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N18/3/BUSMT/SP2/ENG/TZ0/XX

Piper Industrial (PI)

a. Define the term capital expenditure [2 marks]

Capital expenditure refers to the purchase by a business of long-term assets (assets that have a useful life longer than one year).

b. i. Using Table 1, calculate for PI: Gross profit (X) [1 mark]

Gross profit is \$10,000,000

ii. Using Table 1, calculate for PI: Tax (Y) [1 mark]

Tax is \$860,000

c. Using Table 1 and your calculations in (b)(i) and (ii), construct a profit and loss account for PI [2 marks]

All figures in 000s

Sales revenue	25,000
---------------	--------

COGS	15,000
Gross profit	10,000
Expenses	4,700
Net profit before interest and tax	5,300
Interest	1,000
Tax	860
Net profit after interest and tax	3,440

d. Using Table 2, calculate the net cash flow (Z) for PI for 2019 (show all your working) [2 marks]

Net cash flow is \$1,500,000 calculated as follows

$$\$24,000,000 \text{ total receipts} - \$22,500,000 \text{ total payments} = \$1,500,000 \text{ net cash flow}$$

e. Explain the difference between profit and cash flow. [2 marks]

Profit is typically calculated on an accrual basis (when revenue or expense actually accrues to the business) but does not reflect the actual movement of funds. Cash flow reflects the actual movement of funds – when a business receives payment and makes a payment. Thus, a timing difference can exist between the accrual of a revenue or an expense and the actual receipt of funds.

Patras Furniture (PF)

a. Define the term batch production [2 marks]

Batch production involves making a group of identical items together, and each stage of operation is performed on the whole group before it moves on to the next stage.

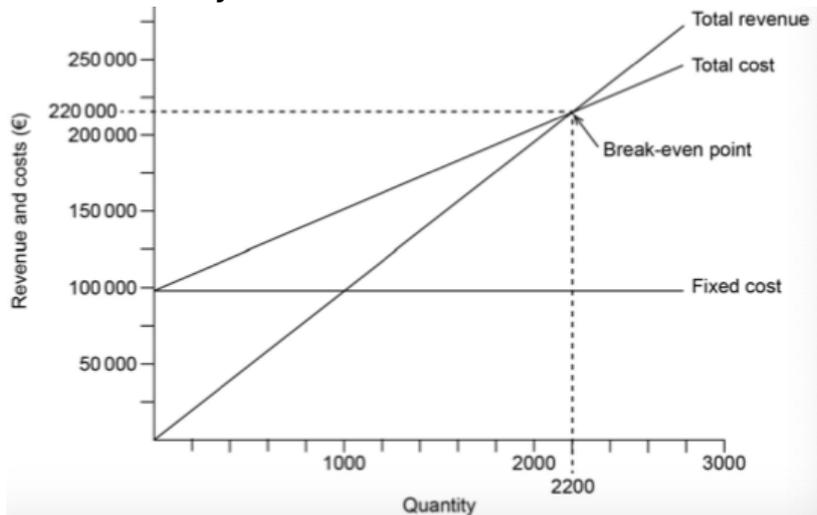
b. i. Calculate the break-even level of output for PF for 2009 [2 marks]

$$\text{Fixed costs: } \text{€}24,000 + \text{€}6,000 + \text{€}11,000 + \text{€}40,000 + \text{€}18,000 = \text{€}99,000$$

$$\text{Contribution: } \text{€}100 - \text{€}50 - \text{€}5 = \text{€}45$$

$$\text{€}99,000 / \text{€}45 = 2200 \text{ chairs}$$

ii. Construct a fully labelled break-even chart, to scale, for PF for 2019 [4 marks]



iii. Calculate the forecasted profit if PF sells 2400 chairs in 2019 [2 marks]

$$(2400 - 2200) * 45 = 9000$$

Jacob Strutz (JS)

a. Define the term multinational company (MNC) [2 marks]

A multinational corporation is a company that operates in two or more countries. A multinational company needs to have a base in those countries, not just sell goods and services there.

b. i. Explain the importance to JS of brand value [2 marks]

Brand value refers to the premium customers or potential customers are willing to pay for a product compared to the competition. For example, if jeans roughly comparable to Jacob Strutz's products sell for \$10 less, some dollar amount can be specifically attached to the value of the JS brand.

ii. Explain the importance to JS of brand loyalty [2 marks]

Brand loyalty refers to the loyalty that customers attach to a particular brand, whether for repeat purchases of the same product (jeans) or the purchase of new products traded under the brand name (jeans jackets, for example). In the case of JS, it has

strong brand loyalty based upon on 100 years of successful marketing. Many customers are loyal to JS even though they could buy other jeans for less or buy jeans that have a certain trendiness now.

c. i. Draw and label a product life cycle for Strutz's No. 5 Jeans [2 marks]



ii. Explain the position of Strutz's No. 5 Jeans on the product life cycle [2 marks]

JS's position is in the decline stage of the product life cycle. Despite strong brand loyalty, an ageing baby-boomer population is buying fewer jeans (thus, JS's sales are down) while, presumably, young people are buying cheaper jeans made outside the US or more "fashionable" jeans made by designers. Regardless, JS's sales are down considerably from their peak.

d. Discuss the role and impact of globalization on the growth and evolution of JS [10 marks]

The role and impact of globalization on JS has been considerable and includes:

- sales growth to \$7.6 billion dollars, which, the stimulus implies, was based upon sales around the world
- the opportunities for offshoring, which has led to the closure of all of JS's manufacturing facilities in the US and, presumably, allowed JS to cut costs and remain competitive
- foreign competition, which has proven significantly challenging for JS, whose sales have decline considerably
- the nature of JS's program of corporate social responsibility (CSR), which has a very globally fashionable "triple bottom line" focus, especially its Strutz's chemical-free jeans.

In each of these ways, Strutz has been influenced by globalization. Some have been very positive for JS (increased sales for many years and lower costs), and some have taken a toll on JS (foreign competition and pressure for more expensive programmes of CSR).

JS must continue to seek out opportunities and minimize threats from a changing world. Of importance for JS is either to find extension strategies that will makes its core products relevant again in the global market place or find new products to sell under its highly recognized and valued brand.

