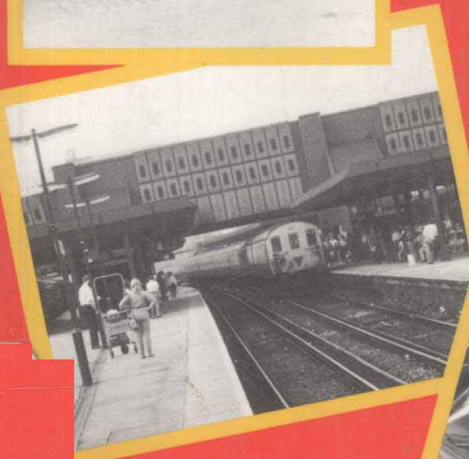
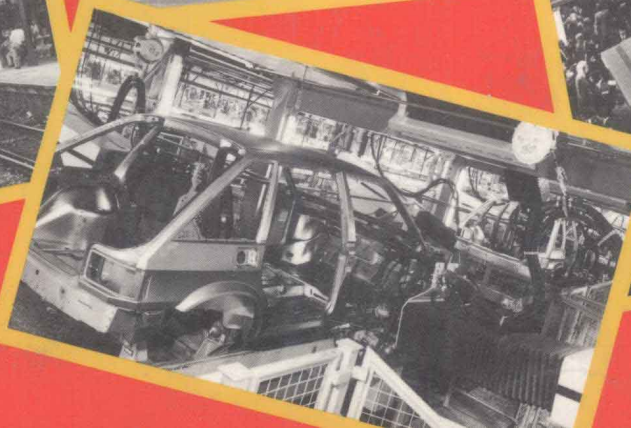
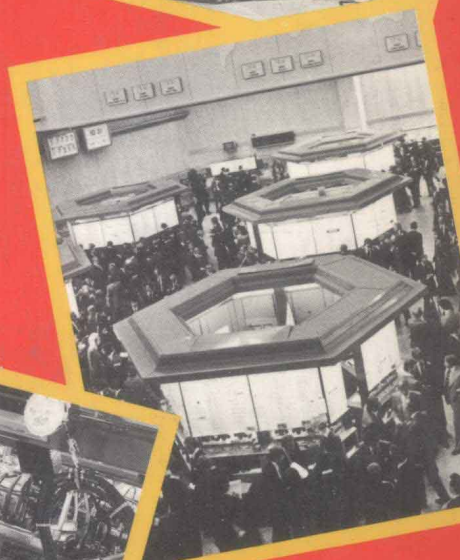
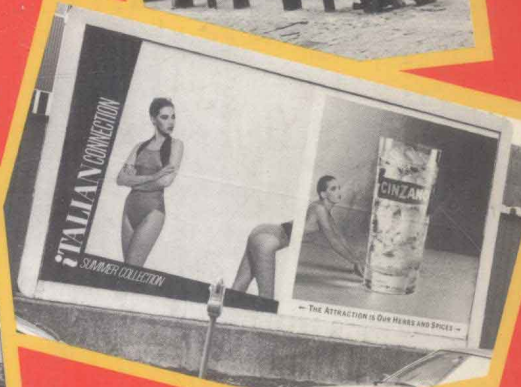
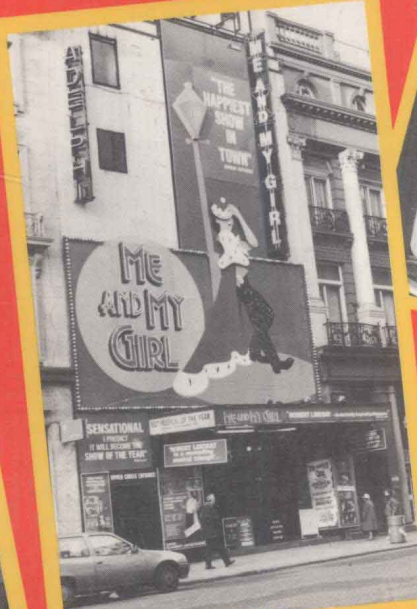
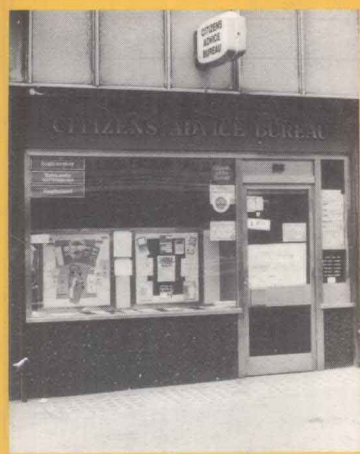


