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GCSE Business Studies

Edxcel Unit 3:

Building a Business

Q&A

Rapid Revision Handbook

- ☑ Step by step guide to key concepts
- ☑ Question and Answer format
- ☑ Glossary

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2011 Edition

tutor2u GCSE Edexcel Unit 3 Building a Business Contents

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Marketing

Marketing and Market research

What is marketing? Marketing involves identifying, understanding and satisfying customer needs profitably. Firms find out what customers want and provide matching products

Why is marketing important? Firms survive by identifying customer requirements and then making products customers need - profitably

How can firms identify customer needs? Firms use market research to find out what customers want from products

How can firms understand customer needs? Firms use the results of market research to identify customer requirements for products eg the desired functions of a mobile phone

How can firms satisfy customer needs? Successful firms create products with the features functions and appearance that meet or even exceed customer requirements

How can firms satisfy customer needs profitably? Firms need to make items that meet customer requirements that sell at a price that more than covers cost.

Give an example of satisfying customer needs profitably. The Apple iPad both meets the requirements of customers and sells at a price that more than covers expenses of production.

Is marketing another name for selling? Firms can only sell if they create products that meet customer needs. This requires a good understanding of what customers want from items

What is market research? Market research is the process of finding information about potential customers, markets and products.

Why do market research? Market research helps a business gather data that better helps them understand their customers, competitors and markets - at a cost

State the two main methods used in market research. *Primary* (field) research gathers *new* information for the first time eg by doing a survey. *Secondary* (desk) research collects data from *existing* information already published eg government statistics, or past sales records

State the two main characteristics of primary research. Primary research data has never been collected before. It is therefore targeted (gathered for a specific reason) and up-to-date

List methods used to collect primary data. Entrepreneurs can collect new information using

- *Surveys* asking questions eg street interviews or sending questionnaires in the mail
- *Focus group*: a small meeting of customers discuss a product, guided by a researcher
- *Observation* of consumers' eg how they shop in a supermarket
- *Experiment* eg test marketing a new product in a regional trial

State the two main characteristics of secondary research. Secondary research data already exists and was therefore collected for another purpose. Facts and figures may be out of date.

What is qualitative research? Qualitative research seeks to identify customer's attitudes and opinions eg why customers prefer one brand to another.

What is quantitative research? Quantitative research seeks to identify facts and figures about customers, competitors and markets eg how many people buy a newspaper every week

How can market research results benefit a business? Firms interpret (analyse) market research data to help decide the 'ideal' marketing mix for their products. Data can reveal the best combination of product, price promotion and place to meet identified customer needs.

Product trial and repeat purchases

What is product trial? Product trial occurs when customers buy and try out an item to see if it is worth buying again. This is called a *trial purchase*.

How can firms encourage trial purchases? Methods include:

- *Advertising*: eg a local newspaper and leaflet campaign announcing a new shop
- *Money off vouchers* offering discounts
- *Free samples*: eg a new baker can hand out free cakes to passers-by on opening day
- BOGOF or *buy-one-get-one-free offers* make a product look good value for money
- *50% extra for free* is an alternative method of tempting customers
- *Money back guarantee* makes any purchase appear risk free

What is penetration pricing? Penetration pricing is setting a relatively low price to boost sales particularly when launching a new product eg 50p a loaf for a new brand of bread

What are repeat purchases? When customers keep buying the firm's products

Why are repeat purchases important? Unless customers continue to buy a product after a trial purchase, sales decline and losses mount. Repeat purchases help build brand loyalty.

Explain customer loyalty. The willingness of customers to make repeat purchases

How can firms best build customer loyalty? By producing products that meet or exceed customer expectations and offer the best value for money when compared with rival items. This means making product customers want at competitive but profitable prices

How can firms generate repeat purchases? By building customer loyalty by offering

- *lower prices than rivals* This means taking action to cut costs without sacrificing quality or accepting a lower profit margin ie the amount of profit made from selling one item
- *Reputation for quality and reliability*
- *Convenience*: easy car parking; a central location; easy-to-use *website*; or *delivery service*.
- *High levels of customer service* so that buyers feel valued

Branding

What is a brand? A brand is a named product customers distinguish from other products and which they can identify with eg Nike

Why is branding important? Branding establishes the identity of a product and helps customers distinguish between items made by the firm and its rivals. This means the firm can:

- Add value
- Achieve greater customer awareness and hence sales in a crowded market place
- Charge higher prices of products customers believe to be 'different and better'
- Increase market share
- Make it harder for rivals to compete with its 'different and better' product portfolio

How can branding help repeat purchases? Customers tend to stick to named products they like know and trust.

How can branding help trial purchases? Existing customers who trust a brand are likely to be willing to try out new product lines launched by the firm

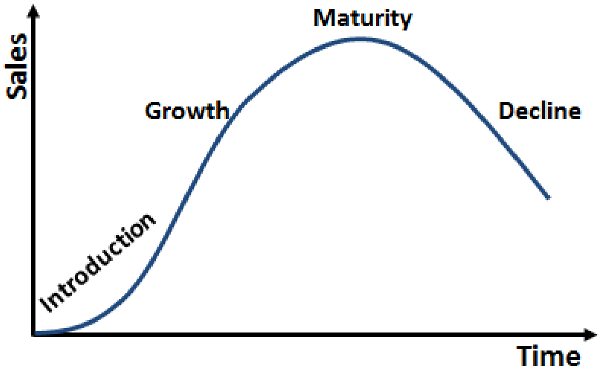
Explain product differentiation. Product differentiation is about making a good or service look different in the eyes of consumers

How can a business create product differentiation? Firms can make an item appear different from its rivals by adjusting the product's features, appearance design, packaging or brand logo

Product life-cycle

What is the product life cycle? The product life cycle is the period of time consumers are willing to buy a given product – products go through different stages.

List the phases in a typical product life cycle.



- *Launch*: the item is first brought out and offered for sale
- *Growth*: sales rise as the item becomes popular. Rivals enter the market
- *Maturity*: sales reach a peak
- *Decline*: sales fall in the item fall. Managers must opt to stop making the product or use an extension strategy to boost sales

Do all products have the same product life cycle? No. Many items can fail at the introduction stage. Well-known brands can maintain sales at the maturity stage over many years eg Hoovers.

What is cash flow? The movement of money in and out of the business over a period of time

What is net cash flow? Net cash flow is the difference between money coming in and money going out over a period. Eg if £200 comes in and £180 leaves, net cash flow is +£20

Explain the link between the product life cycle and cash flow.

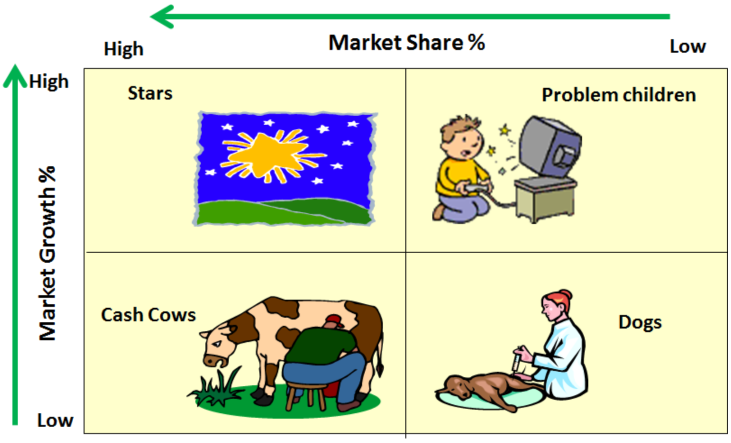
- At the launch phase, the cost of promotion and hiring staff probably outweighs the money coming in from early sales. Net cash flow is likely to be negative.
- In the growth phase, firms often need to invest in new equipment and staff to supply extra sales. Net cash flow begins to become positive
- In the maturity phrase, there is no need to invest in new equipment staff. If promotion costs are low, net cash flow is likely to be positive and at its highest. The cost of extension strategies reduces net cash flow

What is an extension strategy? Steps taken by a firm to maintain sales of mature product.

List potential extension strategies. Extension strategies to extend the life cycle include

- *Updating* the product's function and appearance so that it is 'new and improved'
- Encourage *repeat use* eg suggesting customers also eat breakfast cereal at lunch
- *Cut prices* to attract on sales
- Find *new markets* or *new uses* eg selling Lucozade as a sports energy drink

The Boston Matrix



What is the product portfolio? A product portfolio, sometimes called a product mix, is the range (portfolio) of items sold by a business

How do firms analyse their product portfolio? Businesses use the Boston Matrix to assess the range of items offered for sale

Explain the Boston Matrix. The Boston Matrix is a tool used to analyse the product portfolio of a business against market share and market growth.

Explain the term market size. Market size is the amount of sales made by all firms operating in an industry eg the pizza take away market is valued at, say, £300m a year.

What is market growth? Market growth occurs when market size increases over time.

Give an example of a growing market. If total sales of pizzas rise from £300m to £310m,

What is market share? The percentage of total sales in a market accounted for by one firm.

Give an example of a firm with a high market share. In 2010 Nokia has a 53% share of the smart mobile phone market. This means Nokia sells more than half of all the mobile phones

List the types of product in the Boston Matrix

- *Stars* products have a high market share in a fast growing market
- *Cash Cows* have a high market share in slow growing market
- *Problem children* products have a low market share in fast growing markets
- *Dogs* are products with a low market share in slow growing markets.

