GCSE Revision 101
Guide to Business Studies
OCR Specification B

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Significant contribution Letts Revise GCSE Business Studies
There are four factors of production to any economy. Factors of production are resources required to produce, market and supply products and services to consumers.

1. Money, or capital, is used to invest in machines, equipment and companies which all contribute towards producing resources.
2. People who are willing to take the risk of setting up a business and make business decisions make the enterprise.
3. Agriculture, housing and leisure activities all require land – this also includes provision of natural resources such as iron ore, and the sea for fish and oil.
4. The number of men and women available to work is labour.

Remember CELL (capital, enterprise, land, labour) when it comes to factors of production.

Because a business has to make so many decisions, it encounters many opportunity costs. This happens when you have a business decision to make, and you choose an option – the opportunity cost is what you have lost from not choosing the other option. For example, if you have the choice of spending £2,000 on more materials or a new machine, and you spend it on more materials, the opportunity cost is losing out on the new machinery. We say that the wants we reject are unsatisfied and so we miss out on them.

Specialisation

A lot of businesses specialise by using division of labour. This is when employees specialise in different jobs, and there are different factions to the work force (for example, you will have a finance, sales, marketing department, etc). This enables a firm to have specialised machinery because experienced employees can manage it.

Specialisation can be applied to an entire country, which all depends on their natural resources available and the climate: for example South Africa with its gold mining.

However, specialisation more often occurs in people. This arises because people receive training to become specialised in a certain line of work. However, these people still require the essentials we do – housing, clothes, plumbing, etc – which is why we still rely on others to do these things for us. This interdependence relies on the money raised from selling goods and services demanded.
Primary, Secondary & Tertiary Production

There are three “stages” of production:

- **Primary production** always involves some means of extraction. Examples include fishing, mining and farming.
- **Secondary production** focuses around either manufacturing or construction. Examples include car manufacture, building houses and bridge construction.
- **Tertiary production** involves the selling of goods and services to consumers. Examples include retail, hospitality and banking.

As a product moves through these production types, it gets **added-value**. It begins with a raw material (primary), and is manufactured into a good (secondary) at which stage it is worth more, and yet more value is added when sold (tertiary).

Economies develop and employments move from sector to sector. When employment moves from the secondary sector to the tertiary sector (i.e. manufacture to service) it is known as **deindustrialisation**.

Population Structure

Population is crucial to a country’s economy. It provides it with entrepreneurs to provide business opportunity, and it also provides labour. The demand of products also depends on population – so any change in population will result in a change in the economy.

Factors affecting the population include birth rate, death rate and migration.

Types of Unemployment

There are several different types of unemployment, and each have their own causes:

- **Frictional unemployment** is temporary and voluntary, and occurs when you are looking for a new job – it is the period of time you are spent without a job looking for a new one.
- **Structural unemployment** occurs when there is a long-term change in supply or demand. For example, when something becomes unfashionable or out-of-date, another cause might be competition from overseas labour causing a downfall in demand in the UK.
- **Cyclical unemployment** (or demand deficient unemployment) occurs when there is a lack of demand for a job in a specific industry in the economy.
- **Seasonal unemployment** can be found in tourism and agricultural industries where people are unemployed at certain times of the year. Another example is a Father Christmas only being employed in December.
- **Technological unemployment** occurs when it becomes possible for someone’s job to be replaced by a machine, immediately placing them out of a job; as an economy mechanises, this becomes a more and more frequent problem.
Business Organisations

The UK Economy

The UK has a **mixed economy** made up of a **public sector** and a **private sector** as shown:

The public sector consists of central and local government firms which run under State control. They are there to provide services, such as education, police and standards agencies. The private sector businesses are owned by individuals, not the State. They can be run by one or thousands of people, and they aim to make a **profit** from producing and selling their products to consumers.

Business Objectives

There are a few different business objectives which a business will hope to achieve:

- New businesses especially will want to **survive**. This means making sure the business does not go into liquidation. Often, a loss will be made – but this can be accepted in hope that the following year the business will do well
- A business may want to increase in size and customer-base. This is called **growth**. A common way of doing this is to increase the local, national or international **market share**
- Since the only reason entrepreneurs are in the private sector is to make some, **profit** is another key objective

Incorporated & Unincorporated Businesses

**Sole traders** and **partnerships** are examples of **unincorporated businesses**. A sole trader is set up, owned and run by one person, such as a traditional corner shop. A partnership can be set up and run by multiple businessmen, and tend to be the professions (such as the dentists and doctors).
A major disadvantage of these unincorporated businesses is that they have unlimited liability. This means that the owners themselves can be held responsible for any debts a business may incur.

Common in the secondary and tertiary sectors are limited companies. These are incorporated businesses, which take more formalities to go through when setting up. However, they have separate legal existence which means they can take legal action through the company’s own name and not theirs – so they have limited liability. This is why a limited company must use “Ltd.” or “plc” in its name to warn traders that if they get into debt with the company, they may not be able to pay them off with limited liability.

An advantage to having this limited liability is that should your business fail, you can only lose as much money as you have invested into the business. Whereas with sole traders or partnerships, the owners’ own personal savings have to be used to pay the debts.

Sole traders (or sole proprietors) are easy to set up and are the most common business in the UK. They are owned and run by one person, and usually the capital is supplied by one person. The table shows advantages and disadvantages for sole traders:

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profits are not shared with others</td>
<td>BUT The owner has unlimited liability</td>
</tr>
<tr>
<td>Small-scale business, so small amounts of capital needed</td>
<td>BUT Small-scale nature makes it difficult to expand</td>
</tr>
<tr>
<td>The owner is their own boss</td>
<td>BUT Responsibility cannot be shared easily</td>
</tr>
<tr>
<td>Quick decisions can be made</td>
<td>BUT Long hours and few holidays</td>
</tr>
<tr>
<td>Easy to establish</td>
<td>BUT Difficult to continue upon the owner’s retirement or death</td>
</tr>
</tbody>
</table>

With partnerships, a deed of partnership (or partnership agreement) is drawn up to set out the key details of a business. The main details needed are shown below:

<table>
<thead>
<tr>
<th>AGREEMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>Names of partners ...............................</td>
</tr>
<tr>
<td>Capital contributed £.................</td>
</tr>
<tr>
<td>£.................</td>
</tr>
<tr>
<td>How profits and losses are shared ..........</td>
</tr>
<tr>
<td>Partnership salary £....................</td>
</tr>
<tr>
<td>paid to ........................................</td>
</tr>
</tbody>
</table>

The Limited Liability Partnerships Act was passes in 2000 which allowed partnerships to be more similar to limited companies. The limited liability partnership has to use “LLP” at the end of its name, and the LLP is a legal person separate from the other members.

