REVISION GUIDE

BUSINESS STUDIES

GCSE O LEVEL

MUHAMMAD TALHA

03133106254

Chapter 1: The purpose of Business Activity

The economics problem: needs and wants.

Basically, all humans have **needs** and **wants**. Needs are things we **can't** live without, while wants are simply our desires that we **can** live without. We all have **unlimited wants**, which is true, since all of us want a new PC, a car, new graphics card, etc. that we actually do not need to live. Businesses produce **goods** and **services** to satisfy needs and wants.

Although we have unlimited wants, there are not enough **resources** for everyone. Resources can be split into 4 **factors of production**, which are:

- **Land**: All natural resources used to make a product or service.

- **Labour**: The effort of workers required to make a product or service.

- **Capital**: Finance, machinery and equipment required to make a product or service.

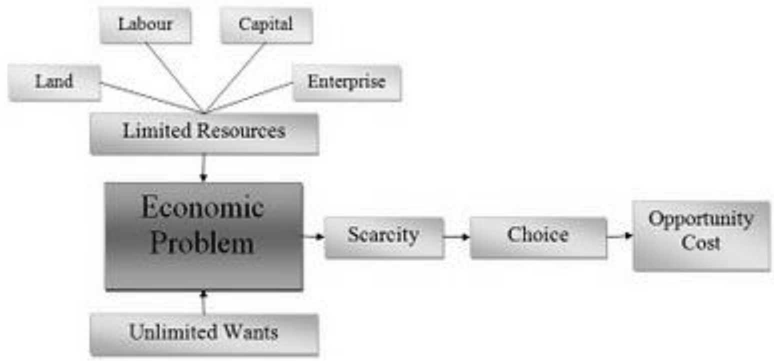
- **Enterprise**: Skill and risk-taking ability of the **entrepreneur**.

Entrepreneurs are people who **combine** these factors of production to make a product.

With these discussed, lets move on to the **economic problem**. The economic problem results from **limited resources** and **unlimited wants**. This situation causes **scarcity**, when there are not enough goods to satisfy the wants for everybody. Because of this, we will have to **choose** which wants we will satisfy (that will be of more benefit to us) and which we will not when buying things. For any choice, you will have to would have obtained if you didn't spend that money. For example, you would have got a book if you didn't buy the pen, or you would have a burger if you didn't buy the chips. Basically, item that you didn't buy is the **opportunity cost**. Make sure that the opportunity cost isn't higher than what you bought!

"Opportunity cost: the next best alternative given up by choosing another item.**"**

Here is a diagram showing the whole economic problem:



Division of labour/Specialisation

Because there are limited resources, we need to use them the most efficient way possible. Therefore, we now use production methods that are as fast as possible and as **efficient** (costs less, earns more) as possible. The main production method that we are using nowadays is known as **specialization**, or division of labour.

"Division of Labour/Specialisation is when the production process is split up into different tasks and each specialized worker/ machine performs one of these tasks.**"**

Advantages:

- Specialized workers are good at one task and increases efficiency and output.
- Less time is wasted switching jobs by the individual.
- Machinery also helps all jobs and can be operated 24/7.

Disadvantages

- Boredom from doing the same job lowers efficiency.
- No flexibility because workers can only do one job and cannot do others well if needed.
- If one worker is absent and no-one can replace him, the production process stops.

Why is business activity needed? (summary)

- Provides goods and services from limited resources to satisfy unlimited wants.

- Scarcity results from limited resources and unlimited wants.

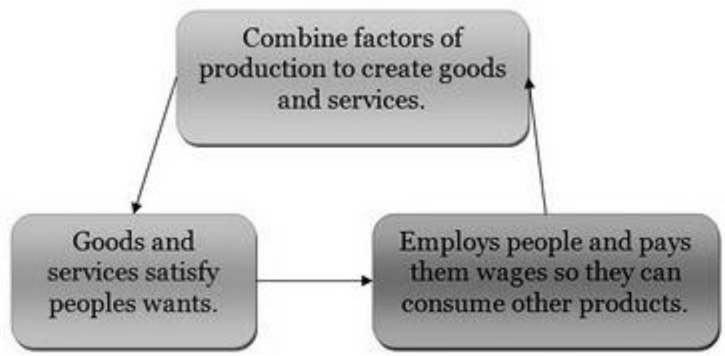
- Choice is necessary for scarce resources. This leads to opportunity costs.

- Specialisation is required to make the most out of resources.

Business activity:

1. Combine factors of production to create goods and services.
2. Goods and services satisfy peoples wants.

3. Employs people and pays them wages so they can consume other products.



Business Objectives:

All businesses have aims or objectives to achieve. Their aims can vary depending on their type of business or these can change depending on situations. The most common objectives are:

1. **Profit:** Profit is what keeps a company going and is the main aim of most businesses. Normally a business will try to obtain a *satisfactory level of profits* so they do not have to work long hours or pay too much tax.
2. **Increase added value:** Value added is the difference between the price and material costs of a product. E.g. If the price when selling a pen is $3 and it costs $1 in material, the value added would be $2. However, this does not take into account overheads and taxes. Added value could be increased by working on products so that they become more expensive finished products. One easy example of this is a mobile phone with a camera would sell for much more than one without it. Of course, you will need to pay for the extra camera but as long as prices rise more than costs, you get more profit.
3. **Growth:** Growth can only be achieved when customers are satisfied with a business. When businesses grow they create more jobs and make them more secure when a business is larger. The status and salary of managers are increased. Growth also means that a business is able to spread risks by moving to other markets, or it is gaining a larger market share. Bigger businesses also gain cost advantages, called economies of scale.
4. **Survival:** If a business do not survive, its owners lose everything. Therefore, businesses need to focus on this objective the most when they are: starting up, competing with other businesses, or in an economic recession.
5. **Service to the community:** This is the primary goal for most government owned businesses. They plan to produce essential products to everybody who need them.

These business objectives can conflict because different people in a business want different things at different times.

Stakeholders:

Stakeholders are a person or a group which has interest in a business for various reasons and will be directly affected by its decisions. Stakeholders also have different objectives and these also conflict over time.

There are two 6 types of stakeholders, and these types can be classified into two groups with similar interests.

Group 1: Profit/Money

- Owners:

1. Profit, return on capital.
2. Growth, increase in value of business.

- Workers

1. High salaries.
2. Job security.
3. Job satisfaction.

- Managers

1. High salaries.
2. Job security.
3. Growth of business so they get more power, status, and salary.

Group 2: Value

- Customers

1. Safe products.
2. High quality.
3. Value for money.
4. Reliability of service and maintenance.

- Government

1. Employment.
2. Taxes.
3. National output/GDP increase.

- Community

1. Employment.
2. Security.
3. Business does not pollute the environment.
4. Safe products that are socially responsible.

<u>Chapter 2: Types of business activity</u>

Levels of economic activity

In order for products to be made and sold to the people, it must undergo 3 different production processes. Each process is done by a different **business sector** and they are:

- **Primary sector:** The <u>natural resources extraction</u> sector. E.g. farming, forestry, mining... (earns the least money)
- **Secondary sector:** The <u>manufacturing</u> sector. E.g. construction, car manufacturing, baking... (earns a medium amount of money)
- **Tertiary sector:** The <u>service</u> sector. E.g banks, transport, insurance... (earns the most money)

Importance of a sector in a country:

- no. of workers employed.
- value of output and sales.

Industrialisation: a country is moving from the primary sector to the secondary sector.
De-industrialisation: a country is moving from the secondary sector to the tertiary sector.

In both cases, these processes both earn the country more revenue.

Types of economiess

Free market economy:

All businesses are owned by the **private sector**. **No** government intervention.

<u>Advantages:</u>

- Consumers have a lot of **choice**
- High **motivation** for workers
- **Competition** keeps prices low
- **Incentive** for other businesses to set up and make profits

<u>Disadvantages:</u>

- Not all products will be available for everybody, especially the **poor**
- No government intervention means **uncontrollable** economic booms or recessions
- **Monopolies** could be set up limiting consumer choice and exploiting them

Command/Planned economy:
All businesses are owned by the **public sector**. **Total** government intervention. Fixed wages for everyone. Private property is not allowed.

Advantages:

- **Eliminates** any **waste** from competition between businesses (e.g. advertising the same product)
- **Employment** for everybody
- All **needs** are met (although no luxury goods)

Disadvantages:

- **Little motivation** for workers
- The government might produce things people **don't** want to buy
- **Low incentive** for firms (no profit) leads to low efficiency

Mixed economy:
Businesses belong to both the private and public sector. Government controls **part** of the economy.

Industries under government ownership:

- health
- education
- defence
- public transport
- water & electricity

Privatisation
Privatisation involves the government selling national businesses to the private sector to increase output and efficiency.

Advantages:

- New **incentive** (profit) encourages the business to be more efficient
- **Competition** lowers prices
- Individuals have more **capital** than the government
- Business decisions are for **efficiency**, not **government popularity**
- Privatisation **raises money** for the government

Disadvantages:

- **Essential** businesses making losses will be **closed**
- Workers could be made **redundant** for the sake of profit
- Businesses could become **monopolies**, leading to higher price

Comparing the size of businesses
Businesses vary in size, and there are some ways to measure them. For some people, this information could be very useful:

- Investors - how safe it is to invest in businesses

- Government - tax
- Competitors - compare their firm with other firms
- Workers - job security, how many people they will be working with
- Banks - can they get a loan back from a business.

Ways of measuring the size of a business:

- **Number of employees.** Does not work on capital intensive firms that use machinery.
- **Value of output.** Does not take into account people employed. Does not take into account sales revenue.
- **Value of sales.** Does not take into account people employed.
- **Capital employed.** Does not work on labour intensive firms. High capital but low output means low effiency.

You **cannot** measure a businesses size by its **profit**, because profit depends on too many factors not just the size of the firm.

Business Growth

All owners want their businesses to expand. They reap these benefits:

- Higher profits
- More status, power and salary for managers
- Low average costs (economies of scale)
- Higher market share

Types of expansion:

- Internal Growth: **Organic** growth. Growth paid for by owners capital or retained profits.
- External Growth: Growth by **taking over** or **merging** with another business.

Types of Mergers (and main benefits):

- Horizontal Merger: merging with a business in the same business sector.

- Reduces no. of competitors in industry
- Economies of scale
- Increase market share

- Vertical merger:
Forward vertical merger:

- Assured outlet for products
- Profit made by retailer is absorbed by manufacturer
- Prevent retailer from selling products of other businesses
- Market research on customers transfered directly to the manufacturer

Backward vertical merger:

- Constant supply of raw materials
- Profit from primary sector business is absorbed by manufacturer
- Prevent supplier from supplying other businesses
- Controlled cost of raw materials

Conglomerate merger:

- Spreads risks
- Transfer of new ideas from one section of the business to another

Why some businesses stay small:

There are some reasons why some businesses stay small. They are:

- **Type of industry the business is in:** Industries offering personal service or specialized products. They cannot grow bigger because they will lose the personal service demanded by customers. E.g. hairdressers, cleaning, convenience store, etc.
- **Market size:** If the size of the market a business is selling to is too small, the business cannot expand. E.g. luxury cars (Lamborghini), expensive fashion clothing, etc.
- **Owners objectives:** Owners might want to keep a personal touch with staff and customers. They do not want the increased stress and worry of running a bigger business.

Chapter 3: Forms of business organisation

Almost every country consists of two business sectors, the private sector and the public sector. Private sector businesses are operated and run by individuals, while public sector businesses are operated by the government. The types of businesses present in a sector can vary, so lets take a look at them.

Private Sector

Sole Traders

Sole traders are the most common form of business in the world, and take up as much as 90% of all businesses in a country. The business is owned and run by one person only. Even though he can employ people, he is still the *sole proprietor* of the business. These businesses are so common since there are so little legal requirements to set up:

- The owner must register with and send annual accounts to the government **Tax Office**.
- They must register their business names with the **Registrar of Business Names**.
- They must obey all basic laws for trading and commerce.

There are advantages and disadvantages to everything, and here are ones for sold traders:

Advantages:

- There are so few **legal formalities** are required to operate the business.
- The owner is his own boss, and has **total control** over the business.
- The owner gets **100%** of **profits**.
- **Motivation** because he gets all the profits.
- The owner has **freedom** to change working hours or whom to employ, etc.
- He has personal **contact** with customers.
- He does not have to share information with anyone but the tax office, thus he enjoys complete **secrecy**.

Disadvantages:

- Nobody to **discuss** problems with.
- **Unlimited liability**.
- **Limited finance/capital**, business will remain small.
- The owner normally spends **long hours** working.
- Some parts of the business can be inefficient because of lack of **specialists**.
- Does not benefit from **economies of scale**.
- No **continuity**, no **legal identity**.

Sole traders are recommended for people who:

- Are setting up a new business.
- Do not require a lot of capital for their business.
- Require direct contact for customer service.

Partnership

A partnership is a group consisting of 2 to 20 people who run and own a business together. They require a **Deed of Partnership** or **Partnership Agreement**, which is a document that states that all partners agree to work with each other, and issues such as who put the most capital into the business or who is entitled to the most profit. Other legal regulations are similar to that of a sole trader.

Advantages:

- More **capital** than a sole trader.
- **Responsibilities** are **split**.
- Any **losses** are **shared** between partners.

Disadvantages:

- **Unlimited liability**.
- No **continuity**, no **legal identity**.
- Partners can **disagree** on decisions, slowing down decision making.
- If one partner is **inefficient** or **dishonest**, everybody loses.
- **Limited capital**, there is a limit of 20 people for any partnership.

Recommended to people who:

- Want to make a bigger business but does not want legal complications.
- Professionals, such as doctors or lawyers, cannot form a company, and can only form a partnership.
- Family, when they want a simple means of getting everybody into a business (Warning: Nepotism is usually not recommended).

Note: In some countries including the UK there can be Limited Partnerships. This business has limited liability but shares cannot be bought or sold. It is abbreviated as LLP.

Private Limited Companies

Private Limited Companies have separate legal identities to their owners, and thus their owners have limited liability. The company has continuity, and can sell shares to friends or family, although with the **consent of all shareholders**. This business can now make legal contracts. Abbreviated as Ltd (UK), or Proprietary Limited, (Pty) Ltd.

Advantages:

- The sale of shares make **raising finance** a lot easier.
- Shareholders have **limited liability**, therefore it is safer for people to invest but creditors must be cautious because if the business fails they will not get their money back.

- Original owners are still able to **keep control** of the business by restricting share distribution.

Disadvantages:

- Owners need to deal with many **legal formalities** before forming a private limited company:

  - **The Articles of Association:** This contains the rules on how the company will be managed. It states the rights and duties of directors, the rules on the election of directors and holding an official meeting, as well as the issuing of shares.
  - **The Memorandum of Association:** This contains very important information about the company and directors. The official name and addresses of the registered offices of the company must be stated. The objectives of the company must be given and also the amount of share capital the owners intend to raise. The number of shares to be bought b each of the directors must also be made clear.
  - **Certificate of Incorporation:** the document issued by the Registrar of Companies that will allow the Company to start trading.

- Shares cannot be freely sold without the **consent of all shareholders**.
- The accounts of the company are **less secret** than that of sole traders and partnerships. **Public information** must be provided to the Registrar of Companies.
- **Capital** is still **limited** as the company cannot sell shares to the public.

Public Limited Companies

Public limited companies are similar to private limited companies, but they are able to sell shares to the public. A private limited company can be converted into a public limited company by:

1. A **statement** in the Memorandum of Association must be made so that it says this company is a public limited company.
2. **All accounts** must be made **public**.
3. The company has to apply for a **listing** in the **Stock Exchange**.

A **prospectus** must be issued to advertise to customers to buy shares, and it has to state how the capital raised from shares will be spent.

Advantages:

- **Limited liability.**
- **Continuity.**
- Potential to raise **limitless capital.**
- **No restrictions** on transfer of shares.
- **High status** will attract investors and customers.

Disadvantages:

- Many **legal formalities** required to form the business.

- Many **rules and regulations** to protect shareholders, including the publishing of **annual accounts**.
- Selling shares is **expensive**, because of the commission paid to banks to aid in selling shares and costs of printing the prospectus.
- **Difficult to control** since it is so large.
- Owners **lose control**, when the original owners hold less than 51% of shares.

Control and ownership in a public limited company:

The **Annual General Meeting (AGM)** is held every year and all shareholders are invited to attend so that they can elect their **Board of Directors**. Normally, Director are **majority shareholders** who has the power to do whatever they want. However, this is not the case for public limited companies since there can be millions of shareholders. Anyway, when directors are elected, they have to power to make important decisions. However, they must hire **managers** to attend to day to day decisions. Therefore:

- Shareholders **own** the company
- Directors and managers **control** the company

This is called the **divorce between ownership and control.**
Because shareholders invested in the company, they expect **dividends**. The directors could do things other than give shareholders dividends, such as trying to expand the company. However, they might loose their status in the next AGM if shareholders are not happy with what they are doing. All in all, both directors and shareholders have their own **objectives**.

Co-operatives

Cooperatives are a group of people who agree to work together and pool their money together to buy "**bulk**". Their features are:

- All members have equal rights, no matter how much **capital** they invested.
- All workload and decision making is **equally** shared, a manager maybe appointed for bigger cooperatives
- **Profits** are shared **equally**.

The most common cooperatives are:

- **producer co-operatives**: just like any other business, but run by workers.
- **retail co-operatives**: provides members with high quality goods or services for a reasonable price.

Other notable business organizations:

Close Corporations:

This type of business is present in countries such as South Africa. It is like a private limited company but it is much quicker to set up:

- Maximum limit of 10 people.
- You only need a simple **founding statement** which is sent to the Registrar of Companies to start the business.
- All **members** are **managers** (no divorce of ownership and control).
- A separate legal unit, has both limited liability and continuity.

Disadvantages:

- The size limit is not suitable for a large business.
- Members may disagree just like in a partnership.

Joint ventures

Two businesses agree to start a new project together, sharing capital, risks and profits.

Advantages:

- Shared costs are good for tackling expensive projects. (e.g aircraft)
- Pooled knowledge. (e.g foreign and local business)
- Risks are shared.

Disadvantages:

- Profits have to be shared.
- Disagreements might occur.
- The two partners might run the joint venture differently.

Franchising

The **franchisor** is a business with a successful brand name that recruits **franchisees** (individual businesses) to sell for them. (e.g. McDonald, Burger King)

Advantages for the franchisor:

- The franchisee has to **pay** to use the brand name.
- **Expansion** is much **faster** because the franchisor does not have to finance all new outlets.
- The **franchisee manages** outlets
- All products sold must be **bought** from the **franchisor**.

Disadvantages for the franchisor:

- The **failure** of one franchise could lead to a **bad reputation** of the whole business.
- The franchisee **keeps** the **profits**.

Advantages for the franchisee:

- The chance of **failure** is much **reduced** due to the well know brand image.
- The franchisor pays for **advertising**.
- **All supplies** can be obtained from the franchisor.
- Many **business decisions** will be made by the franchisor (prices, store layout, products).
- **Training** for staff and management is provide by the franchisor.
- Banks are more willing to **lend** to franchisees because of **lower risks**.

Disadvantages for the franchisee:

- **Less independence**
- May be **unable** to make **decisions** that would suit the local area.
- **Licence fee** must be paid annually and a **percentage** of the **turnover** must be paid.

<u>Public Sector</u>

Public corporations:

A business owned by the government and run by Directors **appointed by the government**. These businesses usually include the water supply, electricity supply, etc. The government give the directors a set of **objectives** that they will have to follow:

- to keep **prices low** so everybody can afford the service.
- to keep people **employed**.
- to **offer a service** to the **public** everywhere.

These objectives are expensive to follow, and are paid for by government **subsidies**. However, at one point the government would realise they cannot keep doing this, so they will set different objectives:

- to **reduce costs**, even if it means making a few people redundant.
- to **increase efficiency** like a private company.
- to **close loss-making** services, even if this mean some consumers are no longer provided with the service.

Advantages:

- Some businesses are considered **too important** to be owned by an individual. (electricity, water, airline)
- Other businesses, considered **natural monopolies**, are controlled by the government. (electricity, water)
- **Reduces waste** in an industry. (e.g. two railway lines in one city)
- **Rescue important** businesses when they are failing.
- Provide **essential services** to the people (e.g. the BBC)

Disadvantages:

- **Motivation** might not be as high because **profit** is not an objective.
- **Subsidies** lead to **inefficiency**. It is also considered **unfair** for private businesses.
- There is normally **no competition** to public corporations, so there is **no incentive** to improve.
- Businesses could be run for **government popularity.**

Municipal enterprises

These businesses are **run by local government authorities** which might be **free** to the user and financed by local **taxes**. (e.g, street lighting, schools, local library, rubbish collection). If these businesses make a loss, usually a government **subsidy** is provided. However, to reduce the burden on taxpayers, many municipal enterprises are being **privatised**.

Chapter 4: Government and economic influences on business

The impact of business activity on society

All business activity has benefits and undesirable effects on society. These reasons are why governments want to have some control over business activity:

Possible benefits:

- Production of **useful goods** to satisfy customer wants.
- Create **employment**/increases workers **living standards**.
- Introduction of new products or processes that **reduces costs** and **widen product range**.
- **Taxes** help finance public services.
- Business earn **foreign currency** in exports and this could be spent on imports.

Possible undesirable effects:

- Business might **ruin** cheap but **beautiful areas**.
- **Low wages** and **unsafe working** conditions for workers because businesses want to lower costs.
- **Pollution**
- Production of **dangerous** goods.
- **Monopolies**
- Advertising can **mislead** customers.

Governments tend to pass laws that restrict **undesirable** activities while supporting **desirable** activities.

Governments and the economy

Government economic objectives:

Governments all have aims for their country, and this is what they are:

- Low **inflation**.
- Low **unemployment**.
- Economic **growth**.
- **Balance of payments**.

Low inflation:

Inflation occurs when prices rise. When prices rise rapidly many bad thing could happen:

- Workers wages **buy less** than before. Therefore their **real income** (how much you can buy with so much money) falls. Workers will be unhappy and demand for higher wages.
- Prices of **local** goods will **rise more** than that of other countries with lower inflation. People may start **buying foreign goods** instead.
- It would **cost more** for businesses to **start** or **expand** and therefore it does not **employ** as many people.
- Some people might be made **redundant** so that the business can cut costs.
- **Standards of living** will **fall**.

This is obviously why governments want to keep inflation as low as possible.

Low levels of unemployment:

When people are **unemployed**, they **want** to work but **cannot find** a **job**. This causes many problems:

- Unemployed people do not work. Therefore **national output** will be **lower** than it should be.
- The government will have to pay for **unemployment benefits.** This is **expensive** and money cannot be use for other purposes.

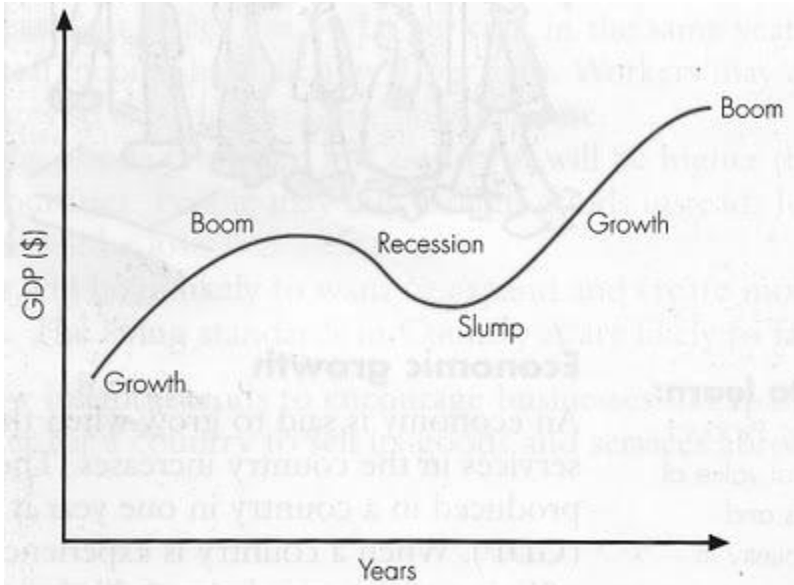
If the level up unemployment is low, it will increase national output and improve standards of living for workers.

