Paper 2 Revision

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Section 4: **Operations**

Topic ▪ Content ✓ *Points to include*	**Red** ☹	**Amber** 😐	**Green** ☺
4.1 Production processes ▪ Different production processes and their impact on businesses ✓ *job, batch, flow* ▪ The influence of technology on production and the impact on businesses ✓ *automation, computers and robotics*			
4.2 Quality of goods and services ▪ The concept of quality ▪ Methods of ensuring quality ✓ *quality control, quality assurance* ▪ The importance of quality in both the production of goods and the provision of services ✓ *reputation of the business, to gain and retain customers, reduce product returns and recalls*			
4.3 The sales process and customer service ▪ Methods of selling ✓ *e-commerce, face to face, telesales* ▪ The influence of e-commerce on business activity ▪ The importance to a business of good customer service including after-sales service ✓ *to gain and retain customers* ▪ The contribution of product knowledge and customer engagement to good customer service			
4.4 Consumer law ▪ The impact of consumer law on businesses ✓ *reputation of the business, safety and satisfactory quality of goods*			
4.5 Business location ▪ Factors influencing business location ✓ *costs, the proximity to market, labour and materials*			
4.6 Working with suppliers ▪ The role of procurement ✓ *identifying goods and services to buy, choosing suppliers, ordering goods and services, receiving deliveries from suppliers* ▪ The impact of logistical and supply decisions on businesses ✓ *time, length of supply chain, reliability of supply, costs, customer service*			

Production processes

✪ *Methods of production*

Method	Definition	Advantages	Disadvantages
Job production	One-off, specialised production; tailor-made to meet the individual needs of a specific customer. Usually 'labour intensive' (relies on skilled workers not machines).	✓ Can sell the product for a premium price = 🡅 revenue ✓ Worker satisfaction is high as they are skilled / involved in whole process = 🡅 motivation 🡇absenteeism 🡇 labour turnover ✓ Goods often ordered & paid for beforehand = better cash flow & reduced waste of stock	× Requires highly skilled workers = 🡅 costs (staff wages & training) = 🡇 profits (in short term) × Specialist equipment might be needed for one job, but not the next = 🡅 costs 🡇 profits × Production is slower than flow & batch = customers have to wait longer = possible customer dissatisfaction
Batch production	Where products are made in groups / batches; e.g. different sizes, shapes, colours. Can also include products made in stages (e.g. doors, bonnets & engines) which are then assembled.	✓ A range of sizes / shapes / colours available to suit a variety of different customer needs (e.g. different shoe / clothing sizes) = 🡅 sales revenue ✓ When batches are made in high quantities, automation can be used (e.g. machines instead of human workers) = 🡇 cost of recruitment, training & wages	× When switching between one batch and the next, there will be 'downtime' – i.e. no products being made during this time, yet the business will still have a number of costs to pay (rent, bills, wages, etc.) × A lot of storage space is needed for a variety of different parts / sizes / types = either 🡅 cost of storage space or 🡇 space available for production
Flow production	Continuous, mass production of the same product, over and over again. Often 'capital intensive' (relies on machines not skilled workers).	✓ Productivity is high (i.e. high number of products made per day) so the cost of each product / unit is low = can either maximise profits, or reduce selling price in a competitive market ✓ Less likely to need highly skilled workers (compared to job production) = 🡇 wage costs = 🡅 profits ✓ Automation can be used (e.g. machines instead of human workers) = 🡇 cost of recruitment, training & wages. Also, can work 24/7, which increases output = 🡅 <u>potential</u> sales / meets high customer demand.	× Repetitive & boring for workers & lack of job satisfaction = 🡅 mistakes 🡅 absenteeism 🡅 labour turnover 🡇 demotivation × Very high costs in the short term if automation is used e.g. millions of pounds to buy machinery, taking a long time to pay off loans & break-even

✪ What is meant by the term '**division of labour**'?

This is where the whole production process (e.g. making an entire car from start to finish) is broken down into individual stages (e.g. 1. putting the doors on, 2. then the bonnet, 3. then the wheels, etc.). Workers are then assigned just one stage each to complete; this a) speeds up the entire process thus reduces costs, and b) means that workers do not need to be highly skilled (so reduces wage & training costs). A possible drawback is employee boredom, dissatisfaction & demotivation.

✪ Automation is a production process involving machinery that is not controlled by a person but usually controlled by a computer.

✪ Robotics is the use of robots in the process of production.

✪ Benefits and drawbacks of **automation** (i.e. using machines & robots in factories, instead of human workers):

Benefits	Drawbacks
▪ Machines can work 24/7, without breaks or holidays, and at a faster rate than humans = 🡹 output = 🡹 potential sales & meet customer demand. ▪ Reduces costs associated with employees in the long term: recruitment, training, wages, motivation methods, appraisals, etc. ▪ Machines can work consistently and accurately to make each product virtually identical to the last = 🡹 consistent quality. • Machines can do dangerous and boring jobs that human workers may be reluctant or unable to do.	▪ Very expensive to buy in the short term (possibly £millions) = short-term damage to profits & cash flow, might need finance / debt such as a bank loan, & might take a long time to break-even. ▪ May need fixing or updating which is expensive. ▪ Break downs could affect productivity / cause 'downtime'. ▪ Machines cannot make individual / hand crafted / personal items. ▪ Replacing humans with machines could give the business a bad brand image / redundancies could lead to strike action. ▪ New skilled workers may need to be recruited. Often, the types of workers needed are in high demand and the business may have to pay them big salaries.

4.2 Quality of goods and services

✪ ***Quality***:

Question	Answer
How can a business ensure it delivers good quality products / services to customers?	❑ Recruit good quality employees – e.g. skilled & experienced workers. ❑ Train workers well. ❑ Provide workers with good quality equipment and machinery. ❑ Use good quality suppliers / materials. ❑ Do random spot checks of finished shoes. ❑ Have a mystery shopper. ❑ Invite customer feedback to find out strengths & weaknesses.
What are the benefits to businesses of giving good quality products / services to customers?	❑ Otherwise, customers will bring the products back and ask for a **refund or replacement**. This will increase the costs of the business (and refunds will reduce the revenue), which will decrease the profits. ❑ The business will build up a good **brand image** which will help to increase sales by attracting new customers and retaining existing ones (**brand loyalty**). ❑ The business will be able to charge **higher prices** for its products. ❑ The employees in the business are likely to be more **motivated** if they are producing good quality products and seeing customers satisfied.
What is a product recall? Can you find a real-life example & add it here?	❑ It's when a business asks customers (or retailers) to return products to the factory because there is a safety issue and customers are at risk. For example, the brakes on a car might be faulty or broken class may have been found in baby food. ❑ A product recall can be very expensive to carry out and very damaging to the brand image. ❑ Current examples can be found on the Trading Standards' website.

✪ Differences between **Quality Control** and **Quality Assurance**:

	Definition	Benefits	Drawbacks
Quality Control (QC)	Quality is checked at the end of the production process. E.g. a Quality Control inspector randomly checks every 10th product before dispatching to customers.	✓ It can help to prevent faulty goods and services being sold. ✓ It is not disruptive to production – workers continue producing, inspectors do the checking ✓ As with any quality system, the business may benefit from an improved reputation for the quality and this may increase sales.	× It does not prevent waste of resources when products are faculty × The process of inspecting the goods or services costs money. E.g the wages paid to inspectors, the cost of testing goods in a laboratory. × It does not encourage all workers to be responsible for quality.

