Year 10 Business Studies Knowledge Book

Business Ownership

Types of ownership	• Sole trader • Partnership • Private limited company (Ltd) • Public limited company (plc) • Not-for-profit organisation

Sole trader = a business with one owner	
Advantages	Disadvantages
Easy to set up	Owners may have to work long hours
You get to be your boss	Unlimited liability
You keep all of the profits	Many be hard to raise the money to start up

Partnership = a business with between two and twenty owners	
Advantages	Disadvantages
More owners mean a greater range of ideas and skills	Decision making is shared
The work can be shared	Unlimited liability
All partners put money in at the start of the business	Each partner gets a share of the profit

Unlimited liability = the business and the owners are seen as the same thing. Therefore if the business owes money, the owner owes money.

Private limited company (Ltd) = a business owned by shareholders. Shares are sold privately.	
Advantages	Disadvantages
Limited liability	Shareholders get a share of the profits. They are paid a dividend
Money from the sale of shares can help the business start up	May be difficult to get a loan from a bank due to limited liability
	More expensive and complicated to set up

Public limited company (plc) = a business owned by shareholders. Shares are sold on the stock exchange	
Advantages	Disadvantages
Limited liability	Shareholders get a share of the profits. They are paid a dividend
Money from the sale of shares can help the business start up	Accounts are made public

Limited liability = the business and the owners are seen as separate legal entities. If the business goes into debt, the owners are not in debt.

Not-for-profit organisation = a business that is not aiming to make a profit. They may be charities, social enterprises or clubs and groups. They are able to set up with either limited or unlimited liability.

Setting business aims and objectives

Aims and objectives	Goals or targets a business aims to achieve
Example aims and objectives	• Survival • Profit maximisation • Growth • Market share • Customer satisfaction • Social and ethical objectives • Shareholder value
Survival	A short term aim to make sure all costs are covered
Profit maximisation	Aiming to make as much profit as possible either by selling more or by keeping costs as low as possible
Growth	Aiming to increase the size of the business. This may include international expansion
Market share	This shows the percentage of total market sales a business has made. The aim is to have a large market share
Customer satisfaction	Aiming to have positive customer feedback
Social and ethical objectives	Aiming to act in a way that is morally right. This might be for customers, employees, the environment…
Shareholder value	Aiming to make high profit levels so that shareholders earn a large dividend.

Business planning

Purpose of a business plan	• Planning a new business • Raising finance • Setting objectives • Planning hoe the four business functions will be organised
Main sections of a business plan	• The business idea • Key targets for the business • Finance required • Market overview • Financial forecasts

Expanding a Business

Methods of expansion	• Organic growth
	  ○ Franchising
	  ○ Opening new stores
	  ○ Expanding through e-commerce
	  ○ Outsourcing
	• External growth
	  ○ Mergers and takeovers
	    ▪ Competitor
	    ▪ Supplier
	    ▪ Customer
	    ▪ Unrelated firm

Method of growth	Advantage	Disadvantage
Franchising	Increases the market share and brand awareness of the firm	A badly run franchise will affect the reputation of the firm
Opening new stores	Low risk strategy to increase sales	Expensive
Expanding through e-commerce	Access to a much larger market	Technology will need to be updated
Outsourcing	Can be quick and cheap	The firm has little control over the quality
Mergers and takeovers	The firm will grow very quickly	May be difficult to get two firms to work together

Economies of scale	As firms grow and expand production average unit cost falls
Purchasing economies of scale	These happen when a large firm buys its supplies in bulk and so get them at a cheaper unit price than a small firm
Technical economies of scale	Larger firms can buy and use more advanced machinery. This will increase efficiency and keep unit costs low.
Diseconomies of scale	This happens when firms get too big and average unit costs start to increase. This is usually because of poor communication and co-ordination
Average unit cost	= total cost / output

Technology

E-commerce	Selling a product or service online. This helps firms reach a wider target market.
Digital communication	The use of technology to communicate with stakeholders
Examples of digital communication	• Social media • Websites • Email • Mobile apps • Live chats

Ethics and the Environment

Ethical behaviour	This requires businesses to act in ways that stakeholders consider to be both fair and honest
Examples of ethical behaviour	• Buying raw materials from Fair trade sources • Paying workers fairly and providing a comfortable working environment • Not using animal testing • Considering the environmental impact
Environmental considerations	• Impact on traffic congestion • Recycling • Disposing of waste • Noise and air pollution
Sustainability	• Global warming • Using scarce resources

Advantages of ethics (for the firm)	Disadvantages of ethics (for the firm)
• Good reputation • Can charge a higher price	• Costs of production are higher • Do consumers care enough?

