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Business management
Standard level
Paper 2

Friday 15 November 2019 (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]**.

Section A

Answer **one** question from this section.

1. Small-Scale Hobbies (SSH)

Scale Airplane Modeller is a magazine produced by *Small-Scale Hobbies (SSH)*. The company sells the magazine through independent retail outlets in the US.

The finance director produced a summary of 2018’s financial information. Last year’s break-even chart showed that *SSH* had a margin of safety of 20 000 units.

Table 1: Selected financial data for SSH for 2018:

Annual fixed costs	\$100 000
Variable costs per magazine produced	\$2
Magazine price	\$4.50

This year, to reduce costs and to increase sales, the company will introduce new production methods, which will reduce:

- unit variable costs by 10 %
- fixed costs by \$5000 per year.

- (a) Define the term *margin of safety*. [2]
- (b) Using the financial data in **Table 1**, calculate:
- (i) the break-even level of output (*show all your working*); [2]
- (ii) the percentage of total costs that were fixed costs for last year (*show all your working*); [2]
- (iii) the level of profit for *SSH* at 2018’s level of production (*show all your working*). [2]
- (c) Explain how the introduction of new production methods will affect the total cost line in *SSH*’s break-even chart. [2]

2. **Daytona Go-Carts**

In 2020, Ron James aims to open *Daytona Go-Carts*, a race track where individuals as young as twelve can rent go-carts and participate in races. Through primary market research, Ron has discovered that many teenagers would enjoy participating in go-cart races.



[Source: <https://www.pexels.com>]

Ron has two options for locations for the go-cart race track:

- **Option 1:** The cost of the site would be \$1.2 million
- **Option 2:** The cost of the site would be \$1.8 million.

Forecasted profits for **Option 1** are:

Year 1	Year 2	Year 3	Year 4	Year 5
\$200 000	\$300 000	\$300 000	\$300 000	\$300 000

Forecasted profits for **Option 2** are \$300 000 in the first year, with profits growing by 20% per year for the next four years.

- (a) State **two** methods of primary market research. [2]
- (b) Calculate, for **Option 1**:
- (i) the average rate of return (ARR) (*show all your working*); [2]
 - (ii) the payback period (*show all your working*). [2]
- (c) Calculate, for **Option 2**, the average rate of return (ARR) (*show all your working*). [2]
- (d) Explain **one** reason why **Option 1** may be a less risky investment than **Option 2**. [2]

Turn over

Section B

Answer **one** question from this section.

3. Top Star (TS)

Top Star (TS) manufactures sports footwear. Its products are sold through retail outlets and online. Sales of *TS*' footwear in retail outlets are falling. However, because e-commerce is growing rapidly, online sales are increasing. In 2018, *TS*' total domestic sales were \$5 000 000 and total domestic market sales for the same time period were \$50 000 000.

TS must consider several challenges:

- Some businesses in the sports footwear industry are finding that selling online leads to many problems and higher costs
- *TS*' website is not user friendly. Customer complaints about the website and ordering problems are increasing
- *TS*' presence in international markets is weak and its product range is limited. The directors of *TS* want to develop a new line of running shoes but the company has insufficient finance for research, development and creating brand awareness.

The directors think that *TS* should follow an external growth strategy. Two options are being considered:

- **Option 1:** Some directors propose a merger with a footwear manufacturer, the multinational company *All Champion*, which would allow *TS* to be more competitive
- **Option 2:** Other directors propose a merger with a footwear retailer that has a strong presence in domestic and international markets.

The finance manager believes that merging with *All Champion* could hurt *TS*' reputation. *TS*' factories may have to close, which the local population may resent.

