

Cambridge Pre-U Specimen Papers  
and Mark Schemes

Cambridge  
**Pre-U**

Cambridge International Level 3  
Pre-U Certificate in  
**BUSINESS AND MANAGEMENT**

For use from 2008 onwards



UNIVERSITY of CAMBRIDGE  
International Examinations



# Specimen Materials

## Business and Management (9771)

Cambridge International Level 3  
Pre-U Certificate in Business and Management (Principal)

For use from 2008 onwards

**QAN 500/4023/6**

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### Syllabus Updates

This booklet of specimen materials is for use from 2008. It is intended for use with the version of the syllabus that will be examined in 2010, 2011 and 2012. The purpose of these materials is to provide Centres with a reasonable idea of the general shape and character of the planned question papers in advance of the first operational examination.

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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS  
Cambridge International Level 3 Pre-U Certificate  
Principal Subject

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**BUSINESS AND MANAGEMENT**

**9771/01**

Paper 1 Business Concepts

SPECIMEN PAPER

**2 hours 30 minutes**

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**READ THESE INSTRUCTIONS FIRST**

**Section 1**

Answer **all** questions.

For each question there are four possible answers **A**, **B**, **C** and **D**. Choose the one you consider correct and record your choice in pencil on the separate answer sheet.

**Read very carefully the instructions on the answer sheet.**

**Section 2**

Answer **all** questions.

**Section 3**

Answer **one** question.

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This document consists of **9** printed pages and **1** blank page.



### Section 1: Multiple Choice

Answer all questions from this section.

You are advised to spend 25 minutes on the 20 questions in this section.

- 1 A business has recorded the following total costs at different levels of output.

Units produced	Total costs (£)
10	5000
11	5250
12	5400
13	5650
14	6000

As the business increases output from 10 to 14 units, which of the following combination of statements is true?

#### Marginal costs

#### Average total costs

- |                                      |                             |
|--------------------------------------|-----------------------------|
| <b>A</b> Fall at first and then rise | Remain constant             |
| <b>B</b> Rise continuously           | Rise continuously           |
| <b>C</b> Fall at first and then rise | Fall continuously           |
| <b>D</b> Rise at first and then fall | Fall at first and then rise |
- 2 In the Boston Matrix, a product that has low market share in a high growth market is called a:
- A** Star/rising star
- B** Dog
- C** Cash cow
- D** Problem child/question mark
- 3 Which of the following is likely to improve a firm's cash flow?
- A** Longer creditor payment times
- B** Reduced creditor payment times
- C** Longer debtor payment times
- D** Paying suppliers in cash when goods are delivered

- 4 Calculate the break-even level of output if fixed costs are £60 000 and direct costs are £40 per unit. The selling price per unit is £100.
- A 1000 units  
B 2000 units  
C 6000 units  
D 10 000 units
- 5 An appreciation of sterling (£) against the euro (€) is likely to lead to:
- A Higher prices for UK exports in the eurozone and fewer eurozone imports into the UK  
B Lower export prices for UK exports in the eurozone and higher prices in the UK for eurozone imports  
C Higher prices for UK exports in the eurozone and lower prices in the UK for eurozone imports  
D Higher UK interest rates and higher UK inflation
- 6 An extract from the accounts of a company contains the following information:
- Acid test ratio = 0.5  
Liquid assets £50 000  
Stocks £25 000
- Based on this information, the current ratio of the company would be:
- A 0.75                      B 1                      C 1.25                      D 2
- 7 A business uses the declining balance method when depreciating fixed assets. New fixed assets costing £5m have been purchased. The rate of depreciation used is 30%. What will be the net book value of these assets after two years?
- A £2.0m                      B £2.45m                      C £2.55m                      D £3.0m
- 8 Which of the following is an example of 'above the line promotion'?
- A Sponsorship of celebrities  
B Press releases from the business  
C Radio advertising  
D On-pack promotions

- 9 A Finance Director has estimated the following cash flows from a new investment project:

End of Year	Cash Out (£m)	Cash In (£m)	Discount factor @ 10%
0	4	-	1
1	-	2	0.91
2	-	3	0.83
3	-	2	0.75
4	-	4	0.68

The Net Present Value of this investment project (at a discount rate of 10%) is:

- A** £11m
- B** £8.53m
- C** £7.35m
- D** £4.53m
- 10 One of the claimed benefits of a regionally decentralised business is:
- A** There is a close monitoring of operations in all countries the business operates in
- B** There is a smaller risk of unethical practices being adopted by subordinate staff in countries the business operates in
- C** Functional departments are free to adopt policies that best suit them
- D** Cultural differences can be reflected in decisions taken within each division
- 11 Calculate the total contribution if the following order is accepted:
- Quantity ordered = 1200 units  
 Selling price = £12 per unit  
 Direct labour and material costs per unit = £9.50  
 Cost of special machine needed to undertake this contract = £2400  
 Total fixed costs of the business = £55 000
- A** £600                      **B** £2400                      **C** £3000                      **D** £3400
- 12 One of the disadvantages of under capacity utilisation is:
- A** Higher direct costs
- B** Higher fixed costs per unit
- C** No time for machine maintenance
- D** High overtime payments



- 13 An example of an anti-competitive practice under UK law is:
- A Price discrimination
  - B Penetration pricing
  - C Selling exclusively on the Internet
  - D Price fixing agreements
- 14 Ansoff's Matrix assesses the risk of business strategies. All of the following strategies are included in the model **except**:
- A Market penetration
  - B Market segmentation
  - C Diversification
  - D Market development
- 15 A Public Limited Company announces a total dividend payment for 2008 of £500m. It has issued a total of 2000 million shares. If the share price at the end of 2008 is £5.00, then the dividend yield will be:
- A 10%
  - B 7.5%
  - C 5%
  - D 1%
- 16 In Critical Path Analysis (network analysis) the formula for calculating the total float on a non-critical activity is:
- A  $\text{EST of next activity} - \text{duration} - \text{EST (this activity)}$
  - B Critical path less duration
  - C  $\text{LFT (this activity)} - \text{duration} - \text{EST (this activity)}$
  - D  $\text{LFT} - \text{duration}$
- 17 Each of the following are typical Hackman and Oldham characteristics for assessing a 'good job' **except**:
- A No training required
  - B Autonomy
  - C Significance of the task
  - D Frequent reporting back on performance

**18** A business has estimated the price elasticity of demand for one of its products at  $-1.2$ . By how much will the total annual revenue from the sale of this product change, assuming the PED estimate to be accurate, if the price rises from £1 to £1.15 per item? Current sales revenue is £35 000.

