

# Answers

## 1 Business activity

### Activity 1.1

- a** Answers could include: water; food; shelter; clothing.
- b** Answers could include: style to enhance the consumer's image; clothing and footwear to improve sporting performance.
- c** Explain **two** reasons why Tyche's sales might have increased. For example:  
The first reason why Tyche's sales might have increased would be a rise in consumer incomes. If buyers of Tyche's sports goods have more disposable income, they are more likely to buy luxury goods like sports clothing and Tyche could experience a rise in sales. The second reason could be because of a promotional activity by Tyche. You need to be analytical here by clearly showing how the rise in sales occurs. An example using Tyche would be very useful to support this.

### Activity 1.2

Resource	Type
The family that initially started the business	Enterprise
Plastic to use in car interiors	Land
Workers who work on the production line	Labour
Metal to use in the production car bodies	Land
Employees who work in the finance department	Labour
Robot technology used on the production line	Capital
The business's IT system	Capital
The shareholder in the car manufacturer	Enterprise

### Activity 1.3

- a** The opportunity cost of D7 spending more money on diamonds is buying a new diamond cutting machine.
- b** As precious stones, diamonds are a very scarce resource and are very limited in supply. Diamonds also have very high demand because of the attractiveness of the product and their opulent reputation. The combination of being so scarce as a product and having such a high demand means that the market price for diamonds tends to be extremely high.

### Activity 1.4

Product	Type of good or service
A dress bought by a mother for her daughter's birthday party	Consumer good
A new building bought by a school	Capital good
A personal computer sold in an electrical retailer for home use	Consumer good
Financial advice offered by a bank to person thinking of retiring	Consumer service
The ticket bought for a professional football match	Consumer service
The vehicles bought by a distribution company	Capital good

### Activity 1.5

- a Value added is the increase in worth a business creates to a good or service as it goes through the production process.
- b The want being satisfied by P & M Ltd is the satisfaction buyers of the magazine get from reading about sports and recreation.
- c The opportunity cost for P & M Ltd is that it would have to give up an upgrade to its IT system if it opens a new office in the US.
- d The capital resources P & M Ltd will need include: office building, IT equipment, fixtures and fittings. The labour resources include: journalists, IT staff, marketing and sales staff.
- e Consider the benefits of specialisation which might include: a higher-quality product, more efficient production and meeting the wants of the target market. Discuss the costs of specialisation including: the risk if market demand for specialist magazines falls and there is a limited market demand for the specialist magazine. It is important to evaluate the benefits of specialisation clearly and include a justified conclusion.

## 2 Classification of businesses

### Activity 2.1

Good or service	Business activity (primary secondary, tertiary)
Dentist	Tertiary
Fishing	Primary
Musical instrument	Secondary
Fridge	Secondary
Social media app	Tertiary
Soya beans	Primary
Personal computer	Secondary
Airline ticket	Tertiary
Diamond mining	Primary

### Activity 2.2

- a The hospital is state owned and managed; the companies that service it are owned and managed by privately owned businesses.
- b Explain that a mixed economy is made up of organisations from both the public and private sectors. The hospital is a public sector business which is owned and controlled by the government. The companies that service it such as the cleaning company are owned and controlled by private sector owners and shareholders.

### Activity 2.3

- a Ganji Academy provides a service so it is in the tertiary sector.
- b Explain that Ganji Academy as a public sector organisation decides: what education service is provided, how the school provides the service and who receives the service provided by the school. Also explain that as it is providing an education service, profit is not its primary focus. Remember that effective analytical skills are needed here.

## Activity 2.4

- a Answers could include any **two** from: profit; revenue; units sold; cash-flow; brand strength; market share.
- b As a private sector business, the coffee shop responds to consumer demand, provides the service as a privately owned and controlled business and produces coffee to be sold to its customers.

## Activity 2.5

- a The tertiary sector is the service activities that support businesses and provide services to final consumers such as insurance and healthcare.
- b Possible objectives might include **two** of the following: increasing profit; increasing revenue; increasing customers served; effective management of cash-flow; improving brand image; improving customer service.
- c Explain the benefits for consumers of NPV being a private sector business, including: lower prices and better service from an efficiently run private sector company. The disadvantages for consumers include: higher prices and poorer service if the private sector company puts profit ahead of public service. The advantages for workers include: more flexible, less bureaucratic employer; possibility of higher wages. Evaluation of the disadvantages for workers: less job security and lower wages if the business puts profit as its main objective. Remember that you need to show clear analytical skills in your explanations along with evaluative skills each time you make a point. A justified conclusion is needed.

## 3 Enterprise, business growth and size

### Activity 3.1

Characteristic	Example
Innovative	has ideas about a new app
Self-motivated and determined	works very long hours
Self-confident	sells her business enthusiastically
Multi-skilled	has a degree in business and an accountancy qualification
Has strong leadership qualities	is never afraid to stand up in front of her workforce and talk about her vision for the business
Takes initiative	sorted out a funding problem by arranging a new type of loan
Results-driven	wants to achieve a revenue of \$5m in three years
Risk-taker	has used her house to secure a loan to start the business
Good networker	knows a large number of people in the industry

### Activity 3.2

- a **Four** ways that the government might support Himari could include: grants; low interest loans; low tax; rent-free premises; information; advice; subsidised training schemes.
- b **Two** elements that might be in a business plan could include: details of the entrepreneur and skills of the management; the business opportunity; the nature of the market; the aims of the business; detailed financial forecasts such as the income statement.
- c **Two** reasons the business plan might be useful to Himari's investors could include: potential returns from financial forecasts on profits and cash-flow; security of a loan or investment; and general future direction of the business, such as expansion into new markets. It is important to analyse the reasons by clearly demonstrating the usefulness of the plan to the investor.

### Activity 3.3

- a Market share, capital employed.
- b Explain that businesses are difficult to compare because they differ in terms of: the work of employees potential sales in the market and the number of employees needed to make a sale. Include analysis by making it clear how it is difficult to compare size.
- c Explain the benefits of government support which include: innovation in markets, employment, greater competition, lower prices and small businesses become large businesses. Analysis of the problems of government support includes: the cost of grants and subsidies, less tax revenue from tax advantages, and the cost of training schemes and advice. Analysis is important in this question so make the link between support and the reason. An overall and justified conclusion is needed.

### Activity 3.4

- a The **two** ways that TEMPO could expand might include: increasing the number of goods currently produced; increasing the number of new products sold; expanding into new markets for its products.
- b **Two** reasons for TEMPO expanding could include: to increase profits; to increase market share; to gain economies of scale; to increase market power; to protect itself against a takeover.
- c Explanation of **two** problems of growth for TEMPO might include: diseconomies of scale; problems of integrating with the German businesses in a takeover/merger; lack of new market knowledge; moving away from its core business. Good analytical skills are important here so link the problem to how it might affect TEMPO.

### Activity 3.5

- a **Four** reasons why businesses might fail could include: poor planning; liquidity problems; competition; poor marketing; poor management.
- b **Two** benefits of Salma being a small business might be: easier internal communication; greater flexibility; improved employee motivation; better relationships with customers.
- c Salma's strengths might include: growing market; use of local produce is popular; her skills and knowledge; a low-price and high-quality product.  
Her weaknesses might include: her inexperience in business; lack of finance; problems of entering a competitive market. This answer needs clear analysis of the strengths and weaknesses. An overall and justified conclusion that says whether Salma is in a good position or not is crucial.

## 4 Types of business organisation

### Activity 4.1

- a A partnership is a business owned by two or more people who will usually share responsibility for the day-to-day running of the business.
- b In the case of failure of a business, in limited liability, the owners risk losing only the amount that they have invested. In the case of unlimited liability, however, the owners are responsible for all of the debt of their business and may have to use their personal wealth.
- c Decision making: In a partnership, decision making is shared, whereas a sole trader makes all the decisions themselves and has full control over the business. While shared decision making can often lead to better decisions, it can also lead to conflict.

Access to capital: Partnerships have greater access to capital than sole traders as there is more than one person investing capital in the business. This makes it easier for partnerships to expand their business.

Other points may include: Profits are shared in a partnership.

- d** A sole trader might find it hard to compete with a larger firm because:
- Sole traders do not have as much access to funds as large firms do because banks will not lend money to them as easily. So, they will find it harder to invest in the latest technology or skills, making them less competitive.
  - Sole traders may lack some of the essential business skills needed for running a business whereas larger companies have the money to hire specialised workers and the reputation to retain them as well.

- e** Example answer: If Sam forms a partnership, he will have someone to share his workload. Having a partner may bring new ideas to improve the business and will also give him greater access to finance.

Working as a sole trader, however, Sam is used to having full control, making decisions on his own and being able to keep all the profits, which will not be the case in a partnership.

My recommendation would be for Sam to form a partnership as the extra funds and extra skills will be helpful with his expansion and painting and decorating plans. Having a partner will allow him to share the workload and be less stressed, which should help with maintaining his image of providing good service and completing jobs in time. He should make sure that he chooses a partner who can contribute expertise and extra funds.

## Activity 4.2

- a** A limited company is a company owned by shareholders who get shares in exchange for their investment. They are not responsible for the business's debts.
- b** Possible reasons why shareholders might be reluctant to become a public limited company might include:
- Loss of control over decision making: Currently, TM Textiles is owned by a very close group of friends and family members where the owners/shareholders have a lot of control but going public will mean many more shareholders. This will dilute the control of the existing shareholders and may lead to a conflict of interest between them and the business.
  - Difficult to manage: A public limited company can grow very quickly and become hard to manage. Decision making can be slow and inefficiencies in communication can arise in a big company with many shareholders compared to the ten shareholders involved in decision making now.

Other points may include: Risk of takeover of a public limited company.

- c** **Two** differences between private and public limited companies could include:
- Owners: Private limited companies usually have a very small number of shareholders who are often friends or members of the same family whereas public limited companies have a very large number of shareholders.
  - Borrowing finance: Private limited companies often find it difficult to raise finance because they are small businesses with low-value assets to offer as security against loans. Public limited companies, on the other hand, can often raise very large sums at good rates of interest because of their reputation and valuable collateral.

Other points may include: Easier to sell shares in a public limited company to raise finance; ownership and control are separated.

- d** Sample answer: If TM Textiles Pvt. Ltd decides to go public, then it will be able to raise the additional capital it needs for buying new machinery through a share issue to the public. However, the legal formalities for setting up a public limited company are more restrictive, time-consuming and costly.

If TM Textiles Pvt. Ltd decides to take a loan from a bank instead, it may find it difficult to get the amount of money it needs because banks usually need an asset as security before giving a loan. It also cannot raise capital easily through issue of additional shares as it can only sell to family and friends and permission is needed from the existing shareholders. It will, however, be able to keep the control of the business within the family and continue to benefit from the fast decision making that it currently has.

I think that TM Textiles should go public because it can raise more capital this way by issuing additional shares as well as borrowing from banks as banks are more likely to lend to a public limited company than to a private limited company. Successful expansion due to the funding will make up for the cost and complexity involved in setting it up.

Other points may include: Cost of interest in case of taking a loan.

### Activity 4.3

- a** A franchise is a business system where entrepreneurs buy the right to use the name, logo and product of an existing business.
- b** Owning an unincorporated business will mean that he will not have a separate identity from the business and may be at a disadvantage because:
- He will be personally responsible for any mishaps at his restaurant. For example, he may get sued if customers get ill after eating food at his restaurant.
  - He will also be fully liable for all the debts of the business and will have to pay back debts out of his personal savings that he has saved in the last ten years.

Other points may include: It will be more difficult to raise finance.

- c** **Two** factors that could be considered are:
- The owner's role in the management of the business: Some owners may want only to invest in a business and have nothing to do with the running of it. If this is the case, then an incorporated business organisation may be a better choice.
  - How quickly the owners want to start operating their business: Unincorporated businesses such as sole traders and partnerships are easier to set up than incorporated ones and so are quicker to start running.

Other points may include: How much capital they have and how they can raise further capital; whether they have the required skills to set up and run the business on their own.

- d** **Four** advantages to Nanda of investing in a franchise might include:
- There is less chance of business failure: Since the national fast-food brand that Nanda plans to buy a franchise for is already popular and is already well established, there are fewer risks and more chances of success.
  - Advice and training by the franchisor: This will help Nanda in the initial setting up of the restaurant, which can be quite difficult for someone like him who is starting a business for the first time.
  - The franchisor will promote the brand: The franchisor will help with financing the promotion of the fast-food brand through national advertising, which will help Nanda keep his advertising costs low.
  - Assured quality of ingredients: The franchisor will already have checked the quality of suppliers, so the franchisee is guaranteed quality supplies.

## 5 Business objectives and stakeholder objectives

### Activity 5.1

- a** A business objective is a statement of a specific target to be achieved by the business in a certain amount of time.
- b** The criteria should be:
- specific
  - measurable
  - achievable and agreed
  - realistic and relevant
  - time-specific.

- c** Here are **four** possible objectives of TekSmart Pvt. Ltd could include:
- To make a profit: Given that Swami and Vina's friends are experts, they will bring new ideas and possibly even new capital to the business, which should increase the profit of the business compared to before.
  - To expand the business: They could measure this by looking at the total revenue earned and the number of clients compared to what they have now.
  - To increase its market share: If its market share increases among the small- to medium-sized businesses that it serves, then it will develop a strong brand image which will help them get more business.
  - To be socially responsible: TekSmart Pvt. Ltd should take business decisions that are socially, ethically and environmentally responsible. For example, it should make sure that it does not use any pirated software in its software development activities.

Note: Survival would not be an objective as TekSmart Pvt. Ltd is in its fourth year.

## Activity 5.2

- a** A social enterprise is a business with social objectives that reinvests most of its profits back into the business or into benefitting society at large.
- b** Kamaria will have different objectives for her shop and her social enterprise:
- Kamaria will have a profit-making objective for her shop while her social enterprise will have an objective of benefitting the villagers who make the handicraft items.
  - The profit obtained from the shop will be for Kamaria to use personally or to invest back into her shop. The profits from the social enterprise, however, will be invested back into the business in order to benefit the villagers.
- c** **Two** characteristics might include: owned and controlled by the state; financed mainly through taxation; they have social objectives rather than profit objectives; their services are often provided free or at a low cost.
- d** The public corporations may provide the following services for free or at a low price to all villagers:
- Giving some basic training to the villagers in running and managing a small business so that they are more efficient in what they do.
  - Holding exhibitions for the villagers to show their handicraft products so that they can market their products and meet potential buyers, business partners and investors.

## Activity 5.3

- a** Internal stakeholders are people who have an interest in the decisions and activities of a business and are part of the business, for example, owners and employees. External stakeholders are people who have an interest in the decisions and activities of a business but are not part of the business, for example, customers and suppliers.
- b** Local community: They would want to benefit from the jobs at the CHL chocolate factory and other infrastructural facilities created by CHL Group.
- Shareholders: The owners/shareholders, who are all family members, have invested money into the business and would want their business to grow and earn profits so that they can get high returns/dividends.
- Current suppliers in another country: Those who currently supply cocoa to CHL Group would want to be treated fairly and receive prompt payment for their supplies.
- Other stakeholders may include: customers, workers, suppliers in the home country, government.
- c** Example answer: The objective of CHL Group was survival to start with because at first its short-term objective would have been to establish a good relationship with the suppliers in another country and understand the operational and marketing considerations. Now that it has

established itself and managed to survive (make enough revenue to cover its costs) for a year or two, then it can review and improve its current operations and think of objectives such as profit and growth. The objectives of profit and growth can be achieved when the business manages to have good revenue and is able to control its costs, for example by expanding and gaining through economies of scale. To be able to do this, it needs to survive the first few years and establish itself first.

