

1 Business

Check your understanding answers

1.1 The purpose and nature of businesses

Reasons for starting a business

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1. A customer is someone who pays for a product, while a consumer is someone who uses the product. For example, if parents pay for a child to attend a summer school, the parents are the customer, while the child is the consumer.
An entrepreneur is a person who takes a financial risk to start a business, for example James Dyson who invented the bagless vacuum cleaner.
2. A person may start a social enterprise, which is a business designed to help others, rather than to make a large profit. Social enterprises include community shops which are often set up in rural areas with few other shops. Those who set up social enterprises are usually more concerned about others in society than with making large profits.
A person may start their own business because they have many commitments and find it difficult to work regular hours. They may decide to set up a business which can operate with flexible hours so that their work can be fitted around their other commitments, such as caring for children or elderly relatives.
Some people decide to turn their interest, hobby or idea into a business. For example, someone who keeps bees may decide to start a business selling honey and offering lessons to others on how to keep bees.

Factors of production

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Land	Labour	Capital
wheat used by a baker	head chef	delivery van
water from a well	nurse	company website
orchard owned by a cider maker	software programmer	doctor's computer

Types of business and their basic functions

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1. The operations function of a business is concerned with producing the goods or services that the business sells. For example, a housebuilder's operations function would be involved in buying land and building houses on land. A restaurant's operations would focus on preparing and cooking meals for diners.
The marketing function involves a range of activities, from finding out what customers want, to designing suitable products, pricing them correctly and advertising and distributing them to customers. The housebuilder's marketing would involve discovering what features house buyers want in their homes, designing suitable houses in the right locations, setting a price that people can afford and advertising that the company had houses for sale.
2. Nissan's operations involve manufacturing cars using supplies of steel, engines, wheels, rubber and electronics. This is carried out on a production line in a factory and may use robots.

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Check your understanding answers

Nissan's marketing involves researching what features consumers want in their cars – for example, is it important to have electric cars rather than those powered by diesel or petrol? It also involves designing cars to fit customers' needs, pricing them to be affordable and distributing the cars to where consumers want to buy them. Finally, its marketing involves advertising the cars using media such as TV.

Nissan's finance function involves raising large sums of money to meet the costs of designing new cars such as its electric Nissan Leaf. Finance is also important to ensure that Nissan has enough money to pay its suppliers on time and its workers each month. The finance function will aim to ensure that Nissan makes a profit each year from manufacturing cars.

The human resource function ensures that Nissan has enough suitably skilled employees to design, build and sell its cars successfully. This may involve training employees and hiring new ones when people leave.

1.2 Business ownership

Partnership

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1. A sole trader is liable for all of their business's debts – referred to as 'unlimited liability'. This means that if the business incurs large debts the sole trader may have to sell their personal possessions, including their home, to pay the debts. This would be a worry for any sole trader whose business was in danger of failing.
2. Limited liability legally separates a business from its owners. This means that if the business fails, or has very large debts to repay, the owners are not liable for those debts and only stand to lose the money that they have invested. This means that their personal possessions are safe.

Companies

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1. A shareholder is a person or an organisation that owns a part of a company. Each shareholder owns a 'share' – or a part – of the business.
2. Shareholders can bring benefits to a business because they provide money in return for receiving a 'share' of the ownership of the business. This finance can be very important in helping an entrepreneur to start or expand a business. Shareholders may also bring expertise to a company, especially a smaller private limited company.
However, shareholders can cause conflict because they may have different objectives to those managing the business. Some may simply want quick profits and not be so interested in the long-term success of the business.

1.3 Setting business aims and objectives

The role of objectives in running a business

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1. 8%
$$\text{Market share} = \frac{£420,000}{£5,250,000} \times 100 = 8\%$$
2. £17.5 million.
$$\text{Total sales} = \frac{£3,500,000}{20} \times 100 = £17,500,000$$

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1.4 Stakeholders

The objectives of stakeholders

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- + Employees and the business's owners might both benefit from a decision to raise prices as the result might be higher pay and higher profits.
- + A business may decide to expand its operations in a particular location. This could create more jobs for employees and larger orders for the business's suppliers.
- + A business might introduce a wider range of products. Customers would benefit from an increased choice of products and the new productions may offer employees more job opportunities.

