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# BUSINESS

AN INTRODUCTION

STEAD E AND LOWRY

ELEVENTH EDITION





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# BUSINESS

## AN INTRODUCTION

### ELEVENTH EDITION

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# Preface

Two students were chatting over coffee. One asked the other, "How's your part-time job?" The other replied, "Compared to what?" And so it is when telling you about this textbook. Although some of the features in this text also may be found in other "Intro to Business" texts, we feel the Eleventh Edition of BUSINESS: AN INTRODUCTION (Stock No. G75) remains unique in what it gives you. So, let's be more specific about what this Eleventh Edition offers when compared to most other "Intro" textbooks and to our previous editions.

## ELEVENTH EDITION HIGHLIGHTS

The key strength of this textbook is its philosophy of providing a comprehensive and balanced coverage of business. Over more than 35 years there have been only four main authors of this text, and we still hold firmly to this philosophy. The instructor who selects this textbook is saying, in effect, "I want a textbook that gives the students their money's worth with a substantive and complete coverage of the topics. I don't want a superficial, 'show and tell' presentation; rather, I want a tightly written, intensive textbook that introduces carefully our remarkable business system to my students."

Business is a complex and dynamic activity, and we want to present this picture to students as they start their study of business. This holds true for nonbusiness and business students at both the undergraduate and MBA levels. In other words, we see this book as an educator, not an entertainer.

Another strength of this book is balance. It emphasizes both traditional concepts and up-to-date materials that will remain current throughout the entire edition. For example, new topics in this edition include current thinking about economic theories of capitalism, corporate culture, the McKinsey 7-S managerial framework, innovation and Gifford Pinchot's "intrapreneurship," Ouchi's Type Z organization, levels of proactive unionism, nature and use of quality circles, expanded coverage of Kanban or just-in-time (JIT) systems, nonbank financial institutions and shared networks, nonstore selling, greenmail and leveraged buyouts, and challenges associated with operating one's own business. Furthermore, a revision highlight of this edition is the use of many documented, real-world examples.

And speaking of the "real world," a new comprehensive case shares with you the actual lessons learned by Howie Snider, a retired U.S. Marine Corps pilot, when he struggled to succeed as the owner/operator of a franchised pizza restaurant. Are you interested in becoming an independent business operator? If so, this may be the most important case you'll read in college. We are grateful to Colonel Snider for the "window of business" that he has provided for our comprehensive case.



The study of business should be exciting and rewarding, not boring or tedious. And there should be no confusion about what each chapter covers. Therefore, we start each chapter in this edition with a chapter outline, an incident that asks for your opinion, and a list of learning objectives. All these provide a current stepping-stone into the chapter.

You will find a comprehensive glossary of business terms at the end of this book. We think you will find this a handy reference for the terms indicated in bold type within the chapters and a good general reference for other business courses. Finally, the supplementary publications that accompany this Eleventh Edition and that are described below have been thoroughly revised.

### **STUDENT STUDY GUIDE**

Each chapter of the *Student Study Guide* (Stock No. G751) helps the student in three basic ways:

1. "Reviewing What You Have Read" consists of (a) organizer and chapter goals, (b) a study outline, (c) a list of terms to know, and (d) data checks on illustrative materials in the text.
2. "Practicing for Exams" includes (a) a vocabulary review in which the student is asked to define key terms, (b) true-false questions which require the student to provide a concise comment regarding why a statement is false, and (c) multiple-choice questions.
3. "Applying Your Knowledge" presents an opportunity to analyze several recent articles from business publications such as *Fortune*, *Business Week*, *Nation's Business*, *Business Horizons*, *The Wall Street Journal*, and many others.

### **INSTRUCTOR'S RESOURCE MANUAL**

Each chapter of the *Instructor's Resource Manual* (Stock No. G75M)\* aids the instructor by providing:

1. Opening comments on the key points for the chapter.
2. A lecture outline which includes objectives and key terms, with keyed-in resources.
3. Topics for lecture and discussion.
4. Notes about the transparency masters.
5. Comments on "What's Your Opinion?" openers in the text.
6. Answers to Questions for Discussion and Analysis in the text.
7. Solutions to Applications in the text.