Economic growth

A country is said to grow when its **GDP** (Gross Domestic Product) is increasing. This is the total value of goods produced in one year. The standards of living tends to increase with economic growth. Problems arise when a country's GDP fall:

- The country's output is falling, fewer workers are needed and **unemployment** occurs.
- **Standards of living** will fall.
- Businesses will **not expand** because they have less money to **invest.**

Economic growth is not achieved every year. There are years where the GDP falls and the **trade cycle** explains the pattern of rises and falls in national GDP.



The trade cycle has 4 main stages:

- **Growth:** This is when GDP is rising, unemployment is falling, and the country has higher standards of living. Businesses tend to do well in this period.
- **Boom:** Caused by overspending. Prices rise rapidly and there is a shortage of skilled workers. Business costs will be rising and they are uncertain about the future.
- **Recession:** Because overspending caused the boom, people now spend too little. GDP will fall and businesses will lose demand and profits. Workers may lose their jobs.
- **Slump:** A long drawn out recession. Unemployment will peak and prices will fall. Many firms will go out of business.

After all of this happens the economy **recovers** and begins to grow again. Governments want to avoid a **boom** so that it will not lead to a recession and a slump. Currently, the government of China is spending a lot of money so that their economy would continue to grow and avoid a boom.

Balance of payments

Exports earn **foreign currency**, while **imports** are paid for by foreign currency (or vice versa). The difference between the **value** of exports and imports of a country is called **balance of payments**. Governments try to achieve a balance in imports and exports to avoid a **trade deficit**, when exports are higher than imports. Of course, the government will lose money and their **reservoir** of foreign currency will **fall**. This results in:

- If the country wants to import more, they will have to **borrow** foreign currency to buy goods.
- The country's **currency** will now worth less compared to others and can buy less goods. This is called **exchange rate depreciation**.

Government economic policies

Governments want to influence the national economy so that it would achieve their aforementioned **objectives**. They have a lot of power over business activity and can pass laws to try to achieve their goals. The main ways in which governments can influence business activity are called **economic policies**. They are:

- **Fiscal Policy:** taxes and public spending.
- **Monetary policy:** controlling the amount of money in the economy through interest rates.
- **Supply side policies:** aimed at increasing efficiency.

Fiscal policy

Government spending could benefit some firms such as:

- Construction firms (road building)
- Defense industries (Iraq war)
- Bus manufacturers (public transport)

Governments raise money from **taxes**. There are **Direct taxes** on **income** and **Indirect taxes** on **spending**. There are four common taxes:

- Income tax
- Profits tax
- VAT (Value Added Tax)
- Import tariffs

Income tax

Income tax is based on a percentage of your income. Income tax is usually **progressive**, meaning that the percentage of tax you have to pay rises with your income. Effects on business and individuals if there was a rise of income tax:

- People will have less **disposable income.**
- **Sales fall** because people have less money to spend.
- Managers will cut costs for more profit. Workers might be made **redundant**.
- Businesses producing **luxury goods** will lose the most, while others producing **everyday needs** will get less affected.

Profits tax or corporation tax

This is a percentage of the profit a business makes. A rise in it would mean:

- Managers will have less **retained profit**, making it **harder** for the business to **expand**.
- Owners will get l**ess return on capital employed**. Potential owners will be **reluctant** to start their own business if the **profit margin** is too low.

Indirect taxes

These taxes are a percentage on the price of goods, making them more expensive. Governments want to **avoid** putting them on **essential goods** such as foods. A rise it it would mean:

- The effect would be almost the same as that of an increase in income tax. People would **buy less** but they would still spend money on **essential goods**.
- Again, **real incomes** fall. Costs will rise when workers demand higher wages.

Import tariffs and quotas

Governments put tariffs on imports to make local goods look more competitive and also to reduce imports. When governments put import tariffs on imports:

- Sales of local goods become **cheaper** than imports, leading to **increased sales**.
- Businesses who **import raw materials** will suffer higher costs.
- Other countries will **retaliate** by putting tariffs on the country's **exports**, making it less competitive.

Quotas maybe used to limit the amount of imports coming in.

Monetary policy and interest rates

Governments usually have to power to change **interest rates** through the central bank. Interest rates affect people who borrow from the bank. When interest rates rise:

- Businesses who owe to bank will have to **pay more**, resulting in less **retained profit**.
- People are more reluctant to **start** new businesses or **expand**.
- Consumers who took out loans such as **mortgages** will now have less **disposable income**. They will spend less on other goods.
- Demand will **fall** for businesses who produces **luxury** or **expensive** goods such as cars because people are **less willing to borrow**.
- Higher interest rates will **encourage** other countries to **deposit money** into **local banks** and earn **higher profits**. They will change their money into the local currency, increasing its demand and causing **exchange rate appreciation**.

Supply side policies

These policies aim to make the countries economy more efficient so that they can produce more goods and compete in the international economy. In doing so their GDP will rise. Here are some policies:

- **Privatisation:** Its aim is to use profit as an incentive to increase efficiency.
- **Improve training and education:** This obviously increases efficiency. This is crucial to countries with a big computer software industry.
- **Increase competition:** Competition causes companies to be more efficient to survive. Governments need to remove any monopolies.

Government controls over business activity

Government also influence major areas of business activity:

- what goods can be produced
- responsibilities to employees and working conditions
- responsibilities to consumers
- responsibilities to the natural environment
- location decisions

Undesirable effects created by business activity make governments want to control business activity:

- Business might **ruin** cheap but **beautiful areas**.
- **Monopolies**.
- Advertising can **mislead** customers.

<u>Why government control business activity</u>

Production of certain goods and services:

Governments can pass laws to restrict and ban certain dangerous goods such as:

- Weapons like guns and explosives.
- Drugs
- Goods that harm the environment

Consumer protection:

Consumers are easily misled by advertising. It is because consumers lack the technical knowledge and advertising can be very persuasive. In the UK, these laws are passed to protect customers from being exploited by businesses:

- **Weights and Measures Act:** to stop underweight goods being sold to customers.
- **Trade Descriptions Act:** all advertisements must be truthful.
- **Consumer Credit Act:** makes it illegal to not give customers their copy of the credit agreement to check how much money they really have.
- **Sale of Goods Act:** Makes it illegal to sell:

- Goods which have serious flaws or problems.
- Products that are not fit for the purpose intended by the consumer.

- Products that do not function as described on their label or by the retailer.

- **Consumer Protection Act:** Make false pricing claims illegal. Consumers can now sue producers or retailers if their products cause harm to them.

Competition policy: Control of monopolies

Monopolies could cause a lot of harm to an economy because there are nobody to compete against them:

- They exploit consumers with high prices.
- They prevent new firms from starting up.
- Monopolies are not encouraged to be efficient because there are no competitors.

In some countries, monopolies are banned and must be broken up into smaller firms. In the UK, monopolies can be investigated by the **Competition Commission**. This government body reports two main types of problems:

- Business decisions that are **against consumer interests**, such as trying to **eliminate all competitors**.
- Proposed **mergers** or **takeovers** that will result in a monopoly.

Protecting employees:

Employees need protection in the following areas:

- Unfair discrimination
- Health and safety at work
- Unfair dismissal
- Wage protection

Protection against unfair discrimination:

Often workers are discriminated in a job because of various reasons. There are laws that protect the employee from such reasons to be discriminated against:

- **Sex Discrimination Act:** people of different genders must have equal opportunities.
- **Race Relations Act:** people of all races and religions mush have equal opportunities.
- **Disability Discrimination Act:** it must be made suitable for disabled people to work in businesses.
- **Equal Opportunities Policy:** That is what everything is all about.

The UK is currently working on an age discrimination act.

Health and Safety at work:

Laws protect workers from:

- protect workers from **dangerous machinery**.
- provide **safety equipment and clothing**.
- maintain reasonable workplace **temperatures**.
- provide **hygienic** conditions and **washing** facilities.
- do **not** insist on excessively **long shifts** and provide **breaks** in the work timetable.

Managers not only provide safety for their employees only because laws say so. Some **believe** that keeping employees safe and happy improves their **motivation** and keeps them in the business. Others do it because it is present in their **moral code**. They are then considered making an **ethical decision**. However, in many countries, workers are still exploited by employers.

Protection against unfair dismissal

Employees need protection from being dismissed unfairly. The following reasons for the employee to be dismissed is unreasonable:

- for joining a **trade union**.
- for being **pregnant**.
- when **no warnings** were given beforehand.

Workers who thing they have been dismissed unfairly can take their case to the **Industrial Tribunal** to be judged and he/she might receive compensation if the case is in his/her favour.

Wage Protection

Employers mus pay employees the same amount that has been stated on the **contract of employment**, which states:

- Hours of work.
- Nature of the job.
- The wage rate to be paid.
- How frequently wages will be paid.
- What deduction will be made from wages, e.g. income tax.

A **minimum wage** rate is present in many Western countries and the USA. There are Advantages and cons of the minimum wage:

Advantages:

- Prevents strong employees to exploit unskilled workers who could not easily find work.
- Encourages employers to train unskilled employees to increase efficiency.
- Encourages more people to seek work.
- Low-paid workers can now spend more.

Disadvantages:

- Increases **costs**, increases **prices**.
- Owners who cannot afford these wages might make employees **redundant** instead.
- Higher paid workers want higher wages to keep on the same **level difference** as the lower paid workers. Costs will **rise**.

Location of Industry

How governments want to locate businesses:

- They **encourage** businesses to move to areas with a high level of **unemployment**, or called **development areas**.
- They **discourage** firms from locating in **overcrowded cites** or sites noted for their **natural beauty**.

How governments will influence the decisions of firms to locate:

- Businesses will be refused **planning permission** (permit to build in a place) if they wish to locate in overcrowded cities or beautiful areas. Building in these areas might be banned altogether.
- Governments can provide **regional assistance**, such as **grants and subsidies** to encourage firms to locate in undeveloped areas.

<u>Governments can help businesses too</u>

Governments can help businesses to:

- to encourage businesses to locate in poorer regions.
- to encourage enterprise by helping small businesses set up and survive.
- to encourage businesses to export.

Regional Assistance:

- Governments want development to be spread evenly over the whole country.
- Grants and subsidies can be used to attract firms to an area.

Small firms

Small firms are important for and economy because:

- They provide **most** of the **employment** because they are usually **labour intensive**.
- Small firms operate in **rural** areas where unemployment tends to be high.
- They can **grow** into very important businesses employing thousands of workers and producing output worth millions of dollars.
- Provides more **choice** for customers. They **compete** against bigger companies.
- They are often managed in a very **flexible** way, and is quicker to adapt to changing demands.

Governments help them by:

- Lower rates of **profits tax**, so they can have more **retained profit**.
- Giving **grants** and **cheap loans**.
- Providing **advice** and **information centres** to small firms.

Exporting goods and services

Why governments want businesses to export:

- Exports earn **foreign currency**, which can be use to buy imports.
- More exports means more people needed to produce them, increasing **employment** and **standards of living**.
- Successful exporters earn more money and have to pay more **profits tax**.

Governments can support exporters by:

- Encourage banks to lend to exporting businesses at **lower interest rates**.
- Offering **subsidies** or **lower taxes** to firms. However, other countries would **retaliate** and there would be no overall advantage.
- Trying to keep the **local currency** as **stable** as possible to make it easier for businesses to know how much they are going to make from exports.
- Organising **trade fairs** abroad to encourage foreign businesses to buy the country's exports.
- Offering **credit facilities**. This means that if a foreign customers refuses to pay for goods, the company could be compensated by the government.

Businesses in the economic and legal environment

Businesses could not ignore the power of the government in controlling business activity. **Multinationals** are an exception although normally businesses cannot afford to move to other countries. Government decisions create the **environment** in which businesses will have to **operate** and **adapt** to. The environment created by **legal** and **economic controls** are one of the **constraints** to managers when making decisions.

Chapter 5: Other influences on business

External constraints and constraints on business activity

Businesses cannot survive by neglecting the "real world", which includes **influences** that forces a business to make certain decisions or **constraints** that limits or controls actions. **External constraints** are things that businesses cannot control, these are:

- Technological change: New products.
- Technological change: New production processes.
- Increased competition.
- Environmental issues.

Here is a table from the book giving examples and the possible impacts on business activity:

Technological changes

Technological change bring about **constant changes** in consumer **products** and **production processes**. By using **R&D** to develop **new products**, companies could open up **new markets** and make huge amounts of money. Such companies include Microsoft, Sony and Apple. However, **new** products quickly **replace old** ones just like how **machines** are **replacing workers** in production processes.

There are two general things a firm could do when facing technological change:

- **Ignore** the changes and operate in the "traditional and old fashioned way". However, they can only sell to a small and **limited market**.
- **Compete** by **welcoming** changes and have an access to huge **mass markets**.

Here are some Advantages and cons of technological change:

External influences	Example	Possible impact on business
Technological change leading to the development of new products	Mobile phones with cameras	■ May make existing products oldfashioned and demand for these could fall. ■ Jobs will be lost in businesses that do not develop new products. ■ But new product ideas create new market opportunities.
Technological change leading to new production processes	Robots used to weld and assemble cars	■ May make existing production methods seem expensive and uncompetitive. ■ Workers may lose their jobs or, at least, will need retraining. ■ But average production costs could fall.
Increased competition	Newly formed low cost airlines competing with national airlines	■ May reduce demand for business already in the industry. ■ Workers' jobs may be lost and profits may fall in the existing businesses. ■ But increased competition could force businesses to become more efficient – this could lead to higher profits in the long run.
Environmental issues	Pollution caused by factories and chemical plants	■ Bad publicity caused by pollution could damage a firm's reputation. ■ Using 'clean' and non-polluting methods may be expensive if the latest machinery has to be purchased. ■ But businesses may create a unique image for themselves by adopting environment-friendly policies.

Advantages:

- New products encourage customers to **buy more**.
- If a business comes up with a **new product** first, they gain a huge **competitive advantage**.
- **"High-tech"** production methods make production more efficient.
- **Fewer workers** are required.
- New production methods can be adapted **very quickly** which gives businesses more **flexibility** in meeting consumer wants.
- **E-commerce** opens up new markets and the Internet is a **medium** of **advertising**.

Disadvantages:

- R&D is **expensive**, without guaranteed success.
- Businesses that do not **develop new products** will fail, leaving workers unemployed.
- New production methods and machines are **expensive**.
- Workers will need retraining which is **expensive**. They might be reluctant to learn or fear that they will not do well. This could lead to a **fall** in **motivation**.
- E-commerce lacks **personal** customer **service**.
- Smaller businesses cannot **afford** these things.

Introducing technological change successfully

Workers and managers may **fear** change. Workers might think:

- Will I be able to operate the new machines?
- Will I lose my job because the machines are more efficient?

Older workers are especially **afraid** of loosing out to **younger** and **better trained** workers. **Managers** also fear change, since recruiting technology experts will make them look more **inferior** in some way.

To make these changes work better, workers need to be **involved** in the changes. Workers might be told why the new machines are necessary and how they will be trained to use them, as well as letting them suggest ways to make work more efficient with the machines. It leads to more **opportunities** for trained and skilled staff and can lead to **new ideas** and products.

Competition

Most businesses have competitors. Most business decisions are based on:

- What competitors are **doing**?
- How they might **react**?

When you develop a **successful** product, other businesses will undoubtedly **copy** you. Therefore, you will need to research and develop even more products, **keeping ahead** of them. Competition is a major influence on business activity.

Environmental constraints on business activity

There are two general opinions on caring about the environment:

- Opinion A: Keeping the environment clean is **too expensive.** We want to keep prices low and this is what **consumers want** too.

- Protecting the environment is too **expensive** and **reduce profits**.
- **Increased prices** mean **increased costs**.
- Firms could become **less competitive** compared to others who are not environmentally friendly.
- **Governments** should pay to clean it up.

- Opinion B: Consumers are now starting to prefer businesses with **social responsibility**. Cleaner and more efficient machinery benefit the business in the long-run.

- Environmental issues affect us **all** and businesses have a **social responsibility** to deal with them.
- Using up **scarce resources** leaves less for **future generations** and **raise prices**.
- Consumers are becoming more **socially aware.** More now prefer firms that are environmentally friendly which could become an **marketing advantage**.
- If a business damages the environment, **pressure groups** could protest and damage its **image** and **reputation**.

Ways to make a business more environmentally friendly

Governments make these business activities illegal:

- locating in **environmentally sensitive** areas.
- **dumping** waste products into waterways.
- making products that cannot be easily **recycled**.

Manufacturers often complain that these laws raise prices. Therefore, **some** governments usually do not make these laws **strict** with the hope of increasing output and in turn **employment**.

Financing penalties, including pollution permits

Pollution permits are licences given to a business to pollute up to a certain level. If "dirty" businesses pollute over the permitted level, they either have to **buy permits** from "cleaner firms" or **pay heavy fines**. This encourages firms to be cleaner and **sell** their permits to dirtier companies for more **money.** Other penalties include **additional taxes**.

Consumer action and pressure groups

Consumers are becoming more **socially aware**, and many of them will stop buying goods from companies which pollute the environment, harming a business' **reputation and image**. Bad **publicity** means lower sales. If they want to keep their sales revenue up firms would have to adapt to more environmentally friendly production processes again.

Pressure groups are becoming very powerful nowadays. They can severely damage businesses that are not **socially responsible**.

These are their powers:

- **Consumer boycotts**
- **Protests**
- **Blocking** waste pipes.

These are times when they are likely to take action:

- They have popular **public support** and has a lot of **media coverage**.
- The group is **well organised** and **financed**.

These are times when they are less likely to take action:

- What a company is doing is **unpopular** but **not illegal**. (e.g. testing drugs on rats)
- The **cost** of making the company cleaner is **more** than **losses** that could be made by losing image and sales.
- The firm supplies other firms and not customers, **public support** will be less effective.

Environmental issues and cost-benefit analysis

Governments are increasingly concerned about the **social** and **environmental effects** of business activity. They have started to use a new type of analysis on businesses and government proposals which will not only take into account **financial costs** but also **external costs**.

Cost-benefit analysis requires and awareness of **external costs** (costs to the rest of society) and **external benefits** (gains to the rest of society). Here are some examples.

Decision: A new chemical plant will be built.

External costs	External benefits
Waste products will cause pollution	Jobs will be created
Smoke and fumes may damage the health of residents	Other firms may move into the area to provide services to the chemical firm
Parkland cannot now be used by local residents	Important chemicals will be produced to benefit society

Private costs	Private benefits
Cost of land	The money made from the sale of the chemical products
Cost of construction	
Labour costs	
Costs of running the plant when it has been built	
Transport costs of materials and completed products	

Social costs are worked out from **private costs** and **external costs**.

Social benefits are worked out from **private benefits** and **external benefits**.

In other words:

- **Social costs** = **private costs** + **external costs**.
- **Social benefits** = **private benefits** + **external benefits**

Chapter 6: Business costs and revenue

Business costs

All business activity involves some kind of cost. Managers need to think about the because:

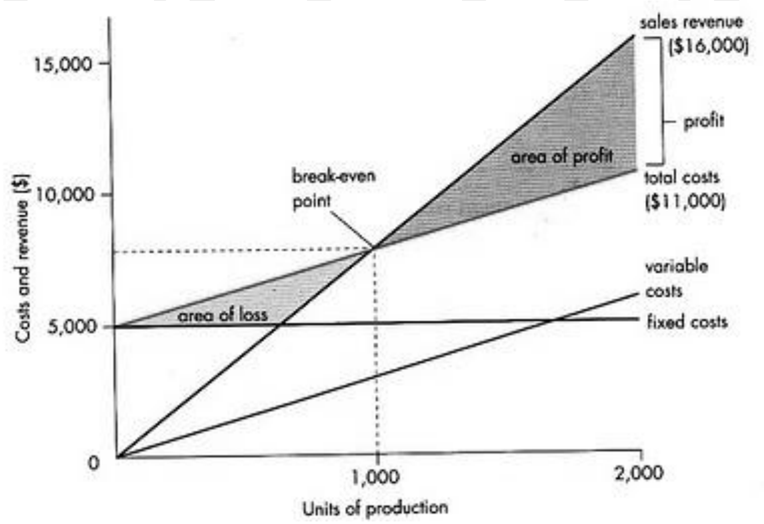
- Whether costs are lower than revenues or not. Whether a business will make a profit or not.
- To compare costs at different locations.
- To help set prices.

There are two main types of costs, **fixed** and **variable costs.** Here are some types of costs:

- **Fixed costs =** stay the same regardless of the amount of output. They are there regardless of whether a business has made a profit or not. Also known as **overheads**.
- **Variable costs =** varies with the amount of goods produced. They can be classified as **direct costs** (directly related to a product).
- **Total costs** = **fixed + variable costs**

Break-even charts, comparing costs with revenue

Drawing a break-even chart



Uses of break-even charts

There are other benefits from the break-even chart other than identifying the breakeven point and the maximum profit. However, they are not all reliable so there are some disadvantages as well:
Advantages:

- The expected profit or loss can be calculated at any level of output.
- The impacts of business decisions can be seen by redrawing the graph.
- The breakeven chart show the **safety margin** which is the amount by which sales exceed the breakeven point.

Disadvantages:

- The graph assumes that all goods produced are sold.
- Fixed costs will change if the scale of production is changed.
- Only focuses on the breakeven point. Completely ignores other aspects of production.
- Does not take into account discounts or increased wages, etc. and other things that vary with **time**.

Break-even point: the calcultion method.

It is possible to calculate the breakeven point withought having to draw the graph. We need two formulas to achieve this:

- Selling Price - Variable Costs = Contribution
- Break-even point = Total fixed costs/Contribution

Business costs: other definitions

There are other types of costs to be analysed that is split from fixed and variable costs:

- **Direct costs:** costs that are directly related to the production of a particular product.
- **Marginal costs:** how much costs will increase when a business decides to produce one more unit.
- **Indirect costs:** costs not directly related to the product. They are often termed **overheads**.
- **Average cost per unit**: total cost of production/total output

Economies and Diseconomies of scale:

Economies of scale are factors that lead to a reduction in average costs that are obtained by growth of a business. There are five economies of scale:

- **Purchasing economies:** Larger capital means you get discounts when buying bulk.
- **Marketing:** More money for advertising and own transportation, cutting costs.
- **Financial:** Easier to borrow money from banks with lower interest rates.
- **Managerial:** Larger businesses can now afford specialist managers in all departments, increasing efficiency.
- **Technical:** They can now buy specialised and latest equipment to cut overall production costs.

However, there are **diseconomies of scale** which increases average costs when a business grows:

- **Poor communication:** It is more difficult to communicate in larger firms since there are so many people a message has to pass through. The managers might loose contact to customers and make wrong decisions.
- **Low morale:** People work in large businesses with thousands of workers do not get much attention. They feel they are not needed this decreases morale and in turn efficiency.
- **Slower decision making:** More people have to agree with a decision and communication difficulties also make decision making slower as well.

