

Mark Schemes and Answers to Mock Examination Paper

FOREWORD

Whilst every effort has been made to provide appropriate mark schemes for the questions posed, the mark schemes should be seen as a set of guidelines, not rigid performance criteria.

Answers to questions posed are not exhaustive. Any valid response should be given due credit.

This section also suggests where the answers put forward have met the specific assessment objectives detailed in the mark scheme, providing even further support for teachers during the run up to the examination. It should be appreciated, however, that mark schemes are open to interpretation by the individual user, and that there is always scope for differences in interpretation, even between experienced examiners.

It should be emphasised, therefore, that these mark schemes and answers are intended as an aid for the teacher who must retain full responsibility for checking specification requirements and the final delivery of subject matter to candidates. In this context, APT is always available to discuss any aspect of these mark schemes and answers, should the teacher wish to discuss APT's interpretation.

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(a) (i) Tick two statements in the table below which show that BMF Ltd operates in a global market. [2]

One mark for each correct identification. (If more than two boxes are ticked only accept the first 2 ticks).

Statement	Tick (✓)
In 2016, 20% of people who attended The Bowton Mountain Festival came from other European countries.	✓
The UK economy has experienced economic growth in each of the past five years and average incomes have risen.	
BMF Ltd's Festival T-shirts have been made by a Chinese supplier.	✓
Businesses and consumers may suffer from a rise in UK interest rates.	

(ii) Lines 12-13 of the case study state that 'The number of visitors from some European Union (EU) countries is influenced to an extent by changes in the exchange rate of pound sterling (£) against the euro (€)'.

The table below shows how the price of one weekend ticket sold to people in the Eurozone would be converted into euros at the exchange rate of £1 = 1.3 euros (€)

Price of one weekend ticket in £s	Price of one weekend ticket at a rate of £1 = 1.3 euros
£60	£60 x <u>1.3 euros</u> 78
	Price in euros

Using the table below, calculate the new price of one weekend ticket bought from BMF Ltd in euros if the exchange rate became £1 = 1.1 euros. [2]

Two marks for the correct answer.

Price of one weekend ticket in £s	Price of one weekend ticket at a rate of £1 = 1.1 euros
£60	£60 x <u>1.1 euros</u> 66
	New price in euros

(b) Section 1, lines 16 to 18 state that the theme of The Festival this year is 'Enjoying but protecting the environment and its people', and that 'The protection of the environment is one of the core values of BMF Ltd and it has taken every opportunity in previous festivals to highlight the importance of this'.

Explain one advantage to BMF Ltd of having and promoting the protection of the environment as one of its core values. [2]

One mark for stating an advantage, one mark for point of explanation of that advantage. (1 + 1)

Possible responses include:

People are becoming increasingly concerned about the impact of a business's activities on the environment, and so having the protection of the environment as one of its core values, and taking every opportunity to highlight the importance of this could improve BMF Ltd's image as an environmentally-friendly business (1). This might...

- help BMF Ltd to attract and retain customers ie Festival attendees (1 or +1). This would help to maximise ticket sales and revenue for BMF Ltd (+1).
- enable BMF Ltd to charge a higher price (than it otherwise could) for its Festival tickets (1 or +1), - as people may be willing to pay a higher price for a company with an 'environmentally-friendly' image (1 or +1). This would help to maximise revenue and increase profit and profitability for BMF Ltd (+1)
- make it easier to attract and retain good staff to help run The Festival each year (1 or +1). This would minimise recruitment and labour turnover and the associated costs (+1).
- make it easier to attract good speakers (1 or +1), which could increase the popularity of individual events (+1) and, thus, the price of tickets for these individual events (+1) and, thus, the total revenue for BMF Ltd (+1).
- make it easier to raise external finance from ethical investors (1 or +1) and, therefore, make it easier to secure the finance required to fund future plans / growth (+1).

(c) Section 2, Fig. 1 provides extracts from the summary of the Development Report for Bowton published by the Economic Development Unit of Bowton Council in 2016.

