

STUDENT BOOK ANSWERS

UNIT 1

MARKETING AND PEOPLE

1 THE MARKET

ACTIVITY 1

CASE STUDY: US DRYBAR

1. Using this case as an example, explain what is meant by a niche market.

A niche market is a small market segment – a segment that has sometimes gone ‘untouched’ by larger businesses. Niche marketing is the complete opposite of mass marketing. It involves selling to a small customer group, sometimes with specific needs. Small firms can often survive by supplying niche markets. In this case, Drybar targets a niche market. Drybar specialises in the provision of affordable, high-quality blowouts. This is when a client’s hair is washed and blow-dried into style without being cut or coloured. Drybar is set up like a bar where clients can relax, watch a film and get a blowout. This service is different from the majority of hair salons in the market.

2. Explain one possible disadvantage to a business like Drybar of targeting a niche market.

Obviously if a market is very small the potential for sales is limited. There may also be limited scope for diversification and new product development. Consequently, firms cannot spread their risk. Small firms operating in a niche market may also be vulnerable. If a firm successfully exploits a niche market it can still attract competition. Niche markets, by their nature, are very small and unable to support more than two or more competing firms. As a result, if a large firm decides to enter a niche market they may find it easy to overrun a smaller rival. If they lose a grip in their chosen market, they are likely to collapse because they do not have other products or markets as a back-up. This could happen with Drybar if other providers copy their idea.

ACTIVITY 2

CASE STUDY: ONLINE GROCERY SHOPPING

1. Explain why online grocery retailing is likely to grow in the future.

In many countries, online grocery retailing is currently trailing behind other forms of online retailing. This is the case in Australia. However, reports suggest that online grocery sales in Australia may rise from AUD 2600 million in 2015 to AUD 5800 million by 2020. A recent survey showed that 39 per cent of Australian shoppers may use online grocery shopping in the near future. This may be because of busier lifestyles and the further integration of mobile technology into our daily lives. People are increasingly becoming ‘on-the-go’ consumers. Online shopping is convenient and can help busy consumers save time.

2. Assess the benefits and drawbacks to supermarkets of online retailing.

Supermarkets are keen for online grocery sales to grow. Many have invested in the click & collect concept which is being introduced around the world. Major retailers in Australia, including Coles and Woolworths, are investing heavily to roll out the service to the majority of their stores as well as remote locations, such as railway stations. There are a number of benefits to online selling. Supermarkets can market their goods to people who prefer to shop from home. From a marketing perspective, it is easier to gather personal information online from customers so that they can be targeted with other products and offers in the future. Marketing costs will also be lower. For example, it is much cheaper to send a marketing message by email to 1000 customers than it is to send 1000 newsletters by post. Supermarkets with an online facility are open 24/7. There are not many stores that can match this level of service – although some supermarkets are open 24 hours a day, 5 or 6 days a week. Finally, it may be possible to reduce some selling costs such as sales staff. Fewer people may be needed in stores if people are shopping online.

However, there may be some drawbacks. There are likely to be some extra costs, both initially and ongoing. Supermarkets will have to invest heavily in IT and delivery fleets, for example. Orders will have to be 'picked', which is labour intensive, and systems will have to be developed to deal with returns, complaints and delivery routes. Overall though, it is likely that the benefits will outweigh the costs and any supermarket that fails to offer online services is likely to lose a competitive edge.

EXAM PRACTICE

GLOBAL EV MARKET

(a) Define market share. (2 marks)

Market share is the proportion of a market that a particular business or product enjoys. In this case, Figure 3 shows that global sales of EVs in 2016 were 774 000 units. This was 42 per cent higher than for 2015 but only 0.86 per cent of the total market for vehicles. This is a very small market share. However, in 2010 market share was only 0.01 per cent.

(b) Explain one reason why the global car market is likely to grow in the next 5 years. (4 marks)

Most markets tend to grow over time. The global car market is almost certainly a market that is likely to grow in the next 5 years. The main reason is because of the growing demand for cars that is likely to come from emerging markets. These include the BRIC countries and other developing nations such as Mexico, Thailand and Indonesia. Car ownership in these countries is probably very low compared with most developed countries. Consequently, there is a lot of scope for car sales to people in these countries in the near future. Disposable incomes in these emerging markets are beginning to rise and many people will want to buy a car.

(c) Discuss how a car manufacturer might adapt to changes in the market. (8 marks)

In competitive markets like the global car market, firms are under pressure to meet ever-changing customer needs. Firms need to be prepared for change. One way is to develop a culture of flexibility in an organisation. A business will need flexible working practices, flexible machinery, flexible pricing and flexible staff. This might mean that staff have to be trained in a variety of skills and be prepared to change the tasks they undertake in the workplace. This might help firms to serve customers more effectively when changes occur.

Businesses must keep in touch with developments in the market. One way to do this is to undertake regular market research. Research might be aimed at current customers or potential customers in the market. Firms need to be aware of any changes in customer needs or tastes.

Those firms that invest in new product development are likely to survive for longer in the market. Although expenditure on research and development is expensive, a failure to innovate could be costly. A unique new version of a product or a brand new model could rejuvenate sales and help win a larger share of the market. In the car industry, firms spend very large sums of money in product development. BMW has enjoyed a larger slice of the small car market by extending the range of its Mini models. Investment might also be needed in training and flexible machinery. Finally, a car manufacturer might adapt by finding a niche in the market. A niche strategy is appropriate if groups of loyal customers can be served profitably. For example, it could be argued that Ferrari has profited from serving the high-end luxury car niche market. At the moment, the EV market may be described as niche. However, many car producers are aware that the sale of EVs is likely to be important and therefore the market may not remain a niche.

If firms cannot adapt quickly to the changing needs of customers, they will lose out to rivals that do adapt. There are different ways of doing this in the car market and each producer is likely to adapt in a way which exploits their strengths.

(d) Assess the factors that might affect the growth of the EV market in the future. (10 marks)

One reason why EVs were developed was to serve customers who were increasingly concerned about the environment. It is often argued that emissions from cars make a big contribution to the 'greenhouse effect' and global warming. Also, governments around the world have signed agreements to reduce carbon emissions and they are keen for growth in the hybrid car market. Indeed, in some countries, financial incentives have been offered to consumers opting for EVs. The increases in sales of these cars between 2010 and 2017 is sharp and illustrated in Figure 3.

One of the barriers to using EVs was, and still maybe, uncertainty about recharging facilities. People are aware of the locations of petrol stations and it is rare to run out of petrol on a busy motorway. In contrast, a lot people do not know where batteries for EVs can be recharged once embarking on a long journey. However, locations for charging have increased at least ten-fold and the number of available grid charged models has increased from 70 to 130 since 2013. Also, the cost of batteries has fallen by 50 per cent in recent years and renewable sources are now roughly the same cost as fossil fuels in electricity generation. This bodes well for the future of EVs.

Looking ahead, there is certainly a lot of potential for growth in EV sales since in 2016 it only had a 0.86 per cent share of the global market. However, whether the market will grow depends on future oil prices, continued pressure to reduce emissions, the effectiveness of marketing strategies used by car producers and the development of recharging facilities. To conclude, the volumes are still small at the moment, but with the government incentive schemes supporting the market and car makers unveiling an even wider range of models, the direction of travel is increasingly clear.

2 MARKET RESEARCH

ACTIVITY 1

CASE STUDY: ONLINE SURVEYS

1. Give one reason why it might be important to find out what people think of a business website.

A badly-designed website could discourage online shoppers from making a purchase. When searching for products online, people like to look at attractive websites and be able to navigate them easily. If a website is unattractive, does not contain the right sort of information or is too difficult to navigate, online shoppers can easily 'click' to another. Even for businesses that do not sell their goods online, an effective website is still important. A company's website is likely to say something about the image of that company, so a business will want to project a positive image through its website.

2. Explain whether the online survey would benefit a company selling to: (a) customers in isolated areas (b) less-developed countries, such as Ethiopia, Bhutan and Haiti.

(a) An online survey would be of benefit to a company selling to customers in isolated areas. It would allow a company to gather information cheaply – for example, without incurring the cost of travelling to such customers. This would be particularly the case if a face-to-face interview were the alternative.

(b) An online survey may not be of benefit to a company selling to customers in undeveloped countries such as Ethiopia, Bhutan and Haiti. This is because many people in these countries do not have access to computers where they can get an internet connection. However, in Bhutan, growth in internet access is relatively fast for a less-developed country. In Haiti, mobile internet use is rapidly rising due to investment from multinational communications companies. Given that those subscribing in Bhutan and Haiti are more likely to be in the higher-earning sectors of the population, it might be worthwhile using online surveys.

3. Discuss the advantages and disadvantages of online surveys.

The main advantage of online surveys is that they can be completed and processed quickly: the respondent keys in the data, which is then fed straight back for immediate analysis. Survey costs are lower because there is no need for printing, postage and keying in. Online surveys are often fun to complete because they may be interactive. They can also be accessed 24/7 and completed at the convenience of the respondent. In addition, online surveys make it easy to give feedback to the respondents, as results can be emailed to them.

However, there are disadvantages. With an online survey, the sample of respondents may not be representative. This is because online surveys are only presented to internet users. The views of others may not be taken into account, even though they may be potential customers.

ACTIVITY 2

CASE STUDY: TEKKONG AND VIRTUAL REALITY

1. Define desk research.

Desk research or secondary research involves the collection of secondary data. This is information that already exists in some form. It can be internal data, from records within the business, or external data, from sources outside the business, such as reports, newspapers or company websites.

2. Figure 2 is an example of quantitative data.

(a) What does this mean?

Quantitative data is information that is expressed in numbers. The data can be measured and presented in graphs, tables and charts. Figure 2 shows quantitative data presented in two pie charts. It shows the market sizes for four different types of wearable technology (fitness trackers, smartwatches, wearable cameras and virtual reality headsets) in 2016 and 2020. The data is expressed in numbers. For example, it shows that in 2016 smartwatches were the most popular type of wearable technology with a market share valued at US\$6300 million. However, in 2020 the market leader was virtual reality headsets with an expected market share valued at US\$4500 million.

(b) Describe one advantage of gathering quantitative data.

One of the main advantages of quantitative data is that it is regarded as being open to less interpretation than qualitative data. This means that it is easier for a range of different analysts to draw common conclusions from the data. Time is not likely to be wasted discussing whether the data means one thing or another.

3. Based on the data in Figure 2, discuss one possible reason why TekKong decided to develop a VR headset.

In 2016, global sales of VR headsets were US\$1700 million. Less money was spent on VR headsets than any of the other three items of wearable technology. However, in 2020 sales of VR headsets are expected to climb to US\$14 500 million. This is a huge increase and means that VR headsets will dominate the market for wearable technology by 2020. Consequently, TekKong believed that this market would provide a more profitable opportunity for a new product. This is presumably why TekKong decided to develop their own VR headset for the market, rather than other types of wearable technology.

ACTIVITY 3

CASE STUDY: BASEL INTERNATIONAL

1. (a) Define random sampling.

Random sampling is where each member of a group or population has an equal chance of being selected in a survey. The sample is selected at random.

(b) Why are samples used in market research?

Ideally, when carrying out a survey, information could be gathered from every single member in the target population. The target population includes all those people whose views a business wants to explore. The target population may be individual consumers, households or other businesses, for example. However, this may take too long and cost too much money. To overcome this problem, businesses collect information from a sample of people in the population. A sample is a much smaller group. However, it is important that their behaviour and views are representative of all those in the population.

(c) Describe one disadvantage of using random sampling.

A random sample, particularly if it is too small, may not be representative of the whole population. This could be a serious problem for a company like Basel International. This is because any conclusions and decisions based on the research results might be inaccurate. This might mean that the business makes errors in its product development, for example.

2. On behalf of Basel International, information was gathered from 20 000 females in 20 different countries. Suggest why it interviewed (a) females only; (b) respondents in 20 different countries rather than one country only and (c) 20 000 people rather than 1000 or 1 million.

(a) Females alone were interviewed because females were the target market in this case. Basel International felt that the business needed to develop more products for females because its current product portfolio was heavily biased towards males.

(b) Respondents from 20 different countries were interviewed rather than one as this would have given a variety of different data about female health. It is possible that health issues vary between different countries. So, obtaining information from different countries may allow Basel International to develop products to meet a variety of needs, or different products for different needs. This would be important to Basel International because it is a multinational company.

(c) The survey might have interviewed 20 000 people rather than 1000 in order to gather a larger amount of information about female health, particularly since the company is aiming to develop products for the global market. Also, by using a larger sample, it is likely to be more representative and therefore the information gathered will be more accurate. The survey probably chose a sample size of 20 000 respondents rather than 1 million in order to limit the costs of the research. Clearly a market research agency would charge Basel International a higher fee if they had to interview more people.

3. (a) What is the difference between open and closed questions in a survey?

Closed questions allow respondents a limited range of responses. An example would be 'How many days work have you missed through illness this year?' The answers to closed questions are easier to analyse and represent numerically. Open questions let people say whatever they want. They do not have to choose from a list of responses. Open questions are best used if there are a large number of possible responses. An example would be 'What type of products would you like to see Basel International develop in the future?'

(b) Describe one advantage to Basel International of using open questions.

The use of open questions gives respondents the opportunity to provide individual answers. This means that Basel International can gather a very wide range of information. The number and type of responses are unlimited. There is also the chance that respondents reveal valuable information that the business had never considered before. This might result in some unexpected and profitable ideas for product development.

EXAM PRACTICE

MARKET RESEARCH ON 'CLICK & COLLECT' ORDERS

(a) Define primary research. (2 marks)

Primary research, or field research, is used to gather information that does not already exist. It involves collecting new information from new sources. Primary data is usually gathered by asking questions or monitoring people's behaviour. Primary research provides original data, and the information gathered can be tailored to the needs of the business.

(b) Explain one benefit of using qualitative market research. (4 marks)

Qualitative research involves the collection of data about attitudes, beliefs and intentions. Focus groups and interviews are common methods used to collect qualitative data. Information gathered using qualitative research may be richer and more diverse. This is because it gives respondents opportunities to say anything they wish. A business might find out information that they were not really expecting.

(c) Explain one way in which the data in the Mintel report might be used by retailers. (4 marks)

Retailers might use the information in the Mintel report in a number of ways. The report might influence their decision making. For example, the report says that 60 per cent of UK consumers only use click & collect for smaller items that are easy to carry, but 53 per cent say they would like drive-through points that offer click & collect for a number of retailers, which suggests opportunities to extend click & collect to heavier and bulkier items. This might encourage retailers to set up joint ventures to organise drive-through points so that customers could pick up larger items.

The report also states that fifty per cent of consumers say the hassle of returning goods through the post is one of the main barriers to buying clothes online. Some 31 per cent of consumers prefer to be able to return their online order to an actual store, and 23 per cent of UK consumers say that an option to deliver to a store to try on before purchasing would encourage them to buy from one online retailer over another. This information may prompt online retailers to improve their returns policy and provide facilities for online shoppers to try on clothes.

The way the data is used may depend on the types of goods a retailer is selling. For example, the report says that click & collect orders made up 15 per cent of all internet retail sales of goods in 2014. However, the collection rate is much higher for non-grocery orders than for groceries. This might mean that grocery retailers (for example, supermarkets) decide that click & collect is not yet a viable option for them. Finally, different retailers may interpret the information in different ways. For example, in 2015 an estimated 17 per cent of all internet retail sales (or 2.2 per cent of all retail sales) would be collected by customers. Some retailers may think this number is small and insignificant, while others may think the opposite.

(d) Assess the usefulness of market research data, like the above information, to retailers. (12 marks)

Businesses spend money on market research because it helps to reduce the risk of failure. Products that are well researched are more likely to be successful. Market research data can help to quantify the likely demand for a product and, most important of all, provide an insight into consumer behaviour. Retailers will be more successful if they can satisfy the needs and wants of consumers. Consequently, it is important that they try to identify these needs and wants as clearly as possible. This inevitably means they need to communicate with customers by using market research. A retailer could opt out of market research and just copy the actions of rivals. However, this might be too risky as they will always be 'one step behind'. They would lose market share to any rivals that satisfied customer needs ahead of them.

The data above is collected by Mintel. Mintel is a world leader and specialist in market research. The data it collects is likely to be of good quality. For example, the report says that 35 per cent of UK consumers had used click & collect services in the previous year and 64 per cent said they shop online more now because more retailers provide click & collect services. Furthermore, 58 per cent said that click & collect encourages them to visit stores more frequently. For retailers this is useful information. It could be argued that if more than a third of people have used click & collect services in the previous year, retailers that fail to set up systems to offer this service will lose out. This is valuable information for retailers.

However, market research can be expensive. If a firm carries out its own research, it will need to use valuable resources. There will be an opportunity cost to consider. A retailer could purchase market research reports from agencies such as Mintel. However, these can also be expensive, with Mintel charging up to £2,500 for a single report. Also, although carrying out market research can reduce the risk of products failing in the market, it is not entirely reliable. Market research data may be biased. For example, if the sample used by a business is not representative, any conclusions drawn on the basis of the sample will be inaccurate. Additionally, human behaviour is unpredictable. Although people may indicate their intentions in a questionnaire, what they do in reality might be quite different. People might change their minds or misunderstand the question. They might also give answers that they think the interviewers want to hear. Finally, a business might use poor research technique. If questionnaires are poorly designed or interviewers have not been trained, the quality of the research might be poor.

To conclude, to meet customer needs effectively, a retailer, like any other business, will have to obtain information from them. Carrying out market research will improve the chances of business success so it is likely that data (for example, as contained in the Mintel report) will be very useful to retailers.

3 MARKET POSITIONING

ACTIVITY 1

CASE STUDY: SUN PHARMACEUTICAL INDUSTRIES

1. Comment on the pattern of R&D expenditure shown in Figure 2.

Figure 2 shows that the amount of money spent by Sun Pharmaceutical Industries has risen steadily between 2011 and 2016. It has increased from Rs 3313 million to Rs 23 025 million. This is an increase of almost 600 per cent. This is a very significant increase over the time period.

2. Explain one benefit to Sun Pharmaceuticals of being product orientated.

One benefit of being product orientated is that Sun Pharmaceutical Industries can concentrate solely on the development of new, high-quality drugs and medicines. It does not have to 'waste' resources on expensive market research, promotion and advertising. For example, once a new medicine has been developed, perfected and tested, Sun Pharmaceutical Industries knows that the market already exists. Also, since the product will be new on to the market, sales are almost guaranteed. Sun Pharmaceuticals can also obtain patents on new products, which prevent other companies from copying their new drugs. This means they will have no competition for a period of time.

3. To what extent is Sun Pharmaceuticals product oriented?

Some businesses are product orientated. This means that they are most concerned about the quality of their products. Their efforts concentrate on the design and manufacture of the product itself. Sun Pharmaceuticals is an example of a product-orientated business. This is because it focuses most of its attention on the development of new drugs and medicines. The need for the products Sun Pharmaceuticals produces already exists. The company does not have to use resources to survey the market. The amount of money Sun Pharmaceuticals spends on scientific R&D is evidence of its commitment to the development of products. In 2016 it spent Rs 23 025 million on R&D. More significantly perhaps is the scale of the increase in R&D expenditure between 2011 and 2016. It has risen by almost 600 per cent.

ACTIVITY 2

CASE STUDY: ATHLETIC FOOTWEAR

Figure 4 shows a perceptual map for athletic footwear.

1. How might a Taiwanese sports shoe manufacturer use the map in Figure 4?

Perceptual maps can be used to identify gaps in the market. If there was an area on the map where a business was not positioned, it could be argued that a new entrant (competitor) could come in and fill the gap. The perceptual map in Figure 4 shows quite a big blank area in the top-right quadrant (expensive and fashionable). Only one brand, Skechers, occupies this area. If the Taiwanese company can develop some footwear that is fashionable and relatively expensive, this might provide the company with an opportunity. However, the fact that there is only one brand currently occupying this area might suggest that such styles are not in great demand.

The bottom-right quadrant represents fashionable and cheap footwear. This might be very attractive for consumers but perhaps not workable for a business. This is because it might not be possible to produce highly fashionable and inexpensive products. However, there are two brands positioned in this area so there might be an opportunity for the Taiwanese company.

The Taiwanese company might decide to avoid the top-left quadrant where there appears to be a lot of competition, with six brands occupying the position. The bottom-left quadrant, however, might

provide opportunities for low-cost performance shoes. If it were possible to manufacture such a shoe, this might be attractive to the Taiwanese company. However, the company would have to consider whether this position would fit into its current image and strategy. If not, it might opt for another position and stand up to the competition.

2. Describe one drawback of the Taiwanese sports shoe manufacturer of using the perceptual map in Figure 4.

The use of market maps may have some limitations. For example, perceptual maps are two-dimensional. This means that only a restricted number of qualities can be analysed on the same map. In this case, performance, fashionableness and price are the only qualities analysed. Also, the information needed to plot the maps may be expensive to obtain, needing the use of primary market research. The map in Figure 4 may be based on one person's perception. A business would be unwise to draw conclusions from such a limited number of market perceptions. Gathering data from, say, 1000 consumers would be time-consuming and expensive. Finally, even if the Taiwanese company did gather data, there may be a difference between consumers' perceptions of the benefits and the actual benefits that are offered by the footwear manufacturers.

3. Assess the position of The North Face brand compared to that of Adidas using the perceptual map in Figure 4.

The North Face brand is positioned right at the top-left corner of the map. It is perceived to be expensive and high-performing. In comparison Adidas is positioned right at the centre of the map. It is mid-priced and perceived to be neither particularly fashionable nor particularly well-performing. It might be described as a 'an average reasonably priced product' which may appeal to many consumers in the market.