- A** (£3 500)      **B** (£1 995)      **C** (£1 150)      **D** £1 995

**19** One of the potential drawbacks of contingency planning is:

- A** The events planned for will never occur  
**B** The events planned for become less likely over time  
**C** Frequently updating staff training can be expensive  
**D** The cost of planning is always greater than the potential cost of a disaster

**20** What would be the weighted Retail Price Index for 2008 (2007 = 100) based on the following data?

Item	2007 price	2008 price	% of average consumer income spent on item
Bread	£1.00	£1.20	25
Petrol	£1.20	£1.32	20
Rent	£60	£75	40
Shirt	£20	£18	15

- A** 115.5  
**B** 111.25  
**C** 105.5  
**D** 101.25

## Section 2: Case Study

Answer all questions from this section.

You are advised to spend 1 hour and 20 minutes on this section.

### Bargain Airways

The newspaper headline was quite clear:

#### **'Another year of record profits for Bargain Airways'**

This airline was set up by Paul Hussey just five years ago. He is a retired pilot for a major international airline. His friend, Sheila Wong, owned her own small plane. They decided to offer flights to passengers to local towns and cities. Paul and Sheila had to meet many legal requirements concerning health and safety standards. Even after the cost of these was accounted for, they were still able to charge much lower fares than larger airlines. They decided to create a private limited company and lease two more aircraft and extend the routes they offered. They had to recruit other trained pilots and the constraints imposed by employment legislation became apparent to Sheila and Paul for the first time. Now, after five years of rapid growth, record profits are being made. The two friends congratulated themselves on their success. 5 10

#### **Business expansion means organisational changes**

Bargain Airways fills a gap in the market for low cost flights without the 'extras' that add to other airlines' costs. So, they charge passengers for all drinks, do not offer food on board and only allow hand luggage onto the planes – no large bags can be carried. Tickets can only be bought via the Internet. 15

Business success brought problems too. Paul and Sheila changed the organisational structure of the business several times as it grew. A management team was recruited and this added two levels to the hierarchy of the company. These changes had not been popular with staff who had become used to Paul and Sheila's laissez-faire leadership style. The new management team insisted on quicker, centralised decision-making and this reduced discussions with staff. 20

An appraisal system for pilots offers them substantial bonuses for good attendance and time keeping. The turnover of staff in other parts of the business has increased recently. One leaver was heard to say, "We do not get paid as much as workers in bigger airlines but we no longer have the advantages of working for a small business". 25

#### **Location decision**

The business was now at a very important stage of its development. Sheila had forecast the demand = (xx) for low priced flights for the next two years. She had done this by analysing past Bargain Airways sales figures and by using secondary research into the growth of airline traffic in other countries. She told Paul: "I am confident that sales of our tickets will continue to rise by 20% for each of the next two years. We will need more aircraft to meet this demand. We may have problems recruiting enough extra staff of the right quality. I am also looking at opening up a new operating base at one of two airports, either in City X or City Y. The Finance Director has done some calculations for me to compare these two locations. (See Appendix A.) Finance should not be a major consideration given our large cash reserves." 30 35

**Appendix A: Analysis of alternative locations for a new Bargain Airways operating base.**

Forecasted:	City X	City Y
Annual fixed costs of site	£2 million	£1.5 million
Contribution per passenger	£10	£9
Capital cost of building (5 year lease)	£2.5 million	£1.4 million
Annual net cash flows (for first 5 years of operation)	£1 million	£0.5 million
Unemployment rate in the city	4%	12%
Number of airlines operating from airport	15	22

40

- 21** Assess the likely usefulness to Bargain Airways of the sales forecasting Sheila undertook for low cost flights. (line 28) [10]
- 22** Discuss how the directors of Bargain Airways might best overcome the resistance to change evident among the staff during the period of rapid growth for the airline. [10]
- 23** Recommend which city Bargain Airways should locate their next base in. Use the data in Appendix A, appropriate calculations from these data and any other relevant information to support your decision. [10]
- 24** Evaluate the likely impact of legislation on Bargain Airways. [10]

**Section 3: Essay**

**Answer one question from this section.**

**You are advised to spend 45 minutes on this section. Relevant references to real world business examples will be expected.**

- 25** To what extent should the success of a business organisation be measured by profits? [40]
- 26** Discuss the implications for a business of a decision to switch from a niche marketing to a mass marketing strategy. [40]
- 27** Evaluate the strategies a business could take when it is approaching full capacity working. [40]
- 28** Discuss the significance of the Human Resources department to the success of a multinational organisation. [40]

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**BUSINESS AND MANAGEMENT**

**9771/01**

Paper 1 Business Concepts

SPECIMEN MARK SCHEME

**2 hours 30 minutes**

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## **MAXIMUM MARK: 100**

Alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

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This document consists of **11** printed pages and **1** blank page.



