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UPDATED TO 2023-2025 SYLLABUS

# CAIE IGCSE BUSINESS STUDIES

SUMMARIZED NOTES ON THE THEORY SYLLABUS

# 1. Understanding Business Activity

## 1.1. Business Activity

- **Needs:** goods or services that are essential for survival.
- **Wants:** goods or services customers desire but are not essential for survival.
- **Economic Problem:** unlimited wants but limited resources to satisfy the wants.
- **Scarcity:** the lack of sufficient products to fulfil the total wants of the population.
- **Factors of production:** resources needed to produce goods and services; they are:
    - **Land** – any natural resource used in production.
    - **Labour** – mental and physical efforts of employees.
    - **Capital** – finance, machinery and equipment needed for the manufacture of goods.
    - **Enterprise** – individual/s who manage/coordinate the three other factors, make decisions and take risks.
- **Opportunity Cost:** the next best alternative is given up by choosing another item.
- Due to scarce resources, a choice has to be made; this leads to opportunity cost.

## 1.2. Importance of Specialisation

**Specialisation**: When people and businesses focus on what they are best at.

- Division of labour is when production is split into different tasks, and each worker performs one of these tasks. It's a form of specialisation.

| Advantages | Disadvantages |
|---|---|
| Workers are trained in one task and specialise in this, increasing productivity and efficiency | repetitive tasks can cause boredom and burnout for employees, reducing motivation and job efficiency |
| Specialisation with division of labour will result in better quality output | If a worker is not present, production will be disrupted, causing a waste of time and resources, as well as less output and efficiency. |
| An increase in efficiency will lead to economies of scale. | Specialised workers require higher wages, and training current employees will increase costs. |
| Workers become more skilled and experienced, reducing waste of time and resources. | |

## 1.3. Purpose of Business Activity

- Businesses combine scarce factors of production to produce goods or services to satisfy people's needs and wants.
- **Business Activity:**
    - Combines scare factors
    - Produces goods and services
    - Employees people

## 1.4. Added Value

- Added value is the difference between the cost of purchasing bought-in material and the price of the finished goods.

*Added Value = selling price – total cost*

- For example, by transforming cotton into a T-shirt, the business adds value to the cotton, as the same material can be sold for more after the transformation.
- It is NOT the profit because added value does not include the expenses of producing this good (e.g. labour, electricity, machinery, etc.)

| Advantages | Disadvantages |
|---|---|
| Maybe able to make a profit if these other costs come to a total less than the added value | Increasing the product's price can lead to lower sales and, perhaps, profit. |
| It can be used to pay other expenses. | |

**To increase added value, a business can either:**

- Increase the selling price by increasing the quality of goods and services to convince customers/consumers
- Reduce the cost of materials but keep the price the same.

## 1.5. Classification of Businesses

- Businesses can be classified into three sectors:
    - **Primary Sector:** Industry extracts and uses the earth's natural resources to produce raw materials for other businesses.
    - **Secondary Sector:** The industry manufactures goods using the raw materials provided by the primary sector.
    - **Tertiary sector:** The Industry provides services to consumers and other industry sectors.
- **Developing Countries:** where the primary sector is the most important, as more employees and output are produced than in secondary and tertiary sectors
- **Developed Countries:** where the output of the tertiary sector is often higher than the other two sectors combined.
- De-industrialisation occurs when there is a decline in the importance of the secondary sector.

- **Reasons for changes in the relative importance of the three sectors over time:**
  - When sources of some primary products become depleted
  - Developed economies are losing competitiveness to newly industrialised countries.
  - Due to the rise in living standards, consumers spend more of their income on services such as travel and restaurants than on manufactured goods.

## 1.6. Mixed Economy

- Has both a private sector and a public sector.
  - **Private Sector:** Businesses NOT owned by the government will decide what and how to produce. The main aim is to make profits.
  - **Public Sector:** Owned by the government. Government will decide what and how to produce (i.e. healthcare, education, defence, public transport). The main aim is to provide a service to customers.
- **Privatisation** refers to selling a public sector business to the private sector.

| Arguments for Privatisation | Arguments against Privatisation |
|---|---|
| Costs can be controlled because the private sector's main objective is profit. | Increased unemployment as private sector businesses may want to cut costs. |
| More efficient use of capital | Less likely to focus on social objective |
| Competition between private sector businesses will help improve product quality. | |

## 1.7. Enterprise, Business Growth and Size

- An **entrepreneur** is a person who organises, operates and takes risk to make the business better
- **Characteristics of Entrepreneurs:**
  - Hard-working
  - Risk Takers
  - Creative
  - Effective Communicators
  - Optimistic
  - Self-confident
  - Innovative
  - Independent.

**Advantages and Disadvantages of being an Entrepreneur:**

| Advantages | Disadvantages |
|---|---|
| Independent, able to choose how to use time and money | entrepreneurs will have to put their own money into the business. |
| Able to put own ideas into practice | many entrepreneur's businesses fail (risky) |
| It may become successful and very profitable if the business grows | Lack of knowledge and experience in starting and operating a business |
| Able to make use of personal interests and skills | Lost income from not being an employee for another business (Opportunity cost) |
| Profits to themselves, no need to share them with anyone | They will have to invest their savings as well as find other sources of finance, which is time-consuming and expensive |
| Income is higher than a regular employee | |

## 1.8. Business Plans

- ~~**Business Plan:**~~ a document containing the business objectives and essential details about operations, finance and owners of the new business.
- Contents of business plan:-
  - Description of the product
  - Products and services
  - The market
  - Business location and how products will reach customers
  - Organisation structure and management
  - Financial information
  - business strategy
- Business plans assist entrepreneurs because:
  - It helps gain finance. Banks will ask for a business plan before agreeing to a loan or overdraft for the business
  - It forces the entrepreneur to plan carefully, which reduces the risk of the business failing.

## 1.9. Government Support for Start-Ups

- Governments encourage entrepreneurs to set up a business because start-ups:
  - reduce unemployment
  - Increase competition
  - Increase output
  - Benefit society
  - Further growth of the economy
- Governments may give support to entrepreneurs by:
  - **Business ideas & help**, organising training for entrepreneurs that gives advice, and support sessions.
  - Finance, they may lend **loans** at low-interest rates or **grants**, as well as low-cost premises
  - Governments provide grants for **training employees** to make them more efficient and productive
  - Governments allow entrepreneurs to use **research** facilities in Universities

## 1.10. Business Size

- **Why is it beneficial to compare business size?**
  - Investors can decide which business to invest in.
  - Government, different tax rates for small and large firms.
  - Competitors, to compare size and importance with other firms.
  - Workers, to have an idea of the number of employees needed.
  - Banks, the importance of the loan compared to business size.
- **There are several different measurements of business size, and they all have limitations:**

| Measurements | ~~Limitations~~ |
|---|---|
| The number of people employed in the business (accessible to calculate) | ~~Capital~~-intensive firms employ fewer people but produce high levels of output. |
| The value of the output of the business (useful for same industry Businesses) | Does not take into account the value of goods sold and the sale of goods. |
| The value of sales (useful for retail businesses, especially if similar products) | different businesses sell different products (expensive and cheap) |
| The total value of capital employed (takes into account all values of capital) | Some businesses use Labour-intensive methods, which require less capital, more workers |

- **Capital Employed:** the total value of capital used in the business
- No method of measuring the size is considered correct, as each method gives different answers. Businesses choose the method they think is the best. Therefore, businesses may use more than one method.

## 1.11. Business Growth

- Benefits of the expansion of the business:
  - The possibility of higher profits for the owner.
  - More status and prestige for owners and managers.
  - Lower average costs.
  - A larger share of its market portion of total market sales it makes is greater.

### Ways of Business Growth

- Businesses can either grow by:
  - Internal Growth
  - External Growth
- Internal Growth is when the business expands its existing operations
- External Growth is when the business takes over or merges with another business.
  - **Takeover:** When one business buys out the owners of another business, which then becomes part of the 'predator' business.
  - **Merger:** When two owners of a business agree to join their businesses together
- There are three types of External Growth:
  - **Horizontal Integration:** The same industry and stage of production firms merge or take over.
    - For example, a chocolate manufacturer takes over another chocolate manufacturer.
    - **Benefits**:
      - Reduces the number of competitors in the industry
      - Opportunities for economies of scale
      - A bigger share of the total market can be achieved
    - Problems include diseconomies of scale and difficulty in controlling and managing the business
  - **Vertical Integration:** when one business merges or takes over another business in the same industry but at different stages of production, it can be forward or backward.
    - Forward integration is when merging/takeover is done with the next stage of production, Ex. a chocolate manufacturing company (secondary sector) merging with a chocolate shop (tertiary sector)
      - **Benefits for forward:**
        - The merger provides an assured outlet for its products
        - The expanded business absorbs the profit margin made by the retailer/Manufacturer.
        - Information regarding consumer needs and preferences can be obtained directly from the manufacturer.
      - Backward integration is when merging/takeover is done with the previous stage of production, Ex. a chocolate manufacturing company takes over a cocoa farm.
        - **Benefits for Backward:**
          - Merger gives an assured supply of essential components
          - The expanding business absorbs the profit margin of suppliers.
          - A supplier could be prevented from supplying to other manufacturers.
          - Costs of components and supplies are controlled.
  - **Conglomerate Merger:** a firm merging/taking over another firm in a different industry. (also known as 'diversification')
    - For example, a chocolate manufacturer is merging with a photography company.
    - **Benefits:**
      - Activity in more than one industry will diversify and spread the risk taken by the business.
      - Transfer of ideas in the different sections can help the business.

### Disadvantages Caused by Business Growth

- Control and management get harder with expansion (can be prevented by carefully planning expansions and adjusting management style and hierarchy).
- Larger businesses lead to poor communication (stronger and more efficient communication channels can prevent it).
- Expansion costs are high and can result in a shortage of finance for businesses (A financial plan must be prepared in anticipation of expansion; it can include short/long-term loans to compensate for financial loss).
- Integrating with another business can have conflicts and difficulties, for example, business culture and style of management. (Compromises will have to be made, or a new style of management can be applied altogether, which can help reduce conflicts)

### Why Small Businesses Remain Small?

- The type of industry the business operates in
- Market share
- Owners' objective

## 1.12. Why Businesses Fail

- **Lack of Management Skills** – from lack of experience, poor choice of managers (family business), bad decisions can occur
- **Failure to plan for change** – businesses must adapt to an ever-changing business environment. It would be best if risks were taken.
- **Over-Expansion** – (diseconomies of scale)
- Poor financial management and liquidity issues
- **Competition with other businesses** – intense competition in the market can make it hard for new businesses to set up, as already established businesses can drive newly established businesses out of the market with their low, competitive prices.

## 1.13. Legal Identity

- **Unincorporated Business**: A business that does not possess a separate legal identity from its owner. These Businesses usually have:
  - **Unlimited liability**: the owner can be held responsible for the business's debts.
  - Greater risk, as owner is putting his personal possessions and living at risk.
- **Incorporated Business**: Business with a separate legal identity. Private/Public limited companies. These Businesses usually have:
  - **Limited liability**: the liability of shareholders in a company is limited to only the amount they invested
  - Less risk, as the owner is only risking the capital they invested, as well as any legal charges effect only the business and not the owner directly

## 1.14. Sole Trader

- It is a business owned and controlled by one person- the owner, who is the sole proprietor. It is a form of an unincorporated business.

| Advantages | Disadvantages |
|---|---|
| Few legal regulations (Easy to set up) | Decisions can be hard to make |
| Complete control | No separate legal identity, unlimited liability |
| Flexible working time | May not be able to raise funds to expand business |
| Ability to respond quickly to the needs and wants of customers | May have to work long hours |
| All profit goes to the owner | Difficult to compete with large firms |
| Complete secrecy in Business matters | May not have the proper skills to run a business |

## 1.15. Partnerships

- **Partnerships:** A form of business in which two or more people agree to own a business jointly. It can be set up by creating a partnership deal. It's a form of unincorporated business.
- **Deal of partnership**: The written and legal agreement between business partners. It is not essential but is recommended
- **Contents of Partnership Agreement:**
  - Amount of capital invested by all partners
  - Tasks to be done by each partner
  - The way profits are shared out
  - How long partnership will last
  - Arrangements for absence, retirement and how partners could be let known

| Advantages | Disadvantages |
|---|---|
| Easy to set up a deed of partnership | Unlimited liability |
| Greater access to funds | Share the profit |
| shared decision-making | Business ceases to exist if one partner leaves |
| shared management and workload | Decisions binding on all partners |
| | Difficult to raise finance |

## 1.16. Private Limited Company (LTD)

- **Private Limited Company**: Business owned by shareholders but cannot sell shares to the public (can only sell to family and friends).
- **Shareholders**: Owners of a limited company who buy shares represent part-ownership of the company.

| Advantages | Disadvantages |
|---|---|

| Advantages | Disadvantages |
| --- | --- |
| Raise capital from the sale of shares | **Cannot** sell shares to the public |
| Limited liability for shareholders | Legal formalities |
| Separate legal identity | Accounts are available for the public to see |
| Continuity | Not easy to transfer shares |

- **Articles of Association**: Contains the rules for managing the company.
- **Memorandum of Association**: Contains vital information about the company and the directors.

**These also apply to a public limited company.**

## 1.17. Public Limited Company (PLC)

- **Public Limited Company:** Businesses owned and controlled by the shareholders, but they sell to the public, and their shares are tradeable on the stock exchange.

| Advantages | Disadvantages |
| --- | --- |
| Can sell shares to the public | Legal Formalities |
| Rapid expansion possible/specialist managers appointed | Disclosure of accounts and other information |
| Limited liability | Divorce between ownership and control |
| Continuity | Expensive to 'go public' |

- **Annual General Meeting (AGM):** A yearly meeting where shareholders may attend to vote for a Board of Directors for the upcoming year.
- **Dividends:** Payments made to shareholders from the profit of a company. They are the return for investing in the company.

## 1.18. Franchise

- **Franchise**: An agreement of a business based upon an existing brand/business
- **Franchisee:** the business a company allows to conduct business using the company's name and brand. Have to pay an original fee to the franchisor and a percentage of its profit for the privilege
- **The Franchisor:** the company that allows another company to conduct business using the company's name and brand.

| Advantages to franchisor | Disadvantage to franchisor |
| --- | --- |
| Franchisee buys the licence, which means another source of finance | Bad reputation if one branch has poor management |
| Expansion is faster | The franchisee keeps some profit |
| Management is the responsibility of the franchisee | Training, some aspects of administration, and advertising are paid by the franchisor |
| Percentage of sale revenue is given to the franchisor every year | |

| Advantages to franchisee | Disadvantages to franchisee |
| --- | --- |
| Chances of business failure are reduced | Less independence |
| The franchisor pays for advertising | Unable to make decisions that would suit the local area |
| Fewer decisions to make with an independent business | The franchisor has the power to withdraw the agreement and can prevent the use of the premises |
| The franchisor provides training for staff and management | |
| Banks are often willing to lend to franchisees due to the low risk. | |

## 1.19. Joint Venture

- **Joint Venture**: is when two or more businesses join together to create a new business

| Advantages | Disadvantages |
| --- | --- |
| Sharing of costs | Profits have to be shared if the project is successful |
| Knowledge and experience can be shared | Conflict in decision-making |
| Risks shared | Different methods of running a business can create conflict |

## 1.20. Public Corporations

- **Public Corporations:** a business in the public sector owned and controlled by the state of government (By appointing a board of directors and setting objectives).

| Advantages | Disadvantages |
| --- | --- |
| Government ownership may be essential to some countries' industries, such as water supply and electricity generation. | The profit objective is not as powerful or important as in private-sector industries. |

| Advantages | Disadvantages |
|---|---|
| Ensure consumers are not taken advantage of | Inefficiency because managers rely too much on the government |
| Reduce wasteful competitors | It can be unfair to the private sector if subsidies are provided to the public sector. |
| Can help stabilize failing businesses to create job opportunities | Lack of close competition can decrease many activities |
| Important public services | It can be used for political reasons, preventing the business from opportunities like other profit-making businesses. |

## 1.21. Business Objectives

- **Business Objectives** are aims or targets a business works towards
- Businesses need objectives to help them be successful. However, they don't guarantee success.
- **Benefits of having business objectives:**
  - A clear target to work towards, thus improving Motivation.
  - It can help in decision-making.
  - It helps unite the whole business towards the same goal.
  - It can be used to compare how the business performs through objectives.
- Private sector business objectives:
  - **Business Survival** - Adjust to business environment, change price of products if necessary
  - **Generating profit** (total income of business revenue subtracted by total cost)– pay a return to owners or provide finance to invest further in business
  - **Returns to shareholders** - discourage shareholders from selling their shares. This can be done by increasing profit or increasing the share price
  - **Growth of business** – increase salaries, economies of scale. This is only achieved if customers are satisfied with the product
  - **Market Share** (the total percentage of total market sales held by one brand or business) - gives good publicity and more influence over suppliers and customers.
    - $\text{Calculation} = 100 \times \frac{\text{Company Sales}}{\text{Total market Share}}$
- **Why business objectives can change:**
  - It will work towards profit after being set up and stable.
  - After achieving a high market share, it aims to "return to shareholders".
  - A profit-making business hit with a crisis now has the short-term objective of survival.

## 1.22. Social Objectives

### Objectives of Social Enterprise

- **Social Enterprise:** an enterprise with social objectives and aims to make a profit to reinvest in the business. It has three objectives:
  - **Social**: to provide jobs and support for disadvantaged groups
  - **Environmental**: to protect the environment.
  - **Financial**: to make a profit to reinvest in the enterprise and expand its social work.

### Objectives of Public Sector Businesses

- **Financial**: Meet profit targets set by the government - either reinvested or funded back to the government.
- **Service**: meet quality targets the government sets and provide services to the public.
- **Social**: protect or create employment in certain areas.

