Oxford Cambridge and RSA

Thursday 13 January 2022 – Morning

Level 3 Cambridge Technical in Business

05834/05835/05836/05837/05878 Unit 3: Business decisions

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INSTRUCTIONS

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INFORMATION

- This Insert contains the pre-release material that you have already seen.
- This document has **4** pages.

Fulmar Caravan Construction Limited

The business

Fulmar Caravan Construction Ltd (*FCC*) is a manufacturer of caravans. The caravans which *FCC* makes are known as 'tourer caravans'. Tourer caravans provide a small mobile home for tourists. They are designed to be towed behind the owner's car to each of their selected caravan sites or holiday locations. Tourer caravans are necessarily compact; but all contain, as a minimum, a seating area, kitchen, bathroom and sleeping area.

The business was founded in 1983 by Jack Jones. The business now operates from purpose-built facilities on the south coast of England. The company manufactures approximately 300 caravans a year. It currently employs 85 staff. Anika, Jack's daughter, took over the running of the business in 2020 when her father retired suddenly due to ill health. Anika, who has a degree in Marketing and Finance, holds 38% of the company's shares. There are currently five other shareholders: four members of the Jones family who each hold an 8% share and Tom Jensen, *FCC*'s Production Director, who having worked alongside Jack when he founded the business, holds a 30% share.

The market

The market for tourer caravans in the UK is very competitive. The largest manufacturer has a market share of approximately 20%. In addition, there are several other manufacturers each with a market share greater than 10%. *FCC*'s market share has shrunk in recent years from a peak of 3% in 2015 to just 1% in 2021.

The problem

FCC is in decline. Its sales revenue has fallen over the last ten years, as has its ability to generate a profit. In 2021 its sales revenue of £4.5 million only generated a gross profit of £500 000 and a net profit of £150 000. Furthermore, the company's net worth on 31 December 2021 was approximately £6 million, down from nearly £9 million in 2017. Even its relatively substantial cash reserves have declined considerably since 2018; currently it has approximately £700 000 in reserve.

Anika has recently commissioned some market research. The results are not encouraging. According to the research, most potential caravan buyers feel that *FCC*'s caravans look and feel outdated. *FCC* has a reputation for being a very traditional caravanning business that produces low-specification caravans. The company has failed to move with the times; its website is very basic and its social media channels are inactive. *FCC* is disliked by younger caravanners and is especially unpopular with young families. Older caravan buyers, who do not always want the latest gadgets and prefer to stick with products they know, rate the company more highly. The market research suggests that there is potential to persuade more of these older caravanners to buy from *FCC*. Unfortunately for *FCC*, this particular market is small and, also, in decline.

In an attempt to turn round *FCC*'s disappointing sales and profit performance, Anika has identified three potential options worthy of consideration. The company cannot afford to implement more than one of them. The chosen option needs to be a success; if it fails then the business is also likely to fail. Should this happen, Anika believes that the business may need to be liquidated, for example by being sold to a competitor.

Anika is not expecting any major disagreements from family shareholders. They are not involved in the day-to-day management of the business and tend to go along with her or Tom's recommendations. However, Anika does have concerns that Tom does not always agree with her. Anika believes that this is partly because she has a background in marketing and finance, rather than production. Tom has told her on more than one occasion that he feels that she does not understand how a manufacturing business works, let alone a manufacturer of caravans. Anika is relatively new to the business. In contrast, Tom has worked his way up the company over many years, since he first started working for Jack as a production supervisor. Consequently, Tom feels that he is the only remaining link to Jack's vision for the company.

Option 1 – Marketing campaign

Anika would create a major publicity campaign for *FCC*. The campaign would include advertising in specialist caravan magazines, retirement magazines and TV channels aimed at caravan owners; as well as increasing the company's attendance at specialist trade fairs. It would also include sponsorship of a local lower-league football team. *FCC*'s social media channels would also be relaunched and updated more frequently. The capital cost for this option is estimated to be £600 000. In addition, this option would increase ongoing revenue expenditure by approximately £50 000 a year.

The capital cost of this option would be funded entirely from cash reserves. Capital investment appraisal for this option suggests a payback period of three years and three months, with an ARR of 4.67% over the first five years.

Option 2 – Update the product range

Tom has estimated that it would take six months to update the existing product range. This option would require the appointment of new staff. Some of these new staff would need to be skilled caravan designers. The remainder would need to be suitably skilled production workers able to build the new range of caravans. The capital cost for this option is estimated to be £1.2 million. In addition, this option would increase ongoing revenue expenditure by approximately £120 000 a year.

The capital cost of this option would be financed by using £600 000 from the cash reserves plus an equity injection from a venture capitalist for a 20% stake in the business. Capital investment appraisal for this option suggests a payback period of four years and one month, with an ARR of 6% over the first five years.

Option 3 – Export to Eastern Europe

Anika is aware that some countries in Eastern Europe are currently seeing a large increase in caravan sales. Anika believes that with the right distribution channels this could be a lucrative market, especially as customers in Eastern Europe are less likely to be able to afford the high-specification caravans that most customers in the UK prefer. However, incomes in some countries in Eastern Europe are rising rapidly. Anika also knows that other caravan manufacturers have plans to increase their promotional activity in Eastern Europe. Tom has identified actions that *FCC* would need to take. These include adapting the caravan models for the overseas market (e.g. meeting electrical and safety requirements), setting up new transport routes, finding local agents and recruiting staff who are specialists in working with Eastern Europe. The capital cost for this option is estimated to be £800 000. In addition, this option would increase ongoing revenue expenditure by approximately £80 000 a year.

The capital cost of this option would be financed by using £600 000 from the cash reserves plus an equity injection from a venture capitalist for a 15% stake in the business. Capital investment appraisal for this option suggests a payback period of exactly four years.

Appendix 1: Caravanning is the trend throughout Europe

Caravanning holidays remain one of the most popular pastimes of Europeans. The European caravanning industry registered sales growth amounting to more than 4% in 2019. The more than 210 000 new caravans sold over the course of the year represent the second-best result in the industry's history. Sales in almost all national markets were up as well, and further sales growth is expected for the coming year.

Appendix 2: UK caravan sales, 2010 – 2017