



**ADVANCED SUBSIDIARY GCE**  
**BUSINESS STUDIES**  
Business Functions

**F292/CS**

**CASE STUDY**

**Thursday 21 January 2010**  
**Afternoon**

**Duration: 2 hours**



**INSTRUCTIONS TO CANDIDATES**

- This is a clean copy of the case study which you should already have seen.
- You should refer to it when answering the examination questions which are printed in a separate booklet.
- You may **not** take your previous copy of the case study into the examination.
- You may not take notes into the examination.
- The business described in this Case Study is entirely fictitious.

**INFORMATION FOR CANDIDATES**

- This document consists of **8** pages. Any blank pages are indicated.

### Fitness is Fun plc (FIF)

One of the biggest growth areas in the UK leisure industry in the last 20 years has been fitness-related. Gym membership has mushroomed, with gym participation rates around 15% of the overall population. Timothy Busfield was one of the first to recognise the potential in the market and he set up Fitness is Fun (FIF) on a small budget in 1995. The business began by importing gym equipment from the USA and then installing it in the growing number of gyms and leisure centres. FIF grew quickly and was incorporated in 2001 to raise the necessary finance for a move into the production of the actual equipment. Timothy is Managing Director of the business. 5

FIF has been profitable for the last six years and employs a total of around 80 staff, all full-time. It has its sales and administrative office in Oxford; with a manufacturing site in Newbury, where roughly 70% of the equipment it sells is manufactured. The remaining 30% is bought from other producers in the USA and China, either as a finished item or in component form. FIF now has a strong position in the market but getting to this point has not been easy. Timothy has been concerned at the poor payment record of customers ever since he established the business. Managing cash flow and risk is a major problem. It is not unusual for a gym to order £20,000 of equipment without paying any deposit and Timothy is always relieved when a cheque finally arrives, sometimes well after the equipment has been installed. 10 15

The gym equipment that FIF sells is grouped into five categories: treadmills, step machines, rowing machines, exercise bikes and strength training machines. In each category there are a number of models available, with varying options. The most popular equipment continues to be treadmills, although they are becoming more and more complex. There is a range of models available from a large commercial heavy duty model to a smaller model which could be suitable for the office or home (see Table 1). 20

**Table 1 – Details of treadmills available from FIF (extract)**

Model	Features	List price	Variable cost*
Classic 760Z	<ul style="list-style-type: none"> <li>Innovative display and suspension technology</li> <li>Personal entertainment monitor with handset control</li> <li>Multi-programmable options</li> <li>Heart rate monitoring</li> </ul>	£2,300	£840
Pro 10+	<ul style="list-style-type: none"> <li>One touch quick start</li> <li>Heart rate monitoring</li> <li>Inclines up to 15%</li> </ul>	£1,200	£400
Sports 10+	<ul style="list-style-type: none"> <li>As Pro 10+ but with no incline ability</li> </ul>	£ 950	£350
Finesse SW3	<ul style="list-style-type: none"> <li>Small overall footprint</li> <li>Surprisingly large running surface</li> <li>Whisper quiet motor</li> <li>Personal entertainment upgrade option available</li> </ul>	£ 650	£300

\* Variable cost at current level of output

All FIF's treadmills are produced in its own factory and are unique to FIF. They are recognised as being some of the most innovative models in the market. FIF has an installation team of six people covering the whole of the UK and the price charged includes full installation and one year's maintenance and repair. The actual price charged can vary considerably from that published in the price list. FIF is always happy to negotiate the final price based on the size of the order and who is ordering. 25

Timothy is keen to retain established customers, as well as attracting new ones. One way of achieving this is to offer price discounts for loyalty and promotional purposes. The treadmill products are also often used as a form of loss-leader in encouraging buyers to purchase the higher contribution generating strength training equipment. Price setting is made even more complicated by the fact that material costs can vary considerably from month to month. Much of the steel and IT components used in the products are imported and are susceptible to dramatic variations in cost. 30

FIF, as part of its short- to medium-term business aims, currently has a target of doubling turnover in the next three to four years. At a recent tactical planning meeting, FIF's Marketing & Sales Director, Emily Proctor, put forward a plan to achieve this challenging target by moving into uncharted waters. 35

"Two market segments to which we do not currently sell are homes and schools," began Emily. "A lot of people are adding extensions to their homes and now have space to dedicate a room as a home gym. The growth in gym membership is beginning to level off and evidence suggests this is due to more and more people having insufficient time to physically go to the gym, along with a desire to cut down on car usage. But, there is still a wish to exercise and it is much easier to do it in the home, before or after work. This is, therefore, an area where we see potential for huge growth." 40

"What about other aspects of going to the gym? Don't a lot of the people see going to the gym as a chance to socialise as well?" asked Timothy. 45

"It seems to be less of an issue nowadays," replied Emily. "You also have to remember the huge cost of gym membership. It can cost as much as £1,600 a year to be a member. This puts many people off. If we can tempt them into a one-off payment to purchase a piece of equipment from us, maybe using a form of credit agreement, many more can afford to keep fit."