## Section 1: Multiple Choice

<i>Question Number</i>	<i>Key</i>	<i>Question Number</i>	<i>Key</i>
1	<b>C</b>	11	<b>A</b>
2	<b>D</b>	12	<b>B</b>
3	<b>A</b>	13	<b>D</b>
4	<b>A</b>	14	<b>B</b>
5	<b>C</b>	15	<b>C</b>
6	<b>A</b>	16	<b>C</b>
7	<b>B</b>	17	<b>A</b>
8	<b>C</b>	18	<b>B</b>
9	<b>D</b>	19	<b>C</b>
10	<b>D</b>	20	<b>A</b>

[1 mark per correct key. 20 knowledge marks]



## Section 2: Case Study

**21 Assess the likely usefulness to Bargain Airways of the sales forecasting Sheila undertook for low cost flights. (line 28) [10]**

	<b>K 1 mark</b>	<b>App 3 marks</b>	<b>An 3 marks</b>	<b>E 3 marks</b>
Level 2		3 marks Points made well applied to case	3 marks Relevant reasoning or theory used to explain answer	3 marks Good judgement shown of the usefulness of sales forecasting in this case
Level 1	1 mark Some knowledge of sales forecasting shown	2–1 marks Some application to points to case	2–1 marks Limited reasoning shown	2–1 marks Limited evaluation of usefulness

- Definition of sales forecasting.
- Two methods used – time series analysis and secondary market research. This reduces the risk of inaccurate sales forecasts – but no method can be guaranteed to give accurate forecasts.
- First method could use moving averages and seasonal adjustment to arrive at a forecast based on past sales of this business. Second method could establish sales trends from other airlines.
- Could be useful to have forecasts to assist with forward planning of resources needed, e.g. numbers of aircraft/pilots needed.
- Evaluation could include: How old was the secondary data set and was the source reliable? How many years' data were used to extrapolate sales? Will the past be a good guide to future ticket sales – terrorist attacks? Overall conclusion or assessment needed for top L4. Do not accept generic evaluation of sales forecasting – must be clearly in context.
- ARA.

**22 Discuss how the directors of Bargain Airways might best overcome the resistance to change evident among the staff during the period of rapid growth for the airline. [10]**

	<b>K 1 mark</b>	<b>App 3 marks</b>	<b>An 3 marks</b>	<b>E 3 marks</b>
Level 2		3 marks Well applied to case	3 marks Relevant reasoning or theory used to explain answer	3 marks Good judgement shown
Level 1	1 mark Some knowledge shown	2–1 marks Some application case	2–1 marks Limited reasoning	2–1 marks Limited evaluation

- Fear of change – even during growth – can cause resistance as jobs are put at risk, nature of jobs change, new levels of management or new management structures, etc. Can be applied to this case.
- Effective communication is essential. Reasons for change, ways of change, impact of change, etc. must be fully explained to staff – opportunity for feedback also important.
- Involvement in change – staff participation can lead to better and more successful change. Difficult for staff who had become used to laissez-faire leadership style to accept a less participative approach.
- Evaluation could include: Are staff prepared and trained sufficiently to participate? Are owners of this business able to accept the change in management style needed? Will involvement of staff slow the process of growth and change? Overall conclusion assessing the ‘best’ ways to overcome resistance, clearly focused on this case, needed for top L4.
- ARA.

**23 Recommend which city Bargain Airways should locate their next base in. Use the data in Appendix A, appropriate calculations from these data and any other relevant information to support your decision. [10]**

	<b>K 1 mark</b>	<b>App 3 marks</b>	<b>An 3 marks</b>	<b>E 3 marks</b>
Level 2		3 marks Well applied to case – or accurate applications of formulae	3 marks Relevant reasoning or theory used to explain answer	3 marks Good judgement shown in supported recommendation
Level 1	1 mark Some knowledge shown, e.g. formula or relevant point made	2–1 marks Some application to to case, e.g. use of formula	2–1 marks Limited reasoning	2–1 marks Limited evaluation, e.g. weakly supported recommendation

	City X	City Y
Break-even point	200000	166666
Payback	2 years 6 months	2 years 10 months
ARR	20%	15.7%

- Analysis of results (allow OFR). For example, is the longer payback really significant in City Y even though it may mean slightly higher interest payments?
- How accurate are the cash flow forecasts?
- What is the current interest rate on borrowed capital and does the firm have a criterion rate of return?
- Does lower unemployment rate suggest that wage rates might be higher in City X?
- Are trained staff available in City Y?
- Does higher unemployment suggest area of low incomes – could affect demand for airline services?
- Is capital available for higher capital cost in Y?
- Evaluation could include: Coherent recommendation based on appropriate evidence – but there is no 'right' answer.
- ARA.

**24 Evaluate the likely impact of legislation on Bargain Airways.****[10]**

	<b>K 1 mark</b>	<b>App 3 marks</b>	<b>An 3 marks</b>	<b>E 3 marks</b>
Level 2		3 marks Points made well applied to case	3 marks Relevant reasoning or theory used to explain impact on business	3 marks Good judgement shown of the overall impact legislation
Level 1	1 mark Some knowledge of legislation shown	2–1 marks Some application to case	2–1 marks Limited reasoning	2–1 marks Limited evaluation

- Legislation such as Health and Safety, employment legislation, minimum wage, etc. impacts on business activity and costs.
- Airlines are likely to be particularly affected – give examples of H and S issues.
- Recruitment of pilots must accord with discrimination legislation – but minimum wage unlikely to be an issue. Length of working week could be, as need to fly back to base airport may exceed maximum EU hours.
- Meeting the requirements of such laws will add substantially to costs – very important for small business that focuses on ‘low prices’.
- Evaluation could include: Laws help to set standards that competitors must meet too so there is less chance of being undercut by illegal/unscrupulous rivals.
- Increased consumer confidence could lead to higher demand.
- Better and safer working conditions could make it easier to recruit good staff – may be very important to the long-run image and reputation of an airline.
- ARA.

