

**MARK SCHEME for the May/June 2012 question paper
for the guidance of teachers**

9771 BUSINESS AND MANAGEMENT

9771/02

Paper 1 (Strategic Decisions), 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, which would have considered the acceptability of alternative answers.

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Using the data in the case:

1 (a) Calculate the gross profit margin in 2010. [3]

Formula: $\text{Gross profit/revenue} \times 100$ (1)

$41.7/396.9$ (1)

= 10.5% (3 marks for correct answer only)

Award 3 marks if no % sign is included.

Award 3 marks if correct to 1 or 2 decimal places.

(b) Calculate the net operating profit margin in 2010. [3]

Formula: $\text{Net (operating) profit/revenue} \times 100$ (1)

$12.7/396.9$ (1)

= 3.2% (3 marks for correct answer only)

Award 3 marks if no % sign is included.

Award 3 marks if correct to 1 or 2 decimal places.

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(c) Comment on the usefulness to Redrow's directors of the results obtained in 1(a) and (b). [6]

	Knowledge AO1 2 marks	Application AO2 4 marks
Level 2	2 marks Candidate shows clear knowledge of net and gross profit and the difference between them.	3–4 marks Candidate clearly explains the usefulness of the results using clear case context.
Level 1	1 mark Candidate shows some knowledge of net and gross profit.	1–2 marks Candidate uses limited case context.

- Definition of gross and/or net profit margin (performance ratios).
- Allows a performance measure over time (comparison of 2010 figures with 2009).
- Gross profit margin 2009 was –32.4% v 10.5% in 2010.
- Net profit margin in 2009 was –39.4% v 3.2% in 2010.
- Profit measures are a key performance indicator (KPI).
- The figures indicate to the Redrow directors that the balance sheet is improving (helped by the rights issue).
- The results help to keep shareholders informed.
- Net profit enables the business to see how well overheads are being controlled.
- The higher the gross and net profit margins the better.
- Comparison with similar business would be useful.
- The difference between the figures suggest Redrow may have significant overheads.
- ARA.

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(d) Analyse the main elements of a **MARKETING** plan that Redrow could use to attempt to increase profit margins. [13]

	Knowledge AO1 2 marks	Application AO2 5 marks	Analysis AO3 6 marks
Level 3		5 marks Candidate fully engages with the case context.	5–6 marks Candidate fully develops analytical points.
Level 2	2 marks Candidate shows clear and precise knowledge of a marketing plan.	3–4 marks Candidate links case material to his answer.	3–4 marks Developed analysis of arguments.
Level 1	1 mark Candidate offers a sufficient definition/ understanding.	1–2 marks Candidate makes a limited attempt to apply knowledge to the case study.	1–2 marks Weak analysis of ideas, failure to develop points.

- Definition/stages of a marketing plan.
- Recognition and use of the key elements of a marketing plan such as marketing audit.
- Recognition of the corporate objectives of Redrow.
- The marketing strategy (4p's).
- Price: consumers are price sensitive (elastic PED?) should the business considering lowering prices to reduce stock? Impact on margins.
- Product: Successful new heritage range. Incentives to attract first time buyers such as free carpets.
- Place: Construct developments in high demand areas with less exposure to government sector jobs.
- Promotion: Budgets are limited but the business could continue the award winning Redrow TV.
- Analysis of the performance of the strategy will be required. This could include surveys, normal distribution analysis and changes to profit margins.
- ARA.

Maximum of 9/13 if the answer only considers the 4p's.

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SECTION 2

	Knowledge AO1 3 marks	Application AO2 6 marks	Analysis AO3 8 marks
Level 3		5–6 marks Arguments are consistently based upon case context.	6–8 marks Candidate fully develops analytical points.
Level 2	2–3 marks Candidate shows detailed knowledge.	3–4 marks Candidate makes a good attempt to apply knowledge to the specific case scenario.	3–5 marks Developed analysis of arguments.
Level 1	1 mark Candidate shows some knowledge.	1–2 marks Candidate makes very limited attempt to apply knowledge to the specific case study.	1–2 marks Weak analysis of the ideas, failure to develop points.

