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**BUSINESS AND MANAGEMENT**

**9771/02**

Paper 2 Strategic Decisions

**May/June 2013**

**3 hours**

Additional Materials: Answer Booklet/Paper

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**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 a soft pencil for any diagrams, graphs or rough working.

Do not use staples, paper clips, highlighters, glue or correction fluid.

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.



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This document consists of **8** printed pages.



## Halfords Group plc

### Introduction

Halfords is the UK's leading retailer of car, leisure and cycling products. Through the £75 m acquisition of Nationwide Autocentres in February 2010 it is also the UK's leading independent car servicing and repair operator. Halfords is a public limited company and in the FT250.

Halfords employs approximately 11 000 staff and sells over 12 000 product lines divided into the following three core areas. 5

1. Car Maintenance – examples include car batteries, car servicing.
2. Car Enhancement – examples include satellite navigation systems, alloy wheels, roof boxes.
3. Leisure – examples include bicycles, tents, camping equipment. 10

Halfords operates over 460 stores in the UK and Republic of Ireland. Customers can visit stores or shop online at Halfords.com to reserve items for store collection or home delivery. Halfords offers a range of services to customers including bike servicing and repair, car care services, paint mixing, bike assembly, oil checking and car valeting.

Following the acquisition of Nationwide Autocentres, Halfords now operates car service centres at 220 sites nationally and offers motorists car repairs and servicing. It is now November 2011. 15

### Corporate Social Responsibility

Halfords is a company that has increased the importance of corporate social responsibility (CSR) within its strategic plans. The directors believe that the strategic, commercial and reputational benefits can be significant. The company uses Key Performance Indicators (KPIs) to assess the effectiveness of its CSR policies. These are shown in Table 1. 20

| <b>CSR Key Performance Indicators</b> |                                                                                                                       |
|---------------------------------------|-----------------------------------------------------------------------------------------------------------------------|
| Workplace:                            | Health and safety record, diversity of employees' backgrounds such as age, sex and race, number of applicants per job |
| Marketplace:                          | Customer service feedback, customer accessibility (compliance with the Disability Discrimination Act)                 |
| Environment:                          | Carbon footprint, energy efficiency within the stores, waste minimisation                                             |
| Community:                            | Charitable donations, supporting community initiatives                                                                |

**Table 1: CSR Key Performance Indicators**

The 2011 Annual Report states: 'we believe effective management of our CSR makes good sense.' Halfords has dedicated an entire section of its 2011 Annual Report to its CSR policies and is keen to highlight some recent successes. These have included an increase in the number of customers who would 'definitely use' Halfords stores again, training of staff in order to prevent accidents, compliance with the Disability Discrimination Act, an increase in the number of old car batteries recycled and a reduction in water consumption per store. 25

It is sometimes difficult to analyse the motives behind CSR. Some prominent business analysts have taken a cynical view of CSR. They argue that it is little more than an attempt to increase long term profitability by enhancing the public's perception of a particular company. 30

## The Economy

The retail sector is facing a number of considerable challenges. The company recently announced the closure of its loss-making operations in mainland Europe. It also intends to focus on cost cutting to maintain margins. The company recently consolidated its supply chain by building a new and larger warehouse and distribution facility. The company now employs a new specialist team that reviews the entire logistical efficiency of Halfords. In the long run this is likely to deliver significant internal economies of scale. Halfords is keen to maintain margins through cost reductions as price increases are unlikely to be accepted by consumers. Exploiting a range of economies of scale is a core element of this policy. 35 40

The Chairman of Halfords, Dennis Millard, is aware that consumer incomes are facing a significant squeeze and the economic climate is very challenging:

- taxes are rising (including VAT)
- real wages have decreased
- intense competition (e.g. from supermarkets)
- increased sourcing costs from countries such as China
- rising unemployment
- it is estimated that the average household has a lower real disposable income than ten years ago. 45

