



22125012



**BUSINESS AND MANAGEMENT
HIGHER LEVEL
PAPER 2**

Monday 21 May 2012 (morning)

2 hours 15 minutes

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.
- Section A: answer one question.
- Section B: answer two questions.
- A calculator is required for this examination paper.
- Clean copies of the ***Business and Management formulae sheet and discount tables*** are required for this examination paper.
- The maximum mark for this examination paper is [75 marks].

SECTION A

Answer **one** question from this section.

1. Safe Passage (SP)

Trent Peters is one of seven partners at *Safe Passage (SP)*. It provides bodyguard* services to film stars, politicians and other important people in Europe and the Americas. Trent would like to satisfy a growing demand from Asia but has to choose from two options for the recruitment and training of bodyguards. These are:

- offshoring by setting up it’s own overseas branch in Asian country X or Y or Z
- subcontracting by using an external agency in Asian country X or Y or Z.

The forecast costs and revenues of offshoring are given below (all figures in US\$ millions):

Option	Forecast costs	Forecast revenue if successful Probability: 0.3	Forecast revenue if not successful Probability: 0.7
1. Offshore to country X: has a history of earthquakes, good infrastructure	4	19	2
2. Offshore to country Y: has no history of earthquakes, poor infrastructure	5	16	4
3. Offshore to country Z: under reconstruction after a recent earthquake	6.4	21	4.2

The forecast costs of subcontracting to the same Asian countries are given below:

Country X: US\$1.5 million.

Country Y: US\$2.8 million.

Country Z: US\$4.2 million.

* bodyguard: a person who is responsible for protecting a person from harm

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(Question 1 continued)

The three suitable Asian countries are located in earthquake zones. An earthquake expert assured Trent that all three areas are safe. Trent is concerned and decides to prepare a contingency plan for each possible location in Asia.

Control over recruitment and training of bodyguards is vital to *SP*. Customer service and trust are their unique selling propositions (USP). Clients will pay high fees to ensure their safe transport to concerts, meetings and important events. However, Trent is refusing valuable contracts in Asia due to a lack of suitably trained bodyguards. As a result *SP* is missing out on large profits.

Trent has mentioned to a previous customer of his plans to subcontract the recruitment and training of bodyguards. She has threatened not to use *SP* again and would tell her friends if the plans went ahead. Trent is concerned as word-of-mouth promotion is crucial to *SP*.

He calls a meeting of all the partners. Three partners prefer subcontracting the recruitment and training as it is cheaper, quicker and less risky. The three other partners prefer offshoring. They believe that subcontracting will damage *SP*'s USP. They argue that the higher costs of offshoring will be covered by the forecast high revenue.

- (a) Describe **two** features of a partnership. *[4 marks]*

- (b) Explain **two** benefits and **one** cost to *SP* of preparing a contingency plan of the three possible locations in Asia. *[6 marks]*

- (c) (i) Construct a fully labelled decision tree and calculate the predicted outcome of each offshoring option (*show all your working*). *[6 marks]*

(ii) Comment on the value for *SP* of using a decision tree as a decision-making tool. *[3 marks]*

- (d) Examine **two** disadvantages for *SP* of subcontracting its recruitment and training of bodyguards. *[6 marks]*

2. GF

Barbara Johnson manages a small business (*GF*) that produces and sells gluten-free* bread. *GF* has been recognized for meeting national quality standards for gluten-free bread which has helped increase sales. Local supermarkets sell their own label brands of gluten-free bread which do not meet national quality standards at a price 20% cheaper than *GF*. Barbara aims to make national quality standard gluten-free bread more affordable and in larger batches.

GF has 21 employees. Four are gluten-sensitive (intolerant) testers who check the quality of the final bread. This traditional method of quality control is important, but takes significant time and resources.

Several hospitals have asked if *GF* can provide them with an additional 1200 loaves of gluten-free bread every day for the next year. Barbara is keen, however in a small market like this, becoming larger does not automatically result in economies of scale. *GF*'s suppliers cannot provide larger quantities of gluten-free flour without increasing their prices and consequently *GF*'s costs.