**Limited Companies**

There are two documents required to set up a limited company, called the memorandum of association and the articles of association.
The memorandum of association is all about the company’s relation to the external world. You can expect to find in it several pieces of information:

- The **name** clause ensures the company name is not copied
- The **objects** clause lays out the purpose of the company
- The **situation** clause states where its principal office is located
- The **liability** clause confirms all members have limited liability
- The **capital** clause describes the amount of capital it will have
- The **association** clause must be signed by some of the members

The articles of association governs the internal workings of the company. It outlines how the directors are to be elected, and the number, rights and duties they have; how meetings are called and how profit is to be shared amongst them.

There are two types of limited company: **public limited companies** and **private limited companies**. A public limited company uses the abbreviation “plc” and floats on the Stock Exchange where they can be bought and sold by members of the public. Private limited companies, “Ltd.” do not. A disadvantage of being on the Stock Exchange is that your company can be taken over by rivals via a **takeover bid**.

### Co-operatives

There are two types of **co-operative** in the UK economy: **worker** (or **producer**) co-operatives and **retailer** co-operatives. Worker co-operatives arise when workers buy out their company often when they are financially troubled and begin to run it themselves.

Retail co-operatives were started by the **Rochdale Pioneers** because they felt exploited by local shops. Examples include the shop the Co-op. Their features include:

- wider aims than most business, for example, **political**, **social** or **ethical** aims
- anyone can join a society by buying a share in it (not sold on the stock exchange though)
- one vote per member, regardless of number of shares held by each person
- members share profits and elect the management committee

### Franchises

A **franchise** works by having a company – the **franchisor** – allowing its **franchisees** (people who have bought a franchise in the company) to use its name, logo and sell its products.

Taking out a franchise reduces the risk of business failure because the franchisee is taking advantage of the franchisor’s previous business successful record. The franchisee also doesn’t have to do the promotion itself nor manufacture the goods to be sold.

The benefits to the franchisor include expansion of the company without investing capital and having a highly-motivated franchisee.
The Public Sector

A public corporation is formed by an Act of Parliament, which sets up its functions and organisation. Its day-to-day running however, is controlled by a board, appointed by a government minister. The government will set its financial targets annually.

Many public sector organisations and nationalised industries have been privatised by the government since the 1990s. This means transferring the organisation from the public sector to the private sector. The reason for doing this is to supposedly make the company more efficient as it experiences competition from other companies. Privatised companies become public limited companies.

Stakeholders

Any group of people which has an interest in, or an influence on, a business, is a stakeholder in that business. These can be internal or external. Examples include the following:

- Suppliers
- Customers
- Shareholders
- Local community
- THE FIRM (Directors, Managers, Employees)
- Lenders

Stakeholders can have a serious effect on business operation. For example, customers may want lower prices, which will eat into a firm’s profit margin, affecting their profits. Employees will be more concerned about job security than short-term performance.
3 Business Structure

Internal Business Structure

There are many different departments in large companies which are all interdependent (i.e. link together and work closely with one another):

- **Production** – this department manufactures goods by turning raw materials (inputs) into finished products (outputs)
- **Finance** – or sometimes the accounting function, obtains, records, controls and analyses a firm’s funds, and its efficient operation is vital for the firm’s success
- **Marketing** – this department is responsible for selling, market research, promotion (advertising), packaging design and distribution
- **Purchasing** – or sometimes the buying function, ensures that the firm purchases the right quantity of raw materials at the right times
- **Human Resources (HR)** – or sometimes the personnel function, is responsible for hiring and firing, as well as staff records, organising their wages, etc

Organisation Charts

These can be used to outline the hierarchy of the business structure, showing the different departments of a firm. Each person on the chart is separated either vertically or horizontally by their status, so they are ranked in order of importance. It also details the communication lines between the functions.

One key feature to an organisation chart is the span of control. This is measured by the number of staff directly controlled by that person. The span of control obviously depends on how important someone is in a business; but it can also be affected by the nature of the work. For example, highly-skilled work will require a lot of supervision, and so the person supervising will only be able to control a limited few people.

The chain of hierarchal structure outlining everyone from the bottom to the top of the business is the chain of command. It shows who makes decisions and who is responsible for whom. It runs from the Board of Directors to the department managers, and then from them to the staff of that department.

A firm may be defined as **tall** or **flat**. A tall organisation has more levels than a flat one, which indicates communication will take longer to send messages around the business; that generally span of controls will be narrower; and that there will be more specialised employees.
Not every decision can be made by the Board and they cannot hold every responsibility, so they are able to delegate these to the managers of departments below them. The department heads will therefore delegate their daily routine jobs to the staff in their department, further down the chain of command. When this happens, the person doing the job will have to be given authority to do the job by the person above them. They then have the responsibility of doing that job.

### Communication

Firms and customers keep documents to serve as proof of purchase and proof of transactions. There is a flow of documents between a buyer and seller:

Communication involves the sender, the message, the medium (i.e. how it is being sent) and the recipient. Communication can take place within the firm (internal) or to people outside the firm (external) like customers or stakeholders. It can be formal or informal, and it can be written or oral.

- A letter can be internal or external. When internal, it is often used to be sent to an employee to warn them that their behaviour may lead to dismissal.
- A memo is less formal than a letter, and is always internal. It is more concise than a letter and so can be more ambiguous.
- Written reports can be published and sent around which are formal and very informative to the recipient.
- Annual reports and accounts are external as they are published to the general publicly to its shareholders.

The two main methods of oral communication are:

- Telephoning – this is both internally and externally used, and is more flexible and faster than letters or memos – although emails are preferable nowadays because it is also quick to send an email, and there is still the written form available in front of you.
- Meetings – these can be formal, where they are minuted and have an agenda or not.
Measuring Business Size & Growth

A firm has a number of reasons to want to grow in size. These include having better chances of survival, and benefiting from economies of scale. There are four main tools to measure the size of a business:

1. Turnover (net sales, i.e. sales less VAT) is the most popular way
2. A firm’s net profit figure can be a good indicator, although certain firms in the same industry operate under a different profit margin
3. The capital employed figure shows the net investment of a firm but can be a difficult figure to measure
4. The number of employees will be affected by a firm’s size too, but this can be confusing because most businesses have both full-time and part-time staff working

Many firms grow organically (naturally via internal expansion). This is done by producing and selling more products, selling products in a new market segment and by introducing new products to the market.

The name given to external growth is integration. This can happen via a takeover which occurs when a company has bought enough of another company’s shares to take control of the business; or via a merger which takes place with the two companies’ agreement.
People in Business

Why Do People Go To Work?

There are a number of reasons people might go to work where they do:

- To fulfil a duty - for example going to join the Army
- Personal development - exploring yourself, finding your talents and hidden potentials
- Self-satisfaction - you may feel a sense of achievement whenever you perform well
- To learn new skills and build a career
- To meet new people - perhaps you want a social job, or maybe just like the presence of pleasant people
- To earn money
- To support a family - similar to earning money - but this is a need and less of a want

Recruitment

A department with a vacancy will need to consider the type of work to be done and the type of person needed to do the job before they can employ someone. The job description contains the details of the work (job title, location, responsibilities, hours, wages, etc) and the person specification outlines the details of the person needed (qualifications, personal qualities, work experience, physical and mental abilities).

