STEPHEN CHAPMAN | ROSALINDA GALLINA | NATALIE DEVENISH

JACARANDA

BUSINESS STUDIES IN ACTION

PRELIMINARY COURSE | 5TH EDITION

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HOW TO USE THIS BOOK

The following examples highlight the structure and main features of *Business Studies in Action Preliminary Course 5th Edition*. An electronic version of the textbook and a complementary set of targeted digital resources — the eBookPLUS — are available online at the JacarandaPLUS website (www.jacplus.com.au).

Each of the three topics has an opening double page that presents the focus area of the topic and lists the syllabus outcomes. A concept map allows students to visualise the key concepts in the topic. An engaging case study with photographs shows business in action.



TOPIC 2

BUSINESS MANAGEMENT

FOCUS AREA

The focus of this topic is the nature and responsibilities of management in the business environment.

OUTCOMES

Students should be able to:

- explain the internal and external influences on businesses
- assess the processes and interdependence of key business functions
- examine the application of management theories and strategies
- analyse the responsibilities of business to internal and external stakeholders
- plan and conduct investigations into contemporary business issues
- evaluate information for actual and hypothetical business situations
- communicate business information and issues in appropriate formats
- apply mathematical concepts appropriately in business situations.

Case study: Andrew Thorburn — a successful business manager

Andrew Thorburn (pictured), the CEO of the National Australia Bank, was ranked as one of Australia's Top 10 CEOs of 2015. After 30 years' experience in banking, as well as experience in senior positions at a number of Australian banks, Thorburn was appointed Group CEO of NAB in 2014, where he has implemented significant change that has turned the company around.

When reflecting on the age-old debate about whether leaders are made or born, Thorburn believes that anyone can be a leader: 'what it takes is character development, ambition, courage and a driving desire to challenge the status quo.' Thorburn has admitted that he once lacked some of these qualities, but through observing mentors and other leaders he was able to develop and learn these skills.

Thorburn spends a lot of his time mingling and talking to customers and frontline staff when he should be talking strategy in the boardroom. He encourages them to say what they think because he recognises that he doesn't always have all the answers. Thorburn believes one of the most effective ways of problem-solving is to listen to different perspectives. One of his favourite parts of the job is to visit different cities, including regional areas, and talk to staff in order to obtain a view from the ground. He encourages two-way communication as he feels he can learn so much from his employees about what needs to be done to support them.

Thorburn believes leadership is all about people; the ability to engage with, and lead, people. He always wears a name badge (the same type worn by staff in the bank's branches) so that when he meets people he can introduce himself and encourage them to talk to him. While he is often described as ambitious and someone who can make tough calls, staff have found Thorburn to be caring and encouraging. He has been described as a people person due to his ability to relate to staff and customers.

One of Thorburn's most effective leadership skills is his ability to adapt to and implement change. From the moment he began at NAB, he has been constantly challenging the status quo. Thorburn recognises that he's operating in an environment that is experiencing an unprecedented level of change; however, rather than viewing change as a threat, he embraces it and views it as an opportunity for the business to shape the industry.

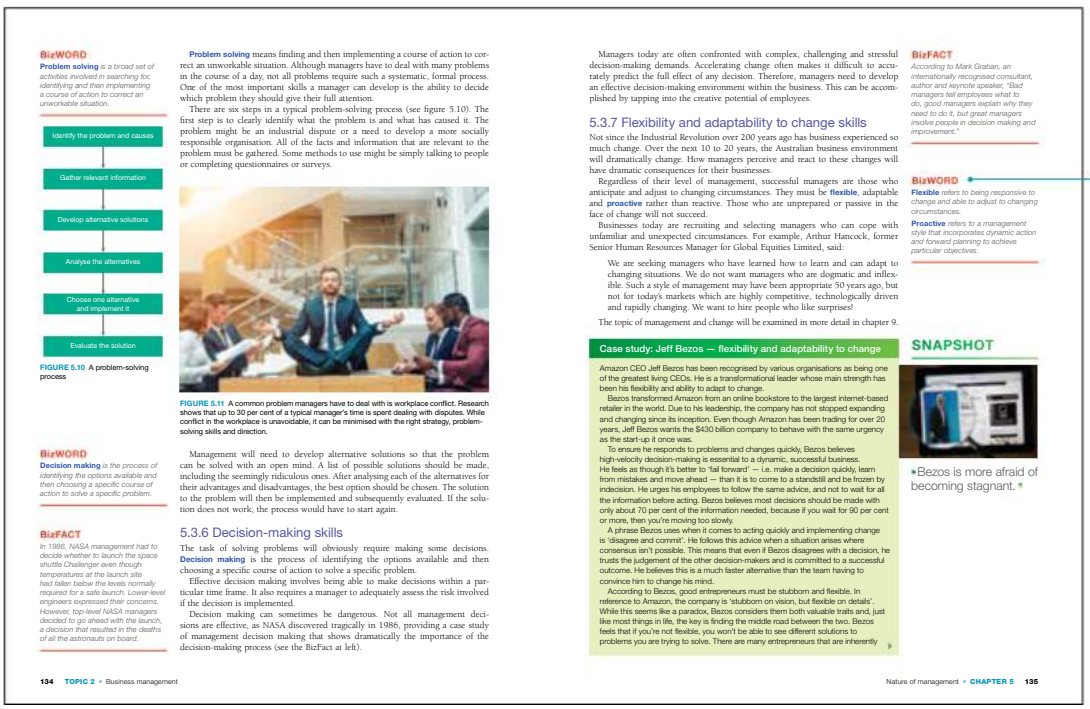
Thorburn possesses a drive for change. He wants to usher it in from the ground up. He also has high expectations of his employees' abilities to implement change. Thorburn continually talks to his staff and focuses on their needs, which demonstrates he is concerned about their welfare. This has reduced the resistance to change in the organisation and led to a culture where employees embrace change.

In order to create a culture of change, Thorburn believes that management needs to have a clear intent about what they want to achieve. They need to create a big strategic goal that inspires people. For NAB, the overarching goal is to make the customer experience better. Once the strategic aim has been communicated, Thorburn relies on change agents to help drive the change. He has created a group of leaders who are passionate but who are also given the freedom to fail, to inspire others in the organisation to adopt change. In order to sustain the change, Thorburn is a firm believer in offering encouragement and recognition to staff.

Thorburn believes leaders should be role models and lead by example. This is why he always acts the way that he expects others to behave. He has come to realise that the biggest driver of culture is the behaviour of leaders and that it's not what they say, it's their actions and what they do that will inspire others. And inspire he has!

… he embraces change and views it as an opportunity …

All Preliminary syllabus outcomes are covered in depth to provide a sound basis of knowledge to prepare students for the HSC course. BizWords, highlighted in the margin for easy reference, provide definitions of the bolded words in the text to build a comprehensive glossary. BizFacts present interesting and topical snippets of supplementary information to engage and extend students. 'Snapshot' case studies present profiles of a wide range of businesses and individuals, and the contemporary business issues they face.



BizWORD

Problem solving *is a broad set of activities involved in searching for, identifying and then implementing a course of action to correct an unworkable situation.*

FIGURE 5.10 A problem-solving process

Problem solving means finding and then implementing a course of action to correct an unworkable situation. Although managers have to deal with many problems in the course of a day, not all problems require such a systematic, formal process. One of the most important skills a manager can develop is the ability to decide which problem they should give their full attention.

There are six steps in a typical problem-solving process (see figure 5.10). The first step is to clearly identify what the problem is and what has caused it. The problem might be an industrial dispute or a need to develop a more socially responsible organisation. All of the facts and information that are relevant to the problem must be gathered. Some methods to use might be simply talking to people or completing questionnaires or surveys.

FIGURE 5.11 A common problem managers have to deal with is workplace conflict. Research shows that up to 30 per cent of a typical manager's time is spent dealing with disputes. While conflict in the workplace is unavoidable, it can be minimised with the right strategy, problem-solving skills and direction.

BizWORD

Decision making *is the process of identifying the options available and then choosing a specific course of action to solve a specific problem.*

BizFACT

In 1986, NASA management had to decide whether to launch the space shuttle Challenger even though temperatures at the launch site had fallen below the levels normally required for a safe launch. Lower-level engineers expressed their concerns. However, top-level NASA managers decided to go ahead with the launch, a decision that resulted in the deaths of all the astronauts on board.

Management will need to develop alternative solutions so that the problem can be solved with an open mind. A list of possible solutions should be made, including the seemingly ridiculous ones. After analysing each of the alternatives for their advantages and disadvantages, the best option should be chosen. The solution to the problem will then be implemented and subsequently evaluated. If the solution does not work, the process would have to start again.

5.3.6 Decision-making skills

The task of solving problems will obviously require making some decisions. **Decision making** is the process of identifying the options available and then choosing a specific course of action to solve a specific problem.

Effective decision making involves being able to make decisions within a particular time frame. It also requires a manager to adequately assess the risk involved if the decision is implemented.

Decision making can sometimes be dangerous. Not all management decisions are effective, as NASA discovered tragically in 1986, providing a case study of management decision making that shows dramatically the importance of the decision-making process (see the BizFact at left).

Managers today are often confronted with complex, challenging and stressful decision-making demands. Accelerating change often makes it difficult to accurately predict the full effect of any decision. Therefore, managers need to develop an effective decision-making environment within the business. This can be accomplished by tapping into the creative potential of employees.

5.3.7 Flexibility and adaptability to change skills

Not since the Industrial Revolution over 200 years ago has business experienced so much change. Over the next 10 to 20 years, the Australian business environment will dramatically change. How managers perceive and react to these changes will have dramatic consequences for their businesses.

Regardless of their level of management, successful managers are those who anticipate and adjust to changing circumstances. They must be **flexible**, adaptable and **proactive** rather than reactive. Those who are unprepared or passive in the face of change will not succeed.

Businesses today are recruiting and selecting managers who can cope with unfamiliar and unexpected circumstances. For example, Arthur Hancock, former Senior Human Resources Manager for Global Equities Limited, said:

> We are seeking managers who have learned how to learn and can adapt to changing situations. We do not want managers who are dogmatic and inflexible. Such a style of management may have been appropriate 50 years ago, but not for today's markets which are highly competitive, technologically driven and rapidly changing. We want to hire people who like surprises!

The topic of management and change will be examined in more detail in chapter 9.

Case study: Jeff Bezos — flexibility and adaptability to change

Amazon CEO Jeff Bezos has been recognised by various organisations as being one of the greatest living CEOs. He is a transformational leader whose main strength has been his flexibility and ability to adapt to change.

Bezos transformed Amazon from an online bookstore to the largest internet-based retailer in the world. Due to his leadership, the company has not stopped expanding and changing since its inception. Even though Amazon has been trading for over 20 years, Jeff Bezos wants the $430 billion company to behave with the same urgency as the start-up it once was.

To ensure he responds to problems and changes quickly, Bezos believes high-velocity decision-making is essential to a dynamic, successful business. He feels as though it's better to 'fail forward' — i.e. make a decision quickly, learn from mistakes and move ahead — than it is to come to a standstill and be frozen by indecision. He urges his employees to follow the same advice, and not to wait for all the information before acting. Bezos believes most decisions should be made with only about 70 per cent of the information needed, because if you wait for 90 per cent or more, then you're moving too slowly.

A phrase Bezos uses when it comes to acting quickly and implementing change is 'disagree and commit'. He follows this advice when a situation arises where consensus isn't possible. This means that even if Bezos disagrees with a decision, he trusts the judgement of the other decision-makers and is committed to a successful outcome. He believes this is a much faster alternative than the team having to convince him to change his mind.

According to Bezos, good entrepreneurs must be stubborn and flexible. In reference to Amazon, the company is 'stubborn on vision, but flexible on details'. While this seems like a paradox, Bezos considers them both valuable traits and, just like most things in life, the key is finding the middle road between the two. Bezos feels that if you're not flexible, you won't be able to see different solutions to problems you are trying to solve. There are many entrepreneurs that are inherently

BizFACT

According to Mark Graban, an internationally recognised consultant, author and keynote speaker, "Bad managers tell employees what to do, good managers explain why they need to do it, but great managers involve people in decision making and improvement."

BizWORD

Flexible *refers to being responsive to change and able to adjust to changing circumstances.*

Proactive *refers to a management style that incorporates dynamic action and forward planning to achieve particular objectives.*

SNAPSHOT

Bezos is more afraid of becoming stagnant.

HSC 'key process verbs' are used consistently in all questions to prepare students for HSC study. Questions are graded according to low-, middle- or high-order thinking skills. The 'key process verbs' are listed and defined in an appendix for ready reference.

18 **Identify** which external influence is affecting the small business in each of the following cases:
(a) Julie runs a small busy restaurant. She recently introduced technology that allows waiting staff to electronically send orders to the kitchen. This means better service for the customer because the order is taken more efficiently and more time can be devoted to other tasks such as the prompt delivery of food and drinks.
(b) John is the manager of a function centre that hosts large weddings and conferences. He makes sure to include an acknowledgement of the traditional owners of the land, the Wurundjeri people and their elders, in his opening remarks.
(c) Mia has to design and print new labels for the foods sold in her deli. This is because changes to the food labelling laws require that all foods list the ingredients by particular portion size. This allows customers to more easily compare different food items. She thinks that this may affect which foods customers choose.
(d) Michael, the owner of a local bottle shop, is no longer allowed to sell imported premixed alcoholic drinks because of a government ban on food and beverage imports from particular countries.

EXERCISE 3.1 EXTENSION

1 **Explain** the impact each of the external influences has on a business and how the business's management responds. The first factor has been completed for you.

Factor influencing the internal environment	Brief explanation	Management response
Political influences	Elected governments at all levels in Australia regulate markets and have the power to make or change laws.	Must comply with the laws and regulations introduced by governments

2 Using an example, **determine** how the development of global consumers encouraged the process of globalisation.
3 (a) **Demonstrate** how technology has affected the way consumers can purchase goods and services.
(b) **Predict** what will happen if an Australian business does not provide the opportunity for consumers to purchase online.
4 In small groups, **examine** and report on a social issue confronting businesses in your local area. You may wish to either prepare a PowerPoint presentation or use a word-processing package for your report.
(a) **Outline** the issue.
(b) **State** how the local businesses have reacted to the situation.
(c) **Determine** what indicators you would use to decide the success or failure of a business's response to the situation.

3.4 Internal influences on business

Internal influences relate to the specific factors within the business that will affect its operations. These factors can be identified and adjusted via feedback and evaluation processes due mostly to the business's interaction with internal factors.

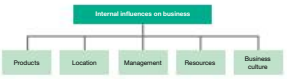


FIGURE 3.19 Internal influences on business

3.4.1 Product influences

Product influences affect a range of internal structures and operations within the business. The main product influences on a business are as follows.
1. The type of goods and services produced will affect the internal operations of a business. If the goods are physically large or require many raw material inputs, there will need to be structures in place to organise and monitor the processes involved in production. In contrast, a service may be delivered by a home-based business or a franchise business, such as Jim's Mowing, and will influence the internal structures or processes differently.
   The range of goods and services refers to the number produced by the business. The larger the number, the more internal impact it will have on the business as it will need to expand operations and internal structures to accommodate the changes. Companies such as Coca-Cola have continually expanded their product range over the last 20 years, and this has meant that internal changes to operations and management have been necessary to allow this expansion to occur.
2. Product influence will be reflected in the type of business (service, manufacturer or retailer). Internally, a service provider will be structured differently to a manufacturer or retailer, and the influences will vary. Some goods or services require extensive preparation, while others are merely deliverers. Consider the difference between the product influences of a clothing manufacturer and that of a clothing retailer.
3. The size of the business, as previously mentioned, will be based on the range and type of goods and services produced, the level of technology utilised, and the volume of goods and services produced. The larger the business the more goods and services being produced, which will in turn influence the internal structures and operations of the business. A cafe will operate at a different scale to a club bistro and therefore the influence on business functions will be relative.



FIGURE 3.20 Manufacturing businesses must have a physical location for their production and stock holding operations, whereas service firms do not require a physical production site. The people creating and delivering the service can be located anywhere.

their own input into the firm. This style of leadership is most effective when a business is operating in an environment undergoing rapid change. Individual employees accept responsibility and can implement changes themselves, making the business more responsive to change. Through activities such as brainstorming, a diverse range of opinions and ideas can be generated resulting in improved decision making.

The main advantages of the participative or democratic management style include the following:
- Communication is a two-way process.
- Employer/employee relations are positive and there is reduced likelihood of industrial disputes because employees are more likely to accept management decisions.
- Motivation and job satisfaction are optimal as employees feel they have played an active role in allocating tasks and implementing actions to meet objectives.
- Employees have a greater opportunity to acquire more skills.
- Power sharing encourages the development of work teams, and employees display high levels of commitment.
- There is a high level of trust, often resulting in improved employee performance.

The main disadvantages include the following:
- Reaching decisions and introducing tasks can be time consuming with differing views having to be considered. The quality of decisions may also suffer because compromises are made rather than decisive, clear directions given.
- The role of management, and the control of the manager, may be weakened and undermined, with employees given too much power in some cases.
- Internal conflict can arise with so many views and opinions being shared. More involvement may actually bring about disagreement.
- The importance of the organisational structure may be minimised, leading to an informal system that could result in a complete collapse in management.
- Not all employees want to contribute.

There is no simple answer to the question: 'What leadership style does a good manager possess?' Management is an art, not a science. This means that no simple management formula can be applied to deal effectively with all workplace situations.

SNAPSHOT

Case study: Jack Stahl — democratic leadership style



'… working with others is the best way to work.'

Jack Stahl is a former Chief Operating Officer and President of Coca-Cola, as well as a former CEO of Revlon. Through his democratic leadership style and knowledge, he brought these two companies to higher profitability. During his tenure at Coca-Cola, the net worth of the company grew from $3 billion to over $130 billion.

Jack Stahl believes that working with others is the best way to work. He knows how to delegate work to employees and can take a step back when necessary. Stahl achieves this through investing in training and development of staff. Training his employees to concentrate on the details reduces the need for micromanagement and allows him to pull back and worry about things from a more strategic perspective.

As a democratic leader, he encourages his employees to be involved in decision making. He keeps staff informed about matters relating to their work and shares problem-solving and decision-making responsibilities. While Stahl ultimately has the final say, he consults with staff before making a final decision. The teams he has led felt trusted and responded favourably to his style. Employees under his management demonstrated higher morale, team spirit and cooperation.

Stahl is a charismatic and visionary leader who is able to effectively communicate his vision to all relevant stakeholders, as well as inspire his employees to turn that vision into a reality. Stahl's inspirational qualities have enabled him to foster both individual and team effectiveness. He possesses an ability to produce results through the use of intrinsic rewards such as recognition, as well as rewarding successful performance. Through his leadership skills he has been able to successfully align employees with each company's purpose.

SNAPSHOT QUESTIONS
1. **Demonstrate** how Jack Stahl adopts a democratic leadership style.
2. **Explain** the impact his leadership style would have on his employees.

SUMMARY

- A manager who adopts a behavioural approach will tend to use a participative or democratic leadership style.
- Participative or democratic leaders share their decision-making authority with their subordinates.
- This style of leadership is most effective when a business is operating in an environment undergoing rapid change.

7.4 Contingency approach to management

While the classical and behavioural management approaches continue to provide important lessons for managers, other ideas have also emerged during the last couple of decades (see figure 7.22). These contemporary management approaches represent major innovations in ways of thinking about management and appropriate management practices. One of the most important contemporary viewpoints is the **contingency approach** to management. It stresses the need for flexibility and the adaptation of management practices and ideas to suit changing circumstances.

BizWORD
Contingency approach *stresses the need for flexibility and adaptation of management practices and ideas to suit changing circumstances.*

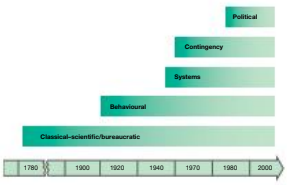


FIGURE 7.22 Timeline of management thought

7.4.1 Adapting to changing circumstances

Contingency theorists point out to managers that no two situations are absolutely identical. Each situation, therefore, requires its own unique solution. For example, you may have used a particular strategy to complete a task for assessment. Although this strategy may have been quite successful for that particular task, another assessable task may well require a completely different approach.

BizFACT
Managers are increasingly finding that creating a sustainable competitive advantage is not just about being the best at doing a particular thing. Instead, businesses must be really good at learning to do new things. Those businesses that thrive are the ones that are quick to read and act on signals of change.

Straightforward explanations of complex concepts are reinforced by numerous up-to-date statistics and easy-to-read graphic organisers. Summaries throughout each chapter encourage a progressive revision of concepts. Weblinks are provided to key business bodies and further resources.

TOPIC 2 SUGGESTED ASSESSMENT TASKS

Business management

MULTIPLE CHOICE QUESTIONS

1. Which of the following would be classified as a social goal?
(a) To increase market share by 10 per cent
(b) To sponsor the local school football team
(c) To provide shareholders with increased returns
(d) To improve the training opportunities for employees

2. Refer to the following information for Question 2.

	$
Sales	150 000
Cost of Goods Sold	65 000
Expenses	42 000

What would the Net Profit be for this business?
(a) $43 000
(b) $127 000
(c) $173 000
(d) $257 000

3. Which of the following are both examples of current liabilities?
(a) Debtors and creditors
(b) Overdraft and debtors
(c) Creditors and overdraft
(d) Creditors and mortgage

4. What is a collective agreement made at a workplace level about terms and conditions of employment referred to as?
(a) Award
(b) Enterprise agreement
(c) Individual common law contract
(d) National Employment Standards

5. Refer to the following Balance Sheet to answer Question 5.

ASSETS	$	LIABILITIES	$
Current Assets		**Current Liabilities**	
Cash in bank	5000	Overdraft	3000
Stock	(?)	Creditors	4000
Non-current Assets		**Non-current Liabilities**	
Building	350 000	Bank loan	310 000
Equipment	17 000	**OWNER'S EQUITY**	
Furniture	13 000	Capital	84 000

What would be the value of the stock?
(a) 2000
(b) 4000
(c) 16 000
(d) 68 000

6. Fletcher & Sons Construction has developed a plan to guide the business over the next five years. What type of planning is this an example of?
(a) Operational
(b) Tactical
(c) Technical
(d) Strategic

7. What does the contingency approach to management emphasise?
(a) Management as planning, organising and controlling
(b) Management as leading, motivating and communicating
(c) The need for managers to be reactive and respond to change after it occurs
(d) The need for flexibility and adaptation of management practices to suit changing circumstances

8. A new furniture store has decided to stock their products through a few selective retailers. Which marketing strategy is this an example of?
(a) Place
(b) Price
(c) Product
(d) Promotion

9. Calculate the value of owner's equity given the following information: Liabilities = $75 000 and Assets = $145 000.
(a) $70 000
(b) $75 000
(c) $220 000
(d) $240 000

10. Shimmering Jewellery relies heavily on their sales assistants to promote their goods by outlining the benefits and features of their products to consumers. This has been successful in persuading customers to purchase their products. Which promotion technique is this an example of?
(a) Publicity
(b) Advertising
(c) Personal selling
(d) Sales promotion

11. Which of the following are both examples of involuntary separation?
(a) Resignation and dismissal
(b) Retirement and resignation
(c) Dismissal and retrenchment
(d) Retrenchment and retirement

12. A manager of a real estate agency always consults with employees when setting targets and making decisions. What type of leadership style would this be an example of?
(a) Autocratic
(b) Democratic
(c) Diplomatic
(d) Hierarchical

13. Beautiful Skin Pty Ltd has decided to produce a razor for women. It has calculated the total production costs for each razor and added a 15 per cent margin to set the final price. What pricing method is this an example of?
(a) Cost-based pricing
(b) Break-even pricing
(c) Market-based pricing
(d) Competition-based pricing

14. Michael is able to manage change in his business by always scanning the environment and attempting to understand the factors that will have an impact on the business. Which of the following best describes the method of managing change effectively used by Michael?
(a) Setting achievable goals
(b) Reducing resistance to change
(c) Identifying the need for change
(d) Utilising management consultants

Sample HSC-style assessment tasks are provided for each topic, comprising multiple choice, short response and extended response questions with appropriate marks allocated.

About eBookPLUS

jacaranda *plus*

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TOPICS

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TOPIC 1

NATURE OF BUSINESS

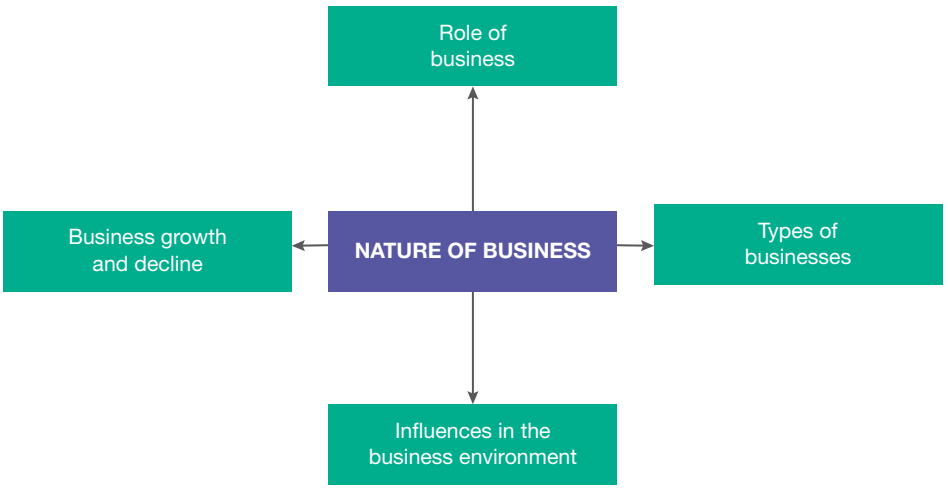
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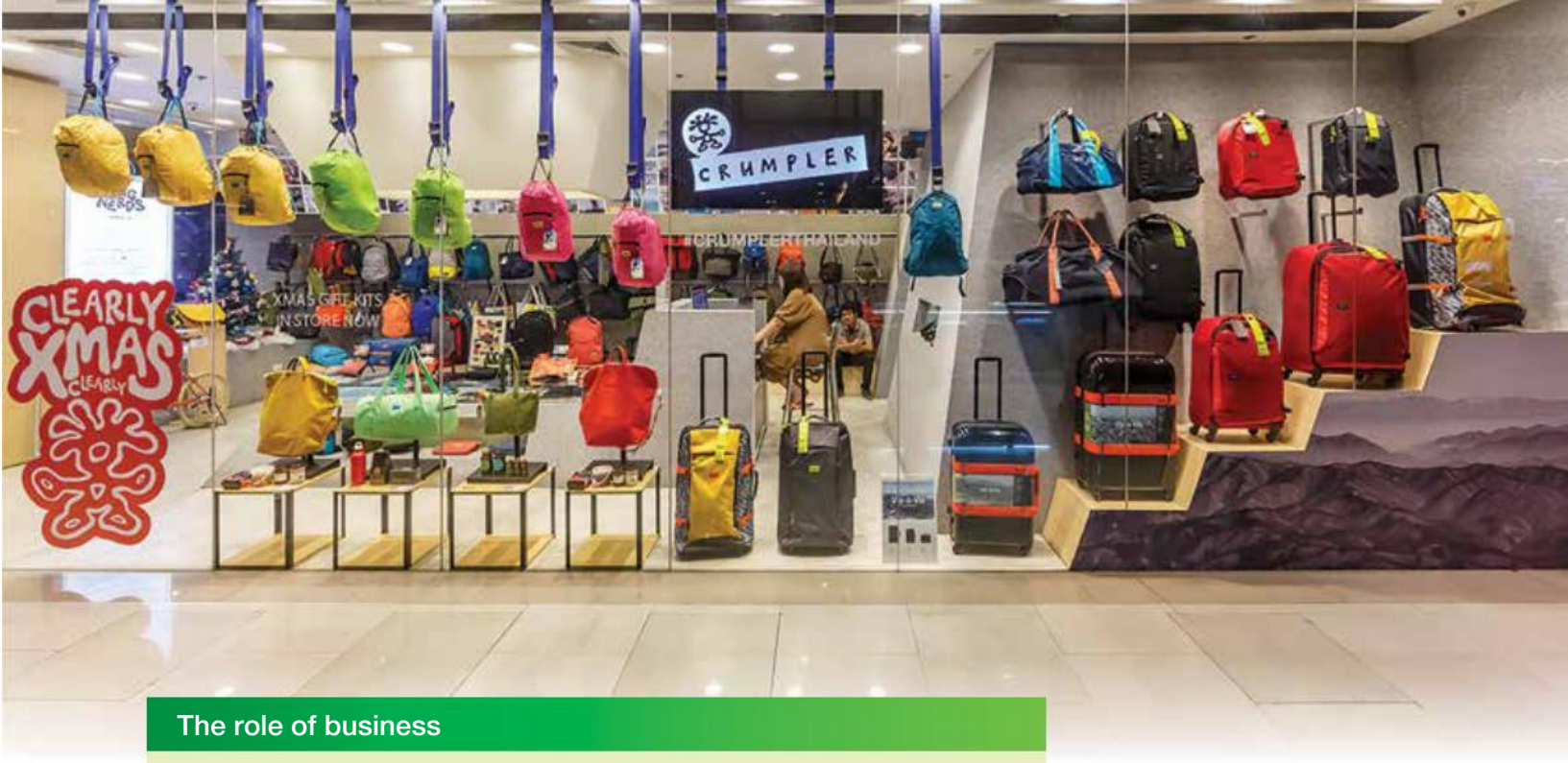
The focus of this topic is the role and nature of business in a changing business environment.

OUTCOMES

Students should be able to:

- discuss the nature of business, its role in society and the types of business structures
- explain the internal and external influences on businesses
- analyse the responsibilities of business to internal and external stakeholders
- plan and conduct investigations into contemporary business issues
- evaluate information for actual and hypothetical business situations.





The role of business

Thousands of Australian businesspeople are involved every day in making decisions about how best to plan and manage their businesses. Businesses play a crucial role in our lives and actively contribute to progress in society. The examples from a variety of organisations given below show the various roles that businesses play.

- *Employment and income* — QANTAS has more than 29 000 employees. In 2017, QANTAS was named as Australia's most attractive company for job seekers by employment firm Randstad. These awards cover the nation's 150 largest employers by workforce size and are based on a survey of approximately 8000 job seekers. QANTAS was picked for its innovation with technology, financial health and strong reputation.
- *Entrepreneurship and risk* — Amanda Young and Matt Braithwaite drew on their previous experience working for companies in the beverage industry to start Springleaf Iced Tea. With three small children, they wanted a better work–life balance. The learning curve has been steep, but they have succeeded in creating a profitable business, as well as having more time for their children.
- *Quality of life* — Nick Savaidis, the founder of Etiko, believes that businesses should make a positive contribution to society. Consequently, from sales of its products, Etiko is able to help fund community development, micro-credit and health care programs around the world.
- *Innovation* — Stuart Crumpler drew inspiration after he couldn't find a bag that let him cycle home with a slab of beer on his back. With the need to solve this basic 'everyday carrying problem', the innovative mind of Stuart Crumpler created the first ever Crumpler bag. He now sells one million bags every year, both online and through around 60 stores in Australia. 'Make things better' is an all-encompassing Crumpler ethos that challenges the company to do their best every day to make their products better and to find solutions to everyday carrying problems through functional product design.
- *Wealth* — Wilson Asset Management (WAM Capital), Australia's largest listed investment company, has generated wealth for its many shareholders. Their share price has grown by 53 per cent over the last five years. They have also grown their dividend every year since the GFC and currently have a dividend yield of 8.68 per cent. The company also helps their own investors (clients) generate wealth with exposure to an actively managed diversified portfolio of companies. WAM Capital's key objectives are to deliver investors a stream of dividends and provide capital growth.

These are just a few examples of the many roles played by businesses in our society. The world of business is most definitely an exciting and interesting one.

> 'The world of business is most definitely an exciting and interesting one.'

CHAPTER 1

Role of business

OVERVIEW

1.1 Introduction
1.2 The nature of a business
1.3 Other functions of business

1.1 Introduction

Think of all the different businesses that operate in your local neighbourhood. Now imagine what the world would be like if they did not exist. Ultimately we would have to become self-sufficient: providing for our own needs and wants. Fortunately, in our society, businesses of all sizes play a crucial role in providing us with a vast array of goods and services. Businesses are at the very core of our economy and our future wealth depends upon them.

Most people associate the word 'business' with large, multinational corporations, such as BHP Billiton, McDonalds, Apple and Westfield, operating in many countries, employing thousands of people and earning millions of dollars in profit. Although these types of businesses are well known, they are few in number. Small to medium enterprises (SMEs) make up about 98 per cent of all businesses in Australia. Take a look around your local area and you will see plenty of examples of businesses that are considered small or medium based on the number of people they employ.



FIGURE 1.1 As consumers, we rely on a large number of businesses to satisfy our needs and wants.

The one common feature shared by both the largest and the smallest business is that they produce a product — goods or service — which is sold in a market where buyers and sellers meet. There are approximately 2.1 million actively trading business entities in Australia, which respond to the needs and wants of around 24 million Australian customers and millions of overseas customers.

1.1.1 Why learn about business?

Business Studies is a very important subject. It is concerned with activities that affect us on a day-to-day basis. You only have to listen to the news or read the newspaper to find stories about business activity. Some of these stories will make you feel optimistic — for example, the developments of new products that have helped improve our standard of living. At other times, business activity may make us feel dejected and cynical — for example, when businesses have misled the public about safety standards or when companies have exploited weaker members of society. Therefore, when studying business, it is essential that you carefully examine business issues in order to make a balanced judgement.

Learning about business is both interesting and useful. It is also challenging and requires imagination.

In learning about business you will need to be creative and have a questioning mind. Business decisions are often open ended; there may be more than one way of going about things. Therefore, you will need to ask lots of questions and weigh up alternative ideas and proposals.



FIGURE 1.2 You're never too young to start a business. More and more young people are seeing the value of entrepreneurship as a rewarding career path. Take, for example, Ali Kitinas, Australia's youngest CEO, who started her first business when she was 11. Now the 16-year-old runs her own company producing an ethical body scrub made from recycled coffee grounds, with a portion of proceeds going to impoverished children.
Source: Ali Kitinas

Business Studies is not a totally new subject to you. In one sense you have been 'studying' business ever since you made your first purchase many years ago — perhaps an ice-cream or lollies. That simple transaction launched you on life's journey as a customer — and as an integral part of the business world. As a high school student, perhaps you have even operated your own 'business', mowing neighbours' lawns, washing windows or setting up a stall at a local community market. You may be employed on a part-time basis and work in a local store or fast-food outlet — both examples of business enterprises.

1.1.2 Importance of business to you

Undertaking this Business Studies course will give you a better understanding of how businesses are established, organised and operated. As well, it will give you an insight into the different roles you will play throughout your life — as consumer, employee, business owner and/or investor. Each of these roles centres around a business as shown in figure 1.3 on the following page.



FIGURE 1.3 Developing an understanding of the world of business will help you in so many ways.

Businesses, through the many products (goods and services) they make and sell, have an enormous impact on our lives every day. They influence how we live, work and play.

SUMMARY

- Businesses play a crucial role in our society, largely determining our standard of living.
- Small to medium enterprises (SMEs) make up about 98 per cent of all businesses in Australia.
- The one common feature shared by both the largest and the smallest business is that they produce a product — goods or service — which is sold in a market where buyers and sellers meet.
- Businesses have an enormous impact on our lives every day.

1.2 The nature of a business

There is one thing people have in common — they all have needs and wants. They need food to eat, clothes to wear and houses to live in. Most of us also want handbags, video games, tablets, smart phones and cars — if only for the pleasure



FIGURE 1.4 Do you have oniomania? That means you are what might be referred to as a shopaholic or compulsive shopper. Market research company TNS found that Australian teenagers are spending an average of $5000 of their parents hard-earned money per year. Young consumers spend an average of $96 a week, with the most money being spent on clothes, transport, mobile phones, electronics and fast food.

they give to us. To satisfy these never-ending wants is the role of business. A **business** can be defined as the organised effort of individuals to produce and sell, for a profit, the **products** (**goods** and **services**) that satisfy individuals' needs and wants.

To satisfy the needs and wants of its customers, the business has to produce the products the customers demand. By producing these products for sale on the market, the business hopes to achieve a number of goals. Making a profit is perhaps the most basic of these.

1.2.1 Producing goods and services

When we go shopping we are choosing from a range of **finished products** — products that are ready for customers to buy and use. Rarely do we stop to think about all the operations that have occurred to transform raw materials into finished products ready for consumption. Business enterprises undertake many activities to provide the products demanded by customers, as shown in figure 1.5. However, by far the most important of all these activities is production. **Production** refers to those activities undertaken by the business that combine the resources to create products that satisfy customers' needs and wants.

BizWORD

*A **business** can be defined as the organised effort of individuals to produce and sell, for a profit, the products that satisfy individuals' needs and wants.*

*A **product** is a good or service that can be bought or sold.*

***Goods** are items that can be seen or touched.*

***Services** are things done for you by others.*

BizWORD

*A **finished product** is one that is ready for customers to buy and use.*

***Production** refers to those activities undertaken by the business that combine the resources to create products that satisfy customers' needs and wants.*

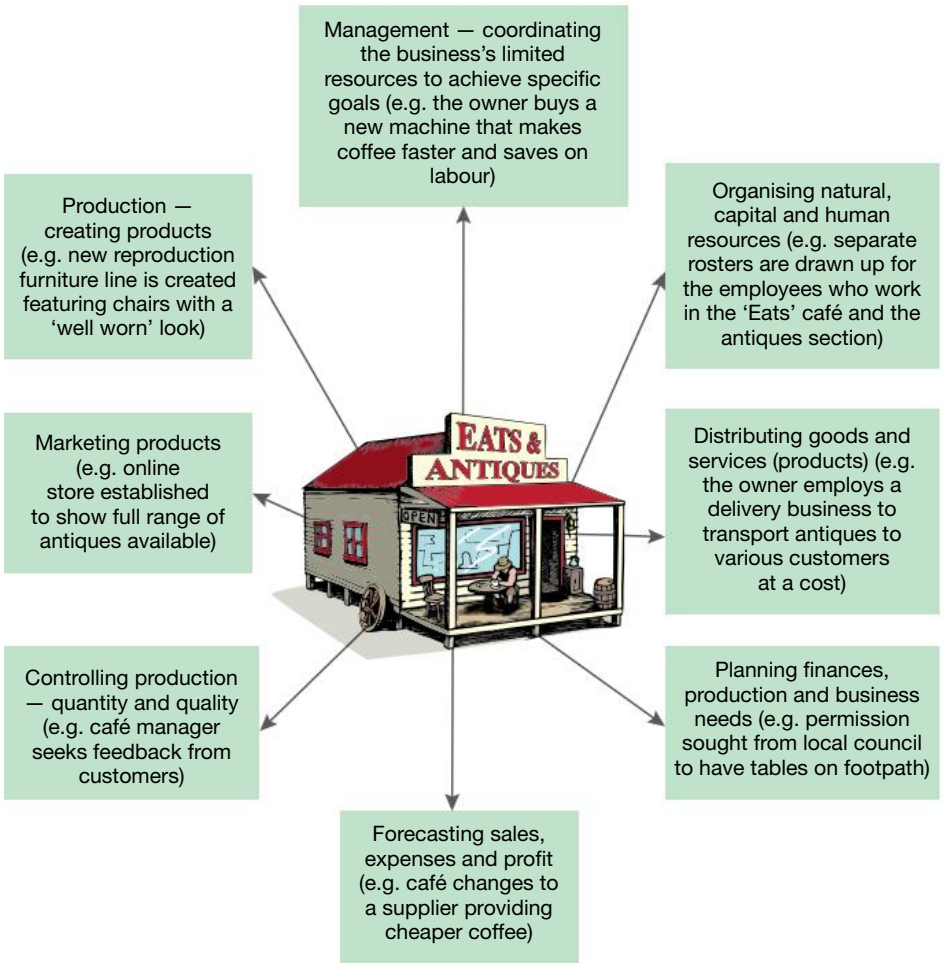


FIGURE 1.5 The main activities undertaken by this business, an antiques dealer with an on-site café, include more than selling furniture and serving coffee.

BizFACT

It is possible to calculate the value of production within an economy. The money value of all the finished products produced in Australia during one year is called the gross domestic product (GDP). This measurement is used as an indicator of Australia's economic growth. In 2016, Australia's annual GDP was $1.67 trillion.

SUMMARY

- The main role of a business is to produce and sell, for a profit, the products that satisfy individuals' needs and wants.
- Business enterprises undertake many activities to provide the products demanded by customers, with production being one of the most important.
- Production refers to those activities undertaken by the business that combine resources to create products that satisfy customers' needs and wants.

EXERCISE 1.1 REVISION

1 **Identify** the one common feature shared by all businesses.

2 **Summarise** how Business Studies can help you better perform the roles of consumer, employee, business owner and investor.

3 **Outline** the role of business.

4 **Define** the term 'business'.

5 **Identify** two goods and two services you recently purchased to satisfy a need or a want. Next to each one write the name of the business from which you bought the product.

6 **Define** the term 'finished products'.

7 **Why** is production regarded as the most important business activity?

8 Gordon Su is the owner of a jewellery store specialising in handmade necklaces and bracelets. Read about his daily business activities (in the first column of the table below) then complete the table to **demonstrate** each business activity Gordon undertakes to operate his business successfully. The first example has been completed for you.

Activity undertaken by business	Example
Production — creating products	Making necklaces and bracelets
Organising natural, capital and human resources	
Marketing products	
Controlling production — quantity and quality	
Forecasting sales, expenses and profit	
Distributing goods	

9 Reflect on what you have learned so far. **State** how this information would influence you if you were intending to start a business.

EXERCISE 1.1 EXTENSION

1 As a class, **discuss** the statement: 'The one thing I've learnt about surviving in business is that it's important to learn from past mistakes — and the more mistakes you make the more you learn.' (Richard Branson, British entrepreneur, founder and CEO of Virgin Group)

2 **Construct** a clippings file of magazine and newspaper articles dealing with various aspects of business and its importance to the Australian economy. Select five articles and paste them onto a sheet of paper. Underneath each article prepare a 12–15 line summary.

3 **Construct** a series of flowcharts to show the interrelationship between producers and consumers.

1.3 Other functions of business

Businesses play an important role in our society. Some of the important functions of business are outlined in figure 1.6.

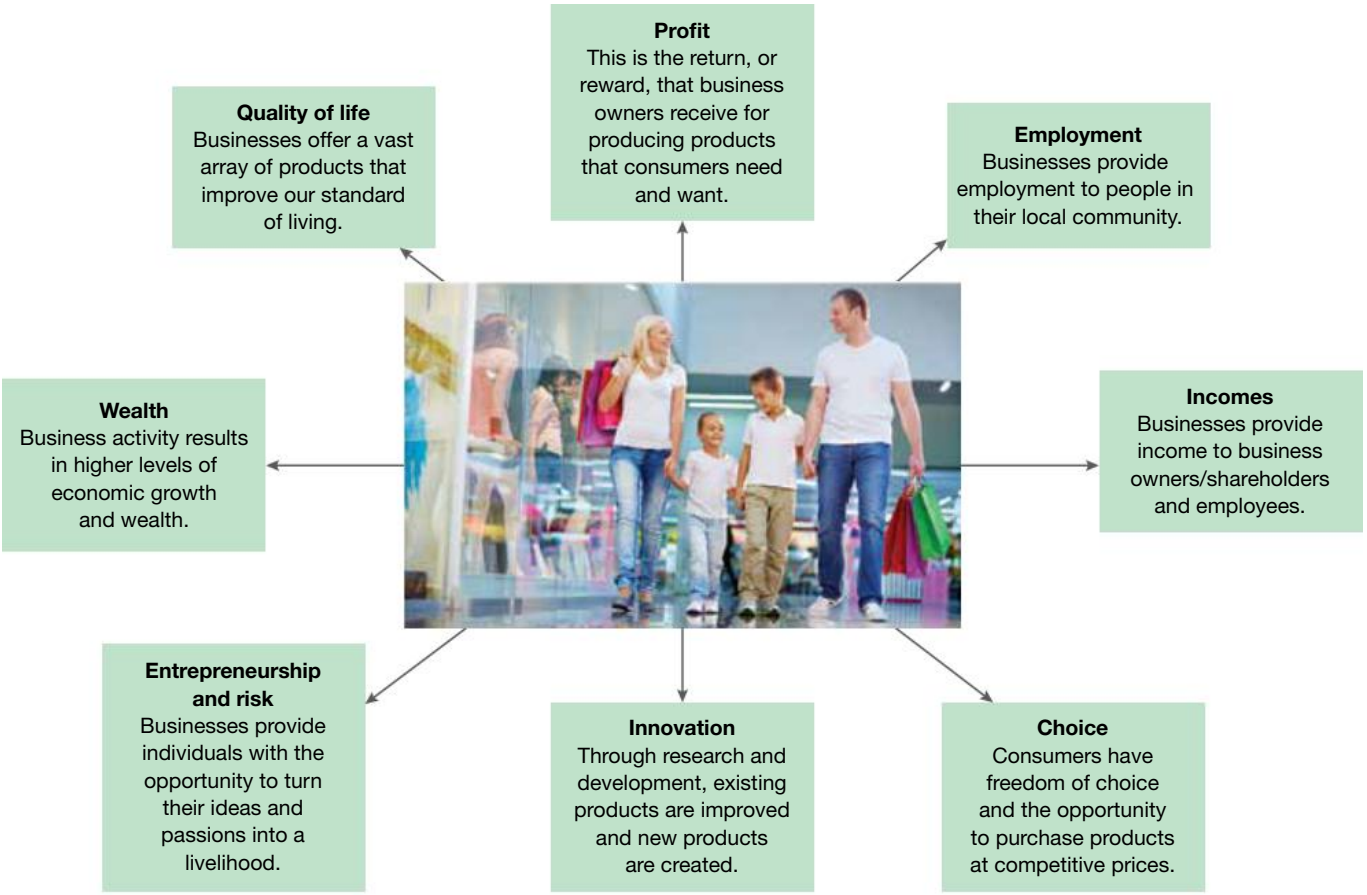


FIGURE 1.6 The economic and social importance of business

1.3.1 Profit

The main activity of a business is to sell products to its customers. A business receives money (sales revenue) from its customers in exchange for products. It must also pay out money to cover the numerous expenses involved in operating the business. If the business's sales **revenue** is greater than its **operating expenses**, it has earned a profit. More specifically, **profit** is what remains after all business expenses have been deducted from the business's sales revenue (see figure 1.7).

BizWORD

Revenue *is the money a business receives as payment for its products.*

Operating expenses *are all the costs of running the business except the cost of goods sold.*

Profit *is what remains after all business expenses have been deducted from sales revenue.*



FIGURE 1.7 A business must earn a profit to survive. Profit is the reward to business owners who have taken the risks involved in starting and operating a business.

BizFACT

A negative profit, which results when a business's expenses are greater than its sales revenue, is called a loss.

BizFACT

Around 61 per cent of businesses in Australia do not employ staff.

The business's profit becomes the property of its owners. For this reason, profit can be regarded as the return, or reward, that business owners receive for producing products that consumers want.

1.3.2 Employment

Employment keeps the economy healthy. To be able to purchase products, consumers need money. Employed Australians will use the money they have earned from working at jobs provided by businesses to buy goods and services to meet their needs and wants, supporting business and opening up further opportunities for job creation. People are employed in many different businesses, as can be seen in table 1.1.

TABLE 1.1 Employment in Australia by industry sector (2017)

Industry sector	Number	%
Health care and social assistance	1 562 600	12.9
Retail trade	1 228 400	10.1
Construction	1 108 300	9.1
Professional, scientific and technical services	1 018 500	8.4
Education and training	971 800	8.0
Manufacturing	906 500	7.5
Accommodation and food services	872 100	7.2
Public administration and safety	812 000	6.7
Transport, postal and warehousing	614 000	5.1
Financial and insurance services	436 100	3.6
Administrative and support services	411 000	3.4
Wholesale trade	391 000	3.2
Agriculture, forestry and fishing	296 700	2.4
Mining	235 800	1.9
Arts and recreation services	215 700	1.8
Rental, hiring and real estate services	212 800	1.8
Information media and telecommunications	211 400	1.0
Electricity, gas, water and waste services	125 500	1.0
Total labour force	**12 133 300**	**95.1***

Source: Australian Bureau of Statistics, Labour Force, Australia, May 2017.

*Excludes 4.9% Other services

The number of employees hired by a business at any time will largely depend on the nature of the products and the number of customers who wish to purchase the products. Generally, the more that is sold the more employees a business will hire. Large businesses employ thousands of people within their organisations.

Businesses employ large numbers of people. However, the SME sector has driven employment growth in Australia, hiring more staff than large businesses do. The SME sector currently accounts for about 66 per cent of all private (non-government) sector employment — approximately 7 million people. During the last 20 years, the SME sector has been the major generator of new jobs in the Australian economy.

Large businesses also make an important contribution. ANZ, for example, employs 21 000 people in Australia. Businesses, therefore, have an important role to play in supporting employment growth in Australia and in reducing unemployment.



FIGURE 1.8 Jobs in the health sector have doubled over the past decade, making the sector the biggest employer in Australia. Two factors that have contributed to this are population growth and ageing demographics.

1.3.3 Incomes

Another important function of business is to provide **income**. For an individual, income is the amount of money received for providing his or her labour. A business's income is the amount it earns after covering all of its expenses: a return on its investments.

There are many different types of income that employees can receive. For example:

- **wage**: money received by workers, usually on an hourly or daily basis, for services they provide to an employer
- **salary**: a fixed regular payment, usually paid on a fortnightly or monthly basis but often expressed as an annual sum, made to a permanent employee of a business
- bonuses: a sum of money added to a person's wages as a reward for good performance
- overtime: time during which work is done outside regular working hours. Such time is usually paid at higher rates.
- commission: the percentage of a sales price received by a salesperson for her or his services
- fringe benefits: an extra benefit supplementing an employee's money wage or salary; for example, a company car, private health care, etc.

A business receives money from the sale of its products. As previously outlined, this is called sales revenue. From this revenue, all the expenses incurred in operating the business must be deducted. The amount that remains is the business's profit. This becomes the business owner's property and consequently their income.

If the business is a private or public company, it will have many owners referred to as **shareholders**. Usually, some or all of a company's profit is divided among shareholders. This type of income is called a **dividend** (see figure 1.9).

BizWORD

Income *is money received by a person for providing his or her labour, or a business from a return on its investments.*

BizWORD

A **wage** *is money received by workers, usually on an hourly or daily basis, for services they provide to an employer.*

A **salary** *is a fixed regular payment, usually paid on a fortnightly or monthly basis but often expressed as an annual sum, made to a permanent employee of a business.*

BizWORD

Shareholders *are people who are part owners of a company because they own a number of shares.*

A **dividend** *is part of a business's profit that is divided among shareholders.*



2014 Interim Dividend

Dear Shareholder(s),

This payment represents an interim dividend of 10 cents per share for the half year ended 31 December 201 shares registered in your name and entitled to participate as at the record date of 11 March 2014. This payme corporate tax rate of 30%.

Please register at www.investorcentre.com/au in order to update your TFN, bank account and other details online.

Sean Simmons
Company Secretary

Class Description	Amount per Security	Number of Securities	Franked Amount	Unfranked Amount	Gross Payment
Ordinary Shares	10 Cents	1,450	$145.00	$0.00	$145.00
				Net Payment	$145.00
				Franking Credit	$62.14

Note: You should retain this statement to assist you in preparing your tax return.

Your Payment Instruction

ANZ
BSB: 014-211 Account number: XXXXXXX72

Amount Deposited
AUD$145.00

FIGURE 1.9 Since shareholders are part owners of a company, they are entitled to a share in the company's profits. Paying a dividend is one way to reward shareholders. A dividend is a distribution of a portion of the company's profit to its shareholders. Let's say Company X generates a profit of $1 million and has a total of 1 million shares on issue. If they wanted to distribute all their profit to shareholders, they could declare a dividend of $1 per share. Most companies, however, prefer to retain at least some of their profits to reinvest in the business.

The amount of income a business can generate to pay wages and salaries, profits or dividends, depends largely on how successful it is in selling its products. A business that is aware of what consumers desire and attempts to satisfy this demand will experience increasing sales. This provides the business with the opportunity to offer higher income payments to employees, business owners and shareholders.

1.3.4 Choice

Choice is the act of selecting among alternatives. For instance, you decide to purchase a new toothbrush. At the local supermarket you find a bewildering array of brands, designs, colours, shapes, textures, packaging, bristle arrangements, sizes and prices. A vast assortment of options — and all for the simple task of brushing your teeth.

In our society, consumers have freedom of choice and the opportunity to purchase a variety of products at competitive prices. An average supermarket will have on display approximately 20 000 product lines, with some hypermarkets carrying in excess of 40 000 lines. Freedom of choice exists when consumers can 'shop around' and select from a range of competitors' products. The more competition there is, the greater the choice available to consumers. Businesses competing with one another are responsible for the wide range of products in the shops. Every day thousands of businesses are producing products for specific sections of the overall market.

BizWORD

Choice *is the act of selecting among alternatives.*

BizFACT

Most businesses usually offer a range of products as this will increase profits in the long term.

SUMMARY

- Profit is what remains after all business expenses have been deducted from sales revenue.
- Profit is the reward that business owners receive for assuming the considerable risks of ownership.
- SMEs provide employment for about 66 per cent of Australia's private sector.
- Businesses generate income for:
  - employees — from wages, salaries, bonuses, overtime, commissions and/or fringe benefits
  - business owners — from profits
  - shareholders — from dividends.
- The amount of income a business can generate as wages, salaries, profits or dividends depends largely on how successful it is in selling its products.
- In our society, consumers have freedom of choice and the opportunity to purchase a variety of products at competitive prices.

1.3.5 Innovation

The definition of **innovation** may vary, but it generally refers to the process of creating a new or significantly improved product, service or process (way of doing something). Invention refers to the development of something that is totally new, but innovation and invention both result in something unique being created.

Ideas for new products, or development of and improvements to existing products, will often provide the opportunity for the establishment of a new business. Many small business concepts are an innovation on an existing product. Blu-ray players and tablet computers, for example, came into existence in the same way as light bulbs and car tyres — that is, through people making technical advances with established products. Sometimes, a person has an idea for a totally new product, an invention, which will satisfy a need that is not presently being satisfied. Patents are legal protection for the exclusive right to commercially exploit an invention.

The way we listen to music has been the subject of innovation over the last century or more. Prior to the invention of the first phonograph by Thomas Edison in 1877, the only way people had been able to listen to music was through live performance. Edison's invention involved playing music that had been recorded on cylinders, but these were eventually superseded by discs in the 1920s. Tape recording was developed in the 1930s and 1940s, with the cassette tape appearing in 1964. Compact discs came onto the market in 1982. Since the 1990s digital recording techniques have allowed for music to be downloaded from the internet, stored on computer hard drives and on solid-state devices such as iPods and USB flash drives. New technological developments soon lead to new products, new markets and new business opportunities.

Many businesses undertake **research and development (R&D)** in order to expand their knowledge of products and processes. According to the ABS, Australian businesses spent $18.9 billion on R&D from 2013 to 2014. Of the $18.9 billion spent, large businesses contributed $11.1 billion, medium-sized businesses contributed $4.6 billion and small businesses contributed $3.2 billion.

SMEs have produced many new products that we take for granted. This is because SMEs generally display a consistently positive attitude towards innovation. They constantly research, develop and test new ideas and products. Many SMEs are built on product innovation.

BizWORD

Innovation *is either creating a new product, service or process, or significantly improving an existing one.*

BizFACT

Each year TIME *magazine publishes a list of what it considers to be the year's 25 great inventions. Some inventions that made the list in 2016 include an artificial pancreas, artificial limbs, Wynd (a portable air cleaner that monitors the air around you and purifies where needed), a levitating light bulb, a folding bike helmet, shoes that tie themselves (Nike Hyperadapt) and tyres that spin in every direction.*

BizWORD

Research and development (R&D) *is a set of activities undertaken to improve existing products, create new products and improve production.*

BizFACT

Businesses in the manufacturing and professional, scientific and technical services industries were the major contributors to the R&D spending.

BizFACT

While Ford closed down their manufacturing facilities in Australia, they retained an Engineering Centre in Broadmeadows, a R&D centre in Geelong and a test facility at Lara. The CEO believes that the Australian R&D facilities are instrumental as part of the company's capability as an innovator and centre of excellence for the Asia–Pacific region. In 2015 alone, Ford spent around $300 million on R&D, bringing to $2 billion the amount of money spent on R&D over the past six years.

Finding new and better ways of doing things has resulted in improved efficiency and increased productivity. Studies confirm that the level of innovation among SMEs employees is much higher than among employees of larger businesses. This is perhaps because Australians have traditionally been a very innovative people, constantly recording the most number of new products per head of population (see the following Snapshot).

SNAPSHOT



'… world-changing inventions that have come out of Australia …'

Great Aussie innovations

How would you describe a country that has invented the Victa lawnmower, Esky, Hills Hoist, Speedo swimwear, StumpCam (a small camera hidden in a cricket stump to provide action replays), wine cask, surf life-saving reel and insect repellent? You might describe it as a sports-loving nation that enjoys an outdoor lifestyle. Of course, the country is Australia! Some other world-changing inventions that have come out of Australia include: black box flight recorders, spray-on skin (to help treat burns victims), the electronic pacemaker, Google Maps, penicillin, polymer bank notes, IVF freezing technique, cochlear implants (for hearing loss), the electric drill, Wi-Fi technology and an ultrasound scanner.

What these lists reveal is that Australians are very innovative. According to the Global Innovation Index, Australia placed 23rd out of 311 countries on the 2017 index on measures of innovation development.

Converting an innovative idea into a business concept often requires the creativity and risk taking of an entrepreneur. Success is something the following Australian business owners achieved due to their innovations:

- Andrew Terry and Michael De Nil began Morse Micro in 2016 based on the development of a new Wi-Fi chip. The pair built a prototype wireless chip called the 'Wi-Fi HaLow' that reaches up to one kilometre, yet only needs one per cent of the power consumed by traditional Wi-Fi chips. This new technology, which is expected to hit the shelves in the next 18 months, is set to power a new generation of smart devices that can talk across neighbourhoods and run for years on a single battery. While the business will initially focus on industrial and agricultural applications, it is hoped the technology will also make its way into smart cities and smart homes by 2020.
- Scott Millar, a seventeen-year-old from Brisbane, began BOP Industries when he was in year 9. The original concept was developed as part of a Year 9 assignment based on running a business. While researching his assignment, he discovered a 'simplistic' form of hologram technology online. From then, it took him just seven days to develop the technology and launch his first product: a holographic entertainment display which is used by event managers, theatre companies and educational facilities.
- The need to solve a problem often leads to a new innovation, as was the case with Hayden Cox who was inspired to develop world-leading surf technology after trying to fix his own broken surfboard. Cox started his business, Haydenshapes, when he was just 15 to build on his passion for surfing and his desire to achieve a better ride. His popular Hypto Krypto boards won the prestigious Surf Industry Manufacturers Association Surfboard of the Year and the surfboard technology he invented has changed the face of the sport.

SNAPSHOT QUESTIONS

1. **Identify** some well-known Australian inventions.
2. **Outline** what is required to convert an innovative idea into a business concept.
3. Select an Australian innovation and **explain** the benefits of that innovation to both the creator and society.

1.3.6 Entrepreneurship and risk

Most of us have seen something advertised and thought, 'That is just what I need'. Someone, somewhere, had the idea to provide this product. Not all inventors or innovators will seek to use their idea as the basis for a business. In many cases

they will be happy to sell their idea to an existing business and let someone else manufacture and market that product. To be willing to take the risk of starting up and operating a business and then working to build that business requires qualities of **entrepreneurship**.

People who transform their ideas into a new business are called **entrepreneurs**. They are prepared to take the **risk** of starting and operating a business venture; of turning their dreams and passions into a livelihood. Entrepreneurs have to take risks because usually they explore untapped markets with no track record of proven consumer demand or guaranteed returns. They cannot be certain that anyone will buy what they plan to sell. But for those whose ideas translate into a successful business venture, the profits are often huge.

If a business fails, its owner may lose all or part of the money he or she has put into it. If people are to take this risk, they must be encouraged by the hope of some reward for success. In our economic system, profit is the return (reward) or payment that business owners receive for assuming the considerable risks of ownership. One of these risks is the risk of not being paid. Everyone else — employees, suppliers and lenders — must be paid before the owners. And if there is no profit, there can be no payment to owners. A second risk is that if the business fails, its owner may lose all or part of the money he or she has put into it.

Bill Gates, co-founder of Microsoft Corporation — the world's most successful computer software company — is a classic example of an entrepreneur (see figure 1.10). While he was a teenager, he decided to take the risk of establishing his own business to market a computer operating system that he and a friend had developed. Today he is one of the world's wealthiest individuals. Entrepreneurs often display flair and creativity. They will frequently find new and innovative ways of promoting their products or services. They will regularly upgrade and adapt their business objectives and recognise new opportunities to expand or diversify their business operations.



FIGURE 1.10 Bill Gates topped the *Forbes* list of the Richest People in the World again in 2017 with a net worth of $85.2 billion. He has held the top spot for 18 out of the past 23 years.

BizWORD

Entrepreneurship *is the ability and willingness to start, operate and assume the risk of a business venture in the hope of making a profit.*

An **entrepreneur** *is someone who starts, operates and assumes the risk of a business venture in the hope of making a profit.*

Risk *refers to the possibility of loss.*

BizFACT

While Bill Gates topped the Forbes *2017 Billionaires List, the next four entrepreneurs on the list (in order) were Warren Buffett (CEO of Berkshire Hathaway, which owns more than 60 companies, including Duracell and Dairy Queen), Jeff Bezos (CEO of Amazon), Amancio Ortega (co-founder of Zara) and Mark Zuckerberg (CEO of Facebook).*

BizFACT

Every new business starts with an idea. Describe a business idea that you could provide and that is, to your knowledge, not already available.

To be a successful entrepreneur you don't need to be running a multi-million dollar company. Many people have achieved entrepreneurial success by running small to medium enterprises (see the following Snapshot).

SNAPSHOT



'… good entrepreneurs should take only calculated risks …'

Case study: Could you be a successful entrepreneur?

Do you have what it takes to be a successful entrepreneur? An entrepreneur is someone who undertakes a new business venture and assumes the risk of its success or failure. One important characteristic many entrepreneurs share is the ability to be highly motivated. Amanda Wong is an example of an entrepreneur with plenty of motivation.

At age 15, Amanda Wong was already turning a profit. In her spare time, she designed brochures and posters for local rock bands and concert events. Today, aged 29, Amanda is the driving force behind Eclipse Publishing & Design, a graphic design business specialising in advertising, brochures, digital photography, logos and publication design. Amanda started the business in 2014, and at the time had no idea it would eventually employ 15 people and have nine overseas clients. Amanda believes 'the business is successful because we offer a diverse range of unique designs not available from many other graphic design businesses'.

In the beginning, cash flow was tight and Amanda had little experience in operating a business. However, she was highly motivated and keen to learn. 'Creating an idea in my head and then seeing it actually appear out there in the world, that's huge to me,' Amanda says. 'I get enormous satisfaction from creating products that delight my clients.'

'If you want to go into business, then you have to realise there will be good days and bad days,' she says. 'I understood there would be risks but good entrepreneurs should take only calculated risks, which is what I did.' In addition to Amanda's self-confidence is her ability to identify business opportunities when they arise. 'If I become aware of an opportunity that will be profitable and help grow the business, it is my responsibility to act. That's the life of an entrepreneur.'

'I knew that commencing a business would require hard work and long hours, but I was totally committed to the idea. I was determined to succeed. Ultimately, it comes down to self-belief. If you want it to work, you've got to believe it will.'

Amanda's venture into the business world has been financially and personally rewarding. She says 'successful entrepreneurs are motivated and passionate about what they do and where they want to go'.

SNAPSHOT QUESTIONS

1. **Identify** the main entrepreneurial characteristics exhibited by Amanda Wong.
2. **Outline** whether you agree with Amanda when she says that good entrepreneurs should take only calculated risks.
3. **Account** for the success of Eclipse Publishing & Design.
4. **Outline** the disadvantages of running your own business.

Entrepreneurial qualities, however, are not confined to adults. For example, at a recent swimming carnival, Yolanda Zurack, a Year 8 student, arranged to take along an Esky filled with cold drinks. To keep her costs down Yolanda bought the drinks through a local wholesaler. During the very hot day she sold all the drinks and made a reasonable profit.

Yolanda Zurack, Bill Gates and Amanda Wong are all entrepreneurs. They organised their business, undertook the necessary arrangements for it to operate and were prepared to take a risk. The size of the profits may differ but they possess identical entrepreneurial qualities: courage, motivation, determination and energy. Without such entrepreneurs and their activities, many of the products we purchase would not exist.

BizFACT

An entrepreneur's drive and motivation to establish and operate a business lies at the heart of our private enterprise economic system.



FIGURE 1.11 At just 12 years old, Bella Tipping started her business Kidzcationz — a website designed to run alongside TripAdvisor which allows kids to get an avatar and rate and review hotels, theme parks and attractions. The business idea started with a brainwave after returning from a family holiday. She saw her mum giving a great review on a hotel that she didn't really like as it was too adult-focused.
Source: Bella Tipping

1.3.7 Wealth

The more that is produced the more wealth is generated within the Australian economy. The thousands of individual businesses operating every day act as the 'engine room' of society, helping drive the economy forward to achieve greater levels of economic growth and wealth.

During normal operations, a business receives money from its customers in exchange for products. At the same time it must also pay out money to other businesses to cover operating expenses. Operating expenses are the costs involved in the day-to-day operation of the business. The difference between the two amounts, the value added, represents the wealth (profit) created by the business. This wealth is then redistributed to employees, governments, lenders, owners/shareholders and the business itself (see figure 1.12).

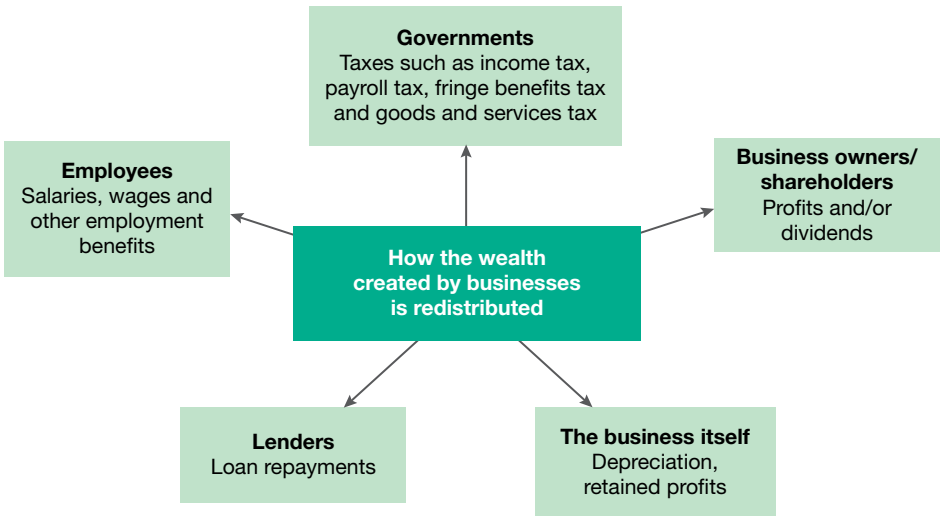


FIGURE 1.12 The distribution of the wealth created by a business

As previously outlined, businesses need to employ people to assist in the production process. These employees receive an income (wage or salary) that can be spent to satisfy their needs and wants. Both the money received and the products purchased add to the wealth of individuals and households. Imagine if all the businesses within your local community were to close down overnight. People would lose their jobs and source of income, fewer products would be available for

purchase, and the flow of money would quickly contract. The end result would be an increase in the levels of poverty, the opposite of wealth creation.

The total output of the country's diverse collection of businesses, ranging from large multinationals to the family-owned local corner store, makes a significant contribution to the wealth of the national economy.

1.3.8 Quality of life

In our society most people want more than the bare necessities; they want to achieve the highest standard of living possible. Overall, we have high expectations about what our economy should provide for us. However, we often want more than simply to have our material wants satisfied. We also desire a high degree of quality in our lives. **Quality of life** refers to the overall wellbeing of an individual, and is a combination of both material and non-material benefits.

For example, we desire to have leisure time for hobbies and recreation. Our quality of life is improved by having access to a number of non-material products such as fresh air and clean water, unpolluted earth, conservation of wildlife and protection from toxic sources. Consumers have become increasingly concerned about waste disposal, the greenhouse effect and the destruction of unique habitats.

Many businesses have responded to quality-of-life issues and are implementing environmentally friendly procedures, for example recycled materials, cleaner cars, less energy-consuming production and 'green' food products. Because business activities play a vital role in our lives, businesses have a responsibility to help provide what consumers want and to minimise what they do not want.

BizWORD

Quality of life *refers to the overall wellbeing of an individual, and is a combination of both material and non-material benefits.*

BizFACT

Sanofi is an Australian pharmaceutical company focused on improving people's health and quality of life. Through investment in medical research and development, the company has developed leading prescription medicines across a range of therapeutic areas, as well as a diverse portfolio of vitamin and mineral supplements. Sanofi are the world's largest vaccine manufacturer and have also produced a range of transformative therapies for people affected by rare and debilitating diseases.

BizFACT

Australia is still seen as one of the best places to live but is sliding in global rankings when it comes to the environment and press freedom. In the 2017 Social Progress Index, which measures quality of life and the wellbeing of society independent of wealth, Australia dropped from 4th to 9th place.

SUMMARY

- Research and development (R&D) leads to innovation (the creation of new products, services or processes, or the improvement of existing ones).
- People who transform their ideas into a new business are called entrepreneurs. They are prepared to take the risk of starting and operating a business venture in the hope of making a profit.
- An entrepreneur's drive and motivation to establish and operate a business lie at the heart of our private economic system.
- Business is a major creator of wealth within the Australian economy.
- Businesses produce a vast range of products that enable us to satisfy many and varied wants, which results in a higher standard of living.
- Quality of life refers to the wellbeing of an individual, and is a combination of material and non-material benefits.

EXERCISE 1.2 REVISION

1 **Recall** the main activity of a business.

2 **Describe** the relationship between revenue, operating expenses and profit.

3 **Calculate** which of the following businesses has made a profit.
   (a) Sally's Pet Shop has expenses of $2000 per week and revenue earned is $3500 per week.
   (b) Ben's Gardening Supplies takes revenue of $6000 each week for a month, but has weekly expenses of $7000 the first week, $8000 the second and third week, and $3000 for the fourth week.

4 **Evaluate** the significance of the SME sector's contribution to total employment within the Australian economy.

5 **Outline** the three ways in which businesses provide income.

6 **Recall** the correct term and complete the table below.

Term	Meaning
A. Income	
B. Wage	
C.	A fixed amount of money paid on a regular basis to a permanent employee of a business.
D. Shareholder	
E.	Part of a business's profit that is divided among shareholders.

7 **Define** the term 'choice'. **Explain** how businesses encourage freedom of choice.

8 **Outline** the role innovation plays within our economy.

9 **Outline** the role of the entrepreneur in our economic system.

10 **Explain** why people take risks.

11 **Describe** the two main risks associated with operating a business.

12 **Identify** the entrepreneurial characteristics that Yolanda Zurack, Bill Gates and Amanda Wong have in common.

13 **Assess** your own entrepreneurial ability by completing the following questionnaire.

Question	Yes	No
(a) Are you willing to take moderate risks?		
(b) Are you easily motivated?		
(c) Do you get on well with people?		
(d) Is your health excellent?		
(e) Do you set realistic goals?		
(f) Are you prepared to accept responsibility?		
(g) Can you tolerate failure?		
(h) Do you have a positive self-image?		
(i) Are you well organised?		
(j) Are you a hard worker?		

Someone with an entrepreneurial personality would answer 'Yes' to most of the questions. Write a self-evaluation report based on your answers. **Compare** your response in class.

14 **How** do businesses create wealth within the economy?

15 **Identify** the ways in which the wealth created by a business is redistributed.

16 **Justify** which is a more important contributor to a person's quality of life — material or non-material benefits. Provide reasons for your answer.

EXERCISE 1.2 EXTENSION

1 A profitable business is one that returns to its owners *more* than they could earn by working for someone else. According to this definition, many businesses operating today would not be considered profitable. **Determine** why their owners continue to run them. Share your answer with the rest of the class.

2 **Construct** a three-minute presentation titled 'How businesses contribute to our economic and social wellbeing'. Prepare some multimedia materials to supplement the oral presentation.

3 'The mother of invention/innovation is necessity.' **Justify** this statement.

4 In small groups, **predict** the social consequences of an economy that is experiencing a large number of business failures. **Compare** your answer with other groups.

5 In small groups, **identify** someone who successfully runs a small business. **Critically analyse** the personal qualities this person possesses that contribute to the success of the business.

6 The Entrepreneur Network for Young Australians Ltd (ENYA) is a not-for-profit public company that 'promotes the active participation of young people in enterprise, in an ethical and sustainable manner'. **Examine** the main functions of this organisation. The **ENYA** weblink in the Resources tab may assist.

on Resources

- **Weblink:** ENYA
- **Digital doc:** Chapter summary (doc-26093)
- **Interactivity:** Chapter crossword (int-7211)
- **Interactivity:** Multiple choice quiz (int-7212)

CHAPTER 2

Types of businesses

OVERVIEW

2.1 Introduction
2.2 Classification by size
2.3 Classification by geographical spread
2.4 Classification by industry sector
2.5 Classification by legal structure
2.6 Types of companies
2.7 Factors influencing choice of legal structure

2.1 Introduction

As explained in chapter 1, any organisation that sells goods and services to consumers in order to make a profit is a business.

Businesses may be organised in a variety of ways. Although no two businesses are identical, some common features that allow similar business types to be classified and grouped together. Figure 2.1 illustrates the four methods commonly used to classify businesses.

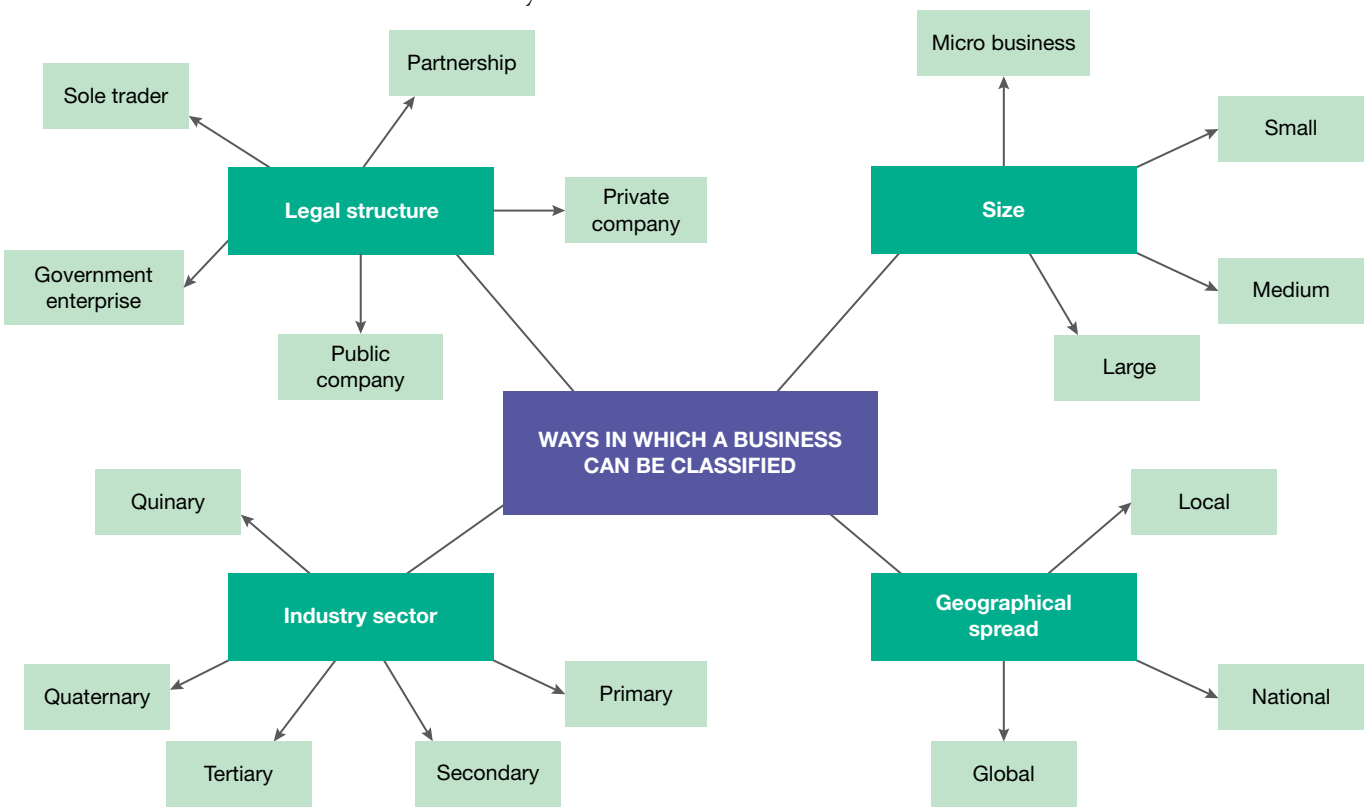


FIGURE 2.1 The four methods commonly used to classify businesses

2.2 Classification by size

Like soft drinks, businesses come in three different sizes: small, medium and large. Most people usually associate the term 'business' with large companies such as Woolworths, Commonwealth Bank and Westfield, which employ thousands of people across hundreds of locations. However, 98 per cent of businesses in Australia are small to medium enterprises.

Although no universally accepted definition exists for a small, medium or large business, a number of measurements can be used to determine the size of a business, including:

- the number of employees — those who are hired to do work for the business
- the number of owners (of the business) — for example, a sole trader is a type of business that has one owner
- **market share** — the proportion of total market sales the business has compared to competitors
- the legal structure — for example, the business is set up as a sole trader, partnership or company.

Apart from quantitative measures, such as the number of employees, qualitative descriptions also help us to determine the size of a business. These qualitative measures are based on personal observation about the business. From a qualitative viewpoint, a business may be classified as small or medium-sized if:

- the owner makes most management decisions, such as who to hire, what to produce and how to advertise a product
- the owner provides most of the capital (finance)
- the business has little control within the market. Smaller businesses do not usually have a large share of the total market sales and therefore have less control over such things as price.
- it is independently owned and operated (for example, the local hamburger shop is run by the owner, who does not answer to a larger organisation such as McDonald's)
- the business is locally based. (This does not mean that it doesn't export, because many SMEs do export. It just means that many SMEs are based in the one location and, unlike a **multinational corporation** or company, do not have offices around the world.)

Using quantitative measurements from the Australian Bureau of Statistics (ABS), businesses can be defined as follows:

- **Micro business**: a business with fewer than five employees.
- **Small business**: a business with 5–19 employees.
- **Medium business**: a business with 20–199 employees.
- **Large business**: a business with 200 or more employees.

A comprehensive definition of small, medium and large business usually relies on a combination of both quantitative measurements and qualitative descriptions, as shown in table 2.1. This table also outlines the features of, and distinctions between, the different sized businesses.

There is an additional category of business size called **small to medium enterprises** (SMEs). SMEs are defined by the Australian Bureau of Statistics as firms with fewer than 200 full-time equivalent employees and/or less than $10 million turnover. SMEs play an especially important role within the Australian economy. As consumers, we rely on a large number of SMEs to satisfy our needs and wants. These businesses also provide employment for about 7 million people. The role and contribution of SMEs will be looked at in greater detail in Chapter 10.

Table 2.2 illustrates the number of businesses by size as of June 2016.

BizWORD

Market share *refers to the business's share of the total industry sales for a particular product.*

BizWORD

A **multinational corporation** *is a company that has branches in many different countries.*

BizWORD

A **micro business** *is a business with fewer than five employees.*

A **small business** *is a business with 5–19 employees.*

A **medium business** *is a business with 20–199 employees.*

A **large business** *is a business with 200 or more employees.*

BizWORD

Small to medium enterprises *are defined by the Australian Bureau of Statistics as firms with fewer than 200 full-time equivalent employees and/or less than $10 million turnover.*

TABLE 2.1 Quantitative measurements and qualitative descriptions of small, medium and large businesses

Characteristics	Small	Medium	Large
Business type	Corner store Local mechanic Hairdressing salon	Services club Motel/hotel Engineering factory	Woolworths Qantas National Australia Bank
Number of employees according to the Australian Bureau of Statistics (ABS) business register definition	Fewer than 20 employees	20–199 employees	200 or more employees
Type of ownership	Independently owned and operated by usually one or two people	Owned and operated by a few people and/or private shareholders	Owned usually by thousands of public shareholders
Most common legal structure	Sole trader Partnership	Partnership Private company	Public company (numerous)
Decision making	Owner responsible for majority of decisions; simple and quick implementation of decisions	Owner basically responsible for majority of decisions; more complicated decision making with slower implementation, due to influence of directors	Complex decision making, due to division of responsibilities among directors, senior and middle management; possibly slow implementation of decisions, due to the layers of management
Sources of finance	Owner (usually from own savings or a loan); difficulty in accessing loans	Owners'/partners' own savings or a loan and/or private shareholders; easier accessibility to larger loans	Many sources, including cash reserves, retained profit, sale of shares, and loans from domestic and overseas institutions
Market share	Small, usually local area; not dominant in the industry	Medium, due to dominance within a geographic region; some market dominance	Large, especially for multinational corporations that dominate the markets of many countries

TABLE 2.2 Number of Australian businesses by size in June 2016

Business by size (by employee no.)	Number
0 employees	1 318 568
1–4 employees	599 392
5–19 employees	198 655
20–199 employees	50 808
200+ employees	3774
TOTAL (AUSTRALIA)	2 171 197

Source: *ABS Catalogue 8165.0 Counts of Australian Businesses, including Entries and Exits, June 2012 to June 2016.*



FIGURE 2.2 While the SME sector is the biggest employer in Australia, is it the better employer? Some of the benefits of working for a SME are that it is usually a more casual environment, there is greater access to management and there is less bureaucracy. The benefits of working for a large business are that there are usually greater perks, access to more resources, better training and development, higher pay and more opportunities for promotion.

2.3 Classification by geographical spread

Consider the suburb or town in which you live. This area can be classified as your local community or neighbourhood — that is, a group of people living and working in the same locality. The consolidation of all these local communities is what forms the nation of Australia. Now, broaden your scope even further. Australia is just one of the 195 independent nations that are part of the global network.

Businesses, too, can be classified as local, national or global according to their **geographical spread**: the presence of a business and the range of its products across a suburb, city, state, country or the globe.

BizWORD

Geographical spread *is the presence of a business and the range of its products across a suburb, city, state or country or the globe.*

2.3.1 Local

A **local business**, such as a newsagent, corner store, hairdresser, mechanic or pharmacy, has a very restricted geographical spread. It serves the surrounding area and is in no position to offer a range of products to another suburb or town. Local businesses such as these will frequently be used by consumers who live nearby. The majority of local businesses tend to be small to medium in size.

BizWORD

A **local business** *has a very restricted geographical spread; it serves the surrounding area.*



FIGURE 2.3 Mario and Rosa own Hair to Toe, a hairdressing salon in Drummoyne. They understand the individual needs of all their clients, and the long-standing support they receive from the local area is testament to this. They provide a range of professional services to people in Drummoyne and surrounding suburbs and have established a great reputation in the area.

2.3.2 National

As a business grows, it increases its range of products and the area it serves. As it does this, it develops into a **national business** — one that operates within just one country. Coles, for example, commenced trading in 1914 as G.J. Coles variety store in Collingwood, Victoria. Started by George Coles and his brother Jim, it employed six people. Today, Coles is a leader in Australian food retailing, with more than 99 000 employees and over 19 million customer transactions a week.

BizWORD

A **national business** *is one that operates within just one country.*

BizFACT

David Jones is not only Australia's oldest department store, but also the oldest department store in the world still trading under its original name. For the 2016 financial year, its sales revenue was $2.2 billion, up 8.4 per cent from the previous year.

Other well-known Australian businesses that serve the national market include:

- Australian Geographic — stores that specialise in Australiana, children's games, gadgets, telescopes, travel and outdoor products. The *Australian Geographic* magazine was started in 1985 by Australian entrepreneur and adventurer Dick Smith. Today the magazine operates more than 70 stores across Australia.
- Sportsgirl — the boutique that became a major Australian fashion brand. The company offers a wide range of fashion and accessories, and has over 120 stores across Australia. Founded in Melbourne in 1948, Sportsgirl today holds a dominant place in Australia's retail fashion market.
- David Jones — one of Australia's oldest department stores. In 1838, just 50 years after the First Fleet arrived in Sydney Cove, Mr David Jones opened 'large and commodious premises' on the corner of George and Barrack streets, Sydney (see figure 2.4) and they now have 43 stores in various locations throughout Australia.
- McGrath Estate Agents — one of the most successful residential real estate groups. John McGrath began the business in 1988 from a small office in Woollahra. Today, the company has expanded to more than 102 offices across the east coast of Australia.



FIGURE 2.4 David Jones originally began with one store in Sydney in 1838. They gradually expanded over the years and now operate 43 stores around Australia.

As a national business expands and increases its sales, it will eventually run out of new customers to sell to; that is, the domestic market becomes saturated. If the business wishes to keep expanding, it can decide to export and sell its products in other countries. This allows the business to tap into new markets.

BizWORD

A **multinational** *corporation is a large company that has branches in many different countries.*

2.3.3 Global

A global business, commonly referred to as a **multinational** corporation, is a large company that has branches in many different countries. The multinational corporation represents the highest level of involvement in global business. For such companies,

national borders do not represent barriers to trade — they are merely lines on a map. Consequently, multinational corporations conduct a large percentage of their business outside their home country.

Multinational corporation come in many different forms and sizes. Coca-Cola, LG, McDonald's, CSR, News Corporation, BHP, Toyota, Unilever, Westfield and Exxon are just a few of the well-known foreign and Australian multinational corporations. However, all multinational corporations have a number of features in common. In a fully developed multinational corporation, finance, assets, technology, information, employees and goods and services all flow freely from one country to another (see the following Snapshot).

BizFACT

Some multinational corporations have grown so large that their annual revenues from worldwide sales exceed the GDP of many nations. (GDP, or gross domestic product, is the total value of all goods and services produced in an economy in a given year.)

The global expansion of one Australian business

Case study: Westfield Group — global expansion

When Frank Lowy and John Saunders first came to Australia in the 1950s, there wasn't one shopping centre in the entire country. At the time, most shopping was done in large department stores in major cities. In 1959 the pair became business partners and opened their first shopping centre in Blacktown. They have both since grown to become one of the world's largest shopping centre owners and managers. The company they began, Westfield, is now a market leader in Australia, New Zealand, the United States and the United Kingdom. Throughout its history, Westfield has played a significant role in changing the way the world shops.

Westfield began as a public company listed on the Sydney Stock Exchange in 1960. In that same year, they built their second shopping centre in Hornsby with the money they raised from the float.

After opening new shopping centres throughout Sydney in the 1960s, Westfield expanded interstate in 1967 with the opening of Toombul in Brisbane, followed by Doncaster in Melbourne in 1969. They continued to expand nationally and currently have centres in all major metropolitan cities as well as some regional centres throughout Australia.

Since the 1950s Saunders and Lowy have made regular trips to the United States to learn more about shopping centres. By the 1970s they had become concerned that Australia could only accommodate a finite number of centres due to its limited population. This concern led them to begin thinking about expanding into overseas markets. In 1980 Westfield expanded globally by acquiring their first shopping centre overseas in Connecticut in the United States. Within three years, they owned another three centres in that market. Since entering the United States market, they have continued to expand. Today, Westfield has a portfolio of 47 centres in the United States.

Westfield entered the New Zealand market in 1998 when they acquired St Luke's Group Ltd, which owned 10 centres. Upon taking over this company, they branded those centres Westfield. Their expansion into New Zealand has mainly been through buying existing shopping centres. They currently have an interest in nine centres in New Zealand.

Also in 2000, Westfield entered the United Kingdom with the acquisition of a centre in Nottingham. This was followed by the establishment of a joint venture interest in other centres in major cities. Today, Westfield has a portfolio of five shopping centres in this market.

In 2011, Westfield entered two new markets, Italy and Brazil. Their entrance into Italy was through a joint venture with Gruppo Stilo. The project involved the development of a world class iconic regional shopping centre in Milan. While they also entered into a joint venture project with Brazilian company Almeida Junior, Westfield sold their 50 per cent share in this venture back to the original partner in 2013. They are, however, still planning a re-entry into Brazil soon.

Westfield Group continues to expand their portfolio by either acquiring sites with development opportunities in new markets or by redeveloping existing malls.

SNAPSHOT



"… Westfield has played a significant role in changing the way the world shops."

on Resources

Weblink: Westfield

SNAPSHOT QUESTIONS

1. **Outline** how Westfield enters new markets overseas.
2. **Explain** why Westfield decided to expand globally.
3. **Construct** a timeline of Westfield's global expansion.
4. **Explain** how Westfield has changed the way the world shops.

SUMMARY

- Businesses can be classified as small, medium or large.
- Their classification will depend on such things as number of employees, market share, ownership and who makes the decisions.
- A micro business (usually a SOHO) employs fewer than five people (including the owner).
- Businesses can also be classified as local, national or global according to their geographical spread.
- A local business has a very restricted geographical spread; it serves its surrounding area.
- A national business operates in just one country.
- A global business — a multinational corporation (MNC) — is a large business with a home base in one country that operates partially owned or wholly owned businesses in other countries.

EXERCISE 2.1 REVISION

1 **Deduce** whether the following businesses are small, medium or large, and **explain** the reason for your decision.
(a) Qantas employs approximately 37 000 people.
(b) National Australia Bank is an international financial services organisation that has customers in Australia, New Zealand, Asia, the United Kingdom and the United States.
(c) Brookfarm is owned by Carolyn and Martin Brook. It produces gourmet macadamia nuts for domestic and export markets, and employs more than 20 staff.
(d) Ripe Maternity Wear was started by two friends in 1996 to manufacture contemporary maternity clothes. It supplies clothes worldwide, employing no more than 20 staff.

2 **Determine** whether the following statements are true or false.
(a) A micro business is a business that sells only miniature products.
(b) SME stands for small to medium enterprise.
(c) Small businesses do not usually have a large share of a particular market.
(d) According to the Australian Bureau of Statistics, large businesses employ fewer than 200 people.
(e) SMEs do not play an especially important role within the Australian economy.
(f) An enterprise is just another name for a business.

3 Complete the following statements by **determining** the correct word from the choices given. Write the sentences in your notebook.
(a) According to the ABS, a business with fewer than *200/300* employees is classified as a medium-sized business.
(b) A common feature of all small businesses is that they are *independently/interdependently* owned and operated.
(c) Small businesses have a *complex/simple* management structure with *few/many* rules and regulations.
(d) The number of employees in a business is a *quantitative/qualitative* measure.
(e) A small business has a *large/small* market share and usually serves the *Australian/local* market.

(f) An example of a small business is *Westfield Limited/Blue Hills Convenience Store*.
(g) Most small businesses are *sole traders/public companies*.

4 **Compare** a micro business with a small business.

5 **Examine** table 2.2 and answer the following questions.
(a) **Calculate** what percentage of businesses would be considered micro businesses.
(b) **Calculate** what percentage of businesses are SMEs in Australia.

6 **Define** the term '*geographical spread*'.

7 **Distinguish** between a local and national business. Provide two examples of each.

8 **Recall** another name for a global business.

9 **Identify** three examples of multinational corporations.

10 **State** what features all multinational corporations have in common.

EXERCISE 2.1 EXTENSION

1 **Construct** a database of seven businesses that you have dealt with over the last few months. Copy and then complete the following table. The first one has been done for you.

Business name	Business activity	Size: small, medium, large
1. Redback Café	Food and drink	Small
2.		
3.		
4.		
5.		
6.		
7.		
8.		

(a) **Calculate** what percentage of the businesses are small.
(b) **Outline** the criteria you used to classify the size of each business.
(c) **Compare** the percentage with the figures for Australia.
(d) **Account** for the similarity/difference between the two figures.

2 **Critically analyse** the following statement: 'Multinational corporations play a crucial role in our society. Without them, consumers would not have such a wide range of products to select from.'

3 Look for five internet or newspaper articles about SMEs that interest you. Start a file of news clippings or printouts and write an information page to attach to each article. On the information page:
(a) **summarise** what the article is about
(b) **examine** some background information about the business.

4 Adidas and Levi Strauss are two multinational corporations that place a great deal of importance on their corporate social responsibilities. Both companies have taken action against overseas suppliers over human rights issues and environmental codes of conduct. Use the **Adidas** and **Levi Strauss** weblinks in the Resources tab and **investigate** their commitment to their social and environmental obligations. **Create** either an oral or written report and present it to the rest of the class.

5 Arrange to inspect an annual report for one of Australia's large multinational corporations. **Investigate** the company's operations. To help you, use the **Multinational corporations** weblinks in the Resources tab.

on Resources

Weblink: Adidas
Weblink: Levi Strauss
Weblink: Multinational corporations

2.4 Classification by industry sector

BizWORD

An **industry** *consists of businesses that are involved in similar types of production.*

Another useful method used to classify businesses is based on the type of activity they undertake. When businesses are involved in similar types of production, they are grouped together in what is referred to as an **industry**. Australian companies like Woolworths, Wesfarmers, JB Hi-Fi and Officeworks belong to the retail industry.

There are five main types of industry groupings or sectors: primary, secondary, tertiary, quaternary and quinary (see figure 2.5).

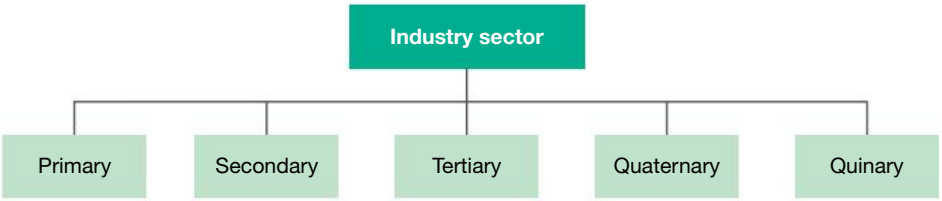


FIGURE 2.5 The five main industry sectors

The relative size of each industry sector is shown in figure 2.6. This graph shows both the percentage of private sector firms and the employment in each industry sector.

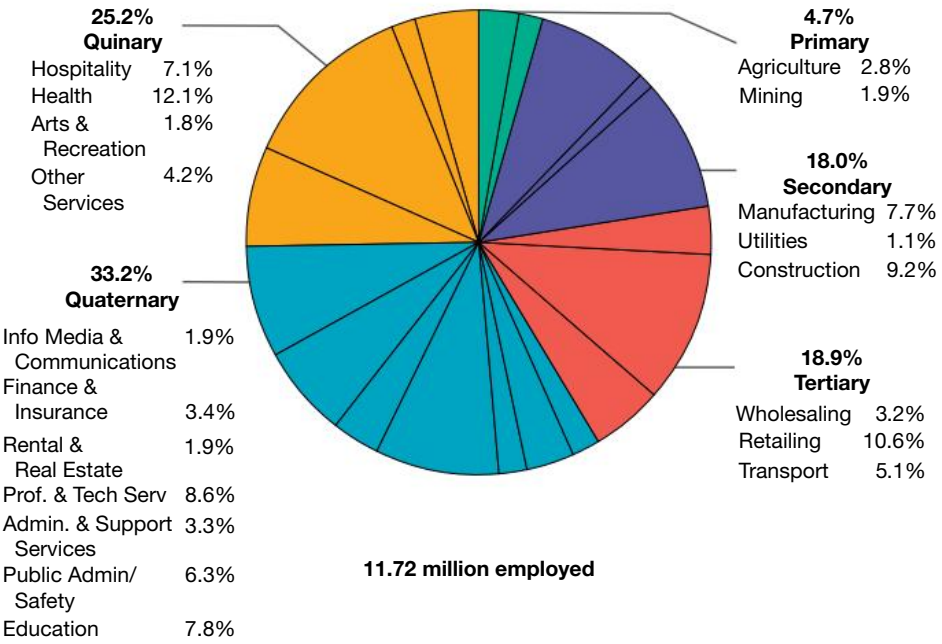


FIGURE 2.6 Australia's industry mix as a share of total employment, 2014–15
Source: ABS and Ibisworld.com.au

2.4.1 Primary industry

BizWORD

Primary industry *includes those businesses involved in the collection of natural resources.*

Primary industry includes those businesses involved in the collection of natural resources. Examples of these businesses include all types of farming, mining, fishing, grazing and forestry. Even though this sector employs only 4.7 per cent of the labour force, its role is essential because it provides all of our food requirements. As well, approximately 60 per cent of all our exports come from these industries.

2.4.2 Secondary industry

BizWORD

Secondary industry *involves taking a raw material and making it into a finished or semi-finished product.*

Secondary industry includes all those businesses that take the output of firms in the primary sector (raw materials) and process it into a finished or semi-finished product. For example, iron ore, coal and limestone are turned into steel — a

semi-finished product that is then used to manufacture cars. Steel and car manufacturers are both examples of secondary industry businesses.



FIGURE 2.7 In June 2016, the construction sector experienced its highest level of growth in 10 months. This was just after the Reserve Bank cut the official interest rate to 1.75% in May. Residential construction (in particular the sub-sectors of house and apartment building) showed the largest growth, recording its fastest rate of expansion in two-and-a-half years. The government's pledge to spend more than $20 billion on infrastructure will also aid the construction and engineering sector.

2.4.3 Tertiary industry

The **tertiary industry** involves people performing a vast range of services for other people. Examples include retailers, dentists, solicitors, banks, museums and health workers.

BizWORD

Tertiary industry *involves people performing a vast range of services for other people.*



FIGURE 2.8 Retail sales have been declining in 2017 and growth in the retail industry has slowed to 2.1 per cent, the slowest rate of growth in almost four years. The decline in retail sales figures can be attributed to low consumer confidence, low wage growth, increasing competition domestically and from overseas, high household debt and the high cost of housing.

on Resources

Weblink: Primary, secondary and tertiary industries

BizWORD

Quaternary industry *includes services that involve the transfer and processing of information and knowledge.*

2.4.4 Quaternary industry

Quaternary industry includes services that involve the transfer and processing of information and knowledge. Examples include telecommunication, property, computing, finance and education.



FIGURE 2.9 Some of the factors driving the growth in the quaternary sector include: the rapid growth in e-commerce and internet-based business activity, advances in telecommunications technologies and an increased demand for online education.

BizFACT

It is estimated that by 2050, the quaternary and quinary sectors combined are likely to account for two-thirds of the economy.

BizWORD

Quinary industry *includes all services that have traditionally been performed in the home.*

2.4.5 Quinary industry

Quinary industry includes all services that have traditionally been performed in the home. Examples include hospitality, tourism, craft-based activities and childcare. It includes both paid and unpaid work.



FIGURE 2.10 In recent years, Australia has experienced a huge surge in demand for formal childcare. The main factor that has fuelled this growth is the expectation that women will go back to work after giving birth. In 2010 there were about 5900 long day care centres nationally, but now there are well over 10 000. Over 660 000 kids are currently enrolled in long day care and the sector is projected to continue increasing dramatically.

2.4.6 How changes in external influences have contributed to the growth of the tertiary, quaternary and quinary industries in Australia

Changes in external influences have altered the proportion of employees working in Australia's historical industry sectors and contributed to the growth of the tertiary, quaternary and quinary industries. In 1900, about one in three employees worked in primary industries, mainly mining and farming. Currently, the proportion of employees working in the primary industry has decreased significantly because of improved methods of farming and mining, as well as the increased use of mechanical equipment. Today, fewer workers are required to produce our food supply and minerals.

For a while, many workers who left the farms and mines moved to jobs within the secondary industries. Recently, however, the proportion of the labour force needed to do factory work has also decreased because many jobs have been eliminated by technology, especially automation. In addition, increased overseas competition, increased trade and changes in government policies have also led to a decline in employment in this industry.

In the past there were only three industry sectors: primary, secondary and tertiary. Since opportunities for employment in the primary and secondary industries have decreased over the past 50 years, the number of businesses and people employed in the tertiary industry sector has grown rapidly, to a point where today, about three out of every four employees and two out of every three businesses are classified as tertiary. Due to this increase, the tertiary sector has been subdivided into two other sectors: quaternary and quinary.

The quaternary sector is expected to undergo dramatic change over the next 20 years due to the rapid advances in telecommunications. Expansion in e-commerce and internet-based business activity will see an increase in the number of people employed in information processing and analysis.

Due to social and lifestyle changes, as well as an increase in the number of two-income households, the demand for quinary-type services is also estimated to expand rapidly during the next two decades. Many small businesses in particular have recently begun providing these services, filling a niche in the market.

This growth in employment in the service industries is expected to continue increasing rapidly due to technological and social changes.

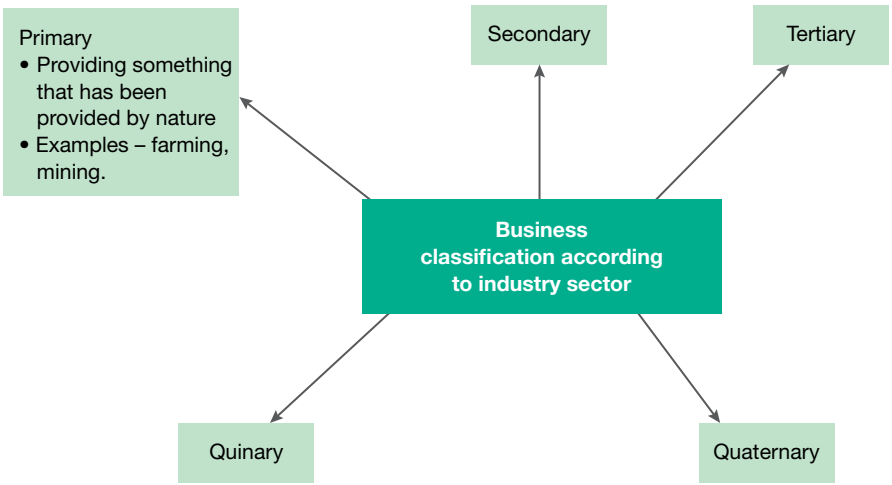
SUMMARY

- An industry consists of businesses that are involved in similar types of production.
- Primary industry — businesses involved in collection of natural resources.
- Secondary industry — production of finished or semi-finished goods.
- Tertiary industry — performing a service.
- Quaternary industry — services that involve the transfer and processing of information and knowledge.
- Quinary industry — services that have traditionally been performed in the home.

EXERCISE 2.2 REVISION

1 **Distinguish** between a business and an industry.

2 **Construct** a mind map summarising the five industry sectors. Provide examples for each sector. The concept map has already been started for you on the following page.



3 In your notebook **construct** a table with five columns. At the top of the columns put the headings Primary, Secondary, Tertiary, Quaternary and Quinary. From the list of businesses, **determine** the correct column for its particular industry group and write in its name. The first one has been done for you.

Primary	Secondary	Tertiary	Quaternary	Quinary
Tallong Orchards				

Tallong Orchards
S. & W. Legal Centre
Bowral Bricks
Clancy's Restaurant
Pollards Removalists
Moo Moo Pastures Dairy
Bald Hill Quarry
Crookwell Real Estate
Finlay's Fine Furniture
Creative Hands Craft School
Data Transfer Computing
National Australia Bank
Tiggy Wiggles Child Care Centre
Hi Plains Merino Stud
Southern Tablelands Towing
Centretown Motel
B. S. Plastics Manufacturers
Country Furniture Constructions
Pioneer Water Tanks
Access TV Productions

4 **Outline** reasons for the growth in the tertiary sector over the past 50 years.

5 Refer to figure 2.6 and answer the following questions.
(a) **Identify** which industry sector employs the most people in Australia.
(b) **Identify** which industry sector employs the fewest people in Australia.
(c) **Why** do you think the industry you identified in part (b) employs the smallest number of Australians?

EXERCISE 2.2 EXTENSION

1 (a) **Construct** a flowchart showing the industry sectors involved in the production of a car.
(b) **Analyse** the relationship between the various sectors.

2 (a) **Construct** a list of tertiary jobs that are essential for the production of a:
(i) television game show
(ii) local newspaper
(iii) hi-fi system, bought at an electronics store.
(b) Place the letters 'Qt' next to those jobs that would be classified as quaternary and the letters 'Qn' for those jobs in the quinary sector.
(c) **Deduce** what your list reveals.

3 **Investigate** why the quinary sector has included in it unpaid, voluntary jobs.

2.5 Classification by legal structure

There are a number of different legal structures to choose from when deciding how a business is to be owned and operated. The four main legal structures of privately owned businesses are shown in figure 2.11 — sole trader, partnership, private company and public company..

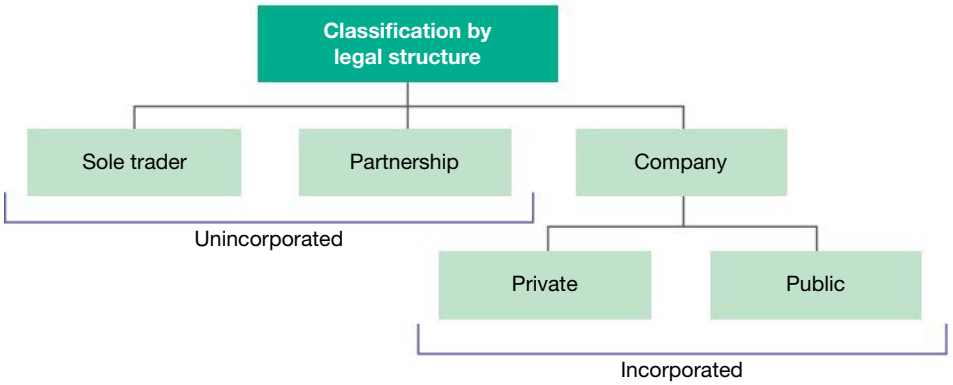


FIGURE 2.11 The four main legal structures of privately owned businesses

BizFACT

ABS data show that the number of partnerships continued to decrease in 2016 by almost 4 per cent. However, after three years of consecutive negative growth, there was a 2 per cent increase in sole traders in 2016.

Meanwhile, companies and trusts increased by 10 per cent each. Companies and trusts have always made up a large portion of Australia's business numbers, and in 2016, they made up over 60 per cent of all businesses.

2.5.1 Incorporated and unincorporated business structures

As figure 2.11 shows, the four main legal structures of privately owned businesses can be further divided into:

- unincorporated businesses, in the case of sole traders and partnerships
- incorporated businesses, in the case of privately and publicly owned companies.

The term **incorporated** refers to the process companies go through to become a separate legal entity from the owner/s. This means the business exists in its own right, its own legal entity. Regardless of what happens to individual owners (shareholders) of the company, the business continues to operate. The business has taken on a life of its own.

BizWORD

Incorporated *refers to the process companies go through to become a separate legal entity from the owner/s.*

An unincorporated business has no separate legal existence from its owner(s) and will be either a sole trader or partnership. This means the business entity and the owner(s) are one and the same. When the owner dies then so too does the business entity.

The most common legal structure for small businesses in Australia is the unincorporated business entity, for example sole traders and partnerships (see figure 2.12),

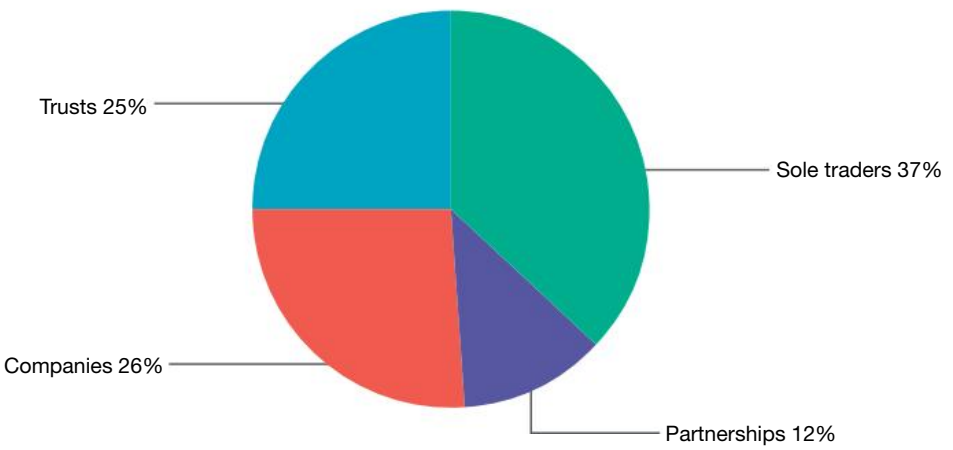


FIGURE 2.12 Business structure for SMEs in Australia

because this structure is the easiest and cheapest to establish. Companies and trusts are examples of incorporated legal structures, and are generally medium to large businesses.

Selecting the appropriate business structure is one of the most important decisions a business owner has to make. Each of the different legal structures is covered by different government regulations that must be followed and, as such, have an enormous effect on the overall running of the business.



FIGURE 2.13 Some businesses, such as Myer, start off small, either as sole traders or partnerships; but because they are limited in size and growth potential they later decide to become incorporated.

2.5.2 Sole trader businesses

BizWORD

*A **sole trader** is a business that is owned and operated by only one person.*

A **sole trader** is a business that is owned and operated by one person. The owner may employ other people to work in the business, but the owner or sole trader is the person who provides all the finance, makes all the decisions and takes all the responsibility for the operation of the business.

This type of business is easy to establish in terms of legal requirements. The only legal requirement specific to a sole trader is that the name of the business be registered if the name is different from that of the owner. For example, if Paul Jones operates a lawn-mowing service under the name of P. Jones or Paul Jones, then the name of his business does not need to be registered. If, however, he calls his business 'Paul's Lawn and Garden Service', he would have to register the name. The name must be registered with the Australian Securities and Investment Commission (ASIC).

BizFACT

ABS data has shown that sole traders have the lowest survival rate, with only 51 per cent surviving from June 2012 to June 2016.

A sole trader is not regarded as a separate legal entity; that is, the owner and the business are regarded as the same. This means that if the business is sued then the owner is sued, or if the business enters into a legal contract then the owner enters into the contract. If the business runs into financial difficulties, it is the owner or sole trader who has the financial problem and is solely responsible for the finances of the business. This responsibility may include selling personal assets, such as property or motor vehicles, to pay for the liabilities of the business. This is referred to as **unlimited liability**.

BizWORD

***Unlimited liability** occurs when the business owner is personally responsible for all the business's debt.*

The advantages and disadvantages of being a sole trader are shown below.

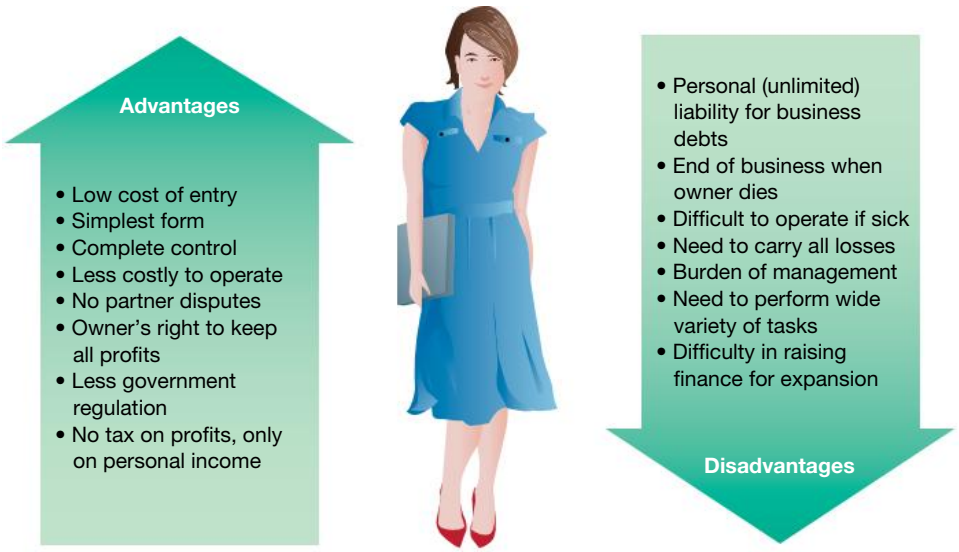


FIGURE 2.14 The advantages and disadvantages of being a sole trader

on Resources

Weblink: Sole trader

SUMMARY

- The four main legal structures of privately owned businesses are sole traders, partnerships, private companies and public companies.
- Privately owned business structures can be either unincorporated or incorporated.
- A business that is incorporated becomes a separate legal entity from the owner/s.
- A sole trader — an unincorporated business entity — is a business that is owned and operated by one person and has unlimited liability.

2.5.3 Partnerships

A **partnership** is a legal business structure that is owned and operated by between two and 20 people. There are exceptions to this number, including medical practitioners and stockbrokers (allowed up to 50 partners); veterinarians, architects and chemists (allowed up to 100 partners); and solicitors and accountants (allowed up to 400 partners). A partnership is similar to a sole trader in that the owner and

BizWORD

*A **partnership** is a legal business structure that is owned and operated by between two and 20 people with the aim of making a profit.*



FIGURE 2.15 Partnerships are a common form of small business structure. The classic saying 'Two heads are better than one' is famous for good reason — it is true in many situations, including in the business world. Of course, finding the right 'mind' or partner is crucial.

the business are regarded as the same; that is, there is no separate legal entity. Consequently, the partners in a business are also subject to unlimited liability and so may be personally responsible for the debts of the business.

A partnership can be made verbally or in writing or by implication; that is, if two people set up a business together *without* a legally binding partnership agreement. A written partnership agreement is not compulsory, but it is certainly worthwhile in case disputes arise.

A partnership agreement usually has a standard set of contents (see the BizFact at left). The size and operations of the partnership are subject to specific requirements under the Partnership Act 1982 (NSW).

Limited partnerships were introduced to allow one or more partners to contribute financially to the business but take no part in the running of the partnership. In this case, the partner is referred to as a silent or sleeping partner. The main reason for their investment is to add more capital or finance to an existing partnership.

There are a number of advantages and disadvantages of a partnership (see figure 2.16).

BizFACT

A partnership agreement contains many points, including:

- *names and addresses of partners*
- *how long the partnership will exist*
- *the amount of money that each partner contributes*
- *how the profits and losses will be shared*
- *the duties of each partner*
- *limitations on the authority of the partners*
- *how the partnership may be dissolved*
- *arrangements regarding a partner wanting to leave and start up a business in competition*
- *methods of resolving disputes.*



FIGURE 2.16 The advantages and disadvantages of a partnership

on Resources

Weblink: Partnership

SUMMARY

- A partnership — an unincorporated business entity — is a business that is owned and operated by between two and 20 people and has unlimited liability.
- The partnership can be made verbally or in writing or by implication.

EXERCISE 2.3 REVISION

1 **Identify** the four main legal structures of privately owned businesses.
2 **Distinguish** between an incorporated and unincorporated business.
3 **Why** are unincorporated businesses the most common form of legal business structure?
4 (a) **Identify** three examples of businesses that might suitably operate as sole traders.
(b) **Explain** why for each case.
5 Using a telephone directory, **identify** five examples of:
(a) sole traders that would not have to register their name
(b) businesses that would have to register their name.
6 **Define** the term 'unlimited liability'.
7 'The advantages of being a sole trader outweigh the disadvantages'. **Assess** the accuracy of this statement.
8 **Distinguish** between a partnership and a sole trader.

9 **Identify** what you consider to be the two main advantages for a partnership. **Justify** your selection.

10 **Outline** the main purpose of a partnership agreement.

11 In pairs, imagine that you and your friend have decided to go into business together. Your business will specialise in designing home pages on the internet. Decide on a business name and then **create** a brief partnership agreement. Refer to the BizFact (page 36) for ideas.

12 The Australian Securities and Investments Commission (ASIC) provides a range of regularly updated information about the legal requirements of business names. Go to the **Australian Securities and Investments Commission (ASIC)** website and find information to answer the following questions.
(a) **Outline** the purpose of a business name.
(b) **Clarify** whether registering a business name gives you ownership of that name.
(c) **Describe** the process involved in selecting a business name.

on Resources

Weblink: Australian Securities and Investments Commission (ASIC)

EXERCISE 2.3 EXTENSION

1 (a) **Explain** why limited partnerships were introduced into some states of Australia.
(b) **Examine** the regulations that apply to limited partnerships.

2 Suppose you are a part-time employee working for a sole trader. The owner has offered you a 35 per cent partnership and you are going to accept. **Create** a list of questions you should ask the owner before you sign the partnership agreement.

3 Arrange to interview a partner of a local business. **Investigate** the following topics.
(a) The number of people in the partnership
(b) The advantages of the partnership
(c) Contents of the partnership agreement
(d) A brief history of the business.

4 'An effective partnership is one in which the partners always agree on all matters related to the business.' **Assess** the accuracy of this statement.

2.6 Types of companies

All companies are incorporated enterprises or have gone through the process of **incorporation**. This means that the company has become a separate legal entity from its owners (shareholders). The idea of a separate legal entity is referred to as the 'veil of incorporation'. This separate legal entity means that the company can sue and be sued; it can lease, sell or own property; and it has perpetual succession (this means it will continue to exist even when the owners change).

The process of incorporation is governed by the Commonwealth *Corporations Act 2001*, and is administered by the Australian Securities and Investments Commission (ASIC). For a business to become incorporated, a company name must be registered with ASIC, who will issue a certificate of incorporation and an Australian Company Number (ACN). Directors must be appointed to run the company on behalf of the owners. Once incorporated, the company has a separate legal entity to its owners, who are known as shareholders (referred to in the Corporations Act as 'members'). Incorporation also brings to the shareholders the benefits of limited liability.

BizWORD

Incorporation *is the process that companies go through to become incorporated, i.e. to become a registered company and a separate legal entity.*

2.6.1 Limited liability

The Limited Liability Act was passed by the British Parliament in 1855. This Act was necessary for the expansion of companies because it offered a degree of protection to shareholders.

In **limited liability** companies, the most money a shareholder can lose is the amount they paid for their shares. Therefore, if the company goes into liquidation, the shareholders cannot be forced to sell their personal assets to pay for the debts

BizWORD

Limited liability *is a feature of corporate ownership that limits each owner's financial liability to the amount of money he or she has paid for the business's shares.*

BizFACT

If directors make false and misleading statements or omissions in a prospectus, if they fail to appoint a company secretary or if they recklessly borrow money knowing that the debts probably will not be repaid, then the protection offered by the company in being a separate legal entity will not cover the directors. Directors accused of such unlawful behaviour may face common law suits and criminal charges.

of the business. This same protection does not extend to the directors of a company, as they have an obligation to ensure the company obeys the law and acts in the interests of the shareholders (see BizFact at left).

As well, financial institutions often ask directors to give personal guarantees for some business loans. Under some circumstances, therefore, directors can be forced to sell their personal assets to help pay for the debts of the business. To offset this risk, companies can insure against such an event.

The letters 'Ltd' signify that the business is a company that offers limited liability. A company can be organised as either a proprietary (private) or public company.

There are a number of advantages and disadvantages to the company form of business ownership as outlined in figure 2.17.

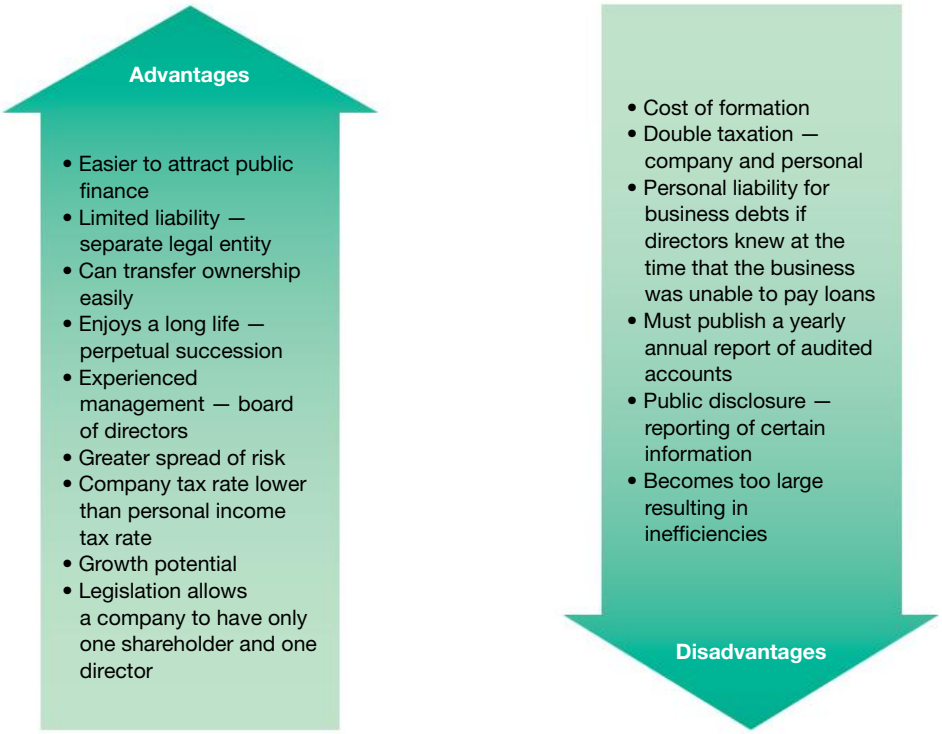


FIGURE 2.17 The advantages and disadvantages of a company

2.6.2 Proprietary (private) companies

BizWORD

A **proprietary (private) company** *is an incorporated business and usually has between two and 50 private shareholders.*

A **proprietary (private) company** is the most common type of company structure in Australia, and usually has between two and 50 private shareholders. Private companies often tend to be small to medium-sized, family-owned businesses.

Shares in a proprietary company are only offered to those people the business wishes to have as part-owners. Shareholders can only sell their shares to people approved of by the other directors. This is why such a company is called a 'private' company. It is not listed on, and its shares are not sold through a stock exchange.

A private company must have the words 'proprietary limited', abbreviated to 'Pty Ltd', after its name. The main advantage of a private company is that shareholders have limited liability protection.

BizFACT

It is possible for a private company to have a single director who is also the sole shareholder of the company.

Sometimes, the decision is taken to close a business. However, closing a proprietary company is much more complex than closing a sole trader business or partnership. All shareholders of the company must agree to the company being wound up. A liquidator will manage the process of selling the company's assets, paying its debts and distributing funds from the asset sales among the shareholders.



FIGURE 2.18 Visy is Australia's largest private company by revenue. In 2016, the company made $5.7 billion. Anthony Pratt, the owner, has no intention to get even bigger by listing on the share market.

2.6.3 Public companies

The shares for public companies are listed on the Australian Securities Exchange, and the general public may buy and sell shares in those companies.



FIGURE 2.19 The top five public companies in Australia in relation to total revenue in 2016 were Wesfarmers, Woolworths, Commonwealth Bank of Australia, Westpac Banking Corporation and NAB.

Whereas private companies tend to be small or medium-sized businesses, most public companies are large in size and market a large range of products — for example, Woolworths, Telstra, BHP and Westfield.

BizFACT

More than 2200 public companies are listed on the Australian Securities Exchange. The share price for each company changes according to demand and supply. If a company is considered a 'good buy', its share price is likely to rise.

A public company has:

- at least one shareholder, with no maximum number
- no restrictions on the transfer of shares or raising money from the public by offering shares
- to issue a prospectus when selling its shares for the first time
- a minimum requirement of three directors (two must live in Australia)
- the word 'Limited' or 'Ltd' in its name
- to publish its audited financial accounts each year, its annual report.

SNAPSHOT



'What structure is best?'

Selecting the most appropriate legal structure

One of the first and most important decisions an owner has to make when starting a new business is the type of legal structure. The answer to the question 'What structure is best?' will depend on the unique needs of the business, as well as the individual circumstances of each business owner. There is no one structure that is better than the others.

The decision should not be entered into lightly and it's important for business owners to seek professional advice from accountants, solicitors or financial advisers when making this decision. It's also important for business owners to keep in mind that they can change structure as their business grows or their circumstances change.

The type of legal structure will depend on the following factors:

1. *Legal liability*: The choice of structure will have important implications on the owner's potential legal liability. Therefore, the owner needs to consider whether their business lends itself to potential liability and, if so, how much they want to be insulated from this. If an owner cannot afford the risk of liability and wants to ensure their personal assets are protected, then a sole trader or partnership may not be the best option.
2. *Tax implications*: The legal structure chosen will have a significant effect on the amount of tax paid and the types of tax that must be paid. There are many more tax options available to companies; however, a disadvantage is that there is double taxation, i.e. income is taxed at both the corporate and personal level.
3. *Cost and complexity of formation*: Each legal structure has different set-up procedures and costs. For example, a sole trader is the simplest to set up and requires few reporting and administrative requirements, whereas a company must be established by a solicitor or accountant and is more expensive to set up. In addition, there are high costs associated with record-keeping and paperwork, as well as the costs involved in incorporation. Taking care of administrative requirements also takes up a lot of the owner's time and therefore creates additional costs for the business.
4. *Control*: Another important factor to consider is the level of control the owner wishes to have over the business. For instance, if the owner wants to have complete control, then being a sole trader would be the most appropriate structure.
5. *Future needs*: Owners also need to consider what they want to happen to the business when they're no longer around to run it. If they wish for the business to be terminated when they choose, then becoming a sole trader would be most appropriate. A sole trader or partnership may dissolve upon the death of its owners, whereas a company can be easily distributed to someone else and will continue to exist.

The table on the page opposite is a summary comparing the benefits of each structure.

	Sole trader	Partnership	Private company	Public company
Is the structure difficult to set up?	No	Somewhat	Yes	Yes
Is it expensive to set up?	No	No	Yes	Yes
Is it easy to raise funds?	No	Somewhat	Yes	Yes
Will the owner be personally responsible for the business's debts?	Yes	Yes	Not likely	Not likely
Does the owner retain complete control?	Yes	No	No	No
Are there complex reporting and administrative requirements?	No	No	Yes	Yes
Does the owner get to keep all the profits?	Yes	No	No	No
Can the legal structure be changed easily in future?	Yes	No	No	No
Does the business dissolve if there is a change in ownership?	Yes	Yes	No	No

SNAPSHOT QUESTIONS

1. **Outline** the factors that should be considered when selecting the most appropriate legal structure.
2. **Explain** which factor you believe is the most critical to consider when making this decision.
3. Imagine you were about to start your own business. **Identify** which legal structure you would choose and **justify** your decision.

on Resources

Weblink: Australian Securities Exchange

2.6.4 Government enterprise

Government enterprises are government-owned and operated. (They are also known as government business enterprises — GBEs.) Businesses operating in the public sector are the least common type of business. In 2015, the ABS estimated that there were only 500 public sector businesses actively trading goods and services. Although only small in number, they are typically large, and include some of the largest employers of people in Australia. GBEs are owned and operated by all levels of government: federal, state and local. Examples include Sydney Trains, Essential Energy, Defence Housing Australia, Sydney Water and Australia Post. They are often referred to as public sector businesses and provide essential community services such as health, education, roads and welfare.

Government business enterprises are established by an Act of Parliament to carry out a function specified in detail in that Act. The Act defines the GBE's powers and functions. The government either wholly or partially owns GBEs.

Beginning in the early 1980s, a wave of **privatisation** — the selling of government controlled businesses to private investors — began to take place in most industrialised economies. Australia followed this trend. During the 1990s, the federal government privatised a number of public sector businesses including:

- AUSSAT — domestic satellite operator (now called Optus)
- Qantas — international airline carrier
- Commonwealth Bank — financial services
- Telstra — telecommunications.

BizWORD

Government enterprises *are government-owned and operated businesses.*

BizWORD

Privatisation *is the process of transferring the ownership of a government business to the private sector.*

BizFACT

Australia Post is also a government business enterprise as the Commonwealth Government of Australia is its sole shareholder. As a GBE, it operates in the public sector, but it also operates in the transport, postal and warehousing industries. It is the oldest surviving GBE in Australia.

Due to the process of privatisation, these organisations changed their legal structure from GBE to public company. The rationale behind this practice is that economic efficiency is increased by transferring enterprises away from the public sector to the private sector. It is argued by some that privately owned and organised business enterprises will be more efficient and profitable than GBEs.





FIGURE 2.20 Over the past 20 years, there has been a worldwide trend to privatise GBEs. This process is known as privatisation. During the 1990s, the Australian Government privatised a number of public sector businesses, including Telstra, Qantas and the Commonwealth Bank.

SNAPSHOT



'As a government business enterprise, NBN is wholly owned by the Federal Government.'

Case study: NBN Co Limited — a government business enterprise

Many of Australia's businesses are household names. You may have heard of the National Broadband Network in the media. What you may not know is that NBN Co Limited (nbn) is a government business enterprise, i.e. it was established by the government. It was created in 2009 to design, build and operate Australia's new high-speed, wholesale local access broadband network, which will enable advanced digital services to be provided to Australians.

As a government business enterprise, nbn is wholly owned by the Federal Government. Since establishment, the Government has presented nbn's mandate and objectives through a Statement of Expectations, which is amended from time to time.

Currently, nbn employs over 3000 people and they have estimated that thousands of local jobs will be created as they continue to build the $38 billion network. nbn's key objective is to connect Australia and bridge the digital divide by ensuring all Australians have access to fast broadband as soon as possible, at affordable prices, and at the lowest cost.

The National Broadband Network is the largest infrastructure project in Australia's history to date. It has to be carefully designed and executed to ensure it delivers maximum value to customers. When the National Broadband Network is finally completed, it will allow people and businesses to access high-speed broadband services all across Australia.

SNAPSHOT QUESTIONS

1. **Describe** the legal structure of nbn.
2. **How** will nbn benefit Australians in the future?
3. **Explain** the benefits of nbn's legal structure.

on Resources

Weblink: NBN Co Limited

SUMMARY

- All companies are incorporated enterprises.
- In limited liability companies, the most money a shareholder can lose is the amount they paid for their shares.
- A proprietary (private) company usually has fewer than 50 shareholders and must have the words 'proprietary limited' (Pty Ltd) after its name.

- The shares for a public company are listed on the Australian Securities Exchange.
- A public company must have the word 'limited' or 'Ltd' in its name.
- Government enterprises are government-owned and operated and provide essential community services.
- Due to privatisation some government enterprises have become public companies.

EXERCISE 2.4 REVISION

1 **Explain** the legal steps required to incorporate a business.

2 **Outline** why you think companies need to have perpetual succession.

3 **Why** was the *Limited Liability Act* of 1855 important for company expansion?

4 **Recall** under what circumstances a director might be personally responsible for debts incurred by a company.

5 **Why** was new legislation introduced to penalise company directors who made misleading statements about the business's ability to repay its debts?

6 **Examine** figure 2.17 (page 38). **Identify** what you believe to be the three main advantages and the three main disadvantages of a company form of business ownership. **Explain** why you chose each one.

7 **Construct** a concept map highlighting the main features of a proprietary company form of business structure.

8 **Construct** another concept map highlighting the main features of a public company form of business structure.

9 **Outline** the ways a private company is 'private' and a public company is 'public'.

10 **Recall** the main role of government enterprises.

11 You are planning to establish the following types of businesses. **Justify** what form of business ownership you would prefer.
(a) a bicycle shop that will offer professional and personal advice
(b) a cattle stud specialising in a large-scale breeding program
(c) a national retailer that would require $467 million to establish.

12 **Identify** the most appropriate terms from the list to complete the following sentences.

public	minimum	stock exchange
sole trader	Ltd	twenty
formal	liability	limited
share	Proprietary Limited	private
unlimited	personal	
Pty Ltd	shares	

A business entity with one owner is called a _____. This person faces _____ liability, which means the owner can be forced to sell his or her _____ assets to pay for the debts of the business.

Partnerships normally consist of between two and _____ partners. Partners _____ the profits and losses and usually operate under a _____ agreement. Partnerships have unlimited _____.

There are two types of companies, private and _____. A _____ company usually has between two and 50 private shareholders. A private company has the words _____, abbreviated to _____, after its name. Public companies are listed on the _____ and the general public may buy and sell _____ in them. These companies must have a _____ number of one shareholder and have the abbreviation _____ in their names. Companies have _____ liability.

13 In your notebook, draw up a table with four columns. At the top of each column put the headings Sole Trader, Partnership, Private Company and Public Company. From the list of businesses shown on the next page, **determine** the correct column for its particular legal structure/entity. The first one has been completed for you.

Sole trader	Partnership	Private company	Public company
Jacinta's Newsagency			
Fairfax Limited M & M Communications Tip Top Bakeries Pty Ltd Paul Banwell Motors		Ozemail Limited David Tyler and Sons Con Chipprio Plumber Tynan Motors Pty Ltd	Jacinta's Newsagency Newcrest Mining Ltd Southcorp Ltd R & R Cook Antiques Pty Ltd

EXERCISE 2.4 EXTENSION

1. Select a public company from the share page of a newspaper or the internet. Purchase a 'virtual' parcel of 5000 shares in this company and plot the price movements over a two-month period. **Evaluate** the performance of your share parcel over this period.
2. Arrange to interview the owner of a local private company. **Create** a report outlining the information listed below.
   (a) The full name of the business
   (b) A brief history of the business
   (c) The business's main activity
   (d) Why the owner decided to incorporate
   (e) The expenses involved in setting up and operating a private company
   (f) The main problems involved in operating the business
   (g) The long-term plans the owner has for the business
   (h) What changes the owner would like to make to the organisation and operation of the business.
3. A friend has decided to establish a new restaurant. She asks you to advise her on the most appropriate legal structure.
   (a) **Construct** a list of questions that you would ask her.
   (b) **Recommend** the most appropriate legal structure suitable to your friend's situation and **justify** your recommendation.
4. In small groups, **investigate** the arguments for and against privatisation. Present your arguments to the rest of the class. **Compare** the group's answers.

2.7 Factors influencing choice of legal structure

BizFACT

The legal structure finally selected is, however, just the beginning. The structure should be reviewed as the business expands and develops, as the business environment evolves and as new laws are passed.

One of the most difficult decisions a business owner must make is what type of legal structure to select. This will depend on a number of particular circumstances influencing the business at certain times. These factors will change as the business expands. Therefore, the legal structure may need to be altered to reflect these changing circumstances.

Of all the factors that influence the business owner when deciding upon the most appropriate legal structure, the three most important are the:

1. size of the business
2. ownership
3. finances.

In reality, these three factors will all be interrelated and act together in influencing the choice made by the business owner.

2.7.1 Size of the business

As sales increase and the business operations grow to meet this higher level of customer demand, the business owner may need to select a more appropriate legal structure. Therefore, some broad generalisations can be made concerning the relationship between the size of a business and the most appropriate legal structure.

Most businesses begin their life as small or micro business enterprises. Therefore, the legal structure that is most suitable at this stage would be either a sole trader or partnership. If sales continue to increase, and the business keeps on growing, then further expansion will be needed and the business becomes a medium-sized one. The business will need to purchase new plant and equipment, which requires the injection of more money. Therefore, a partnership or private company may be formed with the new partners or private shareholders bringing with them extra finance, skills and expertise. If expansion is rapid, then the owners may wish to seek the protection of limited liability, in which case the private company legal structure will be chosen.

As the business continues to grow, it now becomes a large national or multinational corporation.

To finance this level of expansion, it will be necessary to draw from a large pool of available finances. The business will now decide to raise this money from a sharemarket float. A **float** is the raising of capital in a company through the sale of shares to the public.

A **prospectus** is issued (see figure 2.21), the business is listed on the Stock Exchange and shares are offered for sale. Also, an established public company can raise additional money from existing shareholders.

Of course, there is no rigid formula as to what legal structure best suits a particular size of business. Some businesses may establish themselves as public companies from the beginning, while others remain a private company even when the business has reached an international level. Each business owner will make a personal decision that best suits the conditions at the time, his or her own personal preferences and the overall business environment.

BizWORD

*A **float** is the raising of capital in a company through the sale of shares to the public.*

*A **prospectus** is a document giving details of a company and inviting the public to buy shares in it.*

2.7.2 Ownership

If a business owner wishes to have complete control and ownership of a business, then becoming a sole trader is the only realistic option. On the other hand, if the owner wishes to share the ownership with other people, then a partnership is the ideal legal structure. Of course, a private company would also allow the owner to maintain a high degree of control and it would also offer the protection of limited liability. This is because a private company structure provides the owner with a large degree of control over who can become a shareholder of the business. As well, in most cases the maximum number of shareholders is restricted to 50.

Once a company floats and sells shares to the public, ownership will be divided among thousands of small, individual shareholders and a few institutional shareholders. The degree of ownership, then, is directly related to the number of shares owned: more shares, more ownership. Therefore, if the original owner/s wished to retain ownership and control of the business, they would need to hold more than 50 per cent of all the shares sold.



FIGURE 2.21 In March 2017, Snap, the maker of Snapchat, went public. The prospectus, filed in February, was the first opportunity for potential investors and outsiders to get a closer look into the company that's known for, among other things, its culture of secrecy. Their shares were initially priced at US$17, but by the end of their first day of trading, the share price jumped 44 per cent to $24.48, enabling the company to raise more than US$28 billion.

2.7.3 Finance

As mentioned earlier, when a business expands it will require injections of finance. This money will be used to purchase new equipment, undertake research and development, hire more staff, exploit new markets and open new outlets.



FIGURE 2.22 It can be hard for sole traders to get finance. This is because financial institutions usually consider sole traders to be higher risk, especially if their business is new and they don't have a strong track record yet. Finance companies may also want some collateral to secure the loan.

Sole traders and partnerships, because of their exposure to risk (unlimited liability) with few business assets, can sometimes find it difficult to obtain adequate finance, especially for research and development (R&D). Traditional sources of finance, especially banks, perceive this type of finance request as high risk. One possible source of finance for R&D is venture capital. **Venture capital** is money that is invested in small and sometimes struggling businesses that have the potential to become very successful. The investors take an equity position in the business (own part of it) and provide supplementary finance.

BizWORD

Venture capital *is money that is invested in small and sometimes struggling businesses that have the potential to become very successful.*

To overcome the difficulty of raising finance from banks or financial institutions, the business owner may decide to sell shares in the business. Therefore, the business will be incorporated and either a proprietary or public company formed. Of course, this legal structure does not guarantee the necessary finance will be obtained. Some floats fail to generate interest and are undersubscribed; that is, not all the shares are sold. However, because of the protection of limited liability offered through incorporation, individuals are more often prepared to invest in this business structure.

SUMMARY

- The most appropriate legal structure to select will depend on many variables including size, ownership and finance.
- As a business expands, it normally moves from an unincorporated structure to an incorporated structure.

EXERCISE 2.5 REVISION

1. **Explain** the general relationship between the size of a business and its legal structure.
2. **Recall** the purpose of a sharemarket float.
3. **Define** the term 'prospectus'.
4. **Outline** the reasons a sole trader would be motivated to alter the legal structure to become either a partnership or public company.
5. Assume you wish to establish a landscaping business. **Determine** which legal structure/s you would choose if you wanted to:
   (a) retain complete control
   (b) share ownership with no more than 20 people
   (c) share ownership with no more than 50 people.
   Give reasons for your answers.
6. **Recall** the percentage of all the shares sold that a person needs to hold in order to own and control a company.
7. **How** will a business's legal structure change as it requires greater injections of finance?
8. **Investigate** the possible advantages and disadvantages of venture capital as a source of finance. Share your answer with the rest of the class.
9. **Explain** why the legal structure a business starts out with may not suit its needs as it grows.

EXERCISE 2.5 EXTENSION

1. 'The majority of small individual shareholders have virtually no say in the running of a public company. The institutional shareholders have the game to themselves.' **Evaluate** the accuracy of this statement.
2. **Construct** a list of 20 businesses that opened around two or three years ago in your local area.
   (a) Place a cross next to the name of each business that is no longer in operation.
   (b) In your opinion, **propose** some reasons these businesses failed.
   (c) **Propose** some reasons for the success of the other businesses.
   (d) Arrange to interview a person whose business succeeded. Have them explain to you the reasons for the business success.
   (e) **Compare** the reasons you gave with those provided by the business owner.
3. Go to the **ASX** website to find a new company floating on the ASX. Follow the link to the company's website. **Investigate** the history of the company and write a brief report that **examines** the likely reasons for its decision to change its legal structure and become a public company.

On Resources

- **Weblink:** ASX
- **Digital doc:** Chapter summary (doc-26094)
- **Interactivity:** Chapter crossword (int-7213)
- **Interactivity:** Multiple choice quiz (int-7214)

CHAPTER 3

Influences in the business environment

OVERVIEW

3.1 Introduction
3.2 Business environment
3.3 External influences
3.4 Internal influences on business
3.5 Stakeholders

3.1 Introduction

Your school is part of your learning environment: the surrounding conditions in which you learn. You have some degree of control over the factors that make up part of your learning environment, such as the subjects you choose to study, extra-curricular activities you participate in, and your interactions with teachers and other students. There are many other factors within your learning environment, however, over which you have little control but that have a direct influence on your learning. This includes such factors as the syllabus subject matter, the introduction of new technology and the changes in government education policies. As a student, you are part of an ever-changing and complex learning environment within which you must manage your education.



FIGURE 3.1 Your learning environment is made up of factors over which you have some control and other factors over which you have little control.

3.2 Business environment

No business — similar to students — operates in isolation. Businesses also have to deal with an ever-changing environment in which they operate. What happens in the larger business environment may have a direct influence on many other

firms. If interest rates increase, for example, then some businesses may not be able to afford to purchase new equipment. Alternatively, reduced competition in the market may result in some businesses increasing their individual market share and profitability. All business decisions about how and what to produce are affected by the environment in which the business operates.

Successful business managers have a good understanding of the environment in which the business operates. This allows them to respond positively to changes that take place and prepare for the impact such changes will have on their business operations.

The **business environment** refers to the surrounding conditions in which the business operates, and can be divided into two broad categories: external and internal (see figure 3.2).

- The **external environment** includes those factors over which the business has little control, such as government policy, technology, economic conditions and social attitudes.
- The **internal environment** includes those factors over which the business has some degree of control, such as products, location, resources, management and business culture.

BizWORD

The **business environment** *refers to the surrounding conditions in which the business operates. It can be divided into two broad categories: external and internal.*

The **external environment** *includes those factors over which the business has very little control.*

The **internal environment** *includes those factors over which the business has some degree of control.*

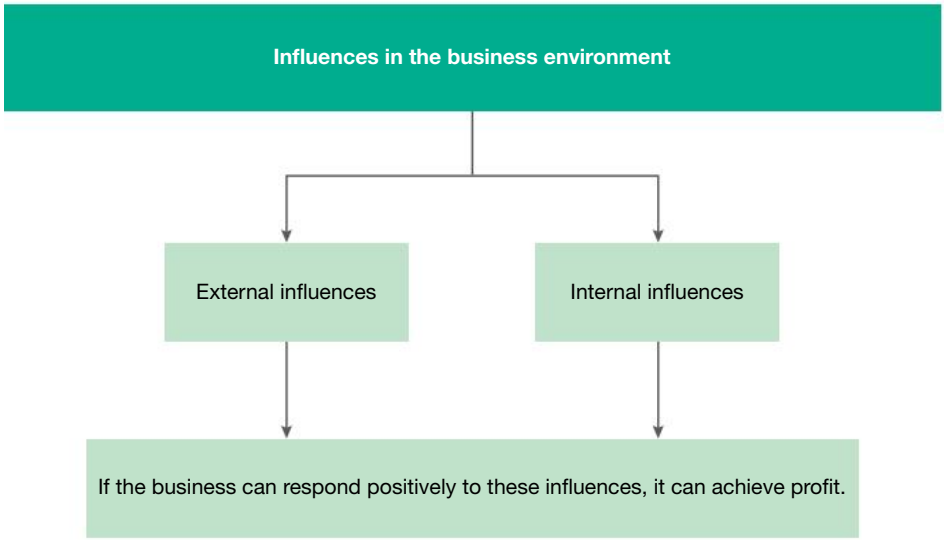


FIGURE 3.2 Influences on business

The factors that make up the business environment are not constant and certain. They are continually undergoing change, and a business must keep 'in tune' with the changes and adapt its operations accordingly.

3.3 External influences

Changes in the external environment make it necessary for managers to make adjustments to business operations. This may include the introduction of new government regulations that require the business to make adjustments; for example, all businesses will need to respond to some type of carbon reduction scheme that will result in organisations paying for the carbon pollution they generate in order to reduce carbon pollution and eventually create a more sustainable economy. Figure 3.3 outlines the main external influences on a business.

on Resources

eLesson: Dinte Group (eles-0834)

3.3.1 Economic influences

Imagine your local shopping centre to be a small-scale representation of the Australian economy. Now, imagine what would happen to the businesses within the shopping centre if all their customers decided to shop at another centre for a day.

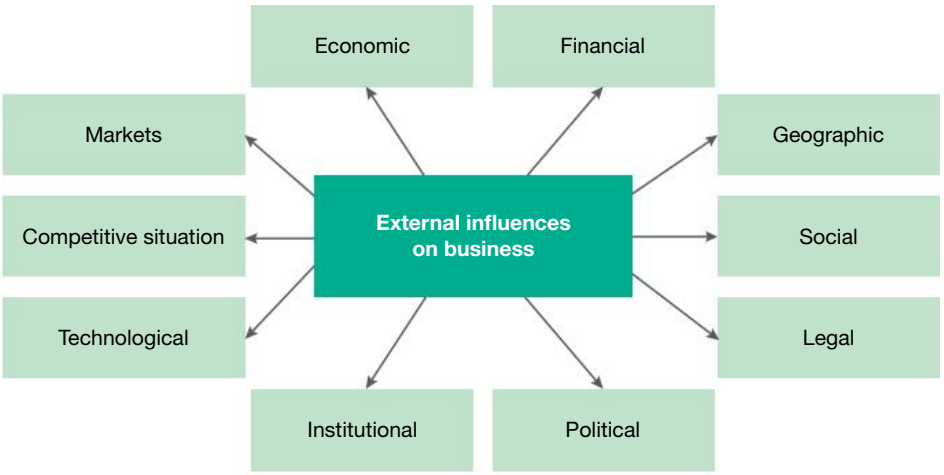


FIGURE 3.3 External influences on business

Economic disaster! If this situation continued for a month then the centre's businesses would close, employees would be laid off, and landlords and suppliers would not be paid. Eventually, as the 'economy' plunged into a recession, business owners would lose confidence in the economy's future. However, at the rival shopping centre, new businesses would open, many new jobs would be created, landlords and suppliers would gain new customers, and the confidence of the local business owners would soar. The 'economy' of this shopping centre would boom.

Although such an extreme situation would not happen in reality, the Australian economy does experience **economic cycles** of 'booms' and 'busts'. These periods of high and low economic activity are referred to as the business cycle. After a period of prosperity, business activity gradually slows until a recession or depression is reached. Eventually, business picks up again until prosperity is restored. This completes the cycle. These cycles are a basic feature of our economic system.

Economic forces have an enormous impact on both business and customers. They influence a business's capacity to compete and customer's willingness and ability to spend. The following figure shows the impact of each phase of the economic cycle on a business's performance.

BizWORD

Economic cycles *(or business cycles) are the periods of growth ('boom') and recession ('bust') that occur as a result of fluctuations in the general level of economic activity.*

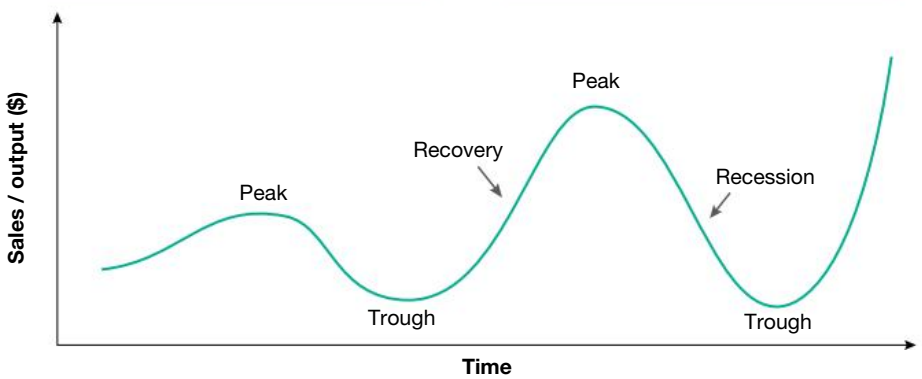
BizFACT

A commonly cited reason for small business failure is adverse economic conditions. Some statistical research on reasons why small businesses fail revealed that 12.4 per cent of small businesses fail due to inflation and economic conditions.

Recovery — key features
- Increasing consumer spending
- Business expectations increasingly optimistic
- Increasing business investment
- Sales and profits rising
- Unemployment falling

Recession — key features
- Decreasing consumer spending
- Business expectations increasingly pessimistic
- Decreasing business investment
- Sales and profits falling
- Unemployment rising

Peaks — key features
- Wages and salaries at high levels
- Business operating at full capacity
- Sales and profits at highest levels
- Low level of unemployment
- Inflation may increase
- An increase in consumer spending



Troughs — key features
- Wages and salaries at low levels
- Business operating at below full capacity
- Sales and profits at lowest levels
- Consumer spending at lowest levels
- High level of unemployment
- Inflation may remain stable or fall

FIGURE 3.4 The economic or business cycle

Information on economic growth, inflation trends, average weekly earnings, consumer confidence, interest rates, consumer spending and unemployment provide businesses with insight into economic trends. This information on the level of economic activity allows businesses to predict possible threats to, and opportunities for, business activity.

