

Business Studies

Advanced GCE

Unit **F297**: Strategic Management

Mark Scheme for January 2012

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All examiners are instructed that alternative correct answers and unexpected approaches in candidates' scripts must be given marks that fairly reflect the relevant knowledge and skills demonstrated.

Mark schemes should be read in conjunction with the published question papers and the report on the examination.

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Annotations

Annotation	Meaning
	Unclear
	Benefit of doubt
	Cross
	Level 1
	Level 2
	Level 3
	Level 4
	Not answered question
	No use of text
	Own figure rule
	Repetition
	Noted but no credit given
	Too vague
	Tick

Subject-specific Marking Instructions

General

- The paper is to be marked to A2 standard.
- Marking should be positive; marks should not be subtracted for errors or inaccuracies.
- Candidates should be regarded as achieving the highest level of response which accurately describes their answer. They do not necessarily have to pass through all lower levels of response.
- In assessing quantitative answers the “own figure rule” (OFR) must be applied, i.e. a candidate must be given credit for calculations which, though wrong, are consistent with an earlier error.
- Materials in italics below refer to possible issues/ content that candidates might use. These suggestions are neither exhaustive nor necessarily required.
- The emphasis throughout this paper should be upon the integration of the material learnt and the context described within the stimulus material. Candidates are expected to treat both in a synoptic manner, considering situations from a variety of perspectives rather than a series of discrete issues by adopting a holistic/ multi-disciplinary approach.