# Comprehensive Business Studies

Alan Whitcomb



Pitman

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# *Comprehensive Business Studies*

**Alan Whitcomb**

BA, MEd, PhD

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# *Preface*

This book is intended for use as a basic text by students preparing for GCSE business studies and other related examinations. Syllabuses obviously vary and some may contain elements not included in this book. However, the aim has been to present a wide-ranging and comprehensive textbook, produced in a readable and interesting style and which can be used in mixed ability situations. It is hoped that the manner in which the material has been presented will prove attractive to students as well as providing support for the classroom teacher.

At the end of each chapter is a section called 'Make a note of it'. This section consists of a series of questions. Some of the questions require only brief answers, others require a more detailed response. All the answers to the questions appear in the text in the same order as they are set in the 'Make a note of it' section. By writing each question followed by the answer the student formulates structured notes on the topic of each chapter. Alternatively, the 'Make a note of it' section can be used to form the basis of a revision test at the end of each unit of study.

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# Part 1 Business structure and organisation

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## 1 *Background to business*

### **Development of economic activity**

#### **Direct production**

Early man was engaged in direct production. He produced all his needs directly for his own use, and unaided by others. He would hunt animals and gather plants and berries for his food. This forced man to lead a nomadic way of life, moving from one fertile area to another and following the herds of animals.

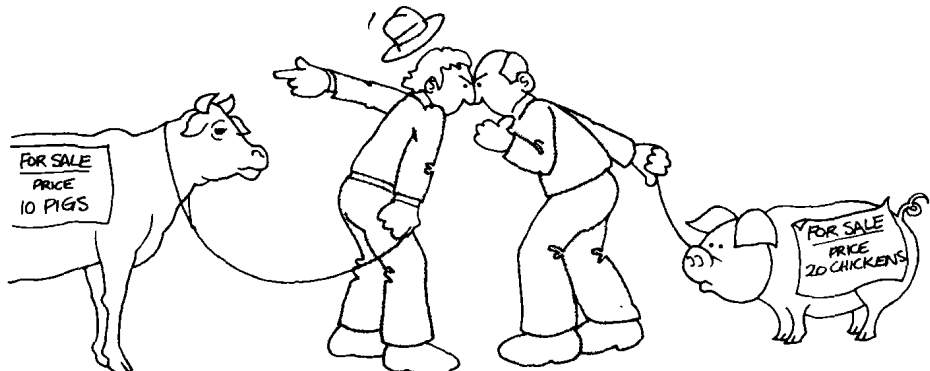
Later man began to farm in a very basic way, penning animals and planting seeds. This enabled him to settle in one place, build a permanent home and improve his way of life. One of the improvements was that he found he was producing more goods than he needed (*surplus*). He began to exchange his surplus goods with the surplus of others.

#### **Barter**

The exchange of one thing for another without the use of money is called barter, and this was the way that the earliest form of trade took place. But there are drawbacks to the barter system, these are as follows:

1 A *double coincidence of wants* has to occur for barter to take place. The person who has a surplus to exchange not only has to find someone who wants his or her surplus, but the person found must also have what is wanted.

2 An *exchange rate* has to be agreed even if a double coincidence of



## 2 Business structure and organisation

wants has occurred. Imagine the difficulty in trying to agree how many chickens a pig is worth.

3 *Divisibility of goods* is not always convenient. Some rates of exchange will not allow exchange to take place because some goods cannot be split into smaller parts. For example, if one spear is worth half a chicken it is not possible to trade with only one spear because you cannot have half a chicken and also have it alive.

4 *Storage of wealth* is difficult with the barter system. At times there is a need to store a surplus for use at a future time when a scarcity exists. But many items used in barter (e.g. food) cannot be stored for long periods of time.