Also in the *Instructor's Resource Manual* is a test bank which includes 800 objective-type questions (grouped into a Set A and a Set B, and selected from among the 2,400 questions appearing in the Examinations Book), mid-term essay exams, final essay exams, and all accompanying answers.

As with previous editions of the *Instructor's Resource Manual*, an alternative comprehensive case is provided.

## EXAMINATIONS BOOK AND MICROSWAT DISKETTES

The *Examinations Book* (Stock No. G75E)\* consists of 2,400 true-false and multiple choice questions. These questions are grouped around main topics of each chapter. The answers to these questions, as well as textbook page references to the answers, are presented in such a way that they can be "blocked out" by the instructor who wishes to make multiple copying-machine copies of the pages in this publication.

To instructors who are interested, these test questions are also available on MicroSWAT diskettes (Stock No. G757-3T\* for use with Apple computers and Stock No. G758-1T\* for use with IBM personal computers).

## TRANSPARENCIES

For the Eleventh Edition of *BUSINESS: AN INTRODUCTION*, a package (Stock No. G75V)\* of 104 transparencies has been prepared. One-half of these transparencies are brand new for this edition.

## ACKNOWLEDGEMENTS

We would like to thank the following persons for their criticisms and suggestions that guided us in preparing the manuscript for this edition: John F. Chisholm, Jr., Allegany Community College; Walter G. Connell, Montgomery County Community College; Bernard W. Weinrich, St. Louis Community College at Forest Park; Herb Tedder, Northwestern Michigan College; and John J. Balek, Morton College.

We also wish to thank Ed White, Danville Community College, author of the *Student Study Guide* and the *Examinations Book* and co-author of the *Instructor's Resource Manual*; and Carolyn Wiley, Texas Woman's University, co-author of the *Instructor's Resource Manual*.

Finally, we want to recognize the years of work lavished on this textbook by one of its original authors, Ray Glos. Dr. Glos is Dean Emeritus of the School of Business Administration, Miami University, Oxford, Ohio. He actively pursued excellence and quality long before this became the thing to do.

We feel good about this edition, and we hope you will, too.

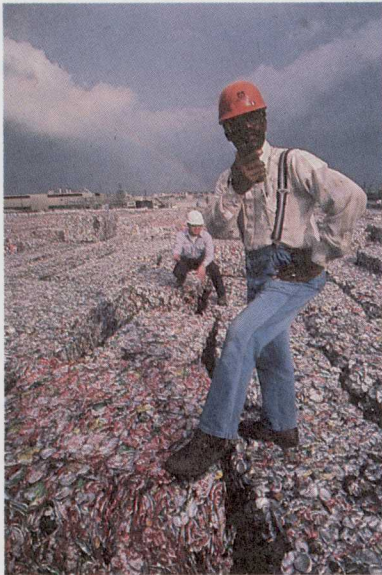
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\*Items marked with an asterisk are provided free of charge to adopters of the textbook.



