

**ADVANCED SUBSIDIARY GCE
APPLIED BUSINESS**

F246/SM

UNIT 7: Financial Providers and Products

STIMULUS MATERIAL

SERIES 3

[It is intended that this stimulus material is used for the January 2008 and June 2008 examination sessions.]

Additional materials: No additional materials are required.



INSTRUCTIONS TO TEACHERS

- This stimulus material provides a vocational context for the internally assessed unit (Unit F246 – Financial Providers and Products).
- Each year one scenario will be released on OCR's web-site which will provide an authentic vocational context for candidates' subsequent investigations.
- Although it is intended that this stimulus material is used for the January 2008 and June 2008 examination sessions, there is no shelf life on this OCR generated stimulus material.
- If you wish to generate your own stimulus material for this portfolio unit, please ensure it is fit for purpose and adheres closely to the guidelines as laid down in the unit specification.
- There are no separate marking criteria with this stimulus material.
- Once the candidate has produced their financial package, they must then consider its effectiveness, given a change in future circumstances to their customer. At this point you must provide additional guidance on what these future changes could be, referring to the unit specification as a source of further information.

INFORMATION FOR CANDIDATES

- This stimulus material has been created to provide you with a vocational context for the internally assessed unit (Unit F246 – Financial Providers and Products).
- If you have any questions regarding the stimulus material, you must consult both your teacher and the unit specification.
- Once your financial package has been generated you must then consider its effectiveness, given a change in future circumstances to your customer. At this point, you will be provided with additional guidance from you teacher to allow you to carry out this evaluative task.

This document consists of **6** printed pages and **2** blank pages.

McCoy's Precision Engineering Ltd (MPEL)

Introduction

MPEL is a family business owned by four shareholders. They are Mr William and Mrs Evelyn McCoy, their son Jim McCoy and their daughter who currently resides in Australia.

The business was originally started 50 years ago by William who is now 80 years old and experiencing good health. William visits the factory at least three times a week but does not play an active part in running the business. He has left the running of the business to his son, Jim. William's wife, Evelyn, who is a sprightly 74 year old, still helps Jim with the administrative side of the business and is fully aware of its current liquidity problems. 5

The business consists of a factory unit. The offices are at the front of the building. There are car parking spaces for up to 10 cars. The business owns the premises outright which were valued at £325 000 a number of years ago. 10

Jim has sole control of MPEL, although he does like to discuss some major decisions with his father; ultimately the final decision is his responsibility. MPEL supplies specialist engineering parts to various manufacturing industries. MPEL experienced major growth nine months ago when it secured some large contracts from the government and a large aircraft manufacturer. 15

The reputation of MPEL has been built on its ability to manufacture specialist parts to a high standard which fully meet the specifications required by the customer. MPEL has always been willing to adapt and change in order to meet differing customer needs. 15

Due to the specialist nature of the products being manufactured, MPEL runs an efficient stock control system which is broadly based on the principles of JIT. Large amounts of stock are not held within the business as they could quickly become obsolete. 20

MPEL has always made a healthy profit and liquidity had never been a problem. Regular and established customers had always met their debts within the agreed 30 day period. This enabled MPEL to keep its bank account in the 'black' and make payments to its own creditors on a regular basis. MPEL was therefore able to build up excellent relationships with its own creditors who had been willing to offer discounts which helped improve the overall profitability of MPEL. 25

Problems

When Jim secured the government and aircraft manufacturer contracts he did not feel the need to follow his usual strict credit control checks. He was blissfully unaware that the larger the organisation, the slower it is to pay.

Jim was so excited about the new large orders he had secured, he happily invested a lot of time and money into the development of the products ordered. These orders were fundamentally much larger than those MPEL was used to handling. Previously, the biggest order MPEL had ever secured was for £25 000. The new orders were often for amounts in excess of £125 000. Jim saw this as a great opportunity to expand MPEL and increase profits. In order to meet the new demands, he invested in new machinery and took on four new employees. MPEL took out a bank loan for £75 000 over five years in order to pay for the machinery which was secured on MPEL's premises. 30 35

Jim, to his horror has discovered such large organisations regularly take four to six months to pay their bills. This has left MPEL with serious liquidity problems. The once healthy bank balance has now turned into an overdraft which is growing on a daily basis.

