Business

A Level | Edexcel | 9BS0

Theme 3: Business Decisions & Strategy

Course Companion for A Level Edexcel Business

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Teacher's Introduction

This resource has been written to support the learning and teaching of Ede
Business (Theme 3: Business Decisions and Strategy). It gives an in-depth v
presenting what specification points students need to know, plus extras alo
learning.

At the beginning of each chapter, you will find a list of contents showing ev
covered. There are also questions and answers at the end of each chapter t
their knowledge into real-world business contexts.

Students get plenty of chance to practise their quantitative skills in this res

- **QS 1:** calculate, use and understand ratios, averages and fractions (cha
- **QS 2:** calculate, use and understand percentages and percentage chan and 3.5.3.)
- **QS 3:** construct and interpret a range of standard graphical forms (cha
- **QS 6:** calculate investment appraisal outcomes and interpret results (c
- **QS 8:** use and interpret quantitative and non-quantitative information (all chapters)
- **QS 9:** interpret, apply and analyse information in written, graphical an (all chapters)

While extremely valuable to a student's revision, this resource should be tr
the many other textbooks and activity guides available. As with any subjec
as possible!

The subjects covered in this resource include everything from corporate cu
strategy, mergers, takeovers and decision trees. The notes included in this
students before a lesson as preparation for a topic, afterwards in order to h
or can be used by teachers as a supplement to in-class exercises and activi

It is hoped that this resource, as well as offering support for teaching the e
Edexcel examination, will help students build on their research and dissem
world is a constantly changing one full of fascinating stories. This resource
these stories as a basis for teaching in the most interesting way possible, m
study from the next generation of business analysts!

Happy teaching!

3.1. Business Objectives and Str

3.1.1. Corporate Objectives

! *Key Points Covered*

- Mission statements
- Corporate and functional objectives
- Critical appraisa

The Mission

Many organisations, especially large ones, develop missions for themselves. The m ongoing purpose of the company, i.e. why it exists. Missions are generally qualita cannot be achieved through numbers.

The Mission Statement

This is how a company communicates its mission to its stakeholders (such as custo suppliers and potential investors).

Some example mission statements:

- **Nike**
  Mission: 'To bring inspiration and innovation to every athlete in the world.'
  Source: ***http://help-en-us.nike.com/app/answers/detail/a_id/113/~/nike***
- **Microsoft**
  Mission: 'To enable people and businesses throughout the world to realise th
  Source: ***https://www.microsoft.com/enable/microsoft/mission.aspx***
- **Virgin Atlantic**
  Mission: 'To embrace the human spirit and let it fly.'
  Source: ***http://www.virgin-atlantic.com/gb/en/footer/about-us.html***
- **McDonald's**
  'Our aim is to provide a fun and safe environment where our customers can e quality ingredients at affordable prices.'
  Source: ***http://www.mcdonalds.co.uk/ukhome/whatmakesmcdonalds/qu business/business-strategy/i-am-trying-to-find-the-mcdonalds-mission- studies-students.html***

Aims and Objectives

Corporate Aims

While a mission statement sets out the main reason for a company's existence, the firm wishes to develop. Corporate aims are set out by a company's director(s) as g their corporate and functional objectives. For example, every manager of a superm focus on profit maximisation and diversification when it comes to considering cor i.e. if any proposed objectives do not fall under diversification or profit maximisati

Business Objectives

There are two types of business objective: *corporate* and *departmental/functional*. company-wide goals for a firm. Functional objectives, on the other hand, focus on of the business. Functional objectives are set out in order to achieve the corporat objectives exist in order for a business to achieve its mission and corporate aims.

! Good to know!
When companies talk about 'business objectives', they are generally referring t

Common Business Objectives

When a business sets its objectives, they are generally in reaction to something (e
a way to prevent adverse circumstances (e.g. lack of profitability).

- **Profit maximisation:** this is the pursuit of creating the largest gap between
The more profit a company makes, the more dividends it can pay to its share
left over for reinvestment.
- **Survival:** this is a common objective for many firms. It is set up as a way to e
of time (e.g. stay above water for the next two years). Companies often use c
diversification into other areas) as a way to survive.
- **Growth:** this has links with survival. Companies set their objectives on growt
market position and, as a result, generate more sales.
- **Diversification:** this objective is used in order to spread risk of the business,
ensures that when one product becomes obsolete it doesn't spell the end of
- **Cash flow:** if a company is making significant profits but also spending a lot,
paying its bills from month to month. As such, some businesses set their obj
cash flow so that they do not become consumed with debt.
- **Ethics:** some businesses, such as non-profit charities, have ethical objectives
profit-centred companies may only set their sights on ethical issues once the
brand image.

Whatever objective a business sets itself, it must be **SMART**.

Specific:	the objective must have an actual target (e.g. reduce waste by 1
Measurable:	there must be some way of assessing this objective
Agreed:	management and subordinates must come together on the obje objective without discussion, employees could become demotiv
Realistic:	by discussing the objective, management and employees can ag target
Time-bound:	it is much easier to assess an objective if there is a time limit (e.g the next three years).

Good to know!

*While missions and corporate aims constitute the general direction of the compa
businesses use as targets, to understand how successful something is. Managem
'become 10 per cent more profitable in the next two years') because they can be*

*Success, however, does not simply come from an objective, no matter how good.
attainable objectives when they have a clearly understood mission.*

Each level works to support the level above

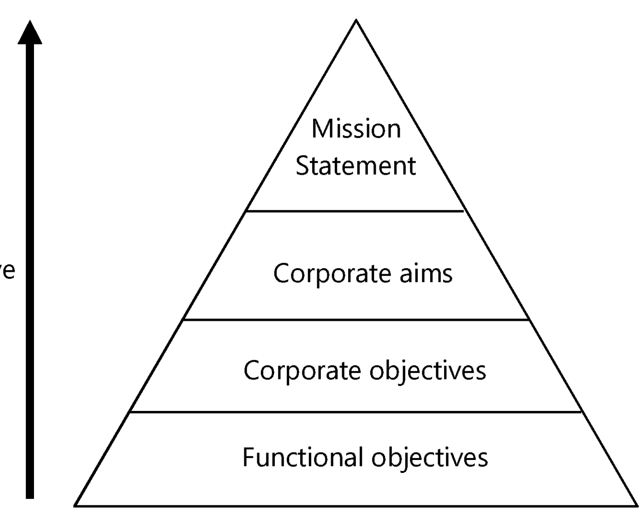


Diagram: The hierarchy of objectives

Critical Appraisal of Mission Statements

Not every company makes a mission statement. Very few do in fact until they dev
Even then, it is important for the business to regularly appraise its mission stateme
for? Does corporate strategy reflect this?

There are benefits and issues that come with setting out a mission statement.

Benefits of Setting a Mission Statement:

- No matter how widespread geographically, every member of the organisation u towards
- Having a mission statement makes decision-making easier, i.e. management ca the overall mission
- Employing a mission can give responsibility to a workforce, helping improve m

Limitations of Setting a Mission Statement:

- If it is unrealistic, the mission statement may get ignored
- If the mission statement says that the company will involve all members but th from employees, this can cause demotivation of the workforce
- Mission statements are only effective if everyone supports them

Stakeholder Perspectives

Businesses have many stakeholders, from workers employed to do a particular tas
looking to make an investment. A firm can, therefore, be viewed from a variety of

Stakeholder	Possible Interests
Employees	• Regular income • Job security • Safe place of work • Opportunities to further career
Customers	• Fair prices that do not fluctuate • Safe products • Good customer service and after-sales service
Shareholders	• Increase in dividends • Rising share prices
Creditors	• Repayment (on time) • Return on any investments made
Suppliers	• Secure supply contract to businesses • Fair prices
Local Community	• Local employment • Low levels of pollution (noise, air, light, etc.) • Business gives back to the local community

3.1.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

1. *What makes a business objective SMART?*
2. *Look back through the mission statement for Nike at the beginning of this sec following:*
   - **a.** *At which stakeholder is the mission aimed?*
   - **b.** *What is the intention of this mission statement?*
   - **c.** *Identify which stakeholder(s) would greatly benefit from the mission stat*

3.1.2. Theories of Corporate Strategy

! Key Points Covered

- Development of corporate strategy
- Theories of corp

Development of Corporate Strategy

Much like the difference between corporate objectives and functional objectives, t by its *corporate strategy* while *functional strategies* are put in place in order to fulf

Businesses analyse potential strategies in a variety of ways, including Ansoff's mat

Ansoff's Matrix

This model helps a business analyse its strategy through the products that it offer competing in. Ansoff's matrix describes four types of strategy:

- **Market Penetration:** when a business sells more of its already-existing produc achieve this through strong product promotion and pricing initiatives, among o Supermarket chains, such as Tesco, use this strategy as a way to increase thei
- **Product Development:** this is the development of a new product (or innovatio which is then introduced to an existing market. Companies work on product d improvements to packaging or innovation on ingredients.
  Coca-Cola has innovated on its soft-drink brand many times over (e.g. *Vanill Life*) and continues to pour cash into research and development.
- **Market Development:** businesses aim at a new segment, such as introducing t repackaging to teenagers. Firms achieve this through pricing initiatives, promo methods.
  In the mid 2000s, Nintendo sparked a new trend in video gaming by marketi consoles to the *grey market* (older market) with titles such as 'Brain Training'.
- **Diversification:** this is the highest risk wherein companies enter a new market the product will help the company spread its risk, i.e. if one market/product fai pick up the slack.

Richard Branson's Virgin brand is a great example of diversification. Virgin has mo drinks, records, air travel, broadband Internet, and now space travel with Virgin Ga

Markets \ Products	Existing	New
Existing	**Market Penetration**	**Product Development**
New	**Market Development**	**Diversification**

Diagram: Ansoff's Matrix

Uses of Ansoff's Matrix:

- A business can better understand the options that are available to it, choosing
- Ansoff's matrix also helps businesses concentrate on the elements of the mark affect them

Drawbacks of Ansoff's Matrix:

- The four cells of this model do not always line up with real-life business
- Ansoff's is the most commonly-used model in strategy. As such, if a business r look to other strategies that are not being used by their competitors.

Porter's Strategic Matrix

Michael Porter first published his generic strategies model in 1985. Since then, his strategic matrix) has taken prominent position in the world of business as an effec gain competitive advantage over rivals, either through a firm, a brand or a produc

Scope		**Cost**	**Differentiation**
	Mass Market	Cost Leadership	Differentiation
	Niche Market	Cost Focus	Differentiation Focus

Source of competitive advantage

Diagram: Porter's Generic Strategies (Strategic Matrix)

Porter's model shows us three generic strategies:

Cost Leadership: this is when a firm leads the market in terms of the lowest possi generated). Businesses running the cost leadership strategy may still sell at the m the absolute minimum (below their rivals). Other businesses meanwhile beat thei their selling prices even further in order to kill off any competition. Businesses use chain innovation as means to achieve cost leadership.

This strategy looks inwards at a business, examining internal actions in order to m example of a cost-leadership business. The company consistently strives to keep competition. One way the business can do this is by purchasing supplies in bulk.

Differentiation: businesses work towards differentiation through innovation in or This strategy requires significant research and development, a highly efficient wor in order to succeed.

This strategy looks outwards from a business to better understand customer need a good industry example here. Sir James Dyson famously worked on 5,127 protot before he finally found success in the mid 1990s.
Source: ***http://gizmodo.com/5790556/praising-failure-james-dyson-talks-va***

Focus: companies concentrate on providing a specialised service to a niche marke differentiation-focused.

Mondelēz International, Inc. (formerly Kraft Foods, Inc.) is a good example of focu concentrates on a particular area: the processed food and beverages market.

Uses of the Strategic Matrix

- It helps businesses better understand the options of competitive advantage av
- By understanding the options available for competitive advantage, companies e.g. to enter a differentiation-focused, niche market, businesses are unlikely to aimed at a mass market

Drawbacks of the Strategic Matrix:

- Porter claimed that a business must fit into one single category in order to ach there are many example companies that buck this trend
- If the market changes, the business's strategy would no longer be relevant

Aim of Portfolio Analysis

Rather than just one product, many businesses have an entire portfolio. This help failing, it can be supported by other more profitable products.

Created by the Boston Consulting Group in the 1970s, the Boston matrix classifies market share and the growth rate of the market. The Boston matrix helps busines should keep/discard and which new products they should add in order to strengt decide this by focusing on market share and growth. Both are important element share represents the possibility of strong customer loyalty for a company while m opportunities for expansion.

		Market Share	
		High	**Low**
Market Growth	**High**	Stars	Problem Children
	Low	Cash Cows	Dogs

Diagram: The Boston Matrix

Stars: the leaders in business, stars achieve high share in a market that is experien increasing sales revenue for a company. However, high-growth markets are very the company will most likely need to invest highly in advertising and promotion, l Nevertheless, after all the product promotion, a star should bring about significan less-profitable products.

YouTube is an example of a star. The service continues to grow, with people usin in a lot of money for its owner company, Google, but requires significant amounts the competition.

Cash Cows: these have a large share of a low-growth market. Cash cows are norm markets. The low growth of these markets makes them less attractive to competit required. Having lots of cash cows is good for business as they earn lots of cash. though, and so might use the cash from these to reinvest in company processes.

Coca-Cola is a good example of the cash cow: the company's product range repre beverage market, though the market itself changes very little (i.e. competition sta

Questions Marks: also known as *problem children*, these are products that compe market. The potential for the product to generate sales increases but the actual m the same. Many products start as question marks and so require much market re successful, however, they can become cash cows or stars.

An example of a question mark is 7UP. Owned by Pepsico, 7UP uses up a lot of re but brings in very little, compared to the Pepsi product itself.

Dogs: in a low-growth market with very little share, these products are the most u times are tough, the dogs get dropped first. Still, there are some products, such a share of a low-growth market and still manage to generate millions in revenue.

An example dog product is the cassette tape. Most people use either CDs, MP3 p play/record music. Though some people are trying to bring it back as a vintage it cassette tape remains on the rubbish dump of forgotten business fads.

Benefits of the Boston Matrix:

- Very simple to understand
- Businesses can see where to place their cash reserves in order to grow / becom
- As it is simple to understand, it is also easy to test potential strategic ideas

Limitations of the Boston Matrix:

- Getting data on the market can be difficult
- It is two-dimensional (looking at only share and growth)
- High market share does not mean never-ending profits

Achieving Competitive Advantage through Distinctive Cap

We looked at competitive advantage with Porter's strategic matrix. Another way t model of distinctive capabilities. Kay breaks down the possibilities for competitive capabilities: *architecture*, *reputation* and *innovation*.

Architecture

This is the network of internal (employees) and external (suppliers, customers, etc.) company. Firms must nurture an environment of cooperation in order to be succe

This involves:

- positive management of relationships (e.g. company to employee, supplier to c
- encouraging individuals to meet the aims of the company
- creating and maintaining a culture of cooperation

Reputation

Kay's model considers quality as absolutely vital for companies in gathering comp cannot afford a product, they will be turned off. Likewise, if it is priced too cheapl low value.

Reputation involves:

- conveying to consumers the quality of a company's products. This is especiall goods, where quality does not present itself for a long time, or until after signi
- selling at a price that is neither too high (compared with lower quality) nor too

Innovation

This third capability is the most difficult for businesses to convert into competitive

This difficulty comes from the:

- costs and uncertainty associated with the innovation process
- management required in order to inspire innovation
- allocation of rewards, i.e. how a business decides whether the innovation was w

Distinctive Capabilities in Business

Most businesses exist in order to make a profit and so the success of a firm is dec to its inputs (e.g. raw materials, stock, etc.). All three of Kay's distinctive capabiliti to a business by giving it competitive advantage over its rivals.

Some examples of distinctive capabilities in business include:

- **Reputation – Coca-Cola:** the company has one of the largest marketing prese afford to continuously promote their brands all over the world.
- **Innovation – Apple:** the Californian tech giant continually invests in its own re helps the firm stay ahead of the curve when it comes to unleashing the 'next b
- **Architecture – Google:** the company started in 1998 and has since become th (source: Alexa, ***http://www.alexa.com/siteinfo/google.com***). Google has m worldwide. Rather than directing their staff, Google's management operates a listening to, and acting upon, new ideas. Employees are allotted innovation tir ideas, which is how the company came up with its Google Maps service.

Now it's your turn:

Work alone or with a partner. Write a list of 10 businesses that operate in you following questions:

Which businesses have competitive advantage? Use Kay's method to explain w
Which businesses are failing to achieve competitive advantage? Use Kay's me

Effect of Strategic and Tactical Decisions on Human, Physical

Much like the decisions a manager of a football team has to make, businesses hav ones.

- **Strategic:** These are long-term decisions that a business makes in order to bu ultimate goals.
- **Tactical:** These are shorter-term decisions that a business makes in order to su

Each type of decision can affect a business's *human*, *physical* and *financial* resourc cutting costs by 10 per cent, for instance, can increase the amount of finance a bu time, decrease the motivation of employees since they now have fewer physical re their duties.

Decision	Strategic or Tactical?	Potentia
Product sales promotion	Tactical	*Financial.* Sudden increase in sale
Keep prices low	Strategic	*Financial.* Consumers associate b increase/decrease sales dependin
Employ more people during the Christmas period	Tactical	*Financial/Human.* Production leve though motivation is not necessa
Investment in training programmes	Strategic	*Human.* Motivation of employees
Purchase of new, improved equipment	Strategic	*Physical/Human.* If the equipmen production process, staff may beg successful, the business may have redundant.
Purchase a slot of television advertising	Tactical	*Financial.* The exposure may gen directly following the advert.
Purchase of new location	Strategic	*Physical/Financial/Human.* The b financial resources in order to gai this also becomes an asset which With a new location, the business case they will need to recruitment

Table: Strategic and Tactical Decisions and their Potentia

3.1.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

3. *Identify whether the following are normally considered tactical or strateg*
   a. *Purchase of full-page spread in a popular magazine.*
   b. *Regular appraisal of a company's customer service.*
   c. *Temporary partnership with another firm for cross-promotional purp*

4. *How do Nintendo and Lego differ in their distinctive capabilities?*

3.1.3. SWOT Analysis

!	Key Points Covered
• Strengths and Weaknesses	• Opportunities an

Businesses of every size take on SWOT analysis: this is the evaluation of a company *opportunities* and *threats*.

Strengths	Wea
Opportunities	**Th**

Strengths and Weaknesses

These are the *internal* factors affecting a business within its control, such as:

Strengths	W
• innovation	• limited opportuni
• quality	• high staff turnove
• efficiency	• too many product
• research and development	• poor communicat
• investment in fixed assets	• bad reputation as
• training	• negative cash flov
• profitability	• limited experience
• communications	• poor location (i.e.

Opportunities and Threats

These are the *external* factors affecting the business that it cannot change. Firms their external environments, such as:

Opportunities	
• new markets opening abroad	• ageing population
• low wages and high unemployment	• taxes increasing fo
• fall in exchange rate (good for exporters)	• maturation of pro
• social trends shifting to 'green' products	• competition levels
• main rival is in financial trouble	• pressure groups t
• government policy encourages spending	• technology makes

Let's use some examples:

Large Book Retail Chain

The following SWOT analysis shows the factors surrounding a large book retailer, gain as much market share as possible.

Strengths	Wea
• Has a reputation for high quality • Many fixed assets (i.e. book stores nationwide) • Employs staff with knowledge of literature	• Literature trends books are often life cycle
Opportunities	**Th**
• Expansion abroad • Less successful chains that are in financial trouble could be purchased	• Competition is h • Anti-chain-store against large bra

Independent Café

The following SWOT analysis shows the factors surrounding a small, independent business is survival.

Strengths	Wea
• The café is an established part of the local atmosphere • Few employees means communication is easy	• Profitability is lo • Cash flow is also
Opportunities	**Th**
• A store down the street is closing down and could be purchased • Social responsibility and local support are becoming more important to the residents	• Rival cafés are lo market • Population is cha children and goi

Small-scale Framing Manufacturer

The following SWOT analysis shows the factors surrounding a small-scale framing produces hundreds of wooden picture frames every day. The main aim of the bus as possible.

Strengths	Wea
• Efficient workforce can produce hundreds of frames per day • The business's location and equipment are valuable assets	• High turnover of • Produces lots of any real specialis
Opportunities	**Th**
• Unemployment is currently low and so no problem finding staff • Potential new markets in manufacturing different products	• Online traders o more convenien • Technology will firm should too

With all of these examples, the SWOT analysis can be used to make effective strat decisions. The large book chain, for instance, is looking to grow market share and opportunities abroad. Likewise, it could react to the threat of pressure groups by well-known branding. The strategy of the independent café, on the other hand, is investigate cash flow as a means of achieving its goals. Finally, the framing manu profitable as possible and so perhaps will look to specialise in order to produce o better than any of its rivals, which (if successful) will help make it more profitable.

3.1.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

5. *Identify two strengths and two weaknesses of your local supermarket.*

6. *Below shows a SWOT analysis for Royal Mail. Fill in the empty sections to com*

STRENGTHS	WEA
• .... • Able to offer the same service to customers across the country	• Low presence on digital platforms • ....
OPPORTUNITIES	**TH**
• Online shopping market continues to grow, bringing more postal business •	• .... • Drones and other postage

3.1.4. Impact of External Influences

! Key Points Covered

- PESTLE Analysis
- Porter's Five For

The lower two sections of the SWOT analysis, opportunities and threats, appear in m

PESTLE

This form of analysis (sometimes referred to as PESTEL or LE PEST) looks at six ext affect a business.

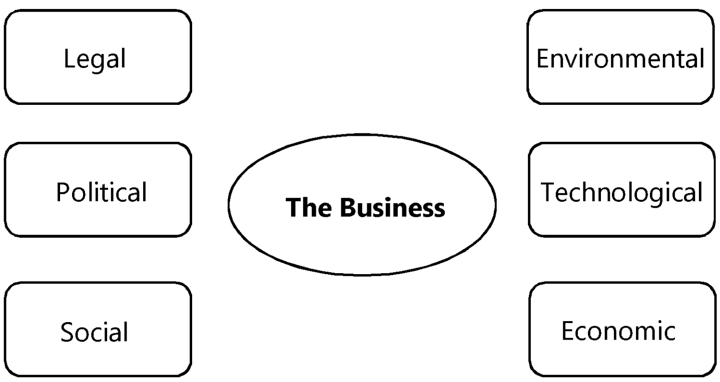


Diagram: PESTLE Analysis

Each element of the PESTLE analysis poses potential effects to a business.

Political

Taxation, whether direct (e.g. corporation tax) or indirect (e.g. value-added tax, or V taxes are increased, businesses must compensate for this somehow. Firms that ch scare away potential consumers while firms that lower their production costs may products and, therefore, suffer in lack of sales.

The European Union (the EU) is another element of this factor. Businesses that op to millions of customers and skilled workers. Firms within the EU can also achieve purchasing in bulk without the high import/export costs. On the other hand, busi standards, which may bring about high setup costs. The free movement of people exceptional labour and materials may go to other EU nations, where they may pre business. This might result in higher production prices and/or lower quality of wo

Economic Factors

Consumer demand increases as an economy moves through the business cycle (i.e recovery and boom). With a rise in demand, companies are able to generate mor increases cash flow, opening more opportunity for investment and employment o

Exchange rates can affect businesses too. A fall in exchange rate, for instance, wo sell their products/services abroad. Rates of unemployment can also greatly affec a highly skilled, low-value workforce increases when employment goes down.

Social
Fashions come and go; this can be devastating for a company that relies on trend demographics are another factor that firms must consider; if the average age of a from 20 years old to 50, businesses must be able to react, otherwise they will find

Ethical business practices have grown in importance for the average consumer an factor is limiting the number of sales they could make. Likewise, pressure groups if a company is doing something that the general public believes to be unethical,

Technological
New, improved processes and rival products are two of the many factors here tha new processes might be available for the business to use or they might be what t market. If the business is using the process, it might increase its efficiency and re are using this technology, on the other hand, it could represent fewer sales for th move on to the competition.

In either scenario, a business must also consider the costs of change involved, i.e. new technology or how much it might lose from not taking on the technology.

