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**BUSINESS AND MANAGEMENT  
HIGHER LEVEL  
PAPER 2**

Friday 10 November 2006 (morning)

2 hours 30 minutes

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**INSTRUCTIONS TO CANDIDATES**

- Do not open this examination paper until instructed to do so.
- Answer four questions.

**1. E-commerce\***

Online retail sales in the world’s biggest markets rose last year by 26 % although this accounts for just 1.6 % of total retail sales.

The spread of fast Internet and broadband connections has been a key factor in contributing to the growth of E-commerce. The Internet has lowered the cost of going into business. Now, for the price of a computer, a fast connection and a good website, anyone with entrepreneurial spirit has the potential to reach customers worldwide with only a small number of legal restrictions.

One of the biggest commercial advantages of the Internet is lower operational costs, such as advertising. This usually results in lower prices.

The Internet is significantly changing consumer behaviour. The access to price information and the ease with which consumers can move from one site to another has made internet consumers very powerful. Consumers are also becoming more confident and are buying a wider range of products.

Many consumers now research their purchase online before walking into a store. Customers come to the shop well informed about the products, prices and available deals.

Competition on the Internet is intense. Firstly, E-commerce firms have to get customers to find their internet site. Then they have to overcome the lack of brand awareness. Trust in the brand and security issues are also concerns that need to be addressed. Indeed, a website is becoming increasingly important to a company’s brand image and service, even if the company does not sell online.

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\* E-commerce – is defined as the conduct of a financial transaction by electronic means. E-commerce often refers to purchases from online stores on the Web, otherwise known as E-commerce Websites. They may also be referred to as “virtual-stores” or Cyber stores.

[Source: adapted from *A Perfect Market* and *E-commerce takes off*, *The Economist* 13 May 2004]

- (a) Based on the information in “E-commerce”, identify **one** example from each of the four PEST factors. *[4 marks]*
  
- (b) Explain two possible advantages **and** one possible disadvantage to consumers of using the Internet. *[6 marks]*
  
- (c) With reference to an example of your choice, discuss the potential of E-commerce for business. *[10 marks]*

## 2. BMW’s Sustainable Value

*BMW* is a multinational German car manufacturing company. The following policy statements are adapted from the company’s “Sustainable Value Report”:

- for the *BMW Group*, commercial success is the prime strategic objective. The *BMW Group* believes that being socially responsible will lead to commercial success. Therefore, the *BMW Group* assumes social responsibility for its employees, shareholders, business partners and also the environment and society as a whole.
- the *BMW Group* seeks to communicate constantly with its numerous stakeholder groups.
- sustainability is about efficient resource management. This includes the use of materials and energy and the influence of these on the environment. The *BMW Group* seeks to reduce the environmental impact of its automobiles on man and the environment.
- the success of the *BMW Group* depends decisively on its attractiveness as an employer.

[Source: adapted from *Sustainable Value Report 2003/2004 BMW Group*]

- (a) Explain **two** possible benefits for *BMW* of operating as a multinational company (MNC). [4 marks]
- (b) (i) Distinguish between strategic objectives and tactical objectives. [2 marks]
- (ii) Explain how the *BMW Group* could implement in practice the following **two** policies
- a reduction of its environmental impact
  - an increase in its attractiveness as an employer. [6 marks]
- (c) Evaluate the view of the *BMW Group* that social responsibility will lead to commercial success. [8 marks]

### 3. Softco

J Welsh was recently appointed as the new chief executive of *Softco*, a software design and manufacturing company. The organization has been through a period of significant losses due to a lack of product innovation and high costs of production.

J Welsh has enormous personal energy and is very action-oriented. She is very keen to:

- deliver results immediately
- solve problems quickly and simply with the involvement of the people who ultimately carry out the decisions
- establish a new culture of trust and collaboration in the workplace
- ensure maximum employee involvement, maximum production as well as minimum wastage of resources
- provide employees from both the design and manufacturing functions with individual short-term contracts that are renewed only if performance targets are reached
- move from the existing tall hierarchy to a matrix structure.

Managers have considerable freedom to manage their departments. In the view of J Welsh giving people self-confidence should be an organization’s primary objective because it motivates employees.

- (a) Explain **three** practices that can be implemented by J Welsh to ensure “minimum wastage of resources”. [6 marks]
- (b) Explain two advantages **and** one disadvantage for *Softco* of moving from “the existing tall hierarchy to a matrix structure”. [6 marks]
- (c) With reference to Maslow’s hierarchy of needs and other relevant motivation theory, evaluate J Welsh’s view that “giving people self-confidence should be an organization’s primary objective because it motivates employees”. [8 marks]

**4. Landofnod**

*Landofnod* is a leading producer and online retailer of mattresses in Canada. It specialises in foam mattresses for double beds. *Landofnod* purchases the foam from a trusted and reliable company in Taiwan, and then manufactures the mattresses in its warehouse/factory in Toronto, Canada. It sells them on-line for \$500 per mattress.

