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Practice exam questions

Lessons from failure

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Check your answer to the question on pp. 8–9 of the magazine. This question relates to the AQA specification.

Sample answer

Business failure can be caused by internal and/or external factors, which can be financial or non-financial.

In the case of the failed Monarch airlines (2017), when compared to Ryanair, there was a lack of long-term management planning that meant Monarch delayed changing to a budget airline until 2009. By this time Ryanair and EasyJet had grown to dominate the market. Monarch managers failed to replace their fleet of ageing Airbus airplanes before 2018, an internal cause of business failure, which may have resulted in them having higher fuel and maintenance costs, making them less competitive.

Another internal cause of business failure may have been using more than one aircraft type during the switch from Airbus to Boeing-737. Monarch was having to pay for the servicing costs of two types of aircraft, rather than just the more cost-effective Airbuses. This may have meant that maintenance and staff training costs were higher, resulting in profit margins being significantly lower than competitors such as EasyJet. This may have reduced profits to a point where Monarch was unable to maintain its cost base producing a loss of £291 million in 2016.

However, Monarch's failure may have been caused more by external factors such as terror attacks and military coups in its destinations such as Tunisia and Turkey. Bookings may have significantly fallen, and reduced passenger numbers cause revenues to fall. At the same time, depreciation of sterling caused fuel costs (priced in US dollars) to increase, which may have damaged cash-flow. Competitors such as Ryanair (Monarch was about a tenth of Ryanair's size) may have been more capable of absorbing fuel costs due to the economies of scale and the bulk purchase of fuel.

According to the Institute of Directors, 57% of small business in the UK experience late payments from customers, which is an external cause of cash-flow issues and business failure. Managing a business's finances may be one of the key attributes of business failure, even businesses owned by experienced entrepreneurs can suffer financial mismanagement issues that end up being terminal to business ventures, such as the collapse of Virgin Orbit in 2023.

For new businesses financial management appears to be a significant internal cause of business failure. For example, the founder of Kentucky Fried Chicken was rejected 1,000 times before sourcing finance to grow the business. Start-ups often overreach in terms of plans for growth without first securing sufficient sources of finance to back them. However, business failure for more established businesses can come from both internal and external causes that create a perfect storm of issues that ultimately force business collapse, as appears to have happened in the case of Monarch airlines. The

key message of businesses and entrepreneurs is to manage risks carefully and learn from any mistakes made, thus hopefully avoiding failure.

Sample examiner comment

Mark: 16/16 (level 4 — an excellent response fully focused on the question)

A thorough knowledge and understanding are shown of the importance of internal and external causes to business failure.

Application is shown through the use of appropriate context applied to the question.

Coherent and logical analysis is linked together, looking at the relevant importance of internal and external causes of business failure to a range of business situations, using context-based quantitative and qualitative data for competing arguments.

An evaluation of competing arguments with context is used to support a judgement about the relative importance of internal and external causes to business failure for start-ups and established businesses.

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