

Tuesday 21 May 2024 – Afternoon

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

- This Insert contains the pre-release material that you have already seen.
- This document has **4** pages.

Safe As Houses plc

The business

Safe As Houses plc (SAH) is one of the UK's leading online estate agents. The business uses its technological expertise and the internet to bring together buyers and sellers of domestic properties e.g. houses and flats. The company has no presence on the high street but conducts its business through its website and digital applications (apps). SAH advertises properties that buyers want to buy, or sellers wish to sell. SAH then arranges for buyers to view properties they are interested in purchasing. SAH then helps buyers to reach an agreement with the sellers to purchase the property. The initiator (whether a buyer or a seller) in each transaction pays SAH a fee for their services. This fee is SAH's main source of revenue.

The business was founded in 2014 by Amaya Jackson. Amaya had worked in a traditional high-street estate agency for several years. She had become convinced that there was a significant gap in the market for a low-cost, web-based, service. A service that would appeal to younger people who were confident using the internet.

The business began as a private limited company. In 2018, the business converted to a public limited company. The stock market flotation helped to fund further investment into mobile apps, increasing the capacity of the business to meet the needs of its growing client base. SAH's market share has grown rapidly. SAH now holds a 5% share of the UK's home buying market. SAH does not currently operate outside of the UK.

Amaya currently has the largest shareholding in the public company (23%). In addition, each company director receives rewards in the form of shares in addition to their salary. The directors' shareholding currently totals 5%. Most of the remaining shares are owned by organisations, including UK banks and pension funds.

Amaya, as Chair of the Board of Directors, is the person responsible for setting the agenda of Board meetings. This means that, although she does not own enough shares to control the decision-making process, she does get to decide what the Board will discuss.

The problem

In recent years the success of the company has resulted in it having substantial cash reserves, currently totalling £65 million. The directors are aware that these cash reserves would become available to anyone who gained control of the business. SAH's shares are publicly traded and this potentially makes the business vulnerable to a hostile takeover.

To solve this problem Amaya would like SAH to use a substantial part of its cash reserves to expand the business. Amaya has prepared three options which she would like to present to the Board of Directors at their meeting in a month's time. Amaya is concerned that some of the other directors might place their own short-term financial interests above the long-term interests of the company. This might lead to strategic decisions being taken that ultimately result in a takeover bid from a competitor or from a multinational company keen to add SAH to its portfolio of businesses.

Option 1: Offer new services to UK homeowners

Amaya is aware that SAH's relationship with customers ends when they buy or sell their property. Amaya's idea is that, in return for a fixed monthly fee, SAH will provide a bespoke range of services to homeowners throughout their ownership of the property. This would cover things such as help with repairs to central heating and plumbing, help with energy conservation and utility bill management.

Amaya estimates that this option would require capital expenditure of £40 million and additional revenue expenditure of approximately £15 million a year. Investment appraisal suggests a payback period for this option of 4 years and 6 months, with an average rate of return (ARR) of 9.64%.

Option 2: Operate in Europe

Amaya is aware that the property market in most of the European Union (EU) is different to the UK. In the EU a higher proportion of properties are still sold through traditional 'bricks and mortar' estate agents. Amaya thinks that the time is right for SAH to start offering its services in other European countries. Amaya's proposal is to begin operations in France and, if after five years that is successful, then widen its field of operations to the rest of the EU.

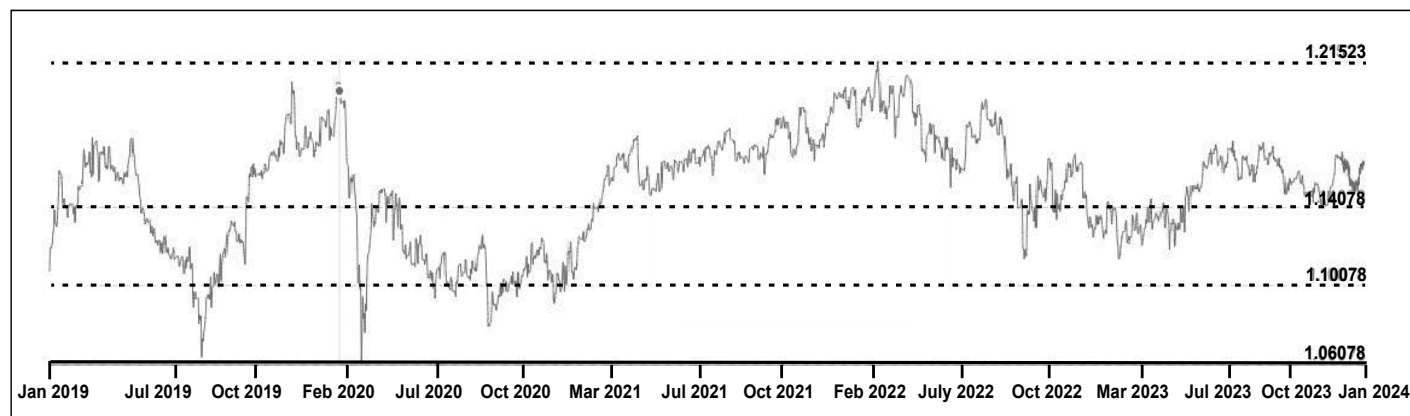
Amaya estimates that this option would require capital expenditure of £50 million and additional revenue expenditure of approximately £12 million a year. Investment appraisal suggests a payback period for this option of 5 years and 5 months, with an ARR of 6.29%.

Option 3: Buy a US health insurance business

Amaya spends much of her non-working time in the United States of America. She is aware that most Americans are expected to pay for their own health care. Health care in the United States is very expensive. As a result, most Americans use health insurance companies. Amaya is aware that a relatively small health insurance business in the USA might be available for sale. Health insurance businesses in the United States are generally quite profitable.

Amaya estimates that this option would require capital expenditure of £60 million and additional revenue expenditure of approximately £10 million a year. Investment appraisal suggests a payback period for this option of exactly 5 years, with an ARR of 5.71%.

Appendix 1: Pound sterling to Euro exchange rate January 2019 to January 2024



Appendix 2: How US Health Insurance Works

Health care in the United States can be very expensive. A single doctor's office visit may cost several hundreds of dollars and an average three-day hospital stay can cost tens of thousands of dollars (or even more) depending on the type of care provided. Most of us could not afford to pay such large sums if we became sick, especially since we do not know when we might become ill or injured or how much care we might need. Health insurance offers a way to reduce such costs to more reasonable amounts.

The way it typically works is that the consumer pays an upfront premium to a health insurance company and that payment allows you to share 'risk' with lots of other people who are making similar payments. Since most people are healthy most of the time, the money paid to the insurance company can be used to cover the expenses of the relatively small number of people insured who get sick or are injured. Insurance companies, as you can imagine, have studied risk extensively. It is their goal to collect enough premiums to more than cover the combined medical costs of those who buy health insurance.

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