No economic system works perfectly all the time under all conditions, and the Australian economy is no exception. The level of economic activity does not remain at a constant level; it fluctuates (moves up and down) over time. In other words, total production, incomes, spending and employment rise and fall.

The state of the economy has a great impact on business. The policies implemented by the government are aimed at keeping the economy growing steadily, without putting pressure on inflation (prices) and wages. The economy is also affected by overseas trends — changes in trade, investment and currency levels all affect Australia's level of economic activity. The continued growth and development of China's economy has benefited Australian businesses in relation to exports. Many businesses are supplying not just raw materials such as coal, but finished products and, to a greater extent, quaternary services such as education and training.

When economic problems start to appear, we as consumers become more cautious with the way we spend our money and our overall confidence begins to fall (see figure 3.5). The reduced spending has an impact on business owners — they find profits falling and cost cutting must occur if they are to survive. Unfortunately, this cost cutting can be in the form of retrenching workers; therefore, the economy falls further into recession. Alternatively, when there is evidence of a growing economy, confidence returns. The consumer is more willing to purchase consumer or luxury goods, which in turn sees spending levels rise and business profits improve.

BizFACT

In 2017, household spending grew faster than household income, which propelled economic growth to 0.8 per cent in June. This led to a 4.6 per cent decline in household saving. Wages and salaries grew just 2.1 per cent over the year, an increase driven by a jump in the number of hours worked rather than pay increases.

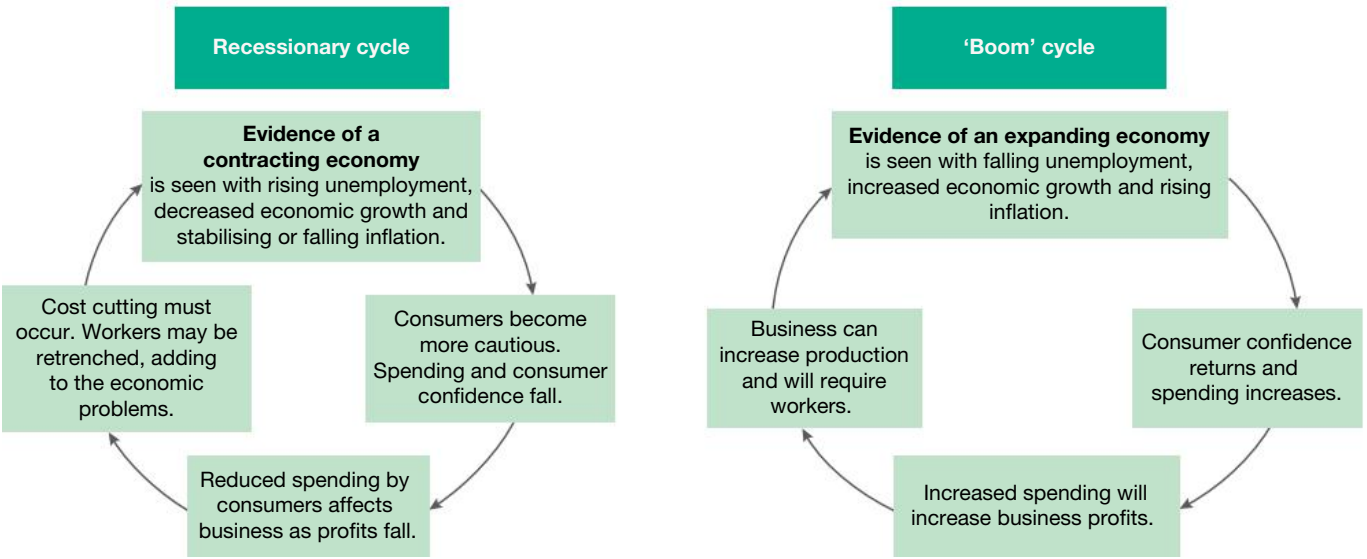


FIGURE 3.5 The recessionary and 'boom' cycles. The government uses its economic policies to stabilise the economy and reduce the fluctuations in the business cycle. It can do this by using monetary and fiscal policies.

One important factor to consider in terms of economic cycles is that not all businesses experience a downturn in revenue and sales during a recession; nor do they necessarily experience an upswing in trade during a 'boom' period. The businesses most susceptible to the 'swings' are those selling consumer or luxury goods, as consumers will cut back on these when they reduce overall spending. Some businesses fare very well during a recession, for example 'bargain shops' or other clearance outlets.

SNAPSHOT



'… proactiveness, connectedness, adaptation, and access to "slack" … resources.'

Four qualities that support success in a bust period

A recent study of the resilience capabilities of 400 small to medium enterprises in Queensland identified several key capabilities that supported success in the bust period and beyond. These are proactiveness, connectedness, adaptation, and access to "slack" (or readily available) resources.

Proactive small firms that grow in the post-boom era are those that actively seek new product and service niches and reorient aspects of their business accordingly. They tend to be the first to initiate competitive actions such as introducing innovative products that are new to the industries they serve. They are quick to recognise new business opportunities based on rigorous marketplace analysis. They fully support new forays by reorganising business structures and investing in new capabilities.

Connected small firms actively cultivate and maintain business network partnerships. They are more likely to see their income increase during lean economic times because they curate and maintain diverse networks to mitigate against market demand fluctuations. By directly engaging with customers and suppliers, well-connected firms actively plan for potential market disruptions, proactively monitor the overall health of industry, and even conduct scenario planning exercises to test their assumptions in each of these areas.

Essentially, it appears that robust external network connections provide the basis from which firms can see, anticipate and exploit market trends.

Adaptive businesses find workable solutions to new challenges and accommodate market disruptions by using existing resources in new ways and by quickly shifting things around to ensure that customers are never let down — no matter what.

Perhaps most important, businesses with slack resources are more hopeful to survive into the future. Active investment in good times in spare equipment, facilities and other production capacity, accruing finances and building and maintaining new staff that are not tied to the existing business, but rather are looking for new opportunities, is therefore crucial.

Source: Jerad A. Ford, John Steen & Martie-Louise Verreynne, *The Conversation*.

SNAPSHOT QUESTIONS

1. **Describe** the four capabilities that support business success in a bust period.
2. **Determine** which quality you believe is most important for a business to ensure survival in a bust period.

3.3.2 Financial influences

There have been enormous changes in global financial markets over the past 30 years.

Deregulation of Australia's financial system began in 1983 and it continues to undergo change. This has resulted in a more flexible, market-oriented approach across the financial sector. A substantial number of new banking products have emerged, aimed at the business sector. The process of financial deregulation has resulted in the opening up of the financial industry to greater competition.

A main source of finance for business is debt finance. Debt finance is significantly influenced by the level of interest rates. As interest rates increase, businesses will become more cautious in relation to taking on extra debt. On the other hand, as interest rates drop, then businesses will take on more debt.

Due to globalisation of the world's financial markets, it is no longer necessary for many large Australian businesses to use only domestic financial institutions for the raising of finance. For example, News Limited, the global media company, can access finance from worldwide sources.

Global financial markets themselves have undergone rapid change over the last decade. Developments in communications technology have enabled the phenomenon of global financial transactions. Global financial speculators may now easily make transactions spread across the globe.

BizWORD

Deregulation *is the removal of government regulation from industry, with the aim of increasing efficiency and improving competition.*

BizFACT

In April 2018, the Reserve Bank of Australia (RBA) left the cash rate on hold at a record low of 1.5 per cent for the eighteenth consecutive month, providing little indication of when it will allow interest rates to rise.

3.3.3 Geographic influences

Two major factors that have an enormous impact on business activity are Australia's geographic location within the Asia–Pacific region and the economic growth in a number of Asian nations, especially China. They provide challenging opportunities for business expansion, sales and profit.

Further changes that are likely to have a profound effect on business activity in Australia originate from changing demographic factors. Demography is the study of particular features of the population, including the size of the population, age, sex, income, cultural background and family size. Changes in any of these factors can lead to changes in demand levels and the nature of products and services.

A major demographic issue that has a considerable impact on businesses is changes in the age structure of our population. Commonly referred to as the 'greying' of the Australian population, baby-boomers — people born between 1946 and 1964 — are now reaching retirement age, meaning that there are more elderly people living in the community than ever before. This will cause some skill shortages in the workforce as well as an increase in demand for age-related services such as health and aged-care. Any change in population growth will also have major implications for Australian businesses, as research shows there is a clear link between population levels and economic growth.

The National Sustainability Council's report in 2013 predicts that the number of retirees will almost double over the next 20 years, straining taxpayer spending on pensions, health and aged care. They suggested increasing the retirement age to 70 as a way to make baby-boomers work longer, since they believe Australia won't have enough people working and paying taxes to support all the retirees and people on welfare. Another recommendation put forward to increase the participation rate of older workers was to support more flexible working conditions and encouragement or incentives for older workers.



Another important geographical influence is that of globalisation. We live in a global world, rather than a world limited by national borders. Consider the news and entertainment we receive from around the planet, the clothing and footwear brands being sold worldwide, the rapid telecommunications access to all parts of the globe, and the large number of products Australia buys and sells on the world market. The Earth is a global community whose individual members are linked through the mechanism of international trade: the buying and selling of goods and services between nations.

BizFACT

Between 1995 and 2016, the proportion of people aged 65 years and over increased from 11.9 per cent to 15 per cent of the population. This is expected to grow to 22 per cent by 2056. In addition, the proportion of people aged 85 years and over almost doubled from 1.1 per cent of the total population in 1995 to 2 per cent in 2015.

BizFACT

In the May 2009 Federal Budget, the Australian government announced that the age pension age would increase to 67 years of age from 2023. It will remain at 65 for anyone born before July 1952. The first shift upwards in Age Pension age will occur in 2017 when the eligibility age increases to 65.5 years, and then in six-month increments every two years, until it reaches the age of 67 in 2023.

FIGURE 3.6 Australia's ageing population will have a significant impact on businesses and the economy. For example, once people retire, their spending patterns change. Consequently, businesses need to market products to suit the changing preferences of their customers.

BizFACT

Globalisation has not been welcomed by everyone. Critics argue that the process results in a 'race to the bottom' in wages and conditions. This inevitably leads to exploitation of workers, especially in developing countries, and the loss of jobs in developed countries.



FIGURE 3.7 Harry's Café de Wheels is an iconic pie cart located on Cowper Wharf Road in Sydney. The café was founded in 1938 and there are now ten other carts operating in Sydney and Newcastle. The business recently expanded into China, with plans to build hundreds of pie carts across the country over the next 15 years. The owner, Michael Hannah, has worked with business partners in China to ensure that the sites and food are authentically Australian. The majority of ingredients are currently sourced in Australia and shipped monthly to China.

BizWORD

Globalisation *is the process that sees people, goods, money and ideas moving around the world faster and more cheaply than before.*

This process has been strengthened by the impact of **globalisation**: a process that sees people, goods, money and ideas moving around the world faster and more cheaply than before. Globalisation, assisted by the technological revolution in communications and computers, is radically altering the shape of world markets, as well as the nature of business and everyday life (see the following Snapshot).

SNAPSHOT



'Globalisation presents both threats and opportunities for business.'

The influence of globalisation on business

Globalisation is the process by which the world is becoming increasingly interconnected as a result of massively increased trade and cultural exchange. It involves reducing the barriers limiting free movement of business, trade, investment and labour across national borders. The process of globalisation has had a significant impact on businesses, some of which are summarised below.

- **Increased competition**: Globalisation has led to increased competition. Customers now have a multitude of choice in the market, therefore each business has to continuously improve its products and standards or create more value for customers in order to remain competitive.
- **Expanded markets**: Today, even small businesses can easily go global. The wide use of the internet and other technologies makes it possible for most businesses to access the global market and start selling products to other countries. As soon as a business has a website, it becomes visible to the world and this could lead to higher demand for its products. Globalisation can therefore help businesses grow bigger.
- **Greater customer expectations**: Consumers are now exposed to a much larger variety of goods and services, and this affects their expectations. Consumers are now very selective when it comes to factors such as quality, service and price. Businesses need to meet these needs, otherwise they will experience a decrease in sales as customers find cheaper or better quality products elsewhere.
- **Economies of scale**: By selling globally, businesses should be able to increase sales, which will result in an increase in production. These businesses will then be able to take advantage of economies of scale. When production

is increased, fixed costs can be spread more thinly over a greater volume of sales, allowing firms to lower their costs, improve efficiency and raise profitability. This makes them more competitive.

- **Location flexibility**: Businesses can take advantage of low-cost labour and other resource expenses and move their production or other facilities elsewhere to achieve savings. Cheaper resources contribute to cheaper costs, which in turn contributes to larger profits for the business.
- **Cheaper materials**: Globalisation enables businesses to seek out the cheapest materials and supplies from around the world, allowing them to be cost competitive. This is referred to as global sourcing. These cost reductions should lead to increased revenue for the business.
- **Diversification**: Globalisation spreads business risk. For instance, if the economy, government regulations or supply issues etc. in one country have a negative impact on a business, that business can still find success in other markets to offset the losses experienced. Globalisation provides businesses with some level of insulation from slumping performance in one region.
- **Access to better labour**: Global companies have access to a much greater pool of talent, which should lead to improved business performance.

Globalisation presents both threats and opportunities for business. Globalisation is not going away, therefore, businesses need to implement strategies to minimise the potential threats that emerge, as well as take advantage of the opportunities that arise from globalisation.

SNAPSHOT QUESTIONS

1. **Identify** the impacts of globalisation on business.
2. **Recommend** strategies businesses can implement in order to manage the impacts of globalisation.
3. **Determine** other impacts of globalisation that exist besides those mentioned.

3.3.4 Social influences

Rapid identification and response to changes in tastes, fashions and culture can lead to sales and profit opportunities, and business growth. Failure to respond to social changes can threaten business stability and viability.

Three social issues are leading to significant change or have the potential to influence major change in business practices. The first concerns a growing awareness of our vulnerable environment. Over the past decade, Australians have become aware of a number of practices that lead to deterioration in the environment. This awareness has led to a call for businesses to adopt environmentally sustainable practices. Environmental sustainability means that business operations should be shaped around practices that consume resources today without compromising access to those resources for future generations. Many businesses have put in place strategies to reduce and minimise waste, recycle and reduce their carbon footprint. Those businesses that are not socially and environmentally responsible can face a consumer backlash if customers find out. At the same time, many consumers will reward those businesses who are environmentally responsible by purchasing more of their products. In recent years, many companies are increasingly disclosing their environmental protection policies.

The second social issue that is leading to significant change is a growing desire for businesses to provide family friendly workplaces. There is a growing belief that businesses must support families, and the provision of better childcare options and more flexible hours are increasingly being considered by businesses. Conflict between work and family responsibilities is a key factor causing women to leave businesses and this high turnover is expensive for business. Consequently, businesses have been under pressure to implement family-friendly workplace practices that assist employees and, at the same time, reduce the associated costs to employers.

BizFACT

As more and more people select healthier food options, fresh and perishable foods like produce and deli-prepared items are booming and the organic goods sector has almost doubled. Packaged goods companies, on the other hand, are struggling to survive the shift.

BizFACT

In 2017, Woolworths and Coles announced plans to phase out single-use plastic bags over the next twelve months to prove they are committed to taking their environmental responsibilities seriously.

BizFACT

Recent analysis by the OECD found that among working Australian mothers aged 25–45 years, 45 per cent work part-time and four-fifths of those that work part-time cite family reasons for doing so. They also work very short hours on average—less than 20 a week. Australia's relatively high childcare costs are a major contributing factor to the high number of mothers who do not work.



FIGURE 3.8 The *Fair Work Act 2009* provided employees with a legal right to request flexible working arrangements. This request forms part of the National Employment Standards (NES). Certain employees have the right to make a request, e.g. a parent of a child who is of school age or younger, a carer, someone over 55 or someone experiencing violence from a member of their family. A request can only be refused on reasonable business grounds.

SNAPSHOT



'… the major benefit is in attracting and retaining staff …'

Small business gets flexible to retain quality workers

Small businesses that invest in paid parental leave and other work–life balance programs are more likely to retain quality employees, a survey has found.

Charles Sturt University's Stacey Jenkins looked at how 219 small and medium-sized enterprises across Australia tried to improve work–life balance for their employees.

The most common practices were flexi-time, which gives employees more control over which hours they work; additional paid parental leave; support benefits, and on-site care arrangements, such as dedicated breastfeeding areas.

'If the employers were offering these it could have positive impact, with employees being more likely to take fewer sick days,' Jenkins said.

She said the research showed how important paid parental leave schemes are in maintaining a high quality workforce.

'Without them, it poses a real difficulty in employees being able to meet the needs of their families but also being able to stay within the workforce,' she said.

'For employers, the major benefit is in attracting and retaining staff, especially for employers in non-metropolitan areas where there's a limited pool of qualified employees.'

The study found that all employees, not just those with families, could benefit from such programs.

'For younger workers or those who don't have children or caring responsibilities, there's still a need for them to manage their stress levels.'

Barbara Pocock, Director of the Centre for Work and Life at the University of South Australia, said increased flexibility is a growing trend for all businesses.

'Flexibility is certainly increasing and we know that many employers, including small businesses, understand that they have to respond to what their employees want in terms of work patterns,' she said.

'A lot of small businesses have invested in their employees, who know their business really well. They don't want to lose those people.'

'That's partly because of the changing nature of the workforce with one in two workers now being women,' she said. 'But it's also about making the best of the people who have experience and qualifications in the business that they're trying to grow.'

Stacey Jenkins' research has been submitted to the *International Journal of Human Resources* today.

Source: 'Small business gets flexible to retain quality workers', *The Conversation*.

SNAPSHOT QUESTIONS

1. **Identify** some of the ways in which businesses can help employees improve work–life balance.
2. **Discuss** the advantages and disadvantages for businesses of investing in work–life balance programs.

The third social issue that is leading to significant change is the growing belief that businesses must cater for workplace diversity. Employees will have different issues that may be related to gender, age, language, ethnicity, cultural background, disability, sexual orientation and religious belief. Businesses are required to effectively manage a diverse range of employees and cater for their specific needs. A business that becomes known as fair and equitable will also have a better chance of attracting and retaining staff. A diverse workforce could lead to increased morale, creativity and productivity, giving the business a competitive edge.



FIGURE 3.9 Businesses that embrace diversity are more innovative and open to change, since people from a wide range of backgrounds are able to bring different perspectives.

SUMMARY

- Business environment is influenced by both internal and external factors.
  - The external environment includes those factors over which the business has very little control.
  - The internal environment includes those factors over which the business has some degree of control.
- External influences on business include: economic, financial, social, legal, political, institutional, technological, competitive situation and changes in the market.
- Economic influences on a business relate directly to their economic environment, which is dependent on changes in economic growth. These changes are characterised by boom and recessionary periods in the economic cycle.
- Changes in the global and domestic financial markets will influence the cost of borrowing money and therefore directly affect the level of investment by a business.
- Three major geographical factors that affect business activity are:
  - Australia's geographic location within the Asia–Pacific region
  - changing demographic factors
  - the process of globalisation.
- Social influences, such as changes to fashion and culture, have the capacity to affect business sales and profits.
- Three social issues that have had a significant impact on business practices include the growing awareness of the environment, the growing desire for businesses to provide family-friendly workplaces and the growing belief that businesses must cater for workplace diversity.

BizFACT

In 2017, NAB conducted research exploring what matters most for Australian SMEs. Their research revealed that while 65 per cent of SMEs are confident Australia will continue to be a great place to operate a business, the burden of red tape and taxation is holding them back. Sixty-nine per cent cited that the pressure of complying with quarterly BAS and all the other day-to-day administrative and regulatory challenges is impeding their success.

3.3.5 Legal influences

Too much government interference! Too much red tape! Too many regulations! These are familiar cries from many business owners who face an increasing number of legal obligations in every aspect of their businesses. Today, small to medium

businesses face levels of regulation similar to those faced by large businesses. While most business owners are willing to comply with regulations, compliance is often time consuming and costly, and regulations can be confusing and contradictory.

Society expects business owners to abide by the laws of a country. Consequently, it is essential that they have a sound working knowledge of the laws that will affect their operations (so that they avoid penalties), and that they understand and accept the legal responsibilities they owe to all stakeholders. All levels of government impose legal responsibilities on businesses and these laws govern every aspect of a business's life.

In the past two decades, a large number of new statutes were introduced, which have had a major impact on business conduct. This legislation includes laws on taxation, industrial relations, work health and safety, equal employment opportunity, anti-discrimination and protection of the environment.

An area of law that has significantly altered business conduct is the *Competition and Consumer Act 2010* (Cwlth), which applies to virtually all businesses in Australia. It is administered by the Australian Competition and Consumer Commission (ACCC), which is an independent statutory authority. The ACCC operates nationally for the enforcement and administration of competition and consumer protection laws. A breach of any of the consumer protection provisions of the Competition and Consumer Act can result in the ACCC taking criminal proceedings against the business concerned. The Act allows the courts to impose penalties of up to $1.1 million for companies, and $220 000 for individuals who breach the Act.

on Resources

Weblink: Australian Competition and Consumer Commission



FIGURE 3.10 The ACCC took ticket reseller Viagogo to court in 2017 for breaching the Australian Consumer Law after receiving more than 400 complaints against the company in one year alone. The ACCC alleged the company misled consumers by making representations on their website that tickets to certain events were scarce and likely to run out soon. This created a sense of urgency, even though tickets were still available through other sources. The ACCC also alleged Viagogo inflated prices and did not disclose additional fees.

3.3.6 Political influences

Government policies have a considerable impact on the business environment (see figure 3.11). Major political change can lead to business uncertainty or business confidence. As governments at all levels in Australia regularly face elections, there is an element of politics in most major issues that affect the business environment.

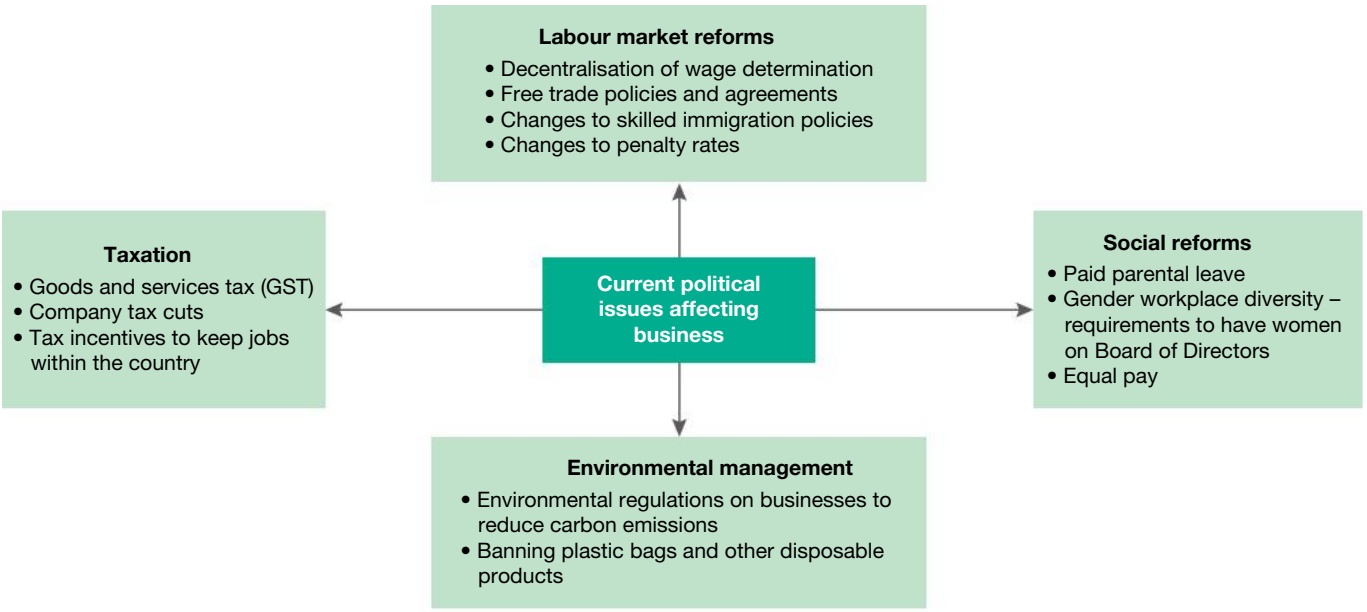


FIGURE 3.11 Current political issues affecting businesses

A political influence that is having an enormous impact on Australian business operations is the policy of free trade. Free trade policies mean that barriers to trade are removed. One such barrier to free trade is a tariff: a tax levied on imported goods. In recent years tariff rates have generally been lowered, meaning that some businesses have been unable to compete with the cheaper imported item and have gone out of business. Other firms have survived the removal of tariffs and compete well with similar imported products that are sold in the Australian marketplace.

3.3.7 Institutional influences

There are three main institutional influences on business, including government, regulatory bodies and other groups such as trade unions and employer associations.

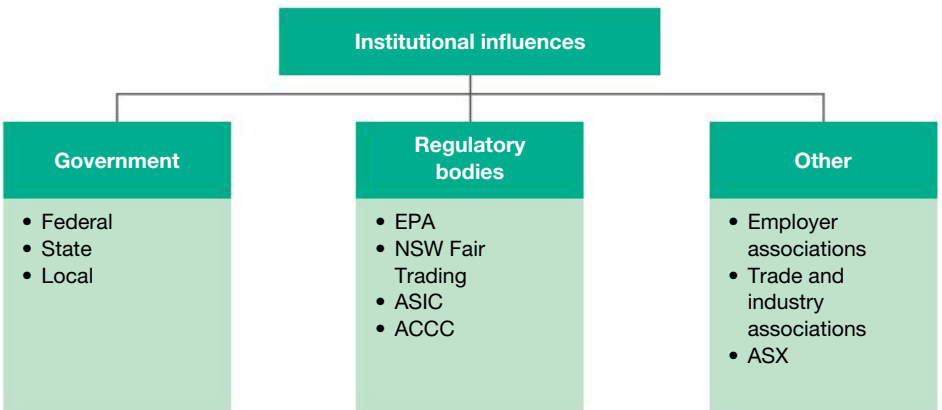


FIGURE 3.12 Institutional influences on business

Government

Australia has three levels of government: federal, state and local. Each level of government imposes a range of **regulations** on businesses to standardise and protect their dealings with consumers and competitors.

BizWORD

Regulations *are rules, laws or orders that businesses must follow.*

Federal government

Federal government obligations include:

- payment of taxes for employees (earning above the minimum taxable income level) and for businesses with company tax and GST
- provision of employee superannuation
- observance of customs regulations
- abiding by relevant legislation that would affect business operations.

State government

State government obligations include:

- provision of employee entitlements, including workers compensation, work health and safety (WHS) requirements, award rates of pay and entitlements
- payment of payroll taxes
- abiding by relevant state legislation (e.g. health, trade practices, employment)
- abiding by pollution controls.

Local government

Local governments (city, municipal and shire councils) have control over the following business activities:

- approving new development and alteration (to an existing building) applications
- fire regulations
- parking regulations (e.g. provision of parking by new businesses)
- size, location and shape of business signs.

FIGURE 3.13 Some business laws relating to the levels of government

on Resources

- **Weblink:** NSW Environment Protection Authority
- **Weblink:** NSW Fair Trading
- **Weblink:** ASIC
- **Weblink:** ACCC

Regulatory bodies

A regulatory body is one that is set up to monitor and review the actions of businesses and consumers in relation to certain issues (such as advertising) and the appropriate legislation. This is to ensure that businesses conduct themselves fairly in relation to the consumer, the community and other businesses. A number of regulatory bodies operate in New South Wales and Australia. They include:

- the NSW Environment Protection Authority
- NSW Fair Trading
- the Australian Securities and Investments Commission
- the Australian Competition and Consumer Commission.

The roles of these regulatory bodies are summarised in table 3.1.

BizFACT

In 2016, the EPA commenced prosecution action in the Land and Environment Court against waste transporter Dib Hanna for alleged illegal dumping offences. He was charged with eight repeat waste offences. Each charge carries a maximum penalty of $250 000 and/or two years' imprisonment.

TABLE 3.1 Major regulatory bodies in New South Wales and Australia

Regulatory agency	Role
NSW Environment Protection Authority (EPA)	• Primary environmental regulator for NSW • Aims to improve environmental performance and waste management for NSW through a wide range of programs and initiatives. • Offers advice and incentives to help businesses improve their environmental performance. • Governed by the *Protection of the Environment Administration Act 1991*
NSW Fair Trading	• Is the NSW consumer protection agency • Provides information and assistance to all consumers and business owners on areas such as fair and ethical practices • Services to business include: – business licence information, e.g. real estate agents, builders, car dealers – information for builders and tradespeople that covers their responsibilities and offers assistance in relation to disputes between themselves and clients/contractors – product safety standards – trade measurements relating to scales/scanners used to weigh and measure products.
Australian Securities and Investments Commission (ASIC) (federal)	• Monitors market integrity and provides consumer protection in areas such as payment systems and financial services such as investment advice. • Aims to ensure all businesses comply with the industry standards and codes of practice. • Operates the Business Names Register that allows people to register, renew and search business names nationally

Regulatory agency	Role
Australian Competition and Consumer Commission (ACCC) (federal)	• Is an independent statutory authority that administers the *Competition and Consumer Act 2010*. This includes monitoring of: – anti-competitive and unfair market practices such as the misuse of market power (e.g. blocking competitors from entering the market), exclusive dealing and resale price maintenance – mergers and acquisitions that could decrease the level of competition – product safety and liability – misleading and deceptive advertising. • It operates nationally for the enforcement and administration of competition and consumer protection laws.

Other institutional influences

In addition to government bodies, other institutions affect how businesses operate in Australia. Some of these are shown in table 3.2.

TABLE 3.2 Other institutional influences on businesses in Australia

Employer associations	• Developed in response to the growth of trade unions • Represent the interest of employers • Assist employers in the following ways: – formulating policies in line with union activities – acting on behalf of employers in negotiating enterprise or collective agreements – promoting industry, trade and commerce – providing submissions, advice and information to governments.
Trade and industry associations	• National bodies that represent larger groups of employers (e.g. lobbying government on certain issues) • Examples include: – Australian Chamber of Commerce and Industry (ACCI) – National Farmers' Federation – Australian Industry Group.
Trade unions	• Main aim was to improve working conditions and pay rates. • Union membership declined substantially in the past 20 years because of: – new legislation that outlaws compulsory unionism – changes to work patterns (increased part-time and casual work) – workplace agreements – privatisation and restructuring of union-dominated industries.
Australian Securities Exchange	• Operates a sharemarket where companies can raise funds by issuing shares in the company. • A business lists itself with the Australian Securities Exchange to become a public company. The main reason for this is to raise extra capital, usually for expansion and development.

BizFACT

Employer associations are more likely to be involved in unionised workplaces, and in mining, manufacturing, wholesaling, health and community services sectors.

BizFACT

Unions can force a business to change its operations or adjust its planning. In 2013, the CFMEU organised a protest against the construction company Grocon, calling for them to improve their safety standards. More than 5000 construction workers stopped work to march through Melbourne's CBD to highlight concerns over safety standards on their work sites.

3.3.8 Technological influences

Global technological innovation has increased at a remarkable pace, revolutionising the workplace and every aspect of daily life. With appropriate technology, businesses can increase efficiency and productivity, create new products and improve the quality and range of products and services. The use of hi-tech robotics in many manufacturing industries is improving productivity, reducing operating costs and eliminating many boring and repetitious tasks (see figure 3.14). Rapid advances in information technology (IT) have reduced communications delays and allow suppliers and customers to interact over great distances.

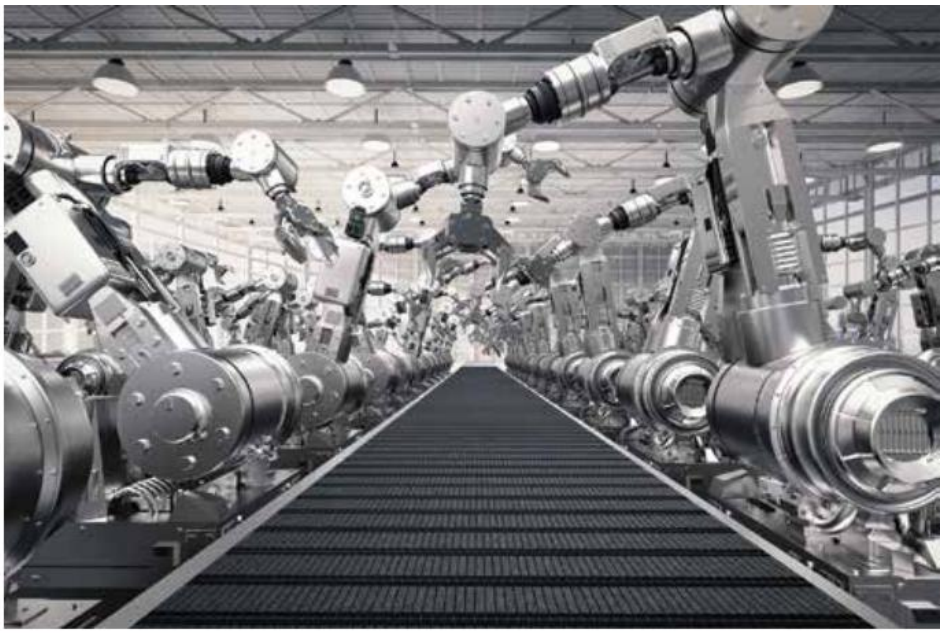


FIGURE 3.14 In 2017, a McKinsey & Company study found that about 30 per cent of tasks in 60 per cent of occupations could be computerised and millions of jobs could be taken over by robots. Those professions that are most at risk are those which are on some level routine, repetitive and predictable, e.g. telemarketing, tax preparers and fast food cooks.

BizFACT

Technological influences have led to the closure of DVD rental stores and CD retailers. Improvements in the speed and capacity of the internet have led to consumers using online mediums such as Netflix and music download services to access content.

BizFACT

Innovations in technology have changed the way consumers access news content. Fairfax Media Ltd was proactive and adapted their business operations to accommodate these changes in the external environment that could have destroyed their business. To respond to these trends, Fairfax developed a portfolio of tablet and smartphone apps, as well as leading websites and digital channels, which led to the renewal of the company.

BizFACT

According to a major report, Australia's Future Workforce?*, published in 2015 by the Committee for Economic Development of Australia, 40 per cent of jobs in Australia—about 5 million of them—are likely to be automated in the next 10 to 15 years.*

New communications technologies allow information to be rapidly transmitted to an ever-increasing number of customers with a speed that now makes communication almost instantaneous. Since the introduction of fibre-optic cables and digital information transmission in the mid 1980s, the speed and capability of transferring communications data has allowed businesses to reorganise their structure and has fundamentally changed workplace practices.

A business that wants to be locally, nationally and/or globally competitive must adopt the appropriate technology. If slow to use and exploit technology, a business is likely to fail: the competition will strive to capture greater market share and develop a sustainable competitive advantage.

Ride-sharing company Uber has transformed the taxi industry through its innovative use of technology. Uber's mobile app connects customers who need to travel with nearby drivers who are willing to transport them. Uber was founded in 2009 and has grown rapidly. It now operates in hundreds of cities in over 60 countries around the world. In many countries, other taxi companies have responded to Uber by implementing their own technologies, such as hailing apps, and challenging the legality of some of Uber's services.

It is impossible to predict the future, but it is expected that over the next five to ten years we will live with more internet-connected devices, including computers, phones, appliances, vehicles and robots. This will generate huge amounts of data, presenting a challenge to businesses — what data is useful and what is not? The ability to analyse this big data will also present opportunities for businesses. There is no doubt that technology will become smarter, meaning that robots and computers will replace more workers completing dangerous, repetitive or mundane jobs. Many businesses will take advantage of 3D printing and wearable technology. Driverless vehicles are already in use in industries such as agriculture and mining. More people will be using autonomous vehicles, and it is likely that pay-per-use will be gradually replacing car ownership. This provides opportunities for more people to work creatively while they are being driven to their destination.

Australian jobs that could be replaced by technology

Technology could make almost 40 per cent of Australian jobs, including highly skilled roles, redundant in 10 to 15 years, a new report has found.

The Committee for Economic Development of Australia (CEDA) report highlighted the need for more funding and a cooperative approach to prepare for huge changes in the workforce.

Almost five million jobs face a high probability of being replaced in the next two decades, while a further 18.4 per cent of the workforce had a 'medium probability' of their jobs being eliminated, the report found.

CEDA chief executive Professor Stephen Martin said the world was on the cusp of another industrial revolution being driven by technology, and it was not just low-paid, manual jobs at risk.

'What we've found is that going right through to dentists, and clergy and chemical engineers — and, dare I say, even editors or newspaper proprietors and, heaven forbid, even economists — all of these are in grave danger of perhaps outliving their usefulness,' Professor Martin said.

The report said jobs that involved 'low levels of social interaction, low levels of creativity, or low levels of mobility and dexterity' were most likely to be replaced by automation.

While automation had already replaced many jobs in manufacturing, agriculture and mining, in the coming decades industries such as the health sector would also be impacted, it was found.

'Health is an especially significant area likely to be impacted, through automation in clinical data and predictive diagnostics (analysis roles), to robotics assisting in areas from surgery to nursing and from hospital logistics to pharmaceutical dispensary,' the report said.

The report found that advances in technologies such as cloud computing, artificial intelligence and big data were largely driving the change.

With approximately a quarter of Australians employed in jobs involving driving, the patenting of a driverless car by Google, enabled by big data, could profoundly change the labour market, the report found.

'Based on the progression of Moore's Law, we shall see computing technology improve approximately 10 000-fold over the next 20 years,' the report said.

'The affordability of autonomous driving systems will improve dramatically.

'Furthermore, if the statistic that 90 per cent of road accidents are caused by human error is correct, governments will inevitably regulate that such systems are mandatory because of the savings to life and health costs.'

CEDA estimated that in December 2012, of the 11.5 million Australians employed nationally, about 28 per cent had jobs that involved driving.

If all vehicles become autonomous in the next 20 years, the report said, those jobs would need to change as the 'human skill of driving a vehicle is no longer an essential part of the job'.

'The customer service aspects of the job will become far more important,' the report said.

If Parliament did not start shaping workplace policy around technological changes, the country would be left behind, Professor Martin warned.

'Every other country in the world is going to be faced with the same sorts of challenges, particularly in the era of globalisation,' he said.

'We simply cannot sit back and say a short-term political cycle will solve the problem. There are many deep and grave issues that this country needs to face to retain its economic first world status.

'We are competing with the rest of the world and tech disruption is going to affect us just like it's going to affect everyone else.'

SNAPSHOT



'… prepare for huge changes in the workforce.'

The CEDA report said Australia had adapted well to the impact of changing technologies on the workforce so far.

'The nation created over six times the number of jobs it lost over the five years to June 2014,' the report said.

'We generally know where the jobs are being lost, and knowing which jobs are a lost cause is important to avoid investing expensive tertiary education in the wrong areas and scarce investment capital that could go into growth industries.'

But the report said where the new jobs would be and why they were being created was the most important challenge for future governments.

Source: Loretta Florance, 'Almost 40 per cent of Australian jobs could be replaced by technology by 2025, report finds', *abc.net.au*.

SNAPSHOT QUESTIONS

1. **Outline** the types of jobs that are most likely to be replaced by technology. Refer to examples.
2. **Explain** the influence technology will have on jobs over the next few years.
3. **Describe** the challenges this creates for government.
4. **Recommend** strategies businesses can implement to prepare for these changes.

3.3.9 Competitive situation influences

BizWORD

A **sustainable competitive advantage** *refers to the ability of a business to develop strategies that will ensure it has an 'edge' over its competitors for a long period of time.*

Competition between firms to be the 'market leader' or to win customer loyalty can benefit the consumer *and* the business. It can provide consumers with more choice, a range of qualities and a variety of prices. From the business point of view, competition can stimulate greater efficiency in production and usually results in a better quality product or service at the lowest cost to the business. Each business aims to achieve a **sustainable competitive advantage** over its competition in order to capture a larger portion of the market.

BizFACT

Blockbuster was once offered the opportunity to buy Netflix, but blew it. Netflix was offered for acquisition to Blockbuster in 2000 for a mere $50 million. Blockbuster CEO John Antioco, thinking that Netflix was a small niche business, declined the offer.

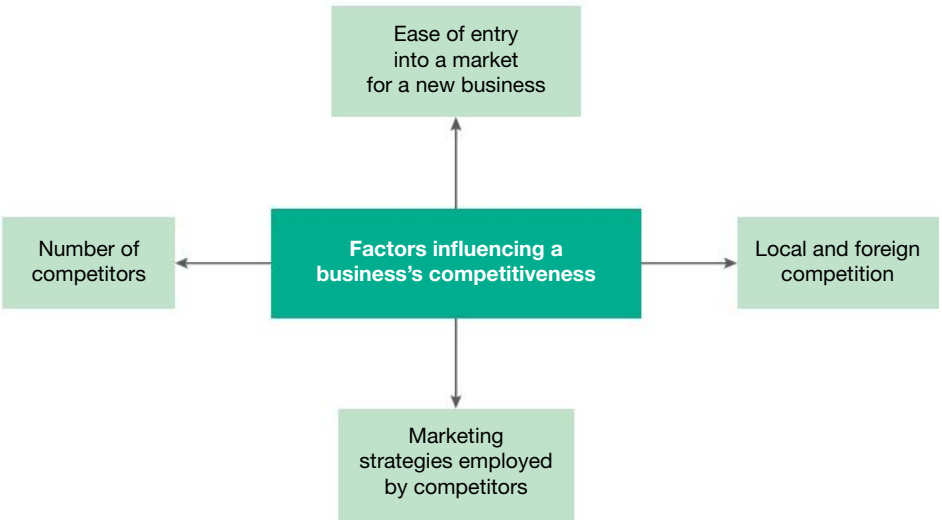


FIGURE 3.15 A business's competitiveness is influenced by a range of factors.

Number of competitors

The number of competitors refers to the size and number of firms that exist within an industry; it is also known as **market concentration**. There are four main types of market concentration (see table 3.3).

TABLE 3.3 Types of market concentration

Types of market concentration	Features/characteristics	Example
Monopoly	• Complete concentration by one firm in the industry • Firm has the ability to decide the price of the good or service because there are no competitors (i.e. the firm is the price maker) • Customer has no influence over the price charged. i.e. the customer is the price taker.	Australia Post Sydney Trains
Oligopoly	• Consists of a small number of larger firms that dominate the market • Are able to stay in control of the market because they spend large amounts of money on advertising and this enables them to restrict the entry of new competitors to the market.	Banks Oil companies Car manufacturers
Monopolistic competition	• Most common type of market in Australia • Large number of buyers and sellers • The goods and services sold are differentiated from competitors using methods such as packaging, advertising, brand names and quality.	Clothing manufacturers Local retailing
Perfect competition	• Large number of small businesses that sell products that are the same or similar • Very little advertising is used to increase market share • The only way to achieve market share is through price competition.	Fruit and vegetable growers

BizWORD

Market concentration *refers to the number of competitors in a particular market. There are four main types of market concentration:*

- *a* **monopoly** *— is complete concentration by one firm in the industry, e.g. Australia Post*
- *an* **oligopoly** *— where a small number of larger firms have a greater control over a market, e.g. car manufacturers*
- **monopolistic competition** *— where there is a large number of buyers and sellers in a particular market, e.g. local retailing shops*
- **perfect competition** *— where there is a large number of small firms that sell similar products. They are unable to differentiate products from each other and so can only use price as a way of achieving market share, e.g. fruit and vegetable growers.*

Ease of entry

Ease of entry refers to the ability of a person (or persons) to establish a business within a particular industry. The ease of entry will be determined by the type of market concentration. When there are many small firms (perfect competition and monopolistic competition), entry is not difficult as businesses are small and it is more affordable for the business owner to gain some part of the market. When a few firms dominate an industry (oligopolies), entry is difficult because the firms are larger and often more established. Potential competitors must have enough resources to gain some control in the market.

When only one firm (monopoly) dominates an industry, no competitors are able to enter the market because the one firm has control over all resources that are being sold.

BizFACT

Examples of businesses with low barriers to entry are food businesses, retail stores, and consulting and professional services. Industries with high barriers to entry include mining, manufacturing, healthcare, agriculture and transportation.

Local and foreign competitors

A business will be influenced by both local as well as foreign competitors. Local competitors are those who produce or sell a good or service in the same market. Local competitors must deal with the same variables as each other. These variables include:

- labour costs
- transport costs
- the economy
- cost of stock/raw materials.

Foreign competitors are those businesses located overseas or offshore. They sell their goods or services in Australia and compete with local businesses. One such global company that has seen opportunities in expanding into the Australian market is the fashion retailer Zara (see the following Snapshot).

BizFACT

In 2016, some major retailers went into administration including Marcs, David Lawrence, Payless Shoes, Pumpkin Patch, Masters and Dick Smith. Competition, especially from the expansion of international stores to Australia, has been a major contributing factor to their decline.



FIGURE 3.16 Netflix, an American entertainment company, has disrupted the Australian media industry, resulting in the demise of competitors such as Blockbuster, as well as declining revenue for free-to-air commercial television networks as well as pay television networks such as Foxtel. By providing customers with the convenience of a wide selection of high quality streamed media at a low price, the company appealed to a mass market. Netflix now serves over 190 countries, with more than 75 million subscribers.

Discuss the expansion into Australia of one global business

SNAPSHOT



'Zara launched in Australia in 2011, shaking up the local fashion sector.'

Case study: Zara — expansion of a global business

Zara launched in Australia in 2011, shaking up the local fashion sector. Since Zara was listed on the Spanish stock market in 2001, they have used expansion to increase their net profit. This global expansion led them to become Spain's largest company as well as the world's largest clothing retailer by sales.

Even though Australia is a much smaller market than other parts of the world, Zara made the decision to expand into Australia because they perceived it as a valuable market of fashion-savvy consumers who desire the latest fashion and international brands. Zara already had an enthusiastic following among many Australians who travelled overseas and desired their high-quality fashion and low prices. For its Australian debut, Zara opened a massive three level store in Sydney. Since then, Zara has continued to expand throughout Australia and currently has 17 stores across the nation.

Zara does not simply rely on its recognisable brand name to aid its expansion into Australia and other countries. The company works hard to research and understand the different local markets, then tailors its retail strategies to suit those different needs. Zara adapted its European style to suit Australian taste and weather, creating custom weather-appropriate collections to complement the climate for its Australian stores.

So, how did Zara's entry into Australia affect other Australian retailers? Other brands such as Witchery and Sportsgirl have seen their sales affected by Zara's entrance into Australia, especially because they share a similar target market. In order to survive, these retailers have been forced to differentiate themselves and re-evaluate their product range, pricing and promotional strategies.

Zara has maintained its tight adherence to its strategy even as it pursues its aggressive global expansion. They have successfully expanded into 93 countries and have over 2200 stores worldwide.

SNAPSHOT QUESTIONS

1. **Outline** why Zara decided to expand into Australia.
2. **Discuss** the effect Zara has had on the Australian fashion industry.

Marketing strategies

A business will be influenced by the type of marketing measures taken by competitors. For example, the business that uses television advertising extensively will have greater exposure to the market than a business that relies on flyers or word of mouth. Of course, the type and extent of marketing will depend on:

- *the size of the market* — the number of existing and potential customers
- *the size of the business* — the larger the business the more likely it is to invest in a range of marketing activities, especially more expensive forms of marketing such as television and newspapers. Smaller businesses may rely on simple marketing methods such as pamphlets, local paper advertisements and word of mouth.
- *number of competitors* — usually the more competitors that there are in a market, the greater the need for marketing. This is necessary to maintain or increase market share.
- *the nature of the product* — this refers to the type of product and whether it requires extensive marketing. Some products, such as postage stamps, don't need to be advertised in order to make sales.



FIGURE 3.17 JB Hi-Fi invests a lot of time and money in their marketing mix. For instance, they have significantly expanded their product range over the years, they improved their website and introduced online sales, their prices are always competitive and they spend a lot of money on promotion, e.g. advertising on television and in catalogues. Other home entertainment retailers would find it very difficult to compete.

3.3.10 Markets

Changes in financial/capital markets

Finance (capital) is now more mobile and flows relatively easily between countries, especially since the 1970s when many countries phased out their controls on foreign exchange trading. As a result, international financial flows have expanded very rapidly over the last three decades. Consequently, the world capital market is now more integrated than ever before.

Capital flows to those countries where the investment opportunities and returns are favourable. It is now much easier for individuals and businesses to access overseas share markets and purchase equity in foreign companies.

Changes in labour markets

The labour market has not been 'freed up' to the same degree as other markets. If anything, the labour market has become less global in the last 60 years. Due to political barriers, the flow of people between countries is now more restricted than it was from 1850 to 1900, when waves of migration occurred. This trend

seems likely to continue, especially the restrictions placed on the movement of low or unskilled labour. For example, even within the European Union, which gives citizens of any member nation the right to work and live in any other, only a small proportion of workers travel across national borders.



FIGURE 3.18 Skilled immigrants on temporary work visas have offset population ageing, improved labour productivity, helped businesses to source skills that are difficult to find at short notice, and addressed the needs of regional areas and industries.

BizFACT

There are currently 95 758 people who have the skilled visa, including family members. The majority of the visa holders come from India, which accounted for almost a quarter of the intake, followed by the UK and China at 19.5 per cent and 5.8 per cent respectively. There are a range of different occupations on the list including neurologists, midwives, cabinet makers and lift mechanics.

However, two trends in the labour market have resulted in the movement of workers. First, the movement of large numbers of temporary skilled migrant workers has been very important in Australia, Europe and Asia. The Temporary Work (Skilled) visa (subclass 457) was introduced in 1996 and was designed to fill job vacancies that are difficult to find Australians for. This was replaced in 2018 by the Temporary Skill Shortage (TSS) visa (subclass 482). The TSS visa program is made up of a short-term (up to two years) visa or a medium-term (up to four years) visa. It aims to support businesses in addressing genuine skill shortages in their workforce. The employee can also bring members of their family to Australia on a secondary visa. The medium-term visa provides a pathway for skilled workers and their dependents to apply for permanent residence under the Migration Program. Second, the growing demand for highly trained employees means that such people are increasingly mobile.

Changes in consumer markets

There has been phenomenal growth in the amount and value of world trade, especially since the end of World War II. For example, during the period from 1995 to 2005, global trade in goods and services increased by approximately 150 per cent. In 2008–09, however, the global financial crisis saw a fall in global output and trade, which was the first of its kind since the Great Depression during the 1920s and 1930s. After the sharpest decline in more than 70 years, global trade was predicted to rebound over the next few years and grow at 9.5 per cent. In 2016, global trade increased only 1.3 per cent, reflecting a slowdown in China and falling levels of imports into the United States. The World Trade Organization (WTO) predicts that global trade will expand by 2.4 per cent in 2017, but only if the global economy recovers as expected. Countries are achieving cost savings by specialising in products they can produce efficiently. This results in cheaper prices on the world market and, in turn, generates increased sales in existing markets. New consumer markets also emerge, particularly in developing countries, like China and India.

Improved technologies and communications have also changed consumer markets. With the advent of the internet, innovative and visionary Australian businesses may reach much larger markets and take advantage of economies of scale. Consumers around the world will just as readily browse an online store as examine a catalogue delivered to their private letterboxes.

SUMMARY

- Legal influences are the regulation (legal framework) within which a business must operate.
- Political influences are derived from state and federal government policies and include free trade policies and the process of deregulation.
- Institutions that influence business include government, regulatory bodies and other groups such as trade unions and employer associations.
- Technological influences can increase business productivity and communication.
- Each business is influenced by their competitors and should aim to achieve a sustainable competitive advantage.
- Factors influencing a business's competitiveness include the ease of entry into a market for a new business, local and foreign competition, the marketing strategies employed by competitors and the number of competitors.
- Other external influences include changes in financial, labour and consumer markets.

EXERCISE 3.1 REVISION

1 **Define** the term 'business environment'.
2 **Distinguish** between internal and external business environments.
3 In small groups, use the brainstorm technique to **identify** the elements that determine the environment of your Business Studies class. Choose a spokesperson to share the group's comments with the rest of the class.
4 **State** what you understand by the 'economic cycle'.
5 **Why** does the level of economic activity fluctuate over time?
6 **Outline** the impact of globalisation.
7 **Justify** why businesses should offer family friendly workplace practices.
8 **Why** is the ACCC so important to business in Australia?
9 **Explain** why it is important for a small business owner to comply with the consumer protection provisions of the Competition and Consumer Act.
10 Choose one of the current political issues affecting business from figure 3.11 and **explain** the impact this policy will have on businesses.
11 Using their websites, investigate the **NSW Environment Protection Authority**, **NSW Fair Trading**, **Australian Securities and Investments Commission (ASIC)** and **Australian Competition and Consumer Commission (ACCC)** and then complete the following questions.
(a) **State** their role.
(b) Briefly **outline** their importance to Australian businesses.
12 **How** has information communication technology, especially the internet, changed existing consumer shopping practices?
13 **Define** the term 'sustainable competitive advantage'.
14 **Describe** what is meant by the term 'market concentration'. Give examples.
15 **Outline** four types of market concentration.
16 **Explain** why the marketing strategies of a competitor will impact on a business's competitive situation.
17 List five different products you use regularly, such as your computer, phone, shoes etc. and:
(a) **identify** the brand name of the product
(b) **identify** the company that made it
(c) **identify** in which country it was made
(d) **determine** why it was made there.
Compare your list with other class members, noting similarities and differences. **Propose** a conclusion you can derive from this investigation about global consumerism.

on Resources

- **Weblink:** NSW Environment Protection Authority
- **Weblink:** NSW Fair Trading
- **Weblink:** ASIC
- **Weblink:** ACCC

18 **Identify** which external influence is affecting the small business in each of the following cases:

(a) Julie runs a small busy restaurant. She recently introduced technology that allows waiting staff to electronically send orders to the kitchen. This means better service for the customer because the order is taken more efficiently and more time can be devoted to other tasks such as the prompt delivery of food and drinks.

(b) John is the manager of a function centre that hosts large weddings and conferences. He makes sure to include an acknowledgement of the traditional owners of the land, the Wurundjeri people and their elders, in his opening remarks.

(c) Mia has to design and print new labels for the foods sold in her deli. This is because changes to the food labelling laws require that all foods list the ingredients by particular portion size. This allows customers to more easily compare different food items. She thinks that this may affect which foods customers choose.

(d) Michael, the owner of a local bottle shop, is no longer allowed to sell imported premixed alcoholic drinks because of a government ban on food and beverage imports from particular countries.

EXERCISE 3.1 EXTENSION

1 **Explain** the impact each of the external influences has on a business and how the business's management responds. The first factor has been completed for you.

Factor influencing the internal environment	Brief explanation	Management response
Political influences	Elected governments at all levels in Australia regulate markets and have the power to make or change laws.	Must comply with the laws and regulations introduced by governments

2 Using an example, **determine** how the development of global consumers encouraged the process of globalisation.

3 (a) **Demonstrate** how technology has affected the way consumers can purchase goods and services.

(b) **Predict** what will happen if an Australian business does not provide the opportunity for consumers to purchase online.

4 In small groups, **examine** and report on a social issue confronting businesses in your local area. You may wish to either prepare a PowerPoint presentation or use a word-processing package for your report.

(a) **Outline** the issue.

(b) **State** how the local businesses have reacted to the situation.

(c) **Determine** what indicators you would use to decide the success or failure of a business's response to the situation.

3.4 Internal influences on business

Internal influences relate to the specific factors within the business that will affect its operations. These factors can be identified and adjusted via feedback and evaluation processes that provide the business with information for change.

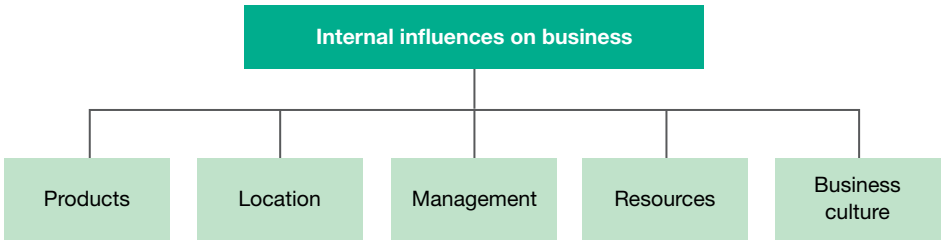


FIGURE 3.19 Internal influences on business

3.4.1 Product influences

Product influences affect a range of internal structures and operations within the business. The main product influences on a business are as follows.

1. The type of goods and services produced will affect the internal operations of a business. If the goods are physically large or require many raw material inputs, there will need to be structures in place to organise and monitor the processes involved in production. In contrast, a service may be delivered by a home-based business or a franchise business, such as Jim's Mowing, and will influence the internal structures or processes differently.

   The range of goods and services refers to the number produced by the business. The larger the number, the more internal impact it will have on the business as it will need to expand operations and internal structures to accommodate the changes. Companies such as Coca-Cola have continually expanded their product range over the last 20 years, and this has meant that internal changes to operations and management have been necessary to allow this expansion to occur.
2. Product influence will be reflected in the type of business (service, manufacturer or retailer). Internally, a service provider will be structured differently to a manufacturer or retailer, and the influences will vary. Some goods or services require extensive preparation, while others are merely deliverers. Consider the difference between the product influences of a clothing manufacturer and that of a clothing retailer.
3. The size of the business, as previously mentioned, will be based on the range and type of goods and services produced, the level of technology utilised, and the volume of goods and services produced. The larger the business the more goods and services being produced, which will in turn influence the internal structures and operations of the business. A café will operate at a different scale to a club bistro and therefore the influence on business functions will be relative.



FIGURE 3.20 Manufacturing businesses must have a physical location for their production and stock holding operations, whereas service firms do not require a physical production site. The people creating and delivering the service can be located anywhere.

3.4.2 Location influences

Location can make the difference between success and failure, sometimes before the doors even open for business. Choosing a location is one of the most important decisions business owners will have to make. The location can affect many aspects of how a business operates, such as total sales and how expensive it is to run. Even online and home-based businesses can be affected by location-dependent rules and regulations. A bad location is a liability that adversely affects sales and profits.

The choice of location is therefore important. This is particularly true for retail and service-oriented businesses, which need a constant flow of people walking past the store — the passing trade — and thus need to be located in a shopping centre, mall or main street. Locating next to **complementary businesses** may be beneficial because more customers may be attracted to a single site, as demonstrated by the clustering of retail outlets.

BizWORD

A ***complementary business*** *is one that sells a similar range of goods and services.*

BizFACT

To assist in selecting the best site, market research companies can be hired to prepare traffic and pedestrian flow measurements, an analysis of demographic data and an investigation of future trends. When selecting a suitable site to locate a new small business, it is crucial to remember real estate agents' three important words: 'location, location, location'.

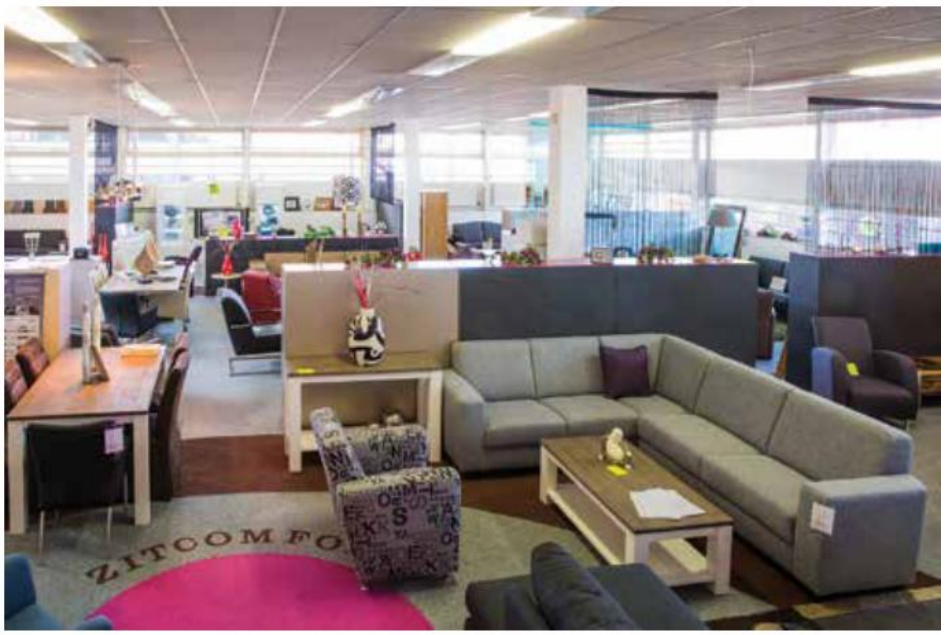


FIGURE 3.21 Locating next to complementary businesses is beneficial in some industries, because more customers may be attracted to a single site. Many homemaker centres contain complementary businesses, such as furniture stores.

Each individual small business must satisfy its own criteria when deciding on the 'best' location. Figure 3.22 outlines the factors to consider when choosing a location.

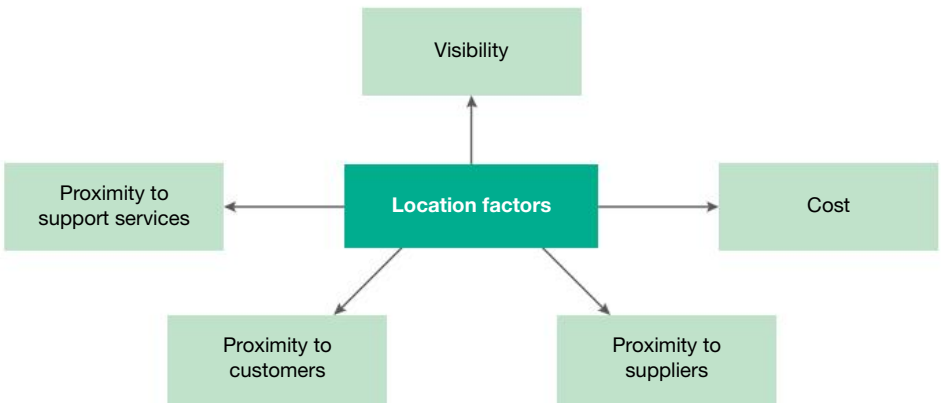


FIGURE 3.22 Factors to consider when choosing a location

The factors in figure 3.22 vary in importance from business to business, and depend on a business's main activity. To understand each factor, it is necessary to consider the differences in a location decision for a retail business (such as a clothing store or café) and for a non-retail business (such as manufacturing or wholesaling).

For a retail business, location is extremely important to its overall success. The location must be convenient for potential customers and central to customers' own location — that is, the business must have passing customer traffic.

Location for non-retail businesses such as manufacturers is about position and convenience. This means being close to transport facilities, which allow for shipping goods to customers and receiving supplies necessary for production. Many wholesalers and manufacturers locate in industrial estates or parks, which have been set up by local councils.

Visibility

If a business is not visible, customers may not make the effort to find the business and optimum customer flow will not be achieved. A business wanting high visibility would locate in a prime shopping area such as a shopping centre or main street. Companies concerned with manufacturing would not consider this to be a crucial consideration, so may choose a low-visibility location 'out of town' and then advertise their location to appropriate customers.

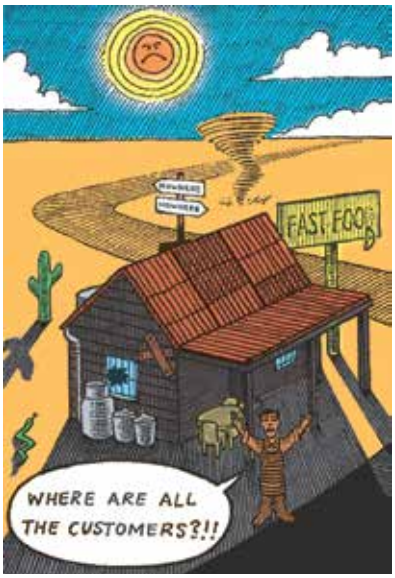


FIGURE 3.23 For many retail businesses, visibility is one of the important factors to consider when deciding on a location.

Cost

Cost is another factor to consider when determining the location of a business. Leasing or purchasing a central location in a busy shopping centre will be far more expensive than in a location with lower levels of passing customer traffic. If the business relies on passing customer traffic and maximum exposure, then the cost factor is unavoidable. These types of businesses include coffee shops or cafés, fast food outlets and retail shops. The business owner will need to be confident of generating sufficient business to justify the higher cost.

On the other hand, location may not be a key consideration if the business does not rely on passing customer traffic. Such businesses search for a low-cost site, especially if they are related to manufacturing and require large premises. These types of businesses include mechanics, car yards, equipment hire, and even solicitors and doctors.

Given the rapid changes in technology, many businesses do not consider their location as important at all. They are able to communicate with their customer base through the internet, which has become the fastest growing avenue for consumer sales. These types of businesses include telemarketers or businesses that sell their products via the internet.

Proximity to suppliers

Proximity to suppliers is an important consideration for some businesses but not others. The main issue is the size and quantity of the raw materials needed for production, or the size of the finished goods to be supplied. A business that relies on bulky raw materials or finished goods — such as a logging company or steel manufacturer — has significant transport costs and will locate closer to the supplier

in an attempt to reduce costs. However, for a business that does not transport bulky goods, proximity to suppliers is not a major consideration. These businesses include florists, bakeries and shoe retailers.

Proximity to customers

The importance of proximity to customers depends on the type of business being established. A retail business must be convenient for their customers and locate close to their customer base, so shopping centres or a shopping strip with off-street parking will be the primary choice. A manufacturing or wholesaling business may decide it is more cost effective to transport the product to the customer, particularly if bulky raw materials are needed. Other location cost factors could include leasing costs in 'prime shopping areas', incentives offered by local councils and general overheads such as rates or utilities.

Proximity to support services

BizWORD

Support services *are the activities needed to assist the core operations or prime function of a business.*

Support services are the activities needed to assist the core operations or prime function of a business. They include accountants, solicitors and government agencies such as Austrade and the Business Enterprise Centre. Small businesses traditionally tend to use external services (mainly as a result of limited finance) whereas medium-sized and larger businesses often provide their own support services internally. But this trend is changing, with businesses now preferring to downsize their work force (in an attempt to reduce costs) and outsource many activities.

Today, proximity to support services is not the most important location factor, because advancements in technology have enabled all businesses (large or small) to access a range of support services through the use of computers (the internet and email), mobile phones, and phone and video conferences.

3.4.3 Resource influences

BizWORD

Human resources *are the employees of the business and are generally its most important asset.*

Information resources *include the knowledge and data required by the business, such as market research, sales reports, economic forecasts, technical material and legal advice.*

Physical resources *include equipment, machinery, buildings and raw materials.*

Financial resources *are the funds the business uses to meet its obligations to various creditors.*

The four main resources available to a business are:

- **Human resources**. These are the employees of the business and are generally its most important asset.
- **Information resources**. These resources include the knowledge and data required by the business such as market research, sales reports, economic forecasts, technical material and legal advice.
- **Physical resources** include equipment, machinery, buildings and raw materials.
- **Financial resources** are the funds the business uses to meet its obligations to various creditors.

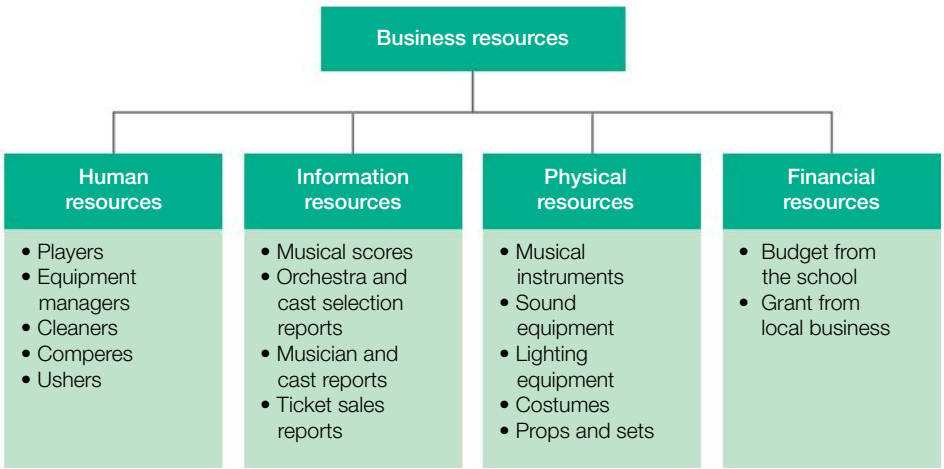


FIGURE 3.24 Resources required to produce a school musical

Although the quantity and quality of these resources varies amongst businesses, it is by combining them that all the goods and services demanded by consumers are produced.

It is important to realise that these are only general categories of resource. Within each category there may be hundreds of more specific resources from which the manager must choose. Gathering, selecting and coordinating the appropriate resources from a complex array requires knowledgeable and efficient managers. The skills and expertise of the management team in coordinating the business's resources will largely determine whether the objectives of the business are achieved.

3.4.4 Management influences

Rapid advances in technology, coupled with the significant pressures on businesses from increased competition due to forces of globalisation, have resulted in businesses flattening their structures. This means that there are fewer levels of management. Such businesses can adapt quickly to meet changing consumer needs and market conditions because there are fewer managers who need to approve decisions.

BizFACT

If a business adopts a traditional hierarchical approach, management may allocate supervisors who have direct control and authority to ensure work processes are carried out. However, if a business adopts a flat management structure, it will emphasise teamwork and shared responsibility for achieving business goals. In today's global environment, there is an ongoing emphasis on 'virtual teams'. Such teams work without time, space or organisational boundaries by making use of sophisticated communications technology.

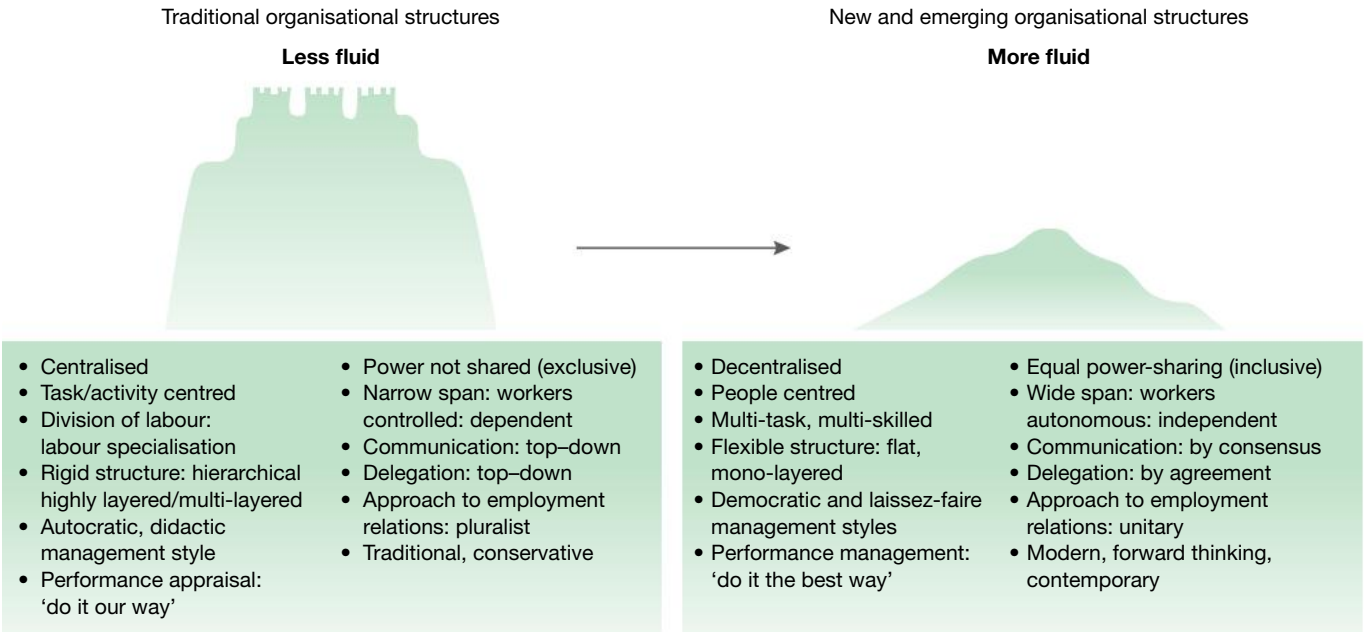


FIGURE 3.25 Pouring water on the sandcastle

Businesses that adopt a flatter organisational structure reduce the number of levels of management, giving greater responsibility to individuals in the business.

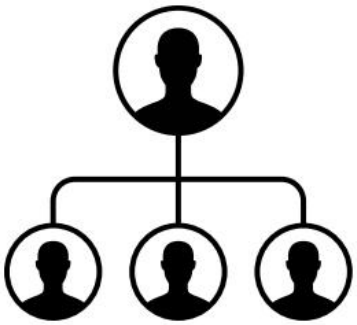
The trends and changes in organisational structures are summarised in figure 3.25. The characteristics listed on the left-hand side apply to the traditional structures, whereas those on the right apply to the most modern structures. Many businesses are in transition — they have adopted the traditional design and taken on elements of the newest designs.

The characteristics of the two organisational structures reflect the important influence management has on business. Collaborative workplaces allow for a more cohesive and inclusive business culture. The management style that the business adopts will depend on its size and main activity — for example, retail, manufacturing or service (see the following Snapshot).



FIGURE 3.26 A Deloitte survey of 7000 companies in 2016 found that only 38 per cent of companies have a traditional hierarchical structure. Most organisations have moved away from top-down hierarchies and are operating their businesses as networks of teams.

SNAPSHOT



'… flat has been all the rage …'

More companies are adopting a flat working structure

A MOVEMENT is sweeping offices all over the world that could fundamentally change the way you work. Are you ready for it?

A FLAT stomach is a good thing. Let's not argue that point.

What's less widely known is that, in a bizarre case of business imitating bellies, a flat company has become just as en vogue.

As a hip, disruptive alternative to hierarchy — and its dreaded tiers of middle management — flat has been all the rage with high-profile adopters including Google and Toyota over the last decade. But is flat a passing trend? And is there proof to justify the massive pain of reorganisation?

Valve is a trailblazing software developer and maker of computer games like *Half-Life* and *Counter-Strike*. It's also a company with a non-hierarchical structure. As the handbook for new employees states: 'Welcome to flatland. We don't have any management, and nobody reports to anybody else.' To create an environment that fosters innovation, Valve has zero layers of management between staff and owners. Employees wield the power to green-light projects, and individuals choose which jobs to work on. With no bosses or managers, it's like an anarchist's dream. But does it work?

'Traditional hierarchy is well suited for improving efficiency, but not for innovating or adapting to change. And the problem is there are multiple industries facing radical change,' says Tim Kastelle, a Princeton alum, University of Queensland professor and world authority on corporate organisational structures. No surprises there. With the inflexibility and waste of company bureaucracy, it's enough to make any company think twice about org charts.

But don't hit delete on your existing management model just yet — the success of flat-structured businesses can be determined by your industry, size and even human nature. A recent Stanford study showed people find hierarchical structures easier to understand, and clear chains of command give a sense of comfort.

After all, the idea of centralised decision-making is older than the pyramids. And if you're at the bottom of the pile, you're not responsible for anything. However, says Kastelle, 'this creates a limited view of what work can be'.

Early adopters like Valve, and web-based hosting service GitHub, have reaped the benefits of a muscular, flat structure — GitHub to the extent that it has no middle managers. Employees are beholden to no one, and are encouraged to define their roles in ways that make sense to them. Before dismissing this as nerdy-hipster nonsense, note as of the last financial year, GitHub had been profitably growing revenue at 300 per cent annually since 2008, and boasts an estimated worth of more than $750m.

But flat is no longer the exclusive realm of supercool start-ups. 'It's not just small companies. Big manufacturing and media companies are trying it for size too,' says Kastelle. 'Even the armed forces are looking to disperse decision-making in combat.'

Toyota has also flattened out, avoiding micromanaging employees. And as far as systems go, it's cashing in. Despite the global recession faced by American companies like General Motors in 2009, Toyota went on to enjoy profits of $16.7bn that year.

And the factors driving change aren't going away. 'Connectedness, both within and from the workplace to the world is a major driver,' says Kastelle. 'Ease of connection improves access to knowledge. Business models based on limited access to information are falling to pieces now.'

But there are times when hierarchy is indispensable, as Google discovered in 2002. The internet giant flattened the organisation in an effort to create an environment conducive to swift concept development. The consequences were dire. Instead of making decisions, employees went straight to co-founder Larry Page for a final call. Before two months were up, Page reinstated all managers after a deluge of requests landed on his desk. Kastelle describes this as a colossal bottleneck: 'The whole advantage of flat is pushing decision-making out to people who are on the frontline, making them more flexible.'

However, former Valve employee Jeri Ellsworth argues that flat start-ups are missing a key component: 'Management makes tough decisions based on facts and carefully collected data, instead of emotional reasons, such as rumours, or whoever can argue the longest.' It seems that within these flat havens of equality exists an Orwellian Animal Farm scenario where some employees are actually more equal than others.

So, if the modern workplace is fluid and connected, why are so many companies still unwilling to trim back unnecessary fat at different levels of management? Kastelle has a few theories. 'If only a handful of people can be trusted to make decisions, or if information is scarce, then hierarchy works well. But the purposes and structures of companies are starting to shift as quickly as the business cultures around them.'

However, experts say it's only a matter of time before more lean structures better suited for the digital age take hold.

Have a look at your manager and console yourself with this thought: in a decade, they might not exist. And prepare yourself for autonomous roles that require more decision-making and innovation. For now though, the impatient among us can seek out the early adopters already travelling flat out. As novelist and future forecaster William Gibson stated, 'the future's already here — it's just not very evenly distributed'.

Source: David Halliday, 'More companies are adopting a flat working structure', *news.com.au*.

SNAPSHOT QUESTIONS

1. **Discuss** the traditional hierarchical approach to management.
2. **Identify** the factors that will impact on the success of flat-structured businesses.
3. **Outline** the benefits of a flatter management structure.

3.4.5 Business culture

All businesses have their own **business (corporate) culture** — the values, ideas, expectations and beliefs shared by the staff and managers of the business. Each business develops its own particular way of doing things. The style or character of a business is consequently reflected in its culture.

Business culture can be revealed officially in the policies, goals or slogans of a business. It can also be seen in the unwritten or informal rules that guide how people in the business behave, such as the way staff dress, the language staff use and the way that staff treat each other and customers.

BizWORD

Business (corporate) culture *refers to the values, ideas, expectations and beliefs shared by members of the organisation.*

BizFACT

Job seekers are increasingly concerned about the corporate culture of a potential employer. It is difficult to determine corporate culture — or 'the way things get done' — at an interview. Things to look out for are the way people dress, how they address each other and even the office facilities. Some offices have gyms and cafés to encourage work–life balance.



FIGURE 3.27 Google is one of the most sought-after employers due to its unique culture. Its workplace has a wide range of amenities for staff and looks more like an adult playground than a place of work. It is designed to be fun and inspiring and has a very casual and relaxed work environment. Google maintains an open culture in which everyone is made to feel comfortable to share their ideas and opinions.

BizFACT

Each year, Great Place to Work studies the world's most notable workplace cultures in order to discover the Best Places to Work. In 2017, the Best Place to Work in Australia for businesses with between 100 and 999 employees was Stryker. Stryker is one of the world's leading medical technology companies. The Best Place to Work for businesses with fewer than 100 employees was Avenue Dental on the Sunshine Coast, which operates three dental practices in the area.

BizFACT

ANZ Bank's core values are integrity, collaboration, accountability, respect and excellence.

A manager must understand and assess all facets of a business's unique culture as this is a powerful tool for achieving goals. Knowing and appreciating a business's culture makes it easier to get things done faster or to initiate a change to routine or procedures. Competent, effective managers will use the business's culture as a force for positive change. Research has shown that businesses with a healthy, well-developed and strong culture are more likely to be successful, because such a workplace is perceived by the employees to be more positive and personalised. Employees who have clear expectations feel better about their work — they develop a sense of belonging. A manager who does not understand a business's culture may experience failure or disappointment.

Elements of a business culture

A business culture normally consists of four essential elements:

1. *Values.* These are the business's basic beliefs, shared among its employees. Business values can include honesty, hard work, teamwork, quality customer service, employee participation and innovation.
2. *Symbols.* These consist of events or objects that are used to represent something the business believes to be important. It is a case of 'actions speaking louder than words'. For some businesses, competitive sports are a key feature of the business's culture. Other businesses have encouraged employee development and loyalty through the use of training and development programs.
3. *Rituals, rites and celebrations.* These are the routine behaviour patterns in a business's everyday life. Regular social gatherings can be held to help develop a sense of belonging among employees who normally work in small teams during the week.
4. *Heroes.* Heroes are the business's successful employees who reflect its values and, therefore, act as an example for others.

Culture and organisational structures

The culture of a business is often evident in its organisational structure. Formal businesses with an emphasis on bureaucracy, line authority, hierarchical management structures, and defined job titles and areas of responsibility often have prevailing cultures that emphasise accountability, communication and cooperation. They also tend to conform to a culture of loyalty and respect for superiors (or, if not for superiors, at least for the positions they may hold). A culture that values and expects defined career pathways may be evident in formal organisations.

Less formal businesses with flatter management structures, less departmentalisation and fewer defined spans of control often exhibit highly flexible, innovative and risk-taking cultures. Apple Inc. is an example of a company that values innovation. Steve Jobs, the company's co-founder, created the atmosphere of innovation that allowed the company to successfully introduce new products such as the Apple Mac, iPod, iPhone and iPad.

Management's role in developing a business culture

Once a positive business culture is established, it needs to be kept alive. This is where management comes in. Management must ensure that staff members are given sufficient training to reflect the values of the business. For example, if treating customers respectfully is important in the business, then this might become part of customer service training.

For a change in business culture to be successful and sustainable, it is vital that senior management be role models for staff in those important values. Management must continually reinforce what the values are by communicating with staff, rewarding employees who display the appropriate values, and recruiting staff who already fit in with the values of the business.

BizFACT

Spotify has planned for employees to be integral to its success. The office culture is part of an internal environment that is designed to be fun and inspiring. At its Australian office, music artists are brought in every few months for employees to enjoy during 'Spotify Sessions'.

Here's why 'cool' offices don't always make for a happier workforce

Who are Britain's happiest workers? The people who staff the London office of US travel tech firm Expedia, according to Glassdoor's annual workplace satisfaction survey. In both 2016 and 2017, Expedia rated highest for employee satisfaction, according to anonymous reviews from current and past workers.

Reading this *Business Insider* profile of the 'happiest office in London' might make you believe that Expedia's high level of employee satisfaction is down almost entirely to the office itself and the various on-site perks — which include table tennis, football, gaming consoles and a cocktail bar. There's no doubt that this is a very attractive office.

But the survey of the employees shows that Expedia's people like working there because of the business, not the fancy office. The most positive ratings cite 'culture' and 'career opportunities'. The physical surroundings barely merit a mention.

This is a trend. Workplace contentment is too often incorrectly attributed to the aesthetics of the office, disregarding more influential factors such as job security or work satisfaction. But since we can't Instagram job security, it's the offices that get the credit.

It's very easy, when profiling a company as *Business Insider* did, to use their expensively designed office as a metaphor for happy employees. It's a false narrative. Happy workplaces don't need beanbags, barbecue stations and ball pits.

Those are (arguably) nice to have, but they're not culture. In their attempts to be seen as fun, happy places to work, modern businesses are venturing very close to turning their offices into circuses in order to improve perceptions to potential hires and journalists.

Yes, Expedia is a happy workplace and yes, it has a very nice office. But that's more likely because companies that invest in creating a nice physical environment are also likely to invest in more meaningful areas of employee contentment too. Expedia offers its people up to US$14 000 a year in travel perks, for example.

HAPPINESS IS NOT A HAMMOCK

Businesses spend billions of dollars every year trying to make their people happy. But it's not working. In America, 70 per cent of the workforce are disengaged. Office workers want more than toys and breakout spaces.

In fact, a study I was recently involved with revealed that approval-seeking quirky perks can actually annoy office workers. People rarely want to work in a hammock or take a crisis meeting in a ballpit.

SNAPSHOT



'… how do companies foster good relations among their people?'

on Resources

Weblink: Expedia

If only employers would listen more, they'd realise their people aren't asking for much. Screen privacy is a big thing for many — 74 per cent of the 1000 office workers surveyed in a related study said the feeling that others can see what they're working on causes them some degree of anxiety. This is an issue that is cheap to fix and which would improve workplace contentment for many. But it's hardly Instagrammable.

Employee satisfaction is more often derived from simple measures such as investing in high-quality, comfortable furniture and providing refreshments, not the hay bales and hammocks cited by study recipients as being among the most pointless attempts at creating an Instagrammable office.

A 2016 Society for Human Resource Management study said it's pay, prospects, feeling respected and trust that give the most happiness to employees. Hardly groundbreaking news. Money aside, it's more about relationships than values, CSR or aesthetics that gets people out of bed on Mondays.

It stands to reason. One of the biggest sources of happiness — in life, not just at work — comes from forging strong and close relationships, according to a study of Harvard's class of 1980.

So how do companies foster good relations among their people? The obvious answer would be office socials, an open-plan workspace and regular activities, something most modern offices are already investing in. Companies such as Expedia also invest in events which combine training with networking opportunities.

Source: 'Here's why 'cool' offices don't always make for a happier workforce', *The Conversation*.

SNAPSHOT QUESTIONS

1. **Why** do employees like working at Expedia?
2. **Identify** what some workplaces have done in an attempt to make employees happy, that have no bearing on culture.
3. **Outline** measures businesses can implement to improve employee satisfaction.

SUMMARY

- The internal influences on a business include product, location, resources, management and business culture.
- Product influences affect a range of internal structures and operations within the business.
- Location will have a direct impact on the sales and profits of some businesses.
- Factors to consider when choosing a location are:
  - visibility
  - cost
  - proximity to suppliers
  - proximity to customers
  - proximity to support services.
- The four main resources that influence a business are human, information, physical and financial.
- Businesses can adopt a traditional hierarchical structure or a flat organisational structure.
- Business culture can be seen in the unwritten or informal rules that guide how people in the organisation behave.
- There are four essential elements of a business culture: values, symbols, rituals and heroes.

EXERCISE 3.2 REVISION

1 **Summarise** one way in which product influences affect a business.
2 **Identify** and **outline** three factors a business must consider when choosing a location.
3 **Describe** the four main resources available to a business. Choose one of these resources and **explain** how it will influence a business.
4 **Distinguish** between a traditional and flat organisational structure.
5 **Define** the term 'business culture'.
6 **Describe** the culture of your school.
7 **How** can business culture influence the success of a business?
8 Briefly **explain** how a manager can influence a business's culture.
9 **Summarise** the four elements of a business culture.

EXERCISE 3.2 EXTENSION

1 **Analyse** the relationship between a business's structure and its culture.
2 **Determine** how the choice of a good or service that a business sells will influence the business's legal structure, size and operations.

3.5 Stakeholders

BizWORD

A **stakeholder** *is any group or individual who has an interest in or is affected by the activities of a business.*

Businesses have many **stakeholders**: the people and groups that interact in some way with the business and have a vested interest in its activities. In this sense you are a stakeholder of your school.

Businesses are expected to be enterprising, to comply with the law, and be socially just and ecologically sustainable in their operations. They are expected to practise ethical management and do the 'right' thing in the interests of all stakeholders.

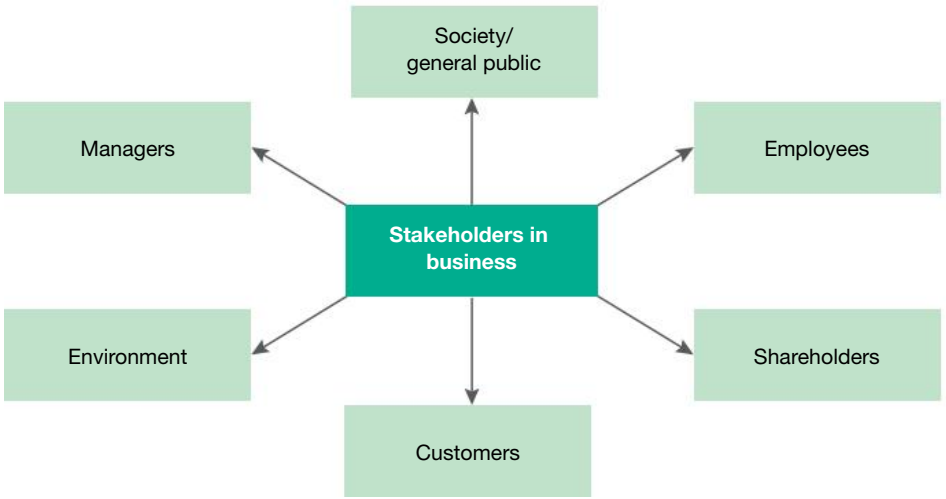


FIGURE 3.28 The main stakeholders of a business

Many businesses are now extremely sensitive to public opinion and strive to be recognised as being good corporate citizens. Businesses recognise that they increase their chances of success when they pursue goals that align with the interests and expectations of their main stakeholders. Every business must be aware of and take into account the needs of the stakeholders.

BizFACT

Presently, 36 per cent of the Australian population own shares. Forty-three per cent of those who have invested in shares are women and only 15 per cent of 18- to 24-year-olds own shares. Most Australians prefer to invest in local shares; just 5 per cent of shareholders have invested in foreign shares.

3.5.1 Shareholders

Shareholders purchase shares in a company, so they are partial owners. Shareholders have a direct influence on a business because they have voting rights on major business decisions. In addition, companies have a duty to hold an annual general meeting where shareholders are able to voice their concerns and are given an opportunity to ask questions of the Board of Directors. Major shareholders can therefore impact on major decisions.

Companies with shareholders also have to ensure that they maximise the return on the shareholders' investment in a sustainable way. Shareholders want the organisation they have invested in to be profitable as they receive a proportion of the profits (called dividends). They also make a capital gain if the value of an organsation's shares increases.

Since shareholders desire immediate returns and profits, managers of public companies usually feel greater pressure to generate revenue quickly. Shareholders will therefore influence managers' decisions and can affect the growth or long-term expansion plans of a company.

3.5.2 Managers

Managers obviously have a major influence on the business. Management has the responsibility of running a profitable or successful organisation. Most managers today understand that ethical and socially responsible activities should lead to increased sales. There are many complex legal issues that managers must understand and contend with today and it is their responsibility to introduce the policies and procedures that will affect the workplace.

A manager's approach or leadership style can have a major influence on employees and their productivity. This will affect the culture of the business and can impact on employee morale.

3.5.3 Employees

Employees are vital to an organisation as they manufacture or produce the product the organisation sells. Employees will influence businesses since the quality of the product depends on their skill and committment to the process. When employees are valued, paid fairly, trained properly and treated ethically, they will be become more valuable to the organisation. If organisations can provide for their needs, employees will be more inclined to put effort into work tasks and will be motivated to meet customer expectations.



FIGURE 3.29 Employees need to feel valued and know that their job is secure in the long term. Employees need a safe and psychologically rewarding work environment. Such an environment would respect individual differences and be concerned for employees' goals, aspirations and welfare. In this sense it is more than just providing a 'pay packet'.

Case study: FedEx cares

FedEx Express is a well-known transportation company, delivering packages all over the world. FedEx Express employs more than 300 000 people — that is a lot of employees to keep satisfied. Nevertheless, FedEx has gained a reputation as a great place to work.

According to Kim Garner, FedEx Express Australasia's managing director, employees are encouraged to excel and contribute to the company. FedEx has a strong people culture; this means that employees are valued and management works towards creating a supportive workplace culture that develops talent.

'At FedEx, our people are the heart and soul of our business. This is why our founding People–Service–Profit (PSP) philosophy is based on the premise that if we take care of our people, they will take care of our customers, and that will take care of our profit', says Garner. 'Our focus has been on our people since we began our operations and our ongoing commitment to building a positive working environment at FedEx through a combination of leadership development and training programs which make our employees feel valued and engaged.'

FedEx has frequently been recognised for its people-first culture, including an Australian HR Award for employer of choice. The company values its diverse workforce and is a supporter of gender equality, mature workers and advancement of women in the workplace.

SNAPSHOT QUESTIONS

1. **Outline** how FedEx improves employee satisfaction.
2. **Explain** FedEx's People–Service–Profit (PSP) philosophy.
3. **Describe** how FedEx builds a positive working environment.

SNAPSHOT



'… FedEx has gained a reputation as a great place to work.'

3.5.4 Customers

Successful businesses know that the consumer is a powerful stakeholder in the external operating environment. Today's consumers are astute, better educated and informed. They are increasingly prepared to seek compensation if they believe they have either been unfairly treated or purchased a product that did not perform as promised. Consumer groups are also prepared to mount publicity campaigns aimed at embarrassing those businesses that do not act ethically or responsibly.

One recent example was the consumer backlash against a manufacturer of sports shoes that was perceived to be exploiting cheap labour in a developing country. Consumers are increasingly putting pressure on businesses (through their spending decisions) to be environmentally aware, demanding products that are 'clean, green and safe'. Examples include recycling, environmentally friendly packaging, reduced packaging and lower factory emissions. An example of consumer power was the pressure put on supermarkets to phase out plastic bags.

BizFACT

Many businesses are changing their operations in order to meet customer expectations and help protect the natural environment. As part of its corporate sustainability strategy, Virgin Australia minimises the environmental impact of its business by offering customers the opportunity to offset carbon emissions on their flight. Under this program, the customer's seat emissions are calculated and an equivalent amount of carbon offset credits are purchased, directly supporting the preservation of Tasmania's native forests.



FIGURE 3.30 In 2016, two major milk processors, Murray Goulburn and Fonterra, slashed the price they paid dairy farmers for their milk, which resulted in many farmers being paid below the cost of production. To show their support for Australian dairy farmers, consumers across the nation boycotted the $1-a-litre supermarket private label milk and switched to premium milk brands. Consumers were willing to spend an extra 90c per litre in an effort to support struggling dairy farmers.

To ensure its future viability and profitability, a business needs to recognise and assess changes in consumer tastes so it can constantly satisfy the consumers' needs and wants.

3.5.5 Society

BizFACT

Since 2005, Toronto-based magazine and research firm Corporate Knights has put together the Global 100, an annual list of the world's most sustainable companies. In the 2017 Global 100 list, two Australian companies featured: CBA was ranked 6th and NAB 50th.

Members of the community increasingly expect organisations to show concern for the environment. Some might be worried about organisations using valuable land resources or showing disregard for carbon emissions. They may be concerned about waste disposal or pollution. Others may be concerned about their future welfare through their own employment within organisations.

Therefore, socially responsible businesses will participate in a range of community projects and activities. For example, The Body Shop organises for its employees to assist with a local charity of their choice. AGL Limited supports a range of educational, fundraising and social welfare programs.



FIGURE 3.31 NAB has been recognised as one of Australia's best performing companies in terms of ethical business strategies. The company aims 'to make a positive and sustainable impact on the lives of customers, people, shareholders, communities, and on the environment' in which they operate. Some recent highlights include spending $7.3 billion in financing activities to address climate change, and $48.9 million in community investment, and the contribution of 23 000 volunteer days by their employees.

3.5.6 Environment

BizWORD

Ecological sustainability *occurs when economic growth meets the needs of the present population without endangering the ability of future generations to meet their needs.*

There is growing pressure for businesses to adopt **ecologically sustainable** operating practices. This is in response to concerns about climate change and the destruction of the natural environment. Concern for our environment operates at both the local level as well as on a global scale.

Over the last two decades, the business community has undertaken many initiatives to put the principle of sustainable development into practice. For example, the jeans manufacturer Levi Strauss and Co. has developed its own environmental philosophy and guiding principles. Levi Strauss will conduct business only with partners who share its commitment to the environment.

BizFACT

The Australian Business Award for Sustainability recognises organisations that execute initiatives demonstrating leadership and commitment to sustainable business practices. The companies that were recognised in 2017 were Blackmores Limited, Fujitsu Australia, GJK Facility Services, Macarthur Centre for Sustainable Living, Pacifico and Paintback Limited.

Businesses that have been successful in their environmental management have learned that new processes, procedures and strategies are often needed. For example, one particular organisational element that many proactive 'green' companies share is the development and implementation of an environmental policy.

Through communication and training, responsible businesses can ensure that all employees and contractors are environmentally aware.

SUMMARY

- Businesses have many stakeholders that will influence their operations.
- Shareholders have a direct influence on a business because they have voting rights on major business decisions.

- Companies need to ensure that they maximise returns on their shareholders' investments.
- Managers will influence organisational policies and procedures as well as employees' productivity.
- Employees will influence the quality of an organisation's products.
- To ensure its future viability, a business should consider the needs of their customers.
- Members of the community increasingly expect organisations to show concern for the environment and to be socially responsible.
- There is growing pressure for businesses to adopt ecologically sustainable operating practices.

EXERCISE 3.3 REVISION

1. **Define** the term 'stakeholders'.
2. **Identify** the stakeholders of your school. **Outline** the influence each of these stakeholders has on the school.
3. Are a shareholder and a stakeholder the same thing? **Explain** your answer.
4. **Outline** the influence managers have on a business.
5. 'Employees are the most valuable resource of any business.' **Discuss** the accuracy of this statement.
6. 'Businesses that respect and satisfy their customers have a much greater chance of success.' **Explain** why this is so.
7. **Examine** the **NAB** website and **outline** some of the approaches the company has taken towards corporate responsibility.
8. **Define** the term 'ecological sustainability'.
9. In small groups, use the brainstorm technique to **identify** reasons businesses should adopt ecologically sustainable operating practices. Share your answer with the rest of the class.
10. Use a table like the one below to **summarise** a business's main stakeholders and their influence.

Stakeholder	Influence

on Resources

Weblink: NAB

EXERCISE 3.3 EXTENSION

1. 'The shareholder should take precedence over all the other stakeholders. They are the ones who have invested their money; they take the risks. Therefore, they should be rewarded with as high a return as possible.' **Evaluate** this statement. **Compare** your answers with other members of the class.
2. **Examine** the role of Fair Wear and **assess** its role in improving workplace conditions. Use the **Fair Wear** weblink in the Resources tab to help you.
3. What do you think motivates a business to engage in socially responsible business programs? Is it:
   (a) altruism — an unselfish concern for others?
   (b) enlightened self-interest?
   (c) avoidance of government regulation?
   (d) fear of being sued?

   Justify why you chose the one you did. Share your answer with other class members.

on Resources

Weblink: Fair Wear

Digital doc: Chapter summary (doc-26095)

Interactivity: Chapter crossword (int-7215)

Interactivity: Multiple choice quiz (int-7216)

CHAPTER 4

Business growth and decline

OVERVIEW

4.1 Introduction
4.2 Business life cycle — stages and responding to challenges
4.3 Factors that can contribute to business decline
4.4 Voluntary and involuntary cessation

4.1 Introduction

Businesses are similar to people in that:

- no two are identical
- each has its own identity
- they are referred to by name or brand
- they possess individual personalities and physical appearances
- they are confronted by life's challenges
- they sometimes succeed and at other times fail
- they rely on each other for survival.

However, the most striking similarity is that, like people, a business will pass through a number of distinct stages as it develops. This is referred to as the **business life cycle**. The business life cycle is a model; that is, a simplified version of 'real-life' situations. Using a model makes it easier to understand the complexities of the business world. The four main stages in the life cycle of a business are shown in figure 4.1.

BizWORD

The **business life cycle** *refers to the stages of growth and development a business can experience.*

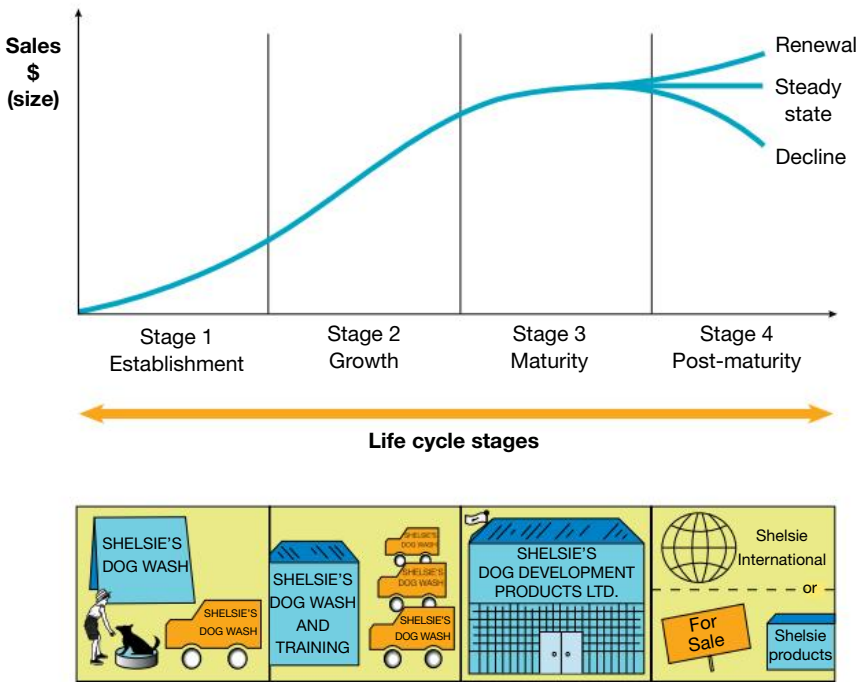


FIGURE 4.1 The four stages of the business life cycle. The graph shows a smooth line with sales increasing up to the post-maturity stage. In reality, the growth in sales will usually show minor increases and decreases within each stage. The line we have drawn represents the average sales changes.

In each stage of the cycle a business is confronted with new challenges — as well as being presented with different opportunities. The nature, operation and organisation of the business changes as the business progresses from one stage to the next. As this occurs, the business owners need to constantly develop strategies to deal with its expansion. To do this successfully, owners must continually assess the business's position on the life cycle. This is important, otherwise inappropriate strategies will be put in place and jeopardise the 'life' of the business. However, the reality is that it can often be difficult for owners to determine their position on the life cycle because they fail to recognise the changes taking place.

There is one very important difference between the human and business life cycles — with the business life cycle, there is no set time limit for each of the stages. For example, some businesses can reach maturity in a short period of time, whereas another business may take decades to move beyond the establishment stage.

Some businesses are able to constantly renew themselves over a long period of time. As they do so, they continually grow and expand, often becoming dominant within their specific market.

BizFACT

Using a life cycle model helps in understanding how the business changes over time.



FIGURE 4.2 Fairfax Media Ltd constantly implements strategies to renew the business in order to adapt to changes in the external business environment. Over a decade ago, 80 per cent of their revenue came from two newspapers — the *Sydney Morning Herald* and *The Age*. When management noticed a decline in print media which was affecting their revenue, they decided to restructure their business model and diversify by investing in digital media as well as radio brands.

Occasionally businesses run into financial difficulty and are forced to restructure. Some of Australia's large businesses, such as Coles, have followed this pattern (see the following Snapshot).

SNAPSHOT

Case study: The life of Coles — a constantly renewed business

Consider the variety of stores located in your local shopping complex. There will probably be a Coles, a Kmart or Target variety store, and perhaps a Liquorland outlet or Officeworks shop. All of these businesses were once part of the Coles Group.

Coles: early beginnings

For almost one hundred years, Coles has had a rich history in Australia. Coles, one of Australia's largest retailers, traces its origins back to a small business retailer.

The first G. J. Coles variety store was opened in Collingwood, Victoria, in 1914 by Mr GJ Coles and his brother Mr JS Coles. It employed six staff. A particular feature of the store's pricing policy was that no item on sale would cost more than one shilling (equivalent to ten cents). Over the ensuing years both businesses expanded and prospered.





By the mid 1920s Coles had opened its Bourke Street, Melbourne, store. The business developed successful marketing strategies and offered a wide range of products that satisfied the tastes and preferences of their customers.

During the Great Depression of the 1930s Coles continued to grow. Sales increased as their products were offered at affordable prices to a large range of customers. Its success reflected the philosophy of its managing director of the time, Sir AW Coles, who wrote, 'A store has no right to succeed just because it is open for business and has a bright display. The goods must reflect the wishes of the community in which the store is located.'

Post–World War II growth

After World War II, Coles consolidated its position within the Australian retail industry by acquiring a number of department, chain and grocery stores in other states.

- In 1960 Coles opened Australia's first supermarket.
- In 1969 Coles established Australia's first discount store, Kmart.
- By 1975 Coles, with 559 stores and 36 000 staff, became the first Australian retailer to achieve more than $1 billion of sales in a single year.
- In 1978 Coles became the second largest private employer of labour in Australia, with more than 50 000 employees.
- In 1982 Coles developed the discount store concept further: it opened its first Super Kmart store.



Coles–Myer merger

In 1985 Coles and Myer — a major retailer that had started in Melbourne in 1900 — merged to form one company — Coles Myer Limited. After the merger the business continued to grow, introducing new retailing strategies such as EFTPOS and Fly Buys, and developing a number of concept stores such as Officeworks and Harris Technology.

At its peak, Coles Myer Limited was Australia's biggest retailer with 1900 stores throughout Australia and New Zealand, and was Australia' largest single employer with 165 000 employees.

During the late 1990s and early 2000s, Coles Myer Limited encountered trading difficulties and was underperforming due to senior management difficulties, IT and supply problems, and too much of an overlap between each division, resulting in them competing for the same market share. For example, Target and Kmart attracted a similar type of customer, as did Myers and Grace Bros. (Myer bought Grace Bros Holding Limited in 1983.)

Wesfarmers takeover

In 2006 the Coles Myer Limited board finally accepted that the mega-merger had failed and sold the Myer chain to a consortium led by private equity firm Texas Pacific Group Capital, with Blum Capital and the Myer Family Company Pty Ltd.

Following the de-merger, the Coles group continued to struggle against its main rival, Woolworths Limited. Its financial performance deteriorated with a resultant fall in profits. It was ripe for a takeover (acquisition), which occurred in late 2007 when the Perth-based conglomerate Wesfarmers — one of Australia's largest public companies — paid $22 billion to buy the Coles retail empire. At the time, this was the largest takeover in Australian history.

Over the past few years, Wesfarmers has been successful in turning around the performance of the Coles division, largely due to improvements in the performance of Target and the Coles supermarket chain. It has streamlined the supermarket division by selling 45 Coles stores and eight Liquorland outlets to the independent grocer FoodWorks for $35 million. The sale was part of Wesfarmer's five-year plan to improve its network of over 800 supermarkets and more than 600 Liquorland stores.

Today, Coles is a leader in Australian food retailing, with more than 102 000 employees and over 21 million customer transactions a week.



'Today, Coles is a leader in Australian food retailing, with more than 102 000 employees and over 21 million customer transactions a week.'

SNAPSHOT QUESTIONS

1. **Identify** the main reasons for the success of Coles up to the 1920s.
2. Many businesses failed during the 1930s Great Depression. **Clarify** why Coles was able to not only survive but prosper.

3. **Describe** the term 'merger'.
4. (a) **Outline** what new
   (i) retail strategies and
   (ii) concept stores were introduced after the merger with Myer.
   (b) **Propose** the reasons for the introduction of these changes.
5. **State** the main reasons for the merged company's underperformance.
6. **Describe** the term 'takeover' (acquisition).
7. **Outline** the strategies Wesfarmers used to improve the performance of Coles.
8. Go to the **Wesfarmers** website and access the Wesfarmers group structure. **Explain** the benefit for Wesfarmers in having such a diversified range of business operations.

on Resources

Weblink: Coles
Weblink: Wesfarmers

SUMMARY

- The business life cycle refers to the stages of growth and development a business can experience.
- The stages are: establishment, growth, maturity and post-maturity.
- In each stage of the cycle, a business is confronted with new challenges and presented with different opportunities.

EXERCISE 4.1 REVISION

1 **Define** business life cycle.

2 Examine figure 4.1 (page 86) and then answer the following questions.
(a) **Identify** the four stages of the business life cycle.
(b) **How** is the size of a business directly related to the amount of sales?

3 Figure 4.1 is referred to as a model. **Explain** how using models can help our understanding of the real world.

4 **State** why it is important for business owners to assess the business's position on the life cycle.

EXERCISE 4.1 EXTENSION

1 There are daily examples of businesses that have suffered because they failed to manage their growth satisfactorily.
(a) **Identify** two businesses you are aware of that have suffered because they failed to manage their growth.
(b) **Investigate** the main reasons for both their rise and decline.

2 According to Edward De Bono, 'Success in business would seem to depend much less on natural talent and a lot more on thinking and personality factors. Certainly success in business often seems spurred by a desire to make things happen.'
(a) **Justify** this statement.
(b) **Investigate** the 'thinking and personality factors' a successful businessperson would possess.

4.2 Business life cycle — stages and responding to challenges

Each stage of the business life cycle has its own special features and challenges. This section will examine the main features of each stage before considering the challenges experienced at each stage. This information will be presented in a table format to help you to compare and contrast the different stages. We will also identify actual businesses at different stages in the business life cycle and observe how they respond to the different challenges of each stage.

4.2.1 Establishment stage

The first stage in the life of a business is its birth — or establishment. Like human babies, recently established businesses are also vulnerable as their hold on 'life' is quite precarious. The overriding concern is to get the business on a solid foundation. This requires enough sales to be generated to bring in the much needed income, which will be used to pay expenses and to generate a positive **cash flow**.

BizWORD

Cash flow *is simply the money coming into the business in the form of cash receipts, and the money leaving the business as cash payments.*

The main features and associated challenges of the establishment stage are outlined in table 4.1.

Establishing a business is not always easy. A number of challenges need to be responded to at the establishment stage. To overcome these challenges, the aspiring business owner needs to become involved in some basic planning. Detailed planning undertaken when establishing the business can help greatly reduce the risk of failing and becoming just another business failure statistic. (Business planning will be examined in detail in later chapters.)

TABLE 4.1 Establishment stage: main features and associated challenges

Feature	Challenges
Alternative names	Start-up, birth, beginning, commencement
Goals	Survival, and setting a firm foundation for future growth
Sales	Normally begin slowly and are somewhat erratic
Marketing	Highlight product advantages by accentuating the product's strengths. Undertake inexpensive promotion strategies
Profit	Usually slow to begin with, occasionally a loss. Sometimes all the profits are put back into the business to ensure its survival.
Financial management	Greatest source of start-up capital is from the owner's personal savings. This can be supplemented with a loan from a financial institution, although such finance is often difficult to obtain because of the high risks involved.
Cash flow	Sometimes erratic, with a period of constant cash outflow in the early stages
Costs	Very high fixed costs. Major cost items include premises, equipment, raw materials and insurance.
Customers	Establishing a customer base large enough to sustain future viability is important. Need to develop a positive relationship with customers. Attempt to accurately forecast customers' needs.
Management	Informal, with all decisions being made by just one or two people. Decisions are often made 'on the run'.
Employees	Normally only a few. Owner establishing work routines and building up relationships
Failure rate	Very high, up to 33 per cent within the first year of trading
Main problems	Lack of money with possible cash flow shortages
Risk level	Extremely high, especially within the first few months. High degree of uncertainty
Business entity	Usually sole trader or partnership

Case study: Cav & Co. — establishment stage

Husband and wife team, Michael and Amanda Cavallaro, had a good understanding of what was required to own and operate a café. Their passion for food and years of experience working in the hospitality industry motivated them to want to own their own café.

Michael is a carpenter by trade and was also a part-owner of another café in Gladesville. While Amanda started out as a full-time event manager, after she began dating Michael, she took up work in his previous café. In 2017, they decided to combine their skills and start this new business venture together.

While both owners play an equal role in management decisions, they each contribute their own specialist skills, knowledge and talents, and have their own unique role to play within the business. Michael's early experience as a carpenter meant that he was able to build and fit out the café. His previous job operating a café also enabled him to develop skills in management, as well as helping to cook and make coffees. Amanda's work history has also enabled her to gain the skills necessary to successfully manage the café, organise the staff roster and take care of the business's marketing.

The couple decided to form a private company, as opposed to a partnership, so that they would benefit from the protection given by limited liability. They did not want to be personally liable for the financial obligations of the business and put their personal assets at risk.

After completing some market research and preparing a comprehensive business plan, Michael and Amanda organised a bank loan to help fund their venture. They then found a vacant shop in the heart of Gladesville that they thought would be perfect for their café. Amanda and Michael sought legal advice to assist them in negotiating the lease; however, this process took quite some time. After a few weeks, the lessor eventually accepted the provision to give them a rent-free period while the café was being built and so the lease was signed. It also took quite some time to gain council development approval and to design the café. Within a few months, however, thanks to Michael's carpentry skills, the shop was revamped into a modern-looking café.

Before they commenced operations, Amanda and Michael also had to recruit and select capable employees to assist them in the café. Prior to recruitment, they determined the exact qualifications and skills they were looking for. They then placed advertisements for both chefs and wait staff on various websites. Once a number of applicants had applied, they carried out interviews to determine the best candidates to hire.

The first few months were hard. They opened the doors on the 17th June 2017 and found trade to be a little slow because many people were not yet aware of the business. It took a few months for sales to pick up and for the business to generate a positive cash flow. Their biggest challenge, however, was getting to know the needs of their target market, determining what foods were popular and forecasting the correct quantity of each food item they should supply, since everything is made fresh on the premises daily.

The owners didn't have a lot of funds to spend on marketing, so they undertook inexpensive forms of promotion to draw customers in. They had posters on the shop windows during the building process and relied extensively on social media advertising (mainly through Facebook and Instagram) to generate awareness.

After those initial months, their sales and profits have been gradually increasing and the business is beginning to generate a good reputation in the area. Their skills, experiences and delicious produce have put the business on a firm foundation.

Source: Amanda Cavallaro

SNAPSHOT QUESTIONS

1. **Outline** what motivated Amanda and Michael to start their own business.
2. **Why** did they decide to form a private company?
3. **Describe** the challenges faced by the owners during the establishment phase.
4. **Deduce** the factors that have contributed to the business's success.

SNAPSHOT



"Their skills, experiences and delicious produce have put the business on a firm foundation."

SUMMARY

- The main challenge at the establishment stage is to get the business on a solid foundation by generating enough sales to create a positive cash flow.
- Detailed planning can help greatly reduce the risk of failing.
- Small businesses, such as a sole trader or partnership, have unlimited liability: that is, the business owner is personally responsible for all the debts of his or her business.

4.2.2 Growth stage

BizFACT

During the growth phase it becomes essential for the business owner to develop long-term plans.

The second stage is a time of accelerating growth. Sales increase and the cash flow is normally positive. A customer base has been established with regular clients accounting for a large percentage of total sales. The business undertakes the development of new products to satisfy different market segments. More emphasis is placed on marketing and the use of complex computerised accounting procedures. In family owned businesses, other members of the family usually take up specialised supervisory and management roles. Loyalty to the business is strong, with many of these businesses taking on the culture of an extended family. The business has a good reputation in the community, and owners develop a sense of pride in the products and personal service on which the business has built and flourished. However, with growth comes complexity, responsibility and the need for long-term planning.



FIGURE 4.3 Since entering Australia in 2009, Costco Australia has experienced significant growth especially over the past couple of years. In 2015 their revenue jumped 50 per cent to $1.52 billion as sales grew at their existing stores and the company opened new stores taking their network of stores to nine. Sales almost doubled between 2013 and 2015, outpacing the growth of other supermarket chains. They are currently looking to increase their online presence in response to the arrival of Amazon.

The main features and associated challenges of the growth stage are outlined in table 4.2.

TABLE 4.2 Growth stage: main features and associated challenges

Feature	Challenges
Alternative names	Take-off, growth spurt
Goals	To constantly increase the average level of sales; to continue growing through mergers and takeovers; to diversify business activities
Sales	Rapid increase, especially in the early stages of the growth phase. New products introduced and some slow-selling products deleted
Marketing	Development of new products to satisfy market niches. Price discounts due to lower production costs. Extensive promotional activities and a widening distribution network. Desire to increase market share by using mass-marketing techniques
Profit	Should increase due to rising sales and falling production costs. As well, profits of other businesses acquired through acquisition (takeover) or merger are available for use.
Financial management	Use of sophisticated, computerised accounting procedures and systems. Raising of finance tends to be easier. Main sources of finances are from financial institutions, the selling of shares or taking on more partners.
Cash flow	Difficulties can be experienced if the growth is too rapid. Adequate cash flow must be maintained to continue expansion. A credit policy needs to be organised. Forecasting of sales and expenditures becomes more crucial.
Costs	Production costs tend to decrease due to economies of scale — that is, cheaper unit costs due to larger production runs. Business becomes more efficient in areas of administration, finance and production.
Customers	Concentration on satisfying existing customer base while at the same time tapping into new market, both domestic and overseas. Mass markets become a possibility.
Management	Delegation of some responsibilities. Development of a formalised organisational structure. Introduction of line managers (supervisors). Clear lines of communication become essential. Specialist departments are established. Some functions may be outsourced.
Employees	Increased specialisation of workforce requiring formal and informal training. Human resource strategies need to be implemented, especially in compiling job analyses and descriptions.
Failure rate	Lessened, especially after successful mergers or takeovers, which result in increased diversification and reduced competition
Main problems	Expanding too rapidly and therefore losing control of the business's direction. Moving away from the core business activities — that is, what the business originally produced. Business may not have enough experience in the new areas. The need for finance to continue with the growth
Risk level	Reduced, due to diversification and less competition. However, if borrowings increased too rapidly the business may leave itself exposed — that is, with liabilities far greater than its assets.
Business entity	Usually some form of incorporated entity; private or public company

on Resources

eLesson: Wildbreads (eles-2307)

eLesson: Stuck on You (eles-0835)

SNAPSHOT



'… went from being flat broke to turning over $32 million …'

Case study: Flip Out — growth stage

Flip Out Trampoline Arena is Australia's first and largest trampoline playground. The company began in 2012, a time when the owner Brent Grundy was so desperate for income that he couldn't even afford to buy Christmas presents for his children.

The idea for the business came about while Grundy was with his kids in a play centre. While he was there, he noticed that half of the play centre was full of children that were either too big for the equipment or waiting for a turn; and many parents and guardians looked bored. This inspired him to create a facility that would not only entertain kids of all ages but also adults. Grundy then came up with the idea to start up trampoline centres not only in Australia, but also around the world. And he did. Within the next 24 hours, Grundy sketched a trampoline park to accommodate 300 jumpers and contacted a manufacturer.

He opened his first arena on Christmas Eve 2012 in the car park of the Penrith Panthers Leagues Club. This first centre was built by family and friends. In the first day of trading alone, 150 kids passed through. Not long after, Flip Out moved to an indoor venue and within just 10 weeks of operation, the company hit a six-figure turnover, making $2.5 million in the first year. By the time he started two centres, he had enough cash to buy the third and the company snowballed from there.

In the two-and-a-half years since launching Flip Out, Grundy continued to achieve significant growth and unprecedented success. In just two years, Grundy went from being flat broke to turning over $32 million using franchising as his business expansion strategy. While still a young company, he has now expanded to 35 locations in Australia and around the world and has over 800 employees. There are currently 13 Flip Out franchises overseas, including in China, Malaysia, Saudi Arabia, Scotland, Taiwan and Afghanistan to name a few.

Over the last two years, two main competitors have entered the market; however, Grundy does not perceive them as a threat. Furthermore, some franchises in Australia have suffered big financial losses due to a variety of factors. None of this has deterred Grundy, who plans to have 800 trampoline centres around the world by the end of 2018.

SNAPSHOT QUESTIONS

1. **Outline** the source of the business idea.
2. **Identify** the characteristics that indicate that Flip Out is in the growth stage of the business life cycle.
3. **Describe** the external factors in the business environment that have had an influence on this business.
4. **Extrapolate** the factors you believe have been instrumental to Flip Out's growth.

During the growth stage the business must continually improve its competitive edge. Failure to do so will see competitors take away customers and the growth will stall. Owners tread a fine line in attempting to do this — a desire not to radically alter a successful formula while at the same time restructuring sufficiently to match what the competitors are doing.

Business growth and expansion can occur in a number of ways. One method frequently used is to integrate with other businesses through a merger or an acquisition (takeover) (see figure 4.4).

A **merger** occurs when the owners of two separate businesses agree to combine their resources and form a new organisation. An **acquisition** (takeover) occurs when one business takes control of another business by purchasing a controlling interest in it.

Sometimes a merger or acquisition is motivated by the desire for a business to continually expand its range of products. No product will last forever; eventually, it will become obsolete. A merger or acquisition is often an effective way a company can quickly increase its range of products. At other times, a merger or acquisition is undertaken to eliminate competition in the marketplace.

BizWORD

*A **merger** occurs when the owners of two separate businesses agree to combine their resources and form a new organisation.*

*An **acquisition** (takeover) occurs when one business takes control of another business by purchasing a controlling interest in it.*

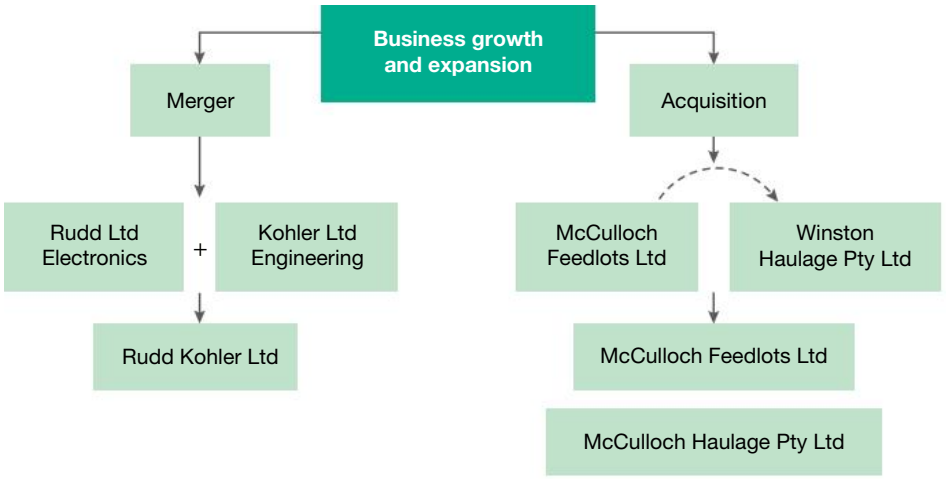


FIGURE 4.4 Methods of business expansion: merger and acquisition (takeover)

There are several different types of mergers or acquisitions. Three types are described below.

- **Vertical integration** occurs when a business expands at different but related levels in the production and marketing of a product.
  - When a business integrates with one of its suppliers this is referred to as backward vertical integration; for example, if a bakery acquires a wheat farm.
  - Forward vertical integration is when a business integrates with a firm it sells to. For example, the bakery could merge with a supermarket chain that sells its bread (see figure 4.5).
- **Horizontal integration** occurs when a business acquires or merges with another firm that makes and sells similar products; for example, if a bakery merges with or is acquired by another bakery (see figure 4.5).

BizWORD

Vertical integration *occurs when a business expands at different but related levels in the production and marketing of a product.*

Horizontal integration *occurs when a business acquires or merges with another firm that makes and sells similar products.*

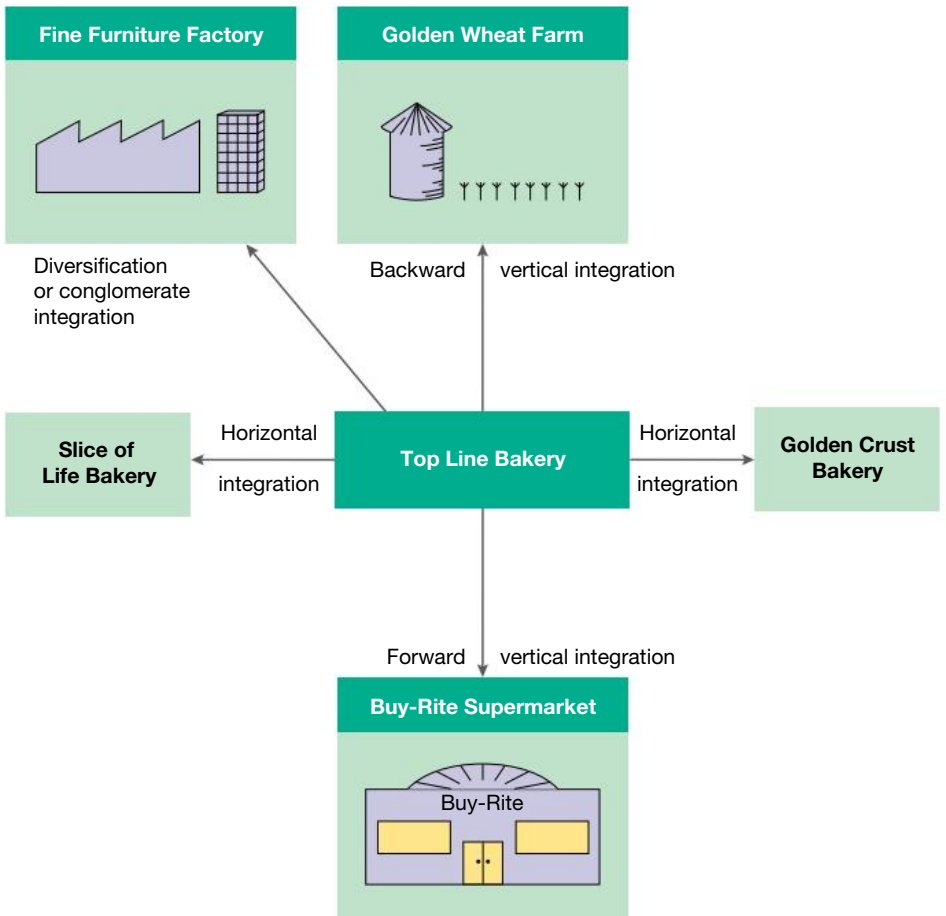


FIGURE 4.5 Types of integration: backward and forward vertical integration, horizontal integration and diversification

BizWORD

Diversification *(or conglomerate integration) occurs when a business acquires or merges with a business in a completely unrelated industry.*

- **Diversification** (or conglomerate integration) occurs when a business acquires or merges with a business in a completely unrelated industry. For example, diversification occurs if a bakery merges with a furniture manufacturer (see figure 4.5).

SUMMARY

- During the growth stage the business has increased sales, a regular customer base, develops new products and improves its cash flow.
- With growth comes complexity and responsibility, which creates the need for long-term planning.
- Growth and expansion can occur either through a merger or acquisition (takeover).
- A merger occurs when the owners of two separate businesses agree to combine their resources and form a new organisation.
- An acquisition (takeover) occurs when one business takes control of another business by purchasing a controlling interest in it.
- Vertical integration occurs when a business expands at different but related levels in the production and marketing of a product.
- Horizontal integration occurs when a business acquires or merges with another firm that makes and sells similar products.
- Diversification (or conglomerate integration) occurs when a business acquires or merges with a business in a completely unrelated industry.

EXERCISE 4.2 REVISION

1. **Why** is generating a positive cash flow crucial for the survival of a business at the establishment stage?
2. **Examine** table 4.1. **Construct** a mind map to show the main features of a business at the establishment stage.
3. One-third of all small businesses fail within the first year of operation. **Propose** why the failure rate is so high.
4. **Outline** three challenges that you believe to be the most serious for a business to confront while at the establishment stage. **Justify** your selection.
5. **Why** could the growth stage be a difficult stage to manage effectively?
6. **Examine** table 4.2. **Construct** a concept map to show the main features of a business at the growth stage.
7. **Outline** three challenges that you believe to be the most serious for a business to confront at the growth stage. **Justify** your selection.
8. **State** what often motivates businesses to merge or make acquisitions.
9. You are the owner of Elite Furniture, a business that makes specialty furniture. **Construct** a diagram to show how your business could expand using:
   (a) vertical (backward) integration
   (b) vertical (forward) integration
   (c) horizontal integration
   (d) diversification/conglomerate integration.

EXERCISE 4.2 EXTENSION

1. Arrange an interview with a local business owner. **Create** a two-page written or five-minute oral report. You might wish to develop your report under the following headings:
   (i) reasons for establishing the business
   (ii) brief history of the business
   (iii) success and failure along the way
   (iv) financial record keeping.

2 Are the advantages of small business really advantages? Wouldn't every small business owner like his or her business to grow into a large firm? **Discuss**.

3 **Investigate** a recent merger or acquisition. **Outline** the main objectives for the merger or acquisition.

4 'Mergers and acquisitions reduce competition in the marketplace. They may be a successful business tactic, but they leave the consumer worse off.' **Evaluate** the accuracy of this statement.

4.2.3 Maturity stage

This third stage of the business life cycle presents unique challenges to the owner. It requires a great deal of rethinking about how the business should be operated to guarantee survival. At this time, the owner realises that the business could easily lose the energy, enthusiasm and vitality of its earlier times. A sense of complacency often envelops the business, affecting both management and staff. What is now required is a more formal, professional approach to planning.

With such a realisation may come the need to completely restructure and reorganise the business, which can sometimes be quite a painful experience. The business might lose its 'family' atmosphere and be replaced with a more clinical, professional culture. The size of the business dictates a more formal organisational structure. The difficulty is to introduce these changes without destroying the entrepreneurial spirit that laid the foundation for the business's success.

However, as figure 4.1 reveals, sales are still increasing but at a slower rate. The growth stage has slowed. This is an early warning signal of imminent danger — possible decline. The main features and associated challenges of the maturity stage are outlined in table 4.3.

BizFACT

Victoria's Secret, one of the largest lingerie brands in the world, is looking to reinvent itself due to the decline in sales experienced over the last year. The brand dropped some categories like swimwear and apparel and made changes to their promotional mix in an attempt to turn its business around.

TABLE 4.3 Maturity stage: main features and associated challenges

Feature	Challenges
Alternative names	Market saturation, market hardening
Goals	To maintain profits at pre-existing levels
Sales	Rate of growth slows and eventually flattens out; plateauing.
Marketing	Maintain customer and brand loyalty through extensive advertising. Due to increased competition, relative market share may decline. Need to improve quality of products
Profit	Rate of growth slows, eventually flattening out. Reflects what is happening to the level of sales
Financial management	All the correct procedures are in place, but their efficiency needs to be improved to protect the profit margin. Finances should be devoted to advertising and development of new products.
Cash flow	If costs are not able to be controlled, then the cash flow position starts to deteriorate.
Costs	Keeping costs under control is now essential. Need to improve efficiency to keep costs down, otherwise profits will start to fall even further
Customers	Due to the size of the business, customers may sense a degree of impersonality. Business is in danger of losing the personalised service that gave the business success in previous stages.
Management	Leadership is crucial. Need to redefine the business's objectives and vision. The organisation's hierarchy becomes too entrenched and unable to quickly adapt to new conditions. Many new regulations and 'red tape' that will strangle any initiative
Employees	Introduce a work team approach, devolving responsibility to employees to avoid complacency. Introduce quality programs such as total quality management or quality circles.
Failure rate	Will increase the longer the business takes to react and reverse plateauing sales
Main problems	Rate of increase in sales begins to falter, sometimes flattening out. Loss of initial enthusiasm. Air of complacency starts to dominate.
Risk level	If costs are not controlled and management becomes slow to respond to market demand, then cash flow falls and the level of risk increases.
Business entity	Normally, no change in the beginning although, if the situation deteriorates, parts of the business may be sold off. Program of downsizing and selling off non-core business activities

SNAPSHOT



'… the slide in profits … has arisen from competing online streaming service providers.'

Case study: Foxtel — maturity stage

Foxtel is one of Australia's most dynamic media companies, delivering a diverse subscription television service to viewers around the nation. The company began as a venture between News Corporation and Telstra in 1995, offering a 20-channel service.

Subscription has increased gradually since its inception and in 1998 Foxtel's main competitor, Australis Media, the owner of a satellite television service known as Galaxy, was declared insolvent. Foxtel was therefore able to significantly boost their customer base by acquiring Galaxy subscribers.

Foxtel announced its maiden annual profit of $4 million in 2006, more than 10 years after it commenced services. Just one year later, the company posted a record $76 million profit. The main contributing factor to this boost in profits was the strong subscriber growth; their customer base grew 12.4 per cent in one year to 1 443 000 subscribers. Also in 2007, Foxtel broadcast their highest-ever ratings events, including the 2007 AFC Asian Cup quarter final between Australia and Japan. This attracted approximately 419 000 viewers, which at the time, was an Australian pay TV record. This ratings record has since been eclipsed numerous times since then.

In 2008, Foxtel's penetration into Australian homes passed 30 per cent. Between 2008 and 2014, Foxtel branched out into a variety of new services and offerings, which enabled it to increase its subscriber base and revenue.

For example:

- In 2009, Foxtel released an additional 25 channels consisting of high definition channels, movie and theme channels. They also began broadcasting free-to-air channels.
- In 2010, Foxtel and Microsoft announced a new way of receiving Foxtel through Xbox LIVE. This new service offered over 30 channels and an additional 12 video-on-demand channels. Foxtel On Demand was also introduced this year.
- In 2011, the company launched Foxtel on T-Box and they acquired Austar, a company that provided subscription television services to 2.4 million households in regional and rural areas of Australia. This resulted in Foxtel becoming Australia's largest pay television operator, with programming available to over 70 per cent of Australian homes. Their number of subscribers increased to over 1.65 million.
- In 2012, Fox Sports and Channel Nine retained the broadcasting rights to the NRL (and eventually the AFL) with the signing of a $1.025 billion, five-year deal.
- In 2014, Foxtel added two new SD channels and nine new HD channels. They also began offering broadband and phone services, which enables subscribers to access live and on-demand content through the internet on various devices via the Foxtel app 'Foxtel Go'.

In 2014, Foxtel slashed their monthly rates in anticipation of Netflix entering the Australian market in 2015. This led to an increase of 230 000 new subscribers (a 9 per cent increase). Despite this aggressive pricing strategy, many customers began switching to on-demand streaming services Netflix and Stan.

In 2015, Foxtel reached its peak of 2.9 million subscribers; however, their revenue fell by $239 million and their profit was down $72 million. This was mainly due to approximately 100 000 subscribers ending their subscription throughout the year. Their total number of subscribers dropped to 2.8 million by December 2016. During that same period, Netflix attracted over 1.8 million viewers after just one year in Australia. This put Foxtel under significant pressure for customers and viewers.

In 2016 Foxtel conducted a review of their business to ensure the company was as efficient as possible. As a result of increased digital competition, the company implemented a number of structural changes, which resulted in some staff being made redundant. In 2017, Foxtel's revenue fell 3 per cent. Only time will tell if the company can stem the slide in profits that has arisen from competing online streaming service providers.

SNAPSHOT QUESTIONS

1. **Why** has Foxtel's rate of growth slowed?
2. **Outline** the strategies Foxtel has implemented to help respond to the challenges it faces.
3. **Propose** other strategies Foxtel could implement to boost sales.

SUMMARY

- The maturity stage requires a more professional approach to planning.
- In the maturity stage, the rate of growth slows and eventually flattens out; an early warning sign of possible decline.
- A sense of complacency often envelops the business.
- Managers may need to restructure or reorganise the business.

4.2.4 Post-maturity stage

Once a business reaches this, the final stage, it is faced with three possible outcomes, these being:

1. *Steady state* — the business continues to operate at the level it has been during the maturity phase
2. *Decline* — falling sales and profits ultimately resulting in business failure
3. *Renewal* — increasing sales and profits due to new growth areas.

The post-maturity stage represents many opportunities but also many threats. The decisions made by the owner will be crucial for the future survival of the business. By constantly monitoring the business environment, the business owner should be able to select the most appropriate path for the business to take.

Steady state

A business in a steady state is neither declining nor expanding. It is much like an aeroplane flying in a holding pattern. Such a business is satisfying customer demand and maintaining profit levels. It displays some of the characteristics of a business in the maturity stage. One significant difference, however, is that it does not continue expenditure on research and development. The owner is more content to produce what it has in the past and rely on marketing replacement products.

However, just as an aeroplane cannot maintain this position forever, neither can a business. Eventually the business environment will change and the business will be adversely affected. Perhaps customers' tastes change or new competitors enter the market with superior products, or more efficient methods of production and cheaper products. Ultimately, this steady state becomes very unstable and the business stagnates. It eventually loses sales and its competitive edge. When this occurs, the business enters another stage of the business life cycle — decline.

Decline

As customers stop buying the business's products the cash flow will be seriously affected. Eventually profits will also decline. This process of decline becomes difficult to reverse for the following reasons:

1. It becomes difficult to borrow money because financial institutions are reluctant to lend money to high-risk businesses.
2. Suppliers will restrict their credit facilities and may insist on cash payments.
3. Products become obsolete, leaving the business with unsold stock.
4. Well-qualified employees may begin to leave and seek better opportunities.

The longer the business attempts to 'stagger on', lurching from one crisis to the next, the greater the risk of failing and ceasing operations — cessation. We will examine the procedures involved in voluntary and involuntary cessation at the end of this chapter.



FIGURE 4.6 The Reject Shop experienced a fall in sales of 4 per cent as well as a 28 per cent drop in net profit in 2017. This decline has been attributed to weak consumer confidence, problems with their merchandising strategy, as well as the chain finding it difficult to compete with supermarkets and department stores on everyday household items.

BizFACT

Lego experienced declining revenue and profits due to the increasingly competitive toy market, with more children using mobile devices for entertainment. To counteract this, Lego has implemented a variety of strategies to bring the company into renewal: they have restructured and slashed jobs, signed licensing agreements with brands like Harry Potter and Star Wars, and entered into the film industry. The CEO believes it will take about two years for the business to return to growth.

Renewal

Business decline can be avoided by carefully planned strategies that result in new markets being tapped and satisfying previously unmet demand. The business undergoes a revival. Sales, cash flow and profits all begin to increase once again. Even a business in decline can be turned around and placed on a path of renewal. It is very difficult to accomplish and takes an enormous effort by both owners and employees, but it is possible.

The key to achieving a long-term, sustainable recovery in sales is to focus production on what the customers are presently demanding — even if this means abandoning once-successful products. As well, an extensive market research program needs to be undertaken to assist in the forecasting of future consumer trends. The more successful the forecasting, the more able the business is to be *proactive*; that is, it can anticipate and plan for future changes. Businesses that tend to be *reactive*; that is, respond to changes after they have occurred, usually respond too late and lose valuable market share. Renewal is as much about planning and timing as it is about successful marketing strategies.

The main features and associated challenges of the post-maturity stage of renewal are outlined in table 4.4.

TABLE 4.4 Post-maturity stage — renewal. Main features and associated challenges

Feature	Challenges
Alternative names	Regeneration, revival
Goals	To increase sales, cash flow and profits. Seek out and exploit previously unmet demand in new markets. Undertake further diversification and integration. Sell off any unprofitable non–corerelated activities or assets.
Sales	Increase over time, especially as newer products are brought onto the market and new markets exploited
Marketing	Conduct market research analysis to determine customers' wants and identify any changes. Advertise in new market areas. Identify new market niches.
Profit	Will improve over the long term, reaching higher levels than previously achieved

Feature	Challenges
Financial management	May need to issue new shares to raise finance to assist with research and development
Cash flow	May decline in the short term as money is spent on research and development of new products and markets
Costs	Research and development, marketing, integration and restructuring costs will be high in the short term.
Customers	New markets exploited; explore possibility of exporting
Management	Implement an organisational development program to realign the objectives, vision statement and organisational structure so it fits in with the new environment.
Employees	Open and honest communication is essential. Employees need to be fully aware of where the business is headed, how the new goals are to be achieved and how individual jobs may be affected. Need to overcome possible resistance to change
Failure rate	Has been lessened compared to the maintaining or steady state phase
Main problems	Anticipated sales may not eventuate due to inaccurate forecasts, poor timing or inappropriate marketing strategies. Initial costs are high, with cash flow shortfalls in the short term. Employees may become disenchanted with the restructuring and having to adapt to constant change.
Risk level	Undertaking any new strategy involves some degree of risk. Risk minimisation techniques can help reduce the exposure to risk.

Case study: Kathmandu — post-maturity stage: renewal

Kathmandu is a retailer that sells travel and adventure outdoor apparel and equipment in New Zealand and Australia. The company was founded by John Pawson and Jan Cameron in 1987. They set up their first retail outlets in Australia, while manufacturing most of their original clothing in New Zealand.

For almost 30 years, the company experienced steady growth as they continually adapted their merchandise to endure different weather conditions and the ever-changing needs of travellers. During the 1990s, Kathmandu became a leader in designing products that were original, sustainable and adaptive. They invested a great deal of resources into market research and innovation and, as a result, their business grew.

By 2002, the company vertically integrated and, since then, the majority of their sales have been Kathmandu-branded products, using materials and designs sourced or created by their own employees. This enabled them to generate strong margins.

Kathmandu was acquired by a group of private equity funds in 2006. The company continued to grow during this period and that growth provided them with new opportunities. Kathmandu began their online and mail order operations in 2008, and in 2009, the company was listed on the ASX and NZX, continuing on its path of steady growth.

In 2014, however, Kathmandu reported a slowdown in sales growth in the Australian market and their shares started to drop. As a result, management began to reassess their sales and pricing strategy. The company also experienced a substantial reduction in gross profit and their net profit declined 52 per cent. Part of this was attributed to the warmer start to winter, as well as aggressive discounting and the holding of excessive stock. This decline led to a multi-million-dollar takeover attempt, which was eventually dropped.

In 2015, Kathmandu posted a 51.7 per cent drop in profit due to decreasing sales, a rise in costs and a series of unsuccessful promotional strategies.

SNAPSHOT



'By 2016, the troubled retailer returned to profit.'

That year a new CEO, Xavier Simonet was appointed. Simonet reduced the number of clearance sales, as customers began expecting their clothing and accessories to frequently be on sale. Less discounting led to an improvement in gross margin. He also implemented new promotional strategies, such as the introduction of digital and social media marketing, as well as cost-cutting measures, which boosted sales and profitability. In addition, the company began holding less inventory and moved towards new and distinctive products with higher prices.

By 2016, the troubled retailer returned to profit. They posted a first half profit of NZ$9.41 million, up more than 600 per centy compared to a loss of NZ$1.8 million for the same period a year before. Sales also rose 9 per cent. Simonet's current plans involve turning Kathmandu into a global brand by selling their apparel in overseas department stores, sporting goods stores and franchised shops. He also wants to grow the company's overseas brand presence through online retail and digital marketing. Simonet believes this is a huge growth opportunity for the company.

SNAPSHOT QUESTIONS

1. **Identify** the factors that led to the decline in sales and profits at Kathmandu.
2. **Explain** the strategies that were implemented that led to the renewal of the company.
3. **Predict** what could happen to the company over the next five years.

SUMMARY

- There are three possible outcomes at the post-maturity stage: steady state, decline or renewal.
- Steady state: the business is neither declining nor expanding.
- Decline: fall in sales, cash flow and eventual business failure.
- Renewal: new products are developed and new markets are created, leading to increased sales and a positive cash flow.

EXERCISE 4.3 REVISION

1 **Why** do you think business owners and staff may become complacent in the maturity stage of the business life cycle?

2 **Construct** a concept map to show the main features of a business that is in the maturity stage.

3 **Outline** three challenges that you believe to be the most serious for a business to confront at the maturity stage. **Justify** your selection.

4 **Explain** why a business might need to restructure in the maturity stage.

5 **Demonstrate** how you could tell whether a business is in the:
(a) steady state stage of the maturity stage
(b) decline stage of the maturity stage.

6 **Construct** a concept map showing the main features of a business that is undergoing renewal.

7 **Outline** three challenges that you believe to be the most serious for a business to confront at the renewal stage. **Justify** your selection.

8 **Recall** the key to achieving a long-term, sustainable recovery in sales in the renewal stage.

9 **Calculate** at which stage of the business life cycle you think the business has to undergo the most radical change. Provide reasons to support your answer. **Compare** your answer with other members of the class.

10 Find information online about the NSW Small Business Commissioner to answer the following questions.
(a) **Clarify** why you think the government provides this information.
(b) Select an area of the website and **evaluate** the range of information presented.

on Resources

Weblink: NSW Small Business Commissioner

11 Complete this exercise by placing the appropriate letter in the space provided. Choose from the letters: A = Establishment, B = Growth, C = Maturity and D = Post-maturity. The first question has been done for you.
(a) _A_ Selecting a suitable location to commence trading
(b) ___ Sales increase, but at a decreasing rate.
(c) ___ Establishing a customer base
(d) ___ Renewal may involve a merger or takeover.
(e) ___ It is sometimes difficult to keep up with the demand for the product.
(f) ___ If there is no improvement in sales then voluntary cessation is an option.
(g) ___ The business owner may become complacent.
(h) ___ It is in this stage that many businesses fail.
(i) ___ A cash flow crisis is most likely to occur.
(j) ___ Specialised managers are appointed and tasks delegated.
(k) ___ Product development is important.
(l) ___ The business owner is content to keep the business just the way it is.

EXERCISE 4.3 EXTENSION

1 Visit your local shopping centre and **identify** any businesses that appear to be in the establishment stage of the business life cycle. Arrange to interview one of these owners and **investigate** what challenges he or she experienced in starting the business.

2 Arrange to visit a local business that is in the post-maturity stage. Interview the owner and **create** a report outlining the:
(a) history of the business
(b) business organisation and structure
(c) strengths and weaknesses of the business
(d) future developments.

3 **Investigate** and **create** a report on the business renewal strategies undertaken by organisations such as KFC, McDonald's and Subway.

4.3 Factors that can contribute to business decline

Business decline (and possible) failure is not usually caused by just one single factor but rather a combination of several. Figure 4.7 outlines several factors that could contribute to business decline.

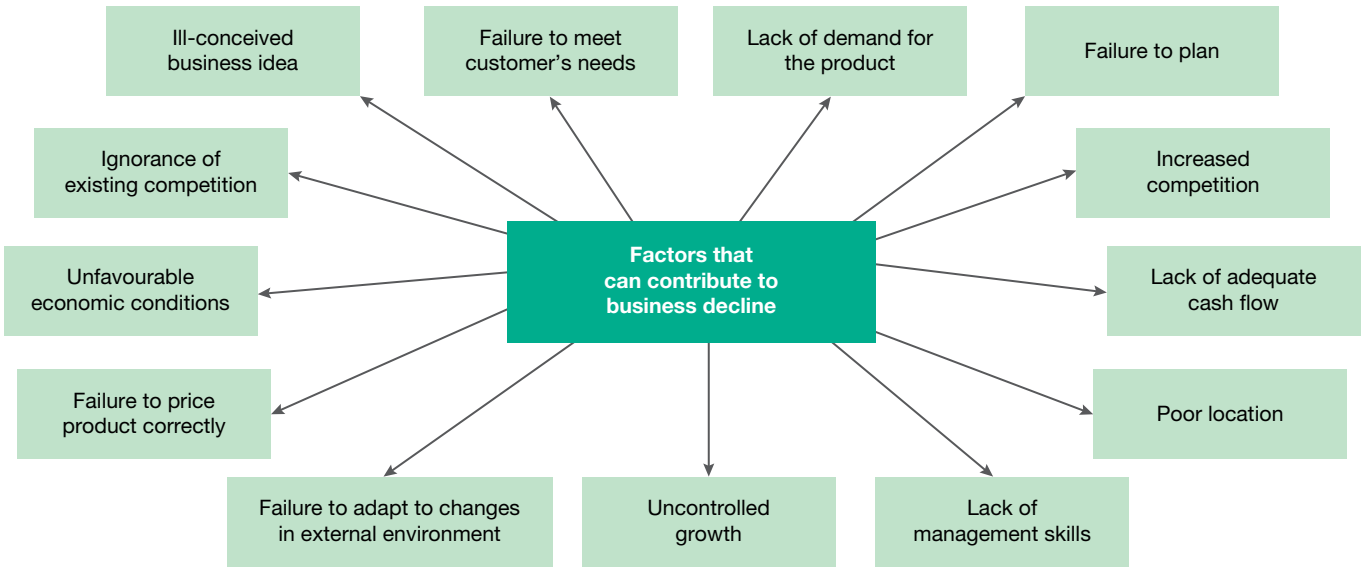


FIGURE 4.7 Factors that can contribute to business decline

However, two main causes of business decline, particularly of SMEs, are:

1. *Lack of management expertise*. When a business either fails to prepare a business plan or fails to keep on modifying an existing plan as the environment changes, the stage is set for imminent failure. It is this situation that gives rise to the often-quoted saying: 'Businesses don't plan to fail, they fail to plan.'
2. *Lack of sufficient money* — **undercapitalisation**. Many small businesses start out on a 'shoestring' budget. Without sufficient capital and a positive cash flow the business will not be able to purchase stock and materials. This inevitably results in lost sales and falling profits.

BizWORD

Undercapitalisation *occurs when there is a lack of sufficient funds to operate a business normally.*

SNAPSHOT



'… the business has struggled recently with increased competition …'

Case study: The decline of Topshop

Almost six years after opening stores in Australia, fashion retailer Topshop Australia has been placed into voluntary administration amid mounting debts.

Administrator Ferrier Hodgson said it will work with Arcadia Group, Topshop/Topman owners in the UK, to convert the Australian business into a sustainable platform going forward.

