

## 1.6: Growth and Evolution: Exam Practice Question



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### 1.6 GROWTH AND EVOLUTION: EXAM PRACTICE QUESTION

Read the case study information below and answer the questions that follow.

#### GROWTH STRATEGY IN DISPUTE AT TRAFFIC CLOTHING PLC



Traffic Clothing Plc. produces suits and dresses and sells them to major retailers in several countries. Sales turnover has grown by around 15% each year from the last decade – a slower rate than some competitors. Traffic's low prices have been possible due to the opening of low-cost factories in developing countries. This internal growth strategy was supported by most of the directors. They believed it had been achieved without excessive external borrowing. There were some real causes for concern, however. Sales revenues were increasing, but profits had remained unchanged for the last three years. This was due to several factors. First, new competitors were entering the

market and driving down prices. Secondly, raw material prices for both natural and manmade inputs were rising. Lastly, the number of mergers between large clothing retailers had increased their bargaining power when dealing with producers like Traffic.

Major shareholders in Traffic were not happy with the directors' growth strategy. At the last board meeting, the finance director proposed a policy of rapid external growth. She argued that this could be achieved by aggressive takeovers of either clothing producers or material suppliers to achieve cost leadership. The marketing director suggested focusing on a smaller, higher-income market segment. This could be reinforced with a merger with a clothing retailer. "Our own shops will give us real power in the high street as we will be able to offer customers a top quality shopping experience – this will allow differentiation in a crowded market". The chief executive suggested that both directors prepare a detailed report on these proposals.

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**25 MARKS, 45 MINUTES**

1. Explain the difference between 'internal' and 'external' growth. **[4 marks]**
2. Explain how the business increased sales revenue, yet gained no increase in profits for the last five years. **[5 marks]**
3. Evaluate the advantages **and** disadvantages of mergers **and** takeovers as strategies for growth at Traffic Clothing Plc. **[8 marks]**
4. Evaluate internal **and** external growth strategies for Traffic Clothing Plc as a multinational company if it has further objectives to expand internationally. **[8 marks]**