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For Examiner's Use	
Examiner's Initials	
Question	Mark
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TOTAL	



General Certificate of Education  
Advanced Subsidiary Examination  
June 2014

# Applied Business

# BS03

## Unit 3 Financial Planning and Monitoring

Monday 19 May 2014 1.30 pm to 2.30 pm

**For this paper you must have:**

- a calculator.

**Time allowed**

- 1 hour

**Instructions**

- Use black ink or black ball-point pen.
- Fill in the boxes at the top of this page.
- Answer **all** questions.
- You must answer the questions in the spaces provided. Do not write outside the box around each page or on blank pages.
- Do all rough work in this book. Cross through any work you do not want to be marked.

**Information**

- The marks for questions are shown in brackets.
- The maximum mark for this paper is 60.
- You are expected to use a calculator where appropriate.
- Questions 2(c) and 4 should be answered in continuous prose. In these questions you will be marked on your ability to:
  - use good English
  - organise information clearly
  - use specialist vocabulary where appropriate.



J U N 1 4 B S 0 3 0 1

### Hebden Carpets plc (pre-issued)

Most of the carpet that is sold in the UK is imported from Europe and Asia. Hebden Carpets plc is one of the few remaining British manufacturers of carpets. The company was established by the Whyte family in the 1920s and became a public limited company in 1982. It has a reputation for supplying high quality carpets manufactured from man-made fibres such as polypropylene, as well as carpets made from wool (which tend to be more expensive). Hebden Carpets plc has won a number of awards, mostly for its environmentally-friendly manufacturing, and it uses these to promote its products. It benefits from regular appearances in the media and has received praise for employing over 5000 people in its two factories which are located in an area of high unemployment within Yorkshire.

The company sells its products mostly in the UK. However, its Board of Directors has recently implemented a strategy of selling to a number of European markets (including Germany and France), financing its expansion mainly through the sale of shares. It faces increasing competition from many other companies, including a major UK rival, Cormar Carpets Ltd ([www.cormarcarpets.co.uk](http://www.cormarcarpets.co.uk)). Since 2004, Hebden Carpets plc's profits have risen slowly, even during the difficult economic period after 2008. However, profits remain low, reaching £12.25 million in 2013, despite sales amounting to over £190 million. Its slowly improving financial performance and valuable brand image led to a take-over bid from a Chinese manufacturer in 2013. However, Hebden Carpets plc's shareholders rejected the bid, believing that the price offered per share was too low.

Despite rising profits, some shareholders are not entirely satisfied with the company's financial performance and are seeking higher profits (and therefore dividends) in the short term. They have opposed some of the Board of Directors' longer term plans which they judge to be too costly and too risky. These include a recovery and recycling scheme for recovering and reusing waste materials produced during manufacturing and from recycling customers' used carpets.

The company has major plans to expand its operations further. The first stage of this plan is to manufacture vinyl flooring for use in kitchens and bathrooms. An investment of £124 million is needed for a new purpose-built factory in Poland. This will be financed by a share issue and a further bank loan. The factory's products will be sold throughout Europe where the volume of sales of vinyl flooring products has risen steadily since 2000.

Hebden Carpets plc has conducted thorough primary market research as part of its financial planning for expansion. A number of large multinational companies supply the European market for vinyl flooring, making it highly competitive. Despite this, profits from vinyl flooring are approximately 50% higher than those from carpets. The company has a good distribution network in Europe and good relations with many major retailers.

#### Pre-examination Research Tasks

- (a) Hebden Carpets plc operates as a public limited company. Research the advantages and disadvantages to its stakeholders of operating in this way.
- (b) Investigate the major issues that a company may consider before deciding whether or not to undertake a large investment.





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**2** Read **Item A** and then answer the questions that follow.

**Item A**

**Flawed plans?**

Hebden Carpets plc's Board of Directors is reviewing its plans following pressure from some shareholders to increase short-term profits.

Market research suggests that if prices of polypropylene carpets are reduced by 5%, the company's sales of this type of carpet would rise from 20 000 to 26 000 rolls per year, whilst fixed costs and the variable costs per roll of carpet would be unchanged. Sales of polypropylene carpets only contributed 20% of the company's profits in 2013. The company's financial performance from the sale of polypropylene carpets in 2013 is summarised in **Figure 1** below.