The impact and influence of stakeholders on a business

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1.
 - a. An increase in prices could benefit the company's employees who may be able to negotiate a pay rise as the company is receiving 'significantly' more revenue. At the same time, the company's customers will have to pay higher prices and the value for money of their purchases may decline.
 - b. In this situation, the employees are disadvantaged as their incomes will fall. If it results in the partnership making a larger profit (or a smaller loss), then the partners could benefit at the expense of their employees.
 - c. This decision may benefit people in the local community as they would not suffer from so much pollution to their immediate environment. However, if the company increases its prices to cover the higher costs of production, consumers may suffer as a consequence of this decision.
2.
 - a. It is possible that customers have more power in this situation as they could decide to avoid buying the company's products, which would have a major impact on the business.
 - b. It may be that the partners have most power in this situation, especially if the employees are low skilled and replacements are relatively easy to find.
 - c. It would perhaps depend on how important price is to the company's consumers. Consumers do have the power to reduce sales, but the local community could generate bad publicity against polluting methods of production or good publicity for cleaner production methods.

1.5 Business location

Factors influencing location

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1. Cost will be an important factor for this start-up business as it will be unlikely to have large funds available and will want a cheap location. The nature of the business – repairing clothes – means that it is likely to attract only local customers. Locating at the owner's home might be the best option.
2. This manufacturing business needs raw materials – coal and iron ore – that are bulky and expensive to transport. It will need to locate close to these raw materials, close to where they are imported or near main transportation links (e.g. motorways or rail network), to keep its costs as low as possible.
3. This business does not need to locate near to its customers as they purchase online. It may need to be close to its suppliers or to locate in a place with good transport links. A site close to a motorway in the centre of the country might be a good choice.

1 Business

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1.6 Business planning

Financial terms contained in a business plan

Page 25

1. Revenue
2. Variable costs
3. A loss
4. The business makes a profit.

Page 25

1. Revenue = $645 \times £250 = £161,250$
2. Total costs = $£125,000 + £345,000 = £470,000$
3. Revenue = $575 \times £900 = £517,500$
Total costs = $£257,250 + £210,250 = £467,500$
Profit = $£517,500 - £467,500 = £50,000$

1.7 Expanding a business

Unit costs and economies and diseconomies of scale

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1.

Monthly output of product (units)	Total cost of production (£)	Unit cost (£)
500	100,000	200
1,000	150,000	150
1,500	187,500	125
2,000	200,000	100
2,500	300,000	120
3,000	435,000	145
3,500	612,500	175
4,000	900,000	225

2.

- a. The business experiences economies of scale when its monthly production is between 500 items and 2,000 items. Over this range of output its average unit cost falls from £200 to £100.
 - b. As its output rises to 4,000 items a month, its average unit costs rise steadily to £225. This shows that the business is suffering from diseconomies of scale.
3. If the business produces 2,000 items each month its average unit costs are at their lowest: £100. This would allow it to sell its products relatively cheaply, offering customers better value for money.

2 Influences on business

Check your understanding answers

2.1 Technology

E-commerce

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1. A small hotel in Cornwall may be affected by e-commerce in the following ways:
 - + It can use its website to advertise its services to people throughout the UK cheaply.
 - + Its customers may be able to make and amend bookings online.
 - + It may buy some of its supplies online.
2.
 - + A bank may be able to attract more customers from a wider market as its banking services would be available 24 hours a day, 7 days a week. This could increase its market share and make it more profitable in the long term.
 - + A bank may be able to reduce its costs as it may not have to provide so many branches if its customers are using online services. It is expensive to provide and staff high street banks so there is a lot of potential to reduce costs. This is why so many banks in the UK are moving to offer more services online.
3.
 - + A retailer would be able to sell its products to a much wider market by using e-commerce.
 - + It may be able to reduce its running costs, allowing it to offer lower prices.

2.2 Ethical and environmental considerations

Ethical considerations

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- + A retailer may refuse to buy its clothes from overseas suppliers who employ child labour. As children used in factories overseas are paid very low wages, not using children and using adults may result in the retailer paying higher prices for its clothes. Its profits may fall unless it can sell at higher prices.
- + The clothes retailer may pay its employees higher wages than is necessary because it believes this is the correct way to treat its workers. The result will be higher wages and potentially lower profits for the retailer.
- + The retailer may ensure that its products are high quality and free from faults. It may also accept returns without queries. All these factors will increase its costs of production. This could lower its profits if it is not able to sell at higher prices.

