CAMBRIDGE
INTERNATIONAL EXAMINATIONS

JUNE 2002

GCE ADVANCED SUBSIDIARY AND ADVANCED LEVEL

MARK SCHEME

MAXIMUM MARK : 60

SYLLABUS/COMPONENT : 9707/2

BUSINESS STUDIES

UNIVERSITY of CAMBRIDGE
Local Examinations Syndicate

1. The Eating Shop

a) Define the following terms

(i) Penetration price strategy

[3]

Content: Price strategy of reducing price in order to achieve volume sales. Appropriate when objective is market share. It might lead to price being raised once brand loyalty is established.

Level 2: Good understanding of each definition	(2-3 marks)
Level 1: Partial understanding of each definition	(1 mark)

(ii) Net cash flow [3]

Content: difference between cash in and cash out, over a period of time. Used to help with forecasting overdraft requirements as well as establishing whether an investment is worthwhile.

Level 2: Good understanding of each definition	(2-3 marks)
Level 1: Partial understanding of each definition	(1 mark)

b) Explain the possible disadvantages of the leadership style adopted by Kevin.

[6]

Content:

- No delegation or sharing of responsibility for long term plans (short term is delegated by nature of business).
- Managers may become disheartened by lack of input to e.g. décor/menu (local tastes may differ).
- May result in higher labour turnover of managers which develops insecurity in subordinates with the consequent effect on levels of service.
- Kevin is overburdened, making expansion more difficult to achieve.
- Stifles possible initiative for change.

Knowledge and application	
Level 2: Explanation of disadvantages in context	(3-6 marks)
Level 1: States possible disadvantages.	(1-2 marks)

c) For the proposed new restaurant

(i) Calculate the payback period [2]

Content: investment = £200,000. EOY1 = £60,000, EOY2 = £70,000 (cumulative = £130,000. EOY3 = £100,000 (cumulative = £230,000). Therefore EOY3.

Or 2.7 years if assuming constant cash flows. Alternative = 2 years 8.4 months. 2 years 252 days. Error of 10 days either way. 2 years 8 months, 2 years 9months both (2)

(2 marks) for correct answer

(1 mark) for correct method, but incorrect execution.

(ii) Calculate the average rate of return [3]

EOY0	-£200,000	
EOY1	£60,000	
EOY2	£70,000	
EOY3	£100,000	
EOY4	£150,000	
EOY5	£160,000	
Ncf	£340,000	(1 mark)
Ncf per annum	£68,000	(1 mark)
ARoR	34%	(1 mark)

Possible alternative answers

Answer	Reason	Marks
No percentage		(max 2);
540/200	No deduction of I.I. no %	(1 mark);
270%	No deduction of I.I. no divide by 5.	(1 marks).
37.7%	Uses £180,000 as I.I.	(2 marks)
200%	Uses £180,000 as I.I. but doesn't divide by 5	(2 marks)
54%	No deduction of I.I.	(2 marks)
108/200	No deduction of I.I. No %	(1 mark)

(iii) Comment on your results [3]

Content:

Financial: payback half way through time horizon, but project may be much longer term (cash flows rising). Comments on AroR need to have comparator e.g. other projects. Cash flow forecasts not always reliable. Might need wider set of parameters before a decision is made. (1 per point made)

Level 2: For comments applied in context (2-3 marks) Level 1: Limited understanding of calculations (1 mark)

d) Discuss the relative advantages and disadvantages of the business continuing to grow in size.

[10]

Content:
Advantages: answers likely to be based on economies of scale

- Easier to launch new restaurants as size increases.
- Purchasing economies of scale due to centralised ordering.
- Easier to finance further expansion if good track record.
- Might allow greater opportunity for a range of different foods.
- Easier to attract employees, assuming company has a good name for its treatment of staff – Kevin's approach to leadership might hinder this.

Disadvantages:

- Difficult to control (given disparate geographical regions)
- Extra cost of distribution.
- Need for regional managers.
- Possible co-ordination and motivational diseconomies

Knowledge and Application	Analysis and Evaluation
Level Two: Shows understanding of the advantages and/or disadvantages with reference to the business (3-4 marks)	Level Two: Evaluates the advantages and/or disadvantages of the business growing in size, based on analysis (3-6 marks)
Level One: States the advantages and/or disadvantages of growing in size. (1-2 marks)	Level One: Analysis of advantages and/or disadvantages. (1-2 marks)

2. The Smart Tile Company

a) Define the following terms

(i) return on capital **[3]**

Content: The profit earned in relation to the investment in the business by its owners. Profit/capital (or a derivative of this). Represented as a percentage yield.

Level 2: Good understanding of each definition	(2-3 marks)
Level 1: Partial understanding of each definition	(1 mark)

(ii) lean production **[3]**

Content: The philosophy of operating a business that means increasing quality whilst cutting costs. Could involve just-in-time, quality programmes, cell production

Level 2: Good understanding of each definition	(2-3 marks)
Level 1: Partial understanding of each definition	(1 mark)

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

[3]

Content:

$$\frac{\text{percentage change in quantity demanded}}{\text{percentage change in price}}$$

= 25%/12% = 2.08

(2-3 marks): 2.08, or 2.1 earns 3 marks; partial execution i.e. formula, with numbers, but incorrect answer, or incorrect demand increase (e.g. 20%), but with correct execution. (2 marks) (1 mark): Formula stated or only increase in demand calculated (25%).

(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]

$$\text{Capacity utilisation} = \frac{\text{actual output}}{\text{Capacity output}}$$

= 10,000/12,500

= 80% (3 marks)

Level 2 (2-3): New volume used but incorrect answer (2).
Level 1 (1) Formula stated or figures inserted but no answer.

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

Content:

- Difficult to reduce work-in progress without faster kilns, but raw materials and finished goods must be targeted.
- Reduction in stock will lower holding costs, financial costs and opportunity costs. Cost savings due to less space required and less opportunity for damage/theft.
- Need to have closer links with retailers and distribution process to facilitate faster shipping.
- Need for close relationships with suppliers due to risk of stock-out.
- Traditional business may mean the new discipline required on stock control may be difficult to manage.

Knowledge and Application	Analysis
Level Two: Shows understanding of impact of stock reduction to the business. (2-3 marks)	Level Two: Good analysis of issue(s) relating to reduction in stock. (3-5 marks.)
Level One: states the impact of lowering stock (1 mark)	Level One: Limited analysis of issue(s) relating to reducing stock. (1-2 marks)

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]

Content

Financial objective - 20% ROCE, therefore reduction in price must be offset by extra volume sold. Answers need to show logical link between different changes to marketing mix, in order to increase volume.

- Place: might require wider distribution, or encouragement of present retailers to stock more (helped by price reductions). Reduction in price might persuade more retailers to stock the product, broadening the possible market exposure. Selling to retailers abroad presents another opportunity, although costs of marketing will increase.

- Promotion: sales promotion (into the pipeline) to encourage more retailers to take on the product. Obvious opportunity to advertise, although niche market, therefore needs careful targeting.

- Product: might change design, although STC probably does this regularly anyway.

Knowledge and Application	Analysis and Evaluation
Level Two: Demonstrates understanding of non-price elements of marketing mix in context of STC (2-3 marks)	Level Two: Evaluates the changes to the marketing mix, based on analysis. (4-7 marks).
Level One: States the other parts of the marketing mix. (1 mark)	Level One: Analysis of changes, in context of the price reduction. (1-3 marks)