Economic Climate

Interest rate	Cost of borrowing and the reward for saving
The effect of a high interest rate	• Borrowing is more expensive. Saving is more attractive = less consumer spending = lower sales for firms • A firm that has a loan or overdraft will have to pay back more interest
The effect of a low interest rate	• Borrowing is less expensive. Saving is less attractive = more consumer spending = higher sales for firms • A firm that has a loan or overdraft will have to pay back more interest

Unemployment	People are unemployed if they are looking for a job but can't find one.
Effects of unemployment on firms	Negative effect: • Unemployment = less spending in the economy = less sales for the firm Positive effect: • Firms that sell cheaper products eg. Lidl may see an increase in sales • Firms may find it easier to fill vacancies
Increase in income	Firms are likely to see an increase in sales and profits
Decrease in income	Firms are likely to see a decrease in sales and profits

Globalisation

Globalisation	This is the process by which businesses and consumers around the world become more connected.
Positive effects of globalisation on UK businesses	• Larger market to sell products to • Manufacturing products abroad can lower unit costs
Negative effects of globalisation on UK businesses	• UK firms may have to compete with cheaper foreign imports • Manufacturing abroad may give the firm a bad reputation

Exchange rate	The cost of one currency in terms of another
Strong Pound (SPICED)	**S**trong **P**ound **I**mports **C**heaper **E**xports **D**earer
Weak Pound (WPIDEC)	**W**eak **P**ound **I**mports **D**earer **E**xports **C**heaper

Legislation

Employment Law	Law to protect employees
Examples of employment law	• National minimum wage/ living wage • The Equality Act 2010
Effects on businesses	• Firms can't cut costs by paying workers less than the legal minimum • Firms can't discriminate when recruiting and setting pay

Health and safety Law	Law to protect employees at work
Examples of Health and safety law	• The Health and safety at work act 1974
Effects on businesses	• Firms need to carry out risk assessments • Firms need to take reasonable steps to reduce risk of accident.

Consumer Law	Law to protect consumers
Examples of employment law	• Consumer Rights Act 2015 • Trades Description Act
Effects on businesses	• Products must be fit for purpose • Products must match their description • Products should be of a satisfactory quality

Competitive Environment

Market	Exists when there is buying and selling of a good or service
Competitive market	Where there are a large number of firms competing for sales
Effects of operating in a competitive market	• Firms will need to be price competitive • Promotion of the good or service will be important • Firms will try to create brand loyalty
Reasons for little or no competition	• Brand new good or service • The market for the good or service is too small • Difficult to enter the market

Sources of Finance

Sources of finance = methods businesses use to raise money

Internal sources of finance	• Family and friends • Retained profit • Selling unwanted assets
External sources of finance	• Bank loan / Mortgage • Overdraft • Trade credit • Hire purchase • Government grant • New share issue

Sources of finance	Advantage	Disadvantage
Family and friends	May not have to pay interest on the loan	Can create problems with the friendship
Retained profit	Doesn't need to be paid back	Owners may want to take the profit out
Selling unwanted assets	Doesn't need to be paid back	Only works if the business has assets they no longer use
Bank loan / Mortgage	Usually quick and easy to take out	Interest has to be paid on the loan.
Overdraft	Only borrow exactly what you need	High interest rate
Trade credit	Gives the firm time to earn money before paying the debt	Late payments may lead to a large fee
Hire purchase	Allows a firm to buy an asset in instalments	The total amount paid for the asset is often much higher than if the firm had bought it with one payment
Government grant	Free money for the firm	Can be complicated to apply for and not all firms will meet the conditions.
New share issue	Does not have to be paid back	New shareholders take a share of the profit

Short term source of finance	• Trade credit • Overdraft
Long term source of finance	• Bank loan / Mortgage • Hire purchase • Government grant

