Cambridge International Examinations
Cambridge Pre-U Certificate

BUSINESS AND MANAGEMENT (PRINCIPAL) **9771/02**

Paper 2 Strategic Decisions **May/June 2018**

3 hours

Additional Materials: Answer Booklet/Paper

0525666818

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 an HB pencil for any diagrams, graphs or rough working.
Do not use staples, paper clips, glue or correction fluid.

DO **NOT** WRITE IN ANY BARCODES.

Answer **all** questions.

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 syllabus is approved for use in England, Wales and Northern Ireland as a Cambridge International Level 3 Pre-U Certificate.

This document consists of **7** printed pages and **1** blank page.

DC (CE) 145245/3

Share plc

Introduction

Share was founded in 1990 and is one of the UK's leading independent stockbrokers. The business provides services to members of the general public to buy and sell shares in public limited companies and investment products.

Clients can make their own decisions about which shares to trade. However, there is guidance available through telephone conversations with an advisor. The *Share* website also gives investors investment ideas and company information. They also publish a magazine called 'The Shareholder' which helps investors to make informed decisions. Currently (2016) 78% of all transactions are conducted through the website, with the remainder completed by telephone.

Revenue streams for *Share*

Revenue primarily comes from three different streams (2016):

A: Dealing commission (45% of revenue). *Share* charges a fee for each transaction to buy or sell shares. Typically this is 1% of the value of each transaction. If investors trade regularly they can choose to pay £20 + VAT per quarter to reduce the fee to a flat rate of £7.50 per transaction.

B: Administration fees (46% of revenue). All investment accounts have an account administration fee. This is typically a monthly fee of £1.50 + VAT per account. *Share* is differentiated from its competitors as the administration fees are fixed and not based on the value of assets. This has helped the company win various awards and to be ranked favourably on comparison websites.

C: Interest income (9% of revenue). *Share* is permitted to earn interest on the cash that is not currently invested in shares but held by investors in their accounts. *Share* uses short term deposit accounts to earn this interest income.

Interest rates

Interest rates affect the revenues and profitability of *Share* because the company can use investors' cash to earn interest. A 0.25% increase in interest rates translates into £0.4m of extra revenue for *Share*. The key variables for this revenue stream are the value of customer cash held and the interest rate earned. Interest accounted for 9% of the group's revenue in 2016 (12% in 2014). In recent years low interest rates have meant far less revenue has come from this source. Higher interest rates would increase this income for the company. However, higher interest rates may encourage clients to take their cash out of *Share* investment accounts and place it in a savings account with a bank. Since the 2008 financial crisis, regulations on financial institutions have become more onerous and the safety of customer funds is a key concern. *Share* can no longer keep customer cash in interest-earning accounts of a fixed term of over 30 days. This is an issue for *Share* as longer term accounts attract higher interest rates.

Marketing and promotion

Marketing is the second largest cost for *Share*. In 2015 it spent £2.3m (£2.2m in 2014). The money is largely spent on promoting the activities of the company, its brand, products and website. It is hoped the increased brand awareness translates into more customers. At the end of 2015 the company had 251,000 customer accounts (248 000 in 2014). As part of the marketing process the company monitors customer satisfaction. A review site for customers called Trustpilot found that over two-thirds of the 400 reviewers gave *Share* the maximum 5 star rating for customer satisfaction. *Share* is very proud of its customer satisfaction and as part of this it also monitors complaints. In 2015 there were 2.18 complaints per thousand customers compared to 2.86 in 2014.

Share marketing executives have generally found it much easier to collate tangible evidence of customer satisfaction and complaints compared to measuring the impact of specific marketing campaigns. Industry experts in this field estimate the advertising elasticity of demand is between 0.8 and 1.3 in the financial services sector. *Share* is keen to quantify the impact of its advertising and promotions to check they offer value for money. Company directors are always keen to review the advertising elasticity of demand figures.

A recent marketing campaign over 10 weeks in a specialist share-trading magazine gave some revealing results. Initial market research before the advertising found that approximately half of the magazine's readership could recall *Share*'s website as www.share.com. After the campaign ended, 1024 subscribers to the magazine were surveyed. Awareness of the *Share* website increased from the expected 512 positive responses to 544 positive responses (1 standard deviation = 16). This data was then compared to normal distribution tables and the marketing department assessed the degree of confidence to which the campaign had been successful.

(z)	Areas under the normal curve from mean to z
1.0	.3413
2.0	.4772
3.0	.4987

Table 1: Standard normal curve areas

Corporate Social Responsibility (CSR)

The *Share* 2015 Annual Report states that:

‘The principal objective of the corporate and social responsibility policy is to ensure a long term sustainable future for *Share*, all its stakeholders and the communities in which it operates.’

