



Oxford Cambridge and RSA

Monday 13 January 2020 – Morning

Level 3 Cambridge Technical in Business

05834/05835/05836/05837/05878 Unit 3: Business decisions

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INSTRUCTIONS

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INFORMATION

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- This document has **4** pages.

Yuletide Joy

The business

Yuletide Joy is a specialist retailer of Christmas-themed ornaments and decorations. It is located in a city in the North of England which is popular with tourists. The business is owned by Sonja Gorniak and her partner Henry Giles. Sonja and Henry met whilst they both worked for a bank. Sonja was an administrative manager and Henry was, and still is, an investment analyst. Sonja was made redundant in early 2017.

In August 2017 Sonja and Henry went to New York on holiday. There, they were amazed to find several Christmas-themed shops selling a range of Christmas-themed ornaments. Many of the ornaments had a New York-related theme, for example Father Christmas hugging the Empire State Building or a reindeer dressed as the Statue of Liberty. Sonja spoke to the shop assistant in one of these shops. The shop assistant told her that the shops were open throughout the year and were especially popular with tourists. Sonja learned, unsurprisingly, that the shop was at its busiest during November and December. Sonja then remembered that she had seen other, similar, shops open all year round in parts of Central Europe. Sonja wondered whether there would be a market for such shops in the UK.

In 2018 Henry attempted to persuade Sonja that her redundancy money provided the ideal opportunity to test her idea of a Christmas-themed shop in the UK. Henry instinctively believed that Sonja's idea was a good one. Sonja was less convinced. She was initially very reluctant to spend this money on an untested business idea. It was okay for Henry, Sonja thought, he enjoys his job because he gets to gamble with other people's money.

After much research, Sonja eventually decided to give the new business venture a try. The couple decided to use Sonja's redundancy money together with a bank loan, secured against some property owned by Henry's father, to fund the new venture.

Sonja identified vacant premises in the city which, although not located in the high street, were being offered for a relatively low-cost lease for a fixed five-year period. The shop opened in May 2019. Two part-time sales assistants are employed to work alongside Sonja. *Yuletide Joy* is owned jointly by Sonja and Henry. The items sold in the shop are sourced from suppliers in Europe and Asia.

Early days

Over the first six months of trading the shop was able to achieve a small profit. However, Henry is not convinced that profits from the shop will be enough to justify the amount that he and Sonja have invested in the business. The shop is located in a part of the city that is less well-frequented by tourists. As a result, revenue and profit is lower than it could be. Henry thinks that the business idea is sound and that reducing stock levels outside the busy Christmas period would prove beneficial.

Both partners agree that the business needs to expand to make it viable. Sonja, who is more cautious than Henry, wishes to expand the business slowly, partly because she is reluctant to keep investing money in the business without a guarantee of success.

The options

Henry is currently considering three expansion options for *Yuletide Joy*. Henry likes to act on his instincts and has not yet conducted any market research. The business has cash reserves of approximately £10 000. All of the options would involve keeping their current shop. Henry will discuss the options with Sonja so that they can decide jointly on how best to expand the business.

Option 1 – Diversify the product range

Option 1 is to widen the shop's focus by diversifying its product range to include other seasonal events such as Easter and Diwali. Henry thinks that this would improve the shop's revenue throughout the year. Henry believes that Sonja will be very reluctant to take this option as she is convinced that the business model depends on a strong association with Christmas. In addition, the name of the shop would need to be changed and Sonja might consider this an unacceptable risk.

Henry estimates that capital expenditure for this option would be approximately £25 000, primarily to cover the costs of rebranding the shop. This would be financed by using the business' cash reserves of £10 000 plus a variable rate bank loan of £15 000 over four years (initially a rate of 9%). Henry estimates that this option would have a payback period of approximately two and a quarter years, with an ARR of 36% over the first six years of trading.

Option 2 – Open a second shop

Option 2 is to maintain *Yuletide Joy's* focus on Christmas and open an additional Christmas-themed shop. Henry has identified another city in the North of England that is popular with tourists. Several sites are available, including some in shopping centres. Henry thinks that having the two shops would generate sufficient profit to justify his and Sonja's financial commitment to the business.

Henry estimates that capital expenditure for this option would be approximately £40 000, primarily to cover securing the lease and renovating the shop. Extra revenue expenditure would also be needed to employ a shop manager and three part-time sales assistants for the second shop and to purchase additional stock. The capital expenditure would be financed by using the business' cash reserves of £10 000 plus a variable rate bank loan of approximately £30 000 over four years (initially a rate of 7%). Henry estimates that this option would have a payback period of approximately three years, with an ARR of 22% over the first six years of trading.