Sustainable methods of production

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- + A coffee shop chain may decide to widely publicise its decision to adopt environmentally friendly policies in order to make itself different from its rivals, such as Costa. This may result in the business attracting larger numbers of customers, leading to an increase in sales. As a result, its profits may increase.
- + The coffee shop chain may be able to increase its prices without losing too many customers. Its customers may be loyal because they support its environmentally friendly policies. Higher prices with roughly the same number of customers could lead to increased profits.

2 Influences on business

Check your understanding answers

2.3 The economic climate of business

Interest rates and the economic climate

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1. If there is a large fall in interest rates, many savers might decide to save less or not to save at all. This is because the extra payment (also referred to as the return) from saving is reduced. The decisions of millions of savers could lead to a very large fall in savings with banks and building societies.
2. Many consumers buy jewellery using borrowed money in some way, especially if the jewellery is expensive. A rise in interest rates increases the cost of buying jewellery in this way and the 'extra' payment becomes larger. Some consumers will decide not to buy jewellery and purchases of these products will be likely to fall.
3. This garage may be strongly affected by a rise in interest rates. It will have to pay more interest on its high levels of borrowing and this may reduce its profits. Furthermore, it may experience falling sales as fewer consumers may decide to take out more expensive loans to buy cars from the garage.
4. Falling interest rates will be likely to represent good news for this house building company. Most house buyers need a loan to purchase a house as they are very expensive. Lower interest rates will make loans cheaper, allowing more people to buy houses. The company may enjoy more sales. At the same time, it may pay less interest on money it borrows to buy land and other resources needed to build houses.

Impact on businesses of changes in employment levels

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A large fall in employment levels in the UK could have two main effects:

- + The demand for the fast-food restaurant's products might fall. People who are no longer employed will have reduced incomes. They may not be able to afford to eat out so often at fast-food restaurants, even though these may be relatively cheap. As a result, sales are likely to fall, especially in areas where more jobs have been lost.
- + Fast-food restaurants employ large numbers of employees in their outlets. If the level of employment falls, more workers may be available to take jobs in the restaurants. The restaurant chain may be able to lower its costs by paying lower wages if more people are looking for work.

2.4 Globalisation

Exchange rates

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1. A UK business that exports can benefit from a fall in the exchange rate. The fall in the exchange rate will lead to the business's exports becoming cheaper in the overseas markets. As a result, the business's sales could rise, especially if price is important to customers. It is quite likely that the business's profits will also rise, along with its sales.
2. In contrast, a UK business that imports raw materials and/or components from overseas will pay higher prices for these resources. This will increase the business's costs of production. The outcome is likely to be falling sales and profits if the business is less able to compete with rivals who do not import their resources.
3. Many UK businesses compete against others that are based overseas. With a fall in the exchange rates, the overseas competitors will gain an advantage as their products will have become

2 Influences on business

Check your understanding answers

cheaper. If prices are important to UK customers, UK businesses may lose sales and their profits may decline.

2.5 Legislation

Employment law

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1. False. Those aged over 18, but under 23 are paid according to the National Minimum Wage. Employees aged over 23 are paid a higher rate per hour as set out in the National Living Wage.
2. True.
3. False. Both types of minimum wages apply to all workers, whether full time, part time or temporary, as well as those paid by piece rate (the quantity they produce).
4. False. Reasons include not being able to perform the job to a satisfactory standard or gross misconduct, such as theft from an employer.
5. False. However, employees do have the legal right to join a trade union.
6. True and false. The definition of discrimination is true, but the examples of factors over which discrimination may occur are false. Discrimination can occur in relation to age, gender, religion or belief, marriage and civil partnership, disability, race, sexual orientation, pregnancy or maternity, gender reassignment (employees whose gender has changed since their birth).