(CSR) Finance education: current CSR policy includes financial education such as running the national Year 12 investment competition called Shares4Schools. *Share* typically funds half of the initial investment capital of £1500 for the teams. The Executive Chairman Gavin Oldham founded The Share Foundation, which is a charity that establishes and administers savings accounts for young people in local authority care.

(CSR) Charitable activities: staff and the company raised £6000 (£2000 in 2014) for a national charity.

(CSR) The environment: the environment is also considered a priority. The company has invested in more bicycle parking at its main office and helps reduce congestion by permitting some flexible working patterns for its staff. The company is also keen to reduce paper and energy waste.

(CSR) Customers: the company could also claim to look after the interests of its customers and numerous awards provide evidence of this (see Table 2).

Award	From
Highest overall client satisfaction	Investment trends 2015 UK online broking report
Best customer service	Investment trends 2015 UK online broking report
Best online stockbroker	ADVFN finance awards 2015
Self select ISA provider of the year	ADVFN finance awards 2015
Best stockbroker	Online personal wealth awards 2015
Best customer service	Online personal wealth awards 2015
Best online broker	Personal finance awards 2015/16
Best customer service	Shares magazine 2015

Table 2: Recent *Share* awards

Whilst *Share* is proud of its CSR policy, some business analysts have questioned whether its motives for CSR are driven by self-interest.

Recruitment and retention of employees

Looking after the needs of its staff is a key focus for *Share*'s directors and human resource management department. Unemployment in the finance sector of the economy is relatively low and talented staff are in high demand. The company is keen to retain its employees and offers a pension scheme that is generous compared to similar companies. Sick pay is above statutory levels and the company operates profit sharing and a share incentive scheme. In 2015 *Share* repeated the annual staff survey that started in 2011. This showed strong levels of satisfaction amongst the workforce with 87% (91% in 2014) agreeing with the statement: 'I am proud to work for *Share*' and 88% (90% in 2014) agreeing that they 'would recommend *Share* as a good employer'. Recruitment is also important as the business has grown. The number of employees has increased with the largest additions to the Technology and Marketing departments. The current total number of staff in 2015 is 169 (149 in 2014) and the annual staff turnover is 22% (15% in 2014).

IT (information technology) investment

Share is proposing to invest £1m in IT in the coming year, which it expects to have a positive impact on the business (see Table 3). The company currently does not have a mobile app, which is a major concern as this is a growth medium for share dealing. Accordingly, the company intends to launch a mobile app in 2016. Significant investment is also being used to further improve the website which some customers have started to view as 'clunky' and old-fashioned. The website will be made more user-friendly and have an increased number of features to guide investors. The company is keen not to be content with past success. One industry analyst described the IT investment as a good decision because long term growth generated by the improved IT systems would more than compensate for the initial outlay.

Year	Net cash flow	Discount factor 6%
0	(£1m)	–
1	£250 000	0.94
2	£300 000	0.89
3	£500 000	0.84
4	£510 000	0.79

Table 3: IT investment predicted returns

	2015 £000	2014 £000
Revenue	14 050	15 042
Cost of sales	(14 944)	(14 590)
Operating profit/loss	(894)	452
Investment revenues	276	308
Sale of minority stakes in other businesses	1 479	60
Profit before tax	861	820
Taxation	(196)	(130)
Profit for the year	665	690

Table 4: Extract from *Share* income statement as at 31 December 2015

	2015 £000	2014 £000
Non-current assets	8 083	9 405
Current assets	19 716	21 316
Total assets	27 799	30 721
Current liabilities	7 681	8 450
Net current assets	12 035	12 866
Non-current liabilities	1 418	1 594
Total liabilities	9 099	10 044
Net assets	18 700	20 677

Table 5: Extract from *Share* balance sheet as at 31 December 2015

Read all the case study material and then answer all the following questions.

Section 1

1 **(a)** Calculate the payback period of the IT investment. [3]

(b) Calculate the return on capital employed in 2014. [3]

(c) Comment on the usefulness to *Share*'s directors of the result obtained in **1(b)**. [6]

(d) Analyse the likely impact on *Share*'s profitability of a fall in UK interest rates. [13]

Section 2

2 Evaluate whether *Share* should invest £1m in IT. Justify your answer, including the use of investment appraisal techniques. [25]

3 To what extent will the recruitment and retention of employees be important to *Share*'s long term success? [25]

4 Evaluate whether *Share* should spend more on promoting the business or on developing its CSR strategy. [25]

BLANK PAGE