A job may be advertised internally – where adverts will be placed on notice boards, published in the company magazine or offered to current staff. Alternatively, external job advertisement involves local ads in newspapers as well as Job Centres and employment agencies. An advantage to internal job advertisement is that no “new blood” is introduced to the company, and the person is already suited and knows what they are doing.

A job application form is filled in by someone who wants to apply for the job which asks them about education and previous experience. They will also be asked to provide references from people prepared to support their application. Alternatively, a curriculum vitae (or CV) may be submitted – created by the applicants themselves.

A short list is drawn up from all the applicants. This list comes about when all of the applicants who did not meet the person specification are eliminated from the decision process.

The next stage is to interview the remaining applicants. In an interview, the interviewer can analyse the applicant’s social and communication skills, as well as their confidence – plus their physical appearance.
Some firms might run tests on the applicants to test their suitability for the job. Examples of these tests include personality tests, intelligence tests and aptitude tests.

### Appointment

After having chosen the correct applicant, they become employed and a contract of employment is drawn up:

### Termination

An employee may be made redundant. Redundancy occurs when a person’s job ceases to exist – for example when a company goes bankrupt. As this is the only reason they are being terminated, it is against the law for the company to rehire someone else to do the job. If the company can afford it, redundancy pay may be dealt to the person (it is usually one week’s pay for every year they have worked there) but is only paid to those who have worked there for at least 24 months. For example, someone who has worked at a company for nine years and is made redundant would receive nine week’s pay.

When there is a good reason to do so, an employee may be dismissed from their job. This occurs when:

- the employee is stealing the company’s goods
- continuation of the employee’s job is illegal (e.g. a lorry driver is banned from driving)
- poor behaviour at work (i.e. drunkenness or violence)

All employees have automatic protection against unfair dismissal, and can have a tribunal if they believe they have been unfairly dismissed. If the panel decides they have been, they can either force the company to rehire the person and pay a small compensation sum, or simply pay a large fine and compensation.

### Training

It is down to the Human Resources department to take care of training employees. When a new employee begins work with a business, they are wanted to start work efficiently as quickly as possible, so they go through induction training, which can be either internal (inside the firm) or external (trained outside the business).
The point of induction training is to get employees to settle in as soon as possible and contributing towards the workforce almost immediately. A typical induction training programme is as follows:

**INDUCTION PROGRAMME FOR NEW STAFF**

<table>
<thead>
<tr>
<th>Day</th>
<th>Activity</th>
<th>Venue &amp; Time</th>
</tr>
</thead>
<tbody>
<tr>
<td>MONDAY</td>
<td>Our company’s history and present day activity</td>
<td><strong>Board Room, 10am</strong></td>
</tr>
<tr>
<td></td>
<td>Tour of the company</td>
<td><strong>Board Room, 11am</strong></td>
</tr>
<tr>
<td></td>
<td>Lunch</td>
<td><strong>Staff Canteen, 1pm</strong></td>
</tr>
<tr>
<td></td>
<td>Human Resources in your development</td>
<td><strong>HR Department, 2.30pm</strong></td>
</tr>
<tr>
<td></td>
<td>The work of your department</td>
<td><strong>Interview Room, 3pm</strong></td>
</tr>
<tr>
<td>TUESDAY</td>
<td>Introduction to your department</td>
<td><strong>Manager’s Office, 9am</strong></td>
</tr>
<tr>
<td></td>
<td>Meet your new colleagues</td>
<td><strong>Department, 9.30am</strong></td>
</tr>
</tbody>
</table>

Internal training (or **on-the-job training**) is the most popular form of training, and it involves being taught whilst you work, usually by a person currently doing the job or by an instructor hired by Human Resources. Advantages include it being quick and inexpensive, and because it is situated at the business’ location itself, the training is strictly related to the firm’s needs. Disadvantages include that the training is only as good as the trainer who may not be properly qualified to train someone.

External training (or **off-the-job training**) involves employees going to local collages or training providers to study and learn new skills. Advantages are:

- training is done by a professional (good quality)
- more motivated trainee because they are studying for a recognised qualification
- introduces new ideas to the trainee from outside the firm

However, off-the-job training is significantly more expensive than on-the-job training.

Another type of training is an **apprenticeship** and the Department for Education and Employment has set up the **New Deal scheme** to help financial costs related to training.

**Motivation**

Motivation is a key part of work, because it is all linked to **productivity**. A business will aim to try and keep its employees as motivated as possible.

- pay rises
- better working environment
- bonuses
- appraisals
- pension plans
- additional responsibilities
- staff social events
- company shares
- promotions
- company car
- staff discount
- team-building activities

**Financial methods**
**Non-financial methods**
Maslow’s Hierarchy of Needs

Abraham Maslow put forward a number of human needs which he believed we went to work to satisfy. He said that as one need became satisfied, another one opened up – so he made a hierarchy of needs.

Maslow says that employers need to recognise that there is this range of needs which needs to be met. So they should try and provide their employees with jobs that satisfy the needs in order to have a high output.

Herzberg

A different psychologist, Frederick Herzberg, identified hygiene factors in work. These are the basic, essential factors such as acceptable working conditions (e.g. safety, cleanliness and rest breaks). Ignoring these factors will create a fall in morale and motivation, leading to lower productivity and an unhappy workforce.

Herzberg said that these needed to be present at work, but they alone would not motivate employees. The motivators for employees include:

- recognition – having all of your efforts noticed by others
- achievement – that “job well done” feeling
- advancement – new skills; actual or possible job promotion
- responsibility – being given new responsibilities to do

Job Enlargement, Job Enrichment & Job Rotation

Other attempts to motivate employees include job enrichment – which is giving employees a range of tasks to use their full abilities and increasing their responsibilities. Job enlargement is increasing the number of duties they have to do. And job rotation is rotating the tasks done between employees so that they are not repeatedly doing the same thing.
Job Satisfaction

There are a number of influences of job satisfaction:

- **Pay level** is an important one because the higher the pay the more disposable cash they will have for material possessions. However, some employees will accept a lower pay level than they might get elsewhere if the other factors are beneficial enough.

- **Perks** (or posh name fringe benefits) including company cars (or subsidised travel), good pensions, private health insurance and a staff discount.

- The **working hours** may be attractive, including paid holidays and the length of time an employee is required to work “unsocial” hours (i.e. late night, bank holidays).

- **Working environment** is another factor – influences on it are noise, cleanliness and quality of the heating and air conditioning available, if any.

Paying Employees

Generally speaking, **wages** are for manual work, such as builders and plumbers, and are paid weekly. A waged employee will be able to work and earn overtime. Employees earning a **salary** are usually clerical-based; and get paid monthly. A salaried employee has a fixed annual sum, which means there is seldom overtime, and they may be less motivated to do a good job – because they get paid the same each month whether their productivity is high or low.