As consumers have become more comfortable with buying goods online, the number of online retailers has grown significantly. *Landofnod* faces much more competition than it did five years ago. Consequently, it has found its stock levels rising. It is now thinking of introducing a JIT (just-in-time) method of production and stock control. It currently uses the LIFO system to value stock and had 30 mattresses in stock at the beginning of November 2005 that had cost \$197 each to purchase.

Purchases and sales for the past six months are shown in the table below.

Date	Purchases (units)	Cost per unit (\$)	Sales (units)
November 2005	100	200	90
December 2005	90	198	94
January 2006	120	202	85
February 2006	75	198	82
March 2006	80	196	75
April 2006	70	197	70

- (a) Suggest **one** reason why *Landofnod's* unit costs vary from month to month. [2 marks]
  
- (b) Using the information in the table, calculate:
  - (i) the value of the closing stock at the end of April 2006 (using the LIFO method of valuation). *(Show all your working)* [6 marks]
  
  - (ii) the value of gross profit for the six-month period November 2005 to April 2006 using the LIFO method of stock valuation. *(Show all your working)* [3 marks]
  
- (c) Examine **one** advantage of moving to a FIFO method of stock valuation. [3 marks]
  
- (d) Evaluate whether *Landofnod* should introduce a JIT (just-in-time) method of production and stock control. [6 marks]

**5. Arica Sportswear plc**

*Arica Sportswear plc* produces sports kits. The kits, which include shirts, shorts and socks, are sold by established sports shops across the European Union. The kits are sold to retailers for a premium price of \$120. In their marketing, *Arica Sportswear plc* justify the relatively high price by emphasizing the quality of the materials used and the fact that each kit is customized with the team's logo and sponsors' names. The *Arica* brand is highly regarded by their target market of 12 to 24 year olds who are extremely loyal to the brand. The company's products are used by many international teams, and endorsed by a number of sports and entertainment celebrities who have their names displayed on their *Arica* kit.

Recently the manufacture of the kits was relocated to a factory in a developing country. Each kit now costs *Arica Sportswear plc* \$43 with an additional printing cost of \$12 per kit. This cost is \$10 lower per kit than when *Arica Sportswear plc* produced in their home country.

Sales representatives receive a commission of \$3 per kit sold to retailers. Some have begun to complain that this commission does not reflect the sales effort required in an increasingly competitive market segment. The transport costs for each kit is \$2. The fixed costs of production are \$720 000 per month. The factory capacity is 16 000 kits per month, and since last month, when a special marketing campaign took place, the factory is working at full capacity. The marketing manager has proposed to the board of directors that the price of the kits to retailers should be increased by 15 % to reflect their popularity and to address the problems posed by their limited production capacity.

- (a) With reference to *Arica Sportswear plc*
  - (i) distinguish between fixed and variable costs. [2 marks]
  - (ii) calculate the contribution earned per kit after relocation.  
(Show your working) [2 marks]
- (b) Construct a break-even chart and identify
  - (i) the monthly output of kits required by *Arica Sportswear plc* to break-even.
  - (ii) the margin of safety if the factory is producing at full capacity.
  - (iii) the monthly level of profit assuming 16 000 kits are manufactured and sold. [8 marks]
- (c) Evaluate the marketing manager's proposal to increase the price of *Arica* sports kits to retailers by 15 %. [8 marks]

**6. Show-off Limited**

*Show-off* is a private limited company producing fashion accessories for laptop computers and mobile phones. The following is an extract from the chief executive officer’s (CEO’s) annual statement to the board of directors:

“The year’s trading has been strong and market trends are upwards reflecting the positive economic environment. Investments made over the last year have contributed to our success. After discussion with the marketing director, I am proposing further expansion of the business into accessories for digital cameras and portable music players. This will require the purchase of a new production facility with technologically advanced manufacturing equipment, plus the recruitment of 200 additional employees.”

The marketing manager supports the proposals, but suggests more detailed market research is needed before a final decision is reached. The financial director provided the following financial data for *Show-off Limited*:

	<b>2004</b>	<b>2005</b>	<b>2006</b>
Sales revenue	\$42 million	\$62 million	\$98 million
Current ratio	1.8	2.2	2.4
Acid test ratio	1.4	1.1	0.8
Return on capital employed (ROCE)	12 %	16 %	22 %
Gross profit margin	42 %	44 %	45 %
Net profit margin	11 %	9 %	8 %
Rate of stock turnover	25 times	30 times	38 times
Gearing ratio	40 %	40 %	70 %

- (a) Describe **two** potential limitations of ratio analysis. [4 marks]
- (b) Analyse the types of market research that *Show-off Ltd* can undertake to support their expansion decision. [7 marks]
- (c) Discuss whether the present financial position of *Show-off Ltd* justifies the CEO’s planned expansion. [9 marks]