Legal
With all employment legislation, such as the Equal Pay Act (1970) and the Disabili are costs involved. Businesses must comply with legislation and so may need to p facilities, which can be a drain on cash flow. On the other hand, a business that co without using 'loop holes') can look attractive to consumers, workers and potenti sales, availability of highly skilled workers and more investment opportunities.

Environmental
Corporate social responsibility (CSR) is an integral element to many businesses. S become law, such as the Climate Change Act (2008); this aims to reduce the carbo business practices.

If a firm voluntarily becomes more environmentally friendly (e.g. by recycling ever attractive to ethical consumers. This change in strategy can also attract more hig by environmental values. If recycling everything requires particular skills, the busi who have the relevant experience. These workers will perhaps be more expensive production costs of implementing such a system could be great, too. However, th value to the company (i.e. competitive advantage), especially if no other rival is wo

The Changing Competitive Environment
Most markets are dynamic. The influence that each of PESTLE's external factors h change at any moment and so their power often fluctuates. If new legislation is b businesses will have to comply, causing a rise in operating expenses. However, o expenses will go down and businesses will have more cash flow. The same goes f are acting more ethically because their consumers expect it. If this trend ever cha likely have to change too.

Michael Porter's Five Forces model also shows how external factors can lead to ch competitive environment.

Porter's Five Forces

Michael Porter (remember his strategic matrix from earlier in the resource?) descri
of a market as determined by its key external factors.

The structure of a dynamic market is constantly changing and so, in order to achie
good information on every external factor. This way, businesses can react accordi

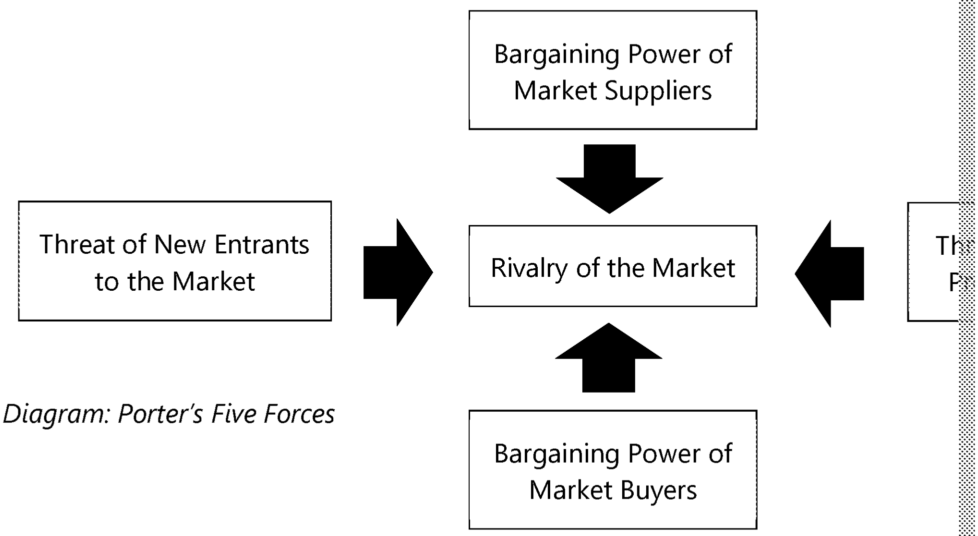


Diagram: Porter's Five Forces

New Entrants

Firms that already exist within the market need their goods to be at the right qual
compete should a new competitor enter the market. Likewise, businesses work on
unique selling points (USPs) of their products in order to stand out from the crow

Businesses look at *barriers to entry* when deciding whether to join a market; howe
existing firms. A market with high barriers to entry (e.g. the telecommunications m
amounts of infrastructure) can benefit already-existing businesses, which have a lo
goods. If a big business decides to enter the market, the already-existing firms co
firms, in order to prevent this loss, draw up exclusive agreements with suppliers in
market.

Substitutes

These are the alternative products/services that a consumer might want to buy ins
The Mars bar, for example, is in direct competition with the Toffee Crisp (i.e. it is a
the Mars bar could be an orange, as it is still considered a snack food though it is
better than!) the Mars bar.

The power of substitutes will depend on many elements, including *price*, *perceptio*
an orange is cheaper, more convenient and perceived to be a better buy than the
move away from the product. It will then cost the company a lot in time, budget a
decide to try to win back their market.

Buyer Power

If a market has many producers but only a few consumers, the buyers have a lot o many consumers and few producers, buyer power is much less significant. Imagin store was a barber shop, the consumers would probably benefit because every ba price and quality. If there was only one barber shop, however, the power would b would have no choice but to buy from them.

Consumers that buy in super bulk have significant power, too. Take a cow farm, fo a large supermarket chain) purchases most of the farm's milk, the farm becomes v The farm now has a regular buyer (the supermarket) but that buyer has a lot of po commanding price reductions and changes in quality.

Changes in technology give more power to the consumer and seller, too. While p banners and promoted placement on search engines such as Google, consumers a right at their fingertips. If a consumer wishes to know the price of a good in orde price is fair, it does not take too much searching online to find out.

Supplier Power

When there are many suppliers to a market, the power that each one has over the the source of goods/services is focused to a select few suppliers, those suppliers h Suppliers in this position can heavily influence prices and standards of quality. An supply is to collude with other businesses in order to decide what to charge and t illegal in most of the developed world, though can still occur (especially if it is not

Microsoft is a good example of how a supplier can gain control over the market. W may not have the most up-to-date image any more, the business is still responsib systems used worldwide (i.e. Windows). As such, the power that Microsoft has ov

3.1.4. Questions

Please write your answers on a separate piece of paper or in an exercise book.

7. *How might the threat of substitutes affect the traditional newspaper market?*
8. *Explain how a small construction business might be affected by economic facto*

3.1. Answers

1. *SMART objectives: specific, measurable, agreed, realistic and time-bound.*

2. **a.** *Students may argue that Nike's mission statement is aimed at its cust will be professional or amateur athletes. Others may argue, then, tha aimed at its shareholders. Overall, the mission statement is aimed at the business practices of Nike and the quality that the business provid*
   b. *Nike appears to incite support for its brand by explaining its intentio*
   c. *Customers would certainly benefit from this mission statement as the to both inspire and support innovative, new products. Suppliers also to innovation, and, therefore, production, could lead to further busine could benefit from this mission if it leads to further innovation in the sharing of responsibility. Shareholders (and the business itself) would selling to every athlete in the world, Nike increases its profits and its*

3. **a.** *Full-page spread in a magazine is tactical because it is a short-term gain more exposure.*
   b. *Appraisal of customer service is a strategic decision because the comp processes are at a standard that encourages repeat business from co*
   c. *Cross-promotional partnership is tactical because it is a temporary m reach more customers. However, once this partnership is over, those company.*

4. *Lego, for instance, has a reputation for selling at the right price: neither to low (implying poor quality). Nintendo, on the other hand, normally releas companies present their products well; however, Nintendo's products are evolving technologies, while Lego's main product has stayed the course for innovated by creating new forms of video gaming. Lego, on the other hand forms of entertainment (e.g. films) related to its main product.*

5. - *For strengths, students might mention profitability, quality, reputatio many others).*
   - *For weaknesses, students might mention staff turnover, reputation an*

6. - *Another strength might be the reputation that Royal Mail has built as the UK.*
   - *Another weakness might be the fact that it has so many physical locat many customers access the services online.*
   - *Another opportunity might be the continual integration of technology*
   - *Another threat might be rival companies, such as FedEx and DPD, wh*

7. *Students should show understanding of the substitutes that are available, television and blogs. As consumers put more faith in these substitutes, esp convenient and even free, the newspaper market has the potential to shrin to compete in different ways, those choosing not to change being left in the*

8. *Students should show that economic factors can be positive and negative. instance, highly skilled workers may demand more in salary. As the econo skilled workers may be more willing to take a pay cut.*

3.2. Business Growth

3.2.1. Growth

! Key Points Covered

- Objectives of growth
- Problems arising f

Objectives of Growth

Most companies look to grow, but not every company has the same objective wh

Economies of Scale

As output increases and becomes more efficient, the average cost of production f technical economies of scale. Businesses achieve economies of scale in other way more a business buys in bulk, the cheaper raw materials can become on average.

Let's use an example:

2000 Teas Ltd is a beverage company that specialises in producing high-quality te its classic breakfast tea, which it buys from one main supplier in India. The cost of 1 kg. 2000 Teas Ltd sells its breakfast tea to supermarkets for £200 per 100 kg.

The calculation to find the selling price for 1 kg of breakfast tea is:

$$\text{Selling Price of 1 kg} = \frac{\text{Selling Price of 100 kg}}{100}$$

$$\text{Selling Price of 1 kg} = \frac{200}{100}$$

$$\mathbf{Selling\ Price\ of\ 1\ kg} = \mathbf{£2.00}$$

The difference between the selling price (£2.00) and the cost of raw materials (£0.5 Teas Ltd receives for every 1 kg of breakfast tea it sells. If, however, 2000 Teas Ltd breakfast tea it purchases from its supplier (i.e. buying in greater bulk), the compa lower price for the raw materials.

Let's calculate the difference again, but assuming 2000 Teas Ltd negotiates the co per 1 kg:

The difference between the selling price (£2.00) and the cost of raw materials (£0.4 continues to sell at the same rate, the company will make much higher profits due gain from buying in greater bulk.

Since 2000 Teas Ltd now pays less for its tea, it could bring down the selling price *generating more sales* and *increasing profitability* as a result.

Increased Market Power over Customers and Suppliers
Remember Porter's five forces model? Businesses are constantly at odds with one markets' suppliers and customers.

Let's use another example:
Frosty Glazers Ltd is a manufacturer of windows that buys its raw materials from a few main suppliers. These same suppliers provide raw materials to most of the window manufacturers in the market and so they can exert a lot of power in the form of setting prices and demands. Frosty Glazers Ltd understands that if the few suppliers decide to increase the price of raw materials, the company will have no choice but to pay it.

One manager at Frosty Glazers Ltd announces that she has found another supplie the same quality and at a lower price. The company starts buying from this suppl buyer over the other suppliers. Frosty Glazers Ltd is also able to reduce its prices competitive and gain market share over its rivals.

Increased Market Share and Brand Recognition
Most supermarket chains, such as ASDA and Sainsbury's, work tirelessly to increas become the one name people think of when they need to do their weekly shop). their customers (and potential customers) as well as push all manner of advertisin These could be anything from posters on bus shelters or double-page spreads in free offers, in-store demonstrations and loss leaders (such as selling televisions at selling price).

Firms often increase their market share and brand recognition as a short- to medi greater goal (strategy) of increased profitability.

Increased Profitability
Profit is the amount of revenue a business has left over once all *expenses and taxe* Profitability, meanwhile, shows how *capable* a business is of turning revenue into as a ratio). Businesses often achieve the objective of increasing profitability throu

- by purchasing raw materials in bulk, a business can decrease its total costs
- by increasing its output, a business can decrease its average operating costs
- through aggressive marketing, a business can increase brand awareness on a v
- by decreasing selling prices, a business can make more sales overall

Problems Arising from Growth
Growth is generally a good thing for business, but there are a few minefields to m

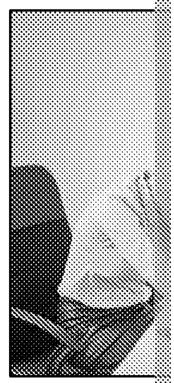
Diseconomies of Scale
Let's look at 2000 Teas Ltd again:

The company is able to sell 100,000 kg of breakfast tea every month (mostly to su 12,000 kg every month. This amount is enough to fulfil demand and have some le fluctuations in demand.

Encouraged by the number of sales generated, 2000 Teas Ltd decides to increase month. However, the company soon realises that demand does not meet this sup raw materials, which increases the total costs and, therefore, the average cost of 1

Internal Communication

Another diseconomy of scale can come from the expansion of a company's processes. As a firm grows in size, the internal network of communication can become more complicated and, therefore, less efficient. If a business grows to an unmanageable point, there is a chance that the bulk of the firm's employees lose sight of whatever vision or strategy they are working towards.



As a manager's *chain of command* grows, it may also become more difficult for subordinate employees to voice their opinions or receive support in pursuing their ideas. This can create rifts in the company and even result in demotivation of a workforce that feels undervalued.

Overtrading

This is a common problem with new businesses.

Cool Beans Ltd is a supplier of coffee beans, which it sources from plantations in C imports the beans and then roasts them and packs them for sale in the UK. Cool B company and so has very little in terms of workforce or infrastructure. Neverthele inundated with demand from the beginning.

Motivated by the influx of custom (mostly fr Beans Ltd has accepted far more orders tha company is overworking its staff and runnin keep up with demand. The workforce quick result and Cool Beans Ltd ends up letting do to loss of earnings for the company.

What seemed like a good idea at the beginn customers) ended up doing more harm to t

3.2.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

1. *Explain* ***two*** *reasons why a business will choose a growth objective.*
2. *Rising Batches Ltd is an independent bakers located in a large city. The compa several years and so its owners are considering an expansion of five additiona cities. What pitfalls could arise from this growth?*
3. *Tiny Desks Ltd designs and manufactures flatpack office furniture. 95 per cent company are sold to IKEA. The company believes that it is not being paid enou to develop more market power for itself. How could Tiny Desks Ltd do this?*

3.2.2. Mergers and Takeovers

! ***Key Points Covered***

- Reasons for mergers and takeovers
- Distinction between mergers and takeovers
- Horizontal and vertical integration
- Financial risks ar
- Problems with ra

Reasons for Mergers and Takeovers

Businesses take part in mergers and buyouts (takeovers) for many reasons, most o tactical or strategic.

Tactical reasons for a merger or takeover might include:

- to increase a business's market share
- to gain skilled staff
- to increase technology
- to gain ownership of intellectual property
- to expand to other locations

Strategic reasons for a merger or takeover might include:

- to increase profitability
- to achieve greater brand awareness
- to increase distribution capabilities
- to move a business into new markets

Distinction between Mergers and Takeovers

Mergers describe the coming together of two or more companies. The merger creates a new company that supports (as closely as is reasonable) the previous strategies of the merging companies. Any shares that each company previously had in their own businesses would be exchanged for shares in the merger company.

A famous merger occurred between mobile network providers Orange and T-Mobile, which came together to form the merger company EE. The merger, which happened in 2010, instantly increased the high-street presence of both com revenue to more than £6bn and giving us multiple advertising campaigns starring

A takeover describes the buying out of one company by another, which usually oc shares. Once a person or company owns more than 50 per cent of all shares in a taken it over.

One of the most successful takeovers of all time was that between Disney and Pixa Pixar had worked together on blockbuster smashes such as *Toy Story* and *Monster* production and design and with Disney leading marketing and distribution. It was sides. However, the partnership contract was coming to an end and so, instead o bought Pixar outright for around $7bn (USD). Since the acquisition, Disney and Pi international hits, including *Up*, *Toy Story 3* and *Wall-E*.

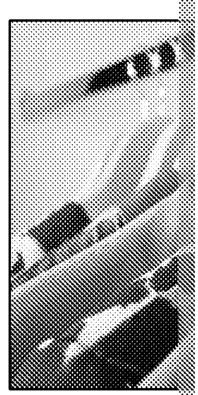
Horizontal and Vertical Integration

Mergers and takeovers can occur at different stages in the production process. H when one business joins another at the same stage of the production process (e.g while *vertical integration* describes when one business joins at a different stage in supermarket buying out a farmer).

Let's use an example:
Dress Nation Ltd is a British clothes retailer. The company has many competitors, online traders. Below shows how Dress Nation Ltd's production process might lo

PRIMARY STAGE	Supplier of raw mater
SECONDARY STAGE	Designer of clothin
TERTIARY STAGE	Manufacturer of cloth
QUATERNARY	Retailer of clothing

Diagram: the production process of Dress Nation L



Dress Nation Ltd is situated on the quaternary (fourth) stage of the production process, i.e. the company is the one selling products that have already been designed, manufactured and supplied. Dress Nation Ltd is now looking to grow and so it might decide to use horizontal integration or vertical integration.

Horizontal: if Dress Nation Ltd buys out another clothing retailer, the company is integrating horizontally. This is because Dress Nation Ltd and the other business are the same (i.e. within same industry sector), they are both clothing retailers.

Vertical: if Dress Nation Ltd purchases a clothing manufacturer, it will be integrati (i.e. different industry sector) and, therefore, entering another stage of the produc

Reasons for Horizontal Integration

This is a common form of integration as businesses can expand relatively quickly. choose horizontal integration, including:

- the buying company instantly increases their market share (assuming that the
- the buyers also benefit from economies of scale, such as having more machine more goods at a more efficient rate
- the expansion of a business can also help it enter a new market segment, such a business that operates in the north of England and, therefore, expanding its

Reasons for Vertical Integration

Many supermarket chains opt for this form of integration, i.e. purchasing a distrib their supply chain (e.g. farmers, wholesalers, etc.). There are many reasons busine such as:

- maintain and control the supply chain
- personally manage the standard of quality (e.g. the 2013 horse meat scandal o supermarkets did not keep tight enough control on their suppliers)
- keep supplies away from rival companies
- access to market, i.e. manufacturers may want to personally take care of their d to display and advertise their goods in the way they wish

Financial Risks and Rewards

As with almost any business venture, mergers and takeovers come with risks. How
can turn several smaller companies into multi-million pound successes.

The risks of a merger or acquisition may include:

- the costs of purchasing another business
- the costs of reorganising the businesses
- redundancies necessary as employees increase their roles or lose their value
- reworking of IT systems to ensure they communicate efficiently
- rebranding of businesses
- the obliteration of share value for either company

The rewards may include:

- revenue gained from the new business(es)
- economies of scale from spreading across organisations and markets, and incre

Problems with Rapid Growth

Successful mergers and takeovers are examples of rapid growth. Once a business
becomes bigger. There are some issues that come with this, including:

- diseconomies of scale, i.e. as the business expands, communications become m
- companies can become so large that they lose their strategic direction
- mergers and takeovers can result in all firms diluting their core competencies (
- clashes of corporate culture, such as one firm holding different values/ethics to
- local culture clashes, i.e. if one firm is bought out by a foreign business, this can

Good to know!

The difference between the company's aims and the actual results can lead to pr
clashes of corporate culture and demotivation of staff. Both outcomes would no
stakeholders in the beginning.

Diseconomies of scale can also occur, through convoluted communications, and
do not work. Examples of this include:

- staff from each firm may not wish to work together
- different IT systems may not function correctly when connected together
- employees may not be willing to share information/skills with their new collea
- the focus of one company may be too different from the other that is mergin

3.2.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

4. *What is the difference between a merger and a takeover?*
5. *Explain the difference between backward vertical integration and forward*
6. **a.** *Draw a vertical integration chain using the business types provided.*

   Supermarkets *Individual farmer* *Wholesaler*

   b. *What could the supermarket in this instance do to better control its s*
7. *International food conglomerates Heinz and Kraft Foods merged in 2015.*
   together many major brands, including Capri-Sun, HP Sauce, Heinz Bake

   Explain the possible reasons for why Kraft Foods and Heinz decided on th

3.2.3. Organic Growth

! ***Key Points Covered***

- Distinction between organic and inorganic growth
- Methods of growing organically
- Advantages and growth

In the previous chapter, we looked at mergers and takeovers. These are examples business instantly expanding its market reach and/or revenue through either purc company. The organic growth of a firm, on the other hand, is achieved by the bus with or being purchased by another.

How to Grow Organically

There are near-limitless ways in which businesses can grow organically. Some of t

Launching a new product/service

This can be an expensive venture but, if performed successfully, has the potential fo expand their consumer reach by releasing new goods or innovations on existing go Apple Inc., become renowned for their product launches, which are promoted as e

Increasing advertising and promotion

Many businesses achieve success because of the amount of time, money and effo Company, for instance, pours millions of pounds into its advertising budget every Christmas season) to make sure as many people as possible around the world kno

Opening new stores/branches

This is a common form of expansion, especially for start-ups that have grown bigg If a company is founded in Burnley and the owners notice market potential in Che achieve organic expansion by making the business available to both locations.

Introducing a new brand

This is more common with larger companies. Mondelez (formerly Kraft) owns hun continue to grow its product portfolio. When a company introduces a new brand existing brand), its sales potential increases because the firm can target more con products differently depending on where/who they are targeting (e.g. deodorant most countries outside the UK).

Market research and experimentation

This can be an expensive method for growth, especially if the company does not g correctly, however, a business can benefit greatly. McDonald's moved into the cra opening up small café-restaurants in Sydney and other areas. The restaurants, na very little McDonald's branding, serve items such as tofu, pulled pork sandwiches the restaurants is to test consumer reactions to other non-McDonald's foods in or chain should be adding to its menu.
Source: ***http://www.usatoday.com/story/money/business/2015/01/06/mcdon corner/21329109/***

Entering/leaving market segments

Businesses enter and exit market segments all the time. If a firm learns that it cou younger demographic, it could repackage its product/service in order to appeal to Conversely, if a product is not doing well in one particular segment (e.g. the teena unusual for a business to remove their product and repackage it for a different au

Expanding the business's workforce

Employing more workers not only helps a business to increase its output, but it ca otherwise may have been overlooked. The larger a business's workforce, the mor new ideas, products and services and, with any luck, generate more sales.

Advantages and Disadvantages of Organic Growth

The potential benefits of organic growth make it a very popular option for busine
beginning stages. Nevertheless, for every benefit, organic growth poses just as m

Advantages of Organic Growth

- it works out cheaper for businesses in the short term
- businesses have more control over their internal factors and so there is less risk
- organic growth means businesses are not forced to change their corporate cul
- maintenance of growth is more manageable (i.e. a business can control it to ho

Disadvantages of Organic Growth

- it is often a much longer process than inorganic growth, which can rack up lon
- the slow rate of organic growth also means it can take longer for the business the innovations of its competitors
- any funds for supporting growth are normally only invested into generating m
- organic growth is not always enough to sustain a business, especially if the bus market, which is particularly competitive

3.2.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

8. *What is the difference between organic growth and inorganic growth?*

9. *Why might a business choose to grow inorganically rather than organically?*

10. *In 2005, three former PayPal employees started YouTube. The very next year, for around USD 1.7 billion. Explain whether this constitutes organic or inorgan*

11. *Hillfarm Safari Park is a zoological centre based in the countryside of North W with local tourists, though its owners would like more visitors from outside No*

The owners have decided to focus on organic growth in order to increase the p two possible disadvantages to this decision.

3.2.4. Reasons for Staying Small

! ***Key Points Covered***

- Small business survival in competitive markets

Small Business Survival in Competitive Markets

Small, big or moderately sized, the majority of businesses are looking to achieve t

When a small business reaches a peak in profitability, it has the choice to either de remain small. In Chapter 3.1.2., we discussed Kay's model of distinctive capabilitie achieve competitive advantage by way of three key capabilities: *architecture*, *repu*

Many businesses have the ability to achieve these key capabilities because they re

Architecture

By remaining small, a business is able to maintain tight controls over its network o external (suppliers, customers, etc.) relationships. It can also be much easier for sr environment of cooperation than large ones because employees feel more directl their actions.

- **Positive management:** with a relatively short chain of command, business ow in company processes, which can help with motivation of staff and, ultimately,
- **Shared strategy:** since owners have a closer relationship with their staff, it is n strategic and tactical decisions. This also means that any changes can be disse efficient rate, allowing the business to react quickly to internal and external infl all its staff informed of aims and objectives, ensuring that all employees work t

Reputation

Kay's model tells us that quality is vital for a business when it comes to asserting c business as a small operation has its benefits here, too:

- **Flexibility:** with a short chain of command (compared to that of a larger firm), relatively quickly to any changes in customer requirements. This sort of flexibil reputation with customers and also works as a promotional tactic to entice mo
- **Customer service:** the flexibility of a business is increased by the fact that it is rather than reams of bureaucracy. As such, small businesses are also able to o comes to customer assistance. Once again, this improves the business's reputa and acts as an attractive element to any potential new customers.

Innovation

In Chapter 3.2.2., we showed how businesses that grow through inorganic means suffer from dilution of their core competencies. Some businesses choose to stay s ensure they continue to do what it is they do best.