'The Australia management team are working closely with the Administrators to ensure the best possible outcome for the business,' Ferrier Hodgson partner James Stewart said.

'Topshop/Topman is one of the world's best known fast fashion retailers, operating nine stand-alone stores, 17 Myer concessions and an online business in Australia.'

Australia separately owns and operates Topshop/Topman's Australian franchise, which opened locally in 2011.

Topshop currently employs 760 staff and has annual sales of approximately $90 million.

Mr Hodgson said employees will continue to be paid and gift cards will be honoured during the administration period.

Topshop Australia facing tough competition

Despite being one of the first international fashion brands to set up shop in Australia, the business has struggled recently with increased competition from major rivals Zara and H&M.

Last year, global brands including Zara, H&M and Uniqlo took $600 million out of Australian clothing retail.

But the sector has been under pressure in recent years, as a number of companies struggle to cope with a climate of stalling wage growth and lower consumer spending.

The announcement also follows the recent collapse of half a dozen well-known fashion brands, including Marcs and David Lawrence, the children's label Pumpkin Patch, cut-price shoe store Payless Shoes, suit-maker Herringbone, and its stablemate Rhodes & Beckett.

Myer holds a 20 per cent interest in Australia and acknowledged the company's restructure of its operations in a statement to the ASX this morning.

Retailers have been recently cautioned that they would see further disruption when Amazon and Alibaba arrive in Australia.

Source: 'Topshop Australia goes into voluntary administration', *abc.net.au*.

SNAPSHOT QUESTIONS

1. **Outline** the internal and external factors that led to Topshop's decline.
2. **Identify** other companies that have recently collapsed.
3. **Propose** strategies Topshop could adopt in order to avoid failure.

4.4 Voluntary and involuntary cessation

As mentioned in chapter 1, the world of business is one of activity, challenges, excitement, change and rewards. Many people are attracted to such a world. They have dreams, make plans, and are enthusiastic and optimistic. Because the majority of businesses are classified as small, they often reflect the character, skills and personalities of their individual owners.



FIGURE 4.8 Business failure is not limited to small businesses. Established in 1990, Pumpkin Patch enjoyed many years of success. At its peak in 2007, the children's fashion retailer was valued at $790 million, with hundreds of stores across the globe. Nine years later, the company was placed into administration owing $76 million. Increased competition as well as its too-fast expansion overseas and reliance on debt led to the company's downfall.

A business may cease operating, either voluntarily or involuntarily. The difference between the two depends on who instigates the process (see figure 4.9 below).

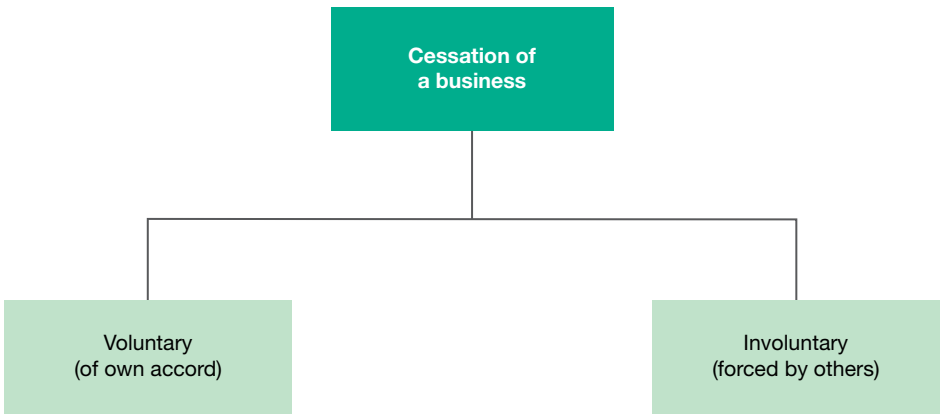


FIGURE 4.9 Cessation of business — voluntary or involuntary

4.4.1 Voluntary cessation

A business may cease operations and voluntarily wind up its affairs. Any assets owned by the business are sold. The business stops operating because the owner may wish to retire, wants a change of lifestyle or, in the case of a sole trader, has died.

BizWORD

Voluntary cessation *occurs when the owner ceases to operate the business of their own accord.*

However, most businesses cease to trade due to business failure. With debts increasing and a negative cash flow, a business owner will soon realise if their business is underperforming. To prevent this accumulation of debt, the owner will need to cease operating the business of their own accord; that is, undergo **voluntary cessation**.

4.4.2 Involuntary cessation

BizWORD

Involuntary cessation *occurs when the owner is forced to cease trading by the creditors of the business.*

Creditors *are those people or businesses who are owed money.*

Many businesses, however, finish involuntarily. The owner is forced to cease trading by the creditors of the business; that is, undergo **involuntary cessation**. **Creditors** are those people or businesses who are owed money.

Even though a business appears to be in financial difficulty, many owners continue operating in the hope that 'things will get better'. In many cases they do not. As the business continues its decline, creditors become worried about the money they are owed and force the business owner into winding up the business.

Figure 4.10 displays the different methods available to wind up a business.

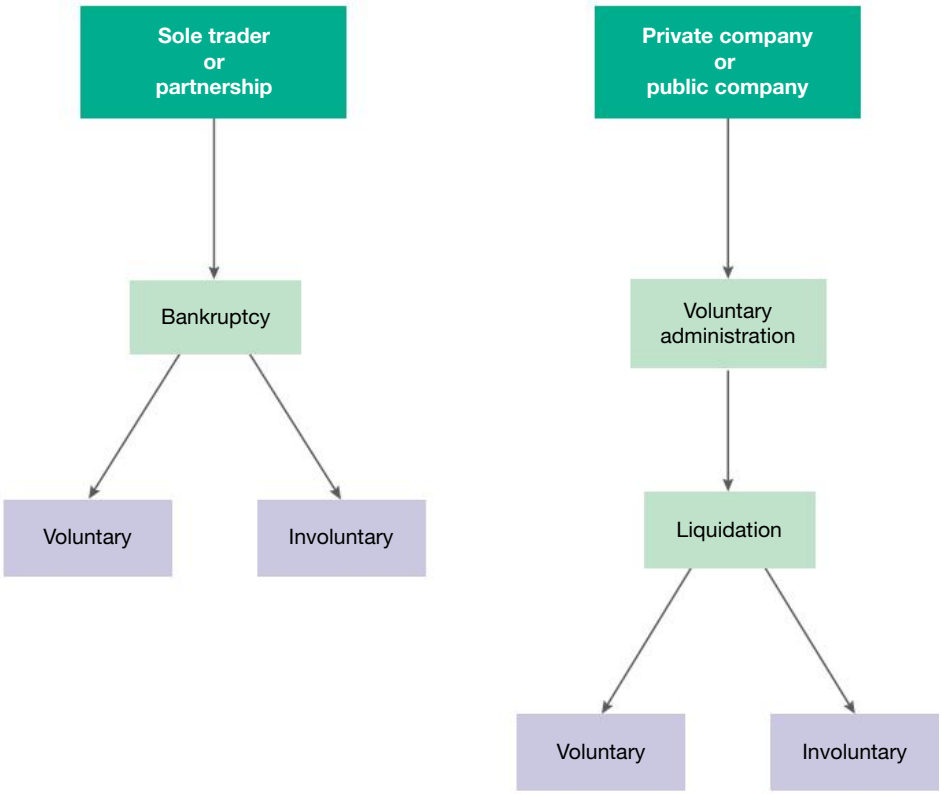


FIGURE 4.10 Different methods available for a business to cease trading

4.4.3 Bankruptcy

BizWORD

Bankruptcy *is a declaration that a business or person is unable to pay his or her debts.*

Realisation *is the process of converting the assets of a business into cash.*

Sole traders (businesses owned and operated by one person) and partnerships (businesses owned and operated by two to 20 people) may end up being declared bankrupt. **Bankruptcy** is a declaration that a business, or person, is unable to pay his or her debts.

Bankruptcy can be either voluntary or involuntary, with either the business owner or a creditor applying to a court for a bankruptcy order to be made. The court then appoints a representative to collect any money owed to the business. This money, along with money raised from the sale of any assets of the business (as well as some personal assets of the owner), is then divided between the creditors. The process of converting the assets of a business into cash is called **realisation**.



FIGURE 4.11 Up to 33 per cent of all small businesses fail within the first year of being established; this rises to an alarming 75 per cent after five years.

4.4.4 Voluntary administration

When a company is experiencing financial difficulties, it can be placed in voluntary administration.

Voluntary administration occurs when an independent administrator is appointed to operate the business in the hope of trading out of the present financial problems. The administrator usually has the combined experiences of a receiver, chartered accountant and investigator. The administrator's main tasks are to bring the business and its creditors together, and examine the financial affairs of the business.

Appointing a voluntary administrator is becoming an increasingly attractive alternative, especially to small business owners. If successful, the business may resume normal trading. If unsuccessful, the business goes into liquidation.

4.4.5 Liquidation

If a company is in financial difficulty, its shareholders, creditors or the court can put the company into liquidation. **Liquidation**, commonly referred to as winding up a company, occurs when an independent and suitably qualified person – the liquidator – is appointed to take control of the business with the intention of selling all the company's assets in an orderly and fair way in order to pay the creditors. Once the creditors have been paid, any surplus cash is paid to the owners of the company.

A company in liquidation can also be in **receivership**. Receivership is where a business has a receiver appointed by creditors or the Courts to take charge of the affairs of the business. Unlike liquidation, though, the business may not necessarily be wound up.

The main features of liquidation are that it:

- can be regarded as the equivalent of bankruptcy for a company (corporation)
- results in the life of a company coming to an end
- normally occurs because the company is unable to pay its debts as and when they fall due – it has become **insolvent**.

BizWORD

Voluntary administration *occurs when an independent administrator is appointed to operate the business in the hope of trading out of the present financial problems.*

BizFACT

Channel 10 went into voluntary administration in June 2017 after their key shareholders, Lachlan Murdoch and Bruce Gordon, decided not to guarantee a new $250 million loan.

BizWORD

Liquidation *occurs when an independent and suitably qualified person – the liquidator – is appointed to take control of the business with the intention of selling all the company's assets in an orderly and fair way in order to pay the creditors.*

Receivership *is where a business has a receiver take charge of the affairs of the business. Unlike liquidation, the business may not necessarily be wound up.*

Being **insolvent** *occurs when a company is not able to pay its debts as and when they fall due.*

BizFACT

Get Qualified Australia (GQA) was an education consultant that assisted job seekers in obtaining qualifications in industries such as beauty, construction and business. In 2017, the company was declared 'unable to pay its debts' and went into liquidation. The company owed more than $1.5 million and left more than 5000 students without the qualifications for which they paid.

There are two types of insolvent liquidation:

1. *Creditors' (voluntary) liquidation*. This is the most common type of liquidation process and can come about in one of two ways. The first method involves creditors voting for liquidation following a voluntary administration. The second method involves the company's shareholders agreeing to liquidate the company and appoint a liquidator.
2. *Court (involuntary) liquidation*. In this situation a court appoints a liquidator to wind up the company, usually after an application has been made from either a creditor, a shareholder, a company director or, in some circumstances, the Australian Securities and Investments Commission (ASIC).

When a company is being liquidated because it is insolvent, the liquidator's prime responsibility is to the company's creditors. The liquidator's main functions are to:

- take possession of and realise – convert into cash – the company's assets
- investigate and report to creditors about the company's financial and related business affairs
- determine debts owed by the company and pay the company's creditors
- scrutinise the reasons for the company failure
- report possible offences by people involved with the company to ASIC
- finally, to deregister or dissolve the company.

A liquidator is not required to do any work unless there are enough assets to pay their costs.

4.4.6 Identify problems that arise for stakeholders when companies go into liquidation

Every year hundreds of Australian companies are placed into liquidation, creating a number of problems for the various stakeholders of the business. The full effect of a company being liquidated can be likened to the ripples on a pond; they radiate out, impacting on the wider community. Eventually the full impact of the liquidation is multiplied, involving many stakeholders. It is estimated, for example, that an average of 30 to 40 people are personally affected by one company insolvency. The main problems that arise for stakeholders are shown in table 4.5.

TABLE 4.5 Main problems arising for stakeholders from company liquidation

Stakeholder	Main problems arising from company liquidation
Company directors	• Possible loss of directorship position and/or disqualified as a director • Could lose personal assets to pay for the company's debts • Possibility of a fine and/or imprisonment
Creditors (unsecured)	• May not recover any of the money owed • If there are funds left over after the payment of the costs of the liquidation and payments to other priority creditors such as employees, it may be possible to receive part payment for the money owed; for example, 5 cents for every dollar owed.
Employees	• Loss of jobs • Have the right, if there are funds left over after payment of the liquidator's fee, to be paid their outstanding wages and superannuation.
Shareholders	• Rank behind the creditors and unlikely to receive any payment • The liquidator can request that holders of unpaid or partly paid shares in the company pay the outstanding amount on those shares.
Society/ economy	• Loss of production from the liquidated companies • Social and personal difficulties associated with job losses • Loss of economic confidence

BizFACT

Generally, the order in which surplus funds are distributed is:

1. *Liquidator's fees*
2. *Employee wages and superannuation*
3. *Employee leave entitlements*
4. *Employee retrenchment pay*
5. *Unsecured creditors.*

Each category is paid in full before the next category is paid. Payment may be on a pro rata basis (proportion of) if there are insufficient funds.

SUMMARY

- The two main causes of business decline (and possible failure) are lack of management expertise or undercapitalisation.
- Voluntary cessation occurs when the owner ceases to operate the business of their own accord.
- Involuntary cessation occurs when the owner is forced to cease trading by the creditors of the business.
- Sole traders and partnerships may voluntarily or involuntarily go into bankruptcy: a declaration that a business, or person, is unable to pay his or her debts.
- A company has two options when facing financial difficulties:
  (a) voluntary administration occurs when an independent administrator is appointed to operate the business in the hope of trading out of the present financial problems.
  (b) voluntary or involuntary liquidation is the process of an appointed liquidator converting the business's assets into cash.
- Liquidation normally occurs because the company is insolvent.
- It is estimated that an average 30 to 40 people are personally affected by one company insolvency.

EXERCISE 4.4 REVISION

1 **Define** the term 'undercapitalisation'.

2 Apart from undercapitalisation and lack of management expertise, **state** three other causes of business failure.

3 As a class, using the brainstorm technique, **propose** the reasons why so many small businesses are undercapitalised.

4 **Distinguish** between voluntary and involuntary business cessation.

5 **Construct** a flowchart showing what happens when a business is declared bankrupt.

6 **Discuss** whether, in your opinion, there is a social stigma attached to bankruptcy today. Should there be? Share your answer with the rest of the class.

7 **Outline** the role of an administrator.

8 **State** the outcome if the process of voluntary administration is:
(a) successful
(b) unsuccessful.

9 (a) **Define** the term 'liquidation'.
(b) **Recall** the common term for liquidation.

10 **Identify** those who can put a company into liquidation.

11 **Distinguish** between 'liquidation' and 'receivership'.

12 **Summarise** the two different types of liquidation.

13 Complete the statements in your notebook by **recalling** the correct word from the list below.

dissolve	realise	debts	financial
possession	failure	report	ASIC
pay	offences	deregister	cash

The liquidator's main functions are to:
- take _____ of and _____ – convert into _____ – the company's assets
- investigate and _____ to creditors about the company's _____ and related business affairs
- determine _____ owed by the company and _____ the company's creditors
- scrutinise the reasons for the company _____
- report possible _____ by people involved with the company to _____
- finally, to _____ or _____ the company.

on Resources

Digital doc: Chapter summary (doc-26096)

Interactivity: Chapter crossword (int-7217)

Interactivity: Multiple choice quiz (int-7218)

on Resources

Weblink: Australian Securities and Investments Commission (ASIC)

14 **Demonstrate** the problems that arise for stakeholders when companies go into liquidation.

15 Use the **Australian Securities and Investments Commission (ASIC)** website as a reference to:
(a) **Identify** some of the signs that may indicate that a company is in financial difficulty.
(b) **Outline** what managers should do if their company is experiencing financial difficulty.

EXERCISE 4.4 EXTENSION

1 In small groups, **create** a list of success strategies for a business that:
(a) has just been established
(b) is in the growth phase
(c) is experiencing a decline of its sales.

2 Assume the Minister for Small Business has established a committee to investigate the granting of business licences. **Propose** the recommendations you would make to the committee regarding the criteria to be used.

3 Most people who start a small business know of the high failure rate.
(a) **Explain** why, in spite of this, they do not take steps to protect their business from failure.
(b) **Determine** the steps you would recommend they take.

Nature of business

MULTIPLE CHOICE QUESTIONS

In the HSC examination you will be required to complete 20 multiple choice questions. Therefore, it is important that you become familiar with answering this type of question. For each question choose the best alternative:

1. Globalisation has had a major impact on businesses. Which external influence in the business environment is this an example of?
(a) Economic
(b) Financial
(c) Geographic
(d) Markets

2. What is the person who risks his or her time, energy and money to start a business called?
(a) A financier
(b) An employer
(c) An innovator
(d) An entrepreneur

3. Which of the following would be an example of a business in the secondary industry?
(a) Zenon Mining
(b) Heritage Motel
(c) Canberra Legal Centre
(d) Plastics Manufacturing Ltd

4. Which business entity is owned and operated by more than two people and has unlimited liability?
(a) Sole trader
(b) Partnership
(c) Public company
(d) Private company

5. In which phase of the business life cycle does complacency amongst management normally occur?
(a) Growth
(b) Maturity
(c) Establishment
(d) Post-maturity

6. What does the business environment refer to?
(a) The surrounding conditions in which the business operates
(b) Those factors over which the business has very little control
(c) Those factors over which the business has some degree of control
(d) A group who has an interest in or is affected by the activities of the business

7. What type of business would National Foods Limited most likely be?
(a) A partnership
(b) A public company
(c) A private company
(d) A government business enterprise

8. Which of the following is an internal influence in the business environment?
(a) Financial
(b) Institutional
(c) Location
(d) Social

9. Which piece of legislation is designed to protect the interests of both consumers and business?
   (a) Small Business Act
   (b) Consumer Affairs Act
   (c) Competition and Consumer Act
   (d) Broadcasting and Television Act
10. Georgia has a hairdressing salon that employs 18 staff. Which of the following is an accurate classification of the business?
   (a) A small business in the tertiary sector
   (b) A small business in the quinary sector
   (c) A medium business in the secondary sector
   (d) A medium business in the quaternary sector

SHORT RESPONSE QUESTIONS

In the HSC examination you will be asked a number of short response questions based on the HSC course.

A short response question generally contains a number of sections, starting with a low order activity and increasing in difficulty. How much you should write for each section is determined by how many marks it is worth. For example, a question that has a value of *two marks* will require double the amount of time and information than one with a value of *one mark*.

1. (a) **State** the main function of business. *2 marks*
   (b) **Demonstrate** the contribution businesses play within the Australian economy in terms of:
   (i) employment *4 marks*
   (ii) incomes *4 marks*
   (iii) choice. *4 marks*
2. (a) **Define** the term 'entrepreneur'. *2 marks*
   (b) **Evaluate** the role entrepreneurship plays in determining business success. *10 marks*
3. (a) **Recall** two quantitative measures and two qualitative measures used to determine the size of a business. *2 marks*
   (b) **Distinguish** between a small and a large business. *5 marks*
   (c) **How** are small businesses, such as local hairdressers or restaurants, able to compete with large, multinational corporations? *10 marks*
4. (a) **Identify** two advantages and two disadvantages of each of the following types of business ownership:
   (i) sole trader *3 marks*
   (ii) partnership *3 marks*
   (iii) company. *3 marks*
   (b) **Distinguish** between an incorporated and an unincorporated business entity. *6 marks*
5. (a) **Define** the term 'business environment'. *2 marks*
   (b) **Distinguish** between the internal environment and the external environment. *6 marks*
   (c) Factors within the internal and external environments can pressure businesses to change practices, policies or products. Referring to a business that you are familiar with, **evaluate** the accuracy of this statement. *12 marks*
6. (a) **Identify** four external influences that can affect a business. *2 marks*
   (b) **Demonstrate** what impact the following internal influences can have on a business.
   (i) Product influences *4 marks*
   (ii) Management influences *4 marks*
   (c) **Assess** the impact of technological influences on retail businesses. *10 marks*
7. (a) **Define** the term 'profit'. *2 marks*
   (b) **Explain** the relationship between sales revenue and profit. *6 marks*
   (c) **Determine** the role profit plays within our economic system. *11 marks*

8. (a) 'Wouldn't every small business owner like his or her business to grow into a large firm?' **Discuss**. *6 marks*
(b) **Determine** whether the advantages of small business really are advantages. *12 marks*

9. The business life cycle consists of four main stages.
(a) **Identify** the four stages. *2 marks*
(b) **Propose** some strategies a business can implement to undergo renewal. *6 marks*
(c) **Assess** the importance of the business owner having an understanding of the business life cycle. *10 marks*

10. Your brother is thinking about starting a family business. He has invited you to be a member of the business and has asked you for your advice.
(a) **Clarify** two legal types of business structure that may be appropriate. *2 marks*
(b) **Discuss** the legal requirements for setting up each type of business. *6 marks*
(c) **Assess** the advantages and disadvantages of each type of business. *12 marks*

11. Ezzra and Jacinta are considering forming a partnership. They have worked for an architect for some time and now feel that they could do much better on their own. Imagine that Jacinta has approached you for advice.
(a) **Define** the term 'partnership'. *2 marks*
(b) **Discuss** the legal requirements for the formation of a partnership. *4 marks*
(c) **Determine** the legal rights and responsibilities of each partner in a partnership. *10 marks*

12. (a) **Identify** the key to determining whether or not a business's actions are socially responsible. *2 marks*
(b) **Outline** the main benefits to a business of conducting a sustainability report. *3 marks*

13. (a) **Define** the term 'stakeholder'. *2 marks*
(b) **Why** are some of these responsibilities incompatible whereas others are compatible? *5 marks*
(c) 'Shareholders' expectations should take precedence over the desires of other stakeholders'. **Evaluate**. *8 marks*
(d) **Determine** the responsibilities a business has to each of its stakeholders. *12 marks*

14. (a) **Why** is it sometimes difficult for a business to satisfy the expectations of all its stakeholders? *3 marks*
(b) **Propose** a number of strategies a business can use to reconcile the conflicting interests of its stakeholders. *5 marks*
(c) **Evaluate** the effectiveness of each of these strategies. *10 marks*

15. (a) **Define** the term 'undercapitalisation'. *2 marks*
(b) **Distinguish** between voluntary administration and liquidation. *6 marks*
(c) **Demonstrate** the main problems that arise for stakeholders when companies go into liquidation. *10 marks*

EXTENDED RESPONSE QUESTIONS

In the HSC examination you will be asked a number of extended response questions based on the HSC course.

One of the extended response questions will require a report style format, a style of writing used extensively in business. Report writing will require you to disregard much of what you have previously been taught when writing traditional essay style answers. Report answers use:

- short statements
- lists of main points followed with explanations when appropriate
- short paragraphs
- headings and subheadings
- diagrams, tables and graphs
- condensed conclusions and/or recommendations when required.

Newspaper articles adopt a report writing style. Each paragraph is brief and to the point with short sentences. It is important that you become familiar with answering this type of question.

Your answer will be assessed on how well you:

- demonstrate knowledge and understanding relevant to the question
- communicate using relevant business terminology and concepts
- present a sustained, logical and cohesive response

1. **Discuss** the importance of business to the Australian economy. In your answer refer to:
   (a) creating value
   (b) social and economic roles
   (c) relevant stakeholders.
2. The internal environment refers to influences that come from within the business itself and can affect business performance. **Discuss**.
3. **Demonstrate** how businesses contribute to our social and economic wellbeing.
4. 'Small business should not be taken for granted.' **Evaluate** the accuracy of this statement. In your answer use some statistics to support your arguments.
5. 'To be effective, business strategy must take into account the interests, needs, and expectations of all the business's stakeholders. Companies should have a strategy that combines business goals and broad social interests'. **Discuss**, using examples, the accuracy of this statement.
6. Natureland Organics is a public company located 280 kilometres from Sydney. It relies on fresh, organically certified farm produce to supply its three Sydney outlets and employs 238 people from the local area. The business has a strong reputation for nutritional value, reliability and support for the environment. The business has recently started exporting to Singapore and Hong Kong. This will require a new production facility to be built. The CEO has identified two areas of concern for future growth:
   - Local residents are complaining that a new plant will cause environmental damage, especially pollution of a nearby river.
   - Shareholders are complaining about the cost of the new plant needed for the extra production.

   (a) Prepare a report that could be given to Natureland Organic's management team. In your report, you should:
      (i) **Identify** Natureland Organic's stakeholders.
      (ii) **Outline** three pressures affecting Natureland Organics.
   (b) Natureland Organics contributes in many ways to the Australian economy. **Demonstrate** two economic contributions that would be lost if Natureland Organics was forced to close.
7. **Discuss** three challenges that you believe to be the most significant in each of the four stages of the business life cycle.
8. **Outline** the main reasons for business failure. **Distinguish** between bankruptcy, voluntary administration and liquidation.
9. Both the quaternary (information processing) and quinary (household services) industry sectors are becoming major contributors to Australia's gross domestic product. **Determine** why you believe these two sectors are thriving.
10. Annika Schute and Gordon Wong, partners in Omega Home Renovations, have been operating their thriving business for five years. They now wish to expand, but cannot decide whether to become a private or public company. They have come to you for advice. Annika and Gordon wish to maintain some degree of control of their business, but they like the idea of gaining access to more funds to allow them to expand more quickly.

    As a business consultant, prepare a report that could be given to Annika and Gordon. In your report, you should:
    (a) **Describe** the main advantages and disadvantages of a private and a public company.
    (b) **Recommend** which of the two options is best suited to their long term goal.

11. You have been employed as a business reporter with the local newspaper. You are asked to **create** an article that examines the external environmental factors that affect business. A major focus within your article should be an analysis of the impact of each factor on specific businesses.
12. 'Improving a business's ethical performance depends on the values of its managers and employees, and the business culture'. **Discuss**.
13. **Contrast** the stages of establishment, growth and maturity in the business life cycle.
14. When a business is wound up, there are usually negative consequences for the many stakeholders. **Determine** the main problems arising from a company liquidation.

TOPIC 2

BUSINESS MANAGEMENT

FOCUS AREA

The focus of this topic is the nature and responsibilities of management in the business environment.

OUTCOMES

Students should be able to:

- explain the internal and external influences on businesses
- assess the processes and interdependence of key business functions
- examine the application of management theories and strategies
- analyse the responsibilities of business to internal and external stakeholders
- plan and conduct investigations into contemporary business issues
- evaluate information for actual and hypothetical business situations
- communicate business information and issues in appropriate formats
- apply mathematical concepts appropriately in business situations.





Case study: Andrew Thorburn — a successful business manager

Andrew Thorburn (pictured), the CEO of the National Australia Bank, was ranked as one of Australia's Top 10 CEOs of 2015. After 30 years' experience in banking, as well as experience in senior positions at a number of Australian banks, Thorburn was appointed Group CEO of NAB in 2014, where he has implemented significant change that has turned the company around.

When reflecting on the age-old debate about whether leaders are made or born, Thorburn believes that anyone can be a leader: 'what it takes is character development, ambition, courage and a driving desire to challenge the status quo.' Thorburn has admitted that he once lacked some of these qualities, but through observing mentors and other leaders he was able to develop and learn these skills.

Thorburn spends a lot of his time mingling and talking to customers and frontline staff when he should be talking strategy in the boardroom. He encourages them to say what they think because he recognises that he doesn't always have all the answers. Thorburn believes one of the most effective ways of problem-solving is to listen to different perspectives. One of his favourite parts of the job is to visit different cities, including regional areas, and talk to staff in order to obtain a view from the ground. He encourages two-way communication as he feels he can learn so much from his employees about what needs to be done to support them.

Thorburn believes leadership is all about people; the ability to engage with, and lead, people. He always wears a name badge (the same type worn by staff in the bank's branches) so that when he meets people he can introduce himself and encourage them to talk to him. While he is often described as ambitious and someone who can make tough calls, staff have found Thorburn to be caring and encouraging. He has been described as a people person due to his ability to relate to staff and customers.

One of Thorburn's most effective leadership skills is his ability to adapt to and implement change. From the moment he began at NAB, he has been constantly challenging the status quo. Thorburn recognises that he's operating in an environment that is experiencing an unprecedented level of change; however, rather than viewing change as a threat, he embraces it and views it as an opportunity for the business to shape the industry.

Thorburn possesses a drive for change. He wants to usher it in from the ground up. He also has high expectations of his employees' abilities to implement change. Thorburn continually talks to his staff and focuses on their needs, which demonstrates he is concerned about their welfare. This has reduced the resistance to change in the organisation and led to a culture where employees embrace change.

In order to create a culture of change, Thorburn believes that management needs to have a clear intent about what they want to achieve. They need to create a big strategic goal that inspires people. For NAB, the overarching goal is to make the customer experience better. Once the strategic aim has been communicated, Thorburn relies on change agents to help drive the change. He has created a group of leaders who are passionate but who are also given the freedom to fail, to inspire others in the organisation to adopt change. In order to sustain the change, Thorburn is a firm believer in offering encouragement and recognition to staff.

Thorburn believes leaders should be role models and lead by example. This is why he always acts the way that he expects others to behave. He has come to realise that the biggest driver of culture is the behaviour of leaders and that it's not what they say, it's their actions and what they do that will inspire others. And inspire he has!



'… he embraces change and views it as an opportunity …'

CHAPTER 5

Nature of management

OVERVIEW

5.1 Introduction
5.2 The features of effective management
5.3 Skills of management

5.1 Introduction

Have you ever been shopping and spent all your money on the first few things you saw, only to later be disappointed when you came across something you would have liked more? What about the assessable task you left until the last minute only to find all the information resources you needed had been borrowed from the library? Or the dental appointment for which you were half an hour late? In these cases you did not manage either your money, assessment requirements or time very well. These cases reveal that you have actually been practising the art of management for a number of years. Sometimes you have managed your affairs successfully; at other times you may have mismanaged them.



FIGURE 5.1 Stephen Cornelissen, Group CEO of Mercy Health, won 2016 CEO of the Year for making a notable difference in the corporate world. Cornelissen joined the not-for-profit organisation as CEO in 2011 and in the 2015/16 financial year, the organisation expanded its aged care services nationally and redeveloped its current facilities. His traits include a willingness to laugh and have fun, as well as placing a significance on integrity through honesty and hard work.

Managing is an essential skill that all people need to develop. How well you perform the task of management will often determine whether you achieve the goals you have set for yourself. In the world of business, just as in your personal life, management is a fundamental activity. It is what makes the business function.

The CEO featured in the opening story of this topic highlights a number of important characteristics of management, including:

1. having the ability to analyse information, attend meetings and communicate with a wide range of people both inside and outside the business
2. possessing the skills to manage change effectively
3. having the vision to see how things could be, rather than just accepting things the way they are
4. providing leadership through the desire to encourage, motivate and guide employees
5. understanding your roles and responsibilities in order to achieve the goals of the business.

The **traditional definition of management** is the process of coordinating a business's resources to achieve its goals.

As outlined in chapter 3 the four main resources available to a business are:

- Human resources. These are the employees of the business and are generally its most important asset.
- Information resources. These include the knowledge and data required by the business, such as market research, sales reports, economic forecasts, technical material and legal advice.
- Physical resources. These include equipment, machinery, buildings and raw materials.
- Financial resources. These are the funds the business uses to meet its obligations to various creditors.

A **manager**, therefore, is someone who coordinates the business's limited resources in order to achieve specific goals.

BizWORD

The **traditional definition of management** *is the process of coordinating a business's resources to achieve its goals.*

BizWORD

A **manager** *is someone who coordinates the business's limited resources in order to achieve specific goals.*



FIGURE 5.2 An effective manager is an essential ingredient for achieving business success. Melinda Gates, co-chair of the Bill & Melinda Gates Foundation, has been recognised as one of the world's greatest leaders. Her vision for the foundation has helped improve the lives of millions of people. The work of the organisation reflects her impatient optimism, passionate commitment to empowering women and her fundamental belief in human dignity.

5.1.1 Contemporary definition

The past few years have seen a subtle, but significant, modification of the meaning of the term 'management'. More contemporary definitions emphasise that **management** is the process of working with and through other people to achieve the goals of the business in a rapidly changing environment, as shown in figure 5.3. Crucial to this process is the effective and efficient use of limited resources.

According to this definition, management requires:

- *Working with and through others.* Management is, above all else, a social process. Those managers who do not interact and communicate well with employees fail to achieve high levels of commitment from staff.
- *Achieving the goals of the business.* Without goals, the business would quickly lose direction. Employees would not understand the ultimate purpose of their work and managers would not be able to measure performance. **Effectiveness** measures the degree to which a goal has been achieved.
- *Getting the most from the limited resources.* All businesses face the problem of limited resources or scarcity. Consequently, managers need to coordinate the resources efficiently. **Efficiency** compares the resources needed to achieve a goal

BizWORD

A more contemporary definition of **management** *views management as the process of working with and through other people to achieve business goals in a changing environment. Crucial to this process is the effective and efficient use of limited resources.*

Effectiveness *measures the degree to which a goal has been achieved.*

BizWORD

Efficiency *compares the resources needed to achieve a goal (the costs) against what was actually achieved (the benefits).*

(the costs) against what was actually achieved (the benefits). The most efficient coordination of resources occurs when the benefits are greater than the costs.

- *Balancing efficiency and effectiveness.* Managers must usually balance both the efficiency and effectiveness of their decisions. A correct balance between efficiency and effectiveness is the key to achieving a competitive position in today's challenging business environment.
- *Coping with a rapidly changing environment.* This is one of the most important tasks of all managers. Successful managers are those who anticipate and adjust to changing circumstances.

on Resources

Weblink: The changing role of managers



FIGURE 5.3 Key aspects of the management process



FIGURE 5.4 A manager's job is never done! Managers can sometimes feel as if they are caught in a neverending cycle of meetings, interruptions, paperwork, emails and trivialities.

5.1.2 Management within the business

Management is a complex task. It is an exciting, challenging, sometimes frustrating but usually rewarding experience. All businesses must be managed; they do not operate automatically. For example, without managers how could 20 000 airline flights a day be achieved without an accident, tens of thousands of motor vehicles be manufactured, hundreds of thousands of students be educated, and hundreds of films and downloads be made available for our entertainment.

The manager's role is similar to that of a musical conductor. It is the conductor who has to coordinate all the members of the orchestra so they stay in time, inspire and lead, encourage superior playing, develop the correct interpretation of the score, and have the orchestra playing as a whole rather than as a group of individuals just playing notes (see figure 5.5).

Observations made of modern managers' work patterns suggest that management is a difficult and demanding job and that there is a gap between how people view the role of a manager and reality. The myths and realities of management are outlined in table 5.1.



FIGURE 5.5 A business manager shares many similar features with an orchestra conductor. Like conductors, business managers bring together all of the varying resources needed to make the business successful and when it is effective, beautiful music is the result.

TABLE 5.1 The myths and realities of a manager's job according to management researcher Henry Mintzberg

Myth	Reality
1. The effective manager is a methodical planner, reflects on what has been achieved, with time to systematically work through problems encountered throughout the day.	The typical manager is constantly interrupted, with no more than approximately 10 minutes spent on any one activity. The manager takes on a great deal and has little time for reflection.
2. The effective manager has no regular activities to carry out. It is all a matter of coordinating other people's responsibilities and then sitting back to watch others do the work.	Although managers' days are constantly interrupted by both trivialities and crises, they still have regular duties to perform. They must interpret and analyse information, attend meetings and communicate regularly with other parts of the business.
3. Management is a science and, as such, can be reduced to a formula and set of 'laws' that, if followed, result in goals being achieved.	The manager's job is more art than science. Managers rely heavily on judgement, past experience, perception and intuition.

5.2 The features of effective management

Every business — whether it be profit or not-for-profit, small, medium or large — needs effective management to succeed. Managers are necessary because society could not function without businesses, and businesses cannot function without managers.

An effective manager needs to be good at:

- **Planning**: the preparation of a predetermined course of action for a business. It refers to the process of setting objectives and deciding on the methods to achieve them.
- **Organising**: the structuring of the organisation to translate plans and goals into action.
- **Leading**: the process of influencing or motivating people to work towards the achievement of the organisation's objectives.
- **Controlling**: compares what was intended to happen with what has actually occurred.

The important role of effective management is to make sure the joint efforts of employees are directed towards achieving the goals of the business. Producing all the goods and services demanded by consumers involves the combined efforts of many people. This combined effort must be effectively coordinated so that the greatest amount of goods and services can be produced for the least cost — that is, efficiently. This coordination needs to be managed on many different levels; for example, within businesses, between businesses and on a national and international level. Businesses must do more than meet the needs of individuals; they must also meet the needs of all the stakeholders in general.

Above all else, what is important to any business is not the number of managers it employs, or the prestigious titles it gives them, but the ability of these managers to achieve the business's goals. To do this effectively, a manager must possess a range of skills.

BizWORD

Planning *is the preparation of a predetermined course of action for a business.*

Organising *is the structuring of the organisation to translate plans and goals into action.*

Leading *is the process of influencing or motivating people to work towards the achievement of the organisation's objectives.*

Controlling *compares what was intended to happen with what has actually occurred.*

BizFACT

Managers' expectations have a direct impact on their employees' productivity. Managers with high expectations lead a more highly motivated and productive staff.

SUMMARY

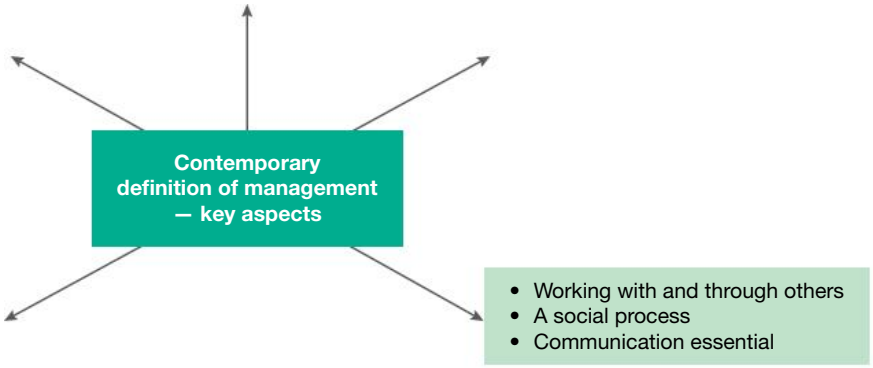
- Management is a fundamental activity that makes the business function.
- Management is the process of:
  (i) coordinating a business's resources to achieve its goals
  (ii) working with and through other people to achieve business goals in a changing environment.
- Whether the goals of the business are achieved largely depends on the skills and expertise of the management team in coordinating the business's resources.
- Every business needs effective management to succeed.
- An effective manager needs to be good at planning, organising, leading and controlling.
- The role of effective management is to make sure the joint efforts of employees are directed towards achieving the business's goals.
- Effective management is usually the major factor influencing the success or failure of a business.

EXERCISE 5.1 REVISION

1 Read about Andrew Thorburn at the beginning of this topic.
(a) **Outline** the features of effective management that Andrew Thorburn displays.
(b) **Assess** the effect his management style would have on both employees and the business.

2 **State** the main function of management according to the traditional definition.

3 **Describe** the four main resources available to a business.
4 **Distinguish** between the contemporary definition of management and the traditional definition.
5 **Construct** a concept map summarising the five key aspects of the management process according to the contemporary definition. The first one has been started for you.



6 **Distinguish** between efficiency and effectiveness.
7 'The performance of managers is often evaluated according to two criteria: efficiency and effectiveness. Of the two, effectiveness is the most important.' **Discuss**.
8 According to observations, **contrast** the 'realities' of a manager's job with the 'myths'.
9 Interview either a head teacher, deputy principal or principal at your school and **create** a list of managerial activities they undertake in the course of a day. **Calculate** to what extent their experiences mirror the realities and myths of a manager's job.
10 **Recall** the important role of effective management.
11 **Why** is effective management so important in our society?
12 'How well you perform the task of management will often determine whether you achieve the goals you have set for yourself.' **Discuss**.

EXERCISE 5.1 EXTENSION

1 Consider the following statement: 'Management is often demanding, complex, stressful and exacting. Contributing to the complexity are globalisation, focus on quality, increasing competition, technological developments, and the rising demand for the ethical conduct of people and organisations. But at the same time, it can be personally rewarding.' **Examine** the positive and negative aspects of being a manager.
2 Some people argue that middle-level managers have a more difficult job than top/senior or lower/frontline managers. This is because the work of a middle-level manager is more varied in managerial and non-managerial duties. **Evaluate**.
3 **Determine** which you think is the more difficult management task: getting employees to work in teams rather than independently, or getting employees to accept change in the workplace. Provide reasons for your answer.
4 'The main difference between employees and managers is that employees work and managers think.' **Assess** to what extent this statement reflects conditions in today's workplace. **Compare** your answers with those of other class members.

5.3 Skills of management

In every occupation, certain skills are needed for success. If you have a **skill**, it means that you have the ability to complete a task effectively. A surgeon must be decisive and have the technical abilities to perform complicated operations. A champion swimmer must have the combination of natural talent and skills that enable him or her to swim better than almost anyone else.

BizWORD

Skill *is the ability that comes from the knowledge, practice and talent to do something well.*

BizFACT

CEOs tend to score higher than the general population on personality attributes such as achievement-orientation, ambition, assertiveness and risk-preference.

Not surprisingly, managers also need certain skills. The more successful managers appear to have more of these skills than the less successful managers. Not every manager requires the same amount of each skill; however, some skills are more important for some job types or workplaces than are others.

In general, effective managers are those who:

- possess a range of specific management skills (see figure 5.6)
- are able to use these skills in a number of different situations.

ENVIRONMENT GROUP MANAGER — $185k pkg neg

- Well-respected international operation
- Engineering, resources focus
- Lead a culture of 'zero harm' and sustainability

As the leader in their market, Alliance & Hudson offers a genuine career opportunity to join a growing success story. Alliance & Hudson is a dynamic, result-oriented environment to work in.

The main responsibility of this position is to develop and implement sustainable production practices across all divisions of the organisation.

As the Environment Group Manager, you will streamline processes, and provide timely and insightful leadership and engagement.

The successful candidate for this position will possess:

- **outstanding interpersonal and communication skills**
- **the ability to effectively convey technical information**
- **experience in leading high-performance teams**
- **superior problem-solving and decision-making abilities**
- **initiative and the ability to work to deadlines**
- **successful management of stakeholder relations**
- **the professional ethics needed to meet the high standards of confidentiality and discretion required.**

Remuneration will consist of a market competitive salary (negotiable), superannuation and leased vehicle. Relevant tertiary qualifications are essential.

To be considered, applicants must apply directly to this advertisement. Visit www.all&hud.com.au/careers, quoting ref no 45930 or phone Maryke Nagy on (03) 8964 2407.

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FIGURE 5.6 Managers are required to possess a range of specific management skills, as shown by this job advertisement.

Normally, a manager is not required to use all these skills constantly. What is important is that these skills and abilities must be available when they are needed so that managers can organise and motivate staff to work effectively towards objectives. These skills take on added significance, given the two fundamental changes that have taken place in the structure of many businesses over the past decade:

1. the movement away from the 'tall' hierarchical structures of many traditional businesses, with their multiple layers of management, towards 'flatter' business structures
2. the development of self-managing work teams.

In 2006, Innovation & Business Skills Australia (IBSA) commissioned the Boston Consulting Group (BCG) to undertake a study into how the role of Australia's senior managers is likely to change between then and 2020. Their report, *2020 vision: The manager of the 21st century*, reinforces the skills that will be needed to respond to these changes. The report says that the trend away from traditional 'command and control' forms of management towards team-based, consultative management styles will continue.

Managers require a range of skills to operate effectively now and into the future. These skills include:

- interpersonal (people)
- communication

on Resources

Weblink: 2020 Vision Report

- strategic thinking
- vision
- problem solving
- decision making
- flexibility
- adaptability to change
- reconciling the conflicting interests of stakeholders.

Why Australian workplaces need much better leaders

Over the last decade, Australia has experienced a productivity slump. Our long-term productivity growth ranks well below the OECD average, and significantly below that enjoyed by leading economies.

However, the reality of falling productivity and its consequences has been masked for most ordinary Australians by the mining boom, which has created jobs and driven up wages.

A number of international studies have suggested that in many workplaces the quality of leadership and management skills can have significant direct effects on productivity, as well as indirect effects through their consequences for how workplaces adapt to changing business conditions and innovate.

A similar picture is now emerging in Australia. This gap is evident in official data on the ability of Australian business to introduce technological innovations, new products or services, or new management systems or organisational innovations. Among SMEs and in certain industries, the record is even more dismal.

Research on the take-up of high-performance management practices also indicates a paradox: while the types of practices that lead to better performance are well established, few workplaces adopt them.

Are Australians bad managers?

Why do Australian businesses have such a dismal record in improving the very things that drive workplace productivity? There are many reasons, but the quality of management and leadership in the workplace is a critical one.

It is clear, for example, that many Australian managers are seriously underqualified for the job they do. Australian Bureau of Statistics data on the qualifications of different occupation groups show that fewer managers have post-school qualifications than do the unskilled and semi-skilled workers they manage.

This is alarming at a time when the challenges of businesses are become more complex. This qualifications gap among our managers is particular acute among small and medium-sized businesses. Clearly, we need to invest more in training managers.

The Centre for Workplace Leadership at the University of Melbourne has begun to track employee perceptions of management and leadership in Australian workplaces.

Our initial survey findings, released today, present a stark picture. A staggering 75 per cent of employees surveyed report that Australian workplaces need better managers and leaders. Perhaps a concerning indicator of future problems is the fact that this view is held by a majority of young people.

We are entering a period marked by the emergence of new, disruptive challenges for business. These challenges are set to undermine the competitiveness of Australian business, and cannot be met by providing businesses with tax breaks or subsidies to continue to operate at a loss.

Meeting new business challenges

The leadership gap goes well beyond formal qualifications. Recent survey evidence shows that many managers and leaders lack a number of critical technical and people skills. That undermines their capacity to maximise productivity.

Among the more significant is an inability to develop a strategic perspective that allows the business to read disruptive changes in markets, identify new opportunities and to adapt.

SNAPSHOT



'… we need to invest more in training managers.'

The flow-on effects are numerous, but inevitably a key one concerns the absence of the skills necessary to manage people, drive continuous improvement and effectively manage change. These challenges are also associated with under-developed and under-resourced HR systems.

This problem typically reflects a lack of knowledge of workplace issues other than in a reactive way. Again, the evidence on these matters shows that these challenges are most acutely felt by managers in SMEs.

Source: Peter Gahan, 'Why Australian workplaces need much better leaders', *The Conversation*.

SNAPSHOT QUESTIONS

1. **Identify** those factors on which the quality of leadership and management skills has a direct effect.
2. **Why** are Australian managers sometimes considered bad managers?
3. **Identify** the management skills that Australian managers lack, according to the article.

BizFACT

Australian Industry Group's Addressing Enterprise Leadership in Australia *report in 2015 found that a lack of self-awareness by ineffective company managers is contributing to Australia's declining reputation of corporate leadership. It found that Australian managers overestimated their company's management capabilities, which is concerning as it leads to an under-investment in leadership development.*

SUMMARY

- In general, effective managers are those who:
  - possess a range of specific management skills
  - are able to use these skills in a number of different situations.
- All managers use their skills to achieve the business's goals.
- Managers require a wide range of technical, conceptual (thinking) and people skills.

5.3.1 Interpersonal (people) skills

Do you know anyone who lacks interpersonal skills? These are the people who are insensitive to the needs and feelings of others; people who speak before thinking and consequently 'put both feet in'; people who say the wrong thing at the wrong time or to the wrong person; people who rub others up the wrong way. Such people generally make very poor managers.

Managers get their work done with and through other people; therefore, **interpersonal (people) skills** are extremely important. Such skills mean a manager can work and communicate with other people and understand their needs.

Interpersonal skills centre on the ability to relate to people, being aware of and appreciating their needs, and showing genuine understanding. People skills include the ability to communicate, motivate, lead and inspire (see the following Snapshot).

BizWORD

Interpersonal (people) skills *are those skills needed to work and communicate with other people and to understand their needs.*

SNAPSHOT



'… crucial to the success of managers and leaders.'

Interpersonal skills crucial to the success of management

An analysis published in 2016 in the *Journal of Managerial Development* by scholars at California State University identified the five interpersonal skills deemed to be the most crucial to the success of managers and leaders. The five interpersonal skills are:

- **Self-management**: Strongly linked to this is self-awareness. Much research proves that as long as someone is self-aware, they can be taught to be a more effective manager. This is because they will then be able to see how their actions influence the emotions and actions of their staff. Once this is realised, they can then modify their behaviour accordingly. Self-management is the alternative to the traditional hierarchical approach to management in which the manager has total responsibility for planning, organising, leading and controlling. Self-management occurs when a manager delegates responsibility for these functions to staff; each employee is responsible for planning their own work, coordinating their actions with their colleagues, acquiring resources and taking corrective action when needed.

- **Communication**: In relation to effective communication, this is more about what isn't said, rather than what's actually spoken. Effective managers listen to their employees and learn from the people who work for them.
- **Supportiveness**: Since most managers are extremely time poor, they are often unaware of their employees' needs because they are so consumed with the myriad tasks demanding their attention. An effective manager creates an atmosphere in which the people who work for them know they are supported. To build a supportive climate, managers need to send messages that acknowledge the efforts of their employees and their needs. Supportive managers exhibit empathy, are non-judgemental and work together with their staff to seek a common solution when things go wrong.
- **Motivation**: Effective managers customise their interactions to suit different employees' needs in the hope of finding ways to influence their behaviour.
- **Conflict resolution**: Studies have shown that Australian managers have a high rate of avoidance leadership, which means that they often avoid giving negative feedback or dealing with conflict because they're fearful of the social repercussions. Effective leaders help parties engaged in disagreement find a resolution. Several skills are needed to resolve conflicts in the workplace effectively: an ability to view problems and issues from multiple perspectives, strong problem-solving skills, active listening, an ability to think critically and objectively and an ability to empathise and compromise.

SNAPSHOT QUESTIONS

1. **Summarise** the five interpersonal skills crucial to the success of management.
2. **Justify** which of the above skills you believe is the most crucial for an effective manager.

A manager who lacks empathy, is arrogant, opinionated, unable to communicate or who has difficulty relating to people will not be able to develop positive relationships with employees. Employees may actually work more efficiently when such a manager is absent because the fear of intimidation or victimisation is reduced.

5.3.2 Communication skills

Communication is as vital as the air we breathe. As babies we learn to cry in order to satisfy our needs; it is a baby's first attempt at communication. Communication becomes more complex, however, particularly in a modern global business environment. It's not just about what you say, it's about how you say it and what medium you choose to get your message across.

One of the most difficult challenges for managers is getting employees to understand and want to achieve the business's goals. Effective communication is at the heart of meeting this challenge. Without effective communication the most carefully detailed plans and brilliant strategies will most probably fail.

Communication is one of the easiest and, at the same time, most difficult of management skills. This is because of the complex nature of communication. Whether communicating with employees within the business or customers in the marketplace, effective communication is essential for the long-term survival of the business. Well-written letters, an inviting telephone manner, pleasant conversation, concise emails, and friendly smiles and gestures reinforce carefully planned business strategies and client networking.

Managers who are effective communicators and who are able to share their thoughts and plans will find it easy to influence others (see the following Snapshot). Only 40 per cent of employees report that they are well informed about their company's goals, strategies and tactics. This uncertainty about the company's direction leads to chronic stress, which inhibits the release of oxytocin and undermines

on Resources

Weblink: Developing interpersonal skills

BizWORD

Communication *is the exchange of information between people; the sending and receiving of messages.*

BizFACT

There is no simple recipe for great communication, but the Chinese philosopher Confucius once said: 'Tell me and I'll forget. Show me and I'll remember. Involve me and I'll understand.'

BizFACT

A 2015 study of 2.5 million manager-led teams in 195 countries found that workforce engagement improved when supervisors had some form of daily communication with direct reports.

teamwork. Openness is the antidote. Organisations that share their 'flight plans' with employees reduce uncertainty about where they are headed and why. Ongoing communication is key.

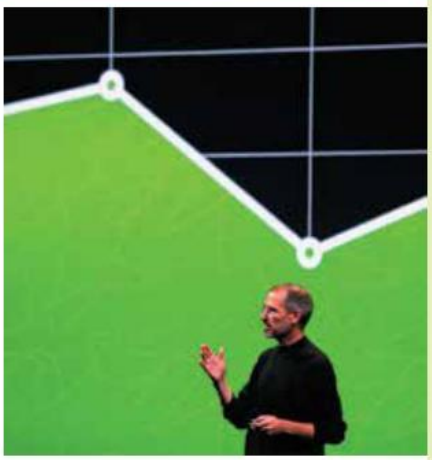
on Resources

Weblink: Business communication



FIGURE 5.7 Clarke Murphy, CEO of executive search firm Russell Reynolds Associates, believes communication skills in today's instant world are essential for a CEO's success. While this might sound very basic, there are many managers who are very good at making decisions and adapting to change, but are unable to articulate to their stakeholders where they are going or why. This skill is crucial to success.

SNAPSHOT



'Steve's presentations became events he wanted the world to watch.'

Case study: Steve Jobs — a great communicator

What is the secret to great communication? Brilliant communicators are often found at the head of highly successful and profitable businesses across the globe. Yet perceptions of what makes a great communicator are, like beauty, often in the eye of the beholder. Steve Jobs, the inspirational, charismatic Apple founder and former CEO who passed away in 2011, believed CEOs should exude a passion and a vision of the business's future. Observers studied Steve's amazing success as a communicator and emphasised some of the strategies that he advised other business leaders and presenters to consider. Let us examine some of Steve's communication techniques.

Firstly, when Steve prepared, he rehearsed over and over, carefully taking into account the nature of the audience, the message and the ideas he wanted people to take 'onboard'. He used his natural speaking voice in a friendly way — as if he was engaged in a normal conversation.

Steve's presentations became events he wanted the world to watch. He believed in creating a drama. For example, when introducing the new iPhone, he had fun with his audience while he acted on stage, pulling the new phone from the smallest pocket in his jeans. Visual ideas were important to Steve. He thought audiences remembered more of what they saw than the words they heard. He always used simple, dramatic, high-quality pictures, but did not overuse the visuals. What do *you* think great communication is?

Steve Jobs, a self-made millionaire, portrayed himself as an individualistic, unconventional entrepreneur. He started Apple in 1976 in California, making the first computer in his garage. Later he created the iPod and started Pixar animations. Today, the company operates more than 400 retail stores in 14 countries and employs over 40 000 people worldwide.

SNAPSHOT QUESTIONS

1. **Define** the terms 'inspirational' and 'charismatic'.
2. **Outline** Steve Jobs' communication techniques.
3. **Propose** why speaking in a friendly way — 'as if he was engaged in a normal conversation' — is a smart communication strategy.
4. **Determine** what you think great communication is. Share your answer with other class members.

Miscommunication

Owing to the complex nature of achieving effective communication, mistakes, misunderstandings and unforeseen barriers sometimes lead to false messages or no message being received. Miscommunication can have disastrous consequences in a business.

The importance of nonverbal communication

Communication is all about sending a message to another person. A message might be verbal, meaning words either written or spoken are used to convey the message. Alternatively, you may choose to convey a message using nonverbal methods as simple as a smile or an image to get your message across.

Nonverbal communication is any message that is not written or spoken. Nonverbal communication mainly consists of body language (posture, facial expressions, placement of limbs and proximity to others).

If you have ever gone to a party, then you are likely to be aware of how effective **body language** can be. A smile, a glance, a stare, the angle of a person's head, a frown, a body movement or the invasion of someone's personal space — they all communicate a message.

It is important for managers to be aware of the power of body language and the messages that can be secretly conveyed. Usually, body language conveys a more powerful message than spoken or written communication. This can result in contradictory messages being intentionally or unintentionally given. A manager who says she is free to talk to an employee about a work problem but then constantly glances at her watch is giving a message that it is not a convenient time to talk. Another example is a manager who expresses one emotion orally, such as confidence, but then has body language reading 'I don't trust you'. Such a contradiction often suggests that actions 'speak louder' (and more accurately) than words.



FIGURE 5.8 "It's not what was said, it's the way she said it." Communication can go awry when the non-verbal aspects conflict with the words being said. For example, if a manager sits forward and smiles during the part of an employment review regarding an employee's strengths, the employee may accept the praise as genuine. When a manager takes the time to match non-verbal messages to verbal ones, the result can be powerful.

BizFACT

Research shows that about 70 per cent of workplace mistakes are the result of inefficient (poor) communication. It is also the most quoted cause of employee frustration and business failure.

BizFACT

A US survey found that miscommunication costs small businesses an average of US$420 000 per year. In another study, 400 businesses with over 100 000 employees each claimed that inadequate communication cost an average $62.5 million per company per year.

BizWORD

Nonverbal communication *is any message that is not written or spoken.*

Body language *is the use of gestures, facial expressions and posture to communicate.*

BizFACT

Extreme care should be taken with body language communication because gestures can have different meanings in different cultures. For example, making a circle with the thumb and forefinger is a friendly gesture in Australia, but it means 'you are worth nothing' in France.

BizFACT

Most researchers agree that 70 per cent or more of the meaning of any message is communicated through nonverbal channels such as eye contact, facial expressions, posture etc. Twenty per cent or so is transmitted through the tone of voice: pitch, timbre, inflection, rate, pauses, volume and so forth. That leaves 10 per cent or less of any message that can be attributed to the words.

5.3.3 Strategic thinking skills

Consider the following quotes:

'Who in the hell wants to hear actors talk?'
Harry Warner, founder of Warner Bros Studios, 1927

'I think there is a world market for about five computers.'
Thomas J. Watson, chairman IBM, 1943

'There is no reason for any individual to have a computer in their home.'
Ken Olsen, president, Digital Equipment, 1977

'Nothing has come along that can beat the horse and buggy.'
Chauncey De Pew, president of the New York Central Railroad, warning his nephew against investing in Henry Ford's new company circa 1911

'Everything that could be invented has now been invented.'
U.S. Patent Office circa 1900

With hindsight we laugh at these quotes. And yet, at the time, most people would have agreed with the speakers. It could be argued that their shortsightedness inhibited strategic thinking. Therefore, they were not able to perceive meaningful patterns in complex circumstances. **Strategic thinking** allows a manager to see the business as a whole — as a complex of parts that depend on and interact with each other, like the gears in a machine and to take the broad, long-term view.

BizWORD

Strategic thinking *allows a manager to see the business as a whole and to take the broad, long-term view.*

The ability to think strategically lets the manager see the 'big picture'. The manager may then:

- visualise how work teams and individuals interrelate
- understand the effect of any action on the business
- gain insights into an uncertain future
- see the business in the context of events and trends, and identify opportunities or threats.

Strategic thinking therefore involves thinking about a business's future direction and what future goals the business wants to achieve. As a student, for example, you were thinking strategically when you made your senior course subject selections in Year 10. You had to imagine what the future job or study requirements would be when you left school, how the workplace may change over time, what future goals you wanted to achieve, and what would interest and motivate you in the future.

Many people assume that strategic thinking skills are the exclusive field of senior management, but that is simply not true. Managers at all levels need to exercise this skill. It will help the business maintain its competitive position within a constantly changing business environment. Although some people seem to have a special gift for being able to predict and comprehend the future, strategic thinking can be learned through practice.

SUMMARY

- Interpersonal (people) skills are those skills needed to work and communicate with other people and to understand their needs.
- Interpersonal skills include the ability to communicate, motivate, lead and inspire.
- Effective communication of business goals and the strategies to achieve them are crucial to achieving business success.
- Managers who are effective communicators and who are able to share their thoughts and plans will find it easy to influence others.
- Miscommunication is to be avoided because it can lead to serious harm to the business.
- It is important for managers to be aware of the power of nonverbal communication, especially body language.
- Strategic management allows the manager to see the business as a whole and to take a broad, long-term view.
- Strategic thinking involves thinking about a business's future direction and what future goals the business wants to achieve.

EXERCISE 5.2 REVISION

1. **Define** the term 'skill'.
2. **Recall** two changes that have taken place in the structure of many businesses over the past decade that have resulted in the skills taking on added significance.
3. **Examine** figure 5.6 on page 124.
   (a) **Identify** some of the desired skills needed to perform this management position.
   (b) **Clarify** which skill you consider to be the most important. **Justify** your answer.
4. **Define** the term 'interpersonal skills'.
5. **Explain** why it is important for a manager to possess good interpersonal skills.
6. 'Interpersonal skills include the ability to communicate, motivate, lead and inspire.'
   Describe a situation, from personal experience, that demonstrates where two of these abilities were used effectively.
7. **Why** should managers strive to improve their ability to communicate?
8. Not everyone is a great communicator, but we can all learn. Identify a poor communication habit you have and **propose** what you might do to improve your communication skills.
9. **Investigate** how well you communicate as a class. Ask your teacher to make up a statement and then conduct your own game of 'Silent whispers', where each member must pass the message on to another person. At the end of the activity, have your teacher read out the original statement and compare it with the final verbal statement from the class member in the group who was told the statement last.
10. **Describe** how you might improve your own nonverbal communication skills with casual acquaintances. Refer to your use of eye contact, facial expression, gesture and voice-tone skills.
11. **Define** the term 'strategic thinking'.
12. **Explain** why managers at all levels need to exercise strategic thinking skills.
13. Draw a table similar to the one following to **summarise** details of the management skills in this section. The first entry has been completed for you.

Skill	Definition	Characteristics	Application to the workplace
Interpersonal skills	It is the ability to work and communicate with other people and to understand their needs.	Managers get their work done through other people. They need to display empathy.	Managers use interpersonal skills to communicate, motivate, lead and inspire.

EXERCISE 5.2 EXTENSION

1. In small groups, imagine you are board members of a medium-sized private company. The company manufactures electronic items for the domestic market. It has 284 employees and its current turnover is approximately $115 million. The company is well established in domestic markets but, due to increasing competition, sales and profits have been decreasing over the past few years.

   The board is preparing to hire a new chief executive officer to lead the company. In your group, **create** a profile of the business leader that you are seeking. Consider qualifications, experience, skills and personality factors.

   Conduct a class discussion on the similarities and differences of each group's profile. **Propose** reasons for any differences.
2. From your knowledge of Steve Jobs, Apple founder and former CEO and his notions of great business leadership, **determine** four communication skills good managers should practise.

on Resources

Weblink: Communication skills test

Weblink: Nonverbal communication

3 Find an online communication skills test or use the **Communication skills test** weblink in the Resources tab and take a test.
(a) **Analyse** your results.
(b) **Deduce** whether you think this is accurate.
(c) **Propose** how you could improve your communication.

4 'Being able to communicate effectively is the most important skill a manager can possess. Without this fundamental skill, all other attributes a manager may possess become less useful.' **Evaluate** the accuracy of this statement.

5 **Construct** a communication pie graph to illustrate the following information: spoken word = 7 per cent, nonverbal communication = 55 per cent and tone of voice = 38 per cent. **Determine** the important observation that can be made from these data.

6 **Create** a PowerPoint presentation lasting no more than five minutes on one aspect of nonverbal communication that is of interest to you. The **Nonverbal communication** weblink in the Resources tab may help you to gather more information on this subject.

5.3.4 Vision skills

BizWORD

Vision *is the clear, shared sense of direction that allows people to attain a common goal.*

BizFACT

Having to develop a vision for the business is very important during times of constant change. Without a vision, any business will ultimately fail.

In his book *Management: tasks, responsibilities, practices*, Peter Drucker explains that it is 'the first response of the manager... to give others vision and the ability to perform'. By **vision**, Drucker means the clear, shared sense of direction that allows people to attain a common goal.

Drucker argues that vision is the essential contribution of management, for without it there can be no sense of cooperation and commitment, which makes achieving goals impossible. Drucker explains that the most effective way for managers to share their vision for the business is through the organisation's goals. Knowing where the business is headed and what it is trying to achieve helps employees understand where the manager wishes to take the business. A manager without a clear vision for the business is like a person who attempts to lead a bushwalk without any idea of where the group wants to go, without a compass or even a map. The walk would become aimless. The same thing happens in a business whose manager has not communicated clearly its vision. The business is without guidance.



FIGURE 5.9 Effective leaders clearly define a vision and communicate it in such a way as to foster enthusiasm and commitment throughout the business. A clear and well-communicated vision is essential for a manager to gain the support of their staff.

BizWORD

Leadership *is the ability to influence people to set and achieve specific goals.*

To share their vision and inspire others, managers will have to display effective leadership qualities. **Leadership** is the ability to influence people to set and achieve specific goals. A manager will use his or her leadership abilities to act as a bridge on which to support team members as they cross from the existing ideas into new and unfamiliar territory.

Case study: Visionary leaders

Visionary leaders inspire others to act in ways that transform a vision into reality. Effective leaders have a clear vision, communicate that vision to those concerned and then motivate and inspire them to actively pursue that vision. Below are examples of three visionary leaders who turned their respective companies around.

1. **Elon Musk, CEO of Space X and Tesla Motors**
   Musk has revolutionised entire industries with his focus on moving beyond the status quo. His tenacity, willingness to take risks and confidence enabled him to turn a pipe dream — an all-electric car company — into a successful business. Both Space X and Tesla Motors faced insolvency in 2008 and, thanks to his successful leadership and vision, have now become billion-dollar companies.

   Elon Musk leads by example, and through his own drive towards excellence, he pushes his employees to their fullest potential and perhaps beyond. He is a transformational leader who demonstrates incredible vision, dedication and perseverance as he strives to achieve his vision. Musk has an ability to make people believe in his vision and get on board with his seemingly crazy ideas, even when they can't conceive it working. Some of his most outstanding qualities are his belief in his own vision, his drive and persistence and his refusal to accept obstacles in his path.
2. **Alan Mulally, former CEO of Ford Motor Company**
   Alan Mulally is seen as the man behind one of the most impressive corporate turnarounds in history. Automaker Ford was losing billions of dollars and on the brink of bankruptcy when Alan Mulally took over in 2006. Within three years, Ford began posting an annual profit every year starting from 2009.

   Mulally initiated a new corporate culture that transformed the way the organisation works. His focus on teamwork and accountability created a new environment that inspired results and focused on positive leadership with a vision toward moving forward. Mulally believes positive leadership and showing confidence that there is always a way forward is crucial, because essentially, that's what leaders are there for — to figure out how to move a business forward. Critical to accomplishing this is reinforcing the idea that everyone is included and part of the team, so everyone's contribution is respected. He fosters a supportive and safe environment in which everyone can have an honest dialogue, especially when things go wrong. Mulally believes it is important to have a compelling vision and a comprehensive plan.
3. **Shantanu Narayen, CEO of Adobe Systems**
   When Shantanu Narayen began at Adobe, he looked down the road and didn't see a future that included distributing software on physical discs. He decided to change the widely-used Adobe Creative Suite to a subscription-based model. Narayen boldly changed his company's distribution model, and the growth in subscription members is proof of his success.

   Shantanu strongly believes that preserving the status quo is not a winning strategy. He not only questions the way things are done, but he ensures he surrounds himself with people who are smarter than he is. He is passionate about creating and empowering teams that drive innovation.

SNAPSHOT QUESTIONS

1. **Identify** the management skills the three CEOs possess.
2. **To what extent** do the above leaders influence the success of their respective companies?

SNAPSHOT



'Visionary leaders inspire others …'

5.3.5 Problem-solving skills

When confronted with a problem, many of us search for an answer, jump at the first workable solution and move on. Management requires a more systematic problem-solving process when confronted with difficult and unfamiliar situations.

BizWORD

Problem solving *is a broad set of activities involved in searching for, identifying and then implementing a course of action to correct an unworkable situation.*

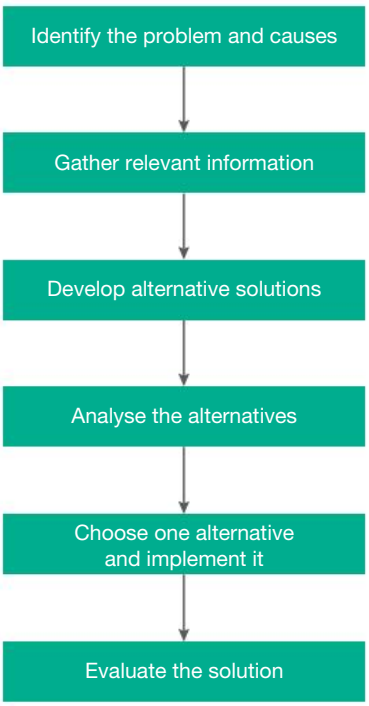


FIGURE 5.10 A problem-solving process

Problem solving means finding and then implementing a course of action to correct an unworkable situation. Although managers have to deal with many problems in the course of a day, not all problems require such a systematic, formal process. One of the most important skills a manager can develop is the ability to decide which problem they should give their full attention.

There are six steps in a typical problem-solving process (see figure 5.10). The first step is to clearly identify what the problem is and what has caused it. The problem might be an industrial dispute or a need to develop a more socially responsible organisation. All of the facts and information that are relevant to the problem must be gathered. Some methods to use might be simply talking to people or completing questionnaires or surveys.



FIGURE 5.11 A common problem managers have to deal with is workplace conflict. Research shows that up to 30 per cent of a typical manager's time is spent dealing with disputes. While conflict in the workplace is unavoidable, it can be minimised with the right strategy, problem-solving skills and direction.

BizWORD

Decision making *is the process of identifying the options available and then choosing a specific course of action to solve a specific problem.*

Management will need to develop alternative solutions so that the problem can be solved with an open mind. A list of possible solutions should be made, including the seemingly ridiculous ones. After analysing each of the alternatives for their advantages and disadvantages, the best option should be chosen. The solution to the problem will then be implemented and subsequently evaluated. If the solution does not work, the process would have to start again.

BizFACT

In 1986, NASA management had to decide whether to launch the space shuttle Challenger even though temperatures at the launch site had fallen below the levels normally required for a safe launch. Lower-level engineers expressed their concerns. However, top-level NASA managers decided to go ahead with the launch, a decision that resulted in the deaths of all the astronauts on board.

5.3.6 Decision-making skills

The task of solving problems will obviously require making some decisions. **Decision making** is the process of identifying the options available and then choosing a specific course of action to solve a specific problem.

Effective decision making involves being able to make decisions within a particular time frame. It also requires a manager to adequately assess the risk involved if the decision is implemented.

Decision making can sometimes be dangerous. Not all management decisions are effective, as NASA discovered tragically in 1986, providing a case study of management decision making that shows dramatically the importance of the decision-making process (see the BizFact at left).

Managers today are often confronted with complex, challenging and stressful decision-making demands. Accelerating change often makes it difficult to accurately predict the full effect of any decision. Therefore, managers need to develop an effective decision-making environment within the business. This can be accomplished by tapping into the creative potential of employees.

5.3.7 Flexibility and adaptability to change skills

Not since the Industrial Revolution over 200 years ago has business experienced so much change. Over the next 10 to 20 years, the Australian business environment will dramatically change. How managers perceive and react to these changes will have dramatic consequences for their businesses.

Regardless of their level of management, successful managers are those who anticipate and adjust to changing circumstances. They must be **flexible**, adaptable and **proactive** rather than reactive. Those who are unprepared or passive in the face of change will not succeed.

Businesses today are recruiting and selecting managers who can cope with unfamiliar and unexpected circumstances. For example, Arthur Hancock, former Senior Human Resources Manager for Global Equities Limited, said:

> We are seeking managers who have learned how to learn and can adapt to changing situations. We do not want managers who are dogmatic and inflexible. Such a style of management may have been appropriate 50 years ago, but not for today's markets which are highly competitive, technologically driven and rapidly changing. We want to hire people who like surprises!

The topic of management and change will be examined in more detail in chapter 9.

BizFACT

According to Mark Graban, an internationally recognised consultant, author and keynote speaker, "Bad managers tell employees what to do, good managers explain why they need to do it, but great managers involve people in decision making and improvement."

BizWORD

Flexible *refers to being responsive to change and able to adjust to changing circumstances.*

Proactive *refers to a management style that incorporates dynamic action and forward planning to achieve particular objectives.*

Case study: Jeff Bezos — flexibility and adaptability to change

Amazon CEO Jeff Bezos has been recognised by various organisations as being one of the greatest living CEOs. He is a transformational leader whose main strength has been his flexibility and ability to adapt to change.

Bezos transformed Amazon from an online bookstore to the largest internet-based retailer in the world. Due to his leadership, the company has not stopped expanding and changing since its inception. Even though Amazon has been trading for over 20 years, Jeff Bezos wants the $430 billion company to behave with the same urgency as the start-up it once was.

To ensure he responds to problems and changes quickly, Bezos believes high-velocity decision-making is essential to a dynamic, successful business. He feels as though it's better to 'fail forward' — i.e. make a decision quickly, learn from mistakes and move ahead — than it is to come to a standstill and be frozen by indecision. He urges his employees to follow the same advice, and not to wait for all the information before acting. Bezos believes most decisions should be made with only about 70 per cent of the information needed, because if you wait for 90 per cent or more, then you're moving too slowly.

A phrase Bezos uses when it comes to acting quickly and implementing change is 'disagree and commit'. He follows this advice when a situation arises where consensus isn't possible. This means that even if Bezos disagrees with a decision, he trusts the judgement of the other decision-makers and is committed to a successful outcome. He believes this is a much faster alternative than the team having to convince him to change his mind.

According to Bezos, good entrepreneurs must be stubborn and flexible. In reference to Amazon, the company is 'stubborn on vision, but flexible on details'. While this seems like a paradox, Bezos considers them both valuable traits and, just like most things in life, the key is finding the middle road between the two. Bezos feels that if you're not flexible, you won't be able to see different solutions to problems you are trying to solve. There are many entrepreneurs that are inherently

SNAPSHOT



"Bezos is more afraid of becoming stagnant."

stubborn and like to take charge and have things done their way. Bezos believes that, while natural leadership skills are good, managers need to be flexible on details.

An example of his flexibility and willingness to change was when the company launched Amazon Auctions to compete with eBay in 1999. This didn't go as well as Bezos expected, but instead of sticking to his guns, he changed his approach. Bezos made some adjustments, abandoned the old idea and moved on to new ideas, which ultimately led to the creation of Amazon's highly profitable third-party sellers program. This example contradicts the traditional leadership mind-set that managers need to be strong, decisive and persistent in achieving their goals. Due to the dynamic nature of the business environment, Bezos' adaptability has been crucial to his success.

Another key feature of Bezos' leadership is that he never stops experimenting: 'If you double the number of experiments you do per year, you're going to double your inventiveness.' At Amazon, experimentation and willingness to invent has always been a part of the culture. In relation to innovation and change, Bezos feels that 'what is dangerous is not to evolve'. While most humans fear change, Bezos is more afraid of becoming stagnant. His inclination to always push the envelope has given Amazon a reputation as an always evolving company.

SNAPSHOT QUESTIONS

1. **Outline** Bezos' decision-making style.
2. **Explain** the phrase 'disagree and commit'.
3. **Demonstrate** how entrepreneurs can be stubborn and flexible.
4. **Demonstrate** how Jeff Bezos is flexible and adaptable to change.

SUMMARY

- Managers must be able to provide a vision as to where the business is headed and what it is trying to achieve.
- To share their vision with others and inspire them, managers will have to display effective leadership qualities.
- Leadership is the ability to influence people to set and achieve specific goals.
- Managers must be able to solve problems — finding and then implementing a course of action to correct an unworkable situation.
- Managers must be able to make decisions — identifying the options available and then choosing a specific course of action to solve the specific problem.
- Managers must be flexible, adaptable and proactive rather than reactive.

5.3.8 Reconciling the conflicting interests of stakeholders

As outlined in chapter 3, there are a number of stakeholders in business. Stakeholders are groups and individuals who interact with the business and thus have a vested interest in its activities. Over the last four decades, there has been a significant philosophical shift in business conduct to meet society's expectations.

Society increasingly expects businesses to accept responsibility and accountability toward all stakeholders for the promotion and management of change. Businesses are expected to be enterprising, to comply with the law, and be socially just and ecologically sustainable in their operations.

Most businesses are now extremely sensitive to public opinion and strive to be recognised as 'good corporate citizens'. Businesses recognise that they increase their chances of success when they pursue goals that align with the interests and expectations of all stakeholders.

All the stakeholders who interact with a business require something different; all place competing demands upon the business. Some of these expectations are

compatible. For example, customers want quality products at reasonable prices. If the business meets this expectation then sales should increase, leading to greater profits. This in turn satisfies the business owners who are rewarded with higher dividends.

However, some expectations are incompatible; that is, they oppose each other. In this case, satisfying one set of stakeholders will most probably result in other stakeholders being dissatisfied. For example, employees and their unions require safe working conditions and reasonable wages while customers want reasonably priced products. Providing safer working conditions or a wage rise is ethically and socially responsible, but it will cost the business money in the short term. If the business wished to retain a high dividend to satisfy the shareholders' expectations, then it may be forced to raise the prices of its products. This action will upset customers. On the other hand, the business may retain prices at the original level, reducing its profit. Doing this could cause disquiet among shareholders.



FIGURE 5.12 In relation to reconciling conflicting interests of stakeholders, Paul Polman, the CEO of Unilever, stated: "I do not work for the shareholder, to be honest; I work for the customer. I discovered a long time ago that if I focus on doing the right thing for the long term to improve the lives of customers all over the world, the business results will come..." He believes managers confronted with conflict should adopt the same outlook; that taking care of consumers' interests is taking care of business.

To maintain its profit, the management of a business may choose to cut costs, for example, and ignore some of its responsibilities. These types of decisions can endanger employees or society, or damage the environment through pollution, raising serious ethical and social responsibility considerations. Management might choose to reduce costs by sacking employees or by compromising on product quality or safety, which also raises other ethical and social responsibility considerations.

Reconciling these conflicting interests is not always easy. Senior management must assess constantly the actions of the business and attempt to satisfy as many stakeholder expectations as possible, while at the same time acting in a responsible manner.

5.3.9 Strategies that could reconcile the conflicting interests of stakeholders

Individuals and corporations purchase shares in companies for a variety of reasons, not least of which is to make a profit. Shares are sometimes purchased and held for only a short time. Such speculation is carried out with the intention of making a quick financial gain. Speculators are not normally concerned with the business's

BizFACT

Corporate social responsibility challenges each business to be accountable for the consequences of its actions. This means businesses must consider effects on all stakeholders while pursuing traditional economic goals.

long-term strategies, philosophies or business practices. They are motivated by a quick return on their investment.

However, other buyers purchase shares with the intention of holding onto them for a reasonable period of time. These non-speculative shareholders are more concerned with the long-term investment strategies of their companies. While these shareholders are still motivated by the desire to make a profit, they are able to adopt a long-term view. They appreciate the responsibility of a business to act as a responsible corporate citizen. They take into account the long-term impact of business decisions with particular regard to the environment and future generations.

The interests of society and future generations are very much reliant on the many decisions taken by businesses. Decisions concerning production processes, workplace practices, employment programs, product development and design, and business expansion will all have an impact on both present and future generations. Businesses have a responsibility to take into account the long-term effects of their current decisions.

One particular strategy that has been adopted by more enlightened businesses is to place greater emphasis on environmental practices. Adopting such a policy has benefits for both shareholders and society (see the following Snapshot).

SNAPSHOT



'Companies are becoming environmental activists because it makes good business sense.'

Why some companies are becoming environmental activists

Clothing brand Patagonia gives 1 per cent of its sales 'to support environmental organisations around the world'. Carpet-maker Interface takes an 'aggressive approach' to reach its goal to source 100 per cent of its 'energy needs from renewable sources by 2020'. Nudie Jeans meanwhile, repairs, reuses and recycles its denim products, as well as using organic cotton to produce them in the first place. So, what's going on? After decades of activists campaigning against companies' poor environmental records, are companies suddenly becoming environmental activists themselves?

Normally, companies are challenged by environmental activists from the outside. That is, NGOs, charities and community groups hold companies to account for their often negative impact on the environment. Think VW — it was an NGO that outed the car manufacturer for gaming the emissions testing system.

Remember too last year's Greenpeace campaign against the Lego–Shell partnership? It was a textbook example of environmental activists using clever social media and protest techniques to raise the public's awareness about the environmental dangers involved in drilling for oil in the Arctic. And it worked.

Companies as activists

But, increasingly, companies have become environmental activists themselves. Take Ecotricity, for example, one of Britain's biggest renewable energy companies, founded by the 'travelling hippy' Dale Vince. The company takes an activist stance against fracking in the UK, producing campaign videos that don't look too dissimilar from those produced by environmental activists. In fact, Ecotricity has teamed up with Friends of the Earth, one of the largest and most influential green NGOs, in its campaign to oppose fracking in the UK.

Cosmetics brand Lush is another successful company that has been very vocal and explicit about opposing fracking in the UK. The company's co-founder and managing director Mark Constantine (a major backer of Frack Off) is explicit about the fact that campaigning is part of the company's core culture. Lush's head of global campaigns, Tamsin Omond, coordinates Lush's involvement and financing of a number of environmental groups, some of which use quite radical direct action tactics to make themselves heard. She herself is a well-known activist who was arrested in 2013 while protesting in West Sussex. The activist ethos of the company is underpinned by the fact that its own employees — 'who are more likely to be drawn from the world of radical politics than business schools' — often play a central role in the environmental causes Lush supports.

This is all a far cry from the questionable attempts by large corporations to green their image. Remember when, about a decade ago, BP tried to tell us that it is now 'beyond petroleum'? Its global, multi-million pound marketing campaign spectacularly backfired when the company's attempt to 'think outside the barrel' was quickly named and shamed by Greenpeace and other environmental groups as a classic case of 'greenwashing'. Why? Because it was mostly talk, and very little walk, which became all too real when BP became responsible for one of the biggest environmental disasters of modern times — the explosion of the Deep Horizon oil platform in the Gulf of Mexico in 2010.

So, why do companies like Lush, Ecotricity and others take such an activist stance for environmental issues? Here are three main reasons:

1. **Companies have always been activists**
   Business has always been about convincing customers, policymakers, employees and the like that companies can be trusted to provide goods and services that contribute to the wider good of society. Henry Ford could be seen as an activist; he wanted to bring automobility to the masses — and he even paid his employees a decent wage so that they could afford his Model T car. So, when Dale Vince founded Ecotricity in the mid-1990s to bring renewable energy to the people of Britain, he, in some ways, is today's Henry Ford.
2. **Capitalism is about competition**
   Activism is also implanted into the doctrine of capitalism because of competition in the market. Shareholder activism has been around for a long time; it's a concept used to depict the attempts by some shareholders to get the most out of their investment, making companies more profitable and competitive.

   What is new is that environmental issues are used to increase competitive advantage. So, when Ecotricity campaigns against fracking, then it also campaigns against its competitor, British Gas, which has invested significantly in fracking. It's about engaging customers and making them choose one company and business model over another.
3. **Motivating employees**
   Environmental issues can also be a good motivating factor for employees. Human resource managers constantly think about new ways to keep employees engaged, motivated and loyal.

   So when Lush encourages its employees to campaign against fracking, the managers will have at least one eye on the motivation, retention and performance of staff.

   Companies are becoming environmental activists because it makes good business sense. But we must scrutinise whether everything that corporate environmental activists tell us is green is indeed green. Employees can function as the litmus paper of corporate green activism. Once we have understood how green activism is reconfigured when it enters the corporate world, we can begin to scrutinise the environmental claims made.

Source: 'Why some companies are becoming environmental activists', *The Conversation*.

SNAPSHOT QUESTIONS

1. **Outline** some strategies companies have introduced to become more environmentally sustainable.
2. **Explain** why some companies have taken an activist stance for environmental issues.

Many business analysts are now starting to refer to the '**triple bottom line**' — economic, social and environmental performance — where shareholder value increases through the careful management of stakeholder value. More businesses are realising that reconciling conflicting interests and increasing stakeholder value ensures long-term growth and survival.

BizWORD

The **triple bottom line** *refers to the economic, social and environmental performance of a business.*

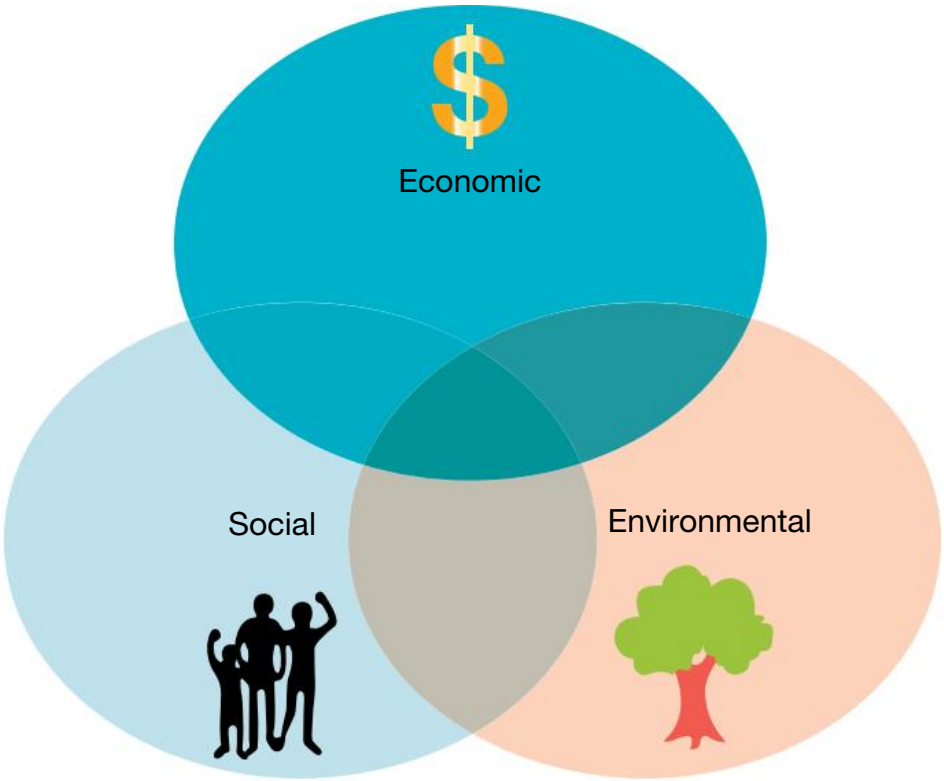


FIGURE 5.13 The Global Reporting Initiative (GRI) is an international standards organisation that helps businesses, governments and other organisations understand and communicate the impact of business on critical sustainability issues. They developed Sustainability Reporting standards and pioneered sustainability reporting in the late 1990s, transforming it from a niche practice to one that is now adopted by a growing majority of organisations. More than 8000 organisations use GRI Guidelines when reporting on their 'triple bottom line'.

To reconcile the conflicting interests between shareholders and employees, businesses can look into employee share acquisition schemes. Such schemes provide the opportunity for eligible employees to purchase shares in a business, often at a reduced price. This aligns the interests of both groups as a number of employees become shareholders.

Another widely used strategy is to offer training and professional development to employees. An educated and skilled workforce works more efficiently, reducing production costs. This results in rising profits, which pleases shareholders. Also, better trained staff produce a higher quality product, thus satisfying customer expectations.

The more successfully a management team achieves the business's goals, the more it will be able to satisfy a greater number of stakeholders. Therefore, to succeed in reconciling the conflicting interests of stakeholders a business needs competent, informed, ethical and socially responsible managers.

In a desire to reconcile the conflicting interests of the various stakeholders, some businesses use a process of stakeholder engagement (see the following Snapshot). **Stakeholder engagement** refers to businesses sharing information with and seeking input from stakeholders, and involving them in decision making. Businesses anticipate that by engaging stakeholders they are more likely to act in an ethical or socially responsible manner.

Businesses also anticipate that a positive image of the business will be maintained if all stakeholders have their expectations satisfied, leading to increased sales as well as an improved reputation for corporate social responsibility.

BizWORD

Stakeholder engagement *refers to businesses sharing information with and seeking input from stakeholders, and involving them in decision making.*

Case study: The ABC stakeholder engagement

Founded in 1929, the Australian Broadcasting Corporation (ABC) is Australia's national public broadcaster, owned and funded by the government. The corporation provides television, radio, online and mobile services throughout metropolitan and regional Australia, as well as overseas.

Not only does the ABC's *Corporate Responsibility Policy* reinforce its commitment to acting ethically and responsibly in all areas of its operations, it also outlines its commitment to engaging with both internal and external stakeholder groups. The ABC is committed to stakeholder inclusiveness and regularly provides opportunities for stakeholders to provide input into the content and sustainability-related subjects of the Corporation.

The ABC demonstrates an understanding of how each stakeholder contributes to their long-term propensity and routinely considers stakeholders' needs in business decisions. Some of the ABC's stakeholder engagement mechanisms have included:

- the annual *ABC Appreciation Survey* conducted in 2016 by OmniPoll. The objective of this survey was to provide an overview of community attitudes and opinions about the ABC. The survey was fielded nationally by telephone among 1913 people aged 14 years and over.
- formal audience feedback and complaints processes. Written complaints about issues such as factual inaccuracy, bias or inappropriate content are referred to the ABC's Audience and Consumer Affairs unit. They investigate written complaints and coordinate responses to them.
- online feedback mechanisms specific to ABC content areas.
- ABC Advisory Council processes. This Council was established in 1983 to provide advice to the Board on matters relating to the Corporation's broadcast programs.

The following are the ways in which the ABC manages the interests of different stakeholders.

Employees

The ABC has a diverse workforce and is committed to creating an environment in which its people can thrive and are motivated to deliver the very best content and services to audiences. To assist with this, the Corporation offers ongoing learning and development opportunities to staff. They also offer media leadership and scholarship programs as well as opportunities for work experience, cadetships and internships.

The ABC have developed policies and procedures regarding WHS, managing diversity, discrimination, bullying and other workplace behaviour. These documents set out the ABC's expectations regarding behaviour at work as well as their position on inappropriate behaviour incompatible with their values. The Corporation also reports yearly on their equity and diversity performance.

Community

The ABC plays an important role in Australian communities, not only because of the content that is broadcast and published, but also because employees live and work in those communities. The ABC's Charter includes an obligation to 'broadcast programs that contribute to a sense of national identity … and reflect the cultural diversity of the Australian community'. Promoting and contributing to culturally significant issues and activities is fundamental to their content strategy.

The ABC *Stretch Reconciliation Action Plan 2016–18* (RAP) committed the Corporation to a long-term strategy to improve opportunities for Indigenous Australians in the areas of employment, content, community links, and cultural understanding and respect. A key aspect of this strategy is to increase Indigenous employment opportunities at the ABC.

Environment

Since the provision of broadcasting and online services is energy intensive, energy consumption, waste, water consumption, fuel consumption and recycling activities are monitored and reported on. The ABC has set targets to reduce its carbon

SNAPSHOT



'… its commitment to engaging with both internal and external stakeholder groups.'

emissions and each year initiatives are introduced to reduce the environmental impact of the materials they use. Operational decisions are guided by the ABC's *Environmental Management Policy (internal)*.

SNAPSHOT QUESTIONS

1. **Identify** the ABC's stakeholders.
2. **Outline** some of the ABC's stakeholder engagement methods.
3. Complete the following table to **demonstrate** how the ABC engages with its stakeholders.

Stakeholder	Description	Engagement method
Employees		
Community		
Environment		
Other		

4. **How** can the management of conflicting stakeholder interests lead to a business being viewed as socially responsible?

on Resources

Weblink: ABC

SUMMARY

- Stakeholders are groups and individuals who interact with the business and thus have a vested interest in its activities.
- Society increasingly expects businesses to accept responsibility and accountability towards all stakeholders.
- Stakeholder expectations can be compatible or incompatible.
- Managers need to reconcile the conflicting interests of various stakeholders.
- Senior managers must attempt to satisfy as many stakeholder expectations as possible.
- Economic development must be accomplished sustainably.
- The triple bottom line refers to the economic, social and environmental performance of a business.
- Reconciling the conflicting interests of stakeholders requires competent, informed, ethical and socially responsible managers.
- Stakeholder engagement is a process that assists in reconciling the conflicting interests of stakeholders.

EXERCISE 5.3 REVISION

1 Draw a table similar to the one below and **summarise** details of the management skills discussed in this section.

Skill	Definition	Characteristics	Application to the workplace

2 Peter Drucker stated that 'vision is the essential contribution of management'. **Explain** this statement.

3 **Outline** the relationship between 'vision' and 'leadership'.

4 (a) **Identify** two or three people who you consider to be effective leaders.
(b) Against each name, **outline** the personal qualities each person displays.
(c) **Determine** what leadership qualities the individuals have in common.
(d) **Compare** your answer with other class members.

5 **Recall** the six steps in a typical problem-solving process.

6 **Explain** the relationship between problem solving and decision making.

7 **Why** is it important for managers to be proactive rather than reactive?

8 **Define** the term 'stakeholder'.

9 **Recall** information to complete the following table. The first one has been completed for you.

Major stakeholders	Influence
Customers	Put pressure on business to satisfy their needs, act ethically and be socially responsible
Employees	
Shareholders/owners	
Society/physical environment	

10 **Demonstrate** the ways in which the interests of stakeholders' conflict.

11 **Distinguish** between compatible and incompatible expectations of stakeholders. Provide examples.

12 In small groups, **recommend** methods a business could use to reconcile the following conflicting interests.
(a) Consumers demanding cheaper products and employees wanting higher wages
(b) Shareholders desiring a higher return on their investment and society wanting a cleaner environment
(c) Managers being required to keep costs of production down and the government demanding improvements in occupational health and safety practices.

13 **Demonstrate** ways a business can show that it is acting in an ecologically sustainable manner.

14 **Explain** how stakeholder engagement can assist in reconciling the conflicting interests of stakeholders.

EXERCISE 5.3 EXTENSION

1 You have been asked to make a three-minute oral presentation at the local chamber of commerce meeting. The topic you have selected is 'The essential skills of management'. **Investigate** the topic and present your report to the class. For each skill, include a definition of the skill, its characteristics and application to the workplace. You might like to use PowerPoint to present your lecture.

2 (a) **Identify** the major stakeholder groups often mentioned in relation to social responsibility.
(b) **Analyse** to what extent these groups apply to your school.
(c) **Determine** what other stakeholders you might add.

3 'To be effective, corporate strategy must take into account the interests, needs, and expectations of all the business's stakeholders. Companies should have a strategy that combines business goals and broad social interests.' **Evaluate** this statement.

4 Complete the following table. **Propose** any skills that you think could be used to achieve the business goals, and **explain** how they could be used. The first two entries have been started for you.

Business goals	Skills	How
Improve the culture of a business	Communication	Explain to staff the changes that will take place.
	Problem solving	Use the problem-solving steps to work out what problems are preventing the culture from improving.
Successfully merge with another company		
Improve social responsibility		
Improve staff satisfaction		

5 **Investigate** online **BHP Billiton**'s Matched Giving program. **Evaluate** how this program would enhance the company's reputation for corporate social responsibility with its stakeholders.

on Resources

- **Weblink:** BHP Billiton
- **Digital doc:** Chapter summary (doc-26097)
- **Interactivity:** Chapter crossword (int-7219)
- **Interactivity:** Multiple choice quiz (int-7220)

CHAPTER 6

Achieving business goals

OVERVIEW

6.1 Introduction: What are goals?
6.2 Business goals
6.3 Achieving a mix of business goals
6.4 Staff involvement

6.1 Introduction: What are goals?

BizWORD

*A **goal** is a desired outcome (target) that an individual or business intends to achieve within a certain time frame.*

People start up a business because they want to achieve something; they have goals they want to attain. From an early age, you have been setting goals. A **goal** is a desired outcome (target) that an individual or business intends to achieve within a certain time frame. For example, when you were in primary school some goals you may have wanted to achieve could have included:

- learning to play a musical instrument
- becoming a member of a sporting team.

In secondary school, the goals will have changed and may now include:

- acquiring a part-time job
- improving your debating skills
- achieving the best possible results in Business Studies.

Success in achieving your goals is often determined by the amount of planning you undertake. Detailed planning increases the likelihood of successfully achieving your goals.

BizFACT

Although some people distinguish between goals and objectives, most managers typically use the terms interchangeably.



FIGURE 6.1 Just as many students are working towards the goal of getting into university for a specific course, goals are the targets that a business and its employees work towards.

As with individuals, businesses:

- need to establish goals
- are required to undertake planning to successfully achieve specific goals.

6.1.1 The importance of goals

Carefully prepared goals — begin with the end in mind — benefit managers by:

1. *Serving as targets*. With goals, managers at all levels would find it easier to make coordinated decisions because they understand what the business is trying to achieve.
2. *Measuring sticks*. Specific goals act as a **benchmark** against which the business can measure its performance — that is, the actual outcome is compared with the planned goal.
3. *Motivation*. Good quality goals represent a challenge — something to aim for. They act as a motivating force. Employees will gain satisfaction when they successfully achieve a challenging goal. Goals also provide managers with a basis for rewarding performance, which in turn acts as a motivator.
4. *Commitment*. Getting an employee to agree to achieve a goal — or better still, having the employee participate in the goal-setting process — gives that employee a personal stake in the success of the business.

BizWORD

*A **benchmark** is a standard by which something can be measured or judged.*



FIGURE 6.2 Once a business has well-constructed goals, the next step is to communicate them effectively to employees. Employees who understand a business's goals are much more likely to work towards achieving them. If employees are unaware of the goals, then goal-setting is futile. A study in *Harvard Business Review* found that 70 per cent of employees were unable to identify their company's objectives, given a choice of six options. Communication is essential to strategic planning.

BizFACT

When communicating about the business plan and goals, managers have to focus not only on addressing the what, when and how, but more importantly the why. The why is what most employees want to understand and it's often the one thing managers leave out when communicating goals to their staff.

To be most effective, business goals should be S.M.A.R.T (see the following Snapshot).

SNAPSHOT

S.M.A.R.T. goals

Using the **S.M.A.R.T.** technique — a common acronym in goal setting — is the best method for writing effective goals. Using this technique will help the business owner to define the goals more easily, and the details involved in achieving them. S.M.A.R.T. goals should be:

1. ***S****pecific*. Goals should be straightforward and emphasise what the business wants to happen.
2. ***M****easurable*. Decide on goals whose progress can be measured so the business owner can see the change occur. This helps the business stay on track.

3. ***A**chievable*. Goals need to be challenging but not be too far out of the business's reach, otherwise the business owner and employees will become unmotivated due to the lack of success.
4. ***R**ealistic*. The goals must represent something that the business owner and employees are both willing and able to work towards.
5. ***T**imebound*. The goals must have deadlines and sub-deadlines attached to them, otherwise the commitment is too vague.

Let's look at an example of a business goal to see how we can turn it into a S.M.A.R.T. goal. Let's imagine a business had the following overall goal:

- I want to grow my cleaning business.

Now, let's turn it into a S.M.A.R.T. goal:

- Specific: I will gain five new clients for my business.
- Measurable: I will measure my progress by keeping track of how many new clients I gain, while maintaining my current client base.
- Achievable: I will gain five new clients as I currently have five available spaces in my fortnightly client scheduling diary.
- Realistic: Adding clients to my customer base will allow me to grow my business and increase my income.
- Timebound: I will have five new clients within four months.

S.M.A.R.T. goal: I will gain five new clients for my cleaning business within a four-month period, filling my current available diary places. This will allow me to grow my business and increase my revenue.

SNAPSHOT QUESTIONS

1. **State** what the acronym S.M.A.R.T. represents.
2. **Construct** a S.M.A.R.T. goal for the following overall goal, using the process outlined in the Snapshot: 'Increase sales for my gardening business'.

SUMMARY

- People start a business because they want to achieve something: they have goals they want to attain.
- A goal is a desired outcome (target) that an individual or business intends to achieve within a certain time frame.
- Success in achieving your goals is often determined by the amount of planning you undertake.
- Carefully prepared goals benefit managers by:
  - serving as targets
  - measuring sticks
  - motivation
  - commitment.
- The best method of writing effective goals is by using the S.M.A.R.T. technique.

on Resources

Weblink: SMART

EXERCISE 6.1 REVISION

1 **Define** the term 'goal'.

2 **Recall** what often determines the success in achieving goals.

3 (a) **Describe** two personal goals.
(b) **Identify** when you want to achieve them.
(c) **Outline** what planning will be required to achieve these goals.

4 **Discuss** what is meant by the statement 'begin with the end in mind'.

5 **Summarise** how carefully prepared goals will benefit managers.

6 **Identify** a benchmark you use to assess your achievement in Business Studies.

7 Read the following two statements. Decide and **justify** which one is a goal and which one is not.
(a) 'To improve customer service.'
(b) 'To respond to every customer enquiry courteously and completely within three hours.'

EXERCISE 6.1 EXTENSION

1. 'We plan to expand our market into Asia, increasing worldwide market share by 2 per cent over the next three years.' **Determine** whether this goal is more likely to belong to a large or small business. Give reasons for your answer.
2. Reflect on a goal you have recently achieved. **Analyse** the reasons why you were successful in achieving this goal.
3. Using the S.M.A.R.T. technique, **create** a suitable goal for the following businesses:
   (a) Blue Hills Corner Store
   (b) Evergreen Nursery
   (c) Banthai Restaurant.

6.2 Business goals

In most cases a driver of a car knows his or her final destination and has a plan of how to get there. All organisations should set goals. This increases their chances of success. Figure 6.3 illustrates six common business goals.

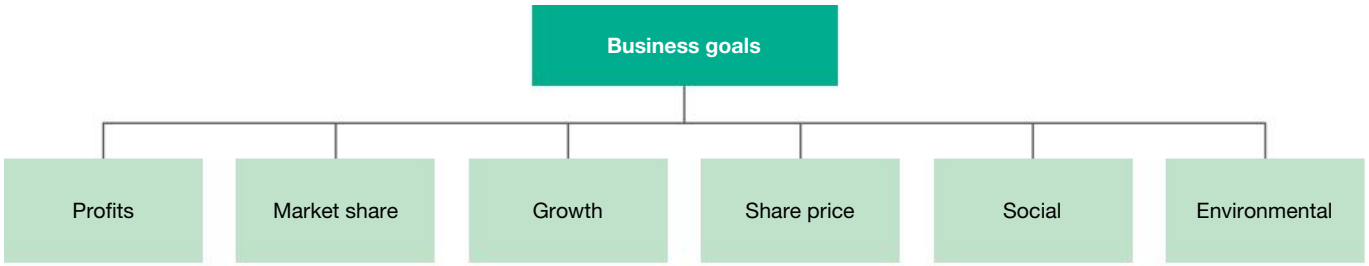


FIGURE 6.3 Common business goals

6.2.1 Profits

Have you ever saved enough money to purchase an expensive item? If so, you probably kept a record of all the money you received (revenue), the money you spent (expenses) and the resulting balance. These records provided you with information about your cash flow position. As you saved more and the balance increased, you were able to determine how close you were to achieving your financial goal. One of the most basic financial goals for businesses is to maximise profits.

As explained in chapter 1, profit is what is left after the costs of producing and supplying the product (expenses) have been deducted from money earned from sales (revenue). If the business is unable to consistently make a profit, it will fail. Only profitable businesses survive in the marketplace.

A major indicator of a business's success is the size of its profit, so many businesses not only want to make a profit, they want to maximise their profit. **Profit maximisation** occurs when there is a maximum difference between the total revenue (that is, the number of sales made multiplied by the price) coming into the business and total costs being paid out (see figure 6.4). The goal of seeking to make as much profit as possible is probably pursued by a larger number of businesses than any other goal.

BizFACT

Many people criticise businesses that are overly focused on profit maximisation. This objective illustrates to stakeholders that the business's primary focus is on profits and that it will do whatever it can to achieve this goal, regardless of the consequences or risks involved. Short-term profit maximisation can lead to a negative public perception and can ultimately affect future sales.

BizWORD

Profit maximisation *occurs when there is a maximum difference between the total revenue (that is, the number of sales made multiplied by the price) coming into the business and total costs being paid out.*

Total sales × price = Total revenue (TR)
Total expenses incurred in operating the business = Total costs (TC)
Profit = TR – TC
Maximum profit = TR at maximum difference from TC

FIGURE 6.4 Profit maximisation

BizFACT

Not all businesses aim for profit maximisation. Some organisations engage in business-related activities, but their aims and objectives are different; e.g. non-profit organisations do not earn profits for their owners, instead, all the money earned or donated is used in pursuing their objectives.

One way of maximising profits is to increase sales. This may be done by lowering the price so consumers purchase more. Alternatively, the business may seek to increase sales through a well-targeted marketing campaign or creating more innovative products or delivering better services.



FIGURE 6.5 There are many ways businesses can increase profit. Price may be lowered to increase the volume of sales or clever advertising may convince the consumer to buy a product.

BizWORD

Market share *refers to the business's share of the total industry sales for a particular product.*

BizFACT

Woolworths and Coles account for approximately 70 per cent of the supermarket industry market share, with 35.7 per cent and 33.2 per cent market share respectively. Aldi's market share has increased to 13.2 per cent and IGA has fallen slightly to 9.3 per cent market share. The two major supermarket chains are continually revising their marketing strategies in an attempt to grab market share.

The profit maximisation goal is likely to be more beneficial to a business if adopted over the long term. Ironically, this may require a business to accept either lower profits or losses in the short term. A business entering a new market or introducing a new product, for example, usually performs best by initially setting low prices to build a large customer base. This is a strategy that Virgin Airlines adopted when it entered the Australian market. It offered cut-price airfares to tempt passengers away from the established carriers. Virgin has as its long-term goal 'the desire to maximise profits', but they realised it would take a number of years to achieve.

6.2.2 Market share

Market share refers to the business's share of the total industry sales for a particular product. This is easy to visualise using a pie chart that shows the percentage of sales the business has in relation to all its competitors. In most industries, market share is usually a goal for only large businesses. Such businesses often develop an extensive product range, using many different brand names to gain an extra few percentage points of market share. Small market share gains often translate into large profits for these

businesses. Bauer Media Group is Australia's leading magazine publisher. They publish more than 30 magazines across a wide range of categories and sell around 35 million magazines a year. The company is home to the highest-selling monthly magazine (*The Australian Women's Weekly*), Australia's best-selling weekly (*Woman's Day*), along with top-selling titles in women's lifestyle (*Cosmopolitan*), youth (*Dolly*), homemaker (*Australian House & Garden*), and business/financial (*Money*). Overall, Bauer Media Group currently captures about 50.8 per cent of the total Australian magazine market share. The company has recently gained momentum in capturing market share due to the introduction of their multichannel approach to content, e.g. digital magazines.

Increasing market share is an important goal for businesses that dominate the market, because small market gains often translate into large profits (see the following Snapshot).

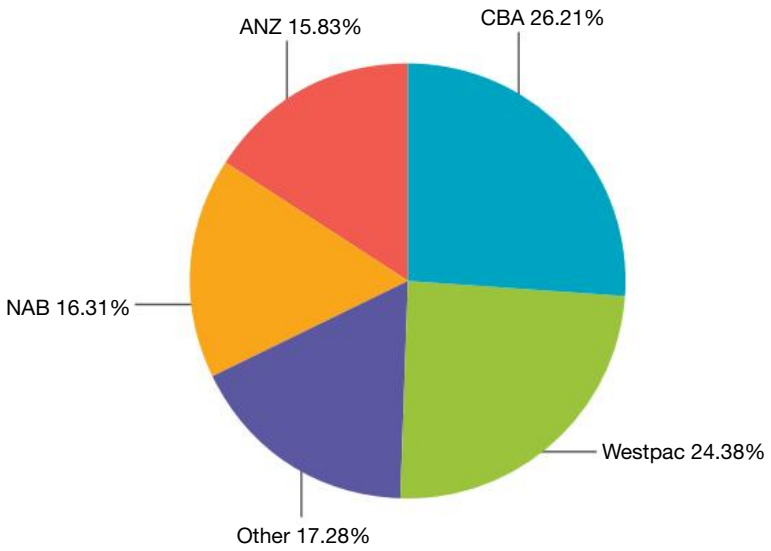


FIGURE 6.6 Competition between the major Australian banks and second-tier banks has resulted in a declining overall market share for the big four. For the third consecutive year, non-major banks and other institutions have taken market share away from the big four. This is despite the market share of the big four banks increasing in relation to loans.

Lack of competition is why government is moving so hard against the banks

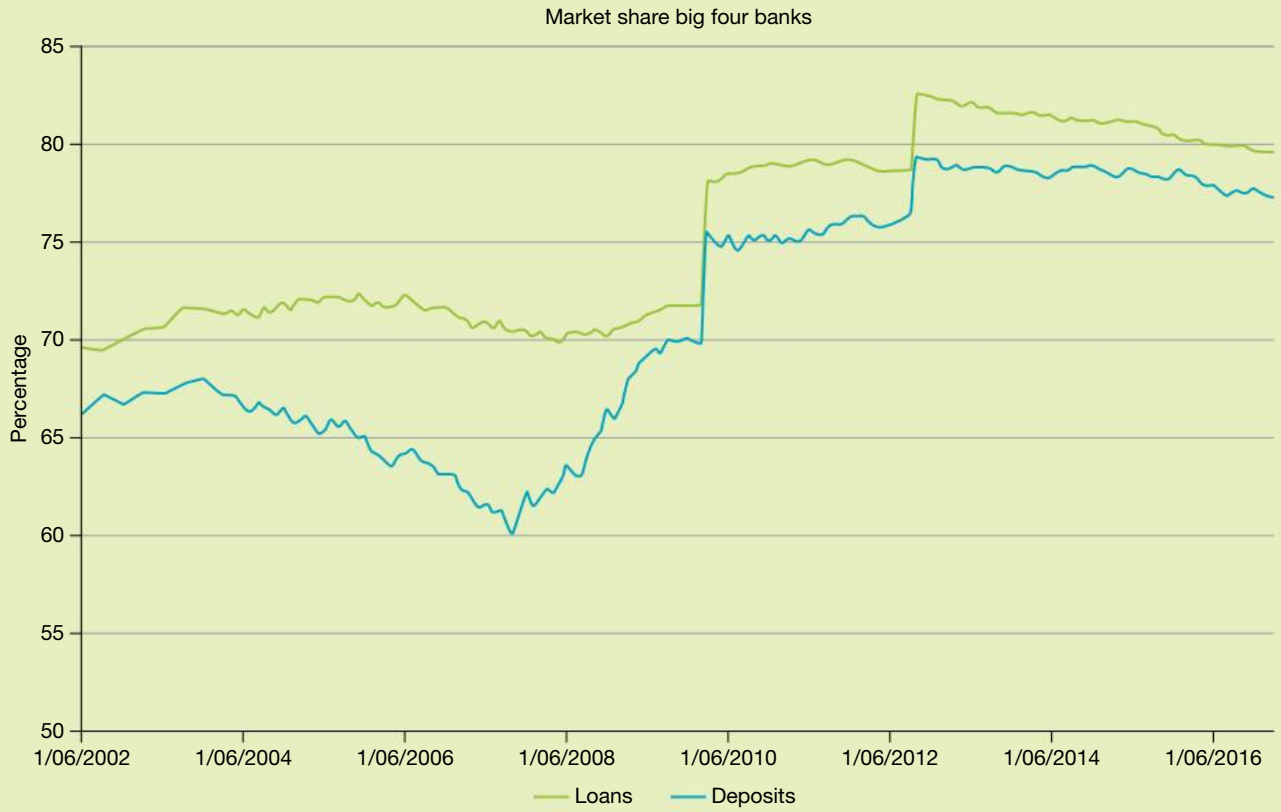
SNAPSHOT

With its latest budget, the government has made a number of moves to create a level playing field in the banking system. It's taxing the five largest banks, announced a review of rules around data sharing, a new dispute resolution system for banks and other financial institutions, and new powers for the regulator to make bank executives accountable.

All of these changes come after a decade of consolidation and upheaval in the financial system, which has hurt competition and increased risk.

The chart on the following page shows the market shares of the big four Australian banks in terms of Australian loans and deposits.





As you can see, since 2002 their market share has grown from 69.7% to 79.6% for loans and from 66.3% to 77.3% for deposits. Also, the gap between market dominance in loans versus deposits has closed since the global finance crisis. This means the big banks are attracting a greater share of bank deposits, which has an impact on the smaller banks.

With limited access to deposits, which is a relatively cheap way of raising capital, smaller banks have had to rely on the more expensive wholesale debt markets. Small banks also have difficulties to tap other funding sources such as covered bonds. This makes their products less competitive, and they have struggled as a result.

In part, that's because a number of banks disappeared or merged with the big banks after the global financial crisis. This includes St George, Bankwest, Bendigo Bank, Aussie Home Loans, Adelaide Bank, RAMS and Wizard.

In addition, rising house prices have led to a further increase in the concentration of mortgage and other housing loans in the Australian banking system. Today Australian banks have about twice as many mortgages on their books as in the next highest developed economy.

New financial startups, such as peer-to-peer lenders, have entered the banking system. In time they may rival the big banks in areas like personal lending, but they remain small in terms of market share. And the big banks' unwillingness to share data may be a hindrance.

Something needed to be done

The concentration in the banking sector does not provide the best outcome to all Australians. It has led to a low range and low quality of financial services as well as high costs. This needed to be addressed.

The new banking levy will support competition, as it pushes up the cost for the big banks. The review into data sharing could also be a boon to financial startups and other competitors, although we don't yet know what the outcome will be.

But even stronger government actions may be needed to create a level playing field. The government should consider separating out of the retail arms, from the other areas, of the large banks. Failing that, the low capital buffers of the big banks need to be addressed.

Source: Harry Scheule, 'Lack of competition is why government is moving so hard against the banks', *The Conversation*.

SNAPSHOT QUESTIONS

1. **Identify** some of the ways in which the government has tried to create a level playing field in the banking industry.
2. **Describe** the market share of the four major banks.
3. **Why** have small banks found it so hard to compete?
4. **Explain** why the government has introduced these new measures to support competition in the banking industry.

The market share of SMEs is usually restricted to the size of the business. A local corner store's market share, for example, is limited to the number of customers living within its immediate area.

One of the most successful strategies used to increase market share is promotion. **Promotion** describes the methods used by a business to inform, persuade and remind a market about its products. Promotion can be used to convince new customers to try a product, while maintaining established customers' product loyalty. Advertising that emphasises the product's features also assures those who *do* use the product that they are making the right decision.

BizWORD

***Promotion** describes the methods used by a business to inform, persuade and remind a market about its products.*

6.2.3 Growth

Most businesses want to grow. They can achieve growth internally (organically) or externally. Internal growth could involve employing more people, increasing sales, introducing innovative products, purchasing new equipment or establishing more outlets. McDonald's has pursued an ambitious growth program by selecting a large number of sites for future expansion.

External growth is achieved by merging with or acquiring other businesses. A merger occurs when two businesses join together to become one — for example, when the airline company Qantas joined with Jetset Travel. Expansion can also take place through acquisition. This means that one business purchases another business — for example, when Coca-Cola Amatil purchased Neverfail Springwater and Mount Franklin bottled water suppliers; SPC Ardmona, IXL and Taylor's food products; and Goulburn Valley packaged ready-to-eat fruit merchandise.

Maximising growth is not a goal that only large businesses can achieve. Many successful SMEs have followed similar strategies and in the process expanded to become large businesses. However, some small business owners are content to maintain the existing size of their business to:

- avoid the added pressures of expansion in a desire for a quiet life or a particular lifestyle
- keep control over the business's operations
- maintain personal contact with the customers.



FIGURE 6.7 Mike Cannon-Brookes and Scott Farquhar co-founded Atlassian, an enterprise software company currently worth $5 billion, in Sydney in 2002. Their strategy for continued growth has been through mergers and acquisitions. The pair have expressed their intention to continue looking for bolt-on acquisitions to help them grow further.

6.2.4 Share price

A **share** is a part ownership of a public company. Shareholders therefore are the real owners of companies. There are two reasons why a person will buy shares. Firstly, they may purchase shares in the hope of selling them for a higher price. Secondly, owning shares in a company entitles an investor to a part of the company's profits, which is distributed in the form of dividends.

BizWORD

*A **share** is a part ownership of a public company.*

For companies that wish to be successful, they need to maximise the returns of their shareholders. This is achieved by keeping the share price rising — constantly improving the share price — and paying back healthy dividends. This is a goal that Wesfarmers has been trying to achieve over the past decade (see figure 6.8).

Of course, businesses must be aware that they operate within a wider community that expects corporations to act ethically. Unethical activities may temporarily improve a company's share price but ultimately end up being detrimental to a business.

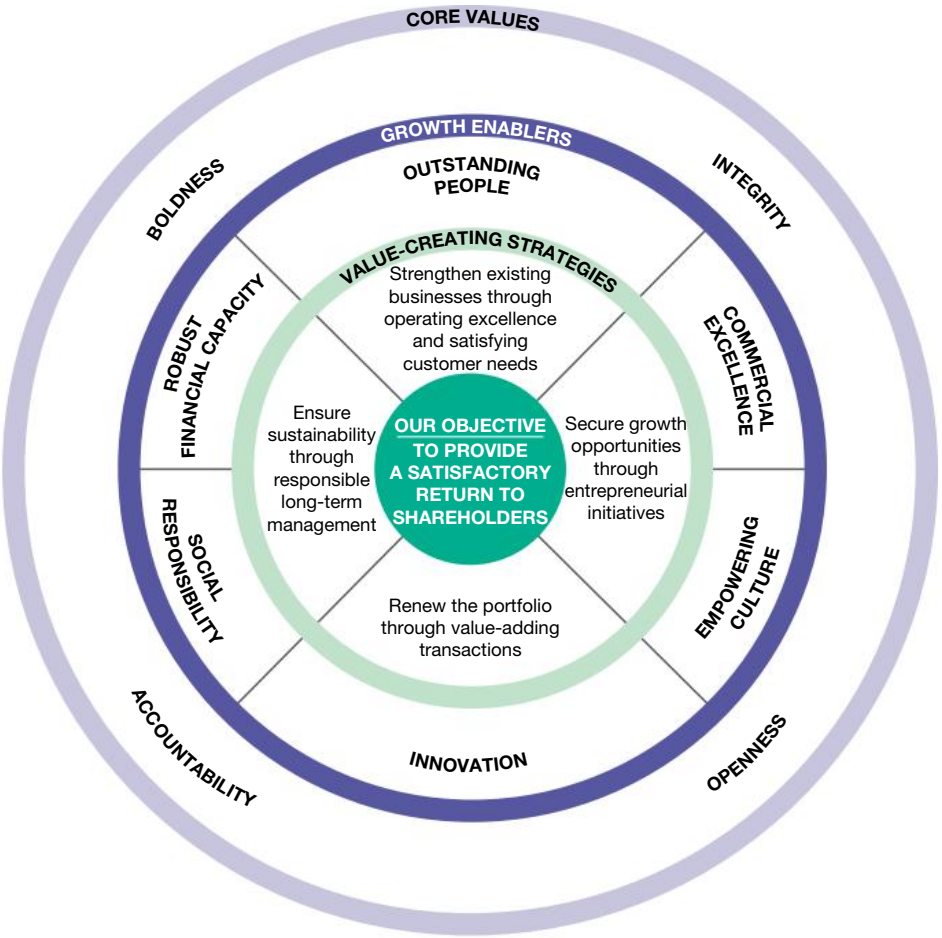


FIGURE 6.8 Wesfarmers' primary objective is to provide a satisfactory return to its shareholders. The measure used to assess the achievement of the objective is total shareholder return over time. The company measures its performance by comparing its return against those achieved by the S&P/ASX 100 Index, i.e. Australia's top 100 companies.
Source: Wesfarmers

BizFACT

Through its numerous values and campaigns, The Body Shop expresses its commitment to social and environmental justice on a local and global level. Recent campaigns include 'Walk in her shoes', 'Stop sex trafficking of children and young people', 'Climate friendly', 'Rethink refugees' and 'Stop violence in the home'. The Body Shop prides itself on being a retail activist.

6.2.5 Social goals

All businesses operate within a community and, like individuals, have certain social responsibilities. Many businesses develop social goals and adopt strategies that will benefit the community, while achieving financial goals. Among the main social goals are:

1. *Community service*. Business sponsorship of a wide range of community events, promotions and programs rapidly increased during the past decade. Many businesses financially support educational, cultural, sporting and welfare activities.
2. *Provision of employment*. Most large businesses do not regard employment of people as a main goal. Many small business owners, however, look at the continuity of their business, sometimes employing family members who otherwise might be unemployed.
3. *Social justice*. Everyone has the right to be treated fairly. A business may be concerned for **social justice** — that is, it adopts a set of policies to ensure employees and/or other community members are treated equally and fairly.

BizWORD

Social justice *in business is about adopting a set of policies to ensure that employees or other community members are treated equally and fairly.*

Case study: BHP's commitment to social goals

BHP are committed to contributing to society through engagement and advocacy on important issues and by supporting targeted development areas to benefit the communities where they operate. One of their priorities is social investment, as can be seen by the Social Investment Framework.

Our Social Investment Framework

We have a responsibility to make a positive contribution to sustainable development and have a longstanding commitment to invest one per cent of our pre-tax profits in programs that aim to improve the quality of life for people around the world. In the 2016 financial year, this investment totalled US$178 million, which is in addition to the economic value that our operations bring to our host communities. We invest directly to support our local host communities and donate to the BHP Billiton Foundation which invests in global and national projects.

Through our Social Investment Framework we aim to make a distinctive contribution to some of the most pressing sustainable development challenges of our generation. Our Framework was implemented in 2015 and underpins our voluntary social investment from the 2016 to 2020 financial years. It aligns strongly with the United Nations Sustainable Development Goals which are most relevant to our business and society. This approach means we can work in genuine partnership with others towards shared outcomes, with a focus on three themes.

Governance

We aim to contribute to good governance with a focus on reducing corruption, enhancing transparency and strengthening of institutions.

Our strategic theme of Governance is deliberately aligned to the following UNSDGs:

- Decent work and economic growth
- Industry, innovation and infrastructure
- Peace, justice and strong institutions
- Partnership for the goals.

Human capability and social inclusion

We aim to enhance human capability and social inclusion through increasing the number of people with improved health and wellbeing, access to quality education and vocational training and enhanced livelihood opportunities.

Our strategic theme of Capability and Inclusion is aligned to the following UNSDGs:

- No poverty
- Quality education
- Gender equality
- Decent work and economic growth
- Reduce inequalities
- Partnership for the goals.

Environment

We aim to contribute to enduring environmental and social benefits through biodiversity conservation, water stewardship and climate change mitigation and adaptation.

Our strategic theme of Environment is aligned to the following UNSDGs:

- Clean water and sanitation
- Sustainable cities and communities
- Climate action
- Life below water
- Life on land
- Partnership for the goals.

SNAPSHOT



'We have a responsibility to make a positive contribution to sustainable development …'

Working with our host communities

As part of making a valuable contribution as community partners, we seek meaningful long-term relationships that respect local cultures and create lasting benefits. We aim to support the development of diversified and resilient local economies that contribute to quality of life improvement that continues beyond the life of our operations.

We base our relationships on open communication, trust and mutual respect to achieve a clear understanding of the context and impacts of our operations. Our approach also informs how we can make a meaningful contribution to economic and social development in our communities with a focus on the themes of our Social Investment Framework.

We use a data-driven approach to understand the specific requirements of each community and the opportunities that exist to make a positive contribution. Projects are designed and implemented with the participation of representatives of the local community.

Matched Giving Program

We encourage employees who are active citizens in their communities to support local charitable organisations. Our global Matched Giving Program recognises the contribution of our employees by matching their personal financial donations up to a specific cap.

In FY2016, more than 7500 of our employees participated in the Matched Giving Program. Employee contributions benefited 768 not-for-profit organisations, which received over US$7.3 million as part of the program.

Source: BHP Billiton Ltd.

SNAPSHOT QUESTIONS

1. **Outline** how BHP demonstrates its commitment to sustainable development.
2. **How** does BHP contribute to good governance, human capability and social inclusions and the environment?
3. **Explain** how BHP creates meaningful relationships with local cultures.

BizFACT

Since 2005, Corporate Knights has put together the Global 100, an annual list of the world's most sustainable companies. They consider about 4000 companies with market values of at least $2 billion and rate firms on 14 key measures. In 2017, the top five most sustainable companies were:

1. *Siemens, Germany*
2. *Storebrand ASA, Norway*
3. *CISCO, USA*
4. *Danske Bank, Denmark*
5. *ING Group, Netherlands.*

6.2.6 Environmental goals

Imagine that the world is like a business. As owners of this business you would be concerned about its future prospects. Every year, more output is demanded and consequently its production lines work faster and faster. However, the raw materials used to produce the vast array of goods and services are shrinking at a frightening rate. In the effort to increase output, essential maintenance is sometimes ignored. The business's water and power supplies are under increasing threat. To continue this way will be unsustainable and the business will eventually fail.

Does this sound unbelievable? Possibly. But in many ways this is what is happening to the world we live in. For quite a while people have treated the Earth just as they like, without giving much thought to the long-term consequences. However, the past is catching up with us. It is obvious that we cannot continue as we have; things will have to change. And the good news is that these changes are already occurring. There are signs that people and businesses are becoming more environmentally aware. Enlightened businesses are adopting practices of 'recycle, renew and regenerate', as well as adopting a 'green' attitude, and developing products and creating ideas that are environmentally friendly (see figure 6.9). These business practices reduce the impact on the planet's health so that future generations are not disadvantaged.

Sustainable development

So far we have painted a somewhat bleak picture of the possible future. Fortunately, however, the world is moving away from many of its past practices. Economic growth must be achieved sustainably. Many in society now argue that economic growth should not occur at the expense of polluting and degrading the air, water



FIGURE 6.9 Eco Office Supplies is a national online retailer that specialises in the supply of environmentally sustainable office consumables for Australian workplaces. From the sourcing of products to delivery, Eco Office strives to minimise adverse environmental impacts in its operations and products. They embrace the three Rs of environmental management: reduce, re-use, recycle.

and forests that are essential to support life on this planet. There needs to be a balance between economic and environmental concerns — in other words, **sustainable development**.

BizWORD

Sustainable development
occurs when the needs of the present population are met without endangering the ability of future generations to meet their own needs.



FIGURE 6.10 Siemens was recognised as the world's most sustainable company in 2017. The German company supports a fundamental technological change: a shift toward energy-efficient economic development, renewable energy sources and environmentally friendly solutions. Its aim is to achieve a threefold benefit: for its customers who improve their competitiveness thanks to lower energy costs and higher productivity; for future generations; and for Siemens itself, by developing attractive markets and growing profitably.

BizFACT

According to the Global Footprint Network, we currently use the equivalent of 1.4 planets to provide the resources we use and to absorb the waste we produce. This is not sustainable. Based on estimates from the United Nations on resource use and population, the Global Footprint Network predicts that, between 2035 and 2050, we will reach the point where we need the equivalent of two planets to support us.

Businesses are starting to play their part in achieving sustainable development. Pressure to change has come from society's increasing awareness of environmental issues. As well, governments are imposing stricter environmental regulations on business practices. This will provide many new business opportunities for environmental services and products (see the following Snapshot).

SNAPSHOT



'… sustainability in action …'

Australian Sustainability Award winners

The Australian Business Award for Environmental Sustainability, conducted annually, recognises businesses that execute initiatives that demonstrate leadership and commitment to sustainable business practices.

Some of the 2017 winners included:

- **Fujitsu**. Fujitsu is a leading service provider of business and information and communications technology solutions. Data centres are facilities that house a large amount of powerful, networking computer servers. As greenhouse gas emissions have continued to increase, Fujitsu Australia partnered with the NSW Government to help bring about greater transparency in relation to measuring the power consumption and energy efficiency of data centres in Australia. This collaboration resulted in the National Australian Built Environment Rating System for Data Centres (NABERS for DC) — a star rating system to help drive greater efficiency in the industry, while also providing customers with a transparent and easily comparable rating system. This initiative led to Fujitsu's data centres now saving 27 gigawatt hours of electricity, avoiding 24 million kilograms of greenhouse gas emissions and operating 27 per cent more efficiently than the market average.
- **Macarthur Centre for Sustainable Living**. The MCSL is a non-profit, community-driven organisation supported by local Macarthur Councils and the Royal Botanic Gardens and Domain Trust. It provides an attractive community place where visitors can see sustainability in action. The MCSL is a showcase for sustainable homes and gardens, with the goal of promoting sustainable living. The unique facility is entirely self-sufficient: it generates its own power, recycles and reuses all rain and waste water, and manages all organic waste on site.
- **GJK Facility Services**: GJK is a provider of cleaning and related property services in Australia. It has implemented an Environmental Management System and a Green Procurement Policy that ensures all materials sourced are environmentally friendly, reduces the wastage of water and energy, and limits chemicals discharged into the environment. GJK strives to use biodegradable, sustainable and environmentally preferable products, as well as implementing strategies that ensure there is no chemical waste, reduce energy consumption and encourage paperless communications to name just a few. GJK head office has converted to 50 per cent renewable energy and created an Energy Action Plan so that it can continue to reduce its emissions. The company has created a guideline to promote the use of Green Equipment itself and for its clients, and staff are also encouraged to use a 'lights off policy', i.e. lights on only in the particular areas they are attending to.

SNAPSHOT QUESTIONS

Select one of the above businesses to answer the following questions. The **Sustainable businessess** weblinks will help you get started.

1. **Outline** the business's operations.
2. **Summarise** the business's commitment to the environment.
3. **Explain** the benefits of the business's environmental initiatives.

on Resources

Weblinks: Sustainable businesses

A 2008 IBM worldwide survey of senior executives highlights this business shift towards sustainability. Sixty-eight per cent of business respondents said they were implementing sustainability 'as an opportunity and platform for growth', and more than 50 per cent said their company's sustainability activities were giving them an advantage over their top competitors.

Despite this positive shift, nearly two-thirds of businesses questioned by IBM admitted they didn't fully understand their customers' concerns around

sustainability. Understanding and responding to customers on this issue is vital for business relationships. As it currently stands, only 17 per cent of the IBM survey respondents said they really engaged and collaborated with customers regarding their sustainability activities.

6.3 Achieving a mix of business goals

The preceding sections outlined some of the financial goals of a business, as well as social and environmental goals. Businesses do not generally have only one specific goal; they have a range of goals because they have different stakeholders who each have different needs. Managers therefore have a mix of goals that they try to achieve simultaneously.

Most business goals are interdependent, that is, they all help the business achieve its prime function. Some goals are compatible in the sense that certain strategies implemented by the business in pursuit of a particular goal will actually assist in achieving multiple goals. For example, strategies employed by a business to achieve the goal of maximising growth may simultaneously help that business achieve the goals of maximising profits and increasing market share.

Sometimes it can be difficult for a business to achieve all of its goals simultaneously because the links between the goals make some of them incompatible; that is, they conflict with each other. Such a situation will force a business owner into deciding to adopt a compromised position; a trade off between conflicting goals. A business owner may face the dilemma of having to choose whether to maximise profits or increase market share. It is sometimes a difficult decision. You have probably faced a similar dilemma: for example, should you go to the movies or prepare for an exam? The two 'goals' are conflicting and, just like a business owner, you must make a decision.



FIGURE 6.11 Coca-Cola Amatil attempts to achieve a mix of business goals. Their current strategic objectives are to continue to provide sustainable returns that are superior to those of their competition; to invest in their capacity and encourage business growth; and to conduct business and operate within the community as a good corporate citizen.

BizFACT

In 2008, Unilever Australia commissioned AMR Interactive Research and Newspoll to look at Australians' attitudes towards corporations and sustainability. It found:

- *90 per cent wanted Australian businesses to invest more in sustainable practices*
- *72 per cent thought companies had a broad responsibility to act responsibly*
- *81 per cent thought companies could still make a profit while being environmentally responsible and taking the welfare of their workers into consideration*
- *64 per cent thought companies needed to focus on sustainability to maintain their future profits.*

SNAPSHOT



'Initially, Atlassian's goal was to gain 50 000 customers.'

Case study: Atlassian achieving a mix of business goals

Scott Farquhar and Mike Cannon-Brookes (pictured, standing left and right) started their enterprise software business in Sydney in 2002 as university drop-outs, working in a garage with some servers and $10 000 on a credit card. This young technology company now sells software to some of the world's largest companies, and has grown from two to more than 2200 employees. It is currently valued at $4.3 billion.

Initially, Atlassian's goal was to gain 50 000 customers. It has achieved this goal — more than 51 000 large and small businesses now use its products — but the company will not stop there. Atlassian has said that its objective is now 100 million monthly active users. Another of Atlassian's goals is to 'unleash the potential in every team'. Its products help teams to collaborate, build software and serve their customers better. Over time, the company's customers have begun to use its software in ways that the founders never imagined and Atlassian has changed its products accordingly.

Atlassian also pursues a range of social goals. It makes its software free for use by not-for-profit organisations and charities. Another way the company fulfils its corporate responsibility obligations is by donating 1 per cent of profit, products and employee time to charity. This pledge has raised more than $40 million, including funding for the education of thousands of children in developing countries.

SNAPSHOT QUESTIONS

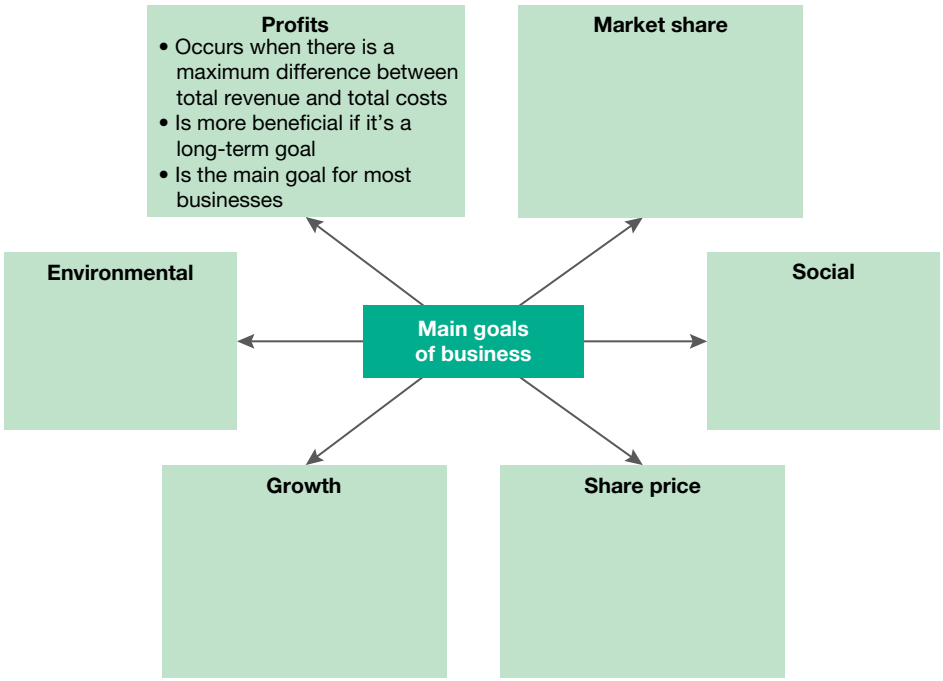
1. **Identify** and classify Atlassian's business goals.
2. **How** have these goals benefitted the company?

SUMMARY

- A business attempts to achieve a variety of goals. These goals relate to:
  - profits
  - market share
  - growth
  - share price
  - social
  - environmental.
- Profit maximisation occurs when there is a maximum difference between total revenue (TR) and total costs (TC).
- Market share refers to the business's share of the total industry sales for a particular product.
- A small change in a business's market share can result in a large change to its profit.
- A business can maximise growth either internally (organically) or externally.
- Companies need to satisfy their shareholders by improving the share price and paying healthy dividends.
- Many businesses develop social and environmental goals and adopt strategies that will benefit the community.
- There are three main social goals a business attempts to achieve:
  - community service
  - provision of employment
  - social justice.
- Enlightened businesses are adopting sustainable development practices.
- Managers should attempt to achieve a mix of the above goals.
- Managers often have to make a trade-off between conflicting goals.

EXERCISE 6.2 REVISION

1 **Construct** a concept map (started below) summarising the main goals of business.



2 In the following examples, **identify** which goal the business is trying to achieve.
(a) The business owner wishes to increase revenue so they conduct a large sale.
(b) A board of directors announces that the company's profits are forecast at 23 per cent over the next 12 months and the dividend will rise by 28 cents per share.
(c) A manager decides to undertake an extensive promotional campaign in an attempt to attract new customers.
(d) Senior executives knew there was only one way to expand the business and that was by buying the opposition.

3 'The main goal of a business is to maximise profits'.
(a) **Define** the term 'profit maximisation'.
(b) **Recount** under what circumstances a manager may be prepared to accept reduced profits in the short term.
(c) In your opinion, **discuss** whether maximising profits should be the only goal of a business.

4 **Describe** two strategies a manager can use to maximise profits.

5 **Why** is profit maximisation more suitable as a long-term goal?

6 Go online to access the latest Coca-Cola Amatil Fact Book. The **Coca-Cola Amatil** weblink in the Resources tab may assist. Then:
(a) **identify** the five products that have the greatest market share
(b) **discuss** why Coca-Cola Amatil wants to increase its market share for each of its products.

7 **Recommend** three strategies either Coles or Woolworths could use to increase their market share. Share your answer with other class members.

8 **Distinguish** between internal and external growth.

9 **Why** are some small businesses content to maintain their existing size?

10 **Outline** the relationship between a shareholder and a public company.

11 **Define** the term 'share'.

12 **Explain** why some companies may not be able to constantly improve their share price.

13 **Summarise** the three main social goals of a business.

on Resources

Weblink: Coca-Cola Amatil

14 **Identify** three examples that demonstrate businesses are becoming more environmentally aware.

15 **Justify** why businesses should adopt sustainable development practices.

16 Using an example, **demonstrate** how business goals can be compatible.

EXERCISE 6.2 EXTENSION

1 Set up a class debate to **critically analyse** the following topic: 'All businesses care about is making as much money as possible'. Share roles so that those not debating are involved either in assisting with research, or in running the debate and keeping notes on both sides' arguments.

2 In small groups, arrange to interview a local small business owner to determine his or her main business goals. **Compare** and **contrast** them with what you have learnt from this topic. Present your findings to the rest of the class.

3 'A business's financial goals sometimes conflict with each other'. **Evaluate** this statement.

6.4 Staff involvement

BizWORD

Staff involvement *means involving employees in the decision-making process and giving them the necessary skills and rewards.*

BizWORD

Labour productivity *measures how much an employee can produce in a set period of time.*

One important goal that all businesses should give a high priority to achieving is that of staff involvement. Sometimes referred to as employee empowerment or employee participation, **staff involvement** means involving employees in the decision-making process and giving them the necessary skills and rewards.

Employees are a business's most important resource. It is important to recruit and select appropriate employees. It is then vital to provide a work environment that maximises employee involvement and satisfaction because this results in high levels of output. Therefore, managers should pursue workplace practices that increase **labour productivity**. Policies that recognise the involvement, knowledge, skills and creativity of the employees will lead to increased productivity and long-term business success.



FIGURE 6.12 There are many benefits of involving employees in decision making. Employees will feel more valued and, as a result, their motivation and morale will be higher. Also, when employees are involved in making the decision, they will usually raise their level of effort and commitment, which will increase the chances of success.

Staff involvement is a type of decentralisation that involves allowing employees some authority to make decisions. Employees are encouraged to accept responsibility for their work. In businesses where true staff involvement occurs, employees gain confidence in their ability to perform their jobs and influence the business's overall performance. One of the most influential results of staff involvement is that employees exhibit more determination and initiative in pursuing the business's goals. Overall, staff involvement provides two advantages: increased employee motivation and solutions to organisational problems. However, staff involvement will only be fully successful if a business provides employees with the necessary expertise as well as recognising the importance of:

- innovation
- mentoring
- motivation
- training.

6.4.1 Innovation

As we outlined in chapter 1, innovation occurs when a new idea is applied to improving an existing product or idea. With markets and competition becoming more global, Australian businesses are being forced to become more innovative. Often, a business can gain a competitive advantage if it innovates successfully. Therefore, all businesses should encourage an innovative business culture by recognising and encouraging one of the most important sources of innovative ideas: employees. For example, in 1968 Spencer Silver, a 3M technician, developed a 'low-tack' adhesive that would not stick — a glue that 3M considered a failure. The product was abandoned. However in 1973, another innovative 3M technician, Art Fry, in a moment of insight, realised the full potential of a reusable bookmark and went on to invent the Post-it Note. It was through the innovative potential of these two employees that the humble Post-It Note has become an absolute necessity in the office. As the basic product evolved into an entire product line, Post-It Notes are to be found in most schools, laboratories, libraries and in homes.

The innovative activities of staff are often referred to as the entrepreneurship within the business. More recently, employees who take on the entrepreneurial roles within businesses are called **intrapreneurs**. In some businesses, these creative people present some managers with a dilemma. Highly creative, innovative thinkers can be nonconformist in their behaviour and dress. Attempts to get creative employees to be conventional and follow the rules and regulations may actually suppress their creativity. However, if a business is to grow and to maintain its competitive advantage, then staff must be encouraged and given the opportunity to be innovative. The most important thing a business can do to achieve this successfully is to demonstrate that it values new ideas and solutions and it does this by taking them seriously. If a business just pays lip service to creativity then the employees quickly 'get the message' and stop coming up with original ideas. Other practices would include:

- rewards given to employees with innovative ideas that become profitable
- a trustful management that does not excessively control — micromanage — people
- sufficient financial, management, human and time resources to achieve goals
- not fearing the consequences of making a mistake
- use techniques such as brainstorming to encourage ideas.

6.4.2 Motivation

Why do some employees work harder than others? Why can an employee with average skills regularly outperform someone with outstanding abilities? The difference between the two employees is most probably their level of motivation.

on Resources

eLesson: Travel With Kidz (eles-0836)

BizFACT

According to the 2016 Global Entrepreneurship Monitor report, Australia is the most intrapreneurial country in the world. While this may be the case, only 9 per cent of the adult population has taken part in the development or launch of new products or services, or in the creation of a new business unit.

BizWORD

*An **intrapreneur** is an individual who takes on the entrepreneurial roles within a business.*

BizFACT

Google is a company that embraces intrapreneurship by offering their employees a 20 per cent timeframe on developing personal projects relating to the business. One such project from an employee, Paul Buchheit, led to the creation of Gmail, which is now one of the most widely-used email platforms on the web.

BizWORD

Motivation *refers to the individual, internal process that directs, energises and sustains a person's behaviour.*

BizFACT

In an attempt to help employees with children better manage work and family, as well as improve the retention rates of women, an engineering firm AECOM will begin piloting a new program giving employees 12 weeks annual leave in their Australian and New Zealand offices. This is due to the recognition that many parents have often been forced to take leave without pay to help them deal with school holidays.

BizFACT

Research reveals that intrinsic motivation — motivation that comes from inside an individual — is a more long-term and powerful motivating force than any external or outside rewards such as money, grades or promotions.

Motivating employees is one of the most important management functions because high levels of motivation result in increasing rates of productivity. **Motivation** refers to the individual, internal process that directs, energises and sustains a person's behaviour.

Put another way, motivation is what drives a person to behave in a certain way, or to achieve a certain goal. For example, what motivated you to:

- return to Year 11 after completing Year 10
- complete the latest Business Studies homework exercises
- watch television instead of reading your English novel?

In a work setting, motivation makes people want to work, but what precisely is it that motivates people? This is a topic which is widely discussed, but often neglected in the workplace. This is mainly because it is an area of human behaviour which is difficult to understand given the conflicting answers provided by research.

For many years, managers have relied on the use of either rewards or punishments to motivate employees. An analogy is often used to try to explain what motivates people. It concerns a donkey and what is most likely to motivate it to move forward — that is, change its behaviour. According to the 'story' either a carrot can be dangled in front of the donkey (a reward) or it can be hit with a stick (a punishment). Either method may motivate the donkey. In the work environment, 'rewards' refer to increased pay and improved conditions, 'punishment' refers to fear of a reprimand, demotion or dismissal.

However, research over the last 70 years has revealed that motivation is much more complicated than just these two variables. Different theories have been formulated which lead to the conclusion that individual employees respond differently to various motivational techniques. Figure 6.14 outlines a number of motivational techniques that can be used. What they have in common is the need to develop a business culture that fosters employee welfare and involvement.

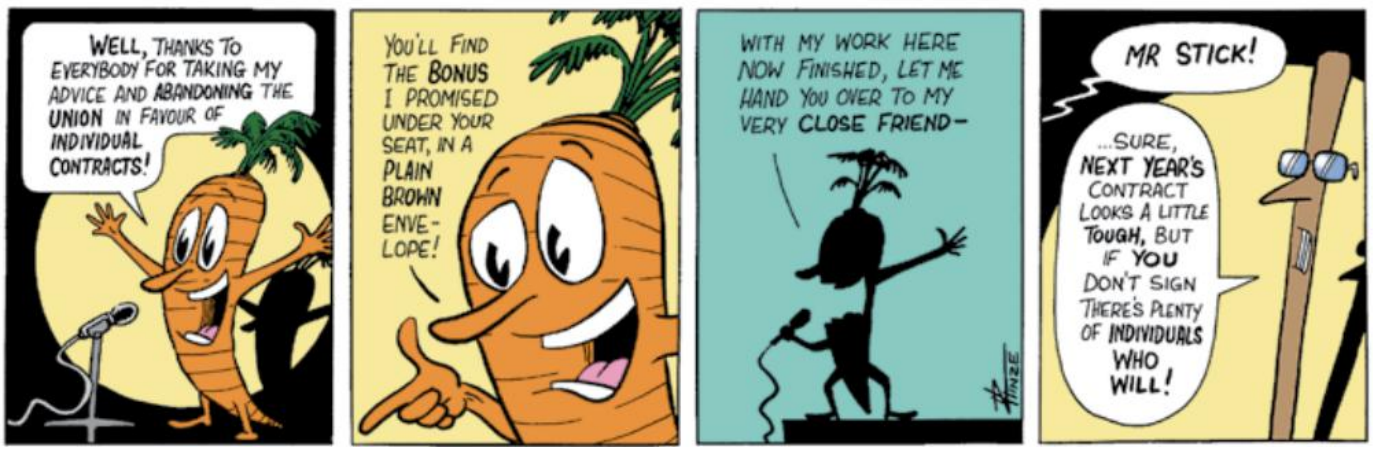


FIGURE 6.13 Motivation — carrot or stick approach

Is money the best motivator?

For generations managers have believed that money is the most powerful motivating force. However, recent research tends to suggest that employee motivation depends on a wide range of factors besides money (see the following Snapshot). For example, imagine you are offered $100 for each assessable task you complete satisfactorily. You would almost certainly be motivated to complete all your tasks. However, after a while your level of motivation would decrease as the stimulus from the financial incentive diminished. Eventually, you would desire a larger incentive to remain highly motivated. It could be argued, from this simple analogy, that money can be a

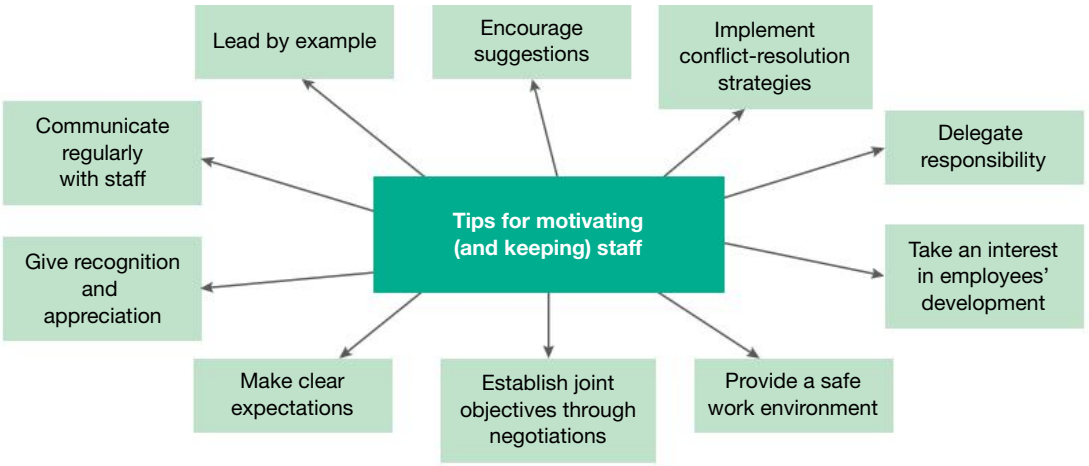


FIGURE 6.14 Non-financial rewards can have an even more substantial impact on employee satisfaction and motivation than traditional financial rewards. Motivational techniques that consider the emotional and physical wellbeing of employees lead to high morale, which in turn improves employee and business effectiveness.

powerful motivator but only in the short term. As the writer Neil Simon expressed it, 'Money brings some happiness. But, after a certain point, it just brings more money.'

The reality is that people want to be involved in their working lives. The successful businesses today will need to give close attention to involving employees in the decision-making process. Good managers should, therefore, also be good motivators, encouraging employees and using positive reinforcement to influence behaviour. The overall success of the business largely depends on motivated and skilled employees who are committed to its goals — that is, everyone working towards a common purpose.