### Section 3: Essay

#### 25 To what extent should the success of a business organisation be measured by profits? [40]

- L4 29–40 marks Coherent recommendation or judgement given based on supporting analysis. A well-balanced conclusion that recognises both the value and the limitations of profits as a measure of success will trigger the top of the band. A one-sided view of profits measuring success would gain marks at the bottom of the band.
- L3 17–28 marks Analysis of arguments and viewpoints that allows a judgement to be made. Profits as an indicator of management efficiency is one line of argument. Profits may also result from market dominance. The benefits and limitations of other indicators of business performance should be analysed to trigger the top of the band.
- L2 7–16 marks Points made are applied to business(es) selected by the candidate. Examples may be taken from different industries, e.g. losses by Ford indicate poor management efficiency at a time when other car makers are profitable. Profits made by oil companies when oil prices are high may not be a good indicator of success. To trigger the top of this band, clear and distinct reference should be made to at least one business or industry.
- L1 1–6 marks Subject knowledge only is demonstrated. To trigger the top of this band knowledge of profits, factors that determine profits or the importance of profit and the role of retained profit need to be demonstrated. A simple profit formula or definition will be at the lower end of the band.
- L0 0 marks No relevant business knowledge or understanding is demonstrated.

- Profits are return for risk. Used for re-investment and payments to investors.
- High profits – (or would high profitability, i.e. relative measure, be more appropriate?) – is one measure of relative success of a business compared to rivals or firms in other industries.
- High profits may result from efficient operations and effective management control – Marks and Spencer turnaround?
- Evaluation could include: High profits may result from market control – abuse of market power? Energy companies? Is this ‘success’? Might it lead to regulators taking action against the business?
- Are high profits short term, e.g. cutting long-term investment and setting high prices which could hit future demand? Or are they long term – resulting from continuous investment and development of new products, etc.? Sony, etc?
- Other measures of success? Social responsibility measures – if businesses fulfil their corporate social responsibility might this lead to higher profits in the future? Is Body Shop’s relatively low profitability an argument against this approach?
- ARA.

**26 Discuss the implications for a business of a decision to switch from a niche marketing to a mass marketing strategy. [40]**

L4	29–40 marks	Coherent recommendation or judgement given based on supporting analysis. The impact of such a strategic decision on the short- and long-term performance of at least one business needs to be assessed and weighed up to trigger the top of this band. Judgements based on one-sided analysis or weak examples would gain marks at the bottom of the band.
L3	17–28 marks	Analysis of arguments and viewpoints that allows a judgement to be made. The importance of economies of scale in mass marketing may allow a real competitive advantage to be gained. The loss of brand image and exclusivity could damage the USP of some businesses, e.g. in the cosmetic industry.
L2	7–16 marks	Points made are applied to business(es) selected by the candidate. Examples of both niche and mass marketing and possible switches from niche to mass marketing need to be considered to trigger the top of this band.
L1	1–6 marks	Subject knowledge only is demonstrated. Lower in the band the answer may contain just one or two definitions. Extending an answer beyond definitions to consider the likely price/profit margin/sales levels in these two market types will trigger the top of this band.
L0	0 marks	No relevant business knowledge or understanding is demonstrated.

- Definition of terms.
- Candidate's own examples – unless patently misunderstood.
- Higher sales. Higher profits – if sales increase greater than loss of mark-up. Economies of scale.

Evaluation could include:

- Loss of exclusive image and high price strategy (if moving down market to the mass consumer market).
- Loss of original low income consumers (if moving up market to the mass consumer market).
- Need for new advertising and promotion to support new image.
- Entire marketing mix may need to be adjusted – this mix strategy needs to be fully integrated so that consistent message is given to consumers.
- Cost of the changeover and the need for mass marketing need to be weighed up against the potential increase in sales and profits.
- ARA.

**27 Evaluate the strategies a business could take when it is approaching full capacity working.**  
**[40]**

- L4 29–40 marks Coherent recommendation or judgement given based on supporting analysis. A full consideration of the possible strategies and supported recommendations based on different business examples will trigger the top of this band. Judgements based on one-sided analysis or limited examples would gain marks at the bottom of the band.
- L3 17–28 marks Analysis of arguments and viewpoints that allows a judgement to be made. Expansion will add to fixed costs – and average fixed costs could increase if sales/output does not rise sufficiently. Use of outsourcing could damage reputation for quality and reliability – scope for appropriate analysis of business examples and these will trigger the top of this band.
- L2 7–16 marks Points made are applied to business(es) selected by the candidate. One limited example will gain the lowest mark in this band. At least two distinct examples that support different approaches to this problem will trigger the top of this band.
- L1 1–6 marks Subject knowledge only is demonstrated. A definition will only access the bottom of this band. An outline of at least two possible ways of approaching the problem will trigger the top of this band.
- L0 0 marks No relevant business knowledge or understanding is demonstrated.

- Explanation of term.

Problems with not taking action:

- Over-working of resources – capital and labour.
- No flexibility to meet exceptional orders or to satisfy loyal customers.
- No or little downtime.
- Subcontract work. Evaluation: concerns over cost and quality.
- Delay delivery times to customers – especially if the full capacity working is just a short-term problem. Evaluation: may lose customers to rivals.
- Raise prices to cut back on demand. Evaluation: potential loss of consumers to competitors and permanent loss of goodwill.
- Increase capacity, which may incur substantial fixed costs. Evaluation: need to use investment appraisal to assess long-term value of this option. Is capital available?
- Final evaluation could include: May depend on how long this situation continues, how competitive the market is and economic/market forecasts. Is it just a seasonal problem? The proposed solution will be very different if it is likely to be long term. Other conclusions possible.
- ARA.