Budgets and forecasts: looking ahead

Business also needs to think ahead about the problems and opportunities that may arise in the future. There are things to try to **forecast** such as:

- sales or consumer demands.
- exchange rates appreciation or depreciation.

- wage increases.

There are some forecasting methods:

- Past sales could be used to calculate the **trend**, which could then be extended into the future.
- Create a **line of best fit** for past sales and extend it for the future.
- **Panel consensus**: asking a panel of experts for their opinion on what is going to happen in the future.
- **Market research**.

Budgets

"Budgets are plans for the future containing numerical and financial targets". Better managers will create many budgets for costs, planned revenue and profit and combine them into one single plan called the **master budget**.

Here are the advantages of budgets:

- They set **objectives** for managers and workers to work towards, increasing their **motivation**.
- They can be used to see how well a business is doing by comparing the budget with the result in the process of **variance analysis.** The **variance** is the difference between the budget and the result.
- If workers get a say in choosing the objectives for a budget, the objectives would be more **realistic** since they are the ones that are going to do it and it also gives them better **motivation**.
- Helps control the business and its **allocation of resources/money**.

All in all, budgeting in useful for:

- reviewing **past** activities.
- controlling **current** business activity - following objectives.
- planning for the **future**.

Chapter 7: Business Accounting

What are accounts an why are they necessary?

Accounts are **financial records** of a firm's **transactions** that is kept up to date by the **accountants**, who are qualified professionals responsible for keeping accurate accounts and producing the final accounts.

Every end of the year, a **final accounts** must be produced which gives details of:

- Profits and losses made.
- Current value of the business.
- Other financial results.

Limited companies are bound by law to publish these accounts, but not other businesses.

Financial documents involved in buying and selling.

Accountants use various documents that are used for buying and selling over the year for their final accounts. They can help the accountant to:

- keep records of what the firm bought and from which supplier.
- keep records of what the firm sold and to which customer.

These documents are:

- **Purchase orders**: requests for buying products. It contains the quantity, type and total cost of goods. Here is an example.
- **Delivery notes:** These are sent by the firm when it has received its goods. It must be signed when the goods are delivered.
- **Invoices:** These are sent by the supplier to request for payment from the firm.
- **Credit notes:** Only issued if a mistake has been made. It states what kind of mistake has been made.
- **Statements of account:** Issued by the supplier to his customers which contains the value of deliveries made each month, value of any credit notes issued and any payments made by the customer. Here is an example.
- **Remittance advice slips:** usually sent with the statement of accounts. It indicates which invoices the firm is paying for so that the supplier will not make a mistake about payments.
- **Receipts:** Issued after an invoice has been paid. It is **proof** that the firm has paid for their goods.

Methods of making payment

There are several ways goods can be paid for:

- **Cash**: The traditional payment method. However, many businesses do not prefer to use cash for a number of **security reasons**. When cash is paid, a **petty cash voucher** is issued by the person in charge of the firm's money who also signs it to authorise the payment. The person making the purchase signs it too to show that the money has been recieved.
- **Cheque**: It is an instruction to the bank to transfer money from a bank account to a named person. In order to do this the bank needs a **cheque guarantee card**, saying that they have enough money in their account to support this payment.
- **Credit card**: Lets the consumer obtain their goods now and **pay later**. If the payment is delayed over a set period then the consumer will have to pay **interest**.
- **Debit card**: **Transfers money directly** from user's **account** to that of the seller.

Recording accounting transactions

Businesses usually use computers to store their transactions so that they can be easily accessed, calculated and printed quickly.

Who uses the financial accounts of a business?

- **Shareholders:** They will want to know about the profit or losses made during the year and whether the business is worth more at the end of the year or not.
- **Creditors:** They want to see whether the company can afford to pay their loans back or not.
- **Government:** Again, they want to check to see if correct taxes are paid. They also want to see how well the business is doing so that it can keep employing people.
- **Other companies:** Other companies want to compare their performance with a business or see if it is a good idea to take it over.

What do final accounts contain?

The trading account

This account shows how the **gross profit** of a business is calculated. Obviously, it will contain this formula:

Gross profit = Sales revenue - Cost of goods sold

Note that:

- Gross profit does **not** take to account **overheads**.
- **Only** calculate the **cost of goods sold**, and forget the **inventory**.
- In a **manufacturing business**, **direct labour and manufacturing costs** are also deducted to obtain gross profit.

The profit and loss account

The profit and loss account shows how **net profit** is calculated. It starts off with gross profit acquired from the trading account and by deducting all other costs it comes up with net profit.

Depreciation is the fall in value of a fixed asset over time. It is also counted as an indirect cost to businesses.

As for **limited companies**, there are a few differences with the normal profits and loss account:

- **Profits tax** will be shown.
- It needs to have an **appropriation account** at the end of the profits and loss account. This shows what the company has done with its net profits, in other words, how much **retained profit** has been put back into the company.
- Results form the **previous year** are also included.

Balance sheet

The balance sheet shows you a business's assets and liabilities at a particular time. The balance sheet records the **value** of a business at the end of the financial year. This is what it contains:

- **Fixed assets:** land, vehicles, buildings that are likely to be with the business for more than one year. They **depreciate** over time.
- **Current assets:** stocks, inventory, ash and debtors that are only there for a short time.
- **Long-term liabilities:** long-term borrowings that does not have to be paid in one year.
- **Short-term liabilities:** short-term borrowings that has to be paid in less than one year.

If your **total assets** are **higher** than your **total liabilities**, then you are said to own **wealth**. In a normal business, wealth belongs to the **owners**, while in a limited company, it belongs to the **shareholders**. Hence the equation:

Total assets - total liabilities = Owners'/Shareholders' wealth

Here are some terms found in balance sheets:

- **Working capital:** is used to pay short-term debts and known as **net current assets**. If a business do not have enough working capital then it might be forced to go out of business. The formula:

  Working capital = Current assets - Current liabilities

- **Net assets:** Shows the net value of all assets owned by the company. These assets must be paid for or finance by **shareholders' funds** or **long term liabilities**. The formula:

  Net assets = Fixed assets + Working capital

- **Shareholders' funds:** The total sum invested into the business by its owners. This money is invested in two ways:

- **Share capital:** Money from newly issued shares.
- **Profit and loss reserves:** Profit that is owned by shareholders but not distributed to them but kept as part of shareholders' funds.

- **Capital employed:** Long-term and permanent capital of a business that has been used to pay for all the assets. Therefore:

Capital employed = net profits
Capital employed = Shareholders' funds + long-term liabilities

Analysis of published accounts

Without analysis, financial accounts tell us next to nothing about the performance and financial strength of a company. In order to do this we need to compare **two figures** with each other. This is called **ratio analysis**.

Ratio analysis of accounts

The most common ratios used are for comparing the **performance** and **liquidity** of a business. Here are five of the most commonly used ratios.

Ratios used for analysing performance:

- **Return on capital employed:** This result could show the efficiency of a business. If the result rises, the managers are becoming more successful.

*Return on capital employed (%) = Operating profit/Capital employed * 100*

- **Gross profit margin:** If this rises, it could mean that either they are increasing added value or costs have fallen.

*Gross profit margin = Gross profit/Sales revenue * 100*

- **Net profit margin:** The higher the result, the more successful the managers are. This could be compared with other businesses too.

*Net profit margin = Net profit before tax/Sales revenue * 100*

Sir Talha Siddiqui
03133106254

Note: Net profit does **not** include tax.

Ratios used for analysing liquidity: This is too see how much cash a business has to pay off all of its short-term debts.

- **Current ratio:** This ratio assumes that all current assets could be converted into cash quickly, but this is not always true since **stock/inventory** could not be all sold in a short time. Generally, a result of 1.5 to 2 would be preferable, so that a business could pay all of its short-term debts and still have half of its money left.

Current ratio = Current assets/Current liabilities

- **Acid test** or **liquid ratio:** This type of analysis neglects stocks, but it is similar to the current ratio analysis.

Acid test ratio = (Current assets - Stocks)/Current liabilites

These ratios can be used to:

- Compare with other years.
- Compare with other businesses.

It must be remembered that a ratio on its own will give you nothing, but when it is compared with ratios from the past and other businesses it will tell you a lot of things.

However, there are still some **disadvantages** of ratio analysis:

- Only shows past results, does **not** show anything about the **future**.
- Comparisons between years may be **misleading** because of **inflation**.
- Comparisons between businesses could be **difficult** since each has its **own accounting methods**.

Chapter 8: Cash flow planning

What is meant by cash flow?

Cash is a **liquid asset**, meaning that i can be spent on goods and services any time. Many business experience **cash flow problems**, meaning that they do not have enough cash to do what they want to do. **Cash flow** means "the flow of money **in** and **out** of a business". These are ways cash flow can occur:

Cash inflows:

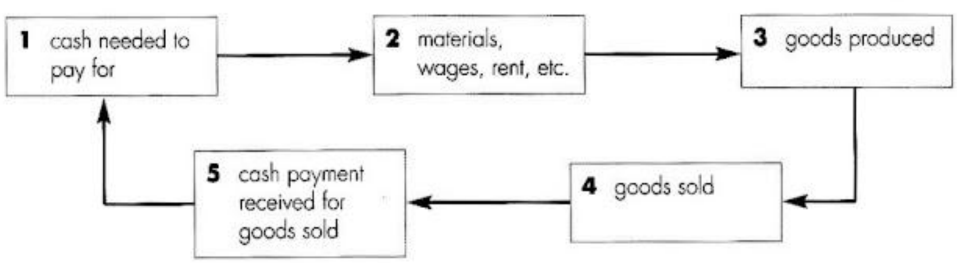
- **Sale** of **goods** for cash.
- **Payment** from debtors.
- **Borrowing** from a source (but will inevitably lead to cash outflow in the future).
- **Sale** of unwanted **assets**.
- **Investment** from investors: shareholders and owners

Cash outflows:

- **Purchasing goods** for cash.
- **Payment** of wages, salaries and others in cash.
- **Purchasing** fixed **assets**.
- **Repaying loans**.
- **Repaying creditors**.

Cash flow cycle

A **cash flow cycle** explains the stages that are involved in the process of cash out and finally into the business. This is what happens:



The longer it takes for cash to get back to the business, the more they will need **working capital** to pay off their short-term debts. This cycle also helps us understand the importance of **cash flow planning**. This is what happens when a company is short on cash:

- Not enough to pay for materials, therefore sales will fall.
- The company will want to insist customers on paying in cash, but they might lose them to competitors who let them pay in credit.
- There could be a **liquidity crisis** when it does not have enough cash to pay for **overheads** (bills, rent, etc.) and the business might be forced to close down by its creditors.

Managers need to plan their cash flow so that they do not end up in these positions.

Cash flow is not profit!

First we need to examine the formula for cash flow:

Cash flow = Cash inflow - Cash outflow

However, when calculating profit, we also take into account **credit** that debtors owe us. Therefore, a company might make $20,000 in profit but only $10,000 is received in cash because half of it is payed by credit card.

This creates something known as **insolvency**:

- Profitable business could run out of cash because of various reasons. This is called **insolvency** and it is one main reason why businesses fail.
- This can be because of several reasons:
  - Allowing customers **too long** to **pay** back, so that they will not have paid off the debts yet by the time the business has **run out** of **cash**.
  - Purchasing **too many assets** at once.
  - Producing or purchasing too much **stock/inventory** when **expanding** too quickly. This is called **overtrading**.

Here is an example of a **cash flow statement**:

	January	February	March
Opening bank balance (A)	10,000	15,000	(5,000)
Cash inflows (B)	35,000	45,000	50,000
Cash outflows (C)	30,000	65,000	40,000
Net cash flow (D) (= B − C)	5,000	(20,000)	10,000
Closing bank balance (= A + D)	15,000	(5,000)	5,000

As you can see, the closing bank balance in February is negative, which means that it has become **overdrawn**.

Cash flow forecasts

Because of the aforementioned problems, it is important for the manager to get an idea of how much cash will be available for which months. A **cash flow forecast** can tell the manager:

- How much cash is available for paying bills, loans and other fixed assets.
- How much the bank might need to lend to avoid insolvency.
- Whether the business has too much cash which could be more useful if used.

Uses of cash flow forecasts:

- **Starting up a business**: In the first months of a business, a lot of capital will be needed to set it up properly. The problem is, not everybody realises that the amount of money they needed is much more than they had expected. Therefore, a cash flow forecast will give them a better idea of how much money will be needed.
- **Keeping the bank manager informed**: It needs to be shown to the bank to inform it of the size of the needed loan/overdraft, when it is needed, how long it is needed and when it could be repaid. Only then will the bank give you a chance to get a loan.
- **Running an existing business**: It is important to know the cash flow of a business so that loans could be arranged in advance in order to get the least **interest** possible. If a firm has cash flow problems and goes to the bank for a loan for the next day, it will charge high interests because it knows that the business has no choice. Also, if a business exceeds the **overdraft limit** without informing the bank, it could be asked to repay the overdraft immediately and could result in closure of the business.
- **Managing cash flow**: If a business has **too much cash**, it should put the cash to some good **use** quickly. Some examples of this is: repaying all loans for **less interest**, paying creditors immediately to get **discounts**.

How can cash flow problems be solved?

Here are some steps to solve cash flow problems:

- Arrange for future loans with the bank when you anticipate **negative cash flow**.
- **Reduce** or **delay** planned expenses until cash is available, e.g. ask to pay in credit.
- **Increasing** forecasted cash **inflow**, e.g. by getting a part-time job.

Chapter 9: Financing business activity

Why do businesses need finance?

Businesses need **finance**, or money, to pay for their overhead costs as well as their day to day and variable expenses. Here are three situations when businesses need finance the most:

- **Starting a business**: Huge amounts of finance is needed to start a business which requires buying fixed assets, paying rent and other overheads as well as producing or buying the first products to sell. The finance required to start up a business is called **start-up capital**.
- **Expanding a business**: When expanding, a lot of capital is needed in order to buy more fixed assets or fund a takeover. Internal growth by developing new products also requires a notable amount of finance for R&D.
- **A business in difficulties**: For example, for loss making businesses money is needed to buy more efficient machinery, or money is needed to cover negative cash flow. However, it is usually difficult for these firms to get loans.

All all cases, businesses need finance for either **capital expenditure** or **revenue expenditure**:

- **Capital expenditure:** Money spent on fixed assets.
- **Revenue expenditure:** Money spent on day-to-day expenses.

Sources of finance

There are many ways to obtain finance, and they can be grouped in these ways.:

- **Internal** or **external**.
- **Short-term**, **medium-term** or **long-term**.

Internal finance:

This is finance that can be taken from within the business itself. There are advantages and disadvantages to each of them:

- **Retained profit:** Profit reinvested into a business after part of the net profit has been distributed to its owners.
    - + Retained profit does **not** have to be **repaid** unlike a loan.
    - - New businesses **do not have much** retained profit.
    - - Retained profit from small firms are **not enough** for **expansion**.
    - - **Reduces payment** to owners/shareholders.
- **Sale of existing assets:** Firms can get rid of their unwanted assets for cash.
    - + Makes better **use** of capital that is not used for anything.

- - Takes time to sell all of these assets.
    - - New businesses do not have these assets to sell.
- **Running down stocks:** Sell everything in the current existing inventory.
    - + Reduces **opportunity cost** and **storage costs** of having inventory.
    - - Risks **disappointing** customers if there are not enough stock left.
- **Owners' savings:** Only applies to businesses that do not have limited liability. Since the legal identity of the business and owners are the same, this method is considered to be internal.
    - + **Available quickly**.
    - + **No interest** paid.
    - - **Limited** capital.
    - - Increases **risks** for owners.

External finance:

This is money raised from individuals or organisations outside a business. It is the most common way to raise finance.

- **Issue of shares:** Same as owners' savings, but only available to limited companies.
    - + A **permanent** source of capital that does not have to be **repaid**.
    - + **No interest** paid.
    - - **Dividends** will have to be paid.
    - - **Ownership** of the company could change hands to the **majority shareholder**.
- **Bank loans:** money borrowed from the bank.
    - + **Quick** to **arrange**.
    - + **Variable** lengths of **time**.
    - + **Lower rates** offered if a large company borrows large sums.
    - - Must be **repaid** with **interest**.
    - - **Collateral** is needed to secure a loan and may be **lost**.
- **Selling debentures:** These are long-term loan certificates issued by limited companies.
    - + These can be used to raise **long-term finance**, e.g. 25 years.
    - + No **collateral** is required, just the **trustworthiness** of a big company.
    - - Must be **repaid** with **interest**.
- **Factoring of debts:** Some businesses (**debt factors**) "buy" **debts** of a firm's **debtors** (e.g. customers) and pay the firm cash in return. The firm now does not worry about worrying about whether their customers will pay or not and 100% of all the debts goes to the factor.
    - + **Immediate cash** is obtained.
    - + **Risk** of collecting debt becomes the factor's.
    - - The firm does **not receive 100%** value of the debt.
- **Grants and subsidies:** can be obtained from outside agencies like the **government**.
    - + Do **not** have to be **repaid**.
    - - They have **conditions** that you have to fulfill (e.g. locating in poor areas).

Short-term finance:

This is **working capital** required to pay **current liabilities** that is needed up to three years. There are three main ways of acquiring short-term finance:

- **Overdrafts:** Allows you do draw more from your bank account than you have.
    - + Overdrafts can **vary** every month, making it **flexible**.
    - + **Interest** only needs to be paid only to the **amount overdrawn**.

- + They can turn out **cheaper** than loans.
    - **- Interest rates** are **variable**, and often **higher** than loans.
    - **-** The bank can ask for the **overdraft** back immediately **anytime**.
- **Trade credits:** Delaying payment to your creditors, which leaves the company with better cash flow for that month.
    - + It is almost a short-term **interest free** loan.
    - **-** The supplier could **refuse** to give **discounts** or to **supply** you at all if your payments are delayed too much.
- **Factoring of debts**

Medium-term finance:

Finance available for 3 to 10 years that is used to buy fixed assets such as machinery and vehicles.

- **Bank loans**
- **Hire purchase:** This allows firm to pay for assets over time in monthly payments which has interest.
    - + The firm does **not** have to come up with **a lot of cash** quickly.
    - **-** A **deposit** has to be paid at the start of the period of payment.
    - **- Interest** paid can be **very high**.
- **Leasing:** Hiring something. Businesses could use the asset but will have to pay monthly. The business my choose to buy the asset at the end of the leasing period. Some businesses sell their fixed assets to a leasing company who lease them back so that they could obtain cash. This is called **sale and leaseback**.
    - + The firm does **not** have to come up with **a lot of cash** quickly.
    - + The leasing firm **takes care** of the assets.
    - **-** The total leasing costs will be **higher** than if the business has purchased it.

Long-term finance:

This kind of finance is available for more than 10 years. The money is used for long-term fixed assets or the takeover of another company.

- **Issue of shares:** Shares are sometimes called **equities**, therefore issuing shares is called **equity finance**. **New issues**, or shares sold by public limited companies can raise near limitless finance. However, a business will want to give the **right issue** of shares so that the amount bought by shareholders will not upset the balance of ownership.
    - + A **permanent** source of capital that does not have to be **repaid**.
    - + **No interests** paid.
    - **- Dividends** will have to be paid. And they have to be paid after **tax** (so taxes become higher), while interest on loans are paid before taxes.
    - **- Ownership** of the company could change hands to the **majority shareholder**.
- **Long-term loans or debt finance:** Loans from a bank, and this is how they are different from issuing shares:
    - Interest is paid before taxes, it is counted as an **expense**.
    - Interest has to be **paid every year** but dividends only need to be paid if the firm has maid **profit**.
    - They are **not permanent** capital.
    - They need **collateral**.
- **Debentures**

How the choice of finance is made in a business

These are the factors that managers consider when choosing the type of finance they need.

- **Purpose and time period:** Managers need to **match** the source of finance to its purpose. It is quite simple, **short-term** finance is used to buy **current assets** and things like that, while **long-term** finance for **fixed assets** and similar things.
- **Amount needed:** Different types of finance depends on how much is needed.
- **Status and size:** Bigger companies have **more choices** of finance. They pay **less interest** to banks.
- **Control:** owners lose control if they own less than **51%** of **shares** in their company.
- **Risk and gearing:** loans raise the **gearing** of a business, meaning that their **risk** is increased. Gearing is can be obtained by calculating the **percentage** of **long-term loans** compared to **total capital**. If long-term loans take up more than 50% of total capital, then the business would be called **highly geared**. This is very **risky** because the business will have to pay back a lot of its loans and has to succeed to do so. Banks are less willing to lend to these businesses, so they will have to find other types of finance.

Will banks lend and will shareholders invest?

Loans will be available to businesses but information about the business is required:

- The firms's **trading records**.
- **Forecasts** about the future.
- **Forecasts** have to show that the firms are **solvent**, i.e. able to repay the loan and the interest back.

Banks will also consider:

- **Experience** of the people running a business.
- **Gearing ratio** of a business.

This is what shareholders will consider if they want to invest:

- The **future prospects** of the company.
- How much **dividends** are given out compared to other companies.
- **Trend** of **share prices**.
- **Gearing ratio**.

Business plans

Banks will want to see a business plan if they are to lend to most businesses, especially a newly created one. A business plan contains:

- **Objectives**.

- How the business will be **operated**.
- How the business will be **financed**.

By creating a business plan owners will have to think carefully ahead about their business to ensure the best plan possible. These are things they will need to consider:

- **Target market** and **consumers**.
- **Profits**, **costs** and **break-even point**.
- **Location** of the business.
- **Machinery** and **workers** required.

Without a **detailed** plan which **works**, bank managers will be reluctant to lend any money to businesses because their owners have not shown that they are serious enough about their business.

Here is an example of a business plan from the book, it shows the things you need to put in a business plan:

Case study example

Business plan for Pizza Place Ltd
(Outline only – other, more detailed information, would be given in an actual plan.)

Name of business	Pizza Place Ltd
Type of organisation	Private limited company
Business aim	To provide a high-class takeaway pizza service including home delivery
Product	High quality home-cooked pizzas
Price	Average price of $5 with $1 delivery charge
Market aimed for	Young people and families
Market research undertaken and the results	Research in the area conducted using questionnaires. Also, research into national trends in takeaway sales and local competitors (See results of all research in the appendix to this plan.)
Human Resources plan	Two staff (the business owners) to be the only staff to be employed initially
Details of senior staff/business owners	Peter Yang – chef of 15 years' experience Sabrina Hsui – deputy manager of restaurant for three years
Production details and business costs	Main suppliers – P & P Wholesalers Fixed costs of business – $50,000 per year Variable costs – approximately $1 per unit sold
Location of business	Site in shopping street (Brunei Avenue) just away from the town centre. Leasehold site (10 years)
Main equipment required	Second-hand kitchen equipment – $4,000 Second-hand motorbike – $1,000
Forecast profit	(See financial appendix to this plan.) Summary: In the first year of operations the total costs are forecast to be $55,000 with revenue of $85,000. Predicted profit = $30,000 Break-even point – 12,500 units per year
Cash flow	(See financial appendix to this plan.) Due to the high set-up and promotion costs there will be negative cash flow in the first year
Finance	$10,000 invested by each of the owners Request to bank for a further $10,000 plus an overdraft arrangement of $5,000 per month

Chapter 10: Organisational Structure

What is organisational structure?

Organisational structure refers to the levels of management and division of responsibilities within a business, which could be presented in an **organisational chart**.