## 1.23. Stakeholder Objectives

- **Stakeholder**: any person or group with a direct interest in the performance and activities of a business
- There are two types of stakeholder groups:
  - **Internal Stakeholders** work/own the company (owners, managers, workers)
  - **External Stakeholders** are outside the business (consumers, government, banks)
- Each stakeholder group has different objectives for the performance of the business
- **Internal Stakeholder** (Owners, managers and employees) objectives are payments or profits; they want business growth, so the value of investment increases, or they get higher status/power
- **Customers'** objectives are reliable products, value for money, good quality, good design and good service
- **Government** objectives include money from taxes, employing more people, increasing the country's output
- **The bank's** objectives are to make a profit out of loans and the payback of interest.
- Since different stakeholders have different objectives, it may cause conflict, to try to please all the stakeholders
- For example, customers want cheap products, but workers want higher salaries.
- Therefore, managers must compromise to decide which objectives are best for the company.

# 2. People in Business

## 2.1. Motivating Employees

### Motivation

- **Motivation**: factors that influence the workers' behaviour towards achieving business goals.
- **Factors that influence motivation at work:**

- Money
- Job Security
- Training
- Promotion
- Status
- Responsibilities
- Work environment

### Benefits of a Well-Motivated Workforce

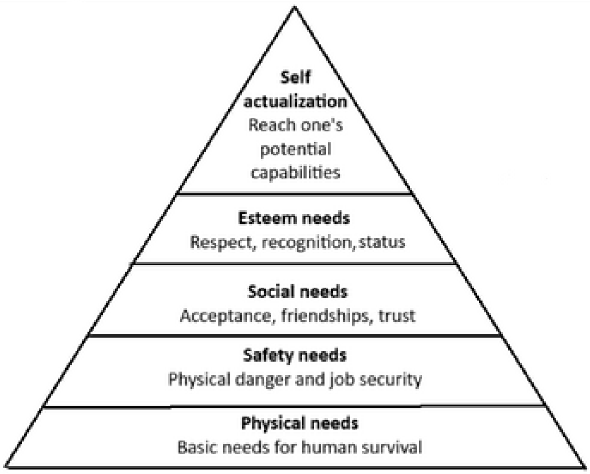
- Improved productivity
- Low rate of absenteeism (Workers' non-attendance at work without a good reason)
- Low rate of labour turnover (The rate at which workers leave the business)
- Better quality goods and services
- Improved labour productivity (A measure of the efficiency of workers by calculating the output per worker)

### Key Motivational Theories

**F.W. Taylor - Scientific Management Theory**

- It aims to reduce inefficiency in the workplace by finding the quickest method of performing tasks and training all workers to use this method.
- The theory of economic man: the theory that humans are only motivated by money, in which Taylor believed that money was the only motivational factor.
- The piece rate method of paying production came from his research.
- **Disadvantages:**
  - His ideas were too simplistic
  - If employees are unfulfilled with their work, productivity won't be gained, no matter how high the wage.
  - If employees' output can't be measured, practical problems arise.

**Abraham Maslow: Concept of Human Needs - Maslow's Hierarchy**




| Advantages | Disadvantages |
|---|---|
| Is it possible for managers to satisfy some or all of their needs | It is difficult to identify how much of the needs have been met or which level each worker is on |
| Easy to set goals and objectives | It doesn't include money as a need |
| | Not all needs are included. |
| | Self-actuation is rarely, if ever, achieved. |

**Fredrick Herzberg - Two-Factor Theory**

- **Hygiene Factors**: The factors that must be present in the workplace to prevent job dissatisfaction.
  - **Working Conditions**: Things that show how clean and safe the workplace is and what facilities are provided
  - **Relationship with others**: Good working relationships with workers and managers, and treated fairly with respect.
  - **Salary and wages**
  - **Supervisions**: Leadership style and how closely works are supervised
  - **Company policy and administration**: rules and procedures that control and affect the workplace.
- Hygiene Factors must be present to prevent job dissatisfaction
- **Job dissatisfaction**: How unhappy and discontent a person is with their job.
- **Motivators (Factors that influence a person to increase their effort):**
  - **The work itself**: Variety of jobs and challenging tasks through job enrichment.
  - **Responsibility**: Giving workers responsibility for tasks they perform.
  - **Advancement**: Opportunity for promotion
  - **Achievement**: They feel like they have reached a challenging goal.
  - **Recognition of Achievements**: Recognised by the people for their achievements

## 2.2. Methods of Motivation

**Financial Rewards**: cash and non-cash rewards paid to workers motivate them to increase their efforts.

- **Hourly Wage rate**: payment to workers based on a fixed amount every hour worked.

| Advantages | Disadvantages |
|---|---|
| Business only pays workers for the number of hours worked | Pay is not linked to how much they produce |

- **Salary:** fixed annual payment to specific grades and types of staff, not based on hours worked or output

| Advantages | Disadvantages |
|---|---|
| They do not receive more payment if they have to work long hours to complete the task. | Salary is not linked to effort or the amount produced |

- **Piece Rate**: Payment to workers based on the number of units produced.

| Advantages | Disadvantages |
|---|---|
| Workers are only paid for the number of items produced | Quality of goods may vary because of the need to produce more goods to increase pay |

- **Commission**: Paying sales staff based on the value of items they sell.

| Advantages | Disadvantages |
|---|---|
| Pay is linked to the value of goods sold | Workers are never sure of how much they will earn |

- **Bonus scheme**: an additional reward paid to workers for achieving target set by managers. Method of performance-related pay.

| Advantages | Disadvantages |
|---|---|
| Linked to a performance target | If the target is unrealistic, it can be demotivating |

- **Fringe benefits**: non-cash rewards used to recruit and retain workers and recognise certain employees' status. (e.g. Car, insurance, health care)

| Advantages | Disadvantages |
|---|---|
| Helping recruitment and retaliation of workers | Linked to status, not performance |

- **Profit sharing**: an additional payment to workers based on the business's profit.

| Advantages | Disadvantages |
|---|---|
| Linked to the performance of the business | Profit to employees may reduce dividends to shareholders or the amount reinvested in the business. |

**Non-financial rewards and methods**: methods used to motivate workers that do not involve giving any financial rewards.

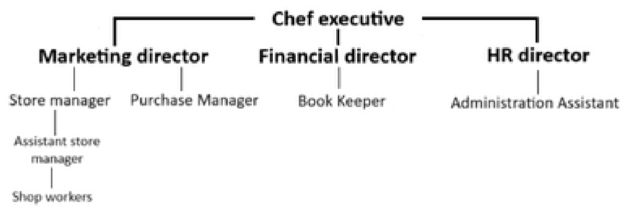
- **Job Rotation**: increasing variety in the workplace by allowing workers to switch from one task to another.
- **Job satisfaction**: how content and happy a person is with their job
- **Job Enlargement**: increasing or widening tasks to increase the variety of workers.
- **Job Enrichment:** organising work so workers are encouraged to use their full ability. This increases job satisfaction.
- **Job redesign**: increasing the variety or difficulty of tasks to discuss more exciting and challenging work for workers.
- **Quality circles**: a group of workers who meet regularly lower down in the organisation.
- **Team working**: organising production so that groups of workers complete the whole unit of work.
- **Delegation**: passing responsibility to perform a task to workers lower down in the organisation.

**Benefits of decrease in labour turnover:**

- There is no need to hire new employees, decreasing recruitment costs, training costs, and retaining skilled employees. This improves productivity.

## 2.3. Organisation and Management

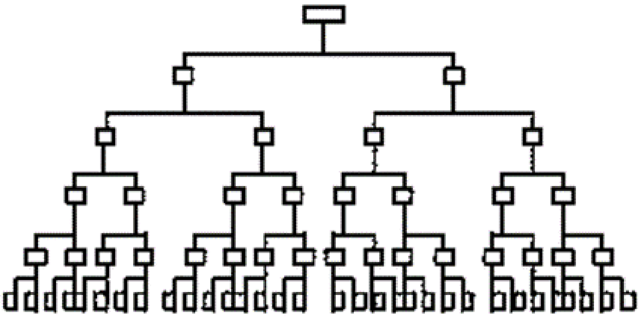
- **Organisational Structure**: refers to the levels of management and division of responsibilities within a company.
- **Organisational Charts**: refers to diagrams that outline the internal management structure.
- **Hierarchy** refers to the levels of management in any organisation.
- **Levels of Hierarchy**: refers to management/supervisors/other employees who are given a similar level of responsibility in an organisation.
- **Example of Organisational Chart:**



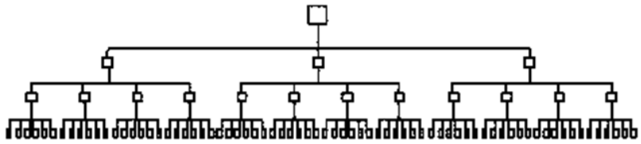

- **Benefits:**
  - The chart shows how everybody is linked in the organisation, which allows employees to be aware of their communication channel (chain of command).
  - Everyone can see what they are accountable for, which they have authority over, and who to take orders from.
  - Everyone is in a department, thus giving a sense of belonging
- **Chain of command** - The structure in an organisation allows instructions to be passed down from senior management to subordinates.
- **The span of control** - The number of subordinates working directly under a manager.
- **Subordinate**: an employee below another employee in the organisation's hierarchy.

There are two types of organisational structures of a business:

- **Tall Structure**: the longer the chain of command is, the 'taller' the organisational structure and the 'narrower' the span of control.



- **Flat Structure**: when a chain of command is short, the organisation will have a 'wider' span of control, thus making it a 'flat' structure.



- **Advantages of short chain of command**:
  - Communication and decision-making are quicker.
  - Fewer management levels to build connections with by the top management.
  - The span of control will be wider, encouraging managers to delegate more and allowing workers to feel trusted.
- **Advantages of a long chain of command**:
  - As decisions get passed down, it is checked by multiple people, thus reducing error and preventing bad decisions from happening
  - Lesser subordinates means management can focus more on their designated workers.
- **Factors affecting the size of the span of control**:
  - Difficulty of the task
  - The experience and skill of workers
  - The size of the business
  - the level of hierarchy
  - Management style
- **~~Delayering~~**: reducing the size of the hierarchy by removing one or more levels, often the middle management.

| Advantages | Disadvantages |
|---|---|
| Reduces cost | Increased workload on managers, thus decreasing the quality of work and its completion. |
| Communication and decision-making are quicker due to reduced chain of command. | Have to make redundancy payments to employees who lost their job |
| Increases the opportunity for delegation, which helps in motivation | Reduction in job security |

| Advantages | Disadvantages |
|---|---|
| Senior managers are in close touch with what is going on in the business | Reduce effective management of subordinates |

- **Delegation**: Giving a subordinate the authority to perform particular tasks.

| Advantages | Disadvantages |
|---|---|
| Application of job enrichment, leading to job satisfaction | Some managers are reluctant to delegate, as they will be held accountable for any errors |
| A form of training for junior managers | Managers lose some control over subordinates |
| Achieving the Esteem needs (Maslow's hierarchy) | |

- **Centralised Organisation**: one where all the important decision-making power is held at the head office/the centre and then passed down to lower levels.

| Advantages | Disadvantages |
|---|---|
| Decision-making is often quicker | Slower communication |
| Decisions are taken for the benefit of the whole business | Unable to respond quickly to changes in the local market |
| Greater use of specialist staff improves decision-making | May reduce motivation |

- **Decentralised Organisation:**

| Advantages | Disadvantages |
|---|---|
| Decisions are made based on local needs. | Decisions taken might not be in the interest of the business |
| It can be used to train junior managers. | Poor decisions might be made often due to lack of experience and skills |
| Delegation helps improve worker motivation. | |

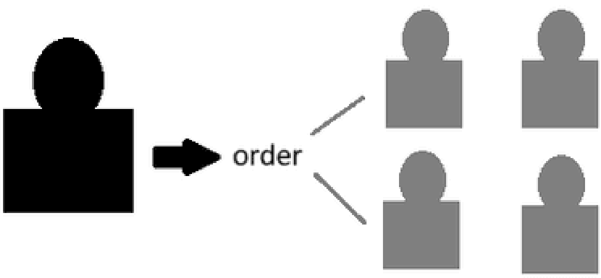
## 2.4. Role and Function of Management

- **Directors**: are senior managers who lead a particular department or division of a business. Responsibilities:
  - Setting strategy (long-term plans)
  - Reviewing the performance of managers.
  - Provide leadership
  - Making sure resources are available
- **Line Managers**: manage employees and are responsible for the team development and performance.
- **Supervisors**: are junior managers who supervise and are responsible for the employees below them in the organisational structure.

- **Staff Managers**: are specialists who provide support information. And assistance to line managers.
- The functions of managers include:
  - **Planning** – Planning is about where the business is now and where it wants to be. Once it has been decided, management must set clear objectives and an action plan.
  - **Organising** – Management will have to decide the best way of completing important tasks at the lowest possible cost to the business.
  - **Communicating -** Control and supervision of subordinates also aim to motivate workers to achieve the planned objectives.
  - **Coordinating -** Making sure that all the different parts of the business are working together to achieve the business's goals and corporate objectives.
  - **Controlling** – involves checking to make sure that the plan is working and if it would be completed in time and the required standard, and if not, then correcting it
- **Extra functions managers do:**
  - Understand the people who work for them
  - Set a good example
  - Delegate tasks
  - Treat subordinates fairly
  - communicate effectively

## 2.5. Leadership Styles

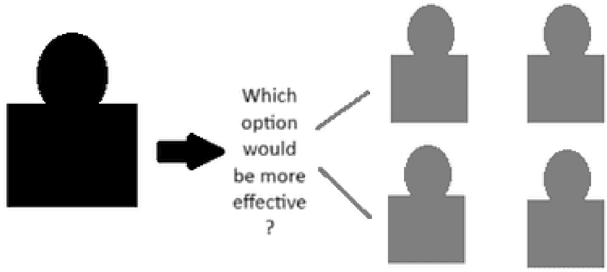
- **Leadership Styles**: are the different approaches to dealing with people and making decisions when in a position of authority.
- There are three leadership styles:
- **Autocratic Leadership:** where the manager expects to be in charge of the business and to have their orders followed. Characteristics:




  - A leader does all the decision-making
  - Don't take input from others.
  - Highly structured working environment

| Advantages | Disadvantages |
|---|---|
| Quick decision-making process | There is no opportunity for employee input into key decisions, which can be demotivating |

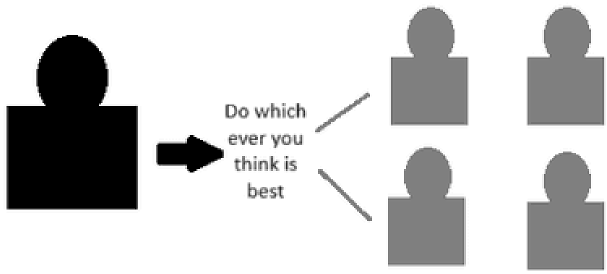
- **Democratic Leadership**: gets other employees involved in the decision-making. Characteristic:




  - Motivation is higher
  - Creativity and engagement with workers are encouraged.
  - Workers and employees are involved in decision-making.

| Advantages | Disadvantages |
|---|---|
| Better Decisions could result from consulting with employees using their ideas and experiences. | Unpopular decisions could not effectively be made using this style |

- **Laissez-Faire Leadership**: makes the broad objectives known to employees, but then they are left to make decisions and organise their work. Characteristics:




  - Workers and employees are expected to make the decisions.
  - The leader will only give guidance.
  - The leader only takes charge when necessary.

| Advantages | Disadvantages |
|---|---|
| Encourage employees to show creativity and responsibility | It is unlikely to be appropriate in organisations with a consistent and clear decision-making structure. |

## 2.6. Trade Unions

- **Trade Unions**: A group of employees who have joined to protect their interests.

**The Role of Trade Unions:**

- Negotiating with employers to improve pay and working conditions.
- Resolving conflict by negotiating a solution on behalf of its members
- Providing legal support and advice.

- Providing services for members including holiday scheme, pension scheme, insurance scheme, etc.

| Advantages | Disadvantages |
|---|---|
| Strength in numbers when negotiating with employer | It costs money to be a member |
| Improved conditions of employment. | Workers may be required to take industrial actions even if they disagree. |
| Improved environment where people work. | Trade unions can organise strikes against employers if they don't receive the pay levels and work conditions they deserve. |
| Improved benefits for members not working because of sickness, retirement, or redundancy. | Wages are likely higher - adding to business costs - when many employees are trade union members. |

## 2.7. Work of Human Resource Department

- **Recruitment and Selection**:
  - **Recruitment**: is the process of identifying that the business needs to employ someone up to the point at which applications have arrived.
  - **Employee Selection:** is the process of evaluating candidates for a specific job and selecting an individual based on the organisation's needs.
- **Wages and Salaries**:
  - These must attract and retain the right people and be sufficiently high to motivate employees.
- **Industrial Relations**:
  - There must be effective communication between representatives of management and the workforce. This may be to resolve grievances and disputes and put forward ideas and suggestions for improvements.
- **Training Programs**:
  - It involves assessing and fulfilling the training needs of employees. This should also be linked to the plan.
- **Health and Safety**:
  - The business must ensure that it complies with all the laws on health and safety.
- **Redundancy and Dismissal**:
  - This involves releasing employees, either because the business changes in some way or because the employee is not satisfactory. The business must comply with all the redundancy, dismissal and disciplinary laws.

## 2.8. Recruitment Process

1. **Analyse the exact nature of the job and duties to be undertaken.**
   - **Job analysis**: it identifies and records the responsibilities and tasks relating to a job
2. **Design a job description**:
   - **Job description**: outlines the responsibilities and duties to be carried out by someone employed to do a specific job. Several functions of a job description:
     - Given to applicants so they know exactly what the job entails.
     - Allows a job specification to be drawn up to see if they are skilled.
     - It shows if an employee is working effectively once they are employed.
   - The contents of a Job description:
     - Condition of employment salary, hours, permission, etc.
     - Training that will be offered
     - Opportunities for promotion
     - Purpose of the job
     - Main duties/addition or occasional duties
3. **Design a job specification**:
4. **Job description**: is a document that outlines the requirements, qualifications, physical characteristics, etc. For a specified job.

   **Usual Requirements:**
   - The level of educational qualification
   - Special skills, knowledge, or a particular attitude
   - Personal Characteristics
5. **Advertise the vacancy**:
   - The first stage is to decide how the post will be filled.