**28 Discuss the significance of the Human Resources department to the success of a multinational organisation. [40]**

- L4 29–40 marks Coherent judgement given based on supporting analysis. To trigger the top of the band the conclusion will consider more than one business situation and assess that the importance will vary with the nature of the business but also that other factors will determine the overall success of any business. Judgements based on a one-sided view of the importance of HR would gain marks at the bottom of the band.
- L3 17–28 marks Analysis of arguments and viewpoints that allows a judgement to be made. Analysing in simple terms the work of an HR department in the context of a multinational will be marked lower in this band. A full analysis of the work and relative importance of this department looking at different business scenarios will trigger the top of this band.
- L2 7–16 marks Points made are applied to business(es) selected by the candidate. Simple consideration of the work of the HR department in just one business situation will be marked at the lower end of the band. To trigger the top of the band, appropriate reference to more than one multinational business situation and the role of the HR department will be necessary.
- L1 1–6 marks Subject knowledge only is demonstrated. Lower in the band the answer will contain little more than a definition. To trigger the top of the band the role of the HR department must be expanded and explained.
- L0 0 marks No relevant business knowledge or understanding is demonstrated.

- Define HR management/department. Outline HR responsibilities. These become more challenging with a multinational organisation. Candidates to use own company examples.
- Workforce planning – need to take into account demand levels and productivity levels in many countries before making such a plan. Vital to ensure adequate staffing levels in all departments in all countries. This task may be delegated to HR managers in each country.
- Employment and recruitment policy. Common one throughout the organisation? Allow different standards in different countries, e.g. reflecting different legal environments? High and common standards of employment conditions and recruitment likely to lead to more cohesive and united organisation.
- Pay levels/systems. Follow market conditions? Common levels in all countries? (Unlikely.) Need to ensure that pay levels/systems are competitive in each country to allow for adequate recruitment of skilled personnel.
- Allow any other relevant discussion/evaluation points.
- HR not the only factor leading to multinational success – final evaluation/conclusion should include an assessment of other factors that determine success of multinationals for top L4.
- ARA.



Question	Knowledge	Application	Analysis	Evaluation	Total
Section 1	20	0	0	0	20
Section 2					
Q21	1	3	3	3	10
Q22	1	3	3	3	10
Q23	1	3	3	3	10
Q24	1	3	3	3	10
Section 3	6	10	12	12	40
Total	30	22	24	24	100

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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS  
Cambridge International Level 3 Pre-U Certificate  
Principal Subject

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**BUSINESS AND MANAGEMENT**

**9771/02**

Paper 2 Strategic Decisions

SPECIMEN PAPER

**3 hours**

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**READ THESE INSTRUCTIONS FIRST**

Answer **all** questions.

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This document consists of **9** printed pages and **1** blank page.



## Tesco PLC

### Tesco Summary

Tesco is one of the leading international retailers. Since the company first used the trading name of Tesco in the mid-1920s, the group has expanded into different formats, markets and sectors. The main activity of the company is food retailing but the long-term strategy is based on four key elements: 5

- 1 Growth in the core UK business
- 2 To expand by growing internationally
- 3 To be as strong in non-food as in food
- 4 To follow customers into new retailing services 10

In the UK Tesco has 1897 stores with a combined sales area of 2.41 million square metres. This is to be supplemented by the planned opening of 124 new stores in 2006/07. The UK remains the most vital part of the Tesco empire, generating 80% of sales and profits. More than £1 in every £8 spent on the British high street now goes into Tesco's tills.

Tesco is keen to become a global player and operates in eleven other countries including Turkey and Malaysia. 15

Tesco employs over 450 000 people in its businesses around the world and in 2005 it announced an annual profit of £2 billion.

### Tesco and non-food

The company is very keen to expand the non-food side of the business. This includes electricals, home entertainment, clothing, health and beauty, stationery, kitchen items, soft furnishings and seasonal goods such as barbecues and garden furniture in the summer. The company has launched a highly successful range of own-brand goods from microwaves to patio chairs. 20

Currently Tesco has less than 7% market share of the total UK non-food sector. This equates to approximately £6 billion sales revenue each year. This is expected to grow and the UK's non-food sales growth is running at around twice that of the rate of food. Tesco has had widespread success across non-food sales and their own-brand clothing has been particularly successful. The £3 value jeans are well known in the industry. The Tesco labels, such as Cherokee, are gaining in prominence and threaten the esteemed position held by the clothing brand George at Asda. Tesco is also targeting larger clothing sizes, and the size 16–26 range is proving popular. The company has diversified its clothing appeal by offering products across price bands. The three main own-brand products sub-groups are Value, Tesco and Finest. 25 30

All Tesco stores sell some non-food items. The Superstore and Extra formats stock the largest variety. Tesco hopes to encourage shoppers to spend more of their disposable income by promoting the convenience factor of offering food and non-food items side by side. 35

The expansion into non-food items has resulted in six of Tesco's thirty distribution centres being dedicated to non-food and clothing.

Now that Tesco is established in the non-food sector, the company is considering opening some completely non-food stores. These stores are likely to sell a wide variety of products including clothes, electrical goods, CDs and DVDs. Tim Mason, Tesco's Marketing Director, thinks it is 'too big an opportunity to ignore'. Indeed Asda has already entered this format with its non-food stores Asda Living and its dedicated clothes stores called George. 40

### Criticism of Tesco

In a relatively short period of time, Tesco has revolutionised the retail industry within the UK. The company has brought product value and convenience to its customers but it has certainly attracted criticism from some quarters. 45

The Competition Commission is currently reviewing the land bank that Tesco has acquired. The company has a large unused property portfolio which is preventing smaller companies and potential competition from developing new stores because it owns 55% of the available land with development potential. The iconic YouTube features a well-made spoof of Tesco creating a retail country. Some recent newspaper headlines have included 'Tesco land bank is threatened in probe' (*Daily Mail*, 1/07) and 'Do shoppers want Tesco tamed?' (*Guardian* online, 10/06) 50

Some suppliers to Tesco have complained that their margins are being squeezed by Tesco's desire to force down the prices it pays. In addition, the ability of Tesco to sell £3 value jeans has raised issues about the working conditions involved in their production. 55

In response, Tesco is keen to point out that it takes its corporate responsibilities seriously. The main website for the company has an entire section devoted to this topic. It covers four key areas: the economy, environment, society, and charities and fundraising.

