

Markscheme

November 2022

Business management

Higher level

Paper 2

23 pages

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The markbands and assessment criteria on page 3 should be used where indicated in the markscheme.

Marks	Level descriptor
0	The work does not reach a standard described by the descriptors below.
1–2	<p>Little understanding of the demands of the question.</p> <p>Few business management tools (where applicable), techniques and theories are explained or applied, and business management terminology is lacking.</p> <p>Little reference to the stimulus material.</p>
3–4	<p>Some understanding of the demands of the question.</p> <p>Some relevant business management tools (where applicable), techniques and theories are explained or applied, and some appropriate terminology is used.</p> <p>Some reference to the stimulus material but often not going beyond the name of a person(s) and/or the name of the organization.</p>
5–6	<p>Understanding of most of the demands of the question.</p> <p>Relevant business management tools (where applicable), techniques and theories are explained and applied, and appropriate terminology is used most of the time.</p> <p>Some reference to the stimulus material that goes beyond the name of a person(s) and/or the name of the organization.</p> <p>Some evidence of a balanced response.</p> <p>Some judgments are relevant but not substantiated.</p>
7–8	<p>Good understanding of the demands of the question.</p> <p>Relevant business management tools (where applicable), techniques and theories are explained and applied well, and appropriate terminology is used.</p> <p>Good reference to the stimulus material.</p> <p>Good evidence of a balanced response.</p> <p>The judgments are relevant but not always well substantiated.</p>
9–10	<p>Good understanding of the demands of the question, including implications, where relevant.</p> <p>Relevant business management tools (where applicable), techniques and theories are explained clearly and applied purposefully, and appropriate terminology is used throughout the response.</p> <p>Effective use of the stimulus material in a way that significantly strengthens the response.</p> <p>Evidence of balance is consistent throughout the response.</p> <p>The judgments are relevant and well substantiated.</p>

Section A

1. (a) State **two** features of a private limited company. **[2]**

Private limited company: is a limited company whose **share cannot be sold to the general public.**

Features of a private limited company include:

- the **owners** have **limited liability**;
- **shares can only be sold to friends and family** and not on the stock exchange. Shares **cannot be offered for sale to the general public** or transferred without agreement of all shareholders.
- **better access to finance** than, for example, sole trader or partnership;
- **legal continuity**;
- often a small to medium sized family business;
- not obliged to share financial information with public hence more privacy than public limited company (PLC) (*do not accept* "no need to publish financial accounts" as all incorporated firms must do this) separate legal identity – same as "incorporation".

Accept any other relevant feature.

*Award **[1]** for each appropriate feature of a private limited company stated (application **not** required), up to a maximum of **[2]**.*

- (b) Using **Table 1** and other information provided, calculate for SSA's second academy:

- (i) the payback period (*show all your working*); **[2]**

Year	Cash inflow (\$)	Cash outflow (\$)	Net cash flow (\$)	Cumulative cash flow (\$)
0		(500 000)	(500 000)	(500 000)
1	160 000	40 000	120 000	(380 000)
2	200 000	50 000	150 000	(230 000)
3	240 000	60 000	180 000	(50 000)
4	375 000	75 000	300 000	250 000
5	700 000	140 000	560 000	810 000

Payback between years 3 and 4.

$$\$300\,000/12 = \$25\,000/\text{month}$$

$$\$50\,000/\$25\,000 = 2$$

Payback is **3 years 2 months**.

(**or 2 years 7 months**, 2.58333 or 2.58 years or 31 months **if only cash inflows used**)

Alternative working: $\$120\,000 + \$150\,000 + \$180\,000 + (\$50\,000/\$300\,000) \times 12$
= 3 years 2 months

Alternative working: = \$120 000 + \$150 000 + \$180 000 + (\$50 000/\$300 000) =3.1666
or **3.17** years (allow rounding) or **38 months**

Award marks as follows:

[1] If a candidate **who has shown working** provides a correct procedure (thus, demonstrates an understanding of the underlying concepts) **but** has made an error in calculation or the answer does not include **years/months**.

[1] If a candidate does not show any working and simply writes the answer.

[2] if a candidate provides the **correct answer with working**. A correct answer must include **years/months**.

N.B. award a maximum of **[1]** if net cash inflows used.

- (ii) the average rate of return (ARR) for the first five years of operation (show all your working); **[2]**

Total returns = \$120 000 + \$150 000 + \$180 000 + \$300 000 + \$560 000 = \$1 310 000
Capital Cost = \$500 000
Years of use = 5

$$ARR = \frac{(\text{total returns} - \text{capital cost}) / \text{years of use}}{\text{capital cost}} \times 100$$

Total return over 5 years = \$1 310 000 - capital cost = \$810 000

Average annual profit = \$810 000 / 5 = \$162 000

ARR = (\$162 000 / \$500 000) x100% = **32.4%**
(Accept 47% if only cash inflows used)

Award marks as follows:

[1] if a candidate **who has shown working** provides a correct procedure (thus, demonstrates an understanding of the underlying concepts) **but** has made an error in calculation or the answer does not include the **percentage sign (%)**.