Consumer law

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Advantages of legislation		Disadvantages of legislation
Employee legislation	+ Employees may perform better if they are protected by legislation. + If employees' rights are protected and they are given a safe and healthy workplace, they may produce more goods and services. Businesses may receive more revenue from sales as a result.	+ Most legislation adds to the costs of production of a business. Employment law, for example, gives workers nearly six weeks' paid holiday each year. + UK laws may be stricter than those in operation in other countries. For example, other countries may not have minimum wage legislation. This means that UK businesses face costs of production that are higher than those of rivals. In these circumstances it can be difficult to compete with foreign businesses in terms of price.
Consumer legislation	+ Consumers may be more willing to buy goods and services, especially expensive ones, if they are protected by legislation. + Without these laws, the level of sales achieved by businesses might be lower, as would their profits.	+ Consumer law prevents the use of dangerous (but cheap) materials in production. These factors mean that businesses' costs may be higher and profits lower.

2 Influences on business

Check your understanding answers

Health and safety legislation	+ Employees may have fewer days off work as a result of health and safety legislation. + Health and safety laws protect against injury and illnesses such as repetitive strain injury (RSI). + Fewer days off work means the output of the workforce may be higher, generating higher incomes for the business.	+ Investing in health and safety training and purchasing safety equipment will increase the costs to a business.
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2.6 The competitive environment

Markets and competition

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Buying products in markets with many sellers does offer consumers advantages. There are more businesses to choose from and competition in these markets is often fierce. Potentially this offers consumers the benefits of:

- + lower prices than might otherwise be the case
- + a wider choice of products.

For instance, when choosing an Indian restaurant in a city, there is usually a lot of choice and this competition keeps prices down.

In contrast, a market with fewer, larger sellers may give a consumer more developed products as smaller businesses may not have the resources to develop sophisticated and advanced products. For example, mobile phones are technologically advanced as they are manufactured by large businesses that invest heavily in researching and developing new products. Small businesses may not be able to do this.

Whether a consumer benefits most depends on how competitive the two types of markets are. Markets with many small- and medium-sized businesses are usually competitive. This is not always the case in markets with fewer, larger businesses. Some markets, such as petrol retailing and gas supply, have a few large businesses and have been criticised for having little competition and relatively high prices.

Markets and competition

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1.

- + The entrepreneur lacks experience of managing a business.
- + Competitors might lower their prices and increase their advertising when the new business is launched.
- + Consumers will not be aware of the business and its products.

2.

- + The entrepreneur might choose to go into partnership with a more experienced entrepreneur, ask advice from consultants/experts or hire skilled employees.
- + The new business could respond to the risk by planning carefully to provide a product which is significantly different from those already available on the market. If this meets consumers' needs, it will give them a reason to buy the products rather than the now cheaper and extensively advertised rival products.

2 Influences on business

Check your understanding answers

- + The business needs as much positive publicity as possible, and this does not necessarily involve paying for advertising. It could try to obtain free publicity in local newspapers and on local radio stations.

3 Business operations

Check your understanding answers

3.1 The competitive environment

Efficiency in production

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An online bookshop, such as Amazon, will need fewer resources to carry out its production process. For example, it will need one or more warehouses, rather than a series of shops in expensive locations such as in high streets and shopping centres. The business may carry lower levels of stocks of books as it will not need to have large quantities in each of its shops. It may employ fewer people as it will only need warehouse staff. It will not need to employ any shop assistants. All of these factors will help it to reduce its unit cost of production, which may result in it being more efficient.

3.2 The role of procurement

Managing stock

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Stock control method	Advantages	Disadvantages
Just-in-time stock control (JIT)	+ Fewer (or no) stocks held, reducing (or eliminating) storage costs. + Risk of stocks being out of date or stolen is removed. + Businesses unlikely to have unsaleable finished products.	+ Delays to supplies can interrupt production. + Purchasing economies of scale may be unavailable and delivery costs increased. + Business may be unable to respond to an increase in orders.
Just-in-time case control (JIC)	+ Production can continue if deliveries of supplies do not occur. + Business can respond to an unexpected increase in sales. + May benefit from purchasing economies of scale.	+ Costs of holding stock can be considerable. + Stock may become out of date or be stolen. + Finished products held as stock may become unfashionable or out of date.