Dana's Handbags (DH)

a. Identify two features of a private limited company [2 marks]

Features of a private limited company include:

- shareholders have limited liability.
- ownership of shares is restricted to a small number of investors (varies from country to country but in general is a low number).
- information does not have to be shared publicly.
- it is less costly to manage shareholders because of lesser disclosure and other legal requirements.
- it is a separate legal entity distinct from the owners of its shares.

b. i. Calculate the net profit margins for DH for 2016 and 2017 [2 marks]

2016	2017
$\frac{1370}{28\,000} = 4.89\%$	$\frac{1300}{29\,000} = 4.48\%$
=====	=====

ii. Calculate the net current assets (working capital) for DH for 2016 and 2017 [2 marks]

In 000s of dollars:	
2016	2017
$5000 - 3000 = \$2000$	$5200 - 3500 = \$1700$
=====	=====

c. Explain one method of above-the-line promotion and one method of below-the-line promotion that DH could use to raise consumer awareness that it is a social responsible company. [4 marks]

Methods of above-the-line promotion that DH could use include:

- television advertising
- radio advertising

- advertising in newspapers, journals, magazines, or trade journals
- cinema advertising
- billboards.

Methods of below-the-line promotion that *DH* could use include:

- direct mailing
- exhibitions and trade fairs
- sponsorship
- public relations
- celebrity endorsement
- personal selling.

d. Discuss DH's decision to develop a policy of corporate social responsibility [10 marks]

DH's decision to develop a policy of corporate social responsibility (CSR) fits well with trends in business today, whereby many companies are doing so. Indeed, sometimes today stakeholder groups exert powerful pressure on companies to practice CSR. The pressure to follow triple-bottom line reporting is also influencing companies to act in a more socially responsible way (despite some criticism of CSR by certain economists).

DH has adopted several approaches that are popular today: giving profits, lending employees, and being more environmentally friendly. All these methods have garnered DH favourable media attention, though less clear is if DH's brand identity has benefited. Sales growth has not improved. The gross profit margin decreased from 50 % to 48.28 %, and the net profit margin declined from 4.89 % to 4.48 %. The costs of donating profits, lending employees and presumably higher-priced biodegradable materials took a toll on profits. The situation also negatively affected the balance sheet, which saw a deteriorated working capital position, falling from \$2 000 000 to \$1 700 000.

One of the commonly cited reasons for practicing CSR is that it is a form of enlightened self-interest: doing good for others will in the long run lead to greater profits. In the case of DH, perhaps that was its intention. Employee morale improved, which can lead to greater productivity and loyalty (labour turnover would probably decline). CSR would enhance DH's reputation, socially responsible consumers would find an additional reason to purchase DH products, and, over time, the company would make more profits than it otherwise would have.

Some shareholders, however, are not satisfied with the results so far. At the annual general meeting, they complained about unimproved sales growth and lower margins, which they directly linked to the CSR programme. Several shareholders suggested that DH develop consumer awareness that it is a socially responsible company. The favourable media attention in the first year was insufficient to make an impact on the revenue side. Were DH to take this approach, reshape its brand identity and raise consumer awareness, it would have to invest in a promotional and public relations campaign, which might be costly. Profits and margins might go down before they go up, and possibly even more shareholders will be dissatisfied.

Benno

a. Define the term innovation [2 marks]

Innovation is about putting a new idea or approach into action. It can be described as the process of translating an idea/invention into a service/good that creates value. Innovation can be achieved by improving existing goods, processes or services

b. Explain two roles of Benno's mission statement [4 marks]

The roles of a mission statement include:

communicating the purpose of the organization to stakeholders

informing decision making and strategy development

developing the measurable goals and objectives by which to gauge the success of the organization's strategy.

For *Benno*, the mission statement has provided a way for the business to differentiate itself from its competitors, especially at a time when competition in the healthy soft drinks market is intense.

The mission statement is also a way to attract new investors who may have empathy with the direction of Benno. This is an important role given the need for Benno to be committed to innovation and CSR

c. Explain one advantage and one disadvantage for Benno of using a focus group of loyal customers [4 marks]

Advantages of a focus group of loyal customers:

- Can obtain detailed information about your own customers about their feelings, perceptions and opinions.
- Are cheaper than performing individual interviews.
- Provide an opportunity to clarify any issues or problems.

Disadvantages of a focus group of loyal customers:

- They can be hard to control and manage.
- You are only getting the views of loyal customers – it tells you nothing about consumers who prefer rival brands and why they prefer them to your soft drink.
- The results are difficult to analyse, especially if the focus group provides qualitative feedback.
- Members may not reveal their own feelings but are swayed by the majority view.
- May not be representative of the target market as a whole.

Possible application:

For *Benno*, an advantage of using a regular focus group is that they will be aware of the company's products and mission. This will reduce the amount of statistical noise and save time in the discussions when looking at new product ideas, such the biodegradable rings.

However, having a regular group for *Benno* increases bias and reduces objectivity of the data researched. It might be a useful exercise for *Benno* to ask customers who are not overly familiar with their products to achieve a more balanced qualitative view.

d. Recommend whether Benno should replace its plastic drink rings with the new biodegradable drink rings [10 marks]

For:

- It fits in well with its mission statement "to produce healthy drinks without damaging the environment" and this may be important in maintaining customer loyalty.
- It fits into its belief in corporate social responsibility, as the current drink rings damage the environment and harm creatures in the seas, such fish.
- Competition in this drinks market is very intense – this could act as a strengthening of its USP for *Benno* and retain loyal customers and attract customers from rivals. It will strengthen its image as a business that has "green" credentials.
- Sales of *Benno's* drinks have fallen significantly over the last five years– so it is important that *Benno* does something to stem this tide.