[1] if a candidate does not show any working and simply writes the answer.

[2] if a candidate provides the **correct answer with working**. A correct answer must include the **percentage sign (%)**.

Award no marks **[0]** merely for writing the formula.

Apply candidate own figure rule (OFR) if candidate uses an incorrect net cash flow figure from (b)(i).

- (iii) the net present value (NPV) at a discount rate of 4% (see **Table 2**) (*show all your working*). **[2]**

Using discount tables:

Year 1	$\$120\,000 \times 0.9615 = \$115\,380$
Year 2	$\$150\,000 \times 0.9246 = \$138\,690$
Year 3	$\$180\,000 \times 0.8890 = \$160\,020$
Year 4	$\$300\,000 \times 0.8548 = \$256\,440$
Year 5	$\$560\,000 \times 0.8219 = \$460\,264$

Total present value = \$1 130 794

Net present value (NPV) = TPV - capital cost

NPV = \$1 130 794 - \$500 000 = \$630 794
(accept \$948 000 if only cash inflows used)

Some candidates may add the \$500 000 as Year 0 and calculate it this way. Please award full marks if the correct answer is arrived at.

Full headings and full calculations are not expected for each year.

Full marks can be awarded if there is some evidence of calculation especially the movement from the total DCF to NPV, if the DCF for each year is not shown but it is clear the candidate understands the method.

N.B. allow the candidate own figure rule (OFR) if using incorrect net cashflow from (b)(i).

*Award [2] if a candidate provides the **correct answer with working**. A correct answer must include **\$ sign**. Award [1] for working and [1] for the correct answer.*

*Award [1] If a candidate **who has shown working** provides a correct procedure (thus, demonstrates an understanding of the underlying concepts) **but** has made an error in calculation or the answer does not include **\$ sign**.*

Award [1] If a candidate does not show any working and simply writes the answer.

Award no marks [0] for writing the formula.

(c) Explain **one** disadvantage for SSA of **only** using the payback period method in making its decision to open a second academy. **[2]**

- **only focuses on how fast it will payback** rather than overall profit as the most important factor. Overall ARR is 32.4%, a very high return;
- using the payback method **can encourage short-termism** as it does not look at the net cash flow made after it has paid back. Student numbers significantly increase after the payback period but this is not accounted for;
- this new soccer academy **seems like a long-term investment**, is payback suitable?
- **fails to consider the time value of money** especially if interest rates change over the 5 years of cash flows being considered.

Accept any other relevant disadvantage and explanation.

This question is about a limitation of the payback method so do not credit either all the figures are forecasted, or this method does not take non-financial factors into account. This is true of all investment appraisal methods.

Award [1] for a relevant and correct disadvantage identified.

Award [1] for a relevant and correct explanation with application to SSA, up to a maximum of [2].

2. (a) Define the term *brand awareness*. [2]

Brand awareness is a marketing term that describes the **degree of consumer recognition of a product or service by its name, logo or sound.**

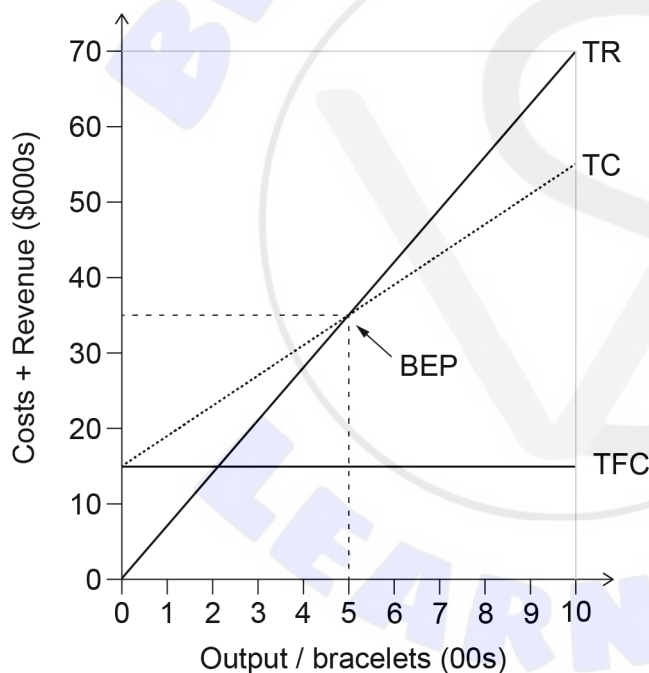
N.B. no application required. Do not credit examples.
Candidates are **not** expected to word their definition **exactly** as above.

Award [0] marks if the candidate writes a response along the lines of repeating the stimulus such as “customers are aware of the brand.”

Award [1] for a basic definition that conveys partial knowledge and understanding of consumer recognition of the product of service.

Award [2] for a full definition that conveys knowledge and understanding similar to the answer above **and** indicates that the consumer recognizes the brand be at least one of the following: name, logo, or sound.