- d** Example answer: The local community and the suppliers from another country may have conflicting objectives; for instance, the local community would want more local jobs and would want CHL Group to source its cocoa locally, whereas the suppliers from another country would want CHL Group to continue buying from them.

Similarly, the local community and the owners would have conflicting objectives as well. The owners do not want to change their suppliers because they have concerns about the quality from the local suppliers, whereas the local community wants CHL Group to source its cocoa locally.

## Exam-style practice questions

- a** The public sector is the part of the economy that is controlled by the state or government [K]. This would be a state-run hospital in the case scenario.
- b** The tertiary sector is firms that supply a service to consumers and other businesses [K]. As a taxi firm, Quick Route Ltd is a service sector business and part of the tertiary sector.
- c** The first reason Quick Route Ltd would want to expand its business is to increase profits [K]. As a larger firm, its revenue will rise, and this will lead to a rise in profits [App]. The second reason would be to increase its market share [K]. This means that it would have more of the total market sales in the town. The increase in market share could give the business greater market power in the taxi market [App].
- d** The first way that Quick Route Ltd will be affected by being a private sector business is that it will need to make profit on its activities [App]. Profit is important because it is the return the owners/shareholders get from the risk of setting up in the taxi market [App]. Without a profit, there would be no incentive for the owners to set up the business [An]. The second way that Quick Route Ltd is affected by being a private sector business is that it experiences the risk of bankruptcy [App]. If Quick Route Ltd operates a poor service, it will not make the revenue needed to satisfy its investors and it will go out of business. This is particularly the case if Quick Route Ltd is unable to repay its loans to the bank [An].
- e** The first way that Quick Route Ltd benefits from targeting **three** types of customer is that it is able to spread risk [K] across three different market segments. This is important when one part of the market experiences a fall in sales [K]. For example, this might be the case if the local contracts have a fall in sales [App] and Quick Route Ltd can increase its sales in the executive cars [An]. This may prove difficult, however, if the business has a limited number of executive cars [Ev]. Secondly, operating in different markets gives Quick Route Ltd the opportunity to increase sales revenue [K]. If, for example, the regular market and contract market do not experience any growth, then the executive market can give the business the potential to increase sales [An]. Finally, operating in three markets gives Quick Route Ltd the chance of increasing its profit margins [App]. This would be the case in the contract and executive markets where consumers are willing to pay higher prices [An]. It may be the case, however, that these markets have higher costs, such as the investment costs in executive cars [Ev]. Operating in three markets does, however, mean that Quick Route Ltd might lose some of the benefits of specialisation [Ev]. It may do better to focus on contract hire, for example, because Quick Route Ltd can be known in the market for this as a unique selling point [Ev]. In conclusion, the benefits of spreading risk seem to be crucial here so operating in three markets does seem to have benefitted Quick Route Ltd [Ev].

## Exam-style case study

### Boiling Point Ltd

- 1 a** Explanations of **two** ways that Boiling Point could add value from: branding; excellent service quality; product features; convenience.
- b** Explanation of the factors that are important for Eskor as an entrepreneur:  
 Innovation: to develop new products.  
 Self-motivation and determination: can keep going when business gets difficult.  
 Strong leadership qualities: the ability to motivate others.  
 Conclusion: Discussion leading to which, in your opinion, is the most important factor. For example, self-motivation and determination may be the most important factor for Eskor to overcome the difficulties faced by such a new business.
- 2 a** Reason 1: For job creation [K] by the business.  
 Explanation: Governments are interested in maintaining low rates of unemployment and employment by a business like Boiling Point Ltd is crucial in achieving this [App]. This could be important in a town or region in Ethiopia where unemployment is high and the jobs that Boiling Point Ltd creates improve the welfare of people [An].  
 Reason 2: This type of business develops new ideas and is innovative [K].  
 Explanation: These innovations are important for the overall development of the Ethiopian economy [App]. If Boiling Point Ltd, for example, develops a new energy-efficient heating system for its kettles, then this could be used throughout the Ethiopian economy and improve wider energy efficiency [An].
- b** The first benefit of Boiling Point Ltd increasing in size is economies of scale. These are the costs of advantages of Boiling Point Ltd operating at a greater scale of production [K]. An example of this would be technical economies of scale where Boiling Point Ltd is able to produce its kettles with technically advanced large-capacity machinery and equipment [App]. The efficiency advantages of doing this lead to falling unit costs so that each kettle can be produced at a lower average cost [An]. Lower average costs mean that Boiling Point Ltd can reduce its prices and increase market share or it can have larger profit margins and increase profits [An]. There is, however, a risk of growth leading to diseconomies of scale, such as communication difficulties, which could increase Boiling Point Ltd's unit costs [Ev].  
 Greater power to control the market means that Boiling Point Ltd uses the market share it gains through growth to have greater control over price [K]. It could, for example, achieve a higher price for its kettles because of its brand influence in the minds of Ethiopian consumers [App]. The higher price could mean greater profit margin on each kettle it sells, which in turn could mean higher total profit [An]. There may, however, be a risk that greater market power attracts the attention of government regulators [Ev].  
 Boiling Point Ltd's growth could mean a rise in total profit as the business sells more kettles [K]. Assuming that revenue rises faster than cost, then total profit will rise [Ev]. This profit could be reinvested in the business and, for example, fund development in technology [An]. There is, however, the risk that cost could increase faster than revenue, especially if investment is needed in capital to increase capacity [Ev].  
 In conclusion, the increase in profit may be the most important benefit if, for example, greater profits could be used to reinvest in Boiling Point Ltd's future growth [Ev]. Economies of scale and the increase in profit margin from having greater power to control the markets are more short-term benefits but the long-term success for Boiling Point Ltd is most likely to come from reinvesting profits [Ev].
- 3 a** Explanation of **four** reasons for business failure from: poor planning and lack of objectives; liquidity problems; poor choice of location; poor management; failure to invest in new technologies; poor marketing; lack of finance; poor economic conditions; high level of competition.

- b** Explanation of each of the options for Boiling Point in Appendix 1:
  - Boiling Point should enter the new market on its own: It has the independence to do things its own way and may not wish to be linked to the unethical behaviour of #Kitchen Services.
  - Boiling Point should enter the new market as a joint venture with #Kitchen Services: #Kitchen Services will give Boiling Point support and expertise and it already has good links with the European market.
  - Boiling Point should not enter the market: It can reduce risk by keeping the business in a market it understands.
  - Conclusion: Discussion leading to a suggestion of which option to choose. For example, you might say that Boiling Point should enter the new market as a joint venture because of #Kitchen Services' expertise.
- 4 a** Explanation of the interests of **four** different stakeholders from: owners and shareholders (profits); managers (bonuses); employees (job security); lenders (security of a loan); suppliers (payment of credit); customers (security of supply); government (tax payments); local community (employment).
- b** Explain the benefits of Boiling Point expanding into the European market in terms of:
  - Sales: increased sales will generate more cash for the business.
  - Profit: increased profit can be used to fund new innovation.
  - Risk: this can be spread by diversifying and producing in different markets.
  - Conclusion: Discussion leading to a focus on the most important benefit, for example, the reduced risk for Boiling Point of operating across different markets.

## 6 Motivating employees

### Activity 6.1

Quote	Reason
'I enjoy meeting so many new people working on reception'	interesting work
'I like the feeling of being in charge of a large group of employees'	responsibility
'It is really good to be able to stay at other hotels in our chain at discounted rates'	fringe benefits
'The income I earn as the conference manager gives me a good standard of living'	pay
'I like the opportunity to make progress to more senior jobs in the hotel'	promotion
'I really enjoy the company of the team of people I work with in the kitchen'	friendship
'I have learnt so many new skills since I've worked with this business'	training
'Being the manager of the hotel means that people really look up to you'	status

### Activity 6.2

- a** Production is the total output of an organisation and productivity is the output per employee.
- b** Well-motivated workers may be more satisfied at work and are less likely to be absent from their job.
- c Two** benefits could include: reduced training costs; reduced recruitment costs; retaining skilled employees. It is important to analyse the link between lower labour turnover and its benefits. For example, if workers stay at a business longer, it means that not as much has to be spent training new workers.

## Activity 6.3

Quote	Need
'I feel under-valued because my job title is not respected'	esteem
'The pay we get is not enough to meet the cost of living'	physical
'I often work on my own in the shop, which makes it boring'	social
'I often worry about losing my job because people are often sacked'	security
'I don't feel I can reach my potential with this business'	self-actualisation

## Activity 6.4

- a** **Two** factors associated with the 'scientific management theory' could include: economic man; piece rates; money as a motivator.
- b** **Two** hygiene factors that Capture might use could include: pay; conditions; relationship with others; supervision; company policy.
- c** Herzberg's motivators allow workers to access esteem and self-actualisation in the hierarchy of needs, which raises their motivation at work. Make sure that you analyse how, for example, responsibility makes a worker more motivated.

## Activity 6.5

Example	Financial reward
The managers at an insurance company will be paid an additional \$5000 on top of their salary if they achieve their performance target.	bonus scheme
The sales staff at a car show room are paid \$500 for each car they sell.	commission
A retail chain pays a \$4000 bonus to each of its employees because of the profit it has made.	profit sharing
A shoe manufacturer pays its employees \$2.50 for each pair of shoes they produce.	piece rate
Managers in public sector hospitals are paid \$80 000 per year.	salary
The staff in a fast-food restaurant are paid \$10 per hour.	hourly wage rate
Senior staff at a publishing company are given private health insurance.	fringe benefit

## Activity 6.6

- a** **Two** characteristics of quality circles might include: groups of employees who meet regularly to discuss work-related problems; employees are given the responsibility to improve quality.
- b** Explain that job enlargement is increasing or widening tasks and job rotation is increasing the variety of tasks in the workplace. Make sure that you analyse how responsibility might improve motivation. An example would be really useful to support this.
- c** Explain Maslow's and Herzberg's theories showing how job enrichment might increase employees' motivation, thus making workers more productive and improving the supermarket's performance. Discuss how job enrichment may, however, increase costs and take time to work. You need to use analysis and evaluation of job enrichment. Make sure that you conclude your answer by, for example, picking out the most important reason why job enrichment might improve the supermarket's performance.

## 7 Organisation and management

### Activity 7.1

Job type	Functional department
Production line workers	operations
Management accountant	finance
Technicians involved in testing new products	research and development
The employees that manage workers' contracts	human resources
The team of staff that work on promotional campaigns	marketing

### Activity 7.2

- The span of control is the number of subordinates reporting to each supervisor/manager. If a manager has five subordinates, the span of control is five.
- Two** factors that determine span of control might include: skill of the manager; nature of the workforce; the task.
- Explain that managers become responsible for more workers as the number of managers is reduced when layers of hierarchy are removed. Do not forget to be analytical by clearly making the link between reduced layers in the hierarchy and managers being responsible for managing more workers.

### Activity 7.3

- Delegation at Pug Gym would mean passing authority down through the organisational hierarchy to a subordinate. For example, Jackson might ask one of his staff to decide what time is best to schedule a gym class.
- Two** characteristics of autocratic leadership could include: centralised decision making; one-way communication; limited involvement of workers in decision making.
- Consider the possible benefits of a democratic management style: access to higher levels of the 'hierarchy of needs', which are Herzberg's 'motivators'; involvement in decision making increases motivation. Discuss the possible problems of democratic management: it slows down decision making and it is not possible in certain situations. Make sure that you show analytical skills when you explain the benefits of democratic management and that your discussion of the possible problems is evaluative. You need to finish with a conclusion – would Pug Gym benefit from democratic management?

### Activity 7.4

Example	Function
A team of employees have to report their monthly sales figures to a manager.	controlling
A manager holds a team meeting because they feel that the team is under-performing.	commanding
Managers hold a meeting to work out a strategy to achieve the coming year's profit target.	planning
A manager puts together the resources that each team will need when they are going out to sell to customers.	organising
The sales manager works with the production manager to make sure that enough of the final product will be available to meet customer demand.	coordinating

## Activity 7.5

- a** **Two** functions of company directors might include: setting strategy; reviewing managers' performance; protecting interests of shareholders; providing leadership.
- b** **Two** characteristics of democratic management might include: delegation; two-way communication; decentralised decision making; a high level of consultation with employees.
- c** **One** problem of decentralised decision making might include: can be time-consuming; can lead to a loss of management control; can make the decision-making process more complex. Try to be analytical here by making the link between decentralised decision making and problems such as loss of management control.
- d** Explain that benefits of better relationships between management and the trade union may include: fewer industrial disputes; more motivated employees; easier decision making. Discuss that failing to improve the relationship may: slow down decision making; lead to higher business costs; cause a conflict of objectives. Remember that it is important to be analytical in the first part of this answer when you explain why better relationships between managers and the trade union will benefit the business. You also need to be evaluative of these benefits and come to a final conclusion.

## 8 Recruitment, selection and training of employees

### Activity 8.1

- a** Internal recruitment is filling a vacant post with someone already employed in the business and external recruitment is filling a vacant post with somebody not already employed in the business.
- b** **Two** benefits to Peace of Mind Security of internal recruitment might include: filling vacancies more quickly; an employee already knows the business; the business knows the strengths and weaknesses of an employee; a promotion opportunity can motivate employees.
- c** Reasons why external recruitment has higher costs than internal recruitment include: it takes longer to fill vacancies; the process costs of recruitment are higher; external candidates usually need more training. Effective analysis is important here, so develop the link between external recruitment and costs such as training.

### Activity 8.2

Stage	Number order
A shortlist is selected from all the applicants.	7
Application forms and job details are sent out.	5
A person specification is produced.	3
The business identifies the need for a new employee and carries out a job analysis.	1
The right candidate is selected.	9
A <b>job description</b> is produced.	2
The job is advertised.	4
Completed applications are received.	6
Shortlisted candidates are interviewed.	8

### Activity 8.3

- a** On-the-job training happens at the workplace and involves watching or following an experienced employee. Off-the-job training takes place away from the workplace, for example at a college, university or a specialist training provider's premises.
- b Two** advantages of using on-the-job training could include: low training costs; employees learn what the business wants; employees are producing while they are learning. Show your analytical skills by developing an advantage of on-the-job training to show how this reduces training costs. An example would be really useful to support this.
- c Two** reasons why on-the-job training might not be effective could include: existing employees' bad habits might be learnt; trainees might not learn the most up-to-date methods; mistakes made by employees when learning have costs; it slows down the production of experienced employees. Make sure that you analyse the problems of on-the-job training such as mistakes made by employees.

### Activity 8.4

- a Four** details of a contract of employment might include: name of employer; name of employee; date of commencement; pay; hours to be worked; job title; responsibilities; holiday entitlement; notice time; disciplinary procedure.
- b Two** factors to take into account when deciding to retain a worker or make them redundant might include: productivity of the employee; the employee's discipline; absenteeism of the employee; the employee's age.
- c** Explain that the minimum wage directly increases the cost of an employee and this increases labour costs. Health and safety regulations lead to higher costs as new systems and equipment are needed. Remember to be analytical in your approach by, for example, making the link between the minimum wage and higher labour costs.
- d** Consider that too much employment regulation could be bad for an employer such as Jouer Et Apprendre because it might slow down decision making; lead to a rise in bureaucracy; and increase labour costs. Discuss how regulation might protect workers and could make Jouer Et Apprendre more socially responsible. Make sure that you are analytical in developing your reason why regulation may be bad for the business. You also need to be evaluative and come to a final conclusion.