Against:

- It will cost \$5m to buy the machinery to produce the new rings and the business has no accumulated retained profits – therefore the funds will need to be raised, probably externally via a bank loan, which will lead to interest charges and an increase in operating costs. It may take time to find a suitable angel investor to help finance this project. Will the angel investor wish to exert some control over *Benno's* operations?
- The unit cost increase is 50 %, a rise from 10 cents to 15 cents per ring, and the business only has a net profit margin of 10 %. As the market is competitive and reports suggest that consumers are price sensitive, a price rise – passing on the cost of the new rings – is probably not going to be possible. The result is that *Benno's* net profit margin will fall.
- Sales are falling, particularly to the 12–18 age group – are they going to be energized into buying a product that is more environmentally friendly, particularly when reports suggest purchases of green products are not increasing?
- In terms of a new way forward for *Benno*, the introduction of the new rings has a great deal of merit. There are a large number of marketing opportunities available in a competitive market and this idea will strengthen *Benno's* brand. However, the forecasted financial implications of this idea are not ideal and if sales volumes do not increase significantly then *Benno* may find itself financially worse off if profits do not increase. One solution may be to wait until some more objective market research via a new untested focus group have given their thoughts on the new ring.

M18/3/BUSMT/SP2/ENG/TZ0/XX

Fishers

a. Define the term current assets [2 marks]

Current assets are items either owned by a business or owed to that business with a life of less than twelve months.

b. Using Table 1, calculate Fishers's net profit before interest and tax for 2017 [2 marks]

Sales revenue – variable costs – fixed costs = net profit before interest and tax

$$900\,000 - (6 \times 75\,000) - 55\,000 = \$395\,000$$

c. **i. Using Table 2, calculate the following forecasted figures for 2018: sales revenue [1 mark]**

\$990 000

ii. Using Table 2, calculate the following forecasted figures for 2018: total variable costs [1 marks]

\$577 500

iii. Using Table 2, calculate the following forecasted figures for 2018: income tax [1 mark]

\$65 500

iv. Using Table 2, calculate the following forecasted figures for 2018: net profit after interest and tax [1 mark]

\$262 000

d. **Explain why Fishers experiences a significant increase in current assets and current liabilities from March to October [2 marks]**

In anticipation of increased sales during the period April through September, Fishers must increase production starting in March. Thus, it buys more stock, which increases both current assets (stock, which later become debtors) and current liabilities (short-term borrowings and creditors). Fishers maintains this higher volume of trading (and levels of current assets and current liabilities) until sales start to contract in October. In anticipation of lower sales from October through March, the reverse of the process above occurs.

Visionary Toys (VT)

a. **Define the term unique selling point [2 marks]**

A unique selling point is any aspect of the organization, brand or product that enables differentiation in consumers' minds from the competitors.

b. **i. Construct a fully labelled balance sheet for VT for the end of 2017 [5 marks]**

Balance sheet for VT for the end of 2017:

Fixed assets	\$30 000	
Less accumulated depreciation:	\$3 000	
Net fixed assets		\$27 000
Current assets:		
Stock	\$4 500	
Debtors	\$3 500	
Cash	\$1 000	
Total CA		\$9 000
Current liabilities:		
Overdraft	\$2 000	
Creditors	\$4 000	
Short-term loans	\$1 500	
Total CL		\$7 500
Net current assets/ working capital	\$1 500	(9000-7500)
Total assets less current liabilities		\$28 500
Long-term liabilities	\$5 000	
Net assets		\$23 500
Financed by:		
Share capital	\$13 500	
Retained profit	\$10 000	
Equity		\$23 500

ii. Calculate the acid test (quick) ratio for VT for 2018 [1 mark]

Current assets: \$9000

Stock: \$4500

Current liabilities: \$7 500

$$\text{Acid test ratio} = \frac{9000 - 4500}{7500} = 0.6$$

c. **Explain one way VT could improve its liquidity [2 marks]**

Ways VT could improve liquidity include:

- attempt to operate with a lower re-order level of stock
- sell fixed assets and lease long-term assets
- pay less in dividends
- raise capital, either more share capital or long-term debt.

JVS

a. **State two stages of the product life cycle [2 marks]**

Introduction; growth; maturity; decline; withdrawal

b. **Apply the Boston Consult Group (BCG) matrix to JVS's current product portfolio [4 marks]**

Award [1] for a basic answer that shows some understanding of the Boston

Consulting Group matrix.

Award [2] for an answer that shows a good understanding of the Boston Consulting Group matrix. This may be descriptive or in the form of a drawn diagram.

Award [3] for an answer that shows a good understanding of the Boston Consulting Group matrix and places both of JVS's products (Izzys and IzzDen) in their correct segments in a BCG matrix or explains their positions. Izzys is a cash cow, IzzDen is a dog.

If a candidate correctly links the products to the BCG matrix but provides no explanation. Award [1] for each correctly linked product up to a maximum of [2].

Example:

Izzy – cash cow

IzzDen – dog Award [2]. For Izzy – star IzzDen – dog Award [1].

c. Explain one advantage and one disadvantage for JVS of using focus groups for its market research [4 marks]

Advantages of focus groups include:

- They can provide detailed information about customer feelings, perceptions and opinions. The introduction of Izzless would represent a risky move by JVS, as the mass-market product could undermine Izzy's established reputation as "high end".
- They are cheaper than performing individual interviews. Already, JVS spends more on market research than its competitors. By relying on focus groups rather than individual interviews, JVS can get detailed information at a lower cost than individual interviews.
- They provide opportunities to clarify any issues or problems. The target market of Izzless is 15 to 19-year-olds, many of whom have low incomes. JVS has limited to no experience with this group. Focus groups, which allow for dialogue and back-and-forth, can allow JVS to get a clearer idea of issues and potential obstacles.

Disadvantages of focus groups include:

- They can be hard to control and manage. JVS will probably have two different types of focus groups: its traditional customers and the new 15 to 19-year-old group who would buy Izzless. Especially with the latter group, controlling and managing them could prove challenging.
- the results are difficult to analyse. Focus group feedback can be inconsistent and contradictory, a problem made worse because of the young age of participants.
- Members may not reveal their own feelings but are swayed by the majority view. This potential problem is true of any focus group but is especially heightened for the product Izzless. Teenagers tend to be more swayed by peer pressure than other groups.
- They may not be representative of the target market as a whole. Unless JVS is willing to go to considerable expense to have focus group participants flown in from across its market area (all of Europe), participants are likely to come from a handful of cities, or as few as one or two cities. These participants may not be representative of the whole market.

d. Recommend whether JVS should launch the new product, Izzless [10 marks]

JVS currently only has two products in its portfolio and will cease production of one of them, IzzDen, later this year. A business with just one product puts itself in a dangerous position, as if demand for that product falls the business could face losses and possibly failure.

