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Cambridge Pre-U Certificate

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BUSINESS AND MANAGEMENT (PRINCIPAL)

9771/02

Paper 2 Strategic Decisions

For Examination from 2016

SPECIMEN MARK SCHEME

3 hours

MAXIMUM MARK: 100

The syllabus is approved for use in England, Wales and Northern Ireland as a Cambridge International Level 3 Pre-U Certificate.

This document consists of **8** printed pages.



Section 1

- 1 (a) Calculate the gross profit margin in 2010. [3]**

Formula: $\text{gross profit/revenue} \times 100$ (1 mark)

41.7/396.9 (1 mark)

= 10.5% (3 marks for correct answer only)

Award 3 marks if no % sign is included.

Award 3 marks if correct to 1 or 2 decimal places.

- (b) Calculate the net operating profit margin in 2010. [3]**

Formula: $\text{net (operating) profit/revenue} \times 100$ (1 mark)

12.7/396.9 (1 mark)

= 3.2% (3 marks for correct answer only)

Award 3 marks if no % sign is included.

Award 3 marks if correct to 1 or 2 decimal places.

(c) Comment on the usefulness to Redrow's directors of the results obtained in 1(a) and (b).

[6]

	Knowledge AO1 2 marks	Application AO2 4 marks
Level 2	2 marks Candidate shows clear knowledge of net and gross profit and the difference between them.	3–4 marks Candidate clearly explains the usefulness of the results using clear case context.
Level 1	1 mark Candidate shows some knowledge of net and gross profit.	1–2 marks Candidate uses limited case context.
Level 0	No rewardable response.	

Answers could include:

- Definition of gross and/or net profit margin.
- Allows a performance measure over time (comparison of 2010 figures with 2009).
- Gross profit margin 2009 was –32.4% v 10.5% in 2010.
- Net profit margin in 2009 was –39.4% v 3.2% in 2010.
- Profit measures are a key performance indicator (KPI).
- The figures indicate to the Redrow directors that the Balance Sheet is improving (helped by the rights issue).
- The results help to keep shareholders informed.
- Net profit enables the business to see how well overheads are being controlled.
- The higher the gross and net profit margins the better.
- Comparison with a similar business.
- The difference between the figures suggest Redrow may have significant overheads.
- ARA.

- (d) Analyse the main elements of a **MARKETING** plan that Redrow could use to attempt to increase profit margins. [13]

	Knowledge AO1 2 marks	Application AO2 5 marks	Analysis AO3 6 marks
Level 3		5 marks Candidate fully engages with the case context.	5–6 marks Candidate fully develops analytical points.
Level 2	2 marks Candidate shows clear and precise knowledge of a marketing plan.	3–4 marks Candidate links case material to his answer.	3–4 marks Developed analysis of arguments.
Level 1	1 mark Candidate offers a sufficient definition/ understanding.	1–2 marks Candidate makes a limited attempt to apply knowledge to the case study.	1–2 marks Weak analysis of ideas, failure to develop points.
Level 0	No rewardable response.		

Answers could include:

- Definition/stages of a marketing plan.
- Recognition and use of the key elements of a marketing plan such as marketing audit.
- Recognition of the corporate objectives of Redrow.
- The marketing strategy (4Ps).
- Price: consumers are price sensitive (elastic PED?) – should the business consider lowering prices to reduce stock? Impact on margins.
- Product: successful New Heritage Collection. Incentives to attract first-time buyers such as free carpets.
- Place: construct developments in high-demand areas with less exposure to government sector jobs.
- Promotion: budgets are limited but the business could continue the award-winning Redrow TV.
- Analysis of the performance of the strategy will be required. This could include surveys, normal distribution analysis and changes to profit margins.
- ARA.

Section 2

2 Evaluate the impact of a sustained increase in UK interest rates on Redrow.**[25]**

	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
Level 3		5 marks Arguments are consistently based upon case context.	6–8 marks Candidate fully develops analytical points.	6–8 marks Extensive, high-quality judgement shown.
Level 2	3–4 marks Good knowledge/ understanding shown.	3–4 marks Candidate makes a good attempt to apply knowledge to the specific case scenario.	3–5 marks Developed analysis of arguments.	3–5 marks Good judgement shown.
Level 1	1–2 marks Some knowledge/ understanding shown.	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study.	1–2 marks Weak analysis of the ideas, failure to develop points.	1–2 marks Weak judgement shown.
Level 0	No rewardable response.			

Answers could include:

Interest rate parameters:

- Definition of interest rates.
- What is the likely interest rate in its historical context?
- How large is the increase (refer to table)?
- How quickly will they rise?

