Cambridge International AS & A Level

Cambridge International Examinations
Cambridge International Advanced Subsidiary and Advanced Level

BUSINESS **9609/31**

Paper 3 Case Study **May/June 2016**

3 hours

No Additional Materials are required.

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READ THESE INSTRUCTIONS FIRST

An answer booklet is provided inside this question paper. You should follow the instructions on the front cover of the answer booklet. If you need additional answer paper ask the invigilator for a continuation booklet.

Section A
Answer **all** questions.
Section B
Answer **one** question.
You are advised to spend no more than 40 minutes on Section B.
The businesses described in this question paper are entirely fictitious.

The number of marks is given in brackets [ ] at the end of each question or part question.

This document consists of **5** printed pages, **3** blank pages and **1** Insert.

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CAMBRIDGE International Examinations

Sandson Electronics Limited (SEL)

'The winner of the 2016 innovation award goes to Sandson Electronics for its new robo-cleaner' announced the award ceremony presenter. Phil Sandson was delighted to receive yet another award for SEL. However, it would be the last time he would represent the company at the annual award ceremony for the European consumer electronics industry. He and his brother Robert, the joint owners of SEL, have just concluded a deal to sell the business to CCP, one of Africa's largest manufacturers of consumer electronics.

SEL was established 20 years ago by Phil and Robert, both engineering graduates. It is based in a European Union (EU) country. The company has established a strong reputation for invention and innovation of floor cleaners and other household appliances. The Sandson brand name has an excellent reputation in the industry. Its products are expensive but of such clever design that demand is high.

CCP's decision to take over the business was made during an emergency Board of Directors meeting, arranged after CCP's Chief Executive heard that SEL was for sale. New product innovation is SEL's strength – but managing the manufacturing operations is one of its weaknesses which has contributed to declining profitability. CCP's decision to acquire SEL was not based on detailed strategic analysis. It was mainly driven by the desire to gain SEL's intangible assets. Following the takeover, CCP's Chief Executive plans to operate SEL as a separate division within the CCP group of companies.

Establishing SEL's selling price

Phil and Robert decided to sell the business to raise the capital to invest in a social enterprise. This will supply clean water to low income families. The brothers studied carefully the data in Table 1 prepared for them by the company accountant. They decided to accept CCP's takeover bid of $35m – half in cash and half in CCP shares. They also considered external economic factors before accepting the bid.

Table 1: SEL selected accounting data

	2014	2015
Operating profit	$15m	$6m
Total non-current assets	$38m	$43m
Intangible non-current assets	$8m	$10m
Shareholders' funds/equity	$16m	$18m
Annual dividends	$2m	$1.5m
Acid test ratio	0.5	0.3
Gearing ratio	55.5%	57.1%

New award winning product – the robo-cleaner

This new product took SEL 9 years to develop and the total research and development cost was $28 million. This expenditure has led to serious cash flow problems. The robo-cleaner has just entered production and initial consumer test reports are very positive. Advance orders are high and an injection of CCP's cash will be necessary to provide the working capital needed for full production to start.

The robo-cleaner is a fully automatic robotic floor cleaner. It is powered by a new SEL designed and patented battery. The user places it in a room, switches it on and then it cleans the floor by itself. In-built sensors detect furniture and walls and the cleaner turns away from these. Three versions

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are available for different types of floor – carpet, wood or tiles. The product is more technologically advanced than rivals' products – this is vital as the industry is becoming increasingly competitive.

Market development – selling SEL's robo-cleaner in foreign markets

When the Sandson brothers owned SEL the company lacked the resources to market its products in foreign countries. CCP is determined to sell the robo-cleaner in as many global markets as possible. Freda, the Marketing Director appointed by CCP, plans to start this process of market development by exporting the robo-cleaner to country X. She will have to make important marketing strategy decisions, including:

- Which model of robo-cleaner should be launched first?
- Should the objective be high market share?
- Will the existing advertising and promotional material for the robo-cleaner be suitable for country X?
- Is it best to use existing well-established wholesalers in country X as a channel of distribution or should the robo-cleaner only be available to purchase online?

Factory workforce performance

The data in Table 2 indicates declining factory workforce performance at SEL's factory before the takeover by CCP. Phil and Robert were interested in design and research, rather than manufacturing. Chris has been Operations manager at the factory since 2013. He uses a hard approach to human resource management. Despite this, the quality of the electrical appliances leaving the factory is high – but many are rejected before they reach this final stage. Factory employees are trained in the specific skill they require. Chris is a very experienced Operations manager and he believes that he can solve all operational problems himself. He is a firm believer in promoting workers he likes and rejects the idea that the factory needs to adopt an equality and diversity policy. The directors of CCP are secretly considering whether they should close this SEL factory and transfer production to one of CCP's factories in Africa.

Table 2: SEL factory workforce – performance data

	2014	2015
Factory employees	250	268
Total annual output of appliances	44 000	44 500
Number of appliances rejected by quality control	2000	2200
Factory employees who left during the year	55	63
Number of days lost through absenteeism (full time contract = 200 days per year)	5000	5400

Communication methods

By commenting on blog posts, employees in the SEL division can use BlogHub to share ideas and knowledge on issues that are relevant to them and the company. BlogHub is an effective collaborative tool and helps to increase awareness of what each engineer, researcher and designer is working on.

Social media communication can have beneficial effects with some customers too. Last year a customer was disappointed with the lack of SEL's appliances in his preferred colour. He wrote a highly critical personal post about his experience and posted this on social media. Much to the customer's surprise, he received a message direct from SEL within minutes and by the end of the week this had been followed up with several phone calls from SEL. The company even posted a discount card so the customer could purchase a specially painted SEL product at a low price. The customer immediately used social media to tell the whole world of the positive customer service he had received!

CCP's future Research and Development (R&D) strategy

SEL invested almost 15% of its annual revenue in recent years in research and development. This is a higher proportion than that invested by competing businesses. CCP's R&D strategy, until the decision to take over SEL, was to minimise investment in new technology but to copy as closely as possible competitors' innovations. Table 3 contains some recent industry data on R&D spending.

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Table 3: R&D spending and other data for major companies in the EU household appliance industry

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Major companies in household appliance market (EU)	Annual average R&D spending 2013–2015 ($m)	R&D spending as % of annual revenue 2015	Operating profit margin 2015	Number of new patents 2013–2015
SEL (before the takeover)	$15m	14.5%	5.8%	6
CCP (before the takeover of SEL)	$8m	2.3%	8.4%	2
DRS	$35m	10%	11.2%	15
HA	$18m	12%	6.2%	1

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Section A

Answer **all** questions in this section.

1 Analyse the benefits to SEL of using social media to communicate with employees and customers. [10]

2 Discuss whether the Sandson brothers made the correct decision to sell their business to CCP for $35m. [16]

3 Assume CCP is to begin selling the SEL designed robo-cleaner in your country for the first time. Evaluate a marketing strategy that CCP could use. [16]

4 **(a)** Refer to Table 2. Calculate for 2014 and 2015:

(i) labour productivity [4]

(ii) percentage of output rejected [4]

(iii) labour turnover. [4]

(b) Discuss the effectiveness of **two** ways that SEL's factory manager could improve workforce performance. [12]

5 Recommend to CCP whether it should maintain SEL's level of R&D spending in the future. [14]

Section B

Answer **one** question from this section.

6 Evaluate the significance to CCP of not undertaking strategic analysis before the decision to take over SEL. [20]

7 Evaluate the importance of strategic management to CCP's future before **and** after the decision to take over SEL. [20]

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