**UK supermarkets data****Table 1: Current Ratios for the major supermarkets: 2005**

Tesco	?
Morrisons	0.41
Sainsbury's	0.85
Waitrose	0.22
Somerfield	0.75

**Table 2: Profitability ratios (Return on capital employed %) 2005**

Tesco	?
Morrisons	5.34
Sainsbury's	0.23
Somerfield	5.42
Waitrose	13.85

(Asda-Wal-Mart figures are not available)

**Table 3: Supermarket UK market share (%) 29/01/06**

Tesco	30.6
Asda	16.6
Sainsbury's	16.3
Morrisons	11.1
Somerfield	5.4
Waitrose	3.7
Iceland	1.8

***Tesco's growth 2001–2005*****Table 4: Turnover (£bn)**

2001	21.0
2002	23.7
2003	26.3
2004	30.8
2005	34.0

**Table 5: Net Assets (£bn)**

2001	4.5
2002	8.6
2003	10.2
2004	12.0
2005	13.3

Table 6

<b>Balance Sheet: Tesco PLC £m</b>	<b>Feb 05</b>	<b>Feb 04</b>
<b>Assets</b>		
<b>Current Assets</b>		
<b>Cash</b>	799.7	670.2
<b>Net Receivables</b>	1 001.7	840.3
<b>Inventories</b>	1 308.6	1 199.4
<b>Other Current Assets</b>	345.9	430.2
<b>Total Current Assets</b>	3 455.9	3 140.2
<b>Net Fixed Assets</b>	15 490.0	14 099.2
<b>Other Non current Assets</b>	1 457.5	1 329.5
<b>Total Assets</b>	20 403.4	18 568.8
<b>Liabilities and Shareholders' Equity</b>		
<b>Current Liabilities</b>		
<b>Accounts Payable</b>	2 818.1	2 434.9
<b>Short-Term Debt</b>	476.8	844.3
<b>Other Current Liabilities</b>	2 775.1	2 340.9
<b>Total Current Liabilities</b>	6 070.0	5 620.1
<b>Long-Term Debt</b>	4 529.5	4 369.6
<b>Other Non current Liabilities</b>	749.8	631.2
<b>Total Liabilities</b>	11 349.3	10 620.9
<b>Shareholders' Equity</b>		
<b>Preferred Stock Equity</b>	0.0	0.0
<b>Common Stock Equity</b>	9 054.1	7 947.9
<b>Total Equity</b>	9 054.1	7 947.9
<b>Shares Outstanding (mil.)</b>	--	--

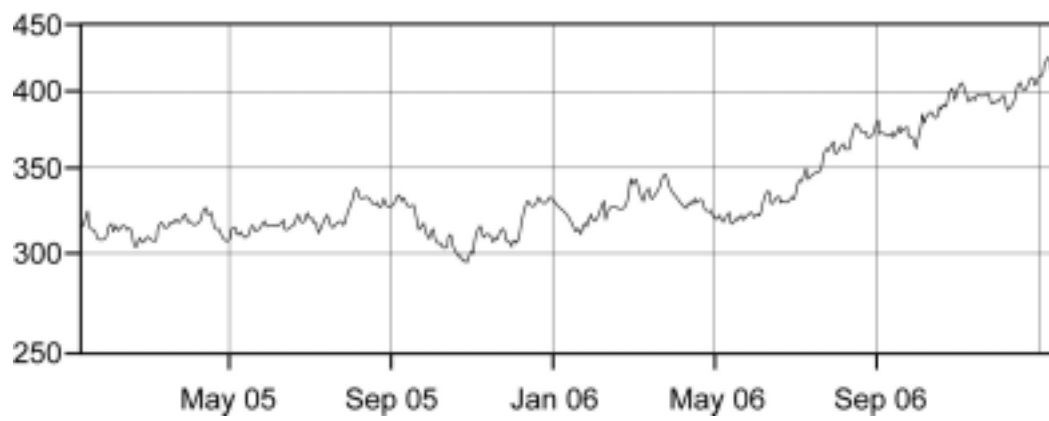


Table 7

<b>Profit and Loss Account: Tesco PLC £m</b>	<b>Feb 05</b>	<b>Feb 04</b>
<b>Revenue</b>	33 963.1	30 825.3
<b>Cost of Goods Sold</b>	31 834.8	28 935.6
<b>Gross Profit</b>	2 128.3	1 889.7
<b>Gross Profit Margin</b>	6.3%	6.1%
<b>SG and A Expense</b>	179.9	154.1
<b>Depreciation and Amortization</b>	62.0	52.0
<b>Operating Income</b>	1 948.4	1 735.6
<b>Operating Margin</b>	5.7%	5.6%
<b>Non operating Income</b>	302.9	--
<b>Non operating Expenses</b>	289.9	135.0
<b>Income Before Taxes</b>	1 961.4	1 600.6
<b>Income Taxes</b>	592.8	498.2
<b>Net Income After Taxes</b>	1 368.6	1 102.4
<b>Continuing Operations</b>	1 368.6	1 102.4
<b>Discontinued Operations</b>	0.0	0.0
<b>Total Operations</b>	1 368.6	1 102.4
<b>Total Net Income</b>	1 365.6	1 100.4
<b>Net Profit Margin</b>	4.0%	3.6%

Fig. 1

Tesco share price 418.5p: as at January 2007



**Read all the case study material and then answer all the following questions.**

**Section 1**

- 1** Using the financial statements information as at February 2005:
- (a)** Calculate the Acid Test ratio. [3]
  - (b)** Calculate the Inventory Turnover ratio (expressed in days). [3]
  - (c)** Comment on the value of the Acid Test and Inventory Turnover ratios for Tesco. [6]
  - (d)** Analyse Tesco's performance from a shareholder's point of view. [13]