## Money

The use of money solves all of the above problems of barter, but early money was not in the form of coins and notes with which we are familiar today. The difficulties of barter led early man to the use of generally accepted items which everyone was willing to take in exchange for their goods. These items included such things as shells, dogs' teeth, beads, grain, spearheads, hides, arrowheads, fishhooks and animals, and they became substitute money.

Even today many things are used instead of money in some parts of the world, and when a country's economy collapses the people may revert to using goods instead of money. For example, in Germany during the latter part of the Second World War cigarettes, coffee and stockings were used as money.

### *Qualities of money*

For something to be considered as money, or in the place of money, it must be:

- *Durable* (hard wearing)
- *Divisible* (easily divided into smaller units)
- *Portable* (convenient to carry)
- *Acceptable* (people must agree to its use)

The use of money allowed early man to sell his surplus of goods in exchange for money and use the money to buy his needs from the surplus of others. Money was now acting as a *medium of exchange*, and the process of trading was much simpler.

In time metal became a popular substance used as money in any part of the world where it was common, and the use of metal eventually led to the development of the coins with which we are so familiar today. Look back at the list of the qualities of money. Can you see how metal money so conveniently meets all those qualities?

### *Functions of money*

Money has three basic functions. It is a medium of exchange, a measure of value and a store of value.

*Medium of exchange* – money makes trading relatively simple and makes barter unnecessary. It enables workers to specialise in labour and accept

money for wages rather than goods. Workers will accept money because they know it is acceptable to others in exchange for goods.

*Measure of value* – money can be used to measure or price the value of goods and services. This is especially important when the items cannot easily be compared. For example, how many hours of work by a farmer is a tractor worth?

*Store of value* – money can be stored for use at some later time, whereas to store goods such as food for a long time is inconvenient. This makes it possible to ‘save for a rainy day’, to have some wealth to draw on when a scarcity occurs. In other words, money can be earned at one time and spent at another.

## Indirect production

In modern industrial society few people satisfy their needs directly. Instead they co-operate with others to indirectly produce the needs of everyone. This is often referred to as *division of labour* or *specialisation*. Work is divided among several people, allowing them each to specialise in doing what they do best, which is to the benefit of everyone. There are two main ways of looking at specialisation.

### *Specialisation by product*

Instead of everyone trying to produce all they personally need, they each concentrate on contributing to one commodity or service, using the money that they earn to purchase the goods or services of others. In this way the total needs of an individual are met by the contributions of many others.

### *Specialisation by process*

By organising production into several stages or processes workers become more specialised and expert in their work. For example, in a car factory each worker might specialise in a part of the assembly of many vehicles in one day as they pass along the production line. By organising production in this way, workers become more specialised and expert in their work. This enables them to produce more with the same resources.

### *Advantages and disadvantages of specialisation*

#### *Advantages*

- Workers become skilled at doing a particular job
- Jobs become simpler and easier to learn
- Time-saving machinery and semi-skilled labour can be used
- Costs per unit produced are less because of the simple processes and better use of labour and tools

#### *Disadvantages*

- Repeating a single task can become boring
- Individual crafts and skills are lost by use of machines
- Greater use of machinery can lead to unemployment of workers
- All production may be halted by strikes, machinery break-down or shortage of materials

#### 4 Business structure and organisation

- Labour is potentially more mobile
- Slow workers may be unable to keep pace with others



*Above and right: high speed machine wrapping*

*Courtesy of Cadbury Ltd*



## Scarcity and choice

In a world where specialisation has become highly developed with not only individuals but whole communities specialising, it is vital for exchange to take place if everyone's wants are to be satisfied. The bus driver works for wages but needs food, so the wages are exchanged to obtain his needs. This involves making choices.

Everytime we go shopping we are involved in a basic economic activity, that of making a *choice* because of *scarce* resources. We have only limited money available, but invariably we would like to buy more than we can afford. Consequently, we have not only to make a choice, but also to form a *scale of preference*. In other words, we put what we want into an order of priority.

Scarcity and choice are not problems that are restricted to individuals alone. Businesses and countries face these problems of choice also. Businesses must decide how to profitably use the capital that shareholders have provided. A country has limited resources and the people or their representatives will try to use or allocate them to the best benefit of the community.