Why is the Boston Matrix useful? The Boston Matrix helps firms assess their product portfolio and take decisions about what to do with items within their product portfolio. Eg

- Dogs: is there any point in investing in products with a low market share in a slow growing market. If the product is not making sufficient profit, then withdraw from sale
- Problem child: why is market share low in a fast growing market? Is it worth investing in product improvements and a re-launch with supporting promotion campaign?
- Cash cows are usually in the maturity phase of the product life cycle and generate positive cash flow and profits. Do they need an extension strategy?
- Stars need support as they are in the growth stage. They may be absorbing cash now but they are tomorrow's cash cows

How can a business manage its brand? Firms can change the image and personality of a product by adjusting its marketing mix eg improved promotion or better product features

Building a successful marketing mix

What is the marketing mix? The marketing mix is the combination of factors firms use to create products that meet customer needs.

List the elements in the marketing mix. The 4Ps in the marketing mix are:

- *Product*: the features and appearance of a good or service
- *Price*: how much customers pay for a product
- *Promotion*: how customers are informed about products
- *Place*: the point where products are made available for customers to purchase

What are the typical features of a premium brand? Typically a premium brand hand bag is made out of long lasting, quality components and is expensive to buy. Premium brand items are often only on sale in exclusive shops and advertised in luxury magazines

Are all branded items premium brands? No. For example, many supermarkets offer value-for-money *own brand* items which combine good quality components, minimal design and packaging with affordable prices eg Waitrose Essential peas, milk etc

Describe some potential marketing mix options

- Product: to use expensive long-lasting components or cheaper options
- Price: do we charge a low 'value' price or high 'premium' price?
- Promotion: what is the most cost effective method of informing customers eg advertising or sales promotions
- Place: do we sell in supermarkets, exclusive shops, the Internet or everywhere we can?

List factors firms take into account when setting price. Price must *cover costs* if the firm is to make a profit and be *competitive*. Customers must be willing to pay the price being asked.

List the main methods of promotion. Firms can inform customers about their products using

- *Advertising* where a business pays for messages about itself in mass media such as television or newspapers.
- *Sales Promotion* are schemes which encourage customers to buy now rather than later eg point of sale displays, 2-for-1 offers, free gifts, samples, coupons or competitions
- *Personal selling* using face-to-face communication eg employing a sales person to make direct contact with customers
- *Direct marketing* using say 'junk' mail shots and weekly 'special offer' emails.

Distinguish between strategy and tactics. The dividing line between strategy and tactics is blurred. However, strategic decisions are normally taken by senior managers and affect the long-term direction of the business. Tactical decisions are normally taken by junior managers and affect the day-to-day operation of the firm

Give an example of a strategic marketing decision. Opting to invest in R&D to launch a new major product involves significant resources and effects of long-term direction of the firm

Give an example of a tactical marketing decision. Running a special offer BOGOF campaign can be taken by junior managers and mainly affects the short-term direction of the firm

Meeting customer needs

Design and research development

What is design? Design is working out how to make a product including its function, appearance and cost

Why is design important? Design helps a product stand out from the competition ie be different and better. Design is a way of creating product differentiation

What is the design mix? Product designers balance three elements:

- *Function*: what a product does and how well it works. Products must fulfil their function
- *Appearance*: how a product looks – an important opportunity for product differentiation
- *Cost*: the expense of making an item

Explain function. Function is what a product does and how well it works eg a raincoat keeps the wearer warm and dry

What is appearance? Appearance is the look of a product. Customers are much more likely to buy a good-looking items – ones they are proud to own and be seen using

Explain the role of cost in the design mix. Cost is the expense of making an item. Using cheap components lowers costs but often reduces reliability and functionality

What is the role of scientific research in design? New inventions and processes means firms can improve existing products and launch new ones – if they invest in R&D

What is R&D? R&D stands for research and development

- **Research** here is not market research but *scientific* research ie trying to find out new ways of making new or improved products
- **Development** is about putting theory into practice ie turning the results of scientific research into new or improved products

State the drawbacks of R&D? R&D requires investment in staff and facilities which raises costs and cuts profits – in the short term. Successful R&D means new products and long term profit

Managing stock

What is stock? Stock is any item stored by a business for use in production or sales. Often called *inventories*

List types of items typically held as stock. A car manufacturer can hold

- *Raw materials* eg cooper and *components* eg engine parts for eventual use in manufacture
- and *finished goods* awaiting held in store so that a customer order can quickly be met ‘from stock’

Why do firms hold stock? Firms store raw materials and components to enable production. By holding finished good the firm can meet an unexpected order immediately.

How does a firm decide on stock levels? The level of stock depends mainly on storage costs and the predictability of demand.

What happens if firms are out of stock? Production stops. Workers and machines stand idle.

Describe the drawbacks of holding stock. Holding stock costs money eg warehousing costs of requires financing. Interest is paid (or lost) on the amount tied up in stock.

What is stock control? Stock control is the method used by a firm to decide on stock levels eg do we need 100 or 10 axles in the warehouse at any one time; when do we need to reorder?

State the type of stock control measures a firm can use. There are two main stock control methods: *buffer stock* for 'just in case' and *JIT* ie just in time

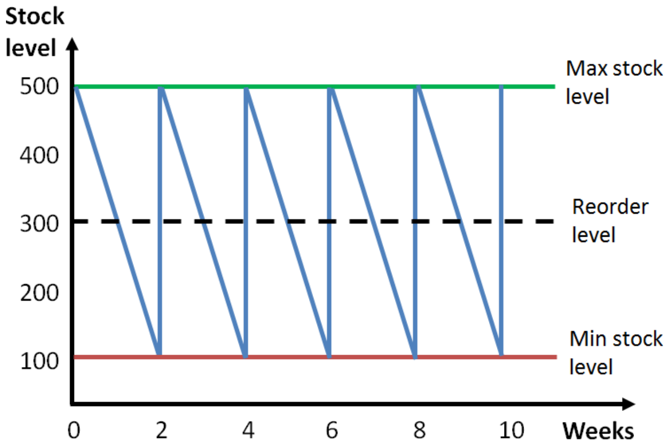
Explain how the buffer stock control works. Managers decide on

- a *maximum stock level*: the largest amount of items to be held
- a *minimum stock level*: the lowest amount of items to be held
- a *reorder level*: the minimum level of stock that triggers a reorder form the supplier

Interpret a bar gate stock control graph. The firm has decided to hold at least 100 components in stock, but no more than 500 at any one time. Its buffer stock level is 100.

When stocks fall to 300 items, the firm reorders 400 items which take around a week to arrive.

The new components are delivered when stock is at its minimum desired level of 100, taking the amount held in the warehouse back up to 500 – the desired maximum



Is there an alternative to holding buffer stocks? Firms can opt to do away with warehouses and buffer stocks and arrange for the delivery of components of the day they are required in production. This is called just-in-time (JIT) the stock management. No just-in-case stock is held.

What happens to suppliers fail to deliver just-in-time? If the firm has no stocks of raw materials and components then production cannot continue.

List the advantages of JIT stock control. Holding stock cost money. If interest rates are 10%, the annual cost of holding say £80,000 of stock is £80,000 x 10% = £8,000. Switching from just in case to just-in-time stock control saves £8000 in interest charges. Warehousing costs fall.

State the potential drawbacks of JIT stock control. Firms become reliant on suppliers who may withdraw bulk buying discounts if they have to make frequent deliveries of small amounts

Managing quality

What is quality? A quality product meets a the standards set by customers

Does high quality mean a high price? If a cheap umbrella keeps a customer dry in a shower, it fulfils its function and meets the standards set by the customer. It is a quality item.

How are quality and price linked? They are not. A quality product does what customers expect it do whether it is expensive or cheap.

How can firms deliver quality? Firms can deliver quality by producing items that meet the standard set by customers.

What happens if firms fail to deliver quality? Firms who supply products that do not meet customer standards lose sales - particularly in competitive markets

How can improving quality help a firm? Improving quality adds value and improves brand image, allowing a premium price to be charged. If demand is price insensitive, profits rise

How do firms manage quality? There are two methods of quality management:

- *quality control*: checking products meet the required standard

- *quality assurance*: ensuring a quality culture is in each stage of the production process

Explain how quality control can work in practice. Products are tested after they are made to ensure they meet set standards. Defects are thrown away, repaired or sold as seconds.

List the costs of traditional quality control methods. Testing finished products to ensure they meet set standards requires inspectors. Correcting defects costs money.

Explain the meaning of the term culture. Culture is the shared attitudes, values and behaviours of a group eg workers attitude to quality.

Explain the term quality culture. A quality culture exists when all staff understand the importance of ensuring all work at all stages of production meets standards

What does zero defects mean? Zero defects means all work meets quality standards

Explain how quality assurance can work in practice. All staff are responsible for checking the own work meet set standards. The aim is zero defects

Outline the main differences between quality control and quality assurance. In quality control, responsibility for fault finding rests with inspectors – not workers. Workplace culture assumes that defects are inevitable. With quality assurance, responsibility for fault finding rests with workers -not inspectors. Workplace culture assumes zero defects is normal in production

Operations and competitiveness

What is productivity? Output per worker ie how many items each employee makes in a period.

How is productivity measured? By dividing total output by the number of workers.