Factors influencing the different pay levels around include:

1. The length of training and the level of qualifications of the employee
   Doctors, accountants and lawyers have high salaries for this reason
2. The type of economy the employee works in: the private sector more often than not pays better than a job in the public sector
3. Supply and demand of labour – if someone possesses a skill which is in short supply but highly demanded, they will be offered a nice payment package
4. If there is a risk of danger or discomfort involved in the job, higher pay may be the case as a potential compensation – such as oil rig workers
5. The location of the work, for example, the UK’s London weighting

Payment Systems

Salaries are paid at a fixed rate (one twelfth of their annual salary paid to them each month) which is a **flat rate** pay. Some waged workers also get paid a fixed amount at the end of their working week, which is also flat rate. The advantage of flat rate to a company is that it is easy to calculate as it is the same each month or week; but the major disadvantage is that an employee might not feel motivated enough to produce such a high output if their pay is the same whether they do or they don’t.
**Time rate** is where employees are paid a certain amount for each hour they work, and after a given number of hours have been worked, they may receive **overtime rates** (common overtime rates are time and a third, time and a half and double time rates). The advantage to the business of this method of pay is that extra work may be done by the employees out to receive higher pay, but it is harder to calculate, as a clocking in and clocking off system is used in this particular pay rate.

Employees manufacturing items are paid using **piece rate**, where they receive a set amount per each item made. The items must be of an acceptable quality to receive pay. Similarly, salesmen might receive **commission** for each sale they make. The advantage is that employees work harder with a higher output, but the disadvantage is that they might rush their work for more pay, so quality falls and as a result more quality control supervision becomes necessary.

### Bonuses

Employees may receive a **bonus** at certain times of the year – usually Christmas. A **merit bonus scheme** is one where employees with the highest efficiency, or employees exceeding their production or sales targets, receive bonuses. This encourages their loyalty, but can cause disputes as the level of bonus to be rewarded is difficult to calculate.

### Trade Unions

Because employees alone are not very powerful, they often act together as a single unit, called a **union**. People join unions to protect their jobs, to improve their working conditions, to have more pay and to gain more say in management’s long-term plans.

There are two types of union – **blue-collar unions** and **white-collar unions**. Blue-collars are all of the unskilled, semi-skilled and skilled workers – such as **craft unions** (e.g. Musician’s Union), **industrial unions** (e.g. the retail trade’s USDAW) and **general unions** (e.g. UNISON). White-collar unions are all of the professional workers, and the clerical employees, such as the **NUT** (National Union of Teachers).

The aims of unions include:

- Negotiating with employers – bargaining usually for pay, bonuses, working hours, etc
- Protecting their members against unfair dismissal, possible layoffs and redundancies
- Advising and representing their members legally
- Influencing other employers, employees and organisations

When a dispute arises between a company and a union, the union can act by organising...

- **overtime bans** leading to a fall in output – but they still work regular hours
- **work-to-rule** work, where the employees will follow all of their work strictly to the rules of the company, which slows down the output
The last resort after these is to completely withdraw labour – and go on strike. This isn’t popular with unions because they lose pay, legal issues may come up, and the business may have to ultimately close – so everyone loses their job. Strikes can be official, organised strikes where union members vote and decide to withdraw labour for a small period of time (e.g. the NUT strike, 2008). They can also be unofficial (or wildcat strikes), but these are less common nowadays. Wildcat strikes often use picketing to discourage others from crossing the picket line and entering the business’ premises.

A dispute might eventually be resolved by an agreement between the union and the business in question, but if it goes on for too long, ACAS may get involved. ACAS (the Advisory, Conciliation and Arbitration Service) will aim to improve the relations:

1. conciliation – an ACAS official talks to both side to find areas of common ground which can form the basis of further negotiations
2. arbitration – when both sides agree, their dispute goes into arbitration – where ACAS provides a third party to listen to both sides and offers a settlement, but by agreeing to go into arbitration both the business and union must accept the settlement no matter what
Methods of Production

Flow production (or mass production) involves a continuous production process, where each and every item produced is identical to the next. This is used when every product manufactured must be the same, for example, making blank CDs.

Batch production allows for different products to be made in batches on the same production line. The type of product being made is rated every so often, to give it time to make so many of that product, and then rotated to make so many of the next product. An example would be making Walker’s crisps.

Job production (or unit production) involves making one unique product at a time which is not the same as the next. The product is based on the user specification (the requirements and the design desired by the consumer).

<table>
<thead>
<tr>
<th></th>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Flow</td>
<td>❖ least expensive</td>
<td>❖ if one station breaks down, the whole production line stops</td>
</tr>
<tr>
<td></td>
<td>❖ not labour intensive</td>
<td>❖ has a reputation for bad quality</td>
</tr>
<tr>
<td></td>
<td>❖ produced rapidly by machines</td>
<td></td>
</tr>
<tr>
<td>Batch</td>
<td>❖ produces multiple products</td>
<td>❖ time wasted changing the production line for a different product</td>
</tr>
<tr>
<td></td>
<td>❖ employees become skilled in their sections, increasing output</td>
<td>❖ stock space is used holding one product whilst another is produced</td>
</tr>
<tr>
<td></td>
<td>❖ relatively cheap, machines used</td>
<td></td>
</tr>
<tr>
<td>Job</td>
<td>❖ meets customer’s unique needs so they will be willing to pay more</td>
<td>❖ very expensive method of production</td>
</tr>
<tr>
<td></td>
<td>❖ product automatically has a USP</td>
<td>❖ very labour intensive – costs the business more in wages/salaries</td>
</tr>
</tbody>
</table>

These production methods have lead to a number of problems including bored staff with low morale, over-specialised machinery not being able to respond to market changes and machinery breakdown/employee strikes halting productions. Therefore, lean production was introduced, which sets out to reduce costs and improve morale and product quality.

A business’ approach to lean production may be based on any of the following:

Cell production: this tries to tackle low morale of employees working on a flow production line. They production line is divided into different cells, which all contain people who work on an individual part, but identifiable part, of the finished product. They become specialised and develop skills from doing this, and feel more satisfied about their contribution.
Just-in-time (JIT) was introduced to reduce stockholding costs by producing stock to order. This is an alternative to producing as much stock as possible to be sold, because holding that stock is very expensive.

Kaizen was introduced on the idea that it is better to invest in the views and ideas of the staff than in new resources such as equipment. Using this approach, employees not only carry out their work, but also look for ways to improve their work. Groups must be established to put the Kaizen approach into practice – for example, a shop-floor production cell may get together to discuss ideas and solutions to existing problems.

### Productivity

We define productivity as how efficient a business is at producing its products. It can be measured by recording the average number of products made per employee.

The term productive capacity refers to a business’ resources. When its premises, machinery, equipment and workforce are all working at their maximum output, it is said to be operating at its full capacity. However, this is not necessarily good always, because it can lead to pressure on staff and pressure on the equipment (i.e. more wear and tear).

### CAD/CAM/ICT

It is essential that a firm’s technology is working as effectively as possible. The use of ICT is so important to a business because it can increase productivity in the use of machines. The introduction of machines to replace human labour is called mechanisation.

