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# Business management

## Standard level

### Paper 2

24 October 2023

Zone A afternoon | Zone B afternoon | Zone C afternoon

1 hour 45 minutes

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#### Instructions to candidates

- Do not open this examination paper until instructed to do so.
- A clean copy of the **business management formulae sheet** is required for this examination paper.
- Section A: answer one question.
- Section B: answer one question.
- Section C: answer one question.
- A calculator is required for this examination paper.
- The maximum mark for this examination paper is **[50 marks]**.

### Section A

Answer **one** question from this section.

**1. Dryed Ltd. (DD)**

*Dryed Ltd. (DD)* manufactures electric kettles. In the final quarter of 2021, *DD* invested in new production facilities in its factory to produce a new and improved kettle. This kettle, using 25% less electricity than competitor products, went on sale in January 2022.

Because competitors would take 12 months to launch a similar product, *DD* adopted a price-skimming strategy for the new kettle. However, sales of the new kettle in 2022 were 15% lower than *DD* had forecast.



**Table 1: Selected financial information for *DD* for the years ending 31 December 2021 and 31 December 2022 (all figures in \$000s)**

	2021	2022
Cash	30	25
Cost of goods sold	2100	2300
Dividends	28	30
Expenses	1200	1300
Fixed assets	1075	1275
Gross profit	<b>X</b>	2350
Interest	10	10
Net profit before interest and tax	<b>Y</b>	<b>Z</b>
Sales revenue	4300	4650
Stock	300	350
Tax	121.1	140

**Table 2: Selected financial ratios for *DD* at 31 December 2021 and 31 December 2022**

	2021	2022
Acid test (quick) ratio	1	0.9
Current ratio	1.5	1.6

- (a) Define the term *price skimming*. [2]
- (b) In **Table 1**, calculate the values of **X**, **Y** and **Z** (*no working required*) [3]
- (c) Using relevant information from **Table 1**, construct a fully labelled profit and loss account for *DD*, for the year ending 31 December 2022. [3]
- (d) Referring to the information in **Table 1** and **Table 2**, explain the change in *DD*'s liquidity between 2021 and 2022. [2]

**2. MotorZycle (MZ)**

*MotorZycle (MZ)*, a manufacturer of motorcycle transmissions, is seeking to establish a strategic alliance with a spare parts dealer.



**Table 3: Forecast fixed costs for MZ for 2024**

Rent	\$60 000
Marketing	\$80 000
Administrative expenses	\$20 000

**Table 4: Forecast variable costs per motorcycle transmission for 2024**

Components	\$800
Direct labour	\$200

*MZ* sells motorcycle transmissions for \$3000 per unit.

*MZ* has forecasted sales of 160 motorcycle transmissions in 2024.

- (a) Define the term *strategic alliance*. [2]
- (b) Calculate, for *MZ*, the break-even quantity/point for 2024 (*show all your working*). [2]
- (c) Construct a fully labelled break-even chart, to scale, for *MZ*, for 2024. [4]
- (d) Explain the impact on *MZ*'s margin of safety if motorcycle transmissions are sold for \$2000 per unit and all costs remain the same. [2]

## Section B

Answer **one** question from this section.

### 3. Anna’s pet salon

In 2024, Anna Holborn plans to start a new business: a pet grooming salon. Although Anna has no managerial experience, she is eager to work for herself. In Anna’s city, three pet salons already exist. The market is very competitive.



**Table 5: Selected data on the three existing pet salons**

Salon	Prices	Reputation out of four stars (★)	Independent or franchise
<b>A</b>	Medium	★★★	Franchise
<b>B</b>	Low	★	Independent
<b>C</b>	High	★★	Franchise

Anna is considering two options for opening her salon:

- **Option 1:** Open it as an independent business, called *AH Salon*.
- **Option 2:** Open it as a franchise of *Paws Boutique (PB)*, a nationwide chain of pet grooming salon franchises that currently has no franchise in Anna’s city.

**Table 6: Anna’s forecasted initial costs of starting a pet salon as an independent business (Option 1) or as a PB franchise (Option 2)**

	Option 1: As an independent business	Option 2: As a PB franchise
Equipment	\$15 000	\$12 000
Grooming supplies	\$10 000	\$10 000
Initial local promotion	\$5 000	\$2 000
Legal fees	\$2 000	\$4 000
Purchase of franchise	Not applicable	\$10 000
Total	\$32 000	\$38 000

If Anna buys a *PB* franchise, she must pay 5% of revenue to the franchiser. The franchiser will pay for regional and national – but not local – promotion. Anna must purchase equipment from the franchiser. In other cities, *PB* franchises are rated medium in terms of price and ★★ in terms of reputation.

Anna has limited financial resources. She has prepared a forecast for the first year. She forecasts, as a *PB* franchise, an average of 200 pet grooming services per month at a price of \$30. As an independent business, she forecasts that sales would be 10% lower. For both options, fixed costs, including her salary, would be \$2800 per month. Variable costs would be \$5 per pet grooming.

