



UNIVERSITY OF CAMBRIDGE INTERNATIONAL EXAMINATIONS  
General Certificate of Education Advanced Level

**BUSINESS STUDIES**

**9707/03**

Paper 3

**October/November 2008**

CASE STUDY

**3 hours**

Additional Materials: Answer Booklet/Paper



**READ THESE INSTRUCTIONS FIRST**

If you have been given an Answer Booklet, follow the instructions on the front cover of the Booklet.

Write your Centre number, candidate number and name on all the work you hand in.

Write in dark blue or black pen.

You may use a soft pencil for any diagrams, graphs or rough working.

Do not use staples, paper clips, highlighters, glue or correction fluid.

**DO NOT WRITE IN ANY BARCODES.**

**Section A**

Answer **all** questions.

**Section B**

Answer **one** question.

You are advised to spend 40 minutes on Section B.

The businesses described in this question paper are entirely fictitious.

At the end of the examination, fasten all your work securely together.

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

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



## Tanroh's dilemma

### Farm incomes are falling

Tanroh studied the accounts of his farming business with a heavy heart. Sales revenue has declined steadily over the last three years. Prices of agricultural products in his country have fallen. Increased imports of food from countries with large government subsidies for farmers has led to a collapse in prices.

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The Farmers Association in Tanroh's country (Country X) has been pushing the government for similar subsidies and for import controls. The government decided against taking these actions. A government spokesman said: 'Our country cannot afford these subsidies and import controls would increase consumer prices. Anyway, these cheap imports provide incentives to our farmers to become more efficient'.

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Tanroh's farm produces maize, sugar cane and vegetables. Produce is sold at the local town market. Tanroh has been wondering what he can do to increase the revenue and profits of his farm. He is considering two alternative options.

### Option A – contract to supply Country Y food importer.

A few months ago, he was visited by a purchasing manager from a large food importing business located in Country Y. The manager was in the country trying to encourage farmers in Country X to sign four year supply contracts for fresh vegetables. He gave Tanroh details of the financial returns he could expect (Appendix A). The crops would be transported to Country Y by air and supplied to top class restaurants that insisted on the best and freshest products.

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The purchasing manager insisted that in return for reasonable prices Tanroh would have to agree to:

- Supply only the best vegetables which would require the use of expensive chemical fertilisers and pesticides. These are only obtainable from a supplier in the capital city who imports them.
- Hand pick all of the vegetables to avoid damage to them – this would make harvesting very labour intensive.
- Wash and package the vegetables ready for transportation. These processes would require Tanroh to lease expensive machinery and to employ trained staff to operate it.
- Not supply any other retailers.

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### Option B – building a safari lodge.

The alternative was to use part of his farm to build a safari lodge. This could accommodate foreign tourists, mainly from Country Y. This diversification away from farming would require careful planning. Tanroh and his sons have sufficient skills to build six cabins with a small restaurant and other facilities on a site near the lake on the farm.

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One of Tanroh's friends started his own safari lodge business three years ago. He has worked out some forecast financial returns for Tanroh's proposed project (Appendix A). Marketing the safari lodges would be a real problem, as his friend explained: 'You must decide whether to aim for a niche market or the mass holiday market with your safari lodge. You will need to do a bit of market research because the type of tourist you are aiming to sell holidays to will have a big impact on your marketing mix. Do you promote the lodge in travel brochures – or let the tourist office do it for you? Don't forget that the tourist office will be giving out details of all of your competitors to tourists too. Will you have quality furniture in each cabin to attract rich tourists? You could charge higher prices if you do. You need to think of a suitable marketing strategy.'

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Tanroh was rather confused after this talk with his friend. He had never heard of most of the terms he had used. Life seemed so much easier when he could just make a living from selling food at the local market. But now that his family's livelihood was at risk he knew something had to change. 50

#### **Other factors for Tanroh to consider**

Abi, Tanroh's daughter, is studying Management Science at the university in the capital city. She has shown her father some economic forecasts for Country X and for Country Y (Appendix B). She believes these would help him decide between the two options. Abi explains what the economic data means – and Tanroh has some doubts about whether a new direction for the business is such a good idea after all. Abi encourages him to see his bank manager to discuss his ideas. She helps draw up a business plan for both options after she explained to Tanroh the importance of this document. She also told him that he will need a human resources plan. 55 60

Finally, she told him: 'Employing more staff for either option will increase your span of control. You will need to delegate much more than you do now. You could start by trusting me and my two brothers much more than you do!'

