

November 2009 examination series - Sample script response with commentary
P1 The Internal Audit Environment – Question 3

- a. **Define** any four elements of the PESTEL framework and **analyse** how each may influence the strategic planning of a chain of high street health food shops. **12 marks**
- b. **Assess** the impact of these strategic influences on the organisation's internal audit function. **8 marks**
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The question is drawn from the elective part of the paper, Part B, from which candidates must answer three of the four questions posed. This question is concerned with external influences on strategic planning in organisations.

Part (a) required candidates to define any four elements of the PESTEL framework and then analyse how each may influence the strategic planning of a chain of high street health food shops. Twelve marks were allocated to this part, allocated as 3 marks for each of the four elements.

Part (b) required candidates to assess the impact of these strategic influences on the organisation's internal audit function. Eight marks were awarded for this part of the question.

The script is an example of a successful answer, which gained 14.5 out of a possible 20 marks. The answer was well structured, with good use of headings throughout and addressed all the specific elements of the question.

- a. The PESTLE framework is a management tool that is extremely useful for understanding, visualising, gathering information on the external influences that may affect an organisation. The total framework is as follows:

P	Political	Political direction or pressures
E	Economic	Economic pressures, interest rates, recession
S	Sociological	Linkage to society as a whole
T	Technological	Technology advances
L	Legal	Legal/statutory regulations
E	Environmental	Green issues, CSR and ethical

Linked specifically to a high food shop in the high street I will cover 4 of these and analyse how the outputs of this tool may influence the strategic planning.

ECONOMIC INFLUENCES

With the current recession in place the public have less real cash to spend on non-essential bills and household costs. The health food industry, although a multimillion pound business is aware that the luxuries of health food and supplements could be effected as the public have less to spend on these products. This could slow their profits and turnover – understanding this factor of a potential slow in sales at the strategic financial level will enable the Board/Senior Management Team to take steps to reserve their cash, perhaps not spend on shop developments or longer term initiatives, also it would influence them to consider the costs of stock, raw materials, production and make them look to efficiencies to

offset the potential downturn in sales.

SOCIOLOGICAL INFLUENCES

With society as a whole far more interested in alternative health products and better healthier living (despite the bite of recession) they are keen to adopt a healthier lifestyle. In particular there are trends that sweep across society in respect of health initiatives eg anti-cancer foods, anti-aging foods, etc. If the organisation is to line to this they can match their product lines to match the public needs and wants for these products. They can be proactive and responsive to societies needs.

TECHNOLOGY ADVANCES

If the Board are aware of the technological advances and changes they can be alive to additional needs, changes or costs of developments that may come their way. They can strategically plan for them and cost, plan for them in advance.

For example the advances in Banking and Cash handling in the high street have meant that the inception of 'chip and pin' technology must be kept up with to stay a competitor. The advances in credit card technology where you wave your card at a reader and also the demise of the personal cheque all have an effect on the technology of the cash/money handling. They must plan for this. Technology can also be found in the production of health foods, better more efficient ways of harvesting raw materials and processing plants at source is an area the company should be alive to, especially if they are directly involved in the production stage of health foods. Their competitors will so to keep a competitive edge they need to stay at the forefront of this work.

ENVIRONMENTAL ISSUES

A major factor in all responsible companies and organisations – especially one like a health food shop. The public and society will look to these type of organisations to lead the way on green and environmental issues, from waste recycling to packaging to environmentally friendly uniforms for staff. The shareholders will be looking at the bottom line of profit, so if the organisation can keep tuned to environmental pressures and react positively they will be better placed to keep their customers happy – therefore better or retained or increased profits. Environmentally the organisation could look wider at corporate social responsibility to add an extra competitive edge over their rivals.

Overall – the PESTLE tool can provide the organisation with external pressures, and can be done in a bespoke way to refine the views therefore inform key decision makers in the Board or Senior Management. It must be taken in context with the business and not treated in isolation.

It can be useful to combine with a SWOT analysis looking at strengths, weaknesses, opportunities and threats where opportunities and threats are externally biased.

10 marks awarded out of a possible 12

A good answer to part (a) which demonstrated a sound understanding and application of the PESTLE model as required by the question. The economic influences could have included interest rates, taxation, inflation and the availability of commercial loans. The social influences could have included demographic aspects and the technological aspects could have included internet shopping.

b. Strategic influences will have a massive effect on the organisation's internal audit function. The IA function is there to provide assurance and consistency to management on the efficacy and efficiency of governance, controls and risks across the organisation. It does this by way of independent and objective tasks – audits, consultancy or advisory roles.

Changes and impacts at the strategic level can require the following:

Changes to the IA Programme – If the organisation changes direction or role to cope with strategic influences it will require the IA programme to reflect the new direction.

Changes to the IA focus – If changes to the organisation are quite radical it may require the internal auditors to work on new subjects or specialisms. This may require additional specialist training or exposure. Or it may include bringing in external auditors with specialist knowledge.

Management changes. Should direction or role be changed it may require the IA team to undertake some specific consultancy work on systems design to assist with the change programme.

Assurance services. There will be work to be done to assume that proposed strategic changes are fit for purpose and robust in nature. The IA team can really add value here in completing 'gap analysis' type activities – securing the 'As-is' situation and looking at the 'should-be' in relation to Board Strategies – then proposing methods and techniques to assist with the strategic goal achievements.

Risk Management. There may be increased work on risk and controls across the organisation as it changes posture or perspective, thus possible introduction of additional or different risks. The IA role is vital in assessing and advising in this crucial area of the business.

Facilitation. Maybe a greater requirement for the IA team to facilitate sessions across the business to understand external and internal influences now being placed upon them.

The use of SWOT, PESTLE and PORTERS 5 FORCES would be useful tools to understand these areas. – Again to inform managers and decisions makers.

4.5 marks awarded out of a possible 8

A reasonable answer to part (b), well structured with good use of headings. The candidate could have adopted an alternative structure using the headings from part (a). This would have ensured that the scope of the answer fully addressed the question and could have resulted in higher marks.