### Activity 8.5

- a** A job description lists the key points about a job: job title; key duties; responsibilities; accountability.
- b Four** stages in the recruitment process might be: identify the need for a new employee; produce a person specification; produce a job description; advertise the job; send application forms; interview candidates; select a candidate.
- c** Far and Wide would use training outside the business at a training company and/or college. This could give employees wider outside experience in terms of issuing tickets and processing payments.
- d Two** benefits of off-the-job training for Far and Wide might include: specialist trainers; no distraction of work; mistakes at work are not made; latest methods are covered. Remember to show your analytical skills here by clearly making the link between off-the-job training and its benefits. An example would be very useful here.
- e** Explain that the benefits of retaining employees during a downturn include: keeping skilled and experienced workers; no cost of redundancy; maintaining the morale of the workforce. Discuss the possible problems of retaining employees: wage costs will need to be covered in a recession; there may not be enough work for the retained labour force. Develop your explanation by analysing the benefits of retaining employees, such as reduced training costs. You must also evaluate these benefits and justify your final conclusion.

## 9 Internal and external communication

### Activity 9.1

Example	Internal/ external
An email is sent by senior managers to A Tread Plc's employees about new data protection rules.	internal
A Tread Plc does a telephone survey with potential customers.	external
A Tread Plc's finance director has a face-to-face meeting with the bank.	external
The CEO has a monthly online meeting with A Tread Plc's management.	internal
A Tread Plc holds a meeting with local residents who live near one of its factories.	external
A monthly newsletter is posted on A Tread Plc's intranet platform for all its employees.	internal

### Activity 9.2

- a Two** characteristics of effective communication might include: clear information passes between two or more people or groups; feedback is given to confirm that the message has been received and understood.
- b Four** types of communication media might include: oral; written; electronic; visual.
- c Two** benefits of effective communication might be: reduced risk of mistakes; faster decision making; quicker response to market changes; improved coordination; improved motivation; improved customer relationships.
- d** Face-to-face communication might improve JLK's performance through: improved quality of feedback; being good for discussion; encouraging two-way communication. Analyse, for example, how face-to-face communication develops two-way communication, which encourages employee involvement in decision making. An example would be very useful to support this.

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### Activity 9.3

Benefit	Limitation	Communication method
personal contact between sender and receiver	no permanent record	oral
provides a permanent record	feedback is slower	written
can be sent to many receivers at the same time	can be accessed by people who are not intended receivers	electronic
creates interest and grabs attention	can be misinterpreted	visual

### Activity 9.4

- a Four** types of electronic communication could include: email; text; social media; intranet; video conferencing.
- b Two** factors that account for Open Sky's choice of electronic communication could include: large number of recipients; significant visual impact; gives a record of communication; a fast speed of delivery.
- c Two** problems of electronic communication might include: too many messages are sent and received; the high cost of setting up the system; possible technical problems; the possible loss of confidentiality. Analysis of the problems is crucial and this should be supported with an example from Open Sky.

## Activity 9.5

- a** Two-way communication is where the receiver is allowed to respond to the message and the sender listens to the response.
- b Two** reasons why a long communication channel might lead to poor communication might be: it could lead to distorted information; senders/receivers can manipulate messages; it is a time-consuming method.
- c Two** negative consequences of poor communication could be: a task may not be completed; it could lead to a fall in motivation; it may damage the business's reputation; some tasks may be done poorly. Show your analytical skills by developing the negative consequences of poor communication, such as poorly motivated employees.
- d** Explain how two-way and short-channel communication would reduce misinterpreted communication in the local government office and improve feedback. Discuss how two-way communication may, however, be more time-consuming and how short-channel communication could lead to increases in cost. Start this answer by fully analysing the benefits of two-way, short-channel communication for the local government office.

## Activity 9.6

- a** Feedback is the receiver's response to a message.
- b Two** forms of written communication might include: noticeboard; memorandum; letter; email.
- c Two** benefits to K&C of effective communication might be: effective completion of tasks; improved motivation; greater efficiency; less conflict between people in the organisation. You must be analytical here when you explain how effective communication, for example, improves employee motivation.
- d Two** problems of using oral communication might include: it can be time-consuming; there is no record of the communication; the receiver may not hear clearly. Analyse the problems of using oral communication. A relevant case example would be useful to support this.
- e** The benefits to K&C of using the intranet and an app might be: faster communication; quicker feedback; effective visual presentation; a record of the communication. Discuss how the intranet and app may, however, be expensive to set up and how there could be a loss of confidentiality. Be clear in your analysis of K&C using the intranet and an app, but also evaluate these benefits and come to a final conclusion.

## Exam-style practice questions

- a** Effective communication is when information passes between two or more people or groups, with feedback given to confirm that the message has been received and understood [K].
- b**  $\text{Output} / \text{number of workers} = \text{labour productivity}$  [K].
- c** The first characteristic of democratic management is delegated decision making [K]. This is where managers at ARB pass on responsibility for decision making to their subordinates [App]. For example, managers at ARB allow employees to make decisions on the new communication system [App].  
The second characteristic is two-way communication between subordinates and managers [K]. This, for example, could be where managers at ARB discuss the introduction of electronic communication with their subordinates [App].
- d** The first of Herzberg's motivators could be responsibility [K]. This is where employees at ARB are given responsibility to manage particular areas of the business, such as an employee being put in charge of a set of customer accounts and having to manage these effectively [App]. This could motivate the employee because their work and decision making are being judged based on how well they manage the accounts [An]. The second motivator could be recognition at work [K] where an employee at ARB is recognised for the quality of the work they do [App]. If, for example, an employee has responsibility for signing up new customers and they do this successfully, they

might be recognised by a senior manager who discusses their good performance with them at a meeting [App]. The recognition may improve the employee's motivation because they feel appreciated at work for their achievements [An].

- e** Internal communication is within the organisation at ARB [K]. The first consequence of poor internal communication is that tasks may not be completed effectively [K]. For example, an employee does not receive accurate information about managing an account and this causes them to make a mistake with a customer [App]. This could result in ARB losing customers and seeing profits fall [An]. The second consequence could be a negative impact of employee motivation [K]. Workers who, for example, do not feel well informed about decisions may become demotivated and do not do their work as effectively [App]. This could increase costs and reduce the bank's profits [An]. A third way that ARB may be adversely affected by poor internal communication would be ineffective decision making [K]. Managers, for example, need accurate information to make effective decisions. If a manager at ARB wants to close a branch, they need to know precise information about the branch's revenues and costs to make the decision [App]. If they do not have accurate information, they may close a branch unnecessarily [An]. In conclusion, ARB has problems with internal communication but it may also have other problems such as management style and changes in the market [Ev]. Without more detailed information about other problems, it is quite difficult to say whether this is the biggest problem, although it is certainly a problem for ARB [Ev].

## Exam-style case study

### Aspire Ltd

- 1 a** Reason 1: It could improve the efficiency of the labour force [K].

Explanation: If the computer game designers are well trained, they can do tasks more quickly and they are less likely to make mistakes, which improves Aspire's efficiency [App]. Improved efficiency can reduce Aspire's costs [An]. This could lead to lower prices, which would increase Aspire's revenues and increase its profits [An].

Reason 2: It could improve worker motivation [K].

Explanation: If computer game designers at Aspire have better skills, then this improves the quality of their work, which raises their motivation [An]. This could be seen as one of Herzberg's motivating factors at work [App]. If workers become more motivated, they will be more effective in their work and they could produce better-quality computer games. This could increase Aspire's revenues and profits [An].

- b** Low cost: On-the-job training means that employees at Aspire are trained at the business [K]. This would mean that new and existing workers are trained by Aspire's experienced staff [App]. This method can be relatively low cost because workers do not have to leave the business to go to, for example, a college where a payment is made for the training [An]. This could improve Aspire's profit margins [An].

Learn the way that Aspire wants: This is done through on-the-job training, which develops workers so that they are more likely to meet Aspire's specific needs [App]. For example, the computer game designers produce games that are specific to the Aspire brand which is attractive to their customers [App]. This could increase Aspire's brand loyalty, increasing revenues and profits [An].

Producing while training: This also happens through on-the-job training [K]. This means that workers are adding value to the business even when they are training [K]. If workers were away from the business, they would not be contributing to Aspire's output [An]. The output that on-the-job trainees contribute could increase Aspire's revenues and profits [An]. On-the-job training does come with some disadvantages as the time spent by employees training staff could reduce the productivity of the staff doing the training [Ev]. Also, the quality of the work done by the staff who are undergoing training may not be that good and this could reduce Aspire's efficiency [Ev].

Conclusion: Probably the most significant benefit is training staff the 'Aspire' way. This strengthens its brand and supports the future development of the business [Ev].

- 2 a Two** benefits, with explanations, to Aspire of a highly motivated labour force from: improved productivity; low rate of absenteeism; low rate of labour turnover; better quality of goods and services produced; Aspire becomes more competitive.
- b** Explanation of how the following might motivate workers in the following ways:  
 Salary and wages: financial incentives.  
 Recognition of achievement: one of Herzberg's motivators.  
 The quality of the work: reaching the highest levels in Maslow's hierarchy of needs.  
 Conclusion: Your discussion could be, for example, that the quality of the work itself is the most important factor at Aspire because of the nature of the people who work in the computer games industry.
- 3 a** Explanation of **four** factors that influence the span of control from: the difficulty of the tasks; the experience and skills of the employees; the size of the business; how many levels of hierarchy there are; the management style.
- b** Explanation of how the following factors might affect Francesca's leadership style:  
 Nature of the workforce: the more skilled, the more democratic.  
 Personality of the manager: more liberal may mean more democratic.  
 Task to be completed: long-term game design may mean more democratic leadership.  
 Conclusion: Your discussion might include, for example, that the most important factor is Francesca's personality because this is something that a manager finds difficult to change.
- 4 a Four** benefits to Aspire of effective communication could include: reduces the risks of mistakes; enables faster decision making; gives quicker response to market changes; improves coordination between departments; improves motivation of the workforce; improves customer relationships. Make sure that you include explanations as to how your four benefits apply to Aspire.
- b** Electronic communication  
 Advantages might include: its speed; a record of communication can be kept; many receivers can be reached at the same time. Make sure that you explain how this advantage might apply to Aspire.  
 Disadvantages might include: excessive number of messages; messages may be misunderstood; setting up the system might be expensive. Make sure that you explain how this disadvantage might apply to Aspire.
- Oral communication  
 Advantages might include: personal communication; immediate feedback; two-way communication. Make sure that you explain how this advantage might apply to Aspire.  
 Disadvantages might include: limited number of people can be communicated with; maybe no record of communication; it is time-consuming. Make sure that you explain how this disadvantage might apply to Aspire.  
 Conclusion: Discuss which method is most effective, justifying how it applies to the nature of the communication situation.

## 10 Marketing, competition and the customer

### Activity 10.1

- a** Customer base is the group of customers that a business sells its products to and market segment is a part of the whole market in which consumers have specific characteristics.
- b** RinxTV might identify consumer wants through market research. Define market research and give an example in context.
- c** Explain the popularity of sports and drama amongst consumers and how consumers are attracted to these products so they will keep buying RinxTV products because of sports and drama. Make sure that you clearly analyse the link between how sports and drama might build brand loyalty for a media business.

### Activity 10.2

Reason	Example
The price of the product	A newspaper business decides to aggressively discount its product.
The price of competitors' products	A low-cost airline loses sales because of the fall in price of a major international airline.
Changes in consumer income	A house builder experiences a rise in demand because average wages in the economy have increased in the last two years.
Changes in tastes and fashion	The sales of a novelty toy rise by 200% in a year because it is seen as a 'must have' product by children.
Spending on advertising and promotion	The market share of a sports goods company rises significantly when a business pays for its tennis racket to be used by the world's number one tennis player.
Changes in population size and structure	A drugs company sees a rise in demand for a drug used to treat arthritis suffered by people over a certain age.

### Activity 10.3

- a** **Four** government actions might include: changes in legal controls; deregulation; free trade agreement; tax changes; government loans being introduced; changes in subsidies.
- b** A rise in minimum wage could increase labour costs and health and safety legislation could add to administrative and capital costs.
- c** Digital books are competition for physically published books so the increase in the digital book market could lead to a fall in Punto Libro Books Ltd's sales. Remember to clearly show your analytical skills by fully developing how digital books are competition for published books. An example would also be very useful to illustrate your answer.

### Activity 10.4

- a** Niche marketing means developing products for a small segment of the market, whilst mass marketing is selling the same product to the whole market.
- b** **Two** benefits of selling in a niche market might include: higher profit margins; less competition; easier to compete against large firms; develop stronger brand loyalty.
- c** Selling to the mass market means higher sales for Cleanall, which leads to economies of scale, giving lower average/unit costs, which increase profit margins and total profit. Use your analytical skills to fully develop the relationship between mass marketing and, for example, how this increases Cleanall's profits.

## Activity 10.5

- a Market segment is the part of the whole market in which consumers have specific characteristics.
- b The **two** types of segmentation are: demographic (women / young athletes) and psychographic (runners).
- c The benefits of segmentation for Yousport are: products can be specifically designed to meet the needs of the consumers, marketing strategies such as advertising can be better targeted and higher prices can be charged. This could increase Yousport's market share but other firms may also be successful and the right market segments need to be targeted. Show your analytical skills by developing the benefits of segmentation and then evaluate the points that you have made. You must then come to a final conclusion. Do not forget examples to support the points that you make.

## 11 Market research

### Activity 11.1

- a Market research: the process of collecting, recording and analysing data about the customers, competitors and market for a product.
- b **Four** ways that market research can help Southern B include: find out about what customers like and dislike about products; identify tastes and preferences; help decisions on the marketing mix; know about market size; predict how the demand for a product might change.
- c To be more market orientated, SouthernB needs to make sure that its service is developed based on its market research to how customers would react to 'comfort and reliability'. Analysis is critical in this answer so clearly develop the points on how SouthernB can be more market orientated and support this with examples.

### Activity 11.2

Example	Types of research
The marketing manager at the shop buys a market research report on the cycling market in the country.	secondary
A person is interviewed about the types of cycling they do.	primary
A student who works part-time at the shop spends a week researching news articles on the internet about the cycling market.	secondary
The shop manager sends an email questionnaire to customers asking them about their satisfaction with the shop's product range.	primary
The owner of the shop uses government publications to find out about population and income in the local area.	secondary
A group of customers is invited to the shop talk about cycling equipment.	primary

### Activity 11.3

- a Market orientated is where a business develops products based on consumer demand as identified by the market research. Product orientated is where a firm decides what to produce and then tries to find the buyers for the product.
- b **Two** types of secondary research could include: government publications; market research reports; internet; newspapers and magazines; business records.
- c **Two** benefits could be: it provides information specific to the business; it is up to date; it is not available to other businesses. Use analysis to clearly develop the benefits of market research to LJK.