The success with which choices are made have a considerable influence on the well-being of individuals, the prosperity of a business and the quality of life of a country's residents. We are fortunate today in that we have many people, organisations and agencies who are available

## 6 Business structure and organisation

to advise us and to help us to make wise decisions on the best way to use the scarce resources available. However, it has taken thousands of years of experience to reach this stage of human development.

### Economic systems

The processes of production, exchange, scarcity and choice looked at so far in this chapter take place within a political framework. In other words, the decision of what to produce or what choices to make with scarce resources available, is influenced by the political situation within which the decision is made. Countries differ in the extent to which they interfere with the economic system. There are three basic approaches adopted by governments: free economy, controlled economy and mixed economy.

#### Free economy

A free economy is based on the private ownership of the factors (means) of production and the means of distributing goods and services. Consumers express their wants through their demand for goods and services, and the private producer seeks to satisfy the demand if the profit motive is sufficient. Therefore, in a free economy the purchaser of goods decides demand and not the state. Sometimes such economies are referred to as market economies, unplanned economies, free enterprise, laissez-faire system, or capitalist system. The USA and Japan are typical examples of a free economy.

#### *Advantages of free economy*

- All members of the community are free to participate in business enterprise for the purpose of making a profit.
- Those engaged in business enterprise have to compete with many others for custom. This has the effect of maintaining efficiency, keeping prices down and improving the standard of goods and services.
- The consumers play a major part in deciding what will be produced because it is the consumer who creates the demand and the producers who try to satisfy this demand.

#### *Disadvantages of free economy*

- Advertising is a major feature of free enterprise and this can be used to create an artificially high demand for some products. In other words, demand may be created by the producer rather than the consumer.
- In a free enterprise society successful businesses may buy out smaller firms in order to obtain control of a larger share of the market. This reduces competition and increases the danger of monopolies arising.
- In response to the profit motive, companies may restrict supplies of some goods or services in order to keep prices and profits artificially high.

#### Controlled economy

In a controlled economy the state controls the factors of production and the means of exchange and distribution. The state estimates what quantity of goods and services the community will need over a given period, and then directs the factors of production to produce these goods

and services. In other words, unlike the free economy, it is the state that decides what the community needs and consequently demand does not originate from the consumers. This type of economy is sometimes called a centralised economy, planned economy, collective economy, or a socialist system. The USSR, China and Cuba are examples of controlled economies.

### *Advantages of controlled economy*

- The state can assess the needs of the whole community and try to provide benefit for all the population. The means of production can then be directed towards this end and wasteful competition can be eliminated.
- It is not possible for a private monopoly to emerge under this system.

### *Disadvantages of controlled economy*

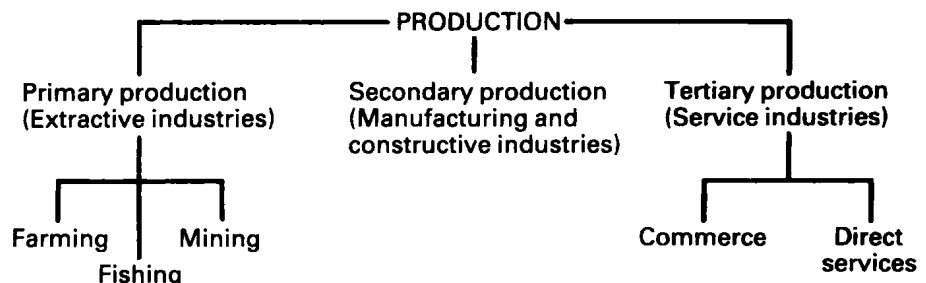
- The state has control over the factors of production and this discourages enterprise and inventiveness.
- A considerable number of non-productive government officials are required to plan and operate the economy. These officials may not necessarily have the skills needed to decide what the community needs, and decisions may be subject to many rules and regulations. This may result in delays in reaching decisions.
- Centralised production may not respond as quickly to changing conditions and trends as private enterprise.
- The absence of competition and profit motive can hinder both creativeness and efficiency.

## Mixed economy

As the term implies, a mixed economy is a combination of elements taken from a free economy and some from a controlled economy. Britain is an example of this type of economic system. Some sections of British industry are owned and operated by the state but large portions of the business world remain in private hands. The contents of this book are largely set in the context of a mixed economy.