Give a worked example of measuring productivity. If a factory employing fifty staff produces 2000 tables a day, then the productivity of each worker is 2,000 tables/50 staff = 40 tables

Why is productivity important? Productivity affects unit costs, competitiveness and the break even level of output

What is unit cost? Unit cost is the average cost of making an item. Eg if the unit cost of making one table is £50 then, on average, a firm spends £50 producing each table

How does an increase in productivity affect costs? If staff increase productivity for no extra pay, then unit costs fall eg from £50 to £40 a table

Define competitiveness. When a business has some kind of advantage over its rivals

How can an increase in productivity affect competitiveness? Increased productivity cuts unit costs. Firms can use these cost savings to cut prices and so gain sales from rivals

How can firms raise productivity? Productivity can be improved by training staff, investing in new equipment and by improving management.

Why spend money on training and investment? The short term cost of training staff and buying new equipment (investment) is worthwhile if the resultant productivity gains mean bigger cost savings in the long run.

List other cost cutting measures a firm can use to increase its competitiveness. Firms can

- *Cut overheads* in administration by making some support staff redundant
- Ask *suppliers to cut their charges* for components and services while maintaining quality
- *Relocate* to countries where staff with appropriate skills can be hired at lower wages
- *Redesign products* so item are easier and so cheaper to make

Customer service

Explain the term customer service. Customer service is the experience a buyer gets when using products made by the business.

What is effective customer service? Effective customer service creates satisfied buyers. The buyer's experience of dealing with the business at least meets customer expectations

What is a delighted customer? Delighted customers find their expectations are exceeded when dealing with a business

Why is customer service important? In competitive markets, buyers have choices. Satisfied customers make repeat purchases and recommend the product to friends.

How can firms deliver effective customer service? A business needs to understand customer expectations and then deliver products that match or exceed those expectations

Outline the link between price and customer service. Customers shopping in discount shops have low expectations. They anticipate a lower level of service than one from a designer shop

How can firms improve customer service? Listening to customers helps a firm adjust to better match consumer needs, and respond to any problems. Managers can also focus on

- *Improving information* eg on packaging so that customers better understand products
- *training staff* to give better advice or hiring extra staff to handle customer enquiries
- Improving *after sales service* eg contacting customers to ask if they are happy
- Improving the *payment process* eg by hiring more till staff to cut queues

List the likely consequences of poor customer service. In competitive markets customers are likely to switch to rivals who offer better customer service. Lower sales lower profits.

Consumer protection laws

What is the law? The law is the body of rules that regulate the way our society operates. The law sets out the rights and duties of both buyers and sellers.

Outline the main features of the Sale of Goods Act. The Sales of Goods Act is a civil law that helps customers get their money back if there is a problem with their purchase:

- Goods must be fit for purpose and of satisfactory quality ie working at the time of sale
- The seller, not the manufacturer, is responsible for ensuring goods are fit for purpose
- Buyers can ask for a repair, replacement or refund if sold faulty goods

Outline the main features of the Trades Descriptions Act. The Trades Description Act is a criminal law that makes it illegal for firms to sell products:

- in *misleading ways* eg advertise shirts as 100% cotton if they also contain nylon
- by *withholding key information* eg failing to mention that shirts are seconds or adding a service charge of 20% without having placed a notice in the restaurant window

Outline the effects of consumer protection law on a business. Businesses must take steps to know and comply with the law. This *increases costs of production*. They must take care to ensure they are selling products as described, of satisfactory quality, and fit for purpose. A firm that breaks a civil law like the Sale of Goods may end up paying compensation. Breaking a criminal law like the Trades Description Act can results in fines or even imprisonment if found guilty

Effective financial management

How to improve cash flow

What is cash flow? The movement of money in and out of the business over a period of time

What are cash inflows? Cash inflows are *receipts*: ie money coming into the business

What are cash outflows? Cash outflows are *payments* ie money leaving the business

What is net cash flow? Net cash flow is the difference between cash inflows eg from sales and cash outflows eg from paying wages. Net cash = business receipts minus business payments

What is wrong with a cash surplus? Surplus cash can earn interest or profits if invested

What is wrong with a cash shortage? Cash shortages means firms must borrow to pay bills

What is financial management? Financial management involves planning ahead and anticipating future cash and finance needs

What is a cash flow forecast? A cash flow forecast predicts the future flow of cash in and out of the business over a given period of time eg three months.

How can firms improve cash flow? Put simply, by increasing receipts and reducing payments

How can firms increase cash receipts? Managers can draw more cash into the business by

- *increasing sales revenue* eg by selling more items at current prices by advertising
- *getting customers to pay bills quicker* eg by tightening trade credit terms
- *selling assets* such as little used equipment or property
- *destocking* ie running down inventories of components and finished items
- *arranging finance* eg an overdraft, new loan or extra share capital from owners

Explain trade credit. Most firms offer trade credit - customers buy now and pay later. Reducing the time customers are allowed to take to pay from 28 days to 14 days improves cash flow

Explain destocking. Destocking occurs when firms reduce their inventories eg by switching to just-in-time stock control, or holding the sale to sell off stocks of finished products

How can extra finance improve cash flow? Arranging a loan improves current cash flow. However future interest payments on the loan increases cash outflows

How can firms reduce cash payments? Firms can stem cash outflows from the business by

- delaying or cancelling orders for supplies
- arranging better credit terms with suppliers or
- delaying payment of bills to creditors – or even workers
- leasing rather than buying new equipment like a company car

How to improve profit

What is profit? Profit is the amount left over from revenue after paying all costs

What is a profit margin? A profit margin is the amount of profit made on each £1 of sales. Eg a profit margin of 20% means 20p for every pound of sales.

Explain losses. A business makes a loss when total revenue is not enough to cover costs

State the formula for calculating profit or loss. Profit or loss = total revenue – total costs

Give an example of profit. The window cleaner estimates he has 40 houses to visit next week. Given an average selling price of £8 total revenue is forecasted to be £8 x 40 = £320. Total costs are £250 giving an expected profit of £320 total revenue less £250 total costs = £70 profit.

Give an example of loss. One day that week the van breaks down and 10 houses are not cleaned. Revenue is £8 x 30 = £240. If costs remain the same at £250, a £10 loss is made

How can firms raise profit? Put simply, profits grow by cutting costs or raising revenues

How can costs be cut? The entrepreneur can attempt to

- Use cheaper components or raw materials - while maintaining quality
- Cut *wages* or even sack some staff – while maintaining productivity
- reduce marketing – while maintaining sales levels
- cutting back on *investment* in new equipment, training and research and development - while maintaining productivity, customer service and new product development

How can revenue be raised? The entrepreneur can try to

- improve marketing to increase the quantity of sales at current prices or to increase price while maintaining the quantity of sales
- launch new and improved products which better meet customer needs - while maintaining profit margins

Does cutting price always increase revenue? Revenue has two components price and quantity. Cutting price has two opposites' effects on revenue 1)more items are being sold – a revenue booster 2) each item is being sold a lower price - a revenue cutter

Cutting price only increases revenue if demand is price elastic. This is because the effect of the percentage increase in quantity outweighs the percentage decrease in price

When does raising price increase revenue? A price increase raises revenue only if demand is price inelastic: the percentage increase in price effect outweighs the percentage fall in quantity

Break even analysis

How is profit calculated? Profit is found by deducting total costs from total revenue

Explain break even. Break even is the output level when total revenue equals total costs. At the break even level of output the business is making neither a profit nor loss. Sales cover costs.

What happens if the firm sells more than its break even level of output? Beyond the break even level of output, revenue exceeds cost and the firm is making a profit.

What happens if a firm fails to sell its break even level of output? Revenue is less than cost, and the business is making a loss.

Define total revenue. The entire income earned by a business from its sales over a period.

Interpret the Total Revenue graph.

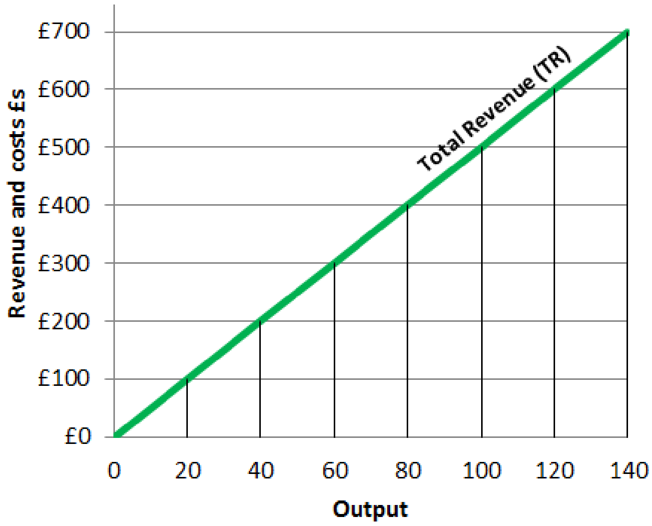
The horizontal axis shows the number or items sold by the firm ie sales, output or quantity

The vertical axis shows the total revenue earned from selling each level of output

The graph tells us that the firm earns £100 from selling 20 units – this is its total revenue

Selling price is £5 per item

The total revenue line slopes upwards because as more is sold, total revenue rises



Define total costs. The entire amount spent by a firm making its products over a period.

What are costs? Cost is the amount spent by firms making products.

State the main types of cost. There are two main types of cost: fixed cost and variable cost

Explain fixed costs. Fixed costs are costs that do not change as output changes. Fixed costs such as rent and interest stay the same even if more is produced.

Make a list of common fixed costs. Rent for business premises, interest payments, loan repayments, administration staff wages, internet and phone bills, insurance payments, and advertising costs. These costs remain the same even if output rises in a period.