**Internal requirement**: is when a vacancy is filled by someone who is an existing employee of the business

| Advantages | Disadvantages |
|---|---|
| Quicker and cheaper than external recruitment. | No new ideas or experiences come into the business. |
| The reliability, ability, and potential of the person are known. | Rivalry and jealousy may arise. |
| The person is already familiar with the organisation's structure and expectations. | The quality of internal candidates might be low. |
| It can be motivating for other employees to see their fellow workers promoted. | |

**External Requirement**: when a vacancy is filled by any suitable applicant outside the business

| Advantages | Disadvantages |
|---|---|
| A more comprehensive selection of candidates. | Increased costs due to advertising. |
| Adding fresh perspective and ideas. | Additional training |
| Enhancing diversity in the organisation. | Adds a transitional period for all employees to adjust to the new |

| Advantages | Disadvantages |
|---|---|
| Finding a specialised candidate that fits the requirements perfectly. | Effects on employee morale. |
| Can help the competitiveness of the business | |
| Reduce tension between employees. | |

5. **Send out application forms to the applicants or read curriculum resumes and letters of application**.
    - Advertising job vacancies can be done in several ways:
        - Local newspapers
        - National newspapers
        - Specialist magazines
        - Online recruitment sites
        - Recruitment agencies
        - Centres run by the government
6. **Produce a shortlist from the applications for interviews and take up references**.
    - Applicants must provide a referee (someone the potential employer can contact, intending to get more information/references from).
    - Interviews are the most used form of selection. Its primary purpose is to assess in the shortest time possible:
        - Applicant's ability to do the job
        - Any personal qualities that could be beneficial or not.
        - The general character and personality of the applicant.
    - Some businesses include tasks in the selection process, such as:
        - Skill test (ability to carry out specific tasks)
        - Aptitude test (candidate's potential of learning a new skill).
        - Personality test (used if a particular type of person is required).
        - Group situation test (to show how well they work with a team).
7. **Hold interviews and selection of tasks**.
8. **Select suitable applicants and offer them the job. Reply to unsuccessful applicants**.
    - The final decision can depend on several factors:
        - Work experience
        - Education and other qualifications
        - Age
        - Internal
        - External
        - Circumstance

## 2.9. Types of Workers

- **Part-time Employees** work for less than 35 hours a week.
    - **Benefits:**
        - Work hours are flexible.
        - Easier to ask employees to work at busy times
        - More accessible to extend business opening/operating hours by working evenings or weekends.
        - It fits in with looking after children or other circumstances such as school, which means employees are willing to lower pay.
        - Reduces business cost
        - In some countries, it's easier to make part-time workers redundant.
    - **Limitations:**
        - They are less likely to seek training, as they see the job as temporary.
        - Tasks longer to recruit.
        - Less commitment to business.
        - Less likely to be promoted due to lack of experience.
        - It is more difficult to communicate outside of work.
- **Full-time Employees** work for more than 35 hours a week
    - **Benefits:**
        - Consistency of schedules and reliability
        - Loyalty - A permanent contract means the employee is more loyal
    - **Limitations:**
        - A permanent contract has to be made, a long-term commitment.
        - Full-time employees have fixed pay, regardless of the number of hours committed to work (ex, sick leave, slow work day, emergency, etc).

    **Note:** full-time employee benefits are the limitations of part-time and vice versa

## 2.10. The Importance of Training and the Methods of Training

- **Importance of training:**
    - To introduce new processes or equipment
    - Improve the efficiency of the workforce
    - Provide training for unskilled workers
    - Decrease the supervision needed
    - Improve opportunity for internal promotion
    - Decrease chances of accidents
- **Aims of training:**
    - Increase skills
    - Increase knowledge
    - Improve employee's attitudes to encourage them to accept change and raise awareness.
- There are three types of training:
- **Induction Training**: an introduction given to an employee, explaining the business's activities, customs, and procedures and introducing them to their fellow workers.

| Advantages | Disadvantages |
|---|---|
| Helps new employees settle into their jobs quickly | Time-consuming |

| Advantages | Disadvantages |
|---|---|
| Maybe a legal requirement to give health and safety training at the start | Workers are being paid while no work is being done |
| Workers are less likely to make mistakes | Delays the start of work for the employee |

- **On-the-job Training**: Occurs by watching a more experienced worker doing their job.

| Advantages | Disadvantages |
|---|---|
| The individual is given in the workplace, so there is no need to send them away. | Trainers won't be as productive because they are teaching employee |
| Ensures there is some production while training | The trainer might have bad habits and pass them on to the employee |
| Usually costs less than off-the-job training | Not recognized training qualifications outside the business |
| Training tailored to the specific needs of the business. | |

- **Off-the-job training**: Involves being trained away from the workplace, usually by specialist trainers.

| Advantages | Disadvantages |
|---|---|
| A broad range of skills can be taught | Costs are high |
| If taught in the evening, employees can work during the day | Workers are being paid but not doing any work. |
| Often uses expert trainers who have up-to-date business practices and knowledge. | Additional qualifications mean an employee's chances of leaving for another job are high. |

## 2.11. Why Reducing the Size of the Workforce Might Be Necessary

- **Workforce Planning**: establishing the workforce the business needs for the foreseeable future regarding the number and skills required.
- Reasons to reduce workforce:
  - Automation (robots replacing human jobs)
  - Falling demand for their goods or services
  - Factory/chop/office closure
  - The business might have relocated abroad
  - Businesses are being **taken over/merged,** and now there are too many workers doing the same job
- **Two ways a business can reduce the number of employees:**
  - **Dismissal**: employment ends against the employee's will, usually for not following an employment contract.
  - **Redundancy**: when an employee is no longer needed and loses their job. It's not due to any aspect of their work being unsatisfactory.
    - **Factors that decide in redundancy:**
      - Workers may volunteer and are happy to be made redundant due to finding another job.
      - Length of time employed by the business - employees might have worked long hours and expect high payments.
      - Workers who have skills that could be used in multiple departments are retained.
      - The worker's employment history- whether they are punctual, good at their job, etc.
      - Which departments need to lose, and which need to retain workers

**Extra information:** workers can retire (get old and want to stop working) and resign (find another job), but it's through the employee's will in those two cases.

## 2.12. Legal Controls Over Employment issues

The most important employment issues affected by legal controls are:

- **The Contract of Employment**: A legal agreement between an employer and employee, listing the rights and responsibilities of workers.
  - **Impact on Employers and Employees:**
    - Both know what is expected from them.
    - Provides security of employment for employee
    - If the employee does not meet the condition of the contract, then legal dismissal is allowed.
    - If an employee fails to meet the conditions of the contract, then the employee can seek legally binding compensation.
- **Unfair Dismissal**: when an employer ends a worker's employment contract for a reason not covered by the contract.
- **Industrial Tribunal**: a law court (legal meeting) judges disagreements between companies and their employees.
  - **Impact on Employer and Employee:**
    - The Employer must have an accurate record of a worker's performance if they want to claim that the employee has broken the contract before dismissing them.
    - Employees have employment security — as long as they fulfil their contract or are not made redundant.
    - Allowed employees to take their employer to an industrial tribunal if they felt like they weren't being treated fairly, and they could get compensation if it were found to be true.
    - It makes businesses less likely to mistreat employees.

- **Protection against discrimination** (due to unfair reasons such as gender, race, colour, etc.).
  - **Impact on Employers and Employees:**
    - Employees have to be careful in wording advertisements for a job.
    - Applicants must be treated equally, or the business will be prosecuted and fined.
    - Employees must all be treated equally, regardless of gender, disability, colour, etc.
    - When businesses recruit and promote staff on merit alone, it helps to increase motivation.
- **Laws of health and safety at work**, such as:
  - Protect workers against 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.
  - **Impact on employers and employees:**
    - Cost to the employer of meeting the health and safety regulations.
    - Time needs to be found to train workers in health/safety precautions.
    - Workers feel 'safer' and more motivated at work.
    - Reduce accident rates and the cost of compensation for workers injured at work.
- **Legal minimum wage and its impact on employer and employee:**
  - It should prevent strong employers from exploiting unskilled workers.
  - As many unskilled workers receive higher wages, it will encourage them to be more productive.
  - It will encourage people to seek work.
  - Low-paid workers will earn more and have higher living standards, making them afford to buy more.
  - Increase business costs
  - Some employers will not be able to afford these wage rates.
  - Higher-receiving workers may ask for higher pay to keep the exact difference between them, increasing business costs.

## 2.13. Internal and External Communication

- Effective Communication is important so that the information sent in the message is received, understood, and acted upon as it should be. Otherwise, lack of communication can lead to severe consequences.
- There are two types of communication in businesses:
  - **Internal Communication**: communication between employees of the same business.
  - **External Communication**: communication between the business and other businesses and individuals.
- External communication has to be especially efficient because it establishes the image and the efficiency of a business
  - i.e. if a company communicates inefficiently with their suppliers, they might receive the incorrect materials
- **Effective communication involves:**
  1. The **transmitter**/sender sending a message to pass on information
  2. A **medium of communication** – the method for sending a message (i.e. e-mail, phone, etc)
  3. The message being sent to the **receiver**
  4. The receiver confirms that the message has been received and responds to it (**feedback**)
- There are two types of communication:
  - **One-way communication** – where the receiver cannot reply to the message (i.e. posters)
  - **Two-way communication** – where the receiver can respond to the message could be just confirmation that the message was received (e-mail)

The methods of communication include:

- **Verbal Methods**: The sender speaks to the receiver (i.e., through meetings, telephone, or video conference)

| Advantages | Disadvantages |
|---|---|
| Information is given out quickly & an efficient way to communicate with many people. | If talking to many people, it's hard to tell whether everyone got the message. |
| Opportunity for immediate feedback | It is unsuitable for accurate messages, and a permanent message record is needed. |
| The speaker's body language reinforces the message. | |

- **Written Methods**: the sender creates e-mails, memos or letters, including the use of Information Technology

| Advantages | Disadvantages |
|---|---|
| Message can be referred to in the future as "hard evidence." | It might lead to too many e-mails and 'information overload.' |
| Easy to explain complicated messages | Two-way communication is difficult |
| It can be copied and re-sent to many people | It is hard to check if the message has been received |

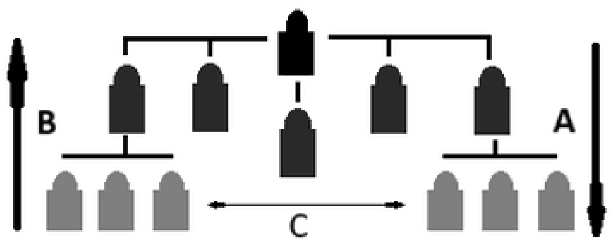
- **Visual Methods**: The sender uses diagrams, charts, videos, PowerPoints

| Advantages | Disadvantages |
|---|---|
| If information is presented more appealingly, people will be more interested in it. | No feedback and needs other methods of communication to go with it |
| It can be used to make written messages clearer, to illustrate the point | Graphs and charts may be difficult for people to understand, and the message may be misunderstood |

## 2.14. Methods of Communication

- **Formal communication**: when messages are sent through established channels using professional language.
- **Informal communication**: when information is sent and received casually using everyday language.

### The Direction of Communication




- **Arrow A** shows **downward communication** - where messages are sent from managers to subordinates. Used for instructions or statements, no feedback.
- **Arrow B** shows **upward communication** - when messages or feedback can be passed from subordinates to managers.
- **Arrow C** shows **horizontal communication** - when people at the same level in an organisation communicate. Ideas and info can be shared. Conflict can happen.

## 2.15. Demonstrate an Awareness of Communication Barriers

### Communication Barriers

- **Communication Barriers** – Factors that stop effective communication of messages.

### Communication Barriers and How Can They Be Reduced or Removed

- **Problems with the sender**:
  - Poor attitude and body language
  - Unclear message
  - Message too long
  - Sent to the wrong person
- **Overcome by**:
  - The sender should ensure that the message uses language which can be understood.
  - The sender should make the message as straightforward as possible.
  - The sender should ensure the message is delivered to the right person.
  - The message should be brief, with the main points to be understood.
- **Problems with the medium**:
  - Too many people pass on the message.
  - The message may be lost.
  - Wrong channel used
  - Technical break down
- **Overcome by**:
  - Insist on feedback; if none is given, the sender can assume the message is lost.
  - The sender must select an appropriate channel to avoid problems.
  - Shortest possible channel to avoid problems
  - Other forms of communication should be available.
- **Problems with the receiver**:
  - Lack of trust
  - Poor attitude
  - Poor listener
- **Overcome by**:
  - The message should be emphasised, and receivers should be asked for feedback to ensure understanding.
  - If trust is not between sender and receiver, then the sender should try to build that trust, or perhaps another sender who is respected by the receiver could be used.
- **Problems with feedback**:
  - Not sent
  - Unclear
  - Not asked for
- **Overcome by:**
  - Perhaps no feedback was asked, or the method of communication required no feedback, so another technique that may allow feedback should be used.
  - Direct lines of communication should be available.

# 3. Marketing

## 3.1. The Role of Marketing

**Marketing Department:**

- **Marketing**: Identifying and satisfying customer needs and satisfying them profitably.
- **Customer**: a person, business or other organisation which buys goods or services from a business.
- The different marketing department sections:
  - **Sales Team**: responsible for the sales of products. If a product is exported, it may be called the export team.
  - **Market Research**: responsible for discovering customers' needs, market changes and the impact of competitors' actions. This report will be used in decision-making, research, developing new products, price levels, etc.
  - **Promotion Section**: deals with organising the advertising for products. Arrange for advertisements and have a market budget.
  - **Distribution:** transports the products to the market.
- **The Role of Marketing:**
  - **Identify customer needs**: this will be done via 'Market Research'. It will influence the development of a

product, its price, and the sales technique.
- A good marketing department should also be able to anticipate changes in customer needs (i.e. due to advancements in technology)
- Find new trends or gaps in the market with potential.

- **Satisfy Customer Needs**: selling the exact product customers want for a price they are willing to pay.
- **Maintaining customer loyalty**: maintaining close customer relationships to discover the product's expectations and changes needed to be made. It's cheaper for businesses to keep existing customers than to attract new ones.
  - **Customer Loyalty**: existing customers continually buy products from the same business. It is achieved by always satisfying customer needs.
- **Building customer relationships to gain information about customers**
  - ~~**Customer Relationships**~~: communicating with customers to encourage them to become loyal to the business and its products.
  - Through customer relationships, changing needs can be understood. Research information can be applied to make effective marketing through these relationships.
- **Anticipate changes in customer needs –**
  - Identify new trends in customer demands or gaps in the market.

- **When the marketing department succeeds in identifying customer requirements and future needs, it will enable the business to:**
  - Raise customer awareness of a product or service of the business
  - Increase in revenue and profitability
  - Increase or maintain market share
  - Maintain or improve the image of the product or business
  - Target a new market or market segment
  - Enter a new market at home or abroad.
  - Develop new products or improve existing products.

## 3.2. Market Changes

- Markets change because **consumer spending patterns change**; this might be due to the following:
  - **Trends and Fashions Change**: for some time, it might be fashionable to have a specific product (i.e., Fidget Spinner), but a month later, no one bought them
  - **Advancement in Technology**: new products provide the latest technology so older versions (i.e., iPads or computers) don't have high sales
  - **Unemployment/Wages**: Economies with high unemployment rates/low wages will not have increased sales of expensive products
  - **Ageing Population**: different ages are interested in other products (i.e. anti-ageing creams)
- Businesses have to keep up with customers' changing needs to stay relevant and maintain their customer base/loyalty. The competitiveness of a business is majorly affected by its ability to respond to any changes in the market.

Some markets have become **more competitive** because:

- **Globalisation**: products are sold all over the world
- **Transportation**: it is cheaper, quicker, and easier to send products around the world now
- **Internet/e-commerce**: customers can now search for products or services and buy from somewhere else around the world
- **The ways businesses respond to changing spending patterns and increased competition:**
  - Keep improving its existing products
  - Bring out new products to keep customer's interest
  - Keep costs low
  - maintain good customer relationships

## 3.3. Market Types

- **Market**: the total number of customers, potential customers and other sellers of a product/service.
- **There are two types of markets:**
  - **Mass Market**: where there is a vast number of sales of a product type.

| Advantages | Disadvantages |
|---|---|
| Total sales are very high | Abundant competition |
| Can benefit from economies of scale | High costs of advertisement and promotion |
| Opportunities for growth (large sales) | Standardised products or services, so it may not meet the specific needs of all customers |
| There are many variations of products, so the risk is spread. | |

- **Niche Market**: a SMALL (usually specialised) segment (part) of a mass market. Specialised and sold by small businesses that would find it difficult to compete in a mass market (ex, a business specialised in scuba diving gear)

| Advantages | Disadvantages |
|---|---|
| Avoid competition with big businesses | Small – limited sale potential |
| Customers' specific needs are focused, leading to high levels of customer loyalty and good customer relations. | Usually, they specialise in just one product; if the product has low demand, it will fail. It would require businesses to have multiple products to spread risks. |

## 3.4. Market Segmentation

- **Market Segmentation**: an identifiable subgroup of a whole market where consumers have similar characteristics or preferences.
- A market can be segmented by:
  - **Age**
  - **Socio-Economic** group – grouping people according to how much money (income) they make
  - **Region/Location** – where people live (ex, people who live in wet areas will buy more waterproof clothing than those who live in dry areas)
  - **Gender** – men's and women's products differ
  - **Lifestyle** – ex: how many children a person has, religion, habits, etc.
  - **Use of the product** - products may be used for different uses (ex, cars for business use and domestic use, each the same product but can be marketed differently)
- **Benefits of Market Segmentation**:
  - You can use it to sell more products, creating different variations for different groups.
  - A more effective marketing strategy can be placed (as the characteristics of consumers are known), resulting in an increase in sales.
  - Identifying a market segment that is not having its needs fully met increases the opportunity for increased sales.
  - Making marketing expenditure cost-effective by producing a product that can closely meet the needs of those customers and targeting its marketing efforts to that group only.
- **Which method of segmentation should be used depends on factors such as:**
  - Detailed analysis of the market and the 'size' of each potential segment in terms of consumers and likely sales.
  - Company image and brand image - 'high-tech ' businesses may not want to produce innovative, high-quality products for low-income consumers.
  - For example, the cost of entering each segment is a specially designed product and advertising campaign.