ACTIVITY 3

CASE STUDY: EMIRATES

1. Describe the different customer groups targeted by Emirates in this example.

Most airlines target customers with the methods used by Emirates. Using this approach allows Emirates to cater for the needs of three different customer groups on its planes. In this example, a flight from Dubai to Sydney will cost AED 5205 travelling on economy class. Most people when they fly travel economy class. This will be the largest customer group. Emirates also targets business customers with its added benefits such as flat-bed seats, personal mini-bars and free Wi-Fi. This is priced at AED 15 515. The final group targeted by Emirates is very wealthy travellers. The first-class service is offered to this customer group at a price of AED 20 165 (nearly four times more expensive than economy class). First class includes a private cabin, as shown in the photograph, and choice from an à la carte dining menu.

2. Discuss how Emirates might benefit from this method of market segmentation.

By targeting different customer groups Emirates will be able to serve a wider range of customers. The three different services also meet the specific needs of three different customer groups. Using this approach means that Emirates can generate more revenue by charging premium prices for business class and first class. If Emirates only offered economy class, it would miss out on the opportunity to charge higher prices to those who are willing to pay for a higher-quality service on board a flight. The additional AED 14 960 generated from selling a first-class ticket instead of an economy ticket is significant.

Emirates might also gain a competitive edge by serving three different market segments. If its rivals cannot match Emirates service they are likely to lose customers. The luxury first-class service might also help to enhance the image of Emirates, which might help to increase sales.

However, if Emirates cannot sell enough first-class and business-class tickets, the space used to provide these services might be wasted. It may have been better to have more economy seats. Emirates would have to analyse the number of tickets sold of first- and business-class accommodation to ensure that it was 'paying off'.

EXAM PRACTICE

HARLEY DAVIDSON

(a) (i) Define market positioning. (2 marks)

Market positioning is concerned with the perceptions consumers have about products. To simplify the choice from a vast array of products, consumers categorise them according to a range of factors. In the case of motorcycles, consumers might include the quality of design, quality of customer service, the reliability of the bikes, the level of customisation and value for money when categorising bikes. It is the categories into which consumers place products that define their 'position'.

(ii) Explain why Harley-Davidson felt the need to reposition its brand. (4 marks)

The Harley-Davidson brand had a distinctive image. It was associated with a powerful, brave and rebellious rider, and an adventurous lifestyle that was attractive to a significant number of males aged between 25 and 35. However, eventually strong competition emerged in the market, particularly from Japan, and Harley-Davidson nearly went bankrupt on more than one occasion. The company faced a number of problems. For example, rival bikes were often more reliable than Harley-Davidsons, the Harley-Davidson brand became associated with biker gangs, such as the Hells Angels, and Harley-Davidsons were eventually perceived as old-fashioned. To resolve these problems the company attempted to reposition the Harley-Davidson. The motorcycles failed to meet the quality standards that the customers demanded. The products were also not appealing to the younger market segments. As a result, Harley-Davidson has addressed its problems and repositioned the brand at the premium end of the market.

(b) Define psychographic segmentation. Use the example in this case to support your answer. (2 marks)

One approach to grouping customers is to use psychographic segmentation. This involves grouping customers according to their attitudes, opinions and lifestyles. In this case, Harley-Davidson uses psychographic segmentation to meet the changing needs of consumers. This is mainly because the motorcycle is a lifestyle brand. Customers choose a Harley-Davidson over rival bikes because they love to buy and ride premium motorcycles. It could be argued that many Harley-Davidson owners belong to a specific culture that 'loves' the brand and enjoys being part of a group that own Harley-Davidson motorcycles.

(c) Explain one way in which Harley-Davidson has developed a competitive advantage. (4 marks)

A business is likely to be more successful if it can gain a competitive advantage in the market. Competitive advantage is a set of unique features of a company and its products that are perceived by customers as significant and superior to the competition. In this case, Harley-Davidson has developed an advantage by offering its customers a wide range of different products and a high level of customisation from the handle, the stand to the overall looks. This also includes the motorcycle accessories riders can wear.

(d) Assess the importance to Harley-Davidson of product differentiation in this case. (10 marks)

Product differentiation is used by businesses to gain a competitive edge over their rivals. In highly competitive markets, where lots of firms produce similar products, firms will try to make their product unique in some way so that it stands out from the pack. This involves supplying goods and services that have different features or physical qualities. The differences in products may be real. This means

that products might look different, have different technical specifications or have different capabilities or performance levels. In this case, Harley-Davidson has differentiated its products by offering its customers a wide range of different products and a high level of customisation from the handle, the stand to the overall looks. This also includes the motorcycle accessories riders can wear. The company has also developed a specific culture for Harley-Davidson bikers through its Harley Owners Group (HOG). This owners-club holds regular meetings where Harley owners from different regions can get together and enjoy a lifestyle of passionate bikers. Rival brands may not offer their customers this opportunity.

The company repositioned itself at the premium end of the market to help the differentiation process. It resolved the technical issues, improved reliability and quality and focused on its strengths, such as providing customers with a wide range of exciting bike designs. Harley-Davidson decided to channel resources from marketing into improving the quality and reliability of its products. It is now enjoying growth and looking to enter more foreign and emerging markets. Most would agree that people who ride bikes see Harley-Davidson as something quite different from another manufacturer's bike. It is probably a very effectively differentiated product. This is very important and has contributed significantly to the company's revival.

4 DEMAND

ACTIVITY 1

CASE STUDY: DIESEL PRICES AND ELECTRICALLY POWERED VEHICLES

1. Calculate the percentage change in the UAE diesel price between May 2016 and May 2017.

The percentage change is given by:

$$\text{AED } 1.97 - \text{AED } 1.6 = 0.37$$

$$0.37 \div 1.6 = 0.231$$

$$0.231 \times 100 = \mathbf{23.1\%}$$

2. What is meant by a complementary good?

Some goods are purchased together. In this example, cars and diesel are purchased together. Once a consumer has bought a diesel car, it is necessary to also buy diesel. In this case, diesel and cars are complementary goods.

3. Explain how the pattern of prices in Figure 3 might affect the demand for (a) diesel-powered cars and (b) public transport in the UAE.

(a) The pattern in Figure 3 shows that diesel prices have been rising since May 2016. They have risen by 23.1 per cent from AED 1.6 in May 2016 to AED 1.97 in May 2017. This is a significant increase and could cause a decrease in the demand for diesel-powered cars since it will be more expensive to run them. When the price of a good rises, the quantity demanded for it is likely to fall, along with the quantity demanded for any complementary goods. However, the overall impact in this case might be more complex. There could be a decrease in the quantity demanded for cars that consume larger quantities of fuel. Examples might include sports cars and four-wheel-drive vehicles. If this happened there might also be an increase in demand for smaller, more fuel-efficient cars. There might also be an increase in demand for petrol cars, which are good substitutes. The overall impact might also depend on whether the diesel price increases are sustained (stable) and whether they continue to rise further.

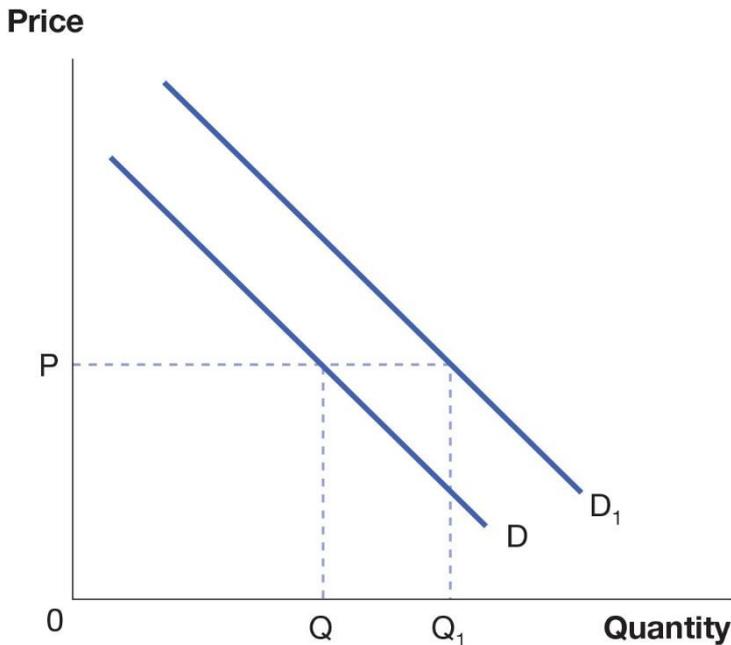
(b) The demand for public transport might be affected by rising diesel prices. Public transport may be a substitute in some circumstances for car transport. For example, a person may have the choice between driving to work or using the bus. With higher diesel prices, such people might favour public transport. As a result, the demand for public transport may rise.

EXAM PRACTICE

GLOBAL CARE GROUP

(a) Draw a diagram showing the likely effect on the demand for Global Care Group's services in the future. (4 marks)

The demand for Global Care Groups services is likely to increase in the future since the number of people in elderly age groups is predicted to rise significantly. For example, Figure 5 shows that the proportion of people in Australia aged over 65 is expected to grow from about 8 per cent in 1970 to around 17 per cent in 2050. As a result, the demand curve will shift from D to D₁ as shown in the diagram.



(b) Discuss how the information shown in Figures 4 and 5 might affect demand patterns in Australia. (8 marks)

Figure 4 shows that the population in key Australian cities is predicted to grow significantly in the future. Perth will see the largest population growth of around 143.9 per cent, from 1.9 million to 4.6 million. However, populations are expected to grow significantly in the other cities – by 64.2 per cent in Sydney, 80 per cent in Melbourne, 91.5 per cent in Brisbane and 40.8 per cent in Adelaide.

This increase could have a big impact on demand in Australia. As the size of the population increases, demand for most goods and services will rise. There will be more demand for essential goods and services like food, housing, transport, financial and personal services, education and healthcare. There is also likely to be an increase in demand for non-essential goods and services, such as tablets, holidays, taxis, restaurants, hotels and a wide range of luxury goods.

Businesses might be particularly interested in the trends predicted in Figure 4. The population growth in the five major cities is not the same. It is expected to be significantly higher in Perth. As a result, businesses in Australia might target those cities with the greatest population growth potential when planning their expansion and investment programmes.

Figure 5 shows that the Australian population is getting older. The proportion of people in Australia aged over 65 is expected to grow from about 8 per cent in 1970 to around 17 per cent in 2050. This is a significant increase and consequently, there will be an increase in the demand in general for the goods and services that this age group favours. For example, Global Care Group is likely to see an increase in demand for its care homes. Indeed, such an increase in demand is being recognised since the company is already expanding. For example, recently, Global Care Group bought some land next to the Northam Country Club in Northam. This will be used to create a new retirement village for the elderly, called Northam Country Estate. Houses in the village will be custom built and residents will have access to the country club facilities, a shared vegetable garden, golf course and many interactive activities. The idea is that residents will live independently but share a similar lifestyle with similar people.

(c) Assess the impact that external factors might have on the demand for services supplied by companies like Global Care Group. (10 marks)

The demand for many goods and services can be influenced by changes in external factors. External factors are those that are beyond the control of businesses. Because they cannot be controlled, the

impact of such changes could be quite influential. To begin with, Global Care Group and similar companies will benefit from the growth in the older population in Australia. Such companies provide care homes for the elderly and demand looks set to increase up to 2050 as the number of 60–84-year-olds grows. This will help Global Care Group and other care home providers to increase revenue and profit. The growth will also encourage investment in the industry. So, there will be an increase in demand for construction companies to build new homes and similar increases for furniture and other related goods. Global Care Group has already started to expand. It recently bought some land next to the Northam Country Club in Northam. This will be used to create a new retirement village for the elderly, called Northam Country Estate

However, in this case, companies like Global Care Group might be worried about the potential threat from new competitors entering the market. The information in Figure 5 suggests that demand for care home services is going to rise. As a result, some new competitors will be attracted into the market. A company like Global Care Group might be negatively affected if these new entrants are more efficient, cheaper and offer better value for money than Global Care Group. However, as Global Care Group is a not-for-profit organisation, its position may not be under as much threat as those businesses that pursue profit.

In recent years, many governments around the world have cut government spending. As a result, the government might cut the number of care home places provided by the public sector. If this were to happen, private sector providers like Global Care Group are likely to benefit.

Finally, there could be a change in social trends in the future. For example, there may be a trend for families to provide their own care for elderly parents at home. If this were to happen, demand for the services provided by Global Care Group might fall. In contrast, the trend might be the complete opposite. People might be keener to find comfortable accommodation with professional and specialised services for their parents. Such changes in social trends, along with changes in other external factors, are difficult to predict. This can make their impact quite difficult when they occur.

5 SUPPLY

ACTIVITY 1

CASE STUDY: FARBOTS

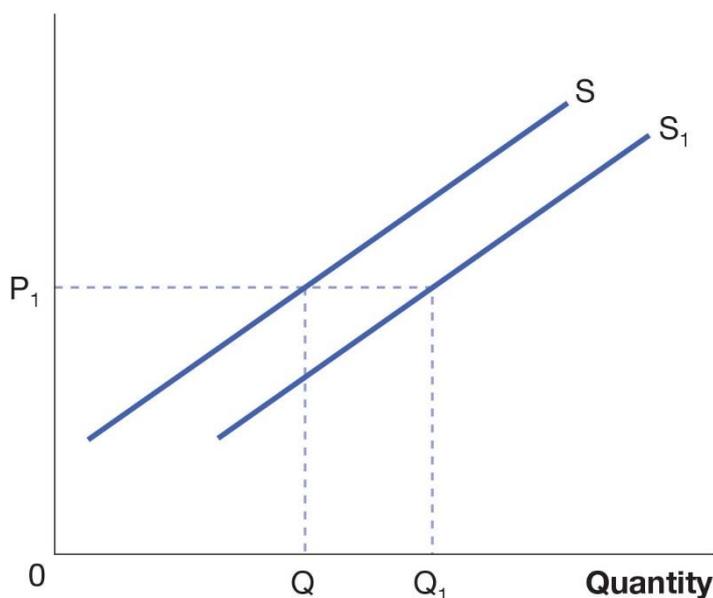
1. Explain one impact that the introduction of farmbots might have on agriculture.

New technology will be more efficient than older technology. This will help to lower production costs and will encourage firms to offer more for sale. In agriculture, a number of new machines are being developed with the capability of raising efficiency and eliminating some of the traditional 'back-breaking' jobs done by farm workers. These new robots can undertake finicky and complex tasks previously considered impossible by large and cumbersome farm machines. For example, a 'lettuce bot' is capable of hoeing weeds away from the base of plants. A 'wine bot' can trundle through vineyards pruning vines. The introduction of these new machines can improve efficiency by replacing expensive labour. Farmbots may also be more reliable and able to work in more extreme conditions.

2. Draw a diagram and analyse the effect that the introduction of farmbots might have on the supply of food.

The introduction of farmbots in agriculture is likely to increase the supply of food in the UK. This is shown (below) by a shift in the supply curve to the right from S to S_1 .

Price



EXAM PRACTICE

GLOBAL OIL SUPPLY

(a) Define supply. (2 marks)

Supply is the amount of a product that businesses are willing to sell in a market at a given price in a given time period. Generally, if market prices rise, producers are willing to supply more in the market. This is because they can make more profit at higher prices.

(b) Explain the possible effects of the fall in the price of oil on (i) oil exploration companies and (ii) haulage contractors (transportation companies). (4 marks)

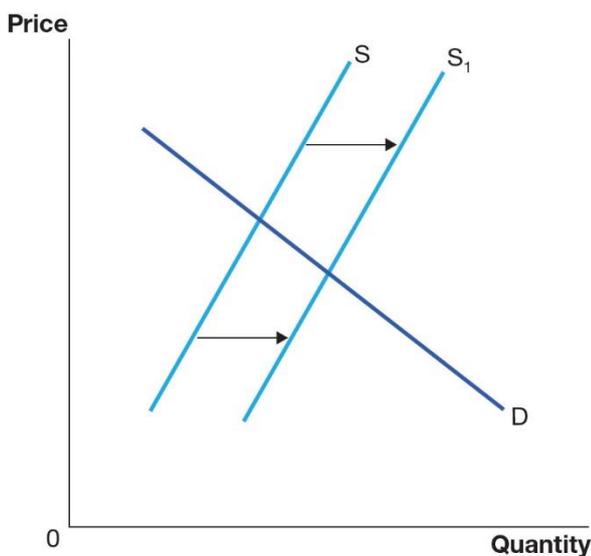
(i) The oil industry has been strongly affected by the fall in the price of oil. Oil companies that extract, process and sell oil have seen their revenues drop. However, oil exploration companies have also suffered. Since the supply of oil has increased, the need for new sources has declined for the time being. Therefore, the demand for the services of oil exploration companies has fallen. This might have resulted in some of the weaker exploration companies leaving the market.

(ii) In contrast, businesses that rely on oil for a raw material have benefitted significantly from the fall in its price. The transport industry, which includes haulage contractors, will have enjoyed the fall in the oil price. This is because the cost of diesel and petrol (made from oil) have also fallen. This means that transport costs have fallen, which should have helped to boost the profits of haulage contractors.

In recent years new technology in oil production such as tracer technology (used to measure flows in reservoirs and assess the economic viability of wells) has helped to reduce costs.

(c) Draw a diagram to show the effect on the supply of oil when new technology in the oil industry is adopted. (4 marks)

The introduction of new technology will help to reduce production costs. As a result, businesses will supply more and the supply curve will shift to the right. In this case the supply curve for oil will shift to the right from S to S_1 when new tracer technology cuts production costs in oil production.



(d) Assess the possible factors that have increased the global supply of oil in recent years. (10 marks)

There is a significant body of evidence in the case study to support the view that the global supply of oil has increased. A number of key reasons are discussed. For example, one of the reasons for this was because OPEC has failed to cut the production of oil, which led to over-supply. In the past, members of OPEC have been able to form agreements that restrict oil production and therefore limit global supply. This drives up the price. More recently such agreements have not been made. OPEC countries supply around 80 per cent of the world's oil. Since OPEC countries supply such a large proportion of global oil, if they are not able to restrict production, then global oil supply will be materially affected.

Supply has also increased because Iran, a major world producer, has been allowed to sell more oil in the market. Iran was subject to sanctions from world powers that prevented it from selling oil. The sanctions were lifted when Iran reduced its development of nuclear facilities. Iran is a large oil producer and its contribution to global supply will be significant.

Another reason for the increase in supply has resulted from new sources of oil. In recent years, the USA has started to extract oil from shale using a process called fracking. For example, in 2017 the Energy Information Administration reported that crude oil storage in the US rose to 8.2 million barrels from the previous week — four times higher than expected. US oil production is now growing at around 9.1 million barrels a day, the highest level in more than a year. The graph in Figure 4 shows that once fracking started, US oil production rose very sharply and continues to rise today. This could be having a very significant effect on the global supply – particularly if it carries on growing.

It is difficult to judge which of these factors has had the biggest impact on global supply. However, since OPEC countries supply 80 per cent of the world's oil, their activities are hugely significant. If they were to reach an agreement and limit production, oil prices might rise sharply again and raise raw material costs right across the global. This is unlikely to be welcomed by world powers.

6 MARKETS

ACTIVITY 1

CASE STUDY: FEEDING LIVESTOCK

1. State the equilibrium price and quantity.

The equilibrium price for large, round hay bales is €25. The equilibrium quantity is 600 000 bales.

2. Using this diagram, explain what is meant by equilibrium price.

In any market, the price is set where the wishes of consumers are matched exactly with those of producers. This price, called the equilibrium price, is where supply and demand are equal. In Figure 2, the equilibrium price is €25. At this price, consumers want to buy 600 000 bales and producers want to sell 600 000 bales. The wishes of buyers and sellers are matched. There is no other price where this happens.

3. What is the value of total revenue at the equilibrium price?

Total revenue is the amount of money generated by the sale of goods. At the equilibrium price of €25 600 000 bales are sold, so total revenue is:

$$TR = P \times Q$$

$$TR = €25 \times 600\,000$$

$$TR = \mathbf{€15\,000\,000}$$

ACTIVITY 2

CASE STUDY: COLD QUEENSLAND

1. Explain the shift in the demand curve from D to D₁.

In Figure 4, the demand curve has shifted from D to D₁. This shows that demand for gas-fired heaters in Queensland, Australia increased. The increase in demand was caused by an unusually cold weather event.

2. What has happened to the equilibrium price and quantity as a result of the shift in demand?

As a result of the increase in demand for outdoor gas-fired heaters, the equilibrium price has risen from AUD 150 to AUD 200. The number of heaters traded in the market rose from 3000 to 4000.

EXAM PRACTICE

THE MARKET FOR ELECTRICITY IN KENYA

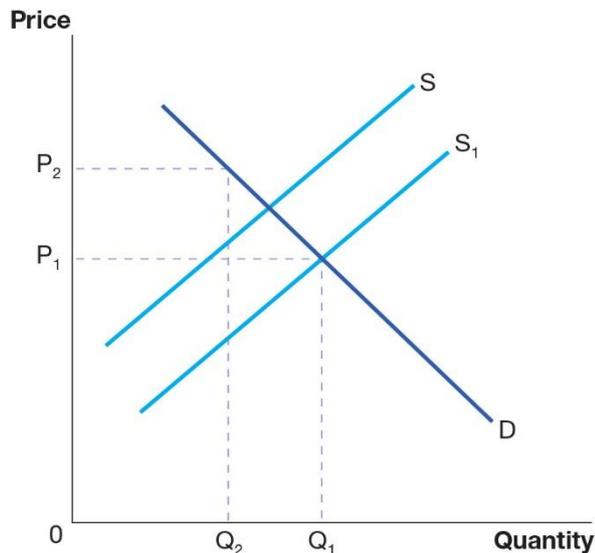
(a) Explain how prices are determined in markets. (4 marks)

In most countries, the prices of goods and services are determined by market forces. In any market, the price is set where the wishes of consumers are matched exactly with those of producers. This price is called the equilibrium price. It is the price where demand and supply are equal. At the equilibrium price the market is cleared. This means that the total amount supplied by producers is bought up by consumers willing to pay that price.

In a minority of cases, governments may set prices. For example, a government might set the price of water. This is probably because many water suppliers are state-owned enterprises and therefore the government has control over prices.