The launch of the new product would take the business into a new market targeting low-income young consumers who want to purchase fashion shorts. It would also broaden JVS's distribution channels as it would now use mass market retail discount stores and online delivery – at present the business only sells through high end independent retailers. Low-income consumers may relish the chance to buy shorts that have a brand name that is associated with high quality and designer fashion at affordable prices – this may give JVS a competitive edge in this highly competitive market.

However, the move is not without risk. The market is very competitive and JVS's products may not be able to establish a foothold in the market. There is also the danger that this new product may impact on the sales of their cash cow, Izzys. This down-market product may damage its brand image, which, according to a marketing expert, is one of the business's major strengths. It would end up with two products aimed at very different markets using premium prices for one product and competitive pricing for the other – this clash of images may not work. Perhaps JVS should consider launching a range of shorts at their current target market and work to its strengths.

Healthy Start (HS)

a. Describe one role of a vision statement for HS [2 marks]

A vision statement for *HS* is likely to help the organization set its short-term and long-term objectives. It is likely to act as an important driver for recruitment, selection and motivation of its young unskilled workforce made up of school leavers.

b. i. Explain how the following can benefit HS: job enlargement [2 marks]

Job enlargement will increase the range of skills and tasks able to be performed by the school leavers who may lack direct experience of working in a national chain and/or batch production. As recruits will hopefully become future managers, it will be important for effective future leadership in the stores to have experience in all jobs offered by HS.

ii. Explain how the following can benefit HS: Intrapreneurship [2 marks]

Intrapreneurship allows for risk taking, creativity and innovation within HS. Given the intense competition from the global fast food restaurants, the opportunity to develop new healthy snacks will be vital to maintain market share.

c. Explain two possible economies of scale available to global fast food restaurants but not HS [4 marks]

Possible economies of scale available to the global fast food restaurants include:

Marketing economies of scale: the global fast food companies are likely through their global reach to experience significant economies of scale in marketing/selling across a whole range of markets. HS is a national chain and will not be able to spread advertising costs, for example, across a whole range of markets. Unit costs of marketing will be much lower for the global restaurants.

Bulk-buying economies of scale: to develop and meet global demand and to fill supply chains, global fast food manufacturers are likely to achieve significant economies through the bulk-purchase of raw ingredients (a number of fast food manufacturers have vertically integrated with suppliers to ensure that logistics are in place). Again, unit costs of operations are likely to be lower than HS's.

Financial economies of scale: being present in global markets allows global fast food manufacturers to borrow funds for expansion at much lower rates than a national chain. It is indicated in the stimulus that HS finances its training and professional development through retained profits.

d. Discuss the two options that Tom is considering for HS in response to the intense competition [10 marks]

The first option, which is to implement flow production, is likely to lead to an increase in production and productivity because of the new technology and specialized roles. Currently, HS uses batch production. With improved productivity, HS can increase its portion size without raising prices. As a result, HS may be able to compete more effectively with the global fast food manufacturers.

However, the introduction of flow production may result in a reduction in the opportunities for job enrichment and intrapreneurship. If the new production process is going to lead to specific jobs on the production, then apart from job enlargement or rotation, the current employees may become demotivated through a restriction on personal growth and development opportunities. Staff turnover may increase as employees seek more innovative or challenging work. It is likely to be expensive to implement flow production both in terms of the financing and inevitable changes in organizational culture at HS.

The second option may be quicker to organize and much cheaper. The online reality TV show will have established HS firmly in the minds of existing and potential customers. A social media campaign will amplify the brand value of HS and should increase market share.

However, measuring the success of social media on market share will be difficult even though the target market should be familiar with this method of promotion. The biggest factor against this campaign, however, is that as a competitive tool against the global manufacturers there will still be this perceived difference in portion size. A social media campaign will not address this aspect. In fact, there is a danger that negative response to the campaign make reduce market share even further.

Both of the responses have some merit, but it would appear that the first option is the most appropriate to tackle the issue of competition with the global fast food manufacturers. The changes in the production process will take some time to bed in and a few staff may leave to work for other snack food manufacturers who have more dynamic or challenging roles. However, the social media campaign will not close the perceived gap between the products offered by HS and those offered by their competitors and, thus, could backfire.

M17/3/BUSMT/SP2/ENG/TZO/XX

Sotatsu Electronics (SE)

a. Define the term price skimming [2 marks]

Price skimming is setting prices high when introducing a new product to the market. This strategy typically works only for a limited time, as competitors will respond to the new product with innovations to their own products. As competitors introduce new products in response, demand for the original company's product (the company price skimming) falls, and prices must be lowered.

b. i. Calculate the values of X and Y in Table 1 [2 marks]

X = \$2200 (millions of dollars)

Y = \$1500 (millions of dollars)

ii. Construct a profit and loss account for SE for 2015 and 2016 [4 marks]

	2015	2016
Sales revenue	4300	5100
COGS	2100	2300
Gross profit	2200	2800
Expenses	1200	1300
Net profit before interest and tax	1000	1500

c. Calculate net current assets (working capital) for 2016 [2 marks]

Net current assets (working capital) is calculated by subtracting current liabilities from current assets (all in millions of dollars):

Current assets – Current liabilities = Net current assets

\$700 – \$300 = \$400

Anubis

a. Outline two appropriate external short-term sources of finance for Anubis other than loans from family and friends [2 marks]

The sources of finance suggested must be external and short term – therefore the only four rewardable answers are:

- Trade credit
- Factoring
- Overdraft
- Short-term bank loan

b. Using the information above, prepare a fully labelled cash flow forecast from January to March 2018 [5 marks]

	Jan	Feb	Mar
Opening balance	8000	2000	1000
Inflows:			
Sales	300000	300000	300000
Tax refund		3000	
Total cash inflows	300000	303000	300000
Outflows			
Rent	2000		
Packaging	15000	15000	15000
Wages	50000	50000	50000
Cost of sales	220000	220000	220000
Heating and lighting	4000	4000	4000
Delivery	15000	15000	15000
Total cash outflows	306000	304000	304000
Net cash flow	(6000)	(1000)	(4000)
Closing balance	2000	1000	(3000)

c. Comment on the predicted cash flow for Anubis for 2018 [3 marks]

The cash flow forecast is a cause for concern. The forecast covers the first three months of 2018 but the closing balance worsens each month and is forecasted to be negative in March. Thereafter, Anubis faces lower gross profit margin because of lower retail prices of

phone cases and higher wages costs. Given that the market is increasingly competitive, Anubis may not be able to generate sufficient additional sales revenue to offset the lower gross profit margin. Thus, the situation for Anubis is not promising.