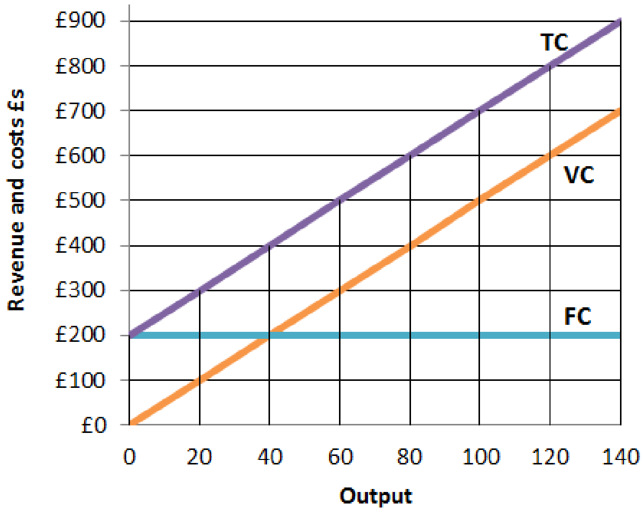
Explain variable costs. Variable costs change with the amount produced. For example, the cost of raw materials used in production rises as more output is made.

Make a list of common variable costs. Examples of variable costs include the wages of production workers; raw materials; fuel, gas, electricity and petrol used in production; packaging of the finished product.

How can entrepreneurs determine which costs are fixed or variable? A business person asked themselves: does this cost go up if just one more item is made? Extra production increases variable costs but leaves fixed costs unchanged

What are total costs? Total costs are the amount of money spent by a firm on producing a given level of output. Total costs are made up of fixed costs (FC) and variable costs (VC).

Interpret the Fixed, Variable and Total Cost Graph



The *fixed cost* line is horizontal because no matter how many items are made, fixed costs like rent stay the same. Fixed costs are £200.

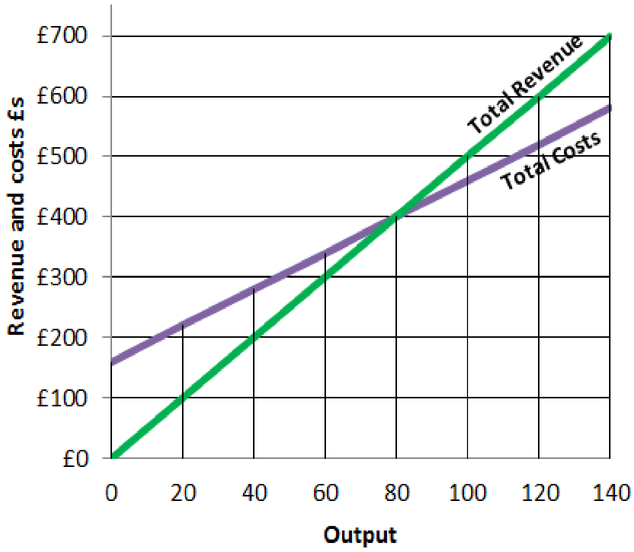
The *variable cost* line slopes upwards because as more items are made variable costs such as packaging rise

Adding the variable cost line to the fixed cost line gives the *total cost* line.

The vertical distance between the TC and VC lines equals the amount of the firm's fixed costs

What is a margin of safety? When the quantity sold is above the break even point. The firm is making a profit.

Interpret the break even chart. The break even chart shows the total revenue and total cost lines, together. The break even level of output (BEQ) is where the total cost and total revenue lines cross ie 80 units



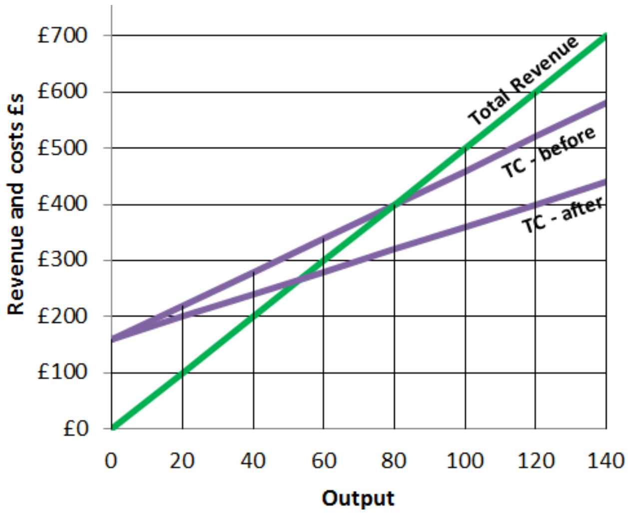
- If the firm sells less than 80 units it is making a loss.
- If the firm can sell more than 80 units it is making a profit

Selling more than 80 units give the firm a margin of safety

How do firms make use of break even analysis? Break even analysis helps a firm forecast the level of sales needed to break even. A firm can see the impact of price and costs changes on BEQ

What happens to cost lines if costs changes? An increase in costs moves a cost line upwards. Any fall in costs, say from a rise in productivity, moves a cost curves downwards

Use a Break Even graph to show the effect of a fall in costs



The Total Cost line moves downwards because variable costs have fallen. The break even level of output falls from 80 units to 50.

Extension point: Note fixed costs have stayed the same at £160. This means the total cost line pivots on the vertical axis around £160.

A change in just fixed costs from, say, cutting overheads causes a parallel shift in the total cost curve, rather than a pivot

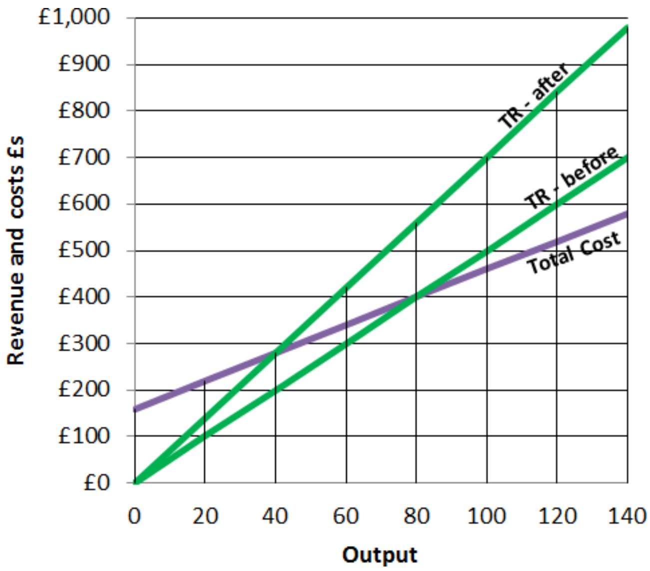
What happens to the total revenue line if price changes? An increase in price causes the total revenue line to pivot around zero and become steeper. A price cut has the opposite effect. The TR line pivots around zero and becomes shallower

Use a break even graph to show the effect of a price rise.

The TR before line shows total revenue for each level of output when price is £5. The break even level of output (BEQ) is 80.

If price rises by £2 to £7, the TR line pivots around zero and moves upwards to TR – after. The BEQ falls to 40 items

Extension point: can the business be confident that customers will still buy their product if price rises by £2. What happens if competitors keep their prices low or if buyers feel the product is now too expensive?



Contribution

What is contribution? Contribution is the extra revenue generated over variable costs when selling a product

How is contribution calculated? Contribution is found by deducting unit variable cost from the selling price

State the formula for calculating contribution. Contribution per unit = selling price– unit variable costs

Give an example of calculating contribution. The price of a pie is £2.50. The average or unit variable cost of making one pie is £1.50. This means each pie sold contributes £1.

What happens to contribution? The contribution made by each item is first used to pay off fixed costs and then towards making a profit

How is contribution used to estimate the break even level of output (BEQ)? Firms use the formula BEQ = fixed costs / contribution per unit

Give an example of contribution analysis. If fixed costs are £10,000 and each unit contributes £5 then the break even output level = £10,000/£5= 2,000.

Financing growth

How can a business grow? To increase its size of operation a business needs to invest in extra staff machinery and premises, R&D or takeover a rival. Each option needs finance.

What is finance? Finance is the amount of money at the disposal of a business

What is a source of finance? The source of finance is the origin of money a business has

What type of debt do firms typically use to finance growth? Some sources of finances are short term, that is, they need to be repaid initial period of time eg an overdraft. Buying new equipment and building is a long-term decision requiring a long-term source of finance

List sources of finance not suited for investing in growth. Overdrafts, trade credit and factoring are best used to manage short-term cash flow problems- not finance long-term growth

How can businesses finance growth? There are two main sources of funds for growth:

- *Internal*: within the firm itself eg from *asset sales* or retained profit
- *External*: outside the firm eg a *debt* (borrowing) or *share capital*

Explain the term assets. Assets are items of value owned by a firm eg equipment and stock

How can firms raise funds from assets? Firms can raise funds for growth by selling unwanted or under-used assets. Eg selling a non-essential building releases funds for growth

What happens to profits? Profits can be

- *Distributed* ie paid out to owners as a reward for risk taking investment or
- *Retained*: kept back to finance extra spending on new equipment or premises

How can retained profits finance growth? Expanding firms need to find the money to buy new buildings and equipment. One method is to make use of past profits. No interest is charged.

How can debt finance growth? Debts arise when firms borrow money eg by taking out a loan

Describe types of debt best suited for financing growth. Businesses can borrow money by

- Taking out a *loan* **-** usually from a bank. Funds are borrowed for a fixed period of time and repaid regularly with interest. Eg £60,000 is repaid monthly over five years with 10% pa interest added
- Selling *bonds* (*debentures*) to banks and private investors. A bond is an IOU promising to pay whoever owns the debenture a regular fixed annual interest payment eg 10%.