(b) Using a demand and supply diagram, illustrate the impact on the market for electricity in Kenya resulting from the increase in capacity funded by the government. (4 marks)

Kenya has been increasing the supply of electricity for a number of years. In 2013, it started an ambitious programme to connect a greater proportion of the population to the electricity network. The government said it would achieve 'universal access' by 2020 and increase the nation's power capacity from 1600 MW in 2013 to 6600 MW in three years. The effect of this programme is to shift the supply curve for electricity to the right from S to S_1 . In theory, this would cause the price to fall from P to P_1 and the quantity traded in the market would rise from Q to Q_1 .



(b)

(c) There is currently an excess supply of electricity in Kenya.

(i) Use a demand and supply diagram to show what is meant by excess supply. (4 marks)

Excess supply occurs when the supply of a product is greater than demand at current prices. In the diagram below, which shows the market for electricity in Kenya, the current price is P_1 . However, at this price the quantity supplied, Q_S , is greater than the quantity demanded, Q_D . There is excess supply.



(ii) Explain how this excess supply has occurred. (4 marks)

There is a gap between the demand for, and supply of, electricity in Kenya. There is excess supply. The main reason for this is because the government has invested heavily in building up generation capacity. For example, it increased power capacity from 1600 MW in 2013 to 6600 MW in 3 years. This was to support its ambitious programme to connect a greater proportion of the population to the electricity network. However, demand for electricity did not rise by the amount predicted by the government. Much of the increase in demand for electricity was expected to come from the manufacturing sector. However, manufacturing performed poorly and demand did not rise. Some of the planned exports of electricity did not occur and domestic demand from the newly connected Kenyan residents was weak. Consequently, by 2017 the supply of electricity was greater than demand. Indeed, in 2017 demand was 1620 MW and supply capacity was 6600 MW.

(d) Evaluate whether or not the excess supply of electricity will continue in Kenya. (20 marks)

The Kenyan government will hope that the current situation in the market for electricity will be short-lived. The government has built up the country's generating capacity to 6600 MW to support its electricity network development programme but unfortunately demand has only grown to 1620 MW. This means that excess supply is equal to 4980 MW (if the generators were operating at full capacity). If this level of excess supply continued it would represent a waste of resources. Obviously, some spare capacity in power generation is desirable to cope with unforeseen circumstances. However, this level is far too high.

Although the government has cancelled some of the new power generation projects, such as the 700 MW natural gas power plant near Mombasa, it would be reluctant to close down current capacity. The answer lies in demand. The government needs demand for electricity to rise.

Increased demand might come from business. Most commercial demand in Kenya comes from the manufacturing sector but in recent years the manufacturing sector has performed poorly. A number of larger companies, such as tyre maker Sameer, battery maker Eveready and confectionery producer Cadbury, have actually ceased production in Kenya. The sector has declined by an average of 10 per cent per annum in the last 10 years or so. However, in the future demand is likely to pick up. The global economy started to grow more aggressively in 2017 and hopefully the Kenyan economy will share in some of this growth.

There may be more demand in the future from domestic producers. Once universal access is achieved and people buy more appliances that use electricity demand from Kenyan residents may grow. Demand might also be boosted if the government supports the plan to introduce street lighting across the country. Electricity retailer, Kenya Power, has expressed an interest in developing a street lighting programme and would benefit from some encouragement and support.

Another way of increasing demand is to export more electricity. However, some obstacles need to be addressed before this can happen. The government needs to negotiate with some of its neighbours to improve the infrastructure required to distribute electricity. At the moment electricity exports have been held back by the lack of, or existence of, low-capacity transmission lines.

To conclude, eventually, the excess supply in the electricity market will be eliminated. Rising demand will 'soak up' the excess supply. Demand will rise as the population of Kenya grows and as the economy picks up. However, the length of time this will take is uncertain. It could be many years. However, if the government can find ways of boosting economic growth and developing the export market, it might be sooner rather than later.

7 PRICE ELASTICITY OF DEMAND (PED)

ACTIVITY 1

CASE STUDY: CARBONATED DRINKS IN MEXICO

1. Calculate the price elasticity of demand for Agrioslimón.

Price elasticity of demand = Percentage change in quantity demanded ÷ Percentage change in price

Price elasticity of demand = $30\% \div -20\%$

Price elasticity of demand = **-1.5**

2. State whether demand is price elastic or price inelastic.

Demand for Agrioslimón is elastic. This is because price elasticity of demand is greater than 1.

ACTIVITY 2

CASE STUDY: IBADAN PIZZAS

1. Calculate the number of pizzas Rita would expect to sell in 2017 if she cut the price to NGN 1950.

$$\text{Price elasticity of demand} = \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in price}}$$

$$-2 = \frac{\text{Percentage change in quantity demanded}}{-25\%}$$

$$-25\% \times -2 = \text{Percentage change in quantity demanded}$$

$$50\% = \text{Percentage change in quantity demanded}$$

Therefore, demand will increase by 50 per cent when the price is cut to NGN 1950.

New demand = $10\,000 + (50\% \times 10\,000) = \mathbf{15\,000 \text{ pizzas}}$

2. Calculate the change in total revenue resulting from the price change above.

For 2016:

$$TR = \text{NGN } 2600 \times 10\,000$$

$$TR = \text{NGN } 26\,000\,000$$

For 2017:

$$TR = \text{NGN } 1950 \times 15\,000$$

$$TR = \text{NGN } 29\,250\,000$$

Therefore, total revenue increases by NGN **3 250 000** as a result of the price cut.

3. Assess whether Rita's decision to cut price might be successful.

Rita's decision to cut price is likely to increase demand from 10 000 pizzas to 15 000 pizzas. As a result, total revenue would rise from NGN 26 000 000 to NGN 29 250 000, an increase of NGN 3 250 000. This suggests that Rita's decision is a good one. However, before making a final decision, Rita would need to consider the effect of the price cut on profit levels. Although, total revenue will increase, she would need to calculate the cost of increasing output from 10 000 pizzas to 15 000 pizzas before making a final decision.

EXAM PRACTICE

ROBBAT ENGINEERING

(a) Define the term 'elastic demand'. (2 marks)

For some goods, a price change will result in a large change in demand and for others a smaller change. It all depends on the type of good. If a price change results in a proportionately larger change in demand, that product is said to have elastic demand. So, for example, if a price cut of 12 per cent results in a 22 per cent increase in demand, demand for that good is price elastic.

(b) Explain one factor that might affect the price elasticity of demand. (4 marks)

A number of factors can influence price elasticity of demand. One of the most important is the level of competition that exists in a market. In highly competitive markets, demand will tend to be more elastic. This means that demand is very responsive to price changes. A firm that raises price can expect to lose customers and revenue. This is because consumers can switch to a rival's product. In contrast, in markets where there is very little competition, demand will be more inelastic. This means that demand is not very responsive to price changes. A firm that raises prices can expect to raise revenue because the fall in demand is proportionately smaller than the price increase. Consumers cannot easily switch to a rival product.

(c) Calculate the expected change in revenue generated by product A in 2017 if the price is increased by 20 per cent. (4 marks)

$$\begin{aligned} \text{Price elasticity of demand} &= \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in price}} \\ -0.8 &= \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in price}} \\ -0.8 &= \frac{\text{Percentage change in quantity demanded}}{20\%} \end{aligned}$$

$$20\% \times -0.8 = \text{Percentage change in quantity demanded}$$

$$-16\% = \text{Percentage change in quantity demanded}$$

Therefore, demand will decrease by 16 per cent when the price is increased to MYR 60.

$$\text{New demand} = 100\,000 - (16\% \times 100\,000) = 84\,000 \text{ units}$$

$$\text{For 2016 TR} = 100\,000 \times \text{MYR } 50 = \text{MYR } 5\,000\,000$$

$$\text{For 2017 TR} = 84\,000 \times \text{MYR } 60 = \text{MYR } 5\,040\,000$$

Therefore, total revenue is expected to increase by MYR40 000 in 2017.

(d) Evaluate whether or not the price changes made by Robbat Engineering will benefit the business. (20 marks)

$$\text{Price elasticity of demand} = \frac{\text{Percentage change in quantity demanded}}{\text{Percentage change in price}}$$

$$-1.2 = \frac{\text{Percentage change in quantity demanded}}{20\%}$$

$$20\% \times -1.2 = \text{Percentage change in quantity demanded}$$

$$-24\% = \text{Percentage change in quantity demanded}$$

Therefore, demand will decrease by 24 per cent when the price is increased to MYR 42.

$$\text{New demand} = 300\,000 - (24\% \times 300\,000) = 228\,000 \text{ units}$$

$$\text{For 2016 TR} = 300\,000 \times \text{MYR } 25 = \text{MYR } 7\,500\,000$$

$$\text{For 2017 TR} = 228\,000 \times \text{MYR } 30 = \text{MYR } 6\,840\,000$$

Therefore, total revenue is expected to decrease by MYR 660 000 over the two years.

8 INCOME ELASTICITY OF DEMAND (YED)

ACTIVITY 1

CASE STUDY: DAR ES SALAAM PAPER

1. Calculate the income elasticity of demand for paper in this case.

Income elasticity of demand = Percentage change in quantity demanded ÷ Percentage change in income

Income elasticity of demand = 1.5% ÷ 2%

Income elasticity of demand = 0.75

2. Explain whether (a) demand for paper in this case is income elastic or income inelastic and (b) whether paper is a normal good or an inferior good.

(a) In this case the income elasticity of demand for standard A4 paper is 0.75. This is less than 1, therefore demand is income inelastic.

(b) Paper is a normal good because income elasticity is positive.

EXAM PRACTICE

CHINESE OUTBOUND TOURISM

(a) Define the term income elasticity of demand. (2 marks)

Income elasticity of demand measures the responsiveness of demand to a change in incomes. Demand for products may be income elastic or income inelastic. For example, demand for luxury products or non-essentials tends to be income elastic. This means that demand for them will change more than proportionately than any change in income.

(b) Calculate the income elasticity of demand for foreign holidays in China between 2010 and 2015. (4 marks)

Between 2010 and 2015, the demand by the Chinese for foreign holidays rose from 57.4 million to an estimated 135 million. This is an increase of 135 per cent.

Incomes in China (as measured by growth in GDP) rose from US\$6100.62 to US\$11 064 66. This is an increase of 81.4 per cent.

Therefore, the income elasticity of demand is given by:

Income elasticity of demand = Percentage change in quantity demanded ÷ Percentage change in income

Income elasticity of demand = 135% ÷ 81.4%

Income elasticity of demand = **1.66**

(c) Explain why an overseas holiday by the Chinese is classified as a normal good. (4 marks)

Foreign holidays taken by the Chinese are a normal good according to the information provided and the calculation in (b). This is because income elasticity is positive. This means that when incomes rise, the demand for holidays abroad also rise.

The demand for foreign holidays by the Chinese is income elastic. This is because income elasticity is greater than 1 (that is, 1.66 in this case). This means that the percentage change in demand is greater than the percentage change in price.

(d) Analyse two factors that might influence income elasticity of demand. (6 marks)

The value of income elasticity for products will depend largely on whether they are necessities or luxuries. Necessities are 'basic goods' that consumers need to buy. Examples include food in general, electricity and water. Demand for these types of goods will be income inelastic. Also, demand for any products that are deemed to be addictive in nature would be income inelastic.

Luxuries are goods that consumers like to buy if they can afford them. Spending on these types of goods is discretionary, which means that customers can choose whether or not to make these purchases. Demand for these goods is income elastic. Examples include air travel, satellite television, fashion accessories and many goods and services in the leisure and tourism industry. It is also argued that the demand for imported goods is income elastic. It has been found that as developing nations become better off, their demand for imports rises significantly.

In this case, demand for holidays abroad in China is elastic (1.66). This is to be expected since foreign holidays are likely to be classified as a luxury good by most people.

(e) Assess how useful income elasticity might be for a business selling holidays to Chinese tourists. (10 marks)

Businesses may be interested in the income elasticity of demand for their products. If businesses know the value of income elasticity for their products, they can predict the effect on demand of changes in income. In this case, the income elasticity of demand for holidays abroad in China is estimated to be 1.66. Therefore, the demand for overseas holidays in China is income elastic. This means that demand is responsive to changes in incomes. In this case, businesses in China that are linked in some way to overseas travel will recognise that as incomes keep growing, demand for their services will rise. Therefore, travel agents and holiday companies that specialise in overseas holidays, and airlines transporting Chinese tourists, for example, can prepare for rising demand so long as the trend in Chinese GDP continues.

If the 1.66 value for income elasticity is accurate, businesses in the overseas travel sector can predict what will happen to demand in the market when incomes rise. This will help these businesses plan for the future. It might help with their investment decisions for example. The trend in Figure 2 shows the rise in demand for foreign holidays is quite stable. This will encourage such businesses.

However, although businesses might know that income elasticity of demand for foreign holidays in China is 1.66, predicting demand for goods which are influenced by the business cycle can be quite difficult. What happens if growth in the Chinese economy starts to fall suddenly? If there was a sudden drop in income, knowledge of income elasticity may not be that helpful. However, a well-run business, knowing that demand for one of its product groups was income elastic, could make plans to deal with such events. Therefore, knowledge of income elasticities would be useful to businesses in general.

9 MARKETING OBJECTIVES AND STRATEGY

ACTIVITY 1

CASE STUDY: GOLF GTI

1. What is meant by an extension strategy?

Extension strategies are used by businesses to prolong the life of the product. They aim to boost the sales of a product by making adjustments to it or investing in a new promotion campaign. A business might try to introduce an extension strategy at the maturity stage, just before sales start to decline.

2. Explain one way in which VW extended the life of the Golf GTI.

The VW Golf GTI has been on the market for over 40 years. However, the model in today's showrooms looks a little different from the Golf GTI Mk 1, which launched in 1975. VW has launched six different Golf GTIs since 1975. The introduction of each new model aims to prolong the life of the product.

The new models usually contain some new features, technological improvements or styling changes. The Mk V GTI, launched at the Paris Motor Show in 2004, was the most powerful GTI yet produced. The vehicle had new springs, dampers and anti-roll bars. The most recent model, the Golf GTI Mk VII introduced in 2012, had a lighter but stronger platform, was the most fuel-efficient GTI to date, and was capable of 0–62 mph (0–100 kpm) in 6.5 seconds. VW used changes to the product as an extension strategy in this case.

3. Explain one advantage to VW of using an extension strategy.

Each time a new version of the model is introduced, VW will expect to see sales pick up. The new, improved versions are fresher and technologically superior. By introducing new versions every few years, VW has been able to keep the Golf GTI on the market for over 40 years. Without these extension strategies, sales of the model would probably have declined. The old Mk I GTI would be out of date today in many ways.

By using these extension strategies VW can carry on enjoying high revenue streams and avoid the costs of launching a brand-new model to replace the GTI. Developing and marketing a brand-new model would be far more expensive than prolonging the life of a popular existing model. For example, a brand-new model would probably need a whole new production line with new tooling and possibly even a new factory. This cost is avoided by prolonging the life of the GTI.

ACTIVITY 2

CASE STUDY: CHEEZYBIX

1. Explain how you would categorise the position of Crackles in the Boston matrix using Figure 6.

Crackles can be described as a 'Cash cow'. Its position in the Boston Matrix shows that, although it has little potential for future growth, it has a high market share. This means that Crackles can continue to generate cash for the business for some time yet. It is likely to be a profitable product for CheezyBix Ltd and there will be less need for investment in the product. The cash generated by Crackles might be used to develop new products.

2. Explain one way in which CheezyBix might use the information in Figure 6.

A business such as CheezyBix Ltd can use the Boston Matrix to help manage its product portfolio.

ACTIVITY 3

CASE STUDY: CREDIT CARD CASHBACK DEALS

1. Calculate the amount of cashback a customer would be entitled to if £5000 is spent on the card in the ninth month of ownership.

The amount of cashback is:

$$(\pounds 3500 \times 0.5\%) + (\pounds 1500 \times 1\%) = \pounds 17.50$$

$$\pounds 17.50 + \pounds 15 = \pounds 32.50$$

2. Explain one way in which cashback cards might help to develop customer loyalty.

Customer loyalty can be developed in several ways, such as communicating with customers using advertising, offering preferential treatment to 'high value' customers, providing high-quality customer service and personalising the relationship between the business and the customer.

However, in this case, American Express is offering customers financial incentives. By offering cardholders cashback every time they make a purchase, customers are encouraged to 'stick with the card'. Many people have several credit cards, but if a particular card offers rewards for continued use, they are more likely to carry on using it.

Also, in this case, the rewards are tapered up so that higher levels of spending on the card give higher rewards. For example, the first £3500 spent on the card generates 0.5 per cent cashback, but if spending reaches more than £7500, the rate rises to 1.25 per cent.

Finally, once people have selected a particular credit card they are likely to retain it for quite a time, because it often requires some effort to obtain a new card. Once people have opted for the Platinum Cashback Everyday Credit Card, American Express may have attracted a loyal customer – possibly for life!

EXAM PRACTICE

ENSCHEDÉ GRASSMAAIERS

(a) Explain what is meant by the marketing mix. (4 marks)

In order to market its products effectively, a business must consider its marketing mix. The marketing mix refers to those elements of a firm's marketing strategy that are designed to meet the needs of its customers. The marketing mix emphasises four particular elements often referred to as the 4Ps – product, price, promotion and place. To meet customer needs and to create an effective marketing mix, businesses must produce the right product, at the right price, make it available in the right place and ensure that customers are aware of its existence through effective promotion.

In this case, Enschedé Grassmaaiers emphasise the quality of their product and after-sales service. The lawnmowers are extremely well made. They are manufactured from high-quality materials and components and very rarely breakdown. The mowers often last for 20 years or more. The company also has a breakdown support team that is on call seven days a week. This means that customers can contact the company and organise a visit from the service centre on the same day in the event of a breakdown.

Enschede Grassmaaiers are able to charge a premium price for their ride-on mowers. This means they charge a high price that reflects the both the quality of the product itself and also the quality of the after-sales service.

There is little evidence in the case to suggest that the mowers are heavily promoted. However, since the products are targeted at a niche market, it is unlikely that the machines will be advertised using mass media, such as television and national magazines. Finally, the lawnmowers are distributed through specialist dealers throughout most of the Netherlands.

(b) Explain how a business like Enschede Grassmaaiers might benefit from having a specific marketing objective? (4 marks)

The marketing activities of a business are likely to be more effective if there are clear and specific marketing objectives. These are the goals that a business is trying to achieve through its marketing. Although the general role of marketing is to help sell products, it is possible to identify specific marketing objectives. These objectives may differ between different business organisations. It is also likely that the marketing objectives of a particular business will vary over time to match its changing marketing needs. Common examples of marketing objectives are to increase market share, increase revenue and build a brand. In this case, the directors of Enschede Grassmaaiers aim to extend the life of their main product for another 20 years. This goal might be achieved by introducing an effective extension strategy.

Finally, a business is more likely to achieve its marketing objectives if they are SMART. This means that they should be specific, measurable, agreed, realistic and time specific. It could be argued that Enschede Grassmaaiers's marketing objective is SMART. The company aims to extend the life of the product for 20 years.

(c) Analyse two possible extension strategies that Enschede Grassmaaiers might consider. (6 marks)

Extension strategies are the methods used to prolong the life of a product before it starts to decline. Extension strategies are popular because they avoid the expense of developing and introducing new products. Two broad approaches might be used by a business. One is to make some adjustments to the product. This might involve updating or modifying the product. Another option is to add value to the product. This might involve adding some 'extras' or improving the functionality of a product. Other common approaches are to extend the product line or change the packaging of the product.

Alternatively, a business may leave the product unchanged and look to promotion as a means of prolonging its life. A business may try to find new uses for the product, explore new markets such as exporting, invest in advertising or encourage more frequent use of the product.

In this case some of the extension strategies are probably not appropriate for Enschede Grassmaaiers. For example, adjusting the packaging, finding new uses or encouraging more frequent use of ride-on lawn mowers are not really suitable for this particular product. However, the company could explore the possibility of exporting to neighbouring countries, such as Germany, Belgium and Luxembourg. The city of Enschede is actually located right on the border with the Netherlands and Germany, which has a population of 80 million and might be an attractive market. The company might also consider investing in some promotion. There is little evidence of heavy promotion expenditure in the case so perhaps this is an option. However, since Enschede Grassmaaiers serves a niche market, the company will need to use some fairly specialised promotion techniques. Finally, the company might consider upgrading the lawnmower. One option might be to develop a robotic version. This might be popular with customers since it avoids the need to ride on the mower. However, a development like this would need some technical expertise, which Enschede Grassmaaiers may not have. Therefore, developing the export market or investment in promotion might be the best way to extend the product in this case.

(d) Assess how the marketing strategies of a business might differ for a business operating in a mass market. (10 marks)

In this case, Enschede Grassmaaiers serves a niche market. The company targets people that own properties with large lawns, sports clubs and small farmers. This is quite a specialised market and the marketing strategies used by the company will be quite different from those used by a business aiming products at a mass market. For example, Enschede Grassmaaiers is not likely to use national television or newspapers to advertise its ride-on lawnmowers.

Mass markets are huge, often global and can have millions of potential customers. Unilever, Heinz, Kellogg's, Pepsi Cola and Honda are examples of businesses that sell into mass markets. They are usually very competitive because the rewards for success in these markets can be significant. A wide range of different marketing strategies might be used in a mass market but some general similarities might be as follows.

In a mass market, there will be many products competing for customer attention. The most successful businesses are likely to be those that can differentiate their product in some way. If a business can develop a unique selling point, that will help their product 'stand out from the pack'. If a business is unable to differentiate its product, it will have to rely on other elements in the marketing mix to compensate.

The prices charged by businesses competing in a mass market are likely to be very similar. This is quite different from Enschede Grassmaaiers which charges a premium price. Firms in a mass market may operate in fear of a price war breaking out which will reduce revenue for every competitor. This helps to explain why businesses are happy to charge the 'going rate' in the market. Price leadership is common in mass markets where the dominant business, perhaps the one with the lowest costs, sets the price and everyone else follows.

