

Business management
Standard level
Paper 2

Friday 9 November 2018 (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. Piper Industrial (PI)

Piper Industrial (PI) manufactures pipe. The company is highly profitable and its corporate tax rate is 20%. *PI* is forecasting major capital expenditure for 2019.

Table 1: Selected forecast financial information for the year ending 31 December 2019

Cost of goods sold	\$15 000 000
Expenses	\$4 700 000
Gross profit	X
Interest	\$1 000 000
Net profit after interest and tax	\$3 440 000
Net profit before interest and tax	\$5 300 000
Net profit before tax	\$4 300 000
Sales revenue	\$25 000 000
Tax	Y

Table 2: Annual cash flow forecast for the year ending 31 December 2019

Receipts from debtors	\$24 000 000
Total receipts	\$24 000 000
Payments to creditors	\$14 000 000
Payments for expenses	\$4 600 000
Payments to banks for debt	\$1 200 000
Capital expenditure	\$2 700 000
Total payments	\$22 500 000
Net cash flow	Z
Opening balance	\$3 700 000
Closing balance	\$5 200 000

(This question continues on the following page)

(Question 1 continued)

- (a) Define the term *capital expenditure*. [2]
- (b) Using **Table 1**, calculate for *PI*:
 - (i) gross profit (**X**); [1]
 - (ii) tax (**Y**). [1]
- (c) Using **Table 1** and your calculations in (b)(i) and (ii), construct a profit and loss account for *PI*. [2]
- (d) Using **Table 2**, calculate the net cash flow (**Z**) for *PI* for 2019 (*show all your working*). [2]
- (e) Explain the difference between profit and cash flow. [2]

2. Patras Furniture (PF)

Patras Furniture (PF) manufactures chairs. *PF* uses batch production.

Currently, *PF* sells 200 chairs per month. Each chair sells at an average price of €100. Below are the forecasted fixed and variable costs for 2019.



Table 1: Fixed costs

Rent	€24 000
Insurance	€6000
Salaries	€11 000
Lease on equipment	€40 000
Cleaning service	€18 000

Table 2: Variable costs per chair

Material	€50
Delivery	€5

- (a) Define the term *batch production*. [2]
- (b) (i) Calculate the break-even level of output for *PF* for 2019 (*show all your working*). [2]
- (ii) Construct a fully labelled break-even chart, to scale, for *PF* for 2019. [4]
- (iii) Calculate the forecasted profit if *PF* sells 2400 chairs in 2019 (*show all your working*). [2]

Section B

Answer **one** question from this section.

3. Jacob Strutz (JS)

Jacob Strutz (JS) is an American multinational company that produces jeans. Founded in 1860, for 100 years *JS* enjoyed steady growth in sales, mostly in the United States and then in Canada and Mexico. In the 1960s and 1970s, when teenagers worldwide began wearing jeans, *JS*'s sales increased significantly. *JS*'s premier product is Strutz's No.5 jeans, one of the best-known brands in the world.

In the late 1970s, *JS* operated 71 factories in the United States. In 1994, its sales peaked at \$7.6 billion worldwide, but then began to decline. In 2002, *JS* made the decision to close its last remaining factories and outsource manufacturing to foreign manufacturers, whose quality was more difficult to control. By 2017, annual sales were only \$4.5 billion. Even sales of Strutz's No.5 jeans declined, and *JS* faced intense competition, including foreign competition.

JS briefly experimented with fast fashion, an industry practice developed in the United States in response to cheap, foreign imports. In fast fashion, new design concepts are quickly manufactured once they have been tested at fashion shows. Unfortunately, fast fashion worked against *JS*'s brand identity. Surveys indicated that *JS*'s brand has value and inspires loyalty, though focus groups of young consumers did not perceive *JS* as cool.

JS has been a leader in corporate social responsibility (CSR). Since the 1890s, it has pursued profits through values. More recently, *JS* introduced Strutz's chemical-free jeans. Because many of *JS*'s suppliers operate in areas with few pollution regulations, to remain consistent with its image of CSR, *JS* is insisting that suppliers follow innovative but expensive chemical-free processes.