List the drawbacks of using loans. Loans are repaid with interest which increases overheads and reduces cash flow for the period of the loan. Collateral may be required.

What is share capital? Some business called companies can raise finance by issuing shares. The value of all the shares sold to investors by company is its share capital.

What is a company? A company is a business with its own legal identity and is owned by shareholders. Sole traders and partnerships are not companies

What is a shareholder? Someone who has bought shares and so owns part of a company

What are shares? A share is a certificate that represents a part ownership of the company. Usually each share gives the owner the right to one *vote* at any shareholder meeting and *part of any profits* distributed to shareholders called a *dividend* (profit payment)

How can a business raise funds using shares? Companies can raise finance for growth by selling new shares to private investors. This is called a *rights issue*.

Why are shares a popular source of company finance? The money invested by shareholders does not need to be repaid. There are no interest payments to make.

List the drawback of issuing shares. Increasing the number of shareholders can mean existing owners lose control and have to share profits

What is the stock market? The stock market is the place where shares are bought and sold

List the two types of company found in the UK. There are two main types of company: private limited company (Ltds) and public limited company often called Plcs

What is the main difference between private and public limited companies? New shares in private limited companies cannot be advertised for sale and are not listed on the stock exchange. Members of the general public can be invited to buy new shares in public limited companies which can be bought and sold on the stock exchange

What is a stock market flotation? A stock market flotation is when a private limited company converts to being a public limited company and offers shares for sale to the general public

Why do private limited companies decide to float? Converting to a plc means a business can raise very large sums of money (£m) by offering new shares for sale to the general public

How do firms decide on the best source of finance? In raising extra funds owners consider:

- *Cost*: how much will borrowers charge for use of their funds eg the interest rate on loans
- *Risk*: eg can the business afford to pay interest charges if it makes unexpected losses
- *Availability:* eg only companies can issue new shares; banks may restrict credit

	Loan	New shares
Cost	Banks's Arrangement fee Annual interest charges. Loans must eventually be repaid	Floatation/rights issue complicated and costly But share capital is like an interest free loan that never needs to be repaid
Risk	Loss making firms must still pay interest charges	Loss making firms stop paying dividends
Availability	Banks may require collateral or refuse to lend	Only companies can issue shares

How can government help finance growth? State can offer interest-free loans, grants that do not need to be repaid and tax breaks to businesses locating in deprived areas or investing in new technologies.

Effective people management

Organisational structure

Explain the tem organisation. The term organisation has two meanings in business studies:

- another way of saying business or firm
- internal structure of a business ie how production and staff roles are arranged

Why is organisation important? Staff need to understand how their own role fits into the whole business. Improving organisation can cut costs and so improve competitiveness.

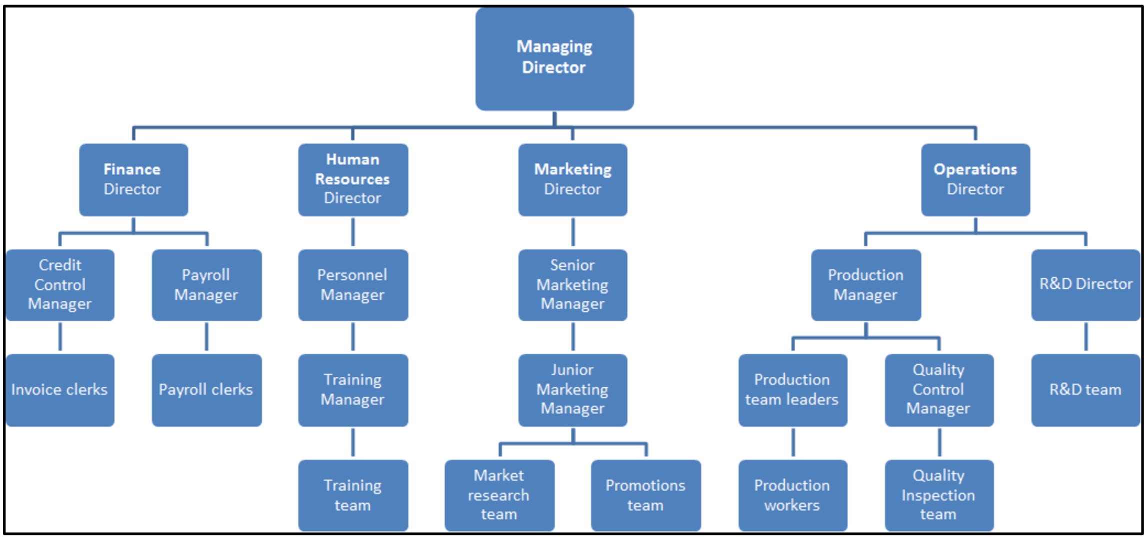
What is a business division? Firms can organise themselves on a product basis with each division responsible for making a particular type of product eg Ford Cars and Ford Vans.

Explain the term subsidiary. A subsidiary is a business owned by another business eg DSG International owns Dixons and PC World.

Why organise a product basis? Organising a business into subsidiaries allow specialisation - each section can focus on what it does best eg televisions (Dixons) and computers (PC World). Each subsidiary is a separate profit centre keeping its own financial accounts. This means directors can assess the individual performance of each business division

Define roles and responsibilities. *Role* refers to the tasks and duties of a member of staff. *Responsibility* is the obligation on staff to finish a task.

What is an organisational chart? An organisational chart is a diagram that shows the role and responsibilities of staff, and their relationship with other workers



What are hierarchies? Hierarchy refers to the number of management levels within a firm ie the 'pecking order'. There are five levels of hierarchy in the organisational chart shown.

What is a line manager? Line managers are responsible for overseeing the work of other staff lower down the hierarchy. Line managers can ask subordinates to undertake tasks.

What are subordinates? Subordinates report to line managers higher up the hierarchy. Subordinates are accountable for their actions to their line manager.

Explain the terms authority delegation. *Authority* refers to the power managers have to direct subordinates and make decisions. *Delegation* occurs when managers entrust tasks or decisions to subordinates

Explain empowerment. Empowerment sees managers passing authority to make decisions down the chain of command to subordinates. Empowerment can be motivational.

What is span of control? The number of subordinates reporting directly to a manager

What is the chain of command? The chain of command is the way in which instructions are passed down a business from line managers to subordinates.

Explain delayering. One method of reducing costs is to remove a layer of management in a hierarchy, while expecting remaining staff to produce the same level of output ie delayering

What is centralisation? In centralised organisations most decisions are taken by senior managers at the top of the organisational chart. Junior workers have little authority and must follow rules and procedures set out by senior managers. This can be demotivating

Explain decentralisation. With decentralisation the authority to take decisions is passed down the chain of command to subordinates who are empowered to take decisions. This process is called delegation. Decentralisation motivates and leads to more 'local' decisions being taken by workers dealing every day with customers and suppliers

Motivation theory

What is motivation? Motivation is the way a business encourages staff to give their best.

Why is motivation important? Motivated staff care about the success of the business and work better than they otherwise would

How can a motivated staff help the business? A motivated staff means

- extra effort from workers resulting in increased productivity hence lower unit costs
- Improved quality as staff take a greater pride in their work
- workers are keen to stay with the firm and reluctant to take unnecessary days off work

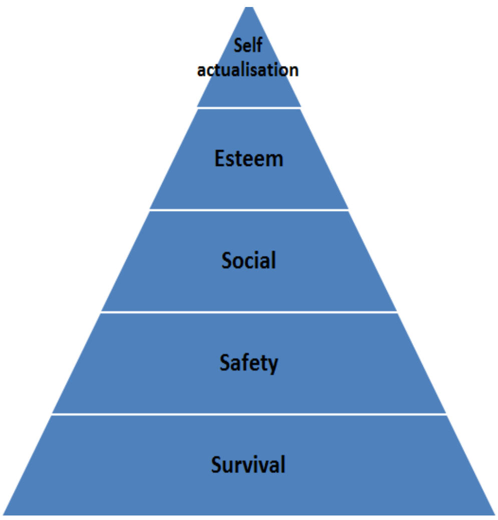
How can managers motivate staff? Managers can influence employee using:

- money: some staff work harder if offered higher pay
- non-monetary factors: Other staff respond to incentives that have nothing to do with pay, eg the chance to win promotion

What is Maslow's hierarchy of needs? Maslow's hierarchy of needs is a motivational theory that seeks to explain why workers take jobs, want to work, gain promotion etc

List the Maslow hierarchies of need. Maslow suggests there are five hierarchies (levels) of need that explain sources of motivation and why people work.

- Staff first want to meet their *survival needs* by earning a good wage.
- Staff safety needs are met by effective work health and safety procedures and offering job security eg long-term contracts
- Social needs are met if firms create a 'one whole family' workplace culture and arrange social events e.g. a work football team or night out
- esteem needs are met and staff feel respected and valued
- self-actualisation occurs when staff believe they can reach their full potential work



What is the link between Maslow's and motivation? Motivation involves offering workers the chance to move to the next level of need Moving staff up a Maslow level is motivational.

Explain the phrase motivation comes from within. There is much business can do to encourage staff to work harder than they otherwise would, the desire to work hard also comes from within the workers themselves. This explains why some staff with the same roles and responsibilities in the business have more enthusiasm for work and others.