## Activity 11.4

- a** **Four** ways that market research data can be displayed could include: tables; bar charts; pie charts; pictograms; line graphs.
- b** Sampling could be used because it reduces research time and reduces cost.
- c** Explain the strengths of primary research: it provides information specific to the business, it is up to date and it is not available to other businesses. Its weaknesses are that it costs and it is time-consuming. You are likely to conclude that it is the only effective way of getting information specific to Safe-sure's consumers. Develop your analysis of the benefits of primary research to Safe-sure and then evaluate these benefits. Make sure that you come to a final conclusion to justify your argument.

## Activity 11.5

- a** Total online purchases in 2017 = 141. Music purchases = 32. So, percentage of music purchases =  $32/141 \times 100 = 22.7\%$ .
- b** Film purchases in 2015 = 20. Film purchases in 2017 = 30. So, percentage increase =  $(30-20)/20 \times 100 = 50\%$ .
- c** The pie chart and the bar chart show an increase in the number of purchases made by the sample group from 2015 to 2017 and if this represents the market then the value of sales over the period would have increased. Discuss how this is a small sample which may not be representative of the whole market; the data covers only the number of purchases but there is no data on value; and there are only five products in the data which is a very small part of total online sales.

## 12 Marketing mix: product and price

### Activity 12.1

- a** A product is the goods and services produced to satisfy a customer need or want. A brand is the name, image or symbol that distinguishes a product from competitors' products.
- b** **Two** product development costs could include: market research; capital expenditure; finance costs.
- c** **Two** benefits of the new product might be: increased revenue; increased profit; keeping up with the competition; spreading risk across different markets. It is important to fully analyse your two benefits by showing the connection between the new product and increased revenues. An example here is important.

### Activity 12.2

- a** The **four** phases of the product life cycle are: introduction, growth, maturity and decline.
- b** **Two** characteristics of the maturity phase of the product life cycle could include: sales have peaked; sales are constant; it is the most profitable phase of the life cycle.
- c** **Two** extension strategies could include: finding a new market for its products; finding new uses for its products; adapting the product; changing the packaging; increasing promotional activity. Do not forget to analyse your extension strategy and use an example to illustrate it from the case scenario.

### Activity 12.3

Example	Pricing method
A confectionary manufacturer sets a discount price when it launches a new chocolate bar.	penetration pricing
A coffee shop bases the price of a cup of coffee on the cost of producing the coffee.	cost-plus pricing
A computer game company sets a high price when a product is first launched.	market skimming
A petrol retailer tries to match the price of other petrol retailers in the area.	competitive pricing
A computer retailer discounts the price of its laptops and PCs to sell more accessories.	promotional pricing

### Activity 12.4

- Four** factors could include: new or existing product; how unique the product is; how much competition there is for YooU; how strong the brand is; the costs of production; YooU's marketing objectives.
- YooU needs to work out the costs of operating a flight, dividing this cost by the number of seats on the flight to get a cost per seat and then adding a mark-up to get the ticket price.
- Loss leadership involves setting a low price for flight tickets and then selling insurance, hotels and seat selection at higher prices to make a profit on these products. Analyse how loss leadership can be used here by referring to YooU Air as an example.

### Activity 12.5

- Price elasticity of demand measures how much demand (sales) for a product changes when there is a change in its price.
- Consumers are more likely to have to stay in a hotel at weekends when they have time off and this makes demand more inelastic.
- Demand tends to be more elastic during the week and revenue rises when price is reduced when demand is price elastic. It is crucial to analyse how elasticity affects revenue when price is changed in this case. Using a numerical example could be useful here.
- Explain that consumer demand is important when setting price in terms of: what the consumer is willing to pay, the PED, and what the competition's price is. Consider other factors that affect price such as cost and alternative marketing strategies such as environmental considerations. Once you have fully analysed the importance of demand on pricing decisions, evaluate this by considering alternative factors that can affect price. Make sure that you come to a justified conclusion based on your argument.

## 13 Marketing mix: place and promotion

### Activity 13.1

- A channel of distribution is the way that a product gets from the producer to the final consumer.
- The distribution channels would be: producer, wholesaler and retailer to the consumer.
- Two** benefits could include: economies of scale from selling in large quantities; they do not have the costs of selling small quantities to small retailers; the wholesaler pays storage costs; wholesalers advertise and promote the product. Make sure that you analyse the benefits by clearly linking the use of wholesalers and, for example, economies of scale.

## Activity 13.2

Example	Method of promotion
A credit card company sends offers to customers through the post.	direct mail
A chain of coffee shops offers a loyalty card to customers which gets them a free cup with every eight that they buy.	sales promotion
A cosmetics business uses a major fashion magazine to promote its products through pictures of models in the magazine.	advertising
A sports goods manufacturer pays a leading tennis player to use its rackets.	sponsorship
A car dealership uses a team of employees to sell cars to customers.	personal selling

## Activity 13.3

- a Informative advertising is where information about a product is communicated to consumers to create product awareness and attract their interest. Persuasive advertising is communicating with consumers with the aim of getting them to buy a firm's product rather than a competitor's product.
- b **Two** advantages of direct selling might include: all the profit is earned by the producer; the producer controls the marketing mix; speed of getting the product to the consumer; the producer has direct control of the production process. Remember to fully analyse the benefits of selling directly by clearly showing how producer control of the marketing mix benefits Holdall.
- c Explain how an increase in the marketing budget can increase market share through different forms of promotion, which leads to an increase in demand from Holdall's consumers which could increase its market share. This assumes that Holdall's marketing is successful and that other businesses do not also increase their marketing budgets. Start this answer by analysing how a greater marketing budget can increase Holdall's market share and then evaluate this by considering, for example, how other factors might affect its market share. Do not forget to come to a justified conclusion based on your argument.

## Activity 13.4

- a E-commerce is the use of the internet and other technologies by businesses to market and sell goods and services to customers.
- b **Two** threats could be: fraud; hacking; no personal service; returning items.
- c **Two** ways might be: use of targeted promotion and advertising by the business; consumers pass on promotion through their own social media; lower cost promotion can lead to lower prices; social media can speed up ordering and payment. Show your analytical skills here by linking the use of social media and Let-us-in's revenue. An example to support this would be very useful.

## Activity 13.5

- a **Four** different methods of promotion might be: personal selling; advertising; sales promotion; direct mail; sponsorship.
- b Above-the-line promotion is paid-for advertising communication with consumers which uses printed and visual media. Below-the-line promotion is not paid for but it uses incentives to encourage consumers to buy.
- c **Two** ways could include: use of targeted promotion and advertising by the business; consumers pass on promotion through their own social media; social media promotion can be changed very quickly to react to market conditions. Fully develop each point by analysing the link between social media promotion and Wild Crocs' sales.

- d** Explain the advantages of using the well-known bands such as: makes the product more attractive to consumers; creates publicity that promotes the jazz club; can be used to support Wild Crocs' promotion. The disadvantages are that it will be expensive and it may create an expectation of the jazz club that cannot be kept up. Start your answer by analysing the benefits of using the well-known bands and then evaluate this by considering some of the disadvantages, such as the costs of the bands. Make sure that you come to a final conclusion based on your argument.

## 14 Marketing strategy

### Activity 14.1

- a** Marketing strategy is a plan to achieve the marketing objectives using a given level of resources.
- b** Price, product, promotion and place.
- c** **Two** benefits of a unique selling point include: attractive to the consumer; makes the product different from the competition; strengthens the brand; gives a focus to promotion.
- d** Explain the advantages of precise marketing objectives, including: they give a target for focusing the marketing mix; they can be used as an incentive for employees; they can be used to measure the success of a marketing strategy. Discussion of the disadvantages might be difficult to set because the future is uncertain and they may put unrealistic pressure on employees if too difficult to achieve. Begin your answer by fully analysing the advantages of marketing objectives and then evaluate the benefits. Finish your answer by justifying your final argument in your conclusion.

### Activity 14.2

- a** **Four** types of legal control might be: protection for consumers from faulty/dangerous goods; prevent misleading advertising; stop monopoly businesses from exploiting consumers with high prices; protect consumers from unethical advertising and promotion.
- b** Unfair competition may come from the multinationals: cutting prices to artificially low levels, punishing customers who switch to Think and trying to stop suppliers of components supplying Think.
- c** **Two** reasons could include: difference in language and culture; economic difference; social differences; legal differences; lack of market knowledge. Make sure that you analyse the problems of producing in China and use the case example to illustrate this.
- d** Answer should explain the advantages of legal controls for consumers, which might include: from dangerous/faulty goods; inflated prices and misleading promotion. Discussion of the disadvantages could be that legal controls lead to higher prices and could restrict consumer choice. Develop your argument by fully analysing the benefits of legal controls for consumers and then evaluate this by, for example, considering how this might affect prices. Make sure that you come to a justified conclusion based on your argument.

### Activity 14.3

Example	Problem
A soft drinks manufacturer finds that its iced tea brand does not sell well because people in a country see tea as a hot drink.	social differences
A washing powder has to change the name of its product because it does not translate well into an overseas language.	difference in language
An economic recession in an overseas market means that the sales of motorcycles are falling.	economic differences
A retailer opens branches in a country and is unaware that people in the country like to shop late in the evening, not during the day.	lack of market knowledge
A car manufacturer has to make right- and left-hand-drive cars.	differences in legal controls

## Activity 14.4

- a Joint venture is an agreement between two or more businesses to work together on a project.
- b **Two** benefits of Redoc expanding into a developing country could include: growth in sales; spreading risk across different markets; economies of scale from higher output.
- c Answer should consider that a lack of knowledge of taste and language in the developing country might make market entry difficult because of: communicating advertising and promotion messages, product instruction information and product design preferences. Try to analyse the problems by using examples using Redoc to illustrate.
- d Answer should consider the benefits of entering a joint venture to enter the market, which might include that the local producer has market knowledge, links with customers and suppliers and lower costs of distribution. Discuss how the costs might be conflict on decision making and the risk that mistakes made by one firm in the joint venture could reflect badly on the other. Start your answer by analysing, for example, how the joint venture gives Redoc market knowledge in the developing country and then evaluate this by considering some of the weaknesses. Finally, come to a justified conclusion.

## Exam-style practice questions

- a Qualitative research is the collection of information about consumers' buying behaviour and their opinions about products [K].
- b Focus groups get the views of Sequin's consumers about the business's products in the form of a group discussion [K]. The information that Sequin gets is in the form of consumer feelings, views and ideas [App]. This is not information that is going to be used in a quantitative form and be turned into data. An example would be Sequin getting the focus group's views on a new clothing design [App].
- c A unique selling point for a business is a characteristic of the product which makes it distinct from other firms in the market [K]. In Sequin's case, this is 'designer style at affordable prices', which means that you can buy its designer clothing at lower prices than other businesses in the market [App]. By doing this, Sequin makes its products more attractive in the mind of the consumer relative to its competition, which increases demand for its products [An]. As demand for its products rises, this may lead to a rise in its sales and revenues [An].
- d Social media promotion means that Sequin targets potential and existing consumers with advertising and promotion through websites such as Facebook and Instagram [K].
 

**One** advantage of Sequin using social media promotion is that it can specifically target its consumers with advertising that appeals to them [App]. This could be consumers whose web searches show to be looking for designer clothes at low prices [App]. More effective promotion could increase Sequin's revenues as customer demand increases [An].

**One** disadvantage of this approach is that it may be ignored by online consumers who get so much information targeted at them when they are online [App]. If they ignore the social media advertising, then the money spent on it by Sequin will be wasted [App]. This means that the cost of the advertising might be higher than any increase in revenue, which reduces profits [An].
- e Sequin uses market research to get information about consumers in the market for its clothing [K]. It can use it to develop its marketing strategy, which is the plan it uses to successfully market its clothing [App]. The first possible benefit is that it identifies consumers' tastes and preferences in the designer clothing market [K]. This information can be used to help Sequin design its clothing to meet the tastes and preference of consumers [App]. This makes consumers more likely to buy the clothes and Sequin successful in achieving its marketing objectives [An]. Secondly, it helps Sequin make decisions about each aspect of the marketing mix. It could, for example, use research information to guide it on the 'place' element of the marketing mix and where to sell its clothing [App]. If the research information is effective, then Sequin is more likely to sell its clothing in the right types of distribution channel, which will increase its

sales revenue [An]. Finally, market research tells Sequin about its competitors in the clothing market, which helps it make strategic decisions to get ahead of its competitors [K]. For example, market research might tell Sequin that it needs to keep prices below a certain level to make them competitive in the clothing market [App] and this could lead to an increase in market share [An]. Sequin should, however, consider some of the weaknesses of research such as the accuracy of information gathered, the problems of sampling, and the costs of research [Ev]. The costs of market research will not be worth it if the information about the clothing market does not accurately reflect the views of consumers [Ev]. In conclusion, market research will help marketing strategy if it is carried out effectively [Ev].

## Exam-style case study

### Spin-it Ltd

- 1 **a** **Four** reasons, with explanations, for how consumer spending patterns might change the cycle hire business from: price of competitors' products change; changes in consumer income; changes in population size and structure; changes in tastes and fashion; changes in advertising and promotion.
- b** Explain the benefits and risks of the **two** different approaches to the information:
  - Look for a new market: benefits could include the potential for greater sales and spreading risk. Risks could include those associated with selling into a market that Spin-it is not familiar with.
  - Product development: benefits could include the potential for greater sales and spreading risk. Risks could include those associated with moving to a new product that Spin-it is not familiar with.
  - Conclusion: Use the market research in the appendices to support your final decision.
- 2 **a** **Four** ways, with explanations, that market research might help Spin-it. These could include: identifying consumer needs; guiding the marketing mix; predicting future trends and preferences; finding out strengths and weaknesses of competitors; finding out market size and growth.
- b** Include explanations of how the following types of market research could be used by Spin-it:
  - Focus groups: finding out what consumers think about cycle renting.
  - Test market: seeing how consumers react to the product when it is sold in a limited area.
  - Consumer survey: getting quantitative data on consumer behaviour.
  - Conclude by justifying which you think is most useful, based on Spin-it's research objectives.
- 3 **a** **Two** reasons, with explanations, for segmentation, which might include: rental service can be designed to meet the needs of consumers; Spin-it might not be able to compete in the whole rental market; marketing strategy can be targeted at specific consumers; it may be able to charge higher prices to certain consumers.
- b** First explain how each of the following pricing methods could be useful to Spin-it:
  - Market skimming – setting an initially high price.
  - Penetration pricing – setting an initially low price.
  - Competitive pricing – setting a price based on competitor prices.
  - To conclude, justify which of these you think is the most effective strategy based on the potential consumers of Spin-it's leisure bikes.
- 4 **a** Promotion is the way that Spin-it communicates with its existing and potential consumers to raise awareness and attract them to buy its products [K].
  - The first method is personal selling [K]. This could be where staff in Spin-it's shop actively try to sell its products to consumers [App]. For example, if someone comes in to rent a bike, the sales people could try to sell them additional products such as clothing and accessories [App]. Effective personal selling could lead to an increase in Spin-it's total revenue as customers are attracted to buy more products [An].

The second method is direct mail [K]. Spin-it could send a leaflet that promotes its rental business to target consumers [App]. This could be done most effectively online through email [App]. The direct mail could raise awareness amongst consumers of an offer that Spin-it has which increases its sales [An].

The third method is sponsorship [K] where Spin-it, for example, sponsors a local cycle race [App]. This increases awareness of its brand name amongst local consumers and could increase local sales [An].

The last method could be advertising through social media such as Facebook and Instagram [K]. This could target specific consumers, raise awareness and attract more customers to rent Spin-it's bikes [App]. As bike rental rises, Spin-it's revenue increases [An].