**(This question continues on the following page)**

**(Question 3 continued)**

- (a) Define the term *variable costs*. [2]
- (b) Using **Table 5**, construct a product position map/perception map of the three existing pet salons. [4]
- (c) Explain **two** problems that Anna may encounter when starting a new business. [4]
- (d) Recommend whether Anna should open her pet salon as an independent business (**Option 1**) or as a *PB* franchise (**Option 2**). [10]

#### 4. WindJam (WJ)

In 1998, major camping equipment manufacturers considered eco-friendly products a niche market. Cameron Harris saw an opportunity, however, and founded *WindJam (WJ)*, a private limited company that manufactures eco-friendly camping equipment. Cameron owned 100% of *WJ*'s shares. *WJ*'s vision statement is, "Promoting environmental experiences while protecting the environment."

*WJ*'s eco-friendly camping equipment is expensive. Since 1998, the popularity of eco-friendly products increased, and *WJ*'s sales have grown every year.

In 2014, *WJ* sold new shares to family members. With a long working capital cycle and increasing sales, *WJ* needed more working capital. This need was heightened when one supplier reduced its credit terms from 60 days to 30. The funds from the sale of the new shares increased *WJ*'s working capital. Cameron now owned 70% of *WJ*.

Initially, *WJ* faced limited competition, but the market began to change. Many large manufacturers are now developing eco-friendly camping equipment. Some large manufacturers use a loss leader pricing strategy, whereas other large manufacturers use a penetration pricing strategy. One competitor has also offered tents at prices that, Cameron suspected, were lower than production costs.

In 2023, *WJ* must compete more effectively. Cameron has two options:

- **Option 1:** Convert *WJ* to a public limited company, which could raise \$10 000 000. With additional finance in the form of a bank loan, this amount would be enough to build a modern, sustainable factory and fund additional working capital. Cameron's ownership of the company would fall to 30%.
- **Option 2:** Outsource all manufacturing to developing countries, where costs are lower. The sale of *WJ*'s existing factory could be used for additional working capital.

- (a) Define the term *niche market*. [2]
- (b) Explain why *WJ* regularly needs more working capital. [4]
- (c) With reference to *WJ*'s new competitors, explain the terms "penetration pricing" and "loss leader". [4]
- (d) Recommend whether Cameron should choose **Option 1** or **Option 2**. [10]

**5. Mattie Eats (ME)**

*Mattie Eats (ME)* is a small fast-food chain selling a range of products. Between 2017 and 2021, *ME* expanded into small local towns.

**Table 7: Information on *ME*'s core products in the local fast-food market**

Year of launch	Core product	Other information about the product and the markets
2017	Traditional beef burgers	Was very profitable. Currently has a low market share in a declining market. It is a loss-making product. Social marketing by the government reduced demand.
2018	Roasted organic potatoes	Currently very profitable, with a high market share. Market growth is low.
2019	Low-fat, 100% organic beef burgers	Was a very successful product. Has a high market share, but the market is maturing/saturating rapidly. The product breaks even.
2020	Vegan* burgers	A commercially successful product. Has a high market share in a mature/saturated market. Profit is levelling off.
2021	Vegan pancakes	Has a very low market share in a highly mature/saturated market. It has not been a commercial success.

Overall *ME* has been profitable, but its profits started to fall in 2020. The chief executive officer (CEO) is concerned about the future.

The competition in the vegan fast-food industry is intense. Consumers see the products as undifferentiated and demand value for money. Last year, *ME* increased its above-the-line promotion to attract more customers.

In 2024, *ME* will launch a 100% vegan drink aimed at health-conscious consumers. A loss leader pricing strategy will be used.

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\* vegan: food and other products that do not contain animal products, including meat, dairy, and eggs

- (a) Define the term *social marketing*. [2]
- (b) Using the Ansoff matrix, explain **two** of *ME*'s growth strategies. [4]
- (c) Explain **one** advantage **and one** disadvantage for *ME* of using a loss leader pricing strategy for the new product that will be launched in 2024. [4]
- (d) Using the Boston Consulting Group (BCG) matrix, evaluate *ME*'s core product range. [10]

## Section C

Answer **one** question from this section. The organizations featured in sections A and B and in the paper 1 case study may not be used as a basis to your answer.

6. With reference to an organization of your choice, examine the impact of **globalization** on operations management **strategy**. [20]
7. With reference to an organization of your choice, examine the impact of **culture** on **ethics**. [20]
8. With reference to an organization of your choice, examine the impact of **innovation** on **change** in human resource management. [20]

*Companies, products, or individuals named in the stimuli are fictitious and any similarities with actual entities are purely coincidental.*

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### References:

1. gerenme, n.d. *Kettle - stock photo*. [image online] Available at: <https://www.gettyimages.co.uk/detail/photo/kettle-royalty-free-image/891596906?phrase=kettle&adppopup=true> [Accessed 14 March 2023]. Source adapted.
2. loraks, n.d. *Gear set. - stock photo*. [image online] Available at: <https://www.gettyimages.co.uk/detail/photo/gear-set-royalty-free-image/478199195?phrase=motorcycle+transmission&adppopup=true> [Accessed 17 May 2023]. Source adapted.
3. BONDART, n.d. *Professional male groomer making haircut of poodle teacup dog at grooming salon with professional equipment - stock photo*. [image online] Available at: <https://www.gettyimages.co.uk/detail/photo/professional-male-groomer-making-haircut-of-poodle-royalty-free-image/1407302298?adppopup=true> [Accessed 9 March 2023]. Source adapted.