providing mortgages to poor credit rating customer history clients.
- 2) Due to the slow-moving of home loan business, another acquisition was on Provident, a credit card lender to lower credit rating customers and in low sales, they lend money to subprime customers who don't pass the criteria to get any debt.
- 3) The hasty decision in spreading its branches without any proper strategy led to several poor venues in several markets resulting in lending mortgages to unqualified customers.
- 4) In 2007 the resale market for mortgage securities crumbled making it harder on WaMu to sell them and \$67 billion mortgages defaulted were made in 2006.
- 5) Towards the end of 2008, when Lehman Brothers bankrupted it had a negative effect on WaMu and its savers withdrew around \$16.7 billion from the bank. Soon enough they went bankrupt with assets over \$307bn and assets of \$188bn.

Below is the summary of the errors in the management:

- Absence of pricing risk to check the decline of the value of the securities of the mortgage lending resulting in credit risk
- The allocation for the losses was insufficiently estimated.
- Credit cards were given to subprime customers under the pressure of increasing sales again resulting in higher defaults.
- Falling in to excessively disbursing on fewer quality securities when lending is easy and interest rates are low & over-dependent on mortgages.
- Low rating customers were given credit hence high defaults.
- No collateral guarantees were taken.
- Background checks of the customers were not done.
- It has a high internal human risk through the customers not making payments.

All in all, the risks are taken by the institution were unavoidable as the management made internal decisions to go ahead with high-risk lending to clients and resulted in the downfall.

## Recommendations

- Do background checks of the customers before lending any debts.
- credit rating scores of the customers should be checked before giving credit cards.
- Collaterals should be put in place before giving debts.
- Loans to be given to customers whosoever can give guarantors who are qualified to be secured over the transaction.
- Before opening new several new branches, strategies, and open branches targeting the expected customers who have higher profiles to meet the eligibility to avail loans.

- They should not have overly depended on housing mortgages when the recession hit in 2008 the demand for the real estate went down it hit the bank adversely.
- They should have done rating checks of the stocks such as S&P 500 ratings on the stocks taken as securities to avoid overly valued stocks which in reality were valued far less which didn't even have a resale market.

## **Case Study 2: Barings Bank**

Barings Bank was established in 1762 by Baring brothers. It had a net worth of \$900 million before the great loss of \$1 billion. They through the subsidiary of Barings Securities Ltd (BSL), differentiated trading in Far Eastern securities. In 1989 Nicholas Leeson (NL) was appointed to futures and options settlement in the London branch.

Leeson had made profits from the futures trading \$2mil to \$20mil before he was transferred to Singapore which gave the bank overconfidence on him. In 1992 he was moved to Barings Future Singapore (BFS) in Singapore as the General Manager and Head trader of futures dealing on the Singapore Monetary Exchange (SIMEX). It brokered the customers who desired to trade on SIMEX.

Due to the misconducts of Leeson in 1995 Barings Bank was bankrupt with a loss of GBP 900 million.

### **What led to the failure of the bank?**

#### **Internal control Procedures**

NL was having dual leadership by being the GM trading as well as head of settlement operations in SIMEX ideally which must go to a different head for the accounting. Which is a clear lacking from its internal control of the bank?

#### **Manipulation**

The lack of supervision, NL was able to gamble on the futures arbitrage market and hide the losses and changed accounts and stop the London office from receiving daily reports on trading.

#### **Overconfidence and lack of knowledge**

Leeson's success over the profits made in the UK blinded the bank to blind trust him to make a profit in the far east. It could be since he was new to the market in Singapore and the Japanese markets his strategies did not work too well with the arbitrage. Plus, the management surely didn't seem to have much knowledge trading and financial markets themselves.

#### **False declarations**

Leeson faked receivables of GBP 50 million to cover up losses in the subsidiary in the auditors and regulatory authorities and piled up losses.

### **Operational risk**

NL was the head of dealing and back-office operations in BFS which lack the segregation of duty. He was not authorized to trade in options even though he did it anyway.

### **Autonomy Risk**

He did not hedge the derivatives instead gambled on them and future contracts which led to disaster. Giving a single individual hefty sovereignty.

### **Recommendations**

- ❖ Management should have taken more effort to fully comprehend the type of business they are involved in.
- ❖ They should have segregated responsibilities for separate departments
- ❖ The job description for each business activity involved must have liaised with the employees.
- ❖ Important internal controls and unbiased risk management should have been in place for all business transactions.
- ❖ Senior management and Audit Committee should have rectified the loopholes and given solutions instantly rather than had the misconducts happen over 3 years.

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Question 1

INTRODUCTION

Etisalat Telecommunications Group Co PJSC was the world's 14<sup>th</sup> ranked mobile operator in the year 2014 and 140<sup>th</sup> in the world as per Financial Times Global 500 ranking in terms of market capitalization is one of the biggest and leading telecommunication services. As of today, Etisalat service subscriptions exceed 167 million. It was also the only mobile operator until 2006, in the United Arab Emirates. After which Du operator who entered the market and now owns 37% of local market share.

The head-office of Etisalat is based in the emirates of Abu Dhabi. It was inaugurated in 1976 by the British company International Aeradio Ltd and the local partners. Later in the year, 1983 ownership changed when the UAE Government acquired 60% and the remaining shares were sold at public auction.

The historic development of this telecommunication goes back to 1991 when the UAE government permitted the wired and wireless telecommunications services is when the Etisalat became the monopolist in the industry for UAE. Later in 1994 they introduced GSM and was the first internet service provider. In 2007, CDPRS was introduced and two years down the

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