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UPDATED TO 2020-22 SYLLABUS

CAIE A2 LEVEL
BUSINESS (9609)

SUMMARIZED NOTES ON THE THEORY SYLLABUS

1. Business Structure

1.1. Local, National and International businesses

- Local businesses operate in a small part of the country. They do not have expansion objectives
- National businesses have branches throughout the country but they do not operate in other countries
- International/multinational businesses operate in more than one country

1.2. International Trade

Businesses

Pros	Cons
Economies of scale	Diseconomies of scale
Access to better information	Higher transport costs
Spreads risks	Higher competition and risk
Access to wider market	Trade barriers
	Cultural and language differences
	Using agents increases prices
	Supply chain issues

Country

Pros	Cons
Improved political and social links	Loss of output and jobs
Higher GDP, employment and living standards	Decline in domestic industries due to increased imports
	High competition making it difficult for new businesses
	Increased chances of dumping
	If value of imports exceeds exports, there's loss of foreign exchange
	Overdependence on other countries

1.3. Protectionism

- Process of protecting domestic firms from foreign competition with the use of trade barriers
- Tariffs – tax on imports
- Quotas – limit on the quantity of imports
- Embargoes – ban of particular imports
- Voluntary export restrictions – an export country agreeing to limit the quantity of exports sold to another country

1.4. Free trade and Globalisation

- Free trade is when countries face no trade barriers while exchanging goods and services
- Globalisation is the increase in movement of labour, capital and goods and services between countries
- Trade blocs and trade organisations help encourage globalisation
- World trade organisation (WTO) – countries committed to reduce trade restrictions
- Free-trade blocs – groups of countries who trade without restrictions. Ex. NAFTA, ASEAN, EU

Benefits of free trade

- Wider choice of goods and services
- Wider choice of raw materials
- Helps developing countries increase the rate of industrialisation
- Low prices, improved quality
- Encourages specialisation
- Economies of scale
- Improved living standards

1.5. Multinational businesses

- A business which produces in many countries

Why become a multinational?

- Avoid tariffs
- Access to cheaper raw materials
- Lower labour costs
- Lower transport costs
- Closer to the market
- Better control
- Access to grants and subsidies
- Economies of scale
- Cheaper rent and site costs

Problems for multinationals

- Cultural differences
- Legal regulations
- Coordination & communication problems
- Diseconomies of scale
- Differences in skill levels of employees, increasing training costs

1.6. Host Country

Benefits	Drawbacks

Benefits	Drawbacks
Economic growth	May not reinvest profits in the country
Higher employment	Exploitation of labour
Higher tax revenue	Exploitation of natural resources
Better infrastructure	Pollution
Better skills for workers (if invest in training)	Drive out domestic firms
Increased quality	Reduction in cultural identity
Increased business opportunities	

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1.7. Privatisation

- It is the process of selling state-owned enterprises to the private sector
- Benefits –
  - Improved efficiency
  - Higher revenue for the government
  - Higher tax revenue
  - Higher quality
  - Higher competition
  - Minimal government influence
  - Wider choice
  - Higher investment
- Drawbacks –
  - External costs may not be considered
  - Monopolies may be formed
  - Exploitation of customers – higher prices
  - Strategic industries require government support and control
  - Reduce opportunities of economies of scale

2. Size of Business

2.1. External growth

- Business expansion done through mergers and takeovers
- Also known as integration

Reasons for –

- Share research facilities and pool ideas
- Economies of scale
- Save on marketing and distribution costs
- Larger customer base
- Higher market share

Reasons against –

- Diseconomies of scale
- Conflicts

2.2. Synergy and integration

- Synergy means that the whole is greater than sum of parts
- The new, larger business will be more successful than the two, formerly separate, businesses

2.3. Types of integration

1. Horizontal integration
   1. Integration in the same industry and stage of production
   2. Economies of scale
   3. Lower competition
   4. More power over suppliers
   5. Scope for rationalisation
   6. Monopoly, increased investigation
   7. Conflicts
2. Vertical forward integration –
   1. Integration in the same industry but forward stage of production
   2. Control over promotion
   3. A secure outlet for the firm's products
   4. Lack of experience and expertise
   5. Uncompetitive behaviour, bad publicity
3. Vertical backward integration –
   1. Integration in the same industry but a backward stage of production
   2. Control over quality, price and delivery time
   3. Increased research & development
   4. Control over competitors supplies
   5. Lack experience and expertise
   6. Business may become complacent
4. Conglomerate integration –
   1. Integration in a different industry
   2. Diversifies risks
   3. Share ideas
   4. Lack of experience, failure
   5. Lack of clear focus and direction

2.4. Joint ventures and strategic alliances

- Joint venture is when two businesses come together to work on one project, sharing capital investment
- Strategic alliances are agreements between firms in which each agrees to commit resources to achieve an agreed set of objectives

2.5. Problems of rapid growth

- Financial
  - Expensive
  - Addition fixed and working capital is needed
  - Increased long-term borrowing and lead to negative cash flow

    - Use internal sources of finance
    - Raise finance through issue of shares
    - During takeovers, offer shares rather than cash
- Managerial
    - Management unable to cope with controlling large operations
    - Lack of coordination and communication
    - Original owner may find it difficult to be a leader and manager
    - Adapt a new management system and structure
    - Decentralise
- Marketing
    - Original marketing strategy may not be appropriate
    - Adopt focused strategies for each product, in each country
    - Conduct market research
- Loss of control of original owners
    - Occurs if sole trade/partnership turns public/private
    - Original owners can try to remain as directors

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3. External influences on business activity

3.1. The impact of the government and law on business activity

- Legal constraints on business activity
    - Laws on employment practices, working conditions
    - Laws on marketing and consumer rights
    - Laws on business competition
    - Laws on location of business
- The law and employment practices
    - Prevent exploitation of workers (minimum wage, working conditions)
    - Control use of trade union action
- Recruitment, employment contracts and termination of employment
    - A written contract of employment must be signed by the employee and employer
    - Minimum wages, working conditions, working hours are controlled
    - Laws against unfair dismissal
    - Unfair dismissal:
        - Pregnancy
        - Refusal to work overtime
        - Joining trade union
        - Incorrect dismissal procedure
- Health and safety laws
    - Aim to protect workers from injury and discomfort at work
    - Equip factories with safety equipment
    - Provide adequate facilities
    - Provide protection & training from dangerous machines
    - Give adequate breaks

3.2. Evaluating the impact on business on employment and health and safety laws

- Increase costs
    - Supervisory cots
    - Higher wage costs
    - Higher costs from giving holidays
    - Increased number of workers
    - Protective clothing & equipment
- Benefits
    - Workers feel more secure, increasing motivation
    - Reduce the risk of accidents
    - Avoid court cases
    - Ability to attract highly-skilled workers
    - Good brand image

3.3. The law, consumer rights and marketing behaviour

- Reasons to protect consumers:
    - Influential advertising is making it difficult for consumers to make rational decisions
    - Protects becoming more scientific and technological, difficult to understand
    - More pressurised selling techniques
    - Increased globalisation
- Laws for consumer protection:
    - Sale of goods act
        - Goods should be fit to sell
        - Suitable for the purpose
        - Perform in the way described
    - Trade descriptions act
        - No misleading descriptions or claims
    - Consumer protection act
        - Firms providing dangerous or defective products are liable for the cost of any damage
        - Illegal to quote misleading prices

3.4. Evaluating the impact of consumer protection laws on business

- Business costs rise – redesigning ads, improving quality control
- Require a change of strategy and culture
- Reduces chances of legal action
- Improved brand image
- Increased sales and profits
- Better brand loyalty

3.5. The law and business competition

- Benefits of free and fair competition to consumers:
  - Wider choice
  - Lower prices
  - Improve quality, design and performance of the product
  - International competition will help strength domestic economy
- Laws on competition:
  - Investigate and control monopolies
  - Limit uncompetitive practices

3.6. Monopolies

- There is only one supplier with 100% market share

How do monopolies develop?

- Invention of new products
- Mergers and acquisitions
- Legal protection
- Existence of barriers to entry

How are consumers affected by monopolies?

- Benefits:
  - Lower prices
  - Increased expenditure on R&D
- Drawbacks:
  - Higher prices
  - Limited choice
  - Less investment due to complacency
  - Lower efficiency

3.7. Uncompetitive or restrictive practices

1. Refusal to supply a retailer if they don't agree to charge the prices determined by the manufacturer
2. Full-line forcing – manufacturer forces retailer to stick the whole range of products
3. Market sharing agreements and price fixing agreements
4. Predatory pricing – firms charge low prices to block out other firms in the industry

3.8. Social audits

- A report on the impact a business has on the society – stakeholders, environment, community
- Benefits:
  - Identifies the social responsibilities met by a business
  - Sets targets for improvement
  - Improves company image
  - Increases sales
- Drawbacks:
  - Expensive
  - Time taking
  - Consumers main aim is high quality goods
  - May be window dressed

3.9. The impact of technology on business activity

Technology – what does it mean?

- Technology means the use of tools, machines and science in an industrial context
- High-technology machines and processes that are based on information technology (IT)
- They are opening new product markets and making businesses more flexible
- Business applications of technology:
  - Word processing
  - Pagemaker and publishing programmes
  - Databases
  - CAD
  - CAM
  - Internet
- Benefits:
  - Accurate
  - Fewer administrative staff
  - Easier and quicker communication
  - Lower costs
  - Flexible
  - Increased productivity & efficiency
  - Add to a firm's competitive advantage
  - Wider target market

3.10. Applying technology to business – limitations

- Increased capital costs
- Training costs
- Redundancy costs
- Reduced job security
- Fall in motivation
- Breakdowns can halt production
- Legal constrains on the use of IT
- Managers fear change

3.11. IT and business decision-making

- Provision of huge amount of data to management through the use of IT is known as management information systems
- Obtain data quickly
- Easy to process and analyse data
- Quick decision making
- Better communication
- Information overloads can lead to information lost
- Power can be abused
- Reduction in authority and empowerment
- Reduce job enrichment and motivation

3.12. Introducing technology effectively

- Analyse – the use of IT
- Involve – managers and other staff
- Evaluate – different systems and programs (cost, efficiency, budget)
- Plan – introduction of new system, training
- Monitor – introduction and effectiveness of the system

3.13. Social and demographic influences on business activity

- An ageing population
  - A larger part of the population is over retirement age
  - Smaller proportion is in lower age range
  - Businesses will have to adapt their goods and services to cater to
  - older people
  - Older population means lesser people in the workforce, increasing demand for workers, increasing wages
  - More training may be required
  - Businesses will have to be more aware of their employees retiring since they are of an older age
  - Since there are more dependents, cheaper products may be more popular
- Changing role of women
- Better education facilities
- Early retirement
- Job insecurity

Patterns of employment

- Transfer of labour from secondary to tertiary sector
- Increase in temporary and flexible employment contracts
- Increase in part time employment
- Increasing pressure on pensions and healthcare services due to an ageing population
- Increase in student employment (on a part-time basis)
- Capital is replacing labour
- Women returning back from maternity leave
- Increase in number of women staying full time
- Part time workers increase flexibility and lower fixed costs
- But it becomes difficult to manage and encourage team work
- Employing more women gives businesses a wider choice of staff and improved motivation amongst workers
- Gives access to higher quality and more qualified workforce
- But costs increase when they take maternity leaves
- Businesses which are able to quickly adapt to changing environments are able to survive successfully
- Having a younger workforce:
  - cheaper
  - more flexible
  - geographically mobile
  - innovative
  - technologically skilled
  - keep changing jobs frequently
  - require greater training
- Having an older workforce:
  - more loyal
  - greater experience
  - hard-working
  - demand higher wages
  - reluctant to change

3.14. Environmental constraints on business activity

The environment and corporate social responsibility

- when a firm accepts it legal and moral obligations to stakeholders other than investors, it is said to be accepting corporate social responsibility

Arguments for and against adopting environmentally friendly business strategies

- For:
  - Marketing and promotional advantage
  - Better brand reputation
  - Avoid pressure group activity
  - Avoid legal problems and court fees
  - Access to skilled employees
  - Long-term financial benefits
- Against:
  - Higher costs, increased prices, lost sales
  - Loss of competitive advantage
  - Reduced profits, limiting expansion
  - Not too strict laws regarding environment
  - Economic development > environment – developing countries

3.15. Environmental audits

- Assessing the impact of a business activities on the environment
- Difficult to measure in monetary terms
- No legal requirements
- Better publicity
- Higher sales
- Better skilled workers

Social audits

- Pollution
- Health and Safety
- Supply Sourcing
- Customer Satisfaction
- Social Contribution

- Accounting and Financial Transparency
- Diversity
- Annual targets to improve social responsibility

Evaluation of environmental and social audits

- Expensive
- Time consuming
- Companies accused of using it as a PR activity
- No general rule and compulsion on these policies

3.16. Environmental and ethical issues – the role of pressure groups

- A pressure group is an organization created by people with a common interest or aim who put pressure on businesses and governments to change policies so that an objective that seeks to influence elected officials to take action or make a change on a specific issue.

How do pressure groups affect businesses?

- The primary goal of a pressure group is to influence some aspect of the way a business operates, including which types of products businesses manufacture.
- Pressure groups can exert influence by finding allies in the media, by organizing protest marches, and by running marketing campaigns to express their concerns.

How do they operate?

- Encourage government to change rules and laws
- Encourage businesses to change policies
- Encourage consumers to change purchasing habits

How they achieve their goals?