- (b) Using **Table 3**, draw a fully labelled break-even chart, to scale, for FS for 2022. [4]



Sales	TFC	TVC	TC	TR	Profit
0	15000	0	15000	0	-15000
100	15000	4000	19000	7000	-12000
200	15000	8000	23000	14000	-9000
300	15000	12000	27000	21000	-6000
400	15000	16000	31000	28000	-3000
500	15000	20000	35000	35000	0
600	15000	24000	39000	42000	3000
700	15000	28000	43000	49000	6000
800	15000	32000	47000	56000	9000

Candidates do not need to create the table above – these are the figures for the break-even chart.

Candidates could also calculate the break-even point using this alternative method:

Break-even point (units) = Fixed costs / (Price per bracelet – Variable cost per bracelet)

Break-even point (units) = \$15000 / (\$70 - \$40) = \$15000 / \$30 = 500 bracelets

Break-even point (\$) = Price per unit x units = \$70 x 500 = \$35 000; or

Break-even point (\$) = Fixed costs + (Variable cost x units) = \$15000 + (\$40 x 500) = \$35000

Break-even point = 500 bracelets (x-axis) and \$35000 (costs/revenues; y-axis)

Award marks as follows:

[1] for a correctly labelled and accurately drawn total revenue (TR) line – can be TR or revenue (but not “sales” on its own).

[1] for a correctly labelled and accurately drawn total cost (TC) line.

[1] for identifying the break-even point. Ideally, the candidate will draw an arrow pointing to the break-even point and label the arrow. However, accept as an accurately labelled break-even point a vertical line from the x-axis to the break-even point, provided that the line is labelled “break-even point”.

[1] for correctly labelling BOTH axes – y-axis must have both costs and revenue; x-axis must have some indication of quantity, e.g. units/quantity/items/bracelets.

A break-even chart that is not neat, not drawn with a straight edge, or is not drawn to scale can be awarded a maximum of **[2]** if the total revenue and total cost lines and axes are all correctly labelled.

If a candidate produces a table rather than a chart, award **[0]**.

N.B. do not penalize if graph paper is not used. However, drawn diagrams must have a consistent verifiable scale, otherwise it cannot be determined if TR and TC are accurate, even if correctly labelled.

(c) Using **Table 3**, calculate:

- (i) the profit or loss in 2022 for *FS* if production and sales increase to 1200 bracelets (*show all your working*);

[2]

Profit = Total revenue – total costs
 Profit = 1200 bracelets x (\$70) – [\$ 15 000 + (1200) x (\$40)]
 Profit = \$ 84 000 – [\$ 15 000 + \$ 48 000]
 Profit = \$ 84 000 - \$ 63 000
Profit = \$ 21 000

Alternative method:
 Profit = [(Price per bracelet -Variable costs per bracelet) x 1200] - total costs
 Profit = [(\$70 – \$40) x 1200] - \$ 15 000
 Profit = [\$30 x 1200] - \$ 15 000
 Profit = \$36 000 - \$ 15 000
Profit = \$ 21 000

Or

Break-even quantity = 500
 Output beyond break even is 1200 - 500 = 700
 Unit contribution = 70 - 40 = 30
Profit = 700 x 30 = \$21 000

Award marks as follows:

[1] If a candidate **who has shown working** provides a correct procedure (thus, demonstrates an understanding of the underlying concepts) **but** has made an error in calculation or the answer does not include \$.

[1] If a candidate does not show any working and simply writes \$21 000.

[2] if a candidate provides the **correct answer with working**. A correct answer must include \$.

- (ii) the price *FS* would need to charge per bracelet if it sells 800 bracelets and wants to make a profit of \$10 000. Assume that the costs remain the same (*show all your working*). **[2]**

Target profit = total revenue – total costs
 \$ 10 000 = \$ 800X – [\$ 15 000 + (800 x 40)]
 \$ 10 000 = \$ 800X – [\$ 47 000]
 \$ 10 000 + \$ 47 000 = 800X
 \$ 57 000 = 800X
 X = \$ 71.25
Price per bracelet = \$ 71.25

N.B. accept alternative working.

Award marks as follows:

[1] If a candidate **who has shown working** provides a correct procedure (thus, demonstrates an understanding of the underlying concepts) **but** has made an error in calculation or the answer does not include \$.

[1] If a candidate does not show any working and simply writes \$71.25.

[2] if a candidate provides the **correct answer with working**. A correct answer must include \$.

Section B

3. (a) Define the term *organizational culture*. [2]

Organizational culture is based on the **beliefs, values and attitudes of the leadership and employees in a business**. It can be classed as “the way we do things around here”.
N.B. *no application required. Do not credit examples.*

*Candidates are **not** expected to word their definition **exactly** as above.*

Award [1] for a basic definition that conveys partial knowledge and understanding.

Award [2] for a full, clear definition that conveys understanding similar to the answer above that shows understanding that culture is driven by the leadership.