Large sums of money are spent promoting and advertising products in mass markets. In the absence of price competition firms look to non-price competition to help gain an edge. This means they are prepared to invest heavily in advertising and promotion because it is such an important part of the marketing mix in mass markets. An overwhelming majority of adverts on the television are placed by businesses selling into mass markets. In contrast, Enschede Grassmaaiers probably spends very little on advertising and promotion.

Businesses serving mass markets will often use multiple channels to distribute their goods. Firms selling fast moving consumer goods will target supermarkets, wholesalers, independents and any other outlet that is suited to their particular product. The Internet is used increasingly by businesses to sell goods and services in mass markets. For example, all banks offer online bank accounts and an increasing number of supermarkets offer online shopping and delivery or 'click & collect' services.

The marketing strategies used by businesses competing in a mass market will depend on a range of factors such as the size of the business and the nature of the product. However, the strategies chosen are likely to differ significantly from those used by a company like Enschede Grassmaaiers, serving a niche market.

10 PRODUCT/SERVICE DESIGN

ACTIVITY 1

CASE STUDY: ERGONOMIC WORKSTATIONS

1. Explain what is meant by an ergonomically designed product.

Ergonomics is the study of how people interact with their environment and the equipment they use – often in the workplace. Some products are ergonomically designed, which means people can interact with them without expending any unnecessary effort. In this case, the workstation is designed so that an employee can sit comfortably. The seat is designed to support the back and is adjustable to accommodate people with different heights, and there are rests for feet and wrists.

2. Explain the possible benefits to a business of using ergonomically designed workstations.

If people are comfortable in the workplace they are likely to be more productive. As a result, businesses will benefit from higher levels of output and better-quality work. In this case, office workers spend a lot of time sitting in front of computers. If their seats fail to support their backs adequately, this could result in staff absence due to back-related medical conditions. Clearly, higher productivity levels and lower staff absence will improve profitability.

ACTIVITY 2

CASE STUDY: THE DESIGN MIX

1. Match the following products with the positions (1–5) shown on the triangle which best represent the design mix in Figure 3. Each of the positions suggests which aspect of the mix may be relatively more important for particular products. (a) designer shoes, (b) a sports car, (c) a life assurance policy, (d) a dining room table, (e) a smartphone.

- (a) designer shoes – 5
- (b) sports car – 3
- (c) life assurance policy – 2
- (d) dining room table – 4
- (e) smartphone – 1

2. Explain how cost might affect the design of a package holiday.

Travel companies and tour operators are likely to consider cost as an important element of the design mix when designing package holidays. A lot of people have a budget to spend on their annual holiday, so it is important for travel companies to keep their prices within the budget range. When they put the packages together, they must try to minimise the cost of flights, hotels, transfers and any other element of the package.

ACTIVITY 3

CASE STUDY: DELL™

1. Explain how Dell reduces waste through its design process.

Dell believes that all materials are valuable and waste should be eliminated. The company has made some progress in recent years by reducing waste. It has added incorporated waste reduction measures to its design process. For example, the company uses environmentally friendly materials such as recycled plastics and exceeds legal requirements when selecting 'safe' materials for production. Between 2015 and 2016, Dell reduced the average energy used to build each item in its

product portfolio by around 16 per cent. Since 2012 the reduction has been 42.8 per cent. Also, the use of glues and adhesives, which are not easily recycled, have been replaced with new 'snap-fits' and other substitutes. These measures, and more, provide evidence which supports the view that Dell has used its design process to reduce waste.

2. Explain how Dell's approach reflects social trends.

Society has become increasingly aware of the effects their lifestyles have on the environment. Worries about global warming, resource depletion and pollution have encouraged many people to adopt more environmentally-friendly lifestyles. Dell has responded positively to social trends by designing products and production process which are sensitive to the needs of the environment. For example, Dell uses a closed-loop plastics supply chain which is able to repeatedly recycle and re-use materials over and over again. Dell also tries to use reputable third-party eco-labels such as ENERGY STAR, EPEAT and the 80 PLUS Program when searching for technology to use in its organisation. These are just a couple of examples which suggest that Dell shares the increasing concerns about the environment.

EXAM PRACTICE

STANLEY MODULAR

(a) Explain how designs that reduce waste benefit Stanley Modular. (4 marks)

Stanley Modular's building designs and construction methods have reduced waste very effectively. The main benefit of this to Stanley Modular is lower costs. For example, if fewer materials are used up in construction, direct costs will be lower. This will help to boost profits or provide an opportunity for the business to lower prices. Lower prices will help to attract more customers. Generally, lower levels of waste in a business will help to improve financial performance.

(b) Explain the aspects of the traditional design mix that might be important to Stanley Modular. (4 marks)

It could be argued that cost and functionality are the most important features in the traditional design mix here. Buildings must be functional. For example, people buy houses primarily for shelter and comfort, so it would be important for buildings to be warm, secure, storm-proof and well appointed, with connections to modern utilities, such as broadband and possibly satellite television. Buildings should also be ergonomically designed and offer convenience to house dwellers.

However, cost will also be important. Stanley Modular has certainly made an effort to build cost effectively. Their designs have reduced waste in a wide range of areas, which helps to keep down costs. Many people have to borrow money to buy a house, so they will appreciate lower costs.

Arguably, aesthetics is less important than cost and functionality in this case. Some of the buildings, such as schools, are designed for the public sector. It will be more important to a government that schools are designed so that costs are minimised, and that they are fit for purpose.

(c) Assess the benefits to Stanley Modular of adapting its designs to reflect changes in social trends. (10 marks)

Although businesses may have to make an effort to reflect social trends in their designs, there are likely to be some lucrative benefits. For example, if businesses can reduce waste they will use fewer resources, resulting in lower costs and higher profits.

Stanley Modular has built a number of waste-minimising measures into its designs, and has cut transport costs. For example, a three-bedroomed house can be transported to site on a single truck, with flat-pack panels on the front, roofing on the back and a 4-metre trailer containing the bathroom modules. More complex parts of the building process require more trips, but far fewer than would be required on a traditional building site.

Also, in a typical build, 1200 kg of timber is wasted – Stanley Modular only wastes around 10 per cent of this.

In addition, the use of computer numerical control (CNC) machinery makes a major time saving in the operation of the Stanley Modular operation, where it is estimated that construction is up to a third faster in the factory than on site. The use of CNC machinery is also 50 per cent faster than manually-controlled machinery.

11 PROMOTION AND BRANDING

ACTIVITY 1

CASE STUDY: WORLD WILD FUND FOR NATURE

1. Define above-the-line promotion.

Above-the-line promotion involves paying the owners of media to place an advert. Businesses pay television companies or newspapers, for example, to have their adverts broadcast or printed. In this case, the WWF would have paid the owners of poster sites, such as billboards and bus shelters, to display its posters.

2. Explain one advantage of using posters as an advertising media.

Posters are a favoured advertising media for a number of businesses. The use of posters can have several benefits. Posters can be used in a national advertising campaign because they can be placed on sites all over the country. They are also likely to be seen repeatedly by people as they pass them – perhaps once a day or more. Posters are particularly good for short, sharp messages and large posters can have a big impact. In this case, the poster is designed to persuade people to think about global warming. The image is clear and does not require any lengthy written message. Posters are sometimes used to support other campaigns, such as television advertising.

(c) Assess to what extent the advert in this poster is meant to be persuasive.

Some advertising is designed to put pressure on consumers to buy a product – or in this case to change behaviour. Persuasive advertisements are often designed to appeal to people's emotions such as desire, fear and pity. Persuasive adverts may also appeal to people's respect for authority and fascination with celebrity.

In this case, the WWF is using a poster campaign to raise awareness about the damage that climate change, caused by global warming, might do to both wildlife and the human race. The image on the poster causes a strong emotional response and is probably designed to encourage people to think about the possible ways they might reduce global warming – such as recycling products, using 'green' energy and buying electric cars rather than those that run on petrol or diesel.

ACTIVITY 2

CASE STUDY: SPORTS SPONSORSHIP

1. Define sponsorship.

Sponsorship is a form of public relations where businesses attempt to communicate with interested parties. It involves making a financial contribution to an event in return for publicity. Many companies attract publicity by linking their brands with events – for example, major sporting tournaments and championships. In 2017, around US\$62 800 million was reported to have been spent on sponsorship worldwide, most of which went on sport.

2. Explain the advantages of sponsorship to a company like Rolex.

Sponsors like Rolex benefit from having their name and logo 'splashed' everywhere at the event. In this case, the Rolex logo would be placed in very prominent positions on the golf course, including on every single tee (where play begins for each 'hole'). The logo will be picked up by the television cameras and broadcast, both live and in highlights packages. For example, the US Open Golf Championship was broadcast around the world, to a massive potential audience. Sponsorship is often considered a cheap way of getting products advertised on television without having to pay the television broadcasters.

ACTIVITY 3

CASE STUDY: BLOGGING

1. Explain the potential role played by fashion bloggers in business.

Blogging involves sharing opinions, information, observations and other content online. Bloggers usually write regular articles, perhaps in a diary form, to express their views and provide updates on a very wide range of topics. One popular and large part of blogging is fashion blogging. In China, fashion bloggers are having an increasing influence on the fashion industry.

Fashion bloggers like 'Li Beika/Becky', offer information and shopping tips to consumers. In this case, Li writes about clothes and fashion accessories sold by well-known luxury brands and those available from little known high-quality independents. Li's background is in journalism – current affairs and politics to be precise. Although she has no real work experience or training in the fashion industry, she has developed the ability to identify trends in the industry, understand what readers like and dislike and what writing styles attract interest. Every day Li advises readers where and how they should spend their money. Li has an excellent reputation for spotting fashion trends and knowing outlets from where products can be purchased.

The role of fashion bloggers like Li is to inform consumers about products in the market and give their opinions on issues such as product quality, trends, availability and prices.

2. Assess the benefits to businesses in the Chinese fashion industry of using social media in this way.

It is important for businesses in China to know about fashion bloggers because their views can influence what consumers buy. If businesses can work with bloggers they may be able to persuade consumers to buy their products. In one of her blogs, Li recommended an Italian handbag brand. It was only known to few and only available in one store that was in southwest China. As a result of her blog, the brand saw very rapid sales growth. This is an example of how fashion bloggers can benefit businesses in the industry.

Also, it is very likely that the cost of working with bloggers is significantly lower than funding other forms of marketing and promotion such as television adverts, for example. Businesses can select specific fashion bloggers that are appropriate for their image and product lines. This will help to target customers more accurately. For example, Li's target audience on her blogging account is women of upper- to middle-income class.

So far Li, who had over 700 000 followers by mid-2016, has worked with brands like Gucci, Chanel, Jo Malone and many others.

EXAM PRACTICE

PROCTOR & GAMBLE (P&G)

(a) Define viral marketing. (2 marks)

Viral marketing involves any strategy that encourages people to pass on messages to others about a product or a business. It creates the potential for rapid growth in the exposure of a message. Like a virus, these strategies exploit the process of rapid multiplication that results from people sending messages to family, friends and colleagues, who then send them on again. In this case, a television advert produced for P&G to promote Ariel called 'sharetheload', went viral in India. The advert features the challenges faced by a young Indian women attempting to balance the demands of raising a family with developing a career. The advert critically explores India's traditional male-dominated society.

(b) Explain one way in which P&G might have benefitted from its Ariel advert that 'went viral'. (4 marks)

When messages go viral on the internet they travel very quickly and can reach huge numbers of people. In this case, the 'sharetheload' advert went viral in India. India has a very large population and the popularity of the advert probably meant that it was seen perhaps by many millions of people. When the advert went viral, P&G would have benefitted from considerable exposure. The advert would also have been broadcast free of charge by the people who sent the message to their friends and family. This 'free' advertising would be highly valuable to P&G. It is also possible that the advert was sent to other countries. This would just add to the benefit.

(c) Explain how P&G differentiates many of its brands. (4 marks)

Many of P&G's brands are positioned at the 'top end' of the market. Much of the company's marketing is designed to show quality in the products, which allows P&G to charge higher prices than many of its rivals. Although P&G invest very heavily in developing and supporting their brands, since they can charge a premium price these costs are likely to be recovered. People are often prepared to pay a higher price if they believe that they are buying a quality product. Suggesting that a product is of high quality is a common way of differentiating it from those of rivals.

(d) Assess the benefits to P&G of having very strong brands. (10 marks)

Many of P&G's brands such as Ariel, Bounty, Charmin, Fairy, Febreze, Gillette, Head & Shoulders, Lenor and Olay are powerful and valuable and are purchased by around 5000 million people. P&G has 23 brands that generate sales of between US\$1000 million and US\$10 000 million each per year. Marketing such strong brands will bring P&G a number of benefits. A strong brand may add value to a product in the eyes of customers. Consumers may feel that P&G's products are of a high quality. As a result, the business will enjoy higher sales as it exploits its competitive edge.

One of the main advantages of a strong brand is the ability to charge a premium price. Products with strong brands can be priced higher than those of competitors. This is because of the customer loyalty that has been built up over a period of time. People are less likely to switch to cheaper brands if they have developed the habit of buying a 'favourite' brand. Many of P&G's products are positioned at the top end of the market and do carry premium prices. However, if the brand remains strong and can hold its position in the market, P&G will be able to charge higher prices for longer. This will generate more revenue and profit for the business.

Another benefit of a strong brand is lower price elasticity of demand. Firms would prefer their brands to have a lower price elasticity of demand. This means that a price increase will have less impact on demand. For example, if a product has price elasticity of demand of -1.5 , a 10 per cent increase in price will result in a 15 per cent decrease in demand. However, if price elasticity is lower at -0.9 , a 10 per cent increase in price will reduce demand by just 9 per cent. Consequently, with a strong brand

and lower price elasticity, P&G may find that fewer customers switch to alternative products if it decides to raise prices.

Although P&G incurs high costs maintaining its brands, the rewards are significant. In 2015, P&G enjoyed sales revenue of over US\$76 000 million and a profit for the year of over US\$7000 million. Also, the Glass Lion award won at the Cannes Film Festival will help to raise the profile of the company and may generate some very positive publicity. This is because the advert, which is associated with one of its strongest brands, addressed issues of gender inequality and suggests that P&G is a socially-responsible corporation.

12 PRICING STRATEGIES

ACTIVITY 1

CASE STUDY: BANGLADESHI STREET FOOD

1. (a) Calculate the prices charged by Raihan for his three best sellers.

The prices of Raihan's best-sellers are given by:

Singara – $\text{BDT } 10 + (50\% \times \text{BDT } 10) = \text{BDT } 15$ (that is, a mark-up of BDT 5)

Fish somosa – $\text{BDT } 12 + (50\% \times \text{BDT } 12) = \text{BDT } 18$ (that is, a mark-up of BDT 6)

Poori bhaji – $\text{BDT } 8 + (50\% \times \text{BDT } 8) = \text{BDT } 12$ (that is, a mark-up of BDT 4)

(b) Calculate the total profit (before overheads) made by Raihan from these sales

The profit (before overheads) made by Raihan is given by:

Singara – $\text{BDT } 5 \times 80 = \text{BDT } 400$

Fish somosa – $\text{BDT } 6 \times 100 = \text{BDT } 600$

Poori bhaji – $\text{BDT } 4 \times 70 = \text{BDT } 280$

Therefore, the total profit (before overheads) was **BDT 1280**.

2. Explain one possible disadvantage to businesses of using cost plus pricing.

Although cost-plus pricing is simple and ensures that costs are covered, the method does have one notable disadvantage: cost-plus pricing ignores market conditions. For example, the mark-up used by a business may be far too high in relation to the prices of rival products. This might result in low sales. In this case, Raihan might need to look at what other street food sellers are charging in the area to ensure that his prices are competitive.

ACTIVITY 2

CASE STUDY: PLAYSTATION 3

1. Explain the pricing strategy used by Sony in this case.

The pricing strategy used by Sony for its PlayStation gaming machines is called skimming or creaming. This involves launching a new product into a market and charging a high price for a limited time period. The idea is to exploit the popularity of a new product while it is unique. Later in the product's life cycle, prices are reduced. This method is common with technical products such as gaming machines. For example, the PlayStation 3 was launched in 2006 for a price of \$599; by 2009, the price had dropped to \$299.

2. Assess the advantages and disadvantages of the pricing strategy used by businesses like Sony.

One of the main advantages of skimming is that high prices are charged to people who are prepared to pay higher prices. This helps to maximise revenue. When PlayStation 4 was launched, its price was \$399 – a price that some people are prepared to pay, because they want to be the first with the new product. Eventually the price will be lowered and other customer groups will be drawn into the market (although in November 2014, Sony said that a price reduction was not imminent). However, in the future most people would expect the price to fall – especially if Sony plans to introduce a new product such as PlayStation 5.

The higher revenues from charging a higher initial price will help Sony to recover the cost of research and development. The higher price also helps to elevate the image of the product.

However, skimming can only be used if demand is price inelastic. A high price cannot be charged if demand is price elastic because demand will fall too sharply. This method of pricing is only suitable for certain types of product in specific markets. The product has to be new and fairly unique in order for people to pay a premium price.

EXAM PRACTICE

ADOBE

(a) Define subscription pricing. (2 marks)

Subscription pricing involves charging consumers a regular fee, usually monthly or annually, for access to a particular product or service. In this case, Adobe has switched from a more traditional pricing strategy, where customers are charged 'one-off' or 'standalone' fees for different software packages, to a £47 a month subscription fee. The subscription to Adobe's Creative Cloud – a web-based system – gives customers access to all of Adobe's software, an online storage system and project management tools.

(b) Explain one reason why Adobe switched to subscription pricing. (4 marks)

The main advantage of subscription pricing is that customers are tied into long-term agreements with businesses. Although customers have the right to cancel subscriptions, many do not. Adobe will continue to receive payment for an indefinite period, which is an attractive proposition. It helps to improve cash flow and removes some of the uncertainty about future sales levels. Also, an Adobe spokesman said the move to a subscription system would release the company from its traditional 18- to 24-month upgrade cycle; instead, improvements would be released as they became available. This would help relieve some of the pressure on the business to update software by a particular deadline, providing some flexibility for Adobe.

(c) Discuss the success of Adobe's subscription pricing strategy. (8 marks)

The subscription pricing strategy was introduced in 2013. Reaction to the strategy has been mixed. For example, according to information in the case, some customers preferred the traditional sales approach. This may not be too encouraging for Adobe. However, the pricing system was only introduced in 2013, so it may be better to evaluate the success of the new strategy a bit further into the future.

In slight contrast, it was widely reported that, by the end of 2014, there were over 3 million subscribers to Creative Cloud, and feedback suggested that the satisfaction level was high. This probably indicates that the new pricing strategy is proving successful.

As subscription pricing becomes more widespread, it could be argued that it will eventually become the norm. In 2011, Microsoft introduced Office 365, a subscription version of Office applications plus other productivity programs. Adobe's introduction of a subscription pricing strategy in 2013 reflected a growing trend for large software firms to adopt a subscription pricing strategy. Feedback on customer satisfaction indicated that more customers were comfortable, as part of this trend, with paying for an online service.

Indications that satisfaction is high among the 3.4 million who have subscribed suggest it might be a shrinking problem. It often takes time for some people to adjust to new regimes. Adobe is probably content with success so far.

(d) Evaluate whether subscription pricing or cost plus pricing would be the most suitable pricing strategy for Adobe. (20 marks)

A wide range of factors can influence the price that a business charges. In the long term, a business cannot ignore its costs; it has to cover costs and make a profit. In this example, the subscription charge of £47 per month in the UK for access to Adobe's Creative Cloud is presumably a price that will generate a long-term profit for the company. There is no indication that this is an introductory offer. Even if businesses use strategies that involve lowering prices for a time, costs will always have an important influence on long-term pricing. This might account for the popularity of cost plus pricing.

Competition in a market will also be a key factor for most businesses. In highly competitive markets, prices are likely to be very similar. Firms will want to avoid a price war by trying to undercut their rivals. In some cases, a dominant firm might set the price and all other firms are just happy to follow the leader. In competitive markets, only those firms with a strong brand or some USP have any chance of charging premium prices. Adobe is a strong brand, but there are other powerful players in the market – such as Microsoft. Adobe will have to consider the pricing strategies used by its rivals when setting its own prices.

Price elasticity of demand is likely to be an important influence. If the demand for a firm's products is price inelastic, there will be scope for price increases. For example, if price elasticity was -0.8 , a business could raise its price by 10 per cent and demand would only fall by 8 per cent. As a result, total revenue would rise. In contrast, if a firm's product is price elastic, it may benefit from price cuts. For example, if price elasticity was -2.7 , a 10 per cent reduction in price would result in a 27 per cent increase in demand. This would increase total revenue. The price elasticity of demand for Adobe's products is not given in this case, but Adobe may consider price elasticity before making changes to its prices.

Changes in social trends may affect pricing in business. For example, it could be argued that today's consumers are more aware and better informed than ever before. As a result, they may challenge the prices that businesses charge. They may 'haggle' or spend more time searching for 'bargains'. They may also be less tied to particular brands, and consider instead the views and experiences of friends and colleagues posted on social media sites.

Businesses are having to adapt to selling goods online. Many businesses use traditional pricing strategies such as cost plus pricing. For others, selling goods online has provided opportunities for new pricing strategies. In this case, arguably, Adobe has responded to changes in social trends. Most of Adobe's sales are made online, and they have now introduced subscription pricing. Adobe is the latest in a number of large software firms that have adopted a subscription pricing strategy. Microsoft has also introduced Office 365, a subscription version of its set of office productivity programs. This may reflect social trends in the way consumers expect to pay for products in the future, as more shopping is done online.

To conclude, Adobe has adopted a new pricing strategy because it is an online business and wants to keep up with changes in social trends. However, when setting prices it will always have to consider costs and the level of competition in the market. These are key.

13 DISTRIBUTION

ACTIVITY 1

CASE STUDY: DRESSMAKING IN FAISALABAD

1. What is the difference between a department store and a chainstore?

A department store is a very large store divided into departments, each one selling a different category of goods. The departments might be menswear, womenswear, children's clothes, home and garden, electricals, sport and leisure, toys and beauty. In contrast, a chainstore is one of a series of shops owned by one company and selling the same products. The chain might be regional or national.