For simpler businesses in which the owner **employs only himself**, there is no need for an organisational structure. However, if the business expands and employs other people, an organisational structure is needed. When **employing** people, everybody needs a **job description**. These are its main **advantages**:

- People who apply can see what they are expected to do.
- People who are already employed will know exactly what to do.

Here is an example of a Job Description taken from the book:

Job Description

Shop Assistant

Main tasks

- To open the shop in the morning
- To be responsible for ordering all goods from suppliers
- To arrange all shelf displays
- To help serve customers
- To assist the manager in other ways directed by him

Working conditions

- Five days a week
- Eight hours a day
- Four weeks' holiday – by negotiation, but not at same time as the manager

When there are more than one person in a small business and they all do different things, it means that they are **specialising** in different jobs.

Delegation

Delegation refers to giving a subordinate the **responsibility** and **authority** to do a given task. However, the **final responsibility** still lies with the person who delegated the job to the subordinate. Here are the advantages of delegation for managers and employees, as well as why some managers choose not to delegate.

Advantages for the manager:

- By letting subordinate do smaller tasks, managers have **more time** to do more important tasks.
- Managers are less likely to make **mistakes** if tasks are done by **specialist** employees.
- Managers can **measure** the **success** of their task more easily.

Advantages for the subordinates:

- Work becomes more **interesting** and **rewarding**.
- Employees feel **important** and **trusted**.
- Helps **train** workers, giving them better **career opportunities**.

Why some managers don't want to delegate:

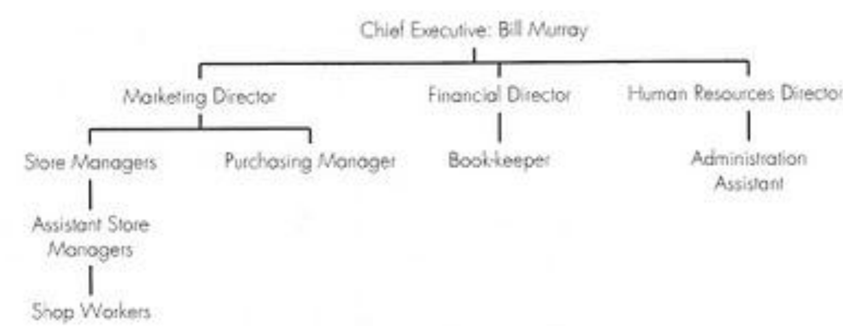
- Managers are afraid that their employees will **fail**.
- Managers want total **control**.
- Managers are scared that the subordinate will do tasks **better** than them, making them feel **insecure**.

Delegation must mean:

- A **reduction** in **direct control** by managers or supervisors.
- An **increase** in **trust** of workers by managers or supervisors.

Organisational charts

Eventually, when a business grows larger and employs many people, they will have to create an **organisational chart** to work out a **clear structure** for their company. Here is another example of an organisational chart from the book:



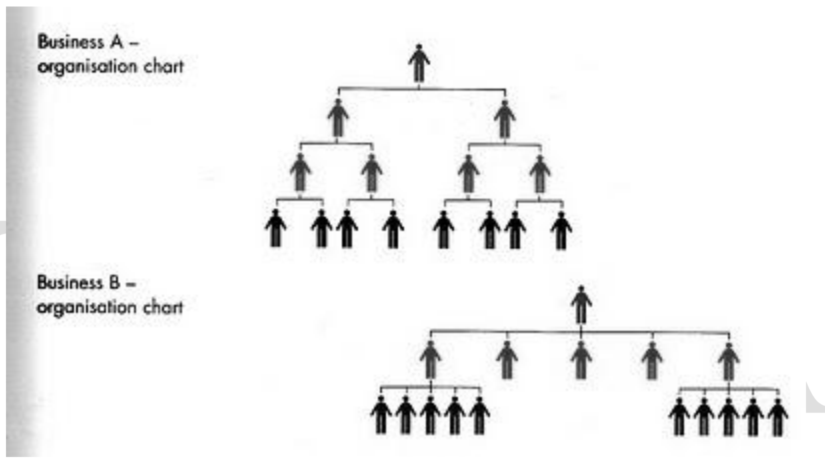
Here are the most **important features** of the chart:

- It is a **hierarchy**. There are different **levels** in the business which has different **degrees of authority**. People on the same level have the same degree of authority.
- It is organised into **departments**, which has their own **function**.
- It shows the **chain of command**, which is how power and authority is passed down from the top of the hierarchy, and **span of control**, meaning how many subordinates one person controls, of the business.

Advantages of an organisational chart:

- The charts shows how everybody is **linked together**. Makes employees aware of the **communication channel** that will be used for messages to reach them.
- Employees can see their **position** and **power**, and who they take orders from.
- It shows the **relationship** between departments.
- Gives people a sense of **belonging** since they are always in one particular department.

Chain of command and span of control:



Here are two organisations, one having a long chain of command and the other a wide span of control. Therefore, the longer the chain of command, the taller the business hierarchy and the narrower the span of control. When it is short, the business will have a wider span of control.

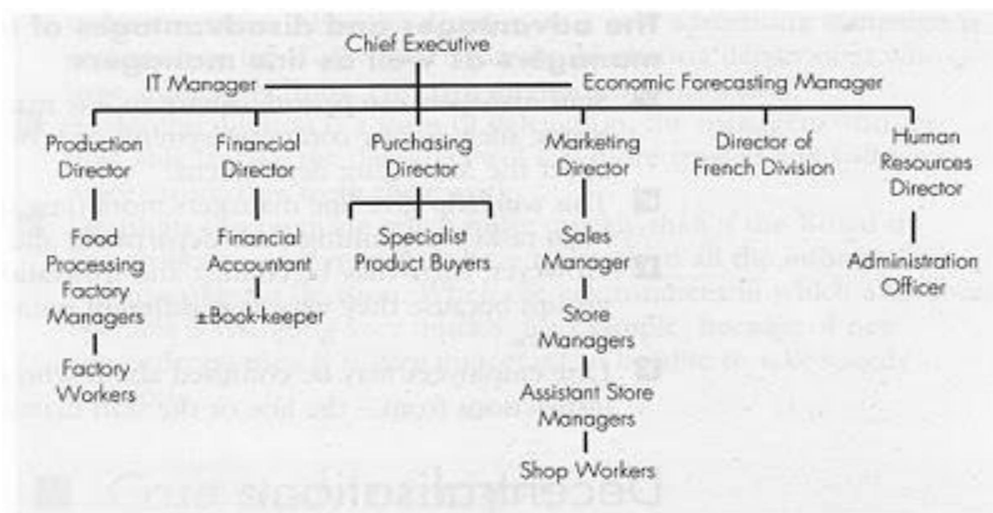
In recent years, people have began to prefer to have their business have a wider span of control and shorter chain of command. In some cases, whole levels of management were removed. This is called **de-layering**. This is because short chains of commands have these advantages:

- **Communication** is **faster** and more **accurate.** The message has to pass through less people.
- **Managers** are **closer** to all employees so that they can understand the business better.
- **Spans of control** will be wider, meaning that the manager would have to take care of more subordinates, this makes:
  - The manager **delegate** more, and we already know the advantages of delegation.
  - Workers gain more **job satisfaction** and **feel trusted** because of delegation.

However, if the span of control is too wide, managers could **lose control**. If the subordinates are poorly trained, many mistakes would be made.

Functional departments

Here is an example of an organisational chart from a larger business from the book:



Here are they key features of this graph:

- The business is divided into **functional departments**. They use **specialists** for each job and this creates more **efficiency**. However, workers are more **loyal** to their department than to the organisation as a whole. Therefore, **conflict** can occur between different departments. Managers working in these departments are called **line managers**, who have direct authority and the power to put their decisions into effect over their department.
- Not only are there departments, there are also other **regional divisions** that take care of outlets that are situated in other countries. They use the local knowledge to their advantage.
- There are some departments which do not have a distinctive function but still employs **specialists** and report directly to the **CEO/Board of Directors**. These departments are the **IT department**, and the **Economic Forecasting department**. Some say the **HR** department fits in this category. These departments give **specialist advice** and **support** to the board of Directors and **line managers**, and the managers of these departments are called **staff managers**. They are often very highly qualified personnel who specialises in only their area.

Here are the pros and cons of employing **staff managers**:

Advantages:

- Staff managers **help** and **provide advice** for line managers on things such as computer systems.

- Helps line managers **concentrate** on their **main tasks**.

Disadvantages:

- There may be **conflict** between the two groups on important decisions and views.
- Line employees may be **confused** and do not know who to take orders form, line or staff managers.

Decentralisation

Decentralisation refers to a business **delegating** important decisions to lower divisions in the business. In a **centralised** structure important decisions are taken at the **centre**, or higher levels of management.

Advantages of a decentralised structure:

- Decisions are made by managers who are "**closer to the action"**.
- Managers feel more trusted and get more job satisfaction due to **delegation**.
- **Decisions** can be made much more quickly.
- The business can **adapt** to **change** much more quickly.

Decentralisation means that:

- Less **central control**.
- More **delegation**.
- Decisions taken "**lower down**" in the organisation.
- **Authority** given to departments/regions

Different forms of decentralisation:

- **Functional decentralisation: Specialist** departments are given the authority to make **decisions**. The most common of these are:
  - Human Resources.
  - Marketing.
  - Finance.
  - Production.
- **Federal decentralisation:** Authority is **divided** between different **product lines**. e.g separate truck/car/bus divisions.
- **Regional decentralisation:** In **multinationals**, each **base** in each country has authority to make its own decisions.
- **Decentralisation by project means:** For a certain **project**, decision-making authority is given to a **team** chosen from all functional departments.

Is complete decentralisation a good idea?

It is dangerous to let the lower-level management make all the decisions. Therefore, it is wise for the **central management** to decide on **major issues**, **long-term decisions**, **growth** and **business objectives**. If these issues are not **centralised** then there would be a **lack of purpose** or **direction** in the business.

Chapter 11: Managing a business

What do managers do?

All organizations have **managers**. They can come by the name of director, headmaster, etc... but they all perform similar **tasks**. These tasks are:

Planning:

Planning for the future involves **setting goals** for a business. These goals give the business a **sense of direction** and **purpose**. Now the whole business will have something to work towards. Managers also need to plan for **resources** which will be needed. These are only two **strategies** managers use to keep the business running.

Organising:

A manager cannot do everything by himself. Therefore, jobs must be **delegated** to employees. Employees need **sufficient resources** to complete their job, so managers need to **organise people** and **resources** effectively.

Co-ordinating:

Managers need to **bring people together** in a business for it to succeed. This is called **co-ordination**. If different **functional departments** do not co-ordinate, they could be doing completely different things which does not follow any common plan. Managers could co-ordinate the departments by holding regular **meetings** or setting up a **project team** with different members from different departments.

Commanding:

Commanding refers to **guiding**, **leading** and **guiding** subordinates which is very important in any organisation. Managers need to make sure that all subordinates are **following targets** and **deadlines**. It is the **responsibility** of the manager to ensure that all tasks are completed and therefore **instruction** and **guidance** must be provided to employees so that they can do so.

Controlling:

Controlling means **evaluating** the **performance** of subordinates, so that **corrective action** can be carried out if the subordinates are not sticking to **goals**.

To sum up, this is what management gives to any organisation:

- a sense of **control** and **direction**.
- **co-ordination** between departments, preventing **wastage** of **efforts**.
- **control** of employees.
- making the most out of **resources** (**organisation**)

What makes a good manager?

There are different views of why some managers are better than others. Some say that managers are born that way, while others say good managers are trained. However, good managers do have these distinct characteristics:

- **intelligence:** to understand difficult ideas and deal with different issues.
- **initiative:** to be able to think of solutions and take control of situations.
- **self-confidence:** to be willing to lead others and be a model image.
- **assertiveness and determination:** to be able to take command of others and take ideas and solutions to the end.
- **communication skills:** to be able to inform subordinates in a clear way so that they will respond positively.
- **energy and enthusiasm:** to work with high effort and involvement so that others will follow.

Styles of leadership:

Different managers use different styles of leadership, and each one makes subordinates react in a certain way. It is important for the managers to choose the appropriate leadership style for the right situation. These styles will be discussed in Chapter 13: Motivation at work.

Management involves taking risks:

All managers need to make decisions in what they do, whether it is planning, organising, co-ordinating, ect. All as you know, all decisions involve some sort of risk.

Are all decisions as important as each other?

There are three types of decisions which has their type of importance and the length of time that is is going to affect the business. They are:

- **Strategic:** These are very important decisions that will affect the overall success of an organisation. They are long-term decisions such as company goals or growth. They are usually taken by the top management.
- **Tactical:** These are decisions that are less important decisions that are taken more frequently. They can include: new ways to train staff, new transportation routes used, advertising methods, etc... They are usually taken by the middle management.
- **Operational:** They are day-to-day decisions taken by the lower management. They tend to be repetitive and previous experience could be used to help making these decisions. They can be: inventory/stock levels, ordering goods, dealing with customers.

All of these decisions involve risk. Since they all cost **time**, **money** and **opportunity** cost one should think well before making a decision.

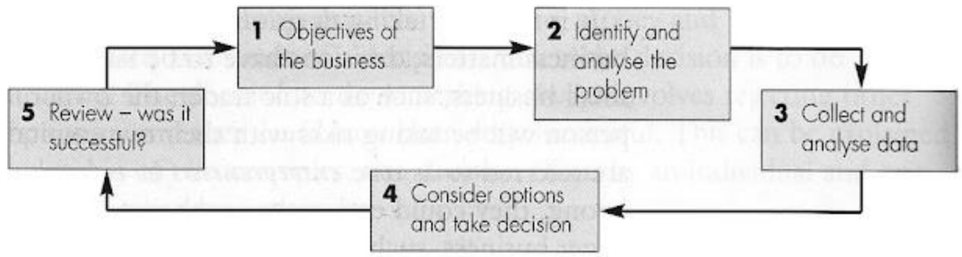
In business, decisions need to be made and the risks need to be accepted. People like sole traders who have unlimited liability risk loosing all that they own by setting up a business are called **entrepreneurs**. As we already know they are the **managers** and **risk-takers** of a company. Managers in a limited company are not "real" entrepreneurs, because they are not risking their assets but the capital of the shareholders.

How can managers reduce risks when taking decisions?

Risks are the **results of failure**. Risks cannot be eliminated, but they can be reduced by the process of making decisions. Here are the steps:

- **Set goals**: It is impossible to make decisions if the aims are not clear.
- **Identify and analyse the problem:** Managers all make decisions to solve a problem. This problem might be how to use your salary in the most efficient way possible, how to spend the rest of your life, etc... It is imperative that you must understand the problem before finding a solution for it. Otherwise, you might make the wrong decision.
- **Collect data on all possible alternative solutions:** It is always important to analyse all possible solutions to find which one is the best. The data collected should also contain **constraints** and **limitations** on the possible decisions (e.g. the law).
- **Make the final decisions and put it into effect:** This is called **implementing the decision**. This means that the manager must see to it that the decision is carried out and is working to plan.
- **Review and evaluation of decision:** This is looking back at the decision to identify pros and cons of a decision so that the experience can be used in the future. This is often hard to do especially when the wrong decision is made. It is nevertheless necessary.

Here is a decision-making flow chart from the book that will help you visualise the process:



Management responsibilities in departments:

Human resources department:

- **Forecasting** staffing needs.
- **Recruiting** staff.
- Preparing the **job descriptions** and **job specifications**.
- Planning and implementing staff **training** programmes.
- **Interviewing** and **selecting** staff.
- **Negotiating** with worker representatives, such as union leaders, on **wages** and **working conditions**.
- Keeping **staff records**.
- **Disciplining** staff

The role of this department is becoming more and more important as the cost of hiring staff rises, so that it is crucial for the HR department to manage people firmly and fairly. An unsuccessful HR department results in a high **staff turnover** (people leaving the business early). The department must also make sure that the business and staff comply with all employment laws.

Marketing department:

- Market research for:
  - New **products**.
  - New **markets**.
  - New **opportunities**.
- **Planning** the release of new products, often working with the Production and R&D departments.
- Decide on the best **marketing mix** (discussed later) for a product and implementing it.
- Keeping track of products so **extension strategies** can be used or to take the product off the market.

The marketing department is crucial for the business to keep in touch with its customers. No business can survive without this kind of function.

Accounting and finance department:

- Recording all **financial transactions**.
- Collecting all the data and presenting it as the **regular accounts**.
- Preparing all **budgets**.
- Analysing the **profitability** of new projects.
- Deciding on which **source of finance** to use.
- Keeping control over business **cash flow**.

Production department/Operations management:

- Ordering **stock/inventory** of **materials** and **resources** used for producing goods.
- **Developing** and **designing** new products.
- **Locating** in the most cost-effective place possible.
- Deciding on the **methods of production** and **machinery**. Purchase of new machinery will involve the Finance department.
- Controlling production to maintain high levels of **efficiency**.
- Maintaining the **efficiency** of **machines**.
- Keeping the **quality** high to meet the **standards** of the consumers. All staff will need to co-operate because poor quality is normally blamed on bad staff.

Administration department:

The responsibilities of the Administration department varies with the business it is in. For example, in smaller businesses, the administration department would be the same as the Accounts and Finance department. A larger business will have more specialized administrative department. These are what the the department does:

- **Clerical and office support services:** Ensure the smooth running of all other departments.
  - **Sorting** of incoming **mail** and sorting and franking of outgoing mail.
  - **Reception** will greet visitors, answer calls, and schedule rooms for meetings.
  - **Office** tasks will include filing all records. e.g. visitors and calls.
  - **Information** and **data** processing.
- **Responsibility for the IT system:**
  - The **IT** department is part of the Administration department.
  - Allows **information** to be **delivered** between departments **accurately.**
  - Provides managers with **data** to help in decision making.
- **Cleaning, maintenance and security:**
  - Vital for **safe** and **healthy working conditions**.
  - Failure to maintain **equipment** and **the building** (e.g. air conditioner) will result in reduced **efficiency**.

The widespread use of **computers** means that many workers in all departments can do some of these tasks by themselves (clerical and support services), reducing the function of the Administration department and make them less common in businesses.

Chapter 12: Communication in business

What is effective communication and why is it necessary?

Communication is when a **message transferred** from one person to another and is **understood** by the latter. We communicate everyday (by talking, by chatting, by texting, etc.) but we need to learn how to communicate **effectively**. Effective communication means that:

*"The information or message being sent is **received**, **understood** and **acted upon** in the way **intended**."*

In business, ineffective communication or communication failure could result in serious problems.

Why do people within business need to communicate with each other?

In business, if we do not communicate, we would be working as individuals with no co-ordination with anybody else in the business. The management, whose tasks are guiding, instructing and commanding subordinates, could not be done because they cannot communicate with them. Here are some common messages found in the workplace:

- No Smoking (sign)
- You are fired because you are always late (letter)
- Do not touch (sign)
- There will be a fire drill 11:00 today (notice board)

There are many more things that are communicated. Consequences would be severe if these matters are not communicated effectively.

The process of effective communication:

Effective communication involves four features:

- The **transmitter/sender** who sends the message. He has to choose the next two features carefully for effective communication.
- The **medium of communication**. It is the method of communication, e.g. notice board, letter, etc...
- The **receiver** who receives the message.
- **Feedback** means that the receiver has received the message and **responds** to it. This confirms that the message has been **understood** and **acted upon** if necessary.

One-way and two-way communication

There are two types of communication. **One-way** communication is when there is no feedback required for the message, or the receiver is not allowed to reply. This might be the sign that says "No smoking", or your boss saying: "give me a biscuit". The other is **two-way** communication, when feedback is required. Therefore, both people are now involved in the communication process. This could lead to better and clearer information.

Advantages of two-way communication:

- The sender can now **know** whether the **receiver** has **understood** and **acted upon** the message or not. If they have not, the message might have to be **sent again** or **made clearer**. Effective communication takes place only if the message is understood by the receiver.
- **Both** people are **involved** in the communication process. This makes the receiver feel more **important** which might **motivate** them to make better contributions to the topic discussed.

Internal and external communication

Internal communication is messages sent between people **inside** a business. For example:

- The boss talking to his subordinates.
- A report sent to the CEO.

External communication refers to messages sent to people or organisations outside the business. For example:

- Orders for goods from suppliers.
- Talking to customers.
- Advertising to the public.

Both types of communication is almost the same, the only difference is **who** is being communicated with.

Why external communication has to work well

External communication can greatly affect the **efficiency** and **image** of a business. Imagine if the wrong information is sent to a supplier and a customer. The supplier would send wrong materials while the customer might buy products from another company. Here are some cases which ineffective external communication might turn out to be very dangerous:

- The Finance Manager writes to the tax office inquiring about the amount of tax that must be paid this year.
- The Sales Manager receives an order of 330 goods to be delivered on Wednesday.
- The business must contact thousands of customers because a product turned out to be dangerous. An add must be put into the newspaper so that customers can return the product for a refund.

Different ways of communicating: the communication media

Information can be transmitted in several ways:

- **Verbal**: Involves the sender **speaking** to the receiver.
- **Written**: The message is **written** to the receiver.
- **Visual**: Using **charts**, **videos**, **images** or **diagrams** to communicate a message.

There is no best method of communication, so the appropriate medium of communication must be selected depending on the situation. First the sender also has to analyse the advantages and disadvantages of each type of communication.

Verbal communication

Verbal/Oral communication might be:

- One-to-one talks.
- Telephone conversations.
- Video conferencing.
- Meetings.

Advantages:

- Information is transferred **quickly**. This is an efficient way to communicate in meeting to lots of people.
- There is opportunity for **immediate feedback** which results in **two-way** communication.
- The message might be **enforced** by **seeing** the speaker. Here the **body language** and **facial expression** could make the message easily understood.

Disadvantages:

- In big meetings, we do not know if everybody is **listening** or has **understood** the message.
- It can take **longer** for **verbal feedback** to occur than **written feedback**.
- Verbal communication is **inappropriate** for storing **accurate** and **permanent** information if a message. (e.g. warning to a worker)

Written communication including electronic communication

Here are some written forms of communication:

- **Letters**: Used for both external and internal communication. Follows a set structure.
- **Memos**: Used only for internal communication.
- **Reports**: Detailed documents about any problem. They are done by specialists who send them to managers to analyse before meetings. These reports are often so detailed that they cannot be understood by all employees.

- **Notices**: Pinned to notice boards that offer information to everyone. However, there is no certainty on whether they are read or not.
- **Faxes**: Written messages sent to other offices via telephone lines.
- **E-mails**: Messages sent between people with the same **computing facilities**. The message is printed if a **hard copy** is needed.
    - **Intranet**: A network inside a business which lets all employees with a computer message each other.
    - **Internet**: The global network for messaging anyone. (e.g. customers, suppliers)

Advantages:

- There is **hard evidence** of the message which can be referred to and help solve **disputes** in the **future** over the content of the message.
- It is needed when **detailed** information is transferred: it could be easily **misunderstood**. Some countries the law states that businesses need to put safety notices up because people could **forget** them.
- The written message can be **copied** and sent to **many people**.
- **Electronic communication** is a **quick** and **cheap** way to get to many people.

Disadvantages:

- **Direct** feedback is not always possible, unless electronic communication is used. However, this could result in too many emails sent (**information overload**). Direct feedback via other means of written communication is hard.
- It is not as easy to **check** whether the message has been **understood** or **acted upon**.
- The **language** used might be **difficult** to **understand**. The message might be **too long** and **disinterest** the reader.
- There is no opportunity for **body language** to be used to **enforce** the message.