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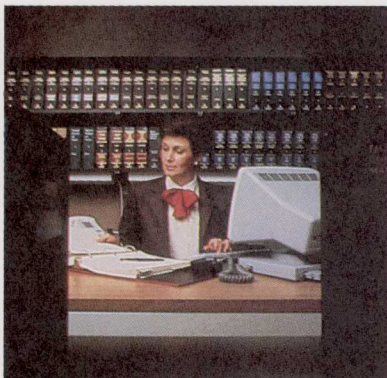
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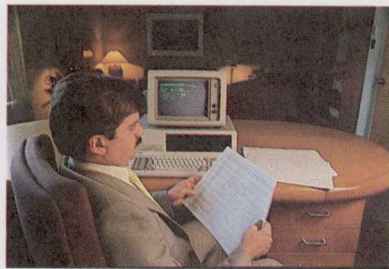
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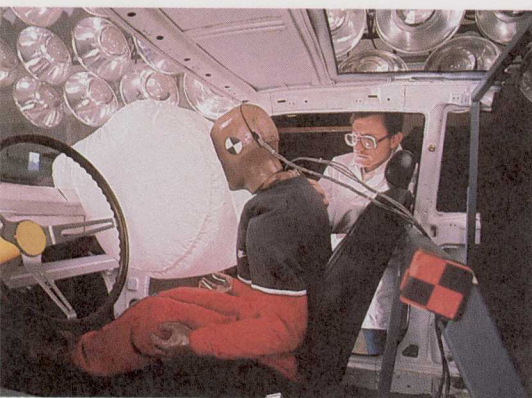
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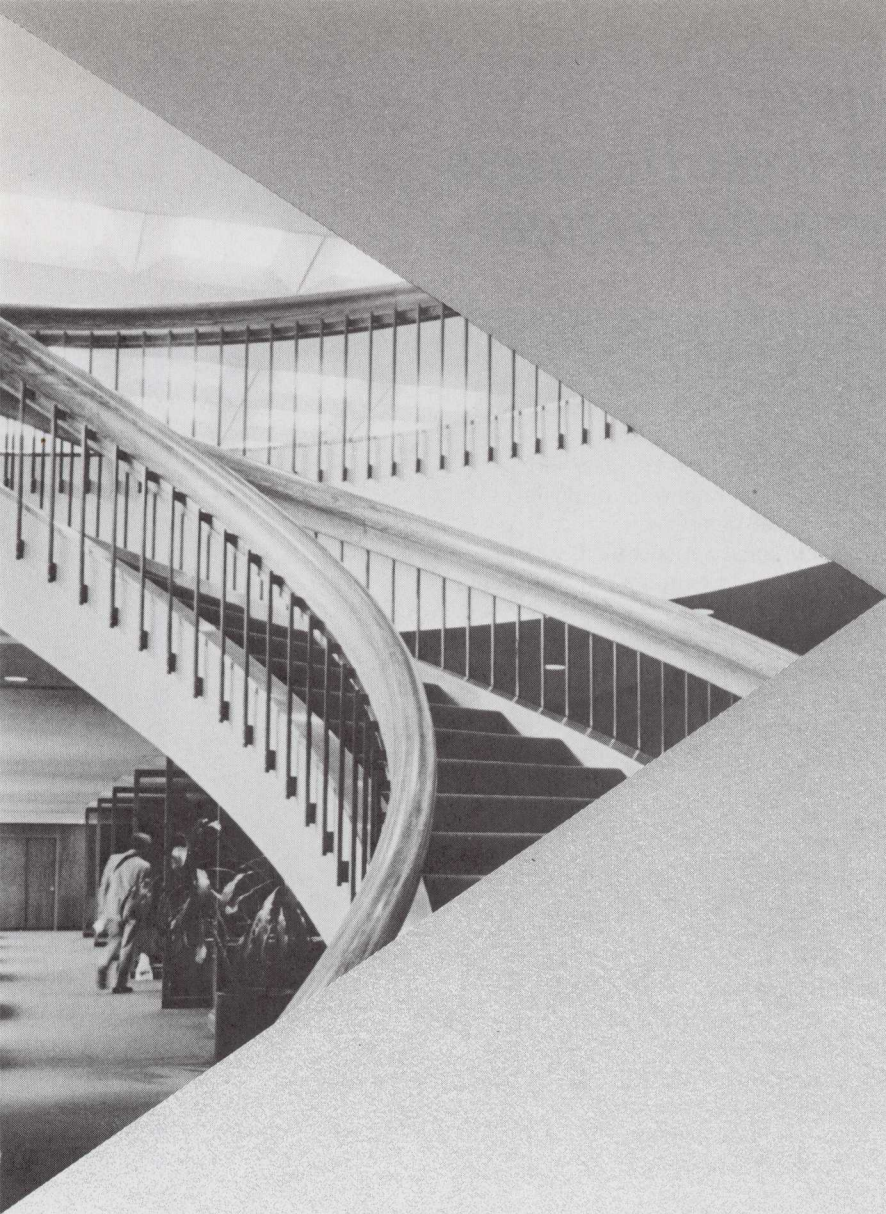
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# *Chapter 1*