(i) The statements below concern the effects that spending cuts by Bowton Council may have on the local community. For each statement tick one box to show if it is true or false. [3]

Statement	True (✓)	False (✓)
Cuts in spending may lead to fewer services for people in Bowton.	✓	
Cuts in spending will mean that businesses in Bowton may have to pay more Council tax.		✓
Cuts in spending could involve people losing their jobs.	✓	

(ii)* The UK government is struggling to achieve its planned reduction in the government deficit and there is some pressure to increase income tax

Assess the extent to which BMF Ltd may be affected by a rise in UK income tax. [8]

Level 1 (1–2 marks): Knowledge and Application. One mark for a statement of how a rise in UK income tax may affect consumers and / or businesses in general. One mark for applying this to BMF Ltd. *Some simple ideas have been expressed. There will be errors of spelling, punctuation and grammar which will be noticeable and intrusive.*

Level 2 (3–6 marks): Analysis. Up to 4 marks for analytical points explaining how a rise in UK income tax will affect BMF Ltd. *Relatively straight forward ideas are expressed relatively clearly, legibly and appropriately. There will be some errors of spelling, punctuation and grammar which will be noticeable and intrusive.*

Level 3 (7–8 marks): Evaluation: Consideration of the **extent of the impact** of a rise in UK income tax on BMF Ltd. NB It will be possible to gain all the evaluation by developing one line of argument. *Straightforward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar but these are unlikely to be intrusive or obscure meaning.*

Possible responses include:

A rise in income tax will reduce the amount of disposable income consumers have available to spend (L1) ie the money left over after compulsory deductions such as tax and national insurance payments have been made. (L1) This might lead to consumers cutting back spending on non-necessities (L1) and / or trading down and buying cheaper alternatives. (L1) This could result in a fall in the number of people within the UK buying tickets to attend the Bowton Mountain Festival, as attendance at a Festival would be regarded as a luxury as opposed to a necessity. (L1, +1) This would result in reduced revenue and overall profit of BMF Ltd. (L2)

Alternatively, it could result in people within the UK, who usually purchase a weekend ticket, trading down and only buying a ticket to attend an individual event or a few individual events at The Festival. (L1) This is because not only is this likely to be cheaper than purchasing a weekend ticket, but it would also mean that those travelling long distances would not have the additional expense of paying for overnight accommodation. (L2) In this scenario, however, BMF Ltd is still likely to suffer a fall in revenue and overall profit. (L2)

The extent of the effect on BMF Ltd will depend on the extent and length of the increase in income tax (L3); the bigger the increase and the longer it lasts, the bigger the impact on ticket sales and, thus, the bigger the impact on BMF Ltd's revenue and overall profit. (L3)

The extent of the effect on BMF Ltd will also depend on the extent to which incomes are rising in the UK. (L3) For example, if incomes are rising at a greater rate than the increase in income tax, then consumers may not be worse off and the demand for BMF Ltd's Festival tickets and, thus, its sales, revenue and overall profit will not be affected. (L3)

(d) Section 3, lines 52 to 54 state 'Following a passionate debate about how the Festival would help the town, and about the costs of running the festival, such as policing, Bowton Council decided to give a grant of £30,000 to BMF Ltd towards the costs of The Festival in 2017'.

(i) Explain one way in which The Festival would help the town. [2]

One mark for stating a benefit to the town, one mark for a point of explanation of that benefit. (1 + 1)

Possible responses include:

- It may boost the income of local businesses (1) eg hotels, restaurants, shops, petrol stations (+1) - as The Festival attracts visitors to the town who are likely to spend money in local businesses (+1).
- It may create jobs for local people (1) - as the festival attracts visitors who may spend money in local businesses (+1), festival staff may be employed from the local area (+1).
- It could reduce the welfare benefits Bowton Council has to pay and, thus, free up money to spend on improving local services (1) - as it creates jobs and reduces unemployment (+1).

(ii) Identify two external costs that might arise from The Festival. [2]

One mark for each external cost identified.

- Drunk and badly behaved people after the nightly parties (1).
- Increased noise from Festival staff, contractors and visitors (1).
- Increased traffic congestion from people coming into the town to visit The Festival (1).
- Increased air pollution from exhaust fumes from Festival staff, contractors and visitors travelling by motor vehicle to / from The Festival (1).
- Other types of pollution - if waste generated from The Festival is not disposed of appropriately (1).