CAD (computer-aided design) packages are used to create efficient product designs which can be easily altered using light pens and touch-sensitive screens. CAM (computer-aided manufacture) is the use of robotics and machines to make products effectively.

### Quality Control

There are two methods of quality control: quality control and total quality management. Quality control itself is a type of quality control which, teamed with quality assurance sets quality standards and implements them in the business. These standards are agreed by the company selling the products as well as the manufacturer. The main aims of quality control are to stop problems arising in the first place; to detect quality problems before the goods reach the consumer and to correct any problems incurred.

Total quality management (TQM) aims to establish a hallmark of quality also, but is implemented at every stage of the production line, therefore, it is more expensive to run and takes a lot more time investment.

A quality circle is similar to Kaizen groups, in that groups of people working on the production line will get together to discuss problems with quality and potential solutions.
A business has to hold stock, but it proves costly. There are conflicting “pulls” which influence the business’ decisions in how much stock to buy and control, as shown:

The best level of stock a business can hold at any one time is called **optimum stock.** This is the level of stock which minimises costs but still has some for production. There are four control levels used to calculate this level:

1. The **reorder quantity** is the number of items of stock the business will need to reorder when the reorder stock level has been reached.
2. The **reorder level** is the point at which stock must be reordered.
3. The **minimum stock level** is the level which stock cannot fall below.
4. The **maximum stock level** is the level of stock which the business will hold more than.

We can show these all on a **stock control chart:**
Economies of Scale

Producing products on a large scale benefits a company as cost per unit begins to fall with increased output. This is called **economies of scale**. Internal economies of scale occur as a result of something internal to the business causing a reduce in production costs:

- **economies of increased dimensions** arise with an increase in size, for example oil companies use “super tankers” which can hold 20 times the capacity of smaller ships but only cost three times as much to produce and run
- **financial economies** – larger businesses are assumed to be more stable and so find it easier to obtain loan capital and can negotiate lower interest rates on their loans
- **managerial economies** – expert, highly-qualified managers can be employed by larger scale businesses who can perform better than those less experienced
- **marketing economies** – larger businesses can afford to purchase the services of specialist marketing companies and advertising agencies; and the cost of promotion is spread over more sales, so cost per unit is reduced
- **purchasing economies** (or **bulk-buying economies**) – larger businesses receive discounts when they buy in bulk; and can negotiate cheaper prices, reducing cost per unit
- **risk-bearing economies** – larger businesses have a larger product mix and so the risk is spread out more between the different products and the different markets
- **technological economies** – larger businesses can invest into better machines which increases productivity, and they can also invest more money into research and development which smaller companies cannot spend much on

As industries grow in size, businesses may also benefit from external economies of scale:

- **information economies** – businesses in the same area may link together and share information to benefit each other
- **concentration** – when many businesses of the same type are focused in one area, suppliers may be encouraged to relocate there
- **skilled staff** – also through location and specialist training programmes, specialist staff can be sent into these businesses
- **reputation** – a local or regional reputation can help firms in that region and encourages other firms to locate in that region also

**Diseconomies of Scale**

A business can become too large that it suffers from **diseconomies of scale**. This causes an increase in cost per unit. These can arise when the firm is so large that there is a tall chain of command, which results in a lack of contact between management and the workforce, causing poor labour relations and employee dissatisfaction which may lead to low morale of the employees, higher absenteeism and lower productivity of the workforce.
6 Market & Good

Consumer markets supply goods and services to consumers like us. These consist of:

- single-use consumer goods such as good or domestic power
- consumer durables such as DVD players and TVs
- consumer services such as barbershops and dentists

An industrial market (or commercial market) supplied the goods and services needed by a business. These include capital goods (major assets such as machinery) and industrial services, e.g. office cleaning, stationery printing, etc.

Markets can also be identified in terms of size. A consumer market may be a mass market which appeals to everyone (for example, consumer durables and most foodstuffs). Within a mass market you might find a niche market which appeals to a small audience, for example certain foods which are eaten by a particular culture.

Market Segmentation

The market for a product can be broken down into different segments (sections). Examples of factors which affect market segments are:

- age – important when, for example, youth fashion would influence a manufacturer’s decision on what product to market
- population – the size and geographical distribution of the population affects how and where to advertise the product and where to store and sell it
- income – the size of the disposable income is also an important factor affecting product price and quality

Socio-economic Groups

People can be grouped into socio-economic groups using the following:

- A executive lawyers, business owners
- B professional doctors, teachers, accountants, solicitors
- C skilled plumbers, electricians, builders, chefs
- C semi-skilled butchers, taxi drivers
- D unskilled retail workers, receptionists
- E unemployed unemployed, retired
Market Research

There are two methods of market research: primary (or field) research is obtaining new information yourself; and secondary (or desk) research uses existing sources of information obtained by other people or by yourself from an earlier date.

Primary research may be in the form of a questionnaire, which has been designed specifically for the task (completed either in a face-to-face interview on the street, over the telephone or sent out by post for completion); focus group or consumer panel which both ask selected people to provide detailed comments on the product they are presented with; or test marketing where the product is released in only one area of the country and its reactions to the product are monitored to decide if it should be released elsewhere. The major advantage of primary research is that it is specific to the product in question.

Secondary research, on the other hand, can be using your own sales statistics, analysing competitors’ existing products and using Government and other published statistics. Mystery shopping is another example of desk research. The advantages of secondary research are that it is less expensive than primary, and far quicker to obtain.

There are research companies who you can pay to do secondary research for you, such as Mintel, but this is costly and the data may be unreliable.

The Marketing Mix

The marketing mix (the 4 Ps) consists of four main areas (five if you include packaging, more often considered part of product) which the marketing department has to consider.

Product

The first area is product. Many business produce and sell their products. The range of products they market is called the product mix. The business must know what market they want to aim a product at before they make a product. A product can be analysed using the product life-cycle. Because all products are finite (i.e. limited), they all go through a number of stages since going on the market before coming back off of the market.
1 **Introduction** – the product has been developed following successful market research and it is introduced to the market – sales are low at this point, so heavy advertising is needed to increase sales

2 **Growth** – more and more consumers buy the product and brand loyalty has been established, so sales rise and the product becomes profitable as sales revenue begins to pay off the earlier development costs

3 **Maturity** – sales are at the highest they will ever be, consumers have brand loyalty to the product, and it has reached market saturation, so the business’ competitors will be releasing rival newer products to knock it off the market

4 **Decline** – the combination of competitors’ newer products, changes in tastes and fashion and technology changes cause sales to quickly decrease, until eventually the business stops producing the product and it comes off the market

To increase the length of the product life-cycle there are a number of extension strategies which can do this. They might be a change in packaging to make the product feel new and improved; a new advertising campaign or more sales promotion (i.e. special offers and BOGOFs).

In order to ensure customers buy their products, businesses try to establish a unique-selling point (USP) with their product. This creates differentiation between rival products and encourages consumers to buy theirs.

