



88045014

**BUSINESS AND MANAGEMENT
STANDARD LEVEL
PAPER 2**

Wednesday 3 November 2004 (morning)

1 hour 30 minutes

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.
- Answer three questions.

1. Superscent launches new product

Superscent, the world’s leading luxury cosmetics company, has announced that it intends to launch Bcool. The new fragrance will target the 15-25 year old market and will emphasize individuality, fun and internationalism. At the same time Bcool will build on *Superscent’s* current market position; namely the highest quality products, sold through exclusive outlets and targeted at customers with a high disposable income and an “extravagant” lifestyle. Bcool will benefit from *Superscent’s* strong cash flow position and industry analysts believe more than \$100m will be spent to establish the product as a suitable addition to the *Superscent* range.

Superscent has decided to promote Bcool with a variety of advertisements featuring sports and pop music celebrities from a diverse range of cultural backgrounds. It intends to sell Bcool through its existing network of retail outlets at a price 10-15 % higher than its closest rivals, but the Bcool range will be priced lower than the *Superscent* range.

- (a) Explain what is meant by the phrase *strong cash flow position*. [2 marks]
- (b) Explain **two** potential advantages for Bcool of aiming their product at a specific group such as “the 15-25 year old market”. [4 marks]
- (c) Analyse **three** factors that could allow Bcool to set its prices “10-15 % higher than its closest rivals”. [6 marks]
- (d) Discuss the potential advantages **and** disadvantages of selling “Bcool through its (*Superscent’s*) existing network of retail outlets”. [8 marks]

2. WMB and globalization

WMB is an established car manufacturer in a wealthy developed country. In recent years *WMB* has faced intense competition from car manufacturers that have focused on producing a range of cars for the global economy to reap the benefits of economies of scale. Whilst domestic car sales have been stable, *WMB*'s share of the global market has shown evidence of decline in recent years.

Kosuke Ozumi has recently been appointed as the chief executive of *WMB*. He plans to introduce a number of financial incentives to improve motivation at *WMB* since Kosuke believes that the individual should be rewarded if he or she produces good results.

Industry commentators have not been impressed by Kosuke's plans. They believe that *WMB* needs to both subcontract* more of its activities and investigate ways to reduce its excessive stock levels which have resulted in the organization having too much money tied up in working capital.

* Subcontract: this means that they will use other companies to carry out their activities.

- (a) (i) What is meant by globalization? [2 marks]
- (ii) Explain **three** factors that have contributed to globalization in recent years. [6 marks]
- (b) Analyse the potential problems for *WMB* if they use “financial incentives to improve motivation”. [6 marks]
- (c) Identify **three** stakeholders with an interest in *WMB* and explain why conflict between them is likely. [6 marks]

3. YNOS

YNOS is the world’s leading supplier in the growing and increasingly competitive electronic consumer goods market. Its product range includes audio visual products and electronic games and toys. In recent years *YNOS* has been losing market share and profits to close rivals in developing countries where labour costs are much lower and other costs are relatively low because government regulation of business is minimal. *YNOS* has also suffered because the local currency, (the Euro) has risen significantly against the US dollar and other major currencies in recent years. Nearly half of *YNOS*’ products are currently exported to the US.

Recent economic data

	Interest rate	Inflation rate	Exchange rate (Euro versus US dollar)
This month	7.25 %	4.9 %	1 Euro = US 1.8
6 months ago	6.25 %	4.3 %	1 Euro = US 1.7
1 year ago	6.0 %	3.8 %	1 Euro = US 1.6
2 years ago	5.0 %	2.0 %	1 Euro = US 1.5

In order to address these external challenges the board of directors at *YNOS* is considering the relocation of most of its production to a developing country where production costs are much lower and the exchange rate is pegged to the US\$. The relocation would mean the closure of several of its domestic factories and the loss of 20 000 jobs in areas of high unemployment. The board of directors also hopes to devise strategies to reduce the current level of gearing which is high and considerably above the average for the electronics industry. They are also hoping that the relocation will enable them to increase the dividend offered to shareholders.

- (a) *YNOS* is described as “the world’s leading supplier”. State **two** ways in which the size of a market may be measured. [2 marks]
- (b) Evaluate to what extent the information given in the case study suggests that the position of *YNOS* as the market leader may be threatened? [6 marks]
- (c) Explain **two** ethical issues that may be associated with the proposed relocation of *YNOS*. [4 marks]
- (d) Assess **three** strategies that *YNOS* could implement to address the threats it faces to its position as the world’s leading supplier. [8 marks]

4. The Colourful Hat Company

The *Colourful Hat Company* sells fashionable hats throughout the European Union. The hats are available in a range of colours and all contain the prestigious *Colourful Hat Company* logo.

The hats are sold to retailers for \$15 each. They cost \$5 per hat to manufacture and the salesperson receives \$0.60 commission for each item sold to retailers. The distribution cost for each hat is \$0.40. The fixed costs of production are \$10 000 per month.

The company would like to expand production and has drafted plans to invest in new machinery costing \$900 000.

Details of the investment are given in the table below:

	Cash in	Cash out
Now		900 000
Year 1	+360 000	
Year 2	+360 000	
Year 3	+360 000	
Year 4	+360 000	

The director of finance believes that the new machinery will reduce variable costs and thus maximize the contribution per hat. He is, however, concerned that increased competition may cause cash flow difficulties since retailers are able to demand longer credit terms. He is also considering whether he should accept a new order from a retailer offering \$17 a hat.

- (a) From the data given above calculate the break-even quantity. (*Show your working.*) [3 marks]
- (b) Explain **two** advantages and **two** disadvantages of using the payback method of investment appraisal. [4 marks]
- (c) (i) Calculate the payback period from the data given in the table above. (*Show your working.*) [3 marks]
(ii) Explain **two** non-financial factors that the *Colourful Hat Company* should consider before proceeding with the investment. [4 marks]
- (d) Assess to what extent break-even analysis could help to determine whether the director of finance should accept the new order. [6 marks]

5. Clare Clothes plc

Clare Clothes plc was set up thirty years ago as a relatively small business whose key objective was growth. The company grew steadily and is now a public limited company established as the market leader for children’s clothes.

Latest annual accounts of *Clare Clothes plc*:

**Balance sheet
(as at 31 December 2002)**

<i>Clare Clothes plc</i>		
	<i>2002</i>	<i>2001</i>
	<i>\$m</i>	<i>\$m</i>
Fixed assets	335	285
Stock	130	120
Debtors	200	220
Cash	10	20
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Creditors	130	100
Overdraft	40	0
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Assets employed	505	545
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Share capital	350	350
Reserves	155	195
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Capital employed	505	545

- (a) Explain the term a *public limited company*. *[2 marks]*
- (b) (i) Identify **three** objectives of *Clare Clothes plc* other than growth. *[3 marks]*
- (ii) Examine strategies and tactics *Clare Clothes plc* could have used to achieve their key objective of growth. *[7 marks]*
- (c) (i) Calculate the level of working capital of *Clare Clothes plc* for 2001 and 2002. *[2 marks]*
- (ii) Discuss how the changes in working capital identified in (c)(i) will affect *Clare Clothes plc*. *[6 marks]*