Visual communication

Here are some forms of visual communication:

- **Films**, **videos**, and **PowerPoint displays**: often to help train new staff or inform sales people about new products.
- **Posters**: can be used to explain a simple but important message. (e.g. propaganda poster)
- **Charts** and **diagrams**: Can be used in letters or reports to **simplify** and **classify** complicated data. Computer technology could help in the design of these charts or diagrams. A printed copy might be needed for **hard** data to add to reports and documents.

Advantages:

- Present information in an **appealing** and **attractive** way that **encourages** people to look at it.
- They can be used to make a written message **clearer** by adding a picture or a chart to illustrate the point being made.

Disadvantages:

- **No feedback** is possible. People need to check via verbal or written communication to check that they have understood the message.

- Charts and graphs might be **difficult** for some people to **understand**. The message might be misunderstood if the receiver **does not know how** to **interpret** a **technical diagram**.

Formal and informal communication

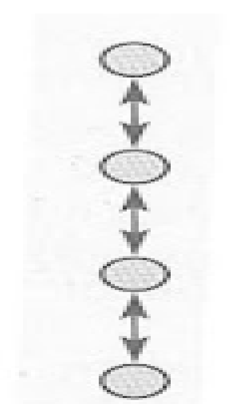
Formal communication is the channel of communication that is **recognised** by the business, such as notices on boards, emails and memos. Formal means of communication is important. It shows that the information given is true.

Informal communication might be communication between friends and co-workers. There is no set structure and the information transferred is not **recognised** by the business. This channel of communication could be used by the manager to **try out new ideas**, before publicly announcing it to the rest of a company. However, informal communication can result in **gossip** can **rumour**, and managers have no way to remove these informal links from people.

Communication nets

There are many groups of people in any organisation, and each of them communicate in different ways. People have connections with each other, and these links form **communication nets**. There are three standard types of communication nets:

Chain network:

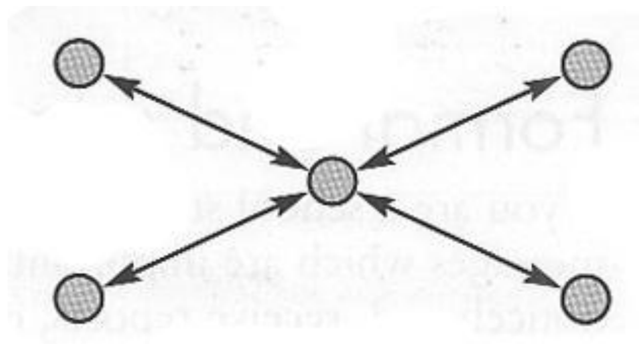


+ Can be used to transfer **important messages** from higher management levels to lower levels.

- This often leads to **one way** communication.

- The message could become **altered** as it passes through different management levels.

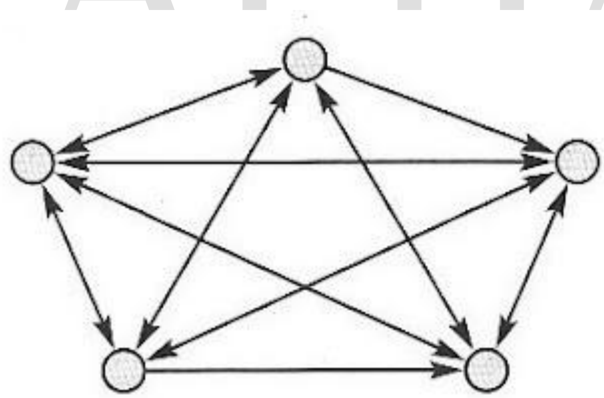
Wheel network:



\+ The central management can pass messages to **all departments** quickly.

- The departments **cannot** communicate **directly between themselves**.

Connected network:



\+ This is used to **create** or **discuss new ideas**.

\+ It specialises in **two-way communication**.

- Can be **time-consuming**.

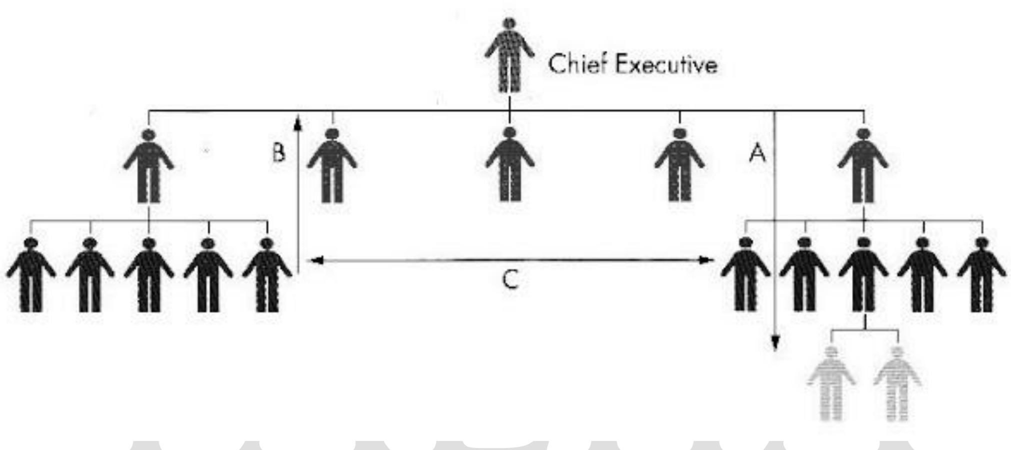
- There is no **clear leader** or **sender** of messages.

Which network works best?

There is again, no best network. A company is likely to use different network at **different times** or for **different groups**.

- The **chain network** is for communicating **important business policies**.
- The **wheel network** is used for sending different messages to different **departments**.
- The **connected network** is used to generate new **ideas** or **solutions** to problems where **group discussion** is the most effective.

The direction of communications



Here is an organisation chart from the book explaining the direction of communications within the business. The arrows are labeled A, B and C which shows the direction of communication:

- **Arrow A (downwards communication)**:
  - Used by managers to send **important messages** to **subordinates**.
  - Does **not** allow **feedback**.
  - The message might be **altered** after passing different levels.
- **Arrow B (upwards communication)**:
  - Used by subordinate send **feedback** to **managers**.
  - Feedback from subordinates ensures that there is **effective communication.**
  - Feedback results in higher **morale** and new **ideas** contributed to the business.
- **Arrow C (horizontal/lateral communication)**:
  - People at the **same level** of management communicate with each other.
  - Information and ideas can be exchanged both **formally** and **informally**.
  - Can cause **conflict** between departments. (e.g. Production department asks the Finance department for a budget to hire new staff but is rejected)

Barriers to effective communication

As we already know, the four parts of effective communication includes the **sender**, **medium**, **receiver** and **feedback**. However, communication may fail if there are problems with one of these four features. If one part fails, it becomes a **barrier to effective communication** which might cause a **breakdown in communication** resulting in serious consequences to the business. Here are some common barriers to effective communication and how to overcome them.

Problems with sender:

- **Problem:** Language is too difficult to understand. Technical **jargon** may not be understood.
  Solution: The sender should ensure that the receiver can **understand** the message.
- **Problem:** There are problems with **verbal** means of communication. (e.g speaking too quickly)
  Solution: The sender should make the message as **clear** as possible and ask for **feedback**.
- **Problem:** The sender sends the **wrong message** to the **wrong receiver**.
  Solution: The sender must ensure that the **right person** is receiving the **right message**.
- **Problem:** The message is **too long** with too much **detail** which prevents the **main points** from being understood.
  Solution: The message should be **brief** so that the **main points** are understood.

Problems with the medium:

- **Problem:** The message may be **lost**.
  Solution: Check for **feedback**. Send the message **again!**
- **Problem:** The **wrong channel** has been used.
  Solution: Ensure the **appropriate channel** is selected.
- **Problem:** Message could be **distorted** after moving down a long chain of command.
  Solution: The **shortest channel** should be used to avoid this problem.
- **Problem: No feedback** is received.
  Solution: Ask for it! Use **different methods** of communication (e.g. meeting)
- **Problem: Breakdown** of the medium.
  Solution: Use **other forms** of communication.

Problems with the receiver:

- **Problem:** They might not be **listening** or **paying attention**.
  Solution: The **importance** of the message should be **emphasised**. Request **feedback**.
- **Problem:** The receiver might not like or **trust** the sender, and may be **unwilling** to **act upon** the message.
  Solution: Trust is needed for effective communication. Use **another sender** to communicate the message.

Problems with the feedback:

- **Problem:** There is **no feedback**.
  Solution: Ask for feedback. Use a different **method** of communication which **allows feedback**.
- **Problem:** The feedback is received **too slowly** and may be **distorted**.
  Solution: Direct lines of communication should be available between the subordinate and the manager.

Note: The **forms** of communication are: verbal, written and visual.The **methods** of communication can be: telephone, e-mail, meeting, etc...

Chapter 13: Motivation at work

Motivation

People work for a number of reasons. Most people work because they need to earn money to survive, while others work voluntarily for other reasons. **Motivation** is the reason why people work, and it **drives** them to work better. Therefore, managers try to find out what motivate workers and use them to encourage workers to work **more efficiency**. This results in higher **productivity**, increased **output**, and ultimately higher **profits**.

- Nowadays, machinery is more common in businesses which results in increased productivity as well. However, the amount that a well motivated workforce can produce must still be recognised, since employees are a firms greatest assets!

Motivation theories

People work very hard when they are working for themselves. When they work for other people, less so. Managers have been looking into what makes employees contribute their fullest to the company and these studies have resulted four main theories of motivation.

F.W.Taylor

Theory:

- **Money** is the main motivator.
- If employees are **paid more**, they **work more**.
- Work is broken down into simple processes, and **more money** is paid which will increase the **level** of **productivity** an employee will achieve.
- The **extra pay** is **less** than the **increased productivity**.

Disadvantages:

- Workers are seen rather like **machines**, and this theory does not take into account **non-financial motivators**.
- Even if you pay more, there is **no guarantee** of a productivity rise.
- It is **difficult** to **measure** an employee's output.

Maslow

Maslow created what is known as the **hierarchy of needs**.

In this diagram, there are 5 different types of motivation:

- **Physiological needs:** basic requirements for survival.
- **Security needs:** the need to by physically safe.
- **Social needs:** the need to belong and have good relationships with co-workers.
- **Esteem needs:** the need for self-respect and to be respected by others.
- **Self-actualisation needs:** the need to reach your full potential and be promoted.

Businesses realise that the more **levels of motivation** are available to workers, the harder they will work. Maslow also suggest that each level of motivation **must** be **achieved before** going to the **next level**. Once one level of motivation is met, more of that will **no longer** motivate the employee.

Disadvantages:

- Some levels are **not present** in some jobs.
- Some rewards belong to **more than one level** on others.
- Managers **need** to **identify** the levels of motivation in any job before using it to motivate employees.

<u>Herzberg</u>

To Herzberg, humans have **hygiene factors**, or basic animal needs of humans. We also have **motivational factors/motivators** that are required for the human to grow psychologically.

Hygiene factors:

- Status.
- Security.
- Working conditions.
- Company policies and administration.
- Relationship with supervisor.
- Relationship with subordinates.
- Salary.

Motivational factors:

- Achievement.
- Recognition.
- Personal growth/development.
- Advancement/promotion.
- Job satisfaction.

To Herzberg, if the hygiene factors are **not satisfied**, they will act as **demotivators**. They are **not motivators**, since the motivating effect quickly wears off after they have been satisfied. True motivators are are Herzberg's motivational factors.

McGregor

McGregor splits his theory into what managers believe. One type believes in **theory X**, while the other type believes in **theory Y**. Here is the table:

Here are some differences in how an **X manager** will work and how a **Y manager** will work:

- X managers believe that people are naturally lazy, and has to be pushed with **external factors** to work harder. (e.g. higher pay).
- Y managers believe that people want to do a good days work but need a good **environment** to do the work. A better environment is an **internal factor**.
- X managers will try to provide **incentives** and **supervision** for employees to work hard.
- Y managers will try to provide a **favourable environment** so that employees can enjoy their work.

Theory's like **Taylor's theory** are X theories, while others like **McGregor's theory** are Y theories. People may say that money is the main motivator, but studies have shown that many people leave jobs because other motivational factors are not available to them.

Why do people work?

Here is a summary of why people work:

- **Money**: to satisfy needs and wants.
- **Security**: knowing that you are physically safe and have job security.
- **Social needs**: to belong to a group, making friends at work.
- **Esteem needs** (self importance): feeling important, feeling the job you do is important.
- **Job satisfaction**: enjoyment from the feeling of having done a good job.

Motivating factors - financial motivators

There are three ways to motivate a workforce:

- financial motivators
- non-financial motivators
- ways to increase job satisfaction

Financial rewards

Pay may be the basic reason why people work, but different kinds of pay can motivate people differently. Here are the most common methods of payment:

Wages

Wages are paid **every week**, in **cash** or straight into the bank account, so that the employee does not have to wait long for his/her money. People tend to pay wages to manual workers. Since wages are paid weekly, they must be calculated every week which takes time and money. **Wages clerks** are paid to do this task. Workers get **extra pay** for the **overtime** that they do. There are some ways that wages could be calculated:

<u>Time rate</u>: Time rate is payment according to how many **hours** an employee has worked. It is used in businesses where it is difficult to measure the output of a worker.

- + Easy to calculate the wage of the employee. A **time-sheet** must be filled out by the Accounts department to calculate the wage.
- - Both good and bad workers get paid the same wages. Therefore, more **supervisors** are needed to maintain good productivity. A **clocking-in system** is needed to know how many hours an employee has done.

Here is an example of a wage slip and time-sheet:

Name:............................ Employee no:............................

Employer:............................ Payment date:............................

Payments		Deductions		To date	
Basic wage	450.00	Income tax	110.00	Tax code	489L
Overtime	50.00	National Insurance	45.00	Tax week	3
		Pension	50.00	Tax	310.54
		Trade Union fees	10.00		
Total	500.00	Total	215.00	Net pay	£285.00

Sir Talha Siddiqui
03133106254

Name: ______________ Employee no: ______________

Department: ______________

Standard rate of pay: $10 per hour
Overtime rate of pay: $15 per hour
Basic number of hours per week: 40

	Start time	Finish time	Total hours
Monday	16.00	24.00	8
Tuesday	16.00	24.00	8
Wednesday	16.00	24.00	8
Thursday	16.00	24.00	8
Friday	16.00	24.00	8
Saturday	16.00	18.00	2
Sunday	–		

Total hours for week = 42

40 hours at $10 = $400
2 hours at $15 = $30
Gross pay = $430

They show:

- **Basic pay + Overtime = Gross Pay**
- **Gross pay - Deductions = Net Pay**

Deductions include:

- Taxes
- Pension
- Union fees
- National insurance: entitles the payee to short-term **unemployment benefits**, **sickness benefits** and **state pension.**

<u>Piece rate</u>: Piece rates are paid depending on **how many units** they have produced. There is usually a base pay (**minimum wage**) and the piece rate is calculated as a bonus on how many units were created. Piece rates are found in businesses where it is possible to measure a workers' productivity.

- + Encourages workers to work **faster** and produce **more goods**.
- - Workers will often **neglect quality**, and businesses will need a **quality control system** which is **expensive**.
- - Workers who **focus** on **quality** will **earn less**. **Tension** is caused when some workers **earn more** than others.
- - If **machinery breaks down**, employees earn less. That is why there is a guaranteed **minimum pay**.

Salaries

Salaries are paid **monthly** and normally straight into the **bank account.** They are usually for **white collar workers**. A salary is counted as an **amount per year** that is divided into **12 monthly accounts.** You **do not** usually receive **overtime**. Managers only need to pay their workers once a month, and since the amount is transferred by the bank, the manager loses much less time and money calculate salary.

Salaries are usually a standard rate, but other **rewards** could be given to employees:

- **<u>Commission</u>:** A **percentage** is paid, usually to sales staff, depending on the **value** of **goods** they have sold. Workers are encouraged to sell more. However, they could persuade customers to buy products they don't really want, making the company look bad. Just like the piece rate, in a bad month where there are little sales, worker's pay will fall.
- **<u>Profit sharing</u>:** Employees receive a **percentage** of the **profits** made. However, they will get nothing if the business doesn't make a profit. This is often used in the service sector, where it is hard to find an employee's contribution to the company.
- **<u>Bonus</u>:** A **lump sum** paid to employees who have done well. It is usually paid at the end of the year or before holidays. However, this could cause jealousy between workers. Giving bonuses to a **team** works better.
- **<u>Performance related pay</u>:** Employee pay is linked to the **effectiveness** of their work. It is often used in organisations where it is hard to measure productivity. It uses the system of **appraisal**: employees are observed and their colleagues are interviewed to determine their effectiveness. Afterwards, the immediate superior of the employee has a meeting with them to discuss their effectiveness.
- **<u>Share ownership</u>:** Employees receive some **shares** from the company. They will either benefit from **dividends** or **sell** the shares when their **price** has **risen**. They will be more **motivated** because they feel like a **part** of the company.

Motivating factors - non-financial motivators

There are other factors that motivate people in a business, and they are often called **perks** or **fringe benefits**. They may be having free accommodation, free car, etc... However, when you look at it, it is just money in different forms. Here is a list of these motivators:

- Children's education.
- Discounts on company products.
- Free Healthcare.
- Company vehicle.
- Free accommodation.
- Share options.
- Expense accounts.
- Pension.
- Free holidays.

<u>Job satisfaction:</u>

Employees will become more motivated by **enjoying** the job they do. Job satisfaction can come in different ways. However, there are some **factors** that **demotivate** employees if they are not satisfied, and must be satisfied before the motivators can take effect. Here are some things that make workers' jobs satisfying:

- Pay.
- Promotion.
- working conditions.
- Fringe benefits.
- Management
- Working hours.
- The nature of the work itself.
- Colleagues, etc...

Herzberg and Maslow stresses that things such as **responsibility** recognition **is also crucial** to provide job satisfaction. Letting workers contribute to the job would also help, making jobs less boring and more creative. Here are some policies to increase job satisfaction:

Job rotation:

Workers in a **production line** can now change jobs with each other and making their jobs not so boring. It helps **train** the employee in different aspects of their jobs so that they can **cover** for other employees if they do not show up.

Job enlargement:

Adding tasks of a **similar level** to a worker's job. Job enlargement simply gives more **variety** to employees' work which makes it more enjoyable.

Job enrichment:

Adding tasks of a **higher level** to a worker's job. Workers may need **training**, but they will be taking a step closer to their **potential**. Workers become more **committed** to their job which gives them more satisfaction.

Autonomous work groups or team working:

This is when **group** of workers are given **total responsibility** to organise themselves and perform a task. This makes the employees feel more **important**, as well as giving them a sense of **belonging** when they are part of a team. If they organise themselves differently every time, the team could get **job enlargement** and **job enrichment** too!

Leadership

Studies have shown that leadership has a great impact on worker's motivation. Good managers have **leadership skills** that **inspire** their workers to work better, as well as directing them with a common **goal**. Managers use many styles of leadership, and they can be summarised into 3 main styles:

Autocratic leadership:

- The manager **controls all aspects** of their subordinates' **work**.
- They keep themselves **separate** from employees.
- Employees are expected to obey every **command** and **cannot contribute** to decisions.
- Communication is only **top-down**.

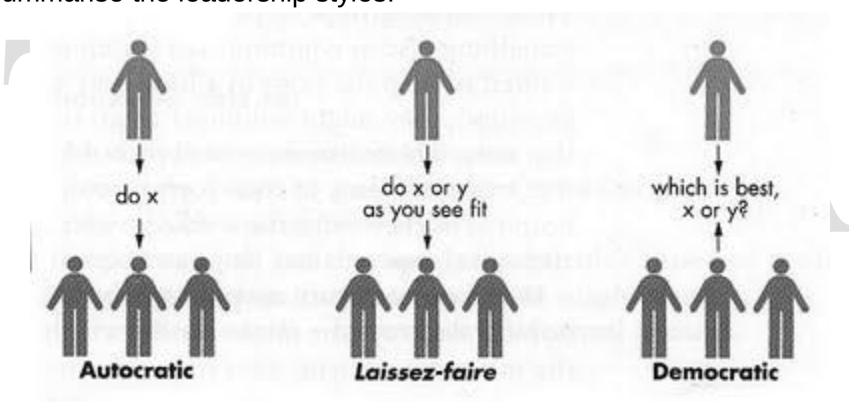
Laissez-faire leadership:

- **Objectives** are shown to employees, but the task is **completely delegated** to them.
- **Communication** can be **difficult** since **clear instructions** are not given.
- The manager has a **limited role** in this type of leadership.

Democratic leadership:

- The manager **discusses** tasks with his employees before making decisions.
- Communication will be **two-way**, both top-down and bottom-up.

Here is a diagram to summarise the leadership styles:



The style of leadership used can vary depending on situations where they are the most effective.

Formal and informal groups

A **formal group** is an **official** group that is formed to do a specific task in an organisation. An **informal group** is a group of people which are formed **independently** by themselves. They are not official, but the people in the group have a **common interest** or **cause**. Both of these groups are needed in business, and let's see why in this example. e.g. a school might create a football team (formal group) but the players need to bond together to play effectively (informal group).

Formal groups in business

Departments within a business are good examples of formal groups. From time to time different groups might be set up to cope with different problems or do different tasks. Sometimes people from different departments could come together in a group to do a **team project**.

Informal groups in business

There are can be many informal groups in a business that can increase the motivation of workers because they have a true sense of **belonging**. e.g. There is a group of factory workers who are interested in basketball, and they form an informal group, as a result, when they get back into their formal group they are likely to co-ordinate better with each other.

There are other scenarios where two departments **merge** to become one, making them one formal group. However, the people from these former departments still see themselves as **separate** from each other. These two groups of people will refuse to co-operate until they are also **merged** into an **informal group**. Therefore, informal groups should be handled carefully in business to yield the best results.

Regular meetings, free holidays, sporting events and such things could be organised to create informal groups and use them in a more positive way to avoid them getting into the way of business activity.

Chapter 14: Recruitment, Training, and human resources

The work of the Human Resources department

We all know that recruitment and selection is one of the tasks that the HR department fulfills. The other tasks will be discussed below:

- **Recruitment and selection:** Involves selecting and attracting the best workers.
- **Wages and salaries:** Must be enough to motivate or attract workers.
- **Industrial relations:** There must be effective communication between departments.
- **Training programmes:** Must meet the training needs of employees and accomplish business objectives.
- **Health and safety:** Must do things according to the law.
- **Redundancy and dismissal:** Must obey all laws when firing workers.

Recruitment and selection

Workers are needed when a business **starts up**, **expands** or an existing employee **leaves**. Businesses use the **recruitment process** to successfully employ the right people. This process is usually undertaken by the HR department, but in small business, HR departments do not exist since the businesses employ too little workers for it to be of much use. Here is a diagram summarising the recruitment process:

1. Vacancy arises.
2. A **job analysis** is done, which identifies the responsibilities and tasks of the job.
3. A **job description** lists that responsibilities and tasks to the candidates who apply for the position.
4. A **job specification** outlines the required **qualifications**, **expertise** and **experience** a candidate needs so that they can be accepted.
5. The job is **advertised** in the **appropriate media**. (e.g. newspapers)

6. Candidates fill out **application forms**, which are **short-listed** so that only the best candidates remain.
7. **Interviews** are held with remaining candidates, and the ones suitable for the job are **selected**.
8. Vacancy filled.