- **Product differentiation:** small businesses can maintain their differences from areas of the market and becoming the experts in their trade. This, rather than s all segments of the market, allows small businesses to improve upon a limited (USPs) that make them stand out from the larger competition.
- **E-commerce:** while many large retailers began as bricks-and-mortar shops an small start-ups have the advantage that they can begin trading online and not presence. Moreover, much like product differentiation, small businesses can fo sector and become the benchmark for quality in this area, too.

3.2.4. Questions

Please write your answers on a separate piece of paper or in an exercise book.

12. *While not as well-known as Amazon or ASOS, many small businesses that trad Explain how small businesses are able to make strong profits in the online env*

13. *Choose a business in your local area and explain one way in which it would be*

3.2. Answers

1. *A business may choose to grow for a number of reasons including economies of increase its market share, improve its competitiveness, spread the risk of failu ambitions.*

2. *Possible pitfalls include diseconomies of scale (demand in the other cities may company has to pay for its additional locations), internal communication (as t increasing number of barriers can be put between staff members) and overtra that it is ready to provide for the demand that is likely to arise once it opens m also consider whether it has the funds available for expansion and how mu*

3. *Students can explain several methods for the business, including finding new c products, devising new ways in which to market the products and finding new*

   Each of these options could help the business create more interest in its goods, secure more market power for itself. IKEA may then react by agreeing to neg might also consider the need to diversify, increase promotion and/or negotia

4. *A merger involves two or more businesses agreeing to join together and operate of directors. A takeover involves one business buying sufficient ownership in an over its running.*

5. *A business could engage in forward vertical integration, which involves them m at a later stage of production. Backward vertical integration involves a busines another which is in an earlier stage of production.*

6. *a.*

PRIMARY STAGE	↓	*Individual farmer*
SECONDARY STAGE	↓	*Processor*
TERTIARY STAGE	↓	*Wholesaler*
QUATERNARY	↓	*Supermarkets*

   b. *The supermarket could initiate a takeover of the processor and/or whole would allow the supermarket to gain more control and cut out any 'midd*

7. *Students should note that there could be tactical and strategic reasons for thi market share of each business, gaining ownership of intellectual property, exp and increasing profitability.*

8. *Organic growth involves a business growing through its activities including inc products and opening more branches. Inorganic growth involves a business em order to grow.*

9. *A business may choose to grow inorganically rather than organically as it can b it reduces competition and improves its market position.*

10. *This purchase is an example of inorganic growth because the company received investment from an external source. Before this purchase, however, YouTube w*

11. *There are many downsides to organic growth that students could mention, in*
    - *it takes a long time; the centre could accrue many expenses in this period t*
    - *as competition increases, the business may find it difficult to stay competit*
    - *organic growth is slow and so the centre may not be able to change quickly*

12. *Small online businesses benefit from not needing many employees, thereby ke is accessible 24 hours a day, so are the firms' online shops. Small businesses g command, too, allowing management to efficiently motivate their staff. Havi offer more personalised customer service, though this can backfire if demand the supply available.*

    Importantly, small businesses can focus on niches that might otherwise be ove

13. *Answers unique to each student, who should focus on USPs, customer service,*

3.3. Decision-making Techniq

3.3.1. Quantitative Sales Forecasting

! ***Key Points Covered***

- Time-series analysis
- Scattergraphs and line of best fit
- Limitation of qu

Sales forecasts are integral to most businesses as they dictate what information go predicted sales help a business decide how many staff it needs to hire, how many how much stock to buy and how much cash it can expect to have available to pay

In order to create their forecasts, businesses use past data among other factors – w happen again! Businesses can use this data to put together *time-series analyses* a what might happen in the future.

Time-series Analysis

Let's use an example:

Marble Merchants Ltd is a toy manufacturer that specialises in the production of m active since 2012 and sells bags of marbles to toy shops around the UK.

Period	Monthly Sales (£)
January 2014	54,625
February 2014	50,500
March 2014	50,450
April 2014	60,100
May 2014	71,000
June 2014	110,000
July 2014	120,800
August 2014	170,400
September 2014	160,650
October 2014	100,725
November 2014	80,600
December 2014	60,000

Table: Sales revenue for Marble Merchants Ltd durin

We can see from the table that the sales of Marble Merchants Ltd are seasonal, i.e during the summer months. This could be from the fact that children are more lik when the weather is sunny. Perhaps if the company was based in southern Spain, lot more marbles all year round!

The overall sales performance of the company could be calculated as:

$$\text{Average sales per month} = \frac{\text{Total sales for year}}{\text{Number of months in ye}}$$

$$\text{Average sales per month} = \frac{1{,}089{,}850}{12}$$

$$\text{Average sales per month} = 90{,}820.83$$

$$\text{Average sales per month} = 90{,}821 \text{ (rounded to the neare}$$

This figure is useful to an extent, but what if we want more information on how th time? For this, we can use *three-period* and *four-quarter* moving averages.

Three-period Moving Averages

This method takes the data from three points (usually the sales from three differe
the case of Marble Merchants Ltd, we have the following:

Period	Monthly Sales (£)	Moving Total (£)	M
January 2014	54,625		
February 2014	50,500		
March 2014	50,450	155,575	
April 2014	60,100	161,050	
May 2014	71,000	181,550	
June 2014	110,000	241,100	
July 2014	120,800	301,800	
August 2014	170,400	401,200	
September 2014	160,650	451,850	
October 2014	100,725	431,775	
November 2014	80,600	341,975	
December 2014	60,000	241,325	

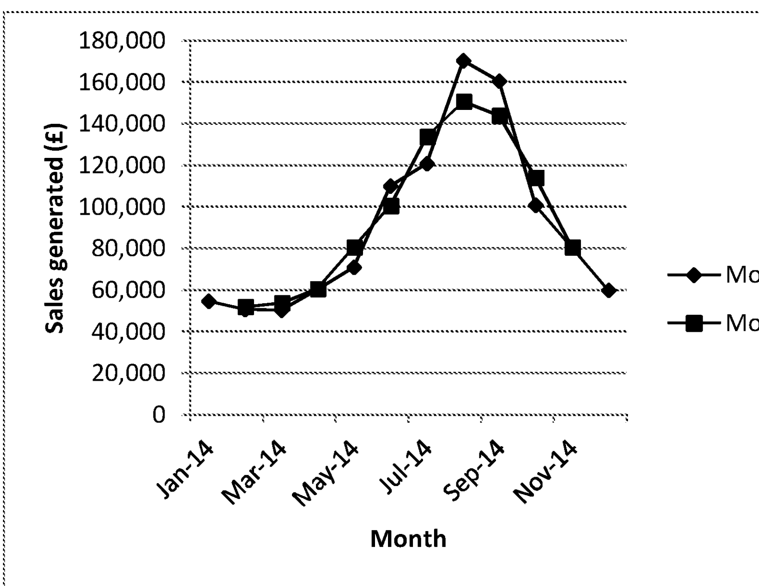
Table: Three-period moving averages for Marble Merchants Ltd (figures

We now have two more columns: *moving total sales* and *moving average*. Each av

- January + February + March = £155,575 and so the moving average is £51,85
- February + March + April = £161,050 and so the moving average is £53,683.
- March + April + May = £181,550 and so the moving average is £60,517.

And so on...

If we put the raw data and moving averages into a graph, we can see a trend appe



Graph: Three-period moving averages for Marble Merch

The trend shows that Marble Merchants Ltd sells more marbles during the summe

Four-quarter Moving Averages

This method looks over longer time than three-period moving averages. The tabl as follows:

Quarter	Quarterly Sales (£)	Moving Total (£)	Mov
Q1 (2012)	101,442		
Q2(2012)	198,108		
		739,544	
Q3 (2012)	250,991		
		753,469	
Q4 (2012)	189,003		
		751,364	
Q1 (2013)	115,367		
		870,034	
Q2 (2013)	196,003		
		872,123	
Q3 (2013)	369,661		
		912,331	
Q4 (2013)	191,092		
		957,428	
Q1 (2014)	155,575		
		1,039,617	
Q2 (2014)	241,100		
		1,089,850	
Q3 (2014)	451,850		
Q4 (2014)	241,325		

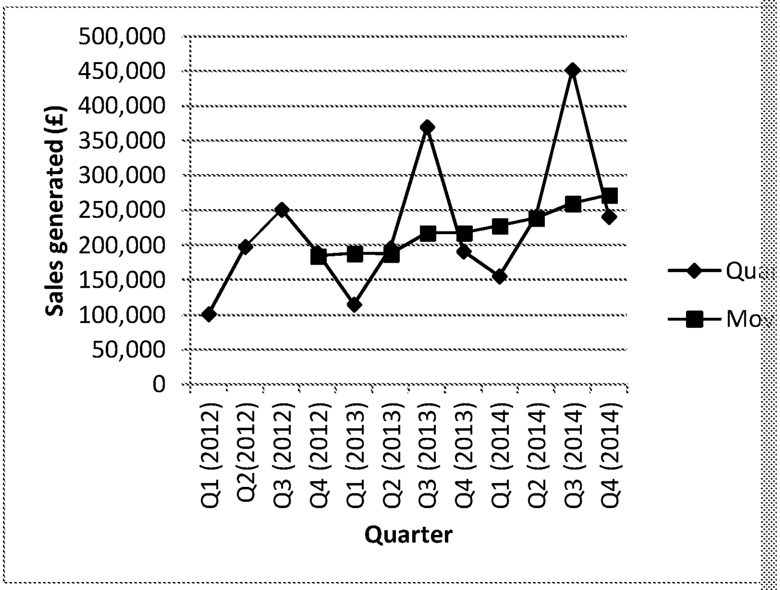
Table: Four-quarter moving averages for Marble Merchants Ltd since 2012 (fig

Unlike three-period moving averages, we follow these sales in quarters (i.e. three- is the sum of four quarters and the *moving average* is the mean of those four qua

- Q1 (2012) + Q2 (2012) + Q3 (2012) + Q4 (2012) = 739,544 and the moving a
- Q2 (2012) + Q3 (2012) + Q4 (2012) + Q1 (2013) = 753,469 and so the movin
- Q3 (2012) + Q4 (2012) + Q1 (2013) + Q2 (2013) = 751,364 and so the movin

And so on…

If we put the raw data and moving averages into a graph, we can see a trend appe



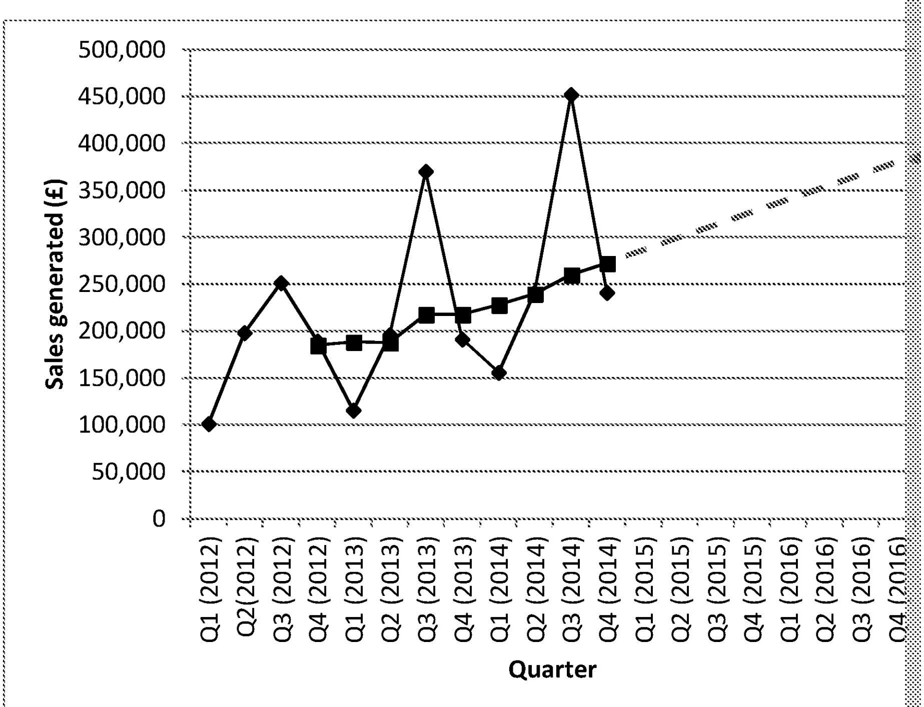
Graph: Four-quarter moving averages for Marble Merch

Now that we are comparing three years instead of just one, we can see a positive t generated by Marble Merchants Ltd. The quarterly data still shows that peak sales however, there is a definite increase in the average number of sales generated.

Extrapolation of Past Data

Businesses use both three-period and four-quarter moving averages to extrapolat predict what might happen in future.

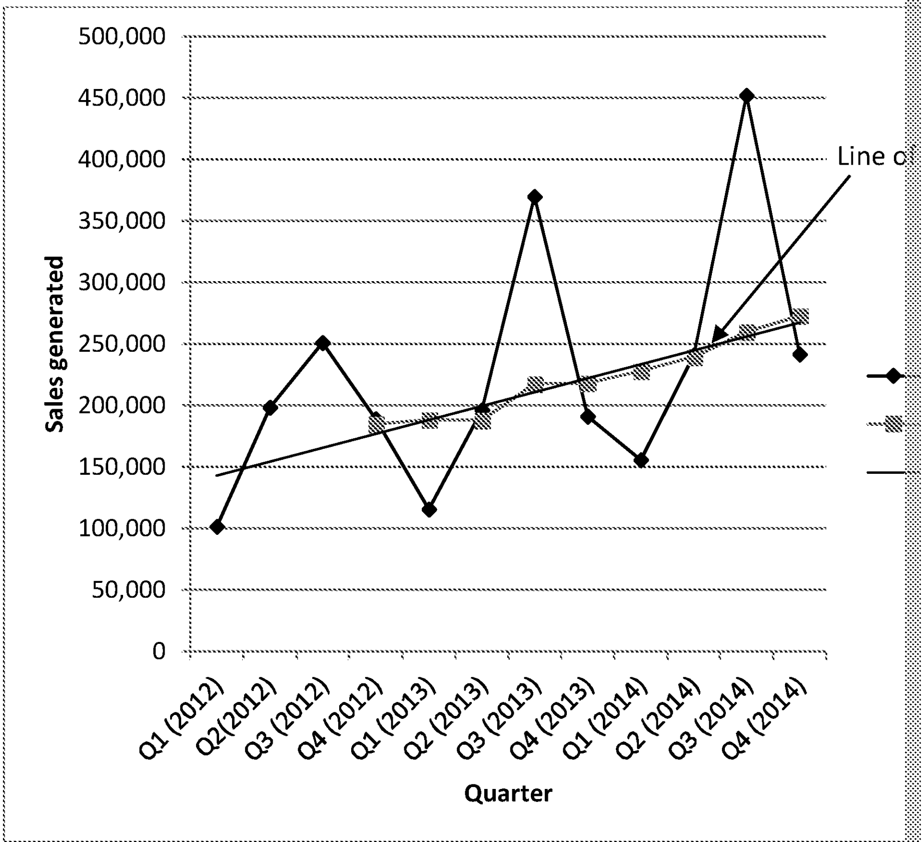
Let's use the graph of Marble Merchants Ltd's four-quarter moving averages as an



Graph: Four-quarter moving averages and extrapolation for Marb

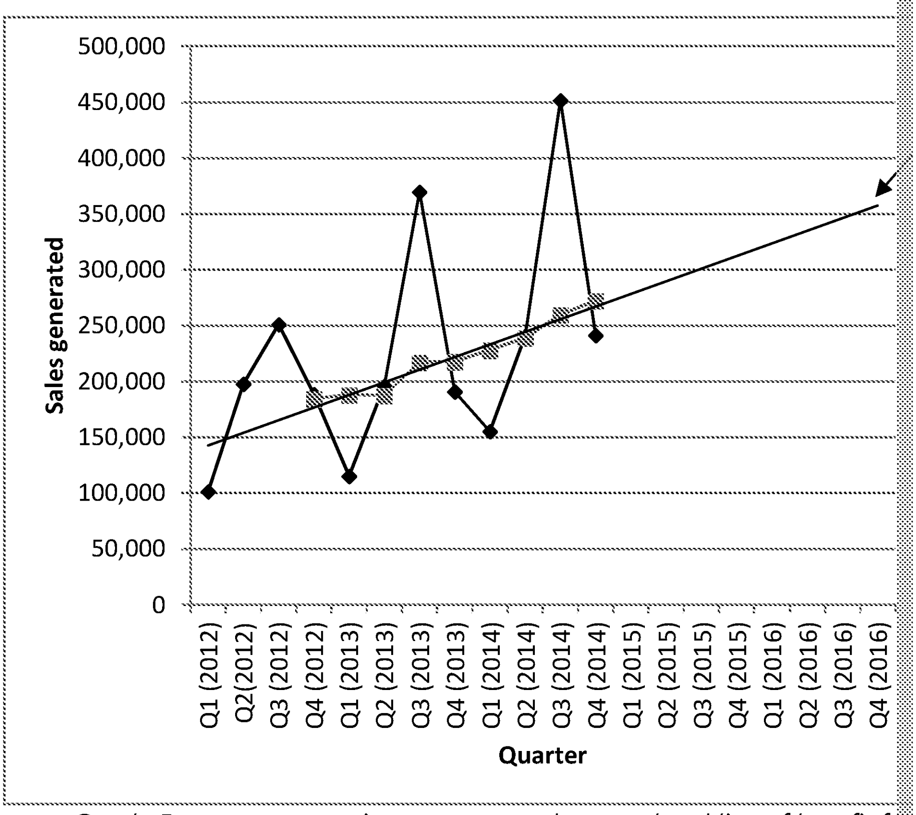
The data between Q1 (2012) and Q4 (2014) shows a steady increase in sales and s Marble Merchants Ltd can extend the moving average line manually (as shown ab

Another way to do this would be to find the *line of best fit*:



Graph: Four-quarter moving averages and line of best fit for Marb

This is a straight line that is as close to as many data points as possible. This line s the moving average and so the business could extend it like so:



Graph: Four-quarter moving averages and extrapolated line of best fit fo

To extrapolate using calculations, we need two figures: *cyclical variation* and *avera*

Cyclical Variation

Many businesses are affected by the seasons, or other repeating patterns (cycles)
sales. We can calculate cyclical variation in the following way:

Cyclical Variation = Actual Data – Trend Data
Cyclical Variation = Monthly Sales – Moving Avera
e.g. Cyclical Variation for May–July 2016 = Sales of Central Month (i.e. Ju
e.g. Cyclical Variation for May–July 2016 = 110,000 – 10
e.g. Cyclical Variation for May–July 2016 = 9,400

Period	Monthly Sales (£)	Moving Total (£)			Mo Avera
January 2014	54,625				
February 2014	50,500				5
March 2014	50,450	155,575			5
April 2014	60,100		161,050		6
May 2014	71,000			181,550	8
June 2014	110,000	241,100			10
July 2014	120,800		301,800		13
August 2014	170,400			401,200	15
September 2014	160,650	451,850			14
October 2014	100,725		431,775		11
November 2014	80,600			341,975	8
December 2014	60,000	241,325			

Average Cyclical Variation

This figure is calculated using the total number of cyclical variations and the sum o

$$Average\ Cyclical\ Variation = \frac{Total\ cyclical\ variat}{Number\ of\ cyclical\ var}$$

$$\frac{(-1{,}358\ +\ -3{,}233\ +\ -417\ +\ -9{,}367\ +\ 9{,}400\ +\ -12{,}933\ +\ 19{,}783\ +}{10}$$

$$Average\ Cyclical\ Variation = \frac{5{,}491}{10}$$

$$\boldsymbol{Average\ Cyclical\ Variation = 549.1}$$

Extrapolation of Cyclical Variation

With enough data, businesses are able to extrapolate their potential sales volume
cyclical variation tables, for instance, can show business owners what sales they ar
month. Average cyclical variations, meanwhile, give an informed view of overall e

Limitations of Quantitative Sales Forecasting Techniques

Quantitative sales forecasting offers many benefits, but companies must be aware

- The forecasting techniques use moving averages, which will always show differ
- These techniques are less useful in periods of change, such as when a compan
- The further a forecast is from the present day the less accurate it is, e.g. a forec will probably be more accurate than a forecast of the next few months
- Businesses should not use these techniques alone, but rather alongside other d
- Sales forecasting works best when a business is stable and functions within a s are very few businesses that can claim to be 100 per cent stable!

3.3.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

1. *Explain the difference between a four-quarter moving total and a four-quarte*
2. *Give two reasons why business leaders should use caution when employing qu*

3.3.2. Investment Appraisal

! ***Key Points Covered***

- Simple payback
- Average rate of return
- Discounted cash flow
- Calculations and
- Limitations of th

Businesses use investment appraisal techniques to answer two key questions:

- If we make an investment, how long will it take to get the money back?
- If we make an investment, how profitable will it be?

Essentially, firms are analysing how beneficial it would be to make a particular inve *investment*.

There are three main methods to answer these questions, namely *simple payback*, *present value*. Each method gives businesses different bits of information to help should invest in something or keep their money in the bank.

All three methods of investment appraisal start with a *cash flow table*. The followi

Year	Cash in (£000s)	Cash out (£000s)	Net cash flow (£000s)
PRESENT	—	36	(36)
Year 1	24	12	12
Year 2	24	12	12
Year 3	24	12	12
Year 4	24	12	12
Year 5	24	12	12
Year 6	24	12	12

The table shows that a business plans to buy a machine costing £36,000. The mac help the business earn £24,000 per year. However, it will cost the business £12,00 net cash flow of £12,000 per year.

Simple Payback

This method of appraisal focuses on the time it takes for a company to *get its mon*

$$\text{Payback} = \frac{\text{Sum invested}}{\text{Net cash per time period}}$$

In the case of the company in the previous table, we can quickly calculate payback

$$\text{Payback} = \frac{\text{36000 invested}}{\text{12000 per year}}$$

$$\textbf{Payback = 3 years}$$

We could already see this answer from the table above. The calculation is quicker precise – this is useful when there is no exact year at which an investment was suc

Let's use another example:

Year	Cash in (£000s)	Cash out (£000s)	Net cash flow (£000s)
PRESENT	—	45	(45)
Year 1	24	12	12
Year 2	24	12	12
Year 3	24	12	12
Year 4	24	12	12
Year 5	24	12	12
Year 6	24	12	12

The investment now costs £45,000 while the net cash flow is the same. The table s able to pay off its investment somewhere between year three and year four – but

By year three, the company still owes £9,000. We can use this figure as the sum in the twelve months of the year to see when exactly the company paid back its inve

$$\text{Payback} = \frac{\text{Sum invested}}{\text{Net cash per time period}}$$

$$\text{Payback} = \frac{\text{9000 from year 3}}{\text{12000 over 12 months}}$$

$$\text{Payback} = \frac{9000}{12000/12}$$

$$\text{Payback} = \frac{9000}{1000}$$

$$\text{Payback} = 9$$

$$\textbf{Payback = 3 years and 9 months}$$

Interpretations of Simple Payback

Simple payback benefits businesses as the calculations show them how long their money is at risk as opposed to being kept in the bank, earning interest.

Business owners often look for the shortest payback period possible with investm at play) and so simple payback can be very useful when comparing two or more o investment takes the least amount of time to pay back will be the one manageme owners may also compare investments on how much the company stands to mak payback can show.

Limitations of Simple Payback

Showing a business the length of time it takes for payback is extremely useful, bu with this method of appraisal:

- This is not a definite estimate: some costs (or taxes even) may increase more th
- If management of a business is too focused on the short-term aspects of payb of long-term investment
- This method only focuses on payback, not profitability, and so a business cann investment opportunities

Average (Accounting) Rate of Return

While payback looks at the timing of cash flow, average rate of return (ARR) focus the average annual return (from an investment) with the amount of money investe

ARR is calculated in the following manner:

$$\text{Average Rate of Return} = \frac{\text{Average Annual Return}}{\text{Initial Outlay}} \text{ x }$$

To get to this calculation, a business must first do a couple of others:

1.

$$\text{Total Profit over lifetime of investment} = \text{Total net cash flows} - \text{In}$$

2.

$$\text{Average annual return} = \frac{\text{Total profit over lifetime of inve}}{\text{Number of years of the investme}}$$

3.

$$\text{Average Rate of Return} = \frac{\text{Average Annual Return}}{\text{Initial Outlay}} \text{ x }$$

Let's use an example:

A business wishes to make an investment of £35,000 over a five-year period. This *initial outlay*.