Quality Assurance (QA)	Quality is checked throughout the entire production process, and all workers are responsible for quality (not just a QC) inspector. This is also known as Total Quality Management (TQM).	✓ Quality is checked throughout the entire process, so mistakes are less likely to be made. ✓ Mistakes are found WHEN they are made, rather than at the END – which is a waste of time and resources. ✓ Staff are motivated because they are trusted and have responsibility.	× It may slow down productivity levels if quality is checked throughout. × Staff may require extra training, which can increase the costs of the business. × Staff may ask for higher wage rates since they have more responsibility.

4.3 The sales process and customer service

✪The influence of e-commerce on business activity

Business activity	Explanation
Location	• Thanks to e-commerce, businesses are able to locate almost anywhere. • A business will only need a telephone connection to take orders – referred to as front end of the business. • The warehouse, storing goods, does not have to be in the same place as the office taking the order. Warehouses can be located nearer motorways etc..
New skill development	• A business launching a product or service through e-commerce will need the workforce to have different skills. • E.g maintain website, reply to e-mails, pack goods in warehouses • This jobs may not have been required before e-commerce started. • Extra training may be required for all levels of staff. • Some staff may feel threatened by new technology.
Levels of employment	• An existing business switching some of their business to e-commerce may need fewer staff due to technology being used. • Staff may be made redundant if they do not have the skills to transfer to digital technology.
Creation of specific departments	• Some businesses such as John Lewis, Next etc.. have created an 'on line department' – to make sure that no business is lost to competitors who may be offering a better price or service.
Click & collect	• A problem with having goods delivered at home is that the customer might not be in. • This is solved by the customer ordering online and collecting the goods from a store at a later time. • Many local shops are now being developed as click & collect centres. • Businesses are having to dedicate more space in-store for click and collect customers.
Delivery options	• The speed as which products can be delivered will be increasingly important in the future. • If a business can deliver goods faster than its competitors, then it may attract more customers.

✪ Methods of selling:

Method	Definition,	Advantages	Disadvantages
E-commerce	Selling products online, instead of (or as well as) a physical shop. E.g. Amazon, Tesco, Sports Direct.	▪ **Large potential audience / worldwide** – one website can reach a massive audience (unlike one shop); increasing potential sales and profits. ▪ **Open 24/7/365** - potential sales and profits, as it is more convenient for shoppers (e.g. those working during the day can shop at night). ▪ **Professional image –** a well-designed website can make a business appear professional and improve their brand image. ▪ **Lower fixed costs –** no need to have expensive high street shop / can have an out of town warehouse.	▪ **Increased competition** – although a business can sell to a wider audience, so can its competitors. ▪ **Cost of delivery** – added cost of delivery vans / drivers, or postage / couriers. ▪ **Cost of returns** – 'distance selling regulations' allow customers to return product bought online easier than shops. ▪ **Online security** – the risk of cyber-attack (loss of data / damage to brand image) and the high cost to prevent it. ▪ **Technological advances** – a website designed today may need updating fairly quickly as technology & shopping habits change quickly.
		Advantages to the customer	**Disadvantages to the customer**
		▪ **Price comparison** – easy to compare prices online from a range of shops (without having to visit each one). ▪ **Open 24/7/365** – shop when it's convenient; good for people working during day / busy with children. ▪ **Wide range of products** – shops can only display a limited number of items; websites can offer more choice.	▪ **Lack of personal contact** – might not be able to ask questions about the product before buying. ▪ **Problems returning goods** – how to return / cost of returning? ▪ **Cannot touch / feel products** – important for products such as clothes & shoes. ▪ **Security** – are my personal & banking details safe? Fraud / fake websites. ▪ **Payment methods** – some customer might prefer to pay cash / do not have a debit/credit card, or Paypal. **Technology** – requires a computer & internet connection; not all customers have this
Telesales	**Selling products over the telephone. E.g. Internet service providers, credit cards, double glazing.**	▪ A two-way conversation with the customer; allowing them to ask for advice / discuss the product / negotiate a deal – might help to make an extra sale. ▪ Sales employees can use tactics to persuade customers to buy; thus increase sales revenue.	• Telesales is an industry with high staff turnover, thus has high recruitment & training costs. • Customer still cannot see / feel the product, so only suitable for certain products.

		▪ Can be cheaper to operate a telesales office (out of town) than a high street shop (with high rent).	• Customers may consider it a 'nuisance' phone call, thus giving the business a bad brand image.
Face-to-face	**Selling products in person – such as in a shop, or door-to-door sales. E.g. any high street shop, or door-to-door catalogues.**	▪ Good interaction and relationship with the customer; might help to build up brand loyalty. ▪ Sales employees can persuade customers to buy; thus increase sales revenue. ▪ Can answer specific questions / problems a customer has, and give advice; customer may feel like they have had a better experience / better customer service (than online sales) = good brand image & customer loyalty. ▪ Get immediate feedback from customers; might help a business to identify a problem (e.g. why customers aren't buying a particular product) & improve.	▪ Shops can be more expensive to operate than a website (high cost of high street rent). ▪ Good quality employees cost money to recruit and train (high costs = lower profits / less money available for other areas of the business). ▪ Some customers don't need advice / know exactly what they want, and it's quicker / easier for them to order online. ▪ Some customers might avoid shops that have 'pushy' sales people – e.g. mobile phone shops.

✪ Three methods of providing good **customer service**:

Method	Explanation – what is it, real-life examples, & benefits?
After sales service	Making sure the customer is happy after they have made a purchase; e.g. offering a money back guarantee, refunds when something goes wrong, checking to see the customer is happy. **Argos** offer a 30-day money back guarantee on most items (more than the legal requirement) and will refund delivery charges / collect for free in some cases. This might help attract & retain customers (= 🡅 sales revenue). However, it can be expensive, especially if abused by customers.
Good product knowledge	Being able to give clear and detailed advice to the customer about the product & its specifications. **Dell** have very detailed product specifications on their website, and have an online chat function available for further questions. Again, this can help attract & retain customers (especially for products where there are lots of detailed / technical specifications e.g. cars, computers). However, this can be very expensive to set up and run.
Customer engagement	Developing a good relationship with the customer through polite & helpful communications; these can be in-store, via newsletters, or online (e.g. social media). **Lush** have an online Q&A forum, a chat function, a newsletter, and presence on Facebook, Twitter, YouTube & Instagram. Good customer engagement can make customers feel special and want to return, and can also be useful for gaining quick feedback from customers (e.g. areas where the business can improve). However, additional workers will need to be employed to manage all these platforms. Social media communication can also give the business a bad brand image (e.g. if lots of customers complain on Twitter) and customers may become dissatisfied if they do not get a prompt response.

