



**BUSINESS AND ORGANISATION
HIGHER LEVEL
PAPER 1**

Tuesday 22 May 2001 (afternoon)

2 hours 15 minutes

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.
- Read the case study carefully and then answer all the questions.

CASE STUDY

MEMENTO

In 1983, Monesh Goswami and Najat Minishi set up in partnership wholesaling women's clothing. Over the years the business became more specialist as they moved into supplying patterned silks, ribbons, buttons and cake decorations. Their products were widely used to make wedding and formal outfits and to provide decorations for celebration cakes. Their silks were produced specifically for them and the craftsmanship was superb allowing premium pricing. The business grew and in 1992, they formed a private limited company called 'Memento', with Monesh and Najat the sole shareholders and directors. They decided to run their business through mail order. They sold their small warehouse and moved into an extension built on to Najat's house. As the stock was not particularly bulky it was kept in boxes in the garage. For the next two years the business continued to trade successfully and stock turnover was high. The sole advertising method was in a telephone business directory. 90% of sales was repeat business to three major clients. Monesh and Najat paid themselves the same salary for 1999 and 2000. When combined the salaries were equivalent to 35% of the sales revenue of the business in 1999. Dividends were good and both bought expensive cars. They hired an assistant Jill Mbiti, who worked three days a week typing letters and price lists and mailing these to existing and previous customers. She also answered phone calls and undertook general clerical work such as filing.

The profitability of Memento's niche segments began to attract competitors and in 1998, an American multinational company, 'Craftshops', set up in the locality supplying amongst other items, ribbons, buttons and decorations. The ranges offered were less extensive than Memento's and of poorer quality, but sold at considerably lower prices. One of Memento's major customers stopped ordering from them and sales to the other two major customers began to decline. Monesh and Najat saw sales revenue and profits decrease worryingly and in 2001 they were faced with the possibility of making a loss.

Monesh's brother, Sanjay, was a successful financial consultant. Monesh and Najat appointed Sanjay as their financial advisor. Sanjay asked Monesh and Najat to complete a questionnaire about their business. Sanjay talked to customers and to Jill, and examined the records of the business. He then met with Monesh and Najat. He presented the following facts about the business (see Table I).

Table I Sanjay's Presentation - Facts about the business

1. Stock (inventory) levels – at a record high. Sanjay believed that as much as 20% of the stock was now obsolete or impossible to sell at full price. There were so many boxes that some had been placed in bedrooms.
2. Mailing list – out of date. 40% of customers on the list had not purchased an item for 4 years.
3. Database – none except for a written journal. Receipts and past records kept in boxes. Jill didn't like using computers.
4. Mark-up on materials – 200% on the cost to the business.
5. Overheads – salaries, wages, postage and telephone bills were not recorded properly or allocated.
6. Orders – small orders treated the same as large orders: discounts not offered and postal charges the same irrespective of size and weight of the package.
7. Debts – several large debts owing; one client owing \$4000 had stopped trading.
8. Lines – silk business profitable; buttons, ribbons and cake decorations running at a loss.
9. Comments from Jill Mbiti – Monesh and Najat spending less time together in the office, they argue about their financial situation. Monesh and Najat do not return telephone calls to customers. Jill has to spend more time dealing with customer questions and complaints.

New supplies of stock still being ordered and several suppliers were seeking payment for overdue invoices.

Table II - Financial Highlights (for year ending 31st December)

	1999	2000
	<i>\$000</i>	<i>\$000</i>
<i>Sales Revenue</i>		
Silks	288	240
Buttons and decorations	144	84
Ribbons	168	96
<i>Purchase Costs</i>		
Silks	96	80
Buttons and decorations	48	28
Ribbons	56	32
<i>Overheads</i>		
(excluding Director salaries)	40	40
<i>Dividends</i>	80	15
<i>Taxation and interest payments</i>	50	10
<u>Key Ratios</u>		
Current Ratio	1.4	2.7
Acid Test Ratio	0.96	0.5
Stock Turnover	18	8
Return on Capital Employed	16%	5%
Debtors' days	60 days	95 days
Creditors' days	55 days	65 days

Table III - Customer Research on Memento:

	Very good	Good	Satisfactory	Poor	Very Poor
1. Quality of products	79	12	7	2	0
2. Standard of Service	2	18	30	40	10
3. Range of products available	88	7	5	0	0
4. Value for money	12	36	19	29	4
5. Competitive prices	3	12	24	44	17

1. (a) Calculate the salaries of Monesh and Najat (the directors) for 1999 and express this as a percentage of sales revenue for 2000. *[3 marks]*

(b) (i) Prepare profit and loss accounts for both 1999 and 2000. *[6 marks]*

(ii) State the amount of profit retained in the business after taxation, interest and dividends had been paid in both 1999 and 2000. *[1 mark]*

 2. Explain **three** reasons for Monesh and Najat's decision to turn their partnership into a private limited company. *[3 marks]*

 3. (a) Analyse why Craftshops are able to offer ribbons, buttons and cake decorations at lower prices than Memento. *[4 marks]*

(b) Assess the competitive advantages that small firms like Memento have over larger organisations. *[3 marks]*

 4. Refer to the key ratios in Table II. Analyse the performance and liquidity of Memento and comment on its present financial position. *[4 marks]*

 5. Prepare a report from Sanjay, the financial consultant, to Monesh and Najat identifying major strengths and weaknesses of Memento. The report must be in a suitable format for a business document. Present justified and prioritised recommendations for action in the following areas:
 - administration
 - stock control and product range
 - finance and pricing
 - marketing.*[12 marks]*

 6. Identify **four** sources of secondary data that Sanjay could use to support his action plan and analysis of Memento's market. Explain how Sanjay could use this information. *[4 marks]*
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