External to Redrow:

- Reduced demand as higher rates increase mortgage costs (fixed rates?).
- Demand for housing is sensitive to interest rates.
- Speculative demand could fall further as net yields fall.
- Redrow specialises in low cost homes that are often bought by first-time buyers. This segment will be extremely sensitive to interest rate rises.
- Increased demand from downsizers?

Internal to Redrow:

- Financing costs have fallen to £12m (2010) from £21.6m (2009) (see accounts – largely due to the rights issue).
- The company is no longer highly geared (2010 = 10.8%).
- Net debt has been reduced to £47.1m (see reduction in bank loans as an example).
- Does Redrow borrow money at market or fixed interest rates?
- Does the builder use risk management strategies such as interest rate swaps?
- Interest cover ratio operating profit/interest $12.7/12 = 1.06$ (very low).
- Construction workers may demand higher pay.
- Reduce stock to minimise opportunity cost.
- Creditors to Redrow will press for quick payment.
- Redrow will try to delay payment to debtors.
- Interest rates are only one factor affecting Redrow and its customers. Other factors include employment levels and mortgage availability.
- ARA.

3 Discuss the extent to which the Board of Directors should respond to shareholder pressure for increased returns. [25]

	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
Level 3		5 marks Arguments are consistently based upon case context.	6–8 marks Candidate fully develops analytical points.	6–8 marks Extensive, high-quality judgement shown.
Level 2	3–4 marks Good knowledge/ understanding shown.	3–4 marks Candidate makes a good attempt to apply knowledge to the specific case scenario.	3–5 marks Developed analysis of arguments.	3–5 marks Good judgement shown.
Level 1	1–2 marks Some knowledge/ understanding shown.	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study.	1–2 marks Weak analysis of the ideas, failure to develop points.	1–2 marks Weak judgement shown.
Level 0	No rewardable response.			

Answers could include:

- Define shareholders and returns.
- Returns in terms of share price and/or dividends.
- Refer to data re FT250 and rival builder Persimmon.
- The Morgans are possibly the largest shareholder so they have a vested interest.
- Redrow could try to increase the sale prices of homes (unlikely).
- Redrow could concentrate on maintaining and improving margins (possible).
- Redrow could try and educate its shareholders that the returns are acceptable in the current environment and point to current successes.
- What return is acceptable? And how can this be achieved?
- The reality of an oligopoly.
- Dividend income is unlikely in the current climate.
- Comparison with peer businesses.
- ARA.

4 Redrow is considering two alternative strategies:

- continue with the current strategy of only building residential houses
- diversify into the construction of commercial property as well as residential houses.

Recommend which of these strategies Redrow should adopt. Justify your recommendation. [25]

	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
Level 3		5 marks Arguments are consistently based upon case context.	6–8 marks Candidate fully develops analytical points.	6–8 marks Extensive, high-quality judgement shown.
Level 2	3–4 marks Good knowledge/ understanding shown.	3–4 marks Candidate makes a good attempt to apply knowledge to the specific case scenario.	3–5 marks Developed analysis of arguments.	3–5 marks Good judgement shown.
Level 1	1–2 marks Some knowledge/ understanding shown.	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study.	1–2 marks Weak analysis of the ideas, failure to develop points.	1–2 marks Weak judgement shown.
Level 0	No rewardable response.			

Answers could include:

Option 1 (arguments for)

- It is Redrow's area of expertise.
- Some encouraging signs in the data.
- Award-winning marketing innovation.
- Vast experience in this sector.
- Take advantage of cost-reduction strategy.
- Potential to expand the land bank at reasonable prices.
- Popular New Heritage Collection range of homes.
- Low interest rates are helping affordability.
- Some signs of improvement in key macroeconomic indicators.

Option 1 (arguments against)

- Lower house prices may stifle demand.
- The credit squeeze.
- Potential interest rate rises.
- The company is not very diversified.
- Very competitive sector.
- Government austerity policies.
- Increasing unemployment.

Option 2 (arguments for)

- Would enable some spreading of risk.
- Ansoff Matrix strategy.
- The sector is similar to residential building.
- Enable diversification of market exposure.
- Redrow started as a civil engineering company and adapted over time.

Option 2 (arguments against)

- Similar to housebuilding.
- Porter's Five Forces/generic strategies.
- Demand is relatively low at the moment.
- It is a competitive industry.
- Redrow should not take risks in the current climate.
- The board and shareholders are divided on this issue.
- ARA.