4.4 Consumer law

✪ Customers are protected by the Consumer Rights Act 2015. This act of parliament gives the customers protection when they buy goods and services which must be:

- Of satisfactory quality
- Fit for purpose
- As described

✪ Main features of the **Consumer Protection Act 2015**:

■ **Goods bought in a shop:** entitled to a full refund if faulty within 30 days; entitled to full refund within 6 months if product can't be repaired or replaced; may be entitled to a partial refund if the product doesn't last a 'reasonable' length of time (up to 6 years).
■ **Goods bought at home (e.g. online or over the phone):** entitled to a 14 day cooling-off period – i.e. can change your mind and get a refund. In addition to this, you have the same rights as when goods are bought in a shop.
■ **Services bought in a shop (e.g. fixing your car / fitting a bath):** entitled to have problems fixed, repaired, or partial refund if the service was not carried out properly first time; carried out in a reasonable time at a reasonable price; 14 day cooling-off period if ordered at home.

✪ Potential consequences to businesses of breaking the **Consumer Protection Act 2015**:
■ **Damage to brand image** – might put off potential customers = ↓ sales revenue & profits.
■ **Legal action / fine** - ↑ costs = ↓ profits.

4.5 Business location

✪ Factors of location and their importance for a business to consider when choosing where to locate their shop / factory:

Factor	Explanation – why is it important to consider?
Cost of rent / land	■ Cheap rent = ↓ costs = ↑ profits ■ Cheap rent = ↓ costs = ↑ budget for other areas of the business e.g. advertising ■ Cheap rent = ↓ costs = ↓ prices = more competitive ■ However, cheap rent might mean the shop / factory is in a poor location e.g. a shop in an area of high unemployment where demand from customers is likely to be low
Proximity to suppliers	■ Having a variety of suppliers nearby means a business can shop around for the best prices & quality stock ■ Having suppliers nearby reduces lead times (delivery time) which ensures the business doesn't run out of stock (which can affect sales for a shop & productivity in a factory) ■ Being near to suppliers is likely to reduce delivery charges
Population size	■ Higher number of potential customers = ↑ potential sales revenue ■ Higher number of potential employees = greater range of people to choose from = likely to get the best person for the job & may be able to offer low wages if large number of unemployed people are desperate for a job.

Proximity to competitors	■ Locating away from competitors means there is less need to spend time & money luring customers away from them e.g. advertising, special offers, price reductions ■ In some cases it can be good to be near competitors e.g. The Jewellery Quarter in Birmingham
Infrastructure (e.g. good transport links)	■ Faster delivery to customers = customer satisfaction & repeat sales ■ Shorter routes = lower transport costs (petrol & driver wages) ■ Faster deliveries from suppliers = reduces lead times (delivery time) which ensures the business doesn't run out of stock (which can affect sales for a shop & productivity in a factory)

4.6 Working with suppliers

✪ What is procurement?

Procurement is the management of purchasing within a business

✪ What is logistics?

Logistics is the management of the transportation and storage of goods.

✪ The four main roles of the **procurement** department in a business?

❶ Identifying goods and service to buy

❷ Choosing suppliers

❸ Ordering goods and services

❹ Receiving deliveries from suppliers

✪ Examples of how the following factors might affect which products / services a business chooses to buy from suppliers (and how many):

Factor	Examples
The time of year (season)	❑ Buy more ice creams / ice lollies to sell in the summer. ❑ Hats & gloves in winter / flip flops & shorts in summer. ❑ Red roses for Valentine's Day. ❑ Spooky costumes & treats for Halloween. ❑ De-icer for cars in the winter
Changes in technology	❑ Streaming music / films, instead of CDs/DVDs. ❑ Voice activated products (Alexa). ❑ New games consoles & VR. ❑ New & improved mobiles. ❑ Smart / fit watches.
Changes in fashion & lifestyle	❑ Fashions in the clothing industry change quickly. ❑ Fads & trends – e.g. fidget spinners. ❑ Healthy eating trends – e.g. veganism, organic, no-carbs. ❑ Ethical trends – e.g. Fair Trade coffee, eco cars. ❑ 'Ready meals' for those on-the-go.

✪ Factors that are important to consider when **choosing which supplier to use**:

Factor	**Explanation – why is this factor important to consider?**
Cost of supplies / stock	■ Cheaper stock = ↓ unit costs = ↑ profit margins OR ■ Cheaper stock = can reduce selling price to be more competitive
Quality of supplies / stock	■ Good quality stock usually results in good quality finished products = more satisfied customers willing to pay higher prices and more likely to return (customer loyalty) / less likely to ask for refunds
Delivery times (lead time)	■ Faster delivery times = less likely to run out of stock = keeps customers happy / maximises sales / keeps production flowing in factories.
Minimum order size	■ If the minimum order size is too large (e.g. must buy at least 1,000 units) then a) a large storage space is needed which increases costs, b) cash flow is damaged and may leave a shortage for other areas of the business, and c) if fashions or tastes change then the business may be left with a lot of unsold / wasted stock.
Customer service & reliability	■ If and when things go wrong, it is important that a suppliers puts it right quickly. E.g. if the wrong number or type of products are delivered to a shop, they will want the supplier to deal with this problem quickly so that it doesn't affect their sales & brand image.

Section 5: Finance

Topic
- Content
  - ✓ *Points to include*

5.1 The role of the finance function
- The purpose of the finance function
  - ✓ *provide financial information, support business planning and decision making*
- The influence of the finance function on business activity

5.2 Sources of finance
- The reasons businesses need finance
  - ✓ *establishing a new business, funding expansion, to run the business recruitment, marketing*
- Ways of raising finance
  - ✓ *loan, overdraft, trade credit, retained profit, sale of assets, owners' capital, new partner, share issue, crowdfunding*
- How and why different sources of finance are suitable for new and established businesses

5.3 Revenue, costs, profit and loss
- The concept of revenue, costs and profit and loss in business and their importance in business decision-making
- The different costs in operating a business
  - ✓ *fixed, variable, total*
- Calculation of costs and revenue
- Calculation of profit/loss
  - ✓ *gross profit, net profit*
- Calculation and interpretation of profitability ratios
  - ✓ *gross profit margin, net profit margin*
- Calculation and interpretation of average rate of return

5.4 Break-even
- The concept of break-even
  - ✓ *total costs = total revenue*
- Simple calculation of break-even quantity
- The usefulness of break-even in business decision-making
  - ✓ *informs marketing and planning decisions*

5.5 Cash and cash flow
- The importance of cash to a business
  - ✓ *providing liquidity, enables business to meet short-term debts/expenses*
- The difference between cash and profit
- The usefulness of cash flow forecasting to a business
  - ✓ *planning tool, anticipates periods of cash shortage, enables remedies to be put in place for shortages, provides targets*
- Completion of cash flow forecasts

5.1 The role of the finance function

✪ The **role of the finance department** includes…

- Identifying and acquiring sources of finance (e.g. bank loans and grants).
- Setting and monitoring budgets for spending in each department (e.g. Marketing, HR, and Production).
- Reporting on the profitability of the business.
- Providing financial information to management, to help with business planning and decision making (e.g. how to be more profitable, whether a potential investment is worthwhile, and how to overcome a cash flow problem).

