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**SATISFYING WANTS AND NEEDS**

Businesses are usually set up to satisfy the wants and needs of customers. Everybody has wants and needs. We **need** food, drink, clothing, shelter and other essentials to stay alive. Other things are not quite so essential, but we still **want** them so our life can be enjoyable.

Business activity is concerned with satisfying these wants and needs. The act of preparing a good or service for sale is called production.

Businesses are set up to satisfy our needs by providing physical goods (manufacturing) and services. When you visit a restaurant not only are you provided with a physical product, the food, but you also receive a service in the form of a member of the restaurant staff bringing the food to the table and making sure that you have everything that you want to enjoy the meal.

**ADDING VALUE**

Businesses aim to provide products and services to customers that are more attractive than those of their competitors. Everything that a business does to make a good more desirable is adding value.

For example, cold fresh orange juice is enjoyed across the globe. Oranges are grown in temperate climates such as California (United States), Libya (North Africa) and Italy (Southern Europe). The oranges are transported in lorries, freight trains and ships across the globe. Hotels and restaurants buy and squeeze the oranges to make a fresh drink for the end customer. Ice may be added to cool the juice.

A restaurant **selling** freshly squeezed orange juice might buy three oranges at 10 cents each (totalling 30 cents) to make a glass of fresh orange juice that it sells to a customer for $1. The **value added** by the restaurant is therefore 70 cents. $1 – 30 cents = 70 cents.

**SCARCITY**

We cannot have everything we want: we have to make choices. This is because resources are scarce: there are not enough for all the things that we would like to do. If we turn a field or park into a car park, then we lose the green space. Choices have to be made all the time.

In the same way, a business makes choices. Farmers make choices about when and how to improve their land. Farmers in Jamaica can decide to grow sugar cane or coffee. They sometimes make choices about who to sell their produce to (e.g. at a local market or to an agent of a food company).
**Stage of production:**

1. **Growing the oranges**
   
   Farmers look after the orange trees for several years before the trees give fruit. Each year they must be treated against pests.

2. **Transporting the oranges**
   
   Fresh ripe oranges are transported closer to **market**.

3. **Preparing the oranges**
   
   The juice is squeezed from the oranges and ice added.

4. **Serving the customer**
   
   The juice is presented to the end consumer in a polite and friendly way.

**Figure 1.1.2** Adding value to a product: the customer benefits from value being added at each stage of production

---

**Did You Know?**

**Opportunity cost** is the term used to describe the cost of a choice made in terms of the next best alternative. For instance, the opportunity cost of the choice made by a business to buy a new computer may be the building repairs that can no longer be afforded.

**Study Tip**

Distribution includes the processes involved in getting goods to consumers. A range of businesses are involved in distribution including transport companies, retailers (all forms of shops and sellers to the end consumer, including online sales), as well as wholesalers who store goods and supply goods to retailers in bulk.

**Summary Questions**

1. In your own words, write definitions for: needs, wants, scarcity, choice, opportunity cost, adding value.


3. Explain the difference between producing goods, supplying services and distributing products.
Factors of production

Factors of production are the resources that go into making products. There are four categories of factors of production.

1. Land. This not only includes physical land but also other natural resources (e.g. rivers and seas providing fish stocks, mines producing coal, lead, tin).
   
   Land is fundamental to enterprise in providing a physical space from which to operate as well as the fundamental natural resources required – whether this be in the form of cotton for cotton textiles, coal and oil for providing energy supplies, or farmland for growing food.

2. Labour consists of the physical and mental effort of employees. Physical labour would consist of activities such as lifting, shovelling, labelling, and so on, while mental labour would be required to make calculations and to engage in clear communications with others.

3. Capital includes all those items that go into producing other things (e.g. machines and tools). In addition, a business needs financial capital in order to pay its bills.

4. Enterprise is the factor that brings other factors together to produce goods. Entrepreneurs are people who take risks by running businesses. Each of these factors will specialise in particular activities and lines of production.

Rewards to factors of production

Each of the factors of production receives a reward in the form of a factor income.

The reward for enterprise typically comes in the form of profit. It is also possible to argue that entrepreneurs will be rewarded in the form of the enjoyment they gain from being their own boss and running an enterprise in a creative way. Profits are not guaranteed. Where enterprises do badly the entrepreneurs may have to pay for losses out of their own funds, which ultimately may drive them out of business.

The reward for labour comes in the form of wages. Typically the higher the level of scarce skill provided by an employee the greater the person’s wage will be.

The reward to land comes in the form of rent.

The reward to capital comes in the form of interest. An example of this would be in the form of interest received for depositing money in a bank.
CASE STUDY

Popinjay

Popinjay is an enterprise based in Pakistan that produces bags made by specialist craftswomen. The bags are then sold both nationally and to global markets.