- (a) Define the term *multinational company (MNC)*. [2]
- (b) Explain the importance to *JS* of:
 - (i) brand value; [2]
 - (ii) brand loyalty. [2]
- (c) (i) Draw and label a product life cycle for Strutz's No.5 jeans. [2]
(ii) Explain the position of Strutz's No.5 jeans on the product life cycle. [2]
- (d) Discuss the role **and** impact of globalization on the growth and evolution of *JS*. [10]

4. Dana’s Handbags (DH)

Dana’s Handbags (DH) is a small manufacturer of women’s handbags. *DH* sells directly to large retail chains in Europe. The company is privately owned and has fifteen shareholders.

Table 1: Selected financial data for *DH* for 2016 and 2017 (figures in \$000s)

	2016	2017
Sales revenue	28 000	29 000
Cost of goods sold	14 000	15 000
Gross profit	14 000	14 000
Net profit after interest and tax	1370	1300
Total current assets (at year end)	5000	5200
Total current liabilities (at year end)	3000	3500
Stock (inventory)	3000	3200
Cash	1000	900

Beginning in 2017, *DH* adopted a programme of corporate social responsibility (CSR) by:

- donating money to charities
- encouraging employees to do three paid hours per week of community service during work hours
- using only biodegradable materials in its handbags.

This programme was expensive.

DH’s management thought that a programme of corporate social responsibility (CSR) would strengthen *DH*’s brand. During the first year of the corporate social responsibility (CSR) programme, employee morale improved and *DH* received favourable media attention.

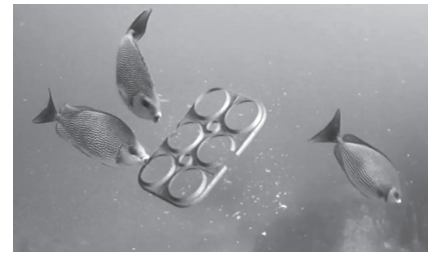
However, at the annual general meeting in January 2018, financial results from 2017 revealed that sales growth had not improved. Several influential shareholders complained about the high cost of the corporate social responsibility (CSR) programme. Other shareholders suggested that *DH* should develop consumer awareness that it is a socially responsible company.

- (a) Identify **two** features of a private limited company. [2]
- (b) Calculate:
- (i) the net profit margins for *DH* for 2016 **and** 2017; [2]
- (ii) net current assets (working capital) for *DH* for 2016 **and** 2017. [2]
- (c) Explain **one** method of above-the-line promotion **and one** method of below-the-line promotion that *DH* could use to raise consumer awareness that it is a socially responsible company. [4]
- (d) Discuss *DH*’s decision to develop a policy of corporate social responsibility (CSR). [10]

5. Benno

Benno is a soft drinks manufacturer. Its mission statement is “to produce healthy drinks without damaging the environment”.

Competition in the healthy soft drinks market is fierce. *Benno* uses a competitive pricing strategy. However, sales of *Benno*’s drinks have fallen significantly over the last five years, particularly in the 12–18 age group. The business has no accumulated retained profits.



Benno is committed to innovation and corporate social responsibility (CSR). Its research and development division has recently invented a new biodegradable drink pack ring that starts to break down within two hours of contact with sea water. It dissolves fully in 48 hours. Currently, 98 % of pack rings are made of plastic and when dumped in the sea are responsible for the death of many sea creatures.

A focus group of loyal customers used regularly by *Benno*’s marketing department is wholeheartedly in favour of the new drink rings. However, the marketing director has read recent studies that suggest:

- purchases of green products are not increasing, despite the positive attitude of many consumers towards sustainability and biodegradable products
- consumers continue to prioritize price when purchasing soft drinks.

To manufacture the new drink rings, machinery costing \$5 million would be needed. Drink ring production unit costs would rise from 10 cents to 15 cents and prices of a six-pack of *Benno* soft drinks would have to increase by 5%. *Benno*’s net profit margin on a six-pack is 10 %.

Benno’s director of corporate social responsibility favours the change to the new drink rings but is opposed by both the finance director and marketing directors.

[Source: Image provided with permission from E6PR™]

- (a) Define the term *innovation*. [2]
- (b) Explain **two** roles of *Benno*’s mission statement. [4]
- (c) Explain **one** advantage **and one** disadvantage for *Benno* of using a focus group of loyal customers. [4]
- (d) Recommend whether *Benno* should replace its plastic drink rings with the new biodegradable drink rings. [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 promotional **strategy**. [20]

 7. With reference to an organization of your choice, examine the impact of **globalization** on **change** in operations management. [20]

 8. With reference to an organization of your choice, examine the impact of **ethics** and **culture** on human resource management. [20]
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