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**BUSINESS AND MANAGEMENT
HIGHER LEVEL
PAPER 2**

Friday 20 May 2011 (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.

SECTION A

Answer **one** question from this section.

1. Strider Retail

Strider Retail is a chain of shops that import and sell electrical appliances, including plasma (screen) televisions. The sale of plasma televisions is seasonal, in particular when major sporting events are being held. Plasma televisions are expensive. Research has indicated that with improvements in technology the cost of importing new models has fallen significantly. *Strider Retail* expects this to continue into the future.

The following information shows *Strider Retail's* purchases and sales of plasma televisions over a six month period from July 2010 to December 2010.

Opening stock of plasma televisions on 1 July 2010: 150 @ US\$900.

Month (2010)	Stock purchased (units)	Stock sold (units)
July		120
August	100 @ US\$900	90
September	75 @ US\$850	75
October	60 @ US\$825	40
November	75 @ US\$800	100
December	100 @ US\$800	120

Strider Retail has conducted additional secondary research, which reveals that the product life cycle for electrical appliances, such as plasma televisions, is getting shorter with new models being produced every three months. This research has suggested that *Strider Retail* may have to reduce its selling prices much more often.

With so many sporting events being shown on television, the seasonal factors in determining the sales of plasma televisions are becoming less important. *Strider Retail's* marketing manager thinks that *Strider Retail* should move to a just-in-case stock control method, rather than the current just-in-time stock control method.

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(Question 1 continued)

- (a) Define the following terms:
- (i) *secondary research* [2 marks]
 - (ii) *just-in-time stock control*. [2 marks]
- (b) (i) Calculate the closing stock value for *Strider Retail* at the end of December 2010 under FIFO **and** LIFO using a table to clearly identify for each month the number of plasma televisions purchased, sold and stock remaining. [8 marks]
- (ii) Comment on the implications for *Strider Retail* of using LIFO as a method of valuing its stock. [3 marks]
- (iii) Briefly explain **one** advantage and **one** disadvantage for *Strider Retail* of using the just-in-case stock control method for plasma televisions. [4 marks]
- (c) Analyse the impact of a shorter product life cycle for plasma televisions on *Strider Retail's* cash flow. [6 marks]

2. Esperanto

After having successfully produced a number of new technological products and conducted considerable research and development in the consumer goods market, *Esperanto* was finally ready to launch the UniTran. The UniTran is the world’s first communication device, which can instantly translate spoken English, French or Spanish into over 121 different languages.

Initial customer feedback before the marketing and product launch has been very positive, despite the very high price of the device (US\$2400). Primary market research was conducted by *Esperanto* using a quota sample of communication experts, international journalists and language teachers. In addition, doctors and rescue workers from the non-governmental organization (NGO) *Medicine Sans Frontiers*¹ were given samples of the UniTran to test and give feedback to *Esperanto* as part of a snowballing market research exercise.

Esperanto felt that a product of such importance needed a suitable campaign to target a number of other niche market² segments. A marketing agency, *New World*, was used to help plan and coordinate the marketing and product launch for 1 January 2011. *Esperanto*’s chief executive officer (CEO) agreed the following sequence of activities with *New World*’s marketing team:

Activity	Estimated duration (weeks)
A	2
B (must follow A)	2
C (must follow B)	5
D (must follow B)	7
E (must follow C)	4
F (must follow D)	3
G (must follow E and F)	3
H (must follow G)	2
I (must follow H)	5

If early sales of UniTran were disappointing, *New World* was keen to make a quick adjustment to the marketing mix. Given the initial feedback on the UniTran, *New World*’s perception was that the product required a very short channel of distribution. *Esperanto* felt the opposite. It was confident that the UniTran had the potential to become a global product and would require much longer channels.

¹ *Medicine Sans Frontiers*: a NGO committed to providing immediate medical aid to war zones and areas of high disease density in the developing world.

