



A-level BUSINESS

Paper 3 Business 3

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Source 1: KMH plc



Source 1**KMH plc**

KMH plc is a multinational company with its headquarters in the UK. It designs, builds and maintains marine engines for ships and yachts. Revenue comes from two major sources. Around half its revenue comes from manufacturing and selling marine engines. The rest comes from providing support services for the engines, from regular checking and simple maintenance to more complex service arrangements. These services include KMH plc technicians monitoring engine performance minute by minute wherever it is in the world and making remote adjustments to the way an engine is operating.

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Two market segments account for most of its engine sales – cruise ships and luxury yachts. KMH plc's market share for cruise ship engines is over 30%. Many of its customers (major cruise ship operators) have begun placing bigger orders as mergers and takeovers reduce the number of companies in this segment of the holiday industry (see **Appendix A**). Larger companies operating cruise ships can negotiate better deals from engine manufacturers, but KMH plc can also gain economies of scale as it works on larger orders, negotiating better deals with its own suppliers.

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KMH plc is also market leader in the luxury yacht market – providing the engines and servicing for the vessels much loved by mega-rich company executives, notably from Russia and Middle Eastern oil-producing countries.

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With key target markets for its marine engines consisting of cruise ship operators and buyers of luxury yachts, KMH plc's marketing mix is very different to many other large multinational businesses. These customers place relatively few orders for marine engines each year, but each purchase involves millions of pounds and complex negotiations. This requires KMH plc to have a specialised and highly skilled sales team with a detailed understanding of the technical benefits of its products and services.

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Secrets of KMH plc's success

KMH plc puts a strong focus on Research and Development, allowing it to be a technological leader in its field, holding thousands of patents for innovative technologies developed in its research centres. KMH plc has invested heavily in training its staff and considers the excellence of its staff to be a fundamental source of competitive advantage. An apprenticeship academy was opened in Hull in 2012. Meanwhile, the company spent a total of £48.5m on training staff in 2016 to keep their skills up to date. Generous salaries alongside the excellent training make KMH plc one of Britain's favourite employers, shown by its low labour turnover. KMH plc aims to reap the rewards of its investment in people through ensuring that its maintenance services are world-class, whilst staff involved in Research and Development have the skills to develop market-leading new engines.

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Much of KMH plc's success is down to the excellent fuel efficiency of its engines – a crucial selling point when oil prices are high. Its newest engine, the result of many years' Research and Development, is claimed to be 25% more efficient than those of its major rivals. In addition, KMH plc's maintenance and support contracts offer its customers peace of mind, aimed at preventing problems from occurring.

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Turbulence for KMH plc

Despite its strengths, KMH plc was still vulnerable to changes in market conditions. 2015 and 2016 had been worrying times for KMH plc shareholders. In February 2015 the company was forced to issue a profit warning – advising the stock market that previous predictions of future profits might be inaccurate. Further warnings followed, each time downgrading expectations of future profits. **Appendix B** shows KMH plc's share price in 2015 and 2016. Financial data for the business can be found in **Appendix C**.

Journalists blamed KMH plc's poor financial performance in 2015 and 2016 on two major issues:

- worsening global economic conditions slowing revenue growth
- excessive costs.

Global economic growth rates have remained low and the incomes of consumers in many rich countries barely increased in real terms and are not forecast to rise for the next few years. This has had an impact on demand for cruise holidays. In addition, global oil prices have fallen. There are no clear signs that oil prices will rise again in the next couple of years.

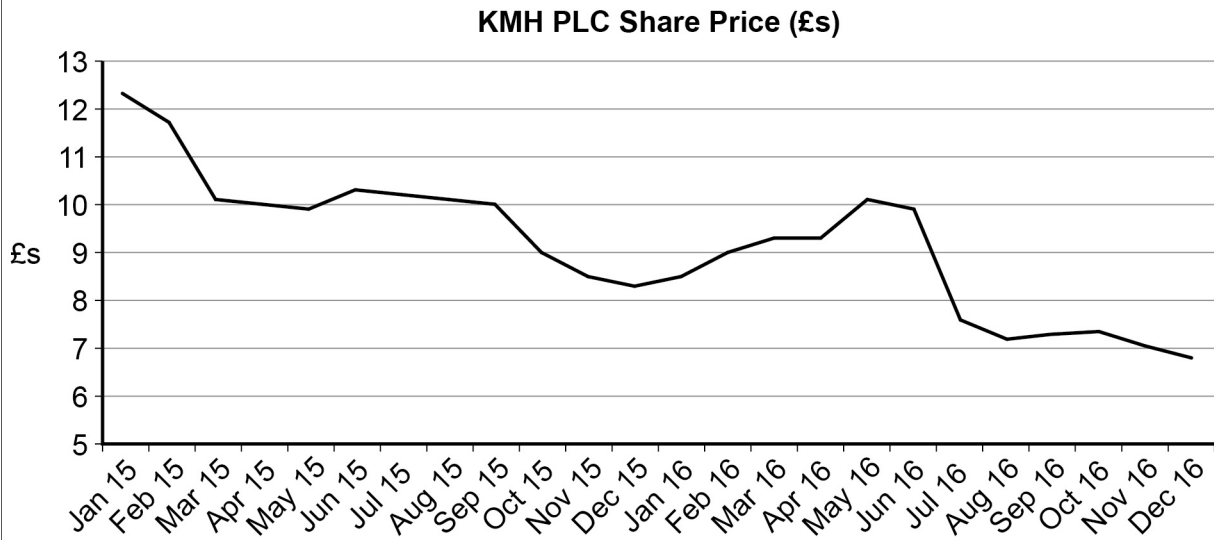
A new captain - a new strategy

In May 2016, KMH plc appointed Sir Rodney Short as its new Chief Executive. Sir Rodney was previously Chief Executive of ZQQZ plc – a British microchip manufacturer that he had turned into a world leader. Within weeks, Sir Rodney announced a major new strategy aimed at solving KMH plc's problems. One feature of the new strategy was an organisational restructuring. This was designed to reduce the size of the workforce. Most of the planned 140 job losses would be amongst senior managers (one in three senior managers would lose their jobs). Sir Rodney claimed that costs would be reduced by around £12m per year as a result after the costs of the restructuring. In addition, major investment (£50m) in new production machinery and a new factory is planned, aimed at reducing manufacturing costs and increasing total capacity. With such major changes planned, KMH plc's share price recovered slightly as the stock market gave Sir Rodney's strategy its approval, but there are plenty of details that need to be finalised, not least, how the changes are to be funded.

Appendix A

Top 5 Cruise Ship Holiday Providers - Market share (2016)	
CCL	48.1%
RCL	23.1%
NCL	10.4%
MSC Cruises	5.2%
Disney	2.8%
Others	10.4%



Appendix B**Appendix C****Table 1** Extracts from KMH plc balance sheets

	2015 (£m)	2016 (£m)
Non-current assets	5518.0	5104.0
Current assets	5594.0	6058.0
Current liabilities	(3842.5)	(4086.5)
Non-current liabilities	(4076.0)	(4567.5)
Net assets	3193.5	2508.0
Total equity	3193.5	2508.0

Table 2 Extracts from KMH plc income statements

	2014 (£m)	2015 (£m)	2016 (£m)
Revenue	7756.5	7441.7	6862.5
Gross profit	1658.4	1562.6	1399.8
Operating expenses	903.5	906.5	910.4
Operating profit	754.9	656.1	489.4

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