Dales

a. Outline two common steps taken by a business in recruitment [2 marks]

Common steps taken by a business in the process of recruitment include:

- identifying position
- evaluating the requirements for the position
- developing a job description
- determining recruitment plan
- determining search committee
- advertizing position
- reviewing applicants and developing a list to interview
- conducting interviews
- selecting the candidate that best fits the description
- offering position and negotiating terms.

b. i. Explain two disadvantages for Wire of introducing a piece rate system of wages for its cleaning staff [4 marks]

- Housekeepers may stop worrying as much about the quality of the job they do, instead only worrying about the number of rooms they can clean per hour to achieve greater earnings.
- The piece rate method may also discourage teamwork in the workplace because individual housekeepers simply want to complete more of their own work.
- The increased stress that results from having to clean more rooms may result in increased staff turnover and make it more difficult to recruit housekeepers in the future.
- Staff may become demotivated because they now have to clean more rooms for less pay.
- The piece rate system could damage Wire's relationship with its customers such as Dales as the bad press could lead Wire's customers not to renew contracts.

ii. Calculate the financial impact on cleaners employed by Wire from the introduction of the piece rate system in 2016 [2 marks]

Wages earned in time-based system = $\$6 \times 8 \times 5 = \240 per week

Wages earned using new piece rate system = $\$2 \times 20 \times 5 = \200 per week

Financial impact on cleaners = $\$40$ per week. The question does not specify a time frame. Therefore, accept any time frame as long as the candidate is consistent. For example, $\$6 \times 8 = \48 and $\$2 \times 20 = \40 . Financial impact on cleaners = $\$8$ per day.

iii. Calculate the change in cleaning costs per room from the introduction of the piece rate system used by Wire [2 marks]

Cleaning wage cost per room in old system = $\$6 \times 8$ divided by 13 rooms = $\$3.69$ per room

New system: $\$2$ per room, therefore the change in cleaning costs = $\$1.69$ per room

c. Recommend if Dales should stop outsourcing the cleaning of hotel rooms [10 marks]

If Dales stops outsourcing its cleaners then costs will rise. Outsourcing did cut costs per room from 5 % of room revenues to 2 % - this is likely to be reversed if they stop outsourcing, unless of course they operate the same system as used by Wire: a piece rate system. Costs could, in the short run, increase - Dales will now be responsible for training and recruitment costs, which are unavoidable. These costs could be significant, especially since in 2016 Dales's profits decreased from $\$24$ m to $\$4$ m. This increase in costs could cause them to make a loss at least in the short term.

However, stopping outsourcing will not deal with Dales's other problems - wage rates at Dales are below the average for the hotel industry. Consequently, staff turnover is high. Recruitment is difficult due to the number of hotels in the area and the wages paid. Cessation of outsourcing of cleaners will have no impact on these issues.

Hotel guests may find that their rooms are cleaned to a higher standard if Dales returns to having cleaners only clean 13 rooms per day rather than 20. However, if Dales sticks with the piece rate system adopted by Wire then nothing will really change and poorly cleaned rooms may continue to be an issue.

Hotel guests are critical not just about room cleanliness but also about food quality and poor customer service across the hotel. Cleaner rooms may help reduce the fall in room bookings but unless other concerns such as food quality and customer service are challenged then insourcing of cleaners may do little to arrest the decline in bookings. Certainly, it is a step in the right direction, but Dales's problems appear deeper than just poorly cleaned rooms and unless these are dealt with the future looks grim.

Dales operates in a highly competitive market and unless it offers wages on par with rival hotels then staff turnover will remain high. Continued high labour turnover will not help it establish better customer care and may be a significant factor in the poor quality of food sold in the hotel. Dales is positioned as a high-price and high-quality hotel – guests that pay high prices expect good food, polite staff and a clean room.

In order to reach the top bands of the markscheme candidates must demonstrate that insourcing will only solve one of Dales's problems and must discuss the importance of the other factors in contributing to their falling room occupancy rates.

Secco Vineyards (SV)

a. Describe one characteristic of a niche market [2 marks]

Describe one characteristic of a niche market.

Characteristics of a niche market include that they:

- are narrow
- are smaller than most markets or a fraction of a market
- often require specialized processes (marketing or operations) to fill the niche
- more specific in terms of features or quality of the product or service
- given the above niche markets or segments may be characterized as having higher final prices to consumers.

b. With reference to SV, explain one advantage and one disadvantage of using secondary market research [4 marks]

Advantages of secondary market research include:

- Efficient in terms of time – the data on wine consumption patterns, for example, has already been collected by someone else and is available.
- Effective in terms of cost – often, secondary research is free and, when not, is typically less expensive than the process of gathering primary research.
- Often, ample secondary research exists. On certain topics or related to certain markets, secondary research can be extensive. It has allowed SV to consider new geographical markets which it may not have considered before.
- Others have often thought through many of the core issues and a business can benefit from the insights of experts of collated data and written about them.

Disadvantages of secondary research include:

- Lack of precise focus on the issue or problem concerning a business
- Lack of timeliness – often secondary research is outdated
- Uncertainty about the quality of the data collection/research.

c. Given the intense competition, explain two pricing strategies SV might consider [4 marks]

Pricing strategies that SV might consider include:

- Cost-plus (mark-up) – SV may want to return to this pricing strategy, which guarantees that for each bottle of wine it sells the business is covering its per unit costs. However, SV's brand identity might suffer if it lowered prices.
- Penetration – SV could use this pricing strategy as it enters new markets. Penetration pricing would allow SV to attract first-time customers in new markets with lower-than-normal pricing. Once some brand loyalty develops, SV could then raise prices.
- Psychological – Whereas psychological pricing sometimes refers to pricing below certain thresholds (\$9.99 rather than \$10.00) for a psychological effect, another form of psychological pricing is pricing a product high as a way of suggesting that the product is of high quality or value. SV might try to strengthen its brand identity with psychological pricing along this line, especially as the competition is intense.
- Loss leader – SV could try a loss-leader strategy, whereby it sells one of its wines at very low prices in an attempt to get consumers to buy SV wines. Other varieties of SV wines, however, would be priced in a fashion to compensate for the losses on the one type. This strategy, like others involving attracting customers through low prices, could weaken SV's brand identity.