## Types of production

Earlier in this chapter we examined direct and indirect production. With direct production, which is a characteristic of countries that are economically backward, individuals or small groups satisfy their wants entirely by their own efforts and unaided by others. Indirect production, which is a feature of all developed societies, involves specialisation,



## 8 Business structure and organisation

working for wages and using the money earned to buy the goods and services produced by other people. Indirect production can be divided into three categories, primary production, secondary production and tertiary production.

### Primary production

Primary production is concerned with the extraction of basic materials provided by nature, which are either above or below the earth's surface. The extractive industries are farming, fishing and mining. Without these much subsequent production would not take place.

*Farming* involves production of foods in the form of fowls, animals and plants and also other produce of the land such as trees and flowers.

*Fishing* has always played a major part in the provision of food for Britain which is not surprising as we are a country surrounded by the sea. Deep-sea fishing is carried out in the open sea and is subject to international rules which try to ensure that each country has its own fair share of the catch. Protected fisheries are a growth industry that exists to farm fish in inland lakes and reservoirs, producing high yields from a small area.

*Mining* extracts raw materials such as coal, ore, oil, gas, etc. from below the earth's surface.

### Secondary production

Secondary production consists of the manufacturing and construction industries. They take the raw materials produced by the extractive industries and change their form into some end product.

*Manufacturers* may be involved in the production of a complete item, or they may make parts which will be assembled into a finished article.

*Construction* industries take raw materials and partly finished products and change them into buildings, roads and bridges, etc.

### Tertiary production

When goods leave the producers they do not usually pass immediately to the consumer. They have to be stored, transported, insured, advertised and sold by traders. These and the many other commercial activities that make up tertiary production further the change of ownership of goods from the producer to the consumers. Tertiary production is sometimes called the service industry, but more often it is referred to as *commerce* and *direct services*.

#### *Commerce*

Commerce can be divided into two clear areas, *trade* and *services to trade*.

- *Trade* is the process of changing ownership. Traders are the businesses directly involved in the buying and selling of goods and services. Trade can either take place within a country (home trade) or between countries (foreign trade). Home trade involves the activities of wholesalers and retailers. Foreign trade involves importers (who buy goods from other countries) and exporters (who sell goods to other countries).
- *Services to trade* are the commercial activities that assist trade in its job of selling goods and services.

The activities that provide these services are:



- 1 Banking – providing short-term finance and providing facilities for easy payment transfer.
- 2 Finance – various institutions (e.g. Stock Exchange) providing long-term finance for industry, commerce and consumer credit.
- 3 Insurance – spreads the risks faced by industrial and commercial businesses.
- 4 Transport – engaged in the movement of commodities from one place to another.
- 5 Communications:
  - (a) Postal – transfer of written communications through mail services.
  - (b) Telecommunications – immediate distance transfer of written, verbal or data communications by electronic devices.
  - (c) Advertising – provides potential customers with information about goods and services available.

All of the elements of both trade and services to trade are the subject of individual chapters in different parts of this book.

### Direct services

In addition to commercial services there are groups of people who provide direct services, which are not related to trade but which people use because they provide services which are essential to the well-being of the community. Direct service occupations include the services of doctors, nurses, teachers, actors and actresses, policemen, hairdressers, authors and many others who offer a personal service.

## Interdependence of industry

Let us now summarise what we have learnt from this chapter.

- *Direct production* is a characteristic of underdeveloped and primitive economies.
- *Indirect production* is a feature of all advanced economies, and this form of production is most common today.
- *Specialisation* is an essential part of indirect production and it involves people doing what they do best.
- *Commercial activities* are positioned between the producer and the consumer and these provide the means of buying and selling goods and services. They play a vital part in allowing people to specialise, earn wages and then buy their wants. They also play a major role in co-ordinating and promoting the activities of producers. We will now examine some of the ways in which this is done.

Traders support producers by carrying out the distribution of goods and bridging the time gap between production and consumption. For example, retailers and wholesalers order goods from producers and hold them until they are required. Exporters are involved in the distribution of home produced goods overseas. This not only provides work for producers, but also raises foreign capital which is needed to pay for the imports of raw materials that the producer needs. Importers buy from other countries the raw materials and finished goods that we cannot economically produce at home, thus allowing home producers to specialise in manufacturing products for which they are best suited.