## 3.5. Market Research

- **Market Research**: Gathering information about consumers' needs or preferences in a market
- **The roles of market research:**
  - Identify demand for the product and how much they are willing to pay.
  - Identifying the target audience is the most effective way to promote to these customers.
  - To measure the competitiveness of the market and the best way to compete with it.
- There are **two types of businesses**:
  - **Product-Oriented Business**: a business that focuses mainly on the product, disregarding market needs and wants. Often, it produces necessities for living, such as agricultural tools or fresh food.
    - It may not have a brand name.
    - Producers' main concern is price and quality.
    - Risky due to the large market and many competitors.
  - *A market-oriented business is a business that focuses on market research and finding out what the customer wants BEFORE a product, such as clothing or electronic devices, is developed.*
    - Better able to survive because of more adaptability to changes in customer taste and trends.
    - Takes advantage of new market opportunities.
- **Market Research Methods**:
  - Quantitive information (quantity related)
  - Qualitative information (where opinion or judgement is necessary).
  Can be gathered through:
- **Primary Research**: Gathering ORIGINAL data by directly contacting existing customers/potential customers.

| Advantages | Disadvantages |
|---|---|
| Up-to-date and relevant | Expensive in both time and money |
| Usually planned and carried out by people who want to use the data first-hand. | Not available immediately |
| It is most effective when used for a specific problem. | |
| Not available to business | |

- **Process:**
  - Purpose of market research
  - Decide on the most suitable method of market research
  - Decide the size of the survey and who is going to be asked.
  - Carry out the research
  - Analyse the data and results
  - Produce a report of the findings
- Methods of Primary Research:
  - **Questionnaires**
    - They may be conducted face-to-face, by telephone, or online.

| Advantages | Disadvantages |
|---|---|
| Detailed qualitative information can be gathered. | If questions are not well-thought-out, answers may mislead the business, as there may not be accurate answers. |
| The customer's opinion can be obtained. | Lots of time and money are needed. |
| Online surveys may be cheaper and make it easier to collate the results. | Collating and analysing data also takes a long time. |

| Advantages | Disadvantages |
|---|---|
| They can be linked to prize draws and encourage people to fill them. | |

- **Interviews**: A person will interview another person and ask questions.
  - Advantages:
    - The interviewer will be able to explain the questions and clear confusion.
    - Detailed information about the interviewee can be gathered.
  - Disadvantages:
    - The interviewer may lead the interviewee to answer in a certain way.
    - It is time-consuming and Expensive.
- **Focus Groups**: collect opinions and feedback from a group of people about a specific product, concept, or service.

| Advantages | Disadvantages |
|---|---|
| Provide detailed information | It is time-consuming and expensive if done by a specialist market research agency. |
| Interacting between members can help businesses understand the reason for peoples' opinions. | The discussion could be based on some people being influenced by the opinions of others. |
| Quicker and cheaper than individual interviews. | A few people can dominate it, so researchers must have experience dealing with this. |

- **Sampling:** A group of people who are selected (randomly) to respond to a market research exercise (i.e. questionnaire). 2 standard methods of sampling:
  - A **Random Sample** is when people are selected randomly as a source of information for market research.
    - Advantage: Everyone has an equal chance to be picked, but not everyone in the population may be a product consumer.
  - A **Quota Sample**: People are selected based on specific characteristics. They can find out the views of a specific group.
    - Advantage: can find out the views of these specific groups.
- **Secondary Research**:
  - Information that has already been collected and is available to others

| Benefits | Limitations |
|---|---|
| It is cheaper than primary as research has already been done by others | You do not get specific results for a particular product or service; you get broad results |

| Benefits | Limitations |
|---|---|
| There is some information (i.e. economic forecasts or population size) that can't be obtained by primary research | Data may be outdated or incorrect as others collected it |
| | It might not have the specific information |

- **Internal Sources** of secondary data – within the firm's own records:
  - Sales department records, price data, customer records, sales reports, etc.
  - Opinions of distribution and public relations personnel
  - Finance department.
  - Customer service department
- **External Sources of Secondary Data:**
  - **Government Statistics**: a detailed source of general information (ex: population and its age structure)
  - **Newspapers**: useful articles about the general economy state
  - **Trade Association**: information about business in the industry
  - **Market Research Agencies**: specialist agencies researching on the company's behalf; the commission is paid.
  - **Internet**: easily accessible source. Paper-based sources can also be found.
- Regardless of which type of research a business chooses to use, the accuracy of the research data depends on the following:
  - How **carefully** the **sample** was drawn up
  - How the questions in questionnaires/interviews were **phrased** to ensure **honest answers** were given.
  - The **sample itself** and its **size**. By using **quota** sampling, you might get more reliable results.
  - **The bias** – some secondary research will be biased (i.e. articles in newspapers), which means the information might be unreliable
  - **Age of the information**: older data might be inaccurate.
- **Presentation of data from market research:**
  - Tables or tally chart
  - Pie Chart
  - Diagram
  - Bar chart
  - Line graph

## 3.6. Marketing Mix

- **Marketing Mix**: a term used to describe all the activities that go into marketing a product or service.
- The marketing mix can be summed up as the 4 Ps:
  - **P**roduct - applies to the product or service. Design, features and quality.
  - **P**rice - the price at which the product is sold, comparisons between prices of competitors.
  - **P**lace - channel of distribution that is selected.

- Promotion - how the productivity is advertised and promoted.
- **You should always mention the 4 Ps when answering questions about Marketing Mix!**

## 3.7. Product

- Some products are sold to consumers, and some to other businesses.
- They are usually grouped:
  - **Consumer goods**: bought by consumers for their own use. Can be perishable goods such as food or long-lasting such as furniture.
  - **Consumer services**: services bought by consumers for their own use. Ex. Cleaners
  - **Producer goods**: there are goods that are produced for other businesses' use to help with the production process. Ex. Trucks
  - **Producer services**: services that are produced to help other business. Ex. Accountants.
  - Identifying the type of product is important as it decides how the product would be advertised/marketed and developed.
- Points to consider about choosing product:
  - Satisfying existing needs and wants of consumers
  - Not be expensive to produce.
  - New and original idea
  - Unique selling point
  - Capable of stimulating new wants from their consumers.

### Development of New Products:

1. Generate ideas
2. Select the best idea for further development
3. Decide if the company will be to sell enough for the product to be a success.
4. Develop a prototype
5. Launch the product in one area to test the market
6. Go to a full launch of the product to the whole market.

| Benefits | Drawbacks |
|---|---|
| USP – a unique selling point: a special feature about a product that differentiates it from its competitors' product. | Costs of carrying out market research and analysing the findings |
| Diversification | Cost of producing trial products, including waste materials |
| Allows businesses to expand into new and existing markets | Brand image is damaged if the product fails to meet consumer demand |
| | The lack of sales if the target market is wrong |

### Importance of Brand Image

- **Brand name**: the unique name of a product that distinguishes it from other brands.
- **Brand loyalty**: when consumers keep buying the same brand again instead of choosing a competitor's brand.
- **Brand image**: an image or identity given to a product which gives it a personality of its own and distinguishes it from its competitors.
- Good branding includes:
  - Brand name
  - Higher quality than unbranded products.
  - Unique packaging
  - Brand loyalty
  - Assured quality
  - Creates a brand image associated with consuming the product.

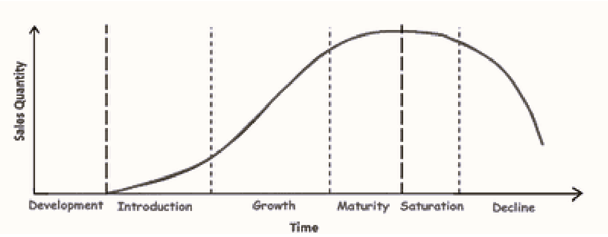
### Role of Packaging

- **Packaging**: the physical container or wrapping for a product. 2 functions - protect and promote product
  - Protects the product and makes it easier to transport
  - Eye catching
  - Carries information about the product
  - Promotes brand image

### Product Life Cycle (PLC)

- **Product life cycle:** describes the stages a product will pass through from its introduction, though its growth until it is mature, and then finally its decline.

1. **Development**: First, the product is developed. The prototype will be tested in the market before its launch. There are no sales during this time.
2. **Introduction:** Then it is introduced or launched in the market. Sales are often slow. No profit made as development costs are not yet covered.
3. **Growth**: The product gains more sales. Advertising is changed to persuade and encourage customer loyalty. Prices reduced due to competitors and profit starts to be made.
4. **Maturity**: sales increase slowly. Competition intense and advertising is used to maintain sales growth and profit is at its highest.
5. **Saturation**: sales have stabilised at their highest point. Competition and advertising is high and stable, but profit starts to fall as sales static and prices are reduced to be competitive.
6. **Decline**: sale of product starts to decline as new products enter, or it has lost its appeal. Product is withdrawn from market and sales, prices and advertising low until it stopped.



### How Stages of PLC Influence Marketing Decisions

- Introduction –
    - Product – newly launched product
    - Price – price skimming or penetration pricing
    - Place – limited range of exclusive shops (if price skimming is used)
    - Promotion – informative advertising
- Growth
    - Product – remains the same
    - Price – raise prices is penetration pricing was used
    - Place – increase the number of outlets, e-commerce
    - Promotion – establish a strong brand identity through promotional activities.
- Maturity/Saturation
    - Product – plans for product changes begin
    - Price – lower prices to competitive
    - Place – full range of distribution channels used
    - Promotion – sales promotion techniques to encourage repeat purchases
- Decline
    - Product – changes made to extend the life cycle
    - Price – lower prices
    - Place – sell through low-cost outlets
    - Promotion – re-launch the product as an extension strategy

### Extending Product Life Cycle:

- **Extension strategy**: a way of keeping a product at the maturity stage of the life cycle and extending the cycle.
- Introduce new variations into the original product
- Sell into new markets
- Make small changes to the product's design, cover, colour
- Sell through additional retail outlets
- Introduce a new, improved version of the old product
- Use a new advertising campaign

## 3.8. Pricing

- The price chosen may not be related to the cost of manufacturing but rather to what consumers are willing to pay, the product's value, and the brand image.
- The business must constantly monitor what its competitors charge for their products to ensure its prices remain constant.
- **A business can adopt new pricing strategies for:**
    - To break into a new market
    - To increase market share
    - To increase profits
    - To make sure all costs are covered and a particular profit is earned

### The Main Methods of Pricing

There are five main types of pricing methods:

- **Cost-plus Pricing:** the cost of manufacturing the product plus a profit mark-up. It involves:
    - Estimating how many of the products will be produced.
    - Calculating the total cost of producing this output.
    - Adding a percentage markup for profit.
    - Total cost /output + % markup.

| Benefits | Limitations |
|---|---|
| The method is easy to apply. | Businesses could lose sales if the selling price is higher than competitors. |
| Different profit markups could be used in different markets. | A total profit will only be made if sufficient product units are sold. |
| Each product earns a profit for the business. | There is no incentive to reduce costs. |

- **Competitive Pricing:** When the product is priced in line with or just below competitors' prices to try to capture more of the market.

| Benefits | Limitations |
|---|---|
| Sales are likely to be high due to realistic level prices. | High-quality products must be sold at higher prices to give them a high-quality image. |
| Avoids price competition | If cost is high and sales are low, competitive prices can lead to loss. |
| Often used when it is difficult for consumers to tell the difference between the products of different businesses. | Detailed research will be needed to determine these prices, which costs time and money. |

- **Price Skimming:** setting the price for a new product on the market. A product is usually a new invention or a new development of a product.

| Benefits | Limitations |
|---|---|
| It can help establish the product as good quality. | High prices may discourage some customers from buying it. |
| If production is unique, a high price may lead to profit, and the price may be reduced. | High prices and profitability may encourage competitors to enter. |
| High research and development costs can be rapidly recovered from profit made. | |

- **Penetration Pricing:** when the price is set lower than the competitors' prices to enter a new market.

| Benefits | Limitations |
|---|---|

| Benefits | Limitations |
|---|---|
| often used for newly launched products to create an impact on customers. | Sold at a low price, therefore, profit per unit may be low. |
| Ensure sales are made and the new product enters the market. | Customers may 'get used' to low prices and reject the product if the price is raised. |
| Market share should build up quickly. | It might not be appropriate for products that have a reputation for quality. |

- **Promotional Pricing**: when a product is sold at a low price for a short period of time. To increase short-term sales.

| Benefits | Limitations |
|---|---|
| Useful for getting rid of unwanted inventory that will not sell. | Revenue will be lowered because the price of each item is reduced. |
| Help renew interest in a product if sales are falling. | This might lead to price competition with competitors. |

- **The impact of psychology on price decisions-**
  - High prices for high-quality products can be purchased for status symbols.
  - When a price is lower than a whole number, it creates the illusion of being cheaper.
  - Supermarkets may choose low prices for products purchased regularly.
  - Repeat sales are often made to reinforce consumers' perceptions of the product.
- **Using different pricing methods for the same product-**
  - **Dynamic pricing**: When businesses change product prices, usually when selling online, depending on the level of demand, for example, Aeroplane tickets.
  - There are ethical issues with some dynamic pricing; using technology, businesses can track customers' buying history and then charge accordingly.

### Price Elasticity of Demand

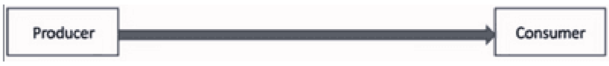
- **Price Elasticity of Demand**: How responsive is a demand for a product to a change in price?
- PEDs are affected by the no of substitutes available
- **Price-elastic demand** is when a product is **very responsive** to a change in demand. The % change in demand is GREATER than the % change in price, i.e., prices increase by 5%, but sales decrease by 10%.
  - Therefore, the business's revenue would be falling with a price increase. Businesses must find another way to increase demand without using the product's price.
- **Price-inelastic demand** is when the product is **not very responsive** to change in demand. The % change in demand is LESS than the % change in price.
  - This means you can increase the price of the product a lot without the demand changing (i.e., oil & petrol because people have to buy it)

## 3.9. Place (Distribution Channels)

- Products should be available when and where customers need them
- Wrong place, low sales and profits
- The place must be convenient for consumers
- **Distribution Channel**: is how a product is passed from the place of production to the customer.

**There are four main distribution channels:**

- **Manufacturer sells products directly to consumers** (i.e. car components to car factories).
  - This channel is most common with business-to-business transactions.




| Benefits | Limitations |
|---|---|
| Very simple | It is impractical because consumers don't usually live near factories |
| Suitable for products that are sold straight out of factories | Not suitable for products that can't be sent quickly by post, especially if they're perishable or easily breakable goods. |
| There is a lower price for consumers (cuts retailer) | It is not cost-effective, as sending products by post is expensive |
| Products can be sold by mail order catalogue or via the internet. | |

- Producers sell to retailers, who sell to consumers (i.e., farms selling food to big supermarkets).
  - This channel is most common where retailers and large such as supermarkets or the product is expensive, Ex. furniture or jewellery.


| Benefits | Limitations |
|---|---|
| Manufacturer sells lots of stock to retailer | There is no direct contact with customers, which makes It hard to create customer loyalty. |
| Cheaper transportation costs because all products go to one place | Price is often higher than 'direct selling' as the retailer has to cover its costs and make a profit |
| Lower storage costs for the manufacturer | |

- **Producers sell to wholesalers**, who buy in bulk, divide their stock into smaller quantities, and sell them to retailers.

Producer → Wholesaler → Retailer → Consumer

| Benefits | Limitations |
| --- | --- |
| Reduces storage costs for small retailers because small quantities are sold | More expensive to buy from a wholesaler than from a manufacturer |
| Small quantities, so transport costs are low | A wholesaler might not have all the products a retailer wants |
| Wholesalers can give feedback on what sells well to producer | It takes longer to get to the consumer |
| | Huge gap between the manufacturer and the customer |
| | Consumer prices may be higher than direct selling, as retailers and wholesalers need profit. |

- A manufacturer hires an agent (person or business) that will sell products on behalf of the manufacturer.
  - Agent: an independent person or business appointed to deal with sales and distribution of a product or range of products.

Producer → Agent → Wholesaler → Retailer → Consumer

| Benefits | Limitations |
| --- | --- |
| Agents know the most profitable places & prices to sell in other markets that manufacturers may not know. | Manufacturers lose much control over how the product is sold to customers. |
| Agents will provide advice on the best ways to survive new markets. | Higher costs for consumers, as agents will need compensation for expenses. |
| Gives the manufacturer some control over the way product is sold. | |

### Methods of Distribution

- **E-Commerce**
  - Selling of goods and services through the internet

| Benefits to the business | Problems to business |
| --- | --- |
| Cheaper | Website must be maintained |
| Customers are encouraged to buy in bulk | High distribution costs |
| Business-2-Business e-commerce is cheaper | No direct contact |
| Wider options for customers, brand image and loyalty | Returns – higher costs |
| | A stock system will be needed. |

| Benefits to consumers | Problems for consumers |
| --- | --- |
| No need to go out | Internet needed |
| Wide options | High chances of fraud and theft |
| Easy Comparison | Products can't be physically examined |
| Payment through net banking | No direct contact |
| Easy access to imported goods | |
| Low prices | |

- Other methods include:
  - Department stores
  - Discount stores
  - Chain stores
  - Superstores
  - Independent retailers
  - Direct sales
  - Supermarkets
  - Mail order

### Selecting Which Distribution Channel to Use

- Type of product
- Is it technical?
- How often is it purchased?
- How expensive is it?
- How perishable is it?
- Where are customers located?
- Where do competitors sell?

## 3.10. Promotion

- **Promotion**: where marketing activities aim to raise awareness of a product or brand by generating sales and helping create brand loyalty. Includes the following:
  - **Advertisement:** Involves 'above-the-line' promotions. Ex. TV, Social media. Newspapers, etc.
  - **Sales Promotion:** Involves 'below-the-line' promotions. Used for short periods of time to reinforce the above-the-line promotions. Ex. Money-off coupons, gifts, protect placements in programmes or newly released films.

