South Tuen Mun Government Secondary School

BAFS_Financial Management_DSE_PP

PP_1. Explain TWO advantages of using debt financing. (4 marks)

PP_2. List TWO activity ratios and state what aspects of management efficiency each of them measures. (2 marks)

PP_9 A company is considering applying for the rights to distribute a branded electric car in Asia. As a risk reduction measure, the company plans to conduct market research to assess the market potential of the electric car.

(a) Describe the steps involved in conducting market research to assess the market potential of the electric car. (8 marks)

(b) Suppose the company finally got the distribution rights. Apart from the risk reduction strategy, discuss the other risk management strategies that the company can adopt for distributing the electric car. (12 marks)

PP Q8

Century. Group is a large local manufacturer of consumer electronics with a mission to provide entertainment to as many people as possible. With the growing popularity of interactive electronic games, the Group has developed a four-dimensional (4D) portable electronic game device. In a management meeting, Mr Lam, the Chief Executive Officer, said, "After spending several years on research and development (R&D), it's time for us to reap our rewards and be the leader in the market."

Ms Ho, the Marketing Manager, responded, "To launch the new product, we need to develop effective marketing strategies. As the 4D portable electronic game device is in the introductory stage of the product life cycle, we have to select our target market carefully and formulate appropriate marketing mix strategies. According to my preliminary analysis, the new product can be marketed as a high-priced version which targets high income professionals, or it can be marketed as a low-priced version which targets the general public." The estimated net cash flows of the two versions are presented in the following table:

(a) Using the budget airline market as an example, explain THREE differences in buying behaviour between the consumer market and the business market. (6 marks)

	High-priced version $ (in millions)	Low-priced version $ (in millions)
Year 0	-100	-70
Year 1	40	30
Year 2	60	50
Year 3	80	80
Year 4	50	60

Payback Period	2 years
Net Present Value	$80 206 270

(Cost of capital is 10%)

Mr Lain said, "Your analysis reminds us that we have to be aware of the financial implications of launching the new product. Since we have already spent a vast amount of capital on the R&D of the new product in the past few years, ii we further spend a considerable amount of money in marketing the new product, the pressure on capital would put our Group into a tight financial situation. As our Group is not able to undertake both versions, we have to choose one of them. I would choose the low-priced version."

Mr Fok, the Financial Manager, remarked, "I think financial control is important. Say for example, although the purchase price of raw materials and the wage rate of our employees were the same as budgeted, the actual spending on these two areas substantially exceeded the budgeted spending in the last financial year."

(a) With reference to the concept of the product life cycle, state FOUR characteristics of the market of the 4D portable electronic game device. (4 marks)

(b) Ignoring any tax implications, calculate (1) the payback period and (2) the net present value of the low-priced version of the 4D portable electronic game device, Show your workings. (4 marks)

(c) Give THREE reasons to explain why Century Group should launch the low-priced version of the 4D portable electronic game device. (6 marks)

(d) Suggest the appropriate marketing mix strategies for the low-priced version of the 4D portable electronic game device. , ' (8 marks)

(e) For (1) raw materials and (2) wages, suggest a reason for each to explain why there was a variance between the actual spending and the budgeted spending of Century Group in the last financial year. (2 marks)

Year		Marks
PP Q1	**<u>Advantages of using debt financing:</u>** ● interest expenses are tax-deductible ● avoid dilution effect ● enjoy leveraging effect *(2 marks for each relevant advantage. max. 4 marks)*	4 marks
PP Q2	**Ratios and aspects of each measure:** **<u>inventory turnover:</u>** measure the efficiency of using inventory in generating sales **<u>collection periods:</u>** measure the ability to collect receivables in a timely manner **<u>total assets turnover:</u>** measure the efficiency of using total assets in generating sales *(2 marks for each relevant point, max. 4 marks)*	2 marks
PPQ9	**<u>a) Steps in conducting market research:</u>** ● define the problem and research objectives ● develop the research plan: ● specific information needs ● research approaches ● sampling plan/Contact methods ● research instruments ● implement the research plan: ● data collection ● data analysis ● interpret and report the findings	
PPQ9	**<u>b) Other risk management strategies:</u>** ● risk avoidance: give up some high risk segments, such as staying away from politically ● unrest regions ● risk assumption: absorb the loss, such as setting up a reserve fund ● risk transfer: transfer the risk to a third party, such as by taking out insurance	
PPQ8	**<u>(a) Characteristics PLC :</u>** sales: slow profit: negative costs: high cost per customer Customers: innovators competitors: few (1 mark for each relevant characteristic	

PPQ8	**b) Payback period of the low-priced version** (1) Payback period of the low-priced version: $[\ 1 + \frac{40}{50}\ ]$ years = 1.8 years	
	(2) NPV of the low-priced version: $\$\left[-70\,000\,000 + \frac{30\,000\,000}{1.1} + \frac{50\,000\,000}{(1.1)^2} + \frac{80\,000\,000}{(1.1)^3} + \frac{60\,000\,000}{(1.1)^4}\ \right]$ = \$99 681 033	
	c) Reasons to launch the low priced version: **<u>size of segment:</u>** number of customers in the general public segment is greater than that of the high income customers **<u>company's resources:</u>** the company is short of capital and launching the low-priced version requires less capital and the payback period is shorter **<u>company's objective:</u>** making the 4D portable electronic game device more affordable meets the company's objective **<u>return/profitability:</u>** the NPV of launching the low-priced version is higher *(2 marks for each relevant reason, max. 6 marks)*	
	d) Marketing mix strategies: **<u>product:</u>** basic product **<u>price:</u>** penetration pricing **<u>promotion:</u>** build product awareness, heavy sales promotion **<u>place:</u>** selective distribution *(2 marks for each relevant strategy, max． 8 marks)*	
	e) Reason for variance (1) usage/wastage of raw materials is more than estimated (2) usage/wastage of labour is more than estimated	