**Section 2**

- 2** Recommend whether Tesco should embark on a strategy to open non-food stores. [25]
- 3** Evaluate the extent to which a significant increase in UK interest rates might affect the strategic decisions of Tesco. [25]
- 4** Discuss how Tesco could maintain its competitiveness, while fulfilling its corporate social responsibilities. [25]

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UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS  
Cambridge International Level 3 Pre-U Certificate  
Principal Subject

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**BUSINESS AND MANAGEMENT**

**9771/02**

Paper 2 Strategic Decisions

SPECIMEN MARK SCHEME

**3 hours**

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**MAXIMUM MARK: 100**

Alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

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UNIVERSITY of CAMBRIDGE  
International Examinations

## Section 1

## 1 Using the financial statements information as at February 2005:

(a) Calculate the Acid Test ratio. [3]

Acid Test ratio 0.35 [1]

$$\frac{\text{Current assets} - \text{stock}}{\text{Current liabilities}}$$
 [1]

Current assets – stock  
3 455.9 – 1 308.6 [1]

Current liabilities  
6 070.0 [1]

[3 marks for correct answer only]

(b) Calculate the Inventory Turnover ratio (expressed in days). [3]

Inventory Turnover 15 days [1]

$$\frac{\text{Inventory}}{\text{Cost of sales}} \times 365$$
 [1]

Inventory/Inventories  
1 308.6 [1]

Cost of sales  
31 834.8 [1]

[3 marks for correct answer only]

(c) Comment on the value of the Acid Test and Inventory Turnover ratios for Tesco. [6]

	Knowledge AO1 2 marks	Application AO2 4 marks
<b>Level 2</b>	<b>2 marks</b> Candidate shows knowledge of both of the ratios	<b>3–4 marks</b> Candidate comments on both ratios using clear case context
<b>Level 1</b>	<b>1 mark</b> Candidate shows knowledge of one of the ratios	<b>1–2 marks</b> Candidate comments on the value of one of the ratios using case context

- Acid Test 0.35
- Seen in isolation it could hint at liquidity problems.
- 0.35 is unsurprising given Tesco is in the retail sector.
- Tesco can easily sell its stock.
- 0.35 means Tesco could pay 35% of its current liabilities, even if it could not sell its stock.
- Inventory turnover 15 days
- The entire inventory is on average sold and replaced every 15 days.
- This is a low ratio and favourable.
- Tesco has a well-planned and effective inventory control policy.

(d) Analyse Tesco's performance from a shareholder's point of view.

[13]

	<b>Knowledge AO1</b> <b>2 marks</b>	<b>Application AO2</b> <b>5 marks</b>	<b>Analysis AO3</b> <b>6 marks</b>
<b>Level 3</b>		<b>5 marks</b> Candidate fully engages with the case context	<b>5–6 marks</b> Candidate fully develops analytical points
<b>Level 2</b>	<b>2 marks</b> Candidate identifies example(s) of shareholders	<b>3–4 marks</b> Candidate links case material to his answer	<b>3–4 marks</b> Reasonable analysis of arguments
<b>Level 1</b>	<b>1 mark</b> Candidate offers a sufficient definition of a shareholder	<b>1–2 marks</b> Candidate makes a limited attempt to apply knowledge of shareholders to the case study	<b>1–2 marks</b> Limited analysis of ideas, failure to develop points

- Ratios are industry specific, relative performance is important (retail).
- Depends on the trend of the ratios over time.
- Ratios are only one of many tools available.
- Profits, dividends and share price (see share price graph).
- Buy or sell.
- AGM voting decisions.
- Depends on who the shareholder is: fund manager v. private investor.
- £2 billion profit.
- Market leader, highest market share.
- Tesco share price v. sector and general market average.
- ARA



## Section 2

## 2 Recommend whether Tesco should embark on a strategy to open non-food stores. [25]

	<b>Knowledge AO1</b> 3 marks	<b>Application AO2</b> 6 marks	<b>Analysis AO3</b> 8 marks
<b>Level 3</b>		<b>5–6 marks</b> Arguments are consistently based upon case context	<b>7–8 marks</b> Candidate fully develops analytical points
<b>Level 2</b>	<b>2–3 marks</b> Candidate shows relevant knowledge and some understanding	<b>3–4 marks</b> Candidate makes good attempt to apply knowledge to the specific case scenario	<b>4–6 marks</b> Reasonable analysis of arguments
<b>Level 1</b>	<b>1 mark</b> Candidate shows some knowledge of a strategy	<b>1–2 marks</b> Candidate makes very limited attempt to apply knowledge to the specific case study	<b>1–3 marks</b> Some analysis of the issues with regard to the opening of non-food stores

	<b>Evaluation Descriptor AO4</b>	<b>Marks</b>
<b>High</b>	Candidate achieves an overall judgement with fully supported reasoning. Coherent conclusions are supported using appropriate case context, theories and concepts, and data. The quality of written communication is generally very good.	<b>5–8</b>
<b>Mid</b>	Candidate achieves an overall judgement having shown some supported reasoning. Generally coherent conclusions are supported with some supporting evidence. The quality of written communication is generally good.	<b>3–4</b>
<b>Low</b>	Candidate offers a largely unsupported judgement. The judgement is barely supported with relevant evidence. The quality of written communication is generally satisfactory.	<b>1–2</b>

- Respond to Asda.
- High growth market.
- Available land bank.
- Already got valuable experience.
- Increased bulk purchase economies.
- Already expanding rapidly.
- Competition commission investigation.
- New competitors apart from the supermarkets.
- Higher interest rates could hit non-food sector.
- Increased negative perception that Tesco is too dominant.