Timothy was also keen for the other directors to hear about the proposals for entering the schools market. This was something that Timothy and Emily had seen being done very successfully on a recent fact-finding trip to the USA. 50

Emily presented the facts about an innovative piece of exercise equipment made by an American exercise equipment producer. The 'CITX' (short for child IT exerciser) combines the attraction of a traditional video game with an exercise machine. Participants need to interact with the action on the video monitor and it is a clever way of getting children to exercise. 55

"This machine provides a powerful new experience that dramatically improves muscle and mental agility, while adding exciting new dimensions of fun and function to exercise. The CITX launches you into an interactive virtual world where reaction, acceleration, speed, power and balance drive on-screen activities. It's a unique and entertaining fitness experience that improves things such as spatial awareness, agility, strength, balance, reaction time and weight management. At the moment the machine is only available in America, but the makers are keen to move into Europe and have expressed a willingness to consider FIF as the sole UK distributor," said Emily enthusiastically. 60

"Just look at some of the recent publicity the machine has gained in the US," added Timothy (see Appendix 1). "These two market segments, homes and schools, although different from our current market, are exciting ideas for the business. They will give the business new impetus and help us to achieve further growth. I want this meeting to approve Emily's ideas so that she can then carry out further work on a plan to access these markets." 65

The rest of the Directors gave their unanimous agreement to Timothy and Emily's plan. Emily now knew that her marketing team had a lot of work to do before the next meeting to develop a marketing plan. 70

At FIF's Newbury factory, the main problem facing the Operations Director, Alyson Maloney, is the increasing amount of time and money being spent on reworking products rejected after the production process. The company's reject rates have typically been less than 2%, but in the last two years they have risen to nearly 10%. Alyson is meeting with the Production Manager, Hiro Arai, to discuss this growing problem. Hiro's main concern is with the new reject rate target that has been set by the Board at 6% by the end of 2010 and 3% by 2012 in order to reduce reworking. 75

"We are really asking for trouble with these new targets. There are too many issues to be resolved in such a short space of time, never mind the fact that expansion is also adding more pressures," started Hiro. "I cannot increase the number of quality checks without more quality supervisors. They are already making as many random checks as possible and the only way to increase them is by cutting down on the checks of finished products. I can't stretch the guys any further." 80

"I don't think we will be able to sanction any further expenditure on quality control staff in the immediate term, although I will raise it with the Board with a view to getting more employees within 18 months," replied Alyson. "What would you say are the main causes of this recent escalation of the reject rate?" 85

Hiro was ready for this question. "As I have repeatedly said over the last year or so, there are two basic and fundamental issues. One, the quality of some of the stock we are buying in from abroad is not consistent enough. Some of the components are badly made and not accurate enough. This then causes problems when it comes to putting the parts together and integrating them with our own parts. Second, frankly the standard of many of the recent workers we have employed is poor. They do not have the ability for, or interest in, what we are asking them to do. They just turn up and take the money. It's even affecting some of our more reliable, established workers. I had two of them in my office only last week moaning about some of the new recruits. It's affecting their workrate and they don't see why they should do things properly, if others are getting away with it." 90

"Well, we need to do something about this and quick," replied Alyson. "Whether you like it or not, we need to find a solution to this problem. We will both be judged on our ability to achieve the new reject rate targets that have been set." 95

A key part of FIF's recent success is the service that it offers. There are many other providers of gym equipment in the competitive UK market. However, a growing proportion of FIF's revenue and profits is being gained from follow-on services such as maintenance plans, financing and consulting services (see Table 2). 100

**Table 2 – Source of revenue and profit for FIF**

	Proportion of total revenue		Proportion of net profit	
	Sale of equipment	Follow-on services	Sale of equipment	Follow-on services
2006	71%	29%	51%	49%
2007	70%	30%	48%	52%
2008	66%	34%	45%	55%
2009*	62%	38%	40%	60%

\* Forecast figures

A favourite saying in the Marketing & Sales Department is: "Others may imitate the products we offer but a reputation for excellent service is very difficult to copy". As the UK economy becomes evermore service-centred, businesses are increasingly dependent on the quality of their customer relationships. It is, therefore, worrying for FIF that it has been having problems with its customer sales and service teams. Labour turnover in these teams has doubled in the last year, new maintenance contracts are down by 4% over the last two quarters and a number of regular service customers have moved to a competitor of FIF. 105

FIF has four regional sales and service teams which operate independently from each other. Each team has its own area of the UK which it covers, with the manager of each team reporting directly to Emily Proctor on a monthly basis. Other than on this occasion, the four teams have very little contact with each other. Queries from potential new and current customers are passed on to the relevant team which is then left to negotiate a deal with that customer on price and delivery. However, all deals must be finally approved by Emily or her assistant, which can sometimes take a week or two to obtain. The sales and service teams are paid a fixed salary, with the managers of each team awarded a quarterly bonus based on the value of contracts gained by their team. 110 115

Emily knows that the next meeting with the team managers could be difficult, as hard questions will need to be asked and changes made.

#### **Appendix 1 – Newspaper article about the CITX machine in the USA**

### **Electronic playground – the future of fitness?**

**Minnesota Monthly** (September 2009)

Staff at Carroll Valley YMCA are hoping that the same technology that has turned youngsters into couch potatoes can be used to make lean machines. A 'virtual gym' will be offered thanks to a federal grant.

A room in the YMCA building has been turned into a computerised play area which encourages youths to stimulate their bodies and minds with the help of popular video games. Each CITX machine offers a variety of interactive games that challenge the user to jump, shuffle, dodge or lunge in order to control a video game player with their motions.

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