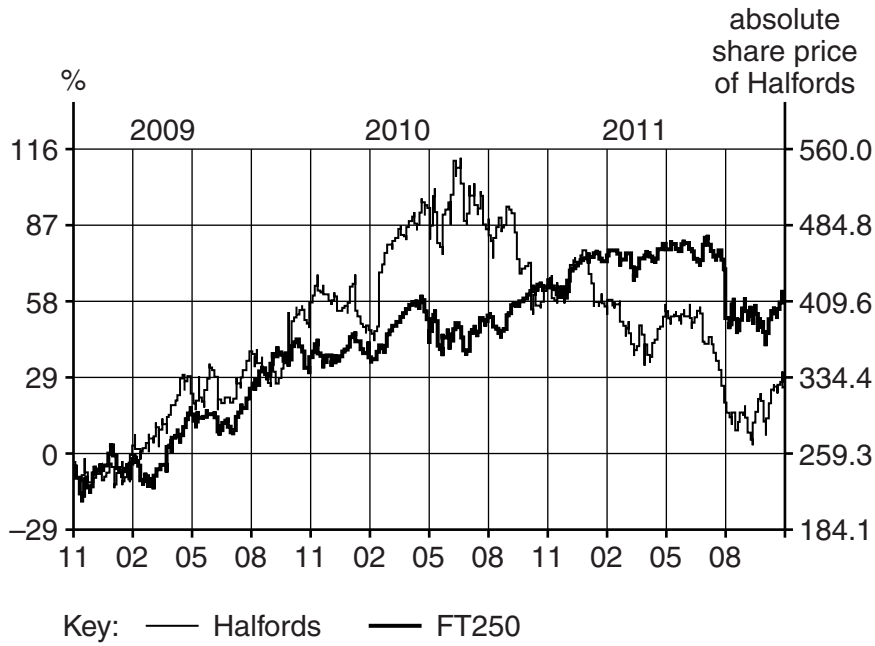
The impact of the economic slowdown is already being felt by Halfords. Sales of car enhancement products such as satellite navigation systems have fallen considerably. 50

The fall in real disposable incomes has also presented some opportunities to Halfords. Some items in the product portfolio have seen steady or rising sales. Halfords sells one in every three bicycles sold in the UK – the faltering economy has led consumers to reduce car usage and turn to cheaper modes of transport such as bicycles. In addition the car repair shops have seen increasing demand as customers repair vehicles rather than purchase new ones. 55

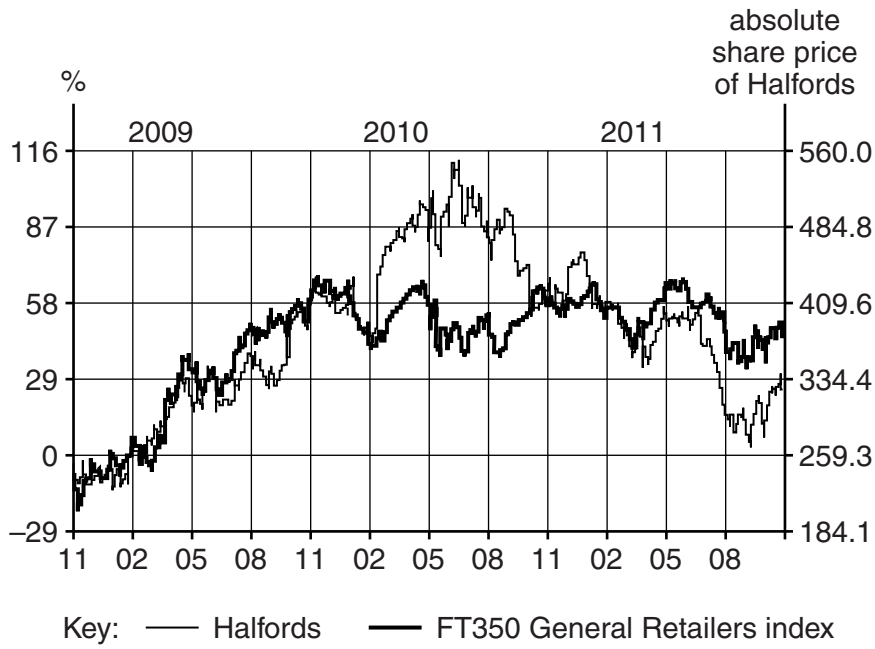
Overall the company is acutely aware of the potential positive and negative impact that reduced real incomes could have on its business. The Chairman's Statement states 'conditions will remain tough' and Halfords will need a clear strategic response.