5.2 Sources of finance

✪ Internal **sources of finance**

Source of Finance (Internal)	Definition	Advantages	Disadvantages
Owner's capital	The owner of a business may put some of their own savings in to help start / grow a business.	✓ It is available immediately. ✓ No need to ask anyone, pay it back/get into debt, or pay interest.	× Unlikely to be enough, so other sources of finance still needed. × A big risk – might lose life savings.
Retained profit	A business may use profits it has made in the past to pay for future expenses.	✓ It is available immediately. ✓ No need to ask anyone, pay it back/get into debt, or pay interest.	× Only available to existing businesses (new businesses haven't made a profit yet). × Shareholders might prefer the short term reward of higher dividends, rather than profits being re-invested.
Sale of assets	A business might be able to sell an asset such as a building, machine or vehicle in order to raise finance.	✓ If the asset is no longer being used, it makes sense to turn it into cash for future projects.	× Depreciation – a second hand van will only be worth a fraction of what it originally cost the business to buy. × It might be time consuming to find a buyer (e.g. for a building) or very difficult (e.g. a machine that only makes a specific type of product).

External sources of finance

Source of Finance (External)	Definition		
Bank loan	A lump sum of money borrowed from a bank, and then repaid over a period of time in affordable monthly payments.	✓ A large sum can be borrowed in a relatively short amount of time (might take a few weeks). ✓ Repayments can be spread out over 3-5 years in affordable chunks. ✓ The bank may be able to offer business advice in addition to the money (good for new / inexperienced entrepreneurs).	× The money has to be repaid with interest added on top; the current rate of interest is important to consider here. × The bank might ask for 'security' on the loan – e.g. if you can't pay back the money, we'll take your house / business assets.
Overdraft	This is where a bank allows a business to go below £0 in its bank account.	✓ This can be used to cover short term cash flow problems; e.g. allows a business to pay day-to-day expenses such as bills, wages and buying stock, thus allowing it to keep trading. ✓ Although the interest rate is likely to be higher than a bank loan (e.g. 15% vs 5%), the total amount of interest repaid might be small since it is only needed for a short period of time.	× If used for prolonged periods, the amount of interest repaid can add up to be a lot of money. × Unlike a bank loan (where a timeframe has been agreed; e.g. pay back over 2 years), the bank can insist that an overdraft is paid back straight away.
Take on a new partner	A partnership can have between 2-20 owners; taking on a new partner is a way to raise finance as they may be willing to invest in the business.	✓ The money raised does not have to be repaid with interest, like a bank loan. ✓ As well as investing money into the business, the new partner might bring new skills and ideas to the business.	× The new partner will be entitled to a share of the profits (meaning that each partner might initially get a smaller amount than before, until the business has had a chance to grow and make more profit). × The new partner will want a say in how the business is run, and there could be disagreements about this.
Share issue	A business can sell shares to shareholders; i.e. investors put money into a business to	✓ The money raised does not have to be repaid with interest, like a bank loan. ✓ A large sum of money can be raised, especially in a plc.	× Some of the profit made is usually given to shareholders in the form of dividends (so reduces the amount that can be

	become part-owners of the business. Shareholders are rewarded with a dividend (a % share of the profit, based on how many shares they have). Private Limited Companies (Ltd) sell shares privately to friends & family, Public Limited Companies (plc) sell shares to anyone in the world on the Stock Exchange.		reinvested back into the business). × Major shareholders will expect to have a say in how the business is run. × In Public Limited Companies (plc) the business may be taken over if someone buys up 51% or more of the shares.
Crowd funding	Money raised from 'sponsors' or 'donors', often through crowdfunding websites.	✓ An alternative for businesses who have been turned down for a loan by a bank. ✓ Can potentially raise a large sum of money.	× Profits need to be shared with sponsors / donors. × Can take a long time to raise the finance (compared to a bank loan).
Trade credit	This is when a supplier allows a business to receive goods / stock now, and then pay for it later (e.g. after 30-60 days).	✓ Give the business time to sell the goods / stock, and then use the income from sales to pay the supplier; thus improves 'cash-flow'.	× May not be available to new businesses that have no positive track-record / history. × The supplier must still be paid even if the goods aren't sold. The business might lose out on a discount that they would have got if they paid up front in cash

5.3 Revenue, costs, profit and loss

✪ Costs

Costs are **payments** that a business makes in order to make goods and provide service. E.g
Wages, raw materials/stock, rent, interest on loans, salaries, insurance etc…
Costs can be classified under two headings: Fixed & variable

	Definition	Examples	Formula
Fixed costs	Fixed costs are costs that do not change with output. Output is the number of units produced.	Rent Rates Wages/salaries Insurance Interest on a bank loan	
Variable costs	Variable costs are costs that do change when the business changes the amount it produces.	Stock/Direct materials Direct labour	Total variable costs = **Variable cost per unit X Output**. Note: the output is the number of units they are or hoping to produce.
Total costs	The total costs of a business are found by adding together the total for all fixed & variable costs		Total costs = **Fixed costs + Total variable costs**

✪ Costs and decision making

Fixed costs

- If a business has high fixed costs, then it must sell a high number of products or services to cover the fixed costs.
- If a decision is made to move to a larger factory which higher fixed costs, such as rent, then the business must make sure that it can sell an increased number of products to cover those higher fixed costs. If not, then revenue and profit will fall.

Variable costs

- Variable costs also need to be carefully analysed.
- The cost of the materials that a business needs might increase. If this happens a business could decide to:
    - Accept the price increase and look for savings elsewhere
    - Look to buy from a different supplier – depend on quality
    - Negotiate with current supplier on a reduction in price.

✪ Revenue

	Definition	Formula
Revenue	Revenue is income coming into a business from the sale of products and services.	Revenue = Selling price per unit X Output/quantity sold

✪ Revenue and decision making

- Should a business increase or decrease their price?
- Depends on the effect on demand

Example:

	Selling price	X	Output	=	Revenue
Current	£25	X	2,000	=	£50,000
If the price is raised to £30	£30	X	1,800	=	£54,000
If the price is reduced to £20	£20	X	2,100	=	£42,000

- In the example above the business should increase their price as it generates an extra £4,000 in revenue. (revenue has increased from £50,000 to £54,000)
- Even though less people want the toasters, (demand has decreased by 200) the revenue is higher.

✪ Factors that can affect revenue due to price changes

The number of competitors	• If there are no competitors = increase price without revenue falling • If there are a lot of competitors, sales might fall as consumers switch to buying from another business.
The action of competitors	• If competitors raise their prices, there is an opportunity for a business to raise their prices without the fear of losing customers. As a result revenue should increase.
The starting price of the product	• If the product/service is already very cheap, an increase in price might not affect consumers too much and revenues might still rise.

✪ How a business can increase revenue

- Increasing sales
    - Expand – open more shops
    - Advertising
- Increasing product range

✪ Profit and loss

- A business makes a loss when it costs (money going out of the business) are greater tha revenue (money coming into the business)
- Profit is the money that is left over from revenue once the costs of operating the business has been paid.

✪ Basic calculations of profit & loss

Basic profit/loss formula: **Revenue – total costs = Profit**

	Revenue	**-**	**Total costs**	**=**	**Profit/loss**
Example 1	£100,000	-	£60,000	=	£40,000 Profit
Example 2	£80,000	-	£100,000	=	(£20,000) Loss

✪ There are two types of profit:

- Gross profit
- Net Profit

✪ Gross Profit

- Gross profit is the amount of profit made by a business as a result of buying and selling goods or services, but without paying for any of the day – to –day or other expenses of running the business.
- It is the profit on trading
- Only deducts one cost from the Revenue and that is the cost of goods sold (The cost of the stock – only for the units that have been sold).