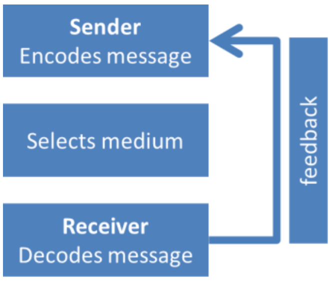
Communication

What is communication? The passing of messages between people or organisations

Why is effective business communications important? Effective communication can mean

- Buyers believe they are being listened to and so receiving good customer service. This encourages repeat business and additional word of mouth sales
- Staff understand their roles and responsibilities and have the information they need to complete tasks quickly and efficiently. Deadlines are understood and met
- Staff believe managers listen and take their views into account. This is motivational

Distinguish between internal and external communication. Internal communication is the passing of messages *within* the organisation. External communication is the passing of messages *outside* the organisation.



Identify the steps in communication. A *sender* encodes (chooses words & images) and sends a *message* (a memo) via a *medium* (email) that is decoded (interpreted) by the *receiver* who then responds (feedback).

What is effective communication? In successful communication, the receiver decodes, understands and acts on a message as intended by the sender. Eg a subordinate orders an extra photocopier having been sent a memo by their line manager

Explain formal channels of communication. Formal channels are recognised by the business as official ways of sending messages eg a company memo, fax, report or e-mail

Explain informal channels communication. Often called the grapevine, informal communications are unapproved messages between staff eg everyday conversation and gossip

Explain channels of communication. The channels of communication is the path taken by a message eg a formal memo, or informal conversation using the grapevine

Why is communication important? Communications can affect motivation, efficiency and productivity, the time taken to make decisions, and customer and supplier relations

What can happen given too little communication? Insufficient communication can leave staff unsure about their role and responsibility and demotivated. Some tasks may not be completed.

What can happen given too much communication? Excessive communication can lead to information overload with staff unable to manage the volume of calls and e-mails. This reduces efficiency and increases costs as more resources are needed to achieve the same result.

List potential barriers to effective communication. Communications can break down given

- a message is *unclear* or becomes *distorted* because it has passed through so many hands
- the receiver does not understand technical *jargon*
- *poor IT* eg a full answer machine or key e-mail is automatically sent a junk email folder

How can manages improve communication? Training staff to send clear, accurate, thorough messages using an appropriate channels improves the quality of communications – especially if there is a chance for feedback

Remuneration

What is remuneration? Remuneration means the way staff are paid eg a salary

Distinguish between blue-collar and white-collar workers. Blue-collar workers do manual work and are usually paid wages weekly. White-collar workers are non-manual staff and are usually paid a monthly salary

Explain wages. Wages are normally paid weekly for working a fixed number of hours plus any overtime. Eg working 35 hours for £8 an hour gives a weekly wage of £280

What is overtime? Overtime are hours worked over and above the basic working week

Explain salary. A salary is a method of payment made to non-manual staff for work done. Normally an annual salary is paid monthly and for the job rather than hours worked. This means overtime is not usually paid.

Explain piece rate. With piece rate staff are paid for every item produced. The more items they make, the more they earn in pay. This can encourage working quickly and so risk quality

What is commission? Commission is a payment link to sales. Eg staff on 10% commission who sell £5,000 of products earn £500 sales related commission.

Explain bonuses. Staff may earn a bonus if they reach a particular target.

Distinguish between full-time and part-time work. Some staff are employed for the entire working week eg 35 hours. Others work for only a fraction eg 10 hours a week

Explain the term temporary work. Temporary work is a job with a business for a limited period of time eg 3 months. Temporary work is often done by freelancers who have little job security. The firm is free to rehire, or take on new staff, at the end of their contract.

Explain freelance work. Typically a freelancer is self-employed and carries out a specific piece of work for a business as a supplier. They are independent contractors who take on temporary work for a fixed period and so have no job security.

Explain fringe benefits. A fringe benefit is a non-monetary method of rewarding workers eg a company car, free medical insurance, pension contributions, canteen or accommodation

What is a time based payment method? In a time-based system, staff pay for the number of hours worked eg wages and overtime.

What is a result based payment method? In a results-based system staff are paid for *outcomes* eg the amount they make (piece rate) or for reaching a target (commission or bonus)

Which is the best method of payment? There is no one ideal method of payment – it depends on the type of work and type of staff. Time based methods give incentive to achieve targets than those working on a results based method of payment. However results based payment methods eg piece rate give an incentive to work fast and focus on quantity rather than quality. Offering commission may encourage aggressive selling that damage the reputation of the firm

How does payment affect motivation? Maslow suggests that staff must earn enough money to meet their survival needs. As workers move up the hierarchy money becomes less of a motivator. Some staff work to socialise or acquire status

The wider world affecting business

Ethics in business

What are ethics? Ethics is a set of moral principles about what is right and wrong

What is ethical behaviour? A business acts ethically when its actions are morally acceptable ie the firms is seen to be 'doing the right thing'. Unethical behaviour involves taking unfair advantage of customers, staff, suppliers, etc

How can firms act ethically? Ethical behaviour requires firms to take account of the wider impact of its actions on stakeholders. Managers making ethical decisions take into account:

- *Impact*: Who does my decision affect or harm?
- *Fairness*: Would my decision be considered fair by those affected?

Give examples of ethical business behaviour. Examples include:

- Ensuring staff are paid a fair wage and have good working conditions
- Paying fair prices for supplies and fair wages to workers
- Paying suppliers promptly and giving them long term contracts
- Protecting the environment by using renewable resources and minimising pollution
- Supporting the local community and charities

Define decision making. Decision making is selecting a course of action between alternatives.

Define choice. Choice involves selecting one option between alternatives.

What are trade-offs? A trade-off is the process of making a choice between alternatives

Give an example of an ethical choice. A furniture maker can source wood using 1) low cost non-renewable timber or 2) sustainable but high cost wood forests where trees are replanted.

Why do some firms opt to act unethically? Acting ethically usually increases costs and so reduces profit margins and competitiveness. Paying the lowest amount possible for raw materials and wages may harm suppliers and workers but benefits profits and owners.

List the potential costs of acting unethically. Firms that are seen as acting unethically to cut costs can lose customers, sales and profits

Why do some firms opt to act ethically? The ethical behaviour of the firm can affect

- *Sales*. Many customers try to buy items sourced and made ethically – even if this means paying higher prices. Eg the Co-op is thriving by marketing itself as an ethical brand attracting customer loyalty and repeat purchases
- *Motivation*. Ethical firms attract staff who are willing to work harder than is normally expected. This means higher productivity, lower costs and so higher profits
- the annual report to shareholders

What are pressure groups? Pressure groups are organisations that aim to influence decision makers and change how business operate

How can pressure groups make change happen? Pressure groups take action to change the attitudes and behaviour of *stakeholders*. For example:

- drawing of *customers* attention to unethical behaviour by organising marches or demonstrations outside shops; writing letters to the press and MPs; newspaper adverts
- attending company AGMs and press conference and asking challenging questions
- persuading the government to introduce new laws and regulations restricting firms
- direct action and disruption

Environmental issues

What is the environment? The natural environment is made up of all living and non-living things occurring naturally on Earth

What are renewable resources? Renewable resources can be replaced after use eg solar energy and trees

What are non-renewable resources? Non-renewable resources can only be used once and so cannot be replaced after use eg coal, gas and oil

List the main short term environmental effects of business activity. Production can lead to

- *noise and air pollution* from production eg CO2 emissions from power stations
- *traffic congestion* as raw materials, components and finished products are moved and staff travel to work

List the main long term environmental effects of business activity. Production can lead to

- *resource depletion* when natural resources are used up and not replaced
- *climate change* in temperature, rain fall, wind speeds and sea levels

How can business activity cause climate change? Burning fossil fuels to generate power releases greenhouse gases eg C02 into the atmosphere. Carbon dioxide acts like a blanket and traps warmth leaving the earth causing *global warming* ie average temperatures to rise.

What is sustainable production? Sustainable production occurs when resources taken from the environment are replaced eg new trees are planted to replace those cut down for timber

How can businesses reduce the impact of their activities on the environment? Firms can

- use non-renewable *energy sources* eg wind power and *resources* eg recycled paper
- replace old energy inefficient or high polluting equipment with *green technology*
- *buy locally made inputs* to reduce traffic congestion and air pollution
- design products to be *recyclable and reduce the amount of packing* used in products
- reduce pollution by making better use of *video conferencing* to avoid travelling

How does going green affect sales and profit? Going green can increase costs and so reduce profits. However being seen to be green can attract new environmentally conscious consumers and so boost sales and profits. Staff may feel motivated by working for a green firm

International income distribution

Explain the term income distribution. Income distribution is how total income is shared out.

How is income distribution between countries measured? One method is to calculate average income per head of the population using US dollars ($) as a common currency

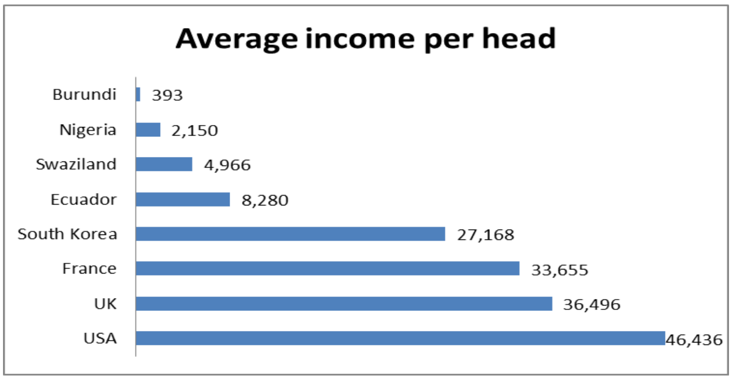
How is average income per head of the population calculated? By dividing the total value of all products made in a country in a year (GDP) by the size of the population

What is GDP? GDP is short for gross domestic product which is the monetary value of all products made in a country in, say, a year.