(iii) Explain one advantage to BMF Ltd of having a grant from Bowton Council towards the costs of The Festival. [2]

One mark for stating an advantage, one mark for a point of explanation of that advantage. (1 + 1)

Possible responses include:

- BMF Ltd won't have to pay the grant back (1), unlike a loan (+1).
- BMF Ltd won't have to pay interest on the grant (1), unlike a bank loan (+1).
- BMF Ltd won't lose any further control over the business (1), unlike selling more shares (+1).

(e)* Section 3, lines 61 to 62 of the case study states that 'BMF Ltd expects that more visitors from the UK will attend The Festival in 2017 compared with 2016'.

Assess whether or not the Bowton Mountain Festival is likely to gain more visitors from the UK in 2017 compared with 2016. In your answer you should use information in Fig. 1, other evidence from the case study and any other information you think is relevant. [10]

Level 1 (1–2 marks) Knowledge and application: Shows knowledge of factors which would affect sales of tickets to visitors from the UK. *Relatively straightforward ideas are expressed relatively clearly, legibly and appropriately. There will be some errors of spelling, punctuation and grammar which will be noticeable and intrusive.*

Level 2 (3–7 marks) Analysis: Explains factors that would cause an increase in demand and those which would cause a decrease in demand. *Straightforward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar but these are unlikely to be intrusive or obscure meaning.*

Level 3 (8–10 marks) Evaluation: Weighs up the factors that will influence whether demand increases or not - discusses the relative importance of the different factors.

Possible responses include:

(Factors which may increase the number of visitors from the UK to Bowton Mountain Festival in 2017 compared with 2016):

The UK economy has experienced economic growth in each of the past five years and average incomes have risen (L1). If this trend continues then The Festival is likely to gain more visitors from the UK in 2017 compared with 2016 (L2). This is because more people will be able to afford to pay for luxuries, such as attending a festival (L2).

The extent of the effect on the number of visitors that attend The Festival from the UK will depend on the extent to which average incomes rise, (L3) which, in turn, will depend on growth in the economy. (L3) This is because, along with a period of increased output, there will be falling unemployment - as firms need more labour to increase output (L2) - and, as a consequence, rising incomes (L2) The bigger an increase in economic growth, the bigger the rise in average incomes and the bigger the increase in the number of visitors from the UK to The Bowton Mountain Festival. (L3)

Section 3 of the case study also informs us that BMF Ltd has secured a grant of £30,000 from Bowton Council towards the cost of The Festival and had asked for this grant so that it could advertise The Festival more than it had done in previous years. (L1) Greater investment in advertising could raise awareness of The Festival amongst more people and, ultimately, increase the number of people attending The Festival this year. (L2) However, whether or not it increased the number of visitors from the UK compared with 2016, would depend on whether or not this advertising was directed at promoting The Festival amongst people within the UK, as opposed to people in other European countries. (L3)

(Factors which may reduce the number of visitors from the UK to Bowton Mountain Festival in 2017 compared with 2016):

However...

The UK government is struggling to achieve its planned reduction in the government deficit and there is some pressure to increase income tax. (L1) If UK income tax rises, people within the UK will have less disposable income (the money available for consumer to spend) on luxuries such as attending a festival. (L2) Therefore, The Festival may gain fewer visitors from the UK in 2017 compared with 2016. (L2) The extent of the effect on the number of visitors will depend on the extent of the rise in income tax; (L3) the bigger the increase in income tax the bigger the impact on the number of visitors likely to attend The 2017 Festival from the UK. (L3)

The Bowton Council's local economist also forecasts that interest rates in the UK will rise (L1). If this happens, this will reduce the amount of disposable income people have available to spend on luxuries, such as attending a festival. (L2) This is because it costs more to borrow and that mortgage holders have more interest to pay, and thus, less discretionary income ie money to spend on non-essential items. (L2) Consumers are also more likely to save rather than spend - as there is more reward for saving. Therefore, The Festival may gain fewer visitors from the UK in 2017 compared with 2016. (L2) The extent of the effect on the number of visitors will depend on the extent of the rise in the interest rate; (L3) the bigger the increase in the interest rate, the bigger the impact on the number of visitors likely to attend The 2017 Festival from the UK. (L3)