Barbara has two options:

- Option 1: Increase *GF*'s production of gluten-free bread and maintain national quality standards by introducing total quality management (TQM) control at a one-off cost of \$4000. This should also speed up the batch production process.
- Option 2: Buy-in the additional 1200 loaves from the company that supplies the local supermarkets and then sell this bread to the hospitals. However this supplier uses flow production and does not meet national quality standards.

The sales price per loaf of *GF* bread is \$6.80 regardless of the option chosen.

Barbara prepared the following figures for each option (in \$):

Option 1: Increase *GF*'s production to make the additional 1200 loaves.

Fixed costs: one-off cost from introducing TQM	4000
Semi-variable costs: additional electricity costs	2000 + an additional 0.20 per loaf baked
Variable costs: additional gluten-free flour overtime pay for staff	0.80 per loaf 0.40 per loaf

Option 2: Buy-in the additional 1200 loaves.

Total variable cost of buying in 1200 loaves from local supermarkets' supplier	7200
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* gluten: a protein found in wheat (flour) which causes health problems for those who are sensitive (intolerant) to it

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(Question 2 continued)

- (a) Identify **two** features of an own label brand. *[2 marks]*

- (b) Define the term *economies of scale*. *[2 marks]*

- (c) Explain **two** benefits and **one** cost to *GF* of meeting national quality standards for its bread. *[6 marks]*

- (d) (i) Calculate the variable cost per loaf to *GF* if they buy-in the additional 1200 loaves from the local supermarkets' supplier. *[1 mark]*

- (ii) Using relevant information given, calculate whether *GF* should either buy-in the additional 1200 loaves from the local supermarkets' supplier, or make the loaves themselves (*show all your working and state any assumptions you make*). *[5 marks]*

- (iii) Comment on whether *GF* should make or buy-in the additional 1200 loaves. *[3 marks]*

- (e) Analyse **two** reasons why *GF* should move from traditional quality control methods to a TQM approach. *[6 marks]*

SECTION B

Answer **two** questions from this section.

3. The \$1.99 toy shop

James Lai's toy shop is popular with no toy priced above \$1.99. The toy shop uses psychological pricing at a level much lower than its competitors. James imports 90% of his stock from China. It is located in a poor part of the city centre. Its target market is low-income families. The shop is very busy at weekends with a long queue (line) at the one cash register. Most employees are teenagers, who are very low paid.

Several stakeholder groups have complained:

- parents are concerned about the quality and safety of the toys and have set up an online social networking web site urging people to stop purchasing from the shop
- older customers have complained about the long queue at the one cash register
- one employee representative (union official) contacted James about employing teenagers on very low wages
- local toy manufacturers have questioned James' use of Chinese suppliers.

Competitors have argued that the \$1.99 toy shop's psychological pricing method is unethical. James replied to stakeholder concerns, in a letter to a local newspaper, by stating that his shop allows young children to purchase affordable toys and provides job opportunities for teenagers. James has decided to create a social networking web site to respond to critics and to manage customers' perceptions.

James admits that the rate of stock turnover could be improved. He admits that the long queue is causing many customers to leave without buying anything. James is considering opening a second, larger toy shop called \$4.99. He announced the opening on his social networking web site, informing stakeholders that he would stock higher quality products and have more cash registers. However, he immediately received negative online feedback from customers who saw the \$4.99 toy shop as just a \$3 price increase for the same toys.

(a) Define the following terms:

(i) *target market* [2 marks]

(ii) *stock turnover.* [2 marks]

(b) Explain **two** disadvantages of James using psychological pricing. [6 marks]

(c) Analyse **two** possible conflicts between stakeholders of the \$1.99 toy shop. [6 marks]

(d) Discuss whether the introduction of the \$4.99 toy shop as a new strategy will change customer perceptions of James' two shops. [9 marks]

4. Motuoro High School (MHS)

Motuoro High School (MHS) is a new residential (boarding) school for 16–18 year olds. It is a public-private partnership funded 60% by the state and 40% by the private sector.