1. Publicity through media coverage
2. Influencing consumer behaviour
3. Lobbying of government

4. External Economic influences on business activity

4.1. Economic objectives of governments

- Economic growth
- Low price inflation
- Low rate of unemployment
- Exchange rate stability
- Long-term balance of payments
- Wealth and income transfers to reduce inequalities

There may be conflicts whilst the government is trying to fulfil these objectives, so the government will have to prioritise
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4.2. Economic growth

- Measured using GDP
- It is measured in monetary terms
- Inflation will increase the value of GDP, which is not true economic growth
- Economic growth occurs as a result of a rise in the real GDP of a country
- Negative economic growth (or recession) occurs when GDP falls
- Benefits of economic growth:
  - Increase in average living standards
  - Higher employment and consumer incomes
  - Reduction in absolute poverty
  - More resources available for the government
  - Rising demand

Factors leading to economic growth

- Increases in output resulting from technological changes and expansion of industry capital
- Increases in economic resources, such as a higher working population or discovery of new resources
- Increases in productivity

4.3. The business cycle

- Economies grow at different rates over time
- Boom –
  - Very fast economic growth
  - Rising income and profits
  - Rising inflation
  - Shortages of skilled labour, higher wage rates
  - Increased interest rates
- Recession –
  - Falling demand
  - Real GDP growth slows down
  - House and asset prices fall
  - Incomes reduce
  - Profits fall
- Slump –
  - A serious and prolonged recession
  - Real GDP falls substantially
  - House and asset prices fall
- Recovery and growth –
  - Real GDP begins to rise
  - Rate of inflation falls
  - Products become more competitive
  - Rising demand

4.4. Is a recession always bad?

- During a recession, output falls, unemployment rises, incomes and demand fall.
- Government revenues fall
- Demand for normal and income elastic goods reduces
- Advantages of recession:
- Capital assets become cheaper
- Demand for inferior goods rises
- Risk of job losses may improve relations

Type of producer	Period of economic growth	Period of recession
Producers of luxury goods and services – e.g. cars	■ increase the range of goods and services ■ raise prices to increase profit margins ■ promote exclusivity and style ■ increase output	■ may not reduce prices for fear of damaging long-term image ■ credit terms to improve affordability ■ offer promotions ■ widen product range with lower-priced models
Producers of normal goods and services – e.g. tinned food	■ add extra value to product – better ingredients/improved packaging ■ brand image may attract exclusive tag ■ do nothing – sales not much affected anyway	■ lower prices ■ promotions ■ do nothing – sales not much affected anyway
Producers of inferior goods and services – e.g. very cheap clothing	■ attempt to move product upmarket ■ add extra value to the product – e.g. higher quality ■ extend the product range to include more exclusive or better-designed products	■ promote good value and low prices ■ free consumer tests ■ increase range of distribution outlets

4.5. Inflation

- Increase in the average price of goods and services
- Fall in the value of money

How to measure inflation

- Measured using CPI (consumer price index)
- It records average changes in goods used by consumers
- Compared with previous months prices
- Weights are added to these price changes
- Then they are averaged and given an index number

Causes of inflation

- Cost push inflation –
  - Depreciation of the currency
  - Rising wage rates
  - Rising raw material costs
- Demand pull inflation –
  - Higher consumer demand

Cause of inflation	Government and central bank policy	Impact on business strategy of government policy aiming to control inflation
Cost–push	■ High exchange rate policy – this could be assisted by higher interest rates set by the central bank. ■ Discourage high wage settlements – may use public sector workers as an example.	■ The high exchange rate will make exports less competitive. Businesses could switch to concentrating on the domestic market. ■ High interest rates will discourage business borrowing and investment. Businesses may cancel investment projects. ■ Consumer credit will also be discouraged, reducing demand, especially for expensive goods. ■ Businesses are unlikely to be influenced by government views on wage settlements – they will pay what is needed to attract and keep staff, as long as the business remains profitable.
Demand–pull	■ Policies designed to reduce aggregate demand such as higher tax rates and lower government spending. ■ Central bank is likely to raise interest rates.	■ Higher taxes will reduce consumer demand. If progressive taxes are increased, there could be a swing away from luxury goods. Businesses may change their product mix to offer less-expensive goods. ■ Lower government spending could hit certain industries very hard, e.g. defence equipment suppliers or hospital equipment manufacturers. These firms may attempt to enter foreign markets. ■ Interest rate increases – these will have same effects as above.

4.6. The impact of inflation on business strategy

- Benefits:
  - Increase costs can be passed to consumers
  - Fall in the real value of debt
  - Increase in value of fixed assets
  - Increased profit margin as inventory is bought in advance
- Drawbacks:
  - Higher wage demands
  - Consumers become more price sensitive
  - Higher rate of interest
  - Cash flow problems
  - Uncertainty
  - Unreliable forecasts
  - Lose competitiveness overseas
  - Reduce chances of receiving discounts and credit periods from suppliers

Business strategies during inflation

- Reduce investment
- Lower profit margin
- Lower debts and borrowing
- Reduce credit period given to customers
- Reduce labour costs

4.7. Deflation

- Fall in the average price of goods and services
- Rise in the value of money

Is deflation beneficial?

- Consumers delay purchases
- Discourage borrowing
- Firms unwilling to invest
- Stocked up inventory reduces in value

4.8. Unemployment

- Members of the working force who are willing and able to work, but cannot find a job

Causes of unemployment

- Cyclical unemployment
  - This occurs during the recession stage
  - During recession, demand falls, encouraging businesses to make employees redundant
  - Using anti-inflationary policies may lead to cyclical unemployment
  - If currency appreciates, demand for domestic goods will fall, leading to cyclical unemployment
- Structural unemployment
  - Exists during rapid growth
  - It occurs due to structural changes in an economy, changing the demand for labour
  - Causes of structural changes:
    - Change in consumer tastes and preferences
    - Increased use of technology, reducing the need to employ workers

- Deindustrialisation
- Increased need for multi-skilled workers
- Provide education and training to workers to avoid structural unemployment

- Frictional unemployment
  - Unemployment when a worker loses their job and are trying to find a new one
  - May lead to cyclical unemployment
  - Provide information about job opportunities, open job centres and recruitment agencies, reduce unemployment benefits, etc to reduce frictional unemployment

Costs of unemployment

- Social problems – crime
- Loss of income and living standards
- Inefficient economy, can produce much more
- Tax revenue used to support unemployed, opportunity cost
- Reduces demand
- Skills may become outdated

4.9. Balance of payments (current account)

- Records the value of goods and services traded between one country and the rest of the world
- Deficit – imports > exports
- Problems of a BOP deficit –
  - Depreciation of the exchange rate
  - Decline in currency reserves
  - Reduced Foreign direct investment (FDI)

4.10. Exchange rates

- The price of one currency in terms of another
- Exchange rates are determined through the forces of demand and supply

Exchange rate fluctuations

- Demand is greater than supply – appreciation – rise in the value
- Supply is greater than demand – depreciation – fall in the value

Appreciation of the currency

- Cheaper raw materials, increased competitiveness
- Reduce inflation
- Cheaper imports may substitute domestic goods
- Higher competition

Depreciation of the currency

- Cheaper in international markets, increased competitiveness
- Lesser price competition in domestic market
- Higher cost of imported raw materials

International competitiveness – non price factors

- Product design and innovation
- Quality of construction and reliability
- Effective promotion and extensive distribution
- After-sales service
- Investment in trained staff and modern technology

4.11. Macro-economic policies

- They impact the entire economy
- Influence the level of AD and AS

Fiscal policy

- Decisions regarding govt expenditure and tax rates
- Revenue > expenditure = surplus
- Revenue < expenditure = deficit
- During a recession, a government will either raise government spending or lower tax rates, so that AD rises, increasing output and employment
- During a period of economic boom, a government will either lower government spending or raise tax rates so that AD falls, lowering inflation, output and employment

4.12. Monetary policy

- Decisions regarding interest rates, money supply and exchange rate of a country
- Recession, lower interest rates, increase AD
- Higher interest rates will increase costs of production for businesses, lower demand and appreciate the country's exchange rate

Type of policy	Measures to slow down economic growth and reduce inflation	Likely impact on businesses
Fiscal policy Decisions about government spending, taxes and borrowing.	Raise direct tax rates.	As consumers' disposable incomes fall, the demand for products will fall. The precise impact will depend on income elasticities (see below). If corporation tax rates are increased, then businesses' retained earnings will decline. This will reduce funds available for business investment.
	Raise indirect tax rates.	The retail prices of the goods affected will increase. The impact on demand will depend on price elasticities.
	Reduce government spending. The combined effect of these measures will reduce government borrowing.	Businesses providing goods and services directly to the government will risk experiencing a reduction in demand. Defence suppliers and construction companies could be hit, for example.
Monetary policy Decisions about interest rates and the supply of money.	The most likely policy measure will be an increase in interest rates.	The impact of higher rates will be: ■ Highly geared businesses will experience increases in interest payments that may endanger their cash flows. ■ Businesses will be less likely to borrow to finance further investment as the costs of loans may exceed the expected returns. ■ Consumers will be affected in two ways: ❑ They will be less likely to buy goods on credit as the interest charges will be higher. This will hit demand for expensive consumer goods, such as cars and household durable goods. ❑ The demand for houses will fall as mortgages are the biggest loan most consumers take out. The interest on existing consumer debts, such as mortgages, will take a higher proportion of incomes. This reduces consumers' discretionary incomes and will impact on consumer demand. The precise effect will depend on income elasticities. ■ Higher domestic interest rates may encourage overseas capital to flow into the country. This will be likely to lead to an appreciation of the currency exchange rate. This will have implications for the competitiveness of businesses.

Monetary policy and the exchange rate

- Higher interest rates will lead to appreciation of a country's currency
- Reasons:
  - Speculation

4.13. Exchange rate policy

- Drawbacks of floating exchange rate & benefits of joining a common currency
  - Fluctuating prices of imported raw materials
  - Unstable demand levels
  - Uncertainty
  - Difficult to make cost comparison as there is no price transparency
  - Increased costs
- Advantages of not joining a common currency
  - Central bank can maintain its status as the interest setting authority
  - Joining a common currency will reduce the independence of each government to control their own tax rates
  - Interest rates can be used to achieve other objectives, rather than focusing on exchange rates
  - Joining a common currency, conversion costs will be high

4.14. Government policies and business competitiveness

- Supply side policies are ones that aim to increase industrial competitiveness
- These include:
  - Lower rates of income tax – encourage workers to earn more as they don't have to pay a higher % in taxes
  - Lower rates of corporation tax – lower tax will increase profits, increasing funds for investment, increasing efficiency and competitiveness
  - Increasing labour market flexibility and labour productivity –
    - Subsidize training programmes
    - Increased funding for higher-education
    - Lower rates of income tax
    - Encouraging immigration of skilled workers
    - Restricting welfare benefits

4.15. Government intervention in industry

- Subsidies to lower prices
- Subsidies to help loss making businesses
- Grants to open up in particular locations
- Financial supports for consumers

4.16. Market failure

- Market failure occurs when there is inefficiency in the market and some goods are overproduced (demerit goods) or under consumed (merit goods)
- Private costs and benefits are borne by the people directly involved in production and consumption
- External costs and benefits are borne by third parties

Examples of market failure	Stakeholder groups most affected	Corrective policy action
External costs – pollution from manufacturing process	■ Consumers – as there may be few alternatives, they may be forced to buy environmentally damaging goods. ■ Government and local authorities, which will be forced to take the issue seriously by voters and pressure groups. ■ Workers, who may be concerned about their own health and job security if bad publicity leads to a decline in sales.	■ Business may take action to reduce externalities if bad publicity leads to lasting damage to reputation and sales. ■ Government can impose fines on polluting businesses or impose strict limits on pollution levels.
Labour training – inadequate provision for training skilled staff	■ Consumers – scarcity of qualified staff may reduce consumer service or lead to higher prices as output is restricted. ■ Government – lack of skilled staff will limit the international competitiveness of industry. ■ Shareholders – potential profits will be lost as output will be below potential.	■ Industry-wide organisations, such as the Engineering Employers Federation, could levy members to pay for industry-wide training, which would benefit all firms in the industry. ■ Government could pay for more training courses at colleges funded from general taxation.
Monopoly producers – restrict output of goods to keep prices high	■ Consumers, who will be concerned about lack of choice, restricted supplies and high prices. There may be a reluctance by monopolies to develop new goods as there is limited competition. ■ Government – high prices and lack of competitiveness of important industries.	■ Consumers who, where at all possible, can purchase from other suppliers. The increasing use of the internet for consumer goods is allowing consumers to choose from a wider range of suppliers and this will break down some monopoly situations. ■ Government can use competition policies. Government can also investigate and act against monopoly practices. Privatisation has led to the break-up of many state-run monopolies.

4.17. Income elasticity of demand

- A numerical measure of responsiveness of demand to a change in income
- YED = % change in demand/ % change in income
- Normal goods – it is positive, between 0 to 1. It means as consumers income increases, demand for these goods rises, by a small proportion
- Luxury goods – it is positive, greater than 1. It means as consumers income increases, demand for these goods rises by a greater proportion
- Inferior goods – YED is negative. Demand for these goods falls as income rises

5. Further Human Resource Management

5.1. HR department

- Deciding employment contracts
- Improving employee performance
- Managing industrial relations

Hard HRM

- It focuses on cost cutting
- Treats workers as machines
- Focuses on short term contracts
- Includes autocratic leadership and has a tall hierarchy

Soft HRM

- It focuses on developing workers
- Ensures they are motivated and reach self-fulfilment
- Treats workers are the most important business resource
- Includes democratic leadership and a flat organisational structure

5.2. Core VS Peripheral Workers

- Groups of workers are divided into core and peripheral
- All full time and permanent employees are considered a part of the core workforce and Soft HRM is used for them
- Temporary, part-time and flexi-time workers are considered a part of the peripheral and Hard HRM is used for them
- This occurs because core workers are considered key for business success, and they should be highly trained and motivation
- The hard HRM used helps save money but only in the short run
- Drawbacks of hard HRM on peripheral workers:
  - Higher recruitment and training costs
  - Demotivated workers (lower job security)
  - Lower productivity and efficiency, higher accidents
  - Bad publicity

5.3. Employment contracts

1. Part time contracts – working for less than 40 hours a week
2. Temporary contracts – contracts that last for a fixed time period
3. Permanent contracts – there contract ends only when the work is dismissed, made redundant or leaves on their own accord
4. Flexi time contracts – allows employees to be called when most convenient to employers
5. Outsourcing contracts – using an outside agency to carry out a particular business function. Helps reduce overhead costs
6. Zero-hour contracts – workers have no minimum working hours and are called in and paid for whenever needed

5.4. Part time and flexi time contract

- Advantages to the business
  - Work only when needed, reducing overhead costs
  - Give competitive advantage due to good customer service
  - More staff available to cover up during absenteeism
  - Ability to assess employee efficiency
  - Using teleworking and reducing overheads
  - Zero-hour contract – lower costs
- Advantages to the workers:
  - Gives greater variety
  - Ideal for workers willing to pursue other hobbies
- Disadvantages to the business:
  - More employees to manage
  - Effective communication becomes difficult
  - Greater reliance on written communication
  - Poor motivation – less involved and committed
  - Difficult to establish teamwork culture
- Disadvantages to the workers:
  - Earning lesser than full time workers
  - Maybe paid a lower rate
  - Reduced security
  - Poor working conditions

Temporary contracts

- Reduces overhead costs
- Lower job security
- Negative effect on motivation
- Employee flexibility

5.5. The Shamrock Organisation

- Core managerial and technical staff – full time permanent contracts, competitive salaries and benefits
- Outsourced functions
- Flexible workers – part time, temporary contracts

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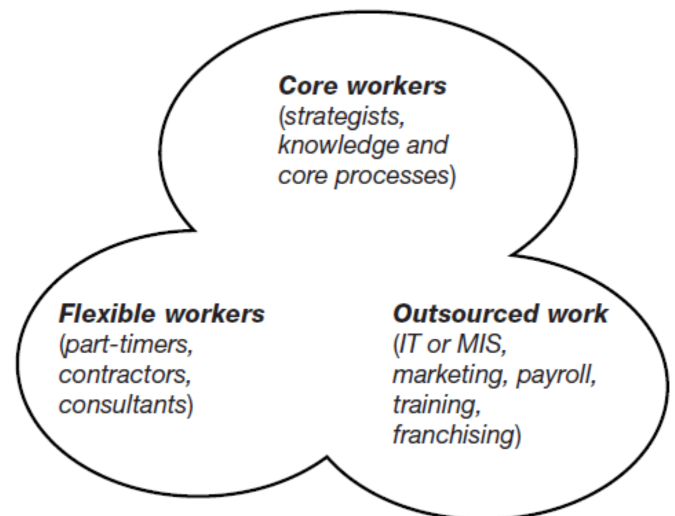

Figure 13.2 Charles Handy's 'Shamrock organisation'

5.6. Measuring and monitoring employee performance

1. Labour productivity
   1. Output per worker
   2. Total output/total workers
   3. Higher labour productivity, higher efficiency
   4. Lower labour costs
   5. Influences business competitiveness

6. Ways to improve labour productivity:
    1. Higher motivation
    2. More efficient
    3. Reliable capital equipment
    4. Increased worker involvement
    5. More training
    6. Improved internal efficiency
2. Reject rates
3. Customer complaints
4. Wastage levels

5.7. Absenteeism rates

- Number of employees absent/total employees * 100
- Lead to poor customer service
- Higher costs
- Indicate poor motivation levels

5.8. Employee performance – strategies to improve it

- Regular appraisal of performance against predefined targets
- Training
- Quality circles
- Cell production
- Financial incentives
- Advanced technology
- Management by objectives

5.9. Management by objectives (MBO)

- Involves breaking down the main corporate aim into departmental and individual targets to motivate workers
- Effective way to delegate authority
- Used during theory Y approach
- Use of annual appraisals
- Benefits:
  - Motivate workers
  - Everyone is aware about what to do
  - Higher productivity
  - Avoid conflict and remain consistent as everyone is working towards the same goal
- Drawbacks:
  - Time consuming
  - Objectives become outdated quickly
  - Does not guarantee success

5.10. Workforce and management – scope for conflict and cooperation

- Depends on culture, legal structure etc

Cause of conflict	Common management view	Common employee view
Business change, e.g. relocation or new technology	Change is necessary to remain competitive and profitable.	Change can lead to job losses, may result in retraining in new skills that causes uncertainty over ability to cope. Demands for increased flexibility from staff may reduce job security.
Rationalisation and organisational change	Business needs to cut overheads and be flexible and adaptable to deal with globalised low-cost competition.	Cost cuts and rationalisation always seem to fall on employees – not the senior managers or owners of the business. Reduced job security will damage employee motivation.