The table below shows the business'ss cash flows over the next five years.

Time Period	Net Cash Flow (£000s)	Cumulative Cash
Year 0	(35)	(35)
Year 1	9	(26)
Year 2	9	(17)
Year 3	12	(5)
Year 4	12	7
Year 5	9	16

The total net cash flow for the business will be £51,000, which leads to a total pro the investment.

We can use these figures, plus the initial outlay of £35,000, to calculate the ARR:

1.

$$\text{Total Profit over lifetime of investment} = \text{Total net cash flows} - \text{In}$$

$$\text{Total Profit over lifetime of investment} = 51000 - 35$$

$$\textbf{Total Profit over lifetime of investment} = \textbf{£16,000}$$

2.

$$\text{Average annual return} = \frac{\text{Total profit over lifetime of inve}}{\text{Number of years of the investme}}$$

$$\text{Average annual return} = \frac{16000}{5 \text{ years}}$$

$$\text{Average annual return} = \frac{16000}{5 \text{ years}}$$

$$\textbf{Average annual return} = \textbf{£3,200}$$

3.

$$\text{Average Rate of Return} = \frac{\text{Average Annual Return}}{\text{Initial Outlay}} \text{ x 1}$$

$$\text{Average Rate of Return} = \frac{3200}{35000} \text{ x } 100$$

$$\text{Average Rate of Return} = \frac{3200}{35000} \text{ x } 100$$

$$\textbf{Average Rate of Return = 9.14 per cent (to 2 dp)}$$

This set of calculations shows that the profitability of the business'ss investment s compared with the £35,000 that it originally invested.

Interpretations of Average Rate of Return

Companies using ARR can take advantage of many benefits, including:

- Setting targets for profitability: if a business decides it will only take on investm profitability or more, it will know not to invest in the example above
- It is easy to compare two or more opportunities on the basis of which stands to
- If there is only one opportunity available, the business can compare the reward money in the bank. The graph below shows an example:

Graph: Example of reward for investment risk

The example in the graph shows that a business stands to make 3.75 per cent in a in the bank. If the business decides to take the investment, however, it will not re if the reward for risk (i.e. making the investment) is 9.14 per cent, the business car of 3.75 to show the true reward of its investment.

$$\text{True reward of investment} = \text{ARR} - \text{Potential bank int}$$

$$\text{True reward of investment} = 9.14 - 3.75$$

$$\textbf{True reward of investment = 5.39 per cent}$$

The higher the potential interest rate, the lower the true reward and, therefore, th
appears to a business.

It Pays to be Big

Small businesses are less likely to make investments where the rewards are small –
Big businesses, on the other hand, can afford to take these risks because they hav
money behind them) to better cover these costs.

Limitations of Average Rate of Return

Some of the drawbacks that businesses find with ARR include:

- The method has a narrow focus as it only looks at overall profitability
- ARR ignores the timings for when cash flows, i.e. the method does not tell bus most/least profitable. This can hinder other forecasts, such as planning when p

Net Present Value

Discounted Cash Flow

While payback only looks at timings and average rate of return only looks at profi takes both of these factors into consideration. Businesses achieve this by focusing investments, i.e. what (or how much) they are giving up by deciding to make their

In the case of discounted cash flow, businesses are giving up the interest rate that keeping their cash in the bank. This means that a business's money is worth more money in three years' time. If interest rates were at 7 per cent, for example, a bus 7 per cent less every year that it is not earning interest in the bank.

Businesses use discount factors to work out how much their money would be wor discount factors, businesses need to know how many years the investment will las

Year	3%	5%	7%	9%
0	1.00	1.00	1.00	1.00
1	0.97	0.95	0.93	0.92
2	0.94	0.91	0.87	0.84
3	0.92	0.86	0.82	0.77
4	0.89	0.82	0.76	0.71
5	0.86	0.78	0.71	0.65
6	0.84	0.75	0.67	0.60

Table: Discount Factors

If a business is looking to make a four-year investment, for instance, and the rate discount factor would be 0.66. The business can then calculate the value of, say, £

Present Value over time = Cash flow x Discount Fac

Present Value after four years = 1,000 x 0.66

Present Value after four years = **£660**

The present value calculation shows that the company's cash of £1,000 would hav time. This is the *opportunity cost* of not keeping the cash in the bank, i.e. of failing

Net Present Value

Present value is useful to a business, but it is only one value. What businesses rea value affects them over time. Net present value (NPV) allows businesses to comp the same investment.

Let's use two examples: Project Alpha and Project Gamma. Both projects require £700,000 and both earn the same amount of revenue over time. The projects also 7 per cent. However, their cash flows are different. Project Alpha earns more reve Project Gamma earns more towards the end.

Project Alpha				P	
Year	**Cash Flow**	**Factor**	**Present Value**	**Year**	**Cash Flow**
0	(£700,000)	1.00	(£700,000)	**0**	(£700,000)
1	£430,000	0.93	£401,869	**1**	£10,000
2	£275,000	0.87	£240,196	**2**	£25,000
3	£10,000	0.82	£8,163	**3**	£17,500
4	£160,000	0.76	£122,063	**4**	£275,000
5	£25,000	0.71	£17,825	**5**	£160,000
6	£17,500	0.67	£11,661	**6**	£430,000
Net Present Value			**£101,777**	**Net Present V**	

Table: NPV Comparison between Project Alpha and Projec

The two tables show that, even though both projects cost the same in initial inves over time, Project Gamma has a lower NPV. This is because the discount factor de company's cash over time: since Project Gamma doesn't earn the majority of its re period, its earnings are worth less than those of Project Alpha.

Interpretations of Net Present Value

Companies can keep close tabs on the timings of their cash flows and the value o its present-day value.

Businesses like to use NPV because it is a handy 'what if?' calculator. A firm can lo their investments based on various factors, such as:

- time period of investment
- differing interest rates
- differing amounts of initial investment
- differing structures of cash flow

Limitations of Net Present Value

Even with its advantages over payback and ARR, this method is still not the be-all problems, such as:

- two or more projects can only be compared if their initial investments are the s
- NPV can be very difficult to calculate
- the method can also be very difficult to grasp and, therefore, communicate to

Limitations of Investment Appraisal in General

As we have seen, each method of investment appraisal has its own benefits and d
limitations span across investment appraisal in general, such as:

- it can take much time to gather the information required for investment apprai deciding whether an investment is too expensive is an expensive process in itsel
- there are many unforeseen costs and taxes that occur in business, which invest
- much of investment appraisal can be difficult to understand (and, therefore, co benefits and drawbacks of certain opportunities are often missed
- business owners and managers often look to the short-term benefits of an inve investment with the least risk being the one chosen. However, this narrow focu term potential of an investment
- by putting a figure on every risk, business owners can lose sight of the rewards

3.3.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

3. *Coffee Table Merchants Ltd has sold high-quality coffee tables since the 1980s company's two founding owners, would like to diversify the business by also se start selling these, the company will need to invest £36,000. Mark projects tha generate £42,000 for the company over a period of 36 months.*

Calculate how many months it would take for Mark's proposed investment to Round your answer up to the nearest month.

4. *The other founding owner of Coffee Table Merchants, Donna Mesa, is sceptica appraisal. Explain one reason why Donna might be sceptical.*

3.3.3. Decision Trees

! Key Points Covered

- Constructing, calculating and interpreting decision trees
- Benefits and lim

Business leaders can make decisions based on intuition or on data. When it comes to
handy.

Decision trees help businesses to make the right choice. They are graphical repre
They consider the choice in question, the probability of its success and the potent
show businesses three key pieces of information:

- The options that are available
- The possible outcomes
- Where the business decision needs to be made

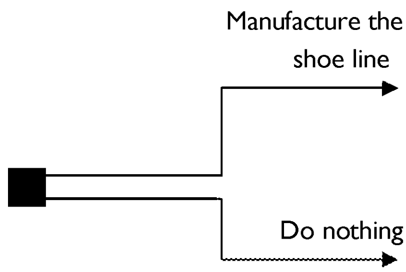
The end goal of a decision tree is to show the business the value of success or fail
option with the most value and the highest probability of success is often the righ
business and its market.

Constructing, Calculating and Interpreting Figures from Sim Tree Diagrams

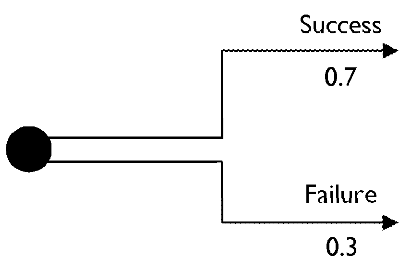
Let's use an example:

Rubber Sole Ltd specialises in manufacturing running shoes for athletes and for sp
considering the manufacture of a new line of sports shoe.

1. Decision:
The decision is either to manufacture the new line or to do nothing. So far, t



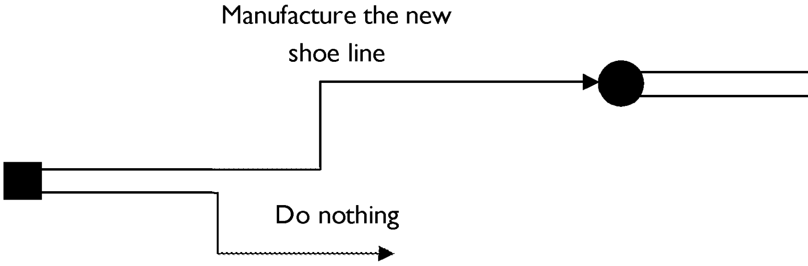
2. Probability:
Whenever the company has introduced a new shoe in previous years, it has ha
Rubber Sole Ltd can use this historical data, therefore, to predict the possible s



Since historical data tells us that a new line of Rubber Sole Ltd shoes general
70 per cent, we can convert this into a probability ratio of 0.7. This means th
because the ratios need to add up to 1.

Note: decision trees show both squares and circles. The squares indicate busines
circles mark chance (i.e. out of control of the business) and so there is a probabilit

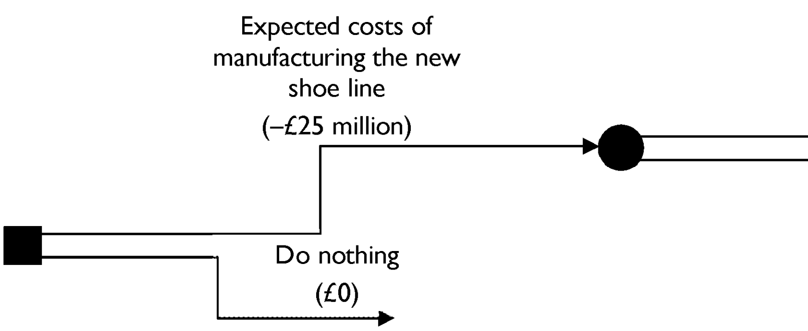
3. Decision tree:
If we put both the decision and probability sections together, we have a deci



We now see that Rubber Sole Ltd can either decide to manufacture the new s
go ahead, it has a 70 per cent chance of success.

We have lots of useful information now, but it's not quite enough. Businesses
probabilities of their decisions, they also want to know the possible costs and r
at *net cash* and *net gain*.

4. The new line is expected to cost £25 million to manufacture. If it is successfu
net cash flow. A failure will only earn the company £7 million. If the compan
new line, their change in cash flow will be nothing.



5. We now have the potential reward in cash flow if Rubber Sole Ltd decides to ma
flow if the firm fails. The net gain for success would, therefore, be £25 million (i.e
£25m cost of manufacture). However, we have not taken into account the proba

We calculate the expected value of success and failure using the following m

$$\text{Reward for success} = £50\text{m x } 0.7 = £35 \text{ million}$$

$$\text{Reward for failure} = £7\text{m x } 0.3 = £2.1 \text{ million}$$

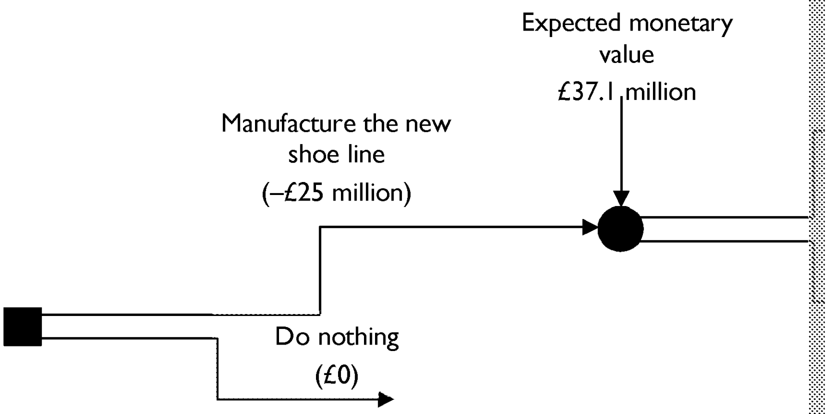
These two figures allow us to calculate the overall Expected Monetary Value (

6. Using the figures for success and failure, the *expected monetary value* for manu be calculated as:

$$\text{Expected value} = \text{Reward for success} + \text{Reward for fa}$$

$$\text{Expected value} = 35 \text{ million} + 2.1 \text{ million}$$

$$\textbf{Expected monetary value} = \textbf{£37.1 million}$$



7. Finally, the company can calculate the net gain of manufacturing the new line of the decision is £37.1 million and the expected cost of manufacturing the s

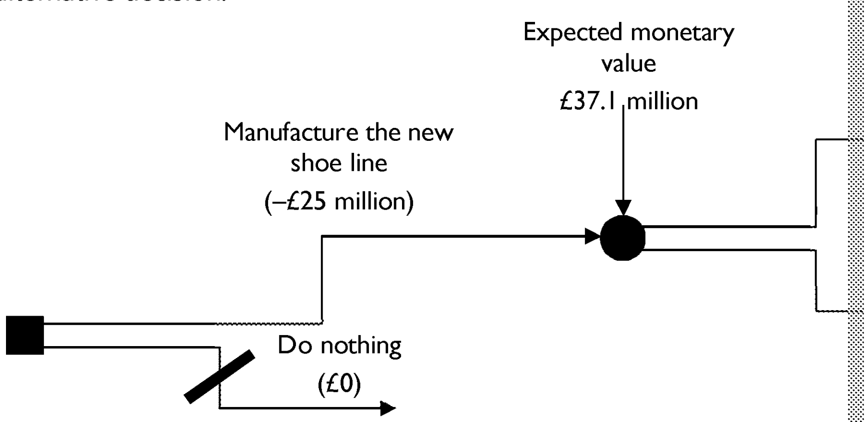
$$\text{Net gain} = \text{Expected value} - \text{Expected costs}$$

$$\text{Net gain} = 37.1 \text{ million} - 25 \text{ million}$$

$$\textbf{Net gain} = \textbf{£12.1 million}$$

The net gain that Rubber Sole Ltd can expect for manufacturing the new line represents enough cash flow for the business, then Rubber Sole Ltd will choo rather than doing nothing.

The fact that Rubber Soul Ltd has decided to go ahead with the new shoe lin the alternative decision.



Benefits and Limitations of Using Decision Trees

Businesses use decision trees for all manner of choices, such as whether to make a
product. Some of the benefits firms get from decision trees include:

- Decision trees make businesses focus on uncertainty, ensuring managers act
- They lay things out so that businesses can see the whole picture – it is easy to
- Decision trees present choices and chance in a logical, easy-to-follow format
- The trees show not just probability, but value too
- They are especially useful for businesses when forecasting something that ha as using historical data on previous product launches to predict the next
- Decision trees are a great method to ensure businesses actually analyse what

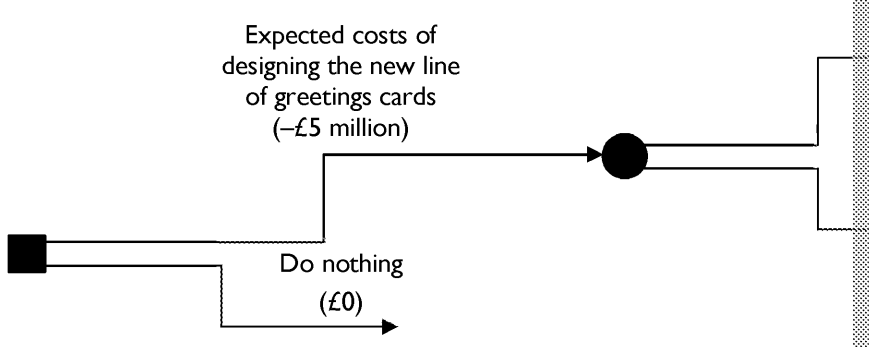
There are limitations that come with this, too:

- Decision trees work best for routine, tactical decisions rather than strategic o many facets to a change in strategy that cannot possibly be accounted for w
- Decision trees are based on probability, so, by their very nature, they do not
- External change can occur at any moment, and often unexpected by the busi the decision tree
- Decision trees take time to create. For some businesses, by the time the pro they may no longer be relevant.
- They are generally concerned with the monetary gain that a decision will brin thing to consider in business. The business is not necessarily looking at emp product quality.

3.3.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

5. *Punrun Ltd is a designer of humorous greetings cards. The company's leaders card designs that could make the company £12 million in net cash flow.*



a. *Calculate the expected monetary value of the decision and add this to the*
b. *Using your answer from 5.a, calculate the net gain of the decision.*

6. *Give two reasons to explain whether Punrun Ltd is correct to use a decision tre investment.*

3.3.4. Critical Path Analysis

! Key Points Covered

- Nature and purpose of critical path analysis
- Using critical path analysis
- Calculations
- Advantages and li[...] analysis

Nature and Purpose of Critical Path Analysis

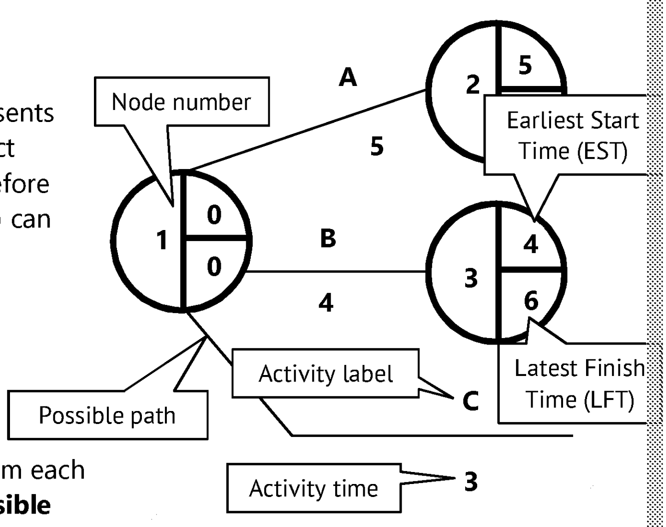
Critical path analysis is a method that managers use in order to organise and simp a 'project' being anything from launching a clothing line to installing brand-new t company's computer operating systems or moving an entire department over to u

The 'critical path' presents the key elements of a project that must be completed i critical path falls behind, the entire project falls behind.

Project managers use critical path analysis in order to identify each element, the re the time that each should take to complete. Managers are then able to calculate t of time that each element should take without causing the project itself to overru

The overall goal of critical path analysis is to utilise the least resources (human an the least amount of time.

Each **node** (circle) represents a milestone in the project that must be reached before later nodes (to the right) can happen.



The lines coming from each node indicate a **possible 'path'** through the project – the next activity that needs to happen.

Each activity that must happen in the project is given a **label** and **time**.

In this example, activities A, B and C can happen simultaneously. So which do we amount of time, so it might make sense to start the longest activity, A, first. Howe happen before other activities can – so the critical path, which completes the proj might dictate that we start with B or C. We will not know until we look at the enti

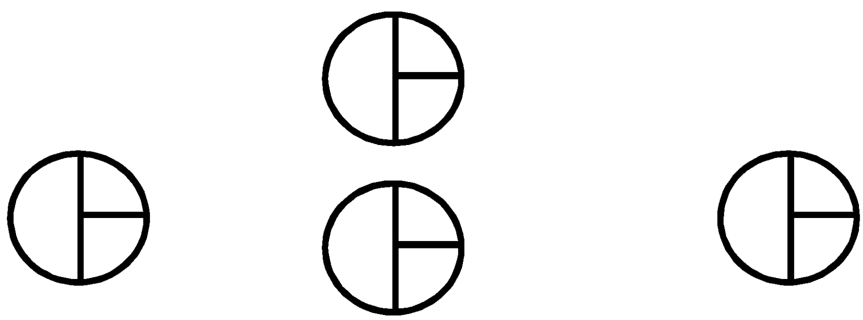
Using Critical Path Analysis

Let's construct an example diagram based on making a cup of tea – start simple!

The following information assumes that milk goes in the cup first then the sugar wi
same time:

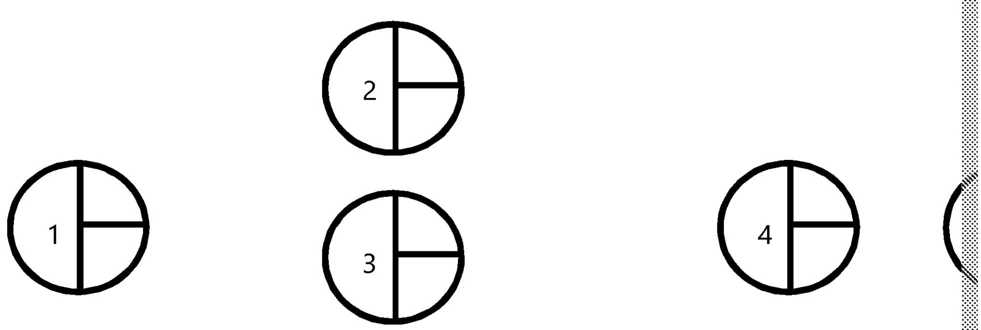
Activity letter	Activity description	Time activity takes to com
A	Boil kettle	3 minutes
B	Pour milk into cup	1 min
C	Put teabag in cup	1 min
D	Put one sugar* into cup	1 min
E	Pour boiling water onto teabag	1 min
F	Squeeze bag	1 min
G	Serve	2 mins

Now let's transfer this data to a CPA diagram:



Here are all the **nodes** in the diagram – the circles are nodes. Every activity or eve
You boil the kettle at node 1 and it stops boiling at a different node.

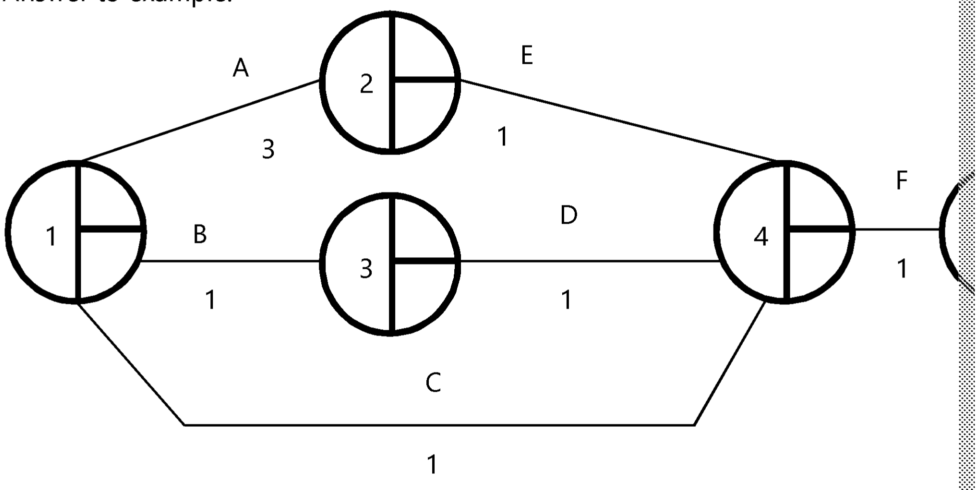
Step 1
Number the nodes. This is not necessarily the exact order of activities – you just a
identification.



