General Certificate of Education
Advanced Level Examination
June 2014

Business Studies BUSS3

Unit 3 Strategies for Success

Friday 13 June 2014 9.00 am to 10.45 am

For this paper you must have:
- an AQA 12-page answer book
- a calculator.

Time allowed
- 1 hour 45 minutes

A

Instructions
- Use black ink or black ball-point pen.
- Write the information required on the front of your answer book. The **Paper Reference** is BUSS3.
- Answer **all** questions.
- Do all rough work in your answer 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 80.
- You will be marked on your ability to:
  – use good English
  – organise information clearly
  – use specialist vocabulary where appropriate.

Formulae for Financial Ratios

Financial ratio	Formula
Current ratio	current assets : current liabilities
Acid test ratio	liquid assets : current liabilities Where liquid assets are current assets – inventories (stock).
Return on capital employed % (ROCE)	$\frac{\text{operating profit}}{\text{total equity + non-current liabilities**}} \times 100$ ** Where this equals capital employed.
Asset turnover	$\frac{\text{revenue}}{\text{net assets}}$
Inventory (stock) turnover	$\frac{\text{cost of sales}}{\text{average inventories (stock) held}}$
Payables (Creditors) days **(Payables'* collection period)**	$\frac{\text{payables*}}{\text{cost of sales}} \times 365$ * Payables = creditors throughout this formula.
Receivables (Debtors) days **(Receivables'* collection period)**	$\frac{\text{receivables*}}{\text{revenue}} \times 365$ * Receivables = debtors throughout this formula.
Gearing	$\frac{\text{non-current liabilities}}{\text{total equity + non-current liabilities**}} \times 100$ ** Where this equals capital employed.
Dividend per share (in pence)	$\frac{\text{total dividends}}{\text{number of issued ordinary shares}}$
Dividend yield (%)	$\frac{\text{ordinary share dividend (in pence)}}{\text{current market price (in pence)}} \times 100$

Read the **case study** and then answer the questions that follow.

KLICK plc

Introduction

Klick plc was one of the internet's first digital media companies. Founded in 1994, it soon became a market leader and now provides the following:

- a search engine
- a news content service that includes current affairs, sports and entertainment
- a range of software programmes, including anti-virus software.

Its customers are other businesses who pay to advertise on Klick plc's website. The amount that Klick plc can charge its customers for advertising depends mainly on the number of visits to the website by its users.

Zak Davies' strategy

Between 2009 and 2013, the Chief Executive of Klick plc was Zak Davies. He had been set the objective of improving the profitability of the business. In 2009, the return on capital employed was only 5%. The shareholders wanted a significant and rapid increase in profits in order to enable greater dividends to be paid.

Zak decided to focus on the news content rather than on other areas of the business. His emphasis was on creating good quality news stories to increase visits to the company's website. More journalists and sales staff were recruited, whilst the budget for technological developments was significantly reduced, resulting in the closure of two of the three research centres.

Zak also significantly changed the human resource (HR) strategy. Previously, employees had been paid large salaries and had benefited from a generous profit share scheme. Zak's HR strategy included:

- lower basic salaries but large bonuses for hitting demanding targets
- removal of the profit share scheme
- reduction in the training budget
- making three thousand employees redundant, mainly software programmers.

This approach produced significant cost savings whilst maintaining revenues, but was also controversial. The profitability of the business was improved and higher dividends were given to shareholders. However, morale amongst the employees had been damaged and Klick plc had found it increasingly difficult to recruit journalists and sales staff.

Furthermore, industry experts had expressed concern about the long-term consequences of focusing on news rather than on technology. This had resulted in a fall in the share price. Klick plc is in a market that changes rapidly in terms of both innovation and consumer tastes. For example, there had been rapid growth in the popularity of software applications (apps) since 2011, but Klick plc had not competed in this market.

Turn over ▶

A new approach

In January 2014, Mehvish Khan replaced Zak Davies as the company's new CEO. Mehvish had been one of the senior product managers at Google who had developed a number of highly successful apps. These apps had encouraged significantly more visits to the Google site and had generated increased revenue.

At Google, Mehvish had a reputation for taking big risks, and because of this Klick plc's directors insisted that she undertake detailed market analysis before recommending her new strategy.

Mehvish has access to the vast amount of information on Klick plc's existing customer and user database which has enabled her to:

- identify the websites that its 700 million users have visited
- analyse which news content items Klick plc's users have found the most popular
- monitor how effective each business's advertising had been.

Mehvish recognised the limitations of using only this database to develop an effective marketing strategy and therefore carried out further market research. This confirmed her decision to take a different approach to Zak Davies. She believes that the business needs to re-establish itself at the forefront of online technology. She thinks that it should begin with apps which would be targeted mainly at new younger users. Klick plc would promote the apps on its website. The majority of its revenue from apps would come from selling them directly to users, with the remainder from increased advertising revenue resulting from more visits to the website.