## *American Business Enterprise System*

### **Chapter Outline**

- I. Elements of Our Business Enterprise System
  - A. Business: A Key Social Institution
    - 1. Structure of Business
    - 2. Sizes and Types of Business Firms
    - 3. Institutional Framework of Business
  - B. Constitutional Democracy
    - 1. Constitutional Support for Business
    - 2. Business and Government Relationship
  - C. American Capitalism
    - 1. Basic Freedoms of Capitalism
      - a. Private Property
      - b. Private Enterprise
      - c. Freedom of Choice
    - 2. Key Factors of Capitalism
      - a. Capital
      - b. Risk
      - c. Profit
    - 3. Roles and Gainful Relationships in Capitalism
      - a. Entrepreneurs
      - b. Managers
      - c. Workers
      - d. Consumers
      - e. A Gainful Relationship for All?
- II. Economic Theories of Capitalism
  - A. Tools of Economic Policy
  - B. Current Economic Theories
    - 1. Keynesian Economics
    - 2. Supply-Side Economics
    - 3. Monetarism
- III. Other Economic Systems
  - A. The Socialist Economic System: In Theory and Practice
  - B. The Communist Economic System: In Theory and Practice
  - C. The Emergence of Creeping Capitalism



It is late 1982 and you are the chief executive officer of a major consumer products firm that has been invited by the Los Angeles Olympic Organizing Committee to bid for recognition as one of the 30 official sponsors of the 1984 Summer Olympic Games. You are aware that the 1984 Summer Olympics will be unique. For the first time, corporate America will pay nearly all of the event's \$500 million in costs. In fact, the city of Los Angeles has passed a resolution saying that not one cent of municipal funds will be spent on the games.

The stakes are high. For example, McDonald's is paying \$5 million in sponsorship fees directly to the Los Angeles organizers, spending \$4 million building a swim stadium and giving \$1 million to the US Olympic Committee. In addition, McDonald's is booking over \$20 million in prime-time Olympic television advertising costs. Indeed, companies that become sponsors must pay from \$4 million to \$15 million in sponsorship fees, and this doesn't cover advertising.

You wonder about your competitors, your shareholders, and the risks of corporate sponsorship. If you don't pay the tab for sponsorship, in all probability one of your top competitors will. And the sponsoring companies will be offered the chance to buy large blocks of tickets that can be used to entertain important customers. Yet, you expect that each sponsor will catch flak from some shareholders and other observers for spending corporate earnings so lavishly. Moreover, sponsors risk an anticommercial backlash from the possibility of promotional overkill. Some people may even argue that commercial use of the Olympics is affordable only by the richest companies when, in fact, the Olympic Games are owned by the people of the world.

In previous games, Olympic money problems were government and taxpayer problems. Canadian taxpayers are still paying off \$1 billion, rather than \$500 million, to put on the 1976 Games in Montreal. But this also included major new construction projects. Other government problems in previous games included acts of terrorism and the imposition of a boycott on the 1980 Moscow Games by the United States. Will political actions once again dampen the image of the Games?

And generally you wonder who should foot the bill for the Olympic Games—business or taxpayers? Is commercialization consistent with the Olympic movement? What will this commercial involvement mean to your company and to the image of business in the United States?