Step 2
Add in **lines** these are the **activities** in your tea-making project. Try that now wit
three activities start at node 1.

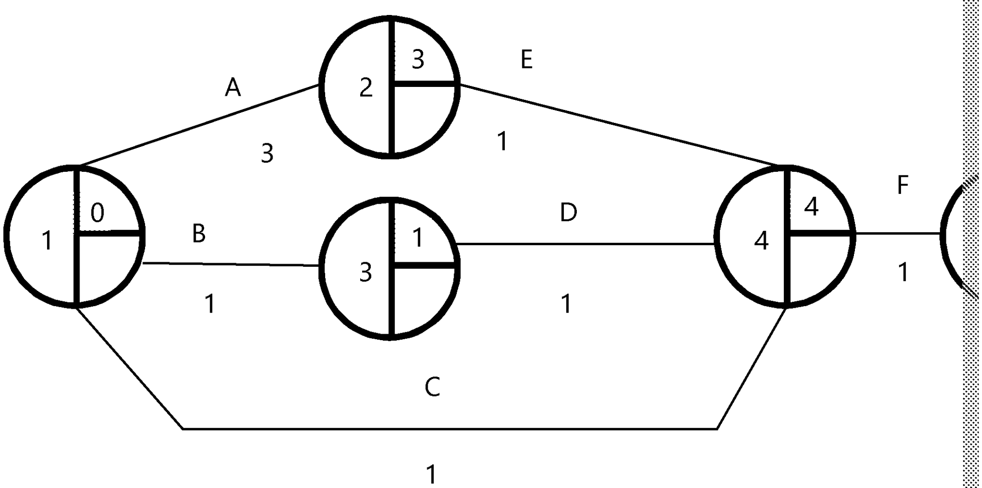
The answer to this example can be found on the next page.

Answer to example:



Step 3
Add to the lines the **name of the activity** (we use letters to make the diagram ea
below the line. So C/1 is 'Bag in cup' and takes one minute to execute.

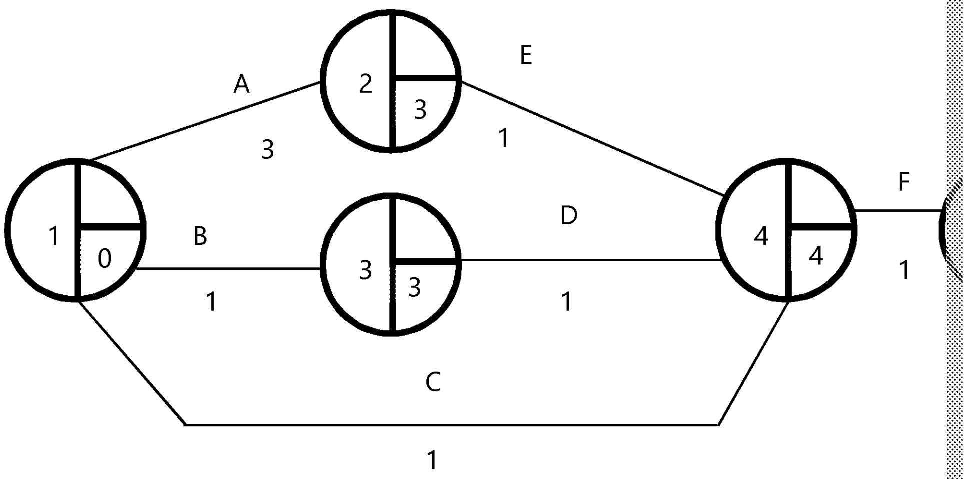
Step 4
Now calculate the **earliest start time** (**EST**) of the project – we always assume the
0 (zero), if you start at day 1 that would be wrong. We put it into the **top right** of



To get the EST figure add the activity times:
Node 2 = 3 minutes = 0+3
Node 3 = 1 min = 0+1
Node 4 = 4 minutes = 0+3+1
Node 5 = 5 minutes = 0+3+1+1
Node 6 = 7 minutes = 0+3+1+1+2

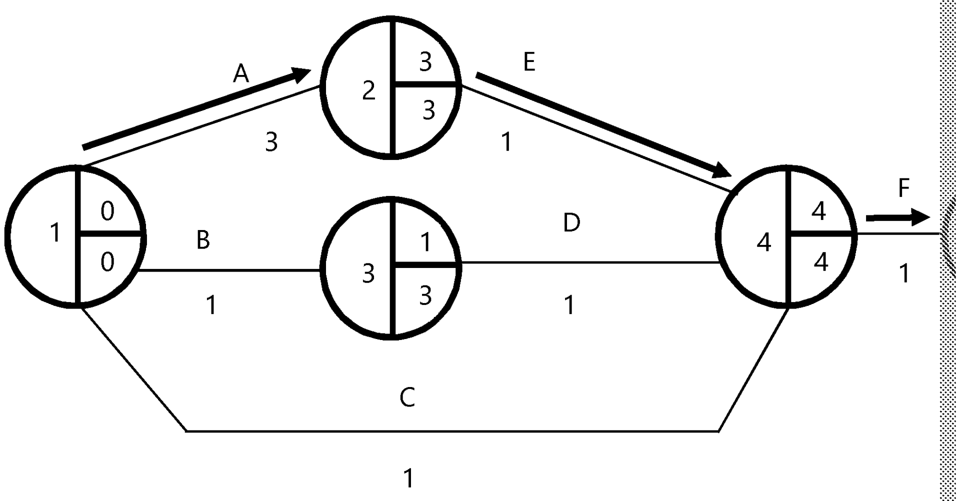
Notice at node 4 the EST is four minutes and not two minutes – you have to wait
completed before moving on. An example is waiting for the plaster to dry before
with no water on it. Some activities just have to wait for others to be done first, w
that kind of thing. Tells a manager what is the earliest some project activities can
for resources to arrive. It also gives a rough finish time if all goes well – in this cas
cup of tea.

Step 5
Now calculate the **LFT** or **latest finish time**. To make this calculation you need to
diagram. LFT times go in the bottom right of the node. Start at node 6.



Node 6 = Task G must be completed by the 7^{th} minute
Node 5 = 7 – 2 = 5
Node 4 = 5 – 1 = 4
Node 3 = 4 – 1 = 3
Node 2 = 4 – 1 = 3
Node 1 = could have been 0 or 3 or 2 (we take 0 because we want the earliest tim

Step 6
Now put both LFT and EST together:



Step 7
The critical path is the one with the EST and LFT the same. This means there must
activity before moving on to the next; if there are delays then the whole project w
the critical activities are A, E, F and G. Let's go back to the original plan and see if

A	Boil kettle	**F**	Squeeze
E	Pour boiling water onto teabag	**G**	Serve

Going for the A grade:

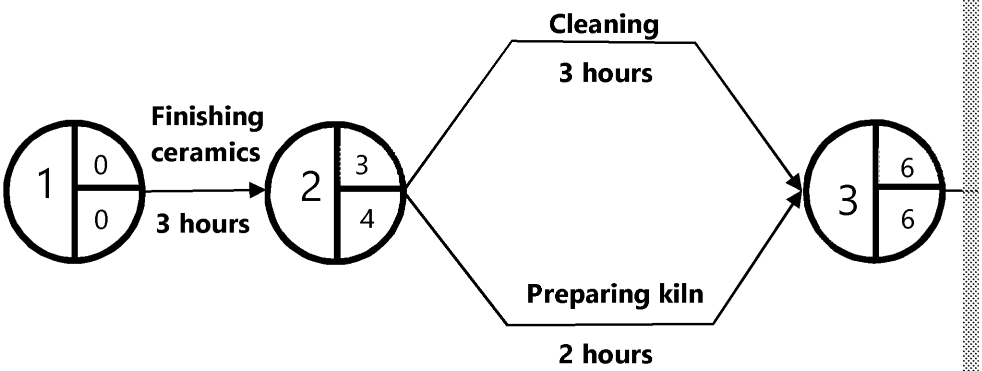
- *You may have gathered that the diagram does not have putting a teabag as a critical activity so obviously there is some room for common sense to to the diagram.*
- *If the kettle is late boiling then the whole project will be delayed, usually needs to be completed before the rest of the project can move on. For ex shed needs to set before the rest of the shed goes up.*
- *The critical path is the longest route through the diagram.*
- *Activities not on the critical path can be delayed and not affect the whole may not turn up on day 1, but it won't delay the finish time of the whole until day 10.*

Advantages and Limitations of Using Critical Path Analysis

Advantages of Critical Path Analysis	Limitations o
Used as a management planning tool, useful for project based management.	Usefulness is limited in the diagrams get too l tool.
Identifies at what point in the project resources are required – this includes perhaps skilled employee participation, e.g. a painter cannot paint until the plaster has dried. Knowing this will prevent the painter from being employed on day 1 and sitting around idle. (Think DIY SOS if you have seen it or similar DIY programmes on TV.)	Requires good resourc diagram, for example i and does not arrive th of the planning and pr
Estimates the minimum completion time of the project – which means that management can quote for a job and give an estimate of the finish date. Many building projects incur late finish penalties if they are late, so a planning tool like this can avoid a hefty fine.	Does not take into acc delay the project, such outside of a house.
Management are able to let the client know if there is a delay prior to it happening. If the critical path activities are delayed at the start of the project then management will be able to make useful decisions based on that knowledge. If tasks are likely to be delayed then management can move resources to try to reduce the delay – for example getting the painter in early to help with the plastering.	May be useful as a gui flexible document it w the project take place, because of its rigidity. need to be constantly companies do use CPA as Gantt charts.
Reduces waste as management can plan ahead; could be wages saved from not having staff sitting around (the painter) or just having resources arrive as and when they are is needed, e.g. a skip or a digger.	Staff are suspicious of use to micro manage a by. They may blame p use it as a scapegoat.

Total Float

The total float of a task shows how much delay is available for it (i.e. whether it ca much time). The process of a ceramic vase manufacturer, for instance, might inclu the vases ready for painting and glazing.



Total Float = Latest Finish Time (LFT) of task – Earliest Start Time (ES

The total float for preparing the kiln, therefore, can be cal

Total Float for Preparing the Kiln = 6 – 3 – 2

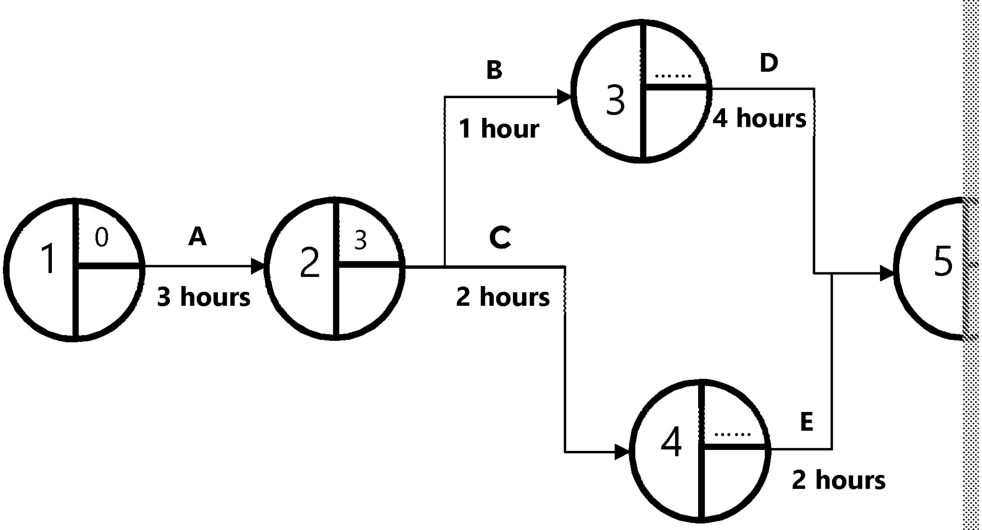
Total Float for Preparing the Kiln = 1 hour

The manufacturer has one hour of leeway when it comes to preparing the kiln. In decide to begin preparing the kiln up to one hour after they have started cleaning

3.3.4. Questions

Please write your answers on a separate piece of paper or in an exercise book.

7. *Ruth Maxton is a seller of used cars. The diagram below shows the tasks (A to has successfully sold a car to a consumer.*



a. Calculate the earliest start times for Nodes 3 and 4.
b. Calculate the latest finish time for Node 6.

8. *Ruth Maxton regularly follows the critical path analysis highlighted in questio for her in relying on this method.*

3.3. Answers

1. *Four-quarter moving total is the total of the four figures while the average is t*

2. *Cautions might include that moving averages are always changing, technique figures are stable, figures from long ago are less accurate than the most recen making tools to be used alongside other decision-making tools.*

3.

$$Payback = \frac{Sum\ invested}{Net\ cash\ per\ time\ period}$$

$$Payback = \frac{£36{,}000}{£42{,}000/36\ months}$$

Payback = 31 months (rounded to nearest mon

4. *Donna may be sceptical of the investment because:*
   - *Payback only focuses on the short-term aspect of generating cash and ther make a positive profit.*
   - *Making money is also not the only thing of note; it may change the way tha customers, suppliers and authorities. Reputation can lead to positive and n*
   - *Proposed costs cannot take into account any unforeseen costs. If these are*
   - *Payback looks at how much cash is paid back into the company rather than profitability. Making £20,000 in payback, for example, is not great if the in brand reputation.*

5.

   a.

Expected value = Reward for success + Reward fo
Expected value = (£12m x 0.6) + (£3m x 0.
Expected value = 7.2 million + 1.2 million
Expected value = £8.4 million

   b.

Net gain = Expected value – Expected costs
Net gain = 8.4 million – 5 million
Net gain = £3.4 million

6. *Reasons FOR the decision tree include (not limited to):*
   - *It shows the business not just how much cash it could generate but also the allows for greater context*
   - *If Punrun Ltd has released a similar line of humorous cards in the past, the tree is likely to be quite accurate for forecasting*
   - *Decision trees are simple diagrams, which make them easy to follow for Pu investors they might need to convince*

   Reasons AGAINST the decision tree include (not limited to):
   - *The proposed probabilities may be correct at the moment. However, gettin decision trees long-winded in their process and lead to out-of-date informa*
   - *Changes to external factors can occur unexpectedly, which decision trees d*
   - *The line of cards does not only represent cash flow but also the company's r might change the way that customers think of the company.*

7. a. *Node 3 = 4 hours. Node 4 = 5 hours.*
   b. *Node 6 = 11 hours.*

8. *Reasons why Ruth Maxton should not rely on critical path analysis include (no*
   - *Critical path analysis looks only at the business's predicted expenses. If an process will be set back.*
   - *Related to the previous point, once the process is set back, the diagram is n*
   - *Ruth needs to have everything organised and ready to go exactly when the if Ruth has not had time to organise everything because she's been busy sel*
   - *Critical path analysis can get complicated quickly, at which point the diagr most businesspeople.*

3.4. Influences on Business Dec

3.4.1. Corporate Influences

! Key Points Covered

- Corporate timescales: short-termism versus long-termism
- Evidence-based decision-making

As markets evolve, businesses will find that some corporate objectives are more s business operating in a very difficult economic climate may be focused on short-t business operating in a relatively steady economic climate with market growth ma long term. Businesses may be experiencing similar economic and market influenc different business decisions. This can be influenced by their market position, fina power, etc.

Influences on corporate decision-making include:

- The **risk** associated with a decision will have a significant influence on wheth A high-risk decision will not be implemented immediately, if at all, as manage analysis into its pros and cons before reaching a final decision. A low-risk str far quicker than a high-risk one, as there could be less at stake and manager outcome.
- The **attitude to risk** can influence whether a decision is implemented or not. is unlikely to implement a high-risk decision, as it is unwilling to do so. Howe taking high-risk decisions will not be so hesitant.
- **Past successes** will influence the decisions made. A decision-maker who has style of decision-making will continue to adopt this approach. However, one a particular style will look to use a different method. For example, if a decisi without the involvement of others, they are likely to continue to do so. One with this method will seek to involve others in the process, in order to impro also to reduce the degree of blame they endure, if unsuccessful.
- The **nature of the industry** will influence the decisions taken. A highly comp onus on thorough market research in reaching a decision, as reaching a wron choosing rivals instead. Hotels are well known for carrying out market resea a particular product or facility. They will amend it in light of the feedback re
- **Stakeholder power** can influence significantly the decisions made. If a pow particular decision the business is likely to abandon it, if the impact is to be example, Netflix, the DVD rental and online film / TV streaming business, aba separate companies due to customer pressure. If the decision had gone ahe use two different companies to access the products. Furthermore, their deta on each website. Rather than posting a review on one of the companies' we they would be required to produce it on each separate website. The custom had to be produced on each website. Consumers were unhappy as the plann amount of time they spent accessing the service, if both DVD and online stre
- The **ethical values** of the business will influence the decisions made, as one will probably be rejected, even if highly profitable. For example, The Co-ope trade with businesses which are known for not implementing basic labour rig
- The **resources available** will influence the decisions made. For example, the available could determine whether a proposed decision is feasible or not or w

Short-termism versus Long-termism

Have you ever bought something without giving it too much thought? In the 199 scrambled to buy Tamagotchi pets for their children only for the trend to fizzle ou toy shop had invested in 20,000 Tamagotchi toys, it may only have been because The shop would then have needed to sell every Tamagotchi as quickly as possible

Short-termism

Short-termism is a form of decision-making that sees companies working mostly figures. Examples of this include:

- **Current cash flow:** a business might opt for taking out a loan in order to aff however this does not necessarily address the original reason why it cannot a the firm in further financial difficulties in future.
- **Change in production:** leadership may decide to produce a new type of iter manner. This may lead to short-term popularity, though can be a risk if deci
- **Training:** a decrease in the amount of training given to employees can help short term, though can worsen its efficiency in the long run.
- **Acquisition:** by taking over a business that is doing well, a firm can increase result can occur, however, if the acquisition is made with a view to improving term. If an IT company buys a particular mobile phone manufacturer becaus now, this may not always be true.
  (Note: acquisition can also represent the long term since purchase of a brand generate high sales over the long run.)

Long-termism

This type of decision-making focuses on the 'bigger picture', i.e. what may happen rather than in just a few months. Companies that concentrate more on the long r research and development than companies that work with only the short term in long-term decisions is likely to have an end result in sight and so make acquisitio do not appear to have any benefit in the beginning. Large companies, such as Co long-term goals while a corner shop that serves only its local community might m paying the month's upcoming bills.

The corporate objectives set will be influenced by the market and trading position economic climate prevailing at the time. A small family-owned business may have limited company, as the nature of owner and market influence may be very differe are unique to the position of each firm, although to the outside eye they appear s

Evidence-based versus Subjective Decision-making

Strategy is a plan for meeting the business objectives. **Strategic decisions** invol implementing actions that will affect an organisation's future abilities to achieve it at times of uncertainty and therefore influence the medium to long-term future o direction for the overall business and involve a large resource commitment. For e involve deciding whether the business should expand into emerging markets or n with clarity can allow departments and managers to structure their own plans to i

Tactical decisions affect the day-to-day implementation of actions required to ac example, should the price of the product be reduced or not? These are based on uncertainty and fewer resources.

Data is a collection of statistics, facts and events which are collected for reference this data, *information* is acquired that provides meaning, which enables businesse many areas including:

- hiring new staff
- improving product quality
- changing the pricing strategy
- entering new markets
- changing the corporate image
- embarking on public relation campaigns in a local area
- deciding on the output level

The *evidence-based* decision-making approach involves selecting a logical choice making a good decision the manager must weigh up the pros and cons of an opti alternatives. A forecast of each option should be possible, which is based on sour circumstances not only facing the business now, but also possibly in the future.

Evidence-based decision making involves taking a logical and research-based app a formal procedure to ensure that decisions are arrived at in an objective manner. bias by ensuring that decisions are based on factual, numerical evidence. A busin to assist in reaching a logical and research-based decision including:

- break-even analysis
- investment appraisal
- decision trees

A business using the evidence-based decision-making approach will use the follo

1. **Set objectives** – objectives are set based on what the business wishes to achieve within a particular timescale.
2. **Gather information** – data is gathered using either primary or secondary research methods. This may provide data on demand, market trends, costs, etc.
3. **Analyse the data** – the data is analysed which provides the basis to make recommendations. Quantitative techniques like investment appraisal, break-even analysis and critical path analysis may be used during this stage.
4. **Select a course of action (plan)** – based on the data analysis a strategy is selected.
5. **Implement the plan** – the chosen strategy is implemented.
6. **Review** – the strategy is reviewed to establish if it is having the desired outcome in relation to the objectives set. This may involve adjustments being made to the strategy or a rejected one being considered again.

The evidence-based decision-making process will usually involve more than one p
likely the strategy selected is in the best interests of the business, rather than an i
decision has been reached in a logical manner, thus providing a greater chance of
direction for the business, whilst encouraging constant monitoring and review of t

The downside of this approach is that it can be time consuming due to the level o
along with the participation of others in reaching a final decision. It does not allo
which can generate a high level of added value, as they are not based on data ana

The business may also use Ansoff's matrix and Porter's generic strategies to assist

The *subjective* decision-making approach is not based on analysis of data, but the
may or may not have a degree of experience in a market related to the chosen str
decision-making, but can be very high risk as the decision is not based on any for

Whether the business chooses the subjective or evidence-based decision-making

- Whether the **business culture** usually favours a particular approach.
- The **size of the business**, as the intuitive approach is likely to be favoured by resources.
- The **risk a business is willing to take**. If they wish to make a low-risk decisio model is likely to be chosen.
- The amount of **time available** to make a decision. If time is limited the intui can be made far quicker than the scientific decision one.
- The **level of certainty** associated with the situation. The higher the level of u scientific decision-making approach will be used, as this will provide greater c chosen can be a success.

Achieving an A grade

In analysing and evaluating a strategic decision chosen by a business, conside main driver in its selection. Establish whether there is any bias associated in this mean it may not be in the best interests of the business when considerin your opinion, another strategy should have been chosen, what are the potent strategic decision, the magnitude of the consequences could be far higher, as associated with these, unlike tactical decisions. For example, Kodak choosing camera market, although it had been the first pioneer of the device, was unw support an ailing area of the market: film-based cameras. This decision was of the business, but a board of directors who were fearful of moving away fro highly profitable. Kodak filed for bankruptcy in January 2012.

3.4.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

1. *Explain the difference between evidence-based decision-making and the subje decision-making.*
2. *Explain one disadvantage of evidence-based decision-making.*

3.4.2. Corporate Culture

! Key Points Covered

- Strong and weak cultures
- Classification of company cultures
- How corporate c
- Difficulties in ch

An organisational culture is the accepted norms, attitudes, beliefs and behaviours
organisation. The culture of a business can be identified in a number of ways, inc

- how employees communicate with each other
- to whom employees are expected to speak regarding issues
- the procedures followed for decision-making
- where people are located within the business
- the routines that are followed, including the type and frequency of meetings
- the extent to which the organisational structure is obeyed regarding chain of
- the criteria which are used to allow people to be part of an informal group o

Business culture is important for a number of reasons, including:

- It influences whether a business can **respond to external changes**. For examp successful business it became complacent and to some degree believed succe was ill-equipped to respond to increased competition from overseas car manu early 2000.
- **Employee relationships** are influenced by the business culture. It will dictate with each other and whether it is in harmony or not.
- The **organisational structure** is influenced by the organisational culture, as th making is centralised or decentralised. The level of employee participation is d making remains at the top of the business if centralised, whilst in a decentralise delegation.
- The **leadership style** adopted by the business is influenced by the organisatio whether an autocratic or democratic approach, for example, is used and wheth style or remain loyal to one type. If the culture is to use one particular style of when the business operates in an unchanging market, but as conditions alter l experience and confidence to apply a different style to cope with it.
- In a **them and us culture** employees will be used to senior managers making to put forward their own ideas, when it could make a real difference to busines
- At times **change** will be a requirement for most businesses. This can be very p which does not support change or allow for it.
- The **success** of the business is determined by the culture which exists. A cultur circumstances can result in business performance suffering.