The extent of the impact on the number of visitors attending The Festival from the UK arising from an increase in income tax and / or interest rates would also depend on whether average incomes also rose and, if so, by how much. (L3) For example, if incomes rose by a greater amount than any rise in income tax and / or interest rate, then The Festival may gain more visitors from the UK in 2017 compared with 2016, despite higher income tax and / or interest rates - as people will have more disposable income to spend on luxuries, such as attending festivals. (L3)

2

(a) Section 4, Fig. 2 of the Case Study provides us with a breakdown of the costs to BMF Ltd of the Bowton Mountain Festival.

Calculate what the actual Film costs were in 2016, and what the Film costs are expected to be in 2017.

Two marks for the correct answer for 2016, and two marks for the correct answer for 2017.

Answer:

2016: £280,000 x 0.05 (1) = £14,000 [2].

2017: £350,000 x 0.07 (1) = £24,500 [2].

(b) Section 5 of the case study tells us that BMF Ltd's Chinese supplier uses flow production to make standard T-shirts in very large quantities and that some of these T-shirts are then printed with The Festival design, using batch production.

(i) The table below lists four statements about flow production. For each statement tick one box to show if it is an advantage or disadvantage of flow production. [4]

Statement	Advantage (✓)	Disadvantage (✓)
It can be expensive to set up - due to the specialist equipment / machinery often required.		✓
Labour costs are low as processes are often automated.	✓	
Large quantities are produced and so there is maximum opportunity for economies of scale.	✓	
A production line may be difficult to adapt once set up to produce a particular product.		✓

(ii) Explain one reason why the Chinese supplier uses batch production to print BMF Ltd's Festival T-shirts. [2]

One mark for a relevant reason and one mark for an explanation of that reason. (1 + 1)

Possible responses include:

Batch production is suitable when a limited number of the same product is required for a limited period of time (1). It is, therefore, appropriate for the printing of BMF Ltd's Festival T-shirts as only a limited number of T-shirts with the same design are required to be printed at a certain time each year (+1).

Students could also be given credit for explaining the advantages of batch production over other methods of production, (as opposed to explaining why it is particularly appropriate for The Festival T-shirts):

- Flexible production (1) - enables the Chinese supplier to ...change from printing one type of t-shirt to another type of t-shirt (+1) ...produce a range of printed t-shirts to meet different customer requirements (+1). This can help maximise sales and market share (+1).
- Higher productivity (than job production) (1) - as workers are able to specialise and so become quicker at doing their job (+1).
- Lower labour costs per unit (than job production) (1) - as workers are able to specialise and so become quicker at doing their job (+1).
- Improved quality / Lower costs associated with poor quality (1) - as workers are able to specialise and, thus, become experts at doing their job - making fewer mistakes (+1).
- Unit material costs may be lower (than job production) (1) - because there is more scope for economies of scale (+1).
- Lower unit costs (than job production) (1) which can result in ...greater competitiveness over price (+1) and / or ...higher profit margins (+1).

(c) Section 5, lines 88 to 90 tell us that BMF Ltd has decided to obtain quotes for T-shirts from a smaller, UK supplier. The UK supplier claims to have 'excellent quality control systems and a good record for delivering orders on time'.

(i) Complete the following sentence using three of the words below. [3]

rejects making testing returns

One mark for each correct insertion.

Quality control is the process of inspecting and testing products in order to reduce the number of rejects in the production process and returns from customers.

(ii) Explain one method of quality control that this smaller, UK supplier might use. [2]

One mark for stating a method of quality control, one mark for an appropriate explanation of it. (1 + 1)

Total Quality Management (TQM) / Self-inspection (1) ie where workers are responsible for checking the quality of the work they do (1 or +1) at each stage of the production process (+1) not just once after the T-shirts have been manufactured and printed (+1).

The use of specialist quality control departments / staff (1) to carry out inspections at the end of the production process (+1).

Random sampling (1) - inspecting a selection of the T-shirts (+1) eg testing the seams (+1).

(d) In Section 5, lines 85 to 87 state that 'some business analysts are suggesting that Chinese firms are becoming too big and, as a consequence, may start to suffer from diseconomies as opposed to economies of large scale production'.