- Price discrimination – SV might consider is price discrimination, where SV sets the prices based upon the market that it is entering. For example, SV might charge more for wines in New York City than in Charlotte, NC. Both cities (major banking centres in the United States) have upscale buyers. Nevertheless, prices of virtually all types of goods and services cost less in Charlotte than in New York.
- Premium pricing – Though premium pricing is not in the guide, candidates are free to use it if they wish. Premium pricing occurs when a business inflates its prices precisely to enhance brand value. Consumers think that, by paying more, they are getting a better product.
- Promotional pricing – setting pricing very low for a short period to get customers to buy your product, often for the first time.
- Value-based pricing – setting a price based upon what consumers perceive the value of the product to be rather than on the actual cost to produce.

d. Recommend which of Option 1 and Option 2 SV should consider in order to increase sales [10 marks]

SV is considering two options:

Option 1: open a business-to-consumer (B2C) e-commerce “store”.

This option would involve selling wines online to consumers. They currently sell directly to customers at the vineyard.

Benefits of this approach include:

- SV can reach a wide market area.
- The website and consumer traffic on the website is relatively inexpensive advertizing. It is important for a new company trying to enter new markets to keep costs of entry low.
- Promotion and advertizing can easily be extended via social network sites.
- Online offers can reach much wider target markets.
- From a consumer perspective, B2C e-commerce also has benefits, especially the convenience and ability to compare prices and explain the differences between wines sold to make an informed decision. Important in a premium market.

B2C e-commerce also has disadvantages, which include:

- SV would have to address consumer concerns that its site is secure.
- SV would have to incur costs making sure that the site is secure.
- Competitors can easily track what SV is doing to promote and sell its products
- Setting up the website and establishing the procedures for fulfilling orders could be expensive. New supply chains to reach new customers may have to be created adding to short-term costs.
- Alcohol is a heavily regulated product, especially in the United States, and it could be complicated and cumbersome for SV making sure that it is in compliance with federal and state laws (and laws regarding alcohol vary from state to state).
- SV would also have to make sure that selling wines online did not conflict with the premium brand identity that SV otherwise tries to maintain.

Option 2: sell SV wines to wholesalers serving the whole of the US market for premium wines.

Advantages of this approach include:

- The wholesaler stores the product, thereby reducing storage costs for SV.
- The wholesaler purchases in bulk and then breaks the bulk purchases into smaller batches for the retailers. This process means that SV does not have to concern itself with small orders by individual retailers. This may be important in a premium market.
- Because SV wants to sell over long distances – the entire United States – this approach pushes much of the complicated processes of distribution to wholesalers.

However, working with wholesalers has disadvantages:

- Wholesalers sell the products of many companies, and their loyalties and highest priorities may be with other brands.
- Working with wholesalers adds another intermediary and mark-up, which can lead to higher prices to consumers (who may respond by purchasing other products) or to thinner margins for SV.
- Working through wholesalers and distributing across the United States, SV may not be able to afford national promotion. If it cannot, it will have to rely on the wholesalers and retailers for much of its promotion. Can SV be confident that the wholesales will position SV’s new wines positively? How will they check?

Overall, option 2 is possibly the longer term option, involves considerable costs, is potentially the greater risk, but the profits could be considerable over option 1. Option 1 is a market penetration strategy effectively trying to sell the same product in the same

market via an online channel. Initially, customers who would have bought directly from the vineyard could go online instead. Overall sales may increase marginally. This will change over time as the e-commerce store becomes more sustainable but from the information given in the stimulus, option 2 would seem to have the greater market potential for growth. (Market development to use the Ansoff terminology but direct application to the matrix is not expected.)

Gen Y Limited

a. Outline two features of an autocratic leadership style [2 marks]

- Decision making in an organization is restricted to a very small group of select individuals.
- Limited consultation and discussion in an organization given by autocratic leadership.
- Communication tends to be downward and one-way only.

b. Apply Daniel Pink's motivation theory to the programmers at Gen Y [6 marks]

Daniel Pink's motivation theory identifies that there are three key drivers, or factors, that influence motivation for cognitive or thinking tasks leading to improved performance for a business. The three key drivers are:

- mastery
- autonomy
- purpose.

From the stimulus we can argue that, before Petra's potential involvement, Gen Y allows for:

- Purpose – high-quality reports providing innovative market research. The business is providing revolutionary work for its clients. This would act as a motivator for Gen Y programmers as they are carrying out ground-breaking work.
- Autonomy – Gen Y allows for employees to work on individual dream projects. They are also empowered to make their own decisions.
- Mastery – there is evidence from the stimulus that Gen Y has used cognitive training. This would presumably build capacity to develop and refine skills of the programmers, again boosting motivation according to Pink and allowing them to be more creative.

c. Explain one reason, other than increased sales revenue, why it is important that Gen Y generates new revenue streams [2 marks]

Gen Y's core business is the creation of innovative market research data reports. The business also allows employees to work on "dream projects" during the working week. In order to remain innovative and sustainable, Gen Y will need to secure new finance through new revenue streams to ensure that the creative and innovative energy continues to flow. New revenue streams will also allow Gen Y to continue to motivate workers through their Pink motivational model, which could be expensive to finance given the cognitive training required. The company has not yet made a profit, so generating alternative revenue streams would be essential, especially if salary costs need to rise to attract new talent in the future.

d. Discuss whether Zack should sell Petra half of his shares with her conditions [10 marks]

By selling his shares to Petra, Zack faces concerns not only of ownership but also that the culture of Gen Y – which by assumption has led to the success and motivation of employees – will have to be systematically changed. It is uncertain at this stage whether this change in culture will bring forward any improvements.