Factors affecting choice of suppliers

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The furniture manufacturer will be concerned about the following issues when choosing its new supplier:

- + Is the supplier able to deliver quickly? It operates a JIT system of stock control and production. This means that it may need supplies at short notice. Furthermore, its sales can fluctuate significantly and at short notice. It will be vital for the supplier to be able to respond to this, so that the manufacturer does not lose sales.
- + Will the supplier offer competitive prices? The furniture manufacturer sells at 'the lowest possible prices'. As this is to be a major supplier, if its prices are relatively high, this will reduce the manufacturer's ability to offer low prices to its customers.

3 Business operations

Check your understanding answers

3.3 The concept of quality

The consequences of quality problems

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Alba Airlines will have to make sure that it provides the luxury service that it promises and that flights depart promptly and arrive on time to meet the expectations of its customers. The nature of this airline's product makes maintaining consistent quality very important.

Failure to meet standards in these areas could lead to a heavy loss of sales. Its customers will be attracted by the quality on offer and many will leave if this is not provided. The airline may have to reduce its prices, or offer refunds/free flights if quality standards are not met.

Maintaining consistent quality

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TQM involves everyone in the business ensuring that they engage in activities that help to meet quality standards. For example, employees such as drivers who deliver the bus services to the public would check the work of those responsible for keeping the buses in good working condition and therefore reliable. This might mean checking that the fuel and oil levels were sufficient, and that lights and other electrical equipment was in working order. Those who support the drivers, for example mechanics, would be responsible for ensuring the company's vehicles are working efficiently. Those working in the administration departments of the bus company would need to ensure that suppliers are paid on time so that supplies such as fuel and spare parts for the buses are always available. With each employee ensuring they do their job effectively and to agreed standards, as well as checking the quality of other employees' work where possible, the bus company is more likely to offer a consistent and high-quality service.

Everyone in a business using TQM also has responsibility for checking the work of others. In the bus company the drivers would check the work of the mechanics to ensure that the buses are in excellent condition and more likely to be reliable. This idea of checking helps to make it more likely that quality standards will be met.

3.4 Good customer service

Methods of providing good customer service

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1. Businesses selling smart TVs. Many consumers buying these products do not fully understand how they work, for example how to link them to the internet. Consumers are also likely to need information about different brands of smart TVs, the differences between them and which will meet their needs most fully.
2. A customer booking an overseas holiday at a travel agent. Customers are likely to have a wide range of questions about matters such as resorts, transport, accommodation, prices and exchange rates. Customers need to be able to ask questions to establish if the holiday will meet their needs. The travel agent's employees will need good product knowledge to answer questions effectively.
3. Businesses selling new build houses. Houses are expensive and complex products to buy. Buyers will have many questions about the houses to establish whether they should purchase this expensive product. Their questions may centre on the features of the house, how energy efficient and environmentally friendly it is, whether a mortgage is available from the seller and guarantees about the property should repairs be needed in the future.

3 Business operations

Check your understanding answers

Advances in ICT and customer service

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Examples of how a business might provide good customer service without the use of ICT:

- + Ensuring staff are well trained, so that they have good product knowledge.
- + Responding quickly and effectively to customers' complaints.
- + Making sure that customers' needs are fully understood as part of the sales process.
- + Providing suitable premises for customers to use, such as hygienic toilets.
- + Offering refreshments to customers if the purchasing process is likely to be lengthy.

4 Human resources

Check your understanding answers

4.1 Organisational structures

Roles and responsibilities within organisational structures

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1. The average span of control will be four. There are four directors and 16 managers, so each director will be responsible for four managers.
2. This statement is correct. There are 480 shop floor employees and 80 team leaders. By dividing the number of employees by the number of team leaders ($480 \div 80$), each team leader will have a span of control of six. Some may have more, and others fewer, but the average will be six.

Centralisation and decentralisation

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A business may choose to remain centralised in the following situations:

1. A small business where a single manager, or a small group of managers, are able to oversee all the business's activities. In this case, the senior managers would be able to take all important decisions without risk of overworking.
2. A business's employees may not have the necessary skills and knowledge to make important decisions. The business will be likely to operate more efficiently if important decisions are taken by a smaller group of more experienced and knowledgeable managers.
3. The nature of the business. Some businesses are highly creative or highly technological. In these situations, it may be better for highly skilled managers to take the important decisions.