- b** E-commerce is where a business such as Spin-it uses the internet and intranet to support its activities [K].

Electronic payment is where customers who hire bikes can pay hire charges using credit cards and bank transfers online [App]. Because of this, customers will be attracted by the ease of payment and the ability to pay in advance without needing to send a cheque [App]. This would be useful to Spin-it's marketing strategy by increasing demand for Spin-it's hire services [An].

Online bike reservation, where Spin-it's customers can reserve bikes online, makes customer service more effective [App]. This could help Spin-it's marketing strategy by making its hire service more attractive to customers who do not have to wait to get their bikes when they arrive at the shop [An]. This means that customers are more likely to get the bikes they want and it will be less time-consuming [An]. This could lead to a rise in Spin-it's revenues and the increased efficiency of customer service may reduce costs [An]. Social media promotion is an effective way for Spin-it to promote its hire service because it can precisely target promotion at cyclists [App]. This will help the business's marketing strategy because Spin-it gets the best return for its promotion spending and this could increase revenues for the lowest promotion cost [An]. Online bike reservation may well be the most important support to Spin-it's marketing strategy because it makes the whole process of hiring a bike easier for customers, which improves the quality of Spin-it's product [Ev]. Electronic payment is useful, but payment can be made at the shop without too much inconvenience [Ev]. Social media marketing could increase sales but making the service more attractive through bike reservation may be more important [Ev].

## 15 Production of goods and services

### Activity 15.1

- a** Production is the process of converting inputs such as land, labour and capital into saleable goods. Productivity is a measure of the efficiency of inputs used in the production process.
- b** Labour production = total output/number of production employees
- c**  $150\,000 / 2000 = 75$  tractors per employee, per year
- d** Well-trained employees have the ability to be more productive and motivated employees have the desire to be more productive. You need to show your analytical skills here by clearly making the link between motivation and productivity. An illustrative example using Dax Breit would be very useful.

### Activity 15.2

- a** Inventories held as raw materials and components are stock to be used in production. Inventories held as finished goods are stock of goods that the business is going to sell.
- b** **Four** types of cost could include: warehousing; handling; shrinkage; insurance; obsolescence; opportunity cost.
- c** **Two** benefits to B&L of holding stock might include: house building should not be interrupted; houses can be completed on time; purchasing economies of scale. Make sure that you are analytical by developing the connection between holding stock and how this leads to economies of scale.

- d** Begin your answer by fully analysing the benefits of reducing stock such as reduced warehousing cost, lower insurance cost and lower handling costs and how this might lead to an increase in profits, and then evaluate the disadvantages of doing this, such as the interruption to production if stock runs out. Make sure that your conclusion is based on the argument that you have developed.

### Activity 15.3

- a** Lean production is the production of goods and services with the minimum waste of resources.
- b** **Four** reasons for waste might include: production defects; high inventories; over production; idle resources; transporting goods.
- c** **Two** things needed for JIT production by Relax Sofa Company from: good relationship with suppliers; delivery of inventory on time; employee flexibility.
- d** Kaizen means workers are involved in the decision-making process to improve quality and production, which means that workers are more motivated and workers help to improve quality. Analyse how Kaizen might improve quality and then productivity. An example using Relax Sofa Company to support this is important.

### Activity 15.4

- a** Job production is the production of one good at a time. Batch production is where each batch of product passed through one stage of production before moving on to the next stage.
- b** Bread is produced using batch production because it is manufactured in a series of stages from mixing to baking to cutting to packaging. Each stage needs to be completed before the next stage can be started.
- c** Explain that the cakes for special occasions are one-off products that need to be produced one at a time. Job production theory needs to be analysed here, using the case example.

### Activity 15.5

- a** CAM is computer-aided manufacturing where computers control the machinery and equipment used in production. CIM is computer-integrated manufacturing where the entire production process is controlled by computers and technology.
- b** Explain that CAM may mean that fewer workers are needed on the production line, which leads to lower labour costs. Make sure that you analyse the link between using CAM and the number of workers needed on the production line. Illustrate your answer by using an example from Tech Clean.
- c** Start your answer by fully analysing the benefits of using technology in production, such as that the use of CAD, CIM and CAM may lead to greater efficiency and better quality of products produced by Tech Clean, and evaluate this by considering the disadvantages, such as investment costs. Finish by concluding whether the use of technology in production can be justified based on your argument.

## 16 Costs, scale of production and breakeven analysis

### Activity 16.1

Examples of costs	Fixed or variable costs
Insurance of capital equipment	fixed
Cotton used to manufacture t-shirts	variable
Salary of the marketing director	fixed
Packaging used for the t-shirts	variable
Information labels attached to each t-shirt	variable
Rent of buildings	fixed
Investment in production line machinery	fixed
Production line workers' wages on piece rates	variable

### Activity 16.2

a Fixed costs are costs that do not change with output. Variable costs are costs that change in direct proportion to output.

b

Output	Fixed cost	Variable cost \$50 per frame	Total cost	Average cost
0	70 000	0	70 000	
10 000	70 000	500 000	570 000	57
20 000	70 000	1 000 000	1 070 000	53.5
30 000	70 000	1 500 000	1 570 000	52.33
40 000	70 000	2 000 000	2 070 000	51.75
50 000	70 000	2 500 000	2 570 000	51.4

c Explain that average costs fall as output increases because the fixed cost element of total cost is a constant value and is divided by a higher output figure as output increases. The use of a numerical example to support your analysis is important here.

### Activity 16.3

a Total cost is all the variable and fixed costs of producing the total output.

b

\$'000s	Brand One	Brand Two	Total
Revenue	200	350	550
Fixed cost	80	100	180
Variable cost	130	160	290
Total cost	210	260	470
Profit	(10)	90	80

\$'000s	Total
Revenue	350
Fixed cost	180
Variable cost	160
Total cost	340
Profit	10

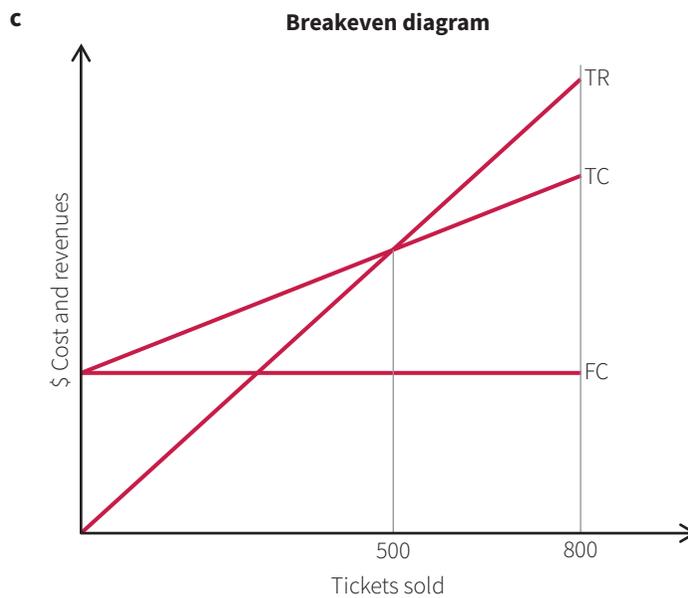
- d** Explain that discontinuing Brand One has the advantage of taking away a loss-making brand. Discuss how the fixed costs have to be paid, so that the total profits fall from \$80 000 to \$10 000. Justify your conclusion, for example by saying that Brand One should be continued because it spreads the fixed costs over two products. Make sure that you clearly analyse the advantages and disadvantages here, using the cost data to support your answer.

### Activity 16.4

Example	Economy of scale
A major international airline gets a loan at a very low rate of interest.	financial
A pharmaceutical company invests in the latest CAM machinery.	technical
A major supermarket chain negotiates a deal to buy soft drinks from a supplier at a very low price.	purchasing
A large advertising agency divides its management into five specialist functions.	managerial
A sports goods manufacturer divides its significant advertising budget by its very large output.	marketing

### Activity 16.5

- a** Four economies of scale might include: financial; technical; purchasing; managerial; marketing.  
**b** Diseconomies of scale could lead to a rise in Educate’s average costs. For example, communication and administration costs.



d	\$
Sales	\$154 000 (220 x 700)
Variable cost	\$56 000 (80 x 700)
Fixed cost	\$70 000
Profit	\$28 000
Margin of safety	200 tickets

- e Make sure that you fully analyse and evaluate the advantages (e.g. for forecasting costs, revenues and profits; shows the impact of decision-making changes; easy to interpret) and disadvantages (e.g. based on forecast data; revenues and costs may now be related to output in a linear way) of breakeven as a management tool and come to a justified conclusion based on your argument.

## 17 Achieving quality production

### Activity 17.1

- a Quality is ensuring that a good or service meets the needs and requirements of its consumer.
- b **Two** ways to achieve quality might include: training labour; investing in quality; improving quality control; improving quality assurance. Make sure that you write your answer in the context of Mugs-on-line.
- c **Two** reasons might include: attracts new customers; increases brand loyalty; reduces complaints; reduces returns; allows business to charge a premium price. Remember to analyse the benefits by making, for example, the link between quality and attracting customers. Write your answer in the context of Mugs-on-line.

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### Activity 17.2

- a Quality standards are the minimum standards of production or service that are acceptable to consumers.
- b **Two** reasons from the following: greater returns lead to higher costs; increases the cost of waste; revenues fall if customer demand falls and Pizza Shack might have to reduce prices. Analyse clearly the link between quality and profit using Pizza Shack as an example.
- c Begin your answer by fully analysing the benefits of hiring younger and fewer staff (e.g. reducing labour costs) and evaluating this by considering the problems of doing this (e.g. this may have the effect of reducing quality, which could lead to higher costs and lower revenues). Make sure that you conclude your answer based on the argument that you have developed.

### Activity 17.3

- a Quality control is checking the quality of goods through inspection. Quality assurance is a system of setting agreed standards for every stage of production.
- b **Two** problems of quality control might include: repetitive and boring work demotivates employees; it does not pick up quality issues during the process; employees are not motivated to improve quality because they do not have responsibility for quality. Write your answers in context.
- c It is important to analyse the link between quality problems and how these might damage brand image if consumers are unhappy with the product. Use an example here to support this.

### Activity 17.4

- a There is a required standard for raw materials and components; quality standards are agreed at each stage of production; products are designed to minimise quality issues; employees are responsible for quality.
- b Explain **one** reason why quality assurance might lead to a fall in costs for R&F Glass from: encourages teamwork; reduces waste; quality problems are discovered earlier. Remember to analyse the reason why quality might reduce costs by, for example, fully developing the reason why quality reduces waste.
- c Start by fully analysing the benefits of quality assurance (e.g. it might increase revenue and reduce costs) and evaluate this by considering the costs (e.g. more skilled workers are needed and training costs rise). Make sure that you come to a justified conclusion based on your argument.

## 18 Location decisions

### Activity 18.1

Example	Quantitative or qualitative factors
Cost of buying the site for the plant	quantitative
Availability and cost of local labour	quantitative
Size and position of the available site	qualitative
Legal restrictions	qualitative
Transport costs	quantitative
Local infrastructure issues	qualitative
Market potential in the region	quantitative
Government tax incentives	quantitative
Environmental and ethical considerations	qualitative

### Activity 18.2

- a Quantitative location factors can be measured in financial terms and will directly affect costs, revenues and profits. Qualitative location factors are those that cannot be measured in financial terms and that indirectly affect costs, revenue and profits. Include OPure Ltd in your examples.
- b Remember to be analytical by making the link between the low-cost site and the local labour force and their benefits for location. Explain that a low-cost site for new bottled water could lead to lower investment costs in the plant and that a well-trained labour force will make its operations of the plant more efficient.
- c Explain why concerns over infrastructure might be a problem for Opure Ltd from: difficult to get products to market; hard for employees to get to Opure Ltd; difficult to access raw materials and components. It is important to clearly analyse the impact that poor infrastructure might have on Opure Ltd.

### Activity 18.3

- a Infrastructure is the basic facilities, services and installations needed for a business to function.
- b **Two** potential problems in expanding to South America might include: lack of market knowledge; managing cultural and language difference; communication difficulties with a new country.
- c Explain that the Brazilian location has the benefits of: being close to the market having good infrastructure; having low labour cost to keep manufacturing costs low. Remember to be

analytical in the way that you make the connection between location in Brazil and its benefits. An example to support this is very useful.

- d** Start your answer by analysing the benefits of expansion overseas (e.g. increasing revenues and profits and spreading risk across different markets) and then evaluate this by considering the disadvantages (e.g. costs such as language, cultural and legal differences). Come to a conclusion based on your argument.

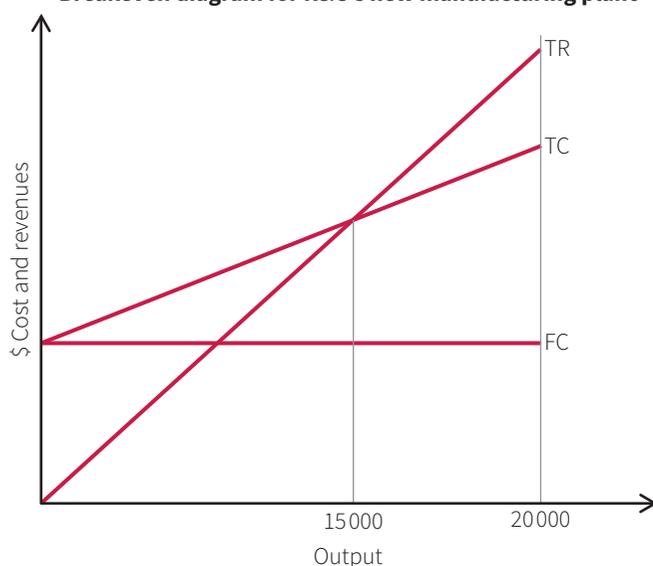
## Activity 18.4

- a** **Four** areas affected by legal controls could include: location rules; employment law; competition regulation; trade regulations; advertising rules.
- b** Working visas for employees are needed if Besure moves to Paris. A leasing contract would be needed by Besure for its office in Paris.
- c** Make sure that you analyse the link between relocating employees and the impact on their motivation, for example by explaining that relocating Besure employees to Paris could have a negative impact on employee motivation if they are unhappy about the move to Paris, which could reduce their efficiency at work.
- d** Begin your answer by analysing the employee and legal problems of locating in Paris and then evaluate this by considering the benefits (e.g. lower operating costs and being closer to the market). Then come to a justified conclusion based on your argument.

## Exam-style practice questions

- a** Computer-integrated manufacturing is the complete use of technology on the production line by an organisation to control production [K].
- b** **Two** location factors that could have affected R&C's decision to locate near Warsaw are firstly the cost of the site [K]. Choosing the lowest-cost location is positive for R&C because it will make the site more profitable [App]. Secondly, infrastructure [K] will be important because R&C will need to get input into the site and move finished goods out of the site efficiently [App]. Good infrastructure will make R&C's overall operation more efficient [App].

- c** **Breakeven diagram for R&C's new manufacturing plant**



- d** JIT means that R&C holds a minimum stock [K] of components needed to make its speakers [App]. The first factor needed by R&C to use JIT is for the business to have strong relationships with its suppliers [K]. For R&C to be able to produce its speakers to meet the demand of its customers, it needs to be able to rely on its suppliers to deliver inventories when they are needed [App]. If suppliers are unreliable and stock is not delivered on time, then R&C cannot

produce goods to meet the demand of its customers [An]. JIT also needs to have a flexible labour force [K] that can adapt to changes in demand of its customers [App]. If, for example, there was a change in demand to another type of speaker, then workers need to have the skills to easily switch to produce a different speaker to meet the change in consumer demand [An].

