

**MARK SCHEME for the May/June 2007 question paper**

**9707 BUSINESS STUDIES**

**9707/03**

Paper 3 (Case Study), maximum raw mark 100

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began.

All Examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

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**1 Discuss the risks and rewards to Ade resulting from his original decision to set up his own business. [14]**

|           | Knowledge                              | Application                           | Analysis  | Evaluation   |
|-----------|--|---------------------------------------|---|--|
| Level two | 2 marks<br>Two or more relevant points | 2 marks<br>Good application to case   | 4–3 marks<br>Good analysis of Risks and rewards                 | 6–4 marks<br>Good judgement of arguments used for both risks and rewards |
| Level one | 1 mark<br>One relevant point made      | 1 mark<br>Limited application to case | 2–1 marks<br>Good analysis of one side or some analysis of both | 3–1 marks<br>Limited judgement shown e.g. by considering one side        |

Examiners' note: Max. of 9 marks if only either risks or rewards analysed/evaluated

- Risks – own capital (but ltd co.).
- Insecurity of income compared to previous job.
- Business could fail – what then?
- No real experience of running a business – but Young Enterprise could have helped him.
- Rewards – own boss – did not like working for large organisation.
- Able to keep profits if successful. These could be substantial.
- He seemed to have many of the necessary skills so rewards might exceed risks.
- In this case the rewards seem to have exceeded the risks – perhaps because of his personality helping to make the business successful.
- Threat to business may be seen as a risk to Ade.

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- 2 (a) Calculate the impact on the company's profit of stopping production of the stone sculptures. [6]

| Candidate answer only contains:  | Explanation  | Mark |
|--|--|------|
| Profit = revenue – total costs   | Formula only   | [1]  |
| Contribution = Revenue – direct costs<br>(Allow 2 marks for both formulae)   | Formula only   | [1]  |
| Profits increase by \$250000 assuming all costs are saved  | Now states or implies (incorrect) assumption   | [2]  |
| Profits will fall as overheads must still be paid – but incorrect result or only considers one of the overheads  | Some understanding of the important difference between direct and overhead costs     | [3]  |
| The product still makes a positive contribution – but incorrect contribution given.  | Recognises importance of this principle.   | [4]  |
| Profit falls by \$1m but no calculation of total profit OR makes contribution of \$1m (or contribution of \$2m if labour costs are assumed not to be direct) | Must have used the contribution principle correctly.                                 | [5]  |
| Profit falls from \$1.95m to \$0.95m OR just loss of \$0.05m   | Allow \$1.95m to a loss of \$0.05m if candidate assumes labour costs are not direct. | [6]  |

- (b) Considering your result from (a) and any other useful information, recommend whether Ade should stop production of the stone sculptures. [10]

|           | Knowledge   | Application                         | Analysis   | Evaluation   |
|-----------|---|-------------------------------------|--|--|
| Level two | 2 marks<br>Good understanding of issues shown e.g. two relevant points made | 2 marks<br>Good application to case | 3 marks<br>Good use of theory to explain points made   | 3 marks<br>Good judgement shown in making recommendation   |
| Level one | 1 mark<br>One relevant point made   | 1 mark<br>Some application to case  | 2–1 marks<br>Some use of theory to explain points made | 2–1 marks<br>Some judgement shown in making recommendation or good judgement but no recommendation |

Use own figure results from (a). Max. L1 for AN/EV if no use of answer to 2 (a) or other information

- Stop producing it: free up workshop space for products that might be more profitable.
- Contribution lowest of the 3 (or it makes a loss if contribution costing not used in a).
- Market research suggest changing tourist tastes; stone running out.
- Keep it: Still makes a contribution.
- Market research evidence may not be clear or unbiased.
- May lead to job losses.
- Will jewellery venture be successful?
- Company well known for these products.
- Outsourcing could lead to problems.

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**3 Evaluate the likely impact on the business of the forecast economic conditions in Appendix A. [14]**

|           | Knowledge                                   | Application                                  | Analysis  | Evaluation  |
|-----------|---|--|---|---|
| Level two | 2 marks<br>Two or more relevant points made | 2 marks<br>Good application to this business | 4–3 marks<br>Good use of theory to explain impact | 6–4 marks<br>Good judgement shown in assessing impact |
| Level one | 1 mark<br>One relevant point made           | 1 mark<br>Limited application to case        | 2–1 marks<br>Some use of theory to explain impact | 3–1 marks<br>Some judgement shown in assessing impact |

Examiner's note: Full marks possible for full evaluation of only two data items

- Inflation rising – adds to costs but might allow higher price rises.
- Unemployment rising – may cut labour costs due to lower wages (or lower wage rises) – will not affect demand much as goods are sold to tourists – but is it a sign that the tourist boom is over?
- Exchange rate depreciating – makes the country's exports look cheaper so good for tourism but if supplies are purchased from abroad then costs could rise.
- Interest rates not very important unless firm has high borrowing – no evidence.
- Overall impact uncertain and **DEPENDS** on several factors – more detail needed – how accurate have government forecasts been in the past, for example.

**4 (a) Using the two ratios suggested by the Finance Director, analyse and comment on the financial efficiency of Craft Designs. [10]**

|           | Knowledge                                | Application                                 | Analysis   |
|-----------|--|---|--|
| Level two | 2 marks<br>Two appropriate formulae      | 2 marks<br>Both ratios correctly calculated | 6–4 marks<br>Good use of theory to explain results |
| Level one | 1 marks<br>One appropriate ratio formula | 1 mark<br>On ratio correctly calculated     | 3–1 marks<br>Some use of theory to explain results |

Should use stock turnover and debtor days.