✪ Gross profit formulas

	Formula
Gross Profit	Revenue – cost of sales
Gross profit margin ratio	Gross profit / Revenue X 100. Note: this symbol '/' means you divide the gross profit figure by the revenue figure

✪ Examples of the calculations of net profit and the net profit margin.

Example 1: Hats Ltd	
	£
Revenue	200,000
Cost of sales	80,000
Gross Profit	**120,000**
Gross profit margin ratio	120,000
	200,000
=	0.60
X 100 =	**60%**

Example 2: Chairs Ltd	
	£
Revenue	50,000
Cost of sales	10,000
Gross Profit	**40,000**
Gross profit margin ratio	40,000
	50,000
=	**0.80**
X 100 =	**80%**

Example 3: Stools plc	
	£
Revenue	100,000
Cost of sales	60,000
Gross Profit	**40,000**
Gross profit margin ratio	40,000
	100,000
=	0.40
X 100 =	**40%**

✪ What could Businesses such as Stools plc do to improve their **gross profit**?

- **They could try to increase sales revenue, by using special offers or advertising more.**
  - Special offers such as BOGOF and 20% off might result in a higher number of sales, but at a lower value (revenue).
  - Increased advertising might increase sales revenue, but result in higher costs (thus might reduce net profit).
- **They could reduce the cost of sales by using cheaper quality materials.**
  - This might reduce the quality of stools made, so damage the brand image / customer loyalty.
  - This might reduce the quality of stools made, so the selling price needs to be reduced.

✪ Interpreting the Gross profit margin

- When analysing ratios a business must calculate the gross profit margin for at least two years

Example: How has Jacquelyn Williams booksellers performed?

	Year 1 (£)	Year 2 (£)
Revenue	150,000	225,000
Cost of sales	80,000	140,000
Gross Profit	70,000	85,000
Gross profit margin	46.7% (70,000/150,000)X100	37.8% (85,000/225,000)X100

Notes:

- You would naturally thing that Yr2 was better in regards to performance.
- Sales increased by £75,000 and Gross Profit increased by £15,000

However…..

- Gross profit margin decreased by 8.9%
- This would indicate that while sales have increased, the business is paying more than it did in year 1 for the books it is selling.
- As you sell more books, you would expect the the cost of sales to increase, however you would expect the % of cost of sales to revenue to stay the same or actually decrease.
- In Yr1 the stock was 47% of the revenue, whilst in Yr2 the stock was 62% of the revenue. (Cost of sales / revenue X 100)
- The cost of the stock should remain constant – the same % or decrease the more they buy due to economies of scale.
- The business will need to action such as:
    - Buy books from a different supplier but ……
    - Ask it present supplier for more of a discount

✪ Net profit

- Net profit takes into account the profit made as a result of buying and selling goods or services but also makes an allowance for the costs involved in running the business – for example, wages, rent etc…
- It is seen as a more accurate reflection of the performance of a business

✪ Net profit formulas

	Formula
Net Profit	Gross profit – expenses (the costs of running the business – the fixed costs)
Gross profit margin ratio	Net profit / Revenue X 100. Note: this symbol '/' means you divide the net profit figure by the revenue figure

✪ Examples of the calculations of net profit and the net profit margin.

Hats Ltd	
	£
Revenue	200,000
Cost of sales	80,000
Gross Profit	**120,000**
Rent	20,000
Salaries	40,000
Bills	20,000
Advertising	10,000
Net Profit	**30,000**
Net profit margin ratio	30,000
	200,000
=	0.15
X 100 =	**15%**

Chairs Ltd	
	£
Revenue	50,000
Cost of sales	10,000
Gross Profit	**40,000**
Rent	10,000
Salaries	10,000
Bills	5,000
Distribution	**5,000**
Net Profit	**10,000**
Net profit margin ratio	10,000
	50,000
=	0.20
X 100 =	**20%**

Stools plc	
	£
Revenue	100,000
Cost of sales	**60,000**
Gross Profit	**40,000**
Rent & bills	10,000
Wage/salaries	10,000
Staff training	20,000
Advertising	20,000
Net Profit	**(20,000)**
Net profit margin ratio	(20,000)
	100,000
=	(0.20)
X 100 =	**(20)%**

Notes:

- Stools plc made a loss as their net profit was (£20,000).
- Brackets in Accounting = a minus figure.
- As their net profit was a loss/minus figure – the net profit margin HAS to be a minus

✪ What could Stools plc do to improve their **net profit**?

- **They could reduce the number of workers (make redundancies):**
  - They might struggle to meet demand from customers.
  - There would be a short term increase in costs (redundancy pay).
- **They could reduce the amount spent on staff training.**
  - This might reduce the quality of stools made.
  - This might reduce the quality of customer service given.
- **They could reduce the amount spent on advertising.**
  - This might reduce costs, at the expense of lower sales (revenue).

✪ Interpreting the Net profit margin

- When analysing ratios a business must calculate the Net profit margin for at least two years

Example: How has Jacquelyn Williams booksellers performed?

	Year 1 (£)	**Year 2 (£)**
Revenue	150,000	225,000
Cost of sales	80,000	140,000
Gross Profit	70,000	85,000
Business expenses	40,000	55,000
Net profit	30,000	30,000
Gross profit margin	20% (30,000/150,000)X100	13.3% (85,000/225,000)X100

Notes:

- Although sales and gross profit (not the margin) has increased, Net profit has stayed the same.
- This is because the business are not controlling their expenses (fixed costs) effectively)
- As sales has increased you would think that it was natural for some of the fixed costs to increase e.g they may need to employ more staff.
- Again the same as cost of sales, the % of expenses to gross profit should stay the same or decrease from one year to the next. This is because fixed costs would be spread across more units.
- However, in Yr1 expenses was 57% of the revenue and in Yr2 it was 65% of the gross profit.
- The reduction is the net profit margin is because the expenses have increased by 37.5% ((difference/original X 100) – The difference in expenses is 15,000 and the original expenses figure was 40,000.
- Action would be required to cut down on expenses such as wages, heating, lighting and insurance etc…

✪ What is it important for businesses to make a **profit**?

- To reward investors; e.g. s share of profits for the owner/partners, or dividends for shareholders.
- To use for future improvement & expansion of the business (using retained profit).

✪ Average rate of return

- Is a method of measuring and comparing the **profitability** of an investment over the life of the investment.
- The phrase 'rate of return' is the amount you receive from making an investment

✪ The three steps in calculating the **Average Rate of Return (ARR)**

Step 1	Calculate the total profit of the investment (Total Income – Initial Investment).
Step 2	Calculate the average profit per year (Total Profit ÷ no. of years).
Step 3	Calculate the size of the average profit per year as a proportion of the original investment ((Average profit per year ÷ initial investment) x 100)

✪ Example of calculating the **Average Rate of Return (ARR)**

Initial Investment	**(£50,000)**
Income Year 1	£20,000
Income Year 2	£40,000
Income Year 3	£50,000

Step 1	£110,000 - £50,000 = £60,000 profit
Step 2	£60,000 ÷ 3 years = £20,000 profit per year (on average)
Step 3	(£20,000 ÷ £50,000) x 100 = 40%
Final Answer	**40% ARR**

✪ Interpreting **Average Rate of Return (ARR)**

- Average rate of return is useful when comparing different investments
- Generally the business would choose the investment which generates the higher return e.g the one that has the highest ARR.
- A business might also look at what else it might do with its money. E.g. interest received from a bank.
- It is a prediction, many things can change and events may not turn out as planned.