The enterprise for Popinjay comes in the form of its owner Saba Gul who came up with the idea and the drive to create networks of highly skilled craftswomen across Pakistan to produce high-quality bags. The business started off as a not-for-profit enterprise with the aim of empowering women to give them fair value for their work. The enterprise offers its women practical training, good wages, dignity and a path to self-sufficiency. It was through Saba’s enterprise that the business has been able to expand from a small network pooling skills to an international brand selling high-quality bags worldwide.

The labour for Popinjay comes in the form of the craft work supplied by the women who provide the handmade bags. The enterprise typically employs older skilled workers.

The capital for the business came originally in the form of Saba’s own savings and a grant to support enterprise that she received from the university where she was studying. More recently, the business has expanded to become an international brand and investors have joined the business who now take a share of the profits. In addition to the financial capital, physical capital is employed in the form of textile manufacturing equipment used by the craftworkers.

The land for the business comes in the form of the company offices and directly owned trading outlets.

Dynamic business

Businesses have to constantly respond to change. They operate in a dynamic (constantly changing) business world and businesses need to respond appropriately (i.e. to be dynamic). For example, competitors will bring out new products, they will alter their prices, and make new offers to consumers. The dynamic business needs to be aware of what competitors are doing and try to stay ahead of them e.g. by bringing out new products of their own. Other examples of the dynamic business world include the growth of competitors from other countries and the development of new technologies.

SUMMARY QUESTIONS

1. Identify a business that you are familiar with. Give examples of the land, labour, capital and enterprise employed by this business.
2. Why does a business need to have an entrepreneur or entrepreneurs?
3. In what circumstances might the rewards to labour be higher than those for enterprise?
Business activity is often broken down into three types:

- extractive (primary industry)
- manufacturing and construction (secondary industry)
- services (tertiary sector).

Brazil is the world’s second-largest ethanol supplier after the United States. The following table shows the three stages involved in providing ethanol fuel for cars in Brazil.

### Extractive industries

<table>
<thead>
<tr>
<th>Stage 1: Primary production</th>
<th>Stage 2: Secondary production</th>
<th>Stage 3: Tertiary production</th>
</tr>
</thead>
<tbody>
<tr>
<td>Farmers grow sugar cane in Brazil</td>
<td>The sugar cane is refined to make ethanol</td>
<td>The ethanol is sold on service station forecourts to car owners and truck drivers in Brazil</td>
</tr>
</tbody>
</table>

Figure 1.1.3.1 The three stages involved in providing ethanol fuel for cars in Brazil

Extractive, or primary, industries are concerned with using natural resources. They include farming, mining and oil drilling. Farmers grow and harvest crops and farm livestock, while miners take fuel and minerals from the ground. Primary industries sometimes produce raw materials such as iron ore (for making steel) and oil (for making petrol, plastics, fibres, etc.). They also produce finished products such as fish and oranges.

### Manufacturing and construction industries

Manufacturing and construction industries are concerned with making and assembling products. Manufacturers use raw materials and parts from other industries. Most products go through several stages of production: when the good is only partly made, it is a semi-manufactured good. Examples of manufactured products are furniture, cars, chocolate and oil rigs. An example of a semi-manufactured good would be the shell of an aeroplane that has not yet had the engine and inside furnishings (seats, etc.) added.

### Service industries

Service, or tertiary, industries give something of value to people, but are not physical goods. You can physically touch or see a packet of biscuits, a bicycle or a computer. You cannot touch or hold a visit to the cinema or a lesson given to you in school: these are both services.

Other services include banks keeping your money safe, public transport carrying people around or hairdressers cutting your hair.
CASE STUDY

Employment by major industry sector in different countries

Employment is classified into different industries by a national classification system such as the Standard Industrial Classification (SIC) in the UK or the North American Industrial Classification System (NAICS) in North America. This identifies and classifies specific sectors such as 11 Agriculture, Forestry, Fishing and Hunting, which is then broken down into further sectors (e.g. 111 Crop production) and then into types of crop production (e.g. 1111 Oilseed and grain farming). The latest forecast figures for the United States for 2016 are that 1.6 per cent of the population will be employed in primary industry, 12.7 per cent in secondary industry, and the vast majority (85.7 per cent) in the tertiary sector. This data for the United States contrasts with that of newly industrialised countries (NICs) such as Brazil. In Brazil, roughly 20 per cent of the population is still engaged in agriculture and other primary industries, and a further 14 per cent in manufacturing, with the remainder working in services.

Questions

1 In your country which is the largest sector of the economy: primary, secondary or tertiary?
2 What are the main types of industries involved in your largest sector?
3 What industrial classification system is used in your country? What industries are recognised in this classification?

SUMMARY QUESTIONS

1 What are service industries? Give five examples of jobs in service industries.

2 State whether you would classify the following industries as primary, secondary or tertiary. Give reasons for your choices.

   Construction / transportation and warehousing / retail trade / financial activities / manufacturing / mining / farming / educational services / leisure and hospitality / fishing.

