BUSINESS AND MANAGEMENT	**9771/02**
Paper 2 Strategic Decisions	**May/June 2019**

MARK SCHEME

Maximum Mark: 100

Published

This mark scheme is published as an aid to teachers and candidates, to indicate the requirements of the examination. It shows the basis on which Examiners were instructed to award marks. It does not indicate the details of the discussions that took place at an Examiners' meeting before marking began, which would have considered the acceptability of alternative answers.

Mark schemes should be read in conjunction with the question paper and the Principal Examiner Report for Teachers.

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Generic Marking Principles

These general marking principles must be applied by all examiners when marking candidate answers. They should be applied alongside the specific content of the mark scheme or generic level descriptors for a question. Each question paper and mark scheme will also comply with these marking principles.

GENERIC MARKING PRINCIPLE 1: Marks must be awarded in line with: •   the specific content of the mark scheme or the generic level descriptors for the question •   the specific skills defined in the mark scheme or in the generic level descriptors for the question •   the standard of response required by a candidate as exemplified by the standardisation scripts.
GENERIC MARKING PRINCIPLE 2: Marks awarded are always **whole marks** (not half marks, or other fractions).
GENERIC MARKING PRINCIPLE 3: Marks must be awarded **positively**: •   marks are awarded for correct/valid answers, as defined in the mark scheme. However, credit is given for valid answers which go beyond the scope of the syllabus and mark scheme, referring to your Team Leader as appropriate •   marks are awarded when candidates clearly demonstrate what they know and can do •   marks are not deducted for errors •   marks are not deducted for omissions •   answers should only be judged on the quality of spelling, punctuation and grammar when these features are specifically assessed by the question as indicated by the mark scheme. The meaning, however, should be unambiguous.
GENERIC MARKING PRINCIPLE 4: Rules must be applied consistently e.g. in situations where candidates have not followed instructions or in the application of generic level descriptors.
GENERIC MARKING PRINCIPLE 5: Marks should be awarded using the full range of marks defined in the mark scheme for the question (however; the use of the full mark range may be limited according to the quality of the candidate responses seen).

GENERIC MARKING PRINCIPLE 6:

Marks awarded are based solely on the requirements as defined in the mark scheme. Marks should not be awarded with grade thresholds or grade descriptors in mind.

Question	Answer	Marks	Guidance

1(a)	**Calculate the asset turnover ratio as at January 2017**
	
	Revenue / net assets [1]
	
	Revenue = £4,097.3 m
	Net assets = £510.5 m [1]
	                  = £4,097.3 m / £510.5 m
	                  = 8.03 [3]
		3	Full marks for correct answer only
			
			Net assets = TA – TL = £2404.8 m – £1893.3 m = £510.5 m

1(b)	**Calculate the interest cover ratio as at January 2017**
	
	Formula: operating profit / finance costs [1]
	
	Operating profit = £827.7 m
	Finance cost = £37.5 m
	                  = £827.7 m / £37.5 m [1]
	                  = 22.07 [3]
		3	Full marks for correct answer only
			
			Alternative formula: profit before tax / finance cost [1]
			= 21.08 [1] (maximum 2 marks out of 3)

Question	Answer	Marks	Guidance
1(c)	**Comment on the usefulness to Next's directors of the result obtained in either 1(a) or 1(b).** *Answers could include:* **Asset turnover ratio:** **Knowledge (K)** • Definition of asset turnover • Often called a financial efficiency ratio **Application (P)** • Value for 2017 is 8.03 v 13.40 in 2016 (trend is down). • In 2016, fewer net assets were producing a higher revenue compared to 2017 • The business could improve this ratio by increasing the turnover generated by the net assets • Falling revenue at Next is likely to lead to further worsening of this ratio **Interest cover ratio:** **Knowledge (K)** • Definition of Interest cover • Often used in conjunction with the gearing ratio • A type of gearing ratio	6	<table><tr><th>Level</th><th>Knowledge AO1 2 marks</th><th>Application AO2 4 marks</th></tr><tr><td>2</td><td>2 marks Candidate shows clear knowledge of the IC or AT ratio. Often 2 clear knowledge statements.</td><td>3–4 marks Candidate clearly explains the usefulness of the IC or AT result using 2 examples of clear case context</td></tr><tr><td>1</td><td>1 mark Candidate shows limited knowledge of IC or AT</td><td>1–2 marks Candidate uses 1 example with limited case context</td></tr><tr><td>0</td><td colspan="2">No rewardable response</td></tr></table> If a candidate uses both ratio results then only award marks for the highest mark ratio used OFR rule applied **ARA**