### Aims of Promotion

- To raise awareness about a firm's products
- Encourage customers to make a purchase
- Increase sales
- Introduce new products in the market
- Create brand image
- Improve the company's image
- Compete with competitors

### Advertising

- **Advertising**: paid-for communication with potential customers about a product to encourage them to buy it.
- **There are two types of advertisements:**
  - **Informative Advertisement**: where advertising or sales promotion emphasises giving complete information about the product. (i.e. the benefits of the product)
  - **Persuasive Advertisement**: advertising or promotion trying to persuade consumers that they need the product and should buy it.
    - The advertising process:
      1. **Set objectives** of advertising to capture new market and increase market share
      2. **Decide the advertising budget**-predict how much sales will be in the future, and spread a certain percentage (between 2% to 10%), or set by how competitors are spending, or simply what the business can afford to spend.
      3. **Create an advertising campaign**- the target audience and objective must be kept in mind.
      4. **Selecting the media to use** the target audience will decide the media, how often AD appears, and should be cost-effective.
      5. **Evaluate the effectiveness of the campaign**- if sales or brand image improved.

### Types of Advertising Media

- **Television**
  - Examples of suitable products/services are food products/drinks, cars, and household products.

| Advantages | Disadvantages |
|---|---|
| It will go out to millions of people. | Very expensive |
| Can be shown in a favourable way (Attractive). | Young consumers often download films/movies and don't watch many television programmes. |
| Reaches the most significant number of consumers and reaches the target audience by showing AD after specific programmes. | |

- **Radio**
  - Examples of suitable products or services: Local services or events, e.g., local shops or car showrooms.

| Advantages | Disadvantages |
|---|---|
| It's cheaper than TV. | It cannot put across a visual message. |
| Reaches a large audience. | It is pretty expensive compared to other methods. |
| Often, it uses memorable songs or tunes so that the AD can be remembered. | The advert needs to be remembered because there is no hard copy. |
| | It's not as broad an audience as television. |

- **Newspaper**
  - Examples of suitable products or services: Local products and events in the local newspaper.

| Advantages | Disadvantages |
|---|---|
| Can be selected to target a particular group | Often, it is black and white; therefore, it is not attractive to the eye. |
| A large number of people buy/read national newspapers. | Many young People do not read/purchase traditional newspapers. |
| Local newspapers are cheap and, therefore, cost-effective. | |
| Adverts are permanent and can be cut and kept. | |
| A lot of information can be put in the advert. | |

- **Magazines**
  - Ex of suitable products/services: Feature in specialist magazines, gold equipment, medical equipment.

| Advantages | Disadvantages |
|---|---|
| An effective way to reach the target population is if there are specialist magazines. | Published once a month or week. |
| Magazine adverts are in colour, thus attractive. | They are more expensive than newspapers. |

- **Posters**
  - Ex of suitable products/services: Local events, products purchased by a large population.

| Advantages | Disadvantages |
|---|---|
| Permanent | It can be easily missed. |
| Relatively cheap | No detailed information can be included |
| Potentially seen by everyone passing | |

- **Cinemas, DVDs, Blu-ray discs:-**
  - Examples of suitable products/services: Coca-Cola (make sure to boycott ;) ).

| Advantages | Disadvantages |
|---|---|
| Shows visual image of product positively. | Scene by only a limited number of people. |
| Relatively low cost. | |

| Advantages | Disadvantages |
|---|---|
| It can be effective if the target audience goes to see a particular film. | |

- **Leaflets**
  - Examples of suitable products/services: local events and retail outlets (can contain vouchers).

| Advantages | Disadvantages |
|---|---|
| Cheap | It may not be read |
| Give out on the street to a wide range of people. | Direct mail, also called 'junk mail,' can be annoying and prevent customers from buying. |
| Direct mail (delivered door to door) | |
| Sometimes contains money-off-vouchers. | |

- **Internet**
  - For example, suitable products/services are familiar, e.g., books, clothes, electronics—services such as train information, ticketing, insurance, etc.

| Advantages | Disadvantages |
|---|---|
| A large amount of information can be placed. | Internet searches may not highlight the website, and it could be missed. |
| A vast number of people can see it | Some countries have limited access to the internet. |
| Orders can be made instantly via the website. | A lot of competition. |
| Direct mail via email is cheap. | Security issues can discourage customers. |

- ~~**Other forms of publicity:**~~
  - Ex of suitable products/services: shops can use bags as a form of advertising, billboards on the street.

| Advantages | Disadvantages |
|---|---|
| Very cheap methods of advertising, e.g. T. Shirt delivery vehicles and bags can be worn, and by walking around, it can be an advertisement itself. | Customers may not see it in the target market. |

## Sales Promotion

- **Sales Promotions**: when incentives (i.e. special offers/sales) are aimed at consumers to achieve a short-term increase in sales.

## Types of Sales Promotion

- **Price Reductions**
  - Includes coupons
  - Linked to loyalty cards
  - Reduced prices of products at certain times of the year.
- **Gifts**
  - Small gifts to encourage purchases
  - The main aim is to get customers to buy at regular intervals
- **BOGOF (Buy One, Give One Free)**
  - Multiple purchases are encouraged
- **Competitions**
  - Packaging can allow customers to enter competitions
  - Encourages sales
  - High prices
- **Point of sale display and demonstrations**
  - Place where the product is sold
  - Special display
- **After-sales services**
  - For expensive products, good after services encourage consumers to buy their products.
- **Free samples**
  - Can be handed out to shops to encourage sales
  - Maybe delivered at home
- **Product placement**
  - Featured in television programmes, movies or music videos.
  - It is expensive to pay for placement and can have a negative effect if the image is unattractive to customers.

## Advantages of Sales Promotion

- It can be used at the times of year when sales are low.
- Encourages new customers to try an existing product.
- Encourages customers to try a new product.
- Increase customer loyalty by encouraging existing customers to buy in greater quantities.
- Encourages customers to buy their product instead of competitors.

## Marketing Budget

- The marketing budget is the financial plan for marketing a product/brand for a period of time.
- When deciding which type of promotion to use, marketing budget is an essential factor
- Businesses will need to compare the cost of advertising and the increase in expected sales. Cost-effectiveness if important.
- This is where small businesses struggle compared to big businesses because their budget is much smaller.

## Factors Influencing Type of Promotion

- Stage of PLC
- Nature of product
- Cultural issues involved in international marketing

- The media used must depend on the following:
  - Literacy rate
  - Poverty rate
  - Availability of radio and cinema
  - Nature of target market

### Public Relations and Sponsorship

- It is concerned with promoting a good image of the brand
- Ways to increase public awareness:
  - Sponsor events linked with good causes
  - Donate to charities.
- All these activities are used to raise the public's awareness of the company and its product and increase their chance of choosing their product over competitors.

## 3.11. Technology and Marketing Mix

### E-Commerce

- It is the 'online' buying and selling of goods and services using computer systems linked to the internet and apps.

| Benefits to the business | Problems to business |
|---|---|
| Cheaper | Website must be maintained |
| Customers are encouraged to buy in bulk | High distribution costs |
| Business-2-Business e-commerce is cheaper | No direct contact |
| Wider options for customers, brand image and loyalty | Returns – higher costs |
| | A stock system will be needed. |

| Benefits to consumers | Problems for consumers |
|---|---|
| No need to go out | Internet needed |
| Wide options | High chances of fraud and theft |
| Easy Comparison | Products can't be physically examined |
| Payment through net banking | No direct contact |
| Easy access to imported goods | |
| Low prices | |

### How technology influences the marketing mix:

- **Social Media Marketing**: a form of internet marketing that involves creating and sharing content on social media networks to achieve marketing goals.
- **Viral Marketing**: when consumers are encouraged to share information online about a business's product.
- **Product**: may change to respond to new technology.
- **Promotion**: social media marketing and viral marketing can be used to promote.
- **Price**: the internet allows businesses to gather information about customer purchasing habits, which means dynamic pricing can be used to increase revenue.
- **Place**: The widespread spread of online purchasing and e-commerce. Can create new opportunities.

### Use of the Internet and Social Media Network for Promotion

- Social media for promotion:

| Opportunities for Advertising on Social Media | Threats of advertising on social media |
|---|---|
| Target specific demographic group | It can alienate customers if they find the adverts annoying. |
| Guarantee it reaches customers | Businesses have to pay for advertising if using pop-ups. |
| Speed in response to market changes: Information can be uploaded regularly. | Lack of control of advertising if used by others. |
| Cheap to use-low cost if placing advertisements. | Messages may be altered or used badly and forwarded to another user, giving bad publicity. |
| It reaches groups that are difficult to reach any other way. | |

- Create your own website for promotion:

| Opportunities of advertising on the business's own website | Threats of advertising on the business's own website |
|---|---|
| No extra cost after setting up a website. | Potential customers may not see the website, as the page may appear in a long results list. |
| Control of advertising as the website is owned. | Relies on customers finding the website. |
| Can change adverts quickly and update pictures, prices, and so on. | The website's design costs can be high. |
| Interactive adverts can be more attractive than magazines or posters. | It would need to be constantly updated, and a team would need to be nearby for any bugs or issues. Which is costly. |
| Can provide more information in adverts and link to other pages with further information and pictures. | |
| Attracts funds and payment from companies who want to advertise their product on the business's site | |

## 3.12. Marketing Strategy

- **Marketing Strateg**y: a plan to combine the right combination of the four elements of the marketing mix for a product or service to achieve a particular marketing objective
- **The Marketing Strategy developed depends on the following:**
  - Size of market
  - Number and size of competitors
  - Marketing objectives
  - Target market
  - Finance available
- **Marketing objectives may include:**
  - Increasing sales
  - Improve the existing product
  - Increasing sales of a new product
  - Maintaining/ increasing market share
  - Increasing sales in a niche market
  - Increase market share/retain market share
- For example, A product is made, priced reasonably, and meets the consumer's needs, but no promotional element exists. No one will buy it because people don't know about its existence.
- Or if a product is made that doesn't meet consumer needs, it won't sell regardless of the price set.
- It is crucial to have all elements working together to influence consumer decisions (buying the product)

### Recommending and justifying a marketing strategy in a given circumstance:-

Important points to include in your answer:

- Marketing objective
- Marketing budget
- Target market
- Balanced marketing mix

## 3.13. Legal Controls in Marketing

- There are many laws in different countries to protect consumers from businesses taking advantage of their lack of knowledge or lack of product information
- These legal controls include (in the U.K.):
  - **Weights and Measures**
    - Selling underweight items or using inaccurate equipment to weigh goods is illegal.
  - **Sale of Goods**
    - Supplying flawed goods (not up to quality standard).
    - Product not fit for its intended purpose.
    - Products which do not perform as described in label or by retailer.
  - **Supply of Goods and Services Act**
    - Service must be provided with skill and care.
  - **Consumer contracts Regulations**
    - A consumer should have a minimum of 7 days cooling period (a consumer should have seven days to change their mind about the purchase they made)
  - **Trade Descriptions**
    - Supplying a good/ service which is unsafe/ not fit for the purpose is illegal.
    - Giving false info or misleading claims is illegal
  - Misleading consumers about the actual price is illegal
  - Making false claims about special deals and offers is illegal
  - Offensive or indecent ads are illegal
- **Complying with all legal controls can raise the total costs of a business by:**
  - Goods/ services may have to be redesigned to ensure quality and safety
  - Ads may have to be altered
  - Some promotion techniques may have to be changed
  - May have to change the packaging
  - Prices may have to be controlled and altered
  - Increase employment

## 3.14. Entering New Markets Abroad

- The globalisation of businesses has been increasing over the years; there are opportunities & problems with this:

| Opportunities | Problems |
| --- | --- |
| Growth potential in other countries: countries are developing, and population incomes are increasing | Lack of knowledge of competitors or consumer habits |
| Markets in the original region might be saturated (sales are low) | Cultural differences: for example, alcohol won't sell well in the Middle East |
| Can produce products abroad and learn about its market to increase sales | Exchange rates: in some countries, their currency isn't stable, so the price of imported goods increase |
| Trade barriers are lowered in most countries, so it is cheaper to enter markets | Transport costs are more expensive |
| | Import restrictions - causes price of goods to increase and sales decrease. |
| | Increased risk of non-payment |

- However, there are many methods to reduce and overcome the problems of entering a new market:

| Problem | Method to Overcome |
| --- | --- |

| Problem | Method to Overcome |
|---|---|
| Lack of knowledge (and cultural Differences) | Joint-Ventures: by working together/merging with local businesses in the same market, a business will gain a lot of necessary knowledge about the culture & market \n Franchising: letting people from the market abroad who have local knowledge to choose the location of the shop |
| Transport costs are expensive. | Licensing: the business permits a local business to sell goods under its name, so they do not have to import all the products physically |
| Cultural Differences | Localising Existing Brands: where a business still has the same brand image but adapts it to the market it is in (i.e. McDonald's cooking vegetarian meals in India) |

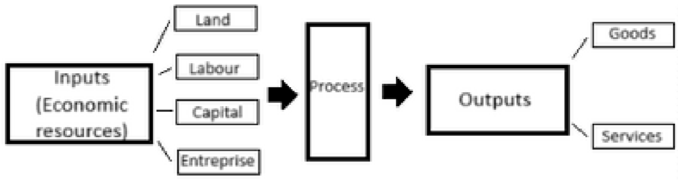
- Limitations to the methods listed above:

| Method | Limitation |
|---|---|
| Joint venture | Management conflict between the two businesses. Profit shared. |
| Licensing | Quality problems caused by an inexperienced licensee could damage brand reputation. Licensee now had access to information about how the product is made - could develop a better version and become a competitor. |
| International franchising | Quality problems or poor service offered by franchisees could damage brand image. Training and support will need to be provided by the franchisor. |
| Localising existing brands | May be less successful than a new product made to meet local cultures and market conditions. Expensive to change packaging, promotion, and so on for each market the product is sold. |

# 4. Operations Management

## 4.1. Production of Goods and Services

**Production Process**




- **Production**: making a product or service to satisfy consumer wants and needs.
- **The factors of production or 'inputs' include:**
  - **Land** – For factories or materials
  - **Labour** – Employees
  - **Capital** – Money/finance
  - **Enterprise** – Managers
- A business combines these inputs to produce a more valuable output (this is added value).
- **Labour-Intensive Production: A** larger workforce is used than machinery to make goods. Usually done in countries with low wages so that it is more efficient (ex: SHEIN).
- **Capital-Intensive Production**: businesses use machinery rather than workers. Usually done in developed countries where the wages are high.

### Operations Department

- The operations department's role is to transform inputs into outputs for consumers.
- An **operations manager** ensures raw materials are available and made into finished goods.
- **Most manufacturing businesses have:**
  - **Factory Manager** - responsible for quality and quantity of products
  - **Purchasing Manager** – responsible for providing the required materials and equipment
  - **Research and Development Manager** – responsible for design and training of employees for new products
- In the retail business, the factory manager will be replaced by the managers for the shop.
- In service businesses, e.g. Restaurants, the operation department will include managers for each shop.

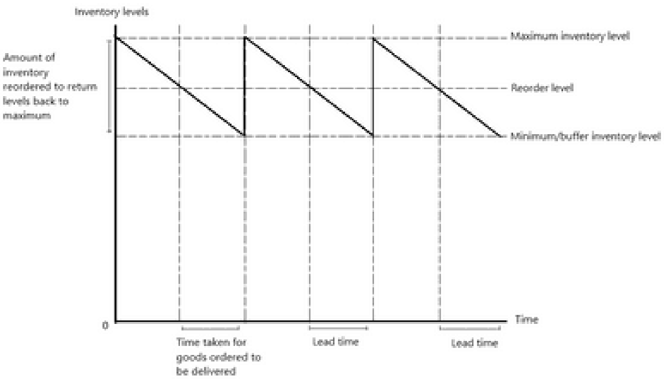
### Productivity

- **Productivity**: a way of measuring a business's efficiency.
- **Note**: Production is the making of the product, while productivity is how efficiently the product is made.
- $\text{Productivity} = \frac{\text{Quantity of output}}{\text{Quantity of input}}$
- $\text{Labour Productivity} = \frac{\text{output}}{\text{no. of employees}}$
- As employees become productive, per-employee output rises, and costs of production fall
- **Many ways to increase productivity:**
  - Improve factory layout to reduce time waste and raise efficiency
  - Introduce automation
  - Improve labour skills by training
  - Improve quality control
  - Improve employee motivation
  - Improve inventory control
- **Benefits of increasing efficiency:**

- More output compared to inputs.
- Lower costs per unit (and therefore lower average cost)
- For example, if the business has a limited workforce, raising their wages will increase motivation and, therefore, also increase productivity.

### Inventory

- Inventory can take various forms. **Inventory includes:**
  - Raw materials
  - Work in progress goods
  - Finished goods
- **Why do businesses hold inventory?**
  - To ensure enough inventory is available to satisfy sudden changes in demand.
  - Production and opportunity costs will also be high if inventory levels are high.
- **Inventories can be managed:**




- The business buys in inventory to fill its holding capacity, known as the maximum inventory level.
- As resources are depleted, inventory levels drop. At this stage, reorders will be made so it reaches the business in time before it runs out.
- **Buffer Inventory Level**: inventory held to deal with uncertainty in customer demand and deliveries of supplies.

## 4.2. Lean Production

- **Lean Production**: various techniques to cut down waste and raise efficiency.
- **Types of Waste:**
  - Transportation - when the goods are being moved unnecessarily → fuel price, chance goods may get damaged
  - Overproduction - leads to high storage costs and possible damage to goods while in storage.
  - Overprocessing - when sophisticated machines are being used to do simple tasks
  - Waiting - when goods are not moving or being processed, waste occurs due to inefficiency
  - Motion - any action made by an employee that does not relate to the production of goods, wastes time
  - Unnecessary inventory
  - Defects - when goods have faults/defects that require them to be inspected/fixed, wastes time
- **Advantages of lean production**
  - Less storage costs
  - Quicker production
  - Better use of equipment
  - Less money tied up in inventory
  - Speed up production by cutting out processes
  - Improved health and safety lead to less time off work due to injuries.
  - No need to repair defects or provide replacement services for a dissatisfied customer.
  - **All these save/reduce costs that lead to lower customer prices and increased business competitiveness and profit.**

### Types of Lean Production

- Kaizen
- Just-in-time inventory (JIT)
- Cell production

### Kaizen

- Kaizen means continuous improvement in Japanese
- Its primary focus is to eliminate waste
- Ideas are thought of by holding frequent meetings with workers to discuss problems and possible solutions.
- **Advantages:**
  - High productivity
  - Less space needed for production
  - Work in progress is low
  - Improved layout of the factory may lead to combining jobs. This will reduce labour demand.

