



**BUSINESS AND MANAGEMENT
STANDARD LEVEL
PAPER 2**

Friday 22 May 2009 (morning)

1 hour 45 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 in this section.

1. Nails by Joomin

Joomin Kim runs a beauty shop called *Nails by Joomin* specializing in manicures and pedicures. The business operates as a sole trader. Joomin wants to take advantage of the growth of the business and its good reputation by opening a second store in a shopping centre about 10 kilometers from the original location.

A friend suggested to her that she could develop the business by franchising and increasing her economies of scale, but Joomin wants to own the new store and maintain control. She is considering restructuring as a private limited company. Joomin will finance the new store using \$25 000 from her savings and \$50 000 from a bank loan.

She anticipates revenues and expenses for the first 6 months of the new store (January to June 2010) as follows:

- initial balance: \$75 000 (savings and bank loan)
- initial start-up expenses: \$15 000
- monthly rent: \$2000
- store manager monthly salary: \$2000 (increasing by 6% in month 3)
- monthly loan payment: \$1000
- monthly expenses for additional labour: \$1000 for the first month, increasing by 20% per month
- initial revenue: \$2000 a month, increasing by 20% each month.

She was able to obtain this loan because of the strength of her personal financial position (she owns her own house and has no mortgage).

(a) Define the following terms:

- (i) *franchise* [2 marks]
- (ii) *economies of scale*. [2 marks]

(b) (i) Prepare a monthly cash flow forecast for the first 6 months of operation of the new store. [6 marks]

(ii) Comment on the projected cash flow forecast of the new store. [4 marks]

(c) Examine **two** difficulties that small businesses like *Nails by Joomin* face in obtaining sources of finance for expansion. [6 marks]

2. Duranjaya Packaging

For 20 years, Nirav Duranjaya has operated a cardboard manufacturing facility on the outskirts of Mumbai specializing in selling mass-produced, low-cost cardboard boxes for industrial users. Price is the most important factor in determining the demand for the boxes. Gross profit and net profit margins in the business are low, and the workers are unskilled and low paid. *Duranjaya Packaging* advertises in specialized publications for the industries in which it sells.

In recent years, with the economy rapidly growing, the market for higher-margin, distinctive and creative packaging solutions has boomed in India. To enter this lucrative higher-margin market and satisfy growing demand, *Duranjaya Packaging* would have to hire three highly qualified packaging designers and create a more flexible workforce. The decision to move into this new market may require a restructuring of the business and a new more democratic management style, with employees taking more responsibility for their work. *Duranjaya Packaging* is currently organized as a tall hierarchical structure with a low span of control. Nirav supervises his employees closely and all decisions have to be passed through him.

Nirav estimates that fixed costs for producing the new creative packaging solutions would be as follows:

- rent: \$36 000
- utilities: \$6000
- packaging designer's salary: \$30 000
- Nirav's salary: \$16 000.

Variable costs for the new creative packaging solutions will be \$0.12 per box and the sales price will be \$1 per box. In the first year Nirav estimates that *Duranjaya Packaging* will produce 140 000 boxes.

- (a) Define the following terms:
- (i) *fixed costs* [2 marks]
- (ii) *variable costs*. [2 marks]
- (b) Prepare a fully labelled break-even chart for *Duranjaya Packaging*. [6 marks]
- (c) Comment on **two** factors that will determine whether Nirav adopts a new management style. [4 marks]
- (d) Examine **two** elements in the marketing mix, **other than price**, that *Duranjaya Packaging* will need to adapt in order to move into the creative packaging solutions market. [6 marks]

SECTION B

Answer **two** questions in this section.

3. PA

PA makes pre-assembled parts of vehicles, called modules, for major car companies. For example, PA assembles cooling systems, which are then shipped to the car manufacturer for installation. Modules are produced in batches at PA and are transported frequently to arrive just-in-time for installation by the car manufacturers.

Major car manufacturers increasingly prefer to buy modules from other firms rather than make them themselves. Doing so allows the major car manufacturers to lower costs and be more flexible.

PA has formed joint ventures with other firms to supply major car manufacturers. One such joint venture, called *Piston Modules LLC*, is between PA and *Continental Teves* to assemble brake modules for several car manufacturers. The joint venture will lease land at PA's Michigan Avenue factory, located in Detroit, creating 100 new manufacturing jobs.