5.11. Approaches to labour-management relations

- Hard or autocratic management
  - Take it or leave it approach
  - Short term contracts
  - Easy to replace them
  - Low labour costs
  - No security, low motivation
  - No training
  - No common objectives
  - Non existent job enrichment and staff involvement
- Collective bargaining between trade unions and major employers and their associations
  - Collective bargaining is when unions negotiation wage levels and working conditions for a large section of the industry
  - Very powerful
  - May threaten strikes
  - Not always suitable and affordable by small companies
  - Causes disruption and loss of output
  - Resist change – lack of investment and development
- Cooperation between labour and management
  - Involve workers in decision making
  - Lower conflicts and strikes
  - Active participation – long term success
  - More competitive and productive workforce

5.12. Workforce planning

- Analysing and forecasting the number of workers and skills the business will require in the future to meet its objectives
- Workforce audit is a check on the skills and qualities of existing employees
- Helps the business plan for future
- Remain flexible

Factors affecting number of employees needed:

1. Forecast demand for the firm's product
2. Staff productivity levels
3. Business objectives
4. Changes in laws
5. Labour turnover and absenteeism rates

Factors affecting skills of workers needed:

1. Pace of technological change
2. Need for flexible and multiskilled workers

5.13. Trade unions and their role in HRM

- Trade union is an organisation whose main objective is to improve pay and working conditions for their members
- Reasons to join a trade union:
  - Power through solidarity (collective bargaining)
  - Collective bargaining > individual industrial action
  - Provide legal support
  - Puts pressure to meet legal requirements

Union recognition and collective bargaining

- Trade unions are not legally recognised everywhere
- Easier to negotiate with workers individually as pressure through collective bargaining isn't present
- However, trade unions save time as negotiations are quicker
- Avoid jealousy amongst workers
- Provide additional communication channels
- Impose discipline on members

5.14. Single-union agreement

- All workers of one organisation will be a part of the same trade union
- Easier to use collective bargaining
- May not represent skilled workers

No-strike agreements

- Improves brand image
- Used in exchange for greater involvement in decision making

5.15. Employees/trade union and employers – what action can they take?

1. Trade union
   1. Negotiations
   2. Go slow
   3. Work to rule
   4. Overtime bans
   5. Strike action
2. Employers
   1. Negotiations
   2. Public relations
   3. Threat of redundancies
   4. Changes in contract
   5. Closure
   6. Lock-outs

5.16. Evaluation

Union/employee power will be strong when:	Employer power will be strong when:
most workers belong to one union all workers agree to take the industrial action decided on the business is very busy, operating close to full capacity, does not want to disappoint customers and profits are high industrial action quickly costs the employer large amounts of lost output/revenue/profits there is public support for the union case, e.g. for very low-paid workers inflation is high, so a high wage increase would seem reasonable to maintain living standards labour costs are a low proportion of total costs	unemployment is high – few alternative jobs for workers to take action taken by employer, e.g. lock-out, has a very quick impact on workers' wages there is public support for employer, e.g. when unions are asking for much higher rises than other workers receive profits are low and threats of closure are taken seriously threats of relocation to low-cost countries are taken seriously, e.g. the business has already closed other plants and relocated them

6. Organisational structure

- It is the internal, formal framework of a business that shows the way in which management is organised and linked together and how authority is passed through the organisation
- It indicates:
  - Overall decision-making responsibility
  - Formal relationships between people and departments
  - The way accountability and authority is passed – chain of command
  - Span of control
  - Formal channels of communication

6.2. Types of organisational structure

Hierarchical structure –

- It is one where there are different layers of the organisation with fewer and fewer people on each higher level
- Advantages –
  - Everyone knows their spot on the corporate ladder
  - Chances of promotion
  - Clear and well-defined role for each individual
  - Clear chain of command
- Disadvantages –
  - Only one way communication
  - Lack of coordination
  - Inflexible
  - Change resistance

Matrix structure –

- An organisational structure that creates project teams that cut across traditional functional departments
- Task & project focused
- Organisations require flexible structure (remove bureaucracy)
- Innovative and creative ideas
- Advantages –
  - Better communication and coordination
  - More innovative and successful ideas
  - Flexible
  - Quicker in responding to market changes
- Disadvantages –
  - Less direct control

    - Conflict of interest

6.3. Key principles of organisational structures

Levels of hierarchy

- Each level represents a grade
- A flat organisational structure has fewer ranks and levels of hierarchy
- A tall organisational structure has many ranks
- Problems –
    - Communication problems
    - Narrow span of control
    - No sense of belonging

Chain of command

- Route through with authority is passed down in an organisation
- Includes instructions and information
- Tall organisational structure – longer chain of command
- Flat organisational structure – shorter chain of command

Span of control

- Number of subordinates reporting directly to a manager
- Wide span of control – many subordinations, encourages delegation
- Narrow span of control – few subordinations, discourages delegation

Delegation

- Passing authority down the organisational structure
- Encourages motivation
- Wider span of control, more delegation
- Employees are accountable for the work, but the manager is still responsible for it
- Benefits –
    - Senior managers can focus on other important roles
    - Indicates trust in workers (motivation)
    - Trains workers for promotions
    - Help achieve self-actualisation
- Drawbacks –
    - Unsuccessful delegation if training is not given
    - Unsuccessful delegation if enough authority is not given
    - Managers may only delegate boring tasks, demotivating them

6.4. Key principles of organisational structures

Centralisation

- It involves keeping all important decision making powers in the head office
- Minimum delegation
- Gives a sense of uniformity and consistency
- Quicker decision making
- Prevents conflicts
- Decisions are taken with the effect on the entire business in mind, not just one division
- Central buying – economies of scale
- Experienced decision makers

Decentralisation

- It involves passing decision making down the organisational structure to empower employees
- Demonstrates trust in employees (motivation)
- Enables localisation as they are closer to the target market
- Develops and prepares them for more challenging tasks (internal promotions)
- Better motivation (delegation & empowerment)
- Quicker and more flexible decisions

6.5. Organisational structures – factors influencing it

- Entrepreneurial structure
- Organisational structure changes with size and range of activities.
- It must be flexible
- Factors:
    - Style of management, culture of managers
    - Retrenchment cause by economic recession or increased competition
    - Corporate objectives
    - Adopting new technologies

6.6. Important links between organisational principles

- The greater the number of levels of hierarchy, the longer the chain of command
    - Smaller span of control
    - Increased delegation
    - Ineffective communication
    - Poor motivation of junior staff
    - Higher business costs
- Problems associated with a tall structure – is delayering the answer?
    - Delayering – remove a whole layer of management
- Delegation: conflicts that can arise and potential benefits
    - Indicates trust on the subordinate
    - Increased motivation
    - Empowerment & self-enrichment
    - Managers may not wish to take risks
- Accountability, authority and responsibility

- Delegation gives subordinates authority to perform tasks
  - If done incorrectly, the worker is accountable for the task
  - However, the overall responsibility of the task is to the manager
- Centralisation and decentralisation
- Line and staff relationships
  - Line managers are workers who have direct authority over people, decisions and resources within the hierarchy
  - Line managers have responsibility for achieving specific business objectives
  - Staff managers are specialists who provide support, information and assistance to line managers
  - They do not have authority over line managers
  - They perform a supporting role to the line managers, but do not make decisions

6.7. Informal organisations

- The network of personal and social relations developed between people over time in an organisation is known as informal organisation
- Power and influence are obtained from membership of informal groups within a business
- Conduct of individuals within these groups is governed by norms or normal standards of behaviour
- It may be that informal group leader may gain more power over the formal group leader

6.8. Organisational structure – the future

- Businesses will need to have a flexible and fluid organisational structure
- Move from command structure to team-based problem solving
- Involves removing horizontal boundaries between departments
- Future success depends on the ability to respond rapidly to the changing business environment

7. Business Communication

7.1. Effective communication

- The exchange of information and instructions between groups or people, with feedback.
- Fey features –
  - Sender
  - Clear message
  - Appropriate medium
  - Receiver
  - Feedback
- Internal communication is between different people or groups within the organisation
- External communication is when the communication occurs with outside parties – suppliers, government, customers, suppliers

7.2. Why is effective communication important?

- Higher staff motivation, labour productivity
- Improve in the number and quality of ideas generated by the staff
- Speeder decision making
- Quicker response to market changes
- Reduced risks of errors
- Effective coordination between departments

7.3. Communication methods – the media used in communicating

Oral communication

- One-on-one conversations, interviews, meetings
- Allows two-way communication and feedback
- Improves worker motivation
- Message can be reinforced with body language
- Maybe ambiguous
- No written record
- Costly, time taking

Written communication

- Letters, memos, notices
- Can be referred to whenever needed
- Allows detailed data to be shared
- No immediate feedback

IT and web-based media

- Emails, fax
- Quick
- Written record
- Need workers to be trained
- Reduces social contact, interpersonal contact is lost
- Security issues
- Information overload

Visual communication

- Accompany oral or written
- Diagrams, pictures, whiteboards
- Increased impact, colour and movements
- Useful during training, marketing

7.4. Communication methods – the media used in communicating

Method	Strengths	Weaknesses
Oral	■ direct ■ can be varied to suit needs of receiver ■ easy to understand ■ can be questioned quickly	■ need to listen carefully ■ affected by noise ■ passive ■ no permanent accurate record ■ can be quickly forgotten
Written	■ recorded – permanent record ■ more structured ■ easy to distribute ■ cannot be varied ■ can be referred to again	■ often difficult to read ■ message identical to each receiver ■ no body language ■ feedback slower ■ no immediate response ■ may be misinterpreted ■ costly and time-consuming
Visual	■ more interactive ■ demands attention ■ often easier to remember ■ creates greater interest	■ needs close attention ■ sometimes too fast ■ not always clear ■ interpretations by receivers can vary
IT/web based	■ great speed ■ interactive ■ messages can be sent to many people ■ encourages response ■ overcomes global boundaries ■ good image for external communication	■ cannot always be received, e.g. poor Internet access ■ relies on receiver responding and acknowledging ■ expensive in hardware ■ risk of communication overload, e.g. excessive emails ■ security issues ■ diminishes interpersonal contact

7.5. Factors influencing choice of appropriate media

- Importance of written record
- Cost
- Advantages to be gained from staff input
- Speed
- Quantity of data to be communicated
- Whether or not more than 1 method id necessary
- Size and geographical spread

7.6. Barriers to effective communication

Failure in one of the stages of the communication process

- Inappropriate medium
- Receiver forgot a part of the long message
- Misleading or incomplete message
- Excessive use of technical language, jargon
- Too much information
- Long communication channel

Poor attitudes of either the send or the receiver

- Sender is not trusted
- Unmotivated workers
- Intermediaries
- Poor opinion or perception

Physical reasons

- Noisy factories
- Geographical distance

7.7. Reducing communication barriers

1. Message is clear and precise
2. Short communication channel
3. Clear channels of communication
4. Build in feedback to the communication process
5. Establish trust between receiver and sender
6. Appropriate physical conditions

7.8. Formal communication networks

- The official communication channels and routes used in the organisations
- Chain network –
  - Used in a hierarchical structure
  - Autocratic leadership
  - One way communication
  - Workers feel isolated, demotivated
- Vertical network –
  - Leader communicates with subordinates directly
  - No group networks
  - Narrow span of control
- Wheel network –
  - Leader is at the centre
  - 2 way communication
  - Poor horizontal communication
- Circle network –
  - One person only communicates with 2 other people
  - Decentralised network
  - No obvious leader
  - Slow rate of communication
  - No feedback
- Integrated network –
  - Full 2 way communication
  - Participative style of decision making

	Centralised networks	Decentralised networks
Speed of learning new procedure	FAST	SLOW
Speed of solution with simple problems	FAST	SLOW
Speed of solution with complex problems	SLOW	FAST
Originality of ideas, e.g. brainstorming	LOW	HIGH
Number of messages sent	FEW	MANY
Satisfaction/morale	LOW	HIGH

Figure 15.7 Effectiveness of communication networks

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7.9. One-way or two-way communication

- One way communication doesn't allow for feedback
- Doesn't give the receiver a chance to question the sender
- No assurance for the sender that the message has been received, understood
- Two way communication allows feedback
- Gives a chance for the receiver to contribute
- More motivating
- Used for democratic leadership
- Time consuming

Motivation → effective communication

Well-motivated staff → more likely to listen and respond positively to messages → better and more accurate communication.

Effective communication → motivation

Effective communication → staff are more likely to feel involved and will receive constant feedback → shorter communication channels reduce remoteness from the 'top' → leads to better motivated staff.