The school has two managers:

- Charles Ledger, a government official, who is responsible for finance.
- Julian Santiago, a successful businessman, who manages the daily operations.

Julian was asked to help set up *MHS* as a new innovative and flexible school. He interviews all new students. They can choose to attend classes or telework from their rooms. *MHS* has an up-to-date Internet system to provide communication and educational resources. It has a flat organizational structure. Teachers and students are at the same level of hierarchy, but below Charles and Julian.

The teachers were selected by Julian and did not sign contracts. Julian and the students meet to decide together on the appraisal process for teachers. The teachers themselves are not present at these meetings.

MHS provides teachers with free accommodation, food and a generous salary. 12 months ago a television series about the opening of the school gave it enormous publicity. This led to many applications from potential students and teachers.

However, a number of problems have now emerged. New student applications are decreasing. Government funding has been reduced. A number of students are missing classes or not submitting work. Teachers are insisting that *MHS* provide contracts. They are also concerned that the informal organization within the school is having too much influence on Julian's decision making. One frustrated teacher complained to Charles without Julian knowing. This caused an issue between Charles and Julian. Julian wanted to dismiss the teacher, but Charles was concerned that dismissing the teacher would have led to strike action. This would have created unwelcome publicity at a time when student numbers were falling. Julian suggested that a no-strike agreement should be put in place and that teachers should consider working at *MHS* as a privilege. The meeting finished without a resolution.

- (a) Define the following terms:
- (i) *appraisal* [2 marks]
 - (ii) *strike action*. [2 marks]
- (b) Explain **one** advantage and **one** disadvantage to the two managers of *MHS* being a public-private partnership. [6 marks]
- (c) Analyse the importance of the informal organization to *MHS*. [6 marks]
- (d) Discuss **two** approaches to conflict resolution at *MHS*. [9 marks]

5. Columbo Coffee (CC)

Columbo Coffee (CC) is a family business that produces four espresso coffee machines. *CC*'s objective is to provide the highest quality machines, but it is currently unprofitable.

Espresso coffee machine model	Price in \$	Existing market share	Future market growth
The Ventura	3000	Low	Low
The Crema	5000	High	High
The Rocket	1000	High	Low
The Fortuna	2000	Low	High

A marketing audit of the four espresso machines had the following results:

- The Ventura was *CC*'s best selling espresso coffee machine. It has the strongest brand loyalty of all four machines, but has been suffering from overseas competition. Many customers of The Ventura want a new, improved version. However, because of its weak financial position, the company has not been able to develop it.
- The Crema is *CC*'s exclusive luxury espresso coffee machine. Considerable publicity for *CC* was gained when it featured in a recent popular television series. Sales of The Crema are forecasted to grow further despite its high price.
- The Rocket has been very successful. However, technical problems have resulted in many customers returning their machines. Reduced brand loyalty and quality control are significant concerns.
- The Fortuna is the company's newest model. It was developed to replace The Ventura but consumer resistance has forced *CC* to keep The Ventura in production. The Chief Executive Officer (CEO) of *CC* sees The Fortuna as a potential market leader, but to achieve brand awareness this would require most of *CC*'s limited marketing budget.

The CEO of *CC* is considering reorganizing the four espresso coffee machines into separate cost centres.

However, before any decision is made the CEO receives an offer from its main competitor to work together. As part of a strategic alliance, the competitor will provide funds to allow *CC* to finance extension strategies or enter new international markets. The only condition is that The Ventura is discontinued. The family is divided. Some family members are worried about the impact of the business losing its most recognizable brand. Others think the competitor's offer will allow *CC*'s other three machines to achieve their full market potential.

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(Question 5 continued)

- (a) Define the following terms:
- (i) *market share* [2 marks]
 - (ii) *extension strategy*. [2 marks]
- (b) Explain **two** values of a marketing audit as a business tool for *CC*. [6 marks]
- (c) Analyse the implications for the CEO of converting *CC* into four cost centres. [6 marks]
- (d) Discuss whether the family should accept the offer of a strategic alliance with its competitor. [9 marks]
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