- e** The first advantage to R&C of making this location decision is that it offers a new market for R&C, which gives it the opportunity to increase its revenues [K]. Warsaw will have potential consumers that will buy R&C's speakers [App] and the additional revenue could lead to an increase in profits [An]. Because this is a new market for R&C, this is a market where there is significant potential for sales growth [An]. The second advantage for R&C is that it gives the business the potential to spread risk [K] by operating in a different market [App]. This means that a decline in the demand for its speakers in Spain could be made up for by growth in Poland [An]. The first disadvantage of R&C locating in Warsaw is communication barriers [K]. There are language differences that R&C would have to deal with when employing local workers who may not speak Spanish [An] and this would make it more difficult for the business to operate efficiently [An]. This could be overcome by offering language training but this would increase R&C's costs [Ev]. The second disadvantage is cultural barriers [K]. The expectations of the workers in Warsaw in terms of things such as breaks, start-times and general working practices could make managing staff in Warsaw more challenging [An]. To overcome this, R&C may have to change management practices, which could increase costs [Ev]. In conclusion, the disadvantages of locating in Warsaw might lead to an increase in costs and management difficulties in the short run but the long-term advantages of greater revenues and spreading risk make the decision to move worth it [Ev].

## Exam-style case study

### The Cabin Company

34

- 1 a Four** methods, with explanations, for how The Cabin Company could improve productivity from: training of employees; incentive schemes for workers; investment in capital; change in production methods; development of technology.
- b** Start by explaining the following benefits of lean production to The Cabin Company:  
 Quality is improved through the use of quality assurance.  
 Holding inventory cost is reduced through use of JIT.  
 Unit costs are reduced through reduced waste.  
 Justify what you think is the most significant benefit; for example, you could say that quality is improved because this is a 'key objective of the business'.
- 2 a Four** different types of economy of scale might include: technical; financial; managerial; marketing; purchasing. Make sure that you explain how each of your four examples applies to The Cabin Company.
- b** Make sure that you explain how the benefits of using breakeven analysis apply to The Cabin Company, rather than treating them as general benefits.  
 Easy to construct and interpret – makes them effective for presenting ideas.  
 Financial information to determine target output – to achieve a profit from production.  
 Show effect of changes in costs and revenues – to help them assess risk if costs and revenues change.  
 Conclude by justifying what you think is the most important benefit, such as the importance of setting a target output for the two locations.
- 3 a Two** aspects that you could explain could include: making sure that inputs are of the required standard; quality standards are agreed at each stage of production; product design to minimise quality issues; all employees have responsibility for ensuring quality. Make sure that your explanations show how these aspects apply to The Cabin Company.

- b** Make sure that your explanations apply to The Cabin Company:  
 Brand image – attracts and retains customers.  
 Costs – reduces cost of waste.  
 Conclude with a justification of which you think will have the most effect on profit; for example, brand image will allow The Cabin Company to increase revenue and profits.
- 4 a** The first qualitative factor that could affect The Cabin Company’s decision to locate its new factory would be infrastructure links [K]. This would be important in terms of getting inputs efficiently to its factory and getting finished goods to customers when they want them [App]. Getting inputs efficiently to The Cabin Company would mean that breaks in production are less likely because of running out of inventory [An]. This also helps with the CEO’s aim to use lean production [App]. Getting its cabins to market means that it can satisfy consumer demand effectively [App], which builds customer loyalty and increases revenues [An]. The second qualitative factor could be ethical considerations [K]. Locating in a place that does not disrupt the local environment and creates local jobs [App] might enhance The Cabin Company’s image as an ethical business [An]. This could enhance its brand image and fit with CEO George’s personal philosophy [An].
- b** On a financial basis, location 1 is the better location. This is because the breakeven output is 1300 units lower than for location 2 [App], which means that The Cabin Company does not have to manufacture as many cabins to achieve a profit [An]. This is a safer position for the business [App]. The profit for location 1 is also \$500 000 greater than for location 2 [App]. This is particularly important to The Cabin Company’s owners, who will be looking for the greatest return on their investment [An]. Location 2, however, has better qualitative factors. There is better availability of labour at location 2, which means that The Cabin Company can access the skilled labour that it needs [App]. This could mean that it does not have to train unskilled employees [An] and that the business does not have to pay such high wages to attract the right employees [An]. This could allow it to have lower costs than location 1 in the long run [Ev]. Location 2 also has better infrastructure, which allows the business to access inputs more easily and get its finished goods more effectively to market [App]. Getting inputs more easily allows The Cabin Company to achieve the lean production methods that it wants [App]. Getting finished goods more efficiently to market could be more attractive to customers [An] and increase revenues in the long run [Ev]. In conclusion, location 1 could be a better choice in the short run because of its profitability and breakeven point [Ev]. Location 2 could be better in the long run because of infrastructure and the availability of skilled labour. For this reason, location 2 should be chosen [Ev].

## 19 Business finance: needs and sources

### Activity 19.1

- a** **Four** reasons why businesses need finance could include: start-up capital; pay for working capital; purchase of machinery and equipment; invest in technology; fund expansion; research into new products.
- b** Capital expenditure is spending by a business on non-current assets such as machinery and buildings.
- c** **Two** types of payment for the bank loan are: interest and repayment.
- d** **Two** reasons why Maria’s business might have problems raising finance could be: risk of being a small business for repayment; lack of capital to secure a loan; Maria’s lack of experience. Remember to analyse here by making the connection between Maria’s business and the problems of raising finance. A case example would be very useful to support this.

## Activity 19.2

- a Long-term finance is debt or equity used to finance the purchase of non-current assets or finance expansion plans. Short-term finance is loans or debt that a business expects to pay back within one year.
- b **One** advantage of using retained profit is that it does not need to be paid back and there are no interest payments. **One** disadvantage of using retained profit is that it cannot be paid to the owners/shareholders. You need to be analytical here by linking, for example, the advantage of retained profit with the fact that there is no interest on the finance.
- c Start your answer by analysing the reasons why Blue Loch should take out the loan (e.g. it will double its capacity and increase profits and revenues) and evaluate this by considering its disadvantages (e.g. interest costs and repayment). Finish by coming to a conclusion based on your argument.

## Activity 19.3

Example	Type of finance
The business issued \$40m of new shares last year.	equity finance
A major industrial customer owes the mining business \$1.5m.	trade receivables
The business plans to sell \$10m of bonds next year.	debenture issue
A finance company has loaned the firm \$14m to purchase a new building which is secured against the value of the building.	mortgage
The mining business sells \$1m of trade receivables to a finance company.	debt factoring
The mining business uses a fleet of company vehicles which it pays \$1.7m per year to use.	leasing
The business has signed an agreement of \$2.5m from the bank to purchase a new drilling machine.	bank loan

## Activity 19.4

- a Micro-finance is small amounts of capital loaned to entrepreneurs in countries where business finance is often difficult to obtain.
- b Explain how Fantasy Socks could raise funds through a large number of people who collectively contribute money that can be borrowed by Fantasy Socks. The lenders contribute using online coordination through the internet. Remember to analyse how Fantasy Socks could use crowd funding by making the link between each stage of the process of raising funds in this way.
- c Begin your answer by analysing the difficulties that small businesses have raising finance (e.g. their risk of failure; lack of capital for security; inexperienced management) and then evaluate this by considering why small businesses might be tempting for lenders to finance (e.g. the profit potential that small businesses have for lenders; not all small businesses are risky; small businesses can still have experienced management). Conclude your answer based on the argument that you have developed.

## Activity 19.5

- a **Four** factors that might influence the choice of finance could include: size and legal form of the business; amount of money required; length of time; existing borrowing.
- b Explain that Henry's got into cash-flow difficulties because of increased cash outflows (tax, costs and suppliers) and reduced inflows (revenues). Make sure that you are analytical in the way that you cover the reasons for the business's cash-flow difficulties. Use the case example cash-flow numbers to support your answer.

- c **Two** alternative sources of funds could include: bank loan; mortgage; debenture issue; leasing; hire purchase. Write your answer in context.
- d Start by analysing the benefits of using the outside investor (e.g. no interest payments, no repayment and do not have to use retained profit) and then evaluate this by considering some of the disadvantages (e.g. loss of control to the outside investor). Finish your answer by coming to a conclusion based on your argument.

## 20 Cash-flow forecasting and working capital

### Activity 20.1

- a **Four** items that The Hot Wok needs cash for include: employees' wages; purchasing stock; expenses such as rent; interest payments; repaying loans.
- b The Hot Wok will have created monthly forecasts of cash inflows such as sales and cash outflows from payments such as wages.
- c Explain that the \$600 000 debt payment means that this is no longer a cash inflow, which means that the net cash flow will be negatively affected by the \$600 000. It is important to analyse the failure of the customer to pay the debt by, for example, making the link to the working capital cycle.

### Activity 20.2

- a Net cash flow for a business is cash inflow minus cash outflow.
- b A 7, B 7, C 13, D 16, E 23, F 16, G 23, H 30. Award half a mark for each correct entry.
- c Explain that as Cool-it Ltd's sales rise, it will need to produce more so more stock will need to be purchased. Purchasing more inventory means that cash flows out of the business to pay for it. Remember to be analytical by making the link between business activity, cost of sales and cash flow. Using a numerical example is important here.

### Activity 20.3

- a The working capital cycle is: inventories purchased on credit, production of goods, goods sold on credit and cash received from debtors.
- b A (5), B (4), C (2), D (2), E 4, F 5, G 9, H 6
- c Methods of raising finance: overdraft; bank loan; trade credit.
- d Be analytical by making the link between slow payment and how this affects working capital, for example by explaining that customers who are slow to pay mean that cash does not flow into the business to pay creditors and expenses. This may make it more difficult to produce goods to sell for future cash inflows.

### Activity 20.4

- a Liquidity is the ability of a business to pay its short-term debts.
- b The \$600 000 cash payment will be a net cash outflow, which will have a negative effect on Fix-it's net cash flow and reduce its liquidity.
- c Explain that the loan to Fix-it will have cash outflows to make interest payments and loan repayments, which will have a negative effect on its net cash flow. Show your analytical skills by making the link between borrowing and future cash payments, such as interest payments.
- d Begin your answer by analysing the benefits of investing in the IT system (e.g. it may improve efficiency, reduce costs and increase sales if the quality of Fix-it's service improves, which will improve its future profits and net cash flow) and then evaluate this by considering the costs (e.g. immediate cost of the investment as a net cash outflow and future cash outflows from loan interest and repayment). Finally, come to a conclusion based on your argument.

## 21 Income statements

### Activity 21.1

- a **Four** types of expenses that make up Tróei's total cost include: wages; heat and light; marketing; administration; rent.
- b Gross profit is revenue less costs of sales. Profit is gross profit less expenses.
- c **Two** reasons why Tróei's revenue might have increased include: advertising by Tróei; new customers attracted by Tróei's quality of product; economic growth; market growth; Tróei's changes in price.
- d Explain that an increase in revenue may mean that Tróei's units sold increases, which means that it may have to purchase more stock and this increases cost of sales. The key here is to analyse the link between rising units sold and costs of sales. A numerical example using Tróei would be very useful here.

### Activity 21.2

- a The cost of sales is the cost of purchasing the goods used to make the products sold.

b, c, d

	Jan	Feb	Mar	Apr	May	Jun
Units sold	9000	11 000	10 000	8000	10 000	12 000
Revenue	\$36 000	\$44 000	\$40 000	\$32 000	\$40 000	\$48 000
Cost of sales	\$18 000	\$22 000	\$20 000	\$16 000	\$20 000	\$24 000
Gross profit	\$18 000	\$22 000	\$20 000	\$16 000	\$20 000	\$24 000
Expenses	\$12 000	\$12 000	\$12 000	\$12 000	\$12 000	\$12 000
Profit	\$6000	\$10 000	\$8000	\$4000	\$8000	\$12 000

- e Expenses are often fixed costs that do not change with output so remain constant as units sold changes over the first six months.

### Activity 21.3

- a Revenue: selling price x units sold.

b, c

\$m	Ice Plc	Shine Skin Plc	So-Pure Plc
Revenue	123	98	143
Cost of sales	43	31	74
Gross profit	80	67	69
Expenses	56	46	24
Net profit	24	21	45

- d** Start your answer by analysing the reasons why So-Pure is the best performer (e.g. using net profit to measure performance). Evaluate this by considering why So-Pure might not be the best performer (e.g. Ice Plc performs better on gross profit; no allowance is made for the size of the businesses; no allowance is made for trends in performance over time; and no allowance is made for non-profit performance factors such as product quality). Finish your answer by concluding based on your argument.

## Activity 21.4

Example	Stakeholders
The high profits of a business have driven up its share price.	shareholders
The losses of a business mean that it might have to make redundancies.	employees
The losses of a business mean that it might struggle to pay for stock.	suppliers
The net profit of a business is used to calculate its tax.	government
The high profit of a business means a bonus for the business's leadership.	managers
The losses of a business mean that it may not be able to pay its debts.	lenders

## Activity 21.5

- a** Sales made on credit record a profit but no cash is received, and payments to suppliers means that cash flows out but no profit is recorded until the goods are sold.
- b** Make sure that you are analytical here by making it clear why a short credit period leads to cash-flow problems. Using an example is important to support your answer, for example that the short credit period given to Dry Farm means that it may have to pay cash for inventories before the cash is received from debtors, which leads to cash-flow problems.
- c** Begin your answer by analysing the benefits of making customers pay more quickly (e.g. cash flows in to Dry Farm more quickly, which reduces cash-flow problems) and then evaluate this by considering the problems of doing this (e.g. customers may switch to another supplier; administration of collecting cash becomes more expensive; and there may be other ways to improve cash flow such as offering discounts to customers that pay in cash). Make sure that you come to a final conclusion based on your answer.

## 22 Statement of financial positions

### Activity 22.1

- a** The statement of financial position is an accounting statement that records the assets, liabilities and owner's equity of a business.
- b** **Four** types of assets might include: buildings; machinery; equipment; inventories; accounts receivable; cash.
- c** Explain that Dry Hill's building might have been valued at its market value as if it were going to be sold. Its inventories might have been valued by the purchase price of the stock when it was bought. Develop your analysis here by developing your answer using examples based on Dry Hill.

## Activity 22.2

Example	Statement item
Retained profit	owner's equity
Shares issued by the business	owner's equity
Mobile phone manufacturing equipment	non-current assets
Building used for production	non-current assets
Money owed to the business by its customers	current asset
The business's overdraft	current liability
Money owed by the business to its suppliers	current liability
Cash in the bank	current asset
Debentures issued by the business	non-current liability
Stock of components used to manufacture the phones	current asset

## Activity 22.3

- a** Current liabilities are the debts of the business which it expects to pay before the date of the next statement of financial position. Long-term liabilities are the debts of the business which will be payable after more than one year.
- b** A 120 (200–80) B 480 (400+80) C 120 D 480 (360+120)
- c** A rise in inventories will increase the value of current assets, which leads to a rise in the value of net assets. Be analytical here by using a numerical example of how a rise in the value of inventories leads to a rise in En Chocolat's net asset value.
- d** Explain that a 30% increase in En Chocolat's profits may increase the value of retained profits which are part of owner's equity so the value of owner's equity will rise. Remember to use a numerical example to support your analysis of a rise in En Chocolat's capital employed.