5.4 Break-even

✪ Break-even number of units

- Break-even is the number of units a business needs to produce when they are not not making a profit nor a loss
- The revenue figure is exactly the same as the total cost figure. TR = TC
- The amount received from revenue just covers the costs of the business.

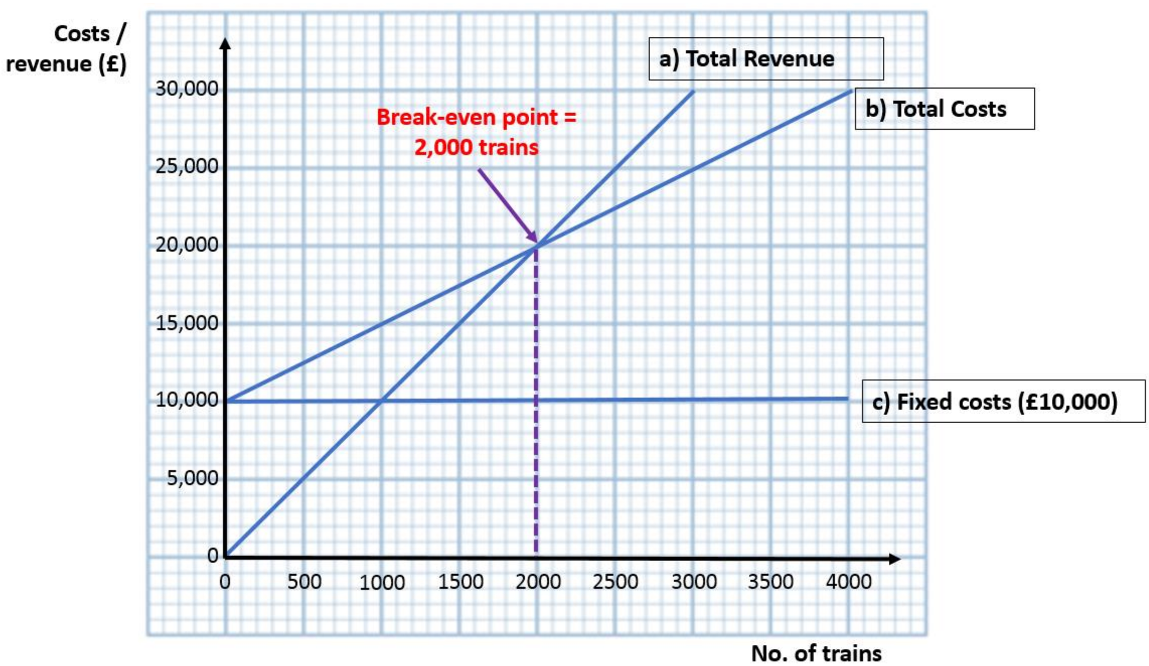
Example: A small factory that makes wooden toys such as trains.

- ❖ You sell each train for £10.
- ❖ Each train costs you £5 to make in materials (e.g. wood).
- ❖ The fixed costs for the factory are £10,000 per month.

Output	Fixed costs	Total variable costs	Total costs	Total Revenue	Profit
		Variable cost per unit X Output	Fixed costs + Total variable costs	Selling price X output	**TR - TC**
0	10,000	5x0 = £0	10,000+0 =10,000	10x0 = £0	0-10,000= (10,000)
500	10,000	5x500 =2,500	10,000+2,500 = 12,500	10x500 =5,000	5,000-12,500 = (7,500)
1,000	10,000	5x1,000 =5,000	10,000+5,000 =15,000	10x1,000 =10,000	10,000-15,000=(5,000)
1,500	10,000	5x1,500 =7,500	10,000+7,500 =17,500	10x1,500 =15,000	15,000-17,500=(2,500)
2,000	**10,000**	**5x2,000 =10,000**	**10,000+10,000 =20,000**	**10x2,000 =20,000**	**20,000-20,000 = 0**
2,500	10,000	5x2,500 =12,500	10,000+12,500 =22,500	10x2,500 =25,000	25,000-22,500= 2,500
3,000	10,000	5x3,000 =15,000	10,000+15,000 =25,000	10x3,000 =30,000	30,000-25,000= 5,000

- As you can see from the table above when the business is producing 2,000 units the total revenue and figure and the total costs figure is £20,000.
- At this point the business is not making a profit nor a loss, the profit/loss is £0

✪ Break even chart



✪ Imagine your business is currently selling **3,000 trains** per month:

- ❑ How much **profit / loss** is being made?
- Total Revenue = £30,000
- Total Costs = £25,000
- **Profit = £5,000**

✪ What is the **margin of safety**?

- Margin of Safety = Current level of sales – break-even point
- Margin of Safety = 3,000 – 2,000
- **Margin of Safety = 1,000 trains per month**

✪ Break-even formula:

$$\frac{\text{Fixed costs}}{\text{Selling price per unit} - \text{variable cost per unit}}$$

✪ Usefulness of break-even analysis in business decision making

- The figures in the forecast will help the business to plan how much to sell in order to make a profit.
- If a person needs a loan from a bank, the bank manager will often ask to see a break-even graph as part of a business plan.
- The forecast can be used to make judgements about prices and costs. The figures may show a need either to increase the price of the product, to raise revenue, or to reduce the costs.
- Help decide whether the business is viable – will be a success. The potential demand is compared to the break-even units. If the demand is lower than the break-even units, the idea is not viable and will not be a success.
- It can show the margin of safety. The business can assess the impact of any external changes on the number of units a business will make profit on.

✪ Identify and explain **two limitations** of using break-even charts / analysis:

- It assumes that all products are sold for the same price. In reality, a business might sell to one customer for £10 per train, but be willing to give a discount to customers who buy in bulk; thus making it cheaper per unit (e.g. £9 per train).
- Business costs can change, which in turn will affect the break-even point. For example, the rent on the shop/factory or costs from suppliers might go up, causing the break-even point to rise.
- It assumes if price increased, total revenue will increase. However the normal rule is, if price increases, demand falls = decrease in revenue.
- Does not account for economies of scale. Assumes the variable cost per unit stays the same regardless of how many units are bought at one time. Generally as output increases the variable cost per unit falls.

5.5 Cash and cash flow

✪ The **importance of cash** to a business (or the consequences of not having enough):

Cash is essential for a business to keep trading / operating.
Without enough cash available to pay for day-to-day expenses, a business might not be able to:

- Pay its workers; therefore they refuse to come to work = the business is unable to make / sell any goods or services.
- Pay suppliers for stock; therefore the business cannot but any new stock to sell to generate income.
- Pay bills (rent, electricity, phone bill, etc.); therefore the business might not be able to stay in the premises or use electrical items / the phone.

Any one of these things could cause the business to fail.

