

General Certificate of Education
January 2003
Advanced Level Examination



BUSINESS STUDIES
Unit 4

BUS4

Monday 27 January 2003 Morning session

In addition to this paper you will require:

a 12-page answer book.

You may use a calculator.

Time allowed: 1 hour 30 minutes

Instructions

- Use blue or black ink or ball-point pen.
- Write the information required on the front of your answer book. The *Examining Body* for this paper is AQA. The *Paper Reference* is BUS4.
- Answer **all** questions.
- The Case Study is printed on pages 2, 3 and 4 which can be unfolded.
- The perforated page, page 5, containing the questions should be detached before the examination.
- Do all rough work in the answer book. Cross through any work you do not want marked.

Information

- The maximum mark for this paper is 84.
- Mark allocations are shown in brackets.
- You will be assessed on your ability to use an appropriate form and style of writing, to organise relevant information clearly and coherently, and to use specialist vocabulary, where appropriate.
- The degree of legibility of your handwriting and the level of accuracy of your spelling, punctuation and grammar will also be taken into account.
- Up to 4 marks will be awarded for the quality of your written communication.

Read the Case Study and answer **all** the questions that follow.

Skiing Out of Control?

Streeter Skiwear's annual results came as a huge shock to Denny. He had expected them to be as poor as his own. For the first time in 12 years as Chief Executive of PIQ plc, Denny felt vulnerable. In two weeks he would be facing City analysts with his annual results - and they were awful: revenue down 4.2 %, operating profits down 31.5 % and retained profit down 39 %. He had been intending to blame 'the difficult world economic position', but as his main rival Streeter had boosted profit by 27 %, this excuse would seem lame. In recent weeks the stock market had slashed the share price of firms with worse-than-expected trading; then traders called for the Chief Executive to be sacked. He knew he would get a huge pay-off if the Board voted him out, but he hated the prospect of being called a failure. 5

Denny's first thought was to talk things through with Karen Almeida, his trusted Finance Director, and Jo Yasin, his Marketing Director. The three of them spent an afternoon considering the options. Denny grilled Jo on how Streeter had done it. Had they boosted market share? No. Clever advertising? No. Price increase? No. Streeter's success had not come from its marketing strategies. Indeed Jo was sure that they had struggled to keep up with PIQ in many markets. 10

Karen had the answer. She had spent the morning looking at the accounts posted onto Streeter's website (see Appendix A for extracts). She explained that Streeter's success came largely from greater financial efficiency. "If we don't do the same" she continued "we'll never be able to keep up with their investment level." 15

Denny muttered his thoughts to his two trusted colleagues. "My concern is about the impact of a sharp cutback on morale and our competitiveness. My hope is for us to become the number one in skiwear, but that requires heavy research and development spending to keep up with the latest clothing materials. Innovation and quality - those have been the twin pillars of our success - but for how much longer? Jo, you're always pressing for us to open a factory in Hungary. Perhaps we should go ahead with that." 20

"Good, I'm glad you're willing to look for radical solutions" said Karen. 25

The next day Denny asked the company's regional trade union organiser to come and see him. She was a whizz-kid unionist, only three years out of Warwick University with a degree in industrial relations, and Denny had come to trust her instincts and ability to keep secrets. He showed her the latest (as yet unpublished) accounts, and those of the rival, Streeter plc. She looked grave and asked how she could help. Denny made it plain that trading conditions were too tough at the moment to allow for growth. The only option was cost cutting. 30

The union organiser took the news surprisingly well. Her main concern was that any pain should be shared equally between the management, the workforce and the shareholders. She even offered to try to persuade union head office to put money into retraining any staff that needed to be redeployed within the company. 35

After three days of conversations and careful thinking, Denny formulated two alternative strategies for PIQ:

1. Move the clothing factory to Hungary, making 300 British staff redundant. This would cost £3 million in the short-term, but cut labour costs per unit to just £1.20 for ski suits with a retail price of £90! The investment should improve profits by £1.2 million for each of the next four years. 40

2. Move the UK business upmarket, abandoning the economy skiwear range and focusing on high fashion, high price ski clothing and equipment. This would require a £4 million investment in new machinery and research and development, but should lead to increased prices and margins resulting in profit increases of: 45

Year 1 £600 000 Year 2 £1 200 000 Year 3 £1 800 000 Year 4 £2 400 000

The union organiser was quick to calculate the payback and Average Rate of Return on the strategy options, then offered union funds to pay for retraining her members if the second option was chosen. She also said that “If you go for option 2, Denny, I’ll do all I can to persuade our members to co-operate with any changes to working practices. You’ve always wanted a no-strike agreement. I’ll put it forward as a way of showing our commitment to your strategy.” 50

Delighted by this reaction, Denny proceeded to talk with Jo about the marketing implications of strategy option 2. Would his team be able to push the product range upmarket? And what problems might there be with a new marketing plan and its co-ordination with the other functions within the business? Jo was happy to look into these points, and within a day had produced a graph showing the correlation between advertising and sales of skiwear (see Appendix B). 55