MPEL's suppliers have been very patient but can no longer wait for payment. They are threatening to stop supplying MPEL if at least 50% of the amount owing within 21 days is not received.

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Jim is now struggling to cope. This is not the way he likes to do business. He has worked with MPEL suppliers for a long time and feels awful that he has let them down so badly. The bank has now called a meeting and wants to discuss how Jim intends to clear MPEL's overdraft which has now peaked at just under £50 000. The current overdraft limit is £50 000 which is also secured on MPEL's premises.

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The bank is still sympathetic, having dealt with MPEL since its conception. However, it wants to know what Jim is going to do. The bank manager has mentioned that if the overdraft goes much higher it will not be able to release the funds to meet the wage payment due in approximately three weeks time.

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With the help of his mother, Jim has managed to collate the following comparative figures for this year and last year – see Fig. 1 below.

| | Sales for year (£) | Purchases for year (£) | Debtors (£) | Creditors (£) | Bank balance (£) |
|------------------|--------------------|------------------------|-------------|---------------|------------------|
| This year | 2 250 000 | 1 575 000 | 780 000 | 370 000 | (50 000) |
| Last year | 750 000 | 525 000 | 75 000 | 42 000 | 26 000 |

Aged Debtors Schedule:

| Months | 1 | 2 | 3 | 4 | 5 | 6 |
|------------------|--------|--------|--------|---------|---------|---------|
| This year | 60 000 | 10 000 | 20 000 | 250 000 | 220 000 | 220 000 |
| Last year | 70 000 | 5 000 | | | | |

Fig. 1

Jim is now seeking advice about what he should do and how these problems could be resolved. He would like ideas and suggestions prior to his meeting with the bank manager. He feels that if he has a better understanding of the options available to MPEL he will not feel so overwhelmed during the imminent meeting. After all he is an engineer not a financial wizard!

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Jim's Personal Situation

Jim lives on his own not far from the factory in what is considered to be a 'nice semi-rural area'. He bought his house 10 years ago and has 15 years left on his mortgage.

Due to mounting financial pressures at work, Jim has continually reduced the amount of money he is taking out of MPEL. He is now facing his own financial problems.

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Having never previously been in debt, he has now found himself with a personal overdraft and large credit card bills. On one credit card he owes £4 500 and the other a further £3 000. Both appear to be charging him astronomical rates of interest. He no longer has any savings left, having used all of these trying to ease the liquidity problems within MPEL.

He has come to the conclusion that his personal financial situation needs to be overhauled and is investigating a wide range of possible financial products and providers to help improve the situation. Jim wants to find out what are the best deals currently available in relation to bank accounts, savings accounts, credit cards e.t.c. He is also open to changing his mortgage provider. He currently owes £62,000 on a repayment mortgage and is paying approximately £430 per month.

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Furthermore, it his parent's Golden Wedding anniversary in five months time. He is planning to take them to Australia for a month to visit his sister and her family. This trip is to be a surprise and, therefore, he needs to arrange all flights and holiday insurance without them finding out. He has investigated the cost of flights and feels that he will need to borrow at least £3,000 as a personal loan in order to make this possible.

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Jim has listed below his monthly income and expenditure (see Fig. 2). All figures relate to six months ago prior to MPEL starting to experience liquidity problems. He feels that if MPEL's liquidity problems can be resolved, he can sort out his own personal financial problems and return to the position he was in six months ago.

Estimated Monthly Income and Expenditure for Jim

| | £ | £ |
|---------------------------------------|-----|-------|
| Salary (net) | | 1 983 |
| Less expenses | | |
| Mortgage payments | 430 | |
| Council tax | 120 | |
| Food | 200 | |
| Electricity | 25 | |
| Oil | 90 | |
| Insurances, house and life | 75 | |
| Motor expenses | 170 | |
| Gym membership | 55 | |
| Credit card payments to clear balance | 250 | |
| Entertainment and leisure | 230 | |
| Savings | 200 | |
| Total | | 1 845 |
| Remaining | | 138 |

Fig. 2

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