Option 3 – Open an online store

Option 3 is to continue to run the current shop as is, adding a website for online sales. Henry thinks that opening an online store would represent a low-cost way to expand the business. A warehouse could be used to store stock and dispatch it directly to customers around the world. He has identified a small warehouse less than a mile from the current shop. Henry thinks that Sonja would be able to manage the warehouse herself, in addition to the shop.

Capital expenditure of £70 000 would be needed, £60 000 to secure the lease and convert the warehouse and £10 000 to build the website. Extra revenue expenditure would be needed to cover the purchase of additional stock, the employment of warehouse assistants and marketing costs to drive people to the website. The capital expenditure would be financed by using the business' cash reserves of £10 000 and a variable rate bank loan of approximately £60 000 over four years (initially a rate of 6%). Henry estimates that this option would have a payback period of approximately four years with an ARR of 12% over the first six years of trading.

Appendix A

Retail footfall takes a hit over Christmas

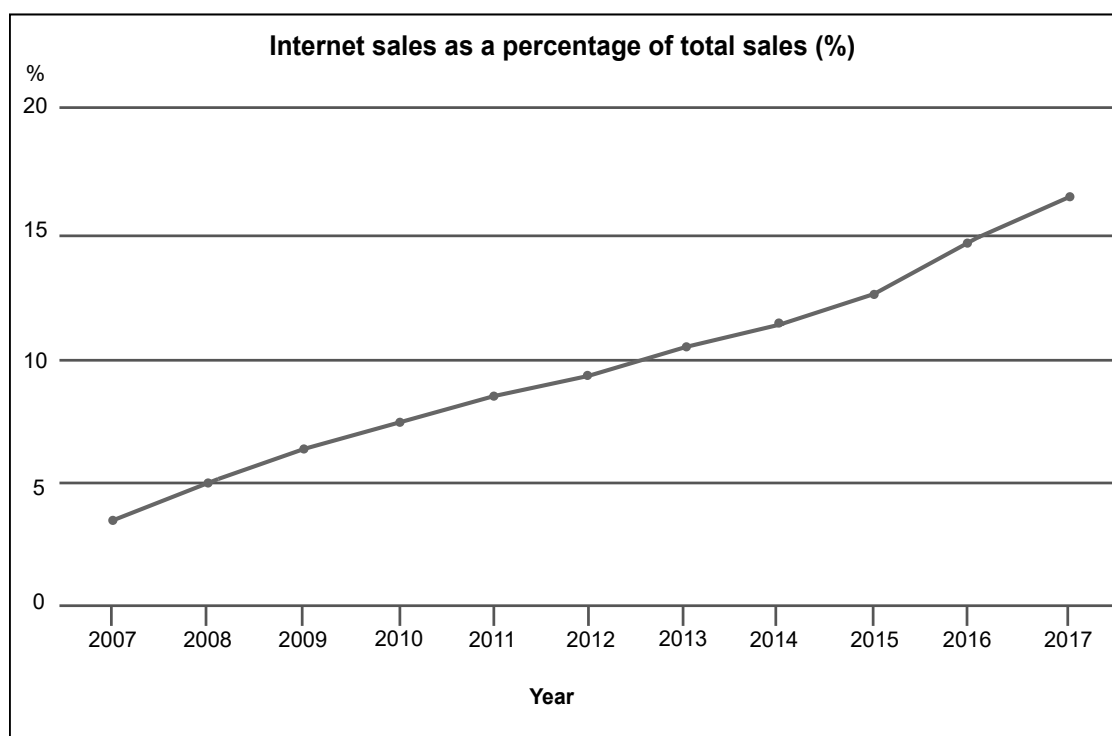
“In the previous few years, shopping habits in the build-up to Christmas have structurally changed,” said Ipsos Retail Intelligence Director, Dr Tim Denison.

Discounting and promotional activity around Black Friday now stretch over a two-week period. This pulls forward Christmas shopping into November but reduces the volume of sales in the run-up to Christmas and in the winter sales immediately following.

The rapid increase in online shopping has also fundamentally altered the way retailers now need to approach the Christmas season.

Appendix B

Internet sales as a percentage of total retail sales, 2007 - 2017



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