2. Explain why distribution through multiples might be more profitable for Mansoor Aslam's business than independent retailers.

Aslam is keen to widen the distribution network of his family's business. The aim is to develop distribution channels with department stores and chainstores. The main advantage of using these channels is that larger quantities can be sold to the new customers. An order from an independent retailer might be for five dresses. In contrast, an order from a regional or national multiple might be for many hundreds. This should help to generate larger revenues for the business. Distribution costs might also be lower. For example, it should be cheaper to transport a very large order to a distribution centre or warehouse belonging to a chainstore than delivering separately to dozens (or more) of small independent retailers in a wide area.

However, large chainstores and department stores would expect to buy dresses from Aslam's business at much cheaper rates than independents. They would expect discounts for buying in bulk. Aslam and his family would have to consider whether supplying customers with large orders at lower rates is profitable.

ACTIVITY 2

CASE STUDY: AGENTS

1. Explain one motive for using an agent when selling overseas.

The use of agents when selling goods overseas is common. When a business exports for the first time it may lack the experience and confidence to 'go it alone'. For example, a UK company trying to penetrate the Chinese market is likely to face a number of obstacles. Using an agent reduces the risk and uncertainty of selling abroad.

2. Assess the advantages of using agents when trying to penetrate overseas markets.

The use of an agent may reduce the risk of exporting, and may provide a number of financial benefits. Using an agent avoids the cost of recruiting, training and paying specialist overseas sales staff; the agent will bear the burden of these costs. An agent is likely to have a network of contacts that can be exploited immediately, rather than spending time to develop contacts when 'going it alone'. Agents may be preferred to distributors because the seller then has more control over matters such as prices, display and brand image. Finally, agents have the experience and knowledge needed to sell in places where culture, trading practices, commercial laws and other customs are different from the UK.

ACTIVITY 3

CASE STUDY: POLISH ONLINE RETAIL

1. Calculate the percentage change in online retail spending between 2014 and 2016.

Between 2014 and 2016 online retail spending in Poland rose from PLN 27 400 million to PLN 38 100 million. The percentage change is given by:

$$\text{PLN } 38\,100 \text{ million} - \text{PLN } 27\,400 \text{ million} = 10\,700 \text{ million}$$

$$10\,700 \text{ million} \div 27\,400 \text{ million} = 0.39$$

$$0.39 \times 100 = \mathbf{39\%}$$

2. Explain one reason which might account for the change in online spending in Poland.

The significant 39 per cent increase in online spending might be explained by a change in social trends. It could be argued that an increasing number of people prefer online shopping. There are some significant advantages of this method. It is cheaper because online retailers often have lower costs. For example, they may not have to meet the costs of operating shops and stores. Consumers can shop 24/7 at their own convenience. They do not have to shop during 'normal' shopping hours. Online shoppers usually have a huge amount of choice – they can browse lots of different websites from suppliers all over the country, or even the world for some products. Finally, people can shop from anywhere they like if they have access to the internet. An increasing number of people are using their mobile devices to do their shopping.

3. Assess the advantages to Polish businesses of online distribution.

A business might enjoy a number of benefits from online distribution. To begin with it can offer goods to a much wider market – in some case it might be able to sell into global markets. A business may also enjoy lower costs. For example, it may not have to meet the costs of operating stores. Start-up costs are also likely to be lower if a business is using online distribution only. The cost of processing transactions is probably lower – many systems are automated and less paper is needed for documents, such as invoices and receipts. Payments can be made and received online using credit cards or a money transfer system like Paypal – they do not need to wait for cash. Finally, a business can serve their customers 24/7 – that is, they are open all the time.

However, there are one or two drawbacks. Businesses will face increasing competition since selling online is a relatively cheaper method of distribution and can be organised from any location in the world. Consequently, businesses will face more competition from overseas. There is also a lack of human contact which might not suit some customers and there is heavy dependence on delivery services where online retailers often lack control on the quality of delivery. There may also be technical problems online. For example, websites may crash, viruses may be used to attack services and internet connections can be unreliable. Finally, there is also a security risk as computer hackers might gain access to sensitive information. An individual business must assess whether the advantages outweigh the drawbacks before setting up an online selling operation.

EXAM PRACTICE

UNILEVER

(a) Define wholesaling. (2 marks)

Wholesaling involves linking manufacturers with retailers. A wholesaler is a business that buys goods from manufacturers and sells them in smaller quantities to retailers. Wholesalers help to break bulk and provide a storage facility to manufacturers. Unilever uses a range of distribution channels, one of which is wholesalers.

(b) Explain one reason why Unilever uses door-to-door selling in emerging economies, such as India. (4 marks)

Unilever uses a number of distribution channels, one of which is door-to-door selling. Unilever uses small-scale retailers in door-to-door selling to distribute goods in hard-to-reach places. Unilever may use this approach in emerging countries such as India, Vietnam and Sri Lanka because there is a lack of other retail outlets, particularly in isolated rural regions. In emerging economies, there is often a lack of infrastructure, even though large regions might be populated by large numbers of people. An organised network of door-to-door sellers is more able to distribute goods to these customers.

Door-to-door selling in developing countries might also improve Unilever's image, by providing job opportunities, recruiting and training people to become part of Unilever's sales network. This can involve providing them with extended credit, marketing, sales and accounting training and bicycles or other equipment. For example, Shakti, Unilever's door-to-door selling operation in India, provides work for 65 000 women in poor rural communities. Similar schemes are used in Bangladesh, Sri Lanka and Vietnam.

(c) Explain one reason why online selling might be an unsuitable distribution channel for Unilever. (4 marks)

Currently Unilever does not target online shoppers as a means of distribution. One reason for this might be because it is not cost effective. Unilever makes fast-moving consumer goods in huge quantities and ships them to over 190 countries around the world. It sells to a mass market: probably over a billion people worldwide buy its products. Distributing low-value goods, such as Knorr stock cubes or packets of Surf laundry powder, to individual customers online would not be cost effective. It is far better for Unilever to distribute through retailers, wholesalers and other similar methods.

(d) Assess the factors that might influence a business like Unilever when choosing distribution channels. (10 marks)

The channel of distribution chosen by a business will depend on a number of factors. One of the most important factors is the nature of the product. Different types of product may require different distribution channels.

For example, businesses producing high-quality 'exclusive' products, such as perfume and designer clothes, will choose their outlets very carefully. The image of their products is important, so they are not likely to use supermarkets, for example.

Some products need an explanation or demonstration. For example, technical products or complex financial products might need to be sold by expert salespeople. These products are likely to be sold by specialists.

Fast-moving consumer goods, such as breakfast cereals, confectionery, crisps and toilet paper, cannot be sold directly by manufacturers to consumers. Wholesalers and retailers play an important role in the distribution of these goods because they break bulk. This is the case with Unilever. Unilever

produces millions of products a day and has to reach, possibly, over a billion customers worldwide. As a result, it uses a range of wholesalers, distributors and retailers.

Businesses will naturally choose the cheapest distribution channels. They will also prefer direct channels because, each time an intermediary is used, they will take a share of the profit. Large supermarkets will try to buy direct from manufacturers because they can bulk buy and get lower prices. Independents are more likely to buy from wholesalers, and have to charge higher prices as a result. Unilever does sell directly to large supermarket chains, but it does not sell directly to final consumers. It is not practical to do so.

Producers selling to mass markets are likely to use intermediaries. Businesses targeting smaller markets are more likely to target customers directly. For example, a building contractor in a small town will deal directly with customers. Producers selling in overseas markets are likely to use agents because they know the market better. Businesses selling goods to other businesses are likely to use more direct channels. In this case, Unilever is selling into a mass market and therefore often requires the services of intermediaries, such as wholesalers.

For some producers, it is important to have complete control over distribution. For example, producers of exclusive products do not want to see them being sold in 'downmarket' outlets. This might damage their image. Most of the products sold by Unilever are directed at mass markets, so image is probably not a priority.

Unilever's priority would be to ensure that everyone has easy access to its products. However, Unilever would not want to be associated with disreputable links in the distribution chain so it would probably monitor distribution channels carefully.

It should also be noted that Unilever, like many businesses, uses a combination of different channels. This helps to widen the distribution network and reach a larger number of potential customers. The most important factor for Unilever is that it sells lots of relatively low-value products to a mass market. It therefore needs a blanket distribution approach using any channel that is cost-effective.

14 APPROACHES TO STAFFING

ACTIVITY 1

CASE STUDY: W. L. GORE & ASSOCIATES

1. Describe one piece of evidence that could suggest that W. L Gore & Associates treats its staff as assets.

Employers who view their staff as assets will value their employees and have concern for their welfare. Such employers will therefore try to meet the needs of employees. In this case, staff, who are called 'associates', receive some attractive benefits. For example, after one year of service staff are entitled to 21 days paid holiday, four weeks unpaid long-term holiday, 35 days fully-paid maternity leave, 3 days paternity leave and 10 days paid sick-leave. On many of the company's sites there are a range of health benefits, such as free breast cancer testing, flu vaccinations, medical facilities and fitness centres. Employees seem very happy working for Gore. Over 18 per cent of staff have been employed for more than 20 years. Few would leave tomorrow if they were offered a job elsewhere. Indeed, staff turnover is well below the global average. Also, according to Figure 1, 91 per cent of staff say they are proud to tell people they work for Gore and 97 per cent of people say that Gore is a physically safe place to work.

Employees are trusted by Gore and, provided associates fulfil their work commitments, there are no set hours of work. Employees are in complete control of their own working day and week (apart from a small number who are required for specific tasks). For example, staff can opt for flexible working, home-working, 4-day working weeks, job sharing and gradual retirement. This suggests that staff at W. L. Gore & Associates are treated as assets – both valued and trusted.

2. Explain one advantage to W. L. Gore & Associates of treating their staff in this way.

Staff appear to be very loyal to W. L. Gore & Associates. Over 18 per cent of staff have been employed for more than 20 years. Few would leave tomorrow if they were offered a job elsewhere. Indeed, staff turnover is well below the global average. With such a low staff turnover, Gore will not need to meet the expense of constantly recruiting new staff when people leave.

The business will also benefit from having a highly motivated workforce. Since staff are valued and trusted they should be happier and more productive. They are given a lot of freedom and encouraged to work in teams. They are allowed to organise their own working patterns and can choose from a range of different working arrangements. This allows them to fit in work with their family and personal lives. There will be a lot of interaction between staff which should help innovation –crucial in the technology sector

ACTIVITY 2

CASE STUDY: PART-TIME WORKING

1. Define a part-time worker.

Part-time workers are defined in *Economic and Labour Market Review* as 'people normally working for not more than 30 hours a week except where otherwise stated'. Part-time workers are employed permanently but work fewer hours than full-time staff.

2. Explain why the proportion of part-time workers varies so much around the world.

Some people prefer to work part-time because it suits their lifestyle. For example, many students take part-time jobs to help support themselves while at college. The proportion of people working part time varies significantly around the world. According to Figure 2, it varies from 1.9 per cent of the workforce in Bulgaria, to 38.5 per cent in the Netherlands. The three countries with the lowest proportion of part-time workers are all in Eastern Europe – Bulgaria, Russia and Poland. Therefore, according to this very small sample, there may not be a culture of part-time work in this region compared to other parts of the world.

Part-time work is most popular in the Netherlands and is particularly popular with women. According to *The Economist* around 76.6 per cent of Dutch women of working age spend less than 36 hours per week working. One reason for this Dutch preference is women arriving late to the labour market. Also, the influence of Christian values in Dutch politics made it a cultural norm for those women to work part time so they could still fulfil traditional family roles. The Netherlands is often reported to be one of the happiest countries in the world. According to surveys, one of the reasons for this is because a high proportion of people only work part time.

3. Explain one reason why businesses employ part-time and temporary workers.

Many businesses like to employ at least a proportion of their workforce on part-time contracts. The use of part-time staff provides flexibility for businesses. For example, part-time staff can be employed during peak hours in restaurants at weekends, for example. This practice helps to keep wage costs down. Temporary workers are those employed for a limited period only. Many businesses need temporary workers from time to time. For example, farmers need workers to help out during the busy harvest period.

With the added flexibility that employing part-time and temporary workers brings, businesses can expand and contract in response to changes in demand for its products. In contrast, a workforce made up entirely of full-time staff is difficult to shrink quickly because of the cost, and because of the time it takes to fulfil legal requirements.

ACTIVITY 3

CASE STUDY: SOUTH AFRICAN CABIN CREW STRIKE

1. What has led to the breakdown in the employer/employee relationship in this case?

In this case, a dispute has developed between the South African Cabin Crew Association (SACCA), which represents cabin crew workers, and South African Airways (SAA). The breakdown in the relationship has occurred because the demands of cabin crew workers were not being met. They wanted their meal allowances on international flights to be increased from US\$130 (ZAR 1699) to US\$170 (ZAR 2217). The workers claimed that they needed the increase to pay for meals when they get to destinations where the living conditions are not the same as those in South Africa.

2. Discuss the possible disadvantages to SAA of collective bargaining.

Collective bargaining involves determining wages, conditions of work and other terms of employment through a negotiation process between employers and employee representatives such as trade unions. These bodies represent the views of their members and try to negotiate in their interests. There are both advantages and disadvantages of this approach to determining wages and conditions for a business. One problem is that negotiations can result in more bureaucracy and take longer, which will add to costs for the business. Negotiation processes can be particularly lengthy if the two bodies are unable to reach an agreement. Another problem is that the owners of a business may feel that their freedom to manage is compromised. In this case, SAA had to cancel 32 flights, which would have inconvenienced customers and lost the company revenue and possibly some goodwill. Finally,

another disadvantage is that disagreement during collective bargaining can lead to a strike. This is the problem here. Cabin crew workers belonging to SACCA wanted an increase in their meal allowance, but this led to a dispute between SAA and SACCA. The strike lasted for a day and was ended by a court ruling. However, a spokesperson for SAA said after the court hearing, 'We are inviting SACCA back to the negotiating table as soon as possible and would like parties to have open minds when deliberating and considering options. It is in the interests of all parties to find lasting solutions to the issues in dispute. We remain confident that a final solution to this matter will be found in the coming days.' This suggests that collective bargaining may resume and a settlement eventually reached.

EXAM PRACTICE

SCHLOSS POWER TOOLS

(a) Define redundancy. (2 marks)

Most people leave a job because they are moving on to another job or because they are retiring. However, some people are forced out of work. They may be dismissed or made redundant. If a worker is made redundant it means they are no longer required because there is either no work or insufficient work. Making people redundant is a lawful means of laying off staff.

(b) Explain one advantage to workers at Schloss Power Tools of multiskilling. (4 marks)

Multiskilling means that workers are trained in more than one specific skill. Schloss Power Tools proposes to train workers in all aspects of production work. This will allow them to move from one workstation to another more easily. The main benefit of this to the employees is that they will develop a greater range of skills, so they will be more capable and can demand higher levels of pay. Also, workers leaving the company may find it easier to get other jobs because they have more to offer and will have more jobs to choose from. Additionally, the chance to do different jobs in the factory might make work more interesting, which could improve levels of job satisfaction.

(c) Explain one possible drawback to Schloss Power Tools of outsourcing the production of some components. (4 marks)

Outsourcing involves getting other people or businesses to carry out tasks that were originally done in-house. This allows a business to focus on its core capabilities and lets others, who are likely to be specialists, carry out peripheral work.

Schloss Power Tools is planning to outsource the production of some components to a Chinese supplier to save €1.5 million per year. This would result in the loss of 12 jobs at the company and may provoke a reaction. For example, there could be a dispute between employees (or their representatives) and the directors, which could escalate and result in a strike with major disruption. Other drawbacks include loss of control and the reliance that Schloss Power Tools will place on suppliers. For example, if the Chinese suppliers fail to deliver on time, the whole production process could be held up.

(d) Evaluate whether (i) training production staff or (ii) employing more temporary workers would have the most impact on improving worker flexibility. (20 marks)

Increasingly, businesses are looking to improve the flexibility of their workforces. In this case, Schloss Power Tools has made two key proposals to help improve flexibility. The directors hope to make the business more competitive and start making a profit again.

One of the main advantages of a flexible workforce is that it can cope more effectively with changes in demand. For example, Schloss Power Tools plans to make more use of temporary workers during the spring and summer when demand for its power tools rises. A workforce made up entirely of permanent staff is less flexible here. To slim down a workforce when demand falls – in the autumn and winter in this case – can be difficult because of the cost and time it takes to comply with legal requirements. Schloss Power Tools might also benefit if employing temporary workers is cheaper.

Schloss Power Tools' proposal to train its workers in a variety of production skills will improve flexibility. People can be moved more easily from one workstation to another, and the business will be better able to cover for absent staff, allowing more labour resources to be directed where they are needed most. Schloss Power Tools is also introducing flexible hours in the company office, so the business will be able to communicate with suppliers, customers and other stakeholders from 7.00 a.m. to 8.00 p.m. each day. This should help to improve customer service.

Despite these advantages, there may be some drawbacks for Schloss Power Tools. For example, some workers may not want to become multi-skilled, because they prefer their jobs as they are or lack the confidence to learn new skills. This could cause a dispute between employers and employees and damage the relationship that might exist.

Some office staff may object to the new flexible hours. There may be a problem getting staff to start earlier and stay later, which could also lead to a dispute.

To conclude, the directors are expecting a negative reaction from the workforce when the proposals are announced. Therefore, they have agreed to increase wages by the CPI (cost of living) plus 1 per cent for the next 3 years. This should help to temper the reaction.

Overall, Schloss Power Tools needs to do something about its loss-making position, and it believes that a flexible workforce is part of the answer. It is difficult to say whether the training of production staff or the use of temporary workers will have the biggest impact. If workers can master a wider range of skills, the benefit to Schloss will be significant. Workers will be more skilled and production would not be held up if a number of workers in the same field of production were absent. Workers might also be more motivated if they recognise that their employer has invested money in their training. However, training is expensive and Schloss will need to compare the costs of training with the benefits.

The use of temporary workers will help deal with higher levels of demand in the summer. However, temporary workers may not be as reliable as full-time staff. Perhaps a better approach would be to offer overtime rates to existing staff. This gives them the opportunity to earn more money and may help to motivate them. Therefore, it could be argued that the training of the production staff would have the most impact on improving worker flexibility.

15 RECRUITMENT, SELECTION AND TRAINING

ACTIVITY 1

CASE STUDY: JOB DESCRIPTION

1. Explain what is meant by a job description, illustrating your answer with examples from Figure 4.

A job description states the title of a job and outlines the tasks, duties and responsibilities associated with that job. The main purpose of a job description is to show clearly what is expected of an employee. Extracts from it are likely to be used in a job advert, like the one shown in Figure 4.

In Figure 4, the job description is for a Grade 1 accounts assistant. The job involves helping out the accounting team recording financial transactions and generating financial information.

Some specific responsibilities include matching, batching and the coding of invoices, investigating aged debtors, allocating cost codes, matching invoices to purchase orders and arranging payments on behalf of the company.

The job description specifies the pay range for the job, which is between US\$24 500 and \$29 000 a year, depending on experience, and it shows that there is an entitlement of 21 days annual holiday.

If a new job is created, a new job description may have to be prepared. If a business is replacing someone who is leaving, the job description may be the same. However, when someone leaves, the job description may be updated.

ACTIVITY 2

CASE STUDY: JOB ADVERTISEMENT

1. Explain one benefit of using external recruitment for The Aspire Park Fitness Centre.

One of the main benefits of external recruitment is that the business will attract a far larger number of applicants compared to internal recruitment. This means that the employer will have a lot more choice when making an appointment. It might also mean that better-quality applicants can be attracted. Additionally, an external candidate might bring some fresh ideas into the business.

2. Discuss the suitability of using a local newspaper to advertise the job shown above.

Businesses often use local newspapers to recruit staff. In this case, a health club is trying to attract some fitness coaches. Using an advert in a local newspaper means that most of the applicants will be from the local area. The business might prefer this because it might think its members would prefer to be coached by a local instructor. Also, local employees might be more reliable because they do not have to travel so far to get to work. Local staff might provide the business with more flexibility: for example, the business might be able to call in local staff to help out at short notice.

ACTIVITY 3

CASE STUDY: HONDA

1. Describe two possible training costs that Honda might incur providing its apprenticeship programmes.

Training costs can be very high for businesses. For example, employees often have to be trained in health and safety issues by law. Businesses may have to pay training providers if they use external training. Even internal training can be expensive if specialist training staff and equipment is needed. In this case, Honda appears to take training very seriously and has invested heavily in training facilities. Honda has purpose-built technical training centres, with practical workshop areas and individual training rooms. Apprentices receive lots of support, using the latest equipment, in a safe and supervised environment. The Honda Institute Centre of Excellence has classrooms, computer rooms, offices and a canteen. There is also a 'Wow Door'. This opens out onto a viewing gallery where you can see a huge space containing all the latest Honda products and technology that is used solely for learning. All of these facilities will incur heavy expenditure.

Young people joining the programme work alongside experienced staff. Some of them will be specialised trainers. The wages of these employees will have to be met. Finally, trainees are paid by Honda even though they are not making any contribution to output during their period of training. This is another cost.

2. Explain one reason why some businesses may be reluctant to invest in training.

Businesses are often reluctant to invest in training because of the high costs outlined in the previous answer. Some firms may lack resources to fund training. They may consider that the opportunity cost is unacceptable. As a result, resources are used for other expenditures. Some businesses are reluctant to invest in training because they fear that once an employee has been fully trained, they may leave the business and take a job with a rival. Consequently, the benefit of any training is enjoyed by another business. Although Honda is prepared to invest in training, it is possible that some apprentices leave and find jobs with other motor car companies, for example.

3. Honda apprentices receive a lot of off-the-job training. Assess the advantages and disadvantages of off-the-job training.

