

CAMBRIDGE INTERNATIONAL EXAMINATIONS
General Certificate of Education Advanced Subsidiary Level
and Advanced Level

9707/2
MAY/JUNE SESSION 2002

BUSINESS STUDIES
PAPER 2 Data Response

1 hour 30 minutes

Additional materials:
Answer paper

TIME 1 hour 30 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 businesses described in this paper are entirely fictitious.

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

This question paper consists of 3 printed pages and 1 blank page.



The Eating Shop

The Eating Shop is a chain of 25 restaurants located across three countries. It began when the owner, Kevin Foo, rented a property in his local town. Initially he used a *penetration price strategy*. The popularity of the menu, along with the low level of competition at the time, meant that he easily achieved his target revenue and profit figures in the first few years. This led to a swift increase in the number of restaurants, financed mainly by retained profit and borrowing. Kevin prefers to purchase property because it provides him with greater security and more control over the business. He thinks that much of his success has been based on his ability to take decisions quickly, which has meant that he has never discussed the long or short term plans of the business with any of his employees. This is an issue that causes considerable frustration to his restaurant managers. 5 10

He has been approached by a commercial property agent who wishes to sell Kevin a restaurant that has recently come onto the market. The purchase price of the restaurant is \$180,000, although decoration and investment in fixtures and fittings will add another \$20,000 to this. Initial market research has revealed that there are two competitors located nearby. Although he estimates sales will be slow to begin with, he is confident that customers will become loyal to the Eating Shop brand. *Net cash flows* for the first five years for the proposed restaurant are expected to be: 15

Time	Net cash flows
End of year 1	\$60,000
End of year 2	\$70,000
End of year 3	\$100,000
End of year 4	\$150,000
End of year 5	\$160,000

- (a) Define the following terms:
- (i) Penetration price strategy (lines 2–3) [3]
 - (ii) Net cash flow (line 16). [3]
- (b) Explain the possible disadvantages of the leadership style adopted by Kevin. [6]
- (c) For the proposed new restaurant:
- (i) Calculate the payback period. [2]
 - (ii) Calculate the average rate of return. [3]
 - (iii) Comment on your results. [3]
- (d) Discuss the relative advantages and disadvantages of businesses such as The Eating Shop continuing to grow in size. [10]

The Smart Tile Company

The Smart Tile Company employs a batch production system in order to manufacture its range of bathroom and kitchen tiles. Recently, sales and profit have fallen. This has meant the business has failed to meet its financial objective of a *return on capital* of 20%. The business is therefore considering ways of increasing sales. With this in mind, the marketing director, Sheila Lee, has suggested that the price of one of its main product ranges (known as tile X) should be reduced. She proposes to reduce the price by 12% to \$1.45 which she believes will lead to a volume increase from 8,000 to 10,000 tiles per month. The business currently sells only to high class retailers in the home market. It spends very little on advertising, preferring to rely on repeat orders from its regular customers. 5

The business is also facing a stock control problem because it did not anticipate the reduction in sales. The result has been a build-up of stock in the business, mainly raw materials and finished goods. This problem has led to the managing director looking at ways of improving efficiency. He accepts that using *lean production* might help improve matters. However, the employees are not used to major changes and might find it difficult to adapt. The managing director feels the business should simply focus on a much tighter control of stock. He has therefore asked the production manager to prepare a brief presentation on the relevant issues that might arise from lowering stock levels. 10 15

(a) Define the following terms:

(i) Return on capital (line 3) [3]

(ii) Lean production (line 13). [3]

(b) (i) Using the data in the case study, calculate the price elasticity of demand for tile X. [3]

(ii) The production capacity of tile X is 12,500 tiles per month. Calculate the expected level of capacity utilisation, following the reduction in price. [3]

(c) Analyse the possible impact on the business of lowering stock levels. [8]

(d) Assume the business decides to lower its prices for **all** its products. Evaluate **other** changes to the marketing mix that The Smart Tile Company might need to adopt. [10]

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