

## Chapter 7: Exam practice question

### Growth strategy in dispute at Traffic Clothing plc

- 1 Use the case study to explain the difference between ‘internal’ and ‘external’ growth. (4)

Internal growth (also known as organic growth) is expansion of a business by means of opening new branches, shops or factories, e.g. Traffic Clothing plc opening factories in developing countries.

External growth refers to the expansion of a business by merging with or taking over another business, from either the same or a different industry, e.g. takeover by Traffic Clothing plc of other clothing producers or material suppliers.

Apply **Resources table 3b** mark bands.

- 2 Explain how the business increased sales revenue, yet gained no increase in profits for the last three years. (5)

Sales revenue increased because:

- Traffic Clothing plc were able to reduce prices because they reduced production costs by opening low-cost factories in developing countries
- new competitors were driving down prices
- the price of raw materials was rising
- merging retailers were able to force down costs.

Thus, even though sales increased, margins went down and so profits remained the same for the last three years.

#### 5 marks:

Four factors recognised and explained using business terminology and linked to the case study.

SL: Apply **Resources table 1** mark band descriptors.

HL: Apply **Resources table 2** mark band descriptors.

- 3 Assess the likely advantages and disadvantages of a cost leadership strategy for this business. (8)

See also Chapter 27 for material on cost leadership.

Define cost leadership strategy: this is a marketing principle based on setting the prices in the market in which the company’s products compete. For this to be possible the business may be the market leader (price maker due to market dominance) or one of the lead players in the market.

Advantages:

- Cost is a primary determinant of consumer choice, so being a cost leader can command significant market domination.
- The price can be set to cover all costs.
- The company can be flexible in adapting to market conditions.
- Any other relevant point.

Disadvantages:

- Margins may be under pressure and so profits may fall if cheaper supplies cannot be found or manufacturing economies cannot be made.
- Competing primarily on price may mean that premium-pricing opportunities may be missed for higher-quality products.
- The company may need to vary their prices if competitors vary theirs.
- Depends on price elasticity of the product.
- Any other relevant point.

SL: apply **Resources table 1** mark band descriptors.

HL: apply **Resources table 2** mark band descriptors.

Links to the case study are required for higher mark bands.

A conclusion is **not** required for this question.

- 4** Assess the likely advantages and disadvantages of a differentiation or a focused strategy for this business. **(8)**

Define differentiation strategy: this involves developing a product or service that offers unique features valued by customers. This added value may allow a business to charge a premium price, and may result from excellent R&D, innovation, quality, or a strong sales team able to promote the perceived strengths of the product.

Advantages of differentiation:

- may allow a premium price to be charged based on USPs
- allows specific marketing of strengths
- any other relevant point

Disadvantages of differentiation:

- fashions may change, making the differentiated product less marketable
- development for a differentiated product and associated image may cost a lot
- any other relevant point

Define focused strategy: this concentrates on a narrow market segment, aiming to achieve either a cost advantage or differentiation.

Advantages of focus:

- may lead to customer loyalty
- product is tailored to the market and so may stand more chance of being sold
- any other relevant point

Disadvantages of focus:

- may lead to imitation by rivals
- may need continued expenditure on maintaining market advantage
- may be significantly affected by fashion changes or if a new competing product renders it defunct
- any other relevant point

SL: Apply **Resources table 1** mark band descriptors.

HL: Apply **Resources table 2** mark band descriptors.

Links to the case study are required for higher mark bands.

A conclusion is **not** required for this question.