General Certificate of Education
Advanced Level Examination
June 2015

# Business Studies BUSS3

## Unit 3 Strategies for Success

Wednesday 10 June 2015 9.00 am to 10.45 am

**For this paper you must have:**
- an AQA 12-page answer book
- a calculator.

**Time allowed**
- 1 hour 45 minutes

A

**Instructions**
- Use black ink or black ball-point pen.
- Write the information required on the front of your answer book. The **Paper Reference** is BUSS3.
- Answer **all** questions.
- Do all rough work in your answer book. Cross through any work you do not want to be marked.

**Information**
- The marks for questions are shown in brackets.
- The maximum mark for this paper is 80.
- You will be marked on your ability to:
  – use good English
  – organise information clearly
  – use specialist vocabulary where appropriate.

**Formulae for Financial Ratios**

| Financial ratio | Formula |
|---|---|
| **Current ratio** | current assets : current liabilities |
| **Acid test ratio** | liquid assets : current liabilities<br>Where liquid assets are current assets – inventories (stock). |
| **Return on capital employed % (ROCE)** | $\frac{\text{operating profit}}{\text{total equity + non-current liabilities**}} \times 100$<br>** Where this equals capital employed. |
| **Asset turnover** | $\frac{\text{revenue}}{\text{net assets}}$ |
| **Inventory (stock) turnover** | $\frac{\text{cost of sales}}{\text{average inventories (stock) held}}$ |
| **Payables (Creditors) days**<br><br>**(Payables'* collection period)** | $\frac{\text{payables*}}{\text{cost of sales}} \times 365$<br>* Payables = creditors throughout this formula. |
| **Receivables (Debtors) days**<br><br>**(Receivables'* collection period)** | $\frac{\text{receivables*}}{\text{revenue}} \times 365$<br>* Receivables = debtors throughout this formula. |
| **Gearing** | $\frac{\text{non-current liabilities}}{\text{total equity + non-current liabilities**}} \times 100$<br>** Where this equals capital employed. |
| **Dividend per share (in pence)** | $\frac{\text{total dividends}}{\text{number of issued ordinary shares}}$ |
| **Dividend yield (%)** | $\frac{\text{ordinary share dividend (in pence)}}{\text{current market price (in pence)}} \times 100$ |

Read the **case study** and then answer the questions that follow.

## Chocolatier plc

### Introduction

Chocolatier plc is a manufacturer and retailer of luxury chocolates. Its product range includes chocolate bars, boxes of chocolates, and seasonal items such as Easter eggs. Chocolatier's products are popular with its predominantly wealthy customers and, in recent years, the company has achieved a steady growth in sales. Chocolatier's products are sold through its 15 prestigious city centre stores.

Chocolatier's Chief Executive, Kate Smith, has ambitious expansion plans for the business. Her aim is for Chocolatier to become one of the market leaders in the UK luxury chocolate market. To achieve this, Kate has established the objective of increasing its market share of the luxury chocolate market significantly.

### The current position

Secondary market research of the luxury chocolate market revealed that:

- supermarkets account for over 60% of luxury chocolate sales
- the market value of the luxury chocolate market is expected to increase by 33% between 2014 and 2018
- demand for luxury chocolate has increased due to the popularity of TV programmes such as 'Masterchef'.

Focus groups of Chocolatier's customers confirmed that consumers:

- liked the 'exclusive' image and high quality of the Chocolatier brand
- appreciated the high levels of customer service.

Chocolatier's products are made at its factory in York. Its location enables quick distribution to the company's stores. Production is labour intensive and the employees are highly skilled. Chocolatier uses a 'soft' human resource strategy. Its employees are well paid and are given a share of the profits. There is extensive use of delegation and empowerment. However, Kate is not satisfied with the factory's current operational efficiency.

The company has a decentralised organisational structure. For example, each store manager has the authority to decide which products to sell based on the local needs of the customers. Significant bonus payments are paid to the best performing store managers. Chocolatier is viewed as a good employer by its employees.

**Turn over ▶**

**Kate's Proposal**

Kate considers that Chocolatier should achieve its objective by selling its products in UK supermarkets rather than by increasing the number of its city centre stores.

She has instructed her Marketing Director to devise a marketing plan that will achieve the objective of increasing Chocolatier's market share to 15% by 2018. The plan will involve the endorsement of a celebrity chef who would be the focus of an extensive marketing campaign. Initial contacts with supermarkets have been positive. They have agreed to place significant orders as long as Chocolatier is able to meet their strict quality and delivery targets. The supermarkets have stressed that Chocolatier needs to be able to deliver their first orders in 15 months' time, to coincide with the crucial pre-Christmas season.

The supermarket orders would require Chocolatier to double its existing production capacity. The York factory is currently producing 35 million units and has only limited spare capacity. The supermarkets are demanding large price discounts. Therefore, in order to maintain its profitability, Chocolatier will need to improve its operational efficiency. Kate proposes to switch to a new purpose-built production facility in Poland which will employ more capital intensive production methods. The existing factory in York will be closed.

Based on her network diagram (**Appendix C**, **Figure 1**), Kate is convinced that the factory in Poland will be operational in 15 months' time. However, the Operations Director has raised concerns, especially as Chocolatier is considering moving its entire operational facilities overseas as well as implementing a totally different production method. One of his team estimates that Kate's figures are too optimistic. The team member believes that there is a 40% probability that it will take at least 3 months to obtain a site for the factory and 4 months to train the new staff.