## Financial Summary 60

In recent months some stockbrokers have become more cautious about advising their clients to buy Halfords shares. The current share price of £3.30 (November 2011) is well below its peak of the last 3 years. This share price weakness is a reflection of the financial markets' concerns about companies in the competitive retail sector and the macroeconomic outlook. The company has stated that it is well placed to deal with the economic downturn and points to its latest annual accounts. The dividend paid to shareholders increased from 20 pence per share in 2010 to 22 pence per share in 2011. The company is keen to stress that an examination of its accounts gives shareholders cause for optimism and stresses the growth in revenue and high dividend yield. 65



**Figure 1: Halfords share performance v FT250**



**Figure 2: Halfords share price v FT350 General Retailers index**

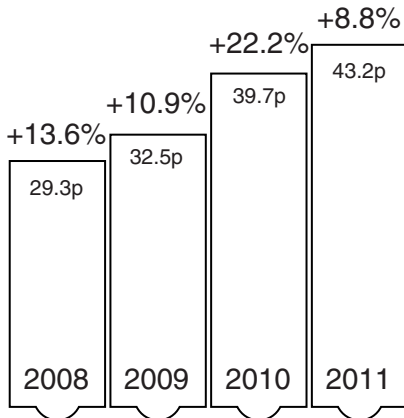
Figures 3–6 show financial highlights for Halfords.



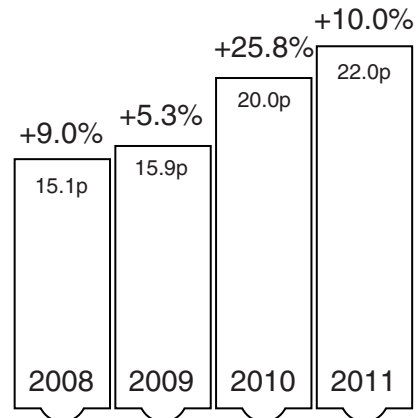
**Figure 3: Revenue**



**Figure 4: Operating profit**



**Figure 5: Earnings per share**



**Figure 6: Dividend per share  
(share price £3.30 as at November 2011)**

| Ratio                      | 2010 | 2011 |
|----------------------------|------|------|
| Asset turnover             | 2.99 | ?    |
| Inventory (stock) turnover | 2.74 | ?    |