Motivating people — getting beyond money

Offering financial rewards is often seen as the best way to motivate staff; however, many studies have shown that non-financial incentives can have an even more substantial impact on employee satisfaction and motivation than traditional financial rewards. Non-financial rewards can not only be cost-effective, they are crucial to making employees feel valued, as well as increasing productivity. Motivated staff are also more likely to stay, reducing separation, recruitment and hiring costs. So, what are the best incentives to motivate and retain staff?

1. **Recognition.** Thanks and praise are among the most common non-financial rewards people value. Feeling appreciated, validated and respected will increase motivation. The more sincere and heartfelt the appreciation is, the more likely someone is to feel rewarded. Managers can show their appreciation by commending or recognising employees for a job well done, sending an email recognising an employee's effort or congratulating a staff member during a meeting.
2. **Provide flexible working arrangements and a family-friendly workplace.** Offering flexible work hours that cater for the needs of employees allows them to achieve a positive work–life balance.
3. **Provide interesting work, including assignments that are challenging and rewarding.** Employees will find their jobs more enjoyable if they are more challenging and interesting. Offer opportunities for employees to work on projects in their own way and without unnecessary supervision.
4. **Train your staff.** Provide in-house or off-site courses that improve employees' skills.

SNAPSHOT



'Motivated staff are more likely to stay …'

5. **Offer opportunities for employees to advance.** Remember to meet your employees' needs as well as expecting them to meet the requirements of the business. If you can't offer promotion, a sideways move to a different position can also provide motivation.
6. **Show respect and courtesy.** This shows your employees that they are valued and improves morale, making for a better and more productive workplace.
7. **Listen to your staff to find out what motivates them.** What are their interests and aspirations? Time off to spend with family or greater autonomy and decision-making responsibilities may be more effective and meaningful incentives than a pay increase.

Non-financial rewards increase morale and productivity and are an important tool in improving staff retention, which can save a business money in the long term. When employees feel a sense of validation in addition to their pay, they are more likely to feel inspired to contribute. It's important to remember, however, that different employees will value different rewards. For example, some people like being publicly recognised for their efforts, while for others this would be excruciating. The right approach often depends on the person.

SNAPSHOT QUESTIONS

1. **Identify** the non-financial rewards that are effective in motivating staff.
2. **Explain** which non-financial reward would be most effective in improving your motivation.
3. Conduct a survey amongst friends and family about what best motivates them in their workplace, then **compare** and **contrast** your findings with the list in the article above.

BizWORD

Mentoring *is the process of developing another individual by offering tutoring and coaching, and modelling acceptable behaviour.*

Socialisation *is the process a new employee undergoes in the first few weeks of employment through which he or she learns how to cope and succeed.*

A **mentor** *is someone — usually a more experienced employee — who helps develop a less experienced employee (the protégé).*

6.4.3 Mentoring

When talking with school students or employees about their school or work experiences, it is common to hear them refer to individuals who influenced them. Many schools and businesses have introduced formalised **mentoring** programs, especially for new students or employees, with the aim of providing advice, guidance and to help with their **socialisation**.

Mentoring is normally done by tutoring, coaching and modelling of acceptable behaviour. Most importantly, though, a mentor acts as a role model. A **mentor** is someone — usually a more experienced employee — who helps develop a less experienced employee (the protégé). They act as a guide, teacher, counsellor, and coach. Such a practice is commonly referred to as taking someone under his or her 'wing'. Ultimately, the protégé learns acceptable attitudes and behaviours. For example, CompuServe, a computer wholesaler, encourages its experienced sales representatives to take new employees on sales calls to the company's largest customers. Teaching new employees what the business expects of them helps strengthen their dedication and commitment to the firm. It also helps to make sure that all employees are exposed to the values the business believes are important.

A formalised mentoring program is enormously beneficial because:

- it ensures access to mentors for all employees, regardless of levels of experience, backgrounds, gender or ethnicity.
- the participants in the mentoring relationship know what is expected of them. This is especially beneficial for new employees as it assists with their transition into the workplace.
- it assists with the training and development of all employees and passes on the skills and abilities of the more experienced staff members.
- it provides career and psychological support — a friend and counsellor — for inexperienced employees as well as allowing mentors to develop their interpersonal skills and provide a sense of satisfaction.
- it increases the possibility of skill transfer.

Mentoring in action

Some mentor programs fail because no clear goals and guidelines are established at the outset of the mentor/mentoree relationship. Ideally, programs need to be structured and overseen by Human Resource departments and work best when both participants are committed to the goals established. At the conclusion of a mentoring relationship, it is vital that an evaluation of the process takes place. Mentoring programs are one way in which companies can both retain and recruit staff.

Macy had been employed with Waratah Press for only a year since completing a communications degree. She was enjoying her role with the company as a junior editorial assistant within a small editorial team. For over 25 years, Waratah Press had offered custom printing and self-publishing services for clients with local printing or publishing needs. She really hoped that she could have a future there, honing her skills in copy editing and project management.

She particularly admired Judith Carew, who headed the managerial team and seemed to know everything about the business. Macy didn't report to Judith but knew if she had the opportunity, she could learn a lot under her guidance. So she was very excited when an internal email arrived in her inbox one morning announcing a mentoring program being introduced within the company. As soon as she could, she approached her supervisor, Curtis, to inquire whether she could apply to be a mentoree and whether Judith might be her mentor. He was supportive and suggested she fill in the expression of interest form and forward it to HR and Judith for consideration. Judith was agreeable and the company's first mentoring partnership began to take shape.

It took some time to establish the guidelines for the mentorship so that both Macy and Judith had a clear idea of the goals and the process for their achievement. They decided on a mentorship period of four months with fortnightly formal meetings as well as more informal contact on a weekly basis. The informal meetings would involve a brief 'catch-up' over coffee in the local café. During both types of meetings, Judith would aim to support Macy with her current projects, help her learn the 'ins and outs' of the industry and act as a 'sounding board' for Macy's questions and ideas.

In their debriefing with HR at the end of the mentorship, Macy felt she had increased her knowledge about the industry, confirmed her career directions and become a much more productive employee as a result. Judith indicated that being a mentor had also given her valuable insights into her own role with the opportunity to share information and resources in a positive way to contribute to the career development of a new employee. For the company overall, it seemed a way to retain staff who promised to be valuable to the company's future, as well as being able to promote the mentorship program as a way of recruiting new staff.

SNAPSHOT QUESTIONS

1. **Outline** the guidelines Judith and Macy established for their mentoring relationship.
2. **Identify** why some mentoring programs might fail.
3. **Assess** the benefits to (a) the mentoree, (b) the mentor and (c) the company of a successful mentoring program.

SNAPSHOT



'Judith would … act as a "sounding board" for Macy's questions and ideas.'

6.4.4 Training

As the nature of the workplace changes, especially due to the introduction of technology, existing employees must be trained and retrained. New employees also need some training, depending on their level of experience. **Employee training** generally refers to the process of teaching staff how to perform their job more efficiently and effectively by boosting their knowledge and skills. It may involve teaching them specific skills, and allows existing employees to continually upgrade their skills with the aim of developing **multiskilled** employees.

Mutiskilled employees are better able to:

- adapt to a rapidly changing technological environment
- provide better customer service

BizWORD

Employee training *generally refers to the process of teaching staff how to perform their job more efficiently and effectively by boosting their knowledge and skills.*

Multiskilling *allows employees to develop skills in a wide range of tasks through ongoing training.*

BizFACT

Ongoing training costs businesses on average $700 to $1100 per employee annually. While training is good for improving employee performance and retention, it can be quite expensive, especially for small businesses. In recent years, many businesses have moved to delivering staff training online. Online training is more cost effective and allows employees to learn at their own pace in a comfortable environment.

- participate effectively in work teams — as outlined previously, increased participation improves the range of ideas available to businesses keen to innovate to maintain their competitive advantage
- gain promotion and therefore their commitment to the business is greater.

The goal of training is to improve employee productivity. Informal on-the-job training is one of the most common training methods used. Formal off-the-job training, consisting of classroom teaching and lectures, is often used for highly skilled, technical employees. Conferences and seminars have become an important format for training in recent years. Businesses should view training as an investment in the human capital of the business, rather than just another expense. Training is necessary for both personal and business growth, as will be examined in more detail in chapter 8.

SUMMARY

- Staff involvement means involving employees in the decision-making process and giving them the necessary skills and rewards.
- A work environment that maximises employee involvement and satisfaction has high levels of labour productivity.
- Businesses should encourage an innovative business culture by recognising and encouraging one of the most important sources of innovative ideas: employees.
- An intrapreneur is an innovative employee who takes on the entrepreneurial roles within a business.
- Motivation refers to the individual, internal process that directs, energises and sustains a person's behaviour.
- Individual employees respond differently to various motivational techniques.
- Good managers should also be good motivators, encouraging employees and using positive reinforcement to influence behaviour.
- Mentoring is the process of developing another individual by offering tutoring, coaching and modelling acceptable behaviour.
- Teaching new employees what the business expects of them helps strengthen their dedication and commitment to the business.
- Employee training generally refers to the process of teaching staff how to perform their job more efficiently and effectively by boosting their knowledge and skills.
- The goal of training is to improve employee productivity.

EXERCISE 6.3 REVISION

1 **Define** the term 'staff involvement'.
2 Think of a situation where you were involved in the decision-making process.
   (a) **State** the decision that needed to be made.
   (b) **Describe** the decision-making process used.
   (c) **Outline** whether you were more committed to the final decision because of your involvement.
   (d) **Discuss** what implications this would have for you if you were a manager.
3 **Account** for the relationship between staff involvement and labour productivity.
4 **Why** should businesses encourage an innovative business culture?
5 **Discuss** the role an intrapreneur can play to assist a business maintain its competitive advantage.
6 **Determine** answers for the three questions on page 162 which analysed what motivated you to behave in a certain way.
7 **Calculate** which you believe to be the more powerful motivating force – rewards or punishment. **Justify** your answer.
8 **Why** is it important for businesses to mentor their employees?
9 **Explain** why spending on training should be considered as an investment and not just a business expense.

EXERCISE 6.3 EXTENSION

1. Suppose that you are the owner of a clothing store and you employ ten staff members. **Demonstrate** what staff involvement techniques you would use with these employees.
2. **Recall** a mentoring program you are familiar with.
   (a) **Investigate** the aim of the program.
   (b) **Evaluate** the effectiveness of the program.
   (c) **Recommend** changes you would make to improve the effectiveness of the program.
3. **Analyse** the system that is used in your school to motivate students. **Propose** how it could be improved.
4. **Investigate** the theories of motivation put forward by Abraham Maslow, Frederick Herzberg and Douglas McGregor. **Create** a written or oral report and present your findings.

on Resources

- **Digital doc:** Chapter summary (doc-26098)
- **Interactivity:** Chapter crossword (int-7221)
- **Interactivity:** Multiple choice quiz (int-7222)

CHAPTER 7

Management approaches

OVERVIEW

7.1 Introduction
7.2 Classical approach to management
7.3 Behavioural approach to management
7.4 Contingency approach to management
7.5 Compare and contrast approaches to management

7.1 Introduction

Management has been practised for thousands of years. The great pyramids of Giza in Egypt, for example, represent the combined efforts of more than 100 000 individuals who worked on the project over a 20-year period. This remarkable achievement was the result of well-coordinated management practices.

BizFACT

Like today's managers, the ancient Egyptian managers needed to:

- *develop plans*
- *acquire human and physical resources*
- *arrange finance*
- *analyse information*
- *keep records and prepare progress reports*
- *monitor performance and coordinate activities*
- *take corrective action whenever required.*

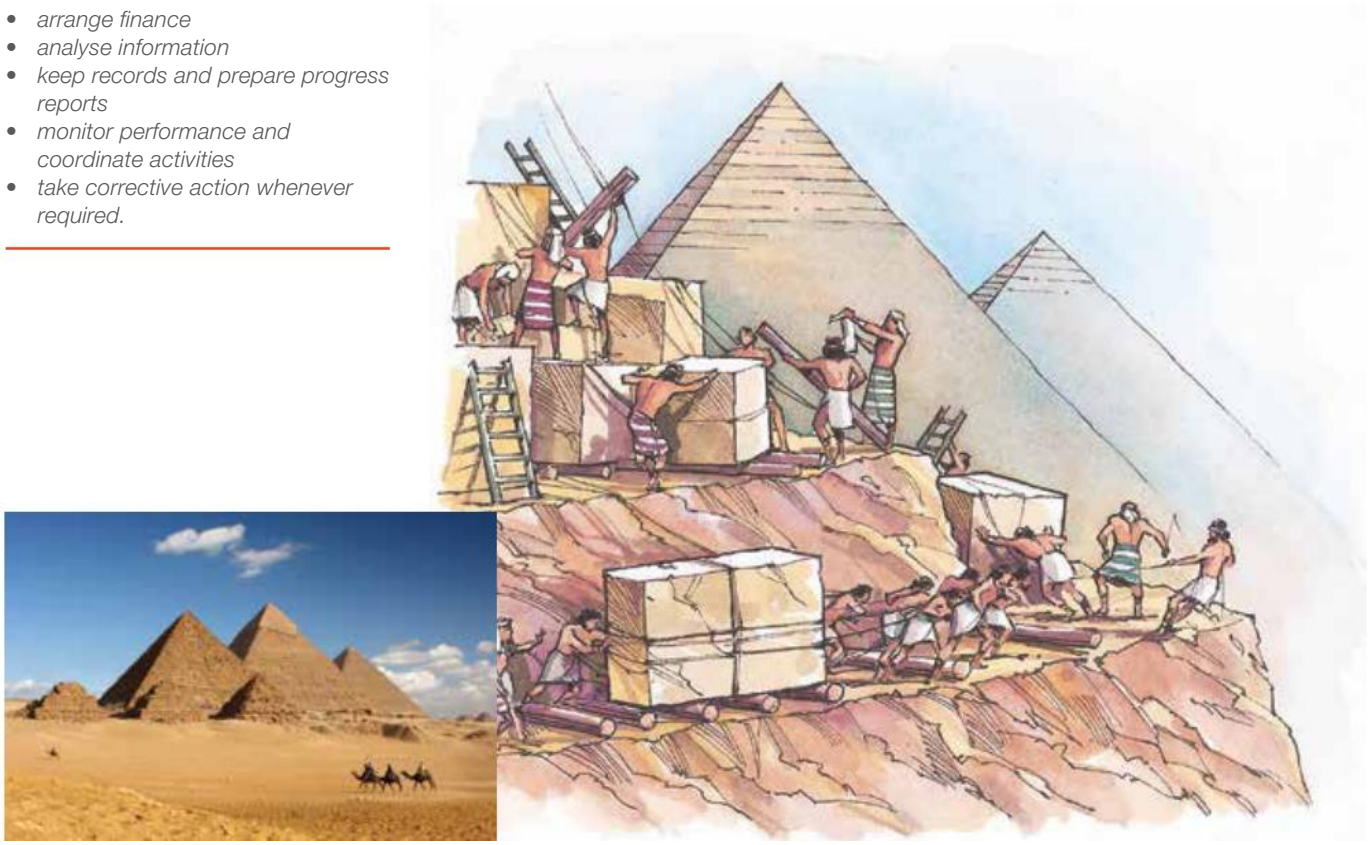


FIGURE 7.1 Effective management practices were applied to building the pyramids of Egypt.

The development of management as a body of knowledge and a subject in its own right is much more recent. The Industrial Revolution of the late 1700s, which encouraged the growth of factories, acted as a catalyst for developing management approaches (theories). As the number of factories increased, there was a need to coordinate the efforts of many people in the continual production of goods and services.

A number of people began thinking and writing about ways of running factories more efficiently. These individuals were the first to develop approaches to management and paved the way for the many management theorists who followed.

These approaches, or theories, outline the main functions of management including planning, organising, leading, motivating, communicating, negotiating and controlling a group of individuals in an attempt to achieve specific goals. To a large extent, management approaches have tended to reflect the customs and traditions of the society at the time. Consequently, as social and economic conditions changed new approaches were developed. However, no single approach to management is universally accepted today. Rather, each approach offers something of value for today's managers.

The management approach adopted by a business will have an enormous impact on all aspects of the business's operation.

In particular, management approaches influence:

- the organisation and allocation of tasks to staff
- the organisational structure
- levels of management
- management styles.

BizFACT

The factory system radically altered how goods were made. Previously, most production was on a small-scale basis that was carried out in the home. The Industrial Revolution resulted in large groups of semi-skilled workers using machines located in big factories.

SUMMARY

- Knowledge about management today is the result of a long and continuing innovative process as ideas evolved over time.
- The business's management approach will have an enormous impact on all aspects of the business's operations.

7.2 Classical approach to management

The Industrial Revolution began with the invention of reliable steam-powered machines. For the first time, businesses could **mass-produce** goods in factories that operated year-round. This posed challenges that earlier businesses had not previously faced. Problems arose in training employees, organising the managerial structure, scheduling complex manufacturing processes and dealing with worker dissatisfaction. Business owners now had to plan, organise, direct, control and staff many different types of operation.

BizWORD

Mass production *is the process of manufacturing standardised goods on a huge scale by automation.*

In response to these many complex problems, managers developed and tested solutions with the focus on finding 'one best way' to perform and manage tasks. The evolution of modern management, called the **classical approach**, had begun.

BizWORD

The **classical approach** *to management stresses how best to manage and organise workers so as to improve productivity (output).*

As the Industrial Revolution continued, this approach generated two perspectives, each with a slightly different emphasis. First came the classical scientific approach, which focused on how best to organise workers and production methods on the factory floor. Then came the classical bureaucratic approach, which emphasised how businesses should be organised or structured.

7.2.1 Classical–scientific approach

One significant management approach that emerged during the nineteenth century was that of Frederick W. Taylor (1856–1915). Taylor (figure 7.2) was an advocate of the production line method of manufacturing, which he viewed as the most

efficient form of production. This production system was used in the industrialised countries of the world until the early 1970s and was based mainly on Taylor's scientific management ideas.

BizWORD

Scientific management *is an approach that studies a job in great detail to discover the best way to perform it.*

Taylor, to assist his analysis, developed the principles of **scientific management**: an approach that studies a job in great detail to discover the best way to perform it.

Taylor's four principles of scientific management are as follows:

1. Scientifically examine each part of a task to determine the most efficient method for performing the task.
2. Select suitable workers and train them to use the scientifically developed work methods.
3. Cooperate with workers to guarantee they use the scientific methods.
4. Divide work and responsibility so that management is responsible for planning, organising and controlling the scientific work methods, and workers are responsible for carrying out the work as planned.



FIGURE 7.2 Frederick W. Taylor (1856–1915) argued that productivity would be improved by preparing plans based on what needed to be done, designing each task scientifically and providing training and incentives for the workers. Some observers criticised Taylor for exploiting workers to get them to produce more.

BizWORD

A **time and motion study** *is a process of examining each of the steps in a production procedure and the time taken to perform them.*

To improve efficiency, Taylor attempted to systematise the way a job was done. He believed that a poorly skilled workforce could be trained to perform simple repetitive tasks effectively. He used **time and motion studies** to analyse the performance of a particular task, with the objective of reducing a task to an effective minimum standard. As well as reducing routine tasks into their most simple format, Taylor advocated the division of labour into function-related units; that is, tasks were divided into small, specialised activities.

Taylor also believed that employees follow their own self-interest and display a natural desire to avoid work. Such a situation, he argued, required tight control by supervisors and managers. He believed in the need for management to control workers and ensure they followed instructions by rigid rules and regulations based on a hierarchy of authority.

One notable student of classical–scientific theory was Henry Ford. Being familiar with Taylor's work, Ford became an enthusiastic believer in scientific management and the use of machines. By combining these ideas, Ford developed his famous mechanised assembly line in 1913.

This approach to car assembly involved a chassis moving down an assembly line on a conveyor belt. A small team of workers would move with the car, fitting the various components that had been carefully set out along the production line. The end result was to reduce the hours spent on the assembly of a car from 728 hours to just 1.5!

McDonald's is another business that uses Taylor's scientific management approach in the preparation of its food. For example, a Big Mac is produced according to a set number of steps. The burger takes a predetermined number of seconds to cook, fixed amounts of lettuce, cheese and other ingredients are added precisely at the correct time and in exactly the same way. However, McDonald's adopts other management approaches when dealing with its employees; approaches that emphasise the 'human relations' aspect.



FIGURE 7.3 Taylor believed that dividing the task into smaller, specific activities would improve productivity.

Of course, the initial ideas of the classical–scientific theorists have been modified over time. However, modern managers realise that without motivated and committed employees, empowered to analyse their own work habits and take responsibility for what they do, productivity will not improve.

7.2.2 Classical–bureaucratic approach

The classical–bureaucratic approach was pioneered by Max Weber and Henri Fayol. According to Weber, a **bureaucracy** is the most efficient form of organisation and should have:

- a strict hierarchical organisational structure
- clear lines of communication and responsibility
- jobs broken down into simple tasks; specialisation
- clearly defined job roles
- rules and procedures
- impersonal evaluation of employee performance to avoid favouritism and bias.

Today, the term 'bureaucracy' is sometimes associated with controversy. People talk about bureaucracy as if it is self-serving and uncaring, but Weber described it positively. He believed that it contributed to a rational and more efficient organisation, because everyone knew their status and position in the organisation.

Fayol identified a number of management functions, including planning, organising and controlling (figure 7.4). His explanation of the functional approach to management provided a type of 'job description' for managers.

Fayol's explanation of the functions of management was so concise and easy to understand that it formed the foundation of most management courses offered during the twentieth century. His explanation was often used as a definition of management itself.

Fayol also developed a number of principles to assist managers, including:

- discipline as a feature of leadership
- the organisation's goals should take precedence over an employee's individual interests
- rewards for effort should be fair
- security of employment is essential
- teamwork should be encouraged.

BizWORD

Bureaucracy *is the set of rules and regulations that control a business.*

on Resources

Weblink: Henri Fayol

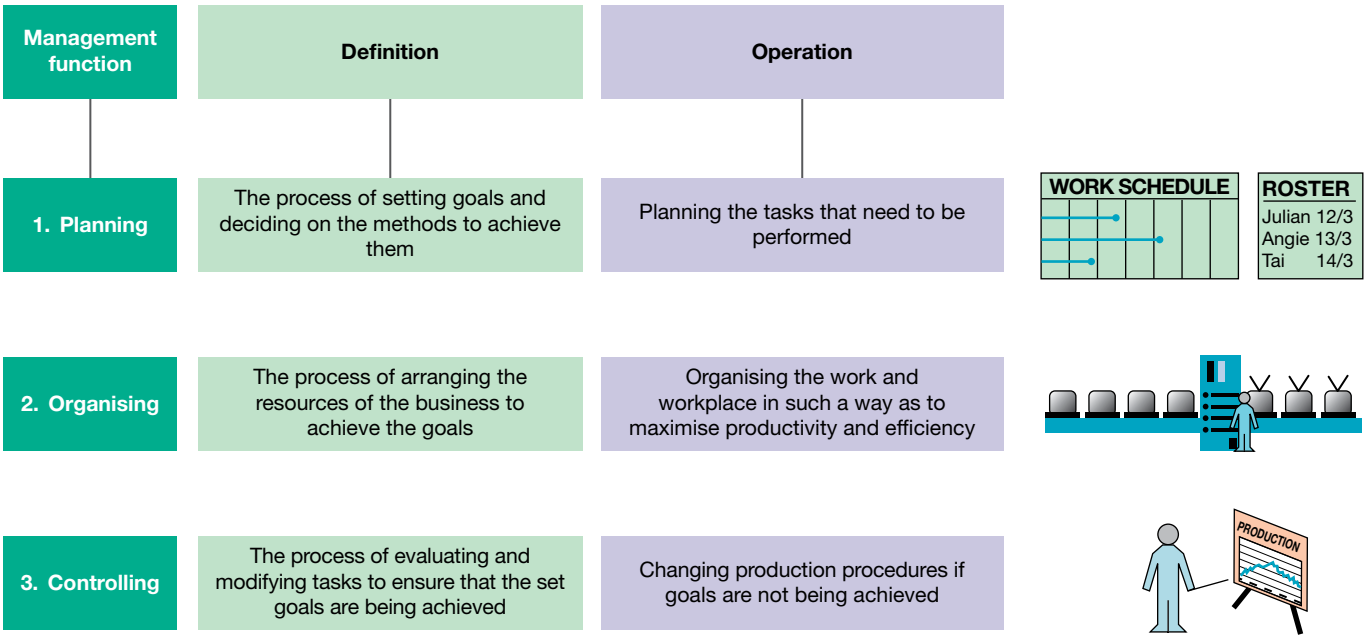


FIGURE 7.4 The main functions of management, according to Henri Fayol

In the nineteenth century, management models were based on a hierarchical system of authority similar to the layered and somewhat rigid organisational structure of the major churches, educational institutions and the army. Such techniques were viewed as appropriate for the production line because they ensured effective control of the workforce.

Table 7.1 outlines the advantages and disadvantages of the classical approach to management.

TABLE 7.1 Advantages and disadvantages of the classical approach

Advantages	Disadvantages
• Shorter time to make decisions • Could lead to improved efficiency • Increased productivity • Clear chain of command	• Specialisation and repetitive tasks could lead to employee boredom • Less job satisfaction, which could lead to increased turnover • Can discourage creativity and innovation • Organisation becomes inflexible and less able to adapt to changing conditions

SUMMARY

- A classical–scientific approach to management, pioneered by Frederick Taylor, studies a job in great detail to discover the best way to perform it.
- The classical–scientific approach led to the development of assembly line, mass-production techniques.
- A classical–bureaucratic approach to management, pioneered by Max Weber and Henri Fayol, advocated:
  - that a bureaucracy is the most efficient form of organisation
  - the main function of management is planning, organising and controlling.
- The main features of classical–scientific and classical–bureaucratic management approaches include:
  - time and motion studies used to reduce inefficiencies
  - production line methods
  - hierarchical organisational structure (bureaucracy)
  - clear lines of authority (chain of command)

- discipline as a feature of leadership
- autocratic leadership style
- rules and procedures.

EXERCISE 7.1 REVISION

1 **Why** is the practice of management not considered a recent invention?
2 **How** did the Industrial Revolution act as a catalyst for developing management approaches?
3 **Recall** two challenges the Industrial Revolution posed for businesses.
4 **Outline** the impact the Industrial Revolution had on the development of management approaches.
5 **Define** the term 'classical approach' to management.
6 **Identify** the two perspectives of the classical approach to management.
7 **Summarise** Taylor's principles of scientific management.
8 **State** the main purpose of time and motion studies.
9 **Demonstrate** the link between Ford cars and McDonald's hamburgers.
10 **Identify** the main bureaucratic features Max Weber believed needed to exist in a business for it to operate efficiently.
11 **Apply** the correct definition to the terms underneath the grid.

1. The process of evaluating and modifying tasks to ensure that the set goals are being achieved
2. The process of arranging the resources of the business to achieve the goals
3. The process of setting goals and deciding on the methods to achieve them

planning	organising	controlling

12 **Compare** and **contrast** Frederick Taylor's ideas on how to improve productivity with the ideas of Henri Fayol. You might like to present your information in the form of a Venn diagram, as shown in figure 7.5.

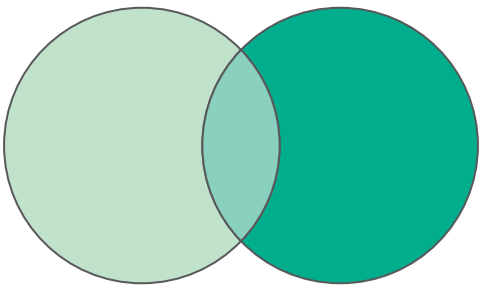


FIGURE 7.5 A Venn diagram is used to compare and contrast information. Points of difference are recorded in the outer parts of the circle and similarities are placed in the area where the two circles intersect.

EXERCISE 7.1 EXTENSION

1 In small groups, **create** a list of advantages and disadvantages of a modern business adopting a purely classical–scientific management approach. Share your research with the class as either a written or oral presentation.
2 **Examine** how the classical approach to management helped Henry Ford build the Ford Motor Company. **Evaluate** the criticisms that have been made of automated production line methods of manufacturing. The **bio.true story** weblink in the Resources tab has a biography of Henry Ford and the working conditions in the early Ford factories that may assist.

on Resources

Weblink: bio.true story

3 **Determine** why supporters of the scientific management approach established bureaucracies within their businesses.

4 'Classical management thinkers looked for the best way to do everything. Their tools were time and motion study, and a scientific approach to studying work and workflow.' **Discuss**.

7.2.3 Management as planning

Planning is often referred to as the primary management function. It provides the key to both the short-term and long-term success of a business. Effective planning provides a vision and goals for a business, strategies to achieve the vision and goals, and anticipation of future directions for change.

The ability of a manager to develop, implement and monitor plans will directly affect a business's success.

Planning is the preparation of a predetermined course of action for a business. It involves showing how the business will achieve its stated mission and business goals.

BizWORD

Planning *is the preparation of a predetermined course of action for a business.*

Levels of planning — strategic, tactical and operational planning

Once the business goals have been determined, decisions have to be made about how they will be achieved. This requires detailed plans for activities at all levels of the business. There are three different types of plans.

1. **Strategic (long-term) planning** is planning for the following three to five years. This level of planning will assist in determining where in the market the business wants to be, and what the business wants to achieve in relation to its competitors.
2. **Tactical (medium-term) planning** is flexible, adaptable planning, usually over one to two years, that assists in implementing the strategic plan. Tactical planning allows the business to respond quickly to changes. The emphasis is on how the goals will be achieved through the allocation of resources.

BizWORD

Strategic planning *is planning for the following three to five years. This level of planning will assist in determining where in the market the business wants to be, and what the business wants to achieve in relation to its competitors.*

Tactical planning *is flexible, adaptable planning, usually over one to two years, that assists in implementing the strategic plan.*



FIGURE 7.6 Planning involves looking ahead and mapping out future courses of action. Action without planning usually ends in failure. It is often said that 'failing to plan is planning to fail'.

3. **Operational (short-term) planning** provides specific details about the way in which the business will operate in the short term. Management controls the day-to-day operations that contribute to achieving short-term actions and goals. Examples of operational plans are daily and weekly production schedules.

BizWORD

Operational planning *provides specific details about the way in which the business will operate in the short term.*

7.2.4 Management as organising

Organising is the next part of the process when management puts into practice the goals that were determined in the planning stage. Organising is determining what is to be done, who is to do it and how it is to be done. It is organising the financial, human and material resources to achieve the goals of the business.

Management has to coordinate activities to translate plans into reality — that is, to ensure that the goals of the strategic, tactical and operational plans are achieved.

BizWORD

Organising *is the structuring of the organisation to translate plans and goals into action.*

The **organisation process** *is the range of activities that translate the goals of a business into reality.*

The organisation process

The **organisation process** is the range of activities that translate the goals of a business into reality. These activities include the following three steps:

1. *Determining the work activities.* The work activities required to achieve management objectives must be determined. Work activities are then usually broken down into smaller steps.
2. *Classifying and grouping activities.* Once the work activities of a business have been broken down into smaller steps, similar activities can be grouped together. This improves efficiency by enabling the most appropriate allocation of resources. For example, it is common practice to group activities into departments or sections and allocate employees and supervisors to each section or department.
3. *Assigning work and delegating authority.* The next step in the organisation process is to determine who is to carry out the work, and who has the responsibility to ensure that the work is carried out. Delegation also involves ensuring that the person who has been given responsibility does carry out the processes.

BizFACT

The following factors need to be taken into consideration when organising: business goals, business size, organisational structure, business culture, technology, business environment, employee skills and available resources.

7.2.5 Management as controlling

Controlling is the process management goes through when it attempts to evaluate performance and take corrective action to ensure that objectives are being achieved.

Controlling compares what was intended to happen with what has actually occurred. If there is a discrepancy between performance and goals, changes and improvements can be made.

BizWORD

Controlling *is the process of evaluating performance and taking corrective action to ensure that the set objectives are being achieved.*

The **control process** *involves establishing standards in line with the goals of the business, measuring the performance of the business against those standards or benchmarks, and making changes where necessary to ensure that the goals of the business have been met.*

Control processes

There are three steps in the **control process** (see figure 7.7).

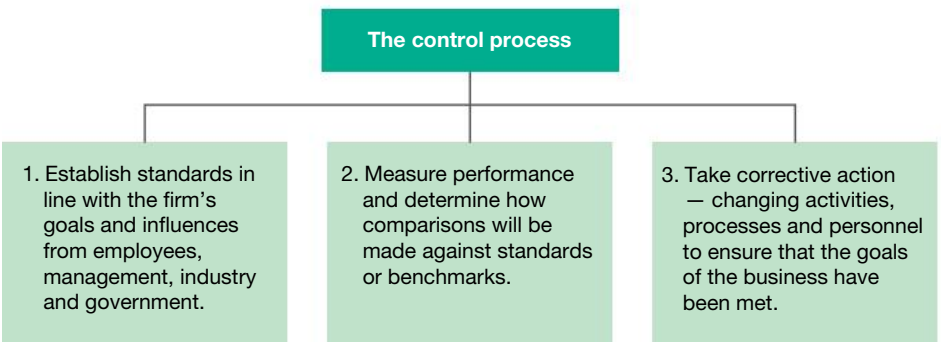


FIGURE 7.7 The three steps in the control process



FIGURE 7.8 PCCA is a compounding pharmacy supplier that has implemented the industry's most comprehensive quality control and quality assurance measures. From the moment a chemical arrives to the time it ships, it is monitored by Quality Control and Quality Assurance employees. The Quality Control lab performs as many as nine qualitative analyses on each chemical lot. If the product is compromised in any way, it fails the inspection and is rejected.

7.2.6 Hierarchical organisational structure

The organisational structure of a business is the way in which its parts have been organised, so that the business can achieve its objectives. An organisation's structure is usually represented diagrammatically in an organisational chart. The chart shows the key positions of responsibility and accountability, and lines of communication.

Think of a business as a three-storey pyramid (figure 7.9). This type of management structure is found in many businesses and is based on the traditional managerial hierarchy. **Management hierarchy** is the arrangement that provides increasing authority at higher levels of the hierarchy. This means that senior managers have greater accountability, responsibility and power compared to those at lower levels of the pyramid. They can be visualised as a pyramid, as shown in figure 7.9.

BizWORD

Management hierarchy *is the arrangement that provides increasing authority at higher levels of the hierarchy.*

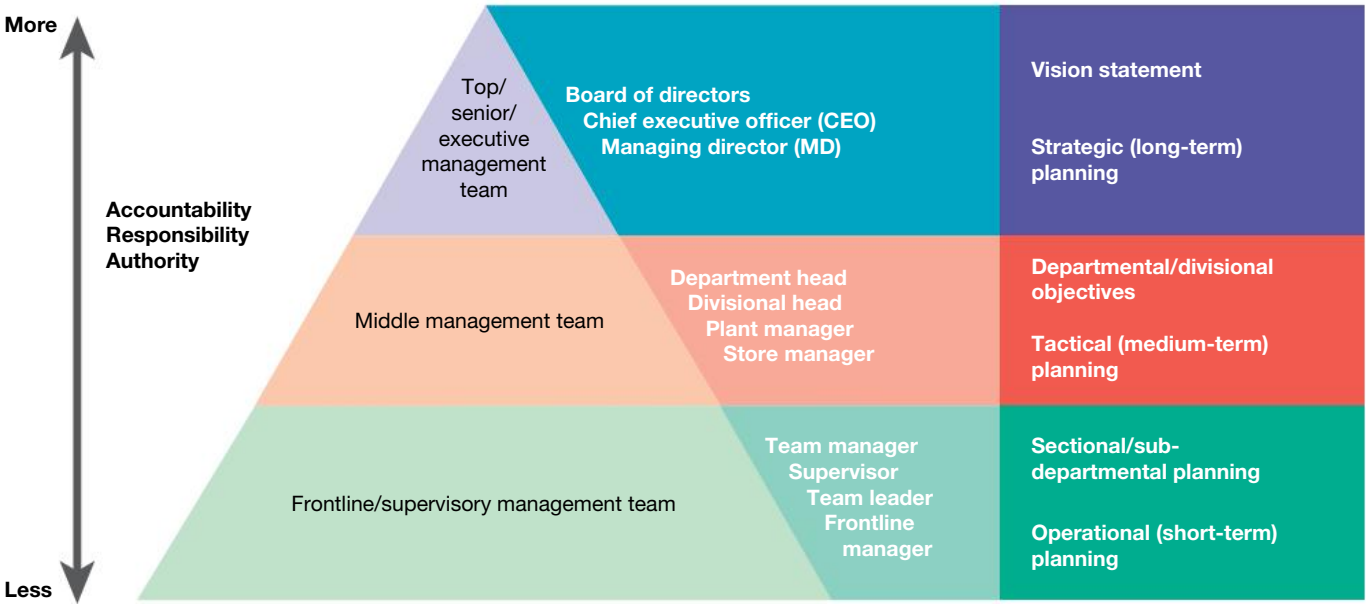


FIGURE 7.9 A management hierarchy. The coordinated effort of all three levels of management is required to achieve the goals of the business.

The primary characteristic of traditional hierarchical organisational structures has been the grouping of people according to the specialised functions they perform (see figure 7.10). These may include marketing, finance, human resources and operations. Even within each of these functional areas, tasks are further subdivided into specialised jobs. People within the operations division, for example, have specialised tasks to perform, such as warehouse manager, clerks, packers, process employees and storeperson. The same principle applies to sporting teams. For example, a hockey team has members who specialise in certain positions, such as coach, captain, winger, goalie or centre. The team is organised in this way to offer the best combination of people's talents to achieve productivity. In this case, the team is performing its best.

Characteristics of the pyramid-shaped organisational structure include:

- rigid lines of communication
- numerous levels of management, from managing director to supervisors
- clearly distinguishable organisational positions, roles and responsibilities
- hierarchical, linear flows of information and direction, with a large amount of information directed downwards
- **specialisation of labour** resulting in tasks being divided into separate jobs
- a **chain of command** that shows who is responsible to whom
- centralised control with all strategic decisions made by senior management.

BizWORD

Specialisation of labour *refers to the degree to which tasks are divided into separate jobs.*

A **chain of command** *is a system that determines responsibility, supervision and accountability of members of the organisation.*

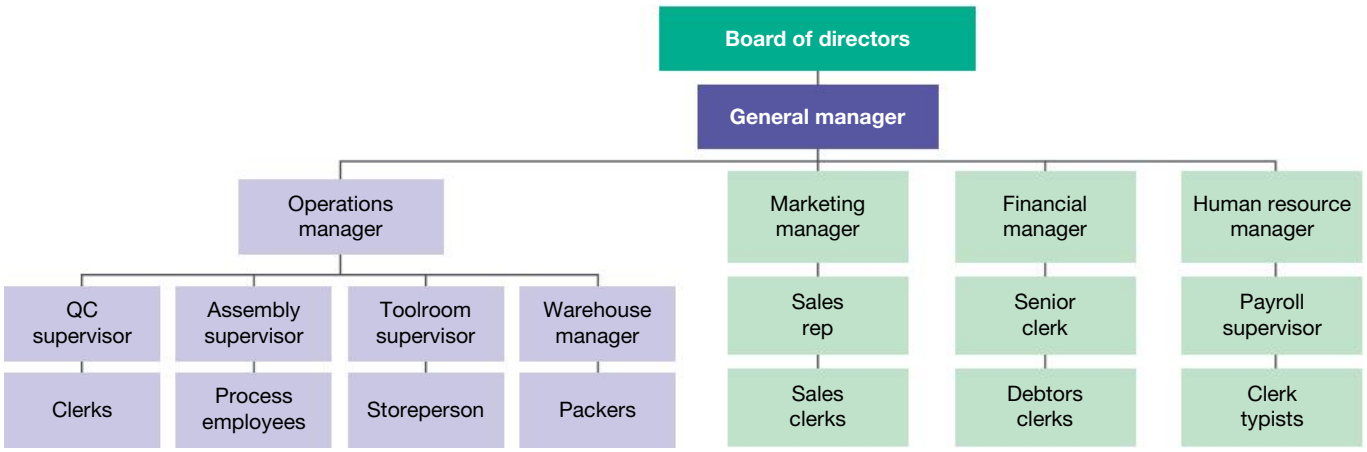


FIGURE 7.10 Typical pyramid-shaped, hierarchical organisational model

SUMMARY

- Management functions include:
  - *planning:* a predetermined course of action. This involves strategic, tactical and operational planning.
  - *organising:* a range of activities that translate goals into reality.
  - *controlling:* compares what was intended to happen with what has actually occurred.
- Management hierarchy is the arrangement that provides increasing authority at higher levels of the hierarchy.
- Senior managers have greater accountability, responsibility and power compared to lower-level managers of the organisation.
- The traditional hierarchical organisational structure has people grouped according to the specialised functions they perform.

7.2.7 Leadership styles

The important task faced by all managers is how best to achieve their business's goals. This task can be accomplished only by working with and through other people, so managers must select a leadership style appropriate to the environment in which they operate.

BizWORD

A manager's **leadership style** *is essentially their way of doing things — their behaviour and attitude.*

A manager's **leadership style** is essentially their way of doing things — their behaviour and attitude. Leadership styles can be placed on a continuum (see figure 7.11) with the autocratic manager at one end through to the participative/democratic manager at the other.

An autocratic or authoritarian manager would be one who makes the decisions and tells employees what tasks to do and how to do them. A participative or democratic management style presents problems, asks for suggestions and works together to make a decision. The assumption is that all types of leaders would appear somewhere on that continuum.

Recent theories indicate that managers bring a range of styles to their leadership position that may change according to the situation. Most managers typically have a dominant style that they frequently adopt, and one or two 'backup' styles.

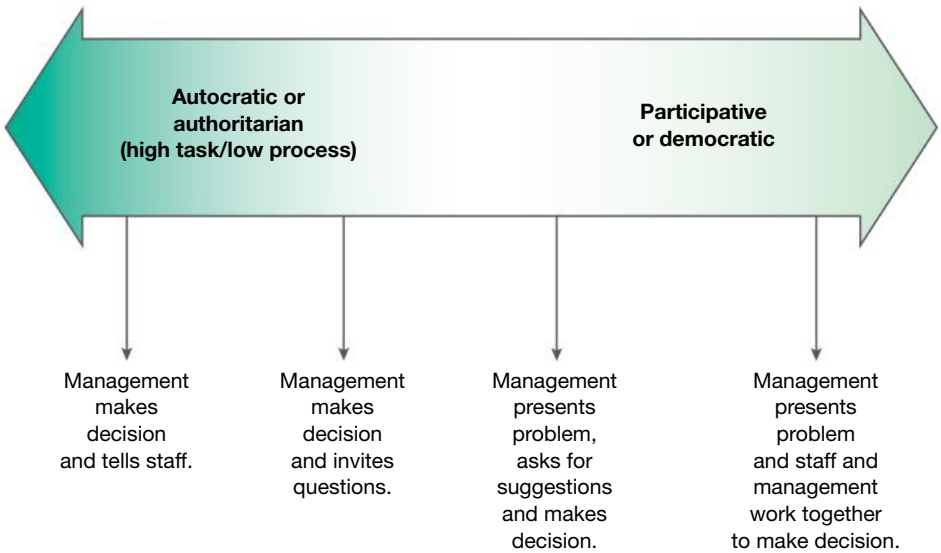


FIGURE 7.11 One theory of leadership style — the continuum

The two main types of leadership approaches and their characteristics are shown in table 7.2.

TABLE 7.2 Characteristics of the two main leadership styles

Key feature	Autocratic or authoritarian manager	Participative or democratic manager
Decision making	Makes all decisions and informs employees	Consults with employees, asks for suggestions then decides
Control	Centralised — controls all activities	Shares decision making with employees
Staff participation	Expects employees to follow orders	High level of employee empowerment
Communication	Top–down	Two-way
Motivation methods	External — rewards (carrot) and sanctions (stick)	Internal — sense of fulfilment, satisfaction
Workplace example	Military officer during wartime; time of crisis	Professional organisations — intellectual abilities of employees are similar or complementary

7.2.8 Autocratic leadership style

Managers who adopt a strict classical–scientific approach usually display an autocratic leadership style. A manager using an **autocratic leadership style** tends to make all the decisions, dictates work methods, limits worker knowledge about what needs to be done to the next step to be performed, frequently checks employee performance and sometimes gives punitive feedback.

The autocratic manager generally provides clear directives by telling employees what to do, without listening to or permitting any employee input. This style of manager controls the people in the business closely and motivates through threats and disciplinary action. Autocratic managers expect compliance and obedience, they are controlling, and they give more negative and personalised feedback.

The autocratic style of leading can be effective in a time of crisis when immediate compliance with rules or procedure is needed, or in meeting an unexpected deadline when speed is important. An army officer, for example, would adopt this management style during military exercises. This approach is also effective when individuals lack skills and knowledge. A McDonald's crew trainer, for example, may adopt this style when supervising new employees. It is generally accepted, however, that this style does not encourage the best performance from employees.



FIGURE 7.12 Donald Trump displayed many of the characteristics of an autocratic manager when running the Trump Organization. He centralised all the decision-making to himself and a selected group of people and limited the input of the rest of his employees. Trump adopts a task-oriented approach, although he does still look after his employees.

The main advantages of the autocratic leadership style include the following.

- Directions and procedures are clearly defined and there is less chance of uncertainty.
- Employees' roles and expectations are set out plainly, so management can monitor their performance.
- A hierarchical structure provides a stable and consistent environment in which the outcomes almost always match management objectives.
- Control is centralised at top-level management, so time is used efficiently and problems are dealt with quickly because there is no discussion or consultation.

The main disadvantages include the following.

- No employee input allowed, so ideas are not encouraged or shared. This means employees do not get the chance to develop their skills or to feel valued in the organisation.
- It ignores the importance of employee morale and motivation. When no responsibility is given to lower level staff, job satisfaction decreases, which ultimately affects issues such as absenteeism and staff turnover.
- Conflict, or potential for conflict, increases. Often workers are competing for the approval of managers, which can lead to tension between employees.
- An 'us and them' mentality may develop in the workplace as a result of the lack of employee input.

BizWORD

A manager using an **autocratic leadership style** *tends to make all the decisions, dictates work methods, limits worker knowledge about what needs to be done to the next step to be performed, frequently checks employee performance and sometimes gives feedback that is punitive.*

on Resources

Weblink: Autocratic leadership

SUMMARY

- The two main types of leadership style are:
  - autocratic or authoritarian — strong, centralised control
  - participative or democratic — authority and power are decentralised.
- A manager using an autocratic leadership style tends to make all the decisions and frequently checks employee performance.

- Managers should bring a range of leadership styles to their positions that can change according to the situation.
- Most managers typically have a dominant style.

EXERCISE 7.2 REVISION

1 **Define** the term 'planning'.

2 **Why** is planning considered to be the primary management function?

3 Complete the following table by **identifying** whether the planning activities are strategic, tactical or operational. The first one has been completed for you.

Planning activity	Type of planning
1. An organisation plans to build a new warehouse.	Tactical
2. A supervisor wants to have regular weekly production meetings.	
3. A marketing department is to relocate to a new site in another city.	
4. A government department decides to undertake planning to fully privatise during the next four years.	
5. A stocktake needs to be completed tomorrow.	
6. A team leader decides to monitor the team's performance over a two-month period.	
7. A new computer system is to be installed.	
8. A large-scale business operating in five countries decides to undertake an extensive restructure of its entire organisation.	
9. A department sales manager requires the sales team to increase sales by 10 per cent over the next six months.	
10. An engineering business wants to develop new production facilities in three countries.	

4 **Explain** why the organising function is important to a business.

5 **Summarise** the three steps involved in the organisation process.

6 **Define** the term 'controlling'.

7 Examine figure 7.7 on page 175. **Identify** the correct terms to complete the following steps in the control process.

Step 1	Establish s_ _ _ _ _ _ _
Step 2	Measure p _ _ _ _ _ _ _ _ _
Step 3	Take corrective a _ _ _ _

8 **Why** is the controlling function important?

9 **Define** the term 'management hierarchy'.

10 **Identify** the three main levels of management.

11 (a) **Construct** an organisational chart of your school.
(b) **Classify**, by highlighting in a different colour, the senior, middle and frontline management divisions.
(c) **Why** do you think the school's organisational structure is hierarchical?

12 **Contrast** an autocratic leadership style with a participative one.

13 **Identify** the leadership style of each of the following managers.
(a) The manager sets high standards of performance and has little sympathy for those who do not meet the standards.
(b) The manager takes care to explain why something must be done in a certain way.

(c) The manager expects his or her orders to be unquestionably followed.
(d) The manager believes that developing close personal relationships with staff is the mark of a good manager.
(e) The manager persuades the employees to do their best.

14 **Describe** a situation when an autocratic management style would be appropriate.

15 **Justify** whether you believe the advantages of the autocratic leadership style outweigh the disadvantages.

EXERCISE 7.2 EXTENSION

1 'The three levels of planning — strategic, tactical and operational — correspond to the three levels of management — top, middle and frontline.' **Explain** the relationship between the level of planning and the level of management.

2 **Account** for the relationship between an organisational chart and an organisation's chain of command. If you were new to a business, **explain** how an organisational chart would help you become oriented.

3 'Managers who adopt a strict autocratic management style normally organise their business along traditional hierarchical lines.' **Evaluate**.

4 **Determine** how autocratic managers motivate their staff to get things done. **Assess** whether their style is successful.

5 Ask your teacher for permission to complete the following activity in class time. The aim of this activity is to put your theoretical understanding of Business Studies into practical use as you solve problems, plan and make management decisions.
Materials required: paper, tape measure, markers (such as flags or witches hats)

Paper plane business — instructions

You are about to embark on your latest venture . . . running a rather large paper plane business. Your team's task is to construct the ultimate paper plane.



1 Arrange your class into groups of three or four. Each of these teams will become a business. Organise for some of the students in the class to be observers.

2 Your business has 30 minutes in which to produce the paper plane that travels the longest distance (you could also have a competition for the best looking plane or most innovative design).

3 As a team, **determine** what the goals for your business will be. Write down an action plan for your business (your strategies). List the key performance indicators (KPIs) that will show whether or not you have met your goals.

4 Establish your management structure (who is going to complete the various activities that need to occur for your business to achieve its objectives). Your teacher will explain the responsibility of each position. You would definitely need a managing director. Make sure each team member's task is clear. Each team member should probably take responsibility for a particular goal.

5 **Discuss** a design for your plane and then produce it, making sure that you do your very best to meet all of your goals.

6 Find a safe place to test your planes. Use the tape measure to determine distance. Make sure you record these measurements.

7 The winner will be the group whose paper plane travelled furthest. Alternatively, the winner could also be the team with the best looking plane, the most innovative design etc.

8 The observers should next report to the class. What did they see happening as groups were planning, organising and controlling? Did any leaders emerge during the activity?

9 After finishing the paper plane activity, list your group's goals. **Assess** how well you planned to achieve these goals. **Identify** the KPIs you planned to use to measure whether or not you met the goals.

10 **Outline** the role that you played in your business. For example, if you were the production manager, outline how you were involved in planning, organising and controlling your business.

11 Using the information from the observers, **discuss** whether anyone emerged as a leader in your group.

12 **Evaluate** how your group performed in terms of meeting its KPIs.

13 After finishing the paper plane activity, complete the following table to **summarise** the role of each member of your business. The first entry has been started for you.

Manager	Planning	Organising	Controlling
CEO	Determined objectives for group	Delegated responsibilities to members of group	Compared planned performance with actual performance
GM			

14 Benchmark your performance against other groups in your class (that is, compare the results to the other results). **Recommend** how you could improve.

7.3 Behavioural approach to management

Scientific management principles did not always lead to increased productivity due to the repetitive and boring nature of many jobs and the dehumanising structure of the workplace. Approximately 50 years after the emergence of scientific management ideas, behavioural, or 'human relations', approaches surfaced. The behavioural school recognised that to make substantial productivity gains, worker participation in the production process was required. It acknowledged the workers' contribution to output.

BizWORD

The **behavioural approach** *to management stresses that people (employees) should be the main focus of the way in which the business is organised.*

Advocates of the **behavioural approach** to management stress that people (employees) should be the main focus of the way the business is organised. They believe that successful management depends largely on the manager's ability to understand and work with people who have a variety of diverse backgrounds, hopes, desires and expectations. The development of this humanistic approach has greatly influenced management theory and practice.



FIGURE 7.13 Harvard professor Elton Mayo (1880–1949), founder of the behavioural approach to management

One major contributor to behavioural management theories was Elton Mayo (1880–1949). Mayo (see figure 7.13), is considered the founder of industrial psychology. Through his revolutionary experiments, conducted at the Western Electric Hawthorne Company in Chicago, he discovered what became known as the 'Hawthorne effect', which demonstrates that meeting people's social needs has a significant impact on productivity (see the following Snapshot). Two significant results from the research were that:

- worker satisfaction to a large extent is non-economic; that is, workers have social needs in addition to economic needs
- being made to feel part of a team increases job satisfaction and output.

Many large businesses recognise the importance of being socially responsible, not just to their external customers but to their internal customers — their employees. It is in the business's best interests to provide for and look after their employees. Some businesses do this by providing extra facilities for their workers such as good canteen facilities, child-minding facilities, access to counselling and so on. Others provide flexible working conditions.

Elton Mayo — the Hawthorne studies (1927–1932)

The Western Electric Company's Hawthorne factory manufactured a range of electrical components such as relay assemblies. Mayo wanted to find out what effect fatigue and monotony had on employee productivity. He selected six female employees from the assembly line, segregated them from the rest of the factory and placed them under the control of a supportive supervisor. The team was involved in assembling telephone relays. Mayo made frequent changes to their working conditions, always discussing and explaining the changes in advance.

To his amazement, Mayo realised that productivity had increased completely independent of any of the changes he made. The six individual employees had become a team and together eagerly participated in the experiment. They were happy knowing that they were working without coercion from senior managers or limitations from the workplace structure. They felt they were working under less pressure, not being pushed or bossed around by anyone. Under these conditions, they developed an increased sense of responsibility, with discipline coming from within the team.

Mayo's findings were at odds with F W Taylor's theory, which stated that workers are only motivated by self-interest. If Taylor was correct, the women's productivity should have decreased when Mayo returned them to longer working hours. However, Mayo realised that the women had formed a harmonious team and felt happier at work, which raised their self-esteem. The women talked, joked and began to meet socially outside of work. Mayo had discovered an elementary concept that seems obvious today: workplaces are social environments and employees are often motivated by much more than self-interest.

The section of the Hawthorne studies that examined the beneficial effects of positive and supportive supervision, and the impact of teamwork became known as the Hawthorne effect.

SNAPSHOT QUESTIONS

1. According to Elton Mayo's research, **explain** why productivity increased even after the original working conditions were reintroduced.
2. **Outline** what is meant by the Hawthorne effect.
3. Imagine you are a manager for a small business. **Discuss** what impact Mayo's research would have on:
   (a) how you organise your workplace
   (b) the management practices you would use.

SNAPSHOT



'… workplaces are social environments and employees are often motivated by much more than self-interest.'

on Resources

Weblink: Hawthorne studies



FIGURE 7.14 CommBank has demonstrated an ongoing commitment to looking after its staff by offering them a variety of perks. For example, it provides discounts on electricity and insurance, offers priority long day childcare places, has a range of facilities to help employees look after their physical and mental health, and offers staff multiple flexible working arrangements and leave options to assist them to juggle their work and personal circumstances.

A different value system emerged from the contributions of the behavioural theorists. Managers were now required to meet the social needs of their employees in addition to production efficiency. Skills in communication, social motivation and democratic leadership were quickly acquired.

Table 7.3 outlines the advantages and disadvantages of the behavioural approach to management.

TABLE 7.3 Advantages and disadvantages of the behavioural approach

Advantages	Disadvantages
• Increased empowerment of employees — can take ownership of their work • Worker recognition and appreciation should lead to increased motivation • Improved relationship between managers and staff	• Lack of control • Powerful people can disrupt the process • Communication can often be so large that confusion may arise • It's difficult to accurately predict employee behaviour

SUMMARY

- The behavioural approach to management, pioneered by Elton Mayo, stresses that people (employees) should be the main focus of the way in which the business is organised.
- The main features of behavioural management approach include:
  - humanistic approach: employees are the most important resource
  - economic and social needs of employees should be satisfied
  - employee participation in decision making
  - team-based structure
  - managers need good interpersonal skills
  - democratic leadership style emerging.

BizWORD

Leading *is the process of influencing or motivating people to work towards the achievement of the business's objectives.*

BizFACT

Research has shown that companies led by more humble individuals perform better. Humble leaders are more modest, emotionally stable and eager to learn. Another strength of humble leaders is self-awareness — confidence in their abilities paired with accurate understanding of their limitations. Finding an authentically humble CEO is rare, however.

7.3.1 Management as leading

Leading occurs when managers endeavour to influence or motivate people in the business to work to achieve the business's objectives. The type of leadership in a business depends on the attitudes and assumptions that managers have about people in the business.

To act as a leader, a manager should display empathy and possess good listening skills. A leader will have high expectations of employees' abilities to initiate and implement ideas. He or she will concentrate on the needs of their employees, building high-performance teams that attain their objectives. Less effective managers tend to focus on tasks and are more concerned with meeting deadlines — that is, they display the natural characteristics of a manager, not a leader. A leader, however, wants to empower (see the following Snapshot).

SNAPSHOT

The difference between a manager and a leader



'… having this title doesn't make them a leader.'

When someone is promoted into a role where they are managing people, they don't automatically become a leader. Anybody can have a title and boss people around, but having this title doesn't make them a leader. A person doesn't become a leader because someone higher up the organisational structure confers a title on them; they can only become a leader when their staff trust them to lead, and that requires them to also trust their employees. While the words 'manager' and 'leader' are often used interchangeably, they mean two completely different things.

Below are some key differences between the two.

- A manager tells their employees what to do, a leader encourages them. Managers rely on control by assigning tasks and directing staff. Leaders resist the temptation to tell their employees what to do and how: they inspire trust, motivate staff and have faith in their potential.

- A manager maintains the status quo, a leader challenges it. Managers stick with what works and constantly refine their current processes in order to make them better. Leaders are change agents and are constantly looking for ways to improve the business. They embrace change and know that even if things are working, there could be a better way forward.
- A manager has subordinates, a leader has followers. Managers have staff who follow directions and seek to please their boss. Leaders have fans; people who will help them build their business and achieve their vision.
- A manager creates goals, a leader sets a vision for their staff. Managers focus on setting, measuring and achieving goals, as well as controlling situations to ensure they can achieve those objectives. Leaders paint a picture of what they see as possible and inspire their employees to turn that vision into a reality.
- A manager makes all the decisions, a leader encourages employees to participate in the decision-making process. Leaders don't assume they have all the answers; they are humble enough to listen to the people around them.
- A manager builds systems and processes, a leader builds relationships. Managers focus on the processes and ensure that the correct systems are in place for the business to achieve their objectives. Leaders focus on people; not only their staff, but all the key stakeholders they need to influence in order to realise their vision. They spend a lot of time with their stakeholders and build loyalty and trust.

SNAPSHOT QUESTIONS

1. **Distinguish** between a manager and a leader.
2. **State** who you would rather work for — a manager or a leader. **Justify** your choice.

BizFACT

Recent survey evidence shows that many Australian managers, especially managers of SMEs, are unable to develop a strategic perspective that allows businesses to read disruptive changes in markets, identify opportunities and adapt. The flow-on effects are numerous, but the key one concerns the absence of the skills necessary to drive continuous improvement and effectively manage change.

Added to these qualities, a successful leader is someone who:

- keeps an open mind, seeks out new ideas and freely shares information
- shows confidence in people, shares credit and recognition
- builds and communicates a clear vision
- sets an example and earns the respect of employees
- **delegates** tasks to suitable employees
- conveys the goals of the business to workers and motivates them
- demonstrates flexibility in dealing with situations
- understands the technical aspects of the industry or business.

Being an effective leader is not an easy task. There may be temporary setbacks, particularly during periods of negotiation. In the end, leadership may still fail. However, not displaying leadership is inviting a greater possibility of failure.

Numerous books have been written about what makes a good leader. Some people believe that good leaders are 'born' rather than 'made'. They argue that the characteristics needed to be a good leader are part of an individual's unique personality and cannot be learnt from textbooks. Other people, however, argue that with appropriate training and coaching, the skills of leadership can be learned. Whichever the case, managers who display 'daring leadership' are best able to inspire their employees.

BizWORD

Delegation *is the handing over of certain tasks or responsibilities to an employee who is suitably capable and qualified to carry them out.*

BizFACT

'A leader is one who knows the way, goes the way, and shows the way.'

John C. Maxwell



FIGURE 7.15 Sir Richard Branson's leadership qualities have enabled his company to achieve continuous growth. Branson is admired by his employees and often gives them a stake in his business ventures to help make sure they're fully motivated to make it as successful as possible. He encourages every employee to become an innovative thinker who can add value in their own way.

7.3.2 Management as motivating

As explained in chapter 6, motivation is the individual, internal process that energises, directs and sustains an individual's behaviour. It is the personal force that causes a person to behave in a particular way.

Some people work harder than others. An employee with outstanding abilities may constantly be outperformed by someone with average skills. The difference between the two employees is their level of motivation. Motivated workers will always perform at a higher level than unmotivated workers. To some extent, a high level of employee motivation is determined by management practices. Efficient managers need to put in place work practices that motivate their employees; they must be aware of the *human factor* involved in the business organisation.

Elton Mayo's Hawthorne studies (see pages 182–183) highlighted the importance of the human factor in employee performance. Merely asking employees to participate in the research gave them a sense of involvement in their jobs. These employees — perhaps for the first time — felt as though they were of value and importance to the business. It was this sense of importance that acted as the motivating force that improved employee productivity.

BizFACT

'Sometimes the most effective motivation is just to say "thank you".'

Zig Ziglar, motivator and trainer

BizFACT

Creating strategies to motivate millennials requires a different approach from that used in the past, due to the generational differences that exist. Managers need to understand what motivates millennials in order to reduce 'employee churn'. According to Deloitte's 2016 Millenial Survey, *millennials are searching for meaningful work and place far greater emphasis on employee wellbeing and development. They are motivated by intrinsic rewards and are less focused on financial goals.*



FIGURE 7.16 Leadership recognition is fundamental to increasing staff morale and motivation. Recognition might just be a pat on the back for a job well done. Some businesses, however, have formal recognition programs so that employees who perform well are rewarded and encouraged to continue the good work.

The Hawthorne studies revealed that such human factors as recognition, selfworth and positive reinforcement are at least as important to motivation as external factors such as pay rates and working conditions. In some cases they may be more important. From this initial research came a flood of other behavioural management approaches focusing on the area of motivation. Overwhelmingly, the research highlights the fact that management would do best to provide a work environment that maximises employee satisfaction. Good managers, therefore, should also be good motivators, encouraging employees and using positive reinforcement to influence behaviour.

How then does a manager go about the task of motivating the business's employees? This question is often asked and has resulted in a wide variety of answers. Numerous studies have identified such diverse factors as trust, respect for the individual, positive reinforcement, empowerment, enhancing self-esteem, employee participation, rewarding team performance, employee encouragement and so on. Managers can use a variety of techniques to improve employee motivation.

BizFACT

'If employees feel a real attachment to the business; it is part of their lives, then they will be much more motivated.'

Adam Bartlett, Strategic Facilities Manager.

However, what the majority of these motivation techniques have in common is the need to develop a workplace culture that fosters employee participation.

7.3.3 Management as communicating

As outlined in chapter 5, one of the most difficult challenges for managers is getting employees to understand and want to achieve the business's goals. Effective communication is at the heart of meeting this challenge.

Communication is one of the easiest and, at the same time, most difficult of management activities. This is because of the complex nature of communication. Unless managers are effective communicators and able to share their thoughts and plans, they will find it difficult to influence others.



FIGURE 7.17 Poor communication has several adverse effects, which can lead to confusion in the workplace and lost business. It can result in decreased productivity, low morale and increased conflict as well as mistakes.

Effective communication is a crucial part of every manager's job. It encompasses every management function and role. Without effective communication, the most carefully detailed plans and brilliant strategies will most probably fail. Many studies have shown that the performance of both individuals and businesses improves when managerial communication is effective. This is especially so when open communication is used to motivate employees by providing them with information regarding the business's goals, plans and overall financial results. Whenever a manager operates on the communication principle of 'tell the employees only what they need to know and nothing else', then the workers will not be motivated to achieve common goals because they do not know what the goals are.

BizFACT

Businesses cannot thrive without open communication. Communication should be a collaborative relationship-driven process, rather than a top-down approach. Managers should allow communication to be a two-way street and involve their employees when making decisions.

SUMMARY

- According to the behavioural management approach, the main management functions are:
  - *leading:* having a vision of where the business should be in the long and short term
  - *motivating:* energising and encouraging employees to achieve the business's goals
  - *communicating:* exchanging information between people; the sending and receiving of messages.

EXERCISE 7.3 REVISION

1 **Define** the term 'behavioural approach' to management.
2 According to the behavioural management approach, **identify** what was required to improve worker productivity.
3 **Recall** the two significant results of Elton Mayo's Hawthorne studies.
4 **Identify** five characteristics a manager should display in order to be a leader.
5 **Calculate** whether the following statements are true or false.

	True	False
(a) Leading and managing are much the same thing.	____	____
(b) Good leaders are important for businesses.	____	____
(c) To be a good leader, you must be authoritarian.	____	____
(d) Before you lead, you must learn to follow.	____	____
(e) Leaders should have only one concern: the task.	____	____
(f) To be an effective leader you must be a skilled communicator.	____	____
(g) A person's leadership style should be fixed and unchangeable.	____	____
(h) Leadership skills can be learned.	____	____

6 **Recall** the meaning of the term 'motivation'.
7 **State** what the Hawthorne studies revealed about employee motivation.
8 **Identify** four factors a manager can use to motivate the business's employees.
9 When talking about motivation, the carrot (reward) and stick (punishment) approach is sometimes mentioned. **Explain** why giving someone a reward or punishment might motivate them to act.
10 'For a business to succeed, effective communication is vital.' **Discuss**.
11 Draw a table similar to the one following to **summarise** details of management skills in this section. The first one has been completed for you.

Skill	Definition	Characteristics	Application to the workplace
Communicating	The ability to transfer information	Communication can be verbal (emails, meetings and face-to-face conversations) and non-verbal (body language, visual).	Managers use it to explain a vision, to instigate change, to answer questions and to listen.
Leading			
Motivating			

EXERCISE 7.3 EXTENSION

1 **Determine** why employees would favour the behavioural approach to management over the classical–scientific approach.
2 **Propose** why the development of behavioural management approaches would be called a significant turning point in the evolution of management approaches.
3 'Leaders know the best course of action, whereas managers know only the best way to follow it.' **Evaluate** this statement.

7.3.4 Teams

A not-so-quiet revolution is rapidly transforming workplace cultures, practices, operations and productivity levels. Many businesses are starting to realise that a team approach can be the catalyst for superior performance. **Teamwork** involves people who interact regularly and coordinate their work towards a common goal.

BizWORD

Teamwork *involves people who interact regularly and coordinate their work towards a common goal.*



FIGURE 7.18 Graham Turner is the Managing Director and founder of Australian-based international travel management company Flight Centre. Flight Centre management adopts a participative management style, with a focus on working in teams and strong management skills, such as communicating and interpersonal skills.

Understanding how such teams function — that is, understanding the group dynamics of teams and teamwork, is vital for managers operating in the modern workplace. It is essential that managers foster a sense of cohesion between team members, otherwise the team is no more than a group of individuals all working separately. Such teams have no common purpose and therefore lack any sense of belonging to the organisation. In such cases, it is quite common for conflict to develop between team members. Ultimately, the team's effectiveness will be diminished.

These self-directed work teams alter some of the traditional roles of management. One obvious change is that managers have to work more closely with people over whom they have no apparent authority. They are required to adopt a team approach, negotiating consensus decisions rather than imposing demands.

Another significant impact of a team approach is the breaking down of the traditional pyramid-shaped hierarchical organisational structure. Hierarchical boundaries are disappearing as people and functions mix together to create much **flatter organisational structures**. Firms that adopt a flatter management structure reduce the number of levels of management, giving greater responsibility to individuals in the business (see figure 7.19).

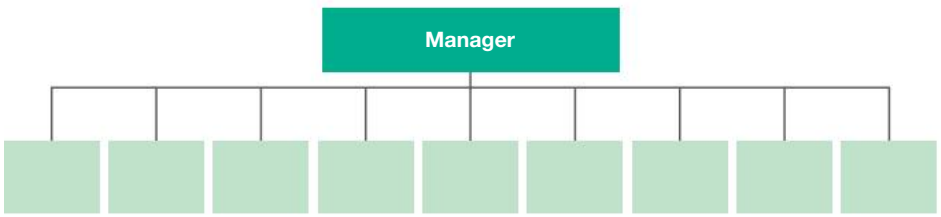


FIGURE 7.19 Flatter management structure — a typical organisation chart. The span of control is wider and management has more direct contact with employees.

The role of managers is therefore changing from controller to facilitator. Without being able to impose their authority, managers have to achieve their aims by balancing the needs of the team with those of the business. This can be accomplished by the manager attempting to understand the views of others, handling disagreements honestly and directly, and persuading others to adopt new ideas. Above all else, the manager must build a sense of trust, teamwork's key ingredient, and develop a common goal. To achieve this, it requires a move away from an autocratic leadership style to one that is more participative or democratic.

BizWORD

Flatter organisational structures *have evolved due to a 'de-layering' of management structures resulting in the elimination of one or more management levels.*

BizFACT

Are you able to work effectively in a team? That's the skill employers most want when they are recruiting new university graduates. Analysis of the recruiting activity on LinkedIn shows that teamwork skills are sought after among Australian employers, yet 63 per cent of hiring managers are finding it hard to find people with these skills.



FIGURE 7.20 To give purpose and direction to employees, managers require a good understanding of team/group dynamics.

SNAPSHOT



'Flatter structure provides a greater degree of flexibility.'

Case study: Companies with flatter management structures

While traditional hierarchical organisational structures are well suited for improving efficiency, they are not optimal for innovating and adapting to change. More and more businesses are adopting a flatter organisational structure.

Some high-profile adopters of this trend towards a flatter management structure include:

- **Valve.** Valve is an entertainment software and technology company who have developed leading-edge technologies and computer games like *Half-Life* and *Counter-Strike*. To create an environment that encourages innovation, Valve has zero layers of management between staff and owners. As their employee handbooks states: 'Welcome to flatland. We don't have any management, and nobody reports to anybody else.' Their employees have the autonomy to move forward with a project and are able to choose which jobs to work on.
- **GitHub.** GitHub is a web-based hosting service. The company has no middle managers and employees are not responsible to anyone. Employees have a high level of autonomy and self-direction and are encouraged to define their roles in ways that make sense to them.
- **Toyota.** Toyota has also recently flattened out in an attempt to avoid micromanaging their staff. Toyota's organisational structure underwent significant changes in 2013 as a response to the safety issues and product recalls that began in 2009. Their old structure had a strong centralised global hierarchy where the company headquarters in Japan made all the major decisions. Individual business units did not communicate with each other, and all communications had to go through headquarters. This structure was widely criticised for being too slow to respond to problems. Toyota's new flatter structure provides a greater degree of flexibility, which has led to the company being more capable of responding to changing influences in the business environment. This flexibility has also enabled the company to respond to issues more speedily and to provide higher quality products.

SNAPSHOT QUESTIONS

1. **Explain** the benefits of moving towards a flatter organisational structure.
2. **Determine** what some possible disadvantages for the above companies might be due to adopting a flatter organisational structure.

SUMMARY

- Teamwork involves people who interact regularly and coordinate their work towards a common goal.
- Well functioning teams can produce superior performance.
- Managers require a good understanding of team/group dynamics.
- The development of work teams has resulted in flatter organisational structures.
- The role of managers is changing from controller to facilitator.
- Businesses are adopting flatter management structures which results in:
  - 'de-layering' of traditional hierarchical structure
  - establishment of market-focused work teams
  - each work team responsible for a wide range of production functions.
- Reducing the levels of management gives greater responsibility to individuals in the business.

7.3.5 Participative or democratic leadership style

A manager who implemented a classical–scientific approach would normally adopt an autocratic leadership style; a manager who practised a behavioural approach would tend to use a more **participative** or **democratic leadership style** (refer to figure 7.11 on page 178).

A participative or democratic leader is one who asks employees for their suggestions and then seriously considers those suggestions when making decisions. In this sense they share their decision-making authority with their subordinates. The degree of sharing can range from the manager outlining a solution, with the possibility of changes being suggested, to allowing the team to participate in the initial decision making.

Sometimes referred to as the 'we' approach, participative or democratic managers recognise the strengths and abilities of employees and actively involve them in the decision-making process. This style is frequently practised in those businesses that have flatter management structures and work teams, and is especially effective in situations where there are diverse groups to be coordinated. The contribution of employees is valued, and employees assist in the decision-making process through regular meetings. Employees have a commitment to the business's goals because of

BizWORD

A **participative** *or* **democratic leadership style** *is one in which the manager consults with employees to ask their suggestions and then seriously considers those suggestions when making decisions.*

on Resources

Weblink: Democratic leadership



FIGURE 7.21 Researchers have found that the democratic leadership style is one of the most effective and leads to higher productivity, better contributions from group members and increased group morale.

their own input into the firm. This style of leadership is most effective when a business is operating in an environment undergoing rapid change. Individual employees accept responsibility and can implement changes themselves, making the business more responsive to change. Through activities such as brainstorming, a diverse range of opinions and ideas can be generated resulting in improved decision making.

The main advantages of the participative or democratic management style include the following:

- Communication is a two-way process.
- Employer/employee relations are positive and there is reduced likelihood of industrial disputes because employees are more likely to accept management decisions.
- Motivation and job satisfaction are optimal as employees feel they have played an active role in allocating tasks and implementing actions to meet objectives.
- Employees have a greater opportunity to acquire more skills.
- Power sharing encourages the development of work teams, and employees display high levels of commitment.
- There is a high level of trust, often resulting in improved employee performance.

The main disadvantages include the following:

- Reaching decisions and introducing tasks can be time consuming with differing views having to be considered. The quality of decisions may also suffer because compromises are made rather than decisive, clear directions given.
- The role of management, and the control of the manager, may be weakened and undermined, with employees given too much power in some cases.
- Internal conflict can arise with so many views and opinions being shared. More involvement may actually bring about disagreement.
- The importance of the organisational structure may be minimised, leading to an informal system that could result in a complete collapse in management.
- Not all employees want to contribute.

There is no simple answer to the question: 'What leadership style does a good manager possess?' Management is an art, not a science. This means that no simple management formula can be applied to deal effectively with all workplace situations.

SNAPSHOT



'… working with others is the best way to work.'

Case study: Jack Stahl — democratic leadership style

Jack Stahl is a former Chief Operating Officer and President of Coca-Cola, as well as a former CEO of Revlon. Through his democratic leadership style and knowledge, he brought these two companies to higher profitability. During his tenure at Coca-Cola, the net worth of the company grew from $3 billion to over $130 billion.

Jack Stahl believes that working with others is the best way to work. He knows how to delegate work to employees and can take a step back when necessary. Stahl achieves this through investing in training and development of staff. Training his employees to concentrate on the details reduces the need for micromanagement and allows him to pull back and worry about things from a more strategic perspective.

As a democratic leader, he encourages his employees to be involved in decision making. He keeps staff informed about matters relating to their work and shares problem-solving and decision-making responsibilities. While Stahl ultimately has the final say, he consults with staff before making a final decision. The teams he has led felt trusted and responded favourably to his style. Employees under his management demonstrated higher morale, team spirit and cooperation.

Stahl is a charismatic and visionary leader who is able to effectively communicate his vision to all relevant stakeholders, as well as inspire his employees to turn that vision into a reality. Stahl's inspirational qualities have enabled him to foster both individual and team effectiveness. He possesses an ability to produce results through the use of intrinsic rewards such as recognition, as well as rewarding successful

performance. Through his leadership skills he has been able to successfully align employees with each company's purpose.

SNAPSHOT QUESTIONS

1. **Demonstrate** how Jack Stahl adopts a democratic leadership style.
2. **Explain** the impact his leadership style would have on his employees.

SUMMARY

- A manager who adopts a behavioural approach will tend to use a participative or democratic leadership style.
- Participative or democratic leaders share their decision-making authority with their subordinates.
- This style of leadership is most effective when a business is operating in an environment undergoing rapid change.

7.4 Contingency approach to management

While the classical and behavioural management approaches continue to provide important lessons for managers, other ideas have also emerged during the last couple of decades (see figure 7.22). These contemporary management approaches represent major innovations in ways of thinking about management and appropriate management practices. One of the most important contemporary viewpoints is the **contingency approach** to management. It stresses the need for flexibility and the adaptation of management practices and ideas to suit changing circumstances.

BizWORD

Contingency approach *stresses the need for flexibility and adaptation of management practices and ideas to suit changing circumstances.*

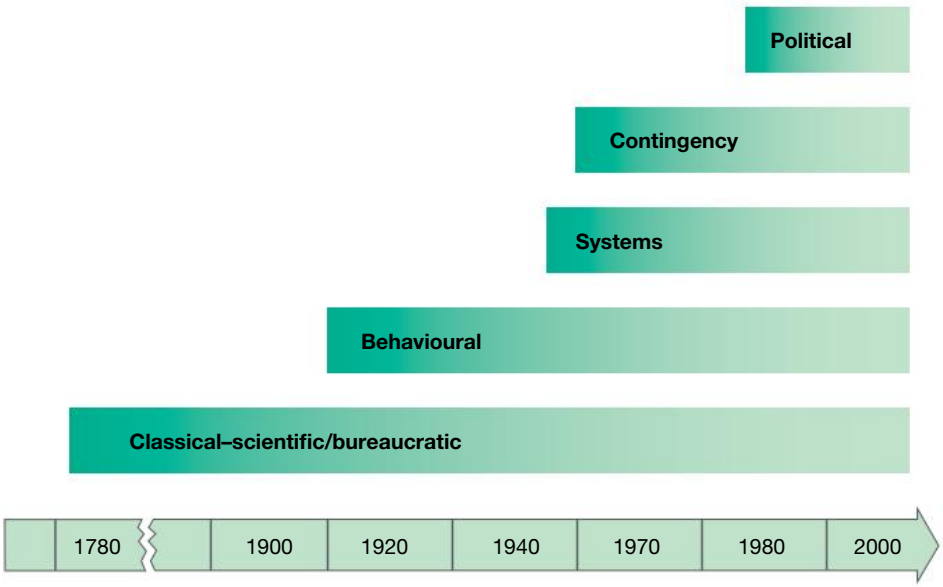


FIGURE 7.22 Timeline of management thought

7.4.1 Adapting to changing circumstances

Contingency theorists point out to managers that no two situations are absolutely identical. Each situation, therefore, requires its own unique solution. For example, you may have used a particular strategy to complete a task for assessment. Although this strategy may have been quite successful for that particular task, another assessable task may well require a completely different approach.

BizFACT

Managers are increasingly finding that creating a sustainable competitive advantage is not just about being the best at doing a particular thing. Instead, businesses must be really good at learning to do new things. Those businesses that thrive are the ones that are quick to read and act on signals of change.

BizFACT

Many companies have restructured in order to improve their ability to respond to change. Cisco, for example, had a traditional hierarchical structure. More recently they decentralised and created a more fluid structure and drove decision-making down to the front lines. This allowed the people most likely to detect changes in the environment to respond quickly and proactively.

Contingency theorists stress that the traditional classical approach to management was not necessarily wrong, but is no longer adequate for our needs today. They also urge managers to borrow and blend from a wide range of management approaches and practices.

Above all, advocates of the contingency approach believe that managers need to be adaptable and flexible in their technique to solving problems. Because management is a discipline that is continually evolving, it frequently produces new ideas and theories, each with some relevance to practitioners.

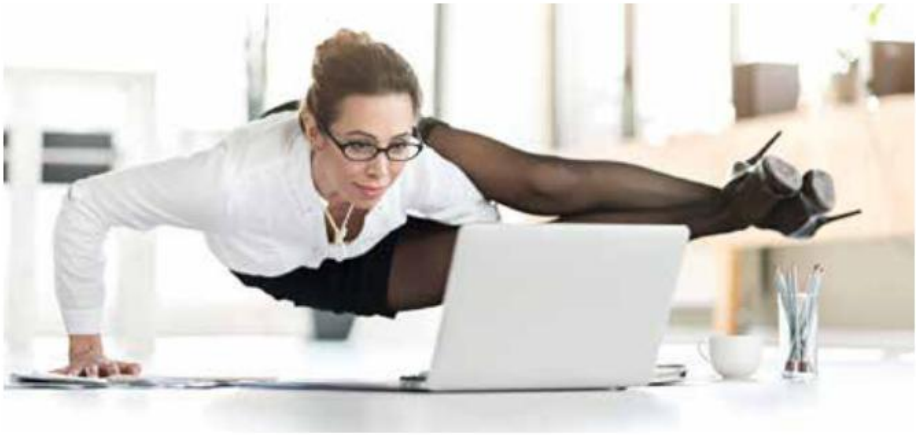


FIGURE 7.23 An appropriate management theory should be selected to suit the situation. Managers need to be adaptable and flexible.

The contingency approach, therefore, advocates that managers extract the most useful ideas and practices from a wide range to best suit their business's present requirements. It stresses that an appropriate management response to one set of circumstances may be quite inappropriate to another. To adopt this approach, managers must sample all the past and present ideas on offer; some refer to this as the 'smorgasbord' approach.

A manager adopting this approach will obviously need to apply the '10 commandments for the modern manager' (see figure 7.24). The advantages and disadvantages of the contingency approach to management are summarised in table 7.4.

THE 10 COMMANDMENTS FOR THE MODERN MANAGER

1. Share your vision with all relevant stakeholders.
2. Manage the relationships and the coalitions, not the employees.
3. Manage your own emotions and help others in the business to maintain an emotional balance.
4. Learn to thrive on diversity not conformity.
5. Lead, rather than simply managing, by inspiring trust and motivation.
6. Cultivate the ability to adapt to changing circumstances.
7. Learn how to access and use appropriate information and manage this knowledge effectively.
8. Be aware of how developments in technology can improve your effectiveness and efficiency.
9. Recognise and use the experiences and expertise of all employees.
10. Encourage ethical behaviour in order to promote pride and commitment in employees.

FIGURE 7.24 The 10 commandments for the modern manager

TABLE 7.4 Advantages and disadvantages of the contingency approach

Advantages	Disadvantages
• Acknowledges the impact of changes in the business environment and enables businesses to be more flexible in reacting to change • Recognises that there are multiple approaches to management and there is not one best way • Recognises that different situations demand different approaches	• Adapting to constant changes in the business environment can be challenging for management • The process of selecting alternative courses of action depending on the situation can be costly in terms of time and money

Managing change effectively

It is said that if you stop moving, you die. The same applies to organisations. They must keep changing and adapting to the never-ending pressure for change. But how do organisations know when they should change? What indications should an organisation look for? Although there are no clear-cut answers to these questions, the 'indications' that signal the need for change are found by examining the forces for change in both the internal and external environments.

We are in a time of extreme turbulence and rapid change. Many leading businesses have fallen behind in industries where they were once dominant, due to their inability to respond to changing circumstances.

How then should managers respond to unanticipated influences in the business environment? To survive, businesses need to embrace change. Managers need to be skilled in reading changes in their industry and then implementing strategies to leverage those changes. This requires leaders to create a work environment that is conducive to change. Sustained change requires constant communication, not only during the initial rollout but after the major adjustments have taken place.

Flexibility and short response time are critical to survival. Leaders need to minimise inertia by modifying the psychology. One of the biggest difficulties with introducing change is that people want things to stay exactly as they are. Leaders need to recognise this aversion to change and help employees adapt to new circumstances. The key to business success lies in management's willingness to accept change, respond speedily to influences in the environment and display empathy for those involved.

SNAPSHOT QUESTIONS

1. **Identify** where the 'indications' that signal the need for change are found.
2. **Explain** how managers should respond to changes in the business environment.

SNAPSHOT



'Organisations must keep changing and adapting to the never-ending pressure for change.'

SUMMARY

- The contingency management approach stresses the need for flexibility and adaptation of management practices and ideas to suit a particular situation.
- Due to the unstable business environment, managers need to be flexible and borrow and blend from a wide range of management approaches.

7.5 Compare and contrast approaches to management

Many managers may not have studied management in any formal way. However, most of them will have a management approach that reflects one of the management theories and management styles summarised in table 7.5.

TABLE 7.5 Summary and comparison of management approaches

Management theory	Characteristics and features	Organisational structure	Levels of management	Management styles
Classical approach	• Based on 'scientific' analysis of work processes • Highly programmed staff performing simple, repetitive tasks — single skilling, task specialisation • Time and motion studies used to reduce inefficiencies • Division of labour into function-related units, employees strictly controlled with tasks rigidly divided • Stresses how best to manage and organise workers so as to improve productivity • Views management as planning, organising and controlling	• Hierarchical pyramid structure reflecting strata in church, army and school • Hierarchical, linear flow of information, with a large amount of communication directed downwards • Strict channels of responsibility from the top down and grouping into specialised activities based on function, product or process with considerable management and supervisory control at each level	• Hierarchical pyramid structure • Many management and supervisory levels with clearly distinguishable and segmented organisational positions, responsibilities and roles • Bureaucratic management of authority believed to be the most effective means of controlling the workforce and ensuring that instructions are followed	• Autocratic • Course of action decided by management with little or no consultation with workforce • Workers believed to be prone to laziness and self-interest, so tight control and external motivation necessary to achieve required organisational goals and objectives
Behavioural approach	• Emphasises that people (employees) should be the main focus of the way in which the business is organised • Views management as leading, motivating and communicating • Recognition that workers have social needs in addition to economic needs • Teamwork and informal work groups important for productivity	• Flatter organisational structure with emphasis on teamwork	• Fewer levels of management	• More participative or democratic aspects emerging
Contingency approach	• Flexibility and adaptation of a variety of ideas and principles from a range of theories mean that a range of options may be pursued to suit the business's requirements	• May be pyramid, flat or decentralised organisational structure, depending on the business's requirements	• Depends on the business's requirements; that is, the nature of the operation and abilities of employees	• Depends on the requirements of the business

EXERCISE 7.4 REVISION

1. **Why** are work teams becoming more common in today's businesses?
2. **State** what impact the development of work teams has on a business's organisational structure.
3. Draw a hierarchical and a flat organisational structure. **Contrast** the two diagrams by listing their differences.
4. **Outline** in what ways self-directed work teams alter some of the traditional functions of management.
5. You have been appointed team leader of a new work group. **Describe** some of the strategies you could use to develop a sense of cohesion within the group.
6. **Outline** the main characteristics of the participative or democratic leadership style.
7. **Describe** a situation where the participative or democratic leadership style would be appropriate.
8. **Identify** what you consider to be the most important (i) advantage and (ii) disadvantage of the participative/democratic management style. **Justify** your answer.
9. **Deduce** the important lessons the contingency approach teaches managers.

EXERCISE 7.4 EXTENSION

1. Reflect upon what you have learned from this chapter. **Determine** which leadership style you would prefer to adopt if you were a senior manager. **Determine** what style of leadership would best suit you as an employee. Present your answers as an oral report to the class.
2. 'At TechVision Limited we do not rely on lists of rules and management authority. We believe our employees understand the link between productivity and profit, and act on it.' Nadall Behling, Managing Director.
   (a) **Identify** what evidence there is that Nadall Behling adopts a participative or democratic leadership style.
   (b) **Predict** the likely outcome if either your sports coach or your school principal adopted this leadership style.
3. **Discuss** the meaning of 'organisation' within the management process. **Construct** a typical organisational structure based on the classical management approach. **Construct** another organisational structure, this time based on the behavioural approach. **Determine** the strengths and weaknesses of the two approaches.
4. 'The contingency approach is centred on two basic questions: (1) What is the level of environmental uncertainty? (2) What type of organisational structure is most suitable?' **Predict** how a business should best respond to these questions.

on Resources

- **Digital doc:** Chapter summary (doc-26099)
- **Interactivity:** Chapter crossword (int-7223)
- **Interactivity:** Multiple choice quiz (int-7224)

CHAPTER 8

Management process

OVERVIEW

8.1 Introduction
8.2 Different ways of coordinating key business functions for a SME
8.3 Operations
8.4 Marketing
8.5 Finance
8.6 Human resources
8.7 Ethical business behaviour

8.1 Introduction

So far in this topic we have discussed only the 'what' of management. We have examined:

- the nature of management: its importance and what skills are needed to be an effective manager
- achieving business goals: what the manager wants the business to achieve
- management approaches: ideas about different ways of performing the task of management.

However, we now come to the 'how' of management: how the task of management is actually done. Once a business has established a set of specific goals, the next step is to determine what needs to be done to achieve the goals. **Strategies** outline how the business will attempt to achieve its goals. Strategies are the series of actions undertaken to achieve an end result. This requires managers to make decisions about how best to administer and coordinate the four key business functional areas — operations, marketing, finance and human resources. This responsibility of management is often viewed as the 'doing things right' responsibility.

BizWORD

Strategies *are the actions that a business takes to achieve specific goals.*

The focus of management's strategies is to ensure that the key business functions are performing efficiently and effectively in order to support and implement the business's overall intentions. Specialist managers in:

- *operations* focus on strategies to improve production processes and to create the ideal factory or office layout
- *marketing* determine the appropriate markets for the business's products, and decide on pricing, product features, promotion and channels of distribution
- *finance* are responsible for the financial requirements, budget allocation and financial record keeping
- *human resources* are concerned with the recruiting, training, employment contracts and separation of the employees who are required to run the business successfully.

BizFACT

Strategies are a number of actions to be undertaken to achieve a goal. Strategies involve:

- *what has to be done*
- *who is to do what*
- *when it is to be done*
- *what resources will be needed.*

For example, imagine if one of Toyota's goals is to increase its market share of hybrid motor vehicles. This would result in changes to the operations

function — how the cars are manufactured. The marketing function would need to develop plans for pricing and promoting the new type of motor vehicles. Additional finance would be required to fund the extra resources needed. Finally, new employees with the necessary skills will need to be recruited and selected, or existing employees retrained.

In a small business, the key business functions are normally carried out by few employees. They are required to undertake numerous tasks that will often overlap (see figure 8.4). Occasionally, a small business will decide to **outsource** one or more key business functions and concentrate on those functions in which it is most skilled. In large businesses, whole divisions or departments, such as the finance department or the marketing department staffed by many people, perform one specific function.

The key business functions are at the core of all businesses regardless of the business's size, location, purpose or length of existence.

BizWORD

Outsourcing *is the use of external sources or businesses to undertake business functions or activities for the business.*



FIGURE 8.1 Due to globalisation and increased pressure to reduce costs and be competitive, there has been a huge growth in the outsourcing of business functions. The aim is to take advantage of specialist skills and to achieve cost savings.

In most businesses, the key business functions are grouped to bring closely related tasks together. Thus, sales and marketing are grouped, finance and administration are grouped, and operations is grouped with research and development (R&D). Consequently, the range of functions is generally reduced to four main functions as is shown in figure 8.2.

The importance of the key functional areas is highlighted by the fact that the High School Certificate Business Studies course is structured around — and examines in more detail — the four key functional areas.

BizFACT

For a business to be successful, it is crucial that all the goals and strategies are linked and working harmoniously.

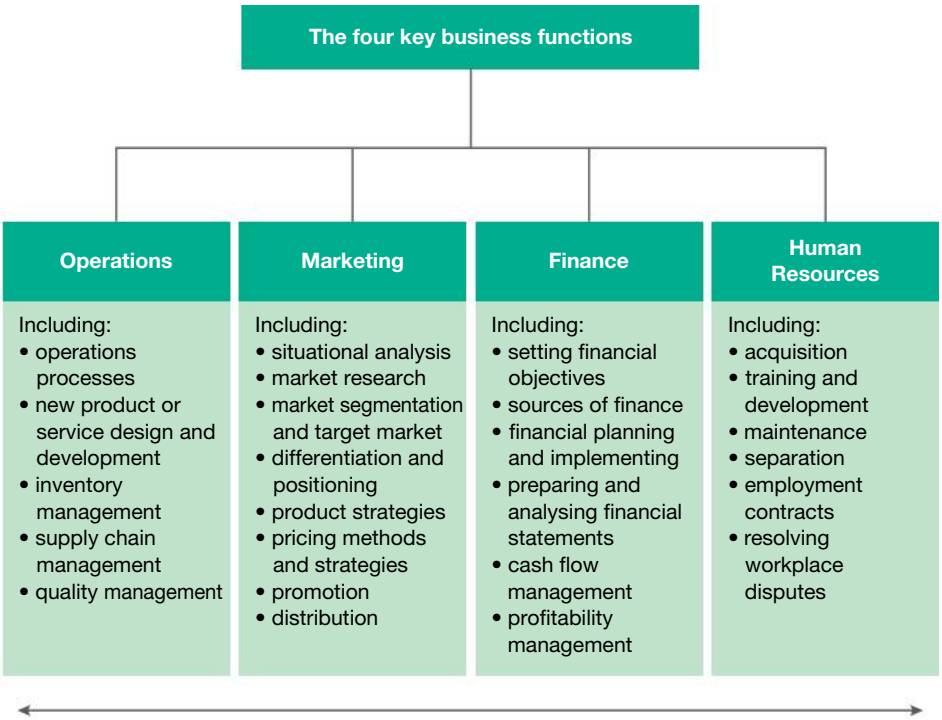


FIGURE 8.2 The four key business functions

8.2 Different ways of coordinating key business functions for a SME

BizWORD

Interdependence *refers to the mutual dependence that the key functions have on one another. The key business functions work best when they overlap, and employees work towards common goals. For each function area to perform at capacity, it depends on the support of the others.*

Though a business can separate the key business functions into departments that perform their distinct roles, the functions are interdependent — each relies on the others to perform effectively. **Interdependence** refers to the mutual dependence that the key functions have on one another. This means that the various business functions work best when they work together. A hockey team might have highly specialised players, for instance a brilliant left wing, a superb fullback and a dynamic goalkeeper. However, despite their individual brilliance, a side will usually win when all players contribute to the game, each working with the others in the team, passing, communicating and playing for the same victory. In the same way, each section of the business may perform its specialised function extremely competently — but if they together do not work as a 'team' and aim for the same business goals, then the business is not likely to achieve its objectives. Interdependence occurs when each key function area is committed to the

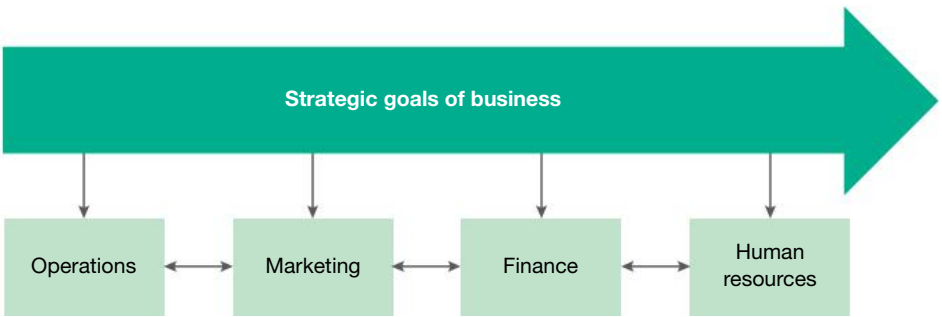


FIGURE 8.3 Although a business may separate the key business functions, they are all interdependent — each relies on the others to perform effectively. The key business functions work best when they overlap and employees work towards common goals. Each function area depends on the support of the others if it is to perform at capacity.

same business goals as the other key areas, and they each work in a coordinated and collaborative way to achieve these goals. Interdependence is always preferred because it provides a unified approach by the business as it works to achieve its objectives.

The coordination of key business functions depends on the broad goals of the business as well as its size. In large businesses, the key business functions are often separated into different divisions or departments headed by separate managers. This is because the key functions require quite different skills and knowledge. Also, as businesses grow, their needs become more complicated: they require many people to carry out each key function. This would mean that each division would have its own specialists. For example, in a large business the employment relations department would have specialists in salaries and pay, hiring of employees, staff training, work health and safety (WH&S), and so on.

The word **division** is often used by businesses to describe the separation of key functions. Division of a business along functional lines enables each part to specialise, but when the functions are separated, coordination between them becomes an important issue. In fact, the greater the divisional separation the more coordinated a business needs to be in order to run smoothly.

Most businesses are not in fact large but small. In the typical small business the work areas are not separated but often overlap. This is shown by the example of the hairdressing salon in figure 8.4.

BizWORD

Division *refers to the separation of key business functions into specialised units or departments. The business is divided into functional areas.*

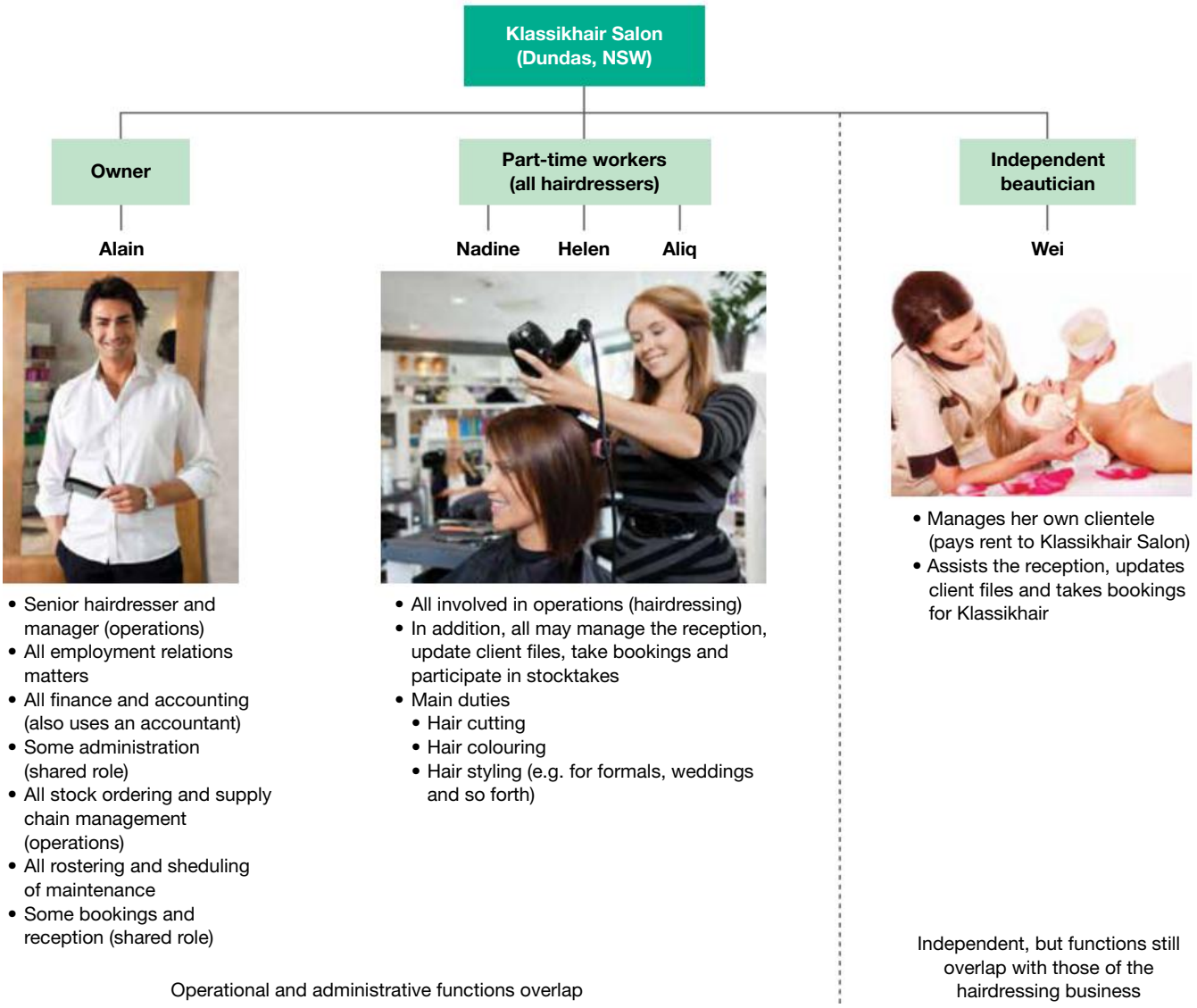


FIGURE 8.4 The overlapping of key functions as occurs in small business

SUMMARY

- Strategies are a series of actions undertaken to achieve specific goals.
- The four key business functions include:
  - operations
  - marketing
  - finance
  - human resources.
- The key business functions are interdependent — each relies on the other to perform effectively.
- All business functions should:
  - work towards the fulfilment of the business's goals
  - be coordinated so that they have a common purpose.
- In large businesses, the key business functions are often separated into divisions or departments.
- In small businesses, the key business functions are not separated but often overlap.

EXERCISE 8.1 REVISION

1. **Define** the term 'strategies'.
2. **Recall** the focus of the strategies developed by management.
3. **Identify** the four key business functions.
4. **Examine** figure 8.2 in section 8.1. **Recall** two activities involved in each of the four key business functions.
5. **Why** are the key business functions sometimes outsourced in small businesses?
6. **Recount** what occurs when there is interdependence between the key business functions.
7. **Why** are the key business functions often separated into different divisions or departments in large businesses?
8. **Demonstrate** what is meant by the overlapping of key business functions.
9. **Explain** why the key business functions need to be coordinated in a business that has separate divisions.

EXERCISE 8.1 EXTENSION

1. **Determine** why it is impractical to expect small businesses to have distinct functional areas.
2. **Predict** what will happen to a business whose key business functions are not united in trying to achieve the business's overall intention.

8.3 Operations

If you have ever attempted to prepare a meal, you will know that you need ingredients and a recipe, or a method, to create a final product. Just like you, businesses will follow a recipe when they are producing their good or service. The area of management that is responsible for this is known as 'operations'.

Operations refers to the business processes that involve transformation or, more generally, 'production'. It is a term that applies both to the manufacturing and the services sector. As explained in section 8.1, all businesses establish a set of goals. Next, the business implements strategies to achieve these goals. The core goal of all businesses is to maximise profits. This is often best achieved through the efficient production of a good or service. Operations management is the strategy used to achieve this goal. The HSC course investigates operations in greater depth, so this chapter will provide an elementary understanding of the main concepts.

Operations management consists of all the activities in which managers engage to produce a good or service. It is concerned with creating, operating and controlling

BizWORD

Operations *refers to the business processes that involve transformation or, more generally, 'production'.*

Operations management *consists of all the activities in which managers engage to produce a good or service.*



FIGURE 8.5 The operations function within any business is shaped by the range and types of goods and services that are produced. Management of operations will differ for businesses producing goods as opposed to those producing services.

a transformational process that takes inputs from a variety of resources, and produces outputs of goods and services that are needed by customers. When you buy a loaf of bread from the supermarket, for example, the bakery will have undertaken a number of processes from buying the ingredients, to mixing and blending them, baking, cooling then wrapping the finished loaves and, finally, delivering the loaves to the retail outlets.

Operations management, therefore, is at the heart of the success of all businesses. Production involves the skilful bringing together of a number of resources, such as finance, equipment, management, technology and people, to create finished goods and services through a series of operations (see the following Snapshot).

Case study: Visy — Operations

Visy is a provider of recycling, paper and packaging products and services. The following is an overview of the main operations strategies that have given the company a competitive advantage and enabled it to be a world leader in its industry.

Processes

Visy has eight paper machines across Australia that are used to produce high-quality recycled paper for the packaging and building industries. The machinery used to manufacture this paper offers flexibility so that they are able to produce a variety of different papers using the same machines. In 2015–16, their machines produced over 1.4 m tonnes of paper, coated liner and plasterboard liner, and over 670 000 tonnes of unbleached kraft paper.

Visy's Reliability and Manufacturing Systems teams ensure that the extensive equipment and systems in their mills are reliable, effective and efficient.

Technology

Visy's Automation team specialises in the engineering and integration of robotic handling and packaging equipment solutions in order to achieve their main objectives of increased productivity, profitability and safety.

Visy also continuously invests in research and development and leading-edge technologies. The company is committed to continuous growth and improvements to ensure it offers the best facilities and services to its customers.

SNAPSHOT



'… increased productivity, profitability and safety.'

Logistics

The guiding principle for Visy's logistics team is 'to make sure we deliver, no matter what'. Originally, its logistics team was responsible for transporting Visy's own products. Now, many customers have taken advantage of Visy's speedy and efficient services and use them for their own deliveries.

Quality management

Visy is committed to continuous improvement in both product quality and service. Many areas of its business operations are accredited, which is achieved by compliance to stringent externally audited standards that are stipulated by internationally recognised regulatory bodies. The company also regularly implements benchmarking programs to compare its business operations against world's best practice.

Visy offers superior technical back up and support and works cooperatively with customers to establish continuous improvement processes to reduce damage and waste throughout the entire supply chain.

SNAPSHOT QUESTIONS

1. **Outline** Visy's manufacturing processes.
2. **Discuss** Visy's investment in leading edge technologies.
3. **Explain** the importance of continuous improvement.

BizFACT

Due to the enormous costs involved in operations processes, many businesses try to gain a competitive advantage through cost leadership. This involves aiming to have the lowest costs in the market. To achieve this, operations managers aim to continuously find ways of minimising costs.

The nature and type of operations vary considerably from one type of good or service to another. However, how the operations management function is carried out will directly affect a business's competitive position because it will:

- establish the level of quality of the good or service
- influence the overall cost of production, given that the operations function is responsible for the largest part of a business's capital and human expenses
- determine whether sufficient products are available to satisfy consumer demand.

The operations management function has a considerable influence on the quality, cost and availability of a business's goods or services. These, in turn, have a direct bearing on whether the business achieves its other main goals — specifically, to maximise profits, to increase market share, to maximise growth or to provide a reasonable return for investors.



FIGURE 8.6 Australia Post highly values operations. Ahmed Fahou, the CEO, stated in a business briefing: 'We have streamlined our operations through automation and process improvement, which has delivered productivity improvements of 5 to 6 per cent, per annum. We have 3000 less people and run a very lean and efficient operation, handling 20 million items, 11 million addresses and 1 million customers in our shops every business day. These changes are necessary to provide the contemporary services and solutions that Australian government, businesses and citizens need.'

8.3.1 Goods and/or services

A manufacturer will transform inputs into goods: tangible products. **Tangibles** are physical products that can be handled and stored before they are sold to the consumer, such as bread, clothing or a car. The production process and consumption are not linked; that is, there is little customer involvement in production.

A service organisation will transform inputs into services. Services are **intangible**, which means that they cannot be touched. For example, if you attend a training course, you cannot physically touch it, but you hopefully benefit from gaining knowledge and learning new skills. Services cannot be stored and the customer may actually need to be present when the service is being delivered. For example, the customer must be present when receiving a haircut.

In reality, many businesses today produce a combination of both manufactured goods and services. When you purchase a product such as a car or electronic equipment it often comes with a warranty and other services. When a customer enters a contract with an internet provider, for example, they will receive a service (their broadband connection), plus the modem and other goods necessary to enable the connection.

BizWORD

Tangibles *are goods that can be touched.*

Intangibles *include services that cannot be touched.*

on Resources

eLesson: Café KitcCh and Hudsons Coffee (eles-0837)

SUMMARY

- Operations management is about producing goods and/or services based on business goals.
- The operations management function has considerable influence on the quality, cost and availability of a business's goods and/or services.
- Operations management is responsible for transforming inputs into outputs.
- The characteristics of operations management differ according to whether the business is a manufacturer of goods or a provider of services. Manufacturers produce tangible products (physical), while service organisations produce intangible products (services).
- Most modern businesses produce a combination of both manufactured goods and services.

EXERCISE 8.2 REVISION

1. **Define** the terms 'operations' and 'operations management'.
2. **State** what operations management is concerned with.
3. 'Operations management is the part of the business that actually gets the job done.' **Demonstrate** this concept on a smaller scale by describing the materials you would need and the process you would undertake to bake a cake (your finished product).
4. **How** will the operations management function directly affect a business's competitive advantage?
5. **Distinguish** between a good and a service.
6. **Account** for why modern large businesses combine goods and services.

EXERCISE 8.2 EXTENSION

1. One strategy to produce goods more quickly is to use better technology. For example, if you used a hand beater to bake a cake it may not have been as efficient as using an electric beater. Fill in the following table and **determine** some strategies that an operations manager might use to achieve the listed business goals. The first entry has been completed for you.

Business goal	Operations management strategy
Improve the quality of service provided	Introduce quality management
Improve the quality of the product	
Reduce production costs	
Contribute to the protection of the natural environment	
Increase profitability	
Increase market share	

2 Use the internet or look at the careers section of the newspaper to find a job advertisement for an operations manager (sometimes called a factory manager). The advertisement will most probably list responsibilities involved in the position. **Classify** these into the four management roles (planning, organising, leading and controlling).

3 Anita's Cosmetic and Beauty therapy is a business specialising in a range of cosmetic and beauty enhancement treatments and products. **Determine** the range of operations activities offered in such a business.

4 **Demonstrate** how an operations manager of a manufacturing plant that produces confectionery might use the roles of planning, organising, leading and controlling in his or her daily job.

8.3.2 The production process

There are three key elements of the production process in any business: inputs, processes and outputs.

BizWORD

Inputs *are the resources used in the transformation (production) process.*

Transformed resources *are those inputs that are changed or converted in the operations process.*

Transforming resources *are those inputs that carry out the transformation process.*

Inputs

Inputs are the resources used in the transformation (production) process. Some resources are already owned by the business, while others come from suppliers. Inputs differ between manufacturing businesses and service businesses. Inputs may be divided into those that are transformed and those that are transforming resources.

Transformed resources are those inputs that are changed or converted in the operations process; they are transformed by the operations process. Transformed resources include:

- *materials:* the basic elements used in the production process.
- *information:* the knowledge gained from research, investigation and instruction, which results in an increased understanding.
- *customers:* customers become transformed resources when their choices shape inputs.

Transforming resources are those inputs that carry out the transformation process. They enable the change and value adding to occur. The two main transforming resources are:

- *human resources:* the people that are employed by the business.
- *facilities:* the plant (factory or office) and machinery used in the operations process.

BizWORD

Transformation *is the conversion of inputs (resources) into outputs (goods or services).*

Transformation processes

The main concept of operations management is **transformation**, which is the conversion of inputs (resources) into outputs (goods or services). Sony, for example, takes plastic, metal, glass and electronic parts, and transforms them into numerous electronic products using an innovative approach and processes of design, manufacturing and assembly. Figure 8.8 illustrates this transformation process.

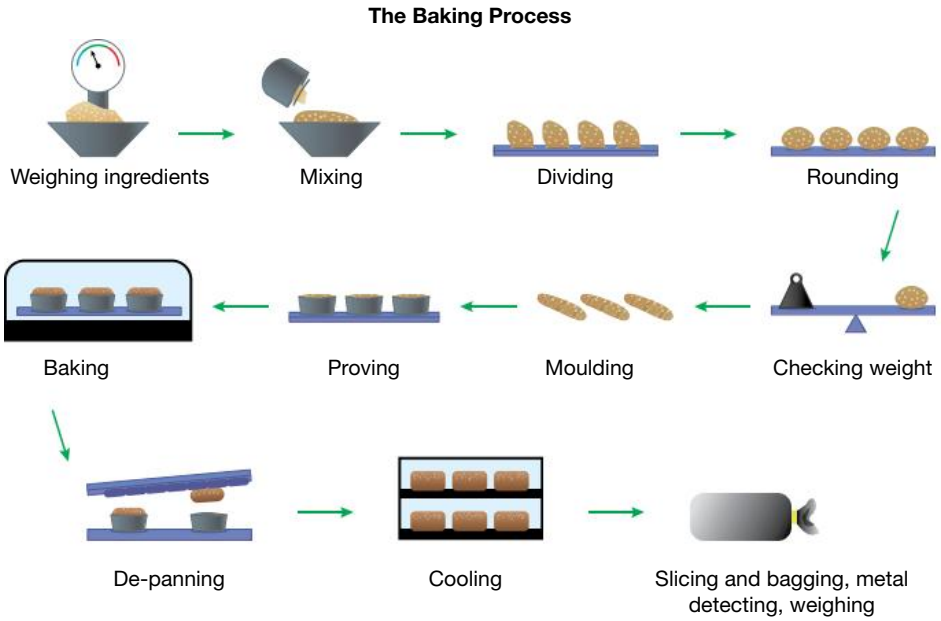


FIGURE 8.7 Tip Top Bakeries currently has over 13 bakeries across Australia and New Zealand and produces around 1 000 000 baked products every day. The main inputs include flour, yeast, water, salt and labour. Their transformation process is very similar to how you'd bake a loaf at home, but on a larger automated scale. It relies on four steps: mixing, proving, baking and cooling. The difference is that their machinery speeds up the process and removes the need for kneading the dough.

The term 'transformation' implies physical changes, but today it also includes the conversion of resources into services. Your school takes its main inputs — the students, the syllabus, the teaching and ancillary staff, and the buildings and other capital — and produces educated, employable graduates. What occurs in this educational setting is a transformation process. It is the task of the operations manager to create, operate and control the transformation process, and table 8.1 illustrates how this happens in a number of different businesses.

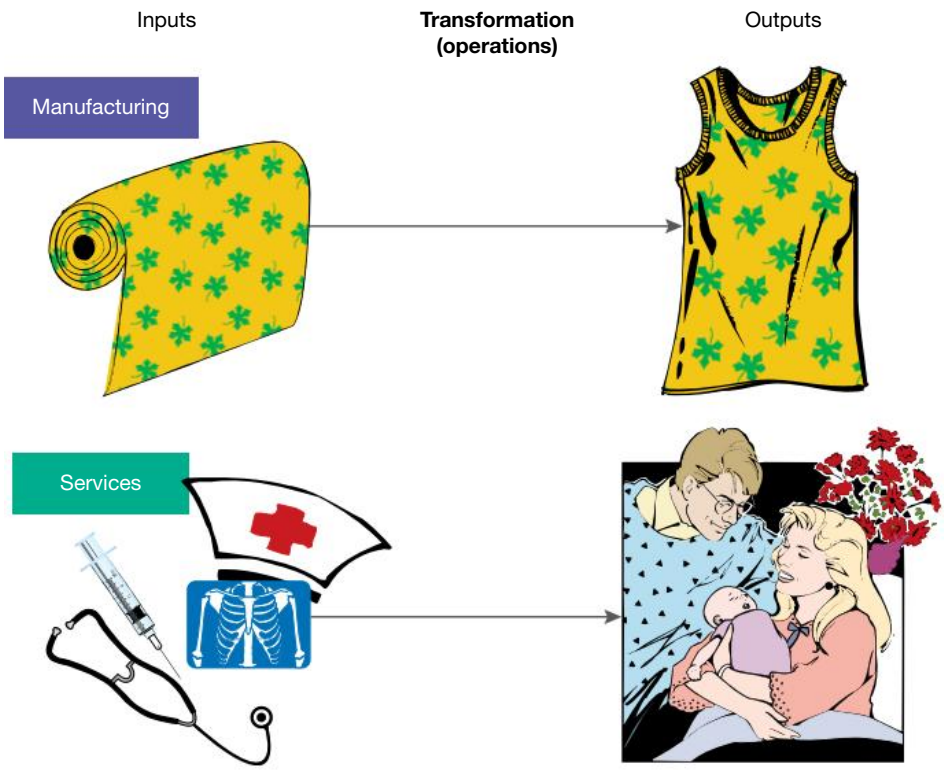


FIGURE 8.8 The transformation process in a clothing factory and a private hospital

BizFACT

Businesses can become more competitive by looking at their production processes. For example, the 'better mango project' identified why so many mangoes were arriving at retail outlets bruised or overripe. Better handling techniques and temperature control have resulted in more consistent fruit quality and better profits.

TABLE 8.1 The transformation process in a manufacturing and service business

Inputs supplied by existing resources or external supplier	Transformation process	Outputs — either goods or services
Clothing factory Pattern cutters, designers, drivers, machine operators, material, sewing machines, labourers	Computer-based designing, dyeing, hand and machine cutting, machining, branding, manual random checking	Dresses, shirts, suits, trousers etc.
Private hospital Nurses, doctors, operating theatre, computers, beds, drugs, laboratory, X-ray facilities	Consultation, diagnosis, assessment of alternatives, treatment (referral to specialist or done by a general practitioner, GP)	Patient returned to health

Owing to the vastly differing nature of business, the transformation process varies from business to business. It is often useful to look at the transformation process in a manufacturing business separately from the process in a service-based business because the transformation processes in manufacturing are far more visible and more easily quantified.

Transformation process in manufacturing businesses

The manufacturing process may involve different kinds of processing. One type takes the most basic resources and transforms them into the final goods for the use of consumers. Other types involve a step-like transformation across a range of processors and businesses.

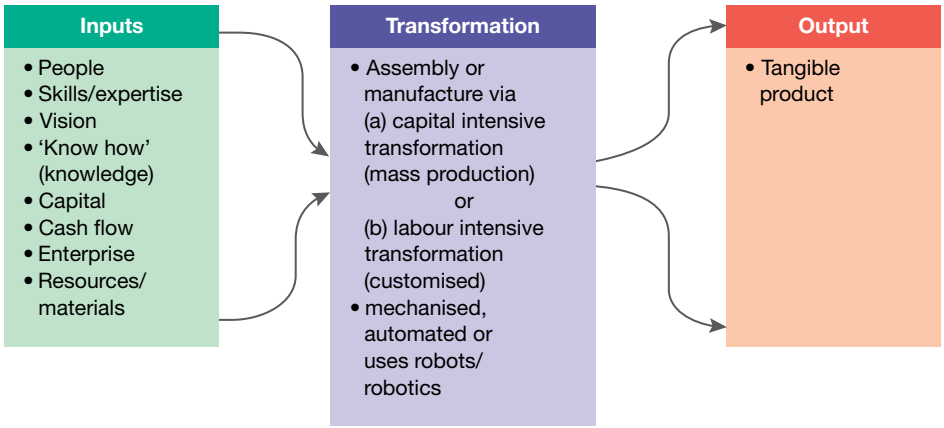


FIGURE 8.9 Operations in the manufacturing process

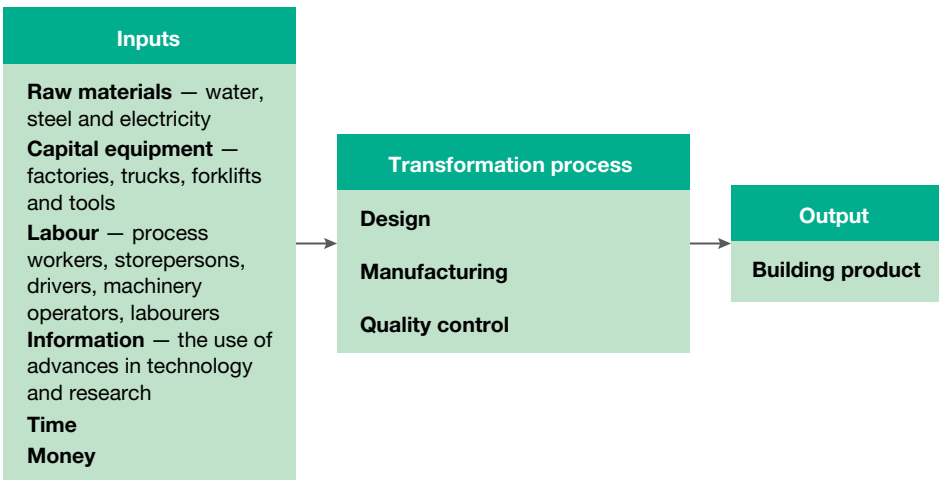


FIGURE 8.10 An operations system for a manufacturing company producing building products

Transformation process in service businesses

Due to the intangible nature of services, the operations processes are less physical or visible. They take the form of knowledge, inputs, expertise and so on (see figure 8.11).

BizFACT

Due to the intangible nature of service businesses, the operations processes are less physical or visible.

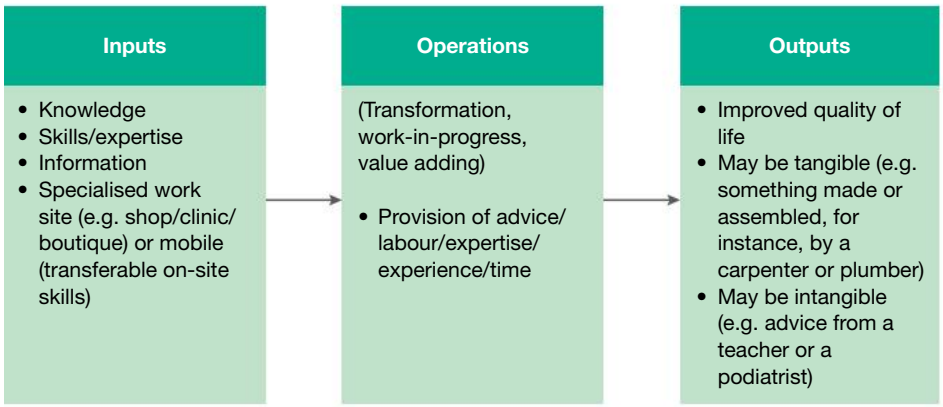


FIGURE 8.11 Operations in service businesses

Transformation processes adopted by service businesses differ from those in manufacturing businesses for two reasons:

1. Outputs of the service business cannot be physically held in stock. A bank, for example, cannot perform transactions on behalf of customers in advance and store these in anticipation of use at a future date.
2. Service businesses rely heavily on interaction with the customer in determining the output. Before an output is generated, the bank, in the example, needs the customer to indicate whether he or she requires a car loan, a deposit, a withdrawal or any other particular service.
3. Service businesses are more labour-intensive. Having skilled employees is crucial as this will impact on the quality of the service provided.

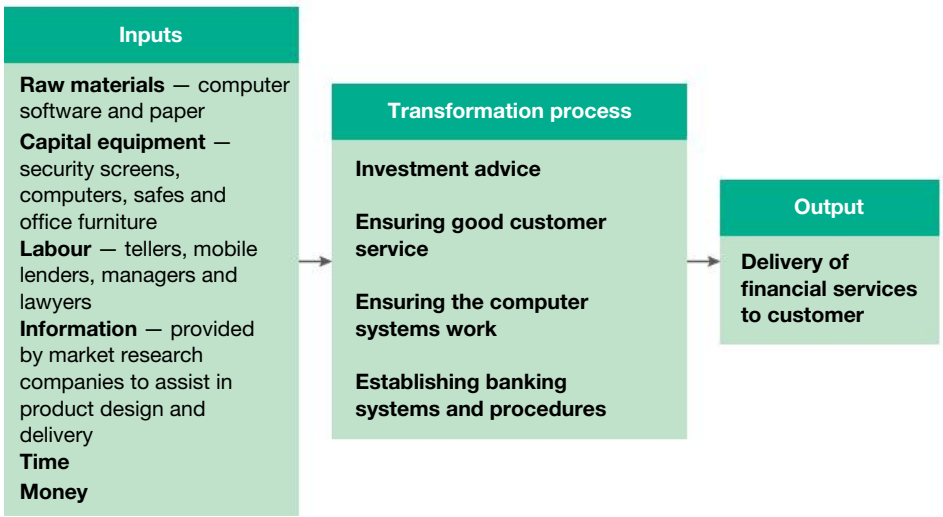


FIGURE 8.12 An operations system for a bank

Table 8.2 highlights the main differences between manufacturing and service operations.

TABLE 8.2 Highlighting the difference between manufacturing and service operations

Manufacturing operations	Service operations
Tangible items are produced — they may be customised, but generally they are standardised and often mass produced.	Intangible and customised, or made to suit the individual's requirements
Generally located close to supplies of raw materials or inputs (transport costs are of major concern)	Must be close to markets — location and proximity to users of services is vital
Zoning determines actual siting.	Zoning may allow for home-based flexibility.
High capital costs in operations but can achieve some economies of scale	High training/education costs but can operate with low capital costs
Employs unskilled or technically skilled people, so average cost of labour/workforce is low.	Focus is on skilled/experienced/semi-skilled and professional staff, so labour costs are relatively higher.
Quality of output is standardised and backed by warranty.	Quality varies depending on the strength of industry regulations, skill, experience, knowledge and honesty of practitioner. Backed by public liability insurance. Customer or client relations are 'everything'.
Uses manufacturing technology	Uses office automation
Manufacturer generally makes the product and then awaits sale (thereby risking unsold stock).	The server only acts once the demand for a service is identified — hence less risk.
The goods last beyond the time over which they are paid for — they tend to be durable.	Services by their nature are inherently non-durable, though the actual work done may have lasting effects.

BizWORD

Outputs *refer to the end result of a business's efforts — the service or product that is delivered or provided to the consumer.*

Outputs

Essentially, **outputs** refer to the end result of a business's efforts — the good or service that is delivered or provided to the consumer. So far, a distinction has been drawn between service and manufacturing operations, but in many cases businesses carry out both types of operation. Toyota, for example, separates its vehicle manufacturing operation from its customer service operation, although both elements are critical to the business's overall success. All businesses carry out many activities that can be isolated from direct involvement with the customer. Insurance companies employ mathematicians called actuaries who use formulas to determine risk and probability in setting the level of insurance premiums. Actuaries never deal directly with the public, but are instrumental in forming parameters or boundaries in which operations will occur.



FIGURE 8.13 The Australian Business Award for Service Excellence recognises small, medium and large organisations that have achieved outstanding results and demonstrate leadership to service excellence. The Observatory hotel in Port Macquarie won the small business award in 2016 due to their commitment to service improvement. The hotel has created an extensive framework for reviewing guest feedback. Once issues are identified, fortnightly meetings are held to project manage improvement initiatives. The hotel also has a loyalty program and uses incentives to create staff engagement.

The operations manager must be able to link transformation processes to the activities performed by other areas of the business. Output must always be responsive to customer demands. Issues of quality, efficiency and flexibility must be balanced against the resources and strategic plan of the business.

While the most obvious output of the transformation process is the goods made or services provided, there are other, more subtle outputs. For example, customer service (which refers to how well a business meets customer expectations) (see figure 8.13) and warranties (promises made by a business to correct any defects in the goods they produce or the services they deliver).

SUMMARY

- The three key elements of the production process include inputs, the transformation process and outputs.
- Inputs are resources used in the production process and include raw materials, capital equipment, labour, information, time and money.
- The transformation process is the conversion of inputs into outputs.
  - Transformation processes in manufacturing businesses are different to those of service-based businesses.
- Outputs are the finished goods or services.

EXERCISE 8.3 REVISION

1. **Identify** the three key elements of the production process.
2. **Distinguish** between the two types of inputs.
3. 'The main concept of operations management is transformation'. With reference to an example, **clarify** the meaning of this statement.
4. **Why** do the transformation processes adopted by service businesses differ from those in manufacturing businesses?
5. Using the process of completing homework, for example, **construct** a diagram that describes the operations component (that is, the transformation from *no* homework done to *all* homework completed).
6. **Identify** the inputs, processes and outputs of the following businesses:
   (a) Hilton Hotel
   (b) Four 'n' Twenty pies.
   Present your answer in table form, as shown in table 8.1 in section 8.3.2.
7. **Distinguish** between 'input', 'transformation' and 'output'.
8. The Rio Tinto Group is an international mining company. Rio Tinto finds, mines and processes mineral resources, which are then converted to products such as coal, copper, gold and silver. **Identify** the inputs, transformation processes and outputs that Rio Tinto uses to produce its products. The weblink **Rio Tinto** in the Resources tab can help you get started.
9. **Discuss** the main differences between the operations function in a manufacturing business and a service-based business.

EXERCISE 8.3 EXTENSION

1. Use the **Cameron Balloons Virtual Factory** weblink in the Resources tab to find the Virtual Factory link. Go to 'Factory floor' and then to 'Production'. Complete the following tasks.
   (a) **State** the stages of production involved in the manufacturing of hot-air balloons.
   (b) **Identify** the inputs, processes and outputs of the balloon factory.
   (c) **Determine** what type of layout is used at the Cameron Balloons plant. Give reasons for your answer. (*Hint:* Examine fixed position layout, product layout, process layout.)
   (d) **Extrapolate** why this type of layout would have been chosen.
   (e) **Propose** whether the production of balloons is capital intensive or labour intensive. Give reasons for your answer.
2. Contact a manufacturing business and survey its response to a range of questions that you, or a small group, have written and emailed regarding the operations function in their business. **Synthesise** your findings and present them to the class.
3. Contact a service-based business and survey its response to a range of questions that you, or a small group, have written and emailed regarding the operations function in their business. **Synthesise** your findings and present them to the class.

on Resources

Weblink: Rio Tinto

Weblink: Cameron Balloons Virtual Factory

8.3.3 Quality management

Quality management is the strategy which a business uses to make sure that its product meets customer expectations. Three quality approaches are quality control, quality assurance and total quality management.

Quality refers to the degree of excellence of goods or services and their fitness for a stated purpose. Quality is very important to Darrell Lea due to the strong focus on customer needs (see figure 8.14). A quality product should have a high degree of excellence and should achieve its stated purpose. A quality product should be reliable, easy to use, durable, well designed, delivered on time, include after-sales services, and have an agreeable appearance.

BizWORD

Quality management *is the strategy which a business uses to make sure that its products meet customer expectations.*

Quality *refers to the degree of excellence of goods or services and their fitness for a stated purpose.*



FIGURE 8.14 Darrell Lea is committed to product quality due to its strong focus on customer needs. The company prides itself in the manufacturing of fine quality confectionery and is committed to continuous improvement so that its products consistently meet customers' needs and comply with food safety regulations. Quality Systems are an integral part of Darrell Lea's management programs. It employs an independent, third party auditor to assess its processes on a regular basis. Feedback from these audits provides valuable input into the company's continuous improvement process.

8.3.4 The benefits of quality management practices

The benefits of implementing quality management practices include:

- reduced waste and defects
- reduced variance in final output
- strengthened competitive position
- improved reputation and customer satisfaction
- reduced costs
- increased productivity and profits.

Operations managers use a variety of approaches to maintain or improve quality. Some of the main quality management strategies include quality control, quality assurance and quality improvement.

BizFACT

Since they entered the Australian market in the late 1990s, Havaianas have been the choice of thong for many Aussies. While they charged a higher price, customers were willing to pay more due to their sturdy, long-lasting rubber and better quality. The brand has recently experienced a decline in popularity, due to an influx of complaints regarding a drop in quality and poor longevity. While Havaianas offer a six-month replacement warranty, this does little to address why they're breaking in the first place.

Quality control

Quality control involves the use of inspections at various points in the production process to check for problems and defects. Quality control reduces problems and defects in the product using inspections at various points in the production process. Many businesses have minimised errors and waste by ensuring that standards are met. Specifications or benchmarks are set before the physical checks are completed. Actual performance is then compared to the established criteria. If the established standards are met, it is likely that the business will be meeting customer

BizWORD

Quality control *involves the use of inspections at various points in the production process to check for problems and defects.*

expectations. Competitiveness increases as the costs associated with waste and faulty products are reduced.

In a service business, an inspection of employee performance can be used as a means of quality control. A bank might inspect teller accuracy, speed or courtesy. In a call centre calls might be monitored for quality assurance and control purposes.



FIGURE 8.15 Beneath the grass of the MCG lies five kilometres of PVC drainage pipe that stops the surface from becoming waterlogged. This pipe is made by Vinidex Pty Ltd, Australia's leading manufacturer of thermoplastic pipe systems. The high-quality pipes produced are also used to pump gas through vast pipelines in NSW and South Australia. Vinidex use meticulous quality control, as well as quality inputs, to maintain excellent customer service. New materials, as well as the processing technology and manufacturing equipment, are carefully examined to make sure that Vinidex continues to achieve high standards in the industry.

BizFACT

Samsung continuously upgrades its quality management system, in an effort to achieve the best quality in all products and services that surpass all expectations. The quality management system consists of four evaluation criteria: reliability, functionality, process and application. Samsung uses state-of-the-art facilities and equipment for all its tests and analysis in order to achieve and maintain the best quality at all times.

Quality assurance

Quality assurance involves the use of a system so that a business achieves set standards in production. This is a proactive approach to quality management that aims to prevent defects or problems from occurring.

BizWORD

Quality assurance *involves the use of a system so that a business achieves set standards in production.*

Quality assurance is an integral part of operations. Most organisations have a quality management system in place to ensure that set standards are achieved. The ISO 9000 series of quality certifications is a widely used international standard. 'ISO' stands for International Organization for Standardization. Meeting these international standards is voluntary, but many businesses comply with their requirements to remain competitive locally and internationally. The ISO provides guidelines on how businesses should establish quality assurance systems by adopting specific procedures, controls, and recording and documentation measures. An effective quality management system gives assurance to customers that a business is able to provide safe and reliable products.

Quality improvement

Quality improvement focuses on two aspects: total quality management and continuous improvement.

Total quality management

Total quality management (TQM) is a commitment to excellence that emphasises continuous improvement in all aspects of a business's operation by sharing responsibility among all the members of the business. Quality becomes both a commitment and the responsibility of every employee in the business. The aim of TQM is to create a defect-free production process, and maintain a customer focus in operations. The adoption of TQM can improve the price competitiveness of a business, but can also improve product quality, allowing the business to attain competitive advantage. To achieve TQM objectives a number of approaches may be used, such as employee empowerment, continuous improvement and improved customer focus.

BizWORD

Total quality management *is an ongoing, business-wide commitment to excellence that is applied to every aspect of the business's operation.*

SNAPSHOT



Quality management process: Plan, Do, Check, Act

Comparison of quality assurance and quality control

Quality assurance …	Quality control …
A system for ensuring quality in the processes by which products are developed so that a business achieves set standards in production.	The use of inspections at various points in the production process to check for problems or defects.
Aims to prevent defects or issues.	Aims to identify and correct defects.
A proactive approach to quality management.	A reactive approach to quality management.
A preventive technique.	A corrective technique.
Has the goal to improve processes so that defects do not occur during production.	Has the goal to find defects after a product is developed and before it is sold.
Establishes standards and procedures that need to be adhered to in order to meet customer requirements.	Verifies that procedures are followed and standards are met.
Sets up measurements to evaluate processes.	Verifies if products meet specific measurements.
A process-oriented exercise.	A product-oriented exercise.
Everyone's responsibility.	The responsibility of a specific team that tests products for defects.

The quality management process can be summarised into four key steps:

- Plan = perform quality assurance by determining the product's quality requirements and standards and establish processes about how these will be met
- Do = develop the product and apply the quality requirements and processes
- Check = undertake quality control by inspecting the product to ensure standards are being met and that there are no defects
- Act = take corrective action if needed









W. Edwards Deming was an American quality expert who was known as the 'founder of the quality movement' and is credited with the development of TQM. Deming believed that quality problems would be best solved with an emphasis on employee involvement. Many businesses use **quality circles** as a means of achieving employee empowerment. Under this approach, teams of up to 10 workers meet regularly to solve problems related to process, design or quality. The groups often make presentations to management with their ideas, in order to improve the performance of the business. Such programs have resulted in substantial cost savings for organisations — for example, at the Northrop Aircraft division that produces Boeing 747s, 55 individual quality circles halved the cost of parts within two years. At Chrysler, a quality circle discovered that heating rubber seals before installation could prevent car door leaks.

Continuous improvement

Continuous improvement is a process that involves a constant evaluation of, and improvement in, the way things are done. Higher and higher standards are set in the continual pursuit of improvement. *Kaizen* (Japanese for 'improvement') emphasises continuous improvement in all facets of a business, from the way the CEO manages to the way assembly line workers perform their jobs. Although perfection is practically impossible to achieve, it is the 'striving' that is important to business culture.



FIGURE 8.16 *Kaizen* is the heart of the Toyota Production System. The Toyota mass-production process requires that all tasks, both human and mechanical, be very precisely defined and standardised to ensure maximum quality, eliminate waste and improve efficiency. Employees have a responsibility to not only closely follow these standardised work guidelines but to also seek their continual improvement. The day-to-day improvements that employees make to their working practices and equipment are known as *kaizen*.

Deming believed that quality should be the responsibility of every employee. The TQM approach considers one of the most important questions a business should ask: 'What does the customer require?' All teams need to realise that they are serving a customer. This is as true for the employees that deal directly with external customers as for those that simply pass work on to other employees inside the business.

BizWORD

Quality circles *are groups of workers who meet to solve problems relating to quality.*

BizFACT

The Schaeffler Group is a leading worldwide automotive and industrial manufacturer. The foundation for their sustained success is through taking the lead in quality, technology and innovation. Their work in all areas is based on the objective of continuous improvement with the aim of achieving 'zero defects'. They have implemented measures to ensure defect prevention and minimisation of risk. Every employee in the company is aware of this commitment to quality and must think and act in accordance with this principle.

BizWORD

Continuous improvement *involves an ongoing commitment to achieving perfection.*



FIGURE 8.17 A robust quality management program is critical to the overall success of construction companies. Calibre Construction Group Pty Ltd is a small builder and developer based in NSW. They have achieved a competitive advantage through their guarantee of zero defects on handover of the project. They achieve this by programming and planning their works in consultation with the client and whole project team and by ensuring that only the best contractors are utilised.

SUMMARY

- Quality management is the strategy that a business uses to make sure that its product meets customer expectations. Three quality approaches are quality control, quality assurance and quality improvement.
- Quality control involves the use of inspections at various points in the production process to check for problems and defects. Performance is measured in relation to set standards or benchmarks.
- Quality assurance involves the use of a system where a business achieves set standards in production. This is a proactive approach to quality management that aims to prevent problems from occurring.
- Quality improvement focuses on two aspects: total quality management and continuous improvement.
- Total quality management (TQM) is an ongoing, business-wide commitment to excellence that is applied to every aspect of the business's operation.
- Continuous improvement is a process that involves an ongoing commitment to achieving perfection.

EXERCISE 8.4 REVISION

1. **Outline** the main features of quality management.
2. **Why** is quality control important for businesses?
3. **Describe** the ways a business can offer quality assurance to customers.
4. **Define** total quality management.
5. **Summarise** the three approaches that make up total quality management.
6. Read the following definitions. If a definition is false, **propose** a correct definition.
   (a) Quality control involves the use of inspections at various points in the production process.
   (b) Quality assurance involves the use of a system where a business achieves set standards in production.
   (c) Total quality management is a commitment to quality that is applied to the business's operations department.
   (d) Continuous improvement involves an ongoing commitment to use of inspections.
7. Ganesh is the production manager for IBX technology, a manufacturer of internet security software. Recently, the level of product defects has increased, although the production process has not changed.
   (a) **Propose** to Ganesh strategies that he should use to determine the cause(s) of the defects.
   (b) **Explain** to Ganesh the value of introducing a TQM approach.

8 The name 'The Reject Shop' suggests that it could not possibly sell quality products. Is this true? Search the company's website and see how many references to quality you can find. **Explain** how The Reject Shop ensures that it receives quality products from suppliers.

EXERCISE 8.4 EXTENSION

1 Find information online about Australian Standards. Use the **Standards Australia** weblink as a starting point. Assess the practical effects of such standards on industry.

2 **Investigate** W. Edwards Deming and his development of TQM. **Justify** whether you think he proposed anything extraordinary or he just made businesses more aware of their production methods.

on Resources

Weblink: The Reject Shop
Weblink: Standards Australia

8.4 Marketing

Marketing is vital to the existence of the business. Just because someone invents a new product or improves an existing one does not guarantee customers will buy it. Without some form of marketing, customers may not even be aware of a product's existence regardless of how 'record breaking', 'new and improved' or 'revolutionary' it may be. Statistics reveal that more than 70 per cent of new products launched on the market self-destruct in the first year of operation, mainly because of poor marketing. Businesses make few sales if they do not market their products successfully, eventually ending in failure (see the following Snapshot).

Case study: Investorist — importance of marketing

Jon Ellis, founder of Investorist, always knew he wanted to be an entrepreneur. The catalyst for him starting his own business came when he was in his 20s and his boss slammed his fist on the table and reminded him who paid his wage. This desire to not have an individual controlling his destiny and causing him stress is what led him to launch his first business, Extension, when he was 26 years old.

A decade later in 2013, Ellis used the money he raised from Extension to begin a second business, Investorist; a platform to connect off-the-plan property developers with agencies and advisors all over the world. The company has been achieving 30 per cent quarter-on-quarter revenue growth over the past 18 months and turned over $3 million in 2017. Much of this success can be attributed to its marketing.

In the beginning, Ellis' marketing approach consisted of employing a small group of sales people to sell his new software platform. After some time he discovered that potential leads weren't converting into sales. The company's approach to marketing was not very successful; while he generated some sales, it wasn't enough.

After a few months, Ellis scrapped the sales approach and instead opted for a marketing approach, which focuses on finding out what customers want and then satisfying that need. He undertook extensive market research to find out customers' needs. He feels that market research is especially crucial when entering into new markets. Ellis created industry white papers in an effort to educate his market about his business. The trackable marketing tool he developed has indicators so that Ellis is able to assess the success of his activities; e.g. number of clicks, shares, forwards and how much content is consumed prior to purchase. Each quarter, Ellis implements new objectives and his marketing budget changes based on those goals. This new approach resulted in more than 100 000 people connecting with the platform over three years.

SNAPSHOT QUESTIONS

1. **Compare** the sales and marketing approaches.
2. **Why** do you think adopting a sales approach is not a very effective approach to marketing?
3. **Outline** the benefits of Ellis' new approach to marketing.

SNAPSHOT



'The company's approach to marketing was not very successful …'

BizFACT

Research by marketing services company Salmat found that, while 51 per cent of small Australian businesses surveyed intended to boost their marketing investment, many lack the time and money to compete against larger companies when it comes to effective marketing. This is concerning, especially considering that failing to attract enough customers is a main cause of business failure, which could be avoided through effective marketing. Marketing strategies will help businesses better understand and meet customer expectations, as well as attract and engage potential customers.

At the same time, many products that would seem insignificant and unimportant have become best-selling 'essential' items as a result of a well-managed and professional marketing plan. Who would have ever thought that brown, sugary, fizzy water with addictive qualities would become the universal product it is today!

Marketing is a powerful business strategy available to all businesses. The HSC course investigates marketing in greater depth, so this chapter will provide an elementary understanding of the main concepts.

8.4.1 Marketing fundamentals

Marketing is not a new subject to you. Over the years you have probably been involved in some type of marketing activity. Consider the following examples:

- helping to organise a stall at a local fete
- setting up a raffle for a local sporting team
- persuading your parents to lend you some money to buy a new phone
- coordinating the publicity for the school musical.

Although all these activities are different, they have one thing in common: they involve a number of marketing activities. (see figure 8.18)



FIGURE 8.18 The four main marketing strategies are commonly referred to as the four Ps of the marketing mix. They include strategies regarding the product, price, promotion and place (distribution).

8.4.2 What is marketing?

Many definitions are used to describe **marketing**. The most commonly accepted definition comes from the American Marketing Association: 'Marketing is the process of planning and executing the conception, pricing, promotion and distribution of ideas, goods and services to create exchanges that satisfy individual and organisational objectives'.

A more simplified definition of marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers. At the heart of these activities is the most fundamental question all businesses should continually ask: 'What do customers want to buy — now and in the future?' This is the essence of marketing — finding out what the customers want then attempting to satisfy their needs.

Sometimes 'selling' and 'marketing' are used synonymously. Many people think that marketing is just a fancy name for selling; however, there is much more involved. Selling is merely getting rid of existing stock, whereas marketing takes a much broader view. Successful marketing involves bringing the buyer and seller together and making a sale. The current view of marketing is such that it does not even have to involve the selling of a product — for example, not-for-profit organisations may want to inform the public of the services they provide.

Some small business owners are excellent 'technicians' but dislike marketing and inadvertently turn away customers. Other small business owners are so convinced of the value of the good or service that they assume it will sell automatically. Unfortunately, this rarely occurs.

Many small business owners feel marketing is not for them. They happily place advertisements in local newspapers, display the name of the business on their cars and perhaps even advertise on a regional radio or television station. However, such advertising is just one part of marketing a good or service.

Small business owners often view marketing campaigns as something only large businesses do, and as too expensive, complicated or time consuming for themselves. What they do not often appreciate is that they can run a marketing campaign and that it can be simple and inexpensive.

All businesses, regardless of size, need to undertake some form of marketing, otherwise customers will not be informed about the business's products.

BizWORD

Marketing *is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.*

Case study: Polasports — marketing a new product line

Polasports is an Australian-owned business that manufactures sunglasses designed with the everyday sportsperson and outdoor enthusiast in mind. Its sunglasses provide a fusion of sports sensibilities with fashionable frames to create an exceptional and enduring product. Up until recently, Polasports was quite an unknown brand on a retail level. A company may offer the greatest product in the world, but unless consumers are aware of it, they may not make a single sale. Products do not 'sell themselves'. Without customers, a product — even one that is superior to its competitors — is useless. One of the most important roles of a business is to generate brand awareness for their products. To ensure their product gets the best visibility possible, they need to consider a wide variety of marketing strategies.

In 2017, Beau Ryan (former National Rugby League star) collaborated with Polasports as a brand ambassador to create his own sunglasses range. Celebrity endorsement is a powerful marketing tool, especially when the target audience align themselves with the ambassador chosen. This endorsement can open up a huge following and increase customer engagement. This is exactly what happened at Polasports. Getting Beau Ryan on board increased sales, as well as traffic to their website, significantly. The greatest advantage, however, was that the partnership grew their brand awareness. This, in turn, led to the company gaining new wholesale customers wanting to stock Polasports.

SNAPSHOT



'Without customers, a product … is useless.'

Polasports has used social media as its main advertising platform to promote its new product range. The company has found that social media advertising has been an extremely effective tool for growing its brand awareness. Not only does the company use social media, but Beau Ryan and his friends have also been posting about the new range. Because they all have such a large social media following, this has greatly assisted the business to grow its online presence and increased traffic to its website.

The company has also affiliated itself with two charities to market its business. Recent studies suggest that millennials (Polasports' target market) have driven the social responsibility movement and will spend more with brands that support causes. With the launch of the new range, Beau Ryan announced that $5 from every pair of sunglasses sold would go directly to his charity of choice, the Men of League Foundation, which is known for its focus on former players in the rugby league community who are doing it tough. This enabled Polasports to get a lot more influencers on board and talking about the brand, since the company was giving back to a charity that most people in league feel very passionately about. The company also donated $5000 to the Starlight Children's Foundation Australia. This charitable element has been a cornerstone of the brand and shows consumers that the company is ethical and trustworthy. Promoting these donations on social media generated goodwill by demonstrating to consumers that the business is dedicated to charitable causes.

After the launch of the new range, Beau Ryan promoted the sunglasses on the NRL *Footy Show*. This promotion, however, wasn't as successful as the company had hoped. While they did get a television plug, they didn't see a return on this, which could be due to the fact that the demographic that watches the show are a lot older and different to the target market.

On the other hand, their radio plug on Nova 969 during Fitzy and Wippa's show had a much greater impact. After the segment, the entire team posted Instagram stories about Polasports, which led to an increase in Polasports' social media followers, as well generating more publicity about the new glasses. This segment also led to even more publicity in *The Sun-Herald*.

SNAPSHOT QUESTIONS

1. **Recall** what is one of the most important roles of a business.
2. **How** did getting Beau Ryan as a brand ambassador benefit the company?
3. **Explain** the benefits of social media advertising.
4. **How** does supporting charities help promote a brand?
5. **Determine** why the publicity on radio was more effective than the publicity on television.

8.4.3 Role of marketing

Marketing has evolved over the past five decades, with new ideas and strategies emerging every year. Traditional marketing is a broad category that incorporates the wide array of advertising channels we see daily, e.g. print media, billboard, TV advertising and radio broadcasting.

Traditional marketing attempted to pull customers to a product, whatever the cost. While traditional channels are not necessarily outdated, they do not really consider the customer to whom they are selling. Contemporary marketing involves much more than placing an advertisement in the local media. It is a way of thinking. Contemporary marketing refers to those strategies that stress the importance of customer orientation. Everything the business does is directed towards putting the customer at the centre of its thinking. Businesses that adopt this approach base their marketing decisions and practices on the needs and wants of their customers (see figure 8.19). This is known as the marketing concept approach.

Businesses that adopt the marketing concept approach also focus on relationship marketing; i.e. developing long-term, cost-effective relationships with their customers. For these businesses, the customer relationship does not end with the sale; it begins there. Businesses using this approach will continuously strive to not simply meet but exceed customer expectations. This means that, at every level of the



FIGURE 8.19 Seven tips to becoming a marketing driven customer-oriented business

business, employees should work towards customer satisfaction by establishing positive relationships with customers. Research has found that businesses that utilise this contemporary marketing approach over the long run have seen an increase in sales and have become far more prosperous than those who use only traditional channels.

SUMMARY

- For a business to make a profit, it needs to create and market products that consumers will purchase.
- Marketing is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers.
- Successful marketing involves bringing the buyer and seller together and making a sale.
- Contemporary marketing refers to those strategies that stress the importance of customer orientation.
- Businesses that adopt a customer-oriented approach base their marketing decisions and practices on the needs and wants of their customers.
- Businesses should also focus on relationship marketing, i.e. developing long-term, cost-effective relationships with customers.