In common with many other start-ups, profit for Gen Y remains elusive despite the considerable sums invested. Zack has tried to finance "dream projects" to turn inventions into innovation but without success. The harsh reality is that without funding coming into the business, the long-term sustainability of Gen Y is in doubt. If he does not take some action now and invite Petra into the business, then all jobs and intellectual property at Gen Y are under threat. Some programmers may leave the company if they sense that for some reason the opportunity to work on dream projects is cut back. Taking on Petra as a partner may weaken Zack's control but will ensure in the short term that Gen Y remains viable.

However, to receive this funding, Petra has added conditions that Zack must accept. These conditions will not be popular in an organization where there are strong links to Daniel Pink's motivational theory. A leadership style change to autocratic will impact on the autonomy currently enjoyed by the employees. The purpose may also be affected, as Petra will wish to have a strong influence in the type of vision or direction, she wishes to see Gen Y move to. The ending of innovative and revolutionary "dream projects" may be the first casualty. Motivation could be destroyed.

Further, the insistence on specific targets for programmers may impose deadlines/restrictions, which may be too much for the employees to take who have been empowered to make their own decisions.

The short-term situation is difficult for Zack. He has to balance the financial issues present in the case study with the idealism and motivation of his workforce. Petra's conditions, whilst restrictive, may save Gen Y. Zack may be forced to sell this idea of Petra

receiving half his shares to his employees. Some employees may quit and be hired by competitors but perhaps they may not have been committed to Gen Y and Zack's purpose. Either way, Zack will find it difficult to turn down Petra's offer.

N17/3/BUSMT/SP2/ENG/TZ0/XX

Pelican Pies (PP)

a. Describe one reason why brand loyalty would be important to PP [2 marks]

Brand loyalty would be important to PP given that they operate in a local market with a number of competitors and that the prices they charge are higher. Given this fact, it would be critical for PP to have brand loyalty or their sales could fall (although not on the stimulus, sharp-eyed candidates may spot that PP's pies are price inelastic given the additional information for 2018).

b. Construct a profit and loss account for PP for the year ending 30 April 2017 based on the figures in Table 1 [4 marks]

	\$
Sales (8000 × \$4)	32 000
Cost of goods sold (8000 × 1.75)	<u>14 000</u>
Gross profit	18 000
Expenses	
Electricity (12 × 200)	2400
Rent (4 × 1000)	4000
Promotional	<u>1000</u>
	<u>7400</u>
Net profit before interest	10 600
8 % of \$40 000	<u>3200</u>
Net profit before tax	7400
Tax @25 % on net profit	1850
Net profit after interest and tax	5550

c. Construct a forecasted profit and loss account for PP for the year ending 30 April 2018 based on the figures in Table 2 [4 marks]

	\$
New sales quantity = 8000 × 1.2	9600
New price (\$4 – 30 %) = \$4 – 1.2 = \$2.8	
Sales (8000 × 1.20 × \$2.8)	26 880
Cost of goods sold (9600 × 1.75)	<u>16 800</u>
Gross profit	10 080
Expenses	
Electricity (12 × 200)	2400
Rent (4 × 1000)	4000
Promotional	<u>3000</u>
	<u>9400</u>
Net profit before interest	680
8 % of \$50 000	4000
Net loss before tax	3320

Moverse

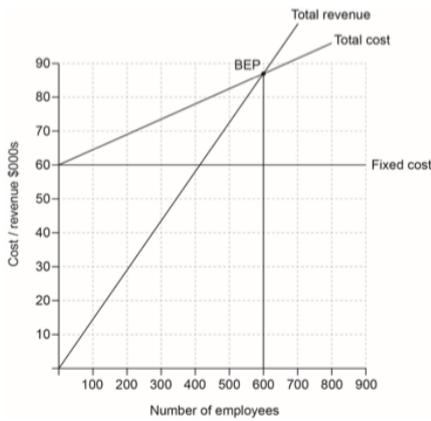
a. Describe the time rate method of paying wages [2 marks]

Employees are remunerated based on the duration of time that they work.

b. Calculate the break-even quantity for Moverse [2 marks]

Break-even level of output = fixed costs / selling price – variable costs = 60000 / 145 – 45 = 600 employees

c. Construct a fully labelled break-even chart, to scale, for Moverse if 800 employees enroll on Moverse's training programmes [4 marks]



d. Calculate the profit or loss if 800 employees enroll on Moverse's training programmes [2 marks]

Number of enrolled participants \times contribution – fixed costs = profit

$$800 \times 100 - 60000 = \$20000 \text{ OR}$$

Revenue (800 \times 145)	116000
Variable costs (800 \times 45)	36000
Fixed costs	60000
Profit	20000

Davenport Electronics (DE)

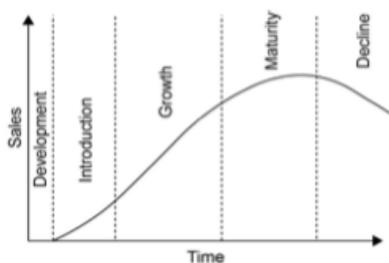
a. Define the term diseconomy of scale [2 marks]

Diseconomy of scale refers to an increase in average unit cost as a business increases in size.

b. Using the table, construct a product position map/perception map for all four companies [4 marks]



c. i. Draw and label a product life cycle curve [2 marks]



ii. Explain how DE's innovation is an extension strategy [2 marks]

DE's sales appears to have been at a maturity. Then, after the hackers, sales began to decline industry-wide. By developing an innovation that prevented the hackers from affecting the security of their product, DE was able to extend the life of its product. Sales not only returned to prior levels but actually began to increase.

d. With reference to DE, discuss the merits of small organizations compared to large organizations [10 marks]

In general, advantages of large businesses include:

- an enhanced ability to survive
- economies of scale
- higher status
- market leader status
- increased market share.

In general, advantages of being small include:

- greater focus
- greater cachet
- greater motivation
- competitive advantage
- less competition.

In the case of *DE*, the above advantages would in general apply. However, the circumstances can be further nuanced based upon the stimulus. Traditionally, the company was small and had a focus on quality, arguably its unique selling point. As the company grew, many insiders worried that *DE* would lose its focus on quality. Now, if it is to have cachet, it will have to rebrand itself and base its USP more on the security that its product offers.