The recruitment process

Job analysis and description:

When a new employee is needed, a **job analysis** needs to be taken to identify the tasks and responsibilities of the position. This should be easy for a job that needs replacement, but not so much for a job that has just been created.

Once all the details of the job has been gathered, a **job description** needs to be drawn up. This job description has several functions:

- Given to **candidates** so they will know what the job will involve.
- Allows a **job specification** to be drawn up which will state the **requirements** for the job.
- Shows whether an employee carries out the job **effectively** or not. It helps **solve disputes** between employees and employers about wages, working hours, etc.

The job description for any business will usually contain:

- The **title** of the job.
- The **department** one will work in.
- Who will be **in charge of** the job-holder?
- Who the job-holder will be **in charge for**.
- The **purpose** of the job (job summary).
- The **main duties** of the job.

Job description sometimes contain information about:

- The **conditions of employment** – working hours, wages, pension schemes.
- **Training** that will be offered.

- Opportunities of **promotion**.

Job specification

After the job description has been drawn up, the **qualifications** for the job can be identified. They usually include:

- The **level** of **educational qualifications**.
- The **amount** and **type** of **experience**.
- **Special skills**, **talents** or **knowledge**.
- **Personal characteristics**. (e.g. type of personality)

Advertising the vacancy

The next stage is on how to get people to know that you have a job to be filled.

Internal recruitment

The vacancy can be filled by an employee already in the business. It might be suitable for employees seeking **promotion**.

Advantages of internal recruitment:

- Saves **time** and **money**.
- The candidates' **reliability**, **ability** and **potential** are **already known**.
- The candidates know the **expectations** and **rules** of the company.
- **Motivates** other employees to work harder to get promoted too.

Disadvantages of internal recruitment

- No **new ideas** or **experience** come into the business.
- May create **jealousy** and **rivalry** between existing employees.

External recruitment

Most vacancies are filled with **external recruitment**, which always involves advertising the vacancy. Here are some suitable media of advertising:

- **Local newspaper:** Usually for **office** and **manual** workers. These people are plenty since the job does not require too much skill.
- **National newspaper:** Used to find workers for **senior positions** that requires a lot of skills. It can be read by people anywhere in the country or overseas.
- **Specialist magazines:** Used for particular **technical specialists** such as physicists. Can be used to hire people in the home country or abroad.
- **Recruitment agencies:** Keeps details of qualified people, and will send the suitable applicants to interviews when a business asks for a worker. Many businesses prefer to use recruitment agencies to find them workers because it is easier. However, it is expensive since their fee is based on a **percentage** of the workers **pay**.
- **Government job centres:** Place where businesses can **advertise** their vacancies. These vacancies are usually for **unskilled** or **semi-skilled** workers.

Possible effects of government legislation on the recruitment process

Many governments pass laws to create equal **employee opportunities**. They state that all employees should be treated **equally** in the work place and receive the **same salary** for doing the same job. People of any sex and people with disabilities are treated equally. Therefore, businesses need to be careful when **advertising** and **treating** their employees because they could be **prosecuted** and **fined**.

Job advertisement

This is what a business needs to decide when drawing up an advertisement:

- **What** should be included?
  - Job description
  - Job specification
- **Where** the ad will be placed.
  - (depends on job)

- Advertising **budget**.
    - (depends on job)

Applications forms and CVs/résumés

When a person applies for a job, he will have to fill out an **application form**, or write an **application letter** with a **CV** enclosed. **CVs** are descriptions about one's qualifications and skills in a set **format**.

Businesses will use application forms and CVs to see whether an applicant match the **job specifications** or not. The closest matching applicants are invited to **interviews** in the **selection stage**. A **short-list** is drawn up.

These are what CVs should contain:

- Name
- Address
- Telephone Number
- Date of Birth
- Nationality
- Education and qualifications
- Work experience
- Positions of responsibility
- Interests
- Names and addresses of **references**.

The letter of application should contain briefly:

- Why the applicant wants the job.
- Why the applicant feels he/she would be suitable.

Applicant forms ask for the same information as the application letter and CV, but may ask for other types of information.

Interviews

Applicants who are invited to interviews will have provided the names and addresses of their **references**. These people can give their opinions on the reliability, honesty and skills of the applicants and they will be likely to tell the truth because the applicants will not know what they have said.

Interviews are the most popular form of **selection**. However, interviews are not always the most reliable process of selection. They aim to find out these things:

- The applicant's ability to do the job.
- Personal qualities that are advantageous and disadvantageous.
- General characteristics – whether they can "fit in"?

These are the likely questions in an interview:

- Why have you applied for the job?
- What do you know about this company?
- What qualities do you have to offer the company?
- What ambitions do you have?
- What are your hobbies and interests?
- Do you have any questions to ask us?

Interviews can be one-to-one, two-to-one, or a **panel** of people to interview people which is used to select people for important jobs. Some businesses include tests in their selection.

- **Skill tests:** To test the skills of the candidates.
- **Aptitude tests:** To test how easily candidates can be trained/learn new things.
- **Personality tests:** To test for people who have specific personal qualities which will fit into jobs – e.g. that has a lot of stress; requires you to work with a team.
- **Group situation tests:** To test how well applicants work with other people.

Rejecting unsuccessful applicants

When applicants fail to get the job, they should be informed and thanked for applying.

Training

Training is often needed to do achieve the needs listed below. These needs can be long-term or short-term.

- Introduce a **new process** or **equipment**.

- **Improve efficiency**.
- **Decrease supervision** needed.
- **Improve** the opportunity for **internal promotion**.
- **Decrease** the chance of **accidents**

Employees should know the benefits of training for them to take it seriously. Here are some **objectives** of training:

- Increase **skills**.

- Increase **knowledge**.
- Change **attitude**, raise **awareness**.

There are three main types of training:

- **Induction training:**
    - Introducing a **new employee** to their business/management/co-workers/facilities.

    - Lasts **one** to **several days**.
- **On-the-job training:**
    - Employees are trained by **watching professionals** do a job.
    - Only suitable for **unskilled** and **semi-skilled** jobs.
    - Cuts **travel costs**.
    - The trainee may **do some work**.
    - The trainer's **productiveness** is **decreased** because he has to show things to the trainee.
    - The trainer's **bad habits** can be passed to the trainee.

- **Off-the-job training:**
    - Workers go to another place for training (e.g. school).
    - Methods are **varied** and usually more **complex**.
    - Usually **classroom training**.
    - Employees still **work** during the day.
    - Employees can learn **many skills**.

Workforce planning

A business will need to forecast the **type** and **number** of employees needed in the future. This depends on the firm's growth and objectives. The forecast can be done by:

- Finding out the **skills** of all current employees.
- Counting out people who are **leaving** soon (e.g. retirement).
- Talk to staff about who would want to **retrain** for new jobs.
- Provide a **recruitment plan**. (how many new staff are needed, and how they should be recruited, internal or external)

Dismissal and Redundancy

There are some situations when businesses need to reduce the number of employees they have. This can be done in two ways:

- **Dismissal:**
    - A worker is **fired** for **unsatisfactory work** or **behaviour**.
    - **Fault** of the employee.
- **Redundancy:**
    - Employees are **no longer needed**.
    - **Not** the **fault** of the employee.
    - Some **reasons** are:
        - A business is **closing down** a factory.
        - A business wants to **cut costs** by reducing the number of employees.
        - A business has merged/taken over another and there are too many staff in certain departments.
        - New machinery replaces workers.

- Employees are given some **money** to compensate for their lost job.
    - The money is often negotiated with **trade unions**.
    - Some government have **laws** that makes businesses pay for their workers this way.
- If only some employees are to be made redundant, trade unions will agree with the **fairest** way to see who goes. These terms are negotiated with the **HR department**.
    - Sometimes there will be **voluntary redundancy** by members.
        - **Older** workers.
        - There may be some who wants to leave because they have **other ideas**.

Chapter 15: Employee and employer associations

In smaller businesses, if employees have any problems they can **talk directly** to their employer. However, in larger businesses that employs many people, it becomes extremely hard to do so. It is also hard for the Human Resources department to make decisions when they have about 500 employees (e.g. who will get a pay rise?). It becomes much easier if decisions are negotiated with a **trade union**, and employee association that represents them. This saves the management a lot of time because they do not have to see individual employees to discuss problems.

Employees might not be treated fairly at work. They may be **overworked** and **underpaid**. Trade unions has the role of **bargaining** with the HR department for better working conditions, conditions of employment and better pay.

Trade Unions

Employees with similar interests (higher pay) form a trade union. Trade unions are a form of **pressure group** with has the ability to influence business activity. There are four main types of trade unions:

- **Craft union:** For workers **skilled** at a particular job.
- **General union:** For **unskilled** and **semi-skilled** workers from different industries.
- **Industrial union:** For all types of workers in an **industry**.
- **White-collar union:** For **non-manual** or **office** workers.

Why do workers join a trade union?

Unions have a **shop steward**, who is an **unpaid** representative of the union. When someone is new to a job they may ask if they may want to join. If the person joins, they will have to pay an **annual subscription**. This money will be use for employing **union officials** who will represent the views of the employees.

Advantages of a union

- **Strength** in **numbers**.

- Improved **conditions of employment**.
- Improved **working conditions**.
- Improved **sickness benefits**, **pensions**, and **retrenchment benefits**.
- Improved **job satisfaction** and encourage **training**.
- **Advice/Financial support** if a worker is **dismissed unfairly/made redundant** or is asked to do something not part of their job.
- Improved **fringe benefits**.
- **Employment** where there is a **closed shop**, which is when all employees in a business must belong to the **same** union.

Trade unions need to:

- Put forward their views in the **media** to influence **government decisions** on pay, employment, etc…

- Improve **communications** between workers and managers.

Closed shop

A **closed shop** is when all employees must join one union in order to be employed. It is because its **members** feel that the union is doing nothing when non-members receive the same pay rises as them. They think it is unfair. Trade unions also gain greater strength if all the employees are members of the union. However, many people think that it is unfair since they are **forced** to join – they should be able to make their **own decisions**.

Single union agreement

Some companies have a **single union agreement**, when a business only agrees to deal with a single union. Any employees who want to join a union can join this union. It is becoming more popular nowadays because many employees are becoming **multi-skilled**, and do not know which union to join.

Advantages to the employee:

- **Discussions** are **clearer** if there is only one union to deal with.
- The union has **greater power**.
- **No disagreements** between different unions.
- A better **working relationship** should develop between the union and the management.
- **Disputes** are solved more quickly.

Advantages to the employer:

- **Discussions** are **clearer**.
- A better **working relationship** should develop, meaning that there would be less **industrial disputes**, benefiting both employees and employers.
- **Disputes** are solved more quickly.
- It is easier to agree to **changes**.

The structure of a trade union

The structure of different unions vary, but most elect a **President** or **General Secretary** to work **full-time** for and get **paid** by the union. They work at the union's **headquarters**. If the union is large, there will be **union officials** to take cared of members in different branches. Each **branch** represents its members in one **work site**, one factory, or one **employer**. Each branch has a **representative**. Unions are usually **democratic** and their union officers are voted up by the members.

Employer associations

Employers join what are called **employer associations/employer federations/trade associations**. Like trade unions, employer associations are made up of businesses and employers and who all pay annual fees for their benefits.

Advantages of joining an employer association:

- They **negotiate** with trade unions on behalf of their members.
- They give advice on **employment laws**, **health and safety**, **taxation laws** etc…
- Strength in numbers, they want to **influence government decisions**.
- They can **share ideas** and **research facilities**.
- They can organise **bulk buying** for members and get **discounts**.

Employer associations and the government.

Employer associations represent similar wants of businesses, and will try to influence the governments to give better conditions for businesses to prosper:

- They want the government to control things such as **inflation, law and order, health and safety,** and **education** for the workforce.
- Lower **taxes**.
- More **freedom** for **businesses**.
- Fair **competition**.
- Good **transport infrastructure**.
- Access to **overseas markets**.
- Reliable source of **power**.

Collective bargaining

This is when **representatives** of different interest groups negotiate and a **collective agreement** is made. The bargaining can be with **businesses** or with the **government**. **Collective bargaining** in businesses usually means that the representatives of one or more trade unions negotiate with one or more employers or employer associations to come up with a **mutually acceptable agreement** on **conditions of employment**.

Why trade unions want wage increases:

- **Inflation**.
- It is difficult to recruit **qualified workers** (so pay them more!).
- Pay **differentials** need to be maintained (everybody's wages should rise when the minimum wage rises).
- **Changes** in the workplace, e.g. new machinery.
- If there are increased **productivity**, wages should **increase** too. There are **productivity agreements**, when managers and trade unions agree to raise prices for increased productivity.

Often agreements take place and the **"middle path"** is taken. However, this does not always happen and if the workers and unsatisfied with the agreements, they will use **industrial action**.

Industrial action

There are various forms of industrial action that try to influence the decisions of employers. Here are some of their most comment forms.

Strikes

Strikes are when workers stop working and leave the workplace to protest against things.

- **Token strike:** Stoppage for an hour, a few hours or half a day to show strong feelings.
- **Selective strike:** Only a few workers go on strike. They are chosen by the union to cause as much **disruption** as possible.
- **All out strike:** All union members stop working and wait until a dispute has been settled.

Unions have to pay their members out of **strike funds** as long as the strike has been approved by the union. All members **vote** to see if the strike is favourable or not.

Picketing

This is when workers **stand outside** the factory holding **signs** to **protest** and **stop** any **people going in** and **out** as well as **goods**. This can halt the production process. The strikers gain **publicity** and gives the firm a **bad image**. This puts **pressure** on the firm to settle the dispute.

Work to rule

This is when workers **stick rigidly** to every **rule** and regulation in the business so that it **slows down** the **production process**. They still get **paid** since they are technically doing nothing wrong, but this still causes a lot of **disruption** in the workplace.

Go slow

All workers deliberately do things very slowly.

Non-cooperative

Workers refuse to work with any **new** rules or follow any new practices they do not approve of.

Overtime ban

Workers refuse to do any **overtime**. This might damage the business if they need to complete some orders quickly.

Possible harmful consequences of industrial action:

- **For employers:**
  - Loss of output.
  - Loss of profit.
  - Loss of customers.
  - Poor reputation.

    - Bad image.
- **For employees:**
    - Loss of wages.
    - They might lose their jobs if the company suffers low profits.
- **For customers:**
    - They need to find another supplier which might cost more (production is stopped)
    - Shortage of products.
    - Deliveries not made.
    - For other businesses:
        - May lose income.
        - May not have materials to produce goods.
- **For the economy:**
    - Workers have less money to spend.
    - Less tax revenue.
    - Country gain bad reputation for late deliveries.
    - Workers may be made redundant.
    - Exports may be lost and imports increased.

Employer's powers

However, employers can do something about the situation. Usually, they will sign a **no-strike agreement** with the union which also involves **pay rises**. The pay rises are determined by an **arbitrator**, an independent person who represents both sides and decides on the best decisions possible. Again, he will most likely choose the **"middle path"**.

Nevertheless, if strikes do happen, here are some things employers can do:

- **Dismiss all workers:** This leave the company in a very terrible position since they can't produce goods or deliver goods.

- **Lock-out the workers:** Stop workers from coming to work or get paid. Used to counter work to rule and go slow strategies.
- **Institute a pay freeze:** Used if employees are refusing to follow new rules, practices or operate new machinery.

Worker participation:

The management needs to let everyone feel that they are part of the business. This means that managers will let **workers participate** in business decisions. There are several ways of doing this:

- **Worker directors:** Some workers become directors, but they are not allowed to attend all board meetings.
- **Works councils:** These are where representatives of employees get together and discuss matters that affect employees with managers. Works councils are called European committees in Europe, and are becoming more common there. Multinationals with more than 1000 workers or 100 workers per branch will have to create a works council and will have to always consult it when making decisions affecting employees.
- **Quality circles:** This is often used in Japanese companies, where workers regularly debate on how to improve quality and efficiency.
- **Using a democratic style of leadership:** Workers are delegated tasks and are consulted in business decisions.

Advantages of worker participation

- It increases the flow of **information** and improve **relationships** between the employer and the employee.
- It increases **motivation**.
- It increases **job satisfaction**.
- It benefits the company since it can use **knowledge** from **experienced** workers.

Disadvantages of worker participation

- It is **time consuming**.
- Workers may **lack necessary technical knowledge**.
- If representation is done via **trade unions**, non union members won't be affected.
- There could be **conflict of interests**.

Sir Talha Siddiqui
03133106254

Chapter 16: The market and marketing

What is marketing?

A **market** is where **buyers** and **sellers** come together and **exchange** their **products** for **money**. It can be in the streets, on the internet, in shops around the world, etc… Customers and sellers exchange both **goods** and **services** for money.

Product-orientated and market-orientated businesses

A **product orientated** business focuses on the quality and price of the product before finding a **market** for it to sell in. These type of businesses usually produce **basic needs**. **New technology** could be developed this way, and customer **wants** are created by **advertising**.

Other big companies cannot afford to produce a product that will not sell, so they have to do **market research** first to find consumer wants **before** developing a product. They are called **market-orientated** businesses. They will need to set up a **marketing budget** for this, which is a **financial plan** for marketing of a product, which contains the amount of money the Marketing department may spend on marketing.

What is marketing

Marketing is the **management process** which identifies consumer **wants**, predict **future** wants, **create** wants and find ways to **use** these wants to the fullest (most profitably). In other words, businesses try to **satisfy** wants in the most **profitable** way possible. Marketing covers a wide range of activities such as: advertising, packaging, promotion, etc…

The Marketing department

Most businesses will have a **Marketing department**, which will have a **Marketing Director**. He will be in charge of things such as R&D, distribution and pricing. Here is an organisational chart showing what departments the marketing director controls:

- **Sales department:** Responsible for sale and distribution of products for each **region**. There may also be an **export department**.

- **Research and Development department:** Responsible for finding out consumer wants and **developing new products**. They also need to find ways to **improve** an existing product.
- **Promotion department:** In charge of advertising and promotion. It will need a **marketing budget** which limits the amount of money it can spend.
- **Distribution department:** It transports products to their markets.

The objectives of marketing

A successful Marketing department should be able to achieve these objectives for the business:

- To increase **sales revenue** and **profitability**.

- To increase **market share** (percentage of sales a product has in a market).
- To maintain or improve **image** of a product or company.
- To target a **new market** or **market segment**.
- To develop **new products** or **improve** existing ones.

SWOT analysis

This is a method to evaluate the statistics of a product of business. It assess these things:

- **Strengths** (internal)

- **Weaknesses** (internal)
- **Opportunities** (external)
- **Threats** (external)

Strengths and weaknesses of a product are its **internal factors**, while opportunities and threats are **external factors**.

Market segments

Market segments are parts of a market which contains people which have similar **preferences** for their products. The Marketing department should know which segment their product fits the most, so that they can advertise and sell their products to it.

There are two ways to **segment** markets. By the **type of product** or the attributes of the **customers** buying it. Here are two types of markets which are segmented based on the product:

- **Mass market:** Where there is a **large** number of sales of a product. (e.g. Pepsi can be bought anywhere)
- **Niche market:** A **small** market for **specialised** products. (e.g. Ferrari cars)

Here is how a market can be segmented regarding people buying the product:

- **Income**
- **Age**
- **Region**
- **Gender**
- **Use of product**
- **Lifestyle**

It is very important to **target** the right market segment since it can **increase sales** by a lot. If a business can analyse all of these market segments, they may find a market segment whose **needs** are **not** being **met**. This is when the business finds a **gap in the market**, and it could produce goods to take advantage of this gap and again increase sales.

The marketing mix

The **marketing mix** is a term that describes how products are **marketed**. You must remember that before marketing can be achieved, **market research** is needed. The rest is summarized into the **four P's**. Let's look at them briefly first, since they will be covered in other chapters:

- **Product:** Design and quality, competitiveness, **packaging**, etc…
- **Price:** There are different pricing strategies. Businesses need to use them so that they increase sales.

- **Promotion:** Advertising and promotion. Discounts, TV adverts, sales, **packaging**, etc…
- **Place:** The location of the **point of sale** (the shop). **Channels of distribution**. Type of shop (wholesaler or retailer?)

A successful product require effective use of the four P's. However, businesses must be careful to not let each of these factors **counteract each other** (e.g. expensive but low quality goods), else the product will fail.

Chapter 17: Market research

Why is market research needed?

Any business should find out what people want to buy and how many people are going to buy that product before producing a product since the chances of failing are very high. Usually, **market research** try to answer these questions:

- What **feature** of the product do they **like/dislike**?
- Are people **willing** to buy the product?
- What **price** are people prepared to pay?
- **Location** of the selling point of the product.
- Type of **customer** who buys the product.
- Type of **promotion** that will be **effective**.
- **Competition** in the same industry.

Businesses need to know these things as well as **consumer wants** to be more competitive. There are **two** main **types** of **information** that can be gathered from market research:

- **Qualitative information:** information where **opinion** or **judgement** is necessary.
- **Quantitative information:** information about the **quantity** of something.

There are two ways to gather any information for market research:

- **Primary research** or **field research.**
- **Secondary research** or **desk research**.

Primary research

Primary research is gathering **original data** which may require **direct contact** with customers. There are several ways to do primary research:

- **Questionnaires**
- **Interviews**
- **Consumer panels**
- **Observation**
- **Experiments**

Note: Questionnaires, interviews and consumer panels are all types of **surveys**.

The process of primary research

1. Identify the **purpose** of the market research.
2. Decide on the best **method of research**. (primary, secondary or both)
3. Decide on the **size** and **type** of **sample** (group of people who will be asked)
4. **Carry out** the research.
5. **Collate data** and **analyse** results.
6. Produce a **report**. (may include recommendations of action paths to take)

Methods of primary research

<u>Questionnaires</u>

Questionnaires involve asking people questions. Deciding **what questions** to ask since sometimes questions may **mislead** people and make them answer what they don't really think.

Advantages:

- **Detailed qualitative** information can be gathered.
- Customers' **opinions** can be gathered.

Disadvantages:

- If the **questions** are bad it could **mislead** customers.
- Takes **time** and **money** to collate the results.

Interviews

Interviews are face-to-face **conversations** with customers where the interviewer has a set of **prepared questions**.

Advantages:

- The interviewer can **explain** any questions the interviewee does not **understand**.
- **Detailed** information about customers' **opinions**.

Disadvantages:

- **Interviewer bias**. The interviewer might unconsciously lead the interviewee to answer in a certain way.
- **Time consuming** and **expensive**.

Samples

A **group** of people who are chosen to do market research on. There could be:

- **Random sample:** A random number of people are selected.
- **Quota sample:** People are selected for some certain **characteristics**.

Consumer panels

Consumer panels are groups of people who agree to provide **information** and **spending patterns** about a product. They may even **test** it and give feedback on likes and dislikes.

Advantages:

- They provide **detailed information** about a product.

Disadvantages:

- They can be **time consuming**, **expensive**, and **biased** if opinions of some is influenced by others.

<u>Observation</u>

Observation involves:

- **Recording:** e.g. meters can be fitted to a monitor to see what people are watching.
- **Watching:** e.g. see how many people go into a shop and actually buy something.
- **Audits:** e.g. counting inventory to see what has sold well. (inspecting)

Advantages:

- It is **inexpensive**.

Disadvantages:

- Only provide **basic figures** and not **reasons** why people do things.

<u>Experiments</u>

Experimenting involves giving products to consumers to see what they think about it.

Advantages:

- **Easy** to **set up**, **carry out**, and gather consumer **opinions**.

Disadvantages:

- People might give **wrong feelings** to avoid **offence**.
- **Representatives** of **samples** may not be asked, just people who shop in an area.
- Many **potential customers** may not be asked.