7.10. Horizontal communication

- Vertical communications is when different people from different levels of hierarchy communicate with each other
- Main method is formal
- Horizontal communication occurs along the organisational structure.
- People of the same status but different responsibility
- Problems –
    - Different departments may not understand the culture, objectives, way of working
    - Outlook and objectives of departments may conflict

7.11. Informal communication

- Unofficial channels of communication

Some managers want to reduce informal communication as much as possible:	Some managers think informal communication serves useful purposes:
■ It wastes valuable working time. ■ It spreads gossip and rumours and these can be unsettling and lead to feelings of insecurity. ■ It may result in informal groups banding together to resist management decisions – even though they may not have been officially communicated yet.	■ All informal communication can help create important feelings of belonging and social cohesion. ■ Management can use the grapevine to 'test out' new ideas and see what the unofficial reaction might be – if it is too negative, they might never make an official announcement. ■ Can help to clarify official messages by talking them over with friends.

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8. Marketing Planning

8.1. Marketing Plan

- A detailed fully researched written report on the marketing objectives and the marketing strategy to be used to achieve them
- It includes:
- Purpose and plan
- Mission of the business
- Situational analysis
- Marketing objectives, strategies, tactics
- Marketing budget
- Executive summary & time frame

8.2. Purpose and mission

- Is it a new business proposal or a launch of a new product from an existing business?
- Detailed background history about the business
- Mission and vision statement

8.3. Situational analysis

- Answer the question – where are we now?
- Time-consuming
- Needs extensive, detailed market research and quantitative data
- Without situational analysis, inappropriate objectives, strategies maybe set
- Includes:
    - Current product analysis
    - Target market analysis
    - Competitor analysis
    - PEST analysis
        - Political, Economical, Social, Technological
    - SWOT analysis
        - Strengths, Weaknesses, Opportunities, Threats

8.4. Marketing objectives

- These are targets for the marketing department which form a key part of the plan
- They must be SMART
- Can be expressed in terms of total sales/units/market share/growth rate
- These objectives can be broken down for more specific targets
- They must be clear and measurable

- They give a sense of direction

8.5. Marketing strategies

- This includes information about how the marketing department aims to achieve their objectives
- Includes:
  - Mass or niche marketing
  - New marketing or existing ones
  - High market penetration or limited penetration
- Strategy depends on:
  - Company's mission and objectives
  - Situational analysis
  - Business resources

8.6. Marketing tactics

- Product – a brief summary of the existing products and planned changes and activities. Key features, USP, branding, packaging and labelling details
- Price – depends on cost, PED, competitors price, market conditions, objectives & strategies
- Place – details of channels used, range and number of outlets and how they are liked to the market segment
- Promotion – advertising, sales promotion, public relations & personal selling. The image created depends on the other 3P's

8.7. Marketing budget

- How much money is required to put the marketing strategy and tactic into effect
- Expected sales performance helps comparison between expenditure and expected sales
- It lays out the spending requirements to meet the overall objectives, with a clear month-by-month timetable for every activity

8.8. Executive summary and timescale

Reviewing the plan – the marketing strategy

- The results of the marketing plan must be collected and checked against original objective
- It is an ongoing process
- If objectives are being met, consumer reaction analysis must be done
- If not, the strategy must be changed
- At the end, overall progress must be identified

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Marketing planning – evaluation

- Used to convince potential investors
- However, marketing plan is just one key aspect of a business plan, needs to be backed up by others
- Marketing plans reduce the risk of failure during new product development and entering a new market
- Planning is essential, allows SMART objectives to be set
- Provide direction and purpose
- However, they must be made with integration of all departments

Potential limitations

- Complex
- Costly
- Time consuming
- Dynamic market – quickly outdated
- However, risk of not planning > cost of planning
- Inflexibility

8.9. Elasticity

- Demand of a product is influenced by:
  - Price
  - Consumer incomes
  - Promotional spending
  - Price of related goods

Income elasticity of demand

- A numerical measure of responsiveness of demand to a change in income
- % change in demand/% change in income
- Inferior goods – negative YED, income rises, demand falls
- Normal goods – positive YED (<1), income rises, demand rises
- Luxury goods, positive YED (>1), income rises, demand rises

Promotional elasticity of demand

- A numerical measure of responsiveness of demand to a change in amount spent on promotional
- % change in demand/ % change in promotion spending
- 1, elastic AED, good to increase spending
- <1, inelastic AED, shouldn't increase spending

Cross elasticity of demand

- Numerical measure of responsiveness of demand of good A following a change in price of good B
- % change in demand of A/ % change in price of B
- Substitutes – positive XED, fall in price of B, fall in demand of A
- Complements – negative XED, rise in price of B, fall in demand of A

8.10. Elasticity - evaluation

- Other factors may affect sales, making AED unreliable
- Economic conditions affect sales
- Competitors actions
- Elasticity is calculated based on old data, not entirely reliable to predict future

8.11. New product development

- A new product to succeed it must:
- Have desirable features
- Have a USP
- Be marketed effectively

8.12. Stages of new product development

1. Generating new ideas
    1. Sources of ideas:
        1. Company's R&D
        2. Adaption of competitors ideas
        3. Market research
        4. Employees
        5. Sales people
        6. Group brainstorming
2. Idea screening
    1. Eliminate ideas which stand the least chance of being commercially successful
    2. Make sure the idea has a reasonable chance to succeed before moving forward
3. Concept development and testing
    1. Ask key questions about the features of the product, cost to make, who are its target market, how much will consumers pay, etc
4. Business analysis
    1. Consider the likely impact of the new product on costs, sales and profits
    2. Set an estimated price for the product
    3. Identify the estimated sales volume and market share, break-even point
5. Product testing
    1. Involves checking the technical performance of the product
    2. Whether or not customer expectations will be met
    3. Develop a prototype
    4. Test in typical conditions
    5. Use focus group opinions
    6. Adapt the product from results
6. Test marketing
    1. Small market must be a representative of a larger market
    2. Actual consumer behaviour can be observed
    3. Consumer feedback can be taken
    4. Reduce the risk associated
    5. Identify any weaknesses
    6. Maybe expensive
    7. Competitors can identify a firm's intentions and create a copy
7. Commercialisation
    1. Full scale launch of the product
    2. Introduction stage of the PLC
    3. Filled up distribution channels
    4. Crucial time in the PLC

8.13. Research and development

- It is the scientific research and technical development of new products and processes

Significance of R&D and possible business strategies

- It allows businesses to survive and grow
- Having a USP gives them a chance to charge premium prices
- It is a risky investment
- No accuracy
- No R&D strategy – copy other businesses
- Offensive R&D strategy is to lead the rest of the industry with innovative products. Aims to gain market share & monopoly power
- Defensive R&D strategy is to learn from initial innovators mistakes and weaknesses. Aims to improve original products

Government encouragement for research & development

- Provide legal security by allowing them to patent/register
- Provide financial assistance

8.14. Factors that influence the level of R&D expenditure by a business

- Nature of industry
- R&D plans of competitors
- Business expectations
- Risk profile/culture of the business
- Government policies towards R&D

R&D – evaluation

- New ideas fail due to design defects/manufacturing errors
- Products may fail due to:
  - Inadequate market research
  - Poor marketing mix
  - Changes in technology
  - Competitor's product is more suited
- Firms still continue as they take the long term view
- Long run benefits > short run costs

8.15. Sales forecasting – potential benefits

- Reduced risks
- Production department is aware of the number of units required
- Marketing department is aware of the number of units to be distributed
- Accurate workforce planning
- Accurate cash flow forecasts and planning
- Forecasts maybe be completely accurate due to the dynamic business environment
- Based on market research – primary and secondary
- Existing products – ask expert opinion/use past sales to forecast future

8.16. Sales-force composite

- Add individual predictions of future sales of all sales representatives in the business
- Sales force representativeness are required to keep close contact with consumers – retails, wholesalers
- Allows them to understand market trends and estimate future demand
- Quick
- Cheap
- Ignores macro-economic changes/developments
- Sales maybe overestimated

8.17. Delphi method

- Long range of qualitative forecasting which obtains forecasts from a panel of experts
- They are anonymous
- Facilitator collects and coordinates with experts
- Several questionnaires round maybe done
- Delphi method increases chances of accuracy

8.18. Consumer surveys

- Questions maybe quantitative or qualitative
- Better accuracy – sample must be large, represent the target market
- Time-taking
- Can use an agency, expensive but accurate

8.19. Jury of experts

- It uses senior managers who meet and develop forecast based on their knowledge and experience
- Cheaper
- Quicker
- Lacks external viewpoint

8.20. Quantitative sales forecasting methods

Correlation – establishing causal relationships

- Relations between sales and other factors maybe identified and used to make predictions
- Establishing correlation doesn't indicate cause or effect
- Doesn't consider other factors of change

Time-series analysis

- Based on sales data

Extrapolation

- Basing future predictions on past results
- Results plotted on a time-series graph, extending the line to identify future trends
- Assumes sales patterns are stable
- Not accurate
- Doesn't consider other factors

8.21. Moving averages

- Helps identify the underlying factors which are expected to influence sales:
  - Trend
  - Seasonal fluctuations
  - Cyclical fluctuations
  - Random fluctuations

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1	2	3	4	5	6	7	8
Year	Quarter	Sales revenue	Four-quarter moving total	Eight-quarter moving total	Quarterly moving average (Trend)	Seasonal variation	Average seasonal variation
2011	1	120					
	2	140					
	3	190			146.25	43.75	51.67
	4	130	580		150.00	−20	−15.4
2012	1	130	590	1170 ÷ 8	156.25	−26.25	−33.3
	2	160	610	1200 ÷ 8	163.75	−3.75	−4.6
	3	220	640	1250	167.5	52.5	51.67
	4	160	670	1310	168.75	−8.75	−15.4
2013	1	130	670	1340	172.5	−42.5	−33.3
	2	170	680	1350	176.25	−6.25	−4.6
	3	240	700	1380	181.25	58.75	51.67
	4	170	710	1410	187.5	−17.5	−15.4
2014	1	160	740	1450	191.25	−31.25	−33.3
	2	190	760	1500	193.75	−3.75	−4.6
	3	250	770	1530			
	4	180	780	1550			

- Four quarter moving total – add sales revenue of 4 quarters
- Eight quarter moving total – add 2 four quarter totals
- Quarterly moving average – eight quarter total/8
- Seasonal variation – sales revenue – quarterly average
- Average seasonal variation = add seasonal variation of different years in the same quarter divided by number of years

8.22. Moving-average sales forecasting methods – evaluation

- Useful to identify and apply seasonal variation to predictions
- Reasonably accurate for short-term forecasts in stable economic conditions
- Assists planning for each quarter in the future
- Complex
- Less accurate, external environment changes
- In the long run, qualitative data is more accurate

9. Globalisation and International Marketing

9.1. Globalisation

- Globalisation occurs when products, labour and capital are unrestricted by barriers
- Barriers to trade are reduced
- Increased MNCs gives greater freedom for capital
- Freer movement of workers

Potential benefits and strategic opportunities	Potential limitations and threats
■ There is greater opportunity for selling goods in other countries. Opening up new markets, which may not have reached saturation as the domestic market may have done, gives the chance of higher sales, economies of scale and improved profitability. ■ Increased competition gives firms the incentives to become more internationally competitive. Hiding behind trade barriers breeds inefficiency and this will no longer be possible. ■ Pan-European or pan-global marketing strategies can be used to create a global brand identity. This saves on the costs of 'different markets – different products'. ■ There is a wider choice of locations – the opportunity to set up operations in other countries and become a multinational. These locations offer, usually, lower costs and direct access to local markets. Working within each country should lead to better market information. ■ Greater freedom to arrange mergers and takeovers with firms from other nations as restrictions on foreign acquisitions are reduced.	■ Businesses from other countries now have freer access to the domestic market, so there will be increased competition. Wider consumer choices will drive firms that are not internationally competitive out of business. ■ The drive for international competitiveness will also be forcing other firms to become more efficient. ■ Pan-European/global strategies can fail to consider the cultural and taste differences between consumers of different nations. Firms may need to 'think global, but act local' – often called global localisation. ■ International locations can lead to significant transport and communication problems. The risk of unethical practices by managers with delegated authority thousands of miles from head office can lead to problems. ■ Businesses are now increasingly at risk of foreign takeovers, e.g. Land Rover and Jaguar by Tata (India), BAA by Ferrovial (Spain). ■ Increasing activity from anti-globalisation pressure groups may result in bad publicity for multinationals in particular and for those firms found guilty of environmental damage in foreign countries. There is growing concern about the environmental impact of globalisation – especially in emerging economies. Coca-Cola is under pressure to limit production in some Indian states due to shortage of water supplies. ■ Governments will have much less influence on business decisions, e.g. preventing closure of factories to relocate in low-cost countries.

9.2. International marketing

- Selling in foreign markets is risky and expensive
- Globalisation – better communication, better transport, freer trade
- Allows them to increase sales and profits
- Increased competition

Why sell products in other countries?

- Saturated home markets
- Higher profits & sales
- Spread risks
- Legal differences creating opportunities abroad

9.3. Why international marketing is different

1. Political differences
2. Economic and social differences
3. Legal differences
4. Cultural differences
5. Differences in business practice

9.4. International markets – different methods of entry

1. **Exporting**
    1. Sell directly to foreign customers
    2. Sell through an agent

Export directly

Benefits	Limitations
■ Exporting directly means that the company has complete control over the international marketing of its product. ■ Agents and traders may represent several other companies exporting goods, so may not give priority to a new exporting business and its products. ■ No commission is taken by intermediaries, so profit margins are not reduced.	■ Exporting directly means that the business will have to have dedicated sales personnel dealing with foreign buyers and company management may have to travel abroad to meet customers if the size of contracts justifies this. ■ The business does not have a local agent or trader supporting them, so may lack important local knowledge, e.g. about import controls into that country. ■ The exporting business has to handle the logistics of transporting and storing the product and dealing with all paperwork.

Export indirectly

Benefits	Limitations
■ The overseas agent or trading company will have local market knowledge and contacts with potential customers and this should aid the marketing of the product. ■ Transport and administrative procedures become the responsibility of the agent. ■ It may be cheaper for the exporting firm as fewer staff involved in selling abroad will need to be employed and fewer visits from senior managers will be needed.	■ A commission or payment will have to be paid to the agent or trading company and this will reduce the exporting firm's profit margin. ■ The intermediary will have other firms' products to sell as well – how much focus and effort will be given to selling any one product?

2. **International franchising**
    1. International franchising means that foreign franchisees are used to operate a firm's activities abroad
    2. Either 1 franchise owns all branches in one country or different franchises for different regions
3. **Joint ventures**
4. **Licensing**
    1. Allows another company to produce the firm's branded products under the licence
    2. There will be strict controls on quality

3. Goods don't have to be physically exported, lower transport cost and time
4. Parent firm avoids capital 'setting costs'
5. Possible lapses om quality
6. Unethical production methods – poor brand image

5. **Direct investment in subsidiaries** \n

Benefits	Limitations
■ Head office has control of operations and may decide to decentralise this control to allow local managers to take decisions that reflect local conditions – there is no agent or joint venture partner to consult with or take joint decisions with. ■ All profits after tax belong to the company – no commission is paid and no sharing of profits with partner business. ■ Foreign governments may be willing to offer some financial support to encourage such inward investment.	■ It is expensive to set up operations in foreign countries – senior staff will need to visit and may need to be based in the country. Much higher capital cost required than exporting directly or indirectly. ■ Foreign operations may be subject to changes in government policy – e.g. nationalisation of assets or, as with Coca-Cola in the 1980s, being asked to leave certain states in India. ■ Decentralised foreign subsidiaries might take decisions that could damage the reputation of the whole business – such as unethical labour practices.