A strong corporate culture is extremely important as it can be the difference betw not one culture which is right or wrong. The internal and external conditions will d for the business.

Strong and Weak Cultures

The strength of a company's culture can depend on a variety of factors, such as ho its organisational structure looks like, its public reputation and even how the busi two businesses are alike, and neither are the factors that determine their cultures.

Strong culture

Social media company Twitter has a thriving culture that encourages employees t towards a set of 10 core values. This fosters a shared spirit within the company w for the same result. Google, meanwhile, has made a name for itself as an employe respects the work-life balance and allows time for employee-led innovation.

By being flexible with time commitments, Google is able to motivate its workforce efficient and remain loyal. Twitter achieves the same result by investing in its peo making clearly defined goals that span departments.

Weak culture

Car-hailing service Uber may be an extremely successful company, but its hierarch makes for a weak culture. While the firm's in-office staff may be motivated in a va of ways, the taxi drivers (i.e. the people doing the flagship work) are employed as drivers have fewer rights than those employed directly by the company, potentiall Drivers are unlikely to visit the Uber offices at any point either, meaning they get business. This can cause a decrease in loyalty and high turnover of the workforce.

Energy provider BP is responsible for the 2010 Deepwater Horizon oil spill that oc Tony Haywood, the company's former chief executive, received significant criticism National Academy of Engineering (NAE) claims that, rather than one person being weak culture that led to cost cutting and, eventually, this disaster. Though BP is n financial costs of a process, the NAE suggests that the company's culture would n from happening.

Classification of Company Cultures

Not all organisations share the same culture, but different ones can be found in th classified four types of organisation culture:

- power culture
- role culture
- task culture
- person culture

A **power culture** is usually found in small businesses. There is a powerful individu small group who are dominant and make all key decisions. As they are at the hea decisions made their influence spreads out to others with employees looking to th guidance on what to do. This culture can allow for quick decision-making, but do develop employees to think independently and make their own decisions. As the business expands those at the centre of decision-making may find they are no lon able to cope due to the increased volume of work.

A **role culture** tends to be implemented as businesses grow. It is very much linke bureaucratic system with employees having clear roles which are prescribed in the description. Control over decision-making and supervision of subordinates is bas the organisational structure and not deviated from. Rules and procedures are sig within a role culture. Communication is based on the chain of command, whilst coordination and control radiates from the top of the hierarchy. An organisation w role culture is considered predictable as employees do as they are told. However, unexpected event can lead to the business being ill-equipped to cope, as a role cu tends to be inflexible and does not allow for individual initiative to problem solve, those at the top of the hierarchy determine the action to be followed.

A **task culture** tends to be associated with a particular job or project. A project w
have a particular team and individuals are brought into them, as and when they a
able to provide a required skill or understanding. The value of the individual is no
based on their job title or age, but the value of the contribution made to the team
task culture is empowering as individuals are given control over the way the proje
to be completed. However, making use of different types of experts can cause
coordination problems, if they are coming from different departments, branches,

A **person culture** is evident in organisations where individuals share a similar educational background and form groups associated with specific professions, including teaching and accountancy. They may work in groups to share their expe
but the organisation is the means for them to further their expertise and possibly
careers. Although groups can be recognised, individuals act independently and b
they are superior to the organisation. This culture is effective in organisations wh
independent working is a requirement, such as hospital doctors, but can be
problematic if a more centralised approach is necessary, as individuals are used to
controlling what they do and how.

> **Good to know!**
> The **entrepreneurial culture** was not classified by Charles Handy, but is one w
> initiative, encourages risk taking and sets both financial and quantitative goals
> demonstrate their initiative the organisational structure is flat and flexible, thu
> over the ideas and decisions they implement. These types of organisations ha
> This can encourage employees to demonstrate their potential not only due to
> not be punished for the odd failure. However, it is unlikely employees will rem
> employed if failure is on a regular basis.

How Corporate Culture is Formed and Changed

Corporate culture can arise through a multitude of factors, from the viewpoints of
founded the company to the type of product that the company sells or even the e
who use the products.

Ownership: the original owners of a company refusing to take a step back from it
a significant impact on the culture. Employees may feel anxious by the feeling of
Depending on the owners' approach, however, employees may feel more secure k
the owner for assistance.

Key staff: recruitment and promotion of main roles, such as HR manager and chie
culture of a company where targets and expectations are fed down the hierarchy.

Hours: companies must provide their employees with a minimum of 20 minutes b
work, though this time does not have to be paid. Some companies choose to offe
pay their staff for breaks and allow more than 20 minutes. A business that choose
to motivate its employees and foster loyalty.

Nature of the business: the type of product or service that a business sells can h
A firm that publishes storybooks for children, for instance, may foster a creative cu
workforce to create good stories. An accountancy firm, on the other hand, may b
and attention to detail. While this may relate to the goods a business sells rather
for most firms that happenings in one area of the business (e.g. goods productio
the overall company culture).

The organisational structure is not static and can change over time for a number o

- A **new leader** may be unhappy with the organisational culture and seek to ch are familiar and believes will provide success. Adam Crozier became chief ex set about modernising it by increasing the levels of technology, changing wo offices and making staff redundancies. Part of his strategy was to modernise European businesses, as the loss-making business has to improve. The cultu from one where industrial action was constantly taken when change was ann unions and employees were willing to work in collaboration with the leaders
- A **merger or takeover** can lead to the culture of one of the businesses being In 1998, the vehicle manufacturers Daimler-Benz and Chrysler merged. The f methodical centralised approach with authority given the appropriate respec Chrysler embraced empowerment and encouraged creativity and flexibility. D attempted to adopt a centralised decision-making approach at Chrysler, but resentment within the latter.
- The **external environment** can lead to an organisational culture changing, p government and economic growth influences. Ford was dominant in the car increased competition from Asian manufacturers revealed the business had b respond to market changes. Allan Mulally who was appointed as CEO in 200 the business, which at the time was known for infighting and demonising tho considered these key factors which influenced Ford's lack of competitiveness structure, so managers were able to stay on top of market changes and emp openly with each other without fear of criticism.
- In the 1980s onwards many UK businesses believed the way to **improve perf** a centralised organisational culture to one that allowed greater employee pa management (TQM) and kaizen. This involved changing the culture of the bu making radiated from the top of the hierarchy to one where employees felt e process, along with putting forward their ideas and implementing change wi command for permission.

Difficulties in Changing an Established Culture

Changing the business culture is not so straightforward, as a leader attempting to following problems:

- Employees may not understand the need for change, either due to the fear the used to the way things have been done and do not see anything wrong with it which is exhibited in the form of many meetings between union representative industrial action. The implementation of strategies required for change could b
- If the **communication** to employees regarding why change is necessary is not commitment. Although they may give the signs that they will work accordingl do not, thus resulting in the culture remaining unchanged.
- If **employee participation** has not been part of the decision-making process i change and how, it could lead to the strategies implemented for change failing process and will not provide the required effort or commitment.
- Changing the organisational culture may involve different **resource allocation** some receive a lower level of funding or allocation of other resources, which ca those employees who are part of the department. This can lead to their comm lacking.
- **Funding** may be needed to change an organisational culture, possibly for trainin culture. It can be difficult for those firms facing financial difficulties to find the fu
- The **organisational structure** may in itself be a problem when changing the org hierarchical with decisions made based on the role of people within it, employee us' culture. Changing a culture to one where there is employee participation ma they may still believe that senior managers wish to control each decision made. the required commitment and effort, as they doubt the integrity of the proposed

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The culture of a business should not be based on how it is described by others; the indicators which are noticeable. The existing culture of one business may inappropriate to another, but if it provides business success it is right in that

Do not presume an organisational culture can change quickly, as the respons influence the time taken.

The person initiating the change will have a significant influence on how othe respected and trusted this is likely to encourage the support of employees, w implement.

Remember how people communicate with each other, the decisions made an all be influenced by its business culture. Any form of change in the business w which exists and will determine the level of success achieved.

3.4.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

3. *Explain the difference between a task culture and an entrepreneurial culture.*

4. *Explain **one** problem of an organisational culture changing.*

3.4.3. Shareholders versus Stakeholders

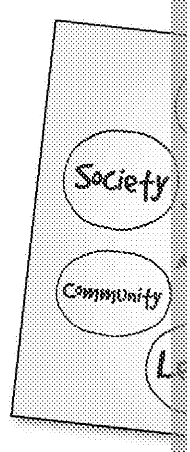
! Key Points Covered

- Internal and external stakeholders and their objectives
- Stakeholder and shareholder influences
- The potential fo and wider objec

Shareholder or Stakeholder?
Stakeholder is the umbrella term for any individual or group that has a vested in residents, employees or council representatives.
A *shareholder* is a type of stakeholder: a person/group that owns part of a privat limited company.

Internal and External Stakeholders and their Objectives

Stakeholders come in all shapes and sizes. As a definition, stakeholders are any individuals or organisations that have a direct influence on or interest in a business. This might include the owners of the business, its shareholders, customers, suppliers and employees, among many others.



Whenever a business makes a decision, it has to consider its stakeholders: their needs and the influence they might have on the business. Some decisions will work out better for different stakeholders and so it is a balancing act for most businesses.

The majority of businesses are no longer just interested in what their shareholders want. Instead, firms look at the bigger picture, which shows multiple different individuals and groups inflicting power over a business'ss decisions. Some stakeholders have more power than others and they all influence the business in different ways stakeholders, their key interests and what power and influence they can have over

	Stakeholder	Key Objectives
Internal	Owners	Survival, growth, positive reputation and acclaime
	Management	Efficiency, low labour turnover, good industrial rel
	Employees	Salary, job security, career progression, motivation
External	Shareholders	Survival, growth and profit maximisation
	Suppliers	High sales, steady growth, good liquidity and pos
	Government	Growth, high turnover, high profits, increased tax awareness
	Financial institutes (banks, etc.)	Repayment of loans/interest, etc.
	Customers	Low prices, quality product, green credentials and
	Local community	Safe place to live, low noise, disruption and pollut

Table: Stakeholders and their key objectives

Stakeholder and Shareholder Influences

Do Businesses Follow Their Stakeholders or Their Shareholders?

While every business exists to make the profit it needs to survive, not every busine maximise its profits. A firm whose goal is social justice, for instance, may invest th business decisions that improve the livelihoods of those it supports. An internatio the other hand, may have powerful shareholders that it needs to satisfy and so thi business decisions.

Whether business decisions and objectives are aimed at satisfying all of a firm's st shareholders will partially depend on how much power and influence each stakeh

Let's use the stakeholder examples again, this time looking at what influence each

	Stakeholder	Influenc
Internal	Owners	Direct missions an
	Management	Enforce objectives in order to m
	Employees	Productivity, potential of strike actio
External	Shareholders	Elect direc
	Suppliers	Availability, pricing, s
	Government	Legislation, prevention of certain busine
	Financial institutes (banks, etc.)	Removal of bankin
	Customers	Spending power, brand aware
	Local community	Complaints to local co

Table: Stakeholders and the influence they have on a business

It is not enough to consider a stakeholder's influence, however; businesses also ne each stakeholder holds.

The power of stakeholders can be broken down into four categories:

Low power, low interest, e.g. unaffected members of the local community
Low power, high interest, e.g. non-management employees
High power, low interest, e.g. suppliers to the company
High power, high interest, e.g. local council

We can draw these stakeholders as a stakeholder map:

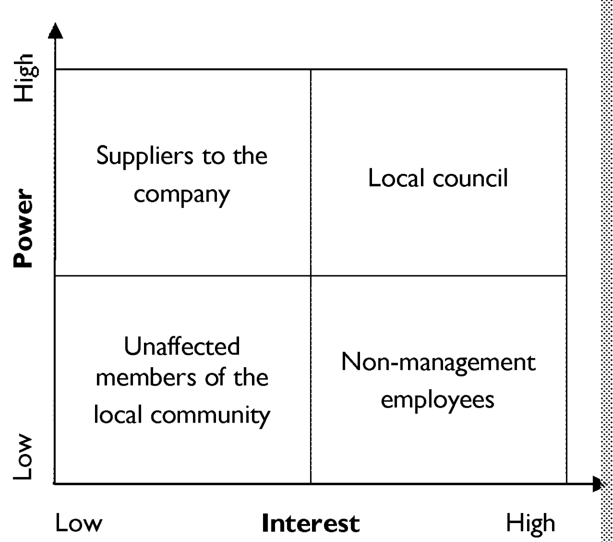


Diagram: An example stakeholder map

The Potential for Conflict Between Profit-based and Wider
The divide between profit-based (shareholder) objectives and wider (stakeholder)
interest for a business.

A business that focuses solely on shareholder expectations is taking a **shareholde**
the business is run purely for the benefit of its owners and any decisions made are
the best return on their investment. The business adopts strategies which maximi
even if it may be to the detriment of other stakeholders.

The shareholder approach may be considered outdated as certain stakeholder gro
requiring the business to give them greater consideration in decisions made. As c
their consumer rights through television programmes and the Internet, businesses
expectations or complaints without serious consideration. Furthermore, the Comp
directors to balance the interests of all stakeholders in the decisions undertaken, r
that attempts to satisfy all stakeholder needs is demonstrating the **stakeholder a**

A business may choose at times to focus on the needs of one particular stakehold
This is known as the **win–lose approach**. Focusing on the needs of one type of st
detriment of another. For example, the Toyota accelerator pedal crisis, resulted in
due to the accelerator pedal sticking whilst cars were being driven. Toyota at this
expectations of consumers who wanted to be driving safe cars. Some models had
problem, which added to the costs of the business. Suppliers may have been put
components at the required standard, as this was the origin of the problem. Shar
to higher operational costs, resulting in a lower dividend allocation, if profits were
business had not acted to deal with the problem its corporate image may have be
both suppliers and shareholders affected, if the continuity of the business was thr

More examples of stakeholder conflict include:

Strikes
betw

- **Management vs Employees:** the management of the company wishes to generate more cash for the company by producing more goods while the employees are not prepared to work harder until their salaries improve.
- **Government vs Owners:** new sustainability legislation means that a company must invest in expensive equipment in order to reduce its levels of carbon dioxide. While important to the environment, this expenditure eats into the potential profits of the company.
- **Suppliers vs Banks:** this conflict occurs as the business needs to keep a positive cash flow in its bank account but also make large payments to its suppliers – if raw materials are not paid for on time, the company will have less flexibility in setting future payment deadlines, or it will have fewer options for ordering supplies in bulk

A business that attempts to balance the needs of all stakeholders is demonstratin
principle all should benefit eventually. A business taking time to work with suppli
increases costs, which possibly could reduce profits and dividend allocations in th
products produced by the business will improve due to the suppliers meeting exp
the reputation of the business which could lead to higher sales and profits. Emplo
allocated a proportion of these in a profit sharing scheme, whilst shareholders gai
dividend allocation. Suppliers obtain repeat business due to their reliability. The
confident of job security in the region with the potential of employment opportur
benefits, as the business is working positively alongside suppliers to improve stan
complying with legislation and reducing emissions. In the short term it may appe
satisfy all stakeholders, but in the medium to long term each one benefits in some

Achieving an A grade

When considering stakeholders how realistic is it that all stakeholders can be s to long term? Does the business need to satisfy the needs of all stakeholders?

3.4.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

5. Explain the difference between shareholders and stakeholders. (4)

6. The sports equipment manufacturer, Tennis Elbow, wishes to create a map o company has 30 employees, most of whom are low-paid factory workers. T materials from one main supplier and sells its products to a select few cons Elbow is based in a small town but the company does not have much impac

Below are three pairs of stakeholders for Tennis Elbow. Explain where each have a conflict of interest.

- Shareholders and Employees
- Suppliers and Consumers
- Business Owners and the Local Community

3.4.4. Business Ethics

! ***Key Points Covered***

- Ethics of strategic decisions and the trade-off between profit and ethics
- Pay and rewards
- Corporate social

Ethics of Strategic Decisions and the Trade-off between Pr

Business ethics relate to the moral values which influence conduct and decisions m whose behaviour and decisions are morally correct. This can be very difficult, as a by one type of stakeholder may not be judged so by another. For example, in 201 selling padded bikini tops aimed at girls as young as seven years. It was considere group should be focused on being children rather than being sexualised. This att coverage, eventually resulting in the product being withdrawn from sale, even tho http://www.guardian.co.uk/business/2010/apr/14/primark-children-padded-bikini

Some of the moral dilemmas faced by businesses include:

- Should charitable donations be reduced as profit margins fall?
- As cigarettes have been linked to illnesses including cancer, should a busines
- Should a business continue to use a supplier who has poor employee workin
- Should a business relocate overseas to reduce costs, even though UK staff wi

Attempting to make ethical decisions that satisfy all stakeholders will be difficult, a expectations and it will be difficult to please all. In particular, there will often be a and acting ethically. Some decisions will require that a business's ethics are (parti order for profit to be possible. A business, therefore, has to balance decision mak it considers the priority.

Making **ethical decisions influences all areas of business activity**:

- **Promotion** – ethical policies used by a business can form part of its promoti brand and differentiates it from others.
- **New product development** – a business may develop products to fit in with consumers, e.g. The Body Shop, Toyota's Prius.
- **Production** – new production techniques may be used to improve efficiency
- **Pricing** – a business may choose to price products based on what is reasona high as the market allows.
- **Human resources** – staff will be trained so ethical standards can be met, but decision-making where possible, so they feel their views are given considerat
- **Financial** – businesses will look to pay suppliers within a reasonable amount o possible. This is very important for small suppliers whose cash flow can be squ not pay promptly. This is a particular problem between some supermarkets ar

Advantages of ethical behaviour include:

- **Easier to recruit and retain staff** – a business that is known for making the the environment, society and its stakeholders, including employees, can find will have a low labour turnover rate. This helps to keep recruitment and train
- **Improved employee motivation** – ethical businesses are believed to have e dedicated and supportive of the business activities than those that are not. T thus leading to high levels of productivity, quality and efficiency.
- **Positive brand image** – making the right moral decisions can help differenti ice cream is renowned not just for its quality, but also the good causes it sup owner as one who has a genuine care about the communities in which they o seeking. This will appeal to consumers who wish to purchase items from eth

- **Competitive advantage** – consumers are now able to find out more about b use, especially with the use the Internet and the requirement for large busine report. A business that is known for making decisions which are detrimental t society could face a fall in demand, as consumers switch to alternatives that s social expectations. A business which meets these expectations will have an a not, which should lead to increased sales and profits.

Disadvantages of ethical behaviour include:

- **Costs** – business costs can increase, as a decision might be made to use a mo provide recyclable materials which are less damaging to the environment. A alongside suppliers to help them adopt more ethical practices, but the time a increases costs. Production changes, in terms of machinery and training, in c and reduce waste will increase costs in the short term. The business may not strategies in the short term, but should in the medium term onwards due to t through efficiency improvements.
- **Lost sales** – The Co-operative Bank will not deal with businesses that produce such as cluster bombs or have poor records on labour rights. This stance resul but it might indirectly gain by attracting consumers who wish to deal with ethi
- **Conflict** – any ethical decision which compromises the profits of the business m shareholders, who do not agree with it. The extent to which an ethical approa influenced by the amount of power shareholders have over this. Balancing the easy, as they have different expectations and this can lead to conflict occurring

The extent to which a business will adopt ethical practices will depend on a range customer expectations, competitors' ethical strategies, influential stakeholder exp changes in the ethical and social environment affect it.

Pay and Rewards

Minimum wage and the difference between a chief executive's pay and that of the in news headlines. This is due to a set of publicly shared ethics. On the whole, co treating its employees unfairly in any way, including when it comes to pay. While of ethics, all other stakeholders (including employees and customers) will have the

When Dyson announced in the early 2000s that it was moving its manufacturing o press and public reacted negatively, some in disappointment while others in outri UK-based complaints was the fact that Dyson had taken jobs out of the country, l Dyson's labour costs had doubled over the 10 years leading to the move. If this tr profits could have fallen even further, a potential outcome that informed Dyson's

Employees in the UK have legislation that protects (among many other rights) the work in a safe environment and their rights to receive fair payment. This is not ne in other parts of the world, however, which can cause problems for companies tha or revenues go down, the business must make a decision in order to stay alive. If important that the company being outsourced to shares the same set of ethics as interests of a business, therefore, to regularly check the company they are outsou expectations, wages and whether child labour is being used).

Businesses that act unethically (either themselves or by outsourcing to unethical c public scrutiny – and those that are caught may never be able to shake off the ne business tries to clean up its unethical act, it can sometimes be too late. Nike and companies that nowadays make certain efforts to be ethical but who are still vilifie who remember their pasts.

Corporate Social Responsibility

Corporate social responsibility (CSR) refers to not only what a business choose… they make them. It addresses how companies deal with their social, economic an… as the effect it has on stakeholders, including customers, suppliers and local comm… acknowledging through its words and actions that it has a duty to these areas an… beyond what is required by the law. Many big businesses now conduct CSR audit… CSR reports which may be made public.

Implementing CSR should provide benefits to both society and businesses. **Socie…**

- **employees** have access to training which allows them to acquire new skills, h… not discriminated against, work in a safe environment and have social events…
- **suppliers** are paid a fair price for their raw materials and components, are pa… training to improve their own working conditions and do not have contracts …
- **customers** receive safe products, which match the description provided. The… into buying and receive good after sales care
- the **local community** benefits from jobs being created, local suppliers receiv… congestion are kept to a minimum, whilst management provides time to sup… to them

Businesses benefit as costs are reduced, the brand image is enhanced, attracting… customer loyalty improves.

CSR strategies can be adopted for a number of reasons:

- CSR underpins the core business values – The Co-operative and The Body Sh…
- operating costs can be reduced through improved efficiency – Toyota Produc…
- fulfilling consumer expectations – car manufacturing industry
- rivals are adopting CSR strategies
- positive brand image – Cadbury sourcing cocoa from Fairtrade farmers in Gh…
- differentiation – Ben & Jerry's
- attract and retain the best employees
- a positive reputation amongst the local community which might make it easi… future plans
- legal requirement

The extent to which a business will adopt CSR strategies will depend on many fact… expectations, the extent to which it is scrutinised by the public and threat of legal … are not complied with will influence the final decision.

3.4.4. Questions

Please write your answers on a separate piece of paper or in an exercise book.

The West Nose plc is a UK-based designer and manufacturer of outdoor clothin… is popular with adventurers, such as climbers and travellers, and also with peopl… fashion. Even though the brand is popular, The West Nose's profits have decrea… company's leadership is now discussing whether to cut its current supplier, a fac… sourcing materials from two factories in Taiwan.

7. *Explain what the trade-off might be for The West Nose choosing to cut its curr…*

8. *Other members of the company's leadership suggest that The West Nose plc u… responsibility (CSR) as a way to improve profitability. Explain how the compan… way.*

3.4. Answers

1. *Evidence-based decision-making requires that business leaders have all the re making a decision. When a decision is finally made, it is often done so as a tea person. Subjective decision-making involves the business leader(s) making a j is right for the business or not.*

2. *A disadvantage of evidence-based decision-making is it can be time consumin analysis involved, along with the participation of others in reaching a final de gut instinct decisions, which can generate a high level of added value, as they*

3. *A task culture is linked to a particular task or project, which brings together a team. It is empowering as the team has responsibility for the completion of th way to complete it, as their different skills and expertise are used at different s entrepreneurial culture encourages employee initiative and risk-taking with r*

4. *An organisational culture can be difficult to change due to staff resistance, co organisational structure which exists and lack of funding.*

5. *A stakeholder is a group or individual who has an interest in the decisions ma them. They may seek to influence these. A shareholder is an owner in a comp stakeholder.*

6. ***Shareholders and Employees:** While shareholders might be looking for high dividends, employees may rather that higher profits were spent on increasing conditions.*

   ***Suppliers and Consumers:** Tennis Elbow's consumers may demand more pr suppliers of raw materials can fulfil.*

   ***Business Owners and Local Community:** If the business owners wish to exp more space in order to do so. This may bring about pollution and/or congesti the local community.*

7. *The West Nose's leadership is considering a trade-off between ethics and costs supporting UK suppliers as a UK company is perceived as ethical. On the othe supplier helps a company's profitability.*

8. *The West Nose plc could focus on CSR when marketing itself to consumers. If those of its consumer base, it could help enhance its brand reputation, enticin Promotion of CSR also helps the company to advertise how it differs from its r*

   The company could focus on CSR when negotiating with suppliers, e.g. securin exchange for agreeing to a six-year contract.