Off-the-job training is training that takes place away from production facilities. In this case, Honda trains apprentices in purpose-built technical training centres, with practical workshop areas and individual training rooms. Apprentices receive lots of support, using the latest equipment, in a safe and supervised environment. The Honda Institute Centre of Excellence has classrooms, computer rooms, offices and a canteen.

One of the advantages of off-the-job training is that trainees cannot be distracted by the work itself. They can focus entirely on learning the skills and knowledge required. Also, the quality of output is not affected by trainee mistakes as they learn, and customers and others are not put at risk. It is also possible for off-the-job training to take place outside normal working hours – in the evenings perhaps.

There are disadvantages of off-the-job training. Trainees do not produce any output so there will be a loss of potential revenue. Off-the-job training can also be very expensive as outlined in the previous answer. The expense may reduce the profitability of the business. It is also possible that some aspects of the work cannot be taught off-the-job and trainees may feel that some of the training is not relevant to them. However, for many businesses such as Honda, the benefits of high-quality off-the-job training outweigh the drawbacks and therefore investment in this method is justified.

EXAM PRACTICE

MILANO IL MIGLIORE (MIM)

(a) Explain one reason why recruitment is such an important activity for MIM. (4 marks)

Recruitment involves attracting and appointing new staff. A business may need new staff because it is expanding and more labour is needed, or perhaps people are leaving and they need to be replaced. Recruitment is important because a business needs high-quality staff. The quality of staff in a business can have a big impact on its financial performance. Poor-quality staff can lead to low productivity, poor customer relations and a negative culture in the organisation.

Recruitment is also important because a poor choice of recruit can prove to be expensive. If new recruits leave, all the costs of advertising, interviewing, induction and training will have to be repeated.

(b) Explain how MIM attempts to overcome the problem of recruiting sufficiently high-quality staff. (4 marks)

When businesses hire new employees they need to attract the best people: those with the right skills and appropriate experience. Attracting poor-quality staff can have a negative impact on a business, so it is important to develop an effective recruitment process.

MIM uses an online system to help recruit staff. The whole recruitment process involves three stages. Applicants apply online and, if successful, are invited to complete a test, also online. If they pass the test, they are invited to an online video interview. Finally, if they pass the online interview they are invited to group interviews at local stores, where their suitability for employment is finally assessed.

This is a rigorous process and candidates have to pass many stages to be successful. This thorough examination of candidates' suitability helps MIM to recruit high-quality staff.

(c) Discuss the benefits of online recruitment to MIM. (8 marks)

A significant part of MIM recruitment process is conducted online. Jobs are advertised online (on the company's website) and candidates submit their application, complete a test and carry out a video interview – all online. This system helps MIM to filter applicants, assess personalities and screen applicants to see if candidates match the company's values and culture.

One of the main advantages of online recruitment is that applicants can be drawn from a much wider area – globally if necessary. It is also possible to attract specialists. MIM uses its online system to recruit buyers, merchandisers and designers. Not only does this allow employers to find candidates with specific skills, but also it can attract passive candidates who may not be actively looking for employment. For example, someone browsing the MIM website might be attracted to the recruitment section, even if they were not looking for a new job.

The cost of using the internet to recruit staff is low compared with other methods. It has been reported that the costs of posting jobs or searching for candidates on job portals can be up to 90 per cent lower than the costs of using traditional methods. Online recruiting involves less human interaction, reaches a far broader audience, files records and provides selection tools electronically. This reduces the cost for storage, as well as the cost of employees to maintain and administer recruitment and selection procedures.

The benefits to MIM of using online recruitment are significant. The company has set up a system that is ongoing, cheap, easy to use and effective. It is likely MIM saves a great deal of money using the system, and that the quality of staff recruited is generally very good.

(d) Assess the importance of training to a business like MIM. (10 marks)

Although training can be expensive, the benefits generally outweigh the costs. Training appears to be important for MIM. The company has its own training programme for graduates. MIM claims that the training and development opportunities provided are revered across the industry. New recruits at MIM start with an introduction to the whole of the business, so that recruits understand the overall objective

of the business before delving into the detail of their specific business area. Recruits are paired with more experienced staff members so that they have all the support they need. By offering numerous training opportunities and encouraging their recruits to learn from colleagues, MIM encourages promotion in less than two years.

Although it is expensive, a number of stakeholders will benefit from training. For example, managers at MIM will benefit because workers may be better motivated and more satisfied. This makes them more co-operative and easier to work with. Workers may also be more flexible which will help managers in their organisation. Providing training may also improve the image of the business and make it easier to attract and retain high-quality staff. MIM shareholders will also benefit from investment in training if productivity improves. Higher levels of productivity mean that costs will be lower, and the business might gain a competitive edge in the market. This should help to improve the financial performance of the business leading to higher profits and dividends for the owners.

Training will also benefit workers. When they have been trained, they will be able to do their jobs more effectively. This should reduce anxieties about their work and provide more job satisfaction. Additionally, employees are likely to feel valued if their employer is paying for their training; they might be more motivated, less stressed and enjoy higher levels of job satisfaction. They might also develop a range of skills that they can use in the future – to gain internal promotion or perhaps seek a better job.

If training improves the quality of workmanship, customers will benefit from better-quality products. Also, if staff members who interact with customers are given training in customer service, customers will benefit from improvements, such as a better service when making complaints.

With so many benefits from investment in training, it could be argued that training is very important to businesses like MIM. However, training costs are significant. For example, businesses will have to pay training providers if they use external training. Even internal training can be expensive if specialist training staff and equipment is needed.

If workers are involved in off-the-job training, they will not be contributing to the company's production/output. This will result in lower output levels. Even if workers are trained on the job there may be a loss of output due to mistakes and slow work associated with 'learners'.

Finally, businesses are likely to get frustrated if employees leave and join a rival company after they have invested in training them. Some businesses actually prefer to recruit workers who have already been trained by others to avoid such costs. However, companies like MIM presumably believe that the costs of training are outweighed by the many benefits.

16 ORGANISATIONAL DESIGN

ACTIVITY 1

CASE STUDY: CHATUCHAK TEXTILES

1. What is the span of control for the manager of Line B?

The span of control for the manager of Line B is three. The manager has responsibility for three supervisors.

2. Using Figure 3, describe the chain of command at Chatuchak Textiles, from the chairperson to the machinists working on all lines.

The chain of command in a business is the path along which orders are passed down through the hierarchy. In this example, an instruction from the chairperson would pass to the managing director, then to the production manager, and then on to the three line managers. Each line manager would pass the instruction on to their respective supervisors, who would then inform the machinists under their control.

3. Explain one reason why the business might produce an organisational chart.

A business is likely to produce an organisational chart to help clarify the organisational structure of the business. Organisational charts help to show the roles of different employees and their job titles, the route through which decisions are made, who is responsible, and who is accountable to whom and for what activities. A chart will also show the relationship between positions in a business, how employees communicate with each other and how information is passed on.

In this case, Figure 3 shows part of an organisational chart for Chatuchak Textiles. It includes the production function, which is responsible for operating three different production lines. The extract from the chart shows the roles of employees and their job titles. For example, in this case there are machinists, their supervisors, a line manager, a production manager, a managing director and a chairperson.

The chart also shows who has responsibility and to whom people are accountable. For example, the machinists are accountable to their line supervisors and the line supervisors are accountable to the line managers.

Finally, the chart shows the relationships between different positions in the business. For example, the managing director provides a link between the chairperson and the functional managers.

ACTIVITY 2

CASE STUDY: VMWARE INC.

1. Define decentralisation. Use the example in this case to illustrate your answer.

Centralisation and decentralisation refer to the extent to which authority is delegated in a business. If there was complete centralisation, subordinates have no authority at all. In contrast, complete decentralisation would mean that subordinates would have all the authority to make decisions. In some organisations, it is common to centralise certain functions. For example, purchasing and IT may be centralised. In this case study, it is reported that many businesses are beginning to decentralise IT. This means that businesses are allowing non-specialists, such as production managers and marketing staff, to make IT decisions for themselves. This means, for example, that IT systems may be purchased to suit the needs of individual departments in an organisation.

2. Explain why IT departments are unlikely to support the decentralisation of IT.

IT departments are unlikely to support the decentralisation of IT in their organisations. This is probably because their workload and responsibilities will be reduced and their positions might become redundant. According to information the case study, 70 per cent of IT managers said that IT should be more centralised, and 79 per cent argued that they should be in control of core functions like network security and compliance. Furthermore, 46 per cent said that IT disaster management was too important to be decentralised and 39 per cent said that data storage should also be their responsibility. This suggests that the business as a whole may not benefit from the decentralisation of IT.

3. Assess the possible impacts of the decentralisation of IT on businesses.

One of the main advantages of decentralisation is that it empowers and motivates workers. In the research carried out in this case, it was found that the decentralisation of IT had contributed to reduce employee turnover. For example, 53 per cent of respondents said that employee satisfaction had improved. This is because workers may have been given more responsibility in decision making. Decentralisation can also improve flexibility in an organisation and speed up decision making. For example, in this case, 56 per cent of respondents in the research carried out said that they were able to develop and launch new products more quickly, and 63 per cent said that there was more freedom in their organisations to drive innovation. This will help businesses to gain a competitive edge in the market. Another possible benefit is that IT managers will have more time to focus on more strategic issues. Their workloads will be reduced and there will be less stress for IT staff.

However, there may be some drawbacks to decentralisation. In this case there will be a loss of control from IT experts over IT developments in businesses and a possible loss of efficiency. For example, 63 per cent of business leaders said that decentralisation was leading to some IT resources being constructed more than once and 62 per cent said that accountability was becoming a problem. Also, 59 per cent said that in some cases, unsecure solutions were being purchased. Seventy-nine per cent of IT managers argued that they should be in control of core functions like network security and compliance. Sixty-four per cent said that IT disaster management was too important to be decentralised and 39 per cent said that data storage should also be their responsibility.

To conclude, although businesses are looking to innovate, improve efficiency and find ways of competing in an increasingly dynamic business environment, it is important to embrace new methods of IT management cautiously. According to a spokesperson for VMware 'Too often, we're seeing this trend (decentralisation of IT) left unchecked and without adequate IT governance, meaning that organisations across Europe, Middle East and Africa are driving up costs, compromising security and muddying the waters as to who does what, as they look to evolve.' This suggests that the decentralisation of IT may be beneficial but should be managed in a systematic and controlled way. This will help to avoid serious problems developing.

EXAM PRACTICE

VALVE

(a) Define a flat organisation structure. (2 marks)

Some organisational structures are flat. This means that there is a small number of layers in the organisational structure. In this case, Valve is an exceptional example of a flat structure. There is only one layer in the organisation chart. There are no managers and all staff have equal status. According to one Valve employee, D. J. Powers, he doesn't report to anyone and no one reports to him. With flatter structures, the chain of command is short but the span of control is wide. This type of structure means that employees are free from strict, close control in the workplace. They have more freedom and responsibility. This is certainly the case at Valve.

(b) Evaluate whether or not Valve will benefit from having a flatter organisational structure. (20 marks)

In common with a number of technology businesses, Valve has a flat organisation. However, many would regard the organisation of Valve as unusual. There are no managers and all staff have equal status. Employees can sit where they want, work on whichever project they choose and even decide their colleagues' pay. Also, once a year they all go on holiday together. According to one Valve employee, D. J. Powers, he doesn't report to anyone and no one reports to him. He says 'We're free to choose to work on whatever we think is interesting. People ask you questions about what you are working on. And the response is not to get defensive but to have that conversation and make sure that we're all invested in each other.'

There are some benefits of flatter structures. With flat structures, communication is better because the chain of command is short. Communication may be quicker and there is less scope for messages to be distorted. For example, in a tall structure, a message from a store manager might say 'Can you ask Marion if she would like to work an extra 4-hour shift on Sunday.' But by the time it has been passed through all seven layers in the hierarchy, Marion might receive a message which says 'The manager said you have got to work an extra shift on Sunday morning.' Clearly, these two messages have very different tones. In the case of Valve, such messages are not needed. This is because employees are responsible for their own working arrangements. Employees do not have to report to anyone and they are free to move around the workplace and communicate directly with anyone they choose. Communication will be direct and there is no chain of command through which messages would pass.

With flatter structures, management costs are lower because there are fewer layers of management. Decision making may be quicker because approval from several managerial layers is not required. Also, employees may be better motivated because they are less closely controlled. Indeed, in many flat structures employees are empowered. They have more responsibility for organising their work and may be allowed to solve their own problems. This can help to make their work more interesting. One employee at Valve said 'I think the fact that we're not managed by people and we're not managing people and you're able to formulate your own ideas and work with whoever it is to come up with a project or feature – that's empowering.'

Academics that have studied the effectiveness of flat organisations reckon that one of the main reasons why they work is because they encourage staff interaction – dialogue and information sharing. They also attract high quality staff or 'elite performers' as one academic put it. However, Powers suggests that the structure works because it was the way the organisation was originally designed. It has always been like this. He also says that it might be a mistake to try and introduce such a flat structure in an organisation that has traditionally been hierarchical.

However, there are some drawbacks with flatter structures. Managers may lose control of the workforce because the span of control is too high. As a result, discipline may be lacking which could have a negative impact on productivity. There could also be co-ordination problems if managers are

responsible for too many subordinates. In the case of Valve there does not appear to be problems of this nature. However, if the company encountered some problems and performance dipped, a lack of managerial direction might make the situation worse. Some employees might need guidance and support from senior members of staff during a crisis, for example.

In this case, the flat organisation structure used at Valve appears to be effective. Valve is a privately-owned company so details about its revenues and profits are not widely distributed. However, it is reckoned that its most popular product, Steam, controls between 50 and 70 per cent of the US\$4000 million downloadable PC games market. It has also been reported that Valve generates higher profits per employee than both Apple and Google. This provides some evidence to suggest that a flat structure works well for Valve.

17 MOTIVATION IN THEORY AND PRACTICE

ACTIVITY 1

CASE STUDY: UJJIVAN FINANCIAL SERVICES

1. Explain one reason why motivation is important to a business like Ujjivan.

Businesses will gain a lot if their workforce is motivated. Generally, people will be happier, easier to manage, more productive, more cooperative and more open to change. In this case, the CEO at Ujjivan understands the importance of a well-motivated workforce. He believes that customers can only be happy if the employees are happy. Ujjivan treats employees as important stakeholders. Consequently, if the workforce is happy, the quality of service that customers receive will be better. This means that it will be easier for the business to retain existing customers and attract new ones. This will help to generate more revenue and profit for Ujjivan.

2. Identify two of Herzberg's hygiene factors at Ujjivan.

Herzberg discovered that certain factors at work would help to give employees job satisfaction, which he called motivators. He also found that other factors can leave workers dissatisfied. He called these hygiene factors. In this case it would appear that Ujjivan offers staff a number of benefits that could be described as hygiene factors. For example, all employees are offered the chance to buy esops (stock options for employees) depending on performance. Employees are also required to take 10 unbroken days of holiday each year – this is in addition to their casual leave. The company believes that staff need time in addition to regular leave to reconnect with themselves and their families. Female employees also have access to free crèche facilities. This helps new mothers when they return to work. Such benefits should help to keep levels of dissatisfaction low at the company.

3. Explain one factor that will help to motivate staff at Ujjivan according to Herzberg.

According to Herzberg, motivators include sense of achievement, chance of promotion, chance of improvement, recognition of effort, responsibility and the nature of the job itself. In this case, one thing appears very clear. Staff enjoy working for the company and they are motivated by the job itself. One of the main reasons why employees think Ujjivan is a great place to work is because the work itself is interesting and satisfying. For example, one employee, management associate Mantasha Mizaj, says that the best thing about working for Ujjivan is the excitement and energy that you get from working with such a young workforce, combined with the opportunity to work with experienced seniors. She also enjoys the meaningful social work that the job involves. It drives her enthusiasm to be part of Ujjivan. In 2016, the company was ranked third among the top 25 companies to work for in India by the Great Places to Work Institute in partnership with *The Economic Times*. This supports the view that staff are well motivated and enjoy their work.

ACTIVITY 2

CASE STUDY: PAID BY OUTPUT

1. Explain the payment system used in this case.

Some workers are paid according to how much they produce. This system is called piece rates or piecework. In this example, the machinist is likely to be paid according to the number of garments completed during a shift. For example, if the employee is paid £0.40 per garment and makes 160 garments in an 8-hour shift, the employee will receive £64 for the shift (£0.40 × 160).

2. Explain which motivational theory this payment system might be based on.

The main benefit of piece rates for businesses is that it rewards productive workers. Workers who are lazy or slow will not earn as much as those who are conscientious and productive. This system helps to motivate workers and businesses are likely to 'get more' out of their employees.

This payment system might be based on Taylor's theory of scientific management. Taylor suggested that, once the 'best way' to carry out a task had been identified, workers should be paid according to what they produce. He reckoned that people should be paid 'a fair day's pay for a fair day's work'. He said that people are motivated mainly by money, and would work harder to earn more.

3. Explain one possible disadvantage of this method as a means of motivating machinists.

Although piece rates reward workers who are conscientious and productive, the system of payment has its problems. For example, the quality of output may suffer if people work too fast. They may take short cuts and make mistakes. In this case, the quality of stitching might be poor – a machinist might not sew in a straight line, for example, which could spoil the appearance of the garment. Also, workers might use dangerous practices as they try to work fast. For example, machinists may remove protective guards to speed up production and therefore risk injury.

ACTIVITY 3

CASE STUDIES: PRP IN FOOTBALL

1. What is performance-related pay?

Performance-related pay (PRP) is a pay system designed specifically to motivate workers. Introduced in the 1980s and 1990s, it is used in a number of countries around the world to pay white-collar workers, such as bankers and other employees in financial services. PRP gives workers extra pay for achieving work-related targets. The extra pay may be a fixed sum or it could be a percentage of a salary. Some PRP systems make distinctions between levels of achievement. For example, one employee's performance might be rated as 'excellent' and therefore entitled to a 10 per cent bonus. Another might be rated as 'good' and receive a 5 per cent payment. In this case, footballers at some clubs are receiving remunerations with a lower basic pay and a larger variable element linked to performance.

2. Explain one reason why football clubs are introducing performance-related pay.

An increasing number of football clubs around the world are making more use of PRP in their organisations. One reason for this is to avoid a situation where a highly expensive player ends up 'seeing out' his €50 000 a week contract (for example) by playing in the reserves or sitting on the substitutes' bench. This might happen because he suddenly loses form or because the player was purchased by a manager that has now been replaced. This is clearly wasteful for a football club and it is also something that irritates supporters. The introduction of performance-related pay in football should help to reduce costs and improve motivation. It will reduce the amount paid to footballers who fail to perform.

3. Explain one possible problem of using performance-related pay to reward footballers.

In football, there are two main approaches to determining PRP. One is to reward individuals for their contributions on the pitch – individual bonuses for goals scored, the number of ‘assists’ or the number of ‘tackles’ won, for example. There is a problem here though. Historically, the analytical tools used to measure player performance lack sophistication. They are not able to reward players without affecting their conscious decision making during games. For example, goal bonuses encourage players to shoot instead of passing, assist bonuses encourage players to pass instead of shooting, rewarding pass-completion percentage means players will play too cautiously and rewarding forward passes means they will take too many risks. Generally, if players’ incentives are linked to such shallow and one-dimensional measures of performance, they will focus on the numbers and creativity in football will be stifled.

However, the statistical analysis of player performance is improving. One British company, Opta Sports, leads the world in analysing live sports data. It gathers information from 35 different leagues around the world and monitors the games from a live video stream in locations such as London, Leeds, Munich, Madrid, Milan, Paris, Amsterdam, Montevideo and New York. Three analysts are employed per match. One covers the home team, one the away team and a third monitors quality control. For example, when a free-kick is hit into a defensive wall and play continues, the first two will carry on in their individual roles. However, the third person reviews their footage and assigns the block to a player in the wall. A spokesperson said ‘We measure passes by using a mouse over a grid of an overhead view of the pitch and hot keys ... There are 16 different types of pass in our categorisation such as long ball, high ball and through-ball and we’re very clear when it comes to differentiating the various classifications.’

EXAM PRACTICE

KAPLINSKY MARINE

(a) (i) Define profit-related pay. (2 marks)

Some employers link pay to the profit made by the business. This means that all, or part, of the earnings received by employees is linked to the profit for the year. In this case, Kaplinsky Marine links part of employees’ earnings to profit. All staff, after 2 years’ service, receive profit-related pay. In addition to their basic annual salary, employees receive 0.05 per cent of the profit made by the business each year.

(ii) Calculate the annual profit-related bonus per employee in 2017. (4 marks)

In 2017, the annual profit-related bonus per employee is given by:

$$0.05\% \times 35\,500\,000 = 35\,500\,000 \div 100 \times 0.05 = \mathbf{17\,750}$$

(b) Explain one possible drawback of profit-related pay. (4 marks)

Profit-related pay is often used to help motivate staff. It helps to unite the objectives of shareholders and employees. If employees work hard and raise their productivity, the business will make higher profits and their pay will be higher. However, there is one serious drawback with this method as a motivator. The profit made by a business does not solely depend on the efforts of the workforce. Profit levels can be influenced by the decisions made by leaders and management. They can also be affected by external factors such as the state of the economy. If employees work very hard but their company makes a loss as a result of a poor managerial decision, for example, inevitably there will be some resentment and dissatisfaction.

In this case, Kaplinsky Marine make luxury yachts. It could be argued that such products are income elastic. Therefore, a slowdown in the economy could see sales of luxury yachts hit quite hard. This might have a significant negative impact on the earnings of workers at Kaplinsky Marine.

(c) Explain how Kaplinsky Marine uses flexible working to help motivate its staff. (4 marks)

Employing a flexible workforce has a number of benefits for a business. For example, it can cope with fluctuations in demand more easily and extend opening hours. However, flexible working may also help to motivate workers. This is most likely if staff can choose their hours of work, work from home or take lengthy periods of leave, for example. In this case, Kaplinsky Marine offers term-time only contracts, 4-day week contracts and unpaid long-term leave. It has also shortened the hours of some office-based staff in return for extending opening hours from 7.00 a.m. to 7.00 p.m. Office staff work from either 7.00 a.m. to 1.00 p.m. or 1.00 p.m. to 7.00 p.m. They are free to switch shifts to suit their personal needs provided the office is fully staffed for the 12-hour working day. Staff are also encouraged to switch teams and learn new skills – particularly in production. These flexible arrangements are likely to benefit a number of workers and as a result, employees may feel better motivated.