### Just in Time

- A production method that reduces or virtually eliminates the need to hold inventories of raw materials or unsold inventories of the finished product.
- **Advantages:**
  - All this reduces the costs of holding inventory.
  - 'Warehouse' space is not needed, reducing costs.
  - The finished product is sold quickly so that money will return to business quickly. Helping cash slow.
- However, to operate in JIT, businesses need to have reliable suppliers and an efficient ordering system. If suppliers are late, it can disrupt the system.

### Cell Production

- This is where the production process is divided into separate units, each making an identifiable part of the good
- **Advantages:**
  - High motivation due to improved morale of employees.
  - More production efficiency.

- Employees feel more valued and are less likely to strike or cause disruption.

## 4.3. Methods of Production

- **3 Main Methods of Production:**
  - **Job Production**: products made one at a time
  - **Batch Production**: a quantity (batch) of a product is made, then a batch of another product is made
  - **Flow Production** (mass): large quantity of products made in a continuous process
- **Job Production:**

| Features | Benefits | Limitations |
|---|---|---|
| Products are made specifically for the customer's order | Good for 'one-off' products | Often labour-intensive, expensive as highly skilled workers are needed |
| Each order is different | Meets the exact requirements of the customer | Production takes longer |
| E.g. bridges, ships, cakes, cinema, films, suits | Varied work increases employee motivation | Any errors made are expensive to fix |
| | Ability to charge higher prices | Materials are more expensive. |
| | | No possibility of purchasing economies of scale |

- **Batch Production:**

| Features | Benefits | Limitations |
|---|---|---|
| A similar range of products is made in batches | Flexible work can change products easily | Machines must be reset to do different batches |
| Ex. bakery: makes one type of bread, then one type of cake and each product is produced in stages or batches. | Gives some variety to worker's jobs | Semifinished products may need to be transported around (+ cost) |
| | More variety, more consumer choice | Need space for stocks of raw material (high storage costs) |
| | Production may not be affected to any grant extent if the machine breaks down. | High work-in-progress inventory |
| | | Expensive and time-taking |

- **Flow Production:**

| Features | Benefits | Limitations |
|---|---|---|
| Large quantities of a product are produced. | High output, capital intensive, more efficient. | It is very boring for employees, leading to decreased motivation over time. |
| Cars, drinks, electronics, and mass-made products are made this way. | Costs are low, therefore low prices, leading to high sales. | High cost of inventory of output & raw materials. |
| | It requires only relatively unskilled workers and some training, maybe needed. | Capital costs for setting up production are very high. |
| | There is no need for moving goods around (all made in the same place). | If one machine breaks down, the whole production stops. |
| | Automated production lines can operate 24*7. | |
| | Benefit from economies of scale. | |

- **Factors influencing which production method to choose:**
  - **Nature of Product** - if unique or individual service, job production can be used.
  - **Size of Market** - if demand increases and more products can be sold but not in large quantities, batch production will be used. International market, flow production.
  - **Nature of Demand** - if large and fairly steady demand, e.g. soap powder flow production, can be used.
  - **The size of the Business** - if the business is small and doesn't have access to large funds, job production can be used.

## 4.4. Technology in Production Methods

- **Automation**: Equipment in a factory is controlled by a computer to perform mechanical processes (i.e., painting a car). Only workers are to ensure it runs smoothly.
- **Mechanisation**: production is done by machines but operated by people. Used to do difficult, precise or dangerous tasks. Work 24/7, quicker and more accurate.
- **Computer-Aided Design (CAD)**: software that helps design or re-style products quickly, allows technical sketches to be very detailed
- **Computer-Aided Manufacture (CAM)**: when computers monitor production and control machines/robots

- **Computer-Integrated Manufacturing (CIM)**: when software that designs the products is integrated with the machines that produce (CAM + CAD).

### Electronic Payment Methods

- **EPOS (Electronic Point of Sale)**: used at checkouts, where barcodes are scanned and displayed on the receipt. The inventory is automatically changed and reordered when the reorder level is reached.
- **EFTPOS (Electronic Funds Transfer Point of Sale)**: it is where an electronic cash register is connected to the retailer's bank accounts, and the money is directly transferred when the shopper's bank info is entered.
- **Contactless Payment**: works by the contactless device having an antenna; when touched against a contactless terminal, it securely transmits intervention about the purchase. e.g. credit cards, key fobs, mobile devices, etc.

| Advantages of Use of Technology | Disadvantages of Use of Technology |
|---|---|
| Productivity is greater as new, more effective methods are used, reducing average costs. | Unemployment could rise. |
| Greater job satisfaction stimulates workers. | It is expensive to invest in new technology; this **increases the risk** as more products would need to be sold to cover the cost. |
| **More skilled workers** may be needed to use and maintain the new technology. Therefore, **motivation and work quality** will increase as training is provided to existing employees. | Employees may be unhappy with the change. |
| Better quality products | New technology is constantly changing and becoming outdated quickly; thus, businesses must replace technology to remain competitive. |
| Quick communication and reduced paperwork, increasing profitability. | |
| The use of IT is much greater and results in better and quicker decision-making. | |
| New 'high-tech' products are introduced as technology makes completely new products available. | |

## 4.5. Costs and Scale of Production

### Business Costs

- **Fixed Costs (overheads)**
  - Costs that do not change with output in the short run.
  - Also known as overheads or indirect costs
  - Fixed Cost = Total cost – Variable cost
  - **Examples of Fixed Costs:**
    - **Rent of factory:** even if you produce lots of products, the rent price will be the same
    - **Insurance:** you set the insurance cost beforehand
    - **Bank fees:** bank fees are a set price; they don't change depending on the products produced
    - **Management Salaries:** they are set regardless of production
    - **Staff cost** (Security)
- **Variable Costs (VC)**
  - Costs which vary directly with output
  - Also known as direct costs
  - Variable cost = Total cost – Fixed cost
  - **Examples of Variable Cost:**
    - **Raw materials**: the more you produce, the more materials you need
    - **Electricity & Gas:** Energy is paid by use. If you are producing more, more electricity is being used
    - **Shipping cost:** Making more products means you have to ship more items, and shipping is paid by weight
- **Total Cost**: Fixed and variable costs combined.
  - Formula 1: Fixed cost + Variable cost.
  - Formula 2: Average cost per unit × output
- **Average Cost (Per Unit)**: total cost of production divided by the total output. Referred to as Unit Cost.
  - $\text{Formula for Average cost} = \frac{\text{Total cost of production}}{\text{Total output}}$

### Usage of Cost Data

- Helps manager set prices
- Deciding whether to stop production or continue.
- Deciding the best location.
- It helps managers to make decisions.
- It is needed to calculate profit and loss.

## 4.6. Economies of Scale (EOS)

- **Economies of Scale (EOS)**: the factors that reduce average costs as a business grows.
- **Types of economies of scale:**
  - **Purchasing Economies**
    - When a business buys in bulk, it tends to receive discounts, decreasing the price of each good.
  - **Marketing & Selling Economies**
    - When the company advertises for goods, it will pay the same amount to advertise a greater number. Therefore, when marketing for a higher output, unit costs fall, decreasing ATC.
  - **Financial Economies**

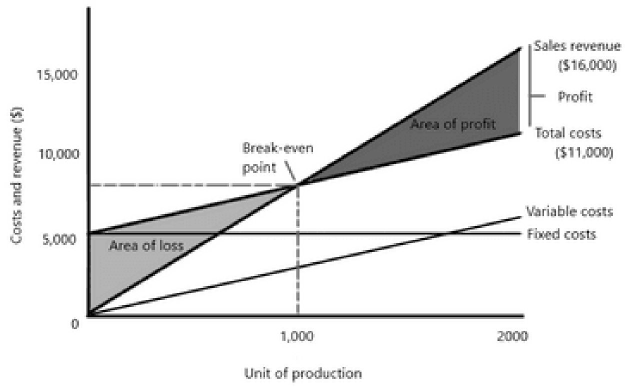
- Banks tend to lend to larger companies with low-interest rates, as they borrow high amounts and their collateral value is high.
- **Managerial Economies**
  - Large firms have opportunities to employ specialists who will help reduce wastage and increase efficiency and productivity.
- **Technical Economies**
  - More capital to invest in newer, more efficient technology and specialist equipment.

## 4.7. Diseconomies of Scale (DEOS)

- **Diseconomies of Scale (DEOS)**: the factors that lead to an increase in average costs as the business grows beyond a specific size.
- **Types of diseconomies of scale:**
  - **Poor communication**
  - **Lack of commitment from employees**
    - Large businesses have many employees, and not everyone is connected to the top management, reducing their motivation levels.
  - **Slow decision-making & weak coordination**
    - Large businesses have longer chains of command, so information and instructions take longer to reach the desired person, slowing communication and decision-making.

## 4.8. Break-Even Analysis

- **Break-Even Level of Output:** the quantity that must be produced/sold for total revenue to equal total costs. (also known as break-even point).
- **Break-Even Charts:** a graph showing how the costs and revenues of a business change with sales. They show the level of sales the business must make to break even.
- **Revenue**: the income during a period of time from sales of goods.
  - Total Revenue = Quantity sold × Price.
- **Break-Even Point**: the level of sale at which total costs = total revenue. The point where they intersect in the graph.
- The break-even point, the **calculation method**:
  - Contribution: selling price less its variable cost.
  - Contribution per unit: Selling price – Variable cost.
  - $\text{Break-even level of production} = \frac{\text{Total fixed costs}}{\text{Contribution per unit}}$
- **An example of a Break-even chart:**




| | Sales($)= 0 units | Sales($)= 1000 units | Sales($)= 2000 units |
|---|---|---|---|
| Fixed costs | 5000 | 5000 | 5000 |
| Variable | 0 | 3000 (1000x$3) | 6000 (2000x$3) |
| Total costs | 5000 | 8000 (3000+5000) | 11000 (5000+6000) |
| Revenue | 0 | 8000 (1000x8) | 16000 (2000x8) |

- **To draw a break-even chart, you must include:**
  - Fixed Costs line
  - Variable Costs line
  - Total Costs line
  - Sales Revenue line
- The shaded area that can be seen, labelled with 'Area of loss', shows how the sales revenue line is below the Total cost line, indicating that anything before the break-even point is a loss.
- The shaded area that can be seen, labelled with 'Area of profit', shows how the sales revenue line exceeded the Total cost line, indicating anything after the break-even (BE) point is a profit.
- 'y' axis measures money amounts (cost & revenue)
- The 'x' axis shows the number of units produced or sold
- **Benefits of break-even charts:**
  - Managers can read off the graph if the company **expects profit or loss** and can see how much profit/loss they will have at any level of output
  - They can **attempt different scenarios** and see the impact it will have on the profit or loss of the business. It lets managers **try out different possibilities** to determine which is the best. (i.e. increasing the selling price, increasing production)
  - It can show the **SAFETY MARGIN** – the **number of sales exceeds the break-even point**. For example, if a business' break-even point is at 1000 units, and they're producing 1500 units, their safety margin is 1500 – 1000 = 500.
- **Limitations of Break-even Charts:**
  - Break-even charts **assume that all products made will be sold**. It does not show the possibility that inventories may build up if they are not sold
  - Fixed costs only stay the same **if the scale of production stays the same** (doubling the output will

also increase the fixed cost because they must need a bigger factory, more machinery, labour, etc.)
- Break-even charts **assume that costs and revenues can be drawn with straight lines**, which doesn't happen in real life.
- It assumes costs and revenue increase at a constant rate.

## 4.9. Achieving Quality Production

- **Quality**: to produce a good or a service which meets customer expectations.
- **Quality is important for businesses because:**
  - It establishes the brand image
  - It builds brand loyalty
  - It maintains a good reputation
  - It will help to increase sales
  - Attracts more new customers
- **If quality is not maintained, businesses will:**
  - Lose customers to other brands/competitors
  - Have to replace faulty products or repeat poor service, which raises costs for business
  - They have a bad reputation because people with bad experiences will tell others, etc. This leads to lower sales & revenue.

### Quality Control

- **Quality Control**: Check for quality, whether a product or service, at the end of the production process.
- Quality control is a traditional way to ensure that products leave the factories without defects.
- Quality inspectors' job is to maintain/check quality regularly for errors.
- The whole production batch might have to be redone if errors are found.
- Their job is also to prevent any production errors before they happen during production, which will lead to money loss.

| Advantages of Quality Control | Drawbacks of Quality Control |
| --- | --- |
| Eliminates faults/errors before the customer receives a product or service. | It is expensive, as employees need to be paid to check the product or service. |
| Less training is required for the workers. | Identifies the fault but not how and why it occurred, so it is difficult to remove the problem. |
| | Increased costs if products have to be scrapped or reworked or service repeated. |

### Quality Assurance

- **Quality Assurance**: checking for the quality standards **throughout** the production process.
- Businesses will ensure quality standards are set, and then employees will apply these standards throughout the business.

| Advantages of Quality Assurance | Drawbacks of Quality Assurance |
| --- | --- |
| Eliminates faults/errors before the customer receives a product or service. | It is expensive to train employees to check products. |
| Fewer customer complaints. | Relies on employees following instructions of the standards set by the business. |
| Reduced costs if products don't have to be scrapped or reworked or service repeated. | |

### Total Quality Management (TQM)

- **Total Quality Management (TQM)**: the **continuous improvement** of products and processes by focusing on quality at **every stage** of production
- Many companies use total quality management.
- It tries to "**get it right the first time**" and has no defects
- It focuses on ensuring 100% that the **customer is always satisfied**. The customer is **not just the final user; it** also includes other people and departments within the business
- Quality must be maintained throughout the business, and no faults should occur.

| Advantages of total quality management | Drawbacks of Total Quality Management |
| --- | --- |
| Quality is built into each part of the production. It becomes a habit for the employees. | It is expensive to train all employees. |
| Eliminates virtually all faults/errors before the customers receive them. | Relies on employees following the ideology of TQM. |
| No customer complaints, so the brand image is improved. | |
| Waste is removed, and efficiency increases, which means less money is wasted (higher profits). | |

### Customers can be assured of quality products/services

- Businesses may apply a quality mark but will have to follow certain rules. This mark, e.g. ISO, makes sure products meet a particular standard.
- For service businesses, recommendations from satisfied customers can be heard or read from online sites, where bad and good reviews can be shown.

## 4.10. Location Decisions

### Businesses look for locations when:

- New business
- The present location is unsatisfactory
- Change in business aims and objectives
- Expansion

### Factors that influence the *choice* of location of a MANUFACTURING business:

- **Production methods and location decisions**
  - Production methods play a significant role in deciding the location of a business.
  - **Job Production**: the business will be small and won't have much effect on competitors there. The location of suppliers won't affect much on the business. Ex. A small jewellery business.
  - If there is large-scale production, then competitors in that area will be highly affected, and the business will prefer closer suppliers as raw materials will be huge. Transportation costs may be high if the supplier is too far.
- **Market**
  - When a product is heavier than its raw materials, businesses decide to locate its factory near the markets rather than the supplier, as a business will find it much cheaper due to transportation costs.
  - Due to advances in transportation facilities, the distances between factories and markets of heavy products don't play a vital role.
  - Perishable products need to be delivered quickly.
- **Raw Materials/Components**
  - Transportation costs will be high if goods and raw materials are very heavy. Then, a company may want its factory to be located near the supplier.
- **External economies of scale**
  - When two firms support each other or work together, they will be able to respond quickly to any important decisions to be made or any breakdowns.
- **Availability of Labour**
  - Every manufacturing business requires labour.
  - If a business requires only skilled labour, it will try to locate near a place where people with various skills live.
  - If a business requires unskilled labour, it will be located where wage rates are low and unemployment is high.
- **Government Influence**
  - When a government wants to encourage businesses to locate in a particular area, it will offer state-funded grants to encourage firms to move there.
  - High unemployed areas may provide grants to businesses to locate there.
- **Transport and Communication**
  - Businesses need to be closer to transport systems.
  - Exported products, ability to reduce transport costs.
  - Reduces time taken.
- **Power and water supply**
  - Availability of power is very important.
  - Some businesses need to have reliable power sources to continue production.
  - Some production processes require a reliable water source.
- **Climate**

### Factors that influence the choice of location of a SERVICE SECTOR business:

- **Customers**
  - Services which require direct contact, must be located near the customers.
  - Services where personal contact isn't required, location doesn't affect.
- **Technology**
  - Technology has allowed e-commerce, so location doesn't play a vital role.
- **Personal preference of owners**.
- **Availability of labour**
  - If a business is labour-intensive, it must be located where labour is easily found, like towns and cities.
- **Climate**
- **Near to other businesses**
  - Some services/ businesses serve large companies and so should be able to reach them immediately; therefore, they must located closer to them.
- **Rent/ taxes**
  - If services don't require personal contact, they can be located in places with lower rents and tax rates.

### Factors that influence the choice of location of a RETAILING business:

- **Shoppers**
  - Retailers want popular areas as they attract customers.
  - It depends on the type of product.
  - Expensive – a place where high-income people live or visit regularly.
- **Nearby shops**
  - Being located near a frequently visited shop means people may shop in between while visiting other shops.
  - A place with high competition attracts more customers as they have greater choice.
- **Customer parking availability/ nearby**
  - Convenient and nearby parking lots will encourage people to visit your shop.
- **Availability of suitable vacant premises**
  - If a proper location isn't available, a company can't locate there.
- **Access to the delivery vehicle**
  - Businesses try to find places near transport businesses to gain easy access to delivery vehicles.
- **Rent/ taxes**
  - Popular area, high demand, and high rent.
  - Less popular, low demand, low rent.

- **Security**
  - A place prone to theft may reduce a business's chances to locate there.
  - Insurance companies may not insure such companies.
- **Legislation**
  - Some countries may have laws restricting trade in some parts.

**Factors influencing the decision of which country to locate operations in:**

- **New market overseas** - when a business sees an increase in sales overseas, it may decide to move/relocate there instead of transporting products there.
- **Cheaper Source of material** – if the raw material runs out, the business must either bring in alternative supplies from somewhere else or relocate to a new country with these raw materials, it also might be cheaper than transporting it.
- **Difficulties with the labour force and wage costs** – if the business is located in a country where wages keep rising, it may be more profitable to relocate to a country with lower wages.
- **Rents/taxes considerations** – if other costs such as rent or taxes increase, this might cause businesses to relocate to countries where it is lower.
- **Availability of government grants and other incentives** - If governments want to increase foreign investment and job opportunities, they will provide grants, subsidies, and lower taxes. They may do this to provide new skills and increase employment.
- **Trade and tariff barriers** – If trade barriers are high, the business's chance of locating there would reduce costs.