3 The following statistics relate to employment in the industrial sector in China. (Source: China Statistical Yearbook, 2015)

<table>
<thead>
<tr>
<th>Year</th>
<th>Primary (%)</th>
<th>Secondary (%)</th>
<th>Tertiary (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1978</td>
<td>70</td>
<td>18</td>
<td>12</td>
</tr>
<tr>
<td>1988</td>
<td>58</td>
<td>22</td>
<td>20</td>
</tr>
<tr>
<td>1998</td>
<td>50</td>
<td>23</td>
<td>27</td>
</tr>
<tr>
<td>2014</td>
<td>34</td>
<td>30</td>
<td>36</td>
</tr>
</tbody>
</table>

Describe the key trends that you see in the data. Explain why these changes might have occurred. Do you expect these trends to continue?

DID YOU KNOW?

The process of development has involved the transformation of society over time. In the first wave of development, the focus was on primary activity – particularly agriculture and fishing. In the second wave, societies experienced an industrial revolution with the growth of manufacturing industry becoming the main form of economic activity. In the (most recent) third wave, developed societies principally focus on tertiary (service sector) activity.

ACTIVITY

Group the following activities under the headings of Primary, Secondary and Tertiary industry.

<table>
<thead>
<tr>
<th>Construction</th>
<th>Mining</th>
<th>Fire fighting</th>
<th>Retailing</th>
<th>Advertising</th>
<th>Banking</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building</td>
<td>Coal</td>
<td>Electrician</td>
<td>Key Cutting</td>
<td>Civil Service</td>
<td>Oil Drilling</td>
</tr>
<tr>
<td>Cloth Making</td>
<td>Laundry</td>
<td>Cinema</td>
<td>Key Cutting</td>
<td>Civil Service</td>
<td>Fishing</td>
</tr>
<tr>
<td>Food Selling</td>
<td>Retailing</td>
<td>Book Publishing</td>
<td>Key Cutting</td>
<td>Public Transport</td>
<td>Food Selling</td>
</tr>
</tbody>
</table>

KEY POINTS

1 It is helpful to classify business activity into primary, secondary and tertiary sectors.
2 There has been a global increase in the tertiary sector.
Being enterprising

An entrepreneur is someone who not only comes up with a great new idea but is also able to put this idea into practice.

Entrepreneurs need to be willing to take a risk. If the business idea is successful then the entrepreneur stands to make a profit. However, should the idea fail then they stand to lose money.

TOPIC AIMS

Students should be able to:
• understand the terms ‘enterprise’ and ‘entrepreneur’
• outline the characteristics of an entrepreneur
• outline the objectives of an entrepreneur.

CASE STUDY

James Dyson and the Dyson Dual Cyclone

James Dyson was doing some housework in 1979. His first job was to vacuum the living room using a Hoover Junior machine. The vacuum cleaner that he was using employed the standard technology of the time.

James felt that the system was very inefficient because there was so much dirt and dust that was not being sucked up. As a consumer he felt that the existing method did not fully meet his needs. He felt that given time he could add value to the machine to make it better.

James was already a well-known designer, having invented (among other things) the ‘ballbarrow’ (a wheelbarrow with a ball rather than a wheel). His business was using an industrial cyclone to capture dust during production. Cyclone towers are a well-known industrial filtering system, with air being dragged into a tower and whirled around, at very fast speeds. James realised that the cyclone system could be applied to vacuum cleaners to enable them to work more efficiently. He started to work on the task, which took him four years and 5127 prototypes (trial models). He realised that for household vacuuming you need a dual cyclone – one to separate out larger items and the second to catch the smaller particles. Unlike traditional vacuum cleaners, the Dyson Dual Cyclone does not use bags. The product has proved to be a great success story, revolutionising the industry and turning the Dyson company into a large and successful international business, manufacturing and exporting the product across the globe.

Questions

1. How did James Dyson turn an idea into an effective product?
2. What does this case study tell you about the qualities of an effective entrepreneur?
Objectives of entrepreneurs

People like James Dyson start their own enterprise for a variety of reasons. Some have a bright idea that they think will make them rich (e.g. a ballbarrow or dual cyclone system). Others find themselves unemployed and start their own business to survive. Some can only be themselves when they are their own boss. Others want to give something to the community and can see no other way of doing it except by setting up on their own. However, setting up an enterprise is not for everyone. It requires a lot of hard work and long hours to make an enterprise a success. It also requires a lot of attention to detail, not just the creation of exciting ideas. Often someone who is creative and imaginative (important qualities for an entrepreneur) will need a business partner with greater attention to detail and who can set firm commercial foundations in place (other qualities of an entrepreneur).

Characteristics of entrepreneurs

Generally speaking, it is possible to identify a number of characteristics of entrepreneurs. As you work through the list consider whether the points apply to you.