9.5. International marketing – alternative strategies

- Globalisation is making differences in tastes, culture are becoming less obvious
- This gives companies economies of scale
- Otherwise, when businesses adapt a global marketing mix to local needs and conditions is called localisation

9.6. Pan-global marketing

- It involves adopting a standardised product across the globe as if the entire world were a single market – selling the same goods in the same way everywhere
- They adopt common products, brand messages and promotional campaigns across the world
- Brands with international appeal may become exclusive, luxury products image

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Advantages	Disadvantages
■ A common identity for the product can be established. This aids consumer recognition, especially in a world of increasing international travel by consumers and the widespread use of satellite TV channels with 'international' advertising. ■ Cost reduction can be substantial. The same product can be produced for all markets, allowing substantial economies of scale. This is particularly important for firms that have to spend huge sums on developing new products that may have only a short product life cycle. The same marketing mix can be used. This allows just one marketing agency and advertising strategy to be used for the whole world or region rather than different ones for each country. ■ It recognises that differences between consumers in different countries are reducing – it is often said that teenagers in different countries have more in common with each other than they have with their parents. Therefore, a pan-global strategy for a product aimed at teenagers could be developed.	■ Despite growing similarity between consumer tastes in different countries, it might still be necessary to develop different products to suit cultural or religious variations. Market opportunities could be lost by trying to sell basically the same product everywhere. ■ Legal restrictions can vary substantially between countries and this does not apply just to product restrictions. It is illegal to use promotions involving games or gambling in certain countries, and restrictions on what can be shown in advertisements vary too. ■ Brand names do not always translate effectively into other languages. They might even cause offence or unplanned embarrassment for the company if the selection of the brand name to be used in all markets is not made with care. ■ Setting the same price in all countries will fail to take into account different average income levels.

9.7. Global localisation

- It involves adapting the marketing mix, differentiated products to meet national and regional tastes and cultures
- Thinking global – acting local

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Benefits	Limitations
■ Local needs, tastes and cultures are reflected in the marketing mix of the business and this could lead to higher sales and profits. ■ There is no attempt to impose foreign brands/products/ advertisements on regional markets. ■ The products are more likely to meet local national legal requirements than if they are standardised products. ■ There will be less local opposition to multinational business activity.	■ The scope for economies of scale is reduced. ■ The international brand could lose its power and identity if locally adapted products become more popular than the 'international' product. ■ There will be additional costs of adapting products, adverts, store layouts, etc. to specific local needs – these costs might lead to higher prices than a global marketing strategy would result in.

10. Capacity Utilisation

- Capacity utilisation is the proportion of maximum output capacity currently being achieved
- Capacity utilisation = current output level/max output level * 100
- This helps determine the operational efficiency of a business
- A firm working at full capacity is said to achieve 100% capacity utilisation, with 0 spare capacity

10.2. Impact on average fixed costs

- Higher the capacity utilisation, lower the average fixed costs
- 100% capacity utilisation –
  - Lowest unit cost possible
  - Gives employees a sense of security
  - Maybe used to advertise 0 spare capacity, indicating their high success rates
  - High workload, pressured
  - No time for errors, accidents
  - Customers may have to be turned away
  - Long waiting
  - No time accounted for machinery breakdown, maintenance

10.3. Excess capacity – options

- Low capacity utilisation = excess (spare) capacity
- Excess capacity exists when the current levels of demand are less than the full capacity output of a business
- When deciding how to reduce spare capacity, time factor must be considered
- Short term problem?
  - High levels of stock
  - More flexible production system
  - Offer flexible employment contracts
- Long term?
  - Rationalisation

10.4. Excess capacity – evaluating the options

1. Short term

	SHORT-TERM PROBLEM – e.g. seasonal downturn	
	Advantages	**Disadvantages**
Option 1: Maintain output and produce for stocks	■ no part-time working for staff ■ job security for staff ■ no need to change production schedules or orders from suppliers ■ stocks may be sold at times of rising demand	■ unsuitable for perishable stocks or those that go out-of-date quickly ■ stock-holding costs can be very substantial ■ demand may not increase as expected – the goods may have to be sold at a substantial discount
Option 2: Introduce greater flexibility into the production process: ■ part-time or temporary labour contracts ■ flexible equipment that can be switched to making other products ■ short-term working, e.g. all staff on three-day week	■ production can be reduced during slack periods and increased when demand is high ■ other products can be produced that may follow a different demand pattern ■ avoids stock build-up	■ staff may be demotivated by not having full-time, permanent contracts ■ fully flexible and adaptable equipment can be expensive ■ staff may need to be trained in more than one product – may add to costs

2. Long term

	LONG-TERM PROBLEM – e.g. economic recession or technological changes	
	Advantages	**Disadvantages**
Option 1: Rationalise existing operations and cut capacity, e.g. by closing factory/offices	■ reduces overheads ■ higher capacity utilisation	■ redundancy costs for staff payments ■ staff uncertainty over job security ■ possible threats of industrial action ■ capacity may be needed later if economy picks up or if firm develops new products ■ business may be criticised for not fulfilling social responsibilities
Option 2: Research and development into new products	■ will replace existing products and make business more competitive ■ if introduced quickly enough, might prevent rationalisation and the problems associated with this	■ may prove to be expensive ■ may take too long to prevent cutbacks in capacity and rationalisation ■ requires long-term planning as new products introduced in haste, without a clear market strategy, may be unsuccessful

10.5. Working at full capacity

- Full capacity is when the business produces the maximum output
- Decisions about whether or not to expand the scale of operations must be taken
- This decision depends on the cost, time factor, economic conditions, etc

10.6. Capacity shortage

- When demand for a firm's product is greater than production capacity
- Cause of excess demand must be analysed

10.7. Outsourcing

- It involves using another business to undertake a part of the production process rather than doing it within the business using the firm's own employees
- It leads to reducing and control of operating costs
  - No need to employee specialists
  - Cheaper to buy in specialist services
- Increased flexibility
  - Fixed costs converted to variable
  - Sub-contractors can be used
- Improved company focus
  - The business can focus of their main, core products instead of diverting attention to peripheral goods and services
- Access to quality service or resources
- Freed-up internal resources
- Loss of jobs
  - Negative impact on job security, motivation, productivity
  - Bad publicity
  - Pressure group action
- Quality issues
  - Internal processes can be monitors using quality control
  - Don't have that option with outside contractors
- Customer resistance
  - Customers may not want to deal with overseas outsourced operations
  - Increased doubts about quality and reliability
- Security
  - Sending important information to outside businesses is risky

10.8. Outsourcing evaluation

- Increased outsourcing as operational efficiency becomes important due to increased globalisation, and increased opportunities
- A cost benefit analysis must be done
- It depends on whether it's a core or peripheral activity

11. Lean Production and Quality Management

11.1. Lean Production

- It involves producing goods and services with the minimum of wasted resources while maintaining high quality
- Aims to increase efficiency

11.2. Types of waste

- T – transport
- O – overproduction
- O – overprocessing
- W – waiting
- M – movement
- E – excess inventory
- D – defects

11.3. Methods of lean production

Simultaneous engineering

- Product development is organised so that different stages are done at the same time instead of in sequence
- It involves important tasks like essential design, market research, costing are done at the same time rather than in a sequence
- New products can be introduced quickly

Cell production

- Splitting flow production into self-contained groups that are responsible for whole work units.
- Instead of each worker performing a single task, the production line is split into units – cells
- Each cell produces complete units of work
- Every cell has a team leader, and every worker is multiskilled
- Performance is measured against pre-set targets
- Benefits –
  - Better worker commitment
  - Job rotation

  - Higher productivity
  - Teamwork, sense of belonging

Flexible specialisms

- Having flexible production techniques –
  - Flexible employment contracts
  - Flexible & adaptable machinery
  - Flexible & multiskilled workers
- Benefits –
  - Quicker response to changes in consumer demand
  - Wider range of products
  - Reduced inventory
  - Higher productivity
- Time based management
- Cuts out waste time in management

11.4. Just-in-time inventory

- Involves fewer resources being tied up in buffer inventories

11.5. Kaizen – continuous improvement

- All workers contribute to improving business operations
- Managers want to keep production up to the mark and look for one-off improvements
- Workers know better than the manager, as they are actually involved in production
- Not just technological investments, series of small improvements
- Conditions necessary –
  - Management culture encourages worker participation
  - Team working
  - Empowerment
  - All employees are involved

Evaluation

- Limitations –
  - Some changes can't be introduced gradually, may require radical & expensive solution
  - Resistance from senior managers
  - Tangible costs in the short run
  - May lead to diminishing returns

11.6. Advantages of lean production

- Waste of time & resources eliminated
- Reduced unit costs
- High profits
- Easier operation, less crowded
- Lesser risk of damage
- Quicker launch of new products

11.7. Is lean production & JIT for all businesses?

- Finance
  - Purchase of equipment and machinery is expensive
  - Lean production is impossible without flexible machinery
  - Small firms, limited resources, difficult to use lean production
  - May choose to specialise in niche market
- Management of change
  - More worker involvement
  - Depends on staff flexibility and corporation
  - Lean production is not suitable –
    - Difficult to forecast demand
    - Expensive to restart production
    - Uses it to make redundancies
    - Depend on customer service as USP
    - Cost of new tech, retraining is high

11.8. Quality

- Product which meets customer expectations
- A good quality product need not be expensive
- Advantages –
  - Easy to create loyalty
  - Reduced costs of complaints, returns
  - Long PLC
  - Less promotion
  - Ability to charge a premium price

11.9. How to achieve quality

1. Quality assurance

- Checking for quality after every production process

2. Quality control

- Checking for quality once the production process is completed
- Stages –
  - Prevention
  - Inspection
  - Correction and improvement

11.10. Inspecting for quality

- Quality inspection is expensive
- Sampling process is used
- Weaknesses
  - Looking for problems, negative culture, resentment among workers
  - Tedious job, demotivated, inefficient
  - Take responsibility of quality away from workers

11.11. Quality assurance

- Setting agreed quality standards at every stage of production
- Self-checking by workers

- More emphasis on prevention
- Getting it right the first time
- Checking of components during delivery, reducing time waste
- Advantages –
  - Job enrichment
  - Increased motivation
  - Used to trace back quality problems
  - Reduces need for final inspection

11.12. Why is it important for businesses to establish quality-assurance systems?

- Involves staff – teamwork, motivation, sense of belonging
- Can check every stage of production
- Reduce costs
- Gain accreditation for quality awards

11.13. Total quality management (TQM)

- An approach to quality that aims to involve all employees in quality-improvement
- It is a method of quality control where every employee is given the responsibility of maintaining quality standards at every stage of production rather than giving the entire responsibility to managers, or a separate quality control department.
- TQM aims to achieve a zero defects policy where the product is made right in the first go.
- However, this can only be done when the worker is given training.
- TQM can act as a motivator for employees, as worker participation and delegation will increase.
- This will not work for autocratic leaders

11.14. What are the costs and benefits of introducing and managing quality systems?

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The potential costs of quality systems	The potential benefits of quality systems
■ market research to establish expected customer requirements ■ staff training costs to ensure that standards are understood and the operations needed to check them can be undertaken – this will be especially important with TQM ■ material costs – rejecting below-standard materials and components before they are used in the production process will almost certainly lead to higher expectations from suppliers ■ equipment costs for checking standards at each stage, e.g. laser measuring machines for accuracy of panel fit on a vehicle ■ inspection and checking costs ■ reworking of faulty products or rejection wastage costs – the aim of quality assurance is to reduce these to an absolute minimum – 'right first time' ■ stopping production to trace and correct quality problems will disrupt output	■ consumer satisfaction and repeat custom as there is nothing like a good experience with the quality of a product to encourage consumers to buy more – and to tell their friends about it ■ good publicity, e.g. from consumer pressure groups and consumer-oriented articles in the media ■ reputation for quality encourages retailers to stock the firm's products, so this will increase the distribution outlets for a product ■ easier to establish new products in the market as consumers will associate the business's good reputation with the new product ■ allows the brand to be built around a quality image, and branding is an important form of non-price differentiation for businesses ■ may allow a price premium to be charged over other similar products in that market segment – quality can be used as a USP or unique selling point and this would be a clear demonstration that 'quality pays', as the extra revenue gained should cover the quality costs explained above

11.15. How can the competitiveness of a business be improved by managing quality?

- More competition, good and consistent quality is necessary to survive
- High quality, USP, premium prices
- Increasing consumer incomes, higher demand for good quality products

11.16. Benchmarking

- It involves management identifying the best firms in the industry and then comparing the performance standards – including quality
- Stages –
  - Identify the aspects of the business to be benchmarked
  - Measure performance in these areas
  - Identify the firms in the industry that are considered to be the best
  - Use comparative data from the best firms to establish the main weaknesses in the business
  - Set standards for improvement
  - Change processes to achieve the standards set
  - Re-measurement

Benchmarking – evaluation

- Benefits –
  - Faster & cheaper way of solving problems
  - Area of greatest significance for customers can be identifies
  - Help improve international competitiveness
  - Crossover of ideas while comparisons
  - Workforce involved, motivation
- Limitations –
  - Depends on obtaining relevant and up-to-date information
  - Merely copying ideas will not help
  - Costs of comparisons may not be covered

11.17. Quality circles

- Staff involvement in improving quality
- Small groups of employees discuss quality problems and come up with solutions

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Main benefits	Main conditions determining success
■ Improves quality through joint discussion of ideas and solutions. ■ Improves motivation through participation. ■ Makes full use of the knowledge and experience of the staff.	■ Circle members must be committed to improving quality. ■ Training given in holding meetings and problem-solving. ■ Full support from management. ■ Team should be empowered to implement the recommendations.