(i) Complete the following sentence using two of the words below. [2]

rise total average fall

One mark for each correct insertion.

Diseconomies of large scale production are factors that cause the average cost of producing a product to rise as a business increases its output.

(ii) Explain one type of diseconomy of scale that Chinese firms might suffer from as a result of 'becoming too big'. [3]

One mark for diseconomy identified, one mark for each point of explanation, up to a maximum of two marks. (1 + 2). No marks for saying that 'it will increase costs' - needs to be more specific.

Possible responses include:

Problems with co-ordination and control (1)

- As a business increases in size regular meetings and increased supervision / checking procedures may be required to fulfil this function (+1) Therefore, overheads can increase quite significantly in large firms (+1).

Problems with communication (1)

- This is because the larger the firm, the more levels there are through which communication has to flow (+1). This can result in:
 - slower decision making (+1).
 - decreased efficiency (+1).
 - workers feeling isolated and far removed from organisational goals (+1).

Problems with staff motivation (1)

- Greater supervision (in order to check and co-ordinate activities) and difficulties with communication can lead to poor relations between management and staff, and workers feeling alienated (+1). This can lead to:
 - low morale and lack of motivation (+1).
 - decreased productivity (+1).
 - increased absenteeism (+1).
 - labour turnover and the associated costs (+1).

(e)* Discuss whether or not BMF Ltd should use the smaller, UK supplier for the supply of Festival T-shirts in 2017, instead of its Chinese supplier. In your answer, you should use the information in Section 5, other evidence from the case study and any other information you think is relevant. [10]

Level 1 (1–2 marks) Knowledge and application: Displays knowledge of factors affecting decisions over suppliers and applies it to BMF Ltd. *Relatively straightforward ideas are expressed relatively clearly, legibly and appropriately. There will be some errors of spelling, punctuation and grammar which will be noticeable and intrusive.*

Level 2 (3–5 marks) Analysis: Makes use of data and information in Section 5 and/or other evidence provided in the case study to analyse the case for **or** against using the UK supplier or for **or** against using the Chinese supplier. *Straightforward ideas have been expressed with some clarity and fluency. Arguments are generally relevant, though may stray from the point of the question. There will be some errors of spelling, punctuation and grammar but these are unlikely to be intrusive or obscure meaning.*

Level 3 (6–10 marks) Evaluation: Weighs up issues, and / or considers what the decision is dependent upon, and / or makes a final judgement which is justified in light of the evidence presented.

Points for moving to the smaller, UK supplier:

There have been reports earlier in 2016 in a UK newspaper criticising the Chinese supplier for the way it treated its employees (very low wages and concerns over health and safety practices in its factories), as well as suggesting the supplier used too many non-renewable resources. If these reports are true, using such a supplier would be in conflict with the theme of this year's Festival 'Enjoying but protecting the environment and its people', as well as BMF Ltd's core value 'protection of the environment'. (L1) Hence, continuing to use this Chinese supplier could have serious negative consequences for BMF Ltd - because customers and other stakeholders may judge BMF Ltd not only in terms of its own compliance with an ethical code, but also in terms of its choice of suppliers. (L2) For example, BMF Ltd could struggle to secure the staff it requires to run The Festival, and / or any external finance required to pay for The Festival running costs or the purchase and selling costs of The Festival T-shirts, and / or struggle to secure the number of Festival attendees required to maintain sales and profits and keep shareholders happy. (L2)

The extent to which BMF Ltd would be negatively affected in this way would depend upon the extent to which BMF Ltd's stakeholders, in particular its customers and shareholders, are aware of and, more importantly, concerned about the reports in the newspaper criticising the Chinese supplier. (L3) This is because, without customers the business will not survive and, in terms of shareholders, the directors of limited companies have a duty to act in the best interest of their shareholders. (L3) It may, however, be argued that, regardless of the awareness and attitudes of BMF Ltd's customers and shareholders, if, upon further investigation, the reports are proved to be true, then BMF Ltd should seek an alternative, more ethical supplier - because it is morally wrong to act unethically or, in this case, to be seen to support businesses that act unethically. (L3)