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>Do you have these characteristics?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Logical, perceptive, organised, realistic, responsible – good at getting things done</td>
<td></td>
</tr>
<tr>
<td>Outgoing, confident</td>
<td></td>
</tr>
<tr>
<td>Good communicator – able to get a point across</td>
<td></td>
</tr>
<tr>
<td>Sociable, good leader – can win people over instead of irritating them</td>
<td></td>
</tr>
<tr>
<td>Single-minded, decisive, independent</td>
<td></td>
</tr>
<tr>
<td>Open-minded, able to take advice</td>
<td></td>
</tr>
<tr>
<td>Flexible, adaptable</td>
<td></td>
</tr>
<tr>
<td>Opportunist, risk taker, ambitious</td>
<td></td>
</tr>
<tr>
<td>Hard-working, committed, determined, ‘get up and go’ type</td>
<td></td>
</tr>
<tr>
<td>Tough – often the best test of a successful entrepreneur is his or her ability to deal with failure</td>
<td></td>
</tr>
<tr>
<td>Individual – not afraid to stand out from a crowd, or of what others think</td>
<td></td>
</tr>
<tr>
<td>Knowledgeable about the dynamic business environment and respond to changes in a dynamic way</td>
<td></td>
</tr>
</tbody>
</table>

These characteristics are important because entrepreneurs need to be confident enough to make decisions and take risks, see Risk and ownership in 1.2.3.

STUDY TIP

Being enterprising does not always involve inventing a totally new product. An entrepreneur may find a new variation or style on an existing product, or a new process of production or selling.

KEY POINTS

The key characteristics of successful entrepreneurs include:
- the willingness to work long hours and to work hard
- willingness to take risks in order to establish a successful enterprise
- ability to take tough decisions and not to be put off by failure
- ability to spot new opportunities
- good communication skills and the ability to get on with people.

SUMMARY QUESTIONS

1 Identify a celebrated local entrepreneur in your country. To what extent does he or she have the characteristics that have been outlined in this unit?
2 How could you go about developing the characteristics required to be a successful entrepreneur?
3 What enterprising ideas do you have? What would you need to turn these ideas into a successful enterprise?
When setting up a business, one of the first decisions is what type of business to form. The type of business chosen determines the legal status of the business and how easy it is to raise capital.

**The sole trader**

This section looks at privately owned businesses – that is, ones that are owned by individuals or groups of owners rather than by the government.

<table>
<thead>
<tr>
<th>Private businesses (private sector)</th>
<th>Public businesses (public sector)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sole traders</td>
<td>Government-owned businesses</td>
</tr>
<tr>
<td>Partnership</td>
<td></td>
</tr>
<tr>
<td>Companies (including multinationals)</td>
<td></td>
</tr>
</tbody>
</table>

Operating as a **sole trader** is the most common way of owning a business and the easiest way to set up. Examples include street-corner flowers or drinks sellers in cities, tailors and operators of shoeshine services. A sole trader is a business owned by one person – though it may still employ a large number of people.

The table below shows some of the advantages and disadvantages of setting up as a sole trader rather than as a larger business.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>It is easy to set up; no special paperwork is required</td>
<td>Having unlimited liability puts personal possessions at risk</td>
</tr>
<tr>
<td>It is usually a small business; less capital is required</td>
<td>Finance can be difficult to raise</td>
</tr>
<tr>
<td>Speedy decisions can be made by the owner – few people are involved</td>
<td>The small scale of the business limits discounts and other benefits of large-scale production</td>
</tr>
<tr>
<td>Personal attention can be given to business affairs</td>
<td>Prices are often higher than those of larger organisations</td>
</tr>
<tr>
<td>Special services can be offered to customers</td>
<td>Ill health, holidays, etc. may affect the running of the business</td>
</tr>
<tr>
<td>A sole trader can cater for the needs of local people; because the business is small, the owner comes into contact with the customers</td>
<td>Only one owner may mean a narrow range of skills</td>
</tr>
<tr>
<td>Profits do not have to be shared</td>
<td>Mistakes may be more likely because there are no colleagues to consult for advice</td>
</tr>
<tr>
<td>Business affairs can be kept private</td>
<td></td>
</tr>
</tbody>
</table>

**Unlimited liability**

When you set up a business you will need capital to run it. Sole traders have only their own resources to draw on. They will finance their business through savings, and borrowing from banks and on their credit card.
Any debt that a sole trader builds up has to be paid by the owner. The owner is personally responsible for all the debts of the business. This situation can be contrasted with larger companies. Owners of a company have legal protection known as limited liability: this limits the debts owed by an individual owner of a company to the sum of money that person has put into the business. In contrast, sole traders’ debts are unlimited. If the sole traders find themselves in debt, they may have to sell their house, car, etc. in order to pay what they owe.

**Partnerships**

A partnership is a business association between two or more owners of an enterprise. Setting up a partnership usually involves creating a legal agreement between the partners. Partnerships usually have between 2 and 20 members, though this can vary. In some countries, legal restrictions allow a maximum of 20 partners. Partnerships are common in many types of business – small shops as well as professional practices for vets, doctors, solicitors and dentists.