² niche market: a highly specialized market segment focused on a group of consumers with particular tastes, income levels, etc. The product is not expected to be consumed in large quantities.

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(Question 2 continued)

- (a) Define the following terms:
 - (i) *research and development* [2 marks]
 - (ii) *snowballing*. [2 marks]
- (b) Briefly explain **one** advantage and **one** disadvantage for *Esperanto* of only conducting primary market research. [4 marks]
- (c) (i) On the lined paper provided for your answer, construct a fully labelled network diagram to represent the sequence of activities in the table. Show the earliest starting time (EST) and the latest finishing time (LFT) for each activity **and** the critical path. [6 marks]
- (ii) Calculate the total float on the network diagram and comment on its implications for *New World* (show all your working). [3 marks]
- (iii) Briefly outline **one** benefit to *New World* from constructing the network diagram. [2 marks]
- (d) Analyse *New World's* suggestion to use short distribution channels for the UniTran. [6 marks]

SECTION B

Answer *two* questions from this section.

3. Lego

Since 1932 the Christiansen family has owned and managed *Lego*, the toy brick maker from Denmark. The toy brick was twice voted “Toy of the 20th Century”. *Lego’s* success has been based on providing a quality product and a strong recognizable global brand. Consistent company objectives have not included maximizing profit. Due to these factors, *Lego* has built up considerable goodwill and other intangible assets such as brand loyalty.

Lego’s financial results from 2004 were a shock to their stakeholders. A move into diversified markets such as clothing, theme parks and watches had resulted in significant losses. A number of rumours began to circulate that *Mattel*, an American toy manufacturer, would try to takeover the struggling European company. However, by 2009, the company had achieved large profits.

Financial information for *Lego* (all figures in US\$ millions)

	2004	2009
Net profit/loss before interest and tax	–332	380
Sales revenue	1513	2010

[Source: adapted from <http://cache.lego.com/downloads/aboutus/annualreport2004UK.pdf> and <http://cache.lego.com/downloads/aboutus/AnnualReport2009GB.pdf>, 20 October 2010]

Lego spokesperson, Charlotte Simonsen, admitted that the company had made some mistakes by moving into diversified markets. She also highlighted other changes in the external environment with social trends suggesting that consumer tastes are moving towards computer games. Using technology, *Lego* has now created a 3D web site where customers can design their own toys and then order the bricks to build it. A computer-generated *Lego* film could also be released in 2012.

Charlotte also believes that *Lego’s* successful return to achieving large profits was due to the economic downturn (recession) of 2008–9. She argues that “during difficult economic times, parents return to trusted global brands for durable quality and familiar toys for their children”.

[Source: adapted from *The New Zealand Herald*, 9 August 2009]

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(Question 3 continued)

- (a) Define the following terms:
- (i) *profit* [2 marks]
 - (ii) *takeover*. [2 marks]
- (b) (i) Briefly explain **two** benefits of brand loyalty to *Lego*. [4 marks]
- (ii) Calculate the net profit margin for *Lego* for 2004 **and** 2009. [2 marks]
- (c) Analyse **two** possible reasons why *Mattel* would have tried to takeover *Lego*. [6 marks]
- (d) Given the changes in the external environment, discuss whether *Lego* has changed its objectives towards achieving larger profits. [9 marks]

4. Enigma

Enigma is a large company, which generates and distributes electricity to over 90% of households in a cold country in Northern Europe. From September to March, daily temperatures are below zero. The average annual wage is the lowest in Europe.

Using price discrimination to generate substantial profits, *Enigma* charges the business community higher rates than it charges rural poorer communities. *Enigma* has calculated that the price elasticity of demand for electricity is such that demand is very unresponsive to price changes. However, by early 2009, some pressure groups felt that *Enigma's* revenue and profits had become too high. *Enigma's* chief executive officer (CEO), Bjorn Andersson, defended the high revenue and profits. He argued that they were necessary for *Enigma* to guarantee electricity supply throughout the cold months.