The smaller UK, supplier claims to have 'excellent quality control systems' and 'a good record for delivering orders on time'. (L1) Both are important in helping BMF Ltd to maintain a good reputation in terms of the quality and delivery (with regard to website customers) of its Festival T-shirts (L1) and, thus, in helping to maximise sales, revenue and profits generated from the sale of the T-shirts. (L2) These are, however, just 'claims' and these claims would need checking to ensure they are truthful. Without such an investigation BMF Ltd would be taking a big risk in moving from its current supplier, which 'has always been very reliable'. (L3)

Points against moving to the smaller, UK supplier:

The reports about the Chinese supplier may not be true and it would be unfair of BMF Ltd to move to another supplier without a proper investigation to establish the facts. (L1) The Chinese supplier claims the reports aren't true, and the fact that it has invited reporters to visit any of its factories without notice suggests it has nothing to hide and that the reports aren't true. (L2) In addition, the fact that, prior to this year, BMF Ltd had never been made aware of any of these concerns might also add weight to this argument. (L2) On the other hand, issues might only have arisen this year - as a result of the Chinese supplier growing and increasing its output at a rate that has not allowed appropriate systems to be put in place to ensure effective communication, coordination and control and, thus, it has begun to suffer from diseconomies of scale. (L2) These could include failure to communicate expectations within its various factories with regard to pay, health and safety procedures and the use of non-renewable resources, and / or insufficient checks being carried out with regard to these things. (L2) If the Chinese supplier is suffering from diseconomies of scale then unit costs will start to rise and BMF Ltd may see the price of the T-shirts rise in the future. (L2) If these rose beyond those charged by the smaller, UK supplier then BMF should use the smaller UK supplier, in order to maintain profit margins and overall profit and, ultimately, protect the interests of its shareholders. (L3)

For a business to meet the expectations of its customers, it is important for its suppliers to be reliable - in terms of delivering the right quantity of goods in the right quality at the right time. (L1) With regard to this, the case study states that, up until now, BMF Ltd has enjoyed a mutually beneficial partnership with its Chinese supplier, which has always been very reliable. (L1) It would, therefore, be risky to move to an alternative supplier without investigating whether their claims regarding 'excellent quality control systems' and 'a good record for delivering orders on time' were true. (L2)

The prices charged by the smaller, UK supplier are higher than those charged by the Chinese supplier, and this would increase BMF Ltd's costs. (L1) For instance, if BMF Ltd purchased 5,000 T-shirts from the smaller, UK supplier it would cost £5,000 more, ie 20% more, than if it purchased these T-shirts from its Chinese supplier. (L2) This would reduce the profit margin on each T-shirt sold and overall profit BMF Ltd would make on the T-shirts, (L2) unless BMF Ltd were able to raise its prices. (L3) In general, as price rises demand falls (and vice versa). (L1) Therefore, raising price could negatively affect demand and, thus, sales of BMF Ltd's Festival T-shirts. (L2) However, this depends on a number of factors and, in this particular case, given that the Festival T-shirts have become 'very popular' and are seen as something as a 'collectors item' among outdoor pursuits enthusiasts (lines 68-69), people may be willing to pay a higher price. (L3)

There is plenty of opportunity for students to demonstrate evaluative skills throughout their answer to this question. Alternatively, this may be demonstrated at the end of their answers, with an overall judgement either way - for example:

If, upon further investigation, the newspaper reports about the Chinese supplier are true I think BMF Ltd should use the smaller, UK supplier over the Chinese supplier because it is morally wrong to act unethically or, in this case, to be seen to support businesses that act unethically.....

I don't think BMF Ltd should use the smaller, UK supplier if it means the cost of its supplies of Festival T-shirts increases. **This is because** if costs rise, unless BMF Ltd can raise price without losing customers, its profits and thus dividends to shareholders will fall, and BMF Ltd's directors have a responsibility to act in the best interests of the company's shareholders.

3

(a) Fig. 6 of the case study is a cash flow forecast for the sale of T-shirts related to the 2017 Festival.

(i) Use the information in Fig. 6 to identify how much finance BMF Ltd will need to fund the expected cash shortfall in July. [1]

One mark for the correct answer.