- Diversification (Ansoff Matrix).
- Lack of first mover advantage.
- Possibility of a trial store.
- Potential diseconomies of over-expansion.
- ARA
- Evaluation could include: A supported decision to go ahead with the strategy, reject the strategy, small-scale venture to judge potential, success would depend to a large extent on external factors such as the state of the economy or competitor actions, likely chance of success with assumptions, further information required to make an informed decision.

**3 Evaluate the extent to which a significant increase in UK interest rates might affect the strategic decisions of Tesco. [25]**

	<b>Knowledge AO1 3 marks</b>	<b>Application AO2 6 marks</b>	<b>Analysis AO3 8 marks</b>
<b>Level 3</b>		<b>5–6 marks</b> Arguments are consistently based upon case context	<b>7–8 marks</b> Candidate fully develops analytical points
<b>Level 2</b>	<b>2–3 marks</b> Candidate shows relevant knowledge and some understanding	<b>3–4 marks</b> Candidate makes good attempt to apply knowledge to the specific case scenario	<b>4–6 marks</b> Reasonable analysis of arguments
<b>Level 1</b>	<b>1 mark</b> Candidate shows some knowledge of a strategy	<b>1–2 marks</b> Candidate makes very limited attempt to apply knowledge to the specific case study	<b>1–3 marks</b> Some analysis of the issues with regard to the opening of non-food stores

	<b>Evaluation Descriptor AO4</b>	<b>Marks</b>
<b>High</b>	Candidate achieves an overall judgement with fully supported reasoning. Coherent conclusions are supported using appropriate case context, theories and concepts, and data. The quality of written communication is generally very good.	<b>5–8</b>
<b>Mid</b>	Candidate achieves an overall judgement having shown some supported reasoning. Generally coherent conclusions are supported with some supporting evidence. The quality of written communication is generally good.	<b>3–4</b>
<b>Low</b>	Candidate offers a largely unsupported judgement. The judgement is barely supported with relevant evidence. The quality of written communication is generally satisfactory.	<b>1–2</b>

- How large is the interest rate increase?
- What is the trend movement in interest rates?
- What is the current interest rate in its historic context?
- How much debt have consumers taken on?
- Different goods will face differing threats from an increase in interest rates.
- Should they stop the specific non-food stores expansion?
- How much debt does Tesco have?
- Gearing ratio.
- Perhaps Tesco could focus on its 'value' ranges.
- Imported goods could become cheaper and vice versa for exports.
- Could focus expansion on overseas stores.
- Reduce stock levels.
- Wage increase pressure. Wage–price spiral.
- ARA
- Evaluation could include: The parameters of the interest rate change such as size, time span, comparison with long-term trend, movements in overseas interest rates relative to the UK, the general outlook for the economy, interest rate sensitivity of Tesco's various current/potential markets, the exposure of consumers to interest rate changes, net savers/borrowers, fixed v. variable rate loan exposure, strategic decisions based upon quantitative/qualitative data from the case study. The balance of any interest rate change on Tesco as a company such as gearing and Tesco as a provider of goods and services to consumers.

**4 Discuss how Tesco could maintain its competitiveness, while fulfilling its corporate social responsibilities. [25]**

	<b>Knowledge AO1 3 marks</b>	<b>Application AO2 6 marks</b>	<b>Analysis AO3 8 marks</b>
<b>Level 3</b>		<b>5–6 marks</b> Arguments are consistently based upon case context	<b>7–8 marks</b> Candidate fully develops analytical points
<b>Level 2</b>	<b>2–3 marks</b> Candidate shows relevant knowledge and some understanding	<b>3–4 marks</b> Candidate makes good attempt to apply knowledge to the specific case scenario	<b>4–6 marks</b> Reasonable analysis of arguments
<b>Level 1</b>	<b>1 mark</b> Candidate shows some knowledge of a strategy	<b>1–2 marks</b> Candidate makes very limited attempt to apply knowledge to the specific case scenario	<b>1–3 marks</b> Some analysis of the issues with regard to the opening of non-food stores

	<b>Evaluation Descriptor AO4</b>	<b>Marks</b>
<b>High</b>	Candidate achieves an overall judgement with fully supported reasoning. Coherent conclusions are supported using appropriate case context, theories and concepts, and data. The quality of written communication is generally very good.	<b>5–8</b>
<b>Mid</b>	Candidate achieves an overall judgement having shown some supported reasoning. Generally coherent conclusions are supported with some supporting evidence. The quality of written communication is generally good.	<b>3–4</b>
<b>Low</b>	Candidate offers a largely unsupported judgement. The judgement is barely supported with relevant evidence. The quality of written communication is generally satisfactory.	<b>1–2</b>

- Corporate social responsibility could look at the economy, environment, society, and charities and fundraising.
- Ultimately consumers will decide as competition in retail is fierce.
- What are its corporate social responsibilities?
- Shareholder pressure.
- Maintaining competitiveness and achieving corporate social responsibility by stocking Fairtrade and organic products.
- Employing 450 000 people.
- Disregard for suppliers by exerting pressure on prices (£3 jeans).
- Reducing packaging reduces costs but also attracts the green pound.
- Minimising the use of plastic shopping bags saves on costs and is seen as environmentally friendly.
- Source more local products.
- Corporate social responsibility can go hand-in-hand with competitiveness as consumer tastes change and people are prepared to pay a premium price for ethical products.
- ARA
- Evaluation could include: The interdependence between corporate social responsibility and social consumer decisions, ultimately it may be difficult to achieve both and thus reference to balance should be rewarded, management of corporate image becomes more important.

Question	Knowledge	Application	Analysis	Evaluation	Total
<b>Section 1</b>					
<b>Q1a</b>	3				3
<b>Q1b</b>	3				3
<b>Q1c</b>	2	4			6
<b>Q1d</b>	2	5	6		13
<b>Section 2</b>					
<b>Q2</b>	3	6	8	8	25
<b>Q3</b>	3	6	8	8	25
<b>Q4</b>	3	6	8	8	25
<b>Total</b>	19	27	30	24	100

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