However, by the end of 2010 *Enigma* made a substantial loss due to the economic downturn (recession). As a result, the country's government organized a "rescue package"* to guarantee electricity supply. At the annual general meeting held in 2011, *Enigma's* financial accounts revealed that senior managers had been awarded substantial performance related payments, despite the significant losses. Most shareholders believed that the rescue package was used to reward inefficient senior managers. They argued that it was unethical for *Enigma* to use public money in this way, especially during the economic downturn (recession).

Bjorn did not agree. He argued that despite the economic downturn (recession), *Enigma* had to reward its senior managers as other electricity companies do; he said that "superstar talent requires superstar reward packages". To ensure that there will be a future generation of highly-skilled senior managers, Bjorn claimed that he had only one option: to offer million dollar reward packages. This practice would also help to recruit and motivate the best university graduates to work for *Enigma*, who could then be trained through job enrichment schemes to become the next generation of senior managers.

* "rescue package": a government financial plan to help key industries affected by the credit crisis to remain in business despite significant losses or liquidity problems

- (a) Define the following terms:
- (i) *price elasticity* [2 marks]
 - (ii) *shareholder*. [2 marks]
- (b) Explain **two** advantages to *Enigma* of using price discrimination. [6 marks]
- (c) Using Herzberg's motivational theory, analyse the motivation of *Enigma's* senior managers. [6 marks]
- (d) Evaluate solutions to **two** possible stakeholder conflicts present at *Enigma*. [9 marks]

5. Ansell

Ansell is a state-owned telecommunications company in Uruguay, South America. It has a 25% market share of the home telephone market and has experienced slow growth in revenue over the last 10 years.

In 2005, the Uruguayan government passed legislation to allow foreign companies to enter the home telephone market. Immediately, *Allo*, a French multinational telecommunications company, spent large amounts of money setting up a network, as selling in Uruguay was seen as a way of entering the South American home telephone market. *Allo* soon became the market leader and its market share doubled that of *Ansell*. *Ansell* missed out on opportunities to compete and earn substantial profits due to limited finance, inappropriate technology and an autocratic leadership style.

The Uruguayan government is now passing further legislation to enable even more competition in the home telephone market. *Ansell* has three options.

- The first option for *Ansell* is to merge with *Ronaldo*, a telecommunications company based in Brazil. *Ronaldo* has a different leadership style to that of *Ansell* and is also struggling financially. The financial and marketing benefits from the merger could be considerable for both companies. However, *Ansell* realizes that the corporate culture of the two companies are very different, which may lead to potential diseconomies of scale. Furthermore, a number of redundancies would be inevitable.
- A second option is to form a joint venture with the Italian multinational telecommunications company *Pronto*. Consequently, *Ansell* could benefit from *Pronto*'s up-to-date technology, knowledge and global experience in the home telephone market to compete against *Allo*. In return, *Pronto* would be able to research potential opportunities to enter into the South American home telephone market. Unfortunately, *Pronto* can only commit to the joint venture for one year, which may not give *Ansell* enough time to compete effectively with *Allo*.
- As a third option, *Ansell* could increase its customer base by expanding its services to the rural areas of the country, where *Allo* and other competitors are not currently operating. *Ansell* is developing a new service called "Rural-Ansell" to cater for the needs of this promising market segment. However, the company's limited finance may compromise this alternative.

(a) Define the following terms:

(i) *corporate culture* [2 marks]

(ii) *diseconomies of scale*. [2 marks]

(b) Explain **two** reasons for the growth of multinational telecommunications companies in Uruguay in the home telephone market since 2005. [6 marks]

(c) Analyse the consequences of clashes in leadership styles if *Ansell* and *Ronaldo* merge (first option). [6 marks]

(d) Discuss the second and third options available to *Ansell*. [9 marks]