£11,200

(iii) Assess the usefulness of cash flow forecasts to businesses such as BMF Ltd. [6]

Level 1 (1-3 marks) Analysis: States uses or limitations.

Level 2 (4-6 marks) Evaluation: Discussion which questions the extent to which cash flow forecasts can be useful. The answer must consider use and limitations and consist of much more than two lists (ie a list of uses and a list of limitations) to secure L2 marks. This might be indicated by a connective eg *however... despite this...*

Possible responses include:

Cash flow forecasts are an essential part of business planning and loan applications. (L1)

Producing a cash flow forecast will enable BMF Ltd to see how much cash will be held / available in the business at a given point in time in the future (L1) and, therefore, it will enable BMF Ltd to assess the business's ability to meet debts as they fall due, ie its solvency or liquidity position (L1), identify any imminent cash-flow problems (L1) and, more importantly, to plan / seek ways - well in advance - to prevent a potential cash shortage (L1).

Producing a cash flow forecast could help BMF Ltd make key business decisions, (L1) eg whether or not to expand or reduce existing Festival activities (L1), include new goods / services / activities at The Festival (L1), or invest in new / additional resources / facilities (L1), as it would highlight potential cash flow problems arising from such decisions / activities that could put the business at risk (L1).

Producing a cash flow forecast could help BMF Ltd secure external finance eg in the form of a bank loan if required (L1). This is because BMF Ltd's bank would use it to assess the business's future ability to meet interest payments and pay back any loans or overdrafts taken out (L1).

Cash flow forecasts could also help BMF Ltd's senior management to control the business (L1) by setting targets relating to cash flow (L1) eg targets such as maintaining a maximum spend through the use of budgets (L1), reducing Festival T-shirt inventory (stock) levels - to free up cash tied up in stock (L1), increasing or reducing a bank overdraft by a certain amount by a certain date (L1), increasing the credit period granted by suppliers for purchases (L1).

(Each of the above paragraphs provides more than just a statement of uses - it provides relevant explanations with examples. However, both sides ie use AND limitations should be considered to secure L2)

However, *(Moving into secure L2 - considering both sides...)*

The cash flow forecast figures might be different to actual because the forecast figures might be based on inadequate research / information. It may also be because forecasting cash flows can be very difficult to do accurately, even with the best research and careful attention to detail. This is because there are numerous factors affecting the forecast figures that are outside a business's control, some of which may be difficult to predict...

In the case of BMF Ltd, for instance, suppliers of The Festival T-shirts may unexpectedly put up prices, resulting in its costs (expenditure) being higher than forecast. A change in income tax or interest rates could also affect BMF Ltd's forecast for sales (income from cash inflows), by increasing or reducing demand for its products (as people have more or less income to spend on goods and services), as well as its expenditure (cash outflows) - if BMF Ltd has funded investment on borrowed funds eg an overdraft or bank loan.

(Secures high Level 2 overall - both use and limitations have been considered with the majority of points raised being developed, as opposed to just a list of use and limitations with no development / explanation).

(b) Section 5, lines 93-95 state that, 'in previous years, BMF Ltd has financed the purchasing and selling costs of the T-shirts using an overdraft', and that 'This year it is considering asking its supplier for trade credit or taking out a bank loan'.

(i) Complete the following sentences using four of the words below. [4]

more limit before less after

One mark for each correct insertion:

An overdraft will enable BMF Ltd to withdraw **more** money from its bank account than that deposited in it, to an agreed **limit**. This will help BMF Ltd to pay for the purchase and selling of the T-shirts, **before** it receives money from the sales of its T-shirts (+1).

(ii) Recommend whether BMF Ltd should ask its supplier for trade credit, or take out a bank loan to finance the purchasing and selling costs of the T-shirts. Give reasons for your recommendations. [8]

Level 1 (1–2 marks) Knowledge and application: One mark for each knowledge point made.

Level 2 (3–6 marks) Analysis: One mark for each point of analysis of either advantages or disadvantages of trade credit or bank loans.

Level 3 (7-8 marks) Evaluation: Weighs up in context. One mark for each point that evaluates the decision.