The joint venture will require specialized equipment costing \$10 million. With a bank loan to be repaid over 5 years, PA will acquire the equipment, which the joint venture will lease. The lease term will be 5 years.

Piston Modules LLC will be 51% owned by PA and 49% owned by *Continental Teves*.

[Source: adapted from *Inc. 500* and <http://www.pistongroup.com/>, November 2007]

- (a) With reference to stock control, define the term *just-in-time*. [2 marks]
- (b) (i) Distinguish between batch production and flow production. [2 marks]
- (ii) Explain **two** economies of scale *Piston Modules LLC* could benefit from. [4 marks]
- (c) Examine **two** human resource issues *Piston Modules LLC* may face as a result of creating 100 new manufacturing jobs. [5 marks]
- (d) Discuss the appropriateness of the bank loan to PA as a source of finance for the \$10 million in equipment. [7 marks]

4. Coolibar®

Coolibar® designs and manufactures clothing that protects wearers from the sun. The firm was founded in 2001 by John Barrow of Australia, who wanted to bring some of Australia’s advanced approaches to sun protection to the American market.

The name *Coolibar*® and the company logo are derived from the Australian eucalyptus tree. All *Coolibar*® brand products block 98% of ultraviolet rays, giving them an Ultraviolet Protective Factor (UPF) of 50. After extensive initial market research, the company designed clothing for fashion and health conscious Americans aged between 18 and 30. Focus groups indicated that many American consumers disliked designs popular in Australia. Surveys indicated that certain Americans would pay a premium price for sun protective clothing.

Coolibar® knew of rising skin cancer rates in the United States and of growing concern among aging Baby Boomers* about skin cancer. Over the last 25 years, melanoma (skin cancer) rates have almost tripled in America. According to the *National Cancer Institute*, American males have a 1 in 82 chance of developing skin cancer.

In 2007, *Coolibar*® was one of the 500 fastest growing privately-held companies in the United States. However, the market for sun protective clothing is growing and many new competitors are entering the market. *Coolibar*®, aware that it must constantly respond to market needs, is planning a new phase of market research in order to write a new 5-year marketing plan.

[Source: adapted from *Inc. 500* and <http://www.coolibar.com/>, November 2007]

* Baby Boomer: a person who was born during the so-called “baby boom” between 1946 and 1964

- (a) Define the term *market research*. [2 marks]
- (b) Distinguish between **three** different market segments for *Coolibar*®’s products. [6 marks]
- (c) Analyse the role that primary market research played in *Coolibar*®’s redesign of their clothing for the American market. [5 marks]
- (d) Discuss the importance and role of branding for *Coolibar*® when launching their clothing in the American market. [7 marks]

5. NetShops

NetShops began as a business to customers (B2C) e-commerce company in 2002. Founded by Doug Nielson, it began with a single online “store” and now owns and operates over 200 online stores selling a wide range of products targeted at various niche markets.

One of the reasons that the firm has grown so quickly is its “*NetShops* Affiliate Program”, which allows other businesses to place links on their own web sites to the *NetShops*’ website. When a customer purchases a product from *NetShops* as a result of following one of these affiliate links, the affiliate company earns a commission on this sale.

NetShops is able to quickly launch additional online stores in niche markets for which traditional channels of distribution do not exist. No single online store accounts for more than 5% of the total sales of *NetShops*.

NetShops maintains an online database of all purchasers. The company uses software to obtain select personal data (e-mail and regular post addresses, for example) and to record purchases in their shops. *NetShops* also knows which of its sites and products customers have viewed. The firm can identify customers’ interests and purchasing trends, from which it can develop consumer profiles.

[Source: adapted from *Inc. 500* and <http://www.netshopsinc.com/>, November 2007]

- (a) Define the term *e-commerce*. [2 marks]
- (b) (i) Explain the difference between internal and external growth. [2 marks]
- (ii) Comment on the nature of *NetShops*’ growth. [4 marks]
- (c) Examine the usefulness of consumer profiles to *NetShops*. [5 marks]
- (d) Discuss the costs **and** benefits to consumers of *NetShops*’ e-commerce approach. [7 marks]
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