   The company could also promote its CSR in order to attract the very best wor workers could then help the business to achieve higher rates of productivity a profitability.

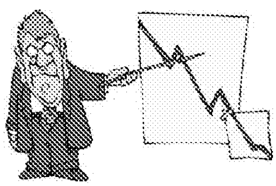
3.5. Assessing Competitiven

3.5.1. Interpretation of Financial Statements

! Key Points Covered

- Statement of comprehensive income (profit and loss account)
- Statement of financial position (balance sheet)
- Stakeholder inte

Statement of comprehensive income (profit and loss accou



The statement of comprehensive income (also called the income statement) will give us a summary of **profit** (or l before and after deductions. In its simplest form, the sta minus expenses. Money in minus money out; what is le company an idea of their financial performance.

Let's use an example:
The following shows a statement of comprehensive income for Multiple Clothing and thousands).

Financial period	2014–2015	2013–2014
Total revenue	9,537,000	9,062,000
Cost of revenue	(6,029,000)	(5,786,000)
Gross profit	3,508,000	3,276,000
Total operating expenses	(8,686,000)	(8,296,000)
Operating income or loss	851,000	766,000
Income from continuing operations		
Total other income/expenses net	-	-
Earnings before interest and taxes	851,000	766,000
Interest expense	(136,000)	(166,000)
Income before tax	-	-
Income tax expense	180,000	199,000
Minority interest	3,000	1,000
Net income from continuing ops	526,000	508,000
Non-recurring events		
Discontinued operations	-	-
Net income	526,000	508,000

Key information of the income statement:

Revenue	Completed sales where goods have been delivered to have been received
Cost of sales (or COGS)	Cost of goods sold (COGS) = Purchases + opening st
Gross profit (SR-COGS)	GP = revenue – cogs
Net profit	NP = GP – expenses
Operating profit	This is profit from regular trading not unusual trading interested in this figure because it shows year on yea performing. Buying shares is risky so shareholders w record of operating profit.
Net income	This is the final figure after all deductions. Start here bottom line', generally look for trends in this increasi the company is in trouble. Total revenue – total expenses.

How do we analyse a statement of comprehensive income?

1. You are looking to compare data either between companies or against a diffe
   Like shoes, you need two sets of data; statements have meaning on their own,
   this meaning is restricted.
2. You need to be looking for trends in expenses, profits or revenue; are they go
   down over time?
3. Once you have established if the figures are going up or down over time you
   causing that effect. Look back through the case study for anything that will h
   - Sales revenue: perhaps a raise in price or sale of larger quantities (as SR
   - Expenses: the company may have been through a period of major refurb
   - Profit: has this significantly fallen or risen? What factors might this be at
     period of retrenchment due to the recession and this has had an impact
     activity meant that they have been price cutting to boost flagging sales?
4. Now look at the revenue and COGS figures. The cost of revenue (cost of sale
   too high compared with the sales revenue. If it is they may run the risk of ma
   if their customers squeeze these margins by demanding lower prices, they co

Statement of financial position (balance sheet)

In very basic terms, a balance sheet is a snapshot in time of what the company ow
It shows what belongs to the company and what the company needs to pay back.
company an idea of their financial position.

Let's use another example:

XYZ food retailing multiple plc (all figures in GB

Financial period	2014–2015	2013–2014	2
Non-current Assets			
Long-term investments	756,000	62,000	
Property plant and equipment	-	-	
Goodwill	3,337,000	3,234,000	
Intangible assets	-	-	
Accumulated amortisation	-	-	
Other assets	-	-	
Deferred long-term asset charges	38,000	49,000	
Current Assets			
Cash and cash equivalents	2,819,000	3,509,000	
Short-term investments	1,314,000	1,233,000	
Net receivables	3,969,000	4,869,000	
Inventory	2,729,000	2,669,000	
Other current assets	597,000	780,000	
Total current assets	11,765,000	13,479,000	
Total assets	**46,023,000**	**45,564,000**	**3**
Current Liabilities			
Accounts payable	5,126,000	4,910,000	
Short/current long-term debt	13,515,000	15,862,000	
Other current liabilities	7,058,000	7,513,000	
Total current liabilities	16,015,000	17,595,000	1
Long-term Liabilities			
Long-term debt	11,822,000	12,195,000	
Other liabilities	-	-	
Deferred long-term liability charges	559,000	453,000	
Minority interest	-	-	
Negative goodwill	-	-	
Total liabilities	**31,427,000**	**32,715,000**	**1**

The balance sheet is split into three sections.

Assets: Items of value owned by XYZ food retailing multiple plc Current assets (likely to be turned into cash within a year): • Inventories (the value of stock held) • Net receivables (debtors: cash owing from credit sales) • Cash and cash equivalents (cash in hand or in the bank) Fixed assets (likely to be kept by the business for more than one year, long term • Vehicles, vans and lorries that make deliveries • Shops and stores • Machinery and equipment like a forklift in the warehouse or even a meat sli • Goodwill, strong brand name, customer loyalty, reputation • Long-term investments, stocks and shares
Liabilities: Items owed to others by XYZ food retailing multiple plc Current liabilities (have to be paid within a year): • Accounts payable (money owed by XYZ to others for goods or services rece • Short/current long-term debt (the portion of long-term debt that XYZ must Long-term liabilities (likely to be paid by the business after one year, longer term • Long-term debt (loans lasting more than one year) • Deferred long-term liability charges (money XYZ owes but has not yet adde
Stockholders' equity • Stockholders' equity is the net worth of a company. It represents the stockh retailer's assets after all creditors and debts have been paid. It shows total a not shown on the previous example for reasons of simplicity (and the data i usually not be required to comment on it in an exam.

Stakeholder Interest

Looking at an income statement and the balance sheet together can provide an e health and performance of a company. Many different stakeholders will want to u for a variety of reasons.

Stakeholder	Balance Sheet	P
Owners, managers, leaders and key employees	These stakeholders may be interested in the financial stability of their company. If, for instance, there is opportunity for the firm to invest, leadership will need to know whether there are already high debts held against the business. They may also may be interested in the ability of their firm to meet the interest charges on outstanding loans or debt; firms go out of business because they run out of money, and the lifespan of the business can be hidden in the numbers of its statements.	Businesses accounts a the accou much easi Businesses doing aga foreign co Business le financial d strategies.
Shareholders	These may find it useful to know how effectively the business it owns; if the company is inefficient this will be revealed by ca management. Inefficiencies are very bad news, particularly in poor dividend yield ahead, so shareholders may choose to inv	
Employees	These stakeholders may be particularly interested in the financial stability of the company. After all, without this employees have less chance of increasing their pay or even feeling secure in their jobs.	Employees salaries m company's whether a possible.
Suppliers	Suppliers that negotiate trade credit will want to know about the solvency of a business, i.e. whether it can pay its long-term financial obligations. Liquidity will be an issue here, too: does the firm have enough working capital available to convert into cash when required?	A profit an a good ind company c time.
Government and Office of National Statistics (ONS)	A government may wish to look at a firm's balance sheet in assessing its liability for tax, or different government departments may look at it to assess the size of a business for policy reasons, e.g. in assessing how competitive the market is or how stable an employer it might be.	Businesses profit and HMRC to c This tax is country's b infrastruct

3.5.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

1. *Explain the meaning of:*
   a. *Cost of sales*
   b. *Current assets*

2. *Pies 'n' Chips Ltd has been in business since 2013. The company, which empl sells pies (catering for all dietary needs) and what local people have come to fried'. The company's leadership has found a new supplier of flour and is look However, the supplier has requested to see some financial information.*
   a. *Identify which type of financial document the supplier might be requesti*
   b. *Explain why the supplier may wish to see this financial document.*

3.5.2. Ratio Analysis

! *Key Points Covered*

- Gearing ratio
- Return on capital employed (ROCE)
- Interpretation of ratios to
- Limitations of ratio analys

Businesses use financial data (such as gross, operating and net profit) in order to already studied ratios in the form of *gross*, *operating* and *net profit margins*. These business is performing by comparing one financial statistic against another. In the business is contrasting its gross/operating/net profit with the amount of revenue *Current* and *acid test ratios*, meanwhile, compare current assets (or current assets current liabilities.

Two more ratios, *gearing ratio* and *return on capital employed*, compare figures w business employs.

Gearing Ratio and Interpretation

Gearing shows how much of a business's finances are secured in long-term borro a company is in. A highly-geared ratio means they are running on a lot of debt, w interest will be a drain on future profits and possible dividends. For example, if a borrows a further £6,000 once they have spent that money they still have to find p pay it back to the lender. Imagine this on the grand scale of a plc borrowing in m is risky, a bad year of trading or a rise in interest rates and the debts could cripple what happens they still have to pay back the loans. If they lose revenue they may the loans. Financing the finance or 'robbing Peter to pay Paul' is an expression yo

	What you are given on the formulae sheet	How to calculate it	
Gearing Ratio	$\frac{\text{Non-current Liabilities}}{\text{Capital Employed}} \times 100$	Divide non-current liabilities by the sum of [total equity + non-current liabilities]. Multiply the result by 100 to get a percentage.	Over 50% geared (lo that a co To solve t issue mor share cap

ROCE and Interpretation

If the main aim of business is to make a profit then looking at how profitable it ha performance as a business. Return on capital employed shows how profitable an money. If you were a marathon runner, for instance, the indicator of your perform useful, but a comparison with last year's performance is even better, i.e. did you r due to the thunderstorm that happened halfway round?

	What you are given on the formulae sheet	How to calculate it	
ROCE (return on capital employed)	$\frac{\text{Operating Profit}}{\text{Capital Employed}} \times 100$	Divide operating profit by the sum of [total equity + non-current liabilities]. Multiply the result by 100 to get a percentage.	ROCE is i needs a c derive me instance, for every favourabl they wou account a

The Bigger Picture
Companies compare their gearing ratios and returns on capital employed with co
market. This helps leaders understand whether the ratios are acceptable.

Highly Geared vs Low Geared

A company that is highly geared (i.e. with a ratio over 50%) will have a lot of debt,
low geared (i.e. with a ratio of less than 50%) will have significantly less debt. The
geared companies come from their shareholders rather than from long-term debt

Being highly geared, therefore, is a risky move. Some of the reasons for compani
- the business plans to expand and needs to take out loans in order to achieve
- a firm needs to purchase machinery in order to generate more goods and, ev
- the firm is buying out a rival company, forecasting that it will be profitable to
- a company is swimming in debt and needs some way of paying it off
- the company is unable to make its day-to-day payments

The Value of Using Ratio Analysis

Ratios can be a useful tool for a business to look at the health and performance o
conclusions about how it is doing from a financial viewpoint.

Comparison

The main benefit is the ability to boil down numbers so that useful comparisons c
another student. How do you know the difference or the similarities between you
looking. What about if you had shoes sizes to compare, or height or even predict
you can make some effective comparisons. It's the same with a business and ratio
format that can be compared.

STEP 1
Find the data in the case study

STEP 2
Calculate the ratios

STEP 3
Compare two ratios, e.g. year on year or company a with company b

Diagram to show steps in the ratio process

Decision-Making

Comparing ratios will give the business useful information from which to draw co
be used as a decision-making tool. The organisation may use the information to s
objectives, link financial strategies to new objectives or create new strategies. Do
for Success so keep coming back and linking your ideas to objectives and strategi

Financial Health

Imagine the start of a journey that will take one year. In order to know where we
we are now and if we are going to be healthy enough to make the whole journey.
this information. It lets them know if the business is efficient enough, if it has eno
new objectives for the next year. Is the business able to meet its short and long-t
trading in a year's time? Does new finance have to be arranged so that the comp

Limitations of Using Ratio Analysis

In your exam you need to see the advantages and disadvantages of just about eve exam writing time should be weighing up ideas for the values and drawbacks and conclusions about which choice the business should make based on your analysis

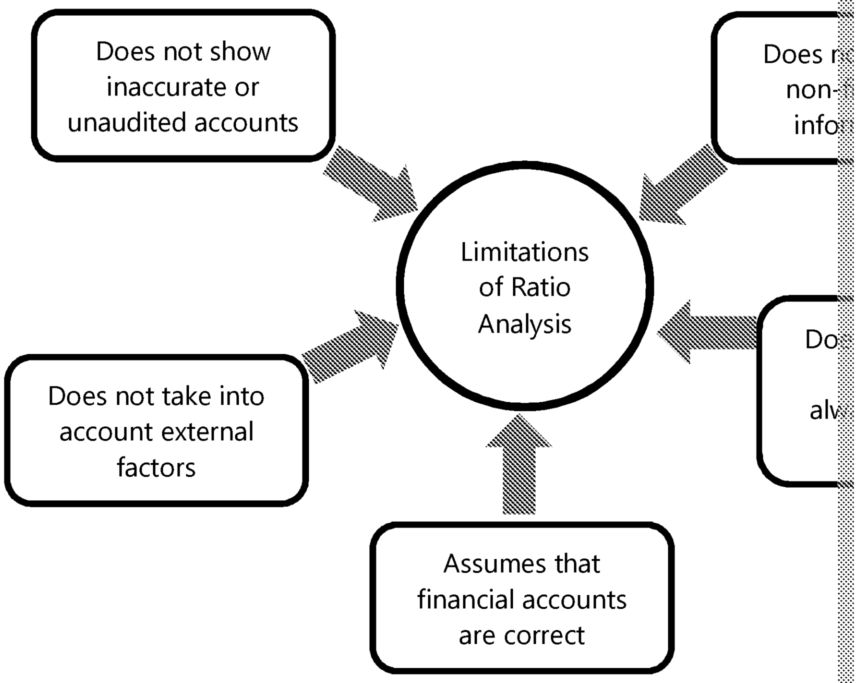


Diagram to show main limitations of ratio analys

Time: Ratios are not much use unless performed over a long-enough period of ti will depend on the industry among other factors. Time can also change businesse cuddly toys but then moves on to wearable technologies, a long-term ratio analys

External factors: Any ratio analysis will not be able to take into account external impact on the results. For example, a company showing 9% growth when inflatio 3% growth.

Financial information: in relation to the time factor, financial statements only co they were constructed. Many other factors could have come into play over the co render a company's profit and loss account an unfair representation of their succe

Non-financial information: Ratio analysis can't show competitor activity or whet through major changes, such as hiring a new MD. Ratio analysis also won't be ab new products have been launched or if the company has been subject to takeove ratio analysis is quantitative not qualitative so can only give you part of the story.

3.5.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

3. **a.** *Identify the meaning of 'gearing ratio'.*
b. *Identify the meaning of 'ROCE'.*

Tomfoolery International Ltd is a designer and manufacturer of jokes. Below i company's finances during 2015–16.

Tomfoolery International 2015–16	
Current assets	*£73,000*
Current liabilities	*£50,000*
Non-current liabilities	*£123,000*
Total equity	*£114,000*

4. **a.** *Calculate the gearing ratio of Tomfoolery International Ltd to 2 dp.*
b. *Explain the financial position of Tomfoolery International Ltd judging by its*

3.5.3. Human Resources

! ***Key Points Covered***

- Calculations and interpretations to help make business decisions
- Increasing produ reducing turnov

The calculation and interpretation of human resources data can inform the decisio bringing with it many other benefits:

- A business can analyse itself against previous figures to understand whether i
- Measurements can inform milestones for both a business'ss leadership and t
- A firm can use its past and present data in order to project potential outcome
- Data over time gives an idea of a business'ss limits

Labour Productivity

Labour productivity shows the number of units that one worker produces per peri An increase in labour productivity shows the business that its workforce is becomi decrease in productivity shows the opposite. There are many factors that can influ including motivation, pay, place of work, health and safety, rival companies and st

Outputs can include the amount of productivity per person, per factory or per machin monitor their employees on how many sales they make. This productivity is measure

Labour productivity is measured using the calculation:

$$\text{Labour Productivity} = \frac{\text{Total Output (over specific per}}{\text{Number of Employees (over specifi}}$$

Let's use an example:

Gloved Elegance Ltd employs a team of 70 textile workers, who produce 3,500 pai labour productivity of the firm's 70 employees in one week, we can calculate:

$$\text{Labour Productivity (in units)} = \frac{\text{Output per week}}{\text{Number of Employ}}$$

$$\text{Labour Productivity (in units)} = \frac{3500\text{ units}}{70\text{ workers}}$$

$$\textbf{Labour Productivity (in units)} = \textbf{50 units per worker pe}$$

We can also calculate labour productivity in terms of time, i.e. how much time it ta use the gloves example again, this time including the total time that employees w hours:

$$\text{Labour Productivity (in time)} = \frac{\text{Labour hours per w}}{\text{Units produced per w}}$$

$$\text{Labour Productivity (in time)} = \frac{2100\text{ hours per we}}{3500\text{ units per we}}$$

$$\textbf{Labour Productivity (in time)} = \textbf{0.6 hr per unit}$$

This tells us that it takes 0.6 hours (around 35 minutes) on average for Gloved Eleg

Labour Turnover

This figure shows the rate at which staff leave a company, either through resignat terminating their contracts. Businesses calculate this figure using the following:

$$\text{Labour Turnover} = \frac{\text{Number of staff leaving per period}}{\text{Average number of staff}}$$

If a firm employs an average of 30 staff and loses 6 members per year, the calcula

$$\text{Labour Turnover} = \frac{\text{6 staff leaving per year}}{\text{30 staff on average}} \text{ x } 100$$

$$\textbf{Labour Turnover = 20 per cent}$$

Labour Retention

We use the opposite calculation to find employee retention. This shows the rate a the firm:

$$\text{Employee Retention} = \frac{\text{Number of staff staying per period}}{\text{Number of staff in the company}}$$

In the case of the previous example, we would subtract the number of people who employee retention:

$$\text{Employee Retention} = \frac{\text{Number of staff staying per year}}{\text{Number of staff in the company}}$$

$$\text{Employee Retention} = \frac{\text{(Number of staff in the company – Number of staff}}{\text{Number of staff in the company}}$$

$$\text{Employee Retention} = \frac{(30 - 6)}{30} \text{ x } 100$$

$$\text{Employee Retention} = \frac{24}{30} \text{ x } 100$$

$$\textbf{Employee Retention = 80 per cent}$$

Absenteeism

This calculation shows the number of staff that are absent from work at any given

$$\text{Absenteeism} = \frac{\text{Total staff absent per period}}{\text{Total staff employed per period}} \text{ x } 1$$

Let's stay with the same firm we originally calculated labour turnover for. Human absenteeism level for 1st June.

$$\text{Absenteeism for 1st June} = \frac{\text{Total staff absent on day}}{\text{Total staff employed on day}}$$

$$\text{Absenteeism for 1st June} = \frac{9}{30} \text{ x } 100$$

$$\textbf{Absenteeism for 1st June} = \text{30 per cent}$$

The company may have decided to calculate this rate because the number of peo noticeable. The average rate of absenteeism for the firm is 5 per cent and so 30 p real concern!

Reasons for absenteeism can range from an employee having a genuine illness or interview and simply wishing to skip work every once in a while. Absenteeism can where an employee feels undervalued or has lost the drive to achieve in their wor

Considerations for Human Resource Data

Each set of data, from labour productivity to absenteeism, represents costs for a b showing up for work, for instance, a firm will need to spend money to replace the workforce will cost the firm in goods production and, therefore, sales.

Data gives a story; however it only gives one side of a story. A business with high have significant human resources problems. However, it is important to also cons market in which it operates. Is this normal? For some industries, such as Teaching (TEFL), it is the norm to hire employees (teachers) on short-term contracts of a yea

The use of human resources data only, without considering why an outcome has a business decisions. A firm may find, for instance, that its labour productivity is low workforce training. This might have an effect if the productivity issue is to do with however, if the drop in productivity is actually down to the machinery available. A human resources data in line with any other means available, such as communicat sharing responsibilities.

Increasing Productivity and Retention and Reducing Turnov

Financial Rewards

By offering employees financial rewards, such as bonuses for high achievement, a productivity. Financial rewards can entice employees to stay with the business an Piece-rate work can also help motivate as the more productive employees receive to continue being productive.

One problem for many a worker is the lack of upward mobility from their role. Th and/or pay increases, therefore, can help retain employees and reduce labour turn the call centre industry, have a significant problem with absenteeism. Some comp bonuses to employees who hit attendance targets.

Employee Share Ownership

Businesses can give employees the chance to purchase shares in their company. B directly affects the business's profits, once employees have shares in these profits more productive.

Share ownership can also improve labour retention rates. Businesses can offer em over a specific period, e.g. five years, with the promise that they can receive a cash This can motivate employees to stay with a company for longer, knowing that the end of the period.

Consultation Strategies

Employee consultation involves including the workforce of a business in the decis normally done by the business informing employees after a decision has been ma decisions to the business (normally through representatives, such as union leaders between the business and its employees.

By being including in a business's decision-making process, employees may feel m loyal to the business. Consultation may, therefore, help increase employee retent also have the potential, however, to reduce productivity of a business if the decisi

Empowerment Strategies

In relation to employees feeling valued, a business can empower its workforce in o as a result, productivity and labour retention. Forms of empowerment include giv responsibility, assigning specialist roles within the organisation, training employee their careers and investing in any extra equipment (e.g. specialist computer progra jobs more efficiently.

3.5.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

5. *A supermarket is calculating its labour turnover over a six-month period. On has a total of 127 employees. During the six-month period, the supermarket*

  (a) *Calculate (to 2 dp) the labour turnover for the six-month period.*
  (b) *Explain what the supermarket should do with this data.*

6. *Explain which human resource strategy might best help the supermarket in qu*

3.5. Answers

1. a. *Cost of sales excludes any of a business's expenses, instead focusing on opening stock plus purchases and its closing stock.*

   b. *Current assets are assets that a business can turn into cash within one y*

2. a. *The supplier may wish to see either the statement of financial position or income.*

   b. *The supplier may wish to see the statement of financial position in order liquidity of Pies 'n' Chips Ltd. The supplier will want to know whether Pie working capital to convert into cash when necessary and that the compa long-term financial commitments.*

3. a. *Gearing ratio shows how much of a company's finances are funded by lon*

   b. *ROCE (return on capital employed) shows the profitability of an investor'*

4. a.

$$Gearing\ Ratio\ (GR) = \frac{Non\text{-}current\ liabiliti}{Capital\ employed}$$

$$GR = \frac{Non\text{-}current\ liabilities}{Total\ equity + Non\text{-}current\ liabiliti}$$

$$GR\ for\ Tomfoolery\ International\ Ltd = \frac{123,}{(114,000 +}$$

$$GR\ for\ Tomfoolery\ International\ Ltd = 51.90$$

   b. *With a gearing ratio of 51.90%, Tomfoolery International Ltd is highly ge position. The company's leadership needs to consider its expenditure in o has on external funding, such as bank loans.*

5. a.

$$\text{Labour Turnover} = \frac{\text{Number of staff leaving per perio}}{\text{Average number of staff}}$$

$$\text{Labour Turnover} = \frac{\text{43 staff leaving per month}}{\text{127 staff on average}} \text{ x 1}$$

Labour Turnover = 33.86 per cent (to 2 dp)

   b. *Labour turnover data on its own gives only the result. There is not much supermarket, therefore, should find any other data to compare this with include other periods of labour turnover and also data from alternative c when there were economic downturns, booms, etc.).*

6. *The supermarket could benefit from any of the following:*

   ***Financial reward strategies:** on the whole, supermarkets do not pay much w The supermarket in question, therefore, could increase the wages of its worke rivals and, in turn, retaining more of its employees.*

   ***Employee share ownership strategies:** this type of strategy would help the from its workers. If enough workers had shares in the business, the business m and service as workers would be aware that the better their employer appear it becomes to shareholders.*

   ***Consultation strategies:** this strategy could help employees feel more includ as if their voices really matter. However, the supermarket may not wish to inc some of them are part-time workers only.*

   ***Empowerment strategies:** the supermarket could employ this strategy by gi employees (such as having responsibility for a certain section of produce). Th retention and also fill employees with pride, delivering a better service to cust*

3.6. Managing Change

3.6.1. Causes and Effects of Change

! ***Key Points Covered***

- Causes of change
- Possible effects o

Businesses can change for a variety of reasons, from pure necessity (i.e. the firm wi
long-term strategy (e.g. leadership wants to grow the company's market share).