- (b) Using Herzberg’s motivation theory, explain **two** reasons for DS’s high employee morale. [4]

Herzberg’s theory believes that **motivators** are the **factors which make employees happy** in their job. The main motivators detailed are:

- **Job enlargement** - giving employees more **variety** in their work, this will then make work more interesting. In DS, employees were able to take advantage of job rotation;
- **Job empowerment** - there is a **democratic leadership** style which means employees **take part in decision making**. Quality circles mean employees can work together to try to solve problems within the business;
- **Job enrichment** - This refers to employees being given more **challenging tasks to allow them to improve their skills**. In DS, employees are given the opportunity to manage tasks – a vertical expansion.

Accept any other relevant reason.

N.B. *Do **not** credit any reference to hygiene factors such as office space, generous breaks or competitive salaries as motivators.*

N.B. *It is not mandatory for candidates to specifically mention “democratic style” since it is not explicit in the stimulus.*

Mark as 2+2

Award [1] for an appropriate reason and an additional [1] for application. Award a maximum of [2] for each reason.

*[2] cannot be awarded per reason if the response lacks either explanation **and** / **or** application.*

For example:

*For an identification or a description of a reason **with or without** application award [1].*

*For explanation of a reason with **no** application award [1].*

*For explanation of a reason **and** application award [2].*

Maximum award overall: [4].

- (c) Explain **two** reasons for the working capital problems at DS. **[4]**

Working capital is the capital of a business which is **used in the day-to-day running of the business**. It is calculated as the current assets minus current liabilities.

Reasons for working capital problems:

- DS's **debtor days ratio is remarkably high**, especially when **compared to creditor days**. In 2021, it was taking almost six months to receive payment for orders of board games;
- the difference between debtor and creditor days ratio means DS are **paying their invoices much quicker than they are receiving payment** from the retailers. This will **cause working capital issues**;
- the **acid-test ratio is worsening**. By 2021, it is 0.61 - this could mean DS is **holding too much stock**, the least liquid of current assets. They **don't have enough liquid assets to cover current liabilities**. **Note:** it is difficult to be specific about the effects of low acid test as this we do not know what is normal for this industry;
- DS are operating on a long working capital cycle with new games taking up to 12 months to develop;
- acid test ratio in 2019 (i.e. 1.32) was in the acceptable range between 1:1 to 1.5:1. It deteriorated in 2020 and 2021, which were much below the acceptable range;
- DS has more employees to pay but without the requisite increase in cash received.

Accept any other relevant reason.

Mark as 2+2

Award [1] for an appropriate reason and an additional [1] for application. Award a maximum of [2] for each reason.

*[2] cannot be awarded per reason if the response lacks either explanation **and** / **or** application.*

For example:

*For an identification or a description of a reason **with or without** application award [1].*

*For explanation of a reason with **no** application award [1].*

*For explanation of a reason **and** application award [2].*

Maximum award overall: [4].

- (d) Discuss whether *DS* should choose **Option 1** or **Option 2**. **[10]**

The candidate is expected to analyse both options in a balanced manner and make reasoned judgments as to what option is most favourable for *DS*.

Option 1: Accept the takeover request from BGI.

If Emma and Laura accept the takeover from BGI they will **receive a significant sum for their share capital**. They are relatively new to business, being recent university graduates, and they might feel they can now look at starting another business.

This offer will **offer security to DS to continue in business**. BGI is a market leader and will **have the funds needed to fix the working capital problems** and enable *DS* to continue to grow. The *DS* brand will continue and the original **owners will still hold a substantial percentage of the share capital**. BGI also has experience in this industry and the new Chief Executive will be able to take *DS* forward.

On the other hand, DS would no longer belong to Emma and Laura. They would have **no input to any strategic decisions** and would effectively be side-lined by BGI.

Might BGI want to take *DS* in a different strategic direction? Currently, *DS* employees are very happy in their work but there could be **redundancies or a change in working practices**. BGI will install their own CEO, they may want to put their own designers, marketing employees into *DS*. This could **negatively the morale** at *DS*.

Option 2: Venture capitalist

Selling 35% of their shares to a venture capitalist will give *DS* capital to **both remedy the liquidity issues and continue their rapid expansion**. This would mean **risks would be spread** and would not all be Emma and Laura's. **Emma and Laura will still have a controlling share** in the business and will have the deciding **vote in any strategic decisions**.

While it is not detailed in the stimulus, it could be assumed there is the possibility of **synergy** with the venture capitalist. *DS* could benefit from skills, experience and resources which the new investor will bring. They could have experience in the board game market or dealing with working capital problems.

On the other hand, is this going to be a significant enough investment for *DS*? The stimulus says it will be sufficient for one year but this doesn't seem enough to pursue rapid expansion. As games can take one year from design to retail there is a danger *DS* will find themselves with the **same problems in a year (and with 35% less ownership)**.

There is the possibility that instead of synergy there is a **degree of conflict with** how the **venture capitalist** wants to run *DS*. We are given no indication of the background or skills of the investor and *DS* will be expected to undertake due diligence before accepting the offer. **Overall**, the takeover **will provide DS with significant finance** but it would mean a **major upheaval** for the company, including Emma and Laura having no further say in strategic decisions. While the **VC offer provides less capital**, it means the **current leadership team stays** in place to provide continuity.

It is expected that candidates provide a conclusion with substantiated judgment.

