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—Visionary IB Education—
Success in the IB Diploma

BUSINESS MANAGEMENT

STANDARD LEVEL

PAPER 1

Practice examination 2019 – **Radeki de Dovnic Manufacturing**

1 hour 15 minutes

INSTRUCTIONS TO CANDIDATES

- Do not open this examination paper until instructed to do so.

A clean copy of the **IB Business Management case study – Radeki de Dovnic Manufacturing** is required for this examination paper.

- Read the case study carefully.
- A clean copy of the **IB Business Management formulae sheet** is required for this examination paper.
- Section A: answer two questions.
- Section B: answer question 4.
- A calculator is required for this examination paper.
- The maximum mark for this examination paper is **[40 marks]**.

SECTION A

Answer **two** questions from this section.

QUESTION ONE

- a. Outline the importance of wholesalers (line 52) to Radeki de Dovnic Manufacturing. **[4 marks]**
- b. With reference to Radeki de Dovnic Manufacturing, distinguish between capital expenditures (line 54) **and** revenue expenditures. **[6 marks]**

QUESTION TWO

- a. Outline **two** key features of a democratic leadership style **and two** key features of a paternalistic leadership style (line 89). **[4 marks]**
- b. With reference to Radeki de Dovnic Manufacturing, explain the importance of branding (line 123). **[6 marks]**

QUESTION THREE

- a. With reference to Radeki de Dovnic Manufacturing, analyse team working as a non-financial method of motivation (line 87). **[4 marks]**
- b. Explain **two** reasons why organisations such as Radeki de Dovnic Manufacturing implement corporate social responsibility strategies. **[6 marks]**

SECTION B

Answer the **compulsory** question from this section.

QUESTION FOUR

To help with the operations management strategy at RDM, Jan has tasked his chief financial officer (CFO) to provide him with detailed financial forecasts and cost estimates regarding alternative locations for the possible new production facility.

When reporting back to Jan, the CFO summarised the financial information in table 1 below. The quantitative information relates to the initial cost and profitability of two alternative locations for the production facility: Poland and Germany.

Each of these locations has good rail, road and seaport infrastructure for exporting into European markets and even further abroad if opportunities arise. Germany would benefit from **economies of scale** more so than Poland.

After a period of research, the CFO was able to produce profitability forecasts based on annual net cash flows for each location, and these are summarised in table 1 below. The costs to purchase the land and build the factory in each country are equivalent. After six years the robotics necessary for mass customisation would likely need to be replaced.

Table 1: Net cash flow forecast estimates for production facilities in two European countries

Year	Option A: Poland	Option B: Germany
0	(€120 m)	(€170 m)
1	€40 m	€30 m
2	€50 m	€40 m
3	€50 m	€50 m
4	€50 m	€60 m
5	€50 m	€70 m
6	€50 m	€80 m

RDM has the option of financing the alternative production facilities through an initial public offering (IPO); i.e. to “go public” [line 117]. It also has the option of securing funding with a long-term bank loan, and the CFO notes that while interest rates are at historic lows bank lending restrictions are relatively tight in the current economic and regulatory environment.

RDM does not have the option of issuing additional shares privately to raise the large amount of capital that is required to finance this project, even for the lowest-cost country.

The balance sheet of RDM is shown (Table 2, below) and this provides important financial information to bankers and prospective shareholders interested in a possible IPO.

Table 2: RDM balance sheet

Radeki de Dovnic Manufacturing Balance Sheet as of 30 April 2019		
	€ m	€ m
Fixed assets		
Fixed assets	50	
Accumulated depreciation	2	
Net fixed assets		48
Current assets		
Cash	1	
Debtors	1.2	
Stock	3.5	
Total current assets	5.7	
Current liabilities		
Overdraft	0.5	
Creditors	1.5	
Short-term loans	2.2	
Total current liabilities	4.2	
Net current assets (Working capital)		1.5
Total assets less current liabilities		49.5
Long-term liabilities (debt)	30	
Net assets		19.5
Financed by:		
▪ Share capital	11	
▪ Retained profit	8.5	
Equity		19.5

- a. Define the term **economies of scale**. **[2 marks]**
- b. Investment appraisal:
- i. Calculate the payback period for the project in each location. **[2 marks]**
 - ii. Calculate the average rate of return for the project in each location. **[2 marks]**
- c. Analyse the appropriateness of the production method to be used in RDM's new factory. **[4 marks]**
- d. Recommend a preferred source of finance for RDM to establish the new production facility. **[10 marks]**