Show how UK average income per head is calculated. The GDP of the UK in 2009 is around £1,265,000m and the population is around 62m. This means average income from every man woman and child in the country is around £20,400 Source: [Measuring Worth]

How is world income distributed? World incomes are distributed very unevenly.

The diagram shows that in terms of US dollars ($) the average income of someone living in Burundi is less than someone in Nigeria and a tiny fraction of the average income of citizens living in developed countries such as the France, the UK and the USA



Import protection and export subsidy

What is international trade? The buying and selling of products between countries

What are exports? UK exports are UK made products sold overseas,

What are imports? UK imports are overseas made products sold in the UK.

How can UK firms compete against foreign rivals? UK businesses can compete against foreign rivals by offering better designed, higher quality products at lower prices.

Explain the term import protection. Import protection is a government measure taken to reduce the amount of overseas made products sold in the UK

Give examples of an import protection measure. Governments can introduce t*ariffs*: a tax on imported products that raises the price of imports and q*uotas*: physical limits on the volume of imports allowed into a country

How do tariffs affect UK firms? Tariffs increase import prices. The impact varies

- UK firms competing against importers benefit
- UK firms importing raw materials and components pay more for inputs and must either pass on cost increases as higher prices or accept lower profit margins
- UK firms exporting to countries imposing tariffs suffer as they must either pay the tariff out of profit or pass on the tariff to customers as higher selling prices

How can quotas affect firms? Quotas restrict the amount of imports creating shortages and higher prices.

Explain export subsidies. A subsidy is a payment made by the government to lower prices. An export subsidy helps UK firms selling overseas to cut prices and gain sales.

The impact of government

How can the government take action to affect businesses? The main ways the state can influence business behaviour is by changing *taxes* and laws and *regulations*

List the main types of taxes that can affect a business.

- *Income tax* taken out of staff wages and salaries. Increasing income tax means workers have less disposable income and so less money to spend in the shops.
- *Value added tax* (VAT) on goods and services. The increase in VAT to 20% in 2010 may increases prices if firms opt to pass on the VAT increase to customers as higher prices.
- *Corporation tax* is a tax on company profits. A rise in corporation tax means companies keep less profit leading to less investment in new equipment and R&D
- *National Insurance contributions* (NIC) are payments made by both the employee and the employer which pay for the cost of a state pension and the National Health Service. A rise in NICs increases costs which can mean higher prices if passed onto buyers.
- Local government collects *rates* from firms. An increase in rates increases overheads

Explain government regulations. Regulations are rules that restrict behaviour ie 'red tape'

Give examples of regulations. The government issues thousands of rules covering eg health and safety, waste disposal, maternity leave, equal opportunities, planning permission, etc

What are the benefits of regulation? Regulations aim to protect the interests of weaker stakeholders and so avoid business exploitation of workers, customers etc

What are the costs of regulation? New rules usually increase costs eg installing disabled access in an historic house or ensuring fathers have paid paternity leave

How is the impact of regulation assessed? New rules create 'winners and losers'. A regulation is effective if the benefits it creates outweigh its costs.

What is the EU? The EU stands for the European Union and is an association of 27 European member states seeking increasing economic and political co-operation

How can EU regulations affect UK businesses? The UK is a member of the EU. This means EU regulations are binding on UK firms eg lorry drivers must take frequent breaks

How does the minimum wage affect businesses? An increase in the minimum wage benefits workers with low wage jobs but increases the costs of the business. Firms may opt to hire fewer staff or pass on cost increases as higher prices to maintain profit margins

How do maternity/paternity rights affect businesses? By law parents are entitled to paid leave on the birth of their child and their job is kept open if they want to return. This means firms are paying for both the parent on leave and their replacement – if one can be found

How do health and safety regulations affect businesses? Health and safety rules protect staff but are costly to implement.

Unit 3 Glossary

Accountability: where subordinates answer to their supervisor and justify their actions and decisions

Added value: when the price of an item is higher than the cost of all the resources used. Consumers value items more than the costs paid to suppliers

Advertising: paid for communication using mass media eg TV adverts that aims to inform and persuade

After sales service: customer support after a product is bought eg guarantees and help desks

Anticipate customer needs: predicting the future wants and desires of buyers

Assets: items of value owned by a business eg cash, equipment and stock

Average cost (AC): The cost of producing one item. Divide total costs (TC) by total output (Q). AC = TC/Q

Bank loan: money lent by a bank that is repaid over a fixed period of time with interest

Barriers to communication: factors preventing the efficient exchange of messages

Blue collar workers: manual workers paid wages weekly

Bonus: a payment made to staff for meeting or exceeding a target

Boston Matrix: a tool used to analyse the product portfolio of a business against market share and market growth

Brand: a named product customers distinguish from other products and which they can identify with eg Nike

Branding: the name or symbol organisations use to differentiate (distinguish) one product from rivals

Break even: sales cover costs without making any profit

Break even forecast: Predicted break even output level based on an estimate of the firm's future costs & revenues

Break even output: The amount of output a business must sell to make neither a profit or a loss

Buffer stock: The amount of inventory held in case of unforeseen shortages or unexpected demand

Business: any organisation that makes goods and services

Business activity: when a firm takes inputs such as staff hours and raw materials and turns them into outputs ie goods and services

Business division: Firms organise themselves on a product basis eg Ford Cars and Ford Vans are self contained business units under the Ford umbrella

Business failure: a business ceases trading

Cash: the amount of money the firm has in notes, coins, and money in the bank

Cash flow: the movement of money in and out of the business over a period of time

Cash flow forecasts: a prediction of how much cash will come in and leave a business over a period of time

Cash flow problems : a firm is running out of cash and the ability to pay its bills. The business is risking insolvency

Cash flow statements: A document stating where cash used by the company came from how it has been used

Cash inflows: receipts of money coming into the business eg from customers paying their bills. Also called receipts

Cash outflows: payments of money leaving the business eg buying stock, wages and rent

Centralisation: when decision making is taken by senior managers at the top of the organisational chart

Chain of command: The line of authority along which instructions are passed. Illustrated by organisation charts.

Climate change: change in temperature, rain fall, wind speeds and sea levels over time

Commission: a payment made to staff linked to sales

Communication: The passing of messages between people or organisations

Company: a business with its own legal status separate from its owners called shareholders

Competition: a market with lots of sellers

Competitive advantage: being able to offer a product which customers prefer to rivals

Competitiveness: when a business has some kind of advantage over its rivals

Consumer: someone who buys products for their own use

Consumer spending: the amount of money spent by customers

Contribution: the extra revenue generated over variable costs when selling a product

Contribution per unit: The amount by which the selling price exceeds unit variable costs. Contribution per unit = selling price minus average variable cost.

Control: the responsibility for running the day-day-to-day affairs of a business and making decisions

Convenience: fit for customer needs and causing little difficulty

Corporation Tax: a tax on company profits paid to the government

Costs: the amount spent by a firm making its products over a period

Creditors: an individual or business that is owed money

Culture: shared attitudes, values and behaviours of a group eg workers attitude to quality

Customer needs: the wants and desires of buyers

Customer service: the experience of buyers when dealing with a business

Customers: individuals or organisations that buy a product

Debentures: firms sell a certificate which pays a fixed rate of interest to the holder. An IOU.

Debtors: an individual or business that owes money

Decentralisation: the authority to make decisions is passed down the chain of command to subordinates who are empowered to take action

Decision making: selecting a course of action between several alternatives

Delayering: Organisations flatten (remove) one or more layers of hierarchy

Delegation: Managers authorise subordinates to carry out specific activities or make decision

Demand: the amount of a product customers want to buy

Design: working out how to make a product including its function, appearance and cost

Design mix: the combination of function, appearance and cost used in making a product

Destocking: when firms reduce their inventories

Direct costs: The expense of making a product eg cost of materials. Other indirect costs are not counted

Distributed profit: that part of profit returned to owners eg dividends

Dividends: the share of company profits paid out to shareholders

Economic growth: an increase in the amount of goods and services produced by an economy

Empowerment: Staff are given responsibility and authority

Environment: the natural environment is made up of all living and non-living things occurring naturally on Earth

Ethics: a set of moral principles

EU: the European Union: an association of 27 European member states seeking increasing economic and political co-operation

Export subsidy: a payment made to UK firms to cut the price of products being sold overseas

Exports: UK made products sold to overseas buyers

Extension strategy: steps taken by the business to maintain sales of mature product

External communication: the passing of messages outside the organisation

External finance: funds raised outside the business eg bank loan

Finance: the amount of money at the disposal of a business

Fixed costs (FC): expenses of production that do not change as a firm changes its level of output eg rent

Forecast: a prediction about the future sales, payments etc which may or may not turn out to happen

Formal communication: methods of sending messages recognised by the business eg a company memo, fax, report or e-mail

Freelance: typically a self-employed individual who does a specific piece of work for a business as a supplier. An independent contractor

Fringe benefits (perks): a non-monetary method of rewarding workers eg free medical insurance

GDP: the monetary value of all products made in a country in, say, a year

Generic product: a non-branded good or service

Good: a physical product such as burger or car

Hierarchy: The number of levels or layers within an organisation ie the 'pecking order'

Holding company: A business that owns other businesses

Identifying customer needs: finding out buyer requirements

Imports: foreign made products sold to UK buyers

Income: money received per period

Income distribution : how total income is shared out

Income tax: a tax on wages and salaries

Informal communication: unapproved messages between staff eg everyday conversation or gossip. Often called the grapevine.