The table shows the advantages and disadvantages of setting up a partnership.

<table>
<thead>
<tr>
<th>Advantages</th>
<th>Disadvantages</th>
</tr>
</thead>
<tbody>
<tr>
<td>Capital comes from partners, so more capital is available</td>
<td>There is unlimited liability (except for ‘sleeping partners’, who put money into the business but do not get involved in its running)</td>
</tr>
<tr>
<td>Partnerships are larger scale than sole traders</td>
<td>There may be disagreements between partners</td>
</tr>
<tr>
<td>Members of family can join</td>
<td>The number of partners is limited (in many countries it is restricted by law to maximum of 20)</td>
</tr>
<tr>
<td>Affairs can be kept private</td>
<td>If the partnership was set up by legal agreement, it will need to be re-formed if one partner dies</td>
</tr>
<tr>
<td>Risks and responsibilities are spread among partners</td>
<td></td>
</tr>
</tbody>
</table>

Most partnerships are not protected by limited liability.

**SUMMARY QUESTIONS**

1. Abdul is considering setting up a small business repairing broken windows and is not sure whether to set up as a partnership or a sole trader. What would be the benefits of forming a partnership in terms of the following?
   - Access to capital / liability / ease of setting up the business / access to skills
   - What other advantages might there be to setting up a partnership?

2. What is limited liability? How does not having limited liability disadvantage many sole traders and partnerships?

3. Set out a table showing the main differences between partnerships and sole traders.

**ACTIVITY**

Choose a business and decide on its purpose. Set out a partnership agreement between yourself and a friend for a small enterprise that you could set up.

The agreement should cover:
- who will provide the capital, and how much
- how the profits or losses will be shared
- the duties of the partners
- when profits will be taken from the business (e.g. monthly)
- procedures for bringing in other partners and for settling disputes.

**DID YOU KNOW?**

In limited partnerships, one or more of the partners can have limited liability: if a partnership runs into debt, the maximum amount in law that partners are expected to lose is what they put into the business. Limited partners would not have to sell off private possessions to pay off the debts of the partnership.

**KEY POINTS**

1. A sole trader enterprise is owned and run by one person. A partnership is owned and run by two or more people.

2. Sole traders and partners typically do not have limited liability. Capital raised is restricted to the person’s own savings, borrowing and any profits made.

3. Sole traders have control over their own business and take all the profits.

4. Partners can share skills and spread the workload of running the business.
A company

‘Company’ suggests a group of companions who have come together to set up a business. The business they set up becomes a legal body, separate in law from the owners. To become a company, a business needs to become legally incorporated. This involves registering the company with the Registrar of Companies in the country in which the company has its head office.

The owners of a company are its shareholders. They appoint a board of directors to make the strategic decisions. The decisions they make include how much profit to distribute to shareholders, and what direction the business should take. The managing director is the senior director, with the lead role for managing the business.

The following are some reasons for incorporating a business.

- If the business gets into financial difficulty, shareholders risk losing only the value of their shareholding in the business. Their private possessions are protected by limited liability and only the assets of the business are at risk.
- An incorporated business is easier to sell than an unincorporated one, because all the complicated arrangements of setting up the business have already been done. Companies are expected to keep detailed accounts so that buyers can immediately see how the company is doing financially when they buy it.

The main disadvantages of a company concern the administration needed to register the company and the requirement to produce annual reports. Detailed accounts have to be kept.

The table shows the two types of limited companies.

<table>
<thead>
<tr>
<th>Private companies</th>
<th>Public companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Shares can only be bought direct from the company with the permission of the board of directors.</td>
<td>1 Shares can be bought and sold on a stock exchange. Anyone can buy them.</td>
</tr>
<tr>
<td>2 The company usually has quite a small number of shareholders. It may be a family-run business.</td>
<td>2 The company can have a large number of shareholders (may be millions) all over the world.</td>
</tr>
<tr>
<td>3 It has access to less capital than a public company.</td>
<td>3 It has access to more capital.</td>
</tr>
</tbody>
</table>

The main advantage of being a private company is that the original owners can stop outsiders from buying up their company. Having a smaller number of people from whom to draw funds, however, may restrict growth. The main advantage of being a public company is access to large amounts of capital, which enables growth.

Franchises

A franchise business is made up of a franchisor and franchisees. The franchisor is an established enterprise (often a public limited company) with a well-known name and products or services. The franchisor grants a licence to a franchisee to produce a product, sell products or provide services in a given area. Examples of franchises include food franchises (e.g. a McDonald’s franchise), a coffee shop franchise (e.g. Costa Coffee or Starbucks), and retail franchises (e.g. United Colors of Benetton) operating in over 120 countries.
Franchisees pay for the franchise to trade in a given area, but will receive training and equipment from the franchisor. They will be expected to share the profit with the franchisor.