(d) Assess the extent to which Kaplinsky Marine meets the needs of employees as identified by Maslow. (10 marks)

Employees have a range of needs and Maslow argued that businesses could motivate people by satisfying these needs at work. Maslow arranged these needs into a hierarchy and presented them in the shape of a pyramid. At the bottom of the pyramid was the physiological needs of the workforce – needs such as food, shelter, drink and rest. Maslow argued that employers could help satisfy these needs by providing a living wage and good working conditions. In this case, Kaplinsky Marine provide a free breakfast for all employees. Also, in addition to their basic annual salary, employees receive 0.05 per cent of the profit made by the business each year. This arrangement was agreed in 2011 after an employee vote showed 87 per cent support for its introduction. An internal survey also showed that 79 per cent of staff were happy with their remuneration and benefits. This suggests that the physiological needs of workers are being met by the business.

The second level of needs in the hierarchy are safety needs, such as protection from danger, insecurity and other threats. In this case, Kaplinsky Marine appear to meet these needs. For example, 94 per cent felt that their employment at the company was secure. There is nothing in the case to suggest that these safety needs were not being met.

The next level of needs is love and belonging. This means that people want to work with colleagues that support them and get opportunities to communicate with others and perhaps work in teams. In this case, the workforce is divided into teams of around 20. Each team concentrates on a specific process, task or business area. For example, design, hull-making, joinery, assembly, fitting, finishing, administration, marketing and finance. Working in teams will give staff plenty of opportunity to communicate and build up relationships. Kaplinsky also provides a free fitness centre and sports club. This will provide further opportunities for staff to mix and develop friendships.

The second highest level of needs are esteem needs. This means that people want to be given recognition for doing a job well. In a survey at Kaplinsky, 87 per cent felt valued by the company and 88 per cent said that managers/team leaders were supportive and open. Kaplinsky also appreciates the importance of training in the organisation. Every new employee recruited to a team undergoes a 6–12-month training period and is assigned to a mentor – an experienced member of staff with special responsibility for mentoring. Investment in training suggests that the company values its workers and recognises that they have skills which can be developed. This shows that people's efforts are appreciated and also rewarded.

Finally, people like to reach their full potential at work. This is a self-actualisation need. At Kaplinsky the personal development of staff is taken seriously. Ninety-three per cent said the company provided opportunities to reach their full potential and learn new skills. The mentor system used by Kaplinsky was introduced to improve training and enrich the jobs of experienced workers. They are sought-after roles and carry a special allowance. This will help to meet self-actualisation needs.

Evidence in the case suggests that Kaplinsky Marine makes every effort to meet employee needs. Over many years of trading the company has developed a highly skilled and well-motivated workforce. The company has created a team of specialists, each highly qualified within their field and who work with shared passion, enthusiasm and commitment. This suggests that staff here are very well motivated and that their needs, as described by Maslow, are being met by a responsible employer.

18 LEADERSHIP

ACTIVITY 1

CASE STUDY: DA HINGGAN AIRLINES

1. Assess the advantages and disadvantages to Da Hinggan Airlines of employing an autocratic leader.

Wen Ailing has been described as an autocratic leader. This means she makes all key decisions herself and expects her management team to implement them without too much question.

The main advantage of this style is that decisions can be taken very quickly. There is no lengthy consultation and decision-making process, which would use up business resources. This helps to save the business money. This style also allows a business to respond to events quickly. It might give a business a competitive edge if a company can respond quickly to changes in the market place, for example. Autocratic leaders can be overpowering and oppressive, but they can also provide some security for staff, if they believe in their leader.

Evidence of Ailing's authoritative approach was witnessed a few years ago when a cloud of volcanic ash headed towards UK airspace and the government grounded all flights. Ailing said the closure was too lengthy and proceeded to fly Da Hinggan Airlines planes. It was argued that she called the government's bluff and as a result the ban was lifted.

This autocratic leadership style seems to have served Ailing and Da Hinggan Airlines very well. Her decisions have helped to grow the company. Figure 2 shows that, between 2011 and 2015, Da Hinggan Airlines's revenue grew by around 50 per cent, from just under £4000 million to just under £6000 million. When Ailing was appointed she identified that slow decision making was a problem. She felt there were too many levels of management, and too many people had to discuss and approve decisions before change could happen. To stop this being an issue, Ailing took swift action and made 50 people redundant, removing an entire management layer and placing herself closer to key people in the organisation's structure.

However, an autocratic leadership style is often criticised. It is argued that this approach means staff can become too dependent on the leader and that it can lead to low motivation levels. High levels of supervision are then needed to ensure that employees carry out their tasks effectively.

The style can also lead to conflict. For example, there was a fractious dispute between Da Hinggan Airlines and the airline's cabin crew. Although there are no details here, it probably meant that strikes were threatened and employees very unhappy.

To conclude, when Ailing took over at Da Hinggan Airlines, the company was struggling since it appeared that competitors were adapting more quickly to market trends. Today, revenues are rising, and the company's financial performance is improving. In this case, the advantages of autocratic leadership probably outweigh the disadvantages.

ACTIVITY 2

CASE STUDY: WARREN BUFFETT

1. Explain the style of leadership used by Warren Buffett.

Warren Buffett has used a laissez-faire style of leadership – in other words, a more ‘hands-off’ approach. A laissez-faire leader provides others with the proper tools and resources needed, and then backs off. The leader gives little guidance and direction, and allows others the freedom to make decisions.

2. Explain one reason why this style of leadership has been successful at Berkshire Hathaway.

Berkshire Hathaway is a holding company. It owns many businesses in a wide variety of sectors such as confectionery, retail, railroad, home furnishings, vacuum cleaners, jewellery and newspaper publishing, along with several regional electric and gas utilities.

Many of these businesses will have their own distinctive cultures, and each is likely to require a specific managerial approach. Therefore, Buffett appoints a person whom he thinks has the right attributes, skills and experience to run each business, then gives that person complete autonomy and enough resources to meet company objectives. Buffett puts a great deal of trust in his employees, which creates a motivated and energised atmosphere. However, if these employees need guidance or support, Warren is always available for consultation.

3. Assess the possible benefits to Berkshire Hathaway of this style of leadership.

The laissez-faire leadership style seems to have worked very well for Warren Buffett and Berkshire Hathaway. In 2016, the business employed 367 000 people and generated US\$223 604 million in revenue.

One of the main benefits of this style of leadership is that staff members feel trusted and valued. This gives them confidence and helps to motivate them, creating an energised atmosphere. As a result, employees work hard because they feel in control and that their efforts will be recognised.

This leadership approach is most effective when employees are highly skilled, experienced, motivated and capable of working on their own. Buffett has been successful in recruiting such people.

However, laissez-faire leadership is not ideal in many situations. This is particularly the case if employees lack the experience or knowledge needed to complete the tasks or make decisions. Also, some people are not capable of setting their own deadlines or managing their own projects. Some people may lack the motivation they need to get certain tasks done on time. Such people usually need an extra ‘push’ from the leader.

In this case, though, laissez-faire leadership has worked well. The problems outlined have not arisen because the right staff have been appointed.

ACTIVITY 3

CASE STUDY: MENOS DE 10S

1. Discuss two changes that might have occurred in Adriana's business role over the years.

If an entrepreneur sets up a business and it becomes very successful, the role of the entrepreneur is likely to change as it expands. Running a sole trader business with two employees and a modest turnover is a different challenge to running a large plc with hundreds of employees and a huge turnover. The change in role stems from the need to deal with growth. For example, growth in the number of employees, the number and size of financial transactions, the number and size of customers, the amount of regulation and the quantity of resources used.

The transition from entrepreneur to leader is likely to require a number of changes in the way the business is run. This usually means that entrepreneurs have to adapt and perform different functions. For example, there is a need for formality. Small businesses can be run on an informal basis. They employ just a few employees and communication between them can be ongoing since they are likely to be working in close to each other. Decisions can be made quickly because the entrepreneur is always at hand. However, in a large organisation, where the entrepreneur becomes a leader, there is a need for formality. Communication between hundreds of employees requires systems and formal structures. The business is likely to be split up into departments or divisions. There will have to be formal communication channels which are recognised and approved by all staff. There will be a need for a formal organisational structure so that the business can be controlled and employees brought to account. The entrepreneur in a small business will become a chairperson or a senior executive with a leadership role.

Another likely change is the increasing need to motivate the workforce. As the size of the business grows there is a need to focus more on the workforce. This is because there are a lot more people to manage. As entrepreneurs develop into leaders, there is a greater need for motivational skills. Some people are self-motivated but most people need encouragement and well-defined goals that leaders have to provide. Workers are also likely to look to the leader for support and inspiration. Leaders also have to develop the talents of others. In this case, Adriana has tended to employ young and flexible staff, which she has motivated with her warm and enthusiastic brand of leadership.

(b)2. Discuss two problems that Adriana encountered when making the transition to corporate leader.

Adriana is now considered a highly competent leader. However, the transition from entrepreneur to leader was not without problems. Initially she was overwhelmed by the increased responsibility. As an entrepreneur running a small business, Adriana obviously had responsibility to employees. They have needs which must be met. However, as Menos de 10s grew into a chain, the number of people employed rose considerably. The livelihoods of these people will often rest on the decisions made by the leader. This is an enormous responsibility. Adriana may also have had responsibility to other stakeholders such as shareholders, suppliers and customers.

Adriana also had a problem changing expectations of herself. She realised this during a break that she took from running Menos de 10s. Entrepreneurs usually have a desire for greater control over their life, career and destiny. They want more autonomy. They want to do things their own way. However, a different approach is needed when the business grows. Leaders have to give up some control. They have to learn to delegate and focus on different things. They have to believe that specialists will do a better job in certain fields. They cannot do everything for themselves. For some people, this is extremely difficult. They have doubts, fears and a lack of trust, which could create a barrier to development. Fortunately, Adriana eventually realised this and changed her approach.

3. Explain two possible methods of coping with stress.

Running a huge business organisation is challenging and often exhausting. This can cause stress and possibly result in health problems. It is important to reduce stress levels and there are various strategies that can be used to help. One approach is to take regular exercise. Exercise is known to improve your health and general well-being. Exercise also releases chemicals in your body called endorphins. These help to reduce pain and produce feelings of pleasure. Exercise might also help to reduce anxiety and depression.

It is also important to organise a balanced lifestyle. Busy people need to appreciate the need to take a proper break from work to relax, spend time with family and friends and pursue hobbies and interests. If a busy person takes time out to relax and enjoy themselves, they will be in a better frame of mind when returning to work. They will be more productive and less tired.

EXAM PRACTICE

UPPSALA TRAVEL

(a) Explain one characteristic of an effective leader. (4 marks)

Good leaders need to have a number of key characteristics to be successful. For example, effective leaders have a positive self-image, backed up with a genuine ability and realistic ambitions. This is shown in the confidence they have. An example in the UK might be Richard Branson, in his various innovative business activities. Leaders also appreciate their own strengths and weaknesses. It is argued that many managers fail to lead because they spend too much time focusing on in short-term activity. Leaders need to be able to get to the 'core' of a problem and make decisions swiftly.

(b) Explain one benefit to Uppsala Travel of Lotta's style of leadership. (4 marks)

The democratic leadership style used by Lotta has some significant advantages. The main one is that better-quality decisions might be made, because more people have an input in decision making. If several people are involved in decision making, there are likely to be more ideas. In this case, Lotta and four senior managers make the decisions, so key business issues are discussed by five people with a wealth of knowledge and experience between them. This should lead to a more powerful generation of good ideas. There will also be more people to analyse and evaluate these ideas. Finally, Lotta received ideas from her staff through the regular voluntary meetings she held. By using a democratic leadership style, she was able to tap into the ideas of the whole organisation.

(c) Evaluate whether the recent success of Uppsala Travel can be attributed to (i) Lotta's leadership or (ii) other factors. (20 marks)

(i) Before the management buy-out, when Lotta took charge of Uppsala Travel, it was performing badly. It had debts of SEK 11.7 million and was struggling due to the economic recession. However, the management team believed that the previous owners had run the business very badly. They had made some inadequate marketing decisions and provided very poor leadership. Also, motivation levels were dire before the buy-out. Between 2010 and 2012, the company made a loss. By 2016, under the leadership of Lotta, the company's financial performance improved radically. In 2016, the profit after tax was SEK 13.35 million. This suggests that Lotta has led the company to success.

There is plenty of evidence in the case study to support this view. Lotta led the company with confidence and verve. She had charm, was well liked by staff and led by example. All key decisions made by the business were 'thrashed out' at management meetings. In the early days of the buy-out some of these meetings were hard work and lasted for several hours – sometimes a whole day. At the end of the meetings, the four senior managers and Lotta would vote on new company policies. Most of the votes were carried unanimously. She also consulted staff and held voluntary meetings in work time to get their views and ideas. Lotta had introduced a democratic leadership style, which certainly seemed to produce results.

(ii) The success of the business may have been the result of a range of other internal and external factors. Internally, the new website was starting to attract an increasing amount of traffic and bookings made via the website had doubled in two years. The marketing agency was also producing good results – it was expert at placing ads that the target market would see. Additionally, the sales team were probably performing well as a result of the new payment system, which was helping to motivate staff.

Externally, as the economy started to grow in 2014, consumer confidence improved and the holiday industry in general picked up. Demographics were working in the company's favour; the proportion of people aged over 55 in the Sweden was a fast-growing sector.

So, although Lotta's leadership style may have been a significant factor in the company's success, a range of other factors may also have made a contribution. It is difficult to separate out the impact that each individual factor makes on a company.

19 ROLE OF AN ENTREPRENEUR

ACTIVITY 1

CASE STUDY: TRAVELIBRO

1. Explain one role played by an entrepreneur when starting a business. Use an example from the case to illustrate your answer.

Businesses such as TraveLibro are started by entrepreneurs. These are people who have a business idea and want to profit by investing money in their idea. They do this by acquiring resources, organising them and setting up a business venture. In this case, Monish Shar and Malhar Gala are entrepreneurs. They set up a travel social networking portal designed to connect users with fellow travellers, bloggers, travel agents and other industry partners. One important role played by these entrepreneurs is taking a risk. They both invested quite large sums of money into the venture. If the business were to collapse they may risk losing some, or all, of this money.

2. Explain how the roles of Monish and Malhar might change as their business grows into much larger organisation.

When Monish and Malhar first set up the business, they were both employed full-time. They had to combine setting up a business with going to work every day. They worked extremely hard – often only sleeping for 3 hours a night. In the early stages of business development, entrepreneurs like Monish and Malhar will be heavily involved in the day-to-day running of the business. However, they employed some staff in 2014 to help out and the business went from strength to strength. TraveLibro launched its website in August 2015 followed by its app in December 2015. Since then the website has received over 400 000 unique visits and 20 000 app downloads from users in 49 different countries.

Assuming that the business continues to grow, the roles of entrepreneurs are likely to change. Monish and Malhar are less likely to be involved in the day-to-day running of operations and more concerned with business development. They may also have been involved heavily in recruitment – making sure that the right type of people were joining the company. They would have been keen to ensure that all new staff were ‘up to standard’ and may have undertaken some training. They may also have been very involved in developing new clients such as travel agents and advertisers. Other tasks such as financial management, marketing and human resource management might have become more important. It is very common for the role of entrepreneurs to change as the business expands and develops.

Monish and Malhar are ambitious, so they want TraveLibro to be the world’s biggest travel social network. If this happens, eventually they will play little role in the day-to-day running of the business. They will be more focused on managing the direction of the company and designing strategies for the future.

ACTIVITY 2

CASE STUDY: GOOGLE

1. What is the difference between an entrepreneur and an intrapreneur?

Intrapreneurs are employees, usually in large businesses, who use entrepreneurial skills to find and develop initiatives that will have financial benefits and promote innovation within a company. These might be new products, services or systems. However, unlike entrepreneurs, intrapreneurs that fail will not suffer financially. It would be the employer that carries the financial burden of failure. In this case, Google introduced a programme called ‘Innovation Time Off’ to help develop an entrepreneurial spirit

in the organisation. Google allowed its employees to spend 20 per cent of their time at work developing their own individual projects. This approach was to encourage innovation, creativity and original thinking.

2. Explain the possible benefits to Google of its 'Innovation Time Off' programme.

Intrapreneurs can drive innovation in a business and uncover new commercial opportunities. This can help a business gain a competitive edge and increase profits significantly. In some cases the discoveries and inventions made by intrapreneurs can have a huge positive impact on a business. A number of years ago, Google's founders, Larry Page and Sergey Brin, talked about how they had empowered their employees to be more creative and innovative by encouraging them to take 20 per cent of their day to work on ideas that would most benefit Google. This approach resulted in the development of some of Google's most successful products. One such project in the case of Google, started by Paul Buchheit, was the development work for Gmail, particularly the search function and increased storage capacity. Today, Gmail remains one of the most widely-used email platforms on the web, driving key traffic to Google's products. In addition to Gmail, intrapreneurs have developed some of Google's most successful products including Google News, Google Maps, Google Talk, AdWords, AdSense, Driverless Cars and Google Glass.

3. Explain why Google has reduced the role of intrapreneurs in recent years.

Google's approach to innovation has been modified recently. It now has a more targeted innovation programme, which is directed by senior management. This is because Google is now a huge global business. It has a number of highly profitable products that need to be fully exploited to maximise the financial benefits. As a result, a different approach to innovation is needed compared to the 'Innovation Time Off' programme employed when Google was an emerging force searching for new products. A different culture, and a workforce with slightly different characteristics is needed to capitalise on its current highly successful products.

However, there are risks to this change. Innovation will now involve fewer personnel selected for focused projects. This might mean that creative staff will be more difficult to recruit and the flow of innovative concepts and potential new products will diminish. Google does still encourage individual employees to pursue their own ideas, but the amount of time and financial support they get is probably less than it was ten years ago.

EXAM PRACTICE

PIOTR SANTOS

(a) Explain one risk that Piotr has taken in this case. (4 marks)

Entrepreneurs are risk takers: they risk losing any money they put into the business if it fails. In this case, Piotr risked £12 000 of his savings when setting up his restaurant. Fortunately, the business became very successful, but if it had collapsed he could have lost the entire £12 000. Also, if he is operating as a sole trader he would be liable for any debts the business had accrued, because sole traders have unlimited liability. However, in this case the risk paid off. In 2013, his restaurant made £48 000 profit.

(b) Explain one factor that could have affected where Piotr decided to locate the restaurant when setting up his business. (4 marks)

One of the stages in setting up a business is finding a suitable location. The importance of location depends on the nature of the business. Many entrepreneurs, such as tradespeople, tutors and website designers, operate from home. However, a shop, beauty parlour, solicitor's office or a restaurant needs to be located near the target market.

Piotr spent a lot of time finding a suitable location for the restaurant. He felt it was vital to find exactly the right place, which would be both attractive and convenient for the Polish community he was targeting. He contacted 12 estate agents and asked them to help with his search. Eventually he found some empty premises in a part of the city frequented by the Polish community. It was also on a bus route that was used by Polish people coming into town. Finding the right location in this case could have been partly responsible for the success of the business.

(c) Explain one barrier to entrepreneurship that almost prevented Piotr from setting up his business. (4 marks)

There are a number of barriers that discourage many would-be entrepreneurs from getting started. These include a lack of entrepreneurial capacity, reluctance to employ staff, 'red tape', a lack of ideas, aversion to risk and fear of failure. In this case, the potential barrier was lack of finance. Piotr had saved £12 000, but needed a further £8000.

Piotr made appointments with four banks to discuss funding, but his meetings were fruitless: none of them was interested in lending him the £8000 he needed. He approached the Polish community to see if anyone would be interested in making a private loan. He had one offer of £5000 but Piotr could not accept the lender's terms. He was on the verge of giving up when a friend mentioned peer-to-peer funding – getting a loan from unrelated individuals online via a specialist website.

Lack of finance is often a barrier to entrepreneurship because the providers of capital and loans may be reluctant to lend money to entrepreneurs. The failure rate is high for new businesses, and financial institutions cannot afford to lose money. In 2012, around 400 000 new businesses were set up but 20 per cent failed in the first year. A further 50 per cent were not expected to survive into 2015.

(d) Assess the impact on Piotr's role in the business as it started to expand. (10 marks)

After the successful launch of the restaurant, Piotr presumably became immersed in the day-to-day running of the business. For many entrepreneurs, this involves working in production. Piotr was the head chef, so a lot of his time would have been spent cooking in the kitchen.

However, running a business requires entrepreneurs to undertake a range of other tasks that are crucial to the success of the business. For example, it would have been important for Piotr to ensure that the business had enough money to fund its operations. This might involve producing cash-flow forecasts, making payments and monitoring cash movements into and out of the business.

Piotr would also have been responsible for the paperwork. A business must keep a record of all its transactions so that profit and tax liabilities can be calculated. It may be necessary to send out invoices, payment demands and receipts, keep stock records, process wage slips, deal with the tax authorities and comply with legislation.

Another important task carried out by Piotr would be purchasing. The restaurant would need resources such as food and beverages. It might also have needed commercial services, such as cleaning, printing and accountancy. Piotr would have been responsible for this, although he could have delegated some of the tasks to junior staff if he felt they were capable. Piotr would also be responsible for his staff, which would involve recruitment, selection and training. These may have been new skills.

As the business grew, Piotr would have found that his role changed quite significantly. Once he started to open other restaurants in 2014, he would have been involved in other types of work. He would have gradually reduced the time he spent in the kitchen, and more of his time would have been spent on administration and financial management. With four restaurants to run, he would need to develop strict control systems, to ensure that cash did not go missing, for example. He would also have needed to recruit more staff – managers for each of the restaurants, for example. These appointments would have been very important because he would have to trust them.