Accept any substantiated judgment.

Marks should be allocated according to the mark bands on page 3 with further guidance below.

For one relevant issue that is one-sided, award up to [3].

For more than one relevant issue that is one sided, award up to a maximum of [4].

If a candidate evaluates only one option, award a maximum of [5].

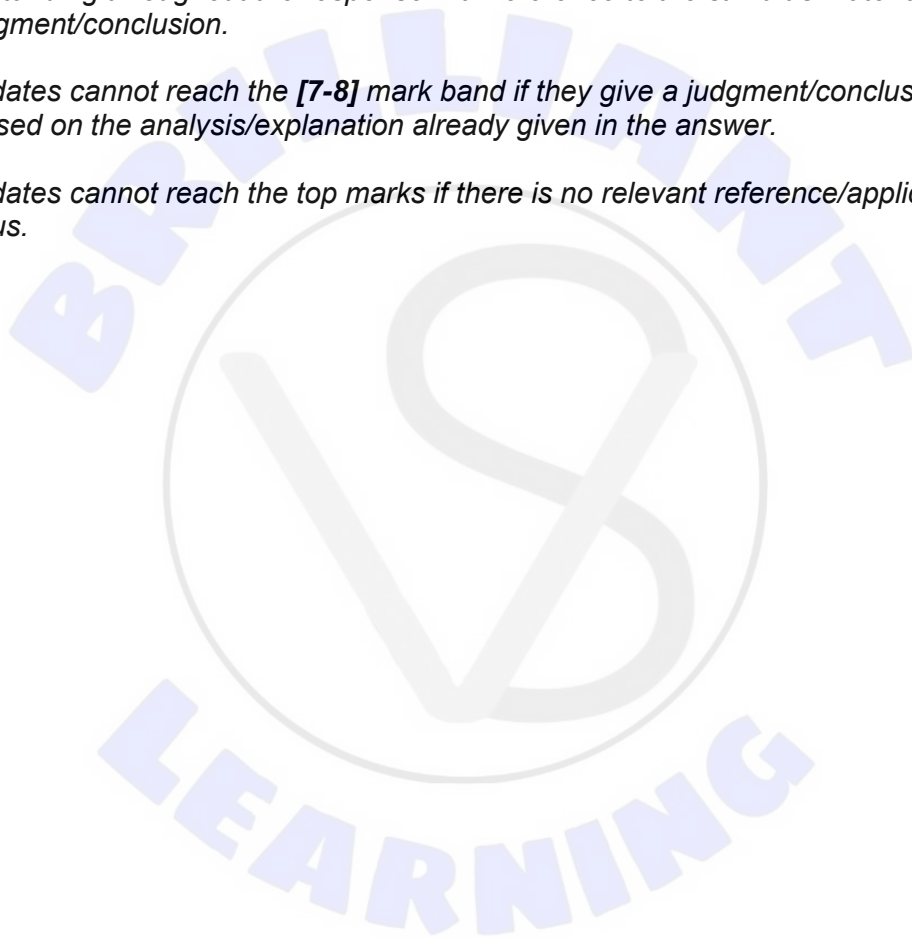
A balanced response is one that provides at least one argument for and one argument against each option.

Candidates may contrast one option with another for a balance as long as at least two arguments are given for each option.

Award a maximum of [6] if the answer is of a standard that shows balanced analysis and understanding throughout the response with reference to the stimulus material, but there is no judgment/conclusion.

Candidates cannot reach the [7-8] mark band if they give a judgment/conclusions that are not based on the analysis/explanation already given in the answer.

Candidates cannot reach the top marks if there is no relevant reference/application to the stimulus.



4. (a) State **two** characteristics of flow production. [2]

Two characteristics include:

- **continuous process** of manufacturing products often using assembly lines
- **standardized** large quantity products are being produced
- often very **capital intensive** with investment in machinery
- often able to utilize relatively low skilled labour.

Accept any other relevant characteristic.

N.B. do not credit advantages.

*Award [1] for each characteristic identified (application **not** required).*

- (b) Explain **one** advantage **and one** disadvantage for ER of commissioning market research using focus groups. [4]

The possible **advantages** for ER of commissioning market research based on focus groups are:

- a deep and meaningful discussion can be carried out by a **professional researcher** with the participants being asked detailed questions about their options/ideas. In this case, the discussion revealed participants' perception towards competitors' pricing (medium) and suppliers' quality (also medium)
- **reactions** of the participant to each of the options can also be **observed by the qualified researcher** (application to the stimulus would be similar to the one above);
- ER was given **insightful information about consumers' opinion, preferences, expectations** and the most important issue, customers prioritise innovative products more than ER being an environmentally friendly business.

The possible **disadvantages** for ER of commissioning market research based on focus groups are:

- ER sells to customers worldwide, while the **focus group** members were chosen **only from the Middle East**;
- the sample is likely to be **unrepresentative** because the location where the focus group took place was limited to the Middle East. The answers might reflect the opinion of particular segments of the population - income, lifestyle, and perceptions of the importance of being environmentally friendly in a biased way.