Kate estimates that the cost of the marketing plan and the new factory will be £500m. The Finance Director believes that the sale of the York factory will raise only £100m and is worried about the consequences of borrowing the additional £400m. Furthermore, she has advised Kate that Chocolatier's investors would expect her proposal to achieve a net present value of at least £40m and payback within 3 years.

Kate's proposal to focus on selling to UK supermarkets and to close the York factory has generated much debate amongst her fellow directors. The Human Resource Director has raised concerns regarding the reaction of the workforce and the cost of the inevitable redundancies. The Marketing Director believes that Kate's proposal will upset Chocolatier's existing customers and is worried how its larger rivals, who currently dominate the UK supermarket sector, will respond. He proposes that Chocolatier should continue with the existing strategy which is generating good profits. His view is that they should continue as they are and gradually open more of their own stores instead.

Next week, Kate will hold a meeting with her fellow directors to discuss whether or not her proposal should be accepted.

## STATISTICAL APPENDICES

### Appendix A: Marketing data

**Table 1: Market shares in the UK luxury chocolate confectionery market 2014**

| Company | Market share |
|---|---|
| Kraft Foods | 30% |
| Thorntons | 20% |
| Nestlé | 15% |
| Chocolatier | 5% |
| Others | 30% |

### Appendix B: Chocolatier plc – Financial data

**Table 1: Selected financial information for year ending 31 March 2015**

| | 2015 £m |
|---|---|
| Current assets | 60 |
| Current liabilities | 61 |
| Non-current liabilities | 120 |
| Total equity | 250 |
| Operating profit (year ending 31 March) | 50.5 |

**Table 2: Selected financial information for year ending 31 March 2014**

| | |
|---|---|
| Operating profit | £30m |
| ROCE | 10% |
| Current ratio | 1.5:1 |
| Gearing | 74.9% |

**Table 3: Investment appraisal data for Kate's proposal**

Initial cost £500m

| Year | Cash inflow £m | Cash outflow £m |
|---|---|---|
| **1** | 175 | 30.0 |
| **2** | 260 | 42.5 |
| **3** | 315 | 50.0 |

5% Discount factors: Year 1 0.95; Year 2 0.90; Year 3 0.86

**Turn over ▶**

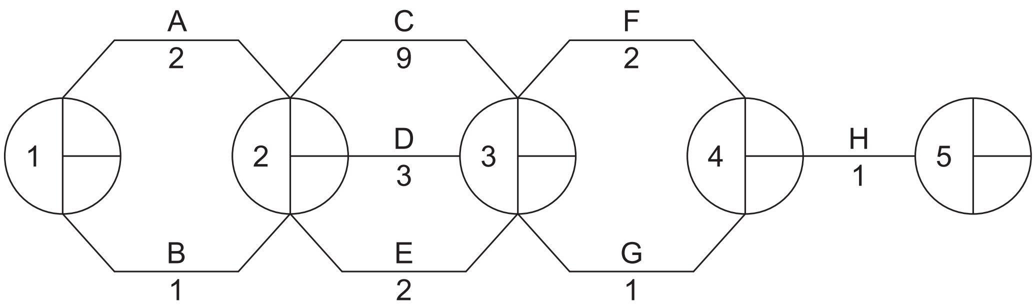
## Appendix C: Operations data

**Table 1: Comparative current (2015) data for the York factory and forecast data for the Poland factory**

| | York | Poland |
|---|---|---|
| Capacity (millions of units) | 40 | 200 |
| Fixed costs per year (£m) | 2 | 5 |
| Variable costs per unit (£) | 0.5 | 0.25 |
| Selling price per unit (£) | 2 | 1.75* |
| Number of factory workers | 300 | 100 |
| % defective products | 2 | 5 |
| Average delivery time to stores | 1 day | 3 days |

* price charged to the supermarkets

**Figure 1 Partially completed network diagram for the proposed Poland factory**




Duration for each activity is in months.

| | | | |
|---|---|---|---|
| Task A | Obtain factory site | Task E | Recruit staff |
| Task B | Obtain planning permission | Task F | Install equipment |
| Task C | Build factory | Task G | Train staff |
| Task D | Obtain equipment | Task H | Test production |

Data provided by Kate Smith

**Figure 2: Human resource data for the York factory for 2014**

| | Chocolatier | Industry average |
|---|---|---|
| Labour turnover | 5% | 10% |
| Labour productivity (units per worker per week) | 2250 | 2500 |
| Average weekly wage | £500 | £350 |
| % of workforce that belong to an employee group | 80% | 60% |
| Average number of days lost due to sickness per employee per year | 5 | 10 |
| Temporary staff as a proportion of total staff | 5% | 25% |

**Question 1**

**0 1** The Finance Director has advised Kate that Chocolatier's investors would expect her proposal to achieve a net present value of at least £40m and payback within 3 years.

Using the data in **Appendix B**, **Table 3**, calculate the net present value and payback for Kate's proposal. State whether it meets the expectations of Chocolatier's investors.

**[10 marks]**

**Question 2**

**0 2** Do you think that Chocolatier was right to adopt a 'soft' human resource strategy at its York factory? Justify your view.

**[18 marks]**

**Question 3**

**0 3** The Operations Director is concerned about whether the factory in Poland will be operational in 15 months' time. Do you think that he is right to be concerned?

You should use numerical evidence to support your answer.

**[18 marks]**

**Question 4**

**0 4** Using all the information available to you, complete the following tasks:

- analyse the key arguments **for** and **against** Kate's proposal
- make a justified recommendation on whether Kate's proposal should be accepted.

**[34 marks]**

**END OF QUESTIONS**

**There are no questions printed on this page**