Cash Flow

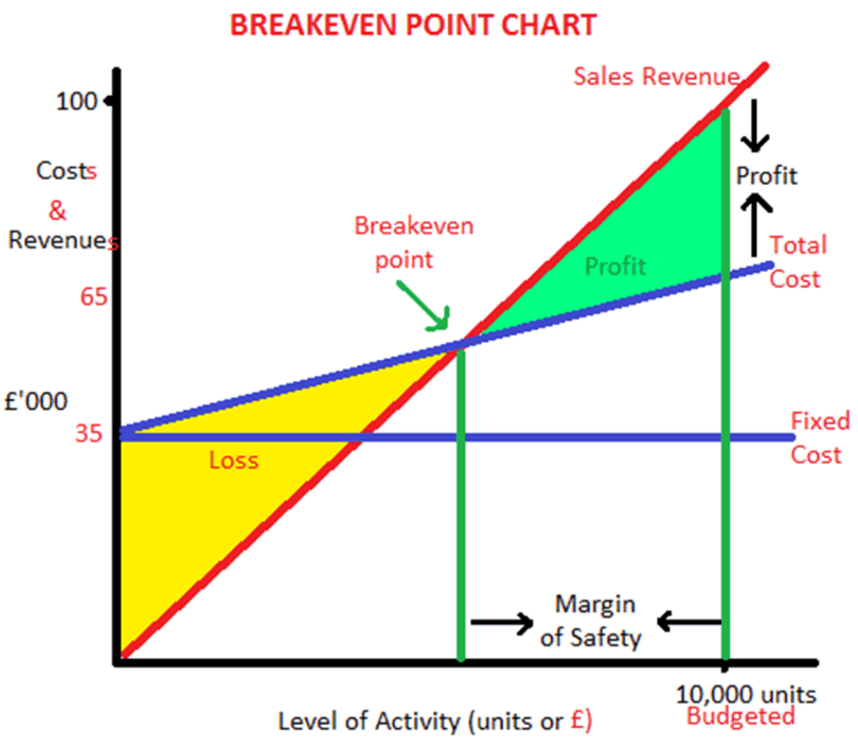
Cash flow	The flow of money into and out of the business
Cash inflow	Money coming into the business usually from sales
Cash outflow	Money leaving the business to pay bill, wages etc..
Net cash flow	Cash inflow – Cash outflow
Positive cash flow	More cash inflow than outflow over a particular time period • This means the business has no problems making payments
Negative cash flow	More cash outflow than inflow over a particular time period • Often called a 'cash flow problem' • The business can't make the payments it needs to
Opening balance	Cash in the bank at the beginning of the month
Closing balance	Cash in the bank at the end of the month (opening balance + net cash flow)

Reasons for constructing a cash flow forecast	• Helps a business plan the cash inflows and outflows • Allows the business to identify when they will need extra sources of finance.
Solutions to a cash flow problem	• Re-schedule payments • Overdraft • Reduce cash outflows – find cheaper suppliers • Increase cash inflow – sell more or increase prices • New sources of finance

Financial Terms and Calculations

Variable cost	Costs that change as output changes e.g. Raw materials
Fixed cost	Costs that don't change with output e.g. rent
Total cost	Fixed cost + Variable cost
Revenue	Money received from sales (selling price x number sold)
Profit	Money left over once all costs have been paid (revenue – total cost)
Loss	This occurs if costs are greater than revenue

Investment	Money put into the business to make improvements in order to make the business more profitable
Example investments	• New machinery • New buildings • New vehicles
Average Rate of Return (ARR)	Shows the percentage earnt by the investment. The higher the better.
ARR Calculation	(average annual profit/initial investment) x 100%
Average annual profit	Total profit / number of years of the project



Break even output	The level of sales where costs are equal to revenue. • If a business sells more than its break even output it will make a profit • If a business sells less than its break even output it will make a loss
Margin of safety	This is how far above the break-even output a business's sales are.
Value of using a break-even analysis	Advantages • Quick and easy to calculate • Will help support an application for a loan at a bank • Allows a business to see what would happen to profit if they changed price or cost Disadvantages • The data is a prediction and therefore may be wrong • Makes an assumption that all products will sold – they may not • Will be complicated if the business sells more than one product

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Analysing Financial Performance

Income statement	A financial document which shows Revenue, Cost and profit for a period of time (usually a year)
Income Statement Part 1	The Trading Account. This records the gross profit or loss Revenue – cost of sales = Gross profit
Income Statement Part 2	The Profit and Loss Account. This records the net profit Gross Profit – expenses = operating profit Operating profit – interest = net profit
Income Statement Part 3	The Appropriation Account. This shows where net profit goes. • Taxation • Dividends • Retained profit

Gross profit margin	(gross profit / revenue) x 100%
Net profit margin	(net profit / revenue) x 100%

Statement of financial position	A document showing where the business has got its money from and what it has used it for
Fixed asset (non-current assets)	Items owned by the business that will last for **more** than one year e.g. buildings, machinery
Current assets	Items owned by the business that will last for **less** than one year • Stock • Debtors – money owed to the business • Cash
Current liabilities	Bills that have to be paid in less than one year
Long term liabilities (non-current liabilities)	Bills that will be paid back over longer than one year
Net current assets	Current assets – current liabilities
Capital employed	The total money put into the business
Use of a Statement of Financial Position	• Shows the value of a firm in snapshot in time • Can be used to compare the performance of the business with previous years.