Market research was undertaken by a professional market research company, however there **might still be** bias as perhaps the more talkative, environmentally concerned, more self-assured, extroverted people joined the group and or expressed their opinion more than other participants. The information upon which ER is going to change its strategic focus may be inaccurate, incomplete and costly.

Accept any other relevant advantage/disadvantage.

N.B. do not credit advantages/disadvantages that are common to ANY primary research.

Mark as 2 + 2

*Award [1] for **one** appropriate advantage and an additional of [1] for a description of how that advantage relates to ER. Award a maximum of [2].*

Award **[1]** for **one** appropriate disadvantage identified and an additional **[1]** for a description of how that disadvantage relates to ER. Award a maximum of **[2]**.

[2] cannot be awarded per advantage/disadvantage if the response lacks either explanation **and / or** application.

For example:

For an identification or a description of an advantage/disadvantage **with or without** application **[1]**.

For explanation of an advantage/disadvantage with **no** application **[1]**.

For explanation of an advantage/disadvantage **and** application **[2]**.

Maximum award overall: **[4]**.

- (c) Explain **one** advantage **and one** disadvantage for ER of raising finance through loan capital from a bank. **[4]**

The **advantages** for ER of taking loan capital from a bank are:

- it is likely that because profit has not been made recently, ER is likely to have experienced a fall in retained profit;
- a loan might be a good option and there is a possibility that being an LTD, ER **can** potentially **raise the large amount of the finance** needed in the form of a bank loan. Collateral is likely to be available in the form of real estate/ factories;
- if the bank agrees, the **process can be quick** and it fits well with ER's desire for a quick response;
- if a bank specializing in SMEs can be found to offer loans at low interest rates this may be beneficial compared to regular banks.

The **disadvantages** for ER of taking loan capital from a bank are:

- ER is **highly geared**; therefore, the likelihood is that the bank will refuse the loan as ER can be perceived as a risky venture for the bank;
- even if the bank approves the bank loan, the likelihood is that the bank will offer the loan with a relatively **high interest rate** which ER will have to pay regardless of their financial position;
- **ER is not profitable and the accumulated interest rate burden can increase the financial problem/ collapse** etc.

Mark as 2 + 2

Award **[1]** for **one** appropriate advantage and an additional of **[1]** for a description of how that advantage relates to ER. Award a maximum of **[2]**

Award **[1]** for **one** appropriate disadvantage identified and an additional **[1]** for a description of how that disadvantage relates to ER. Award a maximum of **[2]**

[2] cannot be awarded per advantage/disadvantage if the response lacks either explanation **and / or** application.

For example:

For an identification or a description of an advantage/disadvantage **with or without** application **[1]**.

For explanation of an advantage/disadvantage with **no** application **[1]**.

For explanation of an advantage/disadvantage **and** application **[2]**.

Maximum award overall: **[4]**.

- (d) Recommend whether *ER* should implement **Option 1** or **Option 2** as a research and development strategy, given the pace of change in the scooter industry. [10]

It is expected that firstly, candidates know how numerous factors such as organizational culture, change of pace, technology, etc., may affect the ability of an individual, a team or a business to innovate successfully – and may influence the R&D practices and strategies of an organization, and secondly, will show a clear understanding of the difference between the two types of innovation.

Option 1-

Adaptive creativity is unlikely to create a new **USP** given the increase in global competition. It appears that customers prefer Innovative creativity /cutting-edge products, **adapting** the scooters. E-scooters using the same positioning, cannot be judged as an example of such cutting-edge innovation as E-scooters are globally available. One may judge this argument against the option as highly significant.

Based on the market **research results**, **demand** is likely to **increase** due to the scooters being electric and therefore **environmentally friendly** and produced by an environmentally friendly organisation. However, **customers did not rate** this issue as the most important. Given the customers identical perceptions of all the scooter manufacturers, this part of the strategy might not be successful and therefore the strategy is likely to make a limited impact on ER's market share/ finance.

ER is going to **subcontract the production of the batteries**; therefore, ER will be **dependent** on a designer and manufacturer of electric batteries in terms of quality, price, and delivery. Perhaps this is too much of a **risk**.

One may also argue that some part of the **overall production will be more ecologically friendly**. However, the **cell production method is not as environmentally friendly** as flow production could be due to the duplication of resources.

Employees' motivation may increase significantly as cellular manufacturing will reduce boredom as employees carry out more tasks, rotate tasks as well as seeing the completion of a particular task/creation of a model. **Training will also boost** the confidence/ morale of the employees. Employees' motivation can be judged as an important factor to consider. This option will be **quicker to implement** and this is what the management would like to do. Still, one may judge this issue as ER having a short- term focus.

Option 2-

The merits of **innovative creativity** are many and are highly significant. This innovative creativity will **satisfy the top priority of the customers** and **creates a new competitive advantage**. More innovative and technologically advanced scooters will be produced- the **new products and the new positioning** away from the competitors **will create a new USP/ competitive advantage/clear differentiation**.

ER will address/ satisfy the main priority of their customers. The **demand for their scooters is likely to increase**.