	Evaluation Descriptor AO4	Marks
High	Extensive reasoned judgement in answer and conclusion.	6–8
Mid	Good judgement shown in the answer and conclusion or extensive judgement in answer or conclusion.	3–5
Low	Weak judgement shown in answer or conclusion.	1–2

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2 Evaluate the impact of a sustained increase in UK interest rates on Redrow. [25]

Interest rate parameters

- Definition of interest rates.
- What is the likely interest rate in its historical context?
- How large is the increase (refer to table)?
- How quickly will they rise?

External to Redrow

- Reduced demand as higher rates increase mortgage costs (fixed rates?).
- Demand for housing is interest rate sensitive.
- Speculative demand could fall further as net yields fall.
- Redrow specialises in low cost homes that are often bought by 1st time buyers. This segment will be extremely sensitive to interest rate rises.
- Increased demand from downsizers?

Internal to Redrow

- Financing costs have fallen to £12m (2010) from £21.6m (2009) see accounts – largely due to the rights issue.
- The company is no longer highly geared (2010 = 10.8%).
- Net debt has been reduced to £47.1m (see reduction in bank loans as an example).
- Does Redrow borrow money at market or fixed interest rates?
- Does the builder use risk management strategies such as interest rate swaps?
- Interest cover ratio operating profit/interest $12.7/12 = 1.06$ (very low).
- Construction workers may demand higher pay.
- Reduce stock to minimise opportunity cost.
- Creditors to Redrow will press for quick payment.
- Redrow will try to delay payment to debtors.
- Interest rates are only one factor affecting Redrow and its customers. Other factors include employment levels and mortgage availability.
- ARA.

3 Discuss the extent to which the Board of Directors should respond to shareholder pressure for increased returns. [25]

- Define shareholders and returns.
- Returns in terms of share price and/or dividends.
- Refer to data re FT250 and rival builder Persimmon.
- The Morgans are possibly the largest shareholder so they have a vested interest.
- Redrow could try to increase the sale prices of homes (unlikely).
- Redrow could concentrate on maintaining and improving margins (possible).
- Redrow could try and educate its shareholders that the returns are acceptable in the current environment and point to current successes.
- What return is acceptable? And how can this be achieved?
- The reality of an oligopoly.
- XPED in terms of competitors pricing policies.
- Dividend income is unlikely in the current climate.
- Comparison with peer businesses.
- ARA.

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4 Redrow is considering two alternative strategies:

- **continue with the current strategy of only building residential houses**
- **diversify into the construction of commercial property as well as residential houses**

Recommend which of these strategies Redrow should adopt. Justify your recommendation. [25]

Option 1 (+)

- It is their area of expertise.
- Some encouraging signs in the data.
- Award winning marketing innovation.
- Vast experience in this sector.
- Take advantage of cost reduction strategy.
- Potential to expand the land bank at reasonable prices.
- Popular new heritage range of homes.
- Low interest rates are helping affordability.
- Some signs of improvement in key macroeconomic indicators.

Option 1 (–)

- Lower house prices may stifle demand.
- The credit squeeze.
- Potential interest rate rises.
- The company is not very diversified.
- Very competitive sector.
- Government austerity policies.
- Increasing unemployment.

Option 2 (+)

- Would enable some spreading of risk.
- (Ansoff matrix strategy).
- The sector is similar to residential building.
- Enable diversification of market exposure.
- Redrow started as a civil engineering company and adapted over time.

Option 2 (–)

- Similar to housebuilding.
- Porter 5 forces/generic strategies.
- Demand is relatively low at the moment.
- It is a competitive industry.
- They should not take risks in the current climate.
- The board and shareholders are divided on this issue.
- ARA.