Piotr was becoming more involved in business development, with plans to open more restaurants and develop a chain. As a result, he would have spent time searching for new locations, arranging finance and developing a marketing strategy. For example, as the business grew there may have been a need to carry out more market research, raise the profile of the business by using social media and invest in some sophisticated promotions.

20 ENTREPRENEURIAL MOTIVES AND CHARACTERISTICS

ACTIVITY 1

CASE STUDY: KAVINDU KUMARA

1. Discuss whether Kavindu has the characteristics to become an entrepreneur.

It could be argued that Kavindu does possess some of the characteristics needed to be an entrepreneur. Dilani De Silva, the Head of Year at Kavindu's school, said in his final school report that he is full of self-confidence, shows initiative and, when interested, can be extremely determined. These are three of the important characteristics needed to be an entrepreneur. Successful entrepreneurs are people who believe that they are going to succeed. They think they have a winning formula for their business. They can persuade other people, for example, to buy the product or help finance the business. Entrepreneurs also need to be determined. They need to think that they can take control of events and turn them into something which will benefit the business. They also need to be able to take the initiative in situations and be able to change.

Kavindu has demonstrated some of these characteristics. In December 2016, he organised a large cricket competition in his local village. The event was well publicised. Kavindu put up posters in neighbouring villages and he persuaded a local newspaper to write an article about the tournament. On the day of the event, ten teams from neighbouring villages near Galle, Sri Lanka, turned up and so did several hundred supporters and curious locals. Kavindu had organised a number of food vendors and stalls to help make some money. The competition was a huge success and Kavindu made SLR 9800.

This is sound evidence that suggests Kavindu can become an entrepreneur – he already has entrepreneurial experience. Finally, his report also says that Kavindu is a charming young man. He is loyal, honest, open and friendly. These are very useful qualities to have as an entrepreneur.

EXAM PRACTICE

MAMA'S SPICES & HERBS

(a) Explain one characteristic that entrepreneurs must have to increase their chances of being successful. (4 marks)

Setting up a business is a common activity and many hundreds of thousands are set up every year in different countries around the world. However, not everyone is suited to becoming an entrepreneur – possibly because they do not possess the necessary characteristics. One of these important characteristics is perseverance. Businesses commonly have successes and failures. There is always an element of risk that a business could struggle or even fail. Therefore, successful entrepreneurs have to show perseverance. They require the ability to get through the bad times and the setbacks. In this case, Mikie Monoketsi set up Mama's Spices & Herbs after a personal crisis. Mikie's previous call centre business and marriage both failed at the same time. This shows that she has the ability to 'bounce back' and persevere.

(b) Explain one reason why some entrepreneurs run their businesses from home. (4 marks)

Quite a number of entrepreneurs set up their businesses from home. They may be tradespeople, such as plumbers, painters, small builders or electricians that use their home as a base for their business. Or, increasingly, they may work from a room or an office at home. For example, self-employed writers, accountants, software designers, tutors and financial analysts. There are two key benefits for homeworkers. The time and expense spent travelling to and from work is eliminated. They also enjoy more flexibility. For example, they can take meals and breaks whenever they want and a parent may be able to fit work around the needs of their children.

(c) Analyse two important skills that entrepreneurs like Mikie Monoketsi need to run a business. (6 marks)

Not only do entrepreneurs need to possess a number of important characteristics to be successful, they will also need to use a wide range of different skills. To begin with, it helps if entrepreneurs are qualified to some extent in their chosen line of business. For example, an entrepreneur setting up a flying school may require piloting experience and an instructor's certificate. Someone starting a commercial radio station will need some broadcasting, transmitting and programming experience. However, it is possible to set up a business in unfamiliar fields. There are also examples of entrepreneurs entering quite diversified lines of business without any relevant experience.

In this case, Mikie Monoketsi emphasised the importance of good communication and networking skills. Mikie used gyms to develop partnerships, get connected and meet people to help build her business. For example, she met a helpful executive producer of a spice manufacturer at a gym who gave her lots of useful advice. Mikie also appears on television and radio which gives her the opportunity to explain her vision on health and fitness, demonstrate exercise routines and occasionally promote her business!

Another important skill which Mikie emphasised was financial management. She said it was very important to monitor spending and account for every single cost – especially labour, packaging, cost of sales, and time. Mikie discovered that a failure to record all costs meant that even though she was increasing sales she wasn't making more money. She had failed to take into account the samples she was giving out. Samples are very important in the food industry and their costs must be recorded. Finally, she also recognised (eventually) that the business could not fund wasteful personal spending. Such transactions were much reduced when she realised that the business was suffering. To keep up-to-date with transactions Mikie recorded all expenses in a notebook and invoiced all customers. Once she started doing this the performance of the business improved.

(d) Evaluate whether Mikie's motives for setting up Mama's Spices & Herbs were (i) financial or (ii) non-financial. (20 marks)

People set up businesses for a wide range of reasons. For example, they may not want to work for an employer any more, they may want to develop a personal interest into a business or they may have been made redundant. A very large proportion of entrepreneurs start businesses because they want to make money. They often think that they could earn far more if they worked for themselves. Profit is the motivator for many entrepreneurs and most businesses would not exist if it wasn't for the desire to make a profit. Two approaches to generating profit can be identified. Some entrepreneurs try to make as much profit as they possibly can in a certain time period. This is called profit maximisation. These entrepreneurs are motivated by money and their key focus is the financial return on their efforts. It might be argued that entrepreneurs that try to maximise profits are likely to take bigger risks. This is because there is usually a direct relationship between risk and reward.

In this case, Mikie may have had a non-financial motive for setting up her business. She was passionate about healthy eating and living. She carried out some research into the eating habits of people living in the neighbourhoods of Diepsloot, Randfontein, Cosmo City and Lion Park. She found that the spices people used were cheap and contained high levels of salt and other unhealthy

ingredients such as MSG, preservatives and bulking agents. These were considered unhealthy and likely to contribute to high levels of illnesses such as hypertension and diabetes. Mikie also discovered what people were cooking – skop, mogodu, maotwana, kota (cows head, intestines, chicken feet, bunny chow), potato chips, fish, braai, stews and curries and fried chicken. This gave Mikie the idea to create her own set of healthy spices that would go well with these particular foods. However, her herbs and spices offered better quality with health benefits at an affordable price. This might also be regarded as an ethical reason for starting her business.

It might also be argued that Mikie wanted to run her business because she was independently minded. A lot of people want to be 'their own boss'. This is an important non-financial motive for setting up a business. These entrepreneurs are driven by the desire to be independent. The freedom to make all the decisions when running a business is very appealing. Some people often dislike being told what to do at work. According to an article and poll by *Startups.co.uk*, having the independence to make your own decisions is considered the key benefit of being an entrepreneur. Nearly 90 per cent of respondents said this was very important. Information in the case does suggest that Mikie is independently minded.

Mama's Spice & Herbs is established and growing steadily. Mikie is diversifying and targeting mainly women with a range of health products such as Flat Stomach Tea and Flat Stomach Power Oats. The business is strong and now provides an online shopping facility. Mama's Spice & Herbs is currently looking to recruit additional agents in the Western Cape, Northern Cape, Eastern Cape (PE and East London), Free State, Mpumalanga, Limpopo and North West. Mama's Spices & Herbs also has a shop in Fontainebleau. Not only is Mikie making a lot of money for herself, she also helps to inspire other young entrepreneurs to set up in business. To conclude, there seems to be a combination of both financial and non-financial motives behind Mikie's decision to set up Mama's Spice & Herbs. However, given the passion that Mikie has for healthy eating and the lengths she goes to promote a healthy lifestyle, it could be argued that originally the main motivators here are non-financial'.

21 BUSINESS OBJECTIVES

ACTIVITY 1

CASE STUDY: SEARS

1. Using an example from this case, explain one reason why Sears might have pursued survival as a business objective.

All businesses will consider survival as important. However, from time-to-time, survival may be *the* most important objective. For example, a business might struggle to survive if new competitors enter the market. If the new entrants have better products or more financial resources, existing businesses may start to focus on survival at the expense of other objectives. The survival of a business might also be threatened when trading conditions become difficult.

In this case, Sears has two clear problems that are threatening its survival. The slow economic recovery from a deep recession has hit the store hard because its target market consists of middle- and low-income consumers. Arguably, this group has been 'hurt' the most by the recession. However, another problem has been stiff competition from 'leaner' operators such as Walmart, Home Depot and Amazon. It was also reported that CEO Eddie Lampert thought that many of the Sears stores were too large and in the wrong locations. If Sears fails to address these problems, the survival of the business might well be threatened. Consequently, survival has become a clear business objective in this case.

2. Discuss whether the measures Sears has taken to survive are likely to be successful.

When the survival of a business is threatened, action has to be taken swiftly to stave off collapse. In this case, Sears has taken a number of measures to help the business survive.

It plans to close more stores, so the number of stores will continue to fall. Sears once owned 3523 stores; in 2015, this figure had reduced to fewer than 2000. Presumably the stores targeted for closure will be the marginal ones – those making a loss or making very little contribution to the business.

The business also plans to borrow more money – including US\$400 million from a hedge fund owned by Eddie Lampert.

Finally, between 200 and 300 buildings will be sold and leased back to improve liquidity. This will give the business more cash, but also allow it to retain the use of the buildings.

Although the company has taken some positive measures to help it survive in the market, survival is not guaranteed. Sears has seen its revenue fall for eight consecutive years, making losses in the last four of those years; alongside this, competition is intensifying, not weakening.

Perhaps the business needs to invest in modernisation and pay more attention to online shopping, as well as addressing the competitive pressure from modern retailers.

ACTIVITY 2

CASE STUDY: FANCYTHAT

1. Explain what is meant by a SMART objective.

Business performance is easier to assess if SMART objectives are set. This means that they should be:

- Specific – stating clearly what is trying to be achieved
- Measurable – capable of numeric measurement
- Agreed – have the approval of everyone involved
- Realistic – able to be achieved given the resources available, and
- Time-specific – have a stated time by which they should be achieved.

In this case, Brad has set a number of SMART objectives. Once the business survived the first year, his objective was to reach a turnover of AUD 400 000 by 2016. This is an example of a SMART objective. It is specific (AUD 400 000 turnover), measurable (in money terms), agreed (there is no reason here to suppose it wasn't), realistic (it was achieved) and time-specific (achieve by 2016).

Brad also set other SMART objectives relating to his cost-cutting drive. His objective was to cut fixed costs by 20 per cent and variable costs by 25 per cent, both by the end of the year.

2. Explain how Brad might cut costs in his business.

Businesses can cut costs in a variety of ways. For example, they can lay off staff to cut labour costs, find new suppliers to get cheaper resources, increase the usage of recycled materials, develop new working practices that use fewer resources and develop ways of saving energy.

In this case, Brad has distinguished between cutting fixed costs and variable costs. To cut fixed costs he might target rent, advertising, insurance, leasing charges and other fixed overheads. He might need to re-negotiate rent or move to new premises and find cheaper leasing companies and cheaper methods of advertising, for example.

To cut variable costs he might target wages, raw materials, utilities, packaging, distribution and energy. To reduce these variable costs, laying off staff is probably not an option since his business is growing. However, he might find some cheaper suppliers of raw materials, energy and commercial services.

EXAM PRACTICE

SONY

(a) Explain why survival may have been a business objective for Sony between 2009 and 2015. (4 marks)

All businesses will consider survival as important. However, from time to time survival may be *the* most important objective. For example, when a business first starts trading it may be particularly at risk. It often takes time for people to recognise the existence of a new business. Entrepreneurs may lack experience and there may be a shortage of resources. Therefore, a target for a new business may be to survive in the first 12 months. A business might also struggle to survive if new competitors enter the market. If the new entrants have better products or more financial resources, businesses may start to focus on survival at the expense of other objectives. The survival of a business might also be threatened when trading conditions become difficult. During the global recession which followed the financial crisis in 2008, many businesses around the world started to struggle for survival.

In this case Sony struggled between 2009 and 2015. Figure 1 shows that for most of this period Sony was making losses. The biggest loss was in 2012 when the company lost JPY 4567 hundred million. This might suggest that while Sony was struggling, their main business objective may have been to survive in the market. Although Sony is a large multinational, it is still subject to strong competition and other external events. Businesses cannot carry on trading at a loss forever – eventually they will run out of money. In this case, the length of time the company was making losses tends to support the view that it was struggling to survive.

(b) Explain how employee welfare might be a business objective. (4 marks)

Some businesses pursue non-financial objectives. For example, in recent years some have realised the benefits of meeting the needs of employees more effectively. Therefore, another objective might be to improve employee welfare. If employee welfare is improved, workers will be happier, better motivated, more productive, more cooperative, more flexible and less likely to leave. A number of measures can be taken to improve employee welfare. For example, a business could improve the working environment by making it cleaner, less noisy and less crowded. It could ensure that staff are given proper breaks and somewhere comfortable to interact with colleagues during those breaks. It could also ensure that staff are equipped with the necessary tools and equipment, provide ergonomically designed chairs for call centre workers, for example. Staff welfare might also be improved if high standards of courtesy are maintained between all staff members. Improving employee welfare is also likely to reduce staff absenteeism through sickness, enhance the image of the business, help to comply with health and safety legislation and make it easier to recruit and retain good quality people.

(c) Discuss the importance of profit to a company like Sony. (8 marks)

Profit is the driving force behind most businesses. Without profit most businesses would not exist. However, some businesses focus on profit more aggressively than others. They want to make as much profit as they possibly can. This is called profit maximisation. If a business pursues this objective, it is usually because the owners have a powerful appetite for more profit. Arguably, this is most likely to be the case if businesses are owned by institutional shareholders such as pension funds and investment funds. These owners need to maximise the returns on their investments to meet the needs of their clients.

If businesses want to maximise profit they will focus on keeping costs as low as possible while raising prices as high as they can before customer loyalty is damaged. Skim pricing is often used by profit maximisers. This involves setting the price of products high and selling to customers who are less sensitive to price. Businesses that sell luxury items, such as designer clothes and expensive perfumes, to a small but affluent customer base often use profit maximisation strategies. Sony may use this pricing strategy for some of their products such as its PlayStation consoles. Some of the products sold by Sony can be targeted at customers who like to own the latest technology, even at higher prices.

To conclude, profit is likely to be very important for Sony. It is a multinational company and probably owned by large institutional investors. These are important stakeholders and invest their money in businesses in the hope of making good financial returns. If the company reduces dividend payments, or stops paying dividends and the share price starts to fall, institutional investors may withdraw their support for the company. They may sell their Sony shares and find alternative investments. Sony made losses for quite a long period of time. However, some evidence in the case suggests that the company retained the support of shareholders. In 2014, Kazuo Hirai, the Sony CEO, planned to introduce an extensive cost-cutting programme and in 2015 Sony shareholders showed their support for the CEO by reappointing him at an AGM. At the meeting, Hirai apologised for the poor financial performance of the company and said that he and other senior executives would not be taking their bonuses for the year.

(d) Assess the extent to which customer satisfaction is a business objective for Sony. (10 marks)

Most businesses will try to meet the needs of customers. The benefits are clear. If customers are satisfied they are more likely to return. Loyal customers are valuable to a business. In order to win their loyalty, some businesses aim to exceed customer expectations. In general, they may do this by ensuring that all customer services staff are trained to a very high level in communication. Their conduct must be polite, professional and friendly all of the time. They may also provide a platform for customer feedback – an online review system for example. Increasingly, companies are interacting with customers using social media – this helps to encourage a two-way flow of information. Businesses may also deal with customer complaints promptly and effectively – to the satisfaction of the customer and monitor customer service regularly – using mystery shoppers for example.

In order to have effective customer service, businesses must know what customers want, provide them with it consistently and ask them how the business is doing. In this case, Sony has been seeking to improve its performance in customer service (CS). In Sony's 2016 annual report it said that Sony was introducing measures to improve its CS function. Sony announced an initiative called the Sony Pledge of Quality – 'Sony employees will always respect our customers' viewpoints in striving to deliver product quality and customer service that exceed their expectations.' For CS this meant improvements in responding to changing customer needs and providing a high-quality repair service. To help support the pledge and achieve the CS improvements, Sony appointed CS officers to coordinate global CS operations and introduced key performance indicators, such as improvement in rate of repair completion within a set period of time. It also set up a network of bases around the world to meet the CS needs of local customers and provided ongoing training for staff in CS operations. In addition, Sony provided more convenient and eco-friendly manuals. This will involve switching from paper to online manuals and using pictures for instructions rather than text (wherever possible).

To conclude, the measures outlined above suggest that Sony takes customer satisfaction very seriously. The company understands the importance of customer service and has used resources to improve the quality of customer service. However, it is likely that profit is the most important objective for Sony – especially after struggling for so long to make a profit. Sony might argue that the improvements in the quality of their customer service are needed to help to company recover and make more profit in the future. It is unlikely that customer satisfaction alone would be Sony's key business objective.

22 BUSINESS CHOICES

ACTIVITY 1

CASE STUDY: BRAZILIAN BIOFUELS

a. Using this case as an example, explain what is meant by opportunity cost.

When making choices, individuals, businesses and governments will face a cost once their choice has been made. This is called the opportunity cost. This cost arises because a sacrifice has to be made when making a choice. In this example, a business has placed its spending desires in order of preference. Therefore, the opportunity cost can be identified. According to the list, Jemerson EthoFuel would prefer to allocate the BRL 40 million to the upgrade of production facilities to improve efficiency by 25 per cent. The opportunity cost of this choice will be the benefit lost from the next best alternative. In this case it will be the benefit lost from not merging with another biofuel company to cut costs.

ACTIVITY 2

CASE STUDY: BOEING DREAMLINER

1. What is meant by the trade-off between risk and reward?

One important trade-off is that between risk and reward. It is often necessary to take bigger risks in order to reap higher rewards. However, with high risk there is the danger of large losses.

In this case, Boeing took a risk by outsourcing the design and manufacture of the new Dreamliner. This was done to reduce development costs but problems were encountered and the financial consequences are still being felt.

2. Assess the possible costs incurred by Boeing as a result of outsourcing its design and production of the Dreamliner.

It has been reported that Boeing's operations decisions relating to the manufacture of the Dreamliner were too risky.

The company chose to have the jet designed and built mostly by other companies. This was to reduce costs significantly. However, as a result, a number of relatively serious problems were encountered. For example, the original delivery date of 2008 was significantly delayed, with the first Dreamliner being delivered three years later in 2011. In the fuselage, many of the components failed to conform to Boeing's specifications. This was very expensive to rectify and caused delays. In January 2013, the entire fleet of 50 Dreamliner planes was grounded after planes had problems with their batteries.

Some have suggested that outsourcing the design and production of the Dreamliner was a mistake. In the absence of cost data, it is difficult to draw a meaningful conclusion. However, if there are further delays and groundings, there will be both a loss of revenue and increased costs. There is also the risk that passengers will choose not to fly on the aircraft because of its problems. The potential loss in revenue this could cause might be the most damaging of all these costs, but it would take some while for these figures to be known.

EXAM PRACTICE

OBERTAUERN FARM

(a) Explain what is meant by a trade-off when making a business decision. (4 marks)

Businesses have to make several decisions and decision makers are frequently faced with trade-offs. This means that opting for one choice involves compromising another.

In this case, there is a trade-off between crop yields and environmental damage. Farmers can enjoy higher crop yields, and therefore more revenue, if they use fertilisers and pesticides. However, the use of fertilisers and pesticides, which contain harmful chemicals, is known to damage the environment. Farmers, and society in general, have to decide whether to increase world food output at the expense of damaging the environment or protect the environment and accept lower yields.

(b) Explain the opportunity cost to Obertauern Farm developing the campsite. (4 marks)

Opportunity cost arises because a sacrifice has to be made when making a choice between different options.

In this case, Marko and Carina Almer are deciding how to spend the profit made by the business. They have identified four options, which are placed in order of preference. They have elected to invest in the development of a campsite on the farm.

The opportunity cost will be the benefit lost from the next best option – buying the holiday home in Andalucia. This might include a possible income stream from renting it out, a capital gain in the property and the pleasure they might have had staying there during holidays.

(c) Explain one way in which the business might find the 'right balance' when weighing up a trade-off. (4 marks)

In this case, Obertauern Farm might try to undertake some market research to find out what customers think about their plans to 'go organic'. Obertauern Farm might also be able to generate some revenue information from its research. It might gain access to cost data so that it can evaluate as accurately as possible the costs to the business of the decision. The more quantitative data gathered, the easier it will be to find the 'right balance'.

(d) Assess the costs to Obertauern Farm of switching to organic production. (10 marks)

The choice between traditional farming methods and organic production may be a difficult one. If Marko and Carina decide to switch farming methods to organic production, the impact is likely to be significant.

A number of costs would have to be considered. Initially, it may be necessary to invest in new machinery and equipment. One of the major costs is the extra time needed for organic farming. For example, weed control is time-consuming and labour intensive. An important cost will be lower yields. It is reckoned that the crop yields for organic farming are 19 per cent less than they would be using traditional methods.

One problem is the extra damage to crops caused by pests. It is also suggested that water use rises and some organic pesticides, such as copper, can remain in the soil and be harmful. The opportunity cost, if the switch is made, would be the benefits lost from using traditional methods, such as higher yields and the time saved in farming techniques.

Although the costs of switching farming methods are significant, there are some benefits. Marko and Carina will get higher prices for their organic produce, which will help to increase revenue and compensate for lower yields. Also, the organic food industry is worth over €1300 million a year.

Obertauern Farm may enjoy the benefits of trading ethically because of the environmental benefits, such as the improvement in natural habitats, healthier food for people and increased biodiversity due to fewer chemicals that harm bees and other insects.

Before making their final choice, Marko and Carina will have to weigh up the advantages and disadvantages of the switch. Their decision might depend heavily on how ethically minded they are. They may be prepared to accept less profit if they are happy in the knowledge that they are making a contribution to the protection of the environment.