Insolvency: a business that runs out of cash and so cannot pay its bills. A major cause of business failure

Interest: the charge made for borrowing money. The cost of borrowing and the reward for saving.

Interest rate: the annual percentage charge made for borrowing money eg a 8% interest rate means £8 is charged for every £100 pounds borrowed

Inventories: the amount of stock held by a firm eg components for use in production and finished goods awaiting sale

JIT: Just in time production makes items from components delivered when needed ie no stocks

Law: the body of rules that regulate the way our society operates

Layers: A given level in the hierarchy

Legislation: the law of the land

Limited company: a business with its own legal identity and is owned by shareholders and controlled by directors. Owners have limited liability.

Line manager: A member of staff directly responsible for a subordinate eg allocating tasks and assessing their performance

Loans: a sum of money borrowed from a creditor and repaid usually with interest over a period of time eg 3 years

Long term finance: funds raised to finance business activities for more than 3 years eg a mortgage

Losses: when total revenue is not enough to cover costs

Margin of safety: When the quantity sold is above the break even point. The firm is making a profit.

Market: any place where buyers and sellers meet to trade products

Market growth: an increase in total market sales eg sales rise by £5m over 12 months

Market research: finding out and analysing information about potential customers, markets and products

Market share: The percentage of total sales in a market accounted for by one firm

Market size: total sales of all the firms in a given market eg the pizza take away market is valued at say £300m a year

Marketing: identifying what customers want and providing matching products

Marketing mix: the combination of factors firms use to create products that meet customer needs. Often called the 4Ps: price product promotion and place

Maslow's hierarchy of needs: a motivational theory that seeks to explain why workers take jobs want to work, gain promotion etc

Maternity/paternity leave: the legal right to paid time off work following the birth of a worker's child. Their job is held open.

Meeting customer needs: when a firm's products satisfy the requirements of buyers

Mortgage: a loan used to buy property. The property acts as security for the loan.

Motivation: encouraging staff to do a job better than they otherwise would

National insurance contributions (NICs): compulsory deduction from wages to pay for benefits such as job seekers allowance

Net cash flow: the difference between money coming in and money going out over a period. Equals cash inflows ie receipts minus cash outflows ie payments over a given period of time

Objective: a target a firm is trying to reach eg make large profits. What a business wants to achieve - its aim

Organisation: 1) a business 2) the internal structure of the business

Overdraft: when the bank allows a customer to spend more than it has in its bank account

Overheads: fixed costs such as office rent and administrative staff salaries

Overtime: a payment made to staff for working extra hours over and above the basic week - usually at a higher rate eg double time

Owners: someone to whom something legally belongs eg by law, a company legally belongs to its shareholders

Part-time work: staff are employed for a fraction of the working week eg 10 hours

Penetration pricing: Setting a low price for a new product to gain trial purchases and sales

Personal selling: Firms discuss products with customers on a one-to-one basis

Piece rate: a method of payment where workers are paid for each item produced

Pressure groups: organisations that aim to influence decision makers

Price: the amount of money a customer pays for a product or the amount firms charge customers

Primary (field) research: a firm gathers new information for the first time using field work eg by doing survey

Private limited companies (Ltd): a business with its own legal status owned by shareholders who have limited liability. Shares cannot be offered for sale to the general public or sold unless other shareholders agree

Producer: a business that creates goods or a service

Product: a good or service used to satisfy a want or need

Product differentiation: making an item different from its rivals eg through design, packaging or brand logo

Product features: the characteristics of a good or service eg its function (what it does), appearance, size, colour and after sales support

Product life cycle: The period of time consumers are willing to buy a given product – products go through different stages

Product mix: Product mix is the range (portfolio) of items sold by a business

Product portfolio: the range of items or brands an organisation has on sale at any one time

Product trial: when customers buy and try out an item to see if it is worth buying again

Production: the business activity of using resources to make goods and services

Productivity: The number of items produced by one worker in a period. Divide total output by number of staff employed

Profit: the money left over from sales revenue once all costs have been paid. Eg if sales revenue = £100 and costs = £75, then a £25 profit has been made

Profit margin: The difference between the price received by a company for its products and the cost of providing them. Often states as a percentage.

Promotion: any activity that makes people more aware of a product or business eg advertising

Promotional pricing: Reducing prices to boost sales of a product eg holding a sale

Psychological pricing: Setting price to make a product seem cheaper and so better value for money eg £4.99 instead of £5.00

Qualitative data: gives information describing feelings, opinions and judgements eg why customers prefer one brand to another

Qualitative research: finding out and analysing information about potential customers attitudes and opinions

Quality: the ability of an item to meet standards set by customers

Quality assurance: ensuring quality is delivered at each stage of the production process

Quality control: the inspection of products to check they meet set standards

Quality management: the system used to delivery quality eg quality control or quality culture (assurance)

Quantitative data: gives number information about facts and figures eg 54% of customers buy brand X

Quantitative research: finding facts and figures about customers, competitors, markets etc eg 45% buy a newspaper each month

Quotas: A limit set by government on the amount of a product that can be imported

Regulations: rules that restrict behaviour

Remuneration: the way staff are paid eg a salary, piece rate, etc

Repeat purchase : customers keep buying the firm's products

Research and development: work undertaken by a business to discover new products and improve existing products. R&D.

Resource depletion: when natural resources are used up and not replaced

Resources: items used to help make products ie land labour capital and enterprise

Results based payment methods: any payment system that rewards staff for outcomes eg piece rate, commission and bonuses

Retailer: a shop

Retaliation: When other countries respond to tariffs & quotas with their own protection measures

Revenue: income earned by a business from sales over a period

Rewards: the benefits of activity eg profit, excitement or job satisfaction

Rights issue: the offer of new shares to existing shareholders by companies wanting to raise finance

Risk: the possibility of difficulty or loss from a business activity

Risk taking: a willingness to take a chance

Rivals: competitor firm offering similar products to customers

Salary: a method of payment made to non-manual staff for work done - normally paid monthly

Sales of Goods Act : a civil law that helps customers get their money back if there is a problem with their purchase

Sales promotion: Schemes that have an immediate impact on sales eg BOGOF or discount coupons

Sales revenue: The amount of money a business earns from selling its products over a period. Eg £250,000 of DVDs were sold in November. Also called sales turnover

Sales volumes: the amount of products sold over a period eg 50,000 DVDs were sold in November

Secondary (desk) research: a firm collects data from existing information already published eg government statistics, or past sales records

Self-actualisation: worker's desire to achieve something. Met by letting staff control their own work

Self-esteem: worker's desire for recognition. Met by praising staff or awards eg 'worker of the week'

Share capital: the amount of money invested in a company by shareholders

Share issue: companies sell new shares to private investors to raise finance that does not need to be repaid

Shareholders: Someone who has bought shares and so owns part of a company

Shares: A certificate giving part ownership of a company

Short term finance: funds raised to finance business activities for up to 12 months eg an overdraft

Shortages: when demand exceeds supply and customers cannot buy the product at the current prices

Social costs: The costs of business activity to everyone and the environment eg pollution

Source of finance: the origin of money a business has eg a bank or owners

Staff: employees

Staff attitude: employee's way of behaving

Staff skill: the ability of employees to do an activity or job well

Stakeholders: anyone with an interest in a business eg owners, staff, customers and community

Start-ups: a new business

Stock: Materials and components stored by a firm for eventual use in manufacture, and finished goods awaiting sale

Stock control: the method used by a firm to decide on stock levels

Stock level: the amount of inventory held by a business

Stock market: the place where shares are bought and sold

Stock market flotation : when a private limited company converts to being a public limited company and offers shares for sale to the general public

Strategy: long term plan of action by which the organisation intends to achieve its objectives

Subordinate: A subordinate is an individual reporting to a manager

Subsidiary: A business owned by another business

Survey: gathering data by asking people questions

Sustainable production : when resources taken from the environment are replaced eg new trees are planted to replace those cut down for timber

Tariffs: An indirect tax on imports

Temporary work: a job with a business for a limited period of time eg 3 months

Temporary workers: staff hired by a business for a limited period of time who are expected to leave at the end of their fixed term contract

Time based payments: Any method of paying staff based on hours worked eg wages and overtime

Time rate: A method of payment where staff are paid for each hour worked

Total costs (TC): The entire amount spent by a firm making its products over a period. Total cost = Fixed costs (FC) and variable costs (VC). TC = FC + VC

Total revenue (TR): The entire income earned by a business from its sales over a period. Total revenue = price x quantity. TR = P x Q

Trade Credit: suppliers agree customers can pay for products sometime after they take delivery eg within 28 days. In effect trade credit is an interest free loan

Trade off: the process of making a choice between alternatives

Trades Description Act: is a criminal law that makes it illegal for firms to sell products in misleading ways

Training: The process of teaching staff the skills needed to do a particular job or activity

Unit cost: the average cost of making one item

Value added: when the price of an item is higher than the cost of all the resources used. Consumers value items more than the costs paid to suppliers.

Value added tax (VAT): a tax on the sale of goods and services

Variable costs (VC): expenses of production that change as the amount produced changes eg wages and materials

Wages: a payment made to employees for working a fixed number of hours

White-collar workers: non-manual staff usually paid a salary eg secretaries and sales persons

Zero defects: all work meets quality standards