**Figure 1: Hebden Carpets plc – revenue, costs and profit from polypropylene carpets in 2013**

Item	£
Revenue from polypropylene carpet sales (20 000 rolls of polypropylene carpet at an average price of £4000 per roll)	80 000 000
Fixed costs	17 550 000
Variable costs of producing 20 000 rolls of polypropylene carpet (at £3000 per roll)	60 000 000
Profit for the year	2 450 000

To be environmentally friendly remained a priority for the Board of Directors. The finance director had been monitoring the company's business plan for recovering and reusing waste materials produced during manufacturing and recycling customers' used carpets. The company invested £20 million during 2012 and 2013 in technology and training to allow it to implement the recovery and recycling scheme. Sixty percent of the investment was financed from the company's profits and 40% from a bank loan. Although the technology is new and untried, it is expected to reduce the company's material costs by a minimum of £2.5 million each year.



**2 (a)** Using **Item A** and **Figure 1**, calculate the change in the company's profit for polypropylene carpets in 2013 if it reduced its prices per roll by 5%. State, by circling, whether the profit is an increase or a decrease.

Complete the table below.

**[8 marks]**

Item	Original figures £	Revised figures £
Revenue	80 000 000	
Fixed costs	17 550 000	
Variable costs	60 000 000	
Total costs	77 550 000	
<b>Profit for the year</b>	<b>2 450 000</b>	

<b>Change in profit</b>	<b>£</b>
	Increase / Decrease

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**2 (b)** Using **Item A**, explain why Hebden Carpets plc's stakeholders would want the company to monitor its recovery and recycling scheme.

**[6 marks]**

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**2 (c)** Do you think that reducing its use of resources by recovering and recycling waste will benefit Hebden Carpets plc? Justify your decision.

**[10 marks]**

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- 3 Read **Item B** and then answer the questions that follow.

**Item B**

**Polish flooring?**

Hebden Carpets plc's plan to invest in a new factory in Poland to manufacture vinyl flooring is nearly complete. The new factory would produce vinyl flooring for sale in Europe. The company has no experience of producing vinyl flooring products, although it has good relations with retailers selling flooring products throughout Europe. The company has involved many of its managers in drawing up its budget for the first year of trading.

The plan to invest in a new factory has not proved popular with some shareholders who are concerned about short-term profits. The company will have to negotiate loans totalling nearly £50 million as well as selling shares to finance its plans. Prices for vinyl flooring products declined by 3% in 2013, as more companies entered the market, and it is difficult to forecast future prices accurately. Costs are also expected to change, though forecasts on this vary.

The new factory will generate 750 jobs in Poland as well as 159 additional jobs in the UK. The UK jobs are planned for an area of high unemployment within Yorkshire.

- 3 (a) The budget for the new factory has been drawn up by the managers. Complete the budget below by filling in the shaded spaces.

**[2 marks]**

**Budget for the new factory (January to December 2015)**

	January – March £m	April – June £m	July – September £m	October – December £m
Sales of vinyl flooring	36.71	43.12	50.73	53.94
<b>Revenue</b>	<b>36.71</b>	<b>43.12</b>	<b>50.73</b>	<b>53.94</b>
<b>Costs</b>				
Interest payments	2.73	2.87	2.91	2.99
Other fixed costs	12.75	12.90	13.01	13.11
Materials	14.21	16.69	20.96	21.40
Wages and salaries	6.93	7.78	9.25	10.47
Other costs, including marketing	4.12	4.81	5.12	6.86
<b>Total costs</b>	<b>(4.03)</b>	<b>(1.93)</b>	<b>(0.52)</b>	<b>54.83</b>
<b>Profit or (loss)</b>	<b>(4.03)</b>	<b>(1.93)</b>	<b>(0.52)</b>	<b>54.83</b>





**4** Hebden Carpets plc’s stakeholders have opposing views on whether the company should go ahead with the new factory in Poland. Analyse the arguments **for** and **against** opening the new factory. You should advise Hebden Carpets plc whether or not it should go ahead with the new factory and justify your decision.

**[16 marks]**

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END OF QUESTIONS



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