High prices can be charged that will eventually **cover the high costs** and enable ER to start making a profit again. **In-house quality control** will improve.

However, the **lengths and the costs of the implementation** could be regarded as a critical issue to consider. The **length of time** to create and implement the innovative creativity **could harm ER financially in the short term**. Despite the fact that some diverse sources of finance are available, ER has **liquidity problems** and might not be able to survive. Still, given some availability of finance, one may judge this issue of less significance.

Maintaining **flow production will not solve employees' complaints**. The new competitive advantage will be due to the new and skilled employees in the R&D department hence, some evidence of demotivation is unlikely to strongly impact on ER.

Overall, it looks as if the arguments for **option 2** outweigh the arguments for **option 1** especially in the long term.

Accept any substantiated evaluation/judgment/recommendation.

It is expected that candidates provide a conclusion with substantiated judgment.

Accept any substantiated evaluation/judgment/recommendation.

Marks should be allocated according to the mark bands on page 3 with further guidance below.

For one relevant issue that is one-sided, award up to [3].

For more than one relevant issue that is one-sided, award up to a maximum of [4].

If a candidate evaluates only one option, award a maximum of [5].

A balanced response is one that provides at least one argument for and one argument against each option.

Candidates may contrast one option with another for a balance as long as at least two arguments are given for each option.

Award a maximum of [6] if the answer is of a standard that shows balanced analysis and understanding throughout the response with reference to the stimulus material but there is no judgment/conclusion.

Candidates cannot reach the [7–8] markband if they give judgment/conclusions that are not based on analysis/explanation already given in their answer.

N.B. *Candidates cannot reach the top marks if there is no relevant reference/application to the stimulus and if there is no clear understanding and use of the two types of innovation / adaptive and creative innovation.*

5. (a) State **two** characteristics of a niche market. [2]

Niche market is a **well-defined segment of a market** with consumers in that market having **specific characteristics**.

Characteristics include:

- is made up of that segment of consumers within the larger market place, who possess a common demographic, purchasing behaviour and lifestyle.
- segment likely to be very small compared the market as a whole.
- it has its own distinctive set of needs, preferences, or identity, making it unrelated from the traditional market.
- it often gives firms the opportunity to deliver goods and/or services that target the audience, and to build a competitive position in the market to defend against new entrants.
- products or services are often tailor-made hence able to charge higher prices.
- products are generally more expensive than products for a mass market.
- customer loyalty tends to be higher than in a mass or large market.

N.B. No application required. Do not credit examples.

Accept any other relevant characteristic.

Award **[1]** for each relevant characteristic stated up to a maximum of **[2]**. An example is not necessary but may help to clarify a definition.

- (b) Explain **two** methods that MM could use to reduce its labour turnover. [4]

Methods include:

- MM could change the **pay structure**, allowing for increases in pay, providing opportunities for bonuses, or offering fringe benefits (perks) to prevent employees from going to competitors who offer better salaries. In 2021, 3 people gave pay as reason for leaving.
- MM could be creative with low-cost rewards, such as flexible work hours, employee discounts, etc.
- MM could **create new posts** with promotion in mind, that way employees become aware of career progress opportunities. In 2021, 2 people gave lack of promotion as a reason for leaving.
- MM could recruit internally for vacant senior posts, that way employees know that they have a chance of promotion provided they meet qualifications. Application similar to above.
- MM could **invest in training**, which subsequently could help promote career opportunities and professional advancement (as stated above), given that according to the table employees left for a more interesting job. This likely to be needed if MM transitions to more complex keyboards with additional features.
- MM could make job more interesting by proceeding with the change marketing strategy which would involve moving from batch to job production methods. In 2021 5 people gave being offered a more interesting job as a reason for leaving.
- MM could provide meaningful feedback in appraisals of employees so that they feel respected and seen (no opportunity for an application mark if a candidate expresses this idea).

N.B. regarding application, **candidates must use wording from the stimulus or directly and explicitly link the response to the stimulus**. For example, if a candidate says “offer better pay” they have not applied that response to the stimulus. Thus, they receive **[1]**. If the candidate says “MM could offer better pay, as 3 employees left last year because of higher pay offered by a competitor,” they have linked the response to the stimulus.

Further, if a candidate writes that “MM should motivate its employees” or “improve motivation,” even if they name a theorist, this response is not enough. They must correctly specify a method to reduce labour turnover.

Finally, if a candidate cites from the table in the stimulus with no precise and appropriate method, award [0].

Accept any other relevant method.

Mark as 2 + 2

For [2], candidates must identify a method, explain it, and apply it to the stimulus up to a maximum of [4].