EXERCISE 8.5 REVISION

1. **Outline** the importance of marketing to a business.
2. **Why** do most new products fail shortly after they are launched?
3. **Identify** some types of marketing activities you have been involved in.
4. **Discuss** how the 'marketing' definition provided in this chapter differs from your previous understanding of the term.
5. **Distinguish** between selling and marketing.

6 **Recall** why all businesses, regardless of size, need to undertake some form of marketing.

7 **Why** should a business adopt a customer-oriented approach to marketing?

8 Refer to figure 8.19. **Identify** which of the 'seven tips' you think is the most important. **Justify** your answer and share it with other class members.

9 **Recall** the correct response to complete the following sentences.
(a) The main emphasis in marketing today is the _____ -oriented approach.
(b) This means the business wants to _____ customers' needs and wants rather than merely produce products.

EXERCISE 8.5 EXTENSION

1 **Construct** a presentation containing 10 dot points that reflect key features of your new understanding of marketing.

2 'Marketing is not the sole responsibility of the marketing manager, but all managers.' **Determine** the accuracy of this statement.

3 **Predict** what will happen to a business that neglects the importance of marketing.

8.4.4 Identification of the target market

Very few businesses can afford to market their products to all consumers or all businesses in Australia. At the same time, few businesses would want to because it is a very rare product that is suitable to all consumers. Until the end of the 1950s, Coca-Cola was such a product. But today Coca-Cola offers consumers a range of carbonated soft drinks based on its original cola formula including Coca-Cola Zero, Diet Coke and Coca-Cola with Stevia, as well as non-cola drinks such as Pump still water, POWERADE and Goulburn Valley juices. Most businesses must select specific groups of customers on which to concentrate their marketing efforts: their **target markets**. A target market is a group of customers with similar characteristics who presently, or who may in the future, purchase the product.

Three broad approaches can be adopted when selecting a target market: the mass marketing approach, the market segmentation approach or the niche market approach (see figure 8.20).

BizWORD

A **target market** *is a group of customers with similar characteristics who presently, or who may in the future, purchase the product.*

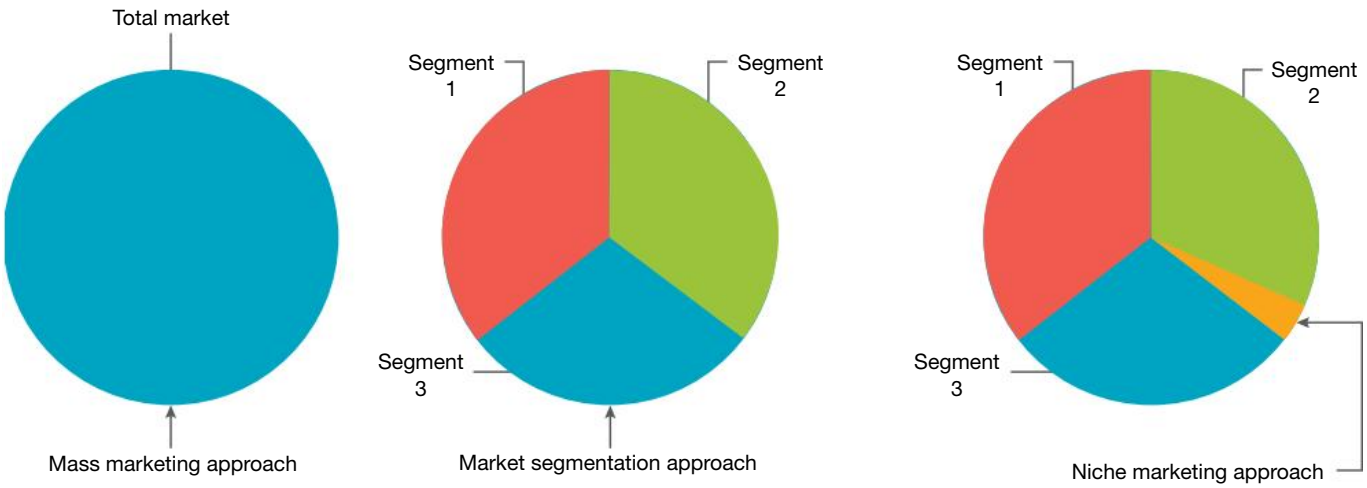


FIGURE 8.20 Selecting a market to be the target market

Mass marketing approach

Fifty years ago, marketers commonly spoke about 'mass market'. In other words, there was a large demand for a standard product. In a **mass market**, the seller mass-produces, mass-distributes and mass-promotes one product to all buyers. The Model T Ford, for example, was the first motor vehicle to be produced and sold to the mass market.

BizWORD

In **mass markets** *the seller mass-produces, mass-distributes and mass-promotes one product to all buyers.*



FIGURE 8.21 In America, mass market retailers are the most important sector in retail, accounting for the greatest percentage of purchases made by American consumers. Australia and many other nations rely on smaller stores that sell specialised items. The American culture of convenience, however, has popularised these one-stop-shop stores with low prices and lots of options. The best known and largest example of a mass market retailer is Walmart.

A mass marketing approach seeks a large range of customers. The business develops a single marketing mix and directs it at the entire market for the product. This means there is one type of product with little or no variation, one promotional program aimed at everyone, one price, and one distribution system used to reach all customers.

Few products today, apart from basic food items, water, gas and electricity, are marketed to the mass market. As a result of greater choice, higher personal incomes and customers seeking more individualised products, the mass market has been replaced by segmented or niche markets.

Market segmentation approach

Few businesses can sell their products to the entire market — the market is just too big. Therefore, a business will divide the market into distinct segments. A business that is marketing motor vehicles, for example, would not direct its marketing efforts towards every person in the total vehicle market. Some people might want only a sports car; others might want a four-wheel drive. The business would thus direct its efforts towards a particular *segment* of the total market for motor vehicles.

Market segmentation occurs when the total market is subdivided into groups of people who share one or more characteristics based on four elements or dimensions: demographic, geographic, psychographic and behavioural, as shown in table 8.3.

BizWORD

Market segmentation *occurs when the total market is subdivided into groups of people who share one or more common characteristic.*

TABLE 8.3 Common elements or dimensions for segmenting customer markets

Demographic — population characteristics	Geographic — where people live	Psychographic — personality characteristics	Behavioural — loyalty to a product
• Age • Gender • Education • Family size • Income • Occupation • Social class • Religion • Ethnicity	• Urban • Suburban • Rural • Regional • City size • Climate • Landforms	• Lifestyle • Personality • Motives • Socioeconomic group • Consumer opinions • Interests	• Purchase occasion • Benefits sought • Loyalty • Use rate • Price sensitivity

A business segments its market so it can better direct its marketing strategies to specific groups of customers, rather than the mass market. The ultimate aim of market segmentation is to increase sales and profits by better understanding and responding to the desires of the target customers.

Once the market has been segmented, the business selects one of these segments to become the target market (see figure 8.22). For example, a rural supplies

business would normally aim its promotion strategies at male, 25 to 60-year-old, rural-based farmers with middle to high incomes. An exclusive women's fashion boutique in central Sydney would have a target market of customers who are female, 25 to 45-year-old, city-based professionals with high incomes.

This approach allows the business to better satisfy the wants and needs of a targeted group, because the business can:

- use its marketing resources more efficiently
- better understand the **consumer buying behaviour** of the target market
- collect data more effectively and make comparisons within the target market over time
- refine marketing strategies used to influence consumer choice.

BizWORD

Consumer buying behaviour *refers to the decisions and actions of consumers when they purchase goods and services for personal household use.*

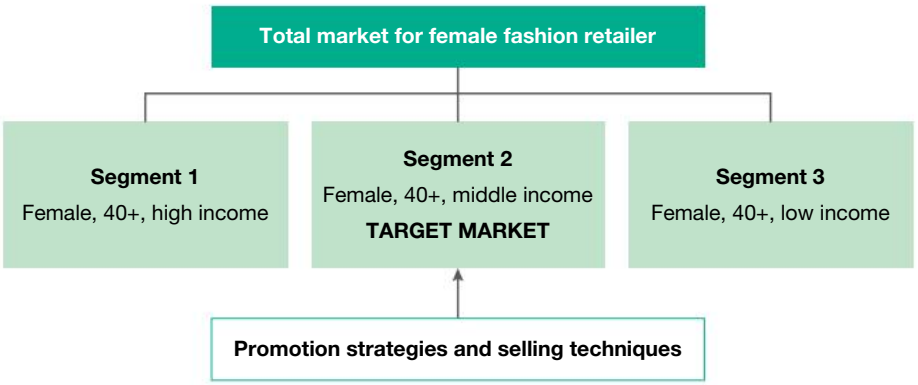


FIGURE 8.22 Selecting a market segment to be the target market is important. In this example, the fashion retailer makes clothes for women over 40 years of age. The clothes are of a reasonable quality but would not be classed as 'designer' clothes. In this business, female middle-income earners are the main target market.

on Resources

Weblink: Smiggle

BizWORD

The **primary target market** *is the market segment at which most of the marketing resources are directed.*

A **secondary target market** *is usually a smaller and less important market segment.*

Sometimes, a business may be able to identify both a **primary** and **secondary target market**. For example, Lush, a cosmetics retailer, primarily targets women of higher socioeconomic class, specifically middle to upper class, aged 18–45 years. They also have a secondary target market of men, as well as children. The ability to choose the correct target market is an important marketing function because it will influence the entire marketing plan (see the following Snapshot). Use the **Smiggle** weblink in the Resources tab to investigate their approach to their target markets.

SNAPSHOT



'A positive experience produces return business.'

Beau's Floral Studio — target market

Beau Wilkes is owner–operator of a retail florist store called Beau's Floral Studio. The business provides fresh and dried flowers, and associated product lines for all occasions. The business markets to a wide cross-section of the population within the surrounding suburbs, but particularly to females aged 15–65 years and males aged 15–25 years.

Size of target market

Potential

Beau's potential target market consists of approximately 74 000 people who live in the surrounding suburbs.

Actual

Beau's primary target market consists of females aged 35–65 years who decorate their homes with floral displays.

The two secondary markets consist of:

- females aged 15–65 years who purchase flowers for special occasions
- males aged 15–25 years who purchase flowers for their partners.

These target markets are important because they represent repeat customers who are essential for the business's long-term survival. The primary target market

consists of approximately 21 000 people. It can be further subdivided according to the benefits sought by the customer, as shown by the following table.

Subdivision of target market

Benefits sought by customer	Customer characteristics
Comfort (sickness and sympathy)	Male and female, aged 15 years and above
Beauty (floral displays)	Predominantly female, aged 35–65 years
Happiness (weddings and parties)	Predominantly female, aged 15–50 years
Affection	Predominantly male, aged 15–45 years

Target market dimensions

Geographic

Beau's Floral Studio targets the residents of the local area. Sales to customers from outside the surrounding suburbs are only occasional, not regular, and do not constitute an important segment for the purposes of her marketing plan.

Demographic

Customer research data collected over the past 12 months reveal that 67 per cent of customers were female and 33 per cent were male. Females aged 35–65 years were the most common type of customer, making up 83 per cent of the total female customer base. Males aged 15–25 years made up 78 per cent of the total male customer base.

Purchase decision maker

Predominantly, the purchase of fresh and dried flower arrangements is considered to be a gift purchase, for either the individual or another person. The experience of a floral purchase should be considered within this context. A positive experience produces return business.

Income level

Beau's Floral Studio caters for the middle to high income groups. These groups consist of individuals and households with high levels of disposable income. They do not perceive the buying of flowers as an infrequent luxury expenditure, but as a regular (weekly or fortnightly) purchase.

SNAPSHOT QUESTIONS

1. **Identify** the primary and secondary target markets for Beau's Floral Studio.
2. **Recall** what four variables Beau Wilkes uses to segment the target markets.
3. **Explain** the importance of these target markets to Beau's Floral Studio.
4. **Analyse** how segmenting the total market helps Beau Wilkes achieve her long-term business objectives.

Niche markets

An extension of the market segmentation approach is that of the **niche market**, which is a narrowly selected target market segment. In a sense, it is a segment within a segment, or a 'micro market' (see figure 8.23). For example, in any newsagency, you will see row upon row of magazines each appealing to a specific niche market — male, female, young, old, high-income, low-income, urban, rural, outdoor lifestyle, indoor lifestyle and so on.

BizWORD

A **niche market** *is a narrowly selected target market segment.*



FIGURE 8.23 Mick and Simone McGrath are the owners of Moregolf, a wholesale business that sells golf products to retailers. While they started off selling a range of hardware, such as golf bags and clubs, they found they could not compete with larger golf equipment outlets. They therefore decided to focus on specialised or niche products instead. Moregolf now wholesales products such as Golf Pride and Lamkin grips, golf club shafts and repair gear. They also offer repairs and sell accessories. The business is now at a stage where it is starting to see profit and is becoming better known in the industry.

SUMMARY

- A target market refers to the group of customers to which a business intends to sell its product.
- Sometimes a business may be able to identify both a primary and a secondary target market.
- Three broad approaches can be adopted when selecting a target market: the mass marketing approach, the market segmentation approach or the niche market approach.
- A mass marketing approach seeks a large range of customers.
- A business segments its market so it can better direct its marketing strategies to specific groups of customers.
- Market segmentation occurs when the total market is subdivided into groups of people who share one or more common characteristic.
- A niche market is a narrowly selected target market segment.

EXERCISE 8.6 REVISION

1 **Distinguish** between mass, segmented and niche markets.
2 **Outline** the purpose of market segmentation.
3 **Recall** the different ways a market may be segmented.
4 **Why** is market segmentation the most common marketing approach used by businesses today?
5 **How** are market segmentation and target market linked?
6 Use an 'M', 'S' or 'N' to **determine** whether the following products are sold in a mass market, segmented market or niche market.
   (a) Electricity
   (b) Ferrari cars
   (c) *Australian Financial Review*
   (d) Avon cosmetics
   (e) Fruit and vegetables
7 **Determine** who is most likely to be the target market for each of the following small businesses. (You may think of more than one market for some businesses.)
   (a) Convenience store
   (b) Mechanic
   (c) Accountant
   (d) Nursing home
   (e) Childcare centre

EXERCISE 8.6 EXTENSION

1 'Any business that neglects the role of marketing will almost certainly experience low levels of sales and reduced profit levels.' **Evaluate** the accuracy of this statement.
2 In small groups, conduct a survey of 30 people to **investigate** what type of movies they watch at the cinema. Using a database, group the respondents by age and sex. Present your results in the form of graphs and charts.
3 In small groups, **create** a customer survey form for obtaining information on a business's level of service, product range, business facilities and suggestions for improvement. **Compare** each group's survey.

8.4.5 Marketing mix

BizWORD

Marketing strategies *are actions undertaken to achieve the business's marketing goals.*

Once the business owner has established the marketing goals (a statement of what the business expects to achieve through the marketing activities) and selected a target market, the next step of the marketing plan is to develop marketing strategies to achieve the goals. **Marketing strategies** are actions undertaken to achieve the business's marketing goals through the marketing mix.

One of the most useful ways of understanding how to develop a marketing strategy is to examine each of the elements of the marketing mix. The **marketing mix** refers to the combination of the four Ps — product, price, promotion and place (distribution). The business has control over these elements and uses them to reach its target market. These four Ps of the marketing mix are considered the basic cornerstone of marketing. However, as the service sector within the economy has grown, three more Ps have been added that apply especially to the service industry. These three extra Ps — people, processes and physical evidence — now form the extended marketing mix (see figure 8.24).

BizWORD

Marketing mix *refers to the combination of the four elements of marketing, the four Ps — product, price, promotion and place — that make up the marketing strategy.*

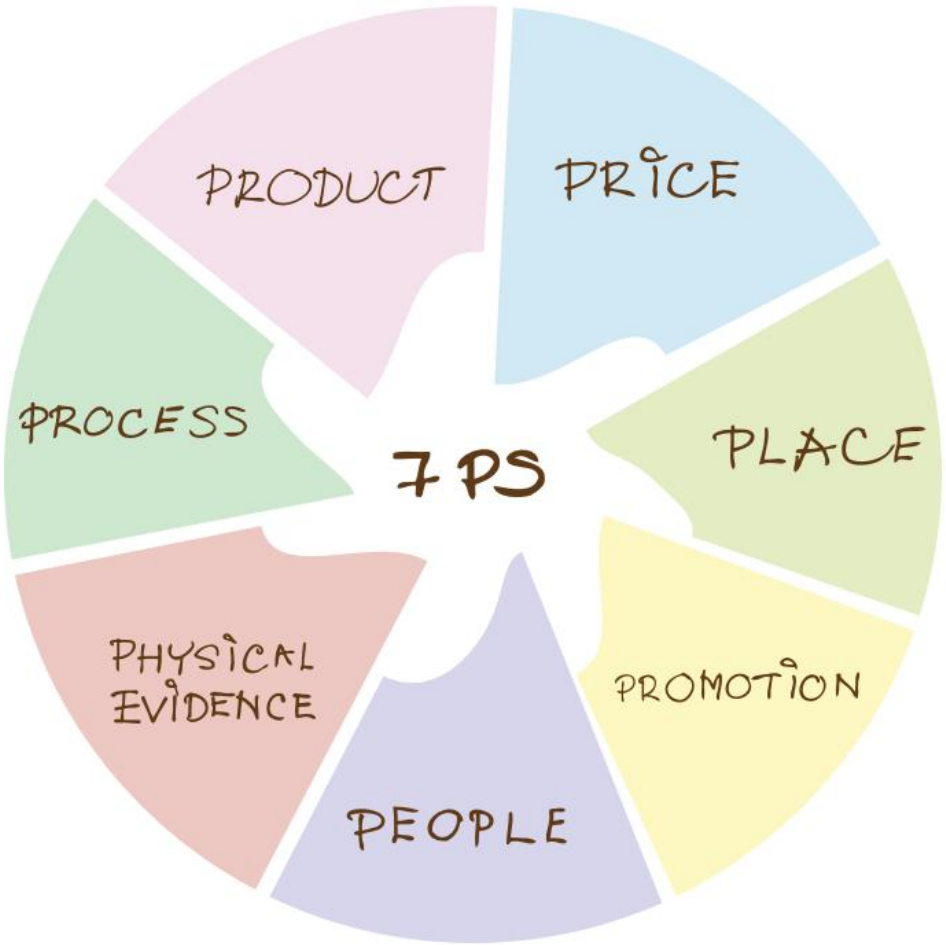


FIGURE 8.24 In recent years, it has become more common to add three new elements to the traditional marketing mix, making a combined 7 Ps. This is known as the extended marketing mix.

Once the four Ps have been established, the business must then determine the emphasis it will place on each of the variables. This will largely be determined by where the product is positioned or its stage in the **product life cycle**. For example, a product that is being marketed with an image of exclusivity and prestige will require a marketing mix totally different from a no-frills, generic item. A different marketing mix will also be required for a product in its introductory stage than when it reaches the decline stage.

BizWORD

The **product life cycle** *describes the life of a product over four stages: introduction, growth, maturity and decline.*

Product

This element of the marketing mix involves much more than just deciding which product (goods or service) to market. The business owner needs to determine the product's:

- quality
- design
- name
- warranty and guarantee.
- packaging
- labelling
- exclusive features

The product is a combination of all these variables. Customers will buy products that not only satisfy their needs but also provide intangible benefits such as a feeling of security, prestige, satisfaction or influence.



FIGURE 8.25 Tip Top recently redesigned their packaging and branding. The objective of the new look was to modernise the image and create packaging which stands out, while also maintaining quality and trust for the iconic brand. They changed the colours to richer tones, modernised the typography, maximised opportunity for brand visibility and added 'established in 1958' to reaffirm Tip Top's heritage and experience. Falling wheat, grains and fruit are included in the relevant bread packs in an effort to reinforce food cues and add appetite appeal and health credibility.
Source: Tip Top — a division of George Western Foods

BizWORD

Packaging *involves the development of a container and the graphic design for a product.*

Product packaging

The **packaging** of a product is sometimes as important as the product itself to assist sales. Well-designed packaging will give a positive impression of the product and encourage first-time customers to purchase. Tasteful packaging can create an image of luxury, sensuality and exclusiveness, helping to promote the product. In addition, packaging helps preserve, inform, protect and promote the product.



FIGURE 8.26 It takes 2.6 seconds for a consumer to choose one product instead of another, so the packaging has to be right. A design student from NSW won the Southern Cross Packaging Design Awards in 2015, conducted by the Packaging Council of Australia. Each part of her packaging can be used to construct a ramp, a racetrack and a garage for the small wooden cars inside.
Source: Packaging Council of Australia

With increasing community awareness of environmental pollution, businesses must also be sensitive to the problems caused by throw-away packaging. Approximately half of all household garbage consists of discarded packaging.

Product branding

An important part of the product development is the **brand** and associated **brand logo**. Combined, these can be a powerful marketing tool. For example, the three-pointed star of the Mercedes-Benz and Coca-Cola's distinctive narrow-waisted bottle are famous brand names and symbols. Some businesses encourage the instant recognition of their brand symbol rather than their brand name. Perhaps the most famous example of this technique is the 'golden arches' symbol used by McDonald's. In some advertisements the brand name does not appear at all, only the brand symbol. This is a clever and subtle method used to reinforce the meaning of the symbol and associate it with a brand name.

BizWORD

*A **brand** is a name, term, symbol or design that identifies a specific product and distinguishes it from its competitors.*

*A **brand logo** is a graphic representation that identifies a business or product.*

BizFACT

A new study of teenagers commissioned by Google revealed what brands teens regard as cool and which ones they regard as daggy. The survey, "It's Lit: A Guide To What Teens Think Is Cool" involved 1100 American teens. According to the study, the top 10 coolest brands (in order) were YouTube, Netflix, Google, Xbox, Oreo, GoPro, Playstation, Doritos, Nike and Chrome.

Price

Many business owners have difficulty selecting the 'correct' price for their product. A price set too high could mean lost sales, unless superior customer service is offered. A price set too low may give customers the impression of a 'cheap and nasty' product. Therefore, correct pricing is important. Business owners normally choose one of three methods for calculating price.

1. *Cost-based:* a pricing method derived from calculating the total cost of producing or purchasing a product and then adding a mark-up for profit (see figure 8.27).
2. *Market-based:* a method of setting prices according to the interaction between the levels of supply and demand — whatever the market is prepared to pay.
3. *Competition-based:* choosing a price that is either below, equal to or above that of the competitors.



FIGURE 8.27 Cost-based pricing is commonly used by large retail stores. The cost price is increased by a fixed percentage to arrive at the selling price. Assume a sporting goods store has a mark-up of 100 per cent. A soccer ball is bought for $40 and, with a 100 per cent mark up, will have a selling price of $80.

Promotion

To sell more of its products, a business has to change customers' behaviour through information or persuasion. This is achieved through promotion. The role of **promotion** is to inform, persuade and remind consumers about a business's products, with the aim of:

- attracting new customers by raising awareness of a particular product
- increasing brand loyalty by reinforcing the image of the product
- encouraging existing customers to purchase more of the product.

BizWORD

***Promotion** refers to the methods used by a business to inform, persuade and remind customers about its products.*

Many people confuse promotion with advertising because of its visibility and frequency. However, advertising is just one of the four elements of the promotion mix. The main forms of promotion are as follows:

1. *Personal selling and relationship marketing:* personal selling involves the activities of a sales representative directed to a customer in an attempt to make a sale. Relationship marketing refers to the development of long-term, cost-effective and strong relationships with individual customers.
2. *Sales promotion:* refers to activities or materials used by the business to attract interest and support for the good or service. Examples include free samples, coupons and point-of-purchase displays.
3. *Publicity and public relations:* Publicity refers to any free news story about a business's products. Public relations are those activities aimed at creating and maintaining favourable relations between a business and its customers.
4. *Advertising:* print or electronic mass media are used to communicate a message about the product. Advertising is used to attract potential customers, create a demand for the product and communicate essential information.

Changes in technology, especially advances in information and communication technology (ICT), are having a significant impact on how businesses promote their products. The internet, for example, has become an effective advertising tool used by businesses to deliver specific messages to its target market. Internet newsgroups, ezines, chat rooms, social networking websites and online publications can all be used in an advertising campaign. The internet has also provided opportunities for many small businesses to undertake more of their own promotional activities. Facebook, Twitter, LinkedIn, YouTube, blogs, podcasts and online communities are all examples of social media channels, and have been behind the recent revolution in social media advertising (SMA). Businesses are becoming increasingly aware that SMA can have positive results, especially when used in combination with traditional advertising methods (see figure 8.28). The main advantages of SMA are that it is:

- inexpensive in comparison to traditional marketing methods
- easy to use and monitor
- an effective method of gaining exposure.

BizFACT

Digital marketing is one of the fastest-growing marketing channels. Despite this, 41 per cent of SMEs have never tried any form of digital marketing. This is surprising considering that this is one of the most cost-effective mediums that small businesses could benefit from, due to their lower marketing budget.



FIGURE 8.28 The Meduri family, owners of La Tavernetta Osteria which is located in the Leichhardt Italian forum, have attracted a great following using social media advertising. They are very active on social media as they find it a very effective way of engaging with their clientele. They use social media to showcase their delicious authentic food, educate users on modern Italian cuisine and to promote theme nights, specials and giveaways. The family also use social channels to promote community events which they help organise in the forum.
Source: Victoria Mecluri

Place

The fourth 'P' of the marketing mix is '**place**' or **distribution**. This refers to activities that make the products available to customers when and where they want to purchase them. A **distribution channel** is a way of getting the product to the customer. This process usually involves a number of intermediaries or 'go betweens', such as the wholesaler or retailer. Apart from the retailer, the other intermediaries are often invisible; that is, the customer knows little about their role and operation. There are three common traditional channels of distribution:

1. *Producer to customer.* This is the simplest channel and involves no intermediaries. Virtually all services, from tax advice to car repairs, use this method.
2. *Producer to retailer to customer.* A retailer is an intermediary who buys from the producer and resells to customers. This channel is often used for bulky or perishable products such as furniture or fruit.
3. *Producer to wholesaler to retailer to customer.* This is the most common method used for the distribution of consumer goods. A wholesaler is an intermediary who buys in bulk from a producer, then sells in smaller quantities to retailers. Producers will use the services of a wholesaler when a large number of retailers sell the product and the producer finds it difficult to deal with them all.

Non-store retailing — that is, retailing activity conducted away from the traditional store — is gaining popularity. Two of the most rapidly developing methods are:

- e-commerce, which refers to the buying and selling of goods and services via the internet
- mobile commerce (m-commerce), which refers to the buying and selling of goods and services through wireless handheld devices, such as mobile phones and tablets.

BizWORD

Place *or* **distribution** *are activities that make the products available to customers when and where they want to purchase them.*

Distribution channels *are ways of getting the product to the customer.*

BizFACT

The Iconic has established a competitive advantage in relation to their distribution. Their suppliers list their products on The Iconic's site and the stock is sent directly to customers rather than to their distribution centre, cutting delivery times and distribution costs. The Iconic is able to offer customers three-hour delivery in major cities and same-day delivery to 75 per cent of Australia.

Case study: Beau's Floral studio — the marketing mix

Product range — product mix

Beau's Floral Studio presently has a wide product mix, offering a diverse range of fresh and dried exotic and native flowers. Complementary product lines include teddy bears, balloons, porcelain ornaments, friendship gifts, plant holders, floral arrangement materials and instructional books.

Beau intends to expand the product mix by introducing a range of aromatic candles, fragrant oils and oil burners. This expansion will allow the business to diversify its existing products and appeal to new segments in the market. At the core of the product range, however, is the belief that Beau's Floral Studio will stock only products of the highest quality. This approach protects the customer base and strengthens the business's image.

Branding

Given that flowers cannot be identified as being sourced from a specific wholesale supplier, Beau will implement strategies to identify purchases from the Floral Studio. These strategies include:

- Introducing distinctively coloured and environmentally friendly gift wrapping paper and packaging. The name of the business, with its logo, telephone and facsimile numbers, and the address of its website will be prominently displayed.
- providing a complementary satchel of Euro Fleur (a special food for cut flowers) with every purchase of fresh flowers. The satchel will also carry the name and all contact details of the business.
- placing a distinctively coloured and designed sticker on all items sold
- designing a new and distinctive business logo

SNAPSHOT



'Setting prices too high will result in customers being lost to the competitors.'

Positioning and image

Beau's Floral Studio will continue to develop a high-quality image for the business. All other elements of the marketing mix will be used to shape and maintain this image. The maintenance of this product positioning is important if the business wishes to exploit its differentiation. Successful positioning of the product will allow for increased profit margins without loss of customers.

Beau's Floral Studio will not attempt to compete directly with the other three florist businesses within the shopping precinct. It will differentiate itself in terms of its quality and 'exclusive' image.

Pricing

Beau's Floral Studio is presently a price follower, being the most recent entrant into the flower market within the area. Setting prices too high will result in customers being lost to the competitors. Prices that are too low will damage the image of the business and give the impression that the quality of the product is inferior.

As a result of the strategies that make up this marketing plan, Beau's floral Studio will be able to raise its prices and thereby increase its profit margin by an average of 35 per cent over the next 18 months. These price rises are not expected to lead to a significant loss of customers, given the increased product range, product differentiation, accurate positioning and the high quality of the products and service.

Promotion

Presently, Beau's Floral Studio relies on the following five methods of promotion:

1. local newspaper advertisements:
2. word-of-mouth recommendation
3. packaging that displays the business name and logo
4. a *Yellow Pages* advertisement
5. eye-catching window displays.

Two new promotional stratergies are planned within the next six months:

1. the use of the website to promote contemporary floral arrangements and the new product lines
2. a personalised direct mail campaign to existing account holders, with exclusive offers for special occasions such as Mother's Day, Easter, Christmas and Valentine's Day.

Expenditure on all forms of promotion will be increased by 15 per cent over the next 12 months and by a further 10 per cent over the following two years. This increased promotional expenditure is required during the establishment phase of the business.



A Yellow Pages advertisement is also an important promotional tool.

SNAPSHOT QUESTIONS

1. **Why** doesn't Beau just sell flowers?
2. **Summarise** the branding strategies Beau's Floral Studio has implemented.
3. **Describe** the positioning of Beau's Floral Studio.
4. **Identify** the pricing methods used by Beau's Floral Studio.
5. **Predict** the effect of the business's new promotional strategies.

SUMMARY

- Marketing strategies are actions undertaken to achieve the business's marketing goals through the marketing mix.
- The main marketing strategies are commonly referred to as the marketing mix or the four Ps — product, price, promotion and place (distribution).
- As the service sector within the economy has grown, three more Ps have been added. These three extra Ps — people, processes and physical evidence — now form the extended marketing mix.
- Products are goods or services, and consist of both tangible and intangible features.
- Packaging helps preserve, inform, protect and promote the product.
- Product branding is the brand and associated brand logo.
- A business must select the most appropriate pricing method suitable to its product and market conditions. Business can choose one of three methods for calculating price: cost-based, market-based and competition-based pricing.
- Promotion refers to the methods used by a business to inform, persuade and remind customers about its products. Some of the main forms of promotion include personal selling and relationship marketing, sales promotion, publicity, public relations and advertising.
- Distribution channels (place) are a way of getting the product to the customer.
- The traditional distribution channels are: producer to retailer, producer to retailer to consumer, and producer to wholesaler to retailer to consumer. Two new distribution channels are e-commerce and m-commerce.

EXERCISE 8.7 REVISION

1 **Define** the marketing mix.

2 **Identify** the marketing strategies that form part of the extended marketing mix.

3 **Identify** four intangible benefits that products may provide.

4 **Clarify** the importance of customer service.

5 Think of a product you recently purchased. **Identify** the intangible benefits you gained from the product.

6 **Why** do marketers prefer to use the term 'total product concept' rather than simply 'product'?

7 **Predict** what may happen to the level of sales if a product's packaging does not match its position.

8 **Explain** the relationship between 'brand' and 'brand logo'.

9 **Why** do businesses spend so much money attempting to establish a brand name?

10 **Evaluate** each of the following brand names. Indicate the strong points of each name.
(a) Nokia mobile phones
(b) Apple computers
(c) LG electronic products

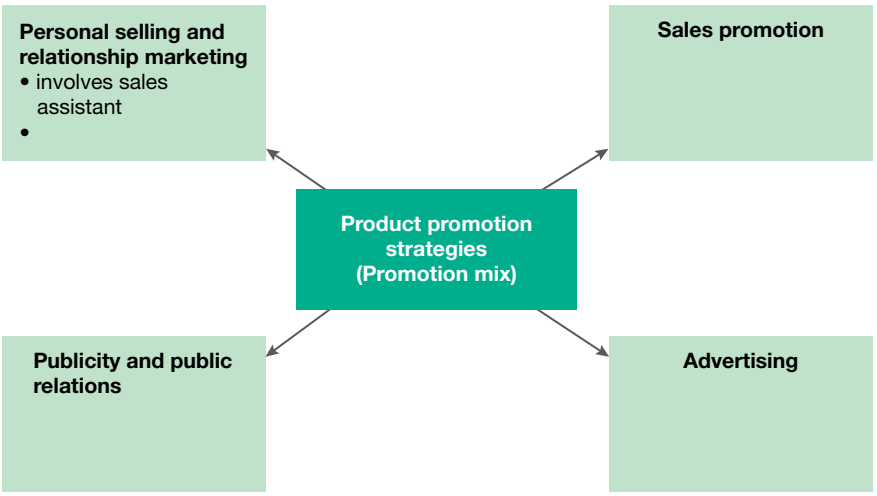
11 **Summarise** the three main pricing methods.

12 As the manager of a shoe store, you have just received a delivery of new boots that cost you $50 a pair. Your usual mark-up is 60 per cent. However, you find out that yours is the only store in town that will be stocking this fashionable product. **Calculate** what price you will set for the boots. **Explain** your decision.

13 **Outline** the role of promotion.

14 **Recall** what promotion aims to achieve.

15 **Construct** a concept map summarising the four main forms of promotion. The first one has been started for you.



16 **Recommend** a distribution channel for the sale of:
(a) a daily newspaper
(b) a washing machine
(c) an imported motor vehicle.

EXERCISE 8.7 EXTENSION

1 When deciding on a brand name and brand logo, **investigate** some of the considerations that a marketer must take into account.

2 **Determine** how a business sets its price when it wants to achieve the objective of profit maximisation.

3 'Some people would argue that "marketing ethics" is a contradiction in terms.' **Evaluate** this statement.

4 Referring to a business you are familiar with, **analyse** and **evaluate** the promotion methods used for one of its goods or services.

5 Using magazines, newspapers and the internet, collect and paste into your notes five advertisements for small businesses.
(a) **Identify** the good or service the business is selling.
(b) **State** what unique features of the business are publicised.
(c) **Determine** whether you think the advertisement fulfils its function of reminding, informing and persuading existing and potential customers. Give reasons for your answer.
(d) Rank the advertisements in the order that they appeal to you, from the most appealing to the least appealing. **Explain** how you determined the ranking order.
(e) **Compare** your ranking with other members of the class and discuss similarities and differences.

8.5 Finance

A thorough understanding of accounting and finance is essential for business managers. Accounting is a management tool that is concerned with providing information on the financial affairs of a business, while finance is concerned with where the business sources its funding.

Management of business finance is a crucial aspect of business success. Management of finance starts with sourcing — where will the funding come from?

Once a business has secured funding, it then needs to ensure that it is applied appropriately. All financial managers would be aware of the need to manage the cash flow of the business. Cash flow is sometimes described as the 'lifeblood' of business. The management of cash flow involves anticipating cash expenditure and ensuring that enough of the income earned comes in the form of cash. A further challenge is to ensure that enough money is saved in the event of unexpected challenges. Some money for **contingencies** needs to be put aside. Contingencies are unanticipated events that can lead to financial difficulty. For a business to be well managed, it needs to have saved money for such events because they can place the business under unexpected financial pressure.

In short, business leaders and managers need to have a good understanding of accounting and finance, and need to draw on this knowledge and skill when managing all aspects of the business.

The HSC course investigates finance in greater depth, so this chapter will provide an elementary understanding of the main concepts.

BizWORD

Contingencies *are unanticipated events that can lead to financial difficulty. For a business to be well managed, it needs to have saved money for such events.*

8.5.1 Accounting — introduction and scope

Accounting is a managerial and administrative tool that involves the recording of financial transactions, so that a clear summary of what has happened to the money coming in and going out can be traced over time. Every financial transaction, from the ordering of stock to the sale of an old stock item, is recorded. These records (which include delivery dockets, sales receipts, invoices, cash register records and e-payment transactions, to name a few) are entered into accounts that may be either computerised or manual (in the form of books). The information in these accounts is then summarised into financial reports and statements that provide very valuable information about the trading period (see table 8.4). The statements are set out in a standard format so that they are easy to read and understand. A well-trained manager can use these statements to get a very accurate picture of the financial status of the business.

BizWORD

Accounting *is a managerial and administrative tool for recording financial transactions, so that a summary of what has happened to business money can be traced.*



FIGURE 8.29 Accounting is more than 'crunching the numbers'. Money is the lifeblood of all businesses. The rate at which it flows into or out of the business determines whether the business is expanding and successful. There is only one sure way to measure the flow of money — develop a system of financial records. No business, no matter how small, can survive without a sound accounting system.

The three main accounting/financial reports or statements are shown in table 8.4.

TABLE 8.4 The main accounting financial reports or statements

Name of statement/report	Description of the statement/report
• *Cash flow statements*	• Indicate the movement of cash receipts and cash payments resulting from transactions over a period of time.
• *Income statements* (also called statement of financial performance, revenue statement or profit and loss (P&L) statement)	• Show the revenue earned and expenses incurred over the accounting period with the resultant profit or loss
• *Balance sheets* (also called statement of financial position)	• Represent a business's assets and liabilities at a particular point in time and represent the net worth of the business

BizFACT

The main purpose of financial statements is to summarise information in a way that is useful for interested parties. Together the reports show accurately how the business is placed financially.

A business is an economic entity — it trades within society and has responsibility both to its internal and external stakeholders (i.e. the members of society who are directly and indirectly affected by the affairs of the business). Accounting provides information that is valuable to managers. It also provides information to employees, owners and shareholders (if it is a company), suppliers, lenders, customers, government (including regulators), competitors and the general public.

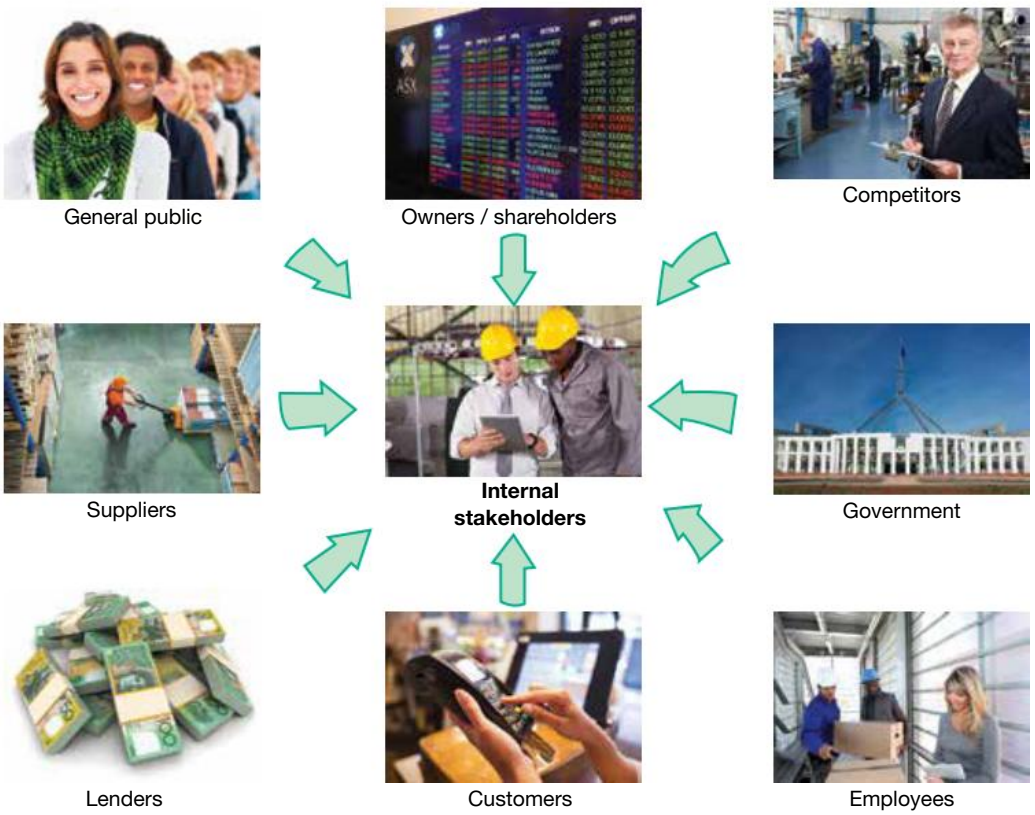


FIGURE 8.30 The stakeholders interested in the accounting information given by business

Accounting is useful, as it provides information in statements about each of the following as it relates to the business:

- financial status/position
- cash status/position
- financing or funding information

- cash flows
- profitability and return on investment
- trends in earnings, borrowings, sales and so on that together indicate the risks the business faces.

The main purpose of accounting then is to provide information that is useful and accurate, and presented in a clear and concise form. This information will encourage:

- judicious and prudent financial decision making
- planning that is purposeful
- confidence in the business's management
- **accountability**, or stewardship.

8.5.2 Finance — introduction and scope

Finance refers to how a business funds its activities — for instance, where it gets the money to trade, why it chooses to use certain lenders — as well as the costs, risks, terms and benefits of different types of borrowings. Financial knowledge requires an understanding of a range of financial instruments. Businesses, even very small ones, generally borrow money at some time — usually when they first set up.

It is vital for a business to be able to manage its borrowing and to use appropriate types of borrowing — namely types that match its earning stream and capital/asset structure. Borrowing represents a useful source of finance — but it is one that comes at a price. It is management of the cost and risk of finance that is the key to successful financial management.

Cost management is crucial because businesses tend to try to maximise profits. In today's highly competitive markets, in Australia and globally, a business succeeds when it can minimise cost (while maintaining quality, reliability, high service levels and so on). Risk management is crucial because businesses can be uncertain regarding their chances of making financial losses. Astute financial management is therefore considered indispensable to business.

An understanding of both accounting and finance is absolutely necessary if business managers and owners are to make *informed* decisions. The ability to interpret financial information helps with the leadership task — which includes planning for future activities; choosing between alternative courses of action when presented with business problems; organising the resources required to produce a product or service; and then effectively researching and marketing it; and controlling and monitoring spending in all aspects of the business.

BizWORD

Accountability *occurs when a business acts in the best and highest interests of its owners. Full and complete 'disclosure', which means to be open and not hide the truth, ensures that the books of account are kept accurately and that the information reflected in them, and which is summarised in reports, is based on the true and actual transactions. Another term for accountability is stewardship.*

Finance *refers to how a business funds its activities — for instance, where it gets the money to trade, why it chooses to use certain lenders — as well as the costs, risks and benefits of different types of borrowings.*

SUMMARY

- Businesses need to be led by managers with a good understanding of accounting and financial management.
- Accounting is a financial management tool that is involved with the recording and analysis of all the business's financial transactions.
- The financial transactions are summarised into financial statements. The main ones are:
  - cash flow statement
  - income statement
  - balance sheet.
- Finance details how a business funds its activities.
- It is vital for a business to be able to manage its borrowings and to use appropriate types of borrowings.

EXERCISE 8.8 REVISION

1 **Distinguish** between accounting and finance.
2 **Recall** what the management of cash flow involves.
3 **Clarify** why some money for contingencies needs to be put aside.
4 **State** what a credit rating assesses.
5 **Explain** why a business would want to have a good credit rating.
6 **Why** is accounting necessary for business?
7 **Identify** the main accounting reports and statements.
8 **Discuss** the role of the internal and external stakeholders who would be interested in the financial situation of the business.
9 **Recall** five reasons why accounting is useful for business.
10 **Explain** the importance of accountability.
11 **Demonstrate** why astute financial management is considered indispensable to business.

EXERCISE 8.8 EXTENSION

1 Find out more about the Australian Accounting Standards Board (AASB). The weblink in the Resources tab is a useful starting point. **Investigate** how accounting standards are developed and implemented.
2 'Shrinkage' refers to the loss of stock from a business. White-collar crime refers to the theft or embezzlement of money from a business. **Analyse** the proposition that: 'if employees were paid higher wages, then there would be no need to audit as there would be no need for anyone to steal from businesses'.
3 Research an auditing firm. The **Count** weblink in the Resources tab is a useful starting point. **Determine** the range of financial services the firm offers and present an advertisement for the business to the class.
4 **Assess** the effect of an economic downturn on a business's financial management.

on Resources

Weblink: Australian Accounting Standards Board (AASB)
Weblink: Count

8.5.3 Financial statements

Introduction to financial statements

BizWORD

Financial statements *are reports that summarise transactions over a period of time.*

All business owners must be able to make judgements about the direction of the business at any given time. To help them achieve this, they need to prepare some **financial statements** — reports that summarise transactions over a period of time. The main accounting reports and financial statements are cash flow statements, income statements and balance sheets. Business owners, for example, will need to be aware of whether the cash flow through the business is sufficient to allow the business to pay its debts on time, whether or not the business is trading profitably, and the financial status of the business.

8.5.4 Cash flow statements

BizWORD

A **cash flow statement** *is a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time.*

Liquidity *refers to the amount of cash a business has access to and how readily it can convert its assets into cash so that debt can be paid.*

A **cash flow statement** is a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time. Cash flow statements are vital for the business to assess whether money inflows can match money outflows. The term '**liquidity**' is often used to describe whether a business has a good or adequate cash flow. Figure 8.31 summarises the typical monetary inflows and outflows. A business is said to be liquid if it has the cash available to meet payments as they are due. Generally a business would prefer its sales to be in cash for precisely this reason — it has a need for cash to meet its own payments. Why do businesses allow credit sales when they prefer cash? This is because they need to match their desire for cash with the customer's ability to pay. By allowing customers to purchase on credit, the business will obtain sales it might otherwise lose.

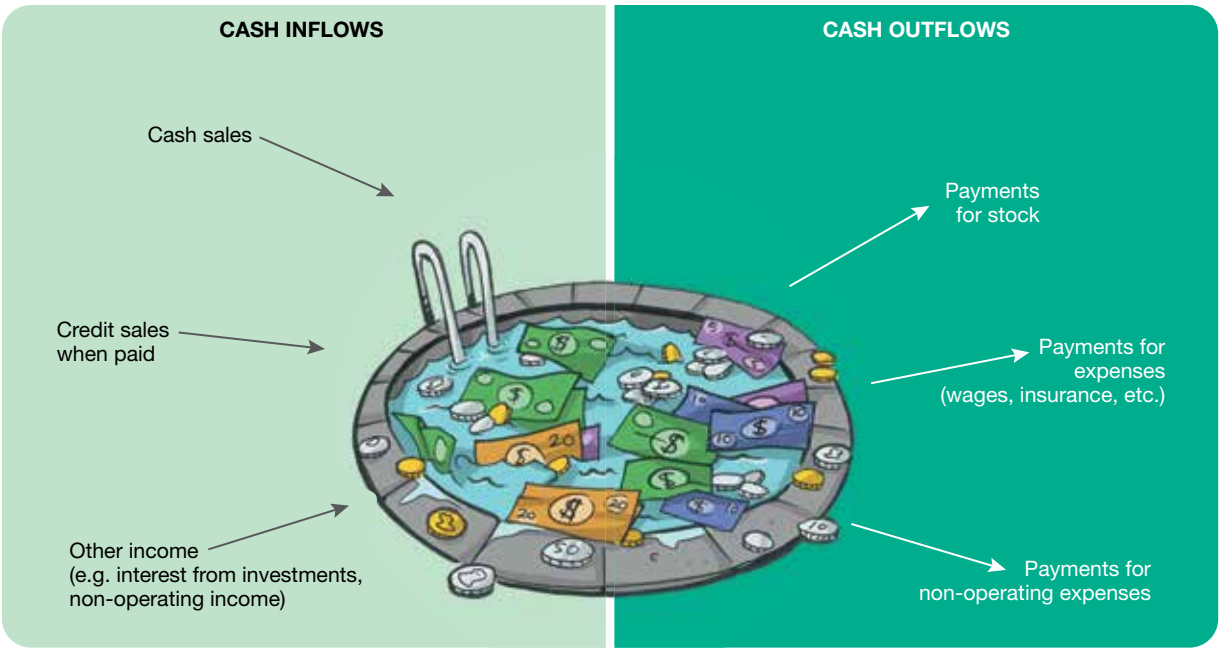


FIGURE 8.31 Cash flow items for a typical business

8.5.5 Examine effective cash flow management

Cash flow statements are closely related to budgets, which are estimates of anticipated future cash flows. Cash flow statements, however, are broader than budgets because they are also used to summarise past information. Cash flow statements are vital for the information they give on the *timing* of payments and receipt of income. A business will keep information on cash movements because this will help it predict future cash flows and hence make provision for payments. A typical cash flow statement can be seen in figure 8.32.

Cash Flow Statement for Plant 1 (first quarter, 2018)	January $	February $	March $
Cash at beginning of year	15 500	26 000	1 119 500
Cash inflows			
Sales:			
retail	20 000	23 000	54 000
public	33 000	36 500	123 000
other manufacturers			
A	1 000 500	2 560 000	2 600 000
B	250 000	250 000	250 000
C	3 400 000	3 200 000	2 800 000
Total inflows	**4 703 500**	**6 069 500**	**5 827 000**
Cash outflows			
Raw materials	3 650 000	3 760 000	4 720 000
Service costs	23 000	23 000	23 000
Leases			
forklifts	11 000	11 000	11 000
equipment	125 000	125 000	125 000
Wages	850 000	990 000	980 000
Other	34 000	67 000	61 000
Total outflows	**4 693 000**	**4 976 000**	**5 920 000**
Cash surplus/(deficit)	**10 500**	**1 093 500**	**(93 000)**
Cash at end of year	26 000	1 119 500	1 026 500

FIGURE 8.32 Typical cash flow statement

A study of the cash flow statement (see figure 8.32) of a manufacturer shows that this business made a cash surplus for two of its first three months of trading for the year the report was made. You can see that the business made a small surplus in January and a large surplus in February. However, in March, this business experienced a cash deficit. It should be clear now why such statements are necessary. A business can track its inflows and outflows over a period of time. It can then use these statements to determine why the inflows and outflows are taking the pattern they are. For example, in January, sales to manufacturer A were down on the usual $2.5 million average. This may have been due to the normal business lull in January. The surplus for February is quite high and an astute manager would have ensured that a portion of this surplus was put aside in case it was needed in future months. As it turned out, the materials costs for March were very high and sales to manufacturer C continued to fall.

The business can see that it needs to take some remedial action. In the short term, if these trends continue, the business could cover cash deficits with the large surplus it made in February. It would not, however, want the pattern of deficits to continue, so managers need to make some decisions. For example, they might ask where they can obtain a regular supply of cheaper raw materials. They could also look at diversifying their sales base.

By using cash flow statements in this way, a business is able to both control finances and plan strategies for financial benefit. Cash flow reporting can be used to plan and predict future cash flow inflows. Outflows tend to follow trends, with some variations over time.

Cash flow statements for larger businesses

While the cash flow statements previously shown are very detailed, they are more suited to small to medium-sized businesses. The format of cash flow statements used by large businesses and public companies is shown in figure 8.33.

Reflections Images Ltd Cash Flow Statement for the year ended 30 June 2018	$000
Cash flows from operating activities	
Sales	600
Payments for stock	(200)
Wages and salaries	(150)
Net cash flow from operating activities	**250**
Cash flows from investing activities	
Sales of non-current assets	500
Purchase of non-current fixed assets	(200)
Net cash flow from investing activities	**300**
Cash flows from financing activities	
New borrowing and currently raised debt	0
Changes in share capital	100
Net cash flows from financing activities	100
Net cash increase/(decrease) from all activities	**650**
Opening cash balance	(340)
Closing cash balance	**310**

FIGURE 8.33 The format of cash flow statements for large businesses and public companies

It can be seen from figure 8.33 that there are various classifications of cash that derived from operating, investing and financing activities. These terms are distinguished below:

- *Cash from operating activities* — these are the cash inflows and outflows relating to the main activity of the business; that is, the provision of goods and services.

- *Cash from investing activities* — these are the cash flows related to the purchase and sale of non-current assets and investments.
- *Cash from financing activities* — these are cash flows related to the acquisition and repayment of both debt and equity finance.

Case study: SME and cash flow

One of the biggest causes of failure among small businesses is running out of cash. Xero launched its Small Business Insights research in 2017, which was based on data from over 500 000 small businesses. Their research found that in recent years in any given month, about half of Australian small businesses are cash flow negative, with more money going out the door than coming in. In fact, in June 2017, only 50.7 per cent of small businesses had a positive cash flow.

Their research also demonstrated that the percentage of businesses operating in the red is tied to how quickly they get paid by their customers. Late payments have continued to impact small businesses, who are currently waiting an average of 44.9 days for payment.

Almost a quarter of small businesses that don't insist on upfront payments have to wait more than a month to be paid, despite the fact they offer 30-day credit terms. This can be hugely disruptive to cash flow. Many small business owners have revealed that they spend on average 12 days a year chasing unpaid invoices. Research has also found that 27 per cent of small businesses that don't insist on upfront payments have been forced to take out loans or use credit to pay for their own expenses such as wages, rent or other outstanding bills.

Fed up with late payments, John Franji and Anthony Daoud who own Flowrite Plumbing decided to dump 30-day payment terms and replace it with 14 days. This has assisted them in managing their cash flow. Since their own suppliers offer them 30 days credit, they are able to purchase the materials they need to complete a job on credit and, by giving their customers only 14 days credit, they usually don't need to use any of their own money to make their repayments. Reducing the payment terms has resulted in an improvement in debtor collections; however, around 50 per cent of their invoices still exceed those terms at any one time and need chasing. Some of their customers pay their debts on average 45 days late. 'Cash flow and collecting payments is vital for us. If debt starts to build up, it can start to snowball and cause problems. We communicate our payment terms up front and chase payments as soon as they are overdue. Throughout the process, we aim to be friendly and helpful as we want the customer to continue with us. We've found that in our industry, it's pretty standard to be chasing late invoices. This is one of the biggest burdens on our business and takes up a lot of our time.'

Chasing late payments is time-consuming and frustrating, and has become a major issue for many small businesses, which affects their cash flow. The Small Business Ombudsman, Kate Carnell, revealed that the number one problem small businesses tell her about is the negative impact late payments have on cash flow. As a result, she conducted an inquiry and in 2017 she released the findings of her *Inquiry into Payment Times and Practices in Australia*. The inquiry found that almost half of all the small businesses surveyed were owed more than $20 000 from late payments and 14 per cent had more than $100 000 owing. Approximately one in two small businesses reported more than 40 per cent of their invoices were paid late in the 2016–17 financial year, which had a big impact on their cash flow.

SNAPSHOT QUESTIONS

1. **Identify** the percentage of businesses that are cash flow negative in any given month.
2. **Outline** the main factor that contributes to this negative cash flow.
3. **How** do John Franji and Anthony Daoud manage their cash flow?
4. **Explain** how late payments affect small businesses.

SNAPSHOT



'… about half of Australian small businesses are cash flow negative …'

SUMMARY

- There are three main financial statements created by accounting processes: the cash flow statement, the income statement (also called revenue statement, profit and loss (P&L) statement or statement of financial performance), and the balance sheet (or statement of financial position).
- A cash flow statement shows the movement of cash receipts (inflows) and cash payments (outflows) over a period of time.
- Liquidity is used to describe whether a business has a good or adequate cash flow.
- Cash flow reports are vital for the information they give on the timing of payments and receipts of income.
- Cash flow statements are divided into three categories: cash flows from operating activities, those from investing activities and those from financing activities.

EXERCISE 8.9 REVISION

1 **Outline** what a cash flow statement is used for.

2 **Define** the term 'liquidity'.

3 **Why** do businesses allow credit sales when they prefer cash?

4 **Explain** the effect (short-term and long-term) of a bank loan on a business's cash flows.

5 **Classify** each of the following items as either a cash inflow or cash outflow, stating your reason for each item.

(a) Credit sales (b) Purchases of stock (c) Payments of wages
(d) Tax on income earned (e) Sales returned (f) Debtor payments
(g) Creditor payments

6 **Why** might a retailer have a variable cash inflow depending on the time of year?

7 **How** can a cash flow statement be used to give a detailed insight into the financial situation facing a business?

8 **Distinguish** between the following cash flow items: those arising from operations, those arising from financing, and those arising from investing activities.

9 Juanita owns a craft shop. During July the business sold $8200 of craft goods and received $200 in bank interest. She paid her sales assistant a monthly wage of $1350. During this month, the business spent $2800 on craft equipment, $350 on rent, $750 on insurance and $150 on electricity.

(a) **Construct** a cash flow statement for the month of July for Juanita's business.
(b) **Calculate** the business's closing cash balance for July if the opening cash balance was $3500.

10 Given the following information for June 2018, **construct** a cash flow statement for Play Safe Pty Ltd.

- Closing cash balance end of May: $19 300
- Monthly wages: $3300
- Weekly sales: $2200
- Weekly rent: $650
- Proceeds from sale of equipment: $8700
- Monthly interest received: $50
- Fortnightly loan repayment: $950
- Dividends paid: $23 000
- Proceeds from issue of shares: $8900

11 The table below shows an extract from a cash flow statement for a business. The opening balance for January is $4000.

	Jan	Feb	March	April	May	June
Cash in ($)	5000	4000	2000	3000	3000	5000
Cash out ($)	2000	3000	6000	5000	6000	4000

(a) **Calculate** the opening cash balance for April.
(b) **Identify** the month in which the business started with a negative cash balance.

EXERCISE 8.9 EXTENSION

1. Cash is often referred to as the 'life-blood' of any business. **Analyse** the effects on a business of carrying too little cash, and outline the problems that could arise if a business carries too much cash.
2. Creditors, or accounts payable, are liabilities owed by the business that are due and payable. Debtors, or accounts receivable, are monies owed to the business by customers. **Assess** how delays in the receipt and payment of cash can have a large effect on a business's cash flow.
3. Research the terms 'liquidity' and 'profitability'. **Distinguish** between these terms and **explain** how sometimes a business will seek greater liquidity for lower profitability (*Hint:* You might like to consider factoring, sale and leaseback, and inventory controls).

8.5.6 Income statement

The **income statement** has also been called the **statement of financial performance**. This alternative title makes the intent and the content of the statement clear. It has had other names including revenue statement, and profit and loss (P&L) statement.

The income statement is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.

As outlined in chapter 1, profit refers to money earned by a business in the course of operating that is in excess of costs; that is, money left after expenses are covered. Mathematically, it is simply the income (or revenue) from all sources less all costs (or expenses).

BizWORD

The **income statement**, *or* **statement of financial performance**, *is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.*

Income statement for year ended 30 June 2018	$
Revenue from sales	2 000 000
Less cost of goods sold (COGS)	1 000 000
Gross profit	1 000 000
Less expenses	500 000
Net profit	**500 000**

FIGURE 8.34 Typical income statement (or statement of financial performance) format (simple)

BizFACT

Good record keeping is essential in order for business owners to be able to complete their financial statements and meet their tax obligations. Businesses who do not keep accurate records will face significant penalties.

Figure 8.34 is a simple income statement that enables you to see the general format. There are several important features to note. First, the statement must have a heading that states the period of time over which the business was operating for the purposes of the statement. Usually this is one year, but it may be half yearly, quarterly, or even every month or six weeks.

Second, there are only five main categories of items:

1. revenue or income
2. cost of goods sold (COGS)
3. gross profit
4. expenses
5. net profit.

Third, the income earned (or revenue) is always stated at the top of the report. If the business had absolutely no expenses then this would be the profit figure. This is not realistic. In truth, the business would have had costs that arose from selling. So, we then deduct the expenses that occurred while the income was being earned.

BizFACT

Occasionally a business will receive money from non-trading sources. Such income is termed 'non-operating' income and includes money from investments that provide a return whether or not the business trades.

This is done in three steps:

1. Calculate the total revenue or operating income.
2. Calculate cost of goods sold (COGS) and calculate the gross profit.
3. Itemise all other expenses (which may be classified into administrative, selling and financial expenses).
4. Calculate net profit.

Step 1. Calculate operating income/revenue

Revenue generally means income from sales. Net sales refers to the amount of revenue a business has earned from sales when the effects of sales returns are deducted.

Sometimes the business will offer discounts to customers who pay outstanding amounts quickly. Such discounts reduce the business income and must be deducted from the calculation of profits. Similarly, when customers return goods, the cost of those goods must be deducted from sales figures. This is the way to work out net sales in the revenue statement:

	$
Sales	100 000
Less discounts allowed to customers	2 000
Less returns of sold items	3 000
Net sales	95 000

BizWORD

Gross profit *is the term given to the revenue less cost of goods sold (COGS).*

The **cost of goods sold (COGS)** *is the value of stock that a business has sold to its customers.*

Step 2. Calculate cost of goods sold (COGS) and gross profit

Gross profit is the term given to the revenue less **cost of goods sold (COGS)** or, mathematically:

Gross profit = Revenue − COGS

The gross profit calculation is important as, essentially, it tells the business how much its mark-up is on the cost price of the goods it has sold. This varies somewhat from business to business but is generally between 50 and 100 per cent. If the mark-up was enormous (say 800 or 1000 per cent), then it would attract other businesses to compete in the market.

The cost of goods sold is an expense to the business. However, it is not grouped with other expenses. This is because the mark-up (or 'contribution margin') on the cost of goods sold determines the level of overall income. In a service-based business, there is no stock and therefore no mark-up. Therefore, income and gross profit are the same. Cost of goods sold affects only businesses that on-sell items they have purchased.

The calculation for COGS is determined as shown below:

BizWORD

Opening stock *is the value of stock (or inventory) that the business has at the start of the financial year.*

Closing stock *is the value of stock on hand at the end of the financial year.*

COGS = Opening stock + Purchases − Closing stock

Opening stock is the value of stock (or inventory) that the business has at the start of the financial year. **Closing stock** is the value of stock on hand at the end of the financial year. Here is an example showing how COGS is calculated:

	$
Opening stock (stock at start of period)	2500
Purchases (during the period)	10250
Closing stock (stock at end of period)	3400

COGS = Opening stock ($2500) + Purchases ($10250) – Closing stock ($3400)
= $12750 – $3400
= $9350

Step 3. Itemise and calculate the total expenses

Expenses are simply costs. Specifically, expenses are the costs incurred in the process of acquiring or manufacturing a product or service to sell, and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service. Expenses must always be subtracted from income to work out net profit. Although not always shown, it is very useful to separate the expenses by type because this helps users of the financial information to target problem areas quickly. In this part of the statement, all the expenses that do not form part of the cost of goods are listed.

The expenses are broken down specifically into three types. These are shown in figure 8.35.

BizWORD

Expenses *are simply costs. Specifically, expenses are the costs incurred in the process of acquiring or manufacturing a good or service to sell and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service.*

Expenses		
Selling	**Administrative**	**Financial**
• Commission • Salaries • Wages • Advertising • Delivery expenses	• Stationery • Electricity • Office salaries • Rent • Rates • Telephone • Depreciation on buildings • Audit fees • Accountant's fees • Insurance payments	• Interest payments • Lease payments • Dividends

Selling expenses:	These relate to the process of selling the good or service and can be directly traced to the need for sales.
Administration expenses:	Costs directly related to the general running of the business.
Finance expenses:	Costs associated with borrowing money from outside people or organisations and to minimising business risk.

FIGURE 8.35 Income statement (or statement of financial performance) expense breakdown by type

Step 4. Calculate the net profit

The final step in the completion of the income statement is to determine the net profit. **Net profit** is the amount remaining when operating and non-operating expenses are deducted from gross profit.

Net profit is shown mathematically as:

BizWORD

Net profit *is the difference between the gross profit and operating and non-operating expenses.*

Net profit = Gross profit – Expenses

If all this information is combined, we can draw a much more realistic income statement (see figure 8.36).

The income statement is always the first one to be compiled at the end of the accounting period. This is because the figures from it are used in the next statement — the balance sheet (or the statement of financial position).

When compiling the income statement, the manager should be mindful of several things — the proportion of gross and net profit to sales and also the level of expenses that accrue to selling, administration and finance. Because the reports collect and summarise a large amount of information, they also provide insight into *how* the business is both earning and spending. This insight is extremely valuable, especially when analysing the statements at the end of the accounting or operating period. The manager would also be aware that the 'bottom line', or net profit, figure, provides more important information than gross profit, which is really only a measure of the mark-up or contribution margin.

BizFACT

The word 'net' means all expenses have been deducted.

U Win Pty Ltd income statement for year ended 30 June 2018

	$	$	$
Sales			5 000 000
Less COGS			3 200 000
Gross profit			1 800 000
Less expenses			
Selling expenses			
advertising	200 000		
sales salaries	300 000		
depreciation on cars	10 000		
delivery	3000		
telephone	9000	522 000	
Administration expenses			
office salaries	400 000		
depreciation on fixtures	5500		
stationery	1500		
security	12 000		
rent	62 500		
insurances	3500	485 000	
Financial expenses			
interest	125 000		
insurances	6000		
leases	6000	137 000	1 144 000
Net profit			**656 000**

FIGURE 8.36 Typical income statement (or statement of financial performance) format (complex)

SUMMARY

- The income statement is a summary of the income earned and the expenses incurred over a trading period.
- The main classification of items in the income statement are revenues, cost of goods sold (COGS) and expenses.
- Gross profit = Revenue − Cost of goods sold (COGS)
- COGS = Opening stock + Purchases − Closing stock
- Expenses are simply costs and can be broken down into selling, administrative or financial.
- Net profit = Gross profit − Expenses

EXERCISE 8.10 REVISION

1 **Identify** the different names given to the income statement.

2 **Define** each of the following terms and, where relevant, write down the mathematical equation that would help in calculating the figure.
- Sales
- Cost of goods sold
- Gross profit
- Net profit

3 **Calculate** the cost of goods sold (COGS), given the following information:

	$
Sales	700 000
Stock (opening)	100 000
Purchases of stock	400 000
Closing stock	50 000

4 Using the figures from question 3, **calculate** gross profit.

5 Using your workings from questions 3 and 4, **calculate** the value of net profit (or loss) if expenses for the period totalled $80 000.

6 Anita Toparis owns and operates Petal's Florist. Last year Anita had a sales revenue of $285 000. Her cost of goods sold totalled $115 000. Her operating expenses were: electricity $5000, advertising $11 000, interest charges $5000, salaries $62 000 and rent $25 000. **Construct** an income statement (statement of financial performance) for Anita and tell her whether she has made a net profit.

7 **Distinguish** between selling, administrative and financial expenses, giving examples for each.

8 **Explain** how an income statement can provide useful information to a business and its stakeholders.

9 Refer to the income statement below and answer the questions that follow.

Income statement for Bella Wedding Accessories for the period ending 30 June 2018

	$	$
Sales		550 000
Less cost of goods sold		
Opening stock	40 000	
Purchases	?	
Closing stock	15 000	
Cost of goods sold		95 000
Gross profit		?
Less expenses		
Selling expenses:		
Advertising	35 000	
Cartage	8 400	
Administrative expenses:		
Rent	?	
Financial expenses:		
Insurance	7 000	
Bad debts	2 500	75 900
Net profit		?

(a) **Calculate** the value of purchases for this period.
(b) **Calculate** the value of the gross profit for this period.
(c) **Calculate** the value of rent for this period.
(d) **Calculate** the value of the net profit for this period.
(e) If the expenses increased by $10 000, **outline** the impact this would have on both the gross and net profit.
(f) **Identify** an alternative administrative expense for this business.

EXERCISE 8.10 EXTENSION

1 Research each of the following items that can be found in an income statement, **define** each, and **determine** where it would be found (under revenue, cost of goods sold, or expenses).
(a) Cartage inwards
(b) Cartage outwards/freight
(c) Commissions
(d) Bad debts
(e) Depreciation
(f) Interest
(g) Security

2 Use the information below to **construct** an income statement (statement of financial performance) for Sathya's Skatehouse:

	$		$
Revenue from cash sales	500 000	Closing stock	20 000
Purchases for the period	50 000	Telephone	15 000
Salesperson's wages	80 000	Rates	3500
Insurance	2000	Revenue from credit sales	50 000
Opening stock	100 000	Depreciation	4 000
Rent	20 000	Electricity	2100
Advertising costs	10 000	Water	3500
Interest costs	2500	Lease costs (machinery)	5500

BizWORD

A **balance sheet** *represents a business's assets and liabilities at a particular point in time, expressed in money terms, and represents the net worth of the business.*

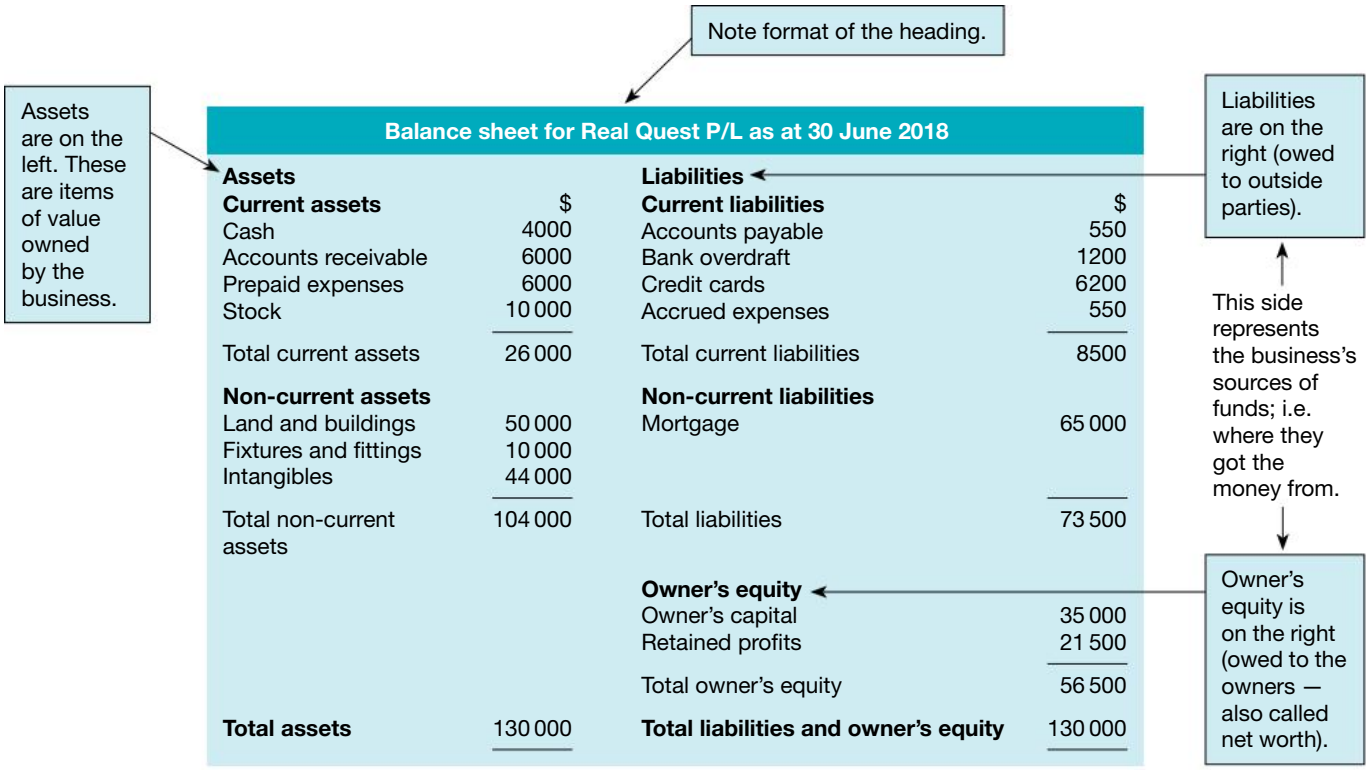
8.5.7 Balance sheets

The **balance sheet**, sometimes called the statement of financial position, is used to help owners keep a watch on their debt and equity levels, compare their overall financial position with that of previous periods, and assist with the process of financial decision making. It is a report that shows the overall financial stability of the business. A typical balance sheet is shown in figure 8.37.

There are several things to note about the balance sheet. First, its heading denotes that it is a snapshot of the business's financial position as at a particular point in time. Second, if a line is drawn between the two columns of figures, the sum of items on the left-hand side 'assets' is equal to, or balances, the sum of items on the right-hand side (liabilities and owner's equity). This format for a balance sheet is called the 'T-format' because we can draw a line down the middle and separate the report into two halves by using the letter T. An alternative format, the narrative format, is explored in Year 12.

Balance sheet items

You will notice that the balance sheet is divided into two parts as shown in figure 8.37. On the left-hand side are recorded the assets — the things the business *owns*. On the right-hand side are recorded the liabilities and owner's equity — the sources of funds.



Balance sheet for Real Quest P/L as at 30 June 2018

Assets		**Liabilities**	
Current assets	$	**Current liabilities**	$
Cash	4000	Accounts payable	550
Accounts receivable	6000	Bank overdraft	1200
Prepaid expenses	6000	Credit cards	6200
Stock	10 000	Accrued expenses	550
Total current assets	26 000	Total current liabilities	8500
Non-current assets		**Non-current liabilities**	
Land and buildings	50 000	Mortgage	65 000
Fixtures and fittings	10 000		
Intangibles	44 000		
Total non-current assets	104 000	Total liabilities	73 500
		Owner's equity	
		Owner's capital	35 000
		Retained profits	21 500
		Total owner's equity	56 500
Total assets	130 000	**Total liabilities and owner's equity**	130 000

FIGURE 8.37 Typical balance sheet (or statement of financial position) showing division into main parts

Assets

Assets are items of value owned by the business that can be given a monetary value. Assets can be divided into several different types: current and non-current, tangible and intangible.

Current assets are assets that a business can expect to use up, or turn over, within 12 months. Examples include cash, accounts receivable (also called debtors) and inventories (stock).

Non-current assets are those assets that have an expected life of longer than 12 months. These include large physical items such as buildings, land, machinery, technology, vehicles, furniture, fixtures and fittings.

Intangible items are also included here. Intangible items are things of worth that have no physical substance. Examples include goodwill, trademarks, designs, copyright and patents. A good name or reputation ('goodwill') or an easily identifiable logo obviously has worth — but how do you value in dollar terms something like good product design, a creative staff or reputation? Nevertheless, intangible assets are a resource that the firm owns and must be recorded in the accounts.

BizWORD

Assets *are items of value owned by the business that can be given a monetary value.*

BizFACT

Intangible assets, such as goodwill, are very hard to value in dollar terms. After ASIC reviewed Nine Entertainment Corp's 2016 full-year financial report, they raised concerns regarding the value of goodwill relating to the Nine Network. In response, Nine reviewed the value of their assets and reduced the value of goodwill from $422 million to $162 million in 2017.

Liabilities

Liabilities are items of debt owed to outside parties and/or other organisations (like suppliers or the banks) and include loans, accounts due to be paid by the business, mortgages, credit card debt and accumulated expenses. The business will divide the liabilities into current and non-current items.

Current liabilities are those in which the debt is expected to be repaid in the short term (12 months or less) and include bank overdrafts, credit card debts, accounts payable (also called creditors) and accrued expenses.

Non-current liabilities are long-term debt items such as mortgages, leases, debentures and retirement benefit funds (money owed to employees upon their retirement from the business). Some of these non-current liabilities can last up to 30 years.

BizWORD

Liabilities *are items of debt owed to other organisations (e.g. suppliers, banks) and include loans, accounts to be paid by the business, mortgages, credit card debt and accumulated expenses.*

Owner's equity

BizWORD

Owner's equity *is the funds contributed by the owner(s) to establish and build the business. It is also called 'capital'.*

The owners give a business money for it to acquire resources and begin operating. This money is called **owner's equity** (capital). As the business operates, it should start to earn an income to cover its costs and then later earn a profit. The business can hold or retain these profits to target money for a particular project or it may put money into 'reserves' for distribution later. The business could also choose to repay the owners who invested their money in the business at the outset.

Over time, a successful business will have its owner's equity amount increase in value. This means that the owner's claim on the business will also increase. This is the owner's reward for risking their money — and is also the reason for people investing in the stockmarket long term.



FIGURE 8.38 The proportion of liabilities (debt) compared to equity is referred to as gearing. Gearing measures the relationship between debt and equity. A business that has more debt than equity is said to be highly geared. The higher the gearing, the greater the risk the business has of not being able to meet its long-term financial commitments.

The balance sheet equation

The balance sheet is called the balance sheet for a good reason — it should always balance. This means that the sum of items on the left-hand side (the assets) must total the sum of items on the right-hand side (liabilities and owner's equity). This is summarised in the balance sheet equation below.

A = L + OE

Assets = Liabilities + Owner's equity

You will immediately see that the balance sheet is set out in a way that mirrors the accounting equation, with assets on the left, and liabilities and owner's equity on the right.

Example 1

	$
Assets	145 000
Liabilities	110 000
Owner's equity	?

Since

A = L + OE then we can say $145 000 + $110 000 + OE.
Therefore owner's equity must be $35 000.

Example 2

	$
Accounts receivable	12 000
Cash at bank	65 000
Mortgage	250 000
Capital	230 000
Accounts payable	3000
Visa Card debt	6500
Land and buildings	?

Step 1: Identify all assets, liabilities and owner's equity items and group them as shown (into the format of the balance sheet).

Assets	$	Liabilities	$
A/cs Rec.	12 000	A/cs Pay.	3000
Cash	65 000	Visa Card debt	6500
Land and buildings	?	Mortgage	250 000
	77 000		259 500
			$
		Owner's equity	
		Capital	230 000

Step 2: Apply the equation and find the unknown quantity.

A = L + OE
$77 000 + ? = $259 500 + $230 000
$77 000 + ? = $489 500
? = $489 500 – $77 000 = $412 500 (value of land and buildings)

By applying the equation we can find the missing item. In general, whenever you see a balance sheet, it is wise to quickly do this equation to satisfy yourself that it is correctly drawn.

SUMMARY

- The balance sheet shows the overall financial stability of the business.
- The main items in the balance sheet are assets, liabilities and owners' equity.
- Assets are items of value to the business and can be either current or non-current.
- Liabilities are debts or business borrowing and can be either current or non-current.
- Owner's equity items refers to the owners' claims and is considered a liability from the point of view of the business.
- The balance sheet should always balance.
- This means the assets must equal the liabilities.
- The balance sheet equation is: Assets = Liabilities + Owner's equity or A = L + OE.

EXERCISE 8.11 REVISION

1 **Identify** the alternative title used for a balance sheet.
2 **Outline** the purposes of a balance sheet.

on Resources

Weblink: Balance sheet

3 **Identify** what is meant by the term 'T-format' used to describe the balance sheet.

4 **Account** for the fact that the balance sheet is called a 'balance' sheet with reference to both sides of the statement.

5 **Define**, with examples, what is meant by the term 'assets'.

6 **Distinguish** between current and non-current assets, with examples of each.

7 **Outline** the intangible items of a balance sheet.

8 **State** what liabilities are, and distinguish between those that are current and those that are non-current.

9 **Explain** how the business owes owners both their investment and also a return for their investment.

10 The balance sheet below as at 30 September has been badly prepared. **Construct** the balance sheet correctly.

Balance sheet as at 30 September

Assets	$	$	Liabilities	$	$
Bank	3400		Motor vehicles	30 000	
Creditors	2500		Debtors	2 000	
Capital	46 000		Stock of materials	1 600	33 600
Loan	10 000		Owner's equity		
			Equipment	23 000	
			+ Drawings	4 000	
				27 000	
			– Net profit	5 500	21 500
		61 900			55 100

11 **Calculate** the missing figure for each of the following:
(a) Assets = $245 000, Liabilities = $43 000, Owner's equity = ?
(b) Assets = $342 000, Owner's equity = $152 000, Liabilities = ?
(c) Assets = ?, Liabilities = $63 000, Owner's equity = $212 500

12 Using the following balance sheet, **calculate** the value of the mortgage.

Balance sheet for Muggers Cups P/L as at 30 June 2018

Assets		**Liabilities**	
Current assets	**$**	**Current liabilities**	**$**
Cash at bank	7000	Creditors*	1250
Debtors*	3400	Bank overdraft	2200
Stock	11 000	Credit cards	4800
Non-current assets		**Non-current liabilities**	
Land and buildings	150 000	Mortgage	?
Fixtures and fittings	12 300		
		Owner's equity	
		Owner's capital	35 000

**Note:* Debtors are accounts receivable; creditors are accounts payable.*

13 **Calculate** the total value of assets, owner's equity and liabilities from the balance sheet in question 12.

14 If retained profits and owner's capital totalled $23 000, instead of $35 000, **calculate** the new value of the mortgage.

15 An artist, Candice Wahler, has asked you to help her construct a balance sheet.
(a) Briefly **explain** to her how a balance sheet is set out.
(b) **Construct** a balance sheet for her as at today's date from the following information: cash at bank $1500, motor vehicle $10 000, accounts payable $6000, equipment $8200, accounts receivable $3000, bank loan $13 500 and stock $3000.

16 Answer the following questions based on the balance sheet below.

Balance sheet for Michael's Café as at 30 June 2018

ASSETS	$	$	LIABILITIES	$	$
Current assets			**Current liabilities**		
Cash in bank	5600		Overdraft	3200	
Debtors	3300		Creditors	4600	
Stock	**(a)**	15 000			
			Non-current liabilities		
			Bank loan	**(e)**	
Non-current assets					
Building	**(d)**		**OWNER'S EQUITY**		
Equipment	17 000		Capital	61 550	
Furniture	13 500	130 600	Retained profits	10 000	
Total			**Total**		

(a) **Calculate** the value of the stock (a).
(b) **Identify** what another name for stock is.
(c) **Identify** what another name for creditors is.
(d) **Calculate** the value of the building (d).
(e) **Calculate** the value of the bank loan (e).
(f) **Calculate** the value of total liabilities.
(g) If this business decided to pay back $1000 to their creditors, **identify** the two items on the balance sheet that would be affected.

EXERCISE 8.11 EXTENSION

1 **Determine** why increases in business wealth add to the owner's equity amount and thereby increase the wealth of those investing in business.

2 **Account** for the fact that the income statement will always be drawn up before the balance sheet.

3 Intangibles are subjectively valued, whereas tangible assets are more easily objectively valued. **Extrapolate** why the value of intangibles — such as goodwill, trademarks, designs, copyright and patents — are very hard to value, while the value of buildings and vehicles can be easier to determine.

4 In accounting, the true value of assets — such as buildings and land (which may be revalued upwards), vehicles (which may be valued downwards) and goodwill — is reflected in accounts as 'depreciation', 'amortisation' or 'revaluation reserves'. Research these terms and **analyse** how they are used to find a truer picture of the value of a business's assets.

5 Goodwill is sometimes determined by the following two methods:
- *method 1* — the difference between the total value of a business's assets and the selling price of the business
- *method 2* — a proportion (e.g. 20 per cent) of the average of the past three years' trading profits.

Application of method 1

A business is offered for sale for $250 000, but the valuation of the assets and stock at cost is $200 000. Thus, the goodwill is $50 000. This reflects the good trading reputation of the business, the stable client base and stable supplier contracts.

Application of method 2

A business records the following profits in the years 2015–2017. **Calculate** its goodwill if goodwill is set at 40 per cent of the average three-year trading profits.

	2015	2016	2017
Net profit	$45 000	$65 000	$50 000

Goodwill = ($45 000 + $65 000 + $50 000) × 0.40 = $160 000 × 0.40 = $64 000

Use the information below to **determine** the value of goodwill in the various scenarios provided:

(a) Ben's Bowling is a business that is up for sale. The selling price is $150 000. The value of the assets totals $120 000.

(b) Leon's Laser Toys has recorded annual profits for the last three years averaging $100 000. The goodwill calculation rate to apply is 33 per cent.

(c) Tina's Video and Film Corporation has assets worth $40 000 in total. Profits are $3000 annually on average, but she has put the business up for sale at $200 000. What should the goodwill be, assuming a goodwill calculation of 30 per cent of average profits over three years? What goodwill is Tina asking? **Analyse** the problems this raises for the valuation of intangible assets.

6 When a Qantas airline skidded off the end of the runway in Singapore, its perfect safety record was tarnished. No longer could it claim to be the 'world's safest airline'. **Predict** the effect this incident could have had on Qantas's goodwill.

8.5.8 The role of the income statement and the balance sheet in describing the financial performance of a business

The income statement helps business owners and other stakeholders see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit.

Analysis of the income statement can also reveal the effectiveness of a business's planning policies concerning pricing, sales, discounts and the valuation of stock, as well as how effective the funds contributed by the owners have been in generating profit.

The balance sheet shows the financial stability of a business. Analysis of the balance sheet can indicate whether:

- the business has enough assets to cover debts
- any money borrowed can be repaid
- the assets of the business are being used to maximise profits
- the owners of the business are making a good return on their investment.

The balance sheet can also reveal the return on the owners' investment, the business's ability to meet both its short-term and long-term financial commitments, whether the business has sufficient assets to continue to make profits in the longer term and how the year's figures compare with previous years, as well as those of competitors.

8.6 Human resources

BizWORD

Human resource management (HRM), *in its simplest terms, is defined as the effective management of the formal relationship between the employer and the employees.*

Employees can make or break a business, so the management of staff has to be top priority for every business owner. **Human resource management (HRM)**, in its simplest terms, is defined as the effective management of the formal relationship between the employer and the employees.

Successful business owners recognise that they rely on the quality of their employees to achieve their goals of improved profit, growth and increased market share. For a business to make best use of its employees, it should:

- take care to hire the best people
- develop cooperative and effective working relationships
- motivate staff to do their best in the workplace
- provide employees with opportunities for training and development.

Also, when an employee turns out to be an excellent worker, retaining that employee may be crucial to ongoing business success. Without dedicated, trained and motivated employees, the best organised plans will never be achieved. The human factor is crucial in all businesses.



FIGURE 8.39 Atlassian has been named the 'Best Place to Work' in Australia by *Business Review Weekly* (BRW) for five years in a row. The company adopts a collaborative approach to management and gives employees the autonomy and freedom to take some chances and innovate. Some of the perks include a fully-stocked kitchen with beer taps, a pool room, a gamers' lounge and a ping pong table. They also offer free yoga, Pilates and boot camp. Although Atlassian doesn't provide monetary bonuses, it gives employees a free holiday for their five-year anniversary.

Most businesses that are successful in the long term maintain a balance between concern for success (expansion or profit) and regard for their employees. Better work and employment relationships, therefore, begin with the business recruiting and selecting appropriate staff members (see the following Snapshot).

SNAPSHOT

Case study: PwC — Australia's Top Company to work for

A radical change to this company's notoriously draconian office rules transformed it into our most popular employer

Meditation rooms, flexible hours and casual clothing: it's all part of working for a big corporation in 2017.

Even Australia's most conservative employers are taking their cue from the tech industry by throwing out the old rule book for workplace decorum, allowing staff to come and go as they please, and wear what they want.

It's how professional service giant PricewaterhouseCoopers — which until recently was known for its draconian dress code — came to be ranked number one on LinkedIn's Top Companies list, released on Wednesday.

The global firm made headlines last year when it sent a London staffer home without pay for not wearing heels to work.

Its former, admittedly 'outdated' workplace apparel rules demanded that male employees wear suits, ties and business socks, while women had to don 'tailored' trousers or dresses and "business-style shoes or boots".

These days, staff are free to dress in whatever way makes them feel 'comfortable and confident' for the day's activities, with jeans and sneakers a perfectly acceptable choice for a day at the office — and it's upped their appeal to job seekers.

At the company's new waterfront HQ at Barangaroo in Sydney, there are plenty of suits and ties on display when news.com.au visits.

But there are signs of a workwear revolution in the breakout meeting spaces that can be found throughout the airy, light-filled office, especially among younger employees.

Sneakers, ripped jeans and edgy haircuts take their place alongside more conservative attire, with those staff members hosting client meetings more likely to dress up.

Sue Horlin, PwC's managing partner for human capital, said the new clothing rules were a powerful symbol of the firm's culture.

'We hire super smart people to do really hard jobs, and I don't think they need an organisation to tell them what to wear every day,' Ms Horlin told news.com.au.



'… small perks … all add up to create strong employer brand …'

'It's not a dress up or down policy; it's just 'get up in the morning and think about what you're doing that day and dress so you feel comfortable and confident'.'

The new rules came into effect a year ago, and the company has transitioned its east coast employees into updated offices in the same time frame.

Walking around the building, it feels more like a trendy hotel than a bean counter's haven.

A smartly-dressed man with a full beard stands at the front desk, against the backdrop of a green-planted feature wall.

Staff arriving for the day tap on touch screens to discover which space their team members have decided to work from — assigned desks being a thing of the past, of course.

Baristas hand out free coffee and there's an open window looking into the kitchen of the in-house restaurant.

Treadmill meetings, ping pong tables and 'activity based working' have been introduced in a bid to foster creativity.

'We wanted to make it a fun, energising open place to work and create an environment to let people show up and work how they want to,' Ms Horlin said.

There's a library where mobile phones and talking are banned, for those who wish to eliminate distractions, while vast open-plan collaboration floors are littered with whiteboards and movable dividers set up as makeshift meeting rooms.

It's an approach that draws inspiration from the tech companies that make up part of the firm's clientele — and aims to lure talent that might otherwise go to work for Apple, Google or one of the big banks.

Small perks add up

Employees at PwC enjoy floating public holidays, allowing them to switch their day off to another date. Even better, no-one at the firm is expected to work on their birthday.

New employees are assigned a buddy to help them settle in, and managers get $1200 a year to spend on the development opportunity of their choosing.

Performance is based on 'outputs, not inputs', Ms Horlin said, with more than half of staff members taking advantage of PwC's work-from-home policy. Employees' comings and goings at the office are not monitored, she said.

LinkedIn Australia's director of talent, Jason Laufer, said financial services firms were looking to create 'a sense of belonging and fun' in order to secure the best talent.

'We know that a company's culture and purpose are key drivers for attracting great talent, but also retaining employees,' Mr Laufer said.

'It definitely helps when organisations offer these small perks, because they all add up to create strong employer brand.'

The corporate social media giant ranks Australian companies on their popularity with job seekers on the platform, with LinkedIn's algorithms taking in job seeker reach and engagement, plus data on employee retention rates.

Source: Dana McCauley, 'PwC named Australia's top company to work for by LinkedIn', *news.com.au*.

SNAPSHOT QUESTIONS

1. **Outline** the strategies employed by PwC that make it one of the best places to work.
2. **Explain** the benefits to the business of being viewed as one of the best places to work.

BizWORD

The **human resource/employment cycle** *covers all stages in the process of employing staff, from initial planning through to recruitment, selection, induction, training and development, performance management, and eventual separation of employment.*

The main functions of staffing are to attract and acquire, train and develop, reward, maintain, and separate the people — the **human resource/employment cycle** — needed to achieve the business's goals. It is crucial for all businesses to select employees whose business approach complements that of the business. How well these functions are managed will largely determine the success of any business. Once a person is selected for a position they must be 'maintained' in the workplace.

Training and development, as well as ongoing feedback on work performance, will assist both the employer and employee. Separation (termination) of employment is the final phase of the human resource cycle; it must be managed to ensure employees are treated fairly and within the law.

The dynamic nature of business means that staffing needs will change over time. As the business expands, or existing employees resign or retire, new positions will be created, so business owners need to constantly monitor their staffing needs. However, at the heart of staffing is the employee. Hiring the 'right' person for the 'right' position is of crucial importance to all businesses.

The HSC course investigates human resources in greater depth, so this chapter will provide an elementary understanding of the main concepts.

BizFACT

Gerry Harvey of successful retail chain Harvey Norman said, 'Businesses are made by people. We've proven time and again that you can have a wonderful shop, and put a bloke in there who's no good, and he'll stuff it up. Put a good bloke in, and it just turns around like that.'



FIGURE 8.40 It's important to hire the 'right' person for the 'right' position. Employees are often one of the most untapped aspects of a company's 'brand'. Not only are they the face of the business and living representatives of a business's brand, they also differentiate one brand from its competitors. They therefore need to be projecting the right image to the outside world. If an employee's behaviour is not in sync with the image of the business, the consequences can be detrimental.

8.6.1 Human resource cycle

The human resource cycle involves a business determining its employment needs in line with its business strategy. As the name suggests, human resource management begins with acquisition — recruiting and selecting people to work for the business. Next, plans and procedures need to be put into place to train and develop these employees. As well, steps must be taken to keep — that is, maintain these valuable resources. Finally, there are times when employees will separate from the business, either voluntarily, through retirement or resignation, or involuntarily, through retrenchment or dismissal.

Figure 8.41 summarises the four main elements of the human resource cycle/staffing process: acquisition, development, maintenance and separation.

Each of these elements consists of related activities (see table 8.5) that are carried out by the human resource department. Each of the four elements complements the other, with the desired outcome being a productive and efficient workforce.

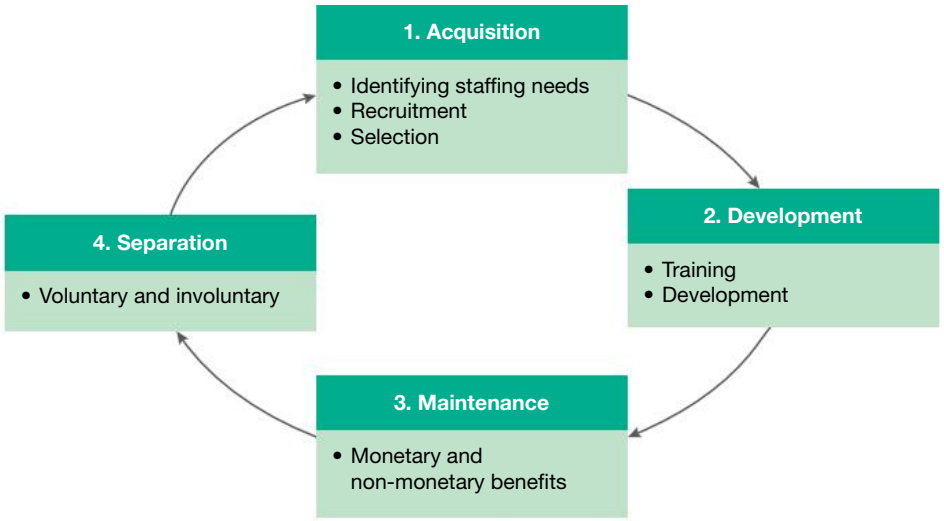


FIGURE 8.41 The four main elements of the human resource cycle/staffing process

TABLE 8.5 Elements of the human resource/staffing process and their related activities

Element	Activities
Stage one *Acquisition* • Hiring new employees	• Planning: identifying staffing needs; job analysis (determining the exact nature of the position to be filled) • Recruitment: attracting people to apply for the position in the business; internal and external recruitment • Selection: choosing and hiring the most qualified; testing and interviewing
Stage two *Development* • Improving employees' skills and abilities	• Induction and training: teaching employees new skills and helping them learn tasks associated with their jobs • Development: the process of improving the skills, abilities and knowledge of staff
Stage three *Maintenance* • Motivating employees to remain with the business	• Monetary benefits: rewarding employees' efforts through financial compensation; pay rates • Non-monetary benefits: rewards such as conditions; fringe benefits
Stage four *Separation* • Employees leaving the business	• Voluntary: employees leaving on own accord; retirement, resignation • Involuntary: employees being asked to leave; retrenchment, dismissal

If handled correctly, 'human resources' can provide a business with a competitive advantage; if mishandled, this key area can generate many problems.

No longer can a business rely on a constant supply of homogeneous employees prepared to join a company for a lifetime. Businesses today must accommodate working parents with daycare needs, the middle-aged employee who has to care for an elderly parent or an increase in people from culturally diverse backgrounds.

Therefore, businesses today are taking their human resources function, especially the staffing process, more seriously than in the past.

BizFACT

Developing a team approach within the workplace can bring about many benefits including enhanced employee morale, higher levels of productivity and more satisfied workers.

SUMMARY

- Employees are the most important resources for business success.
- Human resource management is the effective management of the formal relationship between the employer and the employee.
- Most successful businesses maintain a balance between concern for success and regard for their employees.
- The main functions of staffing are to attract and acquire, train and develop, reward, maintain and separate the people needed to achieve the business's goals.

EXERCISE 8.12 REVISION

1. 'People are the business's most valuable resource.' **Outline** what is meant by this statement.
2. **Define** the term 'human resource management'.
3. **Recall** what a business should do to make the best use of its employees.
4. **Identify** the main functions of staffing.
5. **Explain** why good staff management is vital to a business's success.
6. **Identify** the main functions of the staffing process.
7. **Why** is the staffing process referred to as a 'human resource cycle'?
8. **Construct** a concept map summarising the four main elements and the related activities of the staffing process/human resource cycle.
9. **Predict** what problems can arise if a business employs a person unsuited to a particular position. Share your answer with the rest of the class.

BizFACT

If a business forecasts a greater demand for employees than the supply available, it will adopt a strategy of attracting new employees. If, however, supply of employees is forecast to be greater than demand, it will plan for a reduction of the workforce.

EXERCISE 8.12 EXTENSION

1. **Demonstrate** the relationship between the human resource cycle and business goals.
2. Traditional human resource management (HRM) practices were developed and administered by the business's human resource department. A recent study of HRM practices revealed that line managers — people responsible for the management of staff contributing to the main function of the business — are playing a greater role in developing and implementing human resource (HR) practices. **Assess** the value a line manager can bring to developing and implementing HR practices.
3. 'The future is unpredictable. The business environment changes so rapidly that it is impractical to make relevant plans for future staffing requirements. HR plans are therefore largely irrelevant.' **Evaluate** the accuracy of this statement.

BizWORD

Acquisition *is the process of attracting and recruiting the right staff for roles in a business.*

Job analysis *is a systematic study of each employee's duties, tasks and work environment.*

8.6.2 Recruitment

As mentioned above, the first stage of the human resource cycle is **acquisition**. Acquisition refers to the process of attracting and recruiting the right staff for roles in a business.

Prior to recruitment, a business must undertake a **job analysis**. There is no sense in hiring people unless the business is clear about what it is hiring them to do. In other words, the business must determine the exact nature of a job before it can recruit the right person to do it. Job analysis is a systematic study of each employee's duties, tasks and work environment.

A job analysis examines:

- actual job activities
- equipment used on the job
- specific job behaviours required
- working conditions
- degree of supervision necessary.

BizFACT

Over the next decade, the workforce will age considerably (often referred to as the 'greying' of the population) as the post–World War II, 'baby boomer' generation grows older. Take, for instance, the nursing profession. In 2001, the average age of both registered and enrolled employed nurses was 42.2 years. Now the average age of a nurse is around 50 years. It is therefore not surprising that in recent years there has been a recruitment drive to attract more people to become nurses, and many nurses from overseas have been employed.

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FIGURE 8.42 An example of a job description and a job specification

BizWORD

A **job description** *is a written statement describing the employee's duties, tasks and responsibilities associated with the job.*

A **job specification** *is a list of the key qualifications needed to perform a particular job in terms of education, skills and experience.*

Recruitment *is the process of finding and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies.*

Internal recruitment *involves filling job vacancies with present employees, rather than looking outside the business.*

The job analysis for a particular position typically consists of two parts:

1. **Job description**: a written statement describing the employee's duties, tasks and responsibilities associated with the job (see figure 8.42).
2. **Job specification**: a list of the key qualifications needed to perform a particular job in terms of education, skills and experience (see figure 8.42).

Once the job description and specification have been completed, it's on to the process of recruitment and selection.

Recruitment involves finding and attracting the right people to apply for a job vacancy using advertisements, employment agencies and word of mouth. When an organisation decides to recruit staff, it may choose internal or external recruitment methods.

Internal recruitment occurs when a business decides to appoint someone already within the business to a vacancy. This usually involves an opportunity for a person



FIGURE 8.43 In an effort to engage with young people and attract new employees, McDonald's launched Snaplications in 2017, which gives Australians the chance to apply for a job at McDonald's through a Snapchat lens. Snapchat users can select a lens which sees them in a McDonald's uniform and from there, they are able to send a 10-second video outlining why they want to work at the fast-food chain to the McDonald's Snapchat account, @Maccas.

Source: McDonald's Australia

to take on different duties, and can mean a promotion to take on greater responsibilities within the business. Internal recruitment is popular and involves less risk, because the employer already knows the person who will be filling the vacancy. Of course, the person recruited internally may then have to be replaced by external recruitment. Table 8.6 outlines the advantages and disadvantages of internal recruitment.

TABLE 8.6 Advantages and disadvantages of internal recruitment

Internal recruitment	
Advantages	**Disadvantages**
Employees are already known to the employer, so choice may be easier.	There may be no-one suitable from within the business.
Applicants are already familiar with the business and its objectives, culture and processes.	If there is more than one internal applicant, it can lead to conflict or jealousies between those employees.
If the position is a managerial or supervisory position, it creates a career path within the business to reward valued employees.	Applicants may be set in their ways and not open to new ideas.
Costs of advertising the position are reduced, and no external agencies need to be paid.	The successful applicant from within may have to be replaced, so an external recruitment process may be necessary anyway.

External recruitment is used to find suitable applicants from outside the business, because staff planning has identified the need for a new position, an existing employee has resigned or retired, or the person previously performing the duties has been transferred or promoted to a new position within the business. Table 8.7 outlines the advantages and disadvantages of external recruitment.

BizWORD

External recruitment *involves filling job vacancies with people from outside the business.*

TABLE 8.7 Advantages and disadvantages of external recruitment

External recruitment	
Advantages	**Disadvantages**
There is a wider range of applicants to choose from.	The applicants are all unknown, so the choice may be more difficult.
Outside applicants may bring new ideas and fresh approaches to tasks.	There are costs associated with advertising the position.
Different qualifications or experience from those already within the business can be specified in the advertising process.	The field of applicants may be larger, so the process of selection may become more time-consuming.
This method allows for rapid growth of the business because it allows for an increase in actual staff numbers.	Qualified employess from within the business may resent outsiders coming in, particularly if it is a managerial or supervisory position.

The recruitment method chosen will depend on the size of the business, the type of position available and the nature of the labour force in the business's particular area. The main sources of employees available to a business include:

- advertisements in the media
- private employment/recruitment agencies
- schools, TAFE colleges or universities
- government employment agencies — for example, Australian Job Search
- internal searches
- online services
- temporary/casual agencies
- word of mouth
- family members.

Most businesses will want to advertise as widely as possible to attract the greatest number of applicants, so they will often use more than one avenue. Many businesses use employment agencies to handle the recruitment of staff. Some agencies specialise in particular industries and will handle all the advertising of vacancies.

This is an expensive, but effective, method — the agency does the preliminary screening of candidates and presents potential employees who fit all the criteria of experience, education and training (see figure 8.44).



FIGURE 8.44 Many businesses outsource the recruitment process and hire recruitment agencies to find them suitable employees as a way of decreasing the time involved in searching for a new employee. They pay an agency to interview applicants and recommend a short list of potential employees suitable for the available position.

Many jobs are advertised online. Businesses, such as Seek Limited, provide an efficient way for job seekers to search online for jobs that meet their qualifications and expectations. Employers and recruiters use businesses like Seek to advertise positions online and therefore reach a wide audience, although some still choose the traditional method of advertising in the newspaper. Advertising in the general media means that a business has to screen applicants and then proceed with interviews. This is often time consuming if the business receives a large number of applications; however, it does prove effective in many cases and small to medium-sized businesses often use this method.

on Resources

Weblink: SEEK



FIGURE 8.45 Job-seekers today are much more likely to search online job advertisements than to use traditional newspaper advertisements. Andrew Bassat, Paul Bassat and Matt Rockman founded Seek Limited, Australia's largest online employment agency, in 1997. In any given month, over 180 000 job advertisements are posted on seek.com.au, with over 4.6 million unique browsers visiting the site.

Once potential candidates have been selected, the business must then choose the best person for the job. **Employee selection** is the means by which the employer chooses the most suitable applicant for a vacancy. This involves identifying the skills, qualifications and experience of each applicant, and relating them to the skills, qualifications and experience listed in the job specification, to achieve the closest possible match.

Selecting the most appropriate candidate can involve all or any of the following options:

- *Written or online application.* Some employers make use of either a printed application form or an online application form to be completed by the applicant, requiring basic personal information, details of qualifications and experience, and names of referees. Alternatively, prospective employees may be able to submit a written application in any form they wish. This will usually include a **curriculum vitae** or **résumé** as well as any other relevant information. Applicants will often try to indicate how their own qualifications and experience match those included in the job specification. The employer usually shortlists a realistic number of suitable applicants.
- *Testing.* Employers may apply a number of different tests to prospective employees. These can include psychological tests or personality tests, which attempt to measure an applicant's personal characteristics; or aptitude tests, which attempt to measure the skills that might be relevant to the job description. Tests may be written, or may require the applicant to perform a number of different tasks.
- *Interviews.* The interview is perhaps the most important procedure in the selection process. Interviews should be well structured and cover a set of common questions to ensure consistency between applicants.
- *Background checks.* Referees can be contacted to verify the accuracy of an applicant's previous experience, and to gain an assessment of their performance in a previous position.

After the successful applicant has been notified and has accepted the position, the other applicants are notified.

BizWORD

Employee selection *involves gathering information about each applicant for a position, then using that information to choose the most appropriate applicant.*

A **curriculum vitae** *or* **résumé** *is a summary of a person's previous employment experience.*

BizFACT

A lot of employee turnover in Australia occurs among newly recruited staff who have spent less than one year in the job. This reinforces research that suggests that most Australian management selection processes are unplanned, subjective, highly susceptible to error and not supported by effective induction programs.

BizFACT

The cost of a poor recruitment decision is believed to be around two or three times the annual salary of the person recruited.

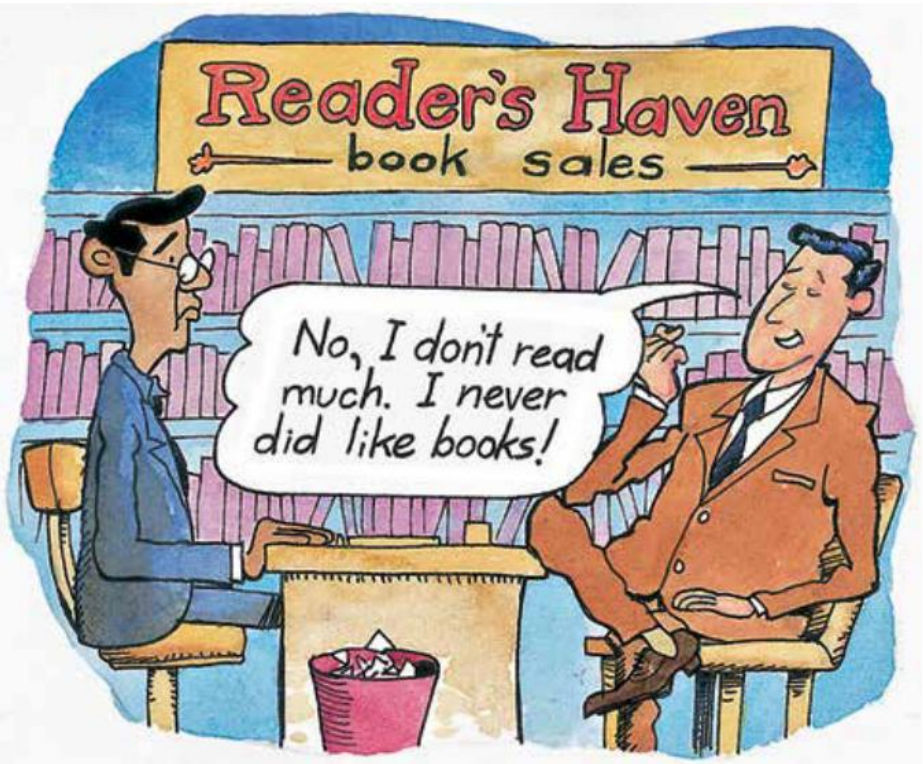


FIGURE 8.46 Hiring the 'wrong' person for the job can be a costly exercise. This is why potential candidates need to prepare well and demonstrate to the employer why they would be the best person for the job.

SNAPSHOT



'… move away from traditional recruitment methods to using technology …'

Case study: NAB ditches CV and résumé

National Australia Bank (NAB) has recently adopted a new approach to recruitment, which has seen the end of reading résumés and traditional job interviews. About twelve months ago, the company scrapped CVs, résumés and face-to-face interviews for thousands of jobs. This is part of a broader trend by many large businesses to move away from traditional recruitment methods to using technology to drastically change how they hire employees.

NAB introduced cognitive assessments and recorded video interviews for candidates applying for entry-level jobs across many parts of the business. This approach has been used for approximately 2500 jobs a year. Candidates are now tested on their natural problem-solving abilities through abstract questions, such as choosing which picture comes next in a series. They then have to send a short, recorded video interview in response to questions. A computer then screens through all the videos for mentions of key words, achievements and experience, and provides the company with a short-list of candidates.

NAB, as well as job candidates, are reaping the benefits of this new recruitment approach. NAB has found that this new model has halved their turnover rate, sped up recruitment and saved the company more than 700 hours a month in management time. The recruitment techniques are also more objective and have reduced the influence of prestigious universities or schools. The new model helps the company to identify and hire great people in a fairer and more effective way and reduces the risk of unconscious bias — it means recruiters are not influenced by people's names or what school or university they attended.

The model has been particularly popular among digitally-savvy candidates, whom the bank is keen to hire. Many candidates have appreciated the new process due to it being much faster and more convenient — they can apply for a job from the comfort of their own homes.

SNAPSHOT QUESTIONS

1. **Outline** NAB's new recruitment approach.
2. **Explain** the benefits of this new model for both the company and job candidates.

SUMMARY

- Acquisition refers to the process of attracting and recruiting the right staff for roles in a business.
- A job analysis is a systematic study of each employee's duties, tasks and work environment. It comprises a job description and job specification.
- After the planning stage, the recruitment of staff commences to find the best person for the job.
- Recruitment involves finding and attracting the right people to apply for a job vacancy.
- A business can recruit from staff within the business or seek new applicants from outside sources.
- Once job applicants are found, the process of selecting the right applicant begins.
- Employee selection is the means by which the employer chooses the most suitable applicant for the vacancy.

EXERCISE 8.13 REVISION

1 **Outline** the process of acquisition.

2 **Explain** the relationship between a job analysis, a job description and a job specification.

3 In each of the following cases, the employer did not plan appropriately. For each example, **construct** a job specification that would have prevented the problem.

(a) Joanne wasn't a qualified veterinary nurse, but the veterinary clinic employed her anyway because she loved animals. On most days, Joanne found difficulty doing simple bandaging and could not provide the advice expected of her.
(b) Carrie was a waiter in a restaurant. When customers came in she would ignore them until she had finished what she was doing and always suggested that tipping was expected.
(c) Janelle was employed as a florist but most of her bouquets fell apart when she handed them to the customer.

4 Undertake a job analysis for the position of 'Year 11 Business Studies student' at your school and **identify** the key elements for consideration.

5 **Construct** job advertisements for two of the following positions:
(a) phone store sales assistant
(b) accountant
(c) motor mechanic
(d) motel receptionist.

Remember to include the job description and the job specification in your advertisement.

6 **Summarise** the two activities in the employment process: recruitment and selection.

7 **Distinguish** between internal recruiting and external recruiting.

8 **Discuss** internal and external recruitment.

9 In small groups, prepare a table of all the recruitment methods with which you are familiar. For each method, **identify** an associated strength and weakness. The first one has been completed for you in the table below.

Recruitment method	Strength	Weakness
Internal advertising	Quick and inexpensive	Draws from existing employees only

10 Select three sources of employees available to a business and **propose** why each is an effective method of recruitment.

11 **Describe** two options that can be used in the selection process.

12 'In the current business environment it is crucial that small business owners recruit and maintain the right people for the job.' In small groups, **discuss** the relationship between good staff and business success.

Vacancy — qualified mechanic

A vacancy exists for a qualified mechanic at TOP CLASS AUTO SERVICE, Main St, Hightown.

Duties will include carrying out the mechanical repair and servicing of a wide variety of different makes and models of cars, vans and trucks, working in a team environment with other mechanics currently employed in the business.

The successful applicant will have completed appropriate apprenticeship qualifications and have at least two years of post-apprenticeship experience in the automotive industry. Qualifications and experience with diesel engines would be a definite advantage for this position.

Applications should include details of qualifications and employment experience, and the names of three referees.

13 Read the above job advertisement and answer the following questions.
(a) **Identify** the job description and job specification.
(b) **Outline** the information people should include in their application.

EXERCISE 8.13 EXTENSION

1. **Determine** how a business's recruiting and selection practices may be affected by the type of position that has to be filled (i.e. a part-time sales assistant compared to a chief executive officer for a large transnational corporation).
2. You have recently been appointed as human resource manager for a national clothing company. The business has a history of high staff turnover and low morale. To correct these problems you have decided to improve the recruitment and selection procedures. **Propose** the steps you might take to identify capable employees. **Determine** how you would screen applicants.
3. In small groups, think of a job you are familiar with and **construct** possible interview questions. Select one person to adopt the role of a human resource manager. Each of the remaining people in the group will become possible candidates for the job. They will need to prepare for the interview and then the human resource manager is to conduct interviews with each person. During the interviews, the remaining members are to act as observers and provide feedback to each candidate. The **Job interview** weblink in the Resources tab has useful tips and advice on how to prepare for a job interview to get you started.
4. **Create** a poster that contains hints for applicants to assist them to succeed at an interview. The **SEEK** weblink in the Resources tab is a useful starting point with hints for applicants preparing for and attending an interview.

on Resources

Weblink: Job interview
Weblink: SEEK

8.6.3 Training

Training and development are aimed at improving employees' skills and abilities — they are necessary for both personal and business growth. New employees may need some training and development, depending on their level of experience. Existing employees also need training and development to continually upgrade their skills. **Training** is teaching staff to perform their job more efficiently and effectively by boosting their knowledge and skills. **Development** is the process of preparing employees to take on more responsibilities in the future through acquiring better knowledge and skills, and gaining more experience in a particular area. Developing staff often involves training. It is interesting to note that many employees expect their business to provide them with opportunities to grow and learn, and ultimately improve their employability.

The aim of training and development is to seek long-term change in employees' skills, knowledge, attitudes and behaviour in order to improve work performance in the business. Many businesses do not, however, spend enough on staff training.

BizWORD

Training *generally refers to the process of teaching staff how to peform their job more efficiently and effectively by boosting their knowledge and skills.*

Development *refers to activities that prepare staff to take greater responsibility in the future.*

BizFACT

Ford Australia claims that employee training has led to halving absenteeism and reducing labour turnover. Can you account for this relationship?



FIGURE 8.47 For Frank Russo of Rainbow Meats, the key to business success is staff training, and the ability to retain great staff. The business currently employs 80 staff across five stores. Frank believes it is important to keep training employees to improve their skills and to ensure a great workforce into the future. His staff are even provided with cooking classes so that they're able to advise customers on the best recipes for different cuts of meat. Frank is committed to the growth of the business through new ideas, but realises that staff training and motivation are crucial to ensuring that new ideas are effectively put into practice.

According to the Australian Centre for Industrial Relations Research and Training, there is little evidence of a strong training culture within Australian workforces. This is unfortunate because a lack of training and development can have long-term implications for a business's ongoing competitiveness, and could lead to higher turnover rates as staff seek development in other forms. Well-organised and well-presented training and development provides benefits for both the employee and the employer (see table 8.8 below).

TABLE 8.8 Training and development provide benefits for both the employee and the employer

Benefits for the employee	Benefits for the employer
• Opportunity for promotion and self-improvement • Improved job satisfaction through better job performance • A challenge — the chance to learn new things • Adaptability — greater ability to adapt to and cope with changes • Improved chances of future employability	• Higher productivity through better job performance and more efficient use of human resources • Goals and objectives more effectively met • Reduced costs due to less labour turnover, errors, accidents, absenteeism • A more capable, 'mobile' workforce • Existing staff more easily retained • Less disruption in the event of staff turnover • An 'insurance policy' — employees are able to cope better with business 'crises' (this is a benefit for employees as well)

An effective training and development program is planned and perceived as integral to the business's strategy, as well as to maintaining or developing a business's sustainable competitive advantage. Ongoing training for all employees is becoming critical due to rapid technological change and global competition — it is so critical that many businesses now promote the concept of a **learning organisation**. A learning organisation is aware of its actions and its environment and tries to improve its understanding of the relationship between the two. All employees are involved in developing knowledge and insights that allow the business to continually grow and improve.

BizWORD

A **learning organisation** *monitors and interprets its environment, seeking to improve its understanding of the relationship between its actions and its environment.*

Case study: Training and retaining staff at acQuire Technology Solutions

Perth-based acQuire Technology Solutions is an employee-owned company that provides a geoscientific information management system to companies operating in the mining and resources industry. It takes great pride in its processes of training staff and retaining them, with staff turnover a relatively low 4 per cent. It either hires geologists and trains them in the IT aspects of the business, or hires technologists with a background in IT, and then trains them in geology. Employees have their career path with the company planned three to five years in advance. Individual career needs and future succession planning are at the centre of these plans, and annual reviews help identify the next steps to be taken in each individual's career path. All employees have access to a training levy to help fund any professional or personal development that is seen to be appropriate in benefiting both the employee and the company.

Employees are encouraged to contribute suggestions for improvement and innovation through a computerised system known as 'Novedad' (Spanish for 'new ideas'). All ideas are assigned to an action officer, who has the responsibility for evaluating them and making recommendations to management. Novedad also provides a forum for other employees to have input into any new suggestions, often allowing for additional ideas to refine and improve the original concept. The company also makes use of a job satisfaction calculator to measure the level of employee satisfaction with their current role, and balance this with their anticipated career path. In completing this calculator, employees allocate 100 points across five

SNAPSHOT



'It takes great pride in its processes of training staff and retaining them …'

employment categories, in terms of current position compared to their ideal job. Scores are discussed with mentors who work with the employee to take action where necessary.

The company has in place a number of strategies to support maximum use of employee skills, and to reinforce the strong desire to retain valued staff. Flexible working hours allow staff to come and go as they please. There are no time clocks, as employees are trusted to put in the necessary time to complete their assigned duties. Staff are also able to work from home if they have a reliable internet connection. Profit sharing also forms part of the company's commitment to retaining staff, with eligible employees able to access shares in the company after three years of service.

SNAPSHOT QUESTIONS

1. **Outline** acQuire Technology Solutions' training initiatives.
2. **Describe** other strategies employed by acQuire Technology Solutions that assist in retaining staff.
3. **Explain** the benefits of these strategies.

Technology creates the need for ongoing training

It is the task of the human resource manager to plan for the effective introduction of new technology. Training needs must be identified well in advance of any proposed technological implementation. This will ensure change happens at a pace consistent with the capabilities and expectations of the workforce. It also means human resource managers must constantly consider the skills required by the workforce in the future. The existing workforce must be trained and, if very rapid technological change demands it, retrained within a short time. While training of employees is often expensive, it cannot be ignored.



FIGURE 8.48 Due to the recognition that people's lives are becoming increasingly demanding, Ford Australia recently invested in mindfulness training for employees to help them de-clutter their daily distractions. Research has shown yoga, meditation or even a workplace nap can help improve focus, productivity, efficiency and creativity. Their mindfulness course involves four days of off-site training, during which Ford employees are taught to develop personal wellness and integrate mindfulness in day-to-day activities. The company believes this investment has enabled them to work more collaboratively and will lead to increased innovation.

Types of training and development

A number of training methods are available to businesses. The most common of these include:

- Off-the-job training — when employees are trained away from the workplace. It usually involves sending individuals or groups of employees to a particular

specialised training institution. This may be a university or TAFE college, where employees can gain a recognised qualification that will assist them in performing more effectively and efficiently at work. It may be a specialist provider, with particular knowledge relevant to an industry, type of equipment or product.

- On-the-job training — this occurs when employees need to learn a specific set of skills to perform particular tasks in the workplace. This training usually occurs within the working environment, and uses the equipment, machinery and documents present in that workplace. It may occur while the employee is performing their regular duties at their regular workstation, or it may occur in a special setting, such as a training room or conference room. Training may be provided by an experienced co-worker, by a leader or manager with particular or specific expertise, or by an external provider.
- Action learning: learning by experience solving real workplace problems — for example, NAB and IBM use this form of training
- Competency-based training: identifies skill strengths and areas where further training is required — for example, medical education uses this form of training.
- Corporate universities: businesses can also form partnerships with academic institutions to develop training — for example, Coles and Qantas have forged partnerships with academic institutions.
- Training technologies — for example, computer-based training (the computer becomes a vehicle for learning), multimedia training, web-based training (training via the internet).

Programs aimed specifically at developing effective managers may focus on the use of:

- job rotation — the employee experiences many different aspects of a business. For example, a manager may move from one section of the business to another, taking with them their management skills and applying them to a different situation.
- mentoring — a mentor acts a bit like a coach, supporting the employee as they learn. The employee is able to gain from the experience and skills of another person in the business.
- formal business training — this may be done through programs such as the Masters of Business Administration (MBA).

Regardless of the type of training, business owners should view training and development as an investment in the human capital of the business, rather than just another expense.

BizFACT

Training at Motorola is high on the agenda. For eight decades, they have been recognised as one of the best employee training companies in the world. In the 1980s, management realised that training should be a continuous learning process involving everyone in the business, so the company set up the Motorola Training and Education Centre; an exclusive institute dedicated to the training and development of all Motorola employees. Every employee must complete 40 hours of training a year. The programs have resulted in improving employee productivity and performance, as well as quality.

SUMMARY

- Training provides employees with the right knowledge and skills to perform their job effectively and efficiently.
- Development focuses on preparing the employee to take on more responsibilities within the business in the future.
- Ongoing training for all employees can be promoted by the business becoming a learning organisation.
- Some common training methods include formal off-the-job training, informal on-the-job training, action learning, competency-based training, corporate universities and training technologies.
- Training needs must be identified well in advance of any proposed technological implementation.
- Training should be viewed as an investment in the human capital of the business.

EXERCISE 8.14 REVISION

1. **What** is the overall aim of training and development?
2. **Distinguish** between training and development
3. **Propose** reasons why you think 'There is little evidence of a strong training culture within Australian workforces'. Share you answer with the rest of the class.
4. **Outline** how training and development can benefit both the employee and the employer.
5. **Distinguish** between informal on-the-job training and formal off-the-job training.
6. **Explain** why training and development expenses should be seen as an investment and not just a business expense.

EXERCISE 8.14 EXTENSION

1. **Propose** what actions you would take, as the human resource manager, if an experienced employee refused to undertake any training.
2. Arrange to interview your school principal or head teacher, and **construct** a report on the training and development policy of the school or faculty.
3. **Evaluate** the following statement: 'When people say they want reward and recognition they really just want a pay increase and that's all.'
4. You are the human resource manager in a large manufacturing company. You have become concerned about the performance of two valuable employees. Peter has worked in the business for many years and is on a high salary because of his experience and skill development. However, he seems to have lost some interest in his work, especially after being recently overlooked for promotion in the business. Veronica is a single mother with young children. She is scheduled to start work at 8.00 am, but is often late to arrive. She says she is unhappy with the poor pay she receives and is looking for a new job. She is a very good worker, who produces good results and is well liked in the business.
   (a) Using this information, **determine** what motivates each employee.
   (b) **Propose** the strategies you would adopt to motivate each employee.

8.6.4 Employment contracts

BizWORD

An **employment contract** *is a legally binding, formal agreement between an employer and an employee.*

When a job applicant accepts an offer from an employer, a contract is established between the two parties. An **employment contract** is a legally binding, formal agreement between an employer and an employee.

An employment contract creates obligations for both employer and employee. All businesses operate within a legal framework of common law and statute law. Contracts of employment are governed by provisions of the *Fair Work Act 2009 (Cwlth)*. A typical employment contract may include some general terms, such as an expectation that the employee will adhere to the policies and procedures of the business, the title or classification of the position the employee is filling, a start date and the name of the immediate supervisor. It may then detail the specific duties to be undertaken, the hours of work, rates of pay, and leave and superannuation arrangements.

Common law

BizWORD

Common law *refers to law developed by courts and tribunals.*

The **common law** is developed by courts and tribunals. Under common law, judges make decisions based on the facts of a case, guided by precedent (decisions made in the past). The body of common law is therefore developed from decisions made over time by judges.

Under common law, both employers and employees have basic rights and obligations in any employment relationship. Figure 8.49 summarises the employer and employee obligations.

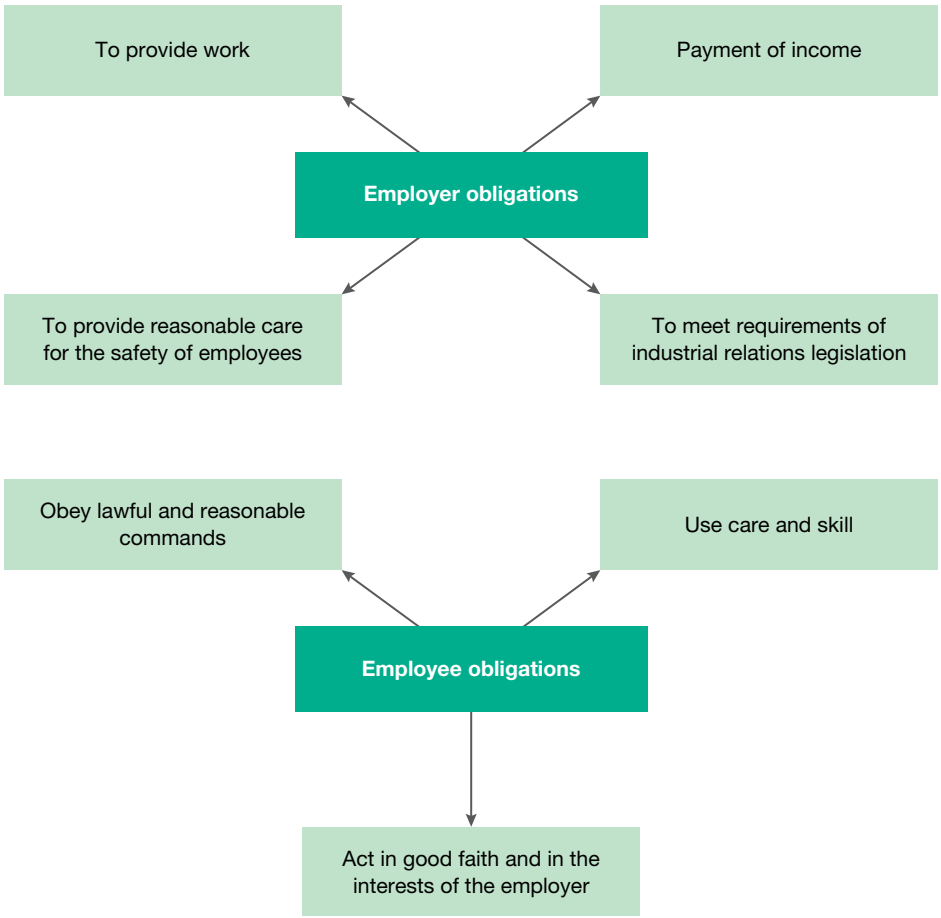


FIGURE 8.49 Employer and employee obligations

on Resources

Weblink: Fair Work Ombudsman

Minimum employment standards

Employees are entitled to a set of minimum employment conditions, known as the National Employment Standards. These were legislated by the federal government in 2010 and apply to all full-time and part-time employees, whether permanent or fixed-term. They generally do not apply to casual employees. The 10 standards are:

- *Hours of work* — for full-time employees, this is generally set at between 35 and 38 hours per week. Employees cannot be required to work longer hours without special provision being made for penalty rates or other compensation.
- *Parental leave* — employees are entitled to 12 months unpaid parental leave in relation to the birth or adoption of a child.
- *Flexible work for parents* — an employee who is a parent of, or has caring responsibilities for, a child under school age will be entitled to request flexible working arrangements after having worked for the same employer for more than 12 months. These could include reduced hours, different start or finish times or home-working arrangements.
- *Annual leave* — for most employees this is four weeks, with part-time employees entitled to a pro rata amount. Casual employees have no entitlement to annual leave.
- *Personal, carer's and compassionate leave* — full-time employees receive 10 days paid personal and carer's leave for every year of service with the organisation, with part-time employees receiving a pro rata amount.
- *Community service leave* — this includes jury service and emergency service duties, such as CFA or SES volunteer work. Employees are entitled to be absent from work for all periods necessary to provide the community service,



FIGURE 8.50 SES volunteers are entitled to take community service leave for emergency work.

including reasonable travelling time and rest time immediately after the activity. Usually this is unpaid leave, although employees on jury service leave can claim make-up pay.

- *Public holidays* — employees are not required to work on public holidays, but will still be paid for the hours they would have worked. If the employer requests the employee to work on a public holiday, the employee may be entitled to a penalty rate or other compensation.
- *Information in the workplace* — employers are required to supply all employees with a 'Fair work information statement' when they commence employment. This is a government document which contains information about the National Employment Standards and other employment related issues.
- *Notice of termination and redundancy* — most employees are entitled to minimum periods of notice of termination of their employment (or pay in lieu of notice), based on their period of continuous service. Fixed-term and casual employees, and employees serving a probationary period of employment, are not included.
- *Long service leave* — permanent employees, whether full time or part time, are entitled to long service leave after a qualifying period. This period varies between different occupations and industries.

Awards

BizWORD

An **award** *is a legally binding agreement that sets out the minimum wages and conditions for a group of employees.*

Awards have been the traditional means of establishing working conditions for employees. An **award** is a legally binding agreement that sets out the minimum wages and conditions for a group of employees. Modern awards came into effect on 1 January 2010. The ten matters that can be included in modern awards are listed in table 8.9. Some businesses will provide above-award payments, especially if they wish to attract more workers to their firm or if they want to hold on to their existing staff. Awards have the following advantages:

- set a minimum for pay and conditions
- cover all employees performing a similar job.

Awards have the following disadvantages:

- can be inflexible and therefore may not suit all employees or businesses
- prevent recognition of individual initiative because all employees are guaranteed the minimum pay and conditions regardless of how productive they are.

TABLE 8.9 Matters covered by awards

The 10 matters that can be included in modern awards
1. Minimum wages, including disability and training wages
2. Types of employment, such as full-time, part-time, outworker
3. Arrangements for the hours during which work is performed
4. Overtime rates where applicable
5. Penalty rates
6. Annualised wages and salaries
7. Allowances
8. Details of leave, leave loading, etc.
9. Superannuation arrangements
10. Procedures for consultation, representation and dispute settlement

Currently there are just over 100 different awards in Australia, providing minimum standards for workers in those industries and occupations. Many of these awards provide the basic terms of an employment contract.

Enterprise agreements

An enterprise agreement provides an opportunity for employers and employees within a particular business or enterprise to negotiate a set of conditions that improve on the standards in an award. **Enterprise agreements** are collective agreements made at a workplace level between an employer and a union, acting on behalf of its employees, or between the employer and a group of employees, about terms and conditions of employment. In addition to the 10 National Employment Standards, enterprise agreements must include the following:

- a nominal expiry date, usually two or three years after the commencement of the agreement
- procedures for settling any disputes that might arise in the implementation of the agreement, including the right of employees to be represented in the dispute settlement procedure
- terms that allow for individual flexibility, so that arrangements can be made between the employer and individual employees
- provisions for consultation with employees on major workplace change.

BizFACT

Modern awards also have a 'flexibility term' that allows employers and employees to negotiate changes to some of the conditions in the modern award. These are called Individual Flexibility Arrangements (IFA). They allow an employer and an employee to come to an agreement that varies the modern award or enterprise agreement in order to address individual circumstances.

BizWORD

Enterprise agreements *are collective agreements made at a workplace level between an employer and a union, acting on behalf of its employees, or between the employer and a group of employees, about terms and conditions of employment.*



FIGURE 8.51 When two parties negotiate, they should bargain in good faith. This means they are to meet regularly, and discuss issues honestly and with a willingness to reach an agreement. Where an employer refuses to bargain, and the Fair Work Commission determines that there is majority employee support for pursuing an enterprise agreement, the Commission can force the employer to bargain collectively with the relevant employees.

Once the parties to an enterprise agreement have concluded their negotiations the agreement needs to be submitted to the Fair Work Commission for approval before it can commence operation. The agreement must be signed by the employer and the bargaining representatives acting on behalf of employees, to certify that the agreement has been entered into voluntarily by both sides. The Fair Work Commission will examine the detail of the agreement to ensure no unlawful content is included in the agreement and that the employees will be better off overall by entering into the agreement than simply being covered by the relevant award.

Enterprise agreements have the following advantages:

- consultation with and involvement of employees, which, if conducted successfully, results in greater employee involvement and empowerment
- possibility of improved pay and conditions, which can be tied to workplace performance
- greater flexibility by agreeing on conditions that suit both the employer and employee.

Enterprise agreements have the following disadvantages:

- more time consuming due to the need to conduct agreement meetings at the individual workplace level
- administratively more onerous, especially as the agreement must comply with all existing laws regarding employee rights and entitlements.



FIGURE 8.52 Negotiating agreements at the workplace level, where workers collectively bargain for better working conditions with their employer, is one way of improving working conditions, and can mean that both the employer and employee 'win'. Often employees negotiate to improve productivity in some way, in order to get better working conditions.

Individual common law contracts

Individual contracts exist when an employer and an individual employee negotiate a contract covering pay and conditions. These individual contracts of service cover employees who are not under any award or enterprise agreements. Individual contracts are more common at the professional and managerial level and apply to those who earn over $100 000. Such contracts are signed individually and are secret; that is, not open to public scrutiny.

Imagine all the students in your Business Studies class sitting down with your teacher and negotiating a set of working conditions for your class. Apart from the essential conditions, such as completing all the work and respecting each other's opinions, you might negotiate a homework-free month in return for one extra assessment task. You have just entered into an *enterprise agreement*.

Now imagine if your Business Studies teacher and you, after a period of negotiation, came to an agreement about your conditions of work for this subject. These conditions would apply only to you. The new contract would do away with the classroom conditions agreed to in the enterprise agreement. For example, the new agreement may offer you a 'classroom (employment) package' that includes more homework in return for the right to attend only two Business Studies lessons each week. You have just entered into a *common law individual contract*.

SUMMARY

- An employment contract is a legally binding, formal agreement between an employer and an employee.
- Under common law, both employers and employees have basic rights and obligations in any employment relationship.
- Employees are entitled to 10 minimum employment conditions, known as the National Employment Standards.
- An award is a legally binding agreement that sets out the minimum wages and conditions for a group of employees.
- Enterprise agreements are collective agreements made at a workplace level between an employer and a union, acting on behalf of its employees, or between the employer and a group of employees, about terms and conditions of employment.

EXERCISE 8.15 REVISION

1. **Define** the term 'employment contract'.
2. **What** are the obligations of both employers and employees?
3. **Identify** which categories of employees are entitled to benefit from the 10 National Employment Standards.
4. Select what you consider to be the three most important standards from the 10 National Employment Standards. **Justify** your selection.
5. **Define** the term 'award'.
6. **Recall** four of the ten matters that can be included in modern awards.
7. **Distinguish** between awards and enterprise agreements.
8. Select whether you would prefer to be covered by an award or an enterprise agreement. **Justify** your selection.

EXERCISE 8.15 EXTENSION

1. Find the modern award relevant to the retail or hospitality industry, or any other industry in which you or your classmates have part-time employment. The **Fair Work Commission** weblink in the Resources tab is a useful reference. **Outline** the key matters that are covered by this award.
2. **Investigate** workplace relations issues for young people. The **Young people at work** and **NSW Office of Industrial Relations** weblinks in the Resources tab are a useful starting point. Select a topic that interests you and **create** a brief report on what you learned.

on Resources

- **Weblink:** Fair Work Commission
- **Weblink:** Young people at work
- **Weblink:** NSW Office of Industrial Relations

8.6.5 Separation of human resources

Gone are the days when a person would commence their full-time working life at the age of 16 or 17, work for approximately 45 years, and then retire. Work patterns and business operations have undergone radical change over the past two decades and this has dramatically altered the movement of people into and out of jobs. Due to increased international competition, many businesses — large, medium and small — have been forced to restructure. As a result, there has been

a marked increase in the number of voluntary and involuntary redundancies being offered.

Separation is the ending of the employment relationship. There are many reasons why employees separate from a business. However, it is possible to classify the different types of separation into two broad categories: voluntary and involuntary (see figure 8.53).

BizWORD

Separation *is the ending of the employment relationship.*

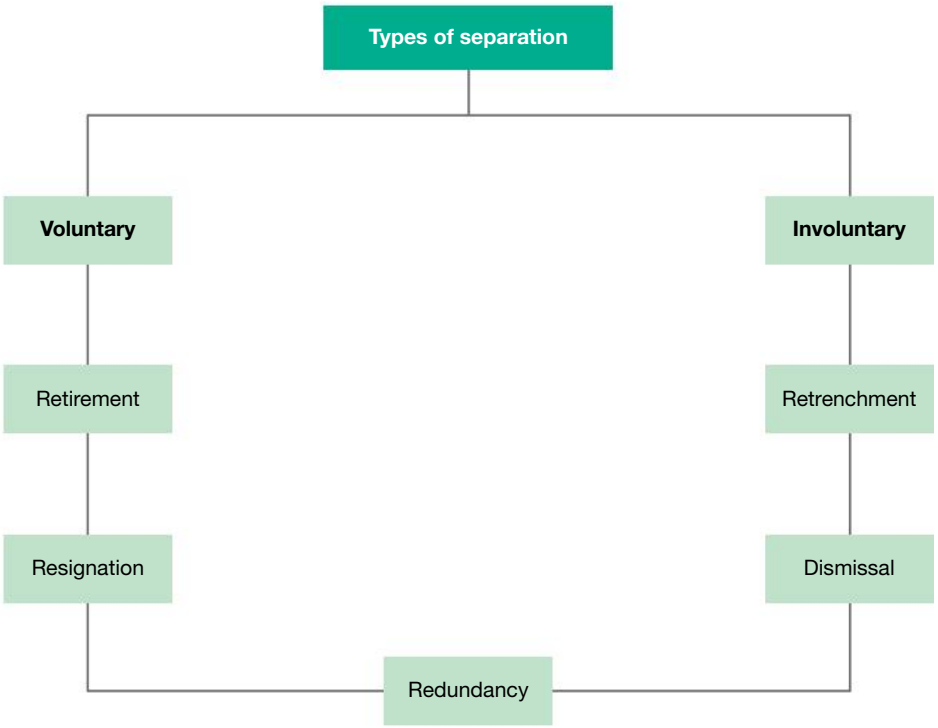


FIGURE 8.53 Separation — voluntary and involuntary

BizWORD

Voluntary separation *occurs when an employee chooses to leave the business of their own free will.*

Retirement *occurs when an employee decides to give up full-time or part-time work and no longer be part of the labour force.*

Resignation *is the voluntary ending of employment by the employee 'quitting' their job.*

BizFACT

Today, the national average time an employee remains with the same employer is 3.3 years (3 years and 4 months). If this plays out consistently, and assuming that people start their working life at 18 and are retired by 75, they will have 17 different employers in their lifetime. Based on statistics showing that most employees will work in three different jobs before upskilling or changing career, this means they will also have about five separate careers in their lifetime.

Voluntary separation

Voluntary separation occurs when an employee chooses to leave the business of their own free will. There are three different forms of voluntary separation: retirement, resignation and redundancy.

Retirement

Retirement occurs when an employee decides to give up full-time or part-time work and no longer be part of the labour force. Until the mid 1980s, it was common for men to retire once they reached 65 years of age and women 60. Since changes to legislation in the 1990s there is now no 'official' retirement age. People now have a choice at what age they would like to retire. A trend that has started to emerge in recent years is for people to retire 'early' — that is, in their mid to late fifties. How businesses have approached employee retirement has also changed. Today, many organisations provide advice and assistance to employees to help them prepare for retirement.

Resignation

Resignation, or 'quitting', is a voluntary ending of the employment relationship. People resign for a variety of reasons including:

- offer of a promotion with another business
- to start their own business
- boredom with their present job
- change of lifestyle.



FIGURE 8.54 An employee may leave a business for many reasons. This results in significant costs for the business. As a general rule of thumb, it costs 40 per cent of the annual salary of a departed worker to replace them.

Usually the employee needs to give the employer sufficient notice of his or her intention to resign. The length of notice varies from job to job, ranging from a few hours for casual employees to a month for some permanent employees.

Whenever a business wants to downsize, that is decrease the size of its operation, it will not fill vacancies that have come about due to retirements and resignations.

Redundancy — voluntary and involuntary

Redundancy is when a particular job a person is doing is no longer required to be performed, usually due to technological changes, a merger or acquisition. Therefore, unless the existing employee can be retrained for another job, they will be made redundant. Redundancy can be either voluntary or involuntary.

Voluntary redundancy occurs when the business wishes to reduce either the size or nature of its workforce and decides how many employees should be 'let go'. Employees are then informed of the situation and given the opportunity to nominate themselves for voluntary redundancy. Employees who choose voluntary redundancy are offered a redundancy package: a payout of a sum of money. If not enough employees volunteer, then the business may be forced to decide which employees will be made redundant — involuntary redundancy.

Involuntary separation

Involuntary separation occurs when an employee is asked to leave the business against his or her will. Apart from involuntary redundancy, the two different types of involuntary separation are retrenchment and dismissal.

Retrenchment

Retrenchment is sometimes called redundancy, but there is a subtle difference between the two terms. Redundancy occurs due to the permanent elimination of some jobs, because organisational or technological change has removed the need for those particular skills. Retrenchment is employee termination due to lack of sufficient work to keep the employee fully occupied.

BizFACT

Laszlo Bock, the Senior Vice President of Google's People Operations and author of Work Rules!, *has claimed that most companies don't know how to hold on to their best people. According to Bock, 'people don't stay for the money', they stay for two main reasons: the quality of the people they work with and the feeling that the work they do is meaningful.*

BizWORD

Redundancy *occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition.*

BizFACT

In 2017, the ABC announced that between 150 and 200 positions would be made redundant due to a major internal restructuring of the company. The company is moving towards a flatter structure by reducing the layers of management, as well as the number of divisions. They therefore want to increase the number of staff for whom each of the remaining managers will be responsible. Middle managers and supervisors will therefore bear the brunt of the redundancies. The money saved will be used to pay for a $50 million content fund.

BizWORD

Involuntary separation *occurs when an employee is asked to leave the business against their will.*

Retrenchment *is when a business dismisses an employee because there is not enough work to justify paying him or her.*

Retrenchment is a cyclical phenomenon tied closely to the level of economic activity. The end result of both retrenchment and redundancy is that the employee is out of a job.



FIGURE 8.55 Staff made redundant through the introduction of new technologies should be treated with sensitivity.

Dismissal

There will be occasions when the behaviour of an employee is unacceptable and it then becomes necessary for a business to terminate the employment contract of an employee. This is called **dismissal**.

The most serious form of dismissal is *summary dismissal* — when an employee commits a serious breach of their employment contract. For example, an employee who is drunk at work or is found to have engaged in criminal activity may be summarily dismissed. If an employee is given a summary dismissal, no notice is required. Another form of dismissal, referred to as *dismissal on notice*, is when an employee is not performing the job satisfactorily. Poor performance may be identified during an appraisal or performance process. The amount of notice (or payment given in lieu of notice) will vary depending on a number of factors, such as whether the employee is governed by a particular award or contract, the age of the employee and how long they have worked for the employer on a continual basis.

Selecting staff for dismissal can be risky and requires awareness of legislation and industrial agreements to avoid litigation and industrial action. Employees must be given proper notice and employers must comply with procedures established in law, including the unfair dismissal laws in the Fair Work Act 2009. To avoid misunderstandings, written warnings and/or notice is preferable. Written confirmation of resignation is also preferable to verbal statements made in the 'heat of the moment'. This way, a lengthy unfair dismissal case can be avoided.

Unfair dismissal occurs when an employee is dismissed by their employer and they believe the action is harsh, unjust or unreasonable. This is an issue of which both employers and human resource managers need to be aware.

BizWORD

A **dismissal** *is when the behaviour of an employee is unacceptable and it then becomes necessary for a business to terminate the employee's employment contract.*

BizFACT

Vicky Oliver, author of Bad Bosses, Crazy Coworkers & Other Office Idiots, *named the fake sick day as a major reason bosses fire their employees.*

BizWORD

Unfair dismissal *occurs when an employee is dismissed by their employer and they believe the action is harsh, unjust or unreasonable.*

An employee who believes they have been unfairly dismissed may lodge an unfair dismissal claim with an industrial tribunal such as the Fair Work Commission. When determining whether a termination is lawful, harsh, unjust or unreasonable, the Fair Work Commission will take into account the procedures followed, whether the grounds were reasonable, the circumstances of the business, whether human resources expertise was available, whether the employee was provided opportunities to respond or have a support person, and any other matters they deem relevant.



FIGURE 8.56 In 2016, a cleaner who was fired for having a cup of coffee on the job won an unfair dismissal case in the Fair Work Commission. One night, the cleaner arrived 45 minutes early for his shift and had a cup of coffee while waiting for his shift to start. Two days later, he was summarily dismissed by his employer, Glad Group Pty Ltd, who characterised the coffee drinking as theft. The Commission awarded the cleaner $9187.20 in damages and the right to get his old job back, after concluding the dismissal was 'unjust and unreasonable'.

BizFACT

In 2016–17, 11 160 cases were brought before the Fair Work Commission for conciliation. Of those, 8880 cases were settled and the employee was awarded compensation, reinstatement and/or a non-monetary remedy. In the same year, there were 1457 cases that went to arbitration. Of those, 196 cases were settled.

Case study: Unfairly dismissed for rescuing a kitten

In August 2012, the Fair Work Commission found that a cleaner who found a kitten at her work and gave it to a friend was unfairly dismissed for doing so. Judith Montague was working as a cleaner at student accommodation in Carlton, Victoria when she found a kitten that Melbourne City Council workers had been attempting to rescue from a drain. She had been led to believe that she would be allowed to keep the kitten if it escaped. However, when it was discovered she had taken the kitten, council workers were upset she had done so, which resulted in her employer dismissing her.

The Fair Work Commissioner pointed out that Ms Montague's employer had failed to follow the Small Business Fair Dismissal Code by not issuing a warning before dismissing her. He found the dismissal to be 'harsh, unjust and unreasonable' and ordered the employer to pay $3940 to Ms Montague.

The employer had offered Ms Montague two weeks' pay in lieu of notice, and had later increased it to five weeks' pay. Ms Montague pointed out that she had barely worked since the dismissal, and had few prospects of gaining new employment.

SNAPSHOT



"He found the dismissal to be "harsh, unjust and unreasonable" …"

SNAPSHOT QUESTIONS

1. **Why** was the dismissal of the cleaner considered to be 'harsh, unjust and unreasonable'?
2. Do you agree with the decision of the Fair Work Commissioner? **Justify** your answer.
3. **Outline** the outcome of the case.

SUMMARY

- The final stage in the employment cycle is the 'separation stage', in which employees leave the workplace on a voluntary or involuntary basis.
- This stage must be handled carefully and sensitively by the human resource manager.
- Voluntary separation occurs when an employee decides to give up full-time or part-time work and includes:
  - retirement
  - resignation
  - redundancy.
- Involuntary separation occurs when an employee is asked to leave the business against their will and includes:
  - retrenchment
  - dismissal
  - redundancy.
- Unfair dismissal occurs when an employee is dismissed by their employer and they believe the action is harsh, unjust or unreasonable.

EXERCISE 8.16 REVISION

1 **Distinguish** between voluntary and involuntary separation, giving examples of each.

2 **Construct** a concept map outlining the different types of voluntary and involuntary separation.

3 **Recall** some of the entitlements of employees who are made redundant.

4 **Distinguish** between summary dismissal and dismissal on notice.

5 **Identify** which of the following scenarios would most likely lead to summary dismissal.

(a) Todd bribed another employee not to tell their manager that he had been accessing pornographic websites during office hours.

(b) Roberto arrives for work entirely drunk. He has just been out to see a client, driving a company car. It's the third time this week he has arrived in such a condition.

(c) Jazmin's not very good at her job. She frequently makes mistakes and doesn't have the knowledge or skills to perform the job satisfactorily.

6 **Recall** three dismissal situations that would be classified as unfair.

7 In 2016, employees of Fairfax across Sydney and Melbourne were informed that 82 redundancies needed to occur. At the beginning of the year, the company said that initially the redundancies would be voluntary. However, in May, up to 30 Fairfax journalists lost their jobs and were forced into redundancy after the company failed to meet their targeted job cuts through voluntary redundancies.

(a) **Explain** the impact both the voluntary and involuntary redundancies would have on staff and the company.

(b) **Predict** why Fairfax may have had to make employees redundant.