Quality issues – evaluation

- Quality isn't an option
- Necessary for business success
- It satisfies customer requirements
- Involving staff – motivation
- Adds value

12. Project Management

12.1. Project

Project

- A project is a specific and temporary activity with a start and end date, with clear goals set, defined objectives needed to be completed in a given budget.
- Elements of a project –
  - Resources (FOP)
  - Money
  - Scope
  - Time
- A project must be planned, managed, cost efficient to be successful
- Key elements of project management
  - Defining the project, setting goals
  - Dividing it into smaller activities
  - Controlling and managing it at every stage
  - Assigning clear roles
  - Quality standards issue

12.2. Impact of project failure

- Bad publicity
- Loss of future contracts
- Penalty payments

12.3. Reasons for failure

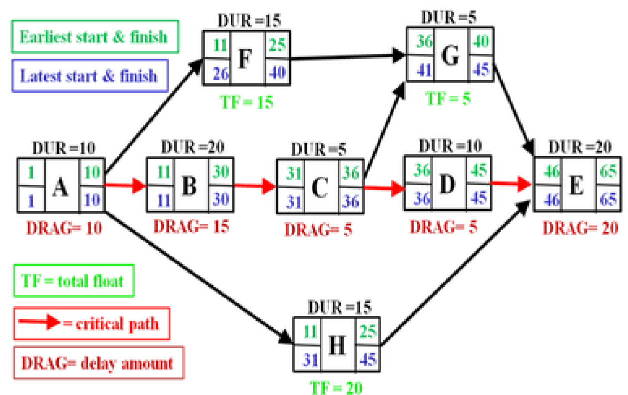
- Not enough information
- Lack of finance, legal issues
- Lack of coordination
- Community against the product
- Errors, wastage
- Bad management, customers could not buy the product
- Workers aren't motivated, not skilled enough, incompetent
- Economic situations (neg)
- Outdated project, quickly changing market
- Bad planning- resources aren't sufficient

12.4. Critical path analysis

- CPA is a planning technique that identifies all tasks in a project, puts them in the correct sequence and allows for the identification of the critical path.
- Activities that must be completed to achieve this shortest time make the critical path
- Process of identifying critical path –
  - Identify the objective
  - Put the tasks in a sequence and draw a network diagram
  - Add durations
  - Identify the critical path

12.5. Network diagrams

- It is a diagram used in critical path analysis that shows the logical sequence of activities and the logical dependence between them – so the critical path can be identified
- EST (Earliest Start Time) = EST of previous activity + duration of current activity
- LFT (Latest Finish Time) = LFT in the previous node- duration of current activity
- Free float shows the length of time an activity can be delayed without delaying the start of next activity
- Free float = EST (next activity)-duration- EST (Current activity)
- Total float = LFT- Duration- EST
- Total float is the amount of time an activity can be delayed by without delaying the whole project
- Total float = 0 the activity is on the critical path and cannot be delayed



12.6. Dummy activities

- Indicated by a dotted line
- Does not consume time or resources
- Used when –
  - A & B start a project, C follows only A but D follows A + B

12.7. Advantages of CPA

- Used to assist planning and management of complex projects
- Helps calculate accurate delivery dates
- Calculation of EST allows special orders to be managed
- Calculation of LFT helps act as a checklist of measuring the success and efficiency
- Knowing the critical path helps understand which activities to focus on, which can't be delayed
- Additional resources needed for speeding an activity could be used from non-critical activities
- Reduces total time taken as it encourages simultaneous development rather than sequential.

12.8. CPA – evaluation

- Doesn't guarantee project success
- Skilled labour, motivated workers also needed
- Good management
- Experienced senior managers

13. Costs

- Managers must be aware about the accurate costs of production to be able to make pricing decisions
- Managers must compare actual costs with budgets and with previous years to identify the most cost effective measures

13.2. Costing methods – a major problem

- Both direct and indirect costs must be included in costing
- However, overheads can not be directly allocated to a particular unit of production

13.3. Cost and profit centres

Cost centres

- A section of a business (department) to which costs can be allocated or charged

Profit centres

- A section of the business to which both costs and revenues can be allocated, therefore profits can be found

13.4. Why divide operations into cost and profit centres?

- Managers and staff will have targets to work towards, MBO if SMART
- Targets can be used to compare with actual data
- Individual department performance can be assessed
- Work can be monitors, help decision making

Problems –

- Managers may consider their department more important, not coordinate with other
- Lead to competition between departments
- Indirect costs, difficult to accurate
- Performance is affected by other factors – external performance, economic conditions

13.5. Overheads and Unit Costs

- Overheads
  - Production overheads
  - Selling and distribution overheads
  - Administration overheads
  - Finance overheads
- Unit cost
  - Total cost/number of units

13.6. Full costing techniques

- Also known as absorption costing
- All fixed and variable costs are allocated to products, services or divisions of a business
- Unit cost = fixed cost + variable cost / total output
- Easy to calculate and understand
- Relevant for single product businesses
- No costs are ignored
- Basis for pricing decisions
- No attempt to allocate costs to cost/profit centres based on actual expenditure
- Lead to inconsistency
- May be misleading
- Must allocate costs on the same basis every year to allow for comparisons

13.7. Contribution or marginal costing

- Allocates only direct costs to relevant profit/cost centres
- Marginal cost = cost of producing 1 extra unit = variable direct costs
- Contribution = revenue (selling price) – variable costs (marginal cost)
- Contribution is NOT equal to profit

- Profit = contribution – fixed costs   Unit contribution = selling price – marginal cost

13.8. Should a firm stop making a product?

- Marginal costing shows managers which product is contributing greatest/least towards profits and overheads
- Using full costing, any loss making products should be stopped
- It ignores their contribution towards fixed costs
- Ending production of products making positive contributions can lead to fall in profits
- Ignores that certain cost centres may incur higher fixed costs than others
- Qualitative factors must be considered

13.9. Should a business accept a contract or a purchase offer at below full cost?

- Profits may increase even if sales are made below the full unit cost as they will provide a small contribution towards the payment of fixed costs which have to be paid either way
- Problems:
  - Existing customers may demand lower prices
  - Negatively effect brand image
  - No excess capacity

13.10. Costing – evaluation

Full costing

- Useful for single product firms
- Provides a quick guideline to the costs
- Inaccurate costing figure, incorrect decisions made
- Can not be used to make comparisons

Contribution or marginal costing

- Assists decision making
- Overheads may be ignored completely

More than 1 costing method must be considered
Qualitative factors must be considered

14. Budgets

- Planning for future provides a sense of direction and purpose
- Budget is a detailed financial plan for the future
- Budgets help measure performance of each department/division
- Purpose of budgets:
  - Planning
  - Effective resource allocation
  - Setting targets to be achieved
  - Coordination
  - Monitoring and controlling
  - Modifying
  - Measuring and assessing performance

14.2. Key Features of Budgeting

- Not a forecast
- Budgets are plans that the business wants to fulfil. Forecasts are predictions made for the future, given certain conditions
- Can be made for any measurable operation
- Coordination between departments is essential
- Must be made while coordinating with employees who will be directly responsible to meet the targets
- Delegated budget involves giving some delegated authority over the setting and achievement of budgets to junior managers. This will improve worker motivation

14.3. Stages in preparing budgets

1. Objectives and strategies for the coming year
    1. This is based on previous performance, external environment and market research
2. Identifying the key or limiting factor
    1. This is sales
    2. No errors and mistakes can be made here
3. Prepare sales budget
    1. Consult all department managers
4. Prepare subsidiary budgets
    1. Cost, labour, admin, cash
5. Coordinate the budgets to ensure consistency
6. Prepare a master budget
7. Present to board of directors

14.4. Setting budgets

- **Incremental budgets**
  - Uses last year's budget as a basis and an adjustment is made for the coming year, specifically for inflation
- **Zero budgeting**
  - Setting budgets to zero each year and budget holder have to argue their case to receive any finance
  - Time consuming
  - Provides incentive for managers to defend their work
- **Flexible budgeting**
  - Cost budgets for each expense are allowed to vary if sales or production vary from budgeted levels
  - Helps variance calculation

14.5. Potential limitations of budgeting

- Lack of flexibilities
- Focused on short term

- May lead to unnecessary spending
- Training needs must be met
- Setting budgets for new projects – time taking, not realistic

14.6. Variance analysis

- Variance is the difference between budgeted and actual figures
- Important as:
  - Measures differences from planned and actual
  - Assists in analysing causes of deviations from the budget
  - Help make more accurate budgets
- Budgeted costs less than actual – adverse
- Budgeted revenue less than actual – favourable
- Budgeted costs more than actual – favourable
- Budgeted revenue more than actual – adverse

Adverse variances	Favourable variances
Causes: ▪ Sales revenue is below budget *either* because units sold were less than planned for *or* the selling price had to be lowered due to competition. ▪ Actual raw material costs are higher than planned for *either* because output was higher than budgeted *or* the cost per unit of materials increased. ▪ Labour costs are above budget *either* because wage rates had to be raised due to shortages of workers *or* the labour time taken to complete the work was longer than expected. ▪ Overhead costs are higher than budgeted, perhaps because the annual rent rise was above forecast.	**Causes:** ▪ Sales revenue is above budget due to higher-than-expected economic growth *or* problems with one of the competitor's products. ▪ Raw material costs are lower *either* because output was less than planned *or* the cost per unit of materials was lower than budget. ▪ Labour costs are lower than planned for *either* because of lower wage rates *or* quicker completion of the work. ▪ Overhead costs are lower than budgeted, perhaps because advertising rates from TV companies were reduced.

14.7. Budgets – evaluation

- Time consuming
- Fails to reflect changes – inflexible
- Helps assess performance
- Provides a sense of direction
- All businesses undertake some form of financial planning

15. Contents of published accounts

15.1. Amending Income Statements

- Format must be the same
- Changes in units sold/produced directly affects sales revenue and variable costs
- Overheads may change according to sales

15.2. Amendments to statement of financial position

Cause of change	Impact on Statement of financial position	Double entry
Sale of inventories for cash (sold for same price as valued in accounts)	Value of inventories will fall	Cash balance will increase
Sale of inventories for cash – sold at higher price than valued in accounts	Value of inventories will fall	Cash balance will increase Shareholders' equity will increase by the value of the profit recorded
Depreciation of equipment	Value of non-current assets will fall	Shareholders' equity will fall – the company is now 'worth less' than before
Intangible assets – such as intellectual property – are revalued	Value of non-current asset increases	Value of shareholders' equity increases
Accounts payable (creditors) ask for much speedier payment	Value of accounts payable falls	Cash balance will decline
Additional shares sold and share capital raised is used to buy property	Value of share capital will increase	Value of property in non-current assets will increase

15.3. Amendments to published accounts

1. Goodwill
   1. It's the reputation and prestige of a business
   2. Value of the business above its physical assets
   3. Usually goodwill of a business is written off
   4. Should not appear as an asset of an existing company as it can easily be disappeared
   5. Appears in the SOFP of a business which bought the other business, which must be written off then
2. Valuing intangible assets
   1. Goodwill is an intangible asset
   2. Patents, copyrights, R&D research are all intangible assets
   3. Known as intellectual property
   4. Difficult to place a monetary value
   5. Only recorded in SOFP during merger/takeover
   6. Market value may exceed need book value providing an incorrect view to stakeholders
3. Capital expenditure and revenue expenditure
   1. Capital expenditure involves spending on non current assets which is not recurring and can be retained for more than 1 year
   2. Revenue expenditure is the day to day costs incurred by a business
   3. Capital expenditure is recorded in the SOFP and revenue expenditure is recorded in the income statement

15.4. Depreciation of assets

- It is the decline in the estimated value of a noon-current asset over time
- This occurs due to:
  - Wear and tear
  - Technological change
- Each year's depreciation is recorded in the income statement as a cost
- NCA are recorded at net book value in the SOFP
- Profits are not overstated (prudence)
- It is a non-cash expense and has no impact on cash flow of a business

15.5. Straight line method of depreciation

- Cost – residual value / expected useful life
- Easy to use and understand
- Estimated life expectancy and residual value which may be wrong
- New NCA depreciate more quickly in the beginning years than in the subsequent years (diminishing return method to be used)
- No recognition of rapid changes in technology
- Repairs and maintenance costs are ignored

15.6. Valuation of inventories

- Inventory maybe raw materials, work in progress and finished goods
- They are recorded at the lower of cost and net realisable value
- Net realisable value is the amount for which inventory can be sold minus cost of selling

16. Analysis of published accounts

16.1. Interpreting company performance

- Profitability ratios – compare the gross and operating profit with sales revenue
- Liquidity ratios – measure of how easily a business can meet its short term debts
- Financial efficiency ratios – indicator of how efficiently the business is using its resources
- Shareholder ratios – used by existing/potential investors to assess the prospects of investment
- Gearing ratio – examine the degree to which the business relies on long term debt to fund operations

16.2. Profitability ratios

Return on capital employed

- Operating profit/capital employed * 100
- Capital employed = non-current assets + current assets – current liability
- Capital employed = non-current liabilities + shareholders equity
- Compares the company's profit with the capital which has been invested
- Higher the %, the better
- Used to compare with competitors and previous years
- Can be compared with other forms of investment – saving in a bank
- Compared with the interest cost of borrowing – less than interest, increase borrowings = lower returns
- Can be increased by increasing the profitable and efficient use of assets
- Not linked with the risks associated

Possible strategies to increase RoCE	Potential limitations
Increase operating profit without increasing capital employed, for example: ▪ raise prices ▪ reduce variable costs per unit ▪ reduce overheads, such as delayering or reducing promotion costs.	▪ demand could be price elastic ▪ cheaper materials could cut back on quality ▪ may not be effective in increasing profit in the short run and may have drawbacks, e.g. less promotion could reduce sales
Reduce capital employed, for example: ▪ sell assets that contribute nothing or little to sales/profit – use the capital raised to reduce debts	▪ assets may be needed in the future, e.g. for expansion of business

16.3. Financial efficiency ratios

Inventory turnover ratio

- Cost of goods sold/value of inventories
- Records the number of times inventory is bought and resold
- Measured in times
- Higher the number, more efficient

Day sales in trade receivables ratio

- Trade receivables/revenue * 365
- Measures how long it takes for a business to recover payments from trade receivables
- Shorter, the better as it indicates better control over working capital
- Can be improved by giving shorter credit periods, cash discounts, etc

16.4. Shareholder or investment ratios

Dividend yield ratio

- Measures the rate of return a shareholder gets at the current share price
- Dividend per share/current share price * 100
- Dividend per share = total annual dividends/total number of issued shares
- If share price rises due to improved prospects however dividend remains the same, dividend yield will fall
- Dividend yield should be compared with other investment returns
- Can be compared with previous years/competitors

Dividend cover ratio

- Dividend cover ratio – profit for the year/annual dividends
- This ratio indicates how many times the ordinary share dividend can be paid after tax and interest
- Higher the ratio, more dividends can be paid, indicating higher margin for reinvesting in the business
- Lower ratio indicates, low retained earnings

Price/earnings ratio (P/E ratio)

- P/E ratio – current share price/earnings per share
- Earnings per share – profit for the year/number of issued shares
- It reflects the confidence the investors have in future prospects of the business
- Higher P/E ratio, investors expect higher earnings growth
- The ratio should be compared with business in the SAME industry only

16.5. Gearing ratio

- It measures the degree to which the capital of the business is financed from long-term loans
- Non-current liabilities/shareholders equity + non-current liabilities * 100
- The ratio indicates the level of which the company's assets are financed from external long-term borrowing
- Above 50% leads to highly geared
- Higher the ratio, greater is the risk
- Risk arises from 2 reasons:
  - Higher the borrowing, more interest must be paid
  - Interest still has to be paid
- Debts have to be paid eventually, affecting liquidity negatively
- Low gearing ratio indicates a safe business strategy

16.6. Interest cover ratio

- It assesses how many times a firm could pay its annual interest charges out of current operating profit
- Interest cover – operating profit/annual interest paid
- Higher the figure, less risky the current borrowings are