### Price

Another one of the 4 Ps is price. There are both internal and external factors affecting pricing decisions within a business. It can choose cost-plus pricing (also called full-cost) where the business adds a mark-up onto its cost of production. For example, if a product costs £2.00 to produce, a mark-up of 50% would put the price at £3.00. However this method of pricing is bad because it ignores competitor pricing.

Basing a product price on breakeven is another popular method. This is called contribution pricing. Other pricing strategies include...

High-pricing strategies:

- **skimming**: when a new, unique product is released on the market, consumers will be desperate to buy it, so the business sets a high price to cream the market, and as interest dies and the product becomes old, the price is lowered to keep people buying it
- **maximising**: for a product with a short product life-cycle, the manufacturer will try to maximise profits by charging high prices before it goes off the market again
- **premium**: premium pricing is used when a business thinks its product is the absolute best in the market and so will charge higher prices for it
Low-pricing strategies:

- **penetration**: the product is introduced at a low price to obtain a low market share, and once brand loyalty has been established, prices increase to get more profit
- **capturing**: used for businesses marketing linked products, such as a computer company selling hardware and software – it may sell cheap hardware so that the consumers buy their expensive software
- **loss leaders**: these sell at prices below the production costs (so the business actually makes a loss for that product) in the hope that the consumer will buy the other products

Other pricing strategies:

- **odd**: using odd numbers at the end of prices, e.g. 99p, £1.95
- **discrimination**: different prices for different market segments
- **psychological**: customers think they are saving money by charging £9.95 rather than £10
- **market**: setting prices at the current favourite rate to avoid price wars

## Promotion

Another one of the Ps is **promotion**. Businesses promote their products to:

1. introduce new products to the market and increase product awareness
2. increase sales of an existing product
3. compete with competitors’ products on the market
4. co-operate with others (e.g. washing powder manufacturer teaming up with a washing machine company)
5. improve company image

**Advertising** is where a sponsor pays for the non-personal presentation of a message. Because it is non-personal it is aimed at a mass market, not one particular segment.

**Sales promotion** pushes products through activities such as displays, demonstrations and shows and offers incentives such as free samples or price reductions.

**Direct marketing** involves approaching consumers direct to sell products, rather than going through retailers – often mail order and direct mail is used here.

**Personal selling** is providing special individual information and contact which impersonal advertising cannot provide – like email, salesmen and using sales agents.

Advertising media can be **print-based** (i.e. permanent) found in newspapers, periodicals and specialist magazines. It can also be **broadcasted** media, such as radio, TV and cinema advertising. **Outdoor** media is the use of posters and illuminated signs, etc.
The nature of an advert depends on the targeted group; the advertising budget; the type of product and its current place in the product life-cycle. An advertising agency can be hired to produce a marketing campaign for a company, but this is more expensive than a business doing its own marketing.

Examples of types of sales promotion are:

- **point of sale (POS)** promotion – this is where the product is promoted at the place it is being sold (a good example is the JML products that used to be sold in Woolworths)
- **after-sales service** which includes things like a money-back guarantee or warrantee
- **sponsorship** is often used by firms

Direct marketing directly approaches the consumer. There are several forms, including mail order catalogues, from which the consumers choose what they want and place an order; direct mail which are leaflets usually asking for customer response, often considered junk mail; and emails, which are more often than not junk mail also.

The public relations department (PR department) is in charge of organising PR for the business. It may use press releases and image advertising, where the company’s name and image is promoted alongside (or maybe instead of) the product.

### Placement

Place is the final of the Ps. One factor a business needs to decide on is its **channels of distribution**: The producer may sell directly to the consumer (A). Some manufacturers allow their products to be sold in bulk in shops like Costco to the consumers (B), but more often the retailers will buy from the wholesalers so that consumers can purchase from the retailers (C). However, probably the most popular method of distribution is the manufacturer selling direct to the retailer and the consumer purchasing from the retailer (D).
Wholesalers bulk-buy from the manufacturers, which means dealing with one larger order rather than many smaller orders. The producer’s own warehousing costs are reduced if the wholesaler stores the produce, and the wholesaler may even do some of the promotion for the producer. A wholesaler buys large and sells small. This means as it sells onto the retailer, it does so in smaller chunks, or even smaller chunks if to the consumer.

There are several types of retail outlet:

- **independent retailers** are the sole trader businesses, such as local butchers and corner shops in small towns
- **chain stores** (or multiple stores) have a head office and a minimum of ten branches across the country, and can be specialist, such as a single clothes line (e.g. Burton) or can be more generic, such as BHS who sell multiple lines
- **department stores** are usually public limited companies like Debenhams and have various departments and sell a wide range of products
- **discount stores** such as Comet buy in bulk but because they control their costs (like for advertising, etc) carefully, they can afford to give consumers discounted prices
- **retail superstores** such as Tesco
- **franchises** (see page 7)

A business also has to consider where it will locate, and factors affecting this might include raw materials (only applicable to certain businesses in the manufacture industry), the local community and availability of jobs. The concentration of similar businesses in the new area is another factor because the amount of competition will change where a business might wish to locate.
The Importance of Finance to a Business

A business has assets which it needs to make or supply their goods and services. When a business is set up, it has short-term debts which came from buying stock on credit. This short term finance is the business’ working capital. The creditors (suppliers on credit) could take legal action if they don’t pay soon, and even take legal action resulting in the closure of the business and them having to sell off their assets to pay the debts.

The business will need long-term capital to expand. Sources for this finance include personal savings (for sole traders) and shares in limited companies.

Sources of Finance

- **retained profit**: This is profit from sales which is reinvested back into the business
- **selling assets**: If an asset is no longer needed, it can be sold for cash
- **trade credit**: Credit offered to the business by suppliers and have 30 days to pay
- **owner's funds**: Investing your own personal savings into the business
- **borrowing**: Having money lent to you from family members and friends
- **loans/mortgages**: Borrowing large sums of money which are paid back with interest
- **overdrafts**: A limit which you can go over drawing out of the bank for 30 days
- **debt factoring**: Getting a company to chase your debtors up who hold some of it

The most important sources of finance for larger businesses are:

- **shares** – these tell us that the holders own a portion of the company; a public limited company sells its shares as it floats on the stock exchange, whereas private limited companies sell theirs privately
- **debentures** (long-term loans), where the lenders receive interest and will have their loan capital paid back at some time in the future

Whether a source of finance is short-term, medium-term or long-term depends on how long it lasts for, and how quickly the business can receive the finance.

Production Costs

- employee wages
- raw material costs
- transport costs
- light, heat and power
- servicing and repairing equipment
## Types of Cost

A cost can be a **fixed cost** or a **variable cost**. Fixed costs do not change with output – whereas variable costs are flexible, they change as output changes.