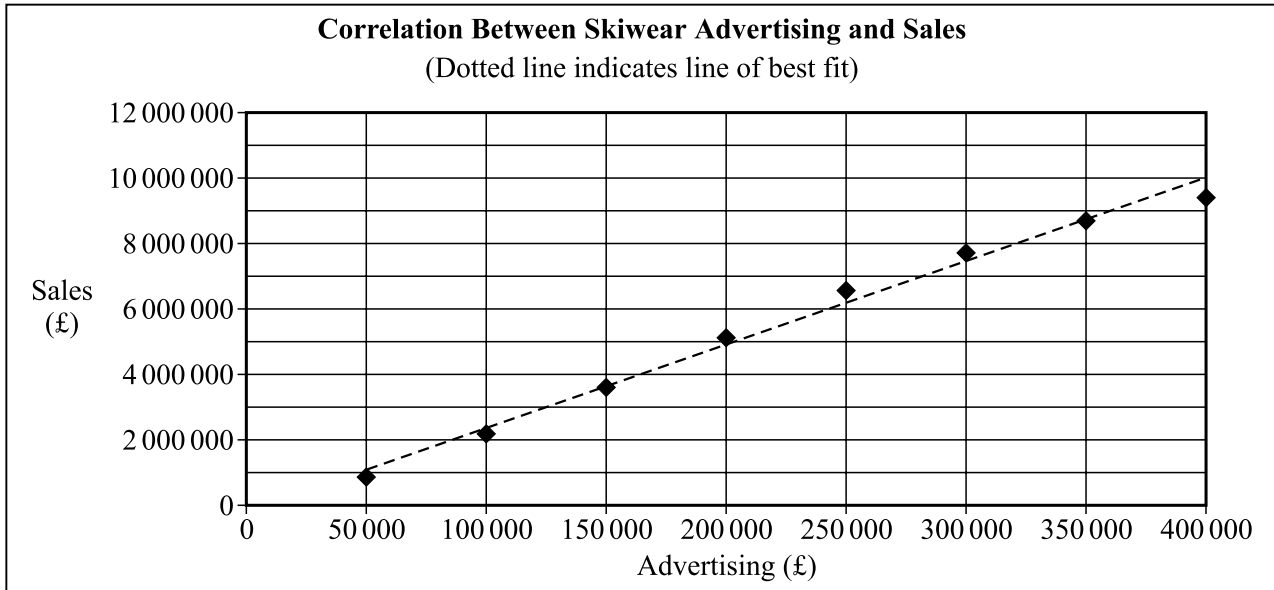
Karen was less impressed. She was very worried about option 2, which she termed “a leap in the dark”. She also seemed worried about how the investment outlays for either investment could be raised. Denny was more relaxed, pointing out that “if the workforce is behind us, there’s a lot of scope for improving our financial efficiency”. He asked Karen to look into this in more detail over the coming days. With the next Board meeting taking place on Monday week, there was still a great deal to be done. 60

APPENDIX A

Extracts from PIQ and Streeter accounts

	PIQ plc (as at 30/10/02) £millions	Streeter plc (as at 31/12/02) £millions
Fixed Assets	120	90
Stock	40	30
Debtors	50	20
Cash	5	15
Less Current Liabilities	35	35
Assets Employed	180	120
Loans	45	40
Shareholders Funds	135	80
Capital Employed	180	120
	PIQ plc (year end 30/10/02)	Streeter plc (year end 31/12/02)
Sales Turnover	365	365
Cost of Sales	200	240
Gross Profit	165	125
Operating Profit	9	24

APPENDIX B



APPENDIX C

Investment Appraisal Data Plus 6 % Discount Factors

Appraisal data for Investment Strategy 1:

Payback: 2 years 6 months

Average Rate of Return: 15 %

Net Present Value: + £1 152 000

Discount factors (6%): Year 1: 0.94 Year 2: 0.89 Year 3: 0.84 Year 4: 0.79 Year 5: 0.75

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- 1 Examine the communication problems that might arise for PIQ plc from a decision to move clothing production to Hungary. *(8 marks)*

- 2 (a) Analyse PIQ's accounts to assess the weaknesses in its financial efficiency. *(10 marks)*

(b) Explain how PIQ might use operations management tools to improve its production efficiency. *(10 marks)*

- 3 Conduct an investment appraisal into Strategy 2, **either** by using Net Present Value (see Appendix C), or by payback **plus** Average Rate of Return. Compare your results with those provided for Strategy 1 and briefly explain which strategy you would recommend based on the numerical evidence (up to 2 marks for this). *(10 marks)*

- 4 (a) To what extent do you consider the union organiser is acting effectively to achieve the objectives of a trade union? *(12 marks)*

(b) If PIQ decides to adopt Strategy 2, to what extent should it rely on an increase in research and development spending to enable it to charge high prices for its skiwear? *(10 marks)*

- 5 (a) Strategy 2 would require an advertising campaign to support higher prices for PIQ's skiwear. Consider the value of Appendix B in setting a suitable budget. *(10 marks)*

(b) Discuss the problems Jo might face in developing a marketing plan for strategy 2. *(10 marks)*

END OF QUESTIONS