8 Refer to the table below to answer the questions that follow.

Unfair dismissal, conciliation — results

Result type	Total 2016–17	2015–16
Total settled	**8800**	**8529**
Settled: Monetary	1660	1712
Settled: Monetary and non-monetary	5511	5122
Settled: Non-monetary	1627	1624
Settled: Reinstatement	42	35
Settled: Reinstatement and monetary	23	17
Settled: Reinstatement and non-monetary	13	11
Settled: Reinstatement, monetary and non-monetary	4	8
Not settled	**2280**	**2321**
Total resulted conciliations	**11 080**	**10 850**

Source: https://www.fwc.gov.au/termination-of-employment/unfair-dismissal/remedies

(a) **Identify** the number of total settled cases in 2016–17.
(b) **Identify** how many people were reinstated back to their position as a result of conciliation in 2015–16.
(c) **Why** do you think reinstatement is not a common remedy in unfair dismissal cases?
(d) **Calculate** how many more unfair dismissal cases were conciliated between 2015–16 and 2016–17.

EXERCISE 8.16 EXTENSION

1 **Compare** voluntary and involuntary departures in terms of:
(a) how difficult each is for the business
(b) effects on the business
(c) effects on staff leaving
(d) effects on staff remaining.

2 Termination management is about managing the final phase of the employment cycle, when the employee leaves. **Investigate** the issues a HR manager must be aware of when dismissing an employee.

3 Read about the following case and then answer the questions.

Natashia Frazer and Civic Printers

I had been employed by Civic Printers for 12 years. One month ago, my new supervisor warned me that if my work did not improve I may be dismissed. Prior to this I had only received favourable work reports.

One Friday afternoon I was told that someone else had complained about my performance and that I was being dismissed. I was not aware of any other complaint. I had never been given any written advice that my work was unsatisfactory. However, the supervisor's decision was final and I was dismissed. I think it is unfair.

(a) After reading the story have a class vote to **determine** whether Natashia's dismissal was fair or unfair.
(b) Now divide the class into small groups. Each group has to **determine** whether the termination of Natashia was fair or unfair, and then report back to the class. **Discuss** the different group responses.
(c) Take another vote to see if the discussion has made any difference to class members' views.
(d) **Synthesise** what you learnt from this activity.

8.7 Ethical business behaviour

BizWORD

Business ethics *is the application of moral standards to business behaviour.*

Ethics are standards that define what is acceptable and unacceptable behaviour. Ethics involves the study of moral issues and choices. It is concerned not with legal obligations but with what is morally right or wrong — and all the shades of grey in between. In many decisions involving ethical questions, it is sometimes difficult to give a definitive answer as to what is 'right' and what is 'wrong'. It often depends upon the individual circumstances surrounding the situation. **Business ethics** is the application of moral standards to business behaviour.

Most businesses want to engage in ethical business practices; to act honestly and morally. These businesses will honour commitments, not engage in misleading or deceptive product descriptions and will provide a safe working environment for their employees.

Not all businesses have adopted such an outlook. Some business owners still regard ethical business practices as a waste of money, the cost outweighing any benefits. They will often attempt to justify their behaviour as 'smart business practice' or 'everyone does it, why shouldn't I?' And like most questions of ethical behaviour, not all the answers are a simple 'black' or 'white' response.

Some businesses have become involved in lengthy and very expensive court cases, which attempt to resolve particular situations that are often centred around a number of ethical issues or socially responsible actions. This frequently results in a deal of negative publicity and a deterioration in the business's reputation. Other businesses have faced consumer boycotts and a deterioration in their reputation due to their unethical practices (see figure 8.57).



FIGURE 8.57 In 2013, the Rana Plaza building in Bangladesh collapsed, killing 1134 garment workers and injuring many more. The horrific event once again shed light on the questionable behaviour of over 150 international brands, which source the cheapest possible garment suppliers on the planet, ignoring crimes inflicted on the impoverished workers. The collapse was caused by a complete disregard of health and safety standards. Subsequently, many consumers boycotted the retail outlets that were sourcing garments from Rana Plaza suppliers.

The majority of business owners, however, regard the cost of ethically and socially responsible actions as a necessary expense — they make such a commitment an essential part of their business operation. They take a great deal of pride in the reputation their business has established and wish to protect its good name. These businesses want to be seen as responsible corporate citizens, conscious of the high standards expected of them by their customers and society at large (see the following Snapshot).

Case study: Pennicott Wilderness Journeys — operating sustainably

Pennicott Wilderness Journeys, which operates cruises and days tours from Hobart, was planned with the intention of operating sustainably, in harmony with the environment and the local community. The ultimate goal of this business is to use its financial success 'to reinvest into the local community and the environment that we live and work in'.

The company, which was founded in 1999 and is operated by Robert Pennicott and his family, has a very strong focus on sustainability. It attempts to employ members of the local community and source services from local businesses. Twenty-five per cent of the profits from the business are donated to local, national and international conservation, community fundraising and humanitarian projects. All of the tours are 100 per cent carbon offset and its energy use, water consumption and waste output are assessed through the EarthCheck system. All the business's products have achieved Advanced Ecotourism certification.

It is no coincidence that the business has won many awards, including the Qantas Award for Excellence in Sustainable Tourism for 2012, 2013 and 2014. Their Bruny Island Cruise also won Australia's Best Tourist Attraction in 2014 and 2015.

Pennicott Wilderness Journeys is now planning to expand the business further. A Wilsons Promontory Cruise, departing from Tidal River, will soon open. The venture is expected to cost $3.5 million and produce $9.7 million in economic benefits for the local community each year, as well as create 16 jobs for the region. More jobs will be created over the next five years and the project will also directly contribute to the conservation of Wilsons Promontory. The expansion was made possible with a $650 000 Federal government grant.

Mr Pennicott says that Wilsons Promontory is well known from the land but few people have experienced the same beauty from the sea. 'We're honoured to have the opportunity to operate cruises that showcase Wilsons Promontory. We understand how important it is to work with the community and together help protect it for future generations. Sustainability is at the heart of everything we do and we will work hard to ensure this venture operates with environmental best practice,' he says.

SNAPSHOT QUESTIONS

1. **Outline** what Pennicott Wilderness Journeys does that makes it socially responsible.
2. **Assess** the impact being socially responsible has had on Pennicott Wilderness Journeys.

SNAPSHOT



'Sustainability is at the heart of everything we do …'

Businesses that take their social and ethical responsibilities seriously are often 'rewarded' with improved business performance. Many businesses today are very much concerned with reporting on the **triple bottom line**. This means that they are no longer simply focused on making a profit at all costs; but rather, they recognise that environmental and social performance are also important.

Sustainability expert John Elkington coined the term 'triple bottom line' and argued that there should be three bottom lines:

1. The 'profit' bottom line, which is a measure of the traditional 'profit and loss' financial bottom line
2. The 'people' bottom line, which is a measure of how socially responsible a business has been
3. The 'planet' bottom line, which is a measure of how sustainable and environmentally responsible the business has been.

A growing number of small businesses today, such as Etiko, exist purely for socially responsible and ethical reasons. Etiko is a small business based in

BizWORD

Triple bottom line *refers to the economic, environmental and social performance of a business.*



FIGURE 8.58 When consumers purchase products with the Fairtrade mark, they are supporting farmers and workers in developing countries. The mark shows people that the Fairtrade ingredients in the product bought have been produced by small-scale farmer organisations that meet internationally agreed Fairtrade social, economic and environmental standards.
Source: © Fairtrade

Ferntree Gully, Victoria, with a strong commitment to ethics and the environment. Etiko sources products from international suppliers who produce **Fairtrade** certified items and/or are sweatshop free (see the following Snapshot).

Like individuals, businesses are frequently confronted with ethical dilemmas. What does a business do:

- with a loyal, long-serving employee who cannot adapt to new technology?
- with confidential information about a competitor's pricing policy that a disgruntled employee leaked?
- when it is asked for a cash payment to help hasten a decision about a tender contract?
- when a competitor engages in unethical business tactics that allows it to offer a cheaper product?
- when it outlines a promotion plan for an employee but later is unable to follow through with the plan?

These are just a few of the ethical challenges that confront business owners and managers. How they respond to these situations will have long-lasting consequences for the image and reputation of the business, as well as the behaviour of employees. It is important for business owners and their managers to have high personal and ethical standards so employees perceive the importance of ethical considerations.

BizWORD

Fairtrade *is a trading partnership that seeks greater equity (fairness) in international trade. It promotes the rights of marginalised workers, especially in low-income countries.*



FIGURE 8.59 Gloria Jean's Coffees ensures that it purchases resources from suppliers that look after their employees and the environment. Its coffees contain a percentage of beans from farms that have been certified by the Rainforest Alliance. The company's coffee beans are sourced from all over the world and from farms of a variety of types and sizes — large plantations, cooperative groups and tiny family farms.

Much of the evidence that 'good ethics is good business' is anecdotal. However, when James Burke, the former head of US company Johnson & Johnson, looked at the performance of a select group of companies committed to best ethical practice, he found that their stock value had increased by 11.3 per cent over a 40-year period. Over the same period, all other stocks increased in value by only 6.2 per cent on average.

Case study: Etiko — corporate social responsibility

The founder of Etiko, Nick Savaidis, believes that businesses should make a positive contribution to society. Etiko is a small business based in Victoria that planned for corporate social responsibility from the outset. Mr Savaidis started the business when he realised that it was impossible to purchase sports products that came with full guarantees that no employee exploitation was involved in production.

Etiko sells fashion, footwear and sports equipment that are made using offshore labour in a carefully chosen factory in Sri Lanka. Etiko fully integrates the principles of sustainability from all perspectives: economic, environmental and social. The company combines socially responsible production practices with environmentally sound materials to produce a range of products that are Fairtrade certified and sweatshop free. However, purchasing products that are manufactured in a socially responsible manner means that Etiko must pay up to three to four times the price that other fashion brands pay for their products.

Mr Savaidis wants Australians to know that they can buy a range of socially responsible fashion items, from t-shirts to underwear and even footwear. He says: 'No-one likes the idea of wearing clothing that is potentially made with child, sweatshop or slave labour. However, the reality is that most people in Australia have got wardrobes full of items made by people, young and old, who have been exploited … simply because we as consumers want cheap fashion. Our brand proves that it is possible to put social and sustainable values into the market and succeed.'

It is no coincidence that Etiko has won many awards in the area of corporate social responsibility, including an Australian and New Zealand Fairtrade Product of the Year award in 2013. Etiko has set the bar high for upholding and campaigning for human rights and achieved the top rating – an A+ for ethical production every year since 2013 in the Australian Fashion Report, which assesses measurements such as the supply chain, worker pay and welfare. From the sales of its products, Etiko helps to fund community development, microcredit and healthcare programs in many developing countries. They have also supported the human and labour rights of cotton growers and rubber tappers, workers in apparel, sports ball and shoe production, and their families and communities in India, Sri Lanka and Pakistan.

Etiko received a $75 000 Impact Investment Readiness Fund grant from NAB at the end of 2015, which it hopes will support the further growth of the business. The company has plans to export and will invest in marketing and distribution to be able to compete against larger retailers.

SNAPSHOT QUESTIONS

1. **Identify** the factors that motivated Mr Savaidis to establish Etiko.
2. **Outline** the ways in which Etiko demonstrates corporate social responsibility.
3. **Discuss** the impacts of Etiko's socially responsible strategies on communities and on the business.

SNAPSHOT



'Etiko fully integrates the principles of sustainability from all perspectives …'

8.7.1 Ethical issues

Within the business world, the following ethical issues regularly occur.

Fairness and honesty

Businesses must obviously obey all laws and regulations. As well, society expects businesspeople to tell the truth and avoid using misleading or deceptive information. Employees expect to be dealt with honestly and fairly. If, for example, a business promises a promotion to an employee, then the business should honour this commitment to the employee (except in exceptional circumstances). Customers and suppliers also expect to be treated honestly and fairly in all their business dealings. If, for example, a business arranges for a delivery of certain items and promises to pay within a set time, then the business should honour this commitment to the supplier.

Respect for people

If business owners treat their staff with respect, then you would also expect employees to act ethically.

Occasionally, a business may become aware of an unethical practice of an employee. This can place the business in a difficult position, especially if the employee is important to the successful operation of the business. At other times, an employee may be placed in a difficult ethical position by other employees — for example, when older employees decide to play a practical joke on a young apprentice. Sometimes, these practical jokes get out of hand and may develop into a serious harassment or negligence case. Other serious workplace ethical issues may involve a situation where confidential information is not kept secret, obligations are not fulfilled or subtle forms of discrimination occur.



FIGURE 8.60 A recent case was brought to a local court in Melbourne, in which a 19-year-old pizza delivery man charged his employer with assault. The manager allegedly locked him in the freezer, tied him to the bonnet of his car while driving, sprayed a fire extinguisher towards him and hit him in the head. In court, the manager defended his actions, claiming they were part of the teenager's 'initiation' into the company. The manager was found guilty, fined $650 and placed on a 12-month good behaviour bond.

BizWORD

A **conflict of interest** *occurs when a person takes advantage of a situation or piece of information for his or her own gain rather than for the employer's interest.*

Conflict of interest

Conflict of interest occurs when a person takes advantage of a situation or piece of information for his or her own gain rather than for the employer's interest. Such conflicts can often occur when gifts or payments are offered. There is a fine line between what is regarded as a gift and what may become a bribe. Corruption undermines the integrity of the business and, if unchecked, infiltrates the workplace culture.

Once a pattern of corruption takes hold and is seen to be acceptable behaviour, it quickly becomes entrenched within the business. Changing the attitudes and practices of individuals within such a business is extremely difficult. What start off as small incidents to which most people turn a blind eye may soon develop into corruption on a grand scale. When such corrupt practices are eventually exposed, the business's image will be severely damaged.

Financial management

Businesses have ethical and legal responsibilities in relation to financial management. In recent years, unethical practices have been highlighted and increasingly questioned. There are growing calls for codes of behaviour to regulate the activities of businesses in relation to financial management.

It is generally accepted that financial management decisions must reflect the objectives of a business and the interests of shareholders. An area in which ethical considerations are important is the valuing of assets.

In preparing budgets, a business estimates its expenditures and revenues. The common practice of overestimating expenditures and understating revenue to allow for unexpected and uncertain events is an ethical issue for an organisation.

All financial records should be regularly audited. Internal and external **audits** assist in guarding against unnecessary waste, inefficient use of resources, misuse of funds, fraud and theft.

BizWORD

*An **audit** is an independent check of the accuracy of financial records and accounting procedures.*

Truthful communication

Advertising can represent real ethical dilemmas. False or misleading advertising is not only unethical, it is also illegal. Terms such as 'special', 'sale', 'low fat' or 'light' can be misleading. For example, what precisely does the word 'special' mean when it is displayed above a product for sale? Most consumers would take this to mean the item is for sale at a cheaper than normal price; however, this may not necessarily be the case. The business owner may interpret the word 'special' to mean that the product has a distinct or particular character, that it can perform a particular function or it is different from what is ordinary or usual. The two interpretations can easily be confused. If the businessperson uses this word attempting to knowingly mislead customers, it would be classified as unethical behaviour. If the businessperson wants to advertise the fact that the product is available at a bargain price, then the words 'on special' would have a clearer meaning.



FIGURE 8.61 Marketers sometimes use words so ambiguous that the consumer will assume the advertiser's intended message. These 'weasel' words — deliberately misleading or ambiguous language — are by their nature vague and allow the marketer to deny any intention to mislead or deceive.

8.7.2 Encouraging ethical business behaviour

It is not always easy to maintain a consistently high degree of ethical behaviour in the real world. Employees who want to act ethically sometimes find it difficult to do so, especially if unethical practices are ingrained into the workplace culture.

One strategy that can be implemented to encourage ethical behaviour is to devise a **Corporate Code of Conduct**. This is a set of ethical standards for managers and employees to abide by.

Many businesses now document and distribute their codes of conduct or core values in order to provide internal stakeholders with ethical guidelines for work-place behaviour and practices (see figure 8.62).

BizWORD

*A **Corporate Code of Conduct** is a set of ethical standards for managers and employees to abide by.*



FIGURE 8.62 In 2015, clothing retailer Cotton On was forced to defend its directions to employees, after it was revealed that their employees are required to follow a code of conduct that includes vague concepts of being 'fun' and 'keeping it real'. According to some reports, Cotton On employees potentially face disciplinary action, which may include warnings, counselling or instant dismissal, if they are found to be engaging in 'unacceptable conduct', including not following the retailer's values.

Training may be given to employees to ensure they understand the values of the business. Most businesses also establish formal proceedings for reporting unethical behaviour in the workplace.

SUMMARY

- The majority of businesses want to be seen as responsible corporate citizens.
- The triple bottom line refers to the economic, environmental and social performance of a business.
- Ethics are standards that define what is acceptable and unacceptable behaviour.
- Business ethics is the application of moral standards to business behaviour such as:
  - fair and honest business practices
  - decent workplace relations
  - conflict of interest situations
  - accurate financial management
  - truthful communication.
- A corporate code of conduct encourages ethical business behaviour.

EXERCISE 8.17 REVISION

1. **State** the benefits of managing a business in an ethical and socially responsible manner.
2. **Explain** whether it is ethical for your school authorities to monitor student email usage on the school's computer resources.
3. 'Everyone cuts corners in business. It is the only way to survive.' **Discuss** this statement.
4. **Identify** the three components that make up the triple bottom line.
5. **Distinguish** between ethical and unethical behaviour.
6. **Recall** what James Burke's research revealed.
7. **Construct** a concept map outlining the five main ethical issues constantly faced by business.

8 **Discuss** what you believe to be the most ethical way to behave in the following situations and then **compare** your answers with other class members. Discuss any similarities or differences.
   (a) A customer is unaware that you have accidentally overcharged her. Do you inform the customer and give back the money or keep it yourself?
   (b) Your boss has told you not to record all the cash payments so as to reduce his taxation payments. Do you comply with these instructions? As an employee, what difficult position have you been placed in? How could you justify your decision?
   (c) A disgruntled employee from your main competitor offers to provide you with confidential information from that business's marketing strategy. Would you accept such information? Give reasons for your answer.
   (d) An employee is suspected of misusing the business's internet facilities. However, the employee is the best salesperson in the business, generating thousands of dollars worth of sales each year. How should the employee be dealt with?

9 (a) **Define** the term 'conflict of interest'.
   (b) In small groups, **propose** some possible strategies a business could use to minimise conflict of interest situations arising.

10 **How** can a code of conduct help encourage ethical business behaviour?

11 **Identify** what is required for a code of conduct to work successfully.

EXERCISE 8.17 EXTENSION

1 **Extrapolate** how socially responsible and ethical business practices might increase a business's sales and profit.

2 **Create** a list of five principles that could be included as part of the code of conduct for your school.

3 You have been contacted by Spencer Manufacturing Limited to assist in the development of a Corporate Code of Conduct. **Create** a series of guidelines that can be incorporated into a code of ethics for the business. Share your guidelines with other class members.

4 'Improving a business's ethical performance depends on the values of its managers and employees, and the business's culture.' **Analyse** this statement.

5 'Ethical business practices do not just happen: they are carefully planned and implemented. Such practices filter through the business. In return, employees are more loyal, committed and proud to work at such a business.' **Assess** the importance of business owners adopting ethical business practices.

6 **Examine** the ways the Fair Trade movement is committed to ethical trade and production practices.

on Resources

Weblink: Fair Trade

Digital doc: Chapter summary (doc-26100)

Interactivity: Chapter crossword (int-7225)

Interactivity: Multiple choice quiz (int-7226)

CHAPTER 9

Management and change

OVERVIEW

9.1 Introduction
9.2 What is organisational change?
9.3 Responding to internal and external influences
9.4 Managing change effectively

BizFACT

With many car manufacturers investing in some sort of vehicle autonomy, driverless cars could be around sooner than you think. For example, in 2017 Fiat Chrysler Automobiles (FCA) joined BMW Group, Intel and Mobileye to develop an autonomous driving platform for other car manufacturers to use. The partnership allows the companies to draw on each other's individual capabilities and resources.

9.1 Introduction

'The only thing that is constant in life is change.' Although these words were written around 2500 years ago by the Greek philosopher Heraclitus, they are as true today as they were then, especially in the world of business. For example, imagine the type of motor vehicle you will be driving in 20 years. It might look like the futuristic car shown below. You might even be able to take to the sky if there is a traffic jam. The motor vehicle industry has to effectively manage change due to dwindling oil supplies, stricter pollution controls, greater safety requirements and broader recycling legislation. Businesses only survive in today's highly unpredictable business environment if they effectively manage change. Businesses that embrace change will profit; businesses that resist change will be left behind.



FIGURE 9.1 Could this be the type of motor vehicle you will be driving in the future? Technology is constantly changing. So too is the world of business. Responding positively to these changes is often a recipe for long-term survival, because well managed changes can become the foundation for future growth and success.

9.2 What is organisational change?

In Australia, over the past decade, there has been extensive and unprecedented change in the business environment. There is every indication that the pace of change will intensify during this decade. The prevailing attitude in business today can be summed up as follows: 'There is only one constant in business and that is change.'

To help guarantee the long-term survival of the business, managers must respond to these changes. Hoping that the changes will either go away or have no impact on their business is a recipe for disaster. Managers also find it frustrating to learn that as soon as they adjust to one change in the business environment, they must readjust to accommodate another. Some managers are fearful of change, seeing it as a destructive force. Others perceive change as an opportunity for creativity and openly embrace it.

Change is any alteration in the internal or external environments; for example, change in consumer tastes, change in production methods, change in markets or products sold, or change in how employees perform their tasks. It could also be a change to the way things are perceived, or new ways of dealing with problems. In response to these changes, many organisations have undergone organisational change: the adoption of a new idea or behaviour resulting in a difference in the form or operation of an organisation over time. The organisation may have modified its corporate culture, implemented new organisational structures, recruited employees with new skills or developed different work practices.

BizWORD

Change *is any alteration in the internal or external environments.*

The rapidly increasing pace of change threatens to overwhelm many businesses. Adapting to change forced by the external environment is never easy for a business.

While change may be the most daunting challenge confronting management, the rewards are great for those who are prepared to accept the challenge and not only react to change but also initiate and manage it.

9.2.1 Managing change

As profitable opportunities can arise from change, it must be considered a fundamental aspect of a business's strategic planning. The ability to manage and, in many cases, embrace and adapt to change will increasingly determine a business's competitive advantage and survival. Successful managers are the ones who anticipate and adjust to changing circumstances rather than being passively swept along or, worse still, caught unprepared. Such people are **proactive** rather than **reactive**.

BizWORD

To be **proactive** *is to initiate change rather than simply to react to events.*

To be **reactive** *is to wait for a change to occur and then respond to it.*

The crucial management issue is *how* to manage change to make it as productive as possible, using it to renew and strengthen the business (see the following Snapshot). However, to be constructive, change must occur at a pace at which it can be absorbed and integrated by the business.

Also, all changes should be thoroughly evaluated to assess their overall impact. Poorly managed changes normally result in employee resistance, tension, anxiety, lost productivity and, ultimately, decreased profits. Managing change is especially difficult when the pace and nature of change is largely beyond the control of the manager.

Change entails risk and requires sound leadership skills and responsive management structures. The long-term survival of any business depends on the ability of its managers to scan the environment, predict future trends and exploit change. While change may be the most daunting challenge confronting management, the rewards are great for those who are prepared to accept the challenge.



FIGURE 9.2 Effective managers need to be proactive in dealing with change.

SNAPSHOT



'… change is a part of our lives — it's not an end in itself.'

Case study: Oxfam — how a leader should manage change

Dr Helen Szoke is the Chief Executive of *Oxfam Australia* and a leader and advocate in the fields of foreign aid, international development, human rights, and gender and race discrimination. With a career spanning the not-for-profit and public sectors, Helen has led Oxfam Australia and its staff of hundreds through several major change processes since taking the helm of the organisation three years ago.

In the lead-up to her keynote address at the 2016 Not-For-Profit People Conference in November, we spoke to Helen about leading teams through transformative change — the highs, the lows, and what you can learn from one of Australia's leading international aid and development NGOs to apply to your organisation's change processes.

Hi Helen, thanks for chatting with us! Oxfam has continued to engage staff and achieve organisational goals through a great deal of change in recent years. What are the changes the organisation has faced in your time as CEO?

Oxfam is part of a global confederation, which basically means that not only are we adapting for our own market, we're actually fitting in with what we're trying to do globally.

So it means that any change process is multi-dimensional, it's usually multi-time zone, and the drivers of change are sometimes drivers that we have to respond to rather than ones we make for ourselves.

I've seen change at a number of levels. We have massively improved planning processes to address the business cycle of the organisation and allow people time to know what is being asked of them.

We've also seen big changes in delegation, mandates and accountability. Each member of the leadership group now works hard at reducing the transaction costs by pushing decision-making down to the action level.

Another major change has seen us now focusing on leadership capability and supporting our middle managers — the culture holders of the group — to build their capability.

And what are some of the main things you did to lead your staff through those changes?

There are some very concrete things that we have to continue to do.

The first thing is to ask: 'Why do we need change?' What is the end point that is actually going to increase our impact as an organisation, and how is the change we're going to take you through going to enhance that?

The second is constant communication. I might have the responsibility for running a change process — it's one of the most important things I'm doing. But the staff who are impacted by the change process, the most important thing they're doing is delivering services, doing monitoring and evaluation, doing financial reports, or whatever the case may be. So there is the principle that you have to keep reinforcing communication on why and how, and what we're doing.

The third thing is to be sufficiently vigilant about the process you're using to enact change, and that you're actually living up to your own values. Things like making sure there's equity, there's not an unconscious bias in the process, that people are well-supported to give their best contribution to whatever new role might be coming up, and so on. That's really critical.

The fourth thing is to actually do it in a timely manner. Oxfam is probably like other NGOs in that because we have such smart, technically competent and engaged staff, I think at times we tend to over-consult. There are moments where I think staff really look at a leadership group and say, 'For God's sake, you're in that role to make decisions — just give me some clarity about the context I'm working in so I can get on with my job properly'.

So what's been the most challenging aspect for you of leading the organisation through change?

I think the most challenging aspect is that I have to deliver the message that change is a part of our lives — it's not an end in itself. And it's part of our lives because the context in which we're operating continues to change. It's part of our lives because we're continuing to try to remain relevant and legitimate as an international NGO so that we can have the sort of impact that we want.

We're also in a challenging market in a general sense, so in order for Oxfam to continue to be able to, for example, raise revenue or do the work we want to do, we have to be looking always to the long game and not the short game. In order to get the kind of change we want globally through our advocacy and policy, again, we have to not only be part of the global movement but we need to be saying, 'What are the implications for the change context we're operating in?'

So that's the most challenging thing — to bring the responsiveness to a change context into our day-to-day operation, and in the case of structural change or organisational change to really apply the principles I raised above.

Source: ethicaljobs.com.au

SNAPSHOT QUESTIONS

1. **Identify** the internal and external influences that have led to change at Oxfam.
2. **Outline** the strategies Helen adopts to lead her staff through change.
3. **Explain** the greatest challenges Helen has faced when implementing change.

SUMMARY

- Organisational change is the adoption of a business's new idea or behaviour in response to internal or external influences.
- The ability to embrace, manage and adapt to change will increasingly determine a business's competitive advantage.
- Successful managers are the ones who anticipate and adjust to changing circumstances.

EXERCISE 9.1 REVISION

1 **Define** the term 'change'.
2 **Explain** the meaning of the phrase, 'There is only one constant in business and that is change'.
3 **Account** for why some managers are fearful of change, whereas others openly embrace it.
4 **Distinguish** between proactive and reactive management.

EXERCISE 9.1 EXTENSION

1 Change is a continuous process, not an event. **Propose** an example from your own experience to illustrate the continuous cycle of change.
2 *Newspaper portfolio*
(a) Select four external influences that affect businesses. Over a 5- to 6-week period, collect four to five articles on each factor from newspapers, internet and journals.
(b) Paste the articles into a scrapbook under the four headings (influences). Ensure that you date and acknowledge the source of each article.

Reports
(a) **Create** four reports of approximately 150 words on each of the external influences. Use a business report style with subheadings, graphs and diagrams to support your text.
(b) Your responses should **synthesise** the theory obtained from your teacher and textbooks, with the information on current business conditions and influences from your newspaper, internet and journal articles.
3 Zoe could not understand why her team members were being so difficult. Couldn't they see that the changes she had made to the work roster would be to everyone's benefit? She thought they had all agreed to the changes when they were discussed at the last team meeting. She was not sure what to do next.
Consider your own experience of the difficulties in trying to predict how something will turn out. **Determine** what managers can do to reduce these difficulties.
4 Flatter management structures often result in higher levels of responsibility and accountability for all employees. Consequently, any organisational restructure that involves removing a layer of management will be perceived by employees as a major change. Assume you are the manager in charge of a restructure that will result in a flat management structure. **Determine** the advantages you would put forward in support of the restructure.

9.3 Responding to internal and external influences

It is said that if you stop moving, you die! The same applies to businesses. Businesses must keep responding to the never-ending pressure for change. Whether the influences driving change come from outside (external) or within (internal) the business (refer to chapter 3), changes to the business will occur. Such changes should be viewed as opportunities to be taken advantage of as opposed to challenges to overcome.

SNAPSHOT



Case study: Qantas and change

Change is inevitable. As a consequence, businesses must transform if they want to survive in today's dynamic business environment. One example of an Australian business that has had to constantly implement change is Qantas Airways Limited. Over the years, Qantas had to radically change its operations, marketing and business structure in response to internal and external influences including:

- global terrorism and increased security
- oil price increases

- fluctuations in the value of the Australian dollar
- increased competition from low-cost airlines
- rapidly changing technology
- trade union problems, especially with maintenance staff
- volcanic ash clouds that closed down European airspace
- an exploding engine that grounded the A380 Superjumbos.

Former Qantas CEO Geoff Dixon often used the phrase 'constant shock syndrome' with reference to the challenges that Qantas management and staff has had to effectively manage. The question for Qantas management is not whether to accept the challenge of change, but how to implement change effectively, how to make the change as productive as possible, and how to make it a process for revitalising and strengthening the business.

In 2014 QANTAS was faced with the task of cutting costs to save an estimated $2 billion. Qantas was successful in reversing its flagging financial performance and, with the cutting of around 5000 jobs, was able to implement the change that has returned it to a profitable position.

SNAPSHOT QUESTIONS

1. **Classify** each of the influences that have had an impact on Qantas as one of the external influences from the syllabus.
2. **Outline** what the questions and challenges are for Qantas in relation to change.
3. **How** did Qantas respond to change in 2014?

'Qantas had to radically change its operations, marketing and business structure …'

9.3.1 Internal influences

Management

Managers have the responsibility of operating a profitable or successful business. The poor financial performance of a business will result in management reviewing processes, staff and systems. For example, when Wesfarmers Limited took over the poorly performing Coles in 2007, management implemented a five-year recovery process. It updated the image of Coles supermarkets, rebuilt the supply chain and improved the freshness of its produce. Keeping costs under control is essential in turning around financial performance. As part of this, Coles introduced self-service checkouts in its supermarkets.

Businesses sometimes face a crisis. For example, a product sold by the business may be found to be unsafe or dangerous. Responding to such unplanned changes requires responsive decision-making from management to reduce the disruption to the business.

The role managers play in the operation of a business means they are key driving forces for change. In a small business, the manager may also be the owner and so the livelihood of the owner is tied very much to the ability of the business to change and maintain sales, profit, market share and its customer base. In a large-scale business, shareholders are seeking a return on their investment. Managers must ensure dividends are paid to shareholders and so a healthy profit is needed. Managers will push for changes that will lead to a better outcome and more efficient achievement of business objectives.

Employees

Employees working for a business expect to be paid fairly, trained properly and treated ethically in return for their vital contribution to production. Employees working in an innovative environment, where ideas are shared and acted on, are likely to recommend changes to policies, production processes or products. Companies such as Panasonic, Samsung, Sony and Toshiba have benefited from



FIGURE 9.3 In 2016, Joshua Brown was killed after neither he nor his Tesla Model S car's autopilot system detected a truck crossing the highway ahead of him. Tesla's CEO, Elon Musk, was bullish in his defence of the company following the death, even claiming that in the last year '500 000 people would have been saved' if the car's feature was widely available. His collection of social media posts reiterated that the accident was merely a 'statistical inevitability'. Experts are labelling Musk's behaviour in the aftermath of the crash as a 'case study' in poor crisis management.

employee creativity (see figure 9.4), enabling them to develop innovative products. This level of innovation within a business can create a need for change in everything from operations to marketing.



FIGURE 9.4 Ken Kutaragi, an electrical engineer at Sony, bought his daughter a Nintendo game console and was displeased with the quality of the gaming system. Sony wasn't involved in computer games at the time, but Kutaragi negotiated to keep his job at Sony while working as a consultant for Nintendo on their gaming devices. Kutaragi saw the market and business opportunity of computer gaming systems and pressed hard to convince Sony to enter the market. The CEO supported Ken's intrapreneurial abilities, which led to the creation of one of the greatest new business inventions in history, the 'Playstation'.

9.3.2 External influences

Competition

Businesses need to monitor the activities of their competition and determine what effect they may be having in the marketplace. Knowledge of such changes enables a business to make modifications to its existing business activities and to plan new ones.

Competitors can drive a business to change through a number of different actions:

- The opening of a new business that will compete with an existing business may cause the existing business to undergo change to stay current and relevant to their customers.
- Pricing policies by a competitor may lead a business to adopt a similar strategy. In recent years, both Coles and Woolworths have sold bread, milk and other staple items at greatly reduced costs in an effort to increase customer numbers. Once one business lowered prices, the other business quickly followed suit.
- The adoption of new technologies, both in production and products, can drive a competitor to change their products or processes. Toyota was the first vehicle manufacturer to introduce a hybrid model car. All major car manufacturers have now released their own versions.
- Advertising campaigns, sales and the development of an online presence are other examples of how competitors can drive change within a business.



FIGURE 9.5 In September 2017, CBA announced they would abolish their 'foreign' ATM withdrawal fees, due to their unpopularity among Australians. Within one day of announcing this change, the other three major banks followed suit.

Legislation

Whenever new laws are passed, businesses must comply with the new legislative requirements. For example, businesses had to alter their unfair dismissal practices in response to the new industrial relations laws implemented by the federal Government in 2009.

In another example, between 2012 and 2014, Australia was subject to a carbon tax. The tax was introduced in November 2011 and established a price on the carbon emissions of businesses in Australia. The pricing mechanism, known generally as the 'carbon tax', was intended as a measure to combat climate change and came into operation on 1 July 2012, but after much opposition, legislation to abolish this tax was passed in July 2014. Businesses had to make changes to respond to the legislation relating to the introduction and removal of this tax in both 2012 and 2014.

While most of us consider legislation to be a national issue, laws can be made by the state governments (for example, laws



FIGURE 9.6 Businesses regularly have to adapt to legislative changes. The carbon tax became a political issue between 2012 and 2014.







FIGURE 9.7 The assembly line was a great technological advancement when it was invented in the early 1900s. Subsequent advances in technology have improved it further, to the point where fewer and fewer human resources are needed. The development of self-serve checkouts has decreased the need for shop assistants.

relating to smoking in public, in the workplace and in cafes and restaurants) and by local councils (for example, parking restrictions, use of the footpath for seating and food service, opening hours for businesses and zoning laws).

Any law or by-law passed by these bodies may require a business to change some aspect of its operations.

Technology

A business that wants to be locally, nationally or globally competitive must adopt the appropriate technology. If it is slow to exploit technology, a business is likely to fail, because its competitors will strive to capture greater market share and develop a sustainable competitive advantage.

Technology allows a business to operate its processes and practices more efficiently and effectively, cutting costs and improving productivity. As such, technology, and any advances in technology, should be considered as a driving force for change.

All businesses, regardless of size, are able to take advantage of technology and so all businesses are driven to change by technology. Local milk bars introducing EFTPOS, couriers using electronic signatures, clothing stores using scanners and electronic security tags, and supermarkets introducing online shopping and self-service checkouts are all examples of technological advances that have driven change.

Social

Businesses operate within society and must adapt to changes in society's attitudes and values. Society's attitudes of what is right and wrong evolve over time and the values that are most important to people also change, affecting the ways in which businesses operate. Increased access to rapid communications has made the world's population more aware of what businesses are doing, for example in their supply chain. Pressure from society has forced businesses to implement procedures to preserve and protect the natural environment and to ensure their supply chain is ethical.

Society requires that large businesses sell safe products and treat staff with respect. Businesses today are also expected to contribute to society by returning something positive to the communities in which they operate. For example, as part of their 'Energy for Life' community program, AGL Energy helps to pay the winter energy bills for shelters for homeless people in New South Wales, Victoria and South Australia. This enables the emergency accommodation services to put funds back into the important work of supporting Australia's homeless.

SUMMARY

- Whether the influences driving change come from outside (external) or within (internal) the business, changes to the business will occur.
- Some of the internal influences that managers will need to respond to include management and employees.
- Some of the external influences that managers will need to respond to include competition, legislation, technology and social influences.

EXERCISE 9.2 REVISION

1 **Summarise** two internal influences to which businesses need to respond.
2 **Explain** how employees can influence a business to change.
3 **How** can competitors drive a business to change?
4 **Identify** a law that has recently been implemented and **explain** how this law has forced businesses to implement change.
5 **Identify** some examples of new technology that have led to changes in businesses.
6 **Why** are businesses that are slow to exploit technology likely to fail?
7 **Outline** some changes in society that have had an impact on businesses.
8 **Discuss** other internal and external influences, besides those mentioned, to which businesses need to respond.

EXERCISE 9.2 EXTENSION

1 **Investigate** a business that is being restructured as a result of changes in its internal environment. Business magazines, journals or the internet are an excellent source of information and frequently report on organisational restructuring in a variety of industries or businesses. Some recent examples of changes you may wish to explore include:
(a) e-commerce
(b) organisational alliances
(c) work–life balance.
2 Arrange to interview someone who has experienced a major change in his or her workplace. **Examine** and report on the impact of this change on the interviewee, his or her colleagues and the business's culture. Critically **analyse** how the change was managed.
3 **Investigate** a business that is undergoing change in response to an influence from the external business environment. **Evaluate** how that business is managing change.

9.4 Managing change effectively

Constant change has made the task of management more demanding and exciting than ever before. Change is the most daunting challenge confronting managers, as well as the most promising opportunity. Now well entrenched and likely to accelerate, change must be considered a fundamental aspect of a business's strategic planning.

Businesses often fail to manage change well. Their record tends to be poor because, in the upheaval of a restructuring process, employees — the most crucial group of all — are often neglected. As well, existing communication channels often break down in the highly emotional climate that surrounds a change program. Strategies to achieve successful change rely on communication, employee involvement in the change



BizFACT

A 2013 Change and Communication ROI Survey found that only 25 per cent of change management initiatives are successful over the long term. Why does organisational change usually fail? A study in 2016, 'Where Change Management Fails' by Robert Half Management Resources, found that most organisational change efforts fail due to ineffective communication.

FIGURE 9.8 Management researcher John Kotter maintains that the change management process consists of the following eight steps:
1. establish a sense of necessity
2. form a guiding group
3. create a vision
4. communicate the vision
5. empower people to fulfil the vision
6. recognise and reward achievements
7. consolidate improvements
8. institutionalise the changes.

Source: Photo by Caroline Kotter. Reproduced with permission of Professor John Kotter.

process, training, support and negotiation. Poorly managed changes normally result in employee resistance, tension, anxiety, lost productivity and, ultimately, unmet objectives.

Change entails risk and requires sound leadership skills and responsive management structures. The long-term survival of any business depends on the ability of its managers to scan the environment, predict future trends and exploit change. While change may be the most daunting challenge confronting management, the rewards are great for those who are prepared to accept the challenge. Change is inevitable. As a consequence, businesses must transform if they want to survive in today's environment.

SNAPSHOT



'The business needed to react to these competitive forces if it wished to successfully change …'

Managing change using Porter's Generic Strategies approach

Michael Porter is a US-born economist, researcher, author, adviser, speaker and teacher known for his theories on competition and competitive advantage. In the 1980s, he developed a theory that attempted to explain how businesses may manage change as they attempt to gain a competitive advantage over other businesses. The objective of gaining a competitive advantage is to improve performance in those areas identified as key performance indicators that are a source of change for a business.

Porter theorised that to gain a competitive advantage, businesses need to evaluate their strengths and act upon those strengths (a form of SWOT analysis). Porter identified five competitive forces exerting influence on a business. The business needed to react to these competitive forces if it wished to successfully change and gain a competitive advantage.

1. **The entry of new competitors**
   Markets that are profitable will always attract new businesses. These new businesses see an opportunity to make sales, earn a profit and expand their own areas of operation. The businesses that currently operate in these markets must be able to survive. Some of the existing businesses are able to survive because they have barriers that are difficult for new businesses to break down. These barriers include patents, economies of scale and supportive government policies, or the business operates in a market where the financial cost of commencing operations is prohibitive. If there are low barriers of entry, new businesses will enter the market and cause profits to fall. Businesses must always be prepared to deal with new competitors entering the market.
2. **The threat of substitutes**
   Some businesses operate in a market where close substitute products exist. Coke and Pepsi are often considered close substitutes, as are banks with regards to interest rates on home loans. In markets such as these, customers may switch to alternatives in response to price increases or changes to the quality of the good or service offered by the business. This reduces both the power of suppliers and the attractiveness of the market, because if new competitors can easily enter the market, businesses may find it difficult to build a solid customer base that will support longevity. This will also frighten suppliers, who thrive on guaranteed contracts to supply established businesses.
3. **The bargaining power of buyers**
   Businesses need to consider how powerful their buyers or customers may be. They need to assess how easy it is for buyers to drive prices down. This is driven by the number of buyers in the market and the importance of each individual buyer to the business. The business also needs to consider the cost to the buyer

of changing their supplier. Businesses with a few large buyers often find that the buyers are able to dictate the terms of their buying.

4. **The bargaining power of suppliers**
   The bargaining power of suppliers refers to how easy it is for suppliers to drive up the price of the item they supply to a business. This is driven by the number of suppliers of each essential input, the uniqueness of their product or service, the relative size and strength of the supplier, and the cost of switching from one supplier to another, which can be influenced by existing contracts and the time taken to undertake this change.
5. **The rivalry among existing competitors**
   The main driver of competition is the number and capability of competitors in the market. If a business is operating in a market with many competitors, most of whom are offering undifferentiated products and services, then a business may find they have a reduced market attractiveness.

The generic strategies approach

Recognising the competitive forces operating upon businesses, businesses that wish to gain a competitive advantage must concentrate on their strengths — in other words, what competitive advantage(s) does the business have?

Porter identified two categories of competitive advantage:

- cost advantage — a competitive advantage is gained through reducing or altering the costs of the business
- differentiation advantage — businesses gain a competitive advantage through differentiating their product or service from others in the market.

Porter's theory then states that there are two generic strategies that can be implemented to achieve competitive advantage. Porter's generic strategies are ways of gaining competitive advantage — in other words, developing the 'edge' that gets the business of the customer and takes it away from your competitors. These generic strategies are:

- **Lower cost strategies**
  These involve a business seeking to achieve the lowest costs in its industry. This allows the business to become more profitable as it can increase its margin — the difference between its costs and its selling price.
  There are three main ways of achieving low costs:
  - *Use assets efficiently*; for example, businesses should minimise idle stock on shelves and should not stock products that do not sell.
  - *Lower costs of operating*; for example, businesses could source supplies from cheaper suppliers, minimise wage costs, source cheaper utility suppliers and offer minimal packaging.
  - *Control the supply chain*; for example, businesses could seek contracts with suppliers and delivery businesses that guarantee prices. At the same time, they could implement stock management systems such as just in time, in order to reduce costs.
- **Differentiation strategies**
  Using a differentiation strategy, a business will make their product unique in some way in order to gain a competitive edge that will allow the business to market itself as a leader or innovator in that industry. Some strategies include making the product more durable, providing better support for customers, and offering extended warranties or different brands within the same market.

SNAPSHOT QUESTIONS

1. **Summarise** the five competitive forces identified by Porter.
2. **Identify** some of the barriers that make it difficult for new competitors to enter certain markets.
3. **Outline** the two categories of competitive advantage Porter identified.
4. **Distinguish** between a cost strategy and a differentiation strategy.

A manager can use a number of strategies to manage change effectively. Management of the change will be more effective if the business can:

- identify the need for change
- set achievable goals
- develop strategies to overcome resistance to change
- use management consultants.

9.4.1 Identifying the need for change

An effective manager should always be scanning the environment, attempting to understand factors that will have an impact on the business. In this way, he or she may better identify current trends and predict future changes.

BizWORD

*A **holistic** approach looks at the whole picture.*

Achieving such a vision requires a **holistic** view of the outside world and awareness of the potential impact on the business of a variety of factors. Correctly anticipating these factors greatly assists the manager in identifying the need for change. This strengthens the business so it may take full advantage of opportunities that favour its long-term survival in an increasingly competitive world. Sharing the vision with employees encourages them to better understand why the change is necessary.

To better understand what changes need to occur, a manager needs access to accurate and up-to-date information.

Business information systems

As a student you rely on measurements — subject marks and school grades — to assess your progress. This information allows you to determine what changes, if any, need to be made to your study pattern. Information is also crucial for any business. Actually, much of a business's success or failure to accurately identify what needs to be changed depends on its ability to collect, organise, process and retrieve information quickly. For example:

- an operations manager of a manufacturing business must collect data about production costs and production schedules
- a marketing manager must gather data measuring sales, product development and customer satisfaction
- a finance manager must collect data about financial transactions and measure cash flows
- a human resource manager must record staff absences, training requirements and overtime payments.

BizWORD

Data *are unprocessed facts and figures such as sales figures and customer complaints.*

Information *is processed data that have been deliberately selected and organised to be useful to an individual manager.*

*A **business information system (BIS)**, also referred to as a **management information system (MIS)**, gathers data, organises and summarises them, and then converts them into practical information.*

Consequently, a successful business must be able to gather, store, combine and analyse masses of **data** quickly and efficiently. Once processed and organised to be useful to an individual manager, this **information** becomes the raw material for decision making. Without it, a business would quickly lose its way because it could not accurately identify what needs to be changed.

Where do managers get the information they need? In most businesses the answer lies in a business information system. A **business information system (BIS)**, also referred to as a **management information system (MIS)**, gathers data, organises and summarises them, and then converts them into practical information to be used by managers who use them to make decisions.

Managers have to plan for the future, implement their plans in the present and evaluate the results against what has been accomplished in the past. Therefore, they need access to information that summarises future possibilities, the present situation and past performance. All this is part of a manager's role in managing change effectively.

9.4.2 Setting achievable goals

A **vision statement** states the purpose of the business. It indicates what the firm does and states its key goals. In conjunction with the vision statement, a business establishes specific company goals that are measurable (usually set on a yearly basis). Reassessment of the vision statement and business goals may be required if management detects changes in the external business environment that may have a major impact on business activities. However, for change to be managed effectively it is essential that any new goals be achievable. This means goals that are attainable and realistic. Unachievable goals will only cause cynicism among employees and damage relationships between employees and supervisors.

On the other hand, achievable goals, devised after consultation with employees and communicated clearly by management, have a much greater chance of being realised (see the following Snapshot).

BizWORD

*A **vision statement** states the purpose of the business.*

Dr Edwin Locke — a goal-setting theory

Dr Edwin Locke did research on goal setting and motivation during the 1960s. Dr Gary Latham, a Canadian researcher, experimented with and tested Locke's theories, producing research results that endorsed the strong connection between goal setting and workplace performance. In 1990, Locke and Latham published *A Theory of Goal Setting and Task Performance*, which further developed Locke's original proposals.

Locke and Latham identified five principles that should be applied when setting goals for employees. They can be summarised as follows:

- **Clarity.** Simply telling someone to 'do your best' or 'improve your performance' is not as effective as setting clear achievable and specific measures, such as 'improve sales by 10 per cent' or 'increase production output by 5 per cent'. Giving goals clarity means making them unambiguous and measurable. Goals should be simple, clear and as specific as possible. It is important that everyone understands what is expected, and the result that will be rewarded. A vague goal such as 'provide leadership to your work colleagues' has very little value as a means of motivation, because it does not include any specific actions that could be taken to achieve this. In addition, goals should be developed within a time frame, so there is a clear end date for the goal to be achieved. This will vary according to the nature of the goal.
- **Challenge.** People are often motivated by achieving something they have not successfully completed before. The opportunity to complete a task that is highly valued by the owner or management of a business can provide a level of challenge that can motivate an employee. The goal should extend the employee, but should still be achievable. There is no point in setting a goal that is beyond the capabilities of the employee, or that sets him or her up for failure. At the same time, a goal that is too easy, or does not seem to have much importance in the operations of the business, will not provide much in the way of motivation. The significance of the challenge should also govern the rewards available to the employee for successfully achieving the goal.
- **Commitment**. In order to ensure the employee will actively pursue the achievement of a goal, there must be a commitment on the part of the employee. While it is possible for the goal to be provided entirely by the employer or management, a goal into which the employee has had some input is more likely to serve as motivation. It is here that management styles can play an important role. A manager who adopts a participatory style will

SNAPSHOT



'… strong connection between goal setting and workplace performance.'

seek to give employees maximum input into the determination of appropriate goals. This does not mean that the employee decides the goal, but that it is negotiated between manager and employee, to achieve a balance between the objectives of the business and the particular strengths and skills of the employee. A consultative manager will also seek input from the employee. It is generally recognised that the greater the input from the employee, the more likely it is that the employee will commit to it. This means that a more challenging goal can be set, leading to greater rewards in the end. Increased rewards for achieving a goal will provide greater motivation for the employee to attempt the next goal.

- **Feedback**. An effective goal program must also include opportunities for feedback to the employee. Frequency of feedback can depend on the timeframe of the goal. Feedback provides opportunities to offer recognition for progress achieved, to make adjustments to the goal if necessary, and to ensure expectations are clear and realistic. Sometimes a goal can be broken down into smaller milestones to allow for progress to be measured along the way and achievements to be recognised. Feedback can be informal and may consist of little more than a catch-up over coffee. For longer term and more complex goals, formal feedback sessions may be necessary to ensure enough detail is communicated.
- **Task complexity**. While goals should be challenging enough to motivate employees, the level of complexity should not overwhelm them. It is important that any additional training that is required to assist the employee to complete the task is provided in a way that allows for genuine skill development over time. It is also important that deadlines and completion dates are appropriate for the task and the skill level of the employee. The aim of the exercise is to motivate the employee to contribute to the objectives of the business, and so every effort should be made to ensure that the process provides success for both the employee and the business.

SNAPSHOT QUESTIONS

1. **Explain** what is meant by 'clarity' when it comes to setting goals for employees.
2. **Why** do you think that setting goals that are easy to achieve might lower motivation?
3. **How** can management styles affect goal setting and motivation?
4. **Why** do you think feedback is important in goal setting?
5. **Why** is 'task complexity' an issue in the process of goal setting?

SUMMARY

- To manage change effectively requires the change to be as productive as possible; to make it a process for revitalising and strengthening the business.
- Managers must develop strategies for managing change effectively.
- Identifying the need for change and setting achievable goals are two strategies to manage change effectively.

EXERCISE 9.3 REVISION

1 **Recall** why an effective manager should continuously scan the business environment.

2 **State** why it is important for a manager to share the business's vision with employees.

3 **State** the purpose of a business information system.

4 **Account** for the importance of current and up-to-date information for a manager attempting to manage change effectively.

5 **Outline** why setting achievable goals can help managers implement change effectively.

EXERCISE 9.3 EXTENSION

Read the scenario below. In small groups, **create** a plan to solve the problems and effectively manage a potentially difficult introduction to new technology. Present your plan to the rest of the class.

Scenario
You are a divisional manager of 30 loyal, long-serving employees. Fierce competition is threatening the long-term viability of the business. Sales and profits are declining due to the lower prices of your competitor. The business could compete if it introduced new technology. (It has the finance to purchase and install the machinery.) The introduction of the new technology is going to mean changes to your division and the current product.

Twenty employees are required to work the new technology so 10 will become redundant.

Even though sales have declined, you have a number of very loyal customers who have expressed satisfaction with the format of the current product.

Problems requiring solution and action:

(a) Retrenching of 10 employees — examine some of the criteria you might consider regarding who should stay and who should go

(b) Training the remaining employees to understand and use the new and more complex technology (quite a radical change from the technology currently in use)

(c) Managing the change with sensitivity: maintaining positive workplace morale and exhibiting leadership

(d) Communicating the change in the product format to the customers and convincing them to maintain their loyalty towards your company and its brand.

9.4.3 Resistance to change

At the same time as managers are undertaking — driving — change for the best of reasons, there will be restraining forces working against the change, creating resistance.

Psychology has shown how difficult it is for individuals to change their behaviour; how difficult it is to eat less, exercise more, stop smoking or be more patient. Resistance to change is strong because for most people personal change is:

- achieved only with considerable effort
- often emotionally stressful.

Businesses, like individuals, also find some changes difficult to cope with. When the pace of change is very rapid or coming from the external environment, then businesses may experience open resistance to the change. For example, consider where you sit in your Business Studies class. It is likely that you and other students sit in the same seats for each lesson. Imagine now that your Business Studies teacher changes the seating arrangement and tells you where to sit. This new seating arrangement will be permanent. No prior warning or explanation of these changes was given. You and your classmates may react with a mixture of annoyance, irritation, frustration, anger or delight. Perhaps you would be angry or upset at not being consulted or involved in the rearrangement process. You may have felt that you had no control over what you regard as your working conditions and organisational structure. Many of you may view the changes as a threat to the status quo.

What does this tell us about resistance to change? This reaction is common among managers and employees. As individuals become accustomed to doing

BizFACT

'Employees who are not informed about why changes are necessary will ultimately resist such changes', says Hannah Russell, a change management consultant. 'When they do not get the information they need, they turn to the rumour mill with all its inaccuracies.'



FIGURE 9.9 A leader who can 'sell' the need for change automatically overcomes one of the main resistance points — that of 'why do we need to change?'

certain things and doing them in certain ways, so too do businesses. As a result, businesses and employees sometimes vigorously resist change.

The most common reasons why change may be resisted include:

1. *Financial costs.* A major reason for resistance to change is the financial cost of its implementation. Even with access to finance, a business contemplating change must weigh up the costs and benefits of the change.
2. *Purchasing new equipment.* The purchase cost of investing in new technology, plant or equipment can be considerable. Although this is expensive, there can be very significant advantages from making this investment. Prior to making the investment in new equipment, managers will need to weigh up the cost of purchase against the cost of leasing new equipment. David Jones, for example, recently upgraded its network of stores and spent $275 million to increase its floor space by over 20 per cent.
3. *Redundancy payments.* Employees who lose their jobs as a result of changes are entitled to financial compensation in the form of a redundancy payment. A redundancy payment is the money that is given to employees when they are forced out of work because their job skills are no longer relevant. Redundancy payments can be very high, especially if many employees are made redundant.
4. *Retraining.* When significant changes are introduced such as new technology, employees must be retrained. Retraining may be performed on the job or off the job.
5. *Reorganising plant layout.* When new equipment is installed, the layout of the plant may require reorganisation to improve efficiency and productivity. There can be high costs associated with reorganising the plant.
6. *Inertia.* **Inertia** refers to an unenthusiastic response to proposed changes. Some managers and employees resist change because it requires moving outside and away from their 'comfort zones'. Many employees and managers of the typical business desire a safe and predictable status quo. Such an attitude is summed up in the phrase, 'But we don't do things that way here'. Change can have a major impact on people. Feelings of lack of control, fear of the unknown and uncertainty about the future can lead to anxiety. The situation is made even worse if there is poor leadership and management during times of change.

BizFACT

Ironically, some people enthusiastically support the changes in public, but then ignore the changes in private. Management consultant Michael Hammer calls this deadly form of resistance the 'Kiss of Yes'. Why do you think people behave this way?

BizWORD

Inertia *refers to an unenthusiastic response to proposed change.*



FIGURE 9.10 Uncertainty about the future is a powerful emotion that can inhibit employees from embracing change. This is made worse if employees do not understand the reason for the change, or if they distrust the people, usually management, behind the change.

Force Field Analysis

Psychologist Kurt Lewin developed a useful model for understanding the change process. Known as Force Field Analysis, the model describes how you can determine which forces drive and which resist a proposed change. All businesses must deal with one constant reality of change: trying to balance the forces driving change with the forces opposing it. **Driving forces** are those forces that initiate, encourage and support the change. The main driving forces for organisational change are the changes in the internal and external environments, as outlined in chapter 3. **Restraining forces** are those that work against the change, creating resistance. The current conditions, or status quo, result from these two forces 'pulling' in opposite directions (see figure 9.11). Managers who are trying to implement a change must analyse the situation to identify and balance the driving and restraining forces.

BizWORD

Driving forces *are those forces that support the change.*

Restraining forces *are those forces that work against the change.*

Any business considering undertaking a new project or implementing change should consider the forces that are exerting pressure at the time. The first area to consider is the aspects of the business that could encourage or support the change, e.g. the people of influence or the systems and processes that are driving the project. Once those factors have been determined, the next step is to consider who and what is restraining the project. For example, some stakeholders of the business will want the status quo to be maintained; that is, they will not want the business to undertake any change. These stakeholders are restraining the change and will not consider any improvements or benefits that might result from the change.

Once management has identified and understood the main reasons why change is being resisted, i.e. the restraining forces, managers need to put in place strategies to reduce the resistance. These strategies seek to reduce or eliminate the restraining forces so the drivers can continue to strengthen the change and bring more drivers to the forefront of the change process.

A great deal of research has been conducted on the most effective methods to reduce resistance to change. Some strategies include:

- *Creating a culture of change*. The workplace culture can greatly affect employee acceptance of change. Since significant change can be quite daunting, there needs to be a supportive environment that reduces fear of change.

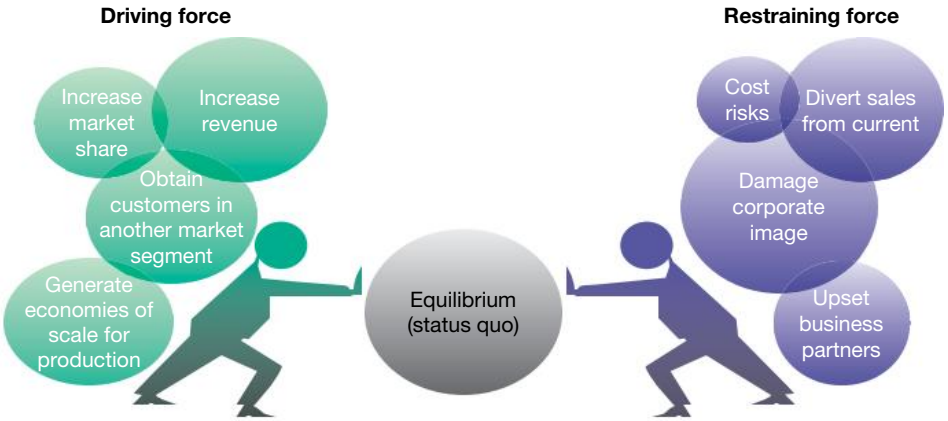


FIGURE 9.11 Driving and restraining forces work against each other, making it difficult for a business to change.

BizWORD

A **change agent** *is a person or group of people who act as catalysts, assuming responsibility for managing the change process.*

BizFACT

'Employees who are not informed about why changes are necessary will ultimately resist such changes', says Hannah Russell, a change management consultant. 'When they do not get the information they need, they turn to the rumour mill with all its inaccuracies.'

- ***Change agents***. The business should identify an individual (or group of people) who are influential in the business to act as catalysts to help manage the change process. These people should help initiate, stimulate and facilitate the change effort within organisations. A change agent can be either internal to an organisation, e.g. a manager or employee, or external, e.g. consultants who are tasked with overseeing the change.
- *Effective communication*. Managers must be able to communicate with stakeholders regarding the need for change and the progress of the change. There should be open communication channels to assist in the transfer of information. Without clear communication regarding the change, there may be resistance.
- *Positive leadership*. How a manager treats his or her employees will largely determine their acceptance of, or resistance to, change. A manager who acts as a leader and has high expectations of employees' abilities to initiate and implement a change process will generally be rewarded with people who are willing to embrace the change. There may still be some points of resistance, but



FIGURE 9.12 Teamwork encourages a supportive culture, which lowers resistance to change.

this resistance can be productively dealt with because the employees believe they have the support and trust of their manager. Employees are generally more prepared to accept the risks involved with change if they feel their manager is concerned with their welfare. Managers who concentrate on the needs of their employees are the most effective, building high-performance teams that attain their objectives. Less effective managers tend to focus on tasks and are more concerned with meeting deadlines — that is, they display the natural characteristics of a manager, not a leader.

Figure 9.13 outlines some other effective strategies for managing change.

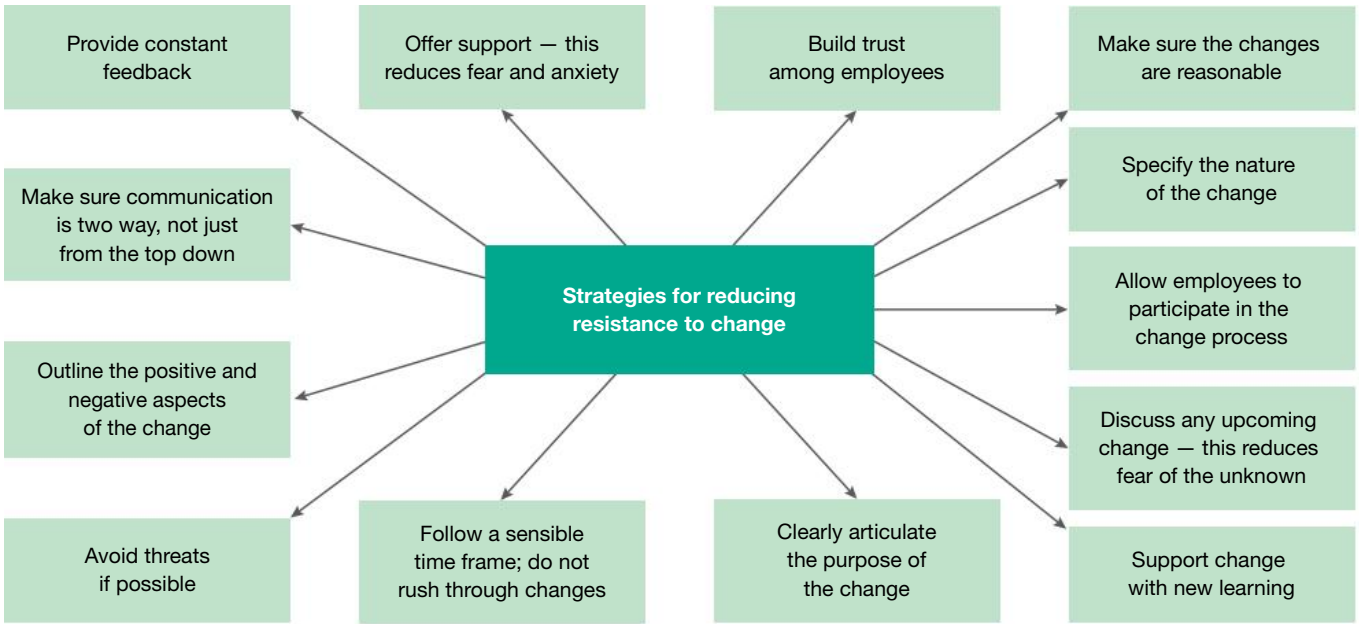


FIGURE 9.13 Strategies for reducing resistance to change.

9.4.4 Management consultants

As a student, if you have difficulty understanding some information within a subject, you will probably consult with someone who is an expert in that area. This could be another student, teacher or family member. This is similar to when you have a consultation with a doctor. You are seeking assistance from someone with specialised knowledge. Businesses also seek advice from **management consultants** who specialise in a diverse range of business-related areas, including risk management, brand protection, business set-up, executive recruitment and sustainability. Businesses hire the services of management consultants because they provide:

- a wide range of business experiences
- specialised knowledge and skills
- an objective (external) viewpoint
- access to the latest research
- awareness of industry **best practices**.

The main role of management consultants is to help businesses improve their performance by investigating existing business problems and developing plans for improvement. Consultants can be especially helpful in providing **change management** advice: a methodical approach to dealing with change, both from the perspective of a business and on the individual level. They can provide strategies to smoothly manage the introduction of business changes by:

- undertaking change readiness reviews
- creating a supportive business culture

BizWORD

A **management consultant** *is someone who has specialised knowledge and skills within an area of business.*

Best practice *refers to those business practices that are regarded as the best or of the highest standard in the industry.*

Change management *is a methodical approach to dealing with change, both from the perspective of a business and on the individual level.*

- actively involving all stakeholders in the change process
- gaining and recognising early achievements.

However, as in all aspects of life, the quality of advice from management consultants can vary. Therefore, it is best to hire those consultants who are members of the Institute of Management Consultants as their members have recognised standards of character, experience and education.

SUMMARY

- At the same time as managers are undertaking — driving — change for the best of reasons, there will be restraining forces working against the change, creating resistance.
- The main reasons for resistance to change include:
  - financial costs (the cost of implementing major changes can be substantial)
  - purchasing new equipment (this can also be expensive)
  - redundancy payments (if employees lose their jobs as a result of change, they are entitled to financial compensation)
  - retraining (when changes are introduced, some employees will require training)
  - reorganising plant layout (the layout of the plant may need to be reorganised if new equipment or technology is introduced)
  - inertia (some managers and employees resist change due to a fear of the unknown).
- Psychologist Kurt Lewin developed a useful model for understanding the change process. Known as Force Field Analysis, the model describes how you can determine which forces drive and which resist a proposed change.
- Driving forces are those forces that initiate, encourage and support the change.
- Restraining forces are those that work against the change, creating resistance.
- Resistance to change is common among managers and employees.
- According to Lewin's model, once management have identified and understood the restraining forces, managers need to put in place strategies to reduce the resistance.
- Two strategies for overcoming resistance to change include:
  - creating a culture of change (encouraging teamwork)
  - providing positive leadership (sharing the vision).
- The main role of management consultants is to help businesses improve their performance and assist with change management.

EXERCISE 9.4 REVISION

1 **Outline** why management and employees commonly resist change.

2 **Explain** how you would feel if your Business Studies teacher was replaced overnight without your knowledge and the new teacher taught very differently to your previous teacher.

3 **Distinguish** between 'driving' and 'restraining' forces.

4 Complete the sentences below by **identifying** the correct term from the following list:

cost	common	fear	effectively	financial
resistance	analysing	managers	strategies	retrained

When change is too rapid or when managers and employees feel they have no control over it, then _____ to the change is to be expected. Resistance to change is _____ among employees and organisations. The resistance needs

to be managed _____. Managers can fail to achieve change by not _____ the situation properly. Employees may resist change because of the _____of the unknown, the _____ costs involved and the need for some employees to be _____. _____ for reducing resistance to change need to be developed by _____.

5 **Outline** how the following can be a restraining force:
(a) lack of time
(b) poor timing.

6 Based on the information from this section, **explain** why there was so much resistance by bank tellers when they were first required to use computers to process customer transactions.

7 **Examine** figure 9.13. Select the two strategies you think are the most important. **Justify** your selection.

8 **Recall** the role of a change agent.

9 **Identify** the features found in a team that help others overcome resistance to change.

10 **Clarify** how positive leadership can help overcome resistance to change.

11 Select a major change in your life, such as moving house, changing schools or starting a new casual job, and complete the following:
(a) **State** the reasons you liked or disliked the change. Share your thoughts with other class members.
(b) **Identify** the reasons that were common among the group.
(c) **Interpret** what this tells you about the best strategy that a manager could use to help overcome resistance to change.

12 **Identify** the benefits of hiring a management consultant.

13 **Investigate** change in Pacific Brands over the last 5 years. The **Pacific Brands** weblinks in the Resources tab are a useful starting point. **Evaluate** the change the company has undergone and the role of leadership and management consultants in this change process. Write a brief report on the journey of Pacific Brands as the company reinvented itself.

on Resources

Weblinks: Pacific Brands

EXERCISE 9.4 EXTENSION

1 **Evaluate** the accuracy of the following quotes concerning change:
(a) 'Change for change's sake is not progress.'
(b) 'Change is life. Life is change.'
(c) 'Change what you can change. Accept what you cannot change.'
(d) 'Change is the new normal for leadership success.'

2 Think about a situation in which you would like to make a change but face some resistance. The situations might involve improving your Business Studies results, changing the arrangement of your timetable or having greater use of the family car.
(a) **Summarise** the status quo.
(b) **Propose** the situation as you would like it to be if you could change it.
(c) **Identify** the main driving forces.
(d) **Identify** the main restraining forces.
(e) **Determine** strategies for reducing the impact of the restraining forces.

3 Because of recent changes to the Work Health and Safety Act you must implement some new safety procedures. You know that some of your employees are going to regard some of these changes as ridiculous. **Propose** what you might do to get the employees to accept the changes.

4 '... the innovator has for enemies all those who have done well under the old conditions, and lukewarm defenders in those who may do well under the new.' Machiavelli (The Prince, 1532). **Evaluate** the accuracy of this statement.

on Resources

Digital doc: Chapter summary (doc-26101)

Interactivity: Chapter crossword (int-7227)

Interactivity: Multiple choice quiz (int-7228)

Business management

MULTIPLE CHOICE QUESTIONS

1. Which of the following would be classified as a social goal?
(a) To increase market share by 10 per cent
(b) To sponsor the local school football team
(c) To provide shareholders with increased returns
(d) To improve the training opportunities for employees

2. Refer to the following information for Question 2.

	$
Sales	150 000
Cost of Goods Sold	65 000
Expenses	42 000

What would the Net Profit be for this business?
(a) $43 000
(b) $127 000
(c) $173 000
(d) $257 000

3. Which of the following are both examples of current liabilities?
(a) Debtors and creditors
(b) Overdraft and debtors
(c) Creditors and overdraft
(d) Creditors and mortgage

4. What is a collective agreement made at a workplace level about terms and conditions of employment referred to as?
(a) Award
(b) Enterprise agreement
(c) Individual common law contract
(d) National Employment Standards

5. Refer to the following Balance Sheet to answer Question 5.

ASSETS	$	LIABILITIES	$
Current Assets		**Current Liabilities**	
Cash in bank	5000	Overdraft	3000
Stock	**(?)**	Creditors	4000
		Non-current Liabilities	
Non-current Assets		Bank loan	310 000
Building	350 000		
Equipment	17 000	**OWNER'S EQUITY**	
Furniture	13 000	Capital	84 000

What would be the value of the stock?
(a) 2000
(b) 4000
(c) 16 000
(d) 68 000

6. Fletcher & Sons Construction has developed a plan to guide the business over the next five years. What type of planning is this an example of?
   (a) Operational
   (b) Tactical
   (c) Technical
   (d) Strategic
7. What does the contingency approach to management emphasise?
   (a) Management as planning, organising and controlling
   (b) Management as leading, motivating and communicating
   (c) The need for managers to be reactive and respond to change after it occurs
   (d) The need for flexibility and adaptation of management practices to suit changing circumstances
8. A new furniture store has decided to stock their products through a few selective retailers. Which marketing strategy is this an example of?
   (a) Place
   (b) Price
   (c) Product
   (d) Promotion
9. Calculate the value of owner's equity given the following information: Liabilities = $75 000 and Assets = $145 000.
   (a) $70 000
   (b) $75 000
   (c) $220 000
   (d) $240 000
10. Shimmering Jewellery relies heavily on their sales assistants to promote their goods by outlining the benefits and features of their products to consumers. This has been successful in persuading customers to purchase their products. Which promotion technique is this an example of?
    (a) Publicity
    (b) Advertising
    (c) Personal selling
    (d) Sales promotion
11. Which of the following are both examples of involuntary separation?
    (a) Resignation and dismissal
    (b) Retirement and resignation
    (c) Dismissal and retrenchment
    (d) Retrenchment and retirement
12. A manager of a real estate agency always consults with employees when setting targets and making decisions. What type of leadership style would this be an example of?
    (a) Autocratic
    (b) Democratic
    (c) Diplomatic
    (d) Hierarchical
13. Beautiful Skin Pty Ltd has decided to produce a razor for women. It has calculated the total production costs for each razor and added a 15 per cent margin to set the final price. What pricing method is this an example of?
    (a) Cost-based pricing
    (b) Break-even pricing
    (c) Market-based pricing
    (d) Competition-based pricing
14. Michael is able to manage change in his business by always scanning the environment and attempting to understand the factors that will have an impact on the business. Which of the following best describes the method of managing change effectively used by Michael?
    (a) Setting achievable goals
    (b) Reducing resistance to change
    (c) Identifying the need for change
    (d) Utilising management consultants

15. A production manager inspects products at various points in the production process to check for problems. Which of the following best describes his approach to quality management?
    (a) Quality control
    (b) Quality assurance
    (c) Continuous improvement
    (d) Total quality management

SHORT RESPONSE QUESTIONS

1. 'To understand management today you must look at its history. Management approaches (theories) and schools of thought represent differing viewpoints and strategies for managing people, making decisions, organising workplaces and solving problems. Each offers something of value for today's manager.'
    (a) **Identify** three management approaches and **summarise** the main features of each. *3 marks*
    (b) **Explain** how these approaches could influence contemporary management practices. *6 marks*
    (c) **Analyse** the relationship between management approach and the types of business structure that a business could adopt. *12 marks*
2. 'Managers need a wide range of skills. The relative importance of these skills depends upon the manager's level in the business.'
    (a) **Identify** four management skills. *2 marks*
    (b) **Explain** how the quantity of the skills needed differs at each level of management. *5 marks*
    (c) **Determine** why it is important for a manager to acquire new skills. *10 marks*
3. (a) **Define** the term 'stakeholders'. *2 marks*
    (b) **Identify** and **describe** two possible conflicts that could arise between various stakeholders. *6 marks*
    (c) **Propose** possible strategies that managers could adopt to reconcile any likely conflicts of interest. *6 marks*
4. (a) **Outline** what is meant by the term 'effective management'. *3 marks*
    (b) **Distinguish** between 'good' and 'poor' management. *5 marks*
    (c) **Evaluate** the importance of good management to the business's overall success. *10 marks*
5. (a) **Outline** the role of managers when organising operations in a manufacturing-based business. *3 marks*
    (b) **How** can a business ensure that quality of outputs is maintained? *6 marks*
6. (a) **Define** the term 'marketing mix'. *2 marks*
    (b) **Outline** the three approaches a business can adopt when selecting a target market. *6 marks*
    (c) **Recommend** a marketing mix for a business you are familiar with. *10 marks*
7. (a) **State** the main role of marketing. *2 marks*
    (b) **Define** target market.
    (c) **Assess** the importance of each of the four Ps of the marketing mix. *10 marks*
8. (a) **Define** the term 'goal'. *2 marks*
    (b) **Identify** four business goals. *4 marks*
    (c) **Explain** how it can be difficult for a manager to achieve a mix of business goals. *4 marks*
    (d) **Assess** the importance of staff innovation, motivation, mentoring and training. *10 marks*
9. **Construct** an income statement and balance sheet in correct format using the following information. You will be required to **determine** profit and to use this figure to balance the balance sheet. *12 marks*

Sales	$400 000	Owner's equity	$45 000
Expenses	$300 000	Debtors	$12 000
COGS	$50 000	Mortgage	$60 000
Cash	$20 000	Land and buildings	$120 000
Stock	$10 000	Goodwill	$8 000
Creditors	$15 000		

10. (a) **Define** the term 'human resource/cycle management'. *2 marks*
(b) **Demonstrate** the four main elements of the human resource cycle. *6 marks*

11. (a) **Describe** the steps to be followed by the human resource department so the most appropriate applicant will be chosen to fill a vacancy. *3 marks*
(b) **Deduce** what problems could arise for a business if an inappropriate candidate was selected to fill a job vacancy. *6 marks*

EXTENDED RESPONSE QUESTIONS

1. In the following situation, **identify** and **explain** the management skills that could be used.

A dispute has arisen between the IT department and the accounting department regarding the introduction of a new computer invoice system. The accountant wants the new system introduced by the beginning of the new financial year, but the IT manager believes that the staff will not be sufficiently trained by then to use it effectively. You are the human resource manager in charge of this project and must negotiate agreement without further delay.

2. **Compare** the classical, behavioural and contingency management approaches. Study a business and **account** for how management theory has influenced the business's structure.

3. 'The only constant in business is change. The pace of change is accelerating, with change coming from both internal and external sources. How a business responds to these changes will ultimately determine its future.' **Critically evaluate** the strategies used to manage change effectively in a business you have studied.

4. Choose a real-life example of a manufacturing-based business and a service-based business. For each example, **outline** the inputs, processes and outputs of their operations.

5. 'An effective marketing mix is crucial if a business wants to increase its market share.' **Discuss**.

6. 'Marketing is a system of business activities designed to plan, price, promote and distribute something of value for the benefit of the customer at a profit.' With reference to a business you have studied, **discuss** and expand on this statement.

7. 'A thorough understanding of accounting and finance is essential for business managers'. **Identify** the three main financial statements and **discuss** their importance.

8. 'If a business wants to be appropriately flexible and responsive to market needs, then it should train all employees to be good at everything. That is, they should be experts in all aspects of each key business function. Generalists, not specialists, are required.' Is this a practical proposal? **Justify** this statement.

9. Imagine you are specialising in accounting services for a small business. Terry, one of your clients, runs a home maintenance business. He admits to you that he regularly offers a discount to customers who pay him in cash, so that he can keep his apparent profit as low as possible to avoid tax, and not have to declare every transaction on his BAS. **Explain** how you would try to convince him to maintain all his financial records in a socially responsible and ethical manner.

10. 'There are only two ways in which to create and maintain outstanding business performance. First, take exceptional care of the customer and, second, develop new products. It is that simple.' **Determine** how accurate this statement is. Give reasons for your answer.

TOPIC 3

BUSINESS PLANNING

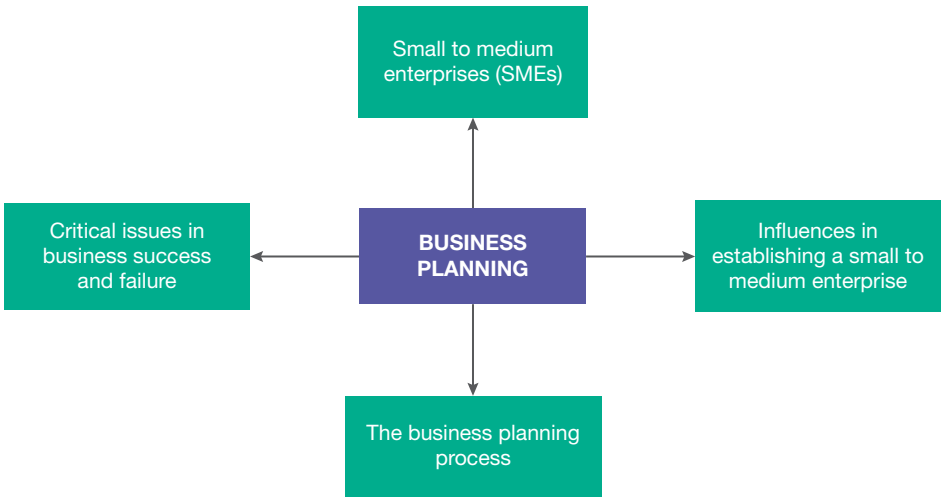
FOCUS AREA

The processes of establishing and planning a small to medium enterprise

OUTCOMES

Students should be able to:

- discuss the nature of business, its role in society and the types of business structure
- describe the factors contributing to the success or failure of small to medium enterprises
- assess the processes and interdependence of key business functions
- analyse the responsibilities of business to internal and external stakeholders
- plan and conduct investigations into contemporary business issues
- evaluate information for actual and hypothetical business situations
- communicate business information and issues in appropriate formats
- apply mathematical concepts appropriately in business situations.





Case study: Influences in establishing a SME — Mibu Medispa

Anyone who seeks to successfully establish a business will need to go beyond the good idea or business concept. Husband and wife team Steve and Violetta Kola are no strangers to running a business, having run a successful wardrobe and shower company for 20 years. Violetta's passion, however, has always been the beauty industry. After years of experience working in day spas and beauty salons, as well as being a distributor of beauty products, she always had the dream of owning her own medispa. In 2016, Violetta had an idea about beginning a new business that would be the first to offer world-class medical aesthetic treatments. 'I thought it was a great business idea, and I did my research and put together a business plan and thought if I don't do it now, someone else is going to do it.' This idea became a reality in 2017 with the opening of Mibu Medispa in Sydney's South West. Steve and Violetta's success has been built on their unique services, but these services alone would not have been for business success.

Mibu Medispa combines the latest medical technology and beauty procedures, together with traditional spa treatments. Since this would be the first business of this nature in the area, Steve and Violetta had to establish a new business from scratch. After the initial idea, they conducted extensive market research. They analysed the demographics of the area, which they found was a growing area with new homes and families. At this time, an ideal location became available for lease, so they jumped on the opportunity. They were persistent in securing the lease, as they considered it a prime location. The site had parking, was quite private, was already zoned commercial, was close to a shopping centre and enabled the business to gain exposure due to its visibility from a main road.

The next consideration was finance. Steve and Violetta decided to use a combination of debt and equity to fund their new venture. They sold their previous business and used the proceeds from the sale as equity. They then organised a bank loan for the remainder of the funds. The business also decided to lease some of their equipment to assist with their working capital management.

All businesses have to conform to a number of legal requirements, and these are important foundations for success. At the time of establishment, Steve and Violetta had to register the business name and hire an accountant to set up a private company. They also established a financial records system so that they could accurately meet their taxation obligations. Steve and Violetta then had to lodge a Development Application with their local council and ensure they complied with certain health regulations, such as the *Public Health Act 2010* and *Public Health Regulation 2012*. Failure to meet legal requirements can lead to prosecution and possible fines, which could both cripple the business financially and destroy its reputation.

'This idea became a reality … with the opening of their Mibu Medispa …'

Since this is a new business in the establishment phase of the business life cycle, potential customers have to be identified and made aware of the existence of the business and what it offers, so a marketing strategy is essential. In order to determine their prices, Violetta and Steve used a combination of both competition-based and market-based pricing (based on their market research data). Once the business was almost ready to launch, Violetta and Steve relied on online marketing to promote it. They created a business website and pages on social media, registered their business with a variety of local pages on Facebook, e.g. Macarthur and Camden Noticeboard, and set up an exclusive event page through Register Now to draw attention to their launch night. Prior to this night, where invited guests were given an opportunity to test the products and services, Violetta generated a lot of publicity via social media. Guests also received goodie bags and went in the draw to win free treatments. The mayor attended the launch, as well as friends, family and potential clients, and a few NRL players made an appearance. Violetta and Steve also ensure they provide the highest quality goods and services in order to take advantage of word of mouth, as they rely on repeat business from regular customers to drive growth.

Before opening, Steve and Violetta had to recruit and select qualified and professional employees. Prior to recruitment, they determined the exact skills and qualifications they were looking for and devised a job description and specification. In order to recruit staff, they placed an advertisement on Seek, as well as their social media pages and they sought the services of Aesthetic Recruitment Agency. They then used interviews to select potential employees. Mibu Medispa currently has four part-time employees, but as the business grows, additional staff may have to be acquired. Highly skilled and enthusiastic employees are also vital for business success.

CHAPTER 10

Small to medium enterprises (SMEs)

OVERVIEW

10.1 Introduction
10.2 Definition of SMEs
10.3 The role of SMEs
10.4 Economic contribution of SMEs
10.5 Success and/or failure of SMEs

10.1 Introduction

Small to medium enterprises (SMEs) are the 'engine room' of the Australian economy.

Governments at all levels have recognised the importance of SMEs and have devised appropriate policies to build on the strengths and overcome the weaknesses of these businesses. These policies focus on areas like access to finance, networking, delivery of government programs, innovation and export programs.

The more adaptive and dynamic SMEs have responded to this environment through increased spending on research and development (R&D), new product developments, improved business practices and an export-oriented business culture.

In recent years the SMEs in Australia have performed better than other sectors of the economy, even during the 2008–09 economic downturn. SMEs have created many new jobs, become more innovative and are increasingly entering overseas markets.



FIGURE 10.1 SMEs play a crucial role in the Australian economy. They are a major source of employment and their total output adds significantly to the economic growth and wellbeing of Australia.

10.2 Definition of SMEs

BizFACT

Turnover, asset values and market share are some of the criteria that have been used to determine whether a business is 'small'.

As outlined in chapter 2, establishing a clear-cut definition of a SME is no easy task. They are much easier to describe than define. Although there is no single universally accepted definition of a SME, a number of quantitative measurements (those based on statistical calculation) and qualitative measurements (those based on personal observations and a description of the business) can be used to determine whether a business is small or medium sized:

- number of employees
- type of ownership
- sources of finance
- legal structure
- market share
- management structure.

One of the most widely accepted quantitative measurements used to determine the size of a business is that devised by the Australian Bureau of Statistics (ABS). This measurement uses the number of employees as its benchmark (figure 10.2). Using these measurements, a SME is therefore a business with fewer than 200 employees.

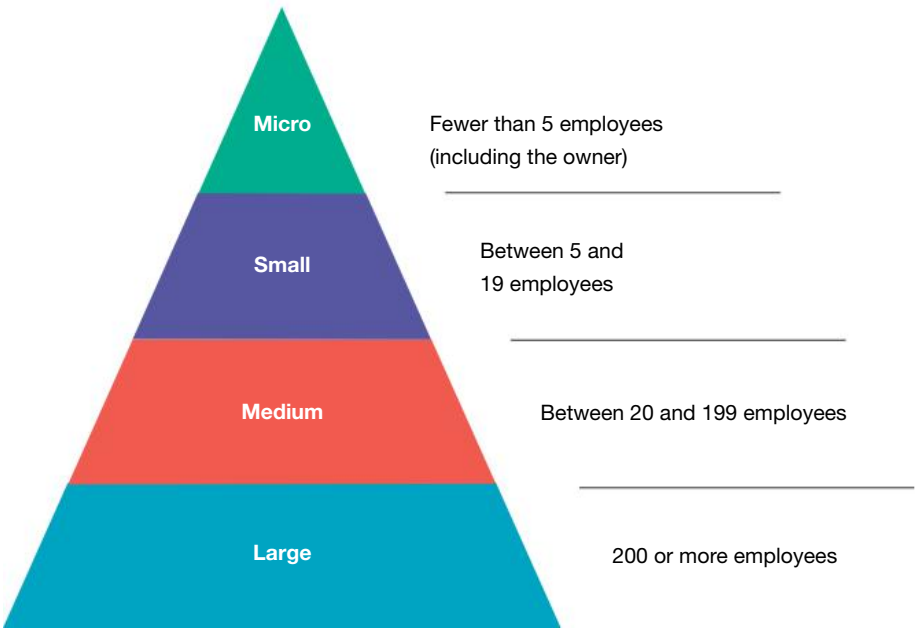


FIGURE 10.2 Australian Bureau of Statistics classification of business size

10.2.1 Common characteristics of SMEs

The definitions outlined above, and in chapter 2, have limitations. Studies have revealed the general public's narrow definition of the term 'small business'. The average person uses the term to refer to an owner-managed business that may employ a few people. It is best then to use a checklist of characteristics (both quantitative and qualitative) to determine the size of a business (see figure 10.3).

Many SME owners want to stay small to avoid the pressures and difficulties often experienced in larger businesses. They are content with the size of their business, especially knowing they can offer personalised service to their customers.

One such small business that has adopted this philosophy is Otaris Marketing (see the following Snapshot).

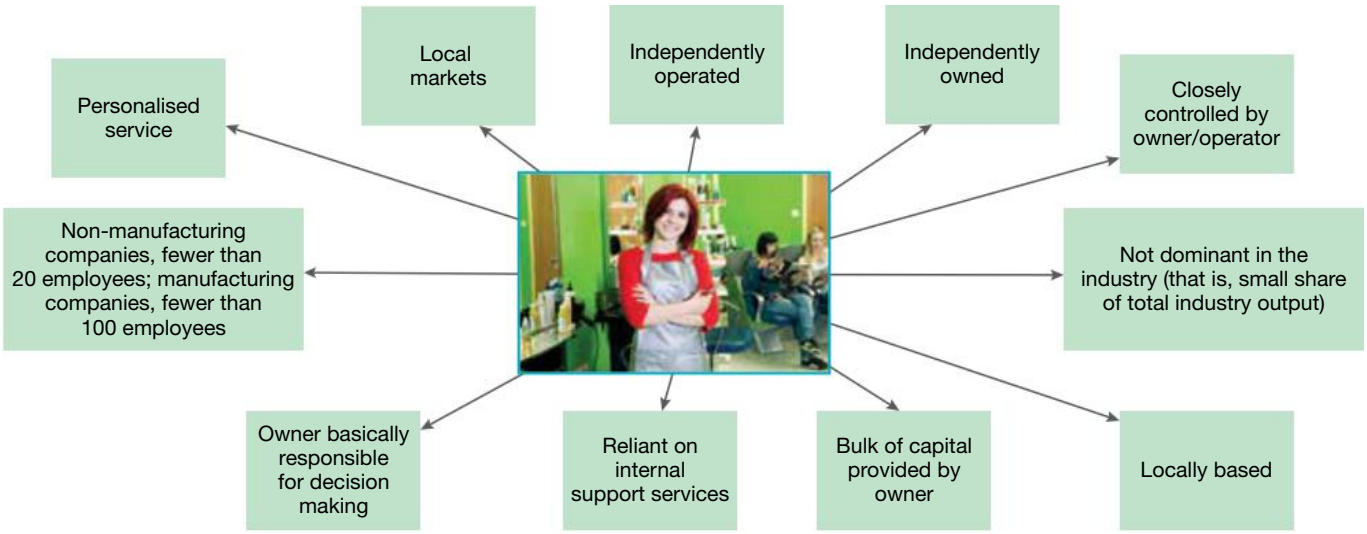


FIGURE 10.3 Common characteristics of a SME

SNAPSHOT



'… staying small isn't about settling for less …'

Case study: Otaris Marketing — keeping it small

After 15 years' experience working in large marketing companies, Melanie Williams started her own business in 2016. Her business, Otaris Marketing, is a boutique marketing agency that provides tailored digital and traditional marketing solutions for small to medium enterprises. Melanie decided to start her own business as it allowed her more flexibility and creativity in her marketing activities, with faster and more visible results. She found that corporate environments often entail large marketing teams, with multiple levels of approval required for each campaign. Therefore, what goes to market is often vastly different from the original creative concept.

Increased flexibility was a powerful motivator to starting her own business. 'As I need to generate new and creative approaches to make each campaign successful and unique, I need to be able to produce material at sometimes very unusual hours. Sometimes I get my best creative ideas at 3 am, sometimes during the afternoon. There are certain times of the day when I do best creating content, other times generating a client pitch, a performance report or utilising down time to do research or updating my skills. With my own business, I have the flexibility to get the very best out of each productive mood as I am not locked in to a strict 8 am–6 pm schedule.'

In business, there is a stereotypical assumption that the bigger the business, the better. However, this may not always be the best option for many business owners. There are many businesses that choose to stay small instead of growing, even if they have what it takes to be bigger. For Melanie, staying small isn't about settling for less; it's about building the company and the life that she desires. Her target market is small businesses who are either starting up or trying to make their way, often with limited budgets. 'The way I can provide them with a great product at a reasonable price is to cut out as many overheads as possible. And, when I think about getting "big", all I think about is increased overhead.' Melanie works from home and outsources what she can to other specialists like her so that she doesn't have to pay for overheads. 'The bigger you get, the less responsive you become. Sometimes it limits how creative and risky you can be, which can sometimes make the difference between a successful campaign and an average one.'

Small businesses, like Otaris Marketing, that can 'get big' with the help of contractors when needed and then 'get small' again after a large project is completed are agile enough to compete for all types of projects, yet are not burdened by the constant pressures that come with having a large business. 'The smaller you are, the less expenses, space and resources you need. Staying small allows me to put money back into the business, instead of spending it on things like monthly rent for a large workspace or employee salaries. By staying small, your overall cost of doing business will stay down as profits increase.'

Another advantage of staying small is that Melanie is able to provide a more personalised level of service. Being small means that she can devote more time to each client and really get to know their needs. She can then tailor her service and offerings to suit each client's requirements. This enables her to develop long-term relationships with her clients and thus secure repeat business. 'When you're smaller, you can really take your clients' needs into consideration and implement changes to your services that better meet their needs.'

SNAPSHOT QUESTIONS

1. **Outline** what motivated Melanie to start her own business.
2. **Why** does Melanie prefer to keep her business small?
3. **Outline** the benefits of remaining small.

10.2.2 The number of SMEs

According to the ABS in June 2016, SMEs account for approximately 99.8 per cent of all private sector businesses. However, it is difficult to provide an accurate count of the number of SMEs in Australia for two reasons. First, as was previously explained, there is no universally accepted definition of a SME. Second, the SME sector is extremely dynamic and changing daily. During a boom time in the economy, the number of SMEs increases rapidly. During a recession, business failures far outweigh business commencements.

According to ABS research, at June 2016 there were 1 917 960 micro businesses, 599 392 small business and 50 808 medium businesses in the Australian economy.

BizFACT

Between 2014 and 2016, the Australian economy added 27 000 net new micro businesses, or an average of just over 1000 per month. This category represented the highest growth; it grew five per cent over the two year period. The industries that experienced the most growth were education and training, real estate, construction, professional services, arts and recreation, financial services, accommodation and food.



FIGURE 10.4 Think of the SME business sector as a pool of water. New businesses enter the pool and increase its size. Others have difficulty staying afloat. They sink to the bottom, leak out and decrease the size of the pool. This means the composition and size of the pool is constantly changing.

It is important to remember that even though medium-sized businesses represent only about 2 per cent of all SMEs, they play an important role because of the large number of people they employ.

BizFACT

Eighty-four per cent of all small businesses are in the services sector. Account for the reasons for such a high percentage within this sector.

BizFACT

Over 99 per cent of all Australian businesses are SMEs. Ninety-six per cent are small and 3 per cent are medium.

10.3 The role of SMEs

By examining some of the main features of SMEs, their overall important role within the Australian economy can be seen. Australian small to medium enterprises:

- employ about 70 per cent of all the people working in the private sector (47 per cent in small businesses and 23 per cent in medium businesses)
- have created 80 per cent of Australia's employment gains during the past ten years
- produce approximately 50 per cent of all the products produced each year
- generate an increasing amount of our total exports
- account for 20 per cent of all money spent on R&D
- provide a wide range of products used by large businesses
- earn more profits and pay more taxes than do large businesses.

Although the individual efforts of each SME may appear insignificant, their total impact is enormous.

Owning and operating a SME can be challenging, rewarding and stimulating, as well as hard work. For those prepared to take the risk, and who finally make it, the sense of achievement and satisfaction is well worth the effort.

SUMMARY

- Small to medium enterprises (SMEs) are the 'engine room' of the Australian economy.
- According to the ABS, a SME is classified as a business employing fewer than 200 employees.
- According to the ABS, SMEs account for 99.8 per cent of all private sector businesses.
- The number of SMEs fluctuates over time according to the state of the economy.
- In recent years, SMEs have created many jobs, become more innovative and are increasingly entering overseas markets.

EXERCISE 10.1 REVISION

1 **Recall** what the letters SME represent.

2 **Distinguish** between quantitative and qualitative measurements used to determine the size of a business. Provide an example of each.

3 **Examine** figure 10.2. Complete the following statements by identifying the correct word from the choices given. Write the sentences into your notebook. According to the ABS:
(a) a business with fewer than *5/20* employees is classified as a small business
(b) a micro business has fewer than five employees *including/not including* the owner
(c) a medium business has between *20 and 199/100 and 199* employees
(d) a business that has more than *100/200* employees is classified as a large business.

4 **Examine** figure 10.3. Select the three characteristics you consider to be the most important and **justify** why you selected each one.

5 **Explain** why it is best to use a checklist of both quantitative and qualitative measurements to determine the size of a business.

6 **State** why many small business owners want to stay small.

7 **Outline** why it is difficult to provide an accurate number of SMEs operating in Australia.

8 **Discuss** why it is useful to think of the SME business sector as a pool of water.

9 **Explain** the relationship between the level of economic activity and the number of business commencements and failures.

10 **Identify** five important features that indicate the overall importance of the SME business sector to the Australian economy.

11 'SMEs are the "engine room" of the Australian economy.' **Justify** this statement.

EXERCISE 10.1 EXTENSION

1 **Contrast** the various definitions of 'small business'.
2 **Construct** a database of five small businesses in your local area. List the following:
   (a) the name of the business
   (b) whether the business is a manufacturing or non-manufacturing business
   (c) the number of employees
   (d) the turnover
   (e) the asset value.
3 **Evaluate** how useful these data are when attempting to define what a small or medium business is.

10.4 Economic contribution of SMEs

Before we can discuss SMEs' contribution to the economy, we must first gain an understanding of what an economy is. An **economy** is a system or way of organising what goods and services are produced, how we produce these goods and services, and how these goods and services are distributed. It's often easier to think about this concept if we consider what would happen if a small group of people were stranded on a deserted island. An economic system or way of doing things would have to be devised for all members of the community to survive. *What we produce* would be dependent on the resources available, such as raw materials (for example, fish from the sea), and *how we produce* would depend on our skills and available tools (for example, fishing rod and knowledge about how to best catch fish) to make that job easier. Perhaps, given there is a small group of people, goods and services produced (production) could be easily divided among all members of the community, therefore solving the question of *who production will go to*.

BizWORD

*An **economy** is a system used to determine what to produce, how to produce and to whom production will be distributed.*



FIGURE 10.5 Australia is a market capitalist economy, which means that it is an economic system in which decisions and the pricing of goods and services are guided by the exchanges between individuals and businesses in the economy. These economies work on the assumption that market forces, such as supply and demand, are the best way of determining what is fair for everyone in society. In a market capitalist economy, there is little government intervention or central planning.

In real life, an economy must answer the three basic questions of:

- what to produce
- how to produce
- who will receive the goods and services produced.

Many different economic systems have been used, but the type of economic system we have in Australia is called a *market capitalist economy*. This means that most answers to the economic questions are provided by private buyers and sellers.

Now that we understand what an economy is, let's consider how SMEs in Australia actually contribute to our economy.

BizWORD

Economic growth *occurs when a nation increases the real value of goods and services over a period of time.*

Gross domestic product (GDP) *is the total money value of all goods and services produced in Australia over a one-year period.*

10.4.1 Contribution to gross domestic product

Economic growth occurs when a nation increases the real value of goods and services over time. One common measure to check whether economic growth has occurred is to see whether our **gross domestic product (GDP)** has grown.

GDP is the total money value of all goods and services produced in Australia over a one-year period. The Australian Bureau of Statistics (ABS) estimates that SMEs contributed about 57 per cent of Australia's GDP. The total output of the country's diverse collection of SMEs, ranging from highly specialised professional and technical firms to the local corner store, makes a significant contribution to the national economy.

BizFACT

Between 2014 and 2016, 27 000 net new micro businesses were established and they alone delivered about 90 000 new jobs.

10.4.2 Contribution to employment

Employment keeps the economy healthy. Employed Australians will use the wage they have earned to buy goods and services to satisfy their needs and wants, supporting business and opening up further opportunities for job creation. SMEs employ around 7 million people, which represents about 66 per cent of total private sector employment (42 per cent are employed by small businesses and 24 per cent by medium businesses). During the last 20 years, the SME sector has been the major generator of new jobs in the Australian economy. During times of economic downturn, as was experienced between 2008 and 2009, the SMEs were more likely to try to maintain their existing employees compared with the large businesses.

In addition to providing employment, SMEs contribute to the revenue raised through taxation. Not only do they pay tax, their employees also pay income tax. Taxation is used to provide goods and services that may benefit the whole community, such as a better education system.

BizFACT

The balance of payments consists of two accounts, which are always in balance. The current account records transactions such as exports and imports, income and transfers. The capital and financial account records borrowing and lending transactions. Historically, Australia has recorded large current account deficits (CAD), often importing more goods and services than it exports. Over the last 20 years, however, Australian exporting industries have become more competitive in global markets.



FIGURE 10.6 Circus Oz is one of Australia's biggest cultural exports. They were a national finalist in the 2013 Australian Export Awards. Circus Oz has successfully exported its world-class, distinctly Australian work for the national and international stage and has been at the forefront of international touring by Australian performing arts companies since its foundation in 1978.

Source: Circus Oz

10.4.3 Contribution to the balance of payments

One of the most dynamic changes to the Australian SME business culture is the increasing awareness of the need to service overseas markets. Evidence of this is the fact that the number of SME Australian exporters is growing faster than large exporters. SMEs in agribusiness, manufacturing and professional services are all experiencing rapid export growth. Over the past two decades, the number of SMEs who have entered the global market has rapidly increased. Today, over

90 per cent of Australian exporters are SMEs and they earn almost 50 per cent of export revenue.

Exporting goods and services contributes to our balance of payments. The **balance of payments (BOP)** is a record of a country's trade and financial transactions with the rest of the world over time, usually one year. One way of maintaining a favourable BOP, as well as encouraging economic growth, is to export more than is imported. This is another crucial role for SMEs as they are often more successful at exporting than large businesses (see the following Snapshot). Many agree that the adaptability and flexibility of SMEs make them more responsive to the needs of overseas markets. The federal government is keen to promote export growth within the small business sector and encourages this with programs operated by Austrade.

BizWORD

*The **balance of payments (BOP)** is a record of a country's trade and financial transactions with the rest of the world over time, usually one year.*

Case study: Typefi Systems — honoured for export success

In 2015, Typefi Systems won the Australian Export Award for Small Business. Founded in 2001, Typefi provides a platform that allows people to publish content faster and in more formats.

The publishing platform can automatically render the source document in over 30 output formats for print, online and mobile in under three minutes. This enables clients to expand their product offerings across multiple platforms, while minimising costs and cutting production time by up to 80 per cent.

The versatility of its platform allowed Typefi to enter markets outside traditional publishing. The company's clients range from individuals to enterprise businesses and global organisations such as Apple, Penguin Random House, Pioneer, Lonely Planet, Cambridge University Press and the World Health Organization.

The company exports to 20 countries, with 90 per cent of its clients from overseas. Exports made up 84 per cent of Typefi's total revenue in 2015–16. Several projects with Apple during the year helped increase revenue by more than 40 per cent.

Typefi employs 40 people worldwide. Senior research and development engineers are based at the company's head office on the Sunshine Coast, and are supported by specialist developers in Europe and a growing team of engineers and support staff in Sri Lanka. Typefi also established a 24-hour helpdesk in 2016.

The judges commended Typefi's clear commitment to pursuing its goals through international business channels. 'The applicant is supported by a diverse workforce and robust and systematic approach to financial and risk management that likely contribute to its success. It adopts a highly client centric approach, tailored to individual market segments which appears to contribute to client retention.'

Source: Typefi Systems

SNAPSHOT QUESTIONS

1. **Outline** the factors that have contributed to Typefi's success.
2. **Assess** how exporting has impacted on this business.

SNAPSHOT



'… clear commitment to pursuing its goals through international business channels …'

on Resources

Weblink: Typefi

10.4.4 Contribution to invention and innovation

Small to medium enterprises are the main source of most inventions and innovations in Australia. An invention is the development of something new. Innovation occurs when something already established is improved upon. Many successful businesses are built on these two forces. SMEs have produced many new products that we take for granted. This is because SMEs generally display a consistently positive attitude towards innovation. They constantly research, develop and test new ideas and products. Many SMEs are built on product innovation.

Invention and innovation are at the heart of our economy. Finding new ways to do things has resulted in improved efficiency and increased productivity. Over the past ten years, SME spending on research and development (R&D) has almost

trebled in real terms. Research and development is a set of activities intended to develop new ideas and improvements in production. Around 40 per cent of SMEs are actively engaged in some form of innovation. According to the ABS, Australian businesses spent $18.9 billion on R&D from 2013 to 2014. Of the $18.9 billion spent, large businesses contributed $11.1 billion, medium-sized businesses contributed $4.6 billion and small businesses contributed $3.2 billion.

Studies confirm that the level of innovation among SME employees is much higher than among employees of larger businesses. This is perhaps because Australians have traditionally been a very innovative people, constantly recording the highest number of inventions per head of population. This has resulted in more than half the major technological advances of the twentieth century originating with individual inventors and SMEs.

A persistent difficulty that SMEs face when undertaking R&D is obtaining adequate finance. Traditional sources of finance, especially banks, perceive this type of finance request as high risk. One possible source of finance for R&D is venture capital. The investors take an equity position in the business (own part of it) and provide supplementary finance.



FIGURE 10.7 Cedar Anderson had a free childhood that nurtured his natural curiosity. He would often pull things apart and figure out how things work. This became an obsession as he grew up, helped by his dad Stuart, the Mr Fix-It guy of the community. For years, Cedar and Stuart tinkered away in a shed trying to come up with a revolutionary new way to harvest honey. In 2015, they launched a crowdfunding campaign to raise funds to produce their invention, the Flow Hive. Eight weeks later they had raised $16 million and had to manufacture 24 000 orders and export them to more than 130 countries.

10.4.5 How SMEs can enter the global market for long-term growth

Over the past two decades, the number of SMEs who have entered the global market has rapidly increased. Today over 90 per cent of Australian exporters are SMEs and they earn almost 50 per cent of export revenue. The main cause of this (besides easier entry to many countries through trade agreements) is the rapid expansion in electronic business (e-business), which has largely been brought about by the development of the internet. E-business has opened the door for many SMEs to sell direct to consumers across national borders (see the following Snapshot).

SMEs can enter the global market by selling directly to customers in export territories, marketing products through a local distributor, participating in a joint venture with a local business partner or selling through a website. Each strategy provides businesses with a different level of cost, risk and control.

Working with distributors provides businesses with a local presence in markets they wish to export to. Distributors buy products from a business and then resell them to their own customers. Distributors offer the business the benefit of established local contacts and market knowledge. Although working with distributors provides the business with access to established markets, the business will have minimal control over the way the distributors deal with customers or market their product.

A joint venture with a local business partner also provides the benefits of local market knowledge and contact. This is where an organisation sets up a business relationship with a company in the local market.

Selling products through a website is a simple, low-cost way of entering the global market. Customers around the world can visit the website at any time to select products and place orders. To improve their chances of success, businesses need to prepare website pages specific to the different markets to which they wish to export. They need to provide product information in the local language, with prices in the local currency. Selling to global customers through a website is suitable for products that do not require demonstration or explanation by a sales representative.

Case study: Shoes of Prey — global expansion

Jodie Fox loves shoes. However, she could never find the exact shoes that she wanted. Along with her ex-husband Michael and old workmate Michael Knapp, she created Shoes of Prey, an online store that allows customers to design their own shoes. Following its launch in 2009, Shoes of Prey has gone on to become a multimillion-dollar medium-sized global business.

Shoes of Prey's online store uses a unique 3D design template that allows customers to create their own shoe. Starting with a style, the customer can then design the shoe, choosing heels, fabrics and textures, colours and height. The site shows the customer a 360-degree rotating sketch so that they can get a complete view during the design process. Once the shoes are designed, they are manufactured in China and then shipped to the customer. Any shoes that are returned are sent directly to Good 360, a not-for-profit that connects businesses who have brand new, unsold goods, with charities that support Australians in need.

The company has staff permanently located in an office in China to ensure that its quality standards are maintained. Shoes of Prey truly has a global focus as it offers worldwide shipping to its customers. It operates French, German, Spanish and Japanese language sites to serve all overseas customers. The website also has a facility for changing the currency at which prices are quoted.

When planning the business, the founders sought to establish a product that was different and something that people would want to talk about. In planning Shoes of Prey, they considered who they believed their customer was, the size of the market, who their competition was, their strengths, weaknesses, opportunities and threats. The founders met with potential suppliers, researched and developed concepts for the design of the website, and determined how they would market the website.

Before the business launched, a business blog, 22michaels.com, was maintained, directing potential customers to the forthcoming website. The blog is still going and now the company also has a Twitter account and a Facebook page. 'My favourite way of communicating with customers is on our Facebook page. We have a strong community there and it's such a nice way to get into a conversation about shoes while getting to know our customers,' Jodie Fox says.

Soon after the business launched, Shoes of Prey hired YouTube beauty guru Blair Flower to sample and review a pair of custom-made shoes. 'The first day the video went live we had 200 000 people visit our website,' says Michael Fox. The Shoes of Prey website received 500 000 hits and this translated into a 300 per cent increase in sales.

As the business has grown, Shoes of Prey has begun to focus on becoming a significant international retailer. The business has recently opened bricks and mortar stores due to customer demand. Customers wanted to see and feel the shoes in real life. The company now has one store in Sydney in David Jones in the CBD,

SNAPSHOT



'… Shoes of Prey has begun to focus on becoming a significant international retailer …'

and five shop-in-shops in Nordstrom department stores across the United States. The process has been challenging because Shoes of Prey does not have the same relationships with suppliers as it does in Australia. However, Shoes of Prey's business model has not changed. 'We're still doing everything on demand and we're still customised,' Jodie Fox says.

Source: Shoes of Prey

SNAPSHOT QUESTIONS

1. **Identify** the source of inspiration for the business.
2. **Outline** the business planning process undertaken.
3. **Describe** the marketing strategies employed by Shoes of Prey.
4. **Deduce** some challenges the business might have experienced when entering the global market.

SUMMARY

- The SME sector contributes:
  - approximately 57 per cent of gross domestic product (GDP)
  - approximately 66 per cent of total private sector employment
  - to our balance of payments, since they are often more successful at exporting than large businesses
  - significantly to the level of R&D.
- SMEs can enter the global market by selling directly to customers in export territories, marketing products through a local distributor, participating in a joint venture with a local business partner or selling through a website.

EXERCISE 10.2 REVISION

1 **Define** the term '*economy*'.

2 **Recall** the three basic questions that all economic systems must answer.

3 (a) **Identify** the type of economic system operating in Australia.
(b) **State** how the economic questions are answered in this type of economic system.

4 **Explain** what happens when economic growth occurs.

5 **Clarify** how economic growth is measured.

6 **Define** the term '*balance of payments*'.

7 **Describe** how a country can maintain a favourable balance of payments.

8 **Identify** the missing words to complete the following sentence. The first letter of each word has been provided.

SMEs contribute to the economy by boosting economic growth, as measured by g_____d_____p_____. SMEs also contribute to taxation revenue because they e_____ approximately 8 million people. The e_____ earnings that SMEs generate through selling goods and services overseas are also significant.

9 **Distinguish** between an invention and an innovation.

10 **Account** for the fact that SMEs often face difficulties in obtaining finance for R&D.

11 **Describe** the role of a venture capitalist.

12 **Summarise** the economic contribution of SMEs by completing the following table.

Characteristic	Summary
Gross domestic product	
Employment	
Balance of payments	
Invention and innovation	

13 **Outline** the ways in which SMEs can enter the global market.

EXERCISE 10.2 EXTENSION

1 **Examine** a small business that has been successful in exporting its goods or services. The **Austrade** weblink is a useful resource. **Create** a short report using the following headings:
(a) Name of the business
(b) What the business does
(c) What the business exports
(d) Where the business exports its goods or services
(e) Reasons the business is successful.

2 You have been asked by the local newspaper to **create** an article evaluating the importance of SMEs to the Australian economy. Your article will appear in a special supplement dealing with small business. Prepare your article exactly as you would like it published, using a desktop publishing program for layout if possible. Use your imagination and choose a thought-provoking headline. After you have prepared your first draft, confer with a partner to edit your article to publishing standard. Display the articles around the room.

3 **Determine** why the level of innovation among small business employees is much higher than among employees of larger businesses.

4 Reflect on what you have read and learned so far. **Assess** how this information would influence you if you were intending to start a small business.

on Resources

Weblink: Austrade

10.5 Success and/or failure of SMEs

Starting and operating a SME certainly is appealing, which is why so many people dream of doing it. Many entrepreneurs are driven by the desire to be their own boss, do what they want to do and turn passions into profit-making businesses. While many people are successful in their business ventures, many others unfortunately experience failure. In fact, of every ten SMEs started, about seven go out of business within five years after opening their doors. The financial risks of running a SME are very high, although some businesses are more risky than others.

In addition to psychological and financial pressures, SME owners tend to be victims of physical stress. Often, they must not only be the owner but also the accountant, marketing manager, sales representative, stock clerk and receptionist. The hours can be long and holidays are rare. SME owners also face major challenges as they attempt to juggle home and work responsibilities.

BizFACT

When it comes to survival of individual businesses, health care and social assistance businesses have the highest rate of business survival, with around 3 in 4 businesses continuing to operate for at least four financial years — nearly a 75 per cent pass rate. Health care and social assistance also had the lowest number of businesses closing down ('business exit rate') in 2016.



FIGURE 10.8 Starting a business may lead to greater independence, but may also increase workload and stress.



FIGURE 10.9 Keys to SME success

However, thousands of people each year balance the risks and potential rewards and decide to become a business owner.

10.5.1 Success of SMEs

All SME owners start off optimistically, believing that their business venture will lead to financial success and security. They will probably have read a few of the many books that have been written about being successful in small business. These books often highlight five common 'keys' to SME success (see figure 10.9).

1. *Entrepreneurial abilities.* The people in SMEs are crucial to the success of the enterprise. Attitudes and personalities of owners will vary enormously. Some will have drive and enthusiasm, many will set targets and some will take big risks. Some will thrive on the challenge of a potential failure, enjoying the process of solving the problem. The majority will be highly motivated and optimistic, as outlined in the next Snapshot.
2. *Access to information.* It is always difficult for a SME owner to choose relevant information and to gauge the quantity of information needed. As a bare minimum, the SME operator must have information regarding profitability, the quality of products and services, and the performance of employees. Accurate and up-to-date information will allow the SME owner to make better decisions.
3. *Flexibility.* The small size of the business allows the owner to adapt quickly to changes in the external environment. Because there are fewer levels of management, decisions can be made quickly. In addition, the close contact between owners and their customers allows the establishment of personal relationships, helping owners to respond quickly to clients' changing tastes and preferences.
4. *Focus on market niche.* Small businesses can concentrate their efforts on a small market of consumers in an attempt to fill their needs and develop a strong, lasting relationship. This provides the opportunity for the SME to become more specialised and able to deliver a high level of service (see the following Snapshot).
5. *Reputation.* Because the SME is servicing a narrow market niche, it can develop enviable reputations for quality and service.

BizFACT

According to a recent study, SMEs are most likely to find success if they adopt a niche marketing strategy. This is because the most fundamental threat to SMEs is the ultra-competitive and over-advertised global marketplace. To overcome this challenge and survive despite having a low budget, SMEs need to find a small market niche so they can operate in an environment with less competition.

SNAPSHOT



'… Scott Bradley and Sean Towner are not short of bravado.'

Yo-get-it — an ambitious SME

At just 23 and 24, former construction project managers Scott Bradley and Sean Towner are not short of bravado. Or brains.

And after chucking in lucrative jobs and opening their first company, Melbourne frozen yoghurt bar Yo-get-it, the pair are also poster boys for healthy ambition.

'What we want to do is knock off Boost,' says Bradley, a baby-faced company director wearing a sideways visor and skate shoes.

'We want to be right across the country — we want to be the next Boost Juice.'

Like Boost Juice founder Janine Allis — whose original Adelaide store multiplied into 189 franchises in the company's first six years — Bradley and Towner had their brainwave while travelling in America. During their six-week trip, the would-be entrepreneurs were keeping one eye on the sights, and another on potential dollar signs.

Bradley had a large bundle of cash sitting at home, after winning $70 000 on television game show *Deal or No Deal*, and Towner had long dreamt of running his own business.

In the United States, the pair saw store after store selling takeaway frozen yoghurt, and after a chance conversation, realised Australia hadn't yet embraced frozen yoghurt as a business concept.

'I always wanted to run my own business, but no way in the world would I have ever thought of a frozen yoghurt bar,' Bradley says.

After further research back home, the pair was convinced they had found their niche, and applied for a bank loan — with little success.

'We tried to go to the bank and ask for money but they needed assets or my parents to go guarantor, but I wanted it to be my sort of thing,' Bradley said.

So instead Bradley bought a 41 per cent share of the company, Sean invested in 36 per cent, and friends and family invested in the remainder.

With the funds in place, and more research, including 12-hour customer-counting stints outside Malvern yoghurt bar Igloo Zoo, the pair felt ready to leave their construction jobs.

'It was a fairly risky manoeuvre to undertake,' Towner said. 'It's a little bit daunting because essentially the buck stops with us.'

The first Yo-get-it, near Glenferrie railway station in Melbourne, opened on Christmas Eve.

The store has several different features that its owners believe set it apart. Customers pour the frozen yoghurt themselves and choose their own toppings, with the price measured by weight, allowing school children with only small change to buy a treat. And anyone who guesses the correct weight to the gram gets their yoghurt free.

Note: In 2017, Yo-get-it had ten stores across four Australian states, as well as three stores in China.

Source: *'Yo! Boosting the hopes of baby-faced bosses',* Larissa Ham, *The Age*

SNAPSHOT QUESTIONS

1. **Identify** the personal qualities of Scott Bradley and Sean Towner that help make their business a success.
2. **Outline** the research the pair undertook before starting their new business.
3. **Explain** the risks and challenges faced by Scott Bradley and Sean Towner.

on Resources

Weblink: Yo-get-it

10.5.2 Failure of SMEs

Sometimes enthusiasm and optimism cloud the owner's vision of reality and poor decisions are made. In the real world, success can be hard to achieve. Unfortunately, many SMEs end in failure. Although we do not want to dwell on the negative, it is important to acknowledge the experiences of many SME owners.

In a sense, it is perhaps too easy to establish a business: there are no interviews, no tests to pass and no previous experience required. All that is necessary is a payment of $35 to register the business name for one year and even this is not required if the business owners trade under their own name. It is not surprising then that many businesses end in failure.

A SME is classified as a failure when it is:

(a) unincorporated and declared bankrupt — a legal process of distributing among the creditors the property of a business or person who cannot or will not pay their debts

(b) incorporated and either forced into liquidation or voluntarily closes down because it cannot pay its debts and faces a cash flow problem.

BizFACT

If a business owner decides to cease operating because of ill health, the loss of a partner or any other personal reason not associated with financial problems, then the business is not described as a 'failure'.

SMEs failure rates

Accurate figures are hard to obtain because not all business failures are reported. However, statistics collected by the Australian Bureau of Statistics point to an alarming trend: one in four businesses will fail within the first year of being established. This means that approximately 80 000 Australian small businesses fail each year — roughly 219 per day.

Table 10.1 shows the SME failure rates, which are calculated from various government surveys.

Within the first five years of commencement, approximately seven out of every ten SMEs will fail. Female-owned businesses have a higher survival rate than those operated by men, and businesses jointly operated by both men and women have

BizFACT

ASIC found that in 2012/13, 81 per cent of businesses that became insolvent were small businesses employing fewer than 20 people. The construction sector was the worst of those affected, with 24 per cent of the insolvencies coming from that sector.

the highest survival rate of all. The figures in table 10.1 tell a sobering story for anyone contemplating establishing a SME: the chances of failure are high. Therefore, it is absolutely essential to undertake thorough planning so as to minimise the risk of business failure.

TABLE 10.1 SME failure rates from year of establishment

Period from commencement	Cumulative total of approximate failure rate (%)
After 1 year	25
2 years	42
3 years	54
4 years	64
5 years	71

Reasons for SME failure

Small to medium enterprises fail for many reasons. Small to medium enterprise failure is not usually caused by one single factor but rather a combination of several factors:

- failure to plan
- lack of information
- leadership crisis
- inaccurate record keeping
- failure to delegate
- complacency
- incorrect marketing strategy
- poor location
- lack of financial planning
- negative cash flow
- new competitors
- illness
- supplier problems
- poor use of external support services
- economic downturn
- new taxes
- change in government policy
- insufficient capital
- partnership problems
- lack of management experience
- incorrect pricing policy
- failure to seek advice
- not enough sales
- staff difficulties
- being under-insured.

BizFACT

According to statistics released by ASIC, the primary cause of business failure is poor strategic management, with 42 per cent of owners reporting this. Forty-one per cent of business owners also reported that inadequate cash flow or high cash use is a driving factor; 32 per cent of businesses are trading at a loss; and 33 per cent are experiencing poor financial control. Their analysis also revealed that many business owners admitted that they are not keeping good records, making this another main cause of business failure.



FIGURE 10.10 Many SMEs have a short life.

Many SMEs start out on a 'shoestring' budget. Without sufficient capital — undercapitalisation — the business will not be able to purchase stock and materials. This inevitably results in lost sales. A business in this position faces disaster unless alternative finance can be arranged.

When a prospective SME operator fails to develop a business plan, the stage is set for imminent failure. Without a detailed business plan, the SME owner has no certain goals or directions; there is no blueprint for the business's future growth.

The most common fault with many SMEs is their lack of adequate financial reporting and evaluation.

BizFACT

Most small business failures are caused by factors within the business under the control of management. The most common causes are managerial inexperience and incompetence, undercapitalisation and lack of planning.

10.5.3 The effect of changes in the business environment on SMEs

Reasons for business failure

Some statistical research on the reasons why small businesses fail revealed interesting results. The following reasons were cited by small business owners as the cause of failure:

- 32.1 % — poor management of financial activities
- 14.6 % — lack of management competence or experience
- 12.4 % — inflation and economic conditions
- 12.3 % — poor books and records
- 10.7 % — sales marketing problems
- 9 % — staffing problems
- 6.2 % — union problems
- 2.7 % — failure to use external advice.

Let's take a look at the above figures and analyse the ramifications. Go back over the reasons cited above and determine whether each reason would be considered external to the business (i.e. outside the business's control), or internal (i.e. within the business's control). Add up all the external factor percentages together and then do the same for the internal factors.

As you can see, the only two factors that would be considered external are inflation and economic conditions, and union problems. If you add these two together, this means 18.6 per cent of small business failure can be attributed to external factors. What this means is that 82.4 per cent of business failure is largely controllable. This is important for business owners to understand in the sense that ultimately their own actions and decisions will have a larger effect on the success or failure of their business than outside influences.

Fundamentally, this means that in most instances, when businesses are experiencing problems, the owners can do something about it. By seeking the right help, they may be able to take action to resolve serious issues and ensure the long-term survival of their business.

SNAPSHOT QUESTIONS

1. **Identify** the top three reasons cited as the cause of business failure.
2. **Classify** each of the reasons cited as either being an internal or external influence on the business.
3. **Analyse** what these statistics signify about small business failure.

SNAPSHOT



'… 82.4 per cent of business failure is largely controllable.'

SUMMARY

- While many people are successful in their business ventures, many others unfortunately experience failure.
- The five common 'keys' to SME success are:
  - flexibility
  - reputation
  - focus on market niche
  - entrepreneurial abilities
  - access to information.

- A SME has failed when it is:
  - unincorporated and declared bankrupt
  - incorporated and either forced into liquidation or voluntary cessation.
- SMEs have a high failure rate.
- The most common causes of SME failure are managerial inexperience and incompetence, undercapitalisation and lack of planning.

EXERCISE 10.3 REVISION

1 **Explain** how a SME owner can maximise his or her chances of success by using the five 'keys' of business success (section 10.5.1).

2 **Recall** what needs to occur for a SME to be classified as a business failure.

3 **Account** for the high failure rate of small businesses in the first few years of operation.

4 **Outline** the two main reasons for small business failure.

5 Answer the following questions by **identifying** and then writing out the answer that you feel is most appropriate when considering the possible effects of small business failure. Share your answers with the rest of the class and **discuss** any differences.
   (a) *Effect on the owners*
      (i) Because most people who go into business know what they are letting themselves in for, there will be no adverse effects on the owners.
      (ii) There could possibly be some physical effects on the owners.
   (b) *Effects on staff*
      (i) Most employees do not mind being retrenched.
      (ii) Being retrenched is never easy to accept and there is usually a certain amount of stress associated with finding new employment.
   (c) *Effects on creditors*
      (i) The high number of SME failures is bound to cause financial hardship to creditors.
      (ii) Most creditors are large companies and can therefore afford for small businesses to go bankrupt without it being too much of a financial drain on them.
   (d) *Effects on consumers*
      (i) When a SME fails, consumers are not inconvenienced at all because there are others to choose from.
      (ii) Often customers find themselves not only inconvenienced by SME failures but also feel left out in the cold when they attempt to receive some type of compensation for their loss.

6 (a) Refer to the list of reasons for SME failure in section 10.5.3. Prepare a table and **classify** each reason using the categories 'internal business environment' or 'external business environment'.
   (b) **Deduce** what this table reveals about the reasons for SME failure.

7 'A business without a plan is doomed to fail'. **Justify** this statement.

EXERCISE 10.3 EXTENSION

1 In small groups, **create** a list of success strategies for SMEs.

2 Most people who start a SME know of the high failure rate and the reasons for it. **Explain** why they do not take steps to protect their business from failure. **Recommend** the steps they should take.

3 Assume the minister for small business establishes a committee to develop a poster highlighting the rules for success in small business. **Create** your poster and display it in the classroom.

on Resources

Digital doc: Chapter summary (doc-26102)

Interactivity: Chapter crossword (int-7229)

Interactivity: Multiple choice quiz (int-7230)

CHAPTER 11

Influences in establishing a small to medium enterprise

OVERVIEW

11.1 Introduction
11.2 Personal qualities
11.3 Sources of information
11.4 The business idea
11.5 Establishment options
11.6 Market considerations
11.7 Finance
11.8 Legal considerations and influence of government on SMEs
11.9 Human resources
11.10 Taxation

11.1 Introduction

The thousands of SMEs in Australia today are owned and operated by all types of people. These businesses all had a beginning; they all had a person or small group of people who decided to 'have a go'. When establishing their businesses, they needed to consider a range of influences that combine to determine the level of success achieved.

11.2 Personal qualities

All types of people own and operate the thousands of businesses in Australia today. Not everyone, however, is suited to the role of business owner as certain skills and personal qualities are required to succeed.

Starting a new business requires courage, determination and energy, and it demands a wide range of skills. It is important for people to recognise their strengths and weaknesses, decide if they have the right personal characteristics to be a business owner and learn the skills they don't presently have. It is best for business owners to select a business opportunity that suits their personality and builds on their strengths. If people have an honest understanding of their own personal qualities, then failure can be minimised: the 'square peg in a round hole' problem can be avoided.

There is no simple checklist of skills and personal characteristics that will guarantee business success. However, many studies have shown that certain personal characteristics are helpful in operating a business, and that the potential business owner should be prepared to honestly answer the questions asked in figure 11.1.

11.2.1 Qualifications

Hundreds of thousands of people start a new business every year. Would you like to be one of them? You do not have to be an exceptional champion of legendary dimensions. Mainly, those who decide to 'give it a go' are ordinary people rather than sensational opportunists who desire adventure. Many start out with only a

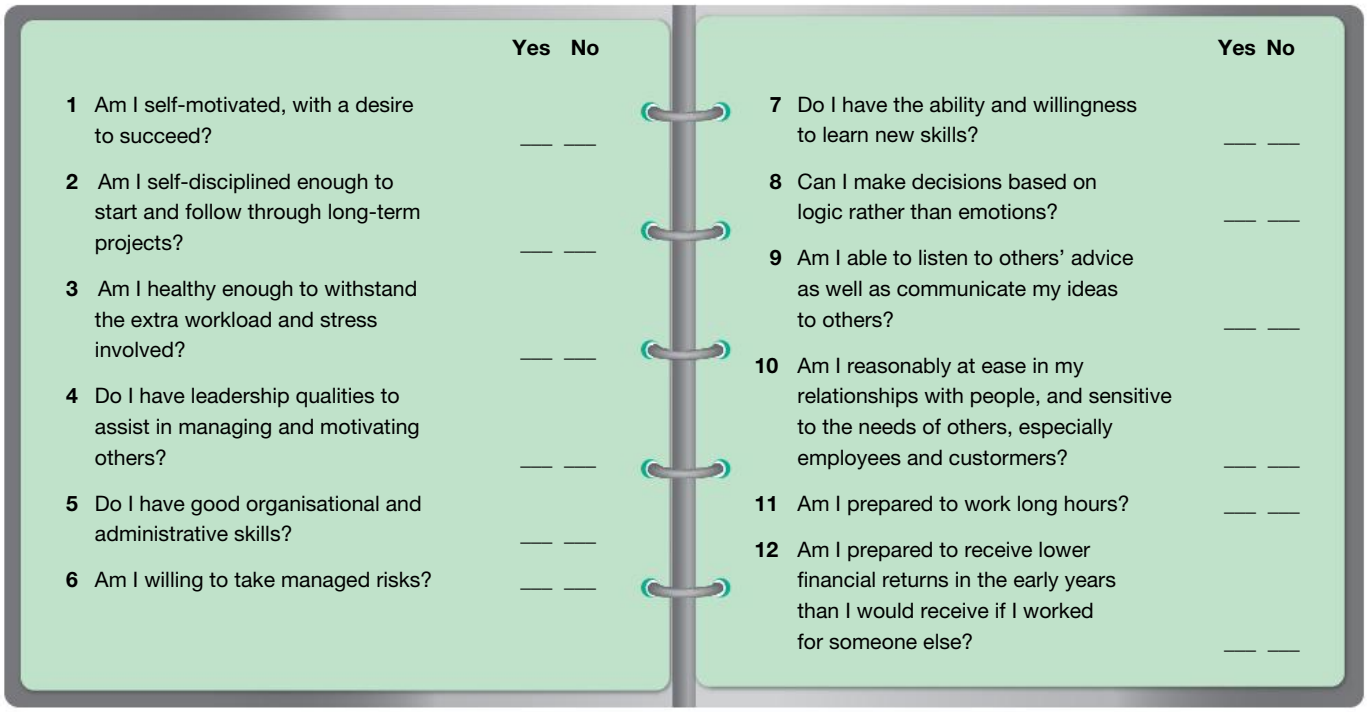


FIGURE 11.1 Some questions to ask yourself to assess your entrepreneurial ability

small amount of money, operating informally from home, at least in the beginning while they are getting established.

Exceptional grades and a dazzling history in business are not essential. What does appear to be important is the eagerness to work long hours. A recent survey found that one in five SME business owners work at least 60 hours a week, highlighting the level of commitment and time required to run your own business. The findings were contained in a Suncorp *SME vs Me Report*, which surveyed around 500 SME business owners from a variety of industry sectors. While the average SME owner works 41 hours per week, 16 per cent of owners work between 60 and 80 hours a week and a further 6 per cent actually work over 80 hours. The results demonstrate how hard business owners are working.

Starting a SME knows no age limits. From the very young to the very old, people are starting new businesses at a rapid rate. Particularly encouraging is the large number of young people aged between 20 and 25 who are operating a SME (see the Snapshot on pages 342–3). Older people are also involved in starting new SMEs; this type of business offers the most opportunities and flexibility to retirees.

For some types of SMEs, few or no formal academic requirements are needed to commence operating. However, for those who want to gain academic qualifications in small business, many tertiary courses are available. The Business Studies course you are studying is of enormous value should you decide to become a SME owner. Such courses give you knowledge and understanding of what is required to successfully own and operate a SME. Knowledge and understanding can also come from experience through working for other businesses. Your part-time job, for example, is providing you with experience in a business's day-to-day operations, how to manage your time and other people, purchasing and pricing decisions, and a variety of other business functions.

SME owners are a varied group. It is extremely difficult to categorise them or the qualifications they possess that make their business a success. As well, a variety of personal factors encourage individuals to go into business. However, two factors that are often mentioned are motivation and the 'entrepreneurial spirit'. They combine to form a powerful desire to create a new business.

BizFACT

Millennials, those born between 1980 and 2000, are increasingly breaking away from traditional forms of employment and instead starting their own small businesses. The Council of Small Business Australia has found that this desire has been driven by a decrease in job opportunities in more traditional areas. Social media and technology have also helped young people run successful businesses. BNP Paribas Wealth Management surveyed millennials around the globe and found that nearly 60 per cent of them want to work for themselves. They came up with the term "millennipreneurs" to describe them.



FIGURE 11.2 Take a look around your school or family. About half of these people will, at some stage during their lives, decide to own and operate their own SME. Age, gender or experience is no barrier.

11.2.2 Skills

Luck has little to do with business success. Skills are essential. These skills can be attained through experience, education and/or training.

Experience

If a person has been working the last few years as a dedicated employee, then during that time, they will have gained valuable experience. They probably also developed new skills as a result of training or exposure to various aspects of the business's operations. Consequently, apart from well-developed management skills, a person with hands-on experience will have a greater chance of achieving business success.

The best time for a person to gain management experience is before establishing the business. This can be done by either completing a management training course or by undertaking a management role within a business. The best way a person can gain business experience is to work in the type of business in which he or she intends to become self-employed.

These experiences provide a platform from which to work. The experienced person will understand and be realistic about the demands, both financial and personal, that a business will place on them. Figure 11.3 outlines possible experiences, from working in other businesses, that could help someone establish their own business.

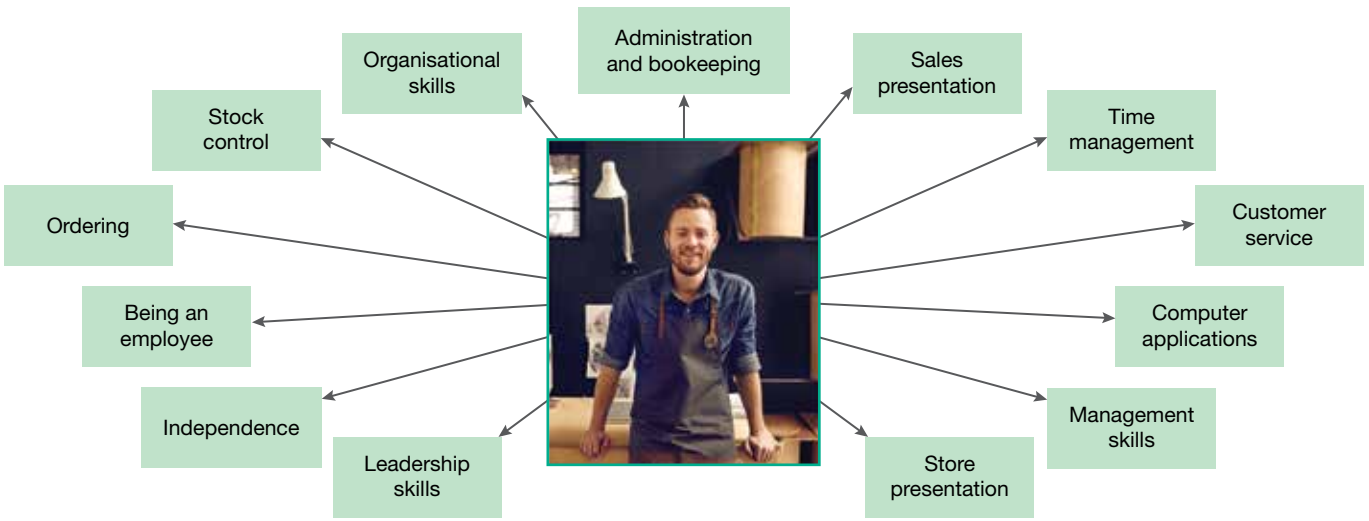


FIGURE 11.3 An individual's range of experiences

Education and/or training

Education and/or training is another way to gain skills. Universities, TAFE and business colleges offer courses in many business and industry fields. These courses may be broad in nature, such as a degree in business management, or specific, such as a degree or diploma in marketing, human resource management, computing or accounting. TAFE and business colleges also offer vocational courses and courses for establishing a SME. The main problem is that some courses are expensive and take years to complete. For this reason they are not always an option, especially for small business owners who may wish to gain the knowledge quickly.

Some government agencies provide opportunities to learn about starting a business. Business Enterprise Centres are an example. The centres are run by business facilitators who have experience in establishing and operating a business. They offer a range of services, such as business start-up advice and assistance, business growth mentoring, seminars, business plan assistance and skills training. They also facilitate networking opportunities and provide information on grants and assistance that may be available.

All of these avenues for education allow the business owner to develop the essential skills necessary for establishing a business. These skills may include:

- accounting
- computer skills
- staff management
- business administration, including inventory control and rosters
- marketing.

BizFACT

Almost 57 per cent of all NSW small business operators have completed Year 12 or equivalent. For those operators who have post-high school qualifications, 45.1 per cent achieved a certificate level qualification, 16.5 per cent an advanced diploma or diploma, 27.2 per cent a bachelor degree, 2.5 per cent a graduate diploma or graduate certificate and 8.7 per cent a postgraduate degree.

11.2.3 Motivation

Motivation refers to your personal drive, determination and desire to achieve a goal or objective. The desire to be your own boss is a major reason for wanting to start your own business. Many people start on their own because they believe they can do better for themselves than if they remain with their present employer. Often they desire the freedom to choose when and where they work, with whom they work and whether to work from home. The underlying attraction is the desire to transform an idea into a successful product by capturing the attention of potential customers (see the following Snapshot).

BizFACT

A recent Suncorp SME vs Me Report *revealed the top 10 reasons why people start their own business. The number one motivator, cited by just over half of all SMEs, was simply being the boss. Other factors that ranked highly among SMEs were doing what you are passionate about, finding a better work – life balance, and taking greater control of your life. The potential for greater financial reward ranked in fifth place. Only 14 per cent of SME owners started their business as a result of a great idea for a product or service.*

PracticeManager 24/7 — Anthony Turri's motivation

SNAPSHOT



PracticeManager 247.com.au is an online business management software program that helps health and fitness professionals run successful practices.

How do you describe your business?
Practice Manager 24/7 has been custom designed and built by Australians, for Australians. It's best suited to personal trainers, massage therapists, physiotherapists, or anyone that has an appointment-based business. Our program does all the hard work so that health professionals can focus on doing the things they love. We strive to give our customers the freedom they deserve and we live by our motto: It's your Practice, made Perfect!

Did you always want to run your own business?
Yes and no. I didn't really dream about running my own business when I was in high school. Although, studying Business Studies definitely piqued my interest. Once I was at university, the urge to run my own business grew stronger and stronger. By the time I finished university I was hooked! After that I've never looked back.
In that time, I have been lucky enough to own and operate multiple businesses, often concurrently, within the fields of my expertise: health and education.

"Self-belief and self-motivation is crucial."

What motivated you to want to start your own business?
A belief that one day I could help change the world to make it a better place. Being a health professional first, the biggest kick I get out of each day is being able to help someone. That's what makes me tick. So, through my entrepreneurial endeavours, my aim is to help thousands of great health professionals achieve two things: firstly, to help them stay in the industry; and secondly, to help them with their business operations so they can focus wholeheartedly on their patients and clients. Achieving these two goals will help the world become a happier and healthier place.

How did the idea come about and what inspired you to get into action?
As a lecturer I have seen some fantastic graduates come through the ranks. When catching up with them a few years later, I was shocked to find that so many of them had given up on running a practice. Many had left the industry altogether, which was the biggest shame, as I knew they had the potential to do great things. I often asked them why they'd given up and the most common answer I received was 'it just got too hard'. On further investigation I'd discovered that these practitioners were great at being health professionals, but not so great at running a business. They just didn't have the necessary business tools required. On completing my research I discovered a gap in the marketplace. I noticed that all the other software programs were way too complicated and created by computer programmers, not health professionals. So I found my niche, a great business partner and a fantastic team of developers. And after three years, Practice Manager 24/7 was born.

What are some of the things you enjoy most about running your own business?
Freedom. The freedom to create, to make your own decisions, to enjoy every day and to determine your own destiny.

What's the biggest challenge you've had to overcome to make your ideas a reality?
Patience. There are going to be times when you can't see the light at the end of the tunnel. Sometimes you can't even see the road! Running a business, just like life, is a marathon, not a sprint. Relax, refocus, review and persevere, and you'll get there. Self-belief and self-motivation is crucial.

What advice can you share with other people trying to start a business?
Try to use as much of your own money as possible when first starting up. You'll be much more motivated when it's your money that you're losing. It's surprising how much harder you'll work.

Do your research. Planning is the most critical stage of any business. We are lucky enough to live in a world where we have access to a plethora of information, so read, read and then read some more. Also, watch and listen to interviews/podcasts/documentaries/TV shows, whatever you can. Ensure your business will work before you embark on any business venture. Find your market, be realistic and do your sums. If the numbers don't add up now, they won't add up later.

Learn from other people's mistakes, not just your own. It's a lot less painful.

Stop comparing yourself to others. There's always going to be someone, bigger, stronger, faster, smarter or prettier. Just be the best you can be!

Have fun! If it's not fun, it's not worth it. If you wake up in the morning and you're not pumped and ready to work on your business (even on 3 hours sleep sometimes) then do something else. Not every day is going to be amazing, but if you don't believe it will be, then it's not the right thing for you. You're going to work harder than most of the people you know so you have to love it.

And finally, be good to as many people as you can. Good people get good things in return. Sometimes it takes a while, but it does and it will happen.

SNAPSHOT QUESTIONS

1. **Identify** the characteristics shown by Anthony Turri that would categorise him as an entrepreneur.
2. **Recall** some of the things Anthony Turri enjoys most about running his own business.
3. **Summarise** Anthony Turri's main challenges.
4. **Determine** why you think Anthony Turri has been successful in business.

Most business owners are motivated by the rewards they believe can be gained from establishing a business, including both monetary and non-monetary rewards (see figure 11.4).

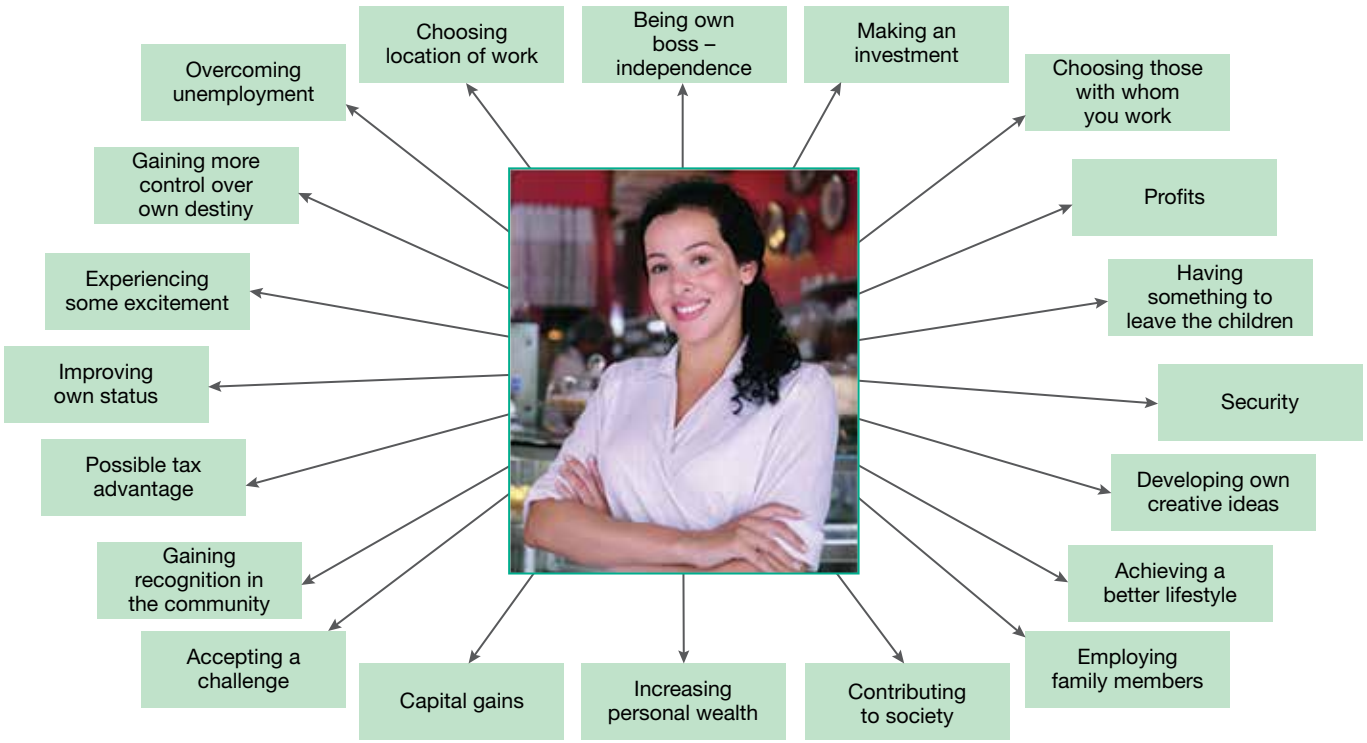


FIGURE 11.4 Examples of the possible rewards of business ownership

11.2.4 Entrepreneurship

As was outlined in chapter 1, an entrepreneur is someone who starts, operates and assumes the risk of a business venture in the hope of making a profit. The term can apply to any person — male or female, mature age or young — willing to establish a business in a bid for success. Not all entrepreneurs begin by setting up a business premises. An increasing number of people work from home, especially as computers have allowed greater access and communication with business markets. Entrepreneurship is not just an avenue to wealth, but a way of making a living and achieving job satisfaction.

Society is constantly changing and thus creating new opportunities for innovative products and services to be developed. The entrepreneur must have a range of personal characteristics that enable them to take advantage of, and be successful with, these opportunities (see figure 11.5).

First, entrepreneurs must be prepared to take a risk and incur the results of this risk, whether it is a success or a failure. They must be confident in decision making and willing to accept all responsibility for their decisions. Sometimes a decision requires 'guts and determination' and such times often lead to success. The entrepreneur must always have a will to succeed: they may not achieve the desired goal with the first venture, so they need drive, determination and an ability to recover from poor decisions or mistakes.

Flair and creativity are also essential for an entrepreneur. They allow the entrepreneur to create or seize new opportunities for business, new niche markets or new products and/or services. Success can sometimes depend on finding a new and more innovative way to sell a good or service. Scott Bradley and Sean Towner, who established Yo-get-it (pages 330–1), are examples of entrepreneurs who successfully developed a niche market. Finally, the most important quality for an

on Resources

Weblink: Top Business Entrepreneurs

eLesson: Global Kidz Oz 1 (eles-2296)

entrepreneur is the ability to set goals and have a vision for the business's future. Having achieved their goals, they must set new goals — continually adjusting to changing business, economic and customer markets.

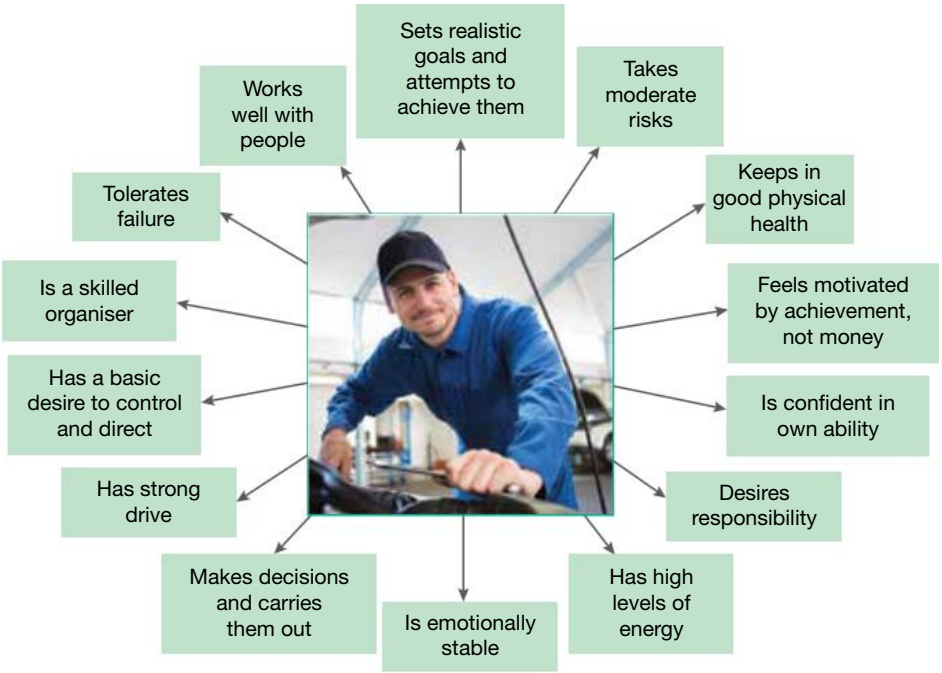


FIGURE 11.5 General personal characteristics of a typical entrepreneur

SNAPSHOT



'… Josh Murray is bucking the trend.'

Case study: Josh's eggsellent free range adventure turns pocket money into big business

For 16-year-old Josh Murray, it all started with a Lego set.

Back when he was nine, the budding entrepreneur really wanted a Star Wars-themed Lego kit, and to earn some pocket money, he started selling a few eggs to the neighbours from his family's farm.

Fast forward to now, and that initial foray of selling a dozen eggs to those next door has grown into Josh's Rainbow Eggs, a fully fledged egg farm that produces 55 000 free-range eggs per week near Gisborne, an hour's drive north of Melbourne.

While recent Australian Bureau of Statistics figures show that the average age of a farmer in Australia is 56, Josh Murray is bucking the trend.

'Ages ago, when we first got the farm, we always had chickens. Mum looked after them and I just collected the eggs,' he said.

'After a while though, I wanted some pocket money so I saw the chickens as a good way to do that.

'From there, I would sell eggs to people at the local shops. Then I went to farmers' markets and it went from there.'

Now Josh has outgrown the capacity of local farmers' markets and his eggs are sold at three large supermarket chains.

But he said he still regularly spruiked his eggs at the local shops.

'I really enjoy meeting the customers, but I also just enjoy the quiet satisfaction of the work, he said.