- (c) Explain **two** ways in which *MM*'s profits could be affected by changing from batch production to job/customized production. **[4]**

Answers should reflect the idea that **profits are determined by (revenues – costs) and that either element could be affected.**

Ways include:

- **smaller volumes** are likely to be **produced**. This could lead to **lower incomes**, and possibly **lower profits** but that depends on the price relative to home/school sales. It states that these individually produced items could be sold at a much higher price. **The profits also depend on what happens to costs;**
- The per unit cost is likely to increase because (1) in general it is cheaper per unit to produce with batch production than by job production and (2) the new keyboards will be more complex. Whether this increases or decreases profits will depend on price.
- the **change in production** method leads to **increased costs** (hiring skilled workers, training existing workers etc.) which would have a downward impact on profits;
- the change in production method is also likely to be more time consuming hence adding to production costs, However, this may not affect profits adversely if higher prices negotiated in advance offset this cost increase;
- **the marketing strategy** is likely to be **different**. The new market is much more of a niche market and easier to target so may cost less. Price is less likely to be a key element of the strategy giving the opportunity for higher prices negotiated in advance with musicians. These suggest a **reduction in marketing costs** and a **possible increase in profits.**

Accept any other relevant influence on profits.

N.B. *answers must reflect the impacts specifically on profits NOT just on costs.*

Accept any other relevant influence on profits.

Mark as 2 + 2

Award [1] for each influence on profits and an additional [1] for an explanation of the influence in context. Award a maximum of [2] per influence.

Maximum award overall: [4].

- (d) Discuss the impact on *MM*'s marketing mix if *MM* changes its target market to professional musicians. [10]

Price:

- **current price is set low** and aimed at consumer market via shops and contracts with schools. Likely to be a standard price, as low as possible;
- **new price is negotiated**. Likely to be different for each professional musician customer, depending on the specification. Likely to be much higher due to the uniqueness of each product and its complexity relative to existing market;
- change is from standard process to negotiated, **custom prices – more work and skills**;
- it is not known whether the new niche market is competitive. If so, this may affect the degree of flexibility with pricing.

Place:

- **currently** distributed **through third party retail outlets** or through **direct supply** to schools. The requirements of these customers remain fairly constant;
- **new** arrangements will be **sales direct to the customer**. *MM* lack experience in this type of marketing where customers often have varied requirements meaning *MM* need to be constantly aware of market changes;
- change is **from mixed retailer/direct to all direct** so some skills already.

Promotion:

- **currently** likely to be **done by retail outlets** with the addition of the free training packages. Currently, *MM* probably relies mostly on below-the-line (BTL) promotion and that is unlikely to change, though it may switch to different types of BTL promotion. Promotion to schools may be done through personal contact or through educational exhibitions, conferences, etc.;
- **new** promotion could be **through musical publications or direct contact**. Mass methods of promotion wasteful and not appropriate. Overall effect could be to lower promotion costs;
- **change is to in house** rather than relying on others. However, this may involve hiring staff with specialist knowledge adding to costs.

Product:

- **currently** a **standard** design, fairly simple in terms of standard features. Appearance may be less important to the current target market. This may enable *MM* to save on finishing costs;
- **changing** to a **tailor-made product** with **customized** features. Musicians likely to each have the owned demands in terms of appearance and features. Lack of standardization of the product however may increase costs of customized production but may well be offset by higher prices.

People:

- Currently, *MM* has 50 employees, and some of them have left in search of better opportunities. *MM* should find out if there is a skills gap to implement the change they have in mind. Those staff involved directly with musicians will need to understand the specific needs of this type of customer. Dealing with schools was likely a much simpler task. Rectifying any skills gap through training or external hiring may prove expensive. However, job production may prove more motivating to staff and hence reduce the high cost of labour turnover.

Process:

- MM should find out if there are any internal barriers in the way to delivering the best customer value at the time of changing the product design by adding the range of different sound features and improving the appearance of the keyboards. This will depend on how MM interact with musicians during the design part of the process.

Physical evidence:

- How does MM reassure the customers? Are MM staff well-trained? Will they continue to offer free online courses? Does MM offer a place where professional musicians can come and try/test the products?

The overall judgment is that no element of the marketing mix will remain unchanged and that MM will have to take on more responsibility for its own marketing and develop some skills. Also, the transition to the new market will not happen overnight, hence, MM will need to run two complimentary marketing strategies alongside each other for an undetermined period of time. This could lead to a lot of marketing confusion regarding where their priorities lie.

A conclusion with judgment is expected.

*Candidates should not be penalized if they **do not** address the extended marketing mix.*

Marks should be allocated according to the markbands on page 3 with further guidance below.

N.B. *The marks listed in the left column are maximum awards. Candidates could technically have a response that addresses two Ps in a balanced way yet still lacks the depth, precision, or application for [4] (for example). In other words, use the table below as a guideline but also make some holistic judgment about the quality of the response.*

1-2	No application, theoretical answer	
3	Some elements, very limited application	lacks depth
4	Two or three elements	Some depth on one P and some discussion of the others.
5	Three elements	Some depth on at least two Ps and some discussion of at least one other but lacks conclusion or conclusion is nominal.
6	Three elements	Some depth on three of four Ps but lacks conclusion or has an unsupported conclusion.
7-8	Three of the Ps considered well	All three in-depth with a conclusion that flows out of the arguments made and has more than a nominal conclusion.
9-10	All 4 Ps	In-depth discussion of all four Ps with a conclusion that flows out of the arguments made. Draws from the stimulus but also makes insightful inferences.