Possible responses include:

Trade credit is when a business (in this case the supplier of Festival T-shirts) provides their customers (in this case BMF Ltd) with an interest free period of grace in which to pay for their goods or services once received. (L1) This is usually 30 days, but in practice it is nearer 70 days. (L1).

Trade credit has the advantage over a bank loan in that it is interest free. (L2) However, some businesses give their customers discounts for paying promptly and, if this is the case with the Chinese supplier and BMF Ltd, by using trade credit BMF Ltd might lose out on discounts previously enjoyed for paying promptly. (L2) This would increase the cost of the T-shirts and, thus, reduce profit margins and the overall profit made on Festival T-shirts sold. (L2)

A bank loan is where a business is advanced a set figure and repays the amount over an agreed period of time, at an agreed rate of interest. (L1) Interest is fixed or variable, although many lenders provide the opportunity of switching from one to the other at pre-specified periods. (L1)

Bank loans are relatively straightforward to arrange - as long as the business is solvent and has a satisfactory financial history (L2) and, unlike overdrafts, which BMF Ltd has currently been using to fund the T-shirts, there is no danger of the loan being recalled before the agreed date expires. (L2) BMF Ltd would, however, have to pay interest on the loan taken out in addition to repaying the loan after the agreed period of time (L1). This increases costs, which has implications for cash flow and reduces profit. (L2) Interest rates might also rise during the period of the loan, which would increase the cost of taking out the loan, if the loan has a variable rate as opposed to fixed rate of interest. (L2)

In addition, unlike asking for trade credit, taking out a loan usually requires security ie collateral in the form of fixed assets, which the bank can claim if interest payments / loan repayments are not met. (L2)

Possible Level 3 response:

BMF Ltd should first and foremost ask its supplier for trade credit. This is because, unlike bank loans, this would be interest free and so would not increase BMF Ltd's costs and reduce profit - as long as the business does not lose out on discounts for paying promptly. If it is likely to lose out on discounts for paying promptly, then BMF Ltd should compare the increase in price paid for the T-shirts arising from the lost discount to the interest applicable on the bank loan, and only opt for bank borrowing if the impact on profit is likely to be less.

(c) Section 6 tells us that there will be many similar businesses selling their goods and services to festival visitors on The Festival Field. This includes five food stalls, six bars, twenty-two specialist retailers of outdoor pursuits products and seven adventure holiday firms.

Explain one way in which competition between businesses may affect each of the following: [6]

One mark for correctly stating the effect, one mark for a point explaining the effect. (1 + 1 x 3)

Possible responses include:

(i) consumer choice; [2]

Consumers will have greater choice (1) because:

there will be a number of sellers who they can buy goods and / or services from (+1).

there will be pressure on sellers to try to make their products and / or the service they provide different from other businesses in order to win sales (+1).

(ii) prices charged. [2]

Prices may be lower (1) because people will buy from the seller with the lowest price (+1) unless the product is considered to be superior in ways that customers value (+1).

(iii) Profits. [2]

Profits may be lower (1) because prices will be lower (+1) reducing the profit margin on products / the difference between revenue and costs (+1)

(d) Section 6, lines 117-118 state that Spirit of Adventure buys in additional stock to sell during The Festival weekend.

Identify and explain one cost to Spirit of Adventure of carrying a higher level of stock.

One mark for identifying a relevant cost and one mark for an explanation of that cost. (1 + 1)

Possible responses include:

- Additional storage costs (1). This includes costs involved in purchasing or renting additional storage space (+1), additional labour required to monitor / check stock is secure (1), additional insurance against fire and theft (1).
- Costs of finance (1). Spirit of Adventure may have to borrow to purchase this additional stock (1), via an overdraft for example (+1) because it may take time to sell all the stock and receive the money from customers (+1).
- Opportunity cost (1). Money tied up in stocks cannot be released until that stock has been sold and paid for (+1). Opportunity cost is, for example, the interest that could be earned on this money (+1) or benefit(s) that could be gained from freeing up storage space for more productive use (+1).
- Stock deterioration or obsolescence (1). If employees know there is plenty of 'back-up' stock they may take less care when handling items (+1) - more might become damaged, or stolen (+1). If the additional stock does not sell during The Festival weekend it may become unfashionable / out of date (+1) and, thus, prove difficult to sell in the future (+1).