#### **Taking the decision**

Tanroh, Abi and the two sons sat together one evening with all of the information about the two options, determined to make a decision. 65

Abi supported option B. 'We need to diversify. We could borrow the finance we need. Banks are in favour of tourism projects. Both short term and long term capital will be needed, as cash flow will be uneven given the seasonal nature of the tourist industry. I have forecast the time taken to build and market the safari lodge (Appendix C). I am confident this will be ready for the start of the tourist rush.' 70

Horatio, one of the sons disagreed. 'I support option A. Farming is what we know best. I don't want to end up making beds for tourists all day. Even though we will only receive payment at harvest time, I am sure the bank will provide for our financing needs if we show them the food importer's contract.' 75

Tanroh was ready to take the final decision. He knew that timing was critical as his market sales today had been the lowest for many years.

**Appendix A: Financial data – from the food importer and Tanroh's friend**

	Option A: Supplying vegetables	Option B: Safari Lodge
Payback on initial capital investment	2 years	2.5 years
Initial capital investment required	\$20 000	\$30 000
Forecast annual net cash flows		
Year 1	\$10 000	\$5 000
Year 2	\$10 000	\$15 000
Year 3	\$10 000	\$20 000
Year 4	\$10 000	\$24 000
Forecast annual average rate of return	25%	Tanroh's friend could not calculate this!
Net present value @10% discount	\$11 700	Tanroh's friend could not calculate this either!

10% Discount factors: 1 year = 0.91; 2 years 0.83; 3 years 0.75; 4 years 0.68

**Appendix B: Economic forecasts**

	2008	2009	2010
Country X unemployment rate	7%	8%	9%
Country X interest rate	10%	11%	12%
Country Y GDP growth per year	4%	2%	1%
Annual appreciation of Country X currency exchange rate compared to Country Y currency	3%	5%	2%

**Appendix C: Activities for completing the safari lodge project**

Activity	Explanation	Preceded by	Duration (weeks)
A	Order materials and await delivery	–	3
B	Prepare land	–	2
C	Prepare a marketing strategy	–	8
D	Build lodge bases	A, B	3
E	Fit walls and windows	D	5
F	Fit electrical connections	E	2
G	Install bathrooms	E	4
H	Fit roofs	E	3
I	Paint lodges	F, G, H	1

**Section A**

Answer **all** questions in this section.

- 1 Analyse the benefits to Tanroh of producing cash flow forecasts. [8]
- 2 (a) Analyse the importance to Tanroh of human resources planning if Option A is chosen. [8]
- (b) Do you agree with Abi that Tanroh will need to delegate if more staff are employed? Give reasons for your answer, explaining the possible advantages and disadvantages to Tanroh. [12]
- 3 (a) Using the data in Appendix C, construct a network diagram (CPA) for the safari lodge project, showing all earliest start times and latest finish times. [10]
- (b) If activity B is delayed by two weeks, briefly advise Tanroh on what steps he could take to avoid the project taking longer than 16 weeks. [4]
- 4 Recommend to Tanroh a possible marketing strategy for the safari lodge project. Fully justify your recommendation. [16]
- 5 (a) Calculate for the safari lodge option, using the data in Appendix A:
- (i) The annual average rate of return [3]
- (ii) The net present value at a 10% discount rate. [3]
- (b) Using your results from 5(a) and other information, recommend to Tanroh which of the two options he should choose. Justify your recommendation. [16]

**Section B**

Answer **one** question from this section.

- 6 Discuss whether the government should support and protect important industries in your country. [20]
- 7 To what extent will the future success of Tanroh's business depend on him setting clear objectives? [20]

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