- (a) Describe **one** feature of a multinational company (MNC). [2]
- (b) Calculate *TS*' market share in 2018 (*show all your working*). [2]
- (c) Explain **two** disadvantages **and one** advantage to *TS* of selling its products online. [6]
- (d) With reference to *TS*, evaluate the two merger options. [10]

4. Imperial Falls (IF)

Imperial Falls (IF) is a luxury hotel in a city centre. The hotel is an old palace, elegantly furnished and overlooking the harbour. Of the highest quality, for decades *IF* has been the preferred hotel for business travellers to the city. Relying on reputation and word of mouth, *IF* does little promotion. Its facilities include a swimming pool and a high-quality restaurant. **Table 1** shows information about the principal hotels located in this city centre in 2018.

Table 1: Selected information about the principal hotels in the city centre in 2018

Hotel	Average room price per night	Service rating
A. Imperial Falls	\$245	5 stars
B. Bellevue	\$179	3 stars
C. Welcome Rest	\$215	4 stars
D. Excalibur	\$155	3 stars

In 2019, bookings at *IF* have begun to decline because of a new hotel, *Guest Rooms (GR)*, which is part of a global chain. Many businesses have employees who travel to major cities, where most business meetings occur. Hotels in city centres are usually luxurious and expensive. *GR* is different. It offers clean, small rooms with Wi-Fi, a small desk and a double bed. Room prices at *GR* are significantly lower than most city-centre hotels. The new *GR* is located near the airport, 6 kilometres (3.72 miles) from the city centre.

GR uses a fee-based membership model and member companies require employees to stay at a *GR* hotel when on business. Employees may also stay there when on personal travel. Guests use self-service check-in machines (similar to those used at airport check-ins), which issue electronic keys. *GR* electronically bills the company directly. Service is minimal. *GR* relies heavily on social media marketing. It also uses above-the-line promotion.

- (a) State **two** types of above-the-line promotion. [2]
- (b) Using **Table 1**, construct a product position map/perception map for all four hotels prior to the opening of *GR*. [4]
- (c) Explain **two** ways in which *GR* is able to offer rooms at a lower price than *IF*. [4]
- (d) Discuss possible changes to *IF*'s marketing mix to reduce the loss of customers to *GR*. [10]

Turn over

5. FrioAire Appliances (FA)

FrioAire Appliances (FA) manufactures medium-priced and medium-quality refrigerators. It is a multinational public limited company. Its factory is located in a less economically developed country that has high unemployment, a tradition of autocratic leadership and labour costs lower than *FA*'s home country. The factory is profitable, and *FA* pays consistently good dividends. Market growth for medium-priced and medium-quality refrigerators is limited.

As part of a strategic objective to increase productivity and to enter a fast-growing market for high-priced and high-quality refrigerators, *FA* is considering building a new factory in and relocating production to Germany. This would require closing the factory in the less economically developed country. The new factory will:

- use innovative technologies, including advanced robotics and 3D processes
- require fewer employees, but those it does require will need to have better skills and qualifications.

Germany has a highly skilled, qualified and productive workforce. The new factory would allow *FA* to reposition its products. However, *FA* would need to raise significant finance to build and equip the new factory.

FA's leadership style at the factory in the less economically developed country is autocratic. Members of *FA*'s board wonder whether this style would be suitable for the new factory in Germany, where workers have more bargaining power because of their high skill level and the labour-friendly cultural traditions. In Germany, *FA* would have to follow more regulations regarding the environment, health and safety, and employee rights.

FA workers in the less economically developed country are very loyal to *FA*, which has continued operation through a civil war at significant cost to itself (for security). If *FA* were to close in the less economically developed country, the workers would not find such good jobs.

- (a) Describe **one** disadvantage of operating as a public limited company. [2]
- (b) Explain **one** benefit **and one** cost to *FA* of using an autocratic leadership style. [4]
- (c) Explain **one** positive **and one** negative impact of *FA* on the developing country. [4]
- (d) Evaluate the option of building a factory in, and relocating, to Germany. [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 business **ethics**. [20]

 7. With reference to an organization of your choice, examine the impact of **innovation** on distribution **strategy**. [20]

 8. With reference to an organization of your choice, discuss the ways in which **culture** can promote or inhibit **change**. [20]
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