The main advantage to franchisors is that they only have to invest a limited amount of capital in each franchise, but they take profits from the franchisee. The franchisee benefits from working with a proven business idea, trading under a well-known name and getting support and materials from the franchisor.

ACTIVITY

Speak to a franchisee in your own country. Find out how the person came to be in the business. What is the relationship with the franchisor? Share your findings with the class.

Joint ventures

A joint venture is formed when two independent businesses set up a new enterprise in which they jointly own a stake. It can take the form of an incorporated business or a partnership. Joint ventures are commonly used when a business from one country wants to enter a new country, but prefers to do so with a local partner. The local partner will have a lot of contacts and know how to conduct business in that market. A lot of oil companies create joint ventures to search for and then exploit oil reserves. Many Western companies have created joint ventures when entering the Chinese, Indian and other South East Asian markets.

Not-for-profit organisations

Not-for-profit organisations have objectives other than making a profit for their owners. A good example is Amnesty International – its objective is to protect human rights worldwide. Any money made by a not-for-profit organisation is used to keep it running and to meet its objectives. In most countries such an organisation is free of government taxes. Money is earned from selling goods and services and from donations. Where an excess of income over spending is made by a not-for-profit organisation this is termed a surplus rather than a profit.

SUMMARY QUESTIONS

1. Why might a group of friends setting up in business for the first time prefer to create an incorporated rather than an unincorporated business?
2. What benefits might a Western European manufacturer of chocolate and confectionery products gain from setting up a joint venture with an existing Chinese manufacturer rather than setting up its own independent plant in China?
3. Fast-food franchises such as McDonald’s are found in many countries. What would be the advantages to a local franchisee of working with McDonald’s rather than setting up his or her own food business?

KEY POINTS

1. A company is owned by shareholders who are able to bring capital into a business.
2. Shareholders are protected by limited liability. The financial risk is limited to the value of the shares they hold.
3. Another way for a business to grow with less risk to its own capital is to sell franchises.
4. A good way of entering a foreign market is to create a joint venture with a local company.
Students should be able to:
- understand the role and function of entrepreneurship
- understand the concept of risk and ownership
- understand the concept of limited liability.

Risk and ownership

One of the words most commonly associated with business is risk. The owners of a business risk the capital that they put into it. The capital may come from their life savings, from money they have received in redundancy pay, or even a loan secured against their house or other valuable possessions. More businesses fail than succeed, and the casualty rate of new businesses is particularly high in the first year of trading.

This principle of risking capital is the same for sole traders, partners, shareholders in a company, franchise operators and owners of joint ventures.

The owners of a business are liable for its debts. The amount of liability that sole traders and most partners are accountable for is not restricted to the sums that they have put into the company. They are required by law to meet all the liabilities of their business. As we have seen, this could mean having to sell their car, their house and other possessions to meet business debts (see 1.2.1).

Limited liability

In the 1850s, the British and French governments passed laws that would allow individuals and groups to invest in companies. This was the principle of limited liability (see 1.1.2). It limits the risk for a shareholder to the sum that person has invested in a company.

Most large businesses are set up as limited companies (incorporated businesses). These companies have shareholders. A shareholder might...
be an individual, with only a small sum of money invested in, say, companies such as Singapore Airlines, Nestlé or Tata. Alternatively, the shareholder might be a huge pension fund, investing the savings of millions of pensioners in these companies. These shareholders would not buy shares in companies if they were held liable for business debts.

Shareholders → invest money in → limited companies.

Shareholders may be individuals or other companies. They are not responsible for the company’s debts unless they have given guarantees (e.g. of a bank loan). However, they may lose the money they have invested in the company if it fails.

The protection of limited liability therefore makes it possible for companies across the globe to raise large sums of money. The Swiss multinational company Nestlé is famous for its products such as Nescafé and Quality Street sweets. The company has over 250,000 shareholders and no single shareholder owns more than 3 per cent of the shares in the company. Each of the 250,000 shareholders is willing to invest in the company because they think that it has good prospects to make profits, and they know that because of limited liability, the maximum amount of capital that they are risking is the value of their shareholding.

**SUMMARY QUESTIONS**

1. Which of the following would have limited liability?
   - An incorporated business / a sole trader / an ordinary partnership / a company / a limited partnership

2. Singapore Airlines is owned jointly by the government of Singapore and by private shareholders. The Singapore government has the majority shareholding in the airline. The airline is an incorporated business. How much would an individual shareholder be liable for in the event that the airline had to meet debts?

3. In what ways might it be more risky to set up a sole trader business than a small incorporated company?

**DID YOU KNOW?**

Some forms of business organisation are specific to particular countries. Indian law recognises the joint Hindu family form of business ownership: members of a family own a business and the eldest member manages it. All members of the family get a share of the profit, regardless of how much they participate. Apart from the eldest member, the liability of the partners is limited.

**KEY POINTS**

1. Limited liability is a legal protection that reduces the risks involved in business.

2. A shareholder or other owner of a business with limited liability is only liable for the value of his or her investment in a business.

