Cambridge International A Level

Cambridge International Examinations
Cambridge International Advanced Level

BUSINESS **9609/32**

Paper 3 Case Study **February/March 2018**

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Allnatural Products (AP)

AP is a public limited company (plc) with its Head Office and final processing and packaging factory in country X. AP produces and sells a large range of skin creams and hair products made from natural ingredients. AP has expanded very quickly since becoming a plc and sells its products through large retailers worldwide. However, the market is becoming increasingly competitive, with retailers offering more of their 'own brand' natural skin and hair products.

Table 1: Percentage change in AP's sales by geographical area

Area	2015	2016	2017
EU	1%	(2%)	(3%)
USA	4%	3%	(1%)
Asia	5%	6%	8%

*Figures in brackets indicate negative change

Economic conditions

The economy of country X is recovering slowly following a recession. Interest rates and inflation remain low. Unemployment is falling and the central bank is predicting a rise in interest rates later in 2018. The Government of country X has decided to end international trading agreements with neighbouring countries. Since the decision, the currency of country X has depreciated by an average of 10% against major currencies. Some economists are now predicting that the ending of trading agreements will lead to a major slow-down in country X's economy. However, AP's CEO, Mary, believes that the new trading environment could offer opportunities for businesses in country X.

Marketing

AP's current range of skin and hair products is aimed mainly at female customers of all ages. The AP brand is well-known for its corporate social responsibility (CSR) including an ethical approach to the sourcing of raw materials and fair prices paid to suppliers. AP also promises customers that ingredients and finished products are never tested on animals.

AP views CSR very seriously and donates part of its profits to support the education of girls in Africa. The packaging of every AP product displays a label with the promise 'the purchase of this product will help a girl in Africa attend school'.

AP's marketing department is working hard to increase the number of large retailers in Asia and the USA who sell the company's hair and skin products. Cherry, the Marketing Director, said at a recent Board meeting: 'our marketing strategy needs to highlight our ethical approach in order to improve sales in these international markets'.

Finance

Dividends to shareholders had increased every year since the company went public eight years ago, but last year both profits and dividends decreased. At the recent Annual General Meeting (AGM) some shareholders expressed their dissatisfaction about the lower dividend and also commented that AP did not seem to be focused on increasing shareholder value.

Mary announced her growth plans for AP at the end of the AGM. In order to make necessary investments in the company's future, she warned shareholders that it may be necessary to decrease dividends again next year. A summary of AP's accounting data and forecasts for 2017–18 is shown in Table 2.

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Table 2: Summary of AP's accounting data and forecasts, as at December 2017

	2017 (actual)	2018 (forecast)
Revenue ($m)	550	580
Operating profit ($m)	56	60
Share price	$4 per share	$3.80 per share
Dividend per share	$0.30 per share	$0.28 per share
Retained earnings ($m)	10	12
Gearing ratio	35%	35%

Operations

AP sources raw materials from many countries in Africa and Asia. The first stage of the production process is often completed in the country of origin; for example, shea butter made from shea nuts in Africa. AP ensures that producers are paid a fair price for the raw materials.

AP's main factory in Africa is old and needs replacing. Production is labour intensive. Recently there have been media reports of worker exploitation and even the use of child labour. Mary has asked the Operations Director to investigate the cost and feasibility of replacing the old factory with a new larger factory, with up-to-date computerised equipment. This would enable all stages of the production and packaging of products to be completed in the new African factory. AP would send a management team from Head Office to supervise this project, including the introduction of modernised processes.

The Operations Director, Nigel, has calculated that the total cost of the project will be $15.5m. He has also estimated the durations of the activities needed to complete the project. These are shown in Table 3. AP's Board of Directors has decided to go ahead with the project, based on these estimates.

Table 3: Estimated times for activities for building and equipping the new factory

Activity		Duration (weeks)	Preceding activities
A	Plan new building and employ building contractor	8	None
B	Remove existing building	2	A
C	Clear and prepare the site	1	B
D	Deliver building materials to site	1	A
E	Complete building work	4	C, D
F	Connect water supply and electricity	2	E
G	Install machinery	3	E
H	Recruit new workforce	4	A
J	Train workforce on site	1	F, G, H.

Human resource management for the new factory

Once the factory is functioning it will be managed and operated by some existing AP employees as well as by new recruits. The workforce in the new factory will be organised into product teams, each of which will be supervised by a team leader. Each team will be set production targets every month and all team members will receive a bonus if targets are met. All workers will be members of Kaizen groups which will meet monthly. Suggestions for new products will also be welcomed by factory managers, who will pass them on to the Head Office marketing team for consideration.

Selling in new markets – a strategic choice

Mary would like to expand AP and she has been carrying out some research. She has identified two possible options for growth.

Option A: Working together with a popular European holiday hotel group, AP would set up and operate small salons within each hotel. AP products would be used in services such as hairdressing and beauty treatments. The hotel would also buy AP products in bulk and provide them for guests to use in their rooms.

Option B: Develop and launch a new range of products aimed at the market for men's skin and hair care. Market research has suggested that this is a high-growth market for products such as skin moisturiser.

Table 4 shows selected information for each option.

Table 4: Information for the two options

	Option A: Salons in hotels	Option B: New range of products for men
Estimated cost of initial investment	$10m	$12m
Forecast payback period	4 years 6 months	3 years
Greatest constraining factor	Lack of AP directors' experience in setting up and operating salons	Existing product development focus on products for women
Greatest driving factor	Increasing the market for AP hair and skin care products	Entry into the growing market for hair and skin care products aimed at men
Estimated chances of strategy success	70%	60%
Greatest risk factor	Seasonal demand for holiday hotels	Competitors already established in the market

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