## Activity 22.4

- a** A 30 000  
B 35 000  
C 400  
D 700  
E 36 100  
F 31 300
- b** The asset value of machinery might have increased if Clear Ver had purchased new machinery.
- c** Explain that Clear Ver's retained profit figure might have increased because it has made a profit in the trading year 2018, which would be added to the retained profit figure. Make sure that you clearly analyse the reasons why the retained profit might have increased, such as increased demand from customers.
- d** Begin your answer by analysing the reasons why the bank should be concerned (e.g. the loan of \$20m would be additional borrowing to Clear Ver, which would add to its existing interest costs and loan repayments, and this would be a concern to the bank, as it wants to receive these payments at a minimum risk) and evaluate this by considering the benefits to the bank of making the loan (e.g. existing borrowing is quite low relative to capital employed and expansion may lead to more profits in the long run). Finish your answer with a conclusion based on your argument.

## 23 Analysis of accounts

### Activity 23.1

- a Total equity is calculated by subtracting the liabilities from the assets.
- b Explain that total equity might have increased from 2015 to 2017 because of the retained profit that Malibu earned over the period, which is added to total equity. It is important to use the figures in the case example to analyse why the total equity has risen.
- c Remember to begin your answer by analysing the data that suggests a deterioration in performance (e.g. revenue and profit have both fallen) and evaluate this by considering other factors before judging Malibu's performance such as: how other firms in the market have performed; market and economic conditions; and we do not know about non-monetary performance factors such as product quality. Then come to a conclusion based on your argument.

### Activity 23.2

- a Gross profit margin = gross profit/revenue x 100; profit margin = profit / revenue x 100.

b

	Aprender	Escucha
Gross profit margin	$19/34 \times 100 = 55.9\%$	$8/15 \times 100 = 53.3\%$
Net profit margin	$5/34 \times 100 = 14.7\%$	$4/15 \times 100 = 26.7\%$
Capital employed	$5/12 \times 100 = 41.7\%$	$4/9 \times 100 = 44.4\%$

- c Explain that Escucha's performance is better than Aprender's because it has the higher return on capital employed, which gives it the higher percentage of profit relative to capital employed. Make sure that you show analytical skills here by using the data to support your answer.
- d Start your answer by analysing the strengths of using financial ratios (e.g. they are a good judge of financial performance because they measure gross profit and profit relative to revenue and profit relative to capital employed; the higher these values, the better the business performance) and then evaluate this by considering other factors that should be accounted for to measure business performance such as trends in performance over time and other measures of performance such as product quality. Finally, come to a conclusion based on your argument.

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### Activity 23.3

- a Current ratio = current assets / current liabilities; acid test ratio = (current asset - inventories) / current liabilities.

b

\$	2016	2017
Current ratio	$28\,000/14\,000 = 2$	$19\,000/11\,000 = 1.73$
Acid test	$(28\,000 - 16\,000 = 12\,000)/18\,000 = 0.67$	$(19\,000 - 14\,000 = 5\,000)/11\,000 = 0.45$

- c The current and acid test ratios have both fallen, which shows a decline in Encore's liquidity.
- d Make sure that you are analytical here about the consequences for Encore of customer bankruptcy and a weak domestic economy, for example, by explaining that the bankruptcy of one of Encore's customers will mean less cash coming into the business, reducing its liquidity; a weak domestic economy might reduce sales, which means less cash coming into the business, reducing its liquidity. A numerical example to support this would be very useful.

## Activity 23.4

- a** A high-value-added product means producing a good where the work done on the product means that the final selling price it can be sold for is much higher at the end of the production process. Make sure that your answer is written in the context of Spinning Blade.

**b**

	2016	2017
Gross profit margin	$140/350 \times 100 = 40\%$	$190/420 \times 100 = 45.24\%$
Net profit margin	$50/350 \times 100 = 14.29\%$	$90/420 \times 100 = 21.43\%$
Capital employed	$50/430 \times 100 = 11.63\%$	$90/520 \times 100 = 17.31\%$

- c** The gross profit margin and profit margin have both increased, which means that Spinning Blade's performance on both criteria has improved and it is making more gross profit and profit on each unit sold.

**d**

\$	2016	2017
Current ratio	$80\,000/50\,000 = 1.6$	$70\,000/60\,000 = 1.17$

Explain that the fall in the current ratio from 2016 to 2017 shows that it has less current assets to pay current liabilities, so Spinning Blade's liquidity position has deteriorated. It is important to be analytical here by using the ratio that you have calculated to show how the growth of the business has affected liquidity.

- e** Start by analysing the strengths of using ratios to judge performance (e.g. providing data) and go on to evaluate this by considering the weaknesses of ratios (e.g. no consideration of non-monetary factors; they need to be compared with other businesses over time; and they do not allow for economic or market conditions). Finish by coming to a conclusion based on your argument.

## Exam-style practice questions

- a** Gross profit is the difference between a business's sales revenue and its cost of sales [K].
- b** A:  $\$170\,000 - \$90\,000 = \$80\,000$ ; B:  $\$70\,000 - \$5\,000 = \$65\,000$  [App].
- c** The first way that Canvas could reduce its cost of sales would be to negotiate lower prices for raw materials from its suppliers [K]. This could, for example, be negotiating a lower price for the materials that it uses to manufacture the soles of its casual shoes [App].  
The second way to reduce its cost of sales is to use cheaper raw materials to produce Canvas's shoes [K]. It could use cheaper materials to produce the laces for the shoes [App].
- d** Revenue is units sold x selling price [K]. The first way that Canvas could increase its revenues is by advertising and promoting its shoes [K]. Effective online advertising using social media could attract additional consumers [App]. Attracting more consumers would increase the units sold, which would increase Canvas's revenues [An]. The second way to increase revenues would be for Canvas to reduce the selling price [K]. Reducing the selling price of its shoes would increase revenues, assuming that demand for Canvas's shoes is price elastic [App]. The price elasticity of its shoes will depend on the number of competitors that it has. More competition often means that demand is more elastic [An].
- e** You could say that Canvas's performance has deteriorated because of falling gross profit and profit from 2016 to 2017 [App]. Profit is an objective of private sector business so its decline suggests deteriorating performance [An]. The reason that gross profit and profit appear to have fallen is because of rising cost of sales [App]. This means that the cost of materials used to produce the shoes has increased, which again suggests deteriorating performance in terms of managing this cost [An]. Rising expenses from 2016 to 2017 also suggest that Canvas's performance has deteriorated because it is managing things such as administration, marketing and heat and light costs less effectively [App]. However, Canvas's revenues have increased, which could indicate improved marketing and sales performance [Ev].

It is also difficult to make a performance assessment because there is no comparison with other businesses in the market and no information on economic and market conditions [Ev]. The shoe market may have experienced rising cost of materials which Canvas could do nothing about [Ev]. Finally, there is no information on non-monetary factors affecting Canvas's performance. The quality of the product may have improved from 2016 to 2017 because of more motivated workers [Ev]. In conclusion, it is very difficult to say that Canvas's performance has deteriorated just based on profit data [Ev].

## Exam-style case study

### The Reel Cinema Ltd

- 1 a** Reasons that The Reel Cinema would need to raise finance might include: to provide cash to fund working capital; to finance new machinery; to finance expansion; to invest in new technology. Make sure that your explanations for **two** of these show how they apply to The Reel Cinema.
- b** Retained profit – funds generated through trading.  
Leasing – not owning assets but paying for them with regular rental payments.  
Bank loan – funds borrowed.
- Explain how these financing methods apply to The Reel Cinema, and conclude by discussing which method of finance you would advise, based on cost, ownership and impact on cash flow.
- 2 a** Reasons why cash-flow forecasting is important might include: to plan for changes in liquidity over time; to make arrangements for funding payment to suppliers and employees; to plan for future borrowing; to provide cash-flow information for banks and investors. Make sure that you explain how the **two** reasons you list apply to The Reel Cinema's situation.

**b**

\$'000s	Jan	Feb	Mar
Cash inflow			
Receipts	22	24	26
Cash outflow			
Payments	27	22	16
<b>Net cash flow</b>	(5)	2	10
Opening balance	2	(3)	(1)
<b>Closing balance</b>	(3)	(1)	9

Begin by explaining that The Reel Cinema could deal with the net cash-flow position by: using an overdraft; arranging a short-term bank loan; increasing cash inflows by pressuring debtors; delaying payments to creditors; taking action to increase revenues; trying to reduce costs. Follow by discussing issues relating to these options such as: interest costs and repayment of borrowing; relationships with debtors and creditors; problems of cutting costs and increasing revenues. This will help you to justify your final advice to The Reel Cinema.

- 3 a** The Reel Cinema's income statement sets out the revenues, costs and profits of the business over a year [K]. It would be useful to The Reel Cinema's shareholders because it reports the profit that it makes [App]. Shareholders are paid dividends based on the profit that the business makes [K]. Dividend is share of profit that the business makes that is paid to the shareholders/owners [App]. The higher the profit, the more dividend the shareholders receive as a return on their investment in the business [An]. Employees will be interested in The Reel Cinema's income statement because of job security [K]. The more profit the business makes, the more secure the business is likely to be [App] which means that the jobs of employees are more secure [An]. Lenders are interested in The Reel Cinema Company being able to pay interest on outstanding debt and repay loans [App]. The more profit the business is reporting in its income statement, the more money it has available to pay

interest and repay loans [An]. The Reel Cinema’s income statement will be useful to the government that is interested in collecting tax from the business [App]. Companies have to pay tax on their profits and the more profit the Reel Cinema makes, the more tax it will have to pay to the government [An].

**b**

	2015	2016	2017
<b>Revenue</b>	\$210 000	\$222 000	\$265 000
<b>Cost of sales</b>	\$120 000	\$135 000	\$167 000
<b>Gross profit</b>	\$90 000	\$87 000	\$98 000
<b>Expenses</b>	\$62 000	\$67 000	\$81 000
<b>Profit</b>	\$28 000	\$20 000	\$17 000

The income statement for The Reel Cinema can be used to measure its performance from 2015 to 2017 in terms of revenues, costs and profits [K]. The revenue has increased significantly from \$210 000 in 2015 to \$265 000 in 2017 [App]. This suggests improved performance from The Reel Cinema Company in terms of selling tickets and the price achieved for the tickets sold [An]. Cost of sales has risen from \$120 000 in 2015 to \$167 000 in 2017, which could represent a deterioration in performance [App]. The Reel Cinema Company may be paying more for the films it shows [An]. This could be attracting more consumers but the costs of sales could be rising because the business is paying more for better films to show [An]. Gross profit has increased from \$90 000 in 2015 to \$98 000 in 2017, which suggests improved performance [App]. This means that revenues are rising faster than cost of sales over the period, which suggests better performance [An]. The Reel Cinema’s expenses have increased from \$62 000 in 2015 to \$81 000 in 2017, which could mean a deterioration in performance [App]. This could be because marketing and administration costs are increasing as a result of greater revenues [An]. Profit has fallen over the period from \$28 000 in 2015 to \$17 000 in 2017, which may mean deteriorating performance [App]. This is because expenses are rising by more than gross profit [An]. There is, however, no information about the cinema market or New Zealand’s economy [Ev]. The Reel Cinema might be doing well in challenging conditions and its performance may be better than its rivals [Ev]. There is also no information about non-monetary factors that might affect performance [Ev]. The Reel Cinema might be producing a better service that could lead to better performance in the long run [Ev]. In conclusion, we need more information beyond The Reel Cinema’s income statement to accurately judge its performance [Ev].

- 4 a** Gross profit margin is the amount of gross profit earned per \$1 of revenue – the higher the value, the better the performance.

Profit margin is the profit made on each \$1 of revenue – the higher the value, the better the performance.

Current ratio measures the value of each \$1 of current assets to pay each \$1 of current liabilities – the higher the value, the more liquid the business is.

Acid test ratio measures the value of each \$1 of accounts receivable and cash to pay each \$1 of current liabilities – the higher the value, the more liquid the business is.

- b** Acid test ratio: The Reel Cinema’s acid test ratio falls, showing a decline in the business’s liquidity from 2015 to 2017.

Current ratio: The Reel Cinema’s current ratio also falls, showing a similar decline.

Conclude by discussing the significance of the falls. Consider how much they have declined, that they back up the business’s and lenders’ concerns over liquidity, but that there is no guide to what are safe current and acid test ratio values.

## 24 Economic issues

### Activity 24.1

- a** Qatar's economy is in the growth stage of the business cycle.
- b**
- An improving balance of payments: because the value of exports has been rising and the imports have been decreasing.
  - Economic growth: because the GDP of the country has been increasing.
  - Low inflation: because the prices are controlled.
  - Low unemployment: because there are plenty of jobs.
- c** The inflation in Qatar is currently controlled so prices of goods are not rising. Consumers can therefore afford to pay for goods and services and have a better standard of living. With increased spending by consumers, businesses have better sales and find it easier to grow.
- The level of unemployment in Qatar is currently low as there are plenty of jobs. Consumers can therefore earn money and have greater spending power and a better standard of living. The effect of lower unemployment on businesses is that they may find it harder to recruit and retain workers as the workers have a lot of choice. Also, businesses may have to pay more to retain their workers.
- Other points may include: identification and analysis of increasing GDP and improving balance of payments (or increase in exports and a decrease in imports).
- d** Low levels of unemployment are beneficial to the economy because (any **two** points from the list below):
- That means that they do not have to spend as much on unemployment benefits and can spend that money on other infrastructural services.
  - The more people are in employment, the more income tax is received by the government and the greater the spending on improving the country.
  - The higher the number of employed people, the greater the contribution to the total output of the country and economic growth.
- A positive balance of payments is beneficial to the economy because (any **two** points from the list below):
- It has a lot of exports, it earns a lot of foreign currency and this is better for the country's international trade.
  - It has more exports than imports, so there is more money flowing into the economy than going out. This money can then be used as needed for the improvement of the economy.
  - It has more exports than imports and so has enough foreign exchange and does not have to borrow from other countries at expensive rates.

### Activity 24.2

- a** The **two** main sources of government income are taxes and borrowing.
- b** **Two** sources could include:
- Value added tax: a charge added to the value of some goods and services.
  - Import tariff/customs duty: a charge added to the price of goods that are imported from other countries.
  - Sales tax: a charge paid by consumers on the purchase of some items.
  - Excise duty: a charge paid by a manufacturer on the production of specific goods within the country.
- c** The corporation tax rate has been increasing over the last four years as it was 15% in 2016 and is 18% in 2019. This means that it has gone up 3%.