<table>
<thead>
<tr>
<th>Fixed Costs</th>
<th>Variable Costs</th>
</tr>
</thead>
<tbody>
<tr>
<td>rent</td>
<td>raw material costs</td>
</tr>
<tr>
<td>office salaries</td>
<td>employee wages</td>
</tr>
</tbody>
</table>

Sometimes it is difficult to distinguish between a fixed cost and a variable cost, it may be a bit of both, so we say that it is a **semi-variable** cost.

A **direct cost** can be linked directly to a particular product line, for example, the cost of raw materials in production and the wages of the production workers. An **indirect cost** (or an **overhead**) is shared amongst the product lines as they do not relate to one specific product. Examples of these include company stationery, salaries, and office and factory rent.

Economies of scale can lower unit cost, and so the **average cost** of production is found by dividing total cost by total output. The **marginal cost** is the cost of making that individual product. For example, take the following business:

<table>
<thead>
<tr>
<th>Total fixed costs are £3000 and variable costs per item are £100</th>
</tr>
</thead>
<tbody>
<tr>
<td>average cost of making one item = £3100 / 1 = £3100</td>
</tr>
<tr>
<td>average cost of making two items = £3200 / 2 = £1600</td>
</tr>
<tr>
<td>average cost of making three items = £3300 / 3 = £1100</td>
</tr>
</tbody>
</table>

The marginal cost of the second and third items is £100 each

## Break-even Analysis

The **break-even point** of a business is where **total costs** equals **total revenue**. This is therefore the point at which the business makes neither a profit nor a loss. Any point after it is where the business makes a **profit**, so break-even is important to any business.

*The Daily Waffle* is a newspaper.

- Each newspaper is sold for 85p
- The variable costs per newspaper is 30p
- The fixed costs are £200,000

We need to calculate the following to work out the break-even:

1. The fixed costs will always be £200,000 as they do not change with output
2. The variable costs will be the number of units produced x 30p
3. The total costs for each number of units is fixed costs + variable costs
4. The total revenue will be the number of units x 85p
We can display the data in a table and then use that information to produce a chart:

<table>
<thead>
<tr>
<th>N° of Units</th>
<th>Variable Costs</th>
<th>Fixed Costs</th>
<th>Total Costs</th>
<th>Total Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>0</td>
<td>£0</td>
<td>£200,000</td>
<td>£200,000</td>
<td>£0</td>
</tr>
<tr>
<td>100,000</td>
<td>£30,000</td>
<td>£200,000</td>
<td>£230,000</td>
<td>£85,000</td>
</tr>
<tr>
<td>200,000</td>
<td>£60,000</td>
<td>£200,000</td>
<td>£260,000</td>
<td>£170,000</td>
</tr>
<tr>
<td>300,000</td>
<td>£90,000</td>
<td>£200,000</td>
<td>£290,000</td>
<td>£255,000</td>
</tr>
<tr>
<td>400,000</td>
<td>£120,000</td>
<td>£200,000</td>
<td>£320,000</td>
<td>£340,000</td>
</tr>
<tr>
<td>500,000</td>
<td>£150,000</td>
<td>£200,000</td>
<td>£350,000</td>
<td>£425,000</td>
</tr>
<tr>
<td>600,000</td>
<td>£180,000</td>
<td>£200,000</td>
<td>£380,000</td>
<td>£510,000</td>
</tr>
</tbody>
</table>

This information can then be plotted onto a graph:

The break-even can also be calculated using a formula. But before we can do that, we need to know the contribution of the product.

\[
\text{contribution} = \text{selling price per unit} - \text{variable costs per unit}
\]

and then breakeven is

\[
\text{breakeven} = \frac{\text{fixed costs}}{\text{contribution}}
\]

So using the same example as before:

\[85p - 30p = 55p\]

\[\£200,000 \div \£0.55 = \£363,636\] which we can round to \£365,000

Notice that this is the same as in the break-even chart.
Budgeting

We use budgets to plan ahead in terms of spending and to control spending. A business budget is a detailed forecast for future plans and actions of the business involving finance. Budgets are followed so that a business can plan for the future, set performance targets and act promptly in the future.

Cash Flow

Cash flow is the movement of money in and out of a business. Whilst there is always money coming in and going out of the business, they are seldom at the same rate. When there is more money coming into the business than coming out, it is a cash surplus; and more money leaving the business than entering is a cash deficit.

Profitability & Liquidity

One reason for keeping financial accounts is to monitor a business’ revenue (income) and expenses, from which profits can be calculated. The amount of profit can be compared with other figures such value of sales made and value of capital invested, to give us an idea of the profitability of the business.

A firm’s liquidity refers to its ability to meet debt payments when they fall due. A company has both current assets (items which can be quickly turned into cash, including cash and stock) and current liabilities (short-term debts, e.g. money owed to creditors). The working capital is the difference between these two figures.

<table>
<thead>
<tr>
<th>Current assets</th>
<th>£000</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Stock</td>
<td>250</td>
<td></td>
</tr>
<tr>
<td>Debtors</td>
<td>490</td>
<td></td>
</tr>
<tr>
<td>Cash in hand</td>
<td>10</td>
<td>750</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Current liabilities</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Creditors</td>
<td>370</td>
</tr>
<tr>
<td>Bank overdraft</td>
<td>30</td>
</tr>
</tbody>
</table>

Working capital: £400 - £350 = £50

Financial Accounts

At the end of each financial year, a business will produce a final set of accounts:

- Its profit and loss account calculates the net profit
- Its balance sheet displays all the assets and liabilities of the business
The profit and loss account contains a section called the **trading account** which is sometimes referred to as its own separate account. Its purpose is to calculate gross profit:

<table>
<thead>
<tr>
<th></th>
<th>£000</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Sales</strong></td>
<td>400</td>
<td></td>
</tr>
<tr>
<td><strong>Less cost of sales:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Opening stock</td>
<td>55</td>
<td></td>
</tr>
<tr>
<td>Purchases</td>
<td>290</td>
<td></td>
</tr>
<tr>
<td><strong>Total cost of sales:</strong></td>
<td>345</td>
<td></td>
</tr>
<tr>
<td>Closing stock</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td><strong>Gross profit</strong></td>
<td>100</td>
<td></td>
</tr>
</tbody>
</table>

This trading account clearly shows that the gross profit is the difference between sales revenue and cost of sales.

\[
gross \text{ profit} = revenue - costs
\]

The purpose of the profit and loss account is to calculate **net profit**, which is the balance after all of the expenses have been deducted from gross profit.

<table>
<thead>
<tr>
<th></th>
<th>£000</th>
<th>£000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gross profit</strong></td>
<td>100</td>
<td></td>
</tr>
<tr>
<td><strong>Less expenses:</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Administration</td>
<td>32</td>
<td></td>
</tr>
<tr>
<td>Selling/Distribution</td>
<td>16</td>
<td></td>
</tr>
<tr>
<td>Financial</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td><strong>Total expenses:</strong></td>
<td>60</td>
<td></td>
</tr>
<tr>
<td><strong>Net profit</strong></td>
<td>40</td>
<td></td>
</tr>
</tbody>
</table>

Taken into account on this document are various administration, selling and distribution expenses (rent and rates, light and heat, etc), as well as **depreciation** and **bad debts** (the cost of selling on credit).

