OCR
RECOGNISING ACHIEVEMENT

ADVANCED GCE

BUSINESS STUDIES **F296/RB**

Business Production

RESOURCE BOOKLET

Monday 24 January 2011
Afternoon

To be given to candidates at the start of the examination. **Duration:** 2 hours

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INSTRUCTIONS TO CANDIDATES

- The information required to answer questions 1 – 6 is contained within this resource booklet.
- Do not hand this resource booklet in at the end of the examination. It is not needed by the Examiner.

INFORMATION FOR CANDIDATES

- This document consists of **4** pages. Any blank pages are indicated.

INSTRUCTION TO EXAMS OFFICER / INVIGILATOR

- Do not send this resource booklet for marking; it should be retained in the centre or destroyed.

Mihail's Olive Oil

The Simos family own an olive farm and have been producing olive oil since 1888. The farm is in rural Northern Greece and has been run for the last 35 years by Mihail Simos – the 'head' of the family. For some time the oil has been branded as 'Mihail's'. There is a relatively small production facility which has evolved very slowly over the last 120 years using a combination of labour and machinery. The production facility is sited adjacent to a large bottling plant. Mihail bottles and sells 360,000 litres of olive oil annually under the 'Mihail' brand.

The business comprises of two separate operations:

- it produces olive oil from Mihail's own olives, bottles it and sells it to a variety of retailers – this accounts for about 30 percent of his sales.
- it also buys in olive oil from surrounding farms – or imports it from Cyprus, Israel and over the nearby Turkish border – then simply bottles and sells it.

Within 70 km there are three other olive oil producers. However, they are all friends with Mihail and he does not really see them as a threat or as direct competitors. At times, they all collectively bulk buy olives from other farms, further afield, to supplement their own production. They also share processing and bottling techniques, ideas and sometimes labour.

The process of making olive oil is relatively straightforward for an experienced producer like Mihail. He reckons his 'First Press Premium Extra Virgin Olive Oil' – made solely from the first 'pressing' of his own olives – is one of the best on the Greek market. He sells it to supermarkets and health food stores at £2.23 for a 0.5 litre bottle. He also sells a 'standard' olive oil which is made from the second pressing. The 'bought in' oil is also subdivided into 'extra virgin' and 'standard'. In terms of costing, Mihail likes to view his products separately. For accounting purposes he treats them as separate profit centres and apportions fixed and variable costs to them accordingly (see Table 1).

Table 1 – Apportionment of costs for First Press Premium Extra Virgin Olive Oil in 2010

Apportioned annual equipment and maintenance costs	£34,000
Apportioned labour costs	£163,300
Apportioned advertising, overheads and other annual fixed costs	£52,000
Variable cost of bottles and labels (per unit)	£0.15
Cost of olives (per unit)	£0.28

In practice, the cost of olives can vary with the season, the weather and demand while Mihail has been known to vary his selling price of olive oil according to the outlet, location and even simply because he 'feels like it'. Occasionally a new machine is added, changing the fixed costs; and the price he pays for bottles depends on the quantity purchased. There is always some production wastage each year, and left over stock which is sold at a later date.

The olives are harvested with nets, collected in sacks and used in the production process as soon as possible. A hand operated machine is used for the pressing and this operation is time consuming. After the 'first press' oil has been drained off, to make the extra virgin olive oil, the remaining olive pulp is 'steamed' and pressed again to make the 'standard' oil. The quality of the oil depends upon the timing of this operation. Finally, the oil is bottled in batches of 48 using an old machine which fits a screw top cap but cannot stick on the very large labels which would make Mihail's oil more appealing. Currently, small labels are stuck on by hand.

Producing two types of oil – extra virgin and standard – ensures that waste should be minimised. However, the biggest drawback is that, with current production facilities, only one type of oil can be produced and bottled at one time and so there is considerable 'down time' (including washing, machine adjusting and bottle re-alignment) when the facility is changed from extra virgin to standard or back again. Mihail keeps the factory running for 10 hours each day, five days a week and employs 17 full time staff, regardless of production schedules and season. He is paternalistic towards his staff and rotates them between jobs. Even when there is very little to do, Mihail likes to keep them occupied with general maintenance, paying them regardless of how productive they actually are.

The First Press Premium Extra Virgin Olive Oil, whilst an award winning product, is expensive on the supermarket shelves. However, the bottle in which it is retailed does not look particularly appealing. Mihail is convinced that his customers 'know a good olive oil when they taste it' and are willing to pay for it. Mihail's younger sister, Georgina, who helps manage the production facility, is not so convinced, and in the face of growing and cheap foreign competition believes they should take another look at 'value'. The fact that retailers sell Mihail's oil at about £6.99 a bottle seems like a high mark up.

For years Mihail has paid little attention to quality control. It was only at the insistence of Georgina, following a faulty batch of oil – the first Mihail could remember – that he started paying attention to quality. Mihail got one of his staff to stand at the end of the production process once a day. His job was to simply sample oil from one 0.5 litre bottle and give a 'considered opinion'. Georgina had suggested that quality control should be a little more sophisticated than this, but Mihail was not interested.

Recently, Mihail had a very tempting offer. A large German multi-national supermarket chain had made contact with Mihail and the three other olive oil producers in the area. The suggestion was that they form a 'consortium' to collectively produce and supply the needs of the new supermarkets it is planning to open in Mediterranean Europe – initially three million bottles per annum. The implications of this were huge. Mihail's production capacity was insufficient, transport links are inadequate and the impacts on suppliers, current customers and Mihail's own staff can only be guessed at. The potential for growth, however, was massive.