Question	Answer	Marks	Guidance																																														
1	<p>(a) For the time period Feb 2011 to Jan 2012 Actual sales = £1,304 + £1,242 + £1,376 + £1,325 = £5,247 Gross profit = £516.3 + £478.9 + £522.8 + £498.7 = £2,016.7</p> <p>Operating profit = £119.6 + £105.7 + £118.6 + £110.0 = £453.9 Net profit = £115.1 + £101.4 + £114.3 + £105.9 = £436.7</p> <p>Answers derived from Q1 November 2011- January 2012 ROCE=9.07% ROE = 10.46% GPM =37.64% NPM = 7.99%</p> <table border="1" data-bbox="324 598 1220 1252"> <thead> <tr> <th>Ratio</th> <th>Formula</th> <th>Data</th> <th>Outcome</th> </tr> </thead> <tbody> <tr> <td rowspan="2">Return on Capital Employed</td> <td>$\frac{\text{PBIT}}{\text{CE}} \times 100\%$</td> <td>$\frac{453.9}{1,212} \times 100$</td> <td>37.45%</td> </tr> <tr> <td>$\frac{\text{NP}}{\text{CE}} \times 100\%$</td> <td>$\frac{436.7}{1,212} \times 100$</td> <td>36.03%</td> </tr> <tr> <td>Return on Equity</td> <td>$\frac{\text{NP}}{\text{Equity}} \times 100\%$</td> <td>$\frac{436.7}{1,012} \times 100$</td> <td>43.15%</td> </tr> <tr> <td>Gross profit margin</td> <td>$\frac{\text{Gross profit}}{\text{Sales}} \times 100\%$</td> <td>$\frac{2,016.7}{5,247.0} \times 100$</td> <td>38.44%</td> </tr> <tr> <td rowspan="2">Net profit margin</td> <td>$\frac{\text{PBIT}}{\text{Sales}} \times 100\%$</td> <td>$\frac{453.9}{5,247.0} \times 100$</td> <td>8.65%</td> </tr> <tr> <td>$\frac{\text{NP}}{\text{Sales}} \times 100\%$</td> <td>$\frac{436.7}{5,247.0} \times 100$</td> <td>8.32%</td> </tr> </tbody> </table>	Ratio	Formula	Data	Outcome	Return on Capital Employed	$\frac{\text{PBIT}}{\text{CE}} \times 100\%$	$\frac{453.9}{1,212} \times 100$	37.45%	$\frac{\text{NP}}{\text{CE}} \times 100\%$	$\frac{436.7}{1,212} \times 100$	36.03%	Return on Equity	$\frac{\text{NP}}{\text{Equity}} \times 100\%$	$\frac{436.7}{1,012} \times 100$	43.15%	Gross profit margin	$\frac{\text{Gross profit}}{\text{Sales}} \times 100\%$	$\frac{2,016.7}{5,247.0} \times 100$	38.44%	Net profit margin	$\frac{\text{PBIT}}{\text{Sales}} \times 100\%$	$\frac{453.9}{5,247.0} \times 100$	8.65%	$\frac{\text{NP}}{\text{Sales}} \times 100\%$	$\frac{436.7}{5,247.0} \times 100$	8.32%	13	<p>Levels of response NB. Remember to apply the own figure rule. NB. Accept either version of ROCE (RONA) and NPM on a consistent basis NB Do not ‘double count’, i.e. reward two versions of ROCE or NPM</p> <table border="1" data-bbox="1377 438 2060 853"> <thead> <tr> <th></th> <th>ROCE</th> <th>ROE</th> <th>GPM</th> <th>NPM</th> </tr> </thead> <tbody> <tr> <td>3 Analysis Correct value, including percentage sign</td> <td>2</td> <td>1</td> <td>1</td> <td>1</td> </tr> <tr> <td>2 Application Attempts to use the case data to calculate ratio(s), including percentage sign</td> <td>1</td> <td>1</td> <td>1</td> <td>1</td> </tr> <tr> <td>1 Knowledge Name or formula of ratio(s)</td> <td>1</td> <td>1</td> <td>1</td> <td>1</td> </tr> </tbody> </table> <p>Correct ROCE = 4 marks 37.45% or 36.03% either is correct. Correct ROE = 3 marks 43.15% Correct GPM = 3 marks 38.44% Correct NPM= 3 marks 8.65% or 8.32% either is correct All four correct, 13 marks Name of ratio and correct answer with no supporting method (formula or case data) = full marks Name of ratio but wrong answer with correct case data but a subsequent arithmetic error = 2 marks Name of ratio but wrong answer with incorrect case data = 1 mark Name of ratio but wrong answer and no supporting method (formula or case data) = 1 mark</p>		ROCE	ROE	GPM	NPM	3 Analysis Correct value, including percentage sign	2	1	1	1	2 Application Attempts to use the case data to calculate ratio(s), including percentage sign	1	1	1	1	1 Knowledge Name or formula of ratio(s)	1	1	1	1
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1 (b)	<p><i>NB. The question is about profitability, not profits. The better candidates will distinguish between margins and profits, either implicitly or explicitly. Further, it requires a <u>strategy</u> and so a series of unconnected ideas does not meet this stipulation</i></p> <p><i>Profit margin figures show a decline through time. In essence, the firm has to either increase revenues whilst maintaining costs, or decrease costs whilst maintaining revenues.</i></p> <p><i>Every quarter the business incurs actual interest charges above its budgeted interest payments. As the firm has constant debt (assuming that the gearing ratio of 16.5% remains constant) this must be due to an ad hoc overdraft. From the balance sheet we can see the CR is 1.36 and the AT is 0.72, so liquidity is fine, so might the firm need to call on an overdraft from time to time to even out cash flow. If so, investigate ways of delaying creditor payments or speeding up debtor collection.</i></p> <p><i>From Table 1, margin on feed is budgeted to be 40% (but comes in at 39% and 41%). Similarly, for non-feed the budget margin is 50% and it comes in at 49%, 49% and 50%. So, to boost profitability focus marketing effort on non-feed items.</i></p> <p><i>If LCTL could get their days debtors closer in line with industry average that would help cash flow and so possibly negate the need for short term borrowing, in turn reducing the interest payments and so boosting profits. But do what extent can a business with barely 5% market share pressures it customers without losing them? NB Change in values when compared to 2010 (see table 2)</i></p> <p style="text-align: center;">4</p>	18	<p style="text-align: center;">Levels of response</p> <p>Level 4: 18-12 marks Candidate demonstrates evaluative skills when recommending a strategy as to how the business might best increase its profitability.</p> <p>Level 3: 11-8 marks Candidate demonstrates analytical skills when considering possible method(s) of increasing profitability.</p> <p>Level 2: 7-4 marks Candidate demonstrates knowledge and understanding when considering method(s) of increasing profitability. No context is required.</p> <p>Level 1: 3-1 marks Candidate offers only theoretical knowledge of profitability/profit.</p> <p>The validity of choice determined by the synthesis of case and subject. There is no single strategy possible in this situation so the mark will reflect the skill shown in putting forward the proposal.</p> <p>“Increase profitability” might be questioned – by how much and over what time period?</p> <p>Similarly, which measure of these four measures of profitability is the priority?</p> <p>Using the same set of data then Days debtors = 103.3 days Days stock = 111.8 days</p>

