GCE

Business Studies

Advanced GCE **2880**

Business Strategy

Mark Scheme for June 2010

OCR (Oxford Cambridge and RSA) is a leading UK awarding body, providing a wide range of qualifications to meet the needs of pupils of all ages and abilities. OCR qualifications include AS/A Levels, Diplomas, GCSEs, OCR Nationals, Functional Skills, Key Skills, Entry Level qualifications, NVQs and vocational qualifications in areas such as IT, business, languages, teaching/training, administration and secretarial skills.

It is also responsible for developing new specifications to meet national requirements and the needs of students and teachers. OCR is a not-for-profit organisation; any surplus made is invested back into the establishment to help towards the development of qualifications and support which keep pace with the changing needs of today's society.

This mark scheme is published as an aid to teachers and students, to indicate the requirements of the examination. It shows the basis on which marks were awarded by Examiners. It does not indicate the details of the discussions which took place at an Examiners' meeting before marking commenced.

All Examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

Mark schemes should be read in conjunction with the published question papers and the Report on the Examination.

OCR will not enter into any discussion or correspondence in connection with this mark scheme.

Any enquiries about publications should be addressed to:

OCR Publications
PO Box 5050
Annesley
NOTTINGHAM
NG15 0DL

Telephone: 0870 770 6622
Facsimile: 01223 552610
E-mail: publications@ocr.org.uk

1 Discuss the extent to which holding two franchises will impact upon MGL's ability to achieve its own objectives. [18]

Main agency cars – price and servicing set so cannot adjust price. Fuel, the same.
So, MGL can only really control the shop (3.7% of revenue), prices and margins on second hand cars and any non-main dealer servicing and ancillary work.

Can a business which cannot control up to 96.3% of its income be expected to be able to control its ability to achieve objectives?

Does franchise brand image actually contribute to sales – fuel is thought to be more because MGL sells a major brand – can this "thought" be measured or substantiated?
But MGL does have some control over many of its costs.

However, as a franchisee MGL will enjoy some degree of market power – for example, being a known brand may attract customers when buying that particular brand of car – so franchise has some positive effect, contributing to volumes. Similarly, franchisor may be able to offer MGL support in key areas; marketing, operations, finance and HR which could make them more efficient as a business than a truly independent operator. However, this support may well come at a cost, so it is swings and roundabouts.

What are MGL's objectives? It's a Ltd so assume profit. Owned by Irene and Albert, and we are told that Albert draws a salary from MGL. As such, his objectives may be less profit focused than his sister's. Also, Albert owns the site and so may simply want MGL to survive so that it can continue to pay him his rent and the interest on his director's loan. But, increasing thoughts about retirement so may be that objective is about maximising the value of the business as a going concern if it is to be sold. However, Irene's son is the Sales Director so the objective might simply to pass control of the business to him whilst the two shareholders sit back and enjoy a future stream of dividends.

Level 4	Discussion is evaluative in balancing different possibilities	**(18-13)**
Level 3	Case material is subject to analysis in considering the franchisors' influence on objectives	**(12-8)**
Level 2	Demonstrates understanding of how other stakeholders, eg franchisors, might affect a business' ability to met its objectives	**(7-4)**
Level 1	Demonstrates knowledge of objectives or franchising	**(3-1)**

2 Should MGL expand its product range by installing a high pressure car wash? Justify your answer. [19]

Installation will take between ten weeks and fourteen weeks, critical path is always BEF. How much disruption to regular operations might there be during this time? Need to allow for any loss of business during construction phase.

Cost of expansion is £25,000, availability of resources; MGL does not have the cash to pay for this expansion, hence the need for a bank loan. This similarly implies that Irene cannot/ will not invest any additional share capital. So, for Albert the issue is does he want to bear the risk which the bank is seeking to transfer to him as an individual rather than to the limited liability company (lifting the corporate veil)? Benefits of expansion have to exceed the cost of capital. What is the cost of finance that Albert would pass to MGL – the new venture has to produce enough extra gross income to exceed the additional interest expense in the P&L. Impact on MGL's gearing 15.9% would rise to 23.5%. Opportunity cost? What else could MGL do with £25,000 of capital expenditure? Downside risk – what if it does not work, how much of the capital cost would be recoverable? Is there a second hand market for automatic car washing machines – if so why does MGL not test the water and buy one first? Owner's attitude to risk?

Employees availability – automatic, so other than occasional maintenance there appears to be no training implication.

Space – they seem to have room "Unused part of the site".

Market, is it big enough, competition 5 miles away. How robust is Albert’s conviction that customers would use it (line 17) – is this hope or is it supported by MR?

Makes strategic sense in terms of "fit" with other products and the business' competencies. Candidates may seek to use Ansoff and discuss risk of diversification.

Would allow MGL to easily return cars "in for a service" nicely cleaned, so may attract more of this type of business.

A part of the business independent of franchisor interference?

Possible increase in sales of related goods if product range is expanded – eat a bag of crisps/read a newspaper etc whilst waiting in the car wash.