✪ What is the difference between **cash** and **profit**?

Cash	Cash refers to the money a business has available at a given point in time (e.g. today), that can be used to pay day-to-day expenses such as rent, wages and stock.
Profit	Profit is calculated over a time period (e.g. a month or a year) by taking total costs away from total revenue for that time period.

✪ Explain the **benefits** to a business of creating a cash flow forecast:

✓ It may be required when asking the bank for a loan (the bank will want to see projected cash inflows & outflows to determine if the business is likely to be able to repay the loan).

✓ To identify periods when there might be a shortage of cash available to pay for the day-to-day running of the business. Identifying this in advance of the problem actually occurring is good, so that the business can:
  - Plan ways to increase cash inflows before the problem occurs.
  - Plan ways to decrease cash outflows before the problem occurs.
  - Identify when sources of finance such as an overdraft or trade credit might be needed in the future.

✓ To see if a project is realistic / viable before going ahead with it.

✪ Cash inflows:

Cash inflows are monies coming into the business:

- Cash & Credit sales
- Receipt of a bank loan
- Receipts of share capital
- Rent received

✪ Cash outflows:

Cash outflows are monies coming out of the business:

- Rent
- Wages/salaries
- Insurance
- Interest on loan
- Loan repayments
- Purchases of assets e.g equipment/vehicles …
- Stock/raw materials

✪ Formulas:

Total cash inflows	Add up all the cash inflows
Total cash outflows	Add up all the cash outflows
Net cash flow	Total cash inflows – total cash outflows
Closing cash balance	Opening cash balance + Net cash flow
Opening cash balance	The 1st month will be given for the rest it is the previous months closing balance.

✪ Example of a cash flow forecast:

	Jan	Feb	Mar
Cash Inflows	£80,000	£100,000	£120,000
Cash Outflows	£100,000	£80,000	£70,000
Net cash flow	-£20,000	£20,000	£50,000
Opening cash balance	£10,000	-£10,000	£10,000
Closing cash balance	-£10,000	£10,000	£60,000

✪ Understanding the figures in a cash flow forecast

- If the closing cash balance is a minus figure, this means the business has a cash deficit.
- A cash deficit is when the business is predicting they will not have enough cash to pay their day to day expenses.
- As it is a prediction, the business will have time to organise an overdraft, trade credit etc…
- Particularly when a business is setting up, it is normally to have a deficit as they will have start-ups costs, and high advertising costs. These will reduce as the months go on.
- Also, sales will be low to begin with until the business becomes more well known.

✪ Disadvantages of a cash flow forecast

- It is only a prediction – sales may prove lower than expected
- Customers do not pay on time
- The cost of raw materials prove higher than expected
- Certain costs are not included.

Section 6: Influences on business

Topic ▪ Content ✓ *Points to include*	Red ☹	Amber 😐	Green ☺
6.1 Ethical and environmental considerations ▪ Ethical considerations and their impact on businesses ✓ *treatment of workers/suppliers/customers, sourcing of materials, marketing decisions* ▪ Environmental considerations and their impact on businesses ✓ *sustainability, waste disposal, pollution, climate change*			
6.2 The economic climate ▪ The economic climate and its impact on businesses ✓ *changing levels of consumer income and unemployment*			
6.3 Globalisation ▪ The concept of globalisation ▪ The impact of globalisation on businesses ✓ *the growth of multinational companies, influences on business location, international branding, how businesses compete internationally*			

Section 7: The interdependent nature of business

Topic ▪ Content ✓ *Points to include*	Red ☹	Amber 😐	Green ☺
▪ the interdependent nature of business operations, finance, marketing and human resources within a business context ▪ how these interdependencies underpin business decision making ▪ the impact of risk and reward on business activity ▪ the use of financial information in measuring and understanding business performance and decision making.			

6.1 Ethical and environmental considerations

✪ **Business ethics**:

Ethics focuses on what is the right or wrong thing to do. What is morally right.

	Examples of ETHICAL / UNETHICAL practice?	Benefits of being ETHICAL	Drawbacks of being ETHICAL
Treatment of workers	▪ Paying fair / decent wages – not just the Minimum Wage (legal vs ethical?) ▪ Health & safety – keeping workers safe ▪ Work-life balance – too many hours vs not enough (zero-hour contracts?) ▪ Perks and benefits – e.g. staff discount & health insurance ▪ Discrimination; e.g. age, race & gender	✓ Recruitment – easier to attract good quality employees ✓ Retention – easier to keep good employees / ↓ labour turnover ✓ Motivation – staff want to work harder/longer/fewer absences	× Costs (for good pay, training, safety & perks) = a) ↓ profits, or b) ↑ prices for customers, or c) ↓ budgets in other areas of the business e.g. Marketing.
Treatment of suppliers	▪ Paying suppliers on time / delaying payment ▪ Paying a 'fair' price – large businesses might abuse their size & power over small suppliers to get very low prices ▪ Charging suppliers for shelf space ▪ Unfair penalties & fines to suppliers	✓ Develop a good relationship with suppliers = might get lower prices, faster deliveries, better payment terms (e.g. 60 days credit) ✓ Develop a good brand image – poor treatment of suppliers can be reported in the news	× costs to pay a 'fair' price = ↓ profits, or ↑ prices for customers × Cash flow problems – might not have enough spare cash if you've paid the supplier promptly
Treatment of customers	▪ Charging fair prices for satisfactory quality products / service. ▪ Price fixing – collusion with competitors ▪ Ensuring customer safety – prompt product recalls where needed ▪ Prompt deliveries ▪ Deal with problems quickly & fairly	✓ Customer satisfaction = brand loyalty = repeat customers ↑ sales revenue ✓ Good brand image = attracts new customers = ↑ sales revenue	× Higher costs (to ensure safety, prompt deliveries, and good customer service) = ↓ profit

Sourcing of materials	▪ Using sustainable materials – e.g. cod, wood ▪ Human rights abuses ▪ Fairtrade	✓ Good brand image = attract & retain customers = 🡅 revenue ✓ Unique Selling Point (USP) = stand out from competitors ✓ Some customers may be willing to pay more = 🡅 revenue (but not necessarily more profit, as costs also likely to be higher)	× Cost of materials likely to be higher
Marketing decisions	▪ Misleading customers about prices & special offers ▪ Claiming health benefits that don't exist / haven't been proven ▪ Targeting children in advertising ▪ The <u>Advertising Standards Authority</u> oversees advertising in the UK to make sure it is done fairly.	✓ Good brand image = attract & retain customers = 🡅 revenue	× Might not be able to persuade as many people to buy products / services if you cannot mislead / exaggerate = 🡇 revenue

✪ Examples of how businesses can use **'sustainable' production methods**, and explain the benefits / drawbacks of doing this:

■ Renewable energy – e.g. solar & wind energy
■ Switching off lights / not leaving devices on standby
■ Turn waste products into something useful
■ Avoid printing if possible
■ Reducing the effects of transportation – fuel efficient vehicles / buy from local suppliers

<u>Benefits:</u>
✓ Improved brand image which might help the business to stand out from competitors & attract customers = 🡅 Revenue.
✓ Reduced costs (e.g. switching off lights saves electricity & less printing saves ink & paper) = 🡅 Profits.
✓ Government support – governments tend to set higher taxes on 'unsustainable' activities; e.g. sending rubbish to landfill, and using vehicles with high CO_2 emissions. 🡇 Taxes = 🡅 Profits.