Emphasis on ethical egg production

By using mobile autonomous sheds, Josh said he produced 'ethical' eggs.

'I want to do what is best for the chickens,' he said.

The giant sheds are mounted on wheels, and can be moved onto fresh grass when chickens in the shed have picked apart and compacted the ground they are on.

'We move the sheds every month, and that means there's enough time for the chickens' poo to affect the soil positively too. It also means the chickens get access to fresh grass.'

The sheds are also autonomous, with feed and water delivered automatically. The shed can be set to open and close at specific times of the day to ensure the chickens are safe at night and do not get out too early in the morning when it is still cold.

Running the sheds can consume a significant amount of power, so in an effort to combat this, the Murrays have invested in solar power so that the shed can run off the grid.

The power generated also runs the conveyer belt that runs down the middle of the shed to collect the eggs. This allows Josh to collect the eggs in about half an hour instead of two hours under the old manual system he used to use.

Source: Australian Broadcasting Corporation

SNAPSHOT QUESTIONS

1. **Identify** some of Josh's personal qualities that have enabled him to become a successful entrepreneur.
2. **Why** did Josh start his own business?
3. **How** has Josh differentiated his business to achieve a competitive advantage?

The benefits of entrepreneurship

A sense of freedom and independence are perhaps the best things about being a business owner. Often, a person will desire the freedom to choose when and where they work, with whom they work, and whether to work from home. The great attraction is the belief that owners will have more control over their own destiny.

Someone willing to work hard may believe that they can earn much more by working for themselves than they would by working for someone else. They would expect their extra effort to be rewarded through the profits from their own business. These rewards may not come immediately — even the most successful businesses may lose money in their early start-up phase — but the hope is that eventually the business owner will earn more from being self-employed.

People who work for themselves also experience the satisfaction of guiding the business's growth. They enjoy the challenge of overcoming obstacles, setting and meeting new targets, and gaining a larger customer base. While it can sometimes be a hectic existence, most entrepreneurs seldom complain that running their own business is routine and boring. Ultimately, they take pride in having made it on their own.

The burdens of entrepreneurship

Small to medium enterprise owners must accept the responsibilities of entrepreneurship. Being in business requires a person's full attention. The work hours for a business owner will invariably be longer than an employee's work hours. As well, self-employed people find it difficult to leave their problems at work; they constantly 'live and breathe' the business's problems. The anticipated freedom and flexibility may be illusive.

Even if the business succeeds, the owner still might have little money to spend apart from the salary the owner pays him or herself. Instead, the owner might have to reinvest the profits to generate long-term growth. Alternatively, short-term accounts may need to be paid with cash. In some cases, the owner may not even be able to draw a salary until the business becomes more established. As one

entrepreneur claims: 'The commitment you have to make is enormous; entrepreneurs usually put everything on the line.'

11.2.5 Cultural background

A person's cultural background can influence their reasons for establishing a business. Cultural influence can arise from a community's traditions and beliefs, such as the 'work ethic' — the willingness to work long and hard in an effort to be successful — which is strong in many European and Asian cultures. Many migrants come to Australia with few resources except a strong desire to improve their lives. Their determination often translates into business success (see the following Snapshot). Cultural influence can also arise from centuries of experience in certain trades or services, enabling a person to use this knowledge to achieve business success. A person from a Thai cultural background, for example, may be able to succeed in a restaurant business that aims to provide quality, specialist Thai food.

BizFACT

Twenty-nine per cent of Australian small business operators were born overseas. Of those born overseas, 23.7 per cent were born in North-West Europe, 17.2 per cent were born in North-East Asia, 12.7 per cent were born in Southern and Eastern Europe, and 10.7 per cent were born in North Africa and the Middle East.

SNAPSHOT



'… success depends on hard work and taking a careful, prudent approach to achieving goals.'

Case study: Culture and business — Rahim makes a healthy choice in Western Australia

Since moving to Western Australia in 2007, Rahim Parkar's life has changed significantly. He now walks a leisurely six minutes to work and is his own boss, running a Stay Healthy franchise in Midland Gate Shopping Centre, 16 kilometres from the Perth CBD.

This is very different from his life as a banker with the United Bank of India, Banque de Paris and Bank Muscat and more recently as Director of Investments and Treasury with Emirates Post, Dubai, a Government of United Arab Emirates entity.

"We considered other migration destinations such as Canada and New Zealand but we chose Australia because it is very beautiful and modern with a free, democratic society and the people here are friendly and peace-loving," Rahim said.

Rahim and his wife Jahan Aara visited Perth several times before making their final decision, but there were many compelling reasons for choosing Perth over other destinations. Rahim's youngest son recently completed his University studies in Perth, and together the Parkars have many friends and relatives in Perth, some having lived here for over 20 years.

Rahim has been as prudent and careful in choosing his new business as he was his new home. In all, he considered 30 business proposals and personally undertook due diligence and investigation of them all. He finally chose a Stay Healthy franchise retailing leading Australian and international brands of vitamins, minerals and a wide variety of health and skin care products.

With an extensive background in accounting and finance, Rahim says there are other considerations to be made when buying a business in Western Australia. Apart from the bottom line (profit), it's also important to look at the total training provided, a good store location and the potential growth of the business. Rahim has proved his theory by achieving significant growth in his first three years of operation.

Rahim advises other potential business migrants to take the time to properly investigate their business options.

'Get all the information and do feasibilities on multiple businesses — not just one or two — and make a careful selection to avoid loss.'

'Selecting the right industry is also important. In Asia and the Middle East, population is high and labour is in abundance. In Western Australia, this is different. When comparing businesses that are labour-intensive with those that are capital-intensive, capital is more favourable due to the high cost and scarcity of labour in Australia.'

'Do not spread your wings into too many businesses,' Rahim warns.

Having received permanent residency in December 2009, Rahim and his wife are now in the process of purchasing a new home close to where they are currently living.

'I am looking forward to buying a new home and finding opportunities to further grow my business socially and economically to benefit my family and the community,' Rahim said.

Rahim is also looking forward to becoming an Australian citizen and taking some time (his first holiday in three years) to see more of his new home state.

'We have visited local tourist places such as Mundaring Weir, Mandurah and Serpentine Dam, but my main priority so far has been to establish my business and work towards achieving our Australian citizenship.'

For others considering a move to Western Australia, Rahim says success depends on hard work and taking a careful, prudent approach to achieving goals.

'Be one hundred per cent determined and prepare to face some ups and downs. Take every step with honesty, integrity and a balanced approach.'

Source: Small Business Development Corporation

SNAPSHOT QUESTIONS

1. **How** has Rahim Parkar's life changed since moving to Australia?
2. **Why** did Rahim choose Perth, Australia to migrate to and open a business?
3. **Outline** the business planning Rahim undertook prior to beginning his own business.
4. **Identify** Rahim's personal qualities and skills that have helped him become a successful business owner.

11.2.6 Gender

Governments of developed economies are realising that employment growth will not come from established large businesses but from the creation or expansion of the small business sector. Policies are being created specifically to assist small business in contributing to the national economy. In response to these policies, and to a general change in social attitudes, many women are setting up their own businesses (in particular in self-employment) at three times the rate of men (see the following Snapshot).

BizFACT

Approximately 68 per cent of Australian small business operators are male and 32 per cent are female.

Case study: 2Step Dance — women and SMEs

SNAPSHOT



It takes determination, courage, persistence and a high level of motivation to achieve success with any business venture — qualities that sisters Nicole and Rebecca Micallef possess. The pair have been dancing together for over 30 years and their long-term dream was to eventually turn that passion for dance into a new business. While a love for dance and the desire to pass on such a beloved art-form are important qualities for running a dance studio, they are by no means sufficient to make it a success. Owning a studio requires capital, business skills, attention to detail and lots of hard work.

After dancing for 20 years, they were eager to begin teaching. This passion to teach gradually developed into a desire to own their own dance studio. The best way to learn about running a studio is to work at one. Nicole and Rebecca worked at a couple of different studios and taught a variety of different classes. The pair learnt a lot from this experience; they were able to observe close up the ins and outs of running this type of business as well as the typical problems and how they're solved.

While working at some well-known dance schools, they choreographed many award-winning eisteddfod routines of their own. Over time, they made a name for themselves and developed a large student following, as well as an excellent

'It takes determination, courage, persistence and a high level of motivation to achieve success …'

reputation in the area. After five years of teaching at various dance studios, they had a growing desire to inspire the dancing generation of today by opening their own studio. When they heard that the owner of the dance school they were working at was closing down her school, they took a leap of faith and decided to open up their own studio: 'We thought it was now or never'.

It took two years of hard work and persistence to get their business started and turn their dream into a reality. Even though they were both very experienced at teaching dance, they knew there was a lot more involved. They realised they needed to develop skills and educate themselves further about *running* a business. Nicole therefore undertook a Diploma of Business in order to develop these skills. 'Running a dance studio involves administration, book-keeping, event coordinating, payroll, hiring of staff, looking after the emotional needs of all students and much more!'

In 2007, they began 2Step Dance. Their aim was to create a studio that provides the support and disciplines that encourage a positive and non-pressured environment for all abilities and skill levels. Their mission is to strive to bring their love of dance to all ages by sharing its beauty, power and vision in fresh and unique ways. Rebecca and Nicole are very involved in all aspects of the studio from being the Principals to also teaching all the jazz classes, show teams and private lessons. Their passion for teaching and their care and dedication for their students is evident in every moment of their classes.

The main challenges they encountered during the establishment phase were promoting their business as well as making sure they complied with all the legal regulations associated with owning a dance school, e.g. acquiring the correct licensing and insurance. An ongoing challenge they've faced is ensuring they have sufficient numbers of student each year to cover all their costs.

'In order to succeed, you need to be persistent, patient and passionate. It takes time to create a successful business, but it's so much easier to motivate yourself when you're energised by what you're doing. In business, you are going to face constant challenges. Success doesn't come easy, but if you have determination and a positive mind-set, you can do anything.'

Rebecca and Nicole's determination has definitely paid off. Over the years, their ground-breaking choreography and style have revolutionised and captivated their audience. In 2016, the pair celebrated the 10 years as 2Step Dance. During this time, they have never had to invest a lot of money in advertising; most of their business has come from word of mouth and recommendations. In the 12 years since they opened, the business has gone from strength to strength but the pair have always remained true to their vision for starting the business in the first place.

SNAPSHOT QUESTIONS

1. **Identify** the personal qualities Nicole and Rebecca possess that have enabled them to achieve success with their business.
2. **Outline** what motivated Nicole and Rebecca to establish their own dance studio.
3. **State** some of the challenges Nicole and Rebecca have encountered.
4. **Describe** the factors that have led to the success of 2Step Dance.

Research undertaken by both federal and state government departments has highlighted the following points regarding women in business:

1. Women own approximately one-third of all small businesses operating in Australia.
2. Over the past decade, there has been a rapid growth in the number of women who chose to be self-employed, growing by a rapid 33 per cent.
3. The major industries in which women own businesses are service oriented.
4. Women own almost half of all home-based businesses.
5. Women setting up businesses from home is the fastest growing sector of the Australian economy.

6. Women-owned businesses have less external debt, are more profitable and are profitable much earlier than those owned by men.
7. Women starting their own business generally:
   - are aged 26–45 years
   - have sole financial responsibility for the business
   - acquired skills used in their business from previous work experience
   - borrow very little money.
8. The main reasons for women establishing a business include the following:
   - desire to be their own boss
   - wanting greater flexibility in terms of family needs
   - personal challenge
   - an avenue to utilise their skills and talents
   - wanting to achieve financial security
   - experience of restrictions in terms of promotion within a previous career.



FIGURE 11.6 The Women's Network Australia is the nation's leading networking organisation for women offering business information, online services, business education and networking events.
Source: Women's Network Australia

on Resources

Weblink: Women's Network Australia

SUMMARY

- Personal qualities, motivation, experience and entrepreneurship are the primary influences on an individual's decision to establish a business.
- Business qualifications and skills can be attained through experience, education and/or training.
- These factors will affect planning decisions on issues such as the type and size of business, the business location and the individual's own role.
- An entrepreneur is someone who starts, operates and assumes the risk of a business venture in the hope of making a profit.
- An entrepreneur must have a range of skills and characteristics to own and operate a business successfully.
- Other influences are at work, including cultural background and gender.

EXERCISE 11.1 REVISION

1 **Assess** your own entrepreneurial ability by completing the questions shown in figure 11.1 in section 11.2.1. Someone with an entrepreneurial personality would answer 'yes' to most of the questions. Write a self-evaluation report based on your answer.

2 Choose a business you would like to own. **Outline** the personal qualities you think are needed to be successful in this business. Share your response with a classmate and **discuss** the main differences in your answers.

3 Divide a page into three columns as shown on the following page. In the first column, **identify** the skills that you presently possess and could bring to a small business. In the second column, **identify** other skills that you would need to develop. In the third column, **outline** how you would go about obtaining these new skills.

Skills I presently possess	Skills I would need to develop	How I would obtain these new skills

4 Refer to figure 11.4 in section 11.2.3 and **classify** the possible rewards of business ownership into monetary or non-monetary benefits. **Interpret** the results.

5 **Describe** the main characteristics of an entrepreneur.

6 Select the characteristic you regard as the most important and **justify** your choice.

7 **Outline** why an entrepreneur should continually set new goals.

8 Prepare a 'T' table format to **summarise** the benefits and burdens of entrepreneurship. The 'T' table has been started for you.

Benefits	Burdens
• Sense of freedom and independence.	

9 **Determine** which you consider to be more persuasive: the benefits or the burdens. Give reasons for your answer. Share your response with the rest of the class.

10 **Propose** what you consider to be the main reasons for women starting their own businesses.

11 In small groups, brainstorm the problems women face when they attempt to establish and operate a SME. **Outline** your problems to the rest of the class.

12 Conduct online research to answer the following questions.
(a) **Outline** the role of Business Enterprise Centres Australia.
(b) **Describe** some of the services BEC offers.

13 Research online to identify two female entrepreneurs. The **Women's Network Australia** weblink in the Resources tab is a useful resource. **Compare** the main factors that made each business a success.

on Resources

- **Weblink:** Business Enterprise Centres (BEC)
- **Weblink:** Women's Network Australia

EXERCISE 11.1 EXTENSION

1 'The entrepreneur has an important role in the Australian economy.' **Assess** the accuracy of this statement.

2 **Investigate** how the role of women in business changed over the past decade. **Predict** the importance of this role in the future.

3 **Create** a rap song explaining the meaning of 'entrepreneur' and describing the qualities needed to be a successful SME owner.

4 Write out the 12 questions asked in figure 11.1 (section 11.2.1) in order of importance, from most important to least important. **Compare** your list with the rest of the class and be prepared to justify your rankings.

11.3 Sources of information

SME owners cannot be experts in all areas of their business. Further, they do not normally have the funds to employ a specialist or consultant to assist with management. They thus need to possess a variety of skills, including marketing, personnel, finance, administration and public relations skills. Obviously, this multifaceted role is not an easy task. However, the SME owner can receive assistance from a large number of government and private support agencies, examples of which are shown in figure 11.7.

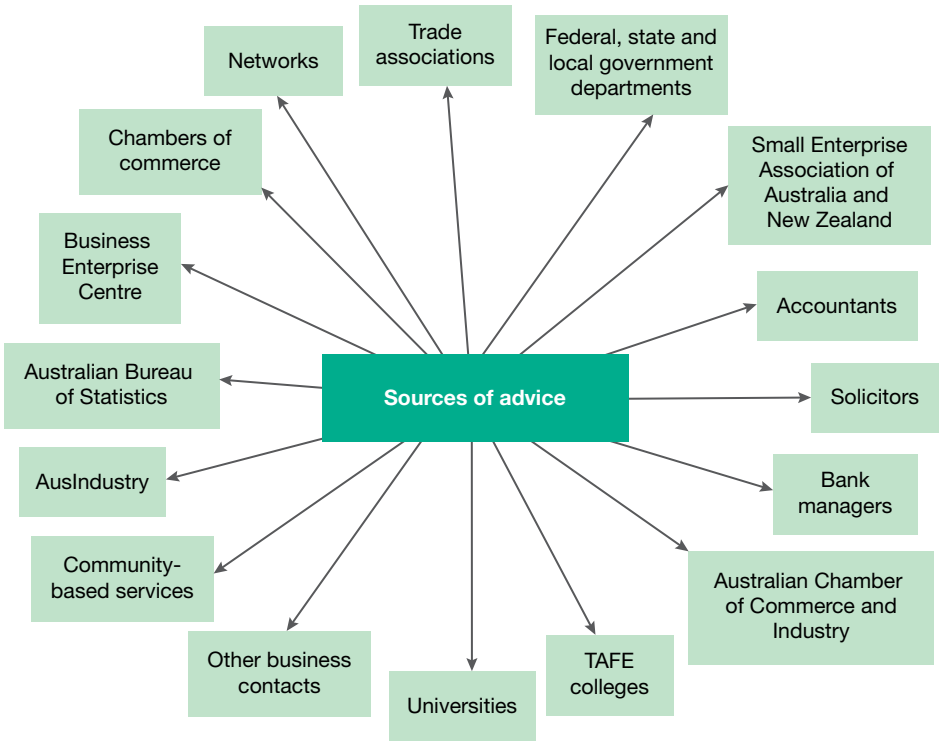


FIGURE 11.7 Sources of help and advice for the SME owner

11.3.1 Professional advisers

It is important for the business owner to have a good relationship with an accountant, solicitor and bank manager, and to keep in touch with them on a regular basis. Management consultants can also be used, especially when restructuring the business or changing its core business activity.

Business owners tend to be totally immersed in the day-to-day operations of their businesses, so they find it difficult to remain objective. However, the professional adviser is able to examine the business much more objectively and provide an independent analysis of the organisation. Professional advisers are also more aware of changes within the legal, economic and financial environment. It is advisable for business owners to make use of the information and advice from the following advisers:

1. **Accountants**. Accountants provide valuable advice on all financial management issues and taxation obligations. They have access to the latest changes to taxation and financial reporting requirements.
2. **Solicitors**. Solicitors provide information concerning business formation and structures, registration, contracts, leases, partnership agreements, patents and legislation. Solicitors are up to date with any changes to company law and can advise the small business owner on how best to deal with such changes.
3. **Bank managers**. The bank manager is another valuable contact who can provide information and advice on financial services, sources of finance and basic business management. The bank manager usually has a wide range of experience to draw on and is able to access the resources of the bank.
4. **Management consultants**. If a business management problem arises that the owner cannot deal with, then the advice of a management consultant may be necessary. Coming from outside the business, the consultant is able to be more objective and view problems in an unbiased manner. When outsourcing to management consultants, it is wise to check their credentials and experience.

11.3.2 Government agencies

State governments

All state governments have established agencies that provide support and advice to business owners. In NSW, the Department of Industry offers a number of programs designed to assist businesses. The main programs are described below.



FIGURE 11.8 The NSW Government's strategy is to make NSW the easiest place to start and grow a business. The strategy demonstrates how the NSW government is unlocking more opportunities for small business. Some key initiatives outlined in the strategy include: enabling better access to cash flow and capital, exploring opportunities for taxation relief, investing in new skills for business and providing tools to build resilient businesses.

Business Connect

Business Connect aims to support small businesses to start up, create jobs through growth, help established SMEs become sustainable and increase business confidence across NSW. Business Connect achieve these aims by:

- providing general and specialist business advice and government information to startups and SMEs
- promoting business growth through innovation, improving resilience and boosting productivity
- supporting digital readiness and regional business development.

Boosting Business Innovation Program

The NSW Government has invested $18 million in the Boosting Business Innovation Program, giving small businesses access to research organisations to build strong local business communities and stimulate economic growth in metropolitan and regional NSW. The NSW Government is working with all 11 NSW universities and CSIRO to deliver a range of new innovation spaces and activities for business communities.

Federal government

The federal government operates a website, business.gov.au, as a service to businesses of all sizes. It is an online government resource for the Australian business community that offers access to all government departments.

business.gov.au offers simple and convenient access to all of the government information, assistance, forms and services businesses need. Government departments such as the Department of Foreign Affairs and Trade, and the Department of Industry provide specific advice and support to businesses on issues such as exporting overseas and research and development of new products.

on Resources

- **Weblink:** Business Connect
- **Weblink:** Boosting Business Innovation Program
- **Weblink:** business.gov.au

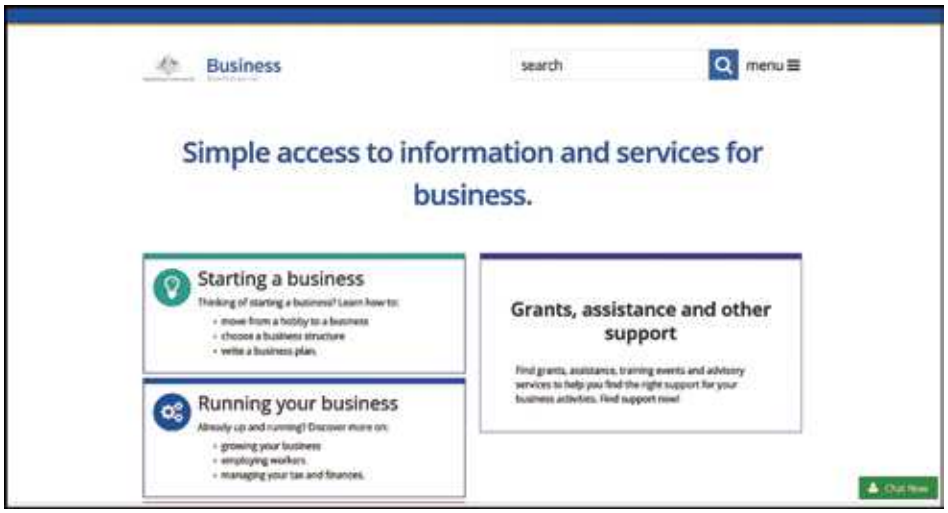


FIGURE 11.9 The federal government website, business.gov.au, is a useful resource for someone establishing, managing or growing a business.

Technological advice

Establishing an online business presence, networking a number of computers within the business premises, or making maximum use of mobile devices can all improve business efficiency. Purchasing equipment from a dealer who offers advice and backup support, or establishing a relationship with an ICT consultant, is another important decision to be made by the prospective business owner. As a technological support service for small business, the federal government has established Digital Business Kits (DBK), which provide industry-specific information and resources to help SMEs and not-for-profit organisations engage in the digital economy and take advantage of the opportunities available through digital technology.

on Resources

Weblink: Digital business kits

Local government

This level of government is becoming more involved in encouraging business because it creates employment. Local councils offer advice on land zoning, assist with subsidised land and consider development applications.



FIGURE 11.10 The Office of the NSW Small Business Commissioner, in partnership with the NSW Business Chamber, launched the Small Business Friendly Councils (SBFC) Program in 2014 to increase the number of NSW councils working proactively with small businesses. Currently, 76 local councils in NSW have joined the Program, demonstrating their commitment to their local small business community.

Source: Office of the NSW Small Business Commissioner

11.3.3 Other sources

Chambers of commerce

Chambers of commerce are local associations of businesspeople, usually centred around a suburb or region. They provide legal and financial help, taxation advice, an explanation of legislation, and industrial relations information. The chambers also organise training seminars, arrange industry conferences and liaise with government departments.

Small Enterprise Association of Australia and New Zealand (SEAANZ)

SEAANZ is a not-for-profit organisation committed to the development and understanding of SMEs within Australia and New Zealand. It is dedicated to research, policy development and the dissemination of ideas relating to entrepreneurship and small business management for the SME sector. They publish a journal, *Small Enterprise Research*, dedicated to small businesses. The association provides a forum for exchanging news and views relating to small business matters. It also organises training days and promotes the role of small business and its importance in the total economy.

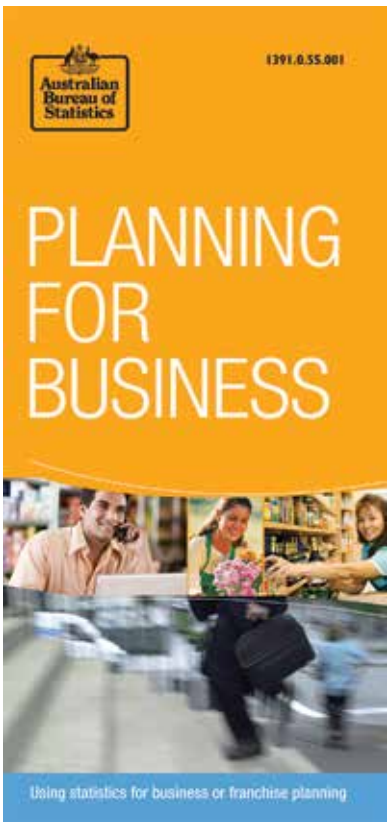


FIGURE 11.11 Whether starting up, or already operating a SME, the Australian Bureau of Statistics provides information to assist making informed business decisions.

Source: © Australian Bureau of Statistics

Trade associations

Trade associations offer specific industry information and assistance. Examples include:

- Australian Retailers Association
- Plastics and Chemicals Industries Association (PACIA)
- Australian Medical Association.

Each association is made up of organisations that are in the same line of business, so it can provide specific details about product development and industry trends.

Libraries and reference material

Libraries are a valuable source of information because they have access to vast amounts of reference material. Most libraries have online access to large databases with search facilities that help locate specific material. Librarians are highly trained and will undertake a search of the literature available. Most libraries also subscribe to trade and industry journals.

Australian Bureau of Statistics

The Australian Bureau of Statistics provides valuable data on social, economic and demographic trends. It also provides specialised data on business activities. Information useful to business owners can be obtained from the following:

- Census on Population and Housing
- Demographic Trends and Statistics
- Household Expenditure Surveys.

Having access to such information assists the business owner in analysing and understanding changes to the external environment.

11.4 The business idea

As well as determining whether or not they have the motivation and personal qualities to start a business, potential SME owners will have a clear idea of what they wish to sell. Sometimes it is an original idea for a good or service that is quite

different from anything already on the market, or a distinct improvement on something already available. Or it may be a realisation that particular goods or services are unavailable in a particular area. All the businesses in the world must have started from an initial idea and then grown according to their success within the market. Coke, for example, started as a medicinal tonic sold off the back of a travelling wagon. Now, Coca-Cola Amatil is an internationally successful business that dominates the soft drink market throughout the world.

The source of a business idea may come from a person's own experiences, interests, abilities or imagination. Inspiration for ideas can be generated by:

- listening to people, particularly for ideas on the goods or services people want, but that may not be readily available
- reading magazines and books, and researching on the internet
- visiting displays and exhibitions in areas such as new technology or new products from overseas
- accessing government statistics and research information
- identifying a 'gap' in the market — that is, a demand not currently being satisfied
- determining improvements that could be made to an existing product.

The successful identification of a gap in the market is a key to establishing a lucrative business. It means that the new business provides something not already available. Breaking into a market that is already well served means that the new business has to do something exceptional to draw customers away from existing businesses. For example, if a shopping centre currently has three hairdressing salons, would a hairdresser be wise in setting up a fourth salon in the same centre? It is unlikely that a gap in the market exists unless the other three hairdressers are so heavily booked that locals find it difficult to make an appointment.

BizFACT

Most new ideas are 99 per cent perspiration and 1 per cent inspiration. This means that a lot of time and effort needs to be put into fully developing a new business concept.



FIGURE 11.12 Visiting a business exhibition can provide ideas for a business concept.

SNAPSHOT



'… she saw a great niche for women's gyms …'

BizWORD

A **business opportunity** *can be described as something an entrepreneur can see as an avenue to success. It is often identified when a person believes they can provide goods or services in a better or different way from those already on the market.*

Case study: Fernwood — a successful business idea

Diana Williams, founder of Fernwood Fitness, was a young, motivated gym fanatic when she saw a great niche for women's gyms in the mid 80's. She was aware of the benefits of strength training but was conscious of the fact that many women avoided the weights area in many male-dominated gyms. She also felt that a lot of gyms weren't the sort of place many women wanted to go to. Her own gym had an unpleasant aroma, weights lying around and a grubby atmosphere. The walls were covered with either men's body building photos or raunchy women's body building photos.

Diana envisaged a girls' club with lovely things women appreciate — like flowers and fresh fruit. She pursued her entrepreneurial idea and, today, Fernwood Fitness is a household brand that has 69 clubs across Australia, employs more than 2000 people, has over 80 000 members and an annual turnover of more than $75 million.

When Diana started her first club, she had no business experience; simply a desire to provide an exercise venue for women only. Initially, Diana did not intend to begin a major national brand, she wanted to establish a small business that she was passionate about and could enjoy running. Fernwood Fitness provides women with an alternative to working out in a mixed-gym environment.

From the first club, Diana prioritised and focussed on member service, staff satisfaction, quality and cleanliness. Understanding the needs of women today and tailoring the business's services to cater to their needs has given Fernwood a competitive advantage. These aspects are the reasons behind Fernwood Fitness' overall success.

SNAPSHOT QUESTIONS

1. **Outline** the source of Diana's business idea.
2. Besides the original business idea, **describe** some other factors that have contributed to the success of Fernwood Fitness.



FIGURE 11.13 A Melbourne couple, Phillis Chan and Ben Chaung came up with the idea for their Big Apple Buddy business after relocating to the US four years ago. When they moved, many of their friends kept asking them to send things that they couldn't get in Australia. This led to the idea for their new business that ships hard-to-get American products to Australia. The couple have made over $3 million since setting up their business.
Source: Phillis Chan and Ben Chaung

11.4.1 Identifying business opportunities

Identifying a **business opportunity** is not just about having an idea. An opportunity is something that a person can see as an avenue to success. It is often identified when a person feels they can provide goods or services in a better or different way from that already in the market. There are many ways of identifying an opportunity, for example:

1. Analysing and reviewing particular parts of the market to find an opening for particular goods or services. Sometimes, you can find the best opportunities by seeking those goods or services that larger businesses are unable or unwilling to provide to their customers. Angela, for example, may want to open a plant nursery, but she is afraid that the larger nurseries will be able to undercut her prices in most products simply because they can buy in bulk. Angela could concentrate on the provision of services — maybe plant delivery services, landscaping, garden consultations, soil testing and more — which the larger nurseries tend to overlook.
2. Identifying whether many other people share a particular interest or hobby. This interest or hobby may become the main catalyst in identifying a business opportunity. An individual is not always driven by the motive to make a profit, but rather by a belief in the product itself. The most important issue is that such interest does not always equal success. There must be a large enough market to sustain sales of the product or service.

Once a business opportunity is identified, a number of areas need further investigation before the business opportunity becomes a reality. The most important of these is a consideration of the competition.

11.4.2 Competition

Competition is rivalry among businesses that seek to satisfy a market. When identifying a business opportunity, the entrepreneur must decide on the type of market in which their goods or services will compete. This means deciding whether to target the goods or services at a broad market (mass market) or a more specialised market (niche market). Once this decision is made, the business owner is able to identify the level of competition and the main competitors.

The business owner must then decide how to make the business competitive or, more simply, how to develop a customer base or gain a market share from its competitors. Again, the type of market will influence the strategies used by a business. If the product is aimed at a niche market, for example, then there may be no competitors. On the other hand, a mass-market strategy will require extensive planning to create market share. There are two main ways of achieving competitiveness — cost of production and differentiation of the goods or services.

1. Cost will largely depend on production techniques. The business that can produce a good or service at the lowest possible cost and thus sell at the lowest price has the greatest ability to attract market share.
2. Differentiation is about making a product or service different, unique or better than its rivals — for example, selling a computer with extra service, lessons or added software.

Competitive advantage is discussed in more detail in chapter 13.

BizWORD

Competition *is rivalry among businesses that seek to satisfy a market.*

SUMMARY

- A variety of support services exist to provide assistance to a business owner who lacks experience. Some of them are free and some are in the form of other businesses that charge for their services.
- A business idea describes the core activities of the business, and the specific features and value of the goods or services it provides.
- A business opportunity is something an entrepreneur can see as an avenue to success.
- Opportunities may arise due to either a 'gap' in the market, or an interest or hobby.
- Competition is rivalry among businesses that seek to satisfy a market.
- SME owners must decide how to make a business competitive. This can be done by either reducing the costs of production or providing something not already available.

EXERCISE 11.2 REVISION

1 (a) **Recall** the professional advisers a business owner should have a good relationship with.
(b) **State** the information each one provides.

2 **Examine** the range of information provided by the business.gov.au website.

3 Jamahl wishes to set up a hot bread shop in his local shopping centre. **Identify** five government agencies or organisations he could approach for support.

4 Use the **Business Connect** weblink in the Resources tab to answer the following questions.
(a) **Outline** how Business Connect supports startups and SMEs.
(b) Click on 'Success stories'. Select a success story from the list and **explain** how Business Connect assisted the SME.

5 There are many ways of coming up with an idea for a business. The following table provides some examples. In small groups, **propose** one suggestion of your own for each example given.

on Resources

Weblink: business.gov.au
Weblink: Business Connect

Source of idea	Example	Your suggestion
An inspiration	A self-filling printer cartridge	
Listening to people	A skateboard facility	
Noticing a gap in the market	A home gardening service	
Own interests and abilities	A graphic design consultant	
Improving an existing product	A better video store	
New technology	A mobile HDTV screen	
Developing a hobby	Making ceramic pottery	
Combining two existing ideas	Antiques/coffee shop	
Social trends	Home-cooked, prepared meals	
'Crazy' ideas	A musical hair dryer	

6 **Define** the term 'business opportunity'.
7 **Summarise** two ways of identifying a business opportunity.
8 Choose a business — large, medium or small. **Identify** its main competitors.
9 Keeping ahead of the competition is essential for long-term business success. **Recommend** five strategies a café can use to keep 'on top' of its competitors.

EXERCISE 11.2 EXTENSION

1 Arrange for a representative of the local chamber of commerce or the local traders' association to visit your class. Before the visit, prepare a number of questions to ask the representative on issues relevant to both informal and formal support services provided for local business owners. If possible, video record the session (obtain the visitor's permission in advance). **Create** a 500-word report on what you learned from the visit.
2 'The business idea is the starting point for any new small business.' **Explain** this statement.
3 When commencing a new small business, **justify** which of the following you think might be the most important.
(a) the money required to commence the business
(b) the development of the business idea
(c) the skills of the people who will operate the business.
4 Choose a good or service you could provide/invent that is (to your knowledge) not already available.
(a) **Clarify** why you chose this good/service.
(b) **Predict** its chance of success.

BizFACT

Seventy per cent of all new businesses start from scratch, while 26 per cent are purchasers of existing businesses. The remaining 4 per cent are businesses that have either been inherited from a family member, restarted from a previously failed business, or bought by the employees from the owners.

11.5 Establishment options

There are three ways of establishing a new business:
1. setting up a new business from scratch
2. purchasing an existing business
3. purchasing a franchise.

Choosing between these options is sometimes quite difficult; each has advantages and disadvantages (see the Snapshot in section 11.5.3).

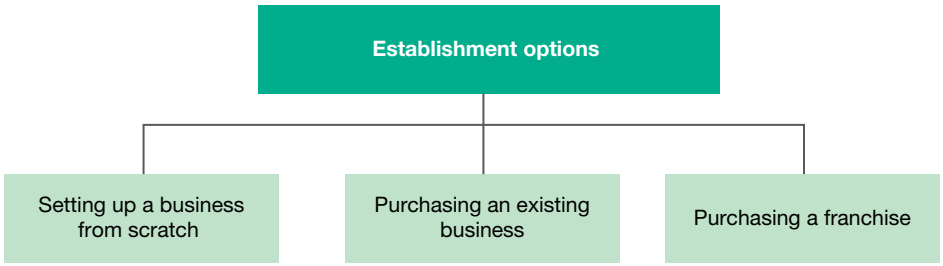


FIGURE 11.14 Many prospective small business owners find it difficult to select an establishment option. Each option has its own advantages and disadvantages, which must be taken into consideration before making a decision. A wrong choice may place the owner in a vulnerable position.

11.5.1 Setting up a new business — starting from scratch

Sometimes conditions are more favourable for starting a new business than for buying an existing operation, for example:

- when a person has created something unique and starts a business to market their innovation or invention
- when a person recognises a gap in the market, where it is clear that customers' needs are not satisfied by existing businesses
- when the market has grown and existing businesses cannot supply all customers.

If these conditions do not exist, then starting from scratch could be more difficult because existing SMEs will provide considerable competition.



FIGURE 11.15 Steve Takchi started his business Path to Health from scratch to pursue his dream of getting people moving and enjoying a quality life without pain. He wanted to create a one stop shop for health and osteopathy that offers personalised healthcare and a holistic approach, while also considering the complete person (physical, psychological and spiritual) in the management of the problem.

Advantages and disadvantages

Starting from scratch has advantages and disadvantages (see table 11.1).

TABLE 11.1 The advantages and disadvantages of starting a business from scratch

Advantages	Disadvantages
• The owner has the freedom to set up the business exactly as they wish. • The owner is able to determine the pace of growth and change. • There is no **goodwill** for which the owner has to pay. • If funds are limited, it is possible to begin on a smaller scale.	• There is a high risk and a measure of uncertainty. Without a previous business reputation, it may prove difficult to secure finance. • Time is needed to set up the business, create procedures, develop a customer base, employ and train staff, and develop lines of credit. • If the start-up period is slow, then the business may not generate profits for some time.

BizWORD

Goodwill *is the monetary value attached to the reputation of a particular business.*

11.5.2 Buying an existing business

BizFACT

If you are buying an existing business, the financial information about the profitability of that business must be fully investigated. According to the Australian Competition and Consumer Commission, if the vendor is reluctant to disclose the full financial details of the business it is better not to purchase it. Buying a business is just like buying a house — a huge cost is involved and the foundations of both must be sound.

When an existing business is purchased, the business is already operating and everything associated with the business is included in the purchase — for example:

- stock and equipment
- premises
- existing customer base
- staff
- location
- reputation and goodwill.

When purchasing an existing business, it is essential for the potential purchaser to know why the business is for sale. If the business has been struggling, it may not be a very good purchase. It is also important to examine detailed accounts for at least the previous three years to determine the financial health of the business. The true value of goodwill is one aspect of the financial statements that is often hard to estimate. The seller of the business may overestimate the value of the business's reputation; therefore, consultation with an accountant is important to confirm the accuracy of the value placed on goodwill by the seller.



FIGURE 11.16 Sam Dimartino purchased an existing business because he believed it would be easier than setting up a new business from scratch. The existing suppliers, equipment and customers helped Sam generate instant income.
Source: © Sunrise Mobile Cafe

Advantages and disadvantages

Buying an existing business has a number of advantages and disadvantages, as shown in table 11.2.

TABLE 11.2 The advantages and disadvantages of buying an existing business

Advantages	Disadvantages
• Sales to existing customers will generate instant income. • A good business history increases the likelihood of business success. • A proven track record makes it easier to obtain finance. • Stock has already been acquired and is ready for sale. • The seller may offer advice and training. • Equipment is available for immediate use. • Existing employees can provide valuable assistance.	• The existing image and policies of the business may be difficult to change, especially if the business had a poor reputation. • The success of the business may have been due to the previous owner's personality and contacts, so may be lost when the business is sold. • It may be difficult to assess the value of goodwill, with the likelihood that the newcomer will pay more than it is worth. • There may be hidden problems. • Some employees may resent any change to the business operation.

BizWORD

A **franchise** *involves buying the rights from another business to distribute its products under its name.*

A **franchisor** *is an individual or business that grants a franchise.*

A **franchisee** *is an individual or business that purchases a franchise.*

11.5.3 Buying a franchise

Under a **franchise** agreement a person buys the rights to use the business name and distribute the products or services of an existing business. The business that grants the right to others to use its name and products is known as a **franchisor**, while the business that buys those rights is known as a **franchisee**. The franchisor supplies a known and advertised business name, the required training and staff development, a method of doing business, management skills and materials. The franchisee supplies the startup money and labour, operates the franchise business and agrees to abide by the terms and conditions of the franchise agreement.

People choose to buy a franchise in the hope of avoiding many of the problems of starting a new business. For a set fee, the small business owner receives the benefits of a successful business formula, a well-recognised name and established trademarks. Franchising has a success rate of almost three times that of independent businesses, largely because it involves an established business name backed up by managerial expertise. Franchising is the area of fastest business growth in Australia. Subway® (sandwiches and salads) is an example of a franchise. Other well-known franchises include McDonald's, Optus 'Yes' stores, Dymocks bookstores, 7 Eleven, Bakers Delight, Domino's Pizza and The Athlete's Foot.

on Resources

Weblink: Franchise Business

BizFACT

In 2016, Poolwerx, Australia's largest pool and spa maintenance franchise, was named Established Franchisor of the Year by the Franchise Council of Australia. It might be 24 years since the company was established, but they show no signs of slowing down. Poolwerx hit 100 stores in 2016 and are predicting that, with the current level of growth, they will more than double their business in the next nine years. The CEO and founder, John O'Brien, anticipates they will reach 350 stores and 1000 vans by 2025.

Advantages and disadvantages

Buying a franchise has a number of advantages and disadvantages, as shown in table 11.3.

TABLE 11.3 The advantages and disadvantages of buying a franchise

Advantages	Disadvantages
• Immediate benefit is derived from the franchisor's goodwill because the name is established. • The franchisor often provides training and management backup. • A franchisee can succeed despite having limited experience. • Equipment and premises design are usually established and operational. • Well-planned advertising often exists. • Volume buying is possible, often resulting in cheaper stock. • A business plan and proven business methods already exist.	• The franchisor controls the operations, with little scope for franchisee individuality. • Profits must be shared with the franchisor through the payment of ongoing franchise fees. • The franchisor often charges additional service fees for advice. • The franchisee is often required to purchase stock from the franchisor and cannot shop around for cheaper supplies. • Contracts may be biased in favour of the franchisor. • The franchisee must share any burden of the franchisor's business mistakes.

BizFACT

According to a report of the Franchise Council of Australia in 2014:
– there were 1160 franchisors in Australia in 2014
– there were an estimated 79 000 franchisees
– more than 460 000 people were employed directly in franchising
– annual sales turnover of the entire franchising sector was estimated at $144 billion.



FIGURE 11.17 Many well-known businesses operate under a franchise agreement.

SNAPSHOT



'Without a strong, proven brand, many start-up businesses struggle to succeed.'

Case study: Mortgage Choice — a successful franchise

An interview with Maria Zappia, owner of Mortgage Choice Gladesville.

Maria, what made you want to start your own business?
I had been working within the business as a broker for a number of years. This experience helped me to gain a very good understanding of the business; the upsides as well as the downsides. When the opportunity to purchase the business came up, I put together a detailed business plan and five-year projections to check the viability of purchasing the business myself. Putting together the business plan highlighted for me where the risks lay, but at the same time, it helped me realise a number of potential opportunities to exploit.

What other business planning did you undertake prior to making the decision to purchase the franchise?
Cost was a major consideration so it was critical to put together a detailed budget that took into account not only the obvious on-going costs such as rent, staff salaries, and general day-to-day running costs, but also had to allow for changes in the business going forward.

I also had to do a SWOT self-analysis to gauge my ability to not only work 'within the business' (as a productive and income generating broker) but also 'run the business' (as a business owner looking after staff, premises and cash flow). One of the challenges for people that transition from being an employee of a business to being the owner of the business is that they need to develop both the mind-set and

the organisational skill to allow time to 'work **within** the business' and 'work **on** the business'. This is an on-going challenge.

When establishing your business, why did you decide to purchase an existing franchise as opposed to establishing a new business?
Buying an established business has its risks, one of main risks being customer and staff loyalty. Having worked within the business for a number of years, I had built a large base of established clients. These were people I knew well, having built relationships and trust over time. In addition (and very importantly) these established relationships were providing repeat and referral business. It made the transition rather seamless for most of our clients and also for me.

The main reason I decided to purchase a franchise was to leverage the benefits of the established brand. Without a strong, proven brand, many start-up businesses struggle to succeed. Mortgage Choice was going from strength to strength and I wanted the added value of a strong and reputable consumer brand as well as the support services that go with the brand.

Another reason I decided to purchase a franchise was to leverage the benefits of Mortgage Choice's well-established market-share. A number of marketing activities performed over several years prior to me purchasing the franchise had lifted local presence and local market share.

What are the advantages of operating a franchise?
1. 'Sameness' and presenting a 'united front' across the network has its advantages with regard to marketing activities, advertising and branding.
2. You are part of a strong brand and can leverage off the strength of the brand.
3. You are part of a large multinational network which competes with other providers for market share.
4. Licencing and regulatory requirements are met by regular compliance audits conducted by the franchisor. Regular training programs and appropriate processes and procedures are provided to ensure compliance.
5. Opportunities provided by the franchisor to diversify into financial planning, car and equipment finance, personal loans, specialist property referrals, and so on. These opportunities to diversify help the franchisee to develop additional income streams and to better meet the needs of clients as a whole, rather than just the home loan.

Are there any disadvantages of operating a franchise?
1. Possible disagreements with the franchisor regarding marketing and advertising; not so much at the local level, as there is always more control over this, but more so nationally. There could be an adverse effect on branding if the franchisor doesn't quite get it right. This is minimised if the franchisee has some input in the formulation of the marketing strategy.
2. Remuneration/commission policies need regular review in the broking industry and we are reliant on the franchisor to set fair and equitable policies with regard to this.
3. There isn't much scope for 'individuality' when it comes to running the business. The whole purpose of belonging to a franchise network is that everyone gets on board with systems and processes, marketing and advertising etc.

What support do you receive from the franchisor?
- Marketing and IT support
- Assistance with compliance and regulatory obligations
- Franchise development support
- Training and development/CPD opportunities: Mortgage Choice offers an intensive two-week induction training course at their head office in North Sydney. In addition, each franchisee is assigned a mentor for their first two years in operation under the Accelerate Program. The mentor is an important and valuable support as it can be hard to quickly absorb all the product knowledge required. This program provides continuous web-based and face-to-face training and development for the whole two-year period.

- Troubleshooting with our lender panel and assistance sorting out any problems with the banks.
- Often lenders make changes to their credit policies, rates, special offers, processes etc. When these changes occur, this is communicated to the network and the Mortgage Choice systems are updated to reflect these changes.
- Mortgage Choice also offers an excellent support system via their Group Office staff. I have daily access to Mortgage Choice's lending support team and the marketing, public relations and finance teams whenever I need them.
- The franchise network is also supported via a comprehensive intranet site. This contains an extensive array of information and resources including marketing material, public relations tools and content, business operations, budgets and just about anything to do with running a mortgage broking business.

SNAPSHOT QUESTIONS

1. **Recall** what motivated Maria to start her own business.
2. **Explain** the benefits of operating a franchise.
3. **Assess** Maria's decision to purchase an existing franchise as opposed to the other establishment options.

SUMMARY

- Starting a completely new business, purchasing an existing business or purchasing a franchise are the three main ways of going into business.
- The most common reason for setting up a completely new business is the recognition of a gap in the market.
- When purchasing an existing business, it is essential for the potential purchaser to know why the business is for sale.
- People choose to buy a franchise in order to make use of an existing brand and reputation.
- There are advantages and disadvantages for each option.

EXERCISE 11.3 REVISION

1 **Recall** in what circumstances someone might choose to start a business from scratch.

2 **Identify** and **explain** what you consider to be the two most significant advantages and two most significant disadvantages of starting a business from scratch.

3 **Identify** and **explain** what you consider to be the two most significant advantages and two most significant disadvantages of purchasing an existing business.

4 (a) Assume you have decided to purchase an existing small business. Select one of the following advertisements and **propose** a list of questions that you should ask before making a purchase.

(b) **Justify** which business offers the best prospects. Give reasons for your answer.

SOUND ESTABLISHED HAIRDRESSING SALON

Well equipped.
Established over 10 years.
Sound financial position.
Taking approx. $2500 p.w.
No goodwill required.
Pay only for premises, fittings and stock.
Excellent opportunity.

Phone 3856 2764

ATTENTION

Sack your boss.
Work from home instead.
Phone (03) 9856 2764
www.lastchance.com.au

SOUND INVESTMENT

Established Convenience Store – Beach Location
Once-in-a-lifetime opportunity to be your own boss.
Easily managed. Training provided.
Low rent only $770 per week.
Current t/over exceeds $5200 per week.
Increases in summer. Price includes fixtures and fittings, the shop plus 4 bedroom residence.

ASKING PRICE $915,000
Phone 0421 01516 7934 AM

5 Consider a small business that you would like to start. **Recommend** which of the three business options would be most appropriate. Give reasons for your answer.

6 **Investigate** why people choose to purchase an established business rather than start from scratch. Compare your answer with other class members.

7 **Outline** the factors potential business owners should consider when buying an established business. Use the federal government's **business.gov.au** weblink in the Resources tab as a reference.

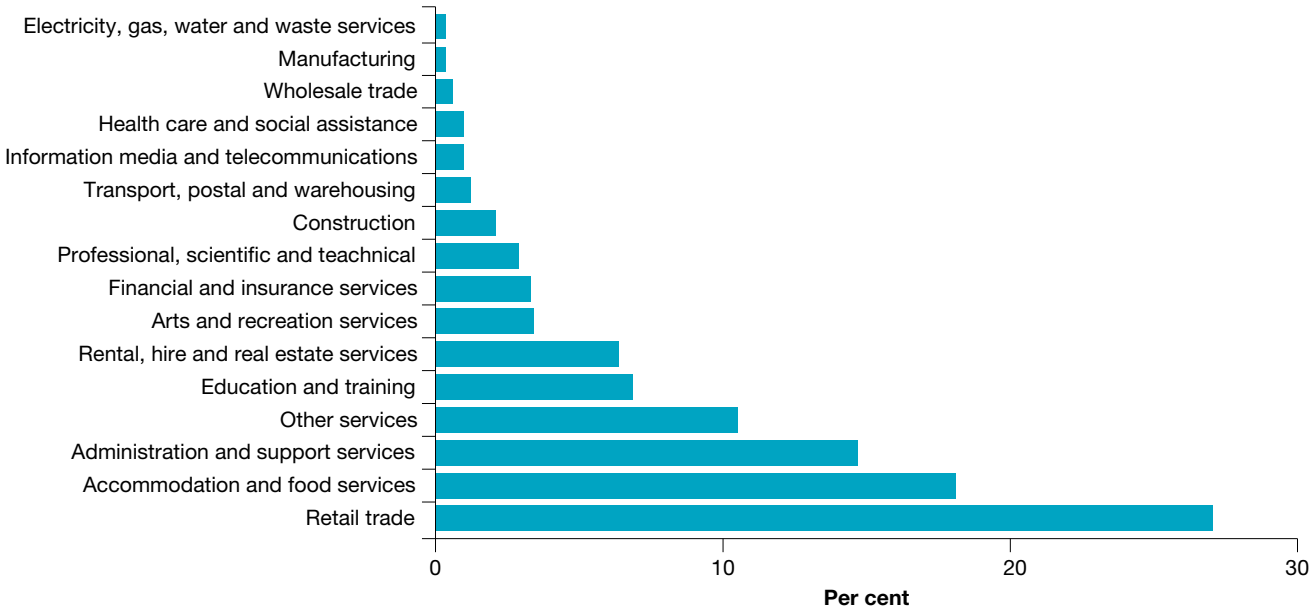
8 The Red Rooster restaurant franchise mission statement is 'Be in business for yourself, but not by yourself'. **Explain** what is meant by this statement.

9 **Clarify** why businesses operating as a franchise have a success rate three times that of independent businesses.

10 **Identify** what the franchisor receives in a franchise agreement. **Identify** what the franchisee receives. **Identify** what each party provides.

11 **Determine** one main benefit of franchising for the:
(a) franchisor
(b) franchisee.

12 The graph below indicates the proportion of franchise units held by franchisors in each industry segment. Use this graph to answer the questions that follow.



(a) **Identify** the industry sector in which the majority of franchise networks are involved.
(b) **Why** do you think the majority of franchises operate in the industry you identified in part (a)?

on Resources

Weblink: business.gov.au

EXERCISE 11.3 EXTENSION

1 Read the following story and then answer the questions.

Bianca was bored working for someone else and decided to start her own business. She lives in a small New South Wales country town with a population of approximately 2500. The town has no major shopping centre and no established franchises. Bianca decided to open a café in the town. Her mother provided the funding for the business and gave her what little advice she could.

After only six months in business, Bianca realised that the business was not profitable. Her debts were increasing and she could see no way out of her problems. She wanted to sell the business but could not find a buyer.

(a) **Determine** whether it would have been wiser for Bianca to purchase an established business rather than commencing from scratch. Give reasons for your answer.
(b) If Bianca had conducted some basic market research, **predict** whether she would have opened a franchise instead of an independently owned business.
(c) **Propose** what Bianca should do. Share your answer with other class members.

2 From the 'Businesses for sale' section of a newspaper, find three advertisements for the sale of a corner store, newsagency or coffee shop. **Explain** all the terms used in the advertisements.

3 Select a small business that you patronise regularly and answer the following questions:
(a) **Outline** why you use this particular business.
(b) **Identify** the strengths and weaknesses of this business.
(c) If this business were for sale, **determine** whether you would consider purchasing it. Give reasons for your answer.

4 **Compare** three franchise operations that interest you (the Franchise Council of Australia website is a useful starting point) and then answer the following questions:
(a) **Summarise** the business's concept.
(b) **Identify** the training provided by the franchisor.
(c) **Outline** the agreement terms.
(d) **State** the level of investment required.
(e) **Describe** the personal qualifications required.
(f) **Assess** which franchise operation you consider to be the best business proposition. Give reasons for your answer.

5 **Create** an information brochure on franchises. Include useful facts, and useful organisations and websites that will assist a potential franchise.

on Resources

Weblink: Franchise Council of Australia

11.6 Market considerations

Many business owners are so enthusiastic about starting that they often overlook these three crucial questions:

- What good and/or service will be sold?
- What is the most suitable price for the goods or service?
- What is the most appropriate location for the business?

More than anything else, the success of any business depends on the research and planning done to answer these three fundamental questions, because sales are the life-blood of a business and the source of its income.



FIGURE 11.18 Market analysis is important to ensure that the good or service provided is likely to satisfy consumers and that the business is aware of the threats and opportunities the market presents. Understanding the market will help business owners identify many different factors that can have an impact on their business.

11.6.1 Goods and/or services

One of the first decisions potential business owners need to make is to determine what they are going to sell. When starting a business, it is very important that the owners possess the knowledge and experience required regarding their good or service.

Many SME owners display such enthusiasm for their new goods or service that they often fail to consider whether any customers want to purchase it. Without customers, a good or service — even though revolutionary, efficient, record-breaking, exciting and so on — is useless. Businesses fail without a market (customers) for their goods or service; therefore, they must always undertake market analysis.

Market analysis involves collecting, summarising and analysing information about the state of the market, customers, the threats and opportunities that the market presents, and any advantages or disadvantages that the business is likely to have over its competitors.

Using a variety of methods, such as surveys, questionnaires and focus groups, market analysis can provide a wealth of information about customers' attitudes, perceptions and opinions. It presents a business owner with questions that focus on who will buy the product, for example:

- Who are our customers?
- What do we know about them?
- What is their age and gender?
- Why do they buy our product(s)?
- What do they see as our strengths and weaknesses?
- How can we gain more customers?
- Who are our competitors? How many do we have?
- What do our competitors offer that we do not?
- What are we really selling?
- To whom would we like to sell?

BizWORD

Market analysis *involves collecting, summarising and analysing information about the state of the market, customers, the threats and opportunities that the market presents, and any advantages or disadvantages that the business is likely to have over its competitors.*

11.6.2 Price

One of the most crucial decisions that any business owner has to make is to determine the prices at which goods and services are provided to customers. This will have a major impact on the success of the business, as prices set too high may drive away potential customers, while prices set too low may make it difficult to achieve a profit.

As discussed in chapter 8, three pricing methods can be used:

1. *Cost-based:* a pricing method derived from calculating the total cost of producing or purchasing a product and then adding a mark-up for profit.
2. *Market-based:* a method of setting prices according to the interaction between the levels of supply and demand — whatever the market is prepared to pay (see figure 11.19).
3. *Competition-based:* choosing a price that is either below, equal to or above that of the competitors.



FIGURE 11.19 It's important for a business to know what customers think they should be paying for a product or service. Customers may see good value from something that isn't expensive to make or deliver. To set a price to simply cover costs in this instance will be denying the owner lots of potential profit. If a product or service is more expensive to provide than customers are prepared to pay, then that too is a problem. Market research can help owners find out what their customers are prepared to pay.

11.6.3 Location

Different types of businesses will be suited to different locations, and the business owner must consider a number of factors when determining the most appropriate location for their particular

business (refer to chapter 3). A suitable location might be a shopping centre or retail shopping strip, or the business owner may choose an online presence or prefer a home-based business.

Local government **zoning** determines where some types of businesses can operate. Zoning is designed to keep business activities separate from residential areas and prevent householders being disturbed by businesses operating late at night. The process sets aside commercial and industrial zones and it is in these areas that most SMEs will operate.

BizWORD

Zoning *is a means by which local councils allocate land for different uses, such as residential, commercial, recreational and industrial.*

Shopping centre complex

The suburban shopping centre complex has been in existence in Australia for less than 50 years. Typical suburban shopping centre complexes have one or more supermarkets and a number of small specialist stores such as hairdressers, clothing stores, pharmacies, cafés, newsagents, and often a post office and bank branches. Larger regional shopping centres, such as Macquarie Centre, Centro Roselands, Westfield Bondi Junction and Warringah Mall often include major department stores and cinemas, as well as the full range of specialist retail outlets.

Although it can be quite expensive, a well-established business in a busy shopping centre is an excellent option for a prospective SME owner wishing to purchase an existing business, although a new business in an established shopping centre is most likely to be successful if there are no existing competitors.

BizFACT

The average rent for businesses in Westfield shopping centres is $1326 per square metre.

Retail shopping strips

In metropolitan Sydney, shopping strips developed along major arterial roads during the second half of the 19th century. The busiest shopping strips were located near public transport, such as tram routes and suburban railway stations. Parramatta Road is an example of a major road in Sydney with extended shopping strips.



FIGURE 11.20 According to a recent report by real estate firm Cushman & Wakefield, Sydney's Pitt Street Mall is ranked as the seventh-most expensive in retail rent globally. The average rent on Pitt Street Mall is $13 335 per square metre. Of course, that's just an average; some shops with a street frontage are paying much more than that. New York's Upper 5th Avenue retained top position, Hong Kong's Causeway Bay ranked second and Paris's Champs-Élysées ranked third.

Many shopping strips in the metropolitan area have struggled to compete with the growth of shopping centre complexes offering off-street parking and an air-conditioned environment. Retail shopping strips offer the advantage of high visibility for passing traffic, but many shopping strips suffer from lack of parking, particularly those located on major arterial roads that are clearways during peak hours. Because many shopping centres close in the evenings, shopping strips have become popular locations for restaurants and 'after hours' entertainment. Norton Street in Leichhardt is a good example of this.

on Resources

eLesson: Sublime Greengrocer and Juice Bar (eles-0839)

Online presence

Given the rapid rise in technology, many businesses do not consider their location as important at all. Most SME owners have the use of a computer and access to the internet. This allows for the possibility of conducting business online, so the business is no longer limited to dealing with people who can physically visit its premises. Such online activities can include:

- using email to communicate with customers or suppliers
- using the internet to find information, such as prices, business contact details, and different products and market trends
- setting up a website to provide information about available products and services, or as a means by which customers can order goods online
- using the internet for online banking and payment of bills.

What's the true cost of an online store vs a physical shop?

Too often I see people jumping into their online store dream without treating it with the proper preparation and respect it deserves.

Trying to get something done on the cheap, yet expecting quick, big results.

You need to ask, would you be doing this if you were embarking on running a physical shop?

The success of an online business really depends on the right investment of time, money and resources into setting up the most effective e-commerce shop for your business.

When starting up an online business, it can sometimes be easy to forget that the hard-earned money you are investing into your new e-commerce store needs to be compared to that of a physical street front shop.

So what really is the true cost of an online store versus a physical shop? Let's try to work that out.

As there are so many variables, in my research I have tried to compare running a small and effective online shop with that of a comparable local small-sized shop.

For the sake of this exercise, let's assume both businesses are selling fishing rods to people in Sydney. And let's further assume both businesses sell about 500 different products and make a 50 per cent profit margin.

Sound fair?

Ok let's set the scene . . .

Business A: Street Front Fishing Rod Shop

Business A employs 2.5 full-time staff to man the shop and rents a $4000/month, 100 square metre shop on a main road in Sydney.

As it is on the main road, Business A gets plenty of street visibility and loads of walk-in customers. Its main customers are really limited to the local area, as it rarely gets customers from further afield.

Let's also say Business A has an annual revenue target of $550 000.

Business B: Online Fishing Rod Shop

Business B, being an online business, only needs to employ 1.5 full-time staff, and runs its business from home.

Having no physical store, Business B also rents out a double car garage-sized storage for $400/month for its products.

Being an online business, Business B needs to put quite a lot of energy into promoting its products online through paid digital marketing. Also, being an online business, they sell to customers all around Australia.

Let's say Business B has a smaller annual revenue target of $350 000.

General costs

Of course, there are a range of general costs that businesses need to pay, regardless of whether they have an online presence or a street front shop.

SNAPSHOT



'… what really is the true cost of an online store versus a physical shop?'

Some of these costs include:

- purchase of inventory
- insurance, licences, registration etc
- bank fees, workers' compensation etc.
- logo and other graphic design.

Set-up costs

So what are the costs to set up each business?

Let's compare the initial investment both businesses need to make to get up and running.

(Please note, these exclude the above general costs and, for the sake of this exercise, I am assuming that Business A is taking over an existing premises, hence doesn't need to build a brand new shop.)

Business A: Street Front Shop
Shop fit-out: $50 000 (typically $30 000 to $150 000)
Shop signage: $3000 (Typically $2000 to $10 000)
Other: $2000
Total: $55 000

Business B: Online Shop
Website: $12 000 (typically $5000 to $25 000)
Photography: $2000
Other: $1000
Total: $15 000

Monthly ongoing costs

Business A: Street Front Shop
Rent: $4000 (typically $3000 to $6000)
Electricity and rates: $400 (typically $300 to $800)
Other: $500
Staff (2.5): $12 500 (based on $60k/yr per FTS)
Total: $17 400/month

Business B: Online Shop
Website hosting and support: $150 (typically $100 to $300)
Digital marketing and promotion: $3000 (typically $500 to $5000)
Stock storage rent: $400 (typically $300 to $500)
Other: $500
Staff (1.5): $7500 (Based on $60k/yr per FTS)
Total: $11 550/month

Summary

Here is a summary of how the costs affect each business.

Set-up cost

As you can see the cost for setting up the physical store for Business A is about $55 000 compared to only $15 000 for setting up an online store for Business B. That equates to a saving of $40 000 which could easily be put towards promoting Business B online!

Ongoing costs

Business A has $17 400 of expenses to cover each month. At a profit margin of 50 per cent, Business A would need to sell over $36 000 in sales every month to break even.

This means Business A needs to be doing $550 000 in annual revenue to run a stable business.

In contrast, Business B has $11 550 in monthly expenses, therefore would need only $23 000/month in sales to break even. This means Business B would need to aim for $350 000 in annual revenue to run a stable business.

As you can see, it is nearly $6000 cheaper per month to run the online store business. And the annual turnover is a whopping $200 000 less to be a stable business.

Overall

The lesson to be learnt here is that it is quite important to make sure you compare the costs for your online store with those of a physical store.

Clearly, it can be far cheaper to run an online business than a street front shop.

But you need to remember you will need to put extra effort into both your website and ongoing online promotion to succeed!

Source: Kevin Fouche

SNAPSHOT QUESTIONS

1. **Identify** the factors that the success of an online business depends on.
2. **Identify** some general costs that will be common to both an online and a physical store.
3. **Compare** the set-up and ongoing costs of an online and physical store.

Home-based businesses

Many tradespeople and other service providers have traditionally run their businesses from home. Plumbers, electricians, painters and various other service providers do not need a dedicated business location as they provide services in the customer's own home or business premises. Increasingly, the development of information and communication technologies has allowed home-based businesses to use mobile phones, the internet and computer applications. Although home-based businesses have traditionally been service providers rather than goods retailers, online ordering and payment has allowed for the expansion of home-based retail businesses.



FIGURE 11.21 Almost one million people run a business from home in Australia. Working from home can offer flexibility and convenience, and can often be a great opportunity to start a new career. Computers and the internet have increased the potential for home-based businesses.

on Resources

Weblink: Home-based businesses

SUMMARY

- The first thing business owners need to determine is what good or service they are going to sell.
- Businesses fail without a market (customers) for their goods or services, so they must always undertake a market analysis.

- A market analysis involves collecting, summarising and analysing information about the market.
- Price can be set by using the cost-based, market-based or competition-based pricing methods.
- One of the key decisions of a prospective small business owner is concerning the actual location of the business.
- Different types of business will be suited to different locations.

EXERCISE 11.4 REVISION

1 **Clarify** the purpose of a market analysis.

2 **State** the methods a SME owner could use to gather information about customers' attitudes, perceptions and opinions.

3 From the following table, **identify** the appropriate number (event) and letter (price-setting method).

Event	Method of setting prices
1. A house is sold at auction.	(a) Cost-based
2. A percentage is added to the cost price of the goods.	(b) Market-based
3. The butchers all copy the prices of Mighty Meats.	(c) Competition-based

4 **Calculate** the selling price for a computer using the mark-up supplied.

Computer cost price	Mark-up	Selling price
$800	50%	
$1000	80%	
$950	100%	

5 **Clarify** two factors to consider when setting a selling price for the item in each of the following cases:
(a) A small publishing business has developed an idea for a new fashion magazine for 16-year-olds.
(b) John wants to sell his car online.
(c) Troy has won a new mountain bike in a raffle but he doesn't need it.
(d) Jemma wants to sell her handmade jewellery at markets and online.

6 **Explain** how local council decisions affect the location of different types of businesses.

7 **Outline** the advantages shopping centres have over traditional 'main street' shopping strips.

8 **Summarise** some of the main types of online activities SME operators undertake.

9 **Demonstrate** how an online presence can assist a business owner to operate from home.

10 **Identify** three types of businesses that can operate as home-based businesses and **explain** why they are suited to this type of operation.

11 In small groups, **propose** what factors need to be considered when choosing a location for the following businesses:
(a) fast-food outlet
(b) dental surgery
(c) agricultural machinery supplier
(d) HSC coaching college
(e) hair salon
(f) panel beater.
Choose a spokesperson to share the group's comments with the rest of the class.

12 Angela is considering purchasing an established sandwich bar that is located on a main street, adjacent to a large industrial estate and near a parking area.
Explain to Angela the importance of each of these factors. In terms of a favourable location, **recommend** whether Angela should purchase this business.

13 **Outline** those factors a potential business owner needs to consider before operating from home. Use the weblink **Home-based businesses** in the Resources tab as a reference.

on Resources

Weblink: Home-based businesses

EXERCISE 11.4 EXTENSION

1 Copy and complete the following table. **Propose** three examples of items sold under each of the methods of setting prices. Use the internet for your research.

	Cost-based pricing	Market-based pricing	Competition-based pricing
Example 1			
Example 2			
Example 3			

2 'Location is a crucial factor for the success of some small businesses but not for others.' **Critically analyse** this statement and provide relevant examples.

3 Visit the local shopping centre or mall. Identify the best located shops. **Determine** why they have the best locations. Arrange to interview the owners of some of these stores and question them about the reasons for their location.

4 Choose a small business that you are familiar with and **explain** the ways in which this business has advantages or disadvantages in relation to:
(a) visibility
(b) cost (in terms of likely premises expenses and transport costs)
(c) proximity to suppliers
(d) proximity to customers
(e) proximity to support services.

11.7 Finance

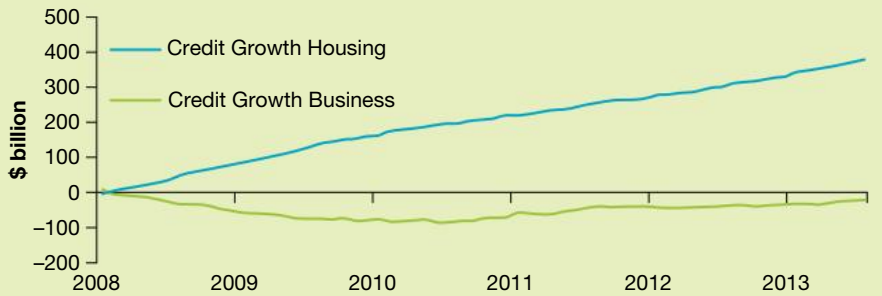
Finance refers to the funds required to carry out the activities of a business. It is a crucial issue when an entrepreneur is identifying a business opportunity, especially considering that it is often difficult to raise (see the following Snapshot).

SNAPSHOT

Small business feeling the lending crunch

Since the global financial crisis, credit growth in Australia has returned. But while growth in home lending between 2008 and 2014 was relatively strong (0.49% per month), it was actually negative for business lending (–0.04% per month).

This pattern of weaker business credit for corporates and small to medium enterprises is not unique to Australia but has been reflected around the globe due to long-term factors, such as the consolidation of banks and the centralisation of credit assessment. The issue has been accelerated by shorter term cyclical factors, such as increased business risk since the GFC and reduced demand for business credit.



Source: Derived from RBA (2014) Table D2



'… restricting the flow of funds to the SME sector can have a significant impact on the economy.'

Small and large business borrowers are relying more heavily on internal funding sources, such as retained earnings, and in the corporate sector there has been an evident diversification towards more market-based funding. But it is the 'bank dependent' SME sector, with limited access to alternative markets, that is feeling the pinch.

Small business: the engine of the economy

While it's recognised businesses should not be funded unless they can generate an adequate return of capital, restricting the flow of funds to the SME sector can have a significant impact on the economy.

In Australia, for example, around two million SMEs account for 68 per cent of all industry employment and 56 per cent of industry gross value added. Starving these businesses of funding will impact on employment growth and growth in GDP.

Negative credit growth for business has its roots in both demand and supply factors. In terms of the demand for credit there has been:

- reduced business leverage
- business diversifying funding sources post GFC
- increased price of SME credit
- stricter lending covenants and increased cost of eligible collateral.

On the supply side, factors that have led Australian banks to have a preference for housing over business lending include:

- regulatory capital requirements
- consolidation in the banking sector
- costs of credit assessment for SMEs.

The potential for capital requirements to adversely impact SME lenders was noted by the Financial Stability Board and Basel Committee's Macroeconomic Assessment Group which stated in 2010 that as a result of tighter regulatory standards 'bank-dependent small and medium-sized firms may find it disproportionately difficult to obtain financing'.

Regulations that provide disincentives for banks to engage in lending to SMEs have particularly grave implications for Australian business, as approximately 90 per cent of all intermediated credit in Australia is provided by banks.

Source: Deborah Ralston and Martin Jenkinson, *The Conversation*.

SNAPSHOT QUESTIONS

1. **Compare** the growth in credit for both housing and businesses.
2. **Identify** factors that have led to negative credit growth for businesses.
3. **Identify** the sources of funds being increasingly relied upon by businesses.
4. **Explain** the impact of restricting the flow of funds to the SME sector.

A number of preliminary factors need to be reviewed before any action can be taken. First, the entrepreneur must consider a series of questions as shown in figure 11.22. These questions allow the entrepreneur to consider the financial concerns of a business opportunity. Second, the entrepreneur needs to determine the most appropriate source of finance.

11.7.1 Sources of finance

Finance can come from a variety of sources, but two main types of sources are available to a business. The business owner can contribute their own funds (equity or capital), which is an internal source of funds. The business can also obtain loans (debt) from external sources (see figure 11.23). Advantages and disadvantages are associated with each source of finance.

on Resources

Weblink: Business finance products

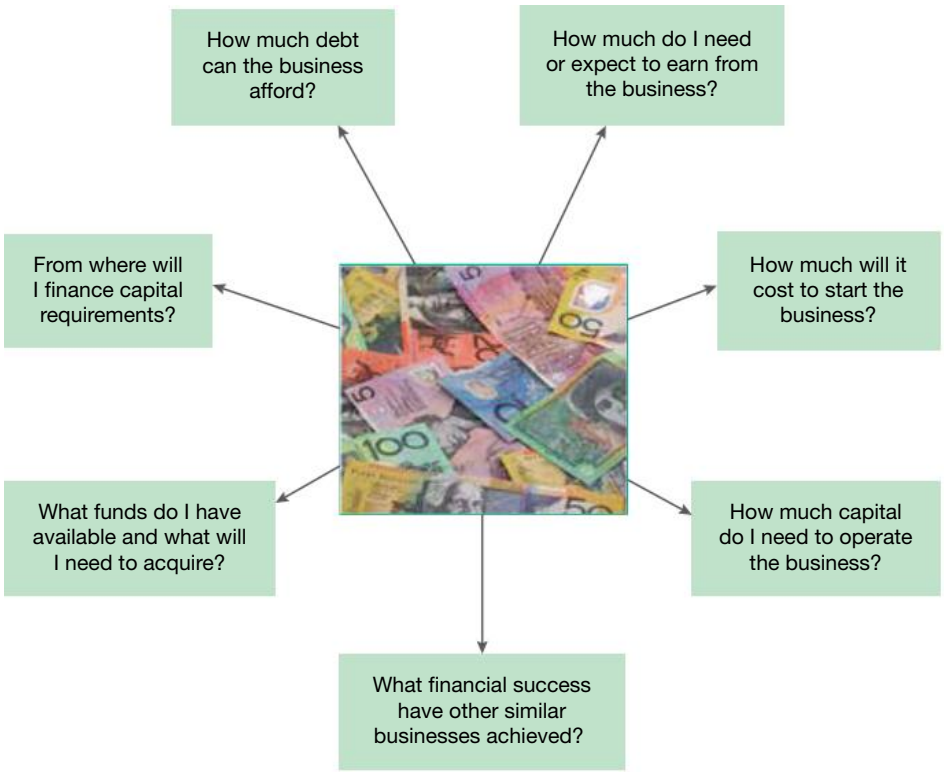


FIGURE 11.22 Questions to consider when assessing finance for a business

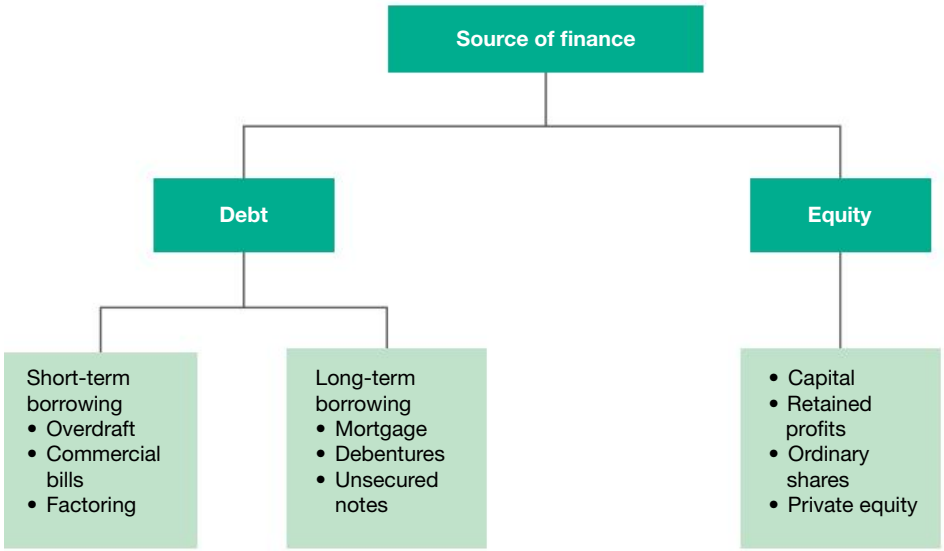


FIGURE 11.23 The two main sources of finance available to business owners

Debt finance

Debt finance relates to the short-term and long-term borrowing from external sources by a business. The main advantage with debt financing is that the owner does not have to sell any ownership in the business. Also, debt financing has certain taxation advantages. For these two reasons, debt financing is the most popular source of finance used by businesspeople when starting a business.

Once the type of finance has been decided, the next step is to choose the appropriate term or length of time. The two main terms for debt financing are:

- short-term — less than one year
- long-term — greater than one year.

BizWORD

Debt finance *relates to the short-term and long-term borrowing from external sources by a business.*



FIGURE 11.24 The NSW Business Chamber found that access to finance is a significant concern for many SMEs. Their research indicated that around 30 per cent of SMEs feel they have missed an opportunity due to a lack of credit. They identified that, of SMEs rejected for a loan: around 55 per cent felt that the rejection significantly constrained firm growth; around 21 per cent felt that it significantly increased their chances of bankruptcy; and 18 per cent had to lay off staff.

Short-term borrowing is money needed to fund the day-to-day workings of the business. For this reason, it is commonly called working capital: current assets (receivables, inventories) less current liabilities (overdrafts, creditors).

The main types of short-term finance include:

- **overdrafts**: where the bank allows a business to overdraw their account up to an agreed limit for a specified time, to overcome a temporary cash shortfall
- **commercial bills**: primarily short-term loans issued by financial institutions, for larger amounts (usually over $100 000) for a period of generally between 30 and 180 days
- **factoring**: the selling of accounts receivable for a discounted price to a finance or factoring company.

Long-term borrowing, for a period of more than a year, is usually used to purchase buildings, land, plant and equipment.

The main types of long-term finance include:

- **mortgage**: a loan secured by the property of the borrower (business)
- **debentures**: issued by a company for a fixed rate of interest and for a fixed period of time
- **unsecured note**: a loan from investors for a set period of time. It is not secured against the business's assets.

Equity finance

Equity finance, also called equity capital, refers to the funds contributed by the business owner(s) to start and then expand the business. If the SME is a company, then this contribution is referred to as shareholder's equity. Equity has an advantage

BizWORD

With an **overdraft**, *the bank allows a business to overdraw their account up to an agreed limit for a specified time, to overcome a temporary cash shortfall.*

Commercial bills *are short-term loans issued by financial institutions, for larger amounts for a period of generally between 30 and 180 days.*

Factoring *is the selling of accounts receivable for a discounted price to a finance or factoring company.*

A **mortgage** *is a loan secured by the property of the borrower (business).*

Debentures *are issued by a company for a fixed rate of interest and for a fixed period of time.*

An **unsecured note** *is a loan from investors for a set period of time. It is not secured against the business's assets.*

BizFACT

Expensive items such as land and buildings, new technology, industrial and office equipment are often leased. Leasing is especially recommended for equipment that becomes obsolete very quickly, such as computers.

BizWORD

Equity finance *is the funds contributed by the business owner(s) to start and then expand the business.*

over other sources of finance because it does not have to be repaid unless the owners leave the business. It is cheaper than other sources of finance because there are no interest payments for the business. An owner who contributes the equity to a business retains control over how that finance is used. A disadvantage is that the owner may expect a good return on their investment, but the small amount of finance may generate only low profits and low returns.

Equity finance can also be raised in other ways — for example, by taking on a new partner, by seeking funds from another investor (who then becomes an owner or shareholder) or by reinvesting net profit back into the business.

11.7.2 Cost of finance

The cost of finance will depend on the following:

- the type of finance
- the source
- the term.

The type of finance used by a business will influence the cost of capital. Debt financing requires the use of money from an external source, such as a bank, building society or finance company, and the cost is the **interest** (cost of borrowing money) charged by the institution.

BizWORD

Interest *is the cost of borrowing money.*

If capital is raised through equity finance, no interest is charged because the entrepreneur and/or partners and shareholders have invested the money. The cost of using this form of capital is the return paid at the end of the financial year if the business makes a profit. This return is called a dividend if the business is a company. The company does not pay a dividend if it does not return a profit.

The cost of equity finance can also be measured in terms of liability. Liability is unlimited if the business is operated as a sole trader or partnership. This means that creditors will sell all business and personal assets to recover the debt. However, liability of a company is limited to just the assets of the company and all funds put in by shareholders. The cost of capital will depend on the term and type of finance used by the business. Table 11.4 outlines examples of the types of loans available to businesses and the cost incurred for each type.

TABLE 11.4 Examples of financing options available to businesses and the costs incurred for each type

Type	Description	Source	Cost
Trading bank loans	Available for the purchase of land and buildings for a period of 3–10 years	Major trading banks — e.g. ANZ, Westpac	Standard interest rate cost for fixed period of time
Overdrafts	Used for short-term finance to assist in the daily operations of a business in times of need	Trading banks	Higher interest rate (not designed for long-term use)
Personal loans	Secured against the borrower's own assets	Trading banks, building societies, finance companies	A general rate of interest with banks and building societies; finance companies usually charge a higher rate of interest than banks and building societies, due to the higher risk involved in lending.
Leasing finance	Allows use of an asset without actual purchase	Trading banks, finance companies	Interest rates that are above those for short- or medium-term loans, but benefit of tax-deductible finance repayments
Owner's equity or shareholders' equity	Money invested by owner/partner or shareholders. Risk of loss of the funds invested if the business fails, but share of profit if the business is successful	Owner of the business or a company shareholder	No interest on the use of these funds, but a return (dividend) on profits to be paid to shareholders

SUMMARY

- A business cannot commence without finance to enable it to pursue its activities.
- SME owners must determine how their business will be financed throughout the life of the business.
- Businesses can obtain funds from either internal (equity) or external (debt) sources.
- Debt finance relates to the short-term and long-term borrowing from external sources by a business.
- Examples of short-term finance available to businesses include an overdraft, commercial bills and factoring. Examples of long-term finance include a mortgage, debenture and unsecured note.
- Equity is the funds contributed by the owner(s) of a business to start and expand the business.
- The business owner must consider the cost of finance. This will depend on the type of finance, the source and the term.

EXERCISE 11.5 REVISION

1 **Account** for the importance of finance in terms of establishing and operating a business.

2 **Distinguish** between equity and debt finance.

3 Prepare a table with two columns to **outline** the advantages and disadvantages of using debt to finance a business.

4 Prepare a table with two columns to **outline** the advantages and disadvantages of using equity to finance a business.

5 **Compare** the following two forms of debt finance by completing the table below.

Form of debt	Main features	Advantages/ disadvantages
• overdraft		
• commercial bill		
• factoring		
• mortgage		
• debenture		
• unsecured note		

6 **Recall** the three factors that will impact on the cost of finance.

EXERCISE 11.5 EXTENSION

1 Contact a bank's loan manager and request a summary of:
(a) the different types of lending options for small businesses
(b) methods of repayment on money borrowed.
Assess the most suitable form of finance for a person wanting to establish a computer repair business that is operated from home.

2 In small groups, collect five advertisements offering different types of finance funding for small businesses. Use information from magazines, banks and websites. **Compare** the offers under the headings in the following table. Display your database in the classroom.

Source	Interest rate	Borrowing limit	Terms	Main advantage

3 **Analyse** why it is important to match the term of a loan to the life of the asset for which the finance was obtained.

11.8 Legal considerations and influence of government on SMEs

Many licences, permits, approvals and authorities must be taken into account by SME owners. All business owners have a legal obligation to observe the statutory regulations when commencing and operating a business. Fulfilling all legal obligations may be frustrating at times, particularly when more than one level of government is involved. However, businesses that do not obey the law risk losing customers and their reputation, being fined, or losing the right to continue trading.

The three levels of government (federal, state and local) all have regulations to which small business owners must adhere. The regulations are imposed primarily to promote fairness, protect consumers and encourage efficiency.

11.8.1 Business name

The Australian Securities and Investments Commission (ASIC) is now responsible for a national business name registration service. Businesses need to register their business name, except when the name is that of the owner and then it is optional. But if something is added to a personal name, such as 'Pty Ltd', 'Motors', 'and Associates' or 'and Co.', then the business name must be registered. This is to prohibit anyone else from trading under a similar name. (If two traders want to register the same name, the first application for registration is accepted and the second trader must register a different name.)

Registration of a business name does not protect or establish any specific rights to that name. If the business name is a crucial part of the business's operation, then it should also be registered as a trademark with the federal agency responsible for intellectual property (IP Australia), which administers the *Trade Marks Act 1995* (Cwlth).

With the rapid growth of e-commerce, it is becoming a necessity for most businesses to develop an online presence. A key element of its online presence will be the domain name, which is the address of the business's website on the internet. It is important that the business chooses a unique domain name that represents its activities. It also helps if the domain name is easy to remember and spell, so that customers can find the website without any hassles — for example, kpaplumbing.com.au.

A business can register multiple domains to help its customers find it more easily and to prevent other businesses from registering a similar domain name that might confuse customers. A business can see whether a domain name has already been registered by checking the registry online. Domain names can be registered through resellers and registrars by visiting the Australian Domain Administration website.

on Resources

Weblink: Registering a business name



FIGURE 11.25 Businesses can register domain names by visiting the Australian Domain Administration website. Although building and hosting a website can costs thousands of dollars, registering a domain name generally costs between $10 and $100 per year.

11.8.2 Zoning

Local government controls zoning regulations. In other words, they have the authority to restrict where certain businesses can locate. Zoning regulations create areas where land can be used only for particular purposes. These regulations specify the areas in which residential, industrial, recreational or commercial activities may take place. This ensures that activities that do not belong together, such as those associated with factories and residential areas, are kept separate. This function assists the local community in terms of planning.

When establishing a business, the owner must inquire with the local council to determine which zoning regulations will affect their business now and in the future. A manufacturing business that uses heavy equipment and wants to operate a 24-hour shift, for example, would need to locate where it is allowed to operate under zoning regulations. It would not be suitable close to a residential area, mainly because the noise is a problem.

11.8.3 Health regulations

Local government also imposes health regulations under the *Public Health Act 2010* (NSW). Each local council supplies businesses (primarily those dealing with food, such as cafés, restaurants, butcher shops and bakeries) with the requirements and standards to meet in order to receive a licence to operate. Some requirements include:

- the temperature for food storage
- kitchen layout
- employee clothing requirements
- time for which food can be kept
- correct food handling.

A health inspector will assess premises regularly and often without warning to ensure the business owner/operator maintains standards. If problems occur, then the business is given a period of time to rectify the situation or they will be closed down.

The purpose of the *Food Act 2003 (NSW)* is to ensure that food for sale is both safe and suitable for human consumption. The NSW Food Authority has a partnership with local councils across NSW and they conduct regular inspections of retail food businesses in their local area (see the following Snapshot). Council environmental health officers (EHOs) are authorised officers under the Act and check that good food safety practices are in place, such as temperature control, cleanliness, hand washing and labelling.



FIGURE 11.26 The NSW Food Authority, in partnership with councils, implements the Food Act at the local level through the monitoring and inspection of food premises. Local councils are required to obtain and test food samples to determine if the food produced is safe and suitable for human consumption.

NSW Food Authority

The NSW Food Authority publishes a 'Name and Shame' register of businesses that have breached NSW food safety laws. Publishing the lists gives consumers more information and confidence when making decisions about where they eat or buy food.

Individuals and businesses can either receive a penalty notice for their alleged offence or be prosecuted before a court. Each of these are listed on a separate register; i.e. there is a 'Register of penalty notices' for those businesses issued with an on-the-spot fine for an alleged food safety offence, and there is a 'Register of offences (prosecutions)' for those businesses that have been prosecuted before a court and have been found guilty of breaching food safety laws.

2017 marked nine years of operation of the 'Name and Shame' register. In this time, more than 7000 food retail businesses have appeared on the register and there have been more than 11 million views of the register webpage. At its peak in 2009–10, 3.4 per cent of food businesses were placed on the register. This figure fell to just 1.6 per cent in the 2016–17 financial year. An average of 1567 penalties are issued each year. The greatest success of the register, however, is that there are very few repeat offenders. The register therefore serves as an excellent deterrent because, once a food business has made the shame file, they definitely don't want to appear on it again.

In 2017, it was revealed that Blacktown, Canterbury-Bankstown, Parramatta and Sydney councils were home to the largest number of food safety breaches in the previous six months. A combination of businesses such as bakeries, seafood stores and restaurants found themselves on the 'Name and Shame' register for failing to prevent pests, neglecting to adequately clean and maintain equipment and leaving food open to contamination, among other things. Cockroaches, flies and rats are the most common pests to attract attention from food inspectors.

While the majority of businesses on the list are lesser-known, independent operators, the 'Name and Shame' list has also included some big name businesses such as Domino's Pizza in Mosman, Bakers Delight in Artarmon and Gloria Jean's in Strathfield.

In June 2017 a chicken producer was ordered to pay more than $40 000 in fines and professional costs after a court found that the business was transporting chicken intended for sale on rusted and corroded trolleys and benches. Inspectors also found unclean equipment and utensils, staff change rooms without soap or paper towels,

SNAPSHOT



'NSW Food Authority publishes a 'Name and Shame' register …'

and rubbish and cigarette butts on site. The owner of the business pleaded guilty to the 12 charges laid against the business.

In the 2016–17 financial year, the most common food safety breaches related to cleanliness of food premises (21 per cent), storage and temperature control (16 per cent), pest control (13 per cent), hygiene of food handlers (13 per cent) and cleanliness of fixtures, fittings and equipment (12 per cent).

SNAPSHOT QUESTIONS

1. **State** the two registers that are kept.
2. **Identify** some of the most common food safety breaches.
3. **Explain** the benefits of having the 'Name and Shame' register.

11.8.4 Other regulations

Competition and Consumer Act

BizWORD

The **Competition and Consumer Act 2010** *(Cwlth) is a law that protects both consumers and businesses. It protects consumers from deceptive or misleading practices, and it regulates the trade practices of businesses.*

on Resources

Weblink: Australian Consumer Law

The ***Competition and Consumer Act 2010*** (Cwlth) has a function to protect both consumers and business, and applies to virtually all businesses in Australia, including the commercial activities of government. First, it is designed to protect consumers from deceptive practices such as misleading packaging or misrepresentation of the place of production. It also deals with product safety and the conditions and warranties associated with products. Further, the act aims to regulate certain trade practices that may restrict competition (such as monopolistic power) because they can affect the price and quality of goods for the consumer. Table 11.5 outlines some of the undesirable and misleading practices that are illegal under the Act.



FIGURE 11.27 The ACCC launched legal action against the paint maker, Dulux, over claims relating to one of its products, InfraCOOL roof paint, which asserted to reduce the temperature of living areas inside homes by up to 10 degrees. Dulux also claimed that its Weathershield Heat Reflect wall paint would significantly reduce the inside temperature of a home. The Federal Court found that both claims were false and misleading and fined Dulux $400 000 after the company admitted they did not have any reasonable grounds for making those statements.

TABLE 11.5 Undesirable and misleading practices illegal under the Competition and Consumer Act

Illegal practices	Description
Misleading or deceptive conduct	Advertisements must not use words that are deceptive or claim that a product has some specific quality when it does not. Such actions convey a false impression of the exact nature of the product. Additionally, price reductions or specials must be genuine.
Unconscionable conduct	This is conduct in business transactions that is unfair or unreasonable and goes against good conscience.
False or misleading representations regarding goods or services	A false or misleading representation is a statement of fact that is untrue, such as claiming that a motor vehicle has a certain fuel consumption performance when it does not.
Offering gifts and prizes in connection with the supply of goods and services and then not providing them	It is illegal for a business to offer a prize in connection with the supply of goods and services and not provide them.
Conduct that may mislead the public	For example, using a brand name similar to a well-known brand, or using an Australian-made logo when the product was made overseas
Bait advertising	A business attempts to attract customers by advertising some products at lower prices. When the advertised products quickly run out, customers are directed (or switched) to higher priced items.
Referral selling	This occurs when a business offers a customer a special deal or special price if the customer refers other potential customers to the seller. This is illegal because it may encourage consumers to spend more money than they planned with the expectation that they may recoup some if they encourage others to buy.

Breaches of any of these provisions may result in penalties of up to $1.1 million for companies and $220 000 for individuals. Other actions may include an injunction — that is, a restraint on a person — or the awarding of damages.

SUMMARY

- All business owners have a legal obligation to observe the statutory regulations when commencing and operating a business.
- Of the many laws and regulations that small business owners need to comply with, some important regulations relate to:
  - business name
  - land zoning
  - health regulations.
- The *Competition and Consumer Act 2010* (Cwlth) is a federal government statute that aims to:
  - promote fair trade and competition in the marketplace
  - protect both consumers and businesses from deceptive or misleading practices.

EXERCISE 11.6 REVISION

1. **Recall** the main objectives of imposing government regulations.
2. **State** when it is compulsory to register a business name.
3. **Outline** the purpose of land zoning.
4. **Demonstrate** how land zoning will influence where specific businesses can locate.
5. **Identify** the types of health regulations that local councils impose on businesses.
6. Read the section 'Competition and Consumer Act' in section 11.8.4. Complete the paragraph below by **recalling** the correct word from the list that follows.

deceptive	Safety	warranties
price	Consumer	regulate
consumers	Misleading	competition

The *Competition and* _____ *Act 2010* (Cwlth) has a function to protect both _____ and business. First, it is designed to protect consumers from _____ practices such as _____ packaging or misrepresentation of the place of production. It also deals with product _____ and the conditions and _____ associated with products. Further, the Act aims to _____ certain trade practices that may restrict _____ (such as monopolistic power) because they can affect the _____ and quality of goods for the consumer.

7 Refer to table 11.5 in section 11.8.4. **Outline** two practices that are illegal under the Competition and Consumer Act.

8 **State** the legal penalties or remedies that might apply after a successful prosecution for breaches of restrictive trade practices provisions of the Act.

EXERCISE 11.6 EXTENSION

1 Find out about the types of licences the following businesses would need to begin and operate. To help you, use the **Australian Business Licence and Information Service (ABLIS)** weblink in the Resources tab.
(a) beauty salon
(b) electrician
(c) tour operator.
Appreciate the importance of having a strict licence system in operation.

2 Imagine you are about to open a pizza restaurant. **Investigate** the government regulations you would need to satisfy.

3 **Evaluate** the role of the ACCC. To help you, use the **Australian Competition and Consumer Commission** weblink in the Resources tab.

4 'Government regulations are needed to create a fair marketplace for businesses and consumers.' **Evaluate** the accuracy of this statement.

Resources

Weblink: Australian Business Licence and Information Service (ABLIS)

Weblink: Australian Competition and Consumer Commission (ACCC)

11.9 Human resources

As outlined in chapter 8, employees are the most valuable resource of any business. Hiring the 'right' people at the 'right' time, with the 'right' skills in the 'right' quantity is crucial for business success. Consequently, one of the most important influences in establishing a SME is staffing: the people side of the business.

In the establishment phase, the SME owner must answer one crucial staffing question: How many employees, if any, will be required to operate the business?

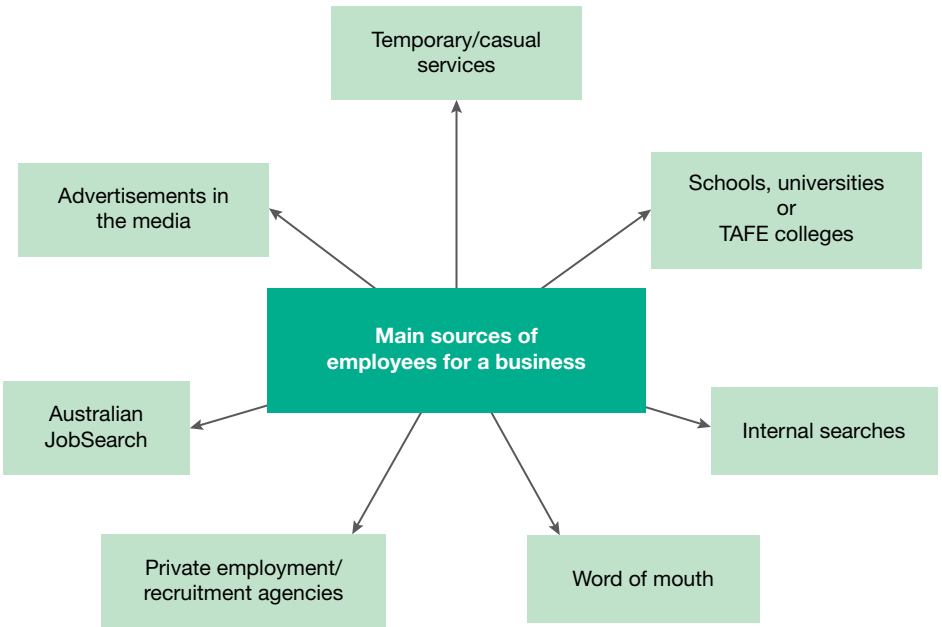


FIGURE 11.28 The main sources of employees for a business

If a SME owner decides to hire staff, many sources are available. The source chosen will depend on the size of the business, the type of position available and the nature of the labour force in the business's particular area. Figure 11.28 outlines the main sources of employees available to a business.

Once the business is operating and if people are employed, the SME owner must fulfil a number of important human resource requirements that deal with:

- staffing objectives
- specific duties to be performed
- the skill base of existing staff
- a forecast of future staff requirements and skills
- methods the business will use to recruit extra staff
- a form of the organisational chart
- administrative records to be kept to manage the employees.

Of all these requirements the most important are those that deal with the skill level of employees. Skilled employees are highly productive and result in creating wealth for the business.

11.9.1 Skills

A business owner should always remember that the overriding objective of recruiting is to attract a pool of qualified applicants — people with the most suitable skills — from which to choose the most appropriate person for a particular job. Skilled employees are more productive and create wealth for the business. This is the same principle that a sports coach uses when selecting a team. To improve the chance of winning, the coach wants those players who possess the highest level of skills.

The skill base of existing employees should also be detailed so that training needs can be identified. If the skills level of employees is not adequate enough for them to fulfil their jobs effectively, then the business owner has two options:

- provide training to improve the skills level of existing employees
- recruit people who have the required skills.

While there will always be job-specific skills that an employer is looking for, that's not nearly as important as some general skills that those responsible for hiring are increasingly looking for. These general job skills are sometimes called 'employability skills' and will make people more effective at work, no matter what job they do. They are sometimes also known as transferable skills because people develop them over time and take them with them as their career develops. Some of the most sought after general skills include good teamwork, communication, problem-solving, initiative, quick learner and the ability to plan and organise work.



FIGURE 11.29 It is important to recruit people who have the required skills since a business's most important asset is its people. Having the right people with the right skills in the right position can make the difference between business success and failure.

11.9.2 Costs — wage and non-wage

BizWORD

On-costs *are payments for non-wage benefits.*

A business will only employ someone if the return is greater than the cost. The total cost of an employee is not solely the wage or salary paid. The employer is also responsible for other employee expenses, referred to as **on-costs**, which account for around 30–40 per cent of the total remuneration package (see the following Snapshot).

SNAPSHOT



'… the total cost of employing someone on a base salary of $50 000 is $67 054.'

Staffing a business — on-costs

When employing new staff, there are many other costs that are not always taken into account. The following case study reveals that these hidden costs quickly add up. The on-costs in the table are based on a salary of $50 000.

Cost breakdown	Amount $
1. **Superannuation**. The employer must pay 9.5 per cent superannuation of all employees earning more than $450 in a calendar month.	4750
2. **Annual leave**. Normally 4 weeks per year. This means that the employer must pay an additional 17.5 per cent annual leave loading for four weeks annual leave.	673
3. **Public holidays**. There are about 10 public holidays in Australia each year. This is 3.85 per cent (2/52).	1953
4. **Sick leave**. Most awards provide for 10 days each year. This is another 3.85 per cent.	1953
5. **Workers' compensation insurance**. The rate charged varies broadly depending on the risk of the industry. In some instances it can be 15 per cent. For this example a rate of 5 per cent will be used.	2500
6. **Payroll tax**. This state government tax is levied once an employer's annual payroll (including superannuation) exceeds a certain amount. In New South Wales the threshold is $750 000 and the rate is 5.45 per cent.	2725
7. **Recruitment**. The average cost of recruiting the base-grade employee is about $5000. This includes the cost of recruiting, lost production and training of the new employee. For this example, assume the employee stays for 2 years.	2500
Total of on-costs	**17 054**

The total of the on-cost for this 'average' employee is $17 054. Businesses are responsible for these costs and must budget accordingly. Therefore, based on this case study, the total cost of employing someone on a base salary of $50 000 is $67 054.

The above table only deals with the most common on-costs for the 'average' employee. For some employees, especially senior executives, other specialised on-costs can include fringe benefit tax, car allowance, housing subsidy, travel and meal allowance, bonus fee and association membership fees.

SNAPSHOT QUESTIONS

1. **Calculate** the percentage on-costs represent of the base salary.
2. **Explain** why on-costs are sometimes referred to as 'hidden costs'.

The main on-costs include:

- work health and safety requirements
- long service leave
- sick leave
- superannuation
- holiday pay
- study leave
- maternity and paternity leave
- workers' compensation
- leave loading.

Two examples of these on-costs (non-wage costs) are superannuation and leave loading.

Superannuation

Under the federal Superannuation Guarantee scheme, all employers must make provision for employees' superannuation. **Superannuation** (otherwise known as super) requires all employers to make a financial contribution to a fund that employees can access when they retire. The main aim of superannuation is to give employees a sum of money that can be used:

- for their retirement
- if they become an invalid
- by the beneficiaries upon a person's death.

In some circumstances they can access the money if they leave a job, although tax disincentives apply. Employers are not required to provide for the superannuation of employees earning less than $450 per month or for employees aged under 18 years old and working 30 hours or fewer per week.



FIGURE 11.30 Prior to July 2013, employers were not required to provide superannuation for workers aged over 70 years. There is now no upper age limit for making superannuation guarantee contributions. The removal of this limit is to encourage people to stay in the workforce longer.

BizWORD

Superannuation *is a scheme set up by the federal government. It requires all employers to make a financial contribution to a fund that employees can access when they leave or retire from a job. The percentage an employer must contribute will increase gradually to 12 per cent by 2025.*

BizFACT

All contributions must be made to a complying superannuation fund that meets the federal government's standards, so as to protect the employee's superannuation. Since 2005, many employees have been able to choose into which fund their employer superannuation contributions are paid.

The employer's main obligation is to make a financial contribution — presently 9.5 per cent of an employee's earnings for their ordinary hours of work — to their employees' superannuation account.

As with taxation, employers are required to keep records of all superannuation-related transactions, including payments contributed, payroll and employee records, and the level of entitlement of each employee. Employees are allowed access to all documentation, especially when leaving a workplace.

BizFACT

There is pressure from employer associations to abolish leave loading.

Annual leave loading

All employees, except casual employees, are entitled to a minimum of four weeks annual leave, or holidays, for each year they work. Leave loading is an extra payment most employees receive on top of their annual leave pay. This extra amount — presently 17.5 per cent — is added to an employee's holiday pay. The amount is calculated on the four weeks annual leave to which each full-time, permanent employee is entitled. Not all employees are entitled to leave loading, although this is a common feature of most modern awards. An employee's award, enterprise agreement or contract will state whether or not they are entitled to this.

It was introduced at a time when workers' wages were low and most worked more than a 40-hour week. Unions negotiated a percentage loading (presently 17.5 per cent) for workers so that the average family could afford to go away for a holiday (in addition to paying their regular rent or house repayments).

SUMMARY

- One of the most important influences when establishing a SME is staffing.
- If a SME owner decides to hire staff, many sources are available.
- The overriding recruiting objective is to attract a pool of qualified applicants with the most suitable skills.
- Skilled employees are more productive and create wealth for a business.
- A business will employ someone only if the return is greater than the cost.
- On-costs are payments for non-wage benefits, including long service leave, workers' compensation and annual leave loading.

EXERCISE 11.7 REVISION

1. **Explain** why hiring the 'right' employee is so important for a business.
2. **Identify** three sources of external employee recruitment.
3. 'Skilled employees are more productive and create wealth for the business.' **Discuss**.
4. **Recall** two options a business owner has if the skills level of employees is not adequate enough for them to fulfil their jobs effectively.
5. **Why** do most employers consider general skills more important than job-specific skills?
6. Unscramble the following on-costs and then **construct** a sentence to explain their meaning.
   (a) ypa dyohlia
   (b) eelav gaoldni
   (c) nnuepsnrtoiaau
7. **Explain** why on-costs are also referred to as non-wage costs.
8. **Outline** what the obligation of employers is towards employees in relation to superannuation.
9. **Discuss** the likely impact of abolishing leave loading from the perspective of (i) an employer and (ii) an employee.

EXERCISE 11.7 EXTENSION

1 Use the **Job interviews** weblink in the Resources tab to **construct** a list of what you consider to be the three most important do's and three most important don'ts for people conducting an interview. You could also enter 'interviewing applicants' in your search engine to find other websites that offer hints for employers when conducting an interview.

2 Competent employees are important for the success of any business. Imagine you need to employ a new staff member in your boutique store. You choose an inexperienced salesperson. **Propose** three strategies you could use to train the employee.

on Resources

Weblink: Job interviews

11.10 Taxation

Taxation is the compulsory payment of a proportion of earnings to the government. Taxation is an important issue when a person is considering all aspects of opening a business.

BizWORD

Taxation *is the compulsory payment of a proportion of earnings to the government.*

11.10.1 Federal and state taxes

Many different federal and state taxes apply to different businesses, and it is important that a person starting a business becomes familiar with all appropriate tax requirements. The main taxes that affect a business (see table 11.6) are imposed by the federal and state governments.

TABLE 11.6 Major taxes that apply to businesses

Tax	Levied by
Income tax — pay-as-you-go (PAYG) • Imposed on the employee • Taken from the employee's salary or wage directly • Lodged with the tax department by the business • Detailed in a group certificate that the employee receives at the end of the financial year • Taxed at progressive tax rates — the more you earn, the higher your rate of tax.	Federal government
Fringe benefits tax (FBT) • Tax on the provision of a benefit to an employee — such as cars for private use, low-interest loans, entertainment expenses, and housing and accommodation — in place of salary or wage • Paid by the employer at a rate of 47 per cent of the value of the benefit provided.	Federal government
Goods and services tax (GST) • A broad-based tax of 10 per cent on the supply of most goods and services consumed in Australia • See page 389 for a detailed explanation	Federal government
Company tax • Paid on the earnings of a company and calculated on the company's taxable income (which is income left after allowable deductions are calculated) • Currently calculated at 30 per cent of taxable income	Federal government
Capital gains tax • Calculated on the profit made on the sale of assets acquired after 19 September 1985, including the sale of a business or properties bought and resold within 12 months	Federal government

on Resources

Weblink: ATO

Tax	Levied by
Stamp duty • A tax levied on the transfer of property (e.g. businesses, real estate and shares)	New South Wales government
Land tax • A tax on land owned by individuals or businesses over a certain value (in 2018 it was $629 000 or more) • Land used for primary production or an individual's primary residence are exempt from land tax	New South Wales government
Payroll tax • Payable on wages paid by an employer to their employees on payrolls that exceed $750 000 at a rate of 5.45 per cent (2018)	New South Wales government

All businesses must pay their taxes if they wish to continue to operate as a legitimate business. Small to medium enterprise owners should structure their records and finances in such a way that they have the necessary information and money to efficiently manage their taxation obligations. Apart from the moral and ethical considerations, tax avoidance normally results in an Australian Taxation Office (ATO) investigation and the possibility of a fine or prison sentence.

Different taxes apply to different businesses, so a person operating a SME must become familiar with all appropriate tax requirements (see the following Snapshot). Businesses pay taxes to their federal and state governments on the basis of what they earn, what they own and even what they purchase. One of the most important tax obligations is the goods and services tax (GST).



FIGURE 11.31 Keeping up with tax requirements can be a daunting task for individuals, let alone businesses with many complicated transactions. It is important for a business to seek help from the Australian Taxation Office or a registered tax agent when unsure.

Operating a business — tax law

Under tax law, a person operating a business must keep records that record and explain all transactions. These records include any documents that are relevant for the purpose of working out the person's income and expenditure. The person must keep his or her records in writing in the English language or, if not in a written form (for example, in an electronic form such as a computer system), in a form that is readily accessible and convertible into writing in English.

Any books of accounts, records or documents relating to the preparation of an income tax return must be retained for a period of at least five years, either on paper or electronically. If a business owner does not keep the right tax records, they can incur penalties.

Business records that must be kept include:

- records of all sales transactions
- records of all business expenses
- lists of creditors or debtors
- records of depreciating assets
- capital gains tax records
- records relating to employees and contractors e.g. tax file numbers, wages or payments made, superannuation contributions etc.

Fringe benefit tax legislation requires records to be kept for five years. Other statutory provisions, such as corporate law, require a company to retain records for seven years after completion of the transaction to which they relate.

SNAPSHOT QUESTIONS

1. **Identify** the records a businessperson must keep.
2. **Outline** how these records must be kept.
3. **State** how long these records must be kept.

SNAPSHOT



'Under tax law, a person operating a business must keep records that record and explain all transactions.'

Goods and services tax (GST)

The **goods and services tax (GST)** is a broad-based tax of 10 per cent on the supply of most goods and services consumed in Australia. One of the stated purposes for the introduction of the GST was to make it more difficult for businesses and individuals operating in the 'cash economy' to avoid tax. The GST had a major impact on many aspects of business operations because businesses became responsible for collecting the tax on behalf of the government.

The GST is paid at each step in the supply chain, with businesses charging GST as part of the price of the goods and services they supply. Any business with an annual turnover of $75 000 or more operating within Australia must register for the GST. The business is then entitled to claim **input tax credits** from the ATO for any GST included in the price of inputs that the business purchases. This means the consumer bears the cost of the GST, not the business providing the good or service. It is the responsibility of the business, however, to pay to the ATO the amount of GST collected from the consumer.

The GST requires all registered businesses to prepare a set of accounts — the **business activity statement (BAS)** — at regular reporting intervals, either monthly or quarterly. The key to successfully managing GST reporting and associated 'paperwork', therefore, is to be organised, especially in terms of the input tax credit. Failure to claim for these credits will result in them becoming a cost to the business.

BizWORD

*The **goods and services tax (GST)** is a broad-based tax of 10 per cent on the supply of most goods and services consumed in Australia.*

*An **input tax credit** is an allowable tax deduction that a business can claim for any GST included in the price of business inputs.*

*The **business activity statement (BAS)** records a business's claim for input tax credits and accounts for GST payable.*

SNAPSHOT

'The furniture manufacturer, who is registered for GST, is entitled to an input tax credit …'

The GST system — how it works

Timber merchant sells timber for $110 including $10 GST	**Business activity statement**		
	GST on sales	$10	
	less input tax credit	$0	
	GST to pay	$10	$10 GST paid by timber merchant to ATO
Furniture manufacturer sells table for $220 including $20 GST	**Business activity statement**		
	GST on sales	$20	
	less input tax credit	$10	
	GST to pay	$10	$10 GST paid by manufacturer to ATO
Retailer sells table for $330 including $30 GST	**Business activity statement**		
	GST on sales	$30	
	less input tax credit	$20	
	GST to pay	$10	$10 GST paid by retailer to ATO
Consumer pays $330 (including $30 GST to the retailer)			**$30 total GST paid**

GST is paid at each step in the supply chain. GST-registered businesses must include GST in the price of goods and services they supply or sell. If you're registered for GST, you can claim back the GST included in the price of your business purchases as input tax credits.

Registered businesses collect GST from sales to their customers, then claim back the GST on business purchases as input tax credits. The cost of GST, therefore, flows along the supply chain and is finally included in the price paid by the end consumer.

Consumers cannot claim input tax credits, so while the liability for paying the GST rests with GST-registered businesses and organisations, the economic cost is borne by the end customer. This can be seen clearly in the example above of the manufacture and sale of a piece of furniture.

The example above shows how three businesses, each registered for GST, charge and pay the GST. The timber merchant sells timber to a furniture manufacturer for $110, including $10 GST. The manufacturer uses the timber to make a table, which he sells to a furniture retailer for $220, including $20 GST. The retailer then sells the table to a consumer for $330, including $30 GST.

The timber merchant pays $10 GST to the ATO. The furniture manufacturer, who is registered for GST, is entitled to an input tax credit for the $10 GST, which is included in the price paid to the timber merchant. The manufacturer will offset that $10 against the $20 collected on the sale of the table to the furniture retailer and pay $10 GST to the ATO.

The furniture retailer, who is registered for GST, is entitled to an input tax credit for the $20 GST included in the price paid to the furniture manufacturer. The retailer will offset that $20 against the $30 GST collected on the sale of the table to the consumer and pay $10 GST to the ATO.

The consumer who buys the table pays the GST, because consumers cannot register for GST and cannot claim input tax credits.

SNAPSHOT QUESTIONS

1. **State** the total GST paid in this example.
2. **Explain** how this amount was calculated.
3. **Identify** who can claim an input tax credit.
4. **Outline** why the consumer pays the GST.

The Australian Business Number (ABN)

As part of the tax reforms and the GST in 2000, the Australian government introduced the **Australian Business Number (ABN)**. The ABN is a single identifying number that a business uses when dealing with government departments and agencies. The ABN also allows the business to participate in the GST system, because input tax credits can be claimed only if a supplier has an ABN. If a business does not have an ABN, tax at the rate of 46.5 per cent can be withheld. This is known as withholding tax and can be avoided by quoting an ABN on invoices for the supply of a good or service.

BizWORD

The ***Australian Business Number (ABN)*** *is a single identifying number that a business uses when dealing with government departments and agencies.*

11.10.2 Local government rates and charges

Although they are often considered of lesser importance compared to the numerous state and federal taxes, local government rates and charges must be considered and budgeted for. Rates — a system of property taxation usually based on the value of land — is the main local government charge a business will face. The three main areas in which fees or charges are levied are:

- water and sewerage
- waste management services
- development and building approval fees
- inspectors' fees
- parking permits
- use of public property.

The income generated from these taxes is used to provide better facilities for the local community. Sometimes a local council will offer exemptions or reductions in the rates and charges to encourage people to establish businesses within the council area.

SUMMARY

- Taxation is the compulsory payment of a proportion of earnings to the government.
- Businesses are responsible for checking their obligations concerning income tax (PAYG), fringe benefits tax, goods and services tax, company tax, capital gains tax, stamp duty, land tax and payroll tax.
- Goods and services tax (GST) is a 10 per cent value added tax imposed on most goods and services.

- The customer pays GST when buying goods and services, which is passed on to the business that in turn passes it on to the Australian Taxation Office (ATO).
- GST collection and payments to the ATO are recorded on the business activity statement (BAS), which is also the means by which a business can claim input tax credits.
- The Australian Business Number (ABN) is a single identifying number that a business uses when dealing with government departments and agencies.
- Property rates is the main local government charge a business will face.

EXERCISE 11.8 REVISION

1 **Distinguish** between income tax — pay-as-you-go (PAYG) — and company tax.

2 **Recall** an employer's obligations in relation to the stamp duty tax system.

3 **Distinguish** between fringe benefits tax and capital gains tax.

4 **State** the business owner's requirements in relation to structuring financial records for taxation purposes.

5 **Explain** the operation of each of the following state taxes:
(a) payroll tax
(b) land tax.

6 Denise runs a real estate agency, which is registered as a proprietary company. She employs eight permanent staff and three casuals and paid a total of $870 000 in wages in the last financial year. The business provides five employees with a car each to assist them to visit properties as well as for their own personal use. Denise regularly uses her business contacts to buy cheap properties, renovate them and sell at a profit. Her business owns its own premises, which are currently valued at over $1 million.

Identify and **explain** each of the Commonwealth and state taxation obligations of Denise's business.

7 **State** what the following acronyms represent.
(a) GST
(b) BAS
(c) ABN

8 **Define** the term 'goods and services tax (GST)'.

9 **Explain** the importance of a BAS.

10 **Describe** the effect of the system of input tax credits on businesses and consumers.

11 An electrical goods manufacturer sold a dozen refrigerators to an electrical retailer for $880 each, which included $80 GST per refrigerator. The electrical retailer then sold each of the refrigerators to its customers for $1320 each, including GST.
(a) **Calculate** the amount of GST paid by each customer.
(b) **Identify** who, in this example, can claim input tax credits.
(c) **Calculate** the amount claimed as an input tax credit for each refrigerator by the electrical retailer.
(d) **Calculate** how much GST the electrical manufacturer would be required to pay to the ATO.
(e) **Calculate** how much GST the electrical retailer would be required to pay to the ATO.

12 **Recall** why it is important for a business to apply for an ABN.

13 **Identify** the main local government rates and charges.

EXERCISE 11.8 EXTENSION

1. In small groups, **critically analyse** the following statement: 'In today's commercial world, tax avoidance happens. The only problem is being caught.' Choose a spokesperson to share the group's comments with the rest of the class.
2. In small groups, arrange an interview with a local accountant. **Create** either a two-page written or five-minute oral report. Use a word-processing package for the written report or a multimedia application for the oral report. You might wish to develop your report under the following headings:
   (a) types and rates of tax payable by a small business
   (b) electronic recording systems for tax records
   (c) completion of the business activity statement
   (d) penalties for non-payment or avoidance.

on Resources

Digital doc: Chapter summary (doc-26103)

Interactivity: Chapter crossword (int-7231)

Interactivity: Multiple choice quiz (int-7232)

CHAPTER 12

The business planning process

OVERVIEW

12.1 Introduction
12.2 Business planning process
12.3 Sources of planning ideas
12.4 Vision, goals and/or objectives
12.5 Organising resources
12.6 Forecasting
12.7 Monitoring and evaluating
12.8 Taking corrective action — modification

12.1 Introduction

Businesses do not plan to fail, they fail to plan — this quotation is a sad reflection of reality. SME owners start keen, convinced their idea will succeed. They are full of optimism. However, while enthusiasm is an essential ingredient in the success of a business, it is not enough by itself. If prospective business owners neglect to undertake thorough planning, so they can put together a carefully researched business plan, the stage is set for business failure. Optimism will turn to despair as the small business owner faces the grim reality. All SME owners must have a good understanding of the:

- role of the business plan
- process of business planning.

12.1.1 The role of the business plan

BizWORD

A **business plan** *is the 'travel itinerary' for future growth and development within a business. It sets out the desired goals and direction of the business.*

A **business plan** is similar to a travel itinerary. You would not go on a year-long trip around Australia without first preparing a plan. You would need to decide which modes of transport you will use to get from place to place, where to stay and what sights to visit. During the trip, you would need to constantly refer to the map to make sure you were heading in the right direction. Also, on hearing about local events or conditions, you would need to modify your travel plan to accommodate for these factors.

It is amazing that many people put more planning into a holiday than they do into their business. Without planning, the business owner does not know where the business is heading. The business 'journey' will probably end in disaster, with the owner asking, 'How did I end up here?' Therefore, the essential role of the business plan is to act as a guide or map on which the business's journey can be plotted. It is one of the most useful management tools a business owner can use. In all businesses, the best results come from effective management and detailed planning (see the Snapshot on the next page).



FIGURE 12.1 A business plan is similar to a travel itinerary — it plots the route the business will travel.

BizFACT

The first task of anyone wanting to commence a business is to undertake thorough planning. The planning will provide the foundation on which the business will be built. Strong, firm foundations will usually result in a successful business.

Case study: McDonald's franchises — role of a business plan

Buying into a franchise requires the franchisee to make a huge financial and time commitment. It takes hard work and long hours to become successful. A business plan is also essential. McDonald's expects its franchisees to be able to create and implement business plans with short-term and long-term objectives.

The owner of the McDonald's franchise in Tecoma, Victoria knows all about business planning. While planning and setting up the outlet, he had to deal with opposition from the Yarra Ranges council, angry protesters demonstrating at the construction site and his Boronia store, and media coverage.

'It's certainly been a long road but I'm really proud of the restaurant we've built — it's a beautiful building that absolutely fits in with the local surrounds and, more importantly, it's created over 100 local jobs,' James Currie says.

James started working for McDonald's when he was 15. He cleaned the floors for two years and then started on a management development program. He became a restaurant manager at age 23. A few years later, he gained the qualifications necessary to became a training consultant and helped to open stores in Victoria, New South Wales, Tasmania and South Australia. He then started to buy McDonald's franchises as a family business with his wife and sons.

'We obviously did our research in Tecoma — as we do with all of our sites — and we knew that there was a demand and local community support for us in Tecoma,' he says.

Mr Currie declared the opening a success. Around 4000 people passed through the Burwood Highway restaurant during its 12-hour opening day in 2014, and more than 20 000 customers passed through in the first week of trading. McDonald's Australia said that it was confident that locals would continue to support the restaurant.

One local who has lived in the town for over 40 years commented that it is the best thing that has happened to the town.

SNAPSHOT QUESTIONS

1. **Identify** the difficulties James Currie faced when planning his new McDonald's store.
2. **Explain** how business planning influenced the success of this franchise.

SNAPSHOT



'McDonald's expects its franchisees to … create and implement business plans …'

However, preparing the business plan is only the first stage. Many SME owners realise the need to prepare a business plan before establishing a business, but they then make a fundamental mistake — they forget to constantly refer back to their plan. This would be similar to a student preparing a set of summary notes for a topic and then never looking at them.

Even if a SME owner manages to avoid the mistake of not regularly consulting the business plan, there is still another trap. An inexperienced person may not be flexible enough to modify their business plan as the internal and external business environments change. Sticking too rigidly to a plan, and not adapting it to suit the changed conditions, can be as detrimental as not having a plan.

The business plan must always be seen as a working document. It is not a straitjacket restricting the business and preventing change. The unexpected can and often does happen. Unfavourable factors, such as a customer not paying an account or a new competitor moving into the market, will force the business owner/manager to modify their plan. Favourable conditions such as a new marketing opportunity will need to be seized and they will also require some modification to the plan.

on Resources

Weblink: Business plan resources

12.1.2 What is a business plan?

A business plan is exactly what it says — a plan for a business. It is a written statement of the business's goals and the steps to be taken to achieve them. In other words, it is a summary and an evaluation of a business idea in written form. The 'writing' is important because ideas tend to be no more than wishful thinking until transferred to paper. Thinking about something is not planning. A few ill-conceived ideas scribbled on the back of an envelope are likely to lead to business failure.

A comprehensive business plan will assist when arranging finance for the business. The plan provides information that lenders need to know and it also shows that the business is being properly organised and managed.

If a business plan is so important, why do some people attempt to establish a business without first preparing one? Figure 12.2 highlights some of the main reasons.

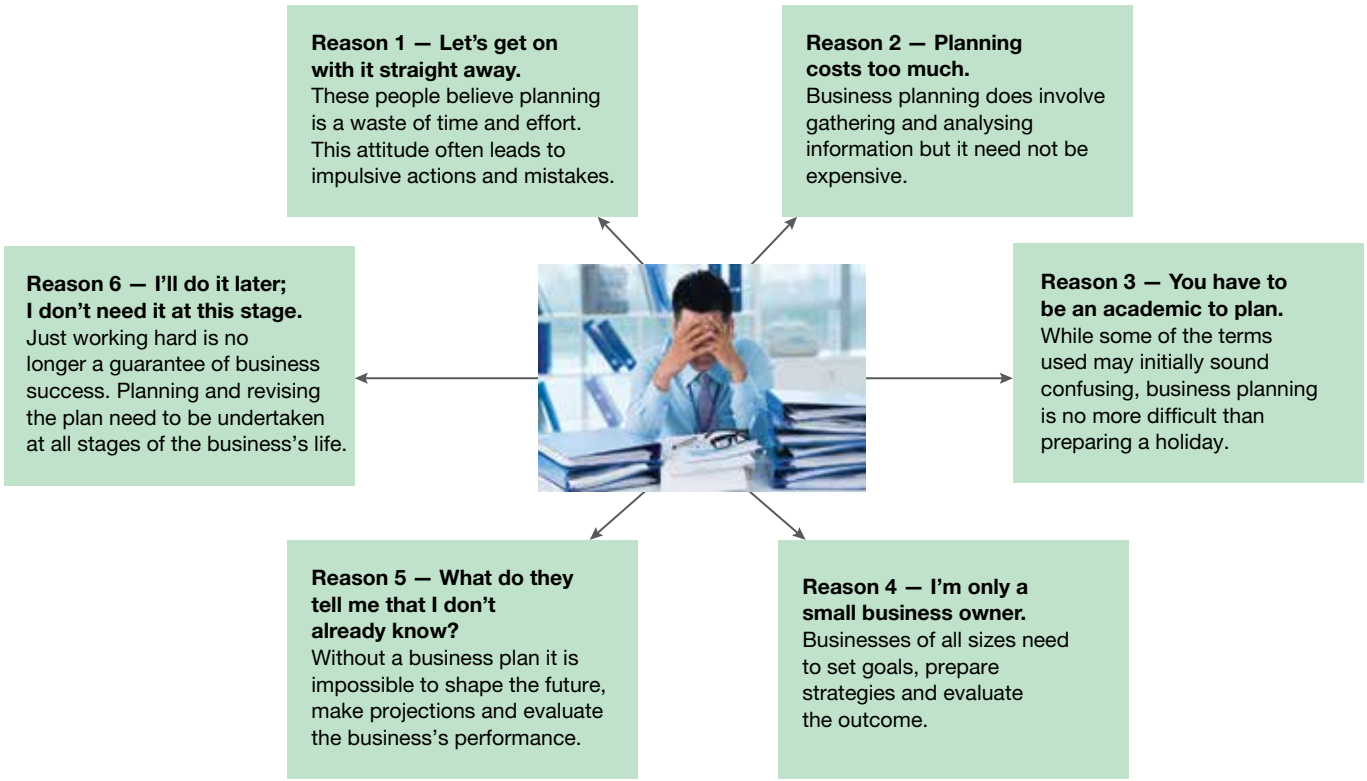


FIGURE 12.2 The main reasons for business owners' failure to plan

Planning is not always easy and it can be time consuming. However, the time invested in planning is never wasted in the long run, for, with it, the chances of success are greatly improved.

Just as no two businesses are identical, neither are any two business plans. Each plan will be unique, containing information and strategies that apply to one particular business. A business plan for a transnational corporation, for example, will be detailed and comprehensive. It will add up to hundreds of pages, having taken much time, effort and money to prepare. Its presentation will be highly professional and distributed to a large number of the company's senior management. On the other hand, a business plan for a SME may be only 10–15 pages in length, word processed at home and circulated to only a few people.

Depending on variables such as the product, the market, the size of the business and its location, each business will have a unique set of information in its business plan. However, regardless of their type, length, appearance and distribution, all business plans have a number of common elements, as shown in table 12.1.

BizFACT

A business plan is essential for those business owners who wish to thrive and not just survive.



FIGURE 12.3 There is nothing mysterious about planning. It simply means deciding in advance where the business is heading and working out the details of how to get there. Planning is required to achieve your goals in assessment tasks. It is the same in business.

TABLE 12.1 The common elements of a business plan

Element	Purpose
1. Executive summary	A brief overview of the plan
2. Goals	What the business hopes to achieve
3. Strategies	An overview as to how the business will attempt to achieve the goals
4. Business description and outlook	An overview of the industry in which the business will operate, including a situational analysis
5. Management and ownership	The nature and type of organisational structure
6. Operational plans	Details the production process and the people required now and in the future
7. Marketing plans	The product, price, promotion and distribution details
8. Financial plans	A description of the business's financial needs and methods for evaluating its performance
9. Human resource plans	Details both the present and future staff requirements

While all business plans contain similar information, a comprehensive and detailed business plan is most beneficial. A sketchy, quickly prepared business plan will not serve any lasting purpose. Some plans may only briefly refer to some of the areas, but all points need to be at least considered.

12.1.3 Benefits of a business plan

The planning process acts as a link or bridge between the business owner's ideas and the actual operation of the business; it is a way of turning dreams into reality. The written plan becomes a useful reference point for the running of the business. Any small business with a plan has direction, which ultimately saves money, time and effort, and also increases the likelihood of success. Preparing a business plan is very similar to completing an assessment task. The result will reflect the amount of time, effort and research that goes into the plan and its final presentation.

BizFACT

'Preparing a business plan allowed me to think through a lot of important issues before commencing my business. This helped avoid many pitfalls.' Troy Bartlett, owner of Bartlett Precision Manufacturing.

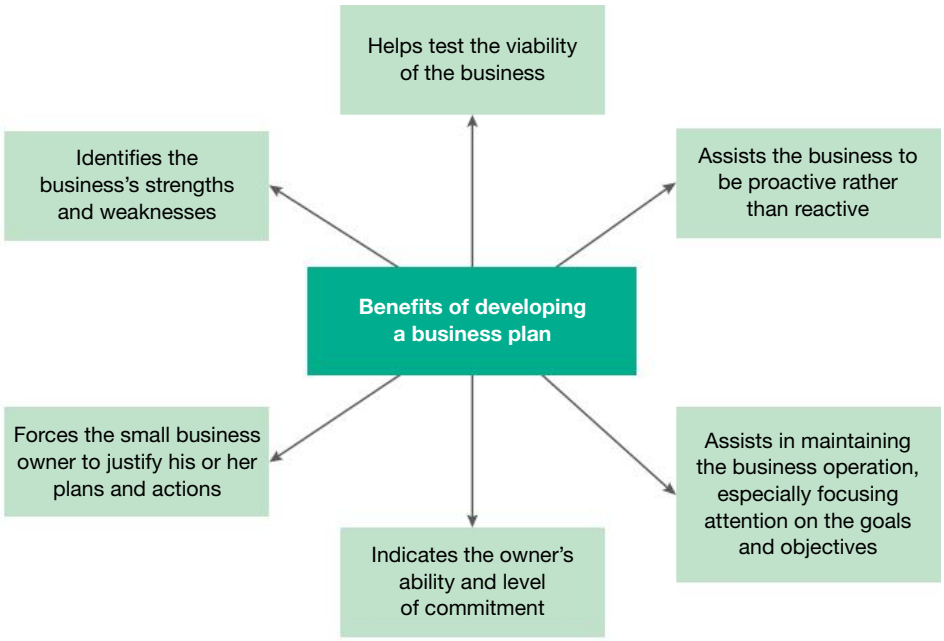


FIGURE 12.4 The benefits of developing a business plan

How one SME determined its business plan

SNAPSHOT



'… business planning brings clarity to his business.'

Case study: Marketing4Restaurants — it's all about the plan

James Eling is the owner of Marketing4Restaurants, a business that provides a variety of marketing tools to help restaurants and cafés find new customers and turn them into repeat customers. He has built a team of employees who are passionate about helping restaurant owners run small businesses that are profitable and fun.

James Eling believes that business planning brings clarity to his business. His business plan acts as a 'road map' for his business. He draws up five-year, one-year and 90-day goals for his company, which then reveal the missing pieces in his strategy that are needed to meet those goals. 'It raises a whole heap of questions and those questions form part of your short-term goals,' he says.

In his business plan, Eling also includes analysis of his industry, the customers and competitors. That analysis revealed, for instance, that distribution channels were the biggest hurdle the business faced, allowing him to focus more effort there.

Eling says he also knows the costs of not having a business plan. Extreme Networks, an IT business founded by him and his wife, was named a BRW Fast 100 company in 2004 and doubled its revenue in 2007, but soon after gave up on business plans. 'At that point, we thought we were really good at running an IT company and we just lost focus and were going backwards,' James says. 'Probably our biggest regret in the 15 years that the company's been running were those five years that were completely wasted.'

SNAPSHOT QUESTIONS

1. **Outline** some of the information that James Eling includes in his business plan.
2. **Explain** how James Eling has benefitted from a business plan.

12.2 Business planning process

Planning is a process, a series of actions to achieve a goal. If you decide to have a party next Saturday night, for example, this becomes your goal. Unless you undertake some planning you will be unable to achieve this goal. You will need to

invite people, organise food and drinks, arrange music and decide on a venue. These tasks are the 'series of actions' — an action plan — that you need to undertake to achieve the goal. **Planning** is therefore the preparation of a predetermined course of action for a business. It refers to the process of setting objectives and deciding on the methods to achieve them.

Planning is not always straightforward. However, a number of activities can be undertaken to make it easier (figure 12.5). A business plan is far more than just listing a few ideas. It is more than merely drawing up a marketing timetable or keeping financial records. The business plan needs to analyse the whole business by examining all parts of the operation. As a result, each part of the business can function effectively and achieve its goals, helping the overall success of the business.

BizWORD

Planning *is the preparation of a predetermined course of action for a business. It refers to the process of setting objectives and deciding on the methods to achieve them.*



Party example	Activities — something you do	Terms — the names of what you will be doing
I think my friends would like a party.	1. Predicting something in the future	Forecasting
I want it to be a successful party.	2. Determining what you wish to achieve	Setting goals
Anyone who becomes aggressive will be forced to leave.	3. Outlining how to cope with any current and future problems that stand in the way of achieving the goal	Formulating policies
I will: • invite people • arrange a venue • organise food and music.	4. Deciding on a course of action — that is, the tasks that will help achieve the goals	Programming Scheduling
I'll borrow $200 from Michelle.	5. Arranging the finances to satisfy the goals	Budgeting
PARTY!	6. Putting the plans into action	Implementing
I want everyone to enjoy the party.	7. Checking on the progress of the activity, evaluating and adjusting the plans if necessary	Monitoring Evaluating Modifying

FIGURE 12.5 You need to consider a range of planning activities, whether your goal is a party or business success.

Government departments — such as the New South Wales Small Business Commissioner or the federal government's business.gov.au — provide free and comprehensive advice on a wide range of small business matters including how to write a business plan. As well, numerous small business magazines often contain articles examining business planning.

on Resources

Weblink: business.gov.au



FIGURE 12.6 The business.gov.au website contains a wealth of information about how to write a business plan, including templates, reference material and an app to help create one.

SUMMARY

- It is vital that a SME owner completes a business plan. Businesses do not plan to fail, they fail to plan.
- A business plan is a written statement of the goals for the business and the steps to be taken to achieve them. It is a summary and an evaluation of a business concept in written form.
- A business plan will also assist the SME owner when arranging finance for the business.
- A typical business plan may include, as a minimum, an executive summary, an operations plan, a marketing plan, a financial plan and a human resource plan.
- The planning process acts as a link or bridge between the business owner's ideas and the actual operation of the business.
- Planning is the process of setting goals and deciding how to achieve them.

EXERCISE 12.1 REVISION

1 **Define** the term 'business plan'.
2 **Explain** why it is important for a business owner to develop a business plan.
3 **Why** do many SMEs fail to prepare a business plan?
4 A friend has asked you to help her prepare a business plan for a new fitness centre she wants to open. **Propose** the elements she should include in the business plan.
5 'A plan is similar to a travel itinerary — it plots the route the business will travel.' **Discuss**.
6 **Explain** how the business plan acts as a link or bridge between the owner's ideas and the actual operation of the business.
7 **Identify** the benefits of developing a business plan.
8 **Explain** why planning is a process.
9 Examine figure 12.5 (section 12.2), then **create** a plan for one of the following:
(a) taking an overseas holiday
(b) completing an assessable task
(c) organising a hockey match.
For each plan briefly **outline** what is required for each activity.

10 **Identify** the most appropriate words from below to complete the following sentences.

plan	strengths
direction	fail
review	costs
link	loan
flexible	goals

(a) Businesses do not plan to _____, they fail to _____.
(b) Business plans should be _____ — that is, modified as conditions change.
(c) A business owner should regularly _____ the business plan and modify it when the business environment changes.
(d) Without a business plan, the business lacks _____.
(e) Many business owners do not prepare a plan because they think it _____ too much.
(f) When reviewing an application for a _____, financial institutions will want to examine the business plan.
(g) _____ are what you want to achieve.
(h) A business plan helps identify the business's _____ and weaknesses.
(i) The planning process is the _____ between the owner's ideas and the actual operation of the business.

11 Use the **Business plan** weblink in the Resources tab or other websites on business start-ups to find advice concerning the preparation of a business plan. **Evaluate** the benefit of this and similar sites to someone wanting to start a small business.

on Resources

Weblink: Business plan

EXERCISE 12.1 EXTENSION

1 'Businesses do not plan to fail, they fail to plan.' **Critically analyse** this statement.

2 Interview a local small business owner to **investigate** the following aspects of the business:
(a) the planning options that had to be considered when starting the business
(b) the purpose of the business plan
(c) the role of the business plan within the operation of the business
(d) the importance of planning to the overall success of the business
(e) the government departments and/or private organisations that offered assistance in developing a business plan.
Present your research as a business report. You may wish to present your report as a presentation.

3 'The process of planning is more important than the finished plan.' **Determine** the benefits this process offers a SME owner.

4 Bruce Thurow, senior loans manager for a local bank, receives a lot of business plans from clients. He recalls one plan that arrived in three cardboard boxes as volumes of looseleaf notebooks. Overkill? 'I knew I wasn't going to read them. I just put them aside.' In small groups, **determine** why such a detailed plan was inappropriate when all the small business owner was requesting was a small loan.

12.3 Sources of planning ideas

We have already examined how the business environment is divided into two categories:

1. *the internal business environment*. This covers the factors within the direct control of the owners. It represents what occurs within the business.
2. *the external business environment*. This is the larger environment within which the business operates. It consists of factors over which the business has little control and represents what occurs on a larger scale outside the business.

Information is the essential ingredient needed to prepare a business plan. Having access to up-to-date, relevant and accurate information will allow the business owner to prepare a much superior business plan. Information for planning is obtained from different sources within and outside the business. The different levels of management and, in many cases, employees, may contribute ideas about how the business could achieve its goals. Research and development undertaken by a business may extensively contribute to planning.



FIGURE 12.7 All of the facts and information that are relevant to the business plan must be gathered. Some methods to use might simply be talking to people or completing surveys.

The external environment is also a source of ideas for planning. Economic, political, social, technological, geographic and legal factors have an impact on the business. The business must account for each factor during the planning stage and gather information about each one. Specialists such as accountants, finance brokers, consultants, bank managers and solicitors all provide knowledge to assist a business in its planning.

12.3.1 Situational analysis

A situational analysis refers to a collection of methods that managers can use to analyse a business's internal and external environment. One method of analysis is a SWOT analysis. A **SWOT analysis** is an excellent technique for gathering information for use in the business plan. SWOT is an acronym for strengths, weaknesses, opportunities and threats (see figure 12.8). It is a powerful tool that can be used at all stages of the planning process. Analysis of the business's strengths and weaknesses is an internal analysis. Given that the business has a degree of control over its internal environment, the analysis will provide information that can help place the business in a stronger financial position. From this position, the business can set new goals.

Analysis of the business's opportunities and threats is an external analysis. Particularly important to the business plan is the identification of unmet or unsatisfied demand that the business can perhaps satisfy. At the same time, the business owner should attempt to convert threats into opportunities.

BizWORD

A **SWOT analysis** *involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment.*

on Resources

Weblink: SWOT analysis

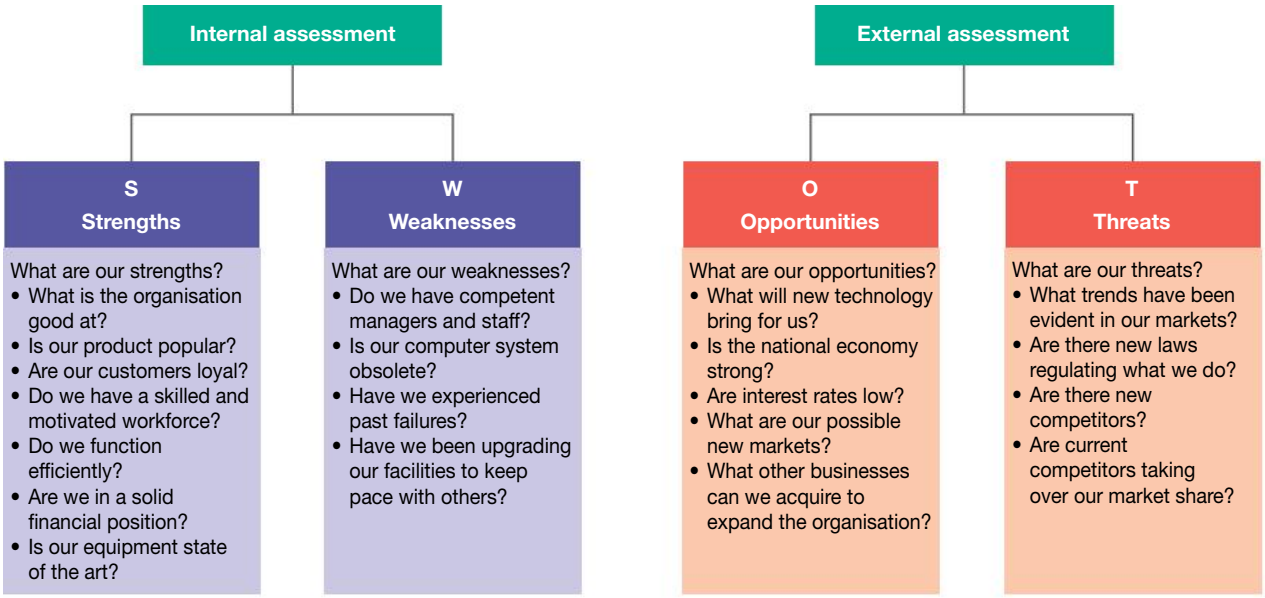


FIGURE 12.8 A SWOT analysis

SUMMARY

- The internal and external business environments are sources of planning ideas.
- Information is the essential ingredient needed to prepare a business plan.
- A situational analysis refers to a collection of methods that managers can use to analyse a business's internal and external environment. One method of analysis is a SWOT analysis.
- A SWOT analysis can be used at all stages of the planning process.

EXERCISE 12.2 REVISION

1 **Distinguish** between a business's internal and external environments.
2 **Identify** two sources of information for planning (i) within, and (ii) outside the business.
3 **Recall** what the acronym SWOT represents.
4 **Outline** the benefits of a situational (SWOT) analysis as a planning tool.
5 **Construct** a situational (SWOT) analysis for either:
(a) a business that you deal with regularly
(b) your school.

EXERCISE 12.2 EXTENSION

1 'The most important aspect of the business planning is the process of examining the environment, one's self and the business opportunities the two represent.' **Analyse** the accuracy of this statement.
2 In small groups, use the brainstorm technique to **determine** the advantages of obtaining ideas from employees in the planning process.

12.4 Vision, goals and/or objectives

12.4.1 Vision

A business's vision is often expressed in their vision statement. A **vision statement** broadly states what the business aspires to become in the future. The vision of the Commonwealth Bank is 'to excel at securing and enhancing the financial wellbeing of people, businesses and communities'.

BizWORD

*A **vision statement** broadly states what the business aspires to become in the future.*

Vision statements may relate to customers (using such phrases as 'maximise customer satisfaction', 'remember that customers are our strength', 'never have a dissatisfied customer') or employees (for example, 'make the firm an enjoyable and rewarding place to work', 'offer opportunities for career advancement', 'remember that our employees are our strength'). A clear vision statement should be concise, creative, focused and realistic. It may contain any special features of the business, what it values and what it hopes to achieve.

The main purpose of the vision statement is to guide and direct the business owners, managers and employees. It creates the culture within the business and acts as a benchmark against which to measure all the business's decisions and operations.

BizFACT

Vision statements are sometimes called mission statements. The two terms are often used interchangeably.

IKEA
'To create a better everyday life for the many people'

Westpac
'To be one of the world's great service companies, helping our customers, communities and people to prosper and grow'

RSPCA
'To be the leading authority in animal care and protection'

National Museum Australia
'A recognised world-class museum exploring Australia's past, illuminating the present, imagining the future'

Oxfam
'a just world without poverty'

FIGURE 12.9 Vision statements from a range of businesses

12.4.2 Goals and/or objectives

Once the owner has formulated the vision statement for the business, he or she can determine specific goals. People start up a business because they want to achieve something; they have a goal they want to accomplish. As explained in chapter 6, a goal states what a business expects to achieve over a set time, which will assist in realising the business's vision.

Goals for businesses could include the following:

- to become the largest business in the market
- to improve market share
- to provide a reasonable return for investors
- to contribute to the wellbeing of the community.

All these goals have one thing in common: they are the motivating force behind the business.

APPLYING BUSINESS MANAGEMENT THEORIES TO A PRACTICAL ACTIVITY

Ask your teacher for permission to complete this activity in class time. The aim of this activity is to apply your theoretical understanding of business management to a practical activity.

Instructions

1. Arrange your class into groups of three to four.
2. Find a place where your class can set up to have shots at basketball rings. You or your teacher may need to book the school gym or the basketball court.

(*Note:* Other sports can be substituted, so long as it is possible to achieve the objective of the activity — to score a goal.)

3. Work out an order among the members of your group. Every student should have 10 shots at goal.
4. As each student is shooting at goal, record the result. Did they score a goal, hit the ring or miss completely?

Materials required

- Basketballs
- Basketball rings
- Space

Questions

1. How can you measure the effectiveness of your group's performance in this activity?
2. Can you think of a way to measure your group's efficiency?
3. Complete the following table, using the results from your goal shooting. The table has already been started for you.

	Efficient	Inefficient
Effective	Score a goal from every shot	
Ineffective		

Levels of goals and objectives

Once the goals have been established, a SME owner usually then decides how to achieve them. As outlined in section 12.2, this involves developing an effective and worthwhile action plan. The action plan breaks down the goals into **objectives** — specific statements detailing what a business (or individual) needs to achieve in order to accomplish its vision. For example, you may have a goal of achieving a certain result in the Business Studies Trial HSC examination. Consequently, you will need to set some objectives, such as increasing by 60 minutes each week the time spent revising past papers, or weekly practice sessions answering 10 multiple choice questions.

In a business, senior management will normally set the **strategic goals**, which focus on long-term, broad aims and apply to the business as a whole. For example, the chief executive officer (CEO) may establish a strategic goal of 'increasing market share'. This will involve the input of the four key business functional areas — operations, marketing, finance and human resources. Middle management set **tactical objectives**, which focus on mid-term, departmental issues and describe the course of action necessary to achieve the business's strategic goals. To use the example of increasing market share, a marketing manager may set a tactical objective of researching consumer tastes and preferences in order to help achieve the strategic goal. Front-line managers or supervisors set **operational objectives**, which focus on short-term issues and describe the course of action necessary to achieve the business's tactical objectives. For example, a marketing supervisor may set an objective of arranging for 20 customers to attend a focus group, research session to help achieve the tactical objective and strategic goal.

In practice, think of the levels of goals and objectives as pyramid-shaped as shown in figure 12.10.

BizWORD

An **objective** *is a specific statement detailing what a business (or individual) needs to achieve in order to accomplish its vision.*

Strategic goals *focus on long-term, broad aims and apply to the business as a whole.*

Tactical objectives *focus on mid-term, departmental issues and describe the course of action necessary to achieve the business's strategic goals.*

Operational objectives *focus on short-term issues and describe the course of action necessary to achieve the tactical objective and strategic goal.*

BizFACT

The terms goal and objective are often used synonymously as both terms refer to something a business wants to accomplish. However, the people, timeframe and resources involved in achieving each goal and objective vary significantly.

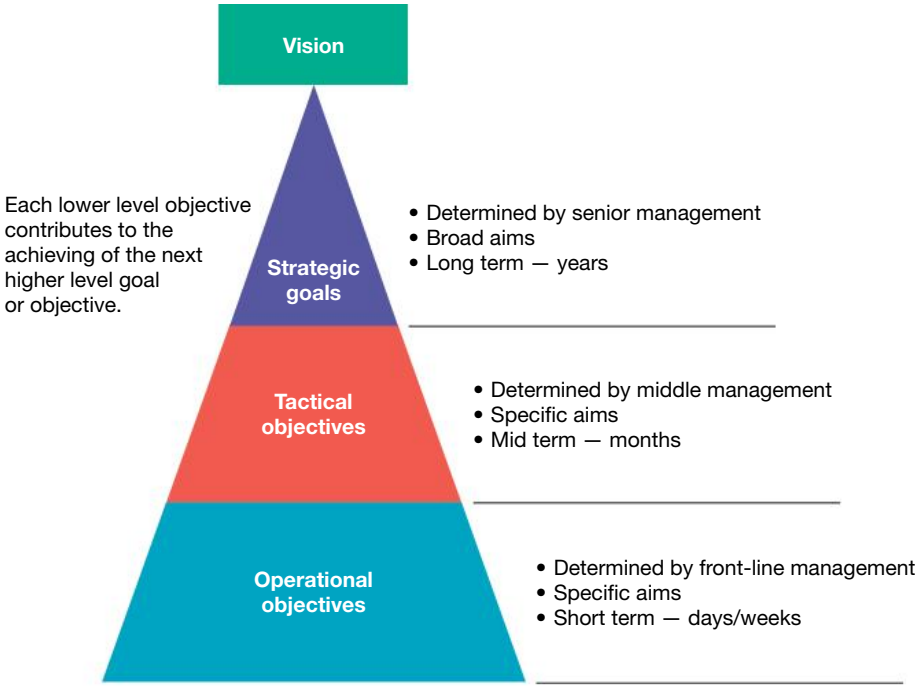


FIGURE 12.10 The objectives established at each layer of the business's hierarchy are devised with the purpose of helping to achieve the strategic goal.

A business needs to have a clear idea of what it is trying to achieve; in other words, it needs clear goals and objectives. It is the interaction between the vision statement, goals and objectives that provide a process for a business to accomplish this (see table 12.2).

TABLE 12.2 The relationship between a vision, goal and objective

Term	Definition	Personal example	Business example — renewable energy company
Vision	Broad statement of overall purpose	Be healthy	To be a company of choice in the alternate energy sector
Goal	More specific statement of what is intended to be achieved	Lose weight	To be the market leader in alternate energy sales
Objective	Very specific statement of how the goal is to be achieved	Lose two kilograms by 1 December	To increase sales by 10% each year

As explained in chapter 6, common business goals include:

- maximising profits
- increasing market share
- growth
- improve share price
- social goals
- environmental goals.



