Business management
Standard level
Paper 2

Friday 29 May 2023 (morning)

1 hour 30 minutes

Instructions to candidates

- Do not open this examination paper until instructed to do so.
- A clean copy of the **business management formulae sheet** is required for this examination paper.
- Section A: answer two question.
- Section B: answer one question.
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- A calculator is required for this examination paper.
- The maximum mark for this examination paper is **[40 marks]**.

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Section A

Answer **one** question from this section.

1. Small-Scale Hobbies (SSH)

Scale Airplane Modeller is a magazine produced by *Small-Scale Hobbies* (*SSH*). The company sells the magazine through independent retail outlets in the US.

The finance director produced a summary of 2018's financial information. Last year's break-even chart showed that *SSH* had a margin of safety of 20 000 units.

Table 1: Selected financial data for *SSH* for 2018:

Annual fixed costs	$100 000
Variable costs per magazine produced	$2
Magazine price	$4.50

This year, to reduce costs and to increase sales, the company will introduce new production methods, which will reduce:
- unit variable costs by 10 %
- fixed costs by $5000 per year.

(a) Define the term *margin of safety*. [2]

(b) Using the financial data in **Table 1**, calculate:

(i) the break-even level of output (*show all your working*); [2]

(ii) the percentage of total costs that were fixed costs for last year (*show all your working*); [2]

(iii) the level of profit for *SSH* at 2018's level of production (*show all your working*). [2]

(c) Explain how the introduction of new production methods will affect the total cost line in *SSH*'s break-even chart. [2]

2. **Daytona Go-Carts**

[Source: https://www.pexels.com]

In 2020, Ron James aims to open *Daytona Go-Carts*, a race track where individuals as young as twelve can rent go-carts and participate in races. Through primary market research, Ron has discovered that many teenagers would enjoy participating in go-cart races.

Ron has two options for locations for the go-cart race track:

- **Option 1**: The cost of the site would be $1.2 million
- **Option 2**: The cost of the site would be $1.8 million.

Forecasted profits for **Option 1** are:

Year 1	Year 2	Year 3	Year 4	Year 5
$200 000	$300 000	$300 000	$300 000	$300 000

Forecasted profits for **Option 2** are $300 000 in the first year, with profits growing by 20 % per year for the next four years.

(a) State **two** methods of primary market research. [2]

(b) Calculate, for **Option 1**:

(i) the average rate of return (ARR) (*show all your working*); [2]

(ii) the payback period (*show all your working*). [2]

(c) Calculate, for **Option 2**, the average rate of return (ARR) (*show all your working*). [2]

(d) Explain **one** reason why **Option 1** may be a less risky investment than **Option 2**. [2]

Section B

Answer **one** question from this section.

3. Top Star (TS)

Top Star (*TS*) manufactures sports footwear. Its products are sold through retail outlets and online. Sales of *TS'* footwear in retail outlets are falling. However, because e-commerce is growing rapidly, online sales are increasing. In 2018, *TS'* total domestic sales were $5 000 000 and total domestic market sales for the same time period were $50 000 000.

TS must consider several challenges:

- Some businesses in the sports footwear industry are finding that selling online leads to many problems and higher costs
- *TS'* website is not user friendly. Customer complaints about the website and ordering problems are increasing
- *TS'* presence in international markets is weak and its product range is limited. The directors of *TS* want to develop a new line of running shoes but the company has insufficient finance for research, development and creating brand awareness.

The directors think that *TS* should follow an external growth strategy. Two options are being considered:

- **Option 1**: Some directors propose a merger with a footwear manufacturer, the multinational company *All Champion,* which would allow *TS* to be more competitive
- **Option 2**: Other directors propose a merger with a footwear retailer that has a strong presence in domestic and international markets.

The finance manager believes that merging with *All Champion* could hurt *TS*' reputation. *TS'* factories may have to close, which the local population may resent.

(a) Describe **one** feature of a multinational company (MNC). [2]

(b) Calculate *TS'* market share in 2018 (*show all your working*). [2]

(c) Explain **two** disadvantages **and one** advantage to *TS* of selling its products online. [6]

(d) With reference to *TS*, evaluate the two merger options. [10]