4.2 Recruitment and selection of employees

Methods of recruitment and selection

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1. External recruitment. The employee required must have specialist skills and, as this is a small business, there may not be a suitably skilled candidate within the business. External recruitment should provide much more choice.
2. Internal recruitment. This is a major retailer that is seeking to appoint someone to a relatively junior position. There will probably be a substantial number of existing employees with the right skills and in-depth knowledge of how the retailer operates.
3. Internal recruitment. This business may not be able to afford the costs of external recruitment and may not need to do so as this is a junior appointment.
4. External recruitment. The business is growing rapidly and so is likely to need additional employees. This is also an appointment to manage the production of a new product, so existing employees may not have the right skills.

Contracts of employment

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Type of contract	Benefits to employers	Benefits to employees
Full-time	✚ The employee is at work for the standard working week. This means that customers and other employees find it easy to contact the employee.	✚ The employee receives pay for a full working week. This provides a higher standard of living. ✚ A full-time employee may find it easier to gain

4 Human resources

Check your understanding answers

	+ Employees can develop more skills and experience from full-time work and have a clearer understanding of work-related matters.	promotion. They may have more experience of the business and more relevant skills.
Part-time	+ Part-time employees can help businesses to satisfy customers during busy periods. This avoids the need to pay full-time employees who may not be needed at all times. + Part-time employees may provide specialist skills that are only needed at particular times. For example, a business might only need an IT expert one day each week.	+ Employees can fit work alongside other commitments such as caring for children or elderly relatives. + Some workers choose to move gently towards retirement by reducing their working hours over a period of time. This allows them to earn an income for longer and can boost their pension.
Zero-hours	+ Some businesses such as delivery services may not be sure how much demand there will be for their services from week to week. Zero-hours contracts allow them to manage staff to match fluctuations in demand. + It helps businesses to control their costs of production. Zero-hours contracts means that people are only employed (and paid) when they are really needed.	+ Some employees want to fit work around other commitments such as studying. A zero-hours contract enables them to choose whether or not to work the hours offered. + It can offer an important way to gain some experience of working without having to commit to regular hours.

4.3 Motivating employees

The importance of motivating the workforce

Page 74

Higher levels of motivation should result in employees achieving higher levels of productivity. This increase in output per worker per time period should lead to lower labour costs for each unit of output that is produced. The business then has two choices:

- + It could reduce prices and sell more products for the same profit per unit.
- + It could leave prices unchanged and make more profit on each product sold.

Both these factors will increase the business's profits.

Improved levels of motivation may also result in higher levels of staff retention and therefore fewer employees leaving. The business will avoid the need to spend money recruiting and training new employees. Profits could be higher as a consequence.

4 Human resources

Check your understanding answers

Methods to motivate employees

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Advantages of using only financial methods to improve motivation	Disadvantages of using only financial methods to improve motivation
+ Techniques such as linking pay to levels of output such as commission and piecework can be offered to encourage employees. + It can be very effective as many employees are motivated by money. + Techniques such as profit sharing encourage employees to take actions to increase the business's profits.	+ It can be expensive for the business – especially if it doesn't improve motivation levels and productivity. It may reduce profits. + Some employees may not be motivated by money – it may be less successful for some employees in a hospital, for example, or for those who work for a charity or school.

4.4 Training

Types of training

Page 78

A business operating in a high technology industry where changes take place very quickly may need to ensure its workforce are fully trained as soon as possible. The employees may need training in new technological developments and existing employees may not have the skills and knowledge to provide this. It may be necessary to go to an external training provider which has suitably skilled training staff and the appropriate technology to train the employees fully.

A business might be growing quickly and recruiting a large number of new employees. It may want to train its new employees but may not have any suitably skilled employees available to do the training as they are likely to be involved in production. In this case, off-the-job training may be the answer.

How businesses choose the most appropriate methods of training

Page 78

1. Off-the-job training. This is likely to be a long-term period of training and will require employees to take external examinations. This type of training would be better provided externally, possibly in a local college.
2. On-the-job training. This is a relatively simple, but business-specific type of training. It is probably best provided internally, possibly by other employees.

5 Marketing

Check your understanding answers

5.1 Identifying and understanding customers

Importance of identifying and satisfying customer needs

Page 79

1. Products where having sufficient information is vital include buying a house, an overseas holiday (especially if several destinations are involved), health insurance, a mobile telephone service and dental treatment.
2. The following are examples of products in which after-sales service will be important to customers: domestic appliances such as a washing machine, dishwasher and fridge, central heating boiler, an extension to a house, a new car or a caravan, hair extensions.