16.7. Ratio analysis – evaluation

- Help take important decisions –
  - Whether or not to invest in a business
  - Whether or not to lend money to a business
  - Whether profitability is rising or falling
  - Whether the management are using resources efficiently

16.8. Limitations of ratio analysis

- One ratio result is not helpful. These results must be compared with other business and past result
- Inter-firm comparisons should only be done with businesses in the same industry
- Trend analysis doesn't take into account external factors which affect business prospects
- Different companies can use different methods of valuing their assets leading to differences in results
- Ratios only take into account quantitative data and ignore qualitative information
- They do not solve problems but rather just highlight the issues

17. Investment Appraisal

17.1. What is meant by investment appraisal?

- It involves evaluating the profitability or desirability of an investment project
- These are quantitative techniques to assess the financial feasibility
- It helps managers understand whether future returns will be greater than the costs and by how much
- Non-financial factors are equally important and should also be considered
- Quantitative methods of appraisal compare the cash outflows with the expected cash inflows of a project

17.2. Quantitative investment appraisal – what information is necessary?

- To be able to judge the profitability of a project through quantitative investment appraisal methods, the following information is required:
  - Initial capital cost
  - Estimated life expectancy
  - Residual value of the investment
  - Forecasted net returns or net cash flows

17.3. Forecasting cash flows in an uncertain environment

- We assume cash inflows equal annual revenues
- Cash outflows equal annual operating costs
- Net cash flow = cash inflow – cash outflow
- Net cash flow is compared to the initial investment cost
- External factors may reduce the accuracy of these estimates

17.4. Payback period

- Payback period is the length of time it takes for the net cash inflows to pay back the original capital cost of investment
- Step 1: list cash inflows
- Step 2: calculate cumulative cash inflows
- Step 3: identify the year with last negative cash inflow
- Step 4: Use formula: Additional net cash flow/annual cash flow * 12
- Example:

Year	Annual net cash flows ($)	Cumulative cash flows ($)
0	(500,000)	(500,000)
1	300,000	(200,000)
2	150,000	(50,000)
3	150,000	100,000
4	100,000 (inc. residual value)	200,000

- Year 0 = time period in which the investment was made
- Cash flow during this time is negative, indicated by brackets ()
- Cash flow is positive in year 3, however we need to note that the entire year 3 is not going to be used to repay the capital cost as only 50000 is due and year 3 has cash inflow of 150000
- Using the formula: 50000/150000*12 = 4 months
- Payback period = 2 years, 4 months

- Longer the pay back period, more uncertain the investment is
- Inflation may make future cash flows less in real value
- Capital has an opportunity cost, if borrowed, interest must be paid

Advantages	Disadvantages
▪ It is quick and easy to calculate. ▪ The results are easily understood by managers. ▪ The emphasis on speed of return of cash flows gives the benefit of concentrating on the more accurate short-term forecasts of the project's profitability. ▪ The result can be used to eliminate or 'screen out' projects that give returns too far into the future. ▪ It is particularly useful for businesses where liquidity is of greater significance than overall profitability.	▪ It does not measure the overall profitability of a project – indeed, it ignores all of the cash flows after the payback period. It may be possible for an investment to give a really rapid return of capital, but then to offer no other cash inflows. ▪ This concentration on the short term may lead businesses to reject very profitable investments just because they take some time to repay the capital. ▪ It does not consider the timing of the cash flows during the payback period – this will become clearer when the principle of discounting is examined in the final two appraisal methods.

17.5. Accounting rate of return (ARR)

- ARR measures the annual profitability of an investment as a percentage of the initial investment
- ARR = annual profits (net cash flow)/initial capital cost * 100
- ARR = annual profit (net cash flow)/average capital cost * 100
- ARR = initial capital cost – residual capital value/2
- Step 1: add all positive cash flows
- Step 2: subtract initial cost of investment
- Step 3: divide by lifespan
- Step 4: calculate the % return

Advantages	Disadvantages
▪ It uses all of the cash flows – unlike the payback method. ▪ It focuses on profitability, which is the central objective of many business decisions. ▪ The result is easily understood and easy to compare with other projects that may be competing for the limited investment funds available. ▪ The result can be quickly assessed against the predetermined criterion rate of the business.	▪ It ignores the timing of the cash flows. This could result in two projects having similar ARR results, but one could pay back much more quickly than the other. ▪ As all cash inflows are included, the later cash flows, which are less likely to be accurate, are incorporated into the calculation. ▪ The time value of money is ignored as the cash flows have not been discounted – this concept is considered later in the chapter.

17.6. Discounting future cash flows

- In order to compare projects with different ARR and payback periods, managers require different appraisal methods with consider both the size of cash flow and timing
- Discounting is the process of reducing the value of future cash flows to give them their value in today's terms
- Discounting calculates the present values of future cash flows so that investment projects can be compared with each other by considering today's value of their returns

17.7. Discounting – how is it done?

- Present value of future money depends on:
  - Interest rates – higher the interest rate today, less value future cash has in today's money
  - How long in future it is received – longer, lesser value

17.8. Discounted payback

- It used discounted cash flows to calculate the payback period of the capital cost
- To get discounted cash flows, you multiple the net cash flow with the discount factor
- Then, use discounted cash flow to calculate the payback period

17.9. Net present value

- Net present value is today's value of the estimated cash flows resulting from an investment
- Stage 1: multiply discount factors by net cash flows
- Step 2: add the discounted cash flows
- Step 3: subtract the capital cost to give the NPV
- Cash flows in year 0 are NOT discounted
- If discount rate is greater than the cost of borrowing the capital cost, the investment will be profitable
- If NPV is greater than 0, the business should go ahead with the investment

Advantages	Disadvantages
▪ It considers both the timing of cash flows and the size of them in arriving at an appraisal. ▪ The rate of discount can be varied to allow for different economic circumstances. For instance, it could be increased if there was a general expectation that interest rates were about to rise. ▪ It considers the time value of money and takes the opportunity cost of money into account.	▪ It is reasonably complex to calculate and to explain – especially to non-numerate managers. ▪ The final result depends on the rate of discount used, and expectations about interest rates may be wrong. ▪ Net present values can be compared with other projects, but only if the initial capital cost is the same. This is because the method does not provide a percentage rate of return on the investment.

17.10. Internal rate of return

- Internal rate of return is the rate of discount that yields a net present value of zero – the higher the IRR, the more profitable the investment is
- This rate must be compared with IRR of other projects, expected cost of capital, rate of interest, cut-off rate
- As the discounted rate increases, NPV reduces until negative values are reached. Plotting this on a graph can help estimate IRR

Advantages	Disadvantages
▪ By giving a percentage rate of return, different projects costing different amounts can be compared. ▪ The IRR is easily compared with the rate of interest or the **criterion rate** of the business. ▪ It avoids the need to choose an actual rate of discount.	▪ The calculation is tedious without a computer. ▪ By giving an exact result, it can mislead business users into believing that investment appraisal is a precise process without risk and uncertainties.

17.11. Qualitative factors – investment decisions are not just about profit

- Impact on the environment and the local community
- Risks involved with certain projects
- Aims and objectives of a business
- Different managers are prepared to accept different degrees of risk

17.12. Investment appraisal – evaluation

- Users of the information maybe misled into assuming that the results must be certain and definite
- Due to uncertainties, investment appraisal methods ONLY act as guides which help managers make their final decision
- Different methods can lead to conflicting results. It depends on the manager's attitude towards risk
- Business objectives must be considered

18. What is Strategic Management?

18.1. Corporate Strategy

- A strategy is a plan, used as a basis to create tactics. They are used to help achieve overall objectives.
- Tactics are smaller, short-term plans to achieve strategies
- Strategic management involves managing resources (factors of production) to achieve your plans and strategies.
- Strategic management is a long term process. Decisions are made by board of directions, CEO, CFO (senior managers)
- Organisational structure must be adapted to the strategy to continue efficient production

18.2. Stages of strategic management

1. Analyse the present situation
2. Set vision, mission and objectives
3. Prepare strategies
4. Integration – coordinating between different departments
5. Allocate resources
6. Monitor, review and evaluate

18.3. Factors considered when choosing a strategy?

- Objectives
- Competition
- Factors of production (resources)
- Other strengths on the business

18.4. Need for strategic management

- Strategic management includes analysis, choice and implementation
- Change management leads to resistance, a business must control this through strategic implementation
- Failing to do this will make the business inflexible and lead to incorrect long-term decisions

18.5. Strategy VS Tactic

- Strategy is long term, tactic is short term
- Strategy can not be reversed
- Strategy is made by to management, tactic is made by department heads, subordinates
- Strategies affect every department, tactics are department/division specific

18.6. Competitive advantage

- It is an edge a business has over other businesses
- Can be achieved through –
  - Cheaper price
  - USP (product differentiation)
  - Quality
  - Brand loyalty
- Same product, cheaper price
- Better quality, higher price
- How to achieve this –
  - Market research
  - Lean production
  - Training
  - Process innovation
  - Technology/automation

19. Strategic Analysis

- It is the process of conducting research into the business environment within which an organisation operates, and into the organisation itself, to help form future strategies
- It involves looking in detail, at the current position and predict changes to the future, ensuring they fit with the long term strategy
- Answers 3 main questions:
  - Where is the business now?
  - How might the business be affected by what is happening or likely to happen?
  - How could the business respond to these likely changes?
  \

19.2. SWOT Analysis

- SWOT analysis is a form of strategic analysis that identifies and analyses the main internal strengths and weaknesses and external opportunities and threats that will influence the future direction and success of a business
- S – STRENGTHS – Internal factors of a business, which can be a basis to develop their competitive advantage. Identified through internal audits
- W – WEAKNESSES – Internal negative factors, such as poor training and motivation
- O – OPPORTUNITIES – Potential areas of expansion for the business to make higher profits. Identified through external audits
- T – THREATS – External factors about the business's economic environment, market conditions which may negatively affect the business performance
- Helps managers assess the likely success of future strategies and their constrains
- Not necessary to pursue the most profitable option, rather focus on developing a USP by exploiting the strengths and opportunities
- Not sufficient to carry out only SWOT
- It is subjective
- No quantitative data
- Should be used as ONLY a guide

19.3. PESTEL Analysis

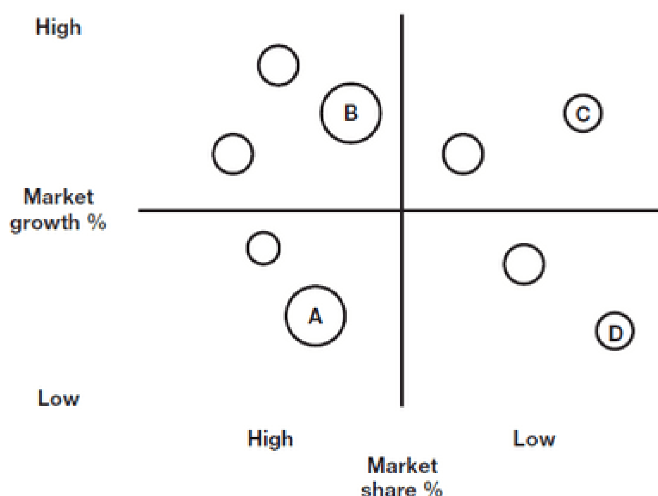
- The strategic analysis of a firm's macro environment including political, economic, social and technological factors
- P – Political
- E – Economical
- S – Social
- T – Technological
- E – Environmental
- L – Legal/Legislation
- Helps assess the chance of success of a business strategy
- PESTEL is complementary to SWOT, not an alternative
- Must be constantly updated – dynamic business environment

19.4. Business vision/mission statements and strategic analysis

- Mission statement is a statement of the business's core purpose and focus, phrased in a way to motivate employees and to stimulate interest by outside groups
- Vision statement is a statement of what the organisation would like to achieve or accomplish in the long term
- Mission statement should answer –
  - What do we do?
  - For whom do we do it?
  - What is the benefit?
- Vision and mission provide a sense of direction and focus and are the basis of developing strategies

19.5. Boston Matrix

- It is a method of analysing the product portfolio of a business in terms of market share and market growth



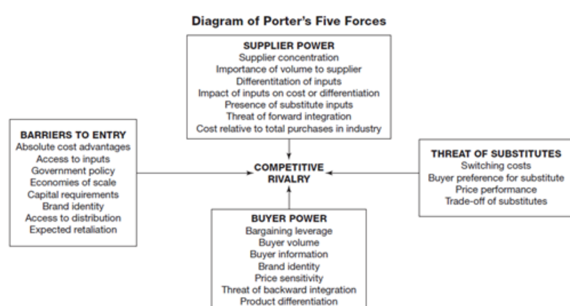
- Low market growth & high market share – CASH COW (A)
  - Well established product, mature market
  - High positive cash flow, profits
  - Low promotional and marketing costs
  - Maintain cash cows for as long as possible
- High market growth & high market share – STAR (B)
  - Successful product, expanding market
  - Maintain market position
  - High marketing and promotion costs – product differentiation
  - High revenue generation
- High market growth & low market share – PROBLEM CHILD (C)
  - Consumes resources, generates very little return
  - Heavy promotion expenditure to help become cash cow
  - Uncertain future – quick decisions
- Low market growth & low market share – DOG (D)
  - Offers very little – sales and cash flow
  - Replaced/withdrawn from the market
- Helps identify products which require support, corrective action through strategies –
  - Building – problem child products to be turned into cash cows
  - Holding – continuing the star product support
  - Milking – using cash flow from cash cows to invest in other products in the portfolio
  - Divesting – identifying dogs and stopping their production
- A business should aim for a balanced portfolio, not too many problem children or dogs
- Relevant when –
  - Analysing performance off existing portfolio

  - Planning action within existing products
  - Planning introduction of new products
- Business success depends on the accuracy of analysis, skills and experience of managers
- Can not predict future, tell what will have to future sales
- Only a planning tool, very complex
- Assumes high profit and high market share are directly linked

19.6. Porter's Five Force Analysis

- Michael Porter identified 5 main forces that models an industry

It can be used to build a competitive edge and helps understand the business's external environment



- Barriers to entry
  - How easily can new competitors enter the market
  - Becomes a threat when:
    - Low EOS
    - Cheap technology needed
    - Easy to access distribution channels
    - No patents/legal restrictions
    - Low need for product differentiation
- Power of buyers
  - Power of customers on the industry
  - Higher power when:
    - Small, undifferentiated suppliers
    - Low cost of switching
    - Limited consumers
- Power of suppliers
  - High cost of switching
  - High brand image
  - Little bargaining power for customers
- Threat of substitutes
  - Substitute products in other industries
- Competitive rivalry
  - Key, most important part
  - Determines the level of competition in an industry
  - Determined by the other 4 forces
  - High rivalry when:
    - Cheap and easy for new firms to enter
    - Threat from substitute products
    - High supplier power
    - High consumer power
    - Large number of firms with similar market share
    - High fixed costs
    - Slow market growth
- Helps firms identify whether or not to enter the market – profitability, competition, whether or not to stay in the market
- Develop strategies to improve competitive position
  - Product differentiation
  - Buying out rivals
  - Market segmentation
  - Communicate and collude with competitors
- Rapidly changing markets, may not remain the same
- Complex