Question	Answer	Marks	Guidance
1(c)	**Application (P)** • Value for 2017 is 22.07 v 27.9 in 2016 (trend is down). This could be a concern to the Next directors • The interest cover (IC) is very high and finance costs are easily covered by operating profit • The IC ratio is falling due to both operating profit falling and finance costs rising • Could be temporary due to falling profits • To be useful to directors they need knowledge of Benchmark IC in the industry • Current borrowing levels for Next are easily covered • Next directors could consider increasing borrowing		

Question	Answer	Marks	Guidance

1(d) **Richard Chamberlain (retail analyst) stated that: 'sales in Next stores were down more than 10% suggesting the price elasticity of demand has been higher than the Directors expected.' (Lines 60–62)**

Analyse two implications of this observation for Next in the short to medium term.

Answers could include:

Knowledge (K)
• Definition of price elasticity of demand
• Identification that the value for Next is elastic
• Sales are very responsive to price changes

Application (P)
• PED = –2.5 (see case data. – 10/4)
• Demand is very responsive to changes in price
• 10% increase in price could lead to a 25% fall in sales
• Next should consider reducing prices to increase revenue
• Competitors are also likely to react in the same way
• Next could reduce costs to enable competitive pricing

Analysis (A)
• Reducing prices may be offset by reducing costs thus maintaining margins
• The PED value is only an estimate
• Price is not the only factor consumers consider. Also includes quality, range, customer service
• Falling sales may be due to other factors rather than price such as falling real incomes or economic uncertainty

Marks: 13

Level	Knowledge AO1 2 marks	Application AO2 5 marks	Analysis AO3 6 marks
3		5 marks Candidate fully engages with the case context	5–6 marks Candidate fully develops analytical points
2	2 marks Candidate shows clear and precise knowledge of PED such as precise definition and/or formula	3–4 marks Candidate links case material to his answer. Expect the PED value of –2.5 and 'elastic' PED	3–4 marks Developed analysis of arguments
1	1 mark Candidate offers a sufficient definition / understanding of PED	1–2 marks Candidate makes a limited attempt to apply knowledge to the case study	1–2 marks Weak analysis of ideas, failure to develop points
0	No rewardable response		

Question	Answer	Marks	Guidance
2	**Recommend a potential strategy that Next could implement to deal with rising inflation** *Answers could include:* **Knowledge (K)** • Definition of inflation • Types of inflation **Application(P)** • Inflation is near 3% and the trend is up • Wages growth is nearer 2% so real wages are falling and consumers are likely to have lower disposable incomes • Strategic responses could include: do nothing, accept lower profit margins, cut costs, hedge currency and/or changing sources of imports **Analysis (A)** • Increased inflation could lead to higher interest rates which could cause the pound to appreciate causing lower prices for imports • Cutting costs to offset inflation may lead to a reduction in quality of service. The case study states one of the areas for savings is 'staff incentives' • Inflation may begin to fall • Could try increasing prices but high PED makes this difficult • Next could hedge against further currency falls or agree longer term fixed exchange rate deals with suppliers • Increase supplies from the UK	25	(see table below)