<u>Drawbacks:</u>
× Increased costs: 'sustainable' raw materials likely to cost more (e.g. sustainable cod & wood, recycled paper, FairTrade coffee).

✗ High short-term / capital costs – e.g. even though solar energy might reduce energy costs in the long-term, the cost of installing solar panels in the short-term is very high; might take years to 'pay back' the investment. Same with fuel efficient vehicles.

6.2 The economic climate

✪ Identify the main features of an '**economic recession**':

■ Jobs are lost, so unemployment rises.
■ As unemployment rises, average incomes fall.
■ As average incomes fall, total spending in the economy falls (& GDP falls – total output).
■ As spending falls, business profits fall, so they need to cut costs, and the cycle starts again (jobs are lost).

The cycle is made worse by a lack of confidence (households save instead of spend because they fear losing their jobs & businesses delay new projects fearing a lack of consumer demand).

✪ Explain how businesses might be affected during a recession:

Winners / losers? Effects on HR, Marketing, Operations & Finance?

✓ Businesses that sell basic needs (e.g. basic food items) might not suffer, as consumers need to keep buying these things.
✓ Businesses that operate at the cheaper end of the market might not suffer / might even do better as consumers switch to cheaper options – e.g. switching from Tesco to Aldi.

✗ Businesses that sell large, expensive, luxury items are likely to suffer from a fall in demand, therefore a fall in sales revenue; when average incomes fall, households will continue to buy basic food items, but will cut back on luxuries such as a new car.

■ **Human Resources** – might need to freeze wages, stop bonuses, make redundancies, and cut money spent on training.

■ **Marketing** – might need to reduce prices, use special offers, and change the product range (more low-end / cheap products & fewer high-end / expensive products).

■ **Operations** – look for cheaper suppliers, or replace workers with technology (e.g. self-service tills).

■ **Finance** – cut budgets for departments in the business, and look to change loans / overdrafts onto lower rates.

NB. All of the suggestions above have <u>consequences</u>.

✪ The impact of changes in income

- Rising income often leads to increased sales for a business (normal goods), increasing revenue and the profits.
- Customers have more disposable income to spend and so want to buy more goods.
- Businesses will want to increase the amount they sell.
- They may need to employ more workers, buy more stock and even build or extend a factory.
- However, rising incomes can sometimes lead to falling sales, revenues and profits. (Inferior goods)
- This can happen when the customers feel that they can now afford more expensive and better products.

✪ How much a business will be affected by a change in income will be influenced by:

- How much the income changes – the bigger the chance in income, the bigger the effect on the business.
- The type of product the business sells. Expensive products will be affected, more by a decrease in income.
- How other businesses respond to the change in income
- How the business itself responds to the change in income.

✪ The impact of changes in employment

- If employment in the economy is rising, it is likely to mean that incomes are also rising.
- If employment is falling, incomes are likely to fall.
- Changes in employment can also affect production and costs.
- If employment rises in the UK, unemployment may fall.
- Firms wanting to hire more workers may struggle to employ enough workers or to find workers with the right skills as there may be a shortage.
- This causes competition for workers and businesses may have to offer higher pay to get the workers they need.
- This may increase the costs of production and reduce the profits of the business.
- It may also mean that businesses simply cannot get the labour they need to expand production.

✪ How much a business is affected by a change in employment is influenced by:

- How much employment changes
- The change in the type of employment. Rise is demand for skilled workers may be more difficult to deal with than a rise in the demand for unskilled workers.

6.3 Globalisation

✪ What is **globalisation**?

Globalisation refers to the increased movement of goods, services, labour and capital around the world as countries become more dependent on each other.

✪ Why has it occurred?

❶	Improvements in transport
❷	Improvements in technology & communication
❸	Free trade agreements (EU, NAFTA, WTO)

✪ What are the benefits and drawbacks of globalisation to **UK businesses**?

■ **Lower costs** - e.g. cheaper labour, land, rent & energy costs. Possibly lower taxes too (e.g. corporation tax). ■ **Expertise** - e.g. access to skilled / trained / experienced workers in industries that might not exist in the UK. ■ **Demand** – greater number of potential customers (population: UK 70m vs World 7bn). ■ **Spread risk** – if sales are lost in one country (e.g. because of recession), then a business can rely on sales from other countries as a back-up.	■ **Communication** – foreign languages might result in miscommunication (e.g. incorrect orders) & higher costs (e.g. new packaging & adverts). ■ **Transport** – potential of higher transport costs and longer lead times if products are made abroad, to be sold back in UK. ■ **Brand image** – reputation might be damaged for making UK workers redundant, using cheap foreign labour, damaging the environment. ■ **Cultural & legal issues** – products, adverts, and HR policies might need to be changed due to foreign laws / trends / culture.

✪ Identify how a change in **exchange rates** might affect UK businesses that import / export:

Strong

Pound

Imports

Cheap

Exports

Dear (Expensive)

So, when the Pound is strong:

■ It is cheaper to import stock / raw materials from suppliers abroad: ↓ costs ↑ profits.
■ It is more expensive for foreigners to buy goods from the UK: ↓ sales revenue for UK businesses that export (e.g. Jaguar car sales to the USA).

When the Pound is weak:

■ It is more expensive to import stock / raw materials from suppliers abroad: ↑ costs ↓ profits.
■ It is cheaper for foreigners to buy goods from the UK: ↑ sales revenue.

7. The interdependent nature of business

✪ Imagine that a business wants to start manufacturing and selling a new product (e.g. scooters).

Give examples what needs to be done in each of the main functional areas (thus showing how the functions are **interdependent** on each other):

Marketing	■ Market Research into customer preferences & competitors ■ Product – designing the product to suit customer needs ■ Price – setting the right price after considering the 3Cs (cost, competitors, customer) ■ Place – choosing the best channel of distribution; e.g. selling direct to customers vs via retailers ■ Promotion – choosing how best to advertise the product & any point of sale promotions (e.g. price reductions)
Human Resources	■ Recruiting new workers (e.g. to produce a new model of scooter to be launched by the Marketing department) ■ Training workers (induction / on / off the job) ■ Motivating workers (financial & non-financial methods)
Operations	■ Procurement – e.g. finding suppliers for the parts for the new scooter & ordering the correct amount ■ Choosing the best production method – job, batch or flow ■ Ensuring the products are made to a high quality standard
Finance	■ Finding sources of finance to make the new scooter – e.g. retained profits, bank loan, trade credit from suppliers ■ Using break-even to set sales targets for the Marketing department ■ Creating a cash flow forecast to predict & plan for possible cash flow problems

✪ Businesses are reliant on other businesses (interdependent).

Primary *Businesses that take raw materials from the earth*	**Secondary** *Businesses that make / manufacture products*	**Tertiary** *Businesses that sell products / offer a service*
A fishing businesses	Bird's Eye fish fingers	Tesco (sells fish fingers)
A cow farmer A gold mine A cotton farm A tree farm	A burger manufacturer A jewellery manufacturer A T-shirt factory A paper manufacturer	McDonald's H. Samuel Next WH Smith