19.7. Core competencies

- Core competence is an important business capability that gives a firm competitive advantage
- Develop core competencies to gain competitive advantage as they help develop core products
- Core products are products based on a business's core competences, but not necessarily for the final consumer
- Being good at one product isn't the same as their core competence
- It depends on integrating multiple technologies and different product skills which already exist in the business
- Doesn't always require huge R&D expenditure

20. Strategic Choice

- Different options available and techniques used to make a choice
- Factors influencing decisions –
  - Resources (capital available, costs)
  - Experience and knowledge (core competencies)
- This process is done based on the management's judgement and skills
- It is a subjective process, differs from people to people

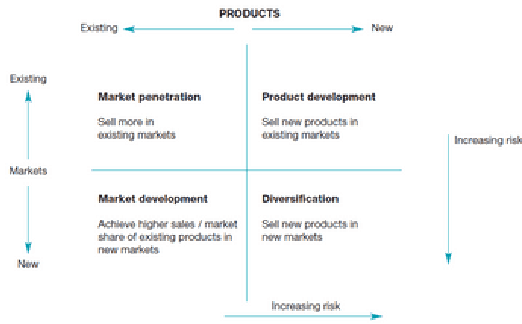
20.2. Techniques

1. Ansoff's matrix
2. Force field analysis
3. Decision tree analysis
4. Investment appraisal

20.3. Ansoff matrix

- It is used to show the degree of risk associated with the 4 growth strategies of market penetration, market development, product development and diversification
- 2 main variables:
  - Market to operate
  - Product to sell
- Market –
  - Remain in the existing market
  - Enter new market
- Product –
  - Continue selling existing product

- Develop new ones



- Market penetration involves achieving higher market shares in existing markets with existing products
- Low risk – market penetration
- Product development involves the development and sale of new products in existing markets
- Market development involves selling existing products in new markets
- Product development involves innovation
- Market development involves repositioning
- Medium risk – market development, product development
- Diversification involves selling, different, unrelated products in new markets
- Diversification involves identifying new areas for growth. If successful, it reduces the overall risk of the business
- High risk – diversification

20.4. Evaluation – Ansoff's matrix

- Allows analyses of the degree of risk associated with each business strategy
- Subjective, requires further research
- Only considers 2 factors
- Must consider external factors – SWOT, PESTLE analysis
- Further research beyond the matrix is required

20.5. Force field analysis

- It is a technique for identifying and analysing the positive factors that support a decision and negative factors that constrain it
- Helps managers understand the pros and cons of a decision, helping them strengthen the driving factors and reduce the negative factors
- Placed on a force field diagram

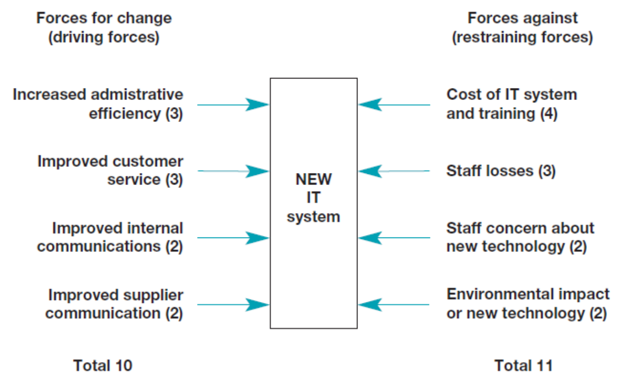
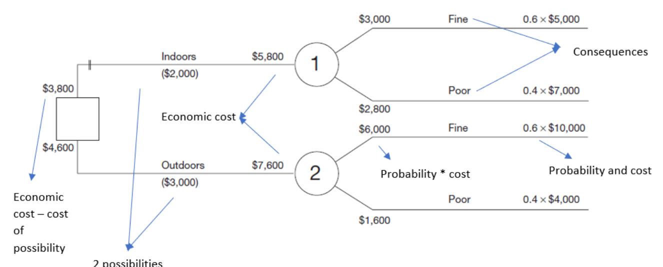


Figure 39.2 A force-field diagram

- Conducting a force field analysis:
  - Analyse the current and desired situation
  - List the driving and constraining factors
  - Allocate a numerical score to each
  - Place them on the force field diagram
  - Sum them and establish whether it is worth moving ahead with the proposal
  - Identify how to reduce the constraining factors
- Unskilled or inexperienced managers may not identify all the all the relevant factors
- Allocation of numerical values is subjective

20.6. Decision Tree analysis

- A diagram that sets out the options connected with a decision and the outcomes and economic returns that may result
- Main features of a business decision:
  - All of the options open to a manager
  - Different possible outcomes which can arise
  - Chances of these outcomes
  - Economic returns
- Depends on the accuracy of data
- Probabilities may be according to past data, not always true for future
- Aid the decision making process, cannot replace risk and impact of non-numerical, qualitative factors consideration
- Features of a decision tree diagram:
  - Constructed from left to right
  - Each branch represents an option with the consequences and chances of their occurrence
  - Circles show the range of outcomes
  - Probabilities are shown alongside the outcomes
  - The economic returns of every outcome are given



21. Strategic Implementation

- Implementation means putting into effect to carrying out an idea
- Strategic implementation is the process of planning, allocating and controlling resources to support the chosen strategies
- Effective strategic implementation requires:
  - Appropriate organisational structure
  - Adequate resources
  - Well motivated staff
  - Leadership style and organisational culture which encourages change
  - Control and review systems to monitor progress

21.2. Business Plans

- A business plan is a written document that describes a business, its objectives and its strategies, the market it is in and its financial forecasts
- Contents of a business plan:
  - Executive summary - overview of the business
  - Description of the business opportunity
  - Marketing and sales strategy
  - Management team and personnel
  - Operations
  - Financial forecasts

21.3. Importance of business plans

- Helps obtain finance
- Provides a sense of direction and purpose
- Helps develop objectives and strategies of a business
- Original forecasts can act as budgets and control benchmarks
- Can be rewritten and adapted to accommodate new and revised strategies

21.4. Corporate plans - what do they contain?

- A corporate plan is a methodical plan containing the details of the organisation's central objectives and the strategies to be followed to achieve them
- They include:
  - Overall objectives
  - Strategies to meet objectives
  - Main objectives of each key departments

21.5. Corporate plans - what are they for?

Benefits

- Helps have a clear focus and a sense of purpose
- Helps communicate the sense of purpose and focus to all managers and employees
- Allows the original objectives to be compared with actual outcomes to see how well the company has performed
- Planning process helps managers consider the business's strengths and weaknesses

Limitations

- Maybe made obsolete due to rapid and unexpected internal and external changes
- The plan must be adaptable and flexible

The value of corporate plans

- Corporate plan contents must be shared with:
  - Potential investors
  - Major lenders
  - Other stakeholder groups
  - Employees

21.6. The main influences on a corporate plan

Internal

- Financial resources
- Operating capacity
- Managerial skills and experience
- Staff numbers and skills
- Culture of the organisation

External

- Macro-economic conditions
- Central bank and government policy changes
- Technology changes
- Competitors actions

21.7. Corporate culture - what is meant by this

- Corporate culture is the values, attitudes and beliefs of the people working in an organisation that control the way they interact with each other and with external stakeholder groups
- Corporate culture - the way we do things around here
- The culture of an organisation gives it a sense of identity
- It effects the way employees act, take decisions

21.8. The main types of corporate culture

Power culture

- Concentrating power among just a few people

- Autocratic leadership style

Role culture

- Each member of staff has a clearly defined job title and role
- Bureaucratic organisations
- Employees operate within the rules and show little creativity
- Power and influence is determined by a person's position

Task culture

- Based on cooperation and teamwork
- Similar to a matrix structure
- Works in teams and are encouraged to be creative

Person culture

- When individuals are given the freedom to express themselves fully and make decisions for themselves
- Most creative type of culture

Entrepreneurial culture

- This encourages management and workers to take risks, to come up with new ideas and test out new business ventures
- Success is rewarded but failure is not criticised

21.9. Changing organisational culture - possible reasons for change

- Product led business responds to changing market conditions
- Investors may demand more transparency and recognition
- Merger and takeover
- Declining profits and market share
- Change in economic conditions

21.10. Problems of changing organisational culture

- Time-taking
- May involve changes to personnel, job descriptions, communication methods and working practices
- Common elements to the different approaches:
  - Focus on the positive aspects and how to strengthen them and how to reduce the negative aspects
  - Establish new objectives and mission statement
  - Encourage 'bottom-up' participation of workers
  - Train staff in new procedures and new ways of working to reflect the changed value system
  - Change the staff reward system

21.11. Corporate culture and strategic implementation

How does a corporation's culture affect strategic implementation

- In a power culture, the business will not consult and communicate with staff on major strategic changes
- They will be imposed in a take it or leave it attitude
- May lead to resentment and resistance
- In a task/people culture, active participation will be encouraged
- Two-way communication may lead to employees willingly accepting change
- Strong culture promotes and facilitates successful implementation, weak culture doesn't
- Strong culture - widespread share of common beliefs , practices and norms in a business

Evaluation - importance of corporate culture

- It drives people's behaviour and attitudes
- Determines the way employees are treated
- Supports brand image and relationships
- Determines how strategic decisions are made and implemented
- Organisational culture affects economic performance and long term success

21.12. Change - techniques for implementing, managing and controlling change

What change means

- Change management involves planning, implementing, controlling and reviewing the movement of an organisation from its current state to a new one
- It is done in response to internal and external pressures
- Occurs whether or not we want it
- Evolutionary or incremental change occurs slowly over a period of time
- Dramatic or revolutionary change id unanticipated

Major causes of change

Nature of change	Examples of change	Managing change
Technological advances – leading to new products and new processes	■ products – new computer games, iPads and iPhones, hybrid-powered cars ■ processes – robots in production; CAD in design offices and computer systems for stock control.	■ need for staff retraining ■ purchase of new equipment ■ additions to product portfolio – other products to be dropped ■ need for quicker product development, which may need new organisational structures and teams.
Macro-economic changes – fiscal policy, interest rates, fluctuations in the business cycle	■ changes in consumers' disposable incomes – and demand patterns that result from this ■ boom or recession conditions – need for extra capacity or rationalisation.	■ need for flexible production systems – including staff flexibility – to cope with demand changes ■ explain need for extra capacity or the need to rationalise ■ deal with staff cutbacks in a way that encourages staff who remain to accept change.
Legal changes	■ changes to what can be sold (raising age for buying cigarettes) or when (24-hour licences for restaurants).	■ staff training on company policy on sale of cigarettes and alcohol ■ flexible working hours and practices.
Competitors' actions	■ new products ■ lower prices – based on higher competitiveness/lower costs ■ higher promotion budgets.	■ encourage new ideas from staff ■ increase efficiency by staff accepting the need to change production methods ■ ensure resources are available to meet the challenge.

Stages of the change process

1. Where are we now and why is change necessary
2. New vision and objectives
3. Ensure resources are in place to enable change
4. Give maximum warning about the change to employees
5. Involve staff in the plan for change and its implementation
6. Communicate
7. Introduce initial changes that bring quick results
8. Focus on training
9. Sell the benefits
10. Always remember the effects on individuals
11. Check on how individuals are coping and support them

Lead change, not just manage it

- Managing change involves:
  - New objectives
  - Resources (FOP and finance) available for implementation
  - Actions to ensure change is introduced
- Leading change involves:
  - Worker motivation at all levels of hierarchy
  - Dynamic leaders
  - Corporate culture which encourages change
  - Support available for all managers to make the process easier

Project champion

- Project champion is a person assigned to support and drive a project forward, who explains the benefits of change and supports the team in its implementation
- Someone who has enough influence in the organisation
- Not involved in day-to-day planning and implementation
- Help remove barriers to implementation

Project groups or teams

- Project groups are created by an organisation to address a problem that requires input from different specialists
- Ideas are exchanged within these groups, helped develop an appropriate action plan
- Responsibility of implementing the plan remains with the senior manager

21.13. Promoting change

- Process of promoting change:
  - Establish a sense of urgency
  - Create an effective project team to lead the change
  - Develop a vision and strategy for change
  - Communicate the changed vision
  - Empower people to take actions
  - Generate short term gains which benefit many people
  - Consolidate these gains to produce more change
  - Build change into the culture

21.14. Resistance to change

- Reasons why managers and employees may resent and resist change:
  - Fear of the unknown
  - Fear of failure
  - Losing something of value
  - False beliefs about the need for change
  - Lack of trust
  - Inertia - reluctance to change in order to maintain their status quo

21.15. Contingency planning and crisis management

- It involves preparing an organisation's resources for unlikely events
- It involves identifying how to minimise the potential impact of a disaster and prevent it from happening in the first place
- Steps in contingency planning:
  - Identify the potential disasters that could affect the business
  - Assess the likelihood of these occurring
  - Minimise the potential impact of risks
    - Involves protecting the company's assets, reputation and public goodwill
  - Plan for continued operations of the business
- Advantages and limitations of contingency planning:
  \

Benefits	Limitations
■ reassures staff, customers and local residents that concerns for safety are a priority ■ minimises negative impact on customers and suppliers in the event of a major disaster ■ public relations response is much more likely to be speedy and appropriate, with senior managers being used to promote what the company intends to do, by when and how.	■ costly and time-consuming – not just the planning process but the need to train staff and have practice dry runs of what to do in the event of: fire, IT failure, terrorist attack, accident involving company vehicles and so on ■ needs to be constantly updated as the number and range of potential disasters can change over time ■ staff training needs increase if labour turnover is high ■ avoiding disasters is still better than planning for what to do if they occur.

22. Enterprise Resource Planning

- ERP involves the use of a single computer application to plan the purchase and the use of resources in an organisation to improve the efficiency of operations
- Using one database program, it becomes easier to coordinate and link together all of the support systems of a business
- Supply chain includes all the stages in the production process from obtaining raw materials to selling to the consumer – from point of origin to point of consumption

22.2. Stages of supply chain management

1. **Plan –** decide which resources
2. **Suppliers –** choose the most cost effective suppliers
3. **Costs –** record at every stage of production
4. **Manufacture –** check quality and monitor progress
5. **Deliver –** identify and pick cost effective transport systems
6. **Returns –** reimburse customers for any defects and returns

22.3. Benefits and Drawbacks

Benefits –

- Production is according to demand, more efficient, lower wastage
- More sustainable
- Ability to use JIT more efficiently
- Reduces costs – supply chain management
- Better customer service
- Better coordination
- Increased information available to the management, help future decision making

Limitations –

- High costs of database and computer systems
- May cause resentment as not using the tried and tested ways of operations
- Implementation takes time – 1-3 years

22.4. Evaluation

- Not for short-term
- Effective way to save costs and increase competitiveness
- Expensive
- If want to do both B2B and B2C, ERP is necessary

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Business (9609)

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