### **WHAT'S YOUR OPINION?**



### Objectives

1. Identify the three main elements that form our business enterprise system.
2. Explain why business is a key social institution in the United States.
3. Distinguish between industrial and commercial businesses.
4. Identify and explain three basic freedoms in our capitalistic economic system.
5. Explain the importance of capital and risk to capitalism.
6. Explain three ways in which profit is crucial to our capitalist economic system.
7. Explain the gainful relationship represented in the circular flow of economic activity.
8. Distinguish among Keynesian, supply-side, and monetarist economic theories of capitalism.
9. Distinguish between the use of monetary policy and fiscal policy as economic policy tools.
10. Distinguish among capitalist, socialist, and communist economic systems.

**The inherent vice of capitalism is the unequal sharing of blessings; the inherent virtue of socialism is the equal sharing of miseries.**

**Winston Churchill**

Over two hundred years ago, in 1781, the Continental Congress turned to Robert Morris, an affluent Philadelphia merchant, to head the Office of Finance and deal with the unstable economy in the closing years of the Revolutionary War. As one author put it, "Morris aptly described what lay before him: 'The Derangement of our Monetary Affairs. The Enormity of our Public Expenditures. The Confusion in all our Departments. The Languor of our General System. The complexity and consequent inefficacy of our Operations' . . . First and foremost, Morris sought to reestablish the financial credit of the U.S. both at home and abroad. This was a prerequisite for creating a nation which he envisioned would ultimately rise to 'Power, Consequence and Grandeur.' His second aim, intrinsically related to the first, was to propel an agrarian, preindustrial nation along the path of economic development. For the Revolution was to Morris as much a struggle for economic as for political liberty. The fruits of independence could be fully secured only by establishing a government committed to encouraging enterprise untrammelled by state economic regulations which violated the 'unrestrained liberty of disposing of private property at the pleasure of the owner.'"<sup>1</sup>

Robert Morris was not alone. At the same time, Thomas Jefferson noted that agriculture, manufacturing, commerce, and navigation were the four "pillars of our prosperity." To this we can add that individual enterprise, or initiative, is the foundation on which these pillars stand. In fact, it was largely



enterprising individuals and organizations seeking private gain who spurred our break with England.

So, our capitalistic business enterprise system has been a key force in the growth of our nation since its founding. Business is the activating element—the engine of growth and productivity—in this system. **Business** is defined as all the commercial and industrial activities that provide goods and services to maintain and improve our quality of life. The purpose of this book is to explain how business combines human, material, technological, and financial resources for profit. Business earns profit by anticipating and satisfying the needs and wants of people in our society and throughout the world.

## ***ELEMENTS OF OUR BUSINESS ENTERPRISE SYSTEM***

In our complex society today, someone must accept the challenge and risk to bring human resources, materials, and capital together before a single gallon of milk can be marketed or a single automobile produced. That job rests with the businessperson. The owner of a lumber mill has to process various types of lumber as efficiently as possible in the amounts and varieties needed. A trucker has to move goods quickly from places where they are not needed to where they are needed. The person who runs a retail store must make a variety of goods available at a price the consumer is willing to pay. These are only a few examples of the almost limitless business activities in our daily lives.

However, our business enterprise system is comprised of more than business firms and activities. It results from the combination of three major elements: business as a social institution, constitutional democracy, and the American capitalistic economy. FIGURE 1-1 shows the relationship of these three elements. Each of these elements will be discussed in this chapter so that we can begin to understand the factors that help shape our enterprise system into a dynamic social and economic force.

### ***Business: A Key Social Institution***

Business is a major institution in our society because its values and consequences are accepted as an important basic part of our lives. Business is also a social institution as it is composed of human groups working toward goals that agree with the overall goals of society.

**STRUCTURE OF BUSINESS.** FIGURE 1-2 shows that the institution of business is formed by industries and business firms. An industry is a distinct group of firms in a particular business activity or area such as automobile manufacturing or entertainment. A **business firm** is a commercial or industrial enterprise owned and organized to buy, sell, manufacture, or provide products or services to society for a profit. This is a broad definition and includes all sizes and types of business firms.