Stock turnover =  $28/4 = 7$  times (accept cost of goods sold/stock too = 4 times). This measures the effective management of stocks. On average stocks are reordered and sold 7 times (or 4 times) a year. This could be a reasonable figure for a manufacturing/retailing business but involves an opportunity cost of finance tied up – other results needed for effective analysis.

Debtor days =  $7/28 \times 365 = 91$  days. This is quite high given that many of the sales will be for cash. Other retail companies must be taking a long time to pay. This suggests poor management of debts/credit control policy.

Accept any ONE liquidity ratio too – may be viewed as a form of financial efficiency.  
E.G. Acid test = 0.66 and current ratio = 1. Allow creditors days ratio/stock days ratio.

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**(b) Outline TWO drawbacks to the ratio analysis that you have conducted. [4]**

|           | Knowledge                           | Application                       |
|-----------|-------------------------------------|-----------------------------------|
| Level two | 2 marks<br>Two drawbacks identified | 2 marks<br>Both drawbacks applied |
| Level one | 1 mark<br>One drawback identified   | 1 mark<br>One drawback applied    |

- Needs other time periods and comparisons with similar craft companies before realistic analysis can be undertaken.
- Have accounts been window dressed? How accurate are the accounts?
- Qualitative factors not considered.
- Other company ratios not provided.
- Analysis limited as only two ratios have been calculated.

**(c) Discuss TWO ways in which the Finance Director could improve the financial efficiency of the company. [8]**

|           | Knowledge                      | Application                     | Analysis                       | Evaluation  |
|-----------|--------------------------------|---------------------------------|--------------------------------|---|
| Level two | 2 marks<br>Two ways identified | 2 marks<br>Both applied to case | 2 marks<br>Both ways explained | 2 marks<br>Both ways are briefly evaluated or one way is well evaluated |
| Level one | 1 mark<br>One way identified   | 1 mark<br>One applied to case   | 1 mark<br>One way explained    | 1 mark<br>One way is evaluated  |

- Cut debtor period to other shops – but may hit sales if other producers are prepared to offer longer credit. How competitive is this market?
- Cut down on stocks e.g. finished goods – but will this offer the tourists less choice?
- Use JIT for supplies – but needs good transport and relations with suppliers and high stocks may be needed for seasonal products.

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**5 Evaluate the importance to Craft Designs of effective market segmentation in the tourist gift market. [14]**

|           | Knowledge  | Application                        | Analysis   | Evaluation   |
|-----------|--|------------------------------------|--|--|
| Level two | 2 marks<br>Good understanding of m. segmentation shown (may be by understanding benefits or by examples) | 2 marks<br>Well applied to case    | 4–3 marks<br>Good use of theory to explain the benefits of m. segmentation | 6–4 marks<br>Good judgement shown e.g. by examining why it might not be that important or why other factors are more important |
| Level one | 1 mark<br>Some understanding shown   | 1 mark<br>Some application to case | 2–1 marks<br>Some use of theory to explain benefits                        | 3–1 marks<br>Some judgement shown  |

- Define what it is – give examples in context. Segments are made up of groups of consumers who share common characteristics – e.g. age, country tourists come from, income, attitude towards environment etc.
- The tourist gift market is not one homogenous whole – market research will identify different groups of consumers who share common tastes and needs – company could aim products at the most profitable segments. This should help to increase sales and profits, could lead to effective market led approach.
- BUT how flexible can the business be?
- Should it move away from traditional products because of short term market research findings?
- Will emphasis on quality and tradition lead to greater success in the long run?
- Impact of macro-economy and effective management decisions in other areas of the business could be more important to sales than effective market segmentation.
- Cost of segmentation must not exceed the additional revenue gained from it.

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6/7 Use this grid

|             | Knowledge                                | Application                            | Analysis   | Evaluation  |
|-------------|--|--|--|---|
| Level three |  |  |  | 10–7 marks<br>Good judgement shown in arguments and conclusion      |
| Level two   | 3 marks<br>Good knowledge demonstrated   | 3 marks<br>Answer well applied to case | 4–3 marks<br>Good use of theory to explain points made | 6–4 marks<br>Good judgement shown in either arguments or conclusion |
| Level one   | 2–1 marks<br>Some knowledge demonstrated | 2–1 marks<br>Some application to case  | 2–1 marks<br>Some use of theory                        | 3–1 marks<br>Some judgement shown in answer                         |

**6 Discuss the relative importance of factors apart from external economic conditions that are most likely to affect the future success of this business. [20]**

- Numbers of tourists and the types of tourists – beyond the control of this company – BUT very important given the importance of tourism to overall sales.
- Natural disasters etc could be referred to from candidate's own experience.
- Quality issues – especially if outsourcing is increasingly used – could damage long term reputation.
- Trend towards environmental concern – could hit demand for products made from non-renewable resources.
- Ade's management of the business as it expands and the internal organisation of it.
- Management of people – attitude of Ops Manager, if typical, could spell trouble for company.
- Some assessment of the likely importance of these and other factors to this business.

**7 The Operations Director has proposed outsourcing all supplies of stone sculptures so that the company could start jewellery production. Discuss how Ade might try to solve what you consider to be the most important human resource and operational management problems that might result from this decision. [20]**

Max L1 for AN/EV if only problems not solutions or just HR or just OpsMan.

- Quality of outsourced products – need for TQM from suppliers?
- Reliability of supplies – need to hold additional stocks?
- New machinery might be required for jewellery – all important Ops Man issues.
- How could these be resolved?
- Training - cost, workforce planning – new skills needed – how to assess likely number of staff needed?
- Motivation of staff in workshops if they cannot retrain – HR issues likely to result from this decision. How might they be resolved?
- Allow evaluation marks for explaining the most important problems and for weighing up how these might be solved.