Although the company probably also experienced a number of economies of scale, it was also experiencing some diseconomies, which invariably reflect that some inefficiencies from growth have crept into the business. With growth, *DE* has probably expanded its workforce. An increase in employees could change the character of the organization. Communication would be more difficult, both in the literal sense (having to communicate to a larger number of people) and in the figurative sense (new employees do not know the "unwritten" rules and norms of an organization, so greater care has to be taken in all communications).

An increase in size brings both advantages and disadvantages. In general, the larger the organization, the more it can benefit financially from size – more product lines and products and, with a diversity of revenue streams, an enhanced ability to survive. However, in *DE*'s case, it still has only one product. If the company grows and it increases its fixed costs, it takes some risks. If one of its competitors develops an ability to provide comparable security to the product of *DE*, *DE*'s sales could fall – but it may now be committed to higher fixed costs.

Grunsborg Textiles (*GT*)

a. State any two stages of the working capital cycle [2 marks]

Typically, stages of the working capital cycle include: purchase of materials from suppliers; production of goods; goods sold, typically on credit (unless a retail store); payment received by debtors

b. i. Calculate for *GT*: the payback period for the €44 million investment in new equipment based on the forecasted increase in net cash flow [2 marks]

Payback period = initial investment cost / annual cash flow from investment = €44000000/€8000000=5.5 years

ii. Calculate for *GT*: the average rate of return (ARR) based on an annual increase in net cash flow of €6000 and assuming an asset life of the new equipment of eight years [2 marks]

$$\text{Average rate of return (ARR)} = \frac{(\text{Total returns} - \text{total cost})}{\text{years of usage} \times \text{capital cost}} \times 100$$

$$\frac{(48\,000\,000 - 44\,000\,000)}{8 \times 44\,000\,000} \times 100 = 1.14\% \quad \text{Accept 1.1\%}$$

c. With reference to *GT*, explain one advantage and one disadvantage of debt factoring [4 marks]

Advantages of debt factoring. The business (*GT*):

- does not have to carry the invoice (receivable) for the duration (or longer) of the credit terms but rather receives cash immediately upon sale to the factor. Thus, factoring reduces the working capital requirements.
- does not have to provide any collateral. Unlike when taking out a revolving or seasonal line of credit, the business does not have to provide a lender with collateral. As a result, the business may use any assets it has available for collateral for other borrowing requirements.
- does not have the credit risk of the debtor, as the factor assumes the credit risk (though, over time, if *GT* routinely sold uncollectable invoices, the factor would adjust its discount rate to account for credit losses or not purchase invoices from certain customers). Without the credit risk, the business does not have to have a collections employee/department and will not have credit losses.

The disadvantages of factoring include:

- The high cost. While the discount rate may vary, the discount rate used by debt factors almost always equates to a higher rate of interest than a loan. Thus, the cost of debt factoring is high.
- Loss of control. Collection of the invoice is in the hands of the factor, who may or may not use collection methods consistent with the approach of the business selling the invoices. Customer relations could suffer if the factor uses harsh collection methods or a negative tone in collection.

- Damage to reputation. In general, some stigma is attached to reliance on debt factors, as it alerts customers that the business (GT) lacks working capital or the ability to borrow. A poor reputation weakens a firm's ability to negotiate and may mean loss of customers (businesses want suppliers who are reliable).

d. Examine Elaine's proposals to cut back on "GT's commitment to its employees and CSR practices" [10 marks]

The main thrust of this question is for candidates to consider the difficult financial situation that *GT* has gotten itself into and how the company may try to resolve the issue. The CFO's idea to cut back on *GT*'s commitments to employees and to CSR rests on the notion that commitments to employees and CSR are costly and that saving those expenses could help pay for the commitment and generate profits to support much needed working capital. However, the stimulus makes clear that commitments to employees and CSR are core values of the company and possibly the very basis for the success of the company. To eliminate them or weaken them may cause other (costly) issues for the business.

Green Clean (GC)

a. Define the term ethical objective [2 marks]

Ethical objectives are the goals of a business based on a set of values or moral beliefs. They should cover all the actions of an organization and guide its decision-making process and strategies. Ethical objectives at GC: using environmentally friendly products to reduce pollution; paying fair wages.

b. Explain one advantage and one disadvantage for GC of recruiting gardeners externally [4 marks]

Advantages could include:

- *GC* will have access to a larger pool of applicants for the job. They will increase their chances of recruiting trained professional gardeners to offer a wider range of quality services.
- New employees will have the necessary professional qualifications when hired.
- Recruiting externally could bring younger workers to the company that could help to motivate current employees and provide a fresher outlook at *GC*.

Disadvantages of recruiting gardeners externally:

- Recruiting gardeners externally can damage morale and motivation at *GC*. Cleaners may feel it lessens their chances of becoming gardeners. Productivity in the cleaning services may fall. Conflict with the union may arise and erode the working environment at *GC*.
- External recruitment could take more time, especially if in the labour market it is difficult to find professional gardeners.
- Externally recruited gardeners could take more time to adjust and adapt to the organization.

c. Explain one advantage and one disadvantage for GC of using off-the-job training for the cleaners who would like to become gardeners [4 marks]

Advantages include:

- An external provider is likely to have more expertise and knowhow in gardening than *GC*.
- It could help motivate cleaners who may see training to become a gardener as a form of promotion due to the higher wage paid.

Disadvantages include:

- Assuming that the training will take place during work time, there will be some disruption to productivity in addition to the cost incurred for the training itself.
- It is difficult for *GC* to monitor what the trainees have learnt. Will there be an examination at the end of the course?

d. With reference to two motivation theories, examine the motivation of cleaners at GC [10 marks]

GC wants to recruit professional gardeners and pay them higher wages. This decision is causing resentment among current cleaners at *GC*.

Candidates may refer to the following motivation theories: the works of Taylor, Maslow, Herzberg, Adams, Pink.

Candidates are expected to use two theories in order to examine the motivation of cleaners. Candidates are tested on their ability to apply theories with constant use of, and reference to, the information from the stimulus.

- Herzberg's motivation factors, for example, can be widened so as to include job satisfaction through being treated fairly, especially as the cleaners perceive the gardeners to be at the same skill level as themselves.
- Candidates could use Adams' theory in relation to the rewards from *GC* not meeting the efforts that cleaners are putting in. Though HR are considering offering employee share ownership scheme, which, if introduced, may cause resentment among shareholders as their wealth is shared.