**The Role of Legal Controls on Location Decisions**

- **Reasons the government influences these location decisions:**
  - To encourage businesses to set up and expand in areas of high employment.
  - To discourage firms from locating in overcrowded areas or on sites with natural beauty.
- **Two types of measures used by the government to influence where firms are located:**
  - Planning regulations (legally restrict business activity from certain areas).
  - Government grants or subsidies encourage them to locate in undeveloped areas.

# 5. Financial Information and Decisions

## 5.1. Why does a Business Need Finance?

- **Finance**: money that is needed to meet the expenses of a business. This is known as capital.
- **Capital is needed for:**
  - Starting up a business
  - Expansion
  - Increase working capital
  - **Capital Expenditure**: money spent on non–current assets.
  - **Revenue Expenditure**: money spent on day-to-day, recurring expenses.

**The Responsibilities of the Finance Department**

- Recording all financial transactions
- Prepare final accounts
- Cash flow forecast
- Make important decisions
- Provide info to managers

## 5.2. Sources of Finance

- **The primary sources of capital include:**
  - **Internal Sources**: Obtained from within the business **itself.**
  - **External Sources**: Obtained from **outside** and separate from the business.

~~**Internal Sources of Finance**~~

- **Retained Profits**: Profit businesses obtain after costs.

| Advantages | Disadvantages |
|---|---|
| It does not have to be repaid. | The new business will not have any. |
| It doesn't incur interest. | Small firms' retained profit may be low to finance the expansion. |
| | Reduces payment to owners, e.g., dividends for shareholders. |

- **Sale of Existing Assets**

| Advantages | Disadvantages |
|---|---|
| Better use of unwanted capital | It can take time to sell the assets, and the amount may not be the same as when purchased. |
| Doesn't increase the debts of a business | Source of finance not available for new businesses. |

- **Sale of Inventories**

| Advantages | Disadvantages |
|---|---|
| Reduces opportunity cost. | It may disappoint customers if a sudden change in demand is not met. |

| Advantages | Disadvantages |
|---|---|
| Reduces storage costs. | |

- **Owner's Savings**

| Advantages | Disadvantages |
|---|---|
| Quick availability | Savings may be low |
| No interest is paid | Increases risks for owners, as they might have unlimited liability. |

### External Sources of Finance

- **Issue of Shares**: Sale of business shares (only for limited companies)

| Advantages | Disadvantages |
|---|---|
| A permanent source of capital | Dividends are paid after tax. |
| It doesn't need to be paid back | Shareholders expect dividends. |
| No interest | Ownership will change if many shares are sold. |

- **Bank Loans**: A sum of money from a bank repaid with interest.

| Advantages | Disadvantages |
|---|---|
| Quick, easy to arrange | Must be repaid with interest |
| Available for varying lengths of time. | Security or collateral security must be given |
| Large companies receive low-interest rates if large sums are taken. | |

- **Selling Debentures**
  - Debentures are certificates issued to a debenture holder for the money they lent, which must be repaid within 20 – 25 years.

| Advantages | Disadvantages |
|---|---|
| Long term finance | Loans must be repaid, and interest must be paid. |

- **Debt Factoring**
  - Debt factors are specialist agencies that buy the claims of debtors of firms for immediate cash.

| Advantages | Disadvantages |
|---|---|
| Availability of immediate cash | The firm doesn't receive 100% amount |
| The risk of collecting the debtors becomes the factor, not the business's. | |

- **Grants and Subsidies**

| Advantages | Disadvantages |
|---|---|
| Don't have to be repaid | Given with strings attached |

- **Microfinance**
  - Providing financial services to poor people not secured by traditional banking.

| Advantages | Disadvantages |
|---|---|
| Small loans can be obtained by start-ups (especially if it's by simple people) | High-interest rates |
| | Greater risk for the lender |

- **Crowdfunding**
  - Funding a project or venture by raising money from numerous people who each contribute a relatively small amount.

| Advantages | Disadvantages |
|---|---|
| It's a fast way to raise a substantial sum. | Crowdfunding platforms may reject the proposal if it is not done well. |
| No initial fees are payable to the platform; only when the goal is reached a % will be taken. | If the total amount is not raised, finance invented by others will have to be repaid. |
| It allows public opinion to be heard to see if the idea is good. | Media interest and publicity are needed for a chance of success. |
| It is often used by entrepreneurs when other traditional methods are not available. | Competitors could steal the idea. |

### Short vs. Long-term Sources

Short-term finance (shortage of ash in short rem can be overcome in 3 ways):

- **Overdrafts**

| Advantages | Disadvantages |
|---|---|
| 'Overdraw' (spend more money than is currently in the account) | Interest rates are variable (vary from each overdraw) |
| Flexible form of borrowing | The bank can ask for the overdraft to be paid quickly. |
| Interest will be paid only in the amount overdrawn. | |
| Overdrafts are cheaper than short-term loans. | |

- **Trade Credit**
  - It is when businesses delay payments to suppliers

| Advantages | Disadvantages |
|---|---|

| Advantages | Disadvantages |
|---|---|
| Almost an interest-free loan | May not provide discounts |
| Reduces cash outflows in the short run | |

- **Factoring of Debt**

### Long-Term (Loans Available for More than a Year)

- **Bank Loans**
  - They are payable over a fixed period
- **Hire Purchase**
  - It allows a business to buy a fixed asset over a long period with monthly payments, including interest.

| Advantages | Disadvantages |
|---|---|
| Doesn't have to find a large cash sum to purchase the asset | A cash deposit is paid at the start of the month |
| | High-interest rates |

- **Leasing**
  - It allows a firm to use an asset without paying for it.

| Advantages | Disadvantages |
|---|---|
| Doesn't have to find a large cash sum to purchase the asset | The total cost of leasing changes will be higher than purchasing the asset. |
| Maintenance is taken care of by the leasing company. | |

- **Issue of Shares**
  - Only available to limited companies
- **Debentures**
- **Long-term Loans or Debt Finance -** this is different from share capital:
  - Loan interest is paid before tax and is an expense.
  - Loan interest must be paid every year.
  - The loan must be repaid.
  - Often 'secured' against particular assets.

### Factors When Choosing the Source of Finance

- **The main factors considered in making the financial choice:**
  - **Size of business & Legal Form** (type of business): Public limited companies have a larger choice of sources of finance because they pay less interest (less risk).
  - **Amount of Capital Required**: if you need just a little money, you won't issue new shares.
  - **Purpose of Capital & Time Period**: The general rule is that the finance source should match the financial need:
    - If the use of capital is long-term, the source should be long-term (same with short-term).
  - **Existing Loans (risk and gearing ratio)**: If a business has already taken out many loans, banks will think it is too risky to finance.
    - Gearing: measures the proportion of total capital raised from long-term loans.

### Common Reasons The Banks Refuse to Loan to Small Businesses

- Weak cash flow
- Lack of security or collateral.
- Poor preparation by the business owner when applying for the loan.

### Banks Need These to Lend

- Cashflow forecast
- Business plan
- Collateral/security
- Forecast income statement available

## 5.3. Cash-Flow Forecasting and Working Capital

- Cash is a **Liquid Asset**: it can be immediately available to spend on goods & services.
- **Cash Flow**: the cash **inflows** (money received by business) & **outflows** (money paid) over some time.
- **Cash Inflow**: money coming into the business.
  - Sale of goods
  - Sale of assets
  - Payments to debtors
  - Borrowing money
  - Investors
- **Cash Outflow**: money going out of the business.
  - Purchase of goods
  - Purchase of non-current assets
  - Payments of salaries
  - Repaying loans
  - Trade payables

### Cash Flow Cycle

- It shows the stages between paying out cash and receiving cash.
  1. Cash outflow to pay for materials, rent, etc.
  2. Goods produced
  3. Goods sold
  4. Cash payment received for goods sold (cash inflow)
- The longer it takes for the cash flow cycle to be completed, the greater the working capital.
- Cash flow is not the same as profit.
- Profit consists of goods sold on credit, whereas cash flow is a business's cash sales in a month.
- When profitable businesses run out of cash, it is known as **insolvency**

- **Due to:**
  - Over-trading
  - Long credit time
  - Less credit time received
  - Many fixed assets purchased

### Cash Flow Forecast

- **Cash-Flow Forecast**: an estimate of a business's future cash inflows and outflows on a month-by-month basis. Shows the expected cash balance at the end.
- **Closing Cash Balance**: the amount the business holds at the end of each month.
- **Opening Cash Balance**: the amount the business holds at the start of each month.
- **Net Cash Flow**: The difference between the cash inflow and outflow (**inflow – outflow**)

| | January | February | March |
|---|---|---|---|
| Opening bank balance (A) | 10,000 | 15,000 | (5,000) |
| Cash inflow (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 |

### Uses of Cash Flow Forecast

- **Starting up a business**
  - The first few months are crucial to every business, as owners don't realise the amount of cash needed, which is why they fail.
  - Businesses need to spend on labour, land, and capital. They even have to advertise and promote extensively.
  - Many owners don't understand the importance of cash flow in a business, so they fail.
- **Keeping the bank manager informed**
  - A cash flow forecast will help a business receive a loan.
  - The bank manager needs to know when the amount is needed, for how long, and when it will be repaid.
- **Managing an existing business**
- **Managing cash flow**
  - Businesses with high bank balances can use their cash effectively in other areas.

### How do you Overcome Cash Flow Problems?

#### Short Term Solutions

- **Increasing bank loans** will inject more cash into the business, but interest and loan must be paid.
- **Delaying payments to suppliers** will decrease cash outflows in the short run, but suppliers may refuse to provide discounts or supply.
- **Reducing credit periods** may help a business increase short-term cash inflows, but customers may switch to competitors.
- **Delaying the purchase of fixed assets** will reduce cash outflows, but in the long run, a company may lack efficiency as they don't have up–to–date technology.

#### Long Term Solutions

- Attracting new investors
- Cutting costs and increasing efficiency using lean production.
- Develop new products

## 5.4. Working Capital

- In the short run, it is the capital available to a business to pay for day–to–day expenses.

**Working Capital = Current Assets – Current Liabilities**

- Working capital can be in the form of:
  - Cash
  - Value of debtors
  - Value of inventory
- Working capital should be handled properly because it shows investors & banks how efficient a business is and its financial strength.

## 5.5. Income Statements

- **Accounts**: the financial records of a firm's transactions.
- **Accountants**: professionally qualified people who are responsible for keeping accurate accounts and producing final accounts.
- **Final Accounts**: These are produced at the end of the financial year and give details about the profit/ loss made over the year and the worth of the business.
- The simple equation for profit:
  **Profit = Sales revenue – total costs**
- **Profit can be increased through:**
  - Increasing the sales revenue so that it is higher than the production costs.
  - Reducing the production costs.
  - A combination of the two.

### Importance of Profits

- **Importance for Private Sectors:**
  - **Reward for enterprise**
    - Entrepreneurs have special qualities, and they must earn rewards for that.
  - **Reward for risk-taking**
    - Shareholders/investors/owners take risks when they provide capital; profits reward those risks.
    - Payments act as incentives to invest more and make the business profitable
  - **Source of Finance**
    - Profits after payments can be used to fund expansion
  - **Indicator of Success**

- Profits show that investing can be profitable, but losses show that investment must not be made.
- However, **Profit ≠ Cash** as profit is derived from revenue, but cash can be derived from many places (e.g. selling assets like cars).

- **Importance of profit to the public sector:**
  - Used as a **source of finance** to develop the state-owned business or be more efficient.
- **Importance of profit to social enterprise:**
  - **Balance profit-making with their aims**, as profit is used for the firm's survival.

### Understanding Income Statements

- **Income Statement**: a financial statement that records the income of a business and all costs incurred to earn that income over some time.
- Managers, banks and other investors will use it to see if a business is making a profit:
  - To compare with previous years - if it is greater than the year before
  - To compare to competitors
- **The main features of an income statement include:**
  - **Revenue**: the income to a business from the sales of goods and services.
    - Equation: **Units sold x Cost per unit**
  - **Costs of Sales**: the cost of production or buying the goods the business sells during a period.
    - Equation: **Opening inventories + Purchases – Closing inventories**
  - **Gross Profit**: the profit made in revenue is greater than the cost of sales.
    - Equation: **Revenue – Cost of sales**
  - **Trading Account**: shows how gross profit is calculated.
  - **Net Profit**: the profit the business makes after deducting all costs.
    - Equation: **Gross profit – Overhead costs (Fixed costs)**
    - Depreciation: the fall in the value of a fixed asset over time.
  - **Retained Profit**: the net profit, after taking away taxes and payments to owners – which is reinvested into the business.
- **Limited companies will have in their income statements:**
  - Corporation tax is paid from net profit.
  - Dividends paid to shareholders.
  - Retain profit after these two deductions.
  - Results from the previous year will allow for easy comparisons.

### Example of Income Statement

| | 2018 | 2017 |
|---|---|---|
| Revenue | $1250 | $1300 |
| Cost of sales | – $900 | – $900 |
| **Gross profit** | **$350** | **$400** |
| Expenses, including interest paid | – $155 | – $160 |
| **Net profit** | **$195** | **$240** |
| Corporation tax | – $35 | – $40 |
| **Profit after tax** | **$160** | **$200** |
| Dividends | – $120 | – $130 |
| **Retained profit for the year** | **$40** | $70 |

- **Uses of income statement:**
  - Know the profit/loss made.
  - Compare their performance.
  - Profitability of individual products.
  - Products to launch.

## 5.6. Statement of Financial Position

- **Statement of Financial Position** – a document that shows the value of the business's assets and liabilities at a time.
- **Assets**: Items of value *owned* by a business.
  - **Current Assets**: (Short-term Assets) Items owned by the business for *less* than 1 year, i.e. Raw material, cash.
  - **Non-Current Assets**: (Long-term Assets) Items owned by a business for *more* than 1 year, i.e. Buildings, land, company cars.
- **Liabilities**: debts *owed* to the business.
  - **Current Liabilities**: (Short Term Liabilities) Debts owed by business for less than 1 year, i.e. bank overdrafts and wages.
  - **Non-current liabilities:** (Long-term Liabilities) debts owed by a business for more than 1 year, i.e., long-term bank loans and creditors (money the business owes to suppliers).
  - The **Total Equity** (AKA Shareholders' funds) is how much a business is worth. (only for limited companies).
    - ***Shareholders' Funds = Total Assets – Total Liabilities***
  - The shareholders' funds are the total money invested in a business by the shareholders/owners.
  - This money can be invested by either **share capital** or **reserves** (Retained profit and loss).
  - If the total equity of a business has increased/fallen, the shareholder's stake in the company will be worth more/less, respectively.

### Example of Statement of Financial Position

| Assets | 2018 ($00) | 2017 ($00) |
|---|---|---|
| **Non-current (fixed assets):** | | |
| Land and buildings | 450 | 440 |
| Machinery | 700 | $600 |
| | 1150 | 1040 |
| **Current assets:** | | |
| Inventories | 80 | 50 |
| Account receivables (debtors) | 50 | 60 |

| Assets | 2018 ($00) | 2017 ($00) |
|---|---|---|
| Cash | 10 | 15 |
| | 140 | 125 |
| **Total Assets** | **1290** | **1165** |
| **Liabilities:-** | | |
| **Current liabilities:** | | |
| Account payables (Creditors) | 65 | 40 |
| Bank Overdraft | 65 | 60 |
| | 130 | 100 |
| **Non-Current liabilities:** | | |
| long-term bank loans | 300 | 245 |
| **Total Liabilities** | **430** | **345** |
| **Total Assets - Total Liabilities** | **860** | **820** |
| Share capital | 520 | 500 |
| Profit and loss reserves | 340 | 320 |
| **Total Shareholders' funds/equity** | **860** | **820** |

### Interpreting Balance Sheets

- Shareholders can see the value of their stake
- Shareholders can also analyse how expansion has been paid for by long-term loans, retained profit, or increased share capital (sales of shares).
- You can calculate the **Working Capital**.
  - **Working Capital = Current Assets - Current Liabilities**
- You can also calculate the **Capital Employed** – the long-term and permanent capital invested in a business.
  - **Capital Employed = Non-Current Liabilities + Total Equity**

## 5.7. Analysis of Accounts

- **Analysis of Accounts**: using data in the accounts to make useful observations about a business's performance and financial strength.
- Used to compare results from other years and other businesses.
- **Liquidity**: the ability of a business to pay back its short-term loans (debt).
- **Illiquid**: assets are not readily convertible into cash.
- **Profitability**: the measurement of the profit made relative to either sales achieved or the capital invested in the business. Also, a measure of efficiency.
- There are 2 types of ratios:
  - **Profitability Ratios** – how profitable a business is
  - **Liquidity Ratios** – how able a business is to pay its short-term debts (current liabilities)
- **Profitability Ratios:**
  - **Gross Profit Margin** (%): how well a company converts sales into gross profit.
    - $\text{GPM}(\%) = 100 \times \frac{\text{Profit}}{\text{Sales Revenue}}$
    - The percentage of how much profit you have to earn from the capital employed. The higher the %, the more efficient the business is with its capital employed.
  - **Net Profit Margin** (%): how well a company converts sales into net profit.
    - $\text{NPM}(\%) = 100 \times \frac{\text{Net Profit}}{\text{Sales Revenue}}$
    - Shows the percentage of gross profit per $1 worth of goods. If the following year's profit increases, either the price increases or the cost of sales is reduced.
  - **Return on capital employed**: how profitable a company is compared to the money used.
    - $\text{RoCE}(\%) = 100 \times \frac{\text{Net Profit}}{\text{Capital Employed}}$
    - Shows the net profit made on each $1 Worth of sales. The higher the results, the more net profit is gained from the sales.
- One profitability ratio isn't helpful by itself. You need to use all the profitability ratios and compare them with previous years of the business.
- **Liquidity Ratios:**
  - **Current Ratio:** how good a company is to pay off its current liabilities with its current assets.
    - $\text{Current Ratio} = \frac{\text{Current-Assets}}{\text{Current-Liabilities}}$
    - Shows whether the business has enough current-term assets to pay off short-term debts; if less than 1 means the business does not have money, 1 is when a business can exactly pay debts, and when more than 2 means it has excessive assets that could be put to use.
  - **Acid Test Ratio**: measures the ability of a company to pay off its liabilities without depending on the inventory sales.
    - $\text{Acid Test Ratio} = \frac{\text{Current assets-inventories}}{\text{Current-liabilities}}$
    - The acid ratio considers only the liquid assets of the business, not the inventories. The uses as the current ratio.

