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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. Fannon Drones Ltd. (FD)

*Fannon Drones Ltd. (FD)* is a private limited company operating in the secondary sector. *FD* manufactures and sells drones. Gary Fannon, the chief executive officer (CEO), owns 100% of the shares. In 2022, *FD* sold an average of 22 drones a month at a price of \$400 each.

**Table 1: Selected financial information for *FD* for the year ending or at 31 December 2022 (all figures in \$000s)**

180-day loan	16
90-day loan	10
Accumulated retained profit	22
Cash	17
Cost of goods sold	33
Creditors	32
Debtors	39
Expenses	56
Long-term debt	54
Net fixed assets	25
Net profit after interest and tax	2
Overdraft	6
Share capital	10
Stock	40

A competitor, *Wexel Flies (WF)*, offered Gary \$35 000 to purchase 60% of his shares on the condition that he remain as CEO for three years at his current salary.

- (a) Define the term *secondary sector*. [2]
- (b) Using the information in **Table 1**, calculate *FD*'s:
- (i) current ratio at 31 December 2022 (*show all your working*); [2]
  - (ii) acid test (quick) ratio at 31 December 2022 (*no working required*); [1]
  - (iii) total equity at 31 December 2022 (*no working required*); [1]
  - (iv) net profit margin for the year ending 31 December 2022 (*show all your working*). [2]
- (c) Comment on *WF*'s offer to purchase shares of *FD* from Gary. [2]

## 2. Alejandro's Aerial Photography (AAP)

Alejandro Tovar owns *Alejandro's Aerial Photography (AAP)* as a sole trader. He currently rents a helicopter on a monthly basis but would like to purchase a professional industrial drone to take his aerial photographs. The bank requested a cash-flow forecast and approved a \$15 000 loan for Alejandro to purchase the drone. Alejandro will be able to purchase the drone in December 2023, and he will take delivery of the drone at the end of February 2024. At the start of March 2024, Alejandro will start to take aerial photographs using the drone.

**Table 2: Alejandro's forecasted figures for AAP for the four months from January 2024 to April 2024**

Sales per month	\$2000, all in cash
Monthly helicopter rent	\$1000
Monthly loan payment	\$300 to be paid starting in January 2024
Opening balance in January 2024	\$0
Drone maintenance	10 % of sales
Alejandro's monthly salary	\$550 for the first two months; \$1000 starting in March 2024

- (a) State **two** features of a sole trader. [2]
- (b) Using the information in **Table 2**, prepare a fully labelled cash-flow forecast for AAP for the four months from January 2024 to April 2024. [6]
- (c) Explain **one** suitable external source of finance, **other than** loan capital, that Alejandro could use to purchase the drone. [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 3: Selected data on the three existing pet salons**

Salon	Prices	Reputation out of four stars (★)	Independent or franchise
A	Medium	★★★	Franchise
B	Low	★	Independent
C	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 4: 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 3**, 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 5: 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, discuss the impact of **ethics** and **globalization** on human resource management. [20]
  
7. With reference to an organization of your choice, discuss the impact of **culture** and **innovation** on operations management. [20]
  
8. With reference to an organization of your choice, discuss the impact of **change** on marketing **strategy**. [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:

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.