Diploma Programme
Programme du diplôme
Programa del Diploma

Business management
Standard level
Paper 2

Friday 10 November 2017 (morning)

1 hour 45 minutes

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]**.

8817 – 5014

7 pages

Section A

Answer **one** question from this section.

1. Pelican Pies (PP)

Pelican Pies (*PP*) produces high-quality pies that have limited brand loyalty outside of their local market. The prices of the pies are higher than those of *PP*'s competitors.

Table 1: Selected financial information for *PP* for the year ending 30 April 2017.

Number of pies sold	8000
Price of each pie sold	$4.00
Cost of goods sold per pie	$1.75
Expenses	
• Electricity per month	$200
• Rent of premises per quarter	$1000
• Promotional expenses per year	$1000
8 % interest per year paid on a loan of	$40 000
Tax	25 % of profits

For 2018, *PP*'s owner, Austin, is looking to increase sales beyond the local market by lowering prices and spending a greater proportion of *PP*'s promotional budget on above-the-line methods such as regional newspaper advertisements. To finance this type of promotion, Austin will have to increase his loan amount by $10 000.

Table 2: Selected financial information for the year ending 30 April 2018.

Number of pies sold	20 % increase on 2017 figure
Price of each pie sold	30 % decrease on 2017 figure
Cost of goods sold per pie	$1.75
Expenses	
• Electricity per month	$200
• Rent of premises per quarter	$1000
• Promotional expenses per year	200 % increase on 2017 figure
8 % interest per year paid on a loan of	$50 000
Tax	25 % of profits

(a) Describe **one** reason why brand loyalty would be important to *PP*. [2]

(b) Construct a profit and loss account for *PP* **for the year ending 30 April 2017** based on the figures in **Table 1** (*show all your working*). [4]

(c) Construct a forecasted profit and loss account for *PP* **for the year ending 30 April 2018** based on the figures in **Table 2** (*show all your working*). [4]

2. Moverse

Moverse operates in the health and fitness sector. *Moverse* is not a traditional gym with machines (equipment) and fitness instructors (trainers). The instructors themselves travel and run fitness classes in the buildings of large companies. Instructors all work part-time and are paid wages on a time rate basis.

Moverse currently sells its services to several large companies. They have a total of 727 employees enrolled on its programme.

- *Moverse* charges a yearly fee of $145 for each employee participating.
- *Moverse*'s fixed costs are $60 000 per year.
- The variable cost per employee taking part in the programme is $45.

(a) Describe the time rate method of paying wages. [2]

(b) Calculate the break-even quantity for *Moverse* (*show all your working*). [2]

(c) Construct a fully labelled break-even chart, to scale, for *Moverse* if 800 employees enroll on *Moverse*'s training programme. [4]

(d) Calculate the profit or loss if 800 employees enroll on *Moverse*'s training programme (*show all your working*). [2]

Section B

Answer **one** question from this section.

3. Davenport Electronics (DE)

Davenport Electronics (*DE*) is a small company that manufactures remote control electronic devices that open garage doors. The devices are kept in owners' cars. For years, *DE* devices operated in a fashion similar to those of its three competitors. When an owner activated the remote control, a unique password was transmitted and the garage door opened.

Unit sales and revenue had not grown for several years until, four years ago, some computer hackers discovered how to steal passwords when remote controls are activated. With the passwords, hackers could later open garage doors and steal their contents. For *DE* and its competitors (whose products operated in a similar manner), sales began to decline.

DE responded by developing a way to change the unique password every time a remote control is activated. Thus, by the time a hacker successfully steals a password, the password no longer works. *DE*'s innovation significantly enhanced the security of a *DE* remote control.

The three competitors are all larger than *DE*.

	Price of remote control	**Quality perception**
Company A	High	Medium
Company B	Medium	Medium
Company C	Low	Medium
DE	Medium	High

As a result of this innovation, *DE*'s market share and scale of operation have increased. However, *DE* is now experiencing diseconomies of scale. Some managers also worry that, with the pressure to meet increased orders, the company will lose its focus on quality. Other managers believe that future success in the industry will depend on frequent innovation.