FIGURE 12.11 Michel's Patisserie's main business goal is to maximise growth. Franchising is the engine behind their incredible growth. The business is well established and resourced for continued growth within Australia.

12.4.3 Long-term growth

As outlined in chapter 6, an important aspect of profit maximisation is the business's ability to maintain profits over time. To achieve this, a business must aim for **long-term growth** — the ability of a business to continually expand.

Long-term growth depends on a business's ability to develop and use its asset structure to increase sales, profits and market share. It is an important goal of management as it ensures that the business is sustainable into the future. Seven West Media's chief executive, Tim Worner, recently outlined his strategy for long-term growth. Since traditional media, such as TV and newspapers, are facing growing competition, Seven's long-term objective is to fuel new growth and diversify their earnings outside of television and newspapers. The way they want to achieve this objective is through investing in new start-ups that will add value to their core businesses. Seven has added more than 10 investments to its portfolio, including Airtasker, Nabo and Society One.

Long-term growth does not happen accidently. Instead, it requires comprehensive, strategic planning. Consequently, for a business to not only survive competition but also prosper and grow, it must have a sustainable competitive advantage. This can be achieved by having a unique good or service, a consistent marketing plan and adopting a relationship marketing philosophy to encourage customer loyalty. For example, a number of factors give Apple a global competitive advantage, such as their product designs, ability to create software that is easy to use, low cost manufacturing, innovation, creative marketing strategies, product and service integration, and their strong brand name and reputation. These are only a few of the factors that have made the company so successful.

Some other strategies that successful businesses have used to achieve long-term growth include:

1. **Customer feedback**. Google, the internet's number one search engine, continuously and rapidly upgrades its operating system by listening to its customers.
2. **Supplier and customer partnerships**. Bridgeport Manufacturing provides customers with the opportunity to develop products in consultation with the business's designers.

BizWORD

Long-term growth *is the ability of a business to continually expand.*

3. **Cost**. IKEA focuses on producing products that are affordable for most people to buy. The company is constantly trying to do do things more efficiently and cost-effectively so they can maintain their low prices.
4. **Sigma Six**. This business management approach, originally developed by Motorola and used extensively in all types of businesses, aims to improve business performance by improving quality, reducing costs and creating new opportunities. A **sigma-six** process is one in which 99.99 per cent of all manufactured products are defect free.
5. **Staff motivation.** Many businesses have found that aligning staff motivation with business objectives inspires employees to work harder to achieve the business's goals.

BizWORD

*A **sigma-six** process is one in which 99.99 per cent of all manufactured products are defect free.*



FIGURE 12.12 Tourism Australia, in cooperation with industry and the Australian and state and territory governments, developed a national long-term tourism strategy, Tourism 2020, which was launched in December 2009. Tourism 2020 is a whole-of-government approach to improve the tourism industry's productive capacity. It focuses on creating a policy framework that will support industry growth and provide the tourism industry with the tools to compete more effectively in the global economy.

SUMMARY

- The vision statement broadly states what the business aspires to become.
- Vision statements guide and direct the business owners, managers and employees.
- Once the goals have been established, a SME owner determines the objectives.
- Objectives are specific statements detailing what a business needs to do to accomplish its vision.
- Strategic goals, tactical and operational objectives are determined by different levels of management.
- Many businesses strive to achieve goals relating to profits, market share, growth and share price as well as social and environmental goals.
- Longer term growth is the ability of a business to continually expand.
- Longer term growth depends on a business's ability to develop and use its asset structure to increase sales, profits and market share.

EXERCISE 12.3 REVISION

1 Select a number of annual reports for public companies. **State** the vision (or mission) statements for each company. **Explain** how these relate to the business's goals. To help you, you could use the **Business vision statements** weblinks in the Resources tab for the following public companies:
(a) Boral Limited
(b) Westpac Limited
(c) Origin Energy Limited
(d) Woolworths Limited.

2 **Identify** which of the following are vision statements. Give reasons for your answers.
(a) All breakages must be paid for.
(b) Care for the customer is our number one priority.
(c) Application of an integrated accounting system
(d) A safe and healthy workplace
(e) Commitment to excellence
(f) To increase sales revenue by 5 per cent in the next six months

3 **Recall** three main goals of most businesses.

4 **Outline** the relationship between goals and objectives.

5 **Identify** three objectives you would need to set if you wanted to achieve the goal of improving your Business Studies results.

6 **Distinguish** between strategic goals, tactical objectives and operational objectives.

7 **Deduce** why a business needs clear goals and objectives.

8 **Recall** the correct level of management that determines the following goal or objective.

Goal or objective	Level of management
Strategic goal	
Tactical objective	
Operational objective	

9 **Define** the term 'longer term growth'.

10 **State** three methods a business can use to achieve a competitive advantage.

11 **Outline** five strategies a business can use to achieve longer term growth.

EXERCISE 12.3 EXTENSION

1 'The main goal of a business is to maximise profits.'
(a) **Define** the term 'profit'.
(b) **Determine** under what circumstances a business may be prepared to accept reduced profits in the short term.
(c) In your opinion, **assess** whether profit should be the only goal of a business.

2 Arrange to interview a local business owner. **Create** a business profile by asking the following questions.
(a) What motivated the owner to start the business?
(b) Why is there a need for the business's goods or services?
(c) How has the business been funded?
(d) Has the business been upgraded or expanded?
(e) What are the future growth areas of the business?
(f) What has been the business's biggest problem or greatest mistake?
(g) What external threats face the business?

3 **Examine** figure 12.9 (section 12.4.1), then answer the following questions.
(a) **Identify** the common features of these vision statements.
(b) **Explain** why it would be important for employees, managers and customers to be familiar with a business's vision statement.
(c) **Determine** under what circumstances the vision statement would need to be altered.

on Resources

Weblink: Business vision statements

12.5 Organising resources

Once the SME owner has formulated the vision, goals and objectives, the next stage in the planning process requires organising the resources — human effort, time, money, equipment and materials — needed to fulfil the plan. As outlined in chapter 7, organising is determining:

- what is to be done
- who is to do it
- how it is to be done.

BizWORD

An **organisational structure** *is the framework in which the business defines how tasks are divided, resources are used and departments are coordinated.*

At this stage, the owner must determine all the activities that employees perform — from ordering stock through preparing financial reports to meeting with clients — and all the equipment, money and facilities that employees need to carry out those activities (see figure 12.13). This results in the creation of an **organisational structure**, which defines how tasks are divided (as shown by the organisation chart) and resources used.

While driving the business towards its central purpose, as expressed in the vision statement, the benefits of a properly implemented organising process is that it:

- establishes a chain of command that results in an orderly way of communicating within the business
- creates a coordinated work environment by outlining sensible guidelines for who does what and who is responsible for various activities
- provides a sense of common purpose so that all employees are working towards a common vision, goal or objective
- organises resources in the most efficient manner so that all employees can perform their tasks.

BizWORD

Resource allocation *refers to the efficient distribution of resources so as to successfully meet the goals that have been established.*

Organising is a device that SME owners can use to gather resources for getting things done. Part of the organising process requires **resource allocation**, which refers to the efficient distribution of resources so as to successfully meet the goals that have been established. Resource allocation establishes what work will be performed by what person and/or machine, and under what conditions. The materials needed must be determined and ordered. The work tasks must be distributed to different departments. Human resource requirements must be calculated and time schedules set for each stage of the production process.

Each of the key business functions — operations, marketing, finance and human resources — require specific resources that need to be effectively organised.

12.5.1 Organising resources — operations

As outlined in chapter 8, the operations function of a business involves transforming different types of inputs (raw materials, labour, equipment and other resources) into finished or semi-finished goods or services. To produce either a good or service, therefore, a business needs to have essential equipment and knowledge. Consequently, to undertake successful production, the following questions will need to be asked.

- What type of equipment and raw materials are needed?
- Which suppliers will be used to purchase the equipment and raw materials?
- How much money needs to be allocated for the purchase of the raw materials and resources?
- What storage, warehouse and delivery systems are required?
- What level of technical expertise will employees need to achieve maximum production from the raw materials and equipment?

Researching the answers to these questions enables the SME owner to clarify what changes may need to be made to either the structure of the business or the production process. For example, Caroma, Australia's leading bathroom manufacturer, needed to purchase automated robots for their production process. To arrange for the finance required to purchase the new machines, the managers had to revise their business plan. Organising their operational resources in this way has enabled the company to become a market leader.

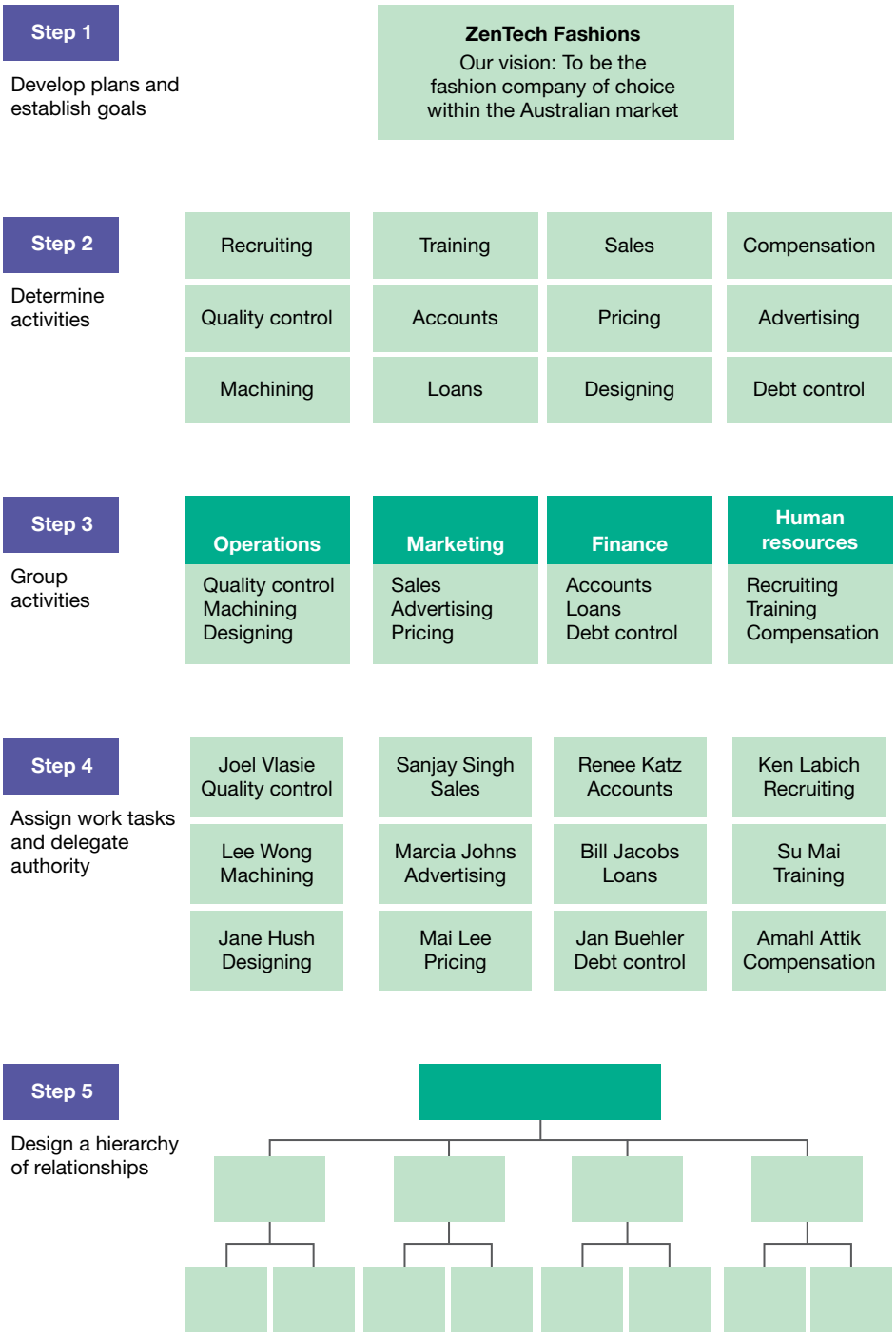


FIGURE 12.13 The five steps involved in the organising process (organising resources)

12.5.2 Organising resources — marketing

As outlined in chapter 8, a marketing plan will succeed only if all sections of the business are involved in satisfying a customer's needs and wants, while achieving the business's goals. This means that the marketing plan needs to become integrated into all aspects of the business. Adequate resources, therefore, must be devoted to the marketing plan. Where existing employees do not have the expertise or levels of skills required, additional training may be needed to bring them up to the levels needed. Additional funds may be needed to accomplish all the marketing objectives given to a specific department or team. The efforts of all employees in the marketing department must be coordinated and this is best achieved by adequate resourcing. For example, the sales consultants, advertising personnel,

market research staff, distribution people and so on must be provided with the informational, financial and physical resources to perform their jobs.

12.5.3 Organising resources — finance

As outlined in chapters 8 and 11, new business ventures, even micro ones, require funds to operate. In organising the financial resources, one of the most important questions the SME owner needs to answer is 'What will be the most appropriate source of financing?' The most common sources are personal savings and/or loans from family, friends or banks.

Another important issue associated with organising finances is the amount of equity (ownership of the business) and potential control a SME owner must hand over to obtain the necessary financing. If the SME owner decides to fund the business by using equity capital, the investor will be given some form of ownership in the business. Frequently, SMEs that are aiming for relatively moderate growth use mainly debt capital with the owners retaining most or all of the equity.

BizWORD

*A **grant** is any monetary or financial assistance that does not generally have to be repaid.*

Finally, when organising the financial resources, the SME owner must explore the wide range of federal and state government **grants** — any monetary or financial assistance that does not generally have to be repaid — and other funding programs. Generally, there are no grants for starting a business. Grants are usually provided for:

- expanding a business
- research and development
- innovation
- exporting.



FIGURE 12.14 Melbourne City Rooftop Honey aims to help save honey bees by encouraging them into the city and suburbs through the deployment of hives on the roof spaces of cafés, restaurants and hotels in and around Melbourne. The business has received grants to assist with starting up and for purchasing materials and equipment, including a $1000 grant from the Awesome Foundation and a $28 000 City of Melbourne grant.

12.5.4 Organising resources — human resources

Of course, new business ventures often require the help of others — employees — besides the entrepreneur or SME owner. In fact, since each employee in a SME represents a large percentage of the business's workforce, a specific individual's

contribution can be especially important to the success of the business. This is why, as explained in chapter 8, employees are a SME's most important resource. A great deal of care and thought, therefore, needs to be given to how best to organise this crucial resource.

SME owners need to use good recruitment and selection processes to find employees who will be invaluable assets as the business grows and expands. For example, when Danaye Stavropolous started her business, Gateway Information Systems Pty Ltd, she decided to employ people who had limited experience but displayed a keen desire to learn and an enthusiasm for the business idea. As the business grew, Danaye organised the business's human resources in such a way as to ensure extensive training for all employees, which allowed her to generally recruit from within. As a result, her business has a skilled group of employees to support her expansion plans.

Other important aspects all SME owners need to consider when organising their human resources is to provide adequate training and development for staff, to seek ways to motivate and retain employees, and to ensure they comply with existing legislation relating to employees. The retailer Myer, for example, was able to retain valuable employees when it introduced a policy of six weeks paid maternity leave for staff who had worked a minimum of 18 months.



FIGURE 12.15 It is crucial that all businesses undertake some human resource planning to accurately identify future staffing needs and help with organising their human resources. Human resource planning includes the development of strategies to meet the business's future staffing needs, forecasting the future demand for employees and estimating the supply available to meet that demand.

SUMMARY

- Once the SME owner has formulated the vision, goals and objectives, the next stage in the planning process requires organising the resources — human effort, time, money, equipment and materials — needed to fulfil the plan.
- Organising is a device that SME owners can use to gather resources for getting things done.
- Resource allocation refers to the efficient distribution of resources so as to successfully meet the goals that have been established.
- Each of the key business functions — operations, marketing, finance and human resources — require specific resources which need to be effectively organised.

EXERCISE 12.4 REVISION

1. Examine figure 12.13 in section 12.5.1. **State** the five steps of the organising process.
2. **Summarise** the benefits of a properly implemented organising process.
3. **Define** the term 'resource allocation'.
4. Imagine you have been asked to make 50 family-size pizzas for a celebration lunch. You have five people to help with the task. In small groups:
   (a) **Identify** the resources you would need to make the pizzas.
   (b) **Classify** the resources as either (i) raw materials, (ii) equipment or (iii) knowledge.
   (c) **Demonstrate** how you would allocate the resources.
5. **Recall** five questions a SME owner needs to ask in order to undertake successful production.
6. **Propose** what may happen if a SME owner fails to organise adequate resources for the marketing plan. Give reasons for your answer.
7. **Identify** the two main sources of finance for a business.
8. **Investigate** the range of grants available for business and industry. You can use the **Grants and assistance** weblink in the Resources tab to help get you started. Select two grants that interest you and briefly **outline** their purpose.
9. Use the brainstorm technique to **deduce** three advantages Gateway Information Systems Pty Ltd received by organising its human resources as it does.

on Resources

Weblink: Grants and assistance

EXERCISE 12.4 EXTENSION

1. **Create** an organisational chart for your school. **Determine** the advantages and disadvantages of this structure for you as a student.
2. 'The purposes of organising are to give each employee a distinct task and to ensure these tasks are coordinated and adequately resourced so that the business achieves its goals.' **Evaluate** the accuracy of this statement.

12.6 Forecasting

BizWORD

Forecasts (or projections) *are the business's predictions about the future.*

A business needs more than just information about present business conditions. It also needs information about possible future events. **Forecasts (or projections)** are the business's predictions about the future.

Students sometimes forecast the results they hope to achieve in an assessable task. But just like weather forecasts, what is predicted and what actually happens may be quite different! Nevertheless, forecasts are needed to enable effective planning. An owner may need to forecast the availability of labour, raw materials, finance and building requirements. For this task, business owners rely on internal and external information sources.

One very useful set of data is the forecast for total revenue and total cost.

12.6.1 Total revenue and total cost

When trying to determine whether a business will be financially successful, a SME owner can attempt to forecast the amount of money the business may receive as sales — its total revenue, and how much it has to pay for business expenses — its total costs.

BizWORD

Total revenue (TR) *is the total amount received from the sales of a good or service.*

Total revenue

Total revenue (TR) is the total amount received from the sales of a good or service and is calculated by multiplying the selling price (P) by the quantity (Q) of units sold. This can be represented mathematically as:

$$P \times Q = TR$$

It is possible to forecast total revenue by estimating how many units are expected to be sold. For example, if the price of each unit is $100 and 25 are expected to be sold, then the total revenue forecast will be $2500.

Estimates of future sales are determined by the demand for the business's good or service and the amount of competition in the marketplace. Sales forecasting data:

- can be gathered by using market research techniques such as customer surveys
- are more precise if the business has some previous sales history to act as a guide.

Total cost

The costs involved in operating a business can be broadly classified as either fixed or variable costs. **Fixed costs (FC)** are costs that do not vary regardless of how many units of a good or service are produced. **Variable costs (VC)** are costs that depend on the number of goods or services produced. Variable cost, therefore, will increase if more goods and services are produced and decrease when fewer goods and services are produced (see the BizFact in section 12.6.2).

The **total cost (TC)** of producing a certain number of goods or services is the sum of the fixed costs (FC) and variable costs (VC) for those units. This can be represented mathematically as:

$$FC + VC = TC$$

It is possible to forecast total cost by estimating the change in variable costs at different levels of production. Fixed cost, of course, will remain the same.

The forecast of total revenue and total cost make it possible to use the very useful forecasting technique referred to as the break-even analysis.

BizWORD

Fixed costs (FC) *are costs that do not vary regardless of how many units of a good or service are produced.*

Variable costs (VC) *are costs that depend on the number of goods or services produced.*

The **total cost (TC)** *of producing a certain number of goods or services is the sum of the fixed and variable costs for those units.*

12.6.2 Break-even analysis

Break-even analysis determines the level of sales (total revenue) that needs to be generated to cover the total cost of production (see figure 12.17). Total cost of production includes fixed costs (costs that do not change regardless of how much is sold) and variable costs (costs that depend on the amount of sales — for example, materials). Sales above the break-even point will mean a profit; sales below the break-even point will mean a loss.

BizWORD

Break-even analysis *is used to determine the level of sales that needs to be generated to cover the total cost of production.*

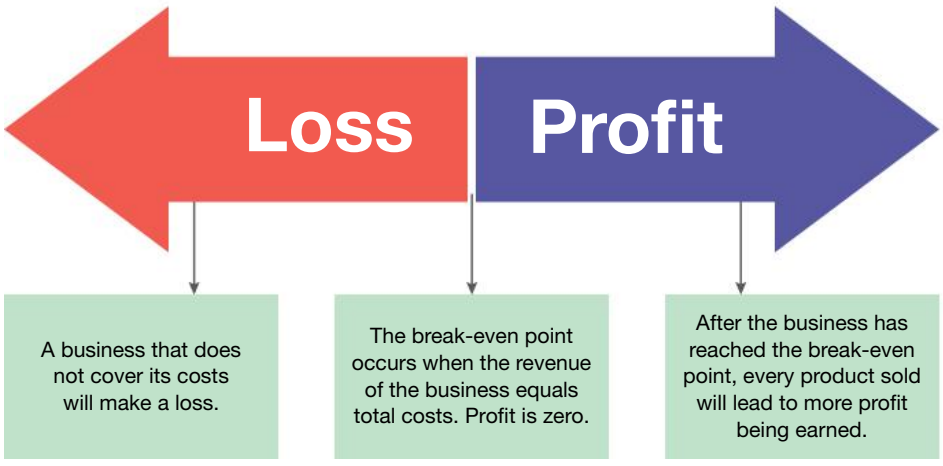


FIGURE 12.16 A break-even analysis is used to determine the number of items that need to be sold to break even — that is, to cover all costs without making either a profit or a loss.

Break-even analysis is an important planning tool because management can determine the level of sales required to obtain a profit. It can also be used to determine the effect on profit if sales increase or decrease. This planning tool is used in the strategic planning stage, before budgets are prepared.

The break-even sales quantity can also be calculated by using the formula:

$$\text{Quantity (Q)} = \frac{\text{Total fixed costs}}{\text{Unit price} - \text{Variable costs per unit}}$$

Example: Break-even quantity

Better Rackets produces different lines of tennis goods, including racquets, tennis balls and tennis bags. It plans to introduce a new style of tennis racquet and estimates that the new racquet should be priced at $200. Fixed costs are $600 000 and variable costs are $80 per racquet. The number of units that need to be produced to break even is:

$$\begin{aligned} Q &= \frac{600\,000}{200 - 80} \\ &= \frac{600\,000}{120} \\ &= 5000 \text{ units} \end{aligned}$$

Break-even is the point where sales equal costs (fixed and variable); that is, where at this point neither a profit nor a loss is made. In this case, 5000 units will need to be sold to break even.

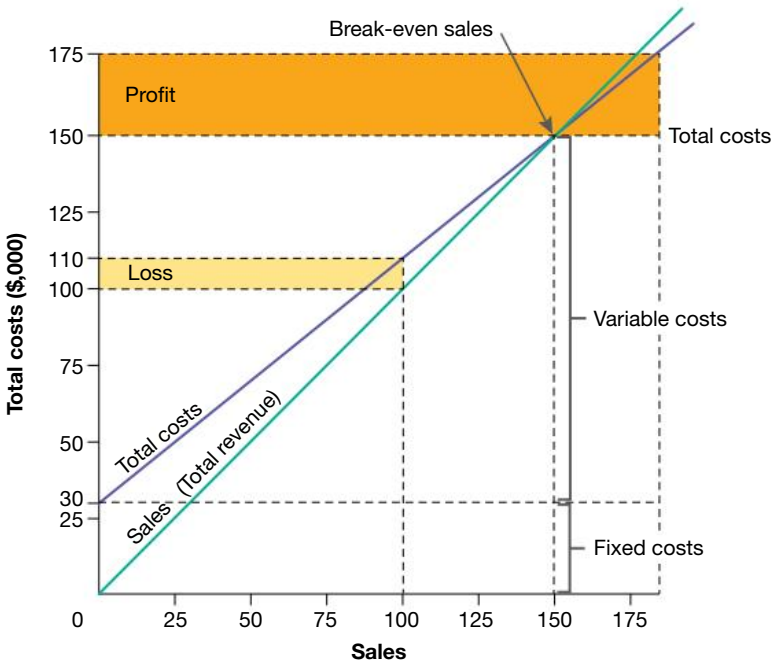
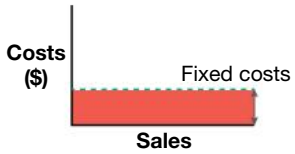


FIGURE 12.17 Break-even analysis. Sales of $100 000 will mean a loss of $10 000 because total costs at this point are $110 000. The point at which total costs ($150 000) intersect total revenue ($150 000) on the diagram is the break-even point at which neither a profit nor a loss is made. Sales above the break-even point indicate a profit of up to $25 000 ($150 000 to $175 000).

BizFACT

Fixed costs do not change as sales increase or decrease. They include rent, insurance, salaries of management and office staff, rates, depreciation, interest on loans, and office expenses.



Variable costs increase as sales increase or decrease when sales go down. For example, for every $1 of sales, a business has estimated that 25c (or 25 per cent of sales) represents variable costs.



Examples of variable costs are direct labour and materials, commission on sales, delivery, freight, packaging.

Total costs are the sum of the fixed costs and the variable costs.



BizWORD

*The **cash flow projection** shows the changes to the cash position brought about by the operating, investing and financial activities of the business.*

12.6.3 Cash flow projections

The **cash flow projection** shows the changes to the cash position brought about by the operating, investing and financial activities of the business. It provides information concerning the business's expected cash receipts (cash inflows) and cash payments (cash outflows) over an accounting period, usually 12 months.

Cash flow plans consist of a month-by-month projection of the flow of money into the business. Cash transactions recorded include cash sales, the collection of debts and the payments the business expects to make. From the information found in the cash flow projection, the SME owner should be able to estimate the business's bank balance for each month and identify the extent and duration of possible cash shortfalls. A positive cash flow occurs when the amount of money coming into the business is greater than the amount leaving it. Overall, this information will point out periods when business expenses are too high or times when a short-term investment is possible to deal with a cash surplus.

The cash flow projection is an important tool for cash flow management. It offers:

- the SME owner a clear indication of how much capital investment the business idea requires
- a bank loans officer evidence that the business is a good credit risk.

It is important to not confuse a cash flow projection with a cash flow statement. The cash flow statement indicates how cash has flowed into and out of the business in the *past* period of time. The cash flow projection shows the cash that is expected to be made or spent over a period of time into the *future*.

Isabella's Sweets
Cash flow projection for January and February 2018

	January ($) Forecast	February ($) Forecast	January ($) Actual	February ($) Actual
Opening cash balance	25500	28320	25500	28410
Cash inflows				
• Cash sales	6000	6100	6100	6300
• Interest received	20	20	20	20
Total inflow	6020	6120	6120	6320
Cash outflows				
• Loan repayments	450	450	450	450
• Wages	2200	2200	2200	2200
• Electricity		300		280
• Supplies	550	560	560	570
Total outflow	3200	3510	3210	3500
Net flow	2820	2610	2910	2820
Closing cash balance	28320	30930	28410	31230

FIGURE 12.18 Example of a cash flow projection

12.7 Monitoring and evaluating

Drivers constantly monitor and evaluate the road conditions, and make necessary changes to speed and direction as they receive updated information. A business also has to monitor and evaluate its environment and take corrective action — that is, it adjusts its business plan to avoid any problems.

Devising a business plan will not guarantee the achievement of the business's goals. The plan must be constantly monitored and evaluated so the business can make accurate modifications as necessary (see figure 12.19 on the next page).

BizFACT

A cash flow projection is used in the financial plan section of the business plan.

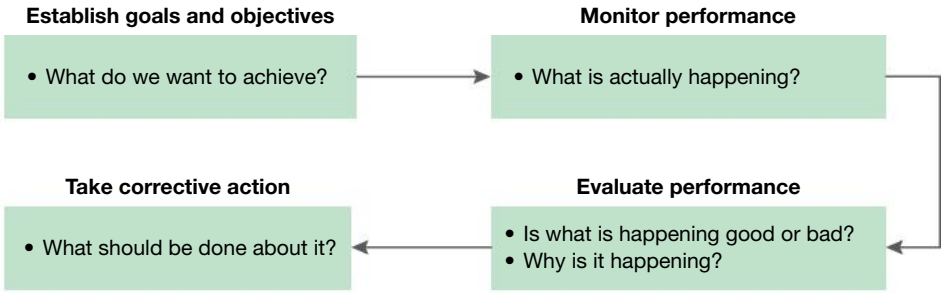


FIGURE 12.19 The monitoring and evaluating process

12.7.1 Monitoring

BizWORD

Monitoring *is the process of measuring actual performance against planned performance.*

Monitoring is the process of measuring actual performance against planned performance. This process involves constantly asking two questions about the business plan:

1. What does the business want to achieve — that is, what are its goals?
2. Are these goals being achieved?

This will indicate the business's true achievements, rather than vague generalisations such as 'things aren't too bad'.

These questions should be asked at every stage of developing the business plan. Such monitoring involves two distinct steps:

1. establishing forecast performance standards
2. comparing actual performance with forecast performance.

BizWORD

A ***performance standard*** *is a forecast level of performance against which actual performance can be compared.*

The first step in the monitoring process requires the business to outline what it wants to accomplish — that is, to establish a performance standard. A **performance standard** is a forecast level of performance against which actual performance can be compared.

A performance standard could be, for example:

- a 5 per cent increase in monthly sales
- a production quota of 1000 units per week.

The second step in the monitoring process is to compare or evaluate actual performance against the performance standard. Budgets, sales statistics and cost analyses can be used to evaluate results. A business owner could compare each individual salesperson's results, for example, with their sales quota. It is only by establishing performance standards and then comparing them with actual performance that a business owner can evaluate the effectiveness of the business plan.

12.7.2 Evaluating

SME owners evaluate their business's performance to determine whether the goals have been achieved. They do this by constantly asking:

- how the business is performing in terms of profit etc.
- whether the business is performing as planned
- whether its performance has improved over time
- how its performance compares to that of similar businesses.

BizWORD

Evaluation *is the process of assessing whether the business has achieved stated goals.*

When a SME owner undertakes this task, he or she is engaged in **evaluation** — that is, the process of assessing whether or not the business has achieved its stated goals.

Once measurements have been collected, the SME owner can compare them with the planned goals. The SME owner needs to ask whether the business operations achieved the desired results and, if not, where and why he or she failed. If the business plan was successful, the SME owner should examine what strategies made it a success and re-use them. By evaluating a successful business plan, the SME owner may also identify weak spots that could be improved and modify the plan to fix them.

The three areas that need constant monitoring and evaluating are sales, budget and profit.

12.7.3 Monitoring and evaluating sales

The number of sales of a product is a measure of the number of goods or services (products) sold. Measuring the number of sales helps a business evaluate its performance, especially its marketing strategies.

Usually, a business will be satisfied with its performance when the number of sales increases over a period of time, even if it means lower profits in the short term due to higher marketing costs. The assumption is that such a strategy will lead to higher profits in the long term.

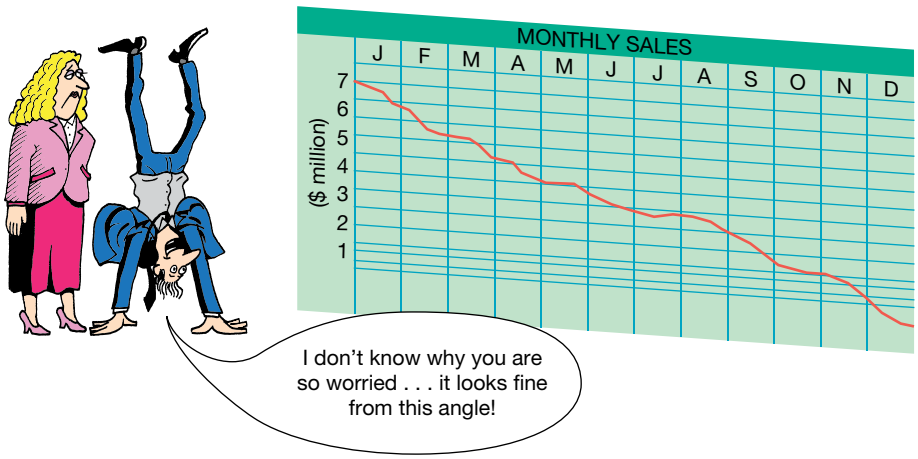


FIGURE 12.20 Sales records indicate whether the business is achieving its objectives.

Sales generate revenue for the business, so it is important that the sales management control function be regularly performed. Sales management control involves comparing budgeted sales against actual sales, and making changes where necessary. For example, if a new selling technique is introduced, the level of sales will need to be closely monitored to determine whether actual sales are above or below what was forecast. The new selling technique will be deemed a success if the sales are above what was forecast. If the figures are below what was forecast, the business will need to take some type of corrective action.

Sales for DeltraWear Fashions Pty Ltd — 2nd quarter

Sales territory	Forecast sales $	Actual sales $	Difference* $	% change^ (– decrease + increase)
1	25 000	29 000	4 000	+16.0
2	40 000	42 500	2 500	+6.3
3	35 000	33 500	–1 500	–4.3
4	32 500	36 000	3 500	+10.8
5	22 500	25 000	2 500	+11.1
Total sales revenue	155 000	166 000	11 000	+7.1

*Difference = Actual sales – Forecast sales

$$\text{\%change} = \frac{\text{Difference}}{\text{Forecast sales}} \times 100$$

FIGURE 12.21 Second quarter sales for DeltraWear Fashions Pty Ltd

Consider the sales figures for April, May and June — the second quarter of the year — for DeltraWear Fashions Pty Ltd (see figure 12.21). The figures reveal that total sales revenue increased by $11 000 or 7.1 per cent above what was forecast.

DeltraWear would be pleased with this result. There would be some concern about the result in sales territory 3, which would require further investigation. However, all the other territories performed above expectations. This tells the business that the new selling technique is a success and should be continued.

12.7.4 Monitoring and evaluating budgets

SNAPSHOT



'The difference between those that become great and the ones that remain small is proper planning and budgeting.'

The importance of budgeting for SMEs

Running a business is not an easy task. So planning in advance is not just recommended, it's a requirement for success. Alongside a strong business plan, an accurate and thought-out budget can be one of the most powerful tools a business has at its disposal when looking towards the future.

Not only can a well-made budget help you make important decisions, but it can also provide useful insights about whether a business is moving towards achieving its goals and objectives, in addition to being a useful way of monitoring performance during the year. A budget is also important because it assists a business to limit expenditures, create a financial road map, secure loans, bring on board new partners and attract investors.

Despite the important role a budget can potentially play in maintaining a business's long-term health, many small and medium enterprises (SMEs) still fail to create and fully utilise a budget. Indeed, the majority of entrepreneurs establish their enterprises with a business plan that lacks a budget. Even for the business plan, few adhere to the script.

The fact that many businesses operate without a business plan or a budget means that decisions regarding expenses are made based on the business that walks through the door. In some cases, this works. However, the mistake that many make is that they don't jump the gap when the money starts coming. When the money comes, no matter how small, a smart business leader will jump the gap from being a one-man band that outsources everything to being a larger business that would attract potential investors.

This does not begin until the business begins to follow a budget. Investors will rarely invest on a one-man show business. They want to see detailed records of audited accounts, tax returns, profits, expenditures etc. Most business owners do not know where to start, and that is why they have remained a one-man show business. The reason for business is money and the reason for money is business. The beginning point is the management of money. The first step to money management in business is budgeting.

It is for this reason that SMEs must budget and be accountable, even when they are making losses and have not broken even. The desire in the heart of a small-sized business leader to be great must be fuelled by accountability and proper management of resources, no matter how small the resources are. The budget should, at a minimum, cover a 12-month period. The business leader then uses the budget as a weapon to seek more funds from potential investors.

A small business leader should have a financial management accountant develop for his business a detailed budget model into which he could input figures, such as staff numbers, sales targets and net profit, so that he can monitor the growth of the business. He should also invest in accounting software that he can use to compare actual performance of the business with projected performance. It is also important for the business to audit invoices, to compare what suppliers are charging and what is actually delivered.

A budget is often referred to as a plan for money, but one can use budgeting in many other areas such as staff budgeting. David Hooton, Managing Director of Telco Platform Network, contends that 'when it comes to budgeting, the key thing is tracking a history of the business's expenses. It is also important to budget for human time and make provisions for contingencies'.

Budgeting is not putting together a wish list of ambitions for future goals. You need to drill to the key drivers in the business, work out how many leads you need to produce a sale and make sure it is realistic. Review the historical data when putting together a budget for your business.

Great leaders are the ones who have a plan in place for the growth of the business. They also make sure that a budget is in that plan. One does not grow big to manage his resources well, instead he manages his resources well so that he can grow big. SMEs that have not been managing and budgeting for their resources should begin budgeting and following the budget. It is the only way for growth in any business.

Once you have a budget you must then begin to review it on a regular basis. Begin to produce monthly reports according to that budget. This would require you to review the budget for your department and report to your manager or the board. For many of us in smaller businesses, we are the board so the concept of writing a report to yourself is a little meaningless. Nevertheless, you should at least review the budget at the conclusion of each month to determine the following:

- Did you meet your revenue goals?
- How is revenue tracking against budget for the year?
- Are expenses in line with your forecast?
- What are the variances and what action can you take now?

A little time spent reviewing the budget at least monthly will ensure that you don't have any nasty surprises down the track. Whatever you do, don't put that budget in a virtual bottom drawer.

One of the most essential figures that you should know is your breaking-even point. This is the point where you start making a profit; or, put another way, the goal you need to reach to stop making a loss. This is really easy to work out if you have a budget. It's the point where revenue is equal to expenses. There is no profit or loss and you have 'broken even'. We cannot overstate the importance of knowing this number. Some businesses break this down to weekly or even daily amounts and it helps keep them focused. If there is one financial metric you should follow in business, this is it.

Lastly, SME leaders should set up management and accountability structures and systems at all levels. This should be done at the planning stages. If you cannot have a five-year strategic plan, then you should at least have a one-year strategic plan and the structures and systems should be drawn according to that plan. Every great business or enterprise begins as a small-sized business. The difference between those that become great and the ones that remain small is proper planning and budgeting.

Source: Office of the NSW Small Business Commissioner

SNAPSHOT QUESTIONS

1. **Outline** the benefits of a budget.
2. **State** some problems businesses can face if they don't have a budget.
3. **Describe** what business owners should do with their budgets once they've created them.
4. **Identify** one of the most essential figures a business owner should know.

No business should commence operating without having prepared a budget. A **budget** is the business's financial plan for the future. It outlines how the business will use its resources to meet its goals. The budget contains projections of incomes and expenses over a set period of time.

Budgets enable constant monitoring of goals and whether they are being achieved. Budgets assist in emphasising the goals of the business and provide a basis for administrative control, direction of sales effort, production planning,

BizWORD

*A **budget** is the business's financial plan for the future.*

control of stocks, price setting, financial requirements, control of expenses and production cost control.

Budgets are used in both the planning and the monitoring aspects of a business; for example, the business owner can measure planned performance against actual performance and take corrective action as needed.

BizFACT

Despite all the benefits of budgets, a large proportion of Australian SMEs don't use formal budgets in their business planning. The main reasons for this are time and expertise. Many SME owners don't know where to start, don't know how to forecast accurately or just can't find the time away from the business to do it.

A budget is an important part of the planning process. Its preparation must account for various factors, such as:

- a review of past figures and trends, and estimates gathered from relevant departments in the business
- potential markets or market share, and trends and seasonal fluctuations in the market
- proposed expansion or discontinuation of projects
- proposals to alter price or quality of products
- current orders and plant capacity
- considerations from the external environment (for example, financial trends from the external environment, availability of materials and labour).

The budget should be regularly compared with actual revenue and expense amounts to detect any discrepancies. For example, once the owner has determined the goals, they can then estimate the business's various costs and its revenue. A profit budget will establish the viability of the business by predicting how much profit is likely to be made from the expected sales. These figures are estimates, but the budget must be realistic. Figure 12.22 illustrates the information that should be included in a profit budget.

Profit budget for 12 months ending …

Sales

Less cost of goods sold
Opening stock
Purchases
Closing stock

Gross profit (Sales – COGS)

Less expenses
Advertising
Insurance
Wages
Rates
Electricity
Water

Net profit (Gross profit – total expenses)

FIGURE 12.22 Example of a profit budget

Once the budget has been completed, the business owner can determine the extent and timing of financial requirements. This profit budget should then be reviewed at least once per month, and the owner should compare the projected amounts and the actual amounts. Modifications must be implemented if there are any discrepancies.

Working to a budget — the school dance

You have been appointed manager of a student group that operates the annual Year 11 school dance as a part of the Business Studies curriculum. This is a major event in the school calendar and your principal has stipulated that the school expected you to deliver a profit of $500. This will be donated to a charity of the students' choice. The school also wants its own costs covered from the evening. The key points to consider are:

- Between 300 and 400 people are expected, depending on the success of your promotion to other schools. Art students at your school will be designing and then distributing posters.
- The event is in the school hall.
- You are expected to provide food, drink, security and music.
- The costs for last year's dance are:
  - **School costs**. Printing of posters, plus electricity, water and gas on the night — $100
  - **DJ Snoopy spins**. Music and light show — $900 for 4 hours
  - **Decorations**. Supplied by local company Party Guys & Sons — $300
  - **Finger food and drink**. Party pies and soft drink — $500
  - **Security**. Two security guards from Crusher Securities — $400 for 4 hours.

SNAPSHOT QUESTIONS

1. **Calculate** last year's costs for the school dance to work out its break-even point (they charged $10 per ticket).
2. (a) As manager of the school dance, **identify** what type of market you are seeking to target.
   (b) **Predict** what might happen if ticket prices and promotional material are not 'positioned' for this market.
3. Working in small groups, **discuss** ways in which you could reduce your costs for the school dance. For example, you might consider offering your suppliers (of catering, security, DJ and decorating services) the chance to promote their businesses on the night in exchange for reduction in their usual charge.
4. As a group, **construct** a cash budget for the dance. You must also explain your price structure in terms of the agreed cost of tickets.
5. You sell 380 tickets at $15 each.
   - The finger food and drink expense increased by $63, but you needed only one security guard.
   - You had to pay insurance of $689 at the last minute.

   All prices include GST. **Calculate** the profit or loss you made for this event. Remember to reduce all amounts by one-eleventh to remove the GST component.

SNAPSHOT



12.7.5 Monitoring and evaluating profit

As the following 2017 headlines suggest, profit is at the centre of a business's activities and one of the most intensely watched financial indicators.

Flight Centre shares soar after company lifts profit outlook.
ANZ Bank cuts thousands of jobs on road to $3.4 billion profit.
Natural disasters take $767m bite out of QBE profits.
Virgin Australia records $185 million loss but stops burning through cash.
Qantas delivers second-highest profit ever.

In a sense, a business's profit levels can be compared to a student's subject grades: they are an indication of performance. Such feedback is crucial to evaluate whether or not specific goals have been achieved and what, if any, changes need to be implemented.

There are five main reasons why a business's profit levels must be carefully monitored and evaluated.

1. *Profit as reward.* As outlined in chapter 1, profit is what remains after all business expenses have been deducted from the business's sales revenue. Profit is regarded as the return, or reward, that business owners receive for taking the risks in operating a business that produces goods and services that consumers want.
2. *Profit maximisation.* In chapter 6, it was explained that one of the main goals of a business is to maximise its profits in the long term.
3. *Profit as a source of finance.* Chapter 11 outlined that one of the most important sources of finance for businesses is profits that have been ploughed back.
4. *Profit as a performance indicator.* The profit level also acts as the main indicator of a business's performance. Changes to the level of profit act as a guide to how well the business is succeeding or failing.
5. *Profit as a dividend payment.* For incorporated businesses a proportion of the profit is allocated to shareholders as dividends.

Evaluating the profit levels will also reveal important information about a business's costs and revenues. These amounts must be accounted for and business owners need to be able to identify their source and quantity. For example, a fall in a business's profit level may be a result of simply a rise in costs or a fall in revenue. Therefore, variations to the profit level act as a 'signal' alerting the business owner to a change in the business's performance.



FIGURE 12.23 Careful monitoring and evaluation by a business of its profits will pay off.

When running a small business, one of the most challenging tasks will be evaluating profitability. Profitability can be evaluated in numerous ways, but a popular method of evaluating profit is to calculate financial ratios. Three financial ratios that will help a business evaluate profit are the net profit ratio, the gross profit ratio and the return on equity ratio. Comparing these ratios to that of competitors and the industry average can help managers evaluate the profitability of their business. (These ratios will be examined in greater detail in the HSC course.)

12.8 Taking corrective action — modification

Students are constantly involved in comparing planned performance with actual performance — for example, planning to score 70 per cent for an assessable task but receiving only 43 per cent. A mismatch between the planned and the actual performances means a student has to take some corrective actions and modify their behaviour: study more for the next assessable task, complete all the homework, drop out of the course or prepare a topic summary.

BizWORD

Modifying *is the process of changing existing plans, using updated information to shape future plans.*

Modifying is the process of changing existing plans, using updated information to shape future plans. Sometimes the planned performance standards are

unrealistic when they are first formulated. At other times, changes to the external environment make the standards unattainable. Whatever the case, the situation cannot continue and the business owner must undertake some corrective action/modification.

Corrective action may involve changes to the materials, products that are the firm's output, the costs of turning raw materials into products, management practices, delivery of products to the market and so on. It may also involve changes to the organisation's human resources, because each individual's performance in the organisation is as important as the finished product.



FIGURE 12.24 Free-to-air commercial television networks have faced increasing competition from pay television and streaming services, which took away some of the networks' market share. As a result, the networks' advertising revenue has fallen. In response, they needed to modify their business practices in relation to their clients: the advertisers. For example, Nine Entertainment partnered with Fairfax Media to provide a new subscription video-on-demand (SVOD) service, StreamCo.

SUMMARY

- Forecasts are the business's predictions about the future.
- Total revenue is the total amount received from the sales of goods or services.
- The total cost of producing a certain number of goods or services is the sum of the fixed and variable costs for those units.
- Break-even analysis determines the level of sales that need to be generated to cover total production costs.
- The cash flow projection shows the changes to the cash position brought about by the operating, investing and financial activities of the business.
- SME owners need to monitor and evaluate the business's performance by asking themselves:
  - Is my business performing as planned?
  - Has the performance of my business improved over time?
  - How does the performance of my business compare to that of similar businesses?
- Budgeted sales should be compared against actual sales.
- The budget should regularly be compared with actual revenue and expense amounts to detect any discrepancies.

- When using indicators, the main types of analysis are:
  - comparing figures within one financial year
  - comparing figures from different financial years.
- Profit levels are an indicator of a business's performance and should be carefully monitored and evaluated.
- Modification is the process of changing existing plans, using updated information to shape future plans.

EXERCISE 12.5 REVISION

1 **Define** the term 'forecasting'.

2 **State** how total revenue and total cost are calculated.

3 **Distinguish** between fixed costs and variable costs.

4 **Identify** three fixed costs and three variable costs your school incurs.

5 **Outline** why the break-even analysis is an important planning tool for businesses.

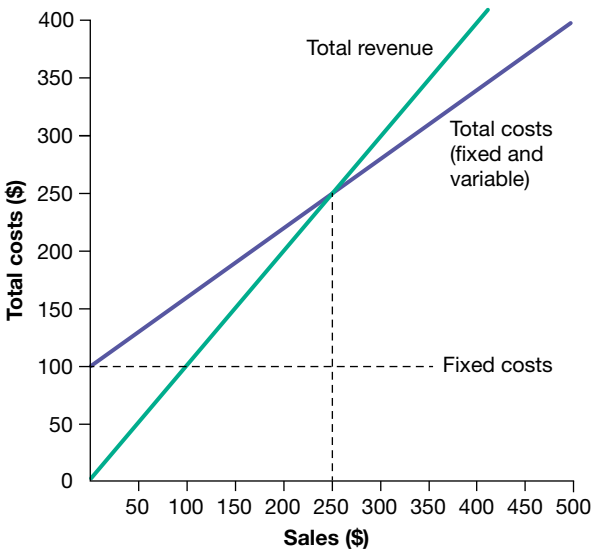
6 **Explain** how a house painter might make use of break-even analysis when providing a quote to a potential customer.

7 (a) **Calculate** the level of break-even sales, given fixed costs of $50 000, variable costs of $11 per unit and a selling price of $16 per unit.

(b) **Calculate** the level of break-even sales, given fixed costs of $600 000, variable costs of $500 per unit and a selling price of $2000 per unit.

(c) From the graph below, **calculate** amounts for (i) to (v).

(i) the amount of fixed costs
(ii) the break-even point
(iii) the loss or profit if sales are $100 000
(iv) the loss or profit if sales are $300 000
(v) the amount of variable costs when sales are $250 000



8 **Why** is a cash flow projection an important tool for cash flow management?

9 **Distinguish** between a cash flow projection and a cash flow statement.

10 Refer to figure 12.18 in section 12.6.3. **Analyse** the cash flow projection for Isabella's Sweets by comparing the forecast cash flow to the actual cash flow.

11 **Distinguish** between monitoring and evaluating. **Discuss** how the two processes are linked.

12 'Any business that fails to monitor its sales will not be able to evaluate the effectiveness of its selling techniques.' **Discuss**.

13 **Identify** the data DeltraWear Fashions Pty Ltd (see section 12.7.3) needed to collect to monitor the new selling technique.

14 A business has a sales potential of $70 000 but achieves actual sales of only $32 000. **Interpret** what this signifies. **Recommend** what the business should do next.

15 You have just been appointed sales manager for Digital@Work Software. One of your first tasks is to conduct a sales management control using the following sales figures:

Sales for Digital@Work — 1st quarter				
Sales territory	**Forecast sales $**	**Actual sales $**	**Difference $**	**% change (– decrease + increase)**
1	29 000	35 000	_____	_____
2	54 000	58 000	_____	_____
3	32 000	36 000	_____	_____
4	37 000	33 000	_____	_____
5	44 000	52 000	_____	_____
Total sales revenue	_____	_____	_____	_____

(a) Complete the table.
(b) **Examine** the forecast and actual sales. **Analyse** what these figures indicate.
(c) **Recommend** whether you would continue with the selling technique. **Explain** your reasons.

16 **Examine** the following market share results for Crystal Water:

Year	Sales revenue ($ million)	Market share (%)
2007	28	18
2008	25	18
2009	33	14

(a) **Explain** how it is possible for sales revenue to decrease but market share to remain the same.
(b) If you were the owner of Crystal Water, **identify** which year's result you would find most pleasing. Give a reason for your answer.

17 'No business should operate without monitoring and evaluating its profit levels.' **Discuss**.

18 **Explain** why the budget should be regularly compared with actual revenue and expense amounts.

19 A business's profits have been declining over the past two years. **Recommend** two modifications the business could take to correct the situation. **Justify** your answer.

EXERCISE 12.5 EXTENSION

1 CCD Enterprises has been very successful producing and selling a range of sporting goods in the Australian market. It has decided that there is potential in the Asian market. **Describe** two planning tools that the company may have used in deciding to expand into the overseas market.

2 'The more accurate the predictions, the better the chances the business has of surviving.' **Evaluate** this statement.

3 Read this case study, then answer the questions that follow.

Anna and Bill are technicians working in a relatively small electronics factory. They are trained and competent tradespeople, and live and work for new developments in the electronics field. At home, both have accumulated journals and papers on what's new in the electronics field. They met by coincidence on an overseas trip and their mutual interests brought them together, eventually to work with the same company. Before joining the company, Bill worked with the government and Anna was in a sales position for a retail firm. This was a position that really came about by accident through personal contacts by her family. The sales position held no real interest and this led to a change in employment.

For some time they have been thinking about an idea that would mean leaving the company and setting up their own business. There are a number of electronic components currently imported from overseas that they believe they could manufacture locally for a reasonable price and perhaps launch into the export arena.

They have both talked with their spouses, immediate families and a number of friends about the possibility of branching out on their own. Together they believe they would have some $60 000 available through equity capital and loans. The amount of money required to establish a factory and various outlets is unknown at this stage, but they are assuming that individual funds would be available from banks or other sources.

(a) **Identify** what other personal factors Anna and Bill should consider before making the final decision.
(b) **Investigate** what factors may be important in the preparation of their business plan.
(c) If you were in their position, **determine** how you would go about analysing market prospects.

4 (a) **Determine** what is the most important aspect of preparing a business plan.
(b) **Explain** why a financial institution would require a business plan before approving a loan to the business.
(c) **Explain** why a business plan should be flexible and constantly revised.

5 **Recall** a situation in which you evaluated your performance. An example could be an assessment task, a part-time job or sports event.
(a) **Identify** your goal for this activity.
(b) **Assess** whether you achieved your goal. Give reasons for your answer.
(c) **Analyse** what corrective action, if any, you were required to take.

on Resources

Digital doc: Chapter summary (doc-26104)
Interactivity: Chapter crossword (int-7233)
Interactivity: Multiple choice quiz (int-7234)

CHAPTER 13

Critical issues in business success and failure

OVERVIEW

13.1 Introduction
13.2 Importance of a business plan
13.3 Management — staffing and teams
13.4 Trend analysis
13.5 Identifying and sustaining competitive advantage
13.6 Avoiding overextension of financing and other resources
13.7 Using technology
13.8 Economic conditions

13.1 Introduction

When a business commences operation, the SME owner/manager is optimistic of success. Most businesspeople are aware of the general pitfalls, but all businesses — regardless of their size or function — must pay close attention to a number of critical issues. These issues include:

- having a business plan
- managing employees
- analysing trends
- identifying and sustaining competitive advantage
- avoiding overextension of financing and other resources
- using technology
- considering economic conditions.

While there are many reasons for business failure (see chapter 4), careful attention to the above factors will allow businesses to avoid failure and achieve success. These critical issues form the basis for discussion in this chapter.

Resources

eLesson: Global Kidz Oz 2 (eles-2297)

13.2 Importance of a business plan

The vital point of the previous chapter was that all business owners must take time to develop a business plan. Chapter 12 also introduced you to the planning process and the activities to be undertaken to prepare the business plan. No two business plans will be identical but they should all contain some common information. Some plans will be structured and detailed; others will be less complex and more informal. However, regardless of its format, a plan must contain reliable and accurate information in enough detail to be valid.

The business plan should contain:

1. a clear, concise statement of the goals of the business — what the business wants to achieve
2. well-developed plans for achieving these goals — how the business is going to achieve the goals

3. reliable control standards for measuring performance — has the business achieved the goals; if not, what needs to be changed?

A comprehensive plan is essential for business success.

As outlined in chapter 12, the business plan is the 'blueprint' for future growth and development within a business. It sets out the desired goals and direction of the business. It is widely accepted that a business plan is essential to long-term success and necessary for all businesses regardless of their size or function. If prospective business owners neglect to develop a business plan or make profit projections, business failure is distinctly possible because there is no clear understanding of the business's future.

Lack of planning can be as disastrous as a lack of capital. In all businesses, the best results come from effective management. This means that the manager uses the business plan and, more importantly, adjusts the plan when changes occur.



FIGURE 13.1 An effective business plan contains a number of important elements that will make the plan an operating tool that assists in the management of the business.

13.2.1 Business plan: presentation and preparation

All business plans should be presented in a professional manner, because they may be read by bank managers, accountants, financial advisers, company directors, potential purchasers or interested partners. These people often have first contact with the details of the business via the business plan, so it is important that the plan reflects the skills and abilities of the business owner. A poorly presented plan will convey the impression that little thought has been given to the planning process. This will reflect poorly on the business owner and their capabilities of getting the business 'up and running'. Sometimes it is a good idea to get professional help from an accountant, business adviser, solicitor or marketing consultant, particularly with plan elements such as the projected profit and loss statements, break-even analysis and market research.

BizFACT

Accuracy and realistic expectations are crucial to an effective business plan. It is unethical to deceive investors and financiers, and it is unwise to deceive oneself.

Preparing a business plan is similar to completing an assessable task. The final result will reflect the amount of time, effort and research that goes into the plan and its final presentation. Any task that is completed quickly and at the last minute will probably lead to poor performance. But businesspeople who use the planning process effectively will end up with a valuable working document that will help guarantee a business's success.

13.3 Management — staffing and teams

As outlined in chapter 5, management can be traditionally described as being concerned with coordinating a business's resources to achieve its goals. More contemporary descriptions highlight that management is the process of working with and through other people to achieve the goals of the business in a rapidly changing environment. What both these explanations have in common is that management:

- must make the best use of limited resources
- is responsible for the business achieving its goals.

Think of a manager's role as being similar to that of a chef whose task is to efficiently combine the resources (ingredients) to effectively achieve a goal (a delicious meal). A skilled, competent chef could probably deliver an appetising meal even with limited resources; whereas an unskilled, incompetent chef would probably serve up an unappealing meal even if he or she had access to superb ingredients. The chef's level of skill (ability) is the critical factor determining how well the goal is achieved.



FIGURE 13.2 Highly skilled employees can provide better service, potentially increasing the business's reputation and revenue.

It is the same for the management of a business. A manager's skill is the most critical factor in determining a business's success or failure. For example, a business may have the most up-to-date computer equipment, well-furnished offices, access to adequate sources of finance, a committed and motivated group of employees, an excellent location, and an outstanding range of goods or services backed up by

a highly-expensive marketing campaign, but if it fails to have a competent manager(s), who can make effective and efficient use of these resources, then the business will not succeed.

Overall, the most important accomplishments a skilful manager will achieve for a business include the ability to:

- solve difficult problems
- set and help attain important goals
- develop attitudes of commitment and ownership
- create a positive business culture through their words and actions
- monitor the business's external and internal environments
- plan and allocate resources
- coordinate teams and departments
- monitor the performance of teams and individuals
- successfully put workplace and business changes into action
- develop and implement schedules and operating plans.

Two important areas of business that a manager must pay special attention to are staffing and teamwork.

13.3.1 Staffing

If a SME owner wants the business to succeed, then it is essential to have employees who are satisfied and motivated (as was outlined in chapters 6 and 8), as they will be more productive. They also provide the business with a competitive advantage, especially if the business offers a service where the customers come into direct contact with the employees. Therefore, the management of the staffing function — the recruiting, selecting, maintaining, training and separating of employees — must be undertaken with care.

BizFACT

'Businesses are made by people. We've proven time and again that you can have a wonderful shop, and put a bloke in there who's no good, and he'll stuff it up. Put a good bloke in, and it just turns around like that.' Gerry Harvey, Chairman of Harvey Norman.

Case study: Filtered Media — going the extra mile for employees

Filtered Media is a content marketing and public relations agency that employs about 30 staff. This Sydney-based SME is going the extra mile — and then some — to make sure their employees know how much they are valued. They have developed a number of human resource policies that demonstrate their commitment to looking after the needs of their employees.

Husband and wife team Heather and Mark Jones, who founded the agency, are firm believers in creating a healthy business culture. For Heather and Mark, creating this culture starts with respect for the individual and gratitude. They are grateful to everyone who joins their company and chooses to spend their working hours with them.

When it comes to end-of-year work celebrations, most businesses take their staff out for dinner. In 2015, Heather and Mark Jones wanted to provide their employees with a memorable experience so they took them to Dreamworld on the Gold Coast for the day.

Heather and Mark also offer their staff two paid 'YOLO' (or 'You Only Live Once') days a year, which employees can use in any way they like: to go to the beach on a sunny day or as a mental health day. They have also embedded mental health care into the culture and policies of the business. The pair recently organised training in mental health first aid for their general manager and initiated 'are you OK?' one-on-one conversations with some employees who didn't seem themselves.

In addition to the two paid 'YOLO' days, Heather and Mark also provide one paid 'Marilyn Day' to celebrate birthdays. This term came about in honour of Marilyn Monroe's famous birthday serenade to US President John F. Kennedy. Under this policy, employees are able to take an extra day of leave one week either side of their birthday.

SNAPSHOT



'… put people before policy.'

Their human resource policies have proven to generate a great return. They have led to an increase in loyalty, productivity and retention rates. This can be demonstrated by the fact that in the first four years that the company was officially incorporated, they didn't lose one staff member voluntarily.

As a small business that has experienced significant growth, the owners believe it is important for them to embed this commitment to valuing staff into their policies. Their advice to other small business owners is to 'live generously, both personally and professionally and to put people before policy'.

SNAPSHOT QUESTIONS

1. **Outline** some of Filtered Media's human resource policies.
2. **Assess** the impact Heather and Mark's approach to human resource management would have on staff and on the business.

BizWORD

Recruitment *refers to the process of finding and attracting the right quantity and quality of staff to apply for a job vacancy.*

One mistake that some SME owners often make is not providing enough time or financial resources to satisfactorily carry out the **recruitment** process. Making hasty recruitment and selection decisions often ends in misfortune for both the SME owner and the employee. For this reason, many SME owners outsource this function and use an external recruitment agency.

Recruitment

It is time consuming to advertise, screen and interview potential employees. Many businesses use recruitment agencies as a way of decreasing the time involved in searching for a new employee. They pay an agency to interview candidates and recommend a shortlist of potential employees or an employee suitable for the available position. Outsourcing of staff recruitment is becoming popular with small businesses, especially as the skill shortage worsens and owners see the advantage of using an expert to make sure they hire the best people.



FIGURE 13.3 Many SMEs are using recruitment agencies to assist them with their staffing needs. The main reason for this is related to the cost of a poor recruitment decision, which is generally believed to be around two or three times the annual salary of the person recruited. A poor recruitment and selection process leads to increased costs and lower productivity.

Employee skills databases

Once people have been employed, the next important staffing management function is to achieve the right mix and level of employees' skills. This is best accomplished by using a skills audit and skills inventory.

Skills audit

It is important for any business to detail the current skills base of the people involved in the business, as well as identifying any skills needed in the future. A personnel skills audit is used for this purpose. A **skills audit** is a process that establishes the current skills levels of employees and future skills requirements.

BizWORD

*A **skills audit** is a process that establishes the current skills levels of employees and future skills requirements.*

The aim of the audit is to identify:

- the skills that will give the business a competitive advantage
- weaknesses in the skills base which, unless overcome by training or recruitment, will threaten the business's survival.

Figure 13.4 provides an example of a skills audit form. One form should be completed for each employee. Once this information is collected, it can be used to produce a skills inventory — that is, a computerised database containing information on the skills and experiences of all present employees.

Skill		1	2	3	4	5
Management	Manages time effectively					
	Punctual					
	Able to meet deadlines					
Computer	Confident using a Mac					
	Able to use all Microsoft products					
	Able to use all Adobe products					
Communication	Able to communicate effectively with customers					
	Able to communicate with colleagues and management					
	Effective written communication skills					
Teamwork	Contributes well to group tasks					
	Interpersonal skills					
	Able to listen to other perspectives					
Self-motivated	Positive and open-minded					
	Helpful					
	Focused and on task					

1 = Poor **2 = Minimal** **3 = Satisfactory** **4 = Good** **5 = Excellent**

FIGURE 13.4 Skills audit form

Skills inventory

An employee database is an important tool used by business owners for recording personal and work details of their employees. This type of database should be regularly updated as new employees join the business and existing ones leave. One particular type of employee database is the skills inventory. A **skills inventory** is a database containing information on the skills, abilities and qualifications of existing staff. It is used to search for appropriate candidates to fill new positions within the business. For example, a business may be seeking a current employee with a commerce or business-related tertiary qualification, at least 10 years' experience, fluency in Japanese, and with some knowledge of marketing. By accessing the skills inventory, a search can quickly identify employees who match these specifications.

BizWORD

*A **skills inventory** is a database containing information on the skills, abilities and qualifications of existing staff.*

BizFACT

In an attempt to cut costs and make the bank more adaptable to change, ANZ Bank recently overhauled the management structure of their Australian division by adopting 'agile' teams. The approach involved flattening their structure by breaking the current divisions into 18 'tribes', which are each made up of 150 'squads' of about 10 people. Staff from different departments work together, rather than being part of traditional divisions. Each of the 150 teams look more like start-ups than traditional parts of a large-scale bank, as they each have the autonomy and agility to adapt to customer needs very quickly.

13.3.2 Teams

As was outlined in chapter 7, many businesses are starting to realise that a team approach can be a catalyst for superior performance. Teams are replacing individuals as the basic building blocks of businesses of all sizes, especially in those businesses that are adopting flatter organisational structures.

Businesses are learning that teams:

- make more informed and creative decisions
- work without the need for close supervision
- create greater levels of employee cooperation
- provide improved customer service and/or production output.

How teams are managed, therefore, is another critical issue determining business success. However, it can sometimes be difficult for SME owners to have the time or expertise to develop highly functioning teams or improve the communication and efficiency of already established teams. Consequently, many SME owners are seeking professional help from training and coaching businesses. By investing time and money in the development and training of team leaders and team members, the business reaps the rewards of improved productivity (see the following Snapshot).

SNAPSHOT



"… the business is structured into five self-directing teams to better service clients."

Case study: Cumberland Realty Group — productive teamwork

In 2016, Francesca Luccitti established her real estate business, Cumberland Realty Group, which currently operates in three locations — Greystanes, Merrylands and Wentworthville. Francesca became a property investor at a young age and developed a passion for property. So, after 20 years in banking finance, she decided to follow her passion and opened her first real estate office.

Francesca's mission was to be the most trusted, ethical and successful agency throughout the Cumberland Local Government Area. Cumberland Realty Group provides a full suite of sales and rentals, and at the core of the business is a strong focus on customer service. Hence the business is structured into five self-directing teams to better service clients.

- *Residential Sales team*: Each seller has a dedicated, skilled and licenced manager who can give them all the focus required to achieve a maximum price. This manager is supported by a team of people who assist in providing the highest level of service to the client.
- *Commercial Sales team*: This team is a separate division to the residential sales team but offer the same resources, systems and procedures. Although their main focus is on commercial and industrial properties, they work closely with the residential sales team as many of their clients deal in both residential and commercial real estate.
- *Property Management (rental) team*: All landlords are served with a dynamic team devoted to providing the best rental returns, while delivering tailored solutions for their clients.
- *Project Management team*: This team works closely with developers and builders in the marketing and sales of various residential property projects. Under the assistance of the Project Manager, this team's dynamic approach and development expertise helps developers and builders sell their projects. They also provide a valuable service to assist buyers interested in buying off-the-plan.
- *Admin and Marketing team*: This team supports all other teams to ensure they all meet audit requirements, industry regulations and best practice. The successful marketing of homes and projects is also the first step required in the journey to sell or lease a client's property. Such extensive experience in marketing properties ensures the company attracts the right buyers or tenants.

An astute investor in today's market has interest in all types of property. The key advantage of a real estate office that offers this full range of real estate services is that it helps better meet clients' needs and provide the highest level of customer service. While each of these teams possess a unique skill set, they all interact and work closely together in order to provide clients with the best possible advice. This interaction and level of service helps the business achieve a competitive advantage.

Francesca sets clear goals at the beginning of each financial year for each individual, as well as for each team overall. Every employee has a set of annual targets that are reviewed quarterly with Francesca. At these quarterly meetings, strategies are put in place to help each employee reach their targets. Ongoing training is also provided to all staff members to ensure they can provide the highest level of service. In addition to this, each team has regular informal and structured meetings where all members are encouraged to offer recommendations on any improvements, refer clients to each other and share good news stories for the week. Although Francesca provides strong leadership, she does not need to micromanage her staff, as she is confident they have a clear expectation of their duties and the skills to meet their job description.

In order to build successful teams, you need to have a positive culture and provide strong leadership. It's important not to become complacent and think the business is going to run itself. 'Your teams need to know that you are in it with them and you need to show each individual that you care about them personally so that you and the team can achieve the shared goals.' Francesca makes it a priority to show respect and recognition for every individual in her business. She always makes herself available to her staff and focuses on giving her teams the confidence they need to achieve their goals. 'Show you respect your staff and they'll be much more likely to return the sentiment.'

SNAPSHOT QUESTIONS

1. **Outline** the role of each team.
2. **Describe** how Cumberland Realty Group achieves a competitive advantage.
3. **How** does Francesca manage her teams?
4. **Explain** what Francesca believes is key to building successful teams.

13.4 Trend analysis

Examine table 13.1 below. What do you notice about the business's net profit results?

TABLE 13.1 Net profit results for OzTrack Logistics Limited 2015–18

OzTrack Logistics Limited	
Year	**Net profit ($ million)**
2015	62
2016	78
2017	85
2018	90

On a quick inspection, you would say that net profit is increasing over the four years. However, upon closer examination, you will detect that the rate of net profit growth is decreasing; that is, net profit is increasing but at a decreasing rate. This *trend* is best shown by graphing the net profit results (see figure 13.5). As a business owner, such a trend could be cause for alarm because it could mean that future net profit may fall.

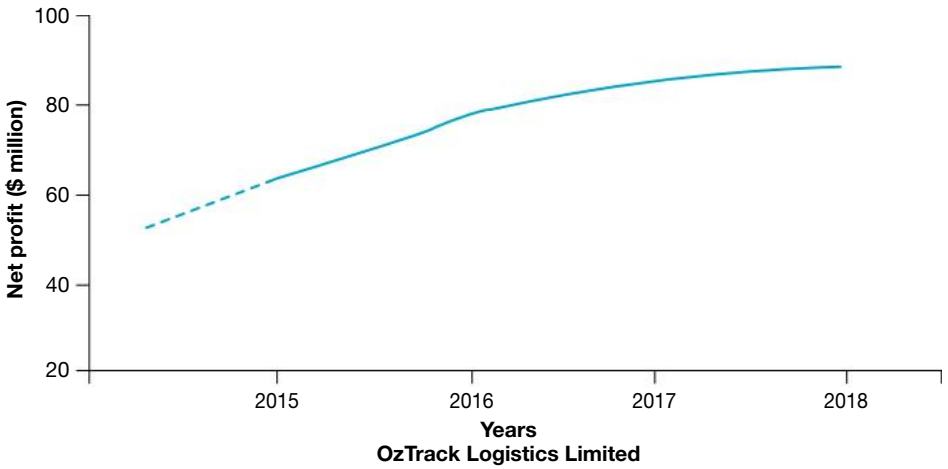


FIGURE 13.5 OzTrack Logistics Limited net profit results 2015–18

BizFACT

Examinations of a business's financial information or total sales are two of the most common applications of trend analysis.

Trend analysis is a process of investigating changes over time and looking for a pattern (trend) in order to predict the future. Trend analysis is based on the idea that what happened in the past provides an idea of what will happen in the future. For example, as a student you probably keep a record of your grades for each assessable task or test. You do this to determine whether your grades are generally rising, falling or stable. Analysing this information also allows you to predict what mark you will receive for a future assessable task or test. You will base your prediction on past performance. The more past grades you have to examine, the more accurate your prediction will be.

Trend analysis is a powerful tool which, when used properly, will assist SME owners to achieve business success by helping forecast such factors as:

- potential sales
- total revenue
- total operating costs
- gross and net profits
- availability of labour.

As was outlined in chapter 12, forecasts are needed to enable effective planning, and trend analysis helps make forecasting more accurate. Overall, trend analysis will provide more reliable information on which a SME owner can base decisions. If, for example, a retailer's trend analysis of past sales forecasts sales to decrease, then appropriate strategies — such as new products or a revamped marketing campaign — can be put in place to avoid the poor performance.

SUMMARY

- Business plans are essential for owners/managers because:
  - they allow the owner to clearly define the goals and future projections (e.g. finance)
  - they assist in the securing of finance from banking institutions or investors
  - they reflect the skills and abilities of the business owner.
- Management:
  - must make the best use of limited resources
  - is responsible for the business achieving its goals.
- A manager's skill is the most critical factor in determining a business's success or failure.
- If a SME owner wants the business to succeed, then it is essential to have employees who are satisfied and motivated as they will be more productive.
- Outsourcing of staff recruitment is becoming popular with SME owners.

- Teams are replacing individuals as the basic building blocks of businesses of all sizes especially in those businesses that are adopting flatter organisational structures.
- How teams are managed is another critical issue determining business success.
- Trend analysis is a process of investigating changes over time and looking for a pattern (trend) in order to predict the future.
- Trend analysis is a powerful tool which assists SME owners achieve business success by helping with forecasts.

EXERCISE 13.1 REVISION

1 **Explain** the purpose of a business plan.
2 **Recall** why a business plan should be professionally presented.
3 **State** what the traditional and contemporary description of management have in common.
4 'To be successful, every business needs skilled managers.' **Discuss**.
5 **Identify** one advantage and one disadvantage of using a private external recruitment agency.
6 **Why** do many businesses outsource their recruitment function?
7 **State** three benefits of working in teams.
8 **Define** the term 'trend analysis'.
9 **How** could you as a student benefit from using a trend analysis?
10 **Examine** figure 13.5 and **explain** why it is easier to identify a trend when using a graph rather than a table of figures.

EXERCISE 13.1 EXTENSION

1 Referring to a business you have studied, answer the following questions.
(a) **Investigate** the planning options that had to be considered when the business was established.
(b) **Examine** what essential components were included in the business plan.
(c) **Determine** how important the business plan was to the overall success of the business.
2 'The output of teamwork is, in many instances, greater than the combined output of its individual members working alone.' **Assess** the accuracy of this statement.
3 'A favourite method of forecasting is to base the estimate entirely on past sales.' **Investigate** the advantages and disadvantages of using this method to predict future sales.

13.5 Identifying and sustaining competitive advantage

Business success and failure is linked (in the long term) to a business's ability to develop a strategy that allows it to gain an advantage over other competitors in its market. A **competitive advantage** can be defined as the strategies used by a business to ensure it has an 'edge' over its competitors. A business cannot always sustain above-average performances in all areas for long periods. For this reason, it must choose a strategy (outlined below) that will allow it to use and develop its strengths as a business. This strategy can give the business a competitive advantage.

BizWORD

Competitive advantage *refers to the strategies used by a business to gain an 'edge' over its competitors.*

13.5.1 Price/cost strategy

The price/cost strategy requires the business to be serious in terms of wanting to be the leader within its industry. The business does not just compete with others, but leads the way by achieving the lowest production costs, which in turn allow

it to reduce the product price. While the price is lower, it is important not to compromise the product's quality in relation to that of competitors' products. Figure 13.6 suggests the main ways in which to develop a cost advantage over competitors.

BizFACT

Labour costs in Australia have grown at twice the pace of other OECD countries over the past decade.

Efficiency of operation refers to the ability of a business to streamline the processes that occur within that business. A manufacturing business, for example, may use more machinery or perhaps specialise parts of the production line (where one operator completes one part of a process, such as placing finished products into boxes while someone else loads the boxes onto the transport).

Low-cost labour is an obvious way to gain a cost advantage over the competition. In Australia, labour is one of the most expensive components of the production process because minimum wages are set by the government. The union movement has fought for these requirements over the past 100 years. They include minimum wages and working conditions, as well as holiday and sick leave entitlements (as outlined in chapter 8).

Economies of scale can achieve a cost advantage for the firm. Simply, this concept relates to the level of outputs for a business and the cost of the inputs (for example, the cost of labour or raw material). To achieve economies of scale, the business tries to reduce the cost of inputs — perhaps by using more machinery, buying in bulk or increasing the specialisation of labour — and increase the level of outputs.



FIGURE 13.6 How to develop a cost advantage over your competitors

Many businesses attempt to reduce the cost of labour by decreasing the size of their workforce and using machinery where possible. Other companies choose to move their operations to countries where labour costs are low. Some countries, such as China, require employers to pay only small wages, so a firm in a labour-intensive industry (such as the clothing and textiles industry) may choose to relocate this part of its operations overseas.

The final way to develop a cost advantage over the competition is to use technology. Nearly all businesses today have found that technology — whether computerisation or the use of automation and robotics — has enabled them to improve efficiency and production. As a result, a business can reduce its overall costs. This is obvious in the car manufacturing industry where computers and machinery have gradually replaced labour.

The changes are more subtle, however, in a service industry: they may include, for instance, the computerisation of client information, or the use of advanced communication mediums such as the internet or email.

13.5.2 Differentiation strategy

The concept behind this strategy is to offer customers something that is not already offered by business rivals. SMEs will find it very difficult to compete on cost due to the large budgets of bigger companies, as well as the economies of scale that can be achieved. They can, however, adopt a differentiation strategy and compete on other factors, such as value, quality, brand image, service and flexibility.

BizFACT

As competition for the entertainment dollar has intensified, Palace Cinemas opened a new $10 million complex in Broadway to position themselves as an upmarket night entertainment venue. Before and after a movie, patrons can go to a craft beer hall, a champagne bar or a wine wall. Inside, there is a call button so that a waiter can collect an order written on a slip of paper and deliver high quality food without a word being spoken. For Palace, it's become less about differentiating on film and more about the experience provided.

Case study: Ajunjo — differentiation

After over 18 years working in IT, business development and sales, implementation, customer service and consulting, Tiz Porreca decided to take a risk and start her own business in 2012 to leverage her strengths and follow her passion. Ajunjo (from the Italian word '*aggiungo*', which means to join or bring together) started out as a business that managed and coordinated events with the unique selling proposition focus on delivering real return on investment to businesses.

A huge challenge Tiz faced in the establishment phase was being referred to as an 'event planner. This caused blocks where companies did not want external event management services and preferred to do the work themselves. Potential clients did not understand the benefits of Ajunjo's true value proposition and it became very apparent that they were misinformed about the services provided. Tiz realised that her message did not focus enough on consulting and, more specifically, about how the business works with organisations at a higher level, educating them about not just running 'events' but creating engagement and real interaction, and strengthening relationships. The focus for Ajunjo is now on consulting in the area of stakeholder management; working with organisations strategically and assisting them to foster better relationships with all their stakeholders. Her strong leadership ability and interpersonal skills make Tiz perfect for this role and enable her to provide the best service and value to her clients.

This improved focus helped with cash flow management. Doing one-off events was unpredictable and there were many times of the year, such as late December to February, where she would often experience a shortage of cash flow. By consulting, Tiz contracts herself out for a minimum of six months, using a retainer model of 'monthly consulting fees'. This enables her to achieve a more consistent cash flow and gives her enough time to better understand the needs of her clients and really work with them to achieve their strategic objectives over a longer period of time.

While Tiz now focuses on consulting, to add to the retainer model, Ajunjo still does provide a full-service delivery arm of event management and logistics. If clients require these, Tiz contracts some tasks out to a team of people who can provide these services under her leadership. The use of outsourcing has helped to address the pitfall of many small businesses in which task delegation usually falls entirely on the business owner. They find themselves 'wearing all the hats' in the business, which is a misappropriation of time, skills and money. Tiz now focuses on finding new business and consulting, which is a better way for her to spend and bill out her time. The admin, event planning and logistics are outsourced and handled at a lower rate and done more effectively.

SNAPSHOT



'… a perfect example of a small business able to match the level of service, skills and expertise provided by larger corporations.'

Business networking opportunities have become one of the most important contributing factors to the success of Ajunjo. Tiz is a member of a variety of networking groups across a wide range of business communities. As a member of these groups, she has also held key leadership roles. Two key groups she is heavily involved with are SHE BUSINESS, which provides business development, mentoring and coaching for female entrepreneurs, and a chapter of BNI called All About Business. Not only do these organisations provide a platform to build relationships with other like-minded business owners, they have had a large impact on Tiz's personal and business development, keeping her focused and competitive.

While most small businesses do not have the personnel or resources offered by large competitors, they continue to flourish. The consulting industry is no exception. Ajunjo is a perfect example of a small business being able to match the level of service, skills and expertise provided by larger corporations. Small businesses like Ajunjo must work even harder to attract and, more importantly, keep clients. Being a small business owner means Tiz has huge 'skin in the game', making her completely dedicated, motivated, goal-oriented and just as professional (if not more) than larger companies. Her performance directly and visibly affects the bottom line; whereas, in larger corporations, consultants may not be as driven since they will still earn a salary, regardless of the level of service provided. Even though Tiz runs a SME, in order to effectively compete with other organisations, she must still demonstrate that Ajunjo comes with a wide range of experience, skills and current industry knowledge. Ajunjo has continued to thrive due to the personalised service that Tiz delivers.

Many of Ajunjo's clients are becoming increasingly aware of the advantages of obtaining services from smaller businesses. A lot of Tiz' success has come about due to her ability to really connect with customers and build strong relationships. Her clients know they are more likely to receive greater attention and personalised service from a small business like Ajunjo that is committed to going the extra mile to retain them as a client, as opposed to a larger corporation where they are more likely to be a mere number on a long list of clients. Going that extra mile means that Ajunjo secures a lot of repeat business. This is made evident by the fact that 100 per cent of Ajunjo's clients come from referrals or repeat business.

As a business owner who is focused on trust and relationships, Tiz makes sure that her clients know they will always be speaking to the same person each time and that the person they speak to will have all the answers. This one-on-one interaction enables her to build that trust, as well as strengthen those relationships. By taking the time to work out exactly what her clients want to achieve and then providing a high level of personalised advice and service, the end result is a physical and emotional connection with her clients, their brand and their corporate goals.

Tiz has been able to sustain a competitive advantage through a blend of both her professional and personal qualities.

SNAPSHOT QUESTIONS

1. **Identify** Tiz's personal qualities that have led to the success of her business.
2. **Explain** the factors that have enabled Ajunjo to create a competitive advantage.

BizFACT

THE ICONIC has become one of Australia's most successful online shopping sites. When launching the business, the founders considered what customers care about when shopping online and came up with ways to exceed their expectations. THE ICONIC offers customers a large range of products at good prices, as well as an easy-to-use website. Through their adoption of smart technology, clever processes and passionate staff, the company is also able to offer three-hour delivery for metropolitan areas. All these factors have given THE ICONIC a competitive advantage.

Many businesses adopt a range of strategies to develop and enhance differences in their product. An example of this strategy is the use of celebrities to endorse and contribute to a product's image, such as Beyonce's association with Pepsi and Justin Bieber's endorsement of Proactiv.

Once a business achieves its product differentiation strategy, the challenge then is to sustain this competitive advantage, especially as competitors attempt to match this strategy.

13.5.3 Ensuring long-term success

Long-term success can be difficult to achieve if a business is unable to develop a competitive advantage. The business may succeed for a short period, but often only because other businesses in the same industry are not striving for any sort of advantage so they all exist at the same level.

Sustaining a competitive advantage is just as important as developing that advantage. Long-term success is assured if a business sustains its competitive edge. The business must be able to resist the actions of competitors who introduce new strategies, while also tracking changes within the industry (especially technological changes).

To limit the advances of competitors, a business must protect itself and reduce opportunities available to the competitors. This may be achieved through:

- research and development, which helps the business develop innovative products
- patents/copyrights, which protect against copying of inventions
- exclusive contracts with suppliers, which mean a supplier gives preference to the business
- lobbying government to limit foreign competition, which aims to restrict imported products.

Most importantly, for a business to sustain a competitive advantage, the actions of management must be dynamic. Staying in front of the competition requires constant action. All businesses operate in a constantly changing environment. The owner/manager must be constantly aware of issues that may affect their operation, market share and profit. If a business is not looking to the future and its impact, then its competitors will be. To sustain a competitive advantage, a manager must be able to predict changes and trends, and act on these predictions.

SUMMARY

- Business success and failure is linked (in the long term) to a business's ability to develop a strategy that allows it to gain a competitive advantage over other competitors in the market.
- A competitive advantage refers to a business's ability to gain an 'edge' over its competitors.
- A competitive advantage is achieved through:
  - *price/cost strategy*. This is best accomplished by achieving the lowest production costs, which in turn allow it to reduce the product price.
  - *differentiation strategy*. The concept behind this strategy is to offer customers something that is not already offered by business rivals.
  - *ensuring long-term success*. This is assured if a business sustains its competitive edge by limiting the advances of competitors.
- A price/cost competitive advantage is best achieved by:
  - efficiency of operation
  - low-labour costs
  - economies of scale
  - technology.
- For a business to sustain a competitive advantage, the actions of management must be dynamic.

EXERCISE 13.2 REVISION

1 **Explain** competitive advantage and how a business can try to achieve it.

2 (a) **Explain** cost advantage.
(b) **Discuss** why it is considered important to a business trying to achieve a competitive advantage.

3 **Outline** the differentiation strategy in terms of achieving a competitive advantage.

4 **Identify** three examples of businesses that may use the differentiation strategy.
5 **Explain** what is meant by a sustainable competitive advantage.
6 **Outline** how a business can limit the advances of its competitors.

EXERCISE 13.2 EXTENSION

'All businesses must be able to achieve a competitive advantage if they wish to succeed.' Assess the accuracy of this statement.

13.6 Avoiding overextension of financing and other resources

Ideally, those financing a business should start small and gradually expand. Unfortunately, some business owners overextend their capacity in the establishment or takeover stage, resulting in excess expenditure that is financed primarily by external sources such as banks. A business can overextend financially by:

- using hire purchase and/or leasing commitments made on:
  - cars
  - equipment
  - office furniture
  - plant and machinery
  - the premises.
- purchasing excess stock
- employing too many staff for the business's current needs.

These types of expenditures are fixed, which means the business has a lease contract that is valid for a certain period (such as one or two years). This can create a higher degree of business risk. If economic conditions weaken, for example, businesses that are highly geared (that is, they have a higher debt-to-equity ratio) come under greater financial pressure and are more susceptible to bankruptcy.

Another expenditure problem can arise if the business owner purchases the business premises. **Leasing** is an effective option, yet many owners decide to buy premises and may find themselves overborrowing. If the business cannot meet its capital and interest repayments, then its working capital will also be affected.

There are many tips for a business of any size and type to avoid overextending financially, including:

- *business planning.* This involves the completion of cash flow projections, preliminary establishment costs, personal financial budgets and financial statements of position, along with the setting of the business's goals and objectives.
- *avoiding an overdependence on debt financing.* This helps avoid problems during weak economic periods when lenders or creditors are unwilling to wait for the business to overcome difficulties.
- *long-term financial planning.* This concerns not just the current financial aspects of the business, but anticipating future problems and planning the business's direction in terms of growth and expansion.
- *a small start.* Many businesses 'walk before they crawl' and quickly find themselves in difficulty. It is important to start slowly and allow the market to determine the right times for expansion and growth.

BizFACT

A study of 600 Australian small businesses by Prushka Fast Debt Recovery in 2017 found that 57 per cent of the businesses surveyed reported having more than $10 000 in outstanding debt.

BizWORD

Leasing *is a long-term source of borrowing for businesses. It involves the payment of money for the use of equipment that is owned by another party.*

13.6.1 Overextension of other resources

Finance is not the only area in which a business can overextend. A business can also overcommit to resources. Resources refer to the inputs necessary for a business to carry out its function. The following two factors have the potential for problems if they are not monitored by management.

Stock

A business that overextends in terms of stock has invested too much money in goods or raw materials. This may occur if the business anticipates customer demand incorrectly, or purchases a 'bargain' from a supplier (such as end-of-season stock) without establishing whether it is saleable among its own customers.

Stock is unrealised sales, and a business with too much stock not only ties up its own cash but potentially loses revenue. Many businesses avoid stockpiling, and prefer to keep only limited supplies and order regularly.

Staff

A business may find itself with too many staff. This may be due to over-optimism about sales levels, or just poor job allocations and hiring. Staff are costly, but options are available for a business to decrease its dependence on this resource and reduce costs in the long term. These options include:

- outsourcing
- redefining current job descriptions
- using more equipment/machinery.

BizFACT

Just-in-time is a method used by some firms to ensure that inventory (stock) is not lying idle. The business has an arrangement with a supplier that orders will be supplied immediately. Thus the business carries little or no inventory and relies on the supplier to fill the orders. Many major companies, including the Coca-Cola bottling plant in Australia, use this practice.

13.7 Using technology

Technology is having many effects on the business world. It is changing the machinery and equipment we work with, and changing the workplace environment. These changes have had a major impact on the internal and external business environments, and the extent and speed of change is likely to continue.

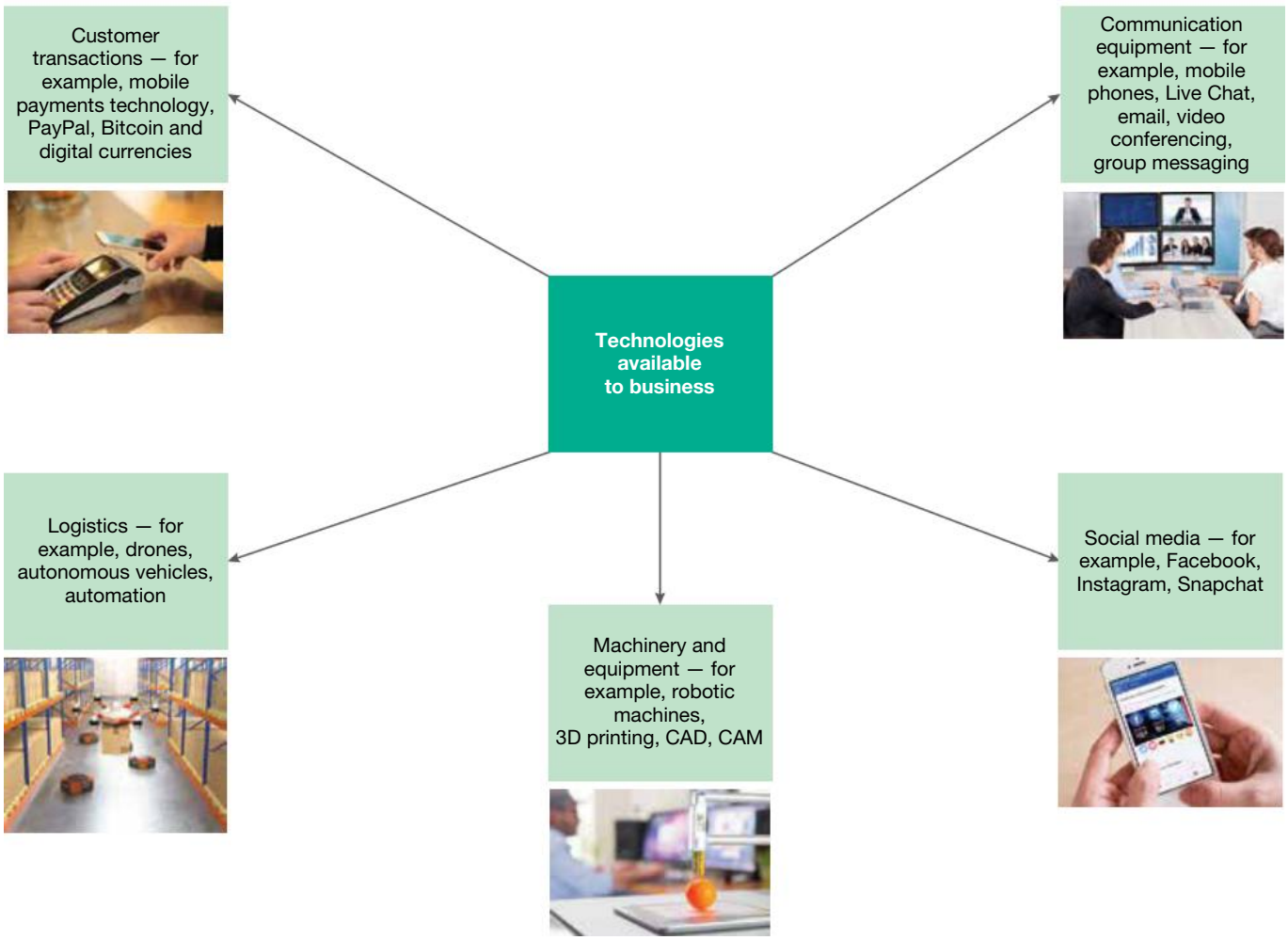


FIGURE 13.7 Examples of the technology available to business

Advances in information technology include:

- iPhones
- Cloud applications
- Skype
- email.

These have reduced communication time delays and improved distance communication between colleagues, suppliers and customers. But not just information technology has advanced: robotics, machinery and equipment for production processes have allowed for faster production times, higher productivity and greater flexibility, which in turn reduce overall costs.

There is little hope for a business that is not prepared to use some forms of technology. Figure 13.7 illustrates some of the technology available for all types of businesses.

13.7.1 Internet applications (e-business and e-commerce)

While most business owners would be aware that taking a business online will increase exposure, about half of SMEs still haven't invested in the benefits of building an online presence.

With over 80 per cent of Australian consumers searching the internet to better inform their purchasing decisions, and over half the online population using their smartphones to access the internet, it is imperative that SMEs acknowledge this growth area and actively develop an online presence.

Figures show that those SMEs that do have an established online presence are able to break through to new market territory. A 2013 survey of Australian SMEs by MYOB found that 46 per cent of online SMEs reported that their website had led to an increase in customer leads and 37 per cent stated that it made their business more competitive. This illustrates that those businesses that do not take advantage of online platforms will be denying themselves great opportunities for growth.

Accessing electronic information services via the internet

BizFACT

The term 'Web 2.0' refers to the transformation of the World Wide Web into a more creative and interactive platform for information sharing, rather than just a means of retrieving information.

One of the main advantages of accessing material electronically is that specific information can be located quickly, 24 hours a day, seven days a week. An internet search is relatively inexpensive and fast. Such a search can also be designed to answer individual requests. These individual requests may include:

- legal requirements for starting a business or changing the formation of a business
- techniques for marketing a good or service
- changes to business administrative requirements, such as taxation changes
- current requirements for industrial relations, such as award conditions
- work health and safety requirements
- support from government agencies, such as Austrade or the Australian Taxation Office.

However, there are some disadvantages, including:

- expense in terms of hardware, software and service provider charges
- slowness to display web pages
- corruption by a virus
- unwanted spam
- information overload.

E-business

BizWORD

E-business *(electronic business) is using the internet to conduct business.*

E-business (electronic business) is using the internet to conduct business. It occurs when a business:

- uses the internet to find information — such as suppliers, prices and product details — and to keep track of delivery schedules

- uses email to communicate with customers and suppliers
- uses the internet to streamline their physical transactions into electronic transactions, e.g. online banking, financial management and stock control
- creates an intranet to manage business activities
- uses the internet to trade goods and services online
- provides online training for their staff
- uses the internet to research market conditions, industry trends and economic forecasts
- uses its website to market its goods and services
- uses the internet to lodge forms or apply for licences via a government department's website.

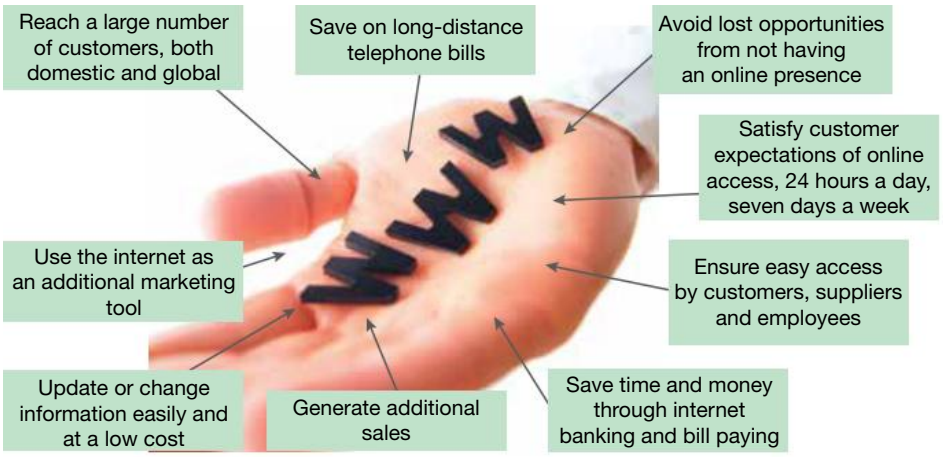


FIGURE 13.8 E-business can bring a range of competitive advantages to the small business owner.

Case study: Furry Godmother — digital technology changing small businesses

Far from the image of dusty roads and old pubs, digital technology is now at the centre of doing business in the Territory.

Richard Flanagan, Google Australia's head of small business marketing, was in Darwin for a nationwide road show organised with the Australian Chamber of Commerce and Industry to encourage local businesses to boost their online presence.

'Pretty much everyone nowadays is using some form of technology to inform decisions they're making about visiting a new business location or finding products or services,' Mr Flanagan said.

'If you don't have that presence online, you're really going to be missing out.'

Mr Flanagan had his own views about what could be holding local businesses back from embracing new technology.

'Business owners are experts in their field and know customers well — but they often aren't experts in the internet or in online advertising,' he said.

However, according to the Google executive, an effective digital strategy does not have to be complex, as long as basic details like contact information are available online.

Mr Flanagan said Google-commissioned research by Pricewaterhouse Coopers (PwC) showed NT businesses stood to gain the most by boosting their online presence, compared with other states and territories.

Darwin business owner Jason Davies sees digital technology as one of the most critical parts of his pet resort business, Furry Godmother.

'For us, we're a trust-based business,' Mr Davies said.

'People want to know their pets are going to be safe and happy and comfortable when they're with us.

SNAPSHOT



'… the business received between 60 and 70 per cent of customers through online sources.'

'Having photos online, having our virtual tour on our website is really handy, so people can come and check out the facility at any time.'

He estimated the business received between 60 and 70 per cent of customers through online sources.

'I don't find that many people are using phone books,' he said.

Mr Davies said while Darwin businesses tended to be less tech-savvy than their counterparts in other parts of Australia, that could change.

'We have the infrastructure, I believe,' he said.

'Certainly a couple of years ago we didn't — but now we have the ability to be just as digital as the rest of the country.

'I think a lot of people are afraid or unsure to get online but once you do get on there, it's definitely beneficial.'

Source: Australian Broadcasting Corporation

SNAPSHOT QUESTIONS

1. **Outline** the reasons Mr Flanagan provides as to what is holding small businesses back from embracing new technology.
2. **State** the percentage of customers Furry Godmother receives through online sources.
3. **Explain** the benefits of digital technology for Furry Godmother.

BizWORD

E-commerce *is the buying and selling of goods and services via the internet.*

BizFACT

A recent study by Sensis found that more than half of Australia's SMEs (54 per cent) are using eCommerce to drive growth. For those using eCommerce, online sales account for 43 per cent of their total sales on average. Also, more than six in 10 (61 per cent) SMEs now have a website and 43 per cent of those are optimised for mobile devices.

E-commerce

The term **e-commerce** (electronic commerce) has a narrower meaning than that of e-business. It refers to the buying and selling of goods and services via the internet — it is a part of e-business. Today consumers expect a business to have an online presence. In response, more Australian small businesses are using the internet to cover all aspects of e-commerce.

Due to the perceived cost and complexity of e-commerce, some small business owners are tentative in their use of it. Apart from having an email facility and a website, they do not make full use of the technology and consequently do not realise its full potential.

13.8 Economic conditions

As outlined in chapter 3, section 3.3, a nation's economy will go through fluctuations; it will experience good times — booms — and downturns — recessions. The economic conditions are an aspect of the external business environment in which the business has no control.

Changes in the economic conditions in the economy have the ability to impact dramatically on a business in regards to success and failure.

BizFACT

The Consumer Sentiment Index is a measure of consumer confidence in Australia. It is based on a survey of over 1200 households. In August 2017, consumer sentiment was 95.5. A result below 100 means there are more pessimistic consumers than optimistic ones. This was the fourth drop in sentiment over the previous five months. This pessimism can be attributed to low wage growth, higher wage costs and concerns about rising interest rates.

13.8.1 Economic conditions that promote business success

When an economy is in a boom, it will most likely mean that consumers are prepared to increase their spending because consumer confidence is high. Consumers are certain their jobs are secure and incomes are expected to increase; they have an optimistic outlook.

In periods of strong economic activity the economy will experience:

- high levels of consumer spending. This will mean businesses have a greater capacity to sell goods and services and therefore profits are maintained and improved. Businesses that sell more luxury type goods and services (such as brand clothing, jewellery and imported cars) will benefit in this type of economic condition because the consumer has a higher level of disposable income.

- falling unemployment. Unemployment is lower as businesses can afford to hire more employees when sales and profits are steady and growing. As well, to meet the increased demand for goods and services, businesses will be required to increase the size of their workforce.
- increased production. Businesses' output will increase to meet buoyant trends that provide opportunities for future increased sales and profit.

13.8.2 Economic conditions that lead to business failure

When an economy is in a downturn, it will most likely mean that consumers are not spending as much. This is because consumer confidence is low. Consumers fear they may lose their job or their wages may not increase. Overall, reduced consumer spending translates to reduced profits for business. This will eventually lead businesses to reducing their production levels.

In periods of weak economic activity the economy will experience:

- lower levels of consumer spending. This will mean businesses have a reduced capacity to sell goods and services and therefore profits will decline. Businesses that sell more necessities and budget-type goods and services (such as groceries and cheaper clothing) will benefit in this type of economic condition. This is because consumers become more cost conscious and will seek out goods and services they consider to be value for money.
- rising unemployment. Unemployment is higher as businesses cannot support current employee numbers when sales and profits are decreasing or negative. As well, cutting back production levels may reduce inventories of goods and services that are potentially unsaleable. Consequently, existing employees may be made redundant.
- decreased production. Businesses' output will decrease in response to the fall in consumer spending. As a result, profits will also decrease.

SUMMARY

- A business can overextend financially by:
  - hire purchase or leasing overcommitments
  - purchasing excess stock
  - employing too many staff for the business's current needs.
- Overextending expenditure can create a high degree of business risk.
- To avoid overextending financially, a business should:
  - undertake thorough planning
  - avoid overdependence on debt financing
  - engage in long-term financial planning
  - grow at a sustainable rate.
- Overextension of stock ties up a business's cash and can lose revenue.
- Overextension of staff results in employing too many staff.
- The integration of technology into the business is essential to succeed in contemporary society.
- E-business (electronic business) is using the internet to conduct business.
- E-commerce (electronic commerce) is the buying and selling of goods and services via the internet.
- A nation's economy will experience periods of boom and recession.
- In periods of strong economic activity, consumer spending, sales of goods and services, production and profits are rising.
- In periods of weak economic activity, consumer spending, sales of goods and services, production and profits are falling.

EXERCISE 13.3 REVISION

1. **Identify** the main ways in which a business can overextend financially.
2. **Outline** how a business can protect against overextending its finances.
3. **Explain** why technology is so crucial in terms of business success and failure.
4. **Distinguish** between e-business and e-commerce. Provide two examples of each.
5. Select and **explain** two advantages and two disadvantages (for a business) of using the internet to access information.
6. **Investigate** the operation of three large e-tailers. Evaluate their sites, reporting on:
   (a) the ease of navigation
   (b) the layout of the home page
   (c) methods of payment
   (d) the ease of product selection
   (e) the return and refund policy.
   The weblinks for **Yahoo! Australia, Amazon** and **THE ICONIC** are provided in the Resources tab, or evaluate other e-tailers of your choice.
7. **Distinguish** between an economic boom and a recession.
8. **Explain** the impact a period of (i) strong and (ii) weak economic growth will have upon most businesses.

on Resources

- **Weblink:** Yahoo! Australia
- **Weblink:** Amazon
- **Weblink:** THE ICONIC

EXERCISE 13.3 EXTENSION

1. **Analyse** the importance of financial planning for short-term and long-term success in business.
2. 'Business expansion should be slow and steady.' **Evaluate**.
3. 'Technology has had a great impact on the internal and external business environment.' **Discuss**.
4. **Determine** the advantages and disadvantages of the dynamic nature of technology in Australian business.
5. **Investigate** one of the following technologies and explain what benefits this technology can bring to businesses:
   - cloud applications
   - mobile payments technology
   - PayPal
   - drones
   - digital currencies
   - video conferencing
   - robotic machines
   - 3D printing.
6. Arrange to interview a small business owner whose business has an online presence. **Investigate**:
   (a) the reasons for going online
   (b) the benefits of a web presence
   (c) the difficulties encountered in setting up the website.
   You may wish to video the interview, then watch and discuss it in class.

on Resources

- **Digital doc:** Chapter summary (doc-26105)
- **Interactivity:** Chapter crossword (int-7235)
- **Interactivity:** Multiple choice quiz (int-7236)

Business planning

MULTIPLE CHOICE QUESTIONS

1. Which of the following characteristics best describes an entrepreneur?
(a) An inventor
(b) A risk taker
(c) An academic
(d) A highly skilled employee

2. What legislation is designed to protect both consumers and businesses?
(a) Fair Work Act
(b) Small Business Act
(c) Consumer Affairs Act
(d) Competition and Consumer Act

3. Which statement is TRUE in relation to equity finance?
(a) Interest is charged.
(b) It doesn't have to be repaid.
(c) It can be acquired at short notice.
(d) You don't lose any ownership control.

4. The variable cost of producing yo-yos is $2 and management suggests that the selling price be $5. The business expects to sell 50 000 yo-yos in the next year. Fixed costs are $30 000. What is the break-even number of units of production of yo-yos required for next year?
(a) 50 000
(b) 10 000
(c) 20 000
(d) 30 000

5. A business has been able to achieve long-term success by having lower costs of production than their competitors.
Which critical issue in business success is this an example of?
(a) Trend analysis
(b) Economic conditions
(c) Avoiding overextension
(d) Sustaining a competitive advantage

6. Which of the following statements is FALSE in relation to a business plan?
(a) A business plan is prepared only when the business is initially established.
(b) A business plan is a statement of goals for the business and the strategies taken to achieve them.
(c) A business plan allows stakeholders to determine the viability and profitability of the business.
(d) Having a business plan is a critical factor determining business success and failure.

7. Which of the following is considered to be an on-cost for a business?
(a) Wages
(b) Superannuation
(c) Staff training costs
(d) Goods and services tax

8. What is an advantage of starting a business from scratch?
(a) Easier to obtain finance
(b) Equipment is available for immediate use
(c) Sales to existing customers will generate instant income
(d) The owner has the freedom to set up the business as they wish

9. The owners of a café have implemented policies to ensure they comply with their local government regulations. Which influence in establishing a SME are they addressing?
   (a) Legal
   (b) Market
   (c) Taxation
   (d) Sources of information
10. Which of the following best describes a vision statement?
   (a) It details the main purpose of the business
   (b) It states what the business aspires to become
   (c) It explains the role of each key business function
   (d) It provides information of the financial stance of the business

SHORT RESPONSE QUESTIONS

1. When establishing a business, the entrepreneur risks capital and personal confidence.
   (a) **Describe** the personal qualities essential to all entrepreneurs. *3 marks*
   (b) **Discuss** entrepreneurship and its importance in terms of the development of new businesses. *6 marks*
2. Referring to a business you have studied, answer the following questions:
   (a) **Identify** the three personal qualities that should be taken into account before establishing a new business. *3 marks*
   (b) **Explain** what considerations are necessary when identifying business opportunities. *6 marks*
   (c) **Determine** how a business can achieve a competitive advantage in terms of its chosen market. *12 marks*
3. (a) **Define** the phrase 'identifying a business opportunity'. *2 marks*
   (b) **Explain** its importance. *4 marks*
   (c) **Determine** what factors need to be considered before the business idea can be developed. *8 marks*
4. (a) **Define** the term 'target market' *2 marks*
   (b) **Demonstrate** why it is essential for a business to identify its target market. *4 marks*
   (c) Once a business has identified its target market, **recommend** three strategies the business can use to achieve a competitive advantage. *6 marks*
5. (a) **Outline** two advantages and two disadvantages of buying an existing business. *4 marks*
   (b) **Explain** how a franchise operates. *4 marks*
   (c) **Examine** the costs and benefits of buying a franchise. *4 marks*
   (d) **Discuss** why franchises have become so popular in recent years. *5 marks*
6. Location is considered crucial in terms of business success.
   (a) **Outline** the main factors that must be considered in terms of choosing a business location. *3 marks*
   (b) **Discuss** the differences in location choice for a manufacturing business and a retail clothing store. *6 marks*
7. 'Government regulations are necessary for the business sector to function efficiently and equitably.'
   (a) **Describe** two of the legal requirements to which businesses must adhere. *4 marks*
   (b) **Discuss** the accuracy of this statement and give reasons for your answer. *5 marks*
8. (a) **Define** the term 'business plan' *2 marks*
   (b) **Explain** the purpose of a business plan. *4 marks*
   (c) **Evaluate** the importance of planning to the overall success of a business. *10 marks*

9. (a) **Outline** what motivates people to start their own business. *2 marks*
(b) **Identify** the personal skills required to successfully operate a small business. *3 marks*

10. (a) **Define** the term 'business concept'. *2 marks*
(b) **Explain** how a prospective business owner might devise a business concept. *4 marks*
(c) **Analyse** the role of innovation and entrepreneurship in the establishment of new businesses. *8 marks*

11. **Identify** the range of support services that small business owners should utilise. *3 marks*

12. (a) **Identify** three advantages that the use of computers can bring to a small business. *3 marks*
(b) **Select** three different examples of business hardware and **explain** the purpose of each. *6 marks*
(c) **Analyse** how the use of information and communication technology can assist a small business owner to make appropriate decisions. *10 marks*

13. (a) **Outline** two business objectives that could be assisted by a business engaging in e-commerce. *2 marks*
(b) **Distinguish** between e-business and e-commerce. *4 marks*
(c) **Recommend** three strategies a small business could implement to increase revenue as a result of engaging in e-commerce *6 marks*

14. (a) **Distinguish** between debt and equity financing. *5 marks*
(b) **Investigate** why funds should be borrowed for as long as it will take the increased profits to repay the loan. *6 marks*

15. Gerry has had an interest in antique and unusual children's toys since he was a child, and has been collecting toys from the 1940s and 1950s for many years. He is interested in setting up a toy shop, incorporating a museum or similar display for his collection. His hope is that the display of antique toys will be a means of attracting customers.
(a) **Identify** the source of inspiration behind Gerry's business concept. *1 mark*
(b) **Outline** how he has sought to differentiate his business from those of possible competitors. *3 marks*
(c) To assist Gerry in making a decision about whether to implement his business idea, **propose** a list of six questions that a market researcher might ask. *6 marks*
(d) **Create** a step-by-step process that Gerry can undertake to determine whether or not there is sufficient demand for the type of business he is proposing. *12 marks*

EXTENDED RESPONSE QUESTIONS

1. Research reveals that women-owned small businesses are good prospects for financial institutions that lend money. Yet women still face discrimination when organising finance and often end up borrowing from family members. **Investigate** why this discrimination still occurs.

2. **Discuss** the key considerations for an entrepreneur in terms of setting up a business. Use examples.

3.

> Phillip and Janice worked in a bank, but had always wanted to run their own business. While on holiday in a small seaside town, they noticed that the local general store and takeaway food shop was up for sale. The business was the only one of its type in the town, but the town is very small and seems to have a reasonably large population only during summer and holiday periods, when the local camping and caravan park, and other holiday accommodation are all full. They are very interested in purchasing the store, but realise they have to make a number of important decisions before committing to making an actual offer on the store.

As a business consultant, prepare a report that could be given to Phillip and Janice. In your report, you should:

(a) **Outline** the main personal qualities needed to successfully operate a small business.

(b) **Create** a list of 10 questions Phillip and Janice should consider before committing to making an actual offer.

4. Referring to a business that you have studied, **determine** three critical issues that will influence the success or failure of the business.
5. 'Competitors can be a threat to a business but they can also ultimately lead to business success.' **Explain** how competition may in fact be good for business.
6. **Investigate** how the following act as the primary influences on an individual's decision to establish a business:
   (i) personal qualities
   (ii) motivation
   (iii) experience
   (iv) expectations.
7. 'Choosing the right location was crucial because not everyone is interested in up-market garden accessories. We chose a location that had the right demographics — people took pride in their gardens and most of the people who live in the area are professional working people with cash to spend. It was also a big decision to set up our website where customers can order our garden accessories online.' Sonya Mezups, proprietor, Blooming nursery.

   Explain how selecting the correct location can make the difference between success and failure.
8. Select a small business that you buy from regularly and **identify** its strengths and weaknesses. If this business were for sale, **determine** whether you would consider purchasing it. Give reasons for your answer.
9. **Assess** the relationship between key success factors and the competitive edge that a small business should seek.
10. You have been employed as a business reporter with the local newspaper. You are asked to prepare an article that **examines** the number of government and private support agencies that provide assistance to small business owners. A major focus within your article should be an evaluation of two government websites that assist small businesses.
11. A friend wishes to go into business for herself. She is not sure whether to purchase an existing business or set up a new business. She comes to you for advice. **Outline** for her the advantages and disadvantages of each option.
12. Jane has just set up a small business as a wedding planner. She hopes that couples planning a wedding will commission her to put together a 'total wedding package', for which she will charge a fee. To create the type of wedding packages her customers want, she has to deal with a number of different wedding service suppliers. These include reception venues, wedding car hire businesses, photographers and video businesses, florists, printers, dressmakers and formalwear hire businesses. Jane wants to make sure she fulfils all her legal responsibilities and she wants to have a reputation as an ethical business owner, because she knows that most of her business will come from personal recommendations and word of mouth.

    Jane's biggest concern is that she doesn't know whether the other businesses she has to deal with share her principles. Imagine you are her solicitor and she comes to you seeking advice. She wants to know how she can tell whether or not the wedding service suppliers she will be dealing with are acting legally and ethically, because any unlawful or inappropriate activities will reflect back on her and her business.

    Construct a report for Jane that will help her identify whether or not her business is meeting its legal responsibilities to its customers, to other businesses and to the community. Your advice should include the following:
    - how to tell whether a business is conforming to the Competition and Consumer Act

- the responsibilities of food businesses, such as reception venues, in ensuring food safety
- what Jane can do to ensure she manages her legal responsibilities in an ethical and socially responsible manner.

13. **Analyse** why it is important for small business owners to have a detailed understanding of the market in which the business will be competing.

14. 'A business plan won't guarantee success but it does improve the chances of success.' **Assess** the accuracy of this statement.

15. 'Undertaking a break-even analysis in the early stages of the planning process is crucial. The information it provides determines how I advise the client to proceed.' Nick Aquilano, small business consultant, BizVest Planning.
(a) **Define** the term 'break-even analysis'.
(b) **Explain** why it is an important planning tool.
(c) **Demonstrate** how to calculate the break-even point.

APPENDIX: UNDERSTANDING KEY PROCESS VERBS

Assessment using key process verbs

The purpose of a key process verb in a question is to provide instructions on how to answer a question and how much to write. There is a direct relationship between the type of key process verb and the mark value allocated. The more thinking skills the key process verb requires, the higher the mark allocated.

Below is a colour coded list of the key process verbs that may be used for assessment. It is divided into three categories based on Bloom's Taxonomy. Each category represents the level of thinking skills required to complete a question. We have also included in the Key Process Verb list common exam terms such as 'Why', 'How', 'What' to help explain how to answer questions using these terms.

Mark allocation

The suggested marks used in these examples are specifically for short answer questions. Essay questions may also include a number of key process verbs.

Lower order thinking questions	**Clarify, define, describe, extract, identify, outline, recall, recount, state, summarise**	**1–3**
Middle order thinking questions	**Account, apply, calculate, classify, compare, construct, contrast, deduce, demonstrate, discuss, distinguish, examine, explain, interpret, investigate, justify, propose, recommend**	**3–6**
Higher order thinking questions	**Analyse, appreciate, assess, create, critically analyse/evaluate, determine, evaluate, extrapolate, predict, synthesise**	**6–12**

Time allocation

In order to complete each question, time allocation is very important. If a student does not complete the examination in time, because they have not calculated the minutes/marks correctly, they will lose marks. A formula for calculating minutes/marks is as follows:

$$\textit{Marks/minute} = \frac{\textit{Total exam time in minutes}}{\textit{Total exam marks}} = \textit{minutes/mark}$$

$$\textit{Example: Marks/minute} = \frac{\textit{180 exam minutes (3hrs)}}{\textit{100 exam marks}} = \textit{1.8 minutes/mark}$$

In the above example, the student would need to allocate 1.8 minutes per mark in an examination. Therefore, a 4-mark question should be allocated 1.8 minutes × 4 = 7.2 minutes (or rounded to seven minutes). This ensures the allocation of an appropriate amount of time for each question.

Definitions and examples

LOWER ORDER THINKING key process verbs
Short answer questions using the lower order thinking key process verbs will typically have a mark value between 1 and 3.
Clarify — make clear or plain.
Define — state meaning and identify essential qualities.
Describe — provide characteristics and features.
Extract — choose relevant and/or appropriate details.
Identify — recognise and name.
List — make a list of.
Outline — sketch in general terms; indicate the main features of.
Recall — present remembered ideas, facts or experiences.
Recount — retell a series of events.
State — describe the main points clearly and specifically.
Summarise — express, concisely, the relevant details.
What — describe, provide characteristics or features.
When — at what time or in what circumstances.
MIDDLE ORDER THINKING key process verbs
Short answer questions using the middle order thinking key process terms will typically have a mark value between 3 and 6.
Account — account for; state reasons for; report on. Give an account of; narrate a series of events or transactions.
Apply — use, utilise, employ in a particular situation.
Calculate — ascertain/determine from given facts, figures or information.
Classify — arrange or include in classes/categories.
Compare — show how things are similar or different.
Construct — make; build; put together items or arguments.
Contrast — show how things are different or opposite.
Deduce — draw conclusions.
Demonstrate — show by example.
Discuss — identify issues and provide points for and/or against.
Distinguish — recognise or note/indicate as being distinct or different from; note differences between.
Examine — inquire into.
Explain — relate cause and effect; make the relationships between things evident; provide why and/or how.
How — explain.
Interpret — draw meaning from.
Investigate — plan, inquire into and draw conclusions.
Justify — support an argument or conclusion.
Propose — put forward (for example a point of view, idea, argument, suggestion) for consideration or action.
Recommend — provide reasons in favour.
To what extent — how much impact, how broadly?
Why — explain the cause and effect relationship.
With reference to — in regards to, relating to.

LOWER ORDER examples
Clarify the reasons for…
Define the term…
Describe four roles…
Extract the issues that may arise…
Identify two effects of…
List the types of...
Outline the roles of…
Recall the factors that…
Recount under what circumstances…
State how a business may address…
Summarise how the two issues affected the…
What are the main parts of the process?
When did the change in owner occur?
MIDDLE ORDER examples
Account for the improvements to…
Apply one of the processes relevant to…
Calculate which you believe to be the more…
Classify the following list of consumers into the…
Compare the problems experienced by…
Construct a SWOT analysis for the following small businesses…
Contrast a range of businesses with different legal structures…
Deduce what impact this had on the…
Demonstrate the opportunities a business can…
Discuss the role of…
Distinguish between internal and external growth…
Examine the reasons for…
Explain the processes undertaken…
How did she improve sales?
Interpret the reasons for the business owner deciding to…
Investigate three options available to the employees…
Justify your selection…
Propose a plan that may provide the business with…
Use the information provided to **recommend** a strategy…
To what extent were the changes in personnel...
Why was the bonus paid?
With reference to your application, you have been successful.

HIGHER ORDER THINKING key process verbs
Short answer questions using the higher order thinking key process verbs will typically have a mark value between 6 and 12.
Analyse — identify components and the relationship between them; draw out and relate implications.
Appreciate — make a judgement about the value of.
Assess — make a judgment of value, quality, outcomes, results or size.
Create — produce; design; invent; devise a new solution or plan.
Critically analyse/evaluate — add a degree or level of accuracy, depth, knowledge and understanding, logic, questioning, reflection or quality.
Detail — give specific information about.
Determine — make a decision or work out an answer after appropriate thought and investigation.
Evaluate — make a judgement based on criteria; determine the value of.
Extrapolate — infer from what is known.
Predict — suggest what may happen based on available information.
Synthesise — put together various elements to make a whole.

HIGHER ORDER examples
Analyse the impact of changes to the…
Appreciate the importance of government bodies…
Assess the importance of…
Create a marketing strategy suitable to a business at this stage…
Critically analyse this statement…
Detail how the process occurred.
Determine whether the change required would…
Evaluate the processes…
Extrapolate the data found in…
Predict the outcome for a business if the following…
Consider a business's function and **synthesise** this information…

GLOSSARY

accountability: occurs when a business acts in the best and highest interests of its owners. Full and complete 'disclosure', which means to be open and not hide the truth, ensures that the books of account are kept accurately and that the information reflected in them, and which is summarised in reports, is based on the true and actual transactions. Another term for accountability is stewardship. p. 237

accounting: is a managerial and administrative tool for recording financial transactions, so that a summary of what has happened to business money can be traced. p. 235

acquisition (takeover): an acquisition (takeover) occurs when one business takes control of another business by purchasing a controlling interest in it. p. 94

acquisition (HR): is the process of attracting and recruiting the right staff for roles in a business. p. 259

assets: are items of value owned by the business that can be given a monetary value. p. 249

audit: an audit is an independent check of the accuracy of financial records and accounting procedures. p. 287

Australian Business Number (ABN): the Australian Business Number (ABN) is a single identifying number that a business uses when dealing with government departments and agencies. p. 391

autocratic leadership style: a manager using an autocratic leadership style tends to make all the decisions, dictates work methods, limits worker knowledge about what needs to be done to the next step to be performed, frequently checks employee performance and sometimes gives feedback that is punitive. p. 179

award: an award is a legally binding agreement that sets out the minimum wages and conditions for a group of employees. p. 272

balance of payments (BOP): the balance of payments (BOP) is a record of a country's trade and financial transactions with the rest of the world over time, usually one year. p. 325

balance sheet: a balance sheet represents a business's assets and liabilities at a particular point in time, expressed in money terms, and represents the net worth of the business. p. 248

bankruptcy: is a declaration that a business or person is unable to pay his or her debts. p. 106

behavioural approach: the behavioural approach to management stresses that people (employees) should be the main focus of the way in which the business is organised. p. 182

benchmark: a benchmark is a standard by which something can be measured or judged. p. 145

best practice: refers to those business practices that are regarded as the best or of the highest standard in the industry. p. 309

body language: is the use of gestures, facial expressions and posture to communicate. p. 129

brand: a brand is a name, term, symbol or design that identifies a specific product and distinguishes it from its competitors. p. 229

brand logo: a brand logo is a graphic representation that identifies a business or product. p. 229

break-even analysis: is used to determine the level of sales that needs to be generated to cover the total cost of production. p. 415

budget: a budget is the business's financial plan for the future. p. 421

bureaucracy: is the set of rules and regulations that control a business. p. 171

business: a business can be defined as the organised effort of individuals to produce and sell, for a profit, the products that satisfy individuals' needs and wants. p. 7

business activity statement (BAS): the business activity statement (BAS) records a business's claim for input tax credits and accounts for GST payable. p. 389

business (corporate) culture: refers to the values, ideas, expectations and beliefs shared by members of the organisation. p. 77

business environment: the business environment refers to the surrounding conditions in which the business operates. It can be divided into two broad categories: external and internal. p. 49

business ethics: is the application of moral standards to business behaviour. p. 282

business information system (BIS), management information system (MIS): a business information system (BIS), also referred to as a management information system (MIS), gathers data, organises and summarises them, and then converts them into practical information. p. 302

business life cycle: the business life cycle refers to the stages of growth and development a business can experience. p. 86

business opportunity: a business opportunity can be described as something an entrepreneur can see as an avenue to success. It is often identified when a person believes they can provide goods or services in a better or different way from those already on the market. p. 354

business plan: a business plan is the 'travel itinerary' for future growth and development within a business. It sets out the desired goals and direction of the business. p. 394

cash flow: is simply the money coming into the business in the form of cash receipts, and the money leaving the business as cash payments. p. 90

cash flow projection: the cash flow projection shows the changes to the cash position brought about by the operating, investing and financial activities of the business. p. 416

cash flow statement: a cash flow statement is a financial statement that indicates the movement of cash receipts and cash payments resulting from transactions over a period of time. p. 238

chain of command: a chain of command is a system that determines responsibility, supervision and accountability of members of the organisation. p. 177

change: is any alteration in the internal or external environments. p. 291

change agent: a change agent is a person or group of people who act as catalysts, assuming responsibility for managing the change process. p. 308

change management: is a methodical approach to dealing with change, both from the perspective of a business and on the individual level. p. 309

choice: is the act of selecting among alternatives. p. 12

classical approach: the classical approach to management stresses how best to manage and organise workers so as to improve productivity (output). p. 169

closing stock: is the value of stock on hand at the end of the financial year. p. 244

commercial bills: are short-term loans issued by financial institutions, for larger amounts for a period of generally between 30 and 180 days. p. 374

common law: refers to law developed by courts and tribunals. p. 270

communication: is the exchange of information between people; the sending and receiving of messages. p. 127

Competition and Consumer Act 2010: the Competition and Consumer Act 2010 (Cwlth) is a law that protects both consumers and businesses. It protects consumers from deceptive or misleading practices, and it regulates the trade practices of businesses. p. 380

competition: is rivalry among businesses that seek to satisfy a market. p. 355

competitive advantage: refers to the strategies used by a business to gain an 'edge' over its competitors. p. 439

complementary business: a complementary business is one that sells a similar range of goods and services. p. 72

conflict of interest: a conflict of interest occurs when a person takes advantage of a situation or piece of information for his or her own gain rather than for the employer's interest. p. 286

consumer buying behaviour: refers to the decisions and actions of consumers when they purchase goods and services for personal household use. p. 224

contingencies: are unanticipated events that can lead to financial difficulty. For a business to be well managed, it needs to have saved money for such events. p. 235

contingency approach: stresses the need for flexibility and adaptation of management practices and ideas to suit changing circumstances. p. 193

continuous improvement: involves an ongoing commitment to achieving perfection. p. 215

control process: the control process involves establishing standards in line with the goals of the business, measuring the performance of the business against those standards or benchmarks, and making changes where necessary to ensure that the goals of the business have been met. p. 175

controlling: is the process of evaluating performance by comparing what was intended to happen with what has actually occurred, and then taking corrective action to ensure that the set objectives are being achieved. pp. 122, 175

Corporate Code of Conduct: a Corporate Code of Conduct is a set of ethical standards for managers and employees to abide by. p. 287

cost of goods sold (COGS): The cost of goods sold (COGS) is the value of stock that a business has sold to its customers. p. 244

creditors: are those people or businesses who are owed money. p. 106

curriculum vitae or **résumé:** a curriculum vitae or résumé is a summary of a person's previous employment experience. p. 263

data: are unprocessed facts and figures such as sales figures and customer complaints. p. 302

debentures: are issued by a company for a fixed rate of interest and for a fixed period of time. p. 374

debt finance: relates to the short-term and long-term borrowing from external sources by a business. p. 373

decision making: is the process of identifying the options available and then choosing a specific course of action to solve a specific problem. p. 134

delegation: is the handing over of certain tasks or responsibilities to an employee who is suitably capable and qualified to carry them out. p. 185

deregulation: is the removal of government regulation from industry, with the aim of increasing efficiency and improving competition. p. 52

development: refers to activities that prepare staff to take greater responsibility in the future. p. 266

dismissal: a dismissal is when the behaviour of an employee is unacceptable and it then becomes necessary for a business to terminate the employee's employment contract. p. 278

distribution channels: are ways of getting the product to the customer. p. 231

diversification: (or conglomerate integration) occurs when a business acquires or merges with a business in a completely unrelated industry. p. 96

dividend: a dividend is part of a business's profit that is divided among shareholders. p. 11

division: refers to the separation of key business functions into specialised units or departments. The business is divided into functional areas. p. 201

driving forces: are those forces that support the change. p. 307

e-business: (electronic business) is using the internet to conduct business. p. 446

ecological sustainability: occurs when economic growth meets the needs of the present population without endangering the ability of future generations to meet their needs. p. 84

e-commerce: is the buying and selling of goods and services via the internet. p. 448

economic cycles: (or business cycles) are the periods of growth ('boom') and recession ('bust') that occur as a result of fluctuations in the general level of economic activity. p. 50

economic growth: occurs when a nation increases the real value of goods and services over a period of time. p. 324

economy: an economy is a system used to determine what to produce, how to produce and to whom production will be distributed. p. 323

effectiveness: measures the degree to which a goal has been achieved. p. 119

efficiency: compares the resources needed to achieve a goal (the costs) against what was actually achieved (the benefits). p. 119

employee selection: involves gathering information about each applicant for a position, then using that information to choose the most appropriate applicant. p. 263

employee training: generally refers to the process of teaching staff how to perform their job more efficiently and effectively by boosting their knowledge and skills. p. 165

employment contract: an employment contract is a legally binding, formal agreement between an employer and an employee. p. 270

enterprise agreements: are collective agreements made at a workplace level between an employer and a union, acting on behalf of its employees, or between the employer and a group of employees, about terms and conditions of employment. p. 273

entrepreneur: an entrepreneur is someone who starts, operates and assumes the risk of a business venture in the hope of making a profit. p. 15

entrepreneurship: is the ability and willingness to start, operate and assume the risk of a business venture in the hope of making a profit. p. 15

equity finance: is the funds contributed by the business owner(s) to start and then expand the business. p. 374

evaluation: is the process of assessing whether the business has achieved stated goals. p. 418

expenses: are simply costs. Specifically, expenses are the costs incurred in the process of acquiring or manufacturing a good or service to sell and the costs (direct and indirect) associated with managing all aspects of the sales of that good or service. p. 245

external environment: the external environment includes those factors over which the business has very little control. p. 49

external recruitment: involves filling job vacancies with people from outside the business. p. 261

factoring: is the selling of accounts receivable for a discounted price to a finance or factoring company. p. 374

Fairtrade: is a trading partnership that seeks greater equity (fairness) in international trade. It promotes the rights of marginalised workers, especially in low-income countries. p. 284

finance: refers to how a business funds its activities — for instance, where it gets the money to trade, why it chooses to use certain lenders — as well as the costs, risks and benefits of different types of borrowings. p. 237

financial resources: are the funds the business uses to meet its obligations to various creditors. p. 74

financial statements: are reports that summarise transactions over a period of time. p. 238

finished product: a finished product is one that is ready for customers to buy and use. p. 7

fixed costs (FC): are costs that do not vary regardless of how many units of a good or service are produced. p. 415

flatter organisational structures: have evolved due to a 'de-layering' of management structures resulting in the elimination of one or more management levels. p. 189

flexible: refers to being responsive to change and able to adjust to changing circumstances. p. 135

float: a float is the raising of capital in a company through the sale of shares to the public. p. 45

forecasts or **projections:** are the business's predictions about the future. p. 414

franchise: a franchise involves buying the rights from another business to distribute its products under its name. p. 359

franchisee: a franchisee is an individual or business that purchases a franchise. p. 359

franchisor: a franchisor is an individual or business that grants a franchise. p. 359

geographical spread: is the presence of a business and the range of its products across a suburb, city, state or country or the globe. p. 23

globalisation: is the process that sees people, goods, money and ideas moving around the world faster and more cheaply than before. p. 54

goal: a goal is a desired outcome (target) that an individual or business intends to achieve within a certain time frame. p. 144

goods: are items that can be seen or touched. p. 7

goods and services tax (GST): The goods and services tax (GST) is a broad-based tax of 10 per cent on the supply of most goods and services consumed in Australia. p. 389

goodwill: is the monetary value attached to the reputation of a particular business. p. 358

government enterprises: are government-owned and operated businesses. p. 41

grant: a grant is any monetary or financial assistance that does not generally have to be repaid. p. 412

gross domestic product (GDP): is the total money value of all goods and services produced in Australia over a one-year period. p. 324

gross profit: is the term given to the revenue less cost of goods sold (COGS). p. 244

holistic: a holistic approach looks at the whole picture. p. 302

horizontal integration: occurs when a business acquires or merges with another firm that makes and sells similar products. p. 95

human resources: are the employees of the business and are generally its most important asset. p. 74

human resource/employment cycle: the human resource/employment cycle covers all stages in the process of employing staff, from initial planning through to recruitment, selection, induction, training and development, performance management, and eventual separation of employment. p. 256

human resource management (HRM): in its simplest terms, is defined as the effective management of the formal relationship between the employer and the employees. p. 254

income: is money received by a person for providing his or her labour, or a business from a return on its investments. p. 10

income statement or **statement of financial performance:** the income statement, or statement of financial performance, is a summary of the income earned and the expenses incurred over a period of trading. It helps users of information see exactly how much money has come into the business as revenue, how much has gone out as expenditure and how much has been derived as profit. p. 243

incorporated: refers to the process companies go through to become a separate legal entity from the owner/s. p. 33

incorporation: is the process that companies go through to become incorporated, i.e. to become a registered company and a separate legal entity. p. 37

industry: an industry consists of businesses that are involved in similar types of production. p. 28

inertia: refers to an unenthusiastic response to proposed change. p. 306

information: is processed data that have been deliberately selected and organised to be useful to an individual manager. p. 302

information resources: include the knowledge and data required by the business, such as market research, sales reports, economic forecasts, technical material and legal advice. p. 74

innovation: is either creating a new product, service or process, or significantly improving an existing one. p. 13

input tax credit: an input tax credit is an allowable tax deduction that a business can claim for any GST included in the price of business inputs. p. 389

inputs: are the resources used in the transformation (production) process. p. 206

insolvent: being insolvent occurs when a company is not able to pay its debts as and when they fall due. p. 107

intangibles: include services that cannot be touched. p. 205

interdependence: refers to the mutual dependence that the key functions have on one another. The key business functions work best when they overlap, and employees work towards common goals. For each function area to perform at capacity, it depends on the support of the others. p. 200

interest: is the cost of borrowing money. p. 375

internal environment: the internal environment includes those factors over which the business has some degree of control. p. 49

internal recruitment: involves filling job vacancies with present employees, rather than looking outside the business. p. 260

interpersonal (people) skills: are those skills needed to work and communicate with other people and to understand their needs. p. 126

intrapreneur: an intrapreneur is an individual who takes on the entrepreneurial roles within a business. p. 161

involuntary cessation: occurs when the owner is forced to cease trading by the creditors of the business. p. 106

involuntary separation: occurs when an employee is asked to leave the business against their will. p. 277

job analysis: is a systematic study of each employee's duties, tasks and work environment. p. 259

job description: a job description is a written statement describing the employee's duties, tasks and responsibilities associated with the job. p. 260

job specification: a job specification is a list of the key qualifications needed to perform a particular job in terms of education, skills and experience. p. 260

labour productivity: measures how much an employee can produce in a set period of time. p. 160

large business: a large business is a business with 200 or more employees. p. 21

leadership: is the ability to influence people to set and achieve specific goals. p. 132

leadership style: a manager's leadership style is essentially their way of doing things — their behaviour and attitude. p. 178

leading: is the process of influencing or motivating people to work towards the achievement of the organisation's objectives. pp. 122, 184

learning organisation: a learning organisation monitors and interprets its environment, seeking to improve its understanding of the relationship between its actions and its environment. p. 267

leasing: is a long-term source of borrowing for businesses. It involves the payment of money for the use of equipment that is owned by another party. p. 444

liabilities: are items of debt owed to other organisations (e.g. suppliers, banks) and include loans, accounts to be paid by the business, mortgages, credit card debt and accumulated expenses. p. 249

limited liability: is a feature of corporate ownership that limits each owner's financial liability to the amount of money he or she has paid for the business's shares. p. 37

liquidation: occurs when an independent and suitably qualified person – the liquidator – is appointed to take control of the business with the intention of selling all the company's assets in an orderly and fair way in order to pay the creditors. p. 107

liquidity: refers to the amount of cash a business has access to and how readily it can convert its assets into cash so that debt can be paid. p. 238

local business: a local business has a very restricted geographical spread; it serves the surrounding area. p. 23

long-term growth: is the ability of a business to continually expand. p. 407

management: a more contemporary definition of management views management as the process of working with and through other people to achieve business goals in a changing environment. Crucial to this process is the effective and efficient use of limited resources. p. 119

management consultant: a management consultant is someone who has specialised knowledge and skills within an area of business. p. 309

management hierarchy: is the arrangement that provides increasing authority at higher levels of the hierarchy. p. 176

manager: a manager is someone who coordinates the business's limited resources in order to achieve specific goals. p. 119

market analysis: involves collecting, summarising and analysing information about the state of the market, customers, the threats and opportunities that the market presents, and any advantages or disadvantages that the business is likely to have over its competitors. p. 365

market concentration: refers to the number of competitors in a particular market. There are four main types of market concentration:

- a **monopoly** — is complete concentration by one firm in the industry, e.g. Australia Post
- an **oligopoly** — where a small number of larger firms have a greater control over a market, e.g. car manufacturers
- **monopolistic competition** — where there is a large number of buyers and sellers in a particular market, e.g. local retailing shops
- **perfect competition** — where there is a large number of small firms that sell similar products. They are unable to differentiate products from each other and so can only use price as a way of achieving market share, e.g. fruit and vegetable growers. p. 65

market segmentation: occurs when the total market is subdivided into groups of people who share one or more common characteristic. p. 223

market share: refers to the business's share of the total industry sales for a particular product. pp. 21, 148

marketing: is a total system of interacting activities designed to plan, price, promote and distribute products to present and potential customers. p. 219

marketing mix: refers to the combination of the four elements of marketing, the four Ps — product, price, promotion and place — that make up the marketing strategy. p. 227

marketing strategies: are actions undertaken to achieve the business's marketing goals. p. 226

mass markets: in mass markets the seller mass-produces, mass-distributes and mass-promotes one product to all buyers. p. 222

mass production: is the process of manufacturing standardised goods on a huge scale by automation. p. 169

medium business: a medium business is a business with 20–199 employees. p. 21

mentor: a mentor is someone — usually a more experienced employee — who helps develop a less experienced employee (the protégé). p. 164

mentoring: is the process of developing another individual by offering tutoring and coaching, and modelling acceptable behaviour. p. 164

merger: a merger occurs when the owners of two separate businesses agree to combine their resources and form a new organisation. p. 94

micro business: a micro business is a business with fewer than five employees. p. 21

modifying: is the process of changing existing plans, using updated information to shape future plans. p. 424

monitoring: is the process of measuring actual performance against planned performance. p. 418

mortgage: a mortgage is a loan secured by the property of the borrower (business). p. 374

motivation: refers to the individual, internal process that directs, energises and sustains a person's behaviour. p. 162

multinational corporation: a multinational corporation is a company that has branches in many different countries. pp. 21, 24

multiskilling: allows employees to develop skills in a wide range of tasks through ongoing training. p. 165

national business: a national business is one that operates within just one country. p. 23

net profit: is the difference between the gross profit and operating and non-operating expenses. p. 245

niche market: a niche market is a narrowly selected target market segment. p. 225

nonverbal communication: is any message that is not written or spoken. p. 129

objective: an objective is a specific statement detailing what a business (or individual) needs to achieve in order to accomplish its vision. p. 405

on-costs: are payments for non-wage benefits. p. 384

opening stock: is the value of stock (or inventory) that the business has at the start of the financial year. p. 244

operating expenses: are all the costs of running the business except the cost of goods sold. p. 9

operational objectives: focus on short-term issues and describe the course of action necessary to achieve the tactical objective and strategic goal. p. 405

operational planning: provides specific details about the way in which the business will operate in the short term. p. 175

operations: refers to the business processes that involve transformation or, more generally, 'production'. p. 202

operations management: consists of all the activities in which managers engage to produce a good or service. p. 202

organisation process: the organisation process is the range of activities that translate the goals of a business into reality. p. 175

organisational structure: an organisational structure is the framework in which the business defines how tasks are divided, resources are used and departments are coordinated. p. 410

organising: is the structuring of the organisation to translate plans and goals into action. pp. 122, 175

outputs: refer to the end result of a business's efforts — the service or product that is delivered or provided to the consumer. p. 210

outsourcing: is the use of external sources or businesses to undertake business functions or activities for the business. p. 199

overdraft: with an overdraft, the bank allows a business to overdraw their account up to an agreed limit for a specified time, to overcome a temporary cash shortfall. p. 374

owner's equity: is the funds contributed by the owner(s) to establish and build the business. It is also called 'capital'. p. 250

packaging: involves the development of a container and the graphic design for a product. p. 228

participative or **democratic leadership style:** a participative or democratic leadership style is one in which the manager consults with employees to ask their suggestions and then seriously considers those suggestions when making decisions. p. 191

partnership: a partnership is a legal business structure that is owned and operated by between two and 20 people with the aim of making a profit. p. 35

performance standard: a performance standard is a forecast level of performance against which actual performance can be compared. p. 418

physical resources: include equipment, machinery, buildings and raw materials. p. 74

place or **distribution:** are activities that make the products available to customers when and where they want to purchase them. p. 231

planning: is the preparation of a predetermined course of action for a business. pp. 122, 174, 399

primary industry: includes those businesses involved in the collection of natural resources. p. 28

primary target market: the primary target market is the market segment at which most of the marketing resources are directed. p. 224

privatisation: is the process of transferring the ownership of a government business to the private sector. p. 41

proactive: refers to a management style that incorporates dynamic action and forward planning to achieve particular objectives. p. 135

proactive: to be proactive is to initiate change rather than simply to react to events. p. 291

problem solving: is a broad set of activities involved in searching for, identifying and then implementing a course of action to correct an unworkable situation. p. 134

product: a product is a good or service that can be bought or sold. p. 7

product life cycle: the product life cycle describes the life of a product over four stages: introduction, growth, maturity and decline. p. 227

production: refers to those activities undertaken by the business that combine the resources to create products that satisfy customers' needs and wants. p. 7

profit: is what remains after all business expenses have been deducted from sales revenue. p. 9

profit maximisation: occurs when there is a maximum difference between the total revenue (that is, the number of sales made multiplied by the price) coming into the business and total costs being paid out. p. 147

promotion: describes the methods used by a business to inform, persuade and remind a market about its products. pp. 151, 229

proprietary (private) company: A proprietary (private) company is an incorporated business and usually has between two and 50 private shareholders. p. 38

prospectus: a prospectus is a document giving details of a company and inviting the public to buy shares in it. p. 45

quality: refers to the degree of excellence of goods or services and their fitness for a stated purpose. p. 212

quality assurance: involves the use of a system so that a business achieves set standards in production. p. 213

quality circles: are groups of workers who meet to solve problems relating to quality. p. 215

quality control: involves the use of inspections at various points in the production process to check for problems and defects. p. 212

quality management: is the strategy which a business uses to make sure that its products meet customer expectations. p. 212

quality of life: refers to the overall wellbeing of an individual, and is a combination of both material and non-material benefits. p. 18

quaternary industry: includes services that involve the transfer and processing of information and knowledge. p. 30

quinary industry: includes all services that have traditionally been performed in the home. p. 30

reactive: to be reactive is to wait for a change to occur and then respond to it. p. 291

realisation: is the process of converting the assets of a business into cash. p. 106

receivership: is where a business has a receiver take charge of the affairs of the business. Unlike liquidation, the business may not necessarily be wound up. p. 107

recruitment: is the process of finding and attracting the right quantity and quality of staff to apply for employment vacancies or anticipated vacancies. p. 260, 434

redundancy: occurs when a person's job no longer exists, usually due to technological changes, an organisational restructure or a merger or acquisition. p. 277

regulations: are rules, laws or orders that businesses must follow. p. 59

research and development (R&D): is a set of activities undertaken to improve existing products, create new products and improve production. p. 13

resignation: is the voluntary ending of employment by the employee 'quitting' their job. p. 276

resource allocation: refers to the efficient distribution of resources so as to successfully meet the goals that have been established. p. 410

restraining forces: are those forces that work against the change. p. 307

retirement: occurs when an employee decides to give up full-time or part-time work and no longer be part of the labour force. p. 276

retrenchment: is when a business dismisses an employee because there is not enough work to justify paying him or her. p. 277

revenue: is the money a business receives as payment for its products. p. 9

risk: refers to the possibility of loss. p. 15

salary: A salary is a fixed regular payment, usually paid on a fortnightly or monthly basis but often expressed as an annual sum, made to a permanent employee of a business. p. 11

scientific management: is an approach that studies a job in great detail to discover the best way to perform it. p. 170

secondary industry: involves taking a raw material and making it into a finished or semi-finished product. p. 28

secondary target market: a secondary target market is usually a smaller and less important market segment. p. 224

separation: is the ending of the employment relationship. p. 276

services: are things done for you by others. p. 7

share: a share is a part ownership of a public company. p. 151

shareholders: are people who are part owners of a company because they own a number of shares. p. 11

sigma-six: a sigma-six process is one in which 99.99 per cent of all manufactured products are defect free. p. 408

skill: is the ability that comes from the knowledge, practice and talent to do something well. p. 123

skills audit: a skills audit is a process that establishes the current skills levels of employees and future skills requirements. p. 435

skills inventory: a skills inventory is a database containing information on the skills, abilities and qualifications of existing staff. p. 435

small business: a small business is a business with 5–19 employees. p. 21

small to medium enterprises: are defined by the Australian Bureau of Statistics as firms with fewer than 200 full-time equivalent employees and/or less than $10 million turnover. p. 21

social justice: in business is about adopting a set of policies to ensure that employees or other community members are treated equally and fairly. p. 152

socialisation: is the process a new employee undergoes in the first few weeks of employment through which he or she learns how to cope and succeed. p. 164

sole trader: A sole trader is a business that is owned and operated by only one person. p. 34

specialisation of labour: refers to the degree to which tasks are divided into separate jobs. p. 177

staff involvement: means involving employees in the decision-making process and giving them the necessary skills and rewards. p. 160

stakeholder: a stakeholder is any group or individual who has an interest in or is affected by the activities of a business. p. 81

stakeholder engagement: refers to businesses sharing information with and seeking input from stakeholders, and involving them in decision making. p. 140

strategic goals: focus on long-term, broad aims and apply to the business as a whole. p. 405

strategic planning: is planning for the following three to five years. This level of planning will assist in determining where in the market the business wants to be, and what the business wants to achieve in relation to its competitors. p. 174

strategic thinking: allows a manager to see the business as a whole and to take the broad, long-term view. p. 130

strategies: are the actions that a business takes to achieve specific goals. p. 198

superannuation: is a scheme set up by the federal government. It requires all employers to make a financial contribution to a fund that employees can access when they leave or retire from a job. The percentage an employer must contribute will increase gradually to 12 per cent by 2025. p. 385

support services: are the activities needed to assist the core operations or prime function of a business. p. 74

sustainable competitive advantage: A sustainable competitive advantage refers to the ability of a business to develop strategies that will ensure it has an 'edge' over its competitors for a long period of time. p. 64

sustainable development: occurs when the needs of the present population are met without endangering the ability of future generations to meet their own needs. p. 155

SWOT analysis: a SWOT analysis involves the identification and analysis of the internal strengths and weaknesses of the business, and the opportunities in, and threats from, the external environment. p. 402

tactical objectives: focus on mid-term, departmental issues and describe the course of action necessary to achieve the business's strategic goals. p. 405

tactical planning: is flexible, adaptable planning, usually over one to two years, that assists in implementing the strategic plan. p. 174

tangibles: are goods that can be touched. p. 205

target market: A target market is a group of customers with similar characteristics who presently, or who may in the future, purchase the product. p. 222

taxation: is the compulsory payment of a proportion of earnings to the government. p. 387

teamwork: involves people who interact regularly and coordinate their work towards a common goal. p. 188

tertiary industry: involves people performing a vast range of services for other people. p. 29

time and motion study: A time and motion study is a process of examining each of the steps in a production procedure and the time taken to perform them. p. 170

total cost (TC): The total cost (TC) of producing a certain number of goods or services is the sum of the fixed and variable costs for those units. p. 415

total quality management: is an ongoing, business-wide commitment to excellence that is applied to every aspect of the business's operation. p. 213

total revenue (TR): is the total amount received from the sales of a good or service. p. 414

traditional definition of management: The traditional definition of management is the process of coordinating a business's resources to achieve its goals. p. 119

training: generally refers to the process of teaching staff how to perform their job more efficiently and effectively by boosting their knowledge and skills. p. 266

transformation: is the conversion of inputs (resources) into outputs (goods or services). p. 206

transformed resources: are those inputs that are changed or converted in the operations process. p. 206

transforming resources: are those inputs that carry out the transformation process. p. 206

triple bottom line: refers to the economic, environmental and social performance of a business. pp. 139, 283

undercapitalisation: occurs when there is a lack of sufficient funds to operate a business normally. p. 104

unfair dismissal: occurs when an employee is dismissed by their employer and they believe the action is harsh, unjust or unreasonable. p. 278

unlimited liability: occurs when the business owner is personally responsible for all the business's debt. p. 34

unsecured note: an unsecured note is a loan from investors for a set period of time. It is not secured against the business's assets. p. 374

variable costs (VC): are costs that depend on the number of goods or services produced. p. 415

venture capital: is money that is invested in small and sometimes struggling businesses that have the potential to become very successful. p. 46

vertical integration: occurs when a business expands at different but related levels in the production and marketing of a product. p. 95

vision: is the clear, shared sense of direction that allows people to attain a common goal. p. 132

vision statement: a vision statement broadly states what the business aspires to become in the future. pp. 303, 403

voluntary administration: occurs when an independent administrator is appointed to operate the business in the hope of trading out of the present financial problems. p. 107

voluntary cessation: occurs when the owner ceases to operate the business of their own accord. p. 106

voluntary separation: occurs when an employee chooses to leave the business of their own free will. p. 276

wage: a wage is money received by workers, usually on an hourly or daily basis, for services they provide to an employer. p. 11

zoning: is a means by which local councils allocate land for different uses, such as residential, commercial, recreational and industrial. p. 366

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