Changes in Organisational Size

It is often presumed that each business's goal is to grow, but this is not necessarily
owners to remain in complete control of how a firm is run. There may be a fear th
lose some control over its running, especially if new owners are introduced to fun
employees are hired to complete the tasks they are unable to give their full attent
not grow beyond a certain size allows the owners to not only keep control, but als
important to them, such as being a traditional family business.

Some businesses wish to grow for a number of reasons including:

- benefit from economies of scale
- increase profitability
- increase its market share
- improved competitiveness
- spread the risk of failure by diversifying
- satisfy the ambitions of the owner

A business which becomes too big may suffer from diseconomies of scale, as com
slow down. This leads to the unit cost increasing as it becomes bigger. It may ch
internal or external reasons.

Issues for Management to Address

- **Communication:** as a firm grows, it must develop its communication system
  not get lost in bureaucracy.
- **Performance Management:** a small business may have an easier time with m
  large business. As a business grows, therefore, management may decide to i
  employees, though at the potential cost of motivation.
- **Training:** a growing business is likely hiring people on a regular basis. Leade
  invest in the training of new employees. This includes time to teach people a
- **Motivation:** as a business grows, earning potential for employees can expan
  between employees, reducing empowerment and motivation. Once the num
  certain level, the leader of a business can also find difficulty when attempting
- **Labour Costs:** growth allows a business to automate many of its processes, r
  demotivate many staff members, however, as they see their peers become re
  addition, part of growing a business involves hiring more people, who repres
- **Impact on Business Culture:** as a business grows, new ideas can develop, al
  either being improved or replaced. Culture is something that every employe
  may resist change if it affects this element of their working lives.

Possible Effects on a Business

- **Competitiveness:** a business can empower itself to become more competitiv another business. This helps the firm gain market share and bargaining pow
- **Productivity:** economies of scale allow a business to improve its efficiency a increasing its number of people, equipment and locations. With a takeover, a processes which help improve the productivity of its workers.
- **Financial performance:** business growth requires investment. A form of pos issue while a negative, highly geared growth might arise from a business taki
- **Stakeholders:** all stakeholders are affected when it comes to business growt buy at cheaper prices while suppliers may receive more business as a result o can be negatively affected if businesses encroach on environmental standard benefit from more opportunities within the organisation as a result of growth

Poor Business Performance

A poor business performance can be identified in a number of ways:

- falling market share
- loss-making
- lack of competitiveness
- falling quality
- poor business reputat
- difficulty in attracting

Usually a business with a poor business performance will struggle to keep shareho confident that strategies are in place to turn it around with the right leader at the missing the existing leader will be replaced. A new leader may be brought in to in including business competitiveness, market position, finances or reputation.

A new leader may be required to make immediate changes, if the continuity of the short term. This may lead to the closure of some divisions with redundancies inev in order to reduce its debt burden or to provide funds for the new strategies to be

A business whose continuity is not under immediate threat may not see any chan months, as the leader familiarises themselves with all its activities from an internal gives them enough time to determine whether the current board of directors have work alongside them effectively, but also to move the business in the required dir new leader feels this is lacking they will look to bring in new employees and direct them. The review of the business also provides the leader with sufficient time to u areas of the business to concentrate on and which ones to dispense with.

As a new leader makes changes the following may form part of their decisions:

- restructuring
- staff redundancies
- new staff may be hired who have the skills to support the long-term vision
- brands or subsidiaries are sold which do not form part of its long-term plans provide income for future plans or can be used to reduce debts
- operational costs may be reduced by introducing new production methods o

Issues for Management to Address

- **Improving business performance:** this is often a motivator for change. Ma a way to change the fortunes of their business. It is important, however, to g jumping from one issue to the next.
- **Resistance to change:** employees, especially if their employer appears to be respond negatively to any changes, seeing them as demotivation. Customer just look at what happened when Coca-Cola introduced *New Coke*!
- **Changing objectives/strategy:** management must be aware of their industr If, for example, a firm's overall objective is profit maximisation but it is perfor need to change to survival. It is also important for managers to consider at w objective can change back to profit maximisation.

Possible Effects on a Business

- **Competitiveness:** poor performance can lead to a business becoming less co the market.
- **Productivity:** poor business performance often stems from low productivity. business is left with locations/equipment that are not reaching their capacity.
- **Financial performance:** businesses may become dependent on borrowing fo geared that it needs to borrow in order to pay day-to-day expenses, it is at ri
- **Stakeholders:** employees may suffer redundancies or even termination if the standard. Businesses can also push too hard due to the threat of poor perfor

New Ownership

A business may grow or even shrink in size due to new owners who have a differe perspective on the direction it should take. The values, attitudes and experiences they bring with them can all influence the aims, objectives and strategies. Some w make changes as soon as they become a member of the business, as they wish to bring in their own management team who they know shares their vision and way o working. This could lead to some managers/directors being replaced or relocated elsewhere in the business. This can leave staff very uncertain about their future, which could lead to an increase in labour turnover, as they find jobs elsewhere. In these circumstances, staff morale may fall due to fears of job security and a difficu getting used to a different style of working. Other new owners will take time to g to know fully the strengths and weaknesses of the business before identifying the corporate strategies to be followed.

Change is automatically assumed with some new owners if they have been broug in to turn around a struggling business. It is assumed they will makes significant c which have gone before their arrival are not working, otherwise their appointmen

A business is likely to be restructured with the arrival of a new owner, especially if competitive and financial difficulties. This often means a change in the organisati and remaining staff required to take on new roles. The restructuring may provide staff to be given greater responsibility, especially if part of the restructuring is due

Issues for Management to Address

- **Role duplication:** if a company merges with, or takes over, another, there is be merged. This can cause conflict between the business and certain employ themselves.
- **Culture clash:** there is more than one way to do most processes. Changes ca and upset the balance for employees.
- **Brand management:** if a takeover is unpopular (e.g. when Nike purchased tr customers may turn away. Likewise, when a business takes over a brand, it m that the brand has created.
- **Communication:** some businesses use instant messaging while others stick t these methods, but it would benefit the business if employees were consulte

Possible Effects on a Business

- **Competitiveness:** new ownership can increase competitiveness as a compan produce, sell and market.
- **Productivity:** new owners might have successful methods of motivation that productivity. On the other hand, new ownership that clashes with the curren and productivity.
- **Financial performance:** new owners will find any acquisition to be expensive resources. However, a buyer's brand can sometimes improve the reputation o sales, even raising the value of the firm on the stock market.
- **Stakeholders:** new ownership can bring redundancies to a company, especia things is different to the business being taken over. Suppliers may also lose o different ones in mind. Shareholders can also lose out if share prices then fa

Transformational Leadership

Businesses sometimes take on new CEOs. In this instance, the business's objectiv influence whether the business becomes smaller or bigger. A business that aims t seek to become larger, as this is a natural outcome of this strategy. A business th activities is likely to become smaller as those divisions which do not fit into these be brought in to address the *financial performance* of the business may lead to so areas being sold to support its continuity, e.g. HMV selling Waterstones. In these becomes smaller.

Issues for Management to Address

- **Resistance to change:** when leadership of a firm changes, every employee is can change, especially if new leadership has been brought in after the previo performance. Whether previous strategies were best for business or not, it ca to convince subordinates and for management to take to the new strategy.

Possible Effects on a Business

- **Competitiveness:** if the change in leader is a positive one, it can significantly opposite would be true, however, if leadership took the company down the i
- **Productivity:** similar to competitiveness, if motivation is reduced due to cha likely suffer.
- **Financial performance:** if strategy suits investors, share price may increase.
- **Stakeholders:** every member of an organisation can be affected if new leade against the previous leadership.

The Market and Other Factors: PESTLE

External factors, such as a *change in consumer tastes*, can either increase demand f As consumers have become more concerned about the treatment of suppliers increased demand for Fairtrade products. As consumers became more willing to b this encouraged Cadbury in 2005 to takeover Green & Blacks.

Competition policy may permit two businesses to merge or one to take over anoth that certain parts of the enlarged group are sold. This is usually to prevent a busi markets or regional areas at the expense of other businesses and consumers. Wh 2004 it had to sell 53 of the latter's stores, otherwise the Competition Commission deal. This was aimed at providing a fairer competitive environment for both com some towns would have a Morrisons and a rebranded Safeway located close toge

The *economic climate* can present opportunities and threats. In a recession a busi as a means to survive, if demand is falling. It will hold onto those parts of the bus The recession can also present growth opportunities for businesses providing goo popularity as consumers' disposable income falls, e.g. Poundland. A growing eco confidence and demand, which results in increased output and expansion throug

Issues for Management to Address

- **Corporate objectives change:** when external factors change, management m objectives. Survival, for instance, may no longer be enough once the market need to increase its presence.
- **New strategy:** similarly, new entrants to the market may force the business's in different ways, such as incorporating more technology.
- **Research and development:** external forces acting on the market and on th investigates new products/services and/or new ways of providing them.
- **Brand strategy adjustment:** as external factors have more sway on the mark more corporate social responsibility), a business must respond accordingly, t

Possible Effects on a Business

- **Competitiveness:** changing markets and their external influences can have g remains competitive.
- **Productivity:** as technology improves, a business's processes can be made m also might affect a company's ability to be productive by outlawing certain a
- **Financial performance:** much like with productivity, legal and environmenta following particular processes, losing the firm essential revenue. Social issue company in a negative light, may, for example, have an adverse effect on sha
- **Stakeholders:** almost all stakeholders can be affected by external changes. S give a company a poor reputation, affecting those who supply it with raw ma force the company to scale down its operations, resulting in redundancies.

Achieving an A grade

Every business will experience some form of change either due to internal or Although a business may be experiencing the same influences as another, wh change and others are not? If a business has changed size what has influence particular method and not another? Have finances had a role to play or is it leader or owner? As the business changes which stakeholders are affected? W influenced differently to the same type of stakeholders at a different business

In an essay if required to consider the benefits and drawbacks of growth try firms, which have used the same method. Analyse why one business has been has not.

3.6.1. Questions

Please write your answers on a separate piece of paper or in an exercise book.

BHS went into administration in April 2016. Though leadership was in talks with announced the closure of the business.

1. *Explain **one** factor that you think should have caused the owner of BHS to m in order for BHS to survive.*
2. *What effects would this change have on BHS? Explain at least one.*

3.6.2. Key Factors in Change

! ***Key Points Covered***

- Organisational culture
- Size of organisation
- Time/speed of c
- Managing resist

Implementing and Managing Change

Managing change is essential within a business, if it is to be carried out with the fu stakeholders and effective use of resources at the right time. Any failure in manag could result in a business delaying the desired effect or not achieving it at all.

Factors that Promote and Resist Change

Organisational Culture

Organisational culture evolves to create a series of accepted expectations. These way things are done in a company, are not necessarily written down or decided up understands them.

Origins of change: A business that is led with a top-down approach, where the C of the team follow, will often experience change from only one source: the very to involve several employees in its decision-making process, leading to more variety

Some changes are brought in as a way to challenge the culture of an organisation split into several departments that have no efficient way of communicating with o leadership may challenge this accepted norm by introducing a computerised mes

Reactions to change: Not all cultures want to change. If a business's leadership h importance of working to deadlines, for instance, and then a director tries to bring creative and methodical manner, it may be met with a negative response from ma Alternatively, the idea may be embraced but then changed over time to mimic the the organisational culture.

Size of Organisation

Organisation size can have significant effect on how change is implemented, whe whether it will be accepted by a firm's employees. Change in a large organisation point of being inefficient. Though decisions are generally fed from a select few at can slow down how employees receive this change. The structure of a business ca implemented. A flat structure may help provide empowerment and delegation wh greater supervision to take place.

Origins of change: a large business, which is organised as a tall structure, may re the top, i.e. from directors or the CEO. A small business, meanwhile, may involve decision-making process and so work as a team in order to enact a change that b the workforce.

Reactions to change: on the whole, large businesses, such as multinationals, are small businesses. This is because the more people there are to change, the harde a large company, such as a giant telecommunications provider, pockets of culture leadership then wants to push a change through, they may need to address each make decision-making extremely inefficient. A taller organisational structure, such probably not allow for great employee participation. This can make staff feel like and morale could suffer.

Not all multinationals find it impossible to make changes, though. *Glocalisation* t
business, such as McDonald's, offers elements of differentiation to particular franc
Big Mac, will appear on every menu, though restaurants can localise to a degree t
sourced from their customers' local areas or offering themed foods that celebrate
method gives empowerment to employees, improving motivation, it can be diffic

Time/speed of Change

The time required for a change can certainly have an effect on whether the chang

Origins of change: the nature of a product/service will have great impact on how
change. A manufacturer of baked beans, for instance, will move through very gra
those changes when the market is clearly open to it. A high-street fashion brand,
change very quickly in order to keep up with (or ahead of) each changing trend. S
trousers, never seem to go out of fashion, though, and so any change to these wi
long period.

Reactions to change: again, this depends on the nature of the product/service. I
Heinz released a new type of 'super-sweet baked beans', there might be mass
interest in the beginning. However, over time, consumer interest would most like
fall until the product became a failure. The baked beans market is saturated and l
by a particular customer expectation. If Heinz was to release 'super-sweet baked
beans', it would only be after a long period of market research and development.

Managing Resistance to Change

Resistance can come from many different factors, internal and external. By unders
resist change and why, business leaders can tailor changes that are most likely to
the workforce.

- **Clear objectives** – a business that has not identified clear objectives to work
clearly at all levels throughout the organisation is unlikely to achieve the desi
strategies which are formulated based on these will not be focused accordin
counterproductive.
- **Communication** – if staff are to commit to the change process they need to
it and their role. Failure to communicate this effectively can lead to staff not
process and not providing the necessary effort in the manner required.
- **Resources** – a business may have the good intentions associated with chang
resources being made available it is unlikely to happen. This could occur du
with the right skills are not available internally or externally, etc.
- **Lack of planning** – failing to plan accordingly can result in uncertainty regar
and when. The resources required are unlikely to be in place when needed.
which could cause stress for some employees who are required to complete
change but are unable to do so, either due to a lack of understanding or lack
available.
- **Staff participation** – employees may prefer to be part of the process rather
Staff may need to understand their role in the change process, but more imp
Failing to allow them to have a say even through an employee representative
- **Economic conditions** – change can be affected by the economic performan
business trades. An economic decline in any of these could lower the reven
which leads to fewer funds being available to support the ongoing change.
- **Leadership quality** – there should not be a presumption that all leaders can
situations are the same, thus different skills and expertise will be required. T
the change occurring based on the skills and experience required. Failure to
is ill-equipped to implement change successfully being placed in that positio
- **Training** – change can require new employee skills and understanding. If sta
new roles they are likely to resist any form of change or not be able to comp
manner required.
- **Employees** – if staff do not support change, it can lead to ongoing negotiatio
in trying to reach a resolution. This can delay any planned change and possib
can have a negative impact on existing business activities, but also those plan

Kotter's Eight Steps

John P Kotter, a Harvard Business School professor, believed that organisations w
fail to succeed. He identified eight steps to successful change which are to be foll

1. **Establish a sense of urgency** – analyse the market and the real competitive p base the latter on a wish, but on the reality of the situation. Use this analysis t opportunities.
2. **Build the team which will inspire change** – assemble a group of people wit who can lead the change effort and work together as a team.
3. **Create a vision** – identify the corporate vision, which will provide the focus fo for its achievement.
4. **Communicate the vision** – use as many relevant communication methods a vision. Adapt the communication to match the needs of the different receive their attention and support. Communicate how the norms and behaviour (cu change through this process and why.
5. **Empower action** – remove any barriers which can hinder change. Change th and organisational structures which could undermine the corporate vision.
6. **Create short-term wins** – set short-term aims, achieve them, recognise the a staff for their role in this.
7. **Do not let up** – be persistent. Change systems, organisational structures and the vision's achievement. Hire, promote and develop employees who can im the process with new projects and change agents; those who will inspire othe work towards it.
8. **Build change into the culture** – communicate how the new organisational c business success. Continue the development of leaders so there can be a suc

3.6.2. Questions

Please write your answers on a separate piece of paper or in an exercise book.

3. *Identify **two** factors that can lead to resistance of change.*

Plant's Plants Ltd is a seller of flowers and other horticultural items owned by split into three locations across Berkshire, Yorkshire and Norfolk. Though eac Plants Ltd, they do not speak to one another, instead communicating only wi The leaders of Plant's Plants Ltd are considering decentralising the business s its offer according to local people. The change will also bring in a communic can speak to one another in order to compare ideas and share successes/cau

4. *Explain one factor that could influence the success of the proposed change to*

3.6.3. Scenario Planning

Key Points Covered

- Identifying key risks through risk assessment
- Planning for risk

Identifying Key Risks through Risk Assessment

Scenario planning is the anticipation of different business situations, emergencies how to manage them. Businesses use risk and probability assessment techniques which scenarios most apply to them and which of these pose the biggest threats.

Natural disasters: most business owners understand that external factors pose a applies to every business. Farmers in the UK, for instance, are regularly affected b for this eventuality. Some years, a farm may have only recently recovered from a arrives to cause thousands of pounds' worth of damage. Multinational corporatio around the world are susceptible to a multitude of disasters, such as earthquakes 2016, Alberta, Canada was hit by giant wildfires that forced more than 88,000 peo that, but it suspended most of the businesses in the area, delivering a blow to the

IT systems failure: the majority of the world's businesses, small to large, are som A small-time café on your local high street, for instance, will probably use a card r Even *Big Issue* vendors can use card readers nowadays! A UK marketing firm may of payment, such as PayPal or credit/debit card. All of these systems will be supp customers save their money.

IT systems make many day-to-day processes quick and painless for the business c were to fall apart, however, there would be trouble. Businesses, therefore, need b example, can still take physical money, as can the *Big Issue* vendor. The marketing with this failure as many of its customers will probably be based abroad.

When it comes to IT, system failure is not the only issue, but security breaches, to was hacked via a third-party application in 2014, losing nearly seven million usern The company was able to stabilise its systems and, in the end, return security to it the real dangers for all businesses that deal with IT on a daily basis.

Loss of key staff: no business wants to lose its key staff. A key member of staff c managing director to a particular marketing executive who drove sales to levels p of staff might even be that IT manager who knows every business process but kee

A business needs to be ready for the eventuality of losing a key staff member. In most key staff member, Steve Jobs, to cancer. Steve Jobs led Apple, Inc. to some products of all time, from the iPod and iMac to the MacBook, iPhone and iPad. W different company, though one that would have had to prepare for if such an eve leader ever came true.

Planning for Risk Mitigation

There are four main areas when it comes to risk mitigation:

- **Risk acceptance:** this involves a business, usually a small one, accepting that risk is greater than the cost of the impact brought on by the risk.
- **Risk avoidance:** this is when a business decides to move away from a risk, p may remove its operations from one part of the world because of risk brough firm may stop producing a particular product because it is causing friction in
- **Risk limitation:** when a business accepts that the risk exists and then, rather mitigate the effects of this risk. An example might be the IT security of a bus to lessen the effects of a computer virus.
- **Risk transference:** this involves a business handing its risk to someone else, part of its operations.

All of these methods of risk mitigation come into play when we talk about *busine succession planning*.

Business Continuity

An important element of risk mitigation, business continuity ensures that a firm re
soon as possible following any disaster. A business continuity plan can help with t

Example of Business Continuity Plan for a Computer Manufactur	
Assess damage caused by impact	Systems are temporarily shut down so that the analysis t have been affected. Other teams work offline in the mea
Agree a strategy	Company has various strategies already prepared in orde types. Leadership discusses with key IT personnel in ord for the situation.
Preparation	Employees are notified of the situation and delivered an to the threat as efficiently as possible. Any equipment o team is also notified so that they can communicate with

Succession Planning

This element of risk mitigation enables a company to prepare itself should it lose a
help to think of this in terms of the monarchy: Queen Elizabeth II has reigned ove
Charles is next in line to the throne and so has been in preparation for years. This
firm with a CEO should have a clear line of succession; this may include an already
action as to how the company finds such a successor. A succession plan can help

Example of Succession Plan for a Perfume Business in Event	
Job description	The business must already fully understand the role and therefore, what would be expected of the successor. Thi change, too, so it is important for the CEO and firm's lea
Find successor	Once the firm understands exactly what would be expec hunt for the successor, i.e. the person who would best fi company or external). This should begin as soon as pos of a successor now or years in the future.
Decision and training	The business should have more than one successor lined way, if one option is no longer available, there will still b choose from. The business can prepare each potential s and work shadowing, among other methods.
Inform	Everyone will eventually find out that the business has a beginning stages, it is most important to inform the com These people can then feed any essential information do
Preparation	Once the key staff are aware of the change, it is then im programmes necessary. It is possible, for example, that successor take on particular tasks of the previous CEO. T strategies that everyone must follow.

3.6.3. Questions

Please write your answers on a separate piece of paper or in an exercise book.

5. *Explain one reason why scenario planning is essential to a business.*

6. *Dyson is a designer and manufacturer of vacuums and hand driers, among m The company's production factories are based in Malaysia. Complete a busin its Malaysian factories were to become unusable.*

Business continuity plan for Dyson in event of Malaysian factories
1.
2.
3.
4.

3.6. Answers

1. *Answers will be unique to each student. Examples include (but not limited to):*
   - ***Poor business performance:*** *BHS must have been performing poorly fo administration two years later. Students might mention stronger marke brand reputation as changes. Perhaps customers were no longer interest (i.e. they could get the same offer, or better, in various other places). If th should have invested time and money into finding out what consumers w*
   - ***The market (PESTLE):*** *external factors, such as new entrants (e.g. ASOS advances (e.g. online shopping), competed BHS out of the market. Rather the same way, BHS could have considered all aspects of the market and e relevant in the eyes of the public.*

2. Again, individual answers. These should include some reference to at least (e.g. loss of competitive advantage through market changes), productivity, f overall performance could be both cause and consequence of low productiv performance) and stakeholders (any negative changes would have conseque particularly in this case employees, through job loss/insecurity).

3. *Factors which can lead to resistance of change include clarity of objectives, qua participation, staff resistance, quality of leaders, depth of planning, resources a structure and economic conditions.*

4. *The change proposed for Plant's Plants Ltd could be influenced by:*
   - ***Organisational culture:*** *though each location feeds directly back to hea certain ownership over the way they do things. By communicating with feel pressured to do things differently, or even compete with their peers i*
   - ***Size of organisation:*** *the organisation is still small enough to control at decentralisation would make any future changes more time-consuming t*
   - ***Resistance to change:*** *staff need to understand the reasoning for the ch clear objectives. Decentralisation is empowering to a point, though staff powerless than empowered if this change is being forced upon them. Sta in particular processes in order to take responsibility for their locations. these changes if they are not actually in line with demands or expectatio*

5. *Scenario planning is essential to business because it allows firms to prepare fo potentially damaging events. Planning can involve anything from moving bus production of a particular item to doing nothing at all. Each plan is suited to could arise.*

6. *Example business continuity plan might be:*
   1. *Assess why the Malaysian factories can no longer be used. If it is equipme potentially be fixed. If it is more related to external factors, e.g. political, move its operations elsewhere.*
   2. *Dyson should have various strategies ready in the event of normal busine strategy being how to manage production without the Malaysian factori a strategy, such as moving production to another outsource firm in the m for a new location. If this strategy is to succeed, Dyson should be in comm businesses should an issue like this ever arise.*
   3. *Employees are split into teams and trained on how to use the equipment location is outside Malaysia, Dyson may need to recruit new employees. prepared to efficiently find new workers and train them in what is requir*
   4. *Leadership and press team are briefed on how to respond to requests for its production to Malaysia was already a big news story in 2011 because redundant. This news story, if handled incorrectly, could also negatively reputation.*