- d** The increase in the corporation tax rate means that the businesses will have a smaller profit after tax, which means that they will have a smaller amount to reinvest and grow. This may lead them to increase prices to cover costs or relocate to other countries with a lower corporation tax rate. The increase in the corporation tax rate also means that the businesses will have a smaller profit after tax and so shareholders will receive fewer dividends. This will discourage existing and new shareholders from investing.
- e** The impact of lowering income taxes on consumers will be that they will have more disposable income so they will spend more on goods and services and have a better standard of living. The impact of lowering income taxes on businesses will be that there will be more demand for their goods and services leading to more sales. Businesses may then increase their production levels to meet the demand.
- f** By increasing the indirect tax rates, the government will collect more from value added tax, sales tax, import tariffs and so on. The increase in the corporation tax rate from 15% to 18% will also increase the government's income as companies will be paying more on their income. However, this may also discourage new businesses from setting up operations there and existing businesses might move their operations to countries with cheaper corporation tax rates. So, over time, the short-term increase in income by increased corporation tax rates will be offset by the loss in income from existing businesses moving operations or the lack of new companies setting up there. The decrease in income tax rates will lead to an increased disposable income and more spending by consumers. This will reduce the income from income tax for the government, but in the long run, businesses will benefit from increased spending by consumers and will make more sales. Increased sales mean more corporation tax (at a higher rate) for the government.

### Activity 24.3

- a** Interest rate is the cost of borrowing money from a bank or the percentage rate earned on savings.
- b**  $(3.0/100) \times 500\,000 = \$15\,000$
- c** The cost of borrowing will increase, therefore consumers will borrow less. Consumers will have more incentive to save as they will earn more interest by depositing their money in the bank, therefore they will spend less.
- d** The cost of borrowing is more expensive so the interest costs for ABC Bicycles will increase and it may decide to postpone its expansion plans. People will spend less and so ABC Bicycles' sales will fall, resulting in a decrease in profits.
- e** An increase in interest rates will make borrowing more expensive for ABC Bicycles and increase its interest costs. Also, consumers will want to save more and spend less so sales of ABC Bicycles may go down. This may make the company defer its plans for expansion. A decrease in the corporation tax rate will mean that ABC Bicycles will have to pay less in taxes and so will have lower costs, which might compensate for the increase in borrowing costs. The overall impact of both of these changes depends on how much debt ABC Bicycle has.

## 25 Environmental and ethical issues

### Activity 25.1

- a** Externalities are the positive and negative effects of business activities on unrelated parties.
- b** **One** example of a positive externality could be: improved infrastructure in the area by having a reliable power supply and better road networks, schools and hospitals. This can be beneficial not only to the employees but also to the community living in the area. Other positive externalities may be: employment for the local people; better products at possibly reduced costs; use of better production techniques so better product possibly at reduced costs.

Example of a negative externality: road congestion caused by delivery lorries, which will also negatively impact the tourism in the area.

Other negative externalities may be: air pollution caused by fumes from the factory; destruction of ecology in the area due to sound and light pollution.

- c** Use renewable sources of energy such as wind power and solar power so that greenhouse gas emissions are reduced.
- Work with employees, customers and suppliers fairly, so that they have better living standards.
- Other steps could be: reduce waste; use packaging that can be recycled; promote telecommuting; use energy-efficient processes and equipment; adopt fair human resource policies.
- d** The social benefits of Synta Plastics setting up operations will be increased employment and improved infrastructure in the area, which will benefit the whole community, not just the employees.
- The social costs of Synta Plastics will be increased pollution in the area, both air and noise. Fumes released from the factory can be harmful and the noise pollution can be an irritant affecting the quality of life of the people there.
- The benefits of increased employment and improved infrastructure will to an extent compensate for the impact of the social costs of increased pollution. Also, Synta Plastics is setting up a factory that uses recycled plastic, showing that it cares about the environment and may possibly have green / environment-friendly operations.

## Activity 25.2

- a** A pressure group is a group of people who join together for a common cause (ethical or environmental).
- b**
- Petitioning: making an oral or written official complaint to the government or food regulatory authority about Tastybites.
  - Demonstrations: this involves a group of people protesting at a rally about the impact of Tastybites on the environment, the health of the people and local businesses.
  - Lobbying: attempting to influence the policymaking/legal controls of the government.
- c** Threat: Tastybites's reputation may be damaged and it may discourage potential customers, employees and investors.
- Other points may include: if regulations are not being followed, then it may create legal problems for Tastybites.
- Opportunity: Tastybites may gain financial incentives for using greener and more environmentally friendly packaging and ware.
- Other points may include: gain publicity which will attract new employees and investors, following government regulations and/or greener methods can give Tastybites a competitive advantage.
- d** The government can use legal controls to minimise the negative effects of business activity by imposing penalties in the form of fines or closure of facilities for ignoring pollution targets or waste disposal laws. To avoid negative publicity, it is likely that businesses will follow all the legal controls.
- The government can also use incentives such as awarding tax credits or allowing tax exemptions for businesses using greener/more environmentally friendly methods of operation. Tastybites could use containers made out of recycled materials to reduce the amount of non-biodegradable waste. The government can also facilitate greener operations by providing the infrastructure for recycling and waste collection.
- Incentives can also be very effective in motivating businesses to go green as this entails a direct benefit for them. They can also gain from the publicity they attract by using green methods.
- Other points may include: government can set up controls which prevent new businesses from opening up in certain areas so that the local businesses are not affected negatively. The government can also set up controls to make restaurant owners and food chains state the nutrition information of food items clearly.

### Activity 25.3

- a** An ethical business practice is a responsible way of carrying out business activity with the interest of all stakeholders in mind.
- b** Any **two** of the following:
- Dangerous working conditions: the toxic fumes produced would be inhaled by the workers causing health issues.
  - Unreasonable workload: not giving appropriate breaks and setting unreasonable targets for workers can be detrimental to their mental and physical health.
  - Working long hours without appropriate compensation: this can be very demotivating for workers and also causes fatigue, resulting in poor work quality.
  - Humiliating discipline: this can be very demotivating, lead to mental health issues and drive workers towards leaving their job.

- c** If Techno Ltd follows ethical business practices, it will benefit from an improved image and reputation, which will help in attracting new investors, workers and customers when it tries to enter new international markets. Workers will also be happier and easier to retain.

However, investing in ethical practices may involve high costs. In the case of Techno Ltd, improving and providing safer working conditions will mean buying safety equipment and clothes, which will cost money. Also, paying the workers fairly will increase its costs. Without a significant increase in sales to compensate, the increase in costs will lead to a decrease in profits.

The improvement in brand image may increase customer base and sales, worker recruitment costs may be reduced and more funding from investors may more than make up for the increased costs, and so I think that Techno Ltd should invest in ethical business practices.

## 26 Business and the international economy

### Activity 26.1

- a** Globalisation is how countries are connected with each other because of trade of goods and services.
- b** Becoming a multinational may provide Moto Automobiles with access to bigger markets, which will help increase the sales of its automobiles and, if costs are controlled, it may lead to an increase in profits.

Moto Automobiles may benefit from lower cost of labour as labour may be much cheaper in Singapore compared to Switzerland. This would help reduce Moto Automobile's total costs and, if revenue is maintained, may help increase profits.

Other points may include: easier access to raw materials, lower production costs, spreading of risk, gain from economies of scale and greater brand recognition.

- c** With Moto Automobiles setting up operations in Singapore, there will be increased employment opportunities for its people. This will help reduce the unemployment rate and increase the standard of living of the local people. However, there will be increased competition for local automobile companies. If Moto Automobiles provides better-quality cars at a better price, then the local automobile companies will suffer a loss in revenue. This may outweigh the benefit of increased jobs and so it may not be a good decision to allow Moto Automobiles to set up in Singapore.

Note: This is an example; other possible answers could also conclude that it may be an overall advantage to Singapore.

## Activity 26.2

- a** A tariff is a tax applied to the value of imported and exported goods.
- b** An increase in import tariffs by Pakistan will increase the cost of the toys so businesses in Pakistan will have to sell the toys at a higher price. This will decrease the demand for the toys. Quotas will limit the number of toys that Tinsel Toys can export to Pakistan, decreasing its sales.
- c** Availability of infrastructure facilities such as roads, transportation and communication can help Tinsel Toys produce toys and video games more efficiently. This can help keep costs low. Availability of a skilled and productive workforce is important to deliver toys on time and keep labour costs low.

## Activity 26.3

- a** A trade bloc would help lower the trade barriers within the member countries and create favourable trade and investment policies.
- b** CH:US  
1 : 3  
So 1 CH = 3 US  
Therefore 20 000 CH = (3 x 20 000) US  
60 000 US
- c** A currency is said to appreciate if the value of the currency increases with respect to another currency.
- d** Effect on Baby Needs:  
Exports from China will become more expensive in the United States, which may decrease demand for baby products from Baby Needs. Baby Needs may suffer from reduced sales and, because of this, may cut its prices or reduce output.  
Effect on consumers:  
The baby products imported from China will become more expensive for importers in the United States. Importers may reduce the amount that they buy from Baby Needs. This may result in consumers having less money to buy and buying alternative baby products (either locally or from other countries in the trade bloc) instead. On the other hand, importers may continue to buy, but sell the products at a higher price, resulting in expensive products for consumers.

## Exam-style practice questions

- a** A company that has operations in more than one country.
- b** A business activity that has a positive impact on the environment and its stakeholders and ensures its survival in the future.
- c**
  - 1** If suppliers are close, then there may be easier access to the products/goods that it sells, which will reduce transportation costs and make sure that goods arrive on time.
  - 2** Lower cost of labour if there is a good supply of labour in the host country.
  - 3** Access to greater markets, which will increase sales revenue and, if costs are controlled, then Universal Stores can benefit from increased profits.
  - 4** Lower production costs because energy costs and rental of business premises may be cheaper in the host country.
- d** Way 1: Fair treatment of all employees. [K]  
Explanation: Though Universal Stores has stores in five different countries [App], it must offer the same wages for the same work regardless of the ethnicity or gender of the worker and irrespective of the country that they are operating in. [An]  
Way 2: Source the goods that it sells from ethical suppliers. [K]

Explanation: As Universal Stores is a departmental store [App] and it sells many different kinds of goods and has many suppliers, it should make sure that the people who make its products are not being exploited or have unsafe working conditions. [An]

- e** Following ethical business practices will help Universal Stores be successful in the two new countries because it will be good for its image and reputation. A good reputation will help in attracting investors and retaining employees as well as in gaining a loyal customer base.

Note: Only one analysis point of impact of good image is needed.

It is important to consider the different cultures of the two new countries because, to be successful, Universal Stores should be sensitive to the culture of the host countries. For example, it may have to provide less of certain food items and fashion clothing, which may not be permitted as per religious beliefs, and more of others which may be more suitable as per the weather and customs.

Note: Either cultural differences or political stability could be considered.

It should also consider political instability as this can make government decision making slower and cause delays for Universal Stores.

In conclusion, Universal Stores should definitely continue to be ethical as it will keep three of its stakeholders happy and be beneficial in the long run. However, it should evaluate the impact of political uncertainty carefully as it will have the least control over it, and be sensitive to cultural differences by adjusting its goods to suit the market tastes.

## Exam-style case study

- 1 a** Advantage: Increased sales [K].

Explanation: Mexico's economy has grown by an average of 2.5% each year since 2013 and grew very fast in 2017. Unless they are being taxed more, consumers have more income and so more of it will be disposable for them to spend on luxuries such as desserts [An in context].

Disadvantage: Falling unemployment [K].

Explanation: Foo Desserts will find it more difficult to find new employees and might have to spend a higher proportion of its budget on wages to attract and retain staff in a competitive job market [An in context].

- b** Consumers have less income: As income taxation increases, the consumers who buy Foo Desserts products may have less income [K], which could lead to a fall in their spending on the goods that they buy [App]. This may mean that Foo Desserts' customers spend less on desserts, which leads to a fall in the business's revenues and profits [An]. This will, however, depend on how responsive Foo's products are to a fall in consumer income brought about by the rise in taxation [Ev]. The desserts are marketed as luxuries rather than essentials so consumers are more likely to stop buying them before other products as their disposable income falls. [An]

Employees might not be as motivated: A rise in income tax could mean that the employees at Foo take home less pay [App] because of higher tax, which could reduce motivation at work [An]. The extent to which this affects their motivation may depend on the size of the tax increase [Ev]; if it is significant, then this could reduce their motivation at work and have a big effect on productivity at Foo [Ev]. If the workforce is motivated by other factors more than by money, such as Foo's strong ethical commitments, and if staff feel well treated in general, then reductions to take-home pay may have a smaller effect on productivity and staff retention. [Ev]

The business has less funding for investment: Higher tax on profits may reduce the funds that Foo has for investment in capital and innovation [App]. Corporation tax has already increased by 7%, which could represent a significant loss of potential investment funds from Foo's profits [An]. If the company has less money for new machinery and equipment, it may be forced to borrow or cancel investment projects [An]. The extent to which this is true will depend on whether the profits tax affects Foo and the other sources of finance that it has access to [Ev].

Conclusion: The most significant disadvantage of the tax increase for Foo Desserts is the impact that it has on its investment funds. Consumer spending on desserts is probably quite low so a tax on income will not have much effect [Ev]. Tax on employees may not affect worker motivation because of the number of other factors affecting motivation [Ev]. A higher tax on profits, however, has a very direct effect on Foo's available funds for investment [Ev], which will affect its longer-term business plan and its ability to trade ethically.

- 2 a** Benefits might include: higher sales if consumers have lower borrowing costs; Foo Desserts will have lowering borrowing costs; and Foo Desserts will find the costs of new investment cheaper with lower borrowing costs. Make sure that your explanations clearly link the benefits to Foo Desserts in context.
- b** You could include the following as effects of new environmental regulations:
- Business costs: costs may rise if there needs to be investment in new capital to meet regulations.
- Administration and bureaucracy: this could become more complicated and time-consuming for Foo, which reduces its efficiency.
- Relationships with the local community: these will improve if the regulations, for example, reduce pollution.
- Conclude with a discussion which helps to justify which of these effects is most important to Foo Desserts. You could, for example, focus on the long-term impacts of administration and bureaucracy if they reduce Foo Desserts's efficiency.
- 3 a** **Four** ways that Foo Desserts might be affected by sustainable development could include: increased costs if there are more environmental regulations to meet; increased bureaucracy and administration to ensure that the business is meeting new regulations; marketing benefits if consumers see Foo Desserts as more environmentally friendly; greater employee motivation if they feel that Foo Desserts is more environmentally friendly. Make sure that your explanations clearly link each example to Foo Desserts.
- b** You could include the following as effects of a more ethical approach by Foo:
- Brand image and reputation: this could be enhanced in the mind of Foo Desserts customers and lead to an increase in sales.
- Motivation of employees: this might improve if employees feel motivated by a more ethical approach.
- Increased cost of materials: this could occur if Foo Desserts's business practices have to change to be more ethical.
- Your conclusion could, for example, focus on increased sales as a key benefit to Foo Desserts because of the long-run increase in profits. Make sure that you justify the decision that you make with examples given in context.
- 4 a** Benefits might include: increased sales from international markets; spreading risks across international markets; economies of sales that result from greater sales and output; increased access to lower-cost inputs from international suppliers. Make sure that your explanations show how these benefits relate to Foo Desserts.
- b** You could include the following advantages and disadvantages of global expansion for Foo. Include explanations of the **two** of each that you state, showing how they will affect Foo:
- Advantages: increased sales revenue from new markets; economies of scales from increasing output by expanding into new markets; spreading risk across different markets beyond Mexico.
- Disadvantages: different operating regulations in Argentina and Brazil; social and cultural differences between Mexico and other South American countries; dealing with the exchange rate between Mexico and other South American countries.
- In your conclusion, discuss whether Foo Desserts should become a multinational by, for example, considering how the market growth that being a multinational gives the business outweighs increased operating costs such as having to comply with more regulations. Justify your reasoning with examples that apply to Foo Desserts's business.