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2	<p>Yes</p> <ul style="list-style-type: none"> • <i>Profitable- see Q1a, npm 9.2% comparative base; last year, industry average (Table 2) so better than last year but still below the industry average</i> • <i>50% dividends so shareholder wanting income will be pleased and see the business as a success</i> • <i>ROE and ROCE, 11.4% and 9.9% - but doe these figures exceed the opportunity cost, so really need some comparative base; last year, industry average (Table 2) bank base rates</i> • <i>Growth in sales suggests suppliers see it as profitable, although Table 1 does show variation in budgeted sales, but this is most likely to be due to seasonality rather than part of a longer term annualised trend.</i> • <i>Liquidity, Days debtors, Days creditors</i> • <i>Provides a product range customers want – allocative efficiency</i> • <i>Provides jobs – multiplier- but what is the nature of those jobs, are they satisfying? What objectives do the employees have? Is it simply financial or also intrinsic challenge, so success will likely vary across employees. Evidence in the case that LCTL is a good place to work, boss shares success with a celebratory team day-out.</i> • <i>External accolades/ awards will suggest the business is successful to both internal and external stakeholders. Many in the community will know very little about LCTL other than what they read in the press, so positive stories would build an image of success.</i> • <i>Attractive to external takeover, an acquisitive firm would be more likely to want to take over a business which is successful, or at least has the ability to be successful</i> 	18	<p style="text-align: center;">Levels of response</p> <p>Level 4: 18-12 marks Candidate demonstrates evaluative skills when considering the success of the business in balancing different possibilities.</p> <p>Level 3: 11-8 marks Candidate demonstrates analytical skills when considering the possible success of LCTL.</p> <p>Level 2: 7-4 marks Candidate demonstrates knowledge and understanding when considering business success. No context required.</p> <p>Level 1: 3-1 marks Candidate offers only theoretical knowledge of business success</p> <p><i>How is success measured, and who measures it?</i></p> <p><i>Candidates may well take a stakeholder view as a framework to argue that for some stakeholders, given their success criteria, the business is/ is not successful.</i></p> <p><i>Candidates will seek to assess success against objectives, either those explicitly in the case or reasonably assumed objectives, e.g. community would have the objective of the business providing employment without excessive intrusion.</i></p>

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	<p>No</p> <ul style="list-style-type: none">• <i>Ethical story in the press might make some stakeholders feel this is not a successful business. But note, the story is in a local paper yet LCTL has a national customer base, so any response to the story is likely not to travel far unless picked up by national media, and then we move from LCTL to the industry. Business only exists to sell a product consumers are willing to pay for, and presumably most consumers can reconcile their ethical beliefs between humans and birds.</i>• <i>Community concerns about operational impact</i>		