3. There are certain types of partnerships that have limited liability status. However, in ordinary partnerships there is unlimited liability of partners.
The private and public sector

Another major classification is into the public and private sectors. The private sector consists of businesses that are owned by private individuals (people that own and run businesses directly themselves) and businesses that are owned by shareholders (people who have bought a share in a company and have the right to share in the profits of the company and to appoint directors to run the business on their behalf).

Most economies in the world today consist of a mix of private sector and public sector enterprises, so they are called ‘mixed economies’.

In some economies the majority of production is carried out by state-owned (government-owned) enterprises. For example, in China and Cuba government-owned enterprises (the public sector) are responsible for the majority of production. In contrast, in the United States, Canada, Mexico, Japan and the EU countries the majority of production is carried out by private businesses in the private sector.

Over the last 20 years, the size of the private sector has increased. For example, in countries such as China and Cuba, where in the past business activity was almost exclusively in government hands, the government has allowed an increasing number of private sector businesses to set up, particularly in the small business sector (e.g. hairdressers, taxi firms, photocopying companies). Increasingly, the government in the People’s Republic of China has encouraged the set up of large private sector businesses that can be competitive on the world stage such as the computer company Lenovo.

You will see in Unit 2, however, that private enterprises may have additional, or secondary, objectives. India’s Tata Group of companies created India’s first steel plant, hydroelectric plant and inorganic chemistry plant. Today the group has operations in six continents and produces many different goods. The group is not concerned solely with profits, for example – in 1941 it created the Tata Memorial Hospital, India’s first hospital for the treatment of cancer.

Setting up and running a private enterprise involves risk. The person who takes this risk is an entrepreneur. If the business succeeds, the entrepreneur makes a profit. Should it fail, he or she will be
responsible for the losses. The loss could involve having to sell personal possessions, in order to meet the business debts.

Public enterprise

In many countries, the government is a major employer. Governments employ public sector workers to carry out work on their behalf, such as providing a police force, education and a health service. The size of the public sector varies from country to country. Figure 1.2.4.2 shows some of these differences.

The goal of a public sector enterprise such as Indian Railways is to provide an essential economic service for the nation. Hundreds of millions of people in India rely on the railway service to get around the country and to transport goods.

Public sector enterprises need to be carefully run. They are often funded by taxpayers’ money, so they need to look after the taxpayers’ interests by providing the best possible value for money.

STUDY TIP

The process of taking an activity into the public sector is nationalisation. Sometimes activities are denationalised or privatised. Think about why such changes might be necessary.

ACTIVITY

Identify a public sector company that operates in your country. When did this company become part of the public sector? What are the main activities of this company?

DID YOU KNOW?

In India, large numbers of people work for government-owned businesses, including India’s largest employer, Indian Railways. The energy companies are also state-owned, as is Indian Airlines.

Indian Airlines is currently facing major competition from the new privately owned low-cost airlines, especially Indigo Airlines, India’s fastest-growing business.

SUMMARY QUESTIONS

1 Explain how goals of public sector organisations may differ from those in the private sector.

2 Read the following statements and then suggest whether the organisation is more likely to be in the private or public sector.
   - Our goal is to make a profit for our owners. We will achieve this by providing excellent customer service.
   - Our goal is to provide an efficient postal service to every single household in the country. This includes providing deliveries every day to out-of-the-way locations.
   - Our goal has always been to make a profit. If we provide additional benefits to the wider community, this is a bonus.

3 Classify the following according to whether they are primary, secondary or tertiary and private or public sector:
   a a state-run mining company
   b a telecoms company owned by shareholders
   c a small family-run hotel company
   d a government-owned steel manufacturer
   e a joint venture between a family business in China operating in insurance and a foreign company.

KEY POINTS

1 The private sector of the economy consists of firms that are owned by private individuals including shareholders.

2 The public sector of the economy is the state-run sector.

3 In recent years there has been a tendency in many economies for a reduction in the number of state-run enterprises.

DID YOU KNOW?

In India, large numbers of people work for government-owned businesses, including India’s largest employer, Indian Railways. The energy companies are also state-owned, as is Indian Airlines.

Indian Airlines is currently facing major competition from the new privately owned low-cost airlines, especially Indigo Airlines, India’s fastest-growing business.
What is a public corporation?

Public corporations are businesses owned by governments. Although the government owns the corporation, the controllers of the corporation are given considerable freedom to make their own decisions. Sometimes they are referred to as stated-owned enterprises (SOEs) or government-owned corporations (GOCs). In India the term ‘public sector undertaking’ (PSU) is used.

A public corporation is created by passing a law to create the new form of business. The government then appoints a chairperson and a board of managers to lead it.

**DID YOU KNOW?**

Government-linked companies (GLCs) are companies in which the government owns some of the shares in the business.