## 5.8. Users of Accounting Information

- **Managers**
  - They will help them keep control over the performance of each product.
  - Help decision-making
  - Ratios are a quick way for managers to compare their ratios with other businesses and previous accounts.
- **Shareholders**
  - Shareholders and potential investors want to know how big a profit/ loss the company has made.
  - They will want to check the profitability and liquidity ratios and decide whether shareholders have to buy more shares.
- **Creditors/Trade Payable**
  - Liquidity ratios indicate the ability of the company to pay back its debts.
- **Banks**
  - Risk of illiquid, no lending.
- **Government**

- To check the tax revenue, whether the firms are paying the right taxes.
- **Workers and trade unions**
  - They just want to assess whether the company's future is secure.
  - Access the profits to help unions improve wages and working conditions of employees.
- **Other businesses – competitors**
  - The managers will compare their profitability and liquidity with other businesses.

### Limitations of Accounting Records and Ratio Analysis

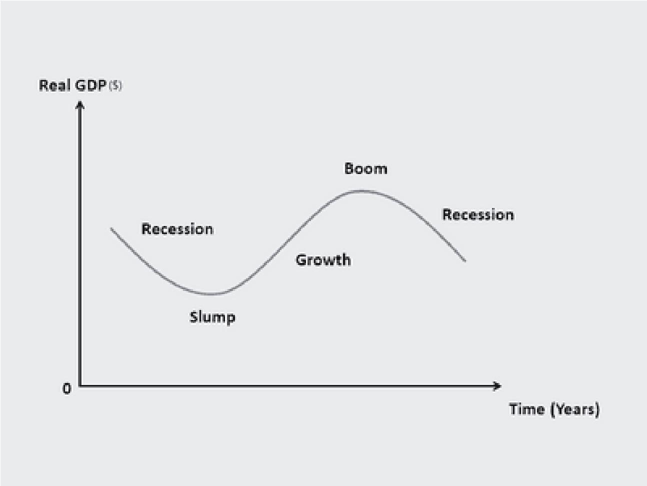
- Managers have access to all account data; external users only have what the business requires to show by the law.
- Ratios are based on past accounting data and can not be used to forecast future business performance.
- Accounting data over time will be affected by inflation, and comparisons can be misleading.
- Different companies may use different ways of accounting. Therefore, comparisons may be difficult.

# 6. External Influences on Business Activity

## 6.1. Economic Issues

### Main Stages of the Business Cycle and Trade Cycle

- **Gross Domestic Product (GDP)**: the total value of the output of goods and services in a country in one year.




- **Recession**: too little spending, falling GDP, demand and prices, workers lose jobs.
- **Slump**: long-drawn-out recession. Unemployment is higher, and prices fall; many businesses fail to survive this point.
- **Growth**: GDP is rising, unemployment is falling, and living standards are higher. (Firms are doing well at this point).
- **Boom**: too much spending, inflation, shortage of workers, and businesses uncertain about the future.

### Impact on Business from Changes in Economic Indicators

- Changes in employment levels will affect the ability of the business to recruit new employees and also the income of customers.
- Rising inflation may increase business costs, leading to higher product prices. The effect of increasing inflation depends on the type of product sold.
- An increase in GDP means the economy is growing. Increase sales, higher income, but recruitment of employees hard.

### Government Economic Objectives

### Low inflation

- **Low Inflation**: Low prices of goods & services so that people will buy more money in the economy.
  - **Inflation**: The increase in average prices of goods & services.
- **Rapid inflation may lead to:**
  - A fall in the value of money falls in real incomes.
  - Wage price spiral.
  - Fall in international competitiveness as prices will be high.
  - Businesses may not want to expand and create jobs.
  - Living standards will fall.
- Low inflation rates will act as an incentive for firms to produce and encourage them to expand.

### Low Unemployment

- **Low Unemployment**: A high % of people work so that they don't rely on government funds.
  - When people want to and have the ability to work but can't work, then they are said to be unemployed.
  - The country's output will be lower if unemployed people don't produce goods and services.
  - It involves an opportunity cost as the government has to pay greater unemployment benefits, which could be used to improve education and increase living standards.

### Economic Growth

- **Economic Growth**: growth of a country's GDP (Gross Domestic Product) – more goods and services being produced and sold.
  - If an economy's total output rises, it is said to be experiencing economic growth.
  - GDP is the total value of goods and services produced in an economy.
  - Economic growth may cause employment to rise, increasing living standards and reducing poverty.
  - **A fall in GDP can lead to:**
    - Unemployment
    - Fall in average living standards as poverty rises

- Less investment

### Balance of Payment

- **Balance of Payment** (of Imports & Exports): the difference between a country's imports and exports balance out (BoP = Exports – Imports).
  - **Exports**: Goods and services **sold** from one country to another.
  - **Imports**: Goods and services **bought** by one country from another.
- Balance of payments is a record of one country's financial transactions internationally.
- Governments will aim for an equal balance of payments: exports equal imports.
- Higher imports than exports lead to a budget deficit.
- Higher exports than imports lead to a budget surplus.
- **Problems of Budget Deficit:**
  - The government can run out of foreign currency reserves and will have to borrow.
  - The exchange rate depreciates – the price of our currency falls as compared to the other currency.
    - **Exchange Rate**: the price of a currency in terms of another.

## 6.2. Government Economic Policies

### Fiscal Policy

- **Fiscal policy**: any changes by the government in tax rates or public sector spending.

**Spending by the Government**:

- Government spending decisions can have a great impact on certain business decisions.
- **If the government decides to increase its spending:**
  - Increase subsidies and grants (to encourage businesses to set up in high-unemployment areas).
  - Increase in welfare benefits, meaning consumers will have a higher portion of income to spend.
  - Stimulation of economic growth.
- **If the government decides to decrease spending:**
  - Increased competition (mainly if privation is used)
  - Disinflation (the reduction in the rate of inflation)

### Tax

- **Direct Tax**
  - Income tax reduces consumer disposable income.
  - Corporation tax on comparing profit.
- **Indirect Tax**
  - Expenditure taxes, e.g. VAT
  - Import tariffs/quotas to reduce imports from abroad.
    - **Import Tariffs**: tax on imported goods.
    - **Import Quota**: a physical limit on the quantity of a product to be imported.
- Governments and spending decisions include a tax measure according to the effect they want to achieve.
- Governments will reduce spending and increase tax rates to reduce inflation.
- Governments will increase spending and decrease tax rates to stimulate economic growth.

### Monetary Policy

- **Monetary Policy**: change in interest rate by the government and the central bank.
- Governments will have a set of objectives they would like to achieve and will present these objectives to the central bank, which will set the interest rate in accordance with these objectives.
- If these objectives seek to **increase the overall demand** in the economy, the central bank will **lower interest rates**, which will lead to -
  - More consumer spending than borrowing.
  - More risk of inflation (Decreases confidence consumers/Businesses have).
  - There is less incentive for firms to invest/expand.
  - Depreciation of the exchange rate (Fall in value of the country's currency) will make for cheaper imports.
- If these objectives seek to **decrease the overall demand** in the economy, the central bank will **raise the interest rate**; this will lead to -
  - Less consumer spending than borrowing.
  - Less risk of inflation (Increases confidence consumers/Businesses have).
  - Increase incentives for firms to invest/expand.
  - Appreciation of the exchange rate (Rise in value of the country's currency) will make for costlier imports.

### Supply-Side Policies

- **Supply-side Policies**: try to increase the competitiveness of industries in an economy against those from other countries. Make the economy more efficient and increase supply.
- These supply policies focus on more long-term objectives, unlike fiscal/monetary, which are more short-term and demand-focused. **They have three main categories:**
  - **Encouraging Competition**: through privatisation/deregulations.
  - **Labour Market Reforms**: through trade unions, minimum wage, and labour legislations.
  - **Incentive-related Policies**: through reduced tax rates and increased subsidies.

## 6.3. Environmental and Ethical Issues

### Social Responsibility

- **Social Responsibility**: when a business decision benefits stakeholders other than shareholders.
- **Examples of business activity impacting the environment:**
  - Emission from transport vehicles.

- Pollution from factories.
- Waste disposal
- Transportation of goods by ship or track burns fossil fuels such as oil, creating carbon emissions, which link to global warming and climate change.

| Arguments against being mindful of the environment: | Argument with being mindful of the environment: |
|---|---|
| It can be expensive and reduce profit. | Pollution and global warming affect all, so social responsibility helps reduce this problem. |
| Increase prices to pay for 'environmentally friendly' policies. | Using non-renewable resources leaves less for the future and raises prices. |
| It can make firms unproductive, reduce salaries and relocate to places without such policies. | Scientists and environmentalists believe that business activity can do permanent damage. |
| Consumers buy less if the price is high. | Consumers are becoming more socially aware, so environmentally friendly products have become a market advantage. |
| The government should pay to clean it up. | Pressure groups can take action to harm the business's reputation and sales. |
| Owners can claim there isn't proof that the activity is causing damage. | |

- **Pressure Groups**: people who want to change business (or government) decisions by taking actions, such as consumer boycotts.

### The Concept of Externalities

- **Private Costs**: costs paid for by a business or the consumer of a product.
- **Private Benefits**: gains to a business or the consumer of a product.
- **External Costs**: costs paid for by the rest of society, other than the business.
- **External Benefits**: gains to the rest of society, other than the business.
- **Social Costs = External costs + Private costs.**
- **Social Benefits = External benefits + Private benefits.**
- If the social benefit exceeds social costs, the scheme will likely be accepted; the government/local community will probably refuse permission.

### Sustainable Development

- **Sustainable Development**: Development which does not risk future generations' living standards.
- **Business can be sustainable by:**
  - Use of renewable energy
  - Recycle waste
  - use fewer resources
  - Develop new 'environmentally friendly' products and production methods.

### Main Reasons Why Businesses Respond to Environmental Pressure

#### Consumers

- Bad publicity can cause them not to buy; if consumers think the products harm the environment, they will stop buying, resulting in the business changing the product or production method.

#### Pressure groups

- Can take actions towards businesses like consumer boycotts.
- The impact of the actions depends on:
  - Public support and media coverage.
  - Consumer boycotts result in a decrease in sales.
  - The group is well-financed and organised.
  - Whether the action is unpopular but not illegal
  - Cost damage methods by the business.
  - If a business sells to another business - public pressure is less effective.

#### Government through legal contracts

- By making certain activities illegal:
  - Locating in an environmentally sensitive area.
  - Producing non-recyclable products.
  - Dumping waste in nearby rivers/seas.
- Pollution permits - licences that allow businesses to pollute to a certain level. If the business exceeds the account, it must buy from a 'cleaner' business or pay large fines.
- Additional taxes on goods or factories resulting in pollution.

### Ethical Issues

**Ethical Decision**: based on a moral code of conduct, sometimes called 'doing the right thing'.

- Offering or taking business from government officials or people working for other businesses.
- Employ child labour, even if it is illegal in some countries.
- Buy supplies that lead to damage to the environment.
- Agree to 'fix high prices' with competitors.
- Pay high to the top of the hierarchy and poorly to the lower levels.

#### Two main extreme views to the ethical standards:

- If the law is not broken, businesses can do whatever to gain profit.

- Even if it is not illegal, therefore wrong even if it may increase profit.

| Potential benefits of ethical decision | Potential limitation of ethical decision |
|---|---|
| Customers may be more inclined to buy products not made by child labour. | Adults paid higher costs, especially if good workers' conditions were involved. |
| Good publicity about ethical decisions provides 'free promotion'. | Prices may be set higher due to higher costs. |
| Long-term profit increases | If consumers are not interested in how it's made and care only for price - then profits fall. |
| Some workers and investors may want to link an 'Ethical business', making recruiting and raising capital easier. | Short-term profit may fall. |
| Less risk of legal actions being taken against the company. | It could be argued that some countries employ children as they may be the only source of income for the family, and may cause them to fall to low levels. |

## 6.4. Business and the International Economy

- **Globalisation**: the world is becoming more interconnected, leading to increasing worldwide trade & people moving.
- **The reasons for globalisation include:**
  - More **Free-Trade Agreements** and economic unions between countries have replaced protection for industries. Consumers can purchase with few or no import controls.
  - **Improved and cheaper travel links and communication** between countries made it easier to transport goods globally. Interest also allows east price comparisons, and online/e-commerce allows orders to be placed anywhere.
  - Many '**Emerging market countries**' are industrialising very rapidly. They can sell globally at cheaper prices because of the loss of growth of the firms and industries.

**The Opportunities and Threats of Globalisation to a Business include:**

| Potential Opportunities for Business | Effect 1 | Effect 2 |
|---|---|---|
| Start selling exports to other countries - opening up foreign markets. | Increase potential sales, especially online sales. | They are expensive to sell abroad, and foreign consumers buy the products even if they are popular at 'home'. |
| Open factories/operations in other countries (become a multinational) | Cheaper to make goods outside than domestically. | Quality good? Ethical issues? Expensive or difficult to set up operations in other countries? |
| Import products from other countries to sell to customers in 'home' country. | No trade restrictions, more profitable to buy, could sell domestically. | Products need maintenance and partly repairs. Will the needed parts be available from the foreign producer? |
| Import materials and components from other countries. But still produce final goods in the 'home' country. | Cheaper purchases of supplies from other countries will free trade and reduce costs. Materials can be supplied 'online'. | Are suppliers reliable? Does greater distance add too much transport costs? |

| Potential Threats to Businesses | Effect 1 | Effect 2 |
|---|---|---|
| Increase imports into the home market from foreign competitors. | If competitors offer cheaper products, domestic sales fall. | Increased competition forces local firms to be more efficient. |
| Increase investment from multinationals to set up operations in the home country. | Create further competition - Multinationals that afford the best employees may have economies of scale. | Local firms become suppliers to multinationals, and their sales could increase. |
| Employees may leave businesses that cannot pay the same or more than international competitors. | In some professions, employees have more choices about where they work - businesses will have to make more effort to retain them. | It might encourage local businesses to use various motivational methods to keep their workers. |

**Why Government Might Introduce Import Tariffs and Import Quotas**

- **Import Tariffs**: tax placed on imported goods in the country.
- **Import Quota**: a restriction on the quantity of a product that can be imported.
- **Protectionism**: when a government protects domestic businesses from Foreign competition using tariffs and quotas. This reduces employment incomes.
- Import tariffs increase the prices of imported goods, making them less competitive than locally produced goods.
- Import quotas decrease the quantity of imported goods; increasing the price means less availability, thus increasing sales for domestic products.

## 6.5. Multinational Companies (MNCs)

- **Multinational (Transnational) Company**: a company that has factories or service operations in more than one country
- *It is not just selling products abroad; it* is having operations abroad
- The benefits of a business and its impact on becoming international:

| Benefits to business | Impact to stakeholders |
|---|---|
| New market | Higher dividends |
| Easier to obtain raw materials as they can be closer | Opportunity to live and work abroad |
| Avoid trade barriers and import taxes | Suppliers increase/decrease depending on the location |
| Low Labour costs | Government gains higher/lower taxes |
| Spread risk (if there are low sales in one country and high sales in another) | |

| Benefits to the business | Benefits to the country |
|---|---|
| Producing goods at lower costs | Jobs are created |
| Closer to resources (i.e. oil) | Investments in the development of infrastructure in the country |
| Closer to market | More exports |
| Avoid expensive taxes on the import of goods (i.e. Korean cars (KIA) being produced in the EU to benefit from free trade) | Tax – more money to the government |
| Spread risks (if there are low sales in one country and high sales in another) | Increased product choice for consumers |

| Advantages to Host Country | Disadvantages to Host Country |
|---|---|
| New investment | Influence the government and economy (bringing outside influences and culture). |
| More export increases the international competitiveness of the country | Due to MNCs ' expertise and activity, existing firms will likely be pushed out of the market. |
| Fewer imports keep domestic businesses active and prevent the BoP deficit. | Depletion of scarce resources and endangerment of natural sites. |
| Jobs created reduced unemployment. | Profits flow out of the country. |
| Increase tax paid to the government. | Often, unskilled work is created. |
| More competition helps increase the productivity and efficiency of domestic businesses. | |

## 6.6. Exchange Rates

- **Exchange Rate**: the price of one currency in terms of another currency.
- For example, 1 Euro is equivalent to 1.2 Dollars
- **Currency Appreciation**: when the value of a currency increases.
  - It can buy more of another currency
  - 1 euro = 1.2 dollars, to 1 euro = 1.5 dollars.
- **Currency Depreciation**: when the value of a currency decreases.
  - It can buy less of another currency.
  - 1 euro = 1.2 dollars, to 1 euro = 1 dollar.
- **2 things influence the exchange rate of a currency:**
  - **Demand for the Currency**: if many people want to buy the currency, the price will increase because there is a 'limited' number of currencies (so it leads to appreciation).
  - **Supply of Currency**: if the central bank prints more money, the supply increases, but the demand is still the same, so the value is lower (leading to depreciation).

**Exchange Rates Can Affect Businesses By:**

| If it Appreciates | If it Depreciates |
|---|---|
| **Import prices fall**: since your currency can buy more of the other currency. | **Import prices rise**: your currency is worth less, so you need more to buy other currencies. |
| **Export prices rise**: your currency is worth more, so it is more expensive for other currencies to buy it. | **Export prices fall**: it is worth less, so other currencies can buy your currency for less than theirs. |

- **This means that if the currency appreciates:**

- The product's **price** in other countries will **increase**
- The business will make **more profit**
- Businesses can lower the price and still make the same amount of money as before – it is **more competitive.**

- **If the currency depreciates:**

- The product's **price** in other countries will **decrease**
- **less profit** will be made
- Businesses need to raise the price to make the same amount of money as before – **less competitive.**

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