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1. A business that provides holidays overseas may attract fewer customers than in the past if it does not understand the new destinations and types of holidays that its customers want. If its customers' tastes have changed from beach holidays in Europe to activity holidays in destinations around the world, for example, the travel company must change its products. If it does not do so it will lose sales to rivals who have adapted to meet customers' needs by changing their products.
2. If some customers of a retailer selling basic foods have suffered a fall in their incomes, the price of basic foods will become very important to these customers. If the retailer's rivals are more price competitive it may lose a significant number of customers and its sales may fall as a consequence.

5.2 Segmentation

How markets are segmented

Page 82

1.
 - a. The restaurant chain would probably segment its products according to the location of its customers. Customers in different parts of the world would expect different menus in the restaurants. For example, in India many customers will not eat beef as the cow is a sacred animal. Therefore, the restaurants in India would have menus that do not include beef products.
 - b. The restaurants may also segment according to local tastes. For example, foods that are popular in a particular country or considered a 'national dish' may be included on the menu in that particular country, but not be available in restaurants in other parts of the world.
2.
 - a. The magazine publisher is likely to segment its market based on gender. Magazines covering beauty and fashion will have mainly female readerships, while titles such as Men's Health, will be targeted at men.
 - b. A magazine publisher will also segment according to age (children's comics, teen magazines) and interest (gardening, cooking, aviation, football, etc.).
3.
 - a. A jeweller might segment its market according to location and income. Its shops in areas where people have higher incomes might stock more expensive jewellery and make products to order. In lower-income areas the stock of jewellery might be less extensive and may be sold at lower prices.
 - b. [To come]

5.3 The purpose and methods of market research

Using market research

5 Marketing

Check your understanding answers

Page 86

1. Market size = $1,500,000 \times £2.50 = £3,750,000$.
2. Market size = $480,000 \times £700 = £336,000,000$.

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1. Market share = $\frac{£1,350,000}{£1,500,000} \times 100 = 90\%$
2. Market share = $\frac{£355,000}{£23,500,000} \times 100 = 1.51\%$

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1. $24,950,000 - 23,700,000 = 1,250,000$
Market growth = $\frac{£1,250,000}{£23,700,000} \times 100 = 5.27\%$
2. $£300,000 - £295,000 = £5,000$
Market growth = $\frac{£5,000}{£295,000} \times 100 = 1.70\%$

5.4 Elements in the marketing mix

Factors that influence the choice of pricing method

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1. Loss leader. This retailer sells many products and needs to attract more customers to its shops. Offering one of its products at very low prices (and advertising this widely) will help to attract more customers into the shops again. This may increase sales of this product as well as other products on which it makes a profit.
2. Penetration pricing. This is a new activity for an existing business which is profitable from its other activities. It should therefore be able to afford to set low prices and risk earning little or no profit, at least for a while, while it builds up its market share. The success of this strategy will depend on how important price is to the target customers.
3. Price skimming. This approach is suitable when a business has a differentiated product, as in this case of the mobile phone with new features. Setting prices high, at least initially, will increase profits and help to pay for the investment in developing the product. Prices can be reduced once competitors launch equivalent products.
4. Competitive pricing. This business may want to avoid strong price competition with equally large – and financially powerful – rivals. Setting a price similar to the ones already on offer should avoid this and allow some profit to be made.

Promotion

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1. The fast-food restaurant might offer free samples or two-for-one offers (such as buy one meal, get one free). This would help to attract local people to the restaurant and could be advertised in local media, such as newspapers and radio. It may also attract free coverage in local newspapers.
2. The clothing manufacturer could engage in a substantial advertising campaign, possibly on national television and in national newspapers. As it is profitable it will be able to afford the cost of producing adverts. As the business wishes to target the whole of the UK (as its sales are falling throughout the country), national TV and newspaper advertising would provide the best way of ensuring all areas of the country are covered.

5 Marketing

Check your understanding answers

3. This business will have to spend money on advertising if it is to compete with the existing businesses and attract customers away from them. It may have to spend a lot of money on advertising, especially if the existing businesses increase their advertising in response to the arrival of the new business.
4. This business should use local media (newspapers, radio or billboards) to reach the customers in this local market. As these people represent the target market for this business, locally based promotion is appropriate.