Level 4	Recommendation is reasoned explicitly in context	**(19-14)**
Level 3	Recommendation is supported by analysis of case material	**(13-9)**
Level 2	Recommendation supported by descriptive use of the data	**(8-5)**
Level 1	Offers an unsupported recommendation	**(4-1)**

3 How might an increase in interest rates affect the strategic direction of MGL? [19]

Interest rates increase push up costs in P&L account, but this is only 1.7% of expense so could argue very little impact.

MGL 15.9% geared, but loan is a director's loan and as such may not have a contractual interest payment.

Interest expense in P&L might simply be on any ad hoc overdraft.

However, if car wash is opened then debt rises and so interest expenses.

Cars are a consumer durable – YED? Interest rates rise results in household disposable incomes falling and so sales of cars may well fall. But MGL also sell 2nd hand cars, so may see a switch from new to these cars. Car sales are 17.6% of total sales so a significant slice of the business. Depends on what extent its customers need to borrow money to finance the purchase of a car. So, MGL may need to refocus their efforts on the parts of the business least affected, whether that is second hand car sales, servicing, MOTs etc.

Fuel, parts etc less likely to be income sensitive, so possibly little fall here. Also, MGF is described as being rural and so there may not be much available public transport so fuel sales to locals will remain buoyant. Workshops, MOTs etc relatively immune to changes in incomes, so little fall. Also, many driving costs are legal requirements, eg MOTs, tyres etc, so this aspect of the business may be relatively immune from changes in household incomes.

Impact on £, would expect that to rise, so fuel costs may come down because crude is sold in $ per barrel, so strong pound means import costs fall (SPICED) Similarly, car franchise is "an imported brand of car" so again if interest rates feed through to £ then MGL's products might become more price competitive against domestically sources competitors. If so, divert resources to selling more new cars and away from other activities.

Evaluation
- Size of change
- Speed of change
- Impact of different parts of the business.

Level 4	Discussion is evaluative in balancing different possibilities	**(19-14)**
Level 3	Case material is subject to analysis in considering the external influence on strategy	**(13-9)**
Level 2	Demonstrates understanding of how interest rates might affect a business' strategy	**(8-5)**
Level 1	Demonstrates knowledge of interest rates	**(4-1)**

4 Create, and justify, a strategy which could boost MGL's profitability. [20]

Profitability is ratio of profits to some input.

Currently
ROCE = 19.96% GPM = 8.59%
OpM=9.45% NPM=1.7%

Simply, either cut costs or increase income!
Where to focus attention?

Fuel is 72.4% of turnover. Cannot increase price (competition and franchise) so can only boost revenue by increasing volume. Increase in volumes this will boost total profit but not profitability on this product line. However, it will increase profitability of the whole business as the size of the gross profit rise faster than indirect costs, so boosting profits, and so in turn profitability. Contribution on fuel is 2.6%, not a lot of scope here.

Shop (don't get fooled by the "loss" which is due to the allocation of overheads). Contribution is 20%. Described as impulse items so might be able to raise prices – a 5% increase in price would lead to £5,750 increase in profits pa.

Car sales 13.8% contribution, most scope on second hand sales because of franchise agreement and trade-ins given to customers.

Workshop has a 56.4% contribution. Fit "unnecessary" parts – ethics?

Cut costs? Staff wages, but need to consider impact on moral, labour t/o, recruitment etc. Materials – impact on quality? And so local reputation for repairs.

Items in P&L account – any possible saving here? Eg legal fees Change of depreciation policy?
Might Albert give up the rent he changes the business and take his reward through additional share of boosted profits?

Offer new products/ service – eg use second hand cars for car hire?
Strategy has to be realistic regarding extent of the problem and the available resources (human, physical space, capital). Also need to consider the objective of the strategy, but how much is profitability to be boosted by?

Level 4	Achieves a coherent strategy having evaluated different sides	**(20-15)**
Level 3	Analysis of material supports creation of strategy	**(14-9)**
Level 2	Recommendation supported by the description of case material	**(8-4)**
Level 1	Offers an unsupported recommendation	**(3-1)**

Assessment Grid

Question:	AO1:	AO2:	AO3:	AO4:	Total:
Q1	3	4	5	6	18
Q2	4	4	5	6	19
Q3	4	4	5	6	19
Q4	3	5	6	6	20
Total	**14**	**17**	**21**	**24**	**76**
QWC					**4**
Paper Total					**80**

OCR (Oxford Cambridge and RSA Examinations)
1 Hills Road
Cambridge
CB1 2EU

OCR Customer Contact Centre

14 – 19 Qualifications (General)
Telephone: 01223 553998
Facsimile: 01223 552627
Email: general.qualifications@ocr.org.uk

www.ocr.org.uk

For staff training purposes and as part of our quality assurance programme your call may be recorded or monitored

Oxford Cambridge and RSA Examinations
is a Company Limited by Guarantee
Registered in England
Registered Office; 1 Hills Road, Cambridge, CB1 2EU
Registered Company Number: 3484466
OCR is an exempt Charity

OCR (Oxford Cambridge and RSA Examinations)
Head office
Telephone: 01223 552552
Facsimile: 01223 552553