CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Level

BUSINESS STUDIES 9707/3

PAPER 3 Case Study **OCTOBER/NOVEMBER SESSION 2002**

1 hour 45 minutes

Additional materials:
Answer paper

TIME 1 hour 45 minutes

INSTRUCTIONS TO CANDIDATES

Write your name, Centre number and candidate number in the spaces provided on the answer paper/answer booklet.

Answer **all** questions.

Write your answers on the separate answer paper provided.

If you use more than one sheet of paper, fasten the sheets together.

INFORMATION FOR CANDIDATES

The number of marks is given in brackets [ ] at the end of each question or part question.

The business described in this paper is entirely fictitious.

You are reminded of the need for good English and clear presentation in your answers.

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The Castle Lodge

The Castle Lodge was established over 50 years ago as a high class hotel offering a quality service to wealthy guests. It has recently been taken over by Nikolai and Christina who became the directors of a newly formed private limited company. To purchase the hotel, they received financial backing from a number of investors and took advantage of generous loan terms from their bank.

Consumer demand within the hotel industry is constantly changing. Recent economic growth and the continuing rise in business activity is creating an increased need for luxurious business conference centres with the very latest facilities. The Castle Lodge was not designed for this kind of centre. Nikolai and Christina are considering a major investment programme. This would add a new section to the hotel which would contain a “state of the art” business conference centre.

To assist in the calculation of the likely cash flows from this investment, the following information has been estimated. The facility is expected to have a life span of five years. Preliminary market research indicates that the centre could achieve an occupancy rate (capacity utilisation) of 80% during the 250 business working days each year. The hire charge would be set competitively at $6000 per day. There will be variable costs of labour and food and additional overhead costs. These extra costs are estimated as being 40% of annual revenue from the centre. The construction cost is estimated to be $2.6 million.

Apart from the financial considerations, another factor to consider is the impact on the staff at the hotel. Currently all staff are on a full-time salaried contract. The conference centre would not be used at weekends. In addition, staff would not be required when the centre was not booked for a conference. Nikolai was convinced that the business would benefit from recruiting only part-time staff prepared to work flexible contracts. These workers would not always be needed to work a full week of 40 hours. They would be called in to work when the conference centre needed them. To be consistent, Christina feels that the existing staff should be given the same conditions of employment. This would give the operations manager of the hotel more flexibility. Nikolai and Christina do not want this change to lead to the existing loyal staff leaving the business as they work very effectively as a team.

Nikolai is convinced that the new conference centre would be profitable but he knows that Christina needs some hard evidence before she will support him. She is worried that they have never managed a new project such as this. Recent news reports that interest rates might have to rise to reduce inflation also concern her. They are also both aware that finance would not be easy to obtain for a large project like this. If they are to proceed with such a complicated investment then careful planning will be essential as there are so many different stages in the construction plans. They also realise that it has to be finished by September next year in order to be open in time for the new business conference season. They will have to move swiftly if they are to meet this schedule.

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Appendix A

Extract from Discount Tables	
Value of $1 at a discount rate of	10%
Now	1.0
End of Year 1	0.91
End of Year 2	0.83
End of Year 3	0.75
End of Year 4	0.68
End of Year 5	0.62

(a) **(i)** Suggest possible advantages to the business of employing a part-time and flexible workforce. [4]

(ii) Discuss how the directors might encourage these new employees to work effectively as part of a team. [8]

(b) **(i)** Conduct an investment appraisal of the new conference centre using the payback and net present value methods of appraisal. You may assume that all costs are paid and revenue is received in cash. [10]

(ii) Recommend whether Nikolai and Christina should proceed with this new investment. Using your results from **(b)(i)** and any other information available to you, explain the reasons for your recommendation. [10]

(c) Analyse the factors that the directors should consider when choosing an appropriate source of finance for this new project, assuming they decide to proceed with it. [8]

(d) Examine the usefulness of critical path analysis in planning and constructing the new conference centre. [8]

(e) Assume the owners decide to go ahead with the new conference centre. Suggest and evaluate a marketing strategy for the launch of this new centre. [12]

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