Mehvish realises that she will need to re-open and to expand the research centres. The business has to retain its existing software programmers and to recruit some of the best in the industry. Mehvish believes that 'the key to success is to have the most talented, creative people you can working for you'. To attract and keep good staff, Mehvish intends to double the average salary paid, to reinstate the profit share scheme and to implement kaizen groups.

A number of Directors are opposed to Mehvish's proposal. One believes that the company does not have the resources to compete with larger scale rivals, such as Google, who are rumoured to be investing heavily in new apps. He thinks that the risk of failure is too high and that Klick plc should remain focused on improving the news content. This approach has generated improved profits and dividends.

The Finance Director is more concerned about the changes in Payables and Receivables days between 2012 and 2013. He worries that the company is giving too much trade credit to its advertisers.

Next week, Mehvish will hold a meeting with the Directors to try to convince them to accept her proposal to invest heavily in the apps business. They have already indicated that they will approve a new project only if it will achieve an average rate of return of 25%.

STATISTICAL APPENDICES

Appendix A: Financial data

Table 1: Selective ratios for Klick plc (year ending 31 December 2012)

Current ratio	1.4:1
ROCE	8%
Payables days	45 days
Gearing	15%
Receivables days	42 days

Table 2: Extracts from financial accounts for Klick plc (year ending 31 December 2013)

Balance sheet	2013	Income statement	2013
	£m		£m
Receivables	900	Revenue	6000
Cash	400	Cost of sales	4250
Total current assets	1300	Operating profit	1250
Payables	600		
Total current liabilities	800		
Non-current liabilities	1500		
Capital employed	12500		

Table 3: Selective industry average ratios 2013

Ratio	Industry average
Current ratio	2:1
ROCE	20%
Payables days	40 days
Gearing	40%
Receivables days	30 days

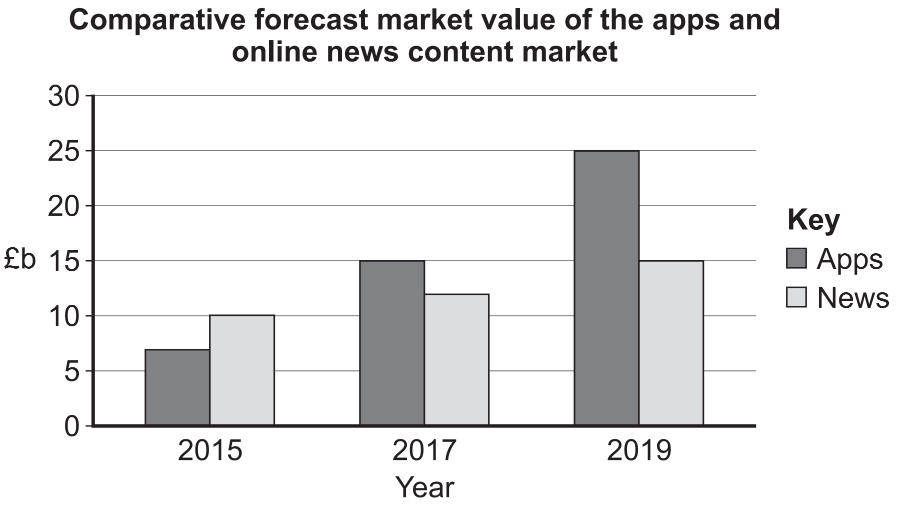
Table 4: Estimated returns of Mehvish's app proposal

Year	Net cash flow £b
0	(3)
1	0.5
2	1.0
3	1.25
4	2.0
5	3.5

Figures provided by Mehvish Khan, based on market research.

Turn over ▶

Appendix B: Marketing data – Secondary research



Appendix C: Human resource data 2009 – 2013

	2009	2013
Labour turnover of journalists and sales staff	10%	20%
Average number of days absent per employee per year	5	15
% of workforce that are software programmers	25%	10%
Annual training budget per employee	£1000	£500
Index of average revenue generated per employee	100	125
Index of labour costs as a % of revenue	100	60

Appendix D: Operations data 2013

	Klick	Apple	Google
% of revenue spent on Research and Development	3	22	20
Number of new software programmes launched	7	52	48
Average number of months to develop new software programmes	1	0.23	0.25

Question 1

0 1 Klick plc holds a vast amount of information on its database. Analyse the limitations if only this database was used when trying to develop an effective marketing strategy for the applications.

[10 marks]

Question 2

0 2 Zak Davies significantly changed the human resource (HR) strategy at Klick plc. Do you think that he was right to do this? Justify your view.

[18 marks]

Question 3

0 3 The Finance Director is concerned about the changes in the Receivables and Payables days figures between 2012 and 2013 shown in **Appendix A**. To what extent do you think that he should be concerned?

[18 marks]

Question 4

0 4 Using the information available to you, complete the following tasks:

- analyse the key arguments **for** and **against** Mehvish's proposal
- make a justified recommendation on whether you think that the Directors of Klick plc should accept Mehvish's proposal.

[34 marks]

END OF QUESTIONS

There are no questions printed on this page