6 Finance

Check your understanding answers

6.1 Sources of finance

Internal sources of finance

Page 100

1. This business is profitable which means that it should have retained profits available. It is also a sole trader business which means if the owner takes this decision, there are no other owners who may object to the profits being used in this way.
2. Trade credit may be the best option for this business. It only needs the finance for a short period of time so this would suit the use of trade credit which is only available for a limited period. The business buys a lot of raw materials from a major supplier. This supplier may give it trade credit as it is an important customer.
3. A sale of assets might be the most obvious approach here. Some of the retailer's shops are suffering a major decline in sales. It could sell these stores to raise some finance. It could also use sale and leaseback for those shops it wished to continue trading and use the finance raised from the sale of the least profitable shops to finance its investment in online selling. Both of these actions would avoid the interest charges associated with borrowing finance.

Influences on the choice of sources of finance

Page 102

Factors influencing a new business's choice of finance	Factors influencing an existing business's choice of finance	Factors affecting both types of business choice of finance
+ Funds available to an entrepreneur's friends and family	+ Business's profitability + Assets owned by the business + Business's past history	+ Type of business + Risk associated with the business + Amount of finance needed

6.2 Cash flow

Importance of cash flow to businesses

Page 103

1. A cash inflow.
2. A cash outflow.
3. A cash inflow and a cash outflow.

Interpreting cash flow forecasts

Page 104

1. The closing balance was (£1,239) – the same as the opening balance for January.
2. Net cash flow = £3,750 – £3,849 = (£99)
3. The opening balance would not change. It would remain at £1,988 as this was the closing balance for February. The closing balance would be £3,243.
4. Closing balance = (£1,112) + £644 = (£468)

Solutions to cash flow problems

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6 Finance

Check your understanding answers

1. An overdraft. Although this solution can be costly, it is appropriate in this instance as the shortage of cash is expected to be a short-term, one-off event. Long-term and more permanent solutions such as a bank loan are not required.
2. This business could seek to reschedule its payments. As it is so profitable it could afford to lose any discounts for prompt payment and simply pay later.
3. The business should increase its cash inflows. It could do this by increasing its prices as customers buy its products for reasons other than price. Raising prices will not reduce sales and, as customers pay immediately, the business's cash inflows will rise.

6.3 Financial terms and calculations

Basic financial terms and calculations

Page 108

1. Revenue = $(45,000 \times £3) = £135,000$
Total costs = £125,000
Profit = £10,000
2. Revenue = $(5,000 \times £33) = £165,000$
Total costs = $£95,000 + £75,000 = £170,000$
Loss = £5 000
3. Revenue = $(10,000 \times £80) = £800,000$
Total costs = $£250,000 + (10,000 \times £50) = £750,000$
Profit = £50,000

Components of financial statements

Page 112

Gross profit = £19.8 million – £13.4 million = £6.4 million

Net profit = £6.4 million – £3.1 million = £3.3 million

Calculating gross and net profit margins

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Last year:

$$\text{Gross profit margin} = \frac{£165,000,000}{£660,000,000} \times 100 = 25\%$$

$$\text{Net profit margin} = \frac{£79,200,000}{£660,000,000} \times 100 = 12\%$$

The year before last:

$$\text{Gross profit margin} = \frac{£196,000,000}{£700,000,000} \times 100 = 28\%$$

$$\text{Net profit margin} = \frac{£98,000,000}{£700,000,000} \times 100 = 14\%$$

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1. The managers may have been unhappy with last year's results simply because the company recorded lower figures for both its gross and net profit margins than in the previous year. A

6 Finance

Check your understanding answers

further cause of dissatisfaction could be that the company's revenue from its sales had fallen by £40 million, or 5.71%. However, their final judgment may depend on how rivals in the same industry had performed. If their competitors' revenue figures and profit margins had fallen more sharply, then the business's managers may have been satisfied to some extent.

2. They would certainly need to know the equivalent figures for the business's closest competitors. This would help them to judge whether the cause of the decline was linked to changes in the market rather than their management of the company. The managers may also want to see data for years prior to the year before last. That might have been an exceptional year and difficult to reproduce.