The balance sheet outlines what the business owns (its assets) and what it owes (its liabilities). Payment the business has made for its assets is **capital expenditure**.

Items in the balance sheet appear under the following headings:

- **Fixed assets** – assets which have a long life – these are not bought to be re-sold
- **Current assets** – assets which are temporary and used in trading, owned by the business purely for future profit
- **Current liabilities** – deducted from current assets to give the working capital (known as the **net current assets** figure on this document)
- **Capital** – this shows us the value of the owners’ investment

Capital includes:

- **share capital**, this indicates the total value of the investment made by shareholders
- **reserves**, including undistributed profits being kept in the company to help it expand
- **loan capital**, e.g. debentures, and important long-term source of finance for companies
These reports are all published annually for public limited companies (they have to by law) in their Annual Report and Accounts document. It often contains more information than these two accounts but these are the essential two documents needed to be seen by potential investors and current shareholders in the company.

### Profitability Ratios

<table>
<thead>
<tr>
<th>Name</th>
<th>Calculation</th>
<th>Purpose</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Gross profit margin (%)</strong></td>
<td>$\frac{\text{Gross Profit}}{\text{Turnover}} \times 100$</td>
<td>To show what percentage of every £1 turnover is gross profit</td>
</tr>
<tr>
<td><strong>Net profit margin (%)</strong></td>
<td>$\frac{\text{Net Profit}}{\text{Turnover}} \times 100$</td>
<td>To show what percentage of every £1 turnover is net profit</td>
</tr>
<tr>
<td><strong>Return on capital employed</strong></td>
<td>$\frac{\text{Net Profit}}{\text{Capital Employed}} \times 100$</td>
<td>To show how profitable the owners’ investment is by showing percentage return</td>
</tr>
</tbody>
</table>

If the gross profit margin figure is increasing, the firm receives more gross profit for every £1 in sales. The gross profit margin decreases as the figure decreases, which occurs with an increase in cost of sales or a cut in selling price. Similarly, the net profit margin behaves in the same way.

The return on capital employed (i.e. how many pence net profit out of every £1 capital employed) can be compared to the rate of return the owners would like to receive if they invested elsewhere. This will tell them whether or not it is worthwhile to continue investing in that particular business.
### Liquidity Ratios

<table>
<thead>
<tr>
<th>Name</th>
<th>Calculation</th>
<th>Purpose</th>
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</thead>
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<tr>
<td><strong>Working capital ratio</strong></td>
<td>Current Assets : Current Liabilities</td>
<td>To check the ability of the business to pay its short-term debts back</td>
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<tr>
<td><strong>The acid test</strong></td>
<td>Current Assets - Stock : Current Liabilities</td>
<td>To see whether or not a business can meet its short-term debts without selling any stock</td>
</tr>
</tbody>
</table>

### Asset Efficiency Ratio

We can calculate the **stockturn** (rate of stock turnover) using:

\[
\frac{\text{Cost of Sales}}{\text{Average Stock}}
\]

which gives us the number of times per period that the average stock is sold.
The Role of the European Union

The European Union (EU) was established in 1957 and it does a lot of things:

- The common agricultural policy (CAP) was established to help farmers increase output and diversify – but the EU has been criticised for making butter mountains and wine lakes and other surpluses.
- EU open markets in areas like IT and telecommunications have led to common standards being set, which British-made equipment must meet.
- The Single Market in areas like financial services and transport have made it so that the British now have to compete with other EU countries in the same area.

The euro is the single currency adopted by 11 of the EU current members from 1999, now Greece has joined. Although we still use Great British pounds, the euro affects our businesses in terms of trading, especially those trading in euro zone. The euro makes price differences more obvious throughout the euro zone. It also eliminates the need to change currencies, avoiding exchange rate fluctuations for importers and exporters.

Business Competition Laws

The Office of Fair Trading (OFT) set up the Fair Trading Act in 1973 so that trading could be monitored and restrictive practices controlled. They also set up the Competition Act in 1980 to prevent competition malpractice between businesses.

Consumer Law

There are a number of organisations who aim to protect consumers against business malpractice. Examples include OFTEL, the communications regulator, and OFWAT, which oversees the water industry.

Some of the consumer protection laws are listed below:

- The Sale and Supply of Goods Act 1994 makes sure that all sold goods must be of satisfactory quality and must be fit for the purpose they were bought for; the product must also match its product description legally.
- The Unsolicited Goods and Services Act 1971 prevents businesses from delivering products to consumers who did not order them and demanding that they pay for them; it also means that if something is delivered to you which you did not buy, you may keep it if uncollected within 6 months.
The Trade Descriptions Acts 1968 and 1972 make it a criminal offence to give a false description of goods or services available for purchase.

The Food Safety Act 1990 makes businesses which sell food ensure that food is off satisfactory quality and must be fit for human consumption.

Employee Protection

Should an employee feel that they have been unfairly dismissed, they may apply for an industrial tribunal which will decide if the dismissal was fair or unfair. All employees under contract are automatically protection against unfair dismissal.

Other laws associated with employment include:

- the Working Time Regulation which limits normal working hours to a maximum of 48
- the Parental Leave Directive which gives staff a right to unpaid leave following the birth of their baby
- the Part-Time Work Directive which ensures equal treatment for part-time staff

The Equal Pay Act 1970 forces employers to pay men and women doing the same work equally. Further protection comes from the Sex Discrimination Acts 1975 and 1987 which make it unlawful to advertise a job, employ someone or dismiss someone on the basis of their gender. People who believe they have been discriminated against can approach the Equal Opportunities Commission (EOC) for advice.

The Race Relations Acts 1968 and 1976 make it illegal for an employer to discriminate on the grounds of race, religion, ethnic origin or nationality. If a person believes they have been discriminated against they can approach the Commission for Racial Equality for advice.

The Disability Discrimination Act 1995 makes it unlawful to discriminate against employing a person on the grounds of their disability – unless that specific disability prevents them from doing the job correctly.

The Health and Safety at Work (HASAW) Act 1974 states the duties of both the employee and the employer regarding health and safety at work. The employer must provide safe working conditions, machinery, working processes and emergency exit arrangements. The employee must take appropriate care of themselves and others around them; must not interfere with anything provided to them for their own personal safety; and must co-operate with their employer with anything regarding health and safety matters. A health and safety executive (HSE) can inspect how well this act is implemented in a workplace.

Pressure Groups & Law Organisations

The Advertising Standards Authority (ASA) protects consumers from bad advertising by making sure all advertisements are truthful, decent, honest and informative).
The Consumers’ Association tests goods and services and reports back to consumers in its magazine, Which? with reviews.

Pressure groups such as Amnesty International, Greenpeace, Friends of the Earth and ASH (Action on Smoking and Health) influence business activity as they continue to campaign for new laws supporting their causes.