Level	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
3		5 marks Arguments are consistently based upon case context	6–8 marks Candidate fully develops analytical points	6–8 marks Extensive, high-quality judgement shown
2	3–4 marks Good knowledge / understanding of inflation and how to deal with it	3–4 marks Candidate makes a good attempt to apply knowledge to the specific scenario	3–5 marks Developed analysis of arguments	3–5 marks Good judgement shown
1	1–2 marks Some understanding shown of inflation	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study.	1–2 marks Weak analysis of the ideas, failure to develop points.	1–2 marks Weak judgement shown
0	No rewardable response			

ARA

Question	Answer	Marks	Guidance
2	**Evaluation (E)** • Length and size of the inflation increase • What happens to wage growth • All retailers are in a similar position so no loss of competitive position (unless they source and produce in the UK) • Exchange rate movements could become favourable		

Question	Answer	Marks	Guidance
3	**Evaluate a potential marketing strategy to increase profits from the Next Directory.** *Answers could include:* **Knowledge (K)** • Definition of a marketing strategy **Application (P)** • Price: customers currently pay for the catalogue, customers seem less price sensitive than for Next Retail as revenue as increased whilst prices have risen, delivery price options • Promotion: personalization of the experience, refer a friend scheme, • Place: largely web or app based purchasing, is a physical catalogue required • Product: mid-price, relatively conservative fashion and homeware, high quality staples **Analysis (A)** • PED for the catalogue? • What is the AED for catalogue advertising? • Is a physical catalogue that costs £3.75 best practice • Current model seems to be doing well in terms of revenue and profit • The Directory seems to provide lucrative credit opportunities **Evaluation (E)** • What are competitors doing • Supply chain and distribution is crucial • Depends on the size of the marketing budget	25	(see table below)

Level	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
3		5 marks Arguments consistently based on case context	6–8 marks Candidate fully develops analytical points	6–8 marks Extensive, high quality judgement shown
2	3–4 marks Good knowledge / understanding shown of a marketing strategy and its main features	3–4 marks Candidate makes a good attempt to apply knowledge to the specific case scenario	3–5 marks Developed analysis of arguments.	3–5 marks Good judgement shown
1	1–2 marks Some knowledge / understanding shown of a marketing strategy	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study	1–2 marks Weak analysis of the ideas, failure to develop points	1–2 marks Weak judgement shown
0	No rewardable response			

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Question	Answer	Marks	Guidance
4	**Discuss whether Next shares would be a good investment for a long term investor. Your answer should include some appropriate calculations** *Answers could include:* **Knowledge (K)** • Definition of a share • Definition of investor **Application (P)** • P/E ratio is relatively low at 10.8 • Dividend yield is 3.6% • Dividend yield including 'special dividends' is 7.7% • Share price has halved to £43.80 so may represent a buying opportunity • Next is still very profitable • Other ratios may be used **Analysis (A)** • Large dividend but is it sustainable • Performance of the Next Directory • Profit performance • Valuation grounds e.g. P/E • Share price has halved • Falling real incomes • Uncertainty re Brexit • Highly competitive market **Evaluation** • What is a 'good' investment • What type of investor; growth, balanced or income • What is meant by 'long term' • Depends on external factors beyond the control of Next	25	(see table below)

Level	Knowledge AO1 4 marks	Application AO2 5 marks	Analysis AO3 8 marks	Evaluation AO4 8 marks
3		5 marks Arguments are consistently based upon case context	6–8 marks Candidate fully develops analytical points and uses quantitative technique(s)	6–8 marks extensive high-quality judgement shown
2	3–4 marks Good knowledge / understanding shown	3–4 marks Candidate makes good attempt to apply knowledge to specific case scenario	3–5 marks Developed analysis of arguments (balanced answer)	3–5 marks Good judgement shown
1	1–2 marks Some knowledge / understanding shown	1–2 marks Candidate makes a very limited attempt to apply knowledge to the specific case study	1–2 marks Weak analysis of the ideas, failure to develop points	1–2 marks Weak judgement shown
0	No rewardable response			

ARA

Question	Answer	Marks	Guidance
4	• Depends on developments in the retail market • More information required to calculate key ratio values such as dividend cover		