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3	<p><i>SWOT, is an analytical framework that can be used to diagnose a business' current position. Knowing where you are is an essential first step in setting strategy, but whether it can be used to set objectives is an altogether different matter. It can though help to identify external opportunities that could be exploitable, and as such inform objectives.</i></p> <p><i>Here the SWOT has been constructed internally. How objective is it? If done by Lucy she may be too close and emotionally bound to the issues to see the reality, particularly given the nature of the size and ownership/ control. So, this SWOT may not be that useful. Far better have it conducted by a neutral external party (but that costs money so possibly get Alana to do it with some of the prize money just gained). But isn't a SWOT is better than no SWOT? Although possibly flawed it will cause Lucy and her business adviser to diagnostically think about the business, and indeed spark debate at the annual general meeting. As such, it might be a catalyst to discussion and so useful for what it sparks rather than what it actually is. So, could well be useful providing it is used as a starting point.</i></p> <p><i>Objectives</i> <i>Non-food products contributing 25% of sales by 2012.</i> <i>Annual revenue growth of 8% for the next five years.</i></p> <p><i>By 2017:</i> <i>Gross profit margin 45%</i> <i>Net profit margin 12.5%</i> <i>Return on capital employed 42%</i> <i>Return on equity 55%</i></p>	18	<p align="center">Levels of response</p> <p>Level 4: 18-12 marks Candidate demonstrates evaluative skills when considering benefits/ limitations of using LCTL's SWOT analysis to set objectives.</p> <p>Level 3: 11-8 marks Candidate Case material is subject to analysis in considering how LCTL's SWOT analysis can assist the setting of objectives.</p> <p>Level 2: 7-4 marks Candidate demonstrates knowledge and understanding of a SWOT analysis and/or objectives. No context required.</p> <p>Level 1: 3-1 marks Candidate offers only theoretical knowledge of SWOT analysis and / or objectives</p> <p>Good candidates will recognise the role SWOT can play in strategy and see it as being a means to an end, not an end in itself.</p>

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4	<p><i>Capacity is about to be reached. Do they need this order, what does it bring to the firm? Is it compatible with the aims and resources available?</i></p> <p><i>Other contribution/ special order issues are pertinent. But it also needs to be seen as what markets do they want to be in etc. Use of Ansoff (market development) and comparison of risk and reward – low risk and low reward. Impact on other customers, might walk away if OFF sell to PP? If so, it leaves a gaping hole on the order book. Is there enough spare capacity in the industry for these disgruntled customers to realise this threat? Conservatively, industry is worth £150m at retail, of which OFF have about £5m, or £10m at retail value. Mean that there are other firms currently producing £140m of retail sales. Do these other firms have spare capacity and so could take OFF's independent customers? OFF is 6.7% of the market, so it is realistic to assume that other firms could increase output to capture a slice of this. PP want 90 days credit, so sensible to consider any impact on cash flow and to compare 90 days to existing credit period offered to customers. The order is 25% of capacity. Is it sensible to have a single customer taking that amount of output? Strategic risk, what if they walk away given the contract is for a rolling 3 months. Order is for £0.2/ kg less than independent customers, so the profit margins on this order will be less. How does that fit with the profit margin objective? However, the size of the order does help meet the sales growth objective. Might PP then want other products, especially the higher margin non-food lines?</i></p> <p>If there is no recommendation, then award at bottom of the appropriate level.</p>	23	<p>Level 4: 23-17 marks Candidate demonstrates evaluative skills when considering whether LCTL should accept/reject the sales order from Price Pulveriser. Discussion is balanced in evaluating recommendation <i>Complex ideas have been expressed clearly and fluently using a style of writing appropriate to the complex subject matter. Sentences and paragraphs, consistently relevant, have been well structured, using appropriate technical terminology. There may be few, if any, errors of spelling, punctuation and grammar.</i></p> <p>Level 3: 16-11 marks Candidate demonstrates analytical skills when considering whether LCTL should accept/reject the sales order from Price Pulveriser. <i>Relatively straight forward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar, but these are unlikely to be intrusive or obscure meaning.</i></p> <p>Level 2: 10-5 marks Candidate demonstrates knowledge and understanding reasons to accept or reject a sale order. No context is required. <i>Some simple ideas have been expressed in an appropriate context. There are likely to be some errors of spelling, punctuation and grammar of which some may be noticeable and intrusive.</i></p> <p>Level 1: 4-1 marks Candidate offers only theoretical knowledge of reasons to accept/reject a sales order. <i>Some simple ideas have been expressed. There will be some errors of spelling, punctuation and grammar which will be noticeable and intrusive. Writing may also lack legibility.</i></p>

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