**CASE STUDY**

The Saudi Arabian Oil Company

The Saudi Arabian Oil Company is owned by the Saudi government because oil is such an important resource to the Saudi Arabian economy. The Saudi government controls the amount of oil produced, which in turn has an impact on the world oil price.

As in any business, governments usually set yearly targets for particular public corporations. The chairperson and the managers must then decide on the best way to meet these targets. With an oil corporation, the government may set a target for the number of barrels of oil to produce in a country. The managers of the oil company will then decide how much to produce from each oilfield and how to maintain supplies for future years. The managers will also supervise the marketing and selling of the oil. Agreements about how much oil to produce and the price to charge has to be agreed between members of OPEC (Organisation of the Petroleum Exporting Countries).

**Questions**

1. Why do you think the Saudi Arabian Oil Company is run as a public corporation rather than as a private sector business?
2. What types of decision are made by the Saudi Arabian Oil Company? How are these decisions important to the economy of Saudi Arabia?

**PURPOSES OF PUBLIC CORPORATIONS**

Public corporations are often created to make sure that important activities that affect the whole nation are carried out well. Indian Railways is a PSU: every day millions of people travel on Indian railways and goods are transported all over India. In most countries there is also a state broadcasting company such as the British Broadcasting Company (BBC). The purpose of the BBC is to try to present news in a fair way that is not influenced by political or commercial interests.
Sometimes public corporations are set up to preserve jobs. The government is able to support public corporations through money it raises from taxpayers. This enables the government to provide services to locations where it is not economical to provide them, such as water supplies to areas of water shortage. In Libya water supplies are transported over 4000 kilometres, down a huge water pipe from under the Sahara Desert to major areas of population.

Government involvement in a particular industry can also reduce wasteful competition. For example, the government might provide the only electricity or water supply using one set of cables and pipelines. This saves having wasteful duplication of pipelines.

When a business or industry is taken over by the government this is described as nationalisation. Selling a public corporation to shareholders is called privatisation.

**ACTIVITY**

Saudi Airlines was recently privatised. Carry out some internet research to find out why this happened. What do you expect the benefits of the privatisation to be? Who owned the airline prior to the privatisation? Who owns it now? Produce a report of your findings.

**KEY POINTS**

1. A public sector business is owned by the government.
2. These businesses have other objectives than just to make a profit.
3. Public sector businesses do not always use resources as efficiently as they would if they faced greater competition.

**SUMMARY QUESTIONS**

1. Give examples of three public corporations in different countries.
2. Suggest three reasons why governments set up public corporations.
3. Why are public corporations sometimes privatised?
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**1 Understanding business activity**

**1.1 Purpose of business**

1.1.1 The purpose and nature of business

**Satisfying wants and needs**

Businesses are usually set up to satisfy the wants and needs of customers. Some businesses are set up to satisfy the wants and needs of other businesses. Businesses may be set up in order to make a profit. Businesses may be set up to satisfy the wants and needs of the country as a whole.

**ACTIVITY**

Copy the following sentence and place the names of the wants and needs into the appropriate boxes.

(a) I want a house. (b) I need a roof. (c) I want a glass of orange juice. (d) I need a glass of orange juice.

**SUMMARY QUESTIONS**

1. List two wants and two needs.
2. Explain what is meant by the phrase ‘needs and wants’.
3. Identify two ways in which the needs and wants of a business may differ from those of an individual.

---

**Adding value**

Businesses are able to provide products and services that are more attractive than those of their competitors. Everything that a business produces or supplies is made up of its inputs.

**KEY POINTS**

- Businesses add value to products and services. This is done by adding value to the finished product or service.
- Adding value is the process of increasing the worth of a product or service.
- Adding value can be done by improving the quality of a product or service.

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**Business activity is concerned with satisfying these wants and needs.**

**Serving the customer**

Businesses are set up to satisfy the wants and needs of the customer. Customers are willing to spend money to satisfy these wants and needs.

**SUMMARY QUESTIONS**

1. Explain the difference between producing goods, supplying goods, and serving the customer.
2. Identify three ways in which businesses add value to their products or services.
3. Explain the importance of customer satisfaction.

---

**Scarcity**

Businesses cannot produce everything they want to produce. Business activity is concerned with satisfying these wants and needs. The art of producing a good or service is to satisfy a customer's wants and needs.

**SUMMARY QUESTIONS**

1. Define ‘scarcity’.
2. Explain how businesses can satisfy their customers when there is scarcity.
3. Identify three ways in which businesses can overcome scarcity.

---

**1.1.1 The purpose and nature of business**

- Businesses are set up to meet the wants and needs of customers.
- Businesses produce goods to meet the needs of consumers.
- Businesses produce goods to meet the needs of consumers.
- Businesses produce goods to meet the needs of consumers.

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**Costs of producing goods**

- Businesses produce goods to meet the needs of consumers.
- Businesses produce goods to meet the needs of consumers.
- Businesses produce goods to meet the needs of consumers.
- Businesses produce goods to meet the needs of consumers.

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