(a) Define the term *diseconomy of scale*. [2]

(b) Using the table, construct a product position map/perception map for all four companies. [4]

(c) (i) Draw and label a product life cycle curve. [2]

(ii) Explain how *DE*'s innovation is an extension strategy. [2]

(d) With reference to *DE*, discuss the merits of small organizations compared to large organizations. [10]

4. Grunsburg Textiles (*GT*)

Grunsburg Textiles (*GT*) is a textile company founded by the paternalistic leader Henrik Steiner. As the company grew, it became very committed to corporate social responsibility (CSR). "Our aims," *GT* says on its website, "include making profits, providing safe and secure employment, contributing to society through investment in environmentally friendly production practices and supporting ethical causes". Many people believe that *GT*'s success is tied to its reputation for taking care of its employees and for its commitment to CSR.

In 2015, *GT* purchased €44 million in new environmentally friendly equipment. It financed the purchase with a bank loan. *GT* originally forecasted that the new equipment would generate €8 million in annual net cash flow. Instead, the actual increase in *GT*'s annual net cash flow from the new equipment was only €6 million. The Chief Financial Officer (CFO), Elaine, warned Henrik that unless net cash flow increased significantly, the average rate of return (ARR) would be significantly lower than originally forecasted.

GT is struggling to make the loan payments and to have sufficient working capital. Elaine determined that one way to shorten the working capital cycle is debt factoring. However, when she approached several (debt) factors, she was discouraged by their proposed discount rates.

Elaine knows that the situation is worse than she had warned. If the economy were to weaken and revenue to decline, she believes that the company could go out of business. Proposals for a solution include cutting back on *GT*'s commitment to its employees and CSR practices.

(a) State any **two** stages of the working capital cycle. [2]

(b) Calculate for *GT*:

(i) the payback period for the €44 million investment in new equipment based on the forecasted increase in net cash flow (*show all your working*). [2]

(ii) the average rate of return (ARR) based on an annual increase in net cash flow of €6000 and assuming an asset life of the new equipment of eight years (*show all your working*). [2]

(c) With reference to *GT*, explain **one** advantage **and one** disadvantage of debt factoring. [4]

(d) Examine Elaine's proposals to cut back on *GT*'s commitment to its employees and CSR practices. [10]

5. Green Clean (GC)

Green Clean (*GC*) is a private limited company controlled by the Hitta family. Its unique selling point (USP) is offering high-quality, reliable cleaning services by teams of professional cleaners who clean offices and houses.

GC has strong ethical objectives. They only use eco-friendly cleaning products and pay their employees fair wages. Labour turnover is low and many cleaners have worked for the company for over two decades.

However, the cleaning market has become very competitive. GC has been slow to react. Other cleaning companies are beginning to offer a wider range of services. *GC*'s management has decided to introduce a gardening service to maximize profit.

GC will recruit professionally trained gardeners. As it is very difficult to find professional gardeners in the market, *GC* will pay them 20 % more than its cleaners. *GC* prefers to use external recruitment. *GC*'s management will also offer cleaners the opportunity to become gardeners even though off-the-job training costs are very high. If most of *GC*'s cleaners choose training, the company could fall short of workers to meet the demand for cleaning services.

The cleaners are becoming demotivated because they are unhappy about the difference in pay between cleaners and future gardeners. They believe that gardeners are not more skilled than cleaners but just have a different skill set. Human resource managers are concerned about the potential impact of demotivated cleaners and are looking for ways to improve morale. One option they are considering is to offer cleaners an employee-share ownership scheme. Shareholders, however, are opposed to this proposal.

(a) Define the term *ethical objective*. [2]

(b) Explain **one** advantage **and one** disadvantage for *GC* of recruiting gardeners externally. [4]

(c) Explain **one** advantage **and one** disadvantage for *GC* of using off-the-job training for the cleaners who would like to become gardeners. [4]

(d) With reference to **two** motivation theories, examine the motivation of cleaners at *GC*. [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 **innovation** on operations management **strategy**. [20]

7. With reference to an organization of your choice, discuss the ways in which **globalization** can influence organizational **culture**. [20]

8. With reference to an organization of your choice, discuss the ways in which **ethics** and **change** can influence human resource management. [20]