**Table 2: Indicative ratio performance of Halfords**

|                                                                   | <b>1 April<br/>2011</b> | <b>1 April<br/>2010</b> |
|-------------------------------------------------------------------|-------------------------|-------------------------|
|                                                                   | £m                      | £m                      |
| <b>Assets</b>                                                     |                         |                         |
| <b>Non-current assets</b>                                         |                         |                         |
| Intangible assets                                                 | 346.7                   | 348.7                   |
| Property, plant and equipment                                     | 102.6                   | 102.9                   |
| <b>Total non-current assets</b>                                   | 449.3                   | 451.6                   |
| <b>Current assets</b>                                             |                         |                         |
| Inventories                                                       | 147.6                   | 138.5                   |
| Trade and other receivables                                       | 42.0                    | 42.9                    |
| Cash and cash equivalents                                         | 3.0                     | 39.5                    |
| <b>Total current assets</b>                                       | 192.6                   | 220.9                   |
| <b>Total assets</b>                                               | 641.9                   | 672.5                   |
| <b>Liabilities</b>                                                |                         |                         |
| <b>Current liabilities</b>                                        |                         |                         |
| Borrowings                                                        | (9.9)                   | (1.0)                   |
| Trade and other payables                                          | (142.0)                 | (131.5)                 |
| Current tax liabilities                                           | (23.4)                  | (17.5)                  |
| Provisions                                                        | (10.4)                  | (20.4)                  |
| <b>Total current liabilities</b>                                  | (185.7)                 | (170.4)                 |
| <b>Net current assets</b>                                         | 6.9                     | 50.5                    |
| <b>Non-current liabilities</b>                                    |                         |                         |
| Borrowings                                                        | (98.3)                  | (191.8)                 |
| Accruals and deferred income — lease incentives                   | (27.7)                  | (28.0)                  |
| Provisions                                                        | (7.5)                   | (3.3)                   |
| Deferred tax liabilities                                          | (0.3)                   | (0.5)                   |
| <b>Total non-current liabilities</b>                              | (133.8)                 | (223.6)                 |
| <b>Total liabilities</b>                                          | (319.5)                 | (394.0)                 |
| <b>Net assets</b>                                                 | 322.4                   | 278.5                   |
| <b>Shareholders' equity</b>                                       |                         |                         |
| Share capital                                                     | 2.1                     | 2.1                     |
| Share premium                                                     | 151.0                   | 146.5                   |
| Other reserves                                                    | 0.1                     | 2.5                     |
| Retained earnings                                                 | 169.2                   | 127.4                   |
| <b>Total equity attributable to equity holders of the company</b> | 322.4                   | 278.5                   |

Table 3: Extract from Balance Sheet

|                                                                            | <b>1 April<br/>2011</b> | <b>1 April<br/>2010</b> |
|----------------------------------------------------------------------------|-------------------------|-------------------------|
|                                                                            | £m                      | £m                      |
| <b>Revenue</b>                                                             | 869.7                   | 831.6                   |
| Cost of sales                                                              | (384.7)                 | (378.9)                 |
| <b>Gross profit</b>                                                        | 485.0                   | 452.7                   |
| Operating expenses                                                         | (356.9)                 | (333.0)                 |
| <b>Operating profits</b>                                                   | 128.1                   | 119.7                   |
| Finance costs                                                              | (4.3)                   | (4.6)                   |
| Finance income                                                             | 1.8                     | 2.0                     |
| <b>Net finance expense</b>                                                 | (2.5)                   | (2.6)                   |
| <b>Profit before income tax</b>                                            | 125.6                   | 117.1                   |
| Tax expense                                                                | (34.7)                  | (34.1)                  |
| <b>Profit for the financial period attributable to equity shareholders</b> | 90.9                    | 83.0                    |

|                           |       |       |
|---------------------------|-------|-------|
| <b>Earnings per share</b> | 43.2p | 39.7p |
|---------------------------|-------|-------|

**Table 4: Extract from Income Statement**

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

### Section 1

- 1 (a) Calculate the asset turnover ratio in 2011. [3]
- (b) Calculate the inventory (stock) turnover ratio in 2011. [3]
- (c) Comment on the significance to Halfords of the results obtained in **1(a)** and **(b)**. [6]
- (d) Analyse **two** 'internal economies of scale' that Halfords could exploit as its business expands (lines 37–40). [13]

### Section 2

- 2 Evaluate the extent to which corporate social responsibility (CSR) and profitability are compatible for Halfords. [25]
- 3 Recommend and justify a potential strategy that Halfords could pursue during a period of falling real disposable incomes. [25]
- 4 Discuss the likelihood that Halfords will be able to maintain or increase its current dividend. [25]

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*Copyright Acknowledgements*

Case Study © *Halfords Group plc Annual Report and Accounts*; 2 April 2010 – 2 April 2011.

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