Secondary research

Secondary research means taking information that has been already collected by others.

Internal sources of information

Data collected from past researches could easily be used again if it is needed. Examples of internal sources of information include:

- **Sales department**: sales records, pricing data, customer records, sales records.
- **Distribution** and **PR personnel**.
- **Finance department**.
- **Customer service department**.

External sources of information

Data collected from sources **outside** the business. The data may still be useful but there are many **limitations** since it has been gathered for other purposes. Sources include:

- **Internet**: gives all sorts of information, but the info must be validated.
- **Trade** and **employer associations**: gives info about things in an industry.
- **Specialist journals**.

- **Research reports**.
- **Newspapers**: about the economy and disposable income of workers.
- **Government reports** and **statistics**: contains things such as age groups and culture.
- **Media reports**.
- **Market research agencies' reports**: detailed reports on the economy. Expensive to buy.

Secondary research is often a much **cheaper** way of obtaining information. It also gains access to data which cannot be gathered by primary research such as **government issues** or the economy.

Who carries out market research?

Normally, research is done by any business who needs it. In smaller businesses, owners use secondary research since they cannot afford to conduct primary research. However, if a business has enough money, it can afford to have a **specialist market research agency** to do the research for it.

Accuracy of market research information

The accuracy of market research depends on **how the research was conducted** and **how carefully samples have been selected**. Here are some ways to make information from market research more accurate:

- A **sample** needs to be truly **representative** of the total population, hence a **quota sample** is normally used.
- The **larger** the sample, the more accurate the results.
- Questionnaires need to be **tested** on a small group of people to see if there are **misinterpretations**. The questionnaires will be **modified** to be as clear as possible.

Concerning secondary research, there are a few problems with it:

- Data collected by others may not be accurate since it was used for other **purposes**.
- Data can be **out of date**.

All in all, it must never be assumed that information collected from market research is completely correct.

How to design and use a questionnaire

Firstly, you need to ask yourself some questions:

- **What** do I need to find out?
- **Who** do I need to ask?
- **Where** will I carry out my questionnaire?

Writing the questions

- Ask **no more** than **12** questions. (impatience)
- Make the questions **simple**. The answers should be **simple enough** to **collate**. (e.g. Yes/No answers)
- Use choice of **age groups**.
- **Avoid open-ended** questions.
- **Avoid misleading** the interviewee with questions. (don't want to cause offence)
- The **order** of the questions should be **logical**.

Carrying out the questionnaire

First you need to figure out:

- **How** you will **ask** the questions.
- **How** you will **collate** the results.

Then:

- **Where** are you going to ask the questions.
- **Who** are you going to ask?

And finally:

- **How many** people will be asked?
- **When** will you ask the questions? (time)

Analysing questionnaires

Analysing the results should be straightforward if you have easily collated the data. It simply involves reading the answers and thinking about what they mean. It takes practice.

Chapter 18: Presentation of information

Presentation of data from market research

Presentation of data is important because it **converts** raw data into a form that is easier to **understand**. Information can be displayed as:

Table/tally chart:
It is the most suitable method of presenting data when **raw data** is needed. However, it offers little more than that and the information should be converted into other forms if it needs to be understood or analysed carefully. It is sufficient for info that is brief or does not contain a lot of different things.

Bar chart:
Charts are a more **meaningful** and **attractive** way to present data. They are normally used to **compare** two or more sets of stats with each other.

Pictogram:
It is similar to a bar chart but uses **symbols** instead of columns. It becomes extremely effective if the data is short and simple.

Pie chart:
Pie charts are ways to show the **proportion** that each components take up compared to the **total figure**.

Line graph:
Graphs show the **relationship** between **two variables**. It can be drawn in a straight or curved line. It is usually to compare things with **time** and to identify **trends**.

Alternative ways of presenting information for coursework

Tables

Tables could be also be used to present data in situations such as when people are interviewed on why they like a product and they are given **multiple choices**.

Photographs

Photos can be used to help **illustrate** your points or **support** your work. However, **avoid** adding them to your work just to make them more **attractive**.

Diagrams

Diagrams are used to **simplify** information. It can be used to show **relationships** of things which all leads to the same **root**, which is usually at the centre of the diagram. It can also be used to show **variation**, e.g. diagram for ways to save water with different ways to do so branching out from the centre of the diagram.

Maps

Maps are usually used to present **location** or **transport routes**, etc… They aim to make the information as **clear** as possible to the reader. This of course, only applies to certain types of information where words and numbers cannot express them.

Chapter 19: The marketing mix: product and packaging

The role of product in the marketing mix

The **product** itself is the most important element in the marketing mix. Without it, the other three wouldn't exist. Most companies today are market oriented, and will identify a suitable product for the market before moving on to determine the other 3 elements. Large companies have **R&D** departments which spends all its time developing new product and analysing the pros and cons of competitors' products.

Types of products:

- **Consumer goods:** Goods that are used up by consumers. (e.g. food, cake)
- **Consumer services:** Services that are produced for people. (e.g. education)
- **Producer goods:** Goods produced for businesses. (e.g. machinery)
- **Producer services:** Services for businesses. (e.g. accounting, insurance)

Each type of product **determines** the price, promotion and place to sell the product. Here are what make products successful.

- Products need to **satisfy** consumer **wants/needs** to be successful.
- The product must be at the right **quality** so that customers are willing to pay for it.
- Costs should be low enough to make a **profit**.
- **Design** of a product is important. This means that its **quality** and **durability** should meet expectations and match the **price** of the product. The design should also enhance the products **brand image**.
- Products are **novelties** (newly introduced to the market).
- Products can **stimulate new wants**.

Product development

Most businesses use a general process to develop any product:

1. **Generate ideas:** Ideas can be generated by:
    1. Employees.
    2. Customers.
    3. Competitor's products.
    4. R&D department.
    5. Sales department.
2. **Further research:** The best ideas are selected and further research is done to see their pros and cons.
3. **Will there be enough sales?:** To see whether there will be enough sales of the product to break-even (development costs included).
4. **Develop a prototype:** To see how a product could be manufactured and identify its problems.
5. **Test launch:** To see if the product can sell or not.
6. **Full launch.**

The importance of branding

Traditionally, a product's unique features and quality were explained by the sellers who made the product. However, since products are usually sold in private retail shops nowadays, these points need to be projected differently. Products therefore need to be **branded** with an **unique brand name** and the products features and quality will be projected with advertisement. The price of branded goods are usually higher, since customers are more confident to buy them. Here are things that are involved with branding:

- **Unique** name.
- **Unique packaging**.
- Needs **advertising** to enforce the brand's qualities.
- **Higher price** than unbranded products.
- **Higher quality** than unbranded products.
- Creates a **brand image** (**unique** image associated with using the product)
- Creates **brand loyalty**.
- **Consistent quality**.

Packaging

Getting the packaging right is very important. Packaging performs several tasks:

- **Protecting** the product (also includes preserving foods)

- Making it **easy** to **transport**.
- Allow the product to be **used easily**. Container must be able to be **opened easily**. (e.g. juice in a can)
- Suitable for the product to **fit in**.

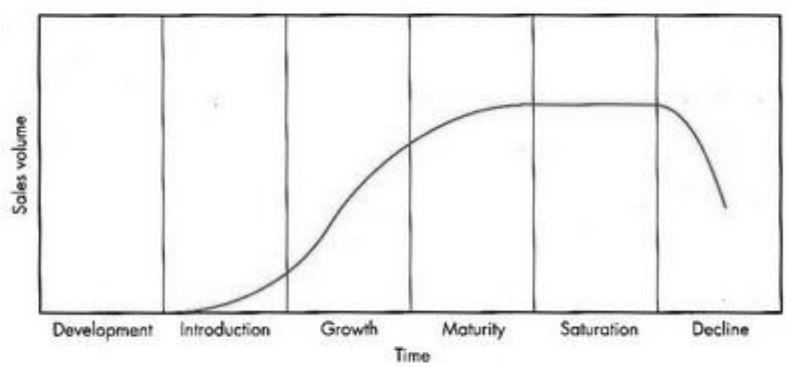
Packaging also helps **promote** the product:

- Make it **eye-catching**.

- Carries **information** about the product.
- **Promotes** the **brand image**.

The product life cycle

Product life cycles show the stages that a product goes through from its introduction, to its growth, and then to its decline. Here is a graph to show the product life cycle:



1. **Development:** The product is under development.

2. **Introduction:** The product is introduced. Sales grow slowly and **informative** advertising start to attract customers. Price skimming could be used if the product is new to the market. The main aim of sales is to breakeven.
3. **Growth:** Prices rise rapidly. **Persuasive** advertising is used to encourage brand loyalty. Prices may be reduced a little. Sales start to generate profits since costs have been covered.
4. **Maturity:** Sales rise more slowly. Competition forces prices to be lowered and the firm uses competitive pricing. Advertising is used to maintain sales. Profits are at their **highest**.

5. **Saturation:** Sales reach their **limit**. There are no new competitors. Sales and advertising becomes stable but profits fall because of lowered prices to be competitive.
6. **Decline:** Product go out of fashion and sales and profits decline. Advertising eventually stops. It is no longer profitable to product the product.

The length of each stage varies with products. The business needs to identify which stage their products are in so that they can use a suitable marketing strategy for it.

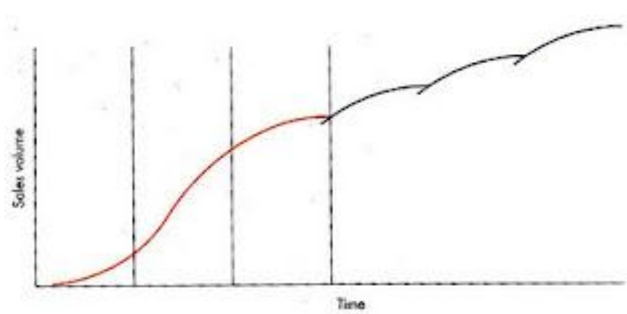
Extending the product life cycle

When a product has reached its maturity or saturation stage a business may adopt **extension strategies** to stop sales from falling which **extends** the product life cycle. Sales are given a **boost** by these strategies.

- Introducing **new variations** of the product.

- Sell into **new markets**.
- Make small **changes** to the products **design** and **packaging**.
- Sell through **additional**, **different** retail outlets.
- **Update** the product (make it better)
- Use a new **advertising campaign**.

Extension strategies aim to prolong the **maturity** stage of a product. Successful extension strategies may result in something like this:



Nevertheless, it must be noted that businesses manufacture more than one product. They should have a product in **growth** stage to **counteract** an older one which is declining.

Chapter 20: The marketing mix: price

The role of price in the marketing mix

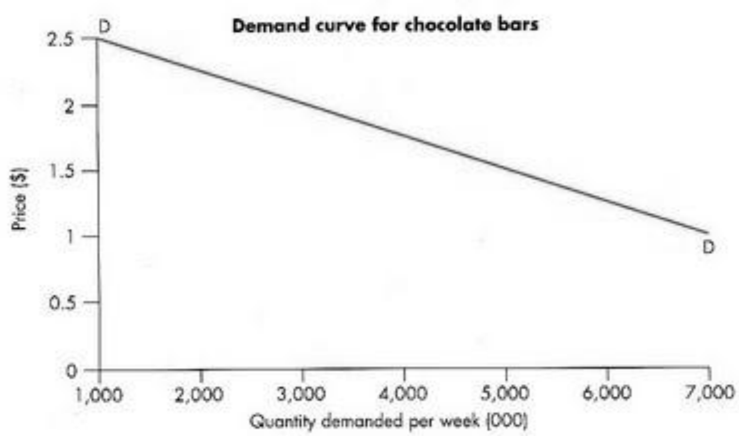
When pricing a product, a business needs to choose one that fits with the rest of the elements in the marketing mix. E.g. high price so that consumers thinks they are buying high quality goods, low price for low quality goods, or competitive prices in a market with a lot of competition.

Price determination in a free market

People think that prices are determined by the seller of the product, but that is not quite so. Prices are driven by market forces called **demand** and **supply**.

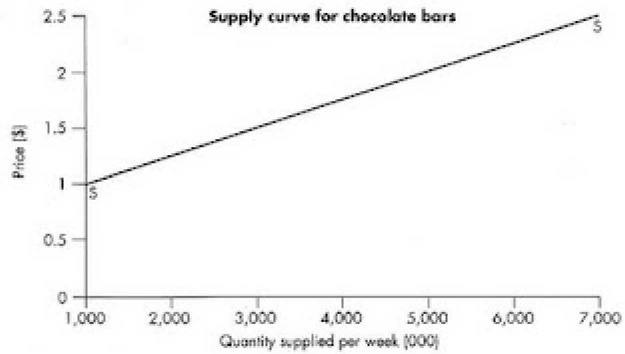
Demand

Demand is not only that people want to buy a product, but that they want it can are **willing to pay** for it. Prices can affect how much demand there is for a product. Normally, if the **price** goes **up**, **demand** goes **down**, and vice versa. This can be shown on the graph below:



Supply

Supply also varies with price. However, it is different. If the **price** goes **up**, then the owners would want to be supplied with more products to take advantage of the high price, thus the **supply** goes **up** (and vice versa). This can be demonstrated on the graph below:



The market price

For the market price to be determined, demand and supply must all be put onto the same graph. The place where the two lines (called **curves**) cross is called the **equilibrium**, where the same number of goods are demanded and in supply resulting in **no leftovers**. All the products are demanded and all of them are sold.

Factors that affect demand and supply

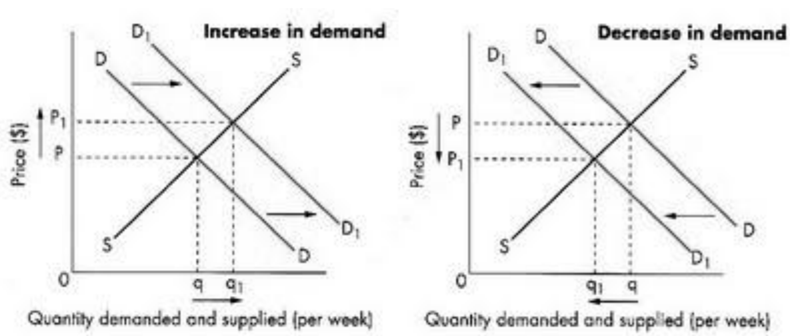
The graphs above assume that the demand and supply of goods are fixed. But these things can change, which moves the demand or supply curve to the left or the right in the graph. Changes in the **price** affects where you are on the **curves**. But changes in **other factors** affect the **position** of the **curve** on the graph.

Factors affecting demand

- The popularity of **substitute products**. (products that can be used **instead of** the product)

- The popularity of **complementary products**. (products that require each other or are **used together**)
- Changes in **income**.
- Changes in **taste** and **fashion**.
- Changes in **advertising**.

The result is: if demand **falls**, the **market price** and **sales** will **fall**, and the demand curve will move to the **left**. If demand **rises**, the **market price** and **sales** will **rise**, and the demand curve will move to the **right**. It is illustrated on the graphs below.



Elasticity of demand

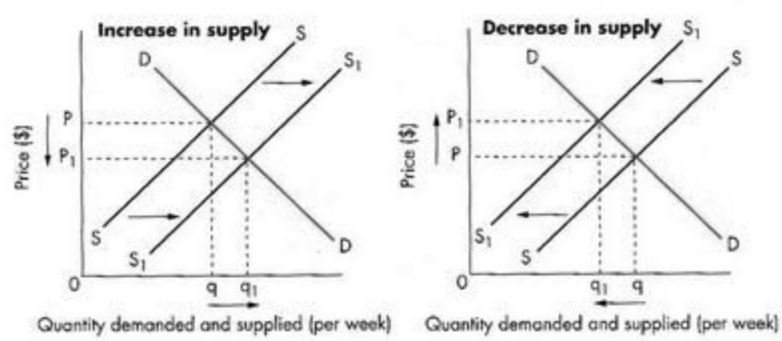
Elasticity of demand is how **easily** demand can **change** when **prices change**. A product with an **elastic demand curve** would have a **higher change in demand** than a **change in price** (uses percentages). A product with an **inelastic demand curve** would have a **lower change in demand** than a **change in price**. The elasticity of demand of a product is mainly affected by **how many substitute** products that it has.

Factors affecting supply

- **Costs in supplying goods to the market:**
    - Price of raw materials.
    - Wage rates.
- **Improvements in technology:**
    - Makes it cheaper to produce goods.
- **Taxes and subsidies:**
    - Higher taxes mean higher costs.

- **Climate (for agricultural products):**
    - Supply of crops depend on weather.

The result is: if supply **falls**, the **market price** will **rise**, **sales** will **fall** and the supply curve will move to the **left**. If supply **rises**, the **market price** will **fall**, **sales** will **rise** and the demand curve will move to the **right**. It is illustrated on the graphs below.



Elasticity of supply
Elasticity of supply is how **easily** and **quickly** supply can **change** when **prices change**. How **quickly** means how quickly products can be produced and supplied, which is not very quick for products made by agriculture. A product with an **elastic supply curve** would have a **higher % change in supply** than a **change in price**. A product with an **inelastic supply curve** would have a **lower change in supply** than a **change in price**.

Pricing strategies

If a product is easily recognizable from other products, it would probably have a **brand name**. And if it has one, it would need a suitable **pricing strategy** to **complement** the brand name that should improve its **brand image**. Here are the strategies that are used:

Cost-plus pricing
Cost-plus pricing involves **covering all costs** and adding a percentage **mark-up** for profit.

- + **Easy** to apply.
- - You **lose** sales if your price is **higher** than your competitors price.

Penetration pricing

Penetration pricing is used to **enter** a **new market**. It should be lower than competitors' prices.

- + Ensures that **sales** are **made** when a product enters a market.
- - Prices will be low. Sales revenue will be **low**.

Pricing skimming

High prices are used when a **new product** is introduced into a market, partly because it has a **novelty factor**, and because of the high **development costs**. High prices could be charged because a product is **high quality**. One last use of it is to **improve** the **brand image** of a product, since people usually associate high price with good products.

- + Skimming can help **establish** a product as being **good quality**.
- - It may **lose potential customers** because of high price.

Competitive pricing

Competitive pricing means setting your price to a **similar** or **lower level** than your **competitors prices**.

- + Sales will be high because your price is at a **realistic level** (not under/over-priced).
- - You have to **research** on your competitors prices which costs **time** and **money**.

Promotional pricing

Promotional pricing means that you **lower** the prices of goods for a short time.

- + Help **get rid** of **unwanted** stock.
- + Can **renew interest** in a product.
- - Sales revenue will be **lower**.

Psychological pricing

Psychological pricing involves setting the price that **changes consumers perception** of a product. This may be by:

- Using high price to make using the product give the user a **status symbol**.
- Pricing a product at just below a **whole number** (e.g. $99) which gives it an **impression** that it is **cheaper**.
- Supermarkets charge low prices for products that are bought on a **daily basis** to give consumers an **impression** that they are being given **good value for money**.

Chapter 21: The marketing mix: promotion

The role of promotion in the marketing mix

Promotion **informs** consumers about the rest of the marketing mix. Without it, consumers do not know about the product, the price, or the place. Promotion is more than just advertising, and it includes several activities. It is crucial when you are selling in a mass market or you have a brand name. Promotion includes:

- **Advertisements:** They can take different forms, e.g. on TV, in newspapers.
- **Promotion:** e.g. Money off coupons.
- **Personal selling:** Sending out sales representatives to talk directly to the consumers.
- **Public relations:** Involves making the public aware of the company, e.g. creating publicity in the media.

The aims of promotion

- To inform people about particular issues.
- To introduce new products to the market.
- To compete with competitors products.
- To improve the company/brand image.
- To increase sales.

Advertising

The advertising process

1. **Set objectives**: A business needs to determine the purpose of advertising.
2. **Decide the**

advertising budget: Set a limit on how much the business can spend on advertising. It can be decided based on:
   1. A percentage of predicted sales revenue.
   2. How much competitors are spending.
   3. How much the business can afford.
3. **Create an advertising campaign**: Decide on what advertising campaign to run. Can be determined based on:
   1. Target audience.
   2. Objectives.
4. **Select the media**: Using the suitable media for advertising that is the most **cost effective**. E.g. TV, newspaper.
5. **Evaluate the effectiveness of the campaign**: Has the advertising met objectives?

Different types of advertising

- **Informative advertising**: Involves giving as much information about the product as possible. (e.g. computer)

- **Persuasive advertising**: Involves persuading consumers that they **need** the product and should buy it. (e.g. perfume)

Different media of advertising

Media	Advantages	Disadvantages	Examples
Television	Millions of people will see it. The product can be presented in a very attractive way. Easy to reach target audiences.	Expensive	Food Cars Household tools
Radio	Cheaper than TV. Uses song or tune which makes ads memorable.	Cannot use visual message. Expensive compared to others. The advert has to be remembered. Not as wide audience as	Local services Shops

		TV	
Newspaper	Can reach many people. Cheap for local newspapers. A lot of info can be put into the ad. Adverts are permanent*.	Not eye-catching if they are in black and white. Does not grab reader's attention.	Local products Cars Banks
Magazines	Can use specialist magazines to reach **only** target audience. Magazine ads are in colour and are more attractive.	They are only published once per month/week. More expensive then newspapers.	Perfume Golf equipment Fashion clothes
Posters/billboards	Permanent* Cheap Potentially seen by anyone who passes by them.	Can easily be missed. No detailed info can be included.	Events Products bought by a large section of the population
Cinemas	Visual image shows product in a positive way. Fairly cheap. Effective if target audience goes to see particular films.	Only seen by people who go to watch films.	Toys for a children's film.
Leaflets	Cheap Given to a wide range of people. Delivered to people's houses. May contain vouchers to encourage readers to keep the advert. Permanent*	May not be read.	Local events. Retail stores like Seven-Eleven
Internet	Can be seen by anybody around the world. Can store lots of info. Orders can instantly be made.	Internet searches may not highlight the website and it could be missed. Internet access is limited in some countries. Competition from other websites. Security issues may discourage people from buying online.	Virtual goods. Services such as banking or insurance. Virtually anything that is not too small.

Others (delivery vehicles or sides of bags)	Cheap	May not be seen by everyone.	Shops put their names on plastic bags. Coca cola use neon signs.

***Permanent:** adverts can be kept for future references.

Design of adverts

Businesses usually use the **AIDA** model:

- **Attention:** Informs consumers that the product exists.
- **Interest:** Consumers need to become interested in the product.
- **Desire:** Makes consumers want the product.
- **Action:** Prompts consumers into buying the product.

The AIDA model is most effective on products that are not used regularly. It is less effective on products that are bought on a daily basis because people will know how good the quality really is.

Promotion

<u>Different types of promotion</u>

Promotion is usually used to **support** advertising and to encourage new or existing customers to buy the product. Its main function is to **boost sales** in the **short-term**, but not in the long term. It is used to attract **new customers** so that they can **try** out items with the hope that they will like it and continue to buy it after the promotion has ended. Here are some ways in which promotion is used:

- **Price reductions:** Involves sales or price reduction coupons.
- **Gifts:** Gifts are placed in the packaging of the product to encourage consumers to buy it. (e.g. toys in McDonald's happy meal).
- **Competitions:** A card may be put in the packaging allowing the consumer to enter contests such as the lottery.

- **Point-of sale displays and demonstrations:** Can be put near the window and displayed attractively. It could also encourage people to buy it if they can see how it works (demonstrated by sales staff)
- **After sales service:** e.g. warranty services. It reassures the customers that if the product has a problem then they can go and fix it for free. This make the product more attractive than others without warranty.
- **Free samples:** Encourages people to **try** the product. It can be included in other products as well. E.g. washing machine comes with free washing powder.

The advantages of promotion

- Can boost sales during the year when sales are traditionally low (encourage **off-season** purchases)

- Encourages people to **try** a product.
- Encourages people to buy a product or the product in **greater quantities**.
- Encourages people to buy a product instead of **competitors'** products.

Which type of promotion should be used?
When deciding on what type of promotion should be used, these points should be considered:

- **The stage of the product life cycle**: e.g. use informative advertisement in the introduction stage of the life cycle.

- **The nature of the product itself**: e.g. consumer goods use coupons but producer goods use discounts on bulk buying.
- **The advertising budget**: obviously the type of promotion depends on how much you can spend.
- **The cultural issues involved in international marketing**: businesses need to consider whether their type of advertising might offend the local people. They should also take into account things such as how many people own TV, literacy level, etc…
- **The nature of the target market**: Different markets require different media for advertising.

Personal selling

- Used when the **nature** of the product **varies**. e.g. housing
    - Price varies.

    - Quality varies.
    - Customer requirements vary.
- When customers need **advice** on what type of product is the most appropriate for their situation.
- When selling **expensive** products such as cars.
- When **negotiation** about price or products is needed. This is common for businesses that sell to other businesses. (e.g. discounts on bulk buying)
- When a business has a stand at a **trade fair**.

Public relations

- Good for improving the brand/company's **image**.

- These activities raise **public awareness** of the company.
- Includes:
    - Sponsoring events such as football matches.
    - Giving products to charity.
    - Employees take part in an activity for a good cause.

Customer service

It is far more expensive to attract customers than to keep old customers, so one key objective for any business is to retain their old ones. In the international business environment, there are many competitors, so businesses need to raise the **value** of their products with **customer service**.

Good customer service is not only producing a good product but also means:

- **Giving advice about the product**: It is always good to give as much information about a product as possible so that the customers can be sure that they have purchased the product that meets their requirements.

- **Delivering goods for customers**: It becomes convenient for the customer which encourages the customer to buy products from the business since they do not have to go anywhere.
- **Providing credit facilities**: This means letting customers pay later or in monthly installments. This make products look cheaper and more affordable encouraging customers to buy them. Credit facilities are usually offered when people buy expensive products. You usually get interest as a result, but you could charge no interest for promotional purposes.

- **Providing product information**: This means giving information on how to use the product and offering help on customer service helplines.
- **After-sales service**: The aim is to show that you care about customers' **satisfaction**. Examples of after-sales service include:
    - Warranties.
    - Regular product checks.
    - Giving refunds for faulty products.
    - Exchanging unsatisfactory goods.

Chapter 22: The marketing mix: place

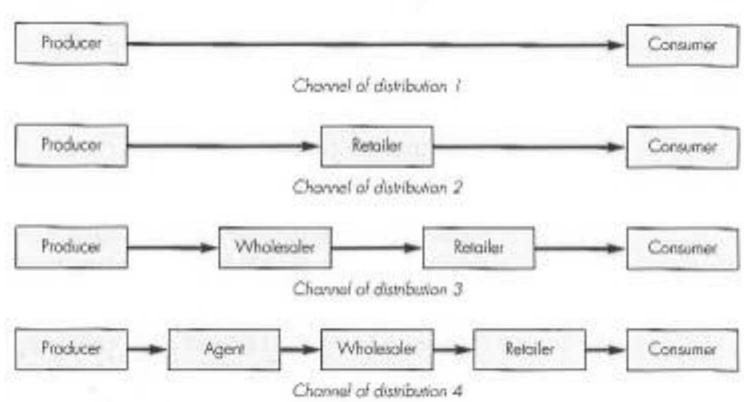
The role of place in the marketing mix

After the product, price, and promotion has been decided, the product/service has to be available to the consumer **where and when they want to buy**. Consumers should be able to get to the product easily, and the product has to be in the right place (e.g. expensive chocolate shouldn't be in a small grocery store) to sell well.

Channels of distribution

Businesses need to know how to get the product to the consumer. They may use a variety of channels of distribution:

- **Channel 1:** The manufacturer sells **directly** to the **customer**. e.g. agricultural goods are sold straight from the farm, businesses buy raw materials from another…
- **Channel 2:** Involves selling to **retailers**. Common when the retailer is large or the product is expensive.
- **Channel 3:** Involves the product going through **wholesalers** as well. Wholesalers **break bulk** so that retailers can buy them in smaller quantities. This is common for perishable items such as foods.
- **Channel 4:** Involve selling the product overseas through an **agent**, who sells them to wholesalers on behalf of the company. This may be because he/she has better knowledge of the local conditions.



Methods of distribution

Methods of distribution for different channels of distribution can include:

- **Department stores**: Usually in the centre of town that sells a wide range of goods from many producers.

- **Chain stores**: Two or more which has the same name/characteristics.
- **Discount stores**: Offers a wide range of products, including branded products, at discount prices. Often all the products are similar.
- **Superstores**: Very large out-of-town stores.
- **Supermarkets**: Very large retail stores with all kinds of goods. (usually daily needs, foods)
- **Direct sales**: Goods are sold directly to the consumer.
- **Mail order**: Customers order via the post by looking at the catalogue
- **Internet/e-commerce**: Customers order via the internet by looking at the website.

E-commerce

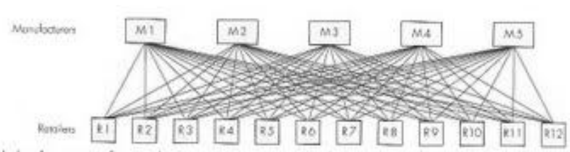
The use of the **internet** to carry out business transactions. Businesses could communicate via **email** as well. Producers as well as retailers can use the internet to sell to customers.

Advantages and disadvantages of a wholesaler

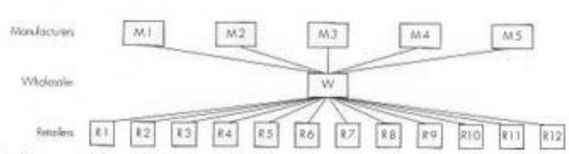
<u>Advantages</u>

- Breaks **bulk**.

- Reduces **storage costs** for retailers and producers.
- Fewer **transactions** are needed for the producers. (only a few wholesalers) they no longer need to do as many **deliveries**.
- Gives **credit** to small retailers.
- May deliver to small retailers reducing their **transport costs**.
- **Promotion** carried out by wholesaler instead of producer.
- They give **advice** to retailers/producers on what is selling well.



Without a wholesaler, a manufacturer has to process many orders from retailers



With a wholesaler, a manufacturer has less paperwork

Disadvantages

- More **expensive** for small retailers.
- May not have the **full range** of products to sell.
- **Takes longer** for perishable products to reach the retailer.
- Wholesaler may be **far** from small shops.

Selecting the channel of distribution to use

When selecting the channel of distribution to use producers need to consider a few things:

- **Type of product?**: Is it sold to other **producers** or **customers**?
- **Is the product very technical?**: Will you need to explain how to use the product? If yes, Channel 1 should be selected (e.g. airplanes)
- **How often is the product purchased?**: If it is bought every day, it should be available in many retail outlets, otherwise people might not bother to buy it at all.
- **How expensive is the product?**: If it is expensive and has an image of being expensive, then it will be sold in a **limited** number of retail outlets.
- **How perishable is it?**: If it is very perishable, it should reach the customers quickly or be available in many outlets so it can be sold quickly.
- **Location of customers?**: Channel 4 might be used for customers overseas. E-commerce would be viable anywhere apart from the countryside.
- **Where do competitors sell their products?**:
  Usually producers will sell their product in retail stores where their competitors sell too so that they can compete directly for consumers.

Methods for transporting goods

This is what kind of vehicles are used to transport the products. They should be **fast** enough for the product to reach its destination in time. However, they must also be **cost efficient** and **safe**. These factors a taken into account when deciding which method of transportation is used.

- **Road haulage**:
  - Cheap and fast.
  - Require no rail links.
  - Can advertise on side of lorries.

    - Not cost effective if lorries are not used often, may need to hire a specialist transport business instead.
- **Railways**:
    - Even cheaper and faster than road haulage.
    - Useful for long distances.
    - Goods need to be transported to retail stores by road haulage at the end of the destination.
- **Canal and river**:
    - Slow but cheap.
    - Good for products far too big/heavy to be transported by road/train.
    - Need canals and rivers.
- **Sea freight**:
    - Used mainly for international trade.
    - Can carry a lot of products.
    - Products are stored in containers, which can be easily loaded onto lorries. Makes it cheap to load and unload the ships.
- **Air freight**:
    - Extremely fast but expensive.
    - Used for small, expensive, or perishable products.
- **Pipelines**:
    - Used to transport liquids or gases over long distances.
    - Cheaper than using road haulage for liquids. Roads are not always available.

Drawing up a marketing plan

Finally, after all the four P's of the marketing mix have been decided, the Marketing department will put them together into one **marketing plan**. It will also consider how the 4 P's will be modified or adapted to fit the **overall image** of the product. If this is successful, sales and profits will be likely to increase.

Note: a detailed drawing of the product must be included in the marketing plan.

Chapter 23: Factors affecting production

What is meant by production?

Production is the **provision** of a product to satisfy wants and needs. The process involves businesses **adding value** to their products. E.g. The production process of matches involve cutting wood into matchsticks, putting phosphorus ends on them and packaging them to sell.

Productivity

Productivity is the **outputs** measured against the **inputs** used to create it. This is measured by:

Output (over a given period of time)/Number of employees

If a worker makes more products in the same amount of time, his productivity increases. Firms aim to be **productively efficient** to be able to make more profits and compete against their competitors.

Methods of production

<u>Job production</u>

- Goods are made individually, by one person.
- Goods are usually specialized, no two goods are the same.
- Usually made to order.

Advantages

- The product meets **exact requirements** of the customer.
- The workers have more **varied** jobs.
- More **job satisfaction** for workers.

Disadvantages

- **Skilled** labour is needed.
- **Slower** and **more expensive** than other methods of production.
- Usually **labour intensive**.

Batch production

- Products are made in **batches** according to **order**.

Advantages

- It is **flexible**. You can easily **change** from making one product to another.
- Still gives some **variety** to workers jobs.
- Production is not too affected by **machinery breakdown**.

Disadvantages

- Expensive to **move** products around the workplace.
- **Storage space** will be needed to store raw materials. **Expensive**.

Flow production

- Large quantities of a product are produced in a **continuous process**.
- Uses **specialization**.
- Benefits from **economies of scale**.
- Is **capital intensive**.

Advantages

- **Low costs**. Low prices. High sales.
- Increased **efficiency**.
- Little **training** is needed.
- Goods are produced **quickly** and **cheaply**.
- Goods do not need to be moved around like batch production. **Saves time**.
- Quality is **high** and **standardized** (courtesy to Muhammad Hassaan Ayyub)

Disadvantages

- **Boring** for the workers. Little **job satisfaction**.
- Needs a lot of **capital** to set up.
- If one **machine breaks down** then the whole production process stops.

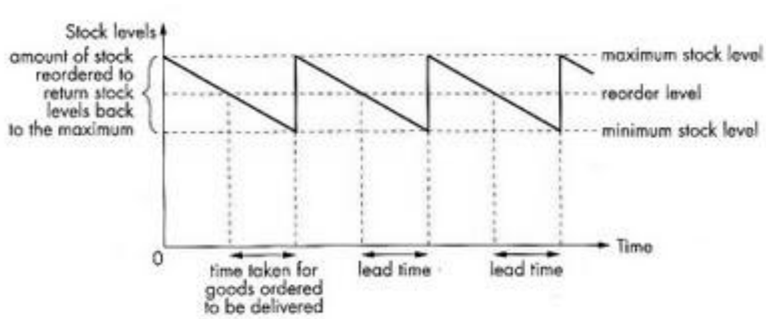
Which type of production should be used?

The type of production that should be used varies with how the product is demanded:

- **Job production**: **Unique** and **individual** service is required.
- **Batch production**: Demand is **higher** but products will not be sold in large quantities. Batches are made to **orders**.
- **Flow production**: Demand for the product is **high** and **steady**.

Stock control

Stock control is important so that a business will **not run out** of stock and be unable to satisfy demands. When stock levels get to a certain point, more goods need to be **reordered** for the stock level to reach its **maximum** again. If more goods are not reordered, stocks could run out because of an **unexpected surge** in **demand**. However, keeping a lot of stock costs money, so the level of stock in a company should always be balanced. The following graph demonstrates how stock can be controlled:



Lead production

- Focuses on **cutting down waste**, increasing **efficiency**.

- It tries to reduce the **time taken** to **produce** a product and transport it the selling point.
- Includes the following methods:
  - Kaizen.
  - JIT production.
  - Cell production.
  - Kanban.

Kaizen

- **Continuous improvement** through the elimination of **waste**.

  - **Ideas** of **workers**.

  - Regular **meetings** of workers to discuss how to increase efficiency.
- The advantages of Kaizen:
  - Increased **productivity**.
  - Reduced amount of **space** needed for the production process.
  - **Work-in-progress** is reduced.
  - Improved **layout** of the factory floor may **combine jobs** of some employees, freeing others to do other things.

Just in time production

- **Eliminating** the need to hold **stocks**.

- Goods are **delivered** to the selling point just when they are **needed**.
- JIT production needs:
  - **Reliable** suppliers.
  - **Efficient** system of ordering raw materials.

Cell production

- Production line is divided into **cells**.

- Each cell makes an **identifiable part** of the finished product.
- Boosts **morale**.

Kanban

- A system of **ordering** used with JIT production.

- Operates with **two component bins**.
    - When one is emptied, production begins to fill it.
    - The other one is then left to be emptied.
    - The first one is filled up when the second one is emptied.

Improvements in technology

Here are some things that technology does in the production process:

- **Automation**: Equipment in the production process is controlled by a computer.

- **Mechanisation**: Tasks are done by machines **operated** by **people**.
- **CAD (computer aided design)**: Used for designing 3-D objects.
- **CAM (computer aided manufacture)**: Computers control machines in the production process.
- **CIM (computer integrated manufacture)**: CAD and CAM are used together. The computer that uses CAD is directly linked with the one that controls the production process.

Here are some things that technology does in shops:

- **EPOS (electronic point of sale)**: When products' bar codes are scanned and the information is printed out on a receipt. Data is also sent to a computer to keep track of **stocks**.

- **EFTPOS (electronic fund transfer at point of sale)**: When the cash register is connected to the retailer's **main computer** and **banks**. The customer's **credit/debit card** is swiped and the money is **debited** from the customer's bank account. A receipt is printed out to confirm the transaction.

The advantages of new technology

- Increased **productivity**.

- **Boring jobs** done by machines. Boosts **motivation**.
- **Training** is needed to operate new machines. Workers become more **skilled**.
- Better **quality**.
- Better **stock control**.
- Quicker **communication** and reduced **paperwork**.
- **Info** is available **faster**, resulting in **faster decision making** (for managers).

The disadvantages of new technology

- **Unemployment**

- **Expensive**
    - To invest in new technology.
    - To replace outdated technology.
- Employees are **unhappy** with **changes** in the workplace.

Quality control

There are three ways to control quality:

Quality control

- Involves checking and removing faulty products at the **end** of the production process.

- **Wastes** a lot of money.

Quality assurance

- Involves inspecting **during** and at the **end** of production.

- Aim to
    - Stop faults from happening.
    - Set a quality standard that all products have to achieve.
- Need teamworking and responsibility.

Total quality management

- Encourages **everyone** to **concentrate** on quality.
- Quality is the **main aim** for all staff.
- Products need to satisfy all **customer need.**

Chapter 24: Factors affecting location

Location of industry

The location of a business is considered when it **starts-up** or when its present location is **unsatisfactory**. The business's objectives as well as the conditions of the environment **change**, so the business may need to look for a new location once in a while.

There are many factors that affect the location of businesses, and these factors are different for each business sector. We'll take a look at them below.

Factors affecting the location of a manufacturing business

Production methods and location decisions

- **Small scale**: transport and location of suppliers are less important.
- **Large scale**: transport and location of suppliers are more important.

Market

- Need to be near to transport **perishable** goods.
- Need to be near to cut **transportation expenses**.

Raw materials/components

- Need to be near to transport **perishable** goods.
- Need to be near to cut **transportation expenses**.

External economies of scale

- How good **nearby** businesses are.
    - For maintenance of equipments.
    - For training workers, etc…

Availability of labour

- **Wages** of the labourers.
- How **skilled** they are.

Government influence

- Grants/subsidies.
- Restrictions on dumping, etc…

Transport and communication

- To be able to transport product easily.

Power

- Need a **reliable** source of power to operate effectively.

Water supply

- A lot of water is needed in the production process (e.g. cooling, cleaning)
- Cost of water.

Personal preferences of the owners

- May locate in areas that:

- They come from.
- They like.
- Pleasant weather, etc…

Climate

- E.g. to reduce heating costs in a warmer climate.
- Some climates are required to produce certain items.

Factors affecting the location of a retailing business

Shoppers

- Do shoppers go there?
- What kind of shoppers go there?

Nearby shops

- Competitors.
- Mass market.
- Gap in the market.

Customer parking available/nearby

- Convenience for the customer.

Availability of suitable vacant premises]

- Goods sites (e.g. in shopping centres) are in short supply.

Rent/taxes

- The more popular the site, the more expensive.

Access for delivery vehicles

- For delivering goods.

Security

- If the area is insecure
  - Goods will be stolen.
  - Insurance will be reluctant to insure the shop.

Legislation

- Laws restricting the trade of goods in certain areas.

Factors that influence a business to relocate either at home or abroad

- **The present site is not large enough for expansion.**
  - If a business simply prefers to expand elsewhere, the factors affecting location will have to be considered.
- **Raw materials run out.**
  - One alternative is to import raw materials from elsewhere.
  - Important for mining industries.
- **Difficulties with the labour force**
  - Wages are too high.
  - Need skilled labour.
- **Rents/taxes rising.**

- **New markets open up overseas.**
    - Cuts transport costs.
    - Bypass trade barriers.
- **Government grants**
    - To attract businesses to locate in development areas.
    - To attract foreign investment.
- **To bypass trade barriers**
    - Tariffs
    - Quotas

Factors affecting the location of a service sector business

Customers

- Whether customers require:
    - Direct contact.
        - Is it convenient for customers to go the business?
        - Will the service arrive at customers' houses in time?
    - No direct contact needed.
        - Mail
        - Internet

Personal preference of owners

- Near their homes.

Technology

- Technology allows businesses to locate in cheaper sites.
    - Telephone.
    - Internet.

Sir Talha Siddiqui
03133106254

    - Transport.
- No need to be near customers.

Availability of labour

- Need to locate to sites where skilled labourers live.
    - Labourers may relocate to be near the business.

Climate

- Important for **tourism**.

Near to other businesses

- Businesses that supply or repair machinery to others need to be near them to respond quickly.
- Post office/banks need to be in busy areas for the convenience of customers. That is, being near malls, shops, etc…

Rent/taxes

- If the business does not need direct contact with the customer, then it could locate in cheaper areas

Chapter 25: Business in the international community

The international dimension

In business, no manager can operate without being affected by the **international community**.

Exchange rates

Exchange rates is the **value** of one currency **compared** to another.

How are exchange rates determined?

There are two type so currencies:

- **Floating rates:** The exchange rate of the currency is allowed to change freely depending on market forces, i.e supply and demand of the currency.
- **Fixed rates:** The exchange rate of the currency is set by the country's central bank.

When the exchange rate rises, it is called **appreciation**. When it falls, it is called **depreciation**.

How are businesses affected by changing exchange rates?

- **Appreciation:**
  - Import prices fall.
  - Export prices rise.
- **Depreciation:**
  - Import prices rise.
  - Export prices fall.

These **exchange rate movements** can cause serious damage to businesses, making business endeavours that would have been profitable make losses because of changes in the currencies. The EU, for example, wants to limit these bad effects, and hence established a **common currency**, the

Euro.

International economic organisations

- **Economic** and **political unions**. (e.g. the EU)

- **Free trade** agreements. (e.g. NAFTA)
- Organisations **working for free trade** between countries. (WTO)

The European Union

- Consists of 25 European countries.

- Creates a **single market** in the EU.
    - To tariffs, quotas or any **trade boundaries**.
    - This results in:
        - A huge market benefiting from **economies of scale.**
        - Increased **competition** resulting in better products.
- **Common currency**.
    - Issue of Euros are controlled by the European Central Bank.
    - **Interest rates** for the Euro become the same.
- The **social charter**:
    - The EU wants to improve **working conditions** and make **finding josbs** equal in the EU.
    - The main conditions include:
        - Workers can look for work **anywhere** in the EU.
        - Workers must be **consulted** on important issues.
        - **Equal** treatment of **full**/**half** time workers.
        - Limits on **maximum** working **hours**.
        - Improved **health** and **safety** rules at work.

Advantages for the UK to join the EU

- Lower costs because:

    - One **price list** throughout Europe can be used.

    - No more **charge** through currency **conversion**.
- Easier to:
    - **Trade** with EU countries.
    - **Compare** costs of supplies with EU countries.
- No risk of **losing out** on exchange rate changes.

Disadvantages for the UK to join the EU

- More **competition** from non-UK firms.
- Consumers might buy **cheaper** products from other EU countries.
- The rate of **interest** might no longer suit UK firms.

<u>Free trade unions</u>

Eliminates **all trade barriers**. Businesses within the free trade union are affected in the following ways:

- More **competition** from foreign firms.
    - Consumers have **more choice** and **prices** are **lower**.
- No '**protection**' by governments.
- More **opportunities** for **exporting**.
    - **Efficient** firms will be more successful.

The long-term aim of the free trade union is to **encourage trade** between the member countries, ultimately improving **living conditions** for the people.

Globalisation

Globalisation is the word used to describe the increased **worldwide competition** and **business activity**. Goods and services that once can only be found in one country has spread all around the world. There are several reasons for this:

- **Free trade agreements** encourage **international trade**.
- Improved **travel links** and **communication**.

- Countries that have been undeveloped before start to develop and **export** their own goods, leading to more **international competition**.

Globalisation results in:

- **More choices** and **lower prices** for the consumer.
- Businesses look into more ways to become more **efficient**.
  - Why many businesses merge to become **multinationals**.
- **Inefficient** businesses **go out of business**.
- **Free trade** results in:
  - More workers losing jobs, since governments can no longer **protect** them from foreign competition.

Multinational businesses

Multinationals are businesses that have **factories**, **services**, or **operations** in **more than one country**. It is important to note that, for a business to become multinationals, they must **produce goods** in more than one country.

Why do firms become multinationals

- **To cut costs:**
  - Labour costs.
  - Raw material costs.
- **To extract raw materials not found elsewhere.**
- **To produce goods nearer to the market.**
- **To bypass trade barriers.**
- **To expand and spread risks.**

Advantages of multinationals operating in a country

- **Jobs** are created.
- New investment increases **national output**.
- **Imports** are **reduced** since there are more goods in the country. More **exports**.
- More **taxes** are paid to the government.

Sir Talha Siddiqui
03133106254

Disadvantages of multinationals operating in a country

- Jobs created are usually **unskilled jobs**.

- **Local firms** are forced **out of business** since they can't compete